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Covid-19: Impact and Response for the Fintech Industry in the United States, the United Kingdom and Europe

Diana Milanesi

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Abstract

Faced by an unprecedented crisis induced by the outbreak of the coronavirus ("Covid-19"), many financial technology ("fintech") companies have come under pressure on a number of fronts over the past 6 months. From lending and insurance to banking, payments and wealth management, fintech companies across every vertical have worked around the clock to improve efficiency, build up capital and liquidity and extend their cash runway. They have displayed resolve and resilience, moving rapidly to protect the health of their employees and customers and ensure the continuity of their services. They have examined their burn rates, implemented significant costs cutting measures and curtailed any spending that wasn't core to their business. At the same time, they have increasingly concentrated on key business metrics, monitored leading business indicators more closely and focused more on profitability and positive cash-flow than growth at all costs. Flexibility and validation in business models, strong management teams and the ability to dial-up/down costs have become critical. A number of fintech companies have also re-considered their strategy and re-focused on their core product roadmap, customer services and mission to best navigate the Covid-19 crisis and prepare for its downstream impact. Inspiring examples of fintech innovation have been witnessed across a variety of sectors, with fintech companies strengthening their capabilities and even launching new products and services to support individuals' and communities' health, business activities and economic productivity.

Access to funding has progressively contracted in the first half of 2020, especially for early-stage fintech companies, as a number of venture capital (VC) investors have pulled back on early-stage investments and focused on supporting their existing portfolio companies to ensure they have enough cash runway to weather the projected recession. When they have made new investments, investors have shown an increasing preference for more mature fintech companies with established business models, a clear path to profitability and sustainable cash flows. Investors have also grown far more cautious with their investments theses and terms, have raised their standards in diligence and have amplified their scrutiny on companies' burn rates and financials. Deal terms have gradually shifted in favor of investors, while eye-watering valuations driven by (often optimistic) assumptions about future growth, profits and exits have been questioned. Down-rounds, hybrid rounds and convertibles have increased as a proportion of the overall funding deals. As the Covid-19 induced market downturn stretches into the second half of 2020, investors will likely remain cautious to get straight back in. Investment committees are expected to become more discerning in their focus and about the companies they can continue funding or should pass as they seek safety with increased flight to quality. Before making major capital available for new investments, investors will first want to deepen their understanding of companies that are best positioned to thrive in the new global economy that is starting to emerge, available consolidation opportunities in the market and how market consumption and engagement will look like post Covid-19 crisis.

In addition, the unprecedented changes in the economic outlook triggered by the outbreak of Covid-19 have rapidly closed down IPO windows for a number of fintech companies and their investors in the first half of 2020, thus forcing a realistic re-assessment of their exit strategy. On the contrary, the same period has been

particularly active for fintech M&As, with fintech companies buying banks, large fintech companies buying emerging players, established financial institutions acquiring high growth fintech companies and established firms combining for scale.

Against the described background, the Covid-19 crisis has led to an unprecedented governmental assistance on a global scale. Among the various initiatives adopted in response to the crisis, governments in the United States, the United Kingdom and Europe have released a number of extraordinary funding support measures of interest to fintech companies. These measures are intended to mitigate the financial impact of the Covid-19 crisis and ensure that companies in some of the most dynamic and innovative sectors receive the investment and liquidity they need to weather the crisis and continue to grow their activities and innovate.

Although we are still in the midst of the Covid-19 crisis, the past few months have already promoted significant developments and provided important signals of what could change further in the fintech industry in the coming months. Social distancing and lockdown measures imposed to prevent the spread and mitigate the impact of Covid-19 have triggered significant changes in consumer behavior, have enhanced a shift towards a “cashless” economy and have triggered a tremendous growth in the use of digital payment solutions. These measures have also amplified the focus on user experience and have accelerated a wider-scale adoption of financial technology through online and mobile channels to conduct banking activities and perform a variety of financial transactions. The combination of these developments has created new opportunities for fintech companies to improve customer acquisition, engagement and retention, drive further efficiency and innovation and prove their differentiated value proposition versus more traditional players in the banking and financial industry.

Actions in the coming months will have a significant impact on performance trajectories for the years ahead. Looking further out, fintech companies will need to examine their core business models and evolve their value propositions to forge a new path forward and stay relevant to their customers. Bold vision and disciplined execution will be key. Fintech companies that went far and beyond to support customers and increased their pace of innovation despite the difficult times are most likely to thrive, see continued customer loyalty and seize new opportunities once the Covid-19 crisis has settled. Only fintech companies that build sufficient resilience and agility and that demonstrate a great ability to evolve their offerings and organizations will be able to drive renewed growth and long-term profitability.

The changes brought by the Covid-19 crisis will likely contribute to reshape the structure of the fintech industry, as well. As the broader economy gradually shifts from respond to recover, leaner organizations are expected to emerge and thrive. The contracting funding environment and reduced revenue streams in the near- to medium-term may force a number of fintech companies to seek growth and cost synergies through collaborations and partnerships with other fintech companies, large tech companies, as well as financial and non-financial strategic players. A number of companies have already begun to strengthen their position in the market and take advantage of the current economic conditions through corporate activities. As valuations materially re-set, fintech M&As are expected to accelerate and the fintech industry is set to become an even more fertile territory for acquisitions and consolidation.

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PREFACE

Fintech companies across all verticals have taken significant steps to manage through the uncertainty and the economic crisis triggered by the Covid-19 outbreak. They have concentrated their efforts on their more robust lines of business and have implemented a wide variety of cost-saving measures, including through workforce reduction. They have increasingly focused on key business metrics, have built up liquidity and capital reserves and have monitored key business and financial indicators more closely. A number of fintech companies have also re-assessed and evolved their strategy, diversified their revenues sources and even pivoted their business in order to survive the economic downturn triggered by the Covid-19 pandemic.

As lockdown and social distancing measures to control the Covid-19 pandemic have taken hold worldwide, there has been an enormous growth in the adoption and usage of online and mobile banking and financial services. The Covid-19 pandemic has also forced many people who normally used cash to rapidly switch to contactless payments and digital payment solutions, thus accelerating the movement towards a "cashless" society. While restrictions are now gradually lifted, banking and financial services are expected to see more long-lasting changes as customers and businesses carry on embracing the digital methods that they have been adopting to a greater extent during the period of Covid-19 outbreak. These changes are expected to reshape the banking and financial services industry and foster the development and growth of new and transformative fintech solutions.

Against this background, this paper analyses the impact on fintech of the crisis induced by the outbreak of Covid-19 and the response of the fintech industry across three main geographic areas – the United States, the United Kingdom and Europe. The paper is organized as follows:

- Chapter 1 examines the effect of the Covid-19 crisis on the fintech financing;
- Chapter 2 discusses the short-term and long-term effects of the Covid-19 crisis on five main sectors of the fintech ecosystem: payments, banking, lending, wealth management and capital markets and insurance;
- Chapter 3 provides an overview of certain Covid-19 governmental funding support measures of interest to fintech companies, which have been implemented in the United States, the United Kingdom and Europe; and
- Chapter 4 outlines how the changes brought by the Covid-19 crisis will act as a powerful catalyst for further fintech innovation, will likely contribute to reshape the structure of the fintech industry and will create new opportunities for fintech companies.

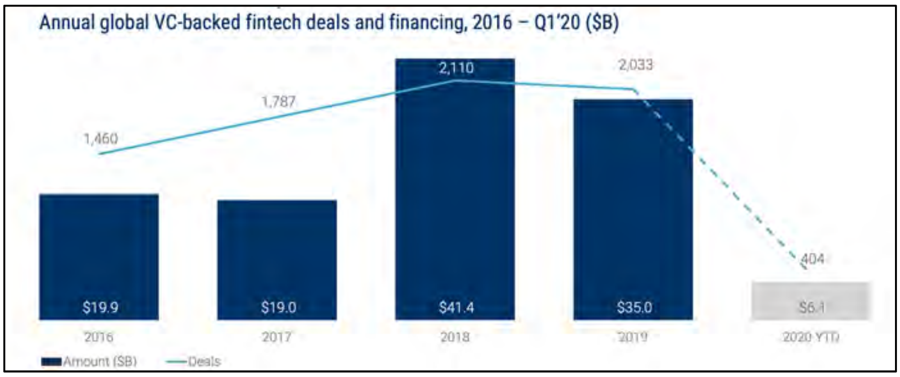
CHAPTER 1

THE IMPACT OF THE COVID-19 CRISIS ON THE FINTECH FINANCING

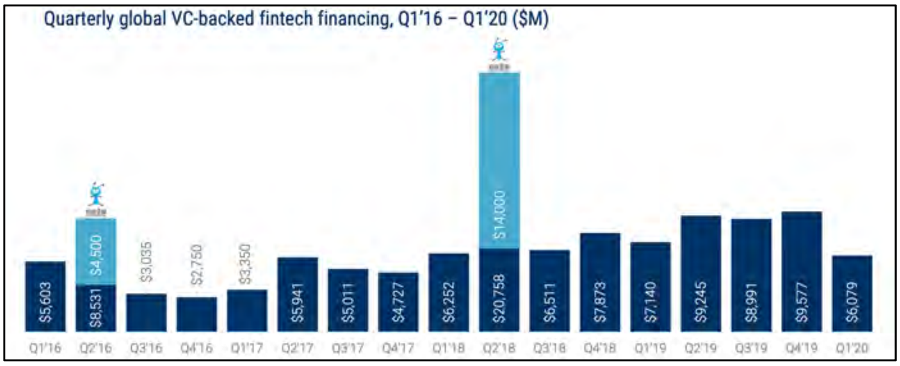
1.1. H1 2020 Fintech Financing: Deal Value and Activity through the Covid-19 Pandemic

The Covid-19 pandemic has had a significant impact on the fintech financing both in terms of number of deals and value. Investor appetite for fintech companies decreased as Covid-19 spread in Q1'20, resulting in Q1'20 being one of the worst quarters in 2 years for venture capital (VC) backed fintech companies.

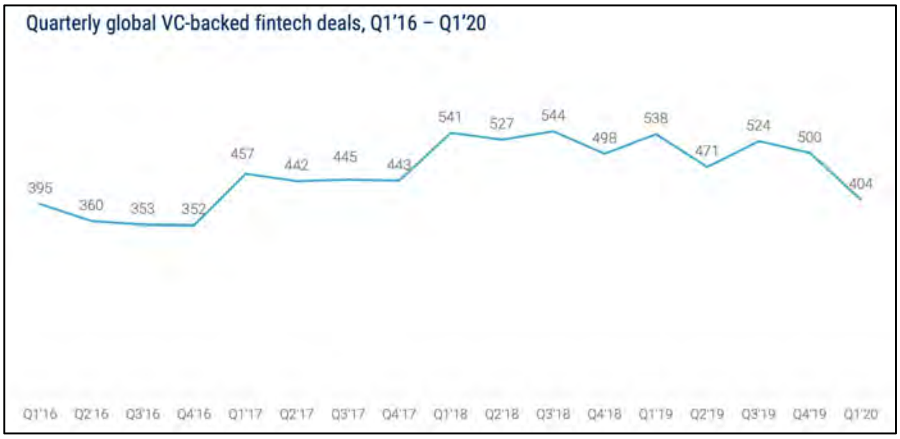
VC-backed fintech activity dropped to $6.1 billion across 404 deals in Q1'20, the worst Q1 since 2016 for fintech deals and the worst Q1 for funding since 2017.



Source: CB Insights, The State of Fintech Q1'20 Report: Investment & Sector Trends to Watch (May 2020).



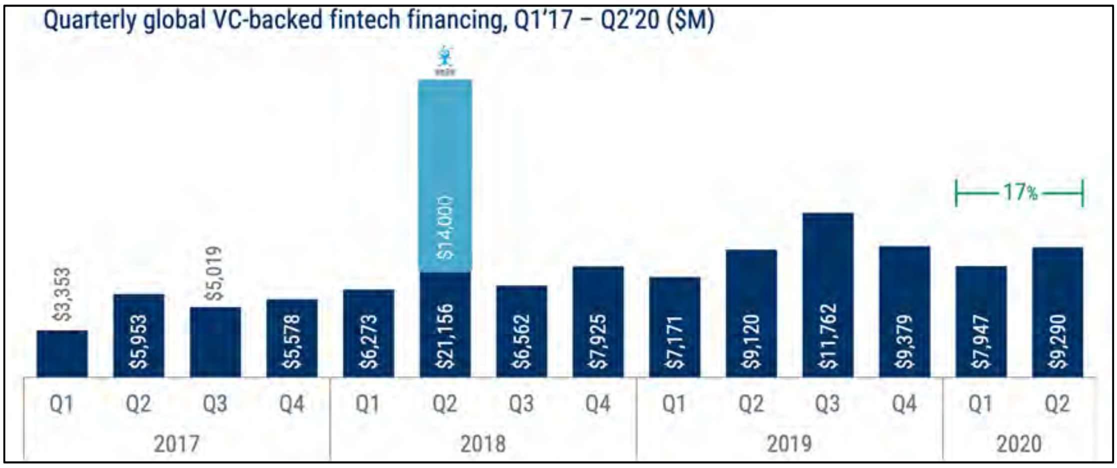
Source: CB Insights, The State of Fintech Q1'20 Report: Investment & Sector Trends to Watch (May 2020).



Source: CB Insights, The State of Fintech Q1'20 Report: Investment & Sector Trends to Watch (May 2020).

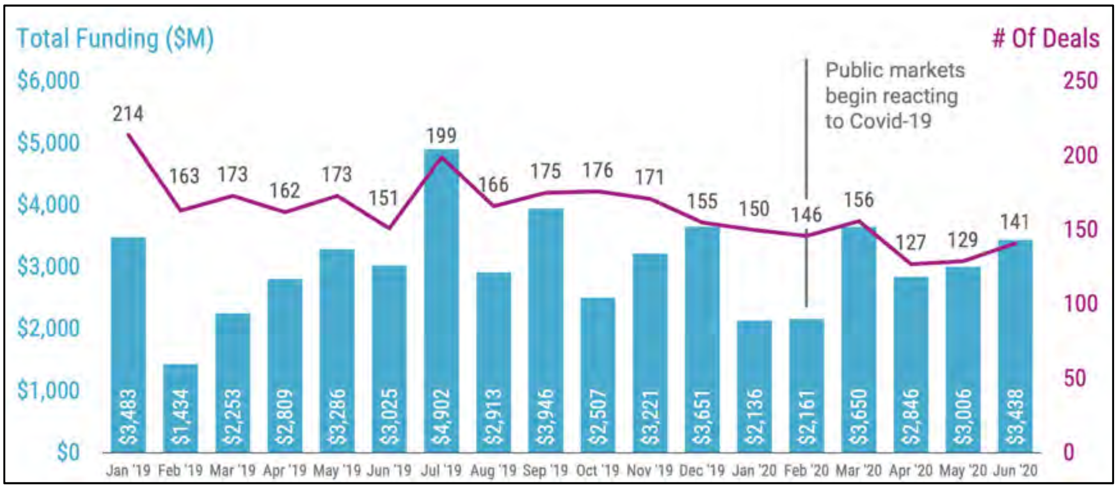
The ramifications of Covid-19 kept the fintech landscape on a holding pattern in Q1'20. A number of VC investors have delayed investments while trying to get a better understanding of the short- and longer-term impact of Covid-19 and the resulting economic downturn. The decrease in deal flow and value in Q1'20 reflects the broader market uncertainty and perceived challenging times ahead.

Fintech funding slightly rebounded in Q2'20, increasing 17% quarter-over-quarter (QoQ) to $9.3B in Q2'20.



Source: CB Insights, The State of Fintech Q2'20 Report: Investment & Sector Trends to Watch (August 2020).

However, monthly deal activity continued to fall, hitting a new low of 127 deals in April 2020 before picking up in June 2020, which recorded 141 deals. The quarterly deal activity continued its decline which began pre-pandemic in Q4'19.



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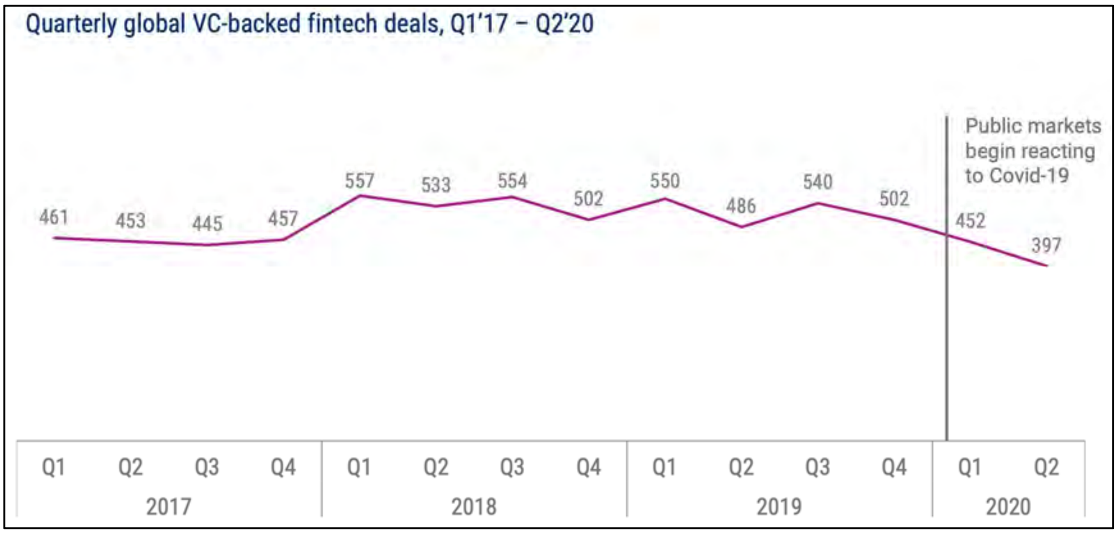
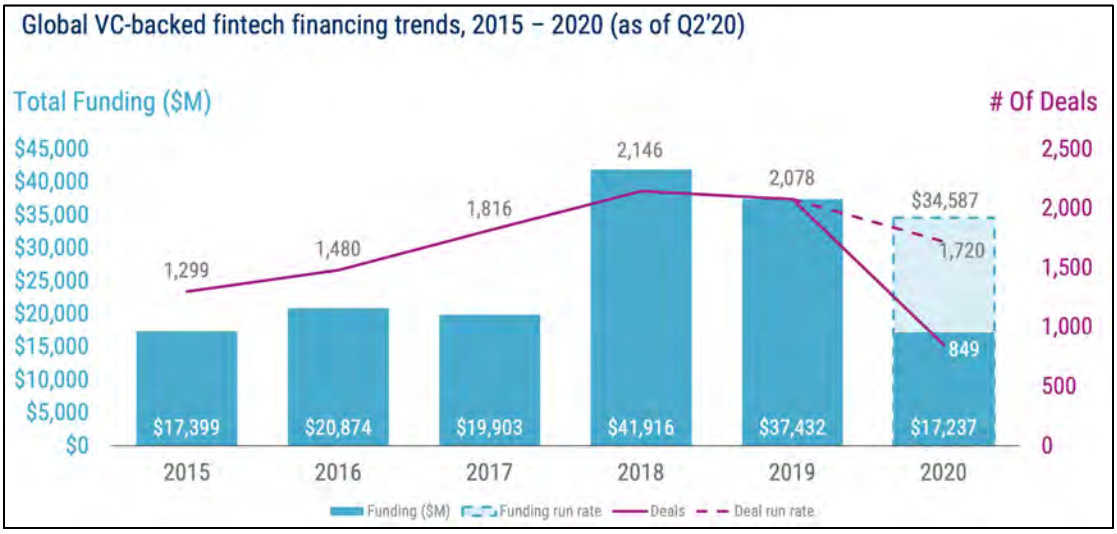


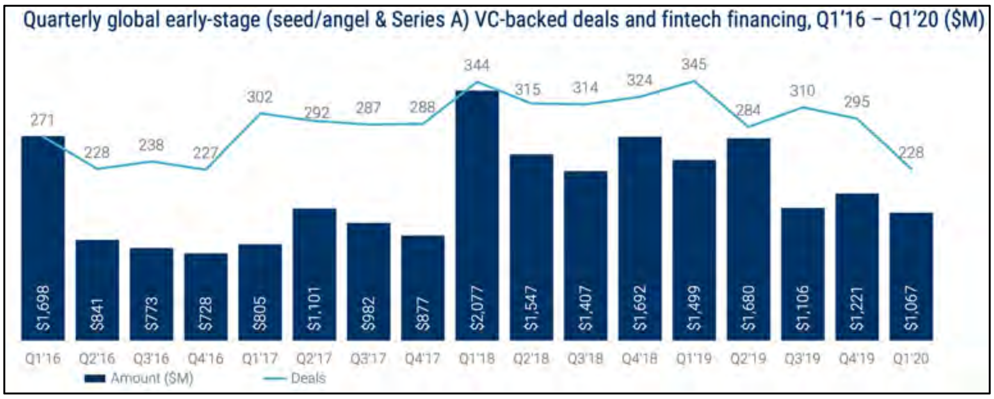
Source: CB Insights, The State of Fintech Q2'20 Report: Investment & Sector Trends to Watch (August 2020).

