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WHITEPAPER

Filling the Void to Meet Accountholders' Cash Flow Needs

Addressing liquidity could be the key to long-term deposit growth amid changing consumer expectations

Growing deposits is a perennial concern for financial institutions. Meanwhile, younger generations increasingly want financial institutions to address issues that have not historically been front and center in their product offerings. In particular, they are concerned about cash flow issues. Changing regulations around overdraft protection products offer financial institutions an opportunity to rethink how they are addressing this persistent customer need.

As the Pew Charitable Trusts recently noted in an issue brief, "Although nearly all large banks have improved their overdraft policies to make them less costly for customers, the new small-dollar loans from banks still provide a much safer and less expensive way for consumers to meet their credit needs."[1] Institutions that effectively address the issues at the core of liquidity challenges could meaningfully improve their market share over the long run.

In 2023, Arizent, parent company of American Banker, surveyed 1,000 adults on behalf of Fiserv to understand the U.S. landscape for banking and checking. In particular, the research explored when and why consumers need emergency funds, and where they turn when they do. The results suggest financial institutions with a suite of short-term liquidity products geared toward managing cash flow needs could be much better positioned to meet the evolving needs of consumers than the competition.

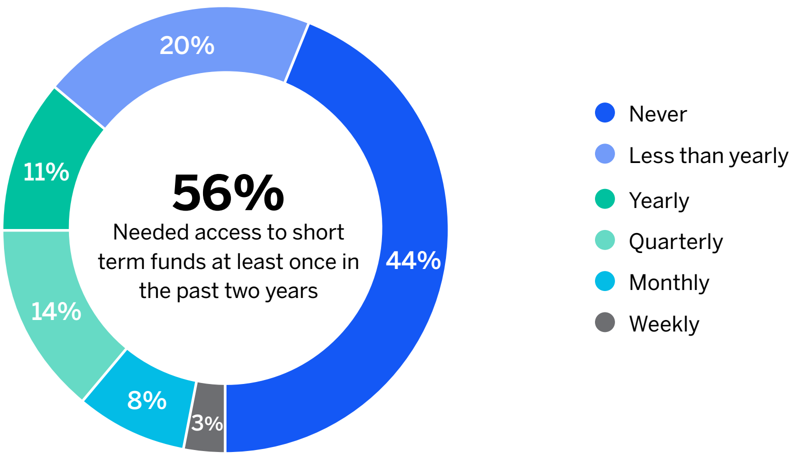
> **Over the long run, solving the liquidity issues that cause overdrafts will be more beneficial for both financial institutions and their customers than simply reducing fees."**
>
> — **Jeff Burton**, VP and General Manager at Fiserv

[1] https://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2023/05/affordable-credit-poised-to-save-consumers-billions

Access to emergency funds means peace of mind

Many people find themselves scrambling to find enough money to cover short-term expenses. In the past two years, just over half of consumers say they have needed access to short-term emergency funds to pay their bills (see Figure 1). While lower-income consumers are more likely to indicate they need funds, they're far from alone. Nearly half of consumers earning between $100,000 and $149,000 (48%) say they have needed access to short-term emergency funds at some point in the past two years.

Figure 1: In the past two years, more than half of consumers needed access to emergency funds



Source: Arizent/American Banker, 2023

In fact, according to the Federal Reserve, 37% of adults faced with an unexpected expense of $400 say they would not be able to easily pay the bill with cash or its equivalent. Most would wind up either having to sell something or to borrow money from family members, payday lenders or their credit card company to pay their bills. A portion of them would not be able to pay the bill at all.

Big-ticket expenses like unexpected car repairs or home repairs are the most common reasons provided for short-term emergency funds needs in the past year. Food and utilities are also common reasons to tap emergency funds, especially among lower-income consumers. Healthcare expenses, payments for housing and overdue bills are also commonly cited causes for turning to emergency funds.

Easy, inexpensive access to liquidity can help address short-term cash flow needs

Regardless of why people need the money, the most common sources of short-term emergency funds are friends and family, overdraft protection services and personal lines of credit. Of these, people tend to say they are happiest with friends and family, personal lines of credit and buy-now-pay-later services. Costs and fees are generally the top concern when looking for the right solution, followed by privacy, immediate availability and easy understanding of how the loan works.

As institutions think about ways to address these concerns, it's important to remember two key things:

1. It's difficult to plan ahead for an emergency. Financial institutions need to be prepared to provide customers the help they need when they need it. Having a suite of easily accessed solutions on hand can provide peace of mind to customers choosing among institutions with otherwise similar product offerings.
2. Cash flow is not necessarily linked directly to a customer's net worth. While products that address short-term cash flow needs can have great appeal for younger or less-wealthy customers, they offer real value to customers across all generations and customer segments.

New regulations are changing overdraft protection

Overdraft protection programs have historically provided a way to manage short-term cash flow problems. While these programs have been popular, they haven't been well publicized. Respondents report that they have rarely been asked to opt into overdraft protection at the time of account opening. Among those who were given an option to opt in, however, 60% took the coverage.

