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WITH THE FED

*Beyond Today's Financial Headlines*



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# **“Fintech”**

## **How Financial Technology Is Transforming Banking**

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# What is fintech? Let's start with a story.

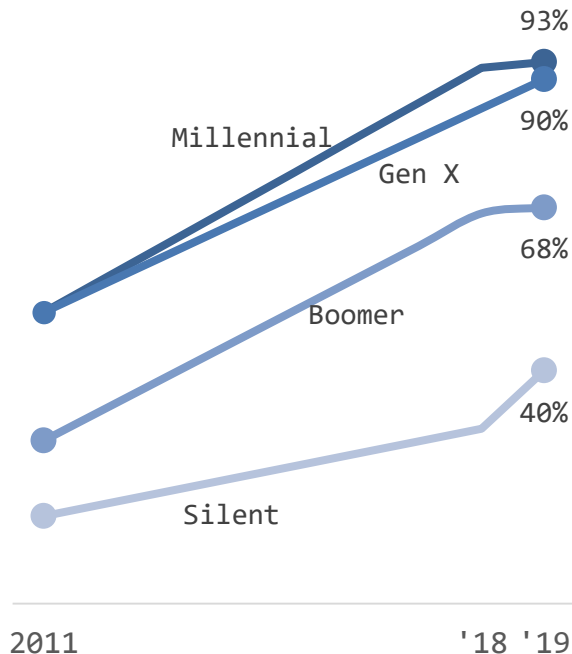


Photo: Getty Images / Kaca Studio

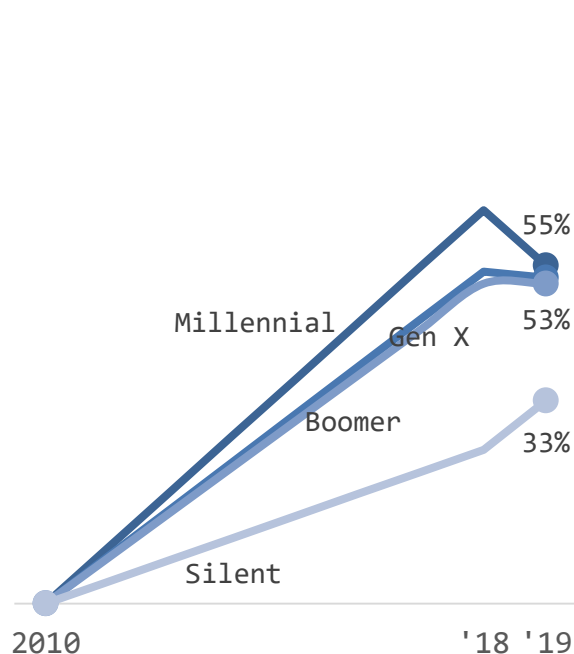
# Not surprisingly, consumers are rapidly adopting the digital life.

