How banks can turn risks into opportunities during a crisis like Covid-19

By Tijsbert Creemers-Chaturvedi

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The South African banking sector has a global reputation for being robust, well-regulated and resilient. These characteristics have stood the industry in good stead during times of crisis in the past - and will undoubtedly help carry them through the challenges of Covid-19. However, they will also need to find ways to mitigate risks and turn them into opportunities for growth.

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The country's banks typically have a healthy return on equity compared to even European or US markets – ranging between about 15-20% – driven by higher risks associated with emerging markets. These risks include bad credit or non-performing loans that lead to risk losses over the long-term. This is why banks need to build up a strong buffer to protect against these risks.

What the coronavirus pandemic has highlighted is the need to consider strategic yet impactful approaches to managing internal operations as well as their risk portfolios, and measures that protect and enable business continuity.

This largely means analysing their credit risk portfolio, how it evolves and reassessing costs reductions to help carry them through the crisis. Banks need to review their clients' credit risk and exposure levels, also considering their loan portfolio, and adjust their approach accordingly – especially around clients whose credit risk has the potential to expose the bank to vulnerabilities.

Additionally, South African banks need to revisit their business continuity plans, particularly on the liquidity and funding sides to ensure that funding continues both in the short and long-term.

The necessity in any crisis is to reexamine how much the bank spends on internal operations, external contracts and costs, and how it can trim the fat and put levers in place to build resilience through a crisis. Well managed banks look at a variety of scenarios and how it will impact their clients, as well as different sectors, and pressure test the measures they have in place to limit and control their credit risk exposure.

Using digital as a lever for banks to build resilience and add value

One of the key levers that banks can utilise to build resilience and lower costs is digitisation. It is well-known that digitisation lies at the heart of resilience in the banking industry, but the COVID-19 pandemic has made it ever more critical for banks to pursue digital transformation.

Banks need to develop a clear digital strategy to unlock the benefits of digital solutions in driving their risk and compliance functions – using AI, machine learning, and other advanced technologies to deliver predictive real-time insights, and execute faster and more efficiently.

The logic for digital banks is strong: if banks want to increase reach into other financial inclusion segments, digital and mobile is a powerful tool that will enable this and presents a major opportunity both globally and in South Africa.

Interestingly, the digital tools banks are applying now in the midst of the crisis, the way they are adjusting operating models and how they think of running credit risk and compliance will all enhance digitisation – so banks will have to ensure they stay relevant for this digital model to work and result in lower costs and greater reach.

There is also the opportunity to move to holistic digital solutions that address entire customer needs – also called eco-system/engagement platforms – while combining financial or insurance products. This involves taking a data-centric view of the customer so banks can serve their needs better. Customers are looking for these sorts of solutions and the possibility is not just expansion for the brand but also new job creation and opportunities.

Making a more large scale move to digital of course has implications for cybersecurity, which is always a critical consideration. Although cybersecurity is not necessarily under pressure during the Covid-19 crisis, it remains an area that banks must rethink as on-the-ground implementation is shifting from mostly an in-person model to remote working.

Remote working creates an environment where security needs to be increased, and compliance in terms of Know Your Customer (KYC) and remote working processes is vital. Banks are currently investing in their compliance and risk departments to guarantee that vulnerabilities in processes around remote working aren't being exposed.

Ultimately, the crisis has emphasised the need to innovate through digitisation to mitigate risks and unlock opportunities to create new value pockets both for customers and the banks themselves – and banks should 'seize the moment' in developing and implementing these digital solutions.

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