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Top Six Banking Trends and Their Impact on Financial Institutions

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Hyland™

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Executive Summary

These are six trends that will define financial services over the coming years. The retail banking environment is evolving, driven by changes in consumer preferences and emerging technologies. One throughline touches on each of the six trends, and that is artificial intelligence (AI), which is arguably the most transformative technology since the adding machine:

- **Adoption of generative AI (GenAI):** GenAI enables streamlined operations, personalized services, and data-driven decisions. To prepare, financial institutions (FIs) must develop an AI strategy, invest in infrastructure and talent, prioritize data governance, and focus on efficiency gains.
- **Personalized digital interactions:** By harnessing AI and data analytics, banks can deliver tailored experiences that boost sales, engagement, and loyalty. Banks must invest in tech, safeguard data, and cultivate a customer-centric mindset to capitalize.
- **Pricing optimizing strategies:** These are powerful levers for banks to boost profitability and competitiveness. By leveraging AI and data analytics, banks can develop sophisticated, targeted pricing that reflects true value and meets customer needs.
- **Cloud-first approaches:** Cloud adoption is transforming banking, enabling agility, innovation, and cost savings. To capitalize on this shift, banks must develop a clear cloud strategy, identify suitable applications for migration, partner with cloud-native solution providers, and establish robust governance and security controls.
- **Recalibrating regulatory compliance:** This is crucial for banks to navigate the evolving regulatory landscape. While it requires investment in new systems and processes, it also presents opportunities for innovation. Banks must proactively adapt to stay compliant and competitive in an increasingly complex regulatory environment.
- **Modernizing technology cores:** Modernizing legacy tech stacks is essential for banks to deliver personalized experiences and stay competitive. While it requires significant investment and planning, embracing AI, cloud, and data analytics can streamline processes, enhance security, and enable innovation.

Adoption of GenAI

AI is here. For better or worse, it remains the most significant opportunity for a return on investment in our time. The following will provide some context and direction and will contain only a reasonable number of Skynet references.¹

Why Is the Trend Important to FIs?

The growing adoption of GenAI is a game-changer for FIs. As AI technologies advance, FIs that embrace GenAI will be better positioned to streamline operations, improve customer experiences, and gain a competitive edge in the market. GenAI has the potential to revolutionize various aspects of banking, from customer service and fraud detection to risk management and investment strategies. By leveraging the power of GenAI, FIs can automate complex processes, analyze vast amounts of data in real time, and make more informed decisions based on predictive insights.

How Will It Impact FIs?

AI has already been incorporated into many back-office processes, primarily in the form of robotic process automation (RPA). The adoption of GenAI will have far-reaching impacts on FIs. First, it will enable FIs to significantly improve operational efficiency through intelligent document management and flexible processes, reduce human error, and optimize resource allocation. Second, GenAI will enhance the accuracy and speed of decision-making processes, allowing FIs to respond more quickly to market changes and customer needs. GenAI will also enable FIs to develop more personalized and innovative products and services, improving customer experiences and prompting them to say, "I'll be back."

