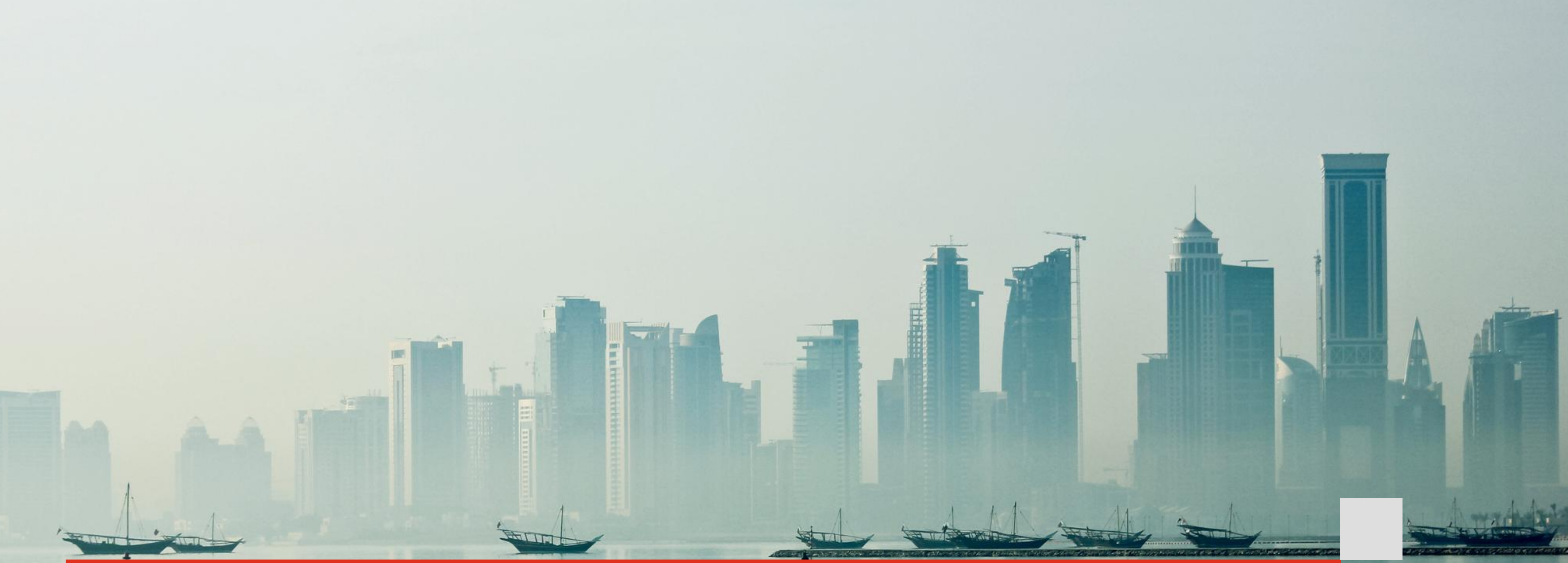
Qatar Banking Sector Report

September 2022



Introduction

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The Qatari banking ecosystem has experienced significant change during the past 12 months, largely stimulated by the impact of the ongoing pandemic, driving digitalisation, and accountability across the sector. Our Qatar Banking Sector Report provides a thorough analysis of trends from across Qatar's financial sector performance in the last year as well as reflecting the direction for the second half of this year.

Though the themes that dominate the evolution of the industry remain consistent by and large with previous years, with an emphasis on growing consumer demands and the need for incorporating contemporary values and technology, there is a greater focus on ensuring compliance especially with the advancing regulatory requirements.

Banking institutions across Qatar are well positioned with their liquidity, stability, and earnings to embrace this change, however they must act swiftly in aligning their operating models to fully internalise the latest trends and remain in line with their global and regional peers.

Global perspectives are having a greater significance on strategic directions being implicated by the country's financial sector as Qatar looks to open itself to international markets. In line with this, we are beginning to see a greater trend towards the adoption of digitalisation and cryptocurrencies, though hesitancy remains a key area of concern, especially for traditional banking models.

The emergence of FinTech players across the region are also having a significant impact on Qatar's operating models, with the pandemic stimulating a significant demand for such solutions to support online retail, ecommerce, and other sectors. This is one area that will need decisive decisions and strategic partnerships to ensure the banking sector continues to evolve to support future consumer and business requirements from their financial providers and partners.

One of the most interesting changes has been the shift towards ethical and cultural governance as both corporates and the general public begin to increasingly place accountability on those who can, and should, look to the legacy of their ESG policies. A clear consideration here, and to ensure the sector does not receive the same criticisms experienced by entities across international markets, is to not adopt a tick the box model, and instead careful strategic planning needs to be implemented to ensure a positive long-term impact.

The full report within these pages provides valuable insights from PwC's expert team, reflecting on the performance of the financial sector and emerging trends while considering the recent and future developments in the banking environment, with an emphasis on both regulatory aspects and customer-centricity. At PwC we remain committed to fostering relationships across the sector, to support the realisation of these emerging trends to achieve business goals.

Executive summary

The financial sector in Qatar is actively recovering as the country evolves post the pandemic, displaying strong volume growth supported by stable margins and effective cost management. The economic support packages offered by the government for the relief of some firms helped ensure sufficient liquidity in the banking sector. However, lingering risk pressure remains high for most of the players with banks being highly exposed to shocks on their legacy portfolios.

Balances

The Qatari banking sector has shown strong high single-digit growth in total balances during 2021 and witnessed further consolidation with a number of important mergers and acquisitions. Lending portfolios however, have witnessed slower dynamics due to lingering effects of the pandemic and more cautious risk appetite as banks continue to invest in more liquid and low-risk wholesale market vehicles.

Earnings

While the market top-line remained largely flat, the sector managed to hit high singles in operating income growth and move into double-digit territory on bottom-line dynamics. However, it is important to notice that the market performed differently at the individual banks level. Revenue diversification towards non-interest driven income has not witnessed fundamental change as of yet.

Stability

Qatari banks remain highly capitalised, far exceeding both local statutory and Basel requirements on capital adequacy – to an extent that may even suggest inefficiencies in capital utilisation. Funding remained largely driven by customer deposits with certain banks successfully diversifying by wholesale financing with bonds, certificates of deposits and other debt instruments. Lending portfolio quality remained under pressure with post-pandemic effects as NPLs kept accumulating on the books and P&L impairment charges rose. However, different banks appear to have different perspectives on portfolio risk going forward.

Profitability

Interest margins remained in the comfort zone, including leveraged benefits of funding diversification, and assured strong top-line growth. Banks have also been very successful in driving down funding expenses and managing costs that highlight the growing momentum of continuous effort in efficiency optimisation. Key bottom-line return indicators: RoAA and RoAE have seen solid mid-single digit dynamics across all major players suggesting top-line growth and cost management offset risk pressure.

