In collaboration with
McKinsey & Company

Fuelling Innovation: Closing Fintech Funding Gaps

WHITE PAPER

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Foreword

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Over the past decade, the financial technology (fintech) industry has become a vibrant and indispensable part of the financial services world. The innovation that fintech brings has helped build out financial services infrastructure and generated benefits across the economy, ranging from greater choice for individual consumers who expect their financial interactions to keep pace with the rest of their digital lives to small businesses looking for ease of use, convenience and low transaction costs. In developing countries, in particular, fintech has played a significant role in improving financial inclusion, allowing millions of previously unbanked adults to access financial services. By offering essential funding and support, venture capital (VC) firms have empowered fintech start-ups to scale their concepts, challenge traditional financial services, and introduce innovative products and services in the market.

However, obtaining VC funding remains a challenge for many fintech companies across regions. A disparity exists between where VC investments are directed and where funding is most needed. This mismatch could impede the progress of fintech innovation, especially in emerging markets where funding tends to be lesser and the potential benefits of fintech development, such as expanded offerings to underbanked segments of the population, can be the greatest.

To confront this pressing challenge, the World Economic Forum and McKinsey & Company (McKinsey) have jointly launched the Fuelling Innovation: Closing Fintech Funding Gaps initiative. Through this report, we examine where fintech funding gaps exist across regions and outline strategies to bridge these gaps, aiming to help build a more robust fintech ecosystem. By conducting research on global and regional trends in fintech funding and engaging with key stakeholders within the fintech industry, we identify factors that fuel or hinder fintech funding. We also present practical strategies for narrowing regional funding gaps to boost fintech innovation and foster a more holistic development of fintech globally.

Addressing funding gaps involves more than aiming for equitable investment distribution. Unleashing the potential of the full fintech ecosystem is crucial for stimulating development, broadening access to financial services, and creating fresh opportunities for individuals and businesses. We hope that this report will motivate action, offer insights to all stakeholders, and contribute to establishing a global financial system that is more inclusive, innovative and resilient.

Executive summary

Digital public infrastructure, regulatory clarity, support networks, local financial capacity, and sustainable growth strategies are key to closing fintech funding gaps.

This report identifies potential fintech funding gaps and proposes strategies to close them. It is based on primary research, quantitative analysis, stakeholder interviews and thematic workshops with the Steering Committee and Working Group members of the Fuelling Innovation: Closing Fintech Funding Gaps initiative of the World Economic Forum and McKinsey. Its key findings highlight recent trends in venture capital (VC) funding in the financial technology (fintech) segment, and define pathways to attract VC investments into fintech ecosystems across regions.

VC funding has been a powerful engine for fintech growth, but momentum has slowed: With more than $350 billion of VC funding invested since 2015, fintech has become an industry with global net revenue exceeding $150 billion as of 2023 and is expected to grow to $400 billion by 2028. VC funding for fintech nearly tripled in 2021 from the previous year, reaching $92 billion. This explosive growth quickly reversed: in 2022, VC funding for fintech declined to $55 billion and fell further to $30 billion in 2023, a 67% decrease from 2021 highs.

Current geographic concentration of funding may not reflect future revenue opportunities: Sub-Saharan Africa (SSA), Latin America and the Caribbean (LAC) as well as the Middle East and North Africa (MENA) collectively only received 10% of global fintech funding during 2020-23, yet are projected to generate 15% of global fintech revenue by 2028.

Despite the global VC fintech funding downturn, funding in MENA and LAC has experienced significant growth: Exceptional fintech growth in some regions bucks the global trend. LAC saw the highest funding compound growth over the last decade, reaching 37% between 2015 and 2023, despite an 81% decrease since the 2021 peak. In MENA, fintech VC investments experienced a compound annual growth of 33% and the volume of fintech VC funding more than tripled from $600 million to $1.9 billion between 2020 and 2023.

Current VC fintech funding distribution across fintech subsectors has broadened and become more balanced: While the payments subsector consistently secures 20-25% of VC fintech funding each year, the share of other subsectors, such as capital markets, banking-as-a-service[1] and embedded finance,[2] has notably increased. The combined share of these subsectors in total fintech VC funding grew from 4% in 2015 to 13% in 2023.

This report identifies five pathways to attract VC investments and close existing fintech funding gaps across regions:

1 Investing in digital public infrastructure

- Accelerate the development and implementation of digital public infrastructure strategies across countries to catalyse fintech innovation.
- Build interoperable and scalable systems for identification, payments and data sharing.

2 Enhancing regulatory clarity and encouraging regional collaboration

- Ensure clarity and transparency in current regulatory frameworks to strike the right balance between consumer protection and creating an environment conducive to fintech innovation.
- Encourage regional collaboration to harmonize regulations to facilitate cross-border fintech growth.

3 Nurturing talent and strengthening support networks

- Develop a local talent pipeline and facilitate access to international talent that includes the highly skilled workforce needed for fintechs to grow and scale.
- Strengthen support networks, such as incubators, accelerators and venture studios, to offer resources, guidance and growth opportunities.

4 Developing local financing capacity

- Expand local fintech financing opportunities beyond VC by tapping into a wider pool of investors and securing innovative debt financing to fuel growth.
- Create a positive feedback loop where successful fintech investments attract further capital, fostering a dynamic and robust fintech ecosystem.

5 Encouraging sustainable fintech growth strategies

- Advise fintechs to focus on building a robust and stable core business with a proven market fit before expanding.
- Encourage fintechs to establish mutually beneficial partnerships, control costs and continue innovating to enhance operational efficiency.

1 A decade of disruption: The role of VC funding in accelerating fintech innovation

VC funding has propelled the fintech industry over the past decade, but momentum has slowed.

The need for fintech products and services has been rising with the growing digitalization of economies. Over the past decade, fintech innovation has provided individuals and businesses with convenient and seamless access to financial services. Nevertheless, the success and growth of fintech companies depends on their ability to secure the funding they need to innovate, expand and develop their businesses.

At a time when the VC funding that fintechs rely on has been declining, this report identifies gaps and imbalances across regions and fintech subsectors, and identifies pathways to encourage investments and foster stronger and more resilient fintech ecosystems.

Venture capital has long played a crucial role in financing waves of technological innovation, and the impact of VC funding on the digital economy is both long-lasting and transformative: six of the top 10 largest companies globally were initially backed by VC.[3] Today, their combined market capitalization exceeds $12.5 trillion, which is larger than the gross domestic product (GDP) of all countries except the United States (US) and China.[4] Over the past nine years, fintech has consistently ranked as one of the top sectors in terms of VC investment,[5] attracting a 12% share of all VC funding on average (Figure 1).

