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THE EVOLUTION OF RETAIL BANKING IN THE UAE

Doing more with less



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The evolution of retail banking in the UAE: Doing more with less

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Statistics provide powerful and objective insights about the economy and the society. However, analyzing different data sets can sometimes result in contradictory conclusions which requires further investigation. We encountered such an interesting paradox as when we examined data sets to evaluate availability of financial service in the UAE. Capital is one of the main inputs of production and competitive economies have advanced financial markets which contributes to the most efficient allocation of these resources thus enabling wealth creation. In the Global Competitiveness Report (World Economic Forum 2017) the UAE rank 24 in the Financial market development pillar. Our aim with this article was to address the question whether the UAE is overbanked or if on the contrary access to financial services was adequate and get a sense of the evolution of banking in the country. To start we

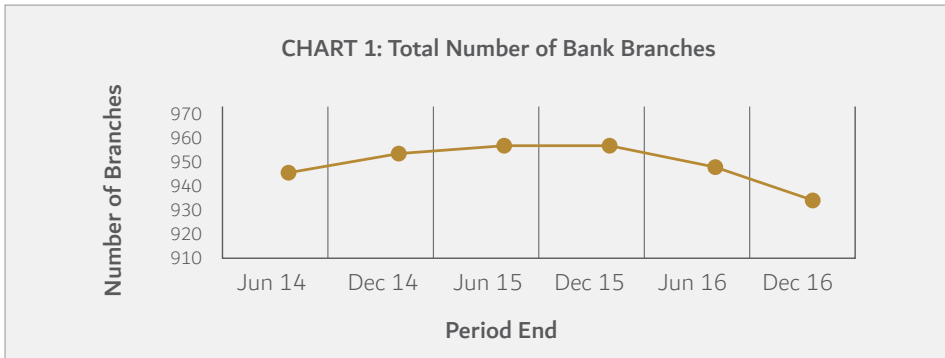
examined the evolution of the banking network leaving aside the thorny question of access to financing. The data sets we analyzed seemed to indicate that the network of branches was becoming less expansive. Nevertheless, when taking into account that the financial sector is constantly investing in technology in order to enhance, secure and improve its offering, a totally different story emerged: while traditional channels were phased out, clients were offered a range of different access options that gives a fascinating perspective on the future of banking prefiguring deep structural changes that will affect tomorrow's banking. A few banks are already paving the way towards the future of banking by experimenting with different technologies such as Artificial Intelligence and blockchain¹ which could eventually lead to the first branchless banks,

¹ A blockchain is described as "an open, distributed ledger that can record transactions between two parties efficiently and in a verifiable and permanent way." (Iansiti, Marco; Lakhani, Karim R "The Truth About Blockchain". Harvard Business Review - Jan 2017)

1. How has the number of banks branches evolved?

The number of locally incorporated banks remained at 23 banks by the end of the second quarter of 2016 (mergers and creation of new establishment remain quite rare)². The number of branches saw a more dynamic evolution (see Chart 1). It steadily increased from June 2014 to December 2015 before going through a significant decline. In addition, the number of

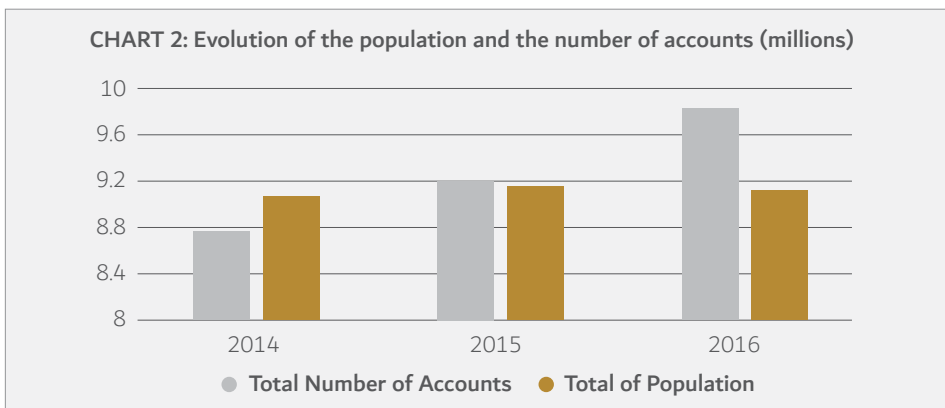
Cash Offices decreased from 90 offices by the end of June 2015 to 86 offices by the end of June 2016. This decline cannot be explained by the decrease in the number of establishment as it did not change. One possibility is that the demand for banking services declined, either through a drop in number of accounts or a drop in population.



2. The decrease in branches compensated by other channels.

Chart 2, convincingly shows that both the population and the number of accounts actually kept increasing, from 2014 to 2016 demonstrating that demand for financial services has not decreased.³ Therefore, it appears that banks are serving more individuals

or managing more accounts with less branches. This leads to questioning if this has been achieved through a degraded service, at least in terms of access or if there is a shift in consumer behavior and emergence of trends in banking that could dispel this hypothesis.

