

# The Accelerating Convergence of Banks and Financial Technology

*A Perspective on Bank/FinTech  
Collaboration*

*January 2018*



Indigo Sky: The intersection of  
strategy and action.

# The Accelerating Convergence of Banks and Financial Technology

## Executive Summary

- I. Financial Technology ("FinTech") companies are proliferating
- II. As technology progresses at an ever-increasing rate, banks are searching for ways to develop innovation strategies
- III. Banks often choose to "fast-track" innovation by collaborating directly with FinTech companies and related technology companies through acquisitions, direct investments, strategic partnerships and incubation
- IV. Of these collaboration models, **FinTech currently comprises a relatively small portion of all bank activity**; but we see this proportion growing as more banks recognize the need to innovate and adapt within the FinTech space
- V. Regardless of the exact nature of the bank/FinTech collaboration, success is based on many factors, including alignment of objectives and the proper use of data
- VI. Indigo Sky works with FinTech companies to help with strategy, capital raising, partnerships, and M&A. We also work with banks and other financial services companies to devise and execute strategies to embrace innovation. We are well positioned to help financial services companies and FinTech firms collaborate.

3% of all recent bank M&A activity has been in the FinTech space and 19% of all direct investments



# The Accelerating Convergence of Banks and Financial Technology

## 1. Financial Technology ("FinTech") companies are proliferating

FinTech companies continue to proliferate as incubators, venture capital and private equity investors fund these new ideas and innovation. Of the roughly 4,000 companies in the U.S. that we classify in the "FinTech" category (1), over a third have received funding from investment firms. This level of activity demonstrates the significant interest and opportunity in this space.

## 2. As technology progresses at an ever-increasing rate, banks are searching for ways to develop innovation strategies

The pressure for banks to innovate and expand their product/service offerings has never been greater. Reliance on legacy technology (among other factors inherent to bank culture and the resulting impact on decision making) makes the iterative "test-and-learn" nature of innovation challenging.

The vast majority of the roughly 7,000 U.S. banks (and even the largest regional and national banks) still rely on legacy core technology systems that are difficult and costly to adapt.

## 3. Banks often choose to "fast-track" innovation by collaborating directly with FinTech companies in several ways:

- A. **Acquisition:** Purchasing 100% of a FinTech company.
- B. **Direct Investment/Private Placement:** Purchasing less than 100% of a FinTech company.
- C. **Strategic Partnership:** Entering into a relationship whereby the FinTech company provides loans, technology, and/or process to its bank partner.
- D. **Incubator/Other Development:** Developing an in-house or proprietary innovation channel, such as development labs or "hackathons."

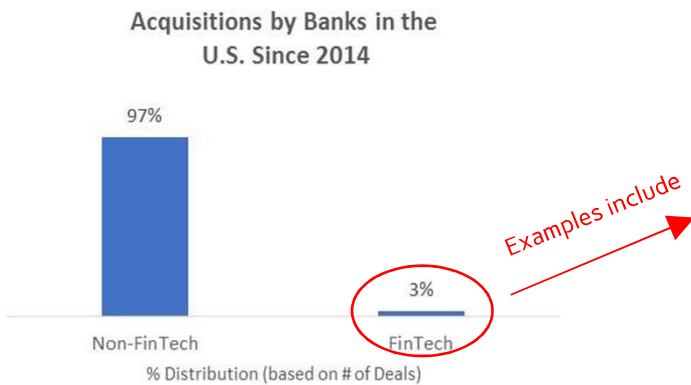
*See examples of these collaborations on the following pages*

(1) We define FinTech as companies in the following industry classifications that can apply their offerings to banks or similar financial institutions: Application software, Consumer Finance, Data Processing, Internet Software and Services, Specialized Finance, Systems Software (Source: Capital IQ)

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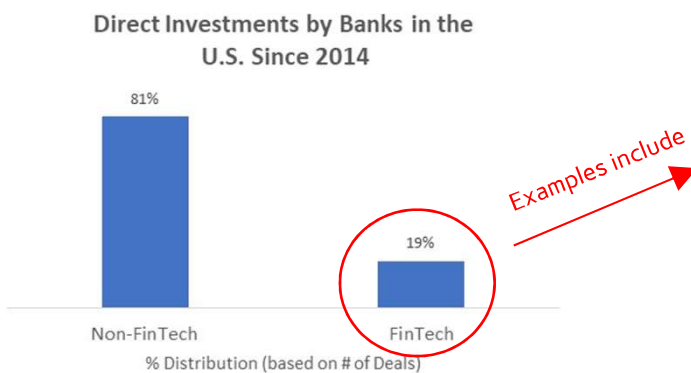
4. Of these collaboration models, FinTech currently comprises a relatively small portion of all bank activity; but we see this proportion growing as more banks recognize the need to innovate and adapt within the FinTech space