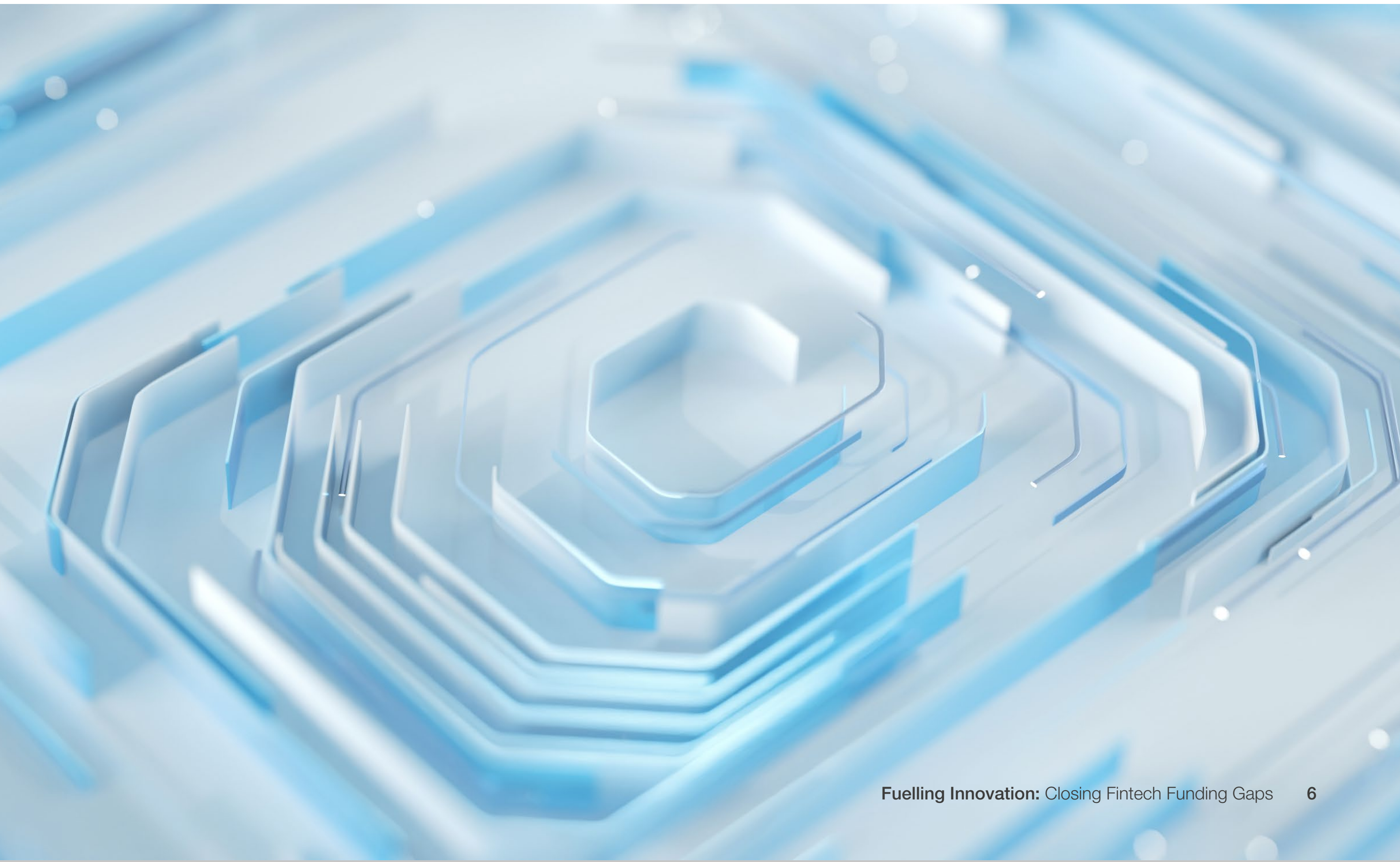
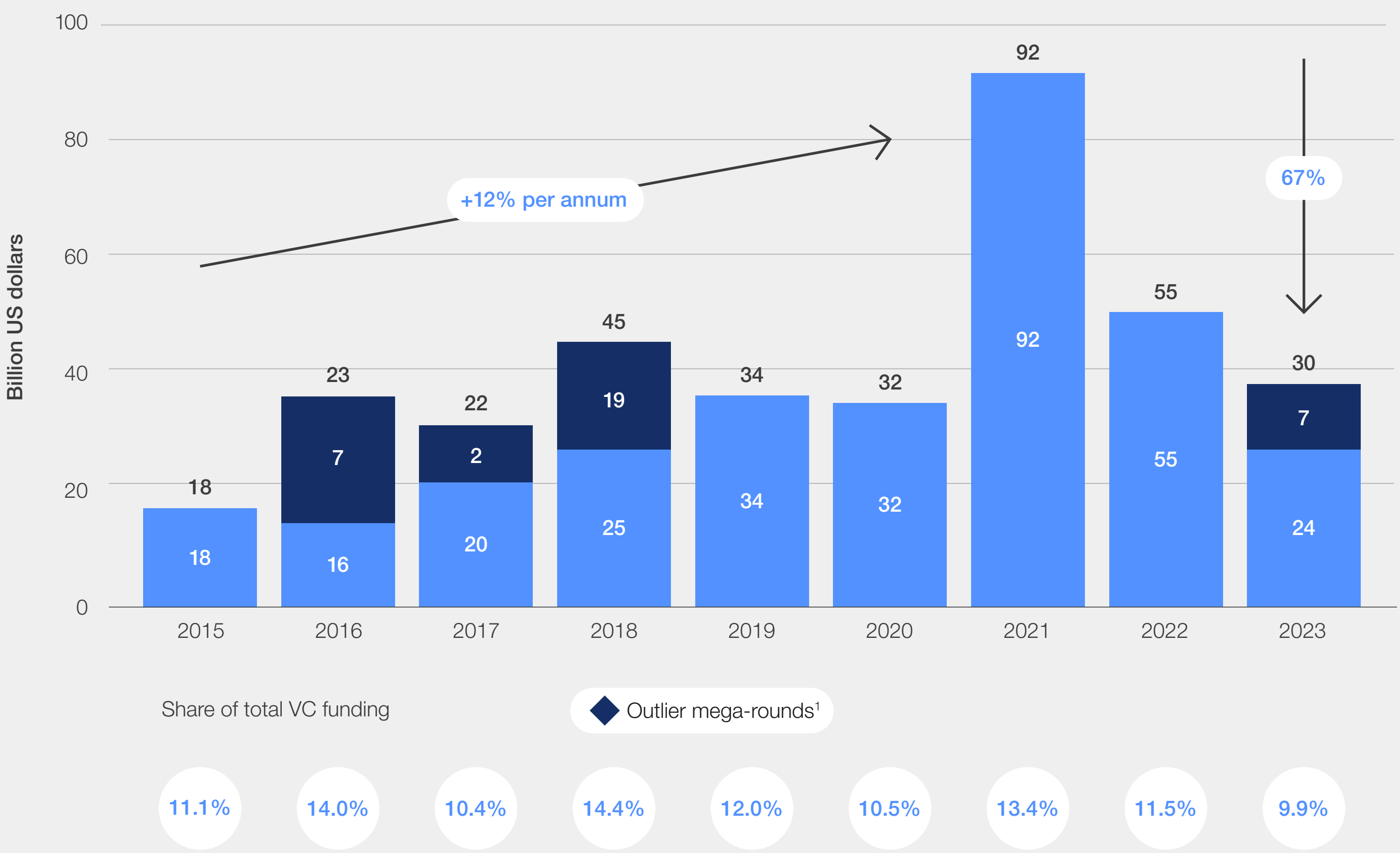
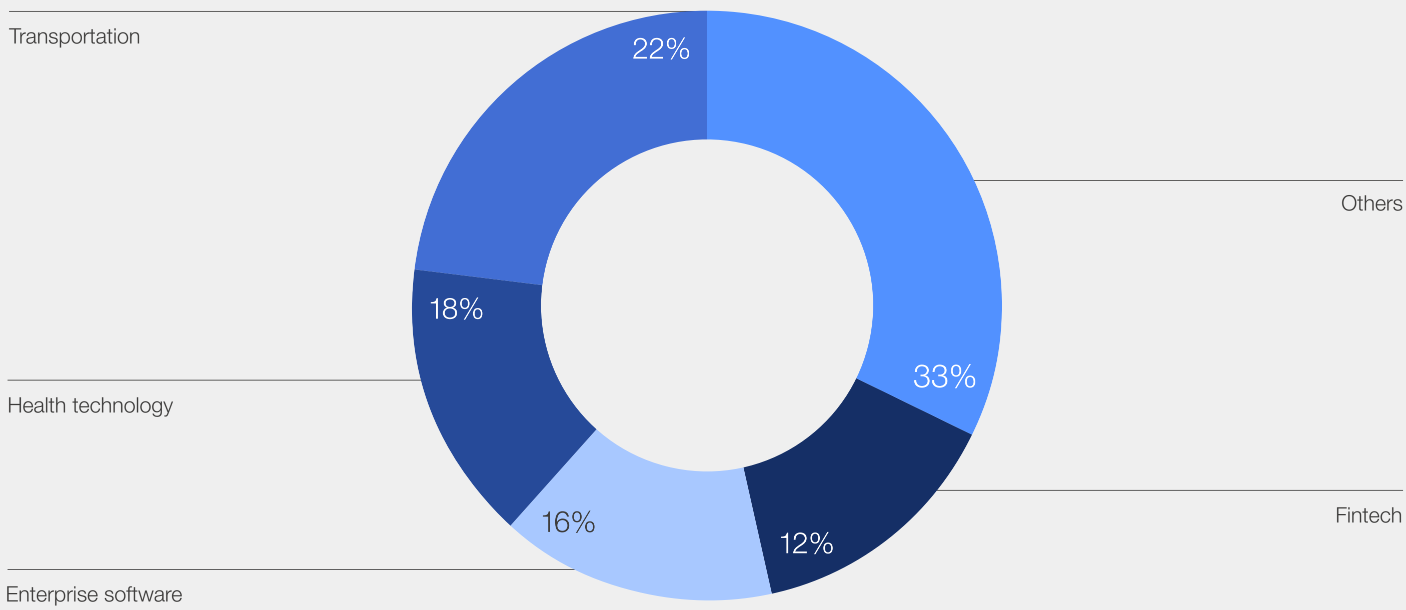


FIGURE 1 | **Share of total VC funding in the fintech industry**

Total VC fintech funding, in billion US dollars



Share of total VC funding 2015-2023



Notes: Numbers in the bars represent VC fintech funding in billion US dollars for each year. 1. Includes Stripe's $6.5 billion in 2023; Ant Group's $14 billion in 2018 and $4.5 billion in 2016; Lufax's $1.2 billion in 2016 and $1.3 billion in 2018; Du Xiaoman's $1.9 billion in 2018; and JD Digits' $1 billion in 2016, $2.1 billion in 2017 and $2 billion in 2018.

Source: Dealroom.co; McKinsey FinTech; McKinsey analysis

With the support of VC funding, fintech has developed into an industry with net revenue exceeding $150 billion, currently representing an estimated 5% of the global banking sector's net revenue.

Global VC funding for fintechs has grown at a steady rate of about 12% annually, from $18 billion in 2015 to $32 billion in 2020. In 2021, supported by the pandemic-induced acceleration of digitalization and global financial markets' being flush with liquidity,[6] fintech funding almost tripled to $92 billion, with a surge in valuation for fintechs across all stages in public and private markets.[7]

This explosive growth quickly reversed, as geopolitical instability and rising interest rates cast a shadow on the economic outlook and dampened the valuations of VC investments. In 2022, VC funding for fintech declined to $55 billion and fell further to $30 billion in 2023, a 67% decline from its 2021 peak.[8] This decline was consistent with a slowdown across sectors – overall global VC funding reached a five-year low in the first quarter (Q1) of 2024, its lowest level since Q2 of 2019.[9]

However, green shoots are emerging, with overall VC funding rising 8% and deal counts growing 17% globally in Q2 of 2024.[10] According to recent estimates from the National Venture Capital Association, the level of dry powder (the amount of committed but unallocated capital) is now at a record high and has reached $312 billion as of the end of 2023, representing a 45% increase compared to its estimated level at the end 2021.[11] As investors become more selective and take longer to deploy capital, focusing on start-ups with clearer paths to profitability and more reasonable valuations, the levels of dry powder have continued to grow.

