Financial technology (FinTech) is a broad term used to describe the integration of technological advancements within financial-related business processes. Many investors might think of the FinTech industry as something that has evolved over the last decade. The term FinTech has only been used over the last few years, but advances in financial technology are not new. It’s clear to us FinTech is well-established, starting in the 1950s with credit cards and followed in the 1960s by automated teller machines (ATMs), the 1970s by electronic trading, the 1980s by mainframe computers, and the 1990s by e-commerce.¹ Historically, most FinTech innovations have come from the financial services industry, but the impacts have been felt in other industries as well.

No one can predict with certainty which areas of FinTech will lead to the next significant wave of disruption. However, we believe there are several growth catalysts for FinTech, including the rise and practical application of artificial intelligence (AI); distributed ledger technology, or DLT (that is, blockchain); and the wide adoption of mobile technology. The latest PwC Global FinTech survey projects annual returns on investment on FinTech-related projects will be 20% globally (Chart 1).

Here we highlight four areas where we anticipate FinTech will significantly shape growth:

- capital markets;
- the financial services value chain;
- developing economies; and
- e-payments.

Navigating the Adoption Curve: Sources of FinTech Growth

Partnerships Between Capital Markets Providers and FinTech Companies

According to a recent McKinsey study, many FinTech companies will look to partner with larger, more established capital markets companies and vice versa.² These capital markets providers comprise a global network of organizations that securely carry out transactions, ranging from trade execution to the custody of assets, across investment markets. Many of these partnership opportunities have proven to be mutually beneficial.

Corporations and capital markets providers view the integration of FinTech as a potential source of new revenue and an opportunity to leverage technological innovation to enhance productivity. While FinTech firms may be able to bypass some of the largest barriers to entry, particularly in developed economies, they often lack the resources or capital needed to compete directly with established capital


markets providers. Consequently, FinTech activity within capital markets infrastructure has grown almost 300% since 2010 (Chart 2). Additionally, a recent report from International Data Corporation estimates financial services firms worldwide will spend approximately $500 billion by 2021 on information technology, up from an estimated $440 billion in 2018. We believe FinTech companies are well positioned to capture a growing portion of these budgets.

Innovation Across the Financial Services Value Chain

FinTech firms are designing new ways to enhance existing processes throughout the entire financial services value chain. For example, crowd-funding platforms offer easier access to capital and simultaneously close any gap between issuers and investors. Fifty percent of consumers use FinTech money transfer and payments services, and 88% anticipate doing so in the future. Additionally, the emergence of robo-advisors has driven fee compression across the investment management industry, making investments more accessible to a larger percentage of the population. Peer-to-peer lending offers relatively low interest rates and quicker access to funds than traditional bank loans. FinTech is also helping to facilitate trade execution,

Robo-advisors offer financial services digitally via the internet with limited human interaction.

---


5 Emerging Markets: Driving the Payments Transformation, PwC Global, https://www.pwc.com/gx/en/industries/financial-services/publications/emerging-markets-driving-payments.html. ©PwC. Not for further distribution without the prior written permission of PwC. PwC refers to the U.S. member firm or one of its subsidiaries or affiliates, and may sometimes refer to the PwC network. Each member firm is a separate legal entity. Please see www.pwc.com/structure for further details.

with a focus on emerging asset classes such as cryptocurrencies.

Today the use of blockchain/DLT has begun to help streamline clearing, custody, and settlement processes, resulting in significant cost savings for financial institutions. McKinsey estimates the use of DLT within the over-the-counter derivative markets alone, for example, is a $4–7 billion value-generation opportunity. The use of DLT in posttrade services has already begun, with the Australian Securities Exchange (ASX) transitioning to a DLT system in March 2018 to help reduce posttrade reconciliation times and costs. Switzerland’s stock exchange recently announced it is building a fully integrated trading, settlement, and custody infrastructure for digital assets, mainly based on DLT. The Swiss exchange will then be able to trade assets that were previously not tradable.

