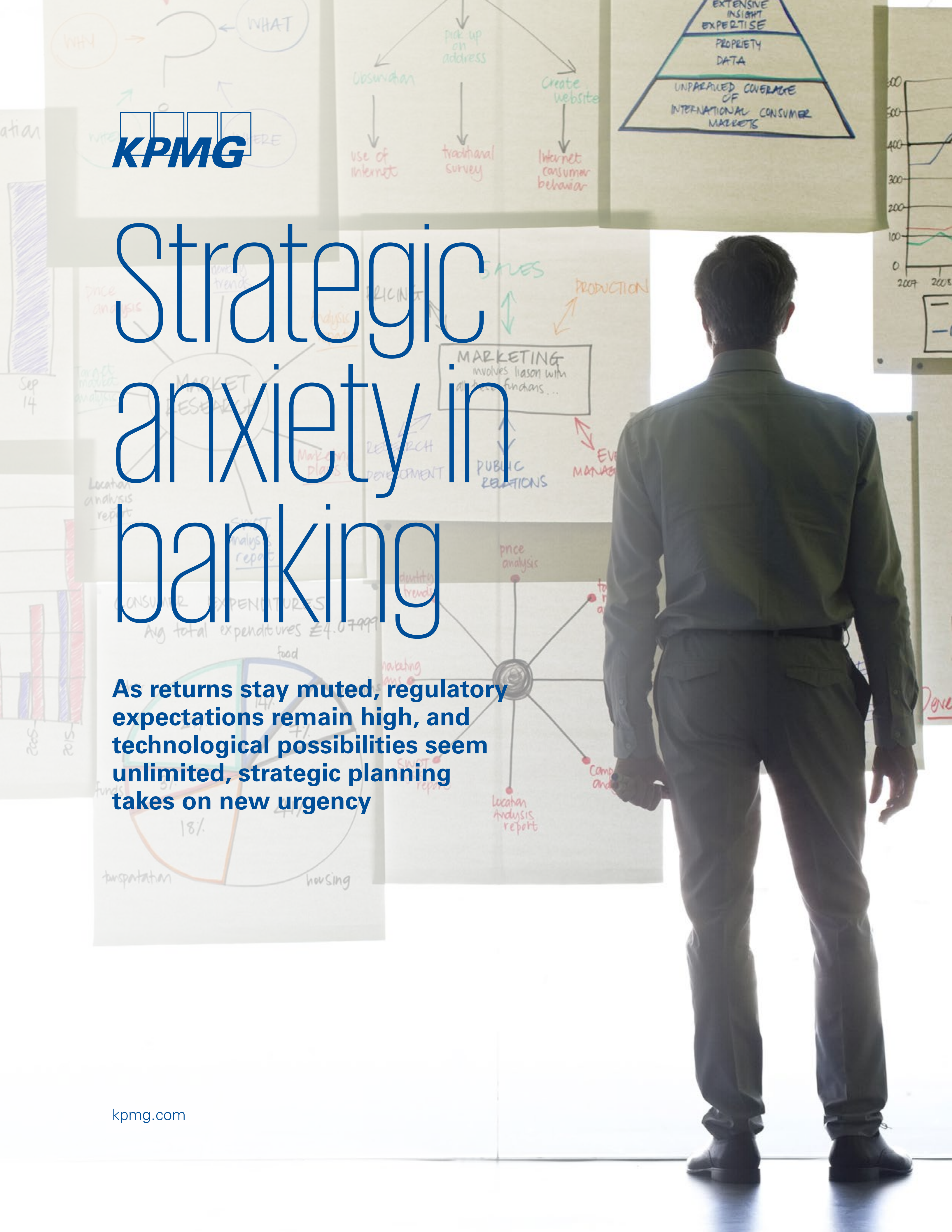

KPMG

Strategic anxiety in banking

As returns stay muted, regulatory expectations remain high, and technological possibilities seem unlimited, strategic planning takes on new urgency

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About the authors

Brian Stephens

Brian is a partner and leads KPMG LLP's (KPMG) U.S. Financial Services practice and has 37 years of experience with the firm. Brian is also the national sector leader of KPMG's Banking & Capital Markets practice, which serves commercial banks, regional and community banks, investment banks and securities firms, and diversified financial companies. He has spent the majority of his career working with large, complex, multinational banking and other financial organizations. Brian is well recognized globally as a thought leader and is frequently quoted on behalf of KPMG in national and industry publications.

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David is a senior Audit partner in KPMG's Banking and Finance practice. Based in New York, he currently serves on the Banking & Capital Markets Leadership Team helping to establish and implement KPMG's strategic approach to the industry. David is the lead partner for a significant international investment bank. He is also a Securities and Exchange Commission (SEC) reviewing partner and has completed two rotations through KPMG's Department of Professional Practice including one where he co-led the Banking and Capital Markets practice. David is on KPMG's Audit Leadership Team and was recently named the partner in charge of the firm's Global Delivery Center.

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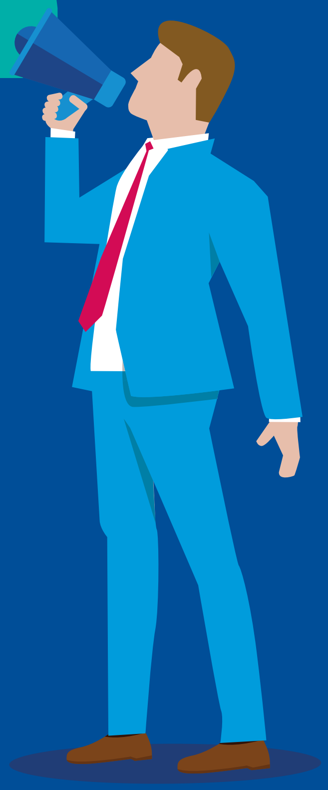


Context and commentary: A letter to our readers

It's a time of opportunity and anxiety in banking.

Planning for future growth in an industry that is rapidly digitizing is complicated and difficult work.

Meeting this challenge through strategic planning has, in our view, produced a very real sense of anxiety among a host of bank management committees and boards. Deciding how to organize that strategy—where to start, where to focus, and how to deliver results—is also proving to be vexing, for at least a portion of the industry.

