Are Banks Prepared to Take Customers' Financial Health Seriously?

A manifesto for providing people with the right tools to meet their financial needs.

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At a Glance

- Economic fallout from the coronavirus highlights the fragility of many households' finances, and banks should design offerings to help customers lead financially healthy lives.
- To do this, banks need to unbundle and rebundle their existing products and services around four core themes: enabling day-to-day household financial management, empowering exchange, unblocking financial accumulation and decumulation, and putting customers in control of their money, relationships and data.
- The approach requires using modern digital and artificial intelligence capabilities to deliver on an agenda of 16 specific product and service innovations.

The coronavirus pandemic is an immediate crisis with likely long-lasting repercussions. The fragile economy of nonpermanent employment, short-term contracts and cheap credit have exposed the lack of resilience in household incomes and budgets. And the price of asking for good citizenship from everyone during the lockdown period will be a huge and enduring fiscal burden.

Almost certainly, the pandemic's response will reopen the debates on societies' approach to household financial resilience (universal basic income, statutory sick pay) and the future of taxation, and of income inequality more generally. Hopefully, banks will also come to take seriously the view that their core purpose is helping customers lead financially healthy lives.

While this isn't a new idea, banks' responses to this have ranged from the frivolous (spending trackers, savings goals) to the paternalistic (financial education, financial heath checks). Implicit in these responses is the presumption that financial ill-health results from customers' indiscipline or ignorance. What banks haven't focused on is how *their products and services* fall short of what's required for managing a financially healthy lifestyle.

Reimagining banking based on real customer needs isn't straightforward. And, offering customers existing products and services with add-ons like interesting data and alerts and better servicing controls won't be sufficient to promote healthy financial habits.

Future banks will likely need to innovate using rather different sources for inspiration. For example:

- **The unbanked.** People living on less than $2 a day already have their own financial-management tools and devices independent of banks.
- **Physical health.** Modern lifestyle-oriented health issues (e.g., obesity, heart disease) are being tackled by helping customers establish and embed good habits.
- **Digital remaking.** The path to digital remaking (say, in music) is the unbundling of existing products and services (Napster, iTunes) into components, followed by rebundling into services more reflective of customer needs and control (Spotify and Pandora).

Ultimately, though, future banks will be defined by how they address or remake banking in four key areas:

- **Enabling day-to-day household financial management.** Unbundle and rebundle basic banking products to give customers the ability to manage their working capital, finance large purchases and have rainy day protection.
- **Empowering exchange.** Extend payment capabilities to address the trust barriers that limit real-world exchanges across person-to-person, e-commerce, sharing-economy and experience-economy scenarios.
- **Facilitating financial accumulation and decumulation over time.** Redesign wealth from focusing on wealth management (asset allocation) to unblocking the real-world barriers to accumulation (such as mortgage access) and effectively drawing down that wealth (adjusting to changes in households and income).
- **Putting customers in control of their money, relationships and data.** Empower customers to control their relationship with the bank, including customer responsibility for selecting the types of services, access points and interactions with the bank. Act as trusted custodians of customers' valuable personal data and digital identity *(see Figure 1)*.

Enabling day-to-day household financial management

Studies of unbanked households consistently highlight three core needs of daily financial management.

- **Managing household working capital:** The ability to transfer money from when it's earned in the month to when it's spent daily;
- **Financing lump-sum purchases:** The ability to mobilize meaningful lump sums for more significant purchases through accessible savings or borrowings, or both; and
- **Providing rainy day protection:** The ability to protect themselves and their families and to cover unforeseen expenses related to, for example, accidents, illness or theft.

The digitalization of banking means that a financial-health provider can unbundle balance sheet-centric banking products and redesign them to serve customers' core needs in ways that are disciplined, cost-efficient and resilient. Following these core points are five themes relevant to the reinvention of day-to-day financial management.

Borrowing as a service

Managing access to, and use of, credit is central to customers' financial health. Disciplined use of debt, such as reverse savings, is one strategy to mobilize income to support household working capital management, lump-sum financing and rainy day protection, as well as investing for the long term *(see Figure 2)*.

