3 Easy Ways to Invest in the FinTech Revolution

Description

For much of the last two centuries, banking hasn't really changed.

The first step is to raise capital, usually in the form of deposits. A bank would then lend that money out to homeowners, businesses, and other decent credit risks. Profit is the difference between the rate paid to depositors and the rate charged to borrowers, minus any operating expenses.

The beauty of banking is the diversification of loans. One loan is risky. A portfolio of thousands of different loans isn't.

This was then used that as a platform to expand into other businesses. Wealth management used to be completely independent of the banks. So was insurance and capital markets. These days, you can get all of these things at your local bank branch.

The depth of products offered isn't the only thing that's changed about banking. Technology has made it possible for customers to do many different things online, including apply for loans, open up investment accounts, and even do enough day-to-day banking to avoid the branch entirely.

It's pretty obvious this part of the financial system is going to have the greater growth going forward. Here's how you can invest in this new high-tech revolution.

Power Financial

Power Financial Corp. (TSX:PWF) is a holding company with stakes in **Great-West Lifeco**, **IGM Financial Inc.** (TSX:IGM) and several different European stocks. Many investors are attracted to the name because it perpetually trades at a discount of 20-30% versus the sum of its parts.

One of Power Financial's smallest investments could actually end up having a huge impact. Back in April 2015, it bought a 59.8% stake in Wealthsimple, one of the leading robo-advisors.

The business model is simple. Wealthsimple uses software to choose an asset allocation that's suitable to an investor's risk tolerance, using low-fee ETFs. Wealthsimple then manages that portfolio at a much lower cost compared to traditional mutual funds.

It isn't entirely software-based, however. If the client has any questions, they can phone in and talk to one of the company's phone representatives.

IGM Financial

Power Financial invested $30 million in Wealthsimple, which is a rounding error for a company with a market cap of $22.5 billion. What makes this investment significant is the ramifications it could have on IGM Financial, which is worth nearly $9 billion.

It's obvious IGM is fighting an uphill battle. Many investors are eschewing expensive mutual funds in favour of cheaper alternatives. IGM may borrow much of Wealthsimple's business model to help keep assets in house going forward.

I believe IGM Financial will be forced to start adopting techniques to keep investor costs down, probably by adopting many of the same techniques currently used by Wealthsimple. IGM isn't a FinTech investment yet, but it likely will be in the near future.

Mogo

A series of start-ups are disrupting the banks in a different way. They're using the internet and software to give loans to people they haven't even talked to.

Mogo Finance Technology Inc. (TSX:GO) is Canada's only pure-play online-only lender. Growth has been on fire of late, increasing members from 250,000 to 300,000 in just over a month. The company has done more than 1.3 million loans since 2007.

The future looks strong too. Mogo's management thinks the company can get its fingers into all sorts of different parts of the market.

If that's the case, why are shares down 65% in the last year?

Even though Mogo's top line is growing like crazy–revenue has spiked from $15.3 million in 2012 to $49.5 million in the last 12 months–it's not translating to profits. Mogo has lost $22.7 million in the last year.

A big part of the reason is Mogo's high write-off rate. It wrote off 22.3% of loans outstanding in its most recent quarter. That's actually an improvement versus the same quarter last year, which saw a charge-off rate of 30%. The company thinks this will go down as it moves more towards longer-term loans.

The bottom line

It's obvious technology will impact the financial industry in a big way. Will the big boys adapt, or can some of the smaller companies actually win? Answer that question correctly, and your portfolio will likely reap the benefits.

CATEGORY

1. Dividend Stocks

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1. Editor's Choice

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