"It certainly is true that many banks in the United States are on the path of reinvention; however, progress appears to be more fragmented than widespread," says David Reavy, KPMG's Professional Practice industry leader in the Banking & Capital Markets practice. "We interact with quite a few C-level executives and board members at banks of all sizes who are dealing with a kind of anxiety about their business strategy. Their bank is under pressure from all sides: regulators, bank and nonbank competition, shareholders and other stakeholders, and increasingly, fintech and other technology service providers. Strategic anxiety generally emerges as management teams try to solve for the approaches that allow their bank to compete best while lowering costs and meeting heightened regulatory expectations."

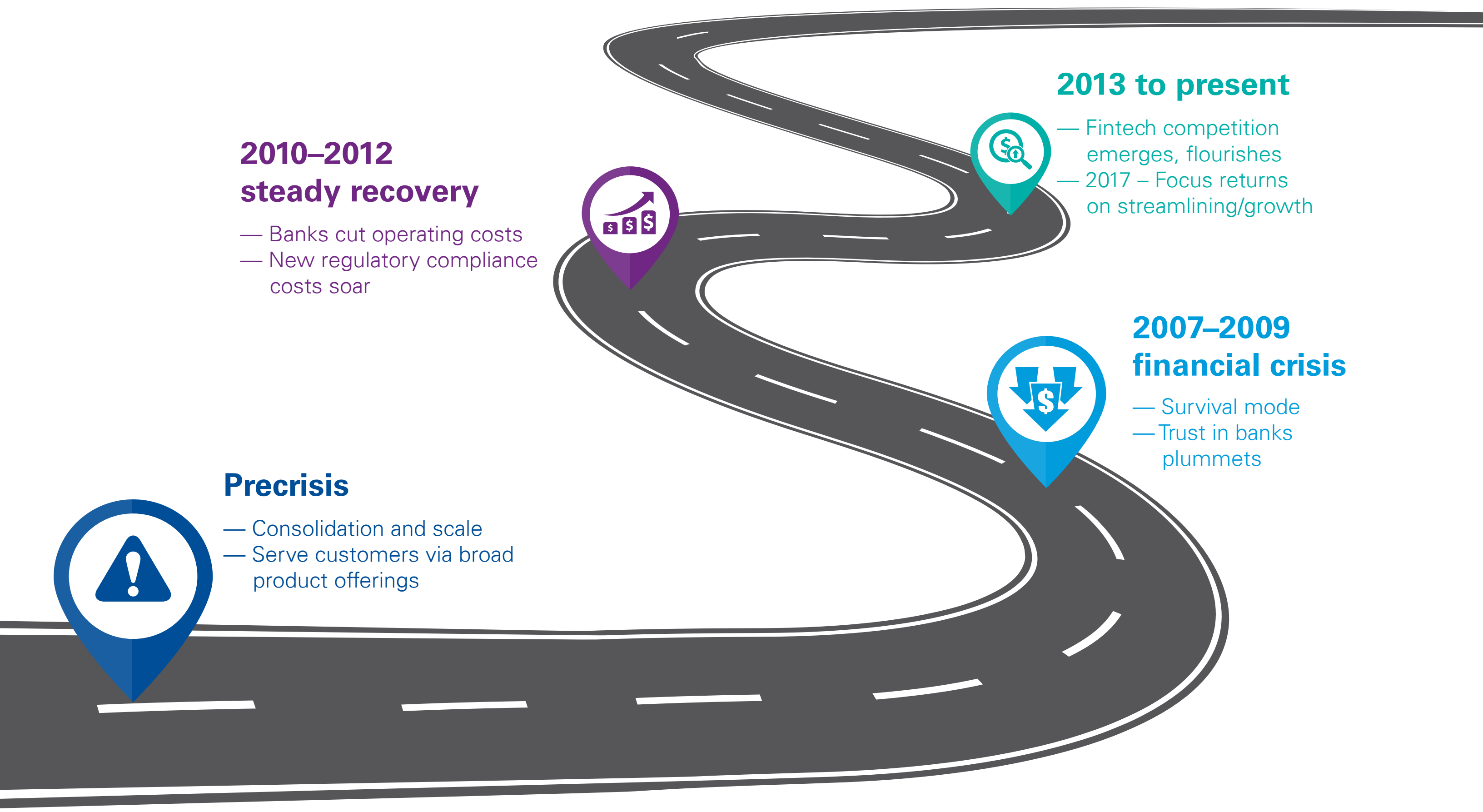
"We are seeing many banks in a 'catch-up' mode," says Brian Stephens, KPMG's national leader of Financial Services, and the national sector leader of KPMG's Banking & Capital Markets practice.

In the pages ahead, we will define strategic anxiety as we see it, offer our views on the evidence and causes of it, and offer some actions to consider to confront and manage it. Our aim in offering this paper is to assist in lifting the fog we believe has settled over the strategic planning process in banking.

Please read on, and we hope you'll join the conversation.

A look back and a glimpse of the future

The winding path to the present



The significance of the changes to the financial services industry since 2007 would be difficult to overstate. Having emerged from survival mode, banks have shifted to a focus on growth through better connectivity to customers and technology enablement.

Attention is squarely focused on confronting a number of forces: the ongoing impact of technology innovators, an acceleration of the network/platform economy, the commercialization of data and analytics, robotic process automation, and cognitive technologies. It has created an environment where banks must innovate or step aside.

While these developments create opportunities, they also have created the anxiety over the strategic planning of many banks.

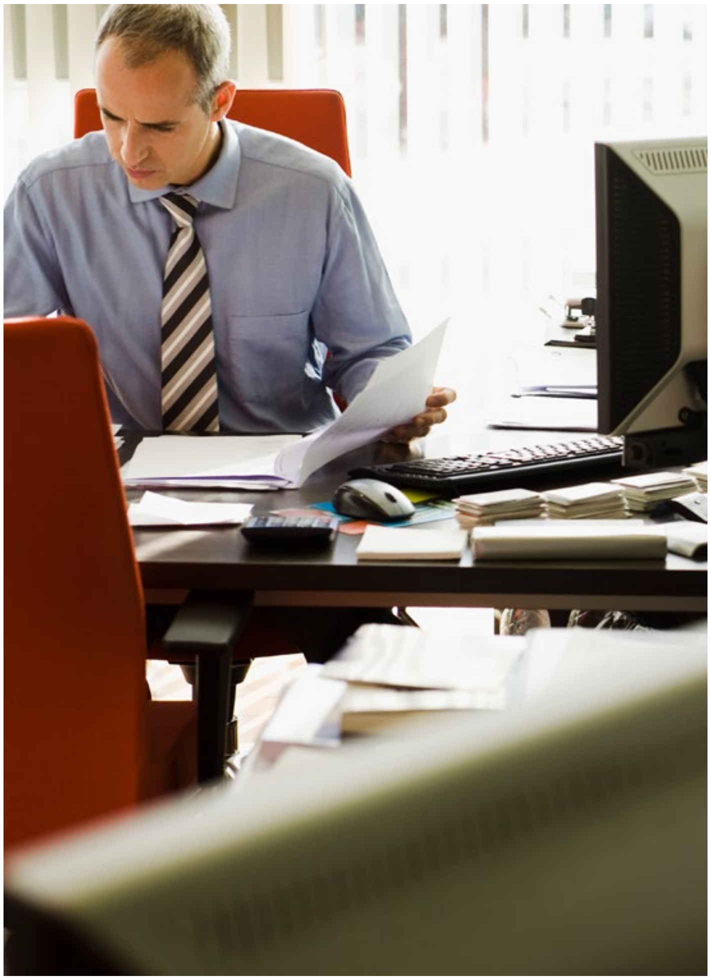
State of the banking industry: Strengthening, yet challenging