## A. Bank/FinTech Acquisitions



Announce Date	Buyer	FinTech Target
05/31/2017	<b>KeyBank</b>	<b>HelloWallet</b>
03/10/2017	JPMORGAN CHASE & CO.	<b>MCX</b> MERCHANT CUSTOMER EXCHANGE
12/12/2016	FIRST REPUBLIC BANK	<b>gradifi</b> paying down, looking up
09/20/2016	JPMORGAN CHASE & CO.	<b>investcloud</b>
08/05/2015	Silicon Valley Bank	<b>STANDARD TREASURY</b>
01/12/2015	<b>Capital One</b>	<b>Levelmoney</b>
02/20/2014	<b>BBVA Compass</b>	<b>SIMPLE</b>

## B. Bank/FinTech Direct Investments



Announce Date	Bank Investor(s)	FinTech Target	Announce Date	Bank Investor(s)	FinTech Target
05/16/2017	JPMorgan, US Boston, CentricCredit	<b>LevelUp</b>	11/26/2015	UMB Financial	<b>Hijro</b>
02/16/2017	JPMorgan	<b>openfin</b>	09/10/2015	Citigroup	<b>SELERITY</b>
01/31/2017	Bridge Bank	<b>buyerquest</b>	07/21/2015	Bridge Bank	<b>KINETIC</b>
12/21/2016	Wells Fargo, Citigroup	<b>AXONI</b>	12/01/2014	Washington Trust Bank, Live Oak Bank	<b>DEFENSESTORM</b>
10/05/2016	Fifth Third Capital Holdings	<b>ApplePie</b>	10/15/2014	Silicon Valley Bank	<b>evertrue</b>
05/13/2016	Wintrust Financial	<b>PAGEVAULT</b>	09/12/2014	Sterling National Bank	<b>USEREADY</b>
04/11/2016	Bridge Bank	<b>ALTITUDE</b>	06/30/2014	Comerica	<b>mblox</b>
01/21/2016	PNC, Citigroup, JPMorgan	<b>Digital Asset</b>	01/17/2014	Fidelity Bank	<b>Dropbox</b>
12/07/2015	UMB Financial	<b>rippleshot</b>			

Source: Capital IQ



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## C. Bank/FinTech Strategic Partnerships

"Strategic partnerships" are harder to quantify, as data for these types of transactions are less available and standardized. But strategic partnerships are an important tool for banks/FinTechs to collaborate in a less structured, more informal capacity (versus acquisition/direct investment). And because of their more informal approach, strategic partnerships may require less legal and regulatory review, making them particularly efficient for connecting FinTech companies into the global financial market.

### Partners

### Description



- On 12/7/17, SoFi and WSFS announced a two-year partnership agreement where WSFS will provide payment processing and debit card sponsorship services for a new cash management account by SoFi Securities, a subsidiary of SoFi
- The new "SoFi Money" account is expected to launch in early 2018



- GreenSky's partner banks make loans online or through the GreenSky® mobile app to customers of 12,000 merchants, ranging from retailers such as The Home Depot, Inc. to individual contractors
- In Sept 2016, GreenSky raised \$50 million in capital and established a \$2 billion lending plan with Fifth Third Bancorp in Cincinnati, Ohio



- Lendavor is a practice finance lender with an innovative software platform that improves efficiency, cost and quality, while dramatically reducing cycle times
- On 9/7/17, Lendavor announced a relationship with First Internet Bank to provide Lendavor with capital and initial funding to become a leading lender in practice finance



- On 2/28/17, Renovate America announced \$200 Million Credit Facility Warehouse line of credit from Bank of America, which will support continued expansion of HERO (Home Energy Renovation Opportunity) financing



- WebBank serves as the origination bank to several online lending marketplaces, including LendingClub and Prosper

Source: CrunchBase, Market Research

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## D. Bank/FinTech Incubator/Development

In addition to the external collaboration previously outlined, several banks have strategies to foster innovation internally:

- Bank of America Innovation Lab
- Wells Fargo Startup Accelerator
- Citi Ventures
- U.S. Bank "Hack Your Tomorrow"
- American Express Ventures



While there are many industry examples, we find the overall number of Bank/FinTech collaborations announced to date to lag what one might expect, given the high volume of industry publications, investor presentations, conferences, news articles, and blogs dedicated to the topic.

## So, what does the future hold?

We believe that the natural fit between banks' capabilities/needs and FinTech firms will promote symbiotic relationships in the future. In fact, continued technological innovation will propel this collaboration, including:

- Online/Mobile Convergence
- Blockchain
- Public Cloud
- Data Analytics/Customer Intelligence
- Artificial Intelligence
- Offshoring
- Cyber Security
- ...and the list goes on...

