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Beyond Fintech

Disruptive innovation in lending

Background

A 2017 report from Deloitte and the World Economic Forum, *"Beyond Fintech: A pragmatic assessment of disruptive potential in financial services,"* examines disruptive innovation in financial services.

The report identifies **8** key forces impacting all aspects of financial services:

Cost Commoditization: Financial institutions will accelerate the commoditization of their cost bases, removing them as points of competition and creating new grounds for differentiation

Experience Ownership: Power will transfer to the owner of the customer interface; pure manufacturers must therefore become hyper-scaled or hyper-focused

Data Monetization: Data will become increasingly important for differentiation, but static data sets will be enriched by flows of data from multiple sources combined and used in real time

Systemically Important Techs: Financial institutions increasingly resemble, and are dependent on, large tech firms to acquire critical infrastructure and differentiating technologies

Profit Redistribution: Technology and new partnerships will enable organizations to bypass traditional value chains, thereby redistributing profit pools

Platforms Rising: Platforms that offer the ability to engage with different financial institutions from a single channel will become the dominant model for the delivery of financial services

Bionic Workforce: As the ability of machines to replicate the behaviors of humans continues to evolve, financial institutions will need to manage labor and capital as a single set of capabilities

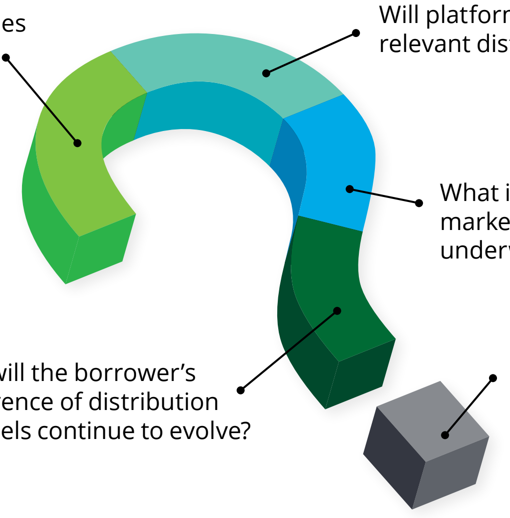
Financial Regionalization: Diverging regulatory priorities and customer needs will lead financial services in different regions of the world down distinct paths

To learn more, visit www.deloitte.com/beyondfintech. Here are some of the key findings for the lending segment.

Trends

Where disruption has occurred	New adjudication techniques have significantly expanded access to credit among underbanked, "thin-file," and subprime customers.
	Individual and small-business borrowers expect their lenders to deliver the seamless digital origination and rapid adjudication that financial technology (fintech) companies pioneered.
	Non-financial platforms are emerging as an important source of underwriting data and a point of distribution for credit.
Where it hasn't	Funding economics put marketplace lenders at a cost disadvantage compared to traditional banks, raising questions about the model's sustainability.

Open questions



Possible futures

Different evolutionary paths	Marketplace lenders must develop more sophisticated capabilities or compete on price with established banks.	Clients will benefit from a fragmenting lending environment thanks to greater competition and sophisticated niche lending.
Shared service providers	The desire for cost-commoditization drives growth in B2B service providers, as two needs come together in one solution.	Outsourcing will improve industry cost structures, but also create new sources of risk.
Distribution 2.0	Non-financial firms move into financial services and disintermediate the traditional broker channel.	As partnerships between banks and non-financial firms proliferate, customers will enjoy more choices and a better experience.

Key takeaways

The lowest funding costs win: Despite their innovations in origination and adjudication, online lenders have limited ability to compete with banks due to high and unstable funding costs. This will drive online lenders to acquire banking licenses – unless alternative funding becomes available.

Lending goes digital: Marketplace lenders and technology firms have reoriented customers. In the future, customers will expect a frictionless application experience and a swift response.

Lenders use data effectively: Leading lenders use new data sources to underwrite applications whose risks they couldn't assess before (e.g. thin-file customers). They also reduce underwriting costs by automating the collection and analysis of key data (e.g. using data gathered directly from a small business accounting platform). Moving forward, lenders will look for more ways that data can inform lending decisions.