AMAZONIZATION 2.0—ONE OF FIVE TRENDS SHAPING INNOVATION

THE EXPONENTIAL PULL OF INNOVATION

Asset management and the upside of disruption

SEI New ways. New answers.®

ADVANCING THE STATE OF THE ART

"*You never change things by fighting the existing reality.* ***To change something, build a new model that makes the existing model obsolete.***"

— R. Buckminster Fuller

Asset management firms are built to withstand revolutions, not embrace them. The objective, after all, is to preserve and grow capital. Despite its staid reputation, the investment business is not static, with regulatory changes and competitive pressures periodically spurring change. Now, the introduction of new technologies and business models is making change a constant and causing the industry to be reorganized, re-engineered, and reinvented before our very eyes.

Successfully harnessing technology in a complex and heavily regulated industry is not easy, even when there is great enthusiasm for it. Generous budgets at incumbent firms can be undermined by cultures that prioritize stability over creativity. Insurgents, often the innovators, can be hobbled by inexperience with how the investment business really works. Like most revolutions, the transformation of financial services is inevitably turning out to be a messy affair.

It isn't clear who will survive or emerge victorious, but the basic contours of change are coming into focus. Data plays a central role and is being analyzed with increasingly sophisticated tools that include various types of artificial intelligence. If other sectors are any indication, the already pivotal role of platforms is set to expand even further. Social media is causing communications to be remade and reconsidered. Even the gig economy is nibbling at the edges of an industry that, for all of its corporate behemoths, has always been open to scrappy startups.

We addressed these topics in 2016 with *The Upside of Disruption: Why the Future of Asset Management Depends on Innovation*. The themes remain relevant, but a flood of venture capital and widespread adoption of new technologies in the intervening years—compounded by the unexpected arrival of COVID-19—accelerated the pace of change. The net result is a vastly more complex ecosystem populated by thousands of firms at all stages of development. Progress has not been linear. For every genuine innovation, there are countervailing examples of fraudulent or poorly conceived technologies, reminding us to stay skeptical and temper our expectations.

To capture a balanced and up-to-date picture of innovation in asset management, SEI collaborated with ANZU Research to revisit the five ongoing developments that are redrawing the industry's competitive environment.

Released serially over the upcoming months, each of the following themes—dubbed as follows—will be explored in detail, with a particular focus on recent developments:

1	**Watsonization**	Artificial intelligence is quickly transitioning from curiosity to critical cog in efforts to monetize data and power applications from front to back office.
2	**Googlization**	Data-smart companies are learning how to access, aggregate and distill competitive knowledge from a vast sea of previously inaccessible information.
3	**Amazonization**	Online platforms are reshaping business dynamics, putting customers in charge and forever altering the customer experience.
4	**Uberization**	By rethinking the value chain, a fast-emerging business model points to new ways of creating value and gaining scale.
5	**Twitterization**	Corporate communication is no longer a one-way street. Technology has transformed how businesses communicate with—and learn from—their customers.

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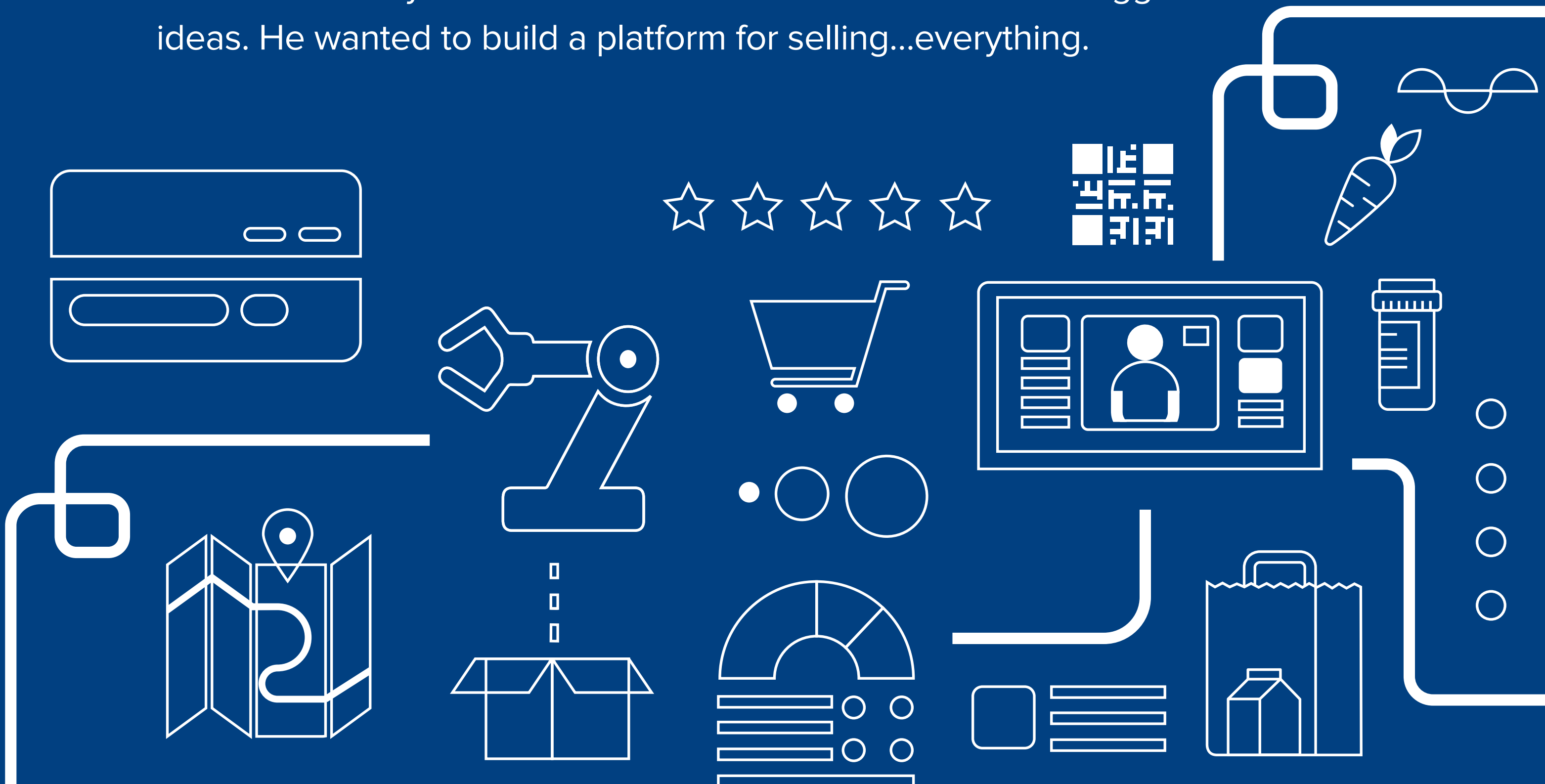
AMAZONIZATION 2.0

