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Digital players in the financial sector: a step towards profitability?

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GENERAL SUMMARY

The purpose of this third study, conducted by the Autorité de contrôle prudentiel et de résolution (the French Prudential Supervision and Resolution Authority - ACPR), and focusing on financial players and intermediaries providing services online or accessible through 100% mobile applications, is to characterise their business models and assess their profitability in relation to their business strategies. It also provides a better understanding of the positioning of these players in the market for banking and financial intermediation, the nature of their relationships with traditional banks and thus the degree of change in the banking landscape in France.
When compared to the two previous editions[1], this study is characterised by three developments.

First, it aims to assess and update the positioning of the different players with regard to their break-even point and the conditions needed to reach this threshold. The situation remains mixed, however. It seems that some of the players, especially those who are not part of a banking group, either are already profitable or they claim they can reach their breakeven point by 2022-2023. This is due to better cost control and to the greater specialisation of their business.

Second, the study pays particular attention to the impact of the Covid-19 crisis, as well as the impact of the interest rate environment on profitability and industry developments.

Finally, the study focuses on the emergence and evolution of strategic partnerships between market participants, developed to broaden the offer of financial products and services to clients of these institutions.

In this study, the term "digital financial players" refers to financial players and intermediaries offering banking or payments services available online or accessible through 100% mobile applications. The development of these players is driven by technological progress and the use of new digital technologies. While entry into the banking market is particularly difficult in a situation where traditional banks have been able to capitalise on their experience and reputation to build customer loyalty, these new players have nevertheless managed to establish themselves in this market in a sustainable manner, in some cases with a sharp increase in their customer numbers.

Digital players in finance have different business models or legal forms and offer a wide variety of services and product ranges. In order to clarify the outline of the survey and to give a more precise analysis of the determinants of their profitability, during the summer of 2021, the ACPR conducted a survey on a sample of 15 institutions, most of which had already participated in the previous studies: Boursorama (Société Générale Group), BforBank (Crédit Agricole Group), Hello Bank (Groupe BNP Paribas), ING Direct (Group ING), Monabanq (Groupe Crédit Mutuel Alliance Fédérale - CIC), Orange Bank (Groupe Orange), Ma French Bank (Groupe La Banque Postale), Nickel (Groupe BNP Paribas), Qonto, N26, Fortunéo (Credit Mutuel Arkéa Group), Revolut, Manager.one, Lydia and Younited Credit[2].

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[1] See: (1) BEAUDEMOULIN N., BIENVENU P. and FLICHE O. (2018), "*Études sur les modèles d'affaires des banques en ligne et des néobanques*", Analyses et Synthèses, Autorité de contrôle prudentiel et de résolution, no. 95, October. https://acpr.banque-france.fr/sites/default/files/medias/documents/20181010_etude_acpr_banque_en_ligne_neobanque.pdf

And (2): CLERC L., MORAGLIA A. and PEYRON (2020), "*Les néobanques : des acteurs en quête de rentabilité*" Analyses et synthèses, Autorité de contrôle prudentiel et de résolution, no. 113, https://acpr.banque-france.fr/sites/default/files/medias/documents/2020_etude_neobanques_as.pdf

[2] Moreover, some institutions contacted by the ACPR, such as Treezor, did not follow up on the ACPR's invitations and surveys.

In the second part of 2021, the survey was then supplemented through bilateral discussions with all of these institutions. The focus was more particularly set on the breakeven point and the impact of the low interest rate environment.

Most of these players directly depend on the traditional banking sector, either because the traditional banking sector acquired the business after a few years of existence, or because they were developed in-house within those groups to counter the emergence of new players or to compete with new offers. This reliance on the traditional banking sector is highly structuring, both in terms of the determinants of profitability, and for the offer of banking and financial products and services.

The digital finance players involved in this study saw a significant increase in their market share in 2020 compared with previous years. For example, the number of their customers doubled between 2018 and 2020. About 16 million customers had an account open with one of the institutions in our sample at the beginning of 2020, compared with 8 million at the beginning of 2018. As regards the opening of new accounts in France, at least 35% of the new current accounts opened by retail customers in 2020 were opened with one of the institutions included in our sample.

In terms of business models, this study identifies two main types of players. First, generalist players, who offer a wide range of financial products to a diverse customer base; second, specialised ones, who do not offer such a wide range of products and services, and rather focus on a narrower customer base while being positioned in market segments that are considered more profitable. Another characteristic of the business models is that of a shift in the composition of the customer base, with a growing share of young customers and a declining trend in the relative share of executives in both existing and new customer numbers.

Thus, on an aggregate level, the strong growth in the number of customers in 2020 is not associated with improvements in operating profitability: net banking income (NBI) is growing at an insufficient rate with respect to overhead costs that remain too steep. The downward trend for premiums paid to customers is not enough to halt the decline in NBI per customer, even if the extent of that decline is limited.

Since the previous study, the two major trends observed in this market are: i) the significant growth of services to businesses, delivered either directly to customers or in "business to business" (B2B) mode, and often coupled with invoicing on a per-use basis[3] as part of credit or payment solutions marketed under a white label, and ii) since the Covid-19 crisis, a high demand for specific financial services such as fractional and deferred payment services (BNPL)[4], which has led the market to prioritise the development of the product offer towards this type of services.

The health crisis and lockdown measures decided on in the first half of 2020 had a limited impact on institutions' business and risk costs. Most market participants experienced in 2020 the resilience of their business model, as the health crisis confirmed the relevance of models based on a remote banking relationship with digital tools (integrated platforms, 7-day customer service) that allowed customers to become more autonomous in their day-to-day banking operations. Moreover, products have not suffered any particular shock, thanks to the dynamism of online commerce and the rise of contactless payment, especially for very small transactions.

[3] Corporate-to-business products or "business-to-business-B2B" are services activities targeted at corporate customers.
[4] "Buy Now Pay Later" refers to the set of solutions that allow consumers to pay for their purchases in a deferred and/or fractioned basis (in several instalments). A third party (Fintech, credit institution, etc.) pays the merchant the full amount of the purchase immediately, in exchange for a fee paid by the purchaser and/or the seller.

Lastly, in terms of methodology, it should be noted that this study is based on a collection of *ad hoc* statistical data, the quality of which was poor for some of the surveyed institutions. Coming from digital players, this might come as a surprise, insofar as the knowledge of customers and their data are key to strategic development and profitability. However, the voluntary nature of this exercise, the strategic dimension of the data required and the institutional organisation and risk governance within some of these banks undoubtedly explain this situation. Moreover, some institutions contacted by the Authority did not follow up. Overall, it is essential to improve the quality of information, both for the sake of customer protection, and with a view to a financial stability.

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CONTENTS

Introduction

This work focusing on digital financial players, carried out by the Research and Risk Analysis Directorate in collaboration with the ACPR's Fintech-Innovation Unit, builds on two previous studies published in 2018 and 2020 focusing on the emergence of financial players and intermediaries offering services online or accessible through 100% mobile transactions.

It relies on two questionnaires, one of them quantitative and the other qualitative, both sent to 15 industry players. The purpose of the questionnaires was to provide as accurate a picture of the market and its trends as possible. Additional information was then collected from participants in bilateral interviews. Compared with the previous edition[5], the sample used in this study partially changed with a view to reflect market developments. First, we observed the repositioning of some market participants towards market segments considered more buoyant. Second, the tendency of large banking groups to acquire or develop in-house fully-fledged legal entities operating in the field of 100% online banking has continued. Third, we have integrated a number of digital intermediaries (excluding large groups) with a 100% digital offer. Some of them target specific customers, while others are specialised in offering financial products or services. Finally, we also sought to take into account new market trends marked by the rise of players who carry out non-banking operations.

In an increasingly competitive environment, where profitability remains to be achieved for most players, some have decided to withdraw from market segments such as the collection of deposits from the public, and focus on seemingly more profitable sectors. This is the case for two actors who were included in the previous edition but are excluded from the present one: Ditto and Carrefour group. Carrefour group and BNP-Paribas group decided to discontinue C-Zam, their traditional banking offer, in July 2020. Carrefour closed its current accounts to focus on credit cards and consumer credit with its Pass offer. The reason for this decision is, on the one hand, the lack of attractiveness of the offer (number of customers far below target[6]) and, on the other, a customer service that customers themselves deemed underperforming. Former C-Zam customers have been offered a compensation offer from Nickel, a member of the BNP-Paribas group. With regard to Ditto, an initiative launched by Travelex in 2018, competitive pressure did not allow it to remain on its original market, a high-end segment targeting the upper-income bracket. In February 2020, Ditto decided to drop its offer

[5] https://acpr.banque-france.fr/sites/default/files/medias/documents/2020_etude_neobanques_as.pdf
[6] https://www.capital.fr/votre-argent/carrefour-va-supprimer-son-offre-c-zam-et-propose-un-compte-nickel-en-echange-1369935

to focus on services to businesses[7]. Finally, ING Banque, the French subsidiary of the Dutch group ING, also decided to withdraw from the French banking market due to high competition coupled with low[8] profitability. ING Banque, which was still in operation in 2020, was included in our sample.

Secondly, all major French banking groups remained very active in the online banking market. In recent years, this has led them to expand their offer and acquire online banks, as well as to develop not only online brands but also offers by fully-fledged legal entities. To keep up with this trend, we included in our sample BforBank, an online bank that is 50% owned by Crédit Agricole's regional banks, and 50% owned by Crédit Agricole S.A., but we have excluded from the sample EKO, another offer from the same group. Similarly, we included Fortunéo, the online bank belonging to Crédit Mutuel Arkéa, in the sampled used for this study[9].

Thirdly, the study includes digital players with a 100% mobile offer that do not belong to one of the major French banking groups. Such players include Revolut, an online bank that develops new products based on a rather limited range of services, as well as Manager.one, an online bank with a range of products specifically tailored to SMEs, TPEs and self-employed workers. Finally, we added two players that operate in a partially different line of business from other sampled players, but who illustrate new market trends: Lydia, a mobile payment platform, and Younited, a credit institution specialising in consumer credit.

Table 1 Studied sample

Participants in this study	Parent banking group if applicable
Lydia	
Manager.one	
Younited Credit	
BforBank	Crédit Agricole Group
Boursorama	General Company Group
Fortunéo	Arkéa Group
Hello Bank!	BNP Paribas Group
ING Banque	ING Group
Ma French Bank	Bank Postal Group
Monabanq	Crédit Mutuel Group Alliance Fédérale - CIC
N26	
Nickel	BNP Paribas Group
Orange Bank	Orange Group
Qonto	
Revolut	

[7] https://billetdebanque.panorabanques.com/actualites/la-neobanque-ditto-bank-ferme-ses-portes/
[8] https://www.ouest-france.fr/economie/banques-finance/la-banque-en-ligne-ing-quitte-la-france-quelles-solutions-pour-les-clients-06dc1c0c-72c1-11ec-aa63-d4f0e90a3def
[9] BforBank and Fortunéo had participated in the first edition of this study (https://acpr.banque-france.fr/sites/default/files/medias/documents/20181010_etude_acpr_banque_en_ligne_neobanque.pdf) but not in the second one.

