The FinTech Movement

How Traditional Banking and Financial Services are Transforming Due to New Technologies and the Impact it has on Small Businesses

Business Impact Group's mission is to mobilize students towards the success of small businesses, social impact organizations, and non-profits across the nation. To contribute to their growth, Business Impact Group offers quarterly student consulting services and develops research reports on topics relevant to small businesses. Based at the Foster School of Business, Business Impact Group is made up of undergraduate students from across the University of Washington.

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Overview

FinTechs refer to companies which depend upon technology and cloud services to provide financial services to their clients with little to no reliance upon their physical locations[1]. FinTech has been experiencing a boom in recent years, especially during the onset of the digital age, albeit with a profusion of fluctuations. According to McKinsey, the total venture capital funding given to FinTech firms skyrocketed from **$19.4 billion in 2015 to $ 33.3 in 2020.**[1] Furthermore, it is predicted that the FinTech industry shall grow at almost three times the growth rate of the overall banking industry. However, the onset of the pandemic wore down independent FinTech companies as banks began to develop their platforms and services, which incorporate such technologies, with **73% of the world's interactions with banks now occurring via digital channels.**[1]

[1] McKinsey & Company. (2023, October 24). *FinTechs: A new paradigm of growth | McKinsey*. McKinsey & Company. https://www.mckinsey.com/industries/financial-services/our-insights/FinTechs-a-new-paradigm-of-growth

The Disruption of the Financial Landscape

Growth of the FinTech Industry

In recent years, FinTech companies have reshaped the financial landscape and challenged traditional banking models. **Digital payments are transforming financial transactions**, replacing conventional methods like cash and checks with mobile payments, online transactions, and contactless payment systems. This directly transforms traditional banking services, which rely heavily on older, more manual systems. Innovations such as Stripe, Visa, and MasterCard are at the forefront of this transformation. **They account for around 60% of market activity and are leading the shift towards a completely digital financial landscape.[2]** The FinTech market is expected to grow sixfold by 2030 — from $110 billion to $698 billion — signaling a significant transformation in financial services, with rapid innovations paving the way for a more efficient and convenient system.[3]

$110 billion	**$698 billion**
2024 FinTech market evaluation[3]	FinTech's expected market evaluation by 2030[3]

FinTech Growth Drivers: Cost-efficiency & Lending

A significant aspect that is propelling FinTech forward is its ability to be cost-efficient. Unlike traditional banks, which rely on physical branches and excessive bureaucratic processes, FinTech firms operate exclusively digitally. They utilize advanced technologies such as artificial intelligence and machine learning to streamline transactions and other processes, minimizing human error and lowering operational costs. **The efficiency of FinTech companies allows them to offer lower fees and**

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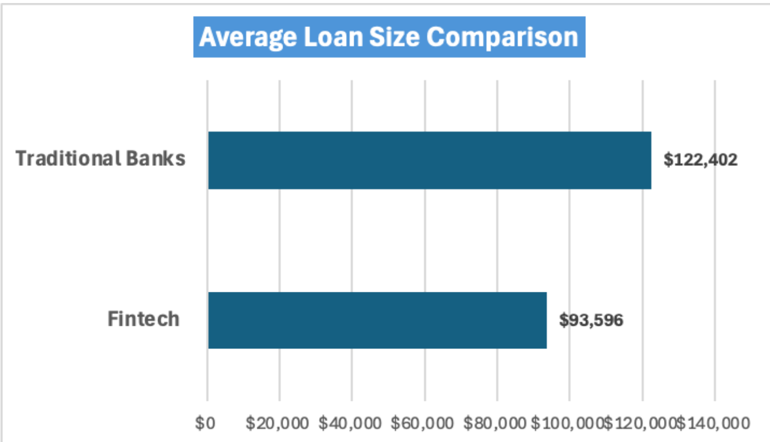
[2] Gupta, S., Ying Xie, & Zafar, H. (2024). FinTech and Digital Payments: Developing a Domain Knowledge Framework. Journal of Information Systems Education, 35(2), 189–202. https://doi.org/10.62273/HIGA9274

[3] Yuen, M. (2024, September 5). FinTech: What it is and what financial professionals need to know. EMARKETER. https://www.emarketer.com/insights/FinTech-ecosystem-report/#:~:text=FinTech%20companies%20harness%20technology%2C%20such,seamless%20alternatives%20to%20traditional%20banking.n

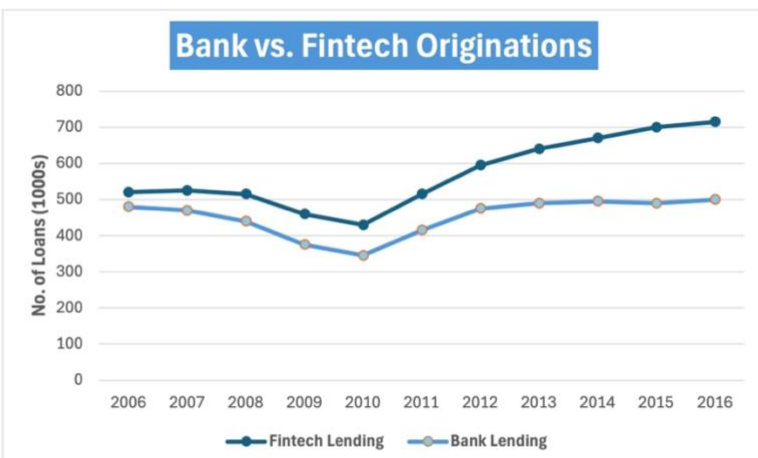
more attractive interest rates, making their services appealing to both consumers and businesses.[4]

FinTech firms often follow similar business models that focus on providing **smaller, short-term loans with flexible collateral options, making the process of acquiring loans less intimidating and accessible** for small businesses that do not meet the strict criteria of traditional banks. Data shows that the average loan size from FinTech lenders is about $93,596, smaller than the average $122,402 loan size from banks. These loans are often approved quickly – within days rather than weeks, offering a more attractive option to those needing capital quickly and flexibly.



Gopal, M., & Schnabl, P. (2022). Rise of Finance Companies and FinTech Lenders in Small Business Lending. Review of Financial Studies, 35(11), 4859–4901. https://doi.org/10.1093/rfs/hhac034

Moreover, UCC data illustrates that **FinTech lending increased by 100% between 2006 and 2016, whereas major banks saw a decline in their loan volumes during the same time period.[5]** This shift highlights the demand for FinTech lending and how FinTech firms have revolutionized the lending space.



