

**CELENT**

# **DIGITAL MATURITY IN BANKING**

Conversations Across Bank Tiers

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This is an authorized reprint of a Celent report. The summary was prepared and arranged for Hitachi Vantara Corporation, but the conclusions and opinions have remained the same.

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# EXECUTIVE SUMMARY

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Leading-class digital banking is achieved by those who focus their entire organization on delivering value to customers through digital and digitally-enabled experiences. Digital maturity by this definition is not simply about the front-end experience; it includes a bank's philosophies, ethos, business models, people, culture, and processes in addition to technologies.



Earlier this year, Celent conducted a series of interviews exploring digital maturity with tier 1 banks in a report titled [Digital Maturity in Banking: Conversations with Tier 1 Banks](#). These institutions were tier 1 in asset size (>\$250 billion); however, they were not the top four “mega banks.” What became clear through our research was a growing perceived divide by bank execs between the largest banks in the US and even the regional/super-regionals. The need to achieve significant scale, the speed of change, and resource availability for transformation were top of mind with these institutions. Some even used the term “haves” (megabanks) and “have nots” (regional/super-regionals) to describe a competitive dynamic where larger banks are looked at through the same competitive lens as megabanks yet are operating at a significant disadvantage. This invites the question: What about smaller banks?

In this context, Celent expands its previous report with interviews among executives at small and midsize institutions—those that are smaller than the regional or super-regionals. The interviews focused on smaller bank digital journeys, challenges, and road maps. We followed the same framework, which includes five technology characteristics understood to be prerequisites to digital transformation and embedded within a larger digital maturity framework: **technology modernization**, **data and analytics**, **technology innovation**, **agile organization**, and **ecosystem configuration**.

Celent captured each institution's perceived importance of the areas as well as their perceived capabilities within them. There is a significant correlation between the importance of an attribute and an institution's perceived capability, suggesting banks are investing in areas they view as critically important. Data and analytics as well as ecosystem configuration both showed the widest gap between perceived importance and capability.

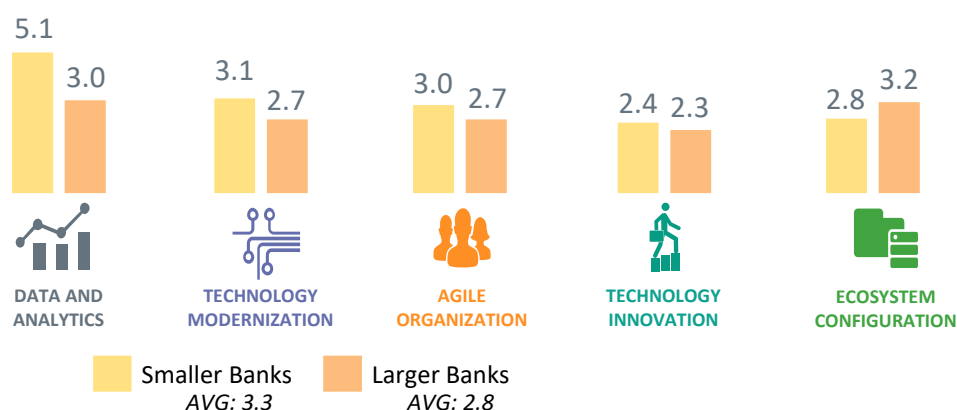
Below we highlight a few meaningful themes which emerged from the interviews with smaller institutions. These summarize the top five issues; a longer list is available in the corresponding section.

- **Change is hard:** Leadership in many small institutions is still stuck in the status quo, the old way of doing things.

- **Small banks are looking at new business models:** Many institutions expressed a desire to support Banking-as-a-Service (BaaS), although it is road mapped with tech modernization.
- **Core banking transformation is becoming more common:** Banks are beginning to run up against the limitations of their core platform for strategic technology initiatives and are exploring options, even cloud-native options.
- **Many banks are testing and learning with digital-only brands:** Banks have launched or plan to launch digital-only brands to use as sandboxes for innovation or potential migration paths.
- **Institutions are looking for partners, not vendors:** Smaller banks know they cannot do it all themselves and are looking for partners to help them leapfrog technical limitations.

In Figure 1, we took findings from the previous report and compared the importance/capability gaps with those of smaller institutions interviewed subsequently. While the immediate needs of digital banking are well known and often shared across tiers, the paths and barriers to get there can be different. While smaller banks showed leadership in areas like emerging business models (intent to offer BaaS capabilities), core migration to next-gen platforms, and customer centricity, the smaller banks showed larger gaps in capability across every digital maturity technology characteristic except ecosystem configuration.

**Figure 1: Average Difference Between Importance and Capability by Bank Size**



Source: Celent, n=10

Celent offers a few conclusions and go-forward recommendations based on these themes:

- **Constantly ask what the value is for the customer before investing.**
- **Keep the big picture in mind.**
- **Don't rush real transformation.**
- **Advocate for C-Level support.**
- **Have a problem to solve and a use case in mind.**

Note that in this report we use the term “smaller banks” to encompass institutions which could be considered both “small” (<\$10 billion in assets) and “midsize” (\$10 to \$100 billion in assets). We intentionally avoid the use of “tiers” as there is no agreed-upon standard.

# THE IMPORTANCE OF DIGITAL AT SMALLER BANKS



Innovation needs purpose. Tech for tech’s sake is a poor investment decision.

