FinTech—Origins and Prognosis

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National Association of Certified Valuators and Analysts

Greater Disruption and Change Awaits the Financial Services Industry

FinTech, or financial technology, has disrupted the financing industry. The FinTech revolution has not only changed the financial services industry, but it has also changed specific sectors, including: retail banking, lending and financing, payments and transfers, wealth and asset management, markets and exchanges, insurance, and blockchain transactions, just to name a few. It will continue to be vital for those who work in such sectors to learn how the FinTech revolution affects them immediately, as well as their future careers and business dealings. This article traces and history and shares the author's thoughts on how the industry will evolve and impact businesses and those seeking financial resources.

Before the term "FinTech," financial technology was already pervasive, it had not yet become so pervasive that this evocative, *facon de parler* had permeated the popular and financial press. Retail-level examples of early FinTech include on-screen trading and robo-advising. Recently, for example, the applications of blockchain, a form of FinTech, have appeared in securities trade clearing, paying debts to friends through Venmo, and instant international money transfers [www.goabra.com]. To look at the early evolution of FinTech, we could start at "the invention of the pantelegraph in 1865" [Backstop Blogs, 2016]. A few more recent financial technology features that were apparent long before now include the following: The Bloomberg Terminal (founded in 1982), Murex (founded in 1986), and PayPal, itself, has allowed us to transfer money since 1998 [Backstop Blogs, 2016]. The next sections will examine the importance of recent FinTech developments and offer a prognosis about its future.

What is FinTech?

Discussing the FinTech revolution, a pundit opined, "We have entered the most profound era of change for financial services companies since the 1970s brought us index mutual funds, discount brokers, and ATMs" [BI Intelligence, 2016]. Not only has the term FinTech exploded on the scene in recent years, but also the potential disrupting effect of FinTech innovations on traditional financial institutions has gained notice. This invokes the question, "What exactly is FinTech?"

The term refers to "an industry composed of companies that use new technology and innovation with available resources to compete in the marketplace of traditional financial institutions and intermediaries in the delivery of financial services" [Wikipedia, 2017]. In other words, FinTech encompasses businesses that utilize new software, modern technology, and other innovations that enable them to best compete in the financial services industry, often alongside and sometimes against such competitors as traditional financial institutions.

Consisting of both startups and established financial and technology companies, FinTech companies try to "replace or enhance the usage of financial services of incumbent companies" [Wikipedia, 2017]. One of the main goals of FinTech companies is to sell financial services and similar solutions to traditional bank customers, thus, directly competing with banks. Traditional banks continue to struggle to keep up with FinTech companies and their speed of innovation, mostly because of regulatory reasons and their internal structures. One bank, though, JP Morgan [JPMorgan, 2016] is embracing the FinTech space, vigorously, by hosting conferences, as well as launching an in-house incubator. FinTech startups have taken full advantage of this area where traditional financial institutions have clearly fallen short because they recognized, early on, that "financial services of all kinds—including money transfer, lending, investing, payments…—need to seamlessly integrate into the lives of the tech-savvy and sophisticated customers of today to stay relevant in a world where business and private life become increasingly digitalized" [FinTechweekly.com, 2017].

Why is FinTech Important?

FinTech Disrupts an Entire Industry

FinTech has disrupted the financial services industry, while also changing financial technology forever. With new startups in the FinTech field sprouting up at a rapid rate, more innovations are constantly underway, which makes it harder for more traditional institutions in the financial services to keep up. For these reasons, there may be even greater disruption to come soon, which no firm will be immune, therefore, even less financial, "tech savvy" firms "must have a strategy to harness the powerful advantages of the new financial technology revolution" [BI Intelligence, 2016]. Still, FinTech will continue to be a major disruptive threat to the financial services industry, despite any firm's greatest strategic efforts, because it most assuredly changed "the nature of almost every financial activity, from banking to payments to wealth management" [BI Intelligence, 2016]. The FinTech revolution has not only changed the financial services industry as a whole, but it has also changed specific sectors, including: retail banking, lending and financing, payments and transfers, wealth and asset management, markets and exchanges, insurance, and blockchain transactions, just to name a few [BI Intelligence, 2016]. It will continue to be vital for those who work in such sectors to learn how the FinTech revolution affects them immediately, as well as their future careers and business dealings. Furthermore, those employed in the digital economy will want to take full advantage and exploit the new technologies that are ever-growing within the FinTech industry, to make their employers more profitable, efficient, and flexible [BI Intelligence, 2016].

