Harnessing the power of disruption

Why financial services needs a new view of disruption – and how to turn it to your advantage

pwc

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This guide was prepared using the capability of Strategy&, PwC's global strategy house, alongside the input of PwC's disruption and financial services experts. We transform businesses by developing actionable strategies that deliver results. We call this, Strategy, made real.

Over the next few months we will be co-creating and expanding on these ideas, via video and workshops, by bringing the best of a wide range of views together from those who work within, or alongside, the financial services industry. We look forward to sharing our developing views.

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It’s time to see things differently

Why financial services needs a new view of disruption.

~£100bn

of revenue subject to disruption by 2030.

Disruption in financial services could total approximately £100bn of revenue in the UK by 2030.

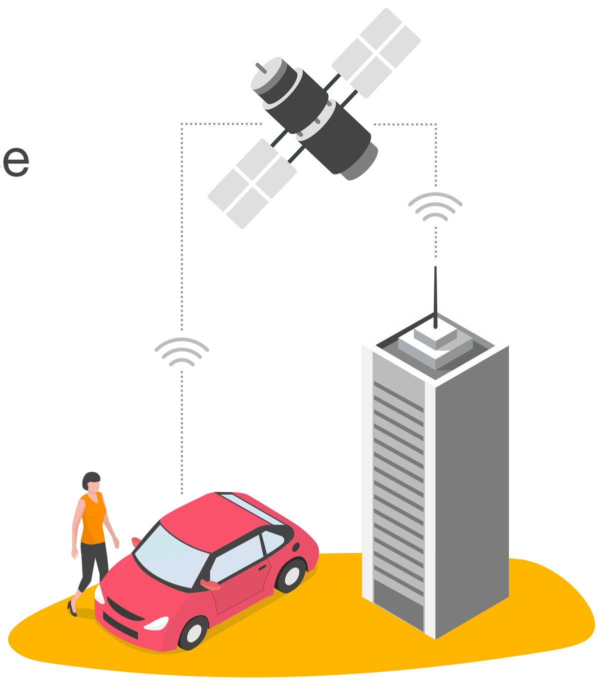
But to take advantage means thinking about disruption in a new way. That’s because disruption is not a single event or trend. It happens when different forces collide: customer appetite for change meets the right enablers: technology, regulation, funding, ease of switching and talent.

Only businesses that understand the currency of collision will be able to spot disruption before it happens – and position themselves to respond and take advantage.

So how do you understand what this looks like for your industry and business? What are the forces that will collide to create disruptive change for you? More importantly, how will you change your perspective to position your business for success?

“Why should my car insurance be based on demographic profiling, rather than my actual usage?”

“Why does my FinTech need a bank to IPO?”

