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Digital Transformation Tipping Point

Exploring how Building Societies must navigate the challenge of meeting customer demands while preserving their unique market position and ensuring a secure digital future.

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Content

INTRODUCTION

At Mason Advisory we have drawn on our experience of the financial services marketplace, and outcomes from working with some of the largest UK building societies, to discuss three key focus areas that need to be addressed to retain and grow market share in these challenging times.

In this series of insight articles covering the digital transformation tipping point, we take a deep dive into how Building Societies need to successfully navigate between meeting customer demand, retaining their unique market proposition and designing a secure digital future.

Insight overview

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Part 1 of 3 - Building societies face a digital transformation tipping point – but where do the challenges really lie?

Customer-facing services are only successful with the right back-end planning and development. A pragmatic, culturally sensitive approach to managing the transformation ecosystem holds the key to success

Industry

Banking

Services

Architecture

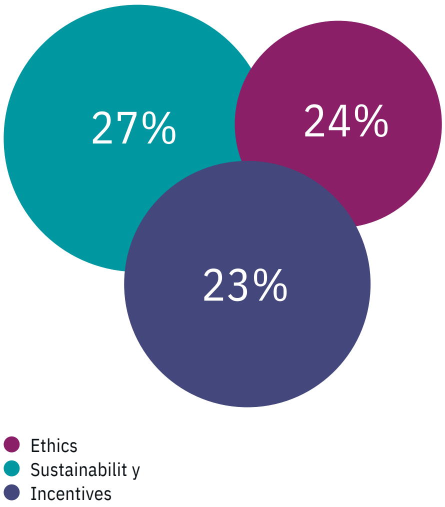
Operating Model & Organisational Design

Cyber

Sourcing

Building societies face a digital transformation tipping point – but where do the challenges really lie?

Figure 1: Factors in customer choice of financial services organisations [Source: YouGov]



Access to digital banking is now a standard customer expectation, and all financial organisations need to evolve their digital services to be competitive. These front-end capabilities, though, are only achievable by a back-end architecture shift to digital core banking platforms. As mutual organisations, building societies face complex challenges when it comes to deciding on how – and how far – to transition legacy core systems. Some of the headline challenges include balancing risk with reward, legacy with opportunity, and tradition with evolution.

Data from YouGov's Future of Financial Services 2022 report reveals that digital transformation presents a rich opportunity for building societies. In choosing financial services, the report says, access to digital banking is a priority for almost half of customers globally (48%). That's hardly surprising in a world emerging from Covid, with rapid innovation rollouts fuelling customer demand. But the landscape is more nuanced than that. The same report highlights an enduring sense of faith in the high street face-to-face experience, with 64% of customers confirming their ongoing trust in traditional banking models. A quarter of customers also say that a company's ethics (27%), sustainability (24%), and incentives (23%) all play a role in their choice of financial services. These are areas where building societies are well placed to deliver, even while enhancing the digital offering, to retain and grow their market share.

In the case of mid-tier banks and building societies, though, blending the branch-led customer experience with new digital offerings is a tricky balancing act. Typically, these mutuals enjoy a regionally-led, loyal customer base – with relationships often built over years of service. Our conversations with such clients tell us that targeting the biggest market share is not necessarily their number one priority. Instead, they look to differentiate from market dominating banks and rapidly emerging FinTechs by offering targeted, personalised products for longstanding and new customers alike.

Of course, to meet the modern customer's needs, digital must be a part of the mix. And, with all transformation comes risk and complexity. This is a particular conundrum for building societies, since their mutual structure creates a perspective driven solely by customer need rather than shareholder benefit. Historically, their robust attitude to risk involved a comparatively cautious approach, with expansion of existing capabilities prioritised over big ticket step changes. The result is that many building societies are embarking on the digitisation path in the context of significant legacies – not just operationally, but culturally. Now, they're reaching a tipping point. Big decisions need to be made between treading a tried and tested path – dependable, but not equipped to flex – or diving into a brave new world of digital architecture. Is it possible to bridge the two?

The answer, of course, varies depending on each building society's objectives, culture, legacy, and supply chain. But, in our experience, some considerations hold true across the board.