Overall annualized deals and dollars fall to pre-2018 levels.

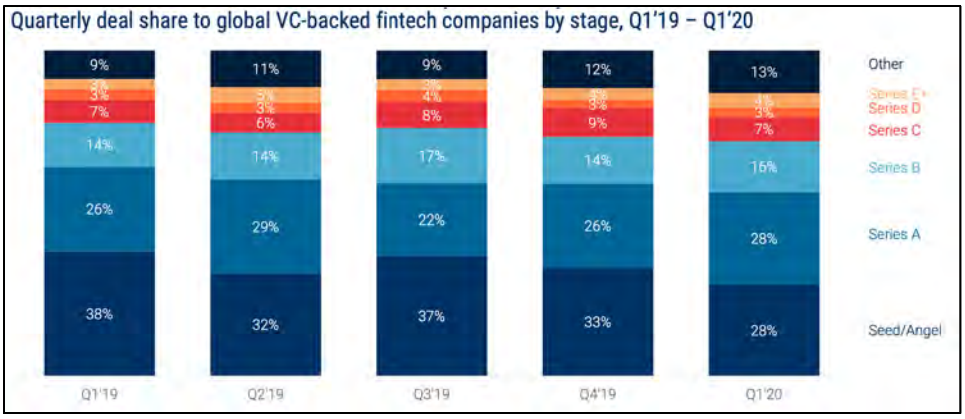


Source: CB Insights, The State of Fintech Q2'20 Report: Investment & Sector Trends to Watch (August 2020).

In particular, the economic shocks caused by the outbreak of Covid-19 have reduced investor appetite for early-stage (seed and Series A) investments. In Q1'20 early-stage fintech startups recorded a total of 228 deals (a 13-quarter low) and $1.1 billion of funding (a 9-quarter low). Investors have gradually pulled back on early-stage investments and shifted their focus from making new bets to supporting their existing portfolio companies, ensuring they have enough cash runway to weather the projected recession. When they have made new investments, investors have focused less on seed and Series A companies and have shown an increasing preference for more established fintech companies with solid business models, a clear path to profitability and sustainable cash flows.

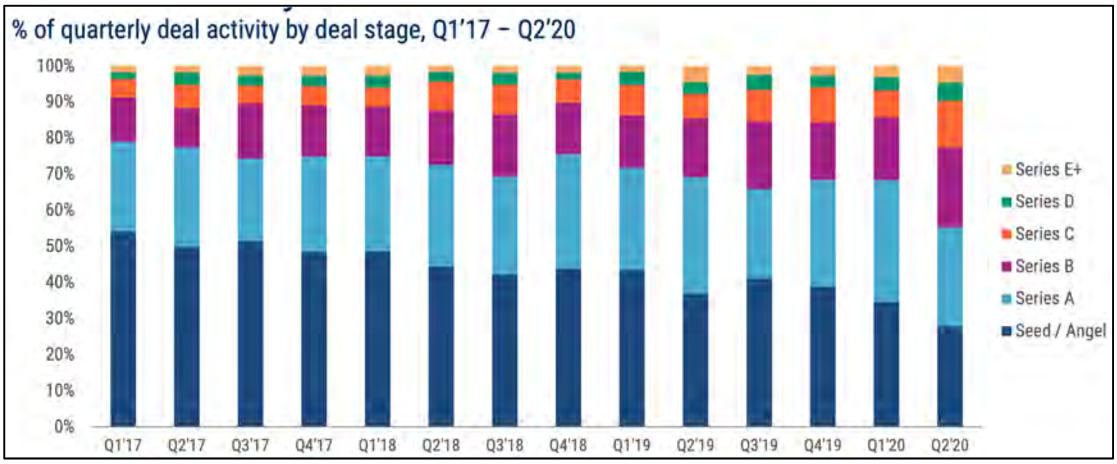


Source: CB Insights, The State of Fintech Q1'20 Report: Investment & Sector Trends to Watch (May 2020).



Source: CB Insights, The State of Fintech Q1'20 Report: Investment & Sector Trends to Watch (May 2020).

The decline in early stage investments continued in Q2'20, which recorded the largest decline in seed and angel deals since Q2'19.



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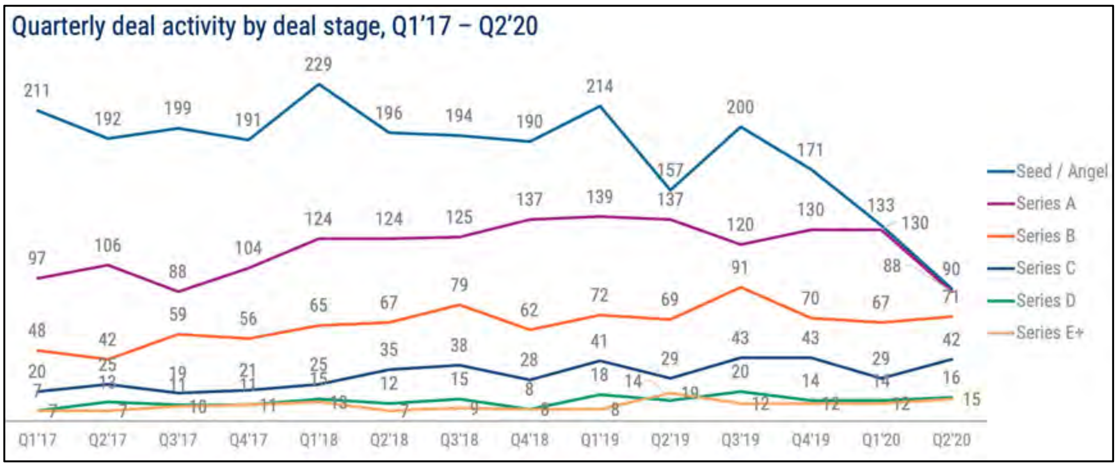
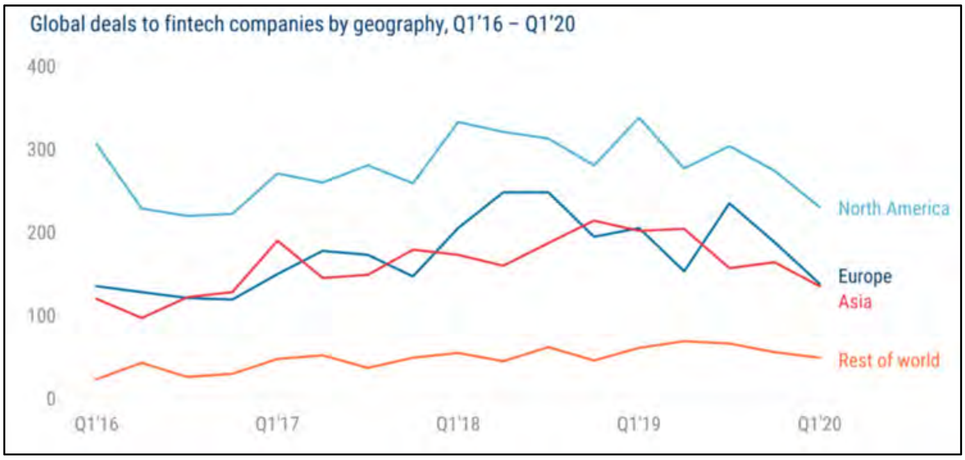


Source: CB Insights, The State of Fintech Q2'20 Report: Investment & Sector Trends to Watch (August 2020).

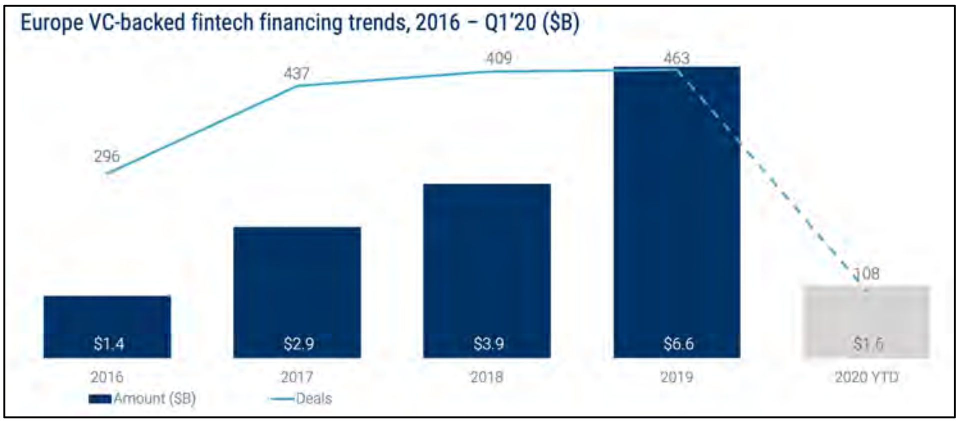
1.2. Regional Trends: Fintech Funding in the United States, the United Kingdom and Europe

Fintech VC-backed equity funding felt across geographies in Q1'20, reflecting the global impact of Covid-19 on the fintech sector.

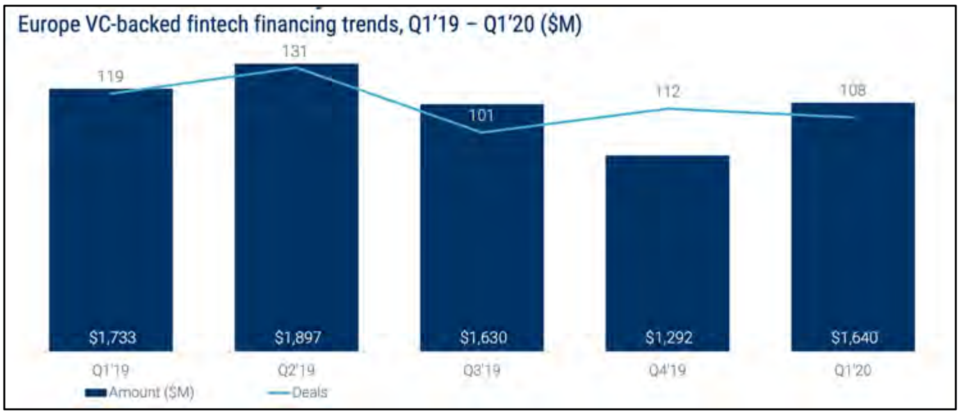


Source: CB Insights

The impact of the Covid-19 crisis in Europe was somewhat muffled due to a strong pipeline of deals in most jurisdictions. After a record 2019, fintech VC-backed equity funding activity stabilized in Europe in Q1'20. The quarter saw a total of 108 deals for aggregate $1.6 billion.

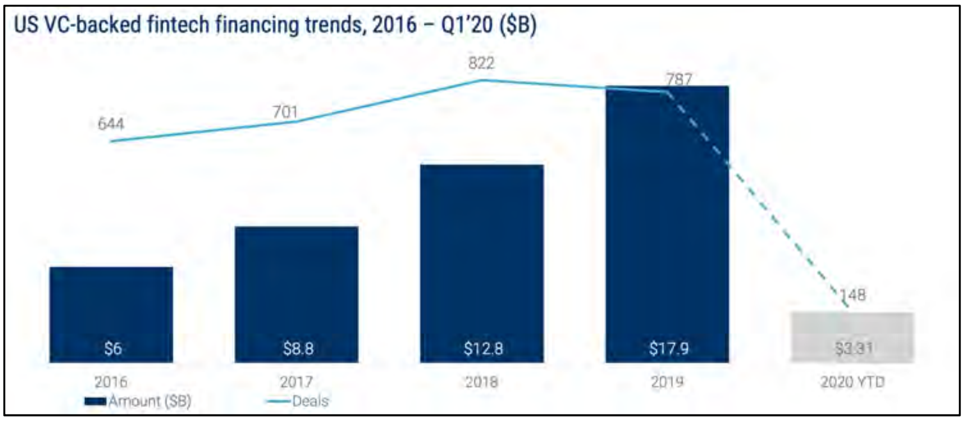


Source: CB Insights, The State of Fintech Q1'20 Report: Investment & Sector Trends to Watch (May 2020).



Source: CB Insights, The State of Fintech Q1'20 Report: Investment & Sector Trends to Watch (May 2020).

US fintech VC-backed equity funding activity dropped in Q1'20, with a total of 148 deals (a 23% decrease quarter on quarter) for aggregate $3.3 billion, the lowest quarterly performance since Q3'18.



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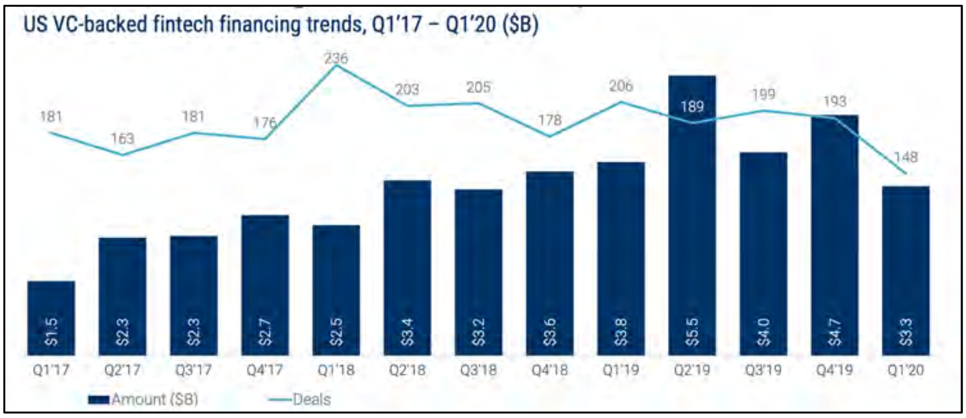
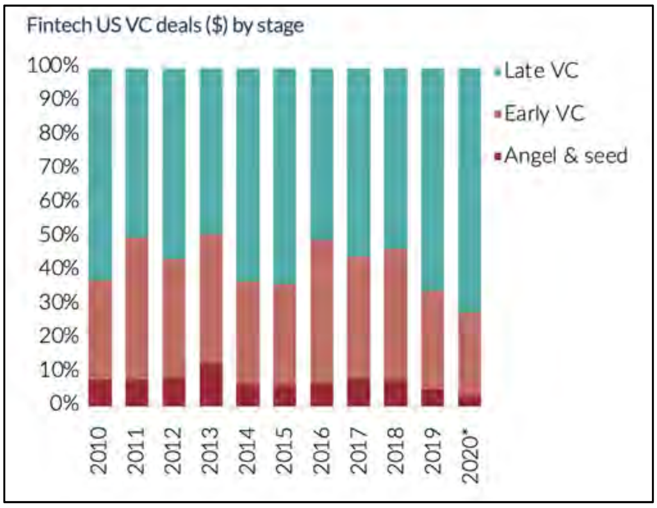


Source: CB Insights, The State of Fintech Q1'20 Report: Investment & Sector Trends to Watch (May 2020).

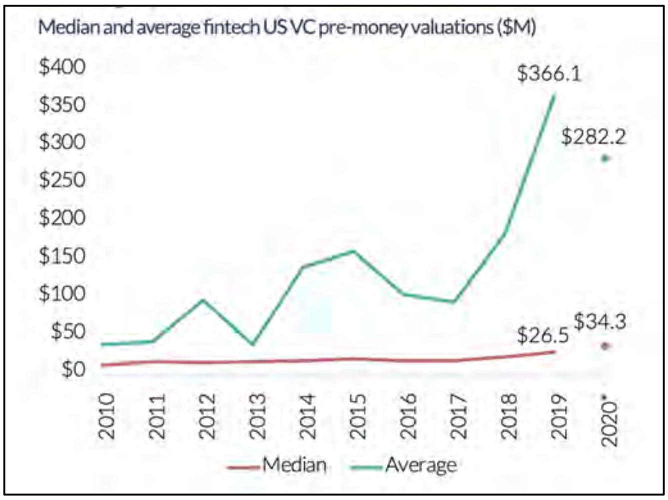
Both the United States and Europe saw a slight increase in fintech funding in Q2'20. However, deal activity in both these regions was either flat or down quarter-on-quarter[1].

Fintech deal-making has continued to concentrate in the later stage and fewer fintech mega-deals (further discussed below) have led to a significant drop in average pre-money valuation.



Source: PitchBook and National Venture Capital Association, Q1 2020 Pitchbook-NVCA Venture Monitor (2020).
*As of March 31, 2020

[1] See, Source: CB Insights, The State of Fintech Q2'20 Report: Investment & Sector Trends to Watch (August 2020), p. 81.

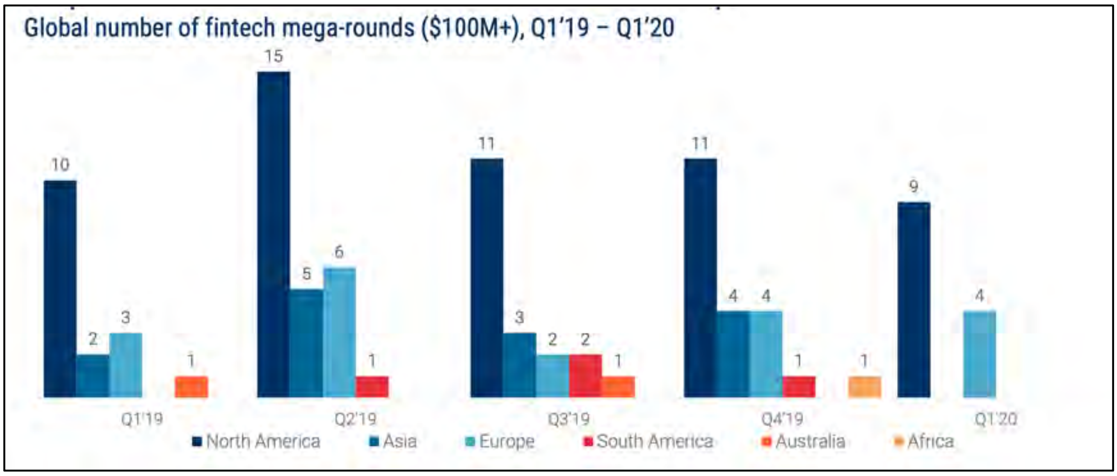


Source: PitchBook and National Venture Capital Association, Q1 2020 Pitchbook-NVCA Venture Monitor (2020).

*As of March 31, 2020

1.3. Fintech Mega-Rounds and Unicorns

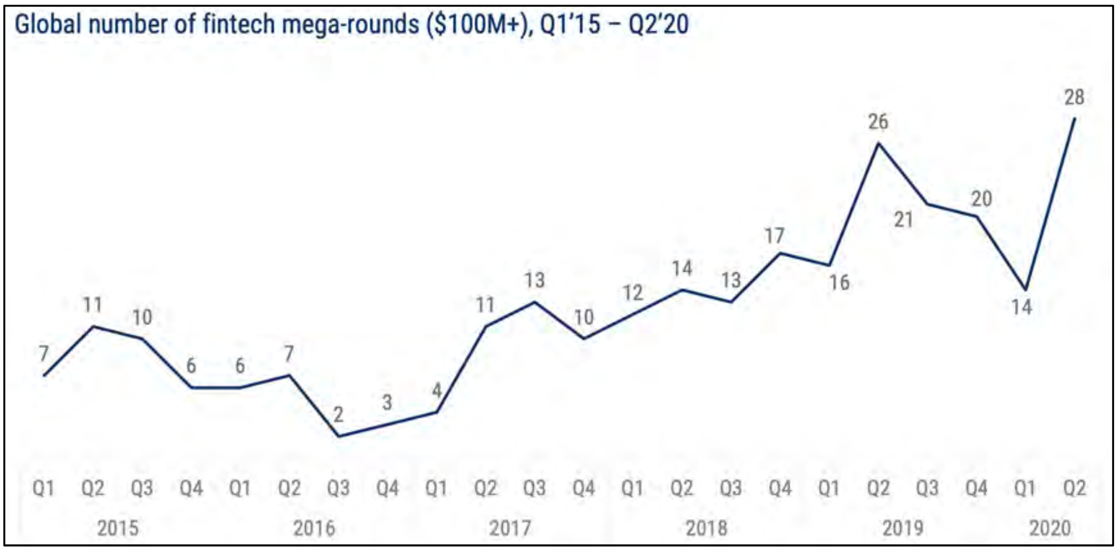
Mega-rounds (i.e., rounds of $100 million or more) stalled globally in Q1’20. The quarter recorded 13 mega-rounds worth a total of $2.6 billion in Europe and the United States, the lowest deal count since Q2’18 and the lowest combined funding since Q3’18. No mega-round was reported outside of Europe or the United States.



