Financial Infrastructure Is Being Rebuilt

As Peter Drucker said, "The greatest danger in times of turbulence is not the turbulence; it is to act with yesterday's logic."

Key Takeaways:

Market volatility benefits our portfolio. Three of our five largest holdings operate exchanges that facilitate risk management and price discovery during periods of uncertainty.

Payment innovation succeeds when it simplifies the user experience. Despite rapid technological change, consumers still prefer payment methods that are familiar, predictable, and frictionless.

Artificial intelligence is beginning to reshape commerce. Agentic commerce may transform product discovery and purchasing behavior, but adoption will depend on maintaining simplicity and trust.

Legacy payment rails are disappearing. The long decline of paper checks reflects the broader modernization of financial infrastructure.

Fintech platforms are moving closer to the regulated banking system. Firms increasingly seek banking charters to control deposits, settlement, and lending infrastructure.

Introduction:

In volatile market environments, our strategy has historically performed well. We obviously did not anticipate that the United States would strike the Iranian regime, triggering heightened instability in the Middle East. However, our portfolio positioning has proven to be well aligned for this type of environment.

Three of our five largest holdings are in the exchange space. These businesses tend to benefit from periods of elevated market volatility. When uncertainty increases, institutions hedge exposures, rebalance portfolios, and manage risk more actively. That activity ultimately flows through the exchanges that facilitate price discovery and risk transfer.

We were not modeling for oil prices to spike due to the potential risk of transit through the Strait of Hormuz, but our portfolio still benefits from the resulting uncertainty. Higher oil prices are not ideal, as they can create inflationary pressure. However, geopolitical instability and macro uncertainty drive market participants to hedge their exposures. Periods of stress also highlight another advantage of our portfolio. All of our companies generate significant free cash flow.

When volatility increases, many companies lose access to capital. Our holdings, however, can deploy capital and play offense. Over the last several weeks, multiple companies in our portfolio have executed strategic investments and acquisitions that competitors simply were not in a position to pursue. We prefer to play offense when others are nervous and hesitant.

Historically, those have been the environments where our companies create the most long-term value. As Warren Buffett once said, "Be fearful when others are greedy and greedy when others are fearful."

While the geopolitical backdrop remains fluid and difficult to forecast, we do not believe there is much value in attempting to handicap macro variables such as interest rates, inflation, or energy prices while a military conflict is unfolding. Instead, we prefer to focus on the areas where we have deep domain expertise. Structural changes in financial technology, payments, and market infrastructure continue to reshape how money moves through the global economy. In our view, the plumbing of the financial system is being rebuilt in real time.

KISS or Keep It Simple Stupid:

Successful innovation removes friction rather than creating it.

We are big fans of the expression KISS, or keep it simple stupid! In our view, simplicity still wins in payments. For all the innovation reshaping payments, consumer behavior remains remarkably consistent. Most shoppers still gravitate toward what feels simple, familiar, and reliable. New technologies may grab headlines, but at the point of sale, convenience and control continue to outweigh novelty.

Despite the growth of digital wallets, agentic commerce, and cashier-less checkout concepts, many consumers still prefer traditional in-person checkout and card-based payments. When given a choice, shoppers often select options that minimize steps, reduce uncertainty, and avoid friction. This preference is not about resistance to technology, but about confidence. Payments work best when consumers do not have to think about them.

This reality creates a disconnect between where retailers are investing and how consumers want to pay. Self-checkout and unattended payment experiences are expanding, yet many shoppers feel pushed into these flows rather than opting in. Complexity, forced account creation, and multi-step checkout processes are common sources of frustration. In contrast, transactions that are quick, intuitive, and predictable leave customers feeling in control.

Cards continue to dominate for this reason. Credit and debit cards remain the default payment method for most consumers because they are universally accepted, require minimal effort, and work consistently across channels. While digital wallets have made progress, particularly outside the US, they have not yet displaced cards as the primary payment choice for everyday commerce. Networks such as Visa and Mastercard have succeeded not by changing consumer behavior, but by embedding themselves invisibly into it.

The lesson for the broader payment ecosystem is straightforward. The most successful payment innovations reduce friction rather than introduce it. New rails, new form factors, and new payment methods must ultimately deliver a faster, simpler, and more reliable experience than what already exists. If they introduce extra steps, uncertainty, or learning curves, adoption will remain limited.

