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The Path to Profitability

Can Malaysia's Digital Banks
Beat the Odds?

When Malaysia granted five digital banking licenses in 2022, the mood was electric. Fintech pioneers promised to rewrite the rules of banking through faster onboarding, smarter credit, and financial inclusion for the 55% of the Malaysian population that were at the time unbanked or underbanked.¹ A few years later, that optimism has waned. Despite bold launches and deep-pocketed backers, Malaysia's digital banks are discovering that innovation alone does not pay the bills.

The path to profitability for digital banks is proving tougher than expected – constrained by cautious regulations, modest deposits and the high cost of earning trust in a relatively conservative market. While most have focused on rapid customer acquisition through lavish incentives, few have succeeded in cracking the code on retention, monetization or scale.

In this article, we examine the real economics of Malaysia's digital banks, exploring:

- Why profitability remains elusive despite high digital adoption and inclusion mandates
- How are regulatory limits and thin-file customers constraining early growth
- Two strategic models and the different routes they offer towards financial sustainability
- The universal success factors separating tomorrow's winners – ecosystem partnerships, data-driven innovation and frictionless design
- The roadmap from wedge product to full-stack platform, showing how digital banks can evolve from niche players into trusted financial ecosystems.

The digital disruption of Malaysian banking has not fizzled out – it is merely entering its endurance phase. The question now is not who can grow fastest, but who can build lasting value once hype fades.

Malaysia's Digital Banks: The Profitability Challenge

Malaysia's digital banks are entering a competitive market with strong incumbent players and increasingly discerning customers.² While initial adoption has been encouraging, several structural and strategic hurdles continue to impact their plan to sustainable profitability. Below we set out the key challenges shaping their early journey.

Customer acquisition over retention and monetization.

Early digital banking strategies have largely emphasized rapid customer acquisition, often through high-yield deposit incentives (typically around 3% in the first year of launch) or unlimited card cashbacks. While these short-term promotions attract customers, many disengage soon after. Too little attention has been given to deepening relationships or driving sustained engagement and stickiness through personalized products or value-added services. Without a clear retention strategy or phased product roadmap, digital banks remain trapped in an endless cycle of expensive acquisition with limited returns in terms of lasting customer loyalty.³

Modest deposit bases limit growth. Even when digital banks succeed in onboarding customers, another challenge quickly emerges: deposit volumes. Average deposit sizes per customer remain far lower than those held by traditional banks.⁴

Our work with banks shows that a major contributor is the lack of trust in digital banks – particularly in emerging markets. In these markets, financial literacy is still developing, and consumers often prefer the familiarity and perceived safety of incumbent banks. Unless digital banks can unlock higher-value customer segments early on, they risk burning through capital before reaching profitability.

This constraint significantly limits their ability to expand lending portfolios or convert deposits

into fee-based income streams such as wealth management, insurance or investment products. Markets like Hong Kong, Japan and Korea benefit from higher average deposit volumes and stronger customer “stickiness.” In contrast, SEA digital banks often see customers withdraw funds once promotional rates end, reverting to their primary banking relationships.

Hard cap on digital banks' retail deposits.

Compounding these challenges, regional regulators have also imposed hard caps on digital banks' retail deposits. For example, in Malaysia, while the regulatory sandbox is slightly more flexible, the foundation phase imposes meaningful restrictions: total assets cannot exceed RM3 billion, and capital requirements must increase from RM100 million to RM300 million by the end of the phase.⁵ Although this phased approach offers room for gradual growth, it also constrains scale in the early years, especially when compared to the country's major incumbent banks.

Regulatory mandates vs. market conditions.

In countries such as Malaysia, digital banks operate under a clear regulatory mandate from Bank Negara Malaysia (BNM) to serve the unbanked and underbanked population. While this mission aligns with financial inclusion goals, it presents a complex operational challenge.

Thin-file customers with little or no formal financial history are difficult to assess using conventional credit scoring methods. Digital banks must therefore rely on alternative data models during onboarding, including eKYC (electronic Know Your Customer) procedures and behavioral analytics, requiring significant technological investment, resulting in rising customer acquisition costs.

However, BNM requires exceptionally high accuracy in these assessments – often at a level that may be considered unrealistic. In mature

markets such as South Korea or Japan, top-performing digital banks typically achieve around 90% accuracy at best. This leaves Malaysia's digital banks in a difficult position.

Unable to meet the stringent accuracy requirements, they may be forced to turn away the very customer segments they were licensed to serve. The result is a strategic contradiction – unable to fulfil their inclusion mandate, digital banks struggle to scale.

