2019 Ukrainian FinTech & Banks Survey
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List of Acronyms

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<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
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<tr>
<td>FST</td>
<td>Financial Sector Transformation Project</td>
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<tr>
<td>M&amp;A</td>
<td>Mergers and Acquisitions</td>
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<tr>
<td>SME</td>
<td>Small and Medium Enterprises</td>
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<td>API</td>
<td>Application Programming Interface</td>
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<tr>
<td>AI</td>
<td>Artificial Intelligence</td>
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<td>BaaS</td>
<td>Banking-as-a-Service</td>
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<td>SaaS</td>
<td>Software-as-a-Service</td>
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<td>CRM</td>
<td>Customer Relationship Management</td>
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<td>HR</td>
<td>Human Resources</td>
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<td>KYC</td>
<td>Know-Your-Client</td>
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<td>IT</td>
<td>Information Technology</td>
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<tr>
<td>DLT</td>
<td>Distributed Ledger Technology</td>
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<td>P2P</td>
<td>Peer-to-Peer</td>
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<td>B2B</td>
<td>Business-to-Business</td>
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<td>B2C</td>
<td>Business-to-Consumer</td>
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<td>C2C</td>
<td>Consumer-to-Consumer</td>
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<tr>
<td>C2B</td>
<td>Consumer-to-Business</td>
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<td>EU</td>
<td>European Union</td>
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<td>CIS</td>
<td>Commonwealth of Independent States</td>
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<td>US</td>
<td>United States of America</td>
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<td>IPO</td>
<td>Initial Public Offering</td>
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<td>ICO</td>
<td>Initial Coin Offering</td>
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<td>WSI</td>
<td>Weighted Sentiment Index</td>
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<td>PSD2</td>
<td>EU 2nd Payment Services Directive</td>
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<td>AIS</td>
<td>Account Information Services</td>
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<td>PIS</td>
<td>Payment Initiation Services</td>
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<td>NBU</td>
<td>National Bank of Ukraine</td>
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<tr>
<td>SWIFT</td>
<td>Society for Worldwide Interbank Financial Telecommunications (International Inter-bank Information Transfer and Payments System)</td>
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<td>SEPA</td>
<td>Single Euro Payments Area</td>
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<tr>
<td>CBS</td>
<td>Core Banking System</td>
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<td>FY</td>
<td>Financial Year</td>
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<td>GDPR</td>
<td>General Data Protection Regulation</td>
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Should the new replace the old, supplement the old, or should the old embrace the new and together transcend to a fundamentally new approach to serving customers? Is the old prepared to talk to the new, and is the new competent enough to replace the old? Should the new be treated as a threat or as an opportunity?

These are the uneasy questions at the core of the current bureaucratic banks versus agile customer-centric FinTech solutions showdown, experienced on a global scale. With over US$53b invested globally into FinTech projects in 2018 (and 2019 shaping up to be similarly strong), the Mean Lean FinTech Machine is arguably gaining ground globally. The revolutionary transformation of financial services and nearly all-encompassing coverage of banking services seems fully upon us.

Yet is it truly? In Ukraine, the global FinTech revolution is still some way off - despite the unparalleled technological and human capital potential the country possesses.

The Ukrainian commercial banking industry has traditionally, albeit with a few exceptions, been wary of innovations, of outsourcing functions, of being customer-centric rather than serving its own needs and goals. An imperfect legislative framework bearing a Soviet Union legacy and the lack of digital era competencies by commercial banking leaders and employees also played their role.

In short, the Ukrainian banking sector was ill-prepared to meet and understand the new FinTech players. The status quo is changing now - but in order to understand just how strong the ‘winds of change’ are blowing through the Ukrainian financial services sector, we saw a need for a detailed survey of the market players from both camps. The survey was conducted with full anonymity to allow us to obtain honest, transparent answers.

The resulting analysis is a mixture of presenting the current state-of-play in the market and an eye-opener full of fascinating insights. Please read on to find out what really makes the Ukrainian financial services sector tick in this Age of Transformation.
Technology enables financial service providers to lower costs and access customers remotely, leading to greater financial inclusion. Technology also opens the door to new players in the financial services market: mobile operators, e-commerce platforms, messengers, social networks, and other big tech firms with a large consumer base.

Competition is a good thing. Some markets have transformed dramatically as a result of digital revolution. In China, for example, Internet-related services conglomerates have changed the market with their innovative financial services products. In India, with arguably the most ambitious national digitalization project in the world, a number of global big tech firms are battling it out in the digital payments arena.

In mature markets, where traditional finance is more developed, new entrants have had a smaller impact. Nevertheless, the variety of new financial service offerings is staggering. Regulators across the world have become aware of the need to accommodate the new financial technology through new regulation, by setting up sandboxes, “light licensing” for new entrants, and tax advantages.

The United Kingdom, Northern European states, Lithuania and Singapore are prime examples of supportive approaches to the new technology.

How does Ukraine, with its bank-dominated financial system and card centric retail payments, relate to the global digital boom?

The short answer is that the country is behind and needs to catch up. Most FinTech startups are heavily reliant on their own capital, and do not have a functioning capital market to turn to for support. The infrastructure for digital finance is inadequate and financial institutions need to start investing in technology. It is necessary to reform outdated regulations to foster a nurturing environment for digital finance entrepreneurship. Sandboxes are nurseries for FinTechs, and Ukrainian regulators need to promote their use to the FinTech industry.

FST and EY surveyed the Ukrainian FinTechs and the banks for their views on the market. The resulting snapshot identifies the change agenda that needs to be pursued for Ukraine to turn its undeniably talented IT industry into a leader in digital financial services.
GLOBAL TRENDS
Rapid technological advance is reshaping the face of the financial services sector globally. FinTech propositions, once thought of as neat welcome additions to existing traditional services that make clients’ lives and operations more comfortable, now challenge all aspects of the financial world at all foreseeable angles. In its Global FinTech Adoption Index 2019, EY defines two key offering types: “disrupted” and “invented”:

A disrupted service is one that has historically been offered by incumbents, such as automotive insurance or foreign exchange trading. FinTech providers use technology to disrupt these services by offering consumers a more compelling offering such as enhanced capabilities, convenience, or lower rates and fees. This profoundly changes customer expectations in the process, pressuring incumbents to develop similar services to stay competitive and retain market share.

An invented service is one that didn’t exist before but is now possible by technology and alternative business models, such as peer-to-peer lending and mobile-phone payments. Some invented services fill niches in the market, and others have the potential to redefine and transform entire financial subsectors.

The FinTech industry has surged upwards. No longer made up of only start-ups, the sector is seeing the incumbent players moving in with both their own in-house developed propositions and through hectic FinTech M&A activity.

Consumer popularity of FinTech solutions is matching the supply. Adoption of FinTech services has moved steadily upward, from 16% in 2015 to 64% in 2019. Awareness of FinTech, even among non-adopters, is now very high. SMEs are trailing behind; however, even within that group every 4th company globally has used at least two FinTech solutions in their day-to-day operations.

We define FinTech as “organizations that combine innovative business models and technology to enable, enhance and disrupt financial services.”

The prime reasons to use FinTech propositions for consumers are attractive rates and fees, as well as significantly improved mobility of use. The SMEs, in turn, are looking for an improved range of functionality and features, either unavailable before or available to large corporate players only, for a fraction of the price.

