Blockchain 2015: Strategic Analysis in Financial Services

by William Mougayar

General Partner
Virtual Capital Ventures

December 22 2015

It All Started with the Internet…

1994 was a Bad Year for Banking

- It signaled the end of IT, and the beginning of the Internet era
- Technology became a slippery slope since then
- For 10 years, financial institutions didn't innovate much with the Internet
- It could be argued that FinTech was a response to that lack of innovation during the early Internet years

  [At the end of 1999, only 20% of US national banks were offering Internet banking, although it represented 90% of banking system]

In the mid-2000's FinTech Attacked the Banks,

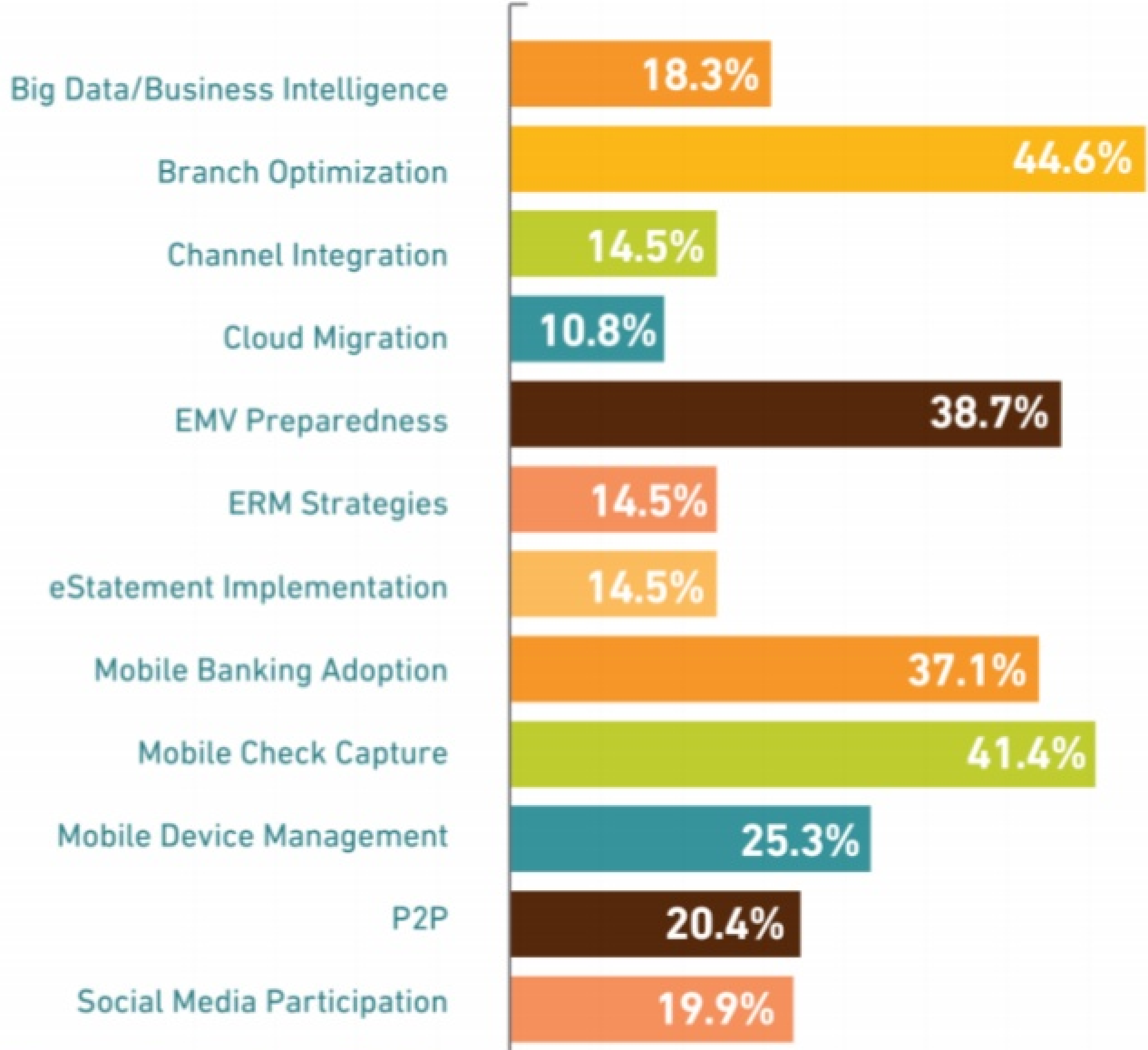
and it was called "Unbundling Banking"

