Chinese Fintech Companies' International Development:

Motivations to Pursue International Expansion

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Public Policy Practise I

April 01, 2017

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1 INTRODUCTION

Chinese Financial Technology, so-called Fintech, companies are rapidly developing and rising as potential leaders in the global Fintech industry. The financial technology sector was mainly dominated by the U.S. and U.K. firms, but Chinese companies are now rising as top innovators in the field. While in 2015 only two Chinese Fintech companies were included in the top 10 global Fintech firms, the number increased to five in the following year.[1] James Lloyd, an Asia-Pacific Fintech Leader at EY consulting company claimed that Fintech is a very China-specific phenomenon and it's booming more quickly there than in any other country.[2] Chinese Fintechs are making immense profits in the domestic market and although they are not first starters in their industry, they are getting more attention than ever. While they keep innovating and targeting more customers in the domestic market, Chinese Fintechs increasingly exert efforts to invest in overseas market and cooperate with foreign companies. This paper analyzes why Chinese Fintechs regard international development as an attractive strategy and pursue this policy despite their advantageous status in the domestic market.

2 DEVELOPMENT OF FINTECH INDUSTRY

2.1 Global Fintech Industry

Despite the fact that the Fintech industry is booming globally, a comprehensive definition of the term Fintech has yet to emerge. According to one possible definition, Fintech "refers to the use of technology to deliver financial solutions."[3] Fintech is the combination of providing financial services with innovative technologies. There are various players in the industry including large conventional financial institutions, technology companies and dynamic start-ups.[4] It is a very broad conception that includes many forms of sectors and companies which offer financial services through innovative technologies to people who couldn't access them before. Services range from payment, wealth management, to peer-to-peer (P2P) lending, and many more.

Many believe that Fintech is a very recent phenomenon as it boomed in past years, but its history begins with the globalization of the late 19th century. Increasing levels of technological

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[1] Angus McNeice, "China Dominates List of World's Top 10 Fintech Companies in 2016," *China Daily Europe*, October 24, 2016, http://europe.chinadaily.com.cn/business/2016-10/24/content_27159456.htm (accessed March 16, 2017).
[2] Haky Moon, "China Unlocks Fintech Potential," *China Daily Asia*, August 12, 2016, http://www.chinadailyasia.com/asiaweekly/2016-08/12/content_15478469.html (accessed March 16, 2017).
[3] Douglas W. Arner, Janos Barberis, and Ross P. Buckley, "The Evolution of Fintech: A New Post-Crisis Paradigm?" *The HKU Scholars Hub* (2015): 3.
[4] PwC's Financial Services Institute, "What is Fintech?" *PwCFintech Q&A* (April 2016): 1-3.

development met financial globalization and a growing number of infrastructures such as transatlantic cables and Automatic Teller Machine (ATM) heralded the start of the Fintech development.[5] Adding to globalization, digitization enabled financial companies to offer broader services starting from the late 20th century.[6] The development of the IT industry and the expansion of the Internet allowed banks to increase the number of customers and transactions through online banking.[7] The current and renewed boom of Fintech started from the late 2000s with more actors emerging in the industry, including a large amount of start-ups.[8] As more companies offer financial services through the internet and these become more accessible through the spread of smartphones, we are witnessing the next step in the evolution of the global Fintech industry.

2.2 Chinese Fintech Industry

Compared to the early development of the global Fintech industry, the Fintech industry in China developed and boomed very recently. The Chinese government carried out financial reforms starting in the late 1970s but until the beginning of the 21st century the financial system still confronted the problem of large groups in the population that did not have access to banking services or the credit system. In comparison with the US financial system where banks are well-developed and serve small-and-medium-sized enterprises (SMEs) as well as individual customers, economic growth in China has been created by big state-owned enterprises that had the implicit backing of the state and therefore preferential access to credit from Chinese banks.[9] This forced especially SMEs as well as individuals to rely to a large extent on the informal banking sector and other channels when accessing credit. Chinese P2P platforms discovered this demand for financial services and their number surged from one platform in 2007 to more than 2000 in 2015.[10]

Not only the P2P sector but also other areas such as payment services with more than 2tn RMB in yearly transaction volume make Chinese Fintechs the internationally leading actors. A report by McKinsey highlights the supportive regulatory environment, the developed e-commerce business, the demand for financial inclusion and the adaptability in China's traditional

5 Douglas et al., "The Evolution of Fintech," 4.
6 Ibid., 6.
7 Ibid., 11.
8 Ibid., 15.
9 Long Chen, "From Fintech to Finlife: The case of Fintech development in China," *China Economic Journal* 9, no.3 (2016): 228.
10 Janos Barberis and Douglas W. Arner, "FinTech in China: From Shadow Banking to P2P," in *Banking Beyond Banks and Money*, ed. Paolo Tasca et al., (Gewerbestrasse: Springer International Publishing, 2016): 70.

banking sector as particular advantageous conditions for the development of Chinese Fintechs.[11] Underpinned by a big potential in increasing Internet penetration which currently stands at 50% of the population in comparison to 70-80% in Western markets[12] and by leapfrogging the development of a traditional banking infrastructure, Chinese Fintechs will contribute to the goal of financial inclusion as well as to the international influence of Chinese Fintechs in the future. In China, the combination of technical advances with the unmet demand for financial services in large parts of the society has catalysed the extraordinary development of Fintech over the past years especially in P2P and payment services.[13]

