

# INNOVATION READINESS PLAYBOOK

FI SEGMENTS PAYMENT PERFORMER  
EDITION



The PYMNTS Innovation Readiness series, in partnership with payments and commerce solutions provider i2c Inc., gauges where banks are on the road to becoming innovators. We surveyed executives at 214 FIs in the U.S. (excluding the largest 25 banks) and scored the institutions from zero to 100 in terms of innovation readiness. The banks in our sample fell into four size groups: assets below \$500 million, \$500 million to \$1 billion, \$1 billion to \$25 billion and more than \$25 billion. We divided the banks into three groups: Top 15 Performers, Middle Performers and Bottom 15 Performers. We then analyzed the data to understand what, exactly, Top Performers are doing so well, and the lessons everyone else can learn from them.

MARCH 2018

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The Innovation Readiness Index: Innovation Playbook was done in collaboration with i2c, and PYMNTS is grateful for the company’s support and insight. [PYMNTS.com](#) retains full editorial control over the findings presented as well as the methodology and data analysis.

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ABOUT

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Banks are currently racing to innovate. FinTech startups like Venmo and Square have chipped away at their business by offering new services like person-to-person (P2P) transfers, leaving many major players scrambling to catch up..

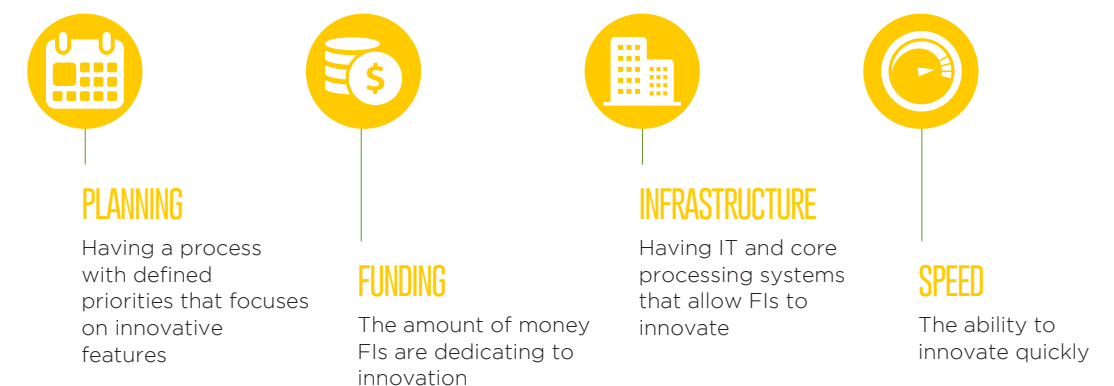
To develop a culture of innovation, ING Bank even resorted to the drastic measure of firing all its employees and then rehiring them to build a new corporate culture.<sup>1</sup> Its new culture, called “agile,” is based on a pastiche of practices from tech firms like Spotify and Netflix. It emphasizes getting products to market quickly to keep up with the innovation race.

But what does it really take for banks to be innovative, and just where are most banks on the road to becoming innovation-ready?

We rolled out our Innovation Readiness Index™ last quarter, a report to gauge where banks are on the road to becoming innovators. Our Innovation Playbook series was developed to dive into specific data from the Index. The first, our Top Payments Performer Edition, published last month and dug deep into what top innovators are doing to make an impact. In this edition, we’re examining mid-sized financial institutions (FIs) with assets ranging from \$5 billion to \$25 billion. They aren’t the big players like Bank of America, instead comprising the next level down, and they’re responsible for handling approximately 14 percent of consumer deposits.

<sup>1</sup> Jacobs, P; Mahadevan, D. and Schlatmann, B. ING’s agile transformation. McKinsey & Company. 2017. <https://www.mckinsey.com/industries/financial-services/our-insights/ings-agile-transformation>. Accessed February 2017..

In our last report, we found that Top Performers distinguished themselves in four key categories: planning, funding, infrastructure and speed. They planned well, focusing on innovating features and defining their priorities for the next three years. At least 50 percent of their budgets were allocated to innovation, and the bulk of their funding was reserved for payments innovation instead of other areas. Their existing IT infrastructure and core systems also made innovation easy, meaning they



**Figure 1:** Mid-Sized FI Composition, by Performance



could go from development to market in six months and complete their projects early or on time.

Overall, mid-sized FIs aren’t winning any prizes for innovation. Approximately 89 percent of them are Middle Performers, and the remaining rank as Bottom Performers. None of them have made it into the Top Performer bracket yet.

Though they are in a position to deliver innovative features and products, mid-sized banks are falling behind their peers — especially in terms of technology and IT Infrastructure. That does not bode well in today’s hyper-competitive market, as traditional mid-sized FIs risk being outflanked by more agile FIs and FinTechs.

We’ll dig down into why this is in the rest of our report. We’ll also discuss how the mid-sized FIs line up on each of the four key attributes separating top and middle innovators — including planning, funding, infrastructure and time required to market — then dive into emerging best practices and remaining challenges.





PLANING



The first attribute we identified as key for becoming a top innovation performer was planning. In our last playbook, we noted that all our Top Performers had defined their innovation strategies for the next three years while also focusing on three or four innovation areas — like payments technology, consumer engagement and digital analytics. Middle and Bottom Performers, meanwhile, tended to have just one or two areas of focus.

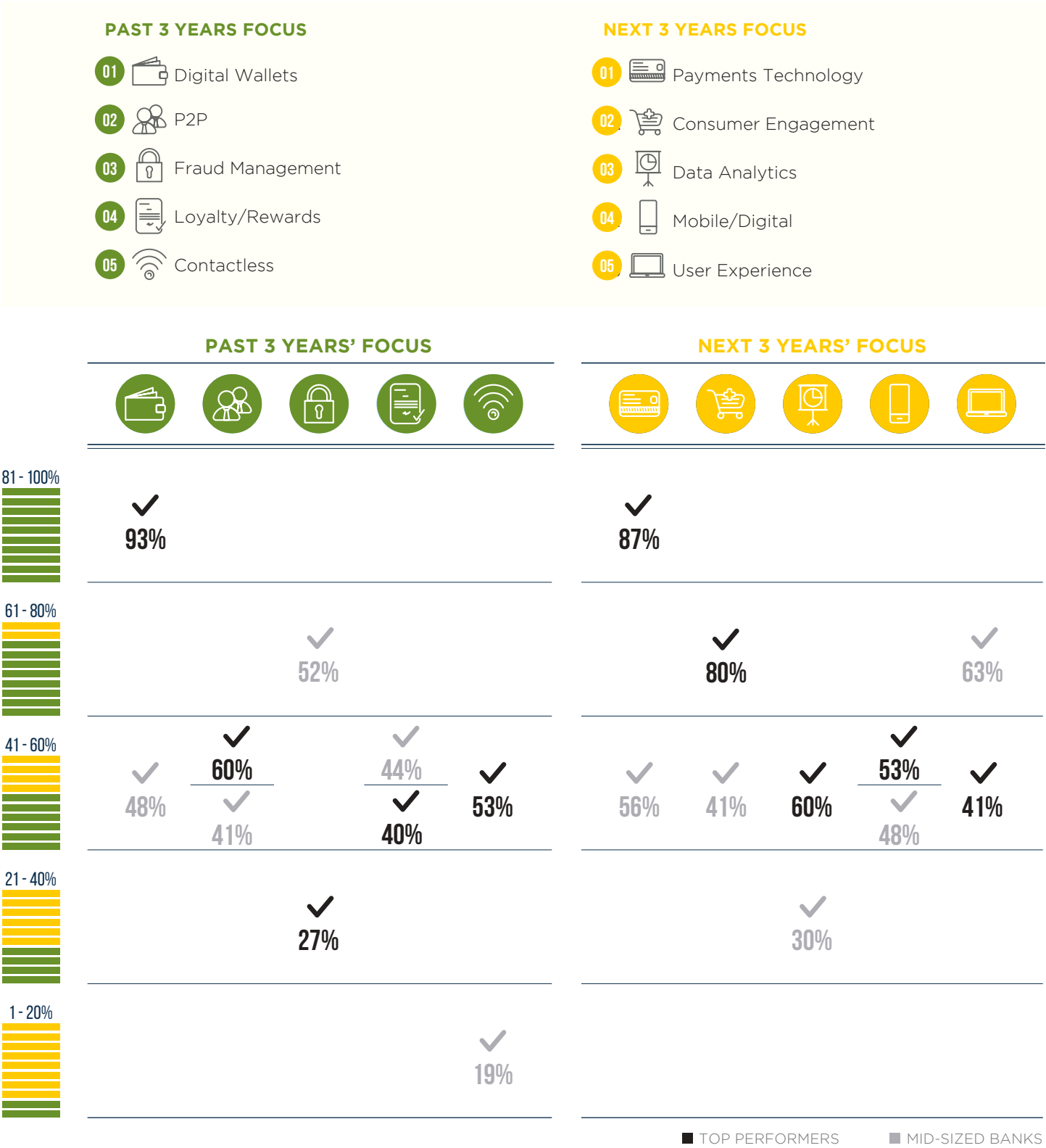
The good news is that mid-sized FIs *are* focusing on three or four different areas. The bad news is that they are more similar to Middle Performers than Top Performers for everything else. Mid-sized FIs are inclined to be more reactive than proactive. Like Top Performers, they focus on testing with customers, testing new features in a sandbox and cash and ROI calculations, but their motives for innovating are like those of Middle Performers, too. This means they place very little priority on serving potential client needs.