The market structure of digital financial players

1. The evolution of the banking intermediation function and the positioning of digital financial players

New information technologies have profoundly transformed our daily lives. Over the last few years, the ways of making and paying for purchases, carrying out financial transactions, managing portfolios and bank accounts have all undergone profound changes. The growth of the digital economy has also resulted in a transition from of a supply-side logic, where financial services were offered by intermediaries to their customers, to a demand-side logic, which is more focused on the needs of the customer and where financial products and services are directly accessible to customers, via IT applications available on smart phones or digital tablets, without necessarily having to rely on "physical" access to an intermediary or financial advisor.

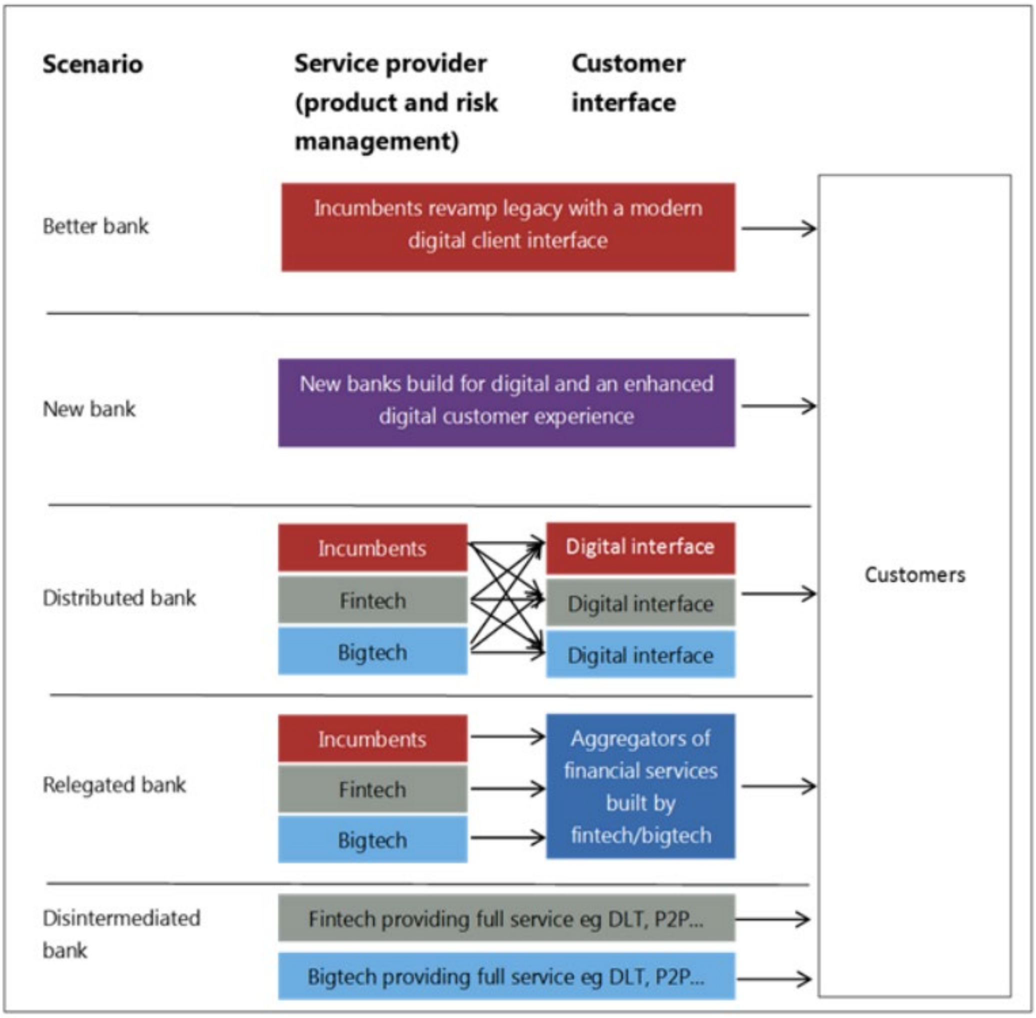
Chart 1 below, drawn from work done by banking supervisors under the aegis of the Basel Committee for Banking Supervision in 2018, presents several possible scenarios for the transformation of the banking landscape.
These different scenarios for the transformation of the banking intermediation function fall between two extreme cases. One of these extremes is a scenario in which the traditional banking system takes full advantage of new technologies and adapts to changing customer needs, to extend its offer of traditional financial services and products online, or even to offer purely digital applications.

The other one corresponds to a scenario where traditional banks have completely disappeared, to the benefit of fintechs or Bigtechs[10] offering a full range of financial applications and allowing direct transactions between individuals (P2P), including the settlement of transactions or investments in crypto-assets. In this context, banking services are being "dismantled" to be offered on digital platforms. These platforms aim to lower intermediation costs by creating competition among providers willing to offer their financial services. This market structure tends to favour the side of the market presenting the highest price elasticity, usually the consumer, hence many free or even subsidised sign-up offers, for example through the payment of a premium.

The trends observed in our previous reports continue. They show in particular the considerable adaptability of traditional banks, as online banking becomes more widespread and new players are almost systematically bought out. For example, several players in our sample were either directly created or acquired by traditional banks: such is the case for Fortunéo (Crédit Mutuel Arkéa), Boursorama (Société Générale Group), Hello Bank! and Nickel (BNP Paribas Group), ING Banque (ING), Ma French Bank (Banque Postale Group), Monabanq (Crédit Mutuel Alliance Fédérale - CIC Group), BforBank (Crédit Agricole Group).

[10] BigTechs are large companies from the technology sector (IT, telecommunication) that expanded to provide direct financial services, or to provide products that are very similar to financial products.

Chart 1 Scenarios for the transformation of the banking intermediation function



Colour code: maroon indicates incumbent banks; purple new players; grey fintech companies; and blue bigtech companies.

Source: Basel Committee for Banking Supervision (2018): "Implications of changing financial technology for banks and banking supervisors", February. https://www.bis.org/bcbs/publ/d431.pdf

There are also a number of offerings from natively digital players proposing limited banking services (current account, credit card, cash withdrawals and credit transfers), such as Revolut and N26. Then come specialised fintechs offering payment services such as Lydia, or offering niche products, but directly competing with certain segments of traditional banking, such as Younited Credit, an online credit institution that uses its platform to offer consumer loans, or Qonto and Manager.one, which specialise in financing professionals and businesses.

Lastly, Orange Bank, an offshoot set up by Orange Group in an effort to diversify its activities, is closer to the BigTechs model. However, unlike the latter, Orange chose to take out a banking licence and to develop this activity by relying on the network of its commercial branches.

These new competitors also contribute to lower transaction costs and to the spread of new technologies in the financial sector.

2. Key figures of the online market

Digital players in the financial sector included in this study saw a significant increase in their market presence in 2020 compared with previous years.

The number of their customers doubled between 2018 and 2020. About 8 million customers (exclusively retail, comprising individuals and SMEs[11]) had an account open with one of the institutions in our sample at the beginning of 2018. This figure rose to 11.5 million at the beginning of 2019, and reached around 16 million customers at the beginning of 2020, i.e. a 100% increase over a two-year period. By comparison, the total number of retail accounts with the six major French banking groups stood at 74 million at the beginning of 2020.

Digital finance players have thus succeeded in strengthening their market share through an increasingly comprehensive product offering, favouring customer autonomy in the fields of everyday banking and savings products, as illustrated in the remainder of this study.

As regards the opening of new accounts in the institutions included in our sample, 4.7 million accounts were opened in the course of 2020, including 2.9 million current accounts. These figures can be compared with the 5.5 million new current accounts opened by retail customers with the six main French banking groups in the same year.

Table 2 New customers and number of account openings with digital institutions included in our sample, 2018-2020

	New customers	Accounts opened	Of which current accounts
2018	3,035,093	3,434,522	1,485,321
2019	4,229,122	4,733,965	3,160,625
2020	4,246,193	4,719,015	2,891,735

Source: ACPR, using data from questionnaires.

It appears therefore that about 35% of the new current accounts opened in 2020 were opened with one of the digital players included in our sample.

These results reflect the effectiveness of the customer acquisition strategies implemented by digital financial players, which remained highly dynamic despite a slight decline in the number of current account openings compared with their 2019 level, when 3.2 million current accounts were opened (-8%). This decrease was partly offset by a 16% increase in other types of accounts, mainly savings accounts, sustainable development accounts and securities accounts. This trend seems to mark the beginning of a second phase in the development of these players, namely that of multiple equipment.

[11] Deposits taken into account in this study are "retail deposits" exclusively, as defined in Article 3 of the Delegated Regulation of the European Union on the liquidity coverage requirements for credit institutions. According to this definition, retail customers include individuals and some SMEs. For more details, the full contents of the Regulation are available at https://eur-lex.europa.eu/legal-content/FR/TXT/PDF/ ? uri=CELEX:32015R0061&from=FR

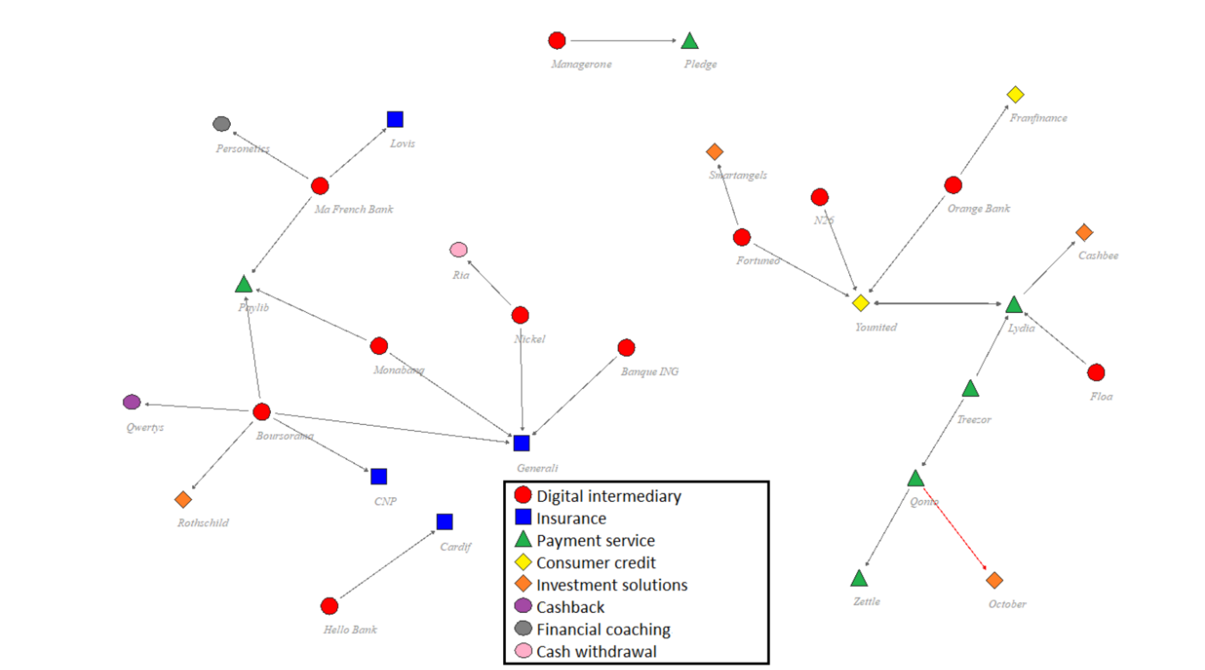
Characterisation of the business models of digital finance players

1. Diversification of the offer through partnerships

A major market development in recent years has been the diversification of the offer through the development of strategic partnerships. Subsidiaries of major banking groups are able to offer a wide range of banking and financial services developed within the group and offered to customers in its branches. New digital players (payment institution, etc.), could not offer the same range of services to their customers at the time of their creation because of their status.

