TEMENOS
Value Benchmark

Temenos Value Benchmark

The case for digital transformation in Latin America

Contents

Executive summary

Despite geopolitical uncertainty and deteriorating macro-economic conditions, the Latin American banking industry has continued to perform. Banks have grown and remained profitable despite the rise of fintechs, largely due to their high interest rate-based business models. However, the sector has yet to embrace customer-centric digital transformation, to both improve the customer experience for the banked and to extend their reach into the large unbanked market. The inaugural Temenos Value Benchmark results reveals that Latin American banks lag global peers in their levels of front-to-back digitization across the bank, and particularly in the front office. However, they are at par in terms of operational efficiency in the back office and their risk and compliance functions. Latin American banks could benefit from increased investment in digital front office and channel capabilities, in order to create customer-centric engagement models along with greater innovation and personalization of products and services to reap the market opportunity.

Industry performance

Latin American banks have performed well with revenue growth of 11.7% over the past 5 years (2012 – 2017) against the rest of the world at 4.9%, despite lower GDP growth averaging at 1.9% versus 3.1% in the rest of the world[1]. This success can be attributed to more aggressive interest rates (19.9% vs. 8.9%), as a well as keeping a clean loan portfolio with a non-performing loan rate of 1.7% vs. 3.4% globally. This is consistent with high-risk lending models in emerging markets such as Africa with interest rates at 14.3%[2].

The market opportunity –

going digital to both better serve the banked and to reach the unbanked

The digital economy will represent over half of Latin America's GDP by 2022 with 70% of investment focused on disruptive technologies such as mobility, cloud, big data, and social media[3].

Meanwhile, 46% of the population still does not have a bank account in Latin America. In 2017, 22% of respondents in Latin American markets[4] attributed their lack of access to a bank account to the fact that the closest branch was too far away from where they lived. By relying on mobile access as opposed to branches, banks could provide access to markets where most people still live in rural areas. Fintechs such as Destacame, Clip, and Tienda pago have already started capitalizing on this[5].

In Latin America, wide access to digital technology could enable rapid growth in the use of financial services. Smart phone adoption is projected to rise from 62% in 2017 to 78% by 2025[6]. Since 2014, the share of adults making or receiving digital payments has risen by 8% in economies such as Bolivia, Brazil, Colombia, Haiti, and Peru. By digitizing cash wage payments, businesses could expand account ownership to up to 30 million unbanked adults[7].

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[1] Lessons from leaders in Latin America's retail banking market – McKinsey and Company

[2] Temenos Value Benchmark: Net interest margin and non-performing loans for Latin American banks vs. the rest of the world

[3] https://www.zdnet.com/article/digital-economy-will-represent-over-half-of-latin-americas-gdp-by-2022/

[4] Findex 2017

[5] https://latam.tech/five-companies-for-unbanked/2018/

[6] GSMAintelligence: The mobile economy Latin America and the Caribbean 2018

[7] Findex 2017, Worldbank.org

Temenos Value Benchmark

Launched in late 2018, the Temenos Value Benchmark is a strategic survey-based program to discuss business performance and value creation enabled by the bank's investment in IT, structured around business and IT metrics and qualitative best practices. Leveraging data from banks selected from Temenos' extensive customer database comprising retail, corporate and universal banks from across the globe, the initiative has allowed identification of global and regional market trends as well as tangible performance drivers that distinguish the best performing banks from the average performers.

> “It was of great value to participate in the Temenos Value Benchmark program and receive performance metrics from banks more mature and larger than us, operating in larger markets. This allowed us to set performance measures that will help us achieve better returns on our IT investment by adopting the best practices in our industry. It also challenged us and offered us new perspectives, which will ultimately benefit our bank.”
>
> – Hector Ovidio Montoya Tobar, CIO, Banco Azul, El Salvador

BancoAzul
de El Salvador

> “Our impression of the Temenos Value Benchmark is that it has been very well received by all management and operational levels of the bank, including IT. Our expectation is that it will allow us to access market best practices on functionalities associated with Transact and Temenos. The Temenos Value Benchmark has given us a better overview of the bank's condition and provided opportunities for improvement.”
>
> – Ivannia Alfaro Rojas, MBA, IT director, Banco Popular de Costa Rica, Costa Rica

Banco Popular

Bridging the digital transformation gap - Latin America vs the Rest of the World

The Temenos Value Benchmark has revealed that **high performing banks (with low cost-income ratios) have higher levels of front-to-back digitization**. Digitization also enables banks to grow their customer base as well as to support more customers efficiently with fewer employees. The level of digitization was measured by the Temenos Digital Index, based on a weighted average of digital interactions (%), digitally active customers (%), straight through processing rates (%) in the front office (sales and relationship management functions), in operations as well as in payments and settlements.

