AI revolutionizes Inclusion & Profitability for Financial Services

Enabling financial empowerment for the next 300 Mn Indians
Acknowledgements

‘AI revolutionizes Inclusion & Profitability for Financial Services’ is a research report published by Google with Knowledge partner, McKinsey & Company, and Data & Insights partner, Experian Credit Information Company.
Introduction

Reference

‘AI revolutionizes Inclusion & Profitability for Financial Services’ is a research report published by Google, with our knowledge partner, McKinsey and Company which analyzes India’s evolving digital landscape and how people buy financial products today.

The research leverages McKinsey analysis, Google insights, primary research, expert interviews and industry sources to shed light on the future of AI-led digital acquisition in BFSI economy in India. The information included in this report is sourced as “AI revolutionizes Inclusion & Profitability for Financial Services Report 2023”, unless otherwise specified.

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Executive Summary

Potential to acquire the next 300 mn BFSI customers online

- With increasing demand for fast, convenient, on-the-fly processes, investing in capabilities to drive end-to-end digital acquisition is a strategic growth lever
- Even though India has 700 Mn active internet users, even the most well penetrated BFSI categories like UPI and non Jan Dhan bank accounts have only touched 300-400 Mn customers - 300 Mn active online users untapped by financial services

Digital acquisition in BFSI can be driven profitably at scale

- ~90% of BFSI customers start their purchase journeys online today, but only 30% end up buying digitally, leaving a huge untapped opportunity on the table
- LTV-to-CAC ratio is at least 30% better for digital channels in life insurance and unsecured personal lending compared to traditional channels for BFSI products

Building a digital BFSI business requires investment in 5 capabilities powered by AI

- AI-based full funnel marketing to best optimize spends across channels and discover new customer bases on previously untested properties
- Personalized, risk-based omnichannel fulfillment journeys, ensuring seamless “pick up where you left off” experiences across digital and physical channels for maximum efficiency
- Build-Measure-Activate Martech to build a true “Customer One” view across siloed data sources and activate the data to enable personalization at scale
- Measurement and Attribution to establish true omnichannel ROAS measurement
- Digital first org with Agile Operating Model that translates marketing goals to business KPIs
The compelling case for AI-enabled digital BFSI growth
4 key trends setting the stage for at-scale digital BFSI businesses

1. Sustained profitability with significant penetration potential

2. Big shifts in digital Adoption over the last 3-5 years

3. Huge potential (3-5X of current sales) to tap into online demand for financial services products

4. Gen AI has the potential to fundamentally transform digital customer acquisition
Indian banks’ profitability at decade high levels

Indian Banks RoA, % movement from FY’13 to FY’23

Key factors affecting RoA, FY’13-22 trend in India

NIM (Net Interest Margin)

Other income

Opex

Risk costs

Note: SCBs ROA breakdown for FY23 yet to be updated on RBI DBIE. All factors are as percentage of weighted avg. assets during the FY as stated by RBI, weights being the proportion of total assets of the bank as percentage to total assets of all banks.

Source: RBI

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Credit growth in India has been driven by increased retailization.

Credit growth in India for commercial banks (AUM), INR Lakh Crore

Source: RBI, CRISIL, McKinsey Analysis
India remains a credit underpenetrated market, with 50% of the eligible population uncovered.

### Retail credit addressable market, FY22 (Crore)

<table>
<thead>
<tr>
<th>Segment</th>
<th>Addressable Market (Crore)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total population in India</td>
<td>135-140</td>
</tr>
<tr>
<td>Aged below 20</td>
<td>46-47</td>
</tr>
<tr>
<td>Aged above 65</td>
<td>5.5-6.5</td>
</tr>
<tr>
<td>Urban population (low income)</td>
<td>9-10</td>
</tr>
<tr>
<td>Rural population (low income)</td>
<td>32-33</td>
</tr>
<tr>
<td>Customer with low credit score (&lt;650)</td>
<td>13-14</td>
</tr>
<tr>
<td>Potential lendable base</td>
<td>32-34</td>
</tr>
</tbody>
</table>

Some proportion of this segment is eligible for microfinance.

