The Rise of LASIC Finance

Innovation for Financial Services Conference, 15-16 Oct 2015, Singapore Management University

Streaming from Silicon Valley, 14 Oct 2015

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Introduction

• The Financial system is being disrupted:
  • Innovative competitors operating on sleek business models and offering **new alternative services are entering at the bottom of the market**, where gross margins are low and latent demand is high
  • Financial services and **banking still enjoy robust margins**, but this is more a function of regulatory protection than the actual value they create
  • Tightening regulation has encumbered large complex financial institutions, **this silo mentality and burdensome physical infrastructure** make it ripe for digital disruption
Acceleration of Disruption: Growth in FinTech Investment

Massive investment in FinTech innovation is signalling the end of traditional banking.

By David Lee

Investment in FinTech (USD)

2003: $34 mil
2008: $930 mil
2014: $4-13 bil
Changes in the Business Model: From High to Low Margin

- In the past, companies with high margins were attractive destinations for capital
  - High margin and barrier of entry
  - No disruption from technology
- Now, companies that attract capital are
  - Innovative
  - Have low margins and low barrier of entry
  - Have potential for high scalability
  - Focus on customer stickiness instead of cash flow
Mobile Banking Led by Non-Banks

• Low penetration of High-speed mobile broadband in Developing Countries

• Worldwide Adults with Financial Deposits: 51% in 2010 -> 62% in 2014*

• Telecom, internet and e-commerce companies leading this change

• Unbanked and under-banked in low-income countries considered too risky and too poor

• Mobile communications technology allowed massive networks with extraordinary scale making servicing these markets with low margin models possible

*World Bank’s 2014 Global Findex Report
M-Pesa: Started as a SMS Payments CSR Project

- Mobile phone platform facilitates payments, money transfers, deposits and withdrawals communicated via text message
- Cash withdrawals and deposits can simply be made through point-of-sale locations at vendors and kiosks
- Kenya: 46 million people – 5 million have bank account and 19 million have M-Pesa accounts
Bank Culture Needs to Change

• FinTech firms innovate, explore, and recalibrate their offerings rapidly

• Banking sector is plagued by a risk adverse culture, dominated by amply staffed regulatory departments and a financial control ethos. None of these characteristics scream innovation or disruption
User Data is New Money

- **Data** is extremely valuable
- Apps that have high user commitment or access to a part of a community have high switching costs, are more customer sticky and collect richer data
- Digital services or apps that have huge captive user bases can generate enormous amounts of valuable data
New Investment Paradigm Based on Stickiness

• In 2013, Facebook bought WhatsApp for US$22b despite WhatsApp’s net loss of US$138.1m. The 400 mil active WhatsApp users can be potentially integrated into a FinTech platform

• Logistic companies that manage valuable customer data are being “acquired” too, e.g. Alipay has invested and increased its stakes in Singpost
FinTech, Beyond Payments

• E-commerce companies are expanding their business beyond simple payment, delivery and settlement services

• These companies are partnering with social media companies to provide the following services
  
  • Lending
  • Microcredit
  • Investment Products
  • Insurance
  • Crowdfunding and many more
FinTech, Beyond Payments: Insurance

• **Online-only insurance company**, ZhongAn was launched in February 2013
  • JV between Alibaba and Tencent partnering PingAn, China’s largest insurer

• **Lucrative insurance premiums** were generated on small margins
  • 11 November 2014, Alibaba had sales of more than US$9 billion of which **RMB$100 million** was generated through online insurance premiums like ZhongAn which sold **50-cent insurance policies** covering package delivery
FinTech, Beyond Payments: Converting Bit and Byte to Profits

• Information Advantage provides internet companies with intimate information of the consumer

• FinTech companies with this information can better forecast customers’ potential financial risk than traditional banks so as to lend and insure at a lower cost

• Cost is further reduced and passed on to more customers on a low margin but fast-moving model due to the scalability of the technology and no need for brick and mortar branches
FinTech, Beyond Payments: Serve the Masses in Many Different Ways

• Profit is secondary, FinTech companies grow by reaching out to the masses, diversifying service offerings and disrupting further up the value chain, attracting more capital in the process.