Developing Economies

Developing economies are home to 85% of the global population and nearly 90% of people under the age of 30. As millions of unbanked or underbanked people in developing economies enter the digital era over the coming years, who will likely require a variety of financial services, there is $380 billion in potential revenue, according to Accenture. FinTech providers are well positioned to lead in these markets, in our view. Digital offerings are more scalable than traditional banking and investment services, which require higher start-up costs relative to FinTech services. Today, most banking services are available online or through mobile applications. For example, mobile payment services such as PayPal and Venmo along with online lenders such as LendingTree or Sofi bypass traditional banking infrastructure, including branches and ATMs.

E-Payments

Historically, digital payment services have served as a gateway technology introducing consumers to digital financial services. For example, PayPal introduced U.S. consumers to mobile payments and ushered in e-commerce in the early 2000s. Developing economies offer a significant growth opportunity for digital payment service providers, with momentum already building (Chart 3). Total digital payment transaction values in dollars continue to be dominated by the developed economies of the United States, United Kingdom, Germany, and Japan.

FinTech companies are leading this digital revolution, and we believe they may dictate the way unbanked and underbanked residents of developing economies enter the marketplace.

---


8 Emerging Markets: Driving the Payments Transformation, PwC Global.

Conclusion

History has shown that technological innovation within the financial services industry is constantly evolving. In our view, advances in financial technology are poised to lead future generations of growth across capital markets, the financial services value chain, and within developing economies.

Erik Casalinuovo, CFA
Director, Investment Strategy

John Ravalli
Managing Director of Portfolio Strategy

Benjamin D. Ziolkowski
Associate Investment Advisor

For more information, please contact your Hawthorn advisor.

The PNC Financial Services Group, Inc. (“PNC”) uses the marketing name Hawthorn, PNC Family Wealth® to provide investment, wealth management, and fiduciary services through its subsidiary, PNC Bank, National Association (“PNC Bank”), which is a Member FDIC, and to provide specific fiduciary and agency services through its subsidiary, PNC Delaware Trust Company or PNC Ohio Trust Company. Standalone custody, escrow, and directed trustee services; FDIC insured banking products and services; and lending of funds are also provided through PNC Bank. This report is furnished for the use of PNC and its clients and does not constitute the provision of investment advice to any person. It is not prepared with respect to the specific investment objectives, financial situation, or particular needs of any specific person. Use of this report is dependent upon the judgment and analysis applied by duly authorized investment personnel who consider a client’s individual account circumstances. Persons reading this report should consult with their PNC account representative regarding the appropriateness of investing in any securities or adopting any investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not be realized. The information contained in this report was obtained from sources deemed reliable. Such information is not guaranteed as to its accuracy, timeliness, or completeness by PNC. The information contained in this report and the opinions expressed herein are subject to change without notice. Past performance is no guarantee of future results. Neither the information in this report nor any opinion expressed herein constitutes an offer to buy or sell, nor a recommendation to buy or sell, any security or financial instrument. Accounts managed by PNC and its affiliates may take positions from time to time in securities recommended and followed by PNC affiliates. PNC does not provide legal, tax, or accounting advice unless, with respect to tax advice, PNC Bank has entered into a written tax services agreement. PNC does not provide services in any jurisdiction in which it is not authorized to conduct business. PNC Bank is not registered as a municipal advisor under the Dodd-Frank Wall Street Reform and Consumer Protection Act. Securities are not bank deposits, nor are they backed or guaranteed by PNC or any of its affiliates, and are not issued by, insured by, guaranteed by, or obligations of the FDIC, the Federal Reserve Board, or any government agency. Securities involve investment risks, including possible loss of principal.

“Hawthorn, PNC Family Wealth” is a registered service mark of The PNC Financial Services Group, Inc.

©2020 The PNC Financial Services Group, Inc. All rights reserved.