Overall the short to mid-term financial outlook looks positive but should be carefully managed to safeguard the banking sector's strength and secure recovery. However, and even more importantly, time is running out for the banks to take bold and transformational steps as Qatar is catching up with global peers on fundamental trends that have important ramifications for the financial sector. Most incumbents are yet to take any concrete and decisive action on their commitment to sustainable finance, making the best use of modern technology, responding to evolving customer demands and the competitive and regulatory landscape.

Executive summary

01

New lifestyle: In pursuit of convenience and leveraging new technologies, customers are increasingly demanding digital features whilst still not yet ready to let go of the personal touch. Banks and challengers are to seek a 'phygital' equilibrium that will take the best of both worlds and respond to evolving market needs in order to remain commercially viable.

02

New values: Both corporate and individual clients are becoming increasingly mindful of working with partners that 'make it right' as the world needs to be rebuilt with an eye toward sustainable investments and environmental protection. Hence for the banks, this is not a tick box approach anymore; in addition to an annual ESG report, deep and structural change needs to happen.

03

New players: As the new financial services landscape is taking shape with the rise of alternative players like fintech, telco, retail & e-com and 'bigtech', incumbent banks can either engage in tough competition or embrace the changes with a well-thought out partnership strategy.

04

New technology: To respond to market demand, Qatari banks need to act quickly and transform into a digitally enabled version of themselves. Just delivering new features and channels will not work; fundamental groundwork needs to be done to transform the core beyond pure technology. This often includes changing processes, the organisation and the culture.

05

New money: Despite the growing popularity of cryptocurrency, most traditional banks are still hesitant to adopt the use of such assets. However, regulators globally are working to change banks' perceptions of digital currencies, believing that these assets can enhance innovation and efficiency among financial institutions.

06

New rules: As the financial sector is getting more complex with increasing amounts of data, technology, new business and operating models, banks should expect fundamental changes in the regulatory agenda and play a more active role in setting out the 'ground rules' going forward. Beyond evolutionary development of 'core' topics like customer and data protection, data infrastructure build and ESG governance, the whole new agenda is building up for the regulators in Qatar and the broader region with open finance, digital currencies and green finance.

2021 Financial sector performance

Key financial performance highlights

Values as of 2021 YE (and year-on-year growth, %)

Balances

Assets	Gross Loans & advances	Deposits	Equity
QAR 1.9 Tn (+6.5%)	QAR 1.4 Tn (+5.4%)	QAR 1.3 Tn (+7.8%)	QAR 0.2 Tn (+7.1%)

Earnings

Gross Income	Operating Income	Profit Before Tax	Net income
QAR 82.1 Bn (+0.9%)	QAR 59.1 Bn (+8.4%	QAR 25.9 Bn (+11.3%)	QAR 24.9 Bn (+12.8%)

Stability

Average Loans-to-Deposits Ratio	Non-Performing loans	Cost of Risk 1	Capital Adequacy Ratio
113% (-4.2%)	QAR 36.1 Bn (+15.4%)	1.20% (+19.8%)	19.3% (+4.7%)

Profitability

Net interest margin	Cost-to-Income Ratio	Return on Average Equity	Return on Average Assets
2.5% (+2.6%)	22.9% (-3.8%)	10.7% (+10.5%)	1.4% (+12.0%)

1 Calculated as annual profit and loss impairment charge over average gross total loans

2021 Financial sector performance (QAR)

Figure 1. Total Assets

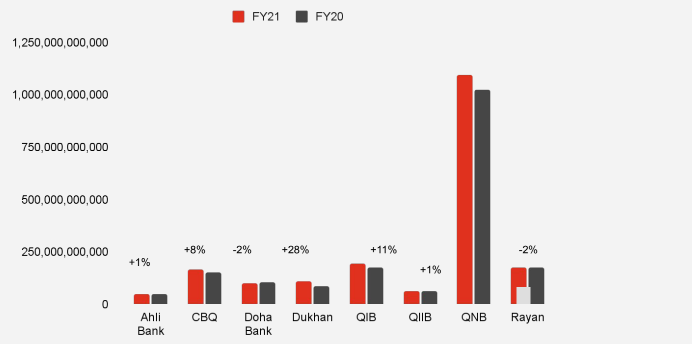
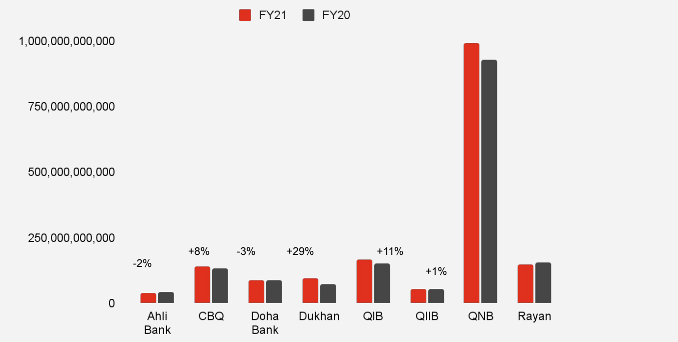


Figure 2. Total Liabilities



Qatari banks have experienced single digit growth in total assets and liabilities over the financial year of 2021 (FY 2021 vs FY 2020), despite the volatility of the past year, as demonstrated by the (consolidated) reports published by listed commercial banks. Growth of the aggregated assets accelerated in FY 2021 by 6.5% to 1.95 Tn compared to 1.83 Tn for FY 2020, and by 6.2% CAGR over the three-year period (FY 2021 vs FY 2019) evidencing that the banking industry in Qatar has been expanding at a fast pace over the past three years. Growth of the aggregated liabilities accelerated in FY 2021 by 6.4% to 1.73 Tn compared to 1.63Tn for FY 2020, and by 6.3% CAGR over the three-year period (FY 2021 vs FY 2019). Assets grew quicker than liabilities hence banks have been growing equity even quicker and using it to help fund the business. However, when you look at bank level the picture is different; CBQ and Bank Dukhan have seen quicker liabilities growth which on the other hand are using other liabilities to fund the growth in assets. Foreign liabilities accounted for 47% of the sector's funding FY 2021 (38% FY 2018) and net external debt increased to a substantial 81% of Qatar's forecast 2021 GDP FY 2021

Figure 3. Gross Total Loans and Deposits

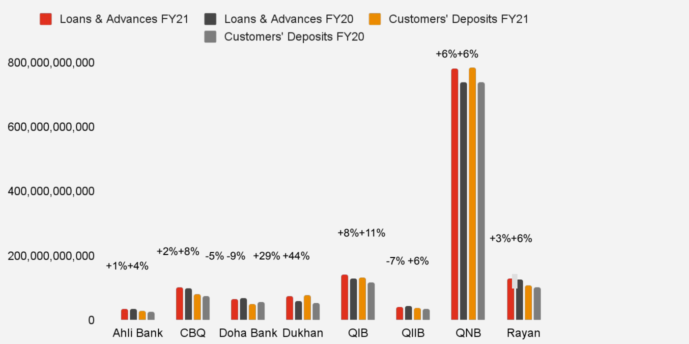
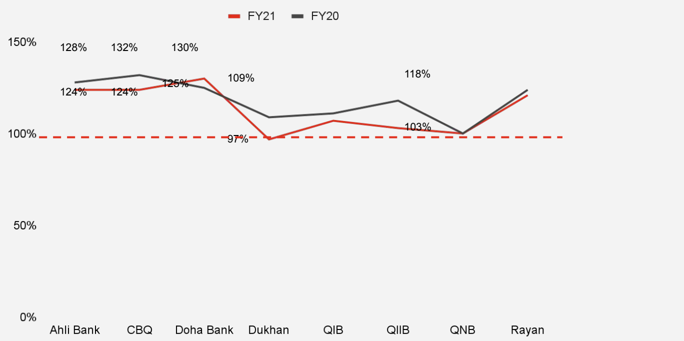


