Chartered Banker

The future of banking

Winter 2020

Open mic: Which regulation would you scrap – or create?

Davidson column: The FCA's role in reshaping regulation.

Country spotlight: Sweden's march towards a cashless economy.

Young Banker of the Year: Past winners: where are they now?

Rewriting the rulebook

Regulation for a new era of banking

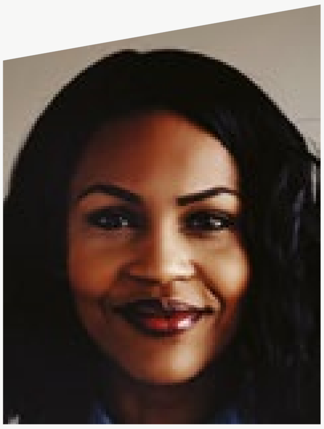
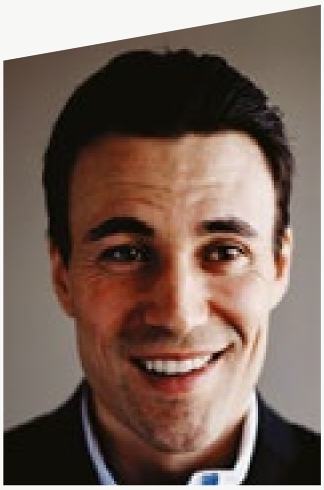
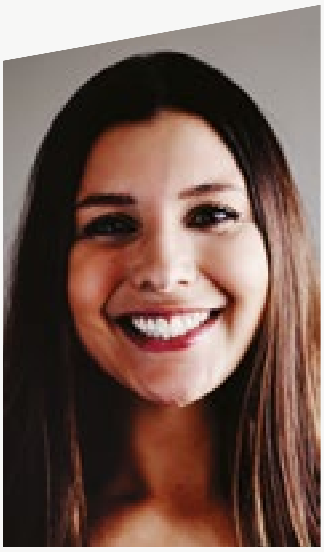
Ten years on
Are banks safer?

Keeping pace
Regulators get proactive.

RegTech reality
A sleeping giant?

Meet SupTech
RegTech for regulators.

Chartered Banker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FINANCIAL

Chartered Banker
The future of banking

The front line

It is time to adapt our regulatory approach to the challenges of the future.

Simon Thompson, Chief Executive

I shall resist the temptation to use the start of a new year – and decade – to make bold predictions about the future. Most of the '2020 vision' forecasts made 10 years ago have long since been forgotten.

Today our greatest collective challenge is transitioning to a sustainable, low-carbon world, so it will come as no surprise that this year's Oxford Word of the Year is "climate emergency". Nor will it be a surprise that the UK's financial regulators are at the forefront of global efforts to identify and disclose climate-related financial risks, and move finance and investment towards low-carbon assets. The Paris Agreement places a special responsibility on the finance sector to lead the transition.

As we enter the 2020s, our financial regulators are also considering the future of regulation more broadly, seeking to identify what has worked well as regulation has been reshaped over the past decade, and what challenges regulation, and regulators, might face in the future.

There have been some notable successes to date but, as always, there is considerable room for improvement. Regulation designed a decade or more ago simply could not have anticipated the scope and scale of the digital revolution. As well as addressing issues relating to ethics and regulation in a digital age, future legislation will need to consider how financial services delivered by a very wide variety of non-banks can be monitored and overseen, and customers protected.

One prediction I will make with confidence is that the role of competent, qualified and professional individuals in delivering banking and financial services that genuinely puts customers' interests first, and recognises the key social purpose of banks and banking, will remain. As the UK's professional body for bankers, together with our Chartered Body Alliance partners, we will be making the case even more strongly than we have over the past decade for the need for regulation to encourage and support professional bankers in delivering responsible, socially purposeful banking in a digital age.

> "Our greatest collective challenge is transitioning to a sustainable, low-carbon world."

In this evolving industry, educating and inspiring new generations of financial services professionals remains as important as ever. One individual has done more than most to lead our work in this area. As we report elsewhere, we ended 2019 by saying farewell to Colin Morrison our Deputy Chief Executive and previously Director of Education and Director of Studies, who has retired after 28 years with the Institute. As we look forward to a new decade, and the challenges it will bring, we wish Colin a very long and happy retirement. CB

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"Innovation and regulation are not mutually exclusive concepts...one complements the other." p22

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The professionals in this issue

Matthew Conway is Director of UK Public Affairs, UK Finance, and is responsible for developing the trade association's political and regulatory engagement strategy. **p14**

Hanif Barma is Co-founder of UK risk governance network the Risk Coalition and founding partner of governance consultancy Board Alchemy. **p26**

Christopher Woolard is Executive Director for Strategy and Competition and a Board member at the FCA. He is also a non-executive board member of the Payment Systems Regulator. **p29**

Sian Fisher is CEO of the Chartered Insurance Institute. A graduate of the University of Oxford, she holds an Executive MBA from Harvard Business School. **p30**

Hikmet Ego is the Chief Executive and co-founder of Swedish FinTech Northmill. He holds an MSc in Industrial Engineering from the Royal Institute of Technology in Stockholm. **p38**

Professor Philip Molyneux is Dean of the College of Business Administration at the University of Sharjah and Emeritus Professor at Bangor University. **p47**

David May is former Director of Learning and Development at RBS. He is a Fellow of the Chartered Banker Institute and Chair of the Institute's new Membership Forum. **p56**

Jim Coke is a Researcher in the Human Centred Design team at Lloyds Banking Group. He is currently completing a PhD at King's College London in the field of behavioural economics, risk and uncertainty in China. **p58**

People & numbers

Green finance in focus

Sustainable finance will be a key focus for financial services firms this year.

The Green Finance Strategy, published by the UK government last year, predicts that not delivering on emission reductions will cost £1.7bn a year in population health impacts by 2020 and £5.3bn a year by 2030.

The strategy's two objectives are to align private sector financial flows with clean, environmentally sustainable and resilient growth, supported by government action – and to strengthen the competitiveness of the UK financial sector.

The UK and Scottish governments last year committed to net zero emissions by 2050 and 2045 respectively.

Financial risk exposure relating to climate change and the low-carbon transition are due to be considered as part of the government's 2020 Managing Fiscal Risks report.

In October, the Bank of England gave major corporations two years to agree rules for reporting climate risks.

Promoting social mobility

NatWest has launched a new apprenticeship programme to support highly talented individuals from economically and socially disadvantaged backgrounds.

Plans are now in place for a nationwide roll-out of the Digital and Innovation Apprenticeship programme, which has been developed in partnership with social mobility charity, Leadership Through Sport & Business (LTSB). Participants will undertake a four-year paid apprenticeship working across the NatWest Ventures and digital teams and simultaneously complete a fully funded degree.

"This programme is about helping young adults in the communities we work in – who otherwise may have been overlooked in traditional application processes – reach their potential," said NatWest Head of Ventures Andy Ellis.

Facts & Figures

£5.3bn

the predicted annual health impact by 2030 of not delivering on UK emission reductions

$1.6bn

customers' money held by Starbucks on preloaded cards and in its payment app

Four years

the length of NatWest's Digital and Innovation Apprenticeship

Could Starbucks be next?

Coffee chain Starbucks could launch into banking in 2020, predicts US research specialist Forrester.

"It's not a huge stretch to imagine a brand such as Starbucks leveraging its digital wallet and huge customer base into banking — it already holds around $1.6bn in customers' money on preloaded cards and in its payment app," said Forrester Senior Analyst Peter Wannemacher. "Low interest rates make it tricky for incumbents to respond with competitive offers, and this onslaught will exert further pressure on banks' net interest margins."

Tandem hires for growth

Tandem Bank has appointed Kunal Malani as its Chief Growth Officer. Malani will lead expansion into new markets including Hong Kong, as well as driving Tandem's domestic growth agenda in the UK.

Malani, who was previously Regional Head of Retail Banking Products, MENA, at HSBC, said: "I am extremely excited to be leading Tandem's international expansion plans as well as the growth agenda we have here at home. We have hit the ground running with Hong Kong and done so at a great time as local consumers are currently massively underserved when it comes to digital banking."

Cash in the community

An initiative to help communities access cash is inviting grant applications. The Community Access to Cash Initiative from trade association UK Finance aims to help identify, report and address gaps and barriers to cash and payment provision.

The initiative will provide grant support and industry guidance to communities to improve access to cash and the adoption of alternative solutions where an ATM is not appropriate or required.

Stephen Jones, Chief Executive, UK Finance, said: "The banking and finance industry is committed to ensuring access to cash remains free and widely accessible for those who continue to need it.

"There is no 'one size fits all' approach and only via collaboration across government, regulators, industry, customer groups and communities can this be achieved."

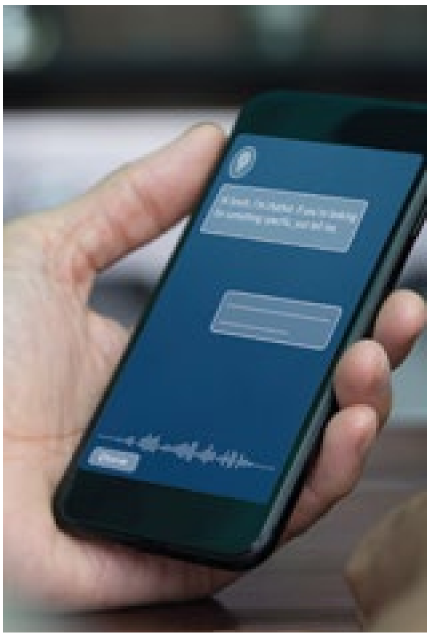
Applications for grant support should be community-led and focused on building towards long-term solutions, for example:

- Digital education awareness programmes
- Driving community cashback
- Increasing awareness of, and access to, available and secure cash provision.

Applications can be submitted via LINK's website until 31 January 2020, with awards to be made by 31 March 2020.

Natalie Ceeney CBE, who led the UK's *Access to Cash Review*, will chair the inaugural meeting of the Award Committee in an independent capacity.

Learning from machines



The impact of machine learning and artificial intelligence (AI) on the UK economy is the topic of a conference hosted by the Bank of England on 25-26 March.

Themes will include the impact of machine learning and AI on growth, productivity and employment, and how inflation and price stability have been, or could be, affected – and the implications for financial stability and systemic risk.

The event is being held in collaboration with the Centre for Economic Policy Research and the Brevan Howard Centre for Financial Analysis at Imperial College, London.

Congratulations to our recent graduates

We are delighted to welcome the following individuals as Chartered Members of the Institute following their recent graduation from the Chartered Banker MBA programme at Bangor University.

Mrs Pempho Nkaonja Chalamanda
Ms Amenaghawon Emerald Akenzua
Mr Benjamin Jerome Bain Jr
Mr Akeem Bode Durotoye
Mr Ambrose Binafiai
Miss Deborah Teresa Williams
Mrs Gwendolyn Culmer
Mr Julian Abenbrook
Mr Simpa Joseph Adaba
Mr Abdullahi Bako Abdullahi
Mr Isa Yahaya Mohammed
Mr Latiff Suwareh
Mr Rakan Kayal
Mrs Kamusiime Pamela Musinguzi
Ms Christina Sasha-Gay Grant
Mr Enroy Prawl
Mr Garth Cranston
Mrs Ijeoma Kelechi Obowu
Mrs Lenore Bartholomew
Mrs Olamide Morenike Gogo-Hassan
Mr Olushola Olurotimi Alao
Mr Omoniyi Olufemi Ibitoye
Mr Quentin Ho Jang
Mr Yusuf Ahmad Bello
Mrs Chinyelu Ogufere
Mr Mduduzi Mathunjwa
Miss Yetunde Adenike Adekoya
Mr Afrique Ramba
Mr Abubakar Sadiq Bello
Mr David Odianosen Ebhodaghe
Mr Deepak Kulathunkal Shivadas
Mrs Helen Amarachi Maduakor
Mrs Nicola Whyms-Stone
Mrs Patience Farida Azuikpe
Mr Samson Adebayo Akinwole
Miss Silvia Vladimirova
Mr Solomon Olatayo Olakunle
Mr Stephen Agyo-Adi Aboshi
Mr Sunday Kolawole Afolabi
Mr Thomas John
Mr Umar Othman Mukhtar
Mr Adedayo Ipadeola Adeyemi
Mr Fidelis Jackson Ibeabuchi
Ms Joy Francis.

People & numbers

Banking with Bó

Newly launched digital bank Bó boasts a brightly coloured bank card and features reminiscent of its FinTech rivals, but there is one key difference. Bó was developed by existing incumbent NatWest – and is very clear about being part of the RBS subsidiary.

Positioned as an account for "everyday spending money", Bó does not currently require its customers to switch their current account or move bills and direct debits.

Bó's development follows previous indications of RBS' digital ambition, including reports that it was considering an attempt to buy Monzo – and its purchase of a 25% stake in Loot, which went into administration in 2019, via an investment through Bó itself. The new bank, which uses NatWest's banking licence, appears as a trading/brand name of NatWest on the Financial Services Register.

