FINTECH VALUATION

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assoFintech

Abstract

Financial technology (FinTech) is an industry composed of diversified companies that use technology to make financial services more efficient.
Fintech is recognized as one of the most critical innovations in the financial industry and is evolving at a rapid speed, driven in part by the sharing economy, favorable regulation, and information technology. Fintech promises to disrupt and reshape the financial industry by cutting costs, improving the quality of financial services, and creating a more diverse and stable financial landscape.

With the advances in e-finance and mobile technologies for financial firms, fintech innovation emerged after the worldwide financial crisis in 2008 by combining the e-finance, internet technologies, social networking services, social media, artificial intelligence, and big data analytics.
The valuation of FinTech companies concerns promising startups and some seasoned firms.
FinTechs have a hybrid business model, as they operate in the financial (banking) sector deploying their technological attitudes.

Evaluators may so wonder if FinTechs follow the typical evaluation patterns of bank/financial intermediaries or those of technological firms.
Preliminary empirical evidence shows that the latter interpretation is the one consistent with the stock-market mood, and the business model of FinTechs.
Evaluation patterns typically follow Discounted Cash Flows (DCF) or other metrics based on market comparables.

The **main areas of activity** are :

• Financial technologies applied to blockchains and distributed ledger technology based on data archives, whose records are public on a computer network and without the need for a central register;
• Crypto and digital money;
• Peer-to-peer loans (P2P);
• Smart contracts (using the blockchain) that automatically execute contracts between buyers and sellers;
• Open banking supported by the blockchain applications that create a service through a connected network of financial institutions and third-party providers.
• IT security, through or decentralized storage of data, and anti-fraud systems;
• Applications in the insurance field (InsurTech) or regulation (RegTech); Asset management (robo-advice, social trading, wealth management, personal financial management apps, or software).

