FINANCIAL INSTITUTION & FINTECH RELATIONSHIPS

FROM BOTH SIDES OF THE TABLE

CORNERSTONE ADVISORS

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CAUTIOUS OPTIMISM

Like peanut butter and chocolate, financial institutions and fintechs find themselves poised for partnership and ready to make each other a lot of money. But real progress requires more than a sugar high in a flashy wrapper. Each side has legitimate reasons to remain wary of the other — and optimal partnerships won't happen without the right recipe and hard work.

While fintechs and FIs increasingly want to work at the same table together, it will be more and more important that they get beyond the dreamy partnership language and recognize that they're on different sides of that table. That's because they have different needs and different areas of dissatisfaction with the relationship.

"It's not that all the fintechs are out to get the financial institutions or that the financial institutions are incompetent when it comes to using fintech products," says Steve Williams, president and founder of Cornerstone Advisors. "The truth is somewhere in the middle."

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To be sure, the $17 trillion banking industry rakes in $250 billion in yearly profits and maintains roughly $2 trillion in capital — along with a large and loyal customer base. But heightened competition makes bank and credit union teams heedful of the endless challenges that ever-evolving technology requires. Further, the sheer number of fintech vendors is overwhelming, while in-house, do-it-yourself technology can result in unending headaches and disproportionate risk. And, ultimately, the pressure to reduce spending is relentless.

Fintechs, meanwhile, typically operate on thin or underwater startup margins and crave more customers. They struggle to justify R&D without return-on-investment certainty — yet innovation is and always will be their lifeblood. The fintechs are painfully aware that, although financial institutions hold the purse strings, they often don't know what they want. And there's always a fintech startup with the latest wrinkle ready to steal away clients.

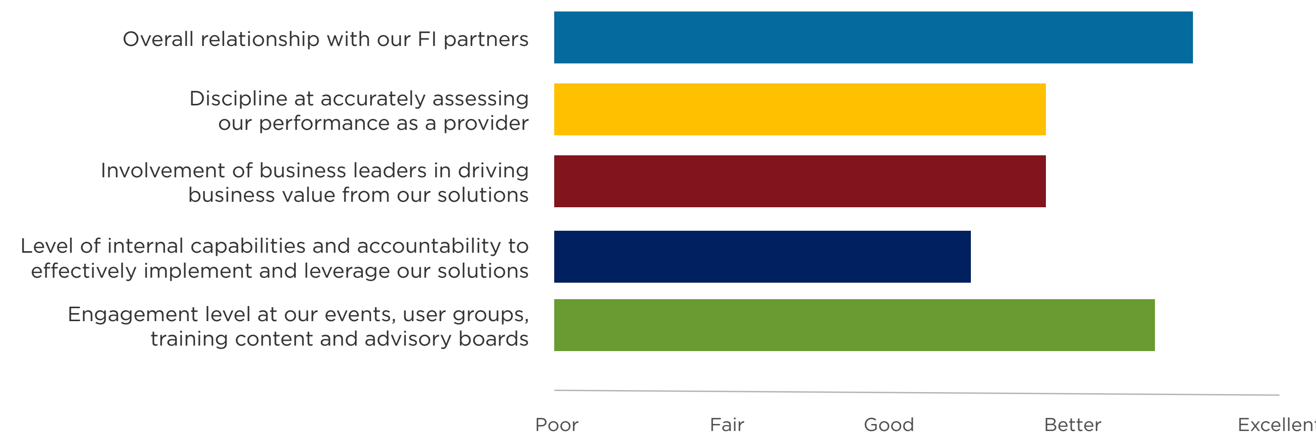
SURVEY SAYS

In reality, there will be far fewer banks and credit unions in 10 years — and those that survive will become future-ready sooner rather than later. Increasingly, that means drawing up agreements with fintechs as full-fledged partners, rather than seeing them as off-the-shelf vendors or competitors honing-in on the traditional turf of financial institutions.

A recent survey by Cornerstone Advisors finds that financial institutions and fintechs are reasonably satisfied with their overall relationships with one another. But deeper digging reveals that both sides are not enamored with important aspects of those relationships.

