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Andy Cecere and
Richard Davis at
U.S. Bank Stadium

With U.S. Bancorp's leadership transition underway, the big question is whether it will deliver faster earnings growth — the one shareholder demand that has proven elusive

Inside handoff

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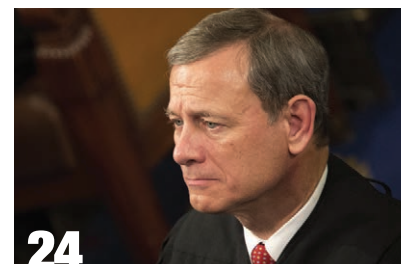
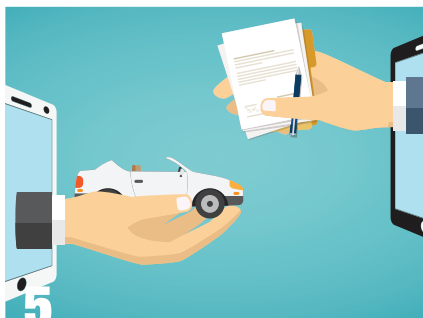


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Andy Cecere takes over in a tricky period for U.S. Bancorp. Its shares trade at a significant premium compared with most of its peers. But the pressure is on to accelerate earnings growth. Can he deliver on the one shareholder demand that has proven elusive even for Richard Davis to achieve?

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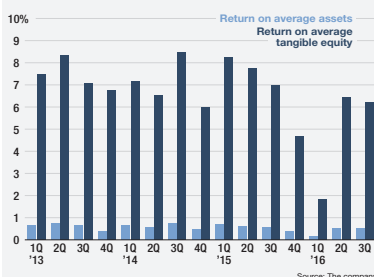
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BBVA Compass' new core platform promised to make it a better bank, but returns since the late 2012 rollout have sputtered



Source: The company

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AMERICAN BANKER

Volume 127, No. 3

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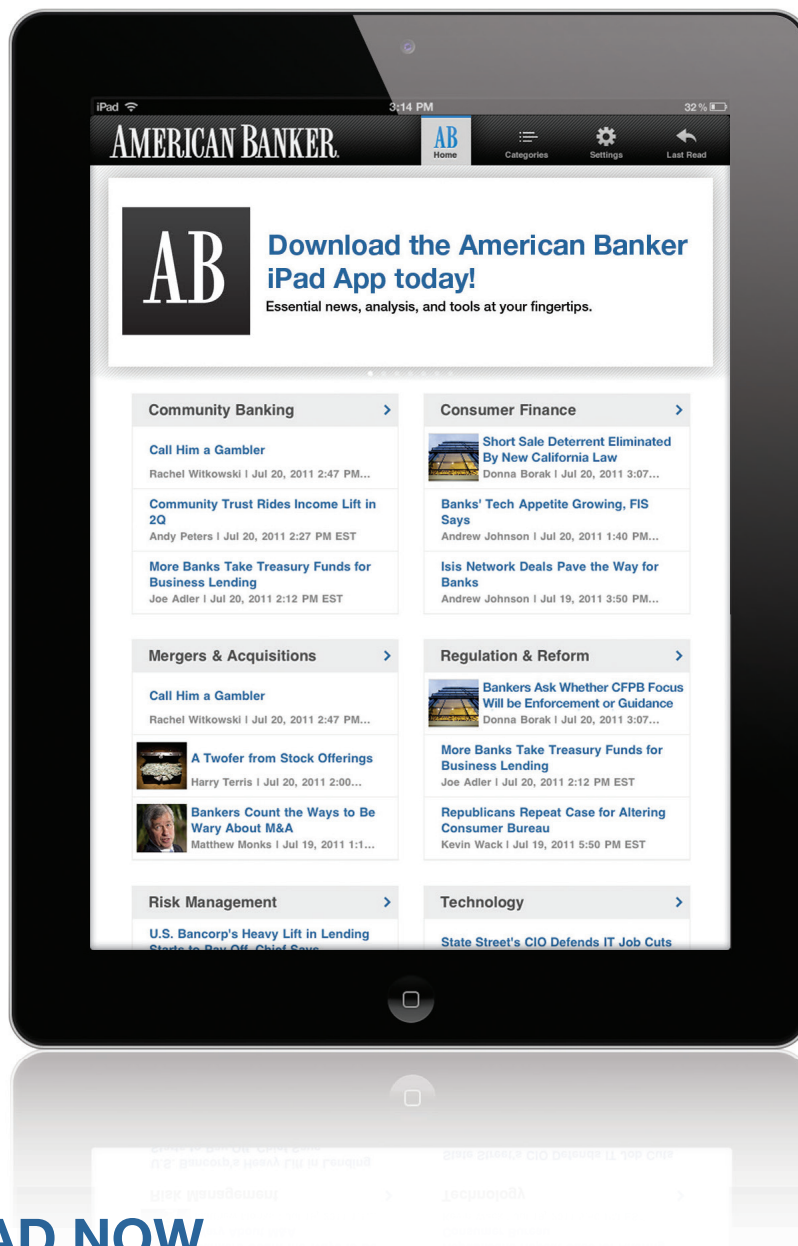
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Editor's Note

BY BONNIE McGEER

Make Sure Your Digital Strategy Creates Value

Bankers are no longer thinking about *whether* to build new and better ways of doing business; rather they are puzzling over exactly *how* to do so.

A lot of projects so far have been about keeping up with customer expectations. But at most that just helps maintain value. Going beyond that is essential to gain a competitive advantage and create value.

So as the industry undergoes a digital transformation – and fintech challengers encroach – make choices about where and how your bank can best compete in this evolving ecosystem, then invest accordingly. The point is to create a digital strategy that fuels shareholder equity, said John Lester, a partner at Oliver Wyman and co-author of a new report that addresses this topic.

“I think the real question CEOs should be asking, and I’m sure are beginning to be asked is, ‘What is the value we’re getting from all of these digital initiatives?’ And I think for too many incumbents, the answer is, ‘Not a lot so far,’ ” Lester said in a video discussing the report. “What we’re exploring is a way to reorganize and rethink the way you do digital transformation so that you actually drive towards value directly, in a systematic way.”

Digitizing all aspects of the businesses generally results in spending a lot and doing nothing really well. Instead, the report, titled “The State of the Financial Services Industry 2017: Transforming for Future Value,” suggests picking one of three business models as a way to help define goals and choose technology best suited to add value.

In the first model, “demand aggregators” provide a frictionless experience that helps customers with all aspects of filling a particular need, like buying a car. This might entail partnering with other providers to offer services the bank doesn’t.

The report cites USAA’s Auto Circle as an example. Over the past five years, USAA went from simply providing auto finance and insurance to assisting customers through the entire car-shopping process. It partnered with the comparison website TrueCar to allow customers to shop for and purchase cars online.

Car shoppers spend most of their time deciding what to buy, then often take whatever loan the dealer offers during the purchase. By inserting itself into the process as customers compare cars, and offering financing and insurance options in real time, USAA set itself up as a preferred provider, the report said. Since the launch of Auto Circle, USAA’s penetration of its customer base for auto loans has more than doubled.

