



A Work Project, presented as part of the requirements for the Award of a Masters Degree in
Management from the NOVA – School of Business and Economics

Disruptive Innovation in Banking – The example of FinTech

[MIM Business Project: A model to support FinTech start-ups to bring value to Millennium's
customers]

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Abstract

This work project explains the context in which FinTechs have emerged as disruption in the banking sector. This called for Millenium BCP's concerns on creating a strategy to deal with these new players, in order to increase value to their customers, which was the central purpose of the Business Project here presented. The proposed strategy and minimum readiness requirements are identified, derived from best practices and hypotheses testing. Finally, this paper includes an academic revision on the theory of disruptive innovation, with FinTech as an example, adding on how it should be managed in the banking sector.

Keywords: Disruptive innovation, Banking, FinTech

*“And, when you want something,
all the universe conspires in helping you to achieve it”*

Paulo Coelho, in *The Alchemist*

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1. Context

1.1 Millennium Banco Comercial Português

Millennium BCP (Mbcp) is the largest private commercial bank in Portugal. It was founded in 1985 after the liberalization and development of the Portuguese banking system, and has become a reference institution in different markets since then. The bank generates value through the creation of relevant banking products and services, delivering through high standards of excellence and corporate responsibility to all its clients. Their vast product range includes current accounts, payment methods, savings and investment products, private banking, asset management and investment banking, credit cards, loans, commercial banking, leasing, factoring and insurance, among others. After reaching a solid position in Portugal, Mbcp made a clear commitment to expand the retail business to other geographies, having achieved a consolidated stand in specific European and African markets, under the branding of *Millennium*. Ensuing its internationalization path, the bank reaches worldwide presence through branches, representative offices, commercial protocols and promoters, as well as transfer agreements.

Serving clients in a segmented manner, the bank emphasizes customer-centricity on their mission, in addition to a rigorous code of conduct and profitability growth compromise, that grants attractive returns to shareholders. Mbcp's vision is to become a reference in service to their retail and enterprise clients, based in innovative distribution platforms on high potential markets. The guiding values of the institution are respect, client-focus, excellence, trust, ethics and responsibility.

After 30 years of operation the bank considers itself agile and modern, which is sustained by their 3 key strategic pillars: innovation, dynamism and financial soundness. Following the harsh 2008 global financial crisis that caused its negative impact on the bank's results, the current

strategic plan is to recover profitability, grow international operations and achieve sustainable growth, namely through new technologies and ground-breaking branches to best reach the relevant segments.

1.2 Market overview

Subsequent to the financial crisis in 2008, the banking sector was seriously harmed from different perspectives: by losing capital on mortgage defaults, by the impairment of credit, and the restraining of interbank lending. This was utterly aggravated by the substantial increase in regulations and the overall depreciation of the economy, accompanied by a downfall in share prices worldwide. The utmost impact was felt by a general decrease in confidence on financial institutions, leading consumers to restrain their savings and, therefore, withering the credit business. If considered that, in addition, banks are commonly viewed as traditional, risk-averse and slow to implement change, it is easy to understand the arise of new players and the shift in customer preferences.

FinTechs appear, then, as disruptive start-ups leveraged on advanced technologies and fast innovation processes, offering alternative financial services mainly in digital payments, business finance, consumer finance and insurance. These new companies target mostly digital customers by offering them personalization, complete mobility, convenience, and novelty services or features. FinTechs are growing increasingly in number, scale and awareness, and hence more and more banks have been pushed to act innovatively, finding ways to accommodate or dispute the arise of new players. Although some banks comprehend FinTech as a threat, countless banks see it as an opportunity and have found strategies to interrelate with the newcomers so as to elevate their products and services, their innovative culture and the ease to reach the new demands of customers.

In Portugal, the scenario is still delayed, mostly due to a slower development of the customer towards digital, resulting from a high penetration of ATM and a more risk-averse attitude concerning innovation. Notwithstanding, a shift in the market is already observable, with increased numbers of digital banking users every year, having reached 28% penetration in 2015 (Statista, 2015). Expecting the disintermediation and disruption of the traditional banking industry even in Portugal, banks aspire to re-think their business models and therefore avoid losing customers to new companies in the market. Simplicity, convenience, transparency and cost saving are now the main value-drivers and an imperative concern for banks.

1.3 Millennium's situation

Currently Mbcp operates more than 1,300 branches with 17,600 employees internationally, with a prominent position in Poland, Switzerland, Angola, Mozambique and also Macau (Mbcp AR, 2015, - see appendix 1). As mentioned, it has the largest market share in Portuguese private banking, with approximately 18% in loans and deposits (Mbcp AR, 2015), closely followed by Santander Totta, with 14,5% (Santander, 2015). With a market capitalization of \$5,7 billion, it is listed as number 1439 in the Forbes Global 2000 largest companies list (Forbes, 2015). Mbcp's total number of clients amounts 5,5 million, of which 2,324 million in Portugal (Mbcp AR, 2015). Among Portuguese customers, the channel distribution is as follows: 34% branches, 4% telephone, 26% digital and 63% ATM. This allocation is in line with the country average, although distinct from worldwide average, especially lagging in digital (Finalta, 2015).

