ONLINE BANKING

Towards frictionless payments

Financial services companies must strike a balance between experience and security to meet consumers' expectations

Sally Whittle

Frictionless commerce has shifted from being a novel retail strategy to a core requirement in many sectors.

From retail to transport, food and travel, organisations are racing to strip time and complexity from the consumer journey to create seamless, convenient experiences.

It's a model that makes sense in the current landscape. According to PwC, 43% of consumers will pay more for a service that is convenient, while half will actively change retailers if a company offers a more frictionless experience. What does that mean for banking, financial services and insurance companies?

"Consumer expectations have changed in finance, driven by retail, commercial and ecommerce sectors. People expect to access almost everything online and without needing to jump through hoops," explains Jason Lane-Sellers, EMEA director, fraud and identity, at LexisNexis Risk Solutions.

The challenge is that finance isn't a sector that naturally lends itself to being a frictionless experience, adds Lane-Sellers. "If I'm accessing my bank or buying an insurance policy or checking my mortgage statement, those are serious transactions and they won't look the same as, for instance, buying a film on Apple TV."

In some cases, friction might be a requirement from industry regulators or designed to minimise fraud, adds Lane-Sellers. "If I want to make a large payment through my banking app, it might ask me to authenticate again or push a message through SMS. I might be trying to make a purchase online and the retailer asks me to authenticate the payment via my banking app. In many cases that extra validation is required by the regulators, but it adds to the process and customers find it frictional."

But while banks might not be able to emulate, for example, Amazon's one-click purchasing, there are other ways to reduce friction in the financial services sector, says Phil O'Neill, financial services director at consulting firm Kin and Carta. "Banks hold enormous amounts of data on customers. It's possible to use that data to power personalised experiences and suggest products before the customer even realises that they need them," he says.

For example, banks could pre-approve customers for certain products, provide 'embedded' services such as insurance, or make a timely recommendation for a service based on data that it already holds, says O'Neill. "This all reduces friction because it saves the consumer time, and that's probably more important for financial services than trying to emulate 'one-click' models.

"Gen Z are positive about frictionless experiences. But I suspect if you asked a gen-Z person who had been attacked by a fraudster how important it is in finance, you'd get a different answer," says O'Neill.

One firm that has taken steps to reduce customer friction is Legal & General, which has implemented several changes to its insurance and pension products. For example, L&G has created a range of dashboards and calculators to help customers understand complex financial products more easily. Recently, the firm has created personalised, animated video messages that are emailed to workplace-pension customers.

"The video explains how much their pension is predicted to be, what annuity they could buy, and a 'click here' option if they wish to increase their contributions," explains Bernie Hickman, chief executive, Legal & General Retail.

This small service reduces the friction typically involved in reviewing pension projections, as it makes it easy for customers to make a change. The video campaign generated engagement from almost 30% of recipients, which shows the appetite for frictionless services, says Hickman.

But consumers don't necessarily want zero friction from their financial services providers. Legal & General Retail has deliberately added 'pauses' into certain consumer journeys, to give customers time to consider what action they're taking. This is important when considering products such as pensions, which can have a long-term impact on the customer's financial wellbeing, says Hickman. "Yes, we want to make ourselves easy to do business with – but it's important that customers have every opportunity to provide honest and complete information when they're taking out a life insurance policy because they will depend on it," he says.

The goal for most financial service providers is to minimise the type of friction that makes customers frustrated and walk away, while adding just enough 'positive' friction to make them feel protected, comments Kate Frankish, chief business development officer at Pay.UK. "We have to balance the desire for things to be quick and easy with a massive increase in things like APP (authorised push payment) scams," she says. "The question is finding the right level of friction so that people get value but are protected."

A good example of positive friction is the introduction of 'confirmation of payee' in online banking. When consumers in the UK make a new bank transfer payment, the bank can check that the account name of the payee matches the account number and sort code. The system can identify a close match and suggest the correct details, or it can confirm that the details do not match and advise the customer not to proceed. Pay.UK's research shows that 70% of consumers felt positive about the introduction of this service, and the service has significantly reduced this type of fraud, says Frankish. "That's an important point of friction and it's slick, so people quickly got used to it," she says.