Main areas of activity

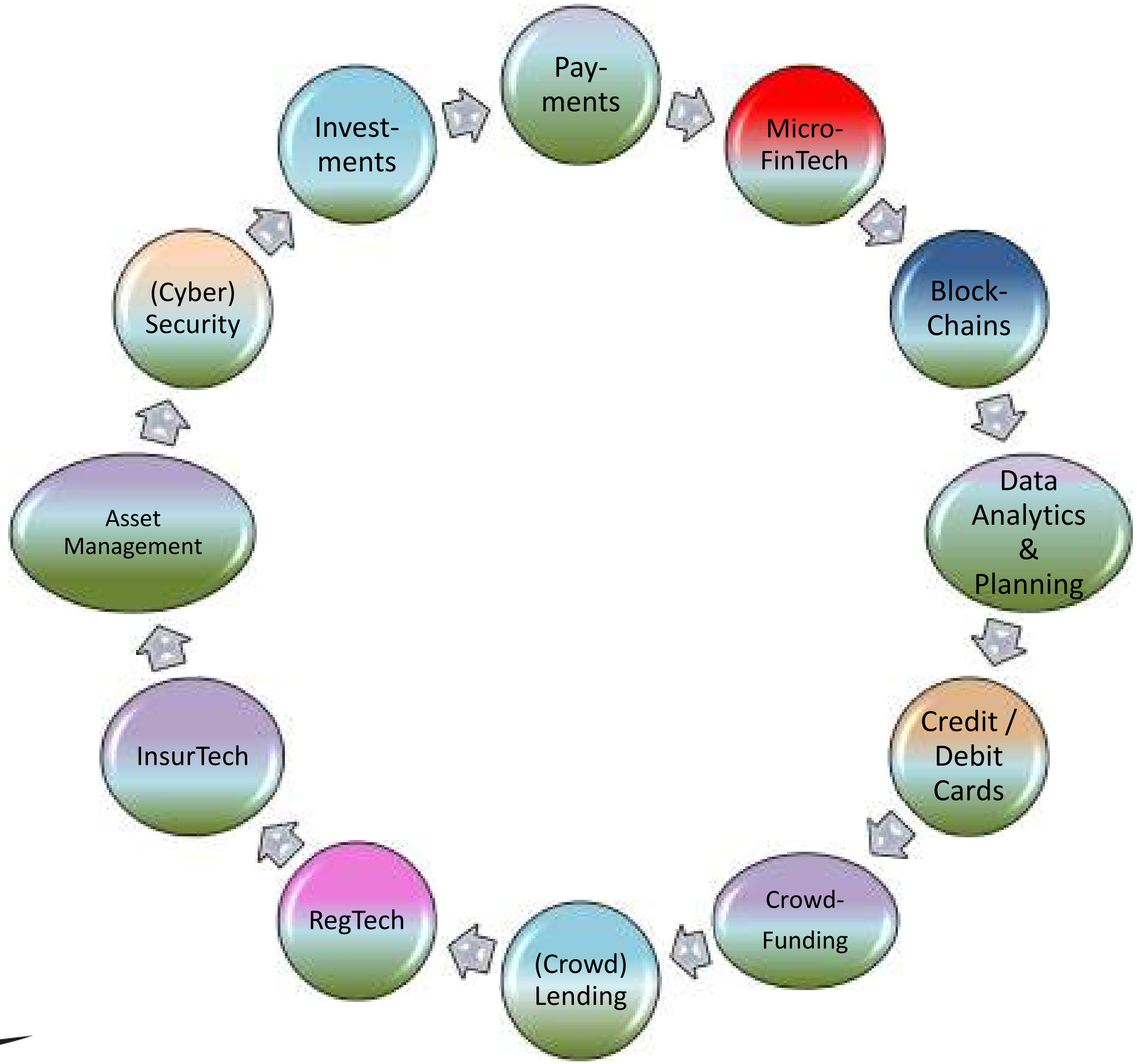


Figure 3. – *Digital platforms*

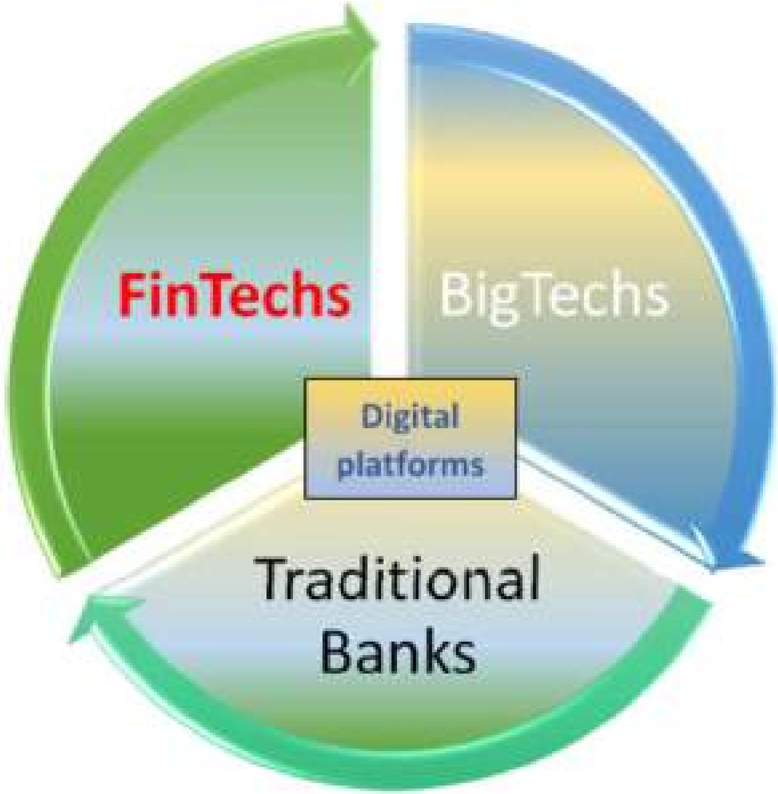


Table 1 – *FinTech typologies and business models*

Typology	Business Model
Financing solutions	Pure equity crowdfunding (retail); club deals; funding from institutional investors.
Blockchain	The blockchain is a decentralized and distributed digital ledger that corresponds to an open database with a pattern of sharable and unmodifiable data that are sequenced in chronological order. The main applications are cryptocurrencies; banking and payments; cyber-security; supply chain management; forecasting; networking & IoT; insurance; private transport & ride-sharing; cloud storage; charity; voting; healthcare; crowdfunding.
Payment systems and processing (PayTech)	Credit cards; mobile payments through apps; virtual POS; online wallet; money transfers. Payment innovations throughout the year have been largely all about mobile e-wallets and contactless payments. PayTech firms also focused on ensuring the security of transactions leveraging artificial intelligence (AI) and machine learning (ML) technologies. Global consumers have grown less reliant on cash, enhancing the growth profile of mobile payments firms.
P2P loans	Peer-to-peer (P2P) lending is the practice of lending money to individuals or businesses through online services that match lenders with borrowers. Peer-to-peer lending companies often offer their services online and attempt to operate with lower overhead and provide their services more cheaply than traditional financial institutions.
