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CATCHING THE FINTECH WAVE

By Anthony Ferguson and Alice Xu

THE RISE OF FINTECH

Fintech is no longer a passing wave but a tsunami taking the financial services industry by storm. While many traditional financial institutions initially raised their eyebrows at early fintech innovators—and perhaps resisted the change—most today would agree that fintech is no longer a trend but a movement bound to leave an indelible mark.

In fact, the top 10 U.S. banks by assets under management have **invested** heavily in the fintech space over the years, participating in 72 rounds totaling $3.6 billion to 56 fintech companies since 2012, according to CB Insights. And while investment activity may have dipped in the first quarter of 2017, the report noted that four of the last five quarters have seen over $1 billion invested into VC-backed U.S. fintech startups.

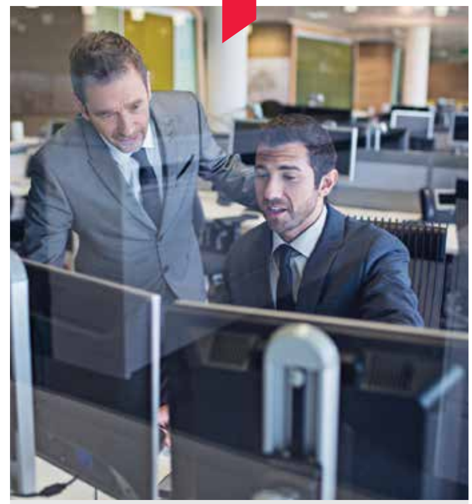
So, what exactly is a fintech company? There are several definitions in the marketplace, but there seems to be a consensus that fintech companies are those that use technology—often in the form of online platforms or mobile applications—to enable alternative delivery of financial products or services. While many different types of fintech companies exist, the most common categories include alternative lending, digital payments and financial management services.

ALTERNATIVE LENDERS

One of the strongest growth areas in fintech has been in the alternative lending space. Companies have come to market with various lending products designed to meet the needs of underserved borrowers who are either unable to access credit from traditional lenders, like banks and credit unions, or struggle to get access to credit at favorable rates.

The typical alternative lending business model involves partnering with traditional banks to originate and fund loans. Other alternative lending business models may also include partnering with individual state banking charters or facilitating direct peer-to-peer funding through a process of matching lenders and borrowers in an online marketplace. Depending on the business model, a loan, once made, can be sold to an investor with servicing rights, retained or kept for investment.

The proposed advantage of the products from alternative lenders over competing products offered by traditional lenders often lies in the former's speed-to-execution rate and the clarity and convenience of their terms. In addition,



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512 391-3515 / blorello@bdo.com

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the offerings made by alternative lenders are often tailored to specific borrower needs and are frequently combined with additional services to enhance the customer experience.

For instance, certain platforms not only provide loan products to help users refinance their student debt, but also provide them with personal loans and wealth management advice. As another example, some platforms offer free financial literacy tools in addition to providing loans to individuals with subprime credit scores. Other platforms focus solely on loans to small- and medium-sized businesses, real estate financing or consumer marketplace lending. Types of loan products range from revolving or invoice factoring lines of credit to more traditional amortizing loan products. While most alternative lenders concentrate on servicing unbanked or underbanked customers, others attract prime borrowers through better interest rates, shorter wait times or greater convenience.

Alternative lending platforms employ different methods to evaluate the creditworthiness of their customers. These may include traditional methods of measuring creditworthiness, such as examining FICO scores, ratios and payment histories, but also may include proprietary algorithms leveraging "alternative data," such as behavioral information, employment data and social media activity, which can provide a more nuanced credit risk profile and expedite credit decisioning.

DIGITAL PAYMENTS

Another category of fintech is the digital payment space. Digital payment companies offer new and innovative ways to make online and mobile payments, such as the transfer of funds between customers and businesses and between individuals. The models in this area enable the electronic transfer of payment, via direct account transfer or credit card payment processing.

The technology can be deployed in a mobile application, as a back-end service for online or brick-and-mortar businesses, or as a stand-alone service provider accessible on demand. These services can be configured to allow for a one-time or continued use to transfer payment and may involve retaining the individual's or business' banking information for future payments. In addition, certain companies provide hardware that enables the mobile processing of card payments, a boon for small businesses. These companies often also offer supplementary business services ranging from lending to inventory management to payroll processing.

FINANCIAL MANAGEMENT SERVICES

Emerging more frequently in the fintech space are companies that provide automated investment advisory and financial management services to individuals, trusts, IRAs and companies. The core objective of these services is to leverage technology to improve investment management and financial planning outcomes at lower fees than their human counterparts. Often these businesses enable investors to set up a portfolio that meets specified investment criteria based on their risk tolerance. The portfolio is then monitored by a proprietary algorithm for performance, rebalancing and tax exposure management.

Data analysis enables investment, savings, budgeting and planning decisions to be executed faster and with less human

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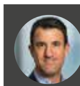
involvement. These services can be provided in a direct-to-consumer model through mobile applications and online platforms, or indirectly as white label products for chartered financial institutions and other service providers.

BDO INSIGHTS

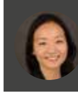
As fintech companies evolve their business models to keep up with technological advances, they can expect to face many industry challenges in the years ahead, including increased legal and regulatory scrutiny and sector competition.

Thankfully, however, we can expect the demand for fintech services to continue increasing as companies scale and voice their need for the painless processing of key financial transactions.

At the same time, the need for fintech companies to analyze large pools of data, operate on integrated lending and servicing platforms, offer more customized credit scoring, and develop new pricing schemes and product offerings creates opportunities for companies that deliver these solutions. These companies include those specializing in data analytics, artificial intelligence, blockchain, cloud services, cybersecurity and more. For tech companies looking to capitalize on a quickly growing market, fintech offers the perfect blend of business opportunity and long-lasting potential.



Anthony Ferguson is an assurance partner and active member of BDO's Technology and Financial Institutions and Specialty Finance industry groups. He can be reached at aferguson@bdo.com.



Alice Xu is an assurance manager at BDO, and can be reached at axu@bdo.com.

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