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TO IMPROVE A BANK'S EFFICIENCY RATIO, INVEST IN DIGITAL TECHNOLOGY – AND YOUR EMPLOYEES

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The adoption of fintech solutions and the shift to digitized operating models have upended traditional banks' business and operating models, paving the way for more nimble, efficient organizations. But mid-market banks have a long way to go before they capture the productivity gains those technologies can deliver, according to a new survey of bank executives.

In 2019, West Monroe Partners and American Banker surveyed more than 150 director-level executives across U.S.-based mid-market banks—entities with $1 billion to $250 billion in managed assets—to gauge the priority they place on boosting productivity. And while nearly all banking executives consider improving productivity and performance top priorities, the survey data shows that based on current efficiency ratios, there are still extensive gains to be made.

Digging deeper into the data uncovered surprising insights about how banks perceive their efforts to increase productivity—what's working, where they are falling short, and how effectively implemented technologies can accelerate productivity and change the way banks think about an optimal efficiency ratio.

Digital technology has changed what's possible when it comes to banking productivity and target efficiency ratios. The mid-market is overwhelmingly aligned around the need to boost productivity by leveraging digital technology, but in order to deliver lower efficiency ratios, they need to focus on implementation around people, process, and culture

CONSENSUS AROUND EFFICIENCY RATIOS, TECHNOLOGY—BUT GAINS ARE LAGGING The efficiency ratio, which measures how effectively a bank converts assets into revenue, is arguably the single most important indicator of how well an institution is being run. It sends a clear signal of the bank's ability to achieve profitable growth and attractive shareholder returns.

The new survey data reveals that the efficiency ratio was among the most important performance indicators for mid-market bank executives; 98% of respondents say that improving efficiency is their number one strategic priority.

Until recently, the unwritten rule in the industry held that the optimal standard for an efficiency ratio was 50%. But the reality today is that successful implementation of new technologies is poised to deliver efficiency ratios much lower than that.

The survey also revealed widespread consensus on investing in technology; 61% of the executives say they are making investments in digital technology specifically to boost productivity.

And yet, the gains have not happened as quickly as they should. Nearly 80% of our survey respondents perceive that they have been extremely or very successful in improving efficiency/productivity at their banks in the past year, but only 34% have an efficiency ratio at or below 50%.

The lackluster gains in productivity are matched in the perceived effectiveness of new technologies; 43% say they don't believe they are getting the full value from their investments.

The good news is that this landscape provides fertile ground for mid-market institutions to make substantial productivity gains heading into 2020. The sector is aligned around the strategic need to boost productivity and its leaders understand that new technologies are the path to get there.

IMPLEMENTING NEW TECHNOLOGY: PEOPLE + PROCESS Technology by itself is not a silver bullet. In our experience, when new technology is not fully aligned with an organization's goals, strategy, people and even available skillsets, results will always lag.

Coupled with the focus on digitizing operations, banks must adopt a considered, strategic approach to how technology will be implemented and utilized by the people working with and alongside it.

Currently, though, just 34% of surveyed executives say that when they implement a new technology to improve a business process, they always redesign the process first. While the vast majority of respondents acknowledge they only sometimes or never take this step, our experience increasingly demonstrates the need to wed process improvement and tech implementation. When investing in new technology, the implementation and process improvement should go hand-in-hand.

Once a bank has a strategic plan to implement new automated processes, the focus should turn to the people in the organization. By its nature, automation takes jobs normally performed by humans and turns them over to a machine. This leaves a pool of workers who can be redirected to higher value tasks. A bank's employees, its human capital, remain a vitally important part of the equation – the formation of teams, roles, diverse talent, and training need to be considered. It's when people and technology can operate seamlessly together that banks will find the largest efficiency gains.

CONCLUSION The mid-market is overwhelmingly aligned around the need to boost productivity by leveraging digital technology, but it has significant ground to make up in the quest to achieve optimal efficiency.

We agree that prioritizing productivity via technology is the right investment for the mid-market, but caution that technology alone is not a silver bullet. Optimizing technology investments can unlock hampered efforts to lower efficiency ratios and boost productivity. In fact, our results revealed an alignment of the mid-market around digital-enabled productivity so strong, we posit that an industry where digital technologies enable more end-to-end online transactions and fewer branch locations, and where automated processes speed up and streamline operations—the mid-market could rewrite the formula around the optimal, achievable efficiency ratio.

Read the full report here.