BankBeat

Features

What might banking look like in 2033?

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Ten years ago, success in community banking could be achieved by paying attention to these fundamentals: Know your customers and make meeting their needs central to your decision-making; match the term of loans to the life of the assets that support them; and hire and train good people. Bankers who understood these fundamentals a decade ago are probably still running a successful institution today.

But competition for customers has intensified. And how banks deliver their services has grown complicated in the last decade, exponentially so starting in March 2020. Anticipating and meeting the demands of the future will require nothing less than fortitude. Will sticking to key fundamentals be enough to grow and thrive?

We like to think the future is implied by the past, but it cannot be, not fully. We don't know what we don't know. Or, as 20th Century humorist, Will Rogers, once said: "It isn't what we don't know that gives us trouble. It's what we know that ain't so."

It's safe to assume important things will change in the decade ahead. And if change is all that's assured, how will you prepare yourselves and your banks to be successful?

The explosion of technology…

In 2013, a survey conducted by the American Bankers Association pegged mobile banking as the fourth most popular way to access banking services, behind online, in-branch, and visiting an ATM, respectively. Today, mobile banking reigns supreme. By 2033, how will banking be conducted? In the metaverse?

"A lot will happen in the next 10 years," said Brooke Ybarra, senior vice president of innovation and strategy for the American Bankers Association. Ybarra's office is looking at how the developing metaverse, along with AI, machine learning, and quantum computing will impact the business of banking.

What even is the metaverse, you might wonder? The definition is astonishingly unclear. According to an article in Wired magazine, "metaverse doesn't really refer to any one specific type of technology, but rather a broad (and often speculative) shift in how we interact with technology," writes Aaron Ravenscraft. Companies, such as Meta (née Facebook), are building virtual worlds and within those worlds, virtual products are being bought and sold. Despite the somewhat oxymoronic name, the market for real estate in the metaverse is projected to grow by more than $5 billion by 2026, according to data cited in The New York Times. This has implications for banking.

Brooke Ybarra

Meanwhile, quantum computing, in an article published by McKinsey, will allow bankers to "more effectively analyze large or unstructured data sets" … helping them make better decisions and improve customer service by basing product offerings on browsing history. McKinsey has called customer data "the new oil – highly-regulated, jealously guarded … a key source of business value." As a solution for the "problem" of maximizing all that data, quantum computing promises to be game changing. "Know it will affect your business," Ybarra said.

"Every community banker knows, based on their existing data, where their customers are," said Dr. Sean Payant, chief strategy officer and senior executive vice president of Lincoln, Neb.-based Haberfeld. Payant said community banks should be using that data to target the neighbors of current customers, both individuals and businesses, with ongoing marketing campaigns. "You have to execute a growth strategy to grow your base of core customers," he said. Doing this will result in loan growth, low cost of funding, and increased non-interest income (because having more customers increases use of income-generating products and services). Importantly, it means less volatility.

Haberfeld clients deploy core customer growth campaigns using demonstrated convenience (targeting non-customers who live near or have businesses close to branches) as well as predicted convenience (using GPS signatures for people driving by or spending time near branches); this is accomplished by capturing GPS signatures within roughly a quarter mile of branches. By casting so narrowly and by using targeted messaging, Payant said community banks can often double the number of core customers they are acquiring, which is key to growing a community bank in spite of any external forces that impact the industry as a whole.

…And how it shapes banking

As "digital first" has gained traction in banking, so has fraud. Every $1 lost to fraud costs the industry $4.36 in related expenses such as recovery and legal fees, according to LexisNexis Risk Solutions. Fraudsters target mobile banking channels, worm their way all along the customer journey, and are increasingly successful at deploying identity-related scams. The future of fraud prevention is emerging through Trusted Digital Identities.

While the digital identity ecosystem is in flux, writes Oliver Wyman in an ABA-sponsored white paper, advancements in real-time payments are also leading system operators to see how they can enhance their defenses by upgrading authentication methods. Trusted digital identities aim to reduce and eliminate fraud in three areas where banks are most vulnerable: Onboarding, authentication and transaction monitoring. Things to watch for in the years ahead include evolving industry standards, the potential for a nationally federated identity system, how vendors respond, and what role the government ultimately plays.