Surprisingly enough, the major developing countries lead the FinTech consumer adoption trend – according to the EY Global FinTech Adoption Index 2019, China, India, Russia and South Africa all have averaged above 80% consumer adoption rate. At that, Canada, USA, France and Japan all clocked 50% or below.
Global Trends

Consumer Trends, Expansion and Convergence

Consumer Trends

The majority of the FinTech offerings for consumers globally are concentrated around just five areas: money transfer and payments, budgeting and financial planning, savings and investment, borrowing and insurance. Money transfer and payments is, by far, the most adopted FinTech service bucket. The number and volume of investment rounds into digital-only challenger banks and omni-channel money transfer services over the past 24 months shows just how prospective this range of propositions is deemed by the global venture and strategic investors.

The incumbents that are most responsive to this competitive threat are those that disrupt their own propositions and offer comparable FinTech services, either through partnerships, acquisitions or in-house development.

In recent years, incumbents have brought forth their FinTech versions of disrupted services in areas such as online foreign exchange, online investment advice and management, and digital-only branchless banking.

At that, the consumer-focused tech is not limited to ‘direct active interaction’ solutions. Insurance-related technologies, for example, include ‘enabling tech’ projects, such as equipping cars with telematics modules to feed information to car insurers or fitness mobile apps connected to health insurers that count steps and other movement and offer insurance discounts based on performance.

Expansion and Convergence

The incumbents in the global financial services sector are now seeing the change of the paradigm very clearly. According to the Ropes & Gray 2019 Fintech M&A report, around 88% of global financial service providers believe their market share is under pressure from FinTech innovators.

In response, 56% of their respondents now incorporate disruption into their core strategy. Over 82% of them are planning to expand partnerships with FinTech propositions. Moreover, 85% of the banks and other financial sector providers are saying FinTech M&A is very important to their core business strategy.

According to the same report, 73% of incumbents say the need to improve customer experience and outreach is driving their plans for FinTech acquisitions. Roughly the same number say they plan to acquire at least one FinTech company in the next two years. Around 70% expect FinTech M&A activity to increase significantly over the next 12 months.

All this bodes well for new FinTech projects across the world. Now considered a legitimate threat to incumbent businesses, they are finding themselves at the center of investment and customer attention. This spurs technological advancements and redefines growth targets.

Challengers have built themselves using a design-first approach and agile work processes. By keeping a technology-forward mindset, they are able to offer FinTech services that are at once personalized, accessible, transparent, frictionless and cost-effective.
Global Trends

Technology Trends

FinTech does not always mean Deep Tech. Some of the top neo-bank and money transfer projects globally are built on ‘less tech, more user experience’ foundations. They enhance service targeting and personalization, analyze user behavior to optimize online and offline experiences, push for better experience in areas such as price, convenience, access and others. Their allure lies in the customer-centric approach, redefining and simplifying customer journeys from origination to day-to-day support.

At that, technology driven by an influx of investments into the space is pushing the boundaries in all directions.

DIGITAL AND OMNI-CHANNEL BANKING

By 2019, the traditional banking world has come to realize that while its traditional middle and senior-aged audience may still prefer offline communication, the younger generation of consumers and corporates alike are looking for much more flexible options that save their time and allow them to choose the channels and modes of communication with their financial service providers.

Investors realize that as well and are now demanding digital banking expansion included in strategic plans from the incumbents in the sector. Some choose to launch proprietary digital services, others rely on partner bank models and release of APIs that third-party FinTech providers may use to create unique solutions.

A notable tech trend that’s gaining momentum is the implementation of omni-channel banking, whereby a consumer may start onboarding with a financial service provider through their website, continue through any of the popular social messaging applications and finalize by e-signing an agreement through a special online client-bank interaction application. Data between the channels is seamlessly synchronized to allow for an immersive experience for the users.

AI-BASED SOLUTIONS

According to the 2018 Digital Trends in Financial Services report by Econsultancy/Adobe, around 20% of financial services providers globally are already utilizing artificial intelligence (AI) in their operations while 41% are planning to implement it in the near future. Smartly designed AI applications are able to both ease day-to-day internal operations by automating repetitive tasks and provide strong support to user targeting, client performance predictions and risk management.

AI-based big data analytics provide hereto unseen opportunities for large-scale financial service providers to react in real-time to consumer and economic trends. AI-based compliance automation systems drastically cut the expenses on bloated legal and risk departments and reduce the margin of human error.

BANKING-AS-A-SERVICE

A result of growing convergence of the financial and non-financial sectors, BaaS is a model that allows non-financial companies to add banking services into their own applications and digital products. A retailer may issue a branded discount card with limited bank functionality. Consumers do not sign any traditional bank papers to open an account but have full use of the specific services embedded. The bank, in turn, benefits from spending data shared by the retailer.
Global Trends

Technology Trends - Continued

**OPEN BANKING**

This trend is a pre-requisite for mass expansion of digital-only banking approaches. Open banking allows creation of plug-and-play APIs that can be used by third-party developers to make use of open financial data provided by the banks. Consumer data from different sources is then readily available to call upon and analyze through a single standardized API. This benefits both the service providers and the consumers as it enhances transparency and reduces profiling risks, improving the service use terms for consumers and reducing losses for the providers.

**CREDIT FOR UNBANKED**

Just as important is the ultimate issue of unbanked. According to World Bank data from 2017, over 1.7 billion people globally were defined as ‘unbanked’ – that is, without a formal account at a financial institution or through a mobile money provider. Reaching that staggering number with financial services remains one of the top priorities of the financial service providers globally and here technology comes into play.

Digitally-administered microfinance solutions were and remain popular. However, now progressive tech-based finance is coming to the forefront. An individual may be unbanked, however his spending habits (mobile phone, shops, insurance, transportation et. al.) are being recorded and analyzed. With a progressively stable or improved spending behavior the individual may be offered credit by any of those sellers or, if the spending data is shared, by a group of them or a third-party loan provider.

**CLOUD COMPUTING**

Top global financial sector providers are already using cloud-based Software-as-a-Service (SaaS) solutions for a range of internal functions, such as accounting, CRM and HR. Cloud-based KYC and security check functionality by third-party providers are also steadily gaining popularity. Investments into cloud-based infrastructure and data storage and processing are becoming a key item in the general IT budgets of the major financial services providers.

**DLT/BLOCKCHAIN**

While heavily associated with cryptocurrency projects in the general public’s view, distributed ledger technologies have a much wider range of applications. By various global experts’ estimates, implementation of DLT infrastructure by financial services providers can cut 30-70% of their costs in such areas as financial reporting, compliance and business operations. Improved transparency, data verification, internal controls, reduced need for reconciliation of data, and limitless possibilities for data sharing are all made available by DLT solutions.
2 METHODOLOGY
Methodology

We define FinTech as organizations that combine innovative business models and technology to enable, enhance and disrupt financial services (source: EY Global FinTech Adoption Index 2019).

To that end, we have applied the following key filters to the universe of FinTech market participants:

1. Organizations that develop and sell a proprietary innovative FinTech mono-service or product (i.e. companies that concentrate on one service or product only);
2. Software development companies that develop and sell multiple distinct FinTech services or products;
3. Organizations that operate fully-developed services or products and generate revenue.

