

FinTech Breakfast

Regulatory and funding update

08 September 2022

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Welcome

Chris Woolard CBE and Tom Bull



Introductions



Chris Woolard CBE

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Regulatory update

Alex Roy



Regulatory drivers:

Cost of living



- ▶ Impact on customers
- ▶ Firm resilience

Digital transformation



- ▶ Crypto/blockchain/DeFi
- ▶ CBDC
- ▶ Open Finance

Global environment



- ▶ Rising fraud and fin crime
- ▶ Post-Brexit realignment
- ▶ Need for long-term capital

Regulatory reform



- ▶ Outcomes focused
- ▶ Data led
- ▶ Accountable

Regulatory plans: is it all business as usual?

FCA



Reducing and preventing serious harm

- ▶ Appointed Representatives
- ▶ Fraud and financial crime
- ▶ Improving redress framework
- ▶ Assertive action on market abuse
- ▶ Strengthening gateway provisions

PRA



Resilience

- ▶ Financial resilience of banks
- ▶ Operational risk and resilience
- ▶ Governance and risk management



Setting and testing high standards

- ▶ New Consumer Duty
- ▶ Environmental, Social and Governance (ESG)
- ▶ Operational Resilience



New and emerging risks

- ▶ Financial risks from climate change
- ▶ LIBOR transition
- ▶ Digitalisation
- ▶ AI



Promoting competition and positive change

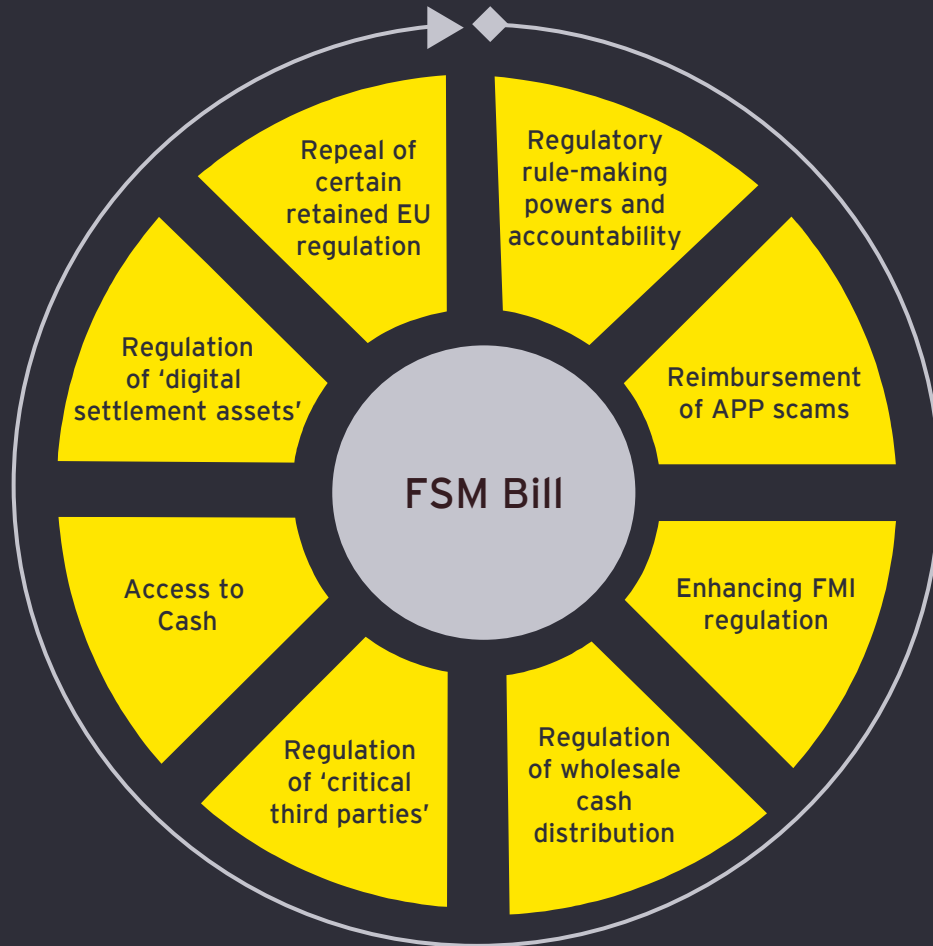
- ▶ Future Regulatory Framework
- ▶ New Stablecoin Regime



Competitive and dynamic markets

- ▶ Future Regulatory Framework Review
- ▶ Simpler prudential rules
- ▶ Firms exiting from the market

The Financial services and markets bill 2022/23



But, the Bill is only the start of the journey and more details/ consultations are to come ...

EU regulatory development: now and next

BNPL



- ▶ UK to bring into scope of STIFC regulation
- ▶ EU to revise CCD to bring into scope
- ▶ Affordability assessments and APR caps (EU) proposed
- ▶ Consultation on draft legislation in 2022 with secondary legislation laid by mid-2023 (UK)
- ▶ Exemptions for specific agreements where risk of customer detriment is low

DORA



- ▶ EU level comprehensive ICT risk management requirements specific to financial services sector
- ▶ Will require assessment of legacy systems and arrangements with third-party providers
- ▶ FCA, BoE and PRA also working on similar operational resilience framework
- ▶ To align with already existing NIS2 but DORA to have precedence

MiCA



- ▶ Expansion of EU regulatory perimeter for crypto-assets not currently covered by existing FS laws
- ▶ Linked to the EU's agreed crypto-assets related amendments to the Transfer of Funds Regulation (TFR)
- ▶ DeFi, crypto lending and most NFTs left out of scope of MiCA
- ▶ Political agreement reached on June 30th

