White Paper: **February 2022**

The Journey Toward the Digital Mutual

What does digital transformation mean for building societies?

Beatriz Barbosa
Ian Bundey
Anthony Burgess

vmware®

"Over the coming months and years, the financial industry dependency on AI to process mortgage applications, chatbots, and make risk decisions and calculations will become widespread. This processing of data will demand huge compute capabilities (unburdened by tech debt), so organisations should expect the continued emergence of fintech and the need for the incumbents to lean heavily into new ecosystems to compete."

Brian Hayes
Financial Services Industry Director
VMware

Executive summary

This paper has been created to guide building societies in the UK to successfully navigate the future requirements for their digital journey. Our findings suggest that technology modernisation is crucial to enable more cost-efficient and effective ways of working. Additionally, it will help meet the needs of a customer base and distribution partners that increasingly turn to digital channels. Ultimately, this can only be achieved when strategies for a culture change of people and processes are effectively planned and implemented. We have developed the following guidance based on our experience helping our financial services customers digitally evolve over the past 20 years.

How technology is shaping the financial sector

The key to longevity in the financial sector is a customer base built on trust and a portfolio of products and services that clients need. In 2022, financial institutions expect to spend more on technology and digital skills[1] than ever before. The pandemic led institutions to realise the importance of investing in digital[2] for higher stability and resilience. Increasing the scale of cloud-based applications and data cloud enables the automation of key business processes, removal of manual tasks, resulting in the optimisation of costs and processes, and a productive and engaged workforce.

The emergence of remote banking has led organisations to facilitate a remote workforce as well as remote services and support to customers. As such, open finance and omnichannel are becoming the norm. There are API management platforms linking customers' financial information though mobile apps, browsers and smart devices[2], which reduce the resources needed on the institution's side while simplifying customer interactions. These high-tech investments have led financial institutions to struggle to differentiate. As ethics increasingly influence consumer buying decisions, they become a differentiating factor, resulting in the expansion of sustainable finance products and services.[1]

The impact on UK building societies

Building Societies and their Mutual Advantage

Building societies are cooperative financial institutions in the UK owned by members and driven by community values. Core services include savings and mortgages, but, unlike banks, profit is distributed among members rather than external shareholders. Traditionally, they have been the chosen partner for families when opening "digital children's accounts"[3], however loyalty is lost around teenage years as they seek digital, contactless services.[4] A new generation of cloud-based core banking systems has introduced competition, and the pioneering fintechs have almost exclusively gone down this route. Nevertheless, today, younger generations are more likely to make purchasing decisions based on a brand's ethics and trust.[5] These values, sought by new challenger financial institutions, have long been kept at the core level by building societies.

As with so many organisations today, UK mutuals need to continually evolve digitally, adopt API-driven approaches to quickly deliver a modern user experience, and remain relevant to current and potential customers. For most, the ability to compete in the

1 Forrester. "Predictions 2022: Banks Will Double Down on Innovation." Aurelie L'Hostis. November 2, 2021.

2 BizTech. "4 Financial Services Tech Trends to Watch in 2022. Alexander Huls." December 07, 2021.

3 Unisys. "To Attract Younger Generations, Building Societies Must Respond to Challenges Posed by Neobanks." December 18, 2019.

4 Cushman & Wakefield. "Are Millennials and Gen Z Powering a Fintech Revolution? Dr. Dominic Brown." January 1, 2020.

5 McKinsey & Company. "True Gen: Generation Z and its implications for companies. Tracy Francis & Fernanda Hoefel." November 12, 2018.

At the start of the COVID-19 pandemic, online capacity could not meet the high demand for mortgages, leading to longer waiting times, lower customer satisfaction and trust, and, consequently, revenue.

In 2019, Newcastle building society was the first to launch a debt advice tool courtesy of open banking technology to facilitate the resources required by the society and speed mortgage applications for members.

mortgage market at sustainable margins is achieved through a combination of fast decision making, non-standard products and criteria, and a strong and efficient broker proposition. Some common examples of barriers to adopting the latest technology:

Legacy debt blocking innovation – Legacy systems are a widely acknowledged issue in the sector, with more than 90 percent of firms relying on legacy in some form. This has left financial institutions with siloed systems with low scalability and high costs. If building societies do nothing, legacy debt will continue to be a blocker for innovation and financial growth, costing them members and revenue.

