Digital Transformation Program for Rural Banks

INTRODUCTION

In this age of digital revolution, institutions providing financial services should be able to cope up with the changing landscape and requirements to provide digital financial services not only to their customers but to their communities where they serve. This supports the financial inclusion initiatives of the government where digital technology provides a convenient and easy way for the unbanked and underserved market to avail of financial services and make cashless payments part of the bigger eco system.

There is an **apparent and immediate need for a digital transformation** for these financial services providers, in particular, the rural banks.

We have seen a change in consumer behavior in the way they do their payments and transfer transactions with the use of E-Wallets such as GCash and Pay Maya and mobile banking platforms that are available 24/7.

Financial technology providers (or Fintech) have been offering digital financial services for cashless payments and remittances. The bigger banks and even new players in the financial sector such as CIMB and Tonik Bank have their own digital banking platforms to target the unbanked and underserved market by onboarding new customers, accepting new deposit accounts and even loan applications.

These players are targeting the unbanked market in the countryside, which is also the market segment of the rural banks.

Going digital will support government's initiative to move towards digital payments and promote bank account opening for the unbanked and underserved market.

Digital Transformation is a process of using technologies that can adopt quickly to changing consumer behavior, business atmosphere and requirements, and brings about a new digital experience for customers that requires changes in the bank's current practices, policies and procedures and in the way banks do business.

The **benefits of Digital Transformation** to the rural banks are:

- ✓ Better customer experience of doing banking transactions anywhere, anytime using preferred channels and devices, with the creation of digital products and services currently not known or made available to existing customers;

- ✓ Empowers employees to work outside the bank premises and do more with productivity tools to market the bank's products and services to the unbanked and underserved market and eliminate tedious manual processes in customer onboarding and loans application processing; and

- ✓ Business Process improvements that:

    - greatly reduces, if not totally eliminate manual intervention and sources of errors,
    - allows digitization of the bank's customer records as mandated in BSP Circular 1002 issued in 2019,
    - facilitates faster turnaround time in processing customer transactions, generation of regulatory requirements, among others,
    - allows bank personnel to focus in doing its core business in generating more deposits and increase loans portfolio, and
    - provides automated controls that reduces associated IT risks;

- ✓ Be able to allow the banks to participate in wider eco-systems through partnership and collaboration that will expand their reach and provides customers additional services other than the traditional deposits and loans products such as bills payments, supplier payments, remittances, bank transfers, disbursing payments to government beneficiaries of financial assistance programs, payment of taxes, among others.

This document provides a guide in planning and implementing a rural bank's digital transformation program and to continue to have the competitive edge in their respective areas of operations where trust plays a major part in choosing a partner to provide for their banking needs.

Digital Transformation Program for Rural Banks

DIGITAL TRANSFORMATION ROADMAP

A. Define the Vision

In developing the roadmap, it is important that the rural banking industry share a common vision that optimizes the use of the industry's over 400 rural banks and a network of over 3,200 branches and offices nationwide.

Rural banks, being in the forefront in areas where other financial institutions are not available or where people feel comfortable and at ease in dealing with trusted institutions in their communities, should act as the primary provider of banking products and services that is more than just the traditional deposits and loans products they currently offer.

This can only be achieved by collaboration and partnership with financial technology providers (or Fintech), who can provide the technology to be used by the rural banks in providing new products and services, such as payments, transfers, remittances, among others, to make them **become a 'One Stop Shop' provider of financial service**s in their respective rural areas.

It is envisioned that:

Rural Banks are interconnected in a secured digital network of interoperable systems and partner solutions that expand the reach of banks to serve the unbanked and underserved market and allows its customers to do banking anywhere, anytime using their preferred platforms and channels.

By making use of an Open Application Programming Interface (API) digital platform, this allows rural banks to connect to this common digital platform with Fintech providers such as payment aggregators, remittance companies, E-Wallet providers as well as government institutions, to be able provide more services to its customers at their convenience.

Advantages of having a common platform for the rural banks are:

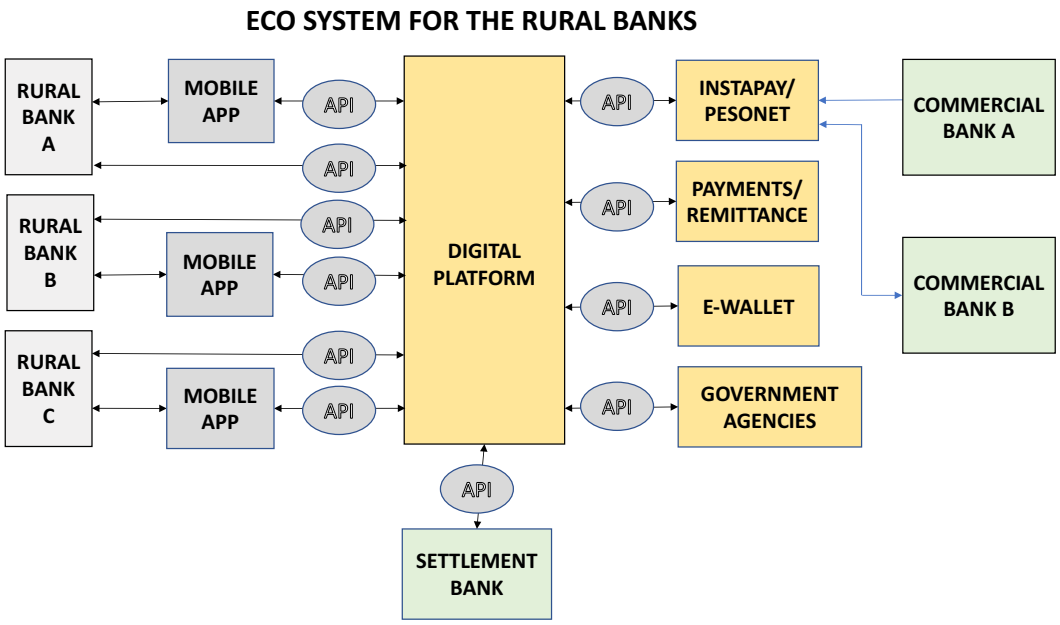
- ✓ Banks need not individually negotiate with Fintech providers when they need such services available with the provider;

- ✓ Banks need only to provide its API for its core banking and mobile banking applications and will be able to avail of the services made available by the Fintech provider that is connected to the platform. Otherwise, each Fintech provider will have to connect individually to the bank's core banking and mobile banking applications which is more difficult and longer time to implement; and

- ✓ Use of APIs will fast track implementation of new products and services of the Fintech provider

Figure 1 below shows the envisioned target eco system.

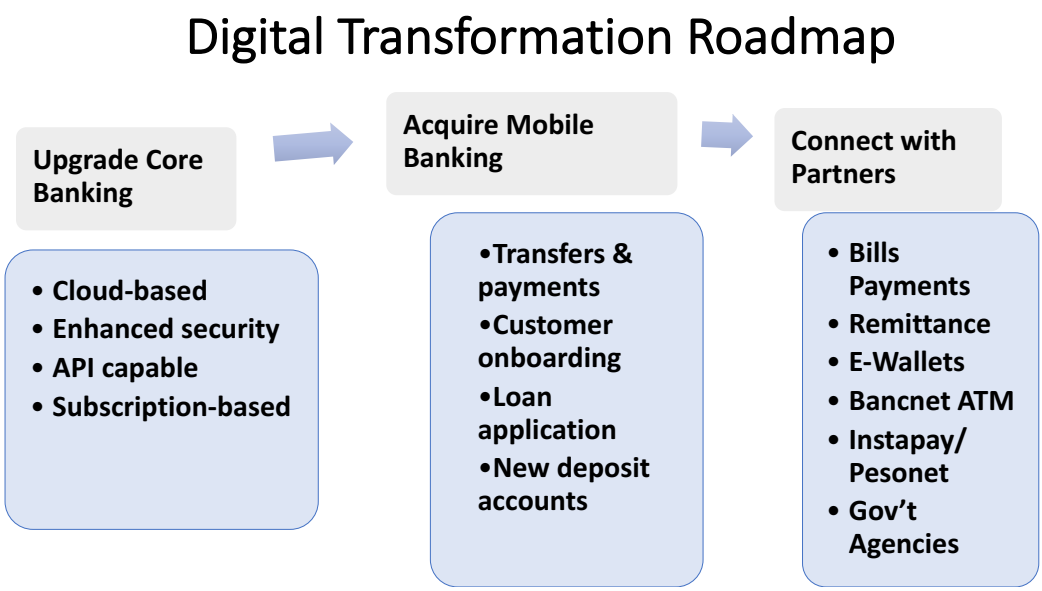
Figure 1: Target Eco System For The Rural Banks



B. Steps to Achieve the Vision

Figure 2 shows a visual digital transformation roadmap that the RBAP and the individual rural banks can adopt to achieve its vision. This transformation also hopes to achieve 'quick hits' and provide immediate benefits to the rural banks in the process in following the roadmap.

Figure 2: Digital Transformation Roadmap



Cloud-based Solutions

Key considerations on the technology infrastructure required for digital transformation are that it be highly reliable, available, resilient, scalable and secure to meet customer needs and demands. A cloud-based implementation is able to provide for all these.

Cloud-based implementation offers a cost-effective way to digital transformation as this is a subscription-based solution. This means that you pay only a monthly fee based on the capacity requirements of the system that you will host in the cloud at a particular moment in time. This is unlike traditional practice where you acquire the hardware that is normally over capacity in terms of CPU, memory and hard disk utilization as this already provides for future projections.