SETTING PRIORITIES:

Our last report found that Top Performers distinguished themselves by setting clear priorities focused on innovative technology, such as digital wallets and contactless payments. Our mid-sized banks are still playing catch up. They’re focusing on digital wallets (but at a much lower rate) and fraud management.

Table 1: Past vs. Future Areas of Focus for Top Performers and Mid-Sized FIs

Top Performers will turn their attention to payments technologies, consumer engagement and data analytics.



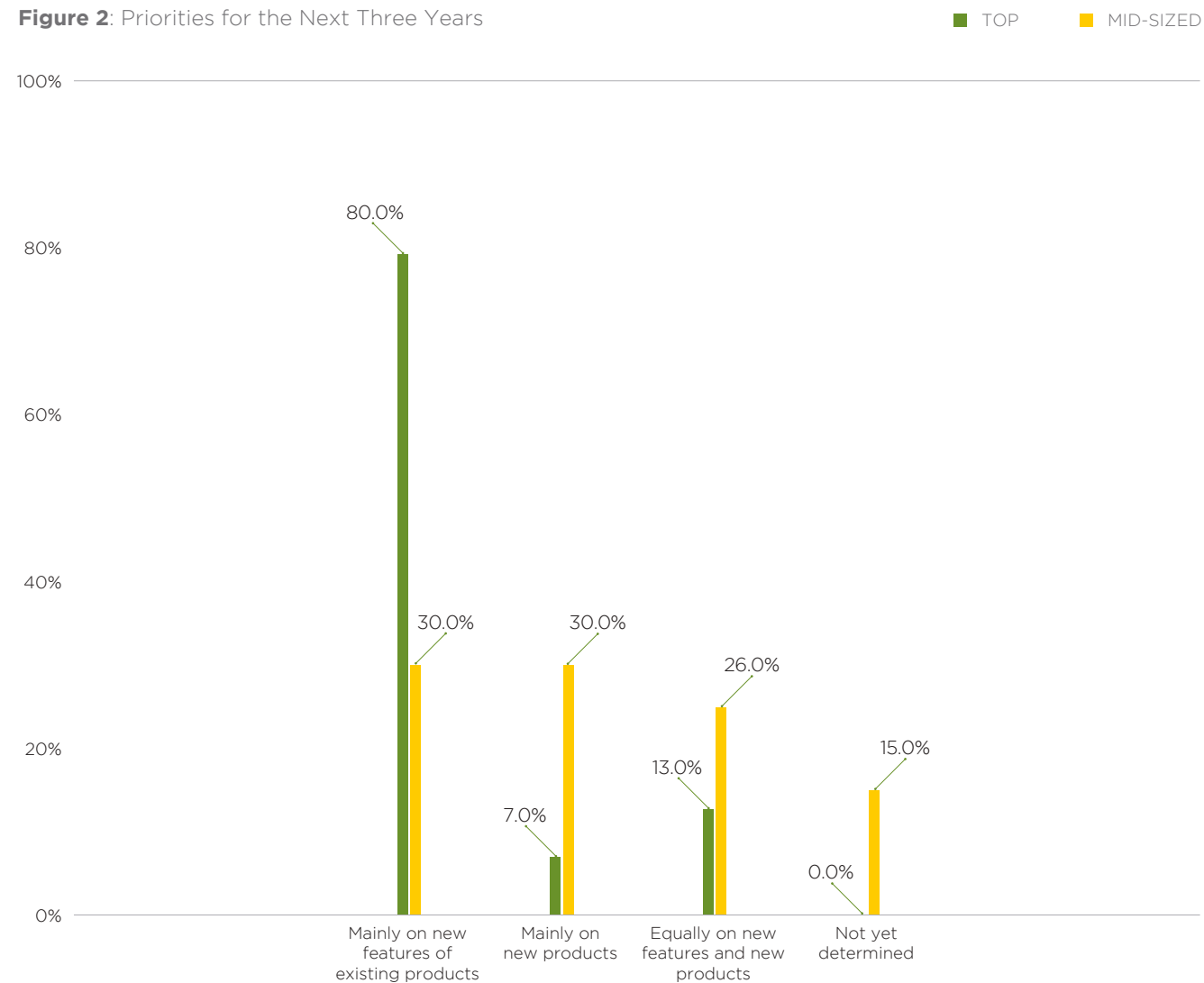


Going forward, Top Performers are focusing on payments technology and consumer engagement. Mid-sized FIs, however, are focusing on user experience, payments technology (at a much lower rate than Top Performers) and mobile/digital payments.

For the next three years, 80 percent of Top Performers will be focused on adding new features to existing

products. In other words, they've rolled out new products and are now making them better. Only 30 percent of mid-sized banks are doing the same, though, and another 30 percent are just scrambling to add new products to match Top Performers. Fifteen percent haven't decided what their priorities will be for the next three years, but we can say with confidence that none of the Top Performers are in that situation.

**Figure 2:** Priorities for the Next Three Years



## KEY TAKEAWAYS AND LESSONS LEARNED:



### PLANNING CHECKLIST

- ☐ Set priorities for an innovation strategy now.
- ☐ Plan for investments in payments technology, consumer engagement and data analytics.
- ☐ "Table stakes" functionalities like P2P, digital wallets and mobile/digital are must-haves.
- ☐ Assess your company's core payments infrastructure to see if it has the flexibility to support rapid roll out of key features.
- ☐ Secure the budget to support your company's innovation initiatives.



### Top performing banks are focusing on making existing products better.

- Mid-sized banks are slow to roll out these same features.



### Mid-sized FIs are behind in setting innovation priorities.

- Top performing innovators set goals and priorities for innovation.
- Mid-sized FIs are playing catch up.



### Engagement will be key in the future.

Engagement = User Experience + Digital + Data Analytics

- Sophisticated consumer engagement is a must. This includes UI, digital and data-driven elements.



### The right payments technology is critical to execution.

- Banks that outperform others have flexible and configurable payments technology in place.

