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FROM CROWDFUNDING TO DIGITAL BANKING: THE EVOLUTION OF FUNDING SOCIETIES

When there is an opportunity, I try to grab it and make the best of it, because there aren't that many.

- Kelvin Teo, Group CEO, Funding Societies Pte Ltd

Despite the interval of a few months, Kelvin Teo felt like his company's most momentous milestone to date had just occurred yesterday. The Group CEO of peer-to-peer (P2P) lending platform Funding Societies Pte Ltd recalled that as late-night revellers were out singing "Auld Lang Syne" and toasting one another on New Year's Eve outside the pubs around the corner, he was taking a break at his office after a nerve-wracking sprint to the finishing line. Teo had completed the final negotiations with his proposed consortium partners for their Singapore digital wholesale bank licence application just days earlier. They had then rushed to submit their application to the Monetary Authority of Singapore (MAS) barely hours before the passing of the deadline – December 31, 2019.

That night, as Teo took a well-deserved breather, he cast his mind back to four years earlier when he had first set up Funding Societies with his then-MBA classmate Reynold Wijaya from Harvard Business School. Never in his wildest dreams would he have thought that the start-up would evolve to the point where he would be putting in an application for a digital banking licence. What is more, Funding Societies had formed a consortium with Xiaomi Corp, one of China's largest smartphone manufacturers; AMTD Group, a Hong Kong investment bank founded by billionaire Li Ka-shing's CK Hutchison Holdings Ltd; and Temasek Holdings-owned SP Group, which owned and operated Singapore's electricity and gas transmission and distribution networks, for the application. It certainly did not hurt that Xiaomi and AMTD were already running Airstar Bank, one of Hong Kong's eight virtual banks¹ which had just launched a pilot trial in end-March 2020.²

Of course, applying for the licence was one thing; obtaining the licence was another. Only three digital wholesale bank licences were available.³ Would his consortium be among the successful contenders? While there was no telling who would make the grade until MAS announced its decision, Teo was nonetheless fairly confident of his chances.

¹ These were essentially similar in nature to the digital banks that MAS was inviting licence applications for. However, the Hong Kong authorities had not made a distinction between full banks and wholesale banks for the territory's virtual banks, whereas MAS had made such a distinction for Singapore's digital banks.

² JD Alois, "Virtual Bank: Airstar Bank Launches Pilot in Hong Kong", Crowdfund Insider, March 30, 2020, <https://www.crowdfundinsider.com/2020/03/159546-virtual-bank-airstar-bank-launches-pilot-in-hong-kong/>, accessed April 2020.

³ "MAS to Issue up to Five Digital Bank Licences", Monetary Authority of Singapore (MAS) press release, June 28, 2019, on MAS website, <https://www.mas.gov.sg/news/media-releases/2019/mas-to-issue-up-to-five-digital-bank-licences>, accessed April 2020.

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Crowdfunding Sector in Singapore and the Region

Relative to more developed Western markets such as the US and the UK, which had started engaging in crowdfunding, particularly the lending-based form, a decade earlier, the Singapore market was generally regarded as small. Nevertheless, from a low base of US\$8.19 million in 2013, crowdfunding volumes in the city-state had soared to US\$190.62 million in 2017 (refer to **Exhibit 1**). The surge was partly due to the entry of new players since 2016 and SMEs becoming more open to adopting alternative financing solutions.

There were 19 licensed crowdfunding platforms in Singapore as at May 2019 (refer to **Exhibit 2**). The majority were lending-based while a few were equity-based, with some operating on a combination of both crowdfunding models.⁴

Within Southeast Asia, Singapore had emerged as the largest market by 2017, with Indonesia and the Philippines in second and third place respectively (refer to **Exhibit 3**). However, when compared against other markets in the larger Asia-Pacific region, Singapore was still behind regional rivals like Australia and South Korea (refer to **Exhibit 4**). The behemoth in the region was China, where crowdfunding volumes had reached US\$358.28 billion in 2017.