% of U.S. adults in each generation who say they

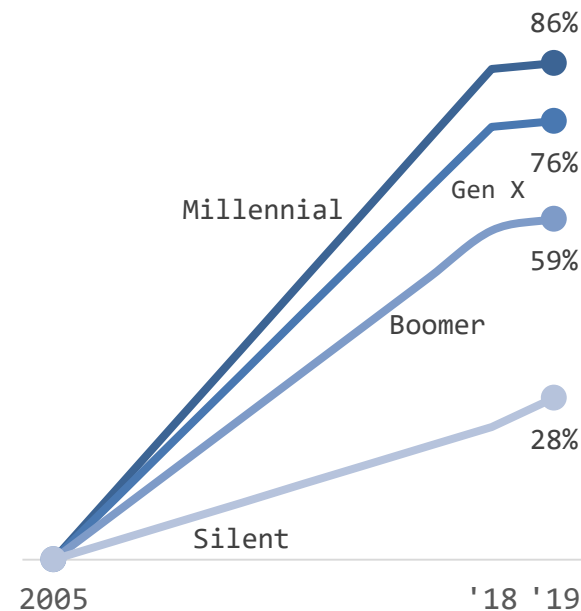
## Own a smartphone



## Own a tablet computer

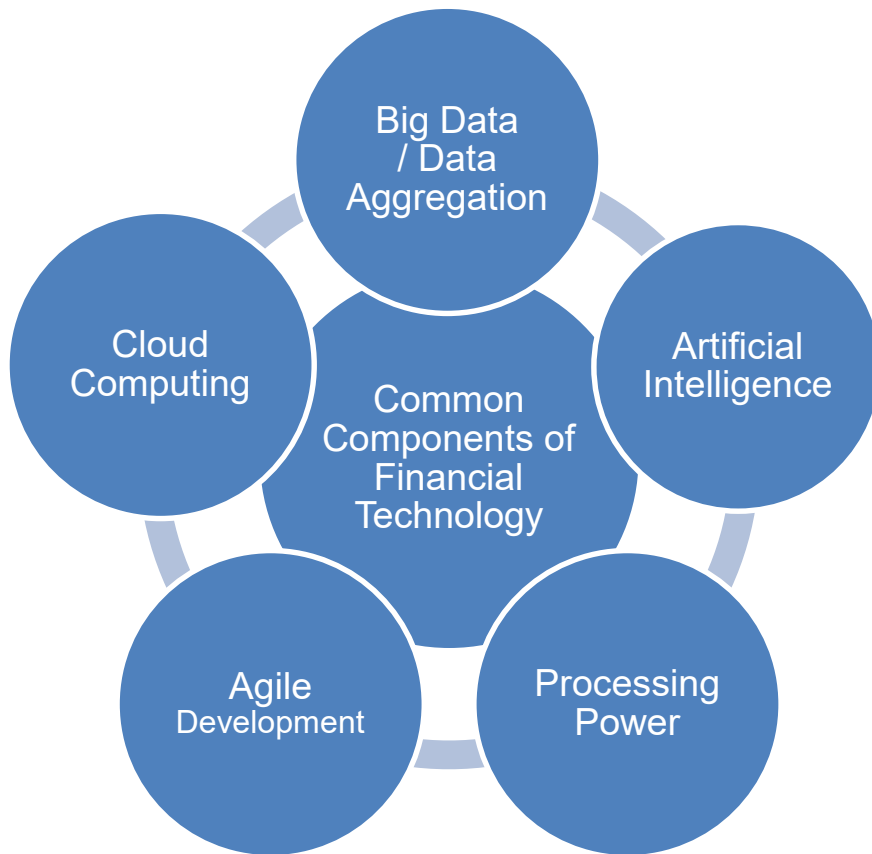


## Use social media



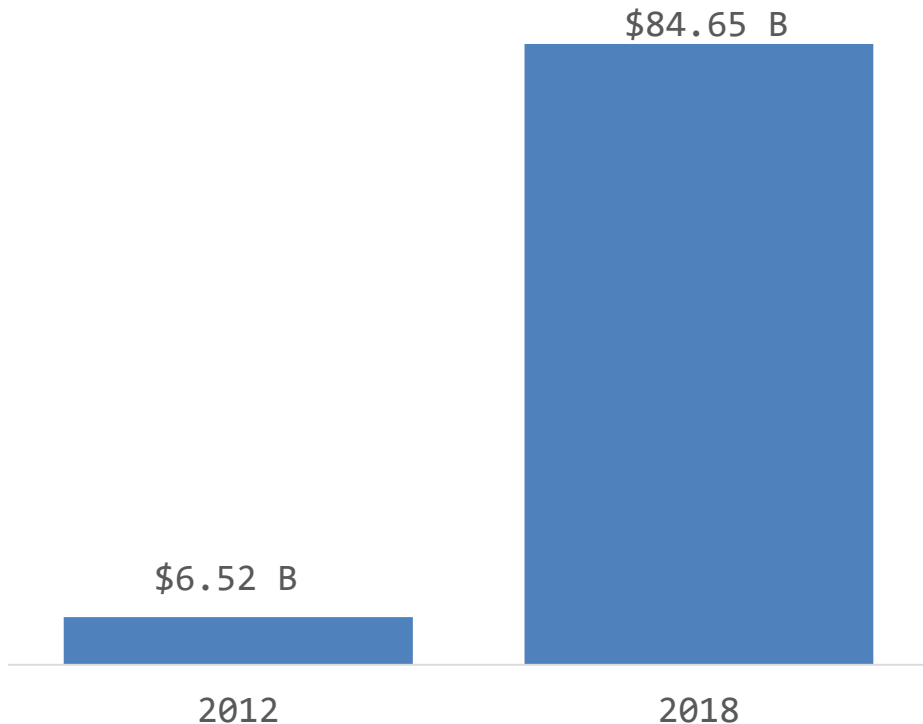
Source: Pew Research Center, September 2019