3 INTERNATIONAL DEVELOPMENT OF FINTECH COMPANIES

In the past years, a number of Chinese FinTech companies have started to make their advances in markets overseas. The decision to take this step and internationalize the operations of a company are diverse and depend on the specific business model of the company concerned. For Fintech companies that provide financial services through internet-based technical solutions, considerations of sourcing or production conditions are of lesser significance than, for example, for a shoe manufacturer. They are more concerned about their own technical advantages and new consumer groups that can improve their financial profits. The literature on international expansion strategies identifies six general motives that apply to Fintech companies and other service-oriented firms.[14]

1. ***The company could seek to grow by diversifying its markets.*** When not entirely depending on developments in the domestic Chinese market anymore, the Chinese Fintech companies would diversify risks that they are facing and could benefit from new opportunities for their business development in other markets.
2. ***The company could earn higher profits and margins on the foreign market.*** If they are able to install themselves successfully in a market abroad and this market offers higher margins for the services or the customer base is larger, the Chinese company would be able

[11] McKinsey Greater China FIG Practice, *Disruption and Connection Cracking the Myths of China Internet Finance Innovation*, (McKinsey&Company, July 2016): 1-32.
[12] Raphael Goué, *The Fintech Industry in China: A New Road to Financial Inclusion*, Athens, Octoboer 7, 2016 (Euracific).
[13] Cheng, Long (2016) "From Fintech to Finlife: The case of Fintech development in China" *China Economic Journal*, Vol.9, Issue 3: p. 228
[14] S. Tamer Cavusgil, Gary Knight, and John R. Riesenberger, *International Business: The New Realities*, (New Jersey: Prentice Hall, 2012): 16.

to achieve higher profits from their investment in that market in comparison to the domestic market.

3. ***The company could gain new insights about the development of its business model.*** Due to the different environment on the foreign markets, the Chinese Fintech company could encounter new demands from customers or gain new ideas for the development of its business model from local employees.
4. ***The company could service customers that have moved abroad.*** The core base of Chinese Fintechs are Chinese citizens who use the financial services at home. With an increasing number of Chinese tourists abroad, the Chinese Fintech companies could follow their core customer base and provide financial services to them abroad as well.
5. ***The company could stifle the growth of foreign competitors at an early stage.*** Chinese Fintech companies could try to stop the development of local alternative to the services they can provide to customers in the foreign markets by gaining market share even before these domestic alternatives had a chance to develop their own market share.
6. ***The company could forge important partnerships with companies abroad for their future development.*** Chinese Fintech companies could especially benefit from strategic partnerships if markets are not entirely open to them which limits their ability to compete with foreign Fintech companies on their domestic market. Under such conditions, partnerships could be an important avenue for Chinese Fintechs to gain market access and to profit from growth opportunities on these markets.

When expanding into a foreign market, usually a company has already developed a firm standing in their domestic environment, although for some companies an international expansion is inherent to their business model. The process to access the new market generally follows a gradual approach of first conducting market research and only experimenting with involvement on the foreign market through the export of basic services. In subsequent steps, the company becomes more confident in its foreign operations and explores conducting and broadening investments in the foreign market. In the final step, the company is genuinely committed to its international operations and the international business is integrated into the regular operations.[15] During this process the company is confronted with the choice between different strategies to drive forward its internationalization. Companies could decide to open up their own subsidiaries, to invest into an existing firm, or to engage in a joint-venture or strategic partnership with a local

[15] Ibid.: 158.

firm in the foreign market. All strategies comprise advantages as well as disadvantages that have to be assessed on a case-by-case basis.[16]

At the current stage, Chinese Fintechs are situated mainly between the stages of initial experimentation and broadening their investments in foreign markets. Depending on their business model, their size, and their international reach, the Fintechs are looking for ways to either expand their experimental involvement or transition towards the last stage of genuine commitment to the operations in overseas markets. As their mode of engagement, the Chinese companies to-date largely favoured the option of investing in already existing companies or engage in joint-ventures or strategic partnerships with companies already established in these markets. Brand recognition of existing local companies helped the development of their investment projects and many countries have regulatory obstacles for foreign financial services providers in place so that only through partnerships can Chinese Fintechs gain full access to the foreign market. Alibaba, one of the most prominent representatives of Chinese Fintechs, has established a complex system around the provision of financial services through activities in online shopping or other services in China and looks to expand in various projects abroad.[17] Most recently, Ant Financial, an affiliate of the Alibaba Group, has acquired US-based payments provider MoneyGram for $880m in January 2017.[18] Previously, Alipay, the payments arm of the Alibaba Group, entered into a partnership with Ingenico, a European payments provider. This will enable Chinese tourists to use the Alipay and Ingenico networks for purchases in stores in Europe.[19]

Chinese Fintech companies have been active not only in developed countries, but are also involved in investment activities in emerging and developing markets. Since 2015, Alibaba and Ant Financial together hold approximately a 40 per cent stake in the Indian digital payment provider Paytm. Additional investments by the two Chinese shareholders played a vital role for Paytm to broaden its coverage of the very promising Indian digital payments market.[20] Furthermore, Alibaba has become active when acquiring a stake of digital payments provider

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[16] Charles W.L. Hill, *International Business: Competing in the Global Marketplace*. (Columbus: McGraw-Hill, 2010).
[17] Sachin Miital and James Llyod, *The Rise of Fintech in China: Redefining Financial Services,* E&Y Asian Insights Office and DBS Group Research, November 2016: 37.
[18] Martin Arnold and Alistair Grey, "China's Ant Financial buys MoneyGram for $880m," *Financial Times,* January 27, 2017, https://www.ft.com/content/8ec362a2-e3dc-11e6-8405-9e5580d6e5fb (accessed on March 20, 2017).
[19] Marie Mawad, "China's Alipay Pushes Into Europe With Ingenico Payments Deal," *Bloomberg Technology,* August 18, 2016, https://www.bloomberg.com/news/articles/2016-08-18/china-s-alipay-pushes-into-europe-with-ingenico-payments-deal (accessed on March 20, 2017).
[20] Reuters Technology News, "Alibaba, Ant Financial inject fresh cash into India's Paytm," *Reuters,* September 29, 2015, http://www.reuters.com/article/us-alibaba-paytm-india-idUSKCN0RT0KY20150929 (accessed on March 20, 2017).