New year, new notes

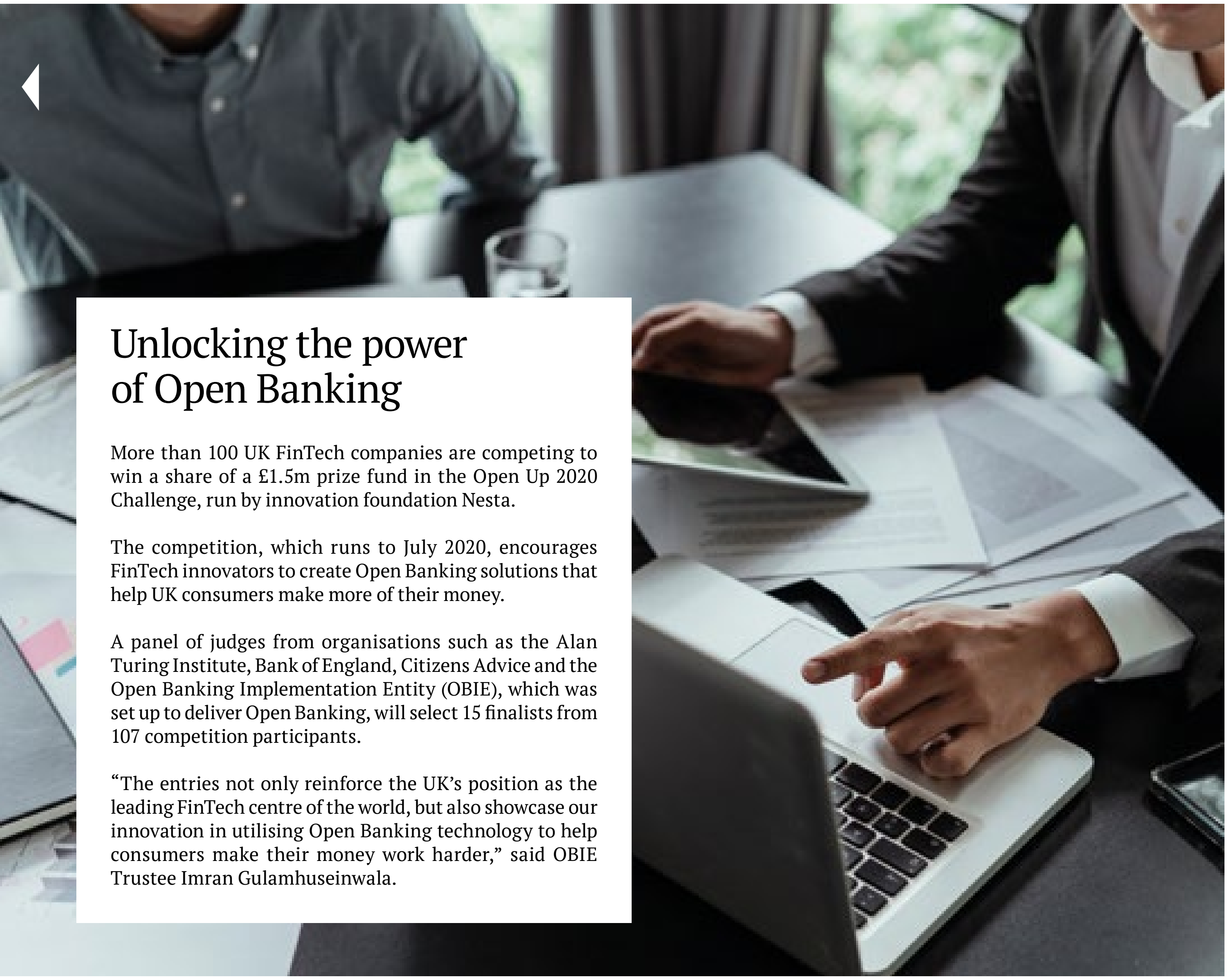
Three new polymer £20 notes are entering circulation this year.

Bank of Scotland is launching a limited edition commemorative note to celebrate the Queensferry Crossing over the Firth of Forth, the longest three-tower, cable-stayed bridge in the world.

A second £20 polymer note also includes the Queensferry Crossing, showing it alongside the Forth Bridge. The front of the note retains images of Sir Walter Scott and The Mound in Edinburgh.

The two notes are slightly smaller than the existing paper £20 notes in circulation, in line with new £20 notes to be issued by the Bank of England and other UK banks this year.

A new Bank of England £20 polymer note featuring the artist J.M.W. Turner will also be launched in February.



Unlocking the power of Open Banking

More than 100 UK FinTech companies are competing to win a share of a £1.5m prize fund in the Open Up 2020 Challenge, run by innovation foundation Nesta.

The competition, which runs to July 2020, encourages FinTech innovators to create Open Banking solutions that help UK consumers make more of their money.

A panel of judges from organisations such as the Alan Turing Institute, Bank of England, Citizens Advice and the Open Banking Implementation Entity (OBIE), which was set up to deliver Open Banking, will select 15 finalists from 107 competition participants.

"The entries not only reinforce the UK's position as the leading FinTech centre of the world, but also showcase our innovation in utilising Open Banking technology to help consumers make their money work harder," said OBIE Trustee Imran Gulamhuseinwala.

Institute agenda

Discounts for members

Deals on eating out, fashion, fitness, tech, and travel abroad are among those being offered to Chartered Banker Institute members through a new partnership with UK student discount card TOTUM.

The TOTUM PRO card is a new product from the National Union of Students (NUS) designed especially for professional learners. It gives members access to wide range of discounts, offers and vouchers on both famous brands and local independents.

The Chartered Banker Institute is delighted to be working with OneVoice Digital and the NUS to make the new TOTUM PRO card available to all current members. Previously, the NUS's flagship TOTUM card was only available to active students.

What if I already have a TOTUM card?

Existing TOTUM cardholders will continue to enjoy the benefits of their TOTUM card until its expiry date and at renewal can apply for a TOTUM PRO card. All new applicants will be able to purchase TOTUM PRO to access the discounts.

How much does it cost?

TOTUM PRO is available for £19.99 for one year, £34.99 for two years, or £44.99 for three years. The card is valid for 12/24/36 months from the date of purchase. Other offers may be available from time to time. A charge of £1.50 applies for home delivery.

Please note that TOTUM PRO only delivers purchased cards within the UK (England, Wales, Scotland and Northern Ireland).

How to apply

- Log into your account at www.charteredbanker.com/login.html
- Go to My member area and then Exclusive membership offers
- Click on the TOTUM button to get your verification code then click on the link to apply or go to https://cards.totum.com/join
- A photograph is required so you'll need either a digital photograph or a webcam.

How do I find out about discounts?

All the information about current discounts is available from users' accounts at www.totum.com. You can also download the TOTUM app from both the Google Play store and the Apple App store.

Key Institute figure retires

Colin Morrison

A key protagonist in the Chartered Banker Institute's transformation from a Scotland-focused to UK body has retired.

Colin Morrison, the Institute's Deputy Chief Executive and Director of Education, retired on 6 December 2019.

"His decision to retire will be a huge loss to the Institute and to all of his colleagues," says Simon Thompson, Chief Executive, Chartered Banker Institute. "Colin has played a key role in leading our transformation from the 'Scottish' institute we were back in 1991, when he was appointed as (then) Director of Studies, to what is now the Chartered Banker Institute, with a UK-wide and growing international remit.

"During that time, our scale, scope, profile, impact and influence have changed beyond all recognition. As Director of Education and (since 2007) Deputy CEO, Colin can take a major part of the credit for this, while ensuring the Institute remained true to its roots and focused on enhancing and sustaining stewardship and professionalism in banking."

Colin will also be missed by the Institute's many UK and international learning partners, not least our colleagues at the European Bank Training Network, where he was President until the end of last year, Thompson adds.

"Colin is truly valued and respected by so many involved in the education, training and assessment of bankers in Scotland, the UK and many parts of the world.

"On behalf of our current and former Presidents, Council, Board and Committee members, colleagues past and present and, of course, our Institute members, we'd like to take this opportunity to congratulate Colin on a wonderful 28 years with the Institute, and send all our best wishes for a very long and happy retirement."

CPD UPDATE:

New-look platform

Professional Financial Advisers undertaking continuing professional development with the Chartered Banker Institute can now access and track their progress more efficiently using a new platform.

Following feedback from Professional Financial Adviser members, the Institute has moved to Competent Adviser, one of the UK's fastest-growing competence testing and learning management providers.

The change, from January 2020, applies to specialist CPD resources and the logging of CPD activities. Competent Adviser has developed innovative tools to help users assess and maintain their competence. Its specialist reporting suite is also able to provide the evidence required by members to demonstrate compliance with the sector's regulatory requirements.

REGISTER NOW:

Showcasing professionalism

Following significant feedback from the Chartered Banker Institute and its partners and members in the Chartered Body Alliance, the Financial Conduct Authority is due to launch a new directory this spring that will enable consumers to check key details of financial services professionals.

The Institute is encouraging all members in Senior Management Functions [SMFs] and Certification roles to check their employer is aware of their professional membership status, as this will be included in the directory for the first time.

The Institute is also launching a new Register of Banking Professionals. There will be a link to this from the FCA website.

You can find the Register on our website at https://bit.ly/2ryNKhf

WEBCAST:

Whose future?

In this webcast, economist Hilary Cooper will explore the issues that affect boomers, Generation X and millennials as they plan their spending, saving and wealth accumulation over their working lives – and into retirement and old age.

The event will challenge and dispel a number of common myths, asking questions such as: 'Are student loans really a debt if they are written off for everyone after 30 years?' and 'What happens when the bank of Mum and Dad runs out of money and cannot afford care?'.

Institute members are part of this conversation both as professionals supplying financial products and services and as consumers in their own right. Join us to hear Hilary's thoughts and participate in the discussion.

Tuesday 18 February 2020, 1pm (GMT)

For more information or to book go to: www.charteredbanker.com/event

Chartered Banker

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* Enhanced, accelerated routes are offered for holders of the CB:PSB's Advanced Standard for Professional Bankers and graduates of the Certified Bank Director programme.

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MORE INFORMATION

For further information and guidance about the eligibility criteria please visit: www.charteredbanker.com/CBBE

Alternatively please contact the Institute's Membership Engagement Team via: info@charteredbanker.com or +44 (0) 131 473 7777.

SPECIAL REPORT

Rewriting the rulebook

Following the announcement in summer 2019 of a "major, long-term review" of the UK's regulatory framework for financial services, *Chartered Banker* asks whether regulation has reached a crucial tipping point at which it risks hampering innovation. Regulators once had time to learn and adapt to industry advances, but to support innovation at its current pace – without risking potentially harmful products and services reaching consumers and markets – it too must innovate.

"The next five to 10 years are going to be the most important we've ever seen in terms of the global alignment of financial services."

SPECIAL REPORT

Ten years on

How well is financial sector regulation working and what are the ongoing issues and challenges for firms?

The past decade has seen the introduction of a plethora of new banking regulations, with some estimates predicting the volume of regulatory reading to reach 300 million sheets of paper by 2020.

Yet even five years ago, with trust in financial services at an all-time low, only a brave person would have suggested the need for more structured and effective external regulation of financial services was in any doubt. But with the roll call of acronyms seemingly growing by the day, from Basel III through MiFID II, PSD2, SM&CR, AIFMD and beyond, is regulation creating a safer and more efficient financial system? And is the ultimate goal of better outcomes for customers being met?

Are banks safer?
In the aftermath of the global financial crisis, one of the first priorities for regulators was to ensure the future stability of the financial system. Professor Emilios Avgouleas, who holds the International Banking Law and Finance Chair at the University of Edinburgh, feels that from a prudential standpoint the right measures have largely been taken – in the UK at least.

"Capital adequacy standards have been very significantly upgraded, the quality of capital itself has been very significantly upgraded, and of course we have a modern and to a large extent functional regime for bank exit or bank restructuring," he says.

In the UK that regime is prescribed by the Bank of England and broadly follows the Basel III requirements and EU banking directives. Banks must have a much higher proportion of their own funds as regulatory capital and the quality of such capital is also scrutinised, with a clear remedial and punitive process if requirements are not followed.

Meanwhile, when it comes to conduct issues, Avgouleas sees regulation as having a positive effect on banks' overall focus.

"The upgrading of conduct of business rules, treating customers fairly, all the debate about ethical standards, have all improved the way the banks see their customers not just as a source of revenue but also as the means to assure the long-term survival of the institution."

Pragmatism and principles

Jake Green, a partner at international law firm Ashurst who advises financial institutions on regulation and compliance issues, feels that the aims of regulators are valid but that a level of pragmatism can be missing, particularly when it comes to EU legislation.

"At the macro level, I think the intentions behind most of the key directives and regulations are well-founded. When you get into the micro level of what is required, though, it all gets a bit disproportionate. So, as examples, the detailed disclosure rules that are required in the Alternative Investment Fund Managers Directive [AIFMD] or the detailed costs and charges rules required for wholesale markets in MiFID [Markets in Financial Instruments Directive] and MiFIR [Markets in Financial Instruments and Amending Regulation]. There is no room for principles or outcomes-based thinking or proportionality."

Addressing risk

Regarding managing risk, Avgouleas points out that although regulation is doing a good job of making financial markets safer, other risks have emerged.

"Because the regulated sector faces constraints, a substantial portion of lending has now moved to the unregulated sector. Also, interest rates have been very low for a very long time, which means institutional investors, if they want to meet their investment objectives and investor expectations, need to undertake risk beyond what would be regarded as acceptable in times when interest rates would offer them a decent return. The most effective market prudential measure is always monetary policy."

Avgouleas believes that misconduct such as manipulation and insider dealing is well-covered by regulation and that regulators are becoming increasingly sophisticated in their handling of these issues. However, he sees a problem with highly speculative trading techniques such as high frequency trading or short selling.

"There is this arms race in terms of speed and exploitation of information. The fact that most of the trading today is algorithmic without much human intervention could badly destabilise the market in a matter of seconds. Trying to control and curb these practices by using the panoply of the market abuse regulations may not be the best way to approach the problem."

