

A descriptive approach of the FinTech sector development and its prospects for the remodelling of financial services

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Abstract:

The rapid development of the FinTech sector has accelerated the use of technology in the provision of financial services, thus reshaping the financial services industry. In developing countries, as is the case of Albania, the development of digital financial services has enabled access to financial services for the first time, especially for consumers not served by the banking system. The main purpose of the paper is to analyse the evolution of FinTech from the perspective of the financial sector. Following a methodology based on the combination of descriptive and explanatory data, through literature review and secondary data collected from existing studies and reports carried out by international and domestic institutions, this paper aims to provide evidence related to the expectations of the FinTech sector in creating new start-up businesses, exploring entrepreneurship among young people and encouraging the creation of new jobs. The research will include, in particular, aspects related to the effects of the FinTech sector in various areas of the financial sector, including business models, financial processes, payment methods, adaptation, challenges and recommendations. Through this research, it is intended to answer the questions: What are the indicators related to the current and potential demand for FinTech services in the Western Balkans and what do they show for the development of this sector? What are the expectations for the future of this sector, especially in Albania?

Keywords: FinTech, digitization, remodelling, financial services, start-up

INTRODUCTION

Digitization is becoming a rapid spreader of technology in every sector of a country's economy. In our daily life we hear more and more about digitalization in agriculture,

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digitalization in education, digitalization in tourism, digitalization of public services, etc. Such a development of technology and, moreover, adaptation to new trends, is increasingly influencing strategies and businesses, to gain a competitive advantage and to be flexible to the needs of customers. The Balkan Barometer study (2020) shows that 80% of managers in the Western Balkans consider digital skills very important for the development of their business and 55% of Western Balkan companies offer some form of training to improve the digital skills of their employees. The European Commission estimates that almost 90% of jobs in the near future will require digital rehabilitation. Digitization as a process takes on special importance for the opportunity it gives businesses to offer their services abroad. This rapid growth in demand for digital services has been supported by FinTech, as a natural solution in driving digital payments especially in the financial services industry.

Financial services enabled by technology are growing rapidly both through their use by banks and financial institutions. A recent study by Ernst & Young estimates that 64% of financial services consumers worldwide used a Fintech provider in 2019, up from 16% in 2015 (World Bank Group, 2020). The transformations offer consumers and micro and SME businesses improved service quality, product choice as well as increased access to finance and lower costs. Small and medium-sized enterprises located in rural areas, such as agritourism businesses, can especially benefit from the benefits of mobile payments, which enable them to pay, buy and get paid more easily. This simplifies cash flow, reduces costs and as a result increases profit while also increasing job creation opportunities. Furthermore, the FinTech sector is expected to create new start-ups, explore youth entrepreneurship and boost the creation of new jobs. Several other findings from the FinTech Jobs Report 2021 conducted by the Centre for Finance, Technology and Entrepreneurship (CFTE) reinforce the rapid growth of the FinTech sector. In the past decade, more than \$200 billion has been invested by venture and private equity funds in FinTech start-ups. Comparing FinTech start-ups to the banking sector, in 2010 the entire FinTech industry represented only 3% of the banking sector. Today, the FinTech sector is equal to 38% of the banking sector in terms of market capitalization. The 100 largest banks have a combined market capitalization of \$7.1 trillion, while the 100 largest FinTech companies have a combined market capitalization of \$2.8 trillion.

The global recession in 2020 has worsened the economic situation around the world. The lower income of the population, the increase in the rate of unemployment and financial insecurity will reduce the number and size of bank deposits and loans such as mortgage loans, car loans, etc. Traditional banks will be oriented by the FinTech sector. The inevitable digitization is not the only reason. Changes in the operating model, granting smaller loans and assessing customers less formally and improvements in the digital skills of the population are opportunities for FinTech institutions to strengthen their market performance in the coming years. There is moderate to high market concentration in the financial sector, which limits levels of competition and innovation. Banks in the Western Balkans, including Albania, tend to compete more on margins and interest rates than on the user experience that differentiates FinTech services. As the banks are mostly owned and headquartered outside of Albania, national branches may have difficulty developing innovative local solutions, due to their context within the structure of their banking group. There are a number of successful Bank-FinTech provider partnership schemes.

LITERATURE REVIEW

Financial technology or "FinTech" refers to the use of technology to provide financial services and solutions (Nicoletti, 2017). While according to Anyfantaki (2016), FinTech refers to technology start-ups that are emerging to compete with traditional banking and financial market players, offering several services, from mobile payment solutions and crowdfunding platforms to online portfolio management and international money transfers. Arner et. al (2015) point out that FinTech is not a natural new development for the financial services industry. In fact, according to them, FinTech simply refers to the application of technology in finance. According to Leong and Sung (2018), fintech can also be considered as "any innovative idea that improves financial services processes by proposing technological solutions according to different business situations".

