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Banking deals continue decline for Q2 but downturn could provide buyout opportunities

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The news: The number and total value of deals in financial services fell in Q2, according to KPMG research, as surging inflation and economic uncertainty continued to hamper dealmakers.

By the numbers: The report found the downward trajectory of M&A has continued as low market confidence impacts deals.

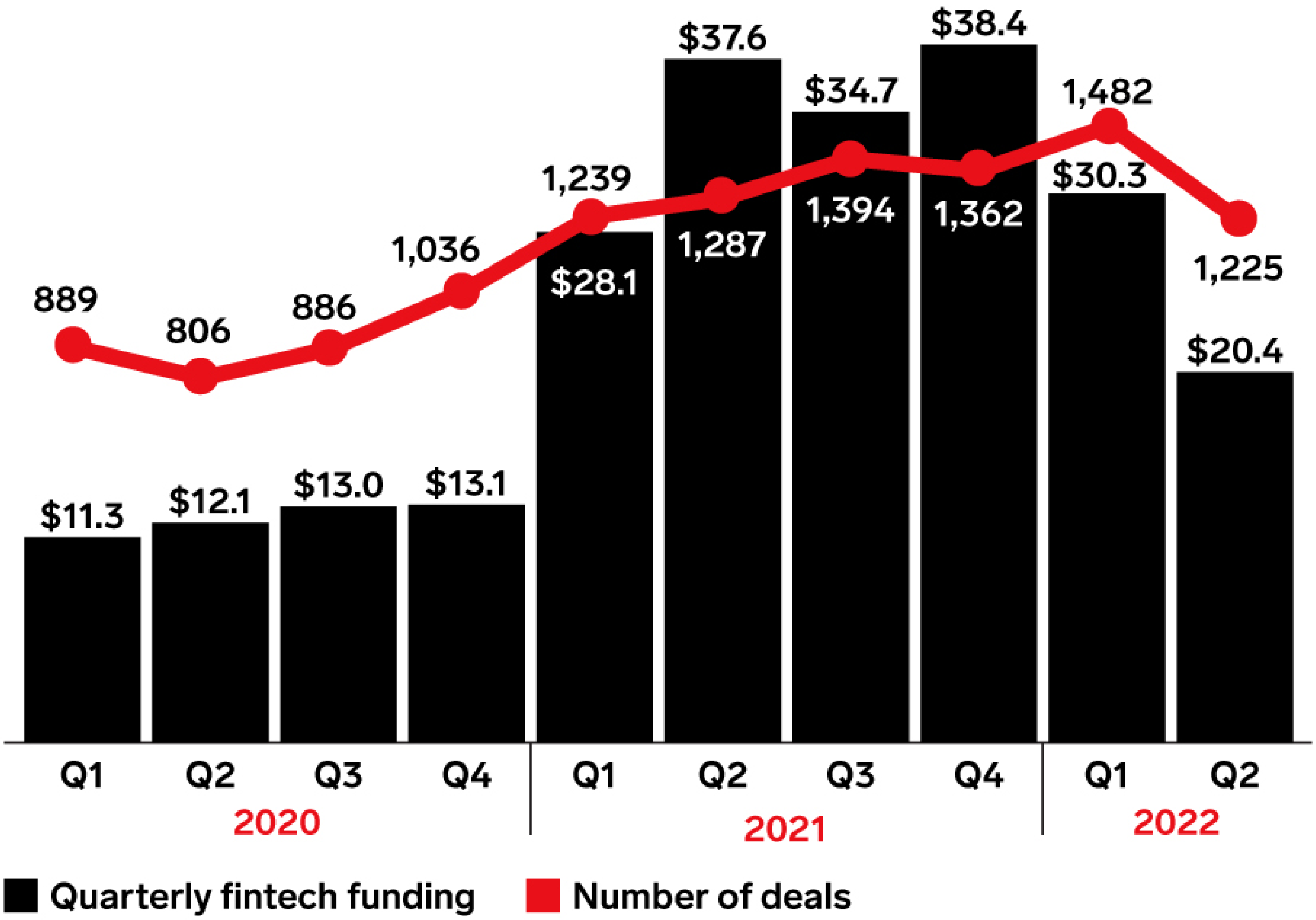
- The **number of financial services deals declined 31% QoQ** to 1,442 in Q2 .
- The total **value of financial services deals dropped 15%** to $163 billion.
- **Banking deal volume fell 47%** compared to Q1 while the total **value of deals was 87% lower.**

Analyst's take: "A perfect storm of factors has cooled fintechs' funding frenzy, including steep inflation, rising interest rates, the war in Ukraine, and fears of a looming recession," says Insider Intelligence principal analyst Eleni Digalaki.

"Weathering the storm will require cost cuts, a singular focus on offering products that can bring in money, and securing good deals for external funding."

Quarterly Fintech Funding Worldwide, Q1 2020-Q2 2022

billions and number of deals



Note: fintech covers subcategories of banking, lending, payments, wealth management, insurance, and capital markets; equity financings into private companies only; includes the investment made in the quarter for tranched investments
Source: CB Insights, "State of Fintech Q2 2022," July 19, 2022

276815 InsiderIntelligence.com

Dwindling deals: The research highlights the wider trend of stuttering M&A activity. The downward spiral, which shows no sign of bottoming out, has been heavily impacted by slashed valuations. Rising interest rates have also made borrowing to fund acquisitions more expensive.

The market's decline could create more affordable acquisition targets for firms, but it can also limit their options by cutting their valuations. Companies with lower valuations may also want to hold off from selling and wait for a potential rebound in their market price.