In the second model, “platform providers” that already process massive amounts of transactions leverage those capabilities on behalf of other companies. Platform providers earn fees, so the more interactions they facilitate between customers and product providers, the better.

The report listed Uber, Airbnb and eBay as examples. Within the financial services sector, payments networks and stock exchanges are both platform providers.

A lesser-known example that the report cited is Goldman Sachs’ Marquee platform, which launched in 2013 to provide access to the global investment bank’s proprietary

analytics. In particular, a structured debt instruments marketplace called SIMON connects brokers seeking debt solutions with banks that issue them.

Offering competitors’ products through SIMON might seem risky, but the strategy has been paying off, with Goldman rising from fourth to first in structured note issuance over the last three years, according to the report.

In the third model, “component suppliers” focus on being the best in what they offer. They invest in consumer insight to design new products and retool existing ones, and plug into as many potential customer experiences as possible, including nontraditional ones, the report said. Low cost, low cycle time and specialized expertise are all important here.

Salesforce.com is one example. It offers automated plug-and-play sales and marketing tools via the cloud and incorporates established technology, including Amazon Web Services, Slack and Microsoft’s email platform, the report said. As such it covers the whole sales and marketing spectrum, rather than just one component, making it more compelling.

Strategic approach aside, going digital is essential to serving millennials, who are less likely to adopt current products, and less likely to acquire products through established distribution models, the report warned.

But regardless of target audience, the key is to focus on providing value to people’s lives, rather than getting caught up in the next big technology craze. And choosing where to invest starts with knowing your own value proposition. □

Briefings

AUTO LOANS | COMPENSATION | COMMERCIAL BANKING



Auto Finance Shifts Into the Digital Age

Ford offers car shoppers a way to buy online and set their own loan terms

By Kevin Wack

THE TRADITIONAL CAR-SHOPPING EXPERIENCE – visiting showrooms, negotiating a price and enduring long waits in a windowless office – is widely loathed. Yet it has endured, even at a time when consumers can buy nearly anything else online in minutes.

There are numerous reasons why. A car is a big purchase. It typically involves multiple transactions, including a loan. An auto dealer, a lender and the carmaker all have roles, adding layers

of complexity.

But in one recent sign that change is coming, Ford Motor Credit announced that it is enabling shoppers to buy vehicles and finance their purchases online.

The Dearborn, Mich., automaker's financing arm is starting with a single Ford dealer in Ohio, but it plans to roll the program out to more locations over time. The idea is to offer U.S. car shoppers – who spend an average of 10 hours researching their purchases online, according to an Ernst & Young report from 2015 – the option of transacting from the comfort of their own homes.

Last fall, Mercedes-Benz's financing arm also began allowing car buyers to arrange financing through a mobile app.

Lee Jelenic, director of mobility at

Ford Motor Credit, said the auto industry must adapt to consumers' changing expectations. He cited research that found today's car buyers make an average of 1.6 visits to the dealership, compared with five visits a decade ago.

"We've seen a huge shift in consumer behavior," Jelenic said. "And we want to stay at the forefront of that."

As part of that effort, Ford Motor Credit is partnering with a two-year-old startup called AutoFi, which has developed a platform for financing automobile purchases online. That platform will be integrated into Ford dealers' websites. Ford Motor Credit also made an undisclosed financial investment in San Francisco-based AutoFi.

Under the partnership, consumers who want to shop online will have the option of customizing their own loan terms. For example, if customers want to make bigger down payments, in order to reduce the amount they owe each month, they will have that choice.

"We put the consumer in charge of constructing their own deal, versus having the dealer do that for them," said Kevin Singerman, AutoFi's chief executive.

Initially, consumers will only see financing offers from Ford Motor Credit. But over time, AutoFi's goal is to present up to three offers from various lenders that the dealer has chosen to put on the network, Singerman said.

The option to transact remotely gives consumers more control than they have had until now. Traditionally, when a car buyer arranges financing, auto dealers shop among a variety of lenders, but they do not share all of the information with the customer.

For traditional lenders, this new reality may present an opportunity or a competitive threat, depending on how quickly they can adapt to the market changes.

"What consumers are increasingly looking for is to be the ones that are in command of the transaction," said Roberto Hernandez, a partner in the consumer finance practice at PwC.

In recent years, some companies, including the electric car maker Tesla, have sought to eliminate middlemen from the car-buying process.

By contrast, Ford Motor Credit and AutoFi are keeping U.S. auto dealers at the center of their business plans. Over time, the industry's shift toward e-commerce could yield substantial benefits for auto dealers, as they may be able to operate with fewer employees.

Hernandez envisions a future in which many consumers opt to arrange financing online before they ever step foot in the dealership.

An Indication On Incentives

Rivals relieved as Wells Fargo retains incentive pay

THE REVISED PAY PLAN THAT WELLS Fargo adopted in the wake of its phony-accounts scandal is not as radical as some other banks feared it could be.

Banks large and small had been waiting anxiously to see how regulators' expectations would change after Wells disclosed that employees had opened millions of unauthorized accounts over a period of years. The worry was that the San Francisco bank, on a short leash with its regulators, would eliminate performance-based pay, putting pressure on other banks to follow suit.

Wells is keeping many details under wraps, but the revised plan appears to align the \$1.9 trillion-asset company more closely with the rest of the industry, consultants said. Notably, the new plan does not get rid of incentive pay, which has long been a staple of compensation plans in retail banking.

"I think the construct was not that radical, and I'm happy that it wasn't," said Darryl Demos, an executive vice president at Novantas. "They could have easily overreacted."

In September, shortly after Wells was penalized, the Office of the Comptroller of the Currency announced a review of sales practices at all of the large and midsize banks it supervises. So the OCC apparently did not object to Wells' new compensation plan, which should ease the industry's fears of a major shift in regulatory expectations.

Here are three other takeaways from Wells' new pay plan.

- **The plan should make employee misconduct less common and easier to detect.**

The new plan eliminates sales quotas, which were blamed for creating a pressure-cooker environment in which widespread sales abuses took place. It also leans more heavily on salary, as opposed to performance-based bonuses. The company said that for tellers, base pay will account for more than 95% of all compensation.

In addition, there is greater emphasis on the performance of an entire branch, as opposed to individual employees. For entry-level bankers, incentive pay will be based entirely on team performance, the company said. For most other positions, the majority of the opportunity for incentive pay will be based on team performance.

Those changes reduce the motivation for employees to cheat.

"As a rule, team measures are much less of a risk for those kinds of bad behaviors," said Mark Blessington, a sales and marketing consultant in Asheville, N.C.

Wells also said that it will be doing more proactive monitoring to ferret out bad behavior, including new oversight at the regional and corporate levels. These steps should protect against the possibility that branch-level employees will get away with breaking the rules because their managers are looking the other way.

- **Wells is trying hard to hold onto its top-performing employees.**

Given the reputational damage caused

by the scandal, Wells already had an employee morale problem.

Now the tilt toward a heavier reliance on base pay could mean a pay cut for those retail bankers who account for an outsized share of the company's sales. So retail banking chief Mary Mack has another reason to worry that her most productive employees might look for new jobs.

