Revenue Recession Realities

The Bankers' Perspective

Banking Industry Research by

strategycorps

Those who analyze the banking industry from the outside say it is experiencing a "revenue recession" due primarily to a continuing and forecasted net margin squeeze, declining overdraft revenue, and cannibalized debit interchange revenue (by alternative payment methods).

But what are actual bankers' thoughts on what they're experiencing? To get this banker's perspective, we polled hundreds of bankers with these inquiries to get their outlook on the reality and severity of a "revenue recession" taking place and what's in store for the next 12 months.

Some banker perspectives were consistent with those who follow the industry, while other perspectives were quite different. Also shared are StrategyCorps' viewpoints on the bankers' responses and what next they may need to be thinking about to survive and thrive the revenue recession.

INQUIRIES

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02 Will the outlook for mortgage originations and refinancings continue to be an ongoing, stable source of revenue?

03 Will overdraft-related fees continue to decline due to market, regulatory, and/or political pressures?

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05 Will debit card-related interchange fees be flat or decrease due to increasing competition from traditional and new products?

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07 Will the net interest margin “squeeze” continue to negatively impact revenue?

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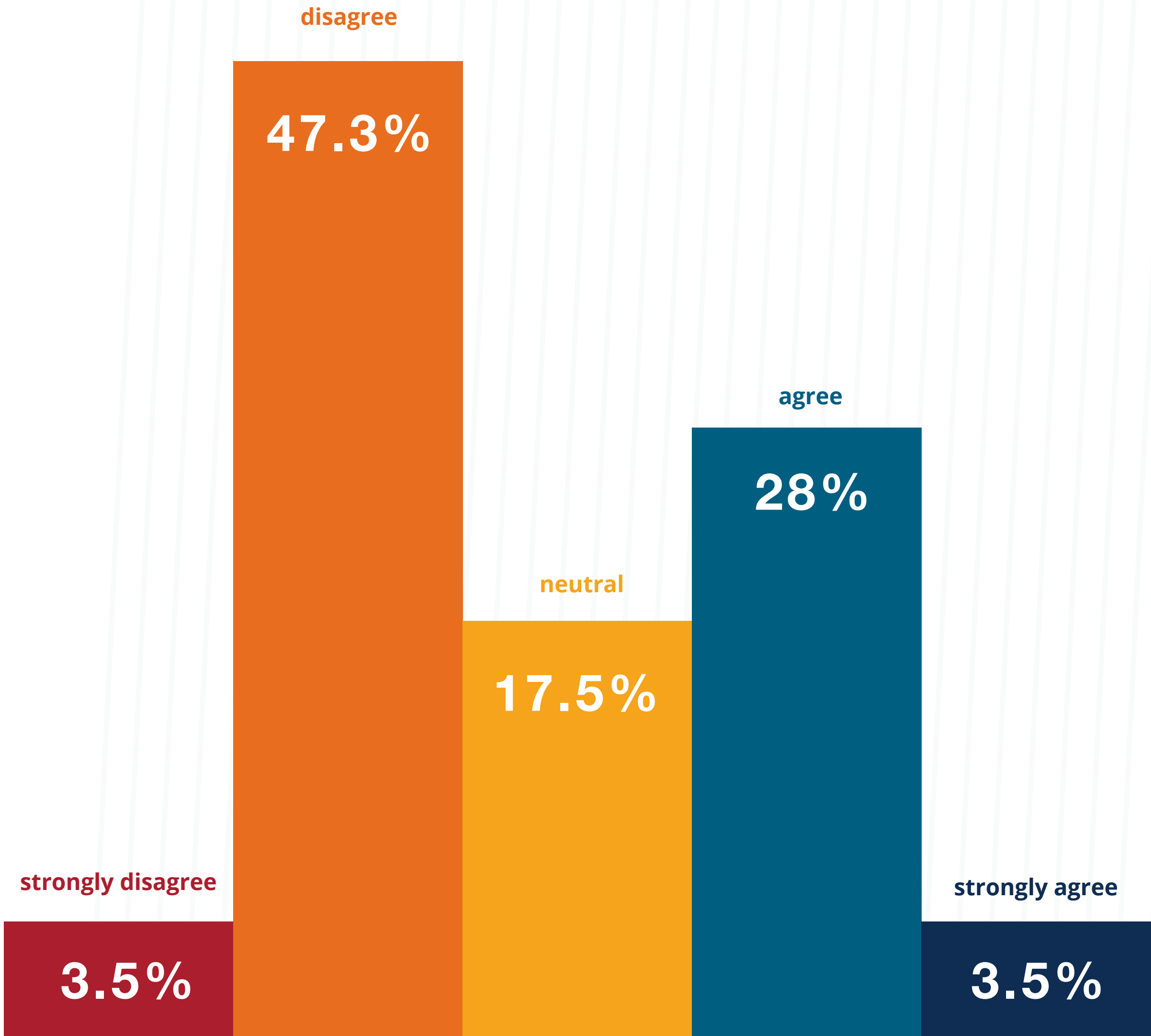
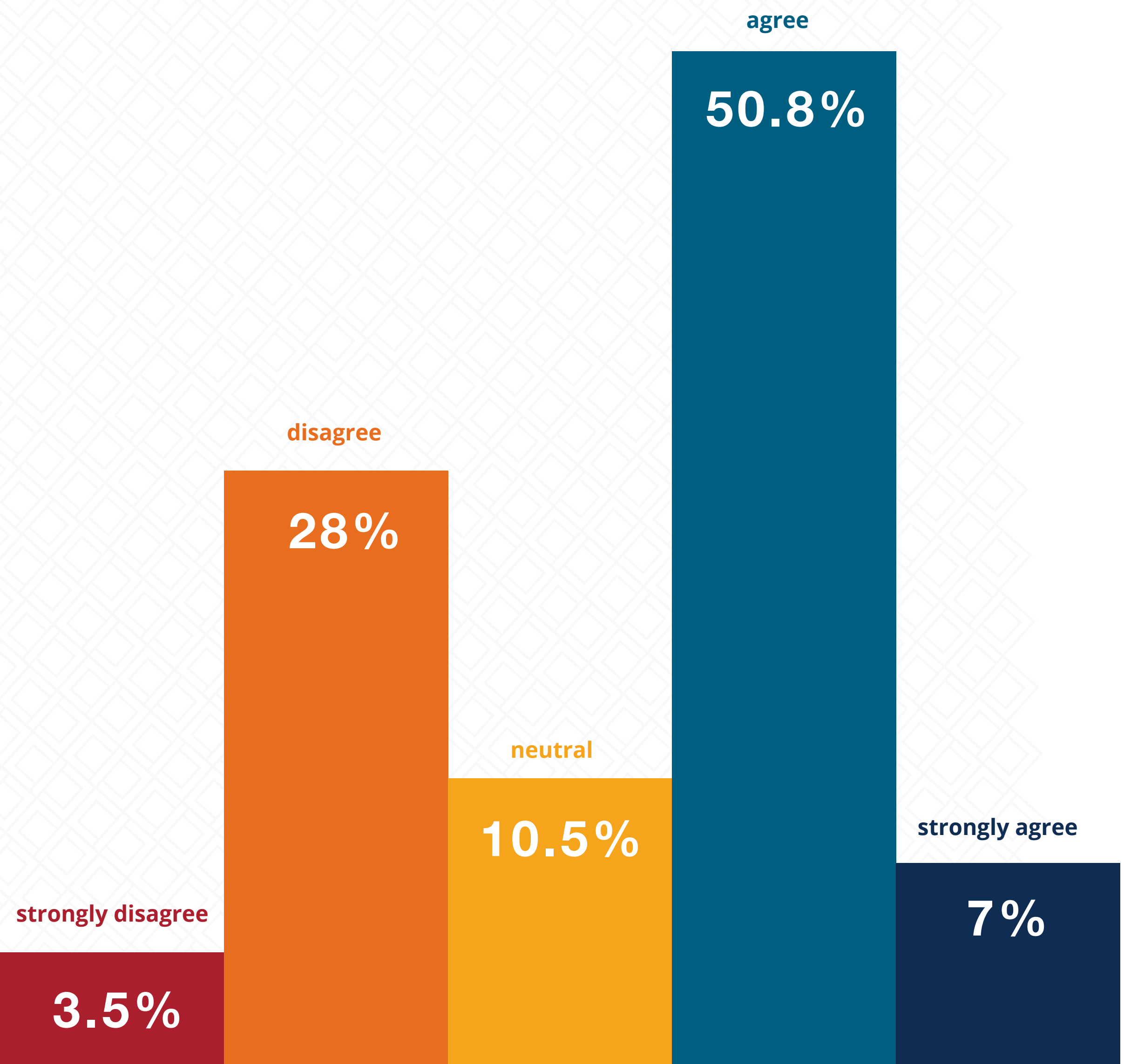
10 Is your financial institution planning to do anything differently to generate replacement revenue?

