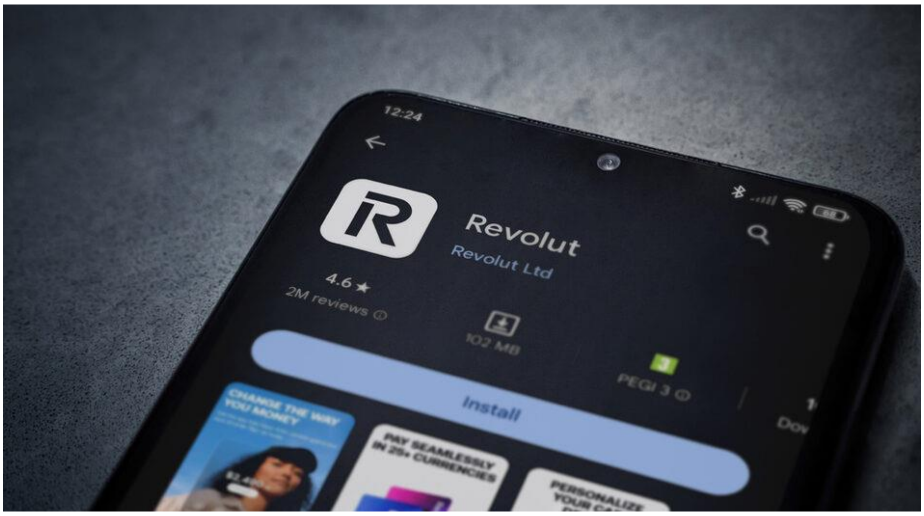
Original link: [Ще бъде ли Revolut-изиран българският банков сектор (capital.bg)]

Article below has been translated in English (from Bulgarian original version)

Marc Strauss 7. September 2024

Will the Bulgarian banking sector get "Revolut"ionized?

Bulgarian banks might forego up to BGN 1.2bn cumulative revenue up to 2030 if the expansion of global neo-bank Revolut continues



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The topic in brief

- **Traditional banks will find it increasingly difficult to charge classic fees and may lose out on deposits, which will ultimately reduce their revenues and profitability**
- **Should Revolut introduce Bulgarian IBAN for customers, revenue losses will accelerate and reach up to total BGN 1.2 billion by 2030 as customers may change their banking relationships**
- **The rise of the unbanked is not just a challenge – it is a call to transform and grow the Bulgarian banking sector**

