FinLab Snapshot:
Helping More Americans Achieve Financial Health

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The Center for Financial Services Innovation (CFSI) is the nation’s authority on consumer financial health. CFSI leads a network of financial services innovators committed to building a more robust financial services marketplace with higher quality products and services. Through its Compass Principles and a lineup of proprietary research, insights and events, CFSI informs, advises, and connects members of its network to seed the innovation that will transform the financial services landscape.

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The Financial Solutions Lab (FinLab) is a $30 million, five-year initiative managed by CFSI with founding partner JPMorgan Chase & Co. The Lab seeks to identify, test and bring to scale promising innovations that help Americans increase savings, improve credit, and build assets. Lab participants share a relentless focus on building products that will improve the financial health of Americans. The Lab provides capital, national partnership opportunities, industry expertise, mentorship, and cutting-edge consumer and design insights necessary to build the next generation of leading financial products and services.

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Most Americans struggle to manage their day-to-day financial lives, establish a cushion for financial resilience, and achieve financial security. This group is larger than just the “unbanked” or “underbanked.” Fully 57 percent of U.S. households are struggling with their financial health, and nearly half of Americans do not have $400 available to them without relying on credit or selling possessions.1 CFSI’s latest Financially Underserved Market Size Study found that underserved Americans spent $141 billion in fees and interest just to manage their daily financial lives, illustrating the immense opportunity for companies to leverage technology to better serve those consumers.

Given the severity of this problem and to encourage a greater diversity of solutions, the Financial Solutions Lab broadened its 2017 Challenge to target innovators who were focused on improving U.S. consumers’ financial health, with a particular focus on addressing the needs of underserved segments that tend to have significantly worse financial health than the overall U.S. population. The Lab – a $30 million, five-year initiative managed by the Center for Financial Services Innovation (CFSI) with founding partner JPMorgan Chase & Co. – has a mission of improving Americans’ financial health through innovation.

This year, the Financial Solutions Lab highlighted the unique challenges facing a number of these communities, including aging Americans, individuals with disabilities, people of color, and women. By shining a spotlight on the financial services needs of the most vulnerable, the Lab seeks to spark greater ideas and action to extend and improve financial services in novel and transformative ways for the most underserved segments.

Applications to this year’s program were accepted from February to April 2017. These applications provide a unique snapshot into the state of consumer fintech innovation in the United States.

This year, 361 applications were received, a slight increase from last year and a 20 percent increase from 2015, the Lab’s inaugural year. These applications represent a wide swath of consumer-focused financial technology companies and inform our perspective on the developments in, and state of, the overall market.

While the applicant pool is not a perfectly representative sample of all consumer fintech solutions in the market, the following analysis strives to provide an illustrative snapshot of trends in the market, allowing us to get a pulse on the latest innovations focused on improving consumer financial health for U.S. consumers.

Key Takeaways

- 361 applicants applied, even with last year and up 20 percent from 2015. Applicants drew from 36 states, two more than last year. The average applicant had raised $630,000, a 40 percent increase from 2016. Average team size was seven, up from six last year.
- Applicants are increasingly focusing on narrower niches early on, while broad personal financial management products are becoming less relevant. These specialized products are proving to be easier to scale and offer a more immediate payoff to the end-user.
- We continue to see limited innovation in insurance.
- Companies are becoming increasingly sophisticated in their use of business, especially employer, channels. Employee-benefit tools are becoming increasingly prevalent and sophisticated.
- Nonprofits are, with some notable exceptions, choosing to partner with for-profit startups as opposed to developing technology in-house.

The Applicants

FinLab’s applicants this year represented a diverse set of organizations that showcase a striking breadth of technologies and innovations to help consumers improve their financial health. Applicants came from 36 states and represented both for-profit startups and nonprofit providers. They represented many product categories and merged traditional silos to form new types of products.

On average, applicants had slightly more mature business models than in previous years. Organizations employed seven people on average, up from six last year. A majority had raised external capital, with an average amount of $630,000, up from last year’s $450,000.

However, we continued to see a wide range of firms applying: the average variance (technically, the population standard deviation) on capital raised was $1.6 million. Similarly, the number of users varied widely, with an average of 16,000 – more than double last year’s 7,000. However, the median number of users was only 30, reflecting the fact that many applicants were pre-product.

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Applicants were spread across a number of product categories, as illustrated below.

A final theme, which builds on observations from previous years, is that companies are either tracking social impact metrics or coming to the Lab for guidance on how to best track their impact on their customers’ financial health. CFSI sees this trend broadly across the financial services industry, and we are continuing to identify ways to communicate our learnings to the industry more broadly.