Online Platforms in Asset Management

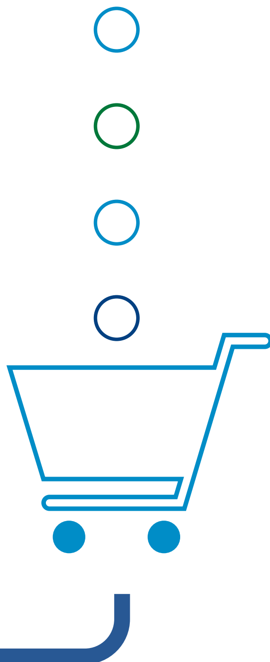
A BRIEF HISTORY

Amazon is so deeply embedded in our modern lives that it can be difficult to recall life before the never-ending streams of cardboard boxes started showing up on our doorsteps. But the 1990s were a different time. When Netscape Navigator first made the internet accessible to the masses, widespread amazement was quickly followed by frustration over what wasn't there. Countless entrepreneurs quickly addressed one niche after another, but few had the vision of the former Wall Streeter who decided—initially—to sell books online. But Jeff Bezos had bigger ideas. He wanted to build a platform for selling…everything.



A BRIEF HISTORY

We first wrote about "Amazonization" in 2016's *The Upside of Disruption*. At that time, it had only been a few short years since Amazon was recognized as the largest online retailer in the world[1], and the term served as convenient shorthand for the growing power of online platforms. China's Alibaba is a similar powerhouse, accounting for well over half of all online retail sales in China and boasting 755 million active users.[2] But it is not only generalist behemoths that are succeeding. Noted in the original white paper for having more than 1.4 million sellers of handcrafted goods on its platform, Etsy now boasts 2.5 million vendors and 45.7 million buyers.

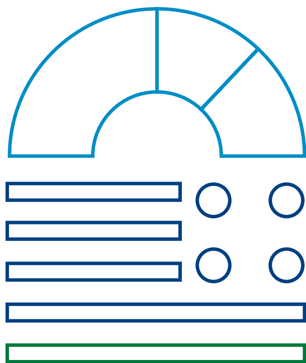


Meanwhile, Amazon has gone from strength to strength, with its share price gaining more than 400% over the five years ending in 2019, almost 10 times the growth of the S&P 500. In that time, it also became one of very few companies to ever record a market capitalization of more than $1 trillion. With $87.4 billion of revenue and $3.3 billion of net income at year-end 2019, **Amazon is still the world's largest online retailer**. It owns approximately 38% of the e-commerce market[3] and has managed to flourish even more during the coronavirus pandemic that brought much of the global economy to its knees. As retailers from Barneys, Neiman Marcus and JC Penney to Hertz, Modell's Sporting Goods and Gold's Gym file for bankruptcy, there is growing concern that Amazon, while doing nothing illegal and taking advantage of the market economy, is becoming too big.

Amazon owns approximately **38%** of the e-commerce market.

The company's dominance means Amazonization is no longer just an observation that a particular segment is being upended by an online competitor generally. It increasingly means an industry is being disrupted by one very specific and voracious firm. As Jeff Bezos famously said, "Your margin is my opportunity."

Acquisitions have been a part of the culture of innovation. By year-end 2019, Amazon had acquired **86** companies.



The fact that Amazonization now has both literal and metaphorical meanings is particularly noteworthy here, because there is still no Amazon of financial services. Despite some tentative moves into vendor financing and consumer credit, Amazon itself is still operating on the fringes of the sector. Meanwhile, the asset management landscape remains as competitive as ever, and the frenzied financing of fintech startups has produced a complex ecosystem of companies that have yet to coalesce around any dominant platform. It is entirely possible that Amazon will find ways to disrupt financial services in the future, but our focus here is more on the impact of the business model, rather than on the company itself.

RECENT DEVELOPMENTS

How did an online bookseller come to dominate commerce? Amazon's growth is attributable in part to a ruthless dedication to low prices, but its outstanding customer experience is equally important and far-reaching. Amazon's combination of price, convenience, transparency, community and insight has raised the bar to lofty heights that few competitors can clear.

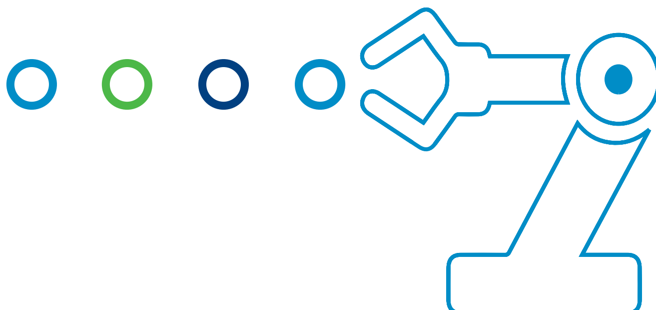
Core values are vital, but Amazon would not be what it is today without innovation. Success is not guaranteed: The Fire Phone and Amazon Destinations are just two examples of the many products that failed to take hold. Conversely, the Kindle and Amazon Web Services (AWS) are both good examples of creating vast, profitable businesses virtually out of thin air.

