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Office of the Vice Provost for Advances in Learning



MODULE 6 UNIT 3

Video 1 Transcript

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CHRISTOPHER MALLOY: How do you regulate something that's never existed? That's a classic question that technology industries have faced for many years. And now this war between government regulators, incumbents, and startups is forefront in the future of FinTech. And in this module we've been grappling with that, and trying to understand what's the right path for government regulation? And how should these FinTech startups and incumbents respond to this situation?

So on this issue of government regulation, the question is, "When is the government going to crack down and when is it not?" And obviously in China, there's been lots of crackdowns recently. Another case that's been quite interesting here in the US, is this Madden versus Midland case. Which is a case that we've discussed, where the government is coming in and potentially regulating FinTech lenders, and saying that they can't charge above a certain interest rate.

LAUREN COHEN: Yeah

MALLOY: And the stated goal of that is, of course, to get rid of what's called predatory lending, and help, you know, consumers from getting ripped off. And the question is, is FinTech ripping off these consumers or not? I mean you could make an argument that FinTech is coming in and helping the exact consumers that the government claims to be worried about.

COHEN: Yeah. And I mean, I think whenever you get into this government regulation issue too, then FinTech it—are they going to be able to find a way around this, right? And if they can't find a way around this, then do you have, like, tech on FinTech? Like FinTech squared? That's going to come in, and be able to figure out a way to do it? Right, somehow implant interest rates into people's minds or something, right? It's like they're—however much the government wants to regulate these things, it seems like there's always ways around these.

And so, it's going to be tough for the government to regulate things like bilateral transactions, right. If you and I agree that, "Okay, I'm going to lend you ten dollars at the beginning of the week, and you want to pay twenty at the end of the week," then of course that's a massive interest rate, right – that's over five thousand percent you're paying, an annualized rate. And yet, we might be happy to do that. Right? I may really use—you know, one of us will really need the money until the other is happy to do that, and we're both better off by making that transaction. So to the extent that the government comes in and tries to tamp down on these – could be not so great for the citizens.

MALLOY: Exactly, and you know, one argument that FinTech companies will make is that these markets don't exist, but they could exist at some price, and we're making consumers better off, and – by creating this enormous market – societies better off.

COHEN: Yeah. And so, then the question becomes, "Okay, who is most hurt by this regulation?" Right? The government comes in, and who does the government go after and who's the most hurt?

MALLOY: Exactly. So are they going to come after the big established players? Or are they going to crack down the new incumbents?



COHEN: Yes, and so look, if history has told us anything, it's that these government regulators – they have jobs too. Right, and so they want to prove that they're really doing a great job, and it's much more newsworthy to take down the big fish. Right? It's much more newsworthy. If you can take down that firm that everyone's heard of. And so, in that sense, incumbents almost have more innovative risk in this space, than a new small innovator.

MALLOY: I agree. They have large established brands and client bases, and to the extent that they don't want to put that at risk, you know, they may be less willing to dive into some of these markets, and perhaps that's why some of these Fintech companies have gotten market share in certain areas where the incumbents have been slow to enter, particularly in developed countries like the US.

COHEN: Yeah, because they're worried about this. But, then, you have this double-edged sword, right – if I'm late to enter into this market and—yeah—and there's some kind of brand equity that can be built up from a LendingClub, or a Prosper, or one of these other people, then by the time I want to get into it, it's too late.

There's a big first-mover advantage. Then, it's late if I want to come in as an incumbent. And then what do I do? Right? I can either try, and then compete late, or I try to partner with them, or try to buy them, and—

MALLOY: Exactly. And so this partnership angle is something that we've seen growing of late. Extent to which, you know, FinTech companies always want to build their own brand, and go public, and build a huge business, but now realizing that maybe it's in their best interest to partner. And of course, on the incumbent side, perhaps the same way. Like building all this expertise in-house is quite costly and difficult. Might just be easier to establish a partnership.

COHEN: Yeah. And so, I think, look, in some—you've seen this in other industries too, right? We've seen this in the biotech-farmer relationship, and how that's evolved over time. And that, now, much the innovation in that—in drugs, is been pushed down to biotech, and now large pharma companies – like a Merck or AstraZeneca – simply buy the biotechs later—

MALLOY: And have a marketing role.

COHEN: Yeah, you can imagine something similar being true here. So, in that sense, what is government regulation do? And what do we need to worry most about in the FinTech space with government regulation? Well, it might not be that it's going to massively impact the rate of innovation, and the technology that's developed, but it impacts who does the innovation.

MALLOY: Yeah, the composition of the innovation.

COHEN: Yeah, and so it may move it down to the smaller firms. And then it makes the larger firms have to be even more awake, right, even more attuned to what's going on, and nimble, so that they aren't passed by, by the time they want to partner with them.

So the most valuable capital that you have, it turns out, is your human capital. So we want you to answer that big question: Where do you want to bet your career? Do you bet your career on that innovative new FinTech startup that's going to change the world? Or with the incumbent firm, that's trying to get into this FinTech space?