Gopal, M., & Schnabl, P. (2022, June 13). *The rise of finance companies and FinTech lenders in small business lending*. OUP Academic. https://academic.oup.com/rfs/article/35/11/4859/6607597

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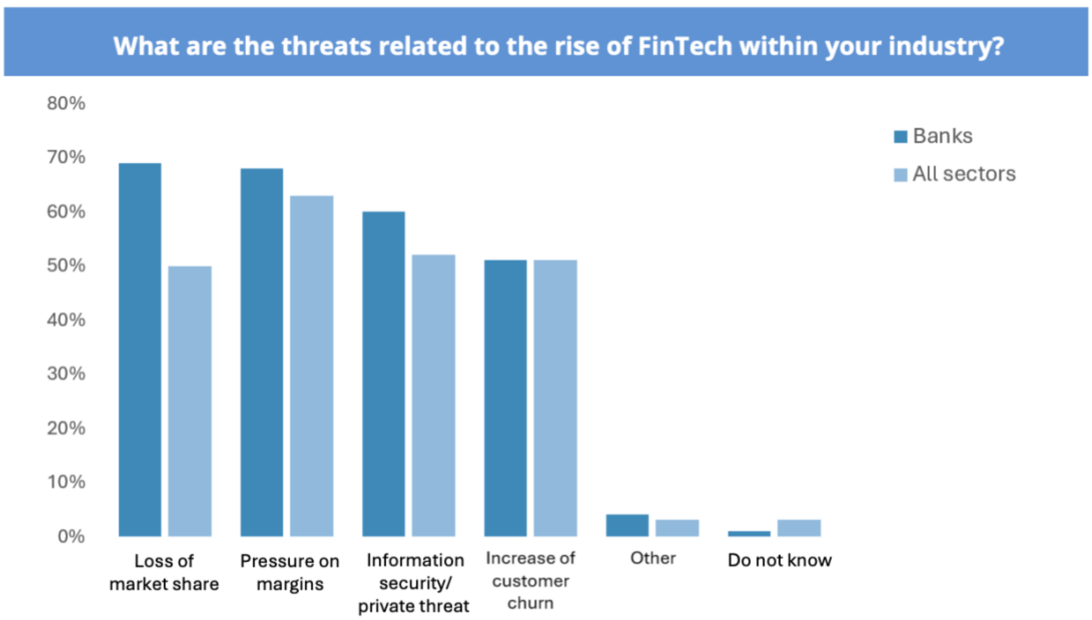
[4] Sharma, S. K., Ilavarasan, P. V., & Karanasios, S. (2024). Small businesses and FinTech: a systematic review and future directions. Electronic Commerce Research, 24(1), 535–575. https://doi.org/10.1007/s10660-023-09705-5

[5] Manasa Gopal, Philipp Schnabl, The Rise of Finance Companies and FinTech Lenders in Small Business Lending, The Review of Financial Studies, Volume 35, Issue 11, November 2022, Pages 4859–4901, https://doi.org/10.1093/rfs/hhac034

The Future of FinTech

Addressing the inefficiencies of traditional banks, FinTechs first emerged as "disruptors" within the financial services industry. Burdened by its stringent legacy systems, banks often struggle to compete with the agility and rapid innovation of FinTechs.[6] This is especially evident in the field of consumer banking, where 73% of financial sector executives believe it to be the most susceptible area for FinTech innovation.[7] As consumers switch to FinTechs due to their efficiency and lower-cost services, banks face threats to market share, pressure on margins, and customer churn.



PricewaterhouseCoopers. (n.d.). Customers in the spotlight: How FinTech is reshaping banking. PwC. https://www.pwc.com/gx/en/industries/financial-services/publications/FinTech-is-reshaping-banking.html

While FinTech companies and banks remain competitors, the relationship between the two has shifted towards "coopetition," a competition-cooperation hybrid[8]. FinTechs excel in innovation and a customer-centric approach but often lack the trust and

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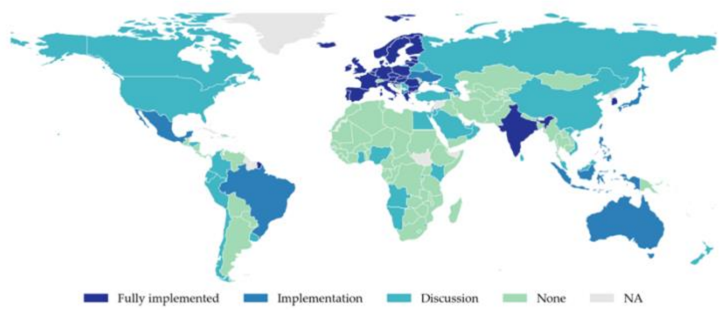
[6] The Future of Financial Services: Collaboration and competition between FinTechs and banks. (n.d.-b). https://www.finextra.com/blogposting/26275/the-future-of-financial-services-collaboration-and-competition-between-FinTechs-and-banks

[7] PricewaterhouseCoopers. (n.d.). *Customers in the spotlight: How FinTech is reshaping banking*. PwC. https://www.pwc.com/gx/en/industries/financial-services/publications/FinTech-is-reshaping-banking.html

[8] Cohen, G. (2024, August 13). *Council post: Banks vs. FINTECHS: The "coopetition" phase is here*. Forbes. https://www.forbes.com/councils/forbesbusinesscouncil/2023/07/14/banks-vs-FinTechs-the-coopetition-phase-is-here/

regulatory expertise banks possess.[9] Similarly, banks stand to benefit from modernizing their systems and adapting to digital trends. By leveraging each other's strengths, the financial services industry can deliver an overall better customer experience.

Key areas of collaboration include open banking, partnerships, and financial inclusion. Open banking is a framework that enables secure sharing of financial data across banks, FinTech companies, and third-party financial firms through Application Programming Interfaces (APIs).[10] By giving FinTech companies access to data traditionally held by banks, open banking accelerates the integration of more digital financial services and fosters collaboration. Proponents of open banking believe this approach increases the availability of financial services, as it provides consumers with a broad, dashboard-style view of their finances (Axway). Open banking allows banks and FinTech companies to focus on innovation and the creation of new product, benefitting the financial services industry as a whole.



Currently, open banking policies are implemented in countries like India and across Europe. However, the Consumer Financial Protection Bureau (CFPB) in the United States has issued open Banking rules that data providers must comply with starting in April 2026.[11]

Furthermore, digital innovations have blurred the lines between banks and FinTechs, making partnerships essential for enhancing competitive differentiation. Collaborations between banks and FinTechs enable both parties to focus on their strengths, resulting in superior solutions, streamlined processes, and enhanced value for customers.[12] For

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[9] The Future of Financial Services: Collaboration and competition between FinTechs and banks. (n.d.-b). https://www.finextra.com/blogposting/26275/the-future-of-financial-services-collaboration-and-competition-between-FinTechs-andbanks

[10] Team, T. I. (n.d.). *Open banking: Definition, how it works, and risks*. Investopedia. https://www.investopedia.com/terms/o/open-banking.asp

[11] *Open banking rules are finally here: What's next for the Financial Services Industry*. Holland & Hart LLP. (n.d.). https://www.hollandhart.com/open-banking-rules-are-finally-here-whats-next-for-the-financial-services-industry#:~:text=On%20October%2022%2C%202024%2C%20the,%2C%20security%2C%20and%20consent%20obligations.

[12] *Future of FinTech & Banking: Partnerships & Collaboration*. Bank of America. (n.d.). https://business.bofa.com/en-us/content/FinTech-and-bank-partnerships.html#:~:text=The%20partnership%20between%20banks%20and,optimize%20their%20own%20software%20solutions.

instance, partnerships between banks and FinTechs can significantly shorten implementation timelines. Historically, integrating data reporting into ERP or TMS systems would take four to five weeks. With FinTech partnerships, current-day or previous-day reporting can be reduced to just one week. Additionally, FinTech-driven automation reduces manual work for banks, allowing them to focus on strategic efforts.[12]

Although collaboration between FinTechs and banks creates a win-win scenario, multiple challenges must be addressed for success. FinTechs, often operating in less regulated environments, will need to adapt to the stringent requirements of traditional banks. Similarly, banks must integrate FinTech solutions without breaching their own regulatory standards. Furthermore, open banking and the sharing of information between FinTechs and banks raise concerns about data privacy and security. As customer data becomes more interconnected, the need for robust cybersecurity measures and strict regulatory compliance grows.

Ultimately, the future of FinTech and banks lies in their ability to collaborate effectively, prioritize customer needs, and navigate regulatory challenges.[13] As the industry moves toward a more hybrid system, collaboration between FinTechs and other financial institutions holds the potential to revolutionize how financial services are delivered.