Amazon has fostered a culture of innovation that is unafraid to look outside its four walls for pioneering approaches that can advance the company's agenda. Its history of acquisitions clearly shows a willingness to ferret out new perspectives, expertise, technology and best practices in other industries. Beginning in 1998 with its purchase of IMDb, Amazon hinted at its aspirations to monetize all types of data, even without a clear roadmap in place. By year-end 2019, it had acquired 85 additional companies.[4] Some of the most

famous acquisitions were clearly aimed at establishing a prominent foothold in specific verticals. Zappos—purchased for $1.2 billion in 2009—provided instant scale in the footwear space. Whole Foods—acquired for $13.7 billion eight years later—provided a unique entrée into the supermarket business.

Most deals, however, have been carefully selected to bolt additional functionality onto the platform's growing infrastructure. So synonymous is Alexa with Amazon now that many people are likely to have forgotten that Alexa.com was purchased for $250 million back in 1999. It has of course gone on to form the foundation of Amazon's omnipresent personal assistant, which offers the ability to retrieve information or make a purchase with only a few spoken words. In 2012, Amazon turbocharged its fulfillment capabilities by buying Kiva Systems for $775 million. Kiva's robots are critical enablers of Amazon's expanding logistics infrastructure, which is now said to include 150 million square feet of warehouse space, delivery trucks and vans numbering in the tens of thousands and even cargo ships and aircraft.[5]

Amazon's most recent acquisition is Chicago-based Health Navigator, which didn't even exist at the time of the Alexa deal. An enterprise that initially seems far removed from Amazon's core business makes significantly more sense in light of its promise to "set the standard for digital health clinical content quality."[6] With the world's attention squarely on health and welfare as a result of the COVID-19 pandemic, it is not hard to imagine how a partnership like this could lead to a revolution in diagnostics, patient care, resource allocation and other aspects of healthcare. It also illustrates a potential path for the financial services industry, where many firms are currently trying to knit together disparate



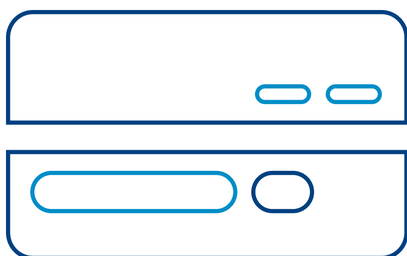
data streams and analytical capabilities into a coherent value proposition. Healthcare is an increasingly important financial consideration in an aging world, particularly in the United States, where costs are high and insurance companies are often closely integrated into the broader asset management sector.

One of Amazon's most prescient acquisitions may have been Twitch. Bought for almost a billion dollars in cash in 2014, this social video platform for gamers is not only paying for itself already, but also **painting a vivid picture of what real-time, data-enriched community interactions look like.** It places Amazon squarely in the middle of the massive global marketplace for electronic games and sports, but it could also prove to be a template for next-generation trading environments.

Venture capital investment in fintech has skyrocketed to more than **$100 billion** in the last two years.

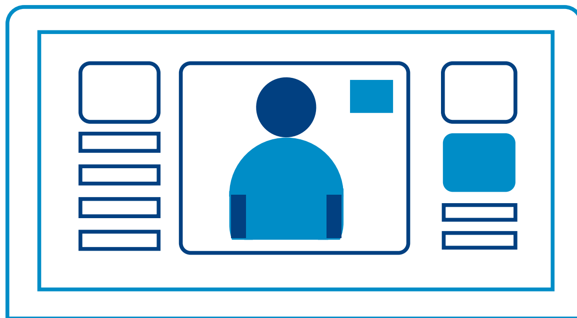
IMPACT ON FINANCIAL SERVICES

If the flow of money is any indication, innovation in the financial sector has shifted into high gear since we wrote *The Upside of Disruption*. Financial services technology has existed for decades. SEI, after all, was founded in 1968, providing the bank loan industry's first computer-based commercial credit simulators. Fintech as a concept, however, was effectively invented in just the past few years,[7] with venture capital investment skyrocketing to more than $100 billion in the last two years alone.[8]



Startups account for much of the activity because the inherently conservative nature of financial services makes full-fledged digital transformation relatively rare among incumbents, who are more likely to choose incremental improvements over radically different approaches. Existing firms thus encounter new faces at every turn. In many cases, these new industry participants offer fundamentally new ways of doing things. **Banking is being redefined by online firms offering greater connectivity.** Payments and transfers are happening across a growing array of applications. Algorithms are informing financial advice.

Many startups address specific niches. Alternative lending platforms, for example, exploded in popularity as many banks withdrew in the wake of the most recent global financial crisis. Hoping to address a key pain point for many firms, security and compliance startups are also popular. Robo-advisors (aka robos) need no introduction at this point, but it is interesting to note how quickly many pivoted toward banking services and integration with human intermediaries. Many tools are being developed to make investment processes more efficient and effective. Some developments are clearly synergistic. Investors have only been able to act on their growing appetite for private securities because a number of technology-driven matchmakers, exchanges and marketplaces have been launched, creating a virtuous cycle.



Financial services and fintech will quickly become impossible to tell apart. The evolution of the combined industry is likely to accelerate as a growing number of infrastructure firms collectively reduce the barriers to entry for new fintech. Bridging the gap between technological innovation and industry expertise becomes much easier when firms are able to integrate external Application Program Interfaces (APIs) that handle challenging aspects of the business like regulatory compliance.