Figure 4. Loans-to-deposits (L/D) Ratio: Gross Total Loans / Total Deposits



The growth dynamics in the aggregated total loans and advances of listed banks, have also been positive – though slower than asset expansion. Total gross loans and advances in FY 2021 grew to QAR 1.37 Tn from QAR 1.30 Tn displaying 5.4% increase at a three-year CAGR of 5.6%. Portfolios are still mostly funded by customer deposits that reached QAR 1.30 Tn in FY 2021 (compared to QAR 1.15 Tn in FY 2020), displaying 7.8% annual growth with three-year CAGR of 6.3%.

The dynamics for loans and deposits is contrary to assets-liabilities evolution as portfolio growth has seen a slowdown in FY 2021, while consumer deposits balances accelerated. This may highlight lingering effects of the pandemic with most banks still displaying higher risk aversion and investments in lower-risk and more liquid asset classes.

The average loan-to-deposit ratio has reduced slightly from an average of 118% in 2020 to 113% in 2021. However, the market features two very distinct groups of players – those (almost) fully relying on deposits to fund their portfolios (Dukhan, QIB, QIIB, QNB) and FIs with sizable portfolio of wholesale funding such as bonds, notes, certificate of deposits and others (Ahli Bank, CBQ, Doha Bank, Masraf Al Rayan).

2021 Financial sector performance

Figure 5. NPL Ratio: Non-Performing Loans / Gross Total Loans (with 3-year CAGR)

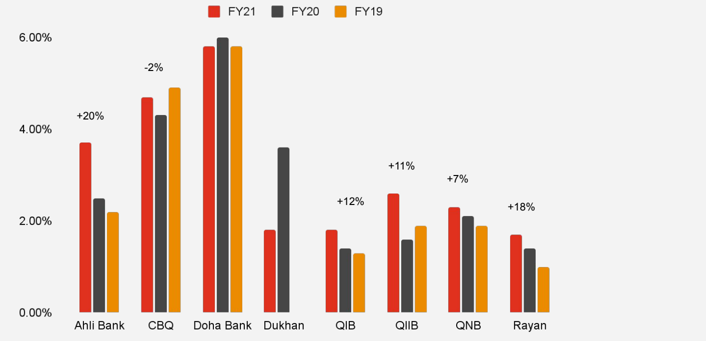
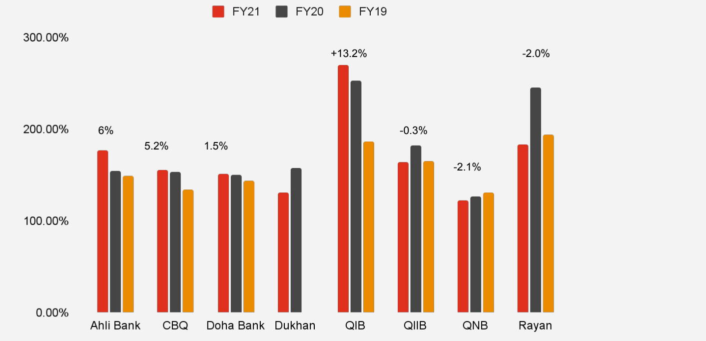


Figure 6. Bad Debt Coverage Ratio: Impairment Allowance / Stage 3 Loans (with 3-year CAGR)



As hinted by lending portfolio dynamics, the market is still recovering from the stretched effects of the pandemic – a larger share of the portfolios accumulated over the last years is falling into the bad debt category. Non-performing loans ratio (NPL) increased by 15% reaching 3.1% in FY 2021 compared to 2.7% in FY 2020. However, while the more objective NPL trend is largely consistent across key players, the pattern of bad debt coverage ratio is not necessarily so, suggesting that different banks may have different views on portfolio riskiness. Some banks such as Ahli Bank, CBQ and QIB continue building up their provisions implying that the downturn effect has either peaked in 2021 or yet to do so. Others, like QNB, tend to unwind some of the provisions believing they may have been overly cautious and most of the negative effects have already materialised. The rest, like Doha Bank, QIIB and Rayan are holding the middle ground by maintaining stable coverage ratios over the last three years.

2 Non-performing loans and advances to total loans and advances are disclosed as presented in the financial statements. Whilst some banks depicted the ratio net of deferred profit, other banks disclosed this ratio as gross. With regards to QIIB, we note a change in values reported, due to a change in the formula used by QIIB for calculating the non-performing loans and advances (NPLs), which are now net of the deferred profits. The change in the formula can be identified by comparing the reported non-performing loans and advances between FY2020 and FY2019.

3 Historic 2020 and 2019 figures for Masraf Al Rayan feature combined balances for Masraf Al Rayan and Khaliji for dynamics comparison purposes

2021 Financial sector performance

Figure 7. Gross Income From Financing And Fees (with YoY growth)

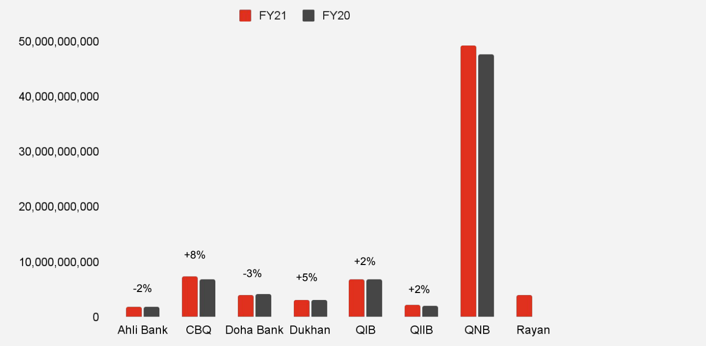
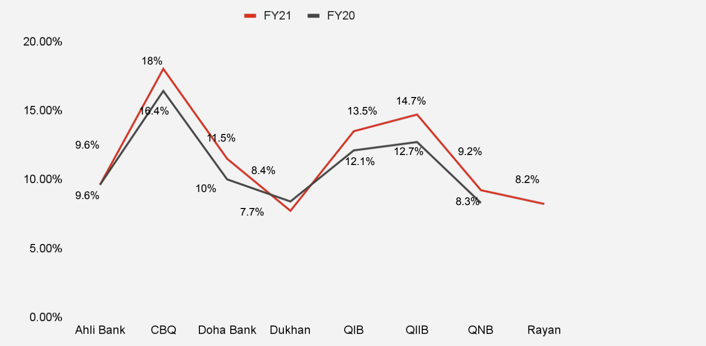


