



July 2023

# The Path to FinTech Profitability Must Be Fraud-Proof

FinTech Tracker® Series

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MARCH 2023  
FinTech Tracker® Series

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PYMNTS®



### Acknowledgment

The FinTech Tracker® Series is produced in collaboration with Sezzle, and PYMNTS is grateful for the company's support and insight. [PYMNTS](#) retains full editorial control over the following findings, methodology and data analysis.

## Need to Know

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# Fraud Is Taxing the FinTech Space

Fraud is an ongoing scourge, but businesses are becoming savvier in dealing with it. For every new fraud scheme that pops up, dozens of FinTechs are responding to quash it. Fraud detection- and prevention-focused FinTechs are deploying artificial intelligence (AI) or analytics, promising cures for identity fraud, fraudulent credit or debit card transactions, cryptocurrency schemes, digital bank fund transfer scams or fraudulent insurance claims.

However, despite their expertise in cutting-edge technology, FinTechs are far from invulnerable to attacks themselves. A recent PYMNTS report found that FinTechs on average lose [\\$51 million every year to fraud](#) — an approximate median of \$400,000 — or the equivalent of 1.7% of their annual revenue. It is no surprise that nearly half of FinTech firms list the cost of fraud as the top challenge they face in doing business.

Fraud is a scourge to financial services, including the [FinTech sector](#).



**\$51M**

**Average revenue lost to fraud annually by FinTechs overall**



**47%**

**Share of FinTechs that see the cost of fraud as the top challenge they face**

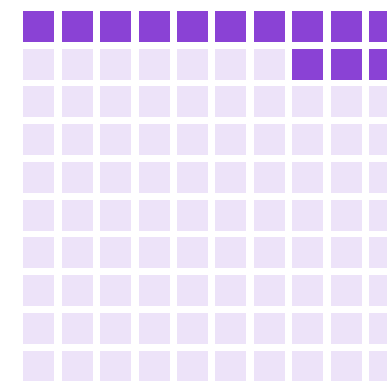
## Need to Know

# Fraud protection fuels profits.

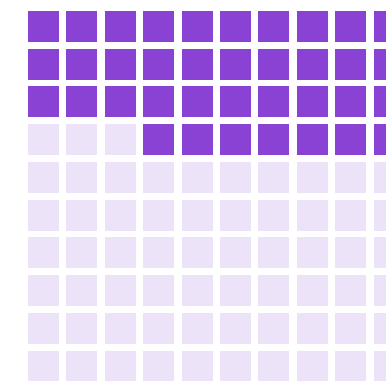
Fraud schemes are mutating alongside — and enabled by — technology. Stolen information is becoming more accessible and easily bought, with highly sophisticated criminal groups offering “[fraud as a service](#)” on the dark web. Against this backdrop, FinTech fraud is on the rise, having grown 13% in the past year. Moreover, FinTech companies were the most likely financial entities to report [higher fraud losses](#) last year.

Dollar amounts lost are far from the only cost of fraud, however. Whether through reputational risk, regulatory penalties, legal costs or the loss of business revenues, fraud schemes pose a myriad threat to FinTechs’ bottom lines. As a result, FinTechs cannot afford to overlook fraud prevention as an integral part of their long-term financial profitability strategies.

Fraud’s sophistication is growing in parallel with technology, posing increasing risks to FinTechs.



**13%**  
**Increase in FinTech  
 fraud in the past year**



**37%**  
**Share of FinTechs losing  
 between \$1 million and  
\$10 million to fraud in  
 the past year**

## Need to Know

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# AI-powered fraud solutions are poised to play a crucial role in the FinTech industry.

With a large majority of FinTech executives anticipating an increase in all fraud this year, more than two-thirds plan to expand their budgets for [fraud prevention management](#) initiatives — especially automated technology that can combat deepfakes.

