

Armapartners

Google and Amazon go after Banking

By Mark Rodrigues



It's a popular topic in FinTech

What will Google or Amazon do in Financial Services? They have the capital. They have trusted platforms with reach. They have formidable access to data on customers, channels, and transactions. They are active investors in FinTech and frequent collaborators and cloud services suppliers with innovative firms such as Goldman Sachs and Fidelity. Where, then, is the change likely to be and how?

Let's start by being clear about what we mean by Financial Services Institutions (FS). Here we mean FS as consumer banks, wholesale banks, asset managers, alternatives such as hedge funds and PE as well as insurance companies. It's a big industry with consumer and wholesale dimensions as well as functional sectors such as payments, risk, markets, and transactions.

As we are speculating on digital transformation let's hold to this wide definition of FS. In the digital world the micro and the macro are more common companions. One can look at a central bank rate hike and have detailed input on how many people are shopping online or in shopping centres. Structured data is linked to unstructured. We can be more expansive on workflow and the value chain. Uber doesn't own cars and AirBNB doesn't own rooms so maybe in our exploration of FinTech we can imagine curators, orchestrators, and brokering without always needing to own the parts or be subject to heavy regulation.

We can also assume that any strategy into FS will do no harm to the existing core. Google and Facebook make their money today from digital advertising and together command 77% of that market. Thus they will not do anything that harms today's source of cash and growth. Amazon's core is from product and service sales so we can be sure that will influence their choices in FS. Further whatever any large cap tech does it will need to contribute to their goals of a Trillion dollar



valuation and beyond. In the world of Google for example, financial services will compete with other big impact ideas such as drones, maps, cyber security, suite of office tools etc.

Google and Amazon have been more measured in FS than their Asian counterparts. Google Wallet is clearly just the start and we can imagine payments going through further upheaval with the implementation of PSD2 and the changing power dynamic between the bank, the merchant and the customer.

Others Techs in Asia are moving even faster. Alibaba got into the Asset management business and raised \$81B in 9 months partnering with Tianhong. We should pay close attentions to TenCent and Ant Financial especially with their newly launched financial market places (Licitong and Caifu Hao respectively). These are among the more innovative digital platforms targeted to mobile millennials.

In M&A there are an estimated 30-40 FinTech Unicorns that might meet the scale objectives of Amazon or Google. The valuations are indeed high. They also have the cash to buy most banks given current valuations. Unclear why they would want the legacy infrastructure – why not let the FS own 'manufacturing' while others go after higher margin distribution and servicing? Thus we expect Google and Amazon to continue to wear the hat of orchestrator, investor and partner looking more for incremental growth.

Target themes for expansion and acquisition

Payments have been the area of early investment and progress.

- How long before Amazon, Google, Apple start to leverage the analytics that come with payments flow and progress predictive modelling, customer credit, and credit monitoring? The capabilities are underway as Amazon Pay Wallet looks to clone eBay and Alipay as alternative non-bank payment portals.
- PSD2 – will the Internet giants use this as a means to be the customer interface to banking with the banks becoming the plumbing – similar to what happened in telecoms. Would one of the large Caps once again go after Square or Stripe?

- Speculation: If Google or Apple gathers European users banking info via API, why would one ever login to their banks' apps? It would be so much easier to speak into Siri, "What is my balance?, transfer \$X from checking to savings, etc."

- Remittance: Similar to what Alibaba has done with MoneyGram. A lucrative sub sector among the huge FS. There are many approaches to pick pieces of the payments space.

Wealth management/asset management, particularly in a world where AI becomes more prevalent in asset management. There are many scenarios including Google as a financial search engine used to channel Asset Managers. They could sell data to financial services firms as well but again this could harm the core business if not done properly. Large Cap Techs have an implicit and explicitly trust with user data. While they can get permissioned by users they have an accountability and trust that influences all strategic decisions.

- We think this marketplace/distribution channel angle could go further than just wealth/asset management. Similar to what Ant Financial and Tencent did in Asia, this can be a financial product marketplace. In addition to ETFs/mutual funds, Google or Amazon can be a search or recommendation engine for credit cards, personal loans, mortgages, etc. Again this approach is working rapidly with millennial who are open to non-traditional financial platforms



- We do not see tech companies using balance sheet to issue loans/cards. It is more likely that they play role of broker and leverage client data to curate products that meet one's financial needs. Note: To pull this off, clients will likely have to opt-in and provide more data on finances, objectives, and risk tolerances. We do not think it can be done effectively just using the data Google and Amazon capture today.

Business lending – using the analytics to provide more competitive and intelligent financing solutions, particularly to the online merchants. Google could bring a new dimension of analytics to the table using partners such as CargoMetrics or Credit Karma. These types of digital platforms can address two issues that have plagued the legacy credit sector credit. Credit risk background and monitoring. On the former, Credit Scoring is a sub industry with room for improvement. New sources of information from social media, correlation of educational background, collateral and other even crowd sourcing can lead to faster, more dynamic and more accurate credit profiles. Eventually creating crowd sourcing but also a secondary market for syndications and securitization.

- Similar to the consumer financial product marketplace mentioned above, couldn't they do something similar with small to mid-sized businesses? If they capture information on SME businesses' financial condition, accounts payables/receivables relative to credit terms, inventory aging, etc., Google or Amazon can then orchestrate potential business loans that are favourable to the business. We think this could be relatively easier for Amazon since they act as re-seller and fulfilment provider for many SME businesses today through its retail marketplace. They already have the community/network; this would just be an extension of services provided to those SMEs.