PSD2 Review



- ▶ European Commission keen to assess application and impact of PSD2
- ▶ Currently in a fact finding phase as Commission is consulting with market participants
- ▶ EBA's recent 200 proposals should be considered by firms
- ▶ Linked to Commission's larger plan to devise an Open Finance Framework to create new and improved services beyond PSD2

AML/CTF



- ▶ Current package is largest overhaul of the EU's AML/CTF legal and supervisory framework
- ▶ Consists of fully harmonised AML single rule book, the creation of a new supervisor at EU level, amendments to TFR and amendments to flagship law (6AMLD). TFR to be finalised first
- ▶ Impact on firms' operations will be significant and therefore require adaptation

EU regulatory development: beyond

Open Finance/DeFi



- ▶ More than just Open Banking and is an important element of the EU's Digital Finance strategy that includes DORA, MiCA, PSD2, ESAP, etc.
- ▶ Refers mainly to third-party service providers access to customer data held by FS intermediaries
- ▶ Has now been delayed by the Commission to 2024

Instant Payments



- ▶ Commission to propose legislation in H2 of 2022
- ▶ Key aims would be to make the EU a global leader in payments, levelling the playing field, accelerating adoption of already existing solutions and improving consumer protection
- ▶ To focus on payments within SEPA

CBDC's



- ▶ Commission plans legislation in early 2023 as foundation for ECB development of digital Euro
- ▶ UK plan to be a crypto-asset technology hub
- ▶ Other jurisdictions are already live testing, developing, or considering the development of CBDC's
- ▶ Risk of disintermediation

AI Act



- ▶ Risk-based approach to AI regulation
- ▶ Act introduces detailed and comprehensive governance framework requirements
- ▶ In the Act, FS sector represents gray area of list of sensitive sectors. Clarifications throughout the legislative process will be needed
- ▶ Just like GDPR, the AI Act could become the benchmark for AI regulations

AML/CTF



- ▶ Due to a lengthy EU legislative process and political considerations, completion of the new EU AML single rulebook (AMLR) and establishment of new EU supervisor to take time
- ▶ The UK has now also started a comprehensive review of its AML/CFT regulatory and supervisory regime (UK)

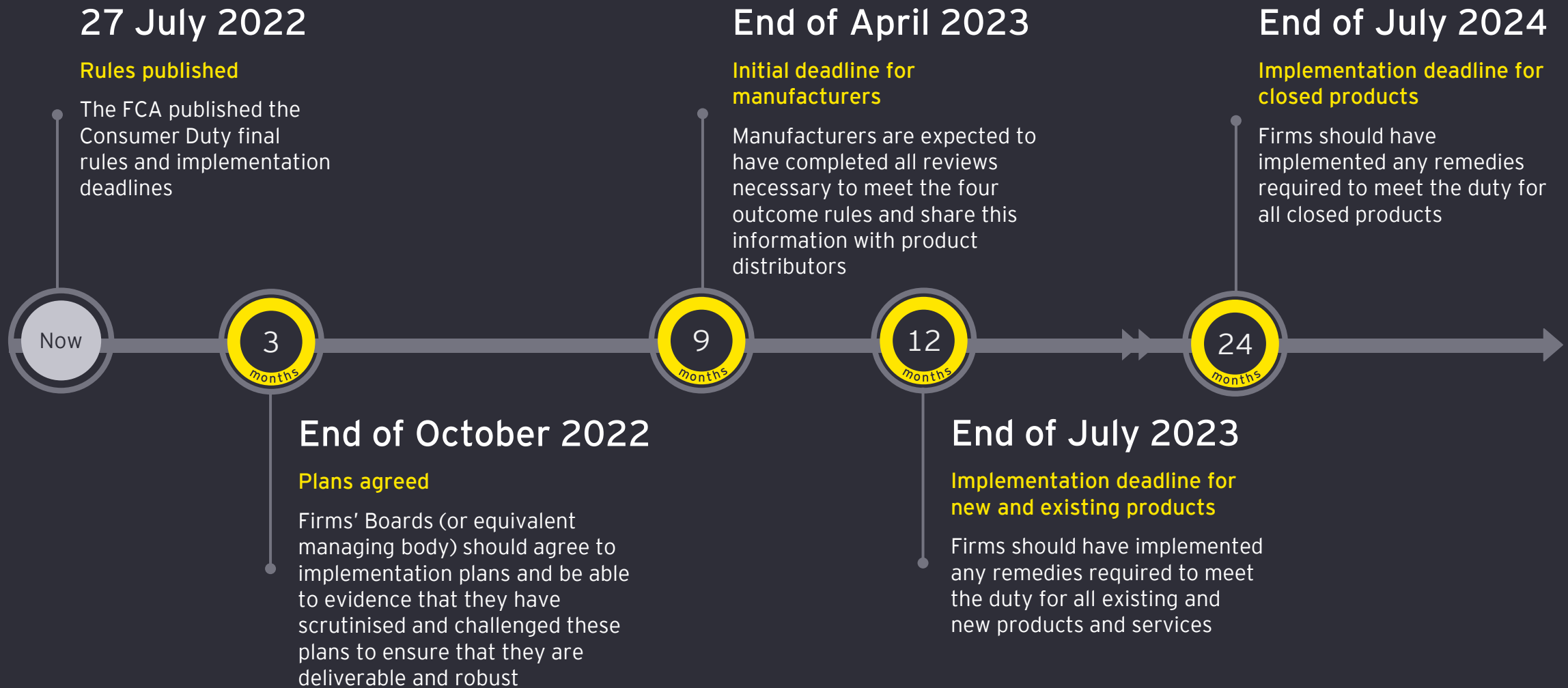
Consumer duty requirements – What would 'great' look like and what are the differences?