Legacies extend beyond systems – but beware eliminating them altogetheronline:

The traditional building society approach is characterised by face-to-face, branch-based services, driven by customer loyalty, and incorporating a sharp focus on risk management and mitigation. But, as demand for digital banking increases, the pendulum is swinging rapidly from a risk of transformational change perspective to a focus on market innovations and the risk of doing nothing. This means that building societies operating within legacy constrictions must make crucial decisions on digital transformation right across the people, process, and technology estate. Many of those relate to systems architecture. Others are less tangible – but still vitally important. Understanding cultural and behavioural dependencies is every bit as important to delivering digital transformation as addressing end-of-life platforms.

Often, a loyal, longstanding workforce brings with it a rich pool of knowledge built over many years. The temptation is to see shiny new platform capabilities as the key to an automated future. In fact, it is the gatekeepers within the organisation who truly know what human input is needed to keep those systems running – and who can provide vital intelligence when tackling transformation challenges. But those gatekeepers rarely have a voice at the executive table. Providing a safe avenue for them to share their lived experiences and practical capabilities, while also identifying and resourcing any skills gaps that may exist in the area of strategic transformation, can make all the difference between a savvy, risk-controlled transformation, and an expensive mistake.

Supply chains must be brought along for the ride

The supply chain ecosystem in this market is limited, and often relationships with suppliers extend over many years. This can be a huge strength – but a comfortable supplier in a long-term contract may have little motivation to change the status quo. After all, facilitating digital transformation for customers may, in this space, also involve vendors addressing their own internal legacies to provide the new architecture required. Legacy ways of working may hinder vendors' ability to work together to offer integrated, hybrid and adaptive solutions for the client. Mix in the fact that the decision-makers often lack the specific technical knowledge needed to advocate for change, and there is a high chance that the supply chain becomes a blocker.

If the supply chain has become complacent, challenging conversations lie ahead. But handled the right way and from the right perspective, there are discussions that can generate new possibilities for the transformation roadmap. Building societies need to ensure that supply chain solutions align in a practical, achievable way to the organisation's objectives, risk landscape and benefits map. Negotiating that may not be easy, but getting these parameters right sets the conditions for success.

The importance of benchmarking the big decisions

For mid-tier building societies, one question around digital transformation always rumbles below the surface:

"What if we get this really badly wrong?"

Market leading multi-nationals may be equipped to risk losing millions on a failed transformation. Mid-tier mutuals, however, are not. So, how can they achieve the peace of mind of knowing that the right decisions are being made for the right outcome?

An important factor to remember is that no change happens in a vacuum. At this market level, whatever strategy is being considered, it will have been modelled before by other organisations in similar positions. So, there are precedents out there that can guide the journey. What's more, sound decisions don't always have to be headline decisions. An 80/20 mindset, which focuses on pragmatic strategies, is a far more effective approach for building societies that cannot justify moving beyond a certain level of risk. Knowing what 'good' looks like and aiming for that, rather than being impossibly ambitious and falling at the first hurdle, will achieve a better outcome for customers investing not just their money, but their trust.

In all these areas, and at every step of the digital transformation, an independent, expert view adds considerable value. The right support equips clients to continuously improve and evolve. What's more, in a regional market, where organisations tend to complement rather than compete, the opportunity for knowledge transfer is ripe, and is a process that independent advisers can facilitate. By embracing that opportunity, understanding cultural and systemic dependencies, adopting a pragmatic mindset, and validating decisions with an independent view, building societies can successfully navigate the balance between meeting new customer demand, managing risk, and designing a secure digital future.

Insight overview

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Part 2 of 3 - For meaningful digital transformation, Building Societies must change the supply chain dynamic

In the rapidly evolving landscape of financial services, building societies find themselves at a digital transformation crossroads. In the second of this three-part series, we explore the intricacies of navigating legacy systems and fostering collaborative, forward-thinking supplier-client relationships to drive digital evolution.

Industry

Banking

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For meaningful digital transformation, Building Societies must change the supply chain dynamic

Customer demand for digital services makes transformation a commercial priority. But, in the risk-aware environment that typifies mutually incorporated organisations, where budgets are not unlimited, moving from incumbent legacy platforms to full digital innovation can feel like a chasmic leap. And the challenges are not simply technical. Building societies must be inquisitive enough to re-examine the supplier/client status quo and seek a new, iterative partnership model to drive the transformation roadmap. The organisation that gets on top of what is as much a cultural as an operational conundrum is the organisation that will win out, says Mason Advisory Managing Consultant, Catherine Randles.

This article is the second of our "Digital Transformation Tipping Points" series for financial services organisations.

You can read the rest of the series here:

Insight 1: Building Societies face a digital transformation tipping point – but where do the challenges really lie?

