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BGLN VIEWPOINTS

Developing strategies for a complex banking ecosystem

July 2024

The financial services ecosystem continues to expand and evolve. To advance digital transformation, banks are partnering with an ever-broadening array of financial technology and other providers as they navigate a changing competitive landscape that includes many of these same players. New ways of delivering banking products and services, such as embedded finance and open banking, are creating more ways for banks to engage with customers and third parties, but banks remain concerned about the risks inherent in sharing data, relying on third parties, cybersecurity, and complying with regulations.

On May 21 (London) and June 13 (New York), board directors and senior executives from the Bank Governance Leadership Network met to discuss how the banking ecosystem has evolved in recent years and the implications for boards' and management teams' oversight of strategy and risk management.

For a list of participants, please see appendix (page 11).

This *ViewPoints*[1] highlights the following key themes that emerged from these meetings and related conversations:

As the relationship between banks and fintechs evolves, competitors and partners multiply

Banks need a more strategic approach to competition and partnerships in a complex ecosystem

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"You saw a lot of fintech businesses say, 'I can do this better' in the beginning, but they've realized that they need to partner with the formal banking system instead."

—Executive

In 2014, JPMorgan Chase CEO Jamie Dimon famously said, "When I go to Silicon Valley … they all want to eat our lunch. Every single one of them is going to try."[2] Ten years later, the landscape has become more complex, with an expanding mix of competitors in different businesses, some of which have also become important partners and providers to banks. As one executive observed, *"It isn't a zero-sum game. Competition between fintechs and banks is artificial; the financial system value chain is so fragmented, even defining what lunch you're eating has become hard to determine."*

The dynamic between banks and fintechs continues to change

Dire predictions regarding fintechs and the future of incumbent banks have not fully come to pass. Many full-stack digital competitors to banks have struggled to scale, and many fintechs that may have initially aimed to compete with banks have become their partners. An executive observed, *"You saw a lot of fintech businesses say, 'I can do this better' in the beginning, but they've realized that they need to partner with the formal banking system instead."* Confirming that assessment, one fintech founder said, *"I realized the only way to achieve my goal of putting consumers first was to work with the banks, because consumers have no choice but to work with banks. It was about trying to use the existing banking system infrastructure to empower customers with their money."*

Through these partnerships, fintechs have become important sources of innovation, automation, and expanding capabilities for banks. A participant described some of the areas in which fintechs can offer solutions to banks: *"I do think there's a lot of truth in the ability of fintechs to provide new technologies to automate and derisk manual processes. The same is true on the data side and looking at correlation of risk. Do you have a system that ties risk together across the organization? Are those systems talking to each other, and do you know the correlation? A lot can be done there with fintech partnerships."*

Entrepreneurs and their investors are always looking for new problems to solve. One participant highlighted balance sheet management as an opportunity for fintechs, as banks seek to reduce their outstanding capital

commitments while continuing to provide credit. *"Banks are always going to be the best owners of credit cards. But the balance sheet component is very difficult. Fintechs [can] step in and run the risk for a portion of that book. The opportunity is to help enable the banks to continue to maintain their relationships but move their capital elsewhere,"* reported an executive.

Fintechs still represent a competitive threat

While many fintechs are now designed to partner with or serve incumbent banks, others remain focused on disruption. Although fintechs may not have eaten the banks' lunches, they have achieved scale in key businesses, like payments, and in some underserved markets. Nubank, a Brazilian digital bank, surpassed 100 million customers in 2024, the first Western digital bank to hit that milestone.[3] The top 20 fintechs now have 3.8 billion customers, while the top 20 banks have only 2.7 billion customers, according to one analysis.[4] And many large fintechs are now operating profitably. Nubank hit $1 billion in yearly profits in 2023, SoFi made its first-ever profit in 2024, and the UK challenger bank Monzo achieved profitability for the first time as well.[5]

"Fifteen years ago, everyone was talking about fintech as a threat, and they didn't compete, and they still haven't, broadly. But they've eaten away at small bits," noted a director. Fintechs have made the greatest impact in areas where banks struggle to serve customers well, partly because digitally native platforms can acquire customers more easily and cheaply than banks. *"Banks have to get the costs right because, for fintechs, the cost to serve this customer is so low,"* stated a director. One participant cited small and midsized enterprises (SME) as an example of a market where fintechs have made inroads: *"The SME space is more dynamic. There is neglect by the formal banking system regarding what businesses need in certain sectors. If the banking system doesn't step up, you'll see fintechs and others step up."*

