BankThink Smaller institutions should embrace, not oppose, fintechs

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Recently, community bank and credit union groups have initiated efforts to use their lobbying influence in Washington to restrict the growth and aspirations of innovative fintech firms. Their arguments, however, amount to the old regulatory catch-22.

On the one hand, they claim that fintech firms are currently getting a lighter touch from regulators. This is just not true — the consumer protection laws and regulation that apply to bank or credit union loans also govern fintech loans.

But at the same time, these groups staunchly oppose any forward-looking changes — such as the de novo charter applications by fintech firms to join their ranks as directly-supervised, deposit-taking banks. Today's incumbents know they enjoy some major advantages: guaranteed deposit funding from the Federal Deposit Insurance Corp. that lowers their cost of capital, Federal Reserve payment system access and discount window borrowing. These are the good parts about being a bank that they'd prefer to keep to themselves.

Yet while some groups might be looking to lobby against fintech competition, their actual member banks and credit unions are increasingly looking to partner with fintech lenders to better serve the needs of actual customers. Even in a good economy, millions of Americans remain stretched financially. Roughly 20% of working Americans aren't saving anything at all. Approximately seven million auto loans are now more than 90 days delinquent. Approximately 40% of American adults say they can't cover a $400 expense. There is now $1.6 trillion in outstanding U.S. student loan debt and $1.1 trillion in outstanding credit card debt. These new huge challenges require new thinking from innovators and traditional institutions alike, not a backward-looking lobbying campaign.

Whether they are looking for credit options or for education to improve their financial health, Americans are going online. TransUnion and Experian data from this year shows fintech lenders now account for 40% of the unsecured personal loan market. This is a well-regulated and fast growing credit option for millions of Americans across the income spectrum, and an established asset class with investor liquidity. Fintech lenders are also serving small businesses with loans that were simply not economical for banks and credit unions to offer through physical branch locations. Student loan refinancing is an asset class that banks had basically abandoned before fintech lenders started helping recent grads find better interest rates and lower monthly payments.

A little more than decade ago, most credit applications were filled out in person at a branch, or printed out and sent via a fax. Today, approximately 50% of all applications for credit are now filled out online, and in the coming years, that number is likely to grow to over 90%. That's why, in standard bank audits, banks both large and small are being told by federal regulators such as the Office of the Comptroller of the Currency that they need to have a digital strategy for customer acquisition, service and retention. Without a viable digital strategy, regulators know that the consumers and businesses in the banks' local markets are at risk of being underserved and left behind.

The irony of these lobbying campaigns is that while the biggest banks in the United States might have credit card offerings that fintech loans compete with, regional and community banks have the most to gain by partnering with and supporting the development of fintech lenders.

These partnerships can take a variety of forms. Banks can be an origination partner for fintech firms, a "white label" partner (where fintech lenders build the capacity of banks to offer their customers a digital experience) or a funding partner, purchasing loans or securities backed by loans. Today a significant percentage of the fintech loans wind up on the balance sheets of regional banks, community banks and credit unions, who often select loans made to prime and super-prime borrowers. With the costs of core deposits rising, these critical community institutions need these yielding assets, and they need to diversify assets beyond commercial real estate and the exhausted indirect auto loan market. Fintech lenders can also help banks and credit unions fulfill their obligations to find and serve customers who live in a certain geographic footprint, or in low- and moderate-income areas within their branch network under the Community Reinvestment Act.

All Americans deserve access to responsible, transparent, simple and fairly-priced credit options that can help them navigate and take some control of their financial health. Increasingly, bank and credit union customers are searching with their browsers, not walking into bank branches. Many small banks are closing branches. Fintech lenders are natural partners to banks and credit unions who need to navigate this new reality and serve their communities. Through partnerships and a more forward-looking approach to public policy, America's banking system, and our financial health, are more likely flourish.

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