Market conditions further complicate digital banks' position in Malaysia. Malaysia's financial landscape is highly saturated with large incumbent banks with advanced digital capabilities, meaning that digital banks are not operating in a "greenfield" environment, but entering a market with high customer expectations and relatively low dissatisfaction. Customer acquisition, therefore, becomes reliant not simply on being digital, but on offering materially better value, faster processes and deeper personalized experiences.⁶

The Path to Profitability for Malaysia's Digital Banks

Getting onto a sustainable path to profitability depends largely on the business model of each digital bank. Broadly, digital banks operate under two principal business models: credit-based and fee-based. Each comes with its own strategic imperatives and success criteria.

Credit-based digital banks. Credit-based digital banks monetize through interest income, with success hinging on their ability to deploy capital efficiently while managing risk. Key profitability drivers include: robust, AI-driven, real-time credit and risk models and diverse credit offerings.

In contrast to traditional banks that rely heavily on historical bureau data and manual credit scoring, digital banks must build real-time, AI-powered credit engines. By tapping into ecosystem-generated alternative data – transaction patterns, utility payments, ride-hailing history, etc. – digital banks can dynamically assess credit worthiness, even for thin-file or underbanked customers. Such models are more inclusive and enable instant lending decisions, a major differentiator in customer experience.

To build a profitable loan portfolio, digital banks must avoid over-reliance on a single product (e.g.,

Buy Now Pay Later (BNPL) or microlending). Instead, they should build a diversified suite of credit products: short-term microloans, personal overdrafts, SME working capital, and eventually, more complex offerings such as auto or home financing. This approach spreads risk, generates new revenue streams and caters to customers as their financial needs evolve.

Fee-based digital banks. Fee-based digital banks focus on transactional revenue, monetizing through payments, subscriptions, remittances, and partnerships. Unlike credit-based digital banks, these digital banks' profitability rides on: smart and granular customer segmentation and nudges to drive customer usage.

While fee-based digital banks employ AI much like credit-based ones, fee-based digital banks apply AI in a different manner. They primarily focus on identifying and prioritizing customer segments that transact frequently – such as gig economy workers, young professionals, expatriates, or microentrepreneurs. These users generate higher transaction volumes, enabling sustainable fee-based revenues even with lower margins.

Secondly, digital banks can take cues from consumer tech to gamify financial engagement – offering rewards, badges, spending insights, or even community-based savings challenges.⁷ These nudges deepen user engagement, build habit loops, and increase stickiness – critical in a market where customer churn is high and switching costs are low.

Universal success criteria. While the nuances of each model differ, there are also several universal success factors that digital banks in Malaysia must embrace to achieve long-term, sustainable profitability.

Regardless of business model, digital banks in Malaysia face common challenges and must execute flawlessly on two foundational pillars:

- leverage partner ecosystems
- delivering seamless UI/UX.

Where traditional banks can rely on the scale of their branch networks and sizeable brand equity, digital banks must build their customer bases from the ground up.

One key competitive advantage for digital banks is their ability to rapidly embed third party partners and ecosystems, enabled by their modern microservices-based technology architecture.

These third-party partners and ecosystems can range from BNPL, thin-file lending vendors, e-commerce platforms, telco, to ride-hailing and retail chains. They not only offer access to existing customer bases, but also: provide an avenue for rapid capability acquisition, generating rich streams of alternative data which are paramount for modern-age underwriting, personalization, and risk modeling.

The second key competitive advantage of digital banks is their innovation-centric culture and design focus.

Today's digitally native consumers expect faster, more intuitive and frictionless banking experience. Our “Bank of the Future” survey, where we surveyed a thousand Malaysians about their retail banking preferences, revealed that 9 out of 10 retail banking consumers want a better online and digital experience.⁸

Coupled with the fact that design and innovation are areas where digital banks can compete favorably against incumbent banks – because design is an area that wins on merit rather than capital – digital banks should treat frustration-free user journeys and seamless end-to-end experiences as must-haves rather than nice-to-haves.



From Wedge Product to Full-stack Financial Platform: The Winning Model

While digital banks operate under different business models (credit-based or fee-based or a hybrid mix), the road to profitability is remarkably consistent. Almost all profitable digital banks in APAC have followed a wedge-to-platform strategy: starting with a narrowly focused but high-value product, then expanding into a full financial ecosystem that captures a broader share of the customer's financial life.

This strategy can be broken down into five key stages:

1. Start with a wedge product to build trust and a healthy customer base
2. Go-live with deposit products
3. Promote aggressively to build the digital bank's deposit base
4. Expand product offerings to drive interest/non-interest income
5. Continuously engage customers to maintain customer retention and boost lifetime value.

Examples of digital banks that have successfully followed this path include South Korea's KakaoBank and China's WeBank.

