



UNTANGLING THE FLOW OF DISRUPTION:



Geeks relate to the novel entitled *The Innovator's Dilemma* by Harvard professor Clayton Christensen because it gives them a backbone for the virtue of disruption. The theory is that well established companies tend to underrate small competition. The top brass

usually concentrates on expensive products targeted to existing customers. However, there could well be cheaper products out there that low-end customers would gladly embrace. Innovative products will always enter the market via the side door and eventually the high-end customers will also buy in. An example is how mainframe computer technology experts didn't see mini computers coming and history repeated itself when mini computer specialists trivialized the advent of personal computers, which have now been disrupted by smartphones.

The system of disruption thrives on mass appeal. Eric Schmidt, chairman of Alphabet, the parent company of Google, is a subscriber to the disruptive approach.

In the banking industry, there are also seeds of disruption. Financial geeks are ready to defy the mindset of well-tailored executives in corporate empires, all with the blessing of Silicon Valley. Fintech start-ups abound and bankers are feeling pressure to change their business model too.

More and more customers are using more and more technology, so if only community bankers could get their core providers to offer the same. These notoriously slow innovators (core systems that is) are holding up the opportunity for community banks and giving larger banks more of an edge when it comes to capturing new customers and retaining existing ones.

Financial technology or fintech companies are abundant. There are tech companies that offer products that alert users when fees are charged by banks or other financial entities; online lending portals; financial decision-making tools; robotic wealth management; online crypto-currency payments systems; wearable security; biometrics; mobile payments; ecommerce payments; and hundreds and hundreds more. It seems nearly everyone wants to eliminate banks these days by taking everything online into an unregulated world far from the reach of banking regulators. Heck, you can even make payments to other people using easily hacked email and no one seems to really care.

We wonder where all this will go and how long it will take to get there. Regulators seem to be waking up quickly to the fact that once financial activities leave the banking world they are unlikely to come back. The Fed needs to control movement of money, interest rates and other things so at the very least we wonder how they can raise interest rates on emailed money outside the system. Imagine the future intricacies our financial system will absorb and where it could eventually end up and your mind can quickly get tired.

For community bankers we think the best move is to bring in the sales rep from your core system provider. Grill them on what technology they have now and what they expect to launch next year. We say this because 4 core providers control everything really in community banking technology, so what they offer will

dictate what you can offer. Basically, anything that touches a customer eventually touches the core, so what they have is what you get. Keep asking, call every so often and check in now and again with other banks to see what they are doing.

Finally, keep talking to customers as you enhance your website, empower your sales teams with technology and try your level best to stay in front of your customers and on top of the technology wave. Doing so is tough, but if you can figure things out along the way even incremental movement is positive.

ECONOMY & RATES:

Yesterday: Oil prices rebounded from a six-year low and Treasuries plunged, raising yields 10bps, as investors remain anxious over the upcoming rate decision.

BANK NEWS:

• **Not Productive:** Newsweek reports the average American wastes 55 minutes per day looking for things they own but can't find. Meanwhile, OrganizedWorld reports the average office employee spends 1.5 hours per day just looking for things and Forbes finds the typical executive wastes 150 hours per year searching for lost information.

• **Millennials:** A Bank of America survey of millennials finds: 33% say the Great Recession affected them personally; 50% say it made it difficult to find a job and changed how they think about saving, investing and spending; and only 21% of millennial small business owners say their companies have fully recovered from the recession.

• **Energy Stress:** The Financial Times reports the head of corporate banking at Wells Fargo is warning of stresses in its energy portfolio related to the ongoing decline in oil. The bank is reportedly talking to clients about saving cash as it reduces undrawn borrower loan limits by an average of up to 20%.

• **Oil Prices:** Oil prices have now declined so far they are getting very close to 11Y lows.

• **High Rent:** CNN reports a study by Harvard University finds people who spend more than 30% of income on rent (cost burdened) has risen to 21.3mm people. Of those, 26% spend more than 50% of their income on rent (severely cost burdened). This could be an ongoing issue when you consider 37% of households rented last year, the highest level in 45Ys.

• **Regulatory Warning:** The OCC indicates its exam teams have seen credit risk rising for retail and commercial loan products over the past 3Ys and projects that will continue in 2016. The regulator points to easing underwriting standards due to increased competition as the primary issue. The OCC warns underwriting trends are "very similar to those that examiners reported just prior to the most recent financial crisis." Bankers take heed to avoid regulatory issues.

Tsy Yields	MTD Chg	YTD Chg	LIBOR Sw ap	Expected FF	
3M 0.20	+0.04	+0.17	1M 0.34	31-Dec 0.22	
6M 0.49	+0.11	+0.38	3M 0.52	31-Mar 0.39	
1Y 0.67	+0.19	+0.46	6M 0.75	30-Jun 0.51	
2Y 0.94	+0.01	+0.28	1Y 1.06	30-Sep 0.62	
5Y 1.65	+0.01	+0.00	2Y 1.02	30-Dec 0.78	
10Y 2.22	+0.02	+0.05	5Y 1.61	31-Mar 0.91	
30Y 2.95	-0.02	+0.20	10Y 2.12	30-Jun 1.04	
FF Market	FF Target	Fed Disc	Prime	Unemployment	Oil
0.14	0.25	0.75	3.25	5.00	36.31



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