In a post-crisis setting, and after 4 years of losses, Mbcp achieved in 2015 a positive net income of €235 million, emerging from net operating revenues of €2,504 million, operating costs of €1,107 million and cost of risk of 150 basis points, backed by a bolster in capital and

liquidity ratios (Mbcp AR, 2015/2014/2013). This puts in evidence the strategic shift from recovery to growth, mainly through redefined distribution channels, leveraged on digital and process automation.

1.4 Business project challenge

Mbcp has been, throughout the years, a synonym of innovation and dynamism, being an industry disruptor itself, conveying innovation and modernization in their product and service offerings to best serve their customers. Withal, in the past few years, mostly after the global financial crisis, the bank has tainted in many dimensions from an early adopter to a “wait-and-see” nature. This arose from the continuous years of losses and needed governmental intervention, that restrained the bank’s investment decisions, shortened budgets in several departments and closely scrutinized banks possibilities, hindering any risk-taking attitude. Moreover, in the Portuguese banking scenario, certain traditional players have started shifting their business to a more internet-based approach and new players have appeared, both novelty banks that are completely digital and FinTechs.

That being said, Mbcp, foreseeing the future disruptions and with the outstanding debt repayment deadline getting closer, has increasingly aligned its strategic direction into growing the bank, regaining its innovative focus, and maintaining its position as market leader in different segments. Wanting to take the most advantages of digital technologies and having in consideration that FinTechs are a growing reality that cannot be dismissed, the bank recognized that constituting a strategy to deal with these companies was indispensable. Built as a follow up to the digital and innovative focus of the bank, the strategy ought to ultimately increase customers’ value.

2. The Business Project

2.1 Problem definition

Taking into consideration that FinTechs are new players in the market that are offering innovative services at high speed of transformation, being agile and technology centered, the bank wants to assure it does not miss opportunities to increase their customers value through them, and that its position is not threaten by the newcomers. Mbcp's central question for this project was, therefore: How can the bank address FinTech start-ups in order to increase customers' value?

After thorough research, mainly within other banks best practices, 6 main forms of interaction between banks and FinTechs were identified: Mergers and Acquisitions (M&A), meaning the combination of 2 companies or purchase of one by other, in this case banks acquiring FinTechs would be the most common practice; Partnerships, which comprises resources, assets, or profits and liabilities sharing between two or more players, depending on the arrangement – the benchmark in the market is for FinTechs to share their products while banks provide access to customers and capital; Venture Capital (VC), or in other words, making money available to start-ups with high growth potential, taking a stake in their business and grasping knowledge on their unique characteristics; Incubators and Accelerators, which involves the support of early-stage start-ups through capital and mentoring – incubators focus on helping start-ups to develop an idea from scratch whereas accelerators typically just give the extra push to grow an already established venture; Research Centers (RC), comprising investigation units in the FinTech industry, its trends and added value for customers, to better incorporate changes and predict disruptions in the market; and lastly Product Development (PD), in which banks identify which products are gaining traction in the market and then build them internally through acquired

know-how and expertise. In appendix 2 a split of interaction strategies between banks and Fintechs is shown. For the project, PD was considered as out of scope, as it does not imply a direct interaction with FinTechs, and further, it is consequential to any of the other approaches and therefore not independent. Furthermore, incubation was similarly dismissed due to a miss-fit with the bank's central objective of knowledge gathering, as there is no direct investment in the start-ups that may thereafter not fully share information regarding their business model. Yet, accelerators were still considered relevant and were kept as part of the analysis.

The central problem was hence, to define which strategy was the most adequate, considering the internal constraints and external environment of the bank, in order to bring the best cost/benefit relation. However, during the progression of the project another central setback was identified, preceding the possibility to develop an approach to FinTechs : when analyzing the requirements for each strategy and once the internal examination was completed, it became clear that there was a gap in some key requirements, transversal to any suggested future course of action. In the center of the readiness of the bank lays a strong digital strategy, which was in Mbcp evaluated as somehow bewildering and underdeveloped. The 3 foundation pillars identified as central mainstays for the development of a solid digital strategy were then: Human capital, Information Technology (IT) and Governance. Ergo, instigating particular transformative initiatives to foster the bank's readiness for a FinTech strategy became a priority for the successful advancement of the project.

2.2 Hypotheses

For the selection of the most suitable approach for the bank to tackle FinTech, several hypotheses were developed, which were then divided in sub-hypotheses to ensure a far-reaching

breakdown. For the general hypotheses, each of the 5 strategies here denoted as S_x [$x = \{1, \dots, 5\}$] were pondered and then tested as follows:

$H_0: S_x$ is the right approach to tackle FinTech

as the null hypothesis, where the alternative hypothesis is then:

$H_1: S_x$ is not the right approach to tackle FinTech

To make a valid inference on which strategy would be possible and beneficial, the team tried to find evidence against its implementation. In other words, if there would be any contradictory indication to the enactment of such scheme, the hypothesis would be rejected.

