ZEB PERSPECTIVE

# The next revenue driver for banks

Online mortgages offer untapped potential

partners for change

# Key findings

1. Mortgage customers value good advice, a trusted partner, transparency and support to navigate the complex process journey

2. Customers are willing to do some of the mortgage process digitally

3. Digital mortgages are a largely untapped source of banking revenue growth

4. Banks should rethink digital lending to exploit this revenue stream

5. Banks should take action now, to gain competitive advantage in a thinly populated market

# What’s in it for you?

In 2020 we conducted a survey of >150 potential mortgage customers in DACH. With trends evidently becoming increasingly similar across Europe, we believe that our results are also applicable to other European banking markets.

We found that 94% of our respondents said they would do online research before visiting their bank to apply for a mortgage. Demand for digital channel options was highest among younger customers, while across all age groups, the survey results suggested that clear guidance about the mortgage process and accompanying services could overcome people’s reservations about online mortgages.

Respondents identified various ways that banks could attract them away from brick-and-mortar branches onto digital channels by offering more attractive online mortgages with some added value; in particular, better terms and conditions (80%), step-by-step guidance (62%) and a faster process (52%).

The survey underlined how beyond-banking offerings could enable banks to capture higher mortgage demand, especially if the service offered is integral to the mortgage process. For example, 63% of respondents thought property valuation would be a useful additional service, and 67% were interested in legal services. The results also confirmed that mortgage customers would like their bank to cover a broader part of their journey towards buying their home.

## Impulse - a house need

## Does the majority of respondents prefer offline or online?

**Research**

**94%**

of respondents would gather information on mortgage offerings digitally

**Advice**

**57%**

would seek mortgage advice offline

**Application**

**84%**

would calculate mortgage options by filling in personal data online

**Verification**

**80%**

consider submitting documents online convenient

**Final Closing**

**53%**

would prefer to sign the contract online

# Online mortgages

## - an overlooked, fast-growing revenue source

This still leaves the key question of whether online mortgages can contribute significantly to revenue growth. While terms and conditions – as we described above from a customer's point of view – are widely regarded as the major driver for mortgage decisions, focusing on a smooth, digital and highly convenient customer journey can definitely pay off. Based on our research, zeb believes that now is the moment for banks to take action and capture a largely untapped source of revenue growth in a thinly populated market.

Over the past decade, mortgages have formed a steadily increasing proportion of banking revenues in major European markets. For example, in Germany, zeb research shows that the contribution of home loans to retail banking revenues grew from 17% in 2011 to 27% in 2019. In Switzerland the share increased from 37% to 67% in the same period, while in Austria the rise was from 19% to 44%.

Our study of these DACH region home loan markets confirms that banks are not keeping pace with the accelerating trend towards digital mortgage products. German, Swiss and Austrian banks are constantly expanding their internet and mobile banking channels.

However, they have been slow to develop online mortgage products, as have banks elsewhere in Europe, with few incumbents positioned to benefit from this trend.

The COVID-19 pandemic has boosted online banking at the same time as emerging best practices in the global mortgage lending industry are bringing digital home loans into the mainstream. Customers who might have previously been resistant to internet banking are increasingly accustomed to performing banking tasks from their homes and talking to their advisors by phone or videoconference. Banks can leverage this lockdown-related surge in online banking to build customer trust in digital channels, which can be used when digital mortgage loans are offered.

Critically, big data analytics and fast-maturing technologies such as robotics, machine learning and Blockchain are enabling online mortgage providers to offer more customized products for individual applicants. For example, some digital home loan providers use Artificial Intelligence (AI)-enabled technology to conduct credit risk assessments of customers; others use machine learning to perform automatic property valuations by image recognition and develop algorithms to compare mortgage options.