A Look at the Trends

1) Increasing specialization and commoditization of Personal Financial Management tools

As the fintech space continues to mature, we have observed companies increasingly targeting specific niches within the broader market. This “nichification” has precluded interest in more broad personal financial management (“PFM”) and education products. While driven partly by general market maturity and a plethora of traditional products available to consumers, this trend is also a response to financing pressures and consumer demand. From our read of the market—and in discussions with founders, investors, and industry experts—we believe that it is likely that a relatively small number of consumers has a strong interest in general financial management products and may be acting as power users within the category. While this dynamic leads to relatively rapid early growth for a number of products, few have been able to scale meaningfully. In our experience, the most impactful companies, such as Albert (selected in 2016) create a virtuous feedback loop, helping to reinforce healthy behaviors, as opposed to simply presenting information.

Entrepreneurs have responded by developing solutions focused on increasingly specific financial challenges that affect a broad swath of consumers. Examples include encouraging automatic savings (Digit, from the Lab’s inaugural class), managing income volatility (Even, also from the Lab’s first class), avoiding overdraft fees (Dave.com, selected in 2017), and financing home equity (Point, also selected in 2017). Importantly, the most successful of these products often are able to achieve very low adoption friction that is difficult to achieve with more general products.
As an example, an automated savings app may only require a savings goal and bank account information, while a more traditional PFM product would require the consumer to engage with a complex set-up, classification and budgeting process, the benefits of which are unclear until several weeks or even months of use have passed.

This is not to say, however, that the ambitions of companies in this segment have changed. While most founders still articulate a goal of providing a full suite of products to their customers to address a range of financial needs, innovators are seeking to gain a toehold in certain niches before broadening their offerings. This approach has created a number of “freemium” models in which the product that the company plans to become known for is expected to be offered for free in perpetuity, while the revenue model is based on alternative services that are planned as future releases. For example, Tomorrow (FinLab class of 2017) offers free end-of-life financial planning, while life insurance commissions provide the revenue model. Given the newness of this approach, we have few data points on the likelihood of success for these revenue models. While standard freemium models typically target conversion rates of two to five percent, it remains to be seen what will be necessary for these new revenue models to be successful.

2) Broad categories remain unchanged

While companies are following increasingly specialized paths to market, the fintech sector is still largely composed of the five primary types of businesses we discussed above: credit; insurance; savings/investing; payments; and education. Over the past three years, we have seen many paths into these markets, but the fundamental segments remain unchanged. Some of the most innovative companies are using technology to bridge between these segments.

Credit, as perhaps the oldest category of financial services, continues to see innovation, particularly in the form of credit analysis, credit-building products such as Petal, and employer-sponsored products. Given the regulatory constraints around lending in the U.S., it is rare to see early-stage companies actually engaged in the process of lending. Most startups that we see are involved in providing superior information or processes to lenders in order to allow these legacy institutions to achieve better-performing loans. As in many sectors, the ability to create a vastly superior user experience tends to be a significant advantage startups have over incumbents. Referrals remain a common revenue stream.

Representing another innovation in lending is one of this year’s winners, Nova Credit, which has built the world’s first cross-border credit reporting agency. Focused on immigrants with thin- or no-file credit history, the company validates and compiles borrowers’ overseas credit information and securely shares this information with lending partners in the U.S. If successful, this product could have profound implications on the financial health of immigrant populations in America; in addition, it opens up a potentially robust stream of now credit-worthy consumers for lenders.
Saving is a similarly well-established segment. Companies in this category either offer direct savings/investment products or provide consumers with information (e.g., budgeting tools) about how to save.

There is a clear trend away from pure budgeting apps towards more automated tools, such as Digit, that require less direct user interaction. As we discussed earlier in the context of PFM tools, this segment is maturing away from broad tools towards targeted solutions that reduce on-boarding friction as much as possible. Prize-linked savings is yet another tool being developed, focusing more on behavior modification than automation.

Money movement—or payments—was one of the earliest categories in fintech, representing the business models of foundational companies like PayPal. In recent years, there has been intense interest in peer-to-peer payments; PayPal-owned Venmo has recently come to dominate this space, while others are playing aggressive catch-up.

Overall, we are seeing fewer payments companies as this sector matures, and most recent pure-play payments businesses have tended towards a B2B model in which closed-loop systems insulate newcomers from the complex state-by-state regulatory framework. As the Lab is focused on the consumer segment, we have noticed that payments and money transmission tend to be side effects of other business models, and are becoming less prominent as primary products. As an example, a savings product may need to transfer money between a checking account and an investment account, but that is a supporting process, not a primary service.