FinTech's Global Market

Market Size and Growth Rates

In 2023, the global FinTech market was valued at USD 294.74 billion with the U.S. and North America holding the world's largest market.[14] Globally and within the U.S., banks held the largest market share (39-40%). In fact, 60% of credit unions and 49% of U.S. banks claim that partnering with FinTech companies is essential. With the rapid increase in digitization and, in turn, the growing emphasis on cybersecurity, countless banks

> *"FinTech is the focus and has been for this year and the past couple years as well. So, I expect that to continue as well. "*
>
> **Anna Butler**
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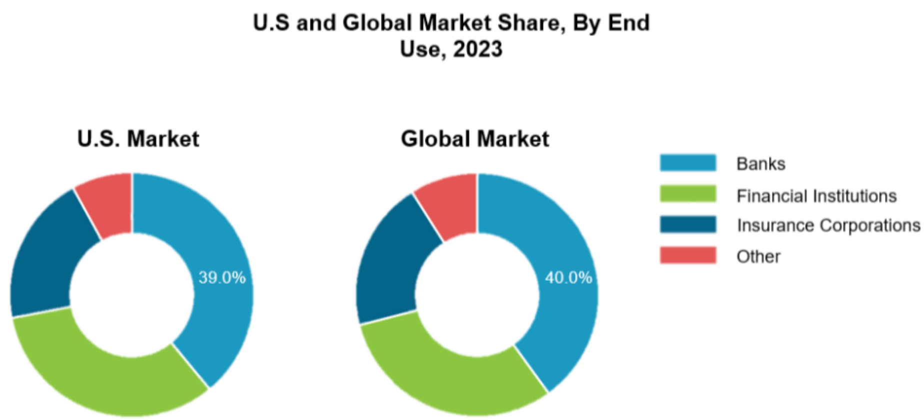
> PitchBook Sales Development Representative

[13] The Future of Financial Services: Collaboration and competition between FinTechs and banks. (n.d.-b). https://www.finextra.com/blogposting/26275/the-future-of-financial-services-collaboration-and-competition-between-FinTechs-and-banks

[14] Mordor Intelligence. (2024). *Global FinTech Market | Growth, Trends, and Forecast (2020 - 2025)*. Www.mordorintelligence.com. https://www.mordorintelligence.com/industry-reports/global-FinTech-market

partner with FinTech companies to ensure a smooth, reliable, and user-friendly experience.



"Global FinTech Market Size, Share & Trends Analysis, [2030]." Fortune Business Insights, 27 Oct. 2024, www.fortunebusinessinsights.com/FinTech-market-108641.

These partnerships also help to reduce manual work, allowing bank staff to allocate more time and effort towards strategic tasks. Largely contributing to this is the implementation of application programming interfaces (API). Using traditional banks' data, FinTech incorporates digital solutions to streamline processes such as onboarding customers to enhance the customer experience. Meg Garand, head of CashPro Payments and CashPro API at Bank of America, in an interview with PYMNTS, explained the value of API, noting that an entertainment company **reduced their time spent on monthly reconciliations from 10 days to two and a half through integrating CashPro API with their ERP system.**[15] Banks also partner with FinTech

90%

of survey respondents enjoy Apple Pay for its ease of use

88%

of survey respondents enjoy Apple Pay for the privacy it provides

[15] Future of FinTech & Banking: Partnerships & Collaboration. (2024). Bank of America. https://business.bofa.com/en-us/content/FinTech-and-bank-partnerships.html

companies to offer new options for payment, namely, digital payment. With phones becoming a necessity in people's daily lives, paying through their phones has become incredibly popular among users. In response to the large and still-growing demand, countless local stores, chain stores, and restaurants now offer digital payment as an option during checkout. With the large success of digital payment, large tech companies such as Apple and Google integrated FinTech services within their products and applications. **Particularly, Apple Pay has shown massive success and growth with more than 744 million active users, doubling their users in 2017.**[16]

In a survey conducted by Morning Consult, 90% of the survey respondents enjoy using Apple Pay for its ease of use and 88% enjoys the privacy it provides.[17]

> *"I think, in terms of innovation, [AI] probably will be the biggest—at least in the near future, 2025."*
> **Anna Butler**
> PitchBook Sales Development Representative

By the end of 2024, the global FinTech market is expected to follow the trend seen in 2023, projecting to increase to USD 340.10 billion. Furthermore, by 2032, the FinTech market is projected to reach USD 1,152.06 billion at a CAGR of 16.5%.[18] This rapid growth will be characterized by AI and the countless new opportunities it opens for companies. **AI is expected to grow at the highest CAGR (2024-2032) among FinTech Market technologies** (AI, blockchain, RPA, and others) due to its ability to save time and money for businesses, while also improving the customer experience. For example, AI elevates the customer experience by providing 24/7 customer support on websites. Doing so, mitigates the frequent issues customers run into, lowering the demand to speak to customer service employees. AI also helps detect financial fraud by monitoring and flagging suspicious activity, which helps aid market growth.

[16] Webster, K. (2024, October 22). *Apple Pay's 10-Year Journey and Its Next Decade of Decisions | PYMNTS.com*. PYMNTS.com. https://www.pymnts.com/apple-pay-tracker/2024/apple-pays-ten-year-journey-and-its-next-decade-of-decisions/
[17] Bailey, J. (2024, October 7). *Apple celebrates 10 years of Apple Pay*. Apple Newsroom . https://www.apple.com/newsroom/2024/10/apple-celebrates-10-years-of-apple-pay/
[18] Fortune Business Insight. (2023). *Global FinTech Market Size, Share & Trends Analysis, [2030]*. Www.fortunebusinessinsights.com. https://www.fortunebusinessinsights.com/FinTech-market-108641

Regional Trends

The two largest FinTech markets by country are the U.S. and China. As of 2024, the U.S. FinTech market values at USD 4 trillion, and China's FinTech market values at USD 3.54 trillion. As seen in the graph to the right,[19] Africa and China have the highest CAGR, however, due to the Asian Pacific (APAC) region's—including China and India, the largest FinTech markets in the APAC region—already high revenue pools, it is expected to surpass North America as the largest FinTech market by 2032.

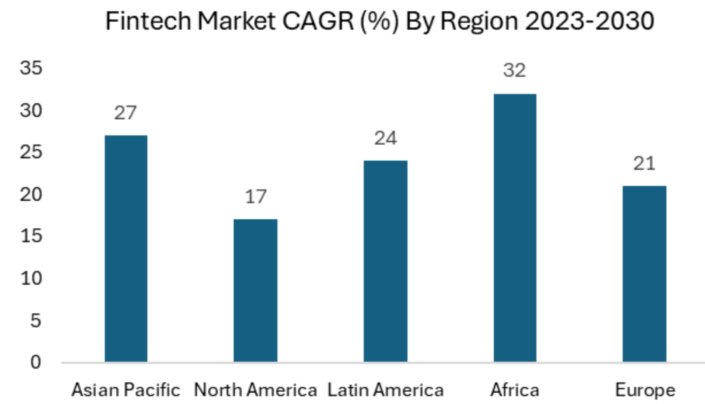


Figure 1 FinTech Market CAGR (%) By Region 2023-2030.