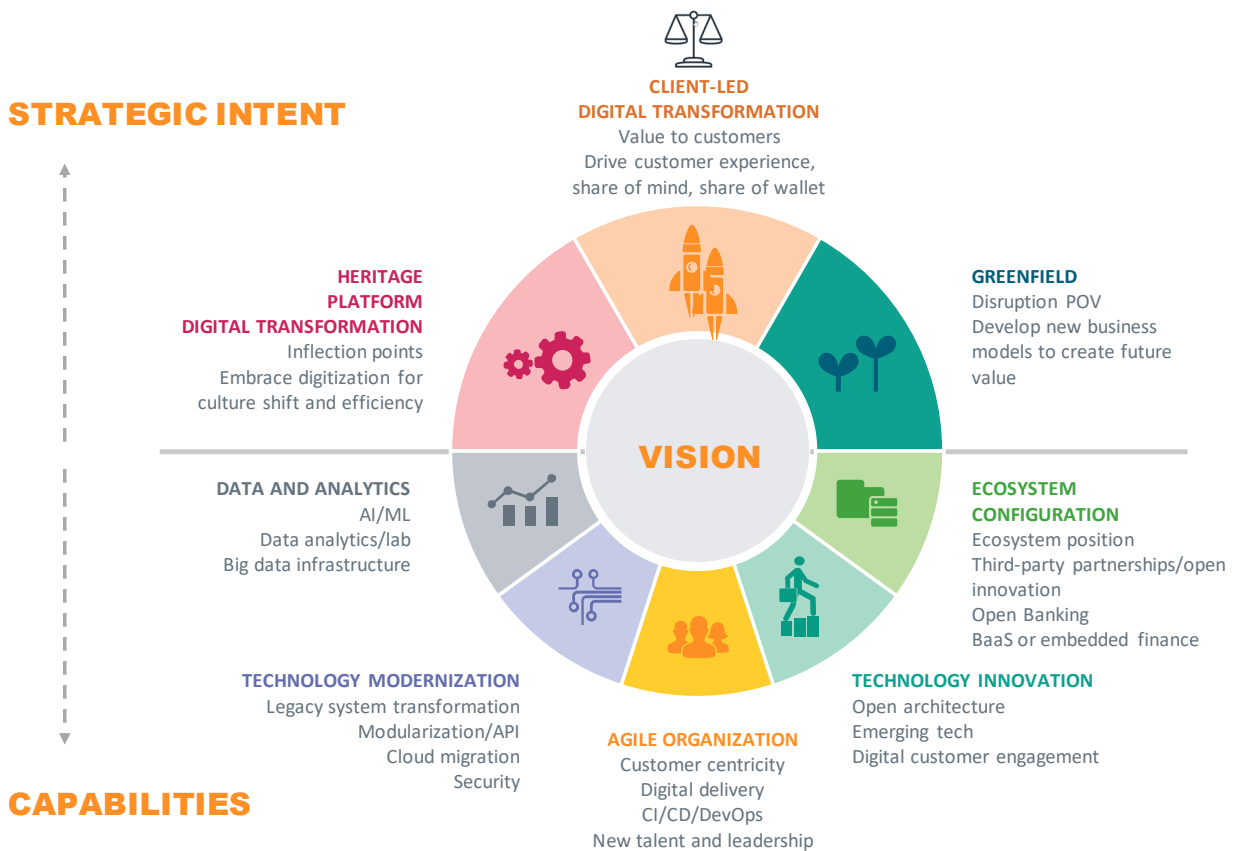
—Chief Digital Officer, Midsize US Bank



Digital transformation is a broad topic. Given the ubiquity and prevalence of digital financial services, everything seems to be digital in some way. Smaller banks driven by a traditionally strong focus on customer centricity are considering how digital transformation can enhance their ability to serve them.

As shown in Figure 1, Celent adapted a digital maturity assessment based on criteria established by Oliver Wyman. The wheel aims to illustrate the interdependence between common strategic intents and requisite capabilities.

Figure 2: Oliver Wyman’s Digital Wheel



Source: Celent, Oliver Wyman

In this view, there are three primary intents that singularly or in combination drive banks’ digital initiatives. Underpinning each of these three intents are five core capabilities. The top half of the wheel reflects intent and illustrates the tradeoffs required to balance short-term value—for an incumbent, investing in legacy or “heritage” systems—versus strategic change, represented as greenfield opportunity. The bottom half of the wheel indicates the key capabilities required to implement digital banking.

We now look at the characteristics of each portion of the digital maturity wheel. Each institution will look different, and “what good looks like” for some may be just table stakes for others.



## Data and Analytics

Financial institutions are undergoing data modernization efforts in hopes of dealing with issues around data silos, data formats/standards, governance, and analysis. Leading banks are working on data infrastructure to support broader uses around AI and machine learning (ML), hyper-personalization, next-best action/offer, predictive insights, and more advanced business intelligence. Banks are establishing strong governance which can then inform changes to the operating model, where data teams work directly with the business to create and deliver tangible outcomes. Most banks are looking at more modern, flexible technology to be an enabler for better utilization of enterprise data. Many cloud-based solutions are emerging for better, real time exploitation of transactional data that institutions are evaluating; however, it is still early days.

Many institutions say data and analytics tend to be an area that needs more work, due in large part to the silos that have grown up around either the growth in applications or M&A integration. Proper data management and governance are critical foundations for more advanced technology innovation use cases, specifically AI/ML. Many banks understand this challenge and continue to move to a positive direction; however, the availability of talent is sparse, and the pace of change is often tied to other modernization efforts.

### What good looks like

#### 360-degree view

Customer-centric value delivered through deep understanding of the customer’s point of view and journey

#### Easy access to data

API-based integration to granular data sets; insights-based reach; segmented and enhanced curation, prioritization, and engagement

#### Cloud for advanced use cases

Data science using cloud-based platforms and cloud services for AI/ML, data storage, and insights generation



## Technology Modernization

Moving away from legacy technology can be a monumental challenge, and despite institutions’ desire to migrate from existing systems, there are inherent risks to consider. Many are following a piecemeal approach to de-risk efforts. Banks are looking at modularizing and API-enabling new or existing technology assets that provide a more seamless path to integration or progressive renovation. Similarly, cloud is on the minds of bankers across the industry, although adoption varies. Less mission-critical applications (e.g., email, CRM,

marketing automation) have gone to the cloud, yet many of the transactional platforms remain on premises. Other systems, such as customer communications management (CCM), involve the movement of large data sets daily, making the proposition slower or more expensive.