The reclassifying of over-estimated loan loss reserves as revenue will continue to be a viable way to generate revenue for the next 12 months.

OUR VIEW: This accounting convention that's created replacement revenue for a while now seems to have had its run. Just over half of bankers think this accounting move is a less viable and sustainable way to boost revenue when all the other sources are underperforming. Plus, the investment community isn't as forgiving on the extra-wide swings in these reserves as they were in the recent past.



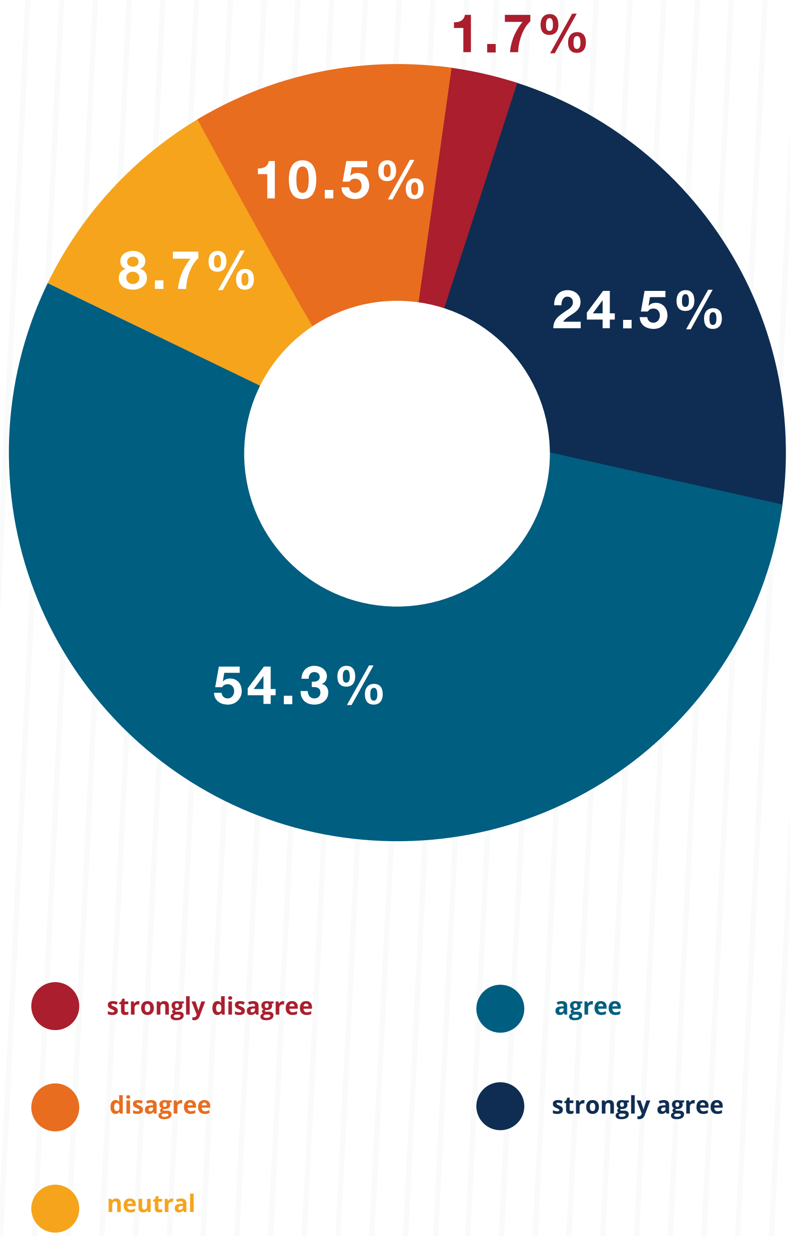


The outlook for mortgage originations and refinancings will continue to be an ongoing, stable source of revenue for the next 12 months.

OUR VIEW: The housing boom and continued historically low interest rates will continue to fuel mortgage-related revenue, according to nearly 60% of bankers. However, every banker knows one surprise move by the Federal Reserve about increasing interest rates or tapering quantitative easing, and this source of revenue will be materially impacted.

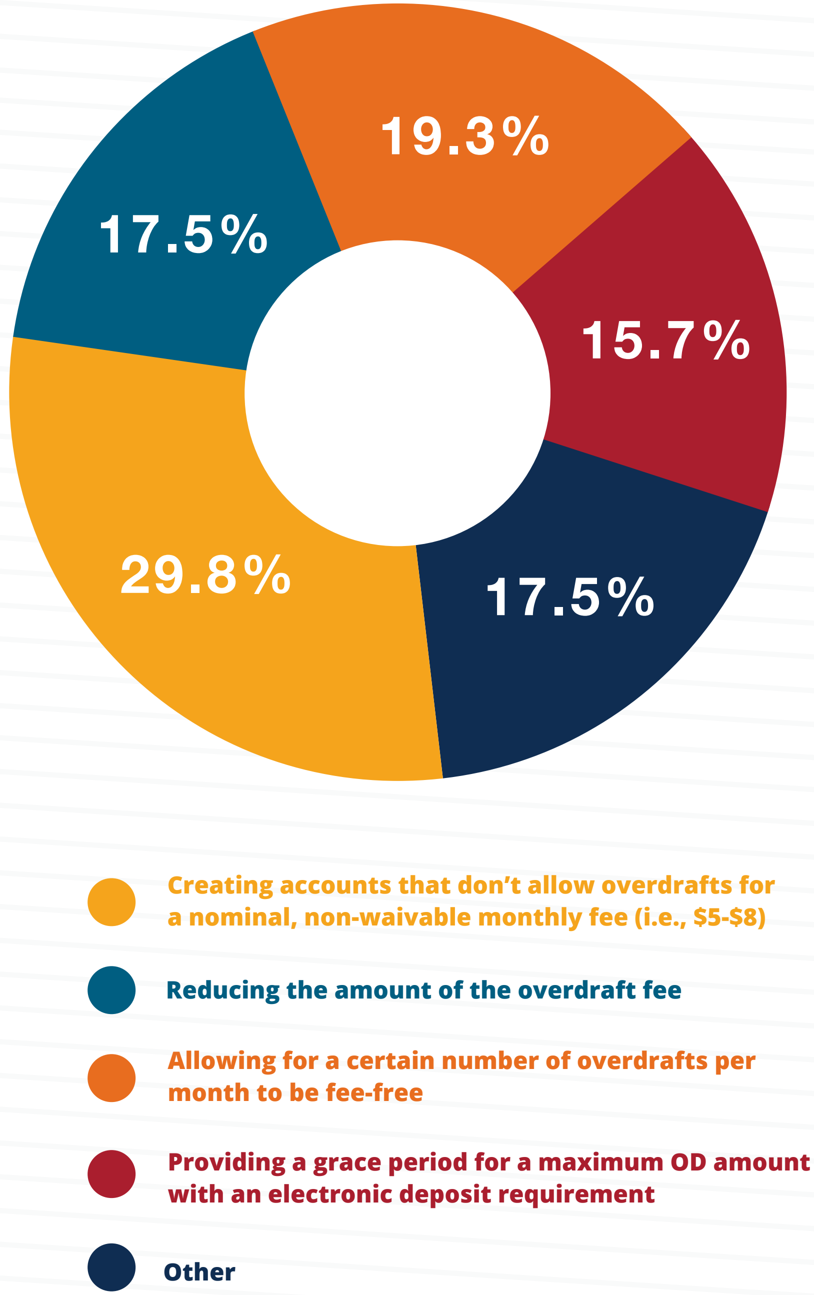
Overdraft-related fees will continue to decline for the next 12 months due to market, regulatory, and/or political pressures?

