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It Will Take More Than Better Digital Banking to Survive the New Normal

Finalytics.ai/Harris Poll Survey: 40% of banking consumers are willing to leave their primary financial institution for digital banking that compares to a great online shopping experience.

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In the seven years prior to the pandemic, there was a steady chorus of voices sounding an alarm about the future of community financial institutions. One of the main causes for such concern is whether these institutions have the ability to effectively respond to the digital revolution.

In 2018, the Wall Street Journal published an article documenting the flow of $2.4 trillion in deposits from community and regional financial institutions to the three largest mega banks over the ten years since the Global Recession of 2008. An analysis of 2020 data by Cornerstone Advisors and Strategycorps documented a 7% increase in the number of consumers identifying digital only banks as their primary financial institution. The same study showed decreases in the number of people identifying mega banks (-6.5%) and credit unions (-1.2%) as their primary financial institution. A Bloomberg article in 2020 highlighted the extraordinary growth of deposits at the 25 largest U.S. banks where, from the end of 2019 to mid-March, new accounts at these largest banks increased by $500 billion in assets. Commentators have described this growth as a “flight to quality.”

These statistics set the table for the findings in this report based on results from a 2021 survey of over 2,000 US adults, including over 1,900 banking consumers, conducted online by The Harris Poll on behalf of Finalytics.ai. This survey describes a crucial tipping point for community banks and credit unions – a tipping point that requires responses far different than those typical of these organizations. To remain relevant and leverage the opportunities that these challenges bring, these institutions will need to do far more than upgrade or replace their digital banking offerings. Instead, locally based banks and credit unions will need to focus their next moves on adopting newly available technology designed to meet the rising level of expectations among customers and members.

Introduction: Dawning of a New Day

However unknown the exact date is for a return to a life without pandemic, the virus's impact on the lives of people across the globe was inevitable. Many of those impacts permanently altered consumer behavior as the threat of contagion required lockdowns; this changed how consumers met their daily needs. It seems likely that the closure of branch channels helped generate an increase in new digital banking users and more use of the same services by those already digitally savvy.

The Finalytics.ai/Harris Poll Survey describes the possible impact of these shifts in people's lives in terms of loyalty, or the lack thereof. Forty percent (40%) of banking consumers said they would be likely to leave their primary financial institution for digital banking that compared to a great online shopping experience. For community banks and credit unions the reality of this mindset among consumers has already manifested. Forty-four percent (44%) of banking consumers agreed with the statement *"I prefer local banks and credit unions, but their digital banking does not meet my needs."* Fifty-three percent of banking consumers (53%) agreed with the statement *"I bank at regional and national banks because they have better digital banking."*

44% of banking consumers prefer community banks and credit unions – but feel their digital banking does not meet their needs.

40% of banking consumers would be likely to leave their primary financial institution for digital banking that was comparable to a great online shopping experience.

Taken together, these statistics indicate a new challenge for community banks and credit unions that cannot be addressed by conducting "business as usual." How community financial institutions respond to this challenge will determine the future of these organizations as well as, in some cases, the future of the communities they serve. Responding to this challenge will require community financial institutions to take a different perspective on how technology can and should serve their customers and members.

More Digitally Savvy Consumers With Higher Expectations

Well before the onset of the pandemic, consumers evaluated the digital experience offered by their primary financial institution using the experiences they had with the e-tailers they frequented. Unfortunately, too many banks and credit unions did not realize that these e-tailers were the benchmarks by which the digital experiences they offered were being evaluated. To compound the impact of this limited view, too many community financial institutions insisted on having their digital experience measured against their peers and competitors. This limited view created a false sense of security regarding the critical need for elevating their digital game, i.e., *"Our digital experience needs work, but our peers are in the same boat."* This mindset also led to a decrease in the sense of urgency institutions had about improving their digital experience, i.e., *"The other institutions can't move any faster than we can, so we can proceed business as usual."*

