

"The future of finance is digital"¹

DIGITAL TRANSFORMATION IN ALBANIAN BANKING SYSTEM

Banks Digitalization Survey 2024

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¹ Digital Finance Strategy for the EU.

What is Digital Transformation in Banking?

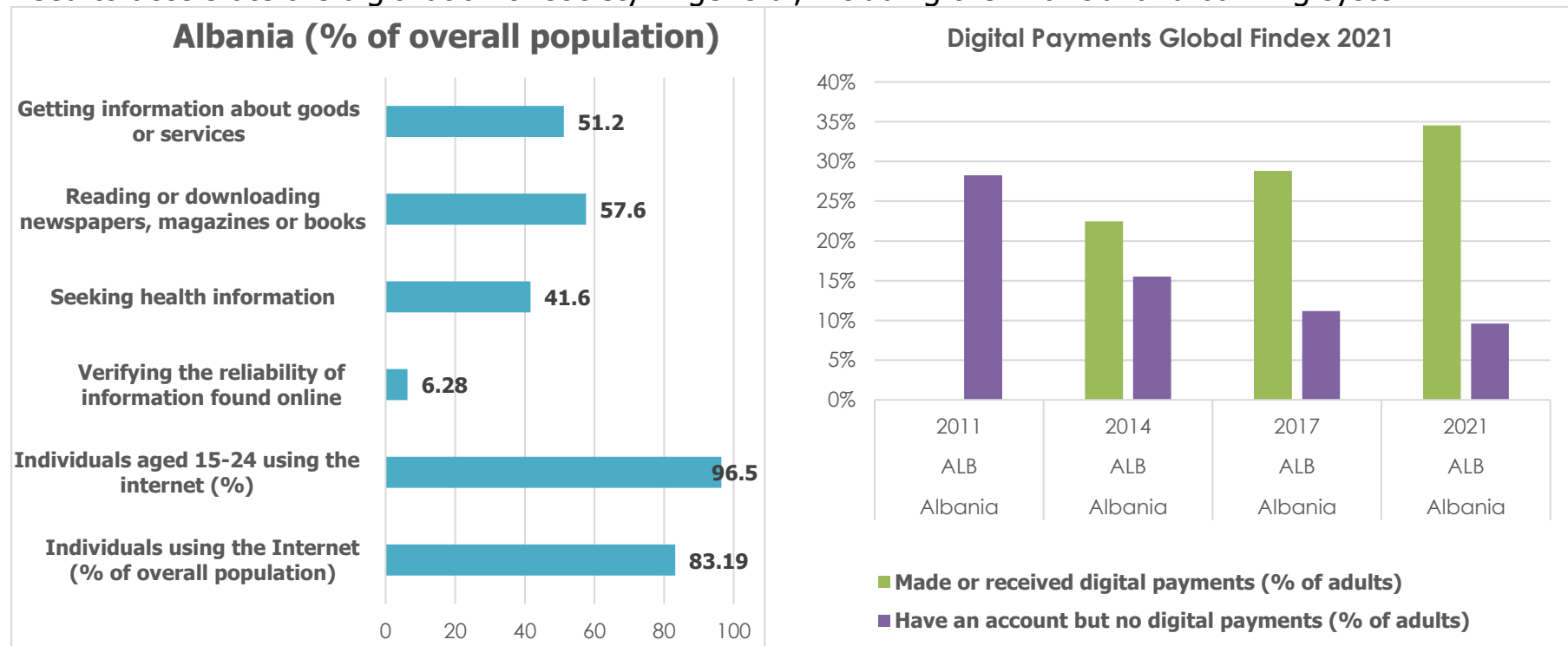
Digital transformation in banking encompasses the modernization of processes, products, and services through the adoption of digital technologies, known collectively as FinTech.

This shift involves more than just adopting new technologies.

The demand for banking digitization is also reinforced by **the shift in society to the digitalization era.**

Digitalization Trends in Albania

In Albania, by ITU, 83.1% of the population had internet access in 2022, compared to 76% in 2021. But there is a gap in digital literacy, with ICT literacy scores rarely exceeding 55%. The above figures show us that there is a need to accelerate the digitization of society in general, including the financial and banking system.



Banks Digitalization Survey 2024

Recognizing the importance of understanding current trends and challenges in the banking digitalization journey, the Bank of Albania conducted its annual FinTech Survey in September 2024.

Objective of the 2024 Digitalization Survey

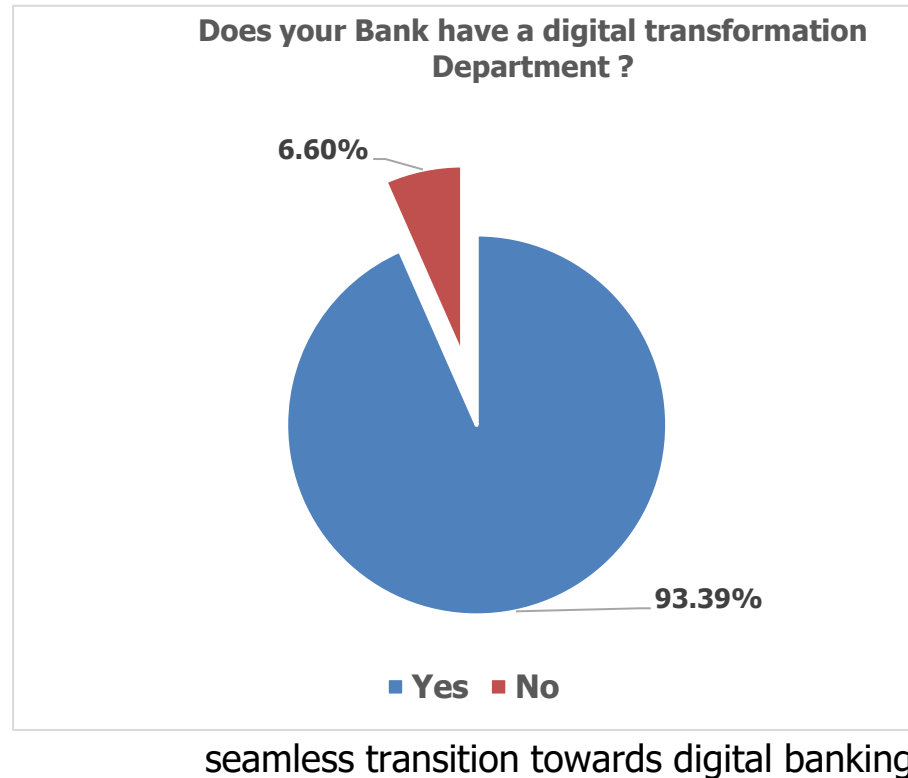
This survey aimed to gather insights into the current state of digital transformation within Albania's banking sector, focusing on the drivers behind digital initiatives, technological adoption, and preparedness to manage associated risks.

The survey collected responses from 10 banks, representing a substantial share of the Albanian banking market as of August 31, 2024. Questions were categorized into three main areas:

1. Drivers and Challenges of Digital Transformation – Assessing the motivations for adopting FinTech solutions and identifying obstacles to implementation.
2. Adoption of New Technologies – Understanding the areas of banking where digital projects are being prioritized.
3. Risk Management and Support Needs – Gauging the potential risks associated with FinTech and evaluating how prepared banks are to mitigate these risks.

