The Banking and Fintech Leadership Forum

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Fintech at an inflection point: consolidation, competition, and partnerships

The global pandemic clearly created risks for banking and the financial system: operations were upended, credit risks multiplied, and the economic impact on businesses and consumers continues to create challenges. It also accelerated some aspects of the broader technology transformation of banking. More customers were forced to embrace digital tools, financial institutions accelerated adoption of cloud-based solutions, and a shakeout among fintechs began, including some significant mergers and acquisitions.

On August 26th, 2020, fintech CEOs and other executives, bank executives and directors, and other industry participants convened virtually for the third Banking and Fintech Leadership Forum hosted by Tapestry Networks and LendIt Fintech. Participants discussed the state of transformation in financial services, where and how collaboration among fintechs and banks might expand, and how the nature of vendor and partner relationships will evolve.

The competitive landscape continues to evolve

Several high-profile deals - Visa acquiring Plaid, Intuit acquiring Credit Karma, American Express acquiring Kabbage, SoFi's acquisition of Galileo, and Lending Club buying Boston's Radius Bank - have captured the attention of industry participants and commentators. But these deals, plus some recent fundraising, demonstrate a growing dichotomy: some large financial institutions are making significant bets, while others worry about capital conservation; some fintechs are struggling through their first real economic and credit cycle, while others have grasped the opportunity to expand; pricing has corrected in some instances, while others see valuations continuing to skyrocket. Forum participants discussed how the market is likely to evolve and whether further consolidation and deal activity was inevitable.

The fallout from COVID-19 will lead to further targeted consolidation

The economic fallout from COVID-19 is likely to intensify M&A activity. Participants identified where that activity is most likely to occur:

- **Selective buyers see opportunities as some firms come under pressure.** The pandemic has adversely impacted some segments of the industry, and some sectors of the economy, more than others, creating openings for acquisitions. An executive observed, *"Small business* *lending just isn't the best sector to be in right now because of the coronavirus. We saw OnDeck get sold and then saw Kabbage get sold to AmEx. I think AmEx smartly looked at the market and saw an opportunity to pick up an asset that's fully built out and has all the tech and a platform, but at this moment in time is maybe a bit cheaper than usual due to the market."*

- **Fintechs may look to combine to gain scale or diversify.** Some fintechs – both larger players looking to achieve real scale and diversify, and those who have seen pressure on revenue growth in the current environment – are looking to combine. *"As things play out, people are seeing where they sit and making determinations. Size, scale, and publicity matter,"* observed one participant. An executive commented, *"We're seeing a bit of a barbell. You've got large players who can raise capital in public and private markets and do M&A. You've then got smaller, niche companies that are combining."* Others are looking for opportunities to enter new markets: *"We're seeing people in digital banking or wealth management saying they want to do more of the other. Companies that do the same thing may also be combining in the market. That's not something you saw in the market previously because perhaps those companies hoped to go public."*
- **Most large incumbents are unlikely to make significant moves.** While some anticipated more M&A as valuations corrected, participants emphasized the challenges for incumbents that will limit significant acquisitions. One said, *"The banks are getting a lot thrown at them at once, especially right now. Even before COVID happened, there were all sorts of accounting and regulatory capital issues that are coming in over the next couple of years. So, in some ways has COVID accelerated their need to find assets again? Yes, but there are some pretty meaningful complicating factors. I think you'll find the vast majority still have too many other things condensing their time."* Another participant stated, *"The bandwidth of the banks is overrated,"* suggesting that they may be challenged to handle significant acquisitions and integrations, or even multiple significant partnerships. A select few number of leading banks and financial institutions may end up making significant acquisitions, however.

Accelerated digitization will change how firms compete

While consolidation and the challenging operating environment are likely to reduce the number of players in the market, accelerated digitization is also likely to alter how the remaining firms compete. Participants described the following trends:

- **Embedded finance will continue to transform the industry.** Embedded finance is likely to create further disruption, particularly for less nimble incumbents. One fintech CEO stated, *"The pace of non-FIs providing financial products is accelerating, with Google accounts being the latest classic example of that. It's amazing to see so many financial institutions who don't even understand what these products or trends are. This whole idea of embedded finance is* *very real, it all comes down to who has mind share with customers. Banks don't get mindshare from us, other platforms do."*

- **Increased digitization will lead to more personalized offerings.** The accelerated deployment and adoption of digital tools will accelerate the trend toward more personalized products and services. *"As I think about what the world looks like for financial services 10 years from now,"* a fintech CEO said, *"All of this is gravitating towards hyper-personalization. Whether you're a fintech, a bank, or tech company, whoever can give an experience and solution set that meets the customer's needs the best and simplifies their life will get the eyeballs."*
- **Fintechs increasingly need to find a path to profitability.** Many fintechs adopted a "growth at all costs" strategy often with the support of the private and public markets. As some of these firms now face financial difficulties, some fintechs are facing pressure to accelerate the path to profitability in order to demonstrate the sustainability of their model. A fintech executive shared, *"Expanding without profitability is absolutely not an option anymore, so you constantly have to ride that fine line of doing innovative things and being exciting while also being profitable. It's a challenge to do everything everyone wants right now and you're pulled in three different directions."*

