Progressive modernization:

a tech leader's blueprint for future-proofing banks

Using your technological roadmap as a path to profitability

As a tech leader in the banking industry, your highest priority is to leverage technology to drive business value. Technology has become the primary catalyst for gaining a competitive advantage and creating a strategic disruption in your sector — which means your technological roadmap *is* your roadmap to profitability.

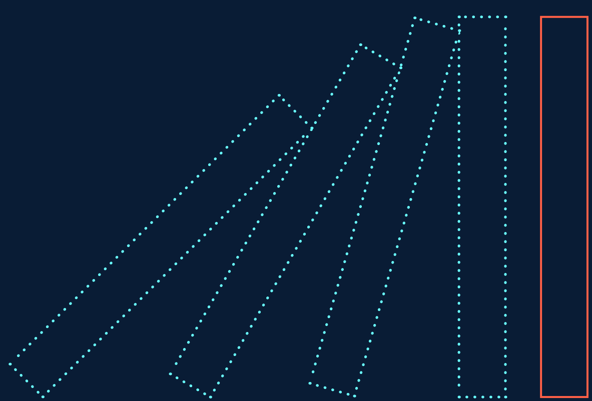
Yet a perplexing reality persists — a significant number of tech leaders in financial institutions are struggling to harness the full power of their technological arsenal and translate it into tangible business value. In fact, McKinsey estimates that, **on average, banks convert just five to ten cents of every dollar of tech spend into additional business value.**[1]

So why, in this era of immense technological prowess, do so many tech leaders find themselves caught in a quagmire of unfulfilled promises and unrealized potential? What's holding you back? Well, among other factors, technical debt.

[1] McKinsey & Company, "Unlocking the banking technology workforce," October 2021.

What is technical debt?

Technical debt is the tax you pay for integrating convenient, but less-than-ideal solutions into your operations. While these quick fixes may work out in the short term, you're borrowing against the future and will have to pay back the effort — with interest. That's because these fixes create a domino effect, compounding the complexity of your technology.



Essentially, it's an accumulation of the off-balance-sheet costs of all the work your IT department needs to do in the future. And it's complicating not only your day-to-day work, but also your ability to make an impact.

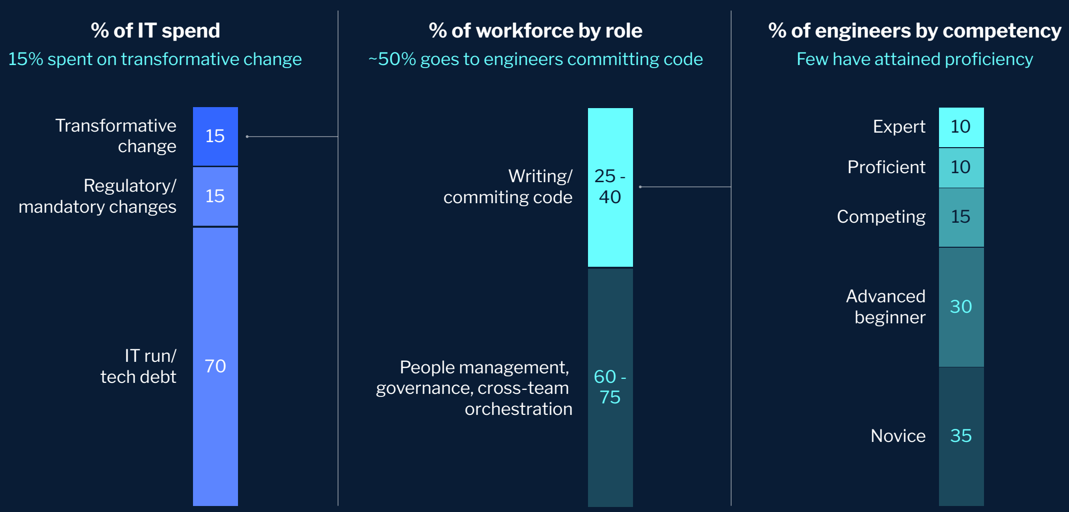
Technical debt compounds the work you have to do

Don't believe us yet? We get it, it's hard to understand the scope of the problem when it affects everything you do. But the numbers speak for themselves. Results from a McKinsey survey reveal that technical debt is:

01. Eating into your innovation budget
10-20% of the technology budget dedicated to new products is diverted to resolving issues related to tech debt.[2]

02. Increasing your total cost of ownership
Tech debt amounts to an estimated 20-40% of organizations' entire technology estate before depreciation.[3] For larger banks, this translates into hundreds of millions of dollars in unpaid debt. And things aren't improving.
In fact, 60% of the CIOs surveyed felt their organization's tech debt had risen over the past three years, but less than 20% of their annual budget was allocated to paying it down.