Insurance remains nascent, as startups struggle to innovate in a saturated and highly regulated marketplace. Most businesses we have seen in this segment are distribution plays, looking to circumvent middlemen and logistical hurdles to purchasing insurance that is ultimately underwritten by legacy providers.

A key challenge in this space is that insurance policies tend to be expensive one-time purchases or recurring policies managed by an agent, which consumers are reticent to switch. As a consequence, the market can support inefficient distribution models. Extensive regulation tends to homogenize various policies, such that automated comparison-shopping tends to yield less value for consumers than in other sectors.

We have, however, seen some very innovative approaches to reapplying insurance products to other means. Blueprint Income, as an example, is leveraging a traditional insurance product, annuities, into a pension-like retirement plan. This combining of insurance into different kinds of financial products is something we expect to see more of in the future.

Finally, there remains a subset of planning tools that focus on educating consumers. These companies continue to be a staple of our applicant pool. Overall, there tend to be two segments here: community-focused, regional organizations that provide in-person guidance and coaching; and apps—often focused on children—that use technology to teach financial responsibility and planning. While we continue to believe there is great promise in leveraging technology to extend the impact of in-person coaching, we have seen few applicants that have the necessary technical expertise and financial resources to execute on this strategy.

Similarly, while we believe there are untapped opportunities to build financial health within families though technology, the vast majority of family and child-focused applications have focused on more affluent families and less impactful use cases, such as streamlining allowances. In addition, we would encourage innovators in these areas—where growth continues to seem elusive—to focus on use cases that are more impactful for less affluent families or where the technology is creating opportunities for shared experiences and learning.

Ultimately, while we continue to be supportive of educational efforts, we hope to see more innovation that is focused on using technology to remove cognitive burdens from users. The best products allow consumers to achieve better financial health outcomes without deliberate effort. In furtherance of this goal, the Lab is working with our existing companies to help them implement key concepts from behavioral design.

3) Increasingly sophisticated use of businesses as channels

While the B2B2C (business to business to consumer) or B2B2E (business to business to employee) sales model can be a highly effective distribution channel, we frequently see this strategy misused as a way to dodge the seemingly finicky individual consumer. Faced with daunting consumer acquisition challenges, entrepreneurs occasionally pivot to business channel distribution as another method to get their product out to consumers. This approach is almost never successful, as products that lack a fundamental consumer appeal rarely gain traction solely by means of a different distribution model. Furthermore, few businesses are willing to distribute a product that has not demonstrated some degree of standalone success.

There are, however, three key situations in which we have seen business channels as viable: first, when used by more mature businesses to reduce marketing costs; second, when pitched as a direct employee benefit; and third, when used to enhance an existing consumer product.

In the first case, we tend to see well-established consumer players eventually pursue a B2B2C distribution model as traditional channel marketing costs increase. At a certain point, the cost of developing a business partnership can become appealing relative to increasing direct-to-consumer marketing costs.
The last two years of the challenge have witnessed a proliferation of entrepreneurs who are selling their product directly to companies as a potential employee benefit or reaching companies by integrating with human resources tools like payroll systems and benefits portals. As offering traditional retirement and healthcare plans has become prohibitively expensive, employers increasingly are seeking alternative perks. Fintech has emerged as an appealing option, with companies like Flexwage and Instant Financial (both of which allow access to accrued wages within a payroll cycle) providing valuable options to employers and employees alike.

A third but less common scenario occurs when a company’s product strengthens the distribution strategy of an existing business or system. This approach is common in insuretech, although we have also seen it used to great effect by two Lab winners: Propel (a member of the Lab’s first class), which streamlines an otherwise difficult and clunky benefits process to make it easier for people to apply for and manage food stamps; and Token Transit, a company in our current class that provides fully electronic public transit ticketing, saving consumers significant cost and time.

These approaches, however, are not without their challenges. While having the cooperation of a partner to acquire users is a major benefit, the needs of two constituents must now be served and reconciled: the end-user (consumer) and the provider of the service (the business channel). If those interests are misaligned, the startup will have to navigate a complex path.

4) Nonprofits are increasingly leveraging tech partnerships, rather than developing in-house

This year is the first in which we do not have a nonprofit in the current Lab class. As the space has continued to mature, nonprofit strategies have evolved. Within our applicant pool, we see less development of in-house tech solutions and more focus on potential partnership opportunities among nonprofits; it is our belief that this trend is largely the result of the costs associated with technology development, though it may also be due to decreasing numbers of nonprofits in our observable applicant pool. Unlike their for-profit peers, nonprofits do not have the ability to pay for development costs in equity or raise venture capital. However, it is also the result of a growing willingness on the part of nonprofits to leverage the innovations in fintech to expand their own services and capabilities through meaningful partnerships.

