Opportunities in the rapidly expanding Spanish fintech sector

Market Report

NEW ZEALAND FOREIGN AFFAIRS & TRADE
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Prepared by the New Zealand Embassy in Madrid.

Summary

- The term 'fintech' is short-hand for financial technology, and refers to a wide variety of technology used to enhance, streamline, digitize or disrupt existing financial services.
- The Spanish fintech industry has grown steadily over recent years, both in terms of the number of players (475) and the level of investment attracted (€600 million over 2020-2021);
- Spanish fintechs cover all categories and services. Although the bulk of activity has traditionally revolved around the lending and payment segments, wealthtech and neobanks/challenger banks are currently two of the fastest growing verticals.
- Despite the solid ongoing growth of fintech in Spain, the industry is a late starter and still relatively undeveloped compared to other big European fintech powerhouses when it comes to company size, revenues and product pipeline.
- Business opportunities for New Zealand companies and investors lie mostly in partnerships with banks and enterprises to support ongoing digital transformation efforts.

Report

Spain´s fintech ecosystem has developed significantly in recent years. The lack of an official register, the rapidly evolving nature of the sector and frequent overlap between clusters make it difficult to compile accurate statistics on the exact size and composition of the market.

However, the latest map released by specialist consulting firm Finnovating showed 475 fintech companies operative in Spain as of last May – approximately 15% of the EU´s total fintech population. The industry employs around 10,000 workers and 80% of fintech activity is concentrated in five main business segments: wealthtech (28%), lending (20%), payments (14%), invoicing/accounting solutions (9%) and financial infrastructure (9%). Less developed verticals include financial product distribution (6%), currencies (6%), equity finance (4%), neobanks/challenger banks (3%) and trade finance (1%).

Spanish fintech market at a glance

The number of fintechs has increased six-fold since 2015, positioning Spain as the sixth-largest global market in terms of fintechs per capita. According to a recent study by EY, Spain ranks 21st globally in consumer fintech adoption rates (56%) and 7th in Europe, behind European powerhouses like The Netherlands (73%) or the UK (71%), but ahead of Italy (51%), Belgium (42%) or France (35%). Several factors have contributed to this expansion.

Both conventional financial institutions and small businesses are speeding up their digital transformation, investing heavily in new technologies aimed at reducing overall costs and improving operational efficiency.

The EU´s revised payment services directive (PSD2), transposed into Spanish law in 2019, is likewise playing a key role, putting greater pressure on incumbent banks to become more agile. Similarly, the recently implemented regulatory sandbox (see paragraphs 12-16 below) is allowing new and existing fintech firms, as well as other interested stakeholders, to test their innovations in a more relaxed regulatory environment.

Growth continues to be driven largely by the lending, payments and invoicing/accounting solutions clusters. However, wealthtech is currently the fastest developing category due to global trends such as the rise in cryptocurrencies, the maturation of the personal finance management app (PFM) and virtual financial advice markets, and the emergence of new B2B digital solutions that are transforming wealth management and private banking.

Equally, despite representing only a small portion of the industry, neobanks and challenger banks are also gaining a foothold in Spain, mainly on the back of millennial and Gen Z consumers. Four companies (British-based neobank Revolut, German digital lender N26, and Spanish challengers Rebellion Pay and Bnext) already have a combined 30% market share of the domestic digital banking market.

Madrid (50%) and Barcelona (25%) are the major fintech hubs, accounting together for 75% of all fintech businesses in the country. They are followed at some distance by Valencia (8%).

Madrid has been actively promoting a more fintech-friendly environment for some time now, as evidenced by initiatives such as Crypto Plaza (self-billed as the largest crypto hub in southern Europe) or MADFinTech, a private non-profit association established with the support of the Madrid city council to encourage the development of the local fintech ecosystem.

Other cities like Malaga, Bilbao or Zaragoza are likewise taking steps to bolster technological progress and financial innovation.

Within the Spanish startup scene, fintechs are seeing some of the fastest growth in terms of investment. The industry has witnessed 300+ deals worth €600m over the past two years - €400m in 2021 alone. While this represents under 2% of total fintech investment in Europe last year (€21.4 billion) and is low compared to European peers like the UK (€10.2bn), Germany (€3.9bn), France (€2bn), Sweden (€1.5bn) or The Netherlands (€1.4bn), it is nonetheless indicative of a growing investor appetite in the Spanish fintech sector, both from national and foreign investor groups.

