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POINTS OF VIEW ON RELATIONSHIPS WITH BIG TECHS

Claire Calmejane,
Chief Innovation Officer,
Societe Generale

In this special edition of the Observatory, we are looking at the Big Techs with two different perspectives: Guillaume Cabrère and Guillaume Marchal from Group Innovation share observations on how financial services engage with them to date and how consumer privacy and security is paramount to a productive relationship, while Guillaume Gombert from FABERNOVEL (our special guest for this edition and the authors of the yearly GAFAnomics reports since 2006) takes a stab at explaining their "superpowers" behind their domination.

#1

PARTNERING WITH BIG TECH : A MATTER OF BALANCE

BY **GUILLAUME CABRÈRE**, OPEN INNOVATION DIRECTOR,
AND **GUILLAUME MARCHAL**, GLOBAL HEAD DIGITAL PARTNERSHIPS,
SOCIETE GENERALE

As emphasized by Fabernovel (an innovation consultancy firm, famous for their GAFAnomics yearly reports), **"GAFA (Google, Apple, Facebook, Amazon) have no markets, only 7 billion potential customers".** As per their business models, these tech behemoths aim to cover as many use cases in order to "simplify the life of their users" and keep them in their ecosystem, whatever their needs. Let's have a quick look on different ways we see traditional organisation co-building innovative products with them for their customers.

"As personalization is at the heart of their success, access to granular customer data is key for Big Techs and transactional data is one of their next coveted playgrounds."

Guillaume Cabrère,
Open Innovation Director,
Societe Generale

Does it mean, though, that partnering with them mainly consists in arming them with extra datasets? Not necessarily. In fact, **partnering with BigTechs can lead to three major types of benefits:**

1 / LEVERAGE THE POWER OF THEIR ECOSYSTEM

Last year, **Amazon announced** it would offer its sellers up to $1 million in credit lines via Goldman Sach's Marcus brand. The deal clearly benefits Amazon: it adds a new source of revenue with the fees from the Marcus credit lines, and its sellers get needed capital to continue selling on the platform. But the deal also benefits Goldman Sachs: with interest rates as high as 21%, fees for late payments, and fees for non-usage of the credit line, Goldman is likely to generate significant revenues. And with a near-zero cost of acquisition—the fee Amazon takes being the only real cost—and a low cost of loan processing, Goldman can live with a higher loss ratio than most banks are willing to. Lastly, Amazon won't have access to credit line usage and performance data since Goldman Sachs has no plan to share them with Amazon.

2/ CO-DEVELOP NEW PRODUCTS

In June 2020, BNY Mellon partnered with Microsoft to create three new data and analytics solutions offerings on Azure: **Data Vault**, a cloud-based data and analytics platform that supports the rapid onboarding of data to provide greater flexibility and accelerate client innovation and discovery; **Distribution Analytics**, a predictive investment data solution, which helps asset managers better understand predictive market demand drivers for mutual funds and exchange traded funds in the U.S. and **ESG Data Analytics** aimed at supporting the customization of investment portfolios to preferred **Environmental, Social, and Governance (ESG)** factors. And such a collaboration did not prevent BNY Mellon to ink a **partnership** earlier this year with Google Cloud on technology that uses artificial intelligence and machine learning to predict when BNY Mellon's clients' U.S. Treasury transactions will fail to settle. According to BNY Mellon, "the model can predict around 40% of settlement failures for trades that are eligible to be settled on the Federal Reserve's FedWire Securities Service, with an accuracy of 90%".