Ascend Money that operates in Thailand as well as other countries in South-East Asia.[21] Other Chinese Fintech giants such as Baidu has been active as well with expansions in Thailand where it made its service Baidu wallet available mostly aimed at servicing Chinese tourists who travel abroad. This expansion is not limited to Thailand but Baidu has plans to expand in other developed countries in Asia such as Japan and South Korea.[22] Coupled with its advances in the online-to-offline business, Baidu aims to connect everyday cash transactions such as hailing a cab or buying movie tickets with an online transaction. Baidu is already very present in this area within China but aims to increase its influence abroad as well.[23] The examples outlined above show that investments and partnerships abroad initiated by Chinese Fintech companies have grown in size and speed. They demonstrate a pronounced interest by the Chinese companies to be important players not only in their domestic market but also in other countries.

4 RESEARCH QUESTION AND HYPOTHESES

These trends highlight a growing influence of many Chinese Fintechs expanding abroad. As is true for many aspects of this international expansion activity, little has been said about the underlying reasons and motivations that drive the behaviour of Chinese Fintechs. This paper tries to address this gap and will examine the question of why some Chinese Fintechs are expanding internationally and others refrain from doing so. Generally, international expansion strategies are driven by the wish to seek new markets and generate profits through investing in these markets. Despite the fact that the Chinese Fintech market is still enormous, a number of Chinese Fintechs invest in or actively cooperate with local companies outside of China.

The first hypothesis to understand this question is that Chinese Fintechs try to expand towards markets outside China based on the companies' own level of development in dimensions such as size, technology, and business model. After their rapid development in China, Chinese Fintechs may want to utilize their advanced technology and business models when entering the overseas market. With sufficient size and capital, those companies can regard international development as a plausible option for further development and broadening of their customer

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[21] Steven Millward, "Jack Ma's Ant Financial shows global ambitions once again with move into Thailand," *Tech in Asia*, November 01, 2016, https://www.techinasia.com/ant-financial-thailand-investment-ascend-money-confirmed (accessed March 20, 2017).
[22] Fintech Asia, "Baidu Wallet expands beyond China," *Fintech Asia*, April 21, 2016, http://www.fintechasia.net/baidu-wallet-expands-beyond-china/ (accessed March 20, 2017).
[23] James Sullivan, "Is Baidu's Latest Investment in Online-to-Offline Services a Positive for the Company?," *The Motley Fool*, July 11, 2015, https://www.fool.com/investing/general/2015/07/11/is-baidus-latest-investment-in-online-to-offline-s.aspx (accessed on March 20, 2017).

base. There are a huge number of Chinese travellers going abroad and there needs have to be met. So, it can be regarded as client-driven strategy for Chinese Fintechs to help Chinese customers to easily make payment overseas. Some of the Chinese Fintechs mainly focus on Chinese who use services abroad but also want to further increase their customer base within the local community.[24] So, basd on their own size and customer base, Chinese Fintechs can expand to overseas market.

The second hypothesis is that the domestic Fintech market has matured after about a decade and companies are faced with the necessity to expand into new markets abroad. Establishing international operations may be a natural step of Chinese Fintechs for further expansion as there are no more opportunities for further expansion within China. A report from McKinsey points out that the firms will face fiercer competition at home due to stricter domestic laws and an impending consolidation in the Chinese Fintech industry.[25] The increasing number of Fintech companies in China and limited number of customers result in increasing level of competition. Some experts argue that friction between Fintech start-ups and conventional financial service providers through the internet is expected to become more serious.[26] So, companies may try to avoid these domestic challenges due to market saturation and change their strategy to more actively operate in other countries.

Such a strategic decision may be in line with increasing financial need in less developed countries that have problems with their conventional banks and financial sectors. Companies and individuals in those countries face difficulties in borrowing from conventional banks due to high interest rate or inaccessibility of the banking infrastructure, so they seek better channels to access financial services. Therefore, Chinese Fintech companies take this opportunity into account and cooperate with local companies. Also, cultural similarity between China and Southeast Asian countries may spur Chinese Fintechs to adopt international development strategy. Cultural similarity can lessen the burden on Chinese Fintechs to research about markets abroad and can find easy ways to adapt to those markets and catch local consumers' needs and market conditions without much effort compared to unfamiliar markets.

The case of Chinese expansion into developed countries like Korea and Japan on the other hand is different as these countries already established a highly developed financial system and their Fintech industry hasn't developed yet due to strict regulations. Thus, strategic

[24] Sachin Miital and James Llyod, *The Rise of Fintech in China: Redefining Financial Services:* 37.
[25] McKinsey&Company, *Disruption and Connection: Cracking the Myths of China Internet Finance Innovation*: 1.
[26] Arner, DW, JN Barberis, and RP Buckley, "The Evolution of Fintech: A New Post-Crisis Paradigm?": 27.

considerations to acquire a head-start might motivate Chinese companies to enter these markets when the industry in those countries are only in the beginning stage of development while they still would face the same regulatory constraints.