Open Banking	In October 2015, the European Parliament adopted a revised Payment Services Directive, known as PSD2. The new rules included aims to promote the development of neobanks or challenger banks use of innovative online and mobile payments through open banking.
Big Data & Analytics	Big data analytics is the often complex process of examining large and varied data sets, or big data, to uncover information - such as hidden patterns, unknown correlations, market trends and customer preferences - that can help organizations make informed business decisions.
Insurtech	Insurtech refers to the use of technology innovations designed to squeeze out savings and efficiency from the current insurance industry model.
RegTech	Regulatory technology, in short, RegTech, is a new technology that uses information technology to enhance regulatory processes. With its main application in the Financial sector, it is expanding into any regulated business with a particular appeal for the Consumer Goods Industry. Regtech, post-financial crisis—with MiFiD II, Basel III and GDPR—may have been the initial external driver to ensure full compliance, and this has ensured a dramatic rise in technological solutions, and crucial in increasing efficiency, for example, by reducing gap-analysis time.
MicroFinTech	FinTech applications to microfinance activities (microcredit; microdeposits; microinsurance; micro-consulting). M-banking boosts volumes and fosters marginality gains (Moro Visconti, 2019).
Artificial Intelligence	AI will transform nearly every aspect of the financial service industry. Automated wealth management, customer verification, and open banking all provide opportunities for AI solution providers.

FinTech versus technological and banking Stock Market index.

