Stars align for fintech M&A as the bull run continues

Established financial institutions are engaging with fintech as never before and are now active participants in fintech M&A. Private equity and venture capital appetite for transactions remains strong. Fintech dealmaking is booming as a consequence, and there is every indication that this will continue for some time yet.

Our 2018 M&A forecast

Fintech

Fintech is the 'darling' of financial sector M&A and will enjoy the spotlight for some time to come as market participants embrace enablers in their quest for competitive advantage.

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Fintechs are offering consumers a richer and smoother experience and are removing friction and cost from market infrastructure. Believe the hype! But proceed with caution...

Guy Potel
Partner, London
Financial Institutions M&A Group

Technology is fundamentally changing the way we deal with money and capital.

Fintech has moved from “disruptor” to “enabler” for many financial institutions and continues to shape the future of the financial sector. Here’s how:

Strategics’ hunger for more fintech M&A

Strategic buyers have seen tangible examples of fintech success, such as Calastone’s purchase and sale of mutual funds using blockchain and Natixis making its first blockchain-powered fund distribution. Case studies like these mean other traditional institutions cannot afford to sit on the sidelines and wait to see how fintech develops. They have had to act and this has prompted a flurry of joint ventures and acquisitions, such as RBS’s partnership with blockchain-based mortgage reporting developer R3 CEV, Santander’s acquisition of transaction processor Elavon and BNP Paribas’s investment in robo-adviser Gambit Financial. Established banks, insurers and asset managers recognise that fintech can accelerate the re-architecture of back-end infrastructure with new efficient and cost-effective models.

293

Number of global fintech M&A deals in Q2 2017 alone

Source:
KPMG

PE and venture capital: Fintech high on the deal radar

Private equity and venture capital investors have continued to invest heavily in the fintech sector, attracted by growth prospects and the willingness of financial services companies to do deals, which increases exit options for sponsors. Payment processors Klarna and iZettle have both received financial sponsor backing this year, while Monzo, OakNorth Bank, Nubank, Neyber, Revolut, Tide, Yoyo, Zopa and Neos all reported successful funding rounds in H2 2017.

US$8.4 billion

Value of global fintech M&A deals in Q2 2017 alone

Source:
KPMG

Fintech’s transformation of financial services sector grows apace

EU finance ministers have emphasised the need to introduce fintech regulations to protect consumers, and the ECB has begun drawing up new licensing regulation for fintech businesses. While increasing regulatory scrutiny remains a concern, on the whole, local governments are supportive of the industry and are competing to attract fintech businesses to their shores. Fintech transformation of the financial services sector continues apace.

Fintech (continued)

2018 outlook

Fintech remains an M&A focus for financial sponsors and an investment omphalos for many established financial institutions. Global banks and insurers are increasingly looking to 'market infrastructure' fintech as a cure for internal cost management.

By contrast, 'customer-facing' fintech is having an increasingly disruptive impact on traditional retail banking models. Such solutions offer the intuitive end-user experiences which High Street lenders struggle to provide. But penetration of such solutions has not been consistent across all financial subsectors—for instance, penetration within the asset management industry has been more gradual.

Current market

Upward, significant

We are seeing

- Expansion of fintech business, through successful fundraisings as well as inorganic growth strategies
- High, and growing, financial sponsor appetite for fintech
- Steady upward trajectory of strategic M&A. Established financial institutions are engaging with fintech in a variety of ways:
  - JVs with existing fintech businesses
  - JVs with competitors to develop fintech
  - Acquiring the whole/strategic stakes in fintech businesses
  - Funding fintech start-ups in exchange for 'early bird' stakes
  - Establishing accelerator programmes to foster ground-up development
- Early signs of profit generation for established financial institutions from M&A

Key drivers

- Fintech is being embraced as an 'enabler' of financial service provision—perception that fintech could be the solution to:
  - Realising cost efficiencies across existing service provision models
  - Maximising existing customer bases, through enhanced data analytics and processing
  - Attracting new consumers, especially millennials, who respond well to just-in-time personalised services
  - Accessing new markets, including unbanked and under-banked communities in China, Africa, India and SE Asia
  - Rapidly growing cybersecurity threats
- Top-down support for fintech businesses, including from national governments across Europe and local EU regulators. However, growing scepticism from supranational regulators could impact M&A levels
- Progressive regulatory and supervisory approach. Both UK prudential regulators are acutely aware of their national imperatives of ensuring the UK financial services market remains 'open for business' as Brexit looms—but they face stiff competition from other regulators across the bloc
- Regulatory intervention (e.g., the European Commission, through PSD2, and the UK Capital Markets Authority, through its February 2017 final banking order, are encouraging 'open banking')