FinTech Initiates a Battle Among the Best

The FinTech revolution has been compared to "a battle" among power-players, old and new, where there will be obvious winners and losers among some of the most influential names in the financial world. However, this battle will create great potential for various growth opportunities and new cost savings for businessmen and women, along with their companies [BI Intelligence, 2016]. Furthermore, within this battle, "the most contentious conflicts (and partnerships) will be between startups that are completely reengineering decades-old practices, traditional power-players who are furiously trying to adapt with their own innovations, and total disruption of established technology and processes" [BI Intelligence, 2016].

The power-players in this battle include: 1) Traditional Retail Banks vs. Online-Only Banks—"Traditional retail banks provide a valuable service, but online-only banks can offer many of the same services with higher rates and lower fees." 2) Traditional Lenders vs. Peer-to-Peer Marketplaces—"P2P lending marketplaces are growing much faster than traditional lenders; only time will tell if the banks strategy of creating their own small loan networks will be successful." 3) Traditional Asset Managers vs. Robo-Advisors—"Robo-advisors like Betterment offer lower fees, lower minimums and solid returns to investors, but the much larger traditional asset managers are creating their own robo-products while providing the kind of handholding that high net worth clients are willing to pay handsomely for" [BI Intelligence, 2016].

When discussing the FinTech revolution, the major conflict will be between old and new firms. FinTech startups are reconfiguring financial services and processes from top to bottom. More traditional firms are trying to devise their own new products without undue cannibalization.

FinTech Has Forever Changed the Business World

Whether consumer or business, FinTech provides a variety of benefits for each of its customers, especially due to the increased speed and accessibility it offers. When explaining the major benefits that businesses have gained during the FinTech revolution, Landers [2017] says it best, "Utilizing much faster, always on Internet connections, big data computing, and mobile connectivity, businesses are now able to buy in to complex, feature rich financial software suites and managed services that a decade ago would have cost millions of dollars in setup fees for equipment, program licenses, and trained technicians, not to mention the IT team to manage the whole solution." Taking advantage of such resources allows businesses to also share those benefits with their customers, allowing them to continuously improve their customer experience. Thanks to the FinTech revolution, "greatly improved software designs and user experiences, fast internet bandwidth, and the universal adoption of smartphones has provided real-time access to financial information and transactions at a level never before possible," which "has led to the rise of omnichannel payments processing, mobile banking, peer-to-peer payments, and even new ways of evaluating credit applications" [Landers, 2017]. The efficiency and immediacy benefits that the FinTech revolution brought the business world will likely continue apace.

New Ventures/Crowdsourcing

Historically, a new business would turn to a bank or an angel or venture investor. Now, thanks to FinTech, new modalities, such as crowdsourcing have emerged as invaluable resources for entrepreneurs. Crowdsourcing, a popular method of obtaining business funds "allows people with big ideas to get funding quickly and easily from anywhere in the world from people they have never met" and "instead of months of investor talks, entrepreneurs can —thanks to the shop-window that is the internet—pitch directly to the world" [Landers, 2017]. Therefore, current entrepreneurs can often see potential funds within a matter of weeks, opposed to months or longer.

Even transferring money across borders has become much easier through such innovations as TransferWise, which has "turned the traditional (and expensive) banking solution to sending money across borders on its head and enables small firms and individuals to transfer money far cheaper than was previously possible" [Landers, 2017]. Also, in the international field, in countries where legal title to property and land is problematical, blockchain approaches guard against easy expropriation [https://bravenewcoin.com/news/factom-tackles-land-title-disputes-with-bitcoins-blockchain/]. There are a number of other examples of how FinTech has changed business transactions and property tracking. Most importantly, FinTech continues to save on major costs, while continuing to change the business world and financial services industry, since FinTech firms do not have the same overheads and regulatory responsibilities that traditional organizations have. Similarly, the small size of FinTech companies often allows them to continuously be innovative in ways that larger, more traditional firms cannot.

FinTech Customer Evolution

Thanks to the rise of the smartphone, customers' daily behavior changed, as we have become a culture that is constantly online, especially due to the abundance of apps and services that feed our online obsessions. Anyone with a smartphone can access endless information. Most importantly, the FinTech revolution helped turn the very same device millions of people use daily, a mobile phone, into a “point of sales” system that offers “millions of businesses and individuals the chance to take payments just like the larger corporations they compete with” [Landers, 2017]. Being able to utilize a mobile phone as a point of sales device also “provides a unique insight into their customers through sophisticated analytics tools previously available only to larger businesses.” FinTech “is a great leveler” because it allows small firms to better compete with larger ones, since customers expect the same range of services from both small and large firms [Landers, 2017].

