



# NEW APPROACHES TO CORE STRATEGY

*Breaking down the behemoth gives bankers more flexibility*

By Anna Burgess Yang

A bank's relationship with its core vendor can be described as love-hate at best and acrimonious at worst. Tensions around lack of service, falling behind in technology, and being nickel-and-dimed rose to a boiling point in the past few years as community banks rushed to bring new products and customer experiences to life.

Brad Smith, a partner at Cornerstone Advisors who leads the firm's Transformation Services practice, said that the presumption that the core vendor is a partner to help community banks compete has dwindled. "As the digital era grew and grew, [community banks] felt like their core vendor wasn't living up to that end of the bargain," he said.

Since the beginning of the pandemic, the need for third parties and non-core vendors

to connect to the core has skyrocketed. Speed is also essential: Bankers can't wait months to years for a core vendor to add a new feature or for a core to make an integration with a fintech possible. It also raised the question: Is a single, primary product still the way of the future?

## **Next-gen cores create pressure and competition**

Some banks are very interested in "next-generation" core platforms. These digital-native, API-centric platforms offer features that are outside the realm of legacy providers, including advanced data analytics, hyper-personalized customer experiences, and conversational AI. Some are even priced differently, relying on Software-as-a-Service models instead of traditional license fees.

As attractive as next-gen cores might be, the decision to migrate

to a next-gen core isn't an easy one. The well-established players in the core industry are backed by decades of experience and the testimonials of satisfied customers. Smith commented that some of the next-gen cores "aren't ready for prime-time yet." They may be unproven in their ability to meet the needs of community banks. In attempting to solve the technical limitations of a traditional core vendor, they may lack the broad range of features that banks need from their core provider.

The other risk is that successful next-gen cores are a prime target for acquisition. Back in 2013, Fiserv acquired Open Solutions, Inc. At the time OSI's flagship product, DNA, boasted modern architecture and a developer's toolkit that let banks create their own apps, much like an open-source product. Along with that acquisition, Fiserv gained 800

account relationships; community financial institutions that had made a decision to go with one vendor suddenly found themselves with another vendor. In April of 2022, Fiserv completed its acquisition of next-gen core provider, Finxact.

Still, the competition might be worth exploring, especially as a bank's strategy often needs to expand beyond the geographical boundaries of its community. Banks can be the foundation for initiatives such as banking-as-a-service or e-commerce partnerships — with the right core platform.

### **Moving from one core to a customized bundle**

Smith, whose team at Cornerstone Advisors evaluates core vendors and assists with core conversions, said that the classic model where a bank is “all in” with their core vendor is dying pretty quickly.

David Foss, CEO at Jack Henry, thinks that even the term “core” may be a thing of the past. Some core providers, Jack Henry included, have begun “unbundling” their products. Foss described this as taking all the pieces that a typical core solution includes and turning them into modules. Banks can create their own “bundle” from separate components, such as wire transfers or a deposit module.

Core unbundling allows more flexibility for community banks. “I think we see a shift coming toward this desire to create a differentiated experience and have this ease of connectivity provided by the primary provider,” Foss explained. “We’re going to provide all these different components that [banks] can easily connect on a public, cloud-native platform.”

A core vendor's ability to effectively unbundle depends, in

part, on its underlying architecture. Many core solutions are based on relational databases that are so interconnected that separation is not structurally possible. Many next-gen cores, on the other hand, were built on microservices: They were always smaller components of a larger whole, making the decoupling effort inherent (and making the product attractive for banks looking to only pay for the services they needed).

As a buffet-style approach becomes more common and more desirable, legacy core providers may find themselves “stuck” — unable to offer an unbundled option to their clients. They, and their client banks, will find themselves married to an outdated data model that cannot keep up with the competition.

### **Evaluating a core vendor's integration capabilities**

In some cases, the “differentiated experience” described by Foss may come from core unbundling. In other cases, it may come from APIs and integrations.

Foss sees a world where banks still provide the primary relationship with their customers, but the customer experience comes from a fintech or another vendor. “If you have the right partner who's providing integration and who's providing a digital platform for you, [it] allows for that presentation layer and that ease of use.” Foss referred to this as banks “embedding the rails underneath the fintech.”

Smith agrees. “The core's ability to provide integrations — easily — has become a major focus and a must-have for many bankers,” he said. There are two sides to evaluating a core's integration capabilities: The architecture (how the integration works) and the licensing (how much will the bank be charged per integration or data exchange).

“Are you relying on the core vendor to make that all work?” Smith wondered. “What's the licensing? Do you need to have some development talent in-house to be able to do that? And just because [cores] have an open API integration doesn't mean they've ever connected with your brand new digital vendor.” All of these are considerations as bankers look at core capabilities. He said that some banks are now looking for core systems that only provide very basic functions, but have really good integrations.

Some banks still want to work primarily with a single core vendor because it makes vendor management and conversations with regulators easier. But on the other end, banks that focus on serving a customer niche want the pieces that serve those customers best. Foss said that these banks are looking for tight integration and core vendors that are committed to APIs and making it easy to connect solutions together.

Smith noted that increasingly community banks have needed to evaluate more nimble middleware solutions or a third-party integration platform to connect their core vendors and key applications. Some banks even have multiple middleware solutions to achieve the connections they want. It all depends on how easy each vendor makes it to connect to other platforms.

A reimagining of the core replaces the “best-in-suite” model with a “best-in-breed” for each bank's unique needs. Of course, the internal teams tasked with choosing a core solution are trying to determine what the future holds. Is it a next-gen core? Core unbundling? Integrations? Or a combination of all of the above? ♦