Disclaimer

Views expressed in this presentation are my own responsibility and do not represent the opinion of CEMLA, nor that of the Fintech Forum Membership.

Contents were prepared using information of the Fintech Forum of CEMLA established in 2018.
“We have an obligation to bring the financial system closer to the people so that everyone benefits from access to credit, savings and insurance products. And we have an obligation to ensure that the benefits of innovation reach everyone and not just a portion of the population. We need to encourage fintech to be built “for the people” – old and young, rich and poor, expert and layman alike”

Keynote speech by Benoît Cœuré, Chair of the CPMI
14th BCBS-FSI high-level meeting for Africa on strengthening financial sector supervision and current regulatory priorities
Cape Town, 31 January 2019
Outline

- Payments’ innovations
- Fintech regional perspective
- Regulatory implications
Payments Innovations

Preliminary findings, CEMLA Payments Forum regional research, 2019
- Fast payments
- Transaction account
- DAVI-PLATA
- Pagadito
- Payment gateway
- POS for smartphone
- VISA & MasterCard fast payments (to be implemented)

- Hybrid Central Bank RTGS
- E-money
- CBDC
- Wallet
- Prepaid card scheme

- "Contactless" ecosystem
- Mobile wallet
- Kushki Bayteq (e-commerce)

- QR payments
- Contactless
- Retail payments via RTGS
- Biometric and digital ID for mobile banking applications.

- Prepaid card scheme (Mach)
- Direct debit
- QR payments
- CVU (Uniform Virtual Key)
- ECHEQ (Electronic cheque)

- Payment gateway
- Fast payments
- E-Money
- QR payments

- Banking Agent
- ACH mobile wallet
- CBDC
- P2P lending
- FX trading (P2P)
- CBDC

- 8% Wholesale
- 2% Retail
- 90% Hybrid

CEMLA
CENTER FOR LATIN AMERICAN MONETARY STUDIES
Retail is in the focus

- Business models and products shifted to customer 360° tailored service
- API keys to embedding new products, shifting connectivity and data transmission
- Cybercrime, a threat to new business models & products

- Speed
- Costs savings
- Remote access
- 24/7 real-time processing
- Other
Incumbents, new entrants, and central banks, too

1. Payment initiation
2. Digital or physical authorization
3. Communications approval/decline
4. Digital or electronic confirmation
5. Settlement order
6. Payment confirmation

Traditional payment service provider (s) 34%
New payment service provider (s) 23%
Existing payment system operator (s) 17%
Central Bank 13%
New payment system operator (s) 6%
Cooperative arrangements 6%

Source: Finovista, 2018
Disrupting the value chain

Digital transactions
Goods & services purchased

Issuer bank
Financial institution

Processing & Servicing
Value added services

Payer

Acceptance & servicing

Intra & Interbank processing

Payee

Value added services

Acquirer bank
Financial Institution

Processing & Servicing

Payment systems’ interoperability
14%

Payments services providers’ functionalities
9%

Payment service features
77%
Fintech across the region

Source: Finovista, 2018
Fintech Regional Perspective

Fintech Forum REG WG Report, 2019
Preliminary findings, CEMLA Payments Forum regional research, 2019
Potential of fintech

Authorities: See fintech relevant for inclusion, competition and efficiency.

New entrants: see fintech as a game changer for financial inclusion, competition and a full transformation of finance.

Incumbents: see fintech an enabler for enhanced efficiency and inclusion.
Fintech is impacting on...

- Financial innovation: 59%
- Fostering competition: 18%
- Economic growth: 76%
- Market completeness: 76%
- Financial information: 47%
- Market integrity: 35%
- Consumer protection: 6%
- Financial stability: 6%

Highly positive: [6%]
Positive: [12%]
Neutral: [24%]
Negative: [24%]
Reintermediation by fintech

- Changes and rearrangements of technological innovation have led to the study of the effects on market concentration, as it has been the case in peer-to-peer economic activities

- Balyuk et.al.: Loan market - fintech companies:
  - Fintech start-up companies: P2P lending platforms.
  - Evolving:
    - from trading venues to new credit intermediaries
  - Potential situation: Moral hazard

- A relevant finding is that given the increasing role of these new players, the end result may be a highly centralized market, with a few platforms' software replacing traditional intermediaries as a key decision maker, posing a challenge for regulators and prudential authorities.

Balyuk, Tetyana and Davydenko, Sergei A. August 2018
Complex ecosystem

- Interconnectedness: important factor in the Global Financial Crisis.