Regulation across borders

Given the increasingly global nature of the financial system, how well-synchronised are regulations in different jurisdictions?

> **"Bank safety regulations adopted with the best intentions, such as ring fencing, might have unintended consequences."**
>
> Professor Emilios Avgouleas

"For now, regulations are, to a large extent, aligned," says Avgouleas. "Even with Brexit, UK regulation will not face any problems in terms of being seen as equivalent, and having the UK regulatory framework being grandfathered by the EU regulators."

The question of equivalence is one that Green sees as being more problematic. "I think the problem with the equivalence regimes is that Brexit has hampered that to a certain degree, because no one's wanted to turn on the equivalence regimes for fear that it undermines the European negotiating position – if the UK standard is equivalent, then Brexit becomes less of a big deal in the financial services market."

Green does not see much evidence of a common global approach emerging. "I think we remain completely fragmented country to country and globally, and this idea of a common standard just doesn't play out. You've seen for example in MiFID that the research and inducements rules have created an issue in America, and the US announced that their no-action letters that were in place until 2020 have now been extended to 2023. So that's allowing certain ways to pay for research to continue, even though that may breach a US rule, in order to allow them to access European markets."

Regardless of the current situation, Avgouleas believes the new challenges and opportunities presented by the rapid evolution of FinTech are likely to result in divergences.

"What's going to happen then is anybody's guess. Some national regulators might feel tempted to lower the standard to ease the burden. How the EU will react to that remains to be seen."

Unintended consequences?

Given the vast range of legislation that has been introduced in such a short period of time, it is perhaps unsurprising that there can be issues in terms of the way rules and directives interact. Matthew Conway, Director of UK Public Affairs at the trade association for the UK banking and financial services sector, UK Finance, says this is a major issue for member firms and cites three key examples. The first problem is that of firms being swamped by the need to simultaneously implement multiple requirements from different regulatory bodies.

"Major banks needed to implement both ring fencing and the changes associated with the New Payments Architecture at the same time, and those were UK requirements that were overlaid with multi-year EU implementation requirements that included GDPR [General Data Protection Regulation) , MiFID II, MiFIR and PSD2 [the second Payment Services Directive]. That's five major implementation programmes all falling on the same range of banks all at the same time."

SPECIAL REPORT

Other problems he cites go beyond resource issues for the firms themselves. "The measures that the FCA [Financial Conduct Authority] has introduced to enable customers on reversion rates in closed books to transfer to new lenders might require those new lenders to hold more capital, because they will be seen as riskier by the Prudential Regulation Authority," says Conway. "That means lenders will have less money to lend to first-time buyers who are seeking mortgages of their own. So there's a mismatch between the way one regulator is trying to solve a problem and the consequences of that for what another regulator requires you to do."

Issues can also arise when similar initiatives from different bodies overlap. "As part of its retail banking investigation, the Competition and Markets Authority introduced Open Banking," comments Conway. "But those requirements, though similar, were different enough to what had already been included in PSD2 that the firms on which those requirements fell found themselves having to implement two similar but slightly different programmes in parallel, with the details of one not being clear until later in the process and being contradictory to what was required by the other."

Perhaps more worryingly, Avgouleas suggests there is potential for regulation intended to make the sector safer to actually create more risk.

"The ring-fencing of commercial banking in the United Kingdom in my view is controversial because it turns the commercial banks into big mono-line mortgage lenders – their main business base is mortgage lending and SME lending." As Avgouleas points out, given that these sources of revenue are both volatile and cyclical in nature, the potential impact of a major recession on UK commercial banking could be severe.

"This is the downside," he comments. "Bank safety regulations adopted with the best intentions, such as ring fencing, might have unintended consequences."

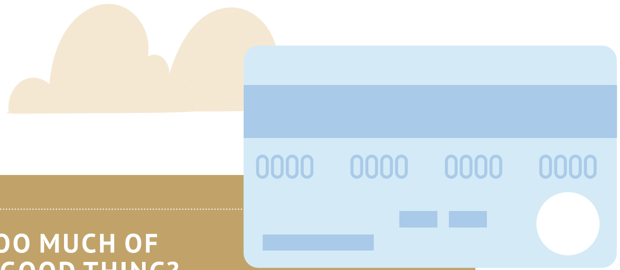
The way forward

Matthew Conway is clear on where regulation should be headed. "What we want to see are three things. The first is that any regulatory intervention is justified by a clear need. Second, we want regulators to propose practical, deliverable remedies that solve the problem, and do so in a way in which the benefits clearly exceed the costs. And third, in a sector with multiple regulators, we want to see coordination, so that problems are identified and solved in a prioritised and orderly fashion and the resolution of those problems doesn't become a problem in its own right."

Meanwhile, for Green, current political uncertainty has brought into sharp focus the need for consistency: "I think Brexit has proven how complicated these issues are and how badly understood they are even by the most competent, be they banks, financial institutions, law firms, academics, consultants or others. You can ask 10 banks and investment firms the same question and you're going to get very different answers, and that is then multiplied by a hundred when you start taking that into Europe. So I think the next five to 10 years are going to be the most important we've ever seen in terms of the global alignment of financial services." CB

"We want regulators to propose practical, deliverable remedies that solve the problem, and do so in a way in which the benefits clearly exceed the costs."

Matthew Conway, UK Finance



TOO MUCH OF A GOOD THING?

Have past problems, from the collapse of Northern Rock to conduct issues such as the Libor scandal which came to light in 2012, been used to justify regulatory change to the point of overregulation?

"I think mostly they have been well used as a rationale for financial regulation both in terms of prudential regulation and in terms of conduct regulation and ethical conduct." Emilios Avgouleas, The University of Edinburgh.

"There is certainly overregulation. But I think it is about embracing an outcomes-based approach and equivalency and perhaps giving regulators more teeth to intervene quicker with less evidence, in exchange for more flexibility on the rules side." Jake Green, Ashurst.

"This is a big issue for us and for our member firms. We've been talking to the government and regulators for the better part of a year about the consequences of poorly coordinated regulatory change. We welcomed the publication in July of the Treasury's call for evidence around regulatory coordination. We are keen that regulatory initiatives are formulated and implemented in a way with what we've termed effective air traffic control, so they are prioritised and implemented in an orderly fashion." Matthew Conway, UK Finance.

SPECIAL REPORT

Which regulation would you scrap – or create?

In this issue's Open Mic feature, we ask industry professionals to rewrite the rulebook and make their own mark on banking regulation.

CHRIS SKINNER,
author and commentator,
TheFinanser.com

1. Which current banking regulation should be abolished?
The regulation that allows 'free banking'. Banking is not free. Banking is a punitive cost to those who can least afford it – the poor with overdrafts and credit issues – and free for those who can most afford it – the rich with good balances and zero issues. We should change this.

2. If you could introduce a new one, what would it be?
Treating customers fairly. You may say we have that already, but why do we have an industry that needs to be regulated to treat customers fairly? Any other industry would treat customers brilliantly. What's wrong with ours? The problem is that the industry has been built by making money from hidden fees that punish customers due to free banking (see above). If we charged for banking, we could start to treat customers with proper service rather than punitive service.

JOANNE MURPHY,
Chief Operating Officer,
Chartered Banker Institute

1. Which current banking regulation should be abolished?
Regulation is introduced as a safeguard for firms, consumers, and the wider economy, so I wouldn't necessarily recommend abolishing any of it. I do think that the challenge for banking regulation is keeping pace with technology changes, particularly those such as machine learning (ML), which may amplify risk and has ethical considerations too. The dynamic nature of ML presents a whole new world of bank regulation complexity.

2. If you could introduce a new one, what would it be?
Personally, I'd make the Women in Finance Charter mandatory not voluntary, particularly aspects around linking senior executives' compensation to delivery of diversity targets. I'd expand diversity in this sense beyond women, though. It has been proven that organisations which embrace diversity and embed inclusion not only outperform competitors in terms of profitability, they reduce risk and enhance employee engagement. For the regulator this has to be a good outcome and the FCA in particular is making great progress in leading by example in this area.

PETER ALDERDICE,
Senior Associate,
Banking and Finance, Shepherd and Wedderburn LLP

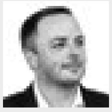
1. Which current banking regulation should be abolished?
Top of my list for the red-tape scrapheap is the complex overlap across the different regulatory regimes for loans and credit. Recent years have seen European Union directives on mortgage lending and consumer credit being implemented in the UK by layering further regulation on top of existing UK regulation, without proper alignment or integration.

The result is a pig's breakfast of incoherent rules that differ markedly for residential mortgages, buy-to-let lending for consumers, unsecured credit to acquire land, and other personal loans. A simpler, clearer body of rules is needed in order to encourage more competition and innovation in lending and ensure consumers are protected from harm.

2. If you could introduce a new one, what would it be?
The FinTech revolution is bringing significant improvements to the financial well-being of many in society. However, the increasing shift toward a cashless economy risks leaving behind some of the more vulnerable members of our communities.

Financial services in general, and payment services in particular, have become like public utilities – essential facilities for daily life. It is incumbent upon the banking industry to ensure that the push for digital solutions takes account of the wider need for financial inclusion, especially when it comes to the ability to pay for life's necessities.

SPECIAL REPORT



SCOTT MOWBRAY,
Co-founder of FinTech start-up, Snoop

1. Which current banking regulation should be abolished?
Ironically it can sometimes feel that the only innovation in banking comes from the regulator. Take Open Banking. It's happening because of regulation targeting more competition and innovation. Many banks have been somewhat reluctant to see it as anything other than a compliance exercise. It could and should be transformative for competition, the sector and consumers. So rather than abolish a piece of regulation – I would abolish incremental thinking and complacency at banks that doesn't enable transformative change.

2. If you could introduce a new one, what would it be?
Rather than introduce a new piece of regulation, I would focus on making Open Banking work and take it to everyone. Doing so will play a significant part in improving financial literacy and help to drive better financial decisions and outcomes. It will make competition for customers a reality and not just a pipe dream. It will improve the efficiency of the market and unleash a wave of innovation that genuinely puts the customer in charge of their data and life. To achieve this, I would encourage the Financial Conduct Authority to invest in giving the Open Banking initiative more oomph, impetus and awareness. It will, after all, put more money back in consumers' pockets than the PPI scandal! Maybe it's time to bring back Arnie...

HANIF BARMA,
Co-founder of the Risk Coalition and founding partner of governance consultancy Board Alchemy

1. Which current banking regulation should be abolished?
New regulation seems to come around faster than Mondays after a weekend. Yes, compliance is an additional burden and cost for financial services companies. But regulation itself (at least in recent history) has been developed in consultation with industry in response to real needs – so I'm not sure there is an imperative to abolish any of it right now as we need to raise standards and build confidence in the sector.

In recent years, some fairly chunky, new regulation has been introduced. In particular, and not just in financial services, personal accountability has become a prime focus for the regulators. Boards, too, should be viewing the greater personal accountability as a good thing for the organisations they oversee, to help drive achievement of their strategic objectives.

2. If you could introduce a new one, what would it be?
Rather than new and more regulation, we now need some time and breathing space to let current regulation feed through and make a real difference.

For example, the Senior Managers Regime will be on all boardroom agendas and should be an important driver of much-needed behavioural and cultural change within financial services.

Let's see what impact the recent regulatory changes have had, so we don't simply add to the cost of compliance without any real benefit. We should really be focused on achieving good outcomes.

SARAH WALKER,
2019 Young Banker of the Year and Branch Director for Santander

1. Which current banking regulation should be abolished?
The ultimate aim of banking regulation tends to be around protecting people's money, ensuring financial stability, combating crime and improving transparency – so I'm not sure I'd abolish any of it.

2. If you could introduce a new one, what would it be?
I would love to see a banking regulation introduced whereby a customer who is suffering with mental well-being and financial difficulty is able to have a payment holiday, while they recover and get themselves back on their feet.

JAMES VARGA,
CEO and founder of Open Banking data specialist, The ID Co.

1. Which current banking regulation should be abolished?
In our experience, the loosening, deregulation or abolishing of banking regulations rarely leads to positive outcomes. The experience of 2008 and the past decade remains fresh in the memory, and we should understand that it is imperative that the banking sector works for all, including the sector, business, and consumers.

"I'd make the Women in Finance Charter mandatory not voluntary, particularly aspects around linking senior executives' compensation to delivery of diversity targets."

Joanne Murphy, the Chartered Banker Institute

We understand the rise in competition within the sector, emanating from new challenger banks, Big Tech, FinTechs, digital currencies and others. To remain competitive, banks must focus on their first priority: customers.

It is only by offering customers new, innovative products and services, using new technologies, that they will retain market share, and the trust of their customers.

2. If you could introduce a new one, what would it be?
We believe it is necessary and desirable for Open Banking to be broadened and strengthened to a system loosely known as Open Finance.

This would see mortgages, insurance, investments and credit cards brought under the Open Banking umbrella. In time, this could also be expanded to telecoms and utilities.

It is only by giving consumers genuine control and empowering them with their own data, that they will be able (and responsible) for using it to save time and money. We already know that Open Banking affords them that opportunity in their everyday banking. By broadening out the legislation to cover Open Finance, they could save money in all aspects of their lives.

MICHAL GROMEK, Head of Compliance at Safello, a Stockholm-based cryptocurrency platform; Head of Insights at Stockholm Fintech Week and author of the *Stockholm Fintech Report 2018*

1. Which current banking regulation should be abolished?
While I deeply support the reasoning behind the EU's General Data Protection Regulation [GDPR], there's a problem. Article 17 of the regulation – the right to be forgotten – establishes that everyone has the right to request that their personal data be erased without undue delay. But this isn't possible.