### # Active loans (Crore)

<table>
<thead>
<tr>
<th>Loan Type</th>
<th>Active Loans (Crore)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit card</td>
<td>7.1</td>
</tr>
<tr>
<td>Personal loan</td>
<td>5.8</td>
</tr>
<tr>
<td>Consumer durables</td>
<td>4.1</td>
</tr>
<tr>
<td>2-wheeler</td>
<td>2.2</td>
</tr>
<tr>
<td>Business Loan</td>
<td>1.2</td>
</tr>
<tr>
<td>Total base (ex-MFI &amp; accounting for overlaps)</td>
<td>12-14</td>
</tr>
</tbody>
</table>

1. Assumed average number of cards per customer to be 1.8 (based on expert input)

India has seen big shifts in digital adoption over the last 3-5 years

- **Smartphone users in India**
  - 450 Mn in 2019
  - 100 Mn 5G smartphone shipments expected by end of Q2 2023
  - 650+ Mn in 2022
  - 665 Mn+ unique visitors on Top 10 e-commerce platforms

- **UPI transactions**
  - ~782 Mn in Apr’19
  - ~8,898 Mn in Apr’23
  - with a monthly transaction value of INR ~14 lakh crore

- **Digital penetration in rural India**
  - 85% of farmers have at least one smartphone in the household
  - 55% farmers are active users of social media, while almost 70% use instant messaging apps

- **New to bank digital accounts**
  - 6X increase in Kotak 811 digital accounts during FY19-22 from ~2 Mn to ~12 Mn and contributing ~150% of incremental SA Balance
  - 7.9 Mn new SB accounts through YONO in FY23 (~64% of total) viz a viz ~2.8 Mn in FY19

- **FasTag transactions**
  - 0.4 Bn in 2019
  - ~8x
  - 3.2+ Bn in 2022

- **JAM-tech based Direct Benefit Transfers**
  - 800 Mn Citizens have received Direct Benefit Transfer through JAM-tech (Jan Dhan, Aadhar, Mobile)

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1. Mix of ETB, NTB and Assisted sales (Fully digital PL sourcing: 54% Axis Bank, 40% ICICI); 2. Phygital CC sourcing: 79% for Axis Bank, 98% for ICICI Bank
DPI is unlocking new data sets that enterprises can leverage to innovate at scale

**1. DigiLocker**
- **631 demographic documents currently:**
  - Identifiers (e.g., Aadhaar, PAN)
  - Certificates (e.g., Academic, Residence, Income, Birth, etc.)
  - Financials (e.g., Insurance, UAN)
  - Property (e.g. property certificates)

**2. Sahamati**
- **Bank statements (current / savings acc.)**
- **Income Tax, Pension data**
- **Securities and Insurance data**
- **Past Tax, future invoice data from GSTIN**
- **Non-financial data (health, telecom data)**

**3. Unified Logistics Interface Platform (ULIP)**
- **Access to 1600+ data fields from 7 ministries:**
  - Fastag, Vahan – Transaction, registration data
  - Gatishakti – Highway, state road data
  - LDB – Container tracking, Port information
  - ICGATE, PCS – Vessel, cargo tracking data
  - Sarathi – Driving license information
  - FOIS – Rail Freight tracking data
  - ACEMS – Air Cargo tracking data

**4. Land Records Digitization**
- **Maps and land ownership records digitization (ownership history, parcel ID #, geo location, digital maps)**
- **20+ states have completed 90%+ digitization**
- **10+ states have established apps/APIs to access digital ownership records using APIs**

**5. AgriStack**
- **UFID – Unique farmer ID with:**
  - Electronic Farm records
  - Land ownership, Land records
  - Production details (Crop sown registry)
  - Financial details
  - Farmer identifiers (Aadhaar, etc.)
  - Directory of industry standards, regulations, products, entities across the Agri Stack

**Agriculture Data Exchange (DeX):**
- Soil health, weather data
- Crop data (Yield, EXIM, production, etc.)
- Historical prices, Real-time mandi data

**Other ready to access data includes:**
- Latest research from Agri universities
- Integrated data across all govt schemes

**Stack Under development; Data access via consent managed API link to UFSI, DeX**

Source: Digilocker, ULIP website, Agristack website, press search
Untapped potential of 300 Mn users

Even the largest BFSI categories cover only 300-400 Mn users of 700 Mn active internet users

Source: RBI, NPCI, IRDA data, Google, Temasek and Bain, India e-Conomy Report 2023
3-5X online demand vs. BFSI unit product sales in FY22

3-5X online demand vs. BFSI unit product sales in FY22

Total indexed online demand as a factor of total unit sales per product

• The annual online search interest for financial products and services has far outgrown the actual sales converted in each category across all channels – digital and physical included.

• Our research indicates that 87% of customers who buy any FS products start their journey online, and most customers undertake 1-2 unique searches on each product category before they decide to purchase.

Source: Google Internal Data, McKinsey Analysis
There are 4 categories of BFSI products based on online demand maturity

- Established digital products are those that have tapered in online demand growth rate, yet the volumes are substantial and sizeable share of the online demand is brand specific

- High potential digital products continue to show high online demand growth, but brand search is still relatively low

- Emerging products are those where significant exploration has started online, especially for price and feature comparison

- Laggards are products where high intent brand demand is much lower and this presents an opportunity for online category creation by leading players

Source: Google Internal Data, McKinsey Analysis
Beyond the FS horizon: Huge untapped potential in allied categories

- In most BFSI category, the BFSI purchase being made is the secondary purchase to support another primary decision. For instance, customers first decide their travel destination, book tickets & then look at purchasing a travel insurance.