As the nation's economy has regained its footing, many commercial and savings banks in the United States have slowly stabilized their balance sheets. Even though industry-wide net income dipped in 2016, compared to the previous year, almost two-thirds of the 5,900 institutions insured by the Federal Deposit Insurance Corporation (FDIC) reported higher earnings in 2016 than in 2015.

Nevertheless, FDIC Chairman Martin J. Gruenberg warned in February 2017 that "the operating environment for banks remains challenging. Low interest rates for an extended period have led some institutions to reach for yield, which has increased their exposure to interest-rate risk, liquidity risk, and credit risk. Banks must manage risks prudently to ensure that industry growth is on a long-run, sustainable path."[1]

These statistical indicators provide additional insight into the financial state of the banking industry[2]:

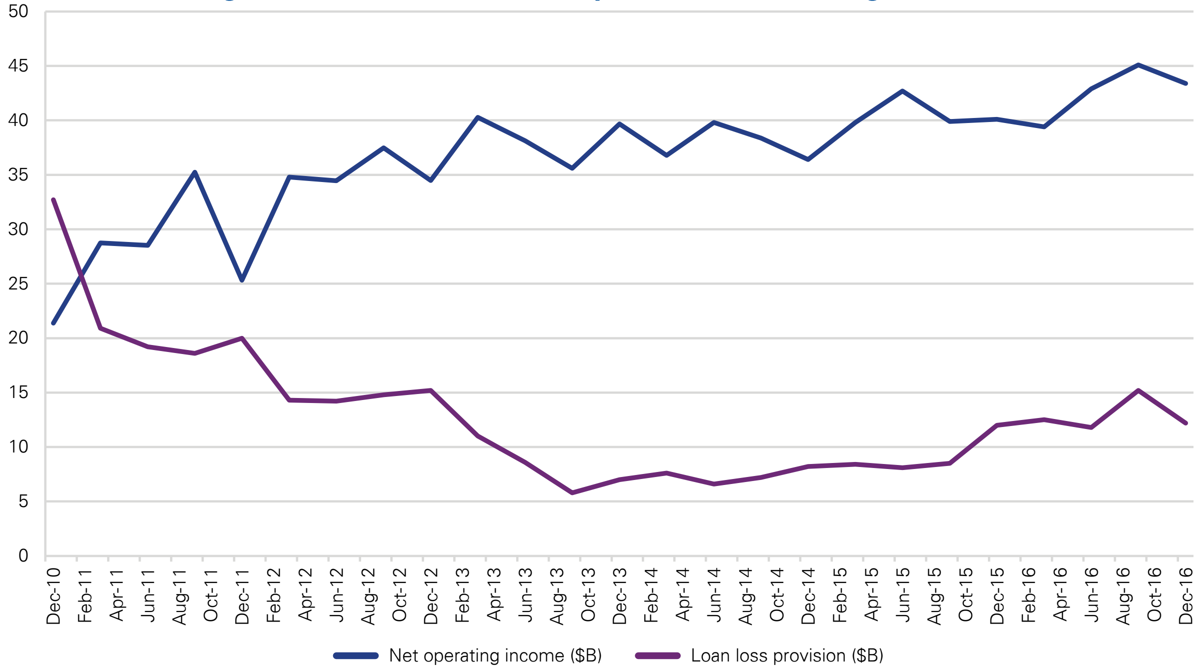
- Net operating revenue grew 4 percent year-over-year, with net interest income increasing but noninterest income declining.
- Average industry-wide net interest margin (NIM) rose 6 basis points to 3.13 percent, and the average return on assets for 2016 was 1.04 percent, unchanged from 2015.
- NIM remains a challenge at the largest banks in the United States. In the fourth quarter of 2009, the NIM for banks with assets in excess of $250 billion was 3.39 percent. In the fourth quarter of 2016, it was 2.75 percent.



[1] FDIC Quarterly Banking Profile, February 28, 2017

[2] Ibid.

