

The Future of Retail Financial Services: What policy mix for a balanced digital transformation?

Proposal for a CEPS-ECRI Task Force

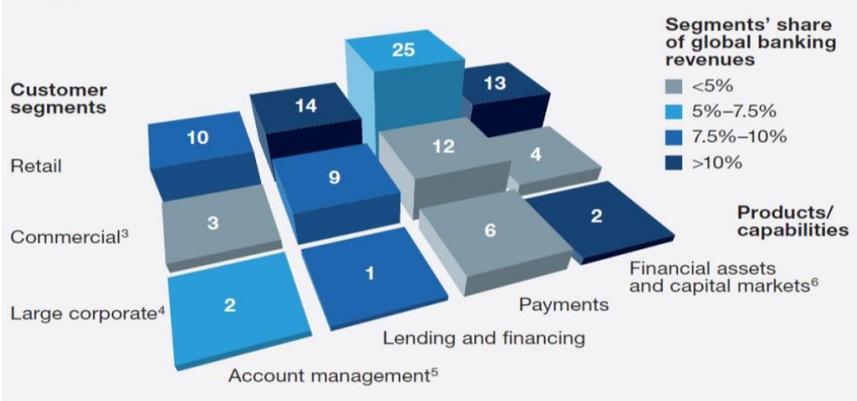
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1. OVERVIEW

In recent years, digitalisation of the economy has accelerated at a steady pace, and retail financial services for households are no exception to this phenomenon.¹ Digital transformation in retail financial services results from the combination of a completely new approach towards data with a new model of interaction between providers and consumers. First, the tremendous growth in available digital data (both financial and personal) and the increasing sophistication in the techniques to exploit this data (big data analytics) are likely to disrupt markedly the traditional models used to collect and exploit data in all phases of the product: advertising, advise, scoring, pricing, prevention, recovery, claims, retention, etc. Secondly, digital platforms that are increasingly user-friendly, personalised and interactive are likely to transform the traditional model of face-to-face interaction with service providers for authentication, advice, assistance, etc. As revealed by several studies (notably by McKinsey in 2015), these disruptions, that are led by FinTech companies and that are increasingly integrated by mainstream banks, affect in particular household lending and payments (see below). Such massive transformation brings numerous opportunities for the financial sector, but also raises a multiplicity of complex regulatory questions.

Financial-technology companies are everywhere, especially in payments.

Customer segments and products of leading financial-technology companies,¹
2015, % of total²



Source: McKinsey & Company (2015).

¹ This Task Force defines "retail financial services" as all household financial services, except those involving an investment component. As such, they encompass products as diverse as loans, accounts, payments, car insurance, property insurance, etc.

In the context of the green paper of the European Commission on retail financial services, CEPS-ECRI directed the study for the European Commission, DG FISMA, on “digitalisation, retail financial services and single market”, with two organisations specialised in the analysis of financial innovations: University College Cork and the Luxembourg Institute of Science and Technology (LIST). Specific interviews and focus groups were conducted with market players in order to better appreciate the potential technological developments in the coming years and their possible impact on the single market for retail financial services. As a follow-up to this study, CEPS-ECRI proposes to organise a Task Force aimed at discussing the policy framework to shape this digital transformation with industry experts, regulators and academics, to culminate in a report with policy recommendations and an action plan that will be addressed to the European regulators (primarily DG FISMA, DG Connect, EBA, ECB and the European Parliament). The objective of the Task Force will be to address the various challenges arising from the digital transformation and possible regulatory responses, notably for peer-to-peer lending platforms, social media data, digital authentication, robo-advisers, blockchain, among others.

2. ORGANISATION

A kick-off meeting of the Task Force will be held 14 September 14th on “The Future of Retail Financial Services: What policy mix for a balanced digital transformation?”. A limited number of individuals will be invited for this meeting, to provide for ample opportunity for exchange with the moderator and the speakers. As described below, the agenda will have three presentations, followed by interactive discussions with the participants. Mr Salles from the European Commission, DG FISMA, will present the latest developments on the work of the European Commission on FinTech. Mr Bouyon and Mr De Groen will present the key findings of the study submitted to the European Commission, DG FISMA, in the context of the green paper. A third speaker will present the point of view of the market on the digital transformation and the possible regulatory needs.

A tentative set of issues to be addressed by the Task Force are listed below. During the kick-off meeting, the Task Force should agree on a priority list of issues to be discussed. CEPS will bring in its own expertise on digital economy, data protection and financial regulation; other external experts will also be invited to kick off the debate. The scope of the products to be covered will be defined during this meeting (as specified above, it can concern all household financial services, except those having an investment component: loans, accounts, payments, car insurance, property insurance, etc).

If successful, this CEPS-ECRI Task Force will meet twice or three times between September and February (in addition to this kick-off meeting). The first meeting will focus on identifying and conceptualising the key characteristics and challenges of the digital transformation of the retail financial sector. During this meeting, the first elements of an action plan for European policies will be discussed. If needed, a second meeting will complete the key findings of the discussion held during the first meeting (the organisation of this meeting will be decided during the previous meeting). Finally, a meeting will be organised to finalise the action plan, based on a broad consensus reached among the Task Force Members.