- ▶ We have outlined key components which we believe should be viewed as **'building blocks' to help shape thinking** and Consumer Duty approach
- ▶ Firms will need to make **key strategic decisions** across each of these, early, to ensure a clear plan for implementation by October '22



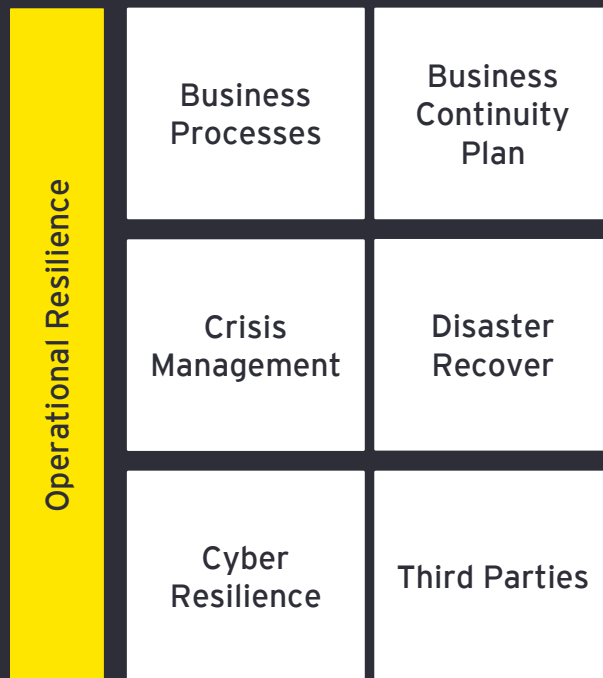
Consumer duty: The timeline



Regulatory focus on Operational Resilience

Operational Resilience brings together business processes, the Business Continuity Plan, Crisis Management, Disaster Recovery, Cyber Resilience and Third Parties.

Resilience-related risks are varied, dynamic, inter-related and cut across various operational risk dimensions (e.g., people, process, technology, data, third parties)



- ▶ Board level governance and senior management accountability for operational resilience
- ▶ Focus on recovery/restoration of end-to-end critical business services (e.g., people, process, technology, Third parties, data)
- ▶ Prioritising market and customer impact of service disruption in assessing criticality of business services
- ▶ Extend resilience focus beyond prevention to assume disruptions will occur and firms need to be prepared to enact contingency plans to continue and/or quickly resume the delivery of critical business services
- ▶ Greater emphasis on an integrated testing framework (inclusive of cyber, crisis management and incident response); more rigour and complexity of testing
- ▶ More emphasis on understanding third-party concentrations and coordination of resilience plans and testing

Operational Resilience – what next ... ?

There are a number of further initiatives planned or recently published.



Cyber stress testing (planned 2022):

Expected to lead to enhancements in response and recovery capabilities.



New Critical third-party Regime:

Legislation coming followed by PRA/FCA consultation. Once rules are in place firms may start to be designated.



Operational resilience and operational continuity in resolution (PS2/22 and CP21/21)

Amendments to PRA rules to ensure group level assessment.



Regulation on digital operational resilience for the financial sector (DORA Regulation):

Upgrading ICT risk requirements across EU financial sector and establishing a streamlined digital operational resilience framework. Establishing an oversight framework for critical ICT third-party service providers.

Development of cryptoassets regulation

1

Stablecoin

- ▶ Legislation to allow the regulation of fiat-backed stablecoin is being introduced through the Financial Services and Markets Bill.
- ▶ Once introduced expect FCA/PRA consultations on the regulatory regime in 2023.

2

Other payment crypto

- ▶ Initial regulatory focus is on fiat-backed stablecoin. HMT expect to consult later in the year on the wider crypto regime.

3

Central Bank Digital Currency

- ▶ Like many other Central Banks, the Bank of England is exploring options for a UK CBDC. Work is at an early stage and we shouldn't expect a CBDC to emerge in 2023.