Tight budgets – These will remain for as long as there is operational complexity. The key is spending to simplify and increase efficiency to expand investment budgets.

Attracting the best talent – The acceleration of digital transformation requires upskilling in-house resources and changing culture to digital first. Thus, institutions must define how to compete in attracting, developing and retaining talent with multinationals and tech companies offering the latest technology infrastructure to employees.

Compliance and legislation – Increasing regulatory requirements create a large overhead[6] and, paired with already tight budgets, are a challenge for the sector.

The 2025 vision for the digital mutual

The core vision for mutuals is to leverage digital and build on community trust to deliver valuable services to members and colleagues. To achieve this, they must:

Drive efficiency, obtain simplicity – Simplicity is a common target within the sector, and technology is key to reduce the complexity of IT systems and infrastructure. As a result, this will not only streamline operations and business, but also increase efficiency and achieve a lower cost model.

Recover and grow member base – Being customer-centric, mutuals strive to provide them a personal experience. Today, the financial sector is using a new set of capabilities, including digital banking and self-service (e.g., digital channels, chatbots), hybrid branches, policy-based initiatives (e.g., open banking), and data insights on customer needs.[7] Hence, while the traditional branch customer still exists, mutuals must extend their reach to other customer profiles who value a remote, fast, digital approach.

Automate mortgage applications – Members and intermediaries desire speed: fast and simple processes, for instance, when applying or processing a mortgage. Likewise, the sector must adopt processes that allow them to deliver the best experience for members and intermediaries.

Guidance 1: Build a strong foundation

Building societies' leaders look at the cloud as the provider of agility, resilience, cost savings and ultimately as an enabler for their transformation into digital mutuals. All too often, a critical aspect of harnessing the cloud model is overlooked: the impact of IT moving to the cloud. VMware has spent the past 10-plus years enabling financial services' IT departments to adopt cloud operating models.

The first step always begins with the analysis of its IT foundation to ascertain its current state of maturity of its technology, people and processes.

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[6] Whitecap Consulting. "2021 Building Society Sector Analysis." April 21, 2021.

[7] Waracle. "Building Societies – The Land that Digital Forgot?" February 5, 2020

Going through the analysis described in the Guidance 1: Build a strong foundation section enabled a Spanish global financial institution to migrate 74,000 servers from legacy environments, achieving cost savings by on-premises decommission and ensuring the institution was operating very well during the COVID-19 crisis.

Based on this analysis, we developed a maturity matrix (Figure 1) that assesses maturity from culture, teams and skills to governance and operations. The matrix highlights how implementing IT investments cannot happen without an adequate culture change strategy. From there, organisations can determine whether legacy debt, such as mainframe systems, will be strategic for them in 10 years' time, or keep holding them back. If the latter, leaders must learn how to exit from legacy debt, starting with understanding the utilisation of existing infrastructure, such as identifying existing automation levels and areas for optimisation to achieve business automation.

	Reactive		Proactive	Predictive	
	Ad-hoc	Controlled	Service Driven	Business Automation	Optimized ITaaS
Culture	Individualist	Individual objectives-driven	Service objectives-driven	Agile and DevOps mindset driven	Business objectives-driven
Team	No organization /single contributor	Hierarchical	Cross-functional	Highly collaborative cross-team	Self-organizing
IT Skills	Technology aligned	Functionally aligned	Service aligned; Full-stack awareness with specialization	Service reliability and automation aligned	Business awareness
Governance	No governance	Process-driven	Policy-driven	Software-based policy-driven	Exception-driven
Process	None	Manual	Integrated; some automation	Automated	Cognitive capabilities
Release Mgmt	Manual	Manual, process-driven	Pipeline-based	Automated, pipeline-based	Continuous deployment
Monitoring	Ticket-driven	Reactive, alerting-based	Proactive, full stack-based	Full observability, self-healing	Predictive, cognitive capabilities
Provisioning	Manual	Config mgmt.; partially scripted	Blueprint-based, automated, self-service capable	CI/CD Integrated, API-driven	Serverless
Ops Tools & Technologies	Legacy tools with limited effectiveness	Purpose-built tools in isolation	Integrated, purpose-built tools	Leveraging advanced capabilities of purpose-built tools	Cognitive capabilities
		CURRENT SITUATION		GOAL	