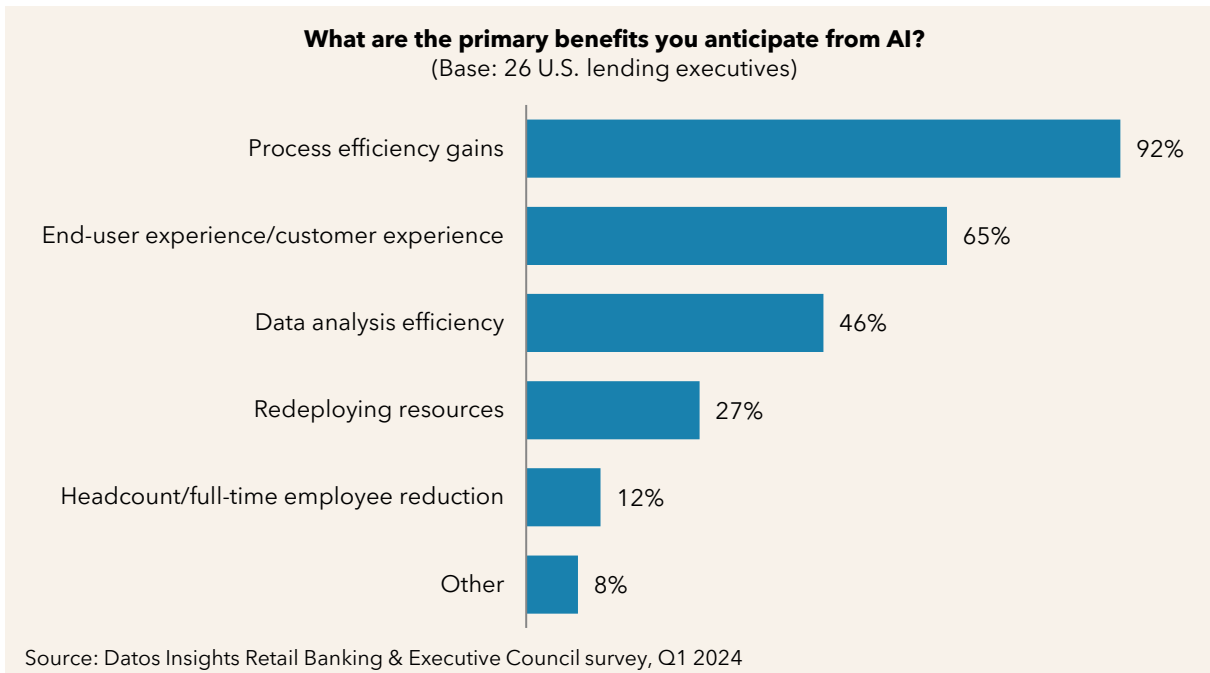
What Should FIs Do Now to Prepare?

To prepare for the adoption of GenAI, FIs should develop a clear AI strategy that aligns with their business goals and customer needs. They should invest in building the necessary infrastructure and talent to support GenAI implementation, including upgrading IT systems and upskilling existing employees. FIs should prioritize data governance and privacy, ensuring they have robust systems to protect sensitive customer data. Having the right partnerships in place is imperative for realizing the full benefit of AI as a back-office tool.

¹ Skynet is a fictional artificial neural network-based conscious group mind and artificial general superintelligence system that serves as the antagonistic force of the "Terminator" franchise.

In a recent Datos Insights survey, retail banking executives were asked what primary benefits AI would anticipate (Figure 1). Efficiency gains were the most frequently selected use case by the retail banking executives who participated in the research. With AI already having a foothold in many back-office processes via RPA, it may have been the first use case to come to mind and the strongest need.

Figure 1: Primary Anticipated Benefits of AI



Personalized Digital Interactions

Hyper-personalization has become a buzzword in banking strategy circles. That said, all FIs must find ways to differentiate themselves from the competition. The best way to do this is to provide a personalized and unique banking experience. In a 2022 survey, J.D. Power found that 78% of respondents would continue using their bank if they received personalized support, but just 44% of banks are actually delivering it.²

Why Is the Trend Important to FIs?

Personalized digital interactions are becoming increasingly important for FIs as customers expect tailored experiences that cater to their unique needs and preferences. By leveraging AI technologies to personalize digital interactions, FIs can drive sales, improve customer engagement, and build stronger customer relationships. Personalization allows FIs to offer relevant products and services at the right time, increasing the likelihood of conversion and customer loyalty.

How Will It Impact FIs?

The impact of personalized digital interactions on FIs will be significant. Firstly, it will enable FIs to increase customer acquisition and retention by offering tailored experiences that meet individual needs and preferences. Secondly, personalized digital interactions will improve customer satisfaction and loyalty, as customers feel valued and understood by their FIs. Additionally, personalization can help FIs optimize marketing spend by targeting the right customers with the right messages at the right time, reducing waste, and improving return on investment.