This insight also helps explain why many emerging payment technologies, including real-time payments and stablecoins, are gaining traction behind the scenes rather than at the point of sale. Consumers do not need to see innovation to benefit from it. The most successful payment systems are those that modernize infrastructure while preserving the simplicity users expect.

In the end, progress in payments is not about offering more choices. It is about making the right choices effortless. The winners will be the platforms and networks that understand that simplicity is not a constraint on innovation, but its ultimate goal.

Agentic Commerce:

AI may change how consumers discover products and make purchases, but adoption will depend on maintaining simplicity and trust.

Payment innovation has rarely been constrained by a lack of ideas. It has almost always been constrained by adoption. New technologies routinely promise faster, smarter, or more personalized experiences, yet consumers consistently gravitate toward what feels simple and reliable. That same dynamic applies today as artificial intelligence begins to reshape how people shop and pay.

This is where the concept of agentic commerce enters the conversation. Agentic commerce refers to AI-driven software agents that act on behalf of consumers to discover products, compare prices, and in some cases complete purchases. Instead of browsing websites or navigating checkout flows, consumers delegate those tasks to intelligent systems that operate based on preferences, budgets, and prior behavior. In theory, this could dramatically reduce friction and decision fatigue.

The appeal is easy to understand. AI agents promise faster discovery, higher conversion rates, and a more personalized shopping experience. Early data suggests that merchants experimenting with agent-driven interactions see meaningful improvements in engagement and efficiency, particularly in retail environments where choice overload is common. For merchants, the incentive to explore agentic commerce is real.

However, the same lesson that governs all payments innovation still applies. Technology only succeeds when it removes friction rather than adds it. Today, most consumers are not yet comfortable allowing AI agents to complete purchases on their behalf. While many are willing to use AI for research or recommendations, full delegation raises concerns around trust, transparency, pricing clarity, and dispute resolution. Consumers want to feel in control, especially at the moment money changes hands.

Merchants and payment providers share similar reservations. Introducing an automated agent between buyer and seller complicates questions around fraud, authentication, chargebacks, and accountability. Existing payment systems are designed around clear human intent and well-defined liability frameworks, making fully autonomous transactions difficult to support without new authentication and governance models. While agentic systems can deliver richer data about shopper intent and budgets, they also introduce new operational and risk-management challenges. As with prior shifts in payments, confidence will be built slowly through experience, not marketing.

This tension reinforces a broader truth about payments behavior. Despite the growth of digital wallets, self-checkout, and cashier-less concepts, most shoppers still prefer straightforward, predictable payment experiences. Cards remain dominant not because they are exciting, but because they work consistently, require minimal effort, and are universally accepted. Even in an agentic world, existing card networks are likely to remain central architects of the ecosystem rather than displaced intermediaries. Innovation that forces consumers into unfamiliar or overly complex flows often feels like friction, not progress.

For agentic commerce to scale, it must pass the same test every successful payment innovation has faced before it. Does it make the experience easier, clearer, and more intuitive? Or does it add opacity and uncertainty? The most likely path forward is incremental. Product discovery and comparison will become increasingly agent-driven, while payments remain anchored to trusted, familiar rails. Over time, as transparency, controls, and safeguards improve, deeper automation may follow. In the end, agentic commerce is not a rejection of the KISS principle. It is a challenge to live up to it. AI-driven shopping will only succeed if it hides complexity rather than exposes it, preserves consumer confidence, and integrates seamlessly into existing payment ecosystems. As with every major evolution in payments, the winners will not be those with the most advanced technology, but those who remember that simplicity is the ultimate feature.

The Slow Death of Paper Checks:

Paper checks are gradually disappearing as outdated payment infrastructure becomes more expensive, risky, and inefficient.

Paper checks are finally approaching their end, not because they stopped working overnight, but because the economics, risks, and infrastructure supporting them no longer make sense. The Federal Reserve's recent decision to solicit public input on reducing its check processing services is a clear signal that the long, gradual decline of checks is entering a more decisive phase.

Check usage has been falling for decades as consumers and businesses migrated to cards, ACH, wires, and digital wallets. What has accelerated the decline more recently is fraud. Check fraud has grown materially, while the infrastructure required to process checks has aged and become increasingly expensive to maintain. From the Fed's perspective, continuing to invest heavily in a shrinking, higher-risk payment rail is becoming harder to justify.

