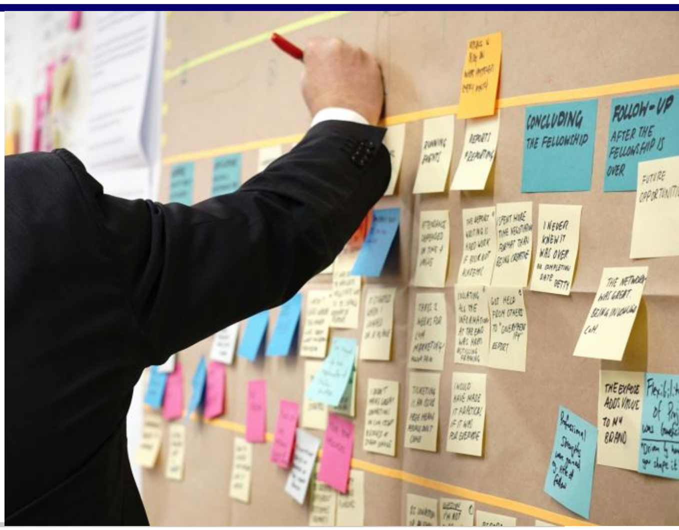
BANKING STRATEGY SERIES · ARTICLE 2

Institutional Friction Impedes Innovation



"Most banks don't struggle to develop good ideas, but instead struggle to move good ideas through the organization."

By Abelian Partners

CONTEXT

In its previous Article 1, Abelian argued that strategy is only valuable when it creates meaningful change. Yet many strategic initiatives lose momentum long before reaching clients due to institutional friction.

WHAT IS INSTITUTINAL FRICTION?

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Institutional friction is the accumulated resistance to change that naturally develops inside every successful organization. Every bank has it. Institutional friction emerges from the organizational structures, competing priorities, and natural complexities of running a modern financial institution.

In many ways, institutional friction is the byproduct of being well-managed. Banks are designed to bring multiple perspectives into important decisions. Business leaders evaluate commercial opportunity while risk managers consider uncertainty. When it's time to fund, finance leaders price the cost of money. These three functions - business, risk & finance - are the traditional "three-legged-stool" of a bank organization. Supporting this triangle is the technology group focused on enabling automation, while the back-office organization determines how to make the wheels turn. And the support functions continue – human resources, legal, compliance, etc. All these functions run within a traditionally risk-averse culture, where having independent perspectives traditionally makes better lending and business decisions.

The challenge is not that these independent perspectives exist. The challenge occurs when these functions work against each other and slow down innovation - instead of working together from the beginning.

THE EXPERTISE BOTTLENECK

The Expertise Bottleneck

Too often, a strategic initiative moves through a banking organization one function at a time without true cross-functional product expertise. Each function evaluates the opportunity through its own lens, asks reasonable questions, and recommends thoughtful changes. By the time the initiative has been examined by all groups – almost like a game of telephone tag - assumptions have shifted, priorities have changed, and work completed weeks earlier must be revisited. All too often, the true commercial value (and the risk) of an initiative is lost in the morass of process.

> **The result is not better execution. The result is rework and lost opportunity.**

As banks try to innovate within this framework, projects often slow and ownership becomes less clear. Teams begin solving different problems and momentum fades long before clients experience the intended value. Overall, the expertise and ownership of true innovation is lost and initiatives flounder due to this institutional friction.

This pattern is damaging precisely because it often goes unrecognized. Each team is doing exactly what it is supposed to do, but there is no "tip of the spear" expert driving completion. The problem is structural and hard to solve.

COORDINATION & PRACTICAL EXPERTISE

Coordination & Practical Expertise

Reducing institutional friction is not about eliminating governance or making decisions faster at the expense of quality. Rather, the disparate areas of the governance model must be *coordinated*. And this coordination needs to come from a knowledgeable innovation owner that can align resources to a practical outcome. The key is to create continuous cross-functional alignment before implementation begins - and then maintain that alignment throughout the life of the initiative.

Coordination starts by asking the right questions together, and earlier in the process than most institutions currently do. *What problem is being solved? What value is being created? How will success be measured? What barriers are most likely to prevent success?* An owner that can see the full 360-degree view of an initiative needs to drive this coordinated process. Certainly, risk and capacity must be considered, but coordinated practical expertise will drive better risk evaluation than independent siloed analysis.

These coordinated conversations cannot happen only during strategy development, but must continue throughout implementation. As work progresses, assumptions should be challenged and execution refined based on what the organization is learning. The practical owner should champion the earliest stages of design through to the final stages of delivery.

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SUSTAINED EXECUTION

Sustained Execution

Institutional friction will always exist. The goal is not to eliminate it, but to turn it into an advantage. Most start-ups yearn for the capacity and practical expertise a financial institution already has within its ranks. But just as Xerox didn't recognize the technology of the "mouse" inside its innovation lab the early 1980s, so do banks often miss the forest for the trees. And innovation often dies within a process-centric set of bureaucratic committees.

Winning institutions will identify internal innovation owners with practical expertise to drive tangible outcomes. Those owners must then coordinate the myriad of internal bank functions and harness the power of that combined internal knowledge. As those resources then empower the innovation owner, visionary progress can be realized. And this cycle can be repeated – turning the components of institutional friction into a coordinated team.

> **The goal is to harness that which creates institutional friction and to ensure that it improves decisions without slowing progress.**

The banks that master this distinction build an institutional capability—a repeatable way of working that makes innovation a continuous strategy rather than a periodic event.

COMING NEXT

The next article will explore how leading institutions build sustainable innovation programs that make this way of working repeatable, allowing strategy to become a continuous capability rather than a periodic event.