Open Forum 2015

Open Forum regional event, Cambridge, 6 November 2015

Background

Charlotte Hogg (Chief Operating Officer, Bank of England) hosted a working lunch in Cambridge on 6 November 2015, where attendees discussed the themes relevant to Breakout Session 2, Panel 2: "How financial innovation and technology can support the economy".

The following summarises the key points raised by attendees.

Main messages

1. UK and financial technology (FinTech)

After the US, the UK is experiencing the most investment in FinTech globally and investment was judged to be "as healthy as it has ever been".

The UK is the leading country on FinTech in the EU. The current engagement on innovation from UK regulators, particularly the FCA's approach on crowdfunding and the establishment of its innovation hub, is welcome and could helpfully be replicated across the EU.

2. Developments in innovation and implications for the financial markets

Innovation was most likely to occur in the following areas:

- "Robo-advice" (automated advice with no human interaction) for people with small sums of money that they want to invest in a simple way.
- Incumbent firms embracing new technologies, such as the blockchain, to make their back offices more efficient.
- Start-ups that offer transparency for consumers as to where their money is invested. (More and more consumers want to know that their money is invested in businesses doing "social good").
- Growth in alternative mortgage providers. (These are growing in size in the US and it is likely that crowd funding for property ownership and investment will grow in the UK).
- Financial technology will impact insurance firms' business models. For example, premiums for motor insurance policies could be driven to zero in a world with driverless cars.

These developments imply that financial markets may become disaggregated and disintermediated.

In addition, some of these activities could enhance interconnectedness which may, in some circumstances if unmitigated, create systemic risk (for example if "robo advisors" use similar models for investing client money, there could be a build-up in concentration of exposures to one sector or product).

3. Funding for innovation

Debt and equity markets are broadly working well for UK FinTech firms. On the whole, the preference is for debt funding if the company is able to service its debt, despite the covenants often imposed; otherwise equity funding is attractive, despite dilution of company holdings.

For smaller projects there is sufficient UK funding from "business angels". However, there is a gap at the £1-£5m range which is too large for business angels but too small for venture capitalists, although syndicated angel investments are taking place. For larger investments of £50m and above, entrepreneurs are going to the US to attract larger venture capitalists and corporate investors.

4. Trust and security

If technology can make access to financial services more convenient and there is transparency, then trust and security concerns would not prevent the take up of new technology by consumers. However, it could lead to a slower adoption rate than previously predicted.

Consumers are more willing to trust non-bank services, even if they are automated, because some have lost faith in the current banking system.

There is likely to be more innovation in identify verification. Identity verification is likely to expand, based on biometrics and on patterns and anomalies being identified. For example, identity will link people to both their bank account and their devices (laptops, mobile phones etc).

5. Relationship between incumbents and start-up firms

It can be difficult for start-ups in FinTech to get services from incumbent banks including bank accounts, even when firms are not looking for any credit, and credit extension. A change in culture within incumbents to assess credit risks from entrepreneurs differently to traditional corporates would be necessary to change this.

Start-up firms are finding it difficult to sell into established financial institutions and, to some degree, government. Financial services firms have multiple points of entry, long established technology teams focused on existing infrastructure and heavy procurement processes.

6. Government/ legal structures

The UK's attractiveness as a location for FinTech firms is affected by its ability to attract skilled workers from overseas, and to sell into overseas markets from a UK base.