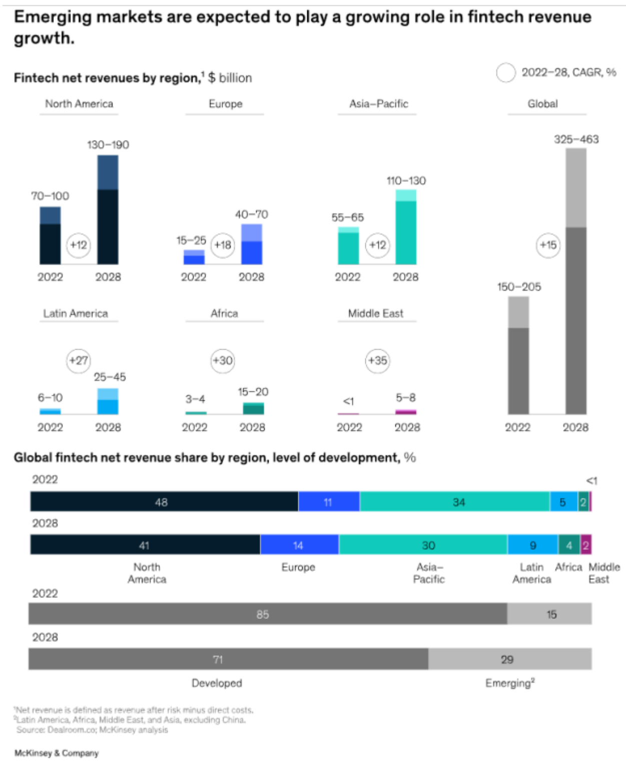
China has a more consolidated FinTech market than the U.S., with very large companies dominating the FinTech market. These companies include Ant Group (affiliated with Alibaba), Tencent (owner of WeChat Pay), Lufax Holding, ZhongAn, and Du Xiaoman Financial. These companies are highly trusted and favored by consumers. **In fact, almost 70% of consumers use WeChat Pay daily and 87% of the digitally active population use at least one FinTech service regularly.**[20] With China's massive population of 1.4 billion and large unbanked and middle-class population, it has grown to be the second largest market in FinTech, globally.

As opposed to China's consolidated FinTech market, the FinTech companies within the U.S. is more fragmented, with thousands of new start-ups appearing each year. However, it has many key players such as Klarna, Stripe, iTrustCapital, and Check. These companies have made great contributions in their respective niches. There has also been a rise of technology-based applications such as Apple and Google which have integrated financial services into their applications. Due to their access to the data of millions of users who use their applications, they have a large competitive advantage over their competitors.

Emerging markets such as China, play a large role in FinTech revenue growth. With the rise of digitalization and the increasing need for computers and phones, FinTech is

[19] FinTechnews Switzerland. (2023, May 4). European FinTech Sector Poised for Fivefold Growth by 2030. FinTech Schweiz Digital Finance News - FinTechNewsCH. https://FinTechnews.ch/FinTech/european-FinTech-sector-poised-for-fivefold-growth-by-2030/59978/

[20] Santosdiaz, R. (2024, September 11). *FinTech in China: Leading the Charge for Economic Progress in 2024*. The FinTech Times. https://theFinTechtimes.com/the-FinTech-landscape-of-china-in-2024/



2McKinsey & Company. (2023, October 24). FinTechs: A New Paradigm of Growth[1]

rapidly growing, especially in regions such as Africa, Latin America, and the Middle East.[1] One of the larger reasons for this is their high unbanked population. Due to the high unbanked population, many people rely on FinTech applications to pay bills and save and transfer money such as M-Pesa, one of the largest mobile banking services in Africa. This is also convenient for the growing middle class in these emerging markets. Due to their busy lifestyles, using FinTech applications to transfer money is highly convenient for them. Not only that, but apps such as Alipay and WeChat offer a variety of services that highly appeal to the middle class. In these apps, users can invest, buy tickets, use wealth management services, and many more services that help manage their wealth and disposable income.[21]

India's FinTech Market and Growth

The COVID-19 pandemic spurred an intense wave of **digital transformation in India**, pushing consumers and businesses to adopt digital financial services at unprecedented rates[20]. Consumers integrated digital payments, online investments, and virtual-only insurance into their lives, while small and medium enterprises (MSMEs) also embraced FinTech solutions to meet their distinct financial needs. India's digital economy is projected to soar to **$800 billion by 2030,** driven by the development of digital public infrastructure, advancements in the Unified Payments Interface (UPI), and the pandemic's digital acceleration.[22]

India's payment ecosystem is rapidly evolving, supported by widespread adoption of technology and continual innovation. The proliferation of digital payment

[21] *A guide to Alipay payments | Stripe*. (n.d.). Stripe.com. https://stripe.com/resources/more/alipay-an-in-depth-guide

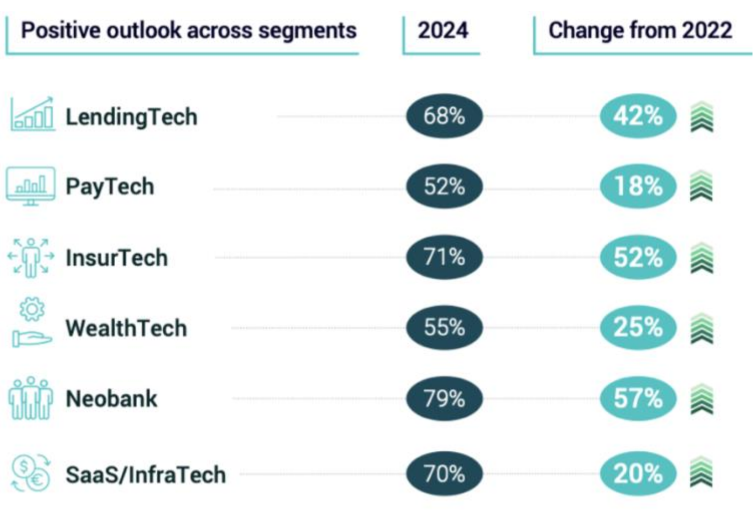
[22] Neetu Chitkara, Yashraj Erande, Vivek Mandhata (2024, August 27). *State of the FinTech Union 2024*. BCG Global. https://www.bcg.com/publications/2024/india-state-of-the-FinTech-union

solutions has led to a suite of secure, efficient, and accessible payment systems. As the landscape expands, FinTech companies have increasingly looked beyond transactional services to create additional value, including opportunities for monetization through diverse offerings that help bridge the profitability gap in the payments sector.

India's neobanking (digital-only banking services) sector has also grown significantly in recent years, fueled by global investor interest and a drive toward hyper-personalized financial product. The number of neobanking startups in India continues to rise, attracting funding as investors recognize the potential of these digital-first banks to transform traditional financial services.[20] The pandemic highlighted the value of neobanks, leading to increased investment and a heightened focus on customer-centric financial products.

Ecosystem banking is another trend shaping the Indian financial services landscape, where banks aim to provide seamless customer experiences and long-term value. By consolidating services traditionally offered through various disconnected applications, ecosystem banking enables a unified platform experience. Rather than developing complex in-house technologies, banks often choose to partner or purchase services, improving both cost-efficiency and customer satisfaction.

In the insurance sector, InsurTech in India has become a force for product and distribution innovation, drawing considerable investor interest. According to S&P Global Market Intelligence, InsurTech firms in India are beginning to move from supporting roles to competing directly with industry incumbents. Over the past few years, innovative business models in InsurTech have attracted steep funding, allowing the sector to expand rapidly and enhance its offerings to underserved demographics. The rise of alternative investment platforms has been notable as well. Historically, Indians



Neetu Chitkara, Yashraj Erande, Vivek Mandhata (2024, August 27). *State of the FinTech Union 2024*. BCG Global. https://www.bcg.com/publications/2024/india-state-of-the-FinTech-union preferred physical assets, real estate, and fixed deposits over capital markets. However, recent years have shown a shift, with a rapid increase in demat accounts as more people venture into equities.[1] During the pandemic, the number of demat accounts more than doubled, reflecting a newfound interest in alternative investment opportunities and signaling a shift toward broader market participation.

