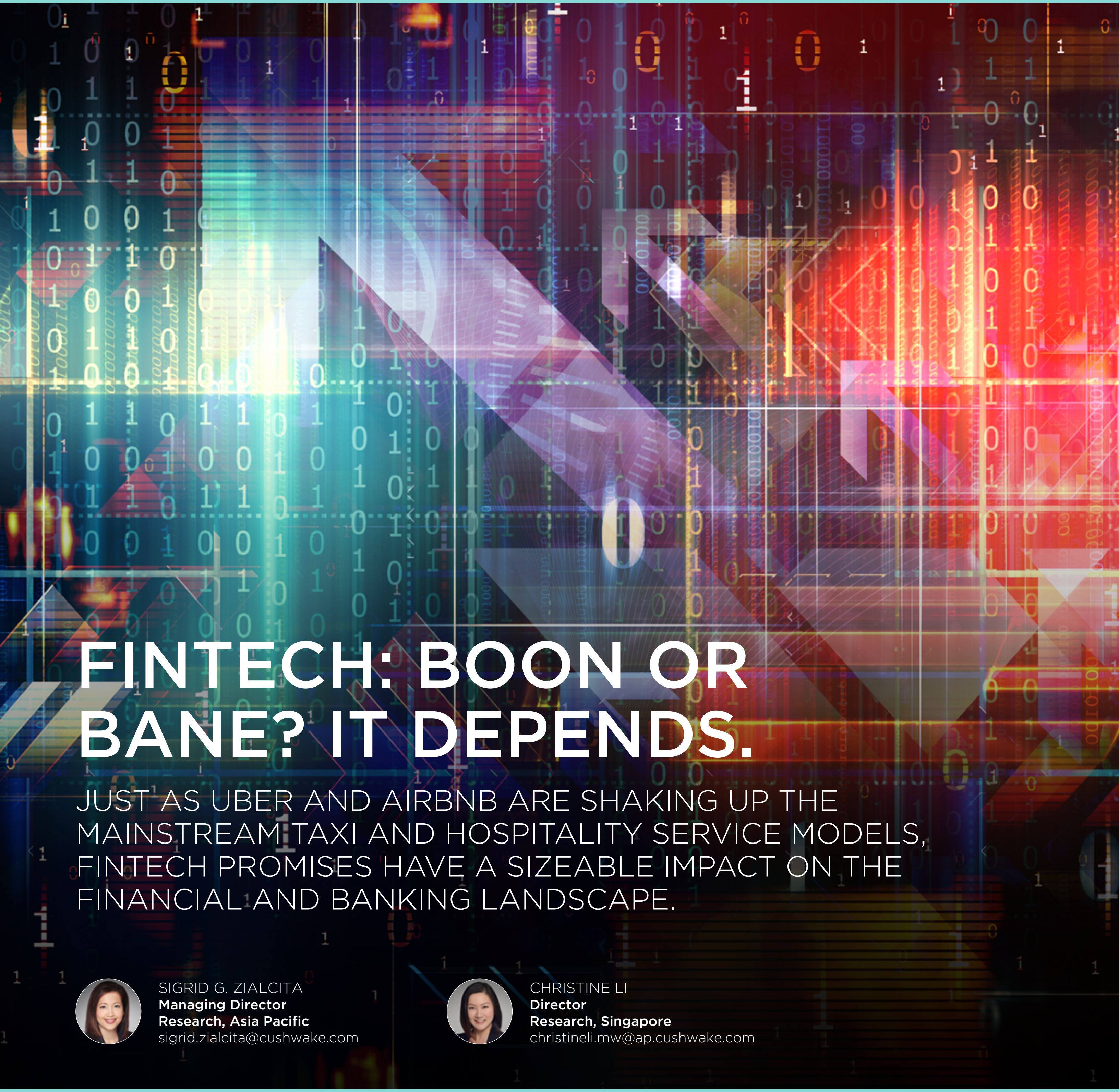

FINTECH: BOON OR BANE? IT DEPENDS.

JUST AS UBER AND AIRBNB ARE SHAKING UP THE MAINSTREAM TAXI AND HOSPITALITY SERVICE MODELS, FINTECH PROMISES HAVE A SIZEABLE IMPACT ON THE FINANCIAL AND BANKING LANDSCAPE.

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Banks are trying to stay ahead of the curve by migrating some offline services to online to enhance the customer experience.

Additional space in the form of co-working environments will be carved out from their existing premises to cater to the change.

The successful fintechs will generate long-term gains in efficiency and productivity. Transportation, communication and trade costs will decline.

Around 30% of the total banking headcount is forecast to be replaced by automation over the next decade.

These trends could drive a substantial downsizing in the banking sector's office occupancy over the medium- to long-term.

Fintech is the new buzzword for the banking and financial services industry.

Financial technology, or "fintech," firms are using technology and innovation to disrupt the traditional ways that banks and financial institutions (FIs) do business to better meet consumers' evolving financial services needs. While many banks and FIs view the rise of the fintech sector with concern, the more agile institutions are embracing fintech firms to make them partners in their business growth. With supportive government policies in Singapore and significant venture-capital backing, fintech is poised to disrupt more than just the banking industry. The emergence of these firms is generating demand for startup hub space and, going forward, will likely have a major impact on the office footprints of traditional banks.