What Should FIs Do Now to Prepare?

To prepare for the trend of personalized digital interactions, FIs should invest in AI technologies and data analytics capabilities that enable them to collect, analyze, and act on customer data in real time. They should develop a clear personalization strategy that defines the key customer segments, channels, and touchpoints where personalization can have the most impact. FIs should prioritize data privacy and security, ensuring they have the necessary safeguards to protect customer data. Finally, they should foster a customer-centric culture, encouraging employees to continuously test and refine personalization approaches based on customer feedback and data insights.

² "U.S. Retail Banks Struggle to Differentiate, Deliver Meaningful Customer Experience as Economy Sours, J.D. Power Finds," J.D. Power, April 7, 2022, accessed June 5, 2024, <https://www.jdpower.com/business/press-releases/2022-us-retail-banking-satisfaction-study>.

Optimizing Pricing Strategies

The idea of turning the pricing function into a competitive and customer experience advantage has not received much airplay. Consumer banking regulation does limit the options, but optimizing pricing can increase yields, manage the cost of funding, gain share, limit risk, and provide customers with personalized pricing. The hurdle has been the inability to consume, manage, and process a large amount of data to manage it effectively. This is one more problem AI and cloud computing can solve.

Why Is the Trend Important to FIs?

Optimizing pricing strategies is becoming increasingly important for FIs as they seek to maximize profitability and compete in a dynamic market environment. By leveraging AI technologies to analyze vast amounts of data on customer behavior, market trends, and competitor actions, FIs can develop more sophisticated and targeted pricing strategies that reflect the true value of their products and services.

How Will It Impact FIs?

Optimizing pricing strategies will significantly impact FIs. Firstly, it will enable FIs to improve their profitability by setting prices that reflect the true value of their products and services and maximize revenue generation. Secondly, optimizing pricing strategies will enable FIs to understand their customers better and develop more targeted offerings that meet their specific needs and preferences. Additionally, optimizing pricing strategies can help FIs reduce costs and improve operational efficiency by automating pricing decisions and eliminating manual errors and inconsistencies.

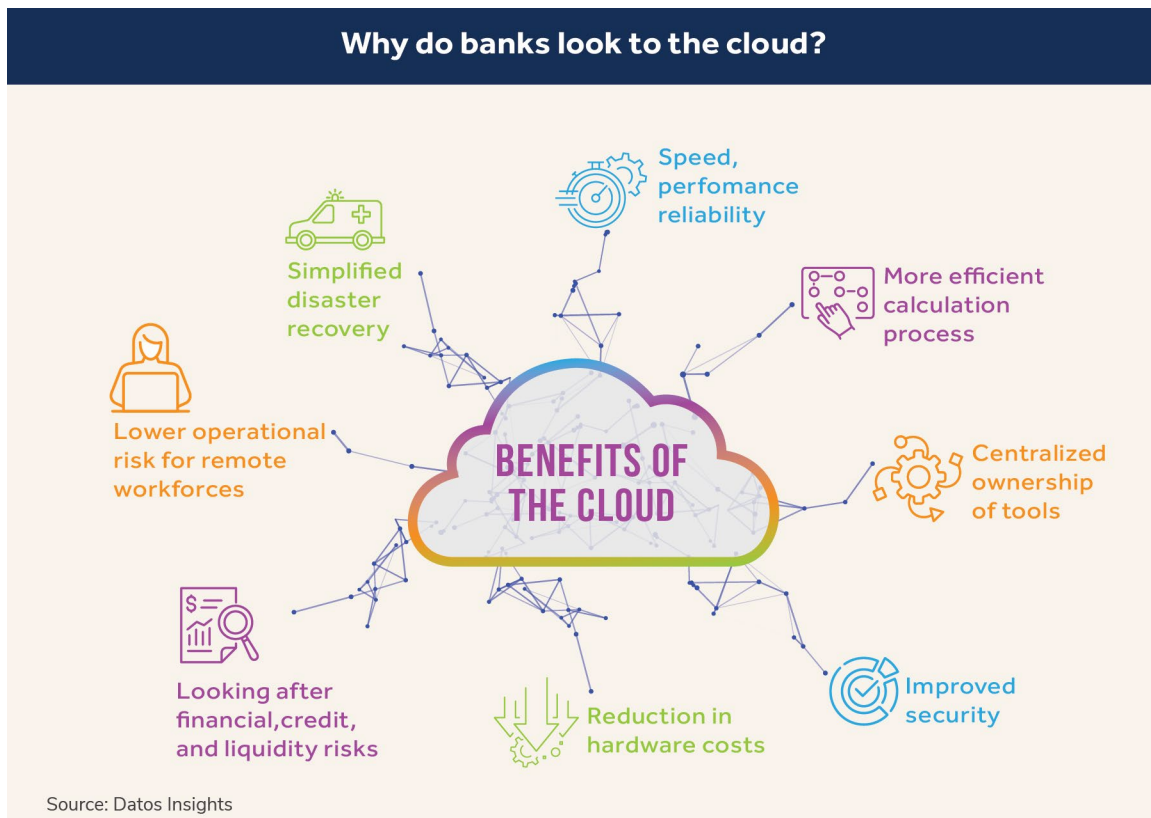
What Should FIs Do Now to Prepare?