Regulation and compliance remain critical focal points for FinTech in India. As digital finance relies heavily on technology, ensuring compliance with data protection, governance, and fraud prevention regulations is essential. Despite advances, recent incidents related to insufficient KYC processes and governance gaps have prompted increased regulatory scrutiny. This growing focus underscores the need for robust compliance frameworks within FinTech companies, especially as they seek sustainable growth in the evolving financial landscape.

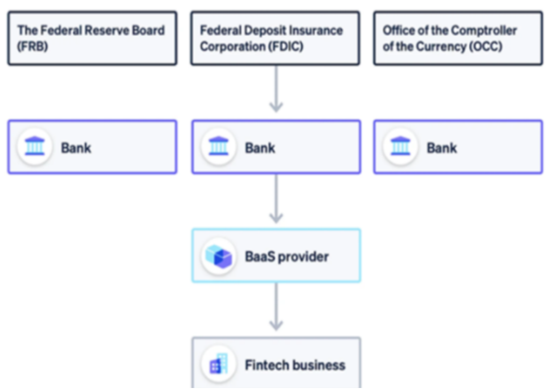
As the Reserve Bank of India (RBI) and National Payments Corporation of India (NPCI) steer the future of the Indian payments landscape, significant initiatives such as enabling credit on UPI and implementing card-on-file tokenization are anticipated to have a profound impact on the digital payments and credit domains. By enhancing customer data privacy and advancing open banking standards, the RBI and NPCI are helping shape a thriving, secure financial ecosystem. Meanwhile, the competitive private FinTech payments sector has seen key players emerge to develop robust financial service offerings aimed at long-term profitability. The impressive growth and innovation in the payments industry have propelled the Indian FinTech sector onto the global stage, with NPCI actively engaging in discussions with over 30 countries to expand the reach of RuPay and UPI internationally.[23]

[23] EY, C. (2024). *Seven key trends shaping the future of FinTech industry*. Ey.com. https://www.ey.com/en_in/insights/consulting/seven-key-trends-shaping-the-future-of-FinTech-industry

FinTech Regulations

Regulations in Washington State

In Washington state, FinTech companies involved in certain activities must adhere to specific legal requirements to ensure compliance and protect consumers. When offering or selling digital assets, such as through initial coin offerings (ICOs) or token sales, these assets may be classified as "securities." This classification triggers the need for registration with the Securities and Exchange Commission (SEC) and licensing as broker-dealers or advisers, depending on the nature of the offering.[7]



Overview of compliance fundamentals for FinTechs in the US. https://stripe.com/guides/overview-of-compliance-fundamentals-for-FinTechs-in-us

For those operating virtual currency kiosks or ATMs, Washington requires a state-level money transmitter license, particularly when these machines enable cash-to-crypto transactions or vice versa.[7] These operators must also meet Anti-Money Laundering (AML) and Know Your Customer (KYC) compliance standards to help prevent financial crimes.

Virtual currency exchange platforms that facilitate the buying, selling, or exchanging of cryptocurrencies may also be required to obtain a money transmitter license.[7] These platforms must adhere to both federal and state regulations, as the exchange of crypto assets is considered a financial transaction that requires consumer protection and anti-fraud measures.

Entities acting as virtual currency storage providers must also be licensed as money transmitters. Since they handle the custody of digital assets on behalf of others, these providers are responsible for securing users' assets against loss or theft, in line with state requirements.[24]

Finally, virtual currency payment processors—FinTech companies that process payments in cryptocurrencies on behalf of merchants—may need a money transmitter license if they facilitate the transfer of funds within crypto networks. This regulation

[24] *FinTech Licensing and Regulation Guidance.* (2024). FinTech Licensing and Regulation Guidance. https://dfi.wa.gov/FinTech/industry

applies to protect the integrity of financial transactions and align with money transmission laws in Washington.[25]

Privacy, Data, and Technology Regulations

The U.S. regulates personal data collection, use, and sharing at both federal and state levels. Key regulations impacting FinTech include the Federal Trade Commission Act (FTC Act), California Consumer Privacy Act (CCPA), and Gramm-Leach-Bliley Act (GLBA)[26] These rules set standards for safeguarding consumer financial information, with oversight varying by regulator (e.g., CFPB, SEC).[9] In 2024, Executive Order 14117 established data transfer restrictions to certain "countries of concern," targeting large-scale transfers of sensitive data to places like China and Russia.[26] Privacy laws also apply to foreign firms interacting with U.S. residents' data, regardless of jurisdiction, underscoring the need for FinTech companies to understand the various applicable state and federal data security and privacy laws. Sanctions for non-compliance may include fines, mandatory program adjustments, and potential lawsuits.

"When there's new regulations and people don't know how to navigate those, it makes investments in those sectors risky."

Anna Butler
PitchBook Sales Development Representative

The future of FinTechs: Risk and regulatory compliance. Deloitte United States. https://www2.deloitte.com/us/en/pages/regulatory/articles/future-of-FinTechs-risk-and-regulatory-

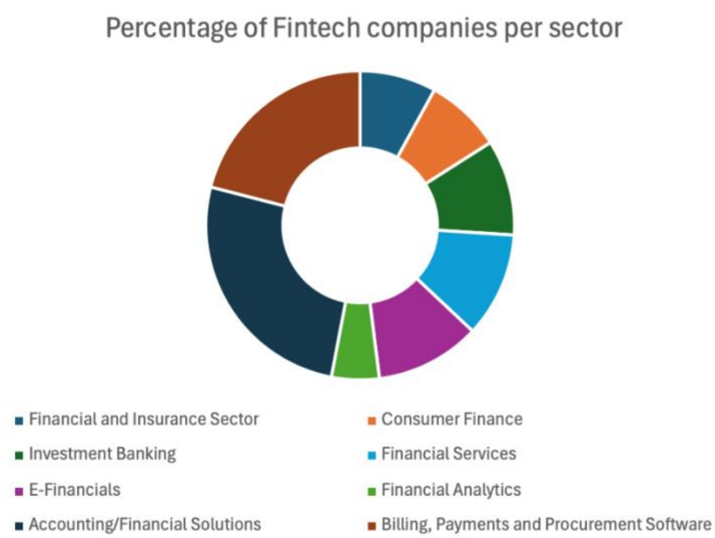
According to Deloitte, the changing relationship between banks and FinTech companies has meant that the regulations which were once applied to traditional banks may not

[25]Global Legal Insights. FinTech Laws & Regulations 2024 | USA. GLI. Published October 23, 2024. https://www.globallegalinsights.com/practice-areas/FinTech-laws-and-regulations/usa/
[26] Gutierrez FH, Finkel R, Smith TJ, Goldman Z. FinTech Laws and Regulations USA 2024. International Comparative Legal Guides International Business Reports. Published July 11, 2024. https://iclg.com/practice-areas/FinTech-laws-and-regulations/usa

necessarily apply to FinTech companies.[27] This discrepancy between FinTech companies and regulators has raised concerns surrounding their compliance with Anti-Money Laundering (AML) laws. The following information details the ways in which FinTechs are adapting to new regulations and the challenges which come with them.

