xignite

White Paper

The Now, The Cloud and the Crowd: What is Shaking Wall Street to Its Core?

There is a fintech revolution going down and it is not happening quietly. JP Morgan's own colorfully outspoken Jamie Dimon said recently that "Silicon Valley was coming" and intending to eat Wall Street's lunch. He did not make it up since inventor-of-the-web-and-great-financier-of-the-unicorns Marc Andreessen himself claimed late last year talking about the bloated financial industry that he and his army of exit-starved entrepreneurs could "re-invent the entire thing." Indeed, while ICE may choose to turn the floor of the NYSE into a night-club and seal the deal on Wall Street becoming nothing but a residential neighborhood, the cool bearded twenty-somethings haunting the digs of startups like Betterment in Chelsea, Motif Investing in the Silicon Valley, Derivitec in London's Level39, eToro in Tel-Aviv, or 8 Securities in Singapore are working 100+ hour weeks to revolutionize financial services.

Never before in the history of the respective eastern and western centers of finance and technology has the war been so drawn out and heated; and Silicon Valley may be winning. The number of defections from Wall Street to fintech startups is reaching an all-time high while the amount of capital raised by these new ventures around the globe is reaching gargantuan proportions. It is now almost impossible to find a venture investor who is not "specialized in fintech" (while no-one would dare touch the sector back in the fall of 2008). Move over, social, SaaS and messaging; fintech is now king of the mountain.

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While the ambiance might be a bit on the frothy side, there is a reason to the madness. A new body of technology has become mature enough to challenge the assumptions on which Wall Street has been built for the last 100+ years and is shaking it to its core. While Wall Street was busy dealing with the aftermath of the mortgage crisis, an evolution has occurred and the people have changed while the industry has not. To be fair, maybe we should blame the governments around the globe for stifling Wall Street's potential. The industry has been burdened with regulation upon regulation, creating a very expensive distraction and leaving no time or resources to innovate. The industry has now exposed its flanks to the armies of razor-sharp private-equity-fed startups that are unbundling its businesses into pieces and throwing billions of dollars of enthusiasm and technology at each sliver of opportunity—a death by a thousand cuts.

FINSERV IS RIPE FOR API DISRUPTION

- Cost Structures are too high
- Adoption of Cloud is still restrained
- Capacity of innovation is too limited
- Regulation is too large a burden
- Meanwhile, newcomers are re-inventing the game by leveraging APIs

At the core, what are the main themes that are enabling this revolution? The Now, the Cloud, and the Crowd. Taken together, these three themes illustrate how fintech startups are taking on Wall Street at its most vulnerable spots: The slow pace of its transactions, the convoluted legacy infrastructures that keep Wall Street on the ground and out of the cloud, and its continued dependence on closed hierarchies that shut out the wisdom of the crowd.

The fintech stars of the moment are striking hard and fast at one or all of these pressure points, and the evidence suggests that are giving the people exactly what they want.

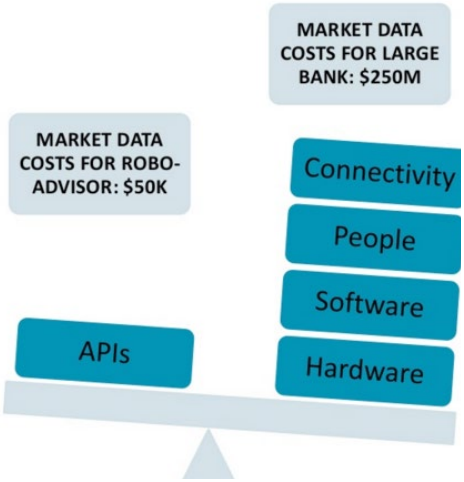
Finance is often the last sector of the economy to embrace new technologies, preferring to shield itself from tech booms that may lead to ruin. This caution hasn't served Wall Street well in the past decade, however, because the industry has lost touch with the changing demands of the next generation of consumers, savers and borrowers. Much of that disconnect can be attributed to the increasing emphasis on regulation, but regardless of the cause, Wall Street fell asleep at the wheel while young entrepreneurs figured out how to reinvent finance for the era of the Now, the Cloud and the Crowd.

