Moving beyond the fintech hype

Country should buck up or run risk of foreign competition in fintech sphere

"WE need banking services but do we need the bank?" This question is often shared within the financial technology (fintech) fraternity. It is easy to see the implication. A number of fintech firms, be they established companies or start-ups serving the needs of online financial transactions, have enjoyed fame and business success of late.

Yet, it is no surprise that fintech has become such a buzzword. Author Malik Khan Kotadia says the main driver behind fintech's global thrust is the banking collapse of 2008. US-based Lehman Brothers went bankrupt, and Merrill Lynch, Royal Bank of Scotland, and AIG were among those that had to be rescued. This caused a frantic search for new avenues to manage the people's wealth. "The public no longer trusts banks and are looking for alternatives," he says.

Kotadia's views come from his experience as a mentor to many fintech start-ups and his over 18 years background in banking and digital business. Closer home, a report on fintech developments in the country by PwC Malaysia and the Asian Institute of Chartered Bankers entitled, Catching the FinTech wave showed that 82% of financial institutions (FIs) perceive it as a threat to their business, compared to 73% of Singaporean FIs or even their global counterparts (67%).

However, a battle between fintech start-ups and FIs may not materialise domestically as the former are actually working with FIs to grow the business. The fintech industry in the country has been around for a long time - possibly since the IT boom when software developers created solutions catering to financial institutions. Fintech Association of Malaysia (PAM) president David Fong says it has over 60 members, including private companies, government agencies and stakeholders that influence the development of fintech.

It is estimated that the domestic scene has about 80 fintech companies, and that Softspace, RinggitPlus, FundbyMe Malaysia and Moneymatch could be among them, though Fong says the figure could be higher.

The number of fintech companies in regional financial centres such as Singapore and Hong Kong tends to be higher owing to a larger concentration of FIs in those markets that have a higher number of financial activities.

Fong is also a senior director of GHL Systems Bhd. The business revolves around offline and online payment services. PwC, Malaysia financial services leader and assurance partner Ong Ching Chuan says there are two types of fintech companies - those that complement the businesses of financial institutions, and those that compete with them.

"Fintechs are most likely already working with financial institutions, while the latter prefer to work on their own. I believe this second group of fintech start-ups can survive without integration with financial institutions. However, it would be challenging given their limited resources and funds," he says.

Going at it solo

Peer-to-peer (P2P) lending is one avenue of fintech that not only does away with FIs but competes directly with bank services. P2P platforms match borrowers to lenders and include Ethis Kapital and Modalku Ventures, which have Securities Commission licences to operate.

They allow SMEs to tap into alternative forms of financing, such as equity crowdfunding.

In November, ice cream start-up Fruit King announced it had raised RM5 mil through CrowdPlus.asia. Their (P2P platforms) solo endeavours, which follow a consumer-to-consumer approach, open the possibility of fintech start-ups eventually eating into banks' profits and market share.

"What we have is a regulatory framework so strict that no one wants to invest in the space. We need to see a change. In the last three years, we have seen a huge investment in fintech in Southeast Asia and Europe. We need the right framework and incentives," Fong says.

Investing in successful financial technology (fintech) start-ups can be a hit-and-miss affair. So what do private equity investment firms like Tryb Asia look for when doing so?

Managing partner and co-founder Markus Grirck says Tryb generally invests in infrastructure technologies and platforms which are changing financial services in ASEAN.

"Our approach is to explore the technology that supports the back-end operations of financial institutions. "The segments we like are trade finance, security, payment processing, capital markets, insurance, compliance and wealth management," he tells FocusMag.

Grirck says these areas mostly involve growth stage technology ventures who have established themselves as niche market leaders and are looking for further expansion.

They also invest in early stage companies, but are far more selective and concentrate on deep technology start-ups exploring big data, the blockchain, and artificial intelligence, among others.

"Digital payments are the most prominent sector in fintech, and likely to propel further since the e-commerce industry has yet to mature. "The distinct insurance gap in the country is presenting a huge opportunity for innovation, especially with the government's push for rapid inclusion," says Grirck on growth opportunities.

Regionally, each market has its own growth areas as well. In Singapore, payments and wealth management are the most prominent sectors. It is also projected that cyber security and data analytics will do well in that market.

Indonesia presents a wider opportunity owing to a largely unbanked consumer population but lack of regulatory clarity is impeding its fintech growth.

Blockchain technology set to challenge financial institutions

THE development of the fintech industry has given rise to a new term known as blockchain technology. As a potentially disruptive force, blockchain is essentially a decentralised ledger of all transactions across a peer-to-peer network.

What this means is that machine-to-machine payment via online currencies is possible, hence replacing the third party intermediary usually the financial institution.

Tryb Asia managing partner and co-founder Marcus Grirck believes the grand vision of a blockchain economy can be realised only upon participation by all stakeholders.

"Government bodies are integral stakeholders. They will play a huge role to effect the adoption of the blockchain, set up proper regulatory systems to govern processes and manage counterparty risks. Consumer education and acceptance is yet another substantive barrier," he says.

That said, a fair amount of resistance from financial institutions is to be expected, as blockchain could eat into their market share as it removes conventional financial institutions from the transaction.

Fintech start-ups that are exploring the technology can be seen in the area of remittance applications.

Fintech Association of Malaysia president David Fong says the take-up of blockchain technology is still fairly low in the country.