FIs should invest in AI technologies and data analytics capabilities that enable them to collect, analyze, and act on vast amounts of structured and unstructured data from various sources to prepare for the trend of optimizing pricing strategies. They should develop a clear pricing strategy that aligns with their overall business objectives and customer segmentation approach. FIs should prioritize transparency and fairness in their pricing practices, ensuring compliance with regulatory requirements and ethical standards.

Cloud-First Approaches

A few years ago, cloud computing was taboo in financial services, but now it's on almost every FI's roadmap. Banks are increasingly turning to cloud computing for its numerous benefits (Figure 2). Cloud adoption is transforming the banking industry by allowing vastly simplified disaster recovery and improved security, reducing hardware costs and enabling more efficient processes.

Figure 2: Benefits of the Cloud



Why Is the Trend Important to FIs?

Cloud-first approaches are becoming increasingly important for FIs as they seek to modernize their IT infrastructure and enable greater agility, scalability, and innovation. By leveraging cloud technologies to store, process, and analyze data, FIs can reduce their reliance on legacy systems and hardware and enable faster and more efficient development and deployment of new products and services. After doing so, document retention, recall, and management become an entirely different function and a source of significant cost savings and improved customer experience.

How Will It Impact FIs?

The impact of cloud-first approaches on FIs will be significant. Firstly, it will enable FIs to accelerate their digital transformation and innovation efforts by providing them with the flexibility and agility to quickly develop and deploy new products and services in response to changing customer needs and market conditions. Secondly, cloud-first approaches will enable FIs to improve their data management, analytics, and AI capabilities by providing them with access to vast amounts of real-time data from various sources and allowing them to apply advanced analytics and machine learning techniques to generate insights and predictions. Additionally, cloud-first approaches can help FIs enhance their security and compliance posture by leveraging the advanced security features and certifications cloud service providers provide.