The latter requirement has been introduced in order to exclude pre-revenue startups in product development stage and include views from market players that have direct exposure to operations and customer interaction on the Ukrainian market.

We have excluded software development companies that develop bespoke white label FinTech solutions for corporate customers.

We have included geographic filters on the potential participant list in order to analyze the current state and expectations of the Ukrainian FinTech market:

1. Organizations that provide FinTech solutions or services to Ukrainian customers; further limited to:
   2. Organizations that operate out of a Ukrainian legal entity; or
   3. Organizations or projects that have Ukrainian founders in their shareholder structure.

In several instances, we have also included organizations from #3 above that have yet to start full-scale operations in Ukraine but operate beyond Ukrainian borders and are in confirmed talks with pilot Ukrainian customers.

Several FinTech sub-sectors required additional definitions. In particular, we have included some crowd financing and P2P lending projects, limited to projects that are directly involved in transactional and fund transfer operations of their users or control transaction procedures through their platforms.

We have excluded from the survey “short term, high cost” lenders, sometimes referred to as “payday lenders”. While these organizations are legitimate businesses according to Ukrainian legislation, they do not meet USAID FST Project definitions of companies that practice financial inclusion: financial products that are useful, affordable, and offered responsibly.
KEY FINDINGS: FINTECH RESPONDENTS
Key Findings: FinTech Respondents

Introduction

The Ukrainian FinTech Catalog 2019, a product of the Ukrainian Association of Fintech and Innovation Companies, compiled with the support of the National Bank of Ukraine and Visa, lists more than 100 companies as participants of the Ukrainian FinTech market.

The companies listed in the Catalog may roughly be divided into service providers, enablers, multi-product developers and non-financial solutions.

Based on the methodology we have employed, we have approached 88 companies and projects. We have invited representatives of the FinTech companies, who hold an executive position at their companies and/or are responsible for the implementation of the technological solutions there.

The survey was intentionally set up as fully anonymous to achieve maximum objectivity and honesty of the answers.

The questions in the survey are divided into three distinct categories: Profiling, Operational and Opinions.

Profiling questions cover key information about who the FinTech organizations are, what they do and their expertise.

Operational questions cover the details on the services and products the respondents provide and their operation models.

Opinions require the respondents to present their qualitative subjective views on a range of issues pertaining to legislation, market prospects and cooperation with the traditional banking sector.

41 companies/projects have successfully completed the survey
48.8% of the respondents consider themselves a startup. This is somewhat surprising considering that revenue generation was a prerequisite for inclusion into the survey participant list.

At that, 73.2% of the respondents have operated on the market for over 3 years, with just 2.4% operating for less than a year. Furthermore, 55% of those who consider themselves a startup, have been operating for over 3 years.

This poses questions as to the definition of a startup by the Ukrainian market participants. Interestingly, 71.4% of the respondents who did not mark their business as a startup, have been operating for over 5 years.

87.8% of the respondents provide B2B services or products. This runs contrary to the global FinTech adoption trends, where corporate adoption lags significantly behind consumer adoption.

Insight Analysis: We attribute the abundance of B2B projects to a number of factors, including 1) weak disposable household income dynamics in Ukraine that limit growth potential for B2C-oriented organizations, 2) lack of financial sector infrastructure, especially in the smaller towns and villages and 3) “trust crisis” by the Ukrainians to financial services following liquidations of a large number of banks. Development of B2C solutions also requires significant investments into wide-scale marketing compared to B2B offerings, which the majority of the FinTech projects typically cannot afford given the overall lack of capital.
Answers to the geographical presence question display strong interest and focus of the respondents on the neighboring international markets.

More than 50% of the companies are operating in the EU (with just close to 20% doing business in non-EU European destinations), with 40+% operating in the CIS region and about 25% in US/Canada and Asian markets, respectively. Surprisingly, Ukrainian FinTech players are reaching out even to the less popular markets of Africa (over 15%), South and Latin America (~10%), Australia and Oceania (~7%).

41.5% of the respondents operate in Ukraine only

100% of the respondents who operate in the US are also doing business in other international geographies.
Financing remains an issue for new technology businesses in Ukraine. A significant number of respondents, namely 61%, are fully self-financed. Interestingly, this result is corroborated by the data provided to the same question in the Ukrainian Fintech Catalog 2019. Private equity and debt investors are two other material sources of funding, followed by strategic investors (excluding banks), accelerators/incubators and commercial loans.

Additionally, 92.7% of the respondents noted that they do not use or plan to use bank loans to finance their development. None of the respondents have used IPO/Private placements as financing sources, with just one respondent saying they are planning one in the future. Only one company has taken advantage of an Initial Coin Offering.

In the future, 26.8% of companies are planning to attract financing from strategic investors (excl. banks), 17.1% - from international finance institutions, 14.6% - from venture funds, 12.2% - from private investors (equity financing). None are looking to personal savings, debt from private investors or an ICO as sources of further funding. Some respondents mentioned re-investment of profit and grants (incl. those provided by the state) as possible financing sources.

**Insight Analysis:** New tech-based projects globally are typically financed by third-party capital. 61% being fully self-financed in Ukraine shows an overall lack of external capital for development which is slowing down the sector – accordingly, rapid expansion is unlikely. Foreign investors are being very cautious, and none of the traditional commercial banks are offering meaningful loan programs and terms to high-tech development stage businesses.
Key Findings: FinTech Respondents

Key Findings: Profiling

97.6% of the respondents said they do not have banks, banking groups, bank-managed corporate accelerators or other bank-affiliated entities in their shareholding structure.

Importantly, 75.6% of the respondents have someone in their top management/Board with multi-year expertise in the traditional financial services market. At that, among those who provide services and solutions to banks that number is even higher – 89.5% (compared to 63.6% among those who do not cooperate with banks).

This shows the FinTech eco-system highly values the hands-on experience gained within the traditional financial sector and is prepared to put it to use in their own offerings.

Insight Analysis: Contrary to global trends where over 80% of banks and other traditional financial service providers are now looking to acquire or finance FinTech solutions in order to expand and improve their service propositions, the Ukrainian FinTech market is predominantly independent of traditional banking influence or funding. Ukrainian banks seem content to either continue operating within their traditional offline environment or go digital through its own internally-developed solutions or selective partnerships with third-party service providers.

Are there banks, banking groups, corporate accelerators/incubators managed by banks or other bank-affiliated entities among your investors or ultimate beneficiaries?

97.6% No

Is there at least one person in your top management that has multi-year work experience in a commercial bank / insurance company / financial services / financial regulations?

75.6% Yes
Key Findings: FinTech Respondents

Key Findings: Profiling - Profile Summary

- Europe-focused
- B2B-oriented
- No investment from banks
- Self-financed
- Has senior management experience in traditional financial services
- Operating for 3+ years but still in development stage
As discussed in the Profiling section, the majority of the respondents have stated they are B2B-oriented. However, when asked to detail specific services or products they provide, 65.9% were found to be multi-modal (offering both B2B and B2C services/solutions). Across the range of services and products offered as answer options to the survey participants:

- 92.7% of the respondents work under the B2B model (incl. the classic B2B and rare C2B interaction modes)
- 73.2% of the respondents work under the B2C model (incl. the classic B2C and less common C2C interaction modes)

At that, 26.8% of the respondents operate solely in B2B, while only 7.3% operate solely in B2C.

