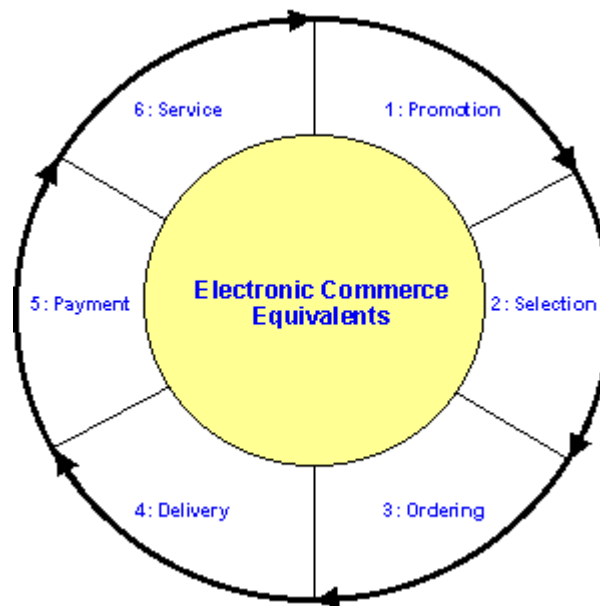




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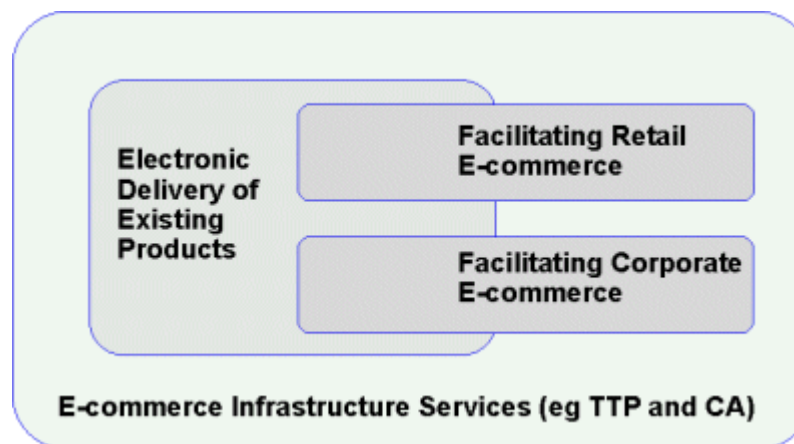
E-COMMERCE OPPORTUNITIES FOR BANKS

Electronic commerce – broadly defined as the transfer of value over the Internet – is revolutionising the way we live and work.



The diagram above illustrates six stages of a generic commercial transaction, from initial promotion and selection of a product or service to be purchased, through ordering, payment and delivery, to after-sales service. At each stage, digital technologies are supplementing, replacing, or extending conventional, physical ways of doing business. There are opportunities for banks in every segment of this "e-commerce wheel of fortune", which, very broadly, can be summarised as **adding value through providing a trusted environment for electronic trading.**

There are four main, overlapping classes of opportunity for banks, illustrated thus:



Electronic delivery of existing products is the most immediately obvious application. Several financial institutions have launched [Internet banking](#) services (see "financial futures" website) which enable customers to carry out a range of on-line financial transactions such as checking account balances, making payments and purchasing new products, conveniently and securely. Almost all banks are apparently planning to launch similar services, which means that this new delivery channel will rapidly become a commodity. The challenge is to create an innovative and compelling **context** component of the [value chain](#) (see "**financial futures**" website), which adds value relative to other delivery channels and differentiates the service from other competitive offerings, for example:

- ❖ The facility to download content such as account details, share prices, or interest rates, directly into a financial planning package such as Quicken or Microsoft Money.
- ❖ Packaging together content from a variety of related sources. For example a mortgage provider could present information about available houses (with pictures), neighbourhoods (schools etc.), related services (solicitors, surveyors etc.), and so on.
- ❖ Hosting a virtual community of customers who share some common interest. For example corporate treasurers would probably value a banking site with articles on treasury technology trends, or best practice, or comparative benchmarking, or a bulletin board for exchanging ideas and making contacts.