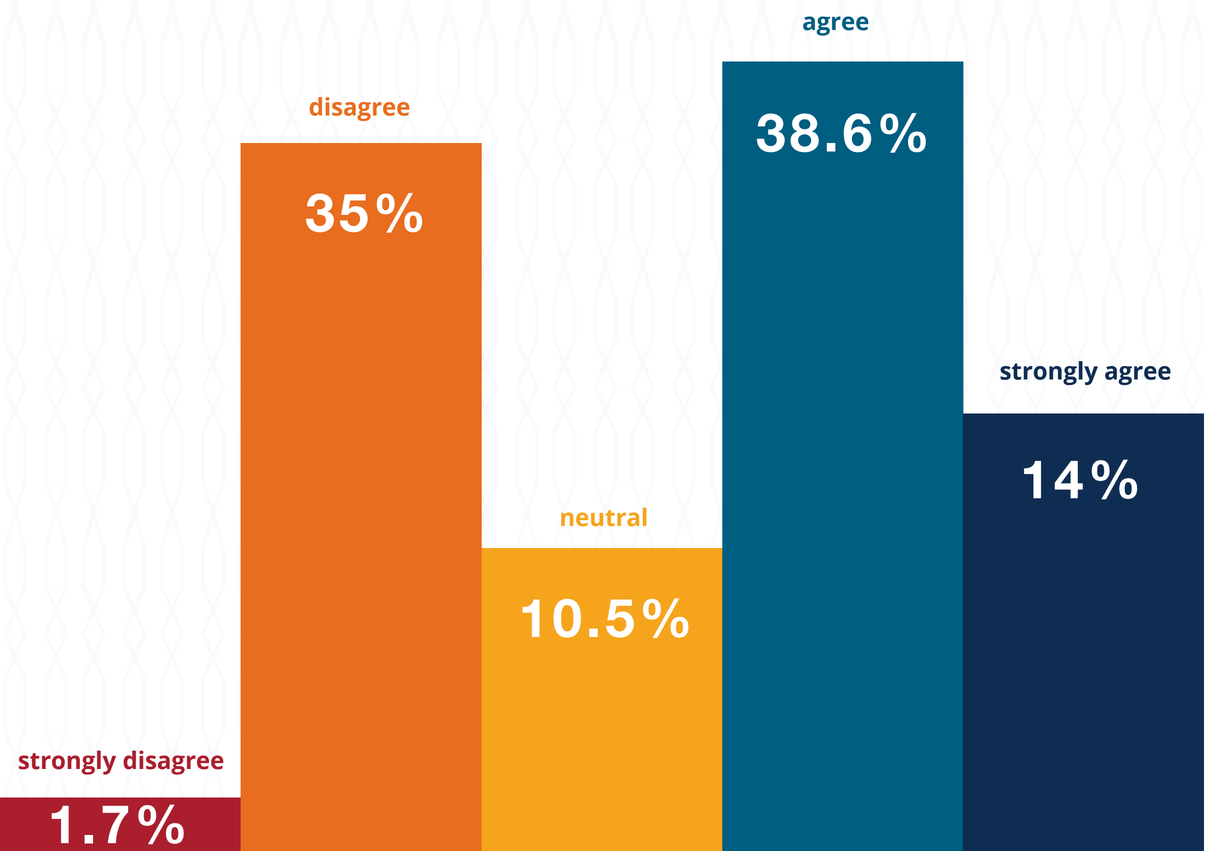
OUR VIEW: Nearly 80% of bankers feel that overdrafts will not be the same revenue generator they have been. In discussions with bankers, few feel that overdrafts will be totally over. Most feel the compounded market effect of lower frequency and reduced OD fees will fuel a quicker decline than has already been experienced. Toss some regulation or political pressure on the pile, and this revenue source will be materially constrained, putting many community FIs in the revenue pressure cooker.



The primary way financial institutions will respond to the pressures on overdraft fees will be?

