2024 Fintech Predictions

BDO

As higher interest and inflation rates persist into 2024, fintechs face a new slate of opportunities and challenges. Deal flow will likely continue at a slow pace, but fintechs will need to address a host of issues, from increased regulatory scrutiny and new disclosure requirements, to maintaining market differentiation, as well as strengthening data privacy and security controls in an evolving threat landscape.

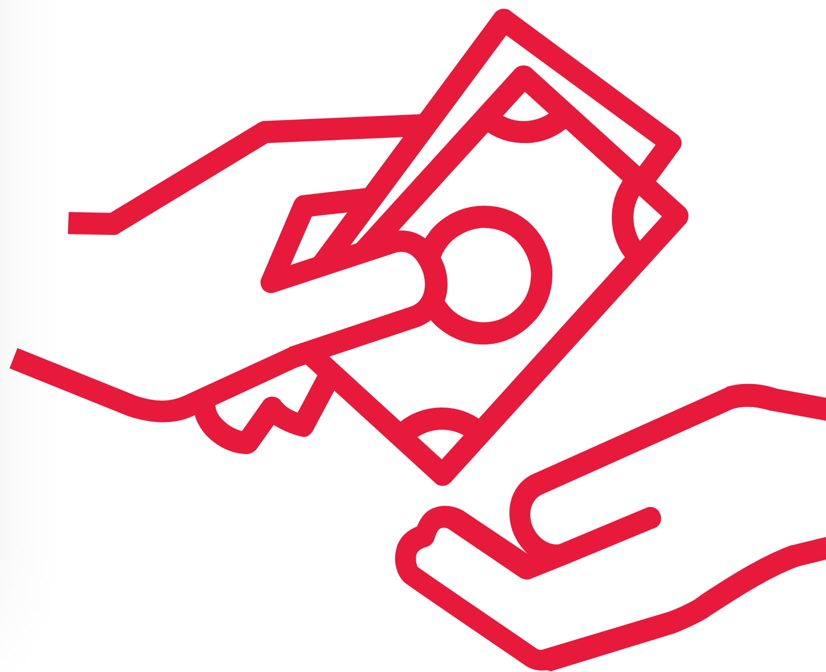
While neobanks face some headwinds, the tokenization of financial assets is primed for growth in the year ahead. Overall, we expect to see fintechs address market challenges with creativity and innovation, finding new ways to heighten competition with incumbent institutions.

End-to-end encryption will be key for biometric payments to break through barriers of entry.

Biometric payments — payment authorization methods using unique physical markers, such as facial, voice, palm, and fingerprint recognition technology — are gaining significant institutional traction. According to **Goode Intelligence**, the global biometric payments market is expected to reach $5.8T by 2026, with several traditional banks having already introduced biometric payments in identity verification.

While consumers are ready to embrace a technology that is more secure and convenient than a security code or PIN, a sizable population still harbors uncertainty or concern about privacy protections, presenting a significant barrier to adoption. **PYMNTS** reports "half of all adult consumers feel their banks must take additional steps to protect their assets and personal information — especially for non-routine transactions." These fears stem from the permanence of biometric data — in the event of a breach, one cannot simply change their fingerprint or their facial composition in the way they might replace a password or PIN.

Establishing consumer trust is therefore essential for fintechs to effectively adopt and deploy biometric payments. One method of doing so is setting extensive guardrails in place to minimize the risk of a data breach. In 2024, we predict a significant uptick in enterprise adoption of biometric payments with end-to-end encryption, which removes third-party interference and allows for more secure collection of biometric data.



More financial assets to be tokenized.

Amid record-high inflation rates in 2023 and an overall tight investor economy — with banks less likely to give out loans — we predict that the conversion of real-world assets to digital assets on regulated platforms or private blockchains is poised for significant growth in 2024 and beyond. This is because there is growing appetite to find liquidity. The answer may lie in globally available tokenized financial products, which expand the user base and draw more liquidity. The time for tokenization is prime as access to traditional borrowing and lending is tight.

Because of this, the industry will likely see fintechs develop and expand on technology for real world asset tokenization, particularly for linear debt instruments, in 2024.

