# Five Things to Know About "Open" Banking Technology

With the emergence of non-traditional financial services providers, the Payment Services Directive (PSD2) regulation in Europe, and players like BBVA and Bank of America launching their own open initiatives, everyone's talking about "open banking." In fact, 77% of banks intend to invest in open banking initiatives before the end of 2019, according to Accenture research. But what does it mean, and why should you care?

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# What is "open banking"?

First, what is "open banking?" We'll start by borrowing a standard definition from Wikipedia, which defines open banking as "the use of open APIs that enable third-party developers to build applications and services around the financial institution."

For those of us who aren't developers, an API, or Application Programming Interface, is a set of published, well-documented 'rules' to a given piece of software that provides developers the 'building blocks' of that software, allowing anyone with development chops to use, rearrange, and build new apps and products with those building blocks.

At Q2, we think about open banking simply as the democratization of financial services through new, easy-to-consume banking technology. In other words, open banking is a movement of new banking tech that allows anyone (fintechs, major retailers, development groups, and of course financial institutions) to easily develop and connect digital financial products. And while this movement is very much based in technology, don't mistake it for simply an IT consideration. We believe it can and will have profound downstream impacts for financial institutions, their providers, and their consumers.

But where are we in this open banking movement? Are there actual providers out there who are selling this stuff? The answer isn't simple, but here's what we do know: Europe seems to be leading the charge, with 75% of European banks stating that open banking is critical to their digital transformation. For comparison, only 53% of US banks responded yes to the same question. In the United States, it remains to be seen how the open banking provider market will shape up, but many incumbent digital banking players (Q2 included) are making investments—either in new, open technology, or in "opening" their existing platforms to be more accessible and configurable via Software Development Kits (SDKs) or API programs.

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# Why does open banking matter to my financial institution?

## [1] Open banking technology is a speedier and more cost-effective way to launch digital products.

Let's come right out and say it—legacy banking technology is not known for its ease of use and affordability. And it's not really the legacy tech's fault - it was developed thirty, forty, fifty years ago, long before the internet, the smartphone, and Amazon. It's also been developed—and developed, and developed—to accommodate an enormous range of functionality, to the point where the cost of full-service systems must account for all the functionality bloat they've taken on over time.

At its core, open banking represents the emergence of new technologies that—while they won't fully replace your core—can provide you functionality that is modular, with a la carte pricing to boot. Because the technology is modular and made available through APIs, your institution can consume only as much as you need for a given product or project, making design and development of new products much faster. And the beautiful thing is, because open banking technology is modern, it delivers all of the scale and cost benefits of the cloud to the financial institutions that use it (finally!).

## [2] Open banking technology supplements and strengthens your digital channel and/or technology stack.

None of the emerging players in open banking (to date) have designed a product set that's intended to fully replace your existing core. This is partially because they don't want to compete with massive conglomerates, but it's also because they don't want to design another large, full-service system. Most of them know the thought of full core conversions—with their complexity and scheduling demands—are enough to send bank and CU executives running.

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As mentioned above, open banking technology is designed to be flexible and modular, specifically so that it can be used piece-by-piece and alongside your existing technology. You only consume the technology that you need, and that's all you pay for. And because of this, you can use API-based, open banking technology to launch just one new product without ripping out and replacing your core or OLB. Many financial institutions have an urge to innovate and deliver new products, but they know they can't afford to disrupt their primary digital channel in the process. Should that stop them? No.

Open banking and its API-based approach will aim to do away with that hesitation, providing a secondary, more modern technology stack where FIs can design, develop, test, and deploy new digital products separate from their existing online or mobile banking platform.

Open banking technology is a speedier and more cost-effective way to launch digital products—one of the best ways to differentiate yourself and grow cost-effectively.

## [3] Open banking technology helps you more easily partner with other companies (including fintechs!).

Whether your institution has made a full-fledged attempt to partner with a fintech company or not, you're likely familiar with the time and cost required to create a new integration with your legacy technology systems. With its APIs, open banking technology is written to be shared, built on top of, and plugged into—and the best part is, it's all written in a language that developers anywhere can understand. This means that it'll be easier than ever for you to connect with third parties, or have your vendor connect with them on your behalf. A technology environment where third-party integration is easy will give financial institutions a new degree of freedom in choosing who they partner with and what features they bring into their digital channel. And this includes fintech companies, who appear to have solved the customer onboarding challenge and are raising deposits, but don't, in fact, have anything to do with those deposits (which also need to be FDIC-insured!). Know anyone looking for new ways to grow deposits to, say, fund their lending business?

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## [4] Open banking technology can provide all-new opportunities to expand or evolve your business model.

Traditional banking was built on geography: your local financial institution was the heart of your community, and your community knowledge and expertise was the number one reason your community banked with you. And the first major wave of digital banking technology—big, full-service core processors and everything built on top of them—was designed around this model too. But as account holders continue to untether themselves from brick-and-mortar banking, and machine learning continues to take the place of community expertise, financial institutions must find a way to evolve their business models beyond what they've known for the past century. Open banking technology provides the foundation for doing just that. For example, using open banking tech, you could build a community-agnostic, millennial-focused banking app that could be adopted by account holders around the country. Still skeptical? Digital-only, branchless banks like Chime and Ally ($150B AUM) are proving this model out.

And that's just the beginning. Think of all the change we could see if we had banking technology that allowed us to completely reinvent the way core functions like bill pay are executed, turning it from a cost center into a revenue source (in fact, we have some ideas on this very strategy at Q2). While it's impossible to predict all the innovation that open banking will enable, it's safe to say that new banking technology will seek to reinvent key FI and account holder pain points and cost centers (think onboarding, bill pay, competitive savings products, and more.).

### [5] Open banking technology does require some tech know-how (which is exciting for your tech team!).

Over the last 15 years, many digital banking vendors—including Q2—have urged their financial institution clients to hand over the keys and leave the technology stuff to the experts. And with good reason—the alternative has been to hand a community bank an online banking SDK and let them develop their own digital channel essentially from scratch.

While these models won't entirely disappear, the open banking movement puts unprecedented power in the institution's hands to determine the direction of their digital channel—and the technology to execute on that direction at scale. Of course, with great power comes great responsibility—if you want the ability to develop modern apps with user experiences that compete with Google and Netflix, you've got to hire and maintain great development talent (or partner with a vendor who's open, innovative, and who you trust to bring your vision to life). Open banking doesn't specifically mean you have to adopt an in-house development approach—but if you want the full benefits of this new banking tech, it might not be too early to start planning the buildout of some development capability within your organization.

## In conclusion…

Q2 believes the five points above describe some of the biggest benefits and outcomes of the open banking movement, and we've used those concepts to inform our own "open" strategy.

While we know the open banking movement hasn't taken hold in the US like it has in Europe, we do know it's on its way. How will you embrace open banking?

**To learn more about Q2's investment in open banking, visit www.q2ebanking.com/api/q2-open/.**

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