Welcome to the LendIt Fintech One-on-One Podcast, Episode No. 341. This is your host, Peter Renton, Chairman and Co-Founder of LendIt Fintech.

(music)

Before we get started, I want to talk about the 10th Annual LendIt Fintech USA event. We are so excited to be back in the financial capital of the world, New York City, in person on May 25th and 26th. It feels like fintech is on fire right now with so much change happening and we'll be distilling all that for you at New York's biggest fintech event of the year. We have our best line-up of keynote speakers ever with leaders from many of the most successful fintechs and incumbent banks. This is shaping up to be our biggest event ever as sponsorship support is off the charts. You know you need to be there so find out more and register at lendit.com

**Peter Renton:** Today on the show, I'm delighted to welcome Ryan Zacharia and Adam Aspes. They are both General Partners at JAM Opportunity Ventures which is part of Jacobs Asset Management which is a well established money manager focused on financial services space, but they have a new joint venture called JAM FINTOP which is super interesting and I wanted to get them on to talk about that.

Here, they've created a fund where all of the OPs of the fund are actually community banks and we wanted to talk about the first fund they've created, the Banktech Fund, which is investing in technology that is going to help banks and then also their second fund which is a specialized blockchain fund which is super interesting. We get into both of those funds in some depth and we also talk about how banks really are thinking about the future of technology, how they're thinking about blockchain. We end with this really interesting perspective from Adam and Ryan about the future of financial services. It was a fascinating episode, hope you enjoy the show.

Welcome to the podcast, Ryan and Adam!

**Ryan Zacharia:** Happy to be here, Peter, thanks for inviting us.

**Adam Aspes**: Thanks, Peter.

**Peter:** Okay, my pleasure. So, I'd like to kick it off by getting a little bit of background from both of you guys. Just tell us a little bit of what you've done in your career to date. Ryan, I'll start with you.

**Ryan:** I'm a General Partner at JAM Special Opportunity Ventures, we invest out of two venture capital funds. Before that, you know, I was working at Jacobs Asset Management where I still work as Director of Research covering financial stocks and private companies in and around the financial services ecosystem. Prior to that, I was an Investment Banker in Citigroup's Financial Institution Investment Banking Group.

**Peter:** Right, and Adam?

**Adam:** Twenty five-year history investing in US financials combination on the buy side and sell side, but across equity research, sales trading, investment banking, did a little bit of everything the last six years at Jacobs Asset Management,

**Peter:** Right, let's get right to it. I want to talk about the origins of JAM FINTOP and JAM, obviously, is the acronym for Jacobs Asset Management, but tell us a little bit about how you guys came together.

**Adam:** So, JAM has a 27-year history investing in US financials, we do it through a hedge fund and private equity funds and focus on US financials, but primarily heavily focused on community banks and what we recognize over the last couple of years was that community banks were clearly falling behind the curve on technology and, you know, for me that experience was really amplified as a board observer of a bank that we had a position in. The bank was effectively having to make a decision on whether or not to upgrade their technology or sell the bank and when we got inside and really saw how the sausage was made, it was kind of frightening that what you saw was bank cores that were built in the 70s and 80s on COBOL technology, that you had ACH systems as a payment rail that was built in 1974, that you had really a huge lift in order to build the modern tech stack.

That bank decided to sell, but coming out of it we said, we really need to spend much more time on the future of financial services, what's the future of banking. You know, Ryan and I really spent time going across Silicon Valley, venture capitalists and what we did is we formed a relationship with a venture capital firm called FINTOP. FINTOP's based out of Nashville stands for Financial Technology Operators where all the general partners were former entrepreneurs and operators that built, run, sold fintechs, you know, super impressive group and we had a shared vision on what that future of community banking was.