The average amount of funding per round is about €5m. Although a large number of fintechs are still at a relatively early stage of development, and typically resort to seed or early-stage financing (i.e. Series A financing), it is becoming increasingly common for local companies to draw larger amounts of investment in Series B and C rounds.

Traditional financial entities are leading the charge. As in most countries, Spanish banks´ initial negative views of fintechs as pure competitors have softened substantially and bank-fintech relations have become more collaborative over time.

Numerous Spanish banks have well-established fintech incubation and acceleration programmes, and consistently invest in both local and international fintech startups through their venture capital arms. Spanish banks hold stakes in fintechs that reach an estimated combined value of €65bn.

Spain´s second biggest bank, Santander, for instance, has various unicorns in its portfolio (Upgrade, Ripple or Ebury), as well as future unicorns like Curve or TrueLayer. All its investments are channeled through its €350m London-based VC fund Mouro Capital.

Similarly, BBVA, the third largest bank, has an independent €400m VC run from San Francisco, Propel, and a portfolio that includes unicorns such as Coinbase, Solarisbank or SumUp. Meanwhile, smaller banks like Sabadell or Bankinter tend to invest more in smaller, up-and-coming domestic fintechs.

Homegrown success stories

Bizum, an instant mobile payment service launched by various Spanish banks in 2016 to offset growing competition from big tech companies (e.g. Apple Pay, Google Pay, Amazon Pay, Samsung Pay, PayPal), is one of the clearest examples of the benefits that practical cooperation between banks and fintechs can bring for consumers.

In its short lifetime, Bizum has become by far the most widespread P2P payment system in Spain: 19 million users – 40% of the total population - and 800m transactions worth €40bn by the end of 2021.

It is especially popular among the 25-44 age group, though also used increasingly by older cohorts, particularly since the start of the pandemic. Its success can be explained by its security, convenience and speed.

Customers can make payments from one bank account to another simply by knowing the recipient´s phone number, without additional details like IBAN or SWIFT codes. The money is received immediately, within seconds.

Initially designed only to cover mobile payments, the bank-owned service has added new features including donations to NGOs, B2C payments and e-commerce payments.

It is considered a reliable, safe payment method because it is built into the websites of the 30 banks that currently offer the service. Worth an estimated €55m, Bizum is reportedly developing its own app and it intends to focus on continuing to grow its customer base and expanding its e-commerce payment portfolio.

Pagatelia is a leading Madrid-based fintech founded in 2010 that specialises in electronic toll services for individuals and enterprises. It is known for having developed Via-T mobe, the first non-banking electronic toll collection device based on Radio Frequency Identification (RFID) that allows contactless payments on all motorways and in 350+ car parks in Spain, Portugal, France and Italy.

The device is small, easy to install on PCs, tablets or smartphones, and offers exclusive advantages for customers like toll discounts, lane preferences, invoice download, online tickets and automatic number-plate recognition.

Among the best-known domestic players in the wealthtech space is Fintonic, a mobile-centric consumer banking platform established in 2012 that provides insurance and investment products, and targeted loans. Valued at €160m, Fintonic initially operated as a financial aggregator, developing a PFM app to help clients improve their financial literacy and cultivate better spending habits.

Since obtaining clearance from the Bank of Spain to simultaneously provide payment initiation and account aggregation services regulated by PSD2, it now also offers the possibility of opening an account and obtaining a debit card with them. Fintonic claims to have over 1 million users and is currently available in Spain, Chile and Mexico.

Growing international interest

Spain is also becoming increasingly attractive for overseas fintech businesses. Numerous household names across multiple verticals, including U.S. behemoths PayPal and Stripe, or Dutch payment unicorn Adyen, already have an established presence. Swedish buy now, pay later giant Klarna entered the Spanish market in 2020 and has confirmed plans to open a technology hub in Madrid, staffed with a 500-strong team of engineers and other high-skilled professionals, to expand operations in southern Europe.

Other fintech unicorns with a growing footprint include British startups Revolut and Checkout.com, German neobank N26, and Brazilian lending platform Creditas. American digital payments giant Square (recently rebranded as Block) has just started operating this year, primarily targeting small and medium-sized enterprises.