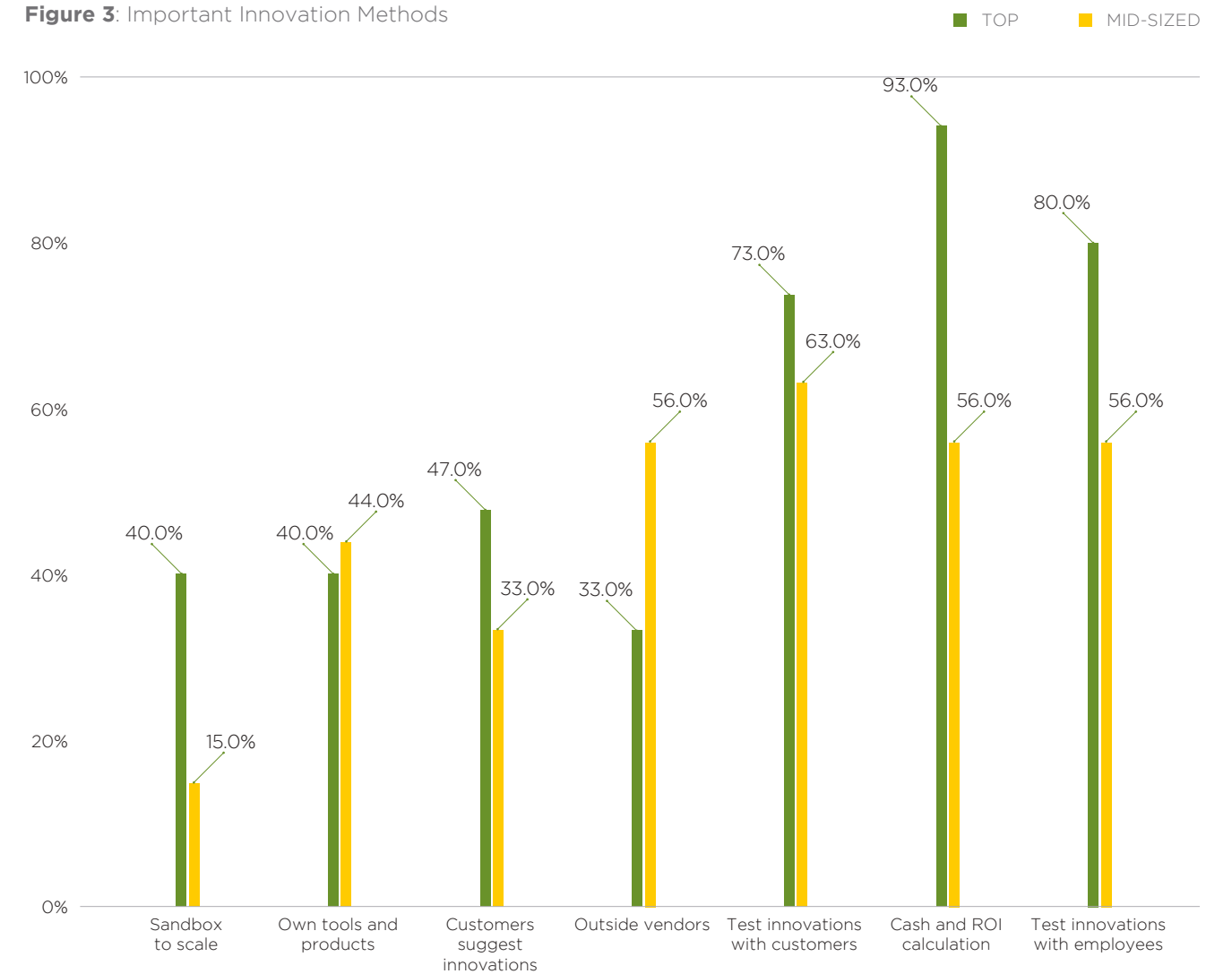
## INNOVATION METHODOLOGIES



Top Performers have a method to their madness: They use several different innovation methodologies. The four that are key for innovation readiness include testing innovations with employees, cash and ROI calculations, testing innovations in a sandbox and paying attention to customers by listening and acting on their suggestions.

Our mid-sized FI group isn't doing well here, either. Instead of focusing on cash and ROI calculations, testing innovations with employees or using sandbox-to-scale functionality, its favored innovation methods are testing innovations with customers and then testing them with employees. This group also relies on outside vendors at nearly twice the rate of Top Performers.

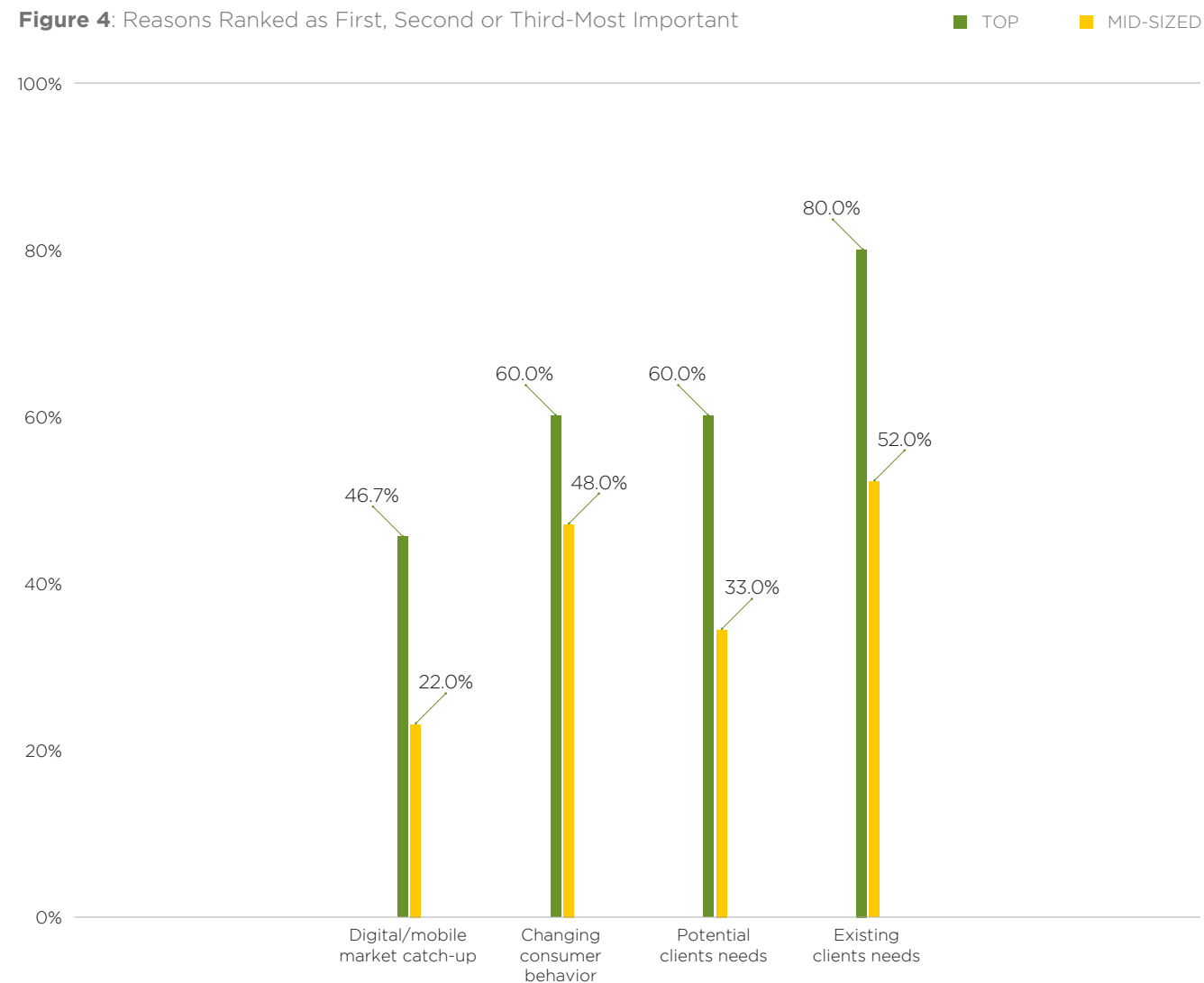
**Figure 3:** Important Innovation Methods



While Top Performers state that their primary reasons for innovating are to serve existing client needs, potential client needs and changing consumer behavior, mid-sized banks are more conservative. They believe in serving existing client needs (though at a

much lower rate than Top Performers) followed by changing consumer behavior, rather than anticipating the future and trying to serve potential client needs. This could explain why their priority setting is more reactive than proactive.

**Figure 4:** Reasons Ranked as First, Second or Third-Most Important



#### METHODOLOGIES CHECKLIST

- ☐ Focus on identifying and then serving existing client needs.
- ☐ Set priorities that focus on payments technology instead of simply playing catch up.
- ☐ Incorporate Top Performers' favorite innovation methods, including:
  - *Using cash and ROI calculations to gauge success*
  - *Testing innovations with customers and employees*

## KEY TAKEAWAYS AND LESSONS LEARNED:



### Mid-sized banks are reactive.

- Mid-sized banks rely on their vendors instead of using multiple methodologies.
- Top Performers have a better balance.



### Leaders tune in to both customer and market needs.

- Top Performers listen to customer needs.
- They measure the ROI of innovation efforts.
- They use multiple innovation methods.