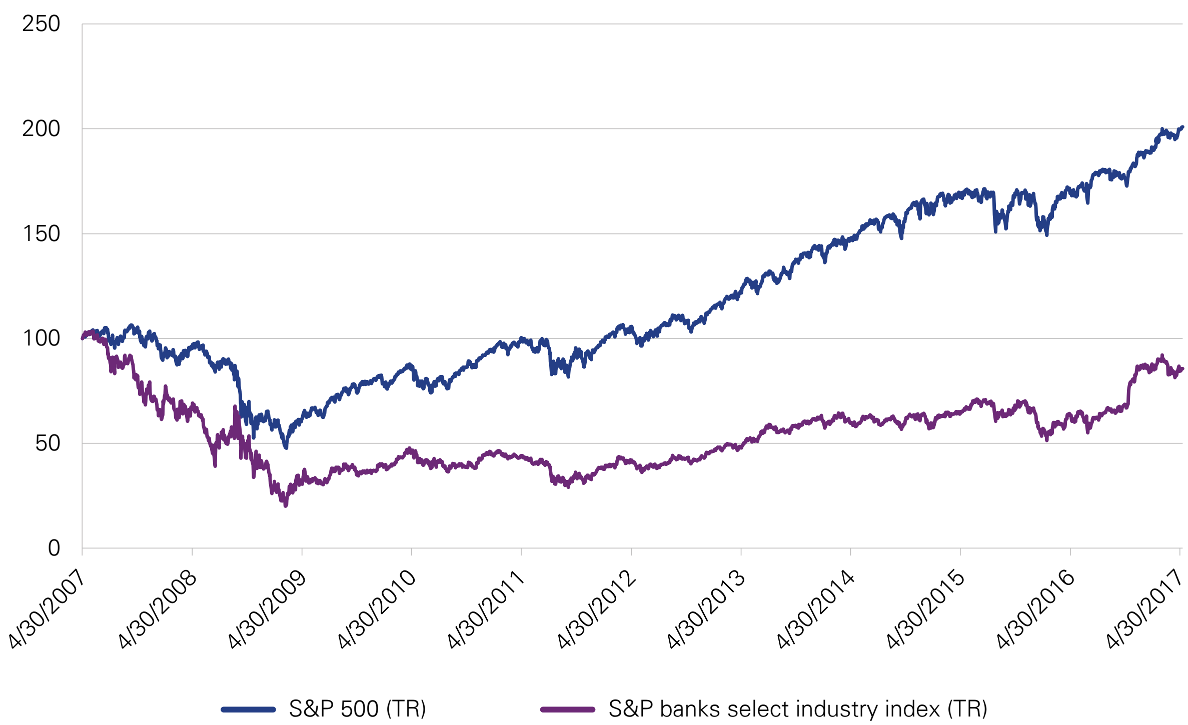
Figure 1: Net income/loan loss provisions 2010 through Q4 2016



Figures 1(above) and 2 (below): Although banks' net operating income has crept higher over the past four years, many banks remain in a challenged position. When viewed over a longer period, bank stocks since April 2007, for example, have lagged the performance of the Standard and Poor's 500. However if viewed over the most recent one-year and five-year periods, bank stocks have performed favorably in comparison to the broader S&P 500 index. This more recent positive performance, particularly over the last year is likely attributable to the pro-business climate in Congress following the recent election, the prospect of tax reform and a rising interest-rate environment.

Source: Net income/loan-loss provision, FDIC, March 2017;

Figure 2: S&P banks select industry index versus S&P 500



The data in the chart are based at 100 for comparison purposes.

Figure 2 source: Stock index, S&P Dow Jones Indices/S&P Global, May 2017.

Evidence of strategic anxiety

Flat return on equity across money-center and regional banks

Figure 3: ROAE of top 1000 U.S. banks

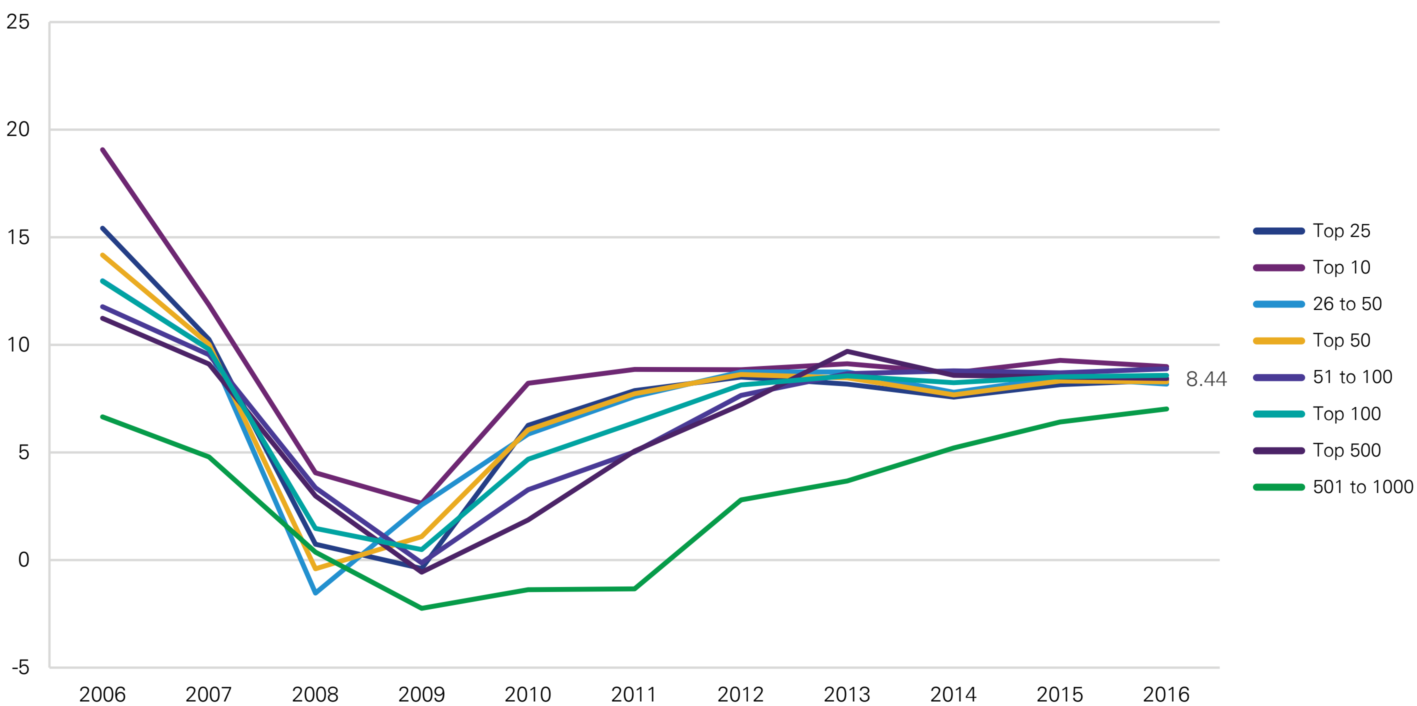


Figure 3 source: SNL/S&P Global Market Intelligence, KPMG Research and Analysis, March 2017

The "bunching up" of returns on equity across a large swath of the industry during the last two to three years, as shown in Figure 3, provides us with evidence that many banks are struggling with developing strategies that create returns that exceed their cost of capital—estimated to be 8 percent or more for money-center and regional banks.[3] Try as they may, most banks' ROE have lagged, with many banks' ROE almost seven percentage points lower now than a decade ago.

In our view, a key aspect in boosting ROE requires, in addition to cost-reduction efforts, leveraging technologies that scan and interpret expansive sets of social, interactive, and personal data to provide insights about the types of banking services and products customers need now.

