

SUSTAINABILITY OF THE BUSINESS MODEL. RISKS AND OPPORTUNITIES OF FINANCIAL DIGITALISATION

The financial sector is undergoing a process of change that may affect banks' business model. Historically, institutions have faced structural difficulties, such as excess installed capacity and cost inefficiencies. On top of this there are other more recent challenges, such as digital transformation or sustainable finance. All of this in a highly competitive environment.

Institutions can adopt different strategies to tackle this new environment; however, in any case, they will need to adapt their processes and distribution channels to the new digital environment and changing customer preferences. Digitalisation, as it became clear during the pandemic, is no longer an option for institutions, but a necessity, and banks that lag behind in this area may find their medium-term viability compromised.

Investment in digitisation can offer institutions new opportunities and avenues for income growth, and serve as a driver to improve their efficiency. It will also allow them to keep pace with technological innovations applied to the financial sector, and thus be able to compete with other players, such as FinTech or large technology companies, where innovation makes a competitive difference.

However, there are also very significant risks and transition costs in the digital transformation process that banks will need to take into account when making their decisions. Also, institutions will need to analyse how these changes affect their customer segments, their business model and their risk management. Among other challenges, institutions need to step up controls to prevent and detect digital fraud, manage the risks associated with the increased volatility of deposits collected through non-traditional channels, adapt know-your-customer

procedures to the new environment, and strengthen the granting and monitoring of risks taken through digital channels, where there is limited interaction with the institution's interlocutors. In parallel, institutions should have solutions adapted to customers who are not fluent in the digital environment.

The banking supervisor is not oblivious to these changes and is stepping up its efforts to be on a par with the initiatives that institutions are adopting and to encourage them to make appropriate decisions in this strategic area. Supervisors need to assess the robustness, profitability and long-term sustainability of institutions' digitisation strategies to ensure that they have the appropriate mechanisms in place (e.g. governance, resources, capabilities, risk management, etc.), but without interfering with management.

To this end, in 2022 a series of surveys were conducted at institutions on their digitalisation strategies and a peer comparison was carried out. Specific monitoring and on-site inspections were also conducted.

In short, banks need to deal decisively and effectively with the profound structural changes that the sector is undergoing. There is a lot of work to be done, with certain matters to be addressed in the short term (e.g. cost rationalisation) and others in the medium term (such as digital strategy). In any case, institutions need to make the necessary assessment of opportunities and risks in order to undertake a sound digital transformation and have the appropriate mechanisms and instruments in place to make their business models sustainable in the long term. The supervisor, in turn, will need to monitor this process closely and, therefore, digital transformation is a supervisory priority in the coming years.

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