- In startup fashion, most attacks aren't head-on, start small & look harmless at first sights, therefore are ignored
- So, the banks didn't feel FinTech initially, because it crept up

Graphs Source: CB Insights

In 2014, Banks Didn't Plan for the Blockchain

Which of the following areas will be a strategic focus in 2015? Choose three:



Source: https://www.fmsinc.org/documents/CSI_BankingPrioritiesSurvey2015.pdf

Actually, they had plans to continue being focused on other priorities:

Source: Deloitte 2015 Banking Outlook
http://www2.deloitte.com/global/en/pages/financial-services/articles/2015-banking-outlook.html

Then, the Blockchain Happened…

…and Suddenly, it's Becoming the New Internet

But there is Good News: Two Outcomes for Banks

① Some blockchain companies will attack your business, although peripherally at first

② Some blockchain technologies/companies are for you, to strengthen or defend your positions

➔ *Blockchain is helpful, doesn't signal the end of banks, but innovation must permeate faster than Internet did in 1995-2000. Early years are formative. Banks shouldn't just see blockchain as cost savings. It's also about new opportunities.*

What is the Blockchain?

Defining Technology Eras

IT Supremacy

- Data computation
- Database applications
- Transaction processing
- Business Intelligence
- Global operations

1994

Internet Years

- Personal Communications
- Self Publishing
- E-Commerce
- Social Interactions

2015

Blockchain Promise

Decentralization of Trust

Enabling

Value Flow without Intermediaries

Taking an ATOMIC DDDive in Explaining the Blockchain

1. PROGRAMMABLE

ASSETS

TRUST

OWNERSHIP

MONEY

IDENTITY

CONTRACTS

2. BASED ON:

3D's

Decentralization

Disintermediation

Distributed Ledgers

3. AFFECTING:

Governance

Value Creation

"Exchanging Assets Without Central Intermediaries"

Everything about the blockchain touches the core of banking.
This is why it will be a challenging encounter.

Consumers Ask Why?

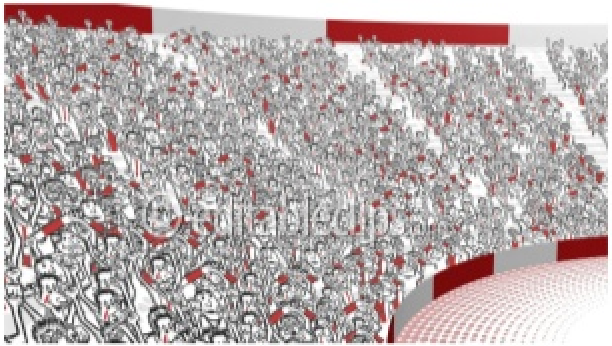
When it comes to covering their risk, banks and credit card companies will give consumers instantaneous answers/settlements (like for purchase authorizations or withdrawing money from an account); but when it comes to our own transactions (e.g. depositing a check or transferring money), we typically have to wait days before receiving confirmations.

➔ *Can the blockchain help?*

The Startup Dilemma

Banks and FinTech Startups: A Strange Relationship

Banks see startups like this strange beast that needs to be examined



Investing in startup ecosystems and accelerators gives them a spectator seat, not a participating one

By staying “close” to them, they think they will benefit from symbiosis, but they are degrees removed from them in reality, because they are only visiting the animals in the zoo