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—Director

A fintech founder explained how they are targeting an underserved demographic: *"We'll never be able to dislodge a 74-year-old wealthy person from their wealth adviser. So, we're targeting affluent people in their 20s and 30s with low six figures of investable assets. Those are the people on the fastest wealth accumulation curve, and that will be the most attractive demographic in 20 years."*

Data sharing and the embedding of finance put banks at risk of disintermediation

The effects of mandated open banking—a system that provides third party access to financial data through the use of application programming interfaces—have been relatively muted since its introduction in some markets. Six years after its launch in the United Kingdom, there are 7 million active users, fewer than some had anticipated.[6] However, one participant observed that this trajectory may be changing: *"After a difficult pregnancy, open banking is up and running around, and I've been really impressed by it."* New regulations promise to bring open banking to the United States. Participants expect Canada to follow soon, and other countries are also promoting market-driven data-sharing frameworks.[7] While many participants questioned what this will mean in practice, one executive declared, *"Open banking is already here, whether we like it or not."*

- **Big Tech may be the biggest beneficiary of open banking's increasing traction**. *"There will always be a question around who controls the customer relationship. If you're a bank, you want to maintain that. Fintechs are now more of a single-product background partner. The bigger threat is Big Tech because they have a customer relationship and [banking is] an adjacent product,"* noted a director. One participant suggested we may now be approaching the point at which big tech companies will take advantage of open banking and remove banks from the customer interface: *"Look at what Apple has done. They bought a small fintech and plugged it into the digital world. Why would you ever log into your banking app? The world's largest tech firms can harvest all consumer transaction data, 24/7, for free. What the regulators never anticipated when they launched open banking was that Big Tech would say, 'So let me get this straight. We can access every consumer's total financial transaction history and authorize payments on their behalf at no cost whatsoever?'"*
- **Payments remains an area ripe for further disruption as they are increasingly embedded and invisible.** An executive observed, *"Payments continue to be the sector that's evolving most, and there's opportunity to do a lot more in payments."* The payments evolution may be transformational, with one participant comparing the coming change to *"the change from copper to fiber and combustion engines to electric vehicles,"* while another predicted,

"Fintechs are now more of a single-product background partner. The bigger threat is Big Tech."

—Participant

"With the introduction of the internet, we moved to a do-it-yourself world, where we've been for a while. The next generation will be that things just happen in the background. With embedded transactions, the financial component is embedded in the customer journey. The future of payments is that they'll disappear."

Another executive said, *"The technology on which money exists right now is about to change, and the payments structure needs to anticipate that. The industry is compelled to focus on resilience, stability, and safety, but there's a whole world out there that's exchanging value outside of that. There are huge amounts of payments changing hands, with more and more nonbank money on nonbank rails. For example, TikTok credits are huge."*

- **Regulation is a double-edged sword for competition.** *"As a sector, I don't know how we survive with these regulatory restrictions,"* stated an executive. But others continue to see regulation as a barrier to entry, protecting banks. Assessing the current competitive environment, another executive said, *"I just don't go to my banking app. And it's such a short step to go from there to embedded finance that it's going to be really hard for banks to compete. The biggest defense the industry has is regulation. Big Tech do not want to find themselves under regulation. But we will see technology players with scale continue to nibble away, not trying to become a bank, but by using emerging capabilities to advance their business models in a way that banks can't."*
- **Banks are also competing for talent and expertise**. A participant asked, *"If you are talented in tech, who do you want to work for? What we can do is play to the strengths of financial services. It begs the question, What can fintechs/banks do that Big Tech can't? In the bank, the biggest frustration is hiring talented people who couldn't do anything because of all the obstacles in their way."*

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—Executive

Banks need a more strategic approach to competition and partnerships in this environment

To navigate the current banking ecosystem effectively and continually enhance their digital capabilities, they need a thoughtful strategy and the ability to manage the associated risks and oversight challenges. A participant summarized the options available: *"Banks always have three*

choices. The first is … to copy the fintechs and build something themselves. As an example, when Venmo came out with P2P payments, a consortium of 29 banks got together and built Zelle. The second is partnering. For example, we white labeled a platform so our clients can use the latest bill payment software. The third is to acquire." In some cases, however, the choice to build needed technologies in-house may be a luxury available only to the largest players. *"We tend to build more than we buy. We do use technology partners lower in the stack, but where we want to differentiate is when we tend to build. We have a tech budget that's bigger than some countries, so we can do that, but not all companies can,"* noted an executive from one of the largest global banks. Another participant agreed, saying, *"Most midsize banks don't have large tech budgets, but they want to leverage this technology and are under same regulatory scrutiny that the largest banks are."*

While all banks will have processes around how and when they partner, participants acknowledged that they need more sophisticated frameworks to inform these decisions, highlight the opportunities and risks, and determine when senior management and the board should be informed.

