THE CAMBRIAN EXPLOSION

The Dawning of a New Era in Banking

ncino

“The Cambrian period, part of the Paleozoic era, produced the most intense burst of evolution ever known. The Cambrian Explosion saw an incredible diversity of life emerge, including many major animal groups alive today. Among them were the chordates, to which vertebrates (animals with backbones) such as humans belong.”

– **National Geographic**

Dear Reader,

The modern American banking industry has been in a constant state of evolution since it was forged in the Civil War's fire more than a century and a half ago. But constant doesn't mean steady.

A survey of history reveals four periods in which the evolutionary forces in banking hastened pace, each marking the start of a new era. The Civil War in the 1860s. The Great Depression of the 1930s. The twin energy and inflationary crises in the 1970s and 80s. And today. These are times of acute peril and opportunity for banks. To survive and prosper through them, one must understand the often-mercurial sources of upheaval as well as the competitive implications likely to emerge therefrom.

That's the point of this study. It offers a sober assessment informed by history and insights from many of America's most celebrated bankers about how the banking industry arrived at today, the dawn of a new era, and where it's likely to go from here. In doing so, we find that success in banking distills to the same forces that dictate success in evolutionary biology. The fittest prevail by capitalizing on random and unforeseeable events, like those brought about by the coronavirus pandemic of 2020.

Regards,

John Maxfield

John J. Maxfield

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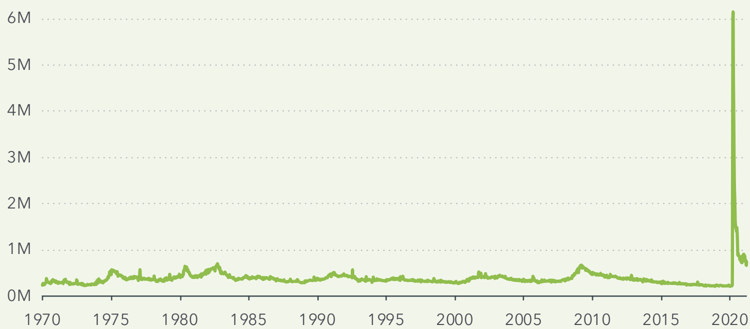
I. The Cambrian Explosion

The efforts to contain the spread of COVID-19 in March 2020 struck the U.S. economy so suddenly and with such violence that it effectively broke the y-axis of economic indicators for generations of chartists.

Nobody knows precisely where or when the novel coronavirus originated, but by the end of December 2019 it had begun spreading throughout Wuhan, a major industrial center and the largest city in Central China. It arrived in the United States two weeks later. And a week after that the World Health Organization issued a public health emergency for only the sixth time in the organization's history.

Weekly Initial Jobless Claims
Millions of applications, 1970–2021



Source: Federal Reserve Bank of St. Louis

It wasn't until the middle of March 2020, however, that the full force of the pandemic would broadside the U.S. economy. On March 11, the World Health Organization formally declared COVID-19 a pandemic, the National Basketball Association canceled the 2020 season and President Trump banned travel from Europe to the United States. Panic ensued. The S&P 500 fell 9.5% the following day and 12% four days later, the worst single-day declines since Black Monday in 1987.

The crisis quickly migrated from the markets to the economy, as states began issuing stay-at-home orders. More than three million people filed for unemployment benefits in the week ended March 21, and more than six million people did so the week after that, exceeding the previous record set in October 1982 by a factor of 10. By the middle of April, 44% of small businesses had either temporarily or permanently closed their doors. And by the end of the second quarter, U.S. gross domestic product had dropped at an annualized rate of 31.4%, three times further than the worst quarterly decline since World War II.

It seemed at first as if the banking industry would bear the brunt of the unfolding economic crisis, buried under a mountain of delinquent loans. The last time employment and output fell so far so fast – in the early years of the Great Depression – more than six thousand banks failed in five years. But that's not how it played out. Banks weathered the storm. Some even reported record earnings in 2020, buoyed by government aid. The industry had flown close to the sun, but unlike Icarus, its wings had not been singed.

Yet even though banks emerged largely unscathed from the pandemic, it'd be a mistake to dismiss the past year as an aberration in the evolution of banking. Just the opposite is true. Technologically speaking, it should be viewed as a wake-up call for the industry – its own Cambrian Explosion, a period 541 million years ago when evolutionary changes occurred at an unprecedented pace to spawn many of the complex biological lifeforms that exist today.