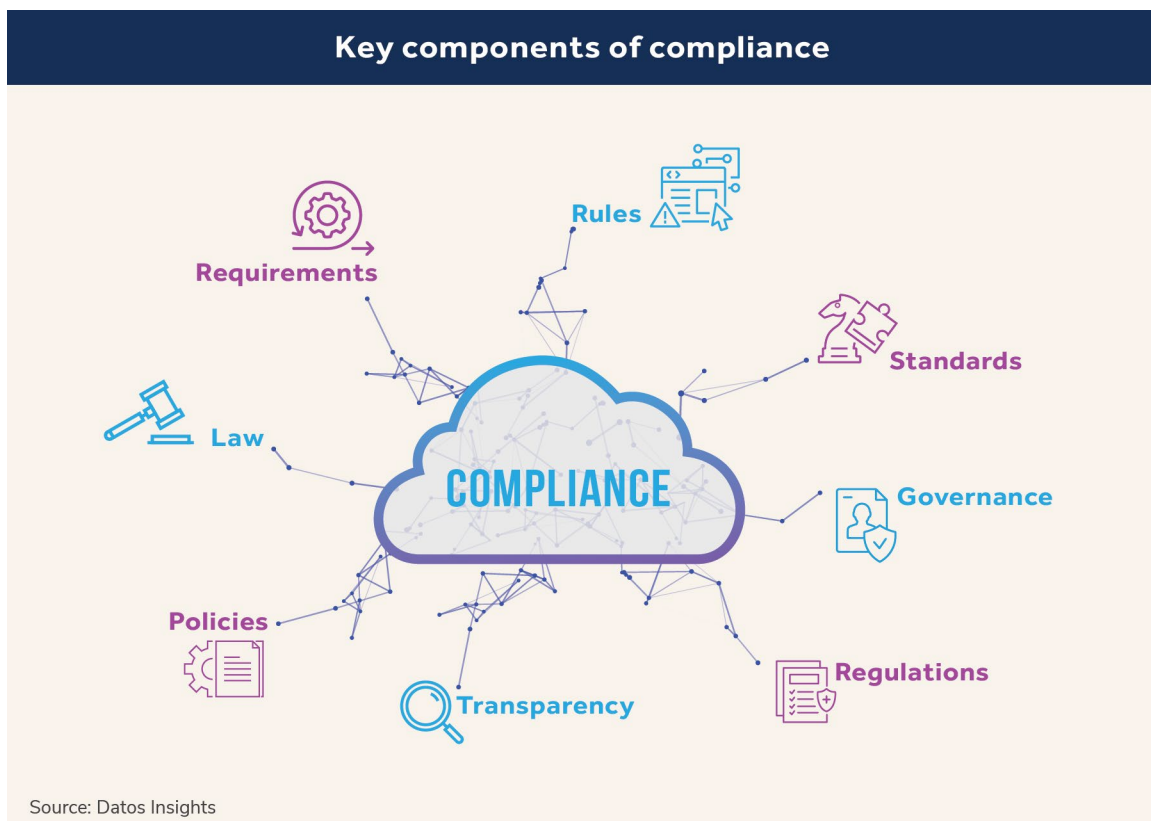
What Should FIs Do Now to Prepare?

FIs should develop a clear cloud strategy that aligns with their overall business objectives and IT architecture to prepare for the trend of cloud-first approaches. They should assess their current IT infrastructure and identify the applications and workloads that are most suitable for cloud migration. FIs should look for point solution partners with cloud-native solutions to leverage the platform more fully. The obvious candidates for migration would be data management, electronic document management (EDM), and CIF (customer information file). Additionally, they should establish robust governance frameworks and security controls to ensure their cloud deployments comply with regulatory requirements and industry standards.

Recalibrating Regulatory Compliance

FIs face escalating compliance risks due to growing regulatory scrutiny and the need for robust risk management frameworks. Recalibrating compliance functions involves adopting new models with core principles such as actively managing risks, emphasizing transparency, and integrating compliance with overall risk management governance. These practices help banks stay compliant with evolving regulations and enhance their operational efficiency. Deploying regulatory compliance technology (RegTech) with the right partner is critical to achieving these goals (Figure 3).

Figure 3: Regulatory Compliance



Why Is the Trend Important to FIs?

Recalibrating regulatory compliance is becoming increasingly important for FIs as they seek to navigate a complex and rapidly changing regulatory landscape. As new technologies and business models emerge, regulators face pressure to adapt their rules

and guidelines to ensure they remain relevant and effective in protecting consumers and promoting financial stability.