These statistics indicate a new challenge for community banks and credit unions that cannot be addressed by conducting "business as usual"

Increased dependency on digital channels became the norm for many consumers during the pandemic. The comparison of these online experiences to those offered by their bank or credit union may have lowered the consumer's tolerance for suboptimal digital engagements. This new level of intolerance could manifest when they are exposed to a better option than what they currently experience at their financial institution. Addressing the gaps between the digital experiences of e-tailers and financial institutions has become more urgent. The results of the Finalytics.ai/Harris Poll survey indicates identifies three of the most important attributes found in an acceptable digital experience. Roughly half of Americans (51%) identified **convenience** – defined as being able to do anything digitally that they can do in the branch, while over a third cited **easy access** and all the latest digital bells and whistles (35%). In addition, more than a quarter of Americans (27%) said they want a digital banking experience that is **unique** with content and offers designed for their specific needs.

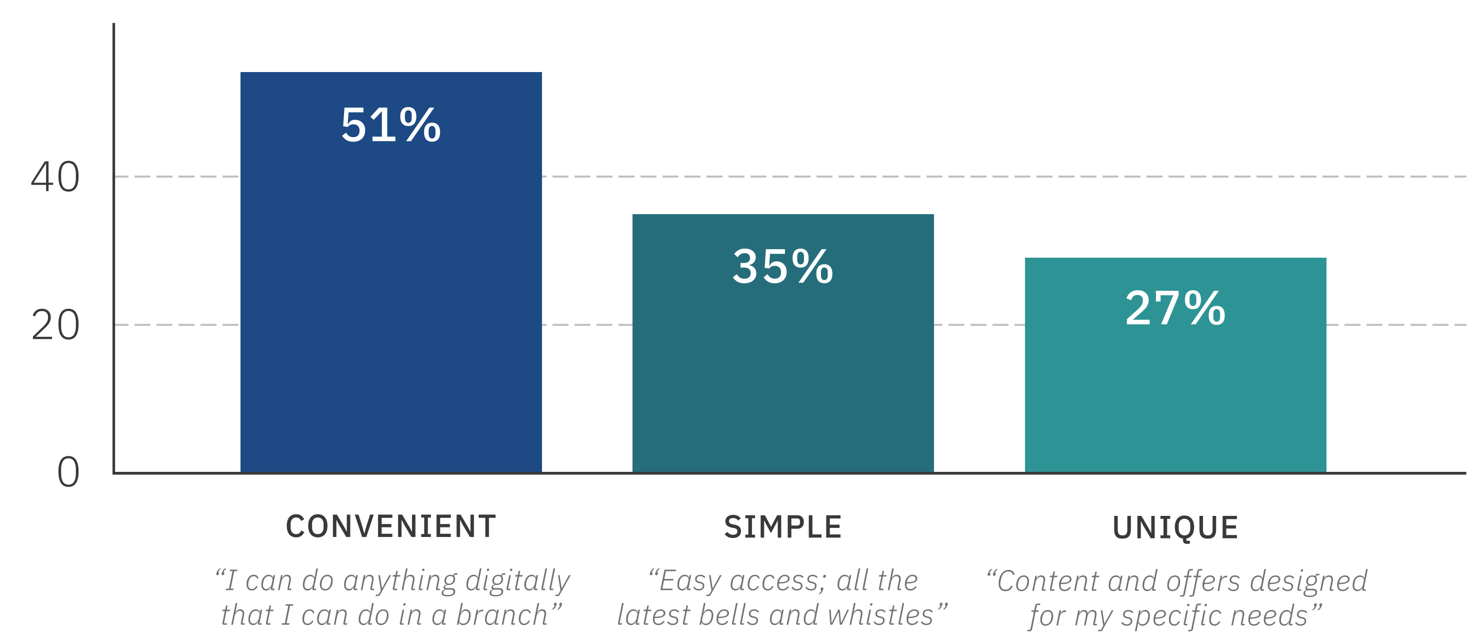
Current Levels of Personalization Are Not Enough

Vendors in the banking industry have aggressively marketed "personalization" as a way to provide relevant content during digital engagement. But personalization in digital banking has manifested in ways that do not meet the expectations of customers and members. Instead, too many institutions have relied on new loan rate banners for Millennials or refi offers for homeowners to meet the unique needs of their clients.