The findings offer a comprehensive view of digitalization in the banking sector, shedding light on where Albanian banks stand in their digital transformation journey and how the Bank of Albania can support this critical shift.

Dedicated Digital Transformation Departments

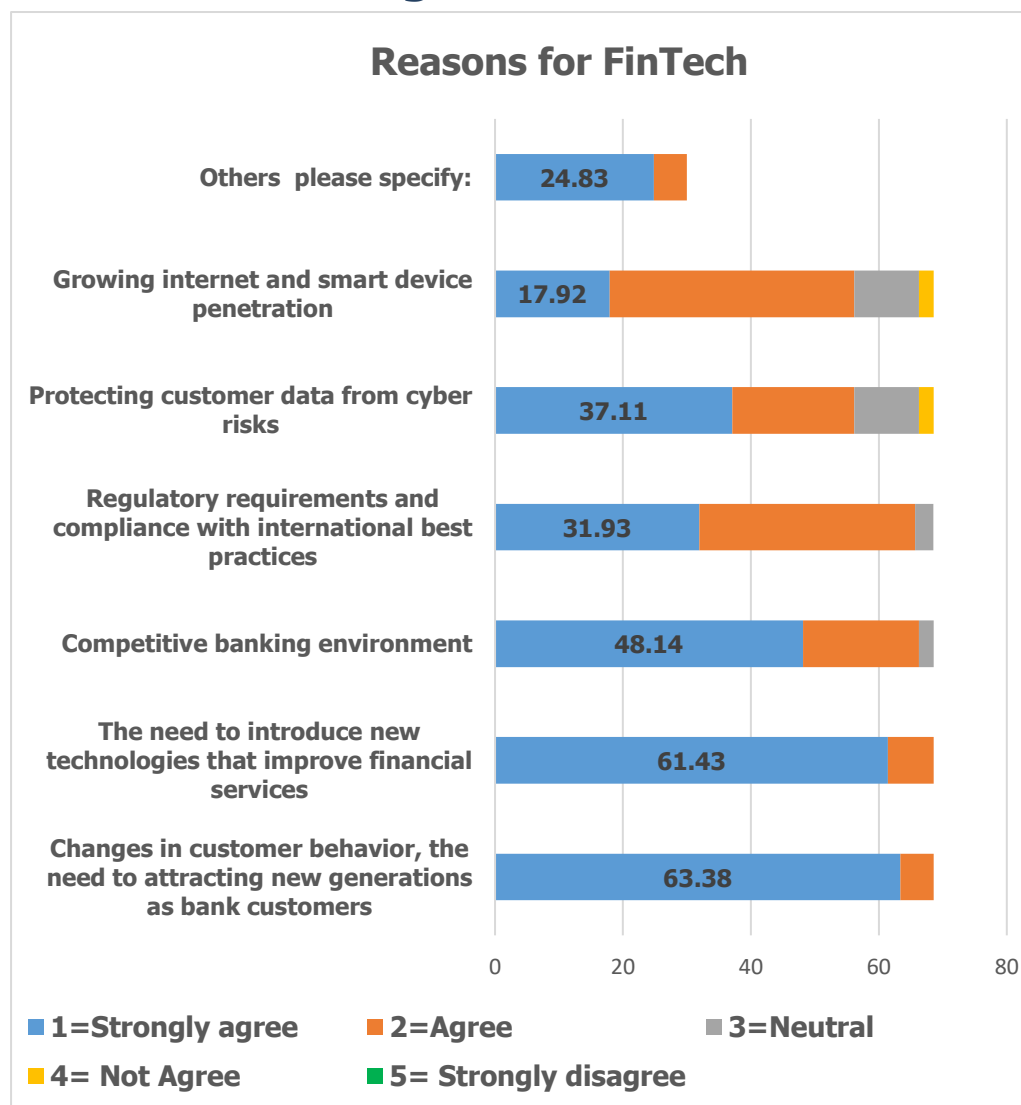


This widespread adoption of digital transformation departments reflects **a strong commitment by Albanian banks to embrace technological change.**

Specifically, 10 banks, representing **93.39% of the total assets in the banking sector, have established dedicated digital transformation departments** or teams focused on FinTech projects. Only one bank, accounting for 6.60% of the sector's assets, reported the absence of a digital transformation function.

By allocating resources to focused teams, these banks are better positioned to expedite digital initiatives, integrate innovative financial technologies, and foster a

The drivers of digital transformation



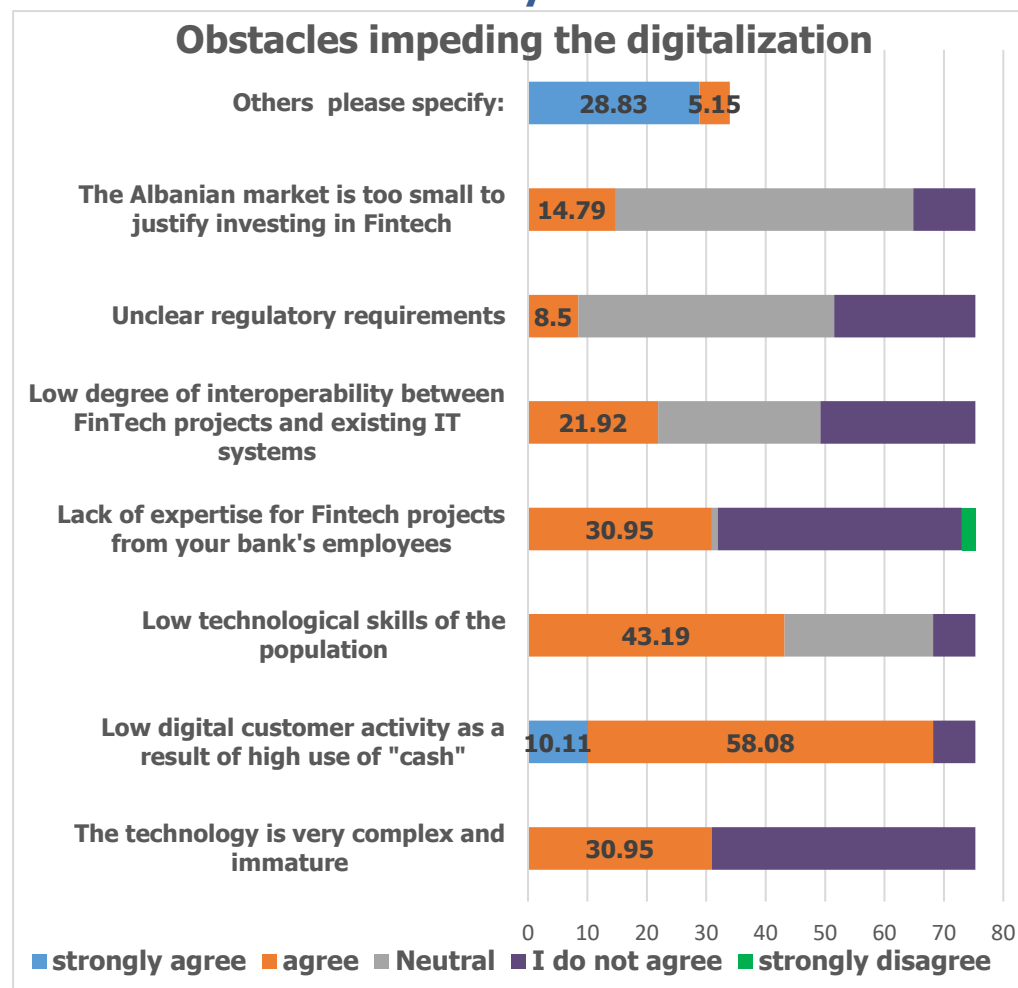
Key drivers for FinTech investments in Albania's banking sector:

- Customer-Centric View:** The shift from a product-centric to a customer-centric view is evident, with seven banks (representing 63.4% of total assets) strongly agreeing and two banks (5.18%) agreeing that **"changes in customer behavior" and the need to attract new generations are primary reasons for FinTech investments.**
- Technological Advancements:** Eight banks, representing 61.43% of assets, indicated that the desire to introduce technologies that enhance financial services is a significant motivation behind their FinTech projects.
- Competitive Banking Environment:** Five banks (48.14% of assets) cited **"changes in the competitive banking environment"** as a reason to adopt digital solutions.
- Regulatory Compliance:** Four banks (31.93% of assets) identified regulatory requirements and alignment with international best practices, an additional three banks (33.7% of assets) agreed that compliance with global standards encourages FinTech adoption.
- Cybersecurity Concerns:** The need to protect customer data from cyber risks has also influenced FinTech investment. Five banks (37.2% of assets) strongly agreed that safeguarding consumer data is a crucial factor in their digital transformation efforts.

Challenges of digital transformation

Digital journey is not without significant challenges.

Key obstacles that banks in Albania face as they adopt FinTech solutions:



strong regulations and slower-moving third-party vendors, making it challenging to keep pace with agile FinTech firms.

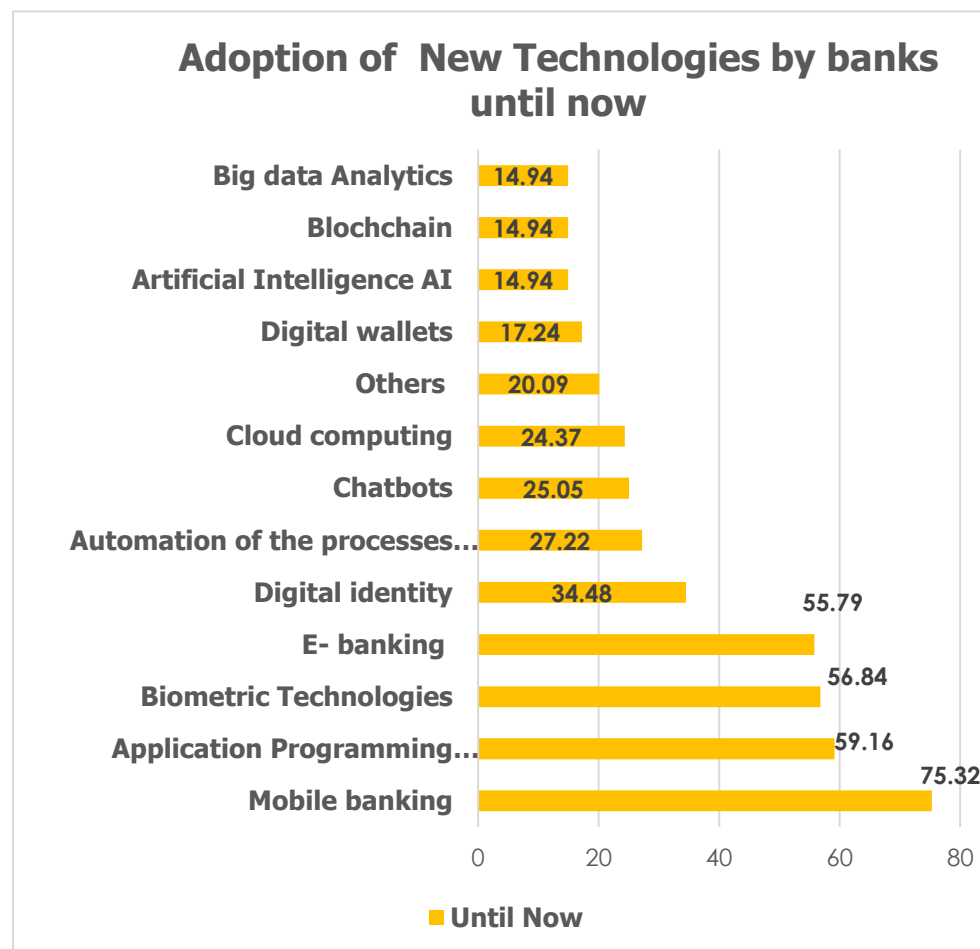
- 1. Low Digital Customer Activity:** Nine banks, representing 68.19% of the sector's total assets, agreed and strongly agreed that "low digital customer activity" impedes digital transformation efforts.
- 2. Low Technological Skills in the Population:** Seven banks, holding 43.2% of total assets, agreed that "low technological skills of the population" are a barrier to digitalization.
- 4. Internal Expertise for FinTech Projects**
Some banks noted challenges in developing internal expertise for FinTech projects. While 41.02% of banks disagreed with the statement "lack of expertise for FinTech projects from bank employees," indicating they have the necessary skills, 30.95% acknowledged that limited internal expertise is a hindrance to digital initiatives.
- 5. High Investment Costs and Cybersecurity Risks**
The high costs associated with FinTech investments and increased cybersecurity risks were additional concerns.
- 6. Regulatory Barriers and Compliance Challenges**
One bank noted that "regulatory barriers related to third-party providers for distance identification and electronic signatures" pose significant obstacles. Additionally, concerns around unclear regulatory requirements.
- 7. Competitive Disadvantages Compared to FinTech Startups**

One bank highlighted the agility advantage that FinTech startups possess, which allows them to innovate more swiftly compared to traditional banks. Established banks often rely on

New Technologies

The survey reveals that Albanian banks have embraced a variety of digital technologies as part of their transformation journey.