We just loved what they were doing there investing in the Series A rounds of the technology that the banks need to know about in order to remain relevant and competitive and just said, I think we should do a fund together, let's do a JV, 50/50, we'll go and raise capital from the banks that we know and we have this deep relationships with and we're going to make sure they are up-to-date and have modern tech stacks. And so, it was sort of an idea on paper, we weren't sure if it was going to work, but we started talking to banks and there was sort of an overwhelming response, went out to raise $100 Million, run of having to cap the size of the fund at $150 Million after being pretty wildly oversubscribed, raised money from 66 community banks. Those banks collectively had $650 Billion of assets and that fund closed in April 2021 and we've been actively investing out of it ever since.

**Peter:** Who are the banks in the network because when I looked at your list you're not talking about a small town bank with $100 Million in assets, right, so just tell us a little bit about the community banks that are in your network.

**Adam:** It's a pretty diverse set of banks so we'll talk about the blockchain fund that we're doing now, but, collectively between the blockchain and the Banktech funds, we now have about 80 banks in our network and it's very diverse. We've got banks in the high end that are, you know, $88 Billion in assets, but we do have banks that are under a billion on the low end and so it is a pretty wide range of banks. But, what they share in common is a tech forward vision and mindset and that what we've realized is it's not really about the size of your bank, it's really about, you know, are you innovative and do you have a vision of the future.

I should say when we started this vision, it was a very bearish vision of the future of community banks and that there was just no way for them to be able to compete. And I'd say as we stand here today, we're super bullish on the small innovative banks that want to lean in and build the modern banking system because the future is open, embedded, blockchain rails, modern cloud course, artificial intelligence, any bank can build those rails. The big banks are, effectively, in some ways at a competitive disadvantage because they can't untangle the mess that they're in and so, you know, there's an opportunity for every bank in that network to really lean in and build the bank of the future.

**Peter:** Right, right. And so, from what I understand on your website looking and reading your materials, you're more than just an investor, right. You're providing investments just like you're engaging with your banking network in a variety of ways. Tell us some of the ways you're actually doing that.

**Adam:** So, we hired a fulltime bank analyst to work with the network, he's on the phone with them every day talking to them about their pain points and opportunities, we did 180 demos in the last nine months of last year where we introduced fintechs to the banks and just telling the banks, this is technology, you need to know about to remain relevant, we do monthly webinars with our portfolio companies, we'll have an annual conference in Nashville later this year, we've got six committees that are constantly engaged. You know, one committee is only for CIOs, one is for the Executive Team, we just talk about emerging technologies, about mindset and so tech surveys were super engaged on knowing what the banks need and that's where we try to position our investments so that we're actually solving their problems.

**Peter:** So, can you tell us a little bit about some of the investments. You said you raised $150 Million, tell us a little but about some of the investments that you've made and how much of the fund has been deployed.

**Ryan:** We've made nine investments, so far, we've deployed about 15% of the capital and central to FINTOP's, you know, investing philosophy, we're not really investing in consumer banking technology so a lot of it is kind of plumbing, infrastructure, the guts of financial services. So, what really excites us are things around process automation, automated underwriting and lending payments platforms so that's where we've got to focus a lot of our kind of deal prospecting and investing.

There's companies like Monit that we've invested in that kind of enabled the bank to embed itself within the accounting systems that small businesses are using and that kind of provides the banks with this rich data set that they can then use to kind of provide credit. We have a company, Treasury Prime that is effectively Banking-as-a-Service enablement and really what they're trying to do there is facilitate the middleware between innovative banks and disruptive financial technology companies and really kind of satisfy what we think is a very lopsided supply/demand dynamic between the amount of innovation and deposits and lending opportunities that are up for grabs versus the amount of banks that have the desire and ability to integrate with those fintechs.

And then, we have another company as an example called Tax Status that is effectively core infrastructure that facilitates the electronic capture of full IRS tax transcripts direct from the IRS and effectively lenders and servicers can use that information to create underwriting score cards kind of for loan surveillance. They are kind of getting real-time information which means tax liens are placed and they're also kind of getting direct from IRS filings information as opposed to relying on potentially fraudulent PDF uploads of tax returns.