Following these hypotheses, the authors of this paper set out to investigate why some Chinese Fintech firms try to expand their operation to the overseas market. This report looks at the development of two sectors in particular - P2P lending and payment services - as companies from these sectors represent the most advanced actors in China who are leading the process of internationalization of Chinese Fintechs. Of course, the paper recognizes differences among these two sectors, notably the advanced stage of the Chinese payments sector in comparison to the considerable domestic expansion opportunities for the P2P sector that have yet been realized. Regarding their international expansion, payment services are generally easier implemented in other markets and oftentimes serve as a stepping stone for more sophisticated financial services such as P2P lending.

Based on interviews with company representatives, research institutions, and government agencies, this paper will first outline the main motivation for international expansion as a collection of factors internal to the company, labelled in this report as company maturity. In the second part, the report will focus in more detail on external factors, namely strong demand in foreign markets, the benefits of technology transfer and exchange, and political strategies, that while important, exert a secondary influence on the decision for Chinese Fintech companies to expand abroad. The last section will bring the two types of factors together and highlight further areas of research.

5 INTERNAL COMPANY MATURITY AS THE DETERMINING FACTOR FOR INTERNATIONAL EXPANSION

The first and foremost factor that affects China Fintech companies going abroad is an internal one: company maturity level. With a higher company maturity level, measured here as a company's customer base, profit or cash flow, growth characteristics and other indicators[27], the sophistication of a company’s international expansion strategy increases. This argument is based on the assumption of the business life cycle, which indicates that all successful businesses will

[27] The method of measurement used here is inspired by Investopedia’s entries of “mature firm” and “growth firm”. Available at: http://www.investopedia.com/terms/m/mature-firm.asp, http://www.investopedia.com/terms/g/growth-firm.asp

go through several phases as establishment, growth, maturity and post-maturity more than once.[28] Thus a Fintech company's current business stage determines its business logic and philosophy, and specifically in this research, its international development strategy.

If taking a panorama view of the current China's Fintech industry, one observation is that the level of company maturity varies widely among forerunners and followers, unicorns and start-ups. The taxonomy of company maturity helps to explain why mature and growth Chinese Fintech companies have adopted different international development strategies.

Mature Fintech companies have the following characteristics in common: they have passed the stage of growth and tend to grow at a steady, lower rate; they have established a large and rather loyal customer base; they also tend to have several equally well-established competitors, making price competition a significant factor in their ability to increase profits. There are few well-known companies, including Baidu, Tencent, Alibaba, who are the forerunners and biggest winners of the e-commerce boom in China, and traditional financial giants entering Fintech such as Ping'an Group.

Mature Fintech companies usually have comprehensive international development strategies and have already put them into full practice. Ant Financial has publicly announced their three-step internationalization strategy while Ping'an is taking similar steps at the moment, albeit with a lower-profile. It is quite understandable why they *could* very likely become forerunners in the wave of going abroad. First, they have strong motives to expand beyond domestic markets. On the one hand, the domestic market is care-free safe zone to them that produces steady annual income; on the other hand, those companies have to seek new momentum of growth, and the domestic market does not offer opportunities to achieve a high growth rate. Second, they have a competitive advantage either in technology or in their business model, which could be used to empower counterparts abroad. This is especially true in Southeast Asia where imbalances between high demand and insufficient supply of fintech-related services are well observed. Last but not least, as their reputation is well-established, it is always the case that overseas potential business partners spontaneously approach these companies rather than the

[28]Adapting the concept from the biological sciences, a number of researchers has proposed life cycles of organizational development from birth to death. As one of the earlier contributors, Chandler (1962) introduced stages to a life cycle model in which he argued that as stages changed, so did firms' strategies and structures and had identified a four-stage model of organization evolution. As to the nature of stages, most authors appear to follow the idea of Chandler's (1962) landmark work, *Strategy and Structure* that organizations develop patterns of organization structure in response to common growth and market challenges. A valid life-cycle model could provide a road map for managers to identify critical organizational changes and problems as organizations grow and develop. Further see: Chandler, AD, 1962. *Strategy and Structure*. MIT Press: Cambridge, MA.

other way around. A complex mechanism of selecting business partners from a "pool" ensures cooperation with the most appropriate partner. Staff from Ant and Ping'an acknowledged that it was common practice for one company to beat hundreds of various competitors before becoming Ant's or Ping'an's strategic partner.[29]

Growth companies are companies in the stage of establishment or growth, and haven't reached the level of maturity yet.Their common characteristics include a rapid growth rate, either negative or positive profits, an expansion of their consumer base, and a quick adaptability to market changes. Large numbers of growth fintech companies in China are now competing fiercely in sub-sectors such as various consumption scenarios, P2P lending, P2B lending, etc.

China's Fintech growth companies have either adopted some kind of international development strategies, but currently remain in the stage of experimentation, or just begun doing research on future international development strategies. Their role as successors in the wave of going abroad is largely determined by their current position in the Fintech industry and corresponding business considerations. Considering the situation on the domestic market, mature Fintech companies are well-established within their markets but sub-sectors remain battlefields for many fintech companies. For the latter, the current priority on their agenda is to win the competition in its own field by all means in the next crucial years. If survival is the prize, how could they consider anything else? Besides, the domestic market has yet been fully exploited with consumers steadily shifting from traditional banking services to individual situational (or scenario) consumer finance. Therefore, growth companies still enjoy opportunities for expansion on the domestic market. Focusing resources on implementing a full-scale international development strategy may undermine their main goal of survival and growth and is for many companies unaffordable. They would rather observe others conducting research and experimentation. Last but not least, their going abroad is far more difficult than for mature fintech industries. Usually they have to adjust their business models by incorporating successful experiences. Thus, they still have to develop the expertise in operating their business model and their technological tools in order to prepare them to expand internationally. Regarding business partners, they can only attract a couple of partners abroad or simply wait for kind offers. The case of Dianrong's Korean fintech business was made possible largely because they grasped the olive branch Hanhua held out rather than taking initiative in finding a cooperation partner.[30]

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[29] This detail was informed in the interviews with Ping'An and Ants.
[30] This detail was informed by Dianrong staff in an interview.