That said, checks persist because the US payments system remains fragmented. Unlike countries that built low-cost, interoperable, real-time payment networks, the US evolved through layers of private systems and legacy rails. While instant payment options now exist, including Fed's FedNow platform, adoption has been uneven and scale remains limited. As a result, checks continue to fill gaps that modern infrastructure has not yet fully closed.

The Fed's request for comment highlights a central tension. Eliminating check services without sufficient alternatives risks disruption, particularly for smaller institutions and certain business workflows. At the same time, maintaining check infrastructure indefinitely slows the transition toward faster, safer, and more efficient payment systems. This is less a debate about checks themselves and more an indictment of how slowly the US has modernized core payments.

Importantly, this moment reinforces a broader trend running through the financial system. As legacy rails become more expensive, risky, and outdated, pressure builds for new infrastructure to take their place. Real-time payments, account-to-account transfers, stablecoins, and tokenized money are increasingly filling roles that checks once occupied, offering faster settlement, better transparency, and lower fraud risk.

The decline of checks should not be viewed as a sudden disruption. It is the predictable outcome of changing technology, economics, and consumer expectations. The Fed's actions suggest that the endgame is no longer theoretical. Paper checks are becoming a legacy exception in a system that is steadily moving toward instant, digital, and programmable money. The only real question is how quickly modern payment rails scale to finally make checks obsolete.

Banking Evolution:

Fintech firms are increasingly moving inside the regulated banking system to control deposits, payments, and lending infrastructure.

For decades, banking was defined by physical distribution and balance sheet scale. Branch networks mattered. Deposits were gathered in person, lending was paper-based, and technology primarily served back-office functions rather than competitive differentiation. That model is being dismantled. Today, banking is increasingly defined by software, data, and connectivity. Payments move faster, accounts are opened digitally, and lending decisions are increasingly automated. APIs replace tellers, mobile devices replace branches, and customer engagement is driven by technology rather than location.

This is not a story about banks disappearing. It is a story about which functions inside a bank now matter most. Payments, liquidity management, risk controls, compliance, and data analytics increasingly drive returns, while physical infrastructure has become far less relevant. We strongly believe that banking is no longer a place customers just visit; it is an always-on infrastructure layer embedded in everyday commerce.

From our perspective, this shift favors FINTECH-native operators. Firms built around payments, software, and data are structurally better positioned to deliver modern banking services than institutions attempting to retrofit decades-old systems. The competitive battleground has moved, and many traditional banks remain anchored to an outdated model.

Regulations:

For much of the past decade, FINTECH innovation developed just outside the traditional banking system. Technology-first firms relied on sponsor banks, state licenses, and payment networks to avoid the cost and complexity of full banking regulation while still accessing critical infrastructure. That model is becoming harder to sustain.

As digital payments, embedded finance, and stable-value instruments grow in size and importance, regulators are pushing activity toward clearer oversight. The message is increasingly straightforward: innovation is encouraged, but systemically relevant financial activity must sit inside a regulated framework. This shift is reshaping competition.

Regulation is no longer just a barrier to entry; it is becoming a differentiator. Firms capable of meeting higher standards around capital, governance, and risk management gain durability, lower funding risk, and greater strategic flexibility than those operating at the edge of the system. Regulation is moving from an obstacle FINTECHs tried to avoid to a framework the strongest platforms now embrace.

Banking Charters as Infrastructure:

As regulation has moved from constraint to catalyst, banking charters have become strategic assets rather than regulatory burdens. For years, many FINTECHs viewed licenses as unnecessary overhead. Today, charters increasingly represent control points within the financial system, defining who can hold deposits, move money, extend credit, and manage risk at scale.

For large payments platforms, bank charters are increasingly about reducing reliance on sponsor banks and gaining direct control over lending, deposits, and acquiring, tightening the link between payments, settlement, and balance sheet products. Owning a banking charter fundamentally changes the economics of a platform. It provides direct access to deposits, lowers funding costs, reduces reliance on third-party intermediaries, and tightens the connection between payments, balances, and lending. Just as importantly, it creates regulatory clarity around supervision, governance, and consumer protection, elements that become more critical as platforms grow and serve larger, more sophisticated customers.

