Commercial Partnerships

What can banks learn from the Roman Empire? Rather a lot.

JOHNSTON CARMICHAEL

Partnerships are in vogue.

Not so long ago, FinTech and InsurTech firms were thought to present an existential threat to traditional financial services providers and their market share. 'Adapt or die' became the mantra. Fast forward a few years and what have we learnt? In the main, both FinTech firms and incumbent financial institutions have realised that there is more to be gained by working collaboratively together than there is from competing aggressively. For example, RBS partnered with Starling to utilise their transaction infrastructure for their standalone bank, Bó.

Indeed, each has strengths or core capabilities to offer that the other wishes to access. The incumbents desire the innovative technology and service offerings that the nimble FinTechs can develop at pace, whereas the FinTechs desperately want access to the large customer base of the incumbents. The natural way to bridge the capability gaps for both parties is to consider developing some form of partnership or alliance.

However, partnerships can be very difficult to launch and make successful if a well thought through strategy and plan is not in place or followed.

Lessons from history

The well-known phrase that ‘those who fail to learn the lessons of history are doomed to repeat it’ should certainly be applied in the case of forming partnerships and alliances. These challenges are not new, from the current political challenges of the European Union and stretching further back to the Roman Empire.

This article will explore the key themes which enabled the Roman Empire to expand from its mythical founding as an Italian backwater in 753BC to the height of its power covering 5 million square kilometres in 117AD, applying their success stories and failures to the challenges facing modern financial institutions as they look to grow through partnerships and alliances.

Doing so will inform a strategic framework which the reader can use to make conscious and thoughtful decisions about their future partnerships and alliances, whilst avoiding some of the mistakes from history.

Developing a framework for partnerships

As the Roman Empire expanded, their leaders had to ensure that the resources at their disposal were fully optimised. In order to do so, it appears that five questions/considerations helped in their decision making process:

1. Does it make **strategic sense** to operate in a particular territory? Are there geographical advantages of doing so e.g. securing grain supplies or the Empire’s frontier? Might we be extending ourselves too far, leaving us vulnerable to attack on another front?

2. Does it make **commercial sense** to agree an alliance? Will the new territory lead to greater overall value for the Empire?

3. Are there insurmountable **cultural barriers** to the alliance? Can we accept the customs of our allies (and vice versa)?

4. What **structure** should the partnership take - imposition of direct rule vs. a hands-off approach?

5. What **action** is required now (and may be required in the future) to support our partners? Will they need defending from competitors?

Of course, it would be folly to assume that these were always considered by the ever ambitious Roman senators, but it appears that the most successful alliances considered the five dimensions of: strategy, commerciality, culture, structure and action.

Johnston Carmichael's Partnership Development Framework

Johnston Carmichael's Partnership Development Framework draws on these parallels as well as industry best practice to show that, in order for financial institutions to successfully partner with third parties (such as FinTech firms), they need to successfully answer five key questions.

Partnership Development Framework

Strategy

Why, **strategically**, should we expand by alliances or partnerships rather than direct competition?

Commercial Agreement

Will the **commercial** agreements in place ensure both parties are incentivised?

Cultural Alignment

Is there **cultural** alignment or an acceptance of cultural divergence?

Structure

What is the most effective way of **structuring** the partnership?

Action

What **action** should be taken to create and maintain the partnership?

Strategy

As the Roman Empire and population grew, they increasingly relied upon imported grain. Egypt was a grain rich exporter and struck an alliance to support the Romans during their wars with Carthage (roughly modern Tunisia) in the 3rd century BC. However, when Egypt became embroiled in the Roman civil war many years later, the strategic importance was so great that the relationship could no longer be entrusted to an alliance - leading to the effective take-over of Egypt by Augustus in 30BC.

This strategic shift shines a light on an important consideration for financial institutions - in which areas of your ecosystem can you afford to rely on an alliance and when / where is it most desirable, strategically, to build your own capability?

A number of strategic rationales may exist, including:

1. Providing a short-term plug for an existing capability gap which, unless filled, will leave the institution behind e.g. TSB partnering with Jumio to offer account opening via a selfie (following in Monzo's footsteps).

2. Putting in place a medium-term solution which enables the financial institution to learn from the FinTech provider whilst, in parallel, developing their own capability. Common examples include partnering with data analytics providers to leverage predictive models, giving banks time to clean, organise and analyse their existing data to build their own predictive models.