All in all, the general law of business is strongly reflected in our observations concerning Chinese Fintechs. The higher maturity level a company has reached, the more sophisticated and crucial their international development strategy will become as an integrated part of company development.

6 EXTERNAL PUSH AND PULL FACTORS OF CHINESE FINTECHS' INTERNATIONAL EXPANSION

The secondary factors influencing Chinese Fintech companies' decision to expand internationally are external to the company: The large demand in foreign markets originating from both Chinese tourists abroad and a financially excluded local population act as the central pull factors for Chinese Fintech companies to move abroad. The advanced Financial technology used by Chinese companies but also the need for such technology abroad when partnering with local firms both act as pull and push factors for the international expansion. Lastly, the political strategies advanced by the Chinese government have a limited impact as push factor to encourage international expansion of Chinese Fintech companies.

6.1 Unfulfilled Consumer Demand Abroad

Ambitious actors in the global market such as Chinese technology and Internet giants and service providers associated with them are naturally attracted to the unfulfilled consumer demand for inclusive and convenient financial services in other countries. With advanced technologies in payment and consumer finance, Chinese Fintech companies are now racing for a global reach, targeting the enormous population of Chinese customers abroad and the potential customers in emerging economies like Southeast Asia.

While a number of global customer groups' demands for financial services have been unmet, consumer finance, followed by the demand for improved payment and consumer-lending systems, is the most significant. In the next section, the report will elaborate on Chinese and overseas clients' demands as well as the current state of partnerships for major Chinese Fintech companies and their foreign partners.

6.1.1 Internationalization of Chinese domestic demand

For Chinese consumers shopping abroad, typically featured as online purchases and tourism, international payment settlement becomes the most important challenge. Reflecting on the combination of consumer preferences for digital payments with the spread of smartphones a decade ago, third party payment providers like Lakala, Alipay (under Alibaba's Ant Financial) and Tenpay conquered China and permeated consumption habits in daily life. In light of the expanding demand for international products, luxury goods in particular, grasping the opportunity to facilitate cross-border payments becomes an inevitable choice.

As shown in the previous section, Alipay's global expansion strategy indicates that only large players can prevail on the international playing field. On top of winning domestic market coverage, Alipay's market coverage extends to over 200 countries, serving 45 million Chinese customers in international markets[31]. Alipay's global partnerships include international payment companies and major merchants for both in-app and physical store payments. For example, collaboration between Alipay and Finnish ePassi[32] simplifies commercial transactions in Finland for Chinese visitors, who on average contribute over 206 euros per day per person, ranking first among other visitors. These partnerships are altogether integrated into the "Alipay+" campaign, in which Alipay displayed its ambition in three major consumption scenarios including airports, shopping markets and food service. Alipay, or in a broader sense, Ant Financial, is expanding globally to establish a digital person-to-all environment worldwide for Chinese customers.

Why Partnerships form

Mutual benefit is a central element in the abovementioned partnerships. For global partners, the large Chinese consumer market means obvious business opportunities and cooperation with Alipay can facilitate the acquisition of Chinese customers. Adoption of Alipay's digital wallet is widespread among Chinese: according to Chinese Ministry of Industry and Information, digital payment in China boasts a penetration rate of 65%, ranking 1st around the globe. Thus, catering to the favorite payment method among Chinese customers is a sensible step for many retail companies that rely on Chinese tourists' purchasing power.

For Chinese Fintech companies, mainly represented by Alibaba Group as a technology company, going abroad is one critical step, although their survival as a company is not necessarily dependent on this expansion. In our observation, at least two key strategic points should be taken into consideration when assessing Alipay's international strategy: differentiation of its payment service and big data collection from consumer groups. On the one hand, the

[31] Alipay, Sina Weibo, October.20, 2016, (accessed on Mar 18, 2017) http://www.weibo.com/1891502860/EdJoeau0j?from=page_1006061891502860_profile&wvr=6&mod=weibotime&type=like#_rnd1489899397150

[32] For details, visit ePassi's official website at http://en.epassi.fi/products/epassi-alipay/ or business media's coverage at http://www.helsinkibusinesshub.fi/article/chinas-biggest-mobile-payment-platform-alipay-expands-to-finland-with-epassi-payments/

international collaborations seamlessly serve their original consumer groups in a broader and more challenging market, while at the same time avoiding isolated islands of information at home and abroad and fulfilling their ultimate goal: to serve the needs of each and every individual. With the potential to become an extremely competitive technology company with its own business eco-system, comprehensive and coherent data on customer behaviors when they are abroad adding quantity and quality to the big data collection, that could eventually lead to the development of artificial intelligence. On the other hand, domestic competition with Tenpay, the payment provider behind WeChat's wallet, is becoming increasingly intense, as Tenpay, in combination with WeChat's social network, is the ideal peer-to-peer payment provider. Therefore, Alipay chooses to differentiate itself in its business operations. Internationalizing is a smart choice to explore other possibilities abroad. Alipay is able to attract more customers who are likely to remain on its platform as they would forego the advantage of using the payment services abroad when switching to Alipay's competitors. In addition, Tenpay seems to be less vigorous in foraying into foreign markets. Once it ventured overseas, WeChat's diverse functions like ordering food, buying movie tickets, or calling taxis that users can use in China were limited to Chinese internet services, leaving it unable to maximize its strongholds in interaction among consumer groups.

