Rialtas na hÉireann
Government of Ireland

Focus on International Financial Services & Fintech

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International Financial Services & Fintech

Description

The global market for internationally traded financial services is generally categorised as:

- Investment/asset management: including real estate, asset servicing/management, hedge funds, aircraft leasing[1] and private equity.
- Banking, capital markets and payments: including trading debt, funds, foreign exchanges, commodity and derivative instruments and non-bank payments.
- Insurance/reinsurance and pensions.

Fintech is a dynamic segment at the intersection of the financial services and technology sectors where technology-focused start-ups and new market entrants cause disruption to the traditional value chain with new forms of products and services. Products and activities include open banking, payment processing, cyber and information security, business analytics, dynamic currency conversion, P2P lending, crowdfunding, cross-border payments and cryptocurrencies, fraud detection, robo-underwriting, virtual advisors (chatbots), Digital Identity (KYC) solutions etc. The segment is characterised by a high degree of innovation and a short innovation cycle.

The Payments industry is undergoing significant disruption. It is a fast-growing and dynamic subsector made up of credit institutions, processing services, card networks, e-money institutions etc. that facilitate card, cash, paper and virtual payments through a variety of methods including in-store PoS technology, prepaid cards, mobile & eCommerce payments and closed loop payment networks.

Financial services is a regulated sector (although some aspects of payments and emerging fintech activities are not encompassed in the current regulatory regime). New business models, technology and disruption to traditional products and services has also seen a more challenging regime for regulation to keep pace with developments.

Regulatory requirements, the emergence of Paytech, Insuretech, Wealthtech and Regtech as new sectors, new entrants to markets which traditionally had high barriers to entry and the disappearance of intermediaries is resulting in increased competition, operating model pressure and a continuation of downward fee pressure on established IFS firms.

[1] Aircraft leasing is covered under the Aerospace and Aviation sector.

Snapshot

<table>
<tr><td rowspan="4">Global</td><td colspan="2"></td><td colspan="2">Market Size</td><td colspan="4">Growth Forecast</td></tr>
<tr><td colspan="2">Investment Banking and Brokerage [i]</td><td colspan="2" rowspan="3">Certain subsectors measured by size of funds managed, others by revenues</td><td colspan="4">CAGR 1.2% (2018-2023)</td></tr>
<tr><td colspan="2">Non-Life Insurance [ii]</td><td colspan="4">CAGR 3.85% (2017- 2022)</td></tr>
<tr><td colspan="2">Banking [iii]</td><td colspan="4">CAGR 5.1% (2018- 2023)</td></tr>
<tr><td rowspan="4">Ireland (Agency supported firms)</td><td></td><td>Exports (2018) [iv]</td><td>% of national exports (2018)</td><td>5-year CAGR of exports (2013-2018)</td><td>Employment (2019)[v]</td><td>% of national employment</td><td>5 -year CAGR of employment (2014-2019)</td><td>DEE [vi]</td></tr>
<tr><td>All Agency</td><td>€3.48bn</td><td>1.43%</td><td>13.93%</td><td>33,320</td><td>1.41%</td><td>5.76%</td><td>€1.53bn</td></tr>
<tr><td>Irish owned Enterprises</td><td>€1.26bn</td><td>0.52%</td><td>17.11%</td><td>4,555</td><td>0.19%</td><td>3.53%</td><td>€0.4bn</td></tr>
<tr><td>Foreign owned enterprises</td><td>€2.21bn</td><td>0.91%</td><td>12.33%</td><td>28,765</td><td>1.22%</td><td>6.14%%</td><td>€1.1bn</td></tr>
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i. Global Investment and Banking Brokerage, Marketline, January 2019
ii. Global Non-Life Insurance, Marketline, September 2018
iii. Global Banks, February 2019
iv. ABSEI 2018, DBEI.% national exports derived from using total exports from ABSEI 2018, €243.8bn.
v. AES 2019, DBEI. National percentages derived using CSO, LFS Q4 2019 figure of 2,361,200*Ireland for Finance* shows employment of 44,000
vi. Direct Economy Expenditure relates to total payroll costs, materials and services sourced from Irish suppliers

Pre-COVID-19 Position

Customer-centric approach, advances in technologies, new entrants and increased competition were significantly shaping the global financial services sector of the future

- Financial institutions are evolving from “product-driven” to “customer-centric”. Companies need to innovate for seamless integration, ease of use, 24/7 accessibility, personalisation by leveraging advances in technology and analytics to respond to changing customer needs and to improve customer experience.
- Advances in technology are enabling new business models and product offerings for all segments of financial services – including insurance (pay per use), regulation, crowd funding/peer-to-peer lending, blockchain, IoT, cloud computing, data analytics, machine learning and artificial intelligence – some of which are in response to the

collaborative/sharing economy that is premised on making better use of underutilised assets.