Across both business models, the two most popular services were card payments and other payment types (excluding card and cross-border payments). Other services consistently present under all business models were e-invoicing and e-money.

The least popular FinTech offerings were found to be treasury services and asset and investment management services. Each of those is provided by one respondent only.
Key Findings: FinTech Respondents

Key Findings: Operational Insights

Interestingly, 6 respondents (14.6%) said they are a challenger or neo-bank. Of those, just one claimed cooperation with a traditional bank. Given that, to the best of our knowledge, none of the FinTech respondents in our list had a banking license, the respondents may be misunderstanding the definition of ‘challenger bank’, or, alternatively, they may provide those services beyond Ukrainian borders.

The respondents’ list includes also companies that operate within the relatively new or uncommon FinTech sectors for the Ukrainian market, particularly InsurTech, RegTech (including Compliance Automation), AI/data analytics and Crowdfunding sub-sectors. While having more than one respondent for each of those areas, the total counts are very low compared to the mass market-oriented offerings.

Insight Analysis: The abundance of payments and e-invoicing solutions shows the eco-system is reacting to the basic mass market demands for quicker and more flexible money transfer, utilities payments and retail-related solutions. This is ‘easy money’ for the project founders compared to the more sophisticated services and solutions that require much more R&D investment, explanatory work to potential clients and often need to be customized or tuned to clients’ requirements.

Lack of investment management, custodial and personal finance management solutions is clearly putting the overall eco-system very far from maturity seen in key global markets. Primarily, this is due to very basic presence of the capital market within Ukraine and lack of access to it.

Cooperation with banks

Overall, the respondents have medium exposure to banks as corporate clients, with 46.3% of the respondents providing at least one service or product to a bank. The most popular services provided to banks were e-invoicing (22% of the respondents), other payment types excl. card and cross-border payments (17%) and cross-border payments (14.6%). Crowdfunding, asset management and retail origination services are not provided by FinTech organizations to banks at all.

While e-money is a top-5 service across all business models, only 12.2% of the respondents issue e-money together with banks. Given that currently only banks are legally allowed to issue e-money in Ukraine, this result conjures questions in regards to the definition of e-money by the market.

Top-3 services provided by FinTech respondents to banks

- E-invoicing - 9
- Payments (excl. card and cross-border) - 7
- Cross-border payments - 6
### Key Findings: FinTech Respondents

**Key Findings: Operational Insights**

#### Which monetization mechanism does your company use for its products/services?

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<th>Mechanism</th>
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<tr>
<td>Transactional commission</td>
<td>65.9%</td>
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<tr>
<td>Subscription-based compensation</td>
<td>48.8%</td>
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<tr>
<td>Revenue sharing</td>
<td>29.3%</td>
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<tr>
<td>Other</td>
<td>22.0%</td>
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<tr>
<td>Pay-per-lead</td>
<td>12.2%</td>
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**Monetization mechanisms**

The most popular way of monetization for the FinTech organizations is transactional commission, with 65.9% of the respondents employing this approach. Subscription-based compensation is another popular model (48.8% of the respondents). At that, 70.6% of the respondents employ a combination of monetization mechanisms for different clients rather than just one.

However, among those that provide services and solutions to banks, the importance of subscription and revenue sharing mechanisms is much higher - transactional commission model is being employed by 68.4%, subscription-based models are used by 63.2% and revenue sharing is implemented by 57.9% of the respondents cooperating with banks.

«Other» is an option that asked respondents to name their own monetization approach. Specific answers included: “brokerage commission”, “royalties”, “payment for service and/or product”, “license fee”.
Key Findings: FinTech Respondents

Key Findings: Operational Insights

Traction and competitiveness

Despite the overall public perception that finding pilot clients for new FinTech solutions is a challenge, 75% of the corporate-oriented respondents required less than 6 months to find their first pilot corporate client after finalizing product development of their solution. Importantly, among those who offer services and solutions to banks, the result is very similar (73.6%).

At that, within that sub-group there are relatively fewer of those who managed to find their pilot within 3 months (42.1% to 50% in overall corporate-oriented respondent group), and more of those who claim 3-6 months (31.6% to 25% in overall group) and 6-12 months for their first client (15.8% to 8.3% in overall group).

61% of the respondents believe they have less than 5 competitors in their specific niche on the Ukrainian market. 5 firms believe they have a unique solution offered by no one else locally. Importantly, among those who provide services and solutions to banks, the number of those claiming to have less than 5 competitors in Ukraine increases to 73.7% - yet just one respondent said “no competitors at all”.

Insight Analysis: The ‘number of competitors’ results are expected, given the overall low number of FinTech solutions operating in Ukraine. Barriers to entry are high enough, given lack of capital and difficulties in persuading clients to start using new service types from new relatively unproven companies. The ‘global competitiveness’ sentiment, however, is a display of overconfidence and lack of realistic understanding of what global markets have to offer - especially, with over 40% of the respondents operating in Ukraine only. This ‘technological arrogance’ may be one of the reasons investors are overlooking many of the Ukrainian-sourced FinTech projects.
Barriers to development

We asked the FinTech community what barriers to FinTech development in Ukraine they consider as the most relevant. The options offered by the survey were: lack of venture capital, difficulty in forming partnerships, bias towards banks, outdated adverse legislation, underdeveloped infrastructure, financial literacy, absence of ecosystem and deficit of talent.

The highest WSI - 50% - was attained by outdated adverse legislation. Two other barriers were also deemed important, though with less of a general consensus - difficulty in forming partnerships and lack of financial literacy. Deficit of talent was considered the least important barrier, with a WSI of -63.5%. Interestingly, lack of venture capital was also among the least important barrier options selected by the respondents.

Among those who provide services and solutions to banks, the legislation barrier was deemed just as important followed by the partnerships formation issue. However, the #3 spot was replaced by 'absence of the eco-system', closely followed by underdeveloped infrastructure. Lack of financial literacy is perceived by that sub-group as much less of an issue, compared to the full respondents group result.

The companies were also asked to suggest their own barriers. Adverse economic conditions in Ukraine and slow and cumbersome decision-making processes by potential corporate customers were among the most popular answers.
# Key Findings: FinTech Respondents

## Key Findings: Opinion Insights

### Need for legislative changes

The respondents were asked to provide an opinion on the most critical legislative changes required for development of the FinTech sector in Ukraine. Of the 16 options offered, **introduction of legal framework for remote client identification** and **introduction of PSD2 rules** were deemed as the most critically sought changes, with a WSI of 62.25% and 52.45%, respectively.

Among those who provide services and solutions to banks, the results were very similar with the exception of **cybersecurity standards**, which were deemed much less important by that sub-group and replaced instead by **encouragement of payments by and to government agencies through digital channels** (in fact, this option moved to hold #4 spot in the ‘banks providers’ sub-group).

FinTechs also had an opportunity to indicate any other legislative or regulating initiatives which they consider important to enable digital finance. Most notable answers included: **legitimization of cryptocurrencies**, **currency regulation for money transfers**, **pension and tax reform**, **capital markets framework**.