With the support of VC funding, fintech has developed into an industry with net revenue exceeding $150 billion, currently representing an estimated 5% of the global banking sector's net revenue.[12] The fintech industry has become the second most prolific creator of unicorns (start-ups that exceed a $1 billion valuation), just behind enterprise software.[13] As of 2023, approximately 362 fintechs globally have reached unicorn valuation, and nearly 150 fintech unicorns have realized an exit.

Despite the recent slowdown in fintech funding, there are reasons to remain optimistic about the sector's long-term prospects.The fundamental drivers of fintech adoption, such as changing consumer preferences, technological advancements, and the need for more inclusive and efficient financial services, remain strong.

Looking ahead, the growth rate of net revenue in the fintech industry is expected to be 15% per year between 2022 and 2028, outpacing the 6% annual growth expected of retail banking in the same period. Prior McKinsey research has estimated that global fintech net revenues could reach between $325 billion and $463 billion in 2028, representing 8% of total banking sector revenue.[14] As the global economy recovers and investor confidence returns, the fintech industry is well-positioned to attract renewed interest from investors, fuelling the next wave of innovation and growth.

BOX 1

Definition and scope

This report defines fintech players as start-ups and growth companies launched in or after 2000 that rely primarily on technology to perform fundamental functions provided by financial services. These companies affect how users store, save, borrow, invest, move, pay and protect money.

For the analyses in this report, funding data for fintech companies has been sourced from Dealroom.co on 20 February 2024. The dataset included around 60,000 fintech companies from 146 countries and their nearly 20,000 funding rounds between 2015 and 2023.

For the funding analysis featured in this report, the following fintech subsectors were included: daily banking, lending, wealth management, payments, investment banking, capital markets, small and medium-sized enterprise (SME), and corporate services, operations and infrastructure (including embedded finance and banking-as-a-service). The analysis excluded cryptocurrency, decentralized finance and insurance technology (insurtech).

For VC funding, pre-seed, angel, seed, early VC, late VC, Series A-I and growth equity were included. For the regional analysis, countries were grouped across six regions: Asia-Pacific (which includes South-East Asia, East Asia, Central Asia and Oceania), Europe, US and Canada, Latin America and the Caribbean (LAC), Middle East and North Africa (MENA), and Sub-Saharan Africa (SSA).

In the funding analysis featured in this report, the data have been normalized to reduce distortion of the overall funding landscape and better understand the nuances across different regions by excluding some of the outlier "mega funding rounds." The calculations that exclude those "mega funding rounds" include fintech VC funding and fintech VC funding as a percentage of GDP by region (Figure 3), the share of VC fintech funding rounds by local and foreign investors (Figure 6), VC fintech investments by region (Figure 7), and global fintech funding by subsector (Figure 8 and 9).

The outlier mega-funding rounds include Ant Group's $4.5 billion series B funding round in 2016 and $14 billion series C funding round in 2018; Du Xiaoman's $1.6 billion growth equity VC funding round in 2018; Lufax's $1.2 billion series B funding round in 2016 and $1.3 billion series C funding round in 2018, JD Digits' $1 billion early VC funding round in 2016; $2.1 billion series A funding round in 2017 and $2 billion series B funding round in 2018; and Stripe's $6.5 billion growth equity VC funding in 2023.

2 Navigating the fintech funding landscape: Disparities and opportunities

Gaps and imbalances have emerged in the distribution of funding, depending on the geography, maturity stage and sectoral focus of fintech companies.

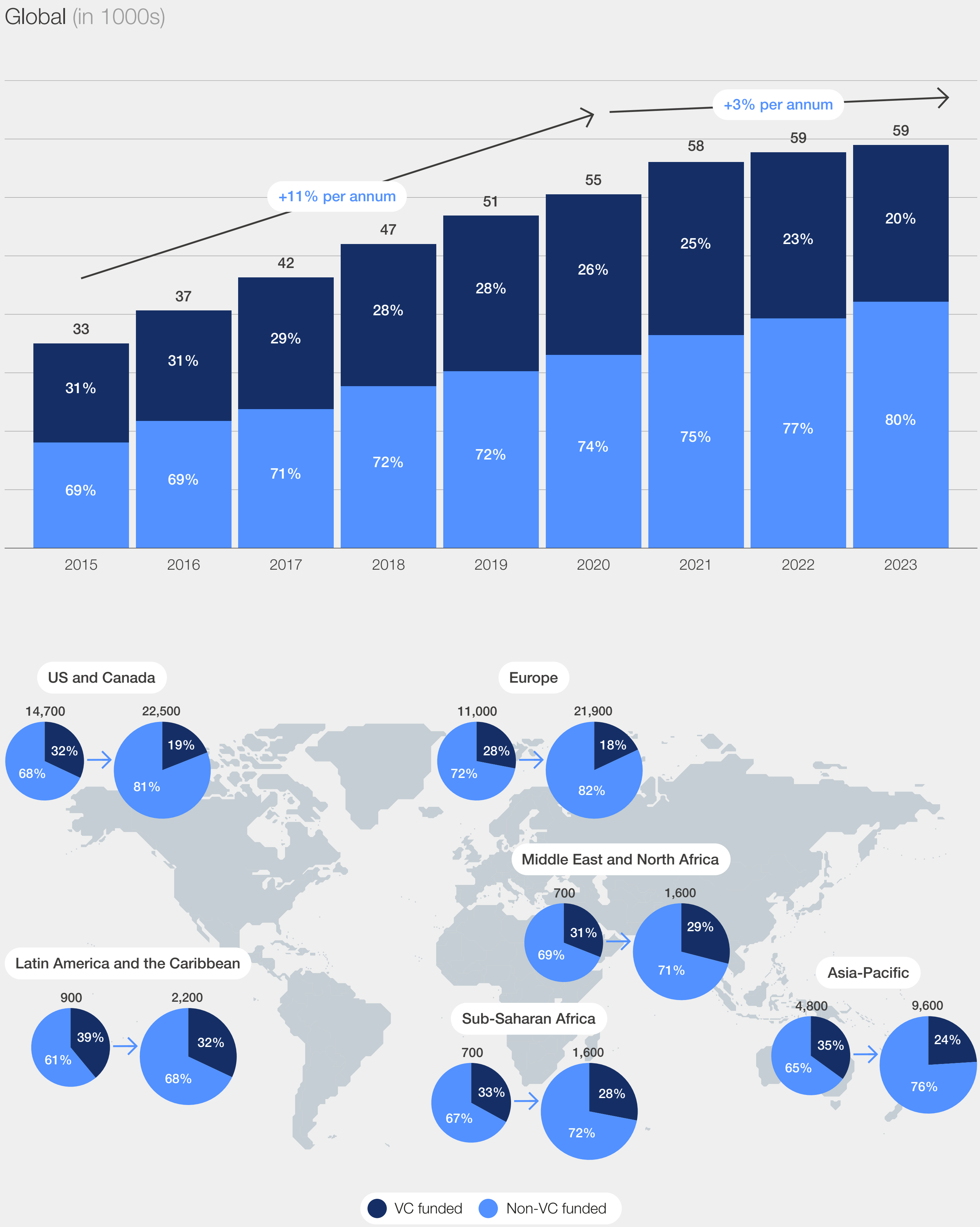
$350 billion

in funding has gone into the fintech industry since 2015.

While more than $350 billion in funding has gone into the fintech industry since 2015, VC funding is distributed unevenly across regions, and among fintech companies at different maturity stages and various fintech subsectors. These variations may result from the distinct nature and intrinsic characteristics of various fintech environments. They could also imply some inefficiencies or limitations within several of these environments. Identifying funding gaps and imbalances, along with the potential underlying causes, can help stakeholders improve their fintech environment and enhance its attractiveness for investment.

The fintech industry has grown rapidly in the past decade. The number of fintechs globally increased from 33,000 in 2015 to 57,000 in 2021, an average annual increase of 10%. In 2022 and 2023, the number of fintechs continued to grow but at an annual rate of just 1%; the industry ended 2023 with a record 59,000 fintechs worldwide. While all regions have experienced growth in the number of fintechs since 2015, there are marked differences in the growth levels across different regions. The US and Canada remains the region with the largest number of fintechs – 22,500, or 38% of the global total, in 2023 – followed by Europe with 21,900, or 37% of the global total (Figure 2).

FIGURE 2 | **Number of fintechs by region and share of VC-funded fintechs (2015-2023)**[1]



Note: 1. The number of fintechs has been estimated by taking into account pre-IPO (initial public offering) and pre-M&A (merger and acquisition) fintechs that have raised VC funding in the last four years.