In Sweden for example, it clashes with the accounting regulation requirement that transaction data is kept for up to seven years. Then there's the blockchain dilemma. Once users' data has been placed online, there's no technical means to erase it.

So we have a clear clash between regulation and technology. Moving forward, GDPR creates a new environment of privacy by design. But what about all the historical data? That's the other big challenge.

2. If you could introduce a new one, what would it be?
I think regulation should be a safe space to develop our FinTech companies.

New technologies, products, and related services have the potential to spur financial innovation and efficiency and improve financial inclusion. So regulation should support this.

"Top of my list for the red-tape scrapheap is the complex overlap across the different regulatory regimes for loans and credit."

Peter Alderdice,
Shepherd and Wedderburn LLP

But the risk-based approach of intergovernmental organisations such as the Financial Action Task Force [FATF], which develops policies to prevent money laundering and terrorist financing, threatens to stifle the cryptocurrency sector.

Its regulation will impose impossible, complicated requests on licensed and regulated cryptocurrency in developed countries – and potentially open up a 'dark' market in which FATF does not have jurisdiction.

I'm all for making FinTechs more secure. But imposing regulation that runs counter to the nature of Blockchain feels like a knee-jerk reaction that has not been thought through.

JOSEPH HEALY, Co-Chief Executive Officer at Australian Judo Bank and author of *Breaking the banks: What went wrong with Australian banking?*

1. What current bank regulation do you think should be abolished?
The current method of determining risk-weighted assets [RWAs] should be repealed and replaced by a standard, uniform capital calculation. Capital overlays can be applied at the Group level based on the regulators' view of business model risk. There are several problems with RWA determination which distort capital allocation and management decisions. The current approach is open to gaming and a bias towards mortgage lending and property secured lending. As a result, SMEs have been disadvantaged.

2. If you could introduce a new one, what would it be?
I would make a commitment to professionalism mandatory. I would do this by prescribing that anyone in a customer-facing role and anyone in a general manager level and above, should be required to be a Chartered Banker or commit to undertake study to qualify as a Chartered Banker. If the industry is to restore societal trust, it must commit to professional standards that are uniform and understood by society in the way that doctors, lawyers and accountants are professionally accredited.

SPECIAL REPORT

Ahead of the curve?

From Open Banking to Big Tech, we look at what could be the key concerns for regulators over the next 10 years.

Open banking

Jake Green, a partner specialising in financial services compliance at law firm Ashurst, sees Open Banking as a regulatory initiative that has the potential to be extremely positive for the consumer but which poses questions from a regulatory perspective.

"What you should have is automation that will sensibly enable people to work out that, for example, if they've got £30 in one account not doing anything they should put it into an account that's going to earn them more interest. It really should revolutionise the way in which retail wealth management and investments are carried out, and it will then decentralise the dominance of banks in relation to savings products. But I think the real fear here is the reliance on technology and liability issues. That is, who is responsible for the way in which APIs and banks and information and instructions interact? And then operational resilience is going to be the key issue as to how this plays out over the next five to 10 years."

A precious resource?

While the ongoing march of digitalisation offers many benefits to consumers, the explosion in digital payments and the corresponding decline in the use of cash is not without its problems. According to the Payment Systems Regulator (PSR), cash use, which has plummeted from 60% to 30% of all transactions in the past 10 years, may drop below 10% within the next decade. PSR Managing Director Chris Hemsley sees a major role for the regulator in protecting cash.

"Cash still has an important role to play and our work needs to protect people who cannot, or do not feel able, to adopt digital payments. The PSR has used its powers to ensure LINK met its commitment to protect the spread of free-to-use ATMs. Our view is that everyone should have a good choice of how to make payments in ways that work well for them, and that is how we are defining our approach.

"We are keen to explore how community needs can be reflected in decisions affecting where ATMs are located. We know that the impact of not having access to cash is worse in deprived areas and remote towns," continues Hemsley. "These considerations can guide decision-making so that actions reflect need."

Like his peers, Hemsley sees the role of the PSR more generally as a proactive and pragmatic one. "We have a role to make sure that all appropriate safeguards are built into the payment systems people rely on every day, but otherwise we need to get out of the way and let innovation happen." He points to the implementation of Confirmation of Payee as an example of the former, while Request to Pay represents an innovation that will benefit consumers by giving them more control over when, how and who they pay.

Too much information?

The use and misuse of data is a huge issue in many aspects of modern life and financial services is no exception. Hemsley is positive about the potential use of anonymised data to support innovation.

"Having access to data is an incredibly useful way of helping develop new initiatives, products and services for everyone. While it isn't appropriate to require regulated payment system operators to open access to scheme-wide data at this point, we will work with Pay.UK to explore the viability of opening up access to data in the New Payments Architecture. This will include assessing the potential role of anonymised datasets in the development of new payment services."

On the issues of misuse, Professor Emilios Avgouleas, International Banking Law and Finance Chair at the University of Edinburgh, sees a potential need to regulate the use of big data and algorithms to avoid the perpetuation and exaggeration of biases.

> **"The PSR has used its powers to ensure LINK met its commitment to protect the spread of free-to-use ATMs."**
>
> Chris Hemsley, PSR

“When it comes to technology, it’s very difficult to determine where that lives and how it breathes.”

Jake Green, Ashurst

“The technology is not yet there, but a lot can be done to regulate the algorithms to safeguard customers and ensure the elimination of gender or racial biases that are sometimes incorporated, either in the algorithm or in the data that the algorithm processes.”

A new model

While still seeing a role for traditional, well-regulated financial institutions which really understand their customers, Avgouleas expects a new model of financial interaction to significantly impact the sector.

“We have a radical change with new technology and new social apps where people interact in a horizontal model, in a decentralised way, rather than with an intermediary. And it’s a structural not a cyclical change, it’s not like a recession that will pass at a point,” Avgouleas says.

This constantly evolving and transforming market presents a challenge for regulators to anticipate and adapt, encouraging competition while ensuring a level playing field. Jake Green sees areas where existing regulations may not always offer the same level of protection to consumers as it does for customers of traditional banks. He cites the example of e-money (the electronic store of monetary value on a device so that it can be used as a means of payment without necessarily involving a bank account in the transaction).

“E-money regulations allow for firms to act and operate to a certain degree like banks without having to have deposit licences and without having great capital associated with them. I think that does allow for competitor tensions for smaller players against banks, which perhaps from a pure economic analysis allows for a more efficient environment. However, I slightly worry that we now seem to have too many e-money players and I do wonder if the systems, controls and protections are adequate.”

Tech without frontiers?

Green also points to a less obvious issue with the increasing use of automation for many financial transactions: the potential lack of clarity around where a transaction takes place and hence under what jurisdiction.

“When it comes to technology, it’s very difficult to determine where that lives and how it breathes and that creates huge issues as to who regulates it, where it should be regulated and how it’s regulated.”

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A larger issue?

However, Avgouleas sees the major threat to traditional financial institutions coming not from FinTech companies but from Big Tech.

"The biggest challenge for traditional financial institutions will not come, in my view, from the FinTechs because the profit margins for FinTechs are very low and they will never be able to build scale. The big challenge will come from the technology companies which turn into financial services companies, like, of course, Facebook with Libra. Google is moving into financial services as well. I would be surprised if Amazon doesn't in the near future, and, as a matter of fact, I expect ecommerce companies and big supermarket chains to develop their own cryptocurrencies."

Although Big Tech's incursion into financial services is a relatively recent development, the sheer scale and access to detailed datasets of these companies makes them not only a huge threat to traditional firms but a big potential problem for regulators.

> **"We have a strategic objective to ensure markets function well, and to do that we have to be proactive."**
> Richard Monks, FCA

"So the landscape is radically changing and the regulators have to adapt as well. There should be a more restrictive approach to the entry into the market of big data companies," concludes Avgouleas.

Where innovation and regulation meet

Regulators themselves are clear that to ensure a healthy future for the financial sector, innovation and regulation should go hand in hand.

"Innovation and regulation aren't mutually exclusive concepts," comments Hemsley. "In fact, one complements the other."

Richard Monks, Director of Strategy, Financial Conduct Authority (FCA), is passionate about the regulator's role in proactively shaping the future of the sector.

"I think the idea that things happen within the industry and then the regulator opines on them afterwards is ineffective. We have a strategic objective to ensure markets function well, and to do that we have to be proactive. It's a very open conversation, almost nothing is off the table. We'd like firms also to think about the future direction and this question of how to regulate in a digital age rather than simply how we regulate now." CB

REGULATION GOES GREEN

In the wake of the FCA's recent Feedback Statement on Climate Change, what is the role of the regulator in supporting the development of green finance?

In October 2019 the FCA published a Feedback Statement which sets out three key priorities:

1. Enabling firms to manage the risks from moving to a low-carbon economy
2. Supporting the development of the green finance market
3. Ensuring consumers are appropriately protected.

Richard Monks, FCA Director of Strategy, says that for the time being the regulator is happy to pursue a pragmatic and collaborative approach to pursuing these aims.

"We're a supporter of the TCFD [Task Force on Climate-related Financial Disclosures – a market-led initiative] recommendations and we're saying to firms 'how might you embed that in your work and processes?' without mandating at this stage."

However, that does not mean firms will be allowed to mislead consumers regarding sustainable finance. "If you are sold a product, marketed as green but which isn't green, that is against our requirements and we take that sort of conduct, 'greenwashing', very seriously," says Monks.

Nick Cook, FCA Director of Innovation, points to the need for clarity around what 'sustainable' means. "I think there's sort of a gap in the taxonomies and how people understand these products at the moment. So, we see there's a role for us to play there."

Meanwhile, some green issues are less obvious, as Cook points out. "For instance, we see a lot of distributed ledger testing through our sandbox and some of them are based on proof-of-work algorithms, which are very expensive from an electricity consumption point of view. We would like to work out what is the right position for us to have on some of these technologies where they offer meaningful value for society in terms of new product, new opportunity, new ways of doing business, but in some instances may not be sustainable in how they go about doing that."

SPECIAL REPORT

Better regulation through technology?

With the need for agile and efficient solutions increasing in an ever-evolving regulatory landscape, we look at RegTech's growing relevance.

Reporting on RegTech back in August 2017, we asked whether the phrase was more than just a buzzword for banks facing a rising regulatory burden. Since then the term has entered the financial services mainstream, but how far has RegTech come in terms of actual implementation?

Given that McKinsey estimates between 10 and 15% of the total financial services' workforce is now dedicated to governance, risk management and compliance, the case for RegTech is not a difficult one to argue. Yet while there's no doubt RegTech has come a long way in the past two years, for those close to the subject its possibilities are still only just starting to be realised.

Callum Grant is Product Director at leading compliance technology provider Trailight. As a self-described 'poacher-turned-gamekeeper', with a 35-year career in insurance and retail banking, he has a strong understanding of the regulatory landscape from both sides of the issue.

"I think as an industry we've made a great start, but there's a very long way to go yet. I also think that we don't all fully understand yet what the potential of RegTech is, in terms of how it can transform and join up compliance management policy and process," he admits.

Nick Cook, Director of Innovation, Financial Conduct Authority (FCA), agrees. "I refer to it as a sleeping giant because the business cases the RegTechs are going after are very profound. The back-office costs of many institutions are substantial both in terms of human resource and in terms of pounds and pence. So there are some big cost lines on the profit and loss sheet and there are some big societal issues that some of the RegTechs are trying to address and help. And yet, at the moment, widespread adoption of technologies in the compliance parts of institutions is slow and it's inconsistent between different institutions and sectors."

"As an industry we've made a great start, but there's a very long way to go yet."
Callum Grant, Trailight

Benefits of RegTech

Recent analysis by Deloitte identified companies providing solutions in a number of areas, including Regulatory Reporting, Risk Management, Identity Management and Control, Compliance, and Transaction Monitoring. It identified a range of benefits from deploying RegTech in these areas:

- Cost efficiency
- Availability of more accurate and granular information
- Flexibility to address an array of compliance and risk management needs
- Improved security through data encryption and secure transmission channels
- Better analytics through data mining and visualisation.

Grant takes as an example the Senior Managers and Certification Regime. "The onus is very much on accountability, responsibility and transparency, and financial services businesses have really struggled to manage these challenges using spreadsheets, proprietary HR

SPECIAL REPORT

systems and adapting internal technology. We can solve that with flexible, highly configurable software that has been built specifically from the ground up. RegTech solutions are really going to help firms, and in particular senior managers, with Duty of Responsibility in mind, deliver a great outcome that is cost effective, secure and much less resource-hungry than manual processes."

Looking to the future, Cook sees the potential of RegTech to embed compliance by design into firms' systems and controls.

"Rather than compliance or risk management being a post-event activity, it will become something you can ensure happens at the point when services are offered. There are definitely compliance opportunities through the use of technology and embedding compliance into the design of those technologies."

Obstacles and challenges

However, while the potential may be there, a number of barriers to uptake remain.

"These are complex technologies about which firms have a limited understanding and they are therefore quite sensibly being cautious about deploying them into their institutions," says Cook.

Grant agrees there is still some natural inertia in terms of firms' appetite to consider RegTech solutions.

"I think there's still an attitude of 'we can do it using spreadsheets, SharePoint etc'. The other challenges we face are often quite lengthy procurement processes, which are quite rightly very detailed in their examination of a potential provider."

For many firms data security is also a key issue. "Because of the type of data we're working with, which is by its nature focused in on people, firms are very keen to get under the hood of data security and how we manage and control that. We welcome this engagement as a software and as a service provider."