Figure 1: A sample maturity matrix from a real-world finance enterprise assessment.

Guidance 2: Optimise and automate

Adopting the approach described in the Guidance 2: Optimise and automate section enabled a European global financial institution to migrate 300 business critical apps off out-of-service-life infrastructure while also removing business-critical apps from the risk register.

Once organisations understand their current and ideal states, they can start building a strategy around their cloud operating model. As the world moves toward a distributed workforce, building societies must facilitate work from anywhere capabilities, providing the best user experience and support to the workforce, including seamless management of remote employees, devices, and applications for administrators. The rise of cybercrime calls for policy-driven security and compliance strategies across the network. Organisations' focus must switch to reducing complexity and driving intrinsic security policies (added by default) to proactively monitor threats on customer and employee data, their edge devices, and branches. Embedded security enables precise risk management and control, and regulatory compliance.

As a next step, organisations should determine their migration strategy. While the term "legacy" sometimes has a negative connotation in software, these systems are often among a business's most mission-critical applications. Few companies are willing or able to simply retire these applications and start over; the costs and productivity losses are too great. Therefore, application modernisation is the most sensible way for building societies to realise the advantage of newer software platforms, tools, architectures, libraries and frameworks, and allow applications to live where it makes the most business sense. In this way, investing in cross-cloud capabilities enables a distributed, heterogeneous world of applications and users across public clouds, datacentres, and edges that institutions can use to power their business. As an outcome, they can expect agility in migrating environments, automation and observability over workloads and security, while also achieving efficient resource allocation.

"Nationwide Building Society has implemented a new Speed Layer as part of its continued investment in innovation and technology. The high-performance system will make data available to Nationwide's Banking App users far quicker than existing systems can achieve today, ultimately making processing times up to 500% faster."

Nationwide Building Society

Guidance 3: Accelerate and scale

The rise of sustainable finance and digital disruption, are, together, challenging building societies on maintaining their competitive advantage. Thus, building societies must provide adequate support for their developer teams to easily build products and services that leverage their core ethical values, and enhance strong relationships with members. Today, some of the strategies used to attract members include targeting channels and features to different customer segments or creating segmented brands, both aiming to build brand loyalty and secure future customers and revenue. For instance, NatWest created Holt's Military Banking to address the needs of the armed Forces.

These type of customer models require a consistent platform for developer teams that features easy-to-use, proactive, full-observability systems, enabling clear repeatable processes for turning new ideas into profitable business models. In turn, it facilitates the delivery of better interfaces for employee applications to avoid the difficulties and ineffectiveness of typical green screen applications. Alongside that, investing in in-house DevOps through an agile culture change will increase developers' productivity and a culture of fail fast through shorter production cycles. Building on a strong foundation of people processes, strong values, and a modern infrastructure with cross-cloud capabilities, building societies must leverage their state-of-the-art capabilities to be the first with the anticipation and delivery of customer needs.

Impact on the business, IT and customers

Mortgage turnaround time – Increasing visibility over mortgage applications and automating processes to remove complexity allows the workforce to dedicate their efforts to more complex cases and simplifies the experience of intermediaries. Thus, organisations can expect a lower period from request to offer and earlier revenue.

Member satisfaction – Once the organisation has the right tools, teams can reduce time to market and regularly deliver new services and features that spike brand loyalty and attract new market share. For customers, accessing applications easily and getting responses quickly increases trust on the provider's ability to adapt and respond to their needs promptly. Brand loyalty is key for member retention and attraction, and ranges from satisfied customers to word-of-mouth or constructive feedback.