How Will It Impact FIs?

Recalibrating regulatory compliance will require FIs to invest in new compliance and risk management systems, regulation technology, and processes to ensure they meet policy requirements. It may also introduce new risks and uncertainties as FIs navigate a changing regulatory environment and adapt to new rules and guidelines.

What Should FIs Do Now to Prepare?

To prepare for the trend of recalibrating regulatory compliance, FIs should closely monitor regulatory developments and engage proactively with regulators and industry groups to provide input and feedback on proposed changes. They should also invest in strengthening their compliance and risk management capabilities, including hiring specialized talent and implementing specialized technologies such as AI-driven RegTech and machine learning to automate compliance processes and detect potential violations. Investments in EDM technology that can manage the increasingly complex regulatory framework around retail banking. Finally, FIs should foster a culture of compliance and ethics, encouraging employees to prioritize regulatory compliance and customer protection in all their business activities.

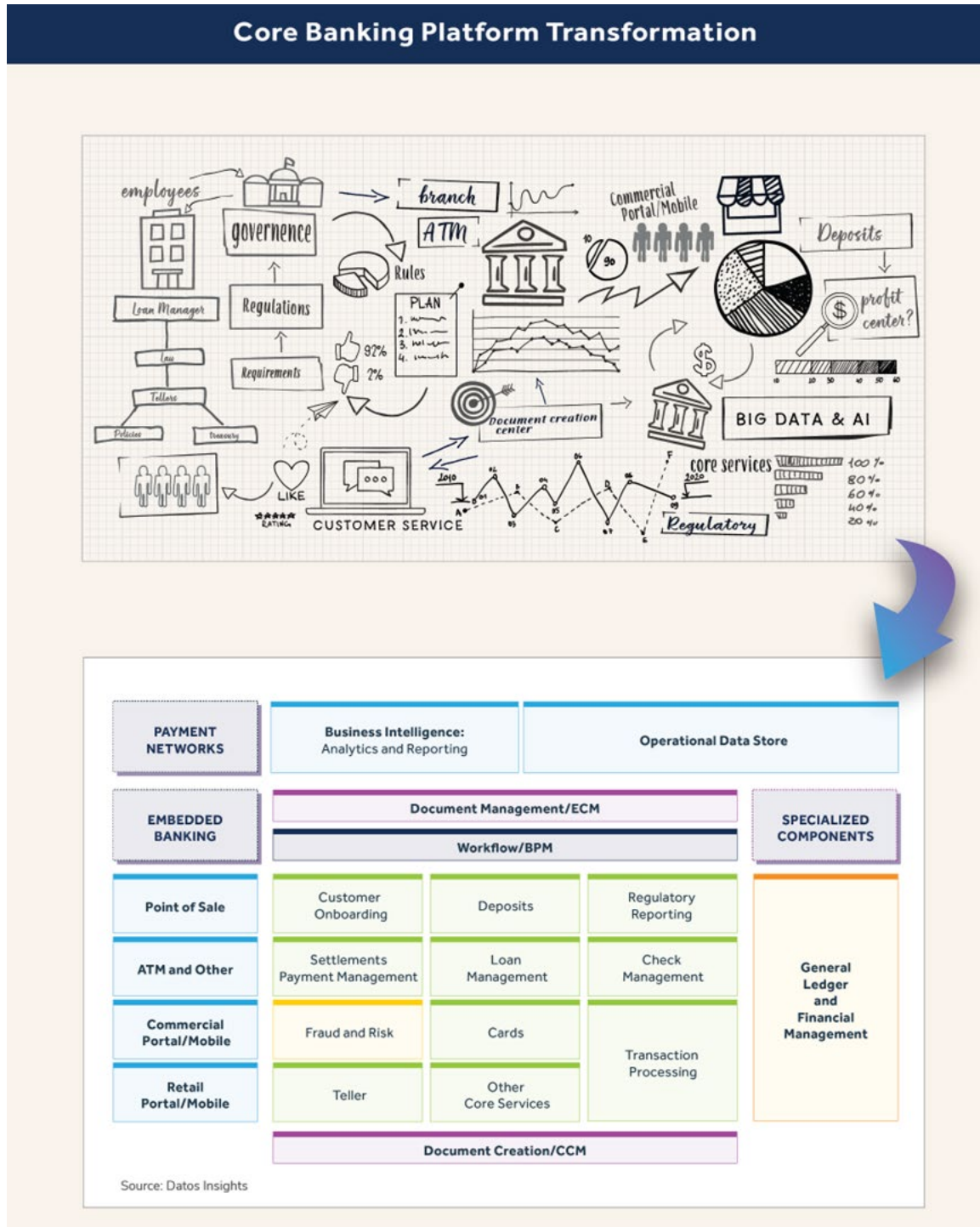
Modernizing Technology Cores

Consumers are increasingly expecting a more personalized experience. They interact with brands every day that customize their interaction, e.g., Starbucks, Amazon, and Apple. FIs have the information to create superior personalized interactions (digitally and in-person). Still, they have had difficulty accessing, aggregating, and applying the data to hyper-personalize their customer's experience. The first step to improving customer experience is addressing issues in the legacy tech stack.

Why Is the Trend Important to FIs?

Modernizing technology cores is becoming increasingly important for FIs as they seek to replace legacy systems with more flexible, scalable, and secure platforms that can support their digital transformation initiatives. As FIs face pressure to innovate and adapt to changing customer needs and expectations, the limitations of their aging technology infrastructure are becoming more apparent, hindering their ability to develop and deploy new products and services quickly and efficiently (Figure 4).

Figure 4: Banking Core Modernization, Before and After



How Will It Impact FIs?

The impact of modernizing technology cores on FIs will be significant. Firstly, it will require FIs to make substantial investments in new technologies and platforms, including cloud