This type of interpretation is now only beginning to take root in banking; however, other industries appear to be much further ahead.

[3] New York University, Stern School of Business: Cost of Capital by Sector (US), Jan 2017.

OCC statement on strategic risk

A January 2017 report on industry risks issued by the Office of the Comptroller of the Currency (OCC) said "strategic risk remains high for many banks, as management teams consider business model changes and search for sustainable ways to generate target rates of return in a persistent low interest rate environment."[4]

The OCC added that while "failure to innovate to meet evolving needs of financial services may place a bank at a competitive disadvantage," the agency also issued a warning about rushing too quickly—without adequate knowledge and preparation—into making radical changes to business operating models, despite the need to act and operate in a more innovative fashion.

The agency said although bank operating models "are under increasing pressure" to connect more closely with customers either directly or through ventures with other parties, "it is important for banks to focus on timely adapting risk management and control processes to these changes in business strategy."[5]

[4] "Semiannual Risk Perspective From the National Risk Committee, Fall 2016," Office of the Comptroller of the Currency, January 5, 2017

[5] Ibid.

Causes of strategic anxiety

If flat-lining ROE, our interactions with senior bankers and statements from the OCC give us evidence that strategic anxiety is a demonstrable issue among bank management and boards, the causes of it are equally as evident. Consider the impacts on profitability (and the need for new strategic action) due to:

— The tight interest margin environment

— The requirement for many of the larger banks to boost capital reserves

— The billions of dollars spent in the past decade on regulatory compliance mandates

— The revenue decline caused by the low interest rate environment

— The hundreds of billions of dollars institutions have paid in fines and settlement fees to government regulators and agencies over the past decade

— The ongoing, multifront attacks on the industry by platform-model businesses and fintechs that are influencing customer expectations when it comes to incumbent banks' products and services.

Customer experience and trust

Bankers are seeing no let-up in the increasing demands of impatient customers who want their banks to act less like their grandfather's stodgy depository institution and more like a contemporary retail institution.

There are consequences if a bank doesn't get customer experience and trust right. For instance, data from Forrester Research Inc.'s "Empowered Customer" and "North American Consumer Technographics" reveals that only half of bank customers are willing to keep their level of business with the bank, and 41 percent are unwilling to purchase additional products and services from their existing bank.[6] In addition, a survey of 2,000 adults with deposit or checking accounts in the United States conducted by Salesforce.com found that only 26 percent agreed that banks had their best interests in mind.[7]

"Know me. Create a suite of ideas and then act like a financial-services concierge. Leverage the vast amount of behavioral data already available about me that other industries are using and then offer customized products and services that fit my individual profile.

And, above all, don't make me wait."

[6] "The Threat (And Opportunities) Facing Banks Today," Victor Milligan, Forrester Chief Marketing Officer blog, November 17, 2016

[7] "2017 Connected Banking Customer Report: Insights Into the Expectations of Today's Retail Banking Customers," Salesforce, January 2017

Since 2010, when there were 319 deals and $9 billion worth of investments globally in fintechs, another 5,235 deals have been made through 2016, totaling $123 billion.

Source: "The Pulse of Fintech Q4 2016," KPMG, February 21, 2017

Despite a significant decrease in annual M&A and PE funding, fintech activity is strong. The decline globally in fintech investments in 2016 was a result of a decrease in mergers and acquisitions (M&A) and private equity (PE) funding in particular. M&A deals fell from $34 billion to $11 billion year over year. However, it is important to recognize that 2015 was a significant outlier in terms of M&A dollars attributable to fintech. The level of M&A deal activity (in 2016) came second only to 2015.

Source: "The Pulse of Fintech Q4 2016," KPMG, February 21, 2017

Fintech's relentless march

Although, the number of fintech deals declined in 2016 compared to 2015, even this level of activity suggests the time remains ideal for fintech partnerships. Fintechs and banks need each other, and customers have demonstrated they like the partnerships.

Global venture capital investment in fintechs reached a new high of $13.6 billion in 2016.[8] The resilience of the VC market for fintech opportunities suggests that fintech will continue to be an attractive sector in the future.

We expect fintechs to continue their invasion of payments and lending, personal finance/wealth management, money transfers, blockchain/bitcoin, equity crowdfunding, and other sectors.

Our conversations with senior bankers suggest many realize they should be "in the fintech game." But, our sense is that often those same bankers have not yet identified the fintech areas where investments would truly make a difference for their institutions and their customers.

In order to be able to assess the value fintech brings, bank executives "need to first have a defined problem statement and alignment on what they are trying to achieve," says Ann Armstrong, KPMG's National Fintech Coleader.[9]

> "Fintech offers a tremendous amount of promise for banks that decide to collaborate with, or directly invest in, fintechs. But, at the same time, the technologies offered through these firms can be complex and it can be unclear how to integrate into a bank's existing delivery processes. So, there is quite a bit of pressure on management to make the right decisions about investments that drive growth, streamline processes, and satisfy customers."
>
> – David Reavy, KPMG's Professional Practice industry leader, Banking & Capital Markets practice

[8] "The Pulse of Fintech Q4 2016," KPMG, February 21, 2016

[9] "The Pulse of Fintech, Q3 2016," KPMG / CB Insights, November 16, 2016

Marcus by Goldman Sachs™: An agile firm adapts

Boe Hartman, chief information officer, Goldman Sachs Bank

Photo credit: Goldman Sachs Bank

Goldman Sachs, a leading global investment banking, securities, and investment management firm that provides a wide range of financial services, continues to take bold strategic steps in shifting the consumer digital finance landscape. Less than a year ago, Goldman Sachs Bank USA (GS Bank) launched Marcus by Goldman Sachs (Marcus), an online lending platform. Marcus utilizes an open source, application programming interfaces-powered (API) business model to offer unsecured, no fee, fixed-rate personal loans to consumers with good credit (FICO 660+), who are looking for an alternative to high-interest-rate credit cards, which often have fluctuating APRs.

Boe Hartman, chief information officer of GS Bank, of which Marcus is a product, spoke with Mitchell Siegel, KPMG's Financial Services Strategy leader and Timothy Dougherty, KPMG's Financial Services Content Creation director, about a range of issues. The issues include how GS Bank was built from the ground up in 12 months, leveraging modern technology, to the benefits and culture of working at a start-up within an established financial services company and the road ahead for the online platform in the months and years ahead. Here is an edited version of that discussion.