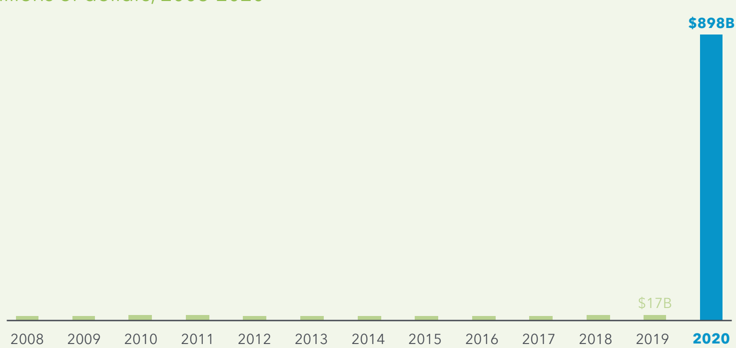
II. Shattering the invisible ceiling

The challenges presented by COVID-19 were unprecedented even for seasoned bankers like John Bugh, chief lending officer at Great Southern Bancorp, probably the most successful bank you've never heard of. If you rank every publicly traded bank in the United States by all-time total shareholder return – dividends plus share price appreciation – the $5.6 billion bank based in Springfield, Missouri, ranks sixth.

"I still remember there was a week in March where it just seemed to happen overnight," Bugh recalled months later, by which point he had been in banking for three decades. "It started with sports getting canceled, schools getting canceled, and then we had the lockdowns. So obviously anybody that was involved in any kind of retail establishment or hotel or restaurants, those folks, all of a sudden, their revenues went to zero."

A turning point came on March 27, when President Trump signed the CARES Act into law. The legislation included hundreds

Total Assets: Small Business Administration
Billions of dollars, 2008-2020



Source: SBA

"If I had to throw a plug-out to somebody, nCino's Bank Operating System was very, very helpful. It allowed us to track all the loans from start to finish, from application to funding, where it was in the system, if the application was complete, if it was sitting in our underwriting team, if we had gotten an SBA number, if we'd closed it, when we had to close it by."

– **John Bugh**
Chief lending officer of Great Southern Bancorp

of billions of dollars in support to small businesses under the Paycheck Protection Program, entitling those with fewer than 500 employees to forgivable loans backed by the Small Business Administration to cover payroll and other expenses.

On the first Saturday after the CARES Act became law, Storey called his counterpart at DocuSign, a pioneer of eSignature technology. "We went from putting our toe in the water – 'Yeah, we're kind of interested in DocuSign, but we won't do any commercial documents using it' – to closing 1600-plus PPP loans in 45 days, all signed via DocuSign."

It was emblematic of a larger trend. DocuSign gained 303,000 new customers in 2020, driven largely by financial institutions trying to expedite the PPP process. At one of the biggest banks in the country, the eSignature company facilitated the origination of over half a million applications for PPP loans, 75% of which were signed in less than 24 hours.

Top 20 Publicly Traded Banks

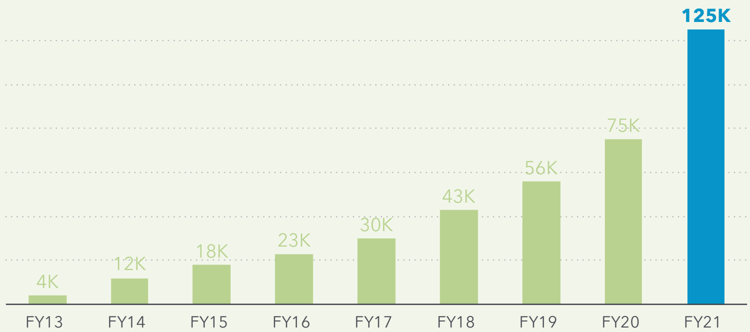
Ranked by all-time total shareholder return

Rank	Bank	All-Time Total Returns
1	SVB Financial Group	55,142%
2	Glacier Bancorp	54,224%
3	M&T Bank	33,709%
4	PNC Financial Services Group	23,639%
5	Fifth Third Bancorp	23,552%
6	Great Southern Bancorp	16,204%
7	Washington Federal	15,875%
8	Synovus Financial	15,376%
9	Arrow Financial	15,295%
10	Wells Fargo	13,011%
11	U.S. Bancorp	12,305%
12	Truist Financial	9,463%
13	CVB Financial	8,997%
14	Commerce Bancshares	8,971%
15	Comerica	8,827%
16	Westamerica Bancorp	8,416%
17	Hingham Institution for Savings	7,524%
18	People's United Financial	7,430%
19	JPMorgan Chase	7,388%
20	First Financial Bankshares	7,284%

Source: YCharts.com

By the end of 2020, the SBA had approved more loans in a single year – by both value and volume – than it had in every year combined since the agency was founded in 1953, including $525 billion in forgivable PPP loans made to more than five million small businesses and nonprofits.

