

Lithuania – Fintech Hub: Cost and Benefit Analysis

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Lithuania has been increasingly bold about the country's aspiration to become a global hub for Fintech, i.e. financial technology. The success of the initiative, which has recently become an interinstitutional government strategy for 2019, has so far been nothing less but impressive - it was estimated that in 2018 the Fintech sector in Lithuania grew by 45% to a total of 170 Fintech companies and more than 2,600 employees in the country.



[Fintech Landscape in Lithuania by Invest Lithuania](#)

However, the success has been also met with the growing public concern that such a rapid increase in financial companies, many coming from abroad, may pose numerous related risks for a relatively small country. The public, members of the local Parliament and some of state institutions have expressed their cautious sentiments, often ignoring the benefits that such companies bring to Lithuania.

The best way to evaluate such a state-level project is to carry out a simple cost-benefit analysis. The analysis below is based on a specific example - one locally licensed Fintech company (an electronic money institution that the author is currently leading) - and other publicly available data.

Benefits from Fintech in Lithuania

1) Increase in competition among local financial market participants. A good example of such competition could be cheaper, more convenient and easily accessible daily banking services offered by companies like *Revolut*, *N26* and *Monzo*, which have been increasingly used by Lithuanian residents and companies. However, the presence of these new market participants was made possible by the single market and unified licensing in the European Union and has not required any additional efforts from the government.



Map of Fintech Companies in Lithuania by Rise

Valuation: 0 EUR since the basic segments of the financial market are already competitive without additional efforts from the government.

2) Foreign Investment. The shareholders of the licensed electronic money institution used as an example have invested nearly 1,000,000 EUR in one and a half years since the start of its operations (it is not worth starting such a company without a hefty investment). Half of these funds are held in a commercial bank as a minimum capital required by the central bank. The bank pays deposit insurance ranging from 0.1 to 0.5 percent from the amount to the government every year. The other half was invested into local IT systems and team. The company paid 21 percent VAT (which cannot be recovered since the financial services are exempt from VAT) and payroll related taxes.

Valuation: Investment of around **500,000 EUR** every year on average (may not have happened without the certain steps from the government), of which 80,000 EUR were paid directly to the government in the form of various taxes.

3) Human capital development. Currently, the example electronic money institution has a local team of around 10 people. Every year the number of employees increases together with their level of their expertise, created added value and compensation. Part of these employees do not have any previous work experience in banking or financial sectors, mainly because there is a lack of supply in the local job market. Soon this may become the major problem for all Fintech businesses in Lithuania.

Valuation: 15,000 EUR assuming an increase of 1,500 EUR in a yearly gross salary per employee on average (between 2% and 10% of annual growth in salary). There are more than 2,600 employees in the Fintech sector in Lithuania.

4) Created innovations. Not all Fintech companies are creating groundbreaking innovations, however, they are more likely to offer more innovative or efficient business models (also more risky) than traditional banks. The alternative could be to evaluate a "success premium", i.e. the likelihood that some of the local Fintechs will succeed in a long term and Lithuania will eventually have its first "unicorn".

Valuation: According to some estimates, only around 5 percent of technology start-ups survive more than 10 years. In order for an example company to survive and grow successfully in the long term, it is needed to reach around 1,000,000 EUR net annual income within 10 years. 5 percent times 1,000,000 EUR equals **50,000 EUR**.

Valuation of all benefits: increase in competition **0 EUR** + Foreign Investment **500,000 EUR** + human capital development **15,000 EUR** + created innovations **50,000 EUR** = **565,000 EUR**.

Additional Costs from Fintech in Lithuania

1) Additional human and other resources incurred by government institutions working with the promoting, licensing, supervision, etc. of Fintech companies in Lithuania. In this case, the "biggest burden" falls on 4 local institutions - the *Bank of Lithuania* (licensing and supervision), *Financial Crimes investigation Service* (supervision), the *Ministry of Finance* (strategy and promotion) and *Invest Lithuania* (promotion). For the time being, the public sector seems to be coping with the new challenge rather well: according to the local *State Social Insurance Fund*, the number of employees in these 4 institutions has increased insignificantly or in some cases even decreased in 2018.