3. Seeking a long-term solution in recognition of the unique value add services of the partner. See Starling Bank's integration with third party apps such as Wealthify, PensionBee etc. as part of their long-term strategy to have a 'marketplace' app for financial products through API integrations.

Failure to lay out clearly the core purpose and rationales for the partnership or alliance could lead to the proliferation of vanity partnerships which add little value.

Commercial Agreement

When forming alliances, the Romans generally ensured their commercial 'ducks' were in a row. When Cleopatra's father became worried about his future, he lobbied (and bribed) the powerful senators in Rome to support him should his Egyptian throne be at risk. In return, the Romans received a payment for the military insurance policy - both parties benefited.

In order for any partnership to succeed, it must be a marriage between equals or at least a win:win situation. One party dominance / benefit is likely to lead to disinterest and a lack of investment in time and energy from the other. Indeed, it is important to remember that the reason for the partnership decision in the first place is that one party has something that the other needs (and vice versa!). This is why many outsourcing deals are doomed from the outset!

It is advised that following important elements of commercial alignment should be detailed at the outset and shared with all that will be exposed to the partnership.

KPIs	Complementary offering & overlaps	Conflicts & escalation points	Commercial pricing
Agree what success looks like for both parties	Outline the partner's clear and complementary offerings	Detail a clear plan to overcome conflicts, including escalation routes and decision frameworks	Define a clear commercial pricing model that values the contribution of both parties

Development costs	Intellectual Property	Group synergies
Outline a clear understanding of the development costs for both sides	Detail where the IP resides	Showcase where further group-wide synergies may exist

Financial Services example

The very public contractual dispute between Co-op Bank and Capita in 2016 is a good example of when partners fail to align commercial incentives - the tenure of this £325m contract was halved and both parties narrowly avoided expensive litigation.

Cultural Alignment

An interesting observation from Roman alliances was the laissez-faire attitude they seemed to take in relation to changing cultural norms. The Romans would subsume allied gods into their pantheon and in return, those allied to Rome would begin to adopt Roman statutes, customs etc.

Similarly, in financial services, if the incumbent institution decides that a partnership is the right model, they must ensure that they are willing to accept the cultural spillover effects of working with agile and innovative partners like FinTech's. Indeed, for some leaders, this is a positive side effect of the collaboration.

However, there is a risk of a culture clash (and prolonged culture wars!) if the incumbent is too entrenched in a "this is what we do around here" attitude. This is usually observed in relation to the bureaucracy surrounding decision making and the incumbent's appetite for risk - which can often be much lower than that of a FinTech.

There needs to be a willingness and realistic chance of achieving a 'cultural compromise' from both parties, otherwise the venture will be a non-starter.

Financial Services example

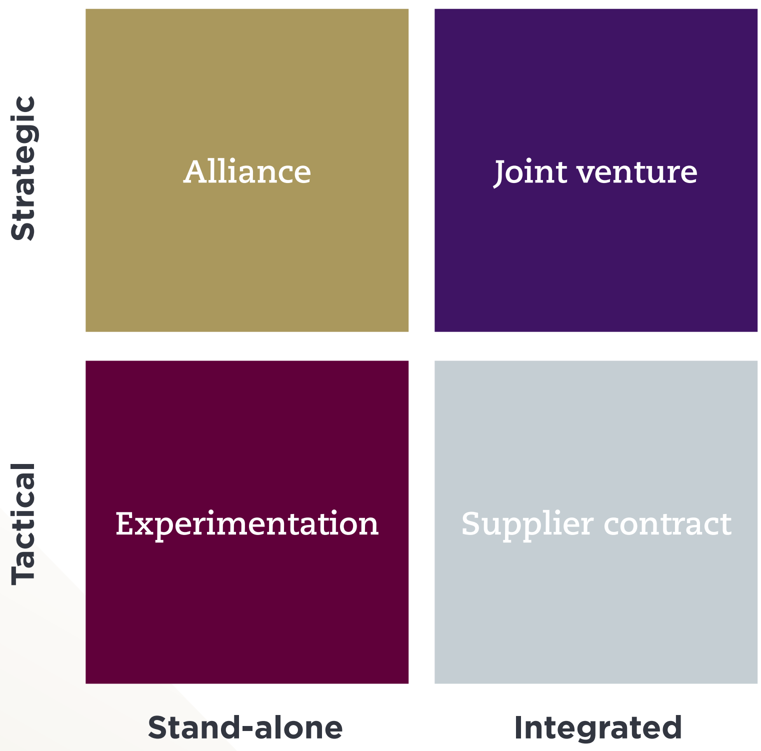
A recent example (albeit an acquisition rather than a joint venture or alliance) of a culture clash emanates from the acquisition by the 200 year old French bank, BPCE and the German mobile-only bank, Fidor.