In order to grow in a highly competitive environment, partnerships have been formed with firms holding complementary authorisations, thereby enabling new players to broaden the range of services offered to their customers. The resulting network reflects a market in which interdependencies and complementarities are created not only within groups, or between business partners, but also between competitors themselves. Chart 2 shows the structure of this network, reconstituted based on public information.

Chart 2 Map of the network of digital finance partners



The chart has been designed using public data only. We have excluded intra-group partnerships, bank card partnerships and partnerships with BigTechs from this map.

Graph 2 is not exhaustive: it was designed relying on the information published by market participants and does not take into account intra-group partnerships (in particular links with parent companies) or those with banking card networks and BigTechs. With regard to the last two cases, since the offer is concentrated around a few key players (Visa, Mastercard or American Express) or payment systems offered by BigTechs (such as Apple-Pay or Google-Pay), these services are integrated in almost all offers. Overall, the chart shows that a digital intermediary (red dot) can rely on a payment institution (green triangle), offer credit insurance to its customers (blue square) and, at the same time, offer them investment solutions (orange diamond), a financial coaching service (grey ellipse), or consumer credit products through a partnership with a specialised institution (yellow diamond).

These offers and services of financial products are usually directly accessible online on the website of the digital actor or on programming interfaces (APIs) for the customers of the intermediary in question.

In addition, these partnerships offer new players the opportunity to develop important synergies by allowing them to outsource certain procedures or services. For example, the constant search for attractiveness to prospective customers has led several online banks to invest in the digitisation of their account opening procedures, by collaborating with technological partners for the remote digital identification of the customer and the automated verification of account opening documents.

2. Broadening of the offer and specialisation of players

An analysis of the evolution of customers and products offered by digital intermediaries allows for the identification of certain trends.

Within our sample, we can distinguish two main types of players: generalist players, who offer a wide range of financial products to a diverse customer base, and specialised players, who do provide a full range of offers and services to a wide customer base, but rather are positioned on seemingly more profitable market segments.

The "generalist" player group consists mainly of online banks belonging to major banking groups. They offer a wider range of products, usually corresponding to financial products and services offered to customers at branches. The 100% digital players who do not belong to major banking groups offer a much more limited number of services and products to their customers, but they stand out from competition thanks to highly innovative services and an ability to market these services by integrating them into highly sophisticated marketing packages. The observed trend is moving towards an extension of the range of financial products and services offered by these specialised players.

We categorised the various financial products and services into 19 categories[12] and we find that, on average, participants from a large group offered 12 out of the 19 products and services listed to their customers in 2020. At the same time, participants that do not belong to a group offer only seven products and services on average. Moreover, while in 2019 only five out of 15 institutions offered property insurance services, there were seven in 2020. Similarly, only two institutions offered brokerage services in 2018, compared with four in 2020. In 2018, brokerage services on listed products contributed on average 15% of net banking income (NBI) of the participants in our study.

[12] Life insurance, property insurance, personal insurance, overdraft credit, consumer credit, housing credit, current accounts, credit card, cash withdrawal, checkbook, PSD 2 initiation and information, securities account, brokerage services, mobile payment, crypto products, regulated savings accounts, "non-regulated" savings accounts, non-financial products.

Its relative contribution to NBI has since increased to 20% in 2020. Finally, consumer credit was offered by eight players in 2018, nine in 2019 and ten in 2020.

More generally, product offering remains an important factor of differentiation. For example, those in our sample who are not members of a large banking group, and in particular those that do not have a banking licence, are more specialised in innovative products such as cashback, investment in crypto-assets, or the possibility of operating on the foreign exchange market. These players are still not very active in the field of savings services (regulated and unregulated savings accounts), insurance products, especially life insurance, and credit products. These products remain mostly the prerogative of traditional online banks. Table 11 in the Annex provides details on the product range of the institutions included in our sample.

3. Specialisation by Socio-Professional category

The second line of analysis distinguishing generalist players from specialised players is the composition of their customer base and its breakdown into the various socio-professional categories (SPCs). In recent years, due to the health crisis, generalist players have accelerated their expansion to segments of the population that were previously excluded or underrepresented. Indeed, the first online banks mainly targeted customers with a high savings capacity, such as executives and retirees.

Thus, the search for new customers started with younger and less well-off customers.

Table 3 Distribution of digital intermediaries' customers by SPC

Socio-Professional Category	2018	2019	2020
Executives	28.4%	26.2%	24.8%
Employees	25.8%	27.1%	28.3%
Students	3%	3.2%	9.5%
Retirees	10.3%	9.9%	9.1%
Intermediate occupations	4.2%	4.2%	4.1%
Labourers	1.6%	1.6%	1.5%
Unemployed	16.7%	16.2%	16.1%
Craftsmen and merchants	6.3%	6.6%	6.9%

Source: ACPR, using data from questionnaires.

Table 3 shows the evolution of the customer base of the players included in our sample.

The least-represented SPCs are farmers (0.1%), workers (1.5%) and intermediate professions (4.2%). The share of executives in these groups' respective customer base remains very high, but its relative share has decreased between 2018 and 2020, along with that of retirees. These two categories with high savings capacity have been joined by younger and less well-off customers. The share of employees grew from 25% to 28%, while the student segment has strengthened significantly, from 3% to 9.5%.

This latest development probably reflects the introduction of dedicated formulas specifically targeting this type of customer, as can be seen from the analysis of the evolution of the age of the customer base.

This analysis (Table 4) shows a gradual rejuvenation of the customer base. Customers aged 18-29, who represent more than 50% of new customers, see their market share increase by more than 12 percentage points between 2018 and 2020.

Table 4 Breakdown of customers by age group

Age	2018	2019	2020
<18	3.4%	2.9%	2.9%
[18-29]	26.8%	34.3%	39.2%
[30-39]	23.6%	23.3%	23.1%
[40-49]	17.4%	15.6%	14.3%
[50-59]	13.7%	12%	10.6%
[60-69]	9.5%	7.5%	6.3%
>70	5.7%	4.3%	3.5%

Source: ACPR, using data from quantitative questionnaires.

Comparing these figures with those of the banking sector as a whole yields particularly interesting results. Table 5 shows the socio-professional categories in which digital players specialise over traditional banks. The comparison is made for the year 2018, the most recent date for which we have data on the banking sector. Among the digital intermediaries' customers, executives, employees, as well as the unemployed and students are overrepresented. Three categories remain particularly underrepresented: intermediate professions, labourers and retirees.

Table 5 Comparison between traditional banks and digital players in terms of SPC (existing customers)

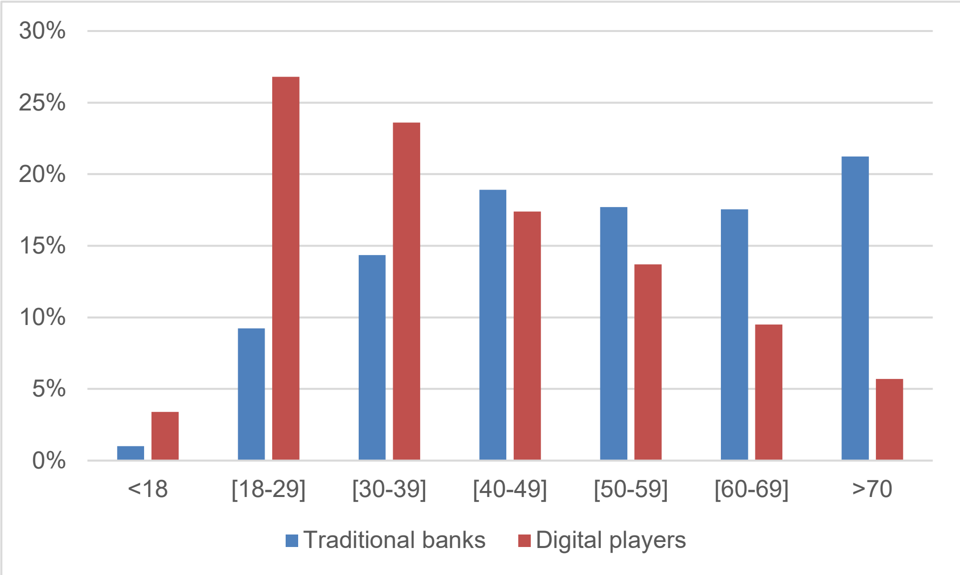
Socio-Professional Category	Traditional banking	Digital players
Executives	11.68%	28.20%
Employees	13.35%	25.70%
Unemployed	2.51%	16.70%
Students	0.85%	7.10%
Craftsmen, Merchants and Business Managers	5.31%	6.30%
Farmers	1.22%	0.20%
Intermediate Professions	14.22%	4.20%
Labourers	13.35%	1.60%
Retirees	36.96%	10.30%

Sources: Enquête Patrimoine 2017-2018, INSEE-BDF, for the traditional banking sector. ACPR, using data from questionnaires.

In addition to the specialisation in terms of socio-professional categories, Chart 3 also shows very clearly that, compared to traditional banks, digital players target younger customers. Fifty-four percent of the customers included in the sample were under the age of 39 in 2018, compared with only 25 percent of the customers of traditional banks.

This "digital native" generation is generally more familiar with digital tools and products than other generations, and therefore naturally sees online accounts as a viable alternative to traditional banks. By contrast, 56% of customers of traditional banks were over the age of 50, compared with 29% of customers of digital players.

