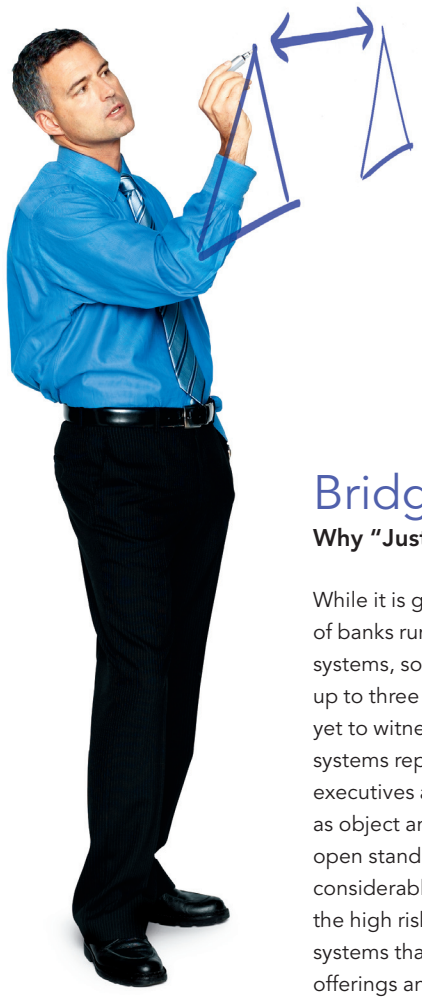

Bridging the Technology Generation Gap

Why "Just Enough is No Longer Good Enough" for the Finance Sector

While it is generally accepted that the majority of banks run on antiquated, siloed internal systems, some of which have been in place for up to three decades, the banking industry is yet to witness a widespread program of core systems replacement. Industry analysts and senior executives agree that new technologies, such as object and service-oriented architectures, open standards and Web services, can offer considerable competitive advantage. However, the high risks associated with replacing the IT systems that form the core of banks' product offerings and customer services, and the costs associated with replacing such business critical technology, are inhibiting the exploitation of the benefits these technologies promise.

Banks will eventually have to make a decision as to whether the potential benefits of core systems replacement outweigh the associated investment costs and perceived business risk. Signs that the current mantra of 'just enough is good enough' is set to change over the next few years are evident in recent industry reports, which suggest that up to one third of banks worldwide are aiming to replace their core systems. There is a definite possibility that when the first handful of major banks makes the decision to replace legacy systems, the competitive advantage they will then secure over their rivals could spark a domino effect in the banking industry, and those banks that cannot or do not take advantage of new technologies may be left by the wayside.

The potential for core systems replacement to deliver improved customer service and efficiencies has already been demonstrated in emerging markets. Banks in Asia and Eastern Europe have skipped the technology generation gap by installing more advanced systems, meaning that now even the biggest external players are struggling to compete and gain a foothold in these territories.

Aside from the obvious driver of delivering better products and services, the need for core systems replacement is also induced by a raft of business pains caused by existing legacy systems — not least the high cost of maintenance. Many banks are operating on IT systems which were built in the 1970s. This means they are operating on systems that were originally designed primarily as processing/accounting systems; while consolidations and acquisitions in the banking

industry have also led to banks running parallel, siloed systems with disparate data held in different applications across various sites.

Add to this a history of customization and a dwindling pool of programmers with the expertise needed to maintain legacy systems and it is no surprise that the Tower Group estimates that of the $180M invested in core systems in 2004, 85 percent of expenditure was on maintenance costs.

Get Rid of the Old?

Legacy systems present banks with a problem rooted, literally, at the core of their business. Whether they face bridging a technology generation gap related to hardware, application software, software infrastructure/design, or the need to address an outdated IT architecture that inhibits the business, addressing this problem will be a long and painful process. And many banks are hesitant to embark on a wholesale overhaul of the processes that form the backbone of their enterprise.

The risks of wholesale core systems replacement were demonstrated by a few high profile failures in the 1980s and 1990s, and the costs of such replacements are high. So banks are right to be cautious in their moves to address the problem. However, new tools, such as SOA, that are driven by services and customer information — rather than financial transactions — offer huge benefits. The technology now exists to allow efficient data alignment, information movement, wide access to data, and collaboration inside and outside the bank with customers and partners. These benefits, combined with the fact that the longer legacy systems are in use, the more maintenance costs will increase and competitive advantage will erode, present a strong case for core systems replacement sooner, rather than later.

What Should Banks Do?

In order to address systems replacement effectively and minimize both risk and expense, banks are rightly looking at core systems replacement in a modular, incremental manner. Banks must first assess where exactly the problems impact across the business. They must look at internal/external operating costs, operational/compliance risk, business retention/growth and overall performance, profit margins and new revenue generation. All are impacted by outmoded, inflexible IT infrastructures. Existing core systems may also inhibit the effectiveness of enterprise application integration (software integration or EAI) and straight-through processing, prevent banks from making effective use of outsourcing, and even impede their ability to communicate with their partners in the 'multi-enterprise' value chain.

Secondly, banks should assess which are the priority areas for systems replacement to address their prevalent business pains. Customer service/CRM and process integration are often cited as primary areas for systems replacement, but priorities could also be risk management, regulatory reporting, payments or accounting — depending on the bank's own priorities and the peculiarities of its particular proprietary core systems.

Some banks are taking a geographical approach to the implementation of core systems replacement with an 'outside-in' strategy that sees smaller regions introducing new systems which are then rolled out across the larger markets. Another approach is to replace core systems across individual lines of business, although for many banks this represents a massive undertaking in itself.

Transition: A Smooth Process

Regardless of how a bank breaks down the task of replacing core systems, one area that must be central to any systems change is process

integration. Process integration solutions should form the basis of any effective migration from legacy systems to new technologies, and as such, it is the process integration capability that must be addressed as the starting point of any core systems replacement.

As well as extending the life of core systems by providing the means to link existing disparate systems, process integration provides the bridge to span the technology generation gap. By integrating existing systems to interact seamlessly with new solutions, process integration is fundamentally important in enabling the incremental migration to new systems. It also reduces the inherent risks of adopting a new system by enabling and managing the parallel running of old and new systems. This allows banks to test the robustness of the new solution in a real world environment, while simultaneously maintaining the old system to provide a fall back contingency should problems occur.

In the course of an incremental replacement it remains essential that new systems can function in the existing (legacy) environment; otherwise, new technology becomes just another silo. Process integration meets this challenge by providing the means to translate new system outputs in line with existing system requirements, enabling benefits to be delivered from day one of implementation.

As well as these internal benefits, process integration ensures that a bank's collaborative partners in its multi-enterprise community are not adversely affected through translating new systems' output to the right formats for use by correspondent banks, customers and other external systems. In the modern banking environment, this ability to ensure that core banking replacement does not impact negatively upon partners in the banking ecosystem is of central importance. Collaborative relationships between banks, their corporate customers, community partners etc, cannot be put on hold while a bank addresses its own internal legacy system issues.

Process integration provides the means to smoothly and safely manage the replacement of core systems in such a way that internal processes are not disrupted, new systems can be tested effectively, and relationships with customers and business partners remain functioning effectively. Process integration ensures that the highest ROI is delivered quickly and with minimum risk.

Whether the banking industry is on the verge of sweeping changes to core systems is a subject of much discussion, and has been for some time. But two things are certain: first, the business need for core systems replacement is very real; and second, process integration will provide the most effective means of managing the transition to new systems and is the key to unlocking the huge business benefits and competitive advantage that these new technologies promise.

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