Opinion: Recent FinTech Woes Have Long-Term Public and Private Market Implications

With several fintech companies reporting earnings disappointments over the last two weeks, and with "FinTech Unicorn" GreenSky, Inc. (GSKY) that IPO'd less than fifteen months ago now considering "strategic alternatives," both public market and private equity investors have to consider the longer tail implications for the sector. Is the public market fairly valuing the underlying business fundamentals and growth opportunities being pursued by fintech companies? Should GreenSky have stayed private? And given the GreenSky situation, will other fintechs be able to gain access to much needed capital (both public and private) for further growth and value creation?

GreenSky has repeatedly underdelivered relative to market expectations. The company reported second quarter earnings this week and produced EPS of $0.19 (versus consensus expectations of $0.23) due to weaker-than-expected lending volume. Not only were earnings short of expectations but transaction volumes grew 20% year-over-year when the company had indicated that it would deliver 30% growth. Add to these disappointing performance metrics the fact that one of GreenSky's key bank partners announced it would not renew its asset buying relationship with the company and GreenSky is now looking for alternative funding arrangements. All of this news was eclipsed by management announcing that it is considering "strategic alternatives". The stock declined 37% on the day the quarter's results were announced, adding to its 29% underperformance for 2019 and a 70% decline since its IPO just last May.

Public companies have nowhere to hide when things do not go as planned. When expectations are repeatedly not met and business models do not deliver the profits that technology enabled business models suggest should be produced, recently minted public companies are punished severely. Public companies cannot contain the bad news to the board room where private equity investors complain loudly but their complaints lack the echo chamber of the public markets. GKSY cannot do a down round in private and has to take its lumps in public. There was similar news for OnDeck (ONDK) last week when ONDK announced alongside its earnings that JPMorgan Chase (JPM) was ending its loan origination partnership (ONDK shares declined 23% that day and is down 49% YTD, and off 85% since its IPO). The fintech world was banking on these bell weather companies delivering strong, sustainable business models that would reshape the financial services landscape. So far, this is not what happened.

GSKY's and ONDK's woes are only the beginning for private fintech companies. Earlier stage fintechs look to the public fintechs as reference points and hope that they can replicate their IPOs and deliver sustainable growth. GreenSky could have been that shining success, but it appears to be example of what can go wrong when a fintech goes public. Growth stage companies tell their private investors that if they grow fast enough and big enough, they can go public — like public companies GSKY and ONDK. But, when these companies underperform with significant market value erosion and talk about exiting the public market, it sends shudders down the backs of private lenders and the investors who back them.

What are the lessons that private companies can glean from the disappointing news coming from the public fintechs? Under promising is a winning strategy. Fintechs have to stop falling into the trap of setting expectations so high that they miss delivering against them. The public market has demonstrated that newly minted public companies will be severely punished for missing performance targets. And while founders want big valuations and private equity investors need big write ups to be viewed as successful, they would both be far better served setting expectations lower by accepting lower initial public valuations and thereby allowing themselves to set lower performance targets for the 12 to 24 months after they IPO. This sort of thinking may seem logical to observers of this market, but when you are neck deep in the fintech market as an operator, investor or banker, it is hard to avoid overheating expectations and valuation. With each capital raise leading to quantum leaps in valuations, private companies have to set very heady goals for their IPOs and for the year post going public. After all, the IPO buyers need a big return too. And this dynamic has ended recently with a very disillusioned fintech market. If we wish to see fintechs deliver on the promise of next-generation financial services with transformational value add, better economics, and broad adoption, we have to give these companies the time to grow into world beaters. It cannot happen overnight and promising such only leads to creating a cynical market that will think twice about investing in early-stage and later-stage fintech innovators.

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