

FinTech, geographic space and economic development. Some directions for research

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Abstract

In recent years, a variety of factors have spurred radical changes in business models and community relations. The ICT technologies that were initially used only for certain back office operations have rapidly been applied to all aspects of providing financial products and services. The 2007-2008 crisis and the credit squeeze that ensued gave rise to crowdfunding, i.e., raising funds through an open call in the Internet targeted to anyone and everyone – a crowd, as the name itself implies – who wishes to take part. Starting from an analysis of the literature, this paper will outline some of the directions that could be taken by the research conducted by the Work Group on the Internationalization of the Italian Economy and the Role of Credit Institutions in the Reorganization of the SME Value Chain now being set up by AGEI, the Italian Geographers' Association.

Keywords: FinTech, crowdfunding, SMEs

1. Open calls via the Internet: crowdfunding

In recent years, a variety of factors have spurred radical changes in business models and community relations. There can be no doubt that technological developments have had a major role in the organization of production, consumption and in bringing together supply and demand. But the pace of change picked up significantly as a result of the 2007-2008 global crisis, which on the one hand drew scholars' attention to the conceptualization of a monetary and financial ecology², and on the other mobilized bottom-up initiatives for overcoming the problems caused by the recession through innovative reformulations of traditional sharing practices.

In today's society, we share and trade via online platforms, where virtual communities meet and interact. The ICT technologies that were initially used only for certain back office operations were rapidly applied to all aspects of providing financial products and services. New FinTech applications have burgeoned, as demonstrated by the statistics available for 2014, when the sector accounted for around 12 billion dollars worldwide (Economyup, 2017).

While an exploration of FinTech in general is provided in the geographic study by David Bassens, Reijer Hendrikse and Michiel van Metereen, (2017), our analysis here will center on only one of the many forms of the *new* financial system, crowdfunding.

Taking its impetus from the credit squeeze that followed the 2008 financial crisis, crowdfunding is a means of raising funds through an open call in the Internet targeted to anyone and everyone – a crowd, as the name itself implies – who wishes to take part (Belleflamme et al, 2013; Mollick, 2013). Originating with initiatives on the part of music groups, environmentalists and philanthropic activists, crowdfunding immediately attracted the interest of small and medium enterprises, start-ups in particular, as well as real estate investment businesses, gaining a prominent position in the FinTech world along with all the other Internet-based financial services addressed to the public at large (Langley and Leyshon, 2017).

In recent years, the capital raised through crowdfunding worldwide has grown sharply, going from 500 million US dollars in 2009 to 2.7 billion in 2012 and 34 billion in 2015, a trend which is expected to continue in the coming years. Geographically, the areas that are most active in this

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² The term ecology has come into common use in all disciplines. In geography, numerous studies refer to financial ecology, though it would not appear to have been precisely defined.

Intuitively, however, it could be seen as the relationship between the financial economy, sustainability and social equity, or in other words, as it is understood in the neurological sciences, as the "relationship of each thing with all the things around it" (Lotto, 2017). For more detail in the ecology of finance (see Douthwait, 2000).

business are the United States and, in Europe, the United Kingdom, but Asia is fast becoming a player on the international scene and could soon join the top ranks in terms of funding volume (Crowdfunding Buzz, 201; Statista, 2017). Currently, most of the specialized platforms that act as financial intermediaries between investors and ventures seeking financing are concentrated in the United States and the United Kingdom (Langley and Leyshon, 2017).

Essentially, it is the same mechanism of transferring resources from parties with a surplus to parties lacking funds which, following the gradual rise of the liberal policies of the 1990s, can be managed by actors other than the traditional ones. But it should be borne in mind that although it can be regarded as a consequence of processes of disintermediation, the differences are substantial. In the Nineties, in fact, regulations governing the liberalization of the financial system were enacted at the institutional level, while the development of information and communication technologies simply played a supporting role, albeit one of primary importance.

In the case of digital finance, on the other hand, the Web itself is the protagonist in organizing financial services, and public powers are called upon to develop an appropriate regulatory framework for the new organization of financial services (Salomon, 2017). The United States and many European countries, in fact, have introduced regulatory measures for eliminating problems of information asymmetry and risk factors, and in particular the risk that investors will be defrauded (Bethlendi and Végh, 2014).

Naturally, in the case of FinTech – and of crowdfunding in particular – as for many others, it must be noted that geographic space is organized along coordinates that differ from the traditional categories, and that consequently geography must devote greater attention to the territorial implications of the changes that have burst onto the worldwide financial scene.

Starting from a brief overview of the many papers published in the English-speaking academic world, the following pages will attempt to outline some of the directions that could be taken by the research conducted by the Work Group on the Internationalization of the Italian Economy and the Role of Credit Institutions in the Reorganization of the SME Value Chain now being set up by AGEI, the Italian Geographers' Association.

2. Brief analysis of several scholars' views of crowdfunding

The new ways of bringing together supply and demand on online platforms have been variously interpreted and are still being scrutinized by economic and managerial science, sociology, geography and communication science. In the latter field, the work of Jose van Dijck (2013) constitutes a benchmark for all scholars interested in the FinTech phenomenon.

Among analyses of business economics, particular interest attaches to those investigations that attempt to determine what role bank credit will have in a period when financial services have been irreversibly revolutionized.

At the beginning of the 1990s, faced with the sweeping changes brought about by globalization, market integration and the pervasive presence of technological tools that made it possible to conduct financial transactions regardless of physical location, some scholars had announced the end of geography (O'Brien, 1992).