- Most BFSI players have not explored "allied categories" beyond the core keywords liked to their products
Potential to tap into online demand from allied categories across sectors

**Online demand for travel is much higher than that for travel insurance**

- Travel Insurance
- Travel
- Low: 100-150x
- High

**Online interest in the broader theme of investments is much higher than that for specific stocks or mutual funds**

- Stocks, Mutual Funds
- Stocks
- Mutual funds
- Low: 10-15x
- Med
- High: 200-250x

CAGR of search volumes between 2019-2022

Source: Google Internal Data, McKinsey Analysis
Gen AI has the potential to fundamentally transform industries, value-chains and the way work gets done.

Across banking industry, technology could deliver value equal to an additional $200 billion to $340 billion annually if the use cases are fully implemented.

Generative AI has the potential to change the anatomy of work. Workforce transformation will accelerate, given increases in technical automation.

Gen AI is uniquely able to handle ...

1. **Insight extraction**
   - Rapidly search large corpuses of text and identify relevant answers

2. **Content generation**
   - Develop complex documents and messages tailored to specific context

3. **User interaction**
   - ‘Out-of-the-box’ human-like conversational ability incl. context memory

Building at-scale, profitable digital BFSI businesses
Our survey indicates that the purchase journey for financial services products today is driven by digital touchpoints.

- **Major online touchpoints:** search, online videos, reviews
- **Major offline touchpoints:** store, agent, offline ads
- **Mix of multiple online and offline touchpoints are used for exploration**
- **Social media & search are most-used**
- **Online search & expert interaction are found to be most-helpful**
- **Majority find online channel to be the most helpful in comparing alternatives**

**Key highlights of the purchase journey:**
- **87%**
  - Start exploring online; 22% of which start with search engine
- **90%**
  - Use one or more online channels for exploration
- **40%**
  - Use search to take purchase decision; 31% use online videos
- **2/3rd**
  - Consumers find online channels to be most helpful in evaluation
- **65%**
  - Digital buyers would buy again from the same brand; <7% would switch to offline purchase

- **1/3rd**
  - Online-only researches still purchase offline

**Source:** Google x Kantar, Shopper Pulse Research, India, May 2023, Sample Personal Loan n=302 Life insurance n=302
Detailed bottom-up cost teardown analysis conducted to compare channel efficiencies

Sources of Insight
- Google Platforms data across BFSI products
- Proprietary Google Surveys across 5K+ BFSI customers in India
- Asia-wide Personal Financial Services surveys conducted by McKinsey and Company over last 5 years
- Expert interviews with digital marketing leaders in BFSI in India
- Credit history assessment across customer acquisition channels by Experian

We evaluated 3 key metrics across products:

1. **LTV**
   - Lifetime value of the customer through the AUM and profits (e.g. interest)

2. **CAC**
   - Customer acquisition cost including all variable costs across the funnel

3. **Quality**
   - Stickiness, default rates

Factors considered for measurement against each metric:

- **For digital:**
  - Average Ticket size (ATS) for the product within the channel
  - Cross-sell and re-purchase rates

- **For physical:**
  - Commissions as per industry standards

We have built detailed models over a product lifetime of 5 years and conducted a full sensitivity analysis with metrics such as ROI, tenure etc. to derive these insights.

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2 product categories evaluated to observe the profitability and customer portfolio quality

We identified two product categories to observe the underlying profitability drivers of digital business:

1. **Life insurance**
   - Typical purchase behavior: Trust-based purchase
   - Conversion cycle: Over 6 to 12 months

2. **Personal loans**
   - Typical purchase behavior: Trigger-based purchase with focus on best rates and disbursal time
   - Conversion cycle: Immediate and short-term purchases

Key findings for digitally acquired customer portfolios across the two product categories:

- **Life insurance**
  - Lower customer acquisition cost (CAC) by best-in-class players (20–30%)
  - Better lifetime value (LTV) versus traditional channels owing to higher engagement and thus more opportunities for cross-sell & up-sell (30–40%)
  - Higher ROI i.e. LTV-to-CAC ratio for digital versus traditional channels (1.3–1.5X)

- **Personal loans**
  - Early indications of portfolio quality (i.e., persistency and NPAs) suggest better quality digital portfolios vs. physical channels

Life Insurance: 30% higher ROI customers in digital portfolio

Optimized at-scale digital players have a 30% higher LTV/CAC\(^1\) over physical channels

Typical persistency rates of digitally acquired customers is 10 to 15% higher in first two years and ~25% higher in years 3 and 4


1. Over a lifetime of 5 years
Life Insurance: 3 key factors drive better quality of digitally acquired portfolio

Customer driven/ DIY
- Self-driven purchase and renewals journeys
- Re-imagined digital journeys enabling the exploration and purchase online
- Reduced documentation and STP approvals

Better Engagement
- Direct association with brand entity
- More understanding of customer patterns and behavior
- Better engagement for cross-sell, autopay, etc.