Bank and fintech partnerships remain attractive, but both parties are more selective

Opportunities for collaboration among banks and fintechs remain attractive; serving large financial institutions in some form is now the core model for many fintechs, even for many of those who started out as competitors to incumbents. As one fintech CEO said, *"I just think there's a real partnership opportunity here for the fintechs and banks. What do the big banks need? One thing is the tech stack, the other is [fintech] management's view of how to go after those businesses. Companies like Chime have an insane focus on the customer experience, and that's what banks are missing."* The rationale for partnerships seems clear, but how banks and fintechs approach these opportunities is evolving. As one bank executive noted, building a true and effective partnership remains elusive: *"In my experience, it's a bit of a needle in a haystack finding two counterparties that can find common ground at the senior levels of the two organizations."*

Banks have accelerated development of their own capabilities

The pandemic has accelerated some aspects of technology transformation at large banks, while also increasing bank leaders' confidence in their ability to move quickly and develop and execute new solutions. As a result, they are likely to be more selective regarding opportunities for partnerships with fintechs.

Banks have drawn some lessons from the crisis

Some participants from large banks shared their perspectives on lessons gleaned from their institutions' experience through the pandemic:

- **Banks can act more like fintechs.** Banks that were able to respond effectively to the initial phases of the COVID crisis, including supporting existing customers and executing against government lending programs, made them more confident in their abilities to be agile. A senior bank leader explained, *"The last few months have taught us that we all need to speed up everything we're doing, and I think that has awoken the eyes of people who hadn't seen it before. Speed is so critical."* A bank executive said, *"PPP has showed us here that there is a different way to do things that we should've done a hell of a long time ago… We went out and looked at the very best technology at the start of this. We concluded that if we could do things differently in terms of clarity of focus, there was no reason why we can't deliver things at pace, at cost, and better than anyone else. And we did."*
- **Banks are investing in internal capabilities.** According to one bank executive, *"We are going to have a 250 person team working on just app development for the bank,"* a bank leader explained, *"So if I look at the increasing amount of pain it takes us to partner versus just using the large app development team, you have to ask what's the best use of my team."*

Banks are looking for partners with aligned expectations

Banks do, however, see a place for fintech to help them. Bankers identified the following key considerations when they explore partnership opportunities in this new environment.

- **Scalability.** For large financial institutions, any potential collaboration needs to be scalable to garner senior leaders' attention and justify the work involved to make it successful. A banker said, *"What do banks struggle with? It's defining what the opportunity is that we can scale."* Another senior banker agreed that this could provide an opening for fintechs looking to partner: *"You can build solutions internally, but it can be really difficult to scale them. Sometimes it's easier to scale from outside, actually."*
- **Targeted solutions.** Banks have faced criticism for their outdated legacy systems for years, prompting some to call for a more comprehensive "rip and replace" approach. But several participants suggested more targeted applications that can be built on top of existing platforms were more likely to be adopted, especially in the current environment. One senior banker shared, *"We're not talking about doing any of the mega billion investments. There are three very specific areas we're looking at: client engagement, investments, and financing."* Another banker agreed, *"PPP has really clarified what we can*

do as a firm. We do need help, but I think it will be in a much more precise and targeted manner, and probably will be with more mature players."

- **Established relationships.** A banker stated bluntly, *"If you're focused on exit, focused on series B, I'm most likely going to work with my team for the next few years and partner with whoever is going to buy you, because I don't have the time to waste."* Several also said they were more likely to work with fintechs in which their banks' venture teams are invested. That brings a degree of vetting from a trusted source and means they get the benefit from any equity upside to the fintech as well.

Fintechs debate engagement models with banks

Accelerated digitization is creating opportunities for fintechs to work with banks. As one fintech CEO said, *"We're seeing many companies focus on digital solutions… It's been interesting to see these firms prefer not to build a separate busines unit or digital bank, but rather digitize their current services."* Another fintech leader added, *"If there's anything else that COVID has shown, it's that banks appreciate the importance of having fully digital products."* Participants shared different perspectives regarding how fintech relationships with banks can be of greatest value:

- **Fintechs must demonstrate value to potential bank partners.** A fintech CEO stated, *"I don't think it's controversial to say that it's on the fintech to make a partnership really compelling for a bank. Has there been a shift in partnerships due to COVID? Sure. But banks are always going to want to leverage their internal capabilities; they all have large IT teams."* A fellow fintech CEO agreed, stating, *"It is ultimately on us to ensure our clients have success in relationships with us."*