Sometimes, positive friction can mean not doing things as quickly as might be possible, adds Lane-Sellers. "Banks can identify customers in milliseconds using behavioural biometrics, and knowledge about your location and device, but they will often 'hold' customers for a second or two and suggest they are authenticating your details," he says. "That's an artificial pause to make you feel that you aren't getting access to your account too easily. That holding page gives you the feeling of security that you're being validated before you can access the app."

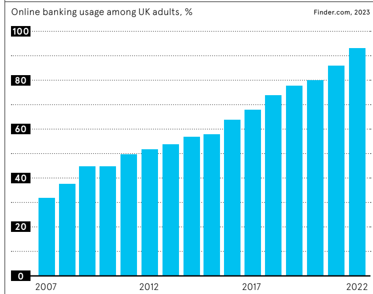
Getting the balance right between positive and negative friction isn't simple but it is critical. In today's marketplace, banks can't afford to ignore the customer experience, says O'Neill. "Banks and insurance providers are commercially sensitive, and they don't want customers dropping out of the process or to see negative net promoter scores," he notes. "People have the option to go elsewhere, and they will do just that if you can't provide a seamless, frictionless experience."

> The question is what's the right level of friction – so that people get value but are protected

ONLINE BANKING ON THE RISE

Online banking usage among UK adults, %

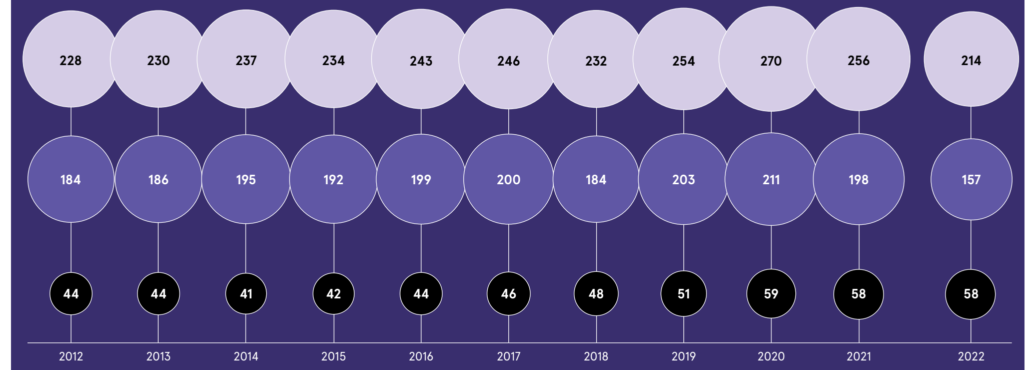
Finder.com, 2023



Commercial feature

THE DEBT-TO-TOTAL-CAPITAL RATIO WIDENED IN 2022

Total capital reported by Aon's Reinsurance Aggregate



How insurers plan to optimise capital in 2023

Reinsurance capital availability hit close to a 10-year low at the January renewals. Now businesses are maintaining a disciplined, data-driven approach to deploying their surplus

The capital market felt its fair share of shocks in 2022. The double whammy of increasing interest rates combined with equity and bond market portfolios trading well below historic averages has generated a material mark-to-market negative adjustment to company financial statements. And the result? Substantial unrealised losses across the board.

The economic slump that set in last year was compounded by heightened natural catastrophe exposures and loss experience resulting from an active US storm season headlined by Hurricane Ian. Paired with rising interest rates, this translated to lower investment yields across the board. Meanwhile, currency fluctuations in foreign exchange also restricted the amount of capacity being deployed.

"It was the perfect storm," says Kelly Superczynski, head of capital advisory at Aon's Reinsurance Solutions. "We had the biggest loss of capital in recent history, coupled with the fact that capital hasn't flowed back into the market like it normally does after an event, which has created a very challenging situation."