How will companies be affected?

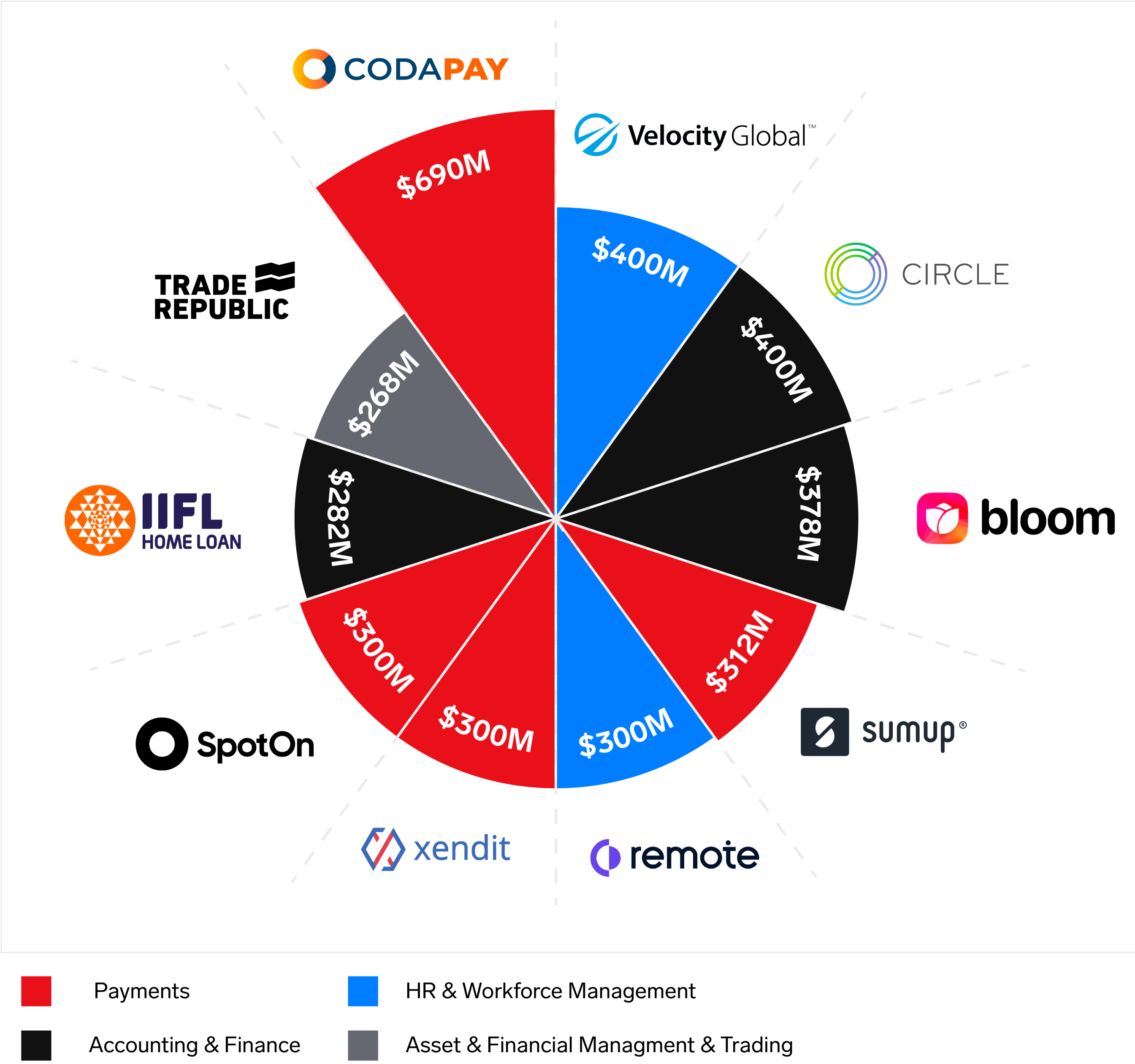
- **Incumbent banks** could benefit from the greater profitability offered by higher interest rates. Larger banks with bigger and more diversified borrower bases stand to gain the most, while smaller competitors that delay raising rates to retain customers are more at risk. This leaves neobanks and smaller high street lenders more exposed to takeovers as market leaders look to consolidate.
- **Fintechs** will find it harder to borrow money and raise capital as interest rates rise and growth declines. They will have to focus more on generating profits and cutting costs as market realities bite. Lower valuations and difficulties in raising cash could leave them vulnerable to acquisitions or force them to sell minority stakes to attract capital.
- **Neobanks** need to focus on profitability to weather a leaner climate for deals and funding. Fewer than 5% break even, per Simon-Kucher & Partners. They need to pivot from a growth-at-all-costs strategy to a profit-centered one to ensure their survival, as **Starling** and **Atom** have successfully done.

The big takeaway: Deal and funding volume is lurching towards a bottom that could still be some way off. The second half of the year looks set to be leaner and meaner.

- Profitable and more established companies can capitalize on the harder climate to make cut-price acquisitions.
- Smaller startups need to focus on cutting costs, rethinking expansion plans, and building out more lucrative revenue streams to weather the downturn—or if they can't raise funding, consider whether seeking a buyout might be the best option.

Read on: *Check out our* ***Analyst Take: Turbulent economy hurts fintech funding—here's how startups can act*** *for more on how fintechs can react to funding and valuation drop-offs.*

Top Fintech Funding Deals, Q2 2022



Source: CB Insights, 2022; Insider Intelligence
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