Chart 3 Comparison between traditional banks and digital players in terms of age groups



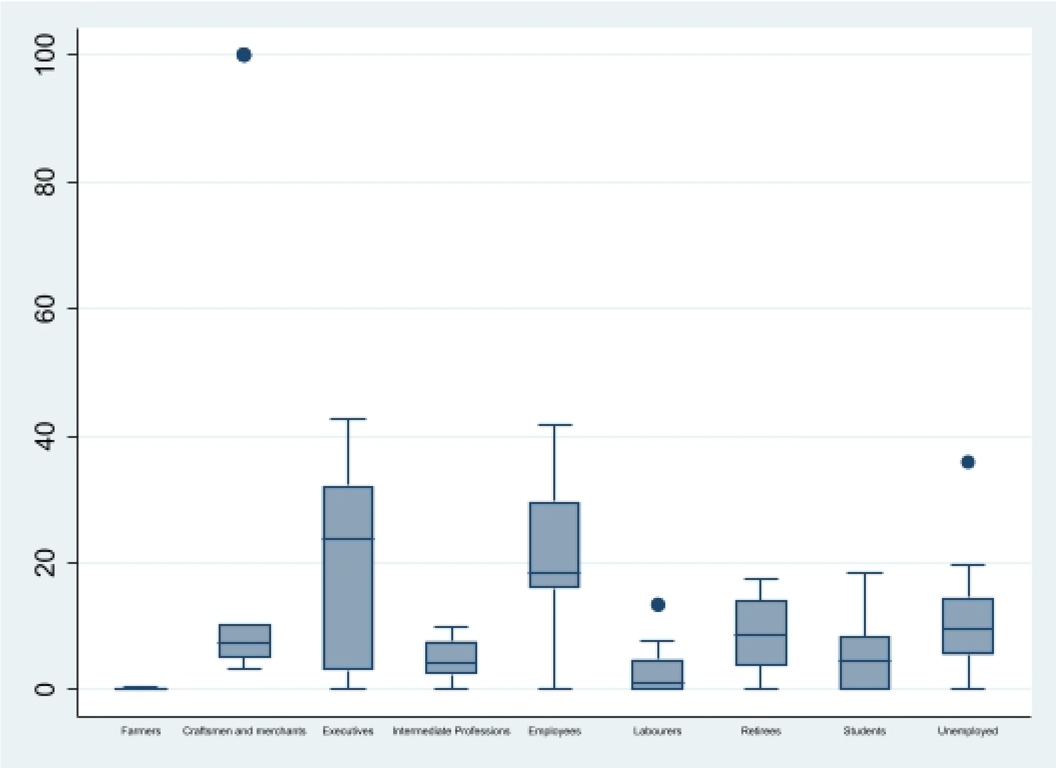
Sources: Heritage Survey 2017-2018, INSEE-BDF, for the traditional banking sector.
Source: ACPR, using data from questionnaires.

Analysing the composition of the digital players' customer base to characterise their business models is difficult for several reasons. First, due to missing data from some specialised players, it is not possible to identify the entire customer base by SPC in a granular manner. In addition, two institutions are specialised in the provision of services exclusively to the self-employed.

Therefore, this section focuses on customer analysis by only taking into account players offering traditional and diversified banking services, whether or not they belong to major banking groups. Some institutions tend to target urban and well-off customers, while others are more geared towards employees.

This phenomenon is clearly visible in Graph 4, which shows the relative weight of the various socio-professional categories included in our sample in 2020. For example, on average, the customer base of participants analysed in this study includes one-quarter (24.76%) executives - see the green box below. However, there is considerable heterogeneity in the sample, ranging from a minimum of 0% in one institution to a maximum of 42% in another. A similar dispersion is found in the employee category. Similarly, while the craftsmen and merchants category, which also includes business managers, represents 8% on average in the sample, it mainly includes the customers of two highly specialised players.

Chart 4 Box plots showing the dispersion of the relative weight that each SPC represents in the customer base of the digital players in our sample.



The outline of the boxes delimits the observations comprised between the 25th and 75th percentiles.
Source: ACPR, using data from quantitative questionnaires.

As there are no longer any account opening conditions based on a minimum level of income, which was still common practice until a few years ago, this promotes the diversification of customer bases in terms of income. This factor is complemented by the emergence of specialised players whose clientele is made up of traditionally unbanked customers or those benefiting from the right to an account. This is clearly visible in Chart 4, where the unemployed and labourers categories are characterised by the presence of a player that has specialised in collecting their deposits.

4. Product innovation, process innovations

Digital players in the financial sector are often described as innovators: while innovation is not the exclusive prerogative of these players, it is quite clear that this dimension has been integrated into their operations and their offering from the outset.

Beyond the diversity of statutes and business models, the innovation driven by these players is primarily visible in the products they distribute.

The core of their offer remains the account and means of payment pair, but these products are undergoing significant changes and players are deploying various strategies to enrich this offer with innovative new financial products. More broadly, innovation can also be commercial, with the creation of offers integrating non-financial products or financial products previously offered by specialised players (1).

The deployment of innovation by digital financial players is also taking another direction: in order to improve their operational efficiency, to reduce their costs or to be able to their build on their product offer and their network of partners, these players are developing and employing numerous tools that harness the potential of new technologies (2).

(1) In terms of product offer innovations, the answers collected from digital financial players reveal several interesting trends. These trends can be classified into two main categories: innovations of a *technical nature* (a), when players offer new products based on novel technologies, or innovations of a *commercial nature* (b) if players introduce new offers that combine existing products in an original way (targeted ranges of products, ancillary services, etc.) or otherwise targeting certain customer segments.

(a) As regards ***technical*** product innovation, breakthrough innovations are relatively limited. As mentioned above, the core product, which is distributed by all players (with the exception of one specialised player), remains the provision of a payment account with a means of payment (debit card)[13]. However, these traditional products are undergoing changes aimed at making their use more flexible.

With regard to **means of payment**, and in addition to the services linked to the payment card (choice of the payment card design by the customer, provision of cards made using specific materials - wood, metal, etc.), the innovation relates to the method used to issue and manage cards. Thus, digital players increasingly offer the issuance of single-use and not single-use virtual cards, directly from the customer's portal on their website and/or from the customer's application, notably with a view to making payments on the Internet more secure, or to segregate certain expenses (specific monitoring of recurring expenses, subscription of offers such as the "first month free"). For players, the core target of which is professional customers, the issuance of payment card "fleets", either virtual or physical, is an important feature of their offering. Indeed, such cards can be finely parameterised, both in terms of the period of validity and in terms of approved transactions (approval or rejection of transactions depending, for example, on the time of day when such transaction is carried out, or on the type of product purchased, when this is technically possible).

In terms of **payments**, the cashback mechanism is a new feature that is increasingly made available: at the time of the discussions with the ACPR, five participants were offering such services, and since then, two other participants included in our sample have implemented this service. This mechanism allows customers to be reimbursed for a fraction of the expenditure made with specific brands, directly on their bank accounts.

Lastly, in terms of **payment accounts**, the main innovation is the possibility, for the customer, to have multiple accounts or sub-accounts. These sub-accounts can consist of a simple internal subdivision within a main account or, alternatively, be full-fledged accounts identified using a separate IBAN. These accounts are most often used to monitor a specific category of expenditure, a particular activity, or to allocate a customer's

[13] Incidentally, it may be noted that the provision of cheque cashing and cheque issuing services - a product that is not very innovative while being particularly costly for the institutions that offer it - is also being promoted by the institutions that offer this service.

savings to a specific project. Once again, these innovative mechanisms are particularly present among players targeting legal entities (with a view to facilitating the financial management of these customers by splitting up expenditure items or income flows).

Innovations relating to **credit products** cover both the way they are granted and their characteristics. Thanks to the use of banking data and alternative data, credit-granting decisions are made more quickly (see below for more details on the development of creditworthiness analysis models based on artificial intelligence technologies). This innovation is especially driven by the development of mini or micro loans (for amounts comprised between EUR 100 and EUR 2,000). Indeed, since these loans are usually taken out to allow for a specific expense or when waiting for a cash inflow, the speed with which they can be granted is a major commercial advantage.

Innovation around credit also unfolds through its further integration into customers' purchasing behaviour, in the form of deferred or fractioned payment. The generalisation of these products, which has been made possible by the faster assessment of customer creditworthiness, tends to blur the boundary between payment and credit[14] frontier. It is worth noting that these innovations are at the heart of the business model of one digital player within the sample. More specifically, its business model is built around the swift provision of loans, either to its own customers or through other players (using the "B2B2C" model).

In the field of **insurance**, there are few innovations: we can only note the development of affinity or on-demand insurance offers, which make it possible, for example, to insure small computer equipment or other objects (e.g. bicycles...) for limited periods of time or according to use.

(b) Extending its definition slightly, product innovation also takes the form of **commercial** innovation –meaning innovation in the structure of the offer- with three notable trends.

The first observed trend focuses on supplementing product ranges with products that are not ***strictly*** financial products, usually made available to customers free of charge. A first family of such products seeks to make the best use of data produced during the financial activities of customers: automated advice services, based on already existing functionalities for aggregating and analysing banking data, fall into this category, as do more recently developed services allowing customers to calculate their carbon footprint or their ecological footprint. A second family of ancillary products, which are still relatively rare, is based on solutions to help with administrative procedures: provision of digital safes to centralise the administrative documents used by customers, assistance with certain administrative procedures. Lastly, a third and final category of products aims to improve the link between financial activities and other activities by integrating banking applications with other business applications. Players targeting legal persons notably develop these solutions: indeed, interconnection with accounting, expense management and payroll software is a strong commercial point of the offer proposed by the two players most strongly oriented towards these customers.

The second observed trend is the creation of offers dedicated to a particular customer segment: minors. Five players have recently developed offers for minors (generally referred to as "youth offers"), consisting of basic services (account and means of payment) associated with specific management methods: spending limits

[14] This credit distribution model is incidentally also known as credit-as-a-payment in the English-speaking world.

(in terms of amount but also according to the type of transaction), appropriate pricing, possibility for parents or guardians to monitor the use of the account...[15]

Finally, the third trend in terms of structuring commercial offers relates to the development of the range of financial investment products (e.g. savings books, stock market investments, life insurance, crypto-assets). Historically, several players have made savings a vector for commercial conquest, by offering brokerage services for stock market products, life insurance or passbooks. Since the last edition of this survey, customer interest in these products has not waned, and players offering investment products have expanded their range by offering, for example, index funds (ETFs) or real estate investments (through property management companies holding the French *société civile immobilière* or SCI status), for example. More recently, some digital financial players have also built investment product offerings that are strongly oriented towards alternative or innovative assets, going as far as offering their customers the possibility to acquire crypto-assets, through partnerships with specialised players.