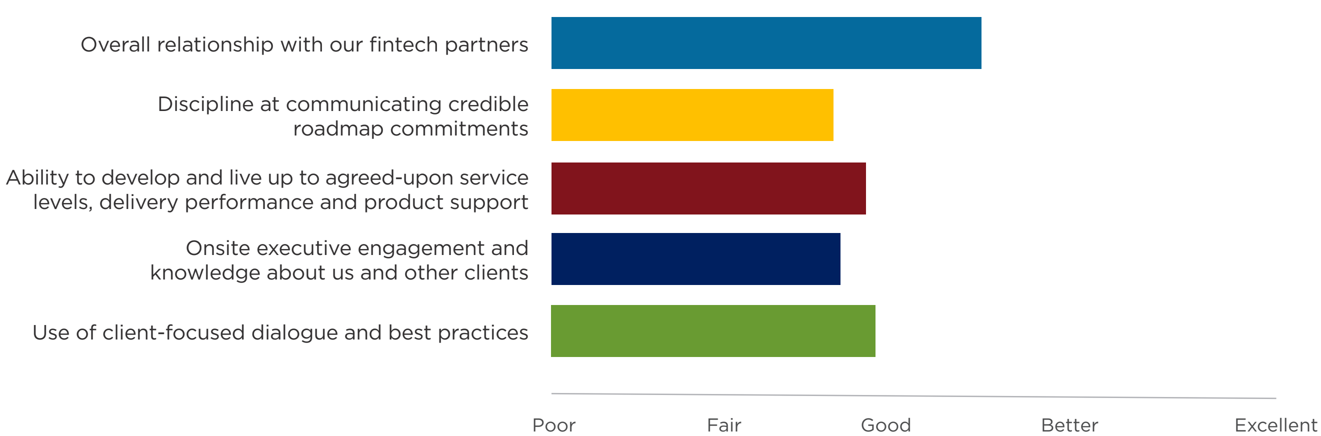
Fintechs lament a lack of cogent performance management on the part of their financial institution customers. They often see bank and credit union business leaders as disengaged from the collaborative process. They frequently find FIs falling short regarding line-of-business justifications for smooth, vested implementation of technology solutions. And, fintechs would like not only more involvement with FI events, user groups, training and advisory boards, but also a greater level of customer feedback from these events.

Survey: Fintech Vendor Responses About Their FI Partners (Averages)



Financial institutions, by contrast, yearn for credible roadmap commitments, better product support, more fintech executive involvement with their institutions and more coherent best practices applied specifically to them.

Survey: FI Responses About Their Fintech Partners (Averages)



"It's like any marriage," says Cornerstone Advisors Senior Director Sam Kilmer. "When you ask how it's going, the marriage is great. But if you peel back the onion and ask about taking out the garbage or doing the dishes, reactions are a little more critical. It's not a deal breaker. It's the difference between needing a divorce lawyer or a marriage counselor."

CULTURE CLUB

The decade since the 2008 financial crisis has been marked by profound changes in the relationship between financial technology and financial institutions to the point where "banking as usual" no longer exists. Acknowledging the differences between two dissimilar organizational structures is a good place to start.

Fintechs build a software solution and wrap services around it to help clients succeed. The romantic notion of an innovative startup in a garage is not far from the truth — and established fintechs often snap up the garage-driven technology. Financial institutions essentially do transactions, sell debt and help people's down-the-road financial outcomes.

"It's about differences in culture," says Ryan Rackley, managing director at Cornerstone. "When people recognize the delta and work without hesitation to bridge the gap, it leads to high-level efficiency and satisfaction on both sides of the table."

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LEARNING TO DRIVE

One such area involves implementation. A fintech can create viable software or a platform to build upon, but the FI needs to have the internal talent to leverage it. A culture of disciplined execution and accountability that ensures the fintech solution will be deployed in a high performance, referenceable way will go a long away in strengthening the partnership.

"It's not just the technology," says Rackley. "It's about the talent needed to drive it."

Financial institutions that value good integration practices can take an active role that leads to successful partnerships.

Rackley relates a story about a middle-America bank four hours away from an airport. The bank had a core system in place with a software development kit (SDK) layer and a recently added application programming interface (API) set. They took two employees, made them part of IT and gave them proper training. Fast-forward six weeks and the bank had a fully integrated card-control button within its mobile app that's connected via core and its card-processor channel.

"They're running circles around the biggest shops out there," Rackley says. "And it's all because they put a framework in place where they can DIY their own integration layer. That's so powerful—it's redefining how we view success moving forward."

It illustrates the notion that financial institutions that value good integration practices can take an active role that leads to successful partnerships. But it also underscores the value of getting outside of IT and involving the decision makers who control where the money goes.