03. Increasing your time to value
Actively managing your tech debt could free up as much as 50% more time for engineers to spend on work that supports your business goals.[4]



Source: McKinsey Digital 2020 benchmarks; panel survey at McKinsey Digital Banking Conference 2021; McKinsey analysis

And, unfortunately, tech debt isn't the only challenge you face — it's just the most pressing. But you'll never begin to reduce your debt if you don't improve on the principal issue: legacy systems.

[2] McKinsey & Company, "Tech debt: Reclaiming tech equity," October 2020.
[3,4] Ibid.

Legacy systems are holding you hostage

Complex, monolithic legacy tech has long been the bedrock of many financial institutions, providing stability and continuity over decades. However, these same systems often become a double-edged sword, eventually leading to a plethora of technical problems that limit progress and innovation.

Let's take a look at the top three ways legacy systems are actively stifling your progress.

Manual software delivery and outdated development methodologies

Banks' legacy systems often lack automated deployment pipelines, continuous integration and delivery (CI/CD) capabilities, DevSecOps practices, and robust testing frameworks. That limits their agility, and the delivery of software updates and new features becomes a manual, time-consuming, and error-prone process.

Integration complexities and interoperability nightmares

When you combine legacy systems with new applications, third-party services, or emerging technologies, things quickly become complex. Without standardized interfaces and protocols, you'll end up having to deal with bespoke solutions and custom integrations that eventually become so unique to your bank, they're almost impossible to migrate during any modernization attempts. This creates even more technical debt, due to the difficulty of managing and maintaining a whole web of interconnected systems.

Low straight-through processing (STP) rates

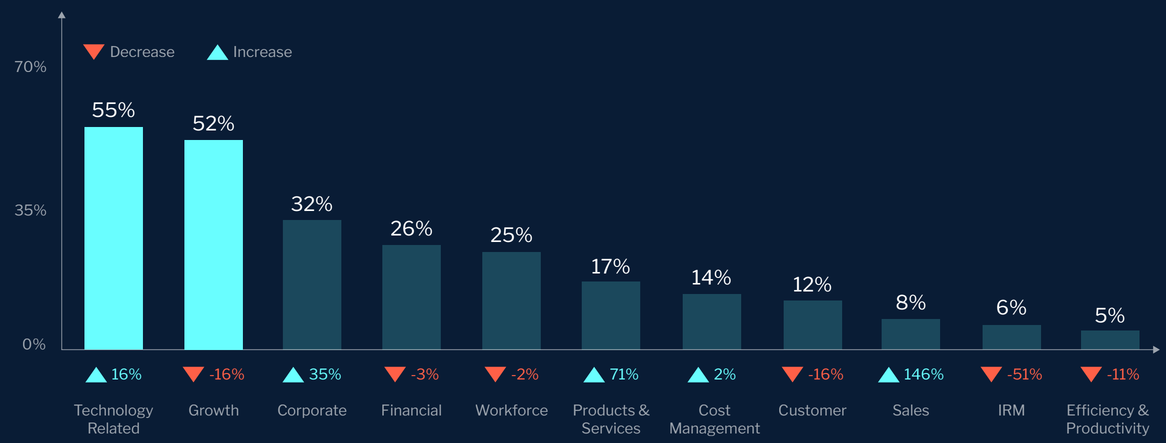
The complex, monolithic structures of legacy systems often lack the seamless integration and automation capabilities required for high STP rates. As a result, banks experience a high level of manual intervention and human touchpoints throughout various stages of transaction processing. And it gets worse: low STP rates limit your bank's ability to scale and handle increased transaction volumes efficiently. As you grow and your number of transactions rises, manual processing becomes a real bottleneck.

A once-in-a-generation opportunity

Imagine a future where agility becomes your competitive advantage, where data flows seamlessly, empowering you to make data-driven decisions with confidence. In this landscape, your customer experiences are elevated to new heights, bolstered by cutting-edge technology solutions that anticipate and exceed their needs. Naturally, your bank thrives as an industry leader, setting new benchmarks for success.

The path to this future lies in your hands. And it could be closer than you think.

According to Gartner, for the first time in a decade, CEOs and senior business executives in financial services are focusing on technology over top-line growth and profitability as a strategic business priority.[5] And within technology investments, the priorities are digitalization and transformation, with an emphasis on ensuring that customers and employees have flexible technology capabilities.