**Peter:** Okay, interesting. I'm curious about….you said you're only 15% deployed with the Banktech Fund, but you decided to create a new fund just simply focused on blockchain. What was the thinking about that rather than just having this come out of the Banktech Fund, why create a new fund?

**Adam:** So, blockchain was always on our radar for all the reasons, you know, cheaper, faster, programmable. replacing trust with truth, but banks have been hesitant to adapt blockchain technology for a variety of reasons, let's say mainly regulation and cyber security and so the Banktech Fund has this huge pipeline that we're working through right now and there's no shortage of idea flow there. What we saw with blockchain is we wound up meeting with Mike Cagney of Figure last spring when they were doing their Series D, Figure was not a suitable investment for the Banktech Fund because that really focuses on Series A investments, but what we saw with Figure is that they have built Provenance.

Provenance is an open decentralized blockchain that was purpose built for financial services with bank grade AML/KYC and they are building proof of concept and we started to see that this was actually a blockchain that we felt banks could actually build on. You know, Mike saw the network of banks that we had, thought it was super interesting, we'd locked some introductions. Because of the engagement that we've talked about, we knew the banks in our network that had actually been asking for blockchain investments and had sort of raised their hand if we run into anything so we started making introductions. The first two banks that we introduced them to, New York Community Bank, NBHC, within a month they had announced strategic partnerships and are actively pursuing multiple endeavors together. So, we saw that the opportunity was actually to build something unique and big and real, but it was much more offensive.

The Blockchain Fund is really having a vision of all assets that can be digital assets will be digital assets. The digital asset market, as Ryan likes to say, will go from $3 Trillion to $30 Trillion, but it's not there today, this is for the banks that want to lean in and build that future where the Banktech Fund is really about we need technology today that can plug & play, operate outside of our core to remain relevant, competitive and build that bridge until…whether it's three, five, seven years from now when we are riding on cloud-based cores, artificial intelligence in a true, fully modern banking system. So, that's the Blockchain Funds for the future, Banktech Fund is relevant for today.

**Peter:** Right, right, okay. So, is it fair to say then it was really a sub-set of the banks in your network that are really interested in blockchain and actually put their money in?

**Adam:** There's a lot of overlap, but we're also seeing that some of the larger banks are ready to move on blockchain rails today leaning in so the newer banks that came in are sort of $50 Billion asset banks and larger and they are actively pursuing live blockchain technology projects today.

**Peter:** So then, the other banks, I guess what's the resistance from the other banks in your network, do they feel like it's too soon, it's just not something that's even going to impact banking? When you're talking to these people, what do they say they don't like?

**Ryan:** Yeah. I mean, I think that it's still, at this stage, very emergent technology and I think that two of the things that regulated financial institutions are most concerned about are cyber risk and regulation. I think everyone kind of sees the value and potential of blockchain, it's really important to try and de-couple what heretofore has been about cryptocurrency and speculation from, you know, kind of the power and potential of open source decentralized immutable ledger and that I think is easier for some institutions to grasp than others. The vision that Adam talks about of digital assets going from $3 to 30 Trillion and cryptocurrencies being just kind of sub-set of that and their being kind of this whole universe of traditionally analog assets like equities and loans and securities as digitally native I think is not something that feels like a here and now for a lot of banks so they feel like they can be fast followers when those opportunities present themselves.

So, I don't think it's really resistance, but it's a matter of triaging what are some of the most important tech investments for banks to make and think that right or wrong, some banks don't view blockchain as being something that they need to develop competency with right now. But, I also think that when you think about where regulation sits today, that kind of makes sense. I mean, it's still murky, it's still early, we have to kind of move away from this idea of anonymity first and the perception of tax dodging and really moving to blockchains that are helping bridge regulated gaps with the Decentralized Finance world.