DocuSign's Enterprise & Commercial Customers
Fiscal Year 2013 - Fiscal Year 2021



Source: DocuSign

In just the first six weeks of the PPP process, Great Southern closed twice as many loans as it closed in all of 2019 utilizing technology like DocuSign and the nCino Bank Operating System. "People here really appreciate nCino – what it's done for us," noted Bugh. "It got brought up several times during the PPP process that, 'man, thankfully we had nCino.'" It was baptism by fire. Phones were ringing off the hook. Executives worked alongside employees to process loan applications. A team of newly hired credit analysts did nothing but input data into the SBA's approval portal.

"If I had to throw a plug-out to somebody," said Bugh, "nCino's bank operating system was very, very helpful. It allowed us to

"The year 2020 underscored the importance of connection – connection with family, friends, coworkers, and even strangers. We adapted how we lived and worked, and we relied on technology more than ever before to remain connected with one another."

– **Joe Turner**
CEO of Great Southern Bancorp

track all the loans from start to finish, from application to funding, where it was in the system, if the application was complete, if it was sitting in our underwriting team, if we had gotten an SBA number, if we'd closed it, when we had to close it by."

The lesson for Great Southern was clear. "When your volume increases like that overnight, in order to meet the needs of our customers, you can't be relying on antiquated processes," said Ryan Storey, the bank's director of loan operations. "You need a streamlined process and the technology to support it."

"The pandemic forced us to move quickly and get across a boundary," Storey continued. "I don't think we will go backwards. Those loans are good, those signatures are valid, the software is in place. We saw that we can do this and break through that invisible ceiling that had been put in place over the years."

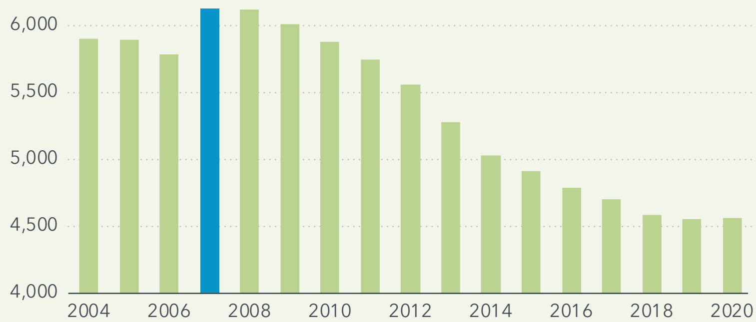
III. The digital imperative

Banks had spent the decades leading up to the coronavirus pandemic constructing and combining vast physical distribution networks. And no one did it better than Bank of America, the nation's second biggest bank by assets. Starting in 1960, the Charlotte, North Carolina-based bank began assembling what would eventually become the first coast-to-coast branch network in the United States.

By 2007, Bank of America's footprint of 6,149 branches covered more than 82% of the U.S. population and 44% of the country's wealthy households. It was a powerful competitive advantage. But that year also marked the beginning of the decline of branch banking. Over the next twelve years, the now $2.9 trillion bank would close nearly a third of its financial centers.

Bank of America's Branch Count

The year 2007 was the highwater mark



Source: Bank of America

It isn't a coincidence that the iPhone was born in 2007. Within three years, Bank of America had 6.3 million mobile users. And by 2019, the number would grow to 29 million, equating to roughly 44% of the bank's total customer base.

Nevertheless, by 2017, digital adoption rates had begun to plateau. Digital deposits at Bank of America climbed incrementally from 75% of total deposits in 2017 to 79% in 2019. Over the same period, its digital sales increased just one percentage point a year, from 30% of total sales in the fourth quarter of 2017 to 32% in the fourth quarter of 2019.

Then the coronavirus struck.

Digital deposits at Bank of America surged to 86% of total deposits by the fourth quarter of 2020, while sales made over digital channels climbed 13 percentage points to 45%.

"Our investments in digital client interfaces across our client groups allowed us to maintain a close relationship with our clients, as they moved seamlessly to digital check deposits, payments, banking and investing."

– **Brian Moynihan**
Chairman and CEO, Bank of America

It’s the same story across a myriad of other metrics:

- Bank of America added over 1 million new mobile check deposit users in the three months ended December 31, 2020, 22% of which were baby boomers or seniors who had been traditionally reluctant to engage digitally.

- There were 2.3 billion digital logins over the same stretch, equating to a year-over-year increase of 20%.

- And average digital logins per user in the fourth quarter of 2020 was up 14% at Bank of America, while logins by its Merrill Lynch wealth management clients doubled relative to the fourth quarter of 2019.