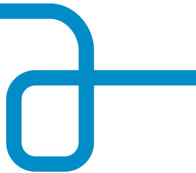
The power of platforms: **bringing order to chaos.**

With every segment, channel, product, service and function now fair game for reinvention, a current snapshot of the financial services ecosystem might not even be feasible. One could use representative firms to illustrate a variety of functional areas, but the resulting map would only hint at the complex multi-dimensional network of connections that is being woven. Asset management is already heavily intermediated, with multiple layers and external influencers and infomediaries. A growing tech stack and network of vendors and partners makes the ecosystem look more like a Jackson Pollock painting than a schematic. This is why platforms are so powerful. They curate connections, facilitate transactions, enable communications, provide liquidity, control transparency and ensure security. They bring order to chaos.

Many investors do not care about brands as much as they used to.

Technology-driven distribution platforms in asset management are nothing new. They date back to the 1990s, when Schwab launched OneSource in the U.S. and Virgin Money was founded in the United Kingdom. The institutional world lagged, but even it is increasingly dependent on data analytics and electronic interactions. Nevertheless, no single firm can begin to rival the impact Amazon has had on the retail landscape.

The slow pace of change may explain why many industry insiders do not view the investments industry as being particularly vulnerable to disruption. While 67% of banking executives say non-traditional firms are having a large impact on mobile payments, for example, only 8% say wealth and asset management services are feeling a major impact.[9]



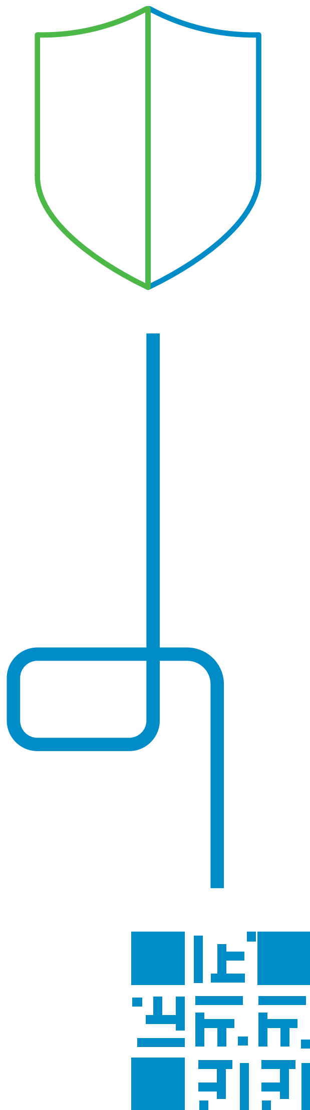
Large distributors may view their assets as relatively sticky, but asset managers are finding it harder to compete, despite booming markets over the past decade: The percentage of mutual funds and ETFs with negative net flows rose steadily from 45% to 52% between 2015 and 2019.[10] It is dismaying for many to hear, but as we pointed out in our 2018 white paper, *Branding Investment Expertise in the 21st Century*, many investors do not care about brands as much as they used to. They are more inclined to trust the overarching platform and focus on convenience, low price, features and reliability. A distribution platform with the features and reach of Amazon would be life-changing for many managers who have already gotten accustomed to their brand being obscured by that of their distributors.

A dominant platform has yet to emerge among incumbents or newcomers. It is theoretically possible that the landscape will remain fragmented. Asset management and wealth advisory, after all, feature some characteristics that clearly distinguish them from the buying and selling of T-shirts and scented candles. For one thing, human relationships and empathetic conversations remain extremely important despite the growing role of algorithms and automation. Furthermore, as important as trustworthiness is for a retailer like Amazon, **it is much more vital for financial platforms to establish reputations for trustworthiness with their vendors, clients and the larger population.** Finally, many investors also remain keenly interested in beating the market, despite the relentless rise of indexing. For any platform to be successful in financial services, it must therefore be able to accommodate non-fungible transactions.

What types of firms are best positioned to **revolutionize financial services?**

Given these circumstances, what types of firms are best positioned to revolutionize financial services with platforms that could rival Amazon's presence in e-commerce? We see five potential scenarios unfolding.

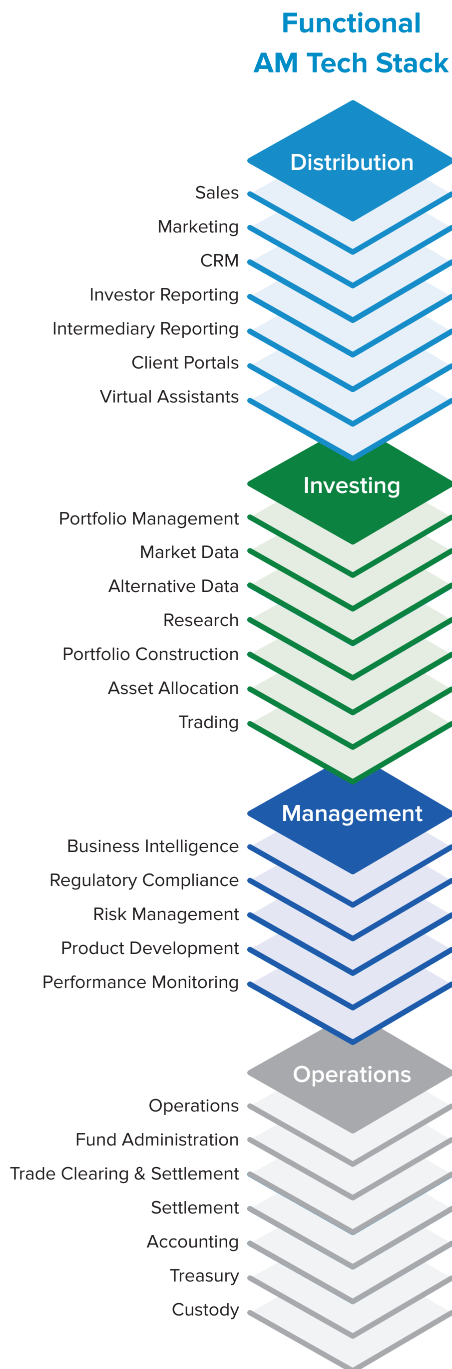
1. **Platforms coalesce around large banks and advisory firms.** This might be the easiest scenario to envisage. Distribution resources are already there, and proprietary products aren't much of an issue anymore. Still, banks and large brokerage organizations haven't capitalized on their head starts as much as one might expect. Innovation does not come naturally to either group, and integrating new acquisitions has historically been—and is likely to remain—challenging. Incremental changes are to be expected, but large balance sheets notwithstanding, transformation might be a step too far for many entrenched players who will all need to fight to avoid going the way of Oldsmobile.
2. **Consultants, database firms and service providers** reskin themselves, leveraging their advantageous positioning amidst vast pools of data. Given effective analytics, they have incredible power at their disposal. Independence and thought leadership give them credibility. Brand names, however, they