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Investment crypto

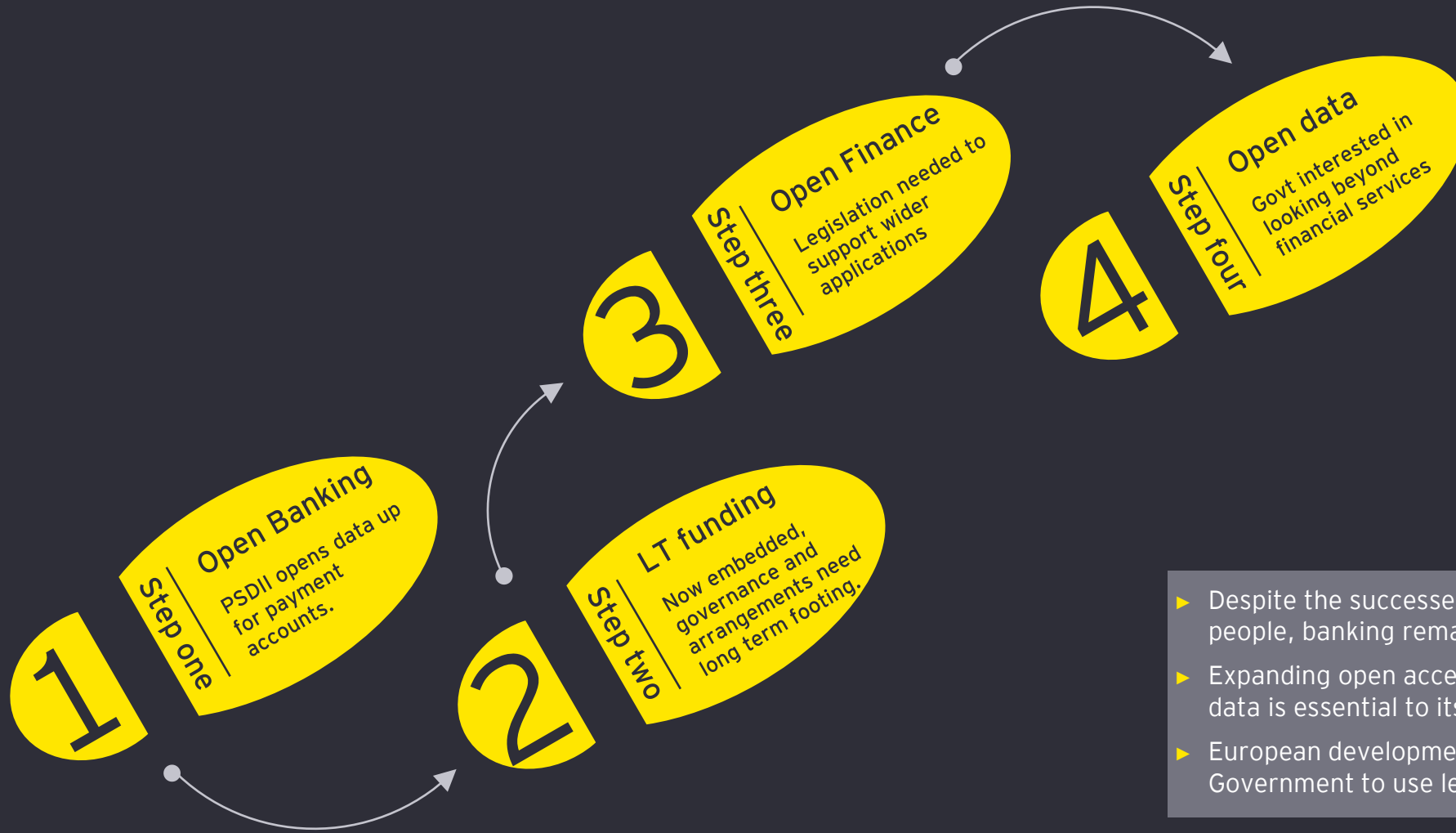
- ▶ Developing a regulatory regime for wider cryptoassets, such as BitCoin will start to be considered in the HMT consultation later in the year.

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Decentralised Finance

- ▶ HMT have said that they will also consider DeFi in their consultation later in the year. We should expect the paper to be fairly light on details.

Maximising the benefits from open banking ...



- ▶ Despite the successes of Open Banking, for most people, banking remains unchanged
- ▶ Expanding open access to a wider pool of financial data is essential to its long term success
- ▶ European developments may put pressure on the UK Government to use legislation to extend its reach

3

Q&A

Tom Bull



4

Funding update

Axe Ali



2021 was an outlier year for FinTech, with a total funding of \$139bn – more than 2x the levels of 2019 or 2020

Muted funding environment

- ▶ H1 2022 funding was \$50.7bn, a fall of 33% q-o-q and 46% y-o-y to \$20.4bn
- ▶ The number of deals fell 17% q-o-q to 1,225 in Q2 2022
- ▶ Mega rounds have declined (mostly)

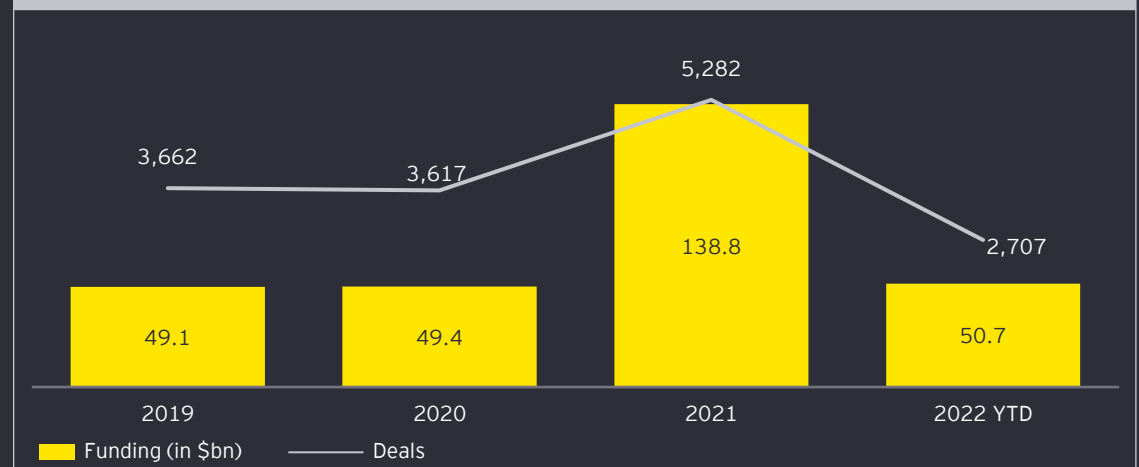
On a positive note

- ▶ At H1 2022, funding for FinTech had exceeded the total of FY20
- ▶ A significant level of dry powder is available for investment, due to the continuous stacking of funds over the years
- ▶ Investors remain active – however the approach to underwriting investments has evolved

