



When Fintech Goes Green

Instead of competing directly with banks, some fintechs are finding opportunities banks haven't noticed.

It would seem that start-up entrepreneurs no longer need a banker to get started. Crowdfunding platforms such as Kickstarter and Indiegogo have enabled good ideas to get plenty of funding in a short space of time. It would also seem that investors no longer need truckloads of money to invest in start-ups. Equity crowdfunding has emerged to give investors interesting returns on investments of US\$1,000 or even less.

Going one step further, small investors can now even get in on some of the megatrends that have traditionally been the domain of investment bankers. Take investing in green energy in Germany for example. Financing renewable energy in Germany has become an established banking market in which banks such as GLS and UmweltBank have spent a significant amount of capital and effort.

Equity crowdfunding platforms, such as GreenVesting, Bettervest and Crowd4Climate are now offering German investors a piece of the action. The total financing volume through platforms in Germany was modest (EUR125.4 million in new loans) by the third quarter of 2017. Hardly enough to make any bank manager sweat. To put this into perspective, the total volume outstanding compares to the savings and loans of a small town in the Uckermark, a region just north of Berlin. What is more impressive is that this number saw a 219

percent growth compared with the year before. While this is not yet a challenge to the banking industry, it does show that a new financing source is emerging and that parts of the investing community are willing to move from banks to the crowd to invest their money.

So it would appear that the growth prospects of green crowd investing are strong. If crowdfunding of environmental projects such as solar parks is well advanced, then it is only a matter of time until crowdfunding disrupts the German banking market as it has in the United States and United Kingdom.

Will banks catch up?

Let us analyse what this niche has already accomplished. Germany has more than 30 platforms that actively offer investors an opportunity to participate in sectors such as real estate mezzanine, renewable energy and bank-like lending platforms. Real estate, at more than EUR100 million volume outstanding, is unsurprisingly the largest sector.

This sector's business model is clear and transparent: A builder seeks equity-like capital from the crowd for the time of construction (brownfield operation), leverages up with currently very cheap debt from a bank, builds medium-size projects, sells the apartments based on prospectus during

construction and pays crowd investors yields between 6 and 7 percent per annum, over a term of two to three years. The builder pays a yield which is twice as high as Greek short-term bonds and lets small investors participate in the German booming real estate market. The most important participants in this segment are Exporo, Zinsland, zinsbaustein, Bergfürst and Engel & Völkers Capital. The latter, a well-known real estate broker, is an interesting case of a successful real estate player, diversifying into fintech in response to the challenges in its traditional business model – selling property for agency fees.

In comparison, the funding of start-ups through platforms in Germany has been paved with upsets. A small number of defaults occurred in the private equity space, which took some German investors by surprise even though they had invested knowing the risks. The cases received substantial publicity, impeding the growth of investments in this sector. Companies such as Seedmatch and Companisto are the main players in this modest category of crowdfunding.

So while German crowdfunding of real estate remains small and start-up financing is simply too insignificant to be disrupted soon, the niche of green energy investing is where we see the largest early challenges to the traditional banking sector. Following the reduction in subsidies for green investments in Germany, projects in this sector have become smaller and smaller. Given banks' relatively high overheads, they simply cannot justify focusing on this area financially. Instead, a more efficient way to match projects and potential investors was needed. This is where crowdfunding of green projects found its niche.

The case of GreenVesting

A German firm founded in 2008, GreenVesting illustrates the pace of development in this industry. It started as a coordinator and operator of renewable energy projects for private and small-to-medium-size investors. The firm identified renewable energy opportunities (mostly solar panel installations), found investors, oversaw the building of the installations and ensured maintenance and control afterwards. It allowed investors in renewable energy to outsource the paper-intensive process of getting a unit up and running. Following the global financial crises and the substantial reduction in state subsidies to environment-friendly projects, GreenVesting's traditional business model came under pressure.

The only way to scale became technology, specifically fintech, to maintain a cost-efficient investment process and investor base. The firm was also forced to innovate given the perceived risks in crowdfunding. After all, if projects fail, investors

lose their money. Refinancing existing projects made investors more familiar with the investment process and increasingly willing to participate in larger and riskier projects to improve on their returns.

German investors can now go online to browse overseas projects and invest in them. In response, established banks have followed green investment opportunities through their in-house platforms. But these remain domestic opportunities. Fintechs are finding new opportunities for investors beyond the realms of traditional banks.

The future holds some **challenges** for these fintechs. Legislators are looking to contain the growth of crowd investing in Germany, specifically green investing, as they see capital ties between issuers and platforms as a conflict of interest. Green investing firms, however, regard these claims as unfounded. These ties, they say, put them in the same boat as investors, which is good for them.

As international and local banks have not opened any monetary valve in the green investing sector yet, green investing firms are the only ones offering German investors “enabling” projects in emerging markets with potentially higher returns. Most of those projects are in countries which enjoy a lot of sun, but still cover the bulk of their electricity needs through diesel generators. As a result, German crowdfunding platforms in renewable energies contribute on a small scale to environmental improvement and climate protection by enabling German capital to flow to emerging markets' underfunded green energy projects. Banks could and should be asking themselves how they can better meet the needs of investors. Green crowdfunding platforms are tapping a desire for yield, but also to do good.

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