<table>
<thead>
<tr>
<th>Top-5 most sought legislative changes for FinTech development in Ukraine, WSI values</th>
<th>WSI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Remote identification</td>
<td>62.25%</td>
</tr>
<tr>
<td>EU 2nd payment services directive (PSD2)</td>
<td>52.45%</td>
</tr>
<tr>
<td>E-money legislation</td>
<td>25.60%</td>
</tr>
<tr>
<td>Introduction of AIS and PIS licensing*</td>
<td>23.20%</td>
</tr>
<tr>
<td>Cybersecurity rules and standards</td>
<td>7.35%</td>
</tr>
</tbody>
</table>

* AIS and PIS are acronyms for: Payment Initiation Services and Account Information Services.
Key Findings: Opinion Insights

Digitalization priorities for banks

The respondents were asked to provide an opinion on which systems / services / processes are top priority for automation / modernization / functionality improvements for commercial banks.

Remote client identification was deemed the most important with a WSI of 48.75%, followed by data analytics for fraud prevention, cybersecurity, customer interaction interfaces and automation/support for the decision-making processes. At that, custodial functions modernization was considered the least priority for banks with a WSI of -67.05%.

Among those who provide services and solutions to banks, the top-5 remained the same, although with a change of order between spots #3, 4 and 5. Custodial functionality remained at the bottom of the ‘importance’ list but has been equally matched by modernization of HR functions.

Top-5 systems/services/processes considered by FinTechs top priority for automation/modernization/functionality improvements for commercial banks, WSI values

- Remote client identification: 48.75%
- Data analytics for fraud prevention: 40.20%
- Cybersecurity: 31.75%
- Customer interaction interfaces: 29.25%
- Automation/support for decision-making processes: 25.65%
Key Findings: FinTech Respondents

Key Findings: Opinion Insights

Non-existent services with best development potential in Ukraine

When asked to grade FinTech services that are non-existent or barely introduced in Ukraine for their development potential, cross-border payments for SMEs and individuals led the consensus with a WSI of 32.9%, followed by financial services for unbanked individuals and e-invoicing. Cross-border investment applications were considered the least interesting niche for development of new projects.

Among those who provide services and solutions to banks, cross-border payments for SMEs and e-invoicing both gained an equal WSI value of 39.5% followed by services for the unbanked with a WSI of 23.7%.

Respondents also had a chance to indicate their own views of the most revolutionary FinTech services and business models not yet available in Ukraine. Among those, who opted to answer this question, the majority believe the most popular revolutionary FinTech service/business models currently missing in Ukraine are PayPal, P2P loans and legal framework for cryptocurrency operations.
Key Findings: Opinion Insights

NBU Innovations Hub

The respondents were asked whether they believe the NBU innovations hub will facilitate FinTech development in Ukraine. With a WSI of -19.55% (-15.79% among those who provide services and solutions to banks), the FinTech community's expectations for the NBU hub's performance and usefulness are low. This may be caused by a misunderstanding of the role of such a Center and the mechanisms of its interaction with other stakeholders within the local market.

The respondents indicated the importance of setting up the working groups on the priority topics with the key market players, as well as the ability to work in the “sandbox” under the regulator's supervision, and to introduce pilot solutions. FinTech companies want to see real help with the advancement of technologies, software and services.

FinTech companies also stated that they would like to see the Hub as: an open platform for the dialogue of traditional and new players of the FinTech industry, a consulting center, a place for events for the key market players, a place that would be open “to hear” the real needs of the market and initiate necessary legislative changes for its development.

Will the NBU innovations hub facilitate FinTech development in Ukraine?
Grade 1 to 5, where 1 - will not facilitate at all, 5 - will facilitate to a major extent.
61% of the respondents said they believe liberalization of the foreign exchange market in Ukraine created opportunities for development of new FinTech services.

Did liberalization of the foreign exchange market in Ukraine create opportunities for development of new FinTech services?

61%

60.8% of the respondents confirmed they frequently experience reluctance of the traditional banking system to embrace new technologies developed by FinTech organizations.

When asked about the most important FinTech occurrence on the market last year, 24.4% of the respondents mentioned the full-scale launch of Monobank and rapid growth of the number of its customers. This was an optional question and accordingly was answered by fewer respondents. Of those who did, Monobank was cited as last year’s most important market occurrence by 50%.

Other frequent answers featured a number of important FinTech-related events and conferences, most notably PaySpace Magazine Awards.

Ukrainian digital banking service Monobank, which went live in 2017, has 1.5 mln customers as of November 2019. In 2017 the service was nominated as the Best Ukrainian FinTech Startup by the PaySpace Magazine Awards. Last year Monobank was selected as the “Neobank of the Year” by FinAwards 2018.

The banking service works through a mobile app and features absence of physical branches, simple mobile-application process, cashbacks, in-app payments and P2P transfers without a fee (except the credit money payments), simple installments arrangements and possibility to activate auto-accrual of interest on the current account balance (non-credit funds).
KEY FINDINGS: BANK RESPONDENTS
Key Findings: Bank Respondents

Introduction

The National Bank of Ukraine listed 76 active banks as of 01.10.2019. We have been able to reach 43 banks out of 76 in regards to completing the survey – however, just 14 have successfully completed the survey.

This completion ratio may indicate the reluctance of the traditional banking sector to discuss their own digitalization plans and their views on FinTech development.

It may also mean the banks who successfully completed the survey are the most progressive with regard to FinTech. Accordingly, the survey results provided below may tend to be overly optimistic compared to the status quo of the Ukrainian commercial banking market in general.

The questions in the survey are divided into three distinct categories: Profiling, Operational and Opinions.

Profiling questions cover key information about who the banks are and their expertise in digital transformation and FinTech issues.

Operational questions cover the details on the digital services and products the respondents provide, their investments into digital infrastructure and cooperation with third-party solution providers.

Opinions require the respondents to present their qualitative subjective views on a range of issues pertaining to legislation, market prospects and cooperation with the FinTech sector.

14 banks have successfully completed the survey
Key Findings: Bank Respondents

50% of the respondents are banks with foreign capital, while the other 50% are banks with Ukrainian capital. None of the state-owned banks have completed the survey.

100% of the bank representatives filling out the survey were either Members of the Board or Heads of Department (Risks, Digital, Financial, Operations).

64.3% of the respondents identify themselves as universal banks, with another 14.3% identifying themselves as corporate-focused banks. Among other respondents of the survey were: one bank with the retail banking specialization, one bank that is a part of the industrial financial group, and one specialized bank for agricultural producers.
85.7% of the responding banks (or their affiliated entities) do not hold equity in FinTech organizations. One respondent mentioned they do own FinTech shares at Group Level and another did not provide any specific details about its FinTech equity.

78.6% of the respondents employ people dedicated to cooperation with software development companies and the FinTech sector. Yet, just 50% have people dedicated to digital strategy and transformation and only 35.7% employ experts specifically responsible for identification and unlocking potential of the FinTech sectors.

Only 28.6% of the respondents have at least one Board Member in their bank with specific expertise in FinTech or digital strategy and transformation. Importantly, 100% of those banks who do have at least one such Board Member also employ people dedicated to cooperation with software developers and FinTech providers and experts responsible for digital strategy and transformation. 75% of those banks also employ people dedicated to identification and unlocking potential of the FinTech sector. This is a clear sign of focusing on digital transformation strategy.

Insight Analysis: Ukrainian commercial banks, given the lack of understanding of the FinTech industry, have been very reluctant to spend time on the survey dedicated to FinTech and digital strategy issues.