Source: CB Insights, The State of Fintech Q1’20 Report: Investment & Sector Trends to Watch (May 2020).

5 of the top 13 deals for VC-backed fintech companies in Q1’20 were $200+ million mega-round investments, with challenger bank Revolut closing the largest round.

After a pronounced pullback during Q1’20, fintech mega-rounds picked up in Q2’20 as a number of large investments came to fruition. Hence, fintech mega-rounds hit a new quarterly high of 28 in Q2’20 as the largest companies in the space and those with high cash-burn rates raised additional funding to weather the Covid-19 crisis and the resulting economic uncertainty.



Source: CB Insights, The State of Fintech Q2'20 Report: Investment & Sector Trends to Watch (August 2020).

The number of fintech companies that reached 'unicorn' status in H1'20 was also limited, with only 3 unicorn births in Q1'20 (HighRadius, Pine Labs and Flywire) and 1 in Q2'20 (Upgrade).

1.4. Fintech Exits: IPO and M&A Activity

The unprecedented changes in the economic outlook triggered by the Covid-19 crisis have rapidly closed down IPO windows for a number of fintech companies and their investors, thus forcing a realistic re-assessment of their exit strategy. Fintech IPO activity decreased significantly in Q1'20. With a few exceptions (including the IPOs of Lemonade, nCino and Fusion Acquisition), fintech IPO activity remained relatively low in Q2'20.

On the contrary, early Q1'20 was relatively active for fintech unicorn M&As. Renewed investors in fintech companies started to see big returns on high-profile M&A exits, including Visa's $5.3 billion acquisition of Plaid[2] and Intuit's $7.1 billion acquisition of Credit Karma[3] (pending closing). In addition, the quarter saw fintech unicorn SoFi acquiring payments processor Galileo for $1.2 billion[4], LendingClub acquiring Radius Bank for $185 million[5], and Morgan Stanley acquiring online brokerage E-Trade for $13 billion[6] (pending close).

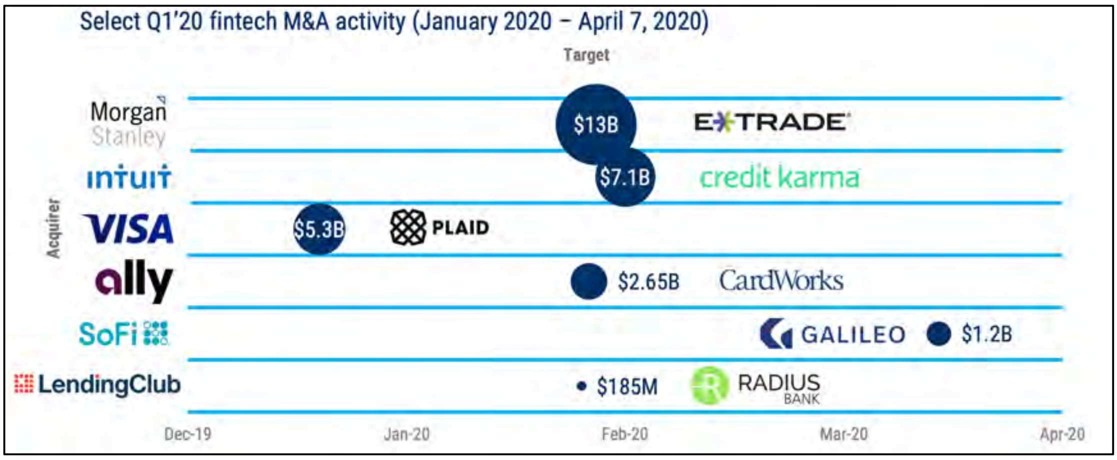
[2] See, Visa Inc., Visa to Acquire Plaid (Press Release, January 13, 2020). See also, Alex Wilhelm and Ron Miller, Visa is acquiring Plaid for $5.3 billion, 2x its final private valuation (TechCrunch, January 13, 2020); Robert Armstrong and James Fontanella-Khan, Visa to buy fintech Plaid in $5.3bn deal (Financial Times, January 13, 2020); Anish Acharya, Scott Kupor and Sonal Chokshi, 16 Minutes on the News #24: What's Up With All These Fintech Acquisitions; SEC Rules (a16z Podcast February 28, 2020).

[3] See, Intuit Inc., Intuit to Acquire Credit Karma (Press Release, February 24, 2020). See also, Nathaniel Popper and Michael J. de la Merced, Intuit to Buy Credit Karma to Create Financial Data Giant (The New York Times, February 24, 2020); Ingrid Lunden, Intuit confirms that it is buying Credit Karma for $7.1B in cash and stock (TechCrunch, February 24, 2020).

[4] See, Social Finance, Inc., SoFi To Acquire Galileo Financial Technologies (Press Release, April 7, 2020). See also, Mary Ann Azevedo, SoFi Acquiring Galileo In $1.2B Deal, Resulting In A '4X' Return For Investor Accel (CrunchBase News, April 7, 2020); Danny Crichton, Another major fintech exit as SoFi acquires banking and payments platform Galileo for $1.2B (TechCrunch, April 7, 2020).

[5] See, LendingClub, LendingClub Announces Acquisition of Radius Bank (LendingClub Press Release, February 18, 2020). See also, Finextra, Online credit marketplace LendingClub acquires Radius Bank (Finextra, February 19, 2020); Sam Maule, A US fintech firm just bought a bank. Now what? (11FS, February 20, 2020); Anna Irrera, Abhishek Manikandan, LendingClub to acquire Radius Bank for $185 million (Reuters, February 18, 2020).

[6] See, Morgan Stanley, Morgan Stanley to Acquire E*TRADE, Creating a Leader in all Major Wealth Management Channels (Morgan Stanley Press Release, February 20, 2020). See also, Gwen Everett, Morgan Stanley to buy online-brokerage giant E-



Source: CB Insights, The State of Fintech Q1'20 Report: Investment & Sector Trends to Watch (May 2020).

These high-profile acquisitions, among others, have highlighted important dynamics in the fintech sector: first, successful fintech and financial services companies tend to own both distribution and products and distribution is where most of the leverage sits today; second, financial services companies that have historically been transactional-oriented need to shift to be truly relationship-oriented and build a much high frequency, trusted and deeper engagement with customers; and third, new generations of consumers are engaging with fintech companies as their primary point of interaction with the financial services ecosystem and many fintech companies are now at a scale where they can represent a new critical growth curve for incumbents targeting new consumer segments[7].

1.5. Valuations and "Flight-to-Quality"

The fintech industry had been on the raise for the a few years before the Covid-19 crisis, with record-high funding levels and rising valuations. As the number of players competing for market share was increasing, numerous fintech companies largely prioritized growth and customer acquisition over profitability. The goal was to keep adding users, keep growing and expanding. However, the unprecedented impact of the Covid-19 pandemic on the fintech industry may have ended this growth-at-all-costs environment[8].

Following the Covid-19 outbreak in Q1'20, eye-watering valuations driven by (often optimistic) assumptions about future growth, profits and exits have been questioned and fundraising has become increasingly difficult and expensive. Down-rounds, hybrid rounds and convertibles have increased as a proportion of the overall funding deals as a result. VC investors have grown far more cautious with their investments theses and terms, have raised their standards in diligence and have amplified their scrutiny on companies' burn rates and financials[9].

Trade for $13 billion (Business Insider, February 20, 2020); Liz Hoffman, Morgan Stanley Is Buying E*Trade, Betting on Smaller Customers (The Wall Street Journal, February 20, 2020).

[7] See, Anish Acharya, Scott Kupor and Sonal Chokshi, 16 Minutes on the News #24: What's Up With All These Fintech Acquisitions; SEC Rules, cit.

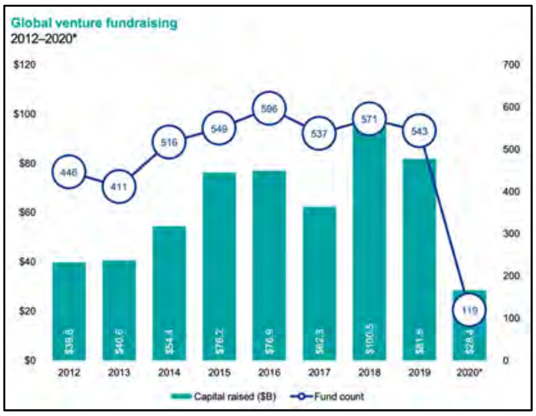
[8] See, CB Insights, How Covid-19 Is Impacting Fintech Financing (CB Insights Research, April 2, 2020 (last updated July 15, 2020)).

[9] See, Goodwin Procter, Five Emerging Trends in Growth Equity Deals (Goodwin Procter Publications, June 29, 2020); Natasha Mascarenhas, Alex Wilhelm, Arman Tabatabai, 8 top fintech VCs discuss COVID-19 trends, signals and opportunities (TechCrunch, April 21, 2020).

Faced with a challenging fundraising environment, fintech companies have been forced to rethink their strategies, tighten their spending and focus more on profitability and positive cash-flow than growth at all costs. This represents a marked shift from the past decade, which saw various companies raise massive amounts of capital without showing a clear path toward profitability[10].

1.6. Venture Capital Fundraising

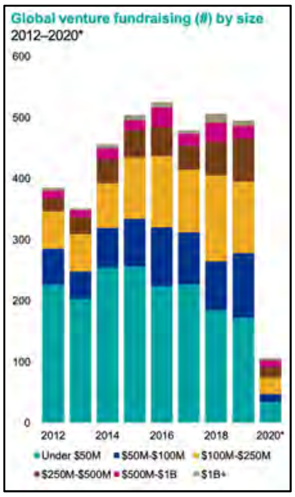
Fundraising was quite strong in Q1’20, with venture capital funds raising a total of $28.4 billion across 119 fundraisings.



Source: KPMG, Venture Pulse Q1 2020.

*As of March 31, 2020. Data provided by PitchBook, April 21, 2020.

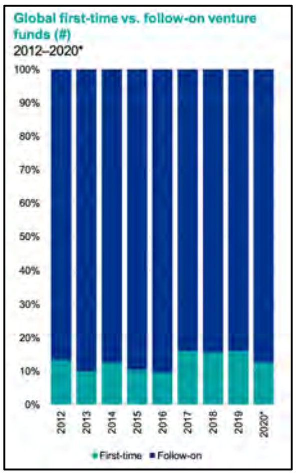
While large VC firms with strong track records have continued to close mega-funds ($500 million+), first-time fundraising have become more difficult as the Covid-19 crisis continues.



Source: KPMG, Venture Pulse Q1 2020.

*As of March 31, 2020. Data provided by PitchBook, April 21, 2020.

[10] See, CB Insights, How Covid-19 Is Impacting Fintech Financing, cit; KPMG, Venture Pulse Q1 2020 - Global Analysis of Venture Funding (KPMG, April 21, 2020), p. 5; Simon Taylor, Is the COVID-19 crisis creating fintech M&A opportunities? (11FS, April 28, 2020); Ernst & Young (EY), How FIs can use M&A in a COVID-19 world to accelerate strategic agendas (EY Insights, May 18, 2020).



Source: KPMG, Venture Pulse Q1 2020.

*As of March 31, 2020. Data provided by PitchBook, April 21, 2020.

A number of VC investors are now sitting on a significant amount of dry powder and lot of funding is waiting to be deployed and invested globally. While VC investors may hold back and remain cautious for the next few months, they will be looking for ways to put their funding at work when the uncertainty around Covid-19 begins to decrease[11].

[11] See, Priyamvada Mathur, Gloom over a new recession shifts the VC narrative for 2020 (PitchBook, March 5, 2020); James Thorne, Mega-funds thrive despite hard times for small and first-time VCs (PitchBook, April 14, 2020).

CHAPTER 2

THE EFFECT OF THE COVID-19 CRISIS ON FIVE FINTECH SECTORS

2.1. The Fintech Ecosystem

As the Covid-19 crisis continues to create uncertainty, many fintech companies have come under significant pressure on a number of fronts. Companies with a cash runway of just a few months have been tapping into a very challenging equity funding environment and, to the extent available, have also been looking for alternative funding sources in the form of debt, convertibles and/or hybrid financing.

Faced with a Covid-19-induced drop in funding, fintech companies with high burn rates and capital-intensive business models, as well as those operating in the hardest hit segments have been forced into large budget cuts, staff layoffs and other measures to cut costs and improve operational efficiency. Those fintech companies which had previously relied heavily on large marketing expenditures to generate growth have come under increased pressure as they could no longer justify large customer acquisition costs in light of weaker transaction volumes.

Some small and medium-sized fintech companies which have struggled to raise additional funding or reposition their business activities during the pandemic have either shut down or suspended their operations, thus underlining the fragile nature of small start-ups through a sustained economic downturn. Contrary, well capitalized fintech companies with high resaleable products have performed relatively better and have showed increasing resilience. The limited operational dependence on brick and mortar offices has also helped most fintech companies weather the crisis, by leveraging existing decentralized teams, remote working, production and distribution systems.

Even in those segments where the current situation has benefitted businesses, most fintech companies have taken significant steps to manage through the current uncertainty. They have curtailed spend that isn't core to survival, have increasingly focused on key business metrics and have been monitoring leading business and financial indicators more closely. Flexibility and validation in business models, strong management teams and the ability to dial-up/down costs have become more and more critical[12].

Many fintech companies have also implemented a wide variety of cost-saving measures, including through workforce reduction. Ensuring that as many expenses as possible are variable and fixed expenses are minimized has been a key priority, particularly for those fintech companies whose revenues are mainly transaction and volume based.

Maintaining operational resilience has been top of mind, as well. Fintech companies have been bolstering their infrastructure to withstand the stress to their systems from higher transaction volumes over an extended period of time. They have accelerated their efforts in supporting functions and employees that provide critical support to their business activities and have assessed their engagement with external service providers and critical suppliers to ensure they are well prepared for a scenario where fintech companies will heavy rely on their services. Fintech companies have also been taking steps to safeguard

[12] See, Andrew Chen, Brian Balfour and Lauren Murrow, Growth in Turbulent Times (a16z Podcast, May 15, 2020).

information security and data protection and have been increasingly vigilant to identify and protect their systems, and promptly detect, respond and recover from data and cyber-attacks.

A number of fintech companies across all verticals have been rethinking and evolving their strategy, diversifying their revenue, or pivoting their business in order to survive the pandemic. Companies have concentrated their efforts on their more robust lines of business and set aside other projects that have not yet demonstrated profitability or were still in an exploratory phase. For example, in March 2020 US-based fintech Moven announced its decision to close all its customers' money management accounts starting on 30 April 2020 and focus exclusively on its enterprise business which outsources the company's technology to banks[13]. More recently, in July 2020 US-based stock-trading app Robinhood announced it was postponing its UK launch indefinitely to refocus its efforts on its home market[14].

A few fintech companies have been accelerating product development to prepare for the impact of Covid-19 and have quickly launched new products or solutions in response to the current environment. For example, U.S. based digital bank, Chime, launched an online solution to deliver advance payments of government-issued economic aid in response to the Covid-19 crisis in April 2020[15]. Other savvy digital providers have been offering specific products and services geared to the crisis. For example, leading payment processing platform, Stripe, launched a series of products aimed at helping platforms and their business customers adapt to a fast-changing economic environment in June 2020[16]. In the UK, fintech companies Fronted, 11:FS and Credit Kudos came together to create 'Covid Credit' in March 2020, which allows self-employed workers to generate a proof statement detailing their past income and the impact of Covid-19 to help them get access to government support[17]. At the same time, several fintech lenders have been accredited to lend under the government lending schemes[18].

Looking at the fintech ecosystem in more detail, the impact of the Covid-19 crisis has been varied with marked differences by sector. Although funding has been down across the whole fintech ecosystem, each fintech sector has been responding to some unique challenges. Some fintech sectors have been hurting significantly, whilst others have proven to be more resilient[19]. Fintech companies that are more closely linked and exposed to industries like travelling, tourism or entertainment have suffered the most. On the other hand, the Covid-19 crisis has reinforced a wider-scale adoption of digital payment solutions and has acted to strengthen the business models of fintech companies specializing in digital payment solutions, ecommerce or online sales platforms. Similarly, the pandemic has accelerated the structural

[13] See, Finextra, Moven to wind down consumer unit as spin-off funding withdrawn (Finextra, March 25, 2020); Rachel Green, US neobank Moven is closing its consumer bank after funding fell through due to the coronavirus (BusinessInsider, March 31, 2020).

[14] See, Steve O'Hear, Robinhood, the stock trading app, postpones UK launch 'indefinitely (TechCrunch, July 21, 2020); Richard Henderson and Madison Darbyshire, Robinhood scraps plans to launch stock-trading app in UK (Financial Times, July 21, 2020).

[15] See, Sarah Hansen, This Digital Bank Is Giving Some Members Their Stimulus Money In Advance Of The IRS Checks (Forbes, April 2, 2020); Jeff Kauflin, Digital Bank Chime Now Offering Stimulus Check Advance To 100,000 Users (Forbes, April 9, 2020).

[16] See, Finextra, Stripe launches products to help platforms powering Covid-19 economic recovery (Finextra, June 29, 2020); Kate Rooney, How Stripe, CNBC's No. 1 Disruptor 50 company, helped keep the U.S. economy afloat during pandemic (CNBC, June 16, 2020).

[17] See, Simon Taylor, The Covid Credit collaboration: how fintech is supporting the UK's self-employed (11:FS, March 24, 2020); Steve O'Hear, UK fintech community comes together to build Covid Credit and let sole traders self-certify lost income (TechCrunch, March 24, 2020).

[18] See, Aisling Finn, Which fintechs are offering government-backed CBILS, CLBILS or Bounce Back loans? (AltFi, May 21, 2020).

[19] See, CB Insights, Covid-19 Has Scrambled Fintech's Winners & Losers. Here's The Short- & Long-Term Outlook (CB Insights, June 3, 2020).

shift to digital banking and digital financial services, thus benefitting challenger banks, lending platforms and other digital players. The following sections will look into the short-term and long-term effects of the Covid-19 crisis on five main sectors of the fintech ecosystem: payments, banking, lending, wealth management and capital markets and insurance.

2.2. Payments

The global Covid-19 pandemic has brought significant changes to businesses' and consumers' spending behaviors. With much of the world in lockdown, international travelling and the use of public and private transports have reduced significantly, thus resulting in a remarkable decline in cross-border business and overseas and travel-related spending. The general economic uncertainty affecting businesses and many individuals at a personal level has triggered a reduction in discretionary spending on all non-essential products and services.

With the focus of the pandemic response being on social distancing and a forced reduction in physical contact, in-store spending has materially reduced relative to online spending. As individuals have become increasingly reluctant to use cash fearing that notes and coins may spread the virus, the decline in the use of cash has also accelerated with the proportion of contactless payments and digital payments materially increasing in recent months[20]. To accommodate the surge in payments made through cards, several EU jurisdictions have increased the applicable contactless payment limits[21].

Against this background, the short-term impact of Covid-19 on the fintech payments sector has been nuanced. On the one hand, fintech payments companies serving verticals hit hardest by Covid-19 (including travel, restaurants, and events and entertainment) have faced existential challenges and have been forced to find new sources of transaction volume in order to survive. The reduction in consumer spending trigged by Covid-19 has also negatively impacted payment processing services and those card issuers which receive most of their revenues from interchange fees[22].

On the other hand, the Covid-19 crisis has contributed to an explosion in e-commerce at the expense of physical retail. As a result, fintech payments companies serving online retails and the e-commerce space have seen their transaction volumes sharply accelerate and have increasingly taken market share away from companies serving physical retailers. As the Covid-19 crisis enhances secular shifts to online payments, these companies have boomed and are now set to be among the biggest long-term beneficiaries of the crisis[23]. Notable examples of these fintech companies include Stripe (which saw its valuation

[20] See, McKinsey & Company, How payments can adjust to the coronavirus pandemic—and help the world adapt, McKinsey & Company Reports (March 31, 2020); McKinsey & Company, Financial life during the COVID-19 pandemic—an update, McKinsey & Company Reports (July 23, 2020); Raphael Auer, Giulio Cornelli and Jon Frost, Covid-19, cash, and the future of payments (BIS Bulletin No.3, April 3, 2020); UK Finance, Cards used for half of payments for first time last year (UK Finance, June 3, 2020).