### Leaders test for success.

- Top Performers test and iterate innovations in a sandbox, then scale them to market quickly.
- They test new features and products with customers and employees.





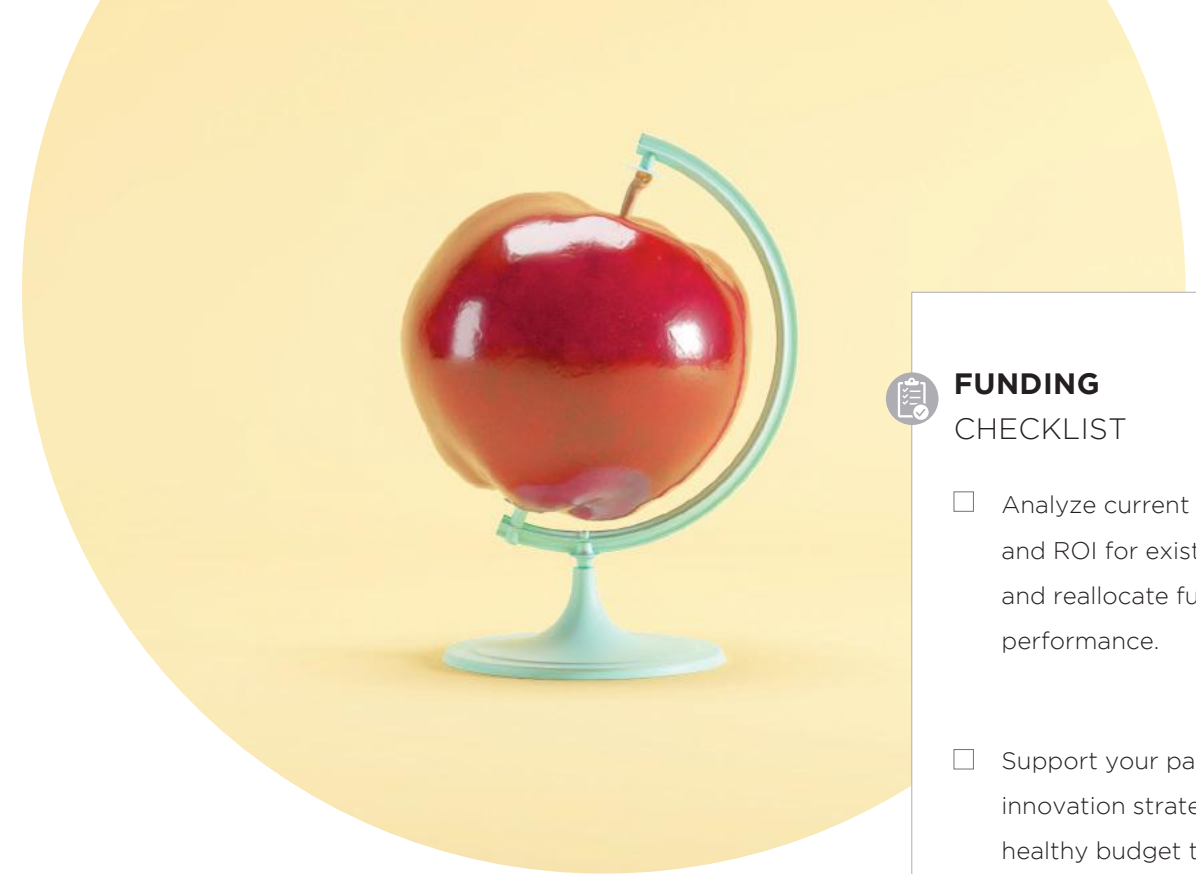
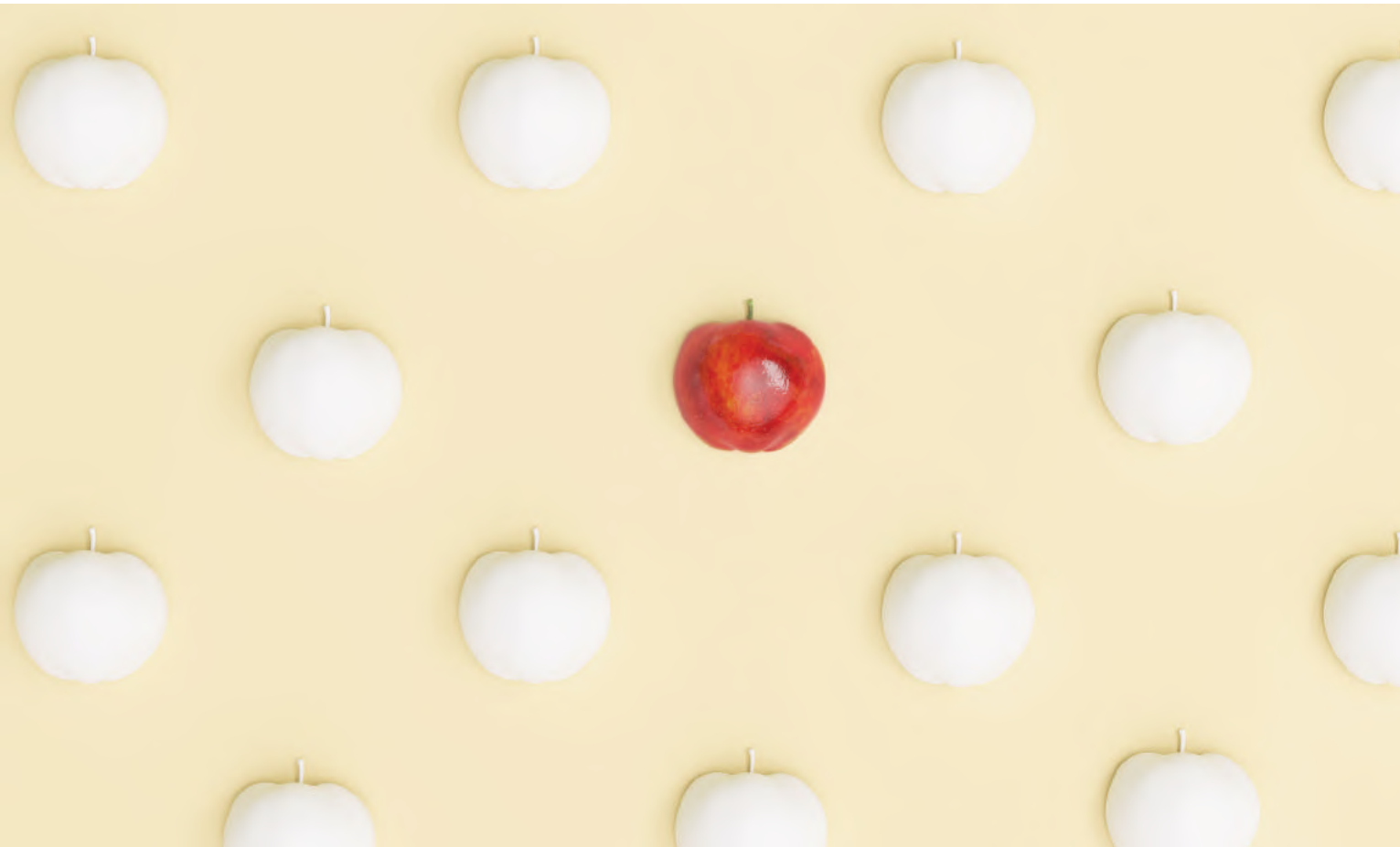
FUNDING





**T**op performers support their important innovation projects with healthy budgets, funding the projects about which they care. In fact, they allocate more than 75 percent of their payments budget toward funding those projects. Two-thirds of FIs with assets between \$5

billion and \$25 billion allocate less than 25 percent their budget toward innovation. By contrast, only 14 percent of Top Performers allocate that little, and more than two-thirds allocate more than half the payments budget for it.



#### **FUNDING** CHECKLIST

- ☐ Analyze current investments and ROI for existing projects, and reallocate funding based on performance.
- ☐ Support your payments innovation strategy with a healthy budget to keep pace with the competition.