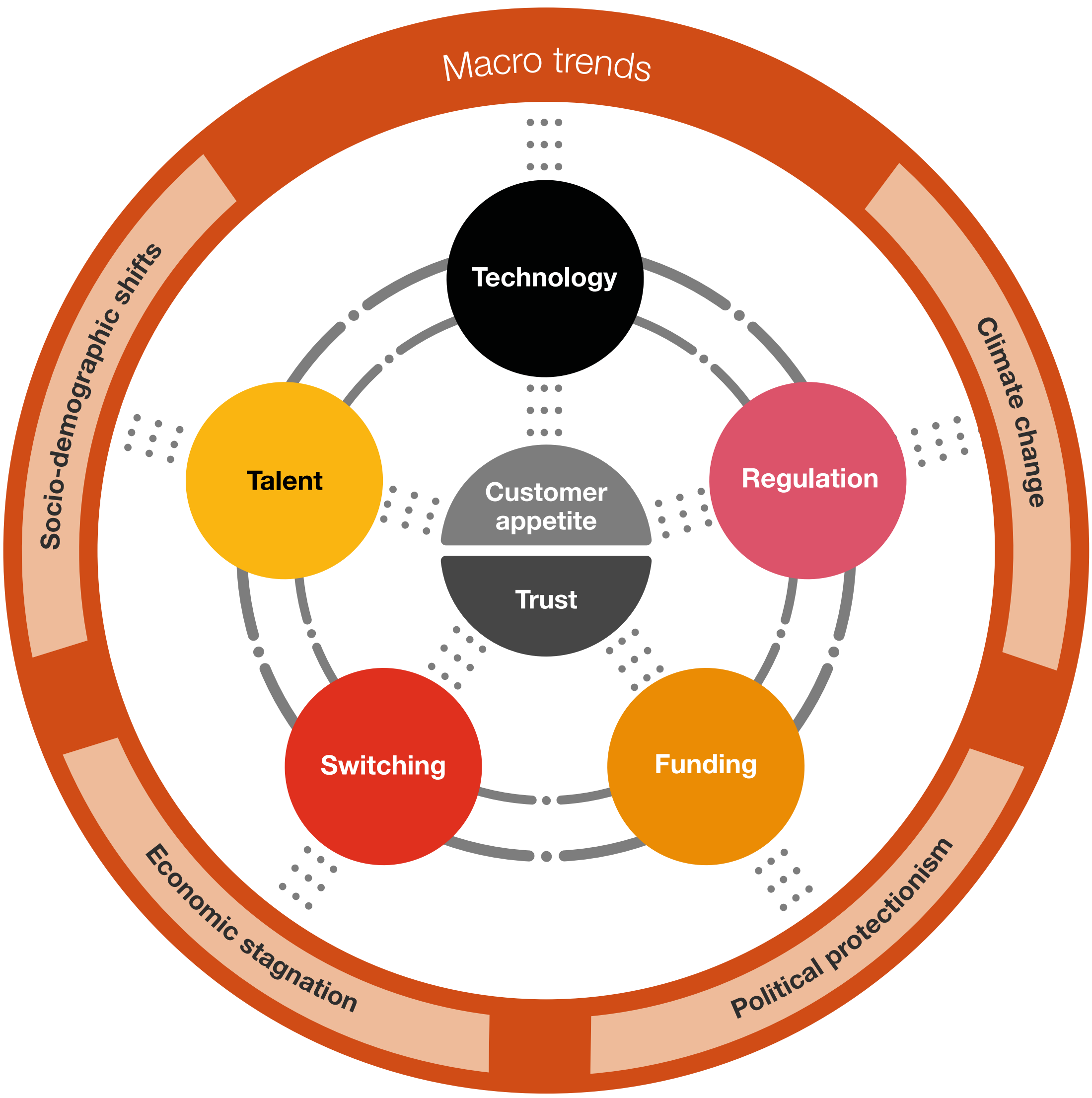


Introducing the currency of collision

Capitalising on the opportunities disruption could provide for your specific sector is not about applying a narrow focus. Quite the opposite. Instead, those that will set themselves apart will be able to do so by broadening their field of vision.

The next wave of disruption will not simply be driven by technological innovation – the real opportunities will be found where the enablers of disruption collide. Where falling trust in banks collides with a wave of new coding talent. Where rapid urbanisation collides with more competition friendly regulation. It is at these collisions where true disruption arises and multiplies.

Conditions for disruption – more than just technological innovation



The collision lens: four factors, one powerful new view

A new perspective of disruption comes from achieving an all-encompassing view. This sees all of its drivers, at once, through a single lens that can capture how they dynamically interact. It is this view which allows you to see when the fundamental assumptions that your business is based on are shifting:

Customer Appetite

Customer appetite changes when there is an opportunity to serve customers in a better way. That could be by improving how their needs are already met through new and better experiences. It might be by reducing price or by addressing currently unmet customer needs.

Example: When banks no longer need a physical branch to serve their customers.

Enablers

The enablers of disruption are the factors making it possible for players to bring a disruptive proposition to market. There are five main enablers that are crucial for disruption in financial services: technology, regulation, funding, ease of switching and talent. Where these enablers collide with customer appetite is where the opportunity lies.

Example: When venture-capital (VC) firms make large volumes of funding available for early stage companies with disruptive ambitions.

Trust

Trust is a key driver for players looking to win in certain financial services sectors. In particular, when customers are parting with a significant proportion of their wealth, trust plays an important role in their selection of a provider. In these instances they are more likely to select an incumbent player with a long track record and a trusted brand. This can make it difficult for new entrants to be successful in these sectors, regardless of how disruptive their propositions may be.

Example: When investment management startups struggle to achieve scale due to a limited track record.

Macro trends

Macro trends can impact all other aspects of the framework. They mainly influence customer demand for new products (e.g. socio-demographic shifts generating demand for new retirement products), but they can also impact the enablers by causing talent, regulators, and investors to turn their attentions towards addressing changing market dynamics.