**Peter:** Right, for sure. So, I want to go back and talk about Mike Carney who we've had on the show several times. I think a lot of the listeners would be aware of the work he is doing at Figure and the Provenance blockchain, but he's been in the news in recent few weeks about the USDF Consortium. Like the Stablecoin, Provenance is I guess issuing or the banks are issuing it, but the USDF Consortium has like, I think they announced five banks publicly, do you have a formal partnership with Figure because, obviously, the banks in the network can all be potential partners, you know, part of the USDF Consortium so tell us a little bit about that.

**Adam:** There is no formal relationship with Figure, they are a lead investor in our Blockchain Fund, we don't have any obligation to work with them or invest alongside with them or do projects specific to Provenance and we fully expect that we will do things on Provenance as well as other layer one watch-ins so the Fund is taking kind of a blockchain agnostic approach. At the same time, you know, the talk about regulation being kind of one of the main impediments for regulated financial services to lean in on blockchain, I feel like Figure which itself has hundreds of state and local licenses to be able to lend and move money on chain has created a level of comfort I think for regulated financial services. So, I think Provenance, definitely, has an ecosystem that lends itself to buy-in from regulated financial services companies, that kind of speaks to our informal relationship with Figure.

Mike Cagney is going to be leading our Blockchain Committee as part of our engagement with our limited partners that'll convene three or four times a year and just speak more broadly about blockchain innovation. The USDF Consortium is separate and distinct so we're a founding member of the consortium subject to the Admissions criteria on the Consortium's website, any bank could effectively join that so that is kind of separate and apart from an investment in our Fund and that's really the way we are thinking about USDF or other Stablecoin is that we take the perspective than an order for digital assets to really reach kind of a critical mass and take off and move beyond the current use cases.

But, there needs to be a big infrastructure layer built out and that's going to encompass things like data solutions and compliance and BSA/KYC and AML and on-chain identity and how we bridge legacy data systems to be able to bring that information on chain and digital asset custody and value transfer. So, how do we facilitate in a compliant manner the ability to move money on chain and from our perspective, the existing kind of privately issued Stablecoin didn't really solve for that and so that's where kind of USDF comes in. So, USDF is a bank-issued Stablecoin, banks are the only minters of the Stablecoin and it operates within the confines of the robust regulatory infrastructure that already exists for depositories.

**Peter:** Right, right. And quick plug, if I may, we've got Mike Cagney, he's going to be on our Keynote stage, our big USA event in May along with a couple of the banks in the USDF Consortium, we're going in-depth on that there. I think it was the President's Working Group or one of the papers that came out recently, talked about banks should be the issuer of Stablecoins and it sounds like that's your thesis and, I mean, as far as the whole regulatory piece that is still, I would say, in development. Is that your thesis that banks will ultimately be enabled by Congress to issue Stablecoins?

**Ryan:** Yeah. That is our thesis that banks are going to be the formal bridge to Decentralized Finance and the way it'll happen is a bank regulatory construct for Stablecoins. Now, whether, it in perpetuity exists only at a bank process or if there are other people that can get access to special purpose charters or trust charters in order to do it remains to be seen, but from where sit today we feel like the regulatory framework, by and large, already exists for banks to be able to do this. I mean, this is already relevant and germane for the business of banking, it's not enabling anything that's incredibly unique, it's the programmability of money and being able to interact with applications that are built on chain, but the core functionality of facilitating payments and the settlement of securities transactions is, you know, not that revolutionary.

**Peter:** Right, right, that's really true. So, I'm interested about some of the advices of other advisors you're working with, you mentioned Cagney, but looking through the deck that you sent, you've got some other interesting names on there as well.

**Adam:** So far, Banktech Fund, our advisors for the ICBA which is they probably represent the most banks in the country then two fintechs, FISPAN and Numerated, and then for the Blockchain Fund we have an advisor, the MBCA which represents over a hundred banks, over $10 Billion in assets so really focusing on the banks that have the ability to lean into blockchain today. And then Piper Sandler came, they're an investment bank that probably has the deepest tentacles across the financial services landscape, they just set up a digital assets group recently and really want to be known as a thought leader in the space and, of course, Figure. As Ryan said, Mike Cagney will lead our Blockchain Committee.