Many leaders of institutions who use personalization in this form find that measuring its impact is difficult. Since the success of such campaigns often depends on the law of large numbers and brute force marketing, the overall financial health of the customer or member acquired is suspect While results from the Finalytics.ai/Harris Poll survey indicate that 53% of respondents feel that *"...regional/national banks have better digital banking"* and 50% of Americans agreed that *"...digital-only banks have better digital banking,"* the demographics behind these numbers makes them even more meaningful. Of those who agreed with one or both statements, those from households with higher annual incomes are more likely to agree than those with lower HHIs.

What Americans identified as attributes of an acceptable digital experience *

* Majority of respondents have an HHI of $100,000+



Among banking consumers, those with an HHI of $100k + are more likely than those with an HHI of less than $100k to bank with regional and national banks because they have better digital banking (62% vs. 48%). Also, those with an HHI of $100k + are more likely than those with an HHI of $50k-$99.9k to believe online/digital only banks have better digital banking (53% vs. 44%). Targeting these households in a way that will attract and retain them will require more from an institution than personalization build on brute force marketing.

There are solutions available to community banks and credit unions that help retain high quality customers and members. To apply these solutions effectively will mean that community institutions must embrace new technologies. In too many cases, decision-makers at these institutions believe that such technology is too expensive and complex for them to use. These perceptions are 180º from the truth.

Business as Usual in Banking Technology

Let's start by describing the general relationship local banks and credit unions have with new technology. Typically, these institutions do not have the expertise nor budget to build the technology they need to serve their customers and members. They depend on third parties for digital banking, core processing, loan underwriting and many of the other systems that support their products and services. When a bank or credit union needs new features and functions to meet the needs of their customers and members, they usually consider if these legacy third party systems need upgrading or replacing.

There are several reasons this approach does not work. The institutions themselves evaluate and purchase technology in cycles that are sometimes four or five years long. The high risk of replacing one of these key systems and the additional time required for implementation make replacement undesirable and purchase cycles increasingly longer. The third parties that institutions depend on are large, multibillion-dollar organizations that often have hundreds of clients, making them slow to bring innovations to market. When they do deliver the desired innovations, implementing them can be very disruptive to the financial institution. Adoption of innovations may even require that the institution hire new expertise so that the value of the feature or function can be fully realized.

In the new normal, community financial institutions will need to go beyond personalization to meet the expectations of the digital consumer.

Regarding these critical systems, it's possible that the largest replacement cycle ever witnessed in the finance industry has been in digital banking. Consumer adoption of technology, especially mobile tech, has forced financial institutions to rethink their digital offerings. This replacement cycle was ignited with the introduction of the smartphone and has been sustained by the introduction of other devices that allow the consumer to do almost anything – anytime, anywhere.

The adoption of new technology has generally been towards digital banking platforms rather than point solutions. However, even if this important step in modernization is made quicker and simpler, it will not prevent community banks and credit unions from becoming irrelevant in the digital age. These institutions need to maintain their relevance to the people they serve in a way that is not complicated, expensive or disruptive.

How Community Institutions Will Level The Playing Field

Chris Skinner is a bestselling author (*Digital Bank, ValueWeb* and *Digital Human*) and financial consultant who does an excellent job of describing the aforementioned misperceptions in community financial institution. Skinner remarks, "What they [the community banking segment] do not understand is that it [new technology] is cheaper and simpler. That is why I cannot handle it when a CEO says, *'that's not for us'.* Thinking that way is like saying, *'I am just going to play dead until I am dead'*".