[21] For example, the UK increased the limit from £30 to £45 across the country starting on 1 April 2020. Other countries that have adopted similar approaches include the Netherlands, Germany, Norway and Poland.

[22] See, CB Insights, Covid-19 Has Scrambled Fintech's Winners & Losers. Here's The Short- & Long-Term Outlook, cit. (highlighting a few examples of fintech payment companies, like Toast (which cut 50% of its staff in early April 2020), TouchBistro (which furloughed 20% of its workforce in April 2020), and Square (card present volume down 60% in final 2 weeks of Q1 2020), which have sought to reduce risk by placing bets in other areas, like government-backed loans: TouchBistro collaborated with Lendio to distribute loans to its restaurateurs and Square has been leveraging its Cash App to distribute loans directly to consumers).

[23] Ibidem.

increase to $36 billion following the closing of its $600 million Series G extension round in April 2020)[24], Adyen (whose stock surged in April 2020 after the company reported a 34% jump in Q1'20 revenue driven by online payments)[25], Checkout (which reported a 250% surge in online transactions between May 2019 and May 2020 and tripled its valuation to $5.5 billion after closing a $150 million Series B funding round in June 2020)[26], Bolt (which raised a Euro 50 million Series C in July 2020)[27] and Finix (which closed its $10 million Series B led by venture firm Sequoia in February 2020)[28].

At the same time, the Covid-19 crisis has also accelerated a trend of technology companies offering and enabling financial services across multiple sectors and a variety of distribution channels. More companies are now following the steps of big technology companies, like Google, Uber, Amazon and AirBnB, and are increasingly embedding payment functionalities in non-financial services, as well as financial products beyond payments – from loans to cards to insurance – into their vertical offerings[29].

2.3. Banking

The Covid-19 crisis has had a mixed impact on challenger banks. Those which generate most of their revenues from debit swipe fees and heavily rely on transaction revenues have been negatively affected by a reduction in interchange and FX fees. Some challenger banks have faced an increase in delinquent loans and default as businesses and consumers have quickly draw down and spent through existing credit lines and have struggled to repay their debt.

A number of challenger banks saw net interest margin compression and their growth rate decrease in their native markets in Q1'20, with a relevant decline in signups and app downloads relative to the previous quarter[30]. For a few players, the number of active users has also contracted[31]. Various reasons may have contributed to these trends, including limited spending, a rapid shift in costumer transaction patterns and the preference of certain customers to consolidate their money in few accounts.

As they navigate the Covid-19 crisis, some challenger banks have put on hold projects still in an early-stage explanatory phase in favor of key business lines and offerings, have focused on operational resilience and core systems, and have taken a number of actions to reduce costs and operating pressures[32].

[24] See, Ingrid Lunden, Alex Wilhelm, Stripe raises $600M at $36B valuation in Series G extension, says it has $2B on its balance sheet (TechCrunch, April 16, 2020).

[25] See, John Reynolds, Adyen reports Q1 revs up 34 per cent and rules out furloughing staff in UK amid Covid-19 (AltFi, April 22, 2020).

[26] See, Ingrid Lunden, Checkout.com, the UK payments startup, raises another $150M, now valued at $5.5B (TechCrunch, June 22, 2020).

[27] See, Ingrid Lunden, Bolt raises €50M in venture debt from the EU to expand its ride-hailing business (TechCrunch, July 16, 2020); Christine Hall, Bolt Secures $50M in Series C Funding to Unveil Checkout Experience Platform (CrunchBase News, July 16, 2020).

[28] See, Alex Wilhelm, Payments infra startup Finix closes $35M Series B led by Sequoia (TechCrunch, February 4, 2020).

[29] See, Kristina Shen, Kimberly Tan, Seema Amble, and Angela Strange, Fintech Scales Vertical SaaS (a16z, August 2020); Angela Strange, Every Company Will Be a Fintech Company (a16z Summit, November 2019); Angela Strange, Why Every Company Will Be a Fintech Company: The Next Era of Financial Services and the 'AWS Phase' for Fintech (a16z Podcast, November 2019); Matthew Harris, Fintech: The Fourth Platform - Part One (Forbes, November 2019).

[30] See, Finextra, Covid-19 hits challenger banks as app downloads slide (Finextra, April 29, 2020); Isabel Woodford, Digital bank signups dive in lockdown (Sifted, April 27, 2020).

[31] Ibidem. See, also, Jeroen de Bel, Loris Vinci, Performance of neo banks in times of COVID-19 (Fincog, June 9, 2020).

[32] See, Michael Deleon, The Challengers 13: COVID-19's impact on digital banking, growth slows at OakNorth, Square as a bank (TearSheet, March 31, 2020); Ernst & Young (EY), How COVID-19 is impacting Challenger & Specialist banks and building societies (EY Report, April 9, 2020); Aurelie L'Hostis, Many Digital Banks Will Struggle Amid The COVID-19-Induced Slowdown, But A Handful Will Innovate And Thrive (Forrester, April 21, 2020).

A number of challenger banks have also raised mega-rounds in Q2'20, thus building up reserves to weather the prolonged downturn triggered by the Covid-19 crisis[33].

As travel bans and Covid-19-imposed restrictions are gradually lifted, growth rate for challenger banks is expected to rebound. Similarly, domestic and international spending are expected to recover while governments are loosening restrictions and travel opens up.

Although they may continue to face some hurdles in the nearer term, challenger banks are certainly positioned to benefit from the changes brought by the Covid-19 crisis in the longer term, including a resulting acceleration towards more digital banking services and an increased focus on mobile and online user experience. The trend of re-bundling multiple banking, payments and investment services should also accelerate, driven by an increased appetite for digital interactions and the need to monetize customer acquisition costs.

Going forward, challenger banks most resilient to a sustained economic slowdown will likely show a number of key attributes: first, they will be well-capitalized to support their operations and activities and consolidate their market position throughout the crisis and beyond; second, they will provide a durable, evolving and high-quality offerings and they will have a strong customer adoption and a loyal base of active users which utilize the challenger account as a primary account (paying their salaries into and linking direct deposits to it); third, they will have robust balance sheets to put them in a stable and lean position and will be profitable or on a clear path to profitability with realizable adoption targets across demonstrated revenue lines; and lastly, they will have an efficient distributed workforce and a resilient and agile technology largely built in-house[34].

2.4. Lending

Online lenders are among the fintech companies being hit the hardest by the Covid-19 crisis. Most of these companies started up right after the last financial crisis of 2009 and many have not yet had their own business models tested in a downturn.

As earnings have dropped or vanished entirely due to a prolonged Covid-19 induced downturn, a growing number of businesses and individual customers have become unable to repay their debts on time and defaults have rapidly increased. As a result, a number of online lenders have come under pressure facing lower net interest margins, falling loan growth, as well as rising delinquencies and defaults. Among them, those online lenders which had begun serving subprime and small/medium businesses before the Covid-19 crisis have seen default rates rising the most and some have discovered to have inadequate reserves to weather the crisis.

Algorithms and credit models to make lending decisions have been severely tested for the first time in a prolonged recession. Some online lenders have found that the data they had typically used to make

[33] See, Steve O'Hear, Monzo confirms £60M down round, with a new pre-money valuation of £1.24B (TechCrunch, June 16, 2020); Romain Dillet, N26 raises another $100M in Series D extension (TechCrunch, May 5, 2020); Sarah Perez, Challenger bank Varo, soon to become a real bank, raises $241M Series D (TechCrunch, June 3, 2020); Alex Wilhelm, Credit-focused fintech startup Upgrade raises $40M after reaching $100M run rate (TechCrunch, June 17, 2020); Romain Dillet, Point to launch new challenger bank with rewards on debit card purchases (TechCrunch, July 1, 2020).

[34] See, CB Insights, Covid-19 Has Scrambled Fintech's Winners & Losers. Here's The Short- & Long-Term Outlook, cit.

underwriting decisions is less reliable in the economic environment impacted by the Covid-19 crisis and have been forced to adjust their models accordingly.

With fewer loans to grant and rising defaults, many online lenders have been forced to implement significant changes to their business activities and drastic costs cutting measures[35]. For example, LendingClub reported a 90% reduction in loan originations on its platform from pre-Covid-19 levels in Q1'20 while also taking significant actions to shore up liquidity, including by reducing its staff by 30% and implementing salary cuts across the company[36]. Other lenders, including Kabbage, Zopa and OnDeck, have temporarily shut off new loan originations and tightened credit standards in an attempt to weather the Covid-19 crisis[37].

Certain lenders have suspended their secondary market activities due to increased concerns that they will not be able to meet the demand for lending. Investors have become more reluctant to invest and a high volume of retail investors have requested early access to funds, in an attempt to exit their positions. For instance, JustUs suspended its secondary market as the Covid-19 pandemic took hold in March 2020[38], followed by Lending Works which announced that it would not accept any new investments and would suspend the use of the secondary market in April 2020[39], as well as Funding Circle which communicated its intention to suspend its secondary market as it reacted to the outbreak of Covid-19 crisis in April 2020[40].

On the contrary, other lending players have demonstrated to be more resilient to the Covid-19 crisis. Some have limited the exposure to a downturn with lending books of medium to low risk and have tightened their underwriting standards to retain the quality of their lending book and mitigate any potential rise in defaults. A few online lenders have also limited eligibility to the most creditworthy customers (thus resulting in low risk and relatively higher performing lending books) and have decided to adopt an even more conservative approach to how they originate lending for the rest of 2020.

Moreover, a number of lenders have played a positive role in the response to the Covid-19 crisis by providing financing via the government business rescue schemes. These include leading fintech companies like BlueVine, PayPal, Intuit QuickBook, Credibly and Square[41]. Similarly, lending marketplaces like Lendio, Fundera, Paychex and Biz2Credit have leveraged their platforms to facilitate access to government assistance loans[42].

Lastly, fintech companies in the lending space which white-label their lending technology to incumbent financial institutions (including Upstart's Powered by Upstart, OnDeck's ODX and Avant's Amount)

[35] See, Jeff Kauflin, Fintechs For Sale: Post-Covid, It's Partner Or Perish For Many Startups. Here's A Buy List (Forbes, May 11, 2020).

[36] See, Bram Berkowitz, LendingClub's Loan Originations Fell 90% in April (Nasdaq, May 8, 2020).

[37] See, Zeke Faux and Jennifer Surane, SoftBank-Backed Lender Kabbage Cuts Off Businesses as Cash Needs Mount (Bloomberg, April 1, 2020); Marc Shoffman, Zopa stops higher risk lending (Peer2Peer Finance News, April 14, 2020); PYMNTS, OnDeck Tightens Credit Standards As Charge-offs Rise (PYMNTS, May 2, 2020).

[38] See, Marc Shoffman, JustUs suspends secondary market as it awaits coronavirus loan scheme clarity (Peer2Peer Finance News, March 25, 2020).

[39] See, Daniel Lanyon, Lending Works introduces "extraordinary measures" amid investor exit queue (AltFi, April 7, 2020).

[40] See, Kathryn Gaw, Funding Circle suspends secondary market (Peer2Peer Finance News, April 9, 2020).

[41] See, Robin Saks Frankel, Need A Loan Now That The Paycheck Protection Program Is Running Again? Try These Nonbank Lenders (Forbes, April 27, 2020); Kimberly Weisul, Fintechs Jump Into Small-Business Loan Chaos (Inc., April 14, 2020).

[42] See, Michael Cohn, Paychex teams up with lenders to help small businesses apply for PPP (Accounting Today, April 24, 2020).

have performed relatively well and are among those more likely to be sustainable in a prolonged downturn[43].

Looking further out, the slow-down in online lending is likely to lead to insolvency for some players and consolidation for others. Only reputed lenders will remain solvent and will come out of the Covid-19 crisis with newfound resilience. Digital lenders that will successfully navigate the downturn caused by the Covid-19 pandemic are expected to update and strengthen their underwriting models, collections and risk management systems. While the trend towards alternative data sources for underwriting may continue, these will likely be utilized in combination with more traditional metrics.

Consolidation is expected to become a dominant theme in the lending sector and many smaller lenders will likely be absorbed by banks or larger and well-capitalized fintech companies. These players have increasingly expressed their appetite for M&A targets and the acquisition of distressed lenders could be a valuable opportunity for them to expand their product offering and technology capabilities[44].

2.5. Wealth Management and Capital Markets

Wealth management and capital markets fintech companies have tapped equity and debt financing sources to weather the Covid-19 crisis and shore up cash reserves. For example, investing app Stash closed a $112 million Series F round in March 2020, which put the valuation of the company at around $812 million[45]. Shortly thereafter, Freetrade completed a Euro 7.8 crowdfunding via the Crowdcube platform in May 2020[46]. Similarly, Robinhood announced the closing of a $280 million Series F funding round in May 2020 increasing its valuation to $8.3 billion, which it subsequently topped up by raising an additional $320 million in July 2020 which took its valuation up to $8.6 billion and a further $200 million at a valuation of $11.2 billion in August 2020[47].

As valuations have become more conservative and competition heats up, consolidation has also increased with smaller firms being acquired by larger players in the market. For example, SoFi announced the acquisition of payment platform Galileo for $1.2 billion in April 2020[48]; Franklin Templeton acquired AdvisorEngine, a digital wealth platform and provider of technology and consulting services, in May 2020[49]; Goldman Sachs acquired Folio, a RIA custodian platform with $11B in assets under custody, for approximately $500 million in May 2020[50]; and Empower, the second-largest US retirement services provider, acquired Personal Capital in a deal valued at $1 billion in June 2020[51].

[43] See, CB Insights, Covid-19 Has Scrambled Fintech's Winners & Losers. Here's The Short- & Long-Term Outlook, cit.

[44] Ibidem.

[45] See, Ingrid Lunden, Amid stock market turbulence, investing app Stash raises $112M led by LendingTree (TechCrunch, April 29, 2020).

[46] See, Aisling Finn, Freetrade smashes crowdfunding target, raises over £5m on Crowdcube (May 15, 2020).

[47] See, Alex Wilhelm, Natasha Mascarenhas, Robinhood raises $280M, pushing its valuation to $8.3B (TechCrunch, May 4, 2020); Lucinda Shen, Robinhood raises another $320 million at an $8.6 billion valuation (Fortune, July 13, 2020); Alex Wilhelm, Robinhood raises $200M more at $11.2B valuation as its revenue scales (TechCrunch, August 17, 2020).

[48] See footnote no. 4.

[49] See, Pavithra R, Franklin Templeton acquires AdvisorEngine for better financial advice future (IBS Intelligence, May 7, 2020); Sean Allocca, Franklin Templeton buys AdvisorEngine (Investment News, May 6, 2020).

[50] See, Elizabeth Dilts Marshall, Goldman Sachs to Buy Boutique Wealth Management Custodian Folio (Reuters, May 14, 2020).

[51] See, Alex Wilhelm, Personal Capital sells to Empower Retirement in deal worth up to $1B (TechCrunch, June 29, 2020); BusinessWire, Empower Retirement Closes Acquisition of Personal Capital (BusinessWire, August 18, 2020).

Longer term, the Covid-19 crisis is expected to bring relevant changes with consumers looking for hybrid robo-advisory services and more deeply integrated platforms[52].

Increased market volatility has highlighted a growing customer preference for human advisors. Companies like Betterment and Wealthfront, which have built large consumer bases over the past decade, have seen higher-than-average engagement with human advisors in Q1'20. Going forward, these and similarly new entrants will likely need to strengthen their hybrid robo-advisory solutions to stay relevant and grow their respective customer bases. They will also increasingly compete with incumbents like Fidelity, Morgan Stanley and Charles Schwab, as customers may seek more trusted human advice offered by established players which can also compete on fees with zero-commission models[53].

At the same time, the Covid-19 crisis has amplified the need for more deeply integrated platforms and centrally managed "autopilot" personal finance solutions[54]. In response to a rapid shift in consumer behavior, wealth management fintech firms are increasingly offering integrated platforms and providing a more holistic suite of services and analytics tools to customers. For example, Betterment announced an addition of FDIC-insured checking and savings account services through partnerships with several banks in April 2020[55], while Wealthfront is currently working on connecting customers with mortgage providers[56]. Moreover, remittance players have gradually introduced investment services among their offerings. Most notably, in July 2020 TransferWise announced the upcoming launch of investment products on its cross-border payments platform, allowing users to invest their deposits and adding a new revenue stream[57].

Going forward, a number of robo-advisors may also start to look more like challenger banks to cater for a new set of customers as they mature over the next decade[58]. As the economy begins to recover from the Covid-19 crisis, more fintech companies are likely to introduce savings features as customers will increasingly value the opportunity to build out tailored emergency savings funds strategies[59].

2.6. Insurance

The near-term impact of the Covid-19 crisis on the insurtech sector has been mixed depending on the specific insurance lines of business. Longer term, digital insurance offerings and services are expected to increase in relevance as consumer behaviors evolve and new business models emerge[60].

As the insurance sector evolves to rebound from the Covid-19 crisis, technology enabled solutions will be core in improving customer experiences. Insurtech companies' new technology and agility will likely enable them to grow and adapt to the new environment quicker and more efficiently than incumbents. Insurtech companies providing online and digital offerings with easier underwriting processes for life

[52] See, CB Insights, Covid-19 Has Scrambled Fintech's Winners & Losers. Here's The Short- & Long-Term Outlook, cit.

[53] Ibidem.

[54] Ibidem.

[55] See, Jonathan Shieber, Betterment adds checking and savings products (TechCrunch, April 21, 2020).

[56] See, Sean Allocca, Wealthfront adds mortgages to its banking ambitions (Financial Planning, December 4, 2019).

[57] See, Steve O'Hear, TransferWise to offer investment products but has 'no plans' to become a bank (TechCrunch, July 1, 2020).

[58] See, Snigdha Kumar, FinTech in Post-Covid 19 World (Medium, April 7, 2020).

[59] See, Eric Rosenberg, The Digit app will build your emergency fund for you, and you won't even notice the money leaving your checking account (Business Insider, February 2, 2020); Eric Rosenberg, 5 foolproof ways to build an emergency savings fund (Business Insider, June 18, 2020).

[60] See, CB Insights, Covid-19 Has Scrambled Fintech's Winners & Losers. Here's The Short- & Long-Term Outlook, cit.

insurance and property insurance are already seeing a significant increase in applications as customers prefer to limit any interaction with medical exams or agents throughout the Covid-19 pandemic[61].

The Covid-19 crisis has highlighted how static and outdated traditional insurance offerings and customer engagements are. Going forward, data driven, flexible and transparent insurance products (e.g., on-demand insurance, parametric insurance and usage-based insurance) are expected to become more and more attractive to consumers[62].

Distribution is also expected to continue to trend towards direct and digital, while digitizing key value chain operations (including underwriting and claims management) will become increasingly important to improve operational efficiency. Successful insurers will likely embrace emerging technology and deepen their understand of the shifts in customer expectations and behavior [63].

[61] See, Willis Towers Watson Securities, Willis Re and CB Insights, Quarterly InsurTech Briefing (Report, July 2020).
[62] See, CB Insights, Covid-19 Has Scrambled Fintech's Winners & Losers. Here's The Short- & Long-Term Outlook, cit.
[63] Ibidem.

CHAPTER 3

GOVERNMENTAL COVID-19 FUNDING SUPPORT

The Covid-19 crisis has led to unprecedented governmental financial assistance to both large and small companies on a global scale. This chapter provides a brief overview of certain Covid-19 governmental funding support measures of interest to startups and growth stage companies which have been implemented in the United States, the United Kingdom and Europe[64].

3.1. The US Government's Covid-19 Funding Measures

The Coronavirus Aid, Relief and Economic Security Act (the "CARES Act") was signed into law on March 27, 2020. The largest fiscal stimulus bill in the U.S. history, the CARES Act provides over $2 trillion in stimulus funds and creates a number of new programs and authorities for executive branch agencies, particularly the Department of the Treasury ("US Treasury") and the Board of Governors of the Federal Reserve System (the "Federal Reserve")[65], which is intended to help the U.S. economy in response to the Covid-19 pandemic and the resulting economic downturn.

This section provides a brief summary of certain assistance programs implemented under the CARES Act and certain regulatory relief granted by U.S. federal banking agencies intended to stabilize the U.S. economy in response to the Covid-19 crisis.