6.1.2 Overseas Market Exploration: Tremendous Opportunity Awaits

Business opportunities in overseas market are closely related to local customer demand: unmet financial needs for the booming e-commerce sector, that is characterized by under-developed means of digital payment. This is largely due to a large community of customers in developing countries, especially in Southeast Asia, that does not have access to a formal banking and financial system. Payment services are the first step for to connect with these customers and in subsequent steps additional financial services can be offered. Two major indicators behind the surging demand for financial services are identified as follows:

(1) Gap between supply and demand: prevailing informal finance

In terms of formal financial inclusion provision, there are significant differences across income categories in Southeast Asian countries with regard to the use of financial services. A survey conducted by the World Bank in the Philippines in 2015[33] indicates that 41% of surveyed adult Filipinos do not use any formal or commercial financial product. Those in the lower

[33] World Bank, *Enhancing Financial Capability and Inclusion in the Philippines*, Group, World Bank Other Operational Studies, 2015 (accessed on March 11, 2017). http://www.responsiblefinanceforum.org/wp-content/uploads/Enhancing-Financial-Capability-and-Inclusion-in-the-Philippines-FINAL1.pdf

quartile normally have much lower awareness of wealth management as a result of rare participation in the financial sector and they usually prefer storing money under mattresses to saving in a bank account. A similar situation can be observed in Indonesia, where less than 30% of the world's fourth-largest population own a bank account. Further contributing to low financial inclusion is the low coverage of financial infrastructure in a number of developing countries, for example many in-store retailers accept only cash in major cities of the Philippines. According to a report written by the Asian Development Bank in 2017[34], primary financial services - *Payments*, *Savings*, *Credits* and *Insurance* in the four countries observed (Indonesia, the Philippines, Cambodia and Myanmar) show significant gaps for people at the base of the pyramid, women and for SMEs. The lack of infrastructure as well as awareness about financial services thus poses tremendous obstacles to daily payments, and constitutes a major barrier for the development of local internet companies like Lazada and GrabTaxi in Indonesia. Even for those who can get access to financial services, the financial system capacity is not sufficiently developed. Generally, local payment systems are underdeveloped as is shown by the rate of failed online payment that stands as high as 20% in the Philippines.

<u>(2) Financial consumption patterns</u>

In light of how local consumers react to the possible entry of Fintech companies, two relevant patterns stand out:

a) Preference for informal financing services. For people in Southeast Asian countries, the formal financial service sector seems less attractive than informal channels, which is partly a consequence of low levels of financial literacy and overall awareness of potential financial risk. Many consumers prefer borrowing money from friends or relatives rather than going through complicated processes in the formal banking system. Due to the lack of credit information, the banking system lacks the necessary information when providing its services and hence might lead to vicious cycles when difficulties arise. In order to strengthen financial resilience regulators and supply-side participants need to collaborate, opening a large opportunity for ambitious actors to enter the market.

b) Tendency towards credit-financed consumption. Although many countries have a low rate of financial inclusion and an underdeveloped financial system, potential consumer demand is unexpectedly strong. According to the observation of Zhen Fund, local Filipinos spend 3$ on a

[34] Asian Development Bank, *Accelerating Financial Inclusion in Southeast Asia With Digital Finance*, Jan 2017 (accessed on March 11, 2017)
https://www.adb.org/publications/financial-inclusion-south-east-asia-digital-finance

Starbucks coffee when they only earn 300$ a month[35]. People like online shopping even if the delivery and quality of goods are barely satisfactory. With regard to consumer finance overseas, Maidanxia, a Fintech company focusing on providing consumer lending, also recognizes the great business opportunity of providing microloans to low-income groups in Southeast Asia. Hu Dan, CEO of Maidanxia, said in an interview that he is in negotiations with Indonesian E-Commerce Company Max for future cooperation in the field of consumer finance[36].

Risks and returns oftentimes coexist. In examining the status quo of these developing countries, we observe a subtle coincidence: the market expansion of the internet industry resembles the trend China witnessed 10 years ago, a time when the internet industry just started booming and unimaginable market potential began to emerge. Still, Chinese Fintech companies recognize the difficulties and obstacles for their international expansion that arise from local differences in regulatory environment or cultural habits.

6.2 Facilitating Technology Transfer through international expansion

The second external factor for Chinese Fintech companies to expand overseas is the synergy of advanced technology on a worldwide scale. In this sense, going abroad is an important means to improve research and development of financial technology *per se*, aside from merely exploring more prospective customers for the existing business model. Considering the strengths of Chinese Fintech companies, technology constitutes the key advantage in their business development overseas. Operational experience is conducive, though, technical experience as represented by core algorithms or user interface optimization is the competitive edge that is most marketable and exportable.