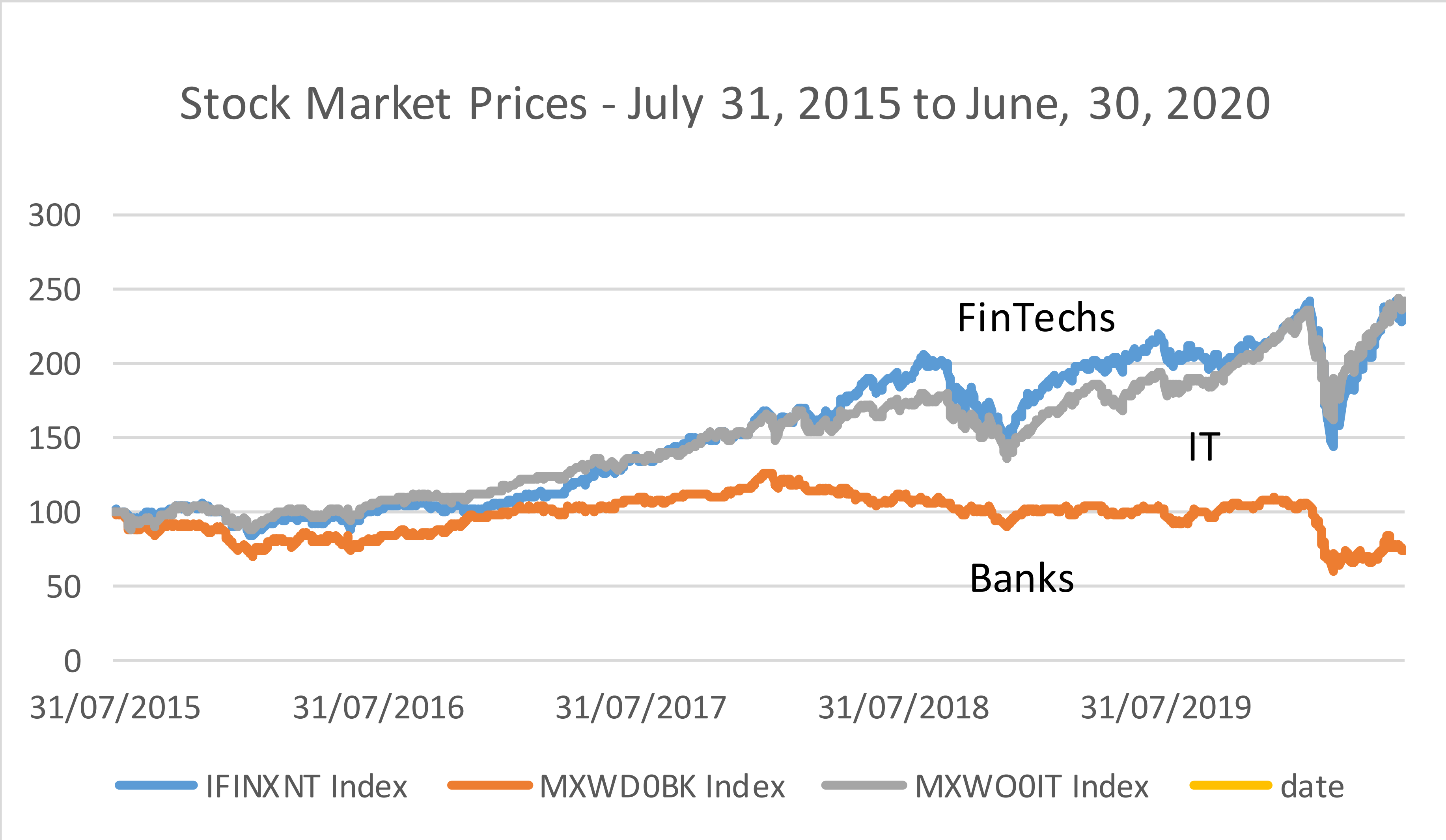
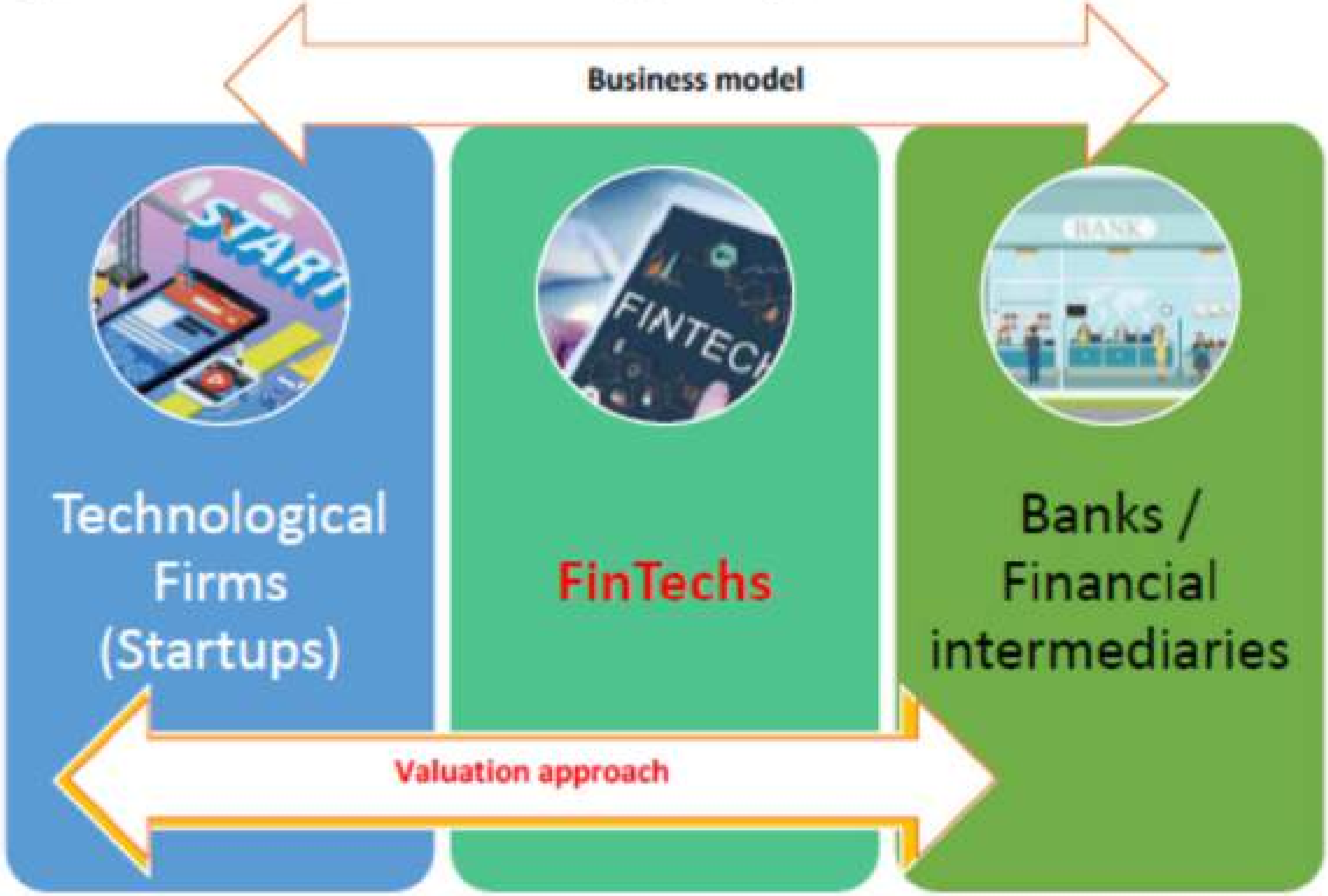