Example: When the poorest 10% of Britons are paying a higher effective tax rate than the richest 10%. (49% compared with 34%).[1]

1 Oxfam – Private Good or Public Wealth – Jan 2019

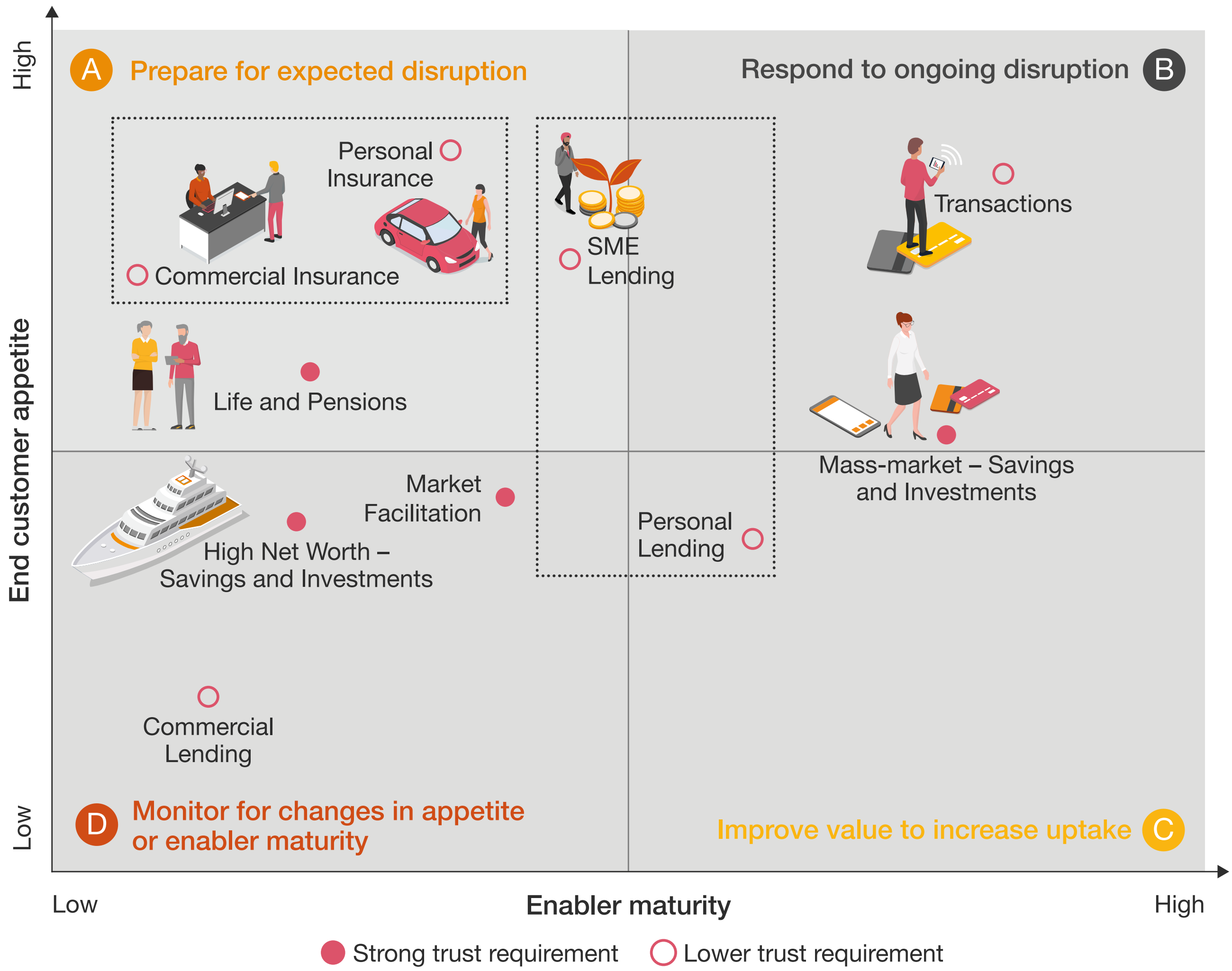
The question is not if, it's when

Understanding the relative disruptive maturity of each market is vital. This doesn't simply help you spot where the biggest opportunities lie, it also indicates how long you will have to respond.

Today, different customer needs are at different stages of readiness for disruption.

It's already happening in transactions as well as savings and investments. The drivers? Strong customer appetite for change in these areas is meeting a mature set of enablers like regulation, increased ease of switching and well-developed technology.

Disruption readiness by financial services sectors



How will you respond?