Moreover, from the anonymous access login data, we know that there were close to 40 attempts at survey completion, but most banks never finished. Given the number of questions requiring deep knowledge of the IT/digital strategy and FinTech-related processes in their respective banks, and the lack of top management employees dedicated to those subjects, many potential respondents might not have been able to complete the survey without recourse to information from multiple departments and hence decided to forego completion.

Very low level of FinTech ownership by the banks coupled with lack of Board-level expertise in FinTech or digital strategy runs contrary to global FinTech acceptance trend by banks. Ukrainian banks seem not to see FinTech or digital transformation as an opportunity, but rather as a ‘parallel universe’.
Key Findings: Bank Respondents

Key Findings: Profiling - Profile Summary

- Universal bank
- Employs people for cooperation with third-party software development
- Has little specific Board-level FinTech expertise or understanding
- Has no equity in third-party FinTech organizations
Key Findings: Bank Respondents

Digitalization of services

The banks were asked to detail their current and planned provision of digital and online services.

100% of the respondents said they are providing or planning to provide deposits and other products remotely. Other digital services the respondents offer or planning to offer - are Internet banking-based payments for utilities and other services for individuals, online conclusion of contracts, foreign currency exchange for individuals as part of their online banking services and direct payments from bank accounts in online stores.

The appearance of the last option (direct payments from bank accounts in online stores) in the Top-5, however, should be viewed cautiously. This service is nonexistent in Ukraine today and to create it a partnership of several big banks and significant investments are needed. Accordingly, given the number of 'offer now' answers, the respondents may either have misunderstood the question or have it on their 'wish lists' rather than in immediate implementation plans.
Key Findings: Bank Respondents

Digitalization of services (continued)

In addition, over 80% of banks are offering or planning to offer remote client identification. The least popular services on the list were certification of electronic keys and stamps and purchase of treasury bonds by individuals through internet banking capacities - none of the respondents are offering those services now, though circa 40% are planning to do so in the future.

None of the respondents issue e-money. At that, 42.9% of the respondents offer e-wallet services, but all of the offerings are international brands (Apple Pay, Android Pay).

Insight Analysis: Commercial banks in Ukraine generally follow the mass market demand trend when devising and launching digitalized services for customers. Accordingly, the most popular digital/remote customer services offered by the banks to retail and SME segments are focused on the day-to-day needs of the target audience.
Key Findings: Bank Respondents

Key Findings: Operational Insights

IT spending

On average, 60.3% of the respondents’ IT budget for 2019 is directed towards support of existing infrastructure. With the exception of two outliers, the stated numbers were very close among the respondents, ranging from 50 to 75%. Just 18.7% on average are devoted to investments in new software infrastructure – again, with the exception of two outliers, the stated numbers were relatively close in the range of 5-25%.

14.1% on average are invested into hardware infrastructure, with the bulk of answers within the range of 10-20%. Finally, only 6.9% on average of the banks’ IT budgets are directed towards strategy, business-process development and planning – 64% of answers declaring 10% for this budget item.

When applying the Mode approach to the answers (the most frequent number in the array of answers), the budget breakdown structure is the following: 50/20/20/10. This might be a better proxy for estimating budget structures of the overall banking system, as it removes outlier influence and focuses on the most frequently cited data.
Key Findings: Bank Respondents

Key Findings: Operational Insights

IT spending (continued)

The majority of banks invest in strategy, business-process development and planning as well as support existing and develop new hardware infrastructure on their own. Half of the respondents involve external providers or consultants to modernize new software infrastructure.

Insight Analysis: Global data on break-down of IT budgets between support of legacy systems and investments into new capabilities is hard to find. However, there is an expert consensus that for mid-sized banks, investment into ‘strategic technologies’ falls within the range of 25-35% of the overall IT budgets. The results of our survey are then more or less in line with the global trend.

What is definitely against the trend is the fact that most of the IT work is being done using internal resources of the banks - especially in the strategy and planning improvements area, which globally is typically referred to third-party support. The global banking system is progressively outsourcing to reduce costs and enhance expertise - yet the Ukrainian banks are keeping things in-house, most likely attributed to cheaper workforce costs compared to third-party provider fees.
The key bank IT systems that were (FY2018) or are (FY2019) the focus of modernization and update include client-bank systems for corporate customers, online banking for individuals, core banking systems, mobile banking and integration of individual systems. Over 70% of the respondents indicated these systems have undergone modernization (or will in the near future). E-wallet was of low interest, with only a third of respondents invested or planning to invest into the function this financial year.

Core banking and client-bank systems for corporate clients were the most popular functions to be modernized using Ukrainian third-party software suppliers followed by internet banking and mobile banking applications.

**Insight Analysis:** On all but two items (CBS and Processing) updates or plans thereof during the current financial year were shown by a larger number of respondents compared to last FY, hinting at greater urgency in regards to modernization of key systems. The overall bias of choice towards Ukrainian software suppliers is also highly noticeable and shows there are enough competitive local solutions for banks.
Regarding processes, internal modernization or update is focused predominantly on the following areas: cybersecurity, mandatory reporting and compliance, online onboarding, data analytics for fraud prevention, management accounting and sales support. Investment into these categories has been or is planned in the near future by over 70% of the respondents.

In 2019-2020, cybersecurity, mandatory reporting and compliance along with data analytics remain the top priority directions for modernization. However, there is an intention to update services related to the acceptance of applications for financial products via electronic channels. Most banks are planning to do this with the help of the Ukrainian suppliers.

**Insight Analysis:** Again, higher urgency to modernize functionality of services and processes year-on-year is also noticeable here. As bureaucratic as the traditional commercial banks are, the realization that the digital era is here and they need to adapt and follow the trends is catching up to them. Dependency on Ukrainian suppliers is lower in this set of options, most likely attributable to lesser number of locally developed software available for such functionalities and higher capabilities of internal IT resources to create in-house solutions.
Key Findings: Bank Respondents

Key Findings: Operational Insights

IT spending (continued)

In other notable IT-related insights, none of the respondents are using or planning to implement Distributed Ledger Technology solutions. Given that DLT/Blockchain implementation in banking environments is gaining strong popularity globally, Ukrainian banks are lagging behind the trend.

Use of cloud solutions is very limited. Less than 10% of the respondents keep over 40% of their services in either a private or public cloud, with an absolute majority keeping from 0% to 20% of the services in the cloud. Again, this runs contrary to the global trends which see major and mid-sized banks increasingly moving their services, processes and functions to the cloud.

What is the share of services your bank keeps in a private or public cloud?

<table>
<thead>
<tr>
<th>Private cloud:</th>
<th>Public cloud:</th>
</tr>
</thead>
<tbody>
<tr>
<td>80% banks</td>
<td>63.6% banks</td>
</tr>
<tr>
<td>0-20% services</td>
<td>0-20% services</td>
</tr>
</tbody>
</table>

Does your bank plan introduction of DLT (distributed ledger technology) infrastructure in the near future?

- No 100%
Key Findings: Bank Respondents

Key Findings: Operational Insights

Does your bank use third-party suppliers / FinTech providers in the following areas?

