Covid-19: Fintech Sector Impact & Response

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People | Ideas | Capital

Covid-19: Fintech Sector Impact & Response – Key Themes

- The Covid-19 pandemic has caused intense distress and tragedy for thousands of people around the world. Just as in other sectors, the global fintech ecosystem is fighting to protect colleagues, customers and local communities. We have seen inspiring examples of compassion and fintech innovation across diverse markets – to preserve health, livelihoods, businesses and economic productivity.
- We hope to continue our close partnership with clients to mitigate the human impact of this crisis. We also aspire to help fintechs and investors navigate the trends emerging from this difficult period. This paper explores those trends and an early outlook for the sector.

Expect renewed focus on mission, customer service, core product roadmap, risk management and sustainable profitability

Financial digitisation will accelerate; pivot towards fintech use cases in ecommerce, digital content, education and health

Impact across fintech sub-segments will be mixed; large payment platforms and leading digital banks to fare relatively well

Consolidation through mergers and partnerships will gain traction; need for scale to drive cost synergies and growth

Strategic acquisition opportunities to arise from funding / valuation compression; new opportunities in tech adjacencies

Covid-19: Fintech Sector Impact & Response – Key Themes

	Current Situation	Potential Outcomes
Business Performance	• Business development is challenged by global recession, but stronger secular trend in favour of digital payments • Fintechs offering new products and crisis support to users • Travel payments and FX platforms negatively impacted • Cost base pressure and early savings – Agile and lower fixed cost fintechs are outperforming – Pressure on staff given high cost technical employees – Growth-at-all-costs mindset is discarded, as weaker topline does not support high customer acquisition costs	• Fintech business models will pivot towards select ecommerce verticals and digital content, education and health use cases • Increased scrutiny of unit economics and profitability • Streamlined product roadmaps and enhanced focus on core mission and customer service, driving retention and growth • Geographic and product diversification will be beneficial • Players with large reliance on in-store POS will underperform • Select emerging markets with weaker health infrastructure and/or heavy reliance on tourism may be slower to recover
Funding Conditions	• Fintech funding in Q1 2020 falls to 2017 levels • Capital raising in Q2 will suffer as investors are looking to fortify balance sheets of existing portfolio companies • Limited seed funding as early-stage investors hold tight • Final flurry of late-stage deals include Grab's $850m fundraise, Ant Financial's investment in Klarna, Nets' acquisition of PeP and Revolut's $550m fundraise	• Greater investor focus on profitable business models • Investor-friendly term sheets (e.g., liquidation preferences) • Valuation opportunities for investors previously priced-out – expect more down rounds, side rounds and convertibles • Late-stage VC-backed fintechs that raised capital in 2019 / Q1 2020 will outperform – potential for super-apps to emerge • Valuation premium for automated supply chain and services
M&A and Partnerships	• Exits via public capital markets are very challenged; M&A appears the most viable option for monetisation and growth • Valuations are tempering for private and public fintechs • Substantially higher cost of capital. Each dollar of opex and capex now costs ~2-3x more vs. pre-Covid-19 period • Recent growth / consolidation through partnerships such as Alipay-Transferwise, Visa-Rapyd and Wirecard-Klarna	• Medium-sized fintechs will be more inclined to drive scale and cost synergies with consolidation via M&A or partnerships • Strategic acquisitions more prevalent; deal terms / pricing swinging in favour of acquirers. Strategics will be on the hunt for fintechs with differentiated products, network & customers; and tech adjacencies in digital content, education & health • VC / private equity will need to double down on fewer assets

