Opening the door to innovation

Vincent Kilcoyne of SmartStream explains why financial technology firms are a very easy elegant way of accessing innovation

Maddie Saghir reports

What trends are you currently seeing around technology in the financial services space?

There are a number of dimensions that are emerging. Traditionally, post financial crisis, which was very much a catalyst for a huge amount of financial technology (fintech) growth within the industry, there were thousands of investment bankers and bankers in general, who moved out of the banking arena because of the onslaught of regulation and the feeling it wasn't going to be as much fun, and there wasn't going to be as much innovation as expected.

From the banking perspective, all of the dollar spend was going on compliance and regulation. This drove the growth outside of the banks in fintech. Effectively, that has driven a lot of fintech initiatives. They have focused heavily on solving operational inefficiencies across the banking diaspora. That has driven a continuous focus on finding areas in which banks are inefficient in solving those problems.

By in large, that area has been very much focused on the customer side, the growing use of platforms, infrastructure, etc. There is an increasing realisation that the industry wants to try and standardise as much as possible, and that is making way for the growing use of utilities. The increasing cloud-based adoption within the industry, and the introspective questioning within the financial industry of when they look at any piece of spend, regulation, or compliance that they need to embark on, the first things that they will do is look at, and say: Is there a better model? Is there any internal IP associated with this? If I do this, is there any market advantage that I am engineering into? And, is there another way for me to solve this problem more cheaply, more cost effectively in a more timely fashion without adding headcount to my organisation?

There are new wedge propositions that are becoming evident as fintechs are increasingly stepping up to provide hosted services, combinations of technology, and market understanding.

So, for example, the second Markets in Financial Instruments Directive (MiFID II), there is an element of ubiquity to the nature of the problem and an increasing willingness to adopt that as an approach.

It could be from a regulatory perspective, but it could also be from an operational improvement, operational cost reduction, and so that is really where I am seeing things coming from.

At what point did technology start being considered at board level?

Technology has always been considered at board level, but its role at board level has changed, and this has been relatively recent for some organisations. If you look at many major financial institutions, some of them saw technology as being a real market edge; some saw it as being a business process support activity.

Increasingly, they are now seeing it as being a differentiator, competitive advantage, and even a defensive strategy. The perception, focus, and interpretation of technology has changed. Previously, most organisations saw it as a cost of doing business whereas now it is seen as an increasingly unacceptable cost of doing business, while some have closely aligned business and technology strategies, where you have high levels of IT literacy at board level.

IT is starting to become a real enabler and a mechanism for change. Regulation has been an enabler for this thinking because of the substantial IT element in such programs. Increasingly, the banks are seeing themselves as technology institutions as opposed to exclusively financial institutions. I hasten to add that there is a substantial difference between a fintech and bank.

I may be controversial in saying this, but a fintech takes technology and uses it to solve a financial problem. However, banks don't do fintech, banks do techfin. If they have a financial problem then they use technology to solve it. There is a different focus in the way in which they do it, there is a different cost dynamic, overhead, operational model, level of oversight, and regulation. Therefore, technology has always been a focus, but the extent and dimensionality and direction of that focus has changed. Probably more so since around 2009/2010, when the banks saw what was happening outside of themselves, from the point of view of increasing fintech growth, growing threats, digital challenges, etc, and they suddenly saw technology as an enabler and a market differentiator.

With all the new fintechs on board servicing predominately the front office, the back office is still being serviced by the more reputable organisations. Why is this the case?

When we look at the front office, I don't think we are necessarily looking at the front office from a treasury or trading perspective. There are interesting emerging technologies in that space. However, I think if we look at it from the front office of the bank and the retail of the bank, and the customer servicing perspective, there is an enormous onslaught of growth in the number of financial technology organisations, emerging banks, platforms, and channels that are servicing the customers in a better way.

This means that there is growth in blockchain because there are a number of interesting open banking initiatives, and payment initiatives. This is going to drive organisations through real time type operational activities, and increasingly the banks are becoming utilities that have a compliance overhead, but for some reason they don't necessarily own the relationship with the customer. In consequence they have a huge amount of cost with increasing margin erosion.

The fintechs have very much been focusing on that side. When you break it down to the operational parts in the back office, I think that the reason why the banks have been perhaps reticent about changing is because in order for the bank to operate viably, and to continue to be compliant they must have reliable technologies. Technologies that have the maturity to support their business, that basically keeps the bank running. You can change front of house, the windows, and the doors but ultimately when it comes to be being compliant from the regulatory perspective, from a systemic perspective, you need to know that you have got mission critical applications which are best in class and are equally poised, ready and able to respond to emerging technologies—with the ability to connect to the blockchain, connect to digital channels and to be able to automate all of the downstream processing that your front of house problems are creating. The banks from an operational perspective must operate at absolute capacity with as low failure rates as possible, because ultimately from a utility perspective they have to be able to respond and satisfy the needs of both their customers—their direct–traditional customer base–indirect customers, and then a new emerging type of customers, which is called the fintech of disemedientation. So the technologies that they have must be robust and be able to accommodate the changes that are occuring outside the traditional operating system.

Do you think collaboration with smaller fintech firms is the answer to innovation around technology in the financial services industry? And why?

