# FinTechs and banks:
# Cooperation and coopetition

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***Abstract***:
Between FinTechs and banks, the die has not yet been cast. Some observers think that the days of the "banking mammoths" are numbered; others, that FinTechs will be disruptive enough to become dominant players in finance. However the future of finance implies cooperation between players on this market, even though competition will exist as long as market positions are not stable. FinTech strategies of innovation clearly stem from a perception of trends in demand, but innovations are not an exclusivity of these newcomers. Forms of cooperation (shareholding or partnerships) in R&D and distribution have already taken shape in the banking and insurance industries. The ACPR, the French regulatory authority, is examining the viability of the business models of some "new" banks and the limits of cooperation (or coopetition) between players. The new paradigm is not yet stable.

The clients of financial services are looking for the fluid, multichannel, uninterrupted experience of operations straight-through processed (STP) around the clock. In the race to improve the "customer experience", can banks win alone? Can they count on the digitization of their services as an answer to client demands? Should they seek out allies? The point was made by Ana Botin, head of Santander, in the following words: "*The way we internalize and appropriate the new technology in the coming years is going determine our success.*"[1]

Since 2014-2015, the majority of traditional banking establishments have preferred partnerships to confrontation. But what forms can these partnerships take? Recent examples illustrate partnerships that have taken shape around services, equity sharing, repurchases or resales. As traders say, "To err is human, and you have to know how to take losses fast." Meanwhile, banks by themselves, without partners, have designed low-cost services.

[1] This article, including any quotations from French sources, has been translated from French by Noal Mellott (Omaha Beach, France). The translation into English has, with the editor's approval, completed a few bibliographical references.

## Innovations are not the prerogative of newcomers

Several scenarios coexist that are leading to changes in banking processes. A few “unicorns” will be able to impose their brands and cruise for a long while on their success. Let us hope some of them will be French! Many others will, to ensure the durability of their business, prefer entering into partnerships with banks. Finally, some of these “neobanks” will abandon the race for want of the necessary volume of business, funding or profitability, while others will choose to be bought out (which is not at all shameful), often by established players. To summarize these scenarios:

- PARTNERSHIPS: Let us cite as example equity alliances: BNP Paribas acquiring Compte Nickel, or Crédit Mutuel Arkéa buying Leetchi, a crowdfunding platform. In synch, BPCE acquired Pot Commun (similar to Leetchi) and then the “mobile bank” Fidor; Crédit Agricole took equity in Linxo (a budget management application); and Edel (a banking subsidiary of E. Leclerc Group) acquired the FinTech Morning. In 2017 and 2018, the number of alliances of this type soared.

- FROM FINTECHS TOWARD BANKS: Making an offer that combines cooperation and coopetition is the DNA of the big digital service-provider firms, like ATOS, especially in four areas — the customer experience, operational excellence, the management of risks and compliance, and “digital” technology (data analytics, cloud services, etc.) — but without excluding competition with the offers of Wordline, which has obtained banking licenses for payment services.

- FROM BANKS TOWARD FINTECHS: in the opposite direction but for identical purposes, Natixis tried, in the autumn of 2018, to buy Ingenico. Initiatives launched by the Big Fours (GAFA and BATX) and telecommunication operators have met with success, at least in operational terms (while waiting for confirmation from the financial results)!

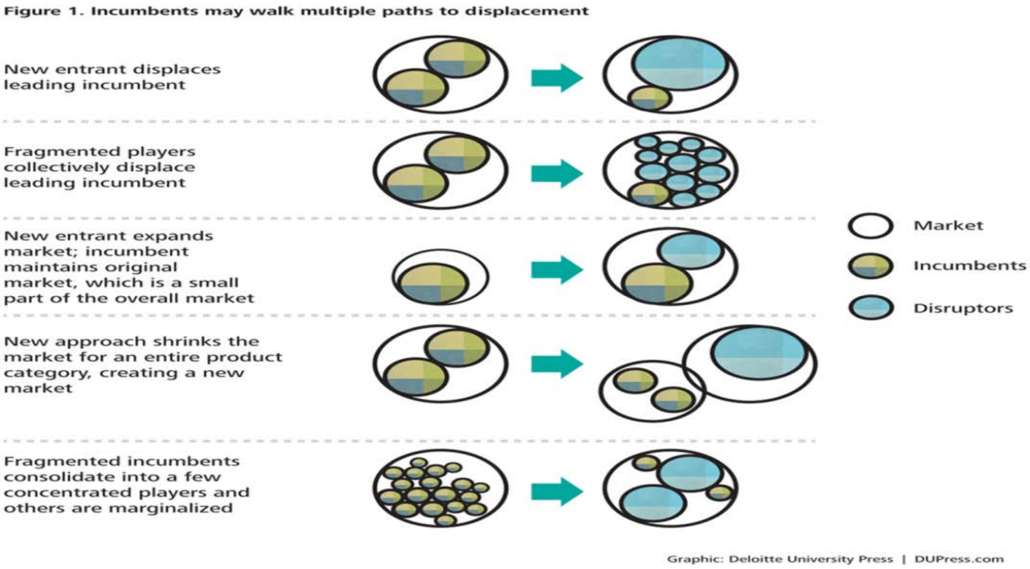
- FINTECHS ALONE: Some FinTechs have grown while competing alone: 27 of them have become unicorns with an equity market capitalization of more than one billion US dollars! During the last three years, venture capital from institutional or private investors has funded several FinTechs. Given this sector’s growth and potential, venture capitalists have not made a mistake. In 2015, investments in start-ups in finance exploded; and recurrent fund-raising campaigns, increasing threefold from 2014 to 2015, held the headlines of business news.