3 / INNOVATE AT SCALE

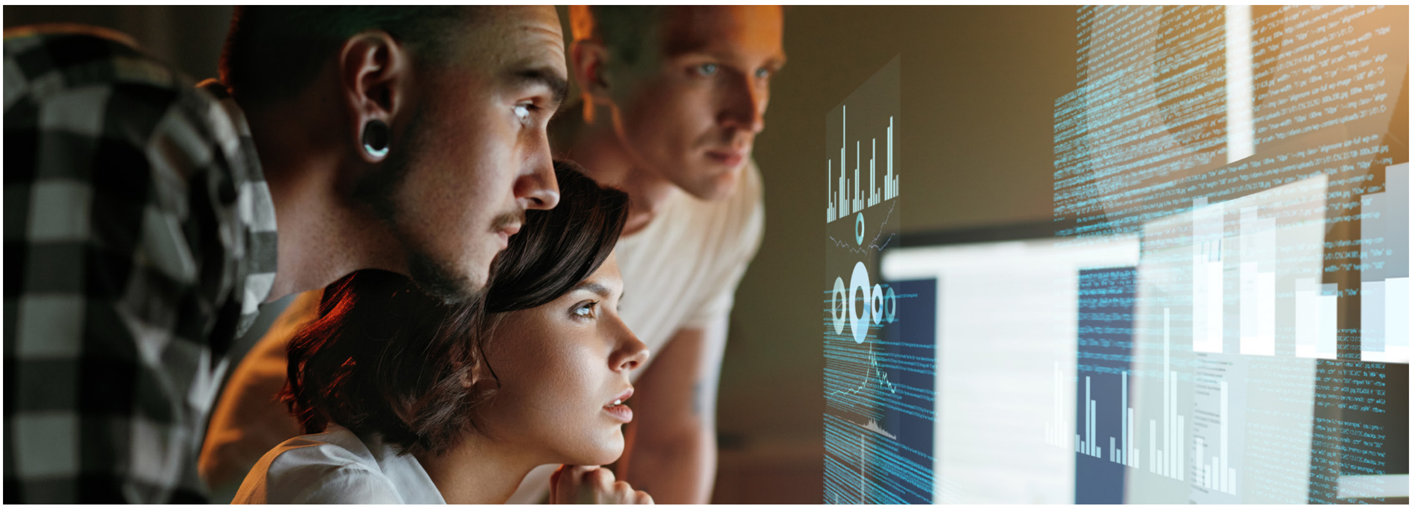
By collaborating with Big Tech, traditional organisation can accelerate their transition to a customer-centric digital delivery model. In the retail industry, this is the path Carrefour has decided to explore. Through its Data & AI Lab jointly launched with Google and Artefact in 2019, Carrefour has successfully advanced from "proof of concept" to "proof of scaling". Part of a wider collaboration with Google, which also includes Google Cloud Platform ("GCP"), G Google Workspace and Google shopping, the AI Lab enables to centralize data practices which were previously addressed in departmental silos and poorly suited to scalability largely due to a lack of test and learn methodology and insufficient expertise. Google supports the Lab in technology, methodology, training and business culture, and has enabled Carrefour to recruit and retain top talent in the AI field. Prior to inking such a partnership, though, Carrefour had invested significantly over several years to build a unique platform, which had made data accessible and exploitable. The availability of such a group-wide data platform was a key success factor of its partnership with Google and possibly a pre-requisite to their AI Lab foundation.

Due to their footprint, learning to work with BigTechs whilst respecting our standards on personal data privacy and security seems inevitable due to the size of their customer base. Many new entrants have already done so.

"The size of their user base, the scale of their platforms, their operating model and velocity make them valuable partners on our path to transformation."

Guillaume Marchal,
Global Head Digital Partnerships,
Societe Generale

The right operating model will involve maintaining a balanced relationship with them and never lose sight of personal data security and privacy according to our role of trusted partners for clients. It's also a strategic imperative to keep developing new business models on Bank as Platform (Shine, Prisméa, Fiduceo offering aggregation...) to serve our customer base.