> "The next generation of financial service companies are being built on APIs and the cloud, and they will benefit from a massively smaller cost structure than their legacy competitors—which in the end, will seal their success."
>
> —Stephane Dubois
> CEO and Founder
> Xignite

The Now

Most of Wall Street services and processes were engineered back when people had time and patience. That is so 1999. The Millennials are a generation defined by instant gratification. (We can thank Steve Jobs and weak parenting for that). Click. Done. Wall Street as an industry is still emerging from the seventies. Understand for instance it still takes three full days for a trade to settle in the US. There are so much legacy infrastructure and processes, layers upon layers of interconnected systems technology and software, much more manual intervention than you would dare to imagine, encumbered by massive regulatory constraints. Wall Street cannot do anything quickly and this has created a huge impedance mismatch with a millennial generation that does not give a damn about mahogany-lined conference rooms and certainly doesn't want to talk to anyone about their investments. If Millennials want to open an account, they want to do it now! If they want to trade, they want to trade now. Don't ask them to sign and fax a piece of paper to open their account because you lost them at paper.

The need for the Now is hitting all facets of the industry: money transfers, banking, lending. But nowhere is it more disruptive than in the area of wealth management. Financial advice used to be about personal relationships. Many believed this would never change. But today Robo-Advisors are threatening the industry. Now that software has been eating the world for a few years, you can delegate advice to a machine. Companies like Wealthfront, FutureAdvisor, Betterment and SigFig have all built-in—to a degree or another—instant gratification around their services. And customers are gobbling it up. Personal Capital just released its app on the Apple Watch this week. Wealth Management is now unified with the one device that is the embodiment of the Now.

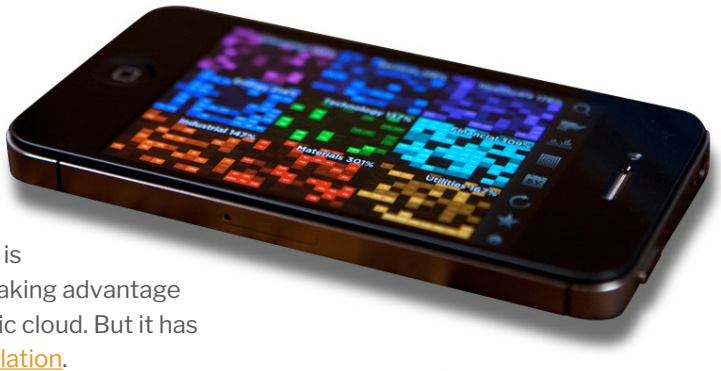


Sure, the fact that Millennials have yet to experience a market downturn suggests that they will come crying to their human advisors at the next correction. But I doubt it. I predict that the so-called "robo-advisor" platforms will manage 15% to 25% of retail investable assets within 5 years.

The Cloud

Xignite has been beating the Cloud drum for years now. Amazon Web Services is now a $5B, business growing 50% a year. But why is this more relevant than ever to Wall Street?

The industry should have figured out how to take advantage of the public Cloud to eliminate the billions and billions of dollars it needs to shave from its cost structure. Instead, everyone builds the same technology infrastructure, deploys the same software, operates the same data centers, builds up the same layers



Stocktouch app on an iPhone

upon layers of brick-and-mortar technology to operate an industry that is essentially virtual. Spare a few ATMs here and there, and you realize that from banking, to lending, to wealth management, to capital markets, the financial services industry is essentially perfectly suited for the ether, ideally positioned for taking advantage of the mutualized technology infrastructure offered by the public cloud. But it has wanted none of it. Why? The usual demons of security and regulation.

But startups don't have that problem, unburdened by regulation, fueled by organic kale, yoga lessons while-you-work, and free lunches, they have embraced the cloud. Xignite deals with fintech startups every day and has hundreds of them as clients. They all pretty much run on Amazon Web Services. The public cloud, and Amazon Web Services in particular, is the operating system of the future. A global processing infrastructure on a stick. Wall Street is fooling itself if it thinks it can beat Amazon at this game. The dice have been thrown.