Proper third party risk management strategies are critical

Even large institutions depend on a growing number of partners and vendors. One director said, *"The complexity of vendor relationships right now is extraordinary, and it's only gotten worse over the last 20 years. Where we've had problems, eight out of ten times, it's a vendor that has caused it."*

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—Director

Given the proliferation of third parties and associated risks, banks must be strategic in assessing future partnerships and vetting potential new vendors and monitor existing vendor relationships vigilantly. Management and boards should be asking questions including:

- How are potential partners and vendors identified and assessed?
- What does effective onboarding look like?
- How much data is shared with partners, how is it shared, and should they be granted direct access to bank systems?

An executive suggested a simple way to mitigate third party risks: *"My general theory is the only real thing you can do is try to limit the number of vendors you use. Because it's really just the more vendors, the more exposure. So, the only real answer is to have fewer vendors."* But a

director cautioned, *"That's risky, because I think if you limit your relationships, you've limited your ability to strategically address the issues you need to address moving forward."*

Participants recommend articulating a risk appetite and creating a framework to help banks think about the nature, size, and number of their third party relationships and related competitive and operational risks. Banks need to improve how they determine thresholds for escalation and review of third party relationships, including which demand board attention, before problems arise. Participants identified some practices for developing third party risk management strategies:

- **Establish a third party risk appetite.** A comprehensive understanding of the institution's appetite for third party risk is critical to developing an appropriate strategy for partnership, including the build, buy, or partner decision, vendor management, and prioritizing the right partnerships. *"We've got to focus on responsible growth with a risk framework and appetite in mind, one that applies to all aspects of the business. Vendors and partners are key aspects of this,"* said an executive. Another executive said, *"I think one way to reframe this is, it's not just managing vendor risk. It's understanding your overall risk appetite and how you want to manage that, understanding that partnerships are introducing a vulnerability."*
- **Focus on assessing critical partners, not just problem vendors.** One risk committee chair acknowledged, *"We tend to focus on the problem vendors, particularly if they're in financial straits, and we're looking at those with resiliency and service issues that are not meeting their [service-level agreement] … We're really focused on problem areas."* Another concurred: *"It's the same thing for my board. We're looking at problem vendors, except for where we're focused on acquisitions or using new vendors."* One director highlighted the reason for a broader approach: *"We need to have a list of critical vendors, do internal audits of those critical vendors, and look to consolidate where we can. Because when we have a vulnerability, that is a major issue, and we need to know."*
- **Evaluate the reputational and regulatory risk implications of each partner.** As third and fourth party risks around security and resilience expand, an executive reminded, *"The reputational risk is always on the bank. There's no world where it's not. The consequences of a breach are always on the bank, no matter how*

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—Executive

much the vendor is at fault." A participant expanded on that: *"We are seeing now this complexity issue, that when a vendor makes a change or something goes wrong and we have an outage, it's not a good look for us. It ends up costing us our reputation and hurts us with regulators. No matter how minor an outage is, it will be held against you from an operational resiliency perspective and could affect your ability to make an acquisition. Vendor risk is huge from this perspective."*

- **Raise the bar for establishing new third party relationships.** Participants agreed that the standard tools for vetting and monitoring partners—questionnaires, periodic audits, third party assessments—bring limited comfort. "*I only have one compelling story about vendor vetting,"* observed an executive, *"and it's because we were considering a core vendor, so I had my expert on infrastructure talk to that [chief information security officer] for hours. Because of that, we declined to use them. They got breached twice in the next two years. It's the only success story out of thousands. I just can't emphasize enough: the tools that are available are not powerful tools, and we're fooling ourselves if we think they can manage the risks."* What banks can do, according to a participant, is *"view the cost of vendors as being higher than we actually realize it is, and aggressively groom your vendor list, see who you're truly dependent on, try to shrink data sharing to zero, and try to have as much resilience as possible."* Another participant suggested that any potential new partner should have to clear a high bar: *"Anything new better be kick ass technology that will make a big difference."*

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—Director

- **Rigorously limit data shared with partners.** In addition to limiting the number of vendors, a related objective should be limiting the amount of data shared with those vendors. *"My intuition is, any data I share with one vendor, I should assume has been shared with 10 subcontractors. That scale of data sharing is discomforting. Even if you have to use the vendor, ask yourself, can I trim the amount of data we share? Often, we find we can be creative and change the amount of data we share,"* reported an executive. A participant suggested this is an area where boards can press management: *"I'll bet the number of vendors that have sensitive data like social security numbers is larger than you expect. That's a number you should apply pressure to, to get down. How do we consolidate vendors? Or can we share less, share for a shorter amount of time? Those are the levers you should be using to get that number down."*