Key technologies currently in use include:

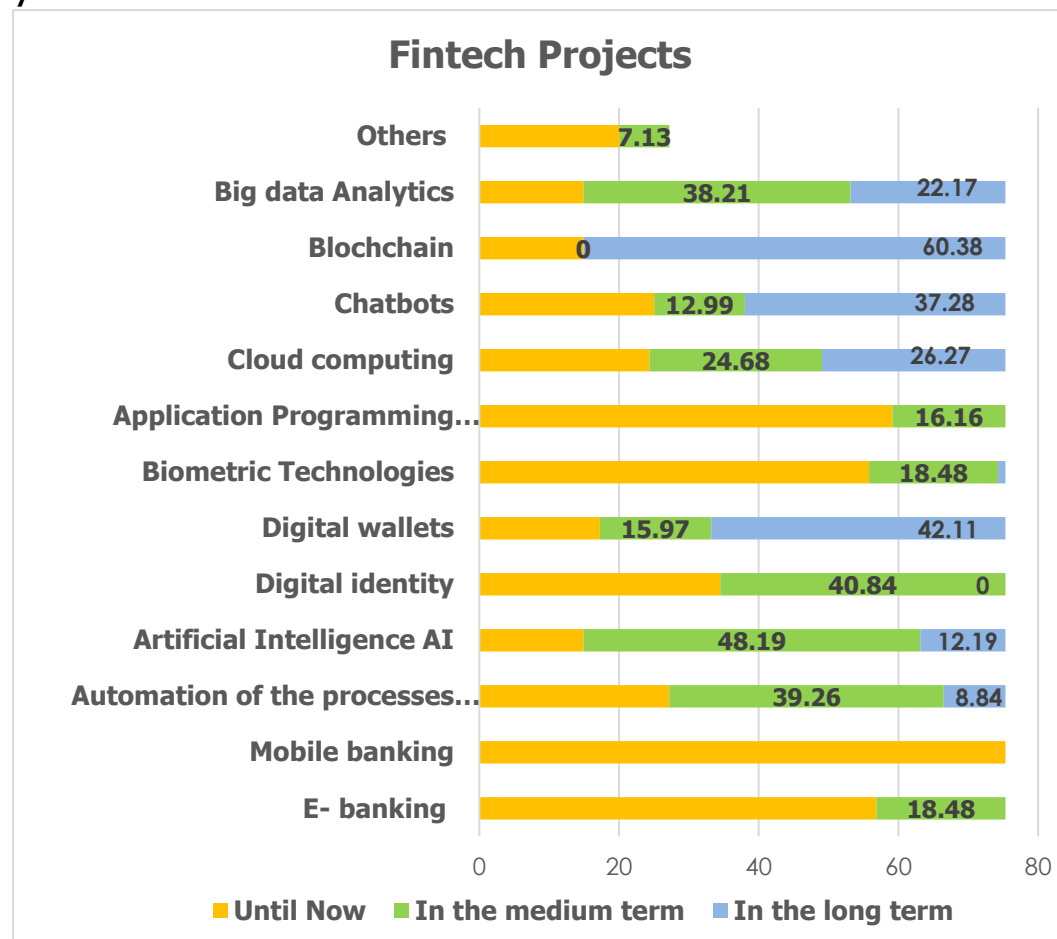


- **Mobile Banking:** Adopted by all banks, mobile banking has become an essential part of Albania's digital banking landscape. This technology allows customers to perform essential banking tasks—checking balances, transferring funds, and viewing transaction histories—directly from their smartphones, providing 24/7 access and convenience.
- **Application Programming Interfaces (APIs):** APIs, implemented by 59.16% of banks, facilitate data sharing and integration, enhancing customer experience by enabling seamless interactions with third-party applications. APIs allow banks to connect with new markets and drive innovation by enabling developers to build custom integrations.
- **Biometric Technologies:** With 56.8% of banks utilizing biometric technologies, security and identity verification have become more robust. Biometric systems improve the security of digital transactions by using fingerprint, facial recognition, or other biometric data to authenticate users.
- **E-Banking:** Adopted by 55.9% of banks, e-banking enables a range of services to be performed online, reducing the need for physical bank visits and enhancing customer accessibility.
- **Digital Identity:** Currently used by 34.48% of banks, digital identity solutions facilitate secure, remote identity verification, an essential component of online banking and digital transactions.

Future FinTech Projects

Banks have laid out strategic plans to introduce additional FinTech innovations in the coming years:

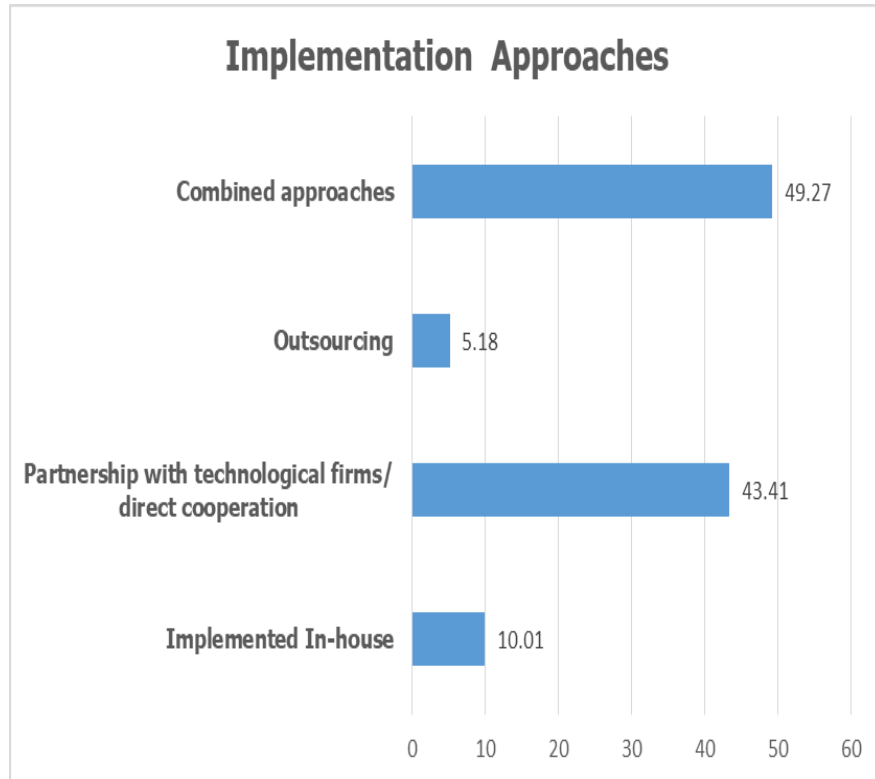
Key future developments include:



- **Digital Identity:** Currently in use but planned for expansion, digital identity technology will see medium-term development in 40% of banks.
- **Digital Wallets:** While still in early stages, digital wallets are projected for long-term implementation by 42.11% of banks, indicating growing interest in providing mobile-based payment solutions.
- **Artificial Intelligence (AI):** Planned for medium-term adoption by 48.19% of banks and long-term by 12.2%, AI is expected to enhance analytics, customer service, and fraud detection capabilities.
- **Blockchain and Chatbots:** Blockchain is anticipated for long-term adoption in 60.38% of banks, while chatbots are projected to be fully developed in 37.2% of banks in the long term, aiming to automate customer service interactions.