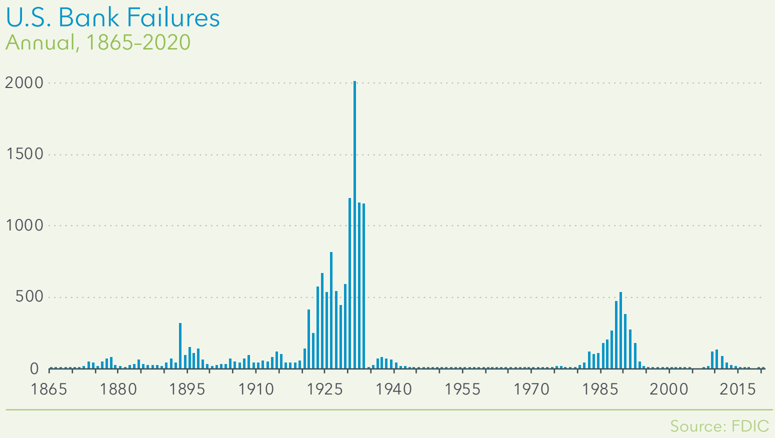
By the end of 2020, mobile and online banking was no longer merely an alternative distribution channel favored by Millennials; it became, for all intents and purposes, the sole channel through which businesses and consumers, irrespective of generation or personal preference, could engage with banks.

IV. Dawning of a new era

It's tempting to look at the digital transformation of banking and attribute its provenance to technology. After all, it was the iPhone's introduction in 2007 that made mobile banking possible in the first place. But this conflates cause and effect. Indeed, while technology is the medium of the ongoing transformation, the impetus for the transformation is older and more structural in nature. It dates back to 1973.

In October of that year, the Organization of Petroleum Exporting Countries (OPEC) enacted an embargo on oil exports to the United States in response to the country's support of Israel in the Yom Kippur War. The decision unleashed a series of forces that molded the next 35 years of banking, as high energy prices triggered rapid inflation which led the Federal Reserve to raise short-term interest rates to a peak of 19% in 1981.

The Federal Reserve's response was effective, though it also sparked a trio of calamities for financial institutions. The Savings & Loan Crisis struck first, as thrifts found themselves in the untenable position of paying twice as much on deposits as they earned on their portfolios of residential mortgages. A crisis across the energy belt struck next, maiming banks in Texas, Oklahoma and Louisiana after oil prices reversed course in 1980. Finally, commercial real estate prices collapsed in the late 1980s, sparking bank failures throughout New England, the Southwest and California.



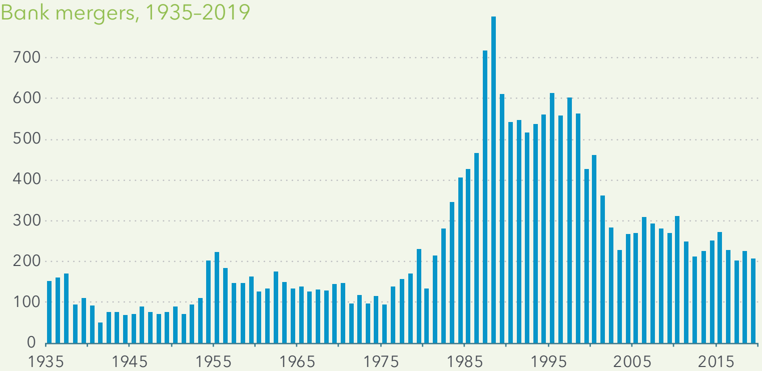
It was the darkest time in banking since the Great Depression. More than 2,900 banks were seized by the Federal Deposit Insurance Corporation from 1980 to 1993, an average of more than 200 failures a year.

But there was an upside. Like plants nourished in the ashes of a forest fire, the banks that survived the carnage spent the next three decades benefiting from policy changes enacted to assuage the crises. Congress phased out interest-rate ceilings on deposits, empowered thrifts to make commercial loans and banks to make adjustable-rate mortgages, and, most importantly, in 1994, mirroring previously passed state statutes, Congress repealed the federal prohibition against branch and interstate banking.

An explosion of mergers and acquisitions ensued. In the nearly 30 years from the end of World War II to the energy crisis in 1973, an average of 116 bank mergers took place each year, largely among community banks within the same state. The pace tripled in the mid-1980s as states entered into regional banking compacts with their neighbors, enabling the growth of regional banks. And by 1995, the year federal restrictions on interstate banking were officially repealed, the number of mergers increased fivefold to 608.

The Era of Consolidation

Bank mergers, 1935–2019



Source: FDIC's Historical Bank Data

The population of banks in the United States was cut in half between 1973 and 2008, while those at the top amassed a dominant share of the financial services market. At the beginning of the era, in 1973, not a single bank boasted more than $250 billion in assets. By the end, around the time of the 2008-09 financial crisis, there were six, accounting for 43% of the industry's total assets. The three biggest banks – JPMorgan Chase, Bank of America and Wells Fargo – each controlled roughly 10% of domestic deposits, a critical threshold that disqualified them under federal law from acquiring additional depository institutions.

Deregulation combined with consolidation were two of three pillars that defined the era. By the end, the most avid consolidators could no longer consolidate. And even among those who could, the pool of potential acquisition targets was a fraction of its former size.

