2023 in Review, Pt. 1 of 2: Challenges and Opportunities

deposits industry update economy

Summary: Over the past year, the financial sector has had to navigate many disruptive forces. In two back-to-back articles, we look at the challenges faced by CFIs and the opportunities that have emerged during 2023. In this first article, we explore how CFIs have responded to economic uncertainty and inflation, intensified competition for deposits, and shaken consumer confidence in the banking industry.

The popular board game Scrabble was invented in 1933 by the architect Alfred Mosher Butts while he was unemployed during the Great Depression. However, he set the game aside when he returned to work when the market picked up — and it was only 15Ys later that the first commercial sets were produced. Scrabble is now available in 30 languages and has sold about 150MM sets. Just as the Great Depression was a catalyst for the invention of an iconic game, disruptive forces in the financial services sector have provided opportunities for community financial institutions (CFIs) to embrace change and find new ways to grow.

In the first of two review articles, we look at three key trends and challenges that shaped the sector this year as well as some of the opportunities available to CFIs willing to take them.

Key trend: Economic uncertainty and inflation. Tight economic conditions continued into 2023 against the backdrop of significant geopolitical tensions, climate concerns, and supply chain disruptions. Although inflation has abated from 9.1% in June 2022 to 3.7% in September 2023, prices remain high and consumers are feeling the pinch. This has resulted in changes to spending and saving habits. According to Transunion's midyear credit report, bankcard balances reached a new high of $963B in Q2, up 17.4% YoY. Gen Z recorded the biggest rise, up by 51.9%. Buy now pay later (BNPL) is also increasing in popularity, with 8% of Americans — double the number in 2021 — using this form of financing to pay for necessities.

CFI opportunities: Financial wellness programs. Consumers are feeling the stress of the economic situation and are looking for ways to improve their money management capabilities, while financial institutions (FIs) want to be able to support their customers better and minimize potential rising delinquencies. To this end, many CFIs have bolstered their financial literacy offering, in some cases using gamification to increase uptake. Many have also developed personalized products to encourage healthy financial habits and help consumers with budgeting and cash flow management. Institutions are at different stages of incorporating analytics and artificial intelligence (AI) to drive insight and deliver automated programs, with some partnering with third parties to move forward.

Key trend: Intensified competition for deposits. With interest rates remaining elevated throughout 2023, FIs have been facing high deposit costs and waning customer loyalty. Deposit outflows peaked in Q1 but have since stabilized and even reversed for CFIs. Amid the emergence of innovative products and the technology-driven ease of switching, competition for deposits is fierce. Customers are now more likely to spread their finances across institutions in search of the best returns.

CFI opportunities: Improved omnichannel experience. This competition has driven leading institutions to renew their focus on enhancing the customer experience to provide personalized content and products consistently across all channels, both physical and digital. By breaking down product silos and investing in technology — both to fine-tune the digital experience and leverage data to deliver meaningful insights — CFIs can deepen their existing relationships to extend their share of wallet and drive customer loyalty.

Key trend: Reduced trust in FIs following the collapse of three major banks. Consumers' trust in FIs took a serious knock after the collapse of Silicon Valley Bank, Signature Bank, and First Republic Bank in the first half of 2023. In the immediate aftermath, a study found that only 10% of Americans had high confidence in the nation's FIs, while 57% had some confidence and 31% hardly any. Among Americans surveyed by Morning Consult, 16% said they moved their money as a direct result of the bank failures.

CFI opportunities: Trust-building strategies. Following the banks' collapse, FIs quickly entered crisis management mode. This included intensifying communication to restore their customers' faith in the institution's ability to keep their money safe. Messaging tended to center around certain core principles: the institution's solvency, the structural integrity of the industry, and the protective measures already in place, such as the FDIC insurance for deposits up to $250K. Leading institutions recognize the need to continue to engage with their customers to build trust by embracing transparency, positioning themselves as industry experts and competent advisors, committing to excellent customer service, and protecting their customers' data.

CFIs have faced many headwinds this year. The disruption has generated opportunities for CFIs to double down on strategies to meet their customers' needs, whether that be through focusing on financial wellness, improving customer service, or building trust. As ever, keeping the customer front and center is key to navigating these challenging times. Join us tomorrow for part two of this series, where we will explore how CFIs have weathered competition from fintechs, cybersecurity risks, and maintaining regulatory compliance this year.

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ECONOMY & RATES

Rates As Of: 12/05/2023 05:36AM (GMT-0800)

Treasury	Yields	MTD Chg	YTD Chg
3M	5.46	0.01	1.04
6M	5.41	0.03	0.65
1Y	5.07	-0.06	0.36
2Y	4.61	-0.08	0.18
5Y	4.17	-0.10	0.17
10Y	4.21	-0.12	0.33
30Y	4.37	-0.13	0.40
FF Market	**FF Disc**		**IORB**
5.33	5.50		5.40
SOFR	**Prime**		**OBFR**

5.37	8.50	5.32