Evolving Dynamics between FinTechs and Banks

Traditionally, FinTechs set themselves apart from banks by operating outside of the strict regulatory frameworks that govern traditional financial institutions. This allowed them to innovate quickly, connect deeply with customers, and respond to market changes with agility. However, the future may see blurred lines between FinTech and banking. Some FinTechs are pursuing bank charters to bypass state-specific regulations and compete on a broader scale, while banks are increasingly partnering with FinTechs to meet the expectations of tech-savvy consumers. Recent regulatory actions reveal increasing scrutiny on FinTechs, with issues spanning customer treatment, operational risk, and potential threats to financial stability. Since 2015, these actions have highlighted expectations for FinTechs to maintain the same standards of consumer protection, security, and risk management as banks, given that FinTech products often resemble traditional banking offerings.[28]



Overview of compliance fundamentals for FinTechs in the US. https://stripe.com/guides/overview-of-compliance-fundamentals-for-FinTechs-in-us

In 2016, the Office of the Comptroller of the Currency (OCC) promoted "responsible innovation," encouraging FinTechs to engage with regulators to address product-specific regulatory concerns. By 2017, FinTechs like Varo Money and SoFi had applied

[27] The future of FinTechs: Risk and regulatory compliance. Deloitte United States. https://www2.deloitte.com/us/en/pages/regulatory/articles/future-of-FinTechs-risk-and-regulatory-compliance.html

11. Goo, J. J., & Heo, J.-Y. (2020). The Impact of the Regulatory Sandbox on the FinTech Industry, with a Discussion on the Relation between Regulatory Sandboxes and Open Innovation. *Journal of Open Innovation: Technology, Market, and Complexity*, *6*(2), 43.https://www.sciencedirect.com/science/article/pii/S2199853122004383#s0015

for national bank charters, sparking debate about charter types and regulatory frameworks for FinTechs.[11] Internationally, the Financial Stability Board (FSB) has reported on FinTech's stability implications, identifying areas for regulatory focus despite no current systemic risks.

Future Trajectory and Stakeholder Confidence

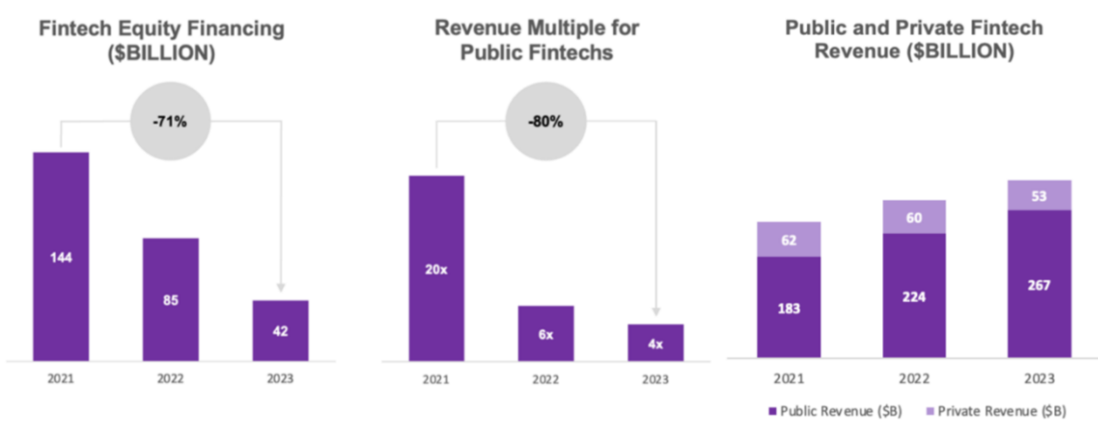
Whether through bank charters or continued independent operation, FinTechs must prioritize strong risk management and regulatory compliance to build public trust, enhance reputation, and potentially increase market share. This proactive approach benefits consumers, boards, analysts, and regulators, helping FinTechs navigate complex environments and turn regulatory compliance into a strategic advantage for sustainable growth.

It is worth noting that states like New York have laws which hold FinTech companies accountable for AML initiatives whereas states like Wyoming are invested in expanding the reach of FinTech companies by easing regulations. Washington has taken a via media of sorts without teetering towards extremities in policy.

The Investment Landscape

VC Funding and M&A Activity

In the first half of 2024, the FinTech investment landscape reflected cautious behavior among venture capital (VC) and private equity (PE) investors, influenced by economic headwinds and a volatile market environment. Compared to previous years, overall capital raised saw a downturn, with many investors opting to reinvest in existing portfolios rather than explore new startups.



Sources: Capital IQ; Pitchbook; companies' investor presentations; desktop research; BCG FinTech Control Tower; BCG analysis. *Average based on market capitalization and LTM revenue for the second quarter of each year.*

"Something that sets them apart is their ability to have knowledge about the financial market, and how it works in order for them to raise capital successfully."

Anna Butler, Pitchbook Sales Development Representative

Global FinTech investments **declined by 9.6% year-over-year** to $14.5 billion across 1,417 transactions, highlighting the ongoing pullback from riskier investments. Investors have shown a growing preference for sustainable and recurring revenue models, leading to an increase in funding directed towards the business-to-business (B2B) and business-to-consumer (B2C) FinTech segments. In contrast, direct-to-consumer (DTC) FinTech ventures have seen reduced deal volume as investors become more selective.

Within this cautious investment environment, several high-profile VC deals still garnered attention. Notable examples include Navro's $32.9 million Series A round, intended for product development and global expansion, and Nasdaq Private Market's $62.4 million Series B funding, aimed at enhancing secondary trading and liquidity services. The limited presence of larger deals reflects a broader hesitation from investors, who are prioritizing stability over growth amid geopolitical uncertainty and upcoming elections.[29]

Merger and acquisition (M&A) activity in FinTech also experienced moderation compared to the frenzied pace observed in 2021. Deal volume remained steady in terms of count, but valuations were subdued, with FinTech companies adjusting their growth expectations. Notably, payments and artificial intelligence (AI)-focused FinTech firms continued to attract significant interest due to their critical role in the financial services landscape. However, valuations across the board have adjusted, with public FinTech valuations showing considerable compression from their 2021 highs, as price to sale multiples for public FinTech firms declined from around 20x in 2021 to more sustainable levels by mid-2024.[30]

[29] Cbriggs@capstoneheadwaters.com. "Financial Technology M&A." *Capstone Partners*, 16 Apr. 2024, www.capstonepartners.com/insights/article-financial-technology-ma-update/.
[30] Goyal, Deepak, et al. "Global FinTech 2024: Prudence, Profits and Growth." *BCG Global*, BCG Global, 27 June 2024, www.bcg.com/publications/2024/global-FinTech-prudence-profits-and-growth.

"With the political climate as well there has been uncertainty, so investors tend to hold off on making decisions after big things like that pass over."

Anna Butler, Pitchbook Sales Development Representative

This period has been marked by a strategic shift among investors, who now favor more mature companies and infrastructure-focused FinTech firms. Despite the decline in revenue multiples, FinTechs have demonstrated robust revenue growth, averaging a compound annual growth rate (CAGR) of 14% across the industry, with standout performance in specific segments like challenger banks and lending. This growth indicates the sector's resilience, driven by a growing emphasis on profitability and sustainable business models over aggressive expansion, which characterized previous years.[31]

Case Study: Advent International's Acquisition of Nuvei

In April 2024, Advent International, a leading private equity firm, announced its acquisition of Nuvei, a global payments technology provider, for $6.3 billion. This landmark deal represents one of the largest M&A transactions in the FinTech sector during H1 2024, reflecting strategic shifts in investment priorities.

Nuvei specializes in next-generation payment solutions, offering businesses a comprehensive platform for processing digital payments, including e-commerce, business-to-business (B2B), and embedded payments. By 2023, Nuvei had processed over $200 billion in payments annually, positioning itself as a leader in the growing digital payments space.