Cook points out that the nature of RegTechs themselves can be an obstacle for larger firms. "Some RegTechs are very small and so as well as having nascent technology, they are nascent businesses. They may not have the working capital or balance sheet to support long-term use, and if a large institution is looking to deploy within a compliance function they treat that with a degree of caution, for good reason."

As a new sector, RegTech is largely inhabited by small players whose natural tendency is to focus on a specific area of expertise. This is an advantage from the perspective of developing strong expertise but can cause issues, particularly when trying to win business with bigger firms.

"What we hear from big institutions is that a number of RegTech companies are focusing on very niche parts of the value chain," says Cook. "And again, there's reticence to open up your systems, your procurement framework and your IT security to solve something that's just a small part of your problem. So I think what we're expecting, and starting to see, are more partnerships between different RegTech companies which can provide a more holistic product."

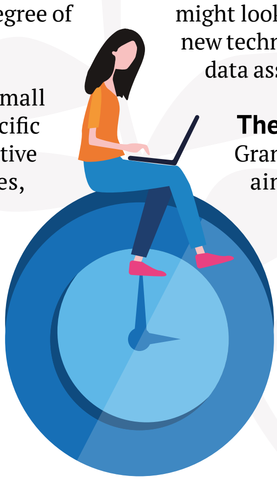
Meanwhile, the disconnect between firms running internal legacy systems and RegTech providers offering more agile solutions can also present problems.

"Most RegTechs are cloud-native by design and not all the institutions necessarily have a cloud infrastructure or security policy that supports the use of those kind of services," adds Cook.

The regulator's role

As Cook explains, the FCA takes its role as a convener and enabler seriously. However, one area where he recognises an unfulfilled need is in supporting RegTech firms to bridge the gap between demonstrating a good idea and being able to prove it is more effective than solutions currently in use.

"An environment such as our sandbox that lets you test on real-world consumers isn't as appropriate for someone who's developing compliance technology for deployment within an institution," Cook admits. "What they really want is high-quality data to test and prove the value of their new technology. Something we're looking at over the next few months is what a digital test environment might look like in the UK, things like A-B testing, comparing your new technology with existing technology, what might some of the data assets in that test environment need to be?"



The ultimate goal

Grant points out that, as with regulation itself, the ultimate aim of RegTech is to ensure that consumers, markets and robust compliance are at the heart of the firm's business model.

"As a RegTech provider we've got to be focused on outcomes, not just from an administrative perspective but in that wider cultural and conduct space. If we've got a really strong financial services industry which is behaving well and delivering fantastic outcomes for consumers, that's fundamentally what it's all about and it's where RegTech can play a key role."

> **"What we're expecting, and starting to see, are more partnerships between different RegTech companies which can provide a more holistic product."**
>
> Nick Cook, FCA

SUPTECH: REGTECH FOR REGULATORS

How are regulators themselves using technology to streamline their monitoring of existing regulation and help develop future regulatory requirements?

Though still a nascent innovation, the use of technology incorporating big data and artificial intelligence (AI) by supervisory bodies already has a name in its own right: SupTech.

Recently published research by the Bank for International Settlements (BIS) analysed SupTech initiatives in 39 financial authorities globally, finding that almost half either have an explicit SupTech strategy or are in the process of developing one.

Most use cases cluster around misconduct analysis, reporting and data management, with the technology also being trialled for virtual assistance, micro-prudential, macro-prudential and market surveillance applications.

While the potential is clear, the BIS report found that most projects are experimental with only 33% of initiatives operational. It points out that the inherently small market limits business opportunities for private providers, calling for international collaboration between regulators to develop SupTech more efficiently.

Nick Cook, Director of Innovation, FCA, is enthusiastic about the potential of SupTech for the organisation. Cook oversees an 80-strong team, around half of which is focused on internal innovation covering many of the areas mentioned in the BIS report.

One approach Cook sees as having high potential is the use of proprietary and market data to build predictive models that can be used to better allocate supervisory resource.

"We have to prioritise where we focus our effort in terms of reviewing specific firms for specific topics. So we've been doing some work using different forms of machine learning to try to build prediction engines to help us prioritise where we should focus our effort."

Big data is also invaluable from a market intelligence perspective, says Cook. "Combining data in new ways can give us richer insights into who's offering what kind of products to whom and how."

Meanwhile, some of the technology being explored is about automation, reducing manual processes and embedding a solution that completes tasks consistently, repeatably and efficiently.

More ambitiously, Cook cites a programme of work around digital regulatory reporting – the writing of regulatory requirements as machine code that could be directly implemented into firms' systems without human interpretation or implementation effort.

"The big bonus for us is that we could change our regulatory requirements efficiently, and in certain areas more dynamically, but the other big benefit would be an increase in the quality of the data we collect."

As Cook points out, with thousands of firms individually interpreting the requirement there are inevitable inconsistencies. Digital regulatory reporting seeks to reduce these.

"It's going to reduce the amount of human interpretation that's needed so we can drive up the quality of the data and so use it to better effect."

Chatbots are another area where Cook sees potential. Having trialled virtual assistants internally, his team is now looking at how chatbots could be used to help firms better understand the regulatory system or interface with the organisation's contact centres.

Finally, he mentions phoenixing (the practice of carrying on the same business or trade successively through a series of companies where each becomes insolvent) as an area where the use of SupTech such as network analytics has huge potential.

"We're looking to use this to better understand connections between certain parts of the market and between individuals so that we can better identify when someone is fronting a new company. There's quite a bit of scope in that space for understanding connections and networks better and using that to inform some of our authorisation and supervision decisions." CB

RISK COALITION

A new approach to risk

New principles and guidance on managing risk in the UK financial services sector have been launched by the Risk Coalition.

More than 10 years on from the financial crisis, failings in financial services remain regular occurrences and the fines continue to mount. Inadequate risk governance and oversight is frequently at the heart of the headlines.

"The issues are quite widespread," says Hanif Barma, Co-founder of the Risk Coalition, a network of not-for-profit professional bodies and membership organisations committed to raising standards of risk governance and risk management in the UK.

"Sometimes it's to do with IT and resilience. It may be to do with cyber and hacking, culture and customer treatment, or companies experiencing financial stress. Often companies end up being in trouble with regulators. So, there's a whole mix of issues that are still quite prevalent."

With new technology and macro risks emerging – and the speed of change accelerating – the need for effective risk arrangements has never been more important.

Managing risk

The Risk Coalition launched the Risk Guidance Initiative in 2018 to provide a framework for UK financial services regulated firms to meet best practice. Through industry consultation, the aim has been to address the challenges of today's changing and demanding environment by developing high-quality, principles-based guidance for board risk committees and risk functions.

The final principles and guidance document was published in December 2019 after two years' work, four months' consultation and more than 60 interviews with respondents including risk committee chairs and members, chief risk officers, chief executives, advisers and academics.

"What we've done is set out a series of principles," Barma explains. "There are eight principles for risk committees. The really important thing, as a starting point, is to recognise that the risk committee is effectively supporting the work of the board. It's a subcommittee that's really an advisory committee, with the board retaining accountability.

"The principles retain that board accountability – it's not the board washing its hands of responsibility for risk and moving it to the risk committee. So, there needs to be good delegation from the board and effective reporting back."

The Financial Conduct Authority has welcomed the Risk Coalition's initiative to raise standards in risk oversight, commenting: "Their approach and guidance complements the personal accountability we regard as an important regulatory objective. It is important that SMF role holders do not simply adhere to the guidance as a box-ticking exercise, but also reflect on how to ensure adequate regulatory outcomes."

Principles and practice

Board accountability is the first of the eight principles set out in the guidance. The others cover risk committee composition and membership; risk strategy and appetite; principal risks and continued viability; risk culture and remuneration; risk information and reporting; risk management and internal control systems and chief risk officer and risk function independence.

"The main areas around the risk committee include its role for overseeing risk strategy and risk appetite and advising the board on that," Barma continues. "To what extent is the organisation operating within its risk appetite? It's also looking at things such as financial viability of the business. It will have some responsibility for overseeing risk culture as well. So, boards will set the culture of the organisation and the risk committee will exercise oversight, monitoring the extent to which that risk culture is actually being lived in the organisation."

"We're not saying, 'This is what you have to do'. We're setting out the principles and providing some guidance."

A key aspect is that the risk committee should not operate in isolation, but needs to work with other board committees overseeing areas that have their own risks.

"As an example of this, risk committees have to work quite closely with the remuneration committee to make sure they set salaries or pay within structures that are aligned with good risk-taking," Barma explains.

"At the end of the year, the risk committee will also be looking at what bonus payouts might be. And if there have been situations with poor risk behaviours, they make an adjustment to an individual's bonus. Again, the information for that would typically come from the risk committee. So, they need to be joined up with other committees.

"Very good coordination is also needed between the risk committee and the audit committee. There's some inevitable overlap between audit and risk and they're both looking at risk-related matters."

Strategic oversight
The Risk Coalition's guidance is not prescriptive, but provides users with good practice principles, supported with practical guidance on their implementation.

"If you're a risk committee chair, we're not saying, 'This is what you have to do'," Barma says. "We're setting out the principles you should be achieving and providing some guidance. Then it's really up to you how to achieve that."

Barma stresses that the principles should be scaled according to the size of the organisation applying them.

"We do recognise that, for the larger banks like Barclays or HSBC, they'll likely have the resource and capability in-house that a smaller challenger bank or FinTech might not have," he says. "So, it's really important that when people look at our guidance, they apply it in a proportionate way."

It's also vital to link risks clearly to the organisation's strategy and objectives.

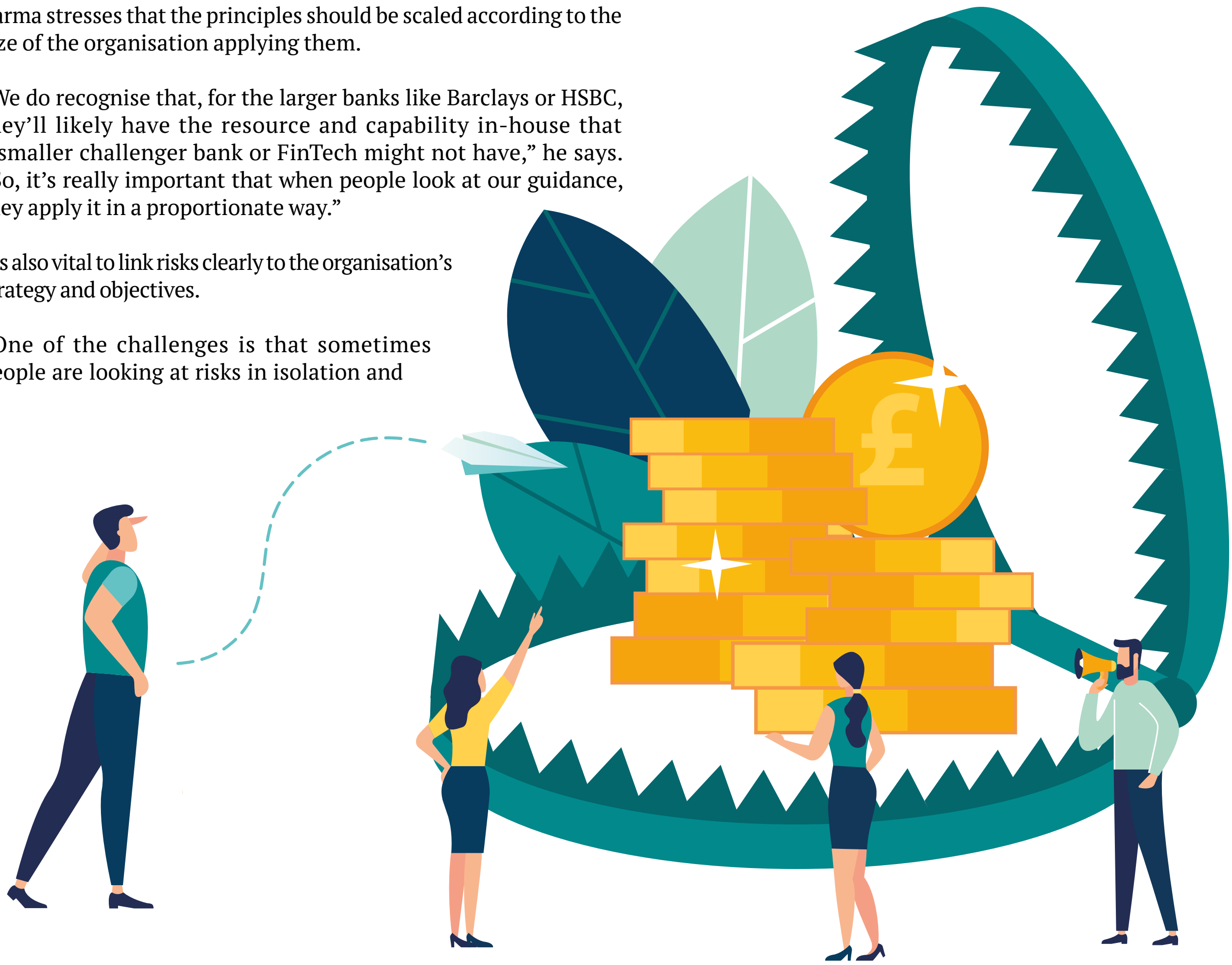
"One of the challenges is that sometimes people are looking at risks in isolation and not really thinking, 'What does this mean for our organisation and the strategy and the objectives we have set?'"

"It's really important that when people look at our guidance, they apply it in a proportionate way."

Risks aren't always negative, Barma adds. Sometimes they present opportunities: "It's important for the risk committee and for the board to be thinking about opportunities. When something changes, things could go wrong. But on the other hand, it's also giving rise to a new opportunity to do something different."