Insight 3: Digital value creation in the Building Society marketplace: how do we marry technology with tradition?

In the first of my insight series on the digital transformation tipping point for building societies, I tackled the strategic decisions that must be considered, understood, and overcome to deliver modern digital banking services while also controlling financial, commercial and regulatory risk. In the same article, I mentioned the complexities of a supply chain where legacy architecture may present a blocker to successful transformation.

I was struck by the response. Mason Advisory's clients confirmed that I had touched on a subject that resonates – and that they would appreciate a follow up piece exploring the supply chain ecosystem in more depth. So, this article looks at how building societies can get the best from their supply chain to support the digital evolution that their business and their customers need.

When it comes to transforming core banking platforms, where do the legacies lie?

As it stands today, most building societies and other mutual and cooperative businesses remain focused on their core banking offerings (savings, mortgages, insurance) and their core customer pledge (personal, trustworthy, often branch-based services). But financial services are evolving– and building societies are keenly aware that balancing evolving digital offerings with their existing USPs will be a crucial strategy to sustain success.

The reality, though, is that most building societies are still operating via legacy systems, typified by single platform architecture. Such platforms, in 2023, may well be thirty-odd years old. Plus, in many cases, they have always represented a pared down version of the available technology, even as it stood in the 1990s. A reliable workhorse, certainly…but not a solution that lends itself to digital innovation.

Why? Because the reality is that digital innovation demands architectural agility. Incumbent core platforms, dependable though they may be, do not have the capacity to underpin a smorgasbord of new, flexible solutions that can be rolled out as opportunities present themselves. Instead, front-end possibilities end up being dictated by the established back-end architecture – which cannot just be switched off at will. Yet, the alternative – a costly and complex total legacy replacement – is unpalatable from a time, cost, and risk perspective.

What's more, suppliers, in their eagerness to retain valued contracts built over decades, may be reticent about admitting their own internal legacy constraints. That's understandable. Longstanding service and long-term relationships bring obvious benefits that are to be embraced. Of course, suppliers are keen to maintain the value they have worked hard to build. But there is no escaping the fact that, if there is no transparency over the supplier's own limitations as well as the client's challenges, an intelligent conversation about what the future holds will be virtually impossible.

'Going Greenfield' in a legacy environment: evolution, not revolution

> *There is only one way to eat an elephant – a bite at a time.*
>
> **Desmond Tutu**

Of course, as the world experiences what many are calling the 'Fourth Industrial Revolution', plenty of disruptors are emerging who offer the kind of agile, Greenfield innovations needed to respond to fast changing customer demand . The question is: to what extent do large legacy suppliers have the capability – or indeed, the appetite - to incorporate those new models and ways of working into their own supply ecosystem? From the supplier's perspective, doing so would require significant financial investment, time, and cultural as well as technical change – and they need motivation to make that commitment. From the client's perspective, moving from 'how can we adapt the core platform we've got?' to 'how can we plug in stackable, scalable technology that will deliver what our customers need?' is a difficult transition to tackle without significant technical expertise and support.

To overcome this dynamic – which can rapidly turn into a blocker to progress – we need to generate a new dialogue, rooted in courage, transparency and trust between supplier and client. Both must be willing to expose their own vulnerabilities and limitations (as well as strengths!) to initiate a meaningful debate around how they can evolve together. This is a change in itself and, like any change, it carries risk. But, as is so often the case, the risk also has the potential to generate significant rewards.

Changing the supply chain dynamic from the inside out

In my experience, it is far better to embark on a supplier/client partnership where defined goals are delivered on a regular basis, than it is to attempt an unrealistic end-to-end transformation that is likely to fall flat, causing considerable cost, delay, and demoralisation when it does. To avoid that scenario, we must move away from a legacy 'waterfall' approach and towards a roadmap where incremental changes are mutually agreed, tried, and tested. New sources of expertise will almost certainly need bringing into the mix to complement existing capabilities. This, in itself, can present a cultural challenge to an incumbent supplier, whose linear working model may not be geared up to accommodate smaller disruptors, with their scrums, sprints, and agile delivery. In a situation where the supplier/client relationship often relies on a precedent established over decades, simply jumping into these conversations can spell disaster if neither party really knows what they're aiming to achieve.