Community financial institutions that are not interested in "playing dead until they are dead" must find a way to harness the power of data. The required data must stretch beyond the internal data that institutions already possess to incorporate numerous, multi-faceted sources. In other words, along with the "small" data they possess, these banks and credit unions must incorporate big data sets from external sources. Given that many organizations already find using internal data is difficult, the idea of integrating big data into their outward facing systems may be overwhelming.

Luckily, while bankers are doing what they do best, companies with decades of experience in financial services have also been doing what they do best. Their experience with data science and the application of advanced technology has resulted in offerings that combine internal and external data to create dynamic segmentation and content.

Combining these elements means that the content presented to each digital visitor is unique to them and their needs. This is determined by AI's analysis of numerous data points including demographic, psychographic and financial information. Further, a segment of one experience may be different each time an individual visits. Imagine the impact such capability would have on a prospective customer or member. By applying this technology from the very onset of the relationship, the institution is anticipating the needs of the prospect.

The same impact could be seen with current customers and members. Most of the respondents to the Finalytics.ai/Harris Poll survey indicate that in addition to the services banking consumers use at their primary financial institution, some of them rely on other services from secondary banks or credit unions. Thirty-six percent identified national banks as their secondary institutions. Dynamic segmentation can mitigate the risk of such clients moving to secondary institutions and deepen the relationship they have with their primary bank or credit union.

VIEW OF DIGITAL QUALITY BY TYPE/SIZE OF FINANCIAL INSTITUTION

53% of consumers bank with regional or national banks because they have a better digital banking experience.

47% of consumers who use regional or national banks do so because they have better digital banking.

44% of banking consumers prefer community banks and credit unions, but the digital banking does not meet their needs.

50% of consumers believe digital-only banks have better digital banking.

Emerging companies are solely focused on how to apply new technology to existing IT landscapes within community banks and credit unions in a fashion that does not disrupt or complicate. Cloud computing has made it possible for this type of solution to be implemented within a matter of weeks and integrated without requiring an institution to train current resources or hire new expertise. With the understanding that legacy technology is complex and expensive, the quickly implemented and integrated emerging technology on the market today can change the competitive nature of an institution.

The Greatest Risk is Doing Nothing at All

It is no easy task to break free from business as usual and lead an organization in adopting a new technology. Some leaders at community banks and credit unions will not believe in the need for such; some will simply not want to pursue it due to certain career goals. However, some leaders will see the application of such technology as a game changer for their institution. These leaders will understand that successfully delivering a digital experience that meets the expectations of prospects and clients is the most valuable step in elevating their institution. In order to do this, they must learn from e-tailers rather than peers or competitors.

Digital transformation is not the first step these leaders will take. Their first step will be to consider what aspects of their organization's culture must be transformed. This technology can create a segment of one experience that evolves in real time to address the needs of the client in any given moment. Organizational leaders will extend access to this technology to every corner of their bank or credit union in order to improve the institution's reaction time and effectively fill the gaps in their digital offerings.

When contemplating fulfilling such a vision, the first step is often difficult to define. Developing a stronger focus and a clear understanding of the landscape are the keys to taking such a step.

Areas to Consider When Defining Your First Step:

FOCUS ON RETENTION

Thanks to stimulus programs and agility in getting those funds distributed, many community financial institutions have survived the pandemic and found themselves with more customers and members as well as fuller deposit accounts. New customers and their deposits are not going to hang around just because they are offered no-fee checking and a savings account. Having the necessary technology to create a data driven approach for daily interactions with new and existing clients is an urgent need. Do not shy away from this because you and your team do not know how to achieve this goal. There are companies entering the market who have been applying data for just this purpose for years. These companies can share the knowledge required to retain your customers and members by delivering a digital experience that speaks specifically to their needs.