The traditional argument cited in favor of tokenized assets was their ability to improve the liquidity of illiquid assets through fractionalization. While this remains a potentially attractive benefit, more timely is the fact that tokenized assets present **opportunity for capital efficiencies** in transacting and settlement, which is particularly beneficial for investors in a high-interest rate environment. For instance, fintechs can tokenize bonds and currency, as many major banks have **in the last year**. Digital assets can also streamline operations and support greater security, since processes often take place on private blockchains. However, institutions will still need to be mindful of security vulnerabilities around the use of smart contracts on the blockchain and are encouraged to use regulator-approved platforms for digital assets. since processes often take place on private blockchains. However, institutions will still need to be mindful of security vulnerabilities around the use of smart contracts on the blockchain and are encouraged to use regulator-approved platforms for digital assets.

In practice, we expect fintechs will deliver more products in this space or work with financial institutions to support investors in their quest to use and store their assets digitally. Developing more liquid instruments could potentially lead to greater market accessibility for accredited investors to participate in private equity markets who would also like exposure to debt, structured products, or receivable monetization schemes.

In 2024, we will likely see incumbent institutions introduce real world asset tokenization to draw more liquidity from their debt products and keep pace with market demand. These institutions often have the resources and compliance departments to effectively respond to regulatory restrictions from the Federal Reserve, FDIC, and SEC regarding capital requirements, valuations, and reporting. Fintechs and financial services companies will want to get involved as the opportunity to scale in this segment is rapidly approaching.

Neobanks, prepare for intensified compliance and charting a new path to profitability.

Neobanks, fintech businesses that enable **mobile and online banking**, saw rapid growth amid the Covid-19 pandemic, with an estimated **900 million** (financial) app downloads during that period. While neobanks have seen continued growth since, they have also started to face significant headwinds from regulatory bodies, presenting a host of new challenges for the industry.

Increased regulatory scrutiny, including **Know Your Customer** (KYC) and Anti-Money Laundering (AML) laws, remain key challenges for neobanks. They need to meet rigorous compliance, policy, and procedure standards to minimize suspicious activity and the risk of fraud. The Consumer Financial Protection Bureau (CFPB) and International Monetary Fund (IMF) are also pushing for more regulation of neobanks, citing consumer risks created by neobanks' current regulation state — which is notably looser than that of traditional financial institutions.

Neobanks have also confronted new disclosure requirements, such as **The Federal Trade Commission's** (FTC) rule, effective November 2023, requiring "non-bank financial institutions to report certain data breaches, including 'notification events' affecting 500 or more consumers, to the FTC 'as soon as possible, and no later than 30 days after discovery.'" While adhering to these and other requirements, neobanks also need to maintain profitability and bolster competitiveness, especially around data privacy and user experience.

In 2024, we predict that compliance challenges will intensify as more **licensing requirements** will likely manifest to enhance consumer trust and transparency, while also bringing neobanks to a similar compliance playing field as their big bank counterparts, signaling credibility. These challenges will also require fintechs to get more creative, with neobanks working to evolve their platforms to expand product offerings and establish market differentiation. Artificial intelligence (AI) can help with this innovation based on its ability to rapidly identify and anticipate customers' evolving needs; however, AI enablement will also expose neobanks to additional scrutiny, potentially presenting a double-edged sword.

Ultimately, determining and defining a path to profitability will remain a key focus for neobanks amid increased regulatory scrutiny and competition with incumbent institutions, which are more mature in both their deposit bases as well as compliant frameworks.

High interest rates mean sober fintech valuations.

Interest rates remain high — on average, 4% — and have not cooled yet going into 2024. These rates have restricted deal flow, which will not only push people out of traditional lending and borrowing markets in 2024, but also contribute to a more challenging credit cycle and potential slowdown in the economy.

While some degree of deal flow will continue, we predict that elevated interest rates will impact deal valuations as investors and buyers remain **selective** in a conservative dealmaking climate. To prepare for this slowdown, fintechs will need to demonstrate profitability and further differentiate their business models, with a specific focus on prioritizing revenue generation and profitable growth.

In light of this pressure, fintechs will need to consider thinking outside the box about innovating their service offerings or exploring new revenue streams. This will help position them for new, and higher, valuations once deal activity picks up — likely later on in 2024.

Distressed fintech deals are on the horizon.

While most M&A activity in the financial services and technology industries is expected to slow down in the next 12 months due to high inflation and interest rates, we predict the deal flow that will persist — and possibly increase — is fintech acquisitions, specifically from other, larger market players in the market.