3.1.1. Paycheck Protection Program (PPP)

The CARES Act (as amended)[66] allocates nearly $670 billion for loans to help small businesses cover payroll and overhead costs and keep employees in their jobs amid the Covid-19 pandemic and the resulting economic downturn. Provided that borrowers meet certain criteria and so long as loan proceeds are utilized for permitted uses in the 24-week period after the loan is disbursed, the amount of principal (and accrued interest) used for the permitted uses will be forgiven. Known as the Paycheck Protection Program ("PPP"), this program is administered by the U.S. Small Business Administration (SBA) through its 7(a) lending program. PPP loans are backed by an SBA guarantee and are originated by the

[64] This chapter does not discuss all of the various governmental financial assistance measures adopted in the United States, the United Kingdom and Europe and is not intended to be a comprehensive review of the ongoing activities and initiatives implemented by the US, UK and European governments in response to the Covid-19 crisis.

[65] In addition to the CARES Act, the Federal Reserve has implemented a number of programs under prior authority in response to the Covid-19 crisis, which are intended to ensure the availability of credit and liquidity to businesses and households. More information on the Federal Reserve's actions can be found on its Covid-19 resources page at https://www.federalreserve.gov/covid-19.htm.

[66] On April 2, 2020, the U.S. Small Business Administration (SBA) issued an interim final rule relating to the implementation of sections 1102 and 1106 of the CARES Act (published in the Federal Register on April 15, 2020). Section 1102 of the CARES Act temporarily adds a new product, titled the "Paycheck Protection Program" (the "PPP") to the SBA's 7(a) Loan Program. Subsequently, the SBA issued a number of interim final rules implementing the PPP. On 5 June 2020, the Paycheck Protection Program Flexibility Act of 2020 (PPPFA) was signed into law, amending the CARES Act, and the SBA published an interim final rule under the PPPFA amending its prior interim final rule published in the Federal Register on April 15, 2020. The PPPFA and the IFR introduced a number of changes which increase the utility of the PPP and make it easier for small businesses to receive loan forgiveness including by: allowing small businesses to use up to 40% of PPP loan proceeds for eligible non-payroll costs; extending the period in which payroll costs can be incurred or paid from 8 weeks up to 24 weeks for PPP loan proceeds received on or after June 5, 2020; and giving small businesses until December 31, 2020, to rehire employees and restore salaries to conform to provisions required under the PPPFA.

SBA's network of SBA-licensed lenders, as well as by other lenders approved by the SBA to participate in the program[67].

Due to high demand, the PPP exhausted its initial $350 billion funding on April 17, 2020. The Paycheck Protection Program and Health Care Enhancement Act, which was signed into law on April 24, 2020, allocated to the PPP an additional US$310 billion, permitting it to resume processing new loan applications through to the end of June 2020. Subsequently, in July 2020, the PPP application deadline was extended by five additional weeks through to August 8, 2020.

Since the original launch in April 2020, 5,212,128 small businesses have received more than $525 billion in PPP loans[68].

The key terms of the PPP are summarized below:

- Eligibility - In general and subject to certain SBA's affiliation rules[69], to be eligible for the PPP a borrower must be: (i) a "small business concern" (as defined by the SBA)[70], (ii) a business concern, nonprofit organization, veterans organization or tribal business with 500 or fewer employees whose principal place of residence is in the United States, or the business meets the SBA's employee-based size standards for the industry in which it operates (if applicable), or (iii) certain sole proprietorships, independent contractors and self-employed individuals. A borrower must have been in operation on February 15, 2020 and must provide the certifications required by SBA which include the following:
    - the uncertainty of current economic conditions makes the loan request necessary to support the ongoing operations of the borrower[71];
    - the funds will be used to retain workers and maintain payroll or make mortgage payments, lease payments, and utility payments;
    - the applicant does not have another Section 7(a) loan application pending for the same purpose and duplicative of amounts applied for; and
    - during the period beginning on February 15, 2020 and ending on December 31, 2020, the eligible recipient has not received any paycheck protection loans.

[67] The terms of the PPP are subject to rules promulgated by the Treasury Department and the SBA. These rules have been in a constant state of flux since early April 2020 and remain under review at the date of writing. The analysis provided in this section is based on the rules currently in effect, which can be found at https://home.treasury.gov/policy-issues/cares/assistance-for-small-businesses. The SBA has continued to issue guidance in the form of updates to its interim final rules on the PPP program, as well as a FAQs document available on the SBA's website at https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Frequently-Asked-Questions.pdf.

[68] See, U.S. Small Business Administration, Paycheck Protection Program (PPP) Report - Approvals through 08/08/2020 (August 11, 2020).

[69] Under the SBA's affiliation rules, private equity portfolio companies or companies with significant VC investments may be required to look at the aggregate number of employees across the PE firm/VC firm's whole portfolio companies rather than their own employees on a stand-alone basis, depending on the size of the fund investment and certain management rights exercised by the fund. See Paycheck Protection Program Loans, Frequently Asked Questions (FAQs) (as of June 25, 2020), Questions no. 5 and 6, available at https://www.sba.gov/sites/default/files/2020-06/Paycheck-Protection-Program-Frequently-Asked-Questions%20062520-508.pdf.

[70] Small business concerns can be eligible PPP borrowers even if they have more than 500 employees, as long as they satisfy the existing statutory and regulatory definition of a "small business concern" under section 3 of the Small Business Act, 15 U.S.C. 632. A business can qualify if it meets the SBA's employee-based or revenue-based size standards for the primary industry in which it operates. In addition, a business can qualify for the PPP as a "small business concern" if it met both tests in SBA's "alternative size standard" as of March 27, 2020: (i) maximum tangible net worth of the business is not more than $15 million; and (2) the average net income after federal income taxes (excluding any carry-over losses) of the business for the two full fiscal years before the date of the application is not more than $5 million. See Paycheck Protection Program Loans, Frequently Asked Questions (FAQs) (as of June 25, 2020), Questions no. 2, 36 and 44.

[71] See Paycheck Protection Program Loans, Frequently Asked Questions (FAQs) (as of June 25, 2020), Questions no. 31, 37, 43 and 46.

- Maximum Loan Amount – Eligible borrowers may borrow up to 2.5 times the borrower's average total monthly payroll costs incurred during the 1-year period before the loan application date, subject to a $10 million cap.
- Maturity for Principal That Is Not Forgiven - Loans issued after June 6, 2020 have a maturity of 5 years. Loans originated prior to that date have a 2-year maturity, although borrowers and lenders may mutually agree to extend the maturity to 5 years[72].
- Interest Rate for Principal That is Not Forgiven – The PPP loans have an annual fixed interest of 1%. Interest accrual begins as of the date of the disbursement[73].
- Permitted Uses – PPP loan proceeds can be used to pay for payroll costs for U.S. employees, interest on mortgage obligations, rent, utilities, interest on other debt incurred before February 15, 2020 and refinancing an SBA Economic Injury Disaster Loans (EIDL) made between January 31, 2020 and April 3, 2020. If the funds are used for unauthorized purposes, the SBA may have recourse against shareholders, members and partners of the borrower. Moreover, if the borrower uses PPP loan proceeds for a non-authorized purpose, the SBA can direct the borrower to repay those misused amounts and the borrower may be subject to additional charges for fraud. PPP loan proceeds cannot be used for the same purpose as EIDL loan proceeds.
- Deferral of Principal and Interest Payments - Under the Paycheck Protection Program Flexibility Act of 2020 (PPPFA)[74], principal and interest payments for amounts that are not forgiven are deferred until the date that a final determination of the PPP loan forgiveness is made (or, if the borrower does not apply for loan forgiveness, 10 months after the end of the borrower's PPP loan forgiveness period).
- PPP Loan Forgiveness - A borrower is eligible for loan forgiveness equal to the 'forgiveness amount'. The CARES Act (as modified by the PPPFA) provides that the forgiveness amount cannot exceed the principal of the PPP loan and is equal to the amount the borrower spends on the following items during the 24-week period after the PPP loan is disbursed (or through December 31, 2020, if a loan is made after November 5, 2020): payroll costs, interest on any mortgage obligation incurred in the ordinary course of business, rent on a leasing agreement, payments on utilities (electricity, gas, water, transportation, telephone, or internet), and for borrowers with tipped employees, additional wages paid to those employees. To be eligible for loan forgiveness, the borrower shall retain its existing employees at or near current salary levels during the PPP covered period. The forgiveness amount is subject to some reductions to encourage employee retention and rehiring (as further discussed below).

  An important limitation to the described expenditure rules is that 60% or more of the PPP loan proceeds must be spent on payroll costs[75]. This means that no more than 40% of the forgiven debt can be attributed to non-payroll costs, including interest on certain mortgage obligations, payments on rent obligations, and utility payments. If a borrower uses less than 60% of the PPP loan amount

[72] The minimum maturity date requirement was increased to 5 years as part of the PPPFA enacted on June 5, 2020. See Paycheck Protection Program Loans, Frequently Asked Questions (FAQs) (as of June 25, 2020), Question no. 49.

[73] The accrued interest on any principal amount that is forgiven will be paid by the SBA.

[74] See footnote no. 66.

[75] This requirement was revised as part of the PPPFA enacted on June 5, 2020, which lowered the threshold from 75% down to 60% of a borrower's PPP loan proceeds.

for payroll costs during the forgiveness period, the borrower will continue to be eligible for partial loan forgiveness, subject to at least 60% of the PPP loan forgiveness amount having been used for payroll costs[76].

- PPP Loan Forgiveness Reduction - The forgiveness amount shall be reduced if there is a decrease in the number of full-time equivalent (FTE) employees or a reduction of more than 25% in wages/salary paid to any employee.
- Re-Hire Safe Harbors – Under the PPP loan program, borrowers are required to maintain the average FTE employees they had prior to the Covid-19 pandemic and maintain salary and wages for all employees making $100,000 or less on an annualized basis at any time during 2019 in amounts at least 75% of the salary and wages they received in the quarter before applying for the PPP loan, or face a proportionate reduction in the amount of the PPP loan that would otherwise be forgiven. The CARES Act (as amended by the PPPFA) and the implementing rules provide for a safe harbor from the PPP loan forgiveness reduction penalty to the extent borrowers restore FTEs and/or salaries and wages, as applicable, by December 31, 2020. This safe harbor is aimed at incentivizing employers to use the PPP loan proceeds to rehire employees and restore pay cuts caused by the Covid-19 crisis.
- A further safe harbor applies which allows borrowers under certain circumstances to treat unfilled positions as if they were filled with rehired employees for purposes of determining the amount of eligible loan forgiveness. In particular, borrowers can treat unfilled positions as if they were filled by the December 31, 2020 deadline if the borrower can in good faith establish and document that: (i) they were unable to rehire individuals who were employees of the borrower on February 15, 2020 and hire similarly qualified employees for the unfilled positions by December 31, 2020; or (ii) they were unable to return to the same level of business activity that the borrower was operating before February 15, 2020 due to compliance with Covid-19 related worker or customer safety requirements or guidance issued by the U.S. Secretary of Health and Human Services (HHS), the Centers for Disease Control and Prevention (CDC), or the Occupational Safety and Health Administration (OSHA) during the period beginning on March 1, 2020 and ending on December 31, 2020.
- Covered Period for PPP Loan Forgiveness – Under the original terms of the CARES Act, borrowers had to use the PPP loan proceeds to pay for the described expenditures in the 8-week period following the PPP loan disbursement. As part of the PPPFA enacted on June 5, 2020, the covered period has been extended to 24 weeks after the date of the disbursement, thus providing greater flexibility for borrowers to qualify for loan forgiveness. Borrowers who had already received PPP loans before the amendment retain the option to use an 8-week covered period. In no event the 'covered period' shall extend past December 31, 2020[77].
- Collateral and Prepayment - PPP loans are unsecured. There is no collateral or personal guarantee required. The PPP loans are non-recourse to the business owner so long as proceeds are used for authorized purposes. No prepayment penalty applies.

[76] See, U.S. Department of the Treasury, Joint Statement by Treasury Secretary Steven T. Mnuchin and SBA Administrator Jovita Carranza Regarding Enactment of the Paycheck Protection Program Flexibility Act (June 8, 2020).

[77] See Paycheck Protection Program Loans, Frequently Asked Questions (FAQs) (as of June 25, 2020), Question no. 20.

- Fees - The SBA shall reimburse lenders for the costs of providing the loans and borrowers should not be required to pay any fees for obtaining a PPP loan.
- Application Process - PPP applications opened on April 3, 2020 for small businesses and sole proprietorships and on April 20, 2020 for independent contractors and self-employed individuals. Barring further legislative action, the PPP applications came to a close on August 8, 2020.

3.1.2. The Emergency Economic Injury Disaster Loans (EIDL) and EIDL Advance Program

The Coronavirus Preparedness and Response Supplemental Appropriations Act enacted on March 6, 2020, together with the CARES Act, expand the existing SBA's Economic Injury Disaster Loan Assistance (EIDL) program aimed at natural disasters to the crisis brought by the Covid-19 outbreak.

Under the expanded EIDL program, the SBA may provide qualifying businesses both EIDL loans and emergency grants. Key terms of the EIDL loans are summarized below:

- Eligible Applicants - Eligible applicants include small business concerns, private nonprofits organizations, and small agricultural cooperatives (as defined by the SBA) with not more than 500 employees (including sole proprietorships and self-employed individuals). The business must have been in operation on January 31, 2020, but it does not need to have been in operation for at least 1-year before the disaster. The SBA's usual requirement that the applicant has not been able to obtain credit elsewhere is waived.
- Maximum Loan Amount – Up to $2 million.
- Maximum Term – The term is determined on a case-by-case basis, depending on the borrower's ability to pay, up to 30 years.
- Interest Rate – 3.75% for small businesses and 2.75% for non-profits.
- Permitted Uses of the Proceeds – Proceeds from an EIDL can be used for any purpose allowed under Section 7(b)(2) of the Small Business Administration Act. These include a wide array of working capital and normal operating expenses, such as continuation of health care benefits, rent, utilities, and fixed debt payments. EIDL loan proceeds cannot be used for the same purpose as PPP loan proceeds discussed above.
- EIDL Advancements – A EIDL loan applicant can receive a prompt advance of $1,000 per employee up to $10,000 that can be used for any allowable use and does not need to be repaid, even if the EIDL loan is ultimately denied. If approved for a PPP loan, then this advance is netted from the loan forgiveness amount (i.e., the advance on the EIDL loan will be deducted from the loan forgiveness amount on the PPP loan).
- Loan Forgiveness - EIDL loans are not forgivable.
- Personal Guarantee - There is no personal guarantee requirement for EIDL advances or loans of $200,000 or less extended in response to the Covid-19 crisis.
- Application process - Qualifying borrowers may apply directly with the SBA[78].

[78] For additional information, see https://www.sba.gov/funding-programs/disaster-assistance/coronavirus-covid-19.

On July 11, 2020, the SBA announced the conclusion of the EIDL advance program[79]. As indicated by the SBA, following the enactment of the Covid-19 emergency legislation, the SBA provided nearly 6 million small businesses employing 30.5 million people with $20 billion through the EIDL advance program. Having allocated all of the $20 billion available funds for the EIDL advance program, the SBA has now discontinued making EIDL advances to new applicants. EIDL loan applications are still being processed even though the EIDL advance program is no longer available.

3.1.3. The Main Street Facilities Program

As part of the CARES Act, on June 15, 2020 the Federal Reserve announced the establishment of the Main Street Lending Program to support lending to small and medium-sized businesses whose financial conditions have been affected by the Covid-19 pandemic[80].

The Main Street Lending Program operates through three facilities for for-profit organizations[81]: the Main Street New Loan Facility (the "MSNLF")[82], the Main Street Priority Loan Facility (the "MSPLF")[83] and the Main Street Expanded Loan Facility (the "MSELF", together with the MSNLF and the MSPLF, the "Main Street Facilities")[84].

In connection with the Main Street Facilities Program, the Federal Reserve of Boston has established a common special purpose vehicle (SPV) that will acquire, at par value, c. 95% participations in loans or

[79] See, U.S. Small Business Administration, SBA Provided $20 Billion to Small Businesses and Non-Profits Through the Economic Injury Disaster Loan Advance Program (July 11, 2020).

[80] The Federal Reserve initially mentioned its intent to create a Main Street Program to facilitate loans to small- and medium-sized businesses in a press release on March 23, 2020. The term sheets outlining the Main Street Program's proposed structure and terms were released on April 9, 2020. The Federal Reserve then issued revised term sheets and a guidance in the form of a FAQs document on April 30, 2020, which is regularly updated and can be retrieved from https://www.bostonfed.org/mslp-faqs. In late May and early June 2020, the Federal Reserve released further updated guidance and legal documentation for the Main Street Program. The legal forms and agreements for eligible borrowers and lenders to participate in the MSNLF, MSELF, or MSPLF can be retrieved from https://www.bostonfed.org/supervision-and-regulation/supervision/special-facilities/main-street-lending-program/information-for-lenders/docs.aspx. See, Federal Reserve, Policy Tools - Main Street Lending Program available at https://www.federalreserve.gov/monetarypolicy/mainstreetlending.htm. See, Federal Reserve, Federal Reserve takes additional actions to provide up to $2.3 trillion in loans to support the economy (The Federal Reserve Press Release, April 9, 2020); Federal Reserve, Federal Reserve Board announces it is expanding the scope and eligibility for the Main Street Lending Program (The Federal Reserve Press Release, April 30, 2020); Federal Reserve Bank of Boston, Federal Reserve Bank of Boston releases additional information for potential lenders and borrowers in the Main Street Lending Program. New Frequently Asked Questions and operational documents available (The Federal Reserve Bank of Boston Press Release, May 27, 2020); Federal Reserve, Federal Reserve Board expands its Main Street Lending Program to allow more small and medium-sized businesses to be able to receive support (The Federal Reserve Press Release, June 8, 2020).

[81] On June 15, 2020, the Federal Reserve announced a proposal to expand its Main Street Lending Program to provide access to credit for small and medium-sized nonprofits that were in sound financial condition before the Covid-19 pandemic. The time period for public comment on the proposal ended on June 22, 2020. On July 17, 2020, the Federal Reserve announced the extension of the Main Street Lending Program to nonprofit organizations and released detailed term sheets for the Nonprofit Organization New Loan Facility (NONLF) and the Nonprofit Organization Expanded Loan Facility (NOELF). See, Federal Reserve, Federal Reserve Board announces it will be seeking public feedback on proposal to expand its Main Street Lending Program to provide access to credit for nonprofit organizations (The Federal Reserve Press Release, June 15, 2020); Federal Reserve, Federal Reserve Board modifies Main Street Lending Program to provide greater access to credit for nonprofit organizations such as educational institutions, hospitals, and social service organizations (The Federal Reserve Press Release, July 17, 2020). The term sheet for the NONLF (effective as of July 28, 2020) can be retrieved from https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200728a10.pdf. The term sheet for the NOELF (effective as of July 28, 2020) can be retrieved from https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200728a11.pdf.

[82] The term sheet for the MSNLF (effective as of July 28, 2020) can be retrieved from https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200728a3.pdf.

[83] The term sheet for the MSPLF (effective as of July 28, 2020) can be retrieved from https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200728a2.pdf.

[84] The term sheet for the MSELF (effective as of July 28, 2020) can be retrieved from https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200728a5.pdf.

upsized tranches of existing loans originated by lenders that satisfy certain eligibility criteria[85]. The SPV will participate *pari passu* with respect to any losses with the eligible lenders, which will retain 5% of the risk of each loan. The U.S. Department of the Treasury, using funds appropriated to the Exchange Stabilization Fund under section 4027 of the CARES Act, will make a $75 billion equity investment in the single common SPV in connection with the MSNLF, the MSPLF and the MSELF. The combined size of the MSNLF, the MSPLF and the MSELF will be up to $600 billion.

The SPV will purchase participations in eligible loans until December 31, 2020[86], unless the Federal Reserve and the U.S. Department of the Treasury extend the facilities under the Main Street Facilities Program. The Reserve Bank will continue to fund the SPV after such date until the SPV's underlying assets mature or are sold[87].

The Main Street Facilities Program limits participation to lenders who fall within any of the following categories: a U.S. federally insured depository institution (including a bank, savings association, or credit union), a U.S. branch or agency of a foreign bank, a U.S. bank holding company, a U.S. savings and loan holding company, a U.S. intermediate holding company of a foreign banking organization, or a U.S. subsidiary of any of the foregoing.