KakaoBank, an offshoot of KakaoTalk, leveraged the messaging app's massive customer base when it first launched in 2016. WeBank, similarly, initially built off its sister company WeChat's massive customer base of 1.3 billion active users per month. Over time, both banks expanded their product offerings, promoted aggressively and continuously engaged customers to drive profitability.⁹

1. Start with a wedge product

In a market where customers already have relationships with incumbent banks, digital banks must identify a clear, underserved financial/non-

financial need and solve it better than anyone else. This initial wedge product must offer immediate value, be easy to use, and deliver a seamless experience that builds credibility.¹⁰

Examples of effective wedge products include: earned wage advance, no-fee international remittances, micro-savings tools, instant messaging (such as in the case of KakaoBank and WeBank).

The goal at this stage is not profitability, but customer acquisition and trust-building. By addressing a focused pain point exceptionally well, digital banks can quickly establish a loyal early user base.

2. Go-live with deposit products

Once the wedge product has created a gateway into users' financial lives, digital banks should prioritize deposit product launches. This includes current accounts, savings accounts, or e-wallets – often bundled with features such as instant transfers, spending insights, or round-up savings.

Launching deposit products early serves two critical purposes:

- builds a stable funding base, which is particularly important for credit-based digital banks that need low-cost capital to lend
- increases customer engagement, which is particularly important for fee-based digital banks, as accounts become the primary interface for day-to-day financial activity.

Digital banks must also ensure that deposits are protected, accessible, and digitally managed, with no hidden fees – reinforcing trust and transparency.

3. Promote aggressively to build the digital bank's deposit base

With deposit products in market, digital banks should enter a phase of aggressive acquisition and engagement, leveraging promotions, incentives, and partner channels to drive rapid deposit growth.

A sizeable and sticky deposit base is the foundation for monetization, allowing digital banks to reduce reliance on external funding, cross-sell services, and better understand customer behavior through transactional data.

4. Expand product offerings to drive interest/non-interest income

Once a critical mass of users and deposits is achieved, digital banks can begin to scale their business model – either towards fee-based services, credit offerings, or a hybrid approach, depending on their strategic positioning and technology capabilities.

- For fee-based banks, this could mean launching international remittances, wealth management tools, subscription-based financial coaching, or insurance marketplaces
- For credit-based banks, this is the stage to introduce AI-driven personal loans, revolving credit lines, BNPL products, or even SME lending – underwritten using behavioral and alternative data collected through prior engagement.

At this stage, the goal shifts towards monetizing the customer base through high-margin services, while maintaining superior customer experience. The product roadmap should be guided by robust data analytics, A/B testing and clear unit economics to avoid overextension.

5. Continuously engage customers to maintain customer retention and boost lifetime value

Acquiring customers is expensive; retaining and monetizing them is essential for profitability. Leading digital banks continuously engage users by embedding themselves in their customers' daily financial routines.

Our research on profitable APAC digital banks reveal several strategies that work well to engage customers: gamification (e.g. savings goals, financial milestones, reward tiers), hyper-personalization powered by real-time data (e.g. smart alerts, personalized offers), community-based features (e.g. shared goals, group savings, peer benchmarking) and lifecycle marketing to trigger relevant financial services as customers' needs evolve.¹¹

The ultimate goal is to increase customer lifetime value by expanding the depth of financial relationships. The more touchpoints a digital bank has across savings, credit, payments and other financial services, the more resilient and profitable its business becomes.

Navigating the Complex Path to Profitability

While the arrival of digital banks in Southeast Asia sparked early optimism, the path to profitability has proven far more complex than anticipated.

In Malaysia and across the region, digital banks are navigating a landscape marked by regulatory constraints, thin-file customers, and the ongoing challenge of building trust in markets historically dominated by incumbent players. Despite these hurdles, the opportunity remains significant – especially given the persistent financial inclusion gaps and the rapid acceleration of digital adoption.

Success will not come from customer acquisition alone. Digital banks must evolve beyond short-term incentives to build robust, data-driven ecosystems that prioritize sustainable value creation. Whether adopting a credit or fee-based model, the key lies in strategic focus: launching with a compelling wedge product, securing a stable deposit base, and layering in high-margin services that addresses evolving customer needs. Leveraging partner ecosystems and delivering seamless, intuitive user experiences are no longer optional – they are foundational.

Ultimately, incumbent banks still hold a competitive edge through scale, trust and regulatory familiarity. However, digital banks that can innovate around these structural advantages by embracing alternative data, behavioral underwriting, and relentless customer engagement – have a viable path to profitability. The race is not over. It has simply shifted from a sprint to a long-distance game of execution and endurance.

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