While we continue to see younger nonprofits led by technical teams (like Onward and Upsolve), and more established non-profits with a demonstrated track record of development success (such as Commonwealth and 2016 Lab Winner EARN), many nonprofits appear to have shifted away from direct development to partnership models. Neighborhood Trust, a nonprofit from the first year of the Lab, is emblematic of this shift. Originally, the organization was developing a comprehensive solution in-house. Through their experience in the Lab, the nonprofit shifted to a partnership model in which they leveraged FlexWage’s innovative technology to dramatically shorten their time to market, expand the capabilities that they can offer, and allow them to focus on serving the needs of their clients at greater scale.

Similarly, this year, the Lab made its first direct grant to a nonprofit service provider to help them pilot new fintech products. Through this grant, GreenPath Financial Wellness is piloting several new products—including a number of FinLab company products—and using their experience to inform the nonprofit community on strategies for successful partnerships. The Lab is planning to support this activity.

To help further encourage this development, CFSI recently created a dedicated Fintech and Nonprofit Working Group to provide a vehicle through which nonprofits can inform product design, identify new partnership opportunities, provide capital for pilots, and share lessons learned broadly across the field. The Lab is supporting this effort as well.

What’s Data Got to Do With It?

Access to consumer financial data is a critical component in many fintech products. Currently, access to such information is highly fragmented, and the information available to companies in this space is often limited and of poor quality. As a consequence, the quality and reliability of many promising offerings has suffered, limiting consumer adoption and trust. CFSI is working closely with industry and government to build a framework for data sharing to ensure that these data are available, reliable, and transmitted securely. For more information, visit http://bit.ly/CFSIDataSharing to see the latest on this important topic.
Looking Forward

We continue to remain extremely enthusiastic about fintech innovation that improves consumer financial health—both in terms of consumer impact and company valuations. We are moving into increasingly complex and exciting challenges that will require more innovative and sophisticated solutions to overcome obstacles on America’s financial health journey.

From both investors and entrepreneurs, we see increasingly specific and targeted solutions that address and solve real-world problems. There has been some discussion of a “great rationalization” in fintech. Given the proliferation of products that address individual problems, some observers have indicated that there is likely to be a consolidation of these feature-products into a more general financial tool. While predictions like these are difficult to analyze, we tend to think that the fragmentation will remain, with more trivial, feature-only companies being selected out naturally or gradually acquired. Unlike traditional products with high distribution costs, software presents little economic rationale for consolidation. Innovation is still continuing at a rapid pace, and the sector is far from mature.

We do not expect the current political environment to have a substantial impact on the early-stage environment. Regulation directly affecting these companies is unlikely to change meaningfully in the near-term, and access to capital remains relatively consistent.

The quality and sophistication of applicants to the Lab has increased steadily over the past three years. We remain impressed and humbled by the quality of companies, the motivation of the teams, the understanding of consumer financial health needs, and the innovative products we see every day. While financial health continues to remain a challenge for most Americans, we are deeply optimistic about the promise of future solutions.

2017 Diversity Survey Results

The Lab remains committed to improving diversity in our industry and work. One small step in that process is to share data about how we’re doing in recruiting diverse founders to apply for the Lab and infusing our selection process with diverse perspectives to ensure that the Lab’s solutions reflect the diversity of our country.

In addition, each year we survey the applicants of the Lab on a number of questions related to the diversity of their teams.

This year, 46 companies responded, representing 13 percent of the total applicant pool. While clearly not a representative sample of all applicants, we believe sharing this information – even if anecdotal – can help advance our collective understanding of diversity in the FinTech community.

Here’s a look at what we learned:

- 96 percent of survey respondents said team diversity is important or very important to their company.
- The average age of founders is 38 (for nonprofits, 43)
- Racial diversity of founders is similar to last year’s survey results: 23 percent reported 1 or more founders who identify as Black or African American, 12 percent as Asian or Pacific Islander, 6 percent as Hispanic, Latino or Spanish origin and 4 percent as American Indian or Alaska Native. These numbers are largely consistent with the survey responses received in 2016 (of which 35 companies participated).
- Founders continue to skew male: Of for-profit survey respondents, 22 percent identified 1 or more founders as female, slightly up from 17 percent reported in 2016. Of nonprofit respondents, 33 percent identified 1 or more founders as female.
- Applicants with female founders have more balanced employee gender ratios. In companies with no female founders, the average gender ratio of employees was reported as 72 percent male vs. 28 percent female. However, companies with at least one female founder had a gender ratio of 50/50. While anecdotal, this seems to support the hypothesis that greater diversity among leadership results in more diverse organizations.