Similarly, to qualify as an eligible borrower under the Main Street Facilities Program, a business shall[88]:

- be established prior to March 13, 2020;
- not be an "ineligible business"[89];
- meet at least one of the following two conditions: (i) having 15,000 employees or fewer, or (ii) having 2019 annual revenues of $5 billion or less[90];
- be created or organized in the United States or under the laws of the United States with significant operations in and a majority of its employees based in the United States;
- participate in only one of the MSNLF, MSPLF and MSELF and may not also participate in the Federal Reserve's Primary Market Corporate Credit Facility; and

[85] The term sheet for the MSPLF as revised on June 8, 2020 increased the Federal Reserve Bank of Boston's participation to 95%, which conforms with the participation levels under the MSNLF and the MSELF. Previously, the Federal Reserve Bank of Boston's participation interest under the MSPLF was set at 85%.

[86] See, Federal Reserve, Federal Reserve Board announces an extension through December 31 of its lending facilities that were scheduled to expire on or around September 30 (The Federal Reserve Press Release, July 28, 2020).

[87] In June 2020, Federal Reserve Bank of Boston President Eric Rosengren indicated that as of June 18, 2020 more than 200 financial institutions had initiated registration and the Federal Reserve continued to see "a steady stream of interest." See, Federal Reserve of Boston Speech by President Eric Rosengren, An Update on the Economy and the Main Street Lending Program (June 19, 2020). As of June 24, 2020, the Main Street Facilities Program was open for lender registration but had not yet purchased any participations in eligible loans. See, Federal Reserve, Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act (July 6, 2020).

[88] For the purposes of the Main Street Facilities Program, a "business" is deemed an entity that is organized for profit as a partnership, a limited liability company, a corporation, an association, a trust, a cooperative, a joint venture with no more than 49% participation by foreign business entities, or a tribal business concern as defined in 15 U.S.C. § 657a(b)(2)(C), except that "small business concern" in that provision should be replaced with "business". Other forms of organization may be considered for inclusion as a "business" under the Main Street Facilities Program at the discretion of the Federal Reserve.

[89] For the purposes of the Main Street Facilities Program, an "ineligible business" is a type of business listed in 13 CFR 120.110(b)-(j) and (m)-(s), as modified by regulations implementing the PPP on or before April 24, 2020. The application of these restrictions to the Main Street Facilities Program may be further modified at the discretion of the Federal Reserve.

[90] The described size tests require aggregation of the borrower with its affiliates. The Federal Reserve guidance incorporates by reference the affiliation rules of the SBA, which shall be considered in determining what entities are affiliates of the borrower for the purposes of these size tests.

- have not received specific support pursuant to the Coronavirus Economic Stabilization Act of 2020 (Subtitle A of Title IV of the CARES Act)[91].

Importantly, meeting the criteria as an eligible borrower discussed above will not automatically entitle an applicant to be approved or to receive the maximum allowable loan amount under any of the three Main Street Facilities. The ultimate decision whether to extend credit will rest with the eligible lenders. Eligible lenders are expected to conduct an assessment of each potential borrower's financial condition at the time of the potential borrower's application, they should apply their own underwriting standards in evaluating the financial condition and creditworthiness of the borrower and they may require additional information and documents from applicants[92]. If the application for a Main Street loan is approved, then the eligible lender will originate and fund the loan. The eligible lender will then be able to sell a 95% participation in the loan at par to the SPV established by the Federal Reserve, while retaining the remaining interest in the loan and servicing the loan. By helping eligible lenders mitigate their credit risks and capital costs associated with the Main Street loans, the Main Street Lending Program aims at creating the right incentives for eligible lenders to extend credit at favorable terms to eligible borrowers and thereby support the economy during the Covid-19 pandemic.

Under the MSNLF, eligible loans are secured or unsecured term loans made by an eligible lender(s) to an eligible borrower originated after April 24, 2020 with a 5-year maturity[93], principal payments deferred for 1 year and interest payments deferred for 1 year (unpaid interest will be capitalized), and prepayment allowed without penalty. Eligible loans must also have an adjustable rate of LIBOR (1 or 3 month) plus 300 basis points, a principal amortization of 15% at the end of the third year, 15% at the end of the fourth year, and a balloon payment of 70% at maturity at the end of the fifth year. In addition, eligible loans must have a minimum loan size of $250,000[94] and be capped at the lesser of (i) $35 million[95] or (ii) an amount that, when added to the eligible borrower's existing outstanding and undrawn available debt, does not exceed 4 times the eligible borrower's adjusted 2019 earnings before interest, taxes, depreciation, and amortization ("EBITDA"). Lastly, eligible loans must not be (at the time of origination or at any time during their term), contractually subordinated in terms of priority to any of the eligible borrower's other loans or debt instruments.

Eligible loans under the MSPLF have features similar to those required under the MSNLF, except that: (i) the size of the loans is capped at the lesser of $50 million[96] and an amount that, when added to the eligible borrower's existing outstanding and undrawn available debt, does not exceed 6 times the eligible borrower's adjusted 2019 EBITDA; and (ii) in terms of priority and security, at the time of origination

[91] Businesses that have received PPP loans are permitted to borrow under the Main Street Facilities Program, provided that they are eligible borrowers under the Main Street Facilities Program.

[92] See Federal Reserve, Main Street Lending Program Frequently Asked Questions (FAQs) (as of July 31, 2020) FAQ no. I.2., available at https://www.bostonfed.org/mslp-faqs.

[93] The Main Street Facilities Program term sheets that were revised on 8 June 2020 increased the term of the loan under each of the three facilities to 5 years. Previously, this was 4 years.

[94] The Main Street Facilities Program term sheets that were revised on June 8, 2020 decreased the minimum loan size under the MSNLF and the MSPLF to $250,000. Previously, this was $500,000.

[95] The term sheet for the MSNLF revised on June 8, 2020 increased the maximum loan size under the MSNLF to $35 million. Previously, the $35 million cap was set at $25 million.

[96] The term sheet for the MSPLF revised on June 8, 2020 increased the maximum loan size under the MSPLF to $50 million. Previously, the $50 million cap was set at $25 million.

and at all times they are outstanding, the eligible loans must be senior to or must rank *pari passu* with the eligible borrower's other loans or debt instruments, other than mortgage debt.

Eligible loans under the MSELF have features similar to those required under the MSNLF, except that: (i) eligible loans are secured or unsecured term loans or revolving credit facilities made by an eligible lender(s) to an eligible borrower originated on or before April 24, 2020, with a remaining maturity of at least 18 months (taking into account any adjustments made to the maturity of the loan after April 24, 2020, including at the time of upsizing); (ii) the upsized tranche of the loan must be a term loan with a minimum size of $10 million and a maximum size equal to the lesser of $300 million[97] and an amount that, when added to the eligible borrower's existing outstanding and undrawn available debt, does not exceed 6 times the eligible borrower's adjusted 2019 EBITDA; and (iii) in terms of priority and security, at the time of upsizing and at all times the upsized tranche is outstanding, the upsized tranche must be senior to or must rank *pari passu* with the eligible borrower's other loans or debt instruments, other than mortgage debt.

Loans made under the Main Street Facilities are subject to certain borrower leverage limitations.

Under the MSNLF and the MSPLF, if an eligible borrower has other loans outstanding with the eligible lender as of December 31, 2019, then those other loans must have had an internal risk rating equivalent to a "pass" in the Federal Financial Institutions Examination Council's supervisory rating system on that date. Under the MSELF, the eligible loan must have had an internal risk rating equivalent to a "pass" in the Federal Financial Institutions Examination Council's supervisory rating system as of December 31, 2019.

Eligible borrowers must pay eligible lenders an origination fee of up to 100 basis points of the principal amount of the eligible loan at the time of the origination or 75 basis points of the principal amount of the upsized tranche of the eligible loan at the time of upsizing; eligible lenders must pay the SPV a facility fee of 100 basis points of the principal amount of the participation sold to it or 75 basis points of the principal amount of the upsized tranche of the eligible loan at the time of upsizing (though they may pass that cost on to eligible borrowers); and the SPV shall pay eligible lenders an annual 25 basis point servicing fee.

Eligible borrowers under the Main Street Facilities Program must attest, among other things, that they require financing due to circumstances caused by the Covid-19 crisis, will not use the proceeds of any eligible loan or tranche to repay other loan balances, will not seek to cancel or reduce outstanding lines of credit from any of their lenders and will not pre-pay off other debt of equal or lower priority before repaying the eligible loan or tranche. Eligible borrowers must also make reasonable efforts to maintain their payroll and employees during the term of the eligible loans and tranches are outstanding[98]. In addition, eligible borrowers are subject to limitations with respect to their ability to make dividend

[97] The term sheet for the MSELF revised on June 8, 2020 increased the maximum loan size under the MSELF to $300 million. Previously, the $300 million cap was set at $200 million.

[98] The Federal Reserve guidance clarifies the "commercially reasonable efforts" standard and explains that a Main Street borrower should undertake good-faith efforts to maintain payroll and retain employees, in light of its capacities, the economic environment, its available resources, and the business need for labor. The guidance also clarifies that businesses that have already laid off or furloughed workers as a result of the Covid-19 crisis may still be eligible for the Main Street program. See Federal Reserve, Main Street Lending Program Frequently Asked Questions (FAQs) (as of July 31, 2020) FAQ no. G.8.

payments and capital distributions, conduct stock buybacks and must comply with certain employee compensation related restrictions.

3.2. The UK Government's Covid-19 Funding Measures

In response to the market disruption brought by the outbreak of the Covid-19 pandemic, on April 20, 2020 the UK government announced a £1.25 billion government support package providing financing to startups and growth stage companies driving innovation and development in UK[99]. As Chancellor of the Exchequer Rishi Sunak explained in a statement, this support package has been designed to ensure that early and high-growth firms in some of the most dynamic sectors of the UK economy – ranging from tech to life sciences – are protected through the crisis and receive the investment they need to continue to develop innovative new products and help power UK growth[100].

The support package includes £750 million of targeted support for small and medium sized businesses focusing on research and development ("R&D"), as well as a new £500 million loan scheme for high-growth firms called the Future Fund.

The £750 million of targeted support for the most R&D intensive small and medium size firms is made available through Innovate UK's grants and loan scheme. Innovate UK, the national innovation agency, has been tasked with accelerating up to £200 million of grant and loan payments for its 2,500 existing Innovate UK customers on an opt-in basis. An extra £550 million is also being made available to increase support for existing customers and £175,000 of support will be offered to around 1,200 firms not currently in receipt of Innovate UK funding[101].

The Future Fund scheme has been designed by the UK government and is delivered in partnership with the British Business Bank. At HM Treasury's request, global law firm Goodwin Procter LLP assembled and led a task force of four law firms (Goodwin Procter LLP, Cooley LLP, Taylor Wessing LLP and Orrick, Herrington & Sutcliffe LLP) with deep expertise in the UK emerging and innovative companies and venture capital sector to advise the UK government on this groundbreaking scheme. The remaining part of this section will discuss the eligible criteria and key features of the Future Fund.

3.2.1. The Future Fund Scheme

The Future Fund provides UK-based companies with between £125,000 and £5 million in the form of a convertible loan which is invested directly by the UK government, with private investors at least matching the government commitment. There is no cap on the amount that the matching investors may loan to the investee company.

The scheme opened for applications on May 20, 2020 and will initially remain open until the end of September 2020[102]. The UK government committed an initial £250 million in funding towards the scheme. On June 30, 2020, the UK HM Treasury announced that more funding was being made available due to the popularity of the Future Fund, with around £320 million already awarded to more than 320

[99] See, UK HM Treasury and Innovate UK, Billion pound support package for innovative firms hit by coronavirus (20 April 2020).
[100] Ibidem.
[101] For an overview of the Future Fund Scheme, see https://www.uk-futurefund.co.uk/s/.
[102] See, UK HM Treasury, Future Fund launches today (May 20, 2020).

companies. As the number of applications to the Future Fund rises sharply, the scale of the scheme remains under review at the date of writing[103].

The scheme is structured as an investor-led scheme, meaning that a lead investor shall apply and shall include information about other investors making up the investment round in connection to an applicant company. Once the lead investor has submitted an application, the applicant company will receive an email with instructions on how to proceed with opening an online account and progress the application. Applications are expected to take a minimum of 21 days from the submission of the application through to the funding being awarded. In the case of approved applications, all parties will then execute a convertible loan agreement and shall satisfy certain conditions set out in the agreement before the Future Fund monies are released, including the delivery of a director's certificate from the investee company and a solicitor confirmation letter (each in the form provided by the scheme)[104]. The distribution of funds for successful applications is handled through a solicitor nominated by the investee company.

The form of the convertible note agreement to be entered into by the lead investors, the other matching investors (if any), the investee company and UK FF Nominees Limited[105] following a successful application is a fixed, standard form document[106]. However, certain terms of the convertible note agreement, including the interest rate, conversion discount, headroom amount and valuation cap are negotiable between the investors (other than the Future Fund) and the investee company in advance of the application.

The key terms of these convertible loans include the following:

- Maturity - A term of 36 months.
- Discount - 20% discount rate, unless a higher rate is agreed by the investee company and the matching investors.
- Interest Rate - 8% non-compounding interest rate, unless a higher rate is agreed by the investee company and the matching investors. The interest is not payable on a monthly basis and instead will accrue until the loan converts or in the event of default of the investee company. On conversion of the loans, only the principal amount of the loans will convert at the discount rate; accrued interest converts without any discount. On conversion of the principal, the investee company can elect (at its sole discretion) to repay the accrued interest, rather than having the interest convert but not at the discount rate.
- Valuation Cap - No valuation cap, unless one is agreed by the investee company and the matching investors.
- Conversion/repayment events – the loans convert as follows:

[103] See, UK HM Treasury, More firms can now benefit from the Future Fund (June 30, 2020).

[104] The Future Fund scheme documents can be retrieve from https://www.british-business-bank.co.uk/ourpartners/coronavirus-business-interruption-loan-schemes/future-fund/scheme-documentation/.

[105] UK FF Nominees Limited is the entity that enters into the convertible loan agreements on behalf of the Future Fund. UK FF Nominees Limited is the legal titleholder to the Future Fund's convertible loans and any shares resulting from their conversion on behalf of the UK government. It holds beneficial interest in the convertible loans (and any shares resulting from their conversion) on bare trust for the benefit of the Secretary of State for Business, Energy and Industrial Strategy.

[106] The form of the convertible loan agreement can be retrieved from https://british-business-bank.my.salesforce.com/sfc/p/#3z000002Naf6/a/3z000000MDFe/MQPBr0RySVNE.QGVZpNIUEkWu_2mbCNOSSGpx.oMxqA.

    - Qualifying fundraising – If the investee company completes an equity funding round at least equal to the aggregate amount of the loans provided under the scheme, all loans provided to the investee company pursuant to the scheme will automatically convert into the same class of shares as issued to the investors participating in the qualifying round at the agreed discount (or the valuation cap, if applicable).
    - Non-qualifying fundraising – If so elected by the holders of a majority of the principal amount of the loans other than the Future Fund ("the lender majority"), all loans provided to the investee company under the scheme will convert into the same class of shares as issued to the investors in a non-qualifying funding round at the agreed discount (or valuation cap, if applicable), provided that if the amount being raised in the non-qualifying fundraising is equal to or less than 25% of the aggregate principal amount of all the loans the investee company has taken in pursuant to the scheme, then the consent of the Future Fund is also required.
    - Exit – All loans provided under the scheme will either automatically convert into the most senior class of shares in issue at the time of the exit at the conversion price or be repaid with a redemption premium (being a premium equal to 100% of the principal of the loan), whichever provides the greater amount for the investors in respect of their loans under the scheme. If the consideration being provided as part of the exit contains any non-cash consideration, the Future Fund (in respect of its loan only) and/or the lender majority (in respect of all loans other than the loan made by the Future Fund) can elect instead to have the loans repaid with the redemption premium.
    - Maturity date – The loans will automatically convert into the most senior class of shares in the investee company in issue on the maturity date. Alternatively, the Future Fund (in respect of its loan only) and/or the lender majority (in respect of all loans other than the loan made by the Future Fund) can elect to have the loans repaid with the redemption premium.
    - Events of default – On an event of default, each investor in the scheme can require repayment of its loan plus interest at the redemption premium. The breach of certain of the covenants in the convertible loan agreement constitute events of default in favor of the Future Fund only, which shall be entitled to demand repayment and the redemption premium in such events.
- Security - The convertible loan shall be unsecured, rank *pari passu* with all other unsecured indebtedness or obligations of the investee company and be subordinated to any secured debt of the investee company.
- Most-Favored Nation - If prior to conversion of the loans the investee company issues further convertible loans or advance subscriptions to investors with more favorable terms than those provided to the investors on their loans under the scheme, then the same terms will apply to the loans provided under the scheme. The investee company shall notify each investor in the scheme of such arrangements and provide documents and details of such favorable rights.

- Other Indebtedness – For so long as the loans provided under the scheme are outstanding, the investee company shall not, without the prior consent of the lender majority and the Future Fund, permit the creation of any indebtedness that is senior to the loans provided under the scheme. This restriction does not apply to *bona fide* senior indebtedness from a person that is not an existing shareholder or scheme investor or pursuant to any *bona fide* venture debt facilities.
- Information Rights – The Future Funds has certain information rights, including those set out in schedule 4 to the convertible loan agreement and, at the Future Fund's request, the same information as is provided by the investee company to its lead or other major investors, subject to the ability of the Board of the investee company, acting reasonably, to withhold information that is commercially sensitive or legally privileged.
- Governance Rights - The Future Fund has limited governance rights. In particular, the convertible loan agreement provides a right for the Future Fund to request a meeting with the investee company once a conversion event is to take place in order to discuss in good faith the suite of shareholder governance rights that may be afforded to the Future Fund on conversion of its loan that are to be commensurate with its proportion of the share capital in the investee company. The investee company is under no obligation to agree to provide any specific shareholder rights in those good faith discussions.

To be eligible for the scheme, a company must meet the following criteria[107]:

1. The company must have raised at least £250,000 in equity from third-party investors in previous funding rounds in the last 5 years (from April 1, 2015 to April 19, 2020 inclusive);
2. If the company is a member of a corporate group, it must be the ultimate parent company;
3. The company does not have any of its shares or other securities listed on a regulated market, a multilateral trading facility, a recognized investment exchange and/or any other similar market, stock exchange or listing venue;
4. The company must be a UK incorporated limited company or be eligible to apply as a non-UK parent company[108];
5. The company must have been incorporated on or before December 31, 2019 (or if a non-UK jurisdiction company, this criterion applies to at least one UK subsidiary operating company); and
6. At least one of the following must be true for the company (if a non-UK jurisdiction company, this criterion applies to the group):
   - Half or more employees are UK based
   - Half or more revenues are from UK sales

[107] See, Future Fund: Information for Companies available at https://www.uk-futurefund.co.uk/s/Business.

[108] The Future Fund was initially open only to companies incorporated in the UK. This meant that UK early stage and fast-growing companies that have moved their legal headquarters overseas to raise funding from international investors were not eligible to the scheme. The UK government expanded the scheme's eligibility criteria in June 2020 so that UK companies that have participated in highly selective accelerator programmes and were required, as part of that programme, to have a parent company outside of the UK would be able to apply for investment under the scheme. This change considers accelerator programmes, such as TechStars or Y-Combinator. See, UK HM Treasury, More firms can now benefit from the Future Fund (June 30, 2020).

If it applies as a non-UK jurisdiction parent company, the applicant company must also meet the following criteria[109]:

7. The company must have participated in an accelerator programme, on or before April 19, 2020, and participation in the accelerator mandated incorporation of the ultimate parent company in a non-UK jurisdiction[110];
8. The company must have received investment from the accelerator programme on or before April 19, 2020;
9. The company must be the ultimate parent company of a group which contains at least one subsidiary operating company incorporated in the UK on or before December 31, 2019; and
10. If the group (or any entity within the group) was in existence before the company was incorporated, the ultimate parent company of the group (or the sole entity, if applicable) must have been incorporated in the UK.

In order to be eligible for the scheme, each of the investor(s) must fall within any of the following categories[111]:

1. An "investment professional" within the meaning given to that term in article 19 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 ("FPO").
2. A high-net worth company, unincorporated associated or high-value trust falling within article 49(2) of the FPO.
3. A "certified sophisticated investor" or a "self-certified sophisticated investor" within the meaning given in articles 50 and 50A respectively of the FPO.
4. A "certified high-net worth individual" within the meaning of article 48 of the FPO.
5. An equivalent professional, high-net worth, institutional or sophisticated investor in accordance with applicable law and regulation in such investor's home jurisdiction.
6. An association of high-net worth or sophisticated investors within the meaning of article 51 of the FPO.
7. A "professional client" within the meaning given in the glossary to the FCA Rules.