Global quarterly funding and deals



Global funding and deals

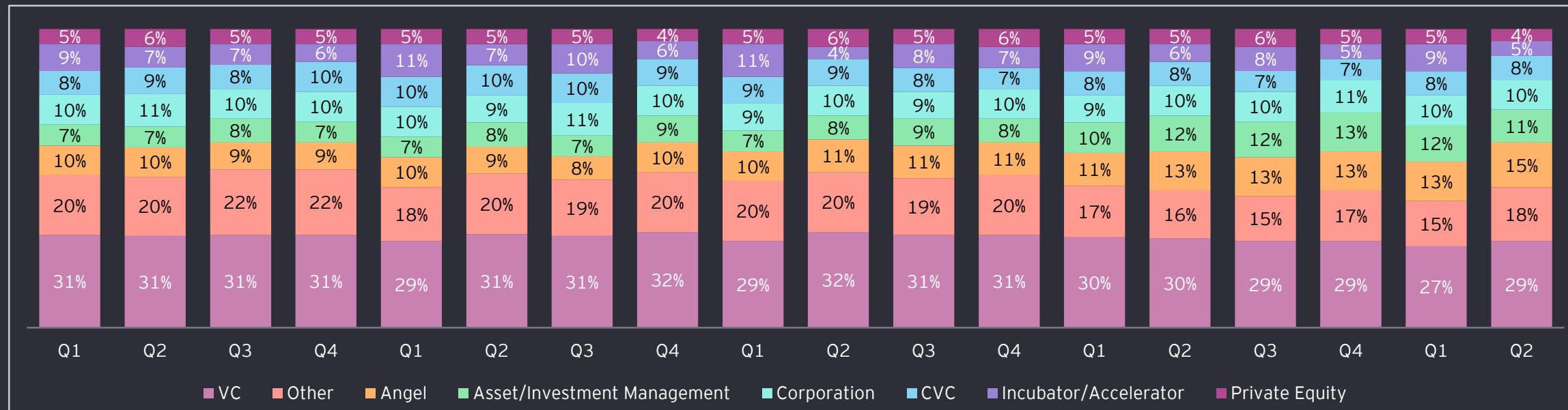


Whilst traditional venture capital remains the largest source of funding (29% in Q2 2022), the investor landscape is evolving

- ▶ Angel investing hits a new high at 15%
- ▶ Increasing trend as FinTech founders and operators have transitioned to becoming investors
- ▶ Creation of specialist funds

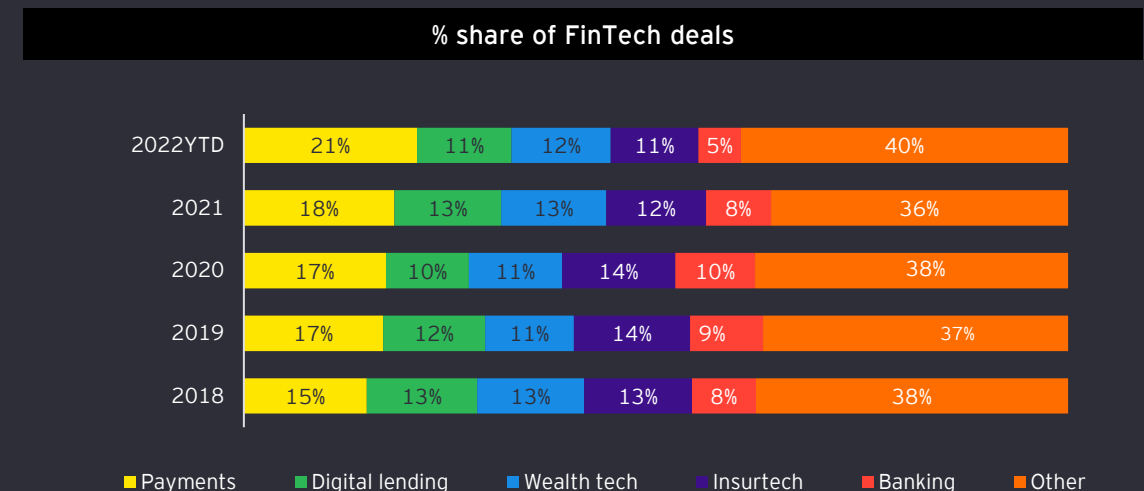
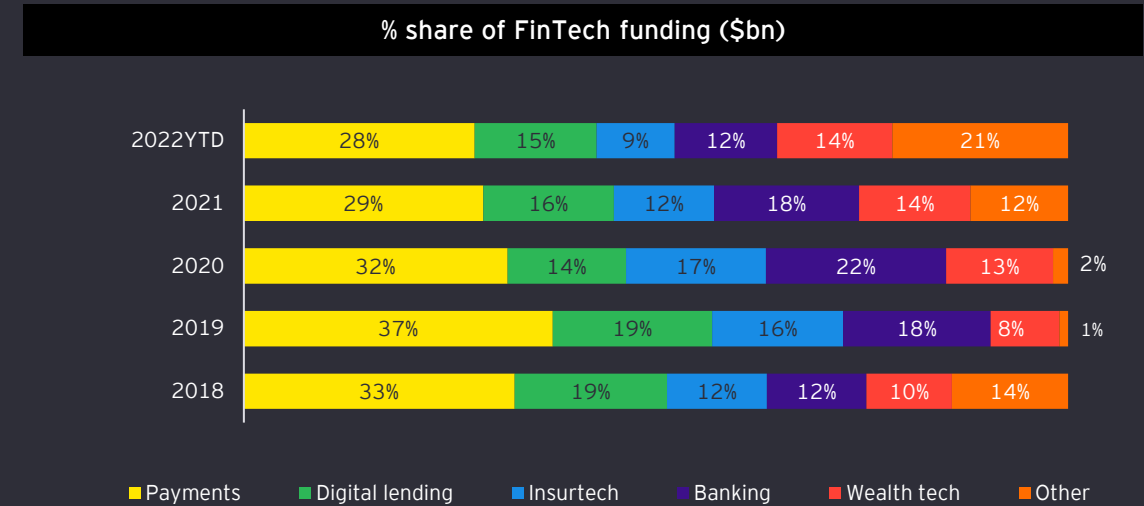
- ▶ Private Equity remains relatively low at 4%
- ▶ Increasingly setting up growth funds alongside traditional buy-out and also taking minority stakes
- ▶ M&A opportunities in current environment