Your best response to disruption – and the urgency you may need to respond with – is affected by two factors: the appetite customers have for something new and the maturity of the enablers of disruption.

A – Prepare for expected disruption

Where high customer appetite for disruption meets low enabler maturity, players need to act now to get ahead of the crowd. For example, incumbents should look to enhance customer loyalty and invest in technology. We've provided some detailed examples on the following pages.

B – Respond to ongoing disruption

High customer appetite and high enabler maturity creates a market dynamic where disruption is already forcing incumbents to make changes. In transaction banking, for example, new digital challenger banks have entered the market and forced incumbents to respond with new propositions, transforming the customer experience. Mature enablers encouraged this activity. Regulation around obtaining banking licenses, for example, were simplified for new entrants, and customers became increasingly likely to bank with multiple providers due to low switching barriers. There were both a significant amount of funding available for new transaction banking startups (accounting for 50% of venture capital FinTech investment in 2017) and a growing talent pool with banking and technology experience. Players in this space, including those in mass-market savings and investments need to respond quickly, for example by developing partnerships and targeting market niches.

C – Improve value to increase uptake

With low customer appetite and high enabler maturity, there is less urgency for players. For example, personal finance may often be cited as vulnerable to disruption, but with limited demand from customers for new propositions, is likely to remain undisrupted at least for now. Historically low and declining margins in this sector indicate that supply is outstripping demand. In addition, upcoming regulatory scrutiny and the pressures of sustaining a full economic cycle may also act as a barrier to disruptive entrants. Avoid the urge to rest on your laurels, however. Players in this sector should keep a close eye on changes in appetite (e.g. the emergence of peer-to-peer lending as a preferable option for those not able to access lending through mainstream sources) by expanding advantages and investing in startups.

D – Monitor for changes in appetite or maturity

With the immediate risk of disruption low due to a lack of both customer appetite and enabler maturity, you'd be forgiven for a 'wait-and-see' mindset. Within commercial finance, for example, there is limited scope for significantly improving either experience or price in corporate wholesale lending. While there is more demand for new ways of raising equity finance, this limited by the high-degree of trust customers demand from providers. The enablers for this sector are also less mature. For example, there are high balance sheet requirements which creates significant funding constraints. There is also low to moderate maturity of technology used to optimise deal origination and servicing. There's still action to be taken, however. Players in these sectors should look to improve value to customers through enhancing offerings or targeting under-served customers. For example, there are some new entrants looking to offer cheaper alternatives to raising finance (e.g. Spotify's recent Direct Public Offering) to traditional investment banks.

Where will it hit next?

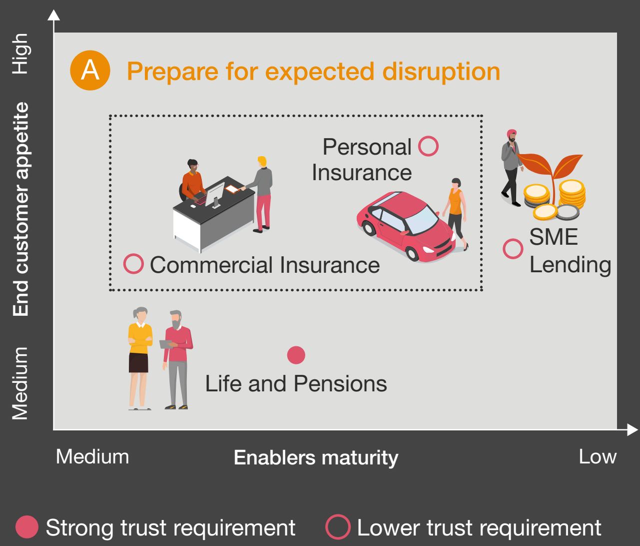
Insurance customers want change. Consumers are looking for more than the traditional, low-touch products they have today. SMEs, too, are eager to explore new ways to access funding and they're open to innovative propositions that will enable them to do that.

£54bn

Section A represents a £54bn revenue opportunity.

And where there's a will – or in this case, customer appetite – there's a way to disrupt either yourself or the market. It is this combination of high consumer appetite combined with rapidly changing enablers, which we believe represents the next wave of disruption in financial services.

By understanding the collision of factors in your sector, you can assess how quickly disruption is likely to have an impact. And then you can start to plan your response with the right amount of urgency.



SME Lending

37%

Adjacent players and P2P lending could disrupt 37% of SME access to finance by 2030.

