Fade to white

In these days of increased emphasis on profitability, both variables of the equation – revenue and expense – can be levered through a white-label partnership. Alka Katwala, vice president at JPMorgan, explains how white-labelling of trade-finance products and services can help improve productivity while increasing revenue.

The financial services industry is at a crossroads. The need for fundamental change and visionary leadership has never been greater. Driven by this need for improved marketplace and financial competitiveness, the performance challenges now facing bankers have never been more daunting. Until now, attempts to remain competitive within an ever-declining global market have centered on the launching of new products and services into new markets in order to increase profitability.

Over the years, various re-engineering models have arisen to re-shape businesses towards obtaining their ultimate objective of profit maximisation and growth. Business models such as outsourcing and in-sourcing have been seen as a powerful way of achieving overall improvement.

Outsourcing has been accepted around the world as a key success factor for business survival. It is seen as one of the best ways of achieving cost and quality objectives, and as an effective restructuring transformational tool. Many successful companies are incorporating outsourcing as a key strategy for growth and differentiation. In a recent survey, companies cited outsourcing as one of the best solutions for addressing the globalisation challenge in a rapidly shrinking world.

In-sourcing, another business tool, can be defined as a sub-contracting function where the organisation buys in resources from a service provider that integrates with the required function, under the control of in-house management. In-sourcing allows business managers some control and flexibility, which is usually lost with complete outsourcing.

While outsourcing and in-sourcing have been useful re-engineering business tools, these options have only been significant in cutting costs. They do not meet the objective of achieving growth. White-labelling as a business-process re-engineering model is designed to expand growth in market share, enabling organisations to enter new markets by introducing new products and services.

White-labelling occurs when a supplier packages an existing product or produces new products for another company with that company’s own label. For white-labelled services, a provider re-brands processes with the name of the user firm. Customers of the user firm believe that it is the user firm that is providing the service and not a third party. The user firm outsources the supply of the service, but controls all the marketing to its customer base. The difference between outsourcing and white-labelling is that generally, under outsourcing, only the current functions carried out by a firm are outsourced, whereas with white-labelling, firms can use a service provider to outsource the production of a new product or the supply of a new service. Firms looking to expand into new market segments with new products and services are pursuing white-labelling strategies. This enables them to increase their revenue while experiencing growth in market share. By outsourcing the manufacturing part of the process to a supplier or service provider, they can control their costs due to reduced investment and still see a growth in their market share. With white-labelling, the fixed cost of extending the service stays the same, but it creates revenue opportunities.

White-labelling began many decades ago, especially in the retail sector. White-labelling started as a description of supermarket chains using suppliers to deliver own-name products. For such retailers, the sale of own-labelled products became the main vehicle for building customer loyalty, as other competitors were not able to stock products with the retailer’s own label.

Consumers choosing own-label products are guaranteed products that are generally manufactured by well-known companies at significantly lower prices. The supplier benefits from the spare production capacity being used to increase volumes and generate income without additional marketing costs. For the retailer buying in the services of a white labeller, entry into a new market or a new product can be gained without investment in new infrastructure.

In the financial sector, banks and insurance companies are all competing in each others’ markets as regulatory barriers have been lowered. Dramatic change has also come with a series of mergers and diversification into other areas. More and more, banks and other financial institutions are introducing white-labelling to non-financial firms, enabling them to enter the financial services industry and offer credit cards, retail banking, mortgage services, insurance and pension services. This strategy has been profitable to both organisations as the service provider...
increases its revenue due to the increased use of its service, and the non-financial firm gains a share in the financial services market. The field for the provision of financial services is open to almost any big organisation with a large database of customers. Many retailers, utility companies and airlines would like to become niche suppliers of financial services.

White-labelling has become an accepted partnering practice in most markets. Banks are attracted because they can use their extra capacity while gaining access to a whole new database of customers to whom they can sell additional services. The benefit to companies using the service is that they can offer their customers something better than the competition.

Trade banks together
The demonstrated effectiveness of the model in the retail sector and the success in financial services can be used as a stepping-stone for introducing white-labelling to other financial service products. In the past, larger banks around the world believed that their requirements for transactional banking products were unique and that their particular set of customers wanted something different from what the customers of other, similar banks wanted. However, banks have come to realise that, with very few exceptions, neither they nor their corporate customers are unique – both have sets of very standard requirements, and it is often only the packaging around the product or service that needs to look unique.

Despite significant growth in global trade, the use of classical trade-finance products like LCs is maturing, with top banks consolidating their market share. Recent research has shown that a half-dozen banks, commanding 60-70% of the market share, will dominate this industry over the next few years. Smaller trade banks see their business squeezed out not only by the downward trend in the use of LCs, but also by reduced market share due to the domination by larger banks. They face a strategic decision to exit the trade-finance business due to the high cost of maintaining a presence versus limited potential growth in volume. In some cases, the cost of providing the service may significantly outweigh its revenue potential. Still, banks cannot afford to withdraw the service. These banks need to provide trade-finance services as part of their overall corporate banking business offering. Consequently, it may benefit some smaller banks to take advantage of the opportunity to outsource in order to maintain a reliable and efficient service without making further investment. At the same time, it may benefit some of the bigger banks to develop a white-label service in order to increase their own volumes and reduce unit costs.

Trade-finance products can be white-labelled where the principal bank is, in effect, outsourcing its trade-finance function to the processing bank. The processing bank would handle the entire trade operations and processing for the principal bank. The processing bank labels the processes with the name of the principal bank. All outward correspondence generated by the processing bank on behalf of the principal bank is in the name of the latter. Clients of the principal bank would not necessarily be aware that they are not dealing with their own bank. All country and political risks are undertaken by the processing bank.

A well-developed operating system is one of the most important variables in any white-labelling effort. For the principal bank, the cost of developing a new system would be reduced or eliminated as additional processing platforms are built on the processing bank’s existing system. A web-based system can be made available to the entire network of the bank. The internet-based service would compete with its current offline competitors and aid towards cross-selling other products via web pages. The main advantage for the processing bank would be that any additional system capacity would be utilised more profitably.

By increasing their trade-finance business, processing banks can create additional employment opportunities to support increased volumes. As the processing of trade transactions is rather specialised, regional banks have difficulty maintaining adequately trained staff. Within a white-label partnership, existing staff can be redirected to revenue-generating activities.

As most service-based products are copied quickly and easily, to succeed in this field both banks, while assessing future competition, will need to take a long and wide view of their partnership. A shared marketing strategy of product differentiation in terms of packaging, design and advertising, and a plan to capture new clients and to retain particular market segments is required. For regional banks, this would translate into selling trade-finance services as a relationship enhancement and – due to its low entry cost into the market – a relatively higher-margin offering.

Risk underlies almost any business decision. New product development, capital investments and implementation of state-of-the-art technology are often put forth as examples of risky business ventures that may lead to major benefits, but may also result in major losses. The various forms of risk inherent in any white-labelled trade offering would have to be considered: operational risk, country and political risk, and credit risk being among the major ones. Due to these risk elements, the successful implementation of white-labelling programmes is more difficult with financial services products. If these risks are managed adequately, there is significant potential for growth in market share and an increase in revenue, as a result of that. White-labelling can be extended into most financial services products and used to create a one-stop shop for the bank’s clients.