ABU DHABI GLOBAL MARKET ACADEMY

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ADGM Academy

RESEARCH CENTRE

THE GLOBAL COVID-19 FINTECH MARKET IMPACT AND INDUSTRY RESILIENCE STUDY

PRODUCED BY

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ABU DHABI GLOBAL MARKET ACADEMY (ADGMA)

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The COVID-19 pandemic has disrupted how people interact with one another and their surrounding environments. Hence, it is not surprising that it has impacted how financial services and products are accessed and used. This study, which builds on previous work, assesses the medium-to-longer-term impact of COVID-19 on the FinTech industry and includes issues such as the customer base of these firms and their potential impact on financial inclusion.

MARKET PERFORMANCE

Retail-facing firms operating in advanced economies (AEs) still dominate in terms of transaction values.

As we describe in more detail below, transaction values in AEs exceeded those in emerging market and developing economies (EMDEs) for all verticals. Furthermore, for all verticals except payments, growth rates were higher for firms operating in AEs. Overall, issues such as the scale and development level of the financial sector may have affected these trends. In addition, many EMDEs still lack regulatory frameworks that allow FinTechs to provide regulated services. Thus, from a policy perspective, authorities should assess whether the lack of a supportive regulatory regime is a factor affecting the FinTech industry's development.

Digital payments were the largest segment by transaction values, followed by digital lending.

The transaction value of digital payment FinTechs accounted for 63% of all retail-facing FinTechs. Although firms in AEs contributed to most of the total value of annual payment transactions, firms in EMDEs grew at a faster pace. This finding indicates there is still significant room for growth in EMDEs, which aligns with market trends in the digital payments industry as a whole. Digital lending was the second-largest market segment, accounting for 20% of transaction values. In contrast with payments, digital lending activities remain largely concentrated in AEs, with most of the activity and growth spurred by platforms in AEs. Furthermore, at a global level, the activities of digital lending firms in EMDEs decreased. Nevertheless, it is important to highlight that in a few larger EMDEs, transactions by lending platforms had already surpassed the billion-dollar mark, indicating the potential of these platforms. The remaining verticals are still concentrated in AEs, including capital raising and insurtech. However, the levels of these activities are lower than those in other verticals.

In contrast to retail-facing firms, both the concentration of activity and growth in terms of transaction values was dominated by market provisioning platforms in EMDEs.

Globally, enterprise technology provisioning and regtech grew swiftly and remained the verticals with the most transaction activity. Conversely, alternative credit and/or data analytics was the only vertical to report a decrease in the number of transactions, performing worse than they had anticipated as reported in The Rapid Assessment Study.

A common finding across retail-facing and market provisioning firms was that a significant number were operating in more than one jurisdiction.

Of respondent firms, 30% reported having operations in more than one country. Furthermore, most firms operating in EMDEs were headquartered in foreign jurisdictions, mainly in AEs. Financial supervisors should assess the importance of this finding in terms of their respective jurisdictions to determine whether they need additional coordination arrangements with foreign supervisors.

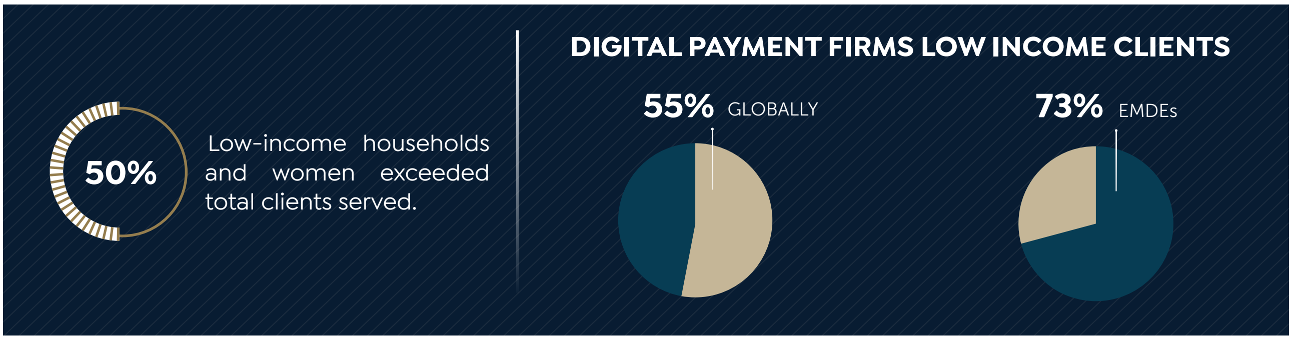
CUSTOMER BASE AND POTENTIAL IMPACT OF FINTECH ON FINANCIAL INCLUSION

One of our most important results relates to the customer base of the platforms and FinTechs' potential contribution to financial inclusion.

A large proportion of FinTech clients were new customers, and customers from groups that in many countries have been underserved by traditional financial institutions (incumbents), such as small and medium-sized enterprises (SMEs), low-income households, and women. Furthermore, in many FinTech verticals, the proportion of low-income households and women exceeded 50% of total clients served.

The percentage reported was even higher for FinTechs operating in EMDEs. For instance, digital payment firms reported that the proportion of low-income clients was 55% globally, and 73% when looking at those in EMDEs.

This may indicate that FinTechs positively contribute to financial inclusion. However, a more detailed analysis, for example, of customer profile and terms of service provisioning, is needed to confirm this.