(2) Beyond the products they offer, the new players in the financial sector are harnessing new technologies **to increase efficiency and improve their internal processes**.

This innovation is primarily materialising through the development and implementation of artificial intelligence tools. As a multifaceted technology with a wide variety of use cases, artificial intelligence is used by many to improve the customer relations by automatically analysing e-mails (five players), to develop automated communication tools (chatbots, 8 players) but also to improve the assessment of customer solvency during credit granting processes or to increase the effectiveness of AM/CFT-related mechanisms (identification of suspicious customer transactions or behaviours). Another sign of the near-universal adoption of these tools is that all but one of the survey participants state that they have at least one tool in production that uses these technologies. Lastly, the second technology the use of which is spreading is Application Programming Interfaces (APIs). They are popular among digital financial players[16], not only to improve the performance of their information systems (their implementation increases the modularity of ISs, thus simplifying their evolution), but also because the increasing interconnectedness between financial institutions makes it necessary to develop tools that enable the quick and reactive integration of new financial services: almost half of all survey participants stated that they had developed APIs both for internal and for external uses.

[15] At the aggregate level, the launch of these offers does not seem to have affected the proportion of underage customers reported by respondents (see Table 4). It should also be noted that some digital financial players, which are not included in the scope of this study, have placed these offers for minors at the heart of their commercial strategy.
[16] According to a Banking-as-a-service or Banking-as-a-Platform logic, the various financial services and IT bricks enabling their distribution are all modules assembled to meet a changing customer demand.

Profitability: a goal that is yet to be achieved

In line with previous research published by the ACPR, the analysis of the results of this new survey shows that digital players in the financial sector are still struggling to achieve sufficient profitability, despite increasing revenue. The withdrawal of ING France from the retail banking market in 2021 shows that this issue may, in the long term, lead to a strategic reorientation of groups when they fail to make their business profitable.

The information collected in the questionnaires was partially supplemented during bilateral interviews. However, information on many aspects of management topics remains incomplete. Moreover, institutions do not assess the measurement of the breakeven point in a uniform manner. The elements presented in the remainder of this document are therefore uncertain and should be viewed with caution.

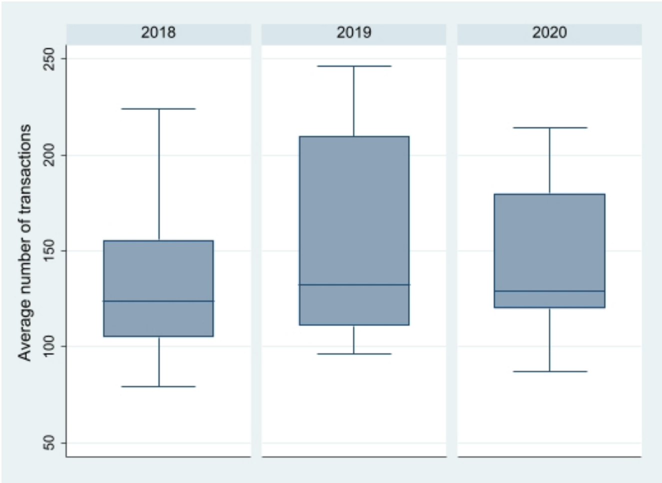
Broadly speaking, the health crisis and lockdown measures implemented in the first half of 2020 had a limited impact on institutions' business and cost of risk. However, they still face a high level of costs, particularly new customer acquisition costs, which weighs on their profitability.

1. Limited impact of the health crisis on profitability

Most online banks and Fintechs emphasise the resilience of their business model through 2020, as the health crisis confirmed the relevance of models based on a remote banking relationship using digital tools (integrated platforms, 7-day customer service) that support customers' greater autonomy in their day-to-day banking operations. In addition, revenues have not suffered any particular shocks thanks to the dynamism of online commerce and the growth of contactless payment, notably used for transactions involving very small amounts.

The health crisis has admittedly resulted in a decrease in the average number of transactions per customer, from 140 in 2019 to 135 in 2020 (Chart 5).

Chart 5 Box plots showing the dispersion of the average number of transactions made with digital players included in our sample in 2018, 2019 and 2020.

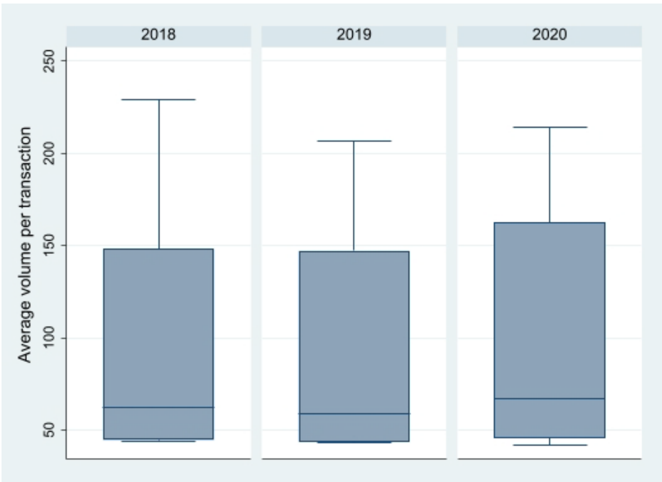


Dark lines in each box represent median values. The outline of the boxes delimits observations comprised between the 25th and 75th percentiles.
Source: ACPR, using data from quantitative questionnaires.

However, the increase in the median business volume per customer is significant, as it went from EUR 125 in 2018 to EUR 131 in 2019, and reached EUR 153 in 2020. When measured since 2018, the variation amounts to + 22.4% (Chart 6).

The decrease in the number of transactions seems offset by the increase in the average basket per customer, as evidenced by the growth of the average transaction volume per customer.

Chart 6 Box plots showing the dispersion of the average volume per transaction made with digital players included in our sample in 2018, 2019 and 2020.



Dark lines in each box represent median values. The outline of the boxes delimits observations comprised between the 25th and 75th percentiles.
Source: ACPR, using data from quantitative questionnaires.

Two additional effects should also be considered. On the one hand, the slowdown in account openings, which led to a cutback in budgets devoted to online marketing.

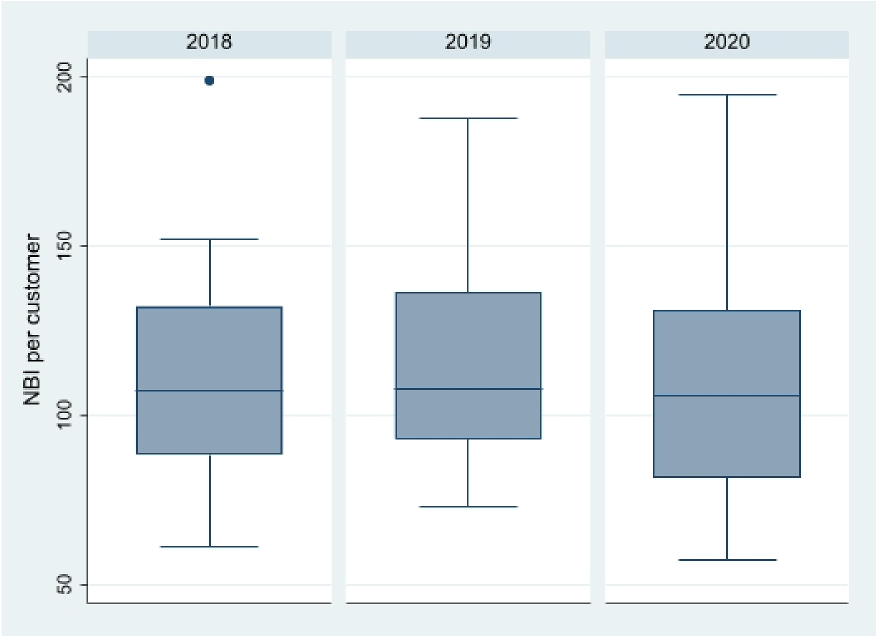
On the other hand, customer support measures taken by certain institutions, such as freezing payment incident fees or suspending card dormancy fees.

2. NBI per customer depends on customer acquisition costs

Chart 7 shows that the median NBI per customer contracted slightly in 2020. At the individual level, performance dispersion remains high, with a minimum of 57 euros and a maximum of 431 euros.

Overall, the most specialised institutions achieve a higher NBI per customer than the institutions offering universal banking services. The average customer-weighted NBI across the sample[17] fell from EUR 100 in 2018 to EUR 72 in 2019 and EUR 57 in 2020, representing a 43% decline over two years.

Chart 7 Box plots showing the dispersion of NBI per customer for the digital players included in our sample in 2018, 2019 and 2020.



Dark lines in each box represent median values. The outline of the boxes delimits observations comprised between the 25 th (Q1) and the 75th (Q3) percentile. Dots represent institutions the indicators of which (here NBI per customer) are more than 1.5 times higher than the interquartile range (Q3-Q1).
Source: ACPR, using data from quantitative questionnaires.

Several factors can explain this slight decrease in NBI per customer. On the one hand, the most recent customers - those of the current year – subscribe to fewer services than longstanding customers do. As a result, on average, they contribute less to NBI per customer than less recently acquired customers. This is because among new prospects, there is a higher proportion of free offers. Thus, the total number of customers at the beginning of the year rose by 41.8% in 2020, after reaching 52% in 2019.

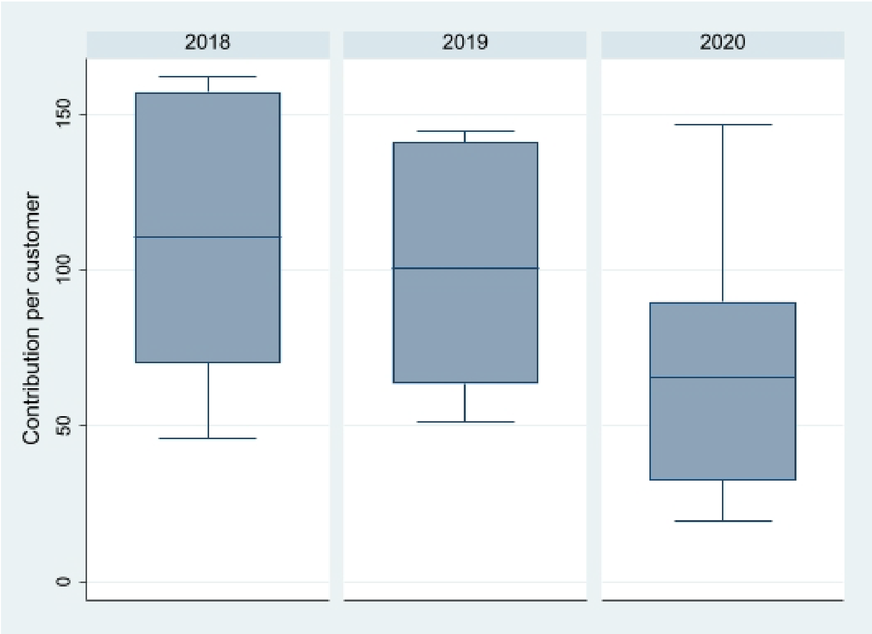
However, the main factor behind that decline is the persistently high customer acquisition costs, which mainly comprise account opening bonuses and marketing expenses. Such costs remain high (on average, they amounted to 16% of NBI, excluding bonuses, in 2020), even though the average contribution per new customer in France shows a downward trend. Digital players, especially online banks, are now devoting more resources to digital marketing in all its forms (TV advertising, online marketing, print advertising).