Source: Gartner, "2022 CEO Survey Insights for Financial Services Leaders: Technology Comes First", 2022

Gone are the days where IT is seen as a support function. Executive boards in financial institutions recognize that, today, technology is at the heart of every successful organization — and they're prepared to invest if it meets business goals.

[5] Gartner, "CEO and Senior Business Executive Survey: Financial Services," 2022.

Seize the day

To take advantage of this paradigm shift, you need to know where to start.

Every digital transformation journey is as unique as a snowflake, requiring considerations of differing tech stacks, partner ecosystems, end-user requirements, in-house tech capabilities, and the list goes on. So we're not going to sit here and tell you there's a "one-size-fits-all" solution that will solve all of your problems.

However, that doesn't mean you have to start from square one. Like McKinsey, we see three clear paths to hollowing out or decomposing your core, each with its pros and cons.[6] You just have to choose the best route for your bank.

01. Big bang replacement

When you started thinking about modernizing your tech infrastructure, your mind probably went to the "big bang" method. And that's natural, of course. This approach is flashy, bold, and sure to impress shareholders and customers alike.

By making a monolithic system update, financial institutions can overhaul their user interface, core systems, and integrations all at the same time. That's why the big bang option is a solid choice for banks with systems that are in urgent need of replacement — or, conversely, banks with a lot of time on their hands.

But when it comes to big bang replacements, financial institutions put themselves at considerable risk. For one thing, they're incredibly time consuming, meaning their solution may even be outdated by the time they launch. And don't overlook the resources required to even pull it off. This approach is by far the most expensive of the three options, and it requires a tremendous amount of dedication from your organization, in particular your in-house teams.

So take the big bang approach with a grain of salt. It's not all doom and gloom, of course. There's absolutely a time and place for this method, just like there's plenty of banks that would do well to select it. But most financial institutions don't have the time, resources, or risk appetite to do it justice — leading to inevitable failure, sometimes after years of work. And that makes a big bang a risky proposition.

[6] McKinsey & Company, "Next-gen Technology transformation in Financial Services," April 2020.

02. Greenfield approach

If you're primarily focused on speed and delivering value fast, the greenfield approach is the way to go. By reusing elements from your existing infrastructure, you can quickly create a cloud-native tech stack, saving you a significant amount of time and money. And on top of that, you can even eliminate the risk of disruption to your normal operations, and that's a powerful selling point. It's a medium-risk endeavor — and a medium-cost one — that prioritizes the speed of product innovation over the potential for data migration challenges.

But make no mistake, there are some real risks. As CCG Insights notes, the purpose of a greenfield approach is to test new tech and customer propositions, and that means there's always the possibility that it will fail entirely.[7] While some financial institutions may consider it a solid gamble, others may not welcome betting it all on a single project.

That's why this method is particularly useful in the case that a major bank wants to create a new offering or sub-brand, one that cuts out the legacy problems that have plagued them in the past. Like JPMorgan Chase and "Finn by Chase," these banks might not be as badly impacted by a bet gone wrong. But most financial institutions simply don't have that luxury.

At the end of the day, a greenfield approach is a solid strategy with a lot of positives, as well as a few negatives. In fact, some consultancies, such as Oliver Wyman, consider it the best choice for the average bank.[8] But — spoiler alert — we can think of one that's more appealing and even lower risk.

03. Progressive modernization

Progressive modernization is the middle-of-the-pack option that gives you medium speed and cost, but at significantly lower risk. Unlike the other approaches, progressive modernization is suitable for almost every bank. Does that make it the perfect approach for every bank? Of course not. Like we said, each transformation is a unique journey. But the pros vastly outweigh the cons, making it your best bet, pound for pound.

Sometimes called "journey-led progressive modernization," this method starts by identifying friction and transforming one journey at a time to improve, for example, the customer experience, employee productivity, and so forth. It's an end-to-end, modular process that saves you time and money, reduces complexity, and accelerates delivery. And on top of that, focusing on a single journey at a time anchors your bank's priorities firmly in the customer experience — an essential thing in the modern era of banking.

Of course, this is only possible after you've adopted a platform model, but with the right tech partner, this is much less daunting than you'd expect. By reimagining your operating model, you'll be poised to capitalize on your underlying capabilities, which will be made reusable and interoperable. Imagine a digital factory, composed of smaller, more skilled teams, all working together on a standardized architecture and automated infrastructure. That's the way you super-charge innovation.

[7] CCG Insights, "What Is a Greenfield Bank?" May 2021.
[8] Oliver Wyman, "Time to start again: how greenfield can transform corporate banking," 2019.