Institutions are looking to join the ranks of cloud-native challengers, but necessary precautions need to be taken before these deployments can be successfully managed. Technology modernization initiatives are also fundamental to digital maturity, yet many institutions continue to move forward with strategies that involve wrapping legacy back-end technology to work around its limitations. However, some institutions are aware of the growing need to modernize the core and move applications to the cloud. Celent expects to see efforts increasing over time.

#### What good looks like

##### Legacy migration efforts

Strategic plans or in-motion programs to move away from existing technology from a risk-adjusted point of view

##### Cloud migration

Broad strategic intentions to migrate applications to the cloud (public, private, or hybrid), while establishing which platforms will remain (and be ring-fenced), be removed, or be migrated

##### Unbundling

Improving flexibility through microservices and API-based interoperability



## Agile Organization

Agility is best understood as a core capability underpinning multiple strategic imperatives under a digital transformation umbrella. Business agility requires focus and constancy of purpose; it is not the natural state of most organizations and work processes. It must therefore be continually and intentionally pursued. Agile also requires defined parameters and governance to ensure adherence to quality standards. While most banks are currently running teams leveraging agile development methodologies, many sit within larger groups that are decidedly not agile. Legacy technology can limit the footprint where agile is effective, where more modern cloud-native deployments can make enhancements, changes, and release cycles much more resilient, faster, and more efficient. Institutions that exhibit agile characteristics combine a fintech-like culture and more modern skill sets to succeed.

Many institutions understand the importance of being an agile organization or an agile development shop; however, they understand that agility is not a silver bullet for the bank's problems. In the words of one interviewee, "An agile hammer makes every problem look like an agile nail." Agile has been around long enough to be understood thoroughly by IT leaders in banks, and healthy skepticism in many instances leads to more pragmatic application.

**What good looks like**

**Create value**

Moving fast and building useful tools, not fast releases of bad products

**Cultural/skill support**

Broad C-level advocacy for digital/innovation and the skills internally to deliver, proper incentives in place to deliver

**Flywheel-life feedback**

Build momentum by continuously improving insights based on ever-improving data and algorithms



## Technology Innovation

Those seeking to innovate are placing their chips wisely, as cost and resource considerations often mean that not every idea or technology is given funding. Technology limitations from either poorly managed data or outdated applications can also give these projects pause or cause banks to fall behind fintech competitors. Leading institutions understand the importance of innovation, but a pragmatic approach requires a thoughtful evaluation of features and product enhancements more likely to make a difference with customers. Other areas of emphasis include emerging technology such as AI in the user interface, virtual assistants, and omnichannel customer engagement. Institutions continue to move toward more open architectures that allow for technologies to be seamlessly integrated across the technology landscape or with third parties.

Many institutions, especially the smaller community-focused banks, know the importance of technology innovation to its operating model. IT leaders are aware of the trends influencing adoption of digital and the importance of emerging tech in that realm. However, many are unwilling to make investments unless an obvious use case or problem area is being solved. Smaller institutions don't have the resources to invest in technology projects that become valuable in two or three years—they need to have impact today. This has been a guiding mantra for institutions with a traditionally customer-centric value proposition.

**What good looks like**

**Investing in innovation**

Fostering and investing in new initiatives, such as change the bank and agility in delivery

**Emerging technology**

Understanding the use cases and definitions of emerging technology, digital architectures underpinned by APIs, and secure protocols

**Products/features**

Implementing customer engagement features or products that are data-driven and engaging



## Ecosystem Configuration

Ecosystem configuration refers to how well-defined a bank's view of its strategic position is within the changing landscape of banking. Third party partnerships and open innovation are critical areas where an organization begins to engage with fintech. While some banks have been more eager, others remain cautious about the degree to which they engage with third parties. Those in the vanguard understand that some products and functionalities are better bought externally than built internally. As the business of banking begins to appear less vertically integrated, organizations will look to new business models emerging in fintech. Open banking has not yet been mandated by regulators in many regions, but leading banks understand it as an inevitability and are acting to put the people,



process, and technology in place to eventually support it—even if their optimism over open banking’s potential is cautious. Success in the future will likely be determined by how well an organization plays within an ecosystem, and the configuration will matter.

Institutions continue to look to ecosystem partners to innovate. For smaller institutions, this is critical to competing. Even the smallest of organizations are looking to implement more open technical architectures, which will allow them to integrate third parties at lower cost and with less friction. With openness and flexibility baked in, more institutions can take a best-of-breed approach free from the traditional limitations of legacy providers.

### What good looks like

#### Business model strategies

Knowing where the organization plays in areas such as open banking and BaaS; leadership articulation of position

#### Embracing fintech

Experience procuring and partnering with fintech collaborators; defined approach to identifying partners that align with the business

#### Standards-based environments

Modern integration standards to easily plug into a broader ecosystem and ensure interoperability

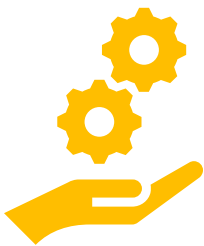
In the next section, we look at five smaller financial institutions with a focus on their digital maturity and the challenges inherent in developing that maturity.

# CASE STUDIES IN DIGITAL TRANSFORMATION



We don't want vendors, we want partners.

—Chief Information Officer, Community Bank in the US

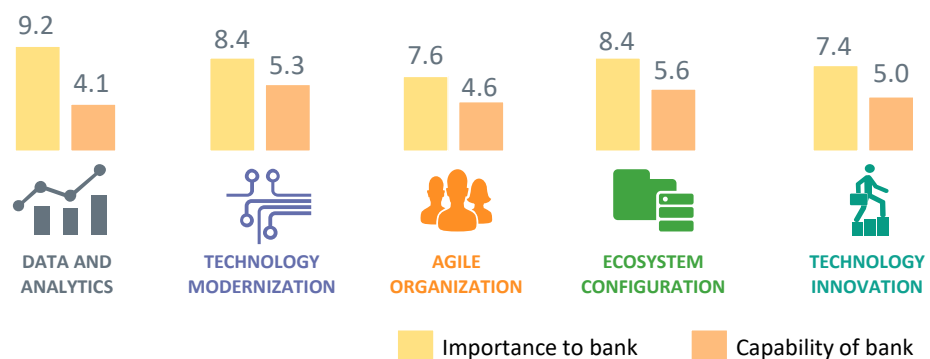


Celent conducted structured interviews with five banks that are undergoing digital transformation initiatives. The interviews covered aspects of digital maturity using the digital wheel shown earlier.