Figure 8. Gross Fee Contribution %: Gross Fee Income / Gross total Income



While growth in the balance book has largely remained in mid-single digits, the gross aggregate income from financing and fees for the listed banks in FY 2021 remained largely flat growing by 0.8% (to QAR 82.1 Bn in FY 2021 from QAR 81.4 Bn in FY 2020) with a few outperformers (CBQ, Dukhan) and those experiencing slight contraction (Ahli Bank, Doha Bank). In terms of income diversification, the market did not display structural changes over FY 2021 featuring two distinct groups of players – those actively leveraging fee income as revenue source with 15%+ share of total top-line (Ahli Bank, CBQ, QIIB) and players relying on more traditional financing income with more modest 9-13% share (Doha Bank, Dukhan, QIB, QNB).

Figure 9. Operating Income: Gross Income from Financing And Fees – Funding Cost and Fee Expenses

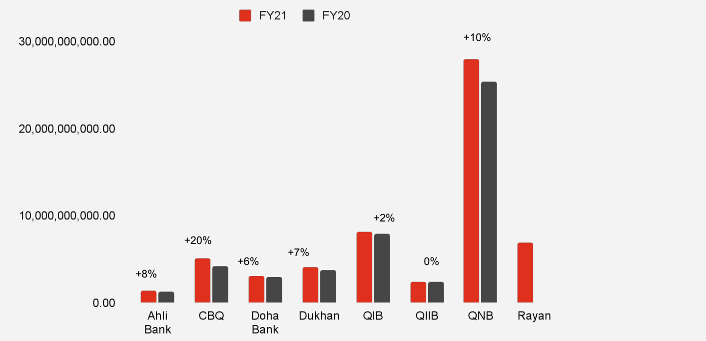
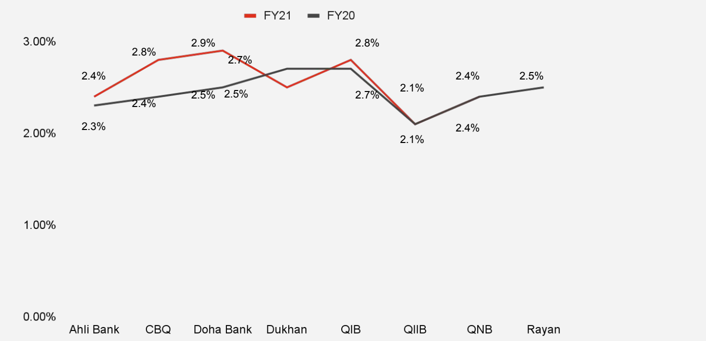


Figure 10. Net Interest Margin: Net Interest Income / Average Earning Assets*



From an operating income and margin dynamics perspective, the market remains in the comfort zone as growth displayed has been much faster than gross top-line due to overall contraction of funding cost and funding diversification by certain players. The market has shown 8.4% YoY improvement in operating income reaching QAR 59.1 bn in FY 2021 compared to QAR 54.5 bn in FY 2020 landing at 2.5% average net interest margin. CBQ has outperformed the market with strong 20% income and 17% margin uplift due to quick portfolio expansion and decreased funding cost. QNB expanded its portfolio by 10% while keeping margins constant; both QIB and QIIB remained largely flat in both income and margin. Doha bank, while improving on margins, only displayed moderate income growth due to portfolio and top-line contraction. the remainder oscillating around market average within 6-10% range. Margin compression for Dukhan is most likely due to the impact of the recent mergers which took place in 2021.

2021 Financial sector performance

Figure 11. Cost-to-Income Ratio: Operating Cost / Pre-Impairment Operating Income

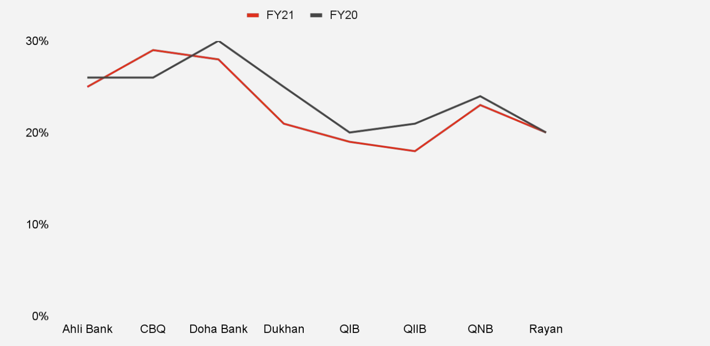
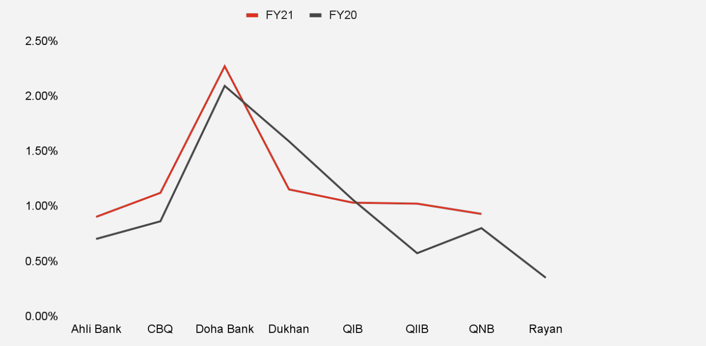


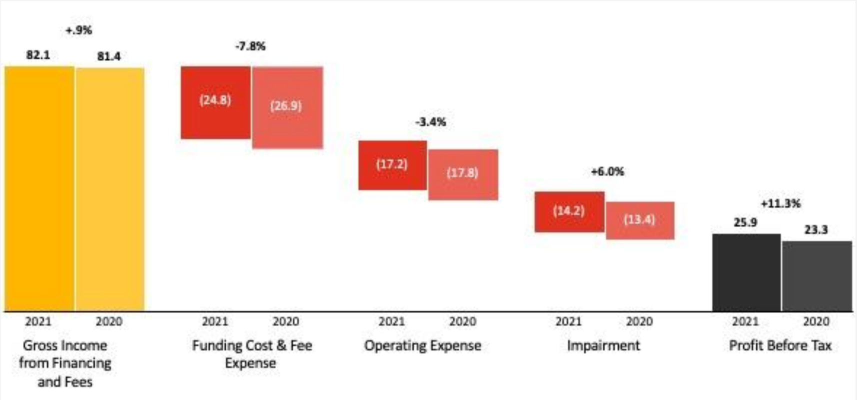
Figure 12. Cost of Risk: Impairment Charge / Average Gross Total Loans



The Cost to Income ratio across all banks has seen an aggregated 4% reduction reaching 22.9% in FY 2021 compared to 23.8% in FY 2020. This shows the growing momentum of banks' continuous effort in efficiency optimisation. The only countertrend outlier is CBQ that has accrued a QAR 0.3 Bn one-off expense to introduce longer-term compensation plan for staff effectively providing a portion of the bank's stock to employees.