The technology exchange takes place between Chinese Fintech companies and companies abroad in two directions. On the one hand, Chinese Fintech companies are making outbound FDI in overseas partners by means of mergers and acquisitions (M&A) or joint-ventures (JV), whereby high-technology is transferred in exchange for access to markets teeming with financially underserved individuals and SMEs. Desirable partners therefore can be local Fintech

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[35] Liu Yuan, "真格VP刘元的印尼手记", Mar 2017, *Zhen Fund's official WeChat Account*, Mar 2017 (accessed on March 10, 2017).
http://mp.weixin.qq.com/s?src=3&timestamp=1489901940&ver=1&signature=csGqay1awdSAj5KpKCPqylbJw08LrfvuO5ZQEg7XOxG7OKgm8DW*NNiBL-nPJXfjeXhqAQ2X9b8*69X0np*ZxDVWN-sQITzaJFYeskSvhjmAOISHAAS78PwZ26ujSNl7fdbOE7kRDwlBJqTbLJFceXVUNQfdd7GnqgYY67Nj7mk=

[36] Sohu Business, "支付单一、金融科技弱、企业低估值,印尼"痛点"竟成最大商机", Mar 14, 2017, (accessed on March 16, 2017).http://business.sohu.com/20170314/n483358168.shtml.

companies in their formative stage, or conventional financial service providers, both of which are more approachable to the communities than a foreign company that inserts itself in the foreign market. With this win-win collaboration model, Chinese Fintech companies can thus vicariously extend their customer base through the local 'agency/client', in which case they offer the cutting-edge technology as an enabler and then receive a quota share of revenue in return. Although no real business is carried out in name of Chinese Fintech companies, they are profiting from the overseas customers in the process. In this regard, as previously argued, technical experience plays the pivotal role, with operational experience only coming second, in enabling the overseas partners because these experiences gained in China are harder applied to other markets than the technology underpinning the business model.

At the end of 2015, Dianrong.com concluded a tentative agreement with Hanwha Group, an established Korean consortium renowned for conventional financial services, to start a P2P lending JV in Korea. According to the official disclosure and our on-site interview with Dianrong.com officers, the Chinese company will assume the main task in terms of technological solutions, from the patented bidding system of Tuan-Tuan-Zhuan to Fintech-related legal services. Meanwhile, Hanwha Group acts as a value-adding brand to the JV as Koreans are mostly aware of Hanwha Group rather than Dianrong.com. By the same token, Ant Financial invested twice in Paytm, an Indian Third-party Payment provider, and transferred its advanced desktop/mobile payment technology to help Paytm successfully grow into the 4th largest payment company in India with a humongous customer base exceeding 135 million. Ascend Money, a Thai version of Ant Financial, also received an offer for strategic collaboration from Ant Financial in November 2016, for resembling reasons.

On the flip side, Chinese Fintech companies, especially mature companies, are actively engaging in acquisition of companies possessing more advanced technology, regardless whether they specialize in financial technology or other relevant fields. The underlying motivations usually boil down to two major ideas. First, acquisition is another way of conducting research and development, and because technology is the engine of future growth, for a visionary Fintech company it proves always advisable to develop in-house innovations as well as acquire advanced technologies. Additionally, the timing of acquisition has to precede the competitors advancing to a higher state of competitivity in the market. Those to be acquired, however, oftentimes tend to be receptive as well, in particular if the companies are no direct rivals prior to the acquisition.

Moreover, instead of being constrained, they are only more likely to switch to a fast track and expedited development, thanks to support and guidance from the mature companies.

As an example, in September 2016, Ant Financial acquired EyeVerify, a Kansas-based leading biometrics company. EyeVerify is reported to have been developing a verification technology using biometrics data of human eyes, which if realized would be a fantastic alternative to password or fingerprint verification. It is fair to assume that this technology could be applied to Ant Financial products to improve security of accounts and transactions. In a more recent M&A practice on January 26, 2017, Ant Financial joined efforts with MoneyGram, an American bank transfer service provider, so as to enable each other in the field of trans-border payments. Likewise, in 2016 PingAn Group joined the R3 block-chain network that connects major Fintech tycoons, in a way that contributes to PingAn's commitment to the future generation of key financial infrastructures. Proceeding along PingAn's path, AIA Hong Kong and China Merchants Bank quickly followed suit.

6.3 Political strategies as a driver for Chinese Fintech expansion

The third external factor for Chinese Fintechs to expand abroad is the international political environment. In 2013, China's central government has put forward the One Belt, One Road strategy with the aim to increase interconnectedness between countries in an area spanning from China to Western-Europe. Due to the large customer base in developing countries along the One Belt One Road such as Thailand or Myanmar but also the inclusion of developed countries in Europe in the One Belt One Road, this political strategy could provide an impetus for Chinese Fintech companies to expand their operations in these markets. Seeing furthermore the potential demand if the promise of economic development is fulfilled for many developing countries along the Belt and Road, using this opportunity seems like an obvious strategic decision.[37]

Especially larger companies who hold a clear international strategy are cognisant of the One Belt One Road in their steps to expand operations abroad and proclaim to support the central government's initiative. Growth companies are of course aware of such strategies but the political initiatives have a lesser influence on their strategic decisions. However, even the leading actors in China's Fintech landscape such as Ant Financial are cautiously refraining from fully embracing the Belt and Road initiative as the core driver of their international expansion

[37] Sabine, Peter "One belt, one road's digital initiative is full of potential, but Hong Kong firms need to be wary of pitfalls," *South China Morning Post,* November 01,2016 (accessed on March 04, 2017). http://www.scmp.com/specialreports/business/topics/one-belt-one-road/article/2041881/one-belt-one-roads-digital

strategies. This is mainly influenced by the limited tangible benefits that the Chinese government's strategy has yielded to date. While political strategies such as the Belt and Road have some form of influence over the decision to expand internationally, the companies still weigh commercial considerations with greater importance when assessing the viability of an international engagement.