During each interview, Celent captured the institution's perceived importance of each topic as well as its self-assessed capability within each (Figure 3). The data below suggests a strong correlation between the perceived importance of an attribute and institutions' self-assessed capability. Taken at face value, this suggests that these banks are investing in areas they view as critically important.

Data and analytics showed the widest gap between importance and capability, as smaller institutions tended to be more critical of their internal capabilities. Many interviewees noted strategic objectives to turn data into actionable customer insights or hyper-personalized experiences, an aspiration in line with this segment's traditional focus on customer centricity. Tech modernization had the second largest gap. Smaller banks tended to emphasize being farther behind on modernization efforts than they would like (e.g., core replacement). In part, this may be a result of community financial institutions being comparatively more reliant on their core systems vendor.

**Figure 3: Perceived Importance vs. Capability**



Source: Celent, n=5

The following sections explore each bank's responses to our interview questions and provide analysis for each case study.

## Larger Super-Community Bank in the US

“The tech needs to be the right fit and can’t be so far in the future that it sits on a shelf...What do the customers need *now* to succeed?”

This institution has \$20–30 billion in assets with more than 60 branches in the western US.






This organization has its hands in a bit of everything, focusing on a variety of strategic initiatives which include greenfield projects as well as modernization initiatives.

Its strategy for 2022 involved three major pillars:

1. Broadening transformation so that digital initiatives aren’t asymmetrical but instead touch all parts of the organization
2. Going deeper on client-led transformation with critical digital touchpoints (e.g., unified front-end)
3. Achieving better customer segmentation through improved data to drive hyper-contextual experiences

The overarching strategic objective for this bank is a deep focus on client-led transformation. This means creating meaningful contextual or persona-based experiences for the customer while driving a focused customer segmentation (or a segment of one). A priority is to unify customer experiences across front-end channels in all lines of business, for both employee-facing and customer-facing applications.

**Figure 4: Digital Transformation Capabilities Self-Evaluation**

		Importance	Capability	Comments
DATA AND ANALYTICS		9	6	<ul style="list-style-type: none"> <li>Extremely important for vision of hyper-contextualization.</li> <li>Disparate current views of data from acquisition growth.</li> </ul>
TECHNOLOGY MODERNIZATION		7	5	<ul style="list-style-type: none"> <li>Legacy transformation is needed but up in the air at the org level.</li> <li>Ring fencing core and working on the outside.</li> <li>Deciding on migration path or best practice.</li> </ul>
AGILE ORGANIZATION		9	4	<ul style="list-style-type: none"> <li>They want to be change agents for agile within the bank, but that vision is hard.</li> <li>Currently customer journey mapping.</li> <li>The outcome is to change processes around agile.</li> </ul>
TECHNOLOGY INNOVATION		7	5	<ul style="list-style-type: none"> <li>Innovation is about current needs.</li> <li>They don’t want tech sitting on a shelf for years if the benefits won’t be realized soon.</li> </ul>
ECOSYSTEM CONFIGURATION		8	6	<ul style="list-style-type: none"> <li>Best approach for them is partnership.</li> <li>They want to do best of breed.</li> <li>Ecosystem needed for true 360 degree view.</li> </ul>

Source: Celent interview Q = For each technology characteristic, please indicate

Part of this transformation will involve embracing broader connectivity, which for them is a greenfield strategy. Connectivity includes API-enabled accounting software, ERP systems, payments platforms, and other applications to better operate in a unified ecosystem. The bank views connectivity as a way to begin building out propositions for Banking-as-a-Service (BaaS) or embedded finance.

This bank grew by acquisition, so solving for some of the challenges of silos is still relevant. Underlying many of its ambitions over the coming years is a need to remove some of the many data silos which can add friction to efforts for personalization or hyper-contextualization.

Moving beyond existing silos in certain instances will involve modernization efforts, however the bank is still exploring routes to take with its core platform. The existing strategy is to ring-fence the core as much as possible, which would allow them to work on front-end capabilities, but questions of long-term viability remain. The bank is also exploring if modern core features like real-time are valuable to customers.

Ultimately, the client centricity of this organization is leading them to make more pragmatic decisions about how they invest in technology. The newest bells and whistles may provide value, but if they are not firmly rooted in the mantra of helping customers today then it's unlikely to garner investment. This focus on what's best for the customer is what drives a best-of-breed approach to technology and drives interest in broadening its base of ecosystem partners.

The bank also underscored the importance of C-level support for new investments into digital. Leadership at the bank understands the need to invest in digital banking, which has not only enabled funding but gives them leverage to have conversations with others in the organization about the importance of change.

#### Key Priorities

**1**

Build on initiatives for broad client-led transformation

**2**

Assess the importance of core migration and viability of options

**3**

Move beyond silos to provide better customer-centric banking

## Midsize National Bank in the US






“Partnerships and openness in an ecosystem are critical to innovation for smaller banks.”

This institution has a little more than \$50 billion in assets and close to 150 branches in the US.

Like many banks, this institution is currently undergoing a merger integration of two similarly sized institutions. Typically, merger integrations can occupy resources within an organization, leaving little room or appetite for additional investment into change-the-bank technology. This bank, however, was very deliberate at the start of the merger that they would take the opportunity to modernize applications during integration. It moved beyond managing the conversion and saw significant transformation, which they admit required significant planning and attention to execution detail.

The goal is to drive 100% end-to-end digital processes for both employees and customers. The bank has already migrated to a new online banking platform, a new small business digital platform, and a modern treasury management solution. Many of the enhancements to these experiences are driven from its Customer Experience (CX) organization internally.