[31] "Pulse of FinTech." *Biannual Analysis of Global FinTech Funding*, KPMG, Aug. 2024, kpmg.com/xx/en/what-we-do/industries/financial-services/pulse-of-FinTech.html.

The acquisition of Nuvei by Advent International presented a strategic opportunity to strengthen its position in high-growth verticals within the financial services sector. By acquiring Nuvei, Advent gained access to thriving areas such as embedded payments and global e-commerce. Nuvei's advanced technology and extensive customer base offered Advent a foothold in a lucrative and rapidly expanding segment of the financial services ecosystem.

One of the key drivers behind the acquisition was Nuvei's strong recurring revenue model. This feature aligned closely with Advent's strategy of investing in FinTech firms that deliver predictable and sustainable income streams. This approach reflects a broader industry trend, with investors increasingly favoring business-to-business (B2B) and business-to-consumer (B2C) FinTech models due to their stability and reliability when compared to direct-to-consumer (DTC) ventures.

Additionally, Nuvei's global operations presented Advent with significant opportunities to tap into the accelerating digitization of payments across multiple continents. The acquisition was expected to not only enhance Nuvei's presence in existing markets but also facilitate its expansion into new regions. This global reach, combined with the potential to broaden Nuvei's product portfolio, underscored the strategic value of the acquisition for Advent.

Advent's $6.3 billion offer represented a **56% premium** over Nuvei's closing stock price of $21.76 in March 2024. This premium highlights the enduring demand for FinTech firms with a proven track record and strategic growth potential, even amidst a broader decline in M&A valuations.

The Nuvei acquisition exemplifies the consolidation trend within the FinTech industry. As economic headwinds persist, private equity firms like Advent are doubling down on established players with scalable solutions and a strong market position. This deal also underscores the strategic importance of payments as a cornerstone of the financial technology ecosystem.[32]

Startups in FinTech

The FinTech startup landscape is characterized by rapid innovation and disruption across various financial services sectors. FinTech startups have significantly transformed areas such as payments, lending, wealth management, and insurance, leveraging technology to create streamlined and accessible financial products.

[32] Person. "Nuvei Goes Private in a $6.3B Deal with Advent International." *Nuvei*, 13 June 2024, www.nuvei.com/posts/nuvei-enters-into-agreement-to-be-taken-private-by-advent-international-alongside-existing-canadian-shareholders-philip-fayer-novacap-and-cdpq-at-a-price-of-us-34-00-per-share.

In payments, startups like Stripe, Toast, and Flywire have captured substantial market share from traditional incumbents by providing software-based payment solutions that prioritize user experience and flexibility. Similarly, the "buy now, pay later" (BNPL) model, championed by companies like Affirm and Klarna, has shifted consumer behavior away from traditional credit cards, highlighting the FinTech sector's influence on changing financial habits.

Beyond payments, startups are also driving changes in banking and finance through innovative consumer and business banking solutions, as well as open finance. Neobanks have provided a seamless entry point for customers, offering services like zero overdraft fees, which traditional banks have since begun to emulate. The shift towards open finance, where startups and traditional financial institutions collaborate to offer consumer-permissioned financial data sharing, is another area of significant growth. The Financial Data Exchange (FDX) initiative exemplifies this trend, with both disruptors and incumbents benefiting from data-driven financial services to enhance customer experiences.

While certain FinTech areas have already undergone profound disruption, others remain poised for future transformation. For example, segments like cryptocurrency, generative AI, and real-time payments have yet to fully realize their potential in reshaping the financial industry. These technologies represent the next wave of FinTech innovation, as companies explore their applications and scalability within financial services.

Despite the rise of disruptive startups, traditional financial institutions have demonstrated resilience, particularly in maintaining high levels of client assets and market capitalization. Top banks and brokerages have significantly expanded their market presence, with major acquisitions like Morgan Stanley's acquisition of E-Trade and Charles Schwab's purchase of TD Ameritrade illustrating the adaptive strategies of incumbents. These moves indicate that while FinTech startups lead in digital innovation, established players continue to secure their position in the financial ecosystem by adopting or acquiring emerging technologies.

Additionally, **AI adoption** within FinTech is expanding rapidly, with startups developing AI-driven solutions across various verticals. Predictive AI tools are becoming prevalent in payments, banking, insurance, and wealth management, providing more personalized services, enhancing operational efficiency, and improving risk management. Generative AI, while still emerging, is anticipated to further impact areas like customer service, fraud detection, and financial advisory services, as more startups explore its applications.[33]

Overall, FinTech startups are continuously reshaping the financial landscape, prompting traditional financial institutions to adapt while opening new avenues for consumer engagement and financial inclusion. With innovations ranging from AI-driven insights to new financial models, FinTech continues to expand its reach and relevance, driving a new era of digital-first financial services.

Case Study: Klarna & H&M

The B2B2C model, a hybrid of business-to-business (B2B) and business-to-consumer (B2C) approaches, leverages digitalization to create seamless customer experiences. This model involves partnerships where a B2B company collaborates with a B2C company to enhance the customer journey. A prime example is the partnership between Klarna, a Swedish FinTech firm, and H&M, a global fashion retailer. This collaboration highlights how such partnerships can streamline operations and deliver significant benefits to all stakeholders.

The Players: Klarna and H&M

H&M, a globally recognized B2C brand, operates over 5,000 stores in 74 countries, complemented by a thriving e-commerce platform. Klarna, a FinTech leader, provides online payment solutions that enable flexible payment options for e-commerce customers. Together, these two companies exemplify the potential of B2B2C partnerships.

The Partnership in Practice

H&M's customers often face scenarios where they prefer not to pay upfront or wish to pay only for items they keep. Klarna addresses this by offering a "pay later" option at checkout. Customers place orders through H&M's website but complete their payments through Klarna after receiving and reviewing their items. This arrangement empowers customers to shop with confidence and flexibility, paying only for what they decide to keep.

[33] "2024 State of FinTech Report." *State of FinTech 2024*, FinTechindex.fprimecapital.com/wp-content/uploads/2024/02/F-Prime-Capital-2024-State-of-FinTech-Report.pdf. Accessed Nov. 2024.

Benefits of the B2B2C Model

This collaboration brings mutual advantages for H&M, Klarna, and their customers. For H&M, the partnership reduces operational burdens by shifting payment follow-ups to Klarna, mitigating financial risks associated with delayed or missed payments.

For Klarna, the alliance provides access to H&M's vast customer base, boosting brand visibility. Additionally, Klarna avoids the costs associated with inventory management and logistics while gaining valuable customer data to refine its offerings and deliver more personalized experiences.

For customers, the arrangement offers flexibility and convenience, enabling them to shop confidently without upfront payment concerns, enhancing their overall experience.

Strategic Insights

This partnership not only improves operational efficiency but also influences customer perceptions. While customers recognize they are purchasing from H&M, their payment experience is closely tied to Klarna. Over time, this association may lead customers to view Klarna as an integral part of their online shopping experience, further solidifying its position in the e-commerce ecosystem.[34]

In summary, the Klarna-H&M partnership demonstrates the strengths of the B2B2C model. By combining their capabilities, both companies enhance the customer journey while achieving significant operational and strategic benefits. This case study underscores how FinTech innovations like Klarna can transform traditional retail and payment systems, paving the way for new opportunities in digital commerce.