About the author

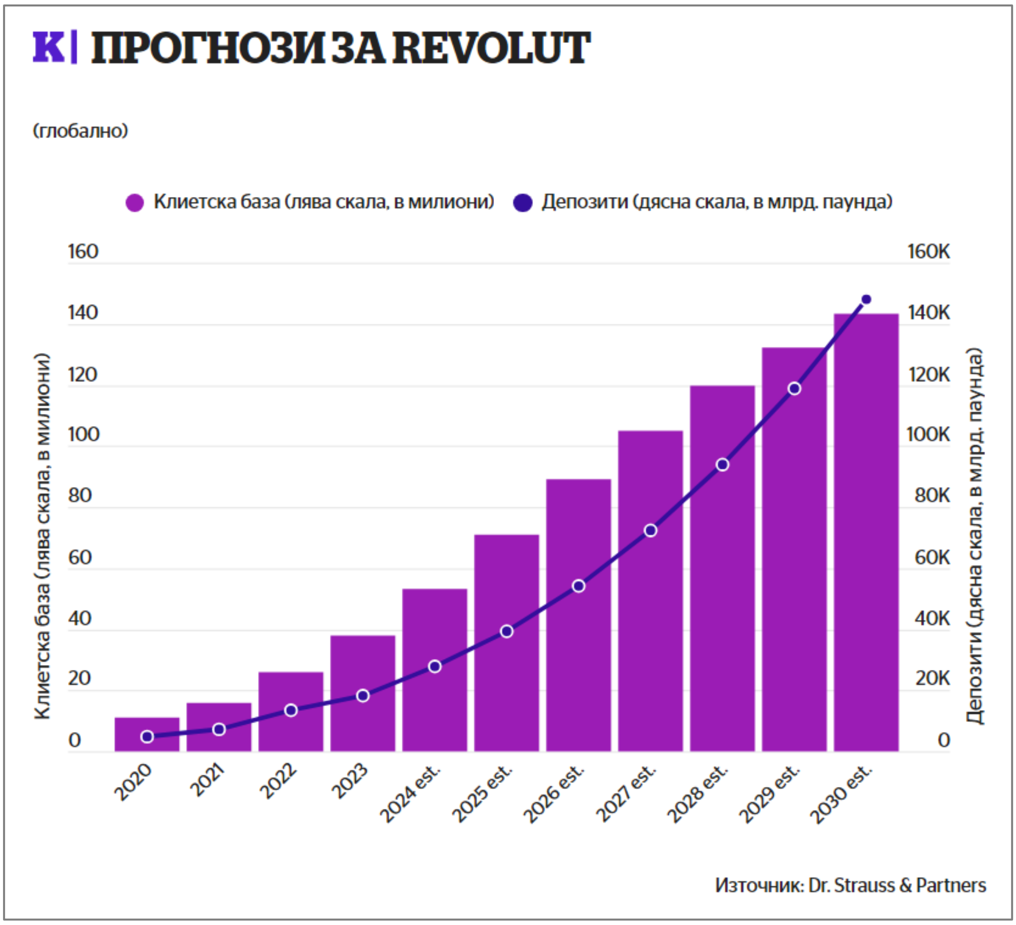
Marc Strauss is a Swiss banking expert and experienced management consultant with more than 25 years of experience (at Julius Bär, UBS AG and others). He holds a PhD in economics and is the author of two books and numerous articles on banking. Dr. Strauss & Partners (www.strauss-partners.com), the Sofia-based consultancy he founded, advises banks and other financial companies on strategy, organizational effectiveness, and digital transformation.

In today's dynamic financial landscape, traditional banks around the world are increasingly feeling the pressure from the rapid entry of nimble fintech companies offering innovative alternatives to often cumbersome, expensive and limited services. Leading this new wave of 'financial disruptors' are companies such as Revolut, Brazil's Nubank and South Korea's KakaoBank, which are rapidly growing their customer bases. For example, as of the first quarter of 2024, Nubank had 99 million customers, representing 54% of Brazil's adult population, with annual growth of 29% over the past two years. Similarly, KakaoBank serves 24 million customers, or 46% of the population, with an annual growth rate of 12%.

In total, by mid-2023, 399 non-banks worldwide serve a staggering 1.1 billion customers – a number that continues to increase rapidly. This increase in the number of customers is accompanied by an increase in deposits, loans, transactions, and investments, resulting in increased revenues and profits.