Source: Dealroom.co; McKinsey FinTech; McKinsey analysis

Mapping the fintech funding landscape across regions

The US and Canada alone accounted for 39% of total fintech funding from 2015 to 2023, and the region also has much higher funding per capita than other regions (Figure 3). Various factors could explain this, including the much larger investor base, with five of the top 10 VC firms (measured by assets under management) being from the US; the presence of a large single market without language or jurisdiction barriers, making it easy and inexpensive to expand; and the large number of mature fintech scale-ups needing funding for further expansion and acquisition.[15]

Europe experienced robust growth of 13% annually on average during this 2015-2023 period, and it was one of the top three funded regions. As of the end of 2023, fintech funding in Europe reached $5.6 billion annually. Fintechs have been substantially improving customer satisfaction and creating value with superior service at lower costs and have been estimated to have generated close to 135,000 jobs across countries.[16] As a result of this rapid growth,

FIGURE 3 **Fintech VC funding, and funding-to-GDP ratio by region (2015 to 2023)**

Source: Dealroom.co; Economist Intelligence Unit; McKinsey analysis

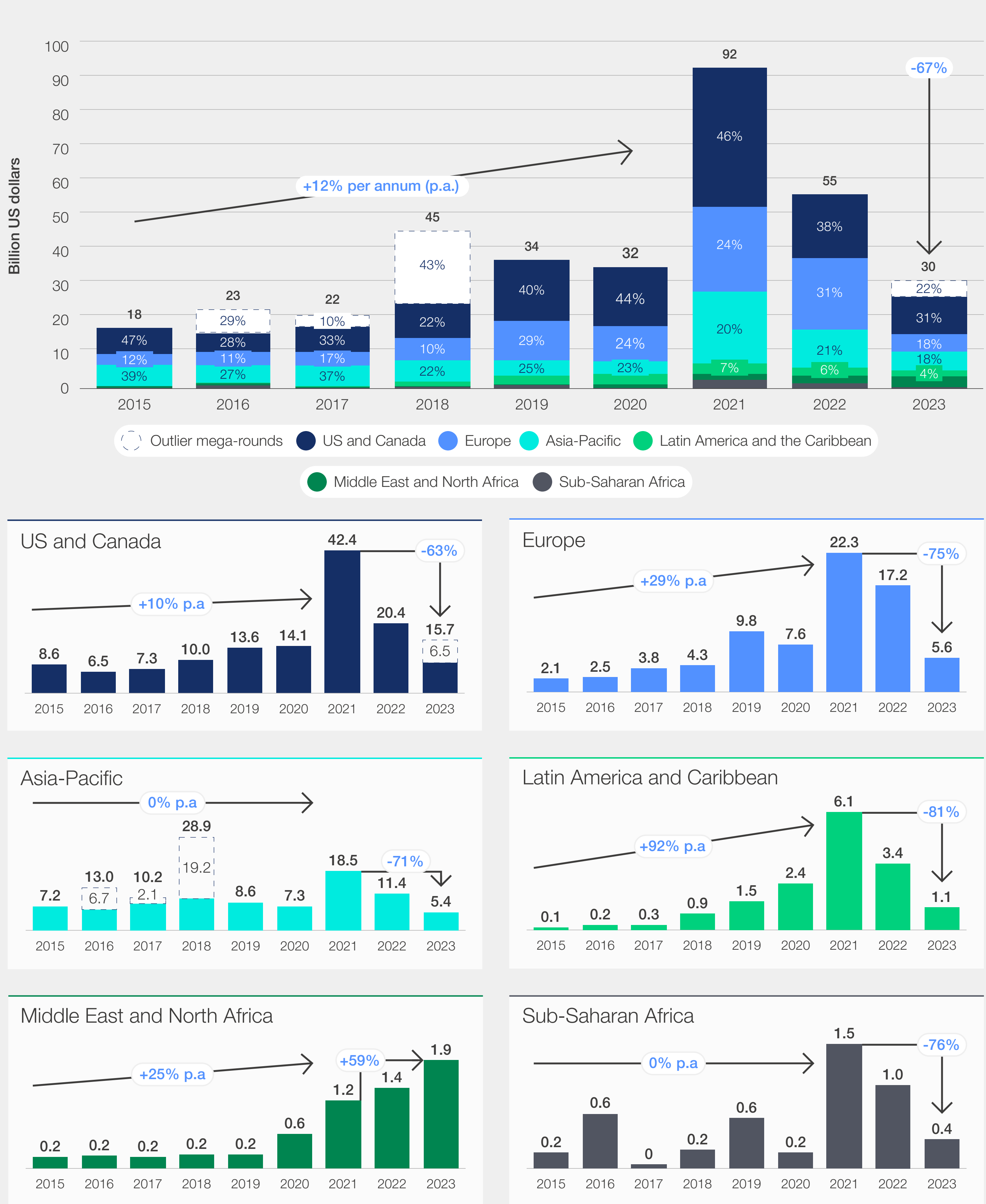
fintechs have transitioned from the periphery to the centre of the European financial services landscape, with some of the largest fintechs by market value now ranking among the top banking institutions in Europe's major economies.[17]

The Asia-Pacific (APAC) was the only region with a negative compound growth rate of 4% over this period. The share of fintech funding received declined from about 39% in 2015 to 23% in 2023. One-off "mega" funding rounds distorted the picture in APAC: this includes a $14 billion fundraising in 2018 by Ant Financial, the largest single fintech fundraising globally by a private company at the time. This transaction alone accounted for 31% of total VC funding to fintech globally that year.

Exceptional fintech growth in some regions is bucking the decline in global VC fintech funding and highlights the potential of these markets to attract investment and foster a thriving fintech ecosystem. LAC has notably seen the highest compound annual funding growth, at an annual average of 37% between 2015 and 2023, despite an 81% decrease since the 2021 peak (Figure 4).

In the past decade, fintechs have shaken up the financial sector in LAC, providing innovation in lending, payments, regulation and compliance, among other segments. In 2021, there were more than 300 million users of digital payments and more than 30 million users of digital banks, mostly concentrated in Brazil and Mexico. Fintechs boosted competition by reducing lending spreads, increased inclusion by serving previously unbanked and underbanked consumers and small and medium enterprises, and provided banks with new technologies and services.[18]

FIGURE 4 **VC fintech funding trends by region (2015 to 2023)**



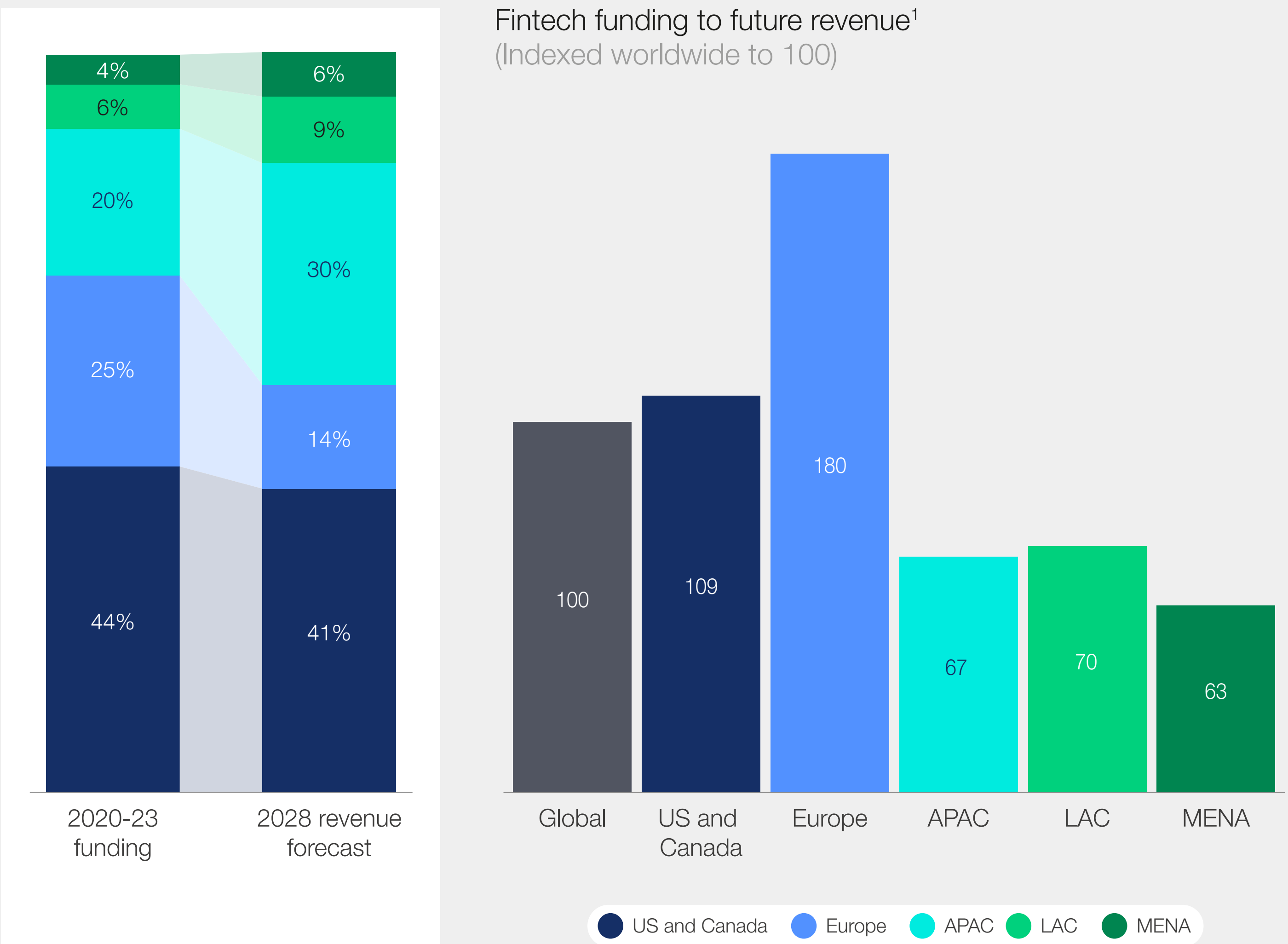
Source: Dealroom.co; McKinsey FinTech; McKinsey analysis