From the companies' point of view, the central government should provide increased support for their international expansion in line with the political strategy through for example enhanced assistance in setting up partnerships. Interestingly, the governmental agencies with whom the authors conducted their interviews voiced a similar expectation towards the Fintech companies. In order to realize the Belt and Road strategy, the companies should strengthen their own efforts to expand into new markets and set up partnerships there. Both the companies and the regulatory agencies are committed to the idea of international expansion if it is perceived as feasible but expect the other side to take the first step in the concrete implementation of this commitment. Therefore, the political strategy is an initial motivation for the Chinese Fintech companies to contemplate expanding internationally and brings the issue to their attention. In terms of concrete projects, however, the Belt and Road initiative's influence as factor of the decision to expand internationally remains of lesser importance. Oftentimes hurdles in the regulatory environment or the lack of cultural knowledge in the foreign market, still represent obstacles for the international expansion.

7 REMAINING OPPORTUNITIES IN CHINESE FINTECH MARKET

Unlike Chinese Fintechs' own size or financial needs in overseas markets, domestic challenges such as stricter regulation and market saturation do not influence Chinese Fintechs' expansions abroad. Some experts have argued that difficulties in China will compel Fintechs to move the interviews, those factors did not influence the decision of Chinese Fintechs to explore new markets, but in some cases rather allowed them to develop and strengthen their own capability inside China.

Many agreed on the point that the Chinese Fintech market has not yet matured or is not yet saturated; therefore, companies still have many opportunities to expand. According to research by KapronAsia, although growth has slowed down, the Chinese Fintech payment industry is still expanding in the domestic market. So, in this situation, Chinese Fintechs may focus more on stabilizing their growth within China rather than expanding abroad. Increasing competition between different players is also not seen as a factor to explain the expansion phenomena because the Chinese market has stabilized and is still growing. Payment industry in China may be the most developed and competitive sector compared to the other Fintech sectors such as P2P that is recently growing. However, despite the fact that it is the most developed industry, it is still regarded as the one that has many opportunities. Although there is competition in the domestic market, it is not a critical factor that pushes Chinese Fintechs to adopt an international development strategy.

The Ant Financial Research Institute further mentioned that the scale of the domestic market is still considerably large, so it won't be saturated for a long time. A researcher at Hengchang, a wealth-management company, highlighted the opportunities in the Chinese Fintech market, implying that Chinese Fintechs do not regard fiercer competition or market saturation as a current phenomenon in the domestic market. Besides the big cities, there are many regions like rural areas in China where Fintech services are not yet fully provided. Market saturation for the whole Chinese market is a very distant story. The interview with Dianrong provided a more detailed analysis of the situation regarding the Chinese Fintech market. As consumer lending is a very recent service provided in China, it is going to keep growing; products will become more advanced and comprehensive in the future. In terms of the P2P market, there was a consensus among different companies that it still provides opportunities to the companies to expand their business models although this industry is already in an advanced stage compared to other Fintech sectors.

The interview with Dianrong further outlined that external factors such as the potential in developing countries are more critical in Fintechs' decision to increase their presence outside of China. Stricter domestic regulation for the Fintech industry was even seen as a positive influence on the domestic market when eliminating bad companies and letting the good ones develop further. Therefore, stricter regulation is distinctly not a pushing factor for Chinese Fintechs to invest in the overseas market. Overall, Chinese Fintechs still believe that China is the best market for their expansion and investment with potential profitable opportunities for the companies.

8 CONCLUSION

In recent years, the Chinese Fintech companies have seen an enormous rise as they overtook American or British firms' role as the leader in the global Fintech industry. With all eyes focusing on China's Fintech industry, a number of high profile cases of international expansion in the form of partnerships or foreign investments have attracted attention towards the Chinese Fintechs' activities abroad. This report has tried to shed light on the underlying drivers and obstacles of these activities.

In the interviews which the authors conducted with various representatives of the Chinese Fintech industry, one internal and three external factors emerged as main influences on the Fintech companies' decision to expand internationally. The former, represented by a company's internal stage of development, exerts the most important influence on this decision. With a rising level of company maturity, the sophistication of the international expansion activity increases. Growth companies, which are in an earlier stage of development, still focus on improving their operations within the domestic market. The latter take a secondary position with regard to the company's decision to expand internationally and can be divided into external pull and push factors. Among these, the demand for financial services abroad caused by the lack of financial inclusion in many developing countries in particular in South and Southeast Asia as well as the internationalization of Chinese domestic demand through for example tourism are the main pull factors for Chinese Fintech companies to expand abroad. Moreover, the technological advantages Chinese Fintech companies have developed and the demand for this technology in partnerships with foreign companies is acting as both a pull and push factor. Lastly, the Chinese One Belt One Road strategy has an additional influence as a push factor for Chinese companies to expand abroad. Interestingly, all companies reaffirmed that increased competition and regulatory tightening did not motivate Fintech companies to expand abroad. This effect is more pronounced for P2P lending platforms while payment providers, incidentally bigger companies with higher company maturity tend to favor international expansion.

Building upon the understanding of drivers and obstacles for Chinese Fintech companies when expanding abroad, the question whether these activities are likely to succeed merits further research. Such an assessment will need to take into account the situation in the many countries where partnerships have formed or investments been made. What can be said for sure is that Chinese Fintech companies are here to stay. Once the competition has produced the next of leading Fintech companies in sectors such as P2P lending and obstacles for international expansion such as regulatory uncertainty and lack of knowledge about markets abroad will be overcome, not only the three big internet companies Baidu, Alibaba and Tencent but also other companies will emerge on the international stage. Chinese Fintech companies will therefore continue to form the epicenter of technological innovation in the near future and play a greater role in overseas markets than they have done before.

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