

BANK LEUMI READIES ISRAELI DIGITAL-ONLY LAUNCH WITH GLOBAL AMBITIONS

*Bank Leumi is gearing up to launch Pepper, Israel's first standalone digital-only bank. Currently at beta stage, the bank will launch to the general public later this year. Pepper, which will offer current and savings accounts, lending products and a P2P payments app, is targeted at millennials. **Robin Arnfield** reports*

We decided to set up a new venture that will be completely separate from our core business, even if the significant thing is that we are competing with ourselves," Bank Leumi CEO Rakefet Russak-Aminoach told the FT Innovations conference in November 2016.

Israeli newspaper Globes reported: "I absolutely believe that the fact that Pepper is being established in Israel – the start-up nation – will help distinguish us, and that ultimately we can also make Pepper into a global company."

FEE-FREE

Pepper says it will enable its customers to fully manage their banking via smartphones, and that it has no ongoing chequeing account-management fees, as all basic banking transactions are free. It will only charge for 'exceptional' items, which it defines as 'special activities and services that you most likely won't use very often'.

"Most traditional banks use digital channels as an extension of their existing services," Pepper's CEO Lilach Bar-David tells RBI. "They basically take their existing banking products and try to fit them into smaller screens. However, Pepper was designed for the needs and lifestyles of millennials.

"Applying a user-centred approach that includes on-going co-creation, ideation and validation with target customers, Pepper is designed to provide a personal, proactive banking experience, with products and services built for the mobile-obsessed generation."

Bar-David says Pepper is the first mobile-only bank in Israel, and that it is focused on challenging the status quo in banking.

"Pepper will allow everything to be done entirely through mobile devices – account-opening, customer service, money management, savings, loans, and payments," she tells *RBI*.

"Millennials are known to be more digitally active, specifically via mobile. In a recent study we conducted, we learned that millennials check their bank accounts at least once a week, and that over 40% use digital banking services. Also, most users surveyed said their banking app is more useful than their credit card app."

"Financial institutions today are facing rapid and irreversible changes across technology, consumer behaviour and the economy," Bar-David continues. "The industry is suffering from a heavy lack of trust. There's a demand from consumers for a Google- or Facebook-like simplicity in their banking experience.

"This has led to a banking products revolution – a new breed of technology-driven and consumer-centric financial institution-challenger banks.

"In order to truly disrupt banking, we needed to create a different organisation," Bar-David says. "As innovation was the topic, culture was our first concern. We are a bank that is full of people with passion for technology, design and, of course, banking.

"We set up our startup in July 2015 with eight people, and grew to over 150 within six months. Thousands of ideas were thrown into the air, and most of them ended up in the trash can. At the end, we came up with

Pepper. Pepper is a bank that speaks in native digital language and is 100% mobile, full of content and insights to help customers optimise their money.”

DESIGN THINKING

The bank worked with Denmark-based Designit to develop its products and customer service experience using what it terms ‘design thinking’ methodologies. The process involved interviewing consumers about their needs and behaviours related to money.

To make Pepper more attractive to millennials, the bank partnered with Israeli digital authoring software vendor Playbuzz to provide personalised, interactive content, including polls and quizzes for its banking app.

“If we can produce clear content that will make people understand their credit and payment options, and provide them with alternatives, we can create a banking experience that people will like and want to return to,” Bar-David said in a news release.

“Content will be at the helm of our communication with users. The goal is to be relevant – both with our content and in the form of presentation, which is similar to how users consume content today.”

“Banks suffer from a relatively negative image due to the nature of the industry and the associated red tape,” Yael Shafrir, Playbuzz’s GM Middle East, Eastern Europe and Africa, tells *RBI*. “They also find it hard to connect with their audience on a personal level. One of the main goals in our collaboration with Pepper was to create a more meaningful, positive user experience through personalised content, which will in turn be translated into a more positive view of the brand overall.

“Imagine customers using Pepper’s app on the day they receive their salary, and engaging with a piece of content in the Pepper app that provides the top 10 ways to plan a budget. This is a friendly approach to a serious topic, and will be presented in an interactive format that encourages social sharing.

“By integrating Playbuzz’s content technology, Pepper is able to study users’ content preferences based on interactions with previous items, and create a more personalised content experience moving forward,” Shafrir continues.

“In addition to the high relevancy level, the interactive formats add a gamification element, making the content-consumption process more enjoyable, and increasing key engagement key performance indicators including dwell time and completion rates.

“Our experience in working with financial services brands shows a strong need for engaging content in this environment,” Shafrir adds. “American Express and Halifax have created interactive content campaigns with Playbuzz, successfully reached their target audience, and created a well-targeted, meaningful dialogue.”

