Banks need to rapidly reinvent to strengthen profitability, boost returns: Report

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NEW DELHI: At a time when growth is slowing, productivity gains are fading and digital pressures are on the rise, the banking sector should consider a suite of radical measures, both organic or inorganic, to strengthen profitability and boost returns, says a report.

The McKinsey's Global Banking Annual Review launched on Tuesday, warned that the bottom third of banks need to rapidly reinvent their business models in the face of continued threat posed by fintechs and big technology companies that are taking stakes in banking businesses.

Banks need to adopt defensive moves like improving risk management with advanced analytics and offensive moves such as dramatically lowering costs by outsourcing non-differentiated cost drivers to industry utilities.

"History tells us that 40 per cent of the top banks today will drop to the bottom half of peers in the next cycle. So the time for bold and critical moves is now," said Joydeep Sengupta, Singapore-based McKinsey senior partner and report co-author.

Sengupta further said that "moves made today, be it to build scale or restructure business models, will have a defining role in combating the probability of that slide."

On India, the report said revenue growth within India's banking sector has dropped from 22 per cent (2002-07) to 10.3 per cent (2010-18).

Moreover, banks in India have experienced a dramatic drop in 'Return on Tangible Equity' over the last five years, from 17.7 per cent in 2013 to 2.3 per cent in 2018, the report said.

It further said that Indian banks typically have a higher cost base, in part because many maintain large on the ground networks to serve rural customers.

As per the report, machine-learning models can improve predictive accuracy in identifying the riskiest potential customers by 35 per cent.

Banks should also consider their options for building scale or competence through inorganic ways including both mergers and acquisitions as well as partnerships.

Moreover, banks need to work hard to close the digital-skills gap, as technology has overtaken banking in perceived attractiveness of compensation and benefits, the report noted.
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