Key drivers

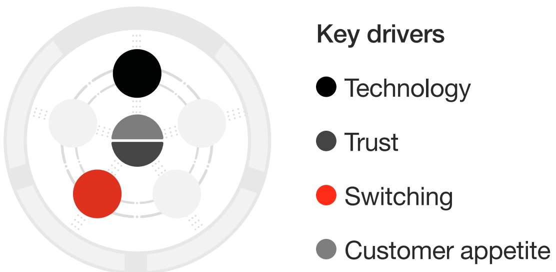
- Technology
- Funding
- Talent
- Customer appetite

SMEs' financial needs are also being met by new players offering an alternative to the traditional sources of funding. In China, for example, internet giants such as Alibaba and Baidu, are able to make rapid credit decisions based on customer data and sales records. They now service c.10% of the SME market. Closer to home, new entrants in the UK like Tide and Starling aim to provide SMEs with a digital banking experience in line with personal services. Other peer-to-peer lending players, such as Funding Circle, are providing SMEs with easier access credit and growing quickly.

Personal Insurance

24%

Due to the changing nature of risk and better data, 24% of personal lines could be disrupted by 2030.



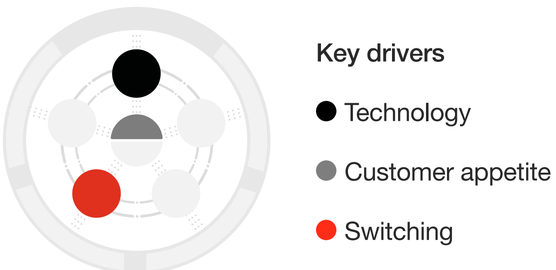
While change in this market has been limited to date, customer appetite for new propositions is high, thanks to the perceived relatively low levels of customer service and relatively inflexible purchasing channels. New entrants are already capitalising on the demand for new, more customer-centric and digitally enabled services.

For example, Lemonade is a startup that sells home and rental insurance via a mobile app. The app is supported by an AI-driven digital assistant that enables customers to buy and manage their policies with minimal effort.

Commercial Insurance

25%

Emerging risks and new tech could drive disruption in commercial lines equivalent to 25% of revenue by 2030.



Commercial insurance, particularly for SMEs, is another strong candidate for disruptive plays. Today, 80% of policies bought by SMEs are via brokers or other intermediaries.

While only 40% of SMEs buy insurance online, many struggle with the inefficiency of the distribution and servicing models that are available today. A US-based startup, Cover Wallet, aims to address those frustrations by making commercial insurance simple, convenient and better value.

Customers can buy directly from Cover Wallet, but the startup also enables SMEs to offer Cover Wallet insurance through their own websites. Brokers are also able to access the platform to help them serve their clients more efficiently.

Life and Pensions

30%

The 2015 Pension Freedom Act and changes in distribution could enable 30% of revenue in life and pensions to be disrupted by 2030.

Key drivers

- Macro trends
- Technology
- Regulation
- Customer appetite

The trends reshaping the pensions and life insurance markets are largely the increased life expectancy of the population, along with changes to regulations governing the pensions market. While the trust that existing policy holders have in their providers and the relative complexity of switching create barriers to new entrants, the opportunity to address the needs of those with little or no long-term provision is likely to be significant.

Whilst pension disruption will be catalysed by regulatory reform, new distribution models could drive disruption in life insurance. For example, Anorak is an automated life insurance platform that aims to help the 8.5 million people in the UK who have either no or inadequate coverage. Anorak's platform uses machine learning applied to customer data to provide tailored insurance recommendations.

Who is best positioned to take advantage?

Responding effectively to disruption takes more than simply spotting where the future opportunities could arise. There's also the need to be agile. You mustn't fall into the trap of believing that first mover advantage belongs to the big tech players or nimble FinTech startups. True, the big tech players and startups have a number of clear advantages, with their digital capabilities being just the most obvious.

However, these new players don't have a monopoly on the creative mindset, responsive business models and transformational approach that winning in a disrupted world demands. If today's incumbents can combine those attributes with their established relationships and foundation of trust, they could be well placed to win and gain from the opportunities that disruption promises.

Who are the contenders – and what do they offer?

New entrants

Startups or totally new business models created to take advantage of disruption.

Objective

Attract customers and build trust.