- Fintech companies are accelerating the digital transformation of the financial services ecosystem. Banks and financial institutions have been forced to modify their strategic plans by speeding up the launch of new digital products and services. Many of them are doing this through a cooperative approach with the fintech sector.
- The competitor landscape is fundamentally altered as new players enter the field including major players from other sectors, consolidations and restructuring continue apace. In the last few years, both Google and Facebook have been authorized by the CBI for Payments & E-Money licenses respectively as the lines between technology and financial services continue to blur. Traditional, established large-scale corporate structures are working hard to adapt to the fintech world in terms of agility, innovation, talent attraction and development. This has seen many take the route of acquisition to expedite their ability to keep pace with new competitors.
- With the high growth in digital/mobile services and apps, institutions are placing an increased emphasis on risk analysis and mitigation, data security, cyber security and information management. Companies must navigate complex regulatory requirements while balancing the demands of consumers for simplicity and ease of use.

Ireland is home to leading global financial services institutions and emerging technology-rich Irish enterprises

- Ireland is a globally-recognised centre for specialist IFS and is home to leading global financial services institutions and technology rich Irish enterprises serving every major economy in the world. The largest banks, asset managers and insurance firms are foreign owned and trading internationally from Ireland.
- The sector makes a significant contribution to the economy of an estimated €11 billion in exports, 6.3% of GDP, and €2 billion in tax receipts. [2]
- The industry encompasses front, middle and back office roles across a range of sub-sectors including asset management, international banking, insurance and reinsurance, funds servicing, fintech, and payments. Significant employment across these sectors includes technology development, engineering, customer support, IT, HR, finance and sales.
- Employment grew from 35,000 in 2015 to approx. 44,000 at the end of 2018. A 25% increase from 2015, representing 90% completion of the targeted 10,000 jobs by 2020.[3] 30% of employment is outside Dublin.
- Ireland is a primary location worldwide for Alternative Investment Funds with €4.7trn worth of assets under administration in Ireland - over 14,000 funds, and promoters from 50

[2] Ireland for Finance
[3] Ireland for Finance, Agency supported employment

countries.[4] The funds industry employs 16,000 FTEs in Ireland and contributes over €0.8 billion per annum in direct tax returns to the exchequer.[5]

- The Irish Insurance Industry employs over 15,000 people and holds €303 billion in assets in Ireland. The industry invests €35 billion in Irish infrastructure and debt and generates €32 billion premium income from domestic and international customers. Irish cross border insurance covers more than 100 countries with more than 25 million customers. 11 of the top 15 insurance companies are based in Ireland.
- 17 of the top 20 global banks have a presence in Ireland. These banks benefit from EU financial passporting which gives regulatory access to the EU single market. Major investment banks are also based in Ireland, including Bank of America Merrill Lynch, and JP Morgan and Barclays.
- Environment, Social and Governance (ESG) fund management is growing and Ireland already has a cluster of renewable energy infrastructure fund managers with €7 billion of assets under management. These include Blackrock, Brookfield Renewable, Greencoat Renewables, NTR, Infram Energy and Mainstream Renewable Capital.

Impact of COVID-19

GLOBAL

- The financial services sector is essential in supporting all other economic activities by stabilising markets and ensuring the flow of credit and payments. Central banks and financial regulators around the world have proactively intervened, showing commitment to using all possible measures with a view to stabilise markets, ensuring the flow of credit to households and firms as well as the continuity of payments, and facilitating the ability of financial institutions to absorb losses in an orderly manner.[6]
- Monetary authorities have been active and creative with different monetary instruments, including the lowering of key/base interest rates, quantitative easing, and the reduction of reserve requirements. Macroprudential measures have also been very varied and have included the reduction of counter-cyclical capital buffers, the easing of liquidity positions, the easing of loan-loss provisions, forbearance for non-performing loans, and relaxation of caps on banks' foreign currency forward positions.[7]
- The impact on general insurers will vary depending on the products and types of coverage offered by the insurers. The pandemic has taken a toll on new premiums on certain lines of business, such as travel, events, and trade credit insurance, and losses from these lines of

[4] https://www.irishfunds.ie/facts-figures
[5] Indecon assessment of Economic Impact of the Funds Industry on the Irish Economy, Irish Funds
[6] Trade in Services in the Context of COVID-19. World Trade Organization
[7] Trade in Services in the Context of COVID-19. World Trade Organization

business may become significant. Other lines of business such as motor and home have remained relatively stable.[8]

- Fintech businesses are likely to have some aspects of their business experiencing an uptick, and other aspects experiencing a downturn. For example, while the move to digital should have a positive impact for payments processors in terms of new customer acquisition; decreased consumer and business spending may mean an overall decrease in revenues. Similarly, while marketplace lenders may see an increase in demand for their products, as businesses and consumers seek to avail of alternative financing options; they are also likely to see an uptick in loan defaults.[9]