Digital Index[8] vs Customer Growth vs Customers per FTE vs Cost-income Ratio (CIR)

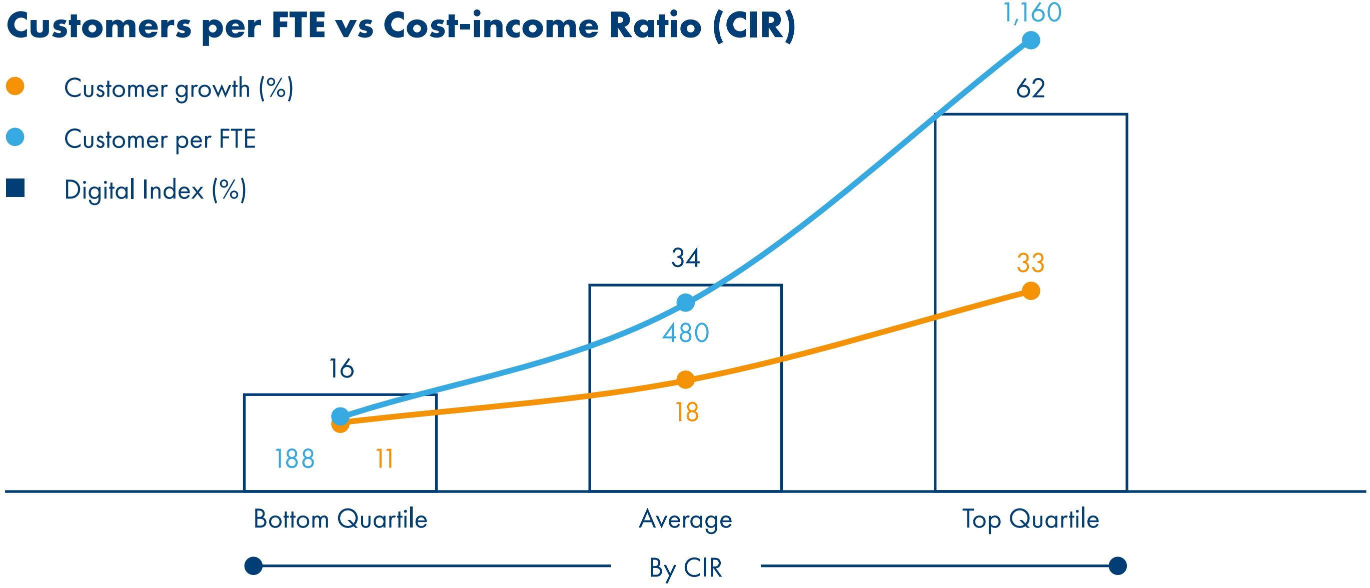

Figure 1: High performing banks have the highest levels of front-to-back digitization

Note: Retail only

However, Latin American banks have a digital index of only 19.8% compared to the benchmark average for the rest of the world at 31.8%. They also have 2.1x lower customer growth rates and 4.8x lower customers per FTE. This is consistent with the 17% higher cost-income ratios in Latin America compared to the rest of the world.