She explains that these interconnected challenges prompted reinsurers to withdraw certain coverages and increase rates by as much as 50% at the January 2023 renewals. Pricing for US property catastrophe and global property retrocessional businesses, in particular, peaked at multi-decade highs.

According to Aon's April 2023 Reinsurance Market Dynamics report, the net effect was that available global reinsurance capital declined by 15% - or $100bn – over the year to December 2022.

All that's to say that insurers needed to be extremely careful about how they deployed the limited capital at their disposal coming into the January renewals. So, with 2023 well underway and a complex risk environment still to consider, how is the insurance sector adjusting its investment portfolios?

Superczynski suggests that some insurers are leaning towards a big-picture approach which allows them to process challenges with an emphasis on outcomes that can temper risk appetites. This often means bringing together data-driven modelling and stress testing to determine the impact of multiple scenarios on investment portfolios at once. As macroeconomic shifts threaten to disorient decision-making, forecasting exercises can set the table for clearly defined strategic direction.

Given the ongoing volatility of the current economic cycle, it can be easy to fall into the trap of adopting an episodic outlook. Regardless, Superczynski urges insurers to focus their access to capital on delivering a consistent and stable outlook. She defines this outlook as one that requires a single source of truth, and that takes a long-term view of risk. The alternative - shoehorning data into a predetermined narrative to fit with the consensus at a particular point in time - is a zero-sum game.

"We saw that play out at the January renewals," says Superczynski. "Because reinsurers were able to be selective in who they provided capacity to, those companies that had solid data and consistent results and, as a result, could tell their story most effectively, secured the limits they needed. Those that didn't had a much more challenging time."

> Companies that had solid data and consistent results secured the limits they needed. Those that didn't had a much more challenging time

On route to developing a consistent outlook, companies have had to adapt their strategic approach to risk management, taking a more considered view of their capital allocation and being led by the data.

"The ability to demonstrate thoughtfulness and a data, fact and experience-driven approach and eliminate volatility ultimately leads to greater stability," says Sherif Zakhary, CEO of Aon's strategy and technology group. "That also enables companies to tell their own compelling story to differentiate themselves from the competition when it comes to securing capacity."

The insurance sector is heavily regulated and frequently assessed by rating agencies, meaning a conservative approach to managing capital and risk often takes precedence. This dynamic requires insurers to hold a large amount of capital to cover their exposures while trying to get a consistent return on their assets.

To optimise their capital, insurers need to first carefully think about the type of capital they want to use, whether that's traditional or structured reinsurance, debt or equity. That may include using a vehicle such as a sidecar or a captive. By the same token, they must also be realistic about the capital pools they can access.

The next step is to consider the risks they have to cover and decide how to allocate the capital. Once that capital has been deployed, its performance must be monitored regularly, and adjustments to the placement can be made if necessary.

"Companies need to get the right balance between different types of capital if they are using more than one," says Superczynski. "Then they need to decide how they are going to best align their risks with that capital, which will determine how it is deployed most effectively."

Most of the capital that is still coming in originates from the legacy market, according to Superczynski. "That market has grown exponentially from $5bn to $20bn in the space of just six years. It represents a huge opportunity for companies seeking capacity," she says.

As Superczynski sees it, the bottom line is that collaboration, resources and financial analysis solutions will play a critical role in allowing insurers to navigate a complex capital market in 2023. Effectively calculating how much economic and regulatory capital is required in real-time lets organisations make more informed decisions, respond nimbly to market shifts, and take advantage of new opportunities.

"Ultimately, capital is the glue that holds organisations together," Zakhary says. "So knowing how to deploy it effectively, particularly in these difficult economic times, is paramount to a company's success." He concludes with the assertion that understanding the true cost of capital, including the volatility of its returns, is the bedrock for any business to optimise its long-term returns.

$41bn

The reduction in total equity in reinsurance during 2022

That reduction was driven by unrealised losses of

$48.1bn

$9.6bn

of net income into reinsurance could not offset those losses

Aon's Reinsurance Aggregate, 2023

For more information, visit aon.com