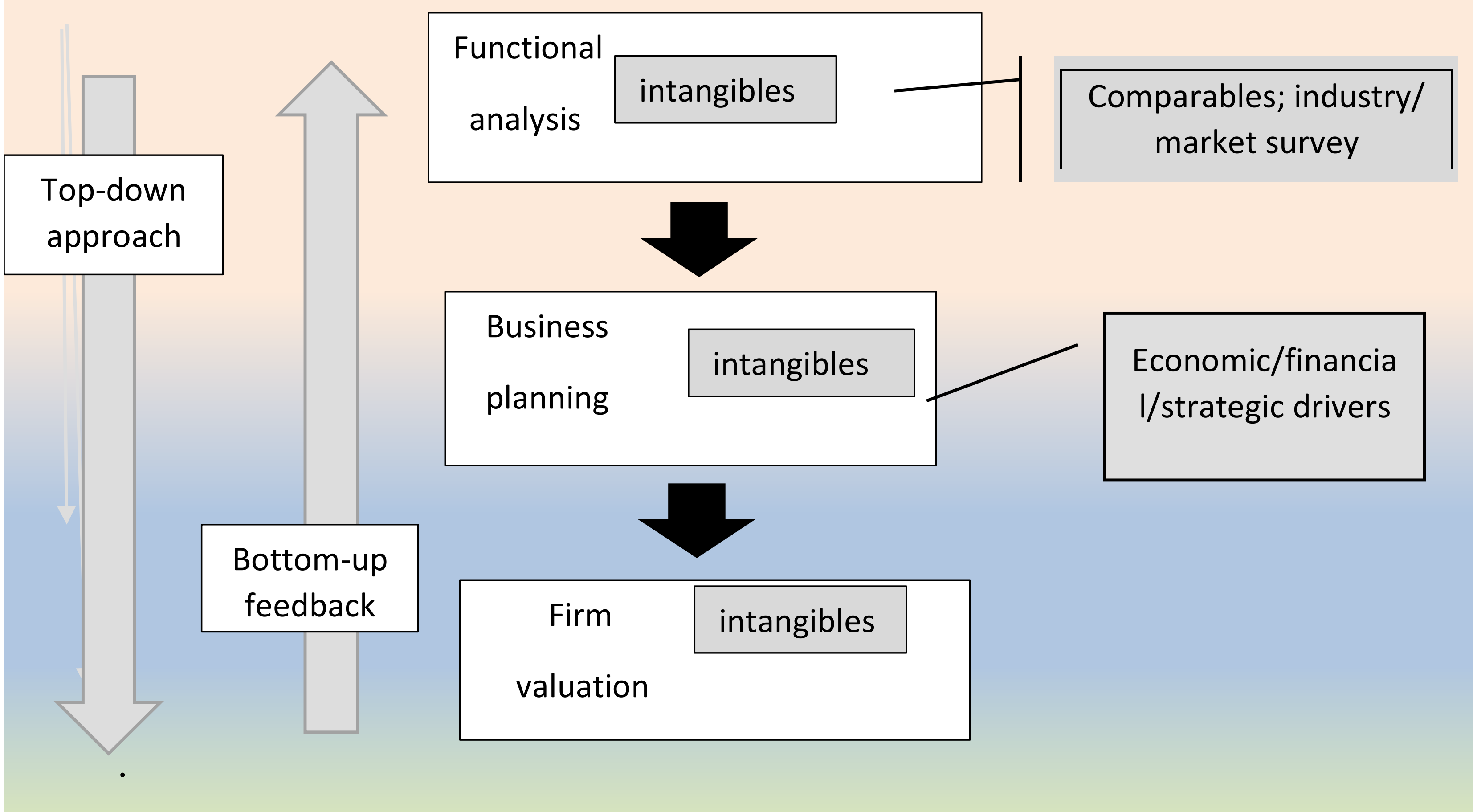