LOOK PAST LEGACY PROVIDERS

As with AI, many of the legacy technology providers will claim that they can provide the data you need to delight your customers and members. Perhaps they can. However, history suggests it will be a while until you see even an approximation of what they promised. A growing number of local banks and credit unions are giving startups and early-stage companies more consideration. There are companies in these categories doing some interesting things with data and machine learning. Financial institutions are finding ways to work with these companies, mitigating the risk that is inherent when engaging with companies that lack a track record. Local financial institutions need to follow the lead of early movers who are embracing this type of partner. In the digital age, the greatest risk is to do nothing at all. Those institutions who don't find a way to partner with these companies are facing a risk much higher than those who access and incorporate the innovations FinTechs, startups and early-stage companies offer.

NO NEED TO BOIL THE OCEAN

Though new technologies are easier to deploy and cheaper to use, time still plays a role in achieving the level of experience required to satisfy consumer expectations. The Finalytics.ai/Harris Poll survey indicates that 44 percent of Americans prefer local banks and credit unions but the digital banking at these institutions does not meet their needs. While in many cases, actions taken by many community financial institutions during the pandemic have added to their cache of good will with their customer, members, and community there is still a need to deliver more of the attributes consumers have identified as part of an acceptable digital experience. Any step taken by your institution toward achieving that goal should help retain clients and even attract a few others. Each step should be a material improvement. Each step should provide an ROI that justifies it. If you cannot do both, you may need another technology partner.

The pandemic has created a now normal that is materially different than our reality before COVID-19. The Finalytics.ai/Harris Poll survey identified many risks that should be concerning. Yet, the report also points to opportunities for local banks and credit unions. Action is required and "business as usual" must be left behind. The pace of change will likely increase. Community financial institutions must embrace the new and powerful technical tools being brought to market by suppliers. These tools convert data into actionable information that has measurable impact on the behavior of prospective or current customers and members. Level the playing field before the game is over.

Survey Method: This survey was conducted online within the United States by The Harris Poll on behalf of Finalytics.ai between April 21-23, 2021, among 2,047 adults ages 18+, among whom 1,934 are banking consumers. This online survey is not based on a probability sample and therefore no estimate of theoretical sampling error can be calculated. For complete survey methodology, including weighting variables and subgroup sample sizes, please contact The Harris Poll.

The Finalytics.ai Story

We are committed to helping communities. Most of us have spent our lives in financial services and believe the best way to help any community is to strengthen its community banks and credit unions. Due to changes in banking, focus on these organizations is vital.

In 2020, credit union membership shrank by 1.2%. In 2020, the community bank space contracted by 3.7%. Deposits in the largest banks continue to grow. In the decade following the financial collapse in 2008, $2.4 trillion in deposits were recorded by the three largest banks in America. Digital-only banks grew their user base by 50 percent in 2020.

We believe these trends can be reversed. Until now, the changes in digital banking have been evolutionary, not revolutionary. The largest and digital-only banks have been the source for most of this evolutionary. Some of these changes have trickled down to community financial institutions but many of these organizations are limited in their range of innovation due to their dependency on traditional legacy technology providers.

There is an opportunity for a revolutionary shift that can break through the commoditization of digital banking in the community space. This revolutionary shift can reverse the flow of customers and members from community banks and credit unions to the largest and digital-only banks. By reversing this flow, the current trends limiting the advantages of competition and choice in the community banking space can be eliminated. The COVID-19 pandemic has amplified the need to achieve each of these goals.

Finalytics.ai has built the technology platform that revolutionizes digital banking for community banks and credit unions. The Finalytics.ai platform uses the same modern technology used by the most innovative organizations in the FinTech space. The API-driven architecture at the center of the Finalytics.ai technology is extensible, configurable and scalable. We believe in communities and this platform is how we will support the banks and credit unions that serve these communities. *The revolution is not coming; it is here.*