The 3 Biggest Ways Technology Companies Threaten Canadian Banks

Description

While speaking at a conference in March, **Royal Bank of Canada** (TSX:RY)(NYSE:RY) CEO Dave McKay said that banks are "on a collision course" with technology companies. **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) CEO Bharat Masrani has also weighed in, saying that tech companies are creating heightened competition, and enjoy the advantage of being more nimble.

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So, how exactly are these newer companies threatening the banks? Below we take a look at the top three. And to honour the recent retirement of David Letterman, we'll count down from three to one.

3. Peer-to-peer lending

In the long term, peer-to-peer lending may be the biggest risk that tech companies pose to the banks. After all, it threatens the banks' most basic function: collecting money from savers and lending it out to borrowers.

Peer-to-peer lending has a number of advantages over the traditional model. Borrowers love how rates are lower than credit card loans, it's a lot easier than borrowing from a bank, and savers are able to get a higher yield. The peer-to-peer lending platforms use far more data points than banks do, which helps reduce risk. And regulators like how credit risk is passed directly to savers (thus eliminating the possibility of a government bailout).

That said, Canadian banks won't be feeling much heat from peer-to-peer lending any time soon. Peer-to-peer lending mostly serves smaller customers, and these people are typically underserved by the banks anyway. Likewise, banks aren't especially keen on unsecured consumer loans. And peer-to-peer lending may be subject to greater regulation down the road. So for now, this threat remains at number three.

2. Robo-advisors

Most people agree that the traditional model of wealth management is broken. After all, why should we pay 2% of our savings to advisors every year when most underperform their benchmark? In Canada, where investment management fees are especially high, the industry is ripe for disruption.

Enter the so-called “robo-advisors,” which use index funds, along with basic algorithms, to generate a low-cost portfolio for their clients. Examples include Wealthsimple, WealthBar, and Nest Wealth.

This will be a slow process. Robo-advisors are most appealing to younger people, who don’t have much money anyway. Older savers, who have more money, tend to have a personal relationship with their advisors. But over time, as the young generation turns into the old generation, banks could easily get left behind.

1. Payments

When you buy something with your bank-issued credit card, your bank benefits three ways: it earns a piece of the transaction, it collects purchase data, and if you don’t pay your bills on time, then your bank will charge you hefty interest.

It’s no wonder that so many players are looking to disrupt this market. The biggest threat, of course, is Apple Pay, which collects 0.15% of each transaction in the United States.

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Apple Pay isn’t looking to collect any data, but rival offerings from companies like **Google. Facebook** is also getting in on the act through its Facebook Messenger app. There are countless other offerings, many of which come from very deep-pocketed companies.

So, this threat absolutely deserves to be number one on this list. Investors, take note.

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