Powering the fintech boom

So far, the financial sector has been spared from major shakeups brought by technological innovation, but the good times may not last for long. Fintech has strong venture-capital backing due to its huge potential to disrupt the lucrative banking industry. According to KPMG, investment in fintech startups and scaleups boomed in 2015, hitting new heights of U.S. $19 billion (S$26 billion). With so much funding available, the threat to the banking industry is real and could materialize sooner than expected. In the latest PwC survey published in March 2016, two-thirds of global financial services companies ranked pressure on profit margins as the top fintech-related threat, followed by loss of market share at 59%. Closer to home, 73% of traditional financial institutions in Singapore believe they are at risk of losing business to fintechs, while the global anxiety average is even higher at 83%.

Government policy also tends to support the rising fintech industry. The Monetary Authority of Singapore (MAS) has created a Smart Financial Center, in line with Singapore's Smart Nation plan – one that embraces innovation and harnesses info-communications technology to increase productivity and improve the welfare of Singaporeans.

Traditional banks are taking note. Since late last year, major banks HSBC, United Overseas Bank (UOB), Oversea-Chinese Banking Corporation (OCBC) and Standard Chartered Bank have geared up for technological innovation by setting up in-house fintech labs in Singapore. These labs are dedicated spaces at a bank's office where startups collaborate with banks to develop innovative technology in key areas such as wealth management, payments and collections, trade and supply chain, insurance, cybersecurity and artificial intelligence. These initiatives mark a significant breakthrough in the collaboration between two major sectors, banking and technology.

Though some fintech firms have found a home in the offices of traditional banks, fintechs worldwide are most likely to congregate around hubs that provide a solid startup ecosystem. Singapore is a fertile ground for such firms. The country clinched the top spot in Asia Pacific in the 2015 Start-up Ecosystem Ranking conducted by Compass, offering a business-friendly environment that hosts 2,400-3,600 tech start-ups. The Singapore government has also been heavily involved in the startup ecosystem to push for innovation with the establishment of JTC LaunchPad at one-north.

Affordable rents, along with an established, vibrant startup community and ease of access to support services and networking opportunities has led to the LaunchPad being the favored choice for budding entrepreneurs. The hub's current capacity is approximately 430,000 SF houses – some 40 incubators and 600 startups – and it aims to grow its capacity to house 750 start-ups by 2017.

What does this mean for real estate?

Banks are trying to stay ahead of the curve by migrating some offline services to online to enhance the customer experience. While a necessary step, this shows that financial institutions are embracing technologies to make their businesses more cost-effective. The real paradigm shift will happen when financial institutions rethink their traditional business models as they are forced to compete with innovations such as mobile wallets, crowdfunding, and robo-advisers, which may prove to be game-changers for the industry through 2016 and beyond.

So what does this mean for real estate? As more banks rush to tie up with fintechs to make them collaborators rather than competitors, additional space in the form of co-working environments will be carved out from their existing premises to cater to the change. Headcounts in the various IT departments within the banks and FIs will also be boosted as a result of these collaborations, which will underpin further demand in the office sector over the near term given the additional space required to run such partnerships.

Additionally, successful fintechs will also generate long-term gains in efficiency and productivity. Transportation, communication and trade costs will decline. The lowered barriers to entry will allow more competitive players to enter the market and could bode well for real estate by opening up new markets and driving growth in markets where such growth was not possible previously.

Finally, the substitution of automation for labor across the entire banking and financial services sector will potentially disrupt the labor market with more low- to medium-skilled jobs being displaced by machines. Venture capitalists have poured billions into two key areas of fintech, lending and payments, which could possibly curb banking headcount mainly at the mid- to back-end offices by 30% over the next decade as automated systems are deployed. Around 30% of the total banking headcount is forecast to be replaced by automation over the next decade. According to the latest fintech report by PwC, 83% of the financial institutions surveyed believe that part of their business is at risk of being lost to standalone fintech companies. In addition, more than 50% of respondents are unsure about and unlikely to be able to respond adequately to cryptocurrencies such as Bitcoin.

These trends could drive a substantial downsizing in the banking sector's office occupancy over the medium- to long-term. Based on the total banking footprint of 10.0 million sf in the CBD Grade A buildings in Singapore and the current employee-to-office-space ratio of one employee per 80-90 sf, the potential downsizing due to fintech could translate to a reduction of 904,000 SF of office space in the CBD.[1] Despite this challenge to banking sector headcount, the more complex and personal aspects of the banking functions are unlikely to be fully replaced by technology.

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Just as Uber and Airbnb are shaking up the mainstream taxi and hospitality service models, fintech promises have a sizeable impact on the financial and banking landscape. Judging by the scale and complexity of the major disruptors such as social, mobile, data analytics and cloud computing, the changes are likely to be unprecedented, and commercial property markets will feel them too. A rising fintech industry will fuel demand for startup space and foster new models of collaboration with traditional banks, which will cause the latter to rethink their office occupancy needs. The spread of automation within the sector is also poised to render large numbers of human workers redundant, which could ultimately curb demand for CBD office space from traditional banking and financial tenants.

[1] Out of the 30% reduction of the total banking headcount, we assumed that the bulk of the headcounts eliminated – approximately 70% – came from the back-end offices such as Business Parks or outsourcing destinations outside Singapore (such as call centers), while the rest came from the front and mid-end offices in Grade A CBD buildings. The banking and financial services currently occupy 40% of the total Grade A CBD stock.