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Top Ten Trends Impacting Bank Technology for 2005

Looking ahead to what bankers can expect in 2005, we find new challenges, some created by the increased use of technology but many that will be solved by new technology and its intelligent application. Technology now touches every area of the organization and is considered an important component in banks' strategic plans and compliance efforts.

To help bankers better plan for these new challenges, we offer ten predictions for 2005:

1. 2005 Will Be the Year of the Online Consumer

As more consumers get broadband Internet access from home, their online activity will increase exponentially, and we will see more rapid adoption of online banking services. Until now, many consumers had a technology mismatch in their homes, old PCs with broadband or new PCs with dial up. This made for an unpleasant online experience. New PCs and broadband are the winning combination that will finally break down the barriers to consumer acceptance of online banking and increase penetration of banks' customer base. Online sales figures for the 2004 holiday season will be the leading indicator of online activity expectations for 2005, and the early indications are for another record year of online sales.

2. Retail Delivery Goes Mainstream

As customers continue to demand multiple delivery channels and increased convenience, bankers will be forced to think more like retailers and less like traditional bankers.

Expect to see more titles like "senior vice president of the customer experience." Branches will be referred to as "stores." These "stores" will resemble your local Starbucks more than your average bank branch. Bankers will focus on customers' life events not just their transactions. Branches are being designed with more of a retail feel. Banks should start thinking about their branches as a retail store. Signage will be

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reviewed as bankers learn from studies such as the one from "Retail Anthropolgist," Paco Underhill, author of *Why We Buy*, that found there is a three-second window to catch a consumer's eye. As a result, branch technology becomes more of a strategic tool to help banks compete. Bankers will be taking a fresh look at ATM deployment, considering biometrics for customer self-service (e.g., accessing the safe deposit box area via palm scan), use of enhanced kiosks, and better use of multimedia to subtly advertise bank products and services and to entertain people standing in line.

3. Changing Times for IT Risk Management Call for New Budget Items

Bank budgets must be revised to reflect the reality of today's regulatory and technology environment. New budget items are being added for IT audits, network vulnerability assessments, managed security services, policy development, risk assessments and other IT risk management issues. In 2003-04 most banks didn't budget for such items. Oversight of IT has become wider in scope and more frequent, making banks more secure but at a cost.

4. Consolidation of Technology Providers Makes Due Diligence Imperative

Bankers are learning that salespeople move on and companies change names, making the due diligence process all the more important when choosing a technology provider. Contracts are being negotiated more fervently than ever with the understanding that the players could change due to mergers and acquisitions and the bank must be able to live with the consequences. There will be more escape clauses for mergers, acquisitions, and the "sunsetting" of technology. Bankers now realize that few companies survive the long haul. Case in point, from 1917 to 1987, only 39 members of the Forbes 100 survived; of those, 37 underperformed the market. The two that outperformed were GE and Kodak.

Additionally, regulators want to see documented due diligence and better vendor management. Expect bankers to take a structured approach to system selection, documenting the process to justify decisions and managing technology provider relationships more closely.

5. Hardware Becomes a Commodity

It's not 1999 anymore. Moore's Law remains applicable as hardware continues to become more powerful at less cost. Some technology providers have succumbed to this fact and now view hardware as a commodity item priced accordingly. Others are having a hard time giving up this revenue stream and still price their hardware platform arbitrarily and exorbitantly. Bankers doing their homework can enjoy some big savings.

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As storage needs increase due to imaging, data warehouses and the like, your vocabulary will expand with new terms such as petabyte (1,000 terabytes) and exabyte (one billion gigabytes). Hardware may be a commodity but demand for storage and better data management strategies will keep those hardware providers that adapt healthy. More data to manage will lead to the “Google-ization” of bank networks making the Windows Explorer model obsolete for retrieving files.

6. Community Banks Will Continue to Thrive and Grow

Community banks are alive and well. Expect the latest round of merger and acquisition activity to spawn another de novo explosion. De novo banks are starting with a clean technology slate and can quickly offer most of the same technology as their big bank competitors with much less bureaucracy and much more personal service. Market forces should allow community banks to thrive.

Community bank IT strategies will continue to differ slightly from large bank strategies. Community banks are more nimble at implementing technology but large banks have the high transaction volumes to better cost justify technology projects and enjoy true economies of scale.

7. Personal Productivity Will Be Expected and Measured

Bankers are expecting more from their people. “Produce or perish” seems to be the harsh reality that faces bank employees. As banks strive to be more efficient and contain costs, those employees not contributing are at risk. Bankers are trying to find the right blend of people and technology to outpace their competitors. Expect increased measurement of personal productivity where bankers can compare their productivity to peer much in the same way they have compared financial performance. There will be scorecards for each office to monitor productivity and performance. By carefully monitoring staffing needs, banks will do a better job of matching personnel supply with demand.

8. Managed Security Services Become Ubiquitous

As more bankers attempt to tackle security issues in a piecemeal fashion, they will discover that an enterprise-wide approach is required. Purchasing network security solutions is very easy, but implementing and maintaining network security solutions is quite difficult. Bankers will also discover that staffing network security 24/7 is not feasible for the typical bank, thus managed security services providers (MSSPs) will provide the around-the-clock monitoring necessary for quick response and peace of mind. Vulnerability scanning, intrusion detection/prevention, firewall monitoring, and

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"malware" (malicious software protection) are a few of the services bankers will rely on third parties to provide.

9. Payments System Continues to Evolve with Check Volumes Declining and Check 21 Slowly Gaining Traction

Check 21 became law on October 28, 2004, a day that came and went without much fanfare. While Check 21 didn't carry a huge impact in 2004, it will clearly increase check electronification and has started a domino effect that will dramatically change the check clearing process.

Technology will take a backseat to business process re-engineering as banks seek better methods to process checks such as least-cost routing. Imaging technology will be a key component, and bankers will evaluate network infrastructure opportunities and increased integration of imaging systems with the core. Image exchange remains voluntary. Larger players will benefit most from this trend. Standards are going to have to be set.

Bankers will struggle with keeping physical transportation of checks alive until this method is no longer needed. Accordingly, the per-unit costs associated with the physical transportation of checks will increase as check volumes decrease.

10. Government Will Get Bigger; the Compliance Burden Will Continue to Increase

Bankers are facing tough challenges as they attempt to balance security and compliance with consumer demand for more open environments and multiple delivery channels. Regulator satisfaction is competing with customer satisfaction. Customers want their banking services anywhere, anytime but safe and secure. Regulators want more controls, better corporate governance and documentation.

Key IT compliance issues facing bankers in 2005 include:

- Section 404 of the Sarbanes Oxley Act (for publicly-traded banks).
- USA Patriot Act (anti-money laundering).
- Gramm Leach Bliley Act (risk assessment, policies)
- More stringent IT examinations (wider scope, more frequent)
- An enterprise-wide approach to network security (strategically planning for security)

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Summary

New regulations, security threats, cost containment concerns, and productivity pressures will be offset by check processing efficiency gains, electronic transaction growth, community bank success, online activity increases, multi-channel integration, improved retail delivery and better IT risk management. 2005 begins with new challenges but bankers now have the technology to sustain competitive advantage and succeed in today's rapidly changing banking environment.

Sawyers & Jacobs LLC helps banks in four major areas: Technology Planning, Risk Management, Network Solutions, and Business Continuity. Our mission is ***to help our clients use technology securely, effectively, and profitably to better serve their customers, comply with laws and regulations, contain costs, and compete.*** To learn more, visit www.sawyersjacobs.com , call 901.487.2575, or email jsawyers@sawyersjacobs.com.

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