are not. It is easy to see why they might prefer to remain in the background—effectively serving as the "Intel Inside" for their clients—protecting their institutional business, rather than entering the fray of competing for retail dollars.

3. **Existing asset management firms step in.** Current industry behemoths are all building capabilities far beyond the manufacturing of investment products. BlackRock demonstrated a willingness to pivot when it rolled out Aladdin, a **central operating system for portfolio and risk management systems that now powers trillions of dollars of investments**. Franklin Templeton acquired AdvisorEngine, which had previously absorbed NestEgg (robo-advisor), Junxure (Customer Relationship Management) and Wealthminder (financial planning). Fidelity, already a major player in the fund supermarket space, has been spending more marketing dollars on its distribution activities than its asset management business. The primary obstacle here is the age-old conflict between proprietary product and open architecture. Firms already offering distribution, custody and fund services would seem to have the edge.

4. **New, purpose-built platforms emerge**, propelled by a combination of organic growth and M&A. With so much dry powder available to private equity investors, it is not hard to imagine efforts to engineer Amazonesque platforms by joining together best-of-breed examples of various functions. While technically feasible, significant challenges would include sustaining a coherent vision and knitting together a robust culture that takes advantage of the underlying wealth of client and investor data. Brand building would—needless to say—be an expensive exercise. **The capital being poured into individual fintech firms is breathtaking, sometimes topping $1 billion.** SoFi has raised $2.5 billion. Figure has raised $1.3 billion. Robinhood has raised $1.2 billion. Revolut has raised more than $800 million.



5. **Tech giants take over.** Google, Apple and Amazon have all tested the waters with modest forays into the world of finance. They have met with varying degrees of success, and it's safe to assume that further incursions are to be expected. In China, Ant Financial Services (Alibaba's financial affiliate) already reports more than 600 million users.[11] With its move from the world's largest money market fund (for its vendors to park their cash) to a much larger array of investment strategies, Ant and Alibaba may have already created a map for migrating from online commerce to investments.

Would Amazon itself jump directly into asset management or financial advice? Possibly, but it seems more likely that the company would use its data and expertise to create a platform for other managers while charging them for shelf space. It is not difficult to imagine an ETF firm partnering with Amazon to develop highly liquid investments tailored to the needs of the vendors in its marketplaces. If successful, Amazon could move upstream, private labeling various aspects of the value chain in much the same way they have private labeled numerous other products.

Ant Financial (Alibaba's financial affiliate) already reports **more than 600 million users**.

ASSET MANAGEMENT **EXAMPLES**

If a dominant platform ultimately emerges, it will need to deftly incorporate a **variety of technologies and skill sets.**

There is no equivalent of Amazon in the asset management industry. There are major players, to be sure, but myriad efforts over the years have left us with a competitive landscape that remains relatively fragmented. No one has managed to assemble all of the pieces in a way that recalls Bezos's baby. Turnkey asset management platforms (TAMPs) might seem to be the obvious place to look, but many firms are subscale, and acquisitions aimed at growth, scope or consolidation are the norm. Leading firms such as Envestnet, SEI, Vestmark, Fiserv, AssetMark, Orion, Brinker and others continue to vie for market share in this fiercely competitive sector.

Whether a dominant platform is ultimately built around an incumbent or a startup, it will need to deftly incorporate a variety of technologies and skill sets. There are already thousands of fintech startups hailing from all corners of the world, with major hubs emerging in the U.K., Switzerland and Singapore alongside those in Silicon Valley, Boston and New York. Many of these companies may not exist a decade from now, having been out-competed or acquired in the rapidly evolving sector. Everyone who lived through the dot-com crash is intimately familiar with how quickly things can go south. Only the well-capitalized firms with sustainable business

models get through. As such, it is not necessarily the names that are important. Even those that survive and thrive are less likely to become platforms with well-known brands than cogs in larger ecosystems. Rather, it is what these companies represent that is important; it is their technological innovations, their strategic direction and the momentum they represent that will be long-lasting.

We have compiled a sample list of firms reflecting at least some of the scope that is likely to be necessary. Fintech encompasses many functions, ranging from security to HR to marketing, but the core of any investor-facing platform is likely to be comprised of investments, banking, trading, lending, media, data and networking. Diversification means many firms defy siloed categorizations, so these have been grouped by their original function, illustrating the many potential entry points for would-be platforms and their constituent parts. The list should not be considered to be exhaustive.

BANKING

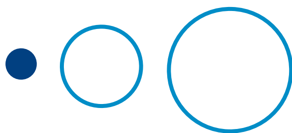
Startup banks focused on daily financial transactions via mobile apps are sometimes referred to as "challenger" banks. With their frontal assault on incumbent banks, they might represent the most direct threat to the status quo of financial services. Despite significant regulatory hurdles, well-funded firms have already taken root globally. **Revolut** and **Monzo** are two prominent examples in the U.K. **N26** hails from Germany and **Nubank** began in Brazil and quickly expanded. **Chime** and **Dave** are just two examples in the large U.S. market. To date the focus has largely been on deposits and cards, but fuller integration with wealth management seems to be just a matter of time.

