

The Deep State is Alive and Well at Most Banks

by Charles Wendel

Many banks are being run or at a minimum highly influenced by the entrenched Deep States operating within them. The Deep State group in banks is every bit as insidious as anything that might be occurring in the government. Ultimately, these groups threaten a bank's existence.

The increasing speed of change, customer expectations, and new competitors require bank management to recognize, challenge, and break up the internal deep state "organization" that may be determining their bank's fate.

The best essay I have read defining the Deep State was published in early 2014 (Mike Lofgren: Anatomy of the <http://bit.ly/2NAxfLQ> via @BillMoyers). In a bank's case, the deep state exists in an entrenched internal bureaucracy, cement-like traditions, and rules that can constrain a bank's flexibility and innovation... becoming an innovation-killing machine. Think about your bank as you read Lofgren's comments:

"There is the visible government situated around the Mall in Washington, and then there is another, more shadowy, more indefinable government that is not explained in Civics 101 or observable to tourists at the White House or the Capitol. The former is traditional Washington partisan politics: the tip of the iceberg that a public watching C-SPAN sees daily... The subsurface part of the iceberg I shall call the Deep State, which operates according to its own compass heading regardless of who is formally in power. "

Lofgren goes on to discuss how and why the Deep State operates. Consider your bank's organization and the internal bureaucracies and "hidden" influencers who impact your bank's ability to compete:

"Yes, there is another government concealed behind the one that is visible at either end of Pennsylvania Avenue... connected to, but only intermittently controlled by, the visible state whose leaders we choose. My analysis of this phenomenon is *not* an exposé of a secret, conspiratorial cabal; the state within a state is hiding mostly in plain sight, and its operators mainly act in the light of day... The institution is not so much sinister (although it has highly sinister aspects) as it is relentlessly well entrenched. Far from being invincible... it is only the Deep State's protectiveness towards its higher-ranking personnel that allows them to escape the consequences of their frequent ineptitude."

A bank's Deep State is also hidden in plain sight and with many of the internal bureaucrats continuing their activities, no matter changes in a bank's leadership. Similarly, a bank's Deep State members are neither a cabal nor evil; typically, they think they are doing the right thing for the bank. But, whether intend to or not they slow decision making, often encourage mediocrity, reward "going along" and, most important, puts themselves and their own interests first, rather than focusing on the customer experience.

Examples exist among line and staff personnel:

- The staff person who controls the numbers and related analytics, keeping information close to the vest rather than making it transparent and easily accessible.
- Some Compliance and Legal personnel and who lack a business sense and operate with a belt and suspenders approach to regulatory requirements.
- Line leaders who accept weak staff because of internal paternalism, sometimes moving a poor employee to another bank area from his own rather than exiting him
- Line personnel who taken the easy path. We know one CEO who was under Board pressure to switch Core providers. He did, moving his bank from one big name firm to another, never considering any new entrants or rethinking the fundamental requirements for a Core, given the rapidly changing IT capabilities and competitors. He did what the Board wanted, he survived for 5+ years, and then retired, I am sure feeling good about himself.
- Line staff that buckle under. More than once I have heard a business “leader” say “I don’t agree with them, but we are following [Insert name of big consulting firm]’s recommendations.” Basically, top management paid for the study, so other will go along rather than take the risk of offering a contrary view.

How can you end or at least curtail your bank’s Deep State? The first step required is to admit this situation exists at your bank. Banks should look at their operating expense ratios and decision-making processes as indications of this problem. By the way, we have seen mini-Deep States existing in community banks and a willingness to identify and eliminate them in Top 50 banks. Mindset and culture pose more of an obstacle to breaking up your Deep State than does asset size.

External forces will play an increasingly critical role in ending the Bank Deep State. Customers want flexibility and expect transparency and value from their banks. Competitors across the banking landscape are working to blow up traditional operating models. Their focus on providing a great customer experience and their management styles do not allow an internal Deep State to grow within their companies...at least not so far. They also cannot afford the cost of a Deep State bureaucracy, a barnacle-like weigh that many banks just accept.

Longren’s essay ends with some hope that the governmental Deep State will be exposed and dismantled. Hope exists for banks as well, but management has to act before customers and nonbank competitors marginalize them.