The next generation of financial service companies—those who will be giving Jamie Dimon a run for his money—are being built on APIs and the cloud (itself a big API). They will benefit from a massively smaller cost structure than their legacy competitors—which in the end, will seal their success. It's not only financial services firms that are being re-invented on the cloud, it is all their network of retail and institutional service providers. When your arms dealers are switching to the next generation technology, it's time to renew your arsenal.

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Nowhere is this problem more visible than in the sector served by Xignite. The market data industry is a $26B market where most of the money is spent on proprietary technology inherited from the 80's and 90's where redundant infrastructure spending is pervasive. Every single financial institution spends billions of dollars on the same technology as its competitors but draws very little competitive or service advantage. The public cloud and its lower cost structure is a lifeline that Wall Street must grab now.

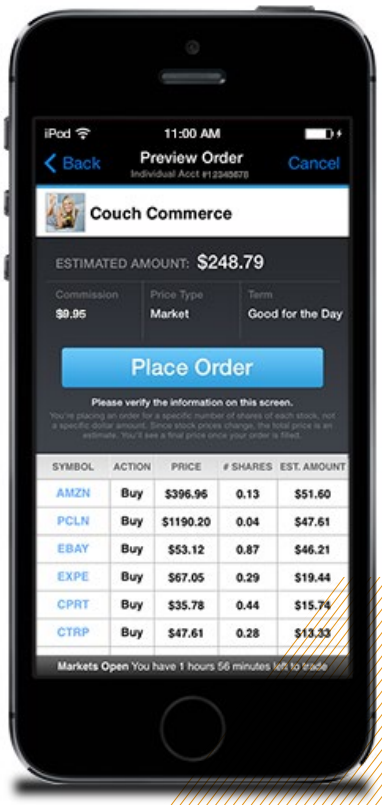
The Crowd

Finally the biggest premise underneath Wall Street is also being challenged; that it is has to be a set of gigantic highly leveraged, highly centralized, too-big-to-fail, century-old institutions to even work. New technologies have simply shattered that assumption with the unbundling of the bank as obviously the first step. Who needs a large bank providing a set of mildly integrated, average-quality services across the board when a crowd of new technology companies are able to provide a set of best of breed services all running in concert on the same device? Or when companies like Yodlee are able to provide those startups with an integrated view of the customer's assets via easy APIs no matter where those assets are held. There is not a single sliver of service or technology infrastructure provided or used by large financial institutions today that is not under attack by dozens of startups worldwide. Take for instance Tradier who can provide you with a complete set of brokerage APIs to build your business upon. Ten years ago, doing this would have taken months and cost millions, whereas now, a brokerage business can be built overnight. Sure, not all startups survive but many will and have already changed the industry forever.

> "We were enabled by 3 technologies, ETFs, trading APIs and market data APIs."
>
> —Andy Rachleff
> Chairman and Founder
> Wealthfront

This not only applies to consumer-facing services like money transfers or savings accounts, it also applies to some core internal supply chains of the capital industry where the power of the Crowd is successfully applied to create alternative sources to Wall Street traditional fare. Estimize for instance, is applying the wisdom of the crowd to the earnings estimates and being very successful doing so—challenging big vendors like Thomson Reuters on a turf that is literally the beating drum of the markets. Vetr is also drawing upon the Crowd to rank stocks in a fashion similar to the way Morningstar built its famous star rating for mutual funds. Examples abound in more obvious categories such as crowdfunding with companies like KickStarter, Crowdnetic, Funding Circle, Lending Club and dozens of others worldwide.

There used to be a distinction between Wall Street and Main Street and at times their interest have not aligned. One of the biggest strengths of Capitalism is its ability to self-improve. Today, Main Street and Wall Street are merging and they are leveraging new technologies to give the next generation what they really want: everything, right now, and for less.



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