Likewise, provocatively titled recent publications have suggested – though the suggestion is still framed as a question – that we may soon see “the end of banks” (Roux, 2015). A more attentive reading, however, shows that their aim is to warn of the difficulties facing the banking system, which not only seems unable (or unwilling) to learn from the crisis and become more prudent, but must also rise to the challenges posed by “finance otherwise”.

According to the experts who have examined these issues, if the banks are to maintain or increase their performance in this new setting, they must adopt business models that are better able to respond to the new players' agility in producing and providing innovative financial services and to changing consumer behavior.

If we look at the considerations voiced regarding the nature of the relationship traditional lending and the new platforms, we see a clear difference of opinion. Some scholars, in fact, argue that the rise of financial digitization results in the *disruption* of traditional systems (McWilliams, 2014), a

term coined to denote a bottom-up innovation that makes a product or service accessible to an ever-increasing number of consumers³. Other scholars, by contrast, hold that the contrast between the banking system and crowdfunding is only apparent and that the two mechanisms can coexist, for example by appealing to different customer targets. In addition, they do not rule out the possibility that institutional investors could start and operate a platform for collecting funds for innovative SMEs. In this case, a new institutional player would appear on the financial scene: the *internet and software platform* (Langlay and Leyshon, 2017).

In the field of geography one can find an extensive literature on the socio-spatial implications of the digitization of finance. Following once again in the footsteps of David Harvey, the phenomenon has been investigated from a critical standpoint, as an evolution of capitalism which, thanks to the use of the Internet and, accordingly, the involvement of a limitless and generic crowd of investors, disguises a democratic and redistributive finance. In this connection, a significant contribution has been made by David S. Bieri (2015), who examines crowdfunding as a tool of the capitalist system to divert capital flows from the production sector to urban real estate and infrastructure, with all the attendant social consequences of which Harvey's many writings warn.

The new credit system – and, more generally, FinTech – is thus seen as the outcome of a particular combination of socio-technical practices and capitalist business practices which has been dubbed *platform capitalism*⁴, a neologism that draws attention to the idea that crowdfunding essentially operates on line with tools such as venture capital that are typical of traditional finance.

3. The platform intermediary and its geographic implications

The platform intermediary operates in the organization of geographic space with concurrent dynamics of dispersion and agglomeration. The most striking feature of crowdfunding is the geographic dispersion of investors. At the time of its first appearances in financing music projects, it was calculated that the average distance between the artist-entrepreneur and investors was around 3,000 miles, as compared to 70 between venture capital and target firms. In a few short years, such operations have eliminated the economic frictions associated with geographic distance. A study of the major platforms found, for instance, that investors in the Amsterdam-based platform Sellaband are located in 80 countries around the world, the greatest concentration being in the United States (Agraval e al, 2011). But geography cannot fail to see that although funding is collected in a virtual space, the projects thus funded undeniably have effects on the social and economic setting of the entrepreneur who turns to crowdfunding in order to bring innovative ideas to fruition.

Again in connection with the geographic dispersion that is characteristic of crowdfunding, it should be noted that a survey of the location of the major platforms providing digital intermediation services found that they are headquartered in the global financial centers. Thus, the more highly qualified functions still tend to cluster in places offering highly specialized human resources and advanced technological infrastructures. This meeting between innovative technologies and financial operators' ability to develop increasingly sophisticated tools has resulted in a concentration of tech firms and financial enterprises in the London metropolitan area, known as the Silicon Roundabout, or East London Tech City, which has been said to embody the "fusion of the technological prowess of Silicon Valley with the financial acumen of Wall Street and, in particular, the City of London" (McWilliams, 2015).

In addition, the financial relationships set up by the platform give rise to a virtual community and thus to a different conception of the notion of *proximity* between parties who are distant in space but brought together by a common project and shared expectations of capital gain. Once again, geographic scholars must acknowledge that even the digitized financial system, though freer from constraints, is organized by actors who operate in a given social and territorial setting.

With a view to analyzing the phenomenon from a different vantage point and at a different scale,

³ The idea of the disruption associated with the digital era was introduced by Christensen in his 1997 book, *The Innovator's Dilemma*, by analogy with Joseph A. Schumpeter's view of capitalism as a process of "creative destruction". Langlay and Leyshon, 2017

⁴ A term introduced by the German blogger Sascha Lobo. Langlay and Leyshon, 2016

one promising area for geographic research would be to explore the opportunities that crowdfunding holds for small and medium enterprises, a topic that immediately brings to mind the nature of the relationships between the traditional banking sector, financing extended via online platforms, and geographical territory. Empirical studies based on conducting structured interviews and administering questionnaires to banks, businesses and investors via social media could conform or refute this hypothesis. Naturally, geographic analysis must necessarily be combined with a thorough scrutiny of the characteristics of the territory, seen as a “complex of conditions” that interact with each other and, if correctly managed, can provide essential support to the organization and development of the economic system (Conti, 2012).

Following this line of thought, research on local production districts and clusters, which are not only home to many small and medium enterprises⁵ but also provide a milieu which acts as an incubator for innovation, could supply valuable insights for the governance of economic and territorial development. In the specific case considered here, the geographer could provide a foundation for policies underpinning the formulation of strategies for mending the relationships between banks and their local areas. These relationships have deteriorated in recent years, both because of the consequences of the global crisis, and as a result of short-sighted governance policies and risky financial transactions that in many cases have undermined savers’ confidence, thus aggravating the credit squeeze affecting small and medium enterprises.

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⁵ For details of the new approaches to SME financing, see OCDE, 2015, and the European Commission, 2015.

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