Valuation: Around 20 new jobs could possibly be created in public sector dedicated purely to Fintech sector. Average gross salary of a public servant in Lithuania in 2018 stood at almost 1,000 EUR. The total cost of all additional jobs would be around 320,000 EUR per year (these costs must not be confused with benefits, i.e. new jobs created). Adding extra trips and other related expenses – the amount could double to a total of 640,000 EUR or around **6,400 EUR per 1 Fintech** company assuming that only a part of 170 companies are currently conducting actual business activities.

2) Additional infrastructure. In this case, it is the payments system *CENTROlink*, created, maintained and developed by the Bank of Lithuania. It makes Lithuania unique in the European Union for the fact that not only commercial banks, but also smaller financial market participants (licensed payment and electronic money institutions, credit unions) can gain access to payments in euros in the Single Euro Payment Area (SEPA) via the central bank. This is one of the main reasons why Lithuania has been so attractive to foreign Fintech companies.



[CENTROlink by the Bank of Lithuania](#)

Valuation: *CENTROlink* requires constant support and development, which can cost up to 1,000,000 EUR per year, while the revenue collected from participants is far from covering the costs at this moment. Around 30 to 40 licensed companies from Lithuania and other EU countries are connected to the system, making the costs stand at around **33,000 EUR for each**.

3) Alternative costs. Local politicians, civil servants, business employees (for example, the ones of commercial banks receiving applications from Fintechs to open a bank account nearly every day), the author of this article, and, of course, you, the reader, devoting your valuable time to understand what Fintech really is about.

Valuation: 0 EUR since the time is deemed to be invaluable.

4) Related risks. Such a rapid growth in the number of financial companies in Lithuania, without a doubt, raises numerous related risks. Out of many, the “most costly” one could be a long term negative impact to the country's reputation, which in the end of the day is just a combination of other related risks - political, money laundering, terrorist financing, fraud, theft, bankruptcy and others.

Of course, the *Bank of Lithuania*, the *Ministry of Finance*, the *Financial Crimes investigation Service* and other government institutions are constantly monitoring and assessing these risks. However, it is important to keep in mind that at the moment the most of mentioned 170 Fintech companies in Lithuania are in the early - licensing, product development, testing or first-time customer acquisition - stages of their business activities, carrying very limited risks. On the other hand, more mature companies also tend to reduce their risks themselves.

Valuation: It is not possible to predict, nor precisely evaluate all the risks associated with the growth of Fintech sector, however, after knowing the other benefits and costs **we can calculate the country's tolerable risk level or “risk premium”**, i.e. the size of the risk that Lithuania can assume so the benefits still outweigh the costs.

Valuation of all costs: additional human and other resources **6,400 EUR** + additional infrastructure **33,000 EUR** + alternative costs **0 EUR** + **related risks = 40,000 EUR + related risks**

Total Benefits vs. Costs of Fintech

One Fintech company in Lithuania brings around 565,000 EUR additional benefits and 40,000 EUR costs as well as risks related to their activities. By simply multiplying these numbers by 100 (still assuming that only a part of 170 companies are currently conducting actual business activities) we can estimate that the **total net benefits to Lithuania from the growing Fintech sector could reach up to 52,500,000 EUR per year.**

Naturally, **the sum of all estimated risks** (probability of occurrence multiplied by a possible loss for each risk) related to the development of Fintech and additional costs dedicated to the management of those risks **should not exceed ~50,000,000 EUR per year.**

Evaluating the necessity for Fintech strategy for a longer period, e.g. 10 years (achieving the desired 15 percent annual sector's growth, 5 percent annual growth in costs, and applying a "conservative" 10 percent discount or money depreciation rate), we can calculate that the **total net benefit of a long-term Fintech strategy for Lithuania could reach up to 660,000,000 EUR** if successfully implemented and managed.

There is no doubt that some of the above mentioned risks would occur over such a long period bringing more or less losses to the country, however, these estimates could act as a starting point for assessing the level of tolerable risk for the country like Lithuania and continuing discussions about its ambition to become a global Fintech hub.

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Full disclosure: Titas Budrys is a director of one of the electronic money institutions used as an example in the text. He is interested in the long-term success of the company and Fintech sector itself as well as the positive attitude from the government institutions and the public towards it. This article should not be considered as any form of advertising and the names of the companies used as examples in the text are not mentioned on purpose. All the statements in this article are nothing more, but a personal opinion of the author, while the calculations conducted are deemed to be inaccurate.



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