Colleague engagement – Automating and simplifying processes and security policies allows to focus on meaningful tasks, reduce exhaustion and increase engagement. Moreover, the flexibility to work from anywhere with a secure and seamless experience creates an empowered workforce. Finally, an agile culture and the right support and tools for developer teams increases productivity. The resulting fast production cycles enable repeated modernisation of employee-facing applications, with consumer experiences similar to customer-facing applications. Employees can better interact and navigate systems and be productive. Nevertheless, being a great place to work goes beyond seamless operations: A foundation based on core ethical values increases employee satisfaction, motivation and engagement.

Climate action – The low carbon journey starts with an analysis of current consumption and a plan to cut emissions. In 2019, VMware helped customers avoid the equivalent of removing 33 million cars from the road by partnering in their digital transformation journeys. As customers increased automation levels and optimised resource allocation, they were able to reduce energy consumption, hardware, and carbon footprints.

Financial strength and growth – During high-demand periods organisations risk system outages, resulting in disappointed customers and lost revenue. With higher control and observability, an organisation can ensure stronger resilience for unexpected events.

Building on that, a fast time to market enables the delivery of new services and updates to revenue-generating apps quickly. In turn, this ensures earlier additional revenue to the business, higher budgets for investment in innovation, and financial growth.

Advice for executing the digital mutual

When forming a digital transformation strategy, there are a few actions to consider from a leadership perspective. To start, it is important to align with the organisation's business strategies and initiatives, informed by the applications and services delivering them. It is also essential to understand, upfront, the journey the organisation will follow, how the capabilities will be delivered, and how the organisation will change to adopt the new operating model. Bringing all this together in a coherent strategy will allow the organisation to proceed, driven by a clear vision everyone can get behind, and delivering quantifiable business value from the outset. The main steps to consider are:

Drivers – Why are we adopting a Digital Transformation? What business benefits will we achieve? Who are the affected stakeholders? How will we measure success? Be clear on what problems you are trying to solve before adopting solutions that may not serve them most effectively.

Analysis – Where are we in our digital transformation journey? What does our future-state architecture look like? What kind of player do we want to be in the financial sector: more of a leader and disruptor, or a more conservative late adopter?

Discovery – How will we get from current to future state? Understand the existing solutions in the market and leverage the knowledge from partnerships with fintechs, technology consultants and partners who can advise you on what best fits your needs.

Enablers – Technology is only ever one part of a solution. Once you identify the right technology tools, develop training plans and mechanisms to get board members, the workforce, and business processes up to speed. No digital transformation can happen without people and processes also transforming.

Delivery

Operations – The delivery of services using modern infrastructure, such as the cloud model, will be different to traditional IT. The methodology will be agile and iterative, delivering smaller more frequent incremental improvements, through automation, everything as code, reusable building blocks, and continuous integration/continuous deployment for infrastructure, services and applications.

Human-technology interactions – Boards should carefully consider how technology and humans interact, whether it involves customers, employees or extended partners.

Leadership – Technology can be transformational. Boards that support a transformation mindset, must pave the way for bold efforts that highlight urgency and priority, what the art of the possible is, and what going in the right direction means for their business.

Why VMware

VMware is the partner of choice for more than 90 percent of the UK financial sector. Wherever the point of need may be, VMware enables financial institutions to modernise IT infrastructure, applications and operations to improve the customer and employee experience online, in person, and everywhere in between. Together, we are transforming IT to safely accelerate digital-first banking experiences while building innovation, agility and resiliency into the core of the organization.

To learn more, visit vmware.com/go/financialservices.

Authors

Beatriz Barbosa
Business Solutions Specialist

bbarbosa@vmware.com

Ian Bundey
Senior Business Solutions Strategist

ibundey@vmware.com

Anthony Burgess
Financial Services Account Executive

aburgess@vmware.com

Financial Services contact at VMware

Brian Hayes
Financial Services Industry Director

hayesbr@vmware.com

Item No: The Journey Toward the Digital Mutual 2/22