OPERATIONAL RESILIENCE AND FINANCIAL HEALTH DURING COVID-19

→ **In tandem with their growth, FinTechs reported significant operational challenges and increases in risks, particularly in EMDEs.**

The types of challenges faced varied by vertical and region, but common challenges included high levels of unsuccessful transactions, platform and partner downtime and increases in liquidity risks, currency volatility, and regulatory risks. Financial supervisory authorities in EMDEs may want to assess how relevant our findings are in the context of their countries to determine whether they need to take any supervisory measure.

→ **FinTechs also reported an increase in all costs, except fixed costs.**

There were two interesting trends related to cost increases. First, FinTechs have been actively recruiting new employees in line with their growth, which explains the increases in human resources costs.

We did not analyse the types of skills firms required but, overall, innovation requires employees with relevant technology skills, who are not always available in all jurisdictions. Second, FinTechs spent a large proportion of their budget on research and development (R&D). This highlights the importance FinTechs place on continued innovation and their perceived growth prospects for the sector. In contrast, overall, firms reported a decrease in fixed costs, which seems to reflect reduced office costs.

→ Despite operational challenges and increases in expenditure, FinTech firms perceive the sector to be relatively resilient.

Overall, firms in all verticals reported increases in revenue and turnover. However, from the data collected, we could not assess whether these increases in revenue and turnover offset the reported increases in costs. Nevertheless, our survey provided important insights into firms' financial sustainability. In particular, firms reported higher valuations and capital raising activities compared to their forecasts outlined in The Rapid Assessment Study. Firms also reported higher future capital raisings in this study. As in other areas, there were important differences across countries and verticals. However, in general, firms in EMDEs reported higher valuations and capital raising. This may indicate investor interest in leveraging the untapped potential and opportunities provided by EMDEs. Regarding capital raising, digital payment firms overall were at a more mature development stage, raising larger funding rounds from venture capital funds (predominantly Series A and B).

CHANGES IN SERVICES

FinTechs prioritised changes that made their platforms more secure.

More than one-third of FinTechs prioritised enhancing cybersecurity features and preventing fraud as the main changes to their services in 2020. These changes seem to be in response to their risk assessment as they were the two most reported risks in 2019.

The changes seem to be effective as firms now reported lower levels of these risks. Other changes (particularly changes related to pricing structures that were made to help clients during the pandemic), such as reducing commissions and fees, were largely discontinued. Finally, only a small proportion of firms reported introducing sustainability products, in particular, environmental, social and corporate governance (ESG) products.

FINTECHS' USE OF REGULATORY AND POLICY SUPPORT, AND USE OF FINTECHS AS DISTRIBUTION PARTNERS

Financial supervisors implemented different regulatory mechanisms to help financial firms and FinTechs mitigate the effects of COVID-19.

Core regulatory support mechanisms, such as support for remote onboarding, cybersecurity and fraud-prevention standardisation, and simplified customer due diligence were the regulatory measures most used by FinTechs. However, overall, FinTechs judged that more support was needed across several areas, especially regulatory support for faster authorisation or licensing processes for new activities and less burdensome supervisory requirements. More generally, firms in EMDEs reported an overall lower level of satisfaction with regulatory support than those in AEs. Hence, more dialogue and engagement between financial supervisory authorities and the FinTech industry may be useful, especially as FinTech growth starts to increase in EMDEs.

Only 18% of FinTech firms reported using government relief measures.

In general, the use was concentrated in AEs, which may be because AEs had more fiscal space to implement relief packages.

Approximately 20% of firms participated as a delivery or implementation partner for a government-based COVID-19 relief scheme.

The Rapid Assessment Study reported governments' limited use of FinTech fir ms as distribution partners. There have, however, been some changes. Governments, especially in AEs, used lending platforms more often than FinTech firms had initially reported, reflecting the adjustments governments had made to their existing policies on selecting distribution entities. Digital lending, digital payments, and insurtech FinTechs were those with the verticals most used by governments to deliver COVID-19 relief programs. Going forward, governments should assess the relative benefits of using FinTechs compared to other solutions in supporting the delivery of government relief programs. In turn, this would help them determine whether they need to implement any changes to their policies to promote efficient delivery of mitigation and relief programs in future crises.

ABOUT ADGM ACADEMY

ADGM Academy is part of Abu Dhabi Global Market (ADGM), an International Financial Centre (IFC) located in the capital city of the United Arab Emirates. The Academy has been established with the vision of becoming one of the leading academies in the region, providing world-class financial research and training services.

Delivering world-class financial education and literacy, ADGM Academy will help to position Abu Dhabi as a leading global financial centre. This will be achieved through globally recognised educational and experiential programmes on a range of topics and qualifications in banking, finance, leadership, entrepreneurship, technical and soft skills.

ABOUT RESEARCH CENTRE

The ADGM Academy Research Centre brings together an ecosystem of academics, financial industry practitioners, government and technology experts to unlock the shared potential to improve the financial environment in MENA and beyond.

The financial industry continues to transform at a rapid pace with new technologies, disruptors, threats and opportunities appearing all the time. Independent research is crucial to be able to understand and utilise this transformation for the benefit of your business, your customers and society in general.

The Research Centre provides that understanding through insights developed in collaboration with the academic community.

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