Implementation Approaches for FinTech Projects

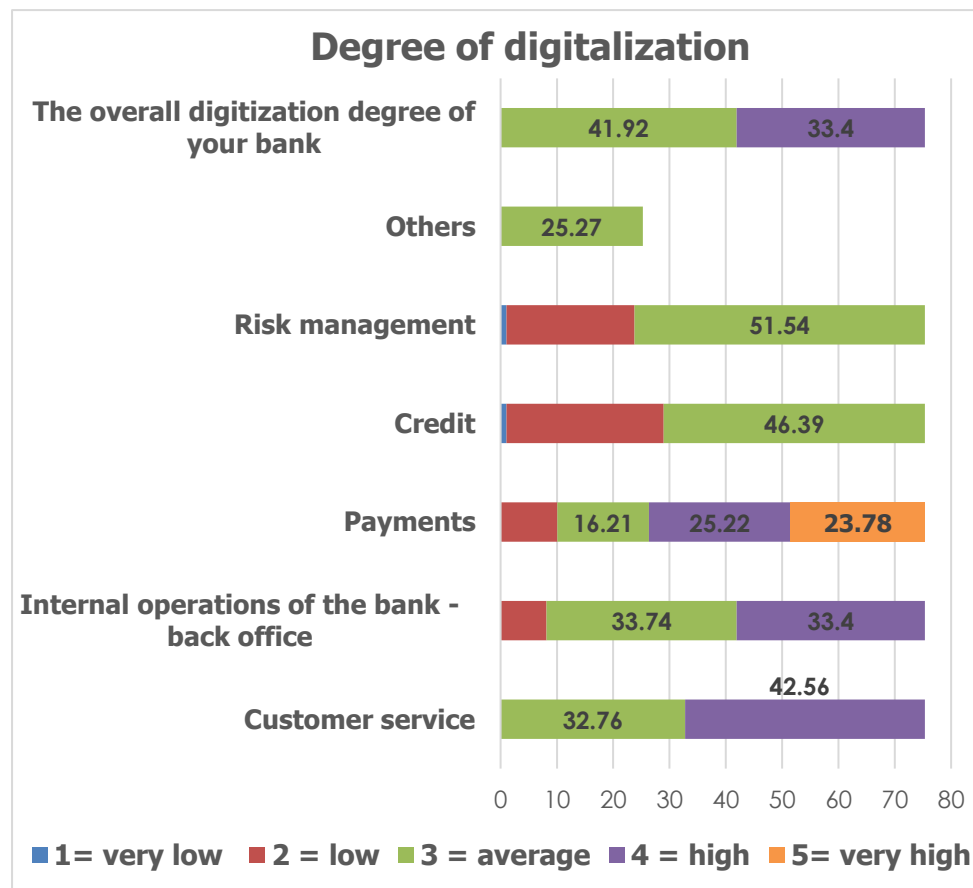
To execute these projects, banks employ different implementation strategies :



- **Combined Approach:** Nearly half (49.27%) of banks utilize a combined approach, balancing in-house development with partnerships with technology firms. This hybrid model allows banks to leverage external expertise while retaining control over core processes.
- **Partnerships with Technology Firms:** Approximately 43.41% of banks prefer direct partnerships with technological firms. By collaborating with external partners, banks can acquire advanced skills and accelerate time-to-market for FinTech solutions.
- **In-House Development:** About 10.01% of banks rely solely on in-house resources, demonstrating their capability and confidence in managing digital projects internally.
- **Outsourcing:** A small percentage (5.18%) use outsourcing to implement their digital projects, opting for third-party expertise to drive innovation. Partnerships with FinTech firms are essential, by fostering proactive partnerships, banks can overcome digital transformation challenging.

BANKS EVALUATION OF THEIR DIGITALIZATION DEGREE.

Overall, 42% of banks rated their digitalization level as **“average,”** while 34% rated it as **“high.”** These self-assessments underscore the sector’s ongoing journey towards a fully digitized operational framework.

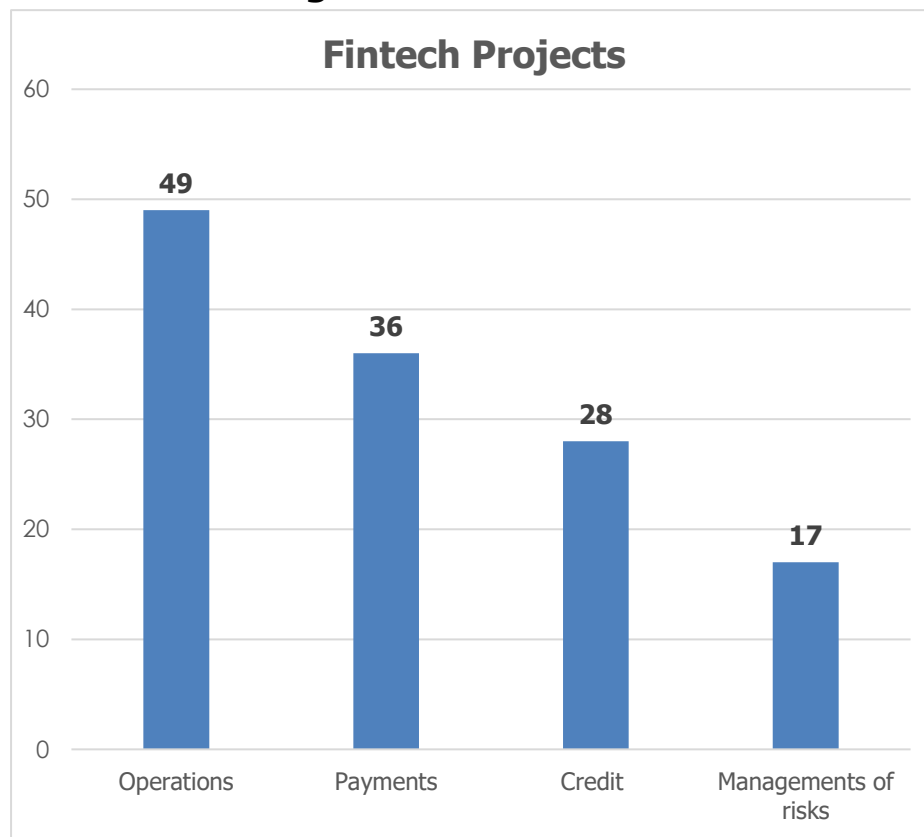


Key findings by business area:

- **Payments:** Payments emerged **as the most digitized area**, with 23.78% of banks indicating a **“very high”** level of digitalization and 25.22% reporting a **“high”** level. This aligns with global FinTech trends, as digital transformation in banking often begins with payment services, which are crucial for customer convenience and engagement.
- **Customer Service:** The second most digitized area is customer service, where 42.56% of banks rated their digitalization as **“high.”** This focus reflects the sector’s growing emphasis on enhancing customer experience through digital channels and automation.
- **Internal Operations (Back Office):** Internal operations have seen moderate digitization, with 33.4% of banks rating this area as **“high.”** Digital transformation in back-office functions is essential for operational efficiency and cost reduction, **yet many banks are still in the early stages.**
- **Credit and Risk Management:** Credit services and risk management **remain the least digitized areas.** Around 27.88% of banks reported a **“low”** degree of digitalization in credit

services, with some even indicating a **“very low”** level. Similarly, risk management has limited digital adoption, reflecting the sector’s conservative approach to these high-stakes areas.

The number of projects indicate and reconfirmed that the least digitized area of bank's operation is the risks managements and the credit area.