## For sure, the banking industry will have to adapt to a new paradigm

Users have taken a liking to these new ways of consuming banking services. They no longer tolerate services that are not on par with those offered by FinTechs: speed, real-time operations, practicality, user-friendly, broad support, transparency….

The banking industry will have to adapt to a new paradigm with the following properties: openness (in the form of APIs) toward third parties and the paragon of open banking; platforms set up in “lego” to facilitate the creation and distribution of services; and novel partnerships with players on all sides (FinTechs, GAFA, automakers, smart cities, the Internet of things, etc.).

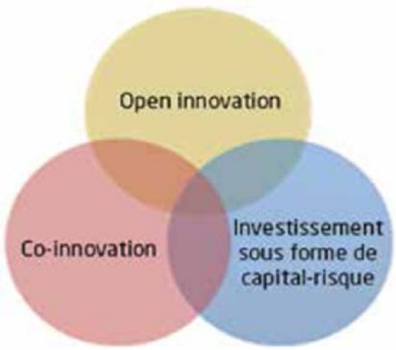
**Figure 1**




Given the possibilities for making price comparisons and the proliferation of business models claiming a low-cost approach, the pressure on prices will intensify, at least for basic services (or the services thought to be basic), as has happened in air travel. This will force historical players to redesign their business models.

Clients, ever more clairvoyant and targeted, will shop for financial products and services as they see fit. They will deal with whoever makes the cheapest or most pertinent offer in relation to their expectations. So, finding one-stop clients who use multiple services will be even harder than nowadays. A client will have his current accounts at one bank, his credit/debit card at another, will make money transfers or take out home or consumer loans or place his savings at other establishments… The EU's second Payment Services Directive (PSD2) boosts the client's position in matters related to current accounts or payment services.

**Figure 2**

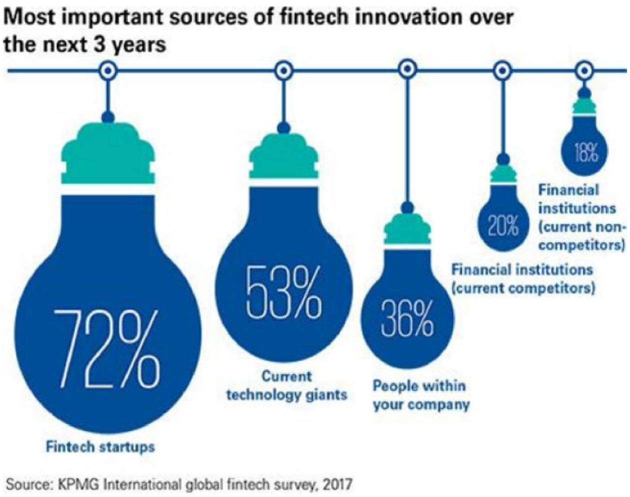



While FinTechs have the wind in their sales, banks have decided to support innovation. The question of cooperation or competition between the big banks and FinTechs is increasingly cogent. Might the answer not be coopetition, this relation in between partnership and competition?

# To the advantage of FinTechs: Their strategies of innovation

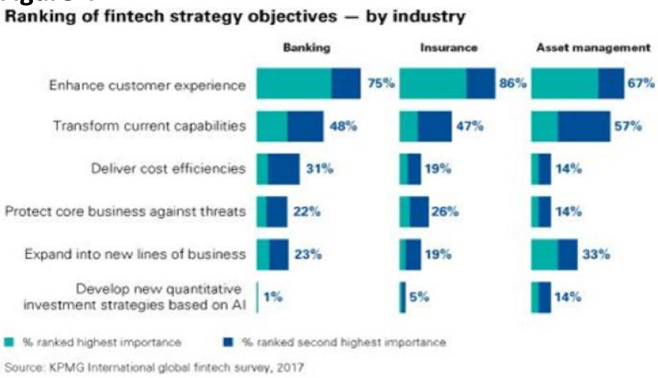
The new financial services called FinTechs benefit from the strong interest of investors and consumers in their ability to offer a value-added, customer-centered service based on digital technology. They thus respond to a need expressed by clients that the big banking institutions have not taken into account.

