Opportunity or threat?

Daniel Martyniuk, Director
CEE FinTech market
Opportunity or threat?
What is FinTech anyway?

**DEFINITION: FINTECH**
nounˈfinˈtek\`

Financial technology, also known as FinTech, is a **software-based business** that provides **financial services**.

FinTech companies are **generally startups** founded with the purpose of **disrupting incumbent** financial systems and corporations that rely less on software.
Retail banking is undergoing a rapid transformation that forces us to rethink existing business models

FORCES OF CHANGE

ACCELERATING TECHNOLOGICAL ADVANCEMENT
- Broader accessibility of products and services
- Automation of once highly manual activities
- Increased market transparency and efficiency
- Leveled playing field for small and mid-sized firms to compete
- Emergence of non-traditional competitors (e.g., Apple, Google)

TRANSFORMING CUSTOMER EXPECTATIONS
- Empowerment through digital connectivity
- Increased information access and products options
- Ability to obtain / share financial advice without intermediaries
- Ability to generate funding without intermediaries

CHANGING REGULATORY ENVIRONMENT
- Need for greater capital levels
- Increased oversight on data security
- Fee caps leading to impact on traditional revenue models
- Uncertain response to cryptocurrencies and non-traditional competitors
Future will be governed by exponential tech and social trends

**NEXT GENERATION OF BIOMETRICS**
- Fingerprint identification and verification are providing customer service enhancements and improving security. However, the spectrum of solutions has broadened, including voice recognition or heartbeat-based authentication

**FINANCIAL SERVICES AND SOCIAL MEDIA CONVERGENCE**
- Cash-rich social media companies could facilitate charitable giving, crowd funding, cash management, and potentially even build up a comprehensive profile of creditworthiness

**WEARABLE BANKING TECHNOLOGY BECOMING MAINSTREAM**
- NFC payments as well as more complex banking services and money transfers, geo-locational alerts and even video conferencing with a bank advisor are becoming a reality

**DEMOCRATIZING TRUST THROUGH BLOCKCHAIN**
- Blockchain is a distributed ledger that provides a way for information to be recorded and shared by a community providing e.g. settlement of stock trading records in real-time, authentication of cryptocurrencies, digitization of assets

**USING DIGITAL TECHNOLOGY TO DRIVE FINANCIAL INCLUSION**
- Expanding financial inclusion has direct bottom-line benefits for mainstream banks. Innovative ways to reach out to customers help reintegrate banking into mainstream public debate and improve the relationship

**REIMAGINING CORE SYSTEMS**
- Organizations are now developing strategies for reimagining their core systems. Targeted investments in core modernization can transform legacy solutions into intuitive and responsive systems that can support business in the digital age
Millennials are mobile, rarely visit their bank and don’t see banking as a ‘first need’

**MILLENIAL DISRUPTION**

- **53%** don’t think their bank offers anything different than other banks
- **70%** think in 5 years, the way we pay for things will be totally different
- **73%** would be more excited about a new offering in financial services from Google, Amazon, Apple, Paypal or Square than from their bank
- **71%** would rather go to the dentist than listen what banks are saying
- **50%** are counting on tech startups to overhaul the way banks work
- **33%** believe they won’t need a bank at all

*Source: The Millennial Disruption Index*
Successful innovators innovate beyond products and integrate multiple types of innovation.

**TYPES OF INNOVATION**

- **Configuration**
  - Profit model
  - Network
  - Structure
  - Process
- **Offering**
  - Product performance
  - Product system
- **Experience**
  - Service
  - Channel
  - Brand
  - Customer engagement

- **Profit Model**
  - The way in which you make money
- **Structure**
  - Alignment of your talent and assets
- **Process**
  - Unique or superior methods for doing your work
- **Product System**
  - Complementary products and services
- **Channel**
  - How your offerings are delivered to customers and users
- **Customer Engagement**
  - Distinctive interactions you foster
FinTech companies are gaining momentum, showing the need for new technologies in finance.

