Practical Considerations for Your Neo-Bank Strategy

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Introduction

The sky is not falling, but it is getting more cloudy.

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Some perspective...

- There is nothing Neo-Banks are offering today that almost any credit union can’t also offer their members.
- Many credit unions are *already* offering objectively better value than popular Neo-Bank and Challenger Bank startups.
- Credit unions are already pretty great at staying focused on understanding their members, which is the key to everything else.
- There are still some very important trends and changes you need to understand and develop a strategy for.

5 Steps...

1. Know your members
2. Know their preferences
3. Know how they choose FIs
4. Undertand how Neo-Banks acquire customers
5. Identify, analyze and borrow the best ideas

Know your members

Who are they today, and who will they be tomorrow?

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Who are your members today?

Looking at national membership demographics provides a great context for examining your own membership.

Latest credit union data and trends research compiled by **Elizabeth Rowe**, banking and payments strategist and *CU Insights* author.

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National credit union demographics

- Average member age is **47**
- 46% of those members are over **52**
- Credit union members are younger than those of community banks, but *significantly older* than the customers of top national and regional banks.

National credit union demographics

Relative to the general population, credit union members are more likely to:

- Be female (**55%** v 50%)
- Be married (**65%** v 47%)
- Have a college degree (**40%** v 24%)
- Be employed full time (**54%** v 39%)
- Own a home (**76%** v 52%)

Who are your members tomorrow?

20% of 18 to 24-year olds consider credit unions their primary financial institution.

Who are your members tomorrow?

By age **34**, *half* of them are now leaving credit unions for banks and other alternatives.

What's happening here?

What can account for this *50% attrition* as those members age from their early 20s to their early 30s?

Their financial lives are changing significantly in that time. They want to:

- Optimize the benefits of multiple financial relationships
- Pay off student loans
- Buy a home
- Invest and save for retirement, travel and big life events
- Get the best rewards-based credit cards
- Look for higher savings interest rates

What's happening here?

- They’re not seeing credit unions as being capable or sophisticated enough of providing the solutions their new challenges require (whether that's true or not).
- Explosion of new specialized products from Neo-Banks, Challenger Banks and other fintech startups now competing for these same consumers with hyper-targeted precision.
- These members are churning out of credit unions just as they enter their peak earning years.

Know their preferences

How do credit union members interact with FIs?

Interaction trends

- All credit union members are interacting with their FIs more frequently.
- For Millennials, Gen X and Baby Boomers, year-over-year transaction volumes are increasing between **15% and 20%**.
- What's driving this increase? Digital.

Digital vs Branch?

- **Mobile and online** are consumers' preferred channels (2018)
- Younger members use digital much more frequently than older members, and older members are much heavier users of branches.
- Most satisfied members are **branch-dependent digital users**.
- Second most-satisfied group are **digitally-dependent branch users**.
- Both groups value having and using digital and physical channel options for their interactions.

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Digital vs Branch?

- Even though they visit branches less frequently, three-quarters of millennials say they have been to a branch in the past three months.
- This aligns with credit union initiatives to maintain the relevancy of their branches (for the branch-dependent) while continuing to build out better digital products and services (for the digitally-dependent).

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Know how they choose

How do consumers shop for and evaluate FIs?

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What's the motivation?

Allowing for multiple responses, consumers say they choose FIs in this order:

1. Lowest fees
2. Presence of a local branch
3. Recommendations of family/friends
4. Reputation and interest rates (paid and charged)

Features-Motivated

- **42%** of members considered “features” motivated.
- Number one item of interest is having great online and mobile banking tools.
- Most likely to mention mobile tools, P2P payments and PFM as key tools in their financial services tool box.

Value-Motivated

- **28%** of members are considered "value" motivated.
- First and foremost looking for a "best overall value for the money."
- Only 16% of this group even mentioned online and mobile banking services.

Fee-Motivated

- 30% of members are considered "fee" motivated.
- Number one criterion for selecting an FI is "lowest monthly fees."

Shifting touchpoints

Significant shift underway. While no channel ever dies, the frequency of use by members changes over time.

Between 2012 and 2018:

- ATM usage is down to a few times a year.
- Branch visits continue trending down to just a few visits per year.
- Online usage is down from a few times per month to a few times per year.
- Mobile banking is up to almost a few times per month.
- Live agent support (phone) is up to a few times per year.

Understand how Neo-Banks acquire customers

How do digital-only FIs acquire and cross-sell customers?

Customer acquisition

There are multiple types of digital only players but their strategies share a key commonality:

They build market share and share-of-wallet *the same way* as traditional financial institutions.

Customer acquisition

Credit unions and banks use the checking account as the foundational relationship from which all other products and services are sold.

