The Asian Fintech Revolution

By Igor Tulchinsky and Richard Hu

Financial technology is transforming Asia’s economy and capital markets, and preparing the region to be a dominant force in the coming decades.
The finTech revolution has reached critical mass in Asia. India has seen the total value of digital wallet transactions skyrocket from $180 million in 2012–2013 to $7.5 billion in 2015–2016, and the monthly number of transactions increase more than 400 percent in just the past year. In China, online payments now account for 38 percent of all settlements, led by Ant Financial Services Group’s Alipay and Tencent’s Tenpay. Fintech also is remaking Singapore, home to 200 banks with assets of more than $2 trillion: Global financial institutions like Citigroup, DBS Bank, Mastercard, OCBC Bank and Wells Fargo & Co. are launching (or already have launched) innovation labs and accelerators in the island city-state.

In the coming decades, financial technology will play a central role in Asia’s economic growth. We have started to see a surge in venture capital (VC) funding in the region’s fintech space, and that is just the beginning. The rise in automation, the emergence of new payment tools, growth in the number of financial services providers and the creation of terabytes of consumer data are opening huge opportunities for entrepreneurs and the venture capitalists that fund them. Banking will be affected as robust automated systems replace traditional manual systems to cater to Asia’s vast population. Credit will be redefined, with fast access to credit for all; the asset management and insurance industries also will witness a radical change. Over the next 20 years, we believe Asia will overtake the U.S. and Europe as home to the world’s largest financial markets.

At WorldQuant, LLC, we have witnessed Asia’s fintech revolution firsthand. WorldQuant opened a research office in Beijing ten years ago. Today, WorldQuant has offices all over the region — in China, India, Singapore, South Korea, Taiwan, Thailand and Vietnam — which are home to more than half of WorldQuant’s 600-plus employees, as well as an affiliated office in Hong Kong. WorldQuant’s research offices in Asia have been critical to its success as a quantitative asset management firm, creating millions of alphas — algorithms or mathematical models that, in combination with historical data, seek to predict future movements of securities and various financial instruments — which its portfolio managers then use to construct their investment strategies.

**Formula for Prosperity**

The importance of financial technology — and the recent excitement surrounding it — were anticipated more than 45 years ago by Michael Milken when he created his prosperity formula. According to Milken, financial technology acts as a multiplier on the total value of human capital (HC), social capital (SC) and real assets (RA) in the equation that governs prosperity:

\[ \text{Prosperity} = FT (HC + SC + RA) \]

In the 1970s and ‘80s, when Milken was running the high-yield-debt business at investment bank Drexel Burnham Lambert, financial technology was used to create things like collateralized loan and bond obligations. Today, what has become known as fintech is largely focused on digital technologies, many of which would not have been possible without the enormous growth of the Internet and the ubiquity of smartphones and other mobile devices.

Digitalization is transforming Asia’s banking industry, allowing people to open new accounts in just minutes — a process that in the past could take as long as two weeks in some countries. Investing in fintech has provided Asian banks with a cost-effective way to connect to new customers and gain market share in locations where the physical distribution of banking services is limited, helping to reduce the world’s unbanked population by 20 percent, from 2.5 billion to 2 billion, between 2011 and 2016. (India saw its bank account penetration increase from 35 percent to nearly 60 percent during that period.) Still, with more than half of the world’s unbanked population residing in Asia, there’s a huge opportunity for fintech to deepen financial inclusion in the developing world, opening the door to greater access to financial services. This should act as a lever for further economic growth.

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Fintech has the potential to reshape Asia’s credit ecosystem. In contrast to the U.S., where firms began tracking consumer creditworthiness more than a century ago, credit bureaus are relatively new to Asia, even in highly developed regions. Hong Kong’s only consumer credit agency has been operating since 1982; Singapore’s credit bureau was formed in 2002. As a result of the lack of transactional data, credit ratings often are imperfect in Asia and access to credit is highly restricted. Nonetheless, the region offers the largest testing ground to understand how supplemental information like social media, e-commerce and other mobile and Internet data — representing about one zettabyte (909 million terabytes) per year, and growing — can be used to predict creditworthiness.