[AI and machine learning \(ML\)](#) are valuable tools that FinTechs and other financial service providers are utilizing to mitigate fraud risk. These solutions quickly process large quantities of data and compare them, identifying patterns to spot aberrations in identity verification processes that would elude human teams and legacy tools. Crucially, AI and ML solutions can also learn new patterns and respond dynamically over time to adapt to fraudsters' ever-evolving techniques.

“We are seeing an increase in very convincing AI-generated deepfakes. These synthetic media would fool almost any human, and our research shows that two in three FinTechs [are] planning to add new automated identity verification technology that can detect true human liveness.”

**RUSS COHN**  
General manager



Source: Financial IT. Nine out of 10 FinTechs Will Hire More Experts in 2023. 2023. <https://financialit.net/news/security/nine-out-10-fintechs-will-hire-more-fraud-experts-2023>. Accessed June 2023.

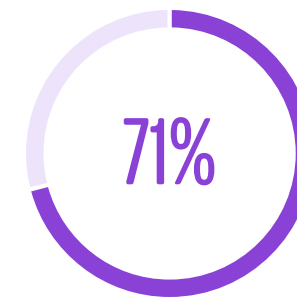
## News and Trends

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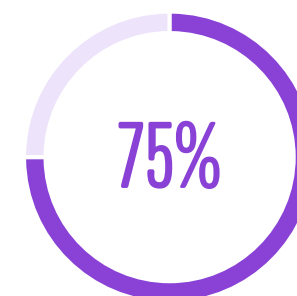
# Phishing, BEC Schemes Hammer Financial Services

A new report on [major fraud trends](#) in the financial services space shows some interesting twists in the past year. Although fraud overall dropped to its lowest rate since 2014, affecting a still-significant 65% of companies, 36% of all financial institutions (FIs) experienced card fraud in 2022, up 26% over the previous year. Drilling down, 75% of all fraud losses to United States lenders were the result of phishing scams, with other financial services experiencing that fraud technique at 66%. Moreover, 71% of FIs reported a security breach due to business email compromise (BEC), in which fraudsters pose as trusted company executives or partners.

Large enterprises were a favorite target, with the number of monthly fraud attacks on banks earning more than \$10 million in annual revenues increasing steadily year over year. Similarly, 84% of companies generating \$1 billion or more saw fraud attacks on more than 100 accounts in the past year.



**Share of FIs that reported a BEC security breach in 2022**



**Share of U.S. lenders' fraud losses that resulted from phishing scams**

## News and Trends

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# Novel FinTech ‘platform fraud’ comprises 57% of all fraud incidents in India

“[Platform fraud](#),” a newly minted economic crime that involves fraudulent activities on social media, eCommerce, enterprise and FinTech platforms, is making headlines in India. A recent PwC report found that this fraud type comprises more than half — 57% — of all fraud incidents in the country. More than one-quarter of Indian companies lost over \$1 million due to platform fraud, and 44% of bad actors committed the fraud for financial gain. Four in 10 incidents were cases of internal fraud, while another 26% of such incidents involved collaboration between internal and external perpetrators. Financial transaction fraud accounted for 89% of all platform fraud incidents, ranging from unauthorized purchases to identity theft and triangulation fraud.



## 26%

Share of companies in India that lost more than \$1M to platform fraud in 2022



## 4 in 10

Share of platform fraud incidents in India conducted by internal actors

## PYMNTS Intelligence

# Why FinTechs Are Leaning into AI to Fight Changing Fraud Threats

As financial fraud evolves in the digital age, the picture that emerges is a complex one. On one hand, fraud in 2022 was at its [lowest rate](#) since 2014, affecting 65% of organizations. Signs also indicated that companies were duly implementing measures to combat it, with 45% of all U.S. financial service firms having fully integrated digital fraud prevention systems, up from 28% in 2020.