“Top performers allocate 75 percent of their payments budgets toward funding projects, while mid-sized banks allocate less than  
**25 PERCENT.**”



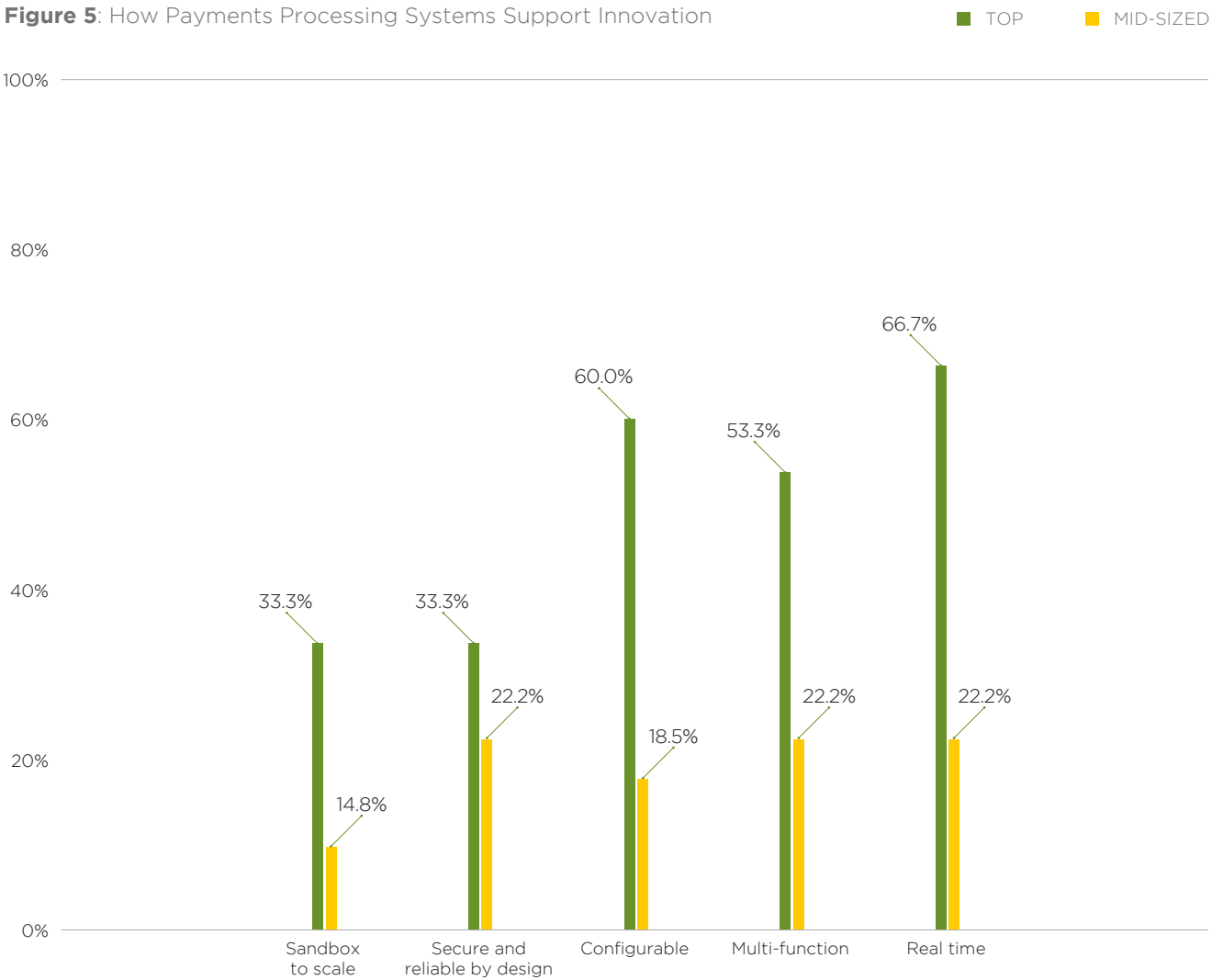
Top Performers don't just plan for innovation and then fund those plans. They also have the infrastructure in place to be able to execute. Seventy-three percent of Top Performers said their core systems were well-suited for innovation compared to 41 percent of mid-sized banks.

Looking closer, the numbers paint an even darker picture. As shown in Figure 5, only 22 percent of mid-sized FIs have both real-time support and payments processing systems that are multifunctional, secure and reliable. Meanwhile, just 19 percent have configurable core systems, and only 15 percent use sandbox-to-scale.

On the other hand, 60 percent of Top Performers have configurable core payments processing systems, compared to just 19 percent of mid-sized banks. The capability is critical for innovation, and mid-sized banks are three times more likely to report their processing systems are not configurable.

In addition, 53 percent of Top Performers report having multifunctional processing systems compared to just 22 percent of mid-sized FIs — 11 percent fewer than middle performing banks in our survey. Multifunctional processing systems that can support any form of debit, credit, prepaid or virtual payments are important, helping banks “future proof” their offerings and more easily add new features at a later date.

Figure 5: How Payments Processing Systems Support Innovation



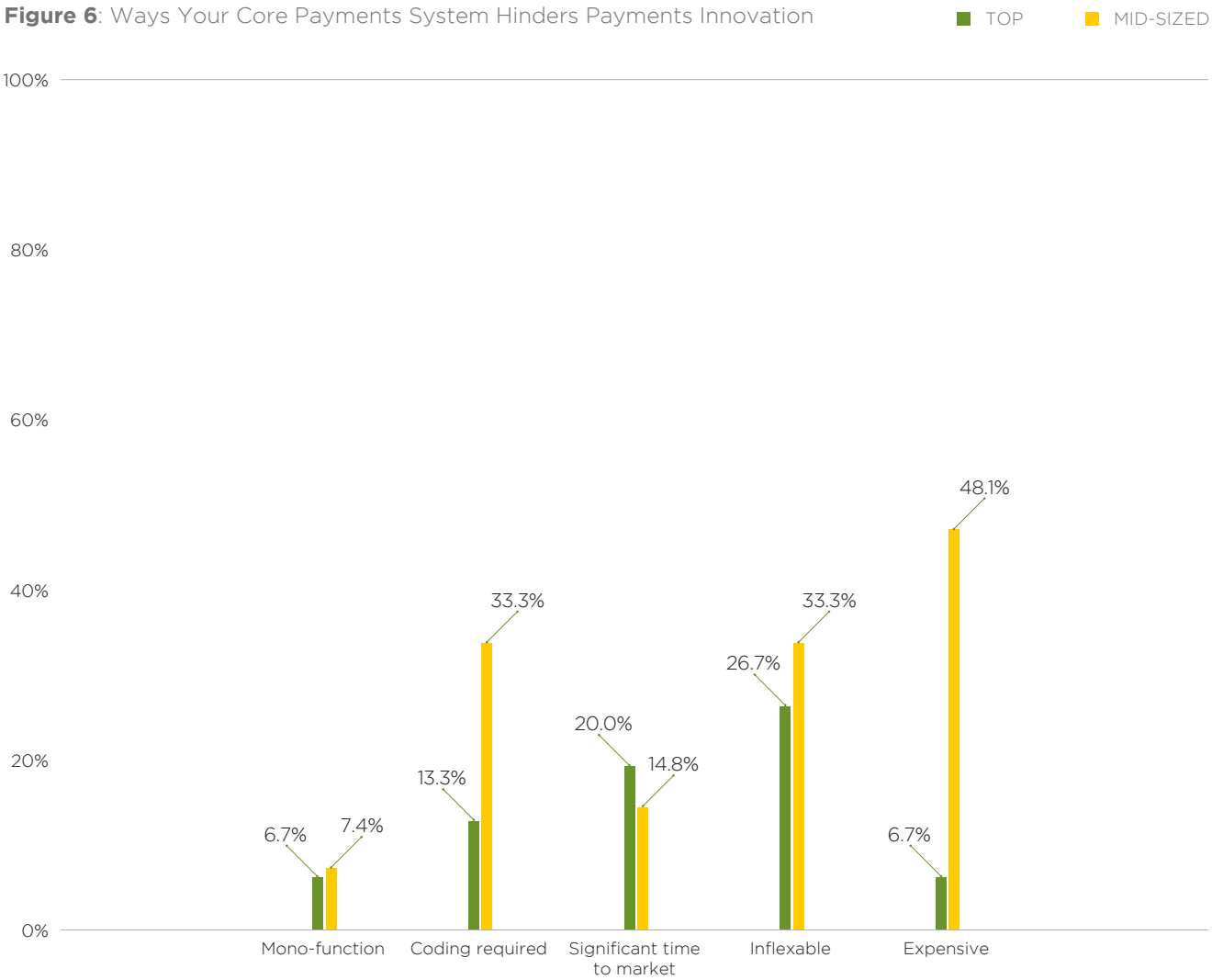
“Mid-sized banks pointed out that their expensive and inflexible core payment systems hindered INNOVATION.”