Spain´s good climate, wide talent pool and competitive salaries compared to northern European nations are among the key reasons behind this increased interest.

Enter Sandbox

In 2020, the government adopted a law for the digital transformation of the financial system, one of whose main strands was the establishment of a regulatory sandbox. The legislation was a long-standing industry demand. However, it was delayed considerably due to the lengthy political impasse that left Spain without a functioning government for much of 2019, and the ensuing COVID-19 pandemic, which put most non-health-related issues on the backburner.
The Spanish Fintech and Insurtech Association (AEFI), a major proponent of the sandbox, is confident that it could help generate up to 5,000 new direct jobs in the sector and an additional €1bn in investment over the next two years.

Consequently, Spain joined a handful of European nations with similar regulatory instruments. Its sandbox provides a controlled testing space for technological innovation projects in the financial services sector, particularly in the areas of banking, insurance and investment services.

The scheme is overseen by the Spanish Treasury, in collaboration with the Bank of Spain, the CNMV or the insurance and pensions regulator (Directorate-General for Insurance and Pensions Funds – DGSFP), depending on the nature of the project. A wide range of interested parties may take part: national and foreign individuals, companies including non-financial institutions, associations, public and private research centres.

The application process is conducted entirely online. The law envisages at least two calls per year and applications are examined on a case-by-case basis. Prospective participants are required to present a thorough description of the project, including a clear indication of its objectives, target group, timetable, compliance with eligibility criteria and how promoters intend to provide the required safeguards specified in the law if the project is accepted.

Projects must be technologically innovative, sufficiently advanced to be tested, and deliver added-value in areas like customer protection, market efficiency or improved regulatory compliance to qualify for entry. Regulators will also consider their potential benefits for the Spanish financial system when assessing proposals.

Selected initiatives are exempt from the legislation normally applicable to the provision of financial services but must comply with a strict testing protocol signed by the promoter and the relevant supervisory authority/ies, setting out the specific rules and conditions under which the project will be tested.

These include a robust system of guarantees to ensure participant safety, especially for trials undertaken with real-life users (e.g. informed written consent and personal data protection, rights of withdrawal, promoter liability, supervisory oversight throughout the process, etc.). Projects can remain in the sandbox for a maximum of two years. Promoters whose projects are successful may obtain fast-track regulatory clearance to bring their products/services to market.

The sandbox has elicited strong interest across the domestic and international financial services sectors (banking, insurance, securities, payments systems), as illustrated by the large volume of applications (80) submitted during the two calls for proposals launched to date, including from Canadian and Israeli firms.

Most projects revolve around biometrics, digital identity, blockchain, cloud computing, AI, IoT, and big data. Among other objectives, they seek to enhance regulatory compliance by creating tools for entities to automate previously manual processes.
Several big Spanish banks (Caixabank, Santander, BBVA), insurance providers (MAPFRE, Generali Seguros) and energy companies (Repsol) are involved in the 20+ projects that made the cut. The next registration windows is expected to open over the first half of 2022.

Comment

Despite the strong current growth of fintech in Spain, the industry is a late starter and still at an early stage in terms of size of companies, revenues and product pipeline. Broadly speaking, business opportunities for New Zealand companies and investors lie mostly in partnerships with banks and enterprises to support their ongoing digital transformation efforts.

Interviews with local fintech representatives suggest that the technologies likely to have the greatest impact on the sector in the immediate future are blockchain, big data analytics, AI and machine learning, onboarding/digital identification, and cloud computing.

Different studies highlight that Spain sits at about the EU average in terms of integration of digital technologies and that the pandemic has triggered a considerable increase in SME online sales. SMEs nevertheless still have a long road ahead to capitalise on the full potential of e-commerce, as they lag behind in areas like AI, big data and cloud.

The regulatory sandbox discussed earlier signals a strong political will to further develop the industry and should pave the way for additional legislative measures that facilitate the growth of fintech and foster financial regulation and supervision that is more agile, efficient and aligned with the new technological context, without undermining financial stability.

Equally, if rolled out successfully, the government´s ambitious strategy to make Spain a more entrepreneurial nation by 2030, which includes the first-ever startup law adopted in the country, is also expected to create a more favourable environment for investment and entrepreneurship, including through tax incentives and lower administrative burdens for tech startups wishing to establish themselves in Spain.

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