Wells did not release enough information to determine how big the pay cuts could be, but Chief Financial Officer John Shrewsberry said in an interview that Mack was cognizant of employee retention as she was designing the new pay plan. "Mary believes that she's got the tools to retain the highest-performing people," Shrewsberry said. "She thinks

that she's captured the ability to reward, attract and retain the best talent."

Wells spokeswoman Mary Eshet said that the company's new compensation plan limits the amount of incentive pay that can be earned in most retail banking positions. But she also maintained that the plan provides competitive earning opportunities.

- **Questions remain about some of the new metrics that Wells will use to calculate incentive pay.**

Under its old pay plan, Wells provided a sales credit to its retail banking employees regardless of whether the customer ever used the product. That gave employees an incentive to open unauthorized accounts that might never be used.

The revised plan bases incentive pay partly on how much a customer uses Wells products. It also looks at whether customer balances grow over time.

"It's not about how many accounts have you opened, how many new products or solutions have you sold. But rather, it's about attracting new primary customer relationships to the bank," Shrewsberry said.

Those changes drew mixed reviews from outside observers.

Demos, the Novantas consultant, said that it makes sense to emphasize customers' product use, as opposed to just sales, in an incentive pay formula. "This one approach, if they'd put that in place, might have kept them out of hot water," he said.

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But Jay Freeman, a former Wells executive who was involved in formulating incentive pay at the company, expressed skepticism about basing a branch employee's incentive pay on how frequently customers use products, or whether their account balances grow over time.

"I'm not sure exactly what a branch employee does to impact this metric," Freeman said. "Wells needs to be clear what it is they are asking people to do or they will get random activities and behavior across the branches as individuals try to sort this question out for themselves."

— Kevin Wack

Commercial Cleaning

Regional banks unload risky commercial loans

BANKS ARE SCRUBBING THEIR commercial loan books, ditching high-risk borrowers before the industry's nearly pristine credit quality takes a turn for the worse.

During the fourth quarter, regional banks such as Fifth Third Bancorp and Regions Financial cut back on some riskier commercial lending, including energy-related credits and leveraged loans to heavily indebted companies.

Fifth Third said it unloaded \$3.5 billion in commercial loans in 2016, including about \$1.2 billion in the fourth quarter. Executives cited concerns about the quality of the borrowers and whether the company was being adequately compensated for the risk it was taking.

Analysts describe the moves as prudent. Credit quality across the industry remains strong, providing an opportune time to jettison the borrowers who could wreak havoc on balance sheets later on.

But the strategy nonetheless carried a short-term cost and curbed loan growth at a time when new revenue is hard to come by.

"We're trying to become the bank that we've communicated we want to be," Greg Carmichael, chief executive of the \$142 billion-asset Fifth Third, said in an interview. High-risk loans "tend to be falling trees in your backyard, so to speak, and create anomalies in your earnings."

Total loans at Fifth Third shrunk 1% from a year earlier to \$92.9 billion as the company pulled back on business lending. In the coming year the Cincinnati company plans to remove another \$1.5 billion in commercial loans from its books.

"It's the smart thing to do, in anticipation of whenever the next credit cycle comes," said Gerard Cassidy, an analyst with RBC Capital Markets.

Regions Financial in Birmingham, Ala., also reported a decline in total loans as it continues to scale back on its participation in shared national credits in cases where it does not already have a relationship with the borrowers.

Total loans at the \$126 billion-asset Regions fell 0.2% from the previous year to \$80.6 billion.

A few other big regionals, such as PNC Financial Services Group and BB&T, reported modest fourth-quarter loan growth.

During earnings conference calls, bank CEOs have said that optimism among business clients has increased following the Republican sweep in the elections and the rising momentum for tax cuts and deregulation. It remains to be seen if borrowing will ramp up in the months ahead and meet the bullish expectations for business loans.

Fifth Third and Regions have gone against the grain, making a concerted effort to shrink their commercial loan books.

Fifth Third began scaling back on risky commercial credits a year ago, ending relationships in a range of industries, including those that are dependent on commodities, according to Carmichael. The company also has scaled back on auto loans.

Carmichael, who became CEO in November 2015, said he means to position the company for the credit cycle in the years ahead and to increase profits.

In the past year, the company's average yield on interest-earning commercial and industrial assets increased 21 basis points to 3.33%.

"The big thing is that you have a new management team that is much more focused on improved profitability and lower risk throughout a credit cycle," said Peter Winter, an analyst with Wedbush Securities.

Winter noted that a spike in the benchmark London interbank offered rate helped Fifth Third exit high-risk relationships more quickly than expected. Higher rates on commercial loans during the fourth quarter encouraged some borrowers to pay down or refinance their loans too.

"The new management team is looking to smooth out earnings" after running into a slew of commercial credit problems after the financial crisis, Winter said.

In the year ahead, Fifth Third plans to expand its commercial loan book by 2% even as it pulls back from major credits. Total commercial loans were \$57.3 billion as of Dec. 31.

The company predicts strong growth in its specialty loan divisions, including for health care, telecommunications and leisure. Loans for manufacturing and automotive companies are also expected to grow, Carmichael said.

Fifth Third will continue to "take a pause" on commercial real estate loans, citing concerns that the market is overheating.

Analysts noted that now is an ideal time for Fifth Third to reposition its balance sheet given that credit quality remains strong. Net chargeoffs, for instance, declined 8% from a year earlier to \$73 million.

"There's nothing that destroys shareholder value more than bad credit," Cassidy said. — Kristin Broughton

BankTechnology



At the ‘Core’ of It, the Question Isn’t If, But When

Fearful banks hesitate on core conversions they need. But what’s more risky? Keeping legacy technology? Or finally replacing it?

By Bryan Yurcan

EXPENSE AND RISK HAS KEPT MANY U.S. banks from modernizing their core systems, but executives at one community bank that completed the project this past summer say they are happier for having done it.

Ultimately, Two Rivers Financial Group in Burlington, Iowa, decided that keeping an old system would end up adding too much expense and risk of its own, said Kent Gaudian, the president and chief executive officer.

Before making the big switch, “we were so focused on getting the system to work and spent so much time on that, we were not getting the job done for our customers,” Gaudian said.

Employees at its \$704 million-asset bank unit now have access to better tools that allow them to be more efficient. A customizable dashboard for each employee eliminates the need to do numerous searches related to daily tasks. A customer relationship management tool gives an overview of individual customers at a glance and tracks communication with them.

Two Rivers also opted for a system that enables a variety of prebuilt custom reports with visual views of data, replacing manual reports stored in Excel files.

Banks of all sizes can gain a competitive advantage by opting to replace their core, said Peter Wannemacher, a senior analyst with Forrester.

But this is especially true for smaller banks, because being tech-savvy is an effective way for them to stand out from competitors, said Wannemacher, citing Eastern Bank of Boston and Umpqua Bank in Portland, Ore., as examples.

“There’s a precedent for smaller banks that are willing to invest being able to punch above their weight,” he said.

Two Rivers’ bank unit went live in early August with a NuPoint core system from Computer Services Inc.

Its search for a new core vendor got underway in 2015, at the end of its contract with a previous vendor that Gaudian declined to name. It settled on CSI just before the new year.

Gaudian cited the data and analytics tools available with the cloud-based NuPoint core among the key selling points.