- ▶ CVC deals has increased by 500% from 2014
- ▶ Large corporations and Financial Institutions active in FinTech investments to enhance their capability and propositions



At a global level – payment related FinTech’s receive the largest share of funding, however other FinTech sectors are gaining traction with strong investor appetite

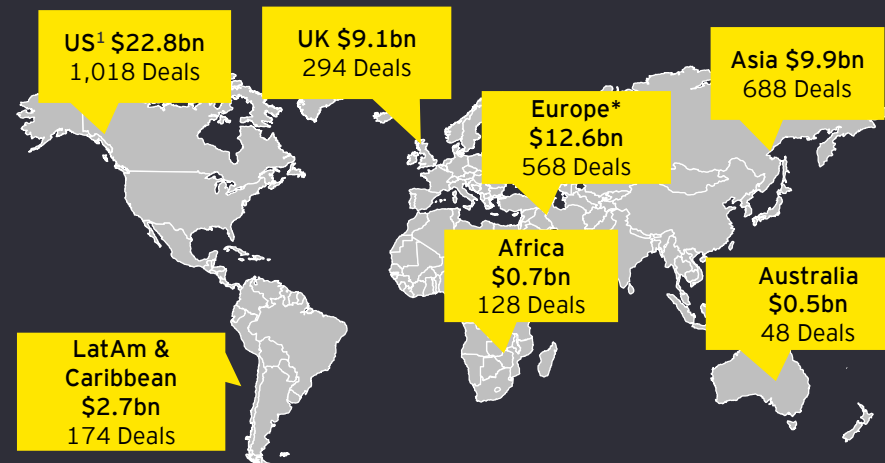
- ▶ Payments has the largest share of funding (28% H1 2022), and continued interest in adjacencies including buy-now-pay-later, embedded banking, and open banking aligned solutions has helped keep the payments niche robust
- ▶ Payments % share of FinTech funding has been decreasing since FY 2022, as innovation through out Financial Services subsectors becomes more prevalent
- ▶ *Evolving FinTech niche funding trends*
 - ▶ Digital lending funding up by 3x to \$22bn
 - ▶ InsurTech funding up by 2x to \$17bn
 - ▶ WealthTech funding up by 3x to 19bn
 - ▶ Capital Markets funding up by 5x to \$6bn



In Europe, the UK continues to receive the largest allocation of FinTech funding – more than the rest of Europe combined

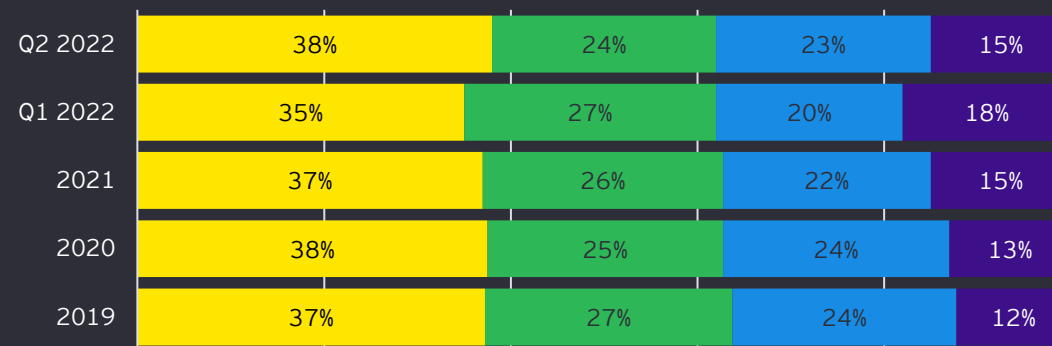
- ▶ FinTech funding in the UK totalled \$14.3bn across 662 deals in 2021, representing an increase of roughly 250% and 12% respectively from the prior year
- ▶ As at H1 2022, the UK had undertaken 294 FinTech deals at \$9.1bn. While fewer UK deals have been reported in H1 2022 (294) compared to H1 of 2021 (375) the \$9.1bn is 24% higher than H1 2020 (\$7.3bn)
- ▶ At a global level, the US received 38%, Asia 24%, Europe 23% and the remaining 15% allocated to all other regions

Global deals and funding (H1 2022)






Note: *Europe includes UK data

Funding % by region (2019 - Q2 2022)