Meanwhile, mid-sized banks pointed out that their expensive and inflexible core payment systems hindered innovation. In fact, the characteristics of their core payment systems most closely resembled Bottom Performers, an ominous sign for mid-sized banks’ ability to be innovative going forward.

**Figure 6:** Ways Your Core Payments System Hinders Payments Innovation



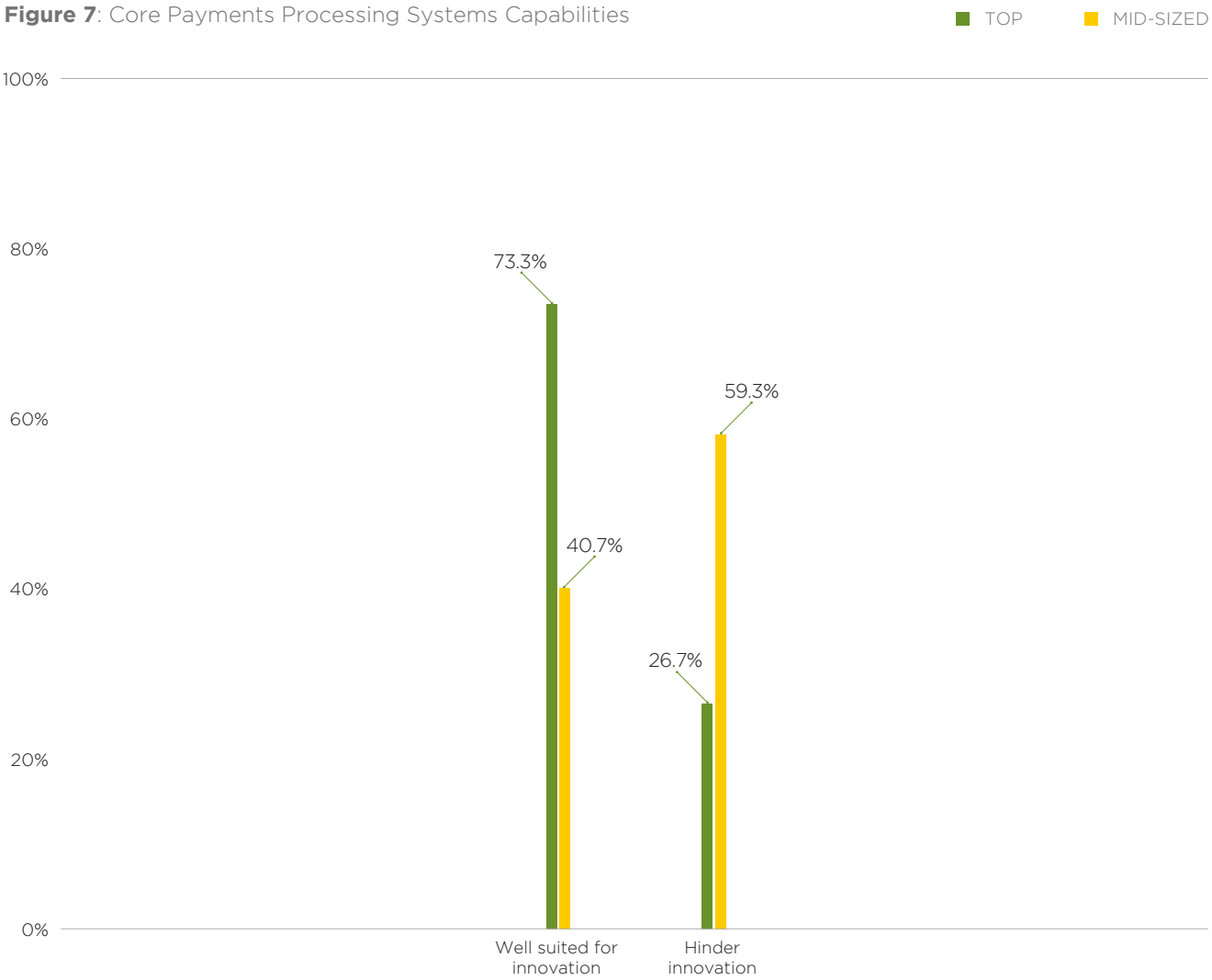
Almost 60 percent of companies in the segment said their payments system hindered innovation. That’s not a small issue when it comes to innovation, as it means those that try to innovate will be spending a lot of their time working with a system that makes the task harder.

As shown in Figure 8, banks with more than \$25 billion in assets reported much higher levels of frustration with their

core payments systems on all counts except mono-functionality. Sixty-eight percent said their systems are inflexible, and 65 percent reported taking significant time to get new products and features to market. This could be due to reliance on legacy processing technology.

In summary, mid-sized banks have a long way to go before they hit their

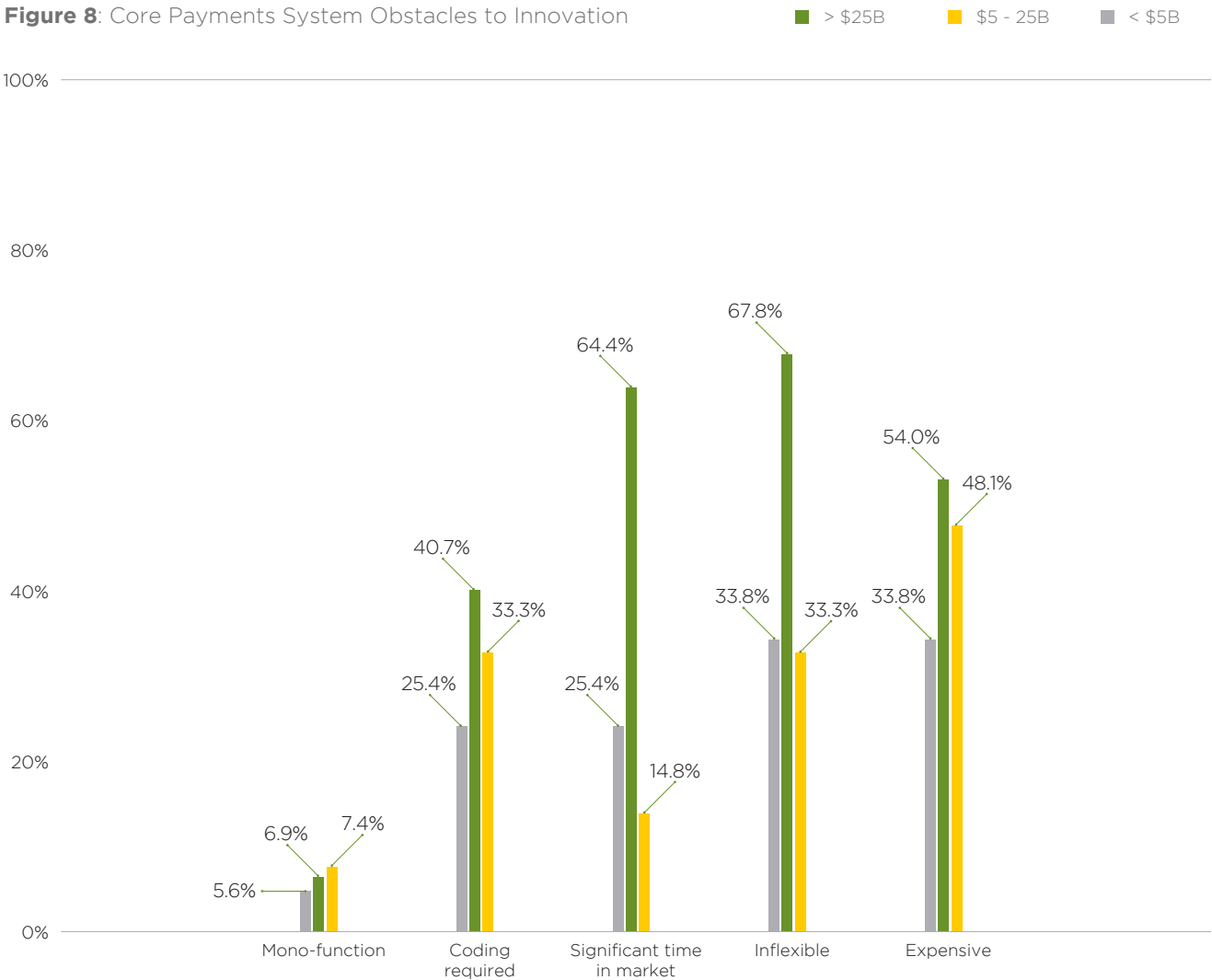
**Figure 7:** Core Payments Processing Systems Capabilities



strides as innovators. Their inflexible core payments systems hinder innovation, a primary reason why there are no top performing banks in this segment. In contrast, Top Performers are able to leverage a key technology advantage: infrastructure that is flexible,

configurable and enables testing of new features in a sandbox environment. As a result, they report far more success when rolling out new features and products — and they can do so faster than their competition.