Nevertheless, fraud continues to spiral upward in new ways. [FinTech fraud](#) was up 13% in 2022. Threats such as [identity fraud](#) are taking a severe toll on the sector, with nearly half of all FinTechs impacted by the use of fake documents. These findings suggest that while the financial industry is responding to the challenge, vigilance and adaptability will be key to succeeding as fraudsters continue to seek — and find — loopholes in defenses at every turn.

“As fraudsters increasingly target mobile payment apps, payment companies will face a greater need to invest in robust fraud detection and prevention services to protect their customers and their own financial interests. This will likely result in increased spending on security measures, technology upgrades and partnerships with specialized fraud prevention providers. Payment companies will need to prioritize security and adapt to the evolving landscape of fraud to maintain customer trust and confidence in their services. We’ve already seen this through our growing and ongoing commitment to building our fraud team and risk management services.”

CHARLIE YOUAKIM  
CEO



## PYMNTS Intelligence

# The double-edged sword of technology

Although technology can offer powerful solutions, it is also an undeniable culprit in the growing battle against fraud. Scams using stolen credentials were once easier to detect, but [synthetic identities](#) developed with these credentials have changed the game in fraudsters' favor, according to a recent report. Fake identities created with real credentials can challenge or fool many fraud-fighting systems' defenses.

In addition to the increase in FinTech fraud, digital goods and services fraud was up by 27% and cryptocurrency exchange fraud by 45%. Buy now, pay later ([BNPL](#)) fraud topped the list with an alarming 211% jump. Moreover, as technology makes it easier to commit fraud, elite criminal organizations are cropping up to offer “as-a-service” fraud products on the dark web.

Despite a drop in the overall financial fraud rate, fraud in some sectors continues to escalate.



**45%**  
Increase in  
cryptocurrency fraud  
in 2022



**211%**  
Increase in  
BNPL fraud  
in 2022

Fraudsters — and those in training — can now purchase and leverage automated scripts to run their scams, allowing perpetrators to overwhelm fraud management teams that lack the proper tools to combat these attacks. Researchers also noted that programs such as [ChatGPT](#) will make fraud more difficult to detect by allowing bad actors to eliminate the grammatical and similar mistakes that are the historic hallmarks of fake sites and phishing emails.

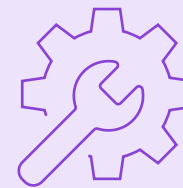
## PYMNTS Intelligence

# Changing tactics call for adaptable solutions

AI and ML have a vital role to play in promoting profitability through fraud protection for the FinTech industry. PYMNTS' research has found that companies relying on legacy reactive and manual digital identity verification solutions lose above-average shares of annual sales to fraud, at 4.5%. However, firms using proactive and automated solutions, such as those powered by AI and ML, reduce their share of lost sales to 2.3%.

In addition, AI solutions using behavioral analytics are both highly accurate and undetectable to users, making for smooth experiences to reduce onboarding time and friction as well as enhance customer loyalty. These factors mean that AI-powered fraud solutions could be a revenue generator for FinTechs — both as end users and as developers offering such solutions to their customers.

Proactive, automated fraud solutions have the potential to halve revenue losses compared to reactive, manual ones.



# 4.5%

Share of annual sales lost to fraud by businesses using reactive and manual digital identity solutions



# 2.3%

Share of annual sales lost to fraud by businesses using proactive, automated solutions

## Chart of the Month

# Fraud Hits Small FinTechs the Hardest

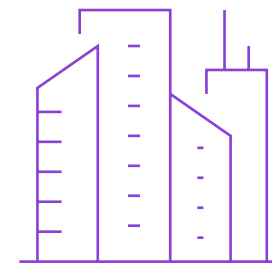
In light of growing risks, fraud is an important concern for all FinTechs, but its impact varies inversely with company size, according to a recent PYMNTS report. [Small firms lose 57% more revenue](#) to fraud than large firms, with the average small FinTech losing 2.2% of its annual revenue to fraud losses, or an average of \$200,000. Mid-sized firms also lose more to fraud than larger firms.