From the point of view of collaborating with fintechs, absolutely. The banks have provided ample evidence. They attend all of the major start-up community events, they observe all of the core parts in many cases they have invested in fintech accelerators and fintech incubators, so engaging with them, absolutely. But, there has to be a measured level of engagement. I ran a fintech incubator for five years, and what I found was that a lot of ideas and a lot of the people that were coming had an appreciation for a problem, but had never really operated in an environment of having sold software. They didn't know how to create a value proposition. They didn't know how to validate or test it, and they were coming up with interesting ideas, many of which never actually sold. The banks have been through a number of iterations of this, we have seen them evolving from being somewhat nascent to slightly more evolved, and slightly more mature, and that means that different levels of discipline have come in. The speed of innovation has perhaps changed to be more measured, more considerate of what's happening. The investment community are not only providing money and investment, but they are also providing industry insight. There is a huge focus across the industry to look at what's happening in the fintechs, and to truly validate how viable the solutions or ideas are. Rather than just piling in and saying it looks interesting—wow. Now its a case of sit down, and mobilise a team to look at it. Within SmartStream, we have created something that's akin to fintech, we've created an emerging technologies practise, an innovation team, comprising of an entrepreneurial team of technologists and industry practitioners who test and validate the ideas and concepts. This team operate very much in a similar way to which investment banks are now engaging with fintechs. Very simply, fintechs are absolutely crucial, they are a very easy elegant way to access innovation—but not all of them succeed. Typically, the ingredients for success are the ability to look at it and test the relevance of the solution to an industry product.

What is SmartStream currently working on in the fintech space?

We set up an innovation group to look at how the core focal capabilities of SmartStream could be improved or enhanced through the use of artificial intelligence and everything that it encompasses, and also by engaging with the blockchain. We have created a team of technologists and industry practitioners. The industry practitioners have 25 to 30 years of experience individually, gained while working across 100s of banks. As you can appreciate, SmartStream has an impressive client base, that means we are testing the validity of an approach, we are not testing it from a lens of a single bank. We are testing it from the experience of hundreds of banks and buy-side institutions and some corporates, looking at that from a geographic lens, a usability in a volume perspective, a different regulatory regime, and a different market dynamic perspective. Almost as if you have taken a single initiative by any investment banker in London, and how they look at fintech, and combined the entire financial ecosystem to look at individual fintech initiatives. This is very much what we are doing, bringing that depth, and wealth of experience and variety, and mobilising it to solve very discreet problems that we can articulate to the customer base and solve problems that are completely relevant—we can understand what the value is to the organisation and to all the different organisations. This we can articulate from the point of view of the value proposition, the technology footprint, the cost of ownership, the benefit and the return of investment. That's the primary focus, how do we use AI or Blockchain technologies to drive real benefit to our customers.

What plans do SmartStream have over the next 12 months in the technology space?

That pretty much dovetails with what we are doing. We have been heavily focused on engaging with our customer base, listening to the key areas that they see from a strategic and cost prospective, and from revenue enhancement control. So we have been reviewing some elements of our technology stack in order make the necessary changes to reduce the cost of ownership. We have been looking at newer technology persistence capabilities, database layers etc, in providing our customers with broader options in terms of cost profile that they want, and to closely align with their technology strategies. So, it is very much around creating more optionality to satisfy the changing technology platforms that we are seeing globally. Being able to support their interest and their appetite for embracing new technology sets. But we have also seen as an additional support arm for our clients because we are not only developing the software and solutions, but we are actually doing it to solve problems that are relevant to them.[Q] Considering how quickly technology within financial services has excelled over the last few years, what predictions do you have for the next five years?Technology has not excelled, it has evolved at an incredible pace, however, if you were to look at the success of the fintech community, there is more likely to be an approximate 60 to 70 percent failure rate. That doesn't mean it has excelled—I think quite the opposite. We have witnessed an incredible evolution in the way technology has advanced, with a number of excellent successes, but they are very much the edge event. We've got the unicorns, the incredibly successful ones that everybody knows about but if you look at the incubation, the acceleration community there is an incredible level of failure there. What we need to look at is: why are they failing? There is a wealth of insight with various different pieces of research, insights and so on, that look into the reason for failures in fintechs. The inability to actually gain client endorsement is right at the very top. You have a situation whereby there is a wealth of fintechs with incredible products and no customers—that is not a recipe for success, but in fact a recipe for a failed investment. There is now a huge amount of caution, a lot more diligence being employed when investors look at fintechs and the initiatives to test for viability.

The venture capital community, the investment community, the acceleration community, incubation community are all typically looking at it and testing it with the broader community to see how viable it is. They are also using that to measure whether or not to make the investment. Another reason why we see fintechs failing is because they are failing to pivot, meaning they fail to move beyond the first customer.

I think the industry will continue to see a deeper set of rigour being associated with any such investment. There are a number of fintech investors who will not touch blockchain technology investments, which is just their choice. There is a lot of suspicion around what is happening around the fintech innovation, however, there is a lot more rigour being associated with it to test for relevance, ability to sign customers, and the ability to pivot, and to scale up.

Vincent Kilcoyne
Executive vice president, product management
SmartStream