In addition to meeting one of the above definitions of eligible investors, to be eligible for the matched funding an investor must be a private investor, person, company or fund who is not a connected person (within the meaning of sections 1122 and 1123 of the Corporation Tax Act 2010) and invests capital into a company, with the objective of helping that company grow and getting a return on their investment.

[109] In relation to non-UK companies, to protect the use of public funds, all applications are being assessed against UK Government investment standards on specific jurisdictions by reference to factors such as sanctions, tax transparency, and the cost and complexity of implementation. The UK government also takes into account concerns around the proper use of public finances and wider public policy risks, as well as whether the proposed investment would undermine the integrity or public credibility of the Future Fund.

[110] See, Future Fund Frequently Asked Questions (FAQs) for non-UK Parent Companies, definition of "Accelerator Programme" available at: https://british-business-bank.my.salesforce.com/sfc/p/#3z000002Naf6/a/3z000000MElk/pOId6dK7xNdrRGm70aB1Py3y9q_qUJZO1Iz81ABQA08.

[111] See, Future Fund: Information for Investors available https://www.uk-futurefund.co.uk/s/Investor.

For investors applying as a group, a minimum commitment of £12,500 is required by the investor completing the application acting as the lead investor[112].

Matching fund investors are encouraged to sign the UK HM Treasury's Investing in Women Code, which commits firms to improving female entrepreneurs' access to tools, resources and finance. The Future Fund is a signatory of this.

The proceeds of the convertible loan agreement must not be used by the investee company to[113]:

- Repay any borrowings from a shareholder or a shareholder related party (other than the repayment of any borrowings pursuant to any bank or venture debt facilities);
- Pay any dividends or other distributions;
- For a period of twelve months from the date of the relevant convertible loan agreement, make any bonus or other discretionary payment to any employee, consultant or director of the investee company other than as contracted prior to the date hereof and as paid by the investee company in the ordinary course of business; or
- Pay any advisory or placement fees or bonuses to any corporate finance entity or investment bank or similar service provider on monies advanced by the Future Fund.

3.3. EU States' Governmental Covid-19 Funding Measures

On March 19, 2020, the EU Commission adopted a Temporary Framework for State aid (the "Temporary Framework") to support the economy in the context of the Covid-19 outbreak based on Article 107(3)(b) of the Treaty on the Functioning of the European Union[114]. The Temporary Framework allows EU Member States to use the full flexibility foreseen under State aid rules to ensure that sufficient liquidity remains available to businesses and to preserve the continuity of economic activity during and after the Covid-19 outbreak. The Temporary Framework provides for five types of aid to support the economy: (i) direct grants, selective tax advantages and advance payments (up to Euro 800,000 per company), (ii) State guarantees for loans taken by companies from banks, (iii) subsidized public loans to companies, (iv) safeguards for banks that channel State aid to the real economy and (v) flexibility to enable short-term export credit insurance.

The Temporary Framework was subsequently amended on April 3, 2020[115]. The first amendment extends the Temporary Framework to enable EU Member States to accelerate the research, testing and production of Covid-19 relevant products, to protect jobs and to further support the economy in the context of the Covid-19 outbreak. In particular, the first amendment provides for five additional types of aid measures:

[112] For a detailed representation of the role of the investor as part of the application process, see https://british-business-bank.my.salesforce.com/sfc/p/#3z000002Naf6/a/3z000000MDFg/EguL.ZGdKfyWkzoPglTIk.ZUzUeflA005TumxowQn0Y.

[113] See, Future Fund: Information for Companies available at https://www.uk-futurefund.co.uk/s/Business.

[114] See, European Commission, Communication from the Commission: Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak (European Commission, March 19, 2020). The Temporary Framework complements the possibilities for Member States to design measures in line with existing EU State aid rules, as set out in the Communication on a Coordinated economic response to the COVID-19 outbreak of March 13, 2020. See, European Commission, COVID-19: Commission sets out European coordinated response to counter the economic impact of the Coronavirus (European Commission Press Release, March 13, 2020).

[115] See, European Commission, State aid: Commission extends Temporary Framework to enable Member States to accelerate research, testing and production of coronavirus relevant products, to protect jobs and to further support the economy in the coronavirus outbreak (European Commission Press Release, April 3, 2020); European Commission, Communication from the Commission: Amendment to the Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak (European Commission, April 3, 2020).

(i) targeted deferrals of tax or suspension of social security contributions, (ii) targeted support in the form of wage subsidies for employees, (iii) support for Covid-19 research and development, (iv) support for the construction and upscaling of testing facilities and (v) support for the production of products relevant to tackling the Covid-19 outbreak. The amendment also expands on the existing types of support that EU Member States can give to companies in need. For example, it enables EU Member States to give (up to the nominal value of Euro 800,000 per company) zero-interest loans, guarantees on loans that cover 100% of the risk, or provide equity. This can be combined with so-called *de minimis* aid (to bring the aid per company up to Euro 1 million) and with other types of aid and it is aimed to promptly address urgent liquidity needs of small and medium-sized enterprises ("SMEs").

On May 8, 2020, the EU Commission approved a second amendment to the Temporary Framework[116]. The second amendment complements the types of measures already covered by the Temporary Framework and existing State aid rules, by setting out criteria on which EU Member States can provide recapitalizations and subordinated debt to companies in need, whilst protecting the level playing field in the EU. As this is intended to be a measure of last resort, the second amendment sets out a number of safeguards to avoid undue distortions of competition. These include: (i) conditions on the necessity, appropriateness and size of intervention, (ii) conditions on the EU Member State's entry in the capital of the company and remuneration, (iii) conditions regarding the exit (including time limits) of the EU Member State from the capital of the company, (iv) governance conditions and (v) the prohibition of cross-subsidization and acquisitions. In order to maintain transparency, EU Member States shall publish the identity of the recipients of the recapitalization aid within three months. Furthermore, beneficiaries, other than SMEs, shall publish information on the use of the aid received, including on how the aid received supports the company's activities in line with EU and national obligations linked to the green and digital transformation.

The EU Commission adopted a third amendment to the Temporary Framework on June 29, 2020[117]. With the third amendment, the EU Commission acknowledged that micro and small companies (i.e. undertakings with less than 50 employees and less than Euro 10 million of annual turnover and/or annual balance sheet total) have been particularly affected by the liquidity shortage caused by the economic impact of the Covid-19 outbreak, thus exacerbating their existing difficulties to access financing compared to larger enterprises. If left unaddressed, these problems could lead to a large number of bankruptcies of micro and small companies, causing serious disturbances to the entire EU economy. On that basis, the third amendment extends the scope of the Temporary Framework to support all micro and small companies (including innovative startups) even if already in financial difficulty on December 31, 2019 (unless such companies are in insolvency proceedings, have already received rescue aid that hasn't been repaid or are subject to a restructuring plan under the EU State-aid rules).

[116] See, European Commission, State aid: Commission expands Temporary Framework to recapitalisation and subordinated debt measures to further support the economy in the context of the coronavirus outbreak (European Commission Press Release, May 8, 2020); European Commission, Communication from the Commission: Amendment to the Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak (European Commission, May 8, 2020).

[117] See, European Commission, State aid: Commission expands Temporary Framework to further support micro, small and start-up companies and incentivise private investments (European Commission Press Release, June 29, 2020); European Commission, Communication from the Commission: Third amendment to the Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak (European Commission, June 29, 2020).

The third amendment also provides incentives for private investors to participate in certain recapitalization measures, with the aim to encourage capital injections with significant private participation in companies, limit the need for State aid and the risk of competition distortions. If a private investor contributes at least 30% of the new equity (at the same conditions as the EU State) then some of the recapitalization restrictions applicable under the Temporary Framework are relaxed. For example, the acquisition ban and the cap on remuneration of the management are limited to 3 years and the dividend ban is lifted for the holders of the new shares as well as for existing shares, provided that the holders of those existing shares are altogether diluted to below 10% in the company. Furthermore, in line with the principle of neutrality towards public or private ownership of the Treaty on the Functioning of the EU, the third amendment enables companies with an existing State shareholding to raise capital from their shareholders similar to private companies. Where the aforesaid conditions relating to the participation of private investors in the capital increase are met and the EU State is an existing shareholder investing pro rata to its existing shareholding, the EU Commission does not consider it necessary to impose specific conditions as regard to the EU State's exit.

The Temporary Framework as amended will be in place until the end of December 2020, except in relation to the recapitalization measures which the EU Commission has agreed to extend until the end of June 2021 to ensure legal certainty.

Within the EU framework, governments across Europe have adopted state-sponsored packages to support businesses affected by the Covid-19 crisis. The measures implemented range from tax forbearance to state-subsidized furlough schemes to financing and grants. The remaining part of this section discusses certain funding related measures implemented by three EU countries in response to the Covid-19 crisis – Germany, France and Italy.

3.3.1. Germany

The German Federal Government and the German Federal States have enacted a number of public funding support programs open to private equity- and VC-backed companies, aimed at mitigating the economic impact of the Covid-19 crisis on these companies and the broader German economy.

3.3.1.A. Economic Stability Fund

In March 2020, the German parliament adopted various Covid-19 related legislative initiatives including the establishment of the Economic Stability Fund ("ESF"). The guarantees and recapitalization measures which can be granted under the ESF are generally limited to large companies of the "real economy" outside of the financial sector which exceed the criteria of SMEs.

However, the recapitalization measures (including debt and equity instruments) can, at the discretion of the committee of the ESF, be extended to start-ups and emerging companies that do not meet the eligibility criteria regarding balance sheet assets, revenues and workforce, provided that these fall within any of the following categories:

- companies that provide services or produce or deliver goods that are particularly relevant for the economy, the security or the common welfare in Germany;

- companies of comparable importance to the security or the economy in Germany; or
- companies that have completed at least one financing round with private investors since January 2017 resulting in a company valuation of at least Euro 50 million.

3.3.1.B. KfW Loan Programs

KfW Start-Up Loan – Universal

Under the German state-owned development bank *Kreditanstalt für Wiederaufbau* ("KfW") Start-Up Loan Scheme, KfW will assume a portion of the risk from client facing banks through back-to-back loans: 80% of the risk is assumed for large companies and up to 90% of the risk is assumed for SMEs.

The eligibility criteria for the KfW Start-Up Loan Scheme are as follows:

- The loan scheme is only available to companies that have been on the market for less than 5 years and which have temporary financing difficulties due to the Covid-19 crisis.
- The companies must not have met the EU definition of "undertakings in difficulty" on December 31, 2019.
- The loan may be used for investments and working capital (e.g., operating resources, warehouse, or acquisition of assets from other companies, including takeovers and active participations). The loans cannot be used to refinance existing exposures, for follow-up financing or to repay drawings on existing credit lines.
- Companies in which private equity investors have an interest (regardless of the size) are eligible. Companies in which banks have a stake of more than 25% are not eligible.
- German companies participating in this scheme are asked to suspend profit and dividend payments for the term of the loan in order to qualify. However, standard remuneration for business owners remain available.

An eligible company can apply for up to Euro 100 million (per company group). The loan amount is limited to a maximum of:

- 25% of the annual turnover in 2019;
- twice the wage costs in 2019;
- the current financing requirements for the next 18 months for SMEs or 12 months for large companies; or
- 50% of the company's total debt in the case of loans exceeding Euro 25 million.

The specific interest rate depends on the term of the loan, the loan amount, the provided collateral and the specific investment purpose.

KfW Entrepreneurial Loan

Enterprises which have been on the market for more than 5 years could apply for the KfW Entrepreneurial Loan, which has eligibility criteria similar to those of the KfW Start-Up Loan – Universal scheme discussed above.

KfW Instant Loan

The KfW Instant Loan scheme is targeted to companies with more than 10 employees that have been active in the market since at least January 1, 2019. Eligible companies must not have been in financial difficulty as of December 31, 2019. In addition, the KfW Instant Loan scheme requires that the companies have reported a profit on average over the last 3 years (or a shorter period if not yet been on the market for 3 years).

Under the KfW Instant Loan scheme, the bank receives a 100% risk assumption from the KfW, secured by a guarantee from the German Federal Government. No further collateral is required. The credit approval process does not involve additional credit risk assessment by the bank or KfW. The amount of each loan is limited to up to 3 months-turnover in 2019, with a maximum of Euro 500,000 for companies with up to 50 employees and a maximum of Euro 800,000 for companies with more than 50 employees. Interest rate of 3% for a term of 10 years, with an interest only period of up to 2 years.

3.3.1.C. KfW Special Program for Syndicate Financing

The KfW offers syndicated large-scale financing for investments and working capital for domestic and foreign medium-sized enterprises and large companies which are mainly privately owned. KfW assumes up to 80% of the credit risk of the financing, but no more than 50% of the applying company's total debt.

The KfW risk share amounts to at least Euro 25 million and is limited to:

- 25 % of the annual turnover in 2019; or
- twice the wage costs of 2019; or
- the current financing needs for the next 12 months.

3.3.1.D. Special Support Program for Start-Ups

In addition to the described loan programs, the German Federal Government has set up a program for the benefit of start-ups and growth-stage enterprises with an aggregate budget of around Euro 2 billion. The start-up support is facilitated through KfW's subsidiary KfW Capital which invests in German and European VC and debt funds and the European Investment Fund ("EIF") (each a "CMF Institution")

The program is based on two pillars: (1) the Corona Matching Facility which aims to provide German startups with needed support as quickly and efficiently as possible in order to bridge liquidity problems caused by the Covid-19 crisis[118], and (2) financial support for start-ups and young growth enterprises not backed by VC funds and thus not eligible for funding under the Corona Matching Facility. The following measures are implemented under each of the described pillars:

- Pillar 1 - The Corona Matching Facility ("CMF")
    - The CMF addresses companies closely related to Germany and backed by VC funds which are managed by accredited European private VC fund managers ("GPs") (excluding corporate venture capital firms) which have successfully completed due diligence by a CMF Institution[119].

[118] For more information on the KFW Corona Matching Facility, see a description of relevant objectives and requirement at https://kfw-capital.de/en/corona-matching-facility and a summary chart available at https://kfw-capital.de/wp-content/uploads/CMF-One-Pager_EN-Kfw-capital-u-EIF.pdf.

[119] The portfolio companies or new investment companies shall be closely related to Germany with no financial difficulties as of December 31, 2019, no financial or strategic majority investor, funding round documentation in place and tender obligation for

    - Under the CMF, financing rounds by GPs' companies are matched by public CMF funding. GPs can choose to match financing rounds of either existing portfolio companies or both existing portfolio companies and new initial investments.
    - The VC funds (and not the start-ups) can apply for the CMF. The GP enters into a co-investment and trust framework agreement with a CMF Institution under which it acts as a fiduciary for public funds made available under the CMF. Funds are made available from the CMF Institution to the GP in an amount matching the funds invested in the company by the GP at a matching ratio selected by the GP (from 50% up to a maximum 70%). A matching ratio above 50% can only be selected if other private or public investors also participate in a financing round as the CMF Institution's share shall not exceed 50% of a financing round[120].
    - The GP has separate tender obligations to offer any future investments in portfolio companies or new investments made until December 31, 2020 for matching under the CMF[121].
    - Funds under the CMF are made available in the same manner (e.g. convertible loans or equity) as any funds invested by the GP and at the same commercial terms. The GP selects the type of exit and timing. No management fee is payable from the CMF Institution to the GP and no carried interest is charged.
- Pillar 2 - Additional support for start-ups/SMEs:
    - The second pillar aims to support young start-ups and SMEs not backed by VC funds (and thus without access to the CMF) through collaboration with the German Federal States.
    - It is intended to provide liquidity support and funding through associations of the federal states or through state development institutes which can then pass the funds on to start-ups and small SMEs via their network. The risk will be shared between the federal government or the federal states and private investors.

3.3.1.E. Emergency Aid for Small Businesses

To ensure the liquidity of small companies, the German Government offers a one-off non-repayable payment for up to Euro 9,000 for companies with up to 5 employees and Euro 15,000 for companies with up to 10 employees. The precise amount depends on the liquidity needs of the relevant company.

3.3.2. France

The French government announced a comprehensive support plan of Euro 4 billion for startups and SMEs in response to the Covid-19 crisis in March 2020. The support plan includes the following measures[122]:

current and new investments until December 31, 2020. Eligible investing schemes and funds can be existing funds or newly established SPVs. Existing funds must have successfully passed KYC and governance checks with standard market terms, fund currency and maturity in line with CMF Institution guidelines, no single majority shareholder and shares of private investors in the fund of less than 50%; whilst newly established SPVs must have state aid conformity and no other GPs or VC funds as investors.

[120] The GP selects the matching ratio for all rounds of financing until December 31, 2020, which has to be the same for all of its portfolio companies. For new investments, the GP can select different matching ratios no larger than the ratio for its portfolio companies.

[121] Applications are open from May 14, 2020 through to December 31, 2020. For any financing round already agreed as of April 2, 2020 and to the extent indicated in the documentation, the CMF can be applied retroactively.

[122] For further information, see https://www.economie.gouv.fr/covid19-soutien-entreprises.

- A Euro 80 million bridge funding program financed by the Investments for the Future Program and managed by Bpifrance (a French state-owned investment bank). The program targets startups whose fundraising plans were stymied by a contraction in the VC activity caused by the Covid-19 crisis. The bridge financing ranges from Euro 100,000 to 5 million, takes the form of convertible bonds with access to capital, and shall be co-financed by private investors.
- State guarantee for treasury loans for an amount of up to twice the company's 2019 French payroll or, if higher, 25% of its annual turnover. The loans are distributed by private banks and Bpifrance.
- Acceleration of the reimbursement of corporate tax credits that can be returned in 2020, including the research tax credit for the year 2019 and VAT credits.
- Acceleration of the reimbursement of innovation aid already granted but not paid in 2020 for an amount of around Euro 250 million.
- Lump payments of Euro 1,500 for the self-employed or very small companies. To be eligible, businesses shall report a turnover of less than Euro 1 million and be subject to mandatory closure or have experienced a decrease of turnover of at least 50% due to the Covid-19 crisis.

In June 2020, the French government announced further measures as part of its support plan for startups and SMEs, including the following:

- A new investment fund for key technology companies. Bpifrance will invest Euro 150 million as part of this fund. The fund could be extended in 2021 to reach Euro 500 million.
- Euro 80 million replenishment of the bridge funding program discussed above.
- Loans from Bpifrance (for up to a total of Euro 100 million) for startups that don't qualify to receive a government-backed loan.
- Reinforcement of innovation aid schemes with an aggregate Euro 155 million injection in various vertical-specific funds (eg, *Programme de soutien à l'innovation majeure*, i-Nov, AI Challenge).
- Euro 200 million financing for deep-tech startups and accelerators through a technology transfer fund and a French Tech Accélération fund.

3.3.3. Italy

The Italian government has introduced a tailored package of financial support measures in response to the Covid-19 crisis[123]. These measures include guarantee schemes from SACE S.p.A. ("SACE"), the Italian government and the Central Guarantee Fund, as well as temporary measures to support the liquidity of startups and SMEs which are briefly discussed below.

3.3.3.A. The SACE Guarantee Scheme

SACE S.p.A., the Italian export credit finance agency, has been tasked with providing up to Euro 200 billion in loan guarantees through to December 31, 2020. Borrowers can request a SACE guarantee for

[123] See, Law Decree no. 34/2020 ("Decreto Rilancio"), Law Decree no. 23/2020, converted into Law no. 40 of June 5, 2020 ("Decreto Liquidita") and Law Decree no. 18/2020, converted into Law no. 27 of April 24, 2020 ("Decreto Cura Italia").

financing provided by banks, national and international financial institutions and other authorized lenders in Italy. These include bonds (with a rating at least equal to BB- (or its equivalent)), loans, as well as assignments of receivables on a *pro solvendo* basis.

A SACE guarantee can be requested by companies with a registered office in Italy that were not classified as an "undertaking in difficulty" as of December 31, 2019 and whose liabilities were not classified as "deteriorated" as of February 29, 2020 (as defined under applicable EU regulation).

A SACE guarantee can be used in relation to financings granted from the entry into force of the "*Decreto Liquidita"*" through to December 31, 2020 for personnel costs, investments, rent or leases of going concern, and working capital relating to relevant operations in Italy. Up to 20% of the financing covered by the SACE guarantee can be used for the payment of loan instalments which are past due or become due during the period from March 1, 2020 to December 31, 2020 (if the repayment of such instalments is precluded as a result of the Covid-19 crisis or the measures aimed at preventing and containing it), and fees for the implementation of Covid-19 prevention measures.

