

In Praise of Incrementalism by Charles Wendel

I just read an excellent but, unfortunately, naïve monograph by an accounting firm most recently best known for its Academy Awards snafu. Its focus centers on the need for traditional lenders to go through a significant transformation, if they are to succeed in digital lending.

Theoretically, their recommendations for an extensive, multi-year effort (aided by them, of course) may make sense but this kind of change simply will not occur at most banks. Instead, banks have shown they are more willing and able to take multiple small steps rather than embark on a major overhaul. That may not be the right textbook approach, but for most banks it is reality and, therefore, vendors and consultants need to accept incrementalism as a way of life, and managers need to make it work for their bank.

The monograph states: “Lenders who don’t first make the necessary changes to their underlying culture, people, processes, and technology will not find digital leadership sustainable, as competitors quickly leapfrog the capabilities that are considered ‘state of the art’ today.” Appropriately, the above lays out the many different areas that require change for long-term success but are so challenging to modify.

The writers go on: “Lenders must take a strategic, holistic approach to maximize the benefits of investment.” Few banks want or can pursue “holistic” changes. In fact, at many banks, suggesting this type of revolution will cause bankers to throw up their hands and simply avoid the topic. I have heard from support staff at more than one bank that senior bankers simply will not engage in this type of conversation. And why should they? For many executives, the downside of failure in this area is personally more threatening than any uncertain down-the-road success. And, too often, those recommending big changes both have little at risk personally and lack experience in the byzantine inner workings of most banks. Internal digital bankers and external consultants present documents demanding “digital transformation” while top bankers respond thinking not opportunity but PITA.

Oftentimes, even those banks that think they are going down the transformation path are deluding themselves. Instead, some resemble high tech versions of the *Emperor’s New Clothes*, whereby, bankers proclaim improvements that are marginal rather than major. Those few banks that are traveling down this path successfully know it is a long and winding road with the occasional dead end.

Chris Skinner is a UK-based expert on things digital who highlights one practical obstacle to digital change. In a recent blog he discussed the CFO of the future. The title of the blog entry, “Your CFO Is an Algorithm” suggests his perspective: “So, I know folks will say this is massively over simplifying the complexity of the Treasury, Accounts and CFO role, but is it? If I could put all of my bills of lading, letters of credit, purchase orders and receivables in a shared ledger connected through APIs to intelligent algorithms that can reconcile and recognise everything, is it really so unimaginable that

my CFO becomes a DFO?” What’s a DFO? “The DFO is an algorithm presented as an API that automates everything.” In other words technology could replace much of a CFO’s role.

However, Skinner goes on to discuss the practical barriers to exploring this approach and goes back to Michael Hammer’s 1990 writings on reengineering, probably written before some of the accounting team writing the digital essay quoted above were born, although many of the concepts they promote are similar. He writes:

“We can reduce financial departments to an API and an algorithm. The CFO is an algorithm presented as an API. The only issue with this is that businesses cannot imagine such an operation. This is, in part, a two-fold dilemma. The first part of the dilemma is to imagine the complete Treasury operation moved into a digital ledger. It can be done, but the idea of not having someone accountable for the processes of billings and receivables, payables and invoicing, just seems wrong. That is an industrial age mentality – we need humans to manage these financial processes – but that mentality is strong... Any CFO, when challenged, will justify having so many people by the complexity of the tasks they do. They are necessary.

The reality is that they are not, but the CFO’s ego will not allow the CEO and executive leadership team to undermine their empire. As a CFO, it has taken them a long time to get there. Now they are there, they have an empire. The empire is sizable and reinforces the stature and power of this role. To even challenge that role’s importance and beg the question: *do you really need so many underlings?* will beg defiance. So, beware when you ask the CFO to automate everything and move it along to a shared ledger that, when you challenge their empire, sometimes the empire strikes back.” I can remember a corporate transformation project from many years ago at a huge financial services company at which the IT exec simply refused to cooperate with the high cost consulting team, and he suffered no consequences from his seniors.

Skinner’s CFO comments apply as well to IT, Product, Compliance, lines of business, in effect any entrenched and established area within a bank. Few bank CEOs have the knowledge, temperament, or time to challenge these silos even in the interest of an improved customer experience and/or a better performing bank. Caution rather than speed and innovation guides many executives. We may wish that the bank reality was different, but wishes are not reality.

Of course, exceptions exist and some banks have been able to embrace the digital frontier and transform themselves. In particular smaller banks with new leadership and banks requiring a turnaround have the flexibility and the need to change themselves.

Conversely, many (but not all) established and successful banks have a long history that, in many cases, may be more of a weight than a benefit when trying to drive change.

Next time we will focus on some recent approaches for introducing digital change that may have set the foundation for a culture shift that can result in the type of holistic change that remains an illusive goal for most banks.