Beyond these target themes for acquisition

is the underlying growth strategy for the large Cap Tech firms. We see determined efforts to reach out and engage smaller early stage firms through investment as well as collaboration. We also see several strategic questions now and going forward. These questions include:

- How well will these firms manage B2B opportunities?
Comments: one of the key differences in B2B is the service and support requirements that are more difficult to scale than B2C. In other words one cannot simply download an app to a bank operator instead you will likely need boots on the ground which is hard (but not impossible) to scale.
- Will they combine balance sheet risk with operation cloud based services?
- Will they invest in content and own it or play the role of network orchestrator with a series of alliances and APIs?
Can they broker or orchestrate resources without owning it?

A final thought ...

Decades ago Walter Wriston, CEO of Citibank said

“ information about money is more valuable than money ”

Consider the huge industries already built around this premise. There are more index funds than there are stocks. There is more money speculating on goods and services than there are actual goods and services. In other words the notional global derivatives market (a series of bets) is 10-20 times larger than the combined Global GDP of actual value creation. Information about money is indeed more valuable or as valuable as money. Information empires need to be both offensive and defensive in their provision of financial information and services. Welcome to Banking!

What do you think?

Please share your thoughts to mrodrigues@armapartners.com.



Mark Rodrigues

Senior Advisor – New York

Joined Arma Partners in 2017. Mark has over 30 years' experience in the global technology and financial services industries as an executive, investor and consultant. Previously he was a Global Managing Director and Leader of Strategic Customers and Solutions at Thomson Reuters, where he was responsible for managing the \$2.9bn global revenue and commercial relationships of Thomson Reuters's largest buy-side and sell-side client accounts. Prior to this, Mark held senior positions at New York-based private equity investor Aquiline Capital Partners; Oliver Wyman, the global management consulting firm; and American Management Systems (now CGI Group), one of the largest independent IT and business process services firms in North America, where he was the Head of Global Financial Services.

Mark holds an MBA from Harvard Business School and a BA in European History from Yale University.

Disclaimer

This presentation is issued by Arma Partners LLP (“Arma Partners”). Arma Partners is authorised and regulated by the Financial Conduct Authority (the “FCA”).

This presentation has been prepared by Arma Partners and is furnished to you solely for your information and for your exclusive use in determining whether to enter into a business relationship with Arma Partners (the “Purpose”). It is not intended to constitute, and should not be construed as constituting, investment advice or a personal recommendation as defined under the FCA rules. This presentation may not be used for any purpose other than the Purpose. In addition, this presentation is strictly confidential and may not be disclosed, revealed, reproduced or redistributed, in whole or in part, to any other person.

The information in this presentation does not purport to be comprehensive. While the information in this presentation has been prepared in good faith, no representation or warranty, express or implied, is or will be made, and no reliance should be placed on, the accuracy, fairness or completeness of the information contained herein and accordingly no responsibility or liability is or will be accepted by Arma Partners or its affiliates or by any of their respective partners, members, officers, directors, employees, consultants or agents in relation to or arising out of, directly or indirectly, the accuracy, fairness or completeness of the information in this presentation, the use of this presentation or any other written or oral information made available to any recipient, and any such liability is expressly disclaimed. The recipient acknowledges and agrees that no person has, nor is held out as having, any authority to give any statement, warranty, representation, or undertaking on behalf of Arma Partners or any of its affiliates in connection with this presentation and the Purpose.

Neither Arma Partners nor any of its affiliates gives an undertaking, and shall not have any responsibility, to provide the recipient with access to any additional information or to update this presentation or any additional information, or to correct and communicate any inaccuracies in it which may become apparent. Recipients therefore shall not be entitled to assume that any or all information in this

presentation are unchanged or that the recipient will be informed of any or all changes. This presentation may not reflect information known to other professionals in other business areas of Arma Partners and its affiliates.

This presentation is not intended to form the basis of any investment activity or decision and no legal relations shall be created by this presentation or by its issue. Neither the information set out in this presentation or referred to in other written or oral information in connection with this presentation or the Purpose nor the fact of its distribution shall form the basis of any contract and should not be relied upon in relation to any contract or commitment.

This presentation does not constitute or form part of an inducement or offer to issue or sell, or a solicitation of any offer to purchase or subscribe for, any securities in any jurisdiction and is not a commitment by Arma Partners or any of its affiliates to provide or arrange any financing for any transaction or to purchase any securities in connection therewith. The information or services described in this presentation are not provided to and may not be used by any person or entity in any jurisdiction where the provision or use thereof would be contrary to applicable laws, rules or regulations of any governmental authority or regulatory or self-regulatory organisation or where Arma Partners or its affiliates are not authorised to provide such information or services.

Recipients are not to construe the contents of this presentation as constituting the provision of legal, commercial or tax advice, nor as a recommendation of any kind.

This presentation shall not exclude or limit any liability for, or remedy in respect of, fraudulent misrepresentation or insofar as such exclusion or limitation is prohibited by the Financial Services and Markets Act 2000, any regulations made under it, the FCA rules or otherwise prohibited by law.

This presentation has been delivered to recipients on the express understanding that they will use it only for the Purpose set out above and by accepting this presentation, the recipient agrees to be bound by the foregoing limitations.