Funding Societies

Incorporated in Singapore in February 2015, Funding Societies had expanded its operations to Indonesia, where it was known as Modalku (“My Capital” in Bahasa), and Malaysia. In Singapore, it provided business financing of sums up to S\$2 million (US\$1.39 million⁵) to small and medium enterprises (SMEs), which often faced challenges on account of cash flow mismatch, extended payment terms from their clients,⁶ and project-based growth opportunities, but at the same time, struggled to obtain loans from banks and traditional financial institutions. Funding Societies obtained its funds for lending primarily through crowdfunding, in which lenders, including accredited and retail investors, could place investment amounts starting from as little as S\$20 (US\$13.9). It essentially matched these investors with the SME borrowers via its digital marketplace platform.

The P2P lending platform offered three key products – business loans, invoice financing and micro loans (known as “FS Bolt”). For business loans, borrowers could take up an unsecured loan of up to S\$2 million (US\$1.39 million) for a period ranging between one and 12 months. Their application could be approved within five days, provided certain terms and conditions were met. Those opting for invoice financing meanwhile could borrow up to 80% of their invoice value for up to 120 days; the maximum amount that could be borrowed was S\$1 million (US\$0.7 million). The loan came with line facilities and the borrower could make early repayment at no additional cost. As for FS Bolt, as the name implied, borrowers could get their loan applications approved in as quickly as two business hours, and their loans disbursed within 24 hours, provided they met certain terms and conditions. Up to S\$100,000 (US\$69,690) could be loaned for a period of between one and nine months.

⁴ For lending-based crowdfunding, individuals/companies lend money to a company that is legally bound to repay the loan at a predetermined interest rate and time upon maturity of the loan tenor. Equity-based crowdfunding meanwhile involves individuals/companies investing in the shares issued by a company in exchange for a share of its profits, which is usually paid out in the form of a dividend.

⁵ US\$1=S\$1.44 as of April 2020.

⁶ Gwyneth Yeo, “P2P Lending in Singapore Gains Speed as Funding Societies’ SME Loans Double to S\$200 Million”, ZUU Online, August 14, 2018, <https://sg.finance.yahoo.com/news/p2p-lending-singapore-gains-speed-104800410.html>, accessed April 2020.

Funding Societies charged lenders a service fee of 18% of interest earned to defray operational costs like customer support and collections (inclusive of the prevailing Goods and Services Tax), and borrowers an origination fee of between 2% and 5% of the loan amount. The interest rate for unsecured loans meanwhile ranged from 0.7% to 1.5% per month. As market competition intensified and Singapore nearly fell into a recession in 2019, the firm's annual weighted average rate of return⁷ had fallen from 16.2% in 2017 to 9.8% in 2019, while its non-performing loan rate for loans that had been unpaid for 90 days or more had risen from 0.08% in 2017 to 1.9% in 2019 for its Singapore operations.

From a team of merely eight individuals,⁸ the company had grown exponentially to a 300-strong organisation by July 2019.⁹ As at November 2019, Funding Societies had loaned S\$1 billion (US\$0.7 billion), while its default rate was 1.5% across more than 1 million loans funded across Southeast Asia.¹⁰ The top three sectors that its borrowers came from were wholesale and retail, information and communications, and fast-moving consumer goods (in descending order). There were more than 120,000 investors registered on its platform as at May 2019.¹¹

Funding Societies had undergone four rounds of financing. After an initial seed round of US\$1.2 million in November 2015, it secured US\$7 million during its series A funding in August 2016, and another US\$25 million during its series B funding in April 2018. The lead investor for its series A funding was Sequoia Capital India, while that for its series B funding was Softbank Ventures Korea. According to Teo, its series C funding was split into two rounds, and by December 2019, a sum of US\$40 million had been committed. The second round of series C funding would only take place if the company was successful in winning the digital wholesale bank licence.

In the course of Funding Societies' short history, it had attained a number of awards. It won third prize in the Singapore SME category in the 2016 MAS FinTech Awards, and the Global SME Excellence Award from the United Nations' ITU Telecom.¹² It was also the only Southeast Asian P2P lending firm to be named in the Fintech 250 list by CB Insights in 2017.