Beyond fraud, innovation needn't mean the wholesale reinvention of banking's business model. Incremental changes can "play in the long-term success of any enterprise," said Dennis Gada, head of financial services for North America at Infosys during a BAI Banking Strategies podcast. "Focusing on the incremental certainly takes the pressure off."

During an American Banker podcast, Michael Abbott, global banking lead at Accenture, said future-ready bank operations can significantly reduce operational costs. Game-changing technologies have been democratized, Abbott said, allowing community banks to compete in areas where they could not have 10 or even five years ago. The latest frontier for generative AI is tackling banking operations. The goal is to significantly reduce the cost of problem-solving for customers by predicting many of the problems they might face when dealing with your bank, he said, and eliminating these troubles before they ever occur. "I see opportunities to get the cost out of operations."

What does it mean to adapt long-held practices using digital tools to better serve customers? "We don't think of [digital] as innovations but as strategies," Ybarra said. "They are table stakes for bankers who want to be in business in 10 years." The real challenge, as she sees it, is modernizing the core banking platforms, and reducing a bank's reliance on third parties, which currently control the bank's technology stack. "Banks need more control."

Working with legacy systems is an ongoing challenge for community bankers. Core vendors haven't always been the enthusiastic partners that community bankers need as they look to innovate or move toward open banking/open API. "As the core providers have grown, it feels like there is less 'roll up the sleeves' time between banks and vendors dealing with thorny issues of execution," said Steve Williams, president of Cornerstone Advisors.

Bankers interested in succeeding in the future will need to reduce their reliance on legacy solutions, integrate middleware platforms where they can, or find next-gen core platforms that are more nimble — especially important as rulemaking on Section 1033 of the Dodd-Frank Act is finalized, which stipulates consumers can be given access to the data they've generated as a result of working with your institutions.

"Sticking with an outdated but familiar legacy core system exceeds the cost of investing in a more modern core banking platform," wrote Murthy Veeraghanta, chair and CEO of VSoft ("On Topic," page 8, March 2023 BankBeat). "As fintechs, banking and payments evolve, bankers must consider whether their core systems pose a threat to their long-term growth."

Yet a Cornerstone survey showed seven in 10 banks don't plan to replace their core system as part of a digital transformation — even as 70 percent called their current tech infrastructure a barrier.

For these banks, future success will come by doubling down on the community banking value proposition: Relationships.

The continued relevance of the ground game

Talk of innovation in banking pushes the threats posed by fintechs to the foreground. Forget fintechs, Payant advised. "Community banks were not created to be fintechs; they were created to serve communities. Community bankers need to implement an on-going strategy built on checking products in order to gain first right of refusal on other products and services," he said. Retail and business checking is the fertile soil in which growth occurs. But — if only to extend the metaphor — that ground is often too weedy to support growth.

The problem for many community banks, as Payant sees it, is that many have checking products that are too complicated, with fine print (policies and processes) that are barriers to growth. Further, he said the people in many community banks aren't trained in a way to maximize the onboarding of new checking customers.

"Too many bank … executives cling to the belief that what differentiates their institution is its 'customer experience' or 'their people,'" writes Cornerstone's Ron Shevlin in Forbes.

"You have to train people to serve really well," Payant said. Unfortunately, community banks offer "average" on a daily basis, he said. "Bankers say, 'It's our people who differentiate us.'" Payant said. "That's only a reality if they are equipped with the skills to be an actual differentiator."

Payant challenged industry executives to shop their competition and have their own branches mystery shopped. Chances are very good that if you do, "you'll be handed a stack of brochures with a smile and sent on your way."

Mediocrity can be resolved, not just by switching customer onboarding to a bot, but by training people to ask questions, listen and then invite prospects to open their accounts on the spot. "What's the community banking difference? People serving people," Payant said.

And while digital account opening at community banks is growing, up roughly 5 percent since the pandemic to 10 percent of all new accounts, those accounts are more transactional and they have lower balances. Attrition is higher as well.

To be successful this year, and next year, and 10 years from now, "you have to feed the front door," Payant said. The best food for future success is core customers between the ages of 24 and 44, because that's when all the big things in life happen."