# Massive amount of data and faster computing drive the experience.



# Square started its business in payments. However ...

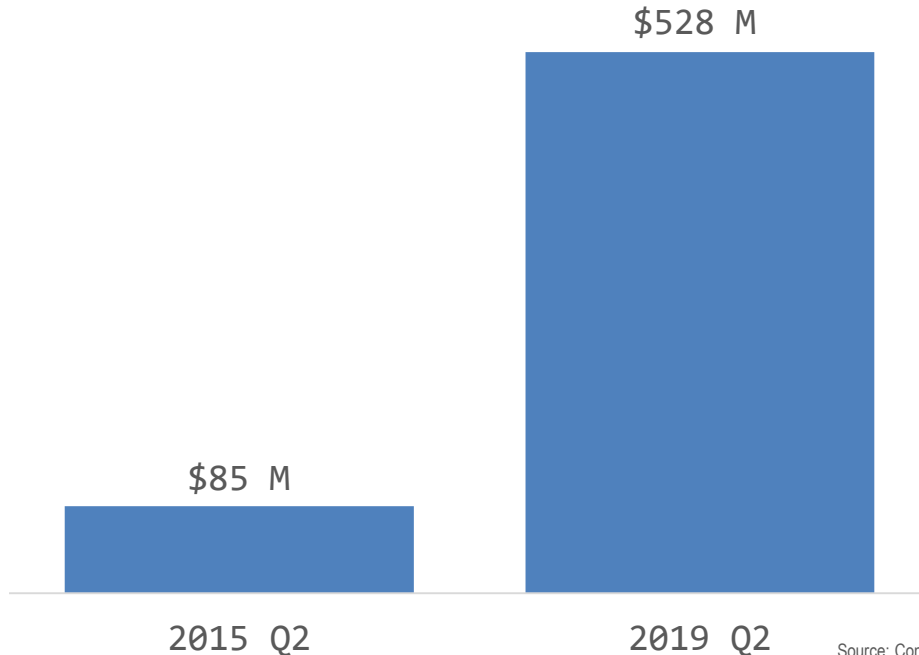
Gross payment volume of Square



Source: Company filings. Photo: Square media resources.

**...the payments data is also cash flow data.**  
**Square parlayed its payments service and introduced Square Capital.**

## Quarterly volume of Square Capital loans

[illegible]