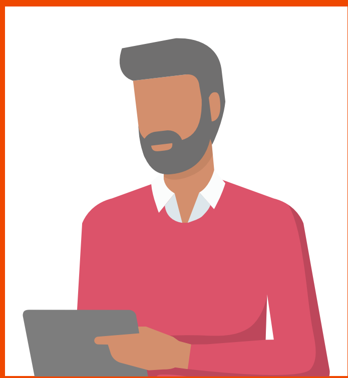
Strengths

Agile model built around customer need, technology-enabled.

Challenges

Need to build reputation and trust with regulators and customers.

Adjacent players



Established businesses from other sectors – typically technology.

Objective

Transfer existing customer trust and relationships from current industry to financial services.

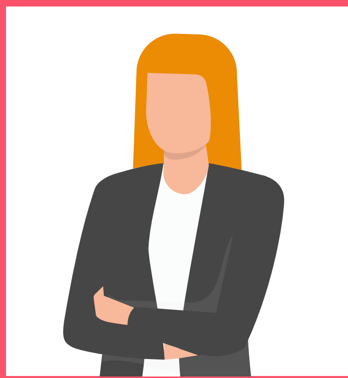
Strengths

Strong brand relationships, data assets, analytics and platform to spot and service unmet customer needs.

Challenges

Limited trust and brand in financial services. Regulatory demands.

Incumbents



Established financial services players.

Objective

Maintain customer relationships as services become modularised, and harness their existing capabilities and scale to defend their market position.

Strengths

Established trust and deep customer relationships.

Challenges

Legacy technology and infrastructure which can hinder agility.

How much is at stake?

Sizing the opportunity

~£100bn

Subject to disruption by 2030.

With approximately £100bn of revenue subject to disruption by 2030, how will you decide where to place your bets – and what will be the size of your stakes?

Where will you be able to play to your strengths? We've assessed the size of the prize and considered the likely winners. To assess the size of the potential prize, take a look below.

Share of the market disrupted
%, by sector, 2030

Sector	Share of the market disrupted	Likely winners: New entrants	Likely winners: Adjacent players	Likely winners: Incumbents	Estimated value of disruption (£bn)
SME Lending	37%	✓	✔		4.1
Transactions	35%	✔	✓		34.6
Life and Pensions	30%			✔	15.9
Commercial Insurance	25%	✓		✔	27.0
Personal Insurance	24%	✔	✓		6.6
Mass Market – Savings and Investment	15%			✔	3.5
Market Faciliation	11%			✔	4.6
Commerical Lending	8%	✓		✔	1.9
Personal Lending	7%	✓		✔	6.2
High Net Worth – Savings and Investment	2%			✔	1.8
					Total revenue c.£106bn

Key: ✔ Primary disruptor ✓ Secondary disruptor

Creating the right response means asking the right questions

Key questions to address when responding to disruption

Strategy & business model	Customer centricity	Deals & structure	Risk & regulation	Data & technology
What will your value proposition be and what differentiating capabilities will you use to compete?	How can you build truly customer centric propositions and operations?	How can you use partnership, restructuring and deals to stay ahead of the market?	How will you ensure that risks are understood and managed, and how will full regulatory compliance be achieved in a rapidly changing environment?	How can you embed world class data analytics into products and deliver a modern technology platform?

Asking the right questions is key. A new, mobile-first bank, for example, needs to know which client segments are more likely to use digital and mobile services.

They'll need to find out what those potential clients want from a service and only then be in a position to develop the digitally-enabled models that can meet a complex range of needs.

Alternatively, they should identify what the potential customer base is for a new offering and how well they're already served by competitors. Or questions may focus on identifying which technology capabilities will be needed to achieve best-in-class product areas.

Canopy

Case Study – How PwC helped a potential disruptor

Take InsurTech startup business, Canopy, as an example of a business aiming to disrupt the rental market. Canopy offers an insurance model that replaces the traditional deposit that renters moving into a new home require. It also provides a RentPassport feature that combines a user's rent and credit history which helps landlords to pre approve renters, and offers a range of insurance products to tenants.

We helped Canopy define its product strategy, redesign its user interface and create new experiences built around the user to make the app as intuitive, useful and easy to navigate as possible. The results saw this new business attract significant new investment from existing insurers as well as forming new partnerships.

Turning disruption to your advantage

Responding positively to the challenges and opportunities of disruption means asking and answering a broad range of questions. By framing your questions – and developing your response – with a quantified awareness of the market and an appreciation of the nature of where enablers collide, you can more quickly and effectively scope the nature of transformation you'll need to win in your markets.

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pwc.co.uk/currency-collision