- **Fintechs must remain nimble and adapt with the bank.** Successful partnerships involve a trusted relationship where a bank or financial institution sees the fintech as a partner who can accelerate their digital transformation. To do so, a fintech executive explained, *"You need to be flexible once you're involved with a bank in a partnership and evolve to other areas of opportunity for that bank… Banks are seeing a lot of pressure from consumers to enhance digital services. You need to think beyond the initial solutions that you offered and that's how it becomes a true partnership."*

- **Vendor models present an alternative to partnering.** For some fintechs, becoming a "partner" may only complicate a more traditional vendor relationship. A fintech CEO explained, *"I'll say there's nothing wrong with being a vendor. Being a strategic partner can mean all sorts of things, but if you want to build a product for tens or even hundreds of banks, that's not a partnership, and that can be the better business."* A fellow fintech CEO also observed the merits of a vendor relationship model stating, *"When we started it was very much a partnership model and it really didn't succeed. Since then, it's become much* *more of a platform and it's been a lot better selling that way. We talk about the banks we work with as our clients, not our partners, because I think it's important to think that way. You can be a vendor and act like a partner."* For banks, the distinction may not really matter. One senior bank leader advised, *"I wouldn't get caught up in vendor vs. partner. Anything that helps us serve our customers better, that would broadly be considered a partnership."*

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The discussion on August 26th provided a unique opportunity for a candid exchange of views among senior leaders from banks and fintechs. It highlighted the changes taking place across the ecosystem and how those changes influence the appetite and models for banks and fintechs to engage in mutually beneficial partnerships and client relationships.

Appendix: participants

On August 26, 2020, Tapestry Networks and LendIt Fintech hosted the Banking and Fintech Leadership Forum. Discussion focused on the continuing evolution of the financial services ecosystem and bank and fintech partnerships during a time of profound transformation and uncertainty. This Summary of Themes draws primarily on insights from this discussion which took place under a modified version of the Chatham House Rule, whereby the names and affiliations are a matter of public record, but nothing is attributed to any individual or institution. Unattributed quotes from these discussions appear throughout.

The following individuals participated in these discussions:

- EJ Achtner, Head of Digital Banking & Strategic Change, US Commercial Bank, HSBC
- Jeremy Anderson, Vice Chairman and Senior Independent Director, Audit Committee Chair, UBS Group AG
- Dennis Andrade, Partner, Tapestry Networks
- Bo Brustkern, Co-Founder and CEO, LendIt Fintech
- Mark Cuthbert, VP General Manager of Strategy, Planning, and Innovation, Transformation, USAA
- Jason Gardner, CEO, Marqeta
- Dave Girouard, CEO, Upstart
- Sam Graziano, CEO, Fundation
- Abhishek Gupta, Head, Open Platform, BBVA
- Adam Hughes, CEO, Amount
- Brennan Kerrigan, Senior Associate, Tapestry Networks
- Bernadette Knight, Managing Director, Cash Management and Trade Business Head, Commercial Bank, Citi
- Steve McLaughlin, CEO, FT Partners
- Tom Mildenhall, Managing Director, Global Head of Technology Business Development, Bank of America
- Tucker Nielsen, Principal, Tapestry Networks
- Nathalie Oestmann, COO, Curve
- Andy Ozment, announced as upcoming Chief Technology Risk Officer, Capital One
- Sankaet Pathak, CEO, Synapse
- Henry Pinnell, Managing Director, Financial Institutions Group, Barclays
- Peter Renton, Co-Founder and Chairman, LendIt Fintech
- Manolo Sanchez, Non-Executive Director, Fannie Mae, OnDeck Capital
- Nikolai Varma, CCO, OakNorth
- Clay Wilkes, CEO, Galileo

About LendIt Fintech

LendIt Fintech is the largest media and events company dedicated to innovation in lending and digital banking. Today we operate three major conferences annually for the USA, Europe and Latin America markets, along with our digital community and our daily news organization.

Like much of the economy today, financial services is experiencing a rapid upheaval. We are seeing a multi-decade transformation where fintech will take center stage as everything becomes digital. LendIt Fintech is there for you, reporting the news on a daily basis, enabling real time discussion and insights with LendIt Fintech Digital and empowering our community with connections and in-depth learning at our physical events.

The LendIt Fintech team believes that there has never been a more exciting time to be in financial services. We immerse ourselves in all things fintech so we can be your guide on this journey.

About Tapestry Networks

Tapestry Networks is a privately-held professional services firm which operates networks, working groups, and research workstreams for senior leaders from many of the largest corporations and institutions in the world. Tapestry events create an environment where leaders—directors, senior executives, regulators, and policymakers—learn from one another, explore new ideas, and collaborate to solve complex problems.