KPMG:
"Building an operating model that relies on open API architecture and offering unsecured loans to consumers seems to be quite a departure from Goldman's traditional business of serving large institutional clients. What was the thinking behind this departure from tradition?"

Hartman:
"Our firm has always looked to use the cutting-edge technologies that are available at the moment. As we look to build from the ground up, we use the most advanced platforms available to us that would enable us to grow going forward. The open architecture that Marcus uses is a simple extension of the philosophy at Goldman Sachs, which has been to embrace innovation and leverage the most advanced technology that allows us to best serve our clients."

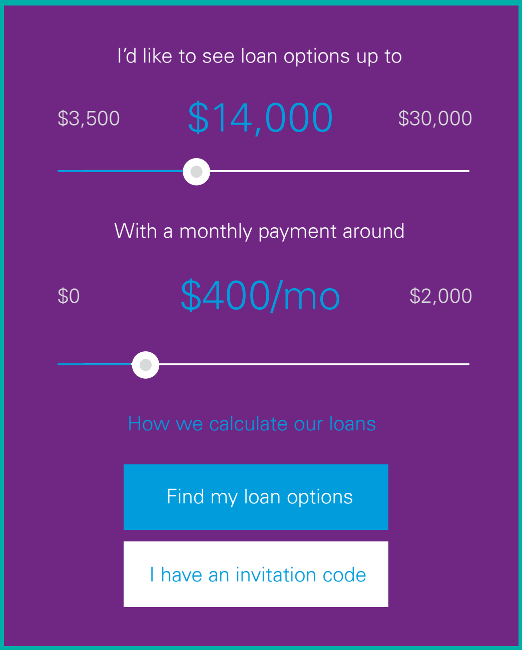
KPMG:
"Were there lessons you've learned about the open API concept and fintech collaborations that weren't apparent in the planning and development stages?"

Hartman:
"We are always learning and making adjustments. What was more important, in addition to employing an open API model, was the selection of the technology partners at the very beginning. The partners allowed us to build a flexible architecture that improves the flow in onboarding customers. After we launched, we saw instances where we could improve the onboarding, and we went back to resequence the flows and improved efficiency, which we were able to do very quickly."

KPMG:
"There is quite a bit of commentary in the industry about a 'disconnect' between consumer banks and customers in terms of speed, transparency, and lower-friction experiences. Would you say your organization has had success in avoiding that 'disconnect,' and, if so, how did you do it?"

Hartman:
"We engaged in extensive targeted consumer research, and we had weekly focus groups with consumers for many months. It's what we call a 'cocreation mind-set' and we spoke to over 10,000 people. Our goal was to understand their pain points in dealing with financial services businesses.

"For example, they told us they disliked fine print about fees. Marcus has no fees ever and we are very transparent in how we present this. We also offer a flexible payment schedule. So, if the borrower needs a loan and wants to pay $375 a month, we try to arrange for the term that fits the borrower's needs. It might be 39 months or 66 months and doesn't have to fit into the traditional three- to five-year time frame. It's very flexible. Our technology on our webpage has what we call a 'slider,' which is a technology mechanism that allows borrowers to pick the amount of the loan, set their desired payment amount, and choose the length of the loan. And, we heard from borrowers that they are tired of variable interest rates, so we offer a fixed rate for the life of the loan."



"Consumers also said that, when they needed to speak to us on the phone, they wanted immediate answers; they didn't want to be put on hold or transferred again and again. Because of this, when you call our call center, real people, not machines answer and, despite rising call volumes, we are answering the phone in under ten seconds."

KPMG:
Did all Marcus employees come from Goldman?

Hartman:
"We are thrilled with the team we have built. Goldman Sachs is a strong brand and we have benefited from that. It is a value of the firm never to compromise on talent and that continued with Marcus since day one. We have a very diverse group. Roughly a third from traditional consumer finance companies and banks. A third were hired from within the firm. And a third from nonfinancial places, such as the top technology companies or large consumer brands whether it is Google, Facebook, Amazon, or Pepsi. Bringing all of these people together creates a special culture. And we all sit together across all functions on the same floor. There is no assigned seating. All our walls are white boards and we have good, positive, sometimes chaotic energy. Goldman Sachs culture is all about client centricity, risk management, execution, and great talent. The Marcus culture is the same. It is just for a different customer segment."

KPMG:
"What intelligence have you uncovered with Marcus that might be migrated to other legacy parts of Goldman in order to establish additional high-tech platforms?"

Hartman:
"One of the things I am most proud of is that we were able to build a digital bank from the ground up in 12 months, and we'll be involved in showing others in the business how we did that. Beyond that, we want to take the learnings to the entire organization and develop the same patterns in the architecture; whether it is agile delivery, story boarding, product creation, or our customer-centric approach. We hope to leverage this experience to convert to a more agile delivery capability across the board."

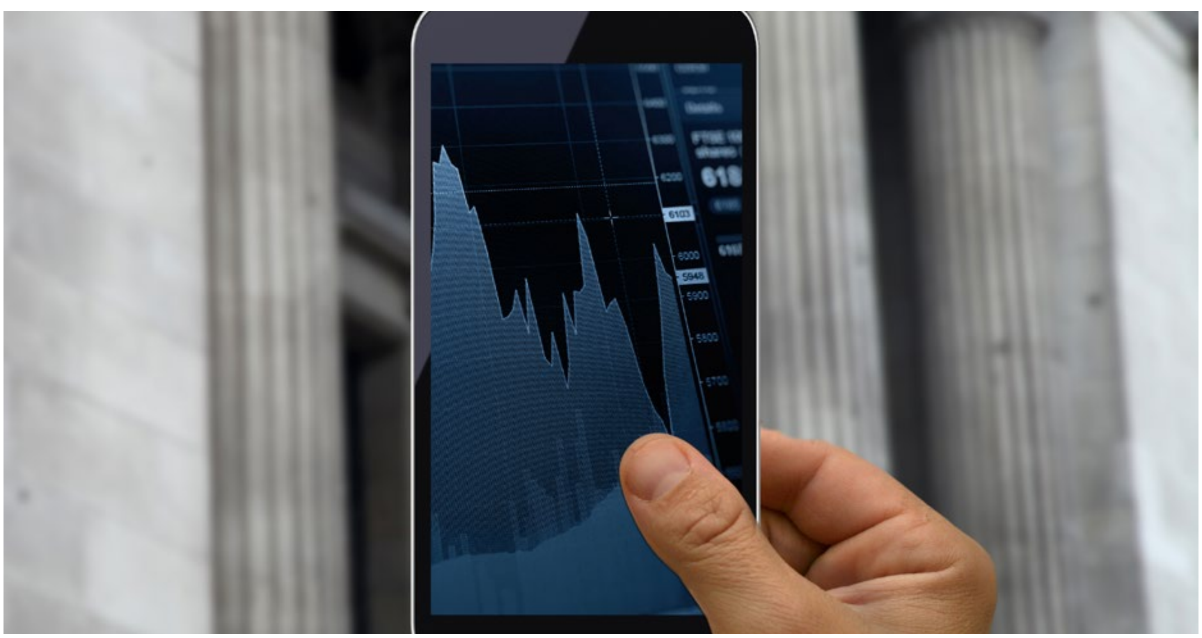
Regulatory uncertainty and the rise of "regtech"

