A FIRESIDE CHAT WITH MOHIT JOSHI: THE BANKING INDUSTRY MUST INVEST IN TECHNOLOGY TO MAKE SENSE IN THE NEW ECONOMY

Feb 10, 2020 Phil Fersht Sam Duncan

Phil Fersht recently had a candid conversation with Mohit Joshi, President, Infosys, about his views on the banking sector and the future of Infosys and the market as a whole.

Mohit openly admits that he had little knowledge of the technology services business while growing up in India; instead, he chose to spend his time studying for a degree in history. He then joined a business school and ultimately found himself in the banking industry. In the opening discussion, Mohit explained that he saw banking in India shift in 2000, becoming more commoditized—this is what sparked his curiosity about the world of technology. Eventually, through a friend, he found himself working for Infosys in Boston as a business development manager. Mohit moved around North America, watching Infosys grow from a $180 million company in 2000 to the almost $13 billion company it is now before moving to London, where he currently resides.

Here is part one of this two-part series, in which Phil and Mohit discuss the banking sector and Mohit's thoughts on its current disruptors and what is hindering digital transformation in the banking industry.

Phil: We're very excited about the impact of digital, and we see a different pace emerging in all the key industries. Banking is interesting; it's a slow-moving industry, but it's also an industry that's more impacted by technology than any other.

How would you describe the pace of change in banking today compared to other industries and what you think we're going to see in the next two years?

Mohit: Banking is a unique industry because the production services are almost completely digital already, so you would think that this industry would be at the forefront of change. You don't have physical products; the pace of change should have been rapid. But I think it comes down to a couple of things. First, and most important, is the regulatory paradigm—banks are taking public money, so regulators have a huge interest in the long-term stability of institutions. That's one thing that has led to a slower pace of change in this industry in comparison to unregulated industries.

The second thing, which a lot of us underestimated, is that customer inertia is very real in this business, and it has taken customers time to demand the digital propositions from their banks that they were demanding from a newspaper, for instance, that didn't have a mobile edition.

But I think people have been much less demanding of their banks and insurers than they have been of other industries.

Third, the structure of the industry in Western Europe and North America hasn't really changed. If we compare the industry pre- and post-crisis, the largest financial institutions in the world are still the largest, with the exception of some that have gone bankrupt or merged. You hear a lot about Starling, Monzo, or N26, but none of these would reach the ranks of the top 100 financial institutions in the world. I think entrants have made less of a disruptive impact on this industry, which goes back to customer inertia and regulatory oversight.

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Having said that, the role of technology within financial institutions has dramatically been reshaped. If we look back to when I joined the industry, even the most radical forward-thinking banks were spending between 2% and 3% of their revenue on technology, but that number has gone up to almost 7% to 8%. Boardroom conversations about technology were rare; the CIO was still reporting to the CFO. This has undergone a dramatic change, and most boards are now staffed with technology experts. There's a huge demand for people who understand enterprise technology; boards are obsessed with the latest technology developments and are actively pushing management to have coherent responses to that.

Concurrent with spending levels increasing dramatically, the vision of a financial institution being a combination of talent, a balance sheet, and a technology platform has really taken hold of the industry. It's not often that incumbents in the industry seek to define themselves as challengers; they typically look down on challengers as providing a shoddier, cheaper, and smaller range of services. The share of banks that want to describe themselves as fintechs is now nearly 100%. Almost every bank is looking to redefine itself as a fintech—so the change, in terms of mentality and outlook, has been huge.

I also feel that banks have realized that we are in a very-low-interest-rate environment. If you are a bank in Belgium, you're probably paying 10 to 15 basis points to your savings account holders, and in the investments that you have in government securities, you're probably losing 70 to 80 basis points. This model is not sustainable unless you start automating huge portions of your enterprise, using technology as a key enabler to reduce costs and operational inefficiencies and to allow for straight-through processing. So, technology as an enabler for cost saving is something that people don't talk about, but it is one key development.