In response to rising interest rates, **budget cuts**, and other issues, it's probable that fintechs will undergo distressed acquisitions. **Pitchbook** predicts that incumbent fintech enterprises are poised to be key drivers of these acquisitions, rather than their traditional financial institution counterparts.

This tactic will be beneficial to all parties involved. Smaller fintechs will gain their acquirers' financial resources and will likely achieve more stability in the year ahead. Larger fintechs will be able to scale even more by acquiring smaller, start-up fintechs with innovative services and product offerings.

Ultimately, larger fintechs will **buy strategically**, meaning smaller fintechs will need to diligently position themselves and their products and services to demonstrate how their solutions add value to the broader sector.

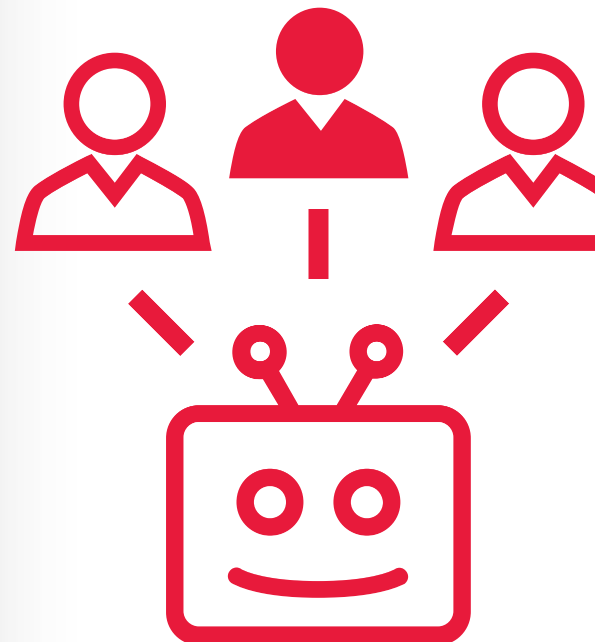
Robo-advisory will leverage generative AI to compete with the traditional broker model.

The robo-advisory sector has seen rapid growth in the financial services sector and is poised to continue a steep upward trajectory. According to **Allied Market Research**, the global robo-advisory market "is projected to reach $129.5 billion by 2032, growing at a CAGR of 32.5% from 2023 to 2032."

Tangentially, financial services companies are expressing their interest and intent to adopt more generative AI tools — such as large language models (LLMs) — for a range of **use cases**, from document research and analysis to augmented virtual assistant capabilities and more.

While financial institutions and servicers may primarily use generative AI to enhance productivity and efficiency in internal operations, it is likely that more companies will soon leverage generative AI to expand and optimize customer services, offerings, and experiences. These two trends may merge, as customers look for cheaper, easier-to-use financial advisory alternatives to the traditional broker model.

With **56% of Americans** in the workforce reporting that they do not feel prepared for retirement, the robo-advisory market may seek to leverage generative AI to improve the retirement planning experience. Generative AI can present new analyses or insights that potentially generate more reliable, stable, and personalized financial recommendations for customers based on patterns in customer data identified by machine learning and AI. Beyond this, generative AI could be used to power investment decisions by harnessing troves of structured and unstructured market data that active fund managers can use to empower predictive allocation and strategy choices.



By automating and improving robo-advisory services, the sector can attract a broader consumer market, including novice investors who might have shied away from these services in the past.

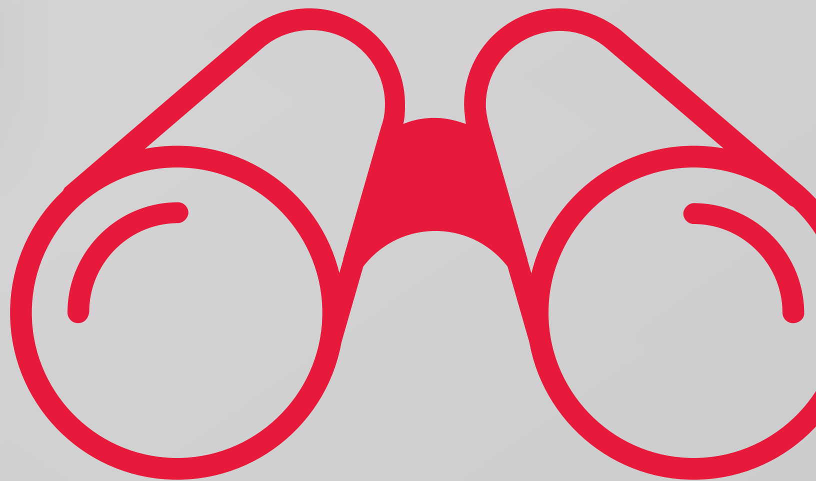
This presents an opportunity for fintechs seeking to expand their offerings. Fintechs should consider the vast ways in which they can leverage and apply generative AI to enhance their products beyond even robo-advisory. By capitalizing on trends such as this, fintechs will be better able to satiate the market's growing appetite for AI tools and meet the moment.