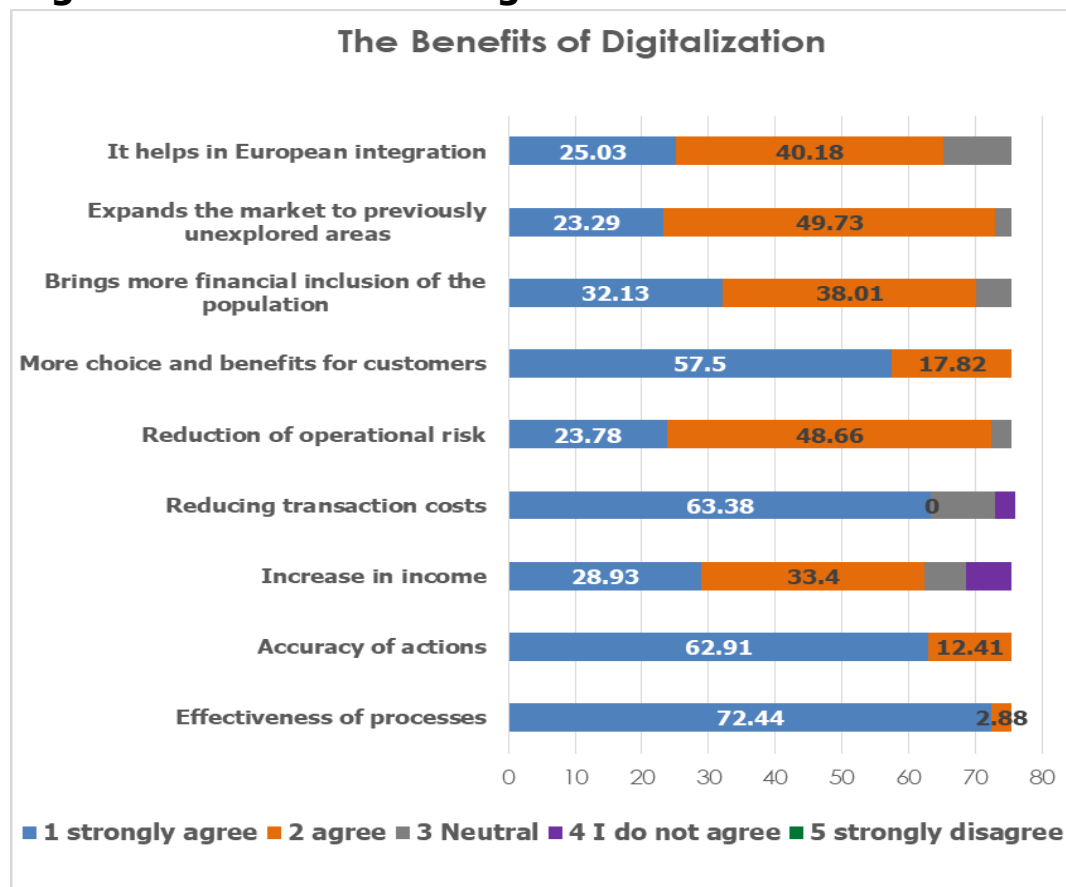
risks associated with digital innovations.

Project Distribution Across Core Activities

- **Operations:** With 49 projects, operations are the primary focus for FinTech initiatives. Key projects include digital communication and confirmation with customers, internal process updates for business clients, back-office process digitization, document collection automation, and chatbot integration to improve customer service.
- **Payments:** Payments account for 36 projects, reinforcing this area's importance in digital banking. FinTech innovations in payments are critical to ensuring seamless, efficient, and secure transactions, enhancing both customer satisfaction and operational efficiency.
- **Credit:** There are 28 projects focused on credit services, highlighting a growing interest in automating and digitizing loan-related processes. Although still in its early stages, digital transformation in credit aims to streamline approval processes, enhance data-driven lending, and improve customer experience.
- **Risk Management:** With 17 projects, **risk management is the least digitized area.** This limited focus on digital risk management may reflect a cautious approach, as banks seek to **ensure regulatory compliance and mitigate the potential**

THE BENEFITS OF DIGITALIZATION

Exploring the benefits of digital transformation is crucial, as it helps assess the tangible impact of digitization on the banking sector.

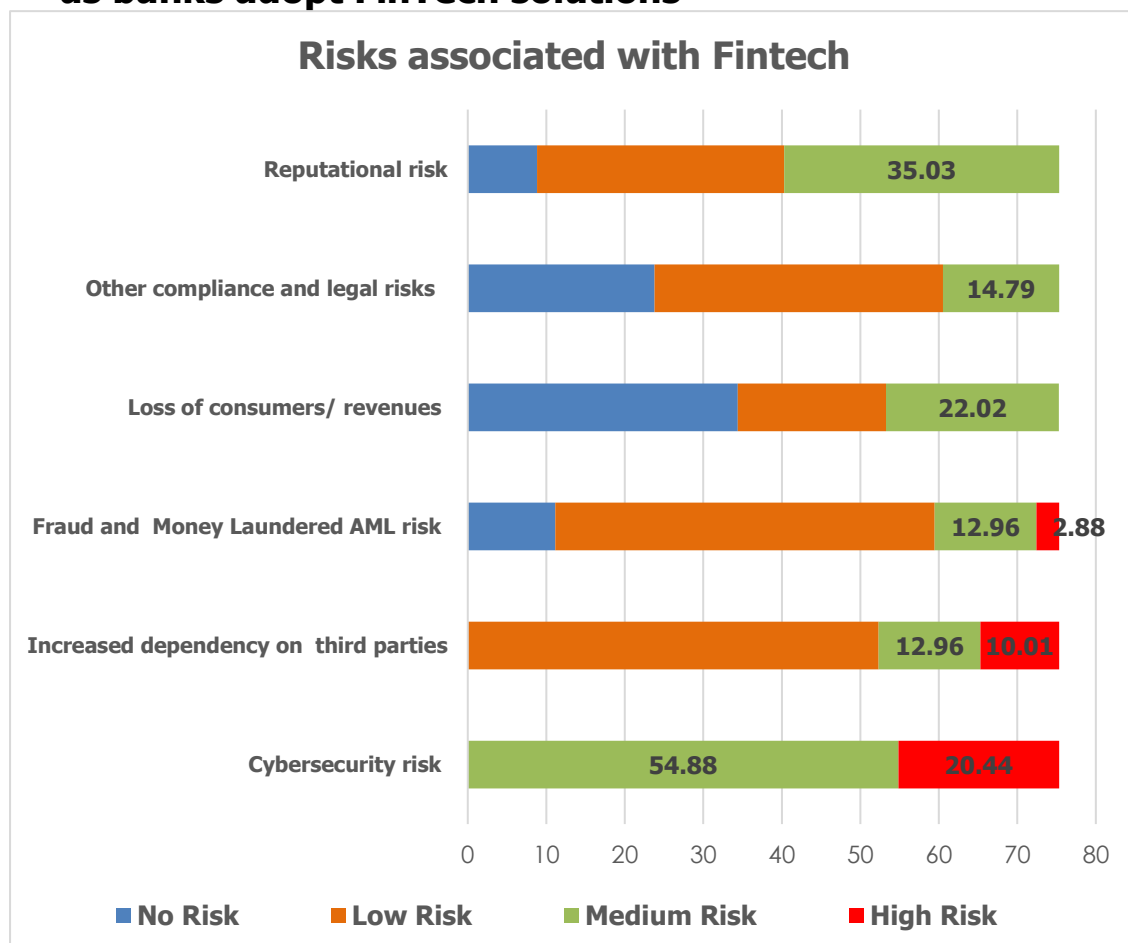


Key Benefits:

- **Effectiveness of Processes:** Ranked as the most significant benefit, 72.4% of banks "strongly agreed" and 3% "agreed" that digitization enhances the effectiveness of banking processes.
- **Accuracy of Actions:** Closely linked to process effectiveness, the improvement in accuracy through digital solutions is another notable advantage.
- **Reducing Transaction Costs:** While the majority of banks recognize cost reductions as a benefit, some responses were neutral, and a small percentage disagreed.
- **Enhanced Customer Choices and Benefits:** Approximately 57.5% of banks "strongly agreed" and 17.82% "agreed" that digitization offers customers more choices and benefits.
- **Expansion into New Markets:** Digitization is also seen as a means to expand into previously unexplored areas of banking, with 49.7% of banks agreeing that FinTech opens new market opportunities.
- **Financial Inclusion and European Integration:**

KEY RISKS

While digital transformation brings numerous benefits, it also introduces specific risks, particularly as banks adopt FinTech solutions

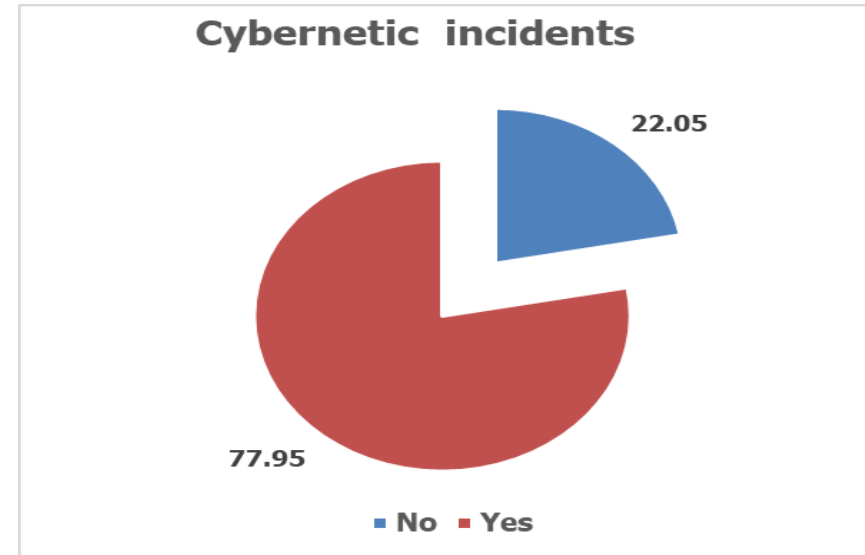
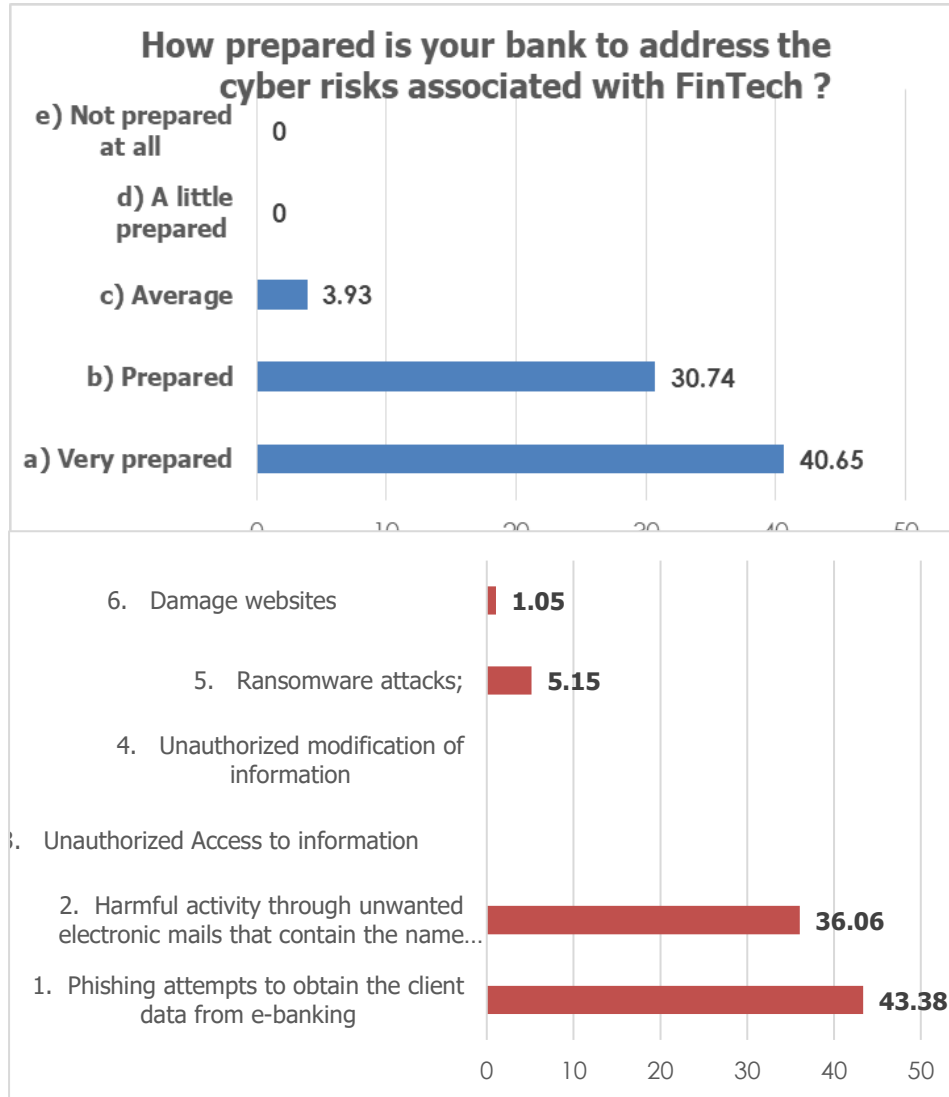


18.87% saw it as a "low risk." This suggests that while customer retention is a concern, most banks feel confident in their ability to retain clients despite digital transformation risks.

- **Cybersecurity Risks:** Identified as the top concern, cybersecurity risks were rated as "high" by 20.44% of banks, while 54.88% considered them "medium" risks
- **Dependency on Third Parties:** Increased reliance on third-party service providers was the second-highest risk, with 10.01% of banks identifying it as a high risk and another 12.96% as a medium risk.
- **Compliance and Legal Risks:** Compliance with regulatory requirements and managing legal risks associated with FinTech were also concerns. Banks must ensure that their digital transformation efforts comply with regulations, especially as they partner with external tech providers.
- **Risk of Fraud and Money Laundering:** Fraud and anti-money laundering (AML) risks are heightened in a digital environment. Banks must implement advanced fraud detection mechanisms to mitigate these risks, with some respondents identifying this as a significant area of concern.
- **Reputational Risks:** As digital services become more prominent, any disruption, such as a data breach or service failure, can harm a bank's reputation. Reputational damage not only affects customer trust but can also have long-term financial implications.