The third pillar was the decades-long decline in interest rates since their peak in 1981. By 2004, the fed funds rate had dropped to 1%, the lowest level since 1958. Four years later, in response to the financial crisis of 2008-09, it would fall to 0%. From there, rates could only go up, turning a 30-year tailwind in the banking industry into a headwind of indefinite duration.

Effective Fed Funds Rate
1955–2021

Source: Federal Reserve Bank of St. Louis

The writing was on the wall: A new era in banking had arrived. To survive and prosper in the years ahead, banks had to radically rethink their approach to business. And the solution, many of them concluded, would be found in technology.

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The Dawning of a New Era in Banking

"There is no better teacher than history in determining the future."

– Charlie Munger

A dozen years ago, the U.S. banking industry entered a new era – its fourth since the industry's birth in the National Banking Acts of 1863 and 1864. The keys to growth and value creation in each era have evolved. To succeed through them has demanded an appreciation for the fundamental forces that define the distinct periods of time. Today is no different. As became clear in the COVID-19 crisis of 2020 – the banking industry's Cambrian Explosion – the keys to banking in the fourth era lay in digitally driven organic growth and value creation.

I. The Early Years: 1863-1945

Laissez-faire regulations combined with rapid economic growth yielded an era of frequent crises in which prudence was the key to survival, which, in turn, was the key to success.

II. The Great Moderation: 1945-1973

Risk aversion and heightened regulations from the Great Depression rewarded patience, prudence and opportunistic growth during the second era – the Great Moderation.

III. The Golden Era: 1973-2008

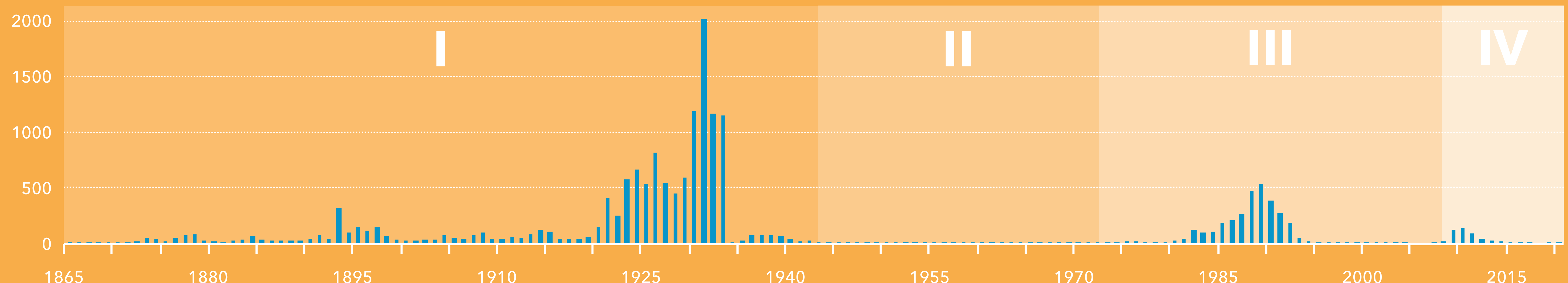
Declining interest rates, frequent banking crises and broad-based deregulation yielded favorable lending margins and rapid consolidation into large branch networks.

IV. The Digital Era: 2008-

Low interest rates, re-regulation in the financial crisis of 2008-09, a well-seasoned consolidation cycle and the proliferation of mobile banking now favor digitally driven organic growth and value creation.

The Four Eras of Modern American Banking

Bank failures, 1865–2020



Source: FDIC

V. Leapfrogging into the future

By 2006, it would have been tempting for Washington Federal to rest on its laurels. The then $9 billion bank had been one of the most efficient and profitable financial institutions in America for two decades, translating into an immense amount of value for shareholders. Today, it ranks seventh among publicly traded banks by all-time total shareholder return, just behind Great Southern Bancorp. It's this incredible success that makes WaFd's decision in 2006 so remarkable. That was the year it decided to rethink its entire approach to banking.

WaFd traces its origins to the founding of Ballard Savings and Loan in a northern suburb of Seattle, Washington, in 1917. It has since changed its name and charter, merged with competitors, acquired other banks, expanded into a total of eight Western states, and, following the 2008 failure of crosstown rival Washington Mutual, been crowned as the biggest bank based in the state of Washington.