The Middle East and North Africa (MENA) had the second-highest growth rate for fintech VC funding between 2015 and 2023, with an annual average growth of 33%. As of 2023, funding had reached $1.9 billion across 93 funding rounds, compared with $200 million in 2019. The volume of funding in the region tripled between 2020 and 2023 and MENA was the only region to see funding growth between 2021 to 2023 (Figure 4). This growth was driven by a series of successful fundraisings by regional fintechs, including the birth of three unicorns: Tabby,[19] Tamara [20] and MNT-Halan,[21] all in 2023. The MENA region has a young, educated and growing population and some of the world's highest mobile, internet and smartphone penetration rates. This suggests significant potential for financial innovation in the region.[22]

In SSA, while fintech funding declined significantly in 2022 and 2023, the region managed to maintain a higher number of funding rounds compared to 2018 and previous years. The adoption of mobile money has been a key driver of the growth in the adoption of fintech services across countries; 33% of adults in the region had a mobile money account in 2021, almost triple the 12% in 2014. These mobile money accounts enabled users not only to transfer and spend but also to save, lend and borrow.[23]

When looking at fintech funding between 2020 and 2023 and comparing it to estimated future revenue by region, one can note that Europe and the US and Canada have received, respectively, 109% and 180% of the 2028 fintech revenue projected.[24] In contrast, regions such as APAC have received only 67%, LAC 70% and MENA 63% of their anticipated future fintech revenue. As highlighted in Figure 5, despite the recent significant funding growth in these regions, global fintech VC funding distribution has not reflected the shifting landscape of growth opportunities. LAC, MENA and Africa collectively received only 10% of global fintech funding during 2020-23, yet are forecasted to generate 15% of global fintech revenue by 2028.

FIGURE 5 **Share of 2020-2023 funding against share of 2028 fintech revenue forecast**



Note: Includes Stripe's mega-round of $6.5 billion; if excluded, ratio for North America would be 102. 1. Defined as share of total VC fintech funding in 2020-2023 divided by share of projected fintech revenue pool in 2028.

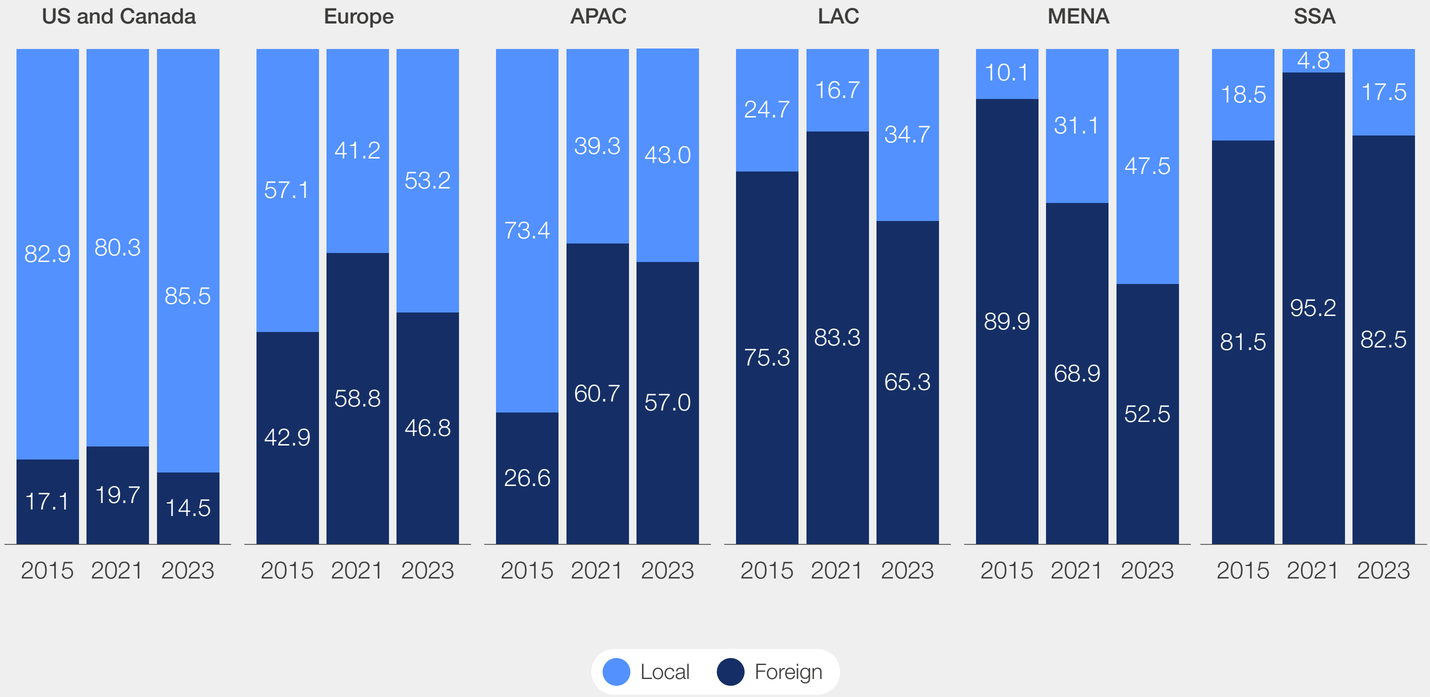
Source: Dealroom.co; World Bank population data; McKinsey FinTech; McKinsey analysis

Concentration of local vs foreign fintech investments

Both local and foreign VC investors play a crucial role in nurturing fintech ecosystems and helping fintechs scale. Local investors can bring intimate knowledge of the domestic market, allowing them to support homegrown fintech start-ups that address specific local needs and challenges. Foreign investors can contribute by providing a global perspective, extensive networks, and often access to larger pools of capital. Ultimately, the collaboration between local and foreign investors is essential.

Fintech funding in the US and Canada has the highest concentration of local investors, above 85% as of 2023, followed by Europe with 53.2% of local investors. Across APAC, LAC, MENA and SSA, the investment landscape looks dramatically different, with an average of 36% investments made by local investors and 64% made by foreign investors. However, the share of local investors has notably increased since 2015. The most impressive growth can be witnessed in MENA, where the share of local investors has grown from 10% in 2015 to 47.5% in 2023. Similarly, in LAC, the percentage of local investors has grown from 24.7% in 2015 to 34.7% in 2023 (Figure 6). Other regions such as APAC and SSA have seen growing foreign VC investment in their fintech sector during this period. The share of funding rounds by foreign investors in APAC has increased from 26.6% in 2015 to 57% in 2023.

FIGURE 6 **Share of VC fintech funding rounds by local and foreign investors (2015, 2021 and 2023)**

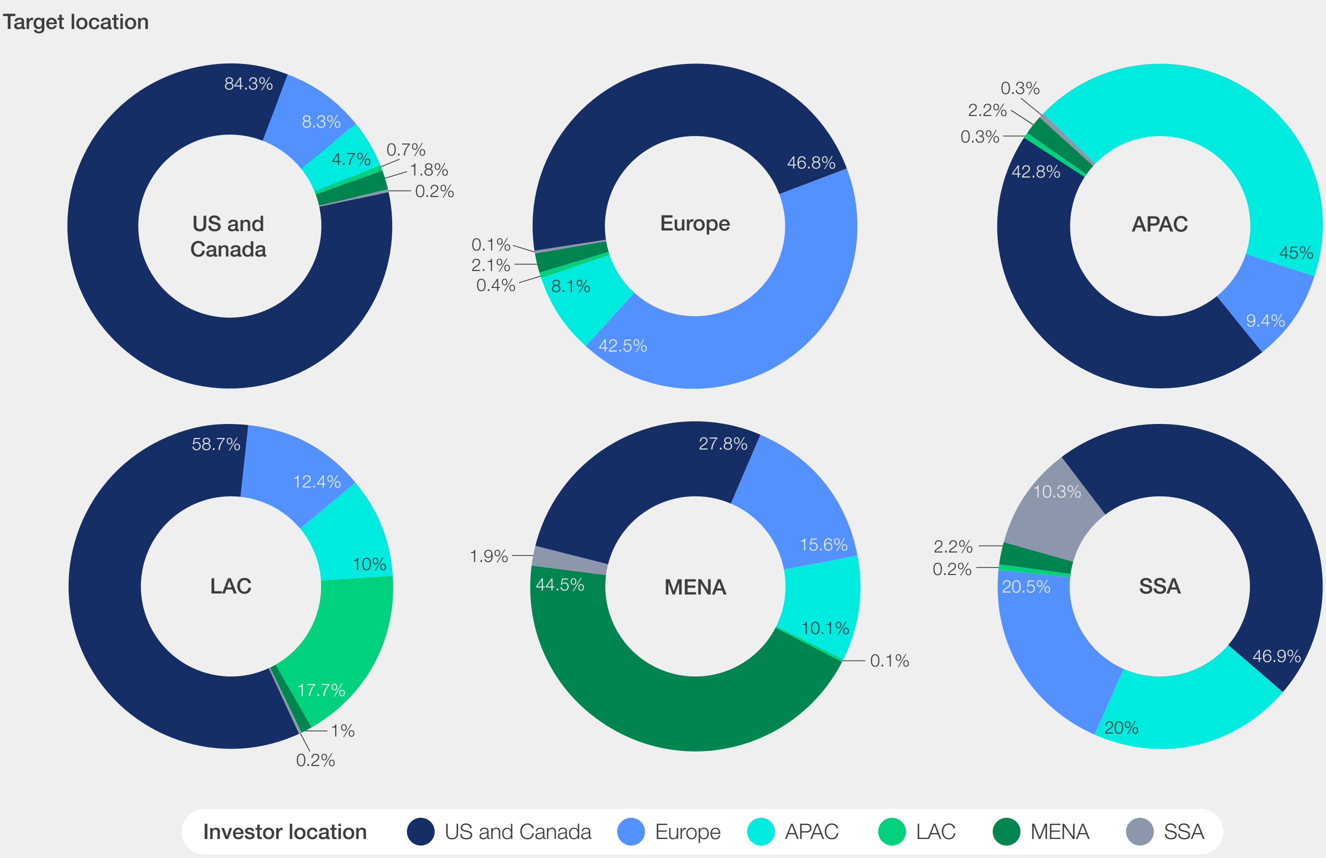


Source: Dealroom.co; McKinsey FinTech; McKinsey analysis

When looking closer at the source of foreign investments, fintechs in LAC and SSA remain highly dependent on investors from other regions, notably the US and Canada. In Europe, the Asia-Pacific and MENA, fintechs can secure more than 40% of their funding from local investors (Figure 7).

