



Report

Fintech in Scotland

A Snapshot of 2020

A word from our CEO



2020 has been an unprecedented time for Scottish fintech. The sector has seen some major challenges and unique opportunities, while navigating a complex, changing, business environment.

While it's easy to talk about Covid-19 and its impact on the industry (and what an impact it was: funding was all but wiped out for the first quarter and best laid plans were derailed) that is only half of the story.

For all of the damage that Covid-19 has wrought, the fintech cluster is making the most of a terrible situation: finding new opportunities through increased collaboration, securing the future of its workforce and seeing a bounce back in venture capital funding.

In Fintech in Scotland: A Snapshot of 2020, we round up the biggest challenges the sector has faced this year, looking at a lack of funding, skills shortages and the impact of global markets and how those challenges have been turned into new opportunities.

We've drawn on some great reporting and thought-leadership to provide a snapshot that we hope will help act as an anchor as we move through the challenges of Covid-19 and the recession and into new opportunities.

If you'd like to talk more about the challenges facing Scotland's fintech community, feel free to get in touch.

A handwritten signature in black ink, reading "Euan Andrews".



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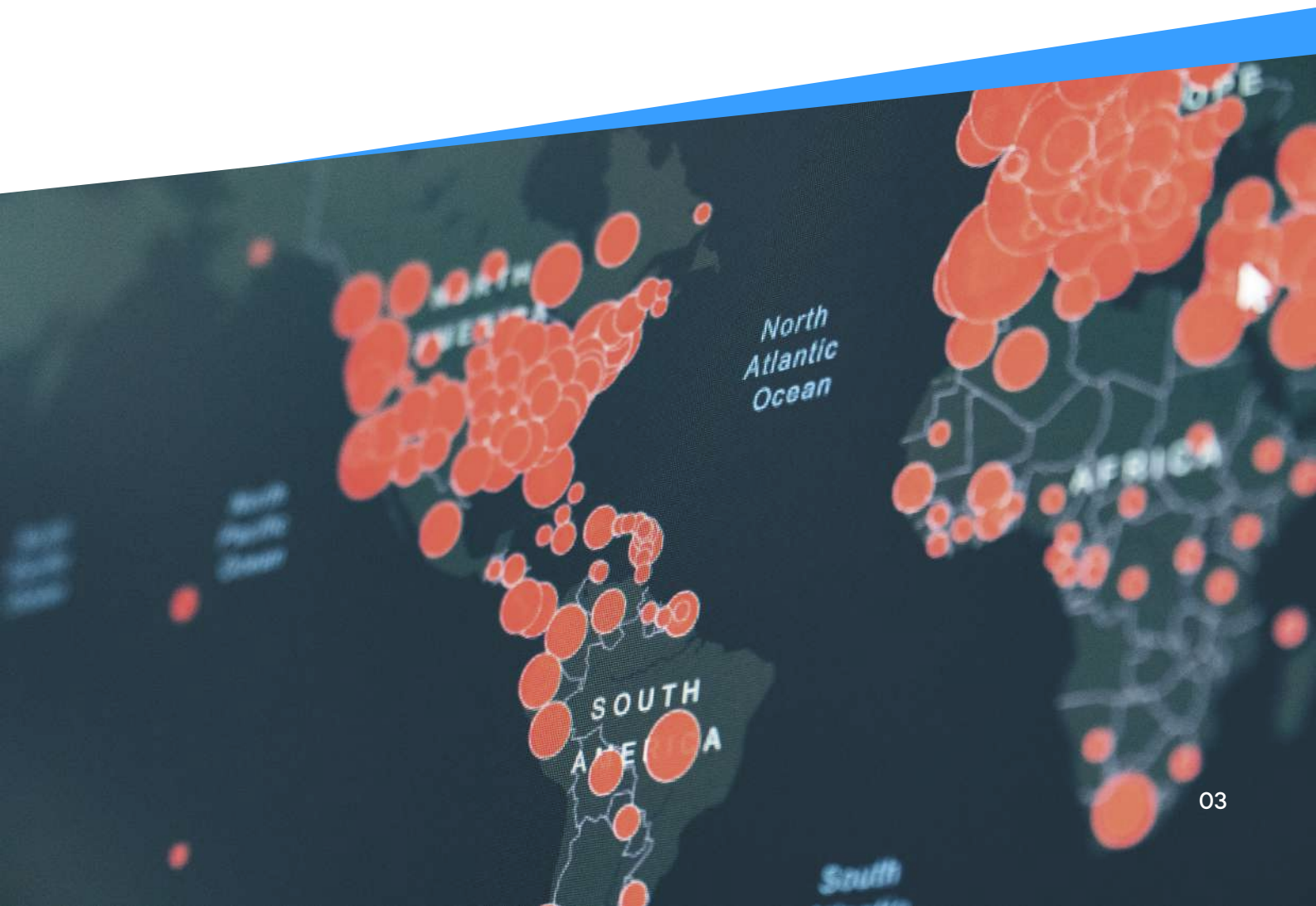
The Shape of 2020