**Figure 3**




FinTech strategies of innovation clearly correspond to this perception of trends in demand. Banks are much less agile than FinTechs for winning over clients, acquiring and managing volumes of data, or rolling out new services. Given their massive clientele however, what makes sense is cohabitation. Banks envy FinTechs' dynamism, technology and feeling for the client experience, while FinTechs dream of gaining access to the clientele of banks. Partnerships with big banks would put them on a fast track for reaching the break-even point and significantly increasing their market share. As for banks, they can but observe the increasing lack of points of transaction with their clients. Even though current account operations are still being made via traditional banking services, some of them are being diverted toward applications (such as Bankin) or robot-advisors (like Yomoni). A partnership with players who have designed solutions that the banks themselves are not capable of offering — owing to regulatory restrictions and to their structural and cultural rigidity — would enable banks to strengthen their now fragile bonds with clients and better adapt their offers to them. Fortuneo and BforBank have clearly understood this, evidence being their white label, the aggregator Linxo.

**Figure 4**



## French regulatory authorities' concern about the profitability of FinTechs

The ACPR (Autorité de Contrôle Prudentiel et de Résolution, the French regulatory authority which oversees the banking and insurance industry), while stating that online banks and "neobanks" have "*gradually managed to settle in the French banking landscape, despite its maturity*" and play an important role "*in the race to innovation*", has also raised questions about their future profitability (BEAUDEMOULIN *et al*. 2018). In this study released in October 2018, the ACPR analyzed these new players' business models and drew attention to the uncertainly surrounding their development.

Based on a panel of twelve establishments (a mix of FinTechs, newcomers from other industries, and banks in big banking groups), this study estimated the market share of FinTechs at 6.5% in France, and 3.9% of current accounts. The positions staked out by FinTechs account for this differential. Since the start of the century, these "neobanks" have oriented their activities toward savings and brokerage. With the upsurge of offers for current account services and real estate loans — activities now at the core of their strategy of conquest — they managed to gain 1.3 million clients in 2017: 33.5% of new clients in the banking industry.

In the medium run however, these players have to continue attracting clients if they are to turn a profit. In effect, they are penalized by an income/client ratio that amounts, owing to their aggressive price-setting, to but €138. According to this study, "*Although the players surveyed in our study have the ambition of reaching a total of 13.3 million clients by the end of 2020, nothing lets us predict a growth of the French market.*" By the way, this total would amount to tripling their clientele. Besides mentioning low demographic growth, the ACPR pointed to the recent decline in the number of persons holding accounts in several banks: down to only 31% in 2017 according to Bain Cabinet. It also pinpointed the still low penetration rates for loan or insurance services (respectively 10% and 20%). Moreover, among the clients of these new banks, 14% are economically inactive; and only 23% make the new establishment their principal bank.

Another challenge to these newcomers in the banking industry is to control costs. According to the ACPR, their average operating ratio is 138%. Furthermore, it is strained by marketing expenditures. The cost of special offers to clients (bonuses, etc.) amount to as much as 24% of their net banking product [*i.e.*, value added]. In the ACPR's opinion, "*What is at stake for these new players is whether they will eventually be able to reduce these marketing expenditures while keeping the clients they have won*" (BEAUDEMOULIN *et al*. 2018).

## Coopetition and its limits

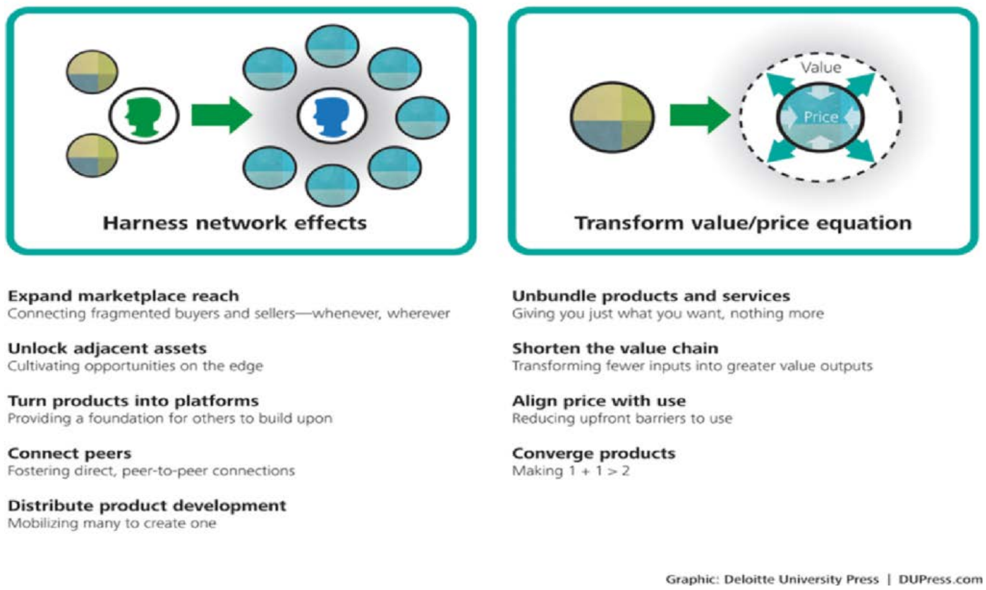
Ever more aware of the benefits to be drawn from cooperation with startups in the world of finance, traditional banks are turning toward FinTechs. Several initiatives have been taken in the past few years for facilitating communications and meetings.