### Average share of revenue lost due to fraud in the past year<sup>1</sup>



**1.7%**

OVERALL



**1.4%**

LARGE  
FIRMS



**1.6%**

MID-SIZED  
FIRMS



**2.2%**

SMALL  
FIRMS

<sup>1</sup>Our study defines small firms as those generating between \$5 million and \$10 million in annual revenue, mid-sized firms as those generating between \$10 million and \$100 million in annual revenue and large firms as those generating more than \$100 million in annual revenue.

Source: PYMNTS

The FinTech Fraud Ripple Effect, November 2022

N = 200 U.S. FinTech business leaders: Complete responses, fielded Aug. 3, 2022 – Aug. 25, 2022

# KEY FINDINGS

## 01

### FINTECH FRAUD

Despite their expertise in cutting-edge technology, FinTechs are far from invulnerable to fraud attacks.



# \$51M

Average revenues lost to fraud annually by FinTechs overall

## 02

### PROFITS PUMMELED

Whether through reputational risk, regulatory penalties, legal costs or the loss of business revenues, fraud schemes pose a myriad threat to FinTechs' bottom lines.



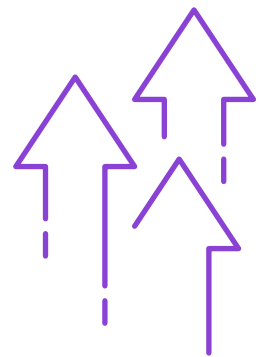
# 1.7%

Average share of annual revenues lost to fraud by FinTechs in the past year

## 03

## RISING RISKS

Despite a drop in the overall financial fraud rate, fraud in some sectors continues to escalate, including FinTech, cryptocurrency and BNPL fraud.



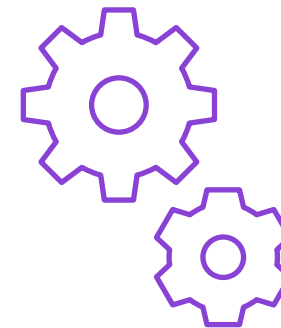
# 211%

Increase in BNPL fraud in 2022

## 04

## SWIFT SOLUTIONS

A rise in synthetic identities has AI-powered fraud solutions poised to play a crucial role in the FinTech industry.



# 2 IN 3

Share of FinTechs planning to add automated identity verification technology to detect human liveness

## What's Next

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# Fraud Detection and Prevention Market Will Eclipse \$90B by 2030

The rise in smartphone usage is fueling explosive growth in the [fraud detection and prevention market](#), which is on track to reach \$90.07 billion by 2030, marking a compound annual growth rate of nearly 18%. Mobile payment apps have become major targets of fraudsters, forcing companies to adopt fraud detection and prevention services. The fraud analytics and identity theft segments are predicted to witness the highest growth over the forecast period. In addition, large businesses are projected to hold more than 70% of the market, as fraud is prevalent in such enterprises, posing a significant threat to profits.



# About

**PYMNTS®** [PYMNTS](#) is where the best minds and the best content meet on the web to learn about “What’s Next” in payments and commerce. Our interactive platform is reinventing the way in which companies in payments share relevant information about the initiatives that shape the future of this dynamic sector and make news. Our data and analytics team includes economists, data scientists and industry analysts who work with companies to measure and quantify the innovation that is at the cutting edge of this new world.



[Sezzle](#) is a payments company on a mission to financially empower the next generation. Sezzle’s payment platform increases purchasing power for millions of consumers by offering interest-free installment plans at online stores and in-store locations. When consumers apply, approval is instant, and their credit scores are not impacted unless the consumer elects to opt in to Sezzle’s credit-building feature, Sezzle Up. This increase in purchasing power for consumers leads to increased sales and basket sizes for the more than 41,000 active merchants that offer Sezzle.

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