Cooperation with third-party software and FinTech solution providers

Cooperation with FinTech solution providers is limited. Card payments is the only third-party service that is systemically in demand by the banks-respondents with 85.7% of the respondents cooperating with third-party providers (71.4% of them are using local providers). Back office software development and maintenance is being done by third-party providers at 57.1% of the respondents. Automation of business processes is the least outsourced solution with only 14.3% of the respondents engaging third-party providers (and none of those providers are local).
Key Findings: Bank Respondents

Key Findings: Opinion Insights

Need for legislative changes

The respondents were asked to provide an opinion on the most critical legislative changes required for development of the FinTech sector in Ukraine. Of the 16 options offered, **introduction of legal framework for remote client identification** and **encouragement of payments by and to government agencies through digital channels** were deemed the most important with a WSI of 35.8% and 17.85%, respectively.

Banks also had an opportunity to indicate any other legislative initiatives which they consider as important to enable digital finance. Surprisingly, no additional answers were provided by any of the respondents.

Non-existent services with best development potential in Ukraine

When asked to grade FinTech services that are non-existent or limited on the Ukrainian market for their development potential, no consensus emerged, with WSI values for all the options being below 0%. At that, the most positive weighted reaction was attained by the direct from account online payments (systems similar to Trustly, iDEAL, Sofort et al.).

For several of the “Opinion” questions on the survey, the participants were asked to grade the importance of an issue from 1 to 5, where 1 meant minimum importance and 5 – maximum importance. This has provided us with a graded sentiment distribution.

Accordingly, we have used proprietary methodology to calculate a **Weighted Sentiment Index (WSI)** on each such question. We normalized the indices, so that they fit into a scale from -100% to 100%, where -100 means the ultimate respondent consensus of non-importance and 100% means ultimate respondent consensus of importance. This allowed us to compare the weighted sentiments between various options provided to respondents for grading.

Top-5 most sought legislative changes for FinTech development in Ukraine

1st: Remote client identification
2nd: Government agencies payments via digital channels
3rd: Implementation of GDPR
4th: Regulation of P2P loans
5th: Rules and standards for outsourcing processes
Key Findings: Bank Respondents

Digitalization challenges for banks

The respondents were asked about their opinion on the biggest challenges to digital transformation for their bank. Cost of digital transformation was an undoubted winner with a WSI value of 53.6%. All other options have shown no consensus, with the WSI values being below 0%. Of these, complexity of key business processes has the highest WSI value, followed by outdated adverse legislation and fears that investing in this process will not increase the bank's revenue.

Importantly, the option ‘No demand for digital transformation by shareholders and/or management’ was almost unanimously seen as the least of the challenges.

**Insight Analysis:** We believe this consensus answer highlighting cost of digital transformation as the most important barrier to going digital is key to understanding the overall sentiment of the banks in Ukraine towards digitalization and rest of the answers to the questions in this survey.

With a few notable exceptions, Ukrainian bank leaders view digital transformation as prohibitively expensive, especially compared to the short-term benefits. Beyond the top-20 banks, the rest are rarely pushed forward by competition and rarely cater to the younger generation of clients that now see digital as a pre-requisite. The fight for SME clients is even less noticeable - another group looking to digital solutions and services - as SMEs were historically considered riskier clients compared to both individuals and large corporate customers.

**Top major challenges for digital transformation within the bank**

1. **Cost of digital transformation** - 53.6%
2. **Complexity of key business processes**
3. **Outdated adverse legislation**
4. **Investment won’t lead to increase in profits**

**Insight Analysis (continued):** The other factor is that while being cheaper than foreign alternatives, local IT solutions for banks are still costly. While the costs are smaller but still comparable to foreign counterparts, the actual IT budgets of the Ukrainian banks are dramatically lower. Only a handful of respondents have stated 2019 IT budget values - a statistically insignificant result - but even from those few answers the average IT budget seems to be within UAH10-15m (US$400-600t at current exchange rates) for mid-sized banks. This is not enough to push digital transformation forward - especially when over 50% of that amount goes to support of existing IT infrastructure.
Key Findings: Bank Respondents

Other notable insights

85.7% of the respondents said they believe liberalization of the foreign exchange market in Ukraine created opportunities for development of new FinTech services.

78.6% of the respondents do not view the FinTech sector as a threat to their bank. Some respondents, who believe FinTech advancements could pose a threat to their Bank in the near future, mentioned that traditional banks may be unable to compete with FinTech players due to more stringent regulatory requirements for banks.

Insight Analysis: The result of this ‘is FinTech a threat’ question suggests that traditional banks in Ukraine tend to underestimate new trends and the innovation culture. As mentioned in the Global Trends section of this report, 88% of global financial service providers do believe their market share is under pressure from FinTech innovators and are looking at opportunities to incorporate those innovations into their own businesses. On the contrary, Ukrainian banks, with a few notable exceptions, neither understand the threat, nor have the strategies in place to deal with it.

Also, interestingly, none of the respondents who do have at least one Board member with expertise in FinTechs or digital transformation, see FinTech sector development as a threat. This may be attributed to two key sentiments: 1) either those respondents based on their expertise do not believe local FinTech offerings are strong enough to be a threat or 2) provided all these banks are focused on digital transformation (as mentioned in the Profiling section), they consider their own current and future capabilities competitive enough to fight off the pressure from third-party FinTechs.

Moreover, none of the banks owned by foreign banking groups see FinTech development as a threat. This may be a confirmation of ‘weak local FinTech solutions’ sentiment in the previous paragraph.
### Comparison of Selected Findings

**FinTechs vs. Banks**

#### List of services/functions that banks automated/updated/added functionality in FY17-18 or planning to do so in FY19-20 most frequently in comparison with processes that FinTechs consider as the top priority for banks

<table>
<thead>
<tr>
<th>FinTechs Opinion</th>
<th>Actual Efforts by Banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1st Remote client identification</td>
<td>1st Cybersecurity</td>
</tr>
<tr>
<td>2nd Data analytics for fraud prevention</td>
<td>2nd Mandatory reporting and compliance</td>
</tr>
<tr>
<td>3rd Cybersecurity</td>
<td>3rd Online onboarding</td>
</tr>
<tr>
<td>4th Customer interaction interfaces</td>
<td>4th Data analytics for fraud prevention</td>
</tr>
<tr>
<td>5th Automation/support for decision-making processes</td>
<td>5th Data analytics: management accounting and analysis, analytical sales assistance, user interface improvements</td>
</tr>
<tr>
<td>6th Automation of business processes</td>
<td>6th Automation/support for decision-making processes</td>
</tr>
<tr>
<td>7th Online onboarding</td>
<td>7th Origination</td>
</tr>
</tbody>
</table>

#### Top FinTech services (non-existent or limited on the Ukrainian market) with best development potential

<table>
<thead>
<tr>
<th>FinTechs Opinion</th>
<th>Banks Opinion</th>
</tr>
</thead>
<tbody>
<tr>
<td>1st Cross-border payments for individuals and SMEs</td>
<td>Internet payments directly from bank accounts (IDEAL, Trusty, Sofort)</td>
</tr>
<tr>
<td>2nd Digital financial services for unbanked - current and savings accounts</td>
<td>Digital financial services for unbanked - current and savings accounts</td>
</tr>
<tr>
<td>3rd E/invoicing</td>
<td>Lending for online purchases (Kiarna)</td>
</tr>
<tr>
<td>4th Internet payments directly from bank accounts (IDEAL, Trusty, Sofort)</td>
<td>Foreign exchange and Forex derivatives for individuals and SMEs</td>
</tr>
<tr>
<td>5th Foreign exchange and Forex derivatives for individuals and SMEs</td>
<td>E/invoicing</td>
</tr>
<tr>
<td>6th Lending for online purchases (Kiarna)</td>
<td>Cross-border payments for individuals and SMEs</td>
</tr>
<tr>
<td>7th Applications for cross-border investments (e.g., purchase of securities)</td>
<td>Applications for cross-border investments (e.g., purchase of securities)</td>
</tr>
</tbody>
</table>
Comparison of Selected Findings
FinTechs vs. Banks

**Insight Analysis:** The difference between FinTech and Bank sentiments and plans on the issues raised within this survey is striking, given they are all part of the same Ukrainian financial services universe. This may partially be attributed to a large number of FinTech organizations operating both in and outside of Ukraine and being exposed to global drivers which aren’t felt so acutely within Ukraine.