Cloud-based solutions are highly reliable and available as they operate in a multi-location environment. This means that the systems that run on a cloud can be located in different physical locations of your choice, thus providing redundancy in the environment you need to run your IT operations. They are resilient as they can easily be reconfigured to adjust to surges in uses or sudden increases in demand in processing power or storage requirements.

Advances in technology, both in hardware and system software are also normally factored in so that users of cloud infrastructure need not worry on the upgrades to these as well.

Cloud-based solutions also already provide the security components to protect the technology infrastructure and have the capability and expertise to monitor and immediately address any security violations or breaches. This is an expensive component for banks if their infrastructure is based in house or in bank premises as they need to invest in hardware and software as well as provide for experienced personnel to handle all these to provide a secure environment for the bank's infrastructure.

The benefits of a cloud-based implementation are:

- ✓ Eliminates building of and maintaining IT facilities, infrastructure and security and can address business continuity plan requirements;
- ✓ Eliminates the need to hire personnel resources to maintain these facilities;
- ✓ Provides high availability and reliability for customers using electronic banking technologies since these are housed in an environment that is highly available, reliable, secure and resilient to changes and surges in business requirements;
- ✓ Makes electronic banking services available at all times as these are not affected by calamities in the area where rural banks are located; and
- ✓ Employees able to work remotely even during lockdowns, calamities or given restricted access to branches and offices.
- ✓ Problems on vendor support to production problems will be addressed as problems can now be addressed and resolved remotely

A cloud-based implementation is recommended for rural banks that plan to offer electronic banking products and services to its customers that requires high availability, reliability and security, which are all part of a cloud-based implementation.

Upgrade Core Banking

Given that a Core Banking System enables the bank's primary business of deposits and loans, the system should be able to connect to digital banking platforms such as mobile banking for individual customers, internet banking for SMEs and corporate customers, and agent banking solutions for bank employees and its agent partners, among others and allows the bank to introduce new electronic banking products and services.

Rural banks that are currently using legacy core banking systems, will find it hard and/or expensive to connect their legacy applications to other solution providers that allows the banks to introduce new services such as bills payments, remittances, fund transfers to accounts in other banks, and the like.

Acquire Mobile, Internet and/or Agent Banking

The next logical step for rural banks that have upgraded their core banking systems is to acquire mobile banking solutions.

Depending on their priorities, the banks can start with any of the following mobile banking applications:

- ✓ Mobile Banking for individual customers,
- ✓ Mobile/Agent Banking for employees and agents, or
- ✓ Internet Banking for SMEs and corporate clients.

For mobile banking for individual customers as well as for internet banking for SMEs and corporate clients, minimum initial features should include payments and transfers. These can be for loan payments with the bank, bills payments, load or top-up for mobile phone, transfer to own account in the same bank, transfer to third party accounts in the same bank and transfer to another account in another bank.

For SMEs and corporate clients, this should allow them to manage their accounts, and know their cash position anytime, pay their suppliers and their employees.

For mobile/agent banking, this can be utilized for customer onboarding, acquiring new deposit accounts, receive loan applications, accept loan and bills payments and the like by engaging with agent partners or having their employees go to the market directly to solicit new accounts and new customers.

Building the Eco System

To maximize the benefits of digital transformation, especially for small rural banks, it is imperative to build an eco system for the industry which can attract more customers, specifically the unbanked and underserved market, and provide expanded services to its customers, which are currently available of from existing financial technology providers such as E-Wallet providers, remittance operators, new digital banks, among others.

E-Wallet providers such as GCash and Pay Maya have started penetrating the unbanked and underserved market and the use of these payment platforms have grown by leaps and bounds because of this pandemic which started in March 2020. They can be easily availed of not just by the unbanked and underserved market but also by rural bank customers. An easy download of the mobile application and they can start using this to transfer money to another person or pay their bills without going out of their homes.

Similarly, the unbanked and underserved market use existing remittance operators to transfer money to their relatives in the provinces.

By partnering with these financial technology providers, the bank can act as agents for these E-Wallet providers, bills payments aggregators and remittance operators. Bank customers and even non-bank customers can avail of these services in the bank branches. Banks should take this as an opportunity to engage non-bank customers and be able to offer them bank products.

In addition, by offering these services, the banks generate additional revenues through transaction fees that are levied for these types of transactions.

While people still have to go to the branch to avail of the additional services, this is a quick and good first step without connecting the core banking systems of rural banks with the systems of their partners nor is there an immediate need to upgrade their core banking systems.