**Peter:** Right, right, okay. So then, is it fair to say, you talked about the Banktech Fund being really the back office, the infrastructure needed to, you know, run these banks in the future, is that the same sort of thing? I mean, Ryan, you did mention that like some of the things that you're interested in, but is that the focus, is it going to be sort of the infrastructure piece?

**Ryan:** Yeah. I mean, I think that that's our competency and I also think it's what's needed the most. So, you know, we think about the investment landscape for investing and blockchain as, you know, you have layer one, you have an infrastructure layer, you have an application layer. In the application layer is got to where the really cool things happen, but we think before you can get to that point at scale, you need to build out the infrastructure and right now, I think we're seeing that the industry needs more of that.

We need more digital asset custodians, we need more solutions that bridge the gap between the legacy system and the blockchain, we need to think about ways to bring customer information on chain and interact with those wallets, we need to think about how we solve for some of the compliance challenges and regulation and law so we're taking kind of a walk before we run approach. The early stages of our blockchain investment focus are going to be around this infrastructure layer then I fully expect that as that's being built out, and that is happening somewhat quickly, but that's when we'll start to see some really compelling applications that are built leveraging the layer one and the infrastructure layer that has been built over the previous year or two.

**Peter:** Right, right. And we should point out too so the listeners are aware, I mean, with Provenance and Figure, every loan they've done, they've done billions of loans now, everything has been done on chain for their company. All the transactions that have happened and loans sales, that's all happening on the blockchain so there is some infrastructure already built. People need to know about that, but you just announced this Fund, I mean, is it too early to kind of talk about some of the companies that you're looking at or, I presume you haven't made an investment yet or where are you at?

**Ryan**: We have not yet made an investment, we have a deal pipeline that's around 55 names, it appears to be taking kind of somewhat of a barbel form so I think there's some early-stage companies that are really interesting and exciting, you know, in some of these infrastructure categories that I mentioned. And then there are some that are just kind of further along so Series B, C names that have gotten some traction already and those are some of the digital asset custodians that we've actually recently seen raise capital, names like Anchorage or Fireblocks that are, you know, have built some infrastructure and licensing and have some kind of regulatory moat in place already and customers and brand recognition.

And then there's some companies that are solving kind of aspects of the KYC value chain, these are companies like Elementhis or Notabene that we think are interesting and we're kind of speaking to anyone and everyone in the space who's trying to tackle some of these problems with an eye towards companies that view regulated financial institutions as part of the future. So, you know, we have kind of drawn a little bit of the line in the sand that we are not DeFi purists, we do think that there is going to be some kind of hybrid that emerges and so it's obviously important as we look to deploy capital that we're investing with companies that view banks as, you know, an important end market for them.

**Peter:** So, some of the companies you mentioned there, they are pretty well established, I mean, are you still looking at Series A type investments or are you going to go across the board?

**Ryan:** I think it will be a little bit broader in the Blockchain Fund versus the Banktech Fund. Banktech Fund really tries and maintain that discipline of early-stage companies at or around a million dollars in annual recurring revenue. I think the Blockchain Fund will look at maybe even earlier-stage companies, but I think it'll look at later stage companies so some of that Series B, C, we would absolutely entertain making investments across that spectrum because we're really going to be driven on where we see the greatest need to bring regulated financial institutions into the ecosystem. As in the case of the Banktech Fund, a lot of the investment processes are going to be driven based on the feedback that we're getting from our network of investors that are telling us what the impediments are, what their pain points are, where they're looking to, you know, make technology investment.

**Peter:** Right, right, okay. So, I'd like to end with hearing from each of you, if I could, about the future of, you know, banking, it feels like this wide-open field here, there's a lot of ways this can go and maybe, Adam, I can start with you. Maybe you can take us through…and Ryan, be prepared, I'm going to ask you about the longer term future, okay, but, Adam, maybe you can take us through the next like three to five years. How are banks going to change and what the future of banking is going to look like.