The role of foreign investors differs by region in terms of stage of investment. LAC, MENA and SSA rely more on foreign investors for early-stage funding, while all regions except the US and Canada rely heavily on foreign investors for late-stage funding.

FIGURE 7 **Source of fintech VC funding as share of total funding for each region (2020-2023)**



Source: Dealroom.co; McKinsey FinTech; McKinsey analysis

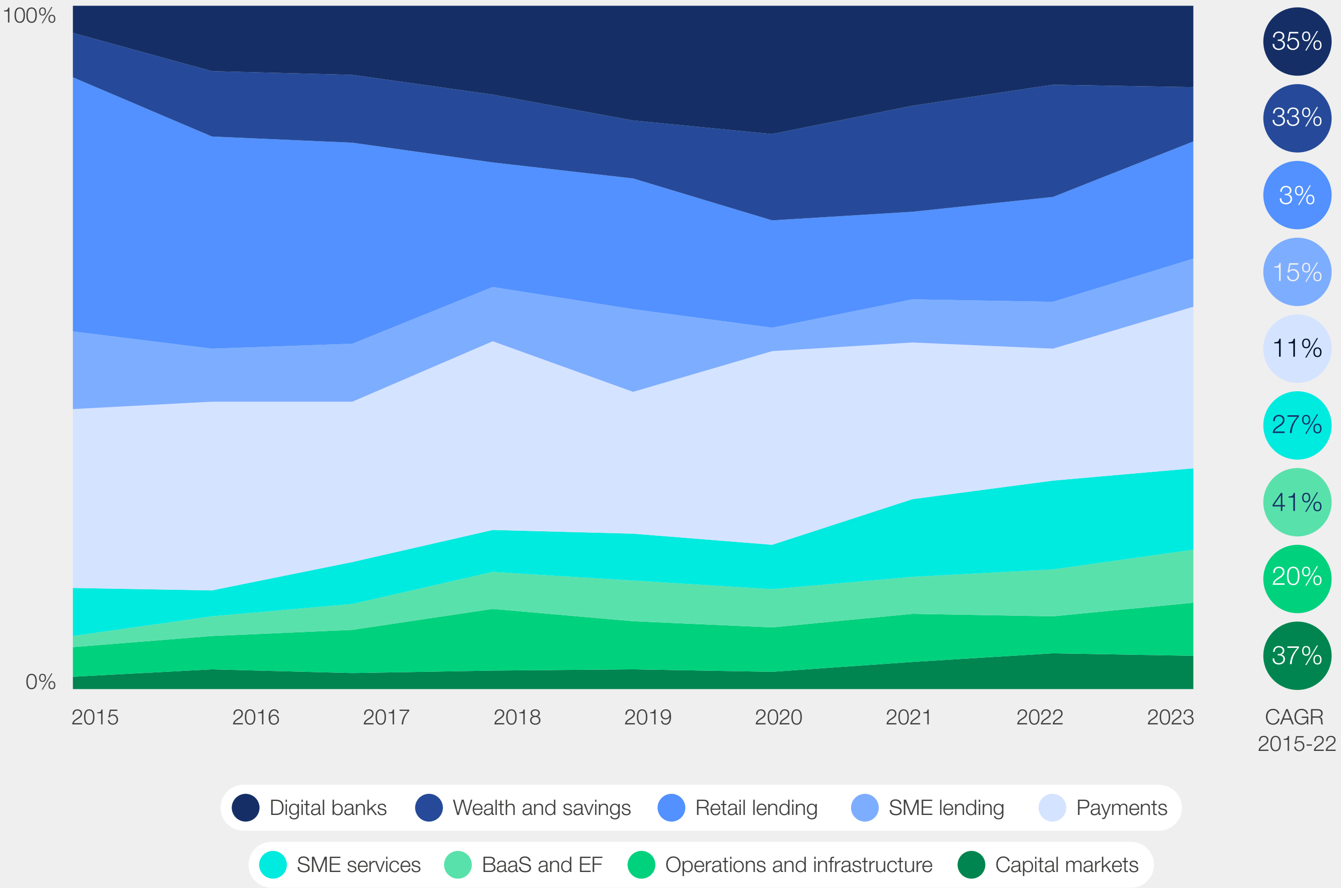
Fintech funding across subsectors: A shifting landscape

Fintech covers a wide variety of banking products and services, including but not limited to banking, payments, lending and wealth. As fintech develops, the products and services it offers grow in both quantity and complexity. Funding for fintechs flowed heavily into retail lending and payments in 2015-16, but more recently, the distribution of VC funding has broadened and become more balanced across the different subsectors. The payments subsector continues to secure about 20-25% of fintech funding, but as fintech activities in other subsectors – such as digital banking,[25] banking-as-a-service (BaaS)[26] and embedded finance (EF)[27]– become more vibrant, the share of these subsectors in total fintech VC funding has increased notably.

Funding for fintechs in the payment subsector continues to grow steadily at an annual average rate of 11%. Funding for BaaS and embedded finance has grown at an average annual rate of 41%, followed by capital markets (37%). Their combined share of fintech funding increased from 3.5% in 2015 to 13% in 2023 (Figure 8).

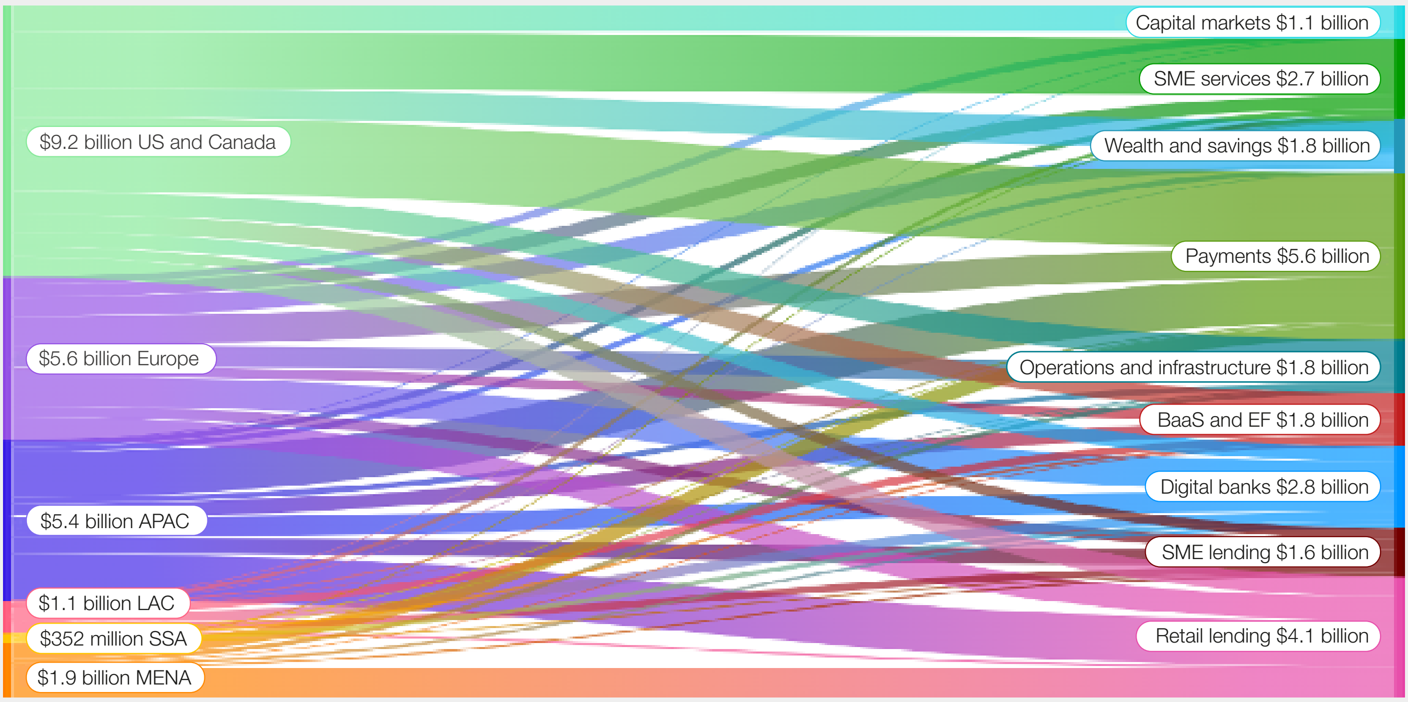
When looking at the distribution of fintech funding by subsectors broken down by region in 2023 (Figure 9), it is evident that the distribution of fintech funding has broadened across subsectors. The subsector that attracted the most funding in 2023 was still the payments subsector, with $5.6 billion in funding primarily targeted towards the US and Canada, APAC and Europe, reflecting strong demand and growth potential for payment technologies in these regions. Retail lending was the second largest fintech subsector, attracting $4.1 billion, with a significant proportion of that funding targeted towards APAC and MENA. The third and fourth most-funded subsectors were digital banks, with $2.8 billion, and SME services, with $2.7 billion in funding in 2023.