Next steps

Digital transformation is hard.

So hard, in fact, that many banks spend years kicking the idea around before market circumstances force them to act. And things don't get any easier in the meantime, as banking tech evolves rapidly. That's why the only way for your bank to truly differentiate itself from its competitors is through constant, incremental innovation.

As the old Chinese proverb goes, every journey starts with a single step, so start small and then iteratively build on the foundation you've created. Not only will you deliver an enhanced customer experience, you'll also future proof your operations at the same time.

But don't try to do things alone, no matter your resources, time limit, or risk appetite. Tech providers are standing by to assist you on your journey. They can help you cut out the guesswork and get to market fast with minimal cost. Just make sure you find a platform partner that strikes the right balance between customization and speed, helps your bank stand out from the crowd, and ultimately drives value for your business.

You're in the middle of a complex journey, no doubt. But if you can keep these things in mind, you'll significantly increase your digital transformation project's odds of success. And the impact you'll make? It will set the tone for your bank's future in the years to come. All you need to do is take that first step.

The Backbase Engagement Banking Platform

The open platform to rapidly modernize your bank

Backbase is here to give your financial institution the power to **break free from the constraints of legacy IT systems** and embrace an Engagement Banking model. With our **powerful whitelabel platform,** you can gradually replace — or even decompose — your disparate systems. And when you factor in over 400+ composable, pre-integrated capabilities, you'll gain the flexibility you need to rapidly modernize your digital channel infrastructure.

Another key to our process is our **unique "buy plus build" operating model,** which enables your bank to gain speed while standing out from the pack. By **buying and adopting out-of-the-box platform features** and adding them directly into your existing tech ecosystem, you'll be ready to deliver immediate value. Our platform can be adopted within your bank's existing polyglot landscape, enabling you to continue leveraging multiple programming languages and technology frameworks. And thanks to our **composable banking fabric,** your in-house developers and vendors will have the freedom to **create unique, differentiating value,** rather than reinventing the wheel by building basic functionalities from scratch. With all the right ingredients in place, you'll be able to reallocate your budget to change your bank, rather than just keeping the lights on

Harness the power of a **new-generation digital banking platform** for rapid innovation. The Backbase Engagement Banking Platform connects quickly and securely to your downstream systems of record, such as core systems and CRMs, as well as third-party fintechs in your tech stack. Our platform offers the **most comprehensive digital engine rooms** on the market today, enabling you to **seamlessly orchestrate all your customer and employee interactions** across any channel. The platform APIs empower you to **rapidly create differentiating user experiences** — so you can focus on delivering real business value.

Discover the power of an omnichannel platform, one that co-exists with your other techs, vendors, and banking standards, allowing you to **create hyper-efficient digital factory models and de-risk your transformation.** Together, we'll dismantle the barriers you're facing and help you **re-architect banking around your customers** — allowing you to lead the way in the future of finance.

Visit our website today to discover how the Backbase Engagement Banking Platform can help you meet your digital transformation goals.

About Backbase

Backbase is on a mission to re-architect banking around the customer.

We created the Backbase Engagement Banking Platform — a unified platform with the customer at the center, helping banks orchestrate seamless journeys across every stage of the customer lifecycle.

We make it simple for banks to orchestrate seamless customer journeys, all on a unified platform. From customer onboarding, to customer servicing, customer loyalty and loan origination, we help financial institutions surpass customers' expectations in every phase of the customer lifecycle. Built from the ground up with the customer at the heart, our Engagement Banking Platform easily plugs into existing core banking systems and comes pre-integrated with the latest fintechs so financial institutions can innovate at scale.

Industry analysts Forrester, Gartner, Celent, Omdia, and IDC continuously recognize Backbase's category leadership position. Over 150 financials around the world have embraced the Backbase Engagement Banking Platform - including Advanzia, Banco Caja Social, Banco de la Nación Perú, Bank of the Philippine Islands, Citizens Bank, ENT Credit Union, Greater Bank, HDFC, Judo Bank, KeyBank, National Bank of Bahrain, Navy Federal Credit Union, Natwest, Raiffeisen, SchoolsFirst Federal Credit Union, Standard Bank, Société Générale, TPBank, Washington State Employee Credit Union and Wildfire Credit Union.

Backbase is a privately owned fintech company, founded in 2003 in Amsterdam (global HQ), with regional offices in Atlanta (Americas HQ), New York, Boise, Mexico City, Toronto, London, Cardiff, Dubai, Kraków, Singapore, and Sydney.

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