The Chartered Banker Institute is a member of the Risk Coalition, alongside organisations including Airmic, the Chartered Institute of Internal Auditors, and the Chartered Insurance Institute. The coalition's observers include the Banking Standards Board and Financial Reporting Council, and its final guidance is available at www.riskcoalition.org.uk. CB

Hanif Barma is founding partner of governance consultancy Board Alchemy and Co-founder of the Risk Coalition.



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THE DAVIDSON COLUMN

The future of regulation

We need an outcomes-based regulatory approach to remain agile in a landscape characterised by change, says Christopher Woolard, Financial Conduct Authority Executive Director of Strategy and Competition.

Technology and innovation, changing consumer needs and new models and services are transforming financial services. This will have an impact on the way the FCA regulates. These drivers of change are the among the reasons why we've launched our work on the future of regulation.

The end of the first wave of post-crisis regulation presents the need to determine what worked well, what could still be improved, and the chance to think about changes in consumer attitudes. Long-term low interest rates mean the search for return is stronger, and consumers are getting older, saving less and inheriting assets later. At the same time, innovation is moving us from an era of digitisation – services moving online – to a truly digital industry of artificial intelligence and machine learning, where new products find their way directly to the consumer, which can have both good and bad outcomes.

The new relationship we will have with the European Union when we leave may provide us with an opportunity to do things differently to ensure we are keeping pace with the changing landscape.

So, making regulation more simple, clear and effective is vital. Clearly, there is no straightforward solution. Any regulatory evolution must have the confidence and consent of everyone involved in financial services – including the general public. This is why we have an open invitation for thoughts and ideas.

Rules will always remain important. They are clear guides to what is expected. But wherever this conversation takes us, we know that our aim is to move from narrow compliance with rules, to a broader focus on delivering positive outcomes for users of financial services as well. What this will look like in practice will depend on a number of key factors.

Clearly stating what outcomes we want to see in markets will determine our approach and ensure we are held accountable. We need to consider how we can better use all the powers in our regulatory toolkit. Employing creativity, such as that found in the Senior Managers Regime, FCA Innovate and targeted use of price caps will build interventions around real consumer behaviours. This is a step away from more traditional tactics, such as a straightforward reliance on disclosure.

Recognising this changing context for regulation, we will harness technological innovation to enable truly digital services that meet the needs of both consumers and firms, and to enable us to do our jobs better and more efficiently. We will also be setting out our analysis of future market trends and our thoughts on long-standing issues, like the Duty of Care.

"Any regulatory evolution must have the confidence and consent of everyone involved in financial services – including the general public."

We have the opportunity to reshape financial services regulation in the UK. The FCA's responsibility to make markets work well, prevent harm and serve the public interest remains as important as ever. Building a more agile regulatory framework requires a bold approach and full use of the regulatory tools we have. Putting outcomes at the heart of the debate will ensure we serve the public interest now and in the long term. The world is changing and so must we. CB

BRIDGING THE GAP

Banking that wins with women

Could banks do more to cater for women's financial needs, both in business and retail?

Half the world's population is female and women's share of wealth, whether earned or inherited, is growing rapidly.

By 2020, women are expected to hold $72tn – 32% – of total global wealth, up from $34tn in 2010 and $51tn in 2015, according to management consultancy Boston Consulting Group.

Diversity is firmly on the agenda for financial services providers – demonstrated, not least, by new RBS Chief Executive Alison Rose becoming the first woman to lead one of Britain's major lenders.

But are banks doing enough to tailor their business and retail offerings to reflect the different risk appetites, biases and preferences of their female customers?

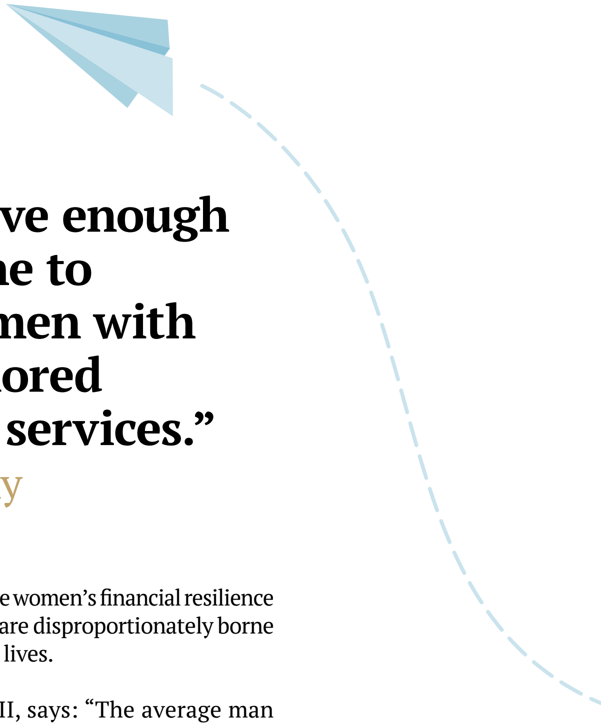
"Research indicates that women are less likely to invest their money than men – and are more averse to taking risks," says Joanne Murphy, Chief Operating Officer, Chartered Banker Institute.

"For some, this will actually just relate to the amount of free income available for investment. For those who do invest, this will influence what they invest in and how much they are willing to risk. Regardless of whether an individual is a corporate or personal customer, they have unique needs and the services they receive should be tailored appropriately to support their specific customer requirements."

Gender bias

Murphy believes banks are on the back foot in this regard and notes the recent case of apparent gender bias in Apple's new credit card, which appeared to offer significantly higher credit limits to men compared with women. Investment bank Goldman Sachs, which issues the card, responded that Apple Card credit decisions were made on an individual basis, based on factors such as personal credit scores, income level, and debt levels.

"I don't believe enough is being done to provide women with suitable tailored products or services," Murphy says. "More work is definitely needed in ensuring that



legacy data, reflective of the previous social norms, does not create future bias."

According to the United Nations, eliminating all types of female bias would increase the world's productivity by 40%, Murphy notes.

"The World Bank estimated in a recent survey that the loss in human capital wealth due to gender inequality is $160.2tn," she adds. "This is not surprising, given that women account for half of the world's population, and they tend to live longer than men.

"Engaging women and girls in finance and educational attainment is critical in ensuring their financial autonomy throughout life, and in turn the ability to achieve their potential. This is both a local and global issue."

Beating historical bias

Women are also far more likely to have serious debt problems in comparison to men, Murphy says. Pay equality would help close this gap.

"There are a number of great organisations and charities making progress and supporting women who find themselves in difficulty," she adds.

"Progress is also being made as more women attend university – and we can see the pay gap decreasing for qualified women at the beginning of their careers. But there's still a lot to do – particularly to tackle the motherhood and carer penalty that emerges mid-career."

Women have not been properly supported or represented across society – not just in banking, Murphy adds. Looking ahead, the industry needs to make sure historical bias does not transfer into the operating systems and machine learning of the future.

The good news is that banking is becoming more reflective of the society it serves, and this is a positive development for consumers.

Murphy says: "I hope creating a profession that has greater neurodiversity and role models will equally benefit individuals, consumers and shareholders – and create a socially responsible banking profession in future."

Financial resilience

Women typically have less financial resilience to bounce back from financial shocks due to the traditional societal pressures placed on them as carers and parents, according to the Chartered Insurance Institute (CII), which represents 127,000 members in the insurance and financial planning professions.

The CII's Insuring Women's Futures programme is a collaborative market-wide

"I don't believe enough is being done to provide women with suitable tailored products or services."
Joanne Murphy

initiative designed to improve women's financial resilience and highlight the risks that are disproportionately borne by women throughout their lives.

Sian Fisher, CEO of the CII, says: "The average man accumulates five times the pension pot of the average woman by the age of 65, with a man having £179,091 and a woman of the same age having just £35,800.

"For divorced women, the situation is considerably more precarious, with average pension pots worth a mere £9,019 compared with £30,341 for divorced men.

"Many decisions around retirement saving are made as a household, and women in long-term relationships may expect to share their partners' pension wealth.

"But our Insuring Women's Futures initiative has found these patterns of pension wealth leave women vulnerable in the event of a relationship breakdown and mean women are more likely to rely on a partner or the state for their income in old age – 48% of divorced women compared with 38% of divorced men."

Tailored support

The aim of Insuring Women's Futures is to refine how the insurance and personal finance professions approach women and risk. Specifically, how solutions, advice and services to enhance women's financial resilience in wider society could be improved. And how improved outcomes for women across all professions could be developed, in a gender-balanced way, through awareness and education.

"We know that women are under-engaged with insurance and personal finance, but there is not enough good information on the reasons why," Fisher continues. "Women's risks are a societal concern, and by improving women's financial resilience, we can help secure a better financial future for all. Government, regulators, businesses, employers, financial services firms, the third sector and society at large all have a role to play."

BRIDGING THE GAP

After engaging with Insuring Women's Futures, organisations including the Association of British Insurers, the British Insurance Brokers' Association, the Financial Conduct Authority, Citizens Advice and the Money and Pensions Service are being encouraged to adopt specific proposals, including supporting education, engagement and change to deliver improved outcomes.

The campaign's Market Task Force, a cohort of 15 senior executives from across the insurance and financial planning profession set up to prioritise and progress key actions, is looking at how the insurance and personal finance professions approach female consumers.

"Areas of focus include gender-neutral language in the law, and the collection and use of gender-disaggregated data in policymaking," Fisher explains. "We are looking at empowering women through tailored approaches to financial engagement, information and guidance, financial advice and customer approaches by the insurance profession.

"We want to improve inclusive customer approaches within insurance and personal finance."
Sian Fisher, CII

"Other key areas of focus include equality pensions measures to tackle the impacts of low pay and gender pay gaps, motherhood and caring, and relationship breakdowns. We want to improve inclusive customer approaches within insurance and personal finance. And we're looking at the role of employers in supporting financial and pensions well-being."

Key life stages

Insuring Women's Futures has proposed a series of potential interventions for the profession and policymakers to consider across six key life stages for women. Published in a new report, *Living a financially resilient life in the UK*, its proposals encourage collaboration between government, regulators, insurance employers and the third sector. They include professional standards and two new pledges in support of financially inclusive customer approaches, and financially flexible working, to which many leading brands have already signed up.

Government and regulators are encouraged to include employers' pension contributions on gender pay gap reporting and reform of earnings eligibility thresholds to automatic enrolment.

They are also encouraged to collect and use gender-aggregated data to inform supervision. The report also calls on the legal profession to make pension sharing the default position in divorce settlements. CB

To find out more about Insuring Women's Futures and how you can become involved in making a difference to this initiative, visit www.insuringwomensfutures.co.uk

WOMEN BORROW LESS – BUT COULD ACHIEVE MORE

On average, women launch their businesses with 53% less capital than men, according to the *Alison Rose Review of Female Entrepreneurship*, an independent review of female entrepreneurship led by the new RBS CEO and published by the Treasury in March 2019. It found that up to £250bn of additional value could be added to the UK economy if women started and scaled new businesses at the same rate as UK men.

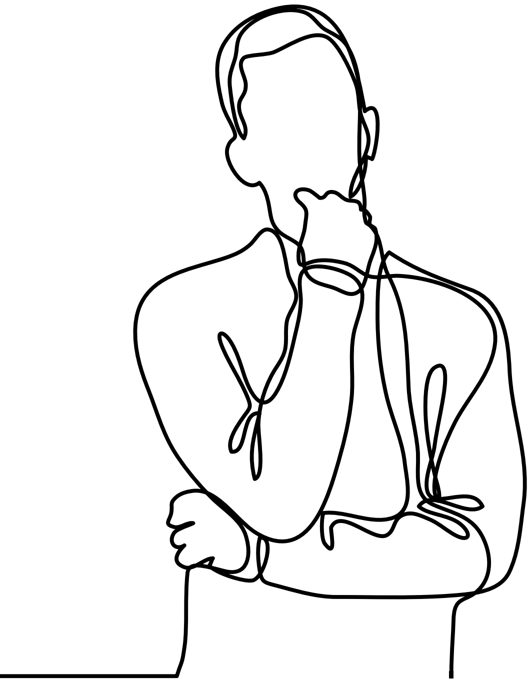
Attitude to risk was one of three interlinking cultural barriers identified. The Review states: "Women typically have higher risk-awareness than men and are more cautious about starting or scaling a business, limiting their willingness to risk their livelihood on an uncertain venture. In our survey, women were 55% more likely than men to cite fear of going it alone as a primary reason for not starting a business."

The Review's recommendations include launching a new Investing in Female Entrepreneurs Code that commits all financial institutions to the principles of gender equality and transparent reporting of gender funding data. Other recommendations include creating new investment vehicles to increase funding to female entrepreneurs and creating new banking products aimed at entrepreneurs with family care responsibilities.

Separate research in Scotland by RBS found more than half of women (52%) surveyed in an online poll had never asked for a pay rise. Four in 10 (37%) said they lacked the confidence to ever ask for a pay rise, and 22% said they didn't feel comfortable talking about money.

"Women were 55% more likely to cite fear of going it alone as a primary reason for not starting a business."

ACCESS TO CASH



The cash conundrum

The publication of two major reports has forced the global cash industry to reflect on its place in modern society. Tom Mitchell, Managing Director – Europe, Currency Research, considers its future.

The publication of two major reports – the independent *Access to Cash Review* and Currency Research's *Cash Industry in Transition* (CIIT) report, both in 2019 – set expectations for government, regulators and industry to act to ensure that the future of cash is not left to be determined by market forces.