INVESTING

Robo-advisors such as **Betterment**, **SigFig**, **Personal Capital**, **Wealthfront** and **Nutmeg** were launched as cost-effective and easy-to-use investment platforms running seamlessly on mobile applications. Their most distinctive feature, however, was automated advice that made it simple to construct ETF portfolios tailored to individual needs and risk tolerances. Robos have found fans and gathered billions in assets with their slick applications and effective algorithms, but organic growth may ultimately be capped by similar services offered by incumbents like **Vanguard** and **Schwab**. Integration with banks (traditional or digital) and more traditional advisory firms may be the most likely avenue for expansion going forward.

There are smaller, more specialized firms competing in this space as well. **Digit** is an app that analyzes spending habits and automatically saves and invests a certain amount each day, effectively making money management a no-brainer. Meanwhile, **Yomoni** is attempting to democratize wealth management in France by bringing sophisticated online investment services to the masses.

BROKERAGE

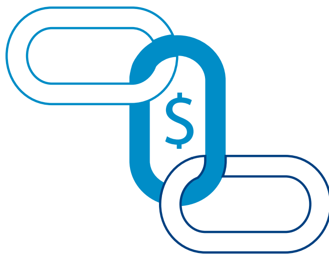


Marrying technology to transactions, discount brokerage firms have been positioned as investment platforms of the future for some time. This doesn't mean they are immune from disruption: Newcomer **Robinhood** immediately made a name for itself when it announced commission-free trading, ultimately causing established players to follow its lead. It has moved on to offer free trading of fractional shares, making investments even more affordable to young investors with fewer liquid assets. Using scalable technology and increasingly lower transaction costs as its backbone, Robinhood demonstrates the power of simple ideas that will almost certainly be found at the heart of any offering by large platforms in the future.

LENDING

Beginning as a marketplace lender, **CreditEase** has grown into a leading fintech conglomerate in China, where it now boasts a range of other businesses such as wealth management, crowdfunding, robo-advisory, insurance technology and blockchain products. The company is also an active investor and incubator of other fintech startups.

REFINANCING



Using its successful student loan refinancing business as a springboard, **SoFi** quickly expanded into other types of lending alongside banking and investing. One of the first fintech unicorns, the company has relatively widespread brand recognition for a firm that is still less than 10 years old. Having proven prolific at fundraising, SoFi's continued expansion through M&A seems inevitable.

Figure represents another flanking maneuver on the larger financial services market. Starting in 2018 with a focus on home equity and based on blockchain technology, the company quickly raised over $1 billion and is expanding its scope. Notably, the company was founded by SoFi's ex-CEO.

DATA SERVICES

Information and insights have proven to be fruitful entry points for a number of companies with larger aspirations. **Bloomberg** began as a pioneering data and analytics firm that became an indispensable part of the operational fabric at many firms before going on to become a global media empire.

Morningstar established its reputation as a trusted data provider before moving into analytics, software, and media. Now applying the full scope of its expertise to offering TAMP services, the company illustrates yet another avenue to Amazonization.

DATA SERVICES (CONTINUED)

Much earlier in its life cycle is **Benzinga**, which provides financial news and analysis. Still small, it is gaining traction by its adept use of social media and focus on sectors with less coverage like the cannabis industry. **YCharts** is focused on market data visualization, an essential aspect of financial services that could prove central to any platform's offering. **Novus**—a portfolio analytics firm—is another narrowly focused firm that could prove to be an integral part of a larger platform, for whose investors it would help manage and analyze risk, performance and exposure.

EXCHANGE

Nasdaq's core business does not require an introduction, but the company has been actively expanding its scope of activities via M&A. Acquisitions like SecondMarket, Solovis, OneReport, Quandl, Cinnober, eVestment, Sybenetix and others make Nasdaq far more than just an exchange for publicly traded shares. Now with Nasdaq Private Market, it is firmly positioning itself in the midst of the growing market for privately owned securities through auction funds and other avenues.

Liquidity solutions for private markets are multiplying. **Forge** (formerly Equidate) positions itself as a marketplace for private equity. Having merged with **SharesPost** in early 2020, the combined company boasts more than $6 billion in transaction volume involving hundreds of companies.

Not all approaches are the same. **Zanbato** is a crossing network for private securities that provides market data, counterparty verification and order execution for broker-dealers and institutional investors. **Palico** is a Paris-based firm aiming to streamline the secondary market for private equity. **OurCrowd** is a global crowd investing platform for accredited investors. **Fundbase** aims to make alternative investing more accessible and efficient, allowing investors to find, trade and monitor high-conviction investments while communicating and collaborating with one another.

INFRASTRUCTURE

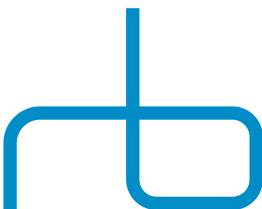
Infrastructure companies are intriguing because they often fly under the radar while being indispensable.

Quovo is a data platform that provides both fintech companies and traditional banks with connectivity and insights for millions of consumer financial accounts across more than 14,000 different institutions. The company's APIs, modular applications and enterprise solutions help predict, transact and personalize their services more effectively.

Plaid began with APIs that amplified data liquidity, connecting financial institutions with consumers and developers. The company now offers analytics products alongside data access. One of the first fintech unicorns, it was acquired by Visa for $5.3 billion in 2020.

Harvest Savings & Wealth Technologies (formerly known as Trizic) provides integrated savings and wealth solutions for the financial industry, essentially serving as a robo for banks. In a sign of things to come, Creative Planning (a major independent advisory firm) took a stake, expanding its access to the mass affluent market and insuring itself against disruption by independent robos.

True Potential delivers a similar value proposition in the U.K., where it provides an integrated wealth management technology platform for advisors. The platform streamlines the entire engagement with investors, with customized plans, client onboarding, fee and commission reconciliation, client servicing support and a client portal. It is used by one out of five financial advisors in the U.K.