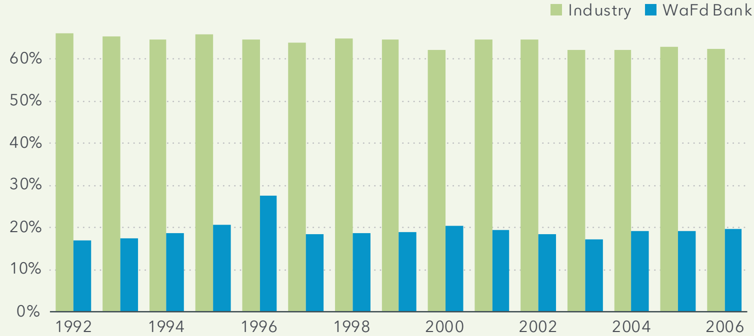
The principal explanation for WaFd's success is its long reign as the king of efficiency. From 1992 to 2006, its efficiency ratio averaged just 19.4%. That compares to 64.1% for the typical bank over the same period.

Pinching pennies wasn't an art at WaFd; it was an obsession. When Beardall joined as controller in 2001, entries in the ledger of the bank's holding company were still made by hand in oversized paper tablets. Typewriters sat on most desks. And to check email, executives had to leave their offices, walk to a central terminal in the middle of the executive suite, and log into an account shared by the entire floor.

"We were unbelievably lean, and we did very few things but did them really well," Beardall explained. "We took in deposits in the form of CDs and lent the money out in home and apartment loans. We did that over and over and over again. We had no ATMs. We barely had checking accounts. We believed that all those complexities added all kinds of costs."

Washington Federal: The King of Efficiency

WaFd's efficiency ratio vs. industry average, 1992–2006



Source: FDIC's Statistics on Depository Institutions

WaFd's lean, monoline model was tailor-made for the falling-rate environment of the 1980s and 90s. Seventy percent of its loans were 15- to 30-year fixed-rate residential mortgages. Meanwhile, most of its funding came from time deposits that matured in 12 months or less. As a result, by the early 1990s, WaFd's net interest margin had expanded to more than 5.2% while similarly sized banks netted closer to 3.9% on their earning assets.

"Small and mid-size banks are getting hammered right now. Look at deposits, they're flowing to the big banks. And now you look at the lending side, and the same thing is happening between fintech and the big banks."

– **Brent Beardall**
CEO of Washington Federal

But then came the paradigm change, when last era of banking gave way to the current one.

After the technology bubble burst in 2000, followed shortly thereafter by the terrorist attacks on September 11, 2001, the Federal Reserve dropped interest rates to the lowest level since the recession in the early 1960s. By 2003, the fed funds rate dipped below 1%. Five years later, it fell to 0%. Rates could go in only one direction from there: up.

The implications for WaFd were dire. In the years to come, as the yield on its loan portfolio remained relatively static, its cost of funds would invariably rise, flipping the bank's competitive advantage on its head.

Making matters worse, as digital banking gained momentum after the 2008 financial crisis, the competitive gap began to widen between the banks with the biggest technology budgets and everyone else. "Small and mid-size banks are getting hammered right now," Beardall noted a few years ago. "Look at deposits, they're flowing to the big banks. And now you look at the lending side, and the same thing is happening between fintech and the big banks."

There was only one path forward: "If we wanted a long-term franchise, we needed to invest," Beardall and his colleagues concluded.

So they rethought their approach to efficiency. "There are two ways to drive efficiency, through cost containment or revenue growth," Beardall explained. "What we've come to realize is that if it's only cost containment, heck, you can run a 25% efficiency ratio for the next three years, but have no business left over after doing that. It's like squeezing a turnip as hard as you can until there's nothing left."

The typewriters had to go; WaFd set its sights on leapfrogging into the future. Its new approach would be rooted in technology investments like nCino's Bank Operating System, which helped financial institutions like WaFd process over 1 million PPP applications for over $100 billion in government-backed loans.

"Historically our recipe for success was based on relationships and the strength of our balance sheet," Beardall said. "Both have served us well, and we're not going away from either of them. But if we can add technology that makes you go, 'Wow. That was easy,' then we win. We absolutely can take market share because the big banks can't have the same quality of relationships with customers."

VI. Keys to success in the new era

It has never been easy to acquire new customers and earn an economic profit – earnings that exceed the cost of capital – in an industry as competitive and commoditized as banking. But it's harder today than ever. "Banks have already been going through a bit of an if you want to call it an existential crisis, pre-pandemic," explained Chris Scislowicz, managing director of financial services at Accenture. "What the pandemic has done is it's changed the rules."

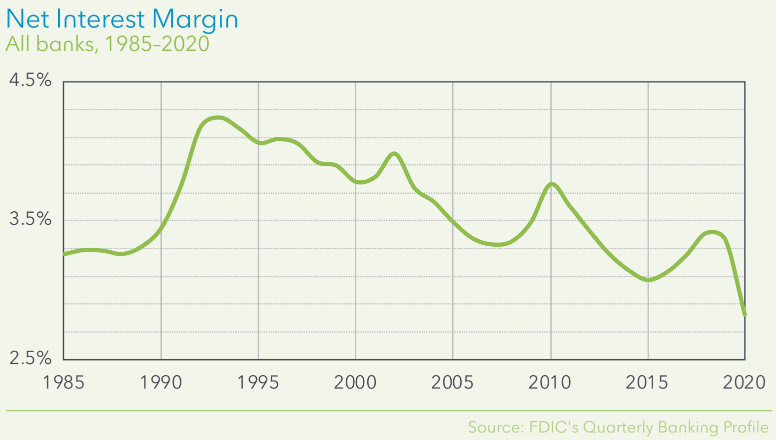
The decades-long decline in interest rates is over. Deregulation has given way to re-regulation. And the nation's biggest banks, shut out from making acquisitions, have turned to organic growth powered by digital distribution channels.