The acquisition has failed to get off the ground, according to the press, because of irreconcilable cultural differences between the two parties. Indeed, the CEO and Founder of Fidor resigned in April this year, walking away from the company he founded in 2009. This case study shows that the cultural aspect of an agreement can be just as important as the commercials.

Structure

The Romans also had to work out the most effective structures to support their allies. Some provinces were directly governed with garrisoned legions, whilst others were left to pay protection money for their alliance, but had little interference from the machinery of Empire.

In our experience there are four main forms of partnership for financial institutions:



The form of partnership that is most appropriate depends on the strategy - there are pros and cons to each method.

Experimentation

Establishing an 'innovation lab' is a common way of creating an 'experiment' environment where the incumbent and partner firm can test their joint proposition with the market in a controlled way (perhaps testing the proposition on a particular segment). They can also co-develop propositions - particularly where the financial institution views themselves as an 'incubator'.

Pros:
- Impact felt quickly
- Ability to gain feedback and change tack
- No formal or long-term ties required
- Option to invest and 'try before you buy'

Cons:
- Only appropriate for short-term capability gap plugs (unless incubating)
- Missed opportunities due to a lack of integration e.g. integration across the product set may be limited
- Costly, particularly where the institution acts as an incubator
- Lack of interest from the incumbent's leadership who view it as a gimmick, leading to a lack of demonstrable benefit

Financial Services example

This model tends to be used by financial institutions with deep enough pockets to fund an innovation team and a multi-skilled team of data analysts, developers and business SMEs. CBInsights highlighted 37 such labs across the globe from well-known brands such as Barclays Accelerator, Santander Innoventures and HSBC Data & Innovation Labs.

Some firms are even going one step further and building independent organisations to encourage innovation e.g. ABN Amro have set up New10 and Franx with separate cultures, office space and IT.

Supplier contract

In some senses, this is one of the most common examples of a partnership. One firm contracts to provide a service for X years and the other promises to pay Y.

Pros:

- Clear deliverables and measurable KPIs
- Defined timescales
- Can be made to measure for specific requirements
- Speed of access to the capability

Cons:

- Lengthy contract negotiations often aimed at one side winning and the other losing can result in an erosion of goodwill
- Culturally viewed as a service provider rather than a partner
- Rigidity due to the contractual nature of the relationship
- Legal nature of the contract can obscure the practical elements of working together effectively, including meeting regulatory responsibilities

Financial Services example

An example of a supplier contract is the recent deal between ABN Amro's digital bank Moneyou and the digital banking platform provider solarisBank. The two parties have struck an agreement whereby solarisBank provide and fund loans by leveraging their digital ecosystem to make the origination journey slick (as little as 7 minutes for loans between €1,000 and €35,000) but Moneyou control the distribution and customer relationship.

Alliance

An alliance is an agreement by two parties to come together for a specific objective whilst retaining their independence.

Pros:
- Clear strategy and KPIs set at the outset
- Access to new skills and knowledge from working closely with partners
- Detachability – no new legal entity is created
- Ability to leverage brand strength from both parties to increase consumer appeal

Cons:
- No common resource pool exists – a potential source of conflict
- Efficiency gains and synergies are limited by the degree of separation of the two entities
- Strategic priorities may diverge over time
- High potential for culture clash
- Potential brand damage should the partner firm have poor customer experience scores

Financial Services example

In 2014, Apple launched Apple Pay which enabled MasterCard cardholders to use their iPhone and Apple Watches for everyday purchases. MasterCard built the foundation for secure mobile transactions and integrated it seamlessly with the payment experience built into Apple customers' phones. The alliance has been a success as subsequent years have witnessed an increasing number of customers using their phones to make transactions.