Covid-19: Mixed Impact Expected Across Fintech Segments

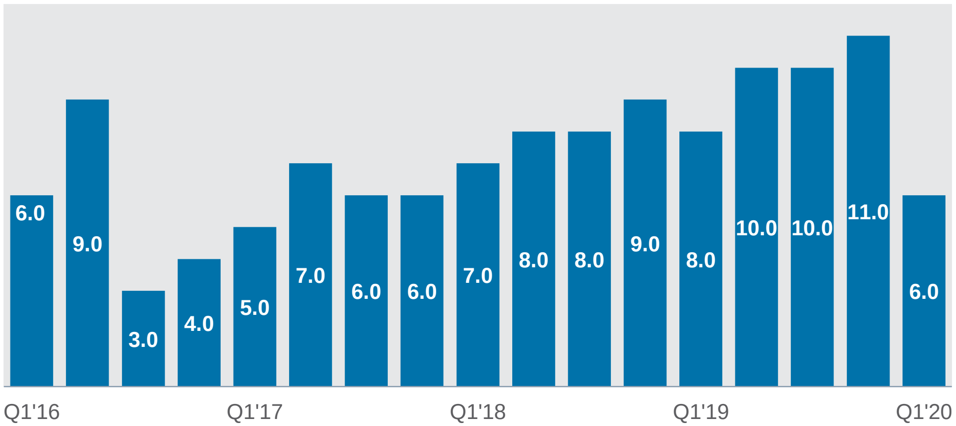
Standard Chartered

Segment	Sample Fintechs	Considerations
Payments Platforms	adyen, 支付宝 ALIPAY, stripe, WeChat Pay	✓ Increased volumes from select e-commerce, digital content and health-related payments ✓ Large-scale processors are likely to weather Covid-19 impact given capital reserves ✓ Physical distancing may increase volumes for e-wallets and peer-to-peer processors × Cross-border payments and FX transactions will fall due to less travel and overseas spending × In-store point-of-sale payment processing to suffer as secular trend towards digital is enhanced
Digital Banks	Revolut, monzo, nu bank, chime	✓ Increased demand with greater shift towards digital work / life and focus on remote user experience ✓ Recent late-stage VC funding rounds will allow the leading challenger banks to defend their position × Crisis may drive flight to incumbents seen as more stable, and new test on digital credit models × NIM compression, heavy reliance on transaction revenues (reduction in interchange and FX fees)
Lending Platforms	OakNorth, Kabbage, Funding Circle, TALA	✓ Increased demand in retail and SME loans (e.g., pay-day, supply chain finance) ✓ B2B lending software providers may prosper as incumbents banks must enhance credit efficiency ✓ Central bank stimulus measures may increase opportunity to underwrite otherwise riskier loans × Negatively impacted by higher funding costs, increasing pressure on revenues and margins × Increased probability of loan defaults and digital credit models facing test in unprecedented crisis
Digital Wealth Managers	nutmeg, EV ELLEVEST, FLAGSTONE THE SMARTER CASH PLATFORM	✓ Potential increase in demand for digital / remote advice and savings platforms as customers flee risk × Short-term market turmoil will otherwise reduce demand (lower fund flows) and margins (lower AUM) × Customers may seek "trusted" human advice offered by incumbents who can also compete on fees ? Significant test on automated strategies to deliver performance and manage risk in a downturn
Institutional Capital Markets Platforms	robinhood, SYMPHONY, eToro, Digital Reasoning	✓ Benefit from increased volatility, trading activity and remote ways of working in financial markets ✓ Regtech and compliance fintechs expected to outperform given new focus on cost savings and risk × Prolonged / excess volatility and market downturn can be detrimental and drive volumes down
Insurtechs	众安保险 ZhongAn Insurance, oscar, BIMA, wefox	✓ Potential boost from increased demand for health, life and business disruption insurance ✓ Other insurtech sectors – analytics, IoT, cybersecurity – are expected to see resilient growth × Lower disposable income, decrease in driving and limited travel adds pressure in select sub-sectors