In order to evaluate different requirements and/or sub-types of interaction for each of the null hypotheses, sub-hypotheses were defined thusly:

M&A - Sub-hypothesis 1: Absorption integration is the most beneficial for Mbc; Sub-hypothesis 2: Mbc has the IT capabilities to acquire FinTechs; and Sub-hypothesis 3: Mbc has the financial resources to acquire FinTechs.

Partnerships - Sub-hypothesis 1: Partnerships allow Mbc to broaden its customer base; and Sub-hypothesis 2: Partnering is a viable option to ease the proximity among Mbc and game-changing technologies.

VC - Sub-hypothesis 1: A VC fund's independence from Mbc grants the best access to FinTechs; Sub-hypothesis 2: An independent VC fund sets the focus on the right strategic positioning; and Sub-hypothesis 3: An independent venture capital fund is a very efficient way of engaging with FinTech.

Accelerators - Sub-hypothesis 1: Accelerators effectively bring Mbc up to date with market development; Sub-hypothesis 2: Mbc has the right brand to develop an accelerator; and Sub-hypothesis 3: Mbc has the capabilities to optimally support the most promising start-ups.

RC – Sub-hypothesis 1: A formal research center should be implemented in Mbcp as a separate unit; and Sub-hypothesis 2: Mbcp should foster research through a collaborative research platform.

2.4 Analysis

The internal analysis of the bank, done through different frameworks, which are further explained in the methodology section, revealed essentially that there is a gap in strategic direction to digital transformation within the bank. Further, it was observable that although Mbcp's capabilities are valuable and some rare, they are easily imitable and replaceable, which is a threat for the bank to sustain its competitive positioning. The bank displays a strong brand and several sturdy digital tools, nevertheless it is slow to market due to an inexact digital strategy, an inefficient IT department and an old legacy system. The combined analysis also revealed other major issues such as: mindset misalignment with digital transformation on a large number of employees; financial constraints from government restrictions; lack of strategic focus in digital (mainly in the strategic directive "Projecto Avançar"); and absence of a structure for innovation within the bank. To tackle some of these concerns, Stage 0 is proposed, in the following recommendations section.

The analysis of each hypothesis stood as follows:

M&A – Banks' acquisition or complete integration with FinTechs is a very fast way to tap into this new disrupted market, immediately enhancing the product portfolio and allowing access to the start-ups exclusive knowledge. Bearing this in mind, the valuable resources of a FinTech become available for the acquiring bank straightaway, becoming exclusive property. However, since FinTechs have such a characteristic mindset and culture, merging it with a stricter and more regulated institution like a bank carries the hazard of lost of entity. Likewise, also the agility and

fast pace of FinTechs innovation streams may be constrained after integration, as they would be operating under banks regulations from that moment, losing a substantial share of their distinctiveness. On top of that acquiring a FinTech involves a very high capital commitment that may even be overvalued in the market. To finalize, in order to ensure a successful integration after M&A procedures, the IT systems need to be extremely responsive, so as to ensure the smooth assimilation of distinct organizations.

Partnerships – At a first glance, partnerships immediately call attention for analysis since this strategy accounts for 1/3 of all bank/FinTech interaction options, namely by pertinent players in the banking industry. This approach has several benefits, namely sharing unique capabilities and competitive advantages between entities. In this case, partnering with FinTechs would allow banks to provide their customers game-changing technologic products, while gaining knowledge on FinTechs' business models. This in turn would allow targeting a broader customer base, as more segments could be under the bank plus the FinTech partner's umbrella. In addition to that, as FinTechs are not subject to such strict regulations, it would allow the bank to benefit from extra agility and dexterity to implement disruption. However, several other factors have to be considered, namely information sharing. This becomes a major setback upon the occurrence of a partnership, as it is target of strict legislation and highly controlled by the banking authorities. Besides, having 2 completely distinctive companies in terms of structure and mindset operating as partners, may lead to culture shocks that hinder any partnering benefits.

VC – Providing funds to early stage FinTechs in return for an equity stake was spotted as a growing trend internationally, and many banks have been implementing VC funding dedicated solely to FinTech start-ups. These can be integrated within a corporation or created as a separate entity with own management, verified in the sub-hypotheses. It was deliberated that VC allows a very efficient access to know-how and insights into FinTechs' business models, as the bank could

achieve a direct participation on the board of the investees. This strategy also promises large long-term returns for the bank in the case of successful companies that are grown through the VC. Nevertheless, it encompasses the risks of investing in FinTechs that later flop; there may not exist a relevant market for VC funding of FinTechs in Portugal; and finally a conflict of interests between the bank and invested FinTechs may surge.

Accelerators – The main considerations in this approach had to do with the bank’s capabilities to implement an accelerator and its impact in gaining knowledge about the FinTech market. In fact, it was possible to infer that accelerators are an efficient way to develop new business ideas and concepts. In Portugal, there is market to implement an accelerator program. Accelerating start-ups would have the benefit of exposing the bank to new products and services, but mostly to a more open and entrepreneurial spirit – therefore bringing the right exposure and boosting the knowledge absorption process. Though, some risks lay in the lack of evidence on post acceleration period success, especially if there are no equity stakes that provide the bank sufficient decisive power. The existence of enough FinTechs in the Portuguese market to justify the accelerator’s costs also arose as a major doubt. Impending from the benchmark analysis, most banks using this strategy partner with a third-party accelerator, simplifying largely the process and still reaching comparable benefits.