A director advised asking, *"What does the data life cycle need to be? If you don't know who owns the data, how long it's out there, or when you need to kill that data sharing, you should concentrate there and safeguard more."*

- **Consider where acquisitions are justified.** Concerns about managing third party risk can lead to decisions to build or acquire technologies rather than partner. A director described their experience acquiring a fintech partner: *"We could justify the entire purchase price because it would enable us to extricate ourselves from a very large vendor that everyone uses that's so expensive. It made sense not to partner but to buy them, and it ultimately enabled us to get out of another relationship that was expensive and also becoming increasingly unreliable and a risk from a cyber perspective."* Another director noted, *"Much of the benefit of acquisition is that you're able to impose the control environment you want—you just took the same set of activities and converted from How do I observe someone else's arrangements? to Now, it's ours."* The first director agreed: *"That was one of the benefits we considered when they first brought the acquisition to the board. It was cost savings, customer capability, and the being able to bring it into our control."*

Streamlining the selection and onboarding of partners can create competitive advantage

Lengthy and cumbersome vendor onboarding processes are a hallmark of the banking industry and complicate banks' abilities to work with new partners. "*It's notoriously difficult to get onboarded at most large banks. It's a very purposefully difficult and rigorous process, and this adds a layer of difficulty to partnership,"* stated an executive. According to another participant, *"We don't make it easy for fintechs to engage with us. It can be like pulling teeth to get through approvals."* Regulatory constraints are regularly offered as justification, but a participant cautioned, *"Many people inside an organization use the regulators as an excuse … I've often asked people to quote the exact regulation [working with a particular vendor] is against. Most of the time they couldn't find it. It's often cultural. They were told 20 years ago it wouldn't work. They just accept it, and they never challenge it."*

"A better onboarding process could actually be a competitive advantage and help you to differentiate and grow."

—Executive

An executive observed, *"It seems like the posture of banks is defense, defense, defense … while boards are also pushing management teams to grow faster."* This executive suggested, *"A better onboarding process*

could actually be a competitive advantage and help you to differentiate and grow."

The challenge lies not just with the banks; fintechs also need to be prepared to work with regulated financial institutions. One director declared, *"It's a parallel effort. Financial institutions need to be more open to working with fintechs and thinking about partnerships, but fintechs need to have an understanding of the regulatory requirements of banks."* A bank executive said, *"The typical fintech founder hasn't spent time learning our frameworks or understanding the parameters banks must operate in. There's an astounding disconnect. We want to work with partners, but they do have to fit into requirements that we have."*

"It's a parallel effort. Financial institutions need to be more open to working with fintechs and thinking about partnerships, but fintechs need to have an understanding of the regulatory requirements of banks."

—Director

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A participant referred to a quote attributed to Bill Gates: "We always overestimate the change that will occur in the next two years and underestimate the change that will occur in the next ten." Ten years ago, financial services were in the early days of an explosion of technology that created a wave of new competitors and predictions about disruption for incumbent banks. But that explosion also created an array of new partners and providers that enabled banks to innovate and enhance their services and operations. In this increasingly complex ecosystem of competitors and providers, bank leaders must be more alert to where and how competition may emerge and more strategic about how they approach partnership decisions. The next wave of technological advances could create another inflection point as finance is embedded, banks and customers use AI in new ways, and more partners, providers, and competitors gain access to bank customer data.

Appendix 1: Participants

The following individuals participated in the meetings or related conversations:

Participants

Homaira Akbari, Non-Executive Director, Santander

Nora Aufreiter, Human Capital and Compensation Committee Chair, Scotiabank

Brian Barnes, Founder and Chief Executive Officer, M1

Craig Broderick, Risk Review Committee Chair, BMO Financial Group

Agnes Bundy Scanlan, Nominating and Governance Committee Chair, Truist Financial

Eric Cantor, Vice Chair and Managing Director, Moelis

Kapil Chhibber, Managing Director, Technology Partnership Development, Bank of America

Stella Clarke, Chief Strategy and Marketing Officer, Fenergo

Terri Duhon, Risk Committee Chair, Morgan Stanley International

Misha Esipov, Chief Executive Officer and Co-Founder, Nova Credit

Joe Garner, Author, Future of Payments Review

Erik Gaston, Chief Information Officer, Vice President of Global Executive Engagement, Tanium