[17] Data from 12 institutions including 9 banks

A majority of participants continue to pay account-opening bonuses to subsidise the acquisition of new customers. This is especially the case for online banks belonging to major banking groups. However, strategies on the matter differ from one institution to the other.

As can be seen from Chart 8, most of these intermediaries have reduced average contribution per customer in recent years. However, one participant in the study is pursuing the opposite strategy.

Chart 8 Box plots showing the dispersion of contribution per customer for the digital players included in our sample in 2018, 2019 and 2020.



Dark lines in boxes represent median values. Dots show extreme values. The outline each box delimits the observations comprised between the 25th and 75th percentiles.
Source: ACPR, using data from quantitative questionnaires.

It should also be noted that some institutions implement more targeted and time-limited campaigns, such as bonuses conditional on higher payouts, in order to limit the impact of bonus payments on profitability and to forestall "bonus hunters".

Lastly, some banks also have physical networks that allow them to keep their distribution costs low, without any reliance on bonus payments to acquire customers. A player that relies on the tobacconist network incurs relatively low management costs for the physical network.

3. Operating profitability: growing income matched by growing expenses

Operating income net of expenses increased significantly in 2020, with an average 22% revenue growth compared to 2018, and 10.8% compared to 2019. This average is associated with a significant growth gap between digital players with credit institution status (+8.2%) and non-banking institutions (+32.4%), as shown in Table 6. Non-banking institutions were able to accelerate the acquisition of new customers through the launch of new products (for both the retail and corporate segments).

Table 6 Average evolution of the Net Banking Income per type of player

Net Banking Income (2018=100)	2018	2019	2020
Credit institutions	100	106	115
Other digital actors	100	159	210
All Actors	100	110	122

To make comparisons easier, the figures are presented relative to the situation in 2018.
Source: ACPR, using data from quantitative questionnaires.

The most significant growth factor stems from commission income, which is very dynamic, while the Net Interest Margin (NIM) tends to stagnate owing to low interest rates. For example, growth for commissions stood at 18.7% in 2020, compared with only 4.3% for the NIM. Commission income is mainly generated thanks to two services: securities transactions - currently only offered by banks - and interchange fees linked to the use of bankcards by customers. The latter fees contribute significantly to the growth of non-banks' service fees, the growth rates of which (+19%) is more significant than that of banks (+0.4%) in 2020.

Furthermore, the income generated by the investment of deposits heavily depends on the interest rate conditions offered by the groups or even by the banking institutions where the deposits of payment institutions' customers are held. While most digital players have been successful in maintaining a positive return on their deposits, some institutions mention negative interest rate as an issue when investing deposits[18].

Table 7 Variations in revenue stemming from commission fees and Net Interest Margin for 2018, 2019 and 2020

Income (2018=100)	2018	2019	2020
Commission	100	130	155
Net Interest Margin	100	99	103

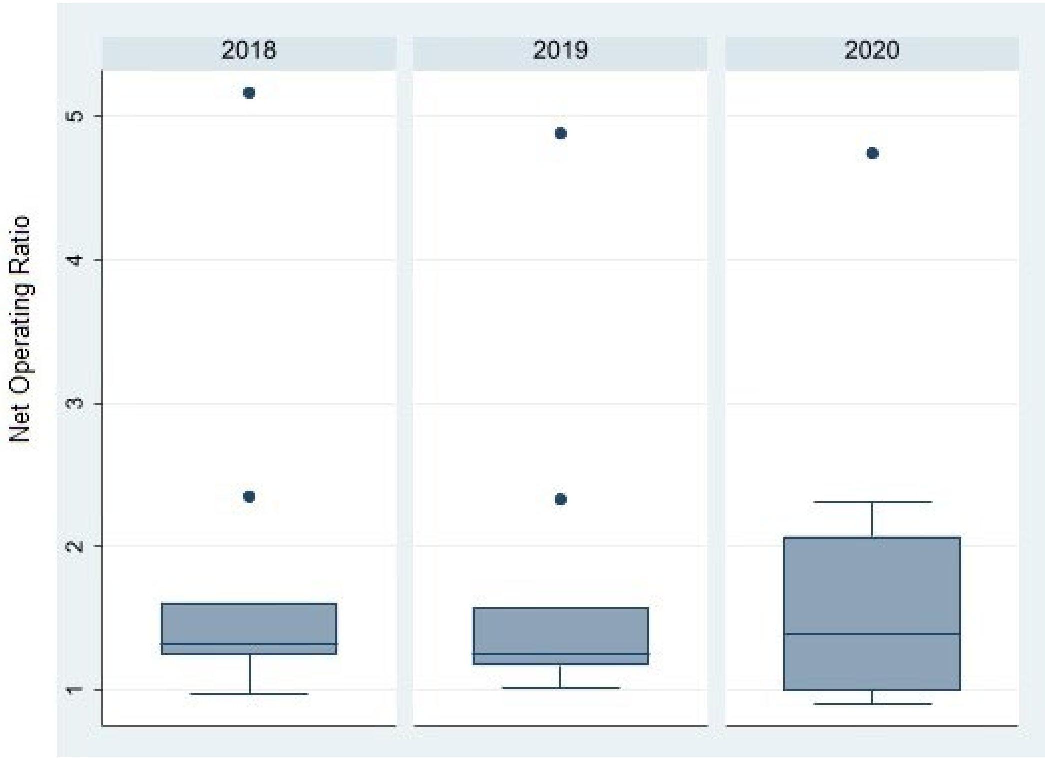
In order to make comparisons easier, the figures are presented relative to the situation in 2018.
Source: ACPR, using data from quantitative questionnaires.

The banking cost/income ratio is an indicator obtained by dividing the operating expenses by net banking income. This ratio is used to measure the share of profits made by a bank in relation to its fixed costs. The lower the coefficient, the higher the profitability of a bank.

After taking into account overheads, the average cost-to-income ratio for the whole sample deteriorated slightly, from 144.4% in 2019 to 150.5% in 2020. At the individual level, operating conditions vary considerably from one institution to another, with a minimum set at 100% and a maximum at 460%.

[18] Refer to the section dedicated to the impact of the low interest rate environment below.

Chart 9 Box plots showing the dispersion of the Net Operating Ratio of the digital players included in our sample in 2018, 2019 and 2020



Dark lines in boxes represent median values. Dots represent extreme values. The outline of each box delimits the observations comprised between the 25th (Q1) and the 75th percentile (Q3). Dots represent institutions the indicators of which (here the cost-to-income ratio) are more than 1.5 times higher than the interquartile range (Q3-Q1).
Source: ACPR, using data from quantitative questionnaires.

The increase in personnel costs, which accounted for 33% of overheads in 2020, goes a long way towards explaining the rise of overheads. Indeed, the +7% variation in personnel costs in 2020 corresponds to a +10.5% increase in overall staff numbers, reaching 1,395 Full-Time Equivalents. This increase is primarily attributable to the internationalisation of the business, which is affecting an increasing proportion of banks. Several institutions are planning to launch the distribution of their services in other countries in the coming years.

This upward trend in the cost/income ratio is also further explained by continued and substantial investments in information technology (efforts to streamline information systems, launch of new features or products), which in turn is accentuated by the fast-paced globalisation of some players.

Indeed, IT expenditure is the second most significant item within overheads, in terms of funds use. Still, this expenditure is growing more slowly than overheads as a whole, and appears to be under control. However, this observation should be put in perspective in more than one respect:

- The discontinuation of some projects has triggered significant one-off write-downs, which weighted on overheads;
- Several banks are planning major IT investments over the next few years in order to optimise their IT infrastructure (streamlining, integration of more services within a single platform, etc....)

Table 8 Average variations in overheads and IT expenditure over 2018, 2019 and 2020

Charges	2018	2019	2020
IT expenditure	100	98	109
Overheads	100	116	130

In order to make comparisons easier, the figures are presented in relation to the situation in 2018.
Source: ACPR, using data from quantitative questionnaires.

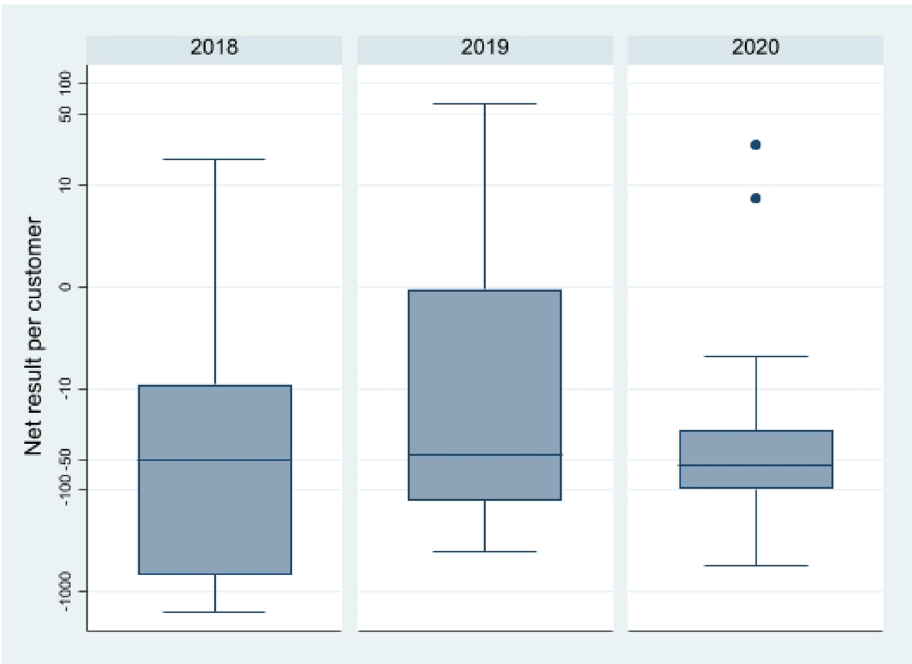
4. Negative net profitability despite cost of risk remaining low

The overall net loss measured for the sample increased further in 2020, from 376 million to 441 million in total. A large part of this deterioration is attributable to two digital players the parent group of which charge them high costs (IT, support functions, regulatory issues, development of core and non-core features, etc.).