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The second is the use of technology to enhance user experience—whether it's the employee or customer experience—and the use of technology to mine data, so banks can truly be at the heart of a customer's financial life rather than on the edges. There is also huge pressure to industrialize, cut costs, digitize, and become more relevant. To do this, banks are changing their organizational structures. Banks today are flatter than they were in the past; they are becoming more agile in terms of the way the business teams are organized. Even mid- to senior-level executives are scrambling to understand what agile and cloud mean for their business. At the same time, it seems like organizations' cultures are transforming, too.

To your question about looking forward, two or three years down the line, we will continue to see more investment in user experience, more use of technology to reduce costs, and more flattening of organizational structures and potential reductions in headcount by automation. I don't think we can expect revolutionary changes because of this sector's importance to the stability of the economy.

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The other change we'll probably see is tech companies playing a more important role within banking. Ten years ago, banks were afraid that Apple would come and eat their lunch by opening a bank, but five years ago, they realized that Apple wasn't interested in being a bank—partly because of the complexities of the US legal code, but also because an industrial company can't really become a bank. Now they have realized that tech companies are going to use the banks as a back end while they provide the front-end skin, skimming off a lot of the profitability in business lines like cards and payments—the real profit engines for banks.

So, over the next two years, we'll see an acceleration of this trend. Apple card has already been the most successful credit card launch in history, and Amazon is doing a lot with its NewDay partnership and lending to the supply chain of its merchants. We'll probably see an acceleration of these trends over the next two years, and not a revolutionary industry shift.

Phil: More players muscling their way into the credit market…

Mohit: Exactly, Phil. I think lending, payments, and the extent that trade is linked to payments are the three hottest areas in banking. The traditional profit engines for banks, like asset management and broker/dealer businesses, are clearly challenged, right? Because the typical ways in which you made money, on the equities desk, the fixed income desk, on brokerage, and through brokerage fees—those businesses are dramatically dropping. So, the profit engines will be lending, payments, and trade, and these businesses have been helped by consumer credit growing exponentially and trade volumes growing.

Phil: And do you see a move—like Amazon's when it acquired Whole Foods—from one of the digital juggernauts into the broader retail banking space? Can you see one of those companies looking at acquiring a BOA or a Barclays?

Mohit: I think it's unlikely, Phil, partly because of compliance and regulatory requirements which make it hard, and sometimes impossible for industrial companies to acquire banks. Legally, they can't get into the space, which is why Walmart has a bank in Mexico but not in the US. Given these regulatory complexities and the fact that most banking CEOs are being summoned to Washington to address the Senate or Congress, I think these digital juggernauts will be a little reluctant to acquire a retail bank.

What we should see are a lot more partnerships, like the Apple/Goldman partnership that we have seen in the credit card space, rather than an outright acquisition. Banks are relatively inexpensive; Barclays is valued at less than $50 billion, while Apple is at a trillion—a twentieth of the valuation of Apple. Having said that, I think they'll be a little bit reluctant to acquire a complex, regulated business, and regulators will also be a little bit concerned about what this might mean for public deposits.

Phil: And then you've got all the data privacy issues around it as well. Maybe the banking industry just isn't that attractive? So, it's easier to partner with it than to actually own it?

Mohit: Absolutely. I think, in the long run, you'll see three kinds of banks:

1. Banks that are like efficient manufacturing entities: efficient at taking in deposits and processing and making payments, and they constitute the backbone of the industry.
2. The boutiques, which will bring in the best of artisanal manufacturers. They might offer a bare-bones current account or savings account, but then have access to a Swiss wealth manager and machine learning quant from New York.
3. Finally, you'll have banks that will be trading on the technology platforms. They'll be allowing other parties to use their platforms and have that as the key profit engine for them.

Banks are unique. If you look at manufacturing, most manufacturers are designing the product and assembling thousands of subcomponents. Boeing is an example; thousands, if not millions, of subcomponents are made by individual manufacturers. A bank is the closest you get to a whole conglomerate, which is front to back, manufactures by itself, and then sells everything at the company store.

Keep an eye out for part two of this interview where Phil and Mohit discuss Infosys, it’s future, and the wider IT services market.