Source: Capital IQ



# The Accelerating Convergence of Banks and Financial Technology

## 5. Regardless of the exact nature of the bank/FinTech collaboration, success is based on many key factors, including alignment of objectives and the proper use of data

### A. An optimal FinTech partner should have a proven value-add solution that solves several bank problems

Given the large number of FinTechs, it can be challenging for banks to prioritize FinTech partnership opportunities. A FinTech partner that can provide multiple solutions will be at a competitive advantage, especially when factoring in the required third-party due diligence and political/bureaucratic hurdles for a bank to assess and execute on a FinTech partnership.

### B. Transparency around data security standards and expectations should be prioritized and re-emphasized during the partnership discussions and execution

Banks are highly regulated and often bureaucratic. As a result, banks have strict operational and compliance standards around how data is gathered, stored, used and (if possible) shared. In order for banks to evaluate the potential for a FinTech partner to solve a business problem, sharing a subset of this data is almost always required.

More often than not, FinTech firms often do not have the same level of standards in place around the use of data and its security.

A recent Crowe Horwath LLP/Compliance survey found that 66% of banks characterize their third-party risk management programs as immature or fairly informal; only a handful of respondents said their programs are mature (1).

We find a "best practice" is to have one person leading a group that is in charge of managing all FinTech partnership relationships throughout the bank. This level of focus can help the bank properly prioritize its focus and to ensure high-quality partnership execution.

(1) <https://www.crowehorwath.com/insights/managing-risk-bank-fintech-partnerships.aspx>

# The Accelerating Convergence of Banks and Financial Technology

5. Regardless of the exact nature of the bank/FinTech collaboration, success is based on many key factors, including alignment of objectives and the proper use of data (cont'd)

C. Both parties should understand each other's cultural and social environment, especially if the partnership is to be highly integrated in nature

Depending on the extent of desired integration, both parties should understand differences in employee culture and employee incentives and motivations. The most effective partnerships are ones with deep collaboration and shared vision/incentives.

According to a PWC survey, 40% of banks and 55% of FinTechs named "culture shock" as one of the most significant challenges to collaboration (1).

One way to address this concern is to avoid too much early focus on the "how" and prioritize focus on the "what." By "what," we mean shared visions and goals. If the ultimate objective remains clearly defined and emphasized, the day-to-day cultural differences are more likely to be overcome.

There are steps both parties can take to promote a stronger cultural awareness within the employee base, including:

- Jointly participate in hackathons and other idea-generating activities
- Highlight and study successful bank/FinTech partnerships
- Seek and encourage outside viewpoints

(1)<http://www.pwc.com/gx/en/industries/financial-services/assets/pwc-global-fintech-report-2017.pdf>



# The Accelerating Convergence of Banks and Financial Technology

**6. Indigo Sky Partners recently announced a partnership and strategic investment between First Internet Bank and Lendeavor, a practice finance lender with an innovative software platform. We are well positioned to help both banks and FinTech firms develop, evaluate and execute collaboration opportunities.**

The Lendeavor/First Internet Bank partnership is an archetype for future financial technology and depository relationships.

Lendeavor is a practice finance lender with an innovative software platform that improves efficiency, cost and quality, while dramatically reducing cycle times. The relationship with First Internet Bank provides Lendeavor with the capital and initial funding to become a leading national lender in practice finance.

The strategic partnership is the first of its kind in the practice finance industry and the first-ever equity investment made by First Internet Bancorp. Indigo Sky's cross-functional expertise and deep knowledge of financial institutions and technology were fundamental to Lendeavor reaching this important corporate milestone.

The opportunity for growth and innovation through Bank/FinTech collaboration is massive. To move forward successfully, market participants need to be strategic in their approach to achieve long-term goals.

Indigo Sky Partners has experience at large, complex financial institutions and is working with FinTech companies and other innovative organizations to reach the next stage in their journey.

Read more about the Lendeavor/First Internet Bank strategic partnership here:

<http://www.indigoskypartners.com/newsroom/>

# Indigo Sky Partners, LLC

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- We are well positioned to help both financial services companies and FinTech firms collaborate.



### STRATEGY CONSULTING

In our changing world, choosing where to focus your business is key to your success.

We help you decide where to deploy scarce resources for maximum leverage in your industry.



### FINANCIAL ADVICE

We find the right financing partners suited to the needs of your business.

We develop strategic partnerships, leveraging your skills and assets.

We architect M&A strategy and advise on execution.



### CAPITAL

We selectively invest capital to help our partners achieve their goals.

We are interested in a wide variety of industries, stages, and structures, preferring situations sourced through our consulting and advisory practice.

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