This year has been one of challenges and curve balls that have caused fundamental shifts across the fintech space.

There have been some big challenges across cash flow, funding and the global markets but there are also some unique opportunities across the sector that will help reshape the Scottish economy.

In the first part of this roundup we tackle the impacts of those challenging global markets and look at some great reporting on the distribution of funding, its reallocation and the Q1 freeze.



The Impact of Global Markets on Scottish Fintech

As with all large-scale economic slumps, the challenges that are presented require a global and community level response. Part of this, as [Pinsent Masons reports](#), is businesses assessing and adjusting their finances, 2020 plans and strategies and the markets that they operate in.

This large scale reassessment of finances and market strategies comes down to the way global markets are responding to Covid-19 and the challenge of creating a unified response: some markets remain challenging, others are sealed off, and a few are open for business.

The challenge this poses for the Scottish fintech cluster is balancing global sales and growth strategies with customer needs and the rates that target markets are opening and ending Covid-19 related lockdowns.

The balancing act becomes clear when looking at [Eversheds Sutherland's report](#) on prevailing global trends and the potential for large scale missed opportunities as funding freezes. When this is combined with challenging markets and [a new customer readiness to switch to products that have less face-to-face time and a stronger digital presence](#) it's easy to see how big a shift this could be.

There is a view, globally, that investors are keeping their powder dry and any freeze in funding is only a temporary measure and fintechs, among other industries, are being temporarily bolstered by SME targeted stimulus packages.

The Challenges of Maintaining Cash flow and Funding

One of the impacts of Covid-19's on the Scottish fintech cluster is the similar downward trends on cash flow and funding, that have been seen across the global markets.

Experts believe that the industry is well equipped to weather the storm but that it will still be a monumental challenge as prospective customers turn away from challenger banks

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that are less equipped to provide support and towards more traditional financial institutions.