**Adam:** So, we see a future that's open and embedded and moving to a cloud-based course, artificial intelligence, blockchain rails, lots of digital assets that the gap that you're talking about in the next three to five years, it's everything you can do to plug & play outside of your core so that you can start building that capability. We think that a lot of banks are going to start spinning up digital banks on the side because their legacy cores are just too hard to untangle and we think there's going to be a very, very significant ramp with Banking-as-a-Service.

We believe that Banking-as-a-Service deposits will grow from $50 Billion to $1 Trillion over the next five years and so you have a huge surge in Banking-as-a-Service and then embedded lending. We've seen a huge growth in embedded payments, but what we're going to see next is embedded lending, it's going to go through the roof and banks need to be prepared for that. We need a bank to meet the customer where they live which is in their software, they need to get connected to the balance sheet, the income statement, statement of cash flows and make their lending decisions based off of that information.

**Peter:** Right, right. And, Ryan, I know you have touched on a couple of things, but I'd love to get your view on sort of longer term future, like banks are…they've embraced the blockchain, they may have embraced DeFi and how that actually is going to look.

**Ryan:** It is possible that the bank of ten years from now does look quite different than it does today and the business lines they're in could be very different. I still think that banks have proficiency when it comes to making loans and underwriting credit and understanding some of the nuances of a given industry or geography. It's possible that the way that loans get funded could change and they could seek out the most efficient forms of capital and DeFi could be an important part of that. So, it's possible that you see banks ten years from now embrace a bit more of a capital-lite model where they're really leaning on the things that they do best and leveraging DeFi to provide kind of the most efficient cost of capital for their customers.

If I'm a bank today, I need to be thinking about how open-minded I am to the potential that my core functionality changes significantly ten years from now and how well set up I am for that, have I developed competency and ability to interact with digital assets and are there any kind of adjacencies or interesting business plans that I can develop off of that competency. We could be on the precipice of a pretty big shift in how we think about what our banking relationship is and it might be something very different from, you know, what we're accustomed to today.

**Peter:** Right. Well, it's going to be super interesting. I feel like there's so much happening right now in the world of finance, it's going to be an exciting time for the rest of this decade to see what the banks do actually. It will actually look very different or whether they'll sort of maintain their core competencies and are just evolving, but regardless, thank you very much for coming on the show today, guys. Ryan and Adam, I really appreciate it.

**Adam:** Thanks, Peter.

**Ryan:** Thanks for having us, Peter.

**Peter:** You know, when I listen to people like Ryan and Adam talk about the future of financial services and about some of the things they're actually doing to really help enable that future, I mean, I just find it so exciting. I feel like we're at this inflection point where there's a lot of change that is in the air, there's a lot of change that's happening. There's some new things that are being developed that haven't got traction yet, but particularly when it comes to traditional banking that when I look at some of the things that are in development, I get really excited.

I feel like, as sort of Ryan said towards the end there, the future in ten years could look very, very different. Banks are still going to issue loans, they will still take deposits and do a lot of the traditional things they've done for decades or even centuries, but the way they do it and how efficient they are and the way the sort of financial services are delivered to consumers and small businesses is going to be very much different and it's going to be far better and I'm excited for that day.

Anyway on that note, I will sign off. I very much appreciate your listening and I'll catch you next time. Bye.

(music)

Before we go, I want to talk about the 10th Annual LendIt Fintech USA event. We are so excited to be back in the financial capital of the world, New York City, in person on May 25th and 26th. It feels like fintech is on fire right now with so much change happening and we'll be distilling all that for you at New York's biggest fintech event of the year. We have our best line-up of keynote speakers ever with leaders from many of the most successful fintechs and incumbent banks. This is shaping up to be our biggest event ever as sponsorship support is off the charts. You know, you need to be there so find out more and register at lendit.com.