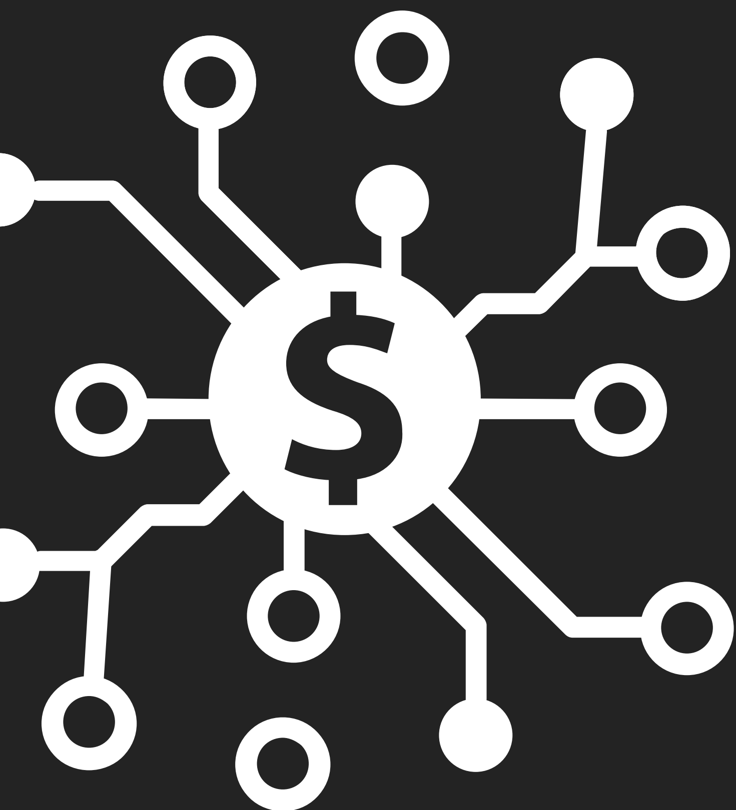
Honorable Mention: Why fintechs should keep an eye on Chevron Deference.

Decided in 1984, Chevron U.S.A., Inc. V. Natural Resources Defense Council, Inc., better known as **Chevron Deference**, established that when "an administrative agency on a particular issue or question is not explicit but rather implicit, a court may not substitute its own interpretation of the statute for a reasonable interpretation made by the administrative agency."

In May 2023, the Supreme Court **reconsidered this rule**, which could hold vast implications for fintechs. An overturn of Chevron Deference could weaken the enforcement power of key regulatory bodies, such as the CFPB and SEC.

In 2024, fintechs should pay attention to whether and how this shift would decrease these agencies' rulemaking and enforcement autonomy — which could mean a more lenient compliance landscape for fintechs. Many fintechs, especially those in the neobank sector, could welcome this type of sea-change in 2024. While it's too early to tell exactly how this case will play out, it is a critical development for fintech executives to watch.





At BDO, our purpose is helping people thrive, every day. Together, we are focused on delivering exceptional and sustainable outcomes — for our people, our clients and our communities. Across the U.S., and in over 160 countries through our global organization, BDO professionals provide assurance, tax and advisory services for a diverse range of clients.

BDO is the brand name for the BDO network and for each of the BDO Member Firms. BDO USA, P.C, a Virginia professional corporation, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms: www.bdo.com

Material discussed in this publication is meant to provide general information and should not be acted on without professional advice tailored to your needs.

© 2024 BDO USA, P.C. All rights reserved.