"It's about tying the person with the purse strings to the person driving the decisions, and then getting connected to the people who create the revenue. It's a huge but worthwhile undertaking," says Kilmer.

PULSE POINTS

One thing fintechs crave is a specific checklist of items the financial institution is seeking. That avoids death-by-a-thousand-cuts frustration whereby the FI keeps adding one more thing after one more thing.

"I hear it all the time from fintechs," Rackley says. "They're saying, 'I don't know how to make these bankers happy.'"

Fintechs also want their bank and credit union clients to help keep tabs on the market in order to stay abreast of what's going on from a business standpoint and what the future might hold. That makes user events vital, because they allow fintechs to course-correct their product roadmaps and refocus their energy where and when needed. It also helps them stay in tune with competitors—because as a fintech, it's a safe bet that clients are being called on by three or four alternative providers.

"It's really important to get those direct client interactions," Kilmer says. "It's not just good information. You can feel your clients leaning into you and sense that they're connecting in meaningful ways."

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At the same time, FIs want clear, credible roadmaps based on business needs and quality—not quantity. Throw a 35-page roadmap with 170 different goals and outcomes in front of someone and they're probably asleep within 30 seconds.

"If fintechs can get it down to a one-page visual roadmap, with firm dates including enhancements, new modules, pilot developments and integrations," Kilmer says, "they have a much better shot at engaging the CEO and COO."

SPEED TRAPS

Financial institutions also place a premium on reliability versus speed. Getting a new widget in place by April rather than June isn't a big deal in the grand scheme of things. What becomes a big deal is mistakenly promising you'll have it ready in April. The institution's marketing machine sets customer expectations.

"All of a sudden the rollout gets delayed two months, and everybody's upset," Rackley says. "Those unmet expectations are what cause failure – not the month it's actually put in place."

> **"We're talking multi-million-dollar contracts. And we're talking tens of thousands of dollars in training. We don't want to fall victim to a penny-wise-pound-foolish mentality."**

Quarterly business reviews are increasingly prevalent but, in too many cases, adequate prep work is missing. Both sides are best served by making a realistic effort to identify things like crucial performance metrics, specific business issues, key working objectives, mutual outcomes and who's accountable for what.

"Otherwise these interactions are like Groundhog Day," Rackley says. "We're meeting again and we don't have an agenda, but at least there's coffee on the table."

Finally, training and system utilization reviews need to find their way into contracts. For instance, an inventory for executive management that details how many users have gone through which modules of training can be vitally important, but it involves only minor add-on costs.

"We're talking multi-million-dollar contracts," Williams says. "And we're talking tens of thousands of dollars in training. We don't want to fall victim to a penny-wise-pound-foolish mentality."

Every little thing can lead to a better partnership. And both sides know they're getting there when the fintech team wants to do right by the institution. Can you pick up the phone for a simple 30-second fine-tuning call without preparation? Can you get through on a Saturday to the right player—and find them with a positive attitude? If you have to rattle cages to get people to work for you, something is broken.

IN THE END

"I see FIs and fintechs doing parts and pieces of these things," Rackley says. "Yet very rarely do I see all these things being put in place. But in those partnerships where it exists—like that little bank in rural America—it's very striking."

In some vital ways both sides are already aligned. And it's still about three core tenets of running a business: Making money, containing costs and reducing risk. The rest involves aligning myriad details into cogent, purposeful steps that move banks and credit unions into the future with minimal hiccups and delays. The sum is bigger than the parts.

"The knowledge for leveraging emerging technology is out there," Kilmer says. "So how do we organize and share that knowledge to become better users?"

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Confectionary lore says that 90 years ago—in a garage—a dairy farmer turned the unlikely pairing of peanut butter and chocolate into peanut butter cups. Nearly a century later, that unlikely partnership has evolved into America's best-selling candy.

Financial institutions and fintechs are positioned to find a much shorter timeline on the road to sweet success. They just need to invest the time and effort to learn what's keeping them from making it happen.

Cornerstone Advisors takes financial institutions from strategy to execution with consulting solutions that address the immediate and evolving challenges of the banking industry. Our experts know fintech, strategy, contracts, performance, technology, mergers and acquisitions, payments, delivery channels and lending—inside and out. And, when we're not advising, we're sharing knowledge through Insight Vault, Cornerstone Performance Report, GonzoBanker, white papers and commissioned research.

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Have questions about this report?

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