**Figure 5: Digital Transformation Capabilities Self-Evaluation**

		Importance	Capability	Comments
DATA AND ANALYTICS		8	6	<ul style="list-style-type: none"> <li>• They feel they are better than peers but admit work needs to be done.</li> <li>• Working on a merger integration which is introducing new silos.</li> </ul>
TECHNOLOGY MODERNIZATION		8	8	<ul style="list-style-type: none"> <li>• Foundational to their digital maturity going forward.</li> <li>• Moving to a more modern real-time core platform which is very leading edge among peers.</li> </ul>
AGILE ORGANIZATION		5	5	<ul style="list-style-type: none"> <li>• Important for them but not critical to success.</li> <li>• They find agile is often used to solve every problem rather than fitting it to purpose.</li> <li>• The org needs to support agile, but know where it works.</li> </ul>
TECHNOLOGY INNOVATION		6	5	<ul style="list-style-type: none"> <li>• Current focus on front-end innovation.</li> <li>• As merger continues and modernization efforts are realized they will leverage open architectures.</li> </ul>
ECOSYSTEM CONFIGURATION		8	6	<ul style="list-style-type: none"> <li>• Partnerships are critical for them to succeed.</li> <li>• They find partners and ecosystems to be critical to allowing for innovation.</li> </ul>

Source: Celent interview

Some banks have decided to begin building 100% digital parallel brands which operate as speedboats to get around the constraints of existing legacy technology. This bank launched a parallel offering to test innovation in a completely digital technology stack. A new cloud-based technology stack allows them to test new cloud-native tools or scalability on cloud infrastructure.

Long term, the bank cites efficiency as critical to compete. This will involve moving more of the existing technology footprint to the cloud, giving them more resource flexibility. This bank, like many in the industry, wants to move spend away from keeping the lights on and toward more value creation.

They are also exploring how to adopt Banking-as-a-Service (BaaS), allowing the bank to leverage its charter to provision capabilities out to non-banks, providing additional revenue streams. This is a road-mapped goal enabled by the modern API-enabled core.

Management of these changes is critical in the bank's view. Risk and compliance have been involved from the very beginning on many of the solutions or technologies deployed. Those groups have been critical to ensuring a smooth transition as they make the jump to cloud. The bank made significant effort to prove robust security for new deployments and has been very careful to not sacrifice customer experience during the transition. A question they often grapple with is how to simplify technology and customer experiences while not sacrificing delivery.

#### Key Priorities

**1**

Grow the footprint of the modern core platform and operationalize real time

**2**

Leverage existing digital brand as a testbed for innovation

**3**

Move toward a more real time API stack to allow for problems to more easily be solved






## Super Community Bank

“The key question we continually ask ourselves is: How does the customer want to do business with us?”

This bank with ~\$10 billion in assets operates approximately 50 branch offices in Arizona, California, Kansas, Missouri, Nevada, and New Mexico, and SBA loan and deposit production offices in Arizona, California, Colorado, Illinois, Indiana, Massachusetts, Michigan, Nevada, Ohio, Oregon, Texas, Utah, and Washington. It offers a full range of commercial and personal banking, trust, and wealth management services.

Traditionally a commercial bank, it was heavily reliant on in-person customer engagement across lines of business. The bank underinvested in digital channels, yet was not experiencing adverse consequences—until COVID-19 “threw them a curve ball.” Prior to the pandemic, the bank initiated an enterprise-wide digital transformation effort in which it sought to leverage its in-person culture, while critically reviewing channel systems. This effort was substantially accelerated because of COVID -19. Despite the importance the bank places on elements of digital transformation, its capabilities remain well behind where they need to be (Figure 6). For example, when many banks attribute 25% of new consumer banking sales to digital channels, they were realizing just 2 to 3 percent pre-COVID. Even now, there is no digital lending capability for business and commercial customers of the bank.

**Figure 6: Digital Transformation Capabilities Self-Evaluation**

		Importance	Capability	Comments
DATA AND ANALYTICS		10	3	<ul style="list-style-type: none"> <li>1-year into enterprise data governance effort.</li> <li>Building a data warehouse.</li> </ul>
TECHNOLOGY MODERNIZATION		9	5	<ul style="list-style-type: none"> <li>Migrating select systems to the cloud. Early systems include CRM, commercial lending.</li> <li>Many systems are decades old still.</li> </ul>
AGILE ORGANIZATION		8	5	<ul style="list-style-type: none"> <li>Tenured employee base. Agility not embraced broadly.</li> <li>Acknowledged need for a significant cultural change.</li> </ul>
TECHNOLOGY INNOVATION		8	4	<ul style="list-style-type: none"> <li>Establishing a “test and learn” culture and work processes.</li> <li>Sunset previous project management office.</li> </ul>
ECOSYSTEM CONFIGURATION		10	6	<ul style="list-style-type: none"> <li>Slowly embracing open platform thinking.</li> <li>Migrating to pivot away from core system vendor in favor of open system vendors with pre-certified integrations to its core.</li> </ul>

Source: Celent interview

Like many of its peer institutions, this bank is heavily reliant on its core banking system vendor. Many legacy applications are decades-old monoliths. It described the bank’s relationship with the vendor as “a story of conceding desired

capabilities for the sake of ease of core banking system integration.” While there are no plans to replace the core system, it is purposefully looking outside its core vendor for open systems vendors with pre-certified integrations to its core.

At this point in its digital transformation journey, the bank remains primarily focused on front-office capabilities, such as digital loan origination and modern identity verification approaches—with no short-term plans to revisit middle and back-office systems and work processes in a comprehensive way. Broadly, Celent sees a two-fold source of friction hampering the bank: culture and technical.

Culturally, the bank is traditional, with a stubborn resilience to maintain the status quo. A significant percentage of senior management have been with the bank for over two decades. Substantive change in this environment can be exceedingly challenging. Moreover, much of the bank’s technology stack is dated. These further hampers progress, making even incremental change costly and time consuming.

### Key Priorities

**1**

Critically review channel systems

**2**

Strategically migrate to open system vendors

**3**

Enhance digital customer engagement once data maturity is achieved



## Northeast US Community Bank

“...Digital transformation means speeding up and aligning on the dramatically fast pace of change.”