Improved customer experience
- Many DIY servicing options e.g., self tax form download via Whatsapp
- Campaigns customized according to customer behaviour

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Personal Loans: 50% higher ROI customers in digital portfolio

~1.5X LTV/CAC for digital channels compared to physical channels for NTB customers

Higher the ROI and tenure, the more attractive the digital channel becomes vs. the physical channel metrics

LTV/CAC over a lifetime of 5 years (ratio)

- LTV is generally higher for physical channels driven by a higher ATS, the higher ratio is driven by a far lower CAC – fully loaded digital CAC for a best in class at-scale player is 70% less than the CAC for physical acquisition
- For select sample portfolios from the bureau across players, the NPAs from the digital portfolio for NTB customers for banks are lower than NPAs for physical customers; the average credit score for digitally acquired customers are also 3-50 points higher

Sensitivity analysis for ROI and tenure

Personal Loans: 3 key factors drive a better quality digital portfolio

Deep integration with ecosystem partners, including at point of sale
- With wide range of partners including for non emergency needs like travel
- Integrations with broader partners like credit bureaus and loan aggregators

Focus on key customer pain points – TAT and interest rates
- Many players have come up with propositions like instant PL in seconds
- Interest rates for online are not higher than offline – customer trust has been built

AI-based full funnel marketing
- Several banks have set up trigger based marketing e.g., targeting for PL based on FD breakage
- Personalized re-approved offers even for NTB customers
5 AI capabilities that BFSI players should invest in
5 capabilities to build a digital BFSI business

Key business outcomes expected:

- **120-165%** conversion rate improvement
- **2-3X** new accounts acquired through funnel and landing page optimization
- **30-40%** AdTech cost savings through consolidation
- **15-30%** increase in revenue from cross-sell
- **20%** spend efficiency improvement
- **3-6X** improvement in speed to value capture through agile org. structures

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**1. AI-powered full funnel marketing**
- Search
- Non Search Performance
- Brand building
- Apps

**2. Digital fulfilment from lead to sale**
- CRO
- UI / UX

**3. Build Measure Activate MarTech**
- Customer Data Mgmt. (CDP)
- 1P Data Optimization

**4. Measurement and Attribution**
- Unified dashboards, KPIs and reporting
- Adopting Advanced Omni ROI measurement and attribution model

**5. Agile operating model**
- Agile ways of working
- Aligned full funnel KPIs with right attribution models

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Several industry leaders have started building these capabilities and are seeing the impact on their digital businesses

1. **AI-powered full funnel marketing**

   Tata AIA Life Insurance adopted DV360 based full funnel marketing with a 3.1% relative lift in brand awareness and a 10-16% incremental brand search uplift.

   Axis Bank used full funnel marketing and Ads Data Hub to measure the impact of branding campaigns across channels to achieve increase in 267% search lift and 18% increase in organic new users.

   HDFC Ergo achieved +1.8x revenue and +49% higher ROAS using a fully automated search strategy with broad match and RSA.

   TATA AIG drives +126% higher ROAS and +8% higher Revenue with value based bidding on Search, and Performance Max.

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Several industry leaders have started building these capabilities and are seeing the impact on their digital businesses.

<table>
<thead>
<tr>
<th></th>
<th>Digital fulfilment from lead to sale</th>
<th>Growww has built end-to-end digital native journeys based on insights from customer behaviour on search to drive higher engagement with high LTV customers</th>
</tr>
</thead>
<tbody>
<tr>
<td>2</td>
<td>Build Measure Activate MarTech</td>
<td>Bajaj FinServ used Discovery ads with its first party data. It generated leads at a 51% lower cost, and improved the cost of eligible leads by 19%</td>
</tr>
<tr>
<td>3</td>
<td>Measurement and Attribution</td>
<td>Max life saw 2x Improvement in ROAS attribution after moving to omnichannel attribution from digital only attribution</td>
</tr>
<tr>
<td>4</td>
<td>Agile Operating Model</td>
<td>Star Health has built a close collaboration between the CMO and CFO’s office to drive full funnel attribution and optimize spends across channels</td>
</tr>
</tbody>
</table>

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