The aggregated average Cost of Risk ratio in FY 2021 witnessed an almost 20% increase hitting 1.2% in FY 2021 compared to 1.0% in FY 2020. Doha bank continues to operate the high-risk portfolio but the dynamics are stable, QIIB has taken a large hit recognising losses on accumulated portfolio while maintaining financing flat, and Dukhan bank has seen significant improvement due to acquisition of lower-risk portfolio of International Bank.

Figure 13. Aggregated Profit and Loss Waterfall and Dynamics



Overall, the total aggregated Profit before Tax across the Qatari banking sector has shown an increase of 11.3% for the FY 2021, from QAR 23.5 Bn in FY 2020 to QAR 25.8 Bn in FY 2021. This can be attributed to an almost 8% reduction in funding cost supported by improved operating efficiency (3.4% reduction YoY). Amount of impairment charge on the books have risen by 6%, but remained outweighed by the combined effect of the two factors above.

2021 Financial sector performance

Figure 14. Return on Average Assets and Return on Average Equity

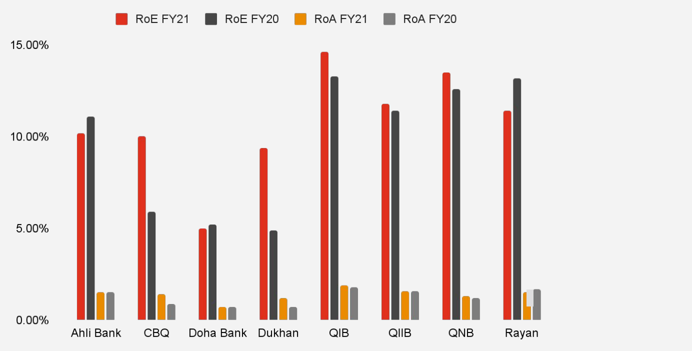
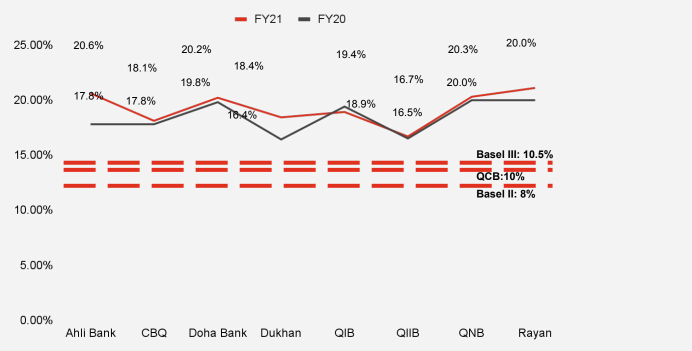


Figure 15. Capital Adequacy Ratios



The aggregated profitability ratios across all banks has proven to be almost stable over the period. Overall RoAE increased by 11% reaching 10.7% in FY 2021 compared to 9.7% in FY 2020 with RoAA following similar dynamics: 12% growth to 1.4% in FY 2021 from 1.3% in FY 2020. CBQ has shown the best performance due to quick top-line extension and managed risk followed by Dukhan that gained efficiencies from acquiring a high performance portfolio of international Bank.

All Qatari banks have shown capital adequacy figures well above both the statutory QCB and Basel thresholds concluding a very well capitalised banking sector. However, this may manifest some sector-wide capital utilisation inefficiencies – especially for those who diverge from the recommended levels like Ahli Bank, Doha Bank, QIB, QNB and Masraf Al Rayan.

Forward looking trends and response strategies

New lifestyle

Respond to fundamental change in customer expectations and behaviour

In recent years, the world has seen the rise of client centricity and customer empowerment coupled with a fundamental shift towards digitalisation. Numerous products, companies, and entire segments like online streaming have evolved as digital natives are bringing in a new era of customer experience. The formula is simple: whoever earns the customer's trust and provides the best experience, wins.

While banks still hold a lot of 'trust' equity when it comes to managing money, they may not be as advanced on the 'convenience' side as some of their peers. This is especially true in the GCC where everything revolves around convenience being a key lifestyle attribute. According to the 2022 global survey of measuring NPS across different sectors, banks have a long way to go to optimise customer satisfaction and be on par with other industries.

NPS Score across Industries

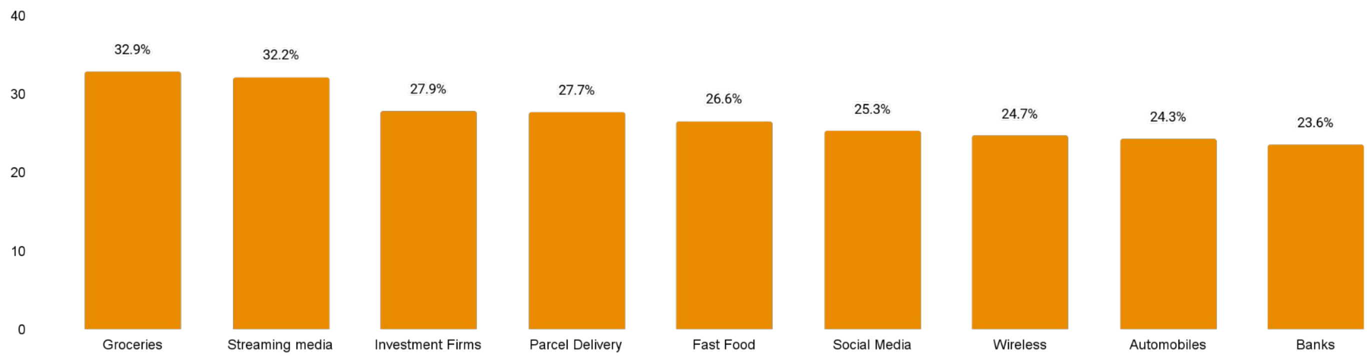


Figure 16

> **The shift to conservatism nudged banks to relook and evaluate their banking and investment products. Customers wish to have tailored products that are in line with their expectations for sustainable income and low risk**
>
> **Ahmed Al Kiswani,** Financial Services Consulting Partner, PwC Middle East in Qatar

Forward looking trends and response strategies

In the Qatar Banking sector, competition is high relative to the size of the market and the number of banks available, thereby resulting in an increase in customer expectations. A significant shift in customer culture is evident post the COVID-19 pandemic, resulting in an unfamiliar mix of conservatism and willingness to maintain the personal touch complemented with an increased reliance on digital technology.

Conservatism is making banks reassess their ambitious digital-only focused transformation programs into a more hybrid and evolutionary journey that retains a real-world touch but; elevates this to a new level of experience.This safeguards their customer base due to increased loyalty.