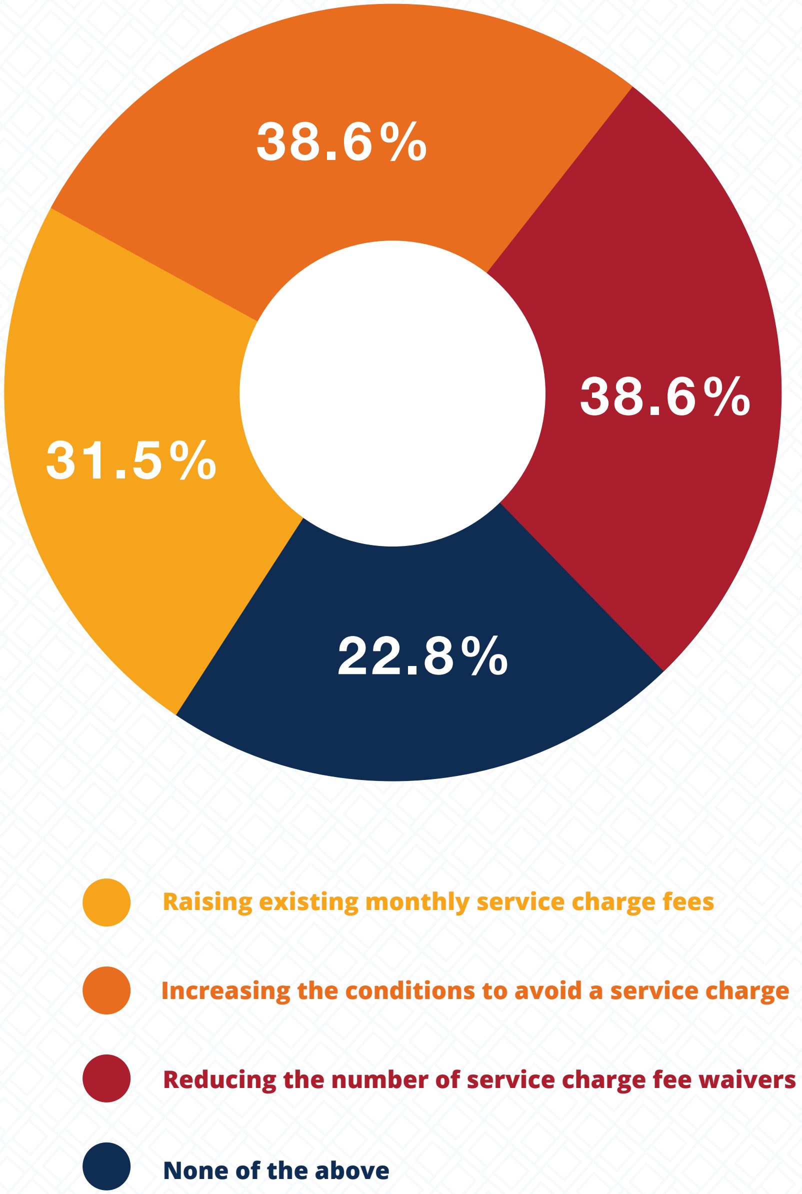
OUR VIEW: At this point, bankers are not sure of any one clear path to replacing lower overdraft revenue. Despite the press coverage, completely eliminating overdrafts isn't likely to happen. More likely, there will be reduced OD fees per occurrence and more ways to waive the fee if there is an OD. For the 30% of bankers thinking that charging a monthly fee for having an account that doesn't charge overdraft fees is the new "overdraft privilege," good luck with that exchange of value for a fee!