Not all charters are designed to do the same things, and that distinction is intentional. Different licenses permit different roles across the banking stack, including custody, settlement, insured deposits, and credit creation. Rather than forcing a single definition of what a bank must be, regulators are allowing multiple charter types to coexist, each optimized for a specific function within the system.

The result is a more modular banking infrastructure. Banking increasingly operates in the background of commerce, with specialized institutions providing discrete capabilities that integrate seamlessly with software platforms and payment networks. Control of critical rails and data flows is becoming more important than physical distribution, while traditional banks increasingly focus on balance-sheet management, underwriting, and regulatory expertise. This shift has raised questions around regulatory consistency and competitive balance, but it is also creating new partnership opportunities, particularly for regional and community banks that may prefer to leverage emerging payment, custody, or tokenization infrastructure rather than build it internally. Banking charters are evolving from regulatory permissions into core infrastructure, shaping how capital, payments, and data move through the modern financial system.

Bridging the Gap Between FINTECH and Banking:

Recent announcements from large FINTECH platforms underscore how quickly theory is becoming reality. Several leading firms have taken concrete steps to establish regulated banking entities in order to bring payments, deposits, and digital asset activity under direct supervisory oversight. While the specific charters and use cases differ, the direction is unmistakable.

These moves reflect a broader realization across FINTECH. Operating adjacent to the banking system is no longer sufficient at scale. As platforms grow larger and handle more critical payment and liquidity flows, reliance on partner banks and fragmented regulatory structures becomes a strategic constraint. Control over funding, settlement, compliance, and customer trust increasingly requires a direct regulatory footprint.

Importantly, this is not a return to traditional banking models. FINTECH firms are not trying to replicate branch networks or legacy operating structures. Instead, they are selectively entering the banking system to control specific infrastructure layers while continuing to leverage software, data, and embedded distribution. In this sense, they are bridging the gap between innovation and regulation and redefining how banking services are delivered. FINTECH leaders are no longer skirting the banking system; they are entering it deliberately to bridge innovation and regulation.

Banking is not being disrupted out of existence; it is being restructured. The industry is moving away from a model defined by branches and physical distribution toward one centered on software, payments, data, and regulated infrastructure. At the same time, regulation is no longer acting solely as a constraint on innovation. Instead, it is drawing systemically important FINTECH activity inside clearer supervisory boundaries, reshaping competition, and raising the bar for scale, governance, and durability.

As a result, banking charters are evolving into strategic infrastructure rather than simple regulatory permissions. FINTECH firms are increasingly seeking targeted ways to enter the banking system, not to recreate legacy institutions, but to control specific functions such as deposits, payments, custody, and credit. The emerging model is modular, technology-driven, and embedded directly into commerce. Over the next decade, the most successful financial platforms will be those that can bridge innovation and regulation effectively, combining modern software and data capabilities with the trust, stability, and economics of regulated banking.

Conclusion & What This Means for Investors:

Financial markets will always be influenced by geopolitical events and macro cycles. However, the long-term drivers of value creation in our portfolio are structural changes occurring inside financial infrastructure.

Payments are becoming digital. Settlement is becoming faster and increasingly programmable. Banking is evolving from physical distribution toward software driven platforms embedded directly into commerce.

These shifts are not cyclical. They represent the continued modernization of the global financial system. Our research and portfolio construction remain focused on identifying the companies building and controlling this infrastructure. As financial systems continue to evolve, we believe the most durable investment opportunities will come from businesses that enable the movement of money, manage risk, and power the next generation of financial networks.

As always, reach out to me to discuss any of these topics and more. I look forward to speaking…

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Cliff Clavin's "Useless" Information:

In the 1980s, one of our favorite TV shows was ***Cheers.*** The know-it-all postal worker was named Cliff Clavin and played by actor John Ratzenberger. This recurring segment of our newsletter highlights a few pieces of trivia and observations that Cliff might appreciate.

- In September of 1987, Charles Schwab launched its IPO, selling 8 million shares of stock to the public at an original price of $16.50 apiece. Just 20 days later, the crash of 1987 hit. The stock market plunged (23%) in a single day, and Schwab's stock was hammered down to $6.50 a share. Showing the true power of compounding, the stock has returned over 52,000% since then.

- According to a recent YouGov study, 40% of Americans didn't read a single book last year. However, the average number of books read per person was 8. This is because the top 4% of readers read 46% of all books consumed. Just another example that using simple averages for analysis can be tricky.

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