Twenty Years
by Charles B. Wendel

SELF-INDUGENCE ALERT! February marks the 20-year anniversary for my firm, FIC. I might have ignored it, but for the many and well appreciated Linked-In prompted congratulations I have been receiving. It is a BIG anniversary that results in some reflection and, I hope, the opportunity to summarize some observations and lessons learned. As additional background, prior to FIC I was a consultant with larger firms, including McKinsey, as well as a commercial banker for about seven years with Citibank and others, when banking was still fun.

Lessons learned fall into two categories: business and personal. Business, first.

Nothing has changed! Twenty years on, I am often amazed by how little has changed at many banks:

- *Small business.* Small business continues to fight for management commitment and the long-term investment it both requires and merits, limiting growth. Management usually says the right things but does not back it up.

- *Compensation.* Compensation policies remain too salary-based and fail to differentiate sufficiently between top tier and mid-level employees, creating morale and performance issues and making it difficult to retain the best people.

- *Personnel.* Management hesitates to exit mediocre employees, despite ample evidence that an employee contributes little. In this week's *Financial Times*, Lucy Kellaway writes of the clear value of getting rid of bad employees as quickly as possible. And, last week, in a speech in Columbus, Ohio, Jaime Dimon said, "Fire the a—holes…They will destroy your company." Banks don't do enough of that.

- *No urgency.* Little sense of urgency to make decisions and execute quickly exists. Whether due to compliance pressures or self-satisfaction, banks seem to take longer than ever to make decisions, many of which, from an outsider's perspective, appear to be no-brainers.

- *Limited cross sell.* While cross-sell activities provide no guarantee of success, they are about as close to a secret sauce as exists in banking. Usually, the more products sold, the more revenues and the higher the return. But, few banks focus rigorously on this critical initiative, allowing internal hurdles and egos to get in the way of providing customer value and making more dollars. The lack of consistent focus here totally amazes me.

- *Insufficient leadership.* Too many employees are holding on. Baby boomers are slowly disappearing, but at many banks they are continuing to maintain their jobs, often by the tips of their fingers. They keep employed but operate as defensive hedgehogs rather than leaders. Too many senior bankers say, "I have a year to go," or "Five years left" as if they are occupants of Sing Sing rather than corner offices. The first time I heard such a comment from a bank president, my jaw dropped, but no more. This results in a lack of innovation (other than innovation tied to technology) and creativity at many banks.

- *Hope as a strategy.* Even after years of low interest rates, some banks continue to base their future forecasts (and even acquisition expectations) on an interest rate spike. This seems fraught with peril, particularly given the stutter-step nature of this recovery.

Everything has changed! Dramatic changes are occurring across financial services, but many banks are failing to develop approaches for addressing these changes. Rather than directing the changes, banks are in a reactive mode.

- *Bye Bye to Baby Boomers*. The consumer customer base is shifting to Gens X and Y with less reliance on Baby Boomers. Bank assets grew along with Baby Boomer growth. How will they grow as the Boomers disappear and become less valuable to banks?

- *Hard to read customers*. Gen X and Gen Y remain a mystery to many banks. Surveys try to capture their characteristics, but they are inherently less stable and predictable as a segment than Boomers. (Most also have fewer dollars for banks to capture.) But, most banks are run by Boomers who to some degree "don't get" what is happening around them.

- *Alternative players have changed the business*. Big name players like Google, Apple, and PayPal are not going away. In fact, they will increase their focus on bank-like activities, both in payments and lending. Private equity firms see a substantial opportunity to pick away at the banking franchise and are doing so in the small business and, increasingly, the middle market spaces. Too many banks are ignoring these initiatives at their own peril. On the lending side, these usually well-financed players offer loan platforms for banks to take advantage of and new revenue streams, including the chance to capture new customers that provide cross-sell opportunities.

- *Channels are changing*. Yes, banks are slowly closing branches, with an emphasis on the word slowly. In some cases bankers are anxiously waiting for the 200-400 basis point rise in rates to make their branches profitable once again. Good luck with that approach. It may be quite a while before rates go that high and, in the meantime, transaction activity at branches is decreasing at the rate of 8-15% a year.

- *Regulators have gone mad…and bankers have allowed them to*. OK, I am exaggerating. However, senior banks at very well performing banks make comments like, “The regulators all want us to be the same,” and “We really are paranoid about the regulators, and “They are calling the shots at our bank.” The industry brought this upon themselves with too tricky concepts like bad CRE lending, ”free” checking (really a scam that harmed those least able to afford being scammed), and abusive mortgage activities. However, a relative handful of banks were involved in those activities, and they have either paid with their corporate lives and/or stiff fines. Time to move on.

  Too many bankers are using the regulators to excuse their own lack of action. What a convenient group to blame. In recent years, only a handful of bankers have publically pushed back while thousands of other silently acquiesce to regulatory demands, even if they are harmful without being helpful. Just last week while Elizabeth Warren stated, “We would be very skeptical of regulatory relief bills that are promoted as helping small banks.” In contrast, also last week, a Harvard White Paper cites community banks’ “declining market share… and the disproportionate losses being realized by particularly small community banks.” The industry needs to do a better job of representing itself; the good news is that it has a strong case to make.

The changes all seem to involve things that are happening to the industry rather than proactive steps that they are taking to define their future, not a good thing. For most players the future holds increased revenue pressure, likely lower margins, continued rises in operating and regulatory costs, and little likelihood the return to a 15%+ ROE for most banks.

Bluntly, this seems to be a good time for banks to evaluate themselves, their future options, and seriously consider sale. Currently, loan portfolios are strong, banks are generating moderate growth, and a substantial number of buyers exist. Those buyers may see value in cost consolidation, additional sales to current customers, and/or the impact of the long-predicted rate rise. Being an early seller while the acquisition enthusiasm remains high should be given substantial consideration now. Waiting to respond reactively to an acquisition offer rather than planning a sale strategy will likely cost dollars and time. Boards should be all over this issue.

Personal. Now for the most self-indulgent part, a personal reflection. During 2014, three clients, one current and two former, died. Two were younger than me, and one of them was for sure in demonstrably better shape than me. Life is short yet we fool ourselves into believing that it is not, a big mistake.