**After Sales**

**95%**

**would check their mortgage statement online**

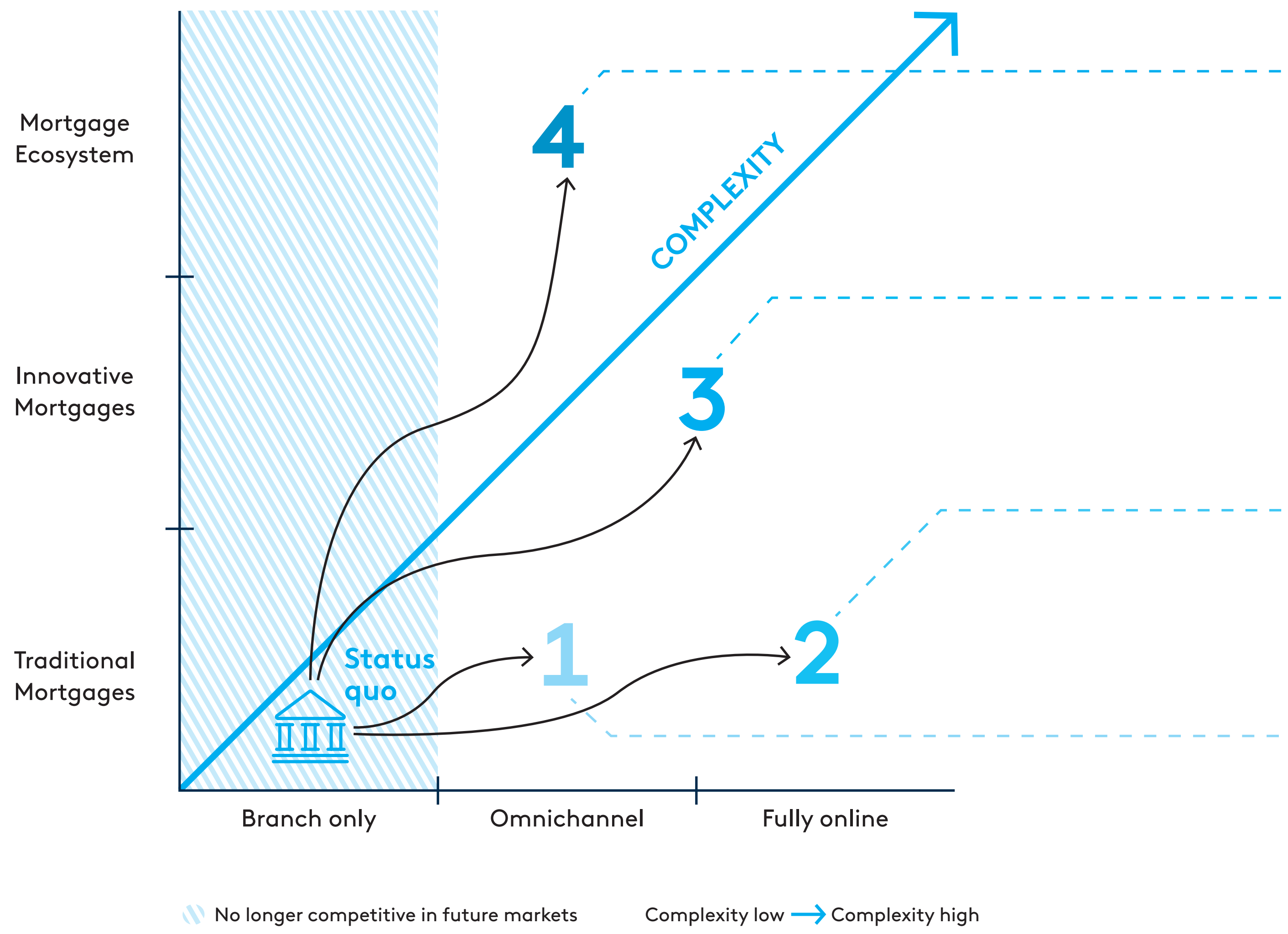
# Four positions for digital mortgage lending

Our research and client work indicated that banks recognize that they must improve their digital mortgage products and services to meet rising customer demand and avoid falling behind digital competitors. We recommend that innovation should occur incrementally, with rapidly maturing technologies enabling banks to encourage more customers to take digital steps on their mortgage journey wherever they are most willing to go online.

