GLOBAL BANKING & Finance review

BITCOIN, BLOCK-CHAIN AND BASEL – HOW BANKS CAN HANDLE THE CHALLENGES

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Although the after-effects of the financial crisis are still being felt in the City, the UK's retail banking sector faces a more long-term set of challenges.

Alongside the increasingly complex requirements of the regulatory authorities, the banking market is changing rapidly. Customers are not only accessing services digitally – especially via smartphones, but every day seems to bring more news of "disruptive" technologies, payment mechanisms and digital currencies such as Apple Pay, Google Wallet and Paym, M-Pesa and Bitcoin.

Using block-chain technology that is based in the internet, digital currencies such as Bitcoin threaten the greatest amount of disruption as they do not require intermediaries such as banks. Should the underlying technology be widely adopted, it could expose the vulnerability of many institutions.

While adapting to these technological threats, established banks are also facing the twin pressures of, on the one hand, new challenger banks that have lower overheads and on the other, financial technology companies that are ready to reduce them to payments utilities.

As they re-organise themselves to weather this sea of change, all too frequently banks find they are held back by fragmented IT systems that have been built up over time in response to previous challenges and opportunities.

Faced with millions of metrics, they cannot narrow them down to what is business-critical and needs to be monitored in real time. This can have very damaging consequences when it comes to a key function such as payments processing – a field where there is set to be significant change.

The EU Payment Services Directive, currently in draft form, for example, is expected to come into force in 2017, with the aim of opening up the payments market to competition from non-bank entities.

The EU regulators are also indicating they want to see the payments processing market shaken up, which may well open the door to fintech companies and retailers as competitors to banks. At the same time, consumer demand for faster payments may lead to consolidation in clearing services.

If we consider the recent high-profile failures of major UK banks to complete hundreds of thousands of payments, we can see the scale of the problem. Institutions with labyrinthine legacy systems monitoring millions of transactions, have not been alerted when critical processes are heading towards failure.

These opaque systems give nobody a true understanding of what is critical. When a significant increase in transactions occurs for example, they never know if the system is coping until it fails.

These systems are not capable of deciding what is really important from among the billions of possible metrics – of applying the right business logic. All banks have monitoring tools, but most are bogged down in the detail. They lack the real-time view of what is really critical which would give banks the chance to intervene before processes collapse.

The same is true in achieving compliance with the Basel Committee on Banking Supervision's regulation BCBS239 which comes into force for the large banks next January (2016). As a set of principles with which a bank has to comply, rather than a defined set of metrics or KPIs, this regulation demands risk reports are timely, complete and accurate. Inevitably, many banks struggle to understand how they should measure themselves against these headings and start off with the wrong, and expensive, approach.

They should start by keeping things simple – defining only what is critical rather than thousands of additional KPIs which do not add value. Then, the monitoring of these fundamental KPIs needs to be embedded into everyday processes, rather than sitting in a solution that adds another layer of complexity.

Proactive alerting through the use of traffic-light monitoring can be built in so that potential problems are flagged up at amber and nipped in the bud in order that they never reach red status.

What a bank needs is a tool that works within conventional process and IT monitoring solutions. It must be built by experts who establish the real flow of business-critical data that needs to be monitored and understand how to monitor it.

They will combine this with their technology skills to ensure that monitoring of the flow is conducted in real time and is full embedded into a bank's existing solution. This is an approach to monitoring that has the logic and intelligence to comprehend the bigger picture and predict a failure, allowing for remedial action.

Once key metrics have been established, performance can be measured against them, building them into a dashboard, supplying business context and insight.

In simple terms, the bank takes conventional end-to-end flow monitoring of processes and boosts its utility immeasurably by applying its own business logic to put key metrics in context.

Such a solution will tell the user at a glance which of their critical processes is compliant and what they should be worrying about. It can quickly be implemented as an add-on, without the need to overhaul an entire IT estate.

If a bank has this end-to-end insight into its processes, it will have greater reassurance that it is providing customers with the services they want and the regulators with the compliance they demand.