#2
GAFAS' SUPERPOWERS

A POINT OF VIEW BY GUILLAUME GOMBERT,
PROJECT DIRECTOR AT FABERNOVEL

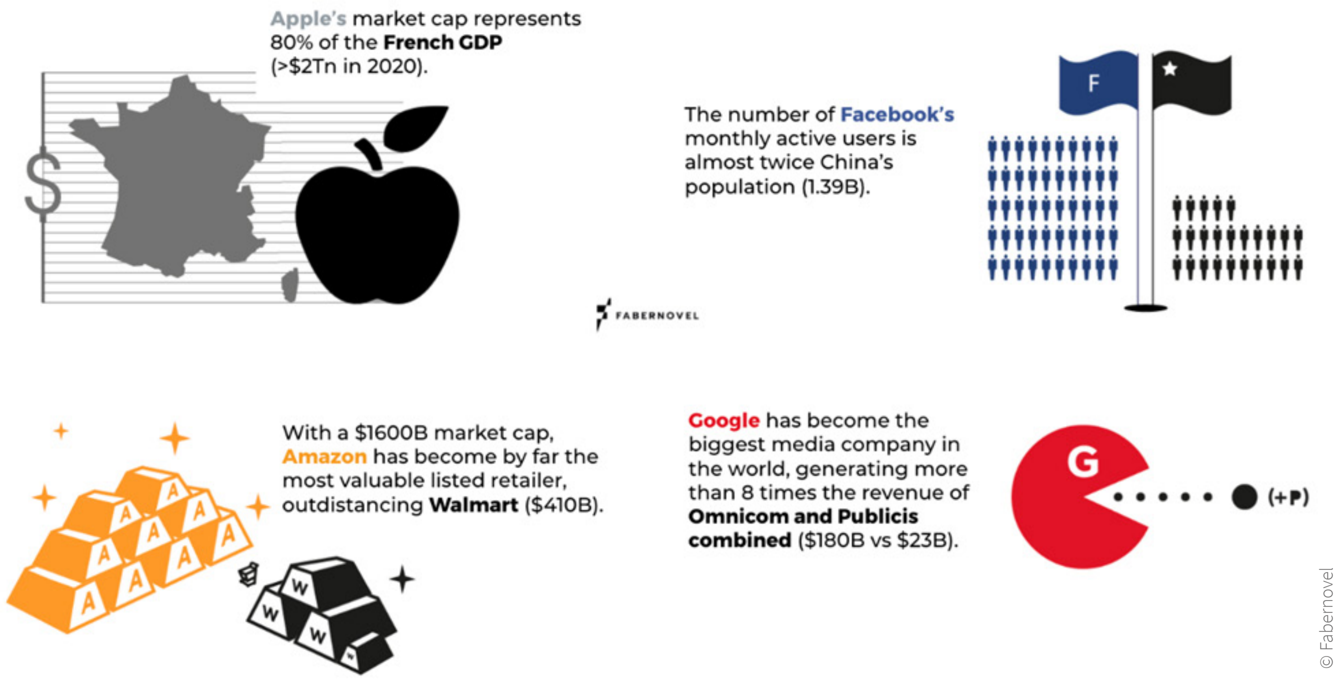
Today, lower digital technology costs, de-regulation and mobile penetration in Western countries enable pure players to create customer experiences and walled gardens that compete with historical actors of the financial industry. Such pure players – and their superpowers – are not only a threat to banks, but also a great source of inspiration and business opportunities in terms of strategy and ecosystem growth. By switching from a product-centric approach to a client-centric one, the GAFA have ushered in a new business paradigm and even set the rules of a new economy.

As a result, GAFA firms have not stayed mere platforms but become gatekeepers, ruling over data and access to captive digital audiences. In 2020, this "monopoly by design" structure and asset light model made them clear winners of the COVID crisis. GAFA had $228.4 billion in total revenue in the last 2 quarters alone, showing a never-seen-before resilience.

"By switching from a product-centric approach to a client-centric one, the GAFA have ushered in a new business paradigm and even set the rules of a new economy."

Guillaume Gombert,
Project Director at Fabernovel

GAFA ARE PLANET-SIZED (AS OF DEC. 2020)