# Credit scores and cash flow data are often used in fintech lending. But nontraditional data can be used, too.

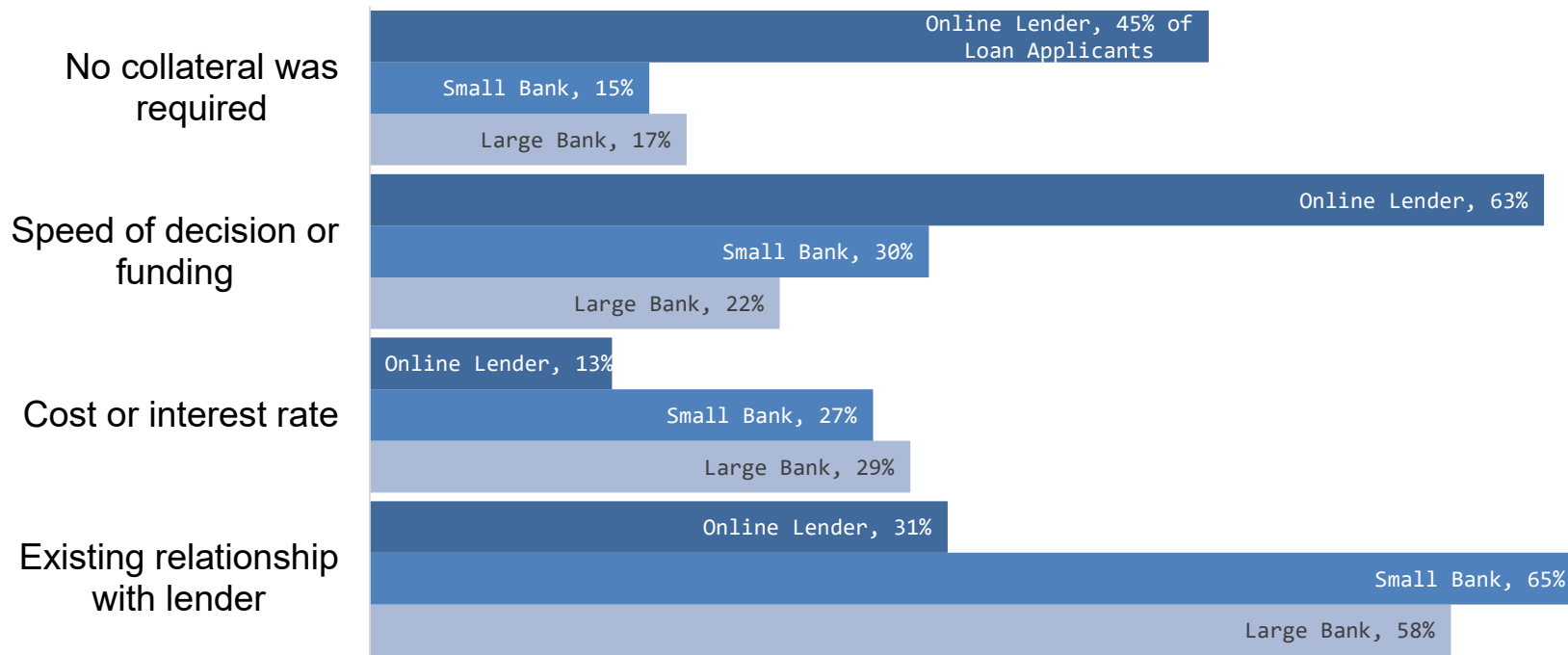
- Billing and payment history, including cable, utilities, phone, insurance and even alimony payments
- Operating system
  - research shows that owning an iOS device is a strong predictor for being in the top quartile of the income distribution, suggesting lower default potential
- Information on level of education
- Digital “breadcrumbs,” such as activity on social and professional networks



# Complex technology can make it more difficult to understand risks to consumers

- Fair lending laws and regulations
- Unfair or Deceptive Acts or Practices (UDAP)
- Fair Credit Reporting Act (FCRA)

# Some businesses choose to use web-based alternatives because of speed and flexibility



Source: 2019 Federal Reserve Small Business Credit Survey

Note: "Online lenders" are defined as nonbank lenders including Lending Club, OnDeck, CAN Capital, PayPal Working Capital, Kabbage, etc.

# Fintech isn't all about lending and payments. Popularity of digital wallets is also rising.



**Cash App by Square**



**Venmo by PayPal**



**Zelle by *your* bank**

Venmo, Square Cash and others have also begun to issue physical payment cards tied to in-app accounts.



Image: Apple media resources

**Online demand is also increasing for savings accounts and certificates of deposit.**



**RISING BANK**



**Marcus:**  
BY GOLDMAN SACHS

 **Citizens**  
**Access** 

# Fintech firms rely on bank partners for certain key services unless they are part of a bank.

- Access to deposits or deposit-related data
- Clearing and settlement services
- Loan origination on a national level



Image: Sorbetto / Getty Images

# Nonbank fintech firms are also exploring other options, such as:

- Becoming a bank
- Becoming an Industrial Loan Company
- Obtaining a national bank fintech charter



AMERICAN BANKER

## **Square's banking bid avoids backlash that doomed Walmart's**

WASHINGTON — As Square seeks federal approval for a Utah industrial loan company, the fintech's bid has so far avoided the kind of loud, public opposition that marred past ILC bids by higher-profile nonbanks.

# Example: Apple's Titanium Card



Image: Apple media resources; Rapha Designs



# Closing thoughts

- Customers are demanding more technology services to deliver traditional banking services.
- Financial technology will allow banks to increasingly compete well outside of their traditional markets, but traditional banking will need to evolve to meet customer preferences. Most likely, consolidation of bank charters and branch closings will continue, if not accelerate.
- Nonetheless, the performance of algorithmic models during stressed conditions is unknown. It is critical that credit remain available during an economic downturn.



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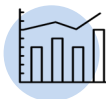
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