Offering a ‘digital only’ model can have ramifications: while for some segments like white-collar expats or young ‘digital natives’ the proposition can be very lucrative (convenient and user-friendly access to financial services without having to pay for physical infrastructure), a large share of the market is not ready to fully let go of the traditional branch-based setup. Traditional banks, which emphasise in-person customer service have a long-established reputation, and may seem more trustworthy than those who do not have any physical touchpoint.

The race between traditional and digital banks is reaching a balance in popularity across the globe. Both sides are aiming to find an equilibrium between the ‘old’ and ‘new’ worlds with incumbents growing or acquiring their digital arms (like separate digital brand for retail banking in Santander) and digital challengers establishing physical touchpoint tokens (like cash-in & out points and self-branded POS terminals of Revolut). In some markets, like the UK for example, neo-banks are strongly holding their ground maintaining digital momentum, while in others,like Australia, traditional banks have caught-up quickly and are now outperforming their ‘digital only’ competitors by leveraging a consumer driven optimal mix of digital and physical capabilities.

For Qatar, the broad answer could also lay in the ‘phygital’ space. Combining a stronger commitment to the ‘P’ part of the equation than in Europe or Asia, coupled with product personalisation, intuitive and easy-to-use interfaces, and digital features that make customers’ lives easier ensuring that Qatari banks can offer their customers a perfectly balanced customer centric banking experience.

Forward looking trends and response strategies

New values

Embrace ESG and ethical banking at the core of banks' operations

Institutions are adapting strategies and practices to have better ESG outcomes as environmental, social, and governance concerns become increasingly hot topics within the banking industry. To become carbon neutral and understand how environmental considerations affect their lending and investment portfolios, banks are now turning their attention to the environment. Social and governance pillars of ESG have already been a large part of the major banks' strategic focus over the past few years.

Qatar's banking industry is increasingly embracing environmental, social, and governance issues. As a result of the pandemic, the world needs to be rebuilt with an eye toward sustainable investments and environmental protection. Even though it is still in the developmental stage, the banking sector plays an important role. Nevertheless, green bonds, green loans, and standard ESG disclosures are already being implemented in this direction. The QCB had emphasised the importance of promoting sustainable investment and green finance. Several Qatari banks have already embraced green initiatives in their business practices such as issuing green bonds, offering green loans/mortgages, and offering green credit cards.

The regulatory framework is still under development; however, banks are proactively sharing ESG initiatives with international investors, customers, and stakeholders. The majority of Qatari banks are introducing these initiatives by starting with a standard checklist approach while in some cases, other banks have evolved to a more comprehensive model that is shifting from a superficial tokenistic approach to readily embedding ESG initiatives into the bank's operating model such as in credit and investment portfolios. There is also an evident change in the banking sector in Qatar on the perception of ESG, where previously this may have been something that must be done to meet regulations, we can currently see major ESG initiatives in many banks in Qatar.

A significant focus by Qatari banks on the development of their ESG annual reports is driven by Qatar's overall ESG strategy, while a major challenge for the banks when developing these reports is to execute and implement the promises and initiatives in the reports. Banks are looking into to what extent they are able and ready to execute these initiatives from a budget, people, and process perspective.

Secondly, significant attention to ESG Risk Management is specific to embedding the Social and Governance within the ERM framework of the banks and creating quantitative factors in the credit risk management and the overall credit risk scoring to recruit environmental and social factors. The consequences of this trend are that banks are facing challenges mainly in the credit portfolio classifications providing effective segmentation of their customers as well as providing a framework that balances the management of environmental/social risks and managing business expectations and targets.

There is an evident trend to create automated tools and technology that can aid banks in capturing the ESG KPIs and providing a timely monetary framework to monitor the progress of achieving ESG requirements periodically. Significant pressure is coming from international investors, rating agencies, and regulators on large banks particularly those who have a significant portion of credit supplied to different segments of companies and large investment books.

Embracing ESG frameworks and sustainable banking at the core of banking operations is the need of the hour and fortunately, banks in Qatar are ensuring that ESG is at the top of their agendas. Although in the preliminary stages and in certain cases imposed by external pressure, ESG practices are slowly becoming the foundation of building a viable future and setting the stage for local and international competition for Qatari banks. However, just like digital transformation, it is of paramount importance that careful consideration is placed by these banks on fully internalising an ESG strategy and placing it at the core of all practices during this transformation to avoid systemic issues in the long run.

Forward looking trends and response strategies

New players

Effectively navigate in an evolving landscape of financial service challengers

The modern financial services landscape has transformed fundamentally, with many new players entering the market and leveraging different business and operating models to provide added value to consumers. The two broad transformation vectors include the rise of FinTech which is designed to elevate the financial services sector, and the emerging interest of non-FS players that wish to offer financial solutions to their clients. For the incumbent players, both types of new entrants can be perceived either as competitors or partners and choosing the right strategy becomes paramount as ignoring such players may lead to severe market disruption.

FinTech

FinTech has grown tremendously over the last decade, and we are experiencing exciting new developments. Due to its impressive efficiency and cost-saving capabilities, FinTech is becoming a global industry. As the Fintech industry leverages emerging technologies to develop customer-focused business models, it has effectively leveraged the focus on digital transformation and changing consumer and business behaviours in a global market. FinTech is a key element of Qatar's Strategic Plan to ensure the financial sector's long-term success. Among the four pillars of the Qatar National Vision 2030, FinTech offers substantial opportunities for economic diversification. Most financial institutions, as well as Qatar Development Bank, the QCB, and the QFC, are part of the Qatar National FinTech Task Force that needs to build a strong and sustainable FinTech ecosystem to compete regionally and internationally.

FinTech offers opportunities in a range of fields, including digital payments, remittances, money management, lending, loyalty, and rewards. To determine the value added for each of these FinTech opportunities, it is important to assess their impact financially and strategically, as well as their relevance to customers and compare that to the traditional model. One example where FinTech players are actively venturing into the banking market is Small and Medium Enterprises (SMEs) where many players are switching from banks to FinTech due to the former's strict underwriting criteria, slow credit application processing, and slow credit decisions. FinTech companies are now creating a storm in the market; however, incumbent financial institutions still have the financial trust of their customers. If however, incumbent players decide to side with FinTech rather than compete, they will greatly benefit from the joint value propositions offered by many FinTech companies and enhance the customer experience by taking the best from both sectors.

Qatar could benefit from several factors in helping FinTech grow rapidly. Regulatory support is perhaps the most significant with QCB adopting an increasingly proactive stance towards FinTech. Through an enhanced regulatory framework to help them establish themselves and function effectively, by bringing best practices to Qatar and focusing on country-specific regulations, Qatar is actively working to ensure consistency with international standards.