Digital Index[8] vs Customer Growth vs Customers per FTE

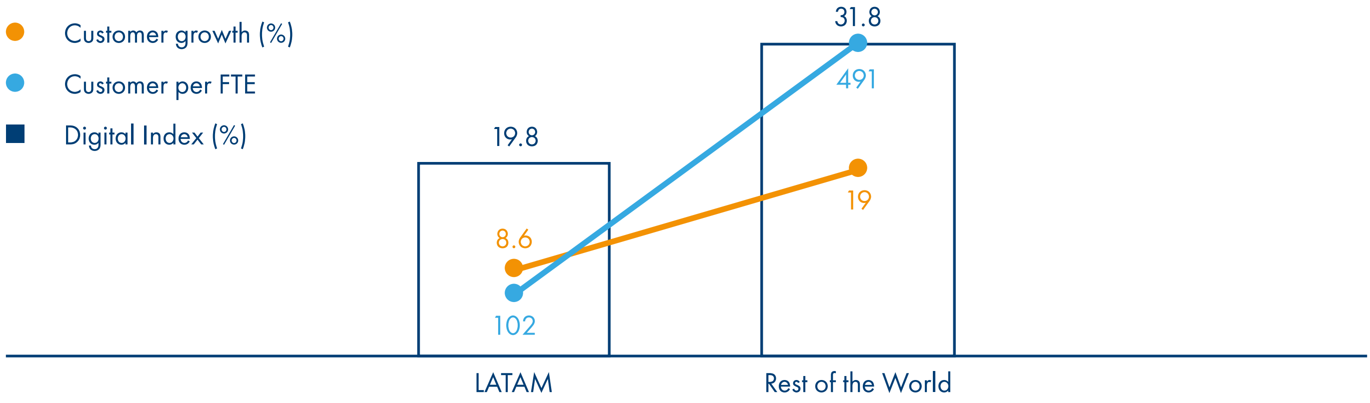

Figure 2: Latin American banks lag global peers in front-to-back digitization

Note: Retail only

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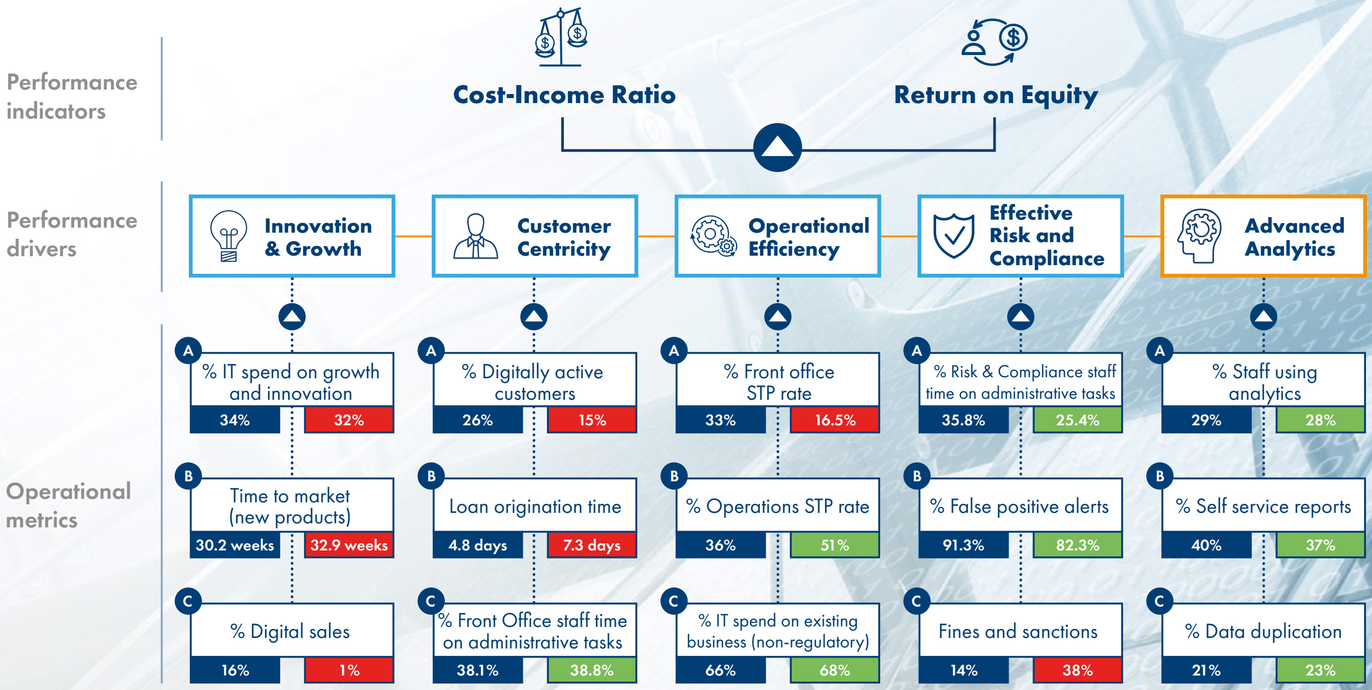
[8] 1. Digital Index: 25% x digital interactions (%) + 20% x digitally active customers (%) + 20% x Front Office straight-through processing rate (%) + 20% x Operations straight-through processing rate (%) + 15% x Payments straight-through processing rate (%)

What can Latin American banks do to improve performance?