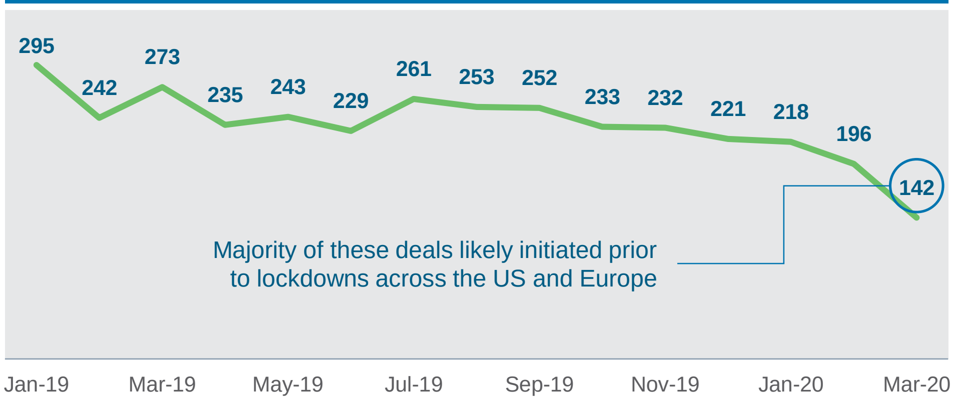
Emerging Fintech M&A and Investment Themes

- Fintech funding has fallen to levels last seen in 2017, with the number of deals in 2020 YTD halving relative to early 2019
- Opportunity for strategics to invest in or acquire fintechs at favourable terms; pressure on mid-stage fintechs to consolidate

Disclosed Fintech Funding (USDbn, Q1 2016 – Q1 2020)



Global Fintech Deals # (Jan 2019 – Mar 2020)



Source: CB Insights

Sub-scale fintechs facing funding shortfall and reduced revenue will seek growth and cost synergies via mergers or partnerships

Exits via M&A likely to be most viable path as IPO markets cool

Buy-side opportunities with valuation compression – likely increase in down rounds, side rounds and/or convertibles

Sub-sectors heated in the fin/tech bull market, such as digital retail banking and ridesharing, could become more accessible

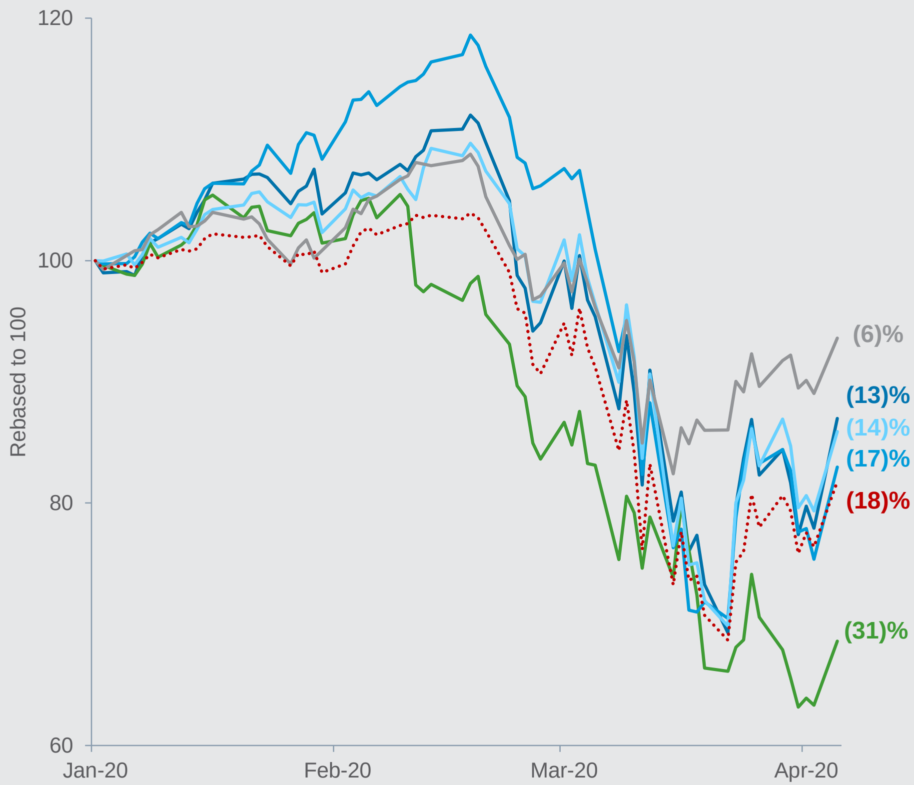
Expect strategic and opportunistic acquisitions by late-stage fintechs, incumbent banks, big-tech and e-commerce platforms