What does this mean for the future of banking? What will it take to succeed in this environment? Certainly, there will be many paths to success. But underlying all of them lies a new approach to three imperatives: efficiency, growth and the decision-making process.

1. Efficiency

"No one wakes up and thinks, 'I'm going to go to the office and be careless with shareholders' money today,'" Patrick Gaughen, president and chief operating officer of Hingham Institution for Savings, recently explained to *Bank Director* magazine. "That's more of an evolved discipline, a series of small choices you make over time."

By the end of 2020, spurred by the Federal Reserve's decision to drop interest rates in response to the COVID-19 crisis, the industry-wide net interest margin had dropped to 2.68%. At that



rate, excluding credit-related costs and benefits, the typical bank will earn just 0.84% on its assets – well below the typical bank's cost of capital.

The efficiency ratio is one of the few levers a bank can use to offset this, either by driving costs lower, pushing revenues higher, or, ideally, by a combination of the two.

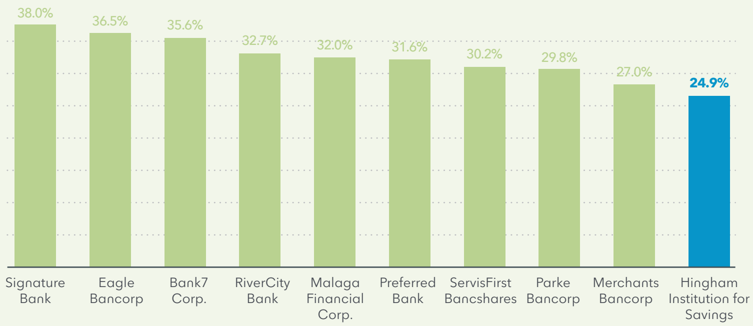
Hingham Institution for Savings offers a case in point. The $2.8 billion bank based near Boston is the most efficient publicly traded bank in the country, with an efficiency ratio of 25% in 2020. The secret to Hingham's success is that it keeps things simple. It specializes in commercial lending and avoids high-cost business lines like investment management.

But a bank cannot cut its way to prosperity by focusing exclusively on the numerator in the efficiency ratio. The key is to simultaneously drive revenue as well by leveraging technology to automate the back office while extending one's reach via digital distribution channels.

"You have dynamics around technology today which I think are incredibly positive," Gaughen observed. "You've gone from a situation in which there are relatively few technology providers where the cost of entry was very high, to a situation where, despite everyone's complaints about the primary core providers, there are a lot more options for integrating technology into your operations either to improve the customer's experience or to do business more efficiently."

10 Most Efficient Publicly Traded Banks

Efficiency ratio



Source: S&P's Capital IQ

2. Growth

Technology will also play an increasingly central role in a bank's ability to grow. The former era of rapid, often indiscriminate consolidation spanning 1973-2008 has given way to a more measured and calculated approach that's focused inward.

The biggest banks, as already noted, are limited exclusively to organic growth catalyzed by digital distribution channels. And even among large regional banks, which can still grow through acquisition, there's an appreciation that digital channels offer the preferred route to expand.

"Fundamentally, to acquire a customer 20 years ago, what did you need?" asked U.S. Bancorp Chairman and CEO, Andy Cecere. "You needed a physical presence. Today you don't necessarily need the same level of physical presence and you can still acquire a customer. Seventy percent of transactions happen digitally. So if you have really good digital capabilities, you can acquire a digital footprint, as opposed to a physical footprint, with much fewer branches."

It's been a strategy that's worked well for U.S. Bancorp, which has doubled its assets over the past decade without completing a major acquisition.