So, where do we start with all of this? First, building societies must take steps to truly understand what they really need across people, process and technology to generate the solutions that their customers want. Then, they must build the right strategy to guide them from their legacy state into that target model. The supplier (including critical tertiary suppliers) needs to be a part of that conversation from the start. And I do mean conversation - not contract. Because planning the journey as a mutually beneficial one, and honestly discussing what needs to change on both sides to deliver, are meaningful first steps to informing productive ways of working moving forwards. You will, of course, need to wrap a contract around what is agreed, but a contract informed by a healthy level of real-world debate is a contract that is far more likely to deliver its intended outcomes.

This whole process is fraught with cultural, technical, and practical pitfalls. The help of an independent advisor can bring invaluable real-world experience to the table, to guide negotiations moving forwards. Similarly, an advisor adds a neutral and authoritative voice, giving both parties confidence that, even if the debate is entering unchartered waters, the course towards digital evolution is being plotted with realistic expectations and everyone's benefit in mind.

Insight overview

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Part 3 of 3 - Digital value creation in the Building Society marketplace: how do we marry technology with tradition?

In today's financial landscape, building societies face a unique challenge - harmonising the timeless appeal of personalised service with the imperative to embrace digital innovation. In the last of this three part series we will address two pivotal questions: How do we seamlessly blend the personal touch our customers cherish with the demands of a digital era? And what, precisely, constitutes digital value in the eyes of our customers?

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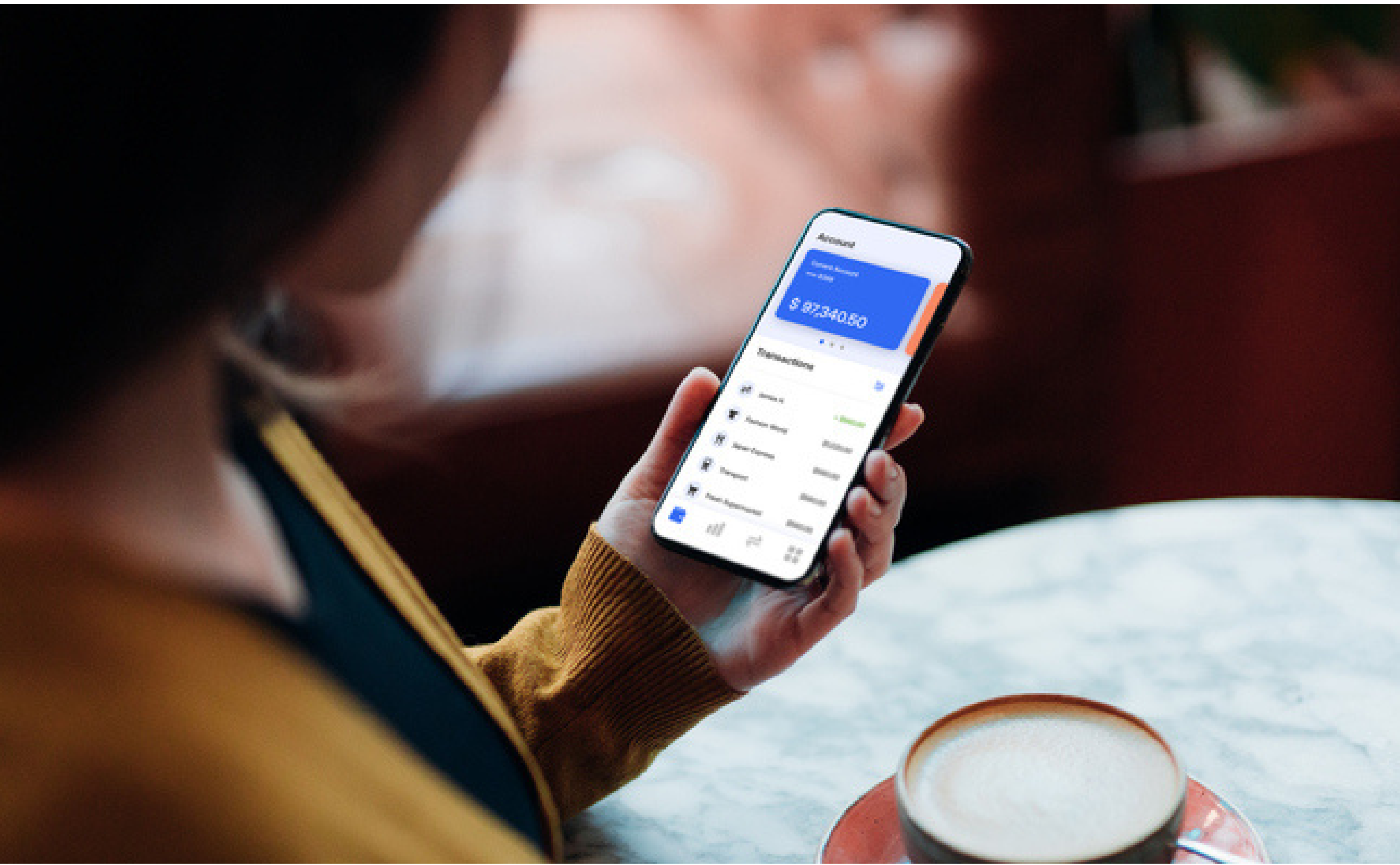