Non-financial services challengers

Competitive pressure on banks has further intensified with the rise of new non-banking entities such as telecommunication, big tech, and e-commerce companies actively exploring opportunities to extend relationships with their clients through financial services. Regionally, telecommunication companies have been perhaps most active in disrupting banking value chains with primary focus on payments and wallets with the most advanced players touching upon fully-fledged credit propositions with buy-now-pay-later services and revolving credit limits. One of the recent regional examples is Saudi Arabia's STC Pay, which is a product launched by Saudi Telecom that is being converted into a digital bank after its large success. STC Pay's business has been granted a licence by Saudi Arabia's Central Bank, with permission to establish a local digital bank.

Though high street retail, e-commerce and 'big tech' have not been overly active in this space regionally, global trends suggest they have high ambitions for their financial offerings. The likes of tech giants (Apple, Google, Facebook, Tencent), large e-commerce conglomerates (Amazon, eBay) as well as more traditional retailers (Walmart, Tesco) have made serious investments into FS infrastructure – from establishing their own banks to technological white-label partnerships. The latter can be illustrated by the most recent launch of "Apple Pay Later" launched in collaboration with Goldman Sachs as its white label infrastructure and balance sheet provider. Banks in Qatar should actively take note and proactively engage in partnerships with these players, potentially starting with high street retailers as e-commerce is still in its infancy in the country and bigtech is not currently actively targeting Qatar.

> "Rise of 'anything-as-a-service' as an enabler of cross-sector partnerships is perhaps one of the hot topics in financial services today. For the industry players this is an opportunity to seamlessly cover one of the key gaps in clients' value chain whereas the bank gets instant access to an extensive and loyal customer base.
>
> **Dmitry Lukin,** Financial Services Consulting Director, Qatar

Forward looking trends and response strategies

New technology

Digitise yourself to digitise the market

Over the last decade, banking has significantly increased its investments in digital capabilities to remain competitive and meet the needs of modern customers through innovative technologies. The COVID-19 pandemic played an important role in the process challenging the status quo and forcing banks to accelerate their digital transformation efforts. Digital transformation encompasses a broad range of initiatives that – at their core – serve two major goals: (1) enhance all major customer interactions with the bank through the use of technology and (2) do that in a most effective and digitally enabled manner. Simply designing good-looking digital channels like internet and mobile apps or offering hyped up digital features won't work – any successful model will require banks to reinvent their own products, processes, legacy technology, organisation and culture. Hence, transformation requires not only the development of cutting-edge solutions but also means a shift in people's mindsets.On the **external or customer facing side** most of the banks are increasingly active in digitising most client touchpoints in online and physical space: enabling instant and seamless payments, credit, analytics and advisory in internet and mobile banks along with intuitive and client-friendly experience in self-service kiosks, digital queuing and latest gadgets in branches. As over 90% of bank customers in Qatar have used at least one digital banking channel, the banks are actively enabling numerous features that have not been there previously. For example, in November 2021, Qatar Islamic Bank (QIB) became the first bank in Qatar to launch video banking via its mobile app. However, this is just the tip of the iceberg as to enable such solutions, the banks need to fundamentally transform internal operational, organisational, and cultural challenges so that technology is regarded as an enabler rather than an obstacle. Though the challenge and the universe of solutions are vast, here are some fundamental technology enablers that help complete the most critical steps of the transformation journey:

> As banks make informed decisions gathered from cloud market and customers' data, it aids in increasing new products based on identified customer's needs
>
> **Nakul Srivastava,** Technology Consulting Director in PwC Middle East

01

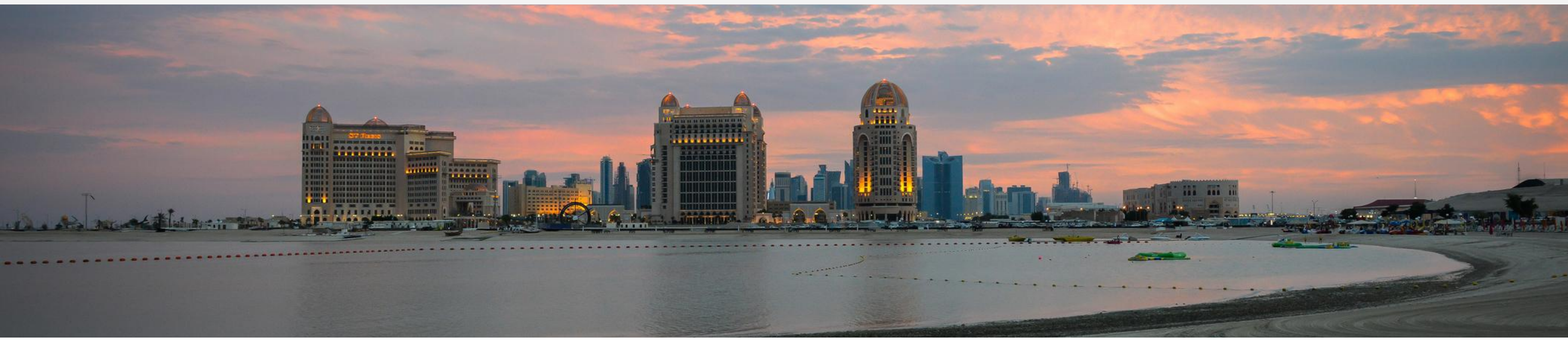
Process and data management solutions are the backbone of any successful transformation as they allow to significantly cut unnecessary steps and automate remaining activities – especially for long, document heavy manual processes that are fairly standard at their core. The use of OCR, data management systems, data warehouses, and highly effective workflow solutions (sometimes with the use of robotics) help optimise internal processes to scale efficiently and deliver quicker services for example, trade-related processes in corporate banking.

02

Shift to **cloud computing** allows a shift from physical servers and their management to a cloud environment, where banks can not only gain cost efficiencies but also mitigate the risk of losing data. Those successfully migrating the workload to the cloud enhance the productivity, market demand, customer satisfaction and create a differentiator for the Bank. This is also an important step for the entire banking ecosystem as it lays one of the steps that enable advanced infrastructure solutions like open banking that further benefit the financial sector and economy as a whole.

03

Data analytics tools serve as the next layer above standard processing solutions that allow harnessing its power. Some of the most popular and impactful use cases are centred around deep personalisation and decision-making based on data trends. Augmenting data with the use of big data, AI and machine learning can help propagate the power of data even further and help banks to innovate customised products and delivery.



Forward looking trends and response strategies

New money

Make the best use of crypto and digital currencies

Despite the global expansion and popularity of cryptocurrency, traditional banks are hesitant to adopt the use of these digital assets believing their inherent risks outweigh their benefits. However, regulators globally are working to change banks' perceptions of digital currencies, confident that these assets can enhance innovation and efficiency among financial institutions.

Whilst virtual assets and crypto are regarded by most as assets, there are some entities that are starting to accept them as currencies. Many countries are currently exploring the establishment of CBDCs (Central Bank Digital Currencies), which would be considered a large leap forward for the digital currencies industry.

Cryptocurrencies are based on a decentralised model; therefore, the role of banks is currently neither in the issuing nor exchange of cryptocurrencies. This affects banks as a portion of transactions are switching from fiat to crypto, consequently, meaning that banks are seeing lower volumes on their balance sheets. Consequently, banks globally are currently thinking about how they can adapt their operating models to accommodate the exchange of cryptocurrencies.