The development of the financial services industry for years has been influenced by digitization in the distribution of financial products and services. Today, more and more people are talking about the concept of digital finance. Digital finance includes a number of new financial products, financial businesses, finance-related software and new forms of communication and interaction with customers offered by FinTech companies and innovative financial service providers (Gomber et. al, 2017).

The FinTech ecosystem consisting of FinTech start-ups, technology developers, governments, financial customers and traditional financial institutions was introduced by Lee and Shin (2018). FinTech covers a wide range of activities from data security to financial services that enable companies to automate their existing business structure and introduce innovative products and services (Nasir et.al. 2021). According to Imerman & Fabozzi (2020), the FinTech ecosystem can be categorized into 8 industry segments, namely:

- i. Payments and money transfers
- ii. Digital banking
- iii. Digital wealth managers, including robot-advisors
- iv. Capital markets innovations including algorithmic trading, high frequency traders.
- v. FinTech lending, including P2P (Peer-to-Peer) service and marketplace lenders
- vi. Crowdfunding
- vii. InsurTech, which refers to innovations in the insurance industry
- viii. PropTech, which refers to innovations in the real estate industry.

FinTech firms have the potential to displace traditional intermediaries by leveraging economies of scale in data analysis and offering financial services at lower cost to their customers compared to incumbents (Chemmanur et. Al, 2020).

Policymakers and regulators see fintech as an opportunity to make the financial system 'more efficient, effective and sustainable' (Carney, 2017). The development and application of FinTech helps more people, especially the poor, get lower-cost and more convenient financial services (Li & Xu, 2021). FinTech innovations promise to provide the poor with access to financial services such as payments, savings, loans and insurance. A total of 1.7 billion people worldwide, most of whom live in developing countries, are excluded from these basic financial services, hindering their ability to escape the clutches of poverty (Demirgüç-Kunt et al., 2018).

CURRENT AND POTENTIAL DEMAND FOR FINTECH SERVICES

The financial technology sector (FinTech) has been developing rapidly in the Western Balkans in recent years. This industry is likely to continue to strengthen its position in the market due to the challenges brought by the pandemic - as more institutions and businesses choose "digital only" services. Convenience and agility are the two competitive advantages of the FinTech industry, which are essential to weather today's economic uncertainties. Quarantine restrictions in Albania increased the use of remote services - from online shopping to delivery, entertainment and mobile payments. People accustomed to the advantages of the digital world are likely to continue to use it actively in the post-COVID-19 period. Digital financial services can easily help both: the final consumer and the institutions/companies. Fintech institutions through their payment services can effectively and efficiently connect entrepreneurs with banks, their employees, suppliers, as well as the entire market. Also, digital payment services provided by FinTech can help government organizations to respond to the needs of a specific group of individuals and small businesses, in a very short time. Despite the high growth in the use of cards and digital payments, there is still untapped potential in the Western Balkan countries for other services offered by the FinTech sector, which come from the increase in internet penetration and IT workers. However, in addition to the pandemic situation, other obstacles will continue not to favour the further development of this sector in our region, such as:

- Limited access to capital and finance
- High use of cash
- Lower access to payment technologies by the consumer,
- Regulatory aspects of the industry.

However, prolonged uncertainty will reduce the number of Fintech start-ups and in turn give momentum to companies capable of meeting the challenges. New players will find it difficult to catch up: limited access to capital will force them to close, leaving the industry to older/more experienced and stronger companies, who have capitalized on this situation to add more services to their portfolios, expand into new geographic markets and invest in their images.

DEMOGRAPHIC AND CULTURAL CHANGES

The Western Balkans region has recently seen growth in the use of FinTech services. Debit card ownership increased by 3% across the region between 2014 and 2017, while the number of people making online payments increased by 7%. However, in 2019 only 8% of the national population of the Western Balkans used online banking services, compared to 58% in the EU (INSTAT 2017, cited in World Bank, 2020). Moreover, account ownership currently remains low with a regional average of 61.3% compared to the Eurozone average of 95.3%. This is despite the fact that 80.3% of households in the Western Balkans (excluding Albania) have internet access and 98.8% SIM card penetration, of which 63% are 3G or 4G mobile broadband. Table 2 provides some key indicators of existing and potential use and demand for FinTech services for the Western Balkans. We can see that the level of internet access is increasing, as is the use of online banking, especially in North Macedonia.