Joint venture

A joint venture sees the financial institution and partner firm pooling their resources in order to achieve a particular goal.

Pros:
- Operational efficiency due to the pooling of resources
- Skills transfer potential is high
- Positive cultural spill-over effects
- ‘Skin in the game’ incentivises both parties
- Potential for exclusivity - developing a USP

Cons:
- Highest potential for significant culture clash
- Increased level of organisational complexity and change resource required
- Requires significant investment over time to make the venture successful
- Upfront investment required - particularly risky for early stage innovations
- Potential brand damage should the partner firm have poor customer experience scores

Financial Services example 1

CYBG have recently entered into a joint venture with Salary Finance, an employee wellbeing FinTech that links with a customer’s payroll to offer savings, loans and financial advice. The joint venture has seen both parties put in £500k to fund the operation and CYBG offering a £100m credit facility.

Financial Services example 2

Aberdeen Standard Investments (ASI) and Virgin Money (part of CYBG) have also committed to a joint venture to offer investment solutions to CYBG’s six million customers. The CEO is the ex. Chief Strategy Officer for Standard Life Aberdeen and will be joined by a team from both ASI and Virgin Money to set up and run the venture.

As can be seen above the structure of the partnership is very important as each option has a number of associated pros and cons. However, it is worth noting that these structures should not be set in stone – it may be a prudent strategy to test the water and progress from a tactical to a strategic vehicle once the partnership has proven to be successful.

Action

When the Romans formed their partnerships, they ensured that the intention and obligations of the partners were enshrined in treaties - this often included the promise to defend their allies should they be attacked and, correspondingly, the obligation on the ally to provide troops to the Roman auxiliaries. The Romans had to be ready to defend their allies with the resources at their disposal, otherwise their clout as an international player would be called into question.

In the same way, financial institutions and their prospective partners must have a clear roadmap and resources to launch and maintain their partnership.

Partnership Pathways - finding a way to agreement

When developing formal agreements between prospective partners and financial institutions, it is imperative that the paperwork and corresponding due diligence are proportionate to the structure agreed. Tying up a FinTech in endless bureaucracy and internal hierarchies for a short-term innovation lab experiment is likely to destroy goodwill. However, a full and thorough due diligence exercise on a long-term joint venture is likely to be expected by both parties.

The solution to this dilemma is to create and agree a set of internal Partnership Pathways. These Pathways outline the level of due diligence and paperwork the partner is likely to face from key partnership on-boarding functions such as:

- Legal
- Procurement
- Data security
- Compliance
- Leadership and management

Operating model design

Finally, in order to launch and run the partnership it is imperative that some form of organisational design or blueprint is in place. The operating model helps all stakeholders understand how the partnership will operate and what needs to be done between now and launch to successfully introduce the joint proposition / service offering to the market. It also outlines where partner capabilities and responsibilities lie, which is imperative given the Senior Manager and Certification Regime.

The importance of having an effective Target Operating Model in place must not be understated - to have come all this way and to fail to design, build and run the partnership would be disastrous.

The decline and fall of the Roman Empire

The subject of the decline and fall of the Roman Empire is vast, but a few common themes appear relevant to partnerships, including:

1. **Strategic overreach** - maintaining frontiers over a vast area whilst relying on loosely-linked allies made the Empire strategically vulnerable to attack from competitors.
2. **Failure to meet commercial obligations to allies** - Rome failed to honour their alliance commitments - at times, with those who were supplying their troops!
3. **Culture crisis** - the resurgence of national / tribal feeling (e.g. resurgence of native languages) caused a rupture in the fabric of the imperial world.
4. **Structural splits** - the Empire became so large that it split into an Eastern & Western Empire. However, the split led to significantly reduced cooperation between the two, leaving them vulnerable to attack.
5. **Loss of trust** - the relentless changing of Emperor led to short-termist and selfish actions, the loss of trust in the leadership amongst the masses and inconsistent strategic intentions and decision making.

These headline issues, despite being linked to the collapse of the Roman Empire, could impact the success of your partnership over time. Therefore, it is important to revisit the Partnership Development Framework periodically to ensure the partnership remains strategically sound, founded upon fair commercials with cultural understanding between the two parties, optimal delivery structures and effective action plans.

If you would like to discuss any aspect of the Partnership Development Framework please get in touch:

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