But planning for a 'less-cash' society while also maintaining a robust cash industry is no easy feat. As former MP for Loughborough Nicky Morgan, then Chair, Treasury Select Committee, said when the final *Access to Cash Review* was launched: "Tinkering around the edges to preserve the status quo will not work. It's clear that something more fundamental is needed."

Key to the cash system's future is the role of the commercial banks as the traditional primary interface between its infrastructure and the public and whether, given fluctuating levels of cash use around the world, commercial banks serve as a help or hindrance to the continued availability of cash.

It varies greatly from country to country, but in its simplest form a country's cash system operates as follows:

1. The central bank creates banknotes and coins, or 'cash,' through state-owned or commercial printworks or mint
2. Commercial banks issue cash to consumers through branch and ATM networks and retailers
3. Cash in transit companies (CiT) take surplus cash deposited with, for example, retailers, for processing. This is performed by a cash management company (CMC), a commercial bank, or in some cases the central bank (most notably in Germany), which count and sort the cash prior to reissuance or destruction
4. Unfit notes are destroyed – usually by the central bank.

Supply and demand

On the creation/supply side, the currency suppliers have to some degree been a victim of their own success. The production of increasingly resilient banknotes and the advances in banknote security features that enable the banks to stay ahead of counterfeiters mean that notes last longer and need replacing less often. The lifespan of the US$1 note has increased from 22 months in 2010 to 71 months in 2017, for example. The Reserve Bank of Australia – the first central bank to make the switch to polymer currency – witnessed a reduction in unfit currency rates from 5.7% in 1992 to 1% in 1998 once polymer currency was introduced. With decreasing demand, the supply industry is under strain.

From the mid-1990s onwards the trend has been for central banks to outsource more of their cash operations

"The current challenge is to convince cash distributors of the benefits of investing in what appears to be a declining market."

to commercial companies in order to cut costs. While the overall supply and use of cash was increasing at this time, outsourcing was a win-win situation with central banks able to reduce costs, commercial operators able to grow revenue from cash-handling activities, and consumers having increased access to cash for their daily needs. The number of bank branches and ATMs soared.

But the 2008 financial crisis caused a wave of consolidation among banks, along with a focus on reducing costs. Internet banking was gaining momentum and banks began to see their bank branch numbers as excessive and costly. In the UK, the growth of cash in the system started to falter by about 2012, as a plethora of alternative payment systems gained traction with the public. Chief among the new payment options was Transport for London's introduction of the Oyster card, which brought the benefits of contactless payments to millions of people practically overnight. It is no surprise that the slowing growth and decline currently being witnessed in the UK's transactional cash use has coincided with the rapid increase in contactless technology.

Cash in circulation is still registering growth on a global basis. However, transactional cash use – the proportion of transactions that cash is used for – is decreasing globally, though it must be pointed out that some regions buck this trend, for example Southeast Asia and parts of Africa.

As transactional cash use stops growing, or even decreases, the per unit cost of maintaining its supply and distribution increases. Banks, for example, earn less from ATM interchange fees if fewer ATM withdrawals are being made. CiT companies run fewer trucks to retailers as consumers deposit (i.e. spend) less physical currency at retailers.

Why continue to invest?

This leads to the heart of the issue – in cash systems predominantly run by private/commercial companies, what incentive is there to continue? In most countries, at least for now, commercial banks are under no obligation to provide cash services and if they do not consider cash services a core or profitable activity, why should they continue to invest in them?

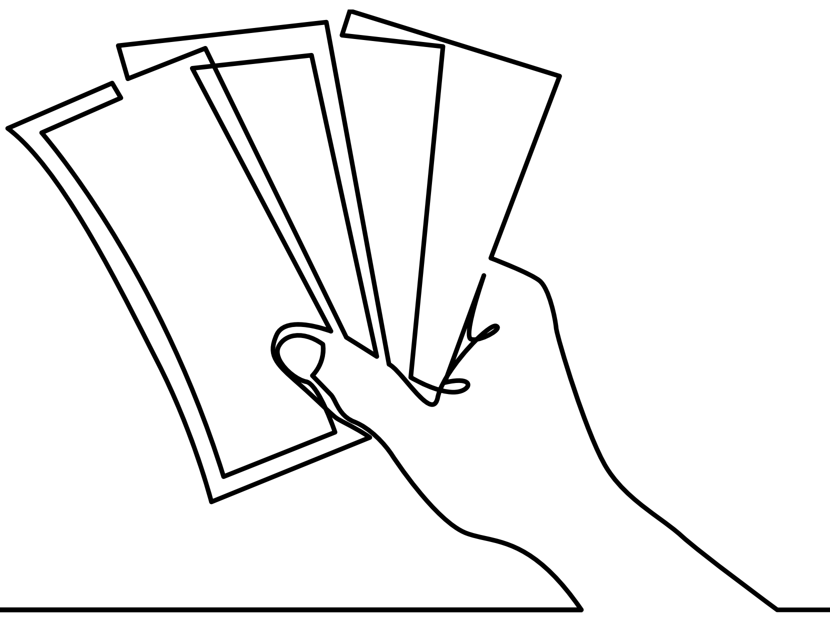
To cut costs, the banks started to reduce their branch and ATM networks and began actively promoting alternative means of payment such as contactless, mobile, and online. All of this made it harder for consumers to access cash. But as consumers turned to, and became more familiar with, alternative payment systems, so the demand for cash decreased – meaning its cost of provision then increased.

> **"Once cash use has declined to a certain level, the withdrawal of commercial operators and commercial distribution infrastructure becomes rather problematic to reverse."**

Cash has a number of inherent benefits that many alternative payment methods attempt to mimic, but have not yet been able to replicate. For example, cash is anonymous, and it's fast, ubiquitous, secure, inclusive, recognisable, trusted, and government backed. To compound the challenge for alternative payments players, there remain serious issues around financial inclusion. To a varying degree across the globe, people who fall outside of the formal financial system may have no other payment option aside from cash. According to the Financial Conduct Authority (FCA) in 2018, in the UK alone 1.3 million people were unbanked, with a much higher number being underbanked.

Short-term benefits

Despite the headlines, no clear link between changes in cash levels and fluctuations in crime or black market activities has been found, whereas seemingly every day we read about system outages affecting hundreds of thousands of customers at a time, national-level data



ACCESS TO CASH

"Until a payment system is able to replicate all of the inherent benefits of cash and be truly inclusive, cash is still the only feasible option."

hacking scandals, and ecurrency founders forgetting their passwords and losing their investors untold sums of money.

In the short term, declining transactional cash use does benefit some sectors. As banks withdraw from cash activities, the CMCs (which transport and process cash) pick up more business. Cash-handling equipment suppliers also do well, as those banks/CMCs remaining in the cash business strive to be as operationally efficient as possible. In another example, state printworks and mints are often required to operate due to political reasons (e.g. as a source of employment and national pride) and do not need to justify commercial returns to their shareholders. As such, they are able to switch to export markets and undercut the commercial industry. Consumers definitely benefit – cash remains available for those who want it, while alternative payments are innovating at breakneck speed for those preferring non-cash methods of payment.

Sleepwalking into risk

So, is there in fact a real problem here? Well – yes. The central bank has a responsibility to maintain stability and promote an efficient payment and settlement system. Until a payment system is able to replicate all of the inherent benefits of cash and be truly inclusive, cash is still the only feasible option. But, as transactional cash decreases, cash is becoming an increasingly less viable option if the cash system is outsourced.

Central banks are becoming increasingly aware of the problem and some in low-cash-use countries are now looking into ways to address these issues. As Sweden's Riksbank recently noted – the removal of much of the cash infrastructure has created a situation where the levels of cash use in Sweden are worrying low, and the sustainability of cash is at risk. The Riksbank, through its role at the top of the Swedish cash system hierarchy, had not intended to allow its cash system to get into such a precarious state, but ended up sleepwalking into a situation where millions of people could potentially be excluded from the economy, and could face increased risks of isolation, exploitation, debt, and rising costs. Remember – this is from Sweden, a country that for years has been at the forefront of promoting a cashless society and is one of the most technologically advanced and digitally inclusive economies in the world.

Is a legislative response required?

The *Access to Cash Review*, published in response to the rapid decline in cash use in the UK, addressed growing concerns that people who cannot use or access cash in an increasingly digital society are being left behind. The UK is certainly not alone in its concern about these issues. Many central banks around the world are launching working groups to investigate the same issues raised by the *Access to Cash Review*, which published five key recommendations:

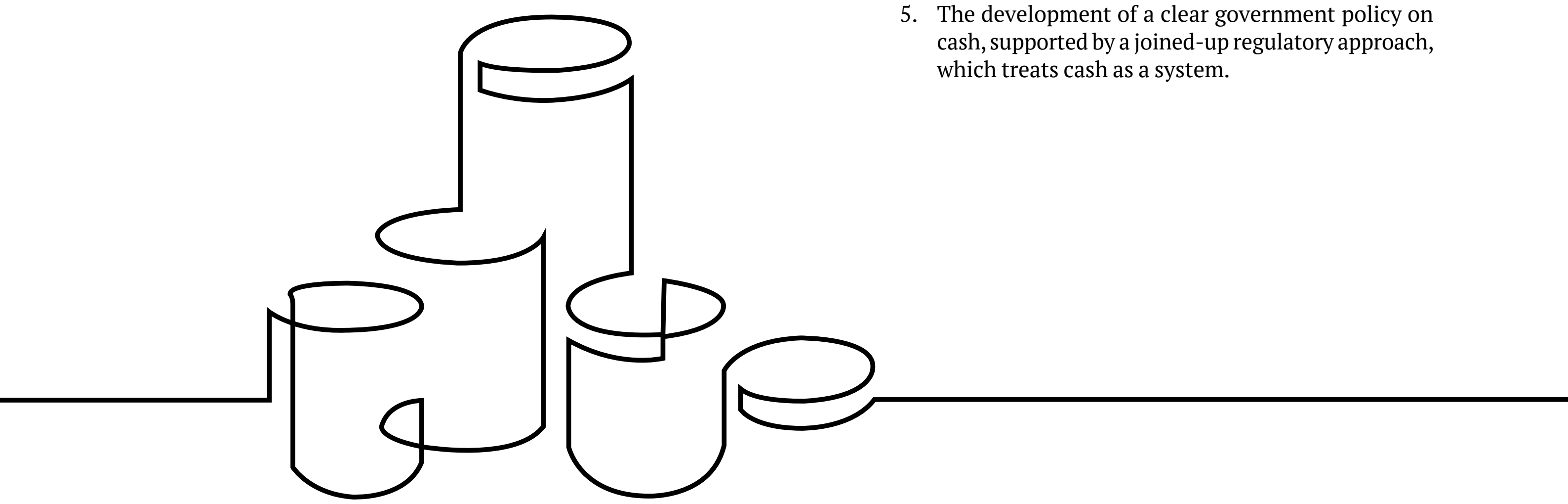
1. Guarantee consumer access to cash – ensuring that consumers can obtain cash wherever they live or work

2. Keep cash accepted, whether by a local coffee shop or a large utility provider

3. Call for radical change to the wholesale cash infrastructure, moving from a commercial model to more of a 'public good' approach

4. The government, regulators, and the industry need to make inclusion in payments a priority

5. The development of a clear government policy on cash, supported by a joined-up regulatory approach, which treats cash as a system.



The report rightly points out that increased political awareness of the situation is critical to ensure the longevity of cash as a product (at least until viable alternatives are in place). In the UK the Joint Authorities Cash Strategy (JACS) working group has been set up to look into these issues.

It is worth noting, however, that the cash supply industry has been aware of these issues for some time. Central banks have been debating the very concepts of money, settlement, and the definitions around legal tender and legal currency in order to make policy recommendations to governments. The low-cash-use Northern European central banks are probably most advanced in this respect.

"In most countries, at least for now, commercial banks are under no obligation to provide cash services."

Sweden and Norway are now considering whether a legislative response is required to force commercial banks to recommence cash activities – in Sweden,[1] a recent white paper indicated that, if enacted, this would also cover virtual banks. As mentioned earlier, this could prove costly for banks which have focused on reducing infrastructure in recent years.

Innovate to protect

While legislation and political interventions appear to concentrate more on the quantity and accessibility of cash, the industry is homing in on innovation to reduce the costs of cash, from more efficient processes in cash production through to network distribution and destruction. Many solutions offer ways to reduce the cost of cash, but the current challenge is to convince cash distributors of the benefits of investing in what appears to be a declining market.

Enough countries have fruitlessly attempted to move citizens away from cash for us to see that, at this time, it is very difficult to achieve a truly cashless society. Those countries that have seen some success in moving to cashless have been confronted with challenges, especially in terms of financial inclusion. Not to mention, once cash use has declined to a certain level, the withdrawal of commercial operators and commercial distribution infrastructure becomes rather problematic to reverse.

One thing is clear, efficiencies and communication at all levels is not only important, it is key to finding the solution. Central banks, commercial banks, CMC/CiTs, cash wholesale companies, and even retailers need to come together in an impartial environment to discuss the different ways in which they are each looking to address the problems of the cost of cash and maintaining its accessibility. The more communication between the parties that can happen, the better the solution for the general public. CB

The CIIT report is available for free download at currencyresearch.com/transition.
Currency Research is the world's resource for currency knowledge with a far-reaching network of cash and payments experts and professionals. It publishes the monthly digital publication, Central Bank Payments News, *and, in a joint venture,* Currency News, Cash & Payments News, *and* Mint News Quarterly.