These allow Two Rivers to analyze each customer relationship and pursue cross-selling opportunities more effectively, he said. The bank can input “what-if” scenarios for a particular account or a group of them, to determine what loan opportunities best fit those customers, for example.

The system also decreases the time it takes to open new accounts by eliminating the need to rekey data multiple times.

Core conversions are relatively rare in the banking industry. Extrapolating from sales data, the research firm Celent estimates that about 2% of the top 1,000 banks opted to do core conversions in 2016. Among smaller banks, such as Two Rivers, the rate of core conversions is likely similar, said Stephen Greer, an analyst in Celent’s banking group.

“Banks always are reluctant to do core migrations because there is a substantial amount of risk,” he said. “You don’t want a scenario where you pull one string and then have some kind of reverberation in another place that you didn’t expect.”

For that reason, many banks simply

layer middleware on top of old legacy systems to add new functionality as needed – a quick fix instead of a long-term solution, Greer said.

Though a core replacement can be a highly involved project with many moving parts, Two Rivers and CSI simplified the process by breaking it into components and dedicating a specific team to each.

“We have anywhere from 15 to 30 people working with the bank, from data movers to staff trainers, support folks and relationship managers,” said Tim Thurman, vice president of implementation for CSI. “We spend a tremendous amount of time on site and have project status meetings throughout the process, usually once per week and then more frequently the last month before going live.”

Near the end of the project, CSI set up a “demo bank” so employees could practice on the new system.

Gaudian described the conversion – which took place on an August weekend – as “seamless.”

“I’ve been through several of these during my time [in banking],” he said. “There were a few hiccups – there always are – but nothing that impacted the customer. We came in on Monday and were up and running.”

He attributed the hiccups to the need for more customer communication rather than something technical. “Due to the call volume we received the first several days after the conversion, we now know we could have done a better job in informing our customers of expected changes,” he said.

The expense of replacing a core system can be daunting. Estimates are hard to come by and vary wildly based on the size of the bank and the type of system. But even a community bank can expect to spend millions of dollars.

Gaudian declined to discuss the cost of the project, saying only that not having to deal with glitches in legacy technology is enough to justify the investment.

CSI’s Thurman predicted that the

pace of core conversions will pick up as more banks get increasingly frustrated with legacy systems.

“There’s always a level of fear, especially when it comes to moving all the data,” he said. “But if a bank is having pain with their current system, then they become more motivated to look into it.”

Tech analysts have heard more bankers at least talk about modernizing core systems lately.

“In the last two years, compared with the 10 prior to that, the number of banks that have told me a core replacement is on their road map has certainly risen,” Wannemacher said.

But given the rapid pace of change in the industry, even the notion of modernizing core systems could become outdated over the next decade, he said.

“Looking 10, 15, 20 years down the road, what it even means to be a bank could drastically change,” he said. “When you look at concepts like banking-as-a-service and open banking, they may not operate in the same way. They may not need some of the functions a current core system provides.”

P2P Premiere

How the launch of Zelle will benefit from past mistakes

IN COMING MONTHS, THE LARGEST U.S. banks are expected to relaunch their person-to-person payments service with a new name, an easy-to-use mobile app and a slick ad campaign.

The revamped product is called Zelle – short for gazelle, the antelope species that can run as fast as 60 miles per hour. Its architects are promising not only real-time speed, but also unmatched security.

Zelle has the backing of JPMorgan Chase, Bank of America, Citigroup and Wells Fargo, along with regionals such as BB&T, Fifth Third Bancorp, U.S. Bancorp, Capital One Financial and PNC Financial Services Group. At its launch, the P2P

THEM

A manually manipulated writing and communications tool consisting of a solid carbon-based core mixed with a clay binder and encased in thin wood, usually hexagonal in section (but sometimes cylindrical), that creates marks through physical abrasion and is capped by an erasure and correction device made from natural rubber or styrene-butadiene.

US



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service will be available to 75 million mobile banking customers, according to its backers. That scale could potentially give the participating banks a big edge in a crowded payments marketplace.

Zelle has been dubbed the banking industry's "Venmo killer" – a reference to the PayPal-owned app that has soared in popularity, particularly among millennials. And the big banks have learned some important lessons from their earlier foray into P2P payments, which failed to capture the public's imagination.

But the large banks' advantages offer no guarantee of success. There are plenty of examples of deep-pocketed incumbents – from bookstores to video rental chains – flailing in their efforts to stave off nimbler upstarts.

Below is an analysis of the big banks' strategy.

Lessons learned

Perhaps the most important change that the banks are making involves branding. For years, the banks enabled person-to-person payments across a shared network – known inside the industry as clearXchange – but they marketed the service under different brand names.

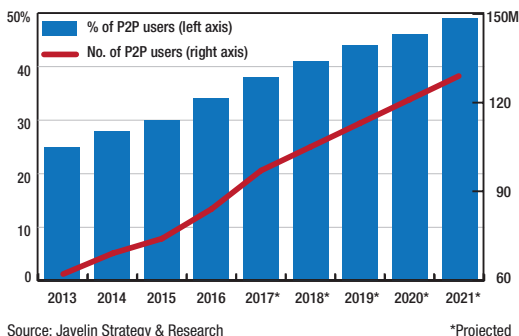
Chase called its version QuickPay; Wells Fargo, SurePay; and U.S. Bank, Send Money. Consumers could use these products to deliver cash to people with accounts at other banks, but that utility was not intuitively obvious.

The Zelle rebranding helps convey a simpler message. "With Zelle, consumers can use an email or a mobile number to send and receive payments," Paul Finch, the CEO of Early Warning Services, said at an October presentation. (Early Warning Services is the bank-owned company that developed the payment system.)

Zelle will be accessible from the banks' own mobile banking apps, as well as from a standalone app. Publicity for the service was expected to begin in February, with the launch to follow later.

Moving money

Nearly half of consumers will make person-to-person payments by 2021 via laptops, desktops or mobile devices



Industry participants are hoping that "Zelle" will catch on as a verb – similar to how many consumers today ask their friends to "Venmo" the amount of cash they owe.

"Don't underestimate the power of just having a simple brand," said Michael Abbott, who leads the digital financial services practice for North America at Accenture.

Ease of use is a priority for the banks too. Products that are hard for customers to find, or inconvenient to use, generally do not get much traction. That problem hobbled the previous generation of P2P payments offered by the big banks.

Last year, only 14 of the top 30 banks were offering person-to-person payments in their mobile banking apps, according to Javelin Strategy & Research. That number should rise in 2017.

Finally, the big banks appear to have learned an important lesson regarding pricing. In the past, some banks had insisted on charging for P2P payments. But few people are willing to pay a fee for the service, when they can use numerous other free options instead.

During a Jan. 13 conference call, PNC Chief Executive William Demchak said that the Pittsburgh-based company sees benefits from offering Zelle, even though its customers will not be paying fees to use the service. Specifically, he argued

that customers who become accustomed to using Zelle will be less likely to switch banks.

"It puts our consumers back in our hands," Demchak said. "It's not a revenue opportunity out of the gate as it relates to the product specifically. But I think it is another part of the customer relationship that makes it more sticky."

Challenges ahead

Still, there are important questions hanging over Zelle's debut.