- EUR 413 bn was spent on IT by global banking and securities institutions.
- EUR 26 bn of revenues was generated by UK FinTech companies.
- EUR 10 bn was invested in the FinTech ventures globally.
- EUR 55 bn was spent on IT in European banks.
- 11 companies were listed in 2014 by Finovate as FinTech unicorns (financial technology companies founded no earlier than 2000 and valued at a minimum of USD 900 million).
- 46 companies were listed a year later, with 37 aspiring to the unicorn status (their valuation between USD 500 million and 800 million).
FinTech start-ups pop-up in all areas of finance, reimagining the ecosystem

Mobile Payments
Integrated Billing
Cryptographic Protocols
P2P Transfers
Mobile Money

Artificial Intelligence / Machine Learning
Big Data
Private Equity / Venture Capital
Share

Social Trading
Automated Advice & Wealth Management
Advanced Analytics

Disaggregated Distribution
Self-Driving Cars
Wearables
Internet-of-Things

P2P
Lean, Automated Processes
Banking as Platform (API)
Evolution of Mobile Banking

Empowered Angel Investors
Alternative Adjudication

Emerging Payment Rails
Cashless World
Value Chain Disaggregation
Internet of Things

Smarter and Faster Machines
New Market Platforms
Shifting Customer Preferences
Alternative Lending

Process Externalisation
Empowered Investors
Business financing - crowdfunding
Capital Rising

Market Provisioning
Investment management
Deposits and Lending
Financial sectors in CEE will need to get ready for the competition with global tycoons ....
… who grow at a tremendous pace and show amazing operational agility

Time needed to reach USD 1 bn company valuation (months)

- Alibaba (1999): 72
- Uber (2009): 54
- SoFi (2011): 47
- Airbnb (2008): 36
- Facebook (2004): 31
- Square (2009): 24
- Zenefits (2013): 23

The difference between old and new paradigm of business model

- Lending Club [2000-2016]
  - 4m* users
  - 1,400 employees
  - $4.1bn valuation
  - $2.91m Value per employee

- Reiffeisen Bank [1927-2016]
  - 15m clients
  - 51,000 employees
  - $4.3bn valuation
  - $0.08m Value per employee

*Assumption that number of users is equal to the number of loans granted
CEE as a whole is an attractive and receptive market for foreign investors and local business activity

<table>
<thead>
<tr>
<th>Country</th>
<th>Population (15-44) [m]</th>
<th>GDP per capita [EUR]</th>
<th>Net FDI inflow as a % of GDP</th>
<th>Smartphone penetration</th>
<th>Internet access</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>4.6</td>
<td>38,500</td>
<td>1.9%</td>
<td>66%</td>
<td>82%</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>2.3</td>
<td>5,900</td>
<td>3.5%</td>
<td>48%</td>
<td>59%</td>
</tr>
<tr>
<td>Croatia</td>
<td>1.7</td>
<td>10,200</td>
<td>6.9%</td>
<td>61%</td>
<td>77%</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>4.3</td>
<td>14,700</td>
<td>2.4%</td>
<td>55%</td>
<td>79%</td>
</tr>
<tr>
<td>Hungary</td>
<td>4.0</td>
<td>10,600</td>
<td>9.0%</td>
<td>50%</td>
<td>76%</td>
</tr>
<tr>
<td>Slovakia</td>
<td>2.4</td>
<td>13,900</td>
<td>0.1%</td>
<td>65%</td>
<td>79%</td>
</tr>
<tr>
<td>Slovenia</td>
<td>0.8</td>
<td>18,100</td>
<td>2.1%</td>
<td>56%</td>
<td>78%</td>
</tr>
<tr>
<td>Poland</td>
<td>14.6</td>
<td>10,700</td>
<td>3.2%</td>
<td>59%</td>
<td>76%</td>
</tr>
<tr>
<td>Romania</td>
<td>8.6</td>
<td>7,500</td>
<td>1.9%</td>
<td>46%</td>
<td>68%</td>
</tr>
</tbody>
</table>
It is therefore hard to tell who will show up in a few months’ time.
Some success stories from CEE give food for thought regarding future development of FinTech ecosystem