NATIONAL

- The financial services sector has appeared to be relatively stable in the face of COVID-19. The sector was considered an essential service from an early stage and the vast majority of companies are working very effectively from home since early March and continue to support customers and clients both nationally and globally. The flexibility and strength of the financial services workforce has been vital to companies' operations during these times.
- On the whole, Financial Services companies are better capitalised than in 2008; they have a diversified loan book and a more manageable credit risk exposure. CBI frameworks and systems created post the Banking Crisis have stood the test of time - as a result, the companies in Ireland have been coping very well with the crisis, continuing to support customers, often requiring major staff-redeployment and the use of capital reserves.
- The Financial and Insurance sector is one of the least affected sectors in terms of forecast for output. 2020 is forecast to reach 94% of pre-COVID-19 levels of output while 2021 will reach 93%.[10]
- Niche sectors have been exposed (e.g. aviation, lending, travel insurance) but most seem to have been relatively steady.[11] However, the broader economic situation may have far reaching impact in the medium-long term. As of mid-June, around 26% of those previously working in the Finance, Insurance and Real Estate are estimated to be on the PUP or TWSS, down from 2% prior to phase one.
- The initial stages of the crisis triggered a surge in business activity for many IDA Ireland IFS clients in Ireland, with market volatility and transaction volumes up. Companies have been working hard to support their clients with liquidity and other solutions as they reconfigured investment portfolios and reallocated assets.

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[8] (https://www2.deloitte.com/content/dam/Deloitte/ie/Documents/FinancialServices/Impact_of_COVID-19_on_the_Insurance_Sector.pdf, 2020)
[9] Covid-19 & the Future of Fintech. A&L Goodbody
[10] Davy Research: Irish Economy
[11] IDA Ireland

- Low valuations imply banks may find it difficult to raise capital through market issuance in the future, forcing them to reduce assets to maintain capital ratios.[12]
- Domestic institutions have introduced significant measures to support customers through the crisis, requiring major employee-redeployment and the use of capital reserves. For all financial services companies, the vast majority of employees – with the exception of frontline staff - are working from home and continue to support clients nationally and globally.[13]
- The financial position of the insurance sector is expected to be under pressure, due to falls in asset values, increases in measured liabilities due to the fall in risk-free rates and the impact of pandemic-related claims on profitability. That said, domestic insurance firms' solvency positions were above regulatory requirements as at 2020Q1.[14]
- While it is still too early to assess the medium-long term implications of COVID-19, an acceleration in the trend towards the use of digital technologies is apparent.
- Environmental, Social and Governance (ESG) has held up well so far, with an increased focus on the "S". Overall Sustainability, Credit and Private Equity are showing strong growth and opportunity.
- Fintechs have been quick to respond to consumer needs in a timely manner. However, the sudden onset of recession has closed some of the exit options for venture capital investors. Valuations based on unrealistic growth expectations will likely spark further acquisitions. Niche fintech subsectors, such as lending and consumer credit have been exposed to the pandemic; however, fintech's which received funding/investment prior to COVID-19 are well place to drive further growth. Overall, the pandemic is pushing the economy online at an accelerated rate, which offers a positive outlook overall, driven by consumer demand, technology advances and an ability to respond quickly.
- Enterprise Ireland note significant impact on Payments and FX businesses as a result of COVID-19.

Issues, Opportunities and Challenges for the Sector

- Resilience demonstrated by the sector throughout the pandemic presents a significant opportunity for Ireland to strengthen its competitiveness as a premier location to attract financial-services focused inward investment, introducing fresh capital and providing additional high-quality employment at a time when needed. By moving quickly and decisively, the financial services sector will be well positioned to secure global market share and bolster the national economy.
- Having managed the initial crisis, forward looking planning activities are now getting underway. Many global companies are looking at how to reconfigure their global operations

[12] Central Bank of Ireland: Financial Stability Review
[13] Ibec Reboot & Reimagine, 2020
[14] Central Bank of Ireland: Financial Stability Review

footprint - and we may see a move to build regional (geographic) hubs to build resilience, diversify operations support and position for future pandemics. A hybrid operating model may also come to the fore; with an increasing focus on remote working and/or work from home solutions. Moreover, reviews of outsourcing partnerships could drive companies to consider near shoring and/or onshoring of activities.

- Companies are also starting to work on reimagining their talent operating environment - what work is done, by whom, and where work gets done. We are likely to see increased focus on talent management, skills mapping and upskilling initiatives across global teams.
- Company revenues are likely to fall across many lines of business with a drop in economic activity, this will place increased operational cost pressure on the business (e.g. loan losses leading to increase in loss provisions); and operational cost will likely increase as companies pivot to digitise, manage claims and related litigation.
- The drive to technology advancement has become increasingly important – and we are seeing increased pressure to deliver technology projects not previously prioritized and/or fully integrated pre COVID-19. There is also an increased interest in automation projects, as companies seek to gain operational efficiencies and lower costs. New digital tools can help companies' lower costs, digitise client interactions and ultimately increase profitability. Moreover, exposure to fraud and technology outages will accelerate the shift to cloud and a focus on cyber security.
- Irish banks had higher levels of capital heading into the COVID-19 crisis than most European countries – putting them in a better position to absorb shock losses as defaults increase.[15] Financial Services Ireland (FSI) objective is that Ireland will be a top 20 global financial centre by 2025 with Ireland the strongest business environment and best location to tackle future challenges for the sector, the global centre for technology and financial services integration, innovation and leadership, a preeminent global location for diversity and culture, a global leader for talent and skills in financial services companies and a world-class location for sustainable finance.

[15] Central Bank of Ireland: Financial Stability Review