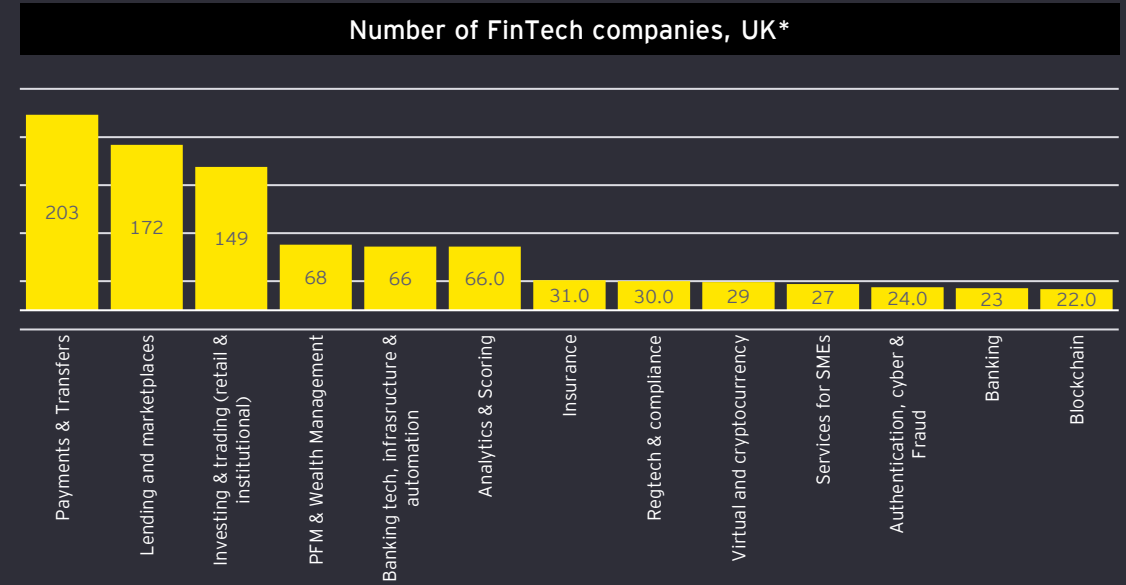
■ US ■ Asia ■ Europe ■ Others

Top 5 equity deals in Q2 2022 included two from the UK

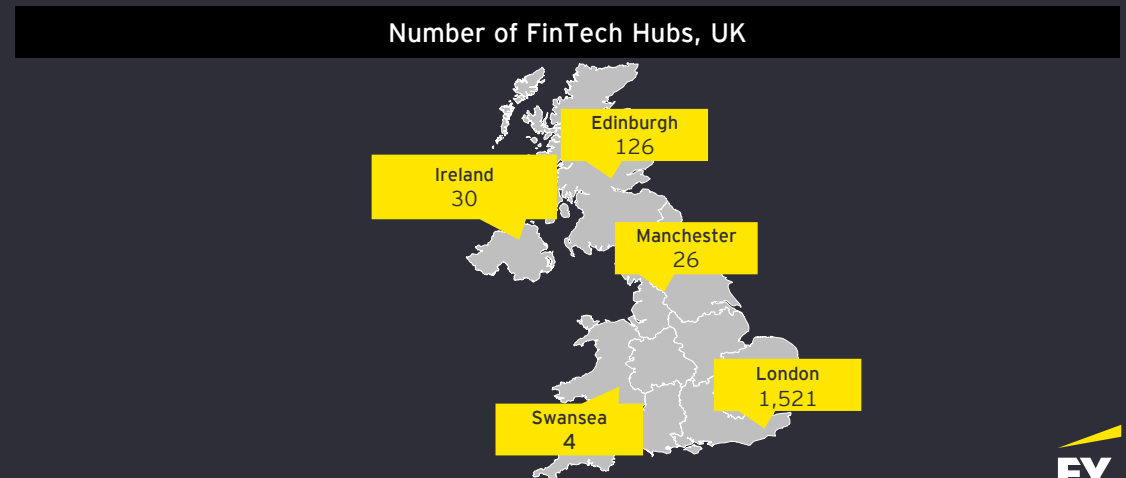
Company	Round amount (\$ m)	Round and date	Round valuation (\$ bn)	Select investors	Country	% of total funding
 CODA PAYMENTS	\$690m	Series C 15-04-2022	\$2.5b	Insight Partners, Apis Partners, GIC, Smash Ventures		3.4
 Velocity Global™	\$400m	Series B 19-05-2022	n/a	Eldridge, Norwest Venture Partners		2.0
 CIRCLE	\$400m	Venture Capital 12-04-2022	n/a	Fidelity Investments, Marshall Wace Asset Management, BlackRock, Fin Capital		2.0
 blo.bm™	\$378m	Series A 26-05-2022	n/a	Credo Capital Management, Fortress Investment Group		1.9
 sumup®	\$312m	Series E 26-03-2022	\$8.5b	Bain Capital Tech Opportunities, Crestline Investors, btov Partners, BlackRock		1.5

The level of innovation and variation of FinTechs within the UK is a key driver for investors

- ▶ The UK ranks second on the Global FinTech index after the US
- ▶ Fintech adoption rate is 71% - above global average of 64%
- ▶ Mature FinTech ecosystem, including evolving regional hubs. Investment outside of London increased by 467% compared to inside the city of London (323%)
- ▶ Supportive regulatory environment - FCA sandbox, Kalifa Review recommendations including CFIT (Centre for Finance Innovation & Technology)
- ▶ The UK's annual FinTech revenue is approximately £7bn (c.\$9.6bn), with the sector growing by almost 70% since 2015



Note: *Global FinTech Index - covers c.1,700 FinTech companies in the UK, provides classification for over 900 FinTech's



Key trends shaping investment into the future of FinTech in the UK include Embedded Finance, ESG, RegTech, and Crypto



Embedded Finance:

- ▶ Continued growth within non-financial firms to provide financial solutions to add-value to customer base