• For example, Alibaba has been offering low-cost loans to merchants and have branched out to micro-loans to consumers.

• Using an e-wallet like Alipay as the mode for transactions, Alibaba can quickly assess an individual’s cash flow in real time and approve low interest rate short term loans in 24 hours.
New Banking Services: Focus on Customers’ Needs and Ability to Raise Funds

• **Compliance costs are low** when fractional reserve banking is not involved

• **P2P lending** democratizes the lending process and allows borrowers to get access to credit within hours while lenders can earn returns in excess of most coupon rates

• For example: Lending Club, an online P2P lending service facilitates unsecured personal loans of up to $35,000 and delivers solid return to lenders while spreading the risk across multiple borrowers

• This model allowed **Lending Club** to raise US$900 m in 2014

• Similar services are also provided by **Singapore based Capital Match** which matches individual lenders to small and medium-sized enterprises
New Banking Services: Democratization and Opportunity From the Masses

• Cross border remittances that charge for less than the traditional fees have been gaining popular usage

• Transferwise provide remittance facilities at 0.5% which is much lower than the typical money transfer services charge of 5%

• This is achieved through crowdsourcing the fund flow, allowing it to bypass traditional banking and payment networks and allows it to avoid currency conversion

• Instead of facilitating a direct transfer from a sender to a recipient, Transferwise reroutes payments from a sender to a recipient of another transfer, which is simultaneously taking place but going in the opposite direction. The disruption is happening from the bottom up
Decentralizing Control and Programmable Sharing Economy

- Powerful trend towards financial disintegration and eventually, towards a completely distributed financial system

- **Blockchain** – distributed database technology that makes public ledger of transactions for cryptocurrencies and beyond possible

- More secure than traditional banking system as hacking would need to overcome security protocol at each node which is extremely costly to have slight success

- While not all will agree, Cryptocurrencies can be self-regulating, democratizing the function of the central bank and Blockchain can remove the need for clearing houses or a custodial bank
Disruption From the Bottom Up: From a Service Sharing to an Asset Sharing Economy

- Thomas Piketty’s “Capital in the Twenty-First Century” demonstrates that the rate of return on capital is greater than economic growth and people without assets are left behind.

- Asset inflation driven by quantitative easing worsens the gap between rich and poor and reduces social mobility.

- However, one type ofasset inherent to all human being exist, apart from their labour; data generated everyday.

- Although internet companies get to profit off this data, users can also take ownership and gain monetary benefit by contributing this data, for example through the app Gems.
P2P + CryptoEquity = Asset Sharing Economy

• A complete disruption of the financial system is not far from happening.

• The continual growth of the sharing economy and the rise of P2P platforms and cryptocurrency are facilitating this disruption.

• The end result: decoupling of the sharing economy from the current economic system, where the asset rather than service sharing economy becomes the dominant system in which control and ownership of the economy is democratized.
Disruption From Bottom Up: LASIC

Disruptors would come from companies that embody the following characteristics: LASIC

- Low margin
- Asset light
- Scalable
- Innovative
- Compliance easy
Concluding Remarks

• China, with over 90% mobile phone penetration, over 60% mobile banking penetration, and a P2P market more than 5x the size of the US, is leading the financial innovation space with banks transforming rapidly with O2O e-commerce and supply chain financing.

• Education, government, supply chain, real estate, medicine and law are beginning to be disrupted as seen in China.

• It is clear: the current service sharing economy world is on the verge of the next disruptive wave of programmable asset sharing economy.

• Adopting LASIC with connectivity inclusion for those excluded will be the main feature of sustainable FinTech business, just like Alipay and M-Pesa.
References and Acknowledgements


http://www.smu.edu.sg/sites/default/files/skbife/pdf/The%20Rise%20of%20Chinese%20Finance%20E9%A2%A0%E8%A6%86.pdf

Special thanks to Editor Christopher Williams Dula, Research Assistants Natasha Singhal and Guo Zongren for their editorial contribution and preparation of these slides.

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