Figure 1: Priorities to reinvent banking around customers’ financial health

	Challenges with today’s banking product set	Elements of financial health reinvention
Enable day-to-day household financial management	• Banks’ manufacturing defines product set • Retail banking products—individually and collectively—imperfectly support customers’ underlying everyday needs – Household working capital management – Lump-sum financing – Rainy day protection	• **Borrowing as a service:** Unbundle borrowing value chain into flexible service elements; reorient for customer control • **Fluid savings:** Remove product distinctions between liquidity and return on investment • **Interrelational banking:** Enable customers to manage financial relationships flexibly and simply • **Protection reimagined:** Provide customers a comprehensive means to protect against everyday bad luck • **Personal CFO:** Use analytics with all of above to help customers make good choices and support good financial habits
Empower exchange	• Payments services accentuate the money transmission process, but exchange in the real world is limited by trust • Empowering exchange recognizes opportunities to create more exchange through extending trust in the process, counterparties and the value of products and services	• **Social payments:** Expand peer-to-peer exchange combining payments with social interaction to enable simple, human assurances and reciprocity • **Buyers’ assurance:** Expand e-commerce payments through extended commerce protections and returns • **Instant contracts:** Enable sharing economy exchange through combining money and counterparty identity attributes • **Protection reimagined:** Expand experience economy exchange
Facilitate financial accumulation and decumulation over time	• Wealth products give primacy to asset allocation that doesn’t sufficiently address accumulation and decumulation challenges • Don’t consistently integrate housing wealth	• **Decumulation reimagined:** Enable household wealth to be drawn down, split or reaggregated to respond to the complex changes in household status, employment status and health events that we now expect over a lifetime • **Sharpened accumulation:** Translate the success of “mortgages as a savings product” into other forms of wealth accumulation • **Home ownership reinvigorated:** Address rigidities in “housing ladder” • **Advice reimagined:** Redefine financial advice as promoting and enabling good habits and choices
Put customers in control of their money, relationship and data	• Product-by-product level origination and servicing undermines end-to-end customer relationship • Bank-defined servicing model limits customers’ ability to control the relationship and interaction model • Bank-centric data model means customers don’t own or control access to their own data	• **Customer control center:** Enable customers to set, edit and manage their touchpoints, products, interactions, alerts and messaging • **Digital identity:** Enable customers to control their data and revoke access to it for banks and third parties • **Rewards wizard:** Promote relationshipwide rewards and maximize redemption flexibility

Source: Bain & Company

Figure 2: Customers use debt and savings to shift their wealth among four types of underlying financial needs over time

	Household working capital management *Covering everyday, in-month expenses and settling on payday*	**Lump-sum financing** *Making lump-sum purchases and spreading the cost over many months' income*	**Rainy day protection** *Accessing emergency funds in periods of misfortune*	**Investing for the long term** *Securing and building wealth for the future*
Typical spending categories	• Food • Utilities • Going out	• White goods, furniture • Consumer durables • Cars	• Accidents, repairs • Loss of income • Medical/travel emergencies	• Home buying • Ventures • Precious assets
Relevant debt instruments	• Revolving credit line	• Installment loans • Asset financing, hire purchase • Pay-for-use, X as a service	• Unused credit line • Emergency credit	• Secured loans • Long-term borrowing
Time horizon	• <30 days	• 2–36 months	• Ongoing	• Over a lifetime
Effective use of debt	• Disciplined household monthly budgets and spending controls • Low-cost, revolving credit line • Spending-relevant offers and rewards	• Planned or budgeted major purchases • Repayments budgeted monthly through predictable installments • Debt cost minimized, where possible, via choice of instrument and provider (supplier finance, renting, subscriptions)	• Preapproved credit or unused credit lines • Low cost when used: competitive rates or convertible into lower-cost debt subsequently	• Considered long-term commitments to using secured long-term debt servicing and repayment to build family wealth • Low-cost secured debt, predictable debt costs and debt-servicing costs

Source: Bain & Company

To support this effort, financial-health providers are increasingly unbundling borrowing around five distinct services:

- **Access to credit.** Helping customers maximize their creditworthiness and capacity;
- **Debt budgeting.** Enabling customers to create and manage different "debt pots" in a disciplined and transparent way (in-month groceries vs. a lump-sum car purchase);
- **Debt configuration.** Helping customers configure or tailor their use of debt and different debt instruments (revolving lines vs. installments) appropriate for different borrowing needs;
- **Debt sourcing.** Assisting customers in sourcing and refinancing debt to minimize debt cost; and
- **Repayment management.** Helping customers repay debt effectively and responsibly.