Figure 8: Core Payments System Obstacles to Innovation



KEY TAKEAWAYS AND  
LESSONS LEARNED:



**Mid-sized banks' inflexible and expensive core payments systems hindered innovation.**

- They require hard coding and are inflexible.



**INFRASTRUCTURE  
CHECKLIST**

- ☐ When assessing a core payments system, make sure it is configurable, flexible and multi-functional.
- ☐ Future proof your company's payments strategy with a multifunction core processing system.
- ☐ Make sure your company can test and iterate new products and features in a sandbox environment.

SPEED

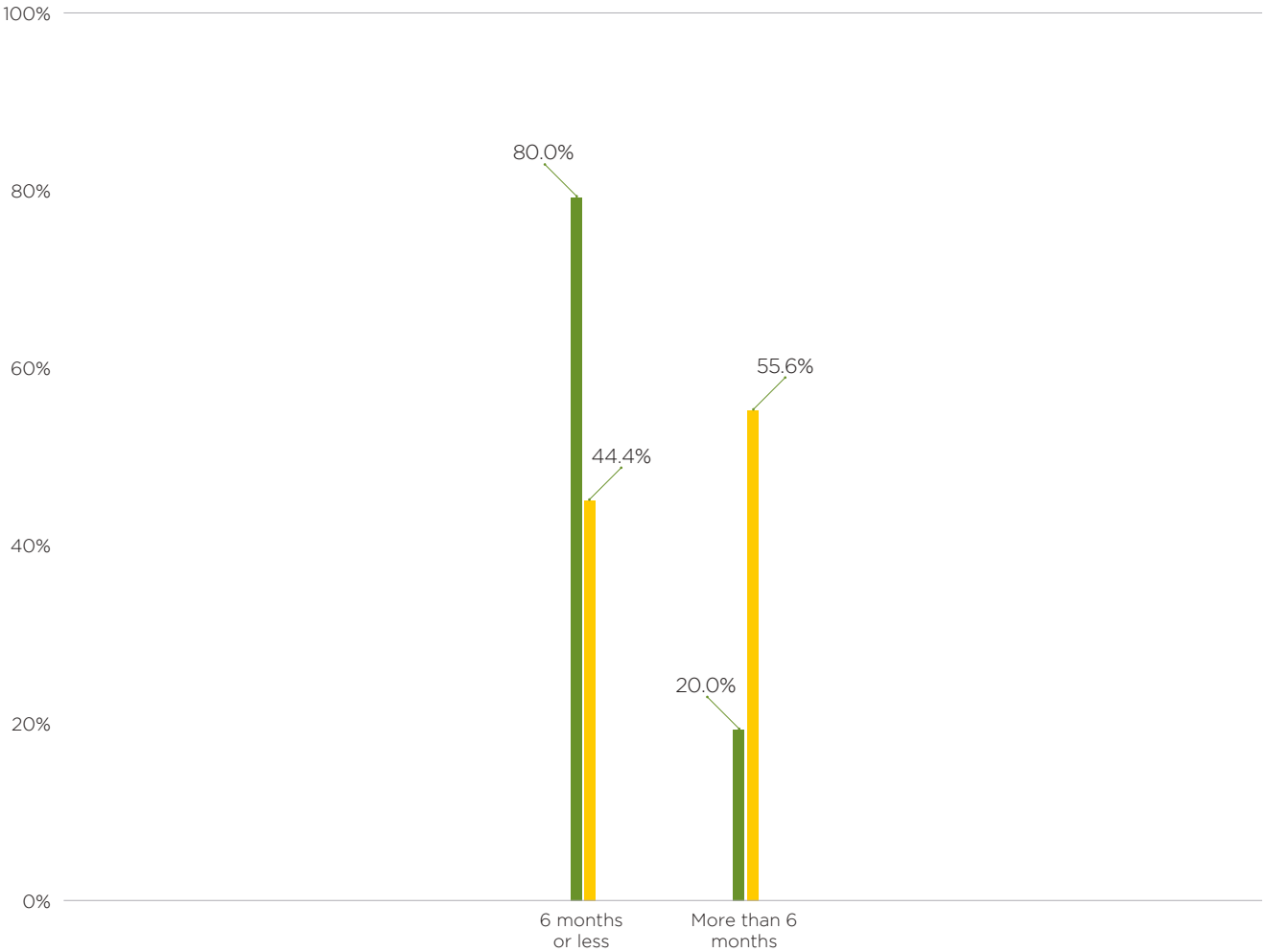


Our last key element is speed. Eighty percent of Top Performers can go to market in six months or fewer, so how do our mid-sized banks stack up? To be brief, they don't. On average, mid-sized FIs need 9.72 months to go to market, and only 44.4 percent of them can do so in less than six.

The good news is that nearly 20 percent of mid-sized banks are doing staggeringly well, taking only three months to go to market. At the other end of the spectrum, however, 30 percent need a year or more to do so. Most — 71 percent — are completing their projects early or on time. They just need to complete them faster.