BNP Paribas' WAI label (We Are Innovation) or Crédit Agricole's Village, which assemble approximately 150 startups, are concrete examples of these banks and neobanks moving closer together. These specialized poles and labels in France are a means for remaining in touch with new market trends and technological innovations (such as big data or artificial intelligence).

Increasingly recognizing the advantages of startups, the big banking groups are trying to understand how these newcomers work. After all, startups, free from any organizational burden inherited from the past, have the advantage of starting out fresh. The big groups draw ideas from these bold, creative, hard-working entrepreneurs and from their way of successfully conducting projects — ideas for reforming the bank's (often long and complicated) business processes. Finally, these big banks use startups for leverage to attract new skills. In 2018, the banking industry's attractiveness on the job market fell (-2.4%) while that of FinTechs rose (14,1%).[2]

**Figure 5**

Figure 5. Nine patterns of disruption




As for FinTechs, these initiatives offer them more visibility and a solid, viable backing. They are a stepping stone, an accelerator of growth.

Besides what has already been mentioned, other forms of cooperation have taken shape. La Banque Postale, Crédit Mutuel Arkéa, Natixis, E. Leclerc Bank, BNP Paribas… all these big names in banking and finance have recently acquired FinTechs to enhance their portfolio with innovative services, develop a new commercial axis and, above all, accelerate their strategies of digitization. The banks are thus trying to adapt to the new patterns (crowdfunding, money transfers, etc.) observed on Web platforms.

Not all FinTechs are fated to be bought out however. SlimPay, which works closely with several established financial institutions (including Ingenico, Arkéa and Crédit Mutuel), makes its technology and know-how in direct debit payment services available to its partners for the joint development of new solutions for e-retailers. Though sometimes competing directly on bid solicitations, the partners share an interest, namely: to offer a rapid, fluid, customer-centered payment service.

So, there is no single form of cooperation. Depending on each party's needs and ambitions, a dialog and communication can be engaged around a common project. Participate in a first project, benefit from the "freshness" of the one party and the "old-hand" skills of the other, and capitalize on the resulting synergy. These two worlds are complementary and can continue growing together.

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[2] Source: Maddyness.

Despite the good intentions that the big groups have toward startups, the latter must remain alert. They have to watch out lest they be swallowed by a big partner, and lest their dependence on cooperation turns them into a mere R&D or proof-of-concept laboratory for a big group (and they thus forget to work out their own sales strategy).

Despite ever more initiatives for accompanying startups and accelerating the digital transformation, only a union of forces will enable France to stand out in the highly internationalized, highly competitive banking and financial industry. Given international markets with quite different investment policies and “interbank” relations, France is lagging with regard to investment and venture capital. The FinTech potential has not been fully explored. It is enormous, a real capacity for overhauling finance in the near future. Will a French unicorn stand out and leap ahead?

## Conclusion: Truth is not black or white

According to PWC’s *Global FinTech Report 2017*, several factors are intensifying competition in retail banking services: a continually increasing number of offers and service-providers; the client’s ease of accessing services and making comparisons; development without borders; the low-cost temptation; the risk of run-of-the-mill products, etc.

Besides stimulating established players, the “neobanks” are imposing new standards. No doubt about it: tomorrow’s bank will be a concentrate of digital high tech, services with added value… and the right dose of humanity.

New indicators are going to be used to categorize players still in the race and position them along a new value chain, which is still changing under the forces stemming from open architecture and APIs, mustered by the catchwords “mobile first” and “cross-channel” connections among service-providers, rallying around new business models and market positions, aiming at the sharing economy, etc. Underlying all of this is the issue of control over customer relations and of the income stream flowing from these relations.

In this moving, even uncertain, environment, banks are not lacking advantages and means that they could use to withstand this tidal wave. Though often accused of being cumbersome, they, too, know how to bring together the right forces for adapting their offers, making clients loyal and launching new conquests.

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