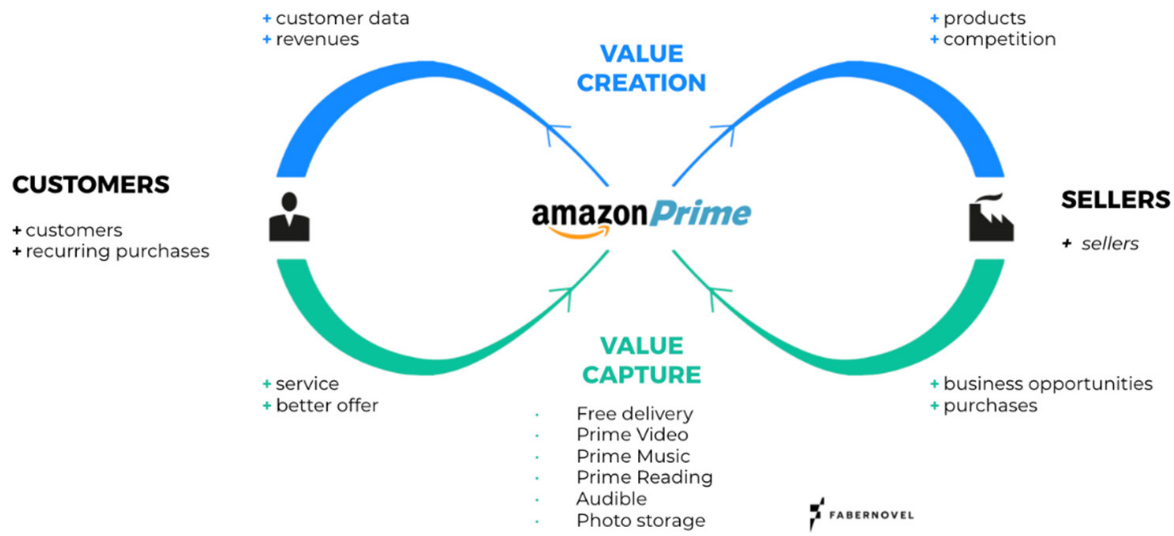


1 / DRAWING ON THESE STRENGTHS, THE GAFA HAVE MADE THEIR WAY INTO FINANCE

THE VALUE LOOP IS AT THE HEART OF THEIR MODELS

The main reason why GAFA are interested in financial services is their potential to fuel value loops. Before the rise of the Internet, value flowed along a **linear value chain: transforming raw materials into added value products.** In the new economy, the ecosystem is in the **shape of a loop that feeds and reinforces itself continuously.** Among a myriad of other players, there is a platform acting as the ecosystem's engine to accelerate usage, data and money and to create virtuous circles.

AMAZON PRIME AND ITS 150M MEMBERS IS THE CORNERSTONE OF AMAZON'S MODEL



GAFA HAVE NO MARKETS, ONLY 7 BILLION POTENTIAL CUSTOMERS

GAFA always reinforce their value loops via two strategies:

- **First,** they try to **capture as much of the share of usage as possible** by continuously adding services to their walled gardens. Day after day, they aggregate services, whether their own or others', with the sole objective of **attracting, engaging and monetising customers over time.** An example of this is Amazon Prime Video, about which Jeff Bezos famously declared: "We manage to monetize Prime in a very unusual way: when we win a Golden Globe, it helps us sell more shoes".
- **Second,** their ability to **collect, standardise and exploit large amounts of data to improve the relevancy of the integrated ecosystem.** A notable example is the Google user account, where information gathered from Gmail can be used to recommend products or services in Search results, or where Search data is sold to advertisers for better ad targeting.

In light of these strategies, **banking and financial services are particularly attractive to the GAFA.** The sector represents a treasure trove of **clients, a long-term relationship and high-value data.** Payment is also a lever of diversification for GAFA's digital ecosystems. Remember **Chinese super app WeChat:** users can access a store of 4M+ mini-programmes connected to WeChat Pay. In 2019 Tencent, its mother company, owned 40% of the mobile payment market share in China with 800M+ users and 1 billion daily transactions (vs. 10 billion for Apple Pay over the whole year!).

GAFA WANT TO HAVE THEIR SHARE OF THE "FINANCIAL" PIE

In the past 10 years, the **GAFA have made a foray into financial services**, either by forging partnerships, buying or investing in companies, or by building their own services:

