Fintech initiative for private placements

Working with banks on debt capital markets

by Frank Scheidig in Frankfurt

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Fintech companies are everybody's darlings. Major financial centres and many banks have their own fintech incubators or accelerators. Unconstrained by legacy systems and processes, fintech companies take pride in their ability to innovate and disrupt. This is seen primarily in retail markets with the establishment of companies such as the peer-to-peer lender Zopa, and TransferWise for foreign exchange transactions. Fintech companies thrive because they can promote their services directly to customers. They make market gains against incumbents by being more cost effective and easier to use, and by focusing on niche areas.

These methods do not always translate to a wholesale environment such as capital markets. Fintech companies must overcome considerable barriers including the complexity of regulations, IT systems, capital requirements and the need for accepted standards. This may well be why those companies backed by banks or other strategic players, such as exchanges, tend to reach maturity faster and become more successful than those without such support.

Disruption in wholesale environments is less common but also less desirable. Fintech companies can work alongside banks and help add value by better monetising existing assets such as data, or by mutualising industry costs. The idea of mutualising costs is already well established through partnerships such as the payment system Swift or the DTCC in the US for settlement issues. A similar approach has been taken by collaborative start-ups such as the R3 consortium in the blockchain environment. Others such as TrustBills are looking more at the commercial banking sector rather than capital markets.

Establishing industry utilities is infinitely more difficult than offering a new niche product to retail consumers. DZ BANK is working with peers to support an industry utility that will revolutionise debt capital markets by mutualising costs that so far have been carried by banks, issuers and investors alike.

The 'european private placement facility' is a neutral and independent platform regulated by the Luxembourg financial sector regulator (CSSF). It allows borrowers – companies, municipalities, regions, sovereigns and agencies – to issue debt securities in a fast, standardised and cost-effective way. This will help banks restore their return on equity and optimise regulatory compliance. Borrowers will be able to tap markets in a way not possible before. Investors will have access to standard documentation, stringent quality control and data hubs for help in carrying out due diligence. The eppf initiative should also benefit countries' economies by bridging national borders, which still limit markets to smaller regional pockets.

By offering the complete value chain of a bond issuance, eppf allows each stakeholder to concentrate on what it does best – banks originate and place bonds, investors analyse and make informed investment decisions, borrowers tap a large universe of potential investors, and regulators supervise efficiently. The link between them all is eppf. Although evolutionary rather than disruptive, the results it achieves are revolutionary. Owing to the immense economies of scale, trades can be settled at T+1 (one day after the trade date). This will improve to T+0 in the future, eliminating the difference between primary and secondary markets. The standardisation of bond documents makes them easier to compare and easier for traders and investors to understand. This will improve liquidity.

Lower costs will enable new issuers to access markets, reducing an economy's dependence on bank funding. If the link between sovereign funding and banking crises is broken, the overall resilience and stability of economies will increase. The private placement initiative is an example of how, with an open-minded approach, fintech can be used to the advantage of a whole market and even entire economies. The hope is that it is the first of many industry utilities that provide revolutionary services in a collaborative way.

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