The remainder is due to increased personnel costs triggered by market expansion.

Net result per customer, which showed some improvement in 2019, declined again in 2020, from a median level set at EUR -45 to reach EUR -57 per customer in 2020 (Chart 10). In addition to this drop in operating profitability, figures also point to a deterioration -albeit rather marginal- in the cost of risk in 2020.

Chart 10 Box plots showing the dispersion of net result per customer (in EUR) among the digital players included in our sample in 2018, 2019 and 2020



Dark lines in each box represent median values. Dots represent extreme ones. The y-axis is plotted in logarithmic scale for easy reading. The outline of the boxes delimit the observations comprised between the 25th (Q1) and the 75th (Q3) percentile. Dots represent institutions the metrics of which (in this case the net result per customer) are more than 1.5 times the interquartile range (Q3-Q1). Source: ACPR, using data from quantitative questionnaires.

However, this measure is uncertain as it is based on the varied definitions of the notion of customer from one institution to another.

In addition, the own funds level of institutions have increased significantly between 2018 and 2020. This increase reflects both fundraising by Fintechs and the capital increases initiated by some online banks with their main shareholder.

Table 9 Net result and own funds of the digital players included in the sample. Aggregated data

EUR millions	2018	2019	2020
Aggregated net profit or loss	-298	-376	-441
Own funds	1269	1556	1783

Source: ACPR, using data from quantitative questionnaires.

5. Risk constraints affect profitability in various ways

Overall, digital financial players are known for their controlled credit risk, as evidenced by an NPL rate below 1.5% at end-2020. This puts them in a favourable position compared to their parent banking groups, which had an NPL ratio set at 2.2% at end-2020 for all customer segments, and 2.6% for households alone[19].

Operational risk (fraud, litigation, KYC) is the main source of risk for digital financial players.

The figures provided by the institutions as regards the assessment of operational risk show that, for many of them, this risk has increased in 2020. Within the operational risk category, fraud is the most significant component; especially fraud in relation to the use of means of payment. Institutions also face increasing occurrences of identity fraud during the account-opening phase, forcing these players to strengthen their customer identification tools using digital processes (certification of documents issued by the bank, for example, such as bank account details or transfers). Lastly, cyber risk is the cause of certain incidents measured by institutions, and the incidence of such events has increased in the recent period[20].

Table 10 Operational risk of digital financial players in EUR millions

Operational Risk	Player A	Pl.B	Pl.C	Pl.D	Pl. E	Pl. F	Pl. G	Average
2019	0.6	1.3	0.5	0.04	0.69	0.26	0.029	**0.49**
2020	0.62	1.6	0.53	0.66	1.37	0.35	0.031	**0.74**
Variation	3%	23%	5%	1590%	98%	35%	19%	**51%**

The table only includes institutions that have submitted data on the matter.
Source: ACPR, using data from quantitative questionnaires.

[19] FINREP data, December 2020.
[20] For example, six institutions included cyber risk as a component of operational risk in 2020, mostly in the form of phishing attacks carried out on their customers

As they are subject to KYC and funds origin verification requirements prior to account opening, institutions have put in place standard account opening procedures. In order to limit friction as much as possible when entering into a business relationship, mobile-only banks, much like 100% digital players, developed pathways that allow customers to go through the entire account opening process in just a few minutes, entirely digitally.

The measures implemented by French institutions and institutions operating under the European passport system may vary, owing to differences among the regulatory frameworks of their respective countries. Lastly, the account-opening procedure of online banks the headquarters of which are located in France is sometimes longer.

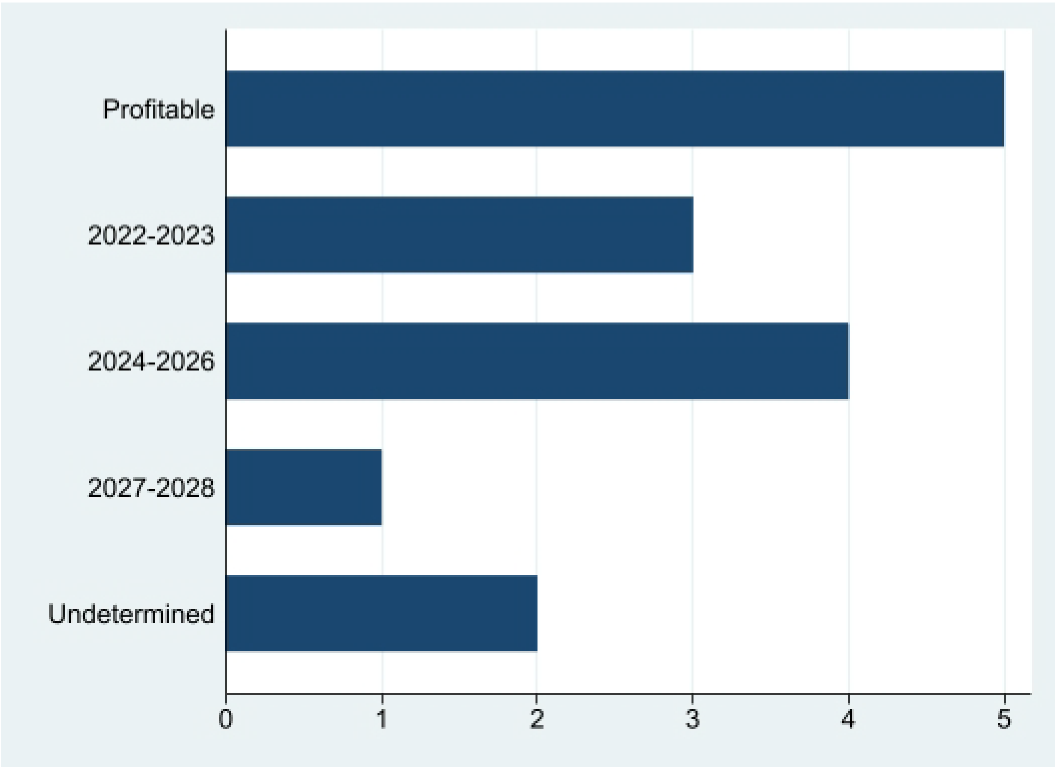
Convergent strategies for achieving the breakeven point

The break-even point, understood as the threshold from which an institution becomes profitable, raises several challenges. On the one hand, digital players must find a realistic strategy to achieve it. On the other, the ability to monitor the "distance to the break-even point" over time requires an understanding of the mechanisms behind profit generation.

1. Heterogeneous and sometimes uncertain break-even point estimates

Chart 11 represents the time horizons identified to reach the break-even point, according to the statements made by survey participants.

Chart 11 Break-even point horizon. Number of institutions



Source: ACPR, using data from qualitative questionnaires.

The players that are not part of a banking group are allegedly all, without exception, either profitable already or report they will reach their break-even point by 2022-2023. 100% mobile players are notably the most profitable ones due to their low management costs and their specialisation in specific market segments.

Among the players that do belong to a traditional banking group, only two appear profitable. For these players, controlling overheads and acquisition costs appears to be a winning strategy in the medium term. One of these players based its business model on a mixed distribution network, relying on both a digital and a physical network ("phygital" model), with high volumes and fee-based services only. The other one, a long-standing player in the market, is characterised by a good cost control as well as a particularly stable customer base.

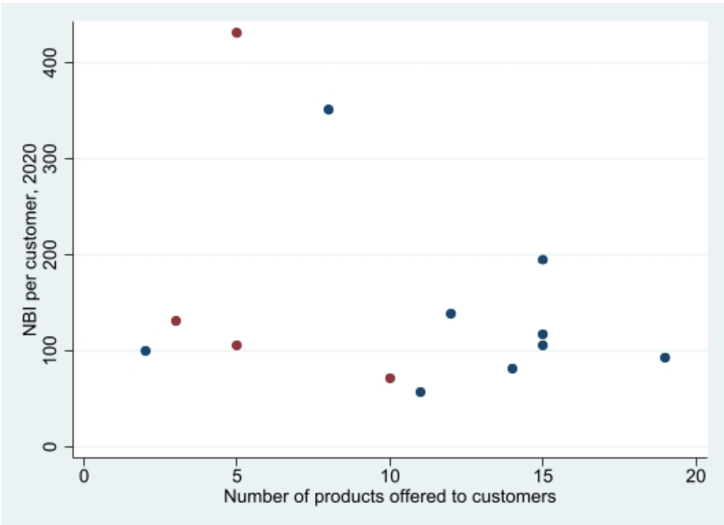
Other online banks did not make profitability an immediate target, focusing either on acquiring new customers or on offering services at a reasonable cost for customers. Finally, some players are not succeeding in achieving positive returns, as low interest rates or costly IT investments have adversely affected their profitability.

Institutions that have precisely defined their break-even point usually refer to it as the tipping point towards an EBITDA indicator (profit before interest, taxes, depreciation and amortisation). This occurs when operating income covers direct operating expenses. Progress towards the break-even point is a logical consequence of economies of scale achieved on certain expenditure items.

2. Commonalities and differences in break-even strategies

In the current situation, no direct link can be established between NBI per customer and diversity of the product offer. In Chart 12, two groups of institutions can be distinguished. On the one hand, online banks belonging to large groups (in blue), and on the other hand, independent digital players (in red). In the former group, the product offer is usually more significant and more diverse, while NBI per customer remains below 200 euros per customer. Among specialist digital players, who are characterised by a generally more limited product range, NBI per customer varies considerably from one institution to another.

Chart 12 Relationship between the number of products offered to customers and NBI per customer per institution, 2020



Source: ACPR, using data from quantitative questionnaires.

Digital players have several commonalities in their respective strategies for achieving the break-even point. Firstly, a key element for all institutions is the acquisition of new customers. Secondly, digital players have in common the strategy based on the diversification of services and products offered to customers, in a context where the profitability varies greatly from one service to another. Lastly, this diversification is coupled with a tendency for institutions to favour fee-based services in order to maximise commission levels.

The acquisition of new customers is considered by all institutions as a key element to move towards their break-even point. In the short turn, acquiring new customers is costly and has a negative impact on profitability. In the medium to long term, however, only a sufficiently large customer base can allow digital players to provide both good quality and profitable services in such a highly competitive market. New customer acquisition is expected to rise sharply by 2023, with expected increases of up to +75% in the number of customers compared to end-2020 level for some players in the sample.

Another strategy shared by all digital players is to diversify the services and products offered to customers, in a context where profitability varies greatly from one service to another.

Various trends can be observed, such as diversification towards savings and credit for payment institutions and the addition of new payment services that are trending among new customers (fractioned payment, cashback, real-time balance, account aggregation, etc.). The analysis of answers also shows that there is significant room for improvement in the area of payment initiation, a service that, in several cases, is absent from the offer.