People now expect to handle most, if not all, of their financial affairs with the same ease as they would their social media or e-mail accounts. “Especially millennials (people born between approx. the early 80s and late 90s) and the following generations prefer quick and easy banking services over walking to a branch, appointments with bank consultants and lengthy processes setting up accounts or putting together a portfolio (as two of hundreds of examples where mobile and digital banking services allow for a more frictionless and stress-free process)” [FinTechweekly.com, 2016]. Having the right FinTech services in place is not only vital, but a major opportunity for all businesses and soon, no business will prosper without it. Therefore, it is quite clear, the “future” of business is in FinTech, but one may ask, “Where exactly is FinTech leading us in that future?” This leads us to our final discussion, where is FinTech going?

Where is FinTech Going?

Seven Factors Shaping FinTech’s Future

“FinTech companies should prepare for a rapidly shifting market driven by new regulations and changes in consumer behavior, according to a report by McKinsey & Company” [Kuepper, 2016]. That said, according to Kuepper, for companies to succeed in this future, seven major aspects have been outlined, including the following: expanding scope, increasing diversity, improving collaboration, impending consolidation, normalizing valuations, shifting regulations, and emerging ecosystems.

First, as for expanding scope, the FinTech industry has not only “expanded into more than thirty different financial services throughout the value chain,” but continues to grow substantially since this article was written. Trends in this area point to “increasing competition for robo-advisors and traditional financial advisors, as FinTech companies involved in ancillary financial services add advisory services to their core product offerings. Continuing to draw from Kuepper, an example can be seen with social finance (sofi.com), a business that has grown from offering financial products to young professionals, and then expanded to career coaching and networking. This leads us into our next factor: increasing diversity.

Secondly, when increasing diversity, FinTech companies are choosing a great variety of business models that target a diverse range of customers. An example here is when “robo-advisors target younger, tech-savvy clients looking for streamlined retirement savings, while other models focus on helping financial advisors offload time-consuming tasks like portfolio rebalancing and focus on value-added activities.” On the other hand, this leads us to our third factor, improving collaboration, which in order to maximize their market share and revenue, FinTech companies have been collaborating with each other and will continue doing so in order to reduce overhead costs, while reaching a “wider potential audience and enhance their technological competitiveness.” As Kuepper goes on to give an example, “BBVA Compass is working with FutureAdvisor to offer low-cost financial advisory services to help customers with portfolio optimization.” This now motivates the next factor: impending consolidation.

Fourth, when discussing impending consolidation, it is likely that larger players will turn to acquisitions to meet their growth objectives, while FinTech firms will see consolidations. For example, “Prosper Marketplace spent $30 million to acquire BillGuard, renamed it Prosper Daily, and enabled users to track spending and credit.”

This leads us to our fifth factor, normalizing valuations, whereas the FinTech industry is beginning to mature, meaning it is actually starting to slow down and valuations for start-ups in FinTech are also slowing down. Therefore, a slower growth could potentially lead to “fewer start-ups and more failures, which means picking established FinTech firms might be a wiser choice” [Kuepper, 2016]. When it comes to best explaining the maturing industry of FinTech, Kuepper points out, “Between 2014 and 2015, valuations for FinTech companies grew by 77% on average before slowing to nine percent between 2015 and 2016.” This leads us to our sixth factor: shifting regulations.

Sixth, when shifting regulations, the same regulations surrounding the financial services industry have begun to adapt to FinTech companies, “and in some cases, these regulatory changes could hurt FinTech companies that have effectively circumvented existing rules.” Therefore, such legal matters will continue to be an ongoing issue that FinTech must address to continue effectively doing business. Last, but not least, this leads us to the seventh factor, emerging ecosystems, which, in order to continuously meet their clients' needs, FinTech firms may begin developing their own ecosystems. An example here is that “peer-to-peer loan providers may eventually decide to branch out into financial advisory businesses since they serve the same client base” [Kuepper, 2016].

Conclusion

In conclusion, though the term FinTech is new, financial technology is not. FinTech has roots from the invention of the pantelegraph in 1865, and a series of events took place after that, which evolved into FinTech, as we know it today. That said, FinTech has been a major phenomenon, almost from the moment, the term, itself, became a “big thing” in 2015. Probably, one of the simplest ways to define it is an industry that represents such businesses that utilize new software, modern technology, and other innovations that enable them to best compete in the financial services industry, often alongside and sometimes against such competitors as traditional financial institutions.

FinTech's role in financial services is important to study because it is disrupting the entire financial services industry. The burgeoning presence of startups, incubators, and in-house innovations will likely create the need for specialized FinTech valuation professionals and databases.

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