RC – Since 2 main types of RCs were identified, traditional and collaborative, it was determinant to understand which, if any, best suited Mbc’s objective, translated into the sub-hypotheses. Although several benefits were identified, such as gaining full knowledge and understanding of market trends and technology, as well as improvement of staff’s mindset towards digital and the bank’s image as digital-centric, this strategy was seen as very dawdling and time-consuming. Moreover, the risk of not gaining full access into the FinTechs uniqueness is high. Implementing a RC takes full involvement of employees and ability to disseminate the outcomes through all

departments to guide decision and align direction. Looking to other bank's practices, RCs appear as a complement to other strategies and more as a marketing tool.

2.3 Methodology

As previously mentioned, the project was divided in 2 main stages, each of them encompassing different methodologies. These were the FinTech readiness and the FinTech approach, accordingly. For the first one, the analysis of current state and capabilities of Mbcp was executed mainly through individual face-to-face interviews with employees from different departments inside the institution. This followed a semi-structured guide, meaning that some key questions and topics were strictly covered, still, when appropriate the interview followed topical trajectories. To complete, the team also accessed internal information from the bank, namely the intranet area, surveys, statistics and other relevant numbers, which were presented in confidentiality. The interviews were then transcribed and delved to highlight the main conceptions gathered.

The overall internal analysis was summarized in a 7-S Model, original authorship of McKinsey, which stresses the internal situation of an organization, assessing its status and monitoring changes. The factors that are considered relevant for an organization's success, if aligned, are: Skills, Strategy, Structure, Systems, Staff, and Style, around the central matter of Shared value. Having scanned each of the components, it was possible to better understand the company's position and their readiness to achieve the proposed goals. Furthermore, the VRIN standard was used to evaluate Mbcp's current resources and capabilities in terms of being valuable, rare, inimitable and non-substitutable, to appraise their competitive standing. Finally, the SWOT tool concluded the internal analysis, highlighting Mbcp's key strengths and weaknesses together with market opportunities and threats.

So as to develop the FinTech strategy, secondary data was used to delineate the possible options for the bank. This came mainly from major consultancy companies' reports on the topic, in addition to other national and international banks' practices scrutiny. After identifying the 5 applicable approaches, the respective benefits, risks, requirements and costs were outlined, also using secondary data from the same sources. This was complemented by an industry analysis, which included a Porter's 5-forces model to evaluate the rivalry degree. At this stage, the team immediately cross-analyzed the different strategies and the minimum requirements' dearth was identified through a Venn diagram, interposing with the internal analysis in parallel.

Subsequently, for the first stage a 6-axes model was built, to specify the current status and the desired standing for specific subjects, serving simultaneously as a monitoring tool for the bank. The axes were defined based on the identified foundation pillars: Mindset, Digital presence, IT, Know-How, Governance, and Strategic positioning. These were then evaluated on a scale of 1 to 10 in collaboration with the Business advisor for the current state, and the anticipated need for each was expressed based on benchmarking and external analysis. Following the use of this model, the project progression was grounded on the assumption that Stage 0 was completed, and hereafter, the bank had the required scores for each mentioned category.

To conjecture the best approach to relate with FinTechs, the procedure was to define the hypotheses and sub-hypotheses mentioned previously. These were then tested, having into consideration the requirements and the capabilities of the bank. The rejection of hypotheses happened when 1 or more of the following occurred: the implementation costs were too high; execution time and hence time to market was too slow; benefits were not in line with augmenting customers' value; access to FinTechs unique knowledge was limited; potential cultural shocks between the 2 entities potentially hindered the relation; and having a lower cost/benefit relation in linear comparison to other hypothesis.

2.5 Recommendations

The main recommendations for the bank were divided in 2 main phases, as revealed before: Stage 0 – FinTech readiness; and Stage 1 – FinTech approach.

For the first stage, it is recommended that the company achieves some level of transformation in key areas that are ground prerequisites to allow a FinTech strategy implementation, according to the defined 6-axes model (see appendix 3), as follows (note that current evaluation and desired state is presented in parenthesis in the form of [x→y]):

Mindset – Crucial for the digitalization process and openness to innovation throughout the bank, should be transformed in all hierarchical levels, starting from top management and ensuring its diffusion in the whole institution. In addition, a solid foundation for innovation should be well thought out - [5→8];

Digital presence – In the center of the technologic transformation is the digital presence of the bank in order to manage customer relations, market relevant segments, and sustain Mbcp's credibility as a digital-centric bank. This too contributes to the lure of FinTechs to the bank to develop any kind of strategy. Some of the changes needed lay in the web and social media presence, that should be grounded in a comprehensive online media plan – [4→7];

IT – All digital transformations and potential FinTech approaches rest in technology, requiring an IT system that is agile and sufficiently capable to process innovation in an efficient way – [5→8];

Know-How – To support any relationship with the FinTech market, the bank's employees should have a holistic understanding of terms, technologies and trends. This should emanate from high-level executives and continuously monitored to respond to the fast changing pace – [6→8];

Governance – To efficaciously process and release to market the innovations brought by a FinTech approach, flexibility and high processing speed is required. This comes mostly from centralizing the digital, while ensuring cross-functional input – [4→7];

Positioning – It is essential to define a digital and customer-centric vision that is common to all units in the bank, certifying aligned decision making – [4→7].