**Path to Adoption**

We’re at an inflection point in Asia, with start-ups and nonbanking financial institutions taking the lead in providing credit in various areas, including online purchases, loans to small- and medium-size enterprises, and peer-to-peer lending. China already is the largest P2P lender in the world, with outstanding loans of $66 billion — less than 10 percent of the country’s overall loan market. India, Indonesia and Singapore are getting into P2P lending at a rapid pace, attracting huge investments from VC firms. These new financial services companies are fast, agile and easily accessible. It wouldn’t be surprising if by 2037 these alternative lending sources hold a major share of the credit market in Asia, displacing conventional banks.

Though traditionally it has embraced technology at a slower pace than the U.S. and Europe, Asia is on the path to becoming the leader in fintech adoption. China and India topped global consulting firm EY’s 2017 FinTech Adoption Index, with rates of 69 percent and 52 percent, respectively, compared with an average adoption rate of 32.8 percent for the 20 countries surveyed.

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Asia’s performance has been powered by 15 percent year-over-year growth in Internet users; more than 1.5 billion people in the region use social media on a daily basis (95 percent of them via mobile devices). Asia’s fintech adoption is partly driven by financial innovation by tech players in adjacent sectors (think Alibaba Group Holding, parent of Ant Financial), a flexible working environment and easy access to capital. Asian governments are putting a huge emphasis on entrepreneurship through initiatives like Startup India, South Korea’s TIPS (Accelerator Investment-Driven Tech Incubator Program for Startup) and the Chinese government’s launch of a $6.5 billion fund for start-ups. Last year, venture capital firms invested $22 billion in Asia, with $8.4 billion earmarked for fintech. Although North America remains the VC capital of the world, accounting for two thirds of all funding, we expect venture capital flows to Asia to dominate the market over the next 20 years.

The fintech revolution is powering an evolution in Asia’s capital markets and the asset management industry. The region is already home to four of the world’s ten largest equity exchanges, and we expect it to overtake the U.S. and Europe to become the world’s largest capital market by 2037. A particularly powerful driver for the current and future volume within equity markets will be algorithmic trading, which is fueled by vast amounts of data, and improvements in artificial intelligence will eventually lead to the commonplace use of robo-advisers. With the aid of machine learning, companies in Asia will be able to use Big Data to better understand their customers and offer hundreds of highly tailored products, seamlessly integrated into smartphones. These new players will shape the wealth management industry of the future.

In China, Ant Financial’s money market fund, Yu’e Bao, already has more than 150 million investors and Lufax has thousands of funds on its online financial marketplace.
Asia’s economic future is not without risks. The region has many sources of potential geopolitical conflict, including disputes over the South China Sea, the fractious India-Pakistan relationship and North Korea’s nuclear ambitions. Asia also must contend with the risks inherent in climate change and the challenge of feeding its ever-increasing population. Still, demographics are likely to play to Asia’s advantage. The median age is 26 in India, 30 in Singapore and 35 in China, much below the European Union (41), Canada (43), the U.S. (45) and Germany (47).

Fintech should reap the benefit. According to EY, nearly half of all 25- to 34-year-olds use fintech — the highest adoption rate among the age groups the firm surveyed. (The 35-44 segment was next highest, with a 41 percent adoption rate.) This is creating a fast-growing cohort of healthier, wealthier, more active and more mobile Asian adults — that is, highly tech-savvy human capital. The Organization for Economic Cooperation and Development forecasts that two thirds of the world’s middle-class population will be based in Asia by 2030. That’s roughly 3.2 billion people who will have a major say in the global economy.

So what can we look forward to in 2037? The fintech revolution will lead to the creation of technology-first companies that will replace many traditional brick-and-mortar financial institutions. As Asia’s capital markets become increasingly dominant, some of the new enterprises will be among the largest companies on the planet. Although Asia currently represents only 30 percent of global GDP, we expect it to account for more than 60 percent by 2037, powered by the huge growth in financial technology and backed by the world’s fastest-growing middle class. Western institutions and investors that want to remain relevant would be wise to look to the East!

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