One issue is whether the revamped payment network can fulfill its ambition of becoming something bigger than a way to split restaurant bills or pay the handyman.

In addition to person-to-person payments, the big banks have their eyes on the business-to-consumer market, as well as the business-to-business market. Zelle is being touted as a new way for insurance companies to pay out claims, or for companies to reimburse their employees for travel expenses. "It works the same for companies as consumers," Lou Anne Alexander, group president of payments at Early Warning Services, said during remarks at the Money 2020 conference in October. "This eliminates the hassle of paper-based payments."

Eventually, participating banks may be able to generate revenue from business uses of Zelle, though it is not clear how strong demand will be in the corporate world. "We are implementing B2B and B2C scenarios with several customers and look forward to announcing those relationships soon," Alexander said in an email.

Another unanswered question involves Zelle's ultimate reach.

Zelle is aiming to connect all 12,000 U.S. bank and credit unions – the holy grail for payment systems, because of the powerful network effects that stem from ubiquity. But it is not clear how many smaller institutions will choose to join a network owned by the big banks.

Of the 18 banks and credit unions listed as participants on Zelle's website, all but five have at least \$50 billion of assets. In January, the \$106 billion-asset BMO Harris Bank unveiled its own branded P2P payment app, opting not to use Zelle.

Zelle also could collide with other more sweeping efforts to modernize payments in the United States.

A task force convened by the nation's Federal Reserve banks is expected to release a report in mid-2017 evaluating 19 proposals to build a faster payments system. One of those proposals is from The Clearing House, which, like Zelle, is owned by the nation's largest banks.

In the meantime, Zelle is taking steps to extend its reach beyond customers of the banks that have signed on to the network. It has partnered with FIS, Fiserv and Jack Henry & Associates, giving smaller institutions that rely on those technology providers a way to plug into the P2P network. Zelle also will allow consumers who have Visa or Mastercard-branded debit cards to send and receive payments over the two major card networks' rails.

— Kevin Wack

But Can They Make Coffee?

Once banks get comfortable with them, bots will be working in every department

BANKS ARE ALREADY EXPERIMENTING with robotic process automation in areas like their compliance functions. But soon the technology could be used in nearly all aspects of running a bank.

As banks become more comfortable with relying on software robots to handle rote tasks, experts say they will be quick to deploy the technology companywide as a way to trim expenses and redirect employees to more crucial tasks.

"I think we're going to see it move from a few narrow functions to across the enterprise," said Alan McIntyre, the

industry managing director for banking at Accenture. "It's going to become an indispensable technology for banks, rather than an interesting experiment."

This could include areas in finance departments that are heavily manual, such as managing and clearing payments. Human resources and administrative functions also could benefit. For example, robots could take over payroll and managing employee incentive programs.

And even if robots don't fully run these departments, they can be used to assist human employees during periods of heavy workloads, said Alastair Bathgate, chief executive and co-founder of Blue Prism, a robotic process automation firm, which has partnered with Accenture to help financial services and other industries implement robotics.

Austria's Raiffeisen Bank International AG is among the first to work with Accenture and Blue Prism to automate various business functions. It is also in the process of creating an in-house robotics center dedicated to experimenting with how the technology can be used in different functions at the bank.

Raiffeisen started out implementing robotic process automation — or RPA for short — in four pilots where the tasks had low-to-medium complexity; rule-based processes with a logical order of steps, and repetitive patterns with clearly defined process options, said Markus Stanek, head of group efficiency management at the bank.

RPA is a tool best deployed like a surgical intervention, automating specific process steps, he said. A project can be implemented in just a couple of weeks.

The technology also has potential uses for consumer-facing functions, not just back-office automation. The most notable use thus far has been so-called robo-advisers, which use simple, rules-based models to choose investment vehicles for an investor after that person inputs basic information about their risk tolerance and investing goals. But beyond robo-advisers and even more com-

plicated wealth management services, the technology can be used to improve customer relationship management for banks, said Mark Schwanhausser, director of omnichannel financial services at Javelin Strategy & Research.

After a major event that affects the stock market (such as Brexit), a financial adviser might have 30 clients with questions about how this affects their portfolio. Calling all 30 would be time-consuming for one person. But using robotics, the adviser could send a message tailored to each individual telling them how the event affects their portfolio, along with a "click to call" button if they do want to talk to the adviser, said Schwanhausser.

Similar ideas can be used to enhance personal budgeting and financial management tools, he said. For example, when logging onto mobile banking, a customer could view personalized information on their progress toward meeting their financial goals with insights into their spending and saving habits.

"It can provide very personalized service," without any human interaction, Schwanhausser said.

Neither Schwanhausser nor McIntyre believes the human element will be removed from banking — just deployed in smarter ways.

"It is a move to automation, but it's a move to automation that complements the human element," Schwanhausser said. "You may not want to talk to someone every time you have any financial question; [robotics] can provide you with a lot of daily information you wouldn't have thought to ask for to begin with. If it just represents an interaction that never would have happened anyway, then it's not a threat to any employee."

Regardless of how it plays out, Schwanhausser said, the move to using robotics in financial services has already passed the point of no return.

"What you are seeing now is the beginning stages of what is going to increasingly become the norm," he said.

— Bryan Yurcan



New quarterback: Andy Cecere, left, is succeeding Richard Davis at a tricky time for U.S. Bancorp. Some investors say the Minneapolis company hasn't grown fast enough.



In the zone

WITH U.S. BANCORP'S LEADERSHIP TRANSITION UNDERWAY, THE BIG QUESTION IS WHETHER IT WILL DELIVER FASTER EARNINGS GROWTH — THE ONE SHAREHOLDER DEMAND THAT HAS PROVEN ELUSIVE

By John Engen
Photography by Thomas Strand

It's an unseasonably warm January night in Minneapolis as employees of U.S. Bancorp pack into U.S. Bank Stadium, the hometown Vikings' new \$1.1 billion playground, for the company's annual all-employee gathering. The brainchild of Chairman and Chief Executive Richard Davis, the event is in its 10th year, but this is the most emotional.

Two days earlier, the 58-year-old Davis surprised pretty much everyone by announcing that he'll be retiring as CEO in April. The \$446 billion-asset company has telegraphed the move for a while, promoting Davis' successor, Andy Cecere, to chief operating officer in 2015, and adding the title of president last year.

Even so, it's rare to see a guy so clearly at the top of his game stepping aside at such an early age. For the 8,000 Twin Cities-area employees in attendance (and 60,000 others watching live around the country), it's bittersweet.

One woman is wearing a pink T-shirt with the name "Richard Davis" printed in the center of a heart. Poster sticks with Davis' head are bobbing in the crowd and the line for selfies with the outgoing CEO constantly refills. Some employees are crying.



The rock-star treatment is understandable. With Davis at the helm, USB rode out the financial crisis better than any large bank, and today is near the top on most performance measures, including return on assets (1.36%), return on equity (13.4%) and efficiency ratio (54.9%).

He's also created a culture that is supremely confident in its capabilities and direction. Listening to the testimonials and war whoops from the crowd, it's evident employees are proud of their company. On stage, Cecere, a 56-year-old USB lifer, leads the tribute, declaring that Davis "is part of the fabric of our culture ... his legacy is our story."