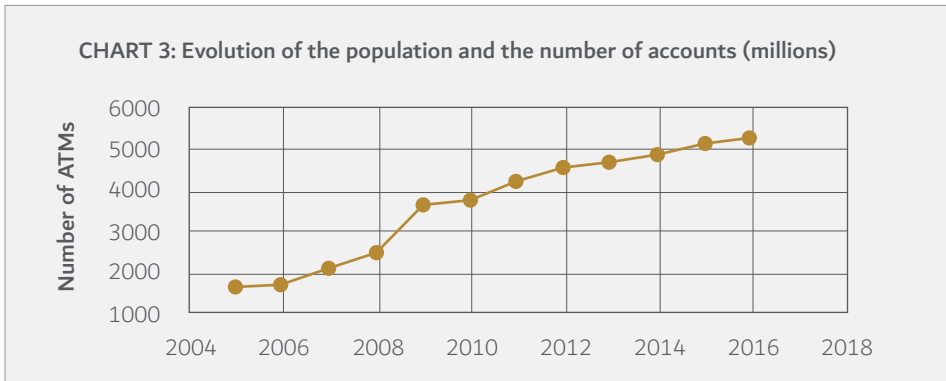


² It is worth noting that there had been a couple of mergers in the recent history, in 2007 between Emirates Bank and National Bank of Dubai creating ENBD and in 2017 between National Bank of Abu Dhabi and First Gulf Bank to create FAB but in this latter case the effect on the number of branches is yet to be evaluated.

³ We eliminate the very unlikely case where the number account holders decreases and number of account per individual would increase.

Chart 3 reveals that despite a drop in branches numbers, there is a significant increase in the number of ATM. Indeed ATMs have become more advanced and provide all services that were performed before by tellers, 24 hours a day seven days a week. Clients have become more comfortable using them as well as other

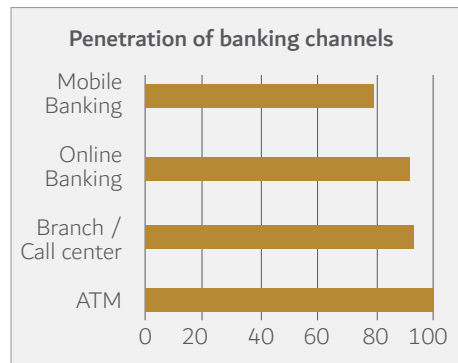
service channels such as phone and internet banking included from their smartphones. These technologies allow bank to reach higher levels of efficiency and serve more accounts with less branches and in some cases bring even more convenience to their account holders.



The development of virtual banking channels

As shown, the increased number of ATM largely compensated the closure of branches. A study conducted by Avaya (a global communication company) shows that UAE consumers use a wide array of channels beside the ATM's to reach their banks without the need to physically meeting a bank advisor by phone (Avaya, noted a report published by gulf news). In fact 90% of the people in the UAE are using digital banking channels. And up to 100% of them use ATMs for their banking transactions. In addition, a high percentage also uses mobile banking. They usually use the internet banking for new products and information request as well as the mobile banking for transactions (Shirish, 2016).

As most of the national banks in the UAE have launched mobile banking apps it is possible to validate the trend by counting the number



of downloads on Google's Playstore (data not available for the iPhone). We have evaluated that across 19 banks there has been between 900,000 to 4,500,000 installs of banking mobile apps. This clearly confirms that a significant number of account holders use different channels.

How will the UAE banking sector evolve in the near future?



The banking sector in the UAE is very dynamic and lately saw a number of initiatives, attempting to innovate to make access more efficient. To make banking more convenient and simple to customers, Emirates NBD has introduced the new artificial intelligence robot “Pepper” who can recognize human emotions and will be available in all bank branches and the bank’s marketing and promotional events, interacting with customers to understand their needs and present the banks different products and services in an engaging way. So one direction for the UAE is maybe a hybrid bank where Robot partially replace humans.

Moreover, if we consider the banking systems evolution in other markets we can see that there are countries, which swiftly move to digital banking, for example in South Korea HSBC bank close about 80% of its branches due to digitalization. In the UAE, there are many other directions that banks are exploring and could embrace in the near future.

For example, as mentioned Al Mashreq bank is going branchless because of automation and self-service technology. They adopted a vision where the entire bank is more technologically advanced and less reliant on people and manual

process in the future (Clowes, 2017).

Another emerging trend is in the development of services powered by smartphones such as moving your money without the need of creating a bank account. ADIB is working on the introduction of an electronic wallet to allow users to use their smartphones for buying, transferring and storing money.

More lately, Emirates NBD has introduced the blockchain technology to process cheques with the aim to decrease fraud and accelerate the settlement process. Before few months, the bank announced the first stage of the initiative under the name “cheque chain which is a beginning to integrate the blockchain into banking products and services. Emirates Islamic bank has also announced that it will be using the blockchain technology in order to prevent cheque fraud. Using these new technologies in banking systems will change the banking experience in the UAE (Al Mahmoud T, 2016). Even if some of these initiatives fail, they will provide valuable insights to the banks and eventually the successful ones will infuse even more dynamism in the sector and make it more efficient.

Towards pure digital banking

The financial services sector in the UAE is on the verge of starting a new journey towards a full digital transformation creating even more disruption. Therefore, the banks need to move quickly to stake their claims in the new landscape.

In the longer term, this raises up the question if the customers will be willing to open an account in banks that don't have any branch.

A study by McKinsey & company shows that people in the UAE are willing to open bank accounts with a digital bank, 48% of the people would agree. The UAE seems ripe for seeing the appearance of a purely virtual bank with no physical branches. With the advent of Artificial Intelligence, maybe we will see the appearance of a bank mainly ran by machines and virtual advisors powered with AI.

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