This ~\$1.5 billion community bank based in the Northeast US has served its communities for more than 150 years with a dedication to personal service, a commitment to community, and user-friendly technology.

While the bank clearly embraces the imperative to deliver a rich digital banking experience, comprehensive digital transformation remains elusive. The bank created an innovation role that reports to the CIO, but many in the bank are not fully committed to the value of technology-based innovation. For example, the bank is only now working on defining and illustrating how data can add value. Led by the CIO, this bank’s fledgling digital transformation program’s intent is not exotic; the goal is simply to create a culture and technical foundation that adds efficiency and agility. The bank is a strong player with a large share in its defined market, so it does not have a desire to experiment with new business models. In fact, its historic success stifles creative thinking and lessens the perceived imperative for change, according to the CIO. In Celent’s view, this kind of complacency is all too commonplace, particularly among community FIs.

For most banks, COVID-19 was a catalyst for change—but not so much for this bank. Instead, the pandemic had a bit of a reverse effect. As the CIO described, “Customers missed seeing us and flocked to our branches when they re-opened.”

The bank’s CIO considers data and analytics coupled with technology modernization as the foundation of digital transformation. On a 1 to 10 scale, he rates the bank 2.5 across those capabilities (Figure 7).

**Figure 7: Digital Transformation Capabilities Self-Evaluation**

		Importance	Capability	Comments
DATA AND ANALYTICS		10	2	<ul style="list-style-type: none"> <li>Still defining and illustrating how data can add value. No broad organizational buy-in.</li> </ul>
TECHNOLOGY MODERNIZATION		10	3	<ul style="list-style-type: none"> <li>Abstracting the core banking system. Sourcing non-core component functionality from open systems vendors.</li> <li>Early in the process.</li> </ul>
AGILE ORGANIZATION		8	4	<ul style="list-style-type: none"> <li>Low organizational agility.</li> <li>Expects agility to improve once core system is abstracted.</li> </ul>
TECHNOLOGY INNOVATION		7	5	<ul style="list-style-type: none"> <li>Absolutely reliant on partners for innovation.</li> <li>Winnowing down use of core system vendor beyond the CBS.</li> </ul>
ECOSYSTEM CONFIGURATION		8	6	<ul style="list-style-type: none"> <li>Considers its migration to open-systems vendors a major initiative that leverages the ecosystem.</li> </ul>

Source: Celent interview

“The better we think we’ve been doing, the less important the perceived imperative for change.”

Like so many community financial institutions, this bank is heavily reliant on third party partnerships. It simply does not have (and cannot afford) a deep technical bench from which to draw upon. Being reliant on partners for innovation also affects its ability to be more agile. For this reason, the bank is appropriately focused on winnowing use of its core banking system vendor in favor of open-systems vendor solutions.

#### Key Priorities

1

Abstract the core banking system

2

Winnow use of core system vendor beyond CBS in favor of open-systems vendor solutions

3

Explore new capabilities while developing a “test and learn” culture

“Make sure you take time to understand your organization’s core competencies and key value proposition. Don’t invest in things that aren’t strategic. Ask, discuss, forge consensus. Don’t rush into it. Outsource the rest.”

## Small Credit Union in the Midwest






“The underlying technology ‘plumbing’ is critical for enabling innovation. Dead weight platforms must evolve.”

This Midwestern credit union has ~\$4 billion in assets and more than 28 branches across its footprint.

For this institution, digital transformation is all about the member experience. Whatever makes the member experience more valuable is where investment dollars for digital maturity will go. This involves agility and flexibility to be where the customer is as they evolve over time. It’s also about more effectively and efficiently providing for their financial wellness and financial needs.

The credit union, however, is generally leery of using the term “digital transformation” internally as it does not provide any specifics. The term could mean any number of things to any number of people, making it more difficult to effect change. For them, defining digital goals is a critical step in being able to set a proper strategic roadmap.

**Figure 8: Digital Transformation Capabilities Self-Evaluation**

		Importance	Capability	Comments
DATA AND ANALYTICS		9	4	<ul style="list-style-type: none"> <li>Need to figure out what to do with the data before they serve it up to customers.</li> <li>Have hired talent and implemented infrastructure which should help here.</li> </ul>
TECHNOLOGY MODERNIZATION		9	5	<ul style="list-style-type: none"> <li>Using a traditional core, but which is relatively more open than some.</li> <li>All new digital applications are on the cloud, but core is on-prem.</li> </ul>
AGILE ORGANIZATION		8	4	<ul style="list-style-type: none"> <li>New engineers bringing in agile capabilities opening up opportunities.</li> <li>Sometimes customer impact unclear.</li> </ul>
TECHNOLOGY INNOVATION		9	6	<ul style="list-style-type: none"> <li>Views plumbing as critical to innovation, so tech innovation often follows underlying projects.</li> <li>As an org doing a good job of incorporating fintech into the product.</li> </ul>
ECOSYSTEM CONFIGURATION		7	4	<ul style="list-style-type: none"> <li>Key for the CU is an open architecture</li> <li>The CU mantra is if they serve customers well that will open up opportunities, but early days</li> </ul>

Source: Celent interview

Still, this credit union pointed out that growth for them is 100% reliant on digital. This makes sense looking at the constrained markets in which credit unions and community banks operate, often with stagnant population or economic growth. Digital will allow this credit union to serve customers in new markets across the country, not just those groups which traditionally fall under their remit. As a strategic objective, moving to digital self-service for this CU is critical.

Yet while ambitions are high, the credit union is definitely feeling the burden of legacy technology, citing the importance of infrastructural “pipes” which

underpin so much of what the bank wants to do in the areas of data/analytics, innovation, ecosystems, etc. As they pointed out, “dead weight platforms can bring you down.”

Interestingly, this institution created an innovation lab to act as the voice of the member. The innovation group is responsible for making sure member needs are being met and any suggestions/ideas are evaluated and potentially implemented.