FinTech's Impact on Customer Experience and Small Businesses

Customer Interactions with FinTech

Customers interact with FinTech through digital banking and payments, primarily through their phone and online platforms, which enhance ease, security, and speed. FinTech-driven mobile, online, and speed. FinTech-driven mobile apps empower transactions from anywhere, minimizing reliance on physical branches and reducing wait times. With instant access to account balance and transaction history, customers

[34] "B2B2C – What Is It and Why Is It Booming? A Klarna Case Study New." *Blastic*, www.blastic.com/blog/e-commerce/b2b2c-what-is-it-and-why-is-it-booming-a-klarna-case-study/. Accessed Nov. 2024.

can make better financial decisions on the go. FinTech apps have added advanced functions like round-up savings programs, which automatically save or invest extra change from purchases, in addition to standard banking services. Additionally, the rise of digital wallets and contactless payments highlights how FinTech has simplified everyday transactions. With apps like Apple Pay, Google Pay, etc., customers can tap their phones or smartwatches on the payment terminals.

Investing and trading platforms have made financial markets much more accessible to everyday investors, thanks to FinTech innovations. Robo-advisors, such as Wealthfront and Betterment, offer automated investment services that use algorithms to manage and enhance portfolios according to each client's risk tolerance, financial goals, and preferences. This approach makes it easier for beginners to invest without in-depth marketing knowledge. By lowering entry barriers, robo-advisors have empowered more people to participate in long-term investing and make informed financial decisions.

Financial education and coaching have become essential features in many FinTech platforms, aiming to enhance user's financial literacy and influence them to make better decisions. Many FinTech companies now have financial literacy tools directly into their apps, offering educational resources on budgeting, saving, investing, credit management, and overall economic health. These resources may include interactive tutorials, video content, articles, and quizzes that make learning more interactive[4] above[4].

Case Study: Recognise Bank and nCino's FinTech Solution for SME Banking

In 2017, Recognise Bank was founded by Jason Oakley, Bryce Glover, and Adrian Golumbina in response to the unmet financial needs of UK small and medium-sized enterprises (SMEs). Recognise aims to offer a relationship-led, digitally enabled banking experience tailored to the SME sector. The founders, however, saw a gap in UK SME banking where traditional banks often provided rigid, impersonal services. Recognise aimed to fill this gap in the UK SME banking market by combining relationship-driven services with innovative digital technology. To achieve this, the bank partnered with nCino, a cloud-based FinTech provider, to implement a digital banking solution tailored for SMEs. nCino's platform streamlined loan origination, automated data processing, and integrated customer relationship management (CRM), allowing Recognise to enhance client interactions and significantly reduce time-to-cash. By leveraging nCino's flexible, scalable system, Recognise was able to launch new products rapidly, improve regulatory compliance, and enable Relationship Managers to focus on client needs. This FinTech collaboration helped Recognise differentiate itself in a competitive market, combining the efficiency of digital services with personalized relationship banking.[35]

FinTech Innovations for Small Businesses

FinTech solutions such as mobile wallets and crowdfunding are changing the way small businesses are built and interact with their customers. These FinTech solutions are flexible and fast, allowing for increased financial stability and cash flow management for small businesses and entrepreneurs. Mobile wallets, for instance, enable customers to complete small transactions efficiently, increasing customer engagement and sales. Industry analysis suggests that using FinTech services will continue to boost sales through increased customer interaction, having a significant impact at the firm level.

Crowdfunding platforms are another key FinTech innovation and solution aimed at helping small businesses. These platforms break down the standard financial barriers that come with traditional banks, diversifying access to funding. Increased access to

[35] 2022, 21st January. (2022a, January 21). Case study: Recognise bank and nCino – digital solution for SME Bank. FinTech Futures. https://www.FinTechfutures.com/2022/01/case-study-recognise-bank-case-study/

capital encourages small businesses to explore various funding options and get their foot in the door. By breaking down entry barriers for new companies and offering tools that promote financial inclusion and independence, FinTech innovations allow small businesses to thrive in competitive markets alongside more significant, well-established companies.

Case Study: Photodom – Improving Small Business with FinTech

Photodom is a full-service camera shop and studio in Brooklyn founded by Dominick Lewis in 2020. Dominick launched his business to create a community to welcome photographers, especially those from an underrepresented community. Photodom provides services such as selling vintage cameras, films processing, and photography equipment.

To manage the daily operations nicely, Photodom uses Square's integrated product ecosystem, a FinTech platform that streamlines various business functions. This system makes it easier for staff management by improving scheduling, making appointment scheduling for seamless booking of studio sessions, and making quick and reliable payment processing for both in-store and online transactions. These tools have improved Photodom's operational efficiency, allowing them to dedicate more time to serving their community and advancing their mission. The flexibility and user-friendly design of Square's tools have been incredible in driving Photodom's success.

The business also gained traction through its crowdfunding campaigns which helped leverage its online store during the COVID-19 pandemic, demonstrating resilience and adaptability. Enabling the business to reach a broader audience while navigating challenges in the retail environment. Dominick's emphasis on the use of digital tools highlights how FinTech can empower small businesses to thrive despite challenges.

Photodom's story highlights the transformative role of FinTech in small business success. By simplifying operations, enhancing customer experiences, and supporting digital transitions, FinTech platforms like Square empower entrepreneurs to adapt and thrive. Photodom stands as an example to how combining technology with a strong mission can drive sustainable growth and meaningful impact, exemplifying how small businesses can leverage modern tools to overcome challenges and build a loyal customer base while staying true to their values[36].

Challenges of FinTech Adoption

Despite these advantages, customer interactions with FinTech can be slowed and looked down upon due to perceptions of FinTech as being too complicated, leading to “technostress.” While digital payment apps and mobile wallets offer convenient and simple solutions, some users may find these innovations to have a learning curve, making them hard to use, leading to stress and resistance. The idea of “technostress” refers to when users feel overwhelmed by the perceived complexity of new digital tools[37]. This is seen as a barrier to the adoption of FinTech. Addressing these concerns by simplifying interfaces and improving the customer experience is crucial for FinTech firms that aim to be leaders in the market.[38]

Conclusion

For small businesses, FinTech offers significant advantages such as quicker and easier access to capital, streamlined payment solutions, and boosting efficiency and customer engagement. However, challenges such as a learning curve for users leading to “technostress" and reliance on emerging, less regulated platforms remain obstacles. Balancing these aspects of FinTech is crucial for small businesses to fully take advantage of everything FinTech has to offer.

[36] Building the photodom brand and community with square: Square. The Bottom Line by Square. (2024, May 8). https://squareup.com/us/en/the-bottom-line/videos/photodom-brand-community

[37] Kim, K., & Park, H. (2018). The effects of technostress on information technology acceptance. Journal of Theoretical and Applied Information Technology, 96(24), 8300-8312.

[38] Sultan, A., Mubashar, A., & Um-e-Rubbab. (2024). Impact of Consumer and FinTech Characteristics on FinTech Resistance: A Study from User Perspective. NUML International Journal of Business & Management, 19(1). https://doi.org/10.52015/nijbm.v19i1.195

Meet the Research Team

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Agnes is studying Informatics with prior experience in business development and UI/UX design. She is interested in product management, consulting and entrepreneurship.

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Kayla intends to study Finance with experience in case competitions and graphic design. She is interested in pursuing consulting as a career.

Aarnav Mehta

Aarnav intends to major in Finance and has prior experience in working with private equity firms. He is passionate about consulting and intends to pursue it as a career.

Yumi Park

Yumi is studying Finance and Marketing with prior experience in entrepreneurship and product marketing. She is interested in consulting and brand management.

Amrinder Singh

Amrinder intends to major in Marketing and has prior experience in entrepreneurship and marketing. He is also interested in consulting and entrepreneurship.

Shragvi Sunil

Shragvi intends to major in Finance and Information Systems. She is interested in business and data analytics and has experience launching a small business.