With the change in administration, no one is sure what regulatory changes may be looming, so banks will need to prepare for the regulatory unknown, all while continuing to manage their inventories of existing regulatory matters. With the right approach, we believe that banks that can simultaneously remediate past regulatory findings, prepare and respond to new initiatives, and improve product competitiveness will come out ahead.

Part of the reason for our optimism is that we believe financial services institutions will soon be leveraging emerging regulatory technologies (regtech), which are already creating benefits for the industry.

With industry-wide compliance costs ballooning to an estimated $70 billion annually in the United States alone,[10] these regtech software applications, often hosted in the cloud, help the analysis of a bank's data (often in silos) to manage complex regulatory compliance requirements in an automated and repeatable manner. Regtech solutions have proven to be the accelerator that helps firms respond to increased regulator expectations while reducing compliance costs, increasing enterprise-wide coordination, and making firms' business strategies more agile.

Regtech solutions provide an excellent platform for supporting banks' strategic growth agenda, accelerating speed to market, and optimizing business processes while meeting regulatory standards. Regtech solutions provide a way to first connect business processes with the labyrinth of complex regulatory obligations and then streamline and simplify regulatory mandates into manageable processes that firms can institute effectively and relatively quickly.[11]



[10] "KPMG 2016 Global CEO Survey," KPMG International

[11] The Nexus Between Regulation and Technology Innovation," KPMG LLP, April 2017

Actions to manage strategic anxiety

Mine behavioral data

Understanding customer behavior is assisted by mining the enormous amount of behavioral data available about people who are connected through mobile devices, apps, and social sites.

There was a time when bankers could have a fairly accurate sense of the future when creating a strategic plan. After all, looking back, changes in banking evolved at a pace where managing them wasn't nearly as confounding as it seems to be at the moment.

If there is one message we believe is important to pass along it is this: The future is here and banks need to build strategic options that will allow them to compete into the future. To be sure, banks are moving in the right direction, yet strategic anxiety and uncertainty are causing resistance to faster change—even though most industry executives understand that change is essential.

Here are some action steps that might be considered:

Leverage customer behavioral data and artificial intelligence

At KPMG's Innovation Lab, where an industry's market signals are mined, analyzed, and put into context, Kesavan T. Sampanthar, the lab's executive director of innovation, says there is a strong belief among his colleagues that "if a bank is going to stay relevant, it must go beyond creating digital experiences or great customer experiences. Those are the end products."

"Change and relevance begin by really understanding customer behavior that is contained in behavioral data, and there is an enormous amount of behavioral data available today with so many people connected through mobile devices, apps, and social sites," he says. "This kind of data is invaluable when we consider how much banks need to understand the kinds of products customers want and how banks will help customers get what they want."

Therefore, a fundamental question that banks should be asking, he says, is whether the kind of data being analyzed is actually customer behavior data. Additionally, banks would be well served using machines for leveraging cognitive or artificial intelligence (AI) focused on customer behavior. "If banks incorporate machine learning into gathering and analyzing behavioral data, then they are going to gain an advantage."

Areas where AI is being deployed by banks, such as intelligent digital assistants to handle certain mundane customer interactions, are the result of machines being "taught" to recognize certain speech patterns or online usage behaviors. But, those are just initial steps for leveraging customer behavioral data using machine learning.

When customer behavioral data is funneled into AI applications, they begin to produce insights that can deliver a better customer experience as time goes on.

Those practices, Sampanthar says, can help a bank go a long way to becoming "more relevant and more predictive about what customers are going to do, and hence stay relevant through the customer experiences."

Banks need only to look at tech giants for clues to the power of behavior data and AI.

The giant retail tech companies may be mislabeled: "They may be selling TVs and computers and the like, but what they really are after is customer data," Sampanthar says. "The more information on a customer's life it gathers—whether it is a customer's media habits, their buying habits, or banking habits—the more insights are produced using machine learning tools." We see all of this feeding into the artificial intelligence, which is hugely hungry for behavioral data. The more behavioral data they have, the better their AI capabilities and that will help serve the customer."

"Banks should not be focused solely on changing all the back-end information technology (IT) hardware and software," he says, "we think that game is kind of in the past. Improving businesses processes is important," he says, "but right now banks need to get better at the future game, which is really understanding where customers are going."

Leverage the platform economy

The rise of the platform economy, and its bearing on how bankers think about their business, increasingly is creating an alternative to banks' traditional focus on a product strategy. One of the opportunities for growth exists when banks create a strategy that focuses on customers' needs, and they leverage the rapidly developing external ecosystem created by fintechs that are innovating services and products that customers say they want.

By aligning their organization with customer demands, and linking with this developing ecosystem, we believe banks may have a greater potential for faster and more compelling innovation. In that way, banks could improve their chances to be viewed in a positive light by discerning customers who seek to do business with innovativeorganizations.

Banks can therefore take advantage of the network effects of a platform business model, where they monetize digital user data by attracting many more users.

Amazon.com Inc.'s Amazon Web Services subsidiary, for example, is an innovation platform that provides cloud-computing services through an on-demand computing platform. It provides computing services, database analytics, and storage, among its 70-plus services. "Ultimately, what Amazon is after is customer data," Sampanthar says. "The more information on a customer's life it gathers—whether it is the customer's media habits, buying habits, or banking habits—the more products they can put in front of them."

That is the kind of strategy that more banks will need to consider pursuing in the future, Sampanthar suggests.

In banking, the platform model largely hinges on the willingness of banks to open their application program interfaces to share their software code to third-party partners as the primary means of innovation and attraction of new customers.