FIGURE 8 | **Global fintech funding by subsector (2015-2023)**



Source: Dealroom.co; McKinsey FinTech; McKinsey analysis

FIGURE 9 | **Fintech funding by region and fintech sub-sectors (2023)**



Source: Dealroom.co, McKinsey Fintech, McKinsey analysis

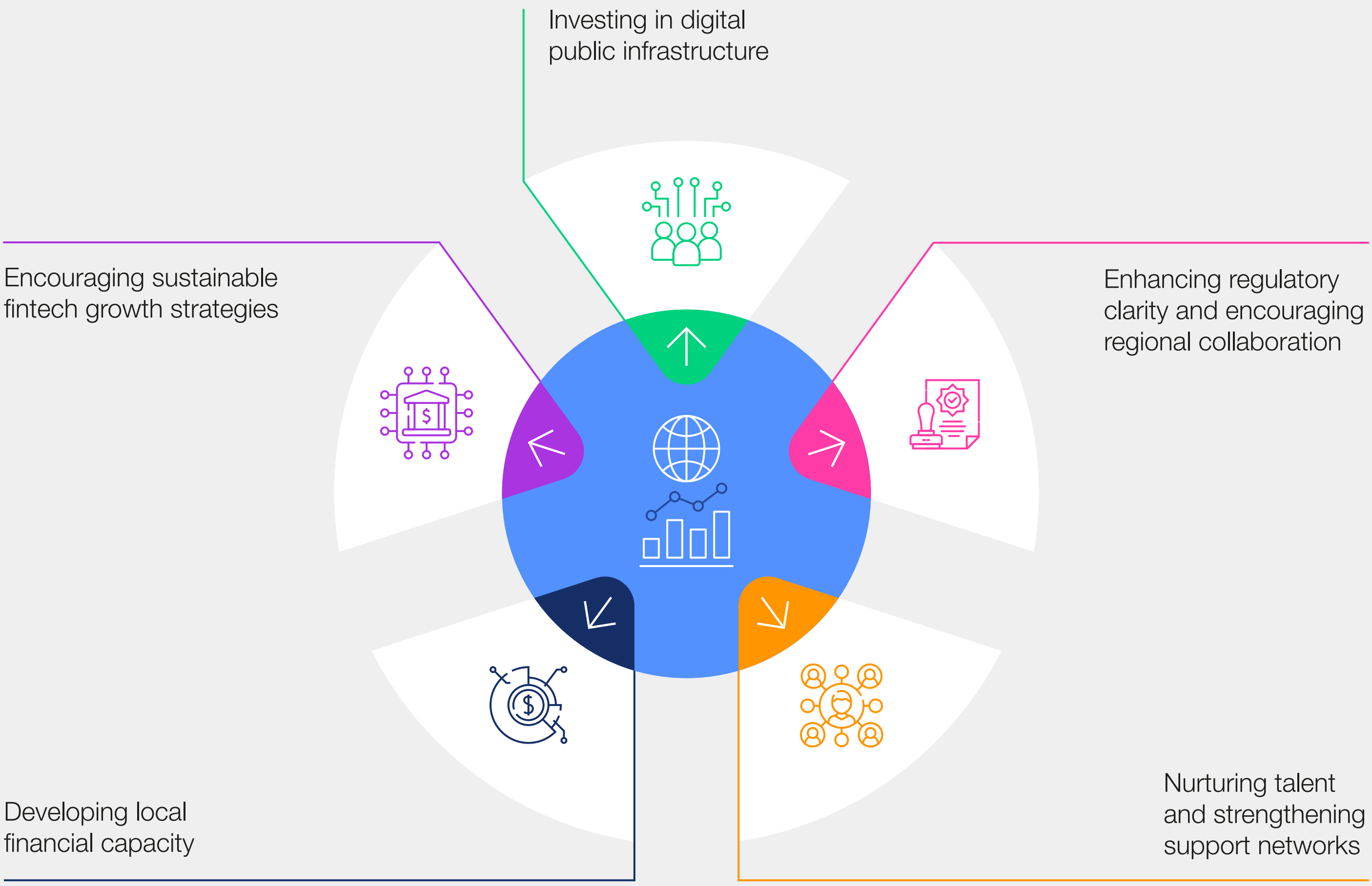
3 Closing fintech funding gaps: Five strategic pathways

These pathways can help close fintech funding gaps while fostering a supportive ecosystem for innovation and growth.

To gain a comprehensive understanding of the challenges faced by the fintech industry, the Fuelling Innovation: Closing Fintech Funding Gaps initiative of the World Economic Forum and McKinsey conducted a series of workshops and one-on-one interviews with key stakeholders in the ecosystem. These included fintech founders, investors and industry experts. Through these in-depth discussions, the primary obstacles hindering VC investment in specific markets were identified, and a clearer understanding emerged of how existing fintech funding gaps could be closed.

This section outlines eight priority actions, grouped into five distinct pathways, each aimed at closing existing fintech funding gaps. Collectively, these pathways provide a comprehensive approach to developing a supportive fintech environment, thus creating attractive fintech investment opportunities. The five pathways are:

FIGURE 10 **Overview of the five pathways to close fintech funding gaps, based on interviews with key stakeholders**



3.1 Investing in digital public infrastructure

Accelerating the development and implementation of digital public infrastructure

Accelerating the development and implementation of digital public infrastructure (DPI) is critical in bridging existing fintech funding gaps. DPI can be classified across four core building blocks: identity, payments, data sharing and other emerging technologies (such as geospatial DPI or artificial intelligence models).[28] The use of open application programming interfaces (APIs) across these building blocks enables both public and private sector innovators to build solutions over a unified, multi-layered set of digital platforms.[29]

Among these building blocks, payment systems play a crucial role in today's real-time digital economy. As of 2024, more than 70 live fast payment systems (FPS) exist across countries.[30] This widespread deployment, coupled with the implementation of interoperable standards in national payment ecosystems, can open the door to expanding cross-border FPS connectivity on a regional scale.[31]

The development and implementation of DPI has the potential to unlock significant investment opportunities and stimulate economic growth. Recent estimates suggest that the adoption and deployment of DPI across low- and middle-income countries could have a substantial positive impact on their economies. Projections indicate that by 2030, this could generate an additional $200-280 billion in GDP, representing a 1% to 1.4% increase in annual economic output. By establishing an interoperable core, common digital public infrastructure can reduce barriers to entry, increase interoperability and fuel fintech innovation.

The rate of adoption of open banking standards is increasing worldwide and as of the first quarter of 2024, almost 70 countries have legislated open banking regulations.

Unlocking the potential of open banking

Open banking allows customers to share their banking data with other financial service providers such as fintech firms. Using the data and infrastructure of open banking standards, fintech companies can tailor their products and services to the needs of different regions and customer segments, often leading to greater financial inclusion and an improved customer experience. With successful user adoption of fintech products and services, fintech firms can attain scale and profitability. On the whole, open banking tends to increase competition in the financial services industry, lower some barriers to entry, and accelerate the growth of fintech ecosystems.[32]

The rate of adoption of open banking standards is increasing worldwide and as of the first quarter of 2024, almost 70 countries have legislated open banking regulations.[33] Many countries are achieving this growth by implementing open finance standards that expand data access and sharing beyond payments to other areas of financial services such as insurance, investments and lending.[34] The United Kingdom (UK) released its first open banking standard in 2018 and since then, open banking adoption in the country has grown significantly, with more than 6 million consumers using open banking-powered products and services, including 660,000 small and medium enterprises as of June 2022.[35]

The European Union has also been one of the first to adopt open banking through the introduction of its revised Payment Services Directive (PSD2) in 2018. In June 2023, the European Commission proposed a regulation on a financial data access (FiDA) framework, which is aimed at supporting open finance and data-driven finance.[36] Open banking and open finance are enablers that allow fintech ecosystems to grow by advancing data access, safe data-sharing and interoperability. In the European Union alone, an estimated 400 non-bank providers have come up since the introduction of PSD2.[37]

3.2 Enhancing regulatory clarity and encouraging regional collaboration

Improving certainty and clarity in banking regulation

As fintech regulatory requirements are constantly evolving, regulatory certainty and clarity are among the key building blocks of a thriving fintech ecosystem. A transparent regulatory framework allows fintech firms to go through the complex process of licence application and business registration, as well as compliance with prudential regulation. For many fintechs, these processes remain challenging.