Tobi Guldimann, Risk Committee Chair, Edmond de Rothschild

Phil Kenworthy, Non-Executive Director, ClearBank

Nick Le Pan, Risk Committee Chair, CIBC US

Nick Lee, Head of Regulatory and Government Affairs, OakNorth

Mark Leonard, Director and Co-Founder, European Council on Foreign Relations

Stuart Lewis, Risk Committee Chair, NatWest

John Liver, Non-Executive Director, Barclays UK

Andrew Lowe, EMEA Head of Business Development for Technology, Bank of America

Alan MacGibbon, Chair of the Board, Chair of the Corporate Governance Committee, TD Bank

Scott Moeller, Chair of the Board, JPMorgan Markets Ltd

Lewis O’Donald, Non-Executive Director, HSBC Bank plc

Andy Ozment, Executive Vice President, Chief Technology Risk Officer, Capital One

Marty Pfinsgraff, Risk Committee Chair, PNC Financial

Sabrina Pucci, Non-Executive Director, Mediobanca

Mark Rennison, Non-Executive Director, Royal London and NatWest Holdings

Sadia Ricke, Group Chief Risk Officer, Standard Chartered

Manolo Sánchez, Non-Executive Director, Fannie Mae

Mohit Sarvaiya, International Chief Information Officer, BNY Mellon

Samantha Seaton, Chief Executive Officer, Moneyhub

Mark Seligman, Senior Independent Director, NatWest

Jeremy Solomon, Partner, Nyca Partners

Paul Taylor, Non-Executive Director, Morgan Stanley International

Kristi Way, Executive Director, Moelis

David Wildermuth, Chief Risk Officer for the Americas and Consolidated US Operations, UBS

EY

Jan Bellens, Global Banking and Capital Markets Sector Leader, EY

Tom Bull, Partner, Head of FinTech Growth, UK Financial Services, EY

Dan Cooper, UK Banking and Capital Markets Leader, EY

Marc Saidenberg, Americas Financial Services Regulatory Lead, Principal US Financial Services Consulting, EY

Rashmi Singh, Partner/Principal, Financial Services, EY

Chris Woolard, Partner, Financial Services Consulting, EY LLP; Global Financial Services Regulatory Network Chair and EMEIA Leader, Financial Services Regulation, EY

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Dennis Andrade, Managing Director

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About this document

The BGLN is a group of banking board members, executives, and stakeholders, engaged with regulators and other subject matter experts, committed to outstanding governance and supervision in support of building strong, enduring, and trustworthy banking institutions. The network is organized and led by Tapestry Networks with the support of EY as part of its continuing commitment to board effectiveness and good governance.

ViewPoints is produced by Tapestry Networks to stimulate timely, substantive board discussions about the choices confronting audit committee members, management, and their advisers as they endeavor to fulfill their respective responsibilities to the investing public. The ultimate value of *ViewPoints* lies in its power to help all constituencies develop their own informed points of view on these important issues. Those who receive *ViewPoints* are encouraged to share it with others in their own networks. The more board members, members of management, and advisers who become systematically engaged in this dialogue, the more value will be created for all.

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Endnotes

[1] *ViewPoints* reflects the network's use of a modified version of the Chatham House Rule whereby comments are not attributed to individuals or corporations. Quotations in italics are drawn from conversations with participants in connection with the meeting.

[2] Craig Birk, "Why Silicon Valley Is Eating Wall Street's Lunch," Yahoo Finance, July 14, 2014.

[3] Daniel Cancel, "Nubank Surpasses 100 Million Clients Across Latin America," Bloomberg, May 8, 2024.

[4] Spring PR Agency, "The Top 20 Fintech Companies Serve 3.8 Billion Individuals vs Top 20 Banks – Only 2.7 Billion: Brett King," Yahoo Finance, April 29, 2024.

[5] Nu Pagamentos, "Nu Holdings Ltd. Reports Fourth Quarter and Full Year 2023 Financial Results," news release, February 22, 2024; "SoFi Soars After First-Ever Profit Beats Estimates," Reuters, January 29, 2024; Ryan Browne, "Digital Bank Monzo Posts First Full Year of Profit after More Than Doubling Revenue," CNBC Disruptor/50, June 3, 2024.

[6] "Joint Regulatory Oversight Committee Sets Out Recommendations for the Next Phase of Open Banking in the UK," Financial Conduct Authority, April 17, 2023.

[7] Douglas Gillison, "US Consumer Watchdog Proposes New Financial Data Sharing Rules in Competition Boost," Reuters, October 19, 2023.