- Risks implied by fintech:
  - For regional authorities: data privacy, cybersecurity and compliance AML/CFT (and traditional risks)
  - Off the radar: new interconnectedness by the technology that support financial innovations (pieces of software).

- Fintech implies an increase in the complexity of the financial networks.
  - Computer architecture
  - Software complexity

- Data importance to:
  - Study possible structural change
  - Analysis possible vulnerabilities
  - Established standards
  - Regulated fintech
  - Mitigate possible systemic risks
Authorities’ fintech concerns

Risk exposure with fintech presence

- Risks ranked as the highest: data privacy, cybersecurity and compliance AML/CFT.
- 63% ranked systemic risk as the lower risk.
- Reputational, legal and systemic risks are perceived as the least important.
Risk perception: public vs. private

- Risks perception differs slightly among the relevant stakeholders:
  - All are worried about data privacy and cybersecurity.
  - Authorities consider AML/CFT compliance also relevant.
  - Incumbents see operational risk as very relevant.
- To address the fintech related risks, the policy agenda for central banks has several priorities:
  - Ensuring proportionality in regulation and risk management as the most relevant, followed by cyber and data protection.
Emerging risks in payments innovations

- Operational risk is one of the highest concerns
  - Default of PSP, PSO, outsourcing (third party risk)
  - Data breach, cyber attack (cyber risk)
- Financial risk are seen more relevant for non-retail payments innovations (e.g. fast payments)
  - PSP and third parties funding is critical to address liquidity risk
  - Credit risk as result of CSM new arrangements, esp. w/ new entrants

![Diagram showing emerging risks in payments innovations]
Some regulatory gaps

- Monitoring new entrants and data availability arise as the main issues related to fintech.
- Coordination issues are frequently referred, in special the lack of clarity and attribution of responsibilities.
- Resistance from incumbents also referred on the need to address interoperability and competition aspects.
Regulatory implications

Fintech Forum REG WG Report, 2019
Preliminary findings, CEMLA Payments Forum regional research, 2019
Priority focus of regulation

- A regulatory functional approach is seen as a priority to address “similar risks equally”
- Cyber and data security are also top priority to adapt regulation
Taking the best approach

Regulatory barriers

<table>
<thead>
<tr>
<th>Reason</th>
<th>Level of Usefulness</th>
</tr>
</thead>
<tbody>
<tr>
<td>Time needed for legislation to adapt to new developments</td>
<td>3.74</td>
</tr>
<tr>
<td>Regulation is not clear or does not provide enough certainty</td>
<td>3.21</td>
</tr>
<tr>
<td>Requirements differ among countries</td>
<td>3.12</td>
</tr>
<tr>
<td>Regulation is not principle-based</td>
<td>2.72</td>
</tr>
<tr>
<td>Regulation does not allow the adoption of new technologies</td>
<td>3.23</td>
</tr>
<tr>
<td>Participants carrying out the same activities are not subject to the same regulation</td>
<td>3.14</td>
</tr>
<tr>
<td>Others</td>
<td>0.67</td>
</tr>
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</table>

Best regulatory approach to enable fintech

Level of usefulness of regulatory approach to enable fintech and innovation (max. 5.0)

<table>
<thead>
<tr>
<th>Approach</th>
<th>Level of Usefulness</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sandbox</td>
<td>3.09</td>
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<tr>
<td>Specific advisory by authorities</td>
<td>3.42</td>
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<tr>
<td>Functional approach</td>
<td>3.59</td>
</tr>
<tr>
<td>Self-regulation</td>
<td>3.14</td>
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<tr>
<td>International coordination</td>
<td>3.14</td>
</tr>
<tr>
<td>Other</td>
<td>0.95</td>
</tr>
</tbody>
</table>
Regulatory implications with payment innovations

- Adapting current regulations more effective to embrace innovations
- Guaranteeing funds and accounts management for new PSO
- QR, NFC generally fitting in
- New regulations needed for products & schemes unfitting in the current framework
- Schemes involving various parties, require enforcement via new rules
- Data reporting (for monitoring) as a common concern for new products and PSP, PSO
- Coordination and communication w/ authorities and industry, playing a key role.
Authorities to build the capacity

- The lack of skilled staff on innovation and technology is seen as a barrier to properly monitoring fintech.
- Absence of a dedicated group could result in duplication of efforts or gaps regarding the regulatory powers.
Fintech, a matter of coordination

- Regional authorities all indicate that there is a need for further involvement from all the relevant authorities.
Thank you for your attention