Opening APIs can allow a bank to start becoming more like a platform business. In that way, a bank can create services that any fintech can "plug and play" into, at which point the banks will gather even more data and understanding about how customers are using the bank's services. In other words, the more products and services it can offer through alliance and open API strategies, the more users it can attract.

In an open-source API environment where customer data is shared, the organizations start to see a melding of cooperation and competition—or "coopetition."

Play in the "sandbox"

Governments recognize the value of fintech innovation to the banking industry and customers.

A number of nations, including the United States, the United Kingdom, Australia, Singapore, Malaysia, and Thailand are either considering or have announced the development of "regulatory sandbox programs," which are technology environments where regulators and fintechs work together to develop ideas without bureaucratic restrictions that could stymie innovation.

These nations realize the importance fintech innovation can play in improving the efficiency of the banking system as well as improving the performance of the economy.

Among the requirements attached to the proposed law, introduced by Representative Patrick McHenry (R-North Carolina), fintechs would need to prove to government regulators that the fintech idea would serve the public interest and not create a systemic risk to the financial system.

Source: "The Pulse of Fintech Q4 2016," KPMG, February 21, 2017; ''U.S. House Bill Aims to Set Up 'Sandbox' for Fintech Innovation," The Wall Street Journal, September 22, 2016

Engage in “coopetition”

Coopetition, we believe, is an arrangement that increasingly makes sense for banks and fintechs. It comes down to the acceptance by both parties that they need each other.

Coopetition offers the significant allure of a “win-win-win” situation. Banks may, in the short term, decide to cease offering certain low-margin products or services, but they could eventually attract many more customers looking for other products and services if they allow innovative fintechs access to the bank’s customer data.

“You could define coopetition as a shift from a model of exclusivity to one of inclusivity,” says David Pessah, a director at KPMG’s Innovation Lab, specializing in financial services. “And that’s not only as it relates to products and services. It’s also about its ability to work with other participants in the banking ecosystem. It’s all about how interconnected the bank can become, and how it can personalize the banking experience.”

Call the concept revolutionary or evolutionary. Regardless, coopetition may be a major step forward in banks’ quest to improve customers’ trust, satisfaction, and user experiences.

Kabbage: An innovator's take on banks' motivation

Rob Frohwein: Head of Kabbage.
Photo credit: Kabbage

Rob Frohwein, head of Kabbage, an online automated lending platform for small businesses, provides his thoughts on fintechs and banks working together and their motivations.

KPMG:
"Banks and fintechs, like Kabbage, are building alliances at a fairly steady pace, although there are suggestions that more banks ought to be engaged in fintech alliances and joint ventures. Is it a fair critique?"

Frohwein:
"Some of the criticism is fair, but if you really examine what's going on, there are a growing number of banks embracing these new opportunities. So, I'm encouraged about the future of our business and about the future of bank partnerships."

KPMG:
"What advice would you offer bank executives who are taking a wait-and-see posture on creating alliances with fintechs?"

Frohwein:
"One major challenge in banking is motivation. People are fundamentally motivated in every decision by two emotions: fear and desire. At some banks, there is a desire to create a strategy that embraces new ideas and technologies, but at others I see some fear about changing what they have. So, they simply put off the decision. And, I think, that is a mistake.

"If there is fear at the top level, it cascades through the organization. When that happens, there is little incentive inside the organization for people to stand up and say, 'Let's pursue something new.'

"But, when there is a sense of innovation at the top, then the opposite happens. People are energized; they embrace new ideas. That's when the chances to grow the business creatively start to improve."

KPMG:
"Would you agree that the idea of change often creates a high hurdle inside organizations?"

Frohwein:
"Think about Steve Jobs when he went back to Apple. At the time, Apple had a long list of products and he said: 'We're done with all of that.' He ripped off the bandage and focused on just a few products. That is what has to happen at banks. They need to refocus, and that will re-energize the bank."

"Many banks have a great brand, they have the customers, and they have incredible talent. Those people will react positively when the bank makes big, bold moves. It will have a tremendous ripple in the organization. The banks that we work with are innovative. They see the market changing, and, instead of resisting change, they embrace it."

KPMG:
"Are you concerned about negative impacts to your business if there is a roll back of banking regulation?"

Frohwein:
"A lot of people have asked me, 'If Dodd-Frank is repealed, will that hurt Kabbage?' I say, 'No, we think banks will continue to want to partner with us. We think those kinds of partnerships are mutually beneficial.' Beyond the regulatory challenges, there still are a very large number of banks stuck with inefficient, legacy IT systems. And, that's where we've been able to help. We think it's a big opportunity."

Closing thoughts

We find that when we see individuals and organizations struggle with strategy, it is often the result of them not having properly defined the challenges they face and not having collectively aligned those challenges with their goals.

Late in the 1990s, when Apple was close to bankruptcy and decided to rehire Steve Jobs as CEO after a 12-year absence, he said that "the cure for Apple is not cost-cutting. The cure for Apple is to innovate its way out of its current predicament."[11]

In the current industry environment, where the speed of digitization of operations is escalating daily, we expect that there will be a shakeout of weaker, less-focused organizations. Tomorrow's successful banks almost certainly will be characterized by those with a clear strategic vision, an ability to leverage fintech coopetition, and a resolve to weather the volatility that is certain to be over the horizon.

We expect banks will continue to play their traditional role as a foundation for the growth and strength of our economy. Banks are a conduit between savers with excess cash and business owners with ideas they want to develop. In these basic, but highly valued, roles in our economy, banks will serve everyone when they thoughtfully determine where they can best compete, deliver value, and capture profits.

Further, successful banking organizations will be characterized by having people who embrace change, prize their agility, and seek an innovative culture with a willingness to listen to—and test—new ideas.

Finally, these organizations will have a laser-like focus on serving commercial and retail customers, and they will institute processes that will continuously listen for signals of change.

Who we are

KPMG's Banking & Capital Markets practice

Our Banking & Capital Markets practice comprises more than 3,800 experienced professionals in the United States. Each day, we work to earn the highest level of confidence of our clients and other stakeholders by building and expanding business relationships, being highly visible in the markets we serve, and providing high-quality and relevant methodologies and insights—all in an effort to be the recognized market leader in providing audit, tax, and advisory services across the banking and capital markets industry.

[11] "Apple Confidential 2.0: The Definitive History of the World's Most Colorful Company," No Starch Press, 1999

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