The question is, can the low-key Cecere, with his more introverted, cerebral style, carry on that legacy and feel-good vibe as effectively as the high-energy Davis?

It's never easy replacing an icon, but most analysts and investors, including Warren Buffett, who owns 5% of the company's shares, have expressed comfort with the move. "I can't imagine a more seamless transition, even for a person as hard to replace as Richard Davis," said John McDonald, a senior research analyst with Sanford C. Bernstein.

Cecere was USB's chief financial officer for most of the past decade, and regularly appeared with Davis at investor conferences. "Andy embodies the same values as Richard about running the company for the good of all stakeholders," McDonald said. "Wall Street looks at them very much as a pair."

Within the company, the two walk in lockstep on strategy and direction, even if Cecere's more deliberative style lacks some of Davis' charisma and storytelling pizzazz.

"There aren't two Richards, and we can't get a rib and clone him. So

you have to pick somebody else," said David O'Maley, a 22-year member of USB's board and its lead director. "Andy is an extraordinarily good choice. He has great leadership skills and the confidence and trust of the board."

Cecere is taking over at a tricky time. USB's returns have its shares trading at more than 16 times earnings and around two times tangible book value, a significant premium to most other big banks. But the rap among some investors is that the company hasn't grown fast enough.

Davis, a fan of sports analogies, promised earlier this decade to get USB playing "more offense," but couldn't meet three-year growth targets set in 2013 in either its banking or powerhouse payments businesses. (USB's other major business, wealth management, hit its goals.)

In 2016, net income was almost exactly the same as the year before, while per-share earnings jumped a modest 2.5%. Consensus estimates peg per-share earnings growth at 4.6% in 2017.

"It's fair to say they have fallen short of expectations," McDonald said. "They invested in wealth management, payments and corporate- and middle-market bankers when other banks were fighting for their lives, and now it's time for them to show the offense that was talked about and outgrow their peers."

With interest rates on the rise and President Trump vowing to boost economic growth and cut back on regulations – all good things for banks – Cecere is under pressure to deliver better results.

"Investors have given them the benefit of the doubt, but they're getting impatient," said Scott Siefers, an analyst with Sandler O'Neill. "With the economy improving, USB needs to start generating more positive operating leverage."

OXOX

Sitting in a conference room several days after the employee event, Davis and Cecere joked easily about reaction to the leadership change. Cecere conceded that some of the attention (his enlarged head was on some of those poster sticks) was unnerving. "You get used to it," Davis deadpanned.

Neither seems fazed by all the talk about growth expectations. U.S. Bancorp has a well-earned reputation for conservatism, and is sometimes best defined by what it won't do – things management considers to be too risky, expensive, or simply wrong.

Last decade, USB famously sat out the subprime housing boom, which helped it emerge from the financial crisis as one of the industry's healthiest players and the nation's fifth-largest banking company.

Today, it has similarly pulled back from several hot sectors, including commercial real estate and auto lending, citing irrational competition.

"Right now, this very minute, there are banks all over the country doing crazy things with commercial real estate loans – 15 years, no recourse, stuff like that. They're making subprime auto loans, assuming the world will never get worse again. They're using nontraditional data that has never been tested over a cycle to underwrite," Davis said.

"It all feels like 15 years ago, very risky. So we're passing," he added. "And then people ask, 'Why were your commercial real estate loans flat last quarter when they went up everywhere else?' It's because we didn't see any loans we wanted to make."

A giant in the payments business (USB owns Elavon, the big processor), the company also has refused to get sucked into the credit card rewards wars because the

cost of winning would hurt profitability.

While analysts and traders might want management to stretch for growth, Davis insists USB's core shareholders care more about "consistent, predictable and repeatable" results, and appreciate that USB doesn't take unnecessary credit risks.

"The point is, culture is not something you mess with as circumstances change," said Davis, who will remain executive chairman to ease the transition. "You pick a course, own it and do the same thing going forward."

If falling a little short on growth targets is USB's biggest issue – and by all accounts, it is – then its executives have reason to stay the course. Banking has been under siege for most of the past decade, blamed for the financial crisis, engaged in constant battles with regulators and squandering customer trust.

USB has had a couple of scrapes with the Consumer Financial Protection Bureau. It also is still working through a 2015 consent order from the Office of the Comptroller of the Currency regarding deficiencies in its Bank Secrecy Act and anti-money-laundering compliance program – a challenge that is costing more than Davis would like and prevents the company from acquiring other banks.

But among the big banks, USB has been a pillar – a "Goldilocks" company that's not too big or too small and can be counted on to provide a steady return in good times or bad.

It has stayed on the high road too. In one recent example, Davis resisted suggestions that USB aggressively pursue customers of rival Wells Fargo after the damaging sales-practices scandal there.

"Not only are we not going to do anything about it, if I find out one of our bankers is out there trying to poach Wells

Fargo customers, I'll probably let them go," Davis recalled telling an investor who broached the topic last September.

It's not an altruistic point of view. "Nobody benefits from us pointing at each other and playing ugly playground games," especially when the industry has worked so hard to recover from its reputation problems, he said.

Over the years Davis has become one of the industry's most respected voices. He's met with former President Obama, sat on committees with former Federal Reserve Chairman Ben Bernanke and served on the boards of key organizations, such as the Financial Services Roundtable.

As chairman of the roundtable in 2010, Davis took the lead on efforts to restore the industry's post-crisis reputation and spearheaded a push for greater industry cooperation on cybersecurity issues. More recently, he's become a go-to source for Washington policymakers seeking an honest assessment of a proposal's impact.

His reputation even among competitors is stellar. "A lot of his colleagues refer to Richard as the best banker in the United States," said Tim Pawlenty, the roundtable's CEO.

In Minneapolis, the Los Angeles native's adopted hometown, Davis has been one of the business community's strongest voices and has served on nearly a dozen civic boards. He's currently chairman of the local economic development authority and the planning committee for the 2018 Super Bowl in Minneapolis.

Davis has brought that same civic-mindedness to USB itself. A program called Community Possible gives employees at least one day off each year to volunteer. When he asks how many in the Minneapolis crowd serve on the board of

a community group, hundreds of hands shoot up. "I'm warning you, as a banker they'll always ask you to be treasurer," Davis joked.

OXOX

At first glance, U.S. Bancorp would appear an unlikely candidate for a kinder, gentler culture. Efficiency has always been a corporate calling card. One of its antecedents, the old Minneapolis-based First Bank System, was run by a guy nicknamed "Jack the Ripper" for his obsession with controlling costs.

Under Davis, USB still cares about efficiency, but approaches decisions with an eye for impact on all stakeholders. When a new product is proposed, a common question is, "Would this be good for my grandmother?"

Davis has made employees feel more like partners by opening lines of communication on strategy and even hiring policy. In 2010, for example, management made a deal with employees: Instead of making 2,400 new hires, as the budget called for, the company would hire only half that many. In exchange, Davis would do what he could to protect their jobs if the economy didn't pick up as expected (which it didn't).

"It was a trade-off for job security," Davis said. "What I heard was, 'I trust you guys to look out for me, because you tell me the truth. If I have to work my tail off because you won't hire more people, but if it means I'll still be here in nine years, I'll do it.'"