Currently banks are not major players in the crypto market unless they want to develop a crypto business, for example as custodians. Banks are however part of the ecosystem; hence they are perceived as enablers.

Adopting cryptocurrency could enrich, and upgrade financial services. Recent advances in the industry have made it easier for banks to deal with their concerns regarding cryptocurrency, and instead, allow them to recognise the benefits. For example, by securing digital currencies against theft or hacking, banks can ease the concerns of cryptocurrency holders. Likewise, banks can offer crypto accounts with interest, acting as trusted third parties, allowing customers to invest the crypto on the back end or with other financial tools.

In the Middle East region, cryptocurrency is still not being widely adopted, however, this is slowly evolving. For example in Dubai, an entity called the Virtual Asset Regulatory Authority was established to regulate virtual assets such as Bitcoin and non-fungible tokens (NFTs). The purpose of moves like these are clear: to legitimise a promising industry and set the stage for success. Therefore, the regulators want to be part of the big movement toward digitising the financial sector through blockchain and cryptocurrency. FTX, a global crypto exchange, obtained an operating licence in Dubai. In addition to that, Binance, one of the largest crypto providers in the world, established a headquarters in Dubai. A major enabler for flourishing cryptocurrencies is government regulations, and in Qatar so far, regulations have been very restrictive regarding cryptocurrencies.

In Qatar the infrastructure in the banking sector is consistently evolving, however currently regulatory institutions have not accepted the adaptation of cryptocurrencies in the country. In Circular No.6 of 2018, the QCB issued strict guidelines regarding cryptocurrencies.

Furthermore, the QCB advises all financial institutions operating in Qatar not to deal with cryptocurrencies. However, looking at international and regional trends in cryptocurrencies and the popularity of blockchain technology, Qatar will most likely review and potentially adopt cryptocurrencies in the future and put in place a regulatory framework to ensure that it is being utilised in a safe manner.

> **The Middle East has taken a major leap forward in digital assets with several new regulatory measures across the region, which have propelled cryptocurrency mainstream within a very short time**
>
> **Serena Sebastiani,** Financial Services Consulting Director, PwC Middle East

The way banks will approach this immense challenge will determine overall success. Qatar is currently at a critical juncture; it is striving toward modernisation and digitalisation but still has a way to go. Banks in Qatar have at their disposal the opportunities to position themselves within a new global financial structure that will be unleashed by digitalisation. Digital transformation is never-ending, and these efforts at banks tend to be incremental, localised, and fragmented, resulting in a pervasive and pernicious “digital trap”. Having a common language across the institution, using a business-first roadmap, and going from technology stacks to solution stacks are necessary for banks to transform at scale. There are opportunities for banks to create a higher purpose-driven brand identity that embodies authenticity and differentiation, and to empower their customers to make the right decisions by providing access to data, tools, and advice that are personalised and actionable.

Forward looking trends and response strategies

New rules

Foresee and contribute to an evolving regulatory landscape

The nature of the Financial Institutions, their operations and customer expectations are evolving and require regulators to adopt quickly to the fast-paced environment. The growing complexity of Financial Services, Neobanks and a wider Financial Ecosystem have resulted in a changing supervisory approach focusing on a vertical and horizontal integration.

Central Banks are shifting to functional supervision with a wider supervisory perimeter that expands to non-financial institutions offering financial services and expands over the whole FS value chain that includes clients, vendors, and competitors. Moreover, the regulation development process itself is changing – Central Banks around the globe are actively engaging industry stakeholders to shape future ground rules.
In the MENA region, key ‘Wave 1’ supervisory initiatives remain focused around core banking business and cover customer and data protection, establishing data infrastructure and ESG.

01

Customer protection: Customer protection is one of the key objectives of every Central Bank as regulators across the world have introduced Conduct Principles for the regulated entities. Regionally, Central Banks have recently updated their consumer protection regulations focusing on customer education, fair pricing, including use of annual percentage rates and customer data disclosure. Regulators in the region launched special programmes to ensure customer protection in respective jurisdictions, SAMACares being the prime example of such initiatives. Customer protection is at the heart of QCB operations delivered through a dedicated Customer Services Protection Department.

02

Data protection and Cybersecurity: As technology evolves, the volume of data exchange between market participants increases exponentially – both on the customer side with frequent interactions via digital channels and financial institutions themselves, including new market participants such as digital banks, P2P lenders and crowdfunding platforms. Digitisation of the Financial Institutions, new digital players and changing customer behaviour result in increased cybersecurity risks with cybersecurity being included in the BIS innovation hub work programme for the years 2022 and 2023. In line with the global trends, Central Banks in the MENA region have updated and enhanced their cybersecurity regulations. Qatar is at the forefront of the Cybersecurity domain and has developed a National Cybersecurity Vision to combat against the threats. QCB plays a vital role in delivering the vision through the robust technology risk regulations, issued in 2018, including cybersecurity risk in the Risk Based Supervision Model as a separate pillar. Further, QCB is in the process of issuing security controls applicable to FinTechs.

03

Data Infrastructure. In the era of technology, one major challenge regulators face is building an infrastructure where accurate, available, and complete data enables analytics-enabled decisions and ensures financial system stability. Data flows are extensive and cover both traditional information exchange with supervised entities like commercial banks, as well as partnering with Credit Bureaus, Ministries and other government-related bodies and even commercial players (like Telecommunication and Big Tech companies). QCB has intensified its efforts in building a data ecosystem investing in new data collection with Credit Bureau, development of new data exchange standards under risk-based supervision and working with the FinTech community focused on data collection and management.

04

ESG: Environmental, Social and Governance matters gain importance across the world as well as in the MENA region. Unlike more mature markets like Western Europe, the regional regulatory landscape around ESG remains fragmented with individual Financial Institutions often leading the charge. However, we anticipate active development and consolidation of individual standards into a comprehensive set of rules. Saudi Central Bank can be used as an example, first publishing Key Principles of Governance in Financial Institutions and further initiating a preliminary assessment on climate related financial risks to better understand the impact, nature, and level of the exposure. In Qatar, the situation is no different: although QCB have not yet published overarching guidelines on ESG yet, Environment and Social Pillars are embedded into the National Vision and will force the regulator to put the full framework in place.

Forward looking trends and response strategies

On top of immediate focus areas, more advanced 'Wave 2' global trends are becoming more prominent in the region making regulators set future state priorities that evolve around Open Finance, supervision of the digital transformation strategies, Central Bank digital currencies, Suptech and Regtech, and next generation Financial Markets infrastructure.

> **Supervisors need to adapt quickly to the recent digitisation trends, new entrants and changing customer behaviours to enable the whole ecosystem as well as ensure the financial stability and customer protection in their respective jurisdictions.**
>
> **Sandeep Srivastava,** Middle East Consulting Financial Services Lead

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