ESG:

- ▶ Impact start-ups recorded £2bn of investment in 2021, as more investors were inclined to balance their portfolio with positive impact as well as positive returns



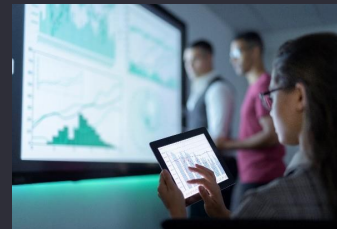
RegTech:

- ▶ The use of technology to streamline the regulatory process in financial services continues to grow and evolve at a rapid pace in the UK



Crypto:

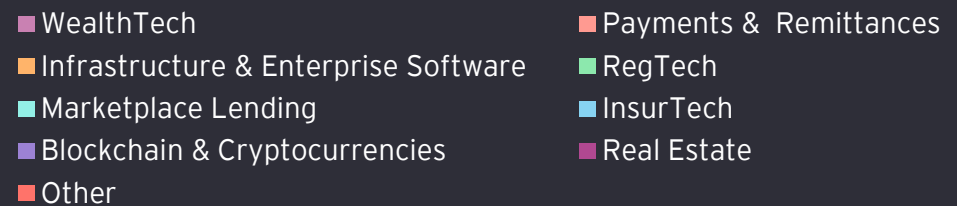
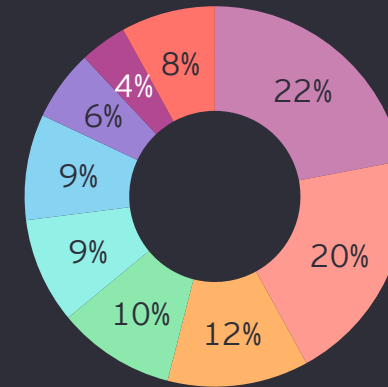
- ▶ Formation of crypto and digital assets group, and introduction of a financial market infrastructure sandbox



WealthTech:

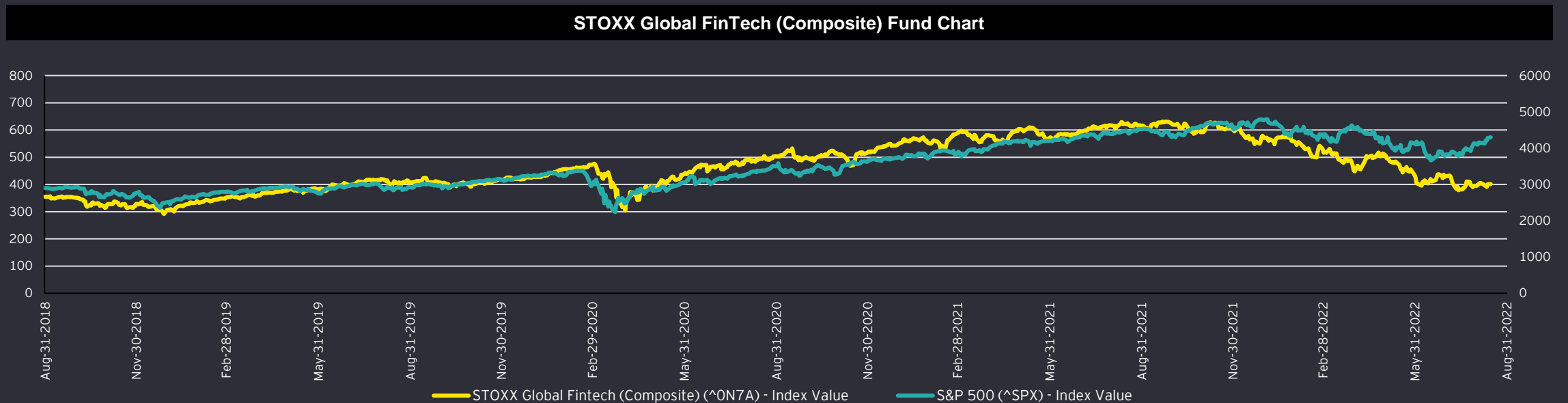
- ▶ Digital solutions being developed for different customer cohorts from retail, mass affluent to high net worth to provide differentiated propositions

UK FinTech funding by sector, Q1-Q3 (2021)



YTD to H1 2022 shows that investor confidence in technology and FinTech has been impacted

- ▶ The share prices for listed FinTech companies had dropped by 50% - almost 2x compared to other markets
- ▶ \$460bn was lost by the listed FinTech companies from their all time high
- ▶ The S&P index fell 18% during the same period



Investor sentiment and founder actions

Investor sentiment

- ▶ The macro environment of rising interest rates, high inflation, and broader economic concerns has resulted in investors becoming more rigorous in their investment approach, considering tighter capital availability
- ▶ Deals will continue to be done
 - ▶ Significant level of dry powder through stacking of funds
 - ▶ Lower valuations providing the ability for investors to enter the market at lower multiples
- ▶ Expect greater consolidation as larger incumbents see the opportunity to gain greater market share and capability through acquiring assets



Founder considerations

- ▶ Are you correctly managing expenses and the cash burn rate?
- ▶ Are you still clear on the value proposition of the product offering?
- ▶ Is your product offering right for the current market and future market?
- ▶ How resilient is your business model?
- ▶ How realistic is the business plan and what is the path to break even and profitably?
- ▶ Do you have the right strategy, channels, and partnerships in place to grow revenue?
- ▶ Do you have the right set of advisors and individuals in place to support from a strategy and execution perspective?

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Q&A

Tom Bull



Thank You



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