A number of companies are experimenting with aspects of borrowing as a service, such as Anyfin and ClearScore on credit accessibility, and American Express and Klarna on debt configuring.

Protection reimagined

A glaring omission in the traditional banking product suite, and in most banks' approach to design, is financial management's role in protecting customers against unforeseen emergencies and repairs. Banks may have viewed themselves less as protectors and more like vendors. In practice, though, having savings and credit buffers, as well as practical insurance in place, is central to a customer's financial health.

Further, general insurance as a sector is being extensively disrupted through digitalization and artificial intelligence, something banks are well placed to support. Overall, there may be four broad types of protection companies emerging from this disruption:

- **Insurance reimagined companies.** Reimagining insurance using the Internet of Things, digital interactivity and artificial intelligence to remake the entire insurance value chain, including targeting, registration and making claims, as well as taking insurance into entirely new sectors and forms;
- **Proactive protection companies.** Integrating prevention and response management with insurance coverage to more effectively limit customers' exposure to unplanned events;
- **Invisible insurance companies.** Supporting X-as-a-service offerings (sharing economy, pay-for-use economy) with integrated service protection and reliability; and
- **New community-based protection.** Reinventing community-based approaches (pooled insurance, supportive protection) using social media to build and maintain relevant communities.

Customer protection is a significant topic for financial health companies that will need to provide customers with easy access to protection against the unexpected. Top categories of unexpected expenses include: medical expenses, car repairs, pet emergencies, home repairs, gadget replacements, work-related expenditures, unexpected gifts and lawsuits, which can all receive new forms of digitally enabled protection. A number of banks have already begun integrating everyday protections into their services.

FIFO savings

The biggest challenge with remaking savings is to break down the product silos that ask customers to make upfront liquidity or interest-rate trade-offs (between current accounts vs. time deposits) that cut across customers' needs. To address this, banks can prioritize rewarding longer-term savings, not the initial upfront outlay. A manifestation of this has been the successful trials involving first-in, first-out (FIFO) savings, where higher interest rates are provided to long-term savings, but the money is always accessible. Digital disruption enables banks to create these kinds of savings services, which wouldn't be possible with legacy core banking systems.

Interrelational banking

Managing household financial health requires the ability to manage interdependent banking involving both relationships with children and other dependents, and sharing and pooling relationships (say, with people outside the immediate family) that may be more fluid than in the past. There's a wealth of innovation in this area, breaking down the barriers to effective sharing of banking services and responsibilities.

Personal CFO

Having unbundled and then rebundled banking products to help households manage working capital, finance large purchases and protect themselves against rainy days, financial-health providers will be better able to offer customers services that can be used in a disciplined and healthy way. Thus, financial health is about good habits, and a personal CFO should earn the permission to intervene in customers' lives to promote good lifelong financial habits.

This intervention can promote one or more of the following good habits for customers:

- **Self-discovery** to avoid self-denial in situations and choices.
  - Make self-discovery nonthreatening and fascinating through features such as gamification.
  - Make committing or aligning accomplishment-oriented and create tangible outputs.
- **Self-actualization** to avoid procrastination and inaction.
  - Make action easy through auto-enrollment or simplified registration by limiting choices.
  - Make action engaging by providing links to learning or competing.
  - Make inaction undesirable by sending reminders and prompts, and communicating positive or negative impact.
- **Self-discipline** to avoid temptation and lack of discipline.
  - Provide real-time alerts and controls, predictive balances and spending controls.

- Automate routine financial management and administrative tasks like sweeps and standing orders.

- Create cues and rewards to reinforce good habits like reaching a savings goal.