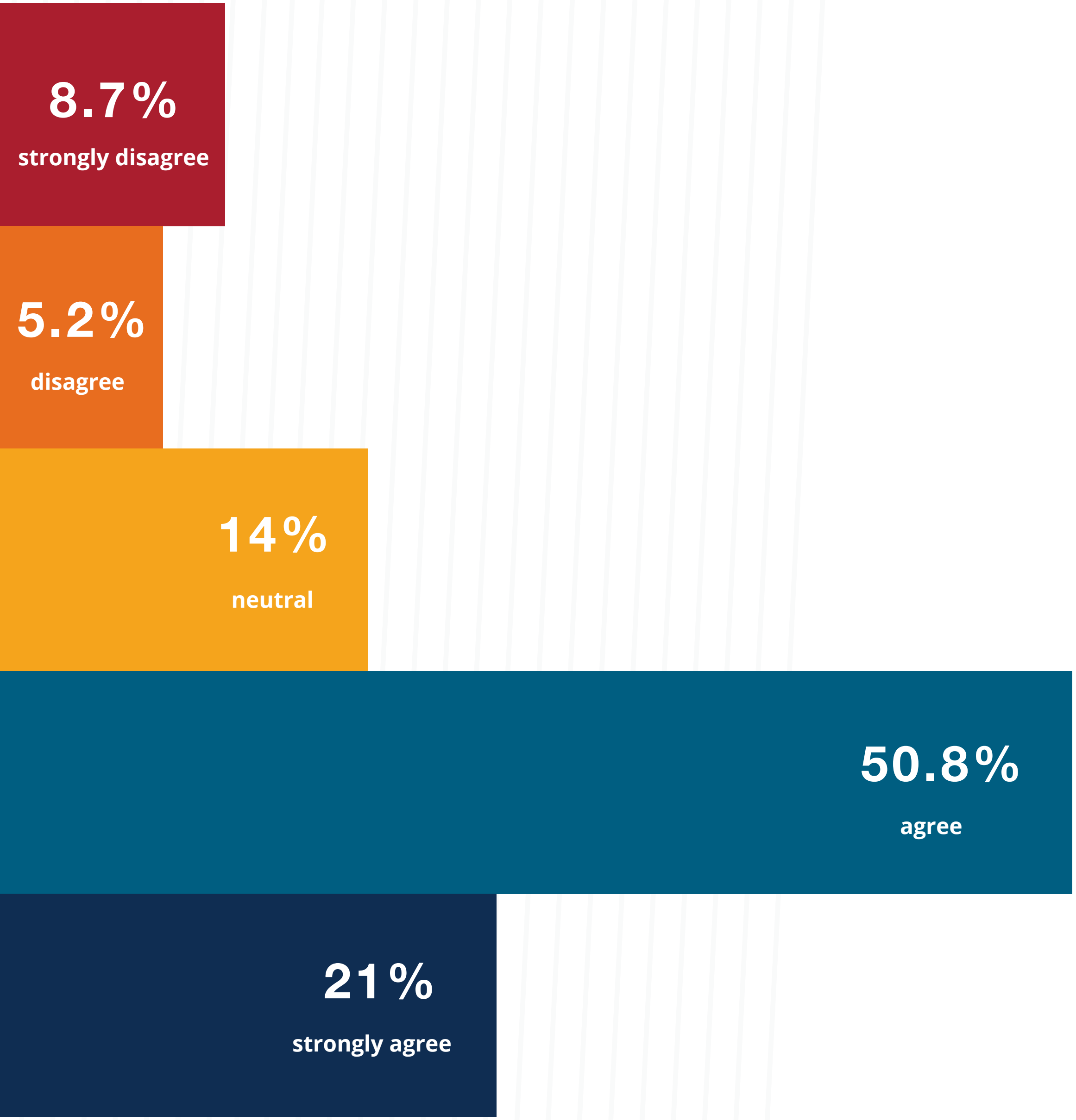
Debit card-related interchange fees will be flat or decrease in the next 12 months due to increasing competition from credit card products, mobile wallets, merchant apps, buy-now-pay-later offerings or cryptocurrency payments.

OUR VIEW: While debit card spending (dollars, not swipes) exceeded credit card spending for the first time ever in 2020, nearly 53% of bankers feel that their debit card interchange revenue is under increasing pressure. And don’t count out credit cards, which will recover quickly once longer-term confidence about the economy materializes.



How can checking account-related revenue be materially increased? (choose all that apply)

OUR VIEW: Not surprising that effectively raising mainly penalty-based service charges is seen by bankers as the most practical replacement revenue strategy. However, unless there is some commensurate tangible value to be provided with these fee increases, consumers will consider these fees even more unfriendly. The impact will be customers/members heading to competitors who actually offer value for a reasonable fee, namely selected digital banks.