The maximum amount covered by a SACE guarantee is equal to:

- 90% of the principal amount of the financing for companies that employ up to 5,000 people in Italy and have annual revenues not exceeding Euro 1.5 billion;
- 80% of the principal amount of the financing for companies that employ more than 5,000 people in Italy, or have annual revenues between Euro 1.5 billion and Euro 5 billion; or
- 70% of the principal amount of the financing for companies that have more than Euro 5 billion annual revenues.

The SACE guarantee is subject to a number of eligibility criteria, including the following:

- The relevant financing shall have a maturity of up to 6 years, with a pre-amortization period of up to 36 months.
- The aggregate amount of all financings granted to the same entity backed by a state guarantee shall not exceed the greater of 25% of the beneficiary's 2019 annual revenue or twice its 2019 employment-related costs.
- Employee-related measures must be managed through agreements with the relevant trade unions.
- The beneficiary of the SACE guarantee and other entities registered in Italy that are part of the same group are prohibited from distributing dividends or implementing a share buy-back in 2020. If the company has distributed dividends or has completed a share buy-back before requesting the financing, then such restrictions shall apply during the 12-month period following the request.

The amount of the annual commission for a SACE guarantee varies depending on the beneficiary: for loans to SMEs, 25 bps (first year), 50 bps (second and third year), and 100 bps (fourth, fifth and sixth year); and for loans to other eligible companies, 50 bps (first year), 100 bps (second and third year), and 200 bps (fourth, fifth and sixth year).

The obligations of SACE arising from the described guarantees are guaranteed by a first-demand, express, unconditional, irrevocable and non-recourse State guarantee. This counter-guarantee covers all of the obligations of SACE with respect to the principal amount, interest and ancillary charges, net of the fees received by SACE for its guarantee.

Two alternative procedures must be followed to benefit from the SACE guarantee. Companies that employ up to 5,000 people in Italy and have annual revenues not exceeding Euro 1.5 billion can access the SACE guarantee through a simplified procedure involving the relevant company, the lender(s) and SACE. For other applicants, the application process for a SACE guarantee involves an approval process by the Italian Ministry of Economy and Finance in consultation with the Italian Ministry of Economic Development. The Ministry of Economic Development's approval is granted by means of a decree, based on a review by SACE and taking into consideration the relevance of the applicant and its activities in the following areas: technological development, supply chain and logistics, critical and strategical infrastructures, strategic production chain, job market and employment levels.

3.3.3.B. CDP Fund

Following the "*Decreto Rilancio*", the Italian Government has endowed Cassa Depositi e Prestiti S.p.A. ("CDP") with a Euro 44 billion fund (the "CDP Fund") to make investments in medium-to-large size industrial companies affected by the Covid-19 pandemic.

The CDP Fund is managed by the CDP Board of Directors and its resources shall be used to support companies (including cooperatives and listed companies) that have a registered office in Italy, do not operate in the banking, financial or insurance sectors and have an annual turnover above Euro 50 million.

Investments by the CDP Fund can be in the form of loans and guarantees, subscription of financial instruments and acquisition of equity instruments on the primary and secondary markets.

3.3.3.C. Central Guarantee Fund Guarantees

The Central Guarantee Fund (*Fondo Centrale di Garanzia*) will provide guarantees for financial liabilities of SMEs and enterprises with fewer than 500 employees until December 31, 2020. Key features of the Central Guarantee Fund guarantees include the following:

- The maximum guaranteed amount for each SME is equal to Euro 5 million.
- With a few exceptions discussed below, the maximum coverage is equal to 90% of the principal amount in the case of direct guarantees and 100% in the case of indirect guarantees.
- New credit facilities granted to SMEs or natural persons whose businesses or activities have deteriorated as a result of the Covid-19 outbreak may benefit from the Central Guarantee Fund guarantees with a coverage ratio of up to 100% either as a direct guarantee or reinsurance provided that the term of the credit facilities is no longer than 10 years, the repayment does not start before 2 years from the date of drawdown, and the amount of the credit facilities does not exceed the greater of 25% of the revenues of the borrower and Euro 30,000.
- The Central Guarantee Fund can also provide guarantees for up to 90% of the credit facilities granted to companies with revenue not exceeding Euro 3,200,000 that have been negatively impacted by the

Covid-19 crisis, where the amount of the credit facilities does not exceed the greater of 25% of the revenues of the borrower and Euro 800,000.

- The Central Guarantee Fund guarantees can be provided for financings made available in the context of a debt-renegotiations with SMEs, provided that an additional credit facility for an amount at least equal to 10% of the residual indebtedness being re-negotiated is made available by the guaranteed institution to the SME (or 25% in case of financings approved by the guaranteed institution after June 7, 2020).
- No fees or commissions apply.
- Any pre-existing guarantee issued by the Central Guarantee Fund will be extended if the guaranteed indebtedness is subject to a suspension of payment or an extension of the termination date as a result of the Covid-19 crisis.
- The Central Guarantee Fund guarantee can be requested for existing financings entered into not earlier than 3 months prior to the request and, in any case, not earlier than January 31, 2020.

3.3.3.D. State Guarantees of CDP Loans

Companies that do not qualify for a Central Guarantee Fund guarantee as discussed above, operate in specific sectors as identified by a ministerial decree and have suffered a significant revenue reduction due to the Covid-19 crisis can apply for a state guarantee in respect of financings made available by CDP. A CDP financing guarantee can cover up to 80% of the underlying liability and is structured as an irrevocable and unconditional first-demand guarantee.

A state counter-guarantee can be issued through a ministerial decree with respect to guarantees issued by CDP by December 31, 2020.

3.3.3.E. Additional Liquidity Measures

SMEs experiencing liquidity constraints due to the Covid-19 crisis can apply for additional financial support measures from banks, financial intermediaries and other lenders, including the following:

- A standstill until September 30, 2020 with respect to any withdrawal of uncommitted credit facilities and facilities for credit advances outstanding as at February - March 2020 as applicable.
- An extension of the termination date of bullet term loan facilities until September 30, 2020.
- A postponement of principal payments to September 30, 2020 and an extension of the duration of the amortizing term loan facilities.
- An extension of certain subsidized loans subject to prior notification to the relevant subsidizing entity.

3.3.3.F. Additional Funding Measures for Startups

In addition to the foregoing, the Italian government has introduced further measures for startups and innovative SMEs in response to the Covid-19 crisis. These include among others:

- A Euro 100 million contribution to the “Smart&Start Italia” program. The eligibility criteria of the program have also been relaxed to enable participation by a wider group of companies.
- Grants up to Euro 10 million to be used for the provisions of services by start-ups accelerators or incubators, universities, innovation hubs or similar programs.

- A Euro 200 million contribution to the Venture Capital Support Fund (*Fondo di sostegno al venture capital*). The additional funding will be utilized to support startups and growth stage companies through equity investments and the subscription of participative financial instruments.
- Up to Euro 200 million of the Guarantee Fund for SMEs are reserved for innovative start-ups to facilitate their access to financing.
- A newly created fund with an initial allocation of Euro 500 million to be managed by Fondazione Enea Tech, the first Italian foundation dedicated to technology transfers.

CHAPTER 4

BEYOND COVID-19: NEW OPPORTUNITIES FOR FINTECH COMPANIES

4.1. Accelerating Trends in Fintech

Faced by an unprecedented crisis induced by the Covid-19 pandemic, many fintech companies have been refocusing on their core product roadmap, customer service and mission. Inspiring examples of fintech innovation have been witnessed across a variety of sectors, with fintech companies strengthening their capabilities and even launching new products and services to support and preserve human and communities' health, business activities and economic productivity.

Looking further out, fintech companies will need to re-examine their core business models and evolve their value propositions to forge a new path forward and stay relevant to their customers. Only fintech companies that build sufficient resilience and agility will be able to drive renewed growth and long-term profitability. Those that went far and beyond to support customers and increased their pace of innovation despite the difficult times are most likely to thrive and seize new opportunities once the Covid-19 crisis has settled.

Beyond the immediate impact of the pandemic, the Covid-19 crisis has pushed larger swathes of the population online and has accelerated secular trends already underway for banking and other financial services. The slowdown induced by the pandemic has also acted as a key altering mechanism for transactional businesses that lack a long-term sustainable revenue model.

With lockdowns imposed across much of the world, people have been adopting new digital services and platforms by necessity and the most effective businesses have been pivoting towards fintech use-cases in highest demand. This shift is expected to endure far beyond the Covid-19 crisis, as users acquire a new pattern of behavior, discover efficiencies and adapt to a new digital life post crisis.

First and foremost, the trend towards digital payments has remarkably accelerated. Large digital payment platforms have flourished and fintech companies powering digital commerce have seen a significant boost[124]. And it's not only about e-commerce. Education, entertainment, health, fitness, medicine and many other industries that have been impacted in various degrees by the Covid-19 crisis will very likely increase their online presence through web and mobile services, more convenient interfaces and faster delivery. These developments can create valuable business and collaboration opportunities for fintech companies. Fintech companies and capabilities are expected to expand into adjacent ecosystems and become more integrated with day-to-day digital life.

Social distancing and lockdown measures have also forced people and businesses to conduct critical financial activities and banking functions online, including opening a bank account, depositing checks, borrowing, paying bills and investing. This has accelerated the adoption of financial technology and the

[124] See, deVere Group, Coronavirus lockdown: Massive surge in the use of fintech apps (deVere Group, March 30, 2020 (noting that in Europe, social distancing measures prompted a 72% increase in the use of fintech apps in a single week at the end of March)); McKinsey & Company, How payments can adjust to the coronavirus pandemic—and help the world adapt cit.; The Wall Street Journal, Digital Payments Soar Amid Coronavirus Restrictions (The Wall Street Journal, March 23, 2020); McKinsey & Company, European consumer finance: Moving to a "next normal" (McKinsey & Company, June 15, 2020 (noting that "e-commerce in Italy has increased by 81 percent compared with the last week of February" and expecting "internet banking penetration to see a steep increase in most European countries.")).

use of online and mobile channels to manage finances and financial transactions. While restrictions are now gradually lifted, banking and financial services are expected to see more long-lasting changes as customers and businesses carry on embracing the digital methods that they have been adopting to a greater extent during the Covid-19 crisis[125]. Fintech companies - including leading challenger banks, online lenders and wealth management platforms – are built for the web and mobile channels and excel in offering presentation, onboarding, underwriting, data visualization, and providing the right context for transactions. As a result, they are best positioned to benefit from the amplified focus on banking and financial digital user experience and are expected to see a steep increase in adoption and customer engagement in the coming months.

Related to these factors, and reinforcing them, is another trend that has already been taking hold – the shift towards a "cashless" economy. The use of cash and checks has been in decline over the past few years as contactless payment cards and smartphone payments have gained in adoption. During the Covid-19 crisis, this movement has accelerated exponentially as cash and physical payment instruments have been recognized as a potential infection source. A number of retails have actively been encouraging payment by card rather than cash. Central banks and financial regulators around the world are also fostering the debate and increasing the pressure to speed up the adoption and roll-out of digital payments and faster payment capabilities.

As a result, the Covid-19 crisis has proved to be a powerful catalyst for the acceleration of existing trends towards more digitalization of payment operations, finance management and banking services. The combination of the described trends not only creates a great opportunity for fintech companies to drive efficient customer acquisition but also an opportunity for them to prove their differentiated value proposition versus more traditional players.

4.2. Funding Conditions

As the Covid-19 induced market downturn stretches into the second half of 2020, investors will likely remain cautious to get straight back in. Investment committees are expected to become more discerning in their focus and about who they can continue funding or should pass as they seek safety with increased flight to quality. Before making major capital available for new investments, investors will first want to deepen their understanding of companies that are best positioned to thrive in the new global economy that is starting to emerge, available consolidation opportunities in the market and how market consumption and engagement will look like post Covid-19 crisis. For companies that successfully

[125] See, KPMG, Covid-19 a catalyst to transform bank payment operations (KPMG Insights, 2020); KPMG, A catalyst for change for bank branches (KPMG Blog, April 22, 2020); Simon Taylor, There has never been a more important time to be truly digital (11:FS, March 25, 2020); KPMG, Can fintech lead innovation post-COVID 19? (KPMG Blog, May 8, 2020); Benjamin Ensor, How The Coronavirus Pandemic Will Affect Banking (11:FS, March 20, 2020); 11:FS, How the COVID-19 pandemic will accelerate digital financial services (11:FS, April 2020); McKinsey & Company, Reshaping retail banking for the next normal (McKinsey & Company, June 11, 2020 (noting that "In Italy, Spain, and the US, 15 to 20 percent of customers surveyed expect to increase their use of digital channels once the crisis has passed; in other markets that percentage ranged from 5 to 13 percent. Notably, preference for handling everyday transactions digitally is as high as about 60 to 85 percent across Western European markets, even for customers 65 years of age or older")); McKinsey & Company, No going back: New imperatives for European banking (McKinsey & Company, May 18, 2020); McKinsey & Company, Stability in the storm: US banks in the pandemic and the next normal (McKinsey & Company, May 13, 2020); Goldman Sachs, COVID-19's Impact on the Future of Fintech (Goldman Sachs Insights, June 3, 2020).

navigate the crisis, large amounts of capital will likely be available and will be invested to scale innovative solutions and enable mergers and acquisitions, market capture and expansion activities[126].

Deal structure and deal terms will likely shift more and more in favor of investors. Valuations will continue to be conservative while down rounds, side rounds and/or convertibles will likely increase. Liquidation preferences are expected to climb up from the traditional 1x during good times to 2-3x amidst a prolonged downturn. Investors will also try to shift away from a "*pari passu*" approach to liquidation preferences and instead negotiating for senior liquidation preferences. Anti-dilution clauses may also become more common, with the introduction of more stringent terms that recent term sheets didn't have[127].

4.3. M&As Opportunities

As valuations are materially re-setting and available funding is contracting in the near- to medium-term, the fintech sector becomes a fertile territory for acquisitions. In the past 6 months, the volume and frequency of fintech M&A deals have been remarkable, with fintech companies buying banks[128], large fintech companies buying emerging players[129], established financial institutions acquiring high growth fintech companies[130] and established firms combining for scale[131].

Fintech M&A activities are now expected to accelerate even further as the slowdown continues. Within the fintech space, the consumer banking, online lending and digital wealth management sectors are those most likely to see a rapid increase in M&A deals. Deal terms and pricing will progressively swing in favor of acquirers[132].

A number of players have begun to consolidate their position in the market and take advantage of the current funding and economic conditions through acquisitions. More strategic buyers may emerge, including financial institutions, large tech firms and foreign buyers. These players will be increasingly looking to use their stronger balance sheets, large cash reserves and wider distribution to buy fintech companies in an effort to increase market share and expand their product offerings. At the same time, late-stage fintech companies that have recently completed funding rounds are also expected to drive

[126] See, Oliver Werneyer, Beyond Covid-19: The future of fintech and payment technology (Data Centre Dynamics, May 22, 2020).

[127] See, Goodwin Procter, Five Emerging Trends in Growth Equity Deals, cit.

[128] See section 1.4 and accompanying footnote no. 5 discussing the acquisition of Radius Bank by SoFi.

[129] See section 1.4 and accompanying footnote no. 4 discussing the acquisition of Galileo by SoFi. On the acquisition of Verse by Square, see Romain Dillet, Square acquires European peer-to-peer payment app Verse (TechCrunch, June 16, 2020); Ruby Hinchliffe, Square buys up Spanish P2P payment app Verse (Fintech Future, June 17, 2020). On the acquisition of RateSetter by Metro Bank, see Kathryn Gaw, RateSetter acquired by Metro Bank (Peer2Peer Finance News, August 3, 2020); Steve O'Hear, Metro Bank is acquiring peer-to-peer lender RateSetter for up to £12M (TechCrunch, August 3, 2020). On the acquisition of challenge bank Stack by Credit Sesame, see Finextra, Credit Sesame buys Canadian challenger bank Stack (Finextra, June 16, 2020); Michael Tattersall, Credit Sesame has acquired challenger bank Stack as it moves further into banking (Business Insider, June 18, 2020). On the acquisition of OnDeck by Enova International, see Alex Hamilton, Enova International acquires struggling lender OnDeck in $90m deal (Fintech Futures, July 31, 2020); Donna Fuscaldo, Struggling Online Lender OnDeck Sold To Enova International (Forbes, July 29, 2020).

[130] See section 1.4 and accompanying footnotes no. 3 discussing the acquisitions of Plaid by Visa and Credit Karma by Intuit. On the acquisition of Finicity by Mastercard, see Finextra, Mastercard to buy Finicity for open banking push (Finextra, June 23, 3030); Jennifer Surane, Mastercard Takes Step Away From Cards With $825 Million Deal (Bloomberg, June 23, 2020). On the acquisition of French neobank Shine by Société Générale, see Ruby Hinchliffe, Société Générale to acquire French neobank Shine (Fintech Futures, July 1, 2020); Aisling Finn, Shine joins a growing list of fintechs acquired by the French investment bank since 2015 (AltFi, July 1, 2020).

[131] See, section 1.4 and accompanying footnote no. 6 discussing the acquisition of E-Trade by Morgan Stanley. On the acquisition of TD Ameritrade by Charles Schwab, see C. Nivedita, Charles Schwab gets U.S. DOJ approval for TD Ameritrade buy (Reuters, June 4, 2020); David McLaughlin and Annie Massa, Schwab's Deal for TD Ameritrade Wins Antitrust Approval (Bloomberg, June 4, 2020).

[132] See, Goodwin Procter, Covid-19 and the Impact on M&A (Goodwin Procter Publications, March 5, 2020).

consolidation and be on the hunt for early or growth stage fintech targets that offer unique technology, great products, and/or access to new customer segments or markets[133].

Exits via M&A are also expected to become a predominant route for liquidity in the coming months. With the IPO market slowing down for the nearer future, company boards and investors who are actively looking to exit may be more open-minded in having strategic dialogues with prospective buyers that were not necessarily on the agenda until recently.

4.4. Expanding Partnership Strategies

The contracting funding environment and reduced revenue streams will likely force a number of fintech companies to seek growth and cost synergies through collaborations and partnerships with other fintech companies, large tech companies, as well as non-financial strategic players. For example, in March 2020, TransferWise partnered up with Alipay for international transfers[134], and in July 2020 Affirm announced a partnership with Shopify to exclusively power shop pay installments in the United States[135]. Partnerships of this kind will become a critical lifeline in the absence of fresh capital for scale and organic growth.

Partnerships between fintech companies and established financial institutions which have increased in recent years[136] are also expected to grow in volume and relevance in a post Covid-19 financial ecosystem. The growth in open banking and banking-as-a-service initiatives will play an important role in accelerating these collaborations on a global scale[137]. Incumbents have been pushed to engage with consumers via online channels and will increasingly be looking to leverage fintech partnerships to drive efficiencies, provide enhanced services to their customers and gain new market share[138].

As they shift from response to recover, large financial institutions are also expected to focus more and more on technology and fintech opportunities to increase the efficiency of their own operations, infrastructures and systems. This is expected to foster even more collaborations between fintech companies and incumbents. It will also likely result in large technology companies becoming key third-party vendors to established financial companies and being more and more intertwined in the financial infrastructures[139].

[133] See, e.g., Nicholas Megaw, Revolut on the hunt for acquisitions (Financial Times, May 5, 2020); Will Hernandez, Now $500 million richer, Chime eyes acquisitions (American Banker, December 6, 2019); Simon Taylor, Is the COVID-19 crisis creating fintech M&A opportunities?, cit.

[134] See, Steve O'Hear, TransferWise partners with Alipay for international money transfers (TechCrunch, March 17, 2020); Finextra, TransferWise targets China through Alipay partnership (Finextra, March 17, 2020).

[135] See, Finextra, Affirm scores major buy now, pay later deal with Shopify (Finextra, July 23, 2020).

[136] See, Rex Salisbury and Anish Acharya, The Partner Bank Boom (a16z report, June 11, 2020); Michael Deleon, The Tearsheet 2020 Guide to Bank/Fintech Partnerships (TearSheet, April 13, 2020); FintechTris, The Rise of FinTech Partner Banks (FintechTris, June 25, 2020); Finextra, Covid-19 aftermath will bring banks and fintechs together (Finextra, April 21, 2020); Paul Schaus, Banks and fintechs need each other more than ever (American Banker, July 16, 2020).

[137] See, e.g., Sebastian Garcia, The Next Generation of Fintech Infrastructure: How API Platforms are Disrupting Banking & Payments (Medium, July 15, 2020); Nikil Konduru, Reining in the BaaS Euphoria (Medium, August 7, 2020).

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