DriveWealth offers a cloud-based, API-driven brokerage infrastructure that can theoretically drive any investment experience desired by the client. **InvestLab** provides a customizable trading platform via a SaaS (software as a service) model to retail brokerages, whose customers can access any market around the world while trading almost any equity, option or commodity available.

INFRASTRUCTURE (CONTINUED)

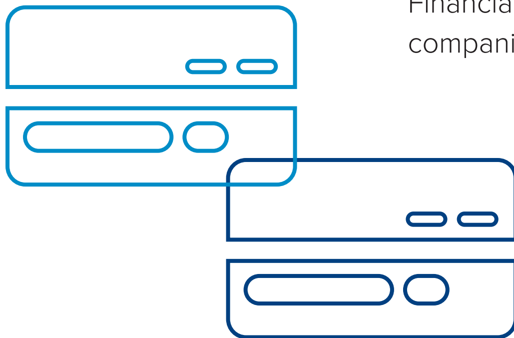
Based in Austria, **Wikifolio** serves traders who are confident that they have something others will want, empowering them to turn their portfolios into fully-fledged financial products (“wikifolios”), listed on Europe’s leading exchange for structured products.

Kurtosys helps financial firms go digital—a transformation easier said than done, since it involves orchestrating a flood of data from various sources in myriad formats.

PAYMENTS

Airwallex is notable for focusing on reducing friction for globalizing businesses. It positions itself as a technology company offering an “end-to-end global financial services platform” for its business clients. Already one of only a few Australian “unicorns,” the company’s most recent round of its $360 million funding came from Salesforce, pointing toward potentially powerful synergies.

No discussion of platforms would be complete without mentioning **Ant Financial**. The Alibaba affiliate famous for once having the world’s largest money market fund, it has quickly evolved to become a financial services powerhouse in China. With its roots as a facilitator of payments, the platform model is in its corporate DNA. Its subsidiary, Ant Fortune, with more than 100 asset management firms offering over 4,000 investment products, offers a glimpse of the future of wealth management.[12] Even with a relatively modest footprint outside of its home market, Ant Financial is already one of the world’s most valuable financial companies, with a valuation in the neighborhood of $200 billion.[13]



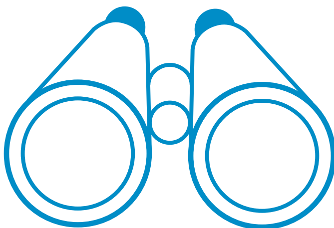
WHAT'S NEXT

We observed in *The Upside of Disruption* that asset management firms are facing a classic case of the Innovator's Dilemma: "Do they embrace disruptive technologies and business models, which may not be profitable for some time, could undercut current product lines and may not succeed at all?" As they weigh this critical decision, some lessons can be learned from Amazon's journey.

INVESTMENTS

Amazon pioneered the modern e-commerce experience, conditioning consumers to expect personalization, convenience, product reviews, insightful recommendations and instant gratification (or at least next-day delivery). Every business is now forced to compete on the customer-experience front.

It is also worth noting what Amazon hasn't done. Despite the potential use of virtual reality in online shopping environments, VR is not a technology the company has chosen to explore in any great depth. Despite substantial investment and no lack of enthusiasm dating back nearly three decades, virtual reality has failed to find a place in our day-to-day lives, and Amazon has to date shown no need to be a pioneer in this regard. Innovation can be a tricky process littered with unanticipated obstacles and dead ends; promising technologies can prove to be solutions in search of problems. For Amazon at least, the basics are vastly more important, and profitable, than bells and whistles.

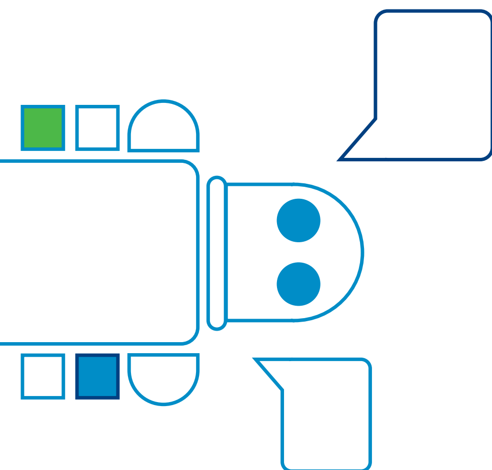


PLAN FOR PRIVATE LABELS

Platforms can provide much needed visibility to smaller vendors, but there is a potentially deadly downside: There is little stopping the platform itself from entering certain product categories, leveraging knowledge it has collected on which features and attributes are most appealing to customers. Amazon has moved into its own private label products in a big way with AmazonBasics (household), Essentials (clothing), Collection (jewelry), Elements

(vitamins), 365 (food) and many other verticals. A strategy pioneered by supermarket chains, private labeling requires scale and a deft touch to succeed. Precursors exist already in asset management, of course, in the form of subadvisory relationships. Any successful platform in financial services should be expected to expand this concept to some degree. Vendors typically don't like the idea, but they may not feel that they have much of a choice, and in fact may embrace it if greatly expands their distribution base. That said, more prominent brands might choose to step away and plant their flag elsewhere, much as Nike did with Amazon.

THE ROBOTS ARE COMING



It doesn't require a dystopian view of the future to acknowledge some facts about the relentless forward march of technology. At companies like Amazon, for example, it is becoming evident that people are often the weakest links in processes designed to provide the most satisfactory experience for end users. Robots are still commonly thought of as warehouse workers, but they are effectively managing human employees in many cases. Algorithms still work for investment professionals, but advances in machine learning mean that dynamic may slow down or even be reversed before long.

TECHNOLOGY IS NOT ENOUGH

Technology is at the heart of the current revolution in financial services, but it is insufficient on its own. Human expertise is required to effectively harness the power of technology in many cases. Consider the relatively cloistered world of illiquid asset classes. Barriers to investing are already being lowered and we expect illiquid assets to be a key area of focus for platforms in the not-too-distant future. But simply setting up an exchange is insufficient. The insights of industry professionals need to be translated into tools that can be used effectively by newcomers.