Considering that Stage 0 is successfully accomplished, a FinTech strategy is recommended based on the verified hypotheses: implementing a VC fund and an external Accelerator. These 2 were corroborated in the basis of matching MbcP's capabilities, providing the best cost/benefit relation towards the end goal of improving customers' value.

VC – The team reached the conclusion that implementing an independent VC fund would be the most suitable approach, as it allows deep knowledge into the business models of FinTechs, creates a trust relationship with the investee and brings the right strategic positioning, focused on improving customers' value. The suggestion is to set it up as an independent entity, to ensure the right focus and to gain agility, contouring some bureaucratic and regulatory hurdles.

For the VC implementation several steps should be followed. Firstly, the bank should certify a proper team set-up, with deep knowledge and understanding of the FinTech market, to take the right investment decisions. This should be accompanied by the initial setting of financials, considering the capabilities of the bank. Subsequently, the portfolio of future investments should be planned in such way that diversification is guaranteed. At this stage it is also of major relevance to build up guidelines and a value creation plan to guide the whole funding process. Lastly, it is vital that communication channels between the bank, the VC, general partners and the corporate accelerator are defined to ensure the success of VC in accomplishing the bank's objectives.

Corporate accelerator – Partnering with accelerators to grown early stage FinTechs guarantees MbcP an immediate access to knowledge and to grow the entrepreneurial spirit of the bank. Additionally, at the end of the acceleration period MbcP will be able to witness which companies are more disputed by investors, giving a sense of what are the most valuable market trends. The

bank's image as an innovative bank can be leveraged and sustained to attract FinTechs. Irrevocably, by using a third party accelerator, the bank can overcome the barrier of insufficient resources to independently support start-ups, without losing much on value-added. By partnering with a corporate accelerator the bank would even be further exposed in the innovation market and be in close contact with industry experts, further enhancing the FinTech Know-How. The accelerator should offer a bundle of services, including financial support, mentorship, assistance and exposure in the start-up environment.

As for the implementation steps, the team recommends Mbcp, in partnership with the corporate accelerator, to build awareness for the acceleration program prior to launch. This can be achieved not only by building a community within both the institutions' network, but also by inviting the early stage FinTechs for seminars. This will of course be done after a careful selection of the corporate accelerator partner that should be aligned with Mbcp's overall objectives and values. Concurrently, a managing team within the bank should be selected, to control the relationship with the partner, and the financials should be settled, namely planning and budgeting. Following this, it is crucial to safeguard a proper portfolio of companies, similarly to the VC fund. This can be achieved by attracting the right start-ups, i.e. in relevant events, and by having a comprehensive selection process. Building a marketing plan is also vital for the success of the accelerator and should be created upon the usage of the right communication channels (such as web and social media), for coherence purposes. In line with the implementation of the VC fund, configuring communication is of foremost importance.

Both these strategies will allow Mbcp to build ground knowledge in the FinTech market, exposing it to product and service innovations, new business models and to the start-up's unique culture. By ensuring synergies between both approaches, the bank will be capable of building a solid foundation for tackling the shifting market, assuring the gathered knowledge is embedded in

the value offering to their customers. Besides, it will also be groundwork for later actions, namely partnerships and acquisitions, eliminating the risk of adverse selection.

RC were rejected on a basis of a slow development process and by being replaceable either by VC or accelerators. Although partnerships could also be a relevant strategy, they were assessed as much riskier due to lack of knowledge and potential clashes.

2.6 Risks

After a detailed review of the proposed strategy, the main risks of each strategy' implementation were also identified.

VC – One of the highest risks of implementing a VC fund is investing in the wrong FinTechs. From a financial perspective there is obviously the risk of flop, but most importantly, if the FinTech is not aligned with the bank's strategy and positioning, the knowledge transfer benefits may be hindered. Adding to that, there is the risk of information asymmetry that can also deter full access to the FinTechs' Know-How. By setting up an independent fund, lack of involvement from the bank's management may lead to a poor understanding of the FinTechs' concepts and hence not fulfilling the objective of knowledge grabbing. Finally, the VC fund will require capital availability that may cause financial distress after just having repaid the government outstanding debt, impeding other prioritized investments.

Accelerator – Building up an accelerator requires costs that may not provide returns of any kind in the future. In the case of poor access to knowledge, the accelerator will become only a cost center and all benefits bewildered. This is strictly related to the problem of adverse selection, as FinTechs that have a feasible and promising business model will usually put efforts into fund-raising rather than mentorship. The knowledge transfer is also riskier by using a third party accelerator that may lead the bank to isolation from the whole process and therefore miss out the

major benefits of the relation. To conclude, management apathy also may also jeopardize the relation with the third party accelerator. In the event of no engagement from the bank's side, it may be considered more as an investor rather than partner.