New success factors challenge the competitiveness of traditional mortgage market positionings

Along the two dimensions depth of offering and availability of offering, four new positions emerge

The strategic fit of the positions depends on the ambition level but also on the type of bank and its markets



While changing customer needs will not alter the fundamental success factors for banks, they will affect how competitiveness is defined in mortgage markets. In future, banks can compete more successfully in mortgage markets by increasing the depth of their offering in areas such as product innovation and pre- and post-purchase services. Banks should also widen the availability of their mortgage products through omnichannel distribution and marketing. In addition, the overall experience for the customer should be improved by offering a higher degree of accessibility, personalization, availability of different channels and transparency at every stage of the mortgage journey.

Within these parameters, banks can choose a suitable development path that best fits their market positioning, strategic vision, customer profile and competitive environment. This study identifies four digital mortgage market positions that banks can adopt to gain a competitive advantage in what is still a relatively clear field:

1. **Innovative incumbent:** enhanced customer journey via omnichannel approach
2. **Focused digitizers:** end-to-end digital mortgage process
3. **Diversified providers:** additional service offerings
4. **One-stop shops:** fully-integrated real estate ecosystem

**ONE-STOP SHOPS**

- → Offer an omnichannel real estate and mortgage ecosystem
- → Become one of the few one-stop shops in the real estate journey

**DIVERSIFIED PROVIDERS**

- → Add banking-related products and new channels
- → Target a broad group with additional services

**FOCUSED DIGITIZERS**

- → Fully E2E digitalize traditional mortgage products
- → Profit from low production cost and fast, low-interaction process

**INNOVATIVE INCUMBENTS**

- → Increase channels for traditional mortgage products
- → Focus on existing products, yet enable an omnichannel approach

"Digital home loans can boost growth by **opening up new customer markets.**"

**Michaela Schneider,**
Partner, zeb

# 1 Innovative incumbents

**Keys to success:**

- **Online and offline mindset and user-friendliness**
- **Omnichannel approach**
- **Efficiency gains to remain digitally competitive**

Innovative incumbents differentiate themselves from competitors by offering offline and online channel options for existing mortgage products at little risk to the bank. In addition to their traditional branch networks, they offer a range of digital channels for customers to use throughout the mortgage process, including comparison platforms, web portals and mobile banking apps.

They create value for both the customer and the bank by providing a focused, convenient product which can be digitalized incrementally based on customer demand at any stage of the mortgage journey. For example, our survey results showed that less digitally advanced older customers usually only wanted research and after-sales services as an online offering. More digitally advanced, younger customers also wanted a digital application and verification process, while the most advanced group wanted online mortgage advice as well. Customers can choose their preferred option at every stage of the mortgage process.

Innovative incumbents can meet all these varying demands by focusing on traditional mortgage products and offering a wide range of offline and online channels. A key benefit for customers is that they are no longer bound to physical branch opening times but can start a mortgage loan process at any hour and at home. The new online customer base generates additional revenue, and the partial digitalization of processes reduces costs.

# 2 Focused digitizers

**Keys to success:**

- → **Leveraging digital capabilities**
- → **Good user interface (UI) and user experience (UX) design**
- → **Back office digitalization**

Focused digitizers develop fully end-to-end (E2E) traditional mortgage products to offer online as an improved, seamless experience for advanced digital customers. Services offered include personalized online advice via video chats and chatbots, and fully digitalized application and verification processes and contract signing. The value for banks which choose to be focused digitizers is that they can: attract and retain a growing customer segment, especially among younger people; increase efficiency by digitalizing processes; and gather strategic customer information using data analytics and technologies such as machine learning and robotics.

