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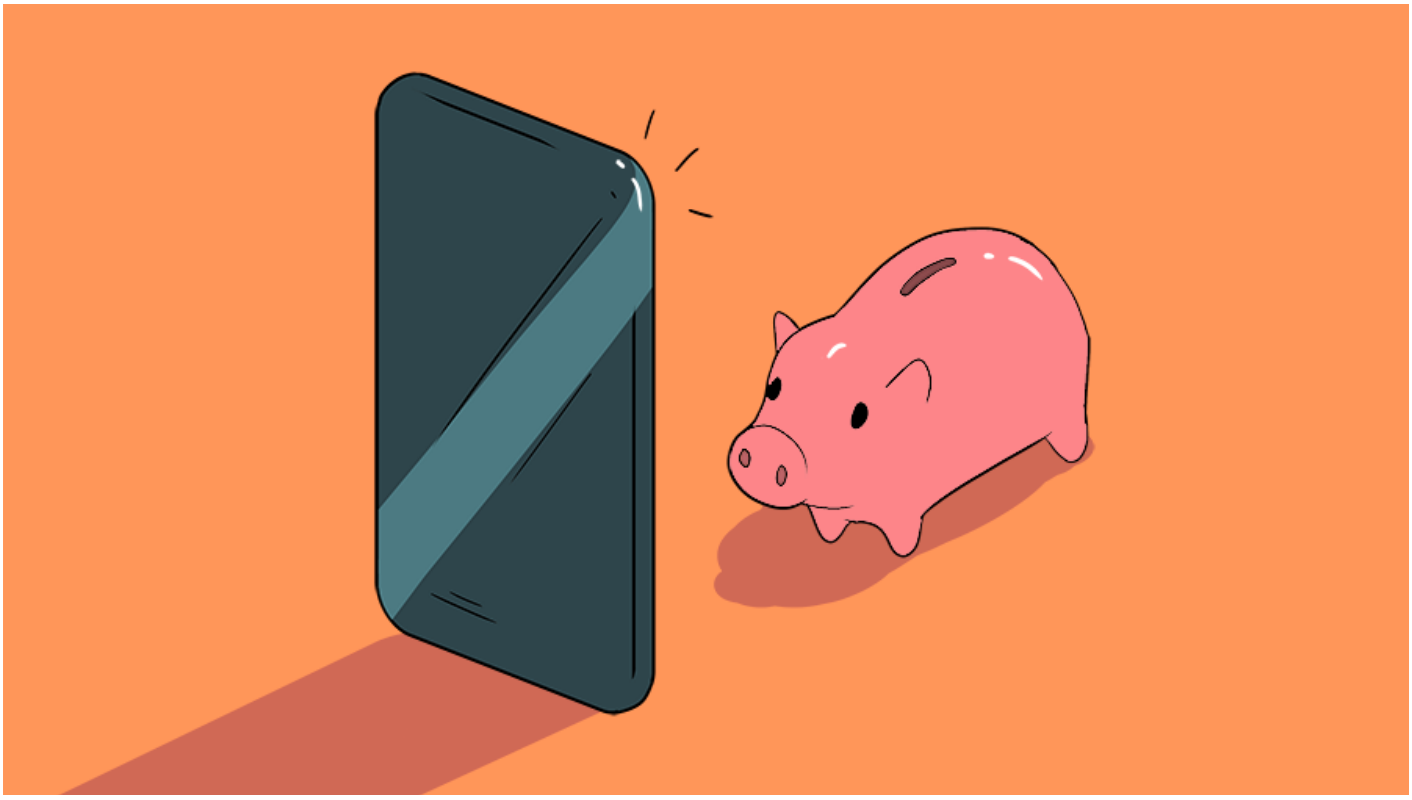
Why Is Every Startup A Bank These Days?

Alex Wilhelm, Natasha Mascarenhas October 30, 2019



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Neo banks (a fancy term to describe upstart digital banks working on everything from savings and checking accounts to mobile debit cards) focus on bringing banking services to users both underbanked and not.

But, notably, it's not just startups that started off life looking to build a neo bank who are building out banking-like

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services. In fact, so many startups are racing to offer banking tools that an early outline of this piece had to be amended to break the examples into several sections for the sake of bucketing and clarity.

In the coming weeks, we'll explore more deeply why the startup banking gold-rush is under way. Today we'll lay out the players and talk over the broad strokes of what's going on.

Recent News

News broke earlier this month that Chime, a well-known startup that we've covered before, is in the process of raising new capital at what Axios pegged as a "valuation north of $5 billion." The news wasn't too surprising. Chime has been on a tear lately, raising a $200 million round this March, and $70 million the preceding May.

A quarter-billion of venture capital in under a year isn't enough for Chime, which appears ready to take on more capital. It's a leading company in the neo banking rush, which, suddenly, is looking more and more like a crowded race as participants of all sorts join the fray.