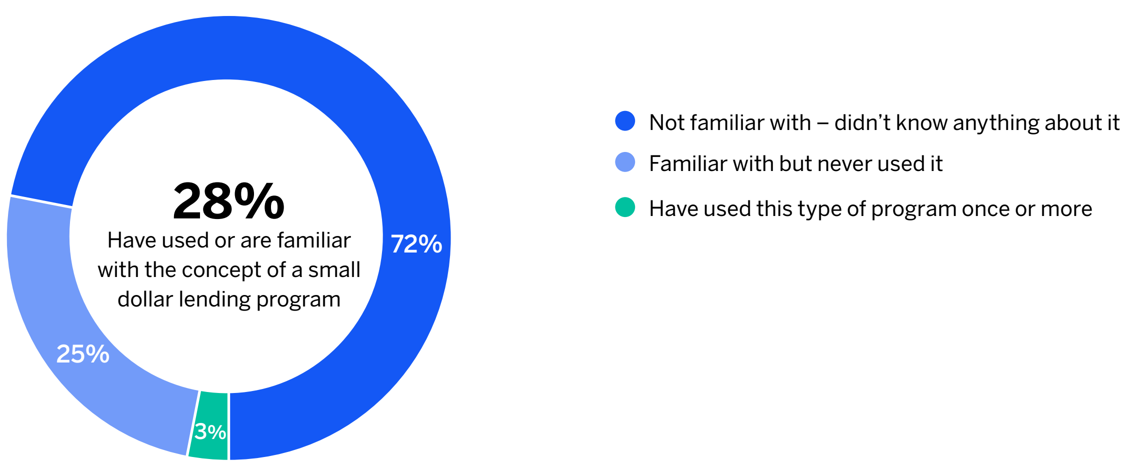
Pending regulations governing overdraft fees could lead to some institutions' apprehension to weigh the overall overdraft risk with the loss of revenue at a time when deposit growth is imperative. More than a third of account holders have experienced an overdraft in their primary checking account in the past year. Among Gen Z, that number rises to more than half. Many of these customers are exactly the ones institutions need to engage to grow deposits over the long term.

Offering smart alternatives to overdraft protection

The value of offering cash flow products goes well beyond replacing revenue streams from overdraft protection fees. As they consider adding cash management products to their offerings, financial institutions need to consider the value of driving engagement and customer loyalty as part of their ROI calculation.

Small-dollar lending programs typically offer flexibility in terms of the timing and amount of repayment options, an extremely important concern for consumers who frequently feel strapped for cash. Very few people have actually used these programs, however (see Figure 2).
The lack of exposure to these products represents an opportunity for financial institutions to provide an effective solution that their customers often don't know exists. Those who have used these programs tend to use them frequently

Figure 2: Few consumers are familiar with the concept of small-dollar lending



Source: Arizent/American Banker, 2023

and enthusiastically. Nearly three in four (73%) who have used these programs have done so in the past two years, and nearly half (45%) have used them at least quarterly in that time frame. And 48% of those who have ever used a small-dollar lending program say it was better than any other small-dollar lending options they've used. A little education could go a long way as well. Four in 10 consumers say they would use a small-dollar lending program at least yearly, including 30% of Gen Z consumers. These programs could also be an attractive tool for deposit growth: 44% say a small-dollar lending program would lead them to consider switching financial institutions.

Immediate access to cash creates a better customer experience

Financial institutions can also mitigate concerns about new regulations on overdraft protection by reducing the conditions that cause overdrafts in the first place. Making customers wait for urgently needed funds to clear can create unnecessary difficulties and make people feel like their financial institution doesn't trust them. By contrast, giving established customers immediate access to their deposited funds promotes a sense of fairness and trust, creates a better customer experience and helps build loyalty. It also helps customers avoid overdrafts and helps obviate the need to tap high-cost short-term credit solutions.

In combination, small-dollar lending programs and solutions that reduce the conditions that cause overdrafts give financial institutions tools that fill a potential void in a new overdraft environment. They also give institutions a way to offer depositors more flexibility than the competition, keeping customers better engaged over the long term as they build and inherit wealth. With younger generations estimated to inherit more than $70 trillion according to Cerulli Associates, that engagement becomes more important still. Banking habits and preferences aren't a part of that inheritance.[2]

Consumers are encountering an ever-greater number of banking options. At the same time, the experiences those institutions offer them increasingly seem faceless and interchangeable. In that environment, customer experience matters. Financial institutions that implement the types of programs customers want but aren't getting from the competition will have an advantage, especially when it comes to younger generations. As these attractive products become table stakes, they also will become key elements of a financial institution's efforts to attract deposits. When products like overdraft protection become more difficult to obtain, the value of these other products will rise further.

A well-constructed suite of liquidity products can help customers of all types, improving the banking experience, driving engagement and loyalty, and ultimately supporting deposit growth. But these products absolutely must be tailored to a specific institution's customer needs. Third-party vendors with extensive knowledge of proven solutions can help ensure financial institutions implement the right set of products to build a better future alongside their customers. "At Fiserv, we've seen voluntary account closures unrelated to charge-offs decline over 30% after implementing new overdraft strategies and alternatives to traditional overdraft solutions," notes Burton. "We have also seen a reduction of over 40% in charge-offs related to accounts entering into overdraft when financial institutions offer alternatives such as short-term credit."

Because these solution sets are typically built to industry standards and already in use at other financial institutions, third-party vendors can also help institutions avoid implementation pitfalls, ease integration with existing systems and preserve valuable technology resources for other initiatives.

"Implementing flexible products that offer attractive and fair services to customers is a win-win for financial institutions and consumers over the long-term, especially as younger generations build and inherit wealth," says Burton.

[2] https://www.cerulli.com/press-releases/cerulli-anticipates-84-trillion-in-wealth-transfers-through-2045

Methodology

This research was conducted online during August-September 2023 among 1,000 consumers. The survey was balanced to match the U.S. population based on age, income, and gender.

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