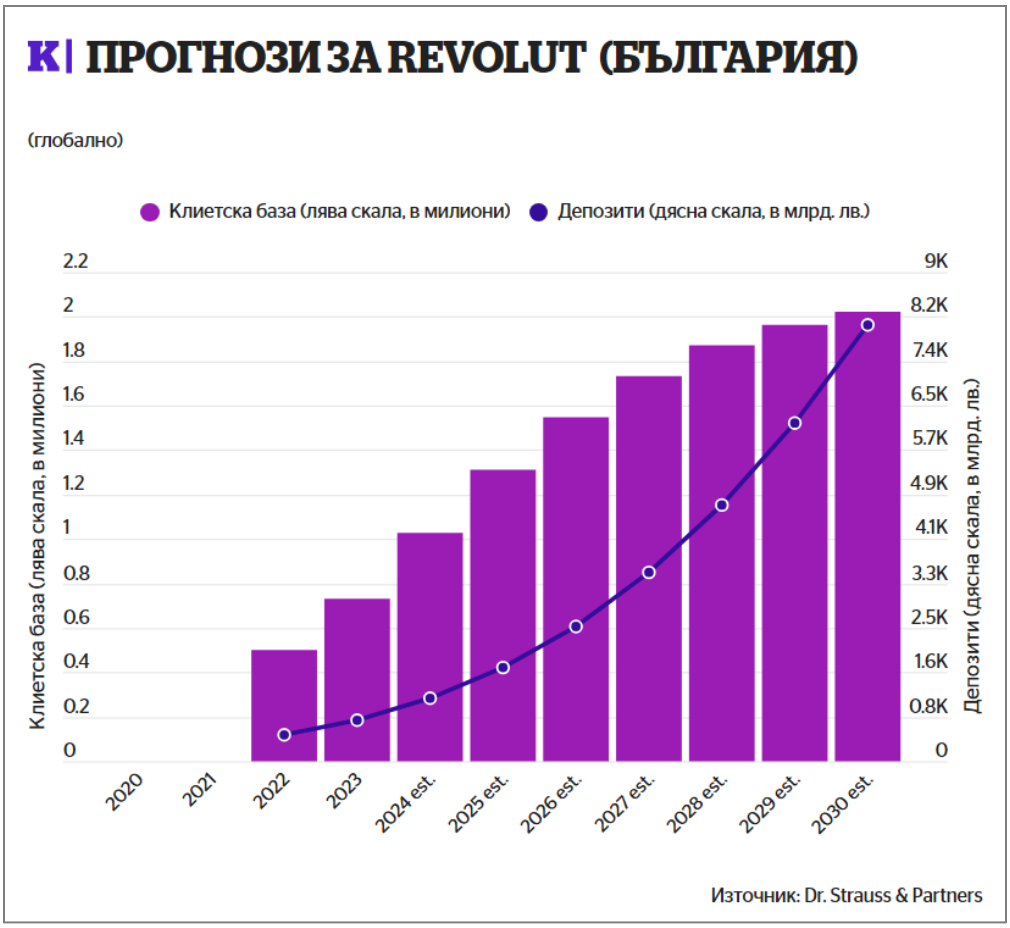
The Creeping Neo-Banking Revolution

Revolut, founded in the UK in 2015, exemplifies the disruptive power of neobanks. Initially offering faster and cheaper money transfers and foreign exchange services than traditional banks, the company has since evolved into a comprehensive financial ecosystem. It now offers both retail and business clients a wide range of services, including spending, saving, investing, borrowing, and managing money.



Revolut's remarkable growth is evident in its expansion in Bulgaria, where its user base doubled from about 500,000 clients at the end of 2022 to c. 1mn by 2024. Although growth is expected to moderate as the market saturates, the company is projected to have around 2mn clients by 2030, covering nearly 50% of the population aged 19-64. Deposits, estimated at about BGN 1.2bn by 2024, are anticipated to surge to BGN 8bn by 2030, driven by a projected average growth rate of 38% from 2025 onward (vs. 67%

currently). This growth reflects not only increasing affluence among Bulgarian clients but also a growing preference for Revolut's services as they progressively become an established habit and accepted means of transaction.



A blow in several directions

The rapid growth of neobanks, fueled by their emphasis on user convenience, lower fees, and innovative services, might mean that revenues – which would have gone to traditional banks – will instead be captured by innovative Fintechs. This is happening along several key lines:

1. Foregone fee income

Both traditional Bulgarian banks and non-banks such as Revolut generally rely on similar fee (and commission) income - comprising four common elements: cards, payments, account management and wealth services (i.e. fund/asset management and/or trading).

Even if the general services seem to be similar, Revolut offers a clear competitive advantage with its free multi-currency accounts as basic offer, fee-free currency exchange (up to certain limits), and low international transaction fees. Its trading options for cryptocurrency, commodities, and securities at transparent rates make it a compelling choice for those seeking a modern banking experience.

Currently, traditional banks in the country do well in terms of fees. Total gross fee & commission revenues in 2023 for the 17 banks is BGN 1.83bn and is expected to reach BGN 3.50bn in 2030 assuming the annual growth rate of 9.7% (2016-23) continues. Yet Revolut´s increasing relevance – with clients using the bank´s services alongside their other banking relations – could have a notable impact: Given a calculated gross fee revenue of BGN 38mn as of 2023 and applying estimated growth rates, Revolut’s fee revenue in Bulgaria might reach BGN 340mn by the end of 2030 (excluding account management fees as accounts are only additional to existing relationships and would not impact banks). This number would translate to about 10% of all banking fee revenue in 2030.