Chime's success in terms of fundraising and valuation growth is a good indicator that it's doing something that investors covet. And as private investors value growth above all else, it's easy to guess that revenue expansion is what Chime is delivering.

Interchange, Part One

The sheer number of startup players moving into banking services is staggering. (You can see the players from this piece in a list here pro .)

Crunchbase News was tipped off about the boom last year when covering Acorns, a company that was initially focused on providing a savings service to users. Acorns moved into the banking space with a debit card in mid-2018, and at the same time, was hunting a $100 million round at a valuation of $700 million move, which we wrote about, too.

When we caught up with Acorns, CEO Noah Kerner cited the firm's debit card as a revenue source. And that brings us to interchange, a key method by which companies in the space make money.

Skipping all the technical talk, interchange fees effectively allow companies like Acorns and Chime to charge a small fee when one of their customers uses one of their debit cards. This makes offering a debit card (and constituent accounts) an attractive offering.

Of course, banks make a ton of money off interest rate spreads. But the quick and regular influx of revenue from interchange has helped attract outsized interest in becoming a bank. In short, lots of startups that started somewhere else in the world of finance have slowly come to circle more traditional banking services as a way to add growth to their businesses.

After all, why not expand into something that seems like a sure win?

Consumer Debit

The Acorns example is canonical in some ways, but also nearly too simple; the startup was already focused on a savings product, adding a way for its users to spend some of their money wasn't a hugely surprising move.

It also wasn't shocking that Wealthfront and Betterment, two early leaders in the robo-advising space are also launching checking and debit services. Wealthfront announced a high-yield savings account earlier in 2019 and promised a debit card later this year. Betterment also put together banking accounts and debit cards for its users this year.

But Robinhood moving into checking-styled accounts was a bit more of a stretch. The well-funded startup has launched cash management accounts and a debit card.

Venmo, the popular consumer-to-consumer money-transfer service? It added a debit card last year.

There are even more exotic examples. SoFi, a unicorn best known for student loan debt refinancing and its support of the Rams, announced SoFi Money earlier this year, a “new, hybrid account” that includes “debit card functionality” among other things.

Then there’s Uber, which recently created an “Uber Money” team. The group is working on an Uber debit card for drivers to manage real-time earnings and track spending and a re-launched Uber credit card for riders to gain points and rewards. The team will also roll out a digital wallet and connected bank accounts in the coming year, per a blog post from the company.

Interchange, Part Two

Let’s return to the engine powering all the news we just summarized, namely interchange revenue.

The New York Times noted that Chime made money off debit card interchange fees in 2018, saying that the company generates revenue “by collecting a fee from Visa every time its customers use [its] debit card to make a payment.” CNBC reported that Betterment was going to “profit off of part of the interchange fee charged when you swipe a debit card” in

2019. TechCrunch covered Robinhood's debit card earlier this month, noting that the firm "earns money by taking a chunk of the interchange fees from transactions on its debit card."

You get the picture. But there's even more activity than merely the consumer-oriented banking boom.

Corporate Revenue

Oftentimes, it's hard for startups, innately risky and volatile, to get a traditional bank to give them a loan. They just don't fit the bill. So, naturally, a slew of startups are rising to help with this pain point and become banks and check-writers as a result.

Let's start with the billboard in the room, Brex. The startup created a charge card for startups that otherwise wouldn't get money through traditional lending

Most recently, the San Francisco company has created a new offering to compete with traditional banks: cash. Brex Cash was created to minimize the expense and time of wiring money through a traditional bank. Intelligently, this is tapping into startups that its original Brex Card wouldn't fit well, namely small businesses that need to meet invoice charges, unexpected purchases, and salaries.

The last time we caught up with Henrique Dubugras, a co-founder of Brex, he said the company is looking to be a bank account replacement.

He also pointed to an anecdote: Scale.AI was able to grab money from Brex when it was only four people and at a seed round. Now it's a unicorn, surpassing $1 billion in valuation. (Brex itself is valued at $2.6 billion.)

Let's get back to listing examples. Beyond and before Brex come Stripe and Square. Stripe is best known for its work providing payment technology to digital companies. Square is best known for its work providing payment technology to IRL companies.

Each, however, are adding banking services to their product mix. Stripe, after adding lending services, is rolling out a corporate charge card. Square, in contrast, is launching a debit card for smaller companies.

Of course, it's not all interchange in the corporate world. Stripe and Square both offer lending and so forth. But it seems reasonably clear that the bug that has bitten the consumer-focused fintech and fin-services world has bitten its corporate-focused analog as well.

More To Come

We need to look more into the mechanics of the debit card boom, because like all booms, it will eventually oversaturate and lead to consolidation. But for now, it's all systems go on becoming a bank.

It's odd, though. Back in 2017, we bet folks would have expected crypto to have taken over this market by now.

Illustration: Li-Anne Dias

Tags acorns Chime fintech neo banking