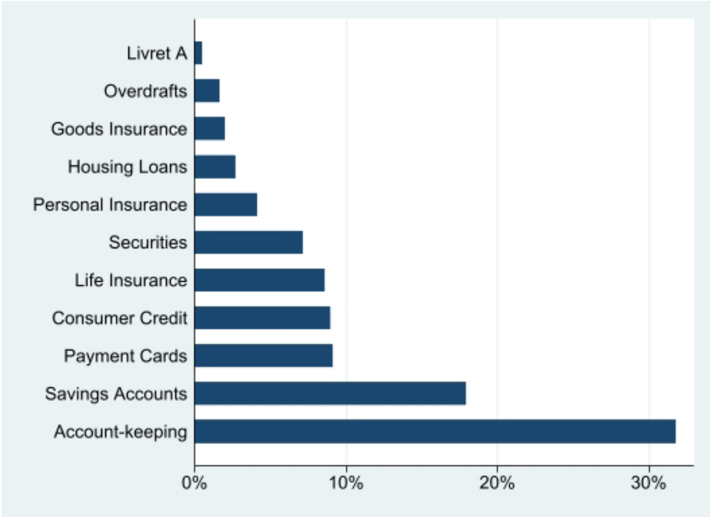
More specifically, three services in particular stand out in terms of contribution to NBI, with account-keeping (30.2%), savings accounts (17.9%) and life insurance (9.5%) generating more than half of the institutions' income. Conversely, products such as loans still contribute relatively little to institutions' NBI, especially overdrafts (1.6%) and housing loans (2.7%).

This diversification is coupled with a tendency for institutions to favour fee-based services in order to maximise commission levels. Indeed, by the end of 2020, most institutions had opted for "freemium" models, meaning a business strategy combining a basic, free offer and a premium, high-end, paying offer. Only three institutions across the sample charge for all the services they offer. Lastly, two specific pricing models are emerging, one offering free banking services (account keeping and debit card) and a second one based on a more specialised, usage-based pricing model.

As a result, basic services are intended to remain limited and provide an incentive to subscribe to paid services. This incentive can be established through the conditional payment of welcome bonuses (e.g. by reserving them for premium accounts) or by extending the benefits associated with the paid packages (addition of new services, increasing volume of services associated with each package as one moves up the range).

Bank account domiciliation is also seen as desirable by some institutions with the aim of encouraging customers to subscribe to more products while reducing the one-year attrition rate. However, some institutions do not view domiciliation as a direct driver of profitability and stress that the rate of use of value-added services is the key determinant of an institution's ability to move towards profitability.

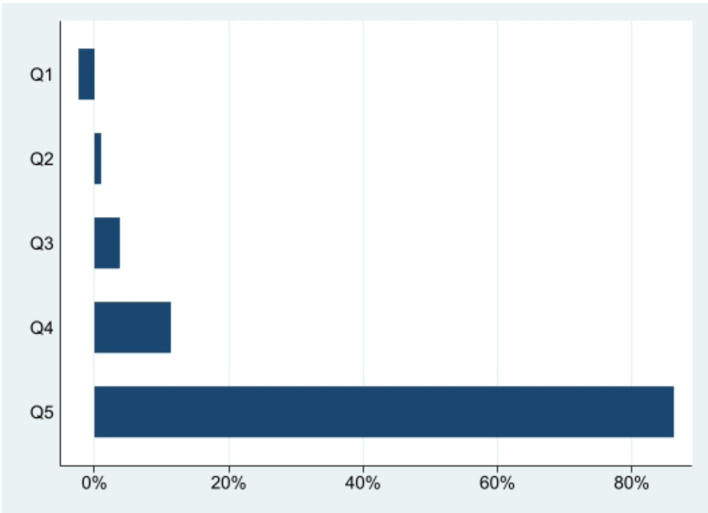
Chart 13 Contribution of various products to the NBI of digital players



Median calculated for 2020.
Source: ACPR, using data from quantitative questionnaires.

Some specialised players also consider the development of Business-To-Business (B2B, business services activities targeting corporate customers) as a priority, without ruling out the diversification of services as a primary strategy for progress towards their break-even point. Although it requires costly investments, B2B generates higher margins than B2C lending due to its licensing revenues. B2B is an integral part of the business model of two institutions in the sample and contributes up to 20% of revenues with the expectation that this share will increase in the next few years.

Chart 14 Relative contribution of customer income quintiles to the NBI of digital financial players



Average calculated over 2020. Interpretation: 86% of the institutions' income is earned on the fifth quintile of the distribution of revenue of the customers of French digital players, on average in 2020.
Source: ACPR, using data from quantitative questionnaires.

The impact of the macroeconomic environment on profitability and on the business model

The years 2020 and 2021 were characterised not only by the effects of the Covid-19 health crisis, but also by the persistence of a low or even negative interest rates environment that could impact the profitability and business model of banks and new digital players.

1. The health crisis

The health crisis has contributed to the acceleration of the digitalization of French society and the economy. As far as the digital community of the financial sector is concerned, the crisis has generally not had a negative impact on the players that are characterised by a varied product offer. This is true both for online banks that are subsidiaries of major French banking groups and for independent online players. This has been possible thanks to the increase volume in certain business lines. In our sample, only the new, highly specialised players that specialised in vulnerable market segments claim they have been adversely affected by the health crisis. Examples of such cases include credit institutions specialised in lending to professionals and mobile payment platforms.

The main notable development arising from the crisis was the build-up of savings by the French population. The health crisis caused households to under-consume, which initially led to a substantial increase in savings and then to the channelling of some of the available funds into more diversified savings and investment instruments.

While the customers of traditional banks favoured the *Livret A* passbook, the customers of digital players have instead turned to more profitable investments, such as investments in the stock market or life insurance. As a result, the institutions that were able to offer these products to their clients saw an increase in investment fees, which helped to compensate for the decrease in transactions and therefore in the resulting fees.

Lastly, it is interesting to note that the crisis had a different impact on customer growth depending on the institutions' business model (100% online or "phygital"). Players with physical branches that were closed during lockdown periods suffered a downturn in their number of subscriptions, while 100% online players or those that were able to take advantage of an open distribution network did not experience any delay in their pre-crisis growth estimates.

2. The interest rates environment

More than the health crisis, it was the continued low- and even negative-interest-rates environment that had the most significant impact on the performance of online financial players until 2021. The following developments are based on the interest rates environment prevailing during the period under review, from 2018 to 2020, reflecting a downward trend in short-term interbank market rates that continued in 2021 and negatively affected the profitability of the survey participants. They do not prejudge the ongoing normalisation of the interest rate environment, which could lead to a more favourable effect on the level of interest rates in 2022 both on the deposit transformation activity and on customer lending.

Low interest rates have in fact led to a mechanical decrease in the net interest margin, to a greater or lesser extent depending on their business model. Four different business models can be identified: institutions that mainly provide consumer credit; institutions that are part of a large banking group and place their customers' deposits within the group to which they belong; intermediaries that reinvest deposits in short-term assets such as money market funds; lastly, those who do not have a banking licence.

The first two types of players are usually unaffected by low interest rates, unlike the third and fourth categories, for which the low interest rate environment is unfavourable.

Digital players that mostly provide consumer lending are not affected by low or negative interest rates, as the activities they engage in provide them with positive margins in relation to their sources of funding, which are remunerated at lower interest rates. Similarly, for those who place their customers' deposits with their parent group, these deposits are typically neither remunerated nor charged[21]. For these institutions, the NBI is exclusively made of commissions.

Intermediaries that reinvest their customers' short-term deposits in the money market or in cash assets have seen their NBI decrease as a result of lower interest rates. All of these players are therefore considering offering fee-based services in order to be less dependent on interest income alone.

Finally, players that do not have a banking licence (such as intermediaries that are exclusively payment institutions) view low and negative interest rates as a significant barrier to market entry. Banks are indeed very reluctant to open holding accounts for payment institutions, both for strategic reasons and because such accounts are not profitable in this environment. In addition, in the case of accounts already opened, banks discourage deposits in two ways: firstly, by setting caps on the amount of deposits; and secondly, by passing negative rates on to the deposits of payment institutions, which then have to pay a charge on their own deposits.

Conclusion

The transformation of the banking landscape is still ongoing, as new players continue to emerge, competing with traditional banks in segments that until now seemed reserved for the latter, such as SME financing. However, traditional banks are constantly adapting, adjusting their offer to that of their competitors or acquiring these new competitors.

In the first case, the strategy seems less tied to the search for profitability -most of the offers remain loss making to this day- rather than to the preservation of their market share or customer base. In the second case, traditional banks are strengthening their position in an already highly concentrated market.

The players offering 100% mobile or digital access seem to have reached their break-even point or are in a position to do so in the very short term, by winning over new customers, especially younger and less well-off ones, and by relying on a limited range of services or by adopting niche strategies.

[21] However, one of the participants included in our sample indicates that it was heavily penalized for making negative rate deposits with its parent company.

Annexes

Table 11 Services offered, per institution

	Hello bank	Boursorama	Bforbank	Monabanq	Fortunéo	ING	Orange bank	Younited	Ma French Bank	Revolut	N26	Qonto	Lydia	Nickel	Manager one
Insurance															
Life insurance	X	X	X	X	X	X									
Goods insurance	X	X		X	X		X		X	X	X				
Personal insurance	X	X		X						X			X		
Credit															
Overdrafts	X	X	X	X	X	X	X		X						
Consumer credit	X	X	X	X	X	X	X	X	X				X		
Housing loans	X	X	X	X	X	X	X								
Day-to-day banking operations															
Current accounts	X	X		X	X	X	X		X	X	X	X	X	X	X
Banking card	X	X	X	X	X	X	X		X	X	X	X	X	X	X
Cash withdrawal/deposit	X	X	X	X	X	X	X		X	X		X	X	X	X
Cheques		X	X	X	X	X	X		X			X		X	
Wire transfers		X	X	X	X	X	X		X	X	X	X		X	X
Savings															
Securities accounts	X	X	X	X	X	X									
Brokerage	X	X			X					X					
"Unregulated" savings accounts	X	X	X	X	X	X	X								
"Regulated" savings accounts		X	X	X	X	X									
Innovative services															
Non-financial products		X		X				X					X		
Account information		X	X	X		X			X	X			X		
Initiation of payments		X				X							X		
Mobile payments		X	X		X	X	X		X	X	X		X		X
Crypto transactions										X			X		
FX international transfers										X	X				
Firms financing															
Instant loans		X											X		
Instant wire transfer											X		X		
Cashback		X					X		X	X	X				
Multi-cards accounts							X			X		X			X
Financial coaching								X	X						
Digital gift cards and vouchers										X			X		