2.7 Individual contribution

Throughout the project execution, responsibilities were distributed among team members. My main contributions during the research phase were the market and customer analysis. Here I performed a deep analysis on Mbcp's internal information, namely the Finalta study (2015), to better understand the current customers' profile and characteristics. This was completed by a deep analysis of secondary data to understand customer trends, and ultimately why are FinTechs and its attributes gaining popularity among different segments. This led to a profiling of digital and FinTech users, fostering the identification of growth opportunities for Mbcp. Hand-in-hand, the European and especially Portuguese market for FinTechs was investigated, through key indicators such as banking channels penetration levels, FinTech and alternative finance usage, etc. This allowed a full understanding of the current standing and expected changes in the near future.

For the strategy elaboration I developed most initiatives in the topic of know-how and digital presence, while also contributing, in a less extent, in the other axes. For the FinTech approach I explored the viability of implementing a Research Centre, performing a benchmark analysis and testing the hypotheses against all the available information and the internal analysis. In this task I was able to recognized 2 different types of research centers, highlighting key benefits and risks of each. However, after a careful comparison with other options, it was concluded to be less beneficial, and hence, disregarded.

Finally I also contributed prominently, in a more bureaucratic perspective, in interview summaries, slide design and all English revision, as a native speaker. Overall, having a structured methodology of work, I was able to maintain objectivity in meetings, allowing the group to be focused on-topic, whenever discussing was getting out of the expected focus.

3. Academic discussion

3.1 Disruptive Innovation

Disruptive Innovation is defined as the process of completely changing a market or commencing a new one, by introducing technologies that shift product and/or services' characteristics dramatically, often affecting processes and operations in such way that a complete new paradigm is put in place (Bower and Christensen 1995, Kostoff et al. 2003, Yu and Hang 2010). Examples of disruptive innovations in different industries mentioned by Charitou and Markides (2003) were: online distribution in general retailing; electronic communication networks in stock exchanges; low cost point-to-point airline services; direct banking through telephone and PC in the banking industry; among many other instances. These had in common the introduction of a groundbreaking way of competing in their respective markets, underlining different product attributes, and usually starting as minor and low-margin corporations (Charitou and Markides 2003). It is true that most disruptive innovation comes from industry outsiders, typically small firms that explore niche and emerging segments, while established companies are usually putting their efforts in maintaining their current sure business, not wanting to "risk an uncertain future" (Markides 1998).

This is strictly related to the Innovators' Dilemma, a concept initially developed by Christensen in 1997, where the author tried to understand the reasons why leading companies were failing to triumph in their industries, whenever new technologies shifted the market. According to Christensen (1997), established companies focus their efforts in meeting their current customers' needs and demands, investing aggressively in product performance improvement – which in theory should be the right management practice. However, the paradox arises from the fact that disruptive technologies start off as emergent concepts that are rejected by the "mainstream customer", only valued by niche segments and therefore, neglected by senior

executives that want to move close to their core customer satisfaction. Adding to that, disruptive technologies are usually hard to predict in the long-term, becoming extremely risky and unattractive for established firms, from a financial perspective (Bower and Christensen 1995).

Although there is no single right way for established companies to respond to disruptive innovation by new players, the answer will depend mostly on motivation and ability. Common responses that may or may have not been successful in the past, as revealed in Charitou and Markides study (2003), have been: focusing and investing in the traditional business, based on the assumption that most disruptive technologies never take up the entire traditional business; ignoring the innovation, viewing it as a distinct business with different customers and players; attacking back, offering new upgraded products based on the recently valued attributes to their already established and loyal customer base; adopting the innovation, maintaining the traditional business and adding the new one, commonly through a separate unit; and lastly some companies have embraced the innovation entirely, forsaking their whole traditional business by scaling up the new model. There are indeed cases where established firms have triumphed in the context of Disruptive Innovation, as mentioned by Markides (1998), nonetheless this demands companies to have a forward vision, overcoming the inertia of success by continuously challenging the way they do business, with a questioning outlook. This may not always be easy to achieve in very traditional industries such as banking, as it will be demonstrated later on.

Some criticism to the theory of Disruptive Innovation has also been mentioned, namely by Jill Lepore (2014)¹, which stated it as *“a theory of history founded on a profound anxiety about financial collapse, an apocalyptic fear of global devastation, and shaky evidence”*, questioning the true need of disruptive innovation and the consideration of it as an inevitable move.