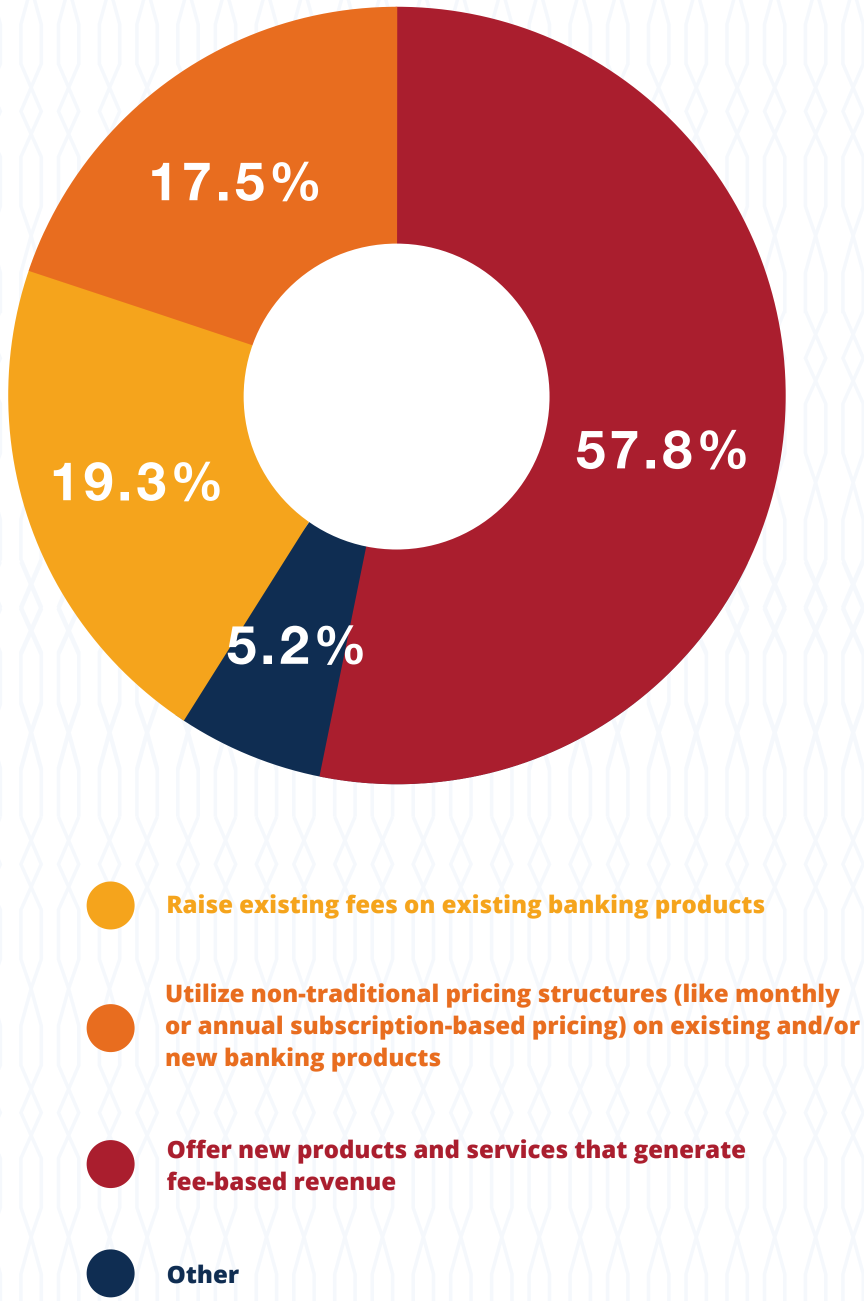


The net interest margin “squeeze” will continue to negatively impact revenue for the next 12 months.

OUR VIEW: The squeeze remains. Nearly 72% of bankers feel that NIM will continue at its already historically low levels. This squeeze has very few available options to loosen its tight grip, which means this primary revenue source is stuck in neutral at best until slow-moving macroeconomic forces (including political ones) allow for some relief. This relentlessness will test the best bankers to figure out how to generate more non-interest revenue creatively and better manage operating expenses, which for many community FIs means selling or merging to achieve scale.

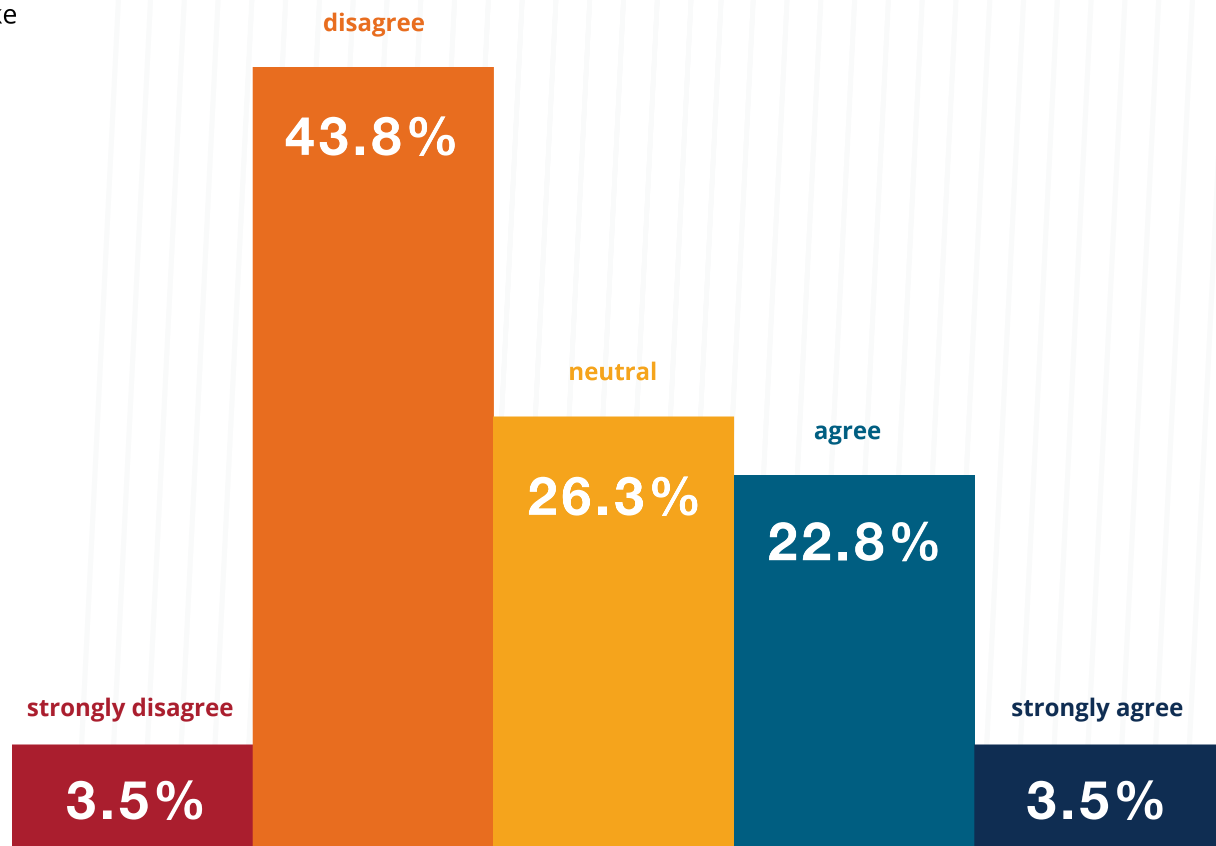
What will financial institutions be required to do to generate replacement revenue?