At the end of the Task Force, ECRI will publish and circulate among EU and member state policy circles an authoritative analysis including policy recommendations together with an ECRI Task Force Report, which will also be officially published in the CEPS Task Force Report publication series and relevant international publication schemes. This report will be based on discussions in the meetings supplemented by research carried out by the rapporteur.

This ECRI Task Force is principally designed for ECRI members but participation will open to non-members as well, at a fee:²

- ECRI Member, Member of both ECRI and CEPS or both ECMI and CEPS: free
- CEPS or ECMI Member: 2,500 euros
- Corporate that is neither ECRI Member nor CEPS Member: 5,000 euros

The study submitted to the European Commission DG FISMA in the context of the green paper will be used as an input to the first meeting on 14 September.

² The fee covers participation in all workshops, documentation, lunches and three copies of the final report; upon request, CEPS will mail additional copies of the final report to persons identified by participants.

3. AGENDA FOR THE FIRST MEETING

11:30	Registration
12:00	Opening remarks by Karel Lannoo , CEO of CEPS
12:05	Opening remarks by the Chairman of the Task Force, Kim Vindberg-Larsen , Senior Consultant, Copenhagen FinTech Innovation and Research
12:15	Latest developments in the work of the European Commission on FinTech Olivier Salles , Head of Retail Financial Services and Payments, European Commission, DG FISMA
12:45	Presentation of the study on “digitalisation and the single market for retail financial services and non-life insurance” (commissioned by the European Commission, DG FISMA) Sylvain Bouyon , Research Fellow, CEPS Willem-Pieter De Groen , Research Fellow, CEPS
13:15	Competition policy and the financial technology revolution in banking Alistair Milne , Professor of Financial Economics, Loughborough School of Business and Economics
13:45	Digital transformation of the retail banking sector: risks and opportunities Olivier Denecker , Director of Knowledge, Global Payment services, McKinsey
14.15	Discussion on the structure of the Task Force (scope, future meetings, etc)
15:00	End

4. LIST OF POSSIBLE ISSUES TO BE ADDRESSED

During the first meeting, the Task Force will discuss which of the below topics will be covered. The final choice of the issues to be covered by the Task Force will depend on the most popular topics and the overall budget allocated to each of them. Due to resource and time constraints, the Task Force will treat up to three or four of the eight below topics. Please note that there may be some overlap between several topics.

- Level playing field between mainstream and alternative providers:** How and to what extent will alternative providers (such as peer-to-peer platforms) affect the offer of products? Will they substitute for mainstream providers or will they be complementary? Do these new entrants contribute to better competition and enhanced consumer welfare? Is a specific European regulatory framework needed to ensure a better level playing field between both types of providers? **(1)**
- Appropriate collection and use of alternative data:** How and to what extent will alternative data (social media data, etc.) shape marketing, scoring, pricing, retention, recovery and prevention for retail financial services? Can social media data help consumers with thin credit files have better access to retail financial services? What are the related risks in terms of data protection, financial inclusion, quality of the scoring and pricing, etc.? **(2)**
- Increasingly sophisticated algorithms that combine both ethics and efficiency:** How to ensure that the increasingly sophisticated algorithms continue to find an appropriate balance between ethics and efficiency? What should be the position of European policymakers to maintain this balance: “pro-active” or “wait and see”? **(3)**
- Financial education promoted by digitalisation:** How and to which extent can the digitalisation be used to contribute to better financial education of consumers? **(4)**
- Risks and opportunities of increasingly digitalised distribution channels:** Will providers be able to completely digitalise the distribution channels of retail financial services? What are the risks and opportunities regarding the *different devices* (screens, tablets and mobiles), the *different phases of the product* (advertising, advice, assistance, scoring, pricing, recovery, prevention, retention, etc.), the *different segments of products* and the *different digital technologies* (digital authentication, video-calls, robo-advisers, etc.)? What is the most appropriate approach at European level? **(5)**
- Best regulatory approach to boost interoperability within and across countries:** What has the eIDAS accomplished so far? Will there be further needs in terms of interoperability (across organisations both within

and across countries: digital authentication, electronic signature, document admissibility, etc.)? How could regulators contribute to further interoperability? What about security concerns? What is the best regulatory strategy to boost the interoperability between the stakeholders involved in retail financial services with more complex processes (such as mortgage products that request extensive documentation and the participation of several external stakeholders such as notaries, land administration, etc.)? **(6)**

Risks and opportunities of blockchain technologies: How might blockchain technology disrupt the market of retail financial services (virtual currencies, “smart contracts”, etc.)? What are the risks in terms of security, capacity, etc.? Should regulators facilitate or not the emergence of blockchain technology? What are the related regulatory needs in terms of standardisation, interoperability, consumer protection, infrastructures, etc.? **(7)**

More and more regulatory initiatives for payments: What is next for this particular sector?: PSD2, SEPA, AML, PAD and MIF, what is the cumulative effect of all recent regulation for payment/account? With the emergence of mobile payments, will service subscription cost models take over? Data protection in online payments: What are the issues? How can a balance be struck? What would be the most appropriate KYC infrastructure? How can policymakers contribute to facilitate the digitalisation of cash transactions? **(8)**