ROSENBLATT SECURITIES

FinTech Investment Banking Viewpoint

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Cutting the Gordian Knot That Has Restricted Financial Inclusion

No Customer Left Behind

Suddenly, Financial Inclusion is hot in America. Five years ago, we used to hear about it, but more often in the context of Africa or South Asia. Now, we have entire conferences on the topic. It's not like we have become more altruistic all of a sudden or developed a conscience. So, what explains all the new FinTechs focused on historically under-served customer segments from the unbanked, to farmers, women, minorities, international students. What's the answer? Once more, it's the technology, stupid!

Inclusion Redefined

We define inclusion more broadly than the narrow interpretation of the term that mainly denotes serving the unbanked. Our definition of Financial Inclusion is the provision of financial services to a customer segment that didn't have, or had limited access to, services in the past. It includes expanding, improving and providing fair access to financial services to customers. As an example, women as a customer segment have access to financial services, but often at a somewhat lower or sub-optimum level than men. Similarly, international students coming to the US to study eventually get banking, investing and insurance services, but don't have access to it in the first few months of arrival due to the lack of a social security number or US credit history. Our definition of inclusion includes all these use cases and therefore, is much broader than simply serving the unbanked.

An Incredible Opportunity

The central structural impediment in providing access to financial services to under-privileged customers or folks at the bottom of the pyramid, has been the high cost of providing services, relative to their customer acquisition costs and the life time value of the customer. To put it simply, it has been too expensive to serve the poor. So any attempts to serve customers at the bottom of the pyramid have been short lived, or difficult to scale. Most successful efforts at serving the under-privileged have been driven by nonprofits or governmental initiatives which are difficult to scale, or politically dependent.

But things have dramatically changed in the last few years in several ways:

- The cost of technology has dropped and new innovations can be leveraged to drastically lower the cost of service provision for all kinds of services, from plain bank accounts to investment advice. That means providers can serve customers at the lower end of the financial scale, and still eke out a profit. The conundrum of 'doing good' and 'making money' has been addressed.
- Digital technology allows services to be customized, personalized or fine tuned to the needs of individual customers. Again, something that wasn't possible earlier when everyone got the 'same sized shirt'. That allows bespoke services to be rendered to customers.
- The third dimension of what's possible now is that we can identify small customer niches and service them with more tailored products. Think products geared towards the specific needs of culturally similar communities (insurance for Hispanics in Florida), or international students coming to US universities.
- An over reliance on cash for transactions and the lack of a transaction account, have also been serious impediments to financial inclusion. Again, a number of technological changes are fixing this issue. Developing regions (sub Saharan Africa, south Asia) have already proven that digital payments can be mobilized through smart phones, and the phone can be then used as a platform for higher value financial services (credit, insurance, investments).
- The last structural impediment to inclusion that technology is addressing is the risk of fraud, abuse and reliability of financial services available to particular customer segments. Certain customers (usually the unbanked) are much more vulnerable to such risks which reduces their adoption of electronic cash and engage in digital transactions. That in turn causes high costs, exploitation and unfair access to financial services. The combination of advanced technology and accompanying infrastructure (digital identity, mobile networks, reliable electricity) removes some of these impediments.

Investing, Banking Opportunities

With the Gordian knot that restricted financial providers from serving customers at the bottom of the pyramid or in narrow customer niches having been cut, we are seeing a healthy pipeline of FinTechs starting businesses that serve customers who were inadequately served until now. VCs are also more willing to fund FinTechs that are on a mission to help the under-served or target neglected customer segments, while building a sustainable, profitable business that can scale, grow and even go public. At Rosenblatt's 11th FinTech Summit, we will showcase five enterprising FinTechs that are using technology to drive change in society while building profitable, high valued businesses. Come, listen to their story…