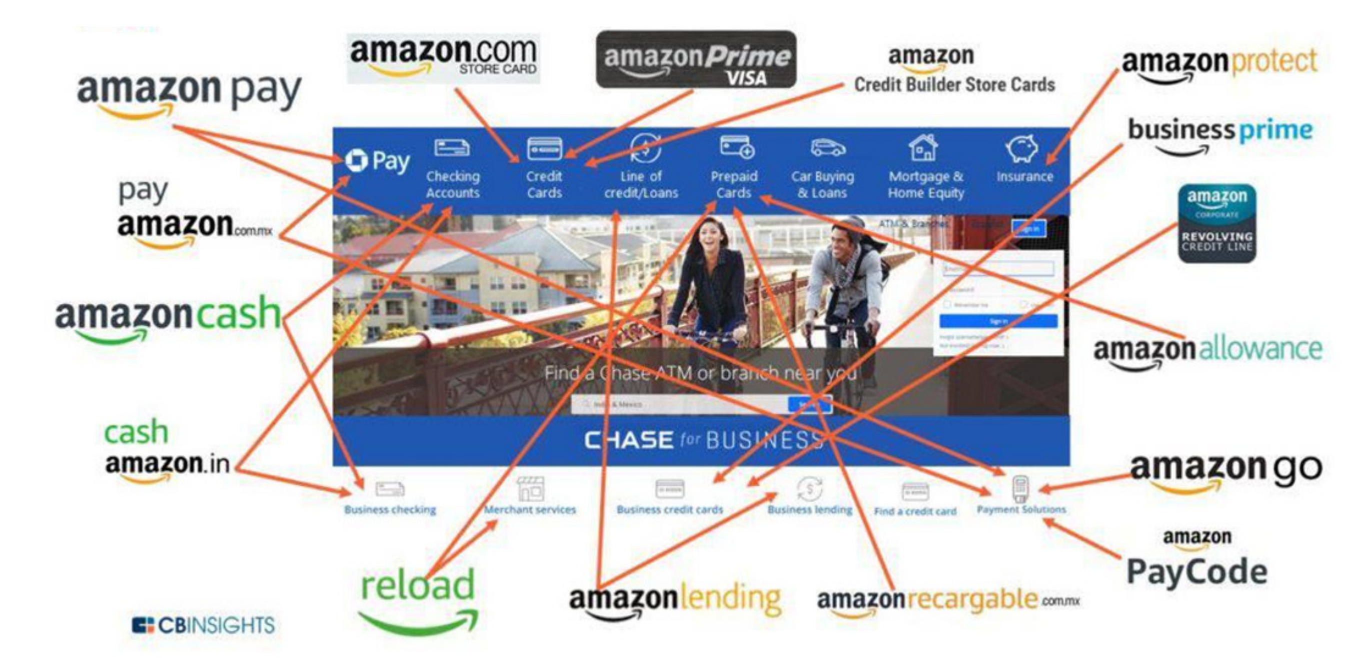
- **Partnerships:** After offering Apple Pay, Apple announced in 2019 the release of its own payment card with Goldman Sachs. It was the **first time that a GAFA had ventured into the field of payment methods**, and it further developed the intimacy the brand is forging with its customers; Moreover, this initiative gave Goldman Sachs access to **a large audience of new customers** since it had only been present on the retail banking market for a very short time through Marcus.
- **Buyouts:** In 2019 Facebook made its first acquisition in the blockchain space. The startup called **Chainspace was building a decentralized "smart contracts" system** that could facilitate payments and other services through blockchain technology.
- **Investments:** Google Ventures has been a **lead investor in several fintech startups,** participating in seed rounds to companies like Digit, Gusto, and Upstart. The VC's earlier fintech investments focused on payments and investment platforms, such Robinhood, CircleUp, and Stripe.
- **Internal development:** In September 2020, Amazon announced Amazon One, a **biometric device linked to a credit card to let users pay with their palms.** It could integrate within its digital and physical ecosystems, especially Amazon Go and Whole Foods stores. Amazon plans to commercialize the technology to third parties such as stadiums or office building.

UNBUNDLING, REBUNDLING: THREATS OR BUSINESS OPPORTUNITIES?

Admittedly, there is a **risk of unbundling** for traditional banks. Amazon, for example, is **integrating financial products into its offering**, making key investments in fintech or forging partnerships with established actors. This supports its core strategic goal: **increasing participation in the Amazon ecosystem.** In 2019, Amazon even started to branch out of its walled garden via a partnership with Worldpay. By integrating Amazon Pay into the Worldpay APIs, any merchant could **offer the former as a payment and shipping option** to its customers. The e-commerce giant is taking core components of banking and adapting them to serve merchants and consumers **within and outside of its ecosystem.**

This shows that **traditional financial actors can also benefit from GAFA's core competency of rebundling, or aggregating, services.** Indeed, if a bank is able to voluntarily open and close its services via APIs ("banking as a service") it can choose to integrate some of them within GAFA ecosystems. This way, they benefit from the latter's global user base, technology infrastructure and state-of-the-art user experience. The GAFA firm, in turn, **derives tremendous value from partnering with a solid, well-respected financial institution**, including the ability to issue credit.