Rationale for Wanting to Venture into Digital Banking

In June 2019, MAS announced that it would issue up to five new digital bank licences, in addition to any issued to digital banks established by Singapore banking groups under the current Internet banking framework. Out of the five licences, a maximum of two would be for digital full banks, which would permit licensees to offer a wide range of financial services and accept deposits from retail customers. A maximum of three other licences would be for digital wholesale banks. These would let licensees serve SMEs and other non-retail segments (for a more detailed account of the

⁷ The weighted average rate of return is the percentage of the sum of all interests (per annum) less fees and charges for all loans (excluding interest payments for defaulted loans) divided by the total amount of loans disbursed during the year. This excludes the amounts disbursed for defaulted loans during the year in question.

⁸ Pieter Kemps, "From Boston to Series B: Funding Societies Ramps up Digital Financing for Southeast Asian SMEs", <https://www.sequoiacap.com/india/article/funding-societies-story/>, accessed April 2020.

⁹ Mike Dias, "Key Lessons from Funding Societies' Hyper-growth Journey", e27, July 1, 2019, <https://e27.co/key-lessons-funding-societies-hyper-growth-20190701/>, accessed April 2020.

¹⁰ "Funding Societies Surpasses SGD 1 Billion in SME Lending", Yahoo! Finance, November 27, 2019, <https://finance.yahoo.com/news/funding-societies-surpasses-sgd-1-021500840.html>, accessed April 2020.

¹¹ Ben Ng, "How Funding Societies Is Able to Grow in P2P Lending Market", EJ Insight, May 14, 2019, <https://www.ejinsight.com/eji/article/id/2136504/20190514-how-funding-societies-is-able-to-grow-in-p2p-lending-market>, accessed April 2020.

¹² Samantha Hurst, "Funding Societies Dubbed First Southeast Asian Company to Win Global SME Excellence Award from United Nations' ITU Telecom", Crowdfunder Insider, September 29, 2017, <https://www.crowdfunderinsider.com/2017/09/122556-funding-societies-dubbed-first-southeast-asian-company-win-global-sme-excellence-award-united-nations-itu-telecom/>, accessed April 2020.

requirements mandated by MAS, refer to **Exhibit 5**, while more information on the various digital banking licence applicants can be found in **Exhibit 6**).

The Need for Credibility

According to Teo, there were three main reasons for Funding Societies to move into digital banking, chief of which was the need for credibility. While P2P lending was a viable form of financing, the situation remained that “non-bank financiers [were] still seen as a secondary option”, he said. This could be due to the fact that commercial and other types of banks throughout the world were subjected to supervision by central banks or other similar regulatory authorities. With such external bodies checking on these banks’ policies and practices, customers could be convinced that they satisfied solid prudential standards.¹³ The same prestige however was not accorded to all P2P lending platforms, despite their being regulated in many Southeast Asian countries as well.

Transcending Product Restrictions

Teo further revealed that if Funding Societies were to remain a P2P lending platform, it would not be able to offer a more comprehensive suite of products such as bank accounts and payments, whereas digital banks could do so by virtue of their different classification and the licence they were awarded. Moreover, the company wanted to support SMEs through their various growth stages, which it would only be able to accomplish if its product offering was more varied and extensive, he added. Finally, Funding Societies wanted to stay true to its name, which stated its goal of financing to be the growth of not just firms, but also entire societies, as in the communities living in various countries.

Greater Ease of Securing Wholesale Credit Lines

Teo also said that if Funding Societies were to become part of a digital bank, it would face less of an uphill journey when seeking to obtain wholesale credit lines. These credit lines were typically raised from wealthy clients looking to park their excess funds in banks or other financial institutions. These institutions usually lent out these funds to interested parties as part of wholesale lending. Just like in the US where such funds were often placed with banks so as to earn additional interest while enjoying Federal Deposit Insurance Corp insurance, these excess funds were also typically placed with Singapore banks to earn interest while enjoying protection from the Singapore Deposit Insurance Corp Ltd (SDIC). Funds placed with P2P lending platforms however did not enjoy SDIC protection, thus investors, however wealthy, would be more hesitant about placing their funds with these platforms.

How the Consortium Took Shape

Teo disclosed that Funding Societies was in talks with two other consortia before finalising its choice of consortium partners. Like a true blue *kiasu* (‘afraid to lose out’) Singaporean, he felt that he “needed to have a backup plan and a ‘backup backup’ plan” in case he was hit by any curveballs.