The Temenos Value Benchmark has provided us with a unique opportunity to identify the factors which make high performing banks different i.e. those with better cost-income ratios and returns on equity, and what characteristics they share. We have revealed 15 key operational drivers that correlate directly with the financial performance indicators (cost income ratio and/or return on equity) that banks must focus on in order to improve their financial performance.

Drivers of Banking performance



Performance drivers		Operational metrics	Rest of the world	LATIN AMERICA
Innovation & Growth	A	% IT spend on growth and innovation	34%	🟥 32%
	B	Time to market (new products)	30.2 weeks	🟥 32.9 weeks
	C	% Digital sales	16%	🟥 1%
Customer Centricity	A	% Digitally active customers	26%	🟥 15%
	B	Loan origination time	4.8 days	🟥 7.3 days
	C	% Front Office staff time on administrative tasks	38.1%	🟩 38.8%
Operational Efficiency	A	% Front office STP rate	33%	🟥 16.5%
	B	% Operations STP rate	36%	🟩 51%
	C	% IT spend on existing business (non-regulatory)	66%	🟩 68%
Effective Risk and Compliance	A	% Risk & Compliance staff time on administrative tasks	35.8%	🟩 25.4%
	B	% False positive alerts	91.3%	🟩 82.3%
	C	Fines and sanctions	14%	🟥 38%
Advanced Analytics	A	% Staff using analytics	29%	🟩 28%
	B	% Self service reports	40%	🟩 37%
	C	% Data duplication	21%	🟩 23%

▇ Rest of the world
🟩 Close to or better than rest of the world
🟥 Significantly worse than rest of the world
LATIN AMERICA

Note: All listed operational metrics correlate with one or more performance indicators.

Innovation and growth

The benchmark has confirmed that banks focused on innovation and growth have better financial performance and achieve higher growth. Though Latin American banks have been consistent with the rest of the world on their IT investment on growth and innovation, this has not translated into lower times to market or higher digital sales.

Latin American banks have been bogged down by regulatory restrictions whereas regulators in the rest of the world are actively encouraging innovation and competition. Therefore, the rest of the world is continuing to innovate by launching more sophisticated personalized and innovative products. Latin American banks rated their ability to offer customer-centric, innovative, feature-rich products on the basis of integrated product building frameworks with re-usable components, 40% lower than the rest of their peers around the world. The rest of the world has also been involved in launching more new products annually with an average of 10.3 compared to 2.4 for Latin America.

Customer centricity

High performing banks engage digitally with more of their customers, originate products faster and their front office staff are more productive and focused on providing value to their customers.

Lack of investment in front office digital capabilities by Latin America has resulted in a lower percentage of digitally active customers. Another indicator of low digital engagement is the higher loan origination time in Latin American banks, which is 50.5% higher than the rest of the world.

Operational efficiency

Higher performing banks have higher levels of automation driven by straight through processing (STP) both, in the front office and the back office and the ability to support more customers with fewer staff. They also spend less of their IT budget on keeping-the-lights-on non-regulatory maintenance.

Latin American banks had 14.6% higher operational STP rates than the rest of the world. This means they have been able to streamline and automate a higher proportion of their operations. However, in the front office, lower STP rates (16.5% lower than the rest of the world) have created a strain on the salesforce, creating more pressure on managing clients face-to-face. Latin American banks have successfully created their back office foundation but have so far not transitioned towards a more digital and automated front office, resulting in lower customers per FTE (102 vs. 491 for the rest of the world – as illustrated in figure 2).

Risk and compliance

Higher performing banks have more efficient and effective risk and compliance functions with higher staff productivity i.e. staff with lower time spent on administrative tasks and more efficient operations i.e. lower false positive alerts. They also successfully avoid fines and sanctions.