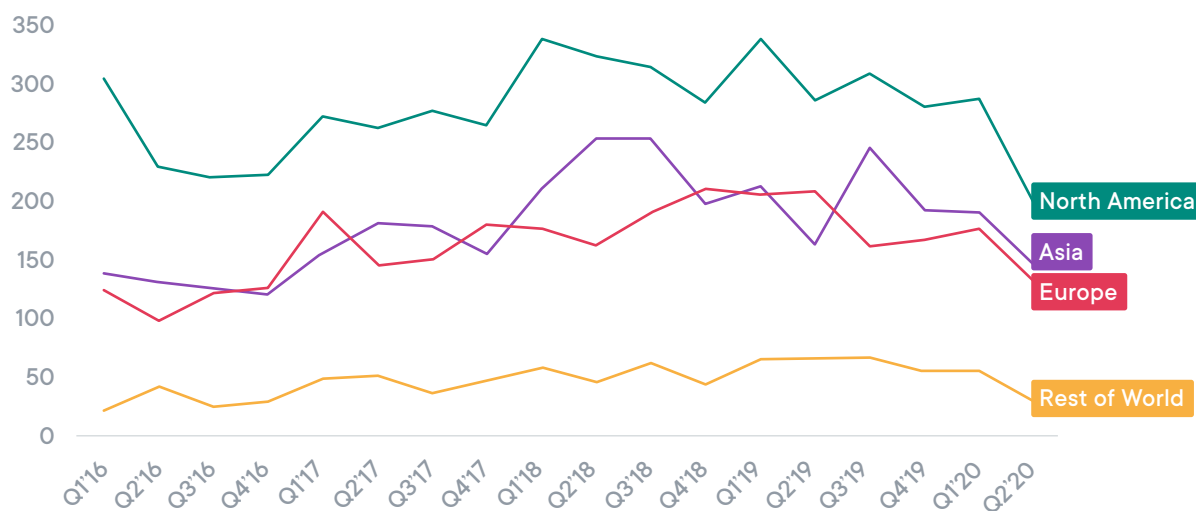
In fact, Law firm Womble Bond Dickinson [reports that the profitability of all financial institutions will be hit by the effects of the crisis](#), further reporting that many of its clients had been inundated with requests for repayment holidays and loan variations.

This is in line with [reports from Fintech Magazine](#) that VC backed funding for some sections of the fintech cluster has fallen quarter over quarter since the pandemic hit. This is in stark contrast to the global year-on-year growth that fintech funding saw from 2015 to 2018, where \$17.1bn quickly grew to more than \$40 billion.

This 180 degree shift has seen the future of Fintech change dramatically with [CB Insights reporting that funding decisions have undergone a rapid shift](#) and the pandemic has ended the thriving, rapid growth environment. This includes a 30% drop in funding for Q2 2020.

Fintech deals are falling across geographies

Global deals to FinTech companies by geography, Q1'16 - Q2'20.



Source: CBInsights

This could disproportionately impact smaller, early-stage, fintechs who are less likely to see funding as investors turn to larger, more mature companies with an eye on doubling down on existing, successful, investments. This began to play out in the second quarter of 2020, where early stage deals saw a crunch and mid-stage rounds saw an 8% increase in deal share.

What's next for Scottish Fintech?



Among the challenges of the global markets and funding and cash flow, it can seem like the industry is in dire straits.

However, [Scottish Development International reports](#) that the crisis has exemplified that Scottish fintechs are leading the way in helping with the economic recovery.

This has been backed up by a recent £22.5 million investment to establish a Global Open Finance Centre of Excellence in the Edinburgh and Central Belt region.

The new R&D centre will help encourage the development of innovation aimed at driving social and economic benefits through open banking and financial data.

The value of the new centre, alongside helping to create citizen-focussed financial services and helping policy makers understand the economic and social impact of policies, is that it will help bolster collaboration across the Scottish fintech sector.



The Need and Opportunity for Increased Collaboration

Increased collaboration across the sector will help businesses break down the silos they exist in and bring more value to their customers and the market.

However, before that collaboration can happen in a meaningful sense across the board, there are some frustrations that need to be worked through.

[Cap Gemini's World Fintech Report](#) says that frustration stems from a lack of agility, ROI, historical processes and not finding the right partner.

The report highlights that:

- Only 21% of banks say their systems are agile enough for collaboration
- Only 6% of banks have achieved the desired ROI from collaboration
- 70% of FinTechs don't culturally or organisationally see eye-to-eye with their bank partner
- More than 70% of FinTechs say they are frustrated with the incumbent's process barriers
- Half of FinTech executives say they have not found the right collaborative partner.

The shift of businesses and customers to a more digital first approach highlights the importance of removing these frustrations to build a stronger, more collaborative approach. In fact, the report goes so far as to say that traditional banks risk being left behind and could depend, in a disproportionate way, on collaboration with the fintech sector.