Establishing partnerships with government agencies will facilitate tax payments to the Bureau of Internal Revenue (BIR), remitting of contributions to Social Security System (SSS), Pag-ibig Fund and Phil-Health, receive pensions and loan releases from government, among others.

Figure 3 below provides a partial list of financial transaction services to different types of entities that provide for convenient transaction processing.

Figure 3: Transaction Matrix

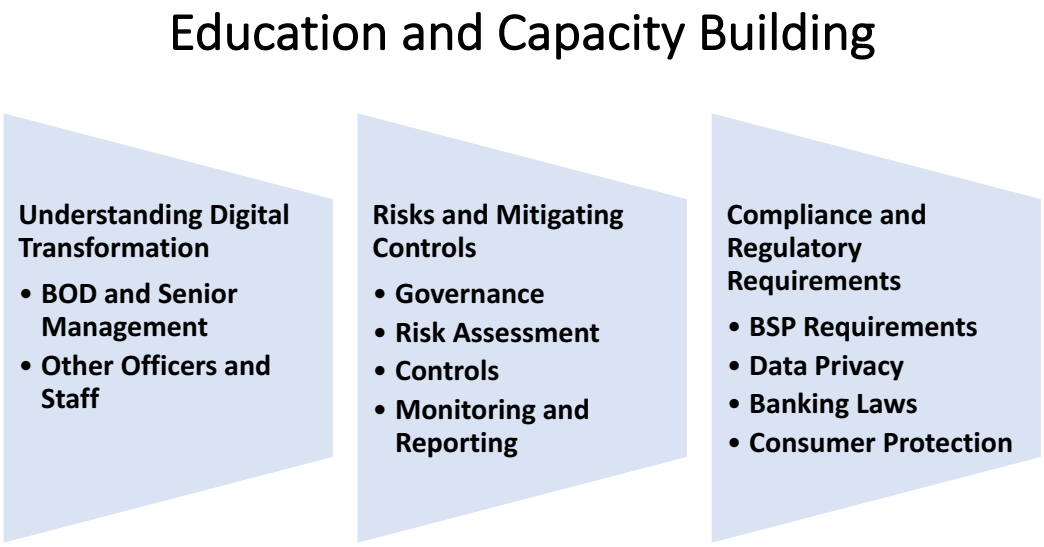
TRANSACTION MATRIX

			FROM	
		PERSON	BUSINESS	GOVT
TO	PERSON	✓ Account to Account Transfer (Same Bank) ✓ Account to Account Transfer (Different Banks) ✓ Account to eWallet ✓ eWallet to Account	✓ Salary Credit ✓ Loan Disbursement ✓ Remittance	✓ Salary Credit ✓ Loan Disbursement ✓ Pension Credit ✓ Cash Grant to the Marginalized
	BSNESS	✓ Loan Payment ✓ Bills Payment ✓ Merchant Payment ✓ Payment to Private Transport	✓ Supplier Payment ✓ Bills Payment ✓ Loan Disbursement ✓ Loan Payment	✓ Supplier Payment
	GOVT	✓ BIR & LGU Tax Payment ✓ Voluntary Contribution to SSS, PhilHealth, Pag-ibig ✓ Loan Payment ✓ Payment to Public Transport	✓ BIR & LGU Tax Payment ✓ Remittance to SSS, PhilHealth, Pag-ibig	

C. Education and Capacity Building

Figure 4 provides a minimum list of capacity building workshops/webinars that rural banks have to undergo during the transformation roadmap. Additional workshops may be added to supplement the current list during this process.

Figure 4: Education and Capacity Building



Part of the process in digital transformation should be educating the stakeholders and senior management as well as building capacity to the banks officers and staff to support the digital transformation initiative.

A primary objective of this Education and Capacity Building program is to **obtain the buy-in of the different rural bank's Board of Directors and Senior Management to go into digital banking** and help bring about a mindset change in the bank.

Secondary objective is understanding **what this digital transformation will do for the rural bank, in particular, the industry, in general and more importantly, what this brings to its customers**. The risks associated with this initiative should likewise be made clear so that appropriate governance structure, policies and programs be developed to mitigate, if not totally eliminate the risks.

Third objective is for the **banks to be able to comply with the BSP regulations** (Manual of Regulations for Banks [MORB]) and circulars such as 808 (Guidelines on Information Technology Risk Management), 899 (Amendments to Guidelines on Outsourcing in MORB), and 1033 (Amendments to Regulations on Electronic Banking Services in MORB), among others, the pertinent banking laws, data privacy act and consumer protection law.

D. Implementation Timeline

Figure 4 provides a three (3) year implementation timeline for RBAP and the industry to achieve its vision. While not all rural banks are expected to be able to participate within the timeline indicated, the digital infrastructure to achieve this vision will be in place within the three (3) year timeline to support any future RBAP or industry initiatives.

Figure 4: Implementation Timeline