The Reality is You Need to Take the Animal Home …

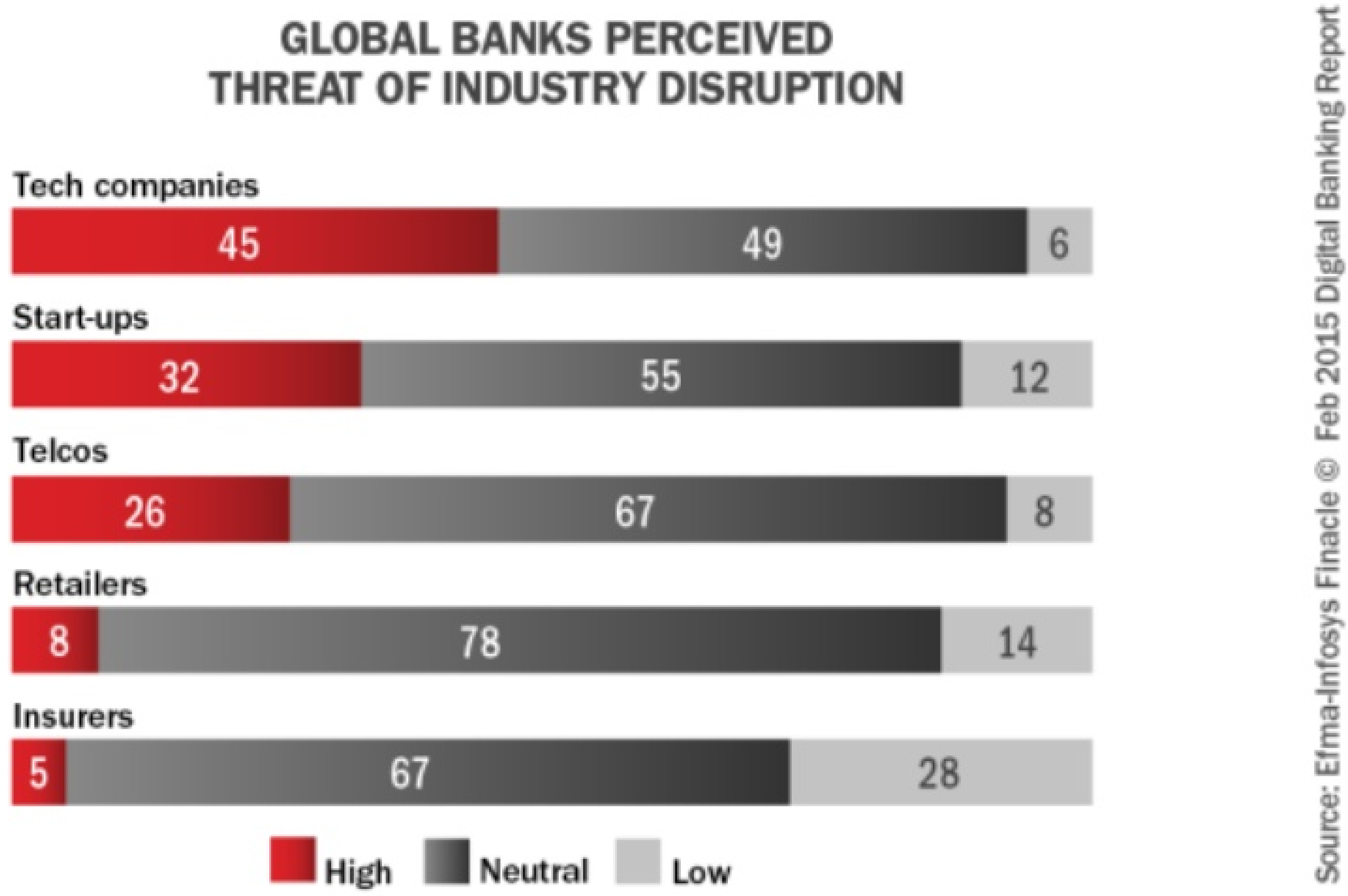
… to see if they will survive

"OK, this domestication thing has gone too far!"

"You'll experience denial, anger, bargaining, depression, acceptance, and finally, stuffing."

This is a common dilemma for large corporations when faced with external innovations that surpass their internal abilities to absorb or usurp

Because the Perceived "Tech" Threats Are Real



Themes that Emerged in 2015

Blockchain vs. Establish Methods/Networks

Blockchain and old constructs, such as clearing houses and private exchange networks (SWIFT, CCP, FIX, DTCC) are like oil and water: they will not mix well because one is based on centrally trusted intermediaries, and the other is based on “no” intermediaries and peer-to-peer trust.

➔ *Warning: Retrofitting the blockchain will be challenging, and may not yield significant benefits.*

Having the Blockchain without Bitcoin

- Banks rejected Bitcoin as a knee-jerk reaction, rooted by regulatory compliance requirements, and loss of control fears; both valid concerns in the short term.
- But Bitcoin is a rich blockchain laboratory. Bypassing it would result in a steeper. learning curve for adopting the blockchain

➔ *Reality Check: Blockchain without Bitcoin is a valid construct*

Doing Proof of Concepts (POC's)

- POCs are timid experiments that don't show commitments.
- POCs won't always allow you to see the potential benefits.
- It's better to implement smaller projects end-to-end, where you can see results.
- But POC's can be used to narrow down the portfolio of committed projects.