TEMENOS

In August 2015, Swiss banking software vendor Temenos signed a multi-year agreement to supply Leumi with a new core banking system based on the Temenos T24 platform and the Temenos Connect digital channel software. In the first phase of the contract, Temenos has provided Pepper with T24 and with Temenos Connect, and the software will gradually be rolled out across all Leumi’s business lines, replacing an ageing legacy core system.

“It’s great news that Leumi is building its digital bank Pepper on a new technology stack,” says Forrester Research analyst Aurélie L’Hostis. Leumi and Temenos are working with Deloitte and Israeli IT firm Matrix on the deployment of T24 and Temenos Connect.

According to Let's Meet Pepper, Banking Services of the Future by Hickry Meirav and Revital Cohen, respectively partner and manager at Deloitte's FSI Solutions/Technology Advisory Services, Leumi's major challenge in the new digital banking era was to become agile enough to support a quick reaction to market opportunities.

"Since [Leumi's] legacy core system lacks the ability to integrate changes within a short timeframe and at reasonable cost, it was decided not to use Leumi's mainframe but to implement Temenos's T24 solution," the Deloitte consultants wrote. "Regulation was one of the project's main concerns.

"The complex and increasing Israeli regulation requirements have defined a major gap between T24's off-the-shelf capabilities and the required solution for Pepper services and architecture. Since our goal was to maintain as minimum developments as possible, this challenge was even more complex."

Deloitte provided guidance to Temenos in complying with Israeli regulatory requirements, Meirav and Cohen wrote.

"Temenos has made great strides and investments to support the digital transformation of its customers," Tom Zink, associate research director of IDC Financial Insights EMEA, tells *RBI*.

"This strategy has been a key priority for the last few years, and ties together Temenos's more recent focus on customer experience, omnichannel capability, actionable data analytics, and a fintech collaboration platform with its world-class core banking system. Temenos has enabled a number of traditional banks to launch a digital- or mobile-only offshoot."

DIGITAL DIVISION

In June 2015, Leumi established a digital division which is overseeing the development and launch of Pepper. The digital division is also responsible for the bank's Leumi Card credit card subsidiary, as well as for Leumi's marketing department, business development department, and Big Data activities.

As of January 2016, over 60% of Bank Leumi's customers used digital channels to carry out their banking operations, with approximately 52% processed through digital channels, the bank said in an investor statement.

Leumi's digital banking plans are part of its efforts to reduce costs, which include an agreement with 695 staff to take early retirement on 30 December 2016, as well as a branch merger program.

During the next five years, an additional 640 employees are expected to retire from Leumi within the framework of normal retirement, the bank says.

"Israel is globally renowned for its entrepreneurial, innovative startup scene leveraging the country's unique advantages such as small size, high mobile engagement, availability of talent in areas such as Big Data, machine learning, and cybersecurity, an unparalleled R&D budget, and a buoyant venture capital scene," says Zink.

"Fintechs have been growing in this environment, however more with an eye to the international market than the domestic market. The Israeli banking system, on the other hand, is dominated by large banks with little room for challengers to penetrate the market, due to regulatory constraints.

"While digital banking has been a key priority for Israeli financial institutions, the state of the industry doesn't differ much from other markets with conservative regulators," Zink continues. "Although almost all transactions can be done digitally, the regulations still mandate that consumers come to a branch for high-value transactions or for opening an account – mandating some form of physical presence.

“In January 2016, the central Bank of Israel (BoI) published new online banking policies allowing existing customers to open bank accounts online or change their bank, without the need to come to a branch.

“While there have been attempts to liberalise the financial sector, the reforms have been moderated by mandates from the BoI, such as minimum capital requirements and licensing requirements restricting smaller platform and service providers’ market access,” Zink explains.

“Currently, the BoI is in the process of liberalising the credit sector, forcing large banks to divest their credit card companies, allowing access to new acquirers and potentially allowing credit card companies to apply for full banking licenses. This could result in the first ‘new’ banks in decades. As today all credit providers are backed by large financial groups, it is no surprise that Pepper is built on the back of Leumi to take its digital transformation to a new level.”

SMALL MARKET

“The Israeli financial sector is a relatively small, local market consisting of a small number of major Israeli banks, insurance companies and institutional investors,” says Zink. “These are often perceived by the public as slow-moving and conservative.

“Banks have understood the potential of cost savings from digital transformation, and the sector is moving towards a level where almost all transactions can be handled digitally. Banks have partnered with fintechs to stay on top of the digital transformation process, launching new products and channels such as virtual branches, contactless payments, robo-advisory services, and social media analytics – but nothing we haven’t seen in other markets.”

“Large Israeli banks are also collaborating with Israeli fintechs to test cybersecurity, data analytics and mobile applications, and are partnering with startup funds such as Elevator Fund and Microsoft Ventures. This is a massive change for the Israeli banks, which traditionally developed most of their infrastructure and apps in-house,” adds Zink.