Digital FIs introduce themselves with whatever their initial niche product is, and that is their gateway to eventually cross-selling additional products and services to those they onboard.

Share-of-Wallet growth

While some are subsidiaries of major banks, investment banks or credit cards issuers, and others operate as stand-alone digital pure plays, in general they all:

1. Have an entry point product (investing, borrowing or deposits).
2. Leverage the customer knowledge gleaned from that product’s use.
3. Forecast and offer the next product that customer will want and how it will be used.

How big is the digital banking market?

Global Market Insights predicts that the market value of digital banking providers will increase from $7 trillion at year end 2018 to **$9 trillion in 2024**.

Over **75%** of the digital banking market is on the retail banking side of the business.

Identify, analyze and borrow the best ideas

Focus specifically on the startups, products and features most relevant to your membership.

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Examples

- How can your credit union "borrow" some of the best ideas?
- Which ones make the most sense for your membership (both today’s members and who you want to be your members in the future)?
- Where do you already offer a features, value or fee advantage?
- How could you re-position and/or modify your existing products, or go about developing and introducing new similar products?

Checking and Savings

- Digital-only checking accounts do not generally pay the super-premium interest rates of credit unions' high interest rates account, but neither do they require a monthly checklist to avoid incurring service charges.

- Credit unions hold the top spots for the interest rates paid by their high yield checking accounts. For members, the challenge for these accounts is that to qualify for the highest rate, the member has to jump through multiple hoops each and every month.

Checking and Savings

SIMPLE

- 2.02% APR interest on checking account balances .
- Combo checking account and Protected Savings Goal account.
- Savings account has a minimum balance of $2,000.
- Funds can be moved between the Goal account and checking account any number of times each month.
- No fees, array of mobile budgeting tools and free foreign ATM withdrawals.

Checking and Savings

- Free checking account with no overdraft fees and unlimited ATM fee reimbursement.
- 2.2% APR on savings account balances.
- 10% of the fees its customers choose to pay it are donated to charities.
- The interesting twist is that Aspiration is actually a securities brokerage and when customers are told deposits are FDIC insured, it’s because balances are swept into FDIC insured institutions each night.
- Balances actually held by Aspiration are protected by SPIC, as are all other account balances held by brokerages.

Investing

Betterment, Stash, Robinhood and Acorns and others offer EFTs or mutual funds through their automatic investing apps.

Each offers an extensive collection of investor education materials. Low fees are a key feature of the group with Robinhood a standout for offering $0 fee trades.

Investing

- Cornerstone advisors has found that half of all deposits into robo advisor accounts come straight from checking accounts.
- By 2020, these fintechs will manage assets between $2.2 trillion to $3.7 trillion and that is forecast to grow to $16 trillion by 2025.

Investing

- For credit unions, the suite of robo advisor investing apps is challenging.
- Credit unions want members to invest and grow the asset classes held by their households.
- Credit unions also want to own the primary relationship with their members and robo advisors are leveraging their core product into debit cards, retirement accounts and automatic savings programs.

Lending

- Digital lenders are spreading into each of the core revolving and installment credit relationship credit unions have with their members.

- Point of sale (POS) financing capitalized on a consumer need post-Global Recession.
- As credit card issuers pulled down their lines of credit and scaled back on card issuing, credit unions stepped in to fill some of that void by approving credit card applications from consumers who were low risk but ignored by the big banks.
- New breed of POS financing companies emerged to offer a non-credit card financing option to credit starved online shoppers.

Lending

- Klarna, Bread and Affirm appear as payment options at online merchants' checkout.
- Merchants can set a dollar level at which the POS lender will be offered (for instance, not for under $100 purchases)
- Consumers can set the length of time they need for repayment and the service is usually presented to the consumer as being free of charge or at low interest rates.
- Missed or late payment results in interest charges being back-billed to the date of purchase.

Klarna. Bread affirm

Recap

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Key Takeaways

- Imperative to continuously understand your membership and anticipate their needs better than ever before.
- Keep tabs on channel preferences and understand the three types of FI "shoppers" (features, value, fees).
- In many cases credit unions are already well-positioned to compete with some minor adjustments.

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Key Takeaways

Consider how you could offer:

- Innovative checking and savings accounts.
- Digital-only products, potentially leveraging a partner to manage the infrastructure for you.
- Investment accounts that are most appealing to younger members.
- Installment loans, even if done retroactively on a member's largest purchases.

Key Takeaways

You don’t always have to beat fintechs.

Strategic partnerships, and adding best-in-class features to your product roster provides your members with the safety and security they value in their credit unions, along with the apps and product mix they value.

Thank you

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