We estimate the cumulative foregone revenue of traditional banks from having to give up c. 40% of their fee base today could amount to as much as a cumulative BGN 540mn by 2030.

2. Foregone Revenue from a Shrinking Deposit Base

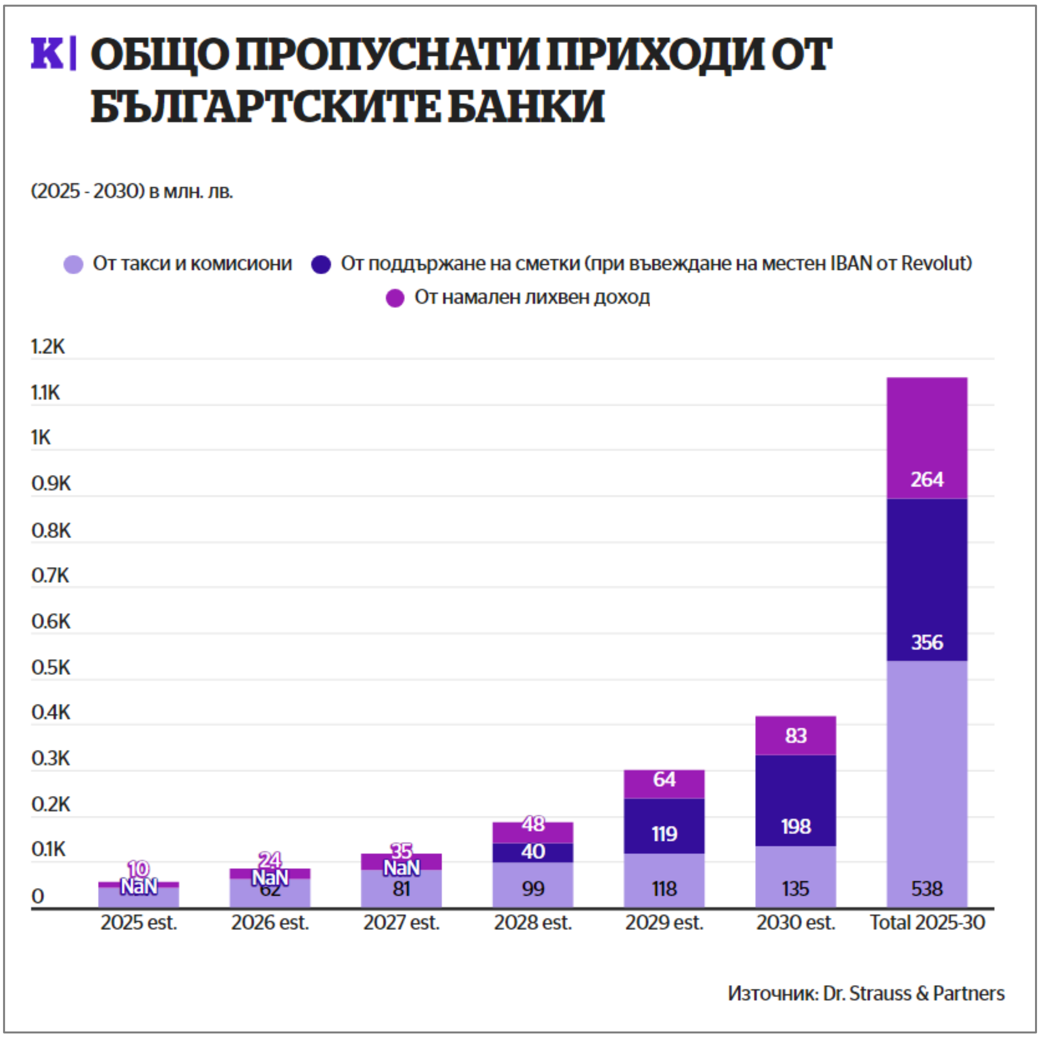
Another significant concern for Bulgarian banks is the potential reduction in their deposit base as more customers transfer funds to Revolut. A smaller deposit base means less capital available for lending, including retail, mortgage, and SME loans. The projected deposits of around BGN 1.7bn by 2025 might grow almost 5-fold to BGN 8bn by 2030. If we then assume that only one-third of these funds had been transferred from traditional banks and would no longer be available for them to lend against and apply an average interest margin of 3.5% (avg. 2016-2023), the deposit shift might have a negative revenue impact of BGN 10mn in 2025, growing to about BGN 83mn in 2030 – cumulatively around BGN 260mn for the 2025-2030 period.