In exchange, he asks employees to be partners in a hostile environment. As the biggest scandal-free bank, "we walk a tightrope that's higher than any other bank, and we have no net," Davis said. "We've been very clear with employees



about this: We can't fall or even lose our balance. If we screw up, we're in trouble."

Such efforts pay off in employee engagement scores that rank in the top quartile of all companies, and have made USB a regular on a list of the "world's most ethical companies" published by Ethisphere. It is also the largest bank on the list.

Tim Erblich, CEO of the Ethisphere Institute, said USB is ahead of most banking peers in recognizing the power of openness and ethical example-setting at the top. Employees take pride when their company tackles society's ills, such as a recent initiative for serving the unbanked. That, in turn, inspires loyalty and extra effort.

"It's a secret sauce for success," Erblich said. "If employees trust the leadership, then your customers trust the employees and it all trickles to the bottom line. It's super-smart business."

It's not easy to align 70,000 employees scattered around the world – USB's retail banking business is in 25 states, and its corporate banking, wealth management and trust businesses are national, while payments is global.

When Kate Quinn started as the company's chief strategy and reputation officer in 2013, she saw a lot of people who instinctively understood the culture, but no centralized mission statement or set of core values to define it. The lack of cohesion made marketing USB to customers, another of her tasks, more difficult.

"It's such a different and unique culture, but there wasn't a set of words or unifying principles that everybody looked to for guidance," said Quinn, who worked for several large health care companies before joining USB.

Quinn led an effort that solicited from customers and employees words and phrases to describe the company.

Eighteen key themes emerged, which the executive team whittled to five core values (including "We do the right thing" and "We put people first") and a purpose statement ("We invest our hearts and minds to power human potential").

Quinn said three main business goals are embodied in the culture: to be customers' most trusted choice, create a unified customer experience across business lines and channels, and continually build better processes and technologies.

Innovation is central to the effort. McDonald, the analyst, said it's not clear if USB is keeping pace with rivals on being the so-called bank of tomorrow. Cecere, a self-described techie, counters that other banks simply talk more about their initiatives.

"We hold our ideas close to the vest, because there's no upside to showing your cards," he said. "It frustrates the analysts, but it's what's best for us."

Dominic Venturo, the company's chief innovation officer, said about 60% of all USB transactions are performed on a mobile device. His 25-person innovation team, which started in the payments group a decade ago, now works with all business lines to identify problems and anticipate what's next.

It has projects going on everything from blockchain to merchant-based mobile apps. One recent launch employs mobile geolocation services already used to help customers find an ATM or branch to match a customer's whereabouts with a merchant's and reduce declines of valid card transactions.

The team also runs what Venturo describes as an in-house version of "Shark Tank," the popular television show. Employees pitch ideas and the good ones get funded. One example: a "high visibility credit card" with large fonts and a divot on one end so customers with failing eyesight can feel which side to slide into

a reader. "It's not all that techie, but it's definitely innovation," Venturo said.

Venturo's unit doesn't have a profit-and-loss statement, but this being USB everything is measured. Projects start small, move through research and development, are tested in experiments and pilots, then get reviewed again. "The process isn't super-cutting-edge, but it's our culture – very methodical," he said.

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Being a "cultural caretaker" may be Cecere's biggest challenge. Davis' departure, particularly when the company he's re-engineered could be poised to capture the growth that has eluded it, puzzles many. Some worry that he or someone in his family is ill; others think that he's simply tired after 10 years of bank wars.

A few have speculated that he witnessed the scandal engulfing his friend and colleague, John Stumpf, the former chairman and CEO of Wells Fargo, and is getting out before something unexpected blows up.

Davis calls the latter notion "offensive." The only thing he's tired of is outsiders trying to "fill in the blanks" on a straightforward story: He got the job at an early age and thinks 10 years is long enough for any CEO to stick around. He also is ready personally for a new challenge. "I've long believed that there's one more thing for me to do in life, probably more mission-based," he said.

If the election had turned out differently, Davis thinks that could have been a role in Washington. Now, he's not sure. He could get more active in one of his causes, such as Step Up, a summer-jobs program for disadvantaged teens he helped launch in the Twin Cities.

The only things he's certain about are that he will not work for another bank, and that he has the right successor.



Cecere is replacing an icon, but most investors and analysts suggest he's up to the task. "I can't imagine a more seamless transition, even for a person as hard to replace as Richard Davis," analyst John McDonald says.

Cecere grew up in Norridge, Ill., then an Italian enclave in suburban Chicago. His parents were bakers, and moved to Minneapolis when Cecere was 16 to open a restaurant. He was the first in his family to complete high school.

After his 1982 graduation from the College of St. Thomas in St. Paul, Minn., Cecere went to work for Control Data, a Minneapolis computer company. Three years later he took a job as a financial analyst for USB predecessor First Bank System.

A stint running mergers and acquisitions during the go-go '90s gave Cecere a unique perspective on the industry. He was U.S. Bank's CFO when it merged in 2001 with Firststar Corp., where Davis was chief lieutenant to CEO Jerry Grundhofer. Following the merger, Cecere headed the new USB's wealth management unit, until Davis made him CFO in 2007. In that

job, he earned a reputation as a sharp numbers guy.

Davis said Cecere is "less loquacious" than he is, but is "one of the smartest human beings I've ever known, and matches that with intuition about the softer issues." He said working in the family restaurant taught Cecere how to manage a service business and win loyalty, while the Catholic-school upbringing made him "a very pure thinker who values honesty, ethics and integrity."

Cecere isn't an attention-seeker. Sri Zaheer, dean of the University of Minnesota's Carlson School of Management, where Cecere earned his MBA in 1991 and is now on the board of overseers, said that when Cecere received an "outstanding achievement award" from the school in 2015, he invited only family members.

"Normally people make a big event of it, but Andy wanted it to be low-key,"

she said.

He also makes time each year to meet with finance students, breaking down complex finance and technology topics. "He's not an extrovert, but he's an excellent communicator, even in front of a crowd," Zaheer said.

On the board of overseers, Cecere is a detail-oriented guy who speaks only when he has something meaningful to say. "Andy doesn't dominate a room, but he always has the best observations and questions," said Robert Kueppers, the board's chairman and a retired senior partner with Deloitte.

"There's an air of humility about him," Kueppers added. "He's credible because he doesn't fill up the air with words."

Maintaining USB's credibility will likely make Cecere a success. Boosting revenue and the bottom line could make him a star, and he sounds confident that the environment will cooperate.

Loans grew 6% in 2016 year over year, but margins remain compressed. Cecere expects two rate hikes this year, which should help spreads. In conversations with business customers, he's hearing talk of economic expansion, which could give the payments business a boost and release pent-up loan demand.

USB has \$110 billion in commercial line-of-credit commitments, for example, but only 25% is being utilized, down from 38% in 2004. Simply returning to those previous levels would add more than \$14 billion to the loan books.

"We've always been thought of as a safe, defensive stock. When the screen is red, we're less red; when the screen is green, we're less green," Cecere said. "As the economy starts improving, I think we're going to be a little greener."