THE EUROPE CASH CYCLE SEMINAR (ICCOS)

ICCOS is the leading global seminar for commercial cash management, distribution and circulation, bringing together all stakeholders in cash circulation to share perspectives, ideas, cost-saving technologies, strategies, best practices, and case studies for the betterment of the industry.

The event will be held on 16-18 March 2020 in Amsterdam.

Institute members can participate in the event at a discounted rate – please see charteredbanker.com/events for further details.

[1] Since time of writing the ECB has issued a legal opinion backing the draft law proposed by Sweden's government aimed at ensuring the country's banks make cash available to citizens. Further, the "ECB considers it important that all Member States, including non-euro area Member States, take appropriate measures to ensure that credit institutions and branches operating within their territories provide adequate access to cash services, in order to facilitate the continued use of cash". https://www.ecb.europa.eu/ecb/legal/pdf/en_con_2019_41_f_sign.pdf

COUNTRY SPOTLIGHT

Sweden's cashless revolution

The Scandinavian nation is tipped to be the first country to abandon notes and coins. Maintaining consumer trust is key to overcoming the challenges and maximising the opportunities this bold move could bring.

In the global march towards digital payments, Sweden is out in front. Only 13% of Swedes paid for their most recent purchase in cash, according to a 2018 report from the Riksbank, Sweden's central bank. This is down from 39% in 2010. The country has the lowest cash use of any advanced economy.

"In today's digital society, cash forms only about 2% of the total amount of money, virtually all the rest is electronic," says Hikmet Ego, Chief Executive and Co-founder of Northmill, a Swedish FinTech that was recently granted a banking licence by the country's financial regulator.

"Swedes are early adopters by nature, so development is driven to a great extent by users' ever-changing habits and expectations. This has been true also historically, for example with mobile phones and personal computers. As early adopters, we demand companies and the state to come up with cost-effective and user-friendly alternatives to cash."

One example is Swish, the digital payment app owned by the country's largest banks. It is used by 5.5 million Swedes – more than half of the country's population, and celebrated one billion transactions in 2019. The Stockholm-based point of sale specialist iZettle has disrupted retail payments globally with its mobile card readers. And Swedish neobank Klarna, which became the biggest FinTech in Europe last year, now has 60 million customers and 170,000 merchants in 17 countries using its 'buy now, pay later' app for online shopping.

> **"As cash use is declining so rapidly in Sweden, there is more pressure on us than on other countries to come to a conclusion."**
> Stefan Ingves,
> Governor, Riksbank

Northmill itself has 200,000 customers using its cloud-based credit and insurance products. These include Rebilla Reduce, which helps people lower their interest rate on existing lines of credit. Its banking licence will allow it to add savings accounts, cards, and payments transfer to its existing customer offering.

Trust in a digital age

How has consumer trust been maintained in this shift to a digital society?

"Swedes seem to trust these systems and solutions," Ego says. "The implementation and high adoption in Swedish society of electronic personal identification systems has enabled this innovation, because the infrastructure has been designed to provide counterparty trust."

Sweden's leading electronic identification system, called BankID, was launched in 2003 and today is used regularly by around eight million people for a wide range of private and public services.

"Swedes have in general a high level of trust in their authorities and institutions like banks, and consequently don't have any privacy issues with the traceability of digital payments," Ego continues. "This is not the case in many other European countries, where there is less trust in society, for historical reasons."

But the journey to becoming a cashless society will not be without its challenges. The rapid pace of change itself poses challenges from a regulatory and risk management perspective – meaning legislation and compliance frameworks must keep up.

"In Sweden, it is projected – very specifically – that as of 24 March 2023, it will no longer be economically defensible to use cash," Ego explains. "Thereby cash will not play any role in the payment system.

"A cashless society means that we face a new situation where payments and money accessible to the general public are issued and controlled by private companies. The Swedish government has recently indicated that, to handle this challenge and include everyone who, for one reason or another, can use only cash, new regulations may be put in place so that the private sector is forced to take greater responsibility."

Similar developments can be expected globally as cash is replaced by a 'more flexible, simple and digital way' of handling one's personal finances.

Supply and demand

The *Access to Cash Review*, which published its final report in March 2019 into rapidly declining cash use in the UK, noted that as few as one in five payments across Northern Europe was now in cash.

Cash use has fallen well below 50% in Sweden, Denmark, Finland, the Netherlands, Canada, France, and the United States.

"Around 20% of Swedish people say they never withdraw cash at all," states the *Review*, which was chaired by former Chief Financial Ombudsman, Natalie Ceeney CBE. "Approximately 900 of the 1,600 Swedish bank branches no longer distribute cash or accept cash deposits. This is worrying some people, though, and a national commission has been established to explore how to make sure people don't get left behind."

Insight from Sweden and China demonstrates that merchants and retailers no longer accepting cash was more likely to cause the death of cash than issues around cash access, the *Review* adds. Its research suggests the rising costs of handling and banking cash, driven in turn by the underlying economics of cash handling and distribution, were the main reasons behind merchants and retailers refusing to accept cash.

Mats Dillén, former Director-General of the National Institute of Economic Research, is head of the Riksbank Committee, the national commission set up to review Sweden's monetary policy. He said in 2018: "If this development with cash disappearing happens too fast, it can be difficult to maintain the infrastructure for handling cash ... one may get into a negative spiral which can threaten the cash infrastructure."

The Committee is proposing that all banks should be obliged to handle cash and that companies would be

"Another issue...is the robustness of the payment system in times of crisis and war."

Rickard Eriksson, Swedish Bankers' Association

COUNTRY SPOTLIGHT

able to deposit their daily cash takings in their bank accounts. Taking this a step further, the Riksbank proposes that banks should also be obliged to ensure that private individuals can make deposits.

Stefan Ingves, Governor, Riksbank, said: "The possibility to make deposits shall be included in the concept of cash services. This is a service that consumers can reasonably expect of banks."

Digital cash

Speaking in London in October 2019 to the Money Macro and Finance Research Group, the national study group for monetary economists, Ingves said of declining cash use: "This development is due to a combination of banks introducing new technology that is cheaper than handling cash and of most people in Sweden perceiving these solutions to be more convenient.

"But a drawback to this development is that if it continues, Sweden may find itself in a few years' time in a position where cash is no longer generally accepted by households and retailers. Technological development may, in other words, make physical banknotes irrelevant.

"This raises a number of fundamental issues about the payment system, which we have not previously needed to consider. If cash were to be completely phased out within a not-too-distant future, there would, basically for the first time in modern Swedish history, no longer be a means of payment whose value is guaranteed by the state, via the Riksbank. We would therefore face a situation where all means of payment available to the general public are issued by private actors, on a payment market that is highly concentrated. This could make it more difficult for the Riksbank to perform its remit of promoting a safe and efficient payment system."

In light of this, the Riksbank has been looking into the scope for issuing a new form of digital cash, the e-krona. Several so-called cryptocurrencies already exist globally and others are on the cusp of being introduced, such as Libra, the controversial blockchain digital currency scheduled to be launched by Facebook this year.

"The Riksbank is far from the only central bank looking at the issue of digital central bank money," Ingves said. "But as cash use is declining so rapidly in Sweden, there is more pressure on us than on other countries to come to a conclusion."

> **"I think cash will still be available, but just a very small amount."**
> Louise Grabo,
> Swedish FinTech Association

Future vision

When the current payment systems emerged in the late 1800s and the early 1900s, everything was on paper, which put a limit on how quickly payments could be made. In the future, we must assume that nothing will be on paper, Ingves told the Money Macro and Finance Research Group.

Setting out his vision for what Sweden's payment system should look like, he continued: "There should be a legal definition of what constitutes electronic legal tender and the e-krona, issued by the state via the Riksbank, should be such legal tender.

"It should also be possible 24/7/365 to make payments in real time in e-krona and in addition make at least smaller transactions between currencies. There should be an electronic state ID document that also defines who a person is in a legal sense, and if electronic systems were to fail, there must, as a contingency measure, be a sufficient amount of physical banknotes in different parts of the country."

Given the economic importance of this issue, the Riksbank cannot take the decision on its own as to whether an e-krona should be introduced and, if so, in what form, Ingves continued. Following a petition from the Riksbank to the Swedish parliament, the Swedish government has been preparing a public inquiry into the future payment market, which is expected to start work early this year.

The Swedish Bankers' Association, which represents banks and financial institutions established in the country, is calling for alternatives to the e-krona to be considered. Its concerns include accessibility and the need for a fallback system in the event of IT failure.

Summarising industry concerns in response to an interim report on the e-krona project, Rickard Eriksson, Analyst, The Swedish Bankers' Association, wrote on its website: "The Swedish Bankers' Association, wonders how the e-krona could make it easier for those including digital novices, persons with seriously impaired vision and persons with neurodevelopmental disorders.

"Another issue raised by many respondents is the robustness of the payment system in times of crisis and war. Several respondents note that increased robustness requires some form of parallelism to the existing payment system. Sparbankernas Riksförbund [a Swedish organisation of current and former savings banks] requests a description of the special arrangements that would be made to ensure that an e-krona would not fail when other payment systems fail."

New ecosystem

Louise Grabo, General Secretary, the Swedish FinTech Association, says: "The e-krona project by the Swedish Riksbank will take form and hopefully provide the citizen with a digital and secure currency in some manner. I think cash will still be available, but just a very small amount for the banks, customers and merchants. The state will make sure of this, even though the cost of providing cash will be even higher.

"From the Swedish FinTech Association's perspective, we hope the Riksbank can provide an open and inclusive financial infrastructure, so that even the small FinTechs can be part of the system, rather than it being just an infrastructure for the old banks."

Swedish people generally are positive about new digital solutions and adopt them quickly, Grabo adds.

"Trust in the government, the system, the banks and the authorities has made Swedish citizens even more positive about other services for payments, lending, and savings," she says.

FinTechs have disrupted the market, using technology to provide faster and cheaper services. The number of FinTechs in the Stockholm area has mushroomed from around 200 in 2017 to more than 400 in 2019.

"This increase in FinTechs has challenged the banks to be more effective and to push down the costs for customers," Grabo continues. "The banks are also investing in FinTechs and using their technical solutions to keep pace.

"Four out of five purchases in Sweden are made electronically, and Sweden's central bank, estimates that between 2012 and 2020, cash circulation will have declined by 20 to 50%."

For merchants, declining cash use has opened up new technical solutions including Bambora, the Swedish online payment processing business acquired by French payments specialist Ingenico for €1.5bn in 2017. For consumers, the move from cash to digital payments is also opening up more opportunities.

In contrast to the viewpoint of Northmill's Ego, Grabo believes financial scandals in Sweden's banking sector have damaged trust and helped to push consumers closer to FinTechs.

"Consumers want customised apps that are user-friendly without hidden fees – and as long as FinTechs can provide this, consumer trust in them will increase," she says. CB

SWEDEN IN NUMBERS

70%
of Swedes say they could live without cash

1661 Sweden's first bank, Stockholms Banco, issues the first banknotes in Europe

2023 Date by which Sweden could be cashless.

YOUNG BANKER OF THE YEAR

Where are they now?

Young Bankers of the Year from the past three decades share their stories – and messages for those thinking of entering the 2020 competition.

Since its launch in 1987, the Chartered Banker Institute's Young Banker of the Year competition has helped to showcase the talent and potential of more than 30 winning banking professionals and scores of finalists.

Ahead of the 2020 competition opening for entry, *Chartered Banker* caught up with three former Young Bankers from the 1990s, 2000s and the 2010s to find out what happened next in their careers, and how they feel today when looking back on their competition experience.

1994 YOUNG BANKER OF THE YEAR

Lynn McLeod, now Head of Learning and Assessment, Chartered Banker Institute

Lynn McLeod was a training officer for Bank of Scotland's direct banking division when she entered the Chartered Banker Institute's Young Banker of the Year competition in 1994.

She pitched a strategy for encouraging customer loyalty – and won – against 225 entries and five finalists.

"It was such an exciting development experience," says McLeod. "To win the competition, and also the award for the best presentation, was amazing. I enjoyed everything about the whole process – shaping my thoughts, writing papers, and presenting my ideas at the final."

The 1990s was a boom time for call centres and it was her prize as 1994 Young Banker of the Year that had the most lasting effect on McLeod's career.

"The prize was two weeks in the US, including visits to showcase call centres at Citizens Bank, Texas Commerce Bank and MCI Telecommunications," McLeod explains. "All three call centres were fantastic. During the prize trip, I learned about best practice in call centre design and operations, the technology used, culture and management style, training and coaching, performance standards, assessments and rewards."

Career progress

While McLeod didn't directly develop her winning idea after the competition, she did progress what she had learned in the US about contact centre operations, service standards and coaching.

"I really did catch the coaching bug," McLeod says. "I took a break for maternity leave and when I came back, I became the call centre quality manager. It was then that I implemented call standards and a structured coaching and benchmarking programme that improved call quality, colleague capability and customer service. After that, I continued to develop this work, because I then spent three years as operations manager in the call centre."

McLeod's passion has always been education and learning. After graduating from the University of Edinburgh in 1984 with a Bachelor's degree in Education, she had planned to become a teacher.

"I joined Bank of Scotland in 1984 as a student for the summer and I was offered a permanent job," she explains. "I could see opportunities for education and training in the bank, so I decided to stay."

During a 21-year career with Bank of Scotland, she had a diverse range of roles, including operational and HR management, and leadership development. She later ran her own leadership coaching and training consultancy for six years, specialising in executive

“Go for it! The world of banking needs people like you and your amazing, innovative ideas!”

Lynn McLeod

coaching, management development and coaching skills training, primarily in the education sector.

Institute insider

In 2