**Key Priorities**

**1**

Build multi-channel and omnichannel engagement

**2**

Create consistent customer journeys across applications

**3**

Build better customer propositions with data-driven insights

# COMPARING ACROSS THE ASSET TIERS



Smaller banks need leverage, whether that comes from ecosystem partners or flexible technology.

—Chief Digital Officer, Midsize US Bank



## Key Takeaways from Smaller Banks

Celent summarizes a few of the most salient points in our conversations with executives at five smaller banks. These are common threads and areas of opportunity echoed in the interviews.

- **Digital is still often a buzzword:** Some continue to regard digital as being all about channel delivery (front end). It is less common to encounter executives that equally embrace digitizing the middle and back office. However, views on this are changing rapidly and many IT leaders say they are receiving more support than ever.
- **Change is hard:** Several bankers spoke of a big gap between perceived importance across the C-suite and others in the organization. Change agents feel passionately, but their passion is often not broadly felt. There remains in many smaller institutions a stubbornly resilient status quo. Momentum to continue in “old-fashioned ways of doing things” continues to run strong in many CFIs.
- **Small banks are looking at new business models:** IT leaders are more eager to explore new business models in banking. Many focused on leveraging the bank’s charter to provide Banking-as-a-Service (BaaS) functionality to third parties, generating additional revenue. However, this is a road-mapped item which will come after modernization of back office applications.
- **Core banking transformation is becoming more common:** Historically a rarity, changing cores came up frequently in interviews, either as something already in progress or in planning stages. Banks are beginning to run up against the limitations of their core platform for strategic technology initiatives. While some are exploring options (e.g., ring-fencing), others were frank about the need to migrate.
- **Cloud is here, but skills are still needed:** The move to cloud is happening, but institutions recognize the need to go slow. New skills and ways of working are required, and a rapid and broad adoption of cloud represents too much risk. It is happening but at pace. Most organizations view the move to mission critical applications to the cloud as inevitable.
- **Some asymmetries in digitization efforts:** Many smaller institutions are innovating largely based around technologies directly impacting the customer. As one larger bank stated, “We had a decidedly customer-centric

approach. We invested in best-in-class experiences for our customers, yet colleagues are using dated tools. I wish I would have kept colleagues and customers aligned. The gap was our own making.”

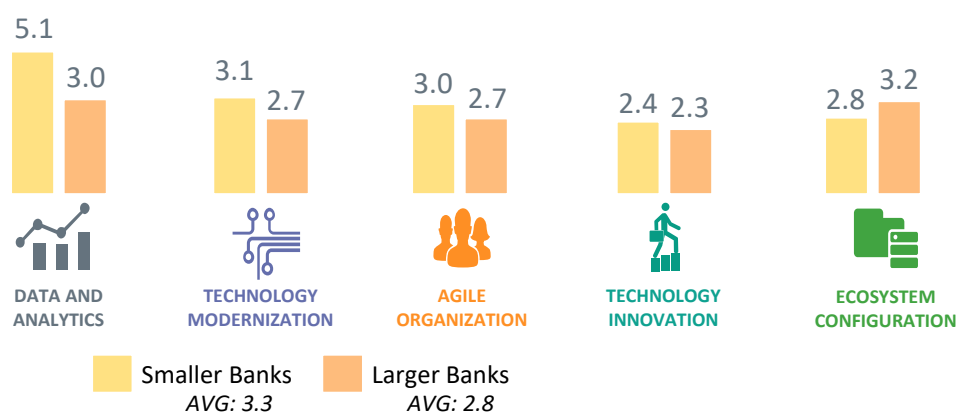
- **Many banks are testing and learning with digital-only brands:** A few institutions have or are considering launching digital-only parallel offerings, which would provide a sandbox for innovation or new ways of working. This would also involve a completely new real time tech stack, and most saw it as a progressive path to migration, not only on a new core but cloud native.
- **Institutions are looking for partners, not vendors:** Smaller banks know they cannot do it all themselves—they need partners to help. Partners could be traditional vendors or newer fintech companies. The culture often does not move fast enough for banks to do it all internally, so external partners are critical.

## Where Smaller and Larger Banks Diverge

Earlier this year Celent released a report titled “[Digital Maturity in Banking: Conversations with Tier 1 Banks](#)” in which we interviewed five C-level executives at larger banks in North America. The findings showed an increasing divide between megabanks (the “haves”) and their slightly smaller top 10–15 peers. As we began this effort with smaller institutions, some key differences and similarities between larger and smaller banks began to emerge.

While the immediate needs of digital banking are well known and often shared across tiers, the paths and barriers to get there can be different. While smaller banks showed leadership in areas like emerging business models (intent to offer BaaS capabilities), core migration to next-gen platforms, and customer-centricity, the group showed larger gaps in capability across every digital maturity technology characteristic except ecosystem configuration (Figure 9) Figure 8: .