¹ The New Yorker. 2014. Jill Lepore. <http://www.newyorker.com/magazine/2014/06/23/the-disruption-machine> (accessed May 15, 2016)

3.2 FinTech as a Disruptive Innovation in Banking

To establish a link between the developed Business Project and the theory of Disruptive Innovation, it is important to clarify how FinTech is evaluated and cultivated as a disruption in the banking industry. In accordance to Bower and Christensen's method (1995), firstly it should be enquired if the technology is in fact disruptive or sustaining. FinTech start-ups are emerging in the financial services' market by offering alternatives in payment systems, business and consumer finance, and insurance, all through digital tools that are now faster, cheaper, simpler, more convenient and accessible, and with higher degree of personalization than ever before. The potential shift in paradigm of banking to a complete remote, self-managed and personal system dominated by new market players is, in true, the needed evidence to prove that FinTechs are disruptive innovations (Kostoff et al. 2003). In Mbcp it was even possible to observe a divergent opinion on the need to support or deal with FinTechs within the bank, with the marketing and risk office considering it a long-term concern while other departments such as Internet and Mobile saw it as an urgency – witnessing these disagreements, mainly fostered by the difference in incentives, corroborate the level of disruption of the technology, as defended by Bower and Christensen (1995). The second important step cited by the authors, is the definition of the strategic importance of the innovation – which in this case is high. This may be inferred, as FinTech undeniably has a very steep projected performance trajectory. Although full replacement of traditional banking is not expected in any near future, it might be the case to dominate certain segments and product offers.

In order not to have their businesses harmed by this trajectory, especially in Portugal, banks need to comprehend that the “branch customer”, which is the mainstream customer, is currently pushing banks to improve their offering through the channels they are familiar with – mostly branches and ATM's. However, the emerging FinTechs that are now targeting only niche

segments are simultaneously growing and developing, and once the benefits are realized by the mainstream customer, the growth rate of FinTechs may already be too fast for banks to respond, leading the pioneers in the new technologies to dominate (Bower and Christensen, 1995).

3.3 Managing Disruptive Innovation in Banking

Having understood that FinTechs are indeed a disruptive force in the market, how can banks manage it? In truth, during the course of the project, it was possible to understand some major challenges in the process of managing innovation, which are specific for the banking industry. This is a traditional risk-averse industry by itself, but aggravating this factor is the extremely strict regulatory environment that surrounds it, many times constraining the processing of innovation. Even if banks spot innovation and try to develop new technological products on their own, the speed to market and the agility to do so is immediately constrained by regulatory issues, which are external to the banks capabilities. Some additional inhibitors identified were the lack of mindset and knowledge gap by managers and employees, which in banking is commonly led by cultural inertia, risk-averse attitudes and fear of losing current standing. Furthermore, Mbcp, but also major banks worldwide, has been slowly recovering from a post-crisis period that further restrained investment capabilities. This, in turn, makes incumbents focus all resources in maintaining the conventional business rather than betting on new markets. Also the large size of banking organizations and the complexity of their governing processes are negatively correlated to disruptive innovation (Yu and Hang, 2009).

Actually, banks fall in the 3 traps that inhibit breakthrough innovations, mentioned by Ahuda and Lampert (2001): The familiarity trap, by focusing in the business areas where experience and competence is already attained; the mature trap, by using technologies that are comprehended and understood by all players, including customers; and the propinquity trap, representing the common practice of banks to find solutions in “neighboring areas of existing

solutions” (a concrete example that represent the 3 traps would be Mbcp’s development of the branch of the future to reach new segments – the banks is familiar with the concept of branches, this solution is known and has worked so far with all people involved, and finally it is still based in the concept of branch, with just slight upgrades).

To overcome these challenges it is crucial that entrepreneurial opportunity is fostered through discovery and opportunity (Hang et al. 2014). Especially in banking, it is crucial that disruption is managed through an independent organization (Bower and Christensen, 1995), as the financials of new technologies may not be attractive, blurring internal management vision and leading them to disregard it. For disruptive technologies it is important to roadmap the development of each alternative scenario, highlighting relevant future actions (Kostoff et al. 2003) in order for the bank not to be caught by surprise. Finally, it is fundamental to oversee strategic health, that may not always be positively correlated with financial health (Markides 1998) and continuously question and adapt it.

3.4 Future research

If fostering and managing disruptive innovation is considered a challenge in established organizations, mostly due to the innovator’s dilemma as mentioned, this becomes increasingly harder in the close, traditional, regulated and risk-averse industry of banks. While some research as tackled this problem for large established organizations, providing some insights on how to foster strategic innovation, many of these suggestions are inapplicable in the case of banking. Therefore, studying disruptive innovation in banking as well as the influence of the context and environment in managing innovative technologies should be pursued in future studies, to better comprehend the topic. Moreover, analyses on the best way to monitor and/or generate innovation in banking would acutely enrich the state of the art of research in the field.

4. Personal reflection

The elaboration of the Business Project, revealed to be a very enriching experience in numerous perspectives. Besides the unequivocal improvement in knowledge in the topic of study, it was the utmost example of teamwork and personal growth.

Throughout the Business Project development, I was able to bring my observant mind, structured thoughts and objective organization as strengths. This allowed putting discussion into perspective, while reflecting on all suggested theories. By managing disordered contributions by my team members, I was able to integrate and moderate discussions into solid and coherent lines of thought. In addition, my calm way of dealing with unexpected flows and difficult phases also contributed to a smoother development of the entire project. In these situations I tried to take a step back and getting the team to stay motivated, while finding new ways of proceeding. In contrast, excess perfectionism revealed to be a weakness, as it could sometimes be interpreted as intrusive and unnecessary. Adding to that, by spending too much time reflecting and pondering the best courses of action, I sometimes delayed the decision-making process within the team, in the pursue of the “right answer”.

Overall the teamwork experience was extremely valuable, especially in terms of cultural awareness. In fact, in a multicultural team, I learnt how different nationalities could bring up such different mindsets. After the initial adaptation period where the team members realized each other’s strengths, it was curious to observe how naturally each ones contributions’ would added up to the others, finalizing in a consistent result. Also of great added value, on a personal perspective, was the project management approach that will be valuable throughout all my academic and professional life in the future. Planning, scheduling, researching, monitoring, among other errands, were just examples of reference tasks in which I gained expertise through the project development.

Taking into consideration the weaknesses that emerged during the project, I should train myself for faster processing of information and “letting go” of some details that sometimes are not a priority. To better achieve this, nothing better than fostering my quick thinking, such as through brainstorm sessions or other fast-paced information flows.

To conclude, if I looked back to the project progress, I would just change one thing. At the beginning, the team decided not to have a single team leader, or in other words, organizer. This person would be in charge of keeping track of schedules, pushing group members to meet deadlines and compile all work done. Although the initial idea was to maintain a more self-governing approach, in some occasions there was confusion with dates and deliveries, that could have been easily avoided, had this person been appointed.

Rather than that, the project really provided a close “real-life” approach to a consulting project, enhancing my capability of researching, analyzing, presenting and delivering results in a professional and consistent manner.

6. Appendices

Appendix 1

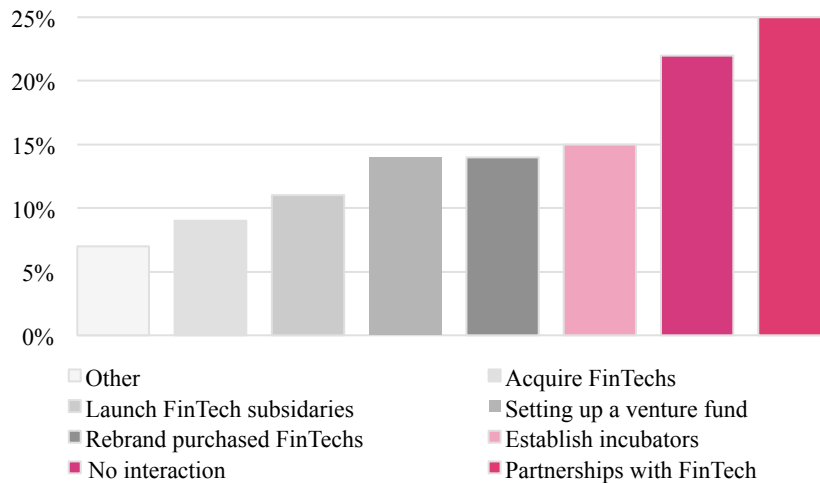
	Portugal	Poland	Angola	Mozambique
Market share				
Loans	18,1%	4,6%	3,8%	28,8%
Deposits	17,5%	5,2%	4,1%	28,6%
Total assets	53,647	15,534	2,344	2,355
Employees	7,459	5,911	1,225	2,505
Branches	671	411	90	169

*In Switzerland operations are based in a private banking platform with personalized services to the Group's high net worth Customers and hence there is only one branch

**In Macau the bank operates through one full licensed on-shore branch
(Mbcp AR, 2015)

Appendix 2

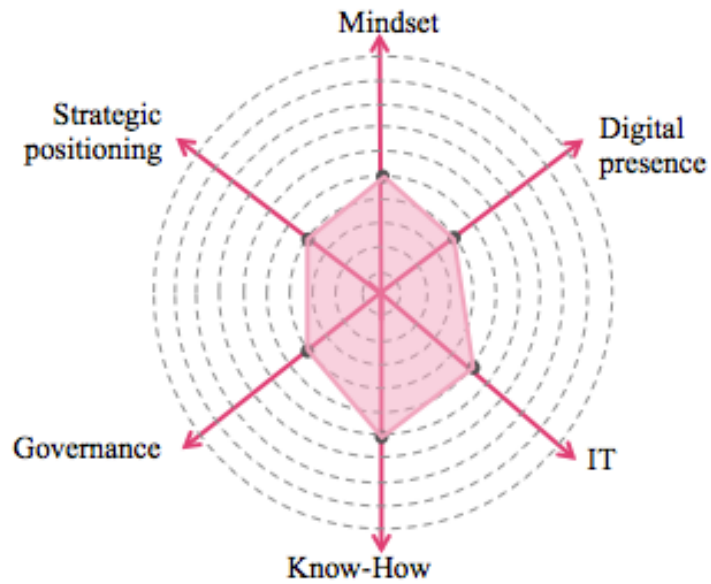
Current way of banks dealing with FinTechs



(PwC 2016)

Appendix 3

The 6-axes model – Current state



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