“Their mindset is changing towards an understanding that banks need to open up from business, cost-efficiency and innovation viewpoints. So it’s no surprise that application programming interfaces are also on top of the Israeli banks’ agenda.”

Lawrence Freeborn, research manager, European banking at IDC Financial Insights EMEA, notes: “It’s interesting that Pepper isn’t planning to charge any fees; Leumi, Hapoalim and other Israeli banks charge for a long list of common tasks. So, for the domestic Israeli market, a fee-free approach could help Pepper get off the ground.

“Pepper is at an advantage compared to independent challenger banks across Europe in that it has the backing of Leumi and so can afford to compete in this way.”

“It’s interesting to speculate on whether, in the long term, a fee-free approach with digital-only touchpoints and relying on analytics for the personalisation of customer service will be more profitable for Leumi than a traditional approach which has to cover the cost of the branch network and employees,” Freeborn continues.

“But the fee-free regime suggests that Leumi will encourage its own customers to move over to the digital-only model.

“In any case, Leumi is positioning itself for the generation of bank customers who are most comfortable in a digital setting. Bearing in mind that the infrastructure will be the same as for Leumi, the product set is also likely to be similar, at least initially.”

SANDBOX

“For a variety of reasons, banks globally will consider the idea of offering a digital subsidiary that gives them a sandbox,” says Stephen Greer, banking analyst with US-based Celent.

“The digital subsidiary is able to free itself from its parent’s legacy technology while offering a digital proposition that lets it enjoy better use of data.

“The digital bank also has a more flexible operating model and greater modularity, so it can experiment with more modern and advanced products and services,” adds Greer.

“Most banks that create standalone digital propositions are using them as a potential long-term strategy for millennial customer acquisition or to move existing mobile-first customers to a digital proposition. Mobile-first customers are still only a small portion of most banks’ customer base, but over time they will become a significant part of a retail bank’s customer base and offering.

“It sounds like Pepper will be capturing a lot of data on its customers so it can offer them lending products via their mobile phones,” says Greer. “This is unique and isn’t being done by many other digital banks, with the exception of innovators such as Poland’s mBank. But what we’ve seen is that very few digital-only banks are profitable yet.”

International retail banking consultant David Cavell warns that the limited size of the Israeli domestic market may restrict Pepper’s growth, citing the example of imaginBank, the digital-only bank launched by Spain’s CaixaBank in early 2016.

“CaixaBank has 3.1 million millennial customers aged 18-35, and this represents 30% of its customer base,” says Cavell.

Also, Spain has a population of around 48 million, compared to Israel’s eight million. In a market like Spain that offers large enough scale, it makes sense for a large, well-resourced and technologically proficient bank like CaixaBank to create a standalone proposition.

“The new sub-brand, imaginBank, will pull customers who weren’t previously with CaixaBank, while existing customers who weren’t engaging with digital banking may migrate to the standalone bank as they find its premise attractive.

“The reality is that setting up Pepper may cost a large amount of money as Leumi has had to use external vendors, and Pepper may not be financially viable due to lack of scale in the Israeli market.”

Designit part of Pepper from day one

The entire product-service experience of Pepper was developed using ‘design thinking’ methodologies. The Designit team was part of Pepper from day one, working closely together to ensure a human-centred approach that puts customers first at every step of the journey.

As a global strategic design firm specialising in digital and business transformation, Designit’s experienced, multidisciplinary team of strategists, designers and technologists from around the world – the US, Spain, Denmark, France, the UK, Colombia, Norway – led the innovation process.

Designit worked closely with Pepper’s product, marketing and development teams to define and design an entirely new banking experience.

Designit also engaged with consumers to discuss their financial needs, to see how they manage their money, and understand what bothers them about banking services today. Designit learned about their lifestyle, and how today’s banking solutions do not help them achieve their goals.

During the process, the Designit team learned that saving money does not necessarily mean depositing it into a savings account. Many people consider making a smart purchasing decision, using a discount or a coupon as great way for saving money and making the most of it.

It also learned that even though many consumers prefer to use digital channels for banking services, it is also helpful and reassuring to know that they can always reach out to real bankers and service representatives if they need help. Insights like these, guided Designit as it worked to design Pepper's products and services. Every Pepper product, service, feature, and experience was developed this way.

There was the added aim of wanting to challenge the status quo of branding design. As a brand built from a digital product, Pepper's design is based on a unique RGB colour palette that cannot be duplicated for print, meaning it is purely digital.

While most banks use single, solid colours for their brands, Pepper uses a range of vibrant colours and a rich visual language, that makes it stand out in the banking design scene and deliver on its promise to provide an innovative range of products, services, and experiences.

The detailed design work is also reflected in Pepper's typography. Its font is custom-made, simple, and bold to reflect Pepper's direct tone and style. The goal is to design an experience that not only provides solutions to customers' financial needs, but is also easy, fun, and similar to other digital products and services.