**Figure 9: Average Difference Between Importance and Capability by Bank Size**

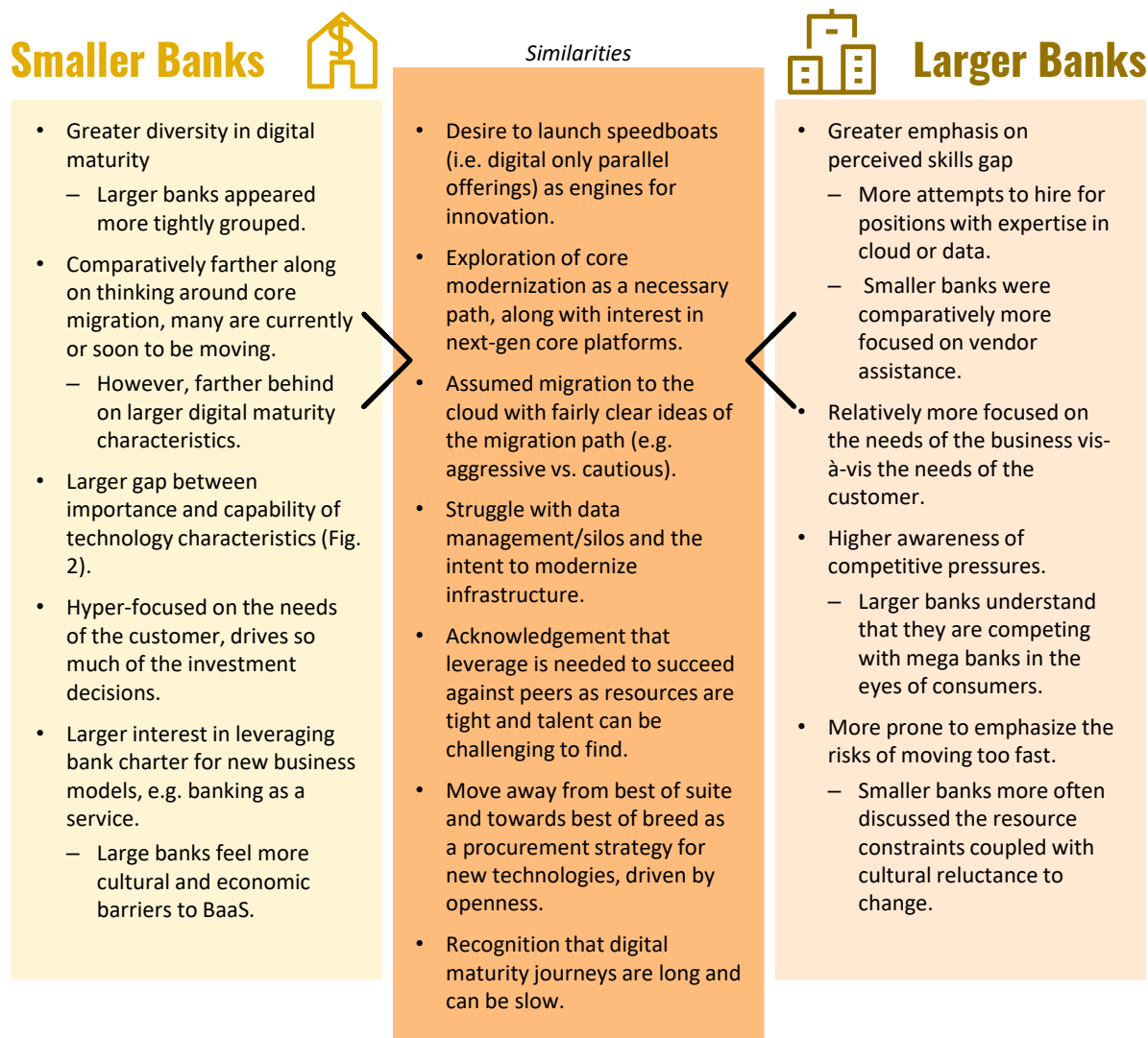


Source: Celent, n=10

Smaller banks have some advantages of dealing with fewer regulations (e.g., Durbin limit), running less complicated technology environments, or dealing with fewer high-fixed cost assets like branch networks. Still, major headwinds exist predominantly with smaller institutions who often consider traditional ways of

doing things as best practice for their customer base. Large-bank leadership tends to have a better grasp of the demands of digital, largely due to the competitive proximity to resource-rich megabanks.

**Figure 10: Similarities and Differences in Digital Maturity**



Source: Celent

It's worth noting in this assessment that there are more than 5,000 chartered banks in the US, and almost the same number of credit unions. There is enormous diversity in the industry. While Celent believes many of the characteristics discussed in Figure 10 are reflective of a large (and growing) portion of the industry, many organizations will take into account their own customers and strategies.

# PATH FORWARD

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You can be on the cloud, use APIs, or any other tech, but at the end of the day you need to solve for real customer problems.

—Head of Digital Strategy, US Credit Union



## Recommendations for Smaller Institutions

The road to becoming a digitally mature institution can be long. As stated earlier, the definition of digital is no longer about just the technology. It also includes a bank's philosophies, ethos, business models, people, culture, and processes. For those native to digital, it's in the lifeblood of the organization, yet for those just starting out the challenge can seem daunting. Celent offers these recommendations to smaller institutions:

- **Constantly ask what the value is for the customer:** Community banks are investing in technology but are often making sure that the investment can be demonstrably linked to a better customer journey. Applying this lens ensures that smaller banks retain the customer centricity which has been such a key value proposition.
- **Keep the big picture in mind:** Often digital can get bogged down within specific lines of business or teams. In other instances, the investment into digital can be asymmetrical. Leading institutions showed an end-to-end digital maturity strategy which included all aspects of the organization.
- **Don't rush real transformation:** Road maps for digital maturity can be long, especially in instances where legacy technology has defined the people and processes. IT leaders are migrating technology, but also looking to find personnel who fit the strategic vision of the organization.
- **Advocate for C-level support:** Support from the top was almost universally identified as a critical success factor for digital maturity. This not only provides sufficient funding for the right initiatives but allows IT leaders to affect change up and down the org chart.
- **Have a problem to solve and a use case in mind:** Many of the interviewees cautioned against using technology "because you have to." This will be an arms race that smaller banks will never win. Instead, focus on customer needs specific to the institution. This will better address pain points while ensuring that investments are made with purpose.



## What's Next

While banks are challenged with entrenched legacy infrastructure, which is often a hindrance, this does not have to be a definitive roadblock to developing new or useful products and services driven by technology. Even size, sometimes an obstacle, can act as an advantage when talent or resources are needed. Banks need to drive cultural change with technology change, while going beyond simply investing in “digital” banking.

Digital maturity will require pulling multiple levers, engaging partners, leveraging modern tools, and receiving dedicated resources. As this report shows, there is no one-size-fits-all recipe for success. Each organization will need to find the path that works based on its current and desired end state.

While smaller banks may not have the resources of a larger bank at their disposal, they are making significant progress toward digital maturity. Headwinds will always exist, but these institutions are showing themselves to be resilient competitors with a bright future

# LEVERAGING CELENT'S EXPERTISE

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Typical projects we support include:

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