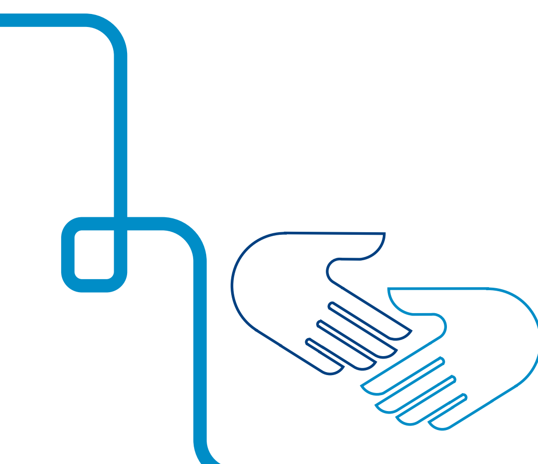
Amazon has hired an army of specialized labor through hiring and a steady stream of acquisitions. Their systematic approach to filling positions that haven't yet been invented might be hard to fathom for asset managers with collegial cultures more used to making key hires from the same few universities and competitor organizations.

BEWARE THE FAST FOLLOWERS

Innovators get the glory, but every MBA student knows that being a "fast follower" can be an equally effective, and perhaps more profitable, strategy. Netflix, for example, pioneered video on demand by sending DVDs to people in their homes. While initially making pricing miscues, they pivoted to online delivery as soon as the bandwidth became available. When capital became available, they plowed it into producing original content. The company's successful case study will be analyzed for years to come, but Netflix faced a suddenly formidable competitor in late 2019 with the launch of Disney+. Building an online distribution platform for one of the most storied media catalogues in history would seem like a no-brainer, but it wasn't without risks. Nevertheless, within five months of launching the service, Disney+ passed 50 million paying subscribers.[14] Netflix CEO Reed Hastings went so far as to praise the Disney+ rollout as the best example he'd ever seen of an incumbent disrupting itself.[15]

DON'T SCARE OFF YOUR PARTNERS

Ceding too much control to distribution partners has long concerned companies in many sectors, and online commerce is no different. Amazon has seen its share of defections in recent years, including giants like Nike, who opted for a direct-to-consumer model in part because they wanted to stamp out grey market distribution and counterfeiting.[16] They are not alone. Vans, Rolex, Louis Vuitton, Patagonia and The North Face are among those that have also cut the cord. That being said, it will be interesting to see how well they fare through the COVID-19 pandemic compared with Amazon.



Smaller companies would find it more challenging to live without the distribution reach, logistics and fulfillment offered by Amazon, but this may change as marketing is increasingly done via social media and a growing ecosystem of companies provides the products and services necessary to deliver a high-quality customer experience online. In the retail world, this includes companies like Shopify, Stripe, Affirm, ShipBob, Returnly and Darkstore. Shopify alone powers more than one million independent online shops. A growing ecosystem of fintech firms looks to mirror this development.

THE IMPORTANCE OF COMMUNITY

Amazon itself has never really built a community, but its system of reviews serves some of the same functions, operating as a forum for dialogue. While the review system is open for misuse, it offers radically more transparency, allowing peers to validate or condemn a product and fixing a bright light on marketing claims and subjecting them to the scrutiny of other consumers. More recently, the remarkable success of Twitch as a video-based community might (subject to regulatory approval) illuminate the path to a new type of interaction among investment professionals and their clients.

REVENUE STREAMS WILL BE REARRANGED

Fee compression has been unavoidable for many managers in recent years, and the growing role of platforms would presumably exacerbate that trend. But this assumes that investment products are increasingly treated as commodities. This is likely to be true for a large swath of the industry, but it does not tell the whole story. As private securities become more liquid and mainstream and machine learning is integrated into a growing number of algorithmic strategies, it is entirely possible, if not likely, that emerging platforms will permit the blossoming of an unprecedented variety of investment products.

FEAR SHOULDN'T OBSCURE THE OPPORTUNITY

Change can be terrifying, but platforms have empowered as many businesses as they have threatened. Sites like TripAdvisor and Yelp can be controversial, but they have also shone a light on outstanding products and services, permitted businesses to learn a great deal more about customer preferences, and enabled new strategies for engaging customers. Platforms such as Amazon accrue a tremendous amount of wealth, but they also democratize markets, opening doors for smaller firms that would have had no ability to compete on a larger stage.

FINAL THOUGHTS

In 2016, we wrote in *The Upside of Disruption* that "Amazon has shown what can be built by starting with the customer and working backward." We should note that while Amazon did indeed build its business based on creating an excellent customer experience, it established its retail hegemony by sacrificing profits for market share over many years. Only in 2019 did operating margins begin to consistently exceed 5%. For most of the previous decade, they hovered between 0% and 3%.[17]

If this sounds familiar, it is because the firms winning the most new business in asset management are the ones most committed to low prices. Investment strategies, of course, are not fungible commodities. Passive investors have benefited from a combination of low cost and high returns for many years—on the back of the longest bull market in history—but it is not hard to imagine a less buoyant or highly volatile market environment taking the shine off of all that beta exposure. Differentiation will always have a place in asset management due to the varying preferences, needs and perspectives of investors who are ultimately more concerned with value than with the lowest price.

This is why platforms will be so critical in the industry going forward. By lowering the barriers to entry and offering easy access to talented investment professionals alongside innovative tools, liquidity and transparency, emerging Amazons of financial services will ultimately improve the investing experience for both individuals and institutions. Most investment firms do not aspire to be platforms. It isn't in their DNA, their goals or their aspirations. That doesn't mean they can ignore Amazonization: Not having an actionable plan for emerging platforms is laying a course toward inevitable failure. More importantly, it could mean missing the opportunity of a lifetime.

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