Frozen high-yield bond and leveraged loan markets could see private equity double-down on fewer assets and dispose others

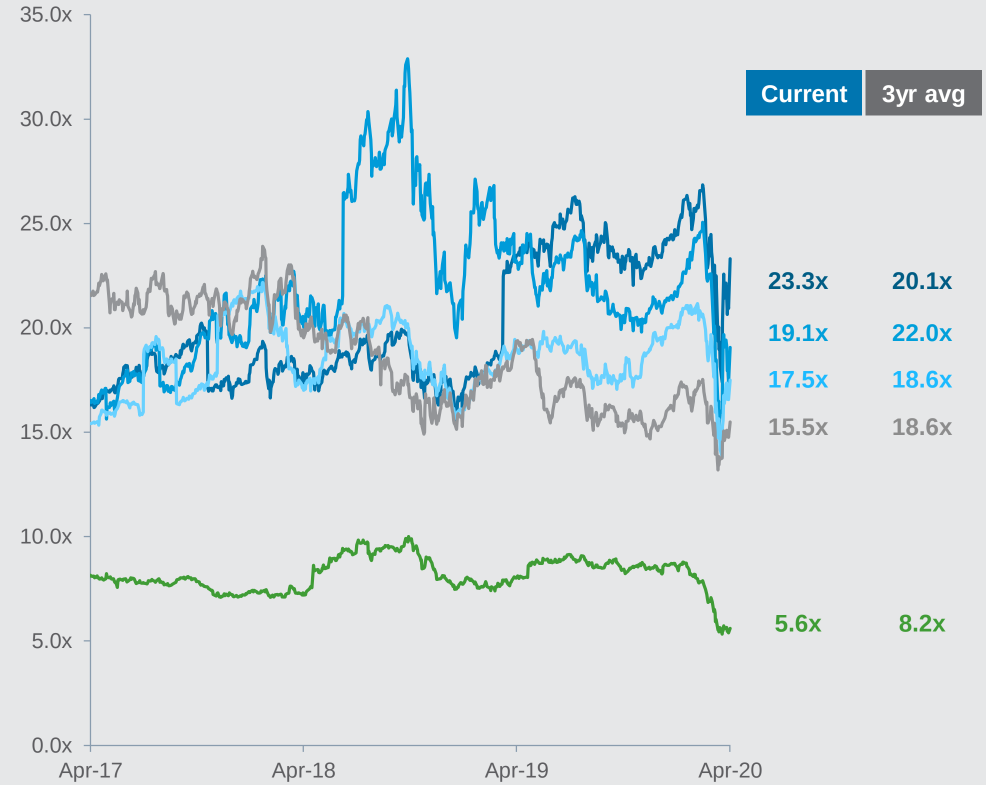
Fintech Public Market Performance

- Most listed fintechs have performed better than or in line with the broader market, given the enhanced shift to digital payments – particularly platforms that are embedded within the e-commerce ecosystem and those with product / geographic diversification
- Remittance, FX and ATM businesses have unsurprisingly been hardest hit, given the reduction in travel and physical contact

Share Price (YTD)



EV / NTM EBITDA (Last 3 yrs)



Key[(1)]: S&P 500 | Card Schemes | Payment Processors | Financial Software | Big Tech / E-commerce | Remittance / ATMS

Source: Capital IQ (6-Apr-20)

(1) **Card Schemes:** Visa, Mastercard, Amex, PayPal; **Payment Processors:** Global Payments, Square, FleetCor Technologies, Wirecard, Worldline, Nexi, Euronet Worldwide, WEX, EVERTEC, EVO Payments, Adyen, Ingenico, Network International; **Financial Software:** FIS, Fiserv, Paychex, Jack Henry & Associates, Temenos, Alfa Financial Software Holdings; **Big Tech / E-Commerce:** Amazon, Alphabet, Alibaba, Tencent, Facebook, JD.com, NetEase, Baidu, eBay; **Remittance / ATMs:** Western Union, Cardtronics, PayPoint, International Money Express, Diebold Nixdorf, OFX Group, MoneyGram International Equals Group

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