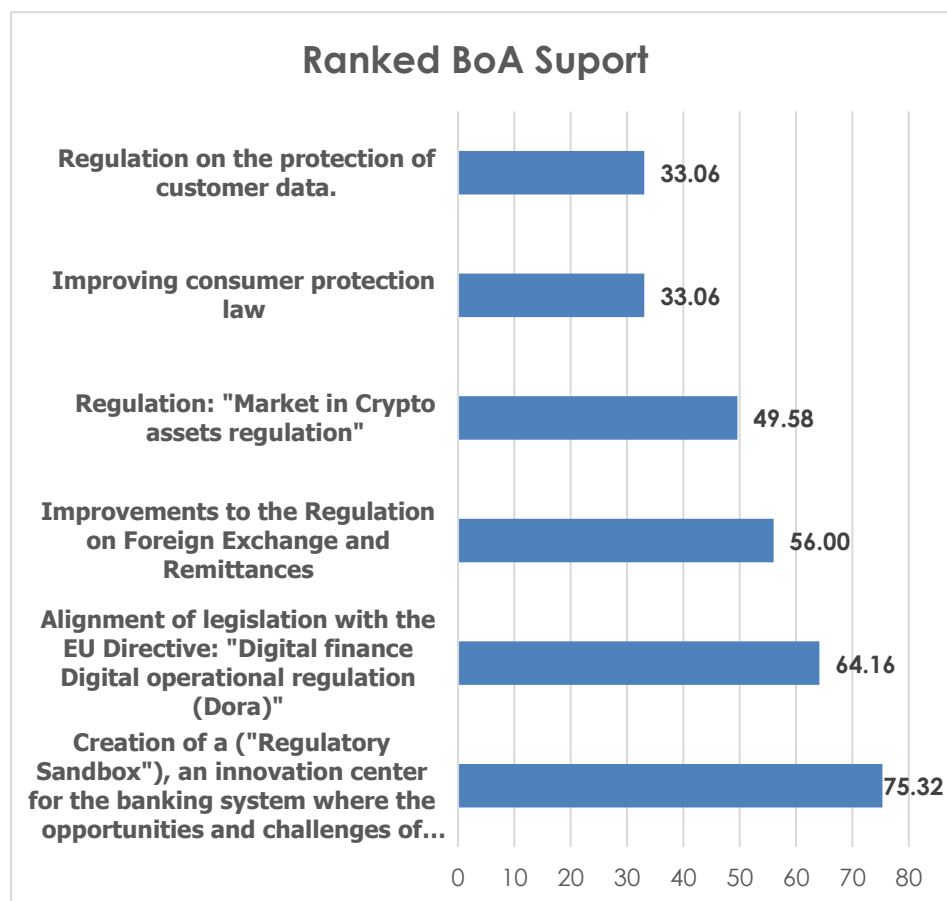
- **Potential Loss of Consumers/Revenues:** Interestingly, 34.4% of banks considered the risk of losing consumers or revenue as negligible ("no risk"), while

When asked about their readiness to address cyber risks associated with FinTech, banks showed confidence in their preparations.



- About 40.65% of banks rated themselves as "very prepared," while 30.74% felt "prepared".
- 78% of banks reported experiencing cyber incidents, while 22% indicated they have not faced such issues.
- Phishing attacks are the most common cybersecurity incidents, targeting customers directly to obtain sensitive information such as internet banking credentials and credit card details. One bank specified that "Phishing attempts have always been a threat vector, and the bank have not noticed an increase in phishing attempts specifically targeting new digital projects".

How can the Bank of Albania support the digital transformation of banking system in Albania?



The responses of this question we sorted by "strong agree" affirmations, so to emphasize the most critical areas where banks feel the Bank of Albania's support is needed.

1. All banks unanimously supported the creation of a **"Regulatory Sandbox"** where the banking sector can explore and test innovative digital solutions in a controlled environment. This initiative was "strongly agreed" by 35.69% of banks and "agreed" by 39.63%.

2. Alignment with EU Directives: Nearly half (45.12%) of banks "strongly agreed" and 19.04% "agreed" that BoA's support should include aligning Albanian regulations with **the EU Directive on Digital Finance (DORA)**. This alignment is seen as essential to ensure consistency with European standards, facilitating smoother cross-border operations and enhanced regulatory compliance.

3. **Regulation of Foreign Exchange and Remittances:** The third most requested area of support is the improvement of regulations around foreign exchange and remittance services, with 31.81% of banks "strongly agreeing" and 24.19% "agreeing." Given the significance of remittances in Albania, modernized regulations in this area could enhance service efficiency and reduce transaction costs.

CONCLUSIONS

The digital transformation of Albania's banking sector has been driven by:

- evolving customer behavior,
- the need to attract new generations of customers,
- the imperative to protect customer data from cyber risks
- and the desire to stay competitive in an increasingly FinTech-driven environment

Digitalization has become **a structural** trend in Albanian banking, prompting a **shift from a product-centric to a customer-centric business model**.

The payments sector is currently **the most digitalized area in Albanian banking**, indicating that the industry is in the early stages of its FinTech development lifecycle. Digitalization is a journey and ask for a continual adaptation of evolving technologies in all banking area business.

This survey demonstrates that Albania's banks have embraced **a collaborative approach**, working closely with technology firms to drive their digitalization efforts.

To this end, **Mobile banking, APIs (Application Programming Interfaces), Biometrics Technology** and E- Banking are increasingly playing a key role in digitalization of banks.

Mobile banking, in particular, has been widely adopted by all banks in Albania, underscoring its importance as a critical component of the digital banking landscape.

At the same time, emerging technologies such as **Cloud Computing, Digital Wallets, and ChatBots** are anticipated to play a significant role in **the medium term**.

CONCLUSIONS

As banks increasingly adopt digital financial services, **they also face a higher risk of cyberattacks**, which represent a new type of threat in the digital era.

Banks showed confidence in their preparations to address cyber risks associated with FinTech.

There is a call from banks for the **Bank of Albania to lead efforts in increasing digital literacy and financial awareness among the population**. This digital education would foster greater adoption of digital services, making financial inclusion a reality for more Albanians.

Furthermore, banks support the creation of **a Regulatory Sandbox**—an innovation hub for the banking sector—to explore new opportunities and tackle challenges in a controlled environment.

Digital transformation is more than just moving from traditional banking to digital; it is a fundamental change in how banks operate, interact with customers, and deliver services, as a bank's CEO noticed ***"we had to reinvent our banking business"***.

The results of this survey are encouraging that with the right measures in place, Albania's banking sector can continue its progress on this transformative journey, building a future-ready industry that meets the evolving demands of the digital era.

THANK YOU
FOR YOUR KIND ATTENTION!