To become focused digitizers, banks should already have an established online presence to provide an existing platform for mortgage products and services, and excellent in-house technology capabilities. From this starting point, they need to develop online products and services with good UI and UX design, competitive conditions and a high level of convenience. Marketing should be targeted at digitally-advanced customers who are looking for home loans on comparison platforms and do not care about brand names or personal relationships with bank advisers. Indeed there is no need for focused digitizers to have any physical interaction with customers during the mortgage journey.

A focused digital strategy can be tested with dedicated minimum viable products (MVP) that can evolve gradually into a full E2E product. The streamlined core mortgage product delivers higher margins by increasing the digital customer base. As a further option, banks can generate additional income by offering low-risk, commission-based white label products to profit from reduced development costs.

# 3 Diversified providers

Keys to success:

→ **Product innovation**
→ **Scalable IT infrastructure**
→ **Network of external service providers**

Diversified providers focus on banking and banking-related services, while offering a multichannel experience to capture value from a broad range of customers. Their core business is a traditional, omnichannel mortgage offering. Banks can leverage their own network to add new, banking-related offerings along the house purchase journey through different channels: for example, pre-purchase property valuations, digital cost planning, legal advice and insurance services.

Banks which adopt this model need strong partners to develop a network of alternative service providers, as well as good IT infrastructure and the ability to innovate to exploit the full potential of additional revenue streams. They also need a strong online channel presence for the core traditional mortgage offering, which acts as the base for developing the other services. Diversified providers leverage public trust in financial institutions regarding banking-related services and target customers according to whether they prefer online, mobile or offline channels. For all channels, our survey findings showed that customers wanted a range of easily comparable offers and fast processes.

Services delivered via an intermediary are more transparent and reinforce customer trust through co-branding, but are more expensive due to commission fees. Direct sales carry no commission fee and allow the bank to leverage its own reputation and focus on the most important services, while requiring a higher level of investment.

# 4 One-stop shops

Keys to success:

→ **Total coverage of customer journey**
→ **Large customer base**
→ **Strong partner network**

One-stop shops use network effects and generate lead fees through partnerships. They offer an omnichannel property and mortgage ecosystem, with services that include mortgage lending, home insurance, legal assistance, and property recommendations. The value for banks which adopt the one-stop shop model is that they can tap into the revenue potential of the entire property and mortgage journey, and gain a core competitive position in the mortgage services market. One-stop property and mortgage shops provide customers with a full range of options for all their real estate needs.

Building a one-stop shop requires immense resources for IT development and third-party integration. Banks must be willing to pursue a central role in the mortgage ecosystem and acquire the necessary expertise to scale up capabilities, resources and partners. They must also have influence over suppliers of services. Since there is only space in the market for a few one-stop shops, banks must be able to adapt to changing customer needs during a transformation phase that can last several years.

Specifically, one-stop shops must be able to: scale up rapidly from niche to mass markets; deliver products and services at pace to defend their market position; ensure their network is sufficiently robust and wide-ranging to preserve their value proposition; and possess IT with the capacity to become a USP and provide rich customer data insights.

# Start now:

## Define strategic pillars, assess economic viability and pave the way

Rethinking digital mortgage lending requires banks to follow a three-stage customer, market and strategic analysis. They must: define the mortgage needs of existing and target customers; assess which of the different digital lending positionings represents the best strategic fit for the bank, evaluating the impact on both the business and operating models; and develop a detailed business plan that covers estimated economic and non-economic profits from potential market scenarios, and possible risks and obstacles.

Operationally, banks need to move fast after this preparatory analysis to gain an early competitive advantage in digital mortgage markets which are still thinly populated. MVPs should be rigorously tested and adjusted in the shortest possible time before executing a rapid, low-key go-to-market roll-out. The critical conditions exist for a successful move by banks into digital mortgages – growing customer demand, increasing market potential and the four strategic positioning options identified in this paper. Banks must seize this opportunity to drive revenue growth, or risk falling behind rivals entering the digital race now.

**"Operationally, banks need to move fast to gain an early competitive advantage in digital mortgage markets."**

**Ulrich Hoyer,**
Partner, zeb

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