According to the latest World Economic Forum Future of Global Fintech Survey, while fintechs in advanced economies, emerging markets and developing economies (EMDEs) rated their regulatory environments quite favourably overall (63% found their regulatory environment to be adequate and appropriate), coordination among authorities and fintech licensing and registration were areas they identified as needing improvement (28% found these aspects to be poor).[38]

Regulatory approaches that strike a balance between fostering innovation and ensuring adequate safeguards are in place can help protect consumers and maintain financial stability. This requires reviewing and strengthening legal, regulatory and supervisory frameworks, as well as technology and financial infrastructures.[39] More than 50 countries to date have introduced regulatory sandboxes to foster financial innovation.[40] These sandboxes enable fintech companies to experiment with their products and services in a secure environment with close monitoring by regulators.[41] Research shows that countries with sandboxes attract more investment in technology-enabled innovation in financial services overall, when compared with countries with similar market environments but without sandboxes.[42]

Fostering regional regulatory collaboration

Through regional cooperation, regulators can share best practices, experiences and insights. This leads to better and more efficient regulation and also, most importantly, fosters interoperability of fintech solutions across countries. When regional regulators collaborate to standardize rules, fintechs that operate across many jurisdictions find it easier to navigate the regulatory environment and cut costs.

As an example, under the harmonized regulation created under the EU passporting system, financial institutions that have been authorized by their domestic authorities have the right to establish a branch or provide services in any other member states of the European Economic Area (EEA) without needing to seek further authorization or another licence.[43] This allows financial institutions to avoid setting up separate legal entities for each EEA country in which they operate and thus grow beyond their home countries, enabling firms to sell their services to the EEA's 450 million consumers.[44]

3.3 Nurturing talent and strengthening support networks

Establishing a local hub for global talent

Fintechs need access to highly skilled talent to be able to grow and scale up.[45] According to a recent survey of global fintech companies, one-third of fintech firms see talent as the second most important supporting factor for growth, after consumer demand.[46] Access to qualified and suitable talent is also essential to an ecosystem, if it is to develop as a leading fintech centre. A dual approach of accessing overseas talent and building a domestic pipeline of talent for the future becomes fundamental.[47]

Offering more incentives and reducing entry barriers are among the range of strategies that can attract international talent, as these individuals, equipped with highly sought-after skills, typically have several attractive location options to choose from. These can take the form of visa programmes, visa quotas, paths to long-term options, spousal visas and shorter processing time, among others.[48] For example, in 2017, the Canadian government launched the Global Skills Stream, which allowed skilled workers to obtain a Canadian work permit with just a two-week processing time. Two years after launch, it has already attracted close to 40,000 highly-skilled workers and created more than 48,000 jobs in Canada.[49] While attracting international talent is vital, developing a local talent pipeline is equally important for sustainable growth in the fintech industry.

In the US, higher education plays a key role in developing local fintech talent. For example, top universities such as the Massachusetts Institute

According to a recent survey of global fintech companies, one-third of fintech firms see talent as the second most important supporting factor for growth, after consumer demand.

of Technology (MIT), Stanford, New York University (NYU) and Berkeley offer programmes tailored to developing fintech talent by engaging industry experts and facilitating employment opportunities at top fintech firms.[50] This also creates a supportive environment to nurture entrepreneurship. Research shows that California is ranked as the top area with the best talent availability due to the size of its overall fintech workforce and its strength in technical and entrepreneurial talent, as well as the best talent pipeline because of numerous STEM education initiatives, a well-established and integrated network of academia and entrepreneurs, and a culture of mentorship.[51]

Other approaches to building a domestic talent pipeline include further education to retrain and upskill through free or subsidized courses, and employee share-ownership schemes to attract talent from incumbents with deep domain experience.[52]

Building a supportive network for start-up clusters

Innovation hubs in the fintech ecosystem bring together start-ups and R&D institutions (such as tech-enabled corporations and universities), as well as venture capital firms, incubators, accelerators and venture studios, creating diverse and connected communities.[53]

Joining an incubator or accelerator helps founders build a network, pursue growth and secure funding. Incubators help founders develop and refine high-potential start-up ideas over a span of one to five years and provide resources, including physical space, mentorship and legal consultation.[54] Research shows that participating in an accelerator can enable founders to raise 50% to 170% more from investors.[55] Venture studios, for their part, create start-ups by incubating their own ideas or ideas from their partners. The internal team can validate the product-market fit and estimate early customer traction, and recruit founders to launch and scale the start-up.[56]

Y Combinator in the US is one example of an accelerator that creates a supportive network for start-ups, including fintechs. It hosts two three-month programmes each year to help start-ups at different stages with funding, mentorship, and resources to rapidly develop their products and grow their businesses. Y Combinator itself invests in the selected start-ups in return for an equity stake.[57] Alumni, speakers and investors in the network provide guidance and resources to the founders (for example, help with public launches and first customer acquisitions).

By June 2021, some 15 years after it was founded, Y Combinator listed 2,830 companies among its alumni, with more than 80% of these still active, acquired or having gone public. In contrast, more than 80% of companies receiving traditional early-stage investments fail within 10 years.[58] By June 2023, it was estimated that 4.5% of the start-ups that had gone through Y Combinator since 2010 had grown to become billion-dollar companies, making Y Combinator one of the leading accelerators globally.[59]

3.4 Developing local financing capacity

Diversifying the investor base and access to debt financing

While VC funding has been instrumental in providing many fintechs with the capital and resources they need to grow, VC investments alone don't always meet the different financing needs of fintechs on their journey to scale. For many fintechs, access to debt financing in local currency is still challenging across several countries, and this financing could help them to scale operations at a lower cost of capital. Debt funding can provide valuable access to liquidity without diluting equity stakes or requiring "down rounds" – selling equity in a business at a lower price than in previous rounds.[60]

Venture debt that is designed specifically for early-stage, high-growth companies with VC backing can also act as a bridge between equity financing rounds.[61] The development of local or regional debt markets is critical to creating more complex financing structures and products, such as securitization and asset-based lending. The development of regional debt capital markets can also promote a more balanced capital structure, and improve asset and liability management and balance sheet efficiency.

Furthermore, fintech ecosystems could benefit from building a broader investor base that reaches beyond traditional VC funds to include corporate venture capital (CVC), minority equity investment from incumbent banks, sovereign wealth funds with growth equity expertise, and family offices. Corporate VC investments can bring operational and strategic know-how while providing access to new distribution channels, expanding to new markets and potentially opening doors to exit opportunities.[62] Family offices also play a significant role in this ecosystem, with their investments accounting for more than 10% of all start-up investment deals and contributing 32.5% of the capital invested worldwide in 2022.[63]

Furthermore, the development of a strong local limited partners (LPs) base is fundamental to fostering thriving, self-sustaining VC ecosystems in any region. Governments can also play an important role in fostering innovation by deploying policy instruments to boost effective investment returns and attract more capital from investors to fund various industries. For example, VC schemes in the United Kingdom offer tax relief to individuals to encourage investment into start-ups.[64] In 2023, the British government initiated a plan to encourage nine major pension funds to invest at least 5% of their assets in British start-ups and VC firms. It also opened a consultation to double the existing local government pension scheme allocations in private equity to 10%, potentially unlocking £75 billion in assets by 2030.[65]

3.5 Encouraging sustainable fintech growth strategies

Adapting to the future growth paradigm

Funding and deal activity have slowed since 2022, with fewer initial public offerings (IPOs) and a decline in new unicorn creation. The macro-environment remains challenging and uncertain. In this new environment, fintechs will need to evolve to survive and remain competitive – moving away from potential efforts to pursue growth at all costs and focusing instead on creating a clear pathway to profitability.

To succeed, fintechs should concentrate on core strategies driving sustainable growth. Implementing disciplined cost management mechanisms and operational adjustments is crucial for withstanding the new funding environment while remaining flexible and nimble. Optimizing growth requires ensuring strong and stable core business with a targeted and proven market fit before expanding. Research shows that companies that focus on their core business and have a strong home market are 1.6 times more likely to generate peer-beating returns.[66]

Strategic merger and acquisition (M&A) opportunities should be carefully evaluated with an emphasis on selecting the right partners and focusing on effective post-deal integration. Continuous innovation remains essential, particularly in adopting disruptive technologies such as AI across products and solutions. According to recent estimates, the deployment of AI across the banking sector could generate an annual value of $200-$340 billion, representing 9% to 15% of operating profits, mainly from increased productivity.[67]

By focusing on sustainable growth strategies and strategically leveraging technologies like AI, alongside demonstrating a clear path to profitability, fintechs can enhance their appeal to investors in a challenging macro-environment.

Conclusion

The fintech industry's expansion over the last 10 years has been a powerful catalyst for innovation, inclusion and growth in the financial services sector and the wider economy. From mobile wallets to banking-as-a-service to embedded finance, fintechs have pioneered new ways of delivering financial services that are accessible, affordable and attuned to users' digital expectations.

Venture capital plays a key role in enabling fintech innovation and has been an important driver of the industry's development. However, many fintech companies across regions still struggle to find the funding they need to grow and scale their activities. To better understand these needs and explore solutions, this report has examined VC funding flows and identified areas where gaps exist in funding fintech. Furthermore, this paper has outlined several pathways to creating an enabling environment to attract venture funding and support from other key stakeholders.

It is hoped that insights from this work will add value to ongoing efforts of public and private sector leaders looking to further develop an innovative and thriving fintech ecosystem, and that by addressing these funding gaps collectively, the fintech industry can reach its full potential.

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