Digital value creation in the Building Society marketplace: how do we marry technology with tradition?

For building societies, marrying future-proofed digital value with a traditional branch-based model is particularly tricky. Two questions are key to tackling these challenges. How do we integrate the personal, flexible service building society customers are accustomed to with the need to 'do digital?'. And what does digital value really mean for customers? Understanding the answers is crucial if building societies are to strike the right commercial balance between new, innovative services and retaining customer loyalty, as Catherine Randles, Managing Consultant with Mason Advisory, explains.

This insight is the third and final in our "Digital Transformation Tipping Points" series for financial services organisations. You can read the rest of the series here:

Insight 1: Building Societies face a digital transformation tipping point – but where do the challenges really lie?

Insight 2: For meaningful digital transformation, Building Societies must change the supply chain dynamic.

In today's world, customer demand for digital banking services is more sophisticated than ever. 2021 saw global investment in Fintech soar to US$130 billion, reflecting the pandemic-driven boom in digital services. Admittedly, investment decreased by 30% in 2022 as the economic climate cooled. Interestingly, though, in the UK, investment held comparatively strong, falling by only 8% in the same year[1]. According to the same cited research:

- **93%** of British adults were using an online bank account in 2022
- **10%** Approx number of British adults intending to get a digital-only bank account in 2023
- **24%** British adults in 2023 with a digital-only bank account (compared to 9% in 2019).

Here's the interesting thing, though… the same research reports that:

- **24%** traditional bank account holders **do not trust** digital-only banks.
- **32%** Brits **do not intend** to get a digital-only bank account

Source:
https://www.finder.com/uk/digital-banking-statistics - Analysis conducted by finder.com

These figures suggest that, even though digital banking continues to grow, a significant proportion of the British public is not yet ready or willing to accept digital-only as a viable banking option. This bears out my own experience of working with Mason Advisory's building society clients. Typically, they retain a loyal, regional, in-branch customer base. Mortgages and savings remain a core offering. Building societies currently hold 24% of the UK's gross mortgage lending share, while savings balances increased by £8.4 billion in 2022, accounting for a 34% share of the UK savings market[2]. As discussed in my first insight in this series, traditional banking still wins out on trust (66% of customers), against digital-only banking (37% of customers)[3]. So, although digital is an indisputable part of financial services moving forwards, it seems that the UK population has not fully bought into the digital-only narrative – or, at least, not yet.

Engineering digital value for both customer and organisation

In fact, this landscape offers a differentiated commercial strength for building societies. Their established model still plays well to the 'trust' theme. Yet, looking ahead, the greatest opportunities exist for organisations that have put in place the fundamental digital foundations for growth and profitability. Building societies are likely to face tough consolidation decisions to stay competitive. Right now, though, a seismic shift that eliminates bricks and mortar in favour of digital-only services seems a shift too far. In what is effectively a hybrid scenario, decisions around digital represent a tipping point for building societies. The key decisions lie in how to ensure that digital does, indeed, create genuine value for the customer as well as engineering commercial value for the organisation. For me, there are three headlines that must be understood to design the right digital value roadmap:

1. Creating digital value is not the same as 'doing' digital transformation

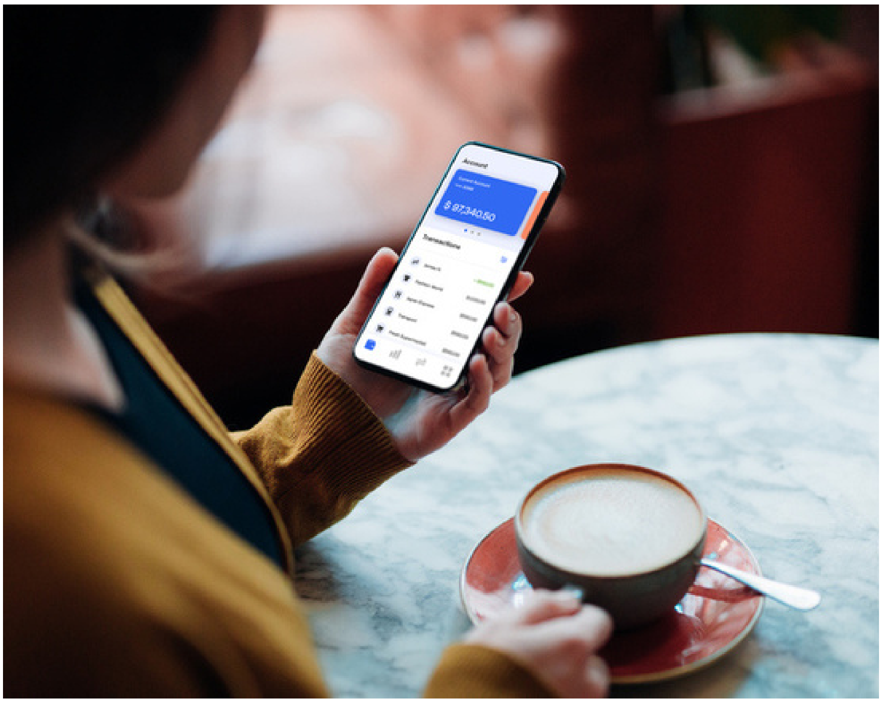
At its core, true digital value lies not in technical delivery, but in the skill and strategy of remaining relevant to the customer at every touchpoint. This means providing a trustworthy experience, a meaningful emotional engagement, and a solution to the customer's problem, all at once. It is a deeply complex objective to achieve. Plus, certainly in the current account and savings markets, today's customers have the freedom to switch financial services providers comparatively easily. Build in the brutal world of digital abandonment (in 2020, 63% of customers abandoned a digital banking onboarding process[4]) and it is easy to see how failing to create a genuine digital value experience can quickly and negatively impact on customer acquisition and retention.

2. Building a digitally capable ecosystem is key

If there is one stark lesson the past two years have taught us, it is that even the biggest businesses can't predict the future. We cannot know with certainty what financial services will look like in a year – let alone five, or ten, years from now. But we can address the digital ecosystem so that, when the next big customer-led evolution comes along, the organisation is equipped to pivot and deliver. This requires work – now – to ensure that stackable, scalable digital infrastructure is in place and ready to adapt. For building societies, that work is extremely challenging, given cautious investment budgets, legacy supply chains, and a high level of risk-awareness. But, complex though the process is, investing in digital value capability is a growing commercial imperative. And it needs to be effectively led, which in turn leads me to…

3. The digital value strategy must be steered with confidence

To ensure building societies remain relevant, those leading the strategy need to ramp up the pace and nature of decision-making. Those decisions will almost certainly be all about change – whether the change is expected and welcome, or not. That, especially when the outlook includes unknowns, is a daunting prospect – even for the most seasoned executive. Nonetheless, decisions must be taken and cascaded effectively, to ensure that the business is ready to stay on the digital front foot, however the landscape pans out.



Fundamental to all this is a recognition that digital value creation is not about doing things faster, or cheaper, or even more efficiently. It is about recognising what a customer values (trust, experience, and relevance), translating that to the online experience and enhancing that value through digital capabilities. Building societies are uniquely positioned to travel that journey from their starting point of customer loyalty. That is not to say that the journey itself isn't difficult. But, with the right understanding and insights into what it really means to create digital value, it is a journey with the potential to generate the next level of commercial success.

[1] Digital banking statistics 2023, Finder.com, February 2023
[2] Latest BSA statistics, bsa.org.uk, December 2022
[3] The future of financial services, business.yougov.com, March 2022
[4] The Battle to Onboard 2020: The impact of COVID-19 and beyond, signicat.com, June 2020)

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About Mason Advisory

Mason Advisory has offices in Manchester and London and employs over 100 staff, with plans to continue its expansion. We enable organisations to deliver value through digital & technology transformation, solving complex business challenges, and helping clients set strategy through the intelligent use of IT resources including architecture, cyber, operating model and organisational design, service management, and sourcing. We operate in sectors such as financial services and insurance, legal and law, government, health and social care, emergency services, retail, FMCG, transport, and not-for-profit.

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