Trends to watch

- Fintech continuing to disrupt traditional retail banking models—how will the High Street banks react?
- Tangible fintech successes boosting M&A activity. We are seeing the first signs of blockchain technology deployment across fund distribution, cross-border FX transfers and securities settlement
- Profit generation for established financial institutions from M&A activity
- Financial sponsors seeking to realise investments through IPOs, disposals and other exit strategies
- Will the UK be toppled as the epicentre of fintech development post-Brexit?
- Regulatory intervention in certain fintech subsectors (e.g., P2P, coin offerings and bitcoin CFD trading)

Fintech – Key deals and situations

Scaling up of fintech businesses	☐ Successful fundraisings: – Monzo, OakNorth, Nubank, Neyber, Revolut, Tide, Yoyo, Zopa and Neos all reported successful funding rounds in H2 2017 (*June – November 2017*) ☐ Deployment of inorganic growth strategies: – Deposit Solutions' acquisition of Savedo (*August 2017*) – Payconiq's acquisition of Digicash Payments (*August 2017*) – My Buck's acquisition of 50% of New Finance Bank (*July 2017*)
Fintech – an "enabler" of financial services	☐ JVs with existing fintech businesses: – Blockchain-based mortgage reporting JV between, amongst others, RBS and R3 CEV (*September 2017*) – E-commerce JVs between CaixaBank and Alibaba (*August 2017*) and Yandex and Sberbank (*August 2017*) ☐ JVs with competitors to develop new technologies: – Commerzbank's, Bank of Montreal's, CaixaBank's, Erste's, UBS's and IBM's joint development of a blockchain-based trade finance platform (*October 2017*) – Barclays', Credit Suisse's, UBS's and HSBC's joint development of a new digital currency (*August 2017*) ☐ Acquisitions of fintech businesses: – Santander's acquisition of Elavon (*July 2017*) – Arkea's acquisition of Pumpkin (*July 2017*) ☐ Acquisitions of strategic interests in fintech businesses: – BNP Paribas's acquisition of a majority stake in Gambit Financial (*September 2017*) – Julius Bar's acquisition of a minority stake in Nectar Financial (*July 2017*) ☐ Funding fintech start-ups in exchange for 'early bird' stakes: – Intesa Sanpaolo's 'Neva Finventures': established in 2016 – Aviva's 'Aviva Ventures': established in 2015 ☐ Establishing accelerators: – RBS's partnership with Entrepreneurial Spark to create the Business Accelerator Hub (*August 2017*) – UBS's partnership with Credit Suisse to create the KickStart Accelerator programme (*March 2016*)
Fintech – a 'disruptor' of financial services	☐ Revolut applied for a European banking licence *(November 2017)*, commenced offering insurance products (*September 2017*), mortgage services (*April 2017*) and consumer loans (*March 2017*) ☐ Klarna's successful Swedish banking licence application (*June 2017*) ☐ Adyen's successful pan-European banking licence application (*June 2017*)
Tangible fintech success whetting appetites	☐ Calastone's successful buying and selling of mutual funds using blockchain technology (*July 2017*) ☐ Natixis's first blockchain transaction completed in fund distribution (*July 2017*) ☐ Banco Bilbao Vizcaya Argentaria's use of blockchain to effect cross-border money transfers (*April 2017*) ☐ Deutsche Bundesbank and Deutsche Börse commenced testing of a functional prototype for blockchain-based securities settlement (*January 2017*)
Profit generation for established banks	☐ Credit Suisse's disposal of Next Investors (*August 2017*) ☐ Goldman Sachs's proposed disposal of Simon (*July 2017*)
Top-down support for fintech. But dark clouds may be gathering…	☐ Government support: – Spain's research, development and innovation tax credits for fintech businesses (*May 2017*) – Sweden's National Innovation Counsel established to support fintech (*May 2017*) ☐ Regulator support: – European Commission raided banking associations in Poland and the Netherlands as part of a crackdown on lenders which block fintech from legitimate access to customer data (*October 2017*) – European Commission's resolution to support expansion of fintech (*May 2017*) ☐ Direct regulator involvement: – UK FCA's continued support of fintech start-ups (e.g., AssetVault, Experian and Sabstone) through its 'regulatory sandbox' (*June 2017*) – Bank of England's launch of its Fintech Forum (*March 2017*) ☐ Regulatory scepticism: – EU finance ministers have emphasised the need to introduce regulation to protect consumers (*September 2017*) – ECB commenced drawing up of new licensing regulation for fintech businesses (*September 2017*)
Financial sponsor interest in fintech	☐ Bain's investments in Acorn, Digital Currency Group, iPay Technologies and Receivables Exchange and TxVia (*2014 – 2017*) ☐ Rocket Internet's and Finstar Financial's investment in Spotcap (*October 2017*) ☐ Zouk Capital's investment in iZettle (*September 2017*) ☐ Permira's acquisition of 10% in Klarna (*July 2017*) ☐ BlackRock's investment in Scalable Capital (*June 2017*) ☐ Northzone's investment in Zopa (*June 2017*) ☐ Pollen Street/BC Partners' acquisition of Shawbrook (*June 2017*) ☐ Passion Capital's investment in Tide (*June 2017*)