A strong performance under Cecere would no doubt make next year's all-employee gathering a celebration, even without Davis. □

BankThink

BY SCOTT RASKIN

Tap into Crowd Power to Thrive Amid Disruption

For evidence of how quickly technology changes the world, just take a look at Stripe. A round of funding in November valued it at about \$9.2 billion, nearly double what it was worth less than two years earlier and making it one of the most valuable U.S. fintech companies. The software company powers online payments for e-commerce sites and is riding the wave of consumer movement from offline to online.

Spending on Black Friday weekend highlights the trend: Internet sales on both days rose in the double digits compared with 2015, surpassing \$3 billion for the first time, and net sales at brick-and-mortar stores fell 5% over the two days. Many of the online transactions passed through Stripe, not through traditional payment processors.

The way we buy today is already different than just a few years ago. In a decade, it will be totally transformed.

Retailers and traditional payment processors aren't the only ones being affected by the broad changes underway. Technology is continually redefining how most industries work, from financial services and health care to manufacturing and energy.

Here is what every company must do to stay relevant and competitive in the coming decade of unprecedented disruption.

• Grasp the Full Scale of Disruption

If you can't see the complete picture of impending changes, then how can you possibly confront those changes?

Keep tabs on emerging technology providers. Be hyperaware of the trends in your sector. And ensure that all employees are educating themselves about the specific disruptions that apply to your business.

You need to continually experiment with new ideas as well. Polaris, which makes motorcycles and off-road vehicles, had a program for employees to generate new ideas. The result was Slingshot, a unique three-wheeler that disrupted the traditional motorcycle business and helped boost Polaris' market capitalization to \$6 billion.

Follow Polaris' model by engaging with employees and customers to gain valuable insight. Experiment with new ideas even if it could cannibalize your business, because you might have stumbled onto the next big disruption in your industry.

• Listen to Employees

While active executive participation remains essential, every business also must demonstrate trust, promote collaboration, and inspire innovation across the entire employee population. Unfortunately, only about a third of U.S. employees today are "involved in, enthusiastic about and committed to their work and workplace," according to Gallup. That has a measurable negative impact. Research shows that unhappy workers end up being 10% less productive than their colleagues.

Giving your employees a voice will inspire them to care enough to help the



company advance. As part of an innovation challenge, Citibank decided to simultaneously connect more than 260,000 employees in 97 countries. The bank was able to generate massive participation from its diverse employee base, ultimately leading to 2,000 new ideas being suggested.

Start with this fundamental question: Is there a way for employees across the organization to easily share their ideas? From there, either introduce new systems or change existing ones so that you're fostering a culture of innovation.

• Break from Tradition

KPMG research found that 54% of insurance companies say their innovation strategies focus on developing new products tailored to changing customer needs. The lesson is, quite simply, that if the old market is disappearing, it's time to look for a new one.

When seeking new ideas, many companies hold quarterly brainstorming sessions with their top executives, but that's no longer enough. Make idea generation and self-disruption an ongoing process that is built into your corporate culture. Be ready to implement the best ideas in almost real time.

Not every idea is transformative, but a lot of improvement can happen incrementally. Crowdsourcing uncovers a range of ideas that can help generate savings, identify new opportunities and improve existing products and services.

And who knows? One of those ideas just might be the next Slingshot. □

OPINION

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Scott Raskin is the chief executive of Spigit, an innovation management software provider. He has two decades of experience building technology brands, including TeleLogic and Mindjet.

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BackPorch



JAY SIDHU

"The best option would have been to keep it, but because of the regulatory environment that is not the best option."

Chairman and CEO of the \$9.6 billion-asset Customers Bancorp, on deciding to sell its digital-only BankMobile unit before the Durbin amendment kicks in

PARRIS SANZ

"We hit a bump in the road and blew out a tire. We just need to change out the tire, and we'll be back on the road."

CAN Capital's acting CEO, on troubles at the online small-business lender that prompted it to stop making new loans and let go of half of its employees

MARTY MOSBY

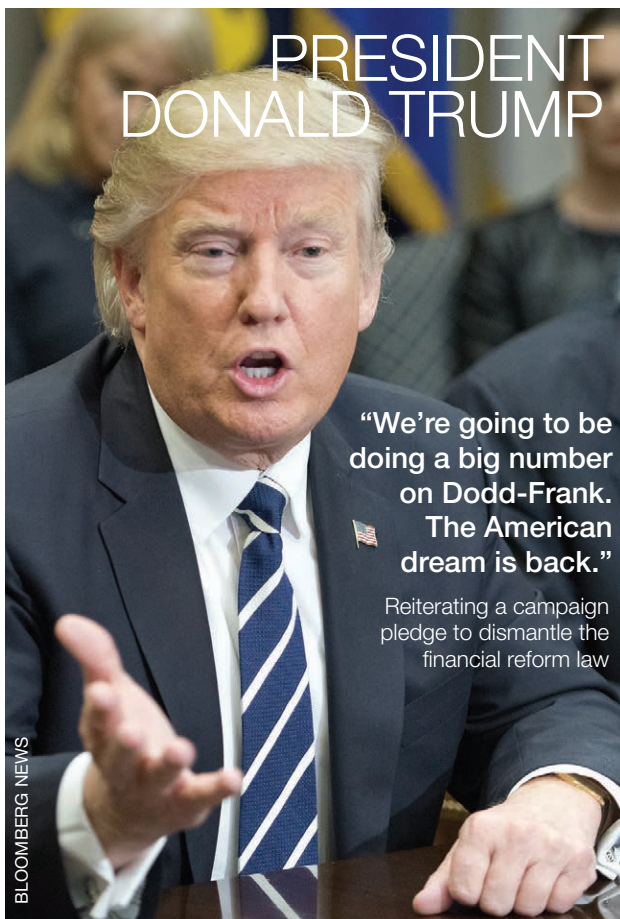
"This is an aircraft carrier, this isn't a speedboat."

Vining Sparks analyst, cautioning that Citigroup likely will be restructuring through 2017, despite having achieved a post-crisis milestone recently

ELISHA WIESEL

"In the same way he was dismayed at the lack of action over Syria, I think he would have been very disappointed at the direction this country seems to be turning."

Goldman Sachs' chief information officer and the son of Holocaust survivor Elie Wiesel, saying his father, who died last year, would have disapproved of Trump's immigration ban



"We're going to be doing a big number on Dodd-Frank. The American dream is back."

Reiterating a campaign pledge to dismantle the financial reform law

MIKE BOUCHET

"I felt a bump, like a jolt of electricity, because it smelled just like money. It was invigorating."

German artist who hired a perfume expert to replicate the smell of U.S. currency

RICHARD PAINTER

"They're playing a game, and they're playing a game to make this person feel beholden to Goldman Sachs."

Law professor and former White House ethics lawyer, on why Goldman expedited pay for its former president, Gary Cohn, as he joins the Trump administration

PETER NAGY

"Trump went from talking about Goldman Sachs and Wall Street having heavy influence on the government, to them literally running it."

Protestor outside Goldman's headquarters, complaining about its executives taking key jobs in the Trump administration

JOHN ROBERTS

"Now hold on. You're saying that the American people are too dumb to understand that if you say \$10 plus a 20-cent surcharge, they can't figure out that that's \$10.20?"

Chief Justice of the U.S. Supreme Court, questioning a Justice Department lawyer in a case about credit card surcharges



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