Research has shown that people will stick with physically healthy habits if they feel energized and confident about managing their health, and won't if they don't. Similarly, it's likely that promoting financially healthy habits also requires helping customers to feel energized and confident about managing their finances.

Empowering exchange

While digitalization and regulatory changes are disrupting the payments process in numerous ways, financial health is better served by focusing on where the provider can address barriers to greater economic exchange. But exchange in the real world is limited by the extent of trust—trust in the process, trust between the counterparties, and trust in the product or service. The provider can empower exchange to extend trust and protection to the customer in the following ways:

- Social messaging-integrated payments enable customers to combine everyday peer-to-peer payments (bill splitting, gift collections, group kitties) with the messaging between friends that makes such exchanges feel natural, friendly and dependable.

- Buyers' assurance expands e-commerce protection to include try-before-you-buy options and simple returns. Providers can offer lines of credit, extensive protections and easy returns to help buyers overcome the barrier of uncertainty about a product's quality, fit and delivery.

- Instant contracts build assurance into the sharing economy by combining digital identity with payment exchanges. Information about the third party is available to consumers, who can verify, for example, that the counterparty owns the service, is qualified and is well-regarded.

- Protection reimagined applies again in this context. By building assurance into the purchase of services or experiences, the provider protects the consumer from cancellations or delays, as well as from accidents and other misfortunes.

Facilitating financial accumulation and decumulation over time

The wealth management industry prioritizes asset allocation—conserving and growing pools of wealth—over the more everyday challenges of accumulating and decumulating wealth over a lifetime. This focus on managing wealth creates some blind spots for the sector. First, mortgages and home ownership aren't viewed as a core part of wealth management, even though they're the most disciplined form of accumulation we observe. Second, the reason mortgages are so effective as a *savings* product—the endowment effect of getting the house when you start the mortgage, not when you complete the payoffs—has never been mirrored in pension arrangements or other long-term asset-building products.

Other long-term savings, such as pensions, are more difficult to treat as a form of wealth accumulation. Therefore, a solution might be to create mortgaged pensions, where a 30-year-old customer purchases a $1 million pension that he or she pays off for 35 years until reaching age 65.

Also, houses, like pensions and life insurance, seem better suited to a time of a single-career, single-household lifestyle with little change. However, most people today will:

- Experience major career changes and probably periods of reduced or fluctuating income over their working lives;
- Live and work longer, and the distinction between working and retirement periods will blur;
- Experience changes in their family circumstances, such as separation or divorce, and dividing or reorganizing assets into new households over their lifetime; and
- For young adults, need a new approach to home ownership such as financial assistance from a family member or a state program.

Therefore, an important aspect of the financial-health provider's role is to reshape the wealth industry, to focus less on effective wealth management and more on effective accumulation and decumulation of wealth. This will address the challenges of indivisibility and illiquidity that make access to wealth unequal.

Having done that, the provider will be better positioned to rebuild financial advice (robo-advice, social group advice, automatic/semiautomatic investing) to help people address the obvious fact that some of what they earn needs to be available when they aren't earning.

Putting customers in control of their money, relationships and data

Financial-health providers also need to recognize their context in the wider transformation of peoples' digital lives, which involves three aspects:

- **Customer control center.** Enable customers to determine their banking services and the amount and type of information supplied to banks.
- **Digital identity.** Provide customers with a safe, reliable place to protect their digital identities online. Give them simple tools to grant and revoke access to their secure personal data to support their everyday lives, such as travel, making claims and proving credentials.
- **Rewards wizard.** Create more flexible, portable rewards—how they're earned and redeemed—for customers.

While banks already attempt to assist their customers to be financially healthy, the current state of banking remains superficial at best. Rather, banks should reconsider their role and how they can better assist all customers, regardless of income level, to improve their financial health. They need to shift the focus away from their own profits and more toward promoting healthy financial habits of their customers.

This plan centers on four themes: managing daily finances; empowering exchanges based on trust and engagement; managing financial accumulation and decumulation of assets; and putting customers in control their money, relationships and data. It can serve as a map for success for both banks and their customers.

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