However, its potential extends beyond online payments and remittance. It is believed that Bank Negara Malaysia is open to the idea of blockchain technology and interested parties are already exploring the possibilities of commercialising it.

Meanwhile, the Philippines central bank will leverage on blockchain technology to develop the E-peso, a virtual currency based on the Philippines stock exchange, building a nationwide electronic payments system.

"ASEAN possesses huge potential for blockchain technology to be applied to remittance and international trade, more so than the other global regions," says Grirck.

As the financial infrastructure is underdeveloped in some countries such as Myanmar, opportunities are available for blockchain technology to be adopted in a timely fashion as the country develops its infrastructure," says Grirck.
Boosting the herbal industry by creating jobs

From previous page different risks, and hence it is important to bear in mind that the same products cannot be sold in different markets. This is due to differing consumer behaviours and tastes.

"For example, Cordyceps will not (sell) in China as it’s too common. Collegen products do well in Malaysia, but will be too competitive in China, so we won’t export or focus on such products there. Different markets require different strategies and products," says Hon.

In tapping the Chinese and Indonesian markets, he explains that product registration is a key obstacle, and that is why Bioalpha has fewer than 10 products under its Alpha Health brand as of Sept 30.

He says the company faces a similar challenge when introducing new products to China. The strategy, he adds, is to start distribution of halal functional foods for northern China by working with local Muslim councils in Xian, Xinjiang, Winggal and Lanzhou as it is difficult to get products registered in the health supplement category.

Bioalpha, however, took a different approach in Indonesia by setting up a processing plant in Blau, Kampar.

"One of the most challenging aspects is to get our products registered. It can take up to two years to introduce one imported product due to lengthy product registration and approval procedures.

"We realised we can do better in Indonesia if we can push more products, so we decided in May to set up a new processing plant there, which can help reduce the time taken to two months," he says.

Its Indonesian plant has two production lines for sachet and teabag packaging. Its local partner PT Herbal Mulindo Makmur manufactures the health supplement products, and Bioalpha handles sales and marketing.

Besides the Blau plant, Bioalpha also has processing plants in Bangi, Selangor; Pasir Raja, Terengganu and Desaru, Johor.

Hon says Bioalpha ventured into cultivate and farming of herbal plants to ensure continuous and sustainable supply of herbs for its manufacturing activities.

"Previously, for example, we purchased Roselle herbs from farmers at RM5 per kg. Then the price went up to RM50, which meant we had no access or control over raw materials. Moreover, we wanted to regulate quality and consistency of the herbs, so we secured the Desaru land:"

Growing on solid ground

The Desaru plant, which is a primary processing plant, covers 120ha leased from the state, of which 80ha is fully planted.

The Pasir Raja plant, covering 401.6ha leased from the government, is also used for primary processing of herbs and raw materials. Under phase one, 49.2ha is fully planted, and the company plans to start land-leveling and planting in the rest of the land by the end of next year.

About RM10 million will be required to undertake phase two, and Hon says the target is to have full farming in the next two to three years.

"We have built primary and secondary manufacturing plants there. A primary plant comes with farming and manufacturing, as well as washing, drying and packing of harvested herbs. The secondary plant is for extraction to bring out the value of the herbs in extract form.

"We anticipate 50 metric tonnes of herbs from phase one and 350 metric tonnes for phase two," he says.

Bioalpha was appointed by the East Coast Economic Region Development Council in 2014 as an anchor company to invest, develop and manage the land to boost the herbal industry by creating jobs.

We have recruited more than 40 local farmers and entrepreneurs to fully pull the key performance indicator of giving opportunities to increase income," says Hon.

This gives Bioalpha additional supply of quality herbal plants for its manufacturing processes, making it one of the biggest herbal farming companies.

Various ways to deal with fintech companies

From page 28 the sandbox stage, such as those which do not operate in the existing banking framework," says Fong.

Based on the AICB PwC FinTech Survey, 59% of FIs say they are dealing with fintech companies in various ways.

This includes engaging in joint partnerships, acquiring fintech companies, setting up venture funds or start-up programmes, launching their own fintech subsidiaries or rebranding purchased services.

"The form of collaboration that will work best for financial institutions would depend on the level of digital disruption the financial institutions choose to focus on.

"Digital disruption can be from relatively slow impacts changes from third party aggregators such as CompareHero, an online financial comparison site.

"It can also involve more fundamental changes in business model and core systems such as P2P lending and blockchain technology (see Blockchain technology set to challenge financial institutions, on page 20)," says PwC’s Ong.

He says start-ups which collaborate with FIs tend to have an upper hand as they have the ability to scale up rapidly and leverage on FIs’ large customer base.

They also have access to customer data to help with rapid prototyping of new applications.

"The processes that financial institutions have are naturally complex. They can also be lengthy due to risk and quality checks, governance, and integration with existing systems.

"Technology adoption must be done in a timely fashion, otherwise there is the risk of becoming irrelevant. Hence financial institutions must meet fintechs halfway in this regard," he says.

The threat of regional solutions encroaching onto our shores is real. Ong cautions that the country should buck up or run the risk of foreign competitors such as China’s Alipay or WeChat Pay bringing their proven fintech offerings to the country.

Ong says foreign competitors may introduce their fintech solutions domestically if Malaysian companies don’t buck up.