<table>
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<tr>
<th>Product</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>PayU</td>
<td>One account to shop everywhere online. 100% certainty that the money will get where it should and of getting money back from an unsuccessful transaction. It operates in X countries.</td>
</tr>
<tr>
<td>SDK.finance</td>
<td>The back-end software for the quick start of any FinTech product. Prefabricated modules can be interfaced with other systems to develop solutions such as e-wallets, lending platforms or loyalty programmes.</td>
</tr>
<tr>
<td>ŽLTÝ MELÓN</td>
<td>Portal connecting people who need to borrow with those who want to invest. By the second half of 2015, it had already provided Slovaks with EUR 2.5 million in loans. It offers both standard, low-value loans and one-to-two year loans of between EUR 20,000 and 30,000.</td>
</tr>
<tr>
<td>oradian°</td>
<td>SaaS-based IT systems that enable the running of a microfinance institution in a few days. Company is helping undeveloped countries in their fight for global financial inclusion.</td>
</tr>
<tr>
<td>Velmoco</td>
<td>Motor vehicle insurance coupled with a mobile device that tracks driving habits. Solution allows to decrease the fuel and servicing costs and gain insurance discount.</td>
</tr>
</tbody>
</table>
Established players will have to co-operate with FinTech companies …

How banks co-operate with FinTechs

- **43%** STARTUP PROGRAMS TO INCUBATE FINTECH COMPANIES
- **20%** SET UP VENTURE FUNDS TO FUND FINTECH COMPANIES
- **20%** PARTNERING WITH FINTECH COMPANIES
- **10%** ACQUIRED FINTECH COMPANIES
- **7%** LAUNCHED OWN FINTECH SUBSIDIARIES

Source: Deloitte analysis
... especially since the boundary between the bank and FinTech entity will become blurred

1 Client opens an application to settle the bill.

2 Application identifies transaction as an unusual – with high volume that can makes a dent in the budget – and sends query about loan offers by API.

3 Client gets a suggestion to take credit and offers that can accept by one click.

Application aggregating finances and PFM
Aggregates all functions of everyday retail banking, from transfers and transaction history to credit cards and cash loans.

Key accelerators – PSD 2 and regulators (Open Banking Working Group – UK)

Potential pretenders

CE Banks
Lending Companies
P2P Platform
FinTech
Global Banks
Trends to watch in the nearest future in CEE go hand in glove with global developments

**BANKING SECTOR**
- Internet banking
- Mobile banking
- Contactless cards

The greatest share of FinTech solutions in all CEE countries is provided by innovations for banking system.

**INSURANCE AND ASSET MANAGEMENT**
- Smartphone apps
- Services based on telematics

Both insurance and asset management sectors gives specific opportunities to break dominance of established vendors.

**PAYMENTS**
- Contactless payments
- Host Card Emulation
- Cryptocurrency

The upcoming implementation of the Directive on Payment Services II may change the payments market in all countries.

**EMERGING TECHNOLOGIES**
- Personal Finance Management tools
- P2P lending
- Automated and cloud-based financial management solutions for SMEs

FinTechs based on Capital rising and financial management are gaining momentum. Data analytics and cyber security are still dominated by global players.

**BARRIERS**
- Legal restrictions (e.g. use of clouds, the legal status of the financial entity)
- Limited domestic demand

Key barriers to market entry are related to demand, regulation and competition.

**ENABLERS**
- Financial forums
- Incubators
- Industry fairs

A vibrant start-up community accelerates the progress of FinTech development and brings it on to the industry agenda.
Key questions that will need to be answered by Retail banks to stay in the game

• How will **empowered, digitally connected consumers** choose you over a myriad of other providers?

• How will **automation** and **commoditization** of high-value activities and **broader accessibility** of financial products change the role of traditional financial institutions?

• What **relevant partnerships** will need to be established to compete effectively?

• How will **regulatory oversight** affect the launch and growth of new business models?

• What **role** will **human capital** play in the transformed future?

• What strategies need to be developed in order to **future-proof** business models?