Specifically, the report highlights the need for banks to invest in middle and back-end operations that focus on building the customer experience and that the role of fintechs in the ecosystem needs to be evolved from serious competitors to formidable and important partners in order to achieve this.

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An important part of creating streamlined and effective collaboration is the [Open X Readiness Index](#), which evaluates banks based on 98 data points to check how ready they are for collaboration across the four pillars of People, Finance, Business and Technology.

Continued Growth Against the Odds

It's good news that, for all intents and purposes, the sector continues to be healthy and increased collaboration (inside and outside of the sector) will help promote growth and maturity in the cluster.

There has continued to be demonstrable growth and innovation in the cluster with [the number of fintechs in Scotland growing by 60% from 2019 to 2020](#).

Scotland's Fintech cluster employs more than 84,000 people and has seen a surge in growth from companies outside the UK relocating to Scotland - including startups from Australia, Hong Kong, Norway and the US. Generally speaking, clusters across all industries [employ on average 25% more people and pay them an average of 11% more than their counterparts outside of an economic cluster](#). They also grow faster than the mainstream economy.

The [Tech Nation 2020 report](#) found that the digital sector adds nearly £150 billion to the UK economy per year and its gross value grew almost six times faster than the rest of the UK economy.

Edinburgh alone saw a 67% increase in venture capital funding across the tech sector, with wider Scotland also getting its share of the £200 million of investment that came through the country in 2019.

The Scottish fintech cluster is home to a vibrant and internationally reaching community and uses its expertise and authority to create [international trade missions of fintech firms from Canada, Hong Kong, France, Switzerland, Singapore and the US](#).

The recognition is international with Scotland's fintech cluster being the first cluster in the UK (and only third in Europe) to be formally recognised by a [European accreditation body as a centre of excellence](#).

Continuing to Fund and Educate the Future Workforce

As opportunities continue to grow in the Fintech cluster in Scotland, it naturally encourages the best talent to head north.

The Fintech and financial services industries in Scotland account for an impressive 9% of GDP (worth £9 billion to the Scottish economy) and the most recent salary data for Scotland's tech workforce (2018) showed a median pay of £42,500.

All of this has helped build Edinburgh as the UK's largest financial centre (behind the City of London) and seen Scotland ranked the best performing destination for inward investment outside London for six consecutive years (2012-2018).

All of this, [combined with being home to the second highest concentration of Global Top 200 universities in the world](#), makes Scotland an incredibly attractive place for founders, tech workers and a vibrant community. In a European first, the University of Strathclyde was the first to launch an MSc in Fintech, a move that was quickly adopted by the Universities of Edinburgh and Glasgow.

The support of universities comes at a time where [75% of employers in tech are reporting skills shortages](#) and difficulties hiring qualified digital staff, where businesses that are not reporting shortages or skills gaps often find themselves [investing in staff training in order to keep up with emerging technology](#).

While the skills shortage means that Scotland isn't in the best position at the moment, the fintech cluster isn't being complacent. [Collaborations are already starting to happen](#) with Inoapps and CodeClan leading the way.

This new collaboration is in line with moves by The DataLab, Equate, the blockchain lab in Edinburgh University and the Fintech MSc at Stirling University, which aim to help make fintech and knowledge building opportunities available to everyone.

Looking Forward

2020 has been a challenging year for Scottish fintech but the UK remains the fintech capital of the world, according to the [UK Fintech State of the Nation report](#) [PDF] and venture capital funding has returned to Scotland with 22 deals completed between April and June ([worth £62 million](#)) while [the rest of the UK faced a 40% drop in VC funding](#).

While it's difficult to pinpoint what will come next in this constantly changing environment, the return of VC funding and historical data of the sector's resilience show that Scotland is well equipped to tackle the challenge.

What is clear is that education will also play a vital part in the future of Scottish Fintech, as universities continue to house innovation, businesses make it easier for people that are out of work to reskill and colleges and academies are able to equip students with skills they need to move straight into the fintech sector.

Get in touch.

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