¹³ Gary H. Stern, “A Nation’s Commercial Banks and Central Bank Are Reflections of Each Other”, December 1, 1994, <https://www.minneapolisfed.org/article/1994/a-nations-commercial-banks-and-central-bank-are-reflections-of-each-other>, accessed April 2020.

Factors Influencing Choice of Consortium Partners

According to him, the firm took into consideration two important factors when selecting its consortium partners. Firstly, their mutual compatibility had to be taken into account. Teo felt that for their bid to be successful, its partners had to each contribute a critical piece of the puzzle for financial innovation in Singapore, while collectively forming a compelling digital bank, one that would not just be competitive for the next five years, but also for decades to come.

Secondly, these partners also needed to have a strong commitment to Singapore but also presence beyond the city-state. As Singapore was a relatively small market, the consortium must have a stronghold in Singapore, as well as good international reach for the digital bank to be viable. Furthermore, given Funding Societies' presence in Southeast Asia, a complementary footprint would be ideal, he said.

The Case for Including Funding Societies

Commenting on the strengths that his company brought to the consortium, Teo said that since its inception in 2015, it had demonstrated its ability to provide financing to SMEs by drawing investor capital, matching borrowers and investors through its digital marketplace, and managing the credit risk of SMEs. With a 100% financing fulfilment rate and one of the P2P lending market's lowest default rates of 1.5% in Southeast Asia, Funding Societies' track record as a successful P2P platform was in its favour. It had also helped a number of SMEs to internationalise and expand within Southeast Asia through its product offerings. The firm was already regulated in Singapore, and had the experience of working with MAS and complying with its standards. Besides, as the digital bank licence was designed to enable financial inclusion for under-served segments such as SMEs, Funding Societies was versatile enough to complement whichever set of consortium partners.

The Final Form the Consortium Took

Teo confessed that initially, Funding Societies had wanted to be the lead member and the largest shareholder of the consortium. However, it eventually agreed to be the second largest shareholder with AMTD taking the lead, followed by both Xiaomi and SP Group together. He explained that he had agreed to the final arrangement so as to form a larger and stronger consortium. Should they succeed in obtaining the licence, Funding Societies would manage the bank through representation on its board of directors.

The Backup Plan

In the event that their application was not successful, Teo said that Funding Societies would seek to partner with one of the successful applicants. Separately, Malaysia's central bank, Bank Negara Malaysia, had also announced in December 2019 that it was planning to issue up to five digital banking licences.¹⁴ One might speculate that Funding Societies, which had operated in the country since February 2017 as the leading platform there, might have had an interest in the licence too.

¹⁴ "Bank Negara to Issue up to 5 Digital Banking Licences", The Star, December 27, 2019, <https://www.thestar.com.my/business/business-news/2019/12/27/bank-negara-to-issue-up-to-5-digital-banking-licences>, accessed April 2020.

Waiting for D-Day

It had been almost four months since that nail-biting night on New Year's Eve. Another public holiday – Good Friday this time – was on the horizon. Just as Teo was mentally ticking off the months left to the MAS announcement of the successful applicants, the breaking news headline in bright yellow above the CNA news ticker on his TV screen announced: MAS would postpone the announcement till the second half of 2020. So the waiting game was to continue for some time more.

In the meantime, his consortium partners had gone on to take additional steps to further their cause. On April 8, 2020, AMTD International had made its debut on the Singapore Exchange main board to much fanfare, albeit the listing ceremony had been conducted online.¹⁵ AMTD had also launched a fintech leadership programme earlier together with Xiaomi, as well as Singapore Management University and the National University of Singapore.¹⁶