computing, microservices architecture, and API-based integration. Secondly, modernizing technology cores will enable FIs to improve operational efficiency and reduce costs by automating manual processes and eliminating the need for expensive maintenance and support of legacy systems. Additionally, it will allow FIs to enhance their cybersecurity posture and protect against emerging threats by making it simpler to implement more advanced security features and protocols.

What Should FIs Do Now to Prepare?

It is crucial to start with a comprehensive assessment of the current system to identify limitations and areas for improvement. FIs should set clear objectives, such as enhancing customer experience, security, and efficiency. All modernization options, including complete system replacement, component-based replacement, or augmenting existing systems (sidecar) should be in the consideration set. A current product and feature roadmap should be incorporated into the decision-making process.

Embracing new technologies like AI, data analytics, cloud computing, and biometrics can streamline processes and improve customer experiences. Prioritizing cybersecurity is essential to protect sensitive data and comply with regulations. Cloud adoption offers simplified maintenance and scalability benefits, but data security and governance concerns must be addressed.

Collaborating with stakeholders, including IT teams, vendors, and consultants, ensures a smooth modernization process. A robust data migration strategy minimizes disruptions and maintains data integrity. Regular communication and employee training are vital for a successful transition. Modernizing legacy core systems is a significant undertaking that requires careful planning and resources.

Key Takeaways

- **AI integration:** Adopt GenAI to streamline operations, improve services, and secure a competitive edge.
- **Personalized engagement:** Utilize AI for tailored digital interactions that enhance sales, loyalty, and engagement.
- **Pricing precision:** AI-driven pricing strategies can optimize profitability and offer customer-centric pricing solutions.
- **Cloud velocity:** Embrace cloud-first strategies for agility, innovation, and cost efficiency in banking operations.
- **Regulatory agility:** Navigate evolving regulations by investing in compliance for innovation and competitive advantage.
- **Tech innovation:** Modernize core tech to enhance security and operational efficiency and deliver personalized customer experiences.

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