ALL THE WAYS AMAZON IS UNBUNDLING THE BANK



Source: "Everything You Need To Know About What Amazon Is Doing In Financial Services", CB Insights

2 / BANKS MUST DRAW INSPIRATION FROM THE GAFA AND DEVELOP THEIR OWN SUPERPOWERS

TOP SUPERPOWERS TO GET A SUPER POTENTIAL IN BUSINESS

For any large organization, the GAFA superpowers offer super potential to scale up its transformation:

— **The "free customer" and the "utility value model":** GAFA make no difference between a paying customer and a non-paying one. **Usage alone makes the customer**, not the transaction or the money they generate. Delivering sustainable customer value **prevails over short-term profitability.** As a result, GAFA think of themselves as problem-solvers: what matters to them is bringing solutions to **jobs-to-be-bone.**

FOR BANKS, it is particularly relevant to develop **new services' bundles even if they do not immediately generate a financial return.** By tweaking the way they are looking at customers, banks too can take a **"customer lifetime value" approach** rather than focus solely on quarterly financial performance.

— **The "infinite enterprise" and "pirate management":** GAFA leverage their powerful infrastructure, large user base and data to **innovate at scale.** They are also king in **business replication:** once a model is fully operational in a sector, GAFA can duplicate it in another vertical, thus **moving faster and at a lower cost than competitors thanks to microservices.** This has minimised the cost of innovation failures for GAFA and, as a consequence, has created **infinite growth potential.**

FOR BANKS, it entails revisiting **the architecture of their technological stack** and setting a **tech-driven culture.** To reach zero-marginal cost of their innovations, they would need to transform their **operational models**; render their services replicable, evolutive and truly interoperable to allow data and value flow within other digital ecosystems.

- **The "intimate" and "real-time" enterprise:** GAFA use customer knowledge and real-time data to **fine-tune the experiences** they deliver to each customer. Their competitive advantages are **customisation at scale** instant product-market fit that they leverage to improve products' value.

HISTORICAL BANKS CAN TAKE INSPIRATION from GAFA's ability to generate loyalty via **ultra-personalization and convenience** of the customer experience, as Neo banks do, to some extent. A strong data infrastructure and culture of real-time data analysis become essential.

The objective is not to become a copycat of GAFA. Every bank is defined by its values, its assets and its talents. First, it is important to **understand these superpowers, learn how to play with them** and, finally, to **revisit one's underlying operating model:** in other words, **think and behave like a GAFA.**

2 APPROACHES TO SUCCEED IN THE DIGITAL ECONOMY

For legacy companies to thrive, **leveraging these superpowers leads to establishing two kinds of relationships** with tech giants:

- **The "plug in" strategy.** As we saw, plugging into a GAFA ecosystem can yield multiple benefits: reducing time to market, accessing a large client base and data, generating loyalty thanks to superior user experience... **The potential trade-off** here becomes letting the GAFA control the customer relationship, **exposing oneself to desintermediation.** In order to mitigate this risk, interoperability is key to develop new revenue streams and "**Banking as a service" capabilities** become the necessary conditions for independence.

- **The "alternative" strategy.** Their large and historical customer base is a key asset upon which banks can do better than digital native competitors. By **targeting a more specific consumer need and developing a dedicated solution to serve it,** competing firms can beat the GAFA at their own game. In 2019 for example, a consortium of India's eleven largest banks launched the first ever blockchain-linked loan system in the country. Instead of multiplying ties with fintechs to try and keep up with GAFA's pace, these **intra-sectoral alliances are able to create competitive technological infrastructures.** Such synergies are only possible if the involved players agree to **open their assets and share value.**

In the end, the first key challenge is to strike the **right balance in the relationship** with Big Tech which requires absolute clarity on the respective contributions of both parties. Find the right partner to co-build, co-brand and co-distribute products and set the conditions to maximize shared value. In a world of connections, forging alliances is a must and innovation becomes a collective sport. Remember the value loop: having an extended ecosystem will allow banks to nurture their own loops and to create attractive services for customers, which after all has been the secret to GAFA's success all these years.

FABERNOVEL

A few words about Fabernovel

Since 2006, Fabernovel has been carrying out the GAFAnomics public studies to contribute to the readability and accessibility of the digital revolution and the major transformations in the economy. They are an opportunity for all to explore subjects of innovation, to gain a better understanding of the digital world and to develop analytical frameworks on the successful recipes of the platforms, unicorns and American and Chinese tech giants. These studies help to understand all the competitive dynamics of this new economy, its performance factors and its development strategy. Discover their latest book, comprehensively deciphering the GAFA model (in French): *GAFANOMICS : Comprendre les superpouvoirs des GAFA pour jouer à armes égales,* François Druel, Guillaume Gombert, Collection GAFAnomics, Éditions Eyrolles.

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