Despite more complex and everchanging regulatory pressures, risk and compliance staff in Latin American banks spent 10.4% less time on administrative tasks compared to the rest of the world. They have also had a 9.0% lower false positive rates than the rest of the world. However, a higher proportion of banks in Latin America (24% compared to the rest of the world) have incurred fines and sanctions compared to banks in the rest of the world.

Advanced analytics

Widespread and effective use of advanced analytics built on a strong data foundation across the enterprise is also a key characteristic of high performing banks. Higher performing banks use analytics more widely and more effectively across the entire organization with better user enablement in terms of higher proportion of self-service reports and a greater proportion of business users utilizing analytics. They also have a stronger data foundation in terms of lower data duplication across their systems.

A couple of Latin American banks have been virtually in line with the rest of the world in analytics, characterized by slightly lower percentage of self-service reports, lower percentage of users utilizing analytics, and more data duplication, all within a couple percentage points. Continuing to improve the analytics function by empowering users to have better access to data will give them a competitive edge in today's digital and open banking world.

Latin American banks have made great strides towards building a strong back office foundation. They are now in a position to invest in front office and digital engagement capabilities. They should embark on digitally transforming themselves by building highly modular and configurable digital engagement platforms to engage digitally with more customers, improve their front office straight-through processing rates and enable more sales and origination digitally. A strong omni-channel customer experience with seamless onboarding and full process transparency will reduce origination times. Automation of repetitive tasks for the salesforce will allow them to focus even more on customer-facing activities leading to higher customer satisfaction and by implication, higher cross-sell and retention, thereby increasing revenues. Improving their fraud detection capabilities by using commercially consolidated watchlists and third-party benchmarks as well as the use of emerging AI will help them improve risk and compliance and reduce the possibility of fines and sanctions.

Conclusion

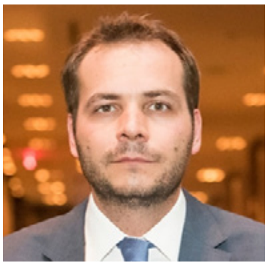
The Temenos Value Benchmark reveals that by embarking on digital transformation and by tightening risk and compliance best practices, Latin American banks can positively improve their financial performance (cost-income ratio and return on equity). Focusing investment on a more digitally-oriented customer engagement model will allow Latin American banks to exploit market opportunities, both, in terms of better leveraging their current customer base and also in pursuing the unbanked market quickly and cost-effectively.

Authors

Kanika Hope

Global Strategic
Advisory Director,
Temenos

Kanika Hope is Global Strategic Advisory Director at Temenos, leading the Temenos Value Benchmark program and strategic advisory practice. Kanika has 25 years of experience in banking technology and operations. Prior to Temenos, she worked as Business Development Director at SAP for 10 years, where she engaged with European retail and corporate banks on core transformation, digital banking and more. Before that, she was a consultant at McKinsey & Company in their Business Technology Office, London focused on Banking, and at General Electric in a variety of global Information Technology roles.



Vincent Chamasrour

Strategic Advisor,
Latin America,
Temenos

Vincent Chamasrour is a Strategic Advisor at Temenos, leading the Temenos Value Benchmark program and strategic advisory practice in Latin America. Vincent has 12 years of experience in strategy and operational consulting in the financial services sector. Prior to Temenos, he worked in management consulting at Accenture and Deloitte Consulting for 10 years, where he engaged with Latin American banks on digital strategy, business operating model transformation, customer experience & customer journey mapping, and process reengineering.

About Temenos

Temenos AG (SIX: TEMN) is the world's leader in banking software. Over 3,000 banks across the globe, including 41 of the top 50 banks, rely on Temenos to process both the daily transactions and client interactions of more than 500 million banking customers. Temenos offers cloud-native, cloud-agnostic and AI-driven front office, core banking, payments and fund administration software enabling banks to deliver frictionless, omnichannel customer experiences and gain operational excellence.

Temenos software is proven to enable its top-performing clients to achieve cost-income ratios of 26.8% half the industry average and returns on equity of 29%, three times the industry average. These clients also invest 51% of their IT budget on growth and innovation versus maintenance, which is double the industry average, proving the banks' IT investment is adding tangible value to their business.

For more information please visit www.temenos.com.

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