Figure 5 - *Business Model and Valuation Approach of FinTechs*



From functional analysis to firm valuation

Functional analysis, business planning, and firm valuation



Main valuation approaches

Table 2 – *Comparison of the main evaluation approaches of traditional firms, technological startups, and banks*

Traditional Firm	Technological Startup (IPEV, 2018)	Bank (Financial intermediary)
Balance-sheet based (Fernandez, 2001)	Venture Capital method	Expected dividends per share / Dividend Discount Models
Income	Binomial trees	Adjusted book value of equity (to proxy Market value)
Mixed capital-income		Excess Return Models
Financial (DCF)		
Market multiples (comparable firms)		

Default of FinTech Startup

Among the reasons that may cause the default of Fintech startups, the following are worth mentioning[2]:

- **Underfunding.**
- **Choosing an unexperienced Venture Capital.**
- **Overlooking compliance.** Regulatory complexity is often underestimated.
- **Thinking a fintech startup is the same as any other tech startup.** psychological behaviors around money, credit, savings, and payments are different from those concerning IT, biotechnologies, etc.
- **Competing solely on cost.** banks have massive (traditional) scale advantages. *Going digital, Fintechs may reengineer traditional business models but the task is uneasy and risky.*
- **Overconfidence.** creating a new market is no easy task. Many Fintechs think that their business model is so innovative that they have no competitors. Whenever there is competition, geographical segmentation may represent a weak barrier, due to increasing financial globalization. Innovation may become increasingly challenging in a crowded and over-competitive market.
- **Underestimation of the length of the sales cycle.** financial institutions are notoriously slow purchasers of anything new.
- **Missing sales strategy**. Fintech startups are often the brainchild of software experts that have limited sales and marketing skills.
- **Lack of understanding of the financial market.** Fintech startups pursuing a B2C business model often overestimate the extent to which consumers will: 1) change their behavior, and 2) pay for a new product or service in addition to all the things they already pay for. While a B2B model may be a better path for some fintech startups, some fail by not understanding that they're a vendor--not a partner--which may require a completely different set of skills and capabilities from those they already have.