Table 1: Indicators of potential demand for FinTech services

2019/2018	Level of internet access in households	Use of online banking (%)	Make purchase online	They don't shop online; concerns about payment security	Individuals with basic digital skills or beyond	Employed ICT specialists (,000)
Albania	/2019	/2	5	:	28/21	:
Bosnia and Herzegovina	72/69	5/5	23/18	5/:	24/:	:
Kosovo	93/93	5/1	30/22	1/9	28/21	:
North Macedonia	82/72	15/9	29/25	12/16	32/22	12/12
Serbia	80/73	18/15	34/35	6/9	46/39	68/64
Montenegro	74/72	3/2	16/12	15/21	4/50	5/5
Bulgaria	75/72	9/7	22/21	3/6	29/29	96/71
Croatia	86/83	47/41	49/41	14/20	49/50	109/156
Romania	84/81	8/7	23/20	3/8	31/29	199/185
EU 28	90/89	58/54	63/60	6/7	58/57	9000/8500

Source: Eurostat 2018 – 2019, cited in World Bank Group, 2020

On the other hand, in Albania, in 2020, according to the Bank of Albania, 60% of the population was considered without access to a bank. 38% of adults had at least one bank account; 6% of adults had at least one credit card and 7% of them make payments online, while 96% of all transactions are still done in cash.

However, since the pandemic situation, people are making more purchases online and have fewer concerns about the security of online payment systems. Regarding the use of ICT in Albanian enterprises, INSTAT provides the following data for the last three years.

During 2020:

- 27.6% of companies have increased the number of remote meetings conducted via Skype, Zoom, MS Teams, etc.
- 19.2% of enterprises have increased the number of employees who have remote access to the enterprise email system.
- 13.5% of enterprises have increased the number of employees who have remote access to enterprise ICT systems other than e-mail.

During 2021:

- 13.3% of enterprises have sold products/services through websites, dedicated applications, e-commerce sites and applications used by various enterprises to trade products.
- The largest share of e-commerce is occupied by enterprises operating in the field of information and communication with 32.2%, followed by accommodation and food service activities with 29.0% and administrative and support services with 26.1%.
- The use of customer relationship management (CRM) software was used by 24.8% of enterprises during 2021 from 22.5% that resulted in 2020.

During 2022:

- 13.8% of enterprises have sold products/services through the website, dedicated applications, e-commerce websites and applications used by various enterprises to trade products.
- The largest share of electronic commerce is occupied by enterprises operating in the field of information and communication with 31.6%, followed by accommodation and food service activities with 29.7% and professional, scientific and technical activities with 25%. 6%.
- 38.6% of enterprises conducted remote meetings using Skype, Zoom, MS Teams, WebEx, etc. and 42.0% of enterprises had remote access to the electronic mail system (email), enterprise documents or business applications or in enterprise software.

- 26.3% of enterprises have specialists in the ICT field whose main task is to develop, operate or maintain ICT systems and applications of the enterprise.

The future looks promising in Albania, due to demographic and cultural changes. The so-called millennial generation can definitely be considered 'digitally' native, as this generation has grown up with digital technologies as the norm, bringing a new psychology and perspective regarding financial services; products and services across all sectors must be mobile-first, delivered using digital channels and personalized for the end user. FinTech truly embodies this demographic and cultural shift in the field of financial services (World Bank, 2020). Making financial services available and affordable to the public can lead to increased activity and economic growth. Research has shown that platforms that are easily accessible to everyone, regardless of their income, and tightly integrated into the financial fabric of society, pave the way for inclusive and accelerated growth. FinTech companies that want to provide electronic money transfers and alternative physical payment methods in real time can push the economy forward, which affects the creation of new job opportunities and financial inclusion. It is expected that this will have a direct effect on reducing the informal economy, increasing e-commerce activities and reducing cases of fraud.

CONCLUSIONS

FinTech is transforming the world of finance at a progressive pace by increasingly using newer technologies. More and more digital services are being developed every day, which have gradually changed customer behaviour and replaced traditional business models. These services have been applied in various industries, especially in the financial sector. Utilizing the advancement of technology, FinTech has facilitated the use of various financial services, for a wide range of users and at a lower cost. This technology sector, despite being recently developed, has created a solid ground for building financial products and services and their future remodelling. This development has clearly resulted in significant challenges for the traditional banking and payment system; however, at the same time it significantly increases the flexibility and use of financial services.

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