3. Further forgone revenue from Revolut becoming a primary bank after an (assumed) introduction local Bulgarian IBANs

A key strategic goal for Revolut is to become the primary bank for its customers in each of its markets. To support this ambition, the company has introduced local IBANs in several EU countries, with plans to further expand. We assume an introduction of Bulgarian IBANs at the beginning of 2028, as the country is one of the smaller, yet strongly growing markets with potential. This could have a severe impact on traditional banks:

Bulgaria's adult population currently stands at 5.4mn, of which about 84% (4.5mn) have a banking relationship. Adding 0.4mio corporations, conservatively assuming one current account per client, this totals around 4.4mn active current accounts. If just 10% per year of these (ca. 440.000) are closed at traditional banks and shifted over to Revolut in the period 2028-2030, the resulting foregone revenue would go from BGN 40mn (2028) to BGN 200mn (2030). To calculate, we used an estimated monthly account fee of BGN 15, based on an average of (mostly) retail and corporate client banking package fees across all banks.

In total, across the 3 categories we highlighted above, cumulative revenue reduction can add up to BGN 1.2bn for traditional banks over the six-year period from 2025 to 2030. This could mean foregone net profit of c. BGN 480mn (conservatively assuming 40% margin).



And even further potential „damage“

Beyond the quantifiable impacts mentioned above, there are other areas where traditional banks might experience negative impact, though the impacts are harder to quantify:

- **Credit Products**: As Revolut expands its offerings to include credit cards and personal loans, traditional banks in Bulgaria could see significant revenue declines amounting to several (tens of) millions BGN annually, depending on the uptake of Revolut's credit products.
- **Cross-Selling Opportunities**: When customers shift to the neobank as their primary financial service provider (2023 alone saw a 68% rise globally), traditional banks lose the opportunity to cross-sell additional products, such as insurance or investment services. This further diminishes their revenue base.

Not all actors will be equally affected by neobanks. Banks focused on retail and SME (Small and Medium Sized) clients may face greater challenges than those serving corporate clients. Additionally, banks with a younger, more tech-savvy customers may be more vulnerable to digital-first competitors.

Possible responses

To navigate these challenges and remain competitive, traditional Bulgarian banks need to adopt proactive strategies:

1. **Enhance Digital Services:** Further prioritize the development of intuitive, user-friendly mobile apps and digital platforms. A seamless digital experience is becoming a customer expectation key to retention and growth.
2. **Rethink Pricing Strategies:** Revisiting pricing models, including transparent fee structures and levels, bundling services, or behavioral pricing, could help increase customer satisfaction and retention.
3. **Pursue Strategic Partnerships:** Collaborating with fintech companies, or acquiring them, can provide incumbents with quick access to innovative technologies.
4. **Focus on Niche Segments:** Targeting customer segments that neobanks might not prioritize or cater to can give traditional banks an opportunity. Offering specialized services tailored to these markets can help differentiate from fintech competitors.
5. **Leverage Data and Analytics:** Utilizing the wealth of proprietary data available to gain better insights into customer behavior can help tailor services and increase customer satisfaction and loyalty.
6. **Optimize Processes:** Streamlining internal operations to improve efficiency and reduce costs is essential. This also allows incumbents to dedicate more resources to invest in client needs.

The potential revenue loss of up to BGN 1.2bn by 2030 underscores the urgent need for traditional banks to adapt to the rapidly changing financial landscape. While the rise of neobanks presents a significant challenge, it also offers a unique opportunity for traditional banks to innovate, adapt, and transform their operations.

By embracing digital transformation, rethinking pricing strategies, leveraging data analytics, and enhancing customer experiences, traditional banks can not only mitigate the impact of neobank competition but also position themselves for future success.

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