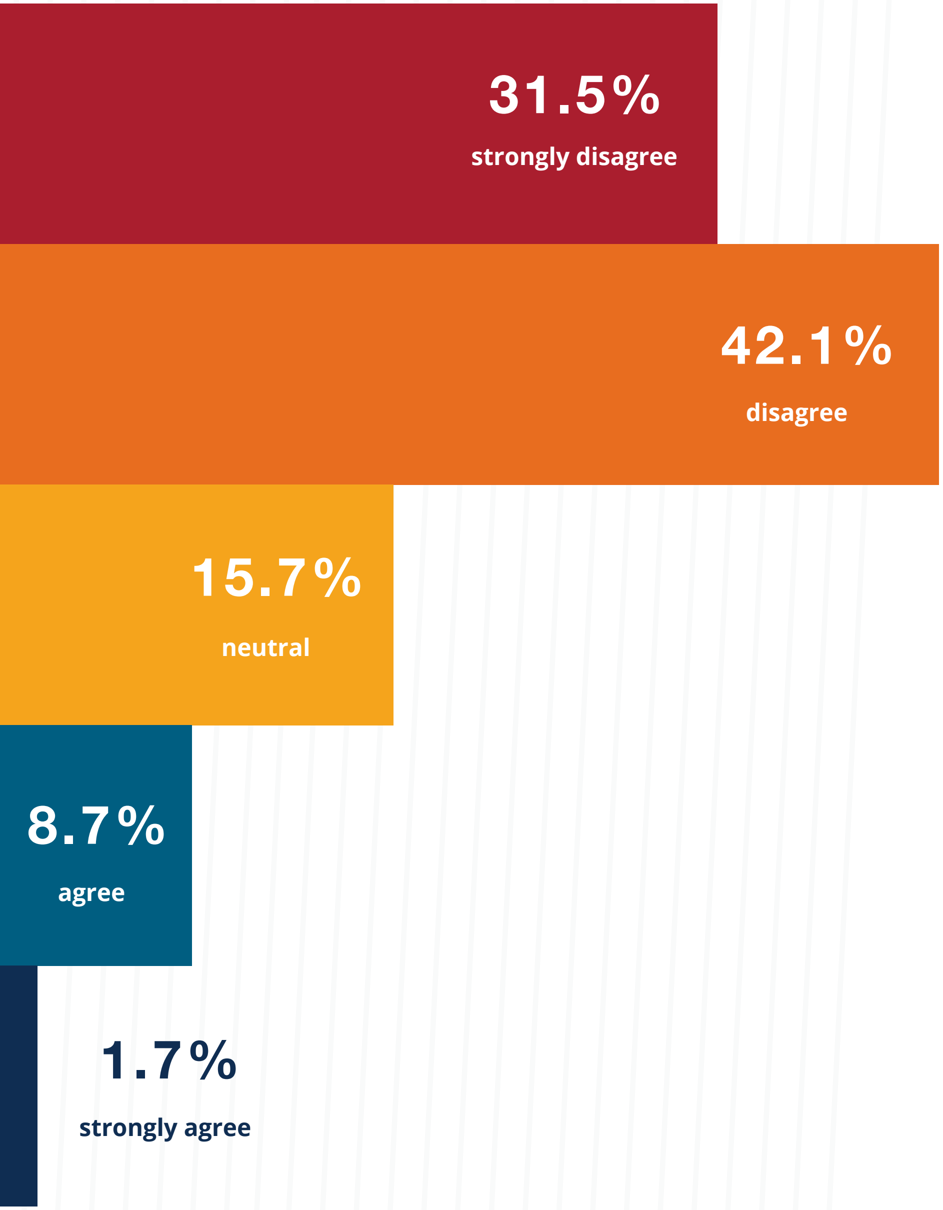
OUR VIEW: It's refreshing to see that nearly 58% feel the way to generate replacement revenue is through new products and services. This begs the question, "what are those new products and services?" There are lots of choices with Fintechs currently leading product innovation. The risk is many of these Fintech product/service choices are unproven in terms of consumer appeal and/or revenue potential. What's not refreshing is that slightly more bankers feel just raising fees, many of them penal in nature, on existing products is better than coming up with new fee structures that are more consumer-friendly.



Neobanks and digital banks are more impacted by this "revenue recession" due to their higher deposit cost of funds and reliance on fee-free products.

OUR VIEW: What's most interesting here is that over a quarter of the responses were "Neutral" on this question. It seems like since these neobanks and digital banks are winning at the expense of nearly all traditional banks other than the megas and super-regionals, that more bankers would be informed enough to have more than just a neutral opinion on this impact to a rapidly growing segment of competitors.





The “revenue recession” isn’t a reality now and won’t be in the next 12 months, so my financial institution isn’t planning to do anything differently to generate replacement revenue.

OUR VIEW: The revenue recession is real. There are no traditional levers left to flip to easily generate new revenue from existing products. Cost-cutting to prosperity won’t work on its own. Not sure what the 10% of bankers are experiencing who agree or strongly agree that it’s not a reality, but for sure, the other 90% of bankers would like to buy you a drink to find out.

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