Importantly, both FinTechs and banks see the need for enabling remote client identification, as the most important legislative change required given the current market demand. This, at least partly, shows the banks are forced to attune their offerings to the growing mobile banking demand and see this as a necessary competitive factor. Again, this might be in part due to the bank respondents being some of the more progressive and receptive to change on the market.

Improvements in cybersecurity processes within banks and fraud prevention analytics are also seen as highly important by both groups.

Finally, and maybe, most importantly, both FinTechs and banks see major potential in future projects focused on financial services for the unbanked – a lucrative niche for new FinTech offerings both from independent parties and incumbents.

At that, unfortunately, development of applications for cross-border investments is not interesting for both sides - meaning the FinTech market and the demand trends in Ukraine are still far from a developed stage.

| Top-7 most sought legislative changes for FinTech development in Ukraine |
|---|---|
| **FinTechs Opinion** | **Banks Opinion** |
| 1st | Remote client identification | Remote client identification |
| 2nd | 2nd Payment Services Directive (PSD2) | Encouragement of digital payments to and by government agencies |
| 3rd | E-money legislation | Implementation of GDPR |
| 4th | New payment services licensing: PIS and AIS | Regulation of P2P loans |
| 5th | Cybersecurity rules and standards | Rules and standards for outsourcing |
| 6th | Simplification of payment systems registration rules | Cybersecurity rules and standards |
| 7th | Consumer rights protection | 2nd Payment Services Directive (PSD2) |
The results of the survey are fascinating. Convergence of the traditional banking sector incumbents and the agile FinTechs is obviously still a long way off, but the reason for this is split equally between the respective sectors.

Let’s take a look at banks first. As it happens, historically almost none of the Ukrainian banks were set up as a banking business. The unwieldy state-owned banks served as deposit guzzlers, savings centers and political financing vehicles. Some banks were private operations of financial-industrial groups (FIGs) and classic money laundering “machines.” None of these banks ever had corporate and consumer clients at the core of their business strategy.

With foreign banking groups establishing a strong foothold in the market, the overall approach changed somewhat and the competition for “peoples’ money” multiplied. Coupled with a dramatic clear-out of non-performing and “pocket” banks, the drive for customer centricity is now visible. Yet traditional operational models are notoriously hard to revamp and, as a result, the old is still wary of the new.

On the other hand, Ukrainian FinTechs are a fascinating animal. Given the size of the country and the population, one would expect a much higher number of projects operating on the market and greater focus on the consumer audience. Yet, less than 100 projects are in existence including the infrastructure enablers, and most are focused on the corporate market.

This state of affairs is a function of several factors: general distrust of financial services coupled with an overall lack of financial literacy, lack of capital for development, reluctance of the bank incumbents and private corporates to embrace these new technologies and approaches, and the near-absence of capital markets in the country. Together, this spells “weak internal market”.

We are often asked why, with a high-tech sector workforce of over 200,000 people (a huge talent pool), there are so few properly developed “scale-ups” - startups several years in operation with proven business models and reasonably sizable revenues - to invest into in Ukraine.

Weak internal market is the answer. With weak demand and disposable income locally, it is notoriously hard to validate business models and start earning. Those startups are then forced to try their hand in foreign markets - and penetrating these markets without a proven business case at home and very limited funding for marketing is equally difficult. Marketing funding means a need for third-party investor capital - and investors are not keen to invest into unproven business models. A vicious cycle, broken by only a handful of entrepreneurs riding on a mix of own funding, progressive customer-centric thinking and a stroke of luck.

Given those adverse market conditions, we believe the number of FinTechs on the market (however small in absolute numbers) and their scaling velocity should be viewed as a definite win and a clear path in the right direction.
Afterword (continued)

Reform of the legal framework is absolutely critical - in more ways than one:

**Harmonization.** Implementation of the 2nd EU Payment Services Directive is absolutely necessary to provide the legal and technological framework for a number of FinTech services not existing in Ukraine. In particular, the open banking concept is only possible by legally forcing banks to open their APIs and hence, client data, to third-party service providers. Remote client identification - a feature most survey respondents focused on - will also be enabled by PSD2.

This may also help in solving the Ukrainian ‘unbanked’ and rural/small town residents challenges - making provision of financial services to these categories much more mobile and less costly and generally involving them in the market.

**Sandbox approach.** The ‘regulatory sandbox’ concept hinted upon by the Ukrainian authorities is a great way to stimulate rapid development of the FinTech projects by lowering law infringement risk and allowing business model validation. At that, proper implementation steps need to be taken first, before the FinTech market gains enough trust in the initiative. The NBU innovation hub question results are a good proxy of just how low that trust currently is to any initiative from the regulators.

**Access to capital.** FinTech development is in dire need of external capital sources. However, in addition to the ‘weak internal market’ catch discussed earlier, investors also perceive Ukrainian-based projects as having a high risk profile, even for venture capital - mostly due to imperfect intellectual property rights protection and judicial system risks. These need to be urgently addressed - otherwise, the best projects will continue to relocate out of Ukraine, reducing competition and quality of the FinTech offerings available locally.

**Crypto/alternative currency market.** A number of survey participants voiced the need for a proper crypto-related legal framework. While still a challenge even for better developed markets, that framework is needed in order to bring numerous crypto infrastructure projects into a legal field and allow them to interconnect with the more traditional financial service providers.

Just as important, however, is continuous work by all stakeholders to find common ground and learn from each other. Banks need to face the reality of the digital era and start building long-term tech-focused strategies, even if that means a margin squeeze in the short term. FinTechs need to stop overestimating themselves and share expertise with the incumbents - both camps will benefit from mutual support. Right now, market growth is less about cutthroat competition and more about raising mutual awareness of the challenges on hand and tech that might solve them.

With improved access to capital, stabilizing economy, actualization of the legislative framework and a growing number of traditional financial services players endearing themselves to the new technologies, we will, most likely, experience rapid growth of the sector - which is already outperforming any other high-tech industry in the Ukrainian market.

The momentum is building and key stakeholder will seems to be there - it is time to put the proverbial foot on the gas.
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The USAID Financial Sector Transformation Project (October 2016 through December 2020) supports financial sector reform in Ukraine and provides assistance in the following areas: building trust in the banking sector, legal and regulatory reform, increasing access to finance in the non-bank financial sector; expanding digital finance solutions; and promoting financial inclusion and consumer protection. For more information about the USAID Financial Sector Transformation Project and its activities, please visit its landing page at: http://www.fst-ua.info/en/ and its Facebook page at: https://www.facebook.com/FSTProject.

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