The Virtues of Organic Growth

U.S. Bancorp's total assets, 1990–2020

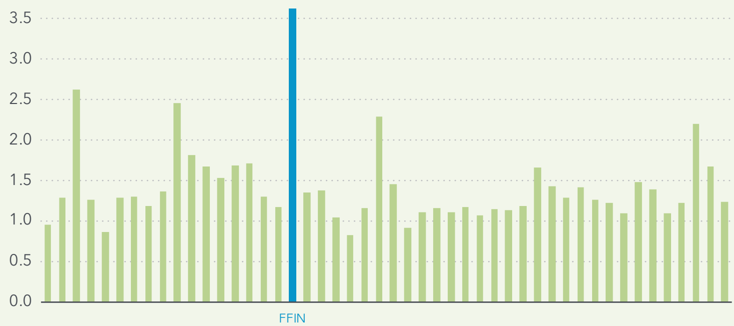
Source: S&P's Capital IQ

And, of course, while the opportunities to consolidate are still present for smaller regional and community banks, it's only a matter of time before that's no longer a viable option. The arithmetic is inescapable. There are a third as many banks today as there were in 1984. And if the industry continues to consolidate at its traditional pace of roughly 4% a year, it won't be long before the population is cut in half again.

3. Decision-making

A few years ago, First Financial Bankshares, a $10.9 billion bank based in Abilene, Texas, was searching for ways to take its customer service to the next level. Its answer was to bring in Horst Schulze, the co-founder and former president of the Ritz-Carlton Hotel Company.

Price to Book Value Ratio
KBW Regional Banking Index, Five-Year Average (2016–2020)



Source: YCharts.com

First Financial is *the* bank in West Texas, holding nearly half of all deposits in Abilene. For the past six years, it's also been the most highly valued bank on the KBW Regional Banking Index. If it were a car, it would be a Bentley. Still, the bank's chairman and CEO, Scott Dueser, wanted to take it to the next level.

Early on, Schulze shared a story with Dueser about room service and, specifically, the decision-making process that helped to resolve it.

When the first Ritz-Carlton Hotel opened in the Buckhead section of Atlanta in the mid-1980s, the number one complaint from guests was slow room service, particularly in the morning. The company promised to deliver meals within 30 minutes of ordering but was falling short. Schulze convened a working group of employees across departments – the order taker, cook, busboy, food runner and others. The problem, they discovered, was the elevator. The food runner often waited up to 15 minutes for the service elevator to arrive. The group stationed one of its members on a stool in the elevator to figure out what was going on. That's when they discovered the issue.

"A good decision-making process involves having the right people in the room with all information fully shared."

– **Jamie Dimon**
Chairman and CEO of JPMorgan Chase

At one point, the person who supplies the maids on each floor with sheets and towels got into the elevator. He got out on the next floor, put a wooden block in the door so it wouldn't close, then stepped out to gather the linens. He repeated this on each floor. The issue, they realized, had nothing to do with room service. The issue was that the hotel, in an effort to contain costs, had only two sets of linens per bed – one on the bed, the other in the laundry. They needed a third set, one that was in transit.

The takeaway for First Financial wasn't about linens; it was instead about the decision-making process that Schulze had employed to improve the speed of room service.

"When I talked to Horst about issues we were having, he would say, 'Hey, you need to put a tiger team on that.' That's when you've got a problem in the bank and something isn't right, and you put a team of people from different areas on it to find out why it isn't right."

– Scott Dueser
Chairman and CEO of First Financial Bankshares

"When I talked to Horst about issues we were having, he would say, 'Hey, you need to put a tiger team on that,'" Dueser recalled. "That's when you've got a problem in the bank and something isn't right, and you put a team of people from different areas on it to find out why it isn't right."

Nowadays, it's known as agile decision-making. And it's all the rage in banking right now for good reason.

“We’ve had to fairly radically change the way we work in order to keep up with the pace of customer expectations,” Tim Welsh, vice chairman of consumer and business banking at U.S. Bancorp, explained not long before the pandemic struck. They’ve done so by introducing cross-functional, fully dedicated, co-located, and largely autonomous teams that include not only product people, but also legal, risk and compliance folks — reconfiguring a vertical chain of command into a horizontal one that’s constantly being fed customer feedback.

“What’s critical about this is they are not asking me to make decisions for them,” Welsh continued. “They are empowered to make the decisions themselves. When you have fully dedicated co-located teams that are empowered to make decisions and getting constant customer input, you can get things done at a much, much more rapid pace than we have historically done.”

The moral of the story is that, while banks will always need to be prudent and patient when assessing credit risk, they also need to make way for a flatter and more streamlined decision-making process that accounts for the accelerating pace of change in an increasingly digital world.

VII. Conclusion

While it's often said that banks and bankers are reluctant to change, the facts tell a different story. The median community bank in the United States based on age is 100 years old this year. And one of the country's oldest banks – The Bank of New York Mellon – was founded more than 200 years ago by Alexander Hamilton. Institutions that are incapable of evolving don't survive that long, much less thousands of them.

Yet, even taking the past two centuries of banking into consideration, it's fair to say that this time is different.

The modern American banking industry has entered a new era – its fourth era. It's an era of tight margins, evaporating external growth opportunities and customers who have become acclimated to conducting their affairs digitally. The banks that embrace these realities will be those that continue to grow and create value for their customers, employees and shareholders.

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