Small Banks, Big Opportunities

How small banks can optimally leverage the potential of data analytics

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The Reserve Bank of India (RBI), during the reign of Raghuram Rajan, granted 10 entities in-principle licenses to open small finance banks towards the end of 2nd quarter, 2015 - another move towards expanding access to financial services in rural and semi-urban areas. Eight out of the 10 entities are microfinance institutions.

For microfinance firms, which give mini loans to low-income earners, the key incentive for converting into small finance banks will be to gain access to deposits. They will also be able to offer a wider range of financial products to customers.

Small banks serve as the backbone of the banking system in India, helping small and mid-sized businesses across the country to grow and invest. The mandate given by RBI to small banks is to serve the unserved and underserved.

"India is over-banked but under-served" - Vishwavir Ahuja, CEO and MD, RBL Bank

Numerous challenges will be faced by small finance banks in coming years but with these additional challenges come additional opportunities.

1. Regulatory load- While small banks find it difficult to keep up with the plethora of regulatory acts and agencies all passed in the past, they have an advantage of being agile and flexible over their competitors

2. More capital- The most significant regulatory change is the increased demand for capital in banking operations. However, small banks are more responsive to customer needs and offer more personalized service to their customers. Building on these existing practices small banks would certainly have an edge over competition. Small banks can make customers understand that some of the increased costs are directly related to the financial safety of their businesses

3. Technology platforms- Challenges such as mobile banking, cloud computing etc. present a spectrum of confusing and hard budget choices. To tackle these, costs can be lowered through subscription based services

4. Competition- Small banks aren't just competing with their peers, but with MFIs and other NBFCs as well. Starting a dependable long-term relationship with customers will ensure more loyalty and stickiness.

"After setting up a bank, it would take nearly two years to merely stabilize the operation" - Samit Ghosh, Founder and MD, Ujjivan Financial Services

"The bigger banks have strength but the last mile connectivity is not the focus, and given our strengths, we find that they are very complementary" - Rajeev Yadav, group CEO, Fincare Business Services

The Banking industry is a fast growing and highly competitive sector in India. According to KPMG-CII report, the banking industry in India has the potential to become third largest by 2025. To stay relevant in the face of increased competition, banks in India are taking the data analytics route to attract new customers, retain them, find opportunities to upsell and cross-sell and minimize losses.

One of the first instances of the use of analytics can be traced back to the early 2000s when a mainstream bank put in place a data warehouse and started investing in technology that would help it make sense of the massive troves of unstructured data captured by its information technology (IT) systems. Now by using data analytics they have managed to reduce their NPAs by 50% over the period of five years.

"The most successful banks are the ones that have embraced and leveraged technology better than the rest" – Bhavish Sood, Research Director, Gartner India

Following are the Instances where analytics can provide an edge over competition:

1. Customer Intelligence- With analytics in place, bank can track every aspect of a typical customer's behavior by:
    - increasing customer loyalty and reducing loan prepayments due to refinancing with other institutions
    - tracking credit histories of customers to disburse loans accordingly
    - generating insights into personal habits of its customers, allowing them to promote offers in a targeted manner
    - segmenting customers based on their behavior to identify their needs in order to develop tailored products and services

2. Risk management and fraud detection- Maximum compliance with regulatory norms will be required right from the moment of bank's inception. Hence it is important for banks to put in place robust processes and analytical platforms for managing risk and containing frauds. These mechanisms only become more efficient over time through their self-learning algorithms. Using predictive analytics, early warning signals can be generated to curb frauds throughout the organization:
    - Based on customer's financial habits and journey with the bank, predictive analytics can bucket defaulters into high, medium and low risk assets
    - Predictive models can be used to allocate defaulters to the

most appropriate collection channel, for example high risk defaulters require a personal visit or a legal action rather than an email or a phone call

- Predictive models can be applied to education loans, automotive loans, housing loans, SME loans etc. to reduce the defaulter percentage

3. Business Intelligence- With the use of data analytics banks can tackle the issue of inaccurate reports being distributed in the organization. Banks can create a common data repository which will help end users get accurate and timely reports and in turn improve efficiency. Reports can be fetched real time and from anywhere at the comfort of the end user

Further, analytics act as an enabler for business to understand and take strategic decisions on complex business scenarios including geographic expansion, channel efficiency measurement, and resource allocation.

"We decided to take a non-traditional approach by building our (analytics) solution on an open source platform" - Sanjay Sharma, head of technology, innovation and customer fulfilment, RBL Bank

The established national lenders are going to improve on their existing capabilities to stay ahead in this competitive scenario. Considering this, small banks, given their strategic goals, must carve out a niche and identify a means to constantly attract prospects and sustainably service their existing customers with highly personalized engagement. This will require small banks to embark on their analytics journey with a better focus on analytical and technological front as compared to traditional banks. Present day customers have multiple choices but at the same time value relevant, personalized and timely interventions.

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