Figure 9: Product Development and Implementation Time

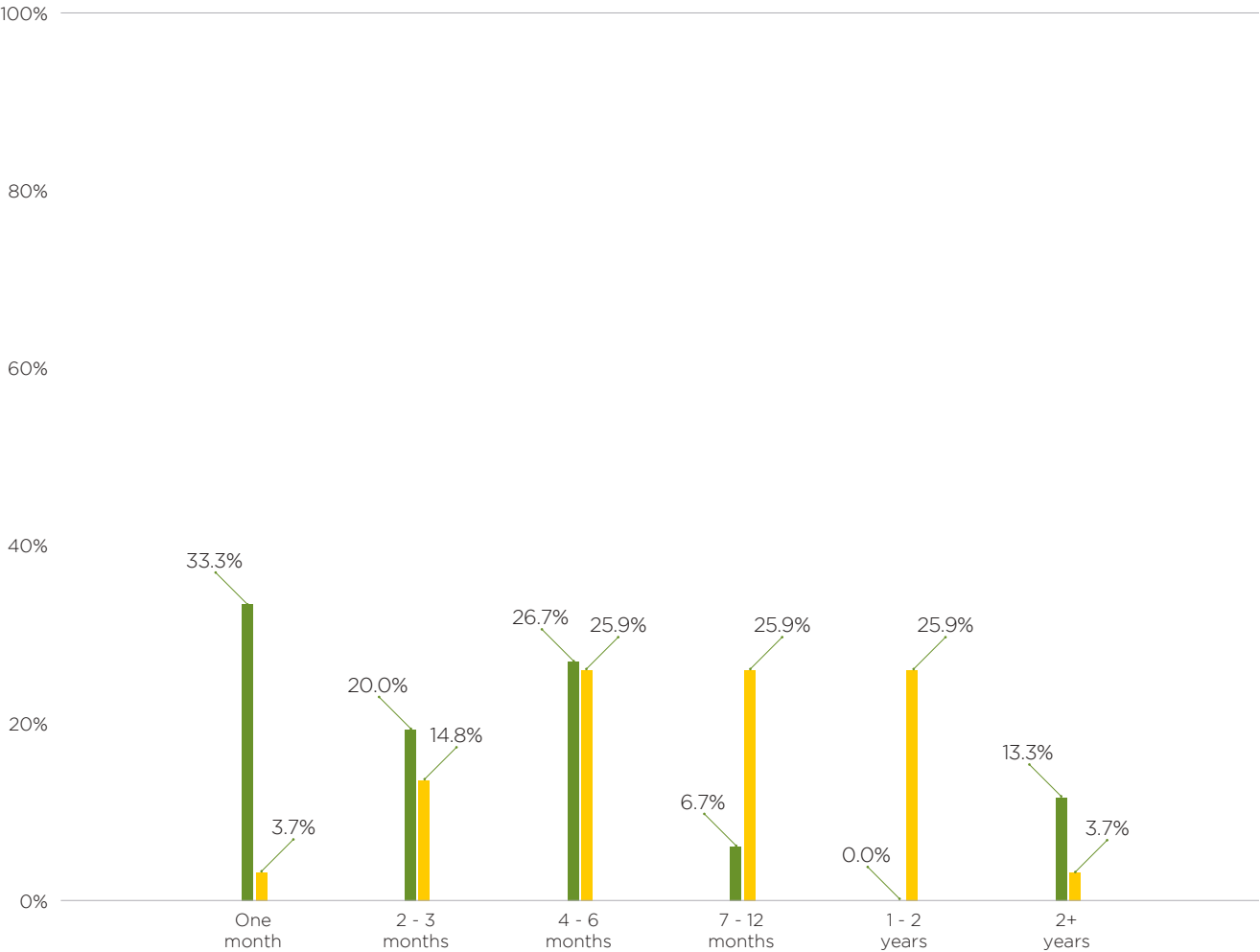
■ TOP ■ MID-SIZED



“Mid-sized FIs need 9.7 MONTHS to go to market, whereas 80 percent of Top Performing banks do so in six months or fewer.”

Figure 10: Product Development and Implementation Time

■ TOP ■ MID-SIZED





# REMAINING CHALLENGES





The road to innovation is long and littered with obstacles, but those roadblocks look different depending on who you are. While Top Performers saw regulations and customer experience as their major obstacles to innovation, mid-sized banks were more like Middle and Bottom Performers. They felt budget and regulations equally hindered them in their innovation process.

We asked mid-sized banks to identify the elements that would most help them improve their performance. The top three were optimized methods (19 percent), a more qualified team (15 percent) and user experience (11 percent). By comparison, Top Performers were split between several options.



Figure 11: Largest Innovation Obstacles

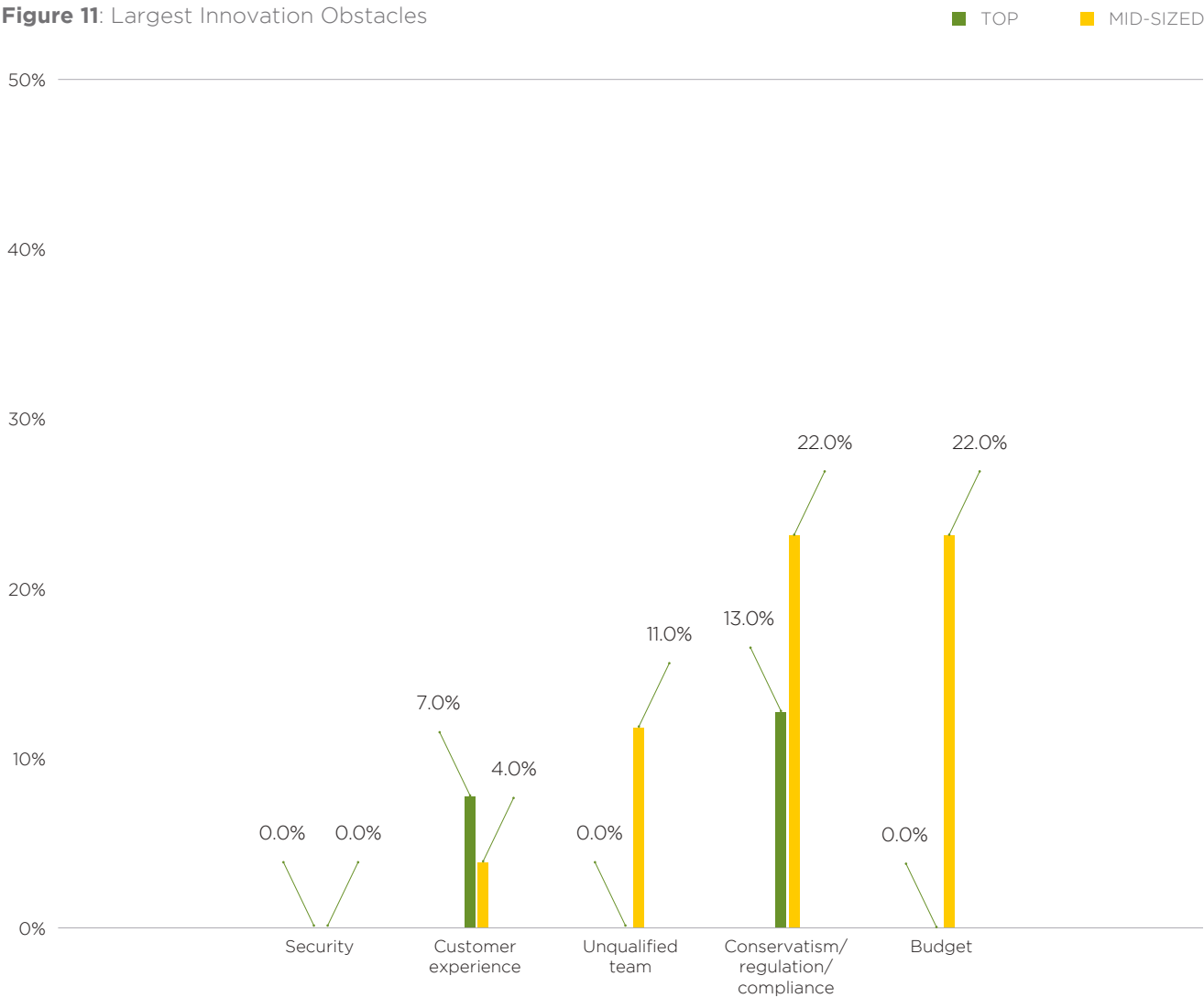


Figure 12: How FIs Would Improve Their Innovation Capacity





# BECOMING A TOP PAYMENTS PERFORMER





The payments innovation journey may seem difficult for mid-sized banks, but the result is remaining a strong competitor in the future.

Mid-sized FIs have a lot to learn from Top Performers, particularly those that have found the recipe for success. These FIs make innovation a core competency by setting priorities, planning strategically, monetizing innovation plans and leveraging flexible technology that keeps them nimble.

Innovation doesn't happen on its own, though, and mid-sized FIs must be proactive. They cannot wait for vendors to innovate for them, and they must listen to their customers and use multiple methods to plan and execute their payments strategy.

Our findings show technology can be an equalizer for FIs of any size, and that the right IT and payments infrastructure is essential for innovation. Mid-sized banks should assess their own and consider a long-term strategy that includes configurable, multifunctional payments systems to “future proof” their systems.

Top Performers’ success provides a roadmap for the industry, and these banks are quickly outflanking their competitors. In the end, time and speed are of the essence, and mid-sized FIs need to act fast — and act now. If they don't, they risk finding themselves left in the dust.

Access the complete [Innovation Readiness Playbook Series](#) here.




IN FOUR STEPS, MID-SIZED BANKS MUST:

01

**BE PROACTIVE,  
NOT REACTIVE**


Listen closely to customer needs and use multiple methods to plan and execute their payments roadmaps. Top Performers do not wait for vendors to innovate for them.



02

**ASSESS AND ADJUST  
YOUR INNOVATION  
INVESTMENTS**


Success can depend on appropriate funding of the right innovation. Mid-sized FIs must look closely at both their current program investments and ROI, then reallocate funding based on performance.



03

**LEVERAGE TECHNOLOGY  
AS AN EQUALIZER**


The right IT infrastructure and payments technology can prove to be a critical investment. It's a great equalizer for FIs of any size when leveraged correctly.



04

**ACT NOW**

The top innovating FIs move quickly, posing a competitive risk to mid-sized FIs that underperform. They need to set clearly defined plans and priorities for their innovation efforts, then budget for them effectively.



“Mid-sized banks need to begin anticipating market needs, not play catch up.”



# ABOUT

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