Markets and business models under pressure: Fintech’s impact in the real economy

Pier Luigi Gilibert, EIF Chief Executive
Rome Investment Forum – 16 December 2017
1. Fintech definition from FSB

“Technologically enabled financial innovation that could result in new business models, applications, processes, or products with an associated material effect on financial markets and institutions and the provision of financial services”.

Financial Stability Board (FSB)
Financial Stability Implications from FinTech: Supervisory and Regulatory Issues that Merit Authorities’ Attention
June 2017
## 2. Disruptive technologies enabling the rise of Fintech

<table>
<thead>
<tr>
<th>Technology</th>
<th>Year</th>
<th>Description</th>
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<tr>
<td><strong>Mobile (smart) phones</strong> (2007)</td>
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<td>iPhone was introduced in 2007. Mobile phones free the users of financial services from having to go to fixed service locations.</td>
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<td><strong>Blockchain / DLT</strong> (2008)</td>
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<td>Blockchains allow to process (smart) contracts and transactions outside the traditional intermediary system relying on banks, freeing both users and providers of financial services from maintaining and protecting multiple ledgers of transactions/contracts.</td>
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<td><strong>Artificial intelligence (AI)</strong></td>
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<td>The term AI was first coined at the Dartmouth conference in summer 1956. Since 2000, a major leap forward in developing AI / ML, potentially replacing human reasoning by software application in a wide range of sectors, incl. financial services.</td>
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Source: A. Kirilenko, Imperial College Business School, UK
3. The future of banking belongs to software companies?

Source: A. Kirilenko, Imperial College Business School, UK
4. Regulators’ views and main areas of regulatory considerations

**European Commission**

**Basel Committee on Banking Supervision**

**World Economic Forum / Deloitte**
Beyond fintech: a pragmatic assessment of disruptive potential in financial services. Final report, Jun 2017

**International Monetary Fund**
Fintech and financial services: Initial considerations, Staff Discussion Papers, Jun 2017

**European Banking Authority**
2018 Work Programme – activity 29 (Fintech)
5. What disruptive technologies have done to other industries

- **Retail commerce**
  - Don’t own any shops

- **Urban transportation**
  - Don’t own any cars

- **Hospitality / hotels**
  - Don’t own any beds

- **Air transportation / national carriers**

- **Combustion engine manufacturers**
6. Strengths/weaknesses of current incumbents

**Strengths**
- Low funding costs
- Strong origination networks
- Perception of safety

**Weaknesses**
- Brick and mortar costs
- Outdated legacy systems
- Slow processing
- High staff costs
- No access to talent (loosing talent)

RISE OF FINTECHS
The industry has evolved from direct competition designed to disrupt traditional banking to one of **growing partnerships and integration** between fintechs and banks.

Partnerships between fintechs and incumbents also **outside banking** (e.g. microfinance and crowdlending, BA/VC financing and crowdfinancing).
8. Critical long-term trends shaping financial services

- Technological **advances** and their growing **acceptance** among consumers
- Rise of the **millennials** and **digital natives** with mobile devices and social media as part of their lives
- **Big tech** and **GAFA** interest in expanding into financial services (e.g. Google, Apple, Amazon, Alibaba, Baidu)
- Currently **fintech business models are still fragmented**: there isn’t a single winning formula. Once found, disruption will be overwhelming.
9. What does this mean for EIF?

“The combination of crowd-based activities, social media and automated matching platforms that apply innovative technology may significantly change the way consumer/SME credit is contracted and the way equity investment flows into start-ups, scale-ups and SMEs more generally. Non-bank financing is offering new channels of access to finance for individuals and small companies facing difficulties to tap the traditional banking channels, especially due to the lack of appropriate collateral or …historical credit information”.

European Commission
Fintechs: A more competitive and innovative European financial sector
Public Consultation, 23 March 2017 – 15 June 2017

FINTECH’S PROMISE OF EASIER AND FASTER ACCESS TO FINANCE
CAPITAL MARKETS UNION DIVERSIFYING SOURCES FOR SMES

EIF’S OWN BUSINESS MODEL DISRUPTED
10. EIF opportunities going forward

**REACTIVE**

**DO NOTHING**

No specific actions taken on platform banking, based on the belief that disintegration of banking value chain is unlikely.

**Impact of Profit Pool**
- Potential substantial shrinkage on revenues if universal banking model becomes unbundled.

**PARTICIPATE IN PLATFORMS**

Identify platforms with the greatest potential and participate as product providers on those platforms.

+ Increase in volume by diversifying distribution channels
- Lower margins on products distributed through platforms

**BECOME THE ENABLER OF PLATFORMS**

Provide infrastructure (e.g., account and payment aggregation services) to enable platforms and their participants.

+ Additional volume-driven revenue stream
- Potential erosion of new revenues as the market consolidates, potentially globally

**BECOME A PLATFORM**

Transform traditional integrated business model into a platform and generate value through making connections.

+ Increase in volume by focusing on scale
- Loss of traditional margins from “manufactured” products
- Potential cannibalization of existing revenue streams
11. Possible engagement model – debt financing
12. Possible engagement model – equity investments

- EIF promotes (all*) board-approved fund opportunities to selected ECF intermediary
- ECF (as nominee for crowd) subscription to fund opportunities
- Commitment by EIF as trustee of ECF
- EIF standard commitment
- Man. account / Co-inv. pool
- VC/PE Funds & BAs
- Investment**
- SMEs
- Investment

*subject to fund manager consent
**GP acting as trustee for EIF (in turn as trustee for ECF)
13. Conclusions

- **There is value in fintech for the real economy.** Being aware of shortcomings, EIF is not ignorant of these developments and is exploring ways for the development of its own business model.

- **Regulation: main challenge is to protect the safety and soundness of the financial system** while not preventing the spreading of useful innovations in the fintech sector.

- **Capital Markets Union (CMU) supports these developments** - and the **diversification of SMEs’ financing sources.**
Thank you for your attention