Facilitating retail e-commerce is a natural opportunity for banks given their trusted status. Although goods such as software, books, CDs, travel and indeed almost everything else are now bought routinely over the Internet by a small number of early adopters, the mass market remains acutely nervous about the perceived insecurity of cyberspace (see "financial futures" website).

- ❖ The first opportunity is therefore for banks to leverage their expertise of encryption technologies and provide a secure trading environment where sensitive financial data such as credit card numbers are encrypted, and buyers and sellers are authenticated using digital certificates (of which more below).
- ❖ Expanding on this, banks could provide a useful service by handling transactional complexities such as VAT, customs duties, currency conversions or refunds.
- ❖ This role becomes more valuable as the transaction becomes more complex, with several counterparties. For example we can envisage a financial institution adding significant value by providing a simple, secure, on-line means of approving and paying for medical services under a company private insurance scheme.
- ❖ There is a major opportunity for banks to expand their payments franchise. The conventional bank credit or debit card is an excellent payment method for

the Internet, and will become even more so when security is improved (although the jury is out on whether the SET standard is the answer, or whether there is scope for a simpler, cheaper scheme).

- ❏ But there is also a terrific opportunity to establish a global **micropayments** system to handle very small payment amounts of a few pence, or fractions of a pence, which cannot be economically handled by the credit card system. This is probably some way off (although there are several pilot schemes in existence) but could form the basis of a completely new digital economy in the long term.
- ❏ Finally, there is undoubtedly a huge demand for some sort of trusted guide to the Internet, which helps users to navigate through the web and deal only with reputable, value-for-money suppliers. This seems a natural role for banks, but attempts to establish **electronic malls**, by, for example, Barclays (with Barclaysquare) and NatWest (with Buckingham Gate), have not been particularly successful to date. It seems that the demand is currently being met, either by strongly branded electronic traders such as Amazon or CD-Now, or by "portals" such as AOL or Cendant.

Facilitating corporate e-commerce is in many respects an even better opportunity for banks since the volume of business-to-business trade is so huge and since the transactions are so complex. Of course electronic trading in the form of EDI has been around for at least a decade, and many banks have attempted to launch EDI services, most without much success. What has changed is that the Internet has made possible a much cheaper and simpler form of EDI – sometimes called "EDI Lite" – which even the smallest business can use to improve productivity, often dramatically. The banking community could come to dominate this new way of working by providing, not just electronic payments, but also secure transmission of trade documentation, and a host of other value added services such as on-line insurance, factoring, letters of credit, accounting, inventory control, and all the other logistics of corporate trade. For SME's in particular, it is possible to envisage banks at the centre of a "value web" of trading partners. The best way of thinking of this type of opportunity is by analogy with a good old fashioned branch manager who would act as a pillar of the local business community, helping local traders to meet and do business together. The electronic equivalent would perform essentially the same services, but in a global, virtual community.

Providing e-commerce infrastructure services is the final area of opportunity for banks, and the most obvious such service is security. Underpinning secure trading over the Internet is a new breed of technology based on public key encryption, which enables trading partners to validate each other, maintain the confidentiality of information, and ensure that messages are delivered intact and unchanged to the right destinations. A global infrastructure of "Trusted Third Parties" is needed to manage this technology, issuing cryptographic keys and digital certificates, and enabling customers to authenticate their identities using digital signatures. This will be a massive new business and banks are the obvious candidates for administering it, by virtue of their familiarity with the technology, their global networks, and, most importantly, their trusted status. Recently, a consortium of eight of the world's leading banks has announced just such an initiative based on Certco's technology. In many respects, what we are witnessing here is a return to the very beginnings of banking when trusted individuals began to make a living by providing a secure financial environment within which merchants could trade. The more innovative bankers are doing the same thing today, but using space-age technology, in cyberspace.

Interested? Please contact Nick Collin on nick@ncollin.demon.co.uk or **+44 (0)207 833 8765** with comments or questions.

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