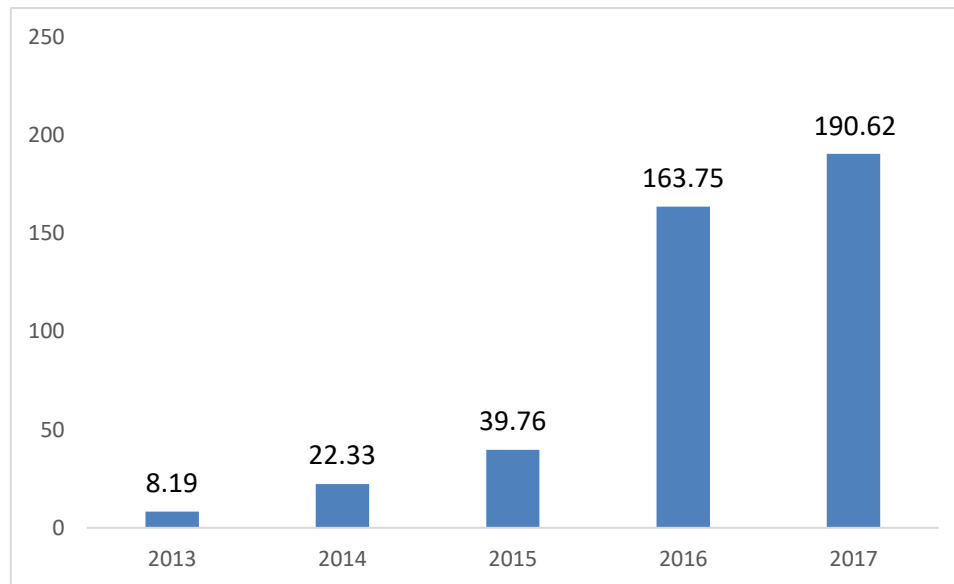
Would all these steps be sufficient to place Funding Societies and its consortium in the winner's circle? Would their efforts be rewarded with the ultimate prize they were hoping for? Teo had no intention of just passively awaiting MAS's decision. Instead, he would “continuously build capabilities and partnerships in preparation for the licence as SME financing ... [was Funding Societies'] bread and butter”.¹⁷

¹⁵ Rachel Mui, “New York-listed AMTD International Makes Debut on SGX at S\$13.95”, The Business Times, April 8, 2020, <https://www.businesstimes.com.sg/companies-markets/new-york-listed-amtd-international-makes-debut-on-sgx-at-s1395>, accessed April 2020.

¹⁶ Ibid.

¹⁷ Aw Cheng Wei, “MAS Extends Assessment Period for Digital Bank Hopefuls”, The Straits Times, April 10, 2020, <https://www.straitstimes.com/business/banking/mas-extends-assessment-period-for-digital-bank-hopefuls>, accessed April 2020.

EXHIBIT 1: SINGAPORE CROWDFUNDING VOLUMES FROM 2013 TILL 2017 (US\$M)



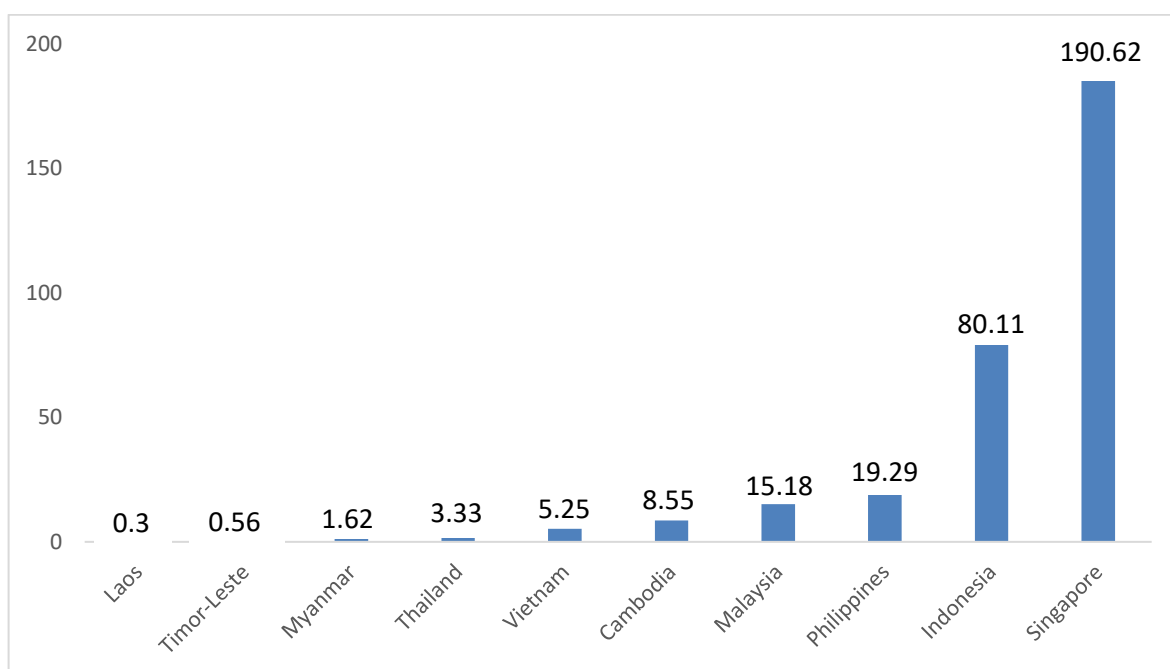
Source: Cambridge Centre for Alternative Finance, “The 3rd Asia Pacific Region Alternative Finance Industry Report”, November 2018, accessed April 2020.

EXHIBIT 2: LICENSED CROWDFUNDING PLATFORMS IN SINGAPORE (AS AT MAY 2019)

No	Name	Loan Book Size (US\$m)	Crowdfunding Model
1	Aces Crowdfund	Not Available	Lending and Equity-based
2	Arcor Capital	Not Available	Equity-based
3	CapBridge	\$626.95 (up to 2018 only)	Lending and Equity-based
4	Capital Match	\$100.21	Lending-based
5	Co-Assets	\$41.8	Lending-based
6	Crowd Genie	Not Available	Lending-based
7	Crowdo	Not Available	Lending and Equity-based
8	FundedHere	In excess of \$69.66	Lending and Equity-based
9	Funding Societies	\$438.07	Lending-based
10	Fundnel	\$557.27	Equity-based
11	Fund Singapore	Not Available	Lending-based
12	FundTier	\$6.76	Lending-based
13	InvestaCrowd	\$696.61	Real Estate and Equity-based
14	Minterest	\$24.38	Lending-based
15	Moolahsense	\$51.81 (up to Feb 2019 only)	Lending-based
16	SeedIn Technology	\$115.64 (excluding China)	Lending-based
17	SmartFunding	Not Available	Lending-based
18	Validus Capital	\$160.38	Lending-based
19	We Crowdfunding	Not Available	Not Available

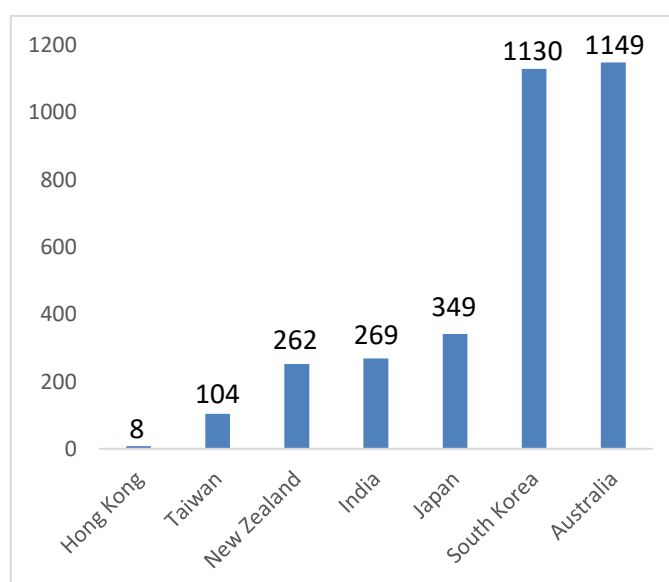
Source: Individual company websites

EXHIBIT 3: SOUTHEAST ASIA CROWDFUNDING VOLUMES IN 2017 (US\$M)



Source: Cambridge Centre for Alternative Finance, “The 3rd Asia Pacific Region Alternative Finance Industry Report”, November 2018, accessed April 2020.

EXHIBIT 4: CROWDFUNDING VOLUMES IN SELECTED ASIA-PACIFIC MARKETS IN 2017 (US\$M)



Source: Cambridge Centre for Alternative Finance, “The 3rd Asia Pacific Region Alternative Finance Industry Report”, November 2018, accessed April 2020.

EXHIBIT 5: REQUIREMENTS FOR SINGAPORE DIGITAL BANK APPLICANTS

Digital full bank licence applicants must be headquartered in Singapore and be controlled by Singaporeans. In the case of a joint venture, there must be one Singaporean party at least, and this party must hold the largest shareholding and have management control in order for applicants to meet the second requirement concerning Singaporean control.

In addition, applicants or their parent group must demonstrate a track record in running an existing business, which should be in the technology or e-commerce domain. They also needed to show how they can serve unmet or under-served needs, and prove that they have a sustainable business model, such that they would not engage in value-destructive competition to gain market share.

In the initial stage, successful applicants must have a paid-up capital of S\$15 million (US\$10.45 million) when operating as restricted digital full banks, but they would need to have a minimum paid-up capital of S\$1.5 billion (US\$1.04 billion) by the time they progress to become a full-functioning digital full bank. While MAS had not prescribed a time period for successful applicants to transition to the full-functioning stage, they must have a viable plan to do so. In addition, they could only have one physical place of business.

Digital wholesale bank applicants meanwhile could be either Singaporean or foreign entities, but the bank would have to be locally incorporated. It would also need to have a minimum paid-up capital of S\$100 million (US\$69.66 million), and not accept Singapore dollar deposits from individual depositors with the exception of fixed deposits of at least S\$250,000 (US\$174,160). There would however be no limitation on its business deposit accounts for SMEs and corporates. Furthermore, applicants had to provide a viable exit plan at the point of application. They should also operate in one physical venue only, just like digital full banks.

The application deadline was December 31, 2019, and the successful applicants were originally expected to be announced in June 2020, but this had now been delayed until the second half of 2020, as a result of the fallout resulting from the Covid-19 pandemic. MAS said this would allow applicants to concentrate on dealing with the immediate repercussions of the pandemic on their businesses, while also letting the Singapore central bank zoom in on safeguarding monetary and financial stability, as well as the resilience of financial institutions.

The successful applicants were slated to start operations by the middle of 2021, but this would likely be pushed back in tandem with the postponement in announcing these applicants.

Source: Monetary Authority of Singapore

EXHIBIT 6: KNOWN APPLICANTS FOR SINGAPORE DIGITAL BANK LICENCES**Total Number of Applications:**

MAS said that it had received a total of 21 applications for a digital bank licence, of which seven were for a digital full bank licence, and 14 for a digital wholesale bank licence. It did not release any applicant names.

Known Digital Full Bank Licence Applicants:

- ❖ Internet platform Sea
- ❖ Ride-hailing operator Grab and telco Singtel
- ❖ Razer Youth Bank (comprising Razer Fintech, supermarket chain Sheng Siong, insurance business FWD, Internet company LinkSure Global, tech venture fund Insignia Ventures Partners, and vehicle wholesale marketplace Carro)
- ❖ Beyond (comprising apex business chamber Singapore Business Federation, lifestyle and wellness luxury group V3 Group, and stored card operator EZ-Link, property group Far East Organisation, investment firm Heliconia Capital, and insurer Mitsui Sumotomo Insurance)
- ❖ Financial services company Enigma Group, cyber-security firm Qrypt Technologies, app developer 2359 Media, and fintech-regtech venture Blockchain Worx
- ❖ Fintech firm MatchMove, finance company Singapura Finance, clearing and settlement network Lightnet, and digital banking and services platform OpenPayd Holdings

Known Digital Wholesale Bank Licence Applicants:

- ❖ Hong Kong financial services group AMTD Group, P2P lending platform Funding Societies, utilities provider SP Group, and Xiaomi Finance
- ❖ Ant Financial
- ❖ Wealth management firm iFast Corp, Chinese fintech company Hande, and Chinese digital bank Yillion
- ❖ Chinese Internet technology company ByteDance
- ❖ Chinese supply chain financial services provider Sheng Ye Capital, financial conglomerate Phillip Capital, and fintech company Advance.AI
- ❖ Chinese property giant Greenland Group and Chinese financing platform MinIPO
- ❖ China-based Zall Smart Commerce Group, Japanese trading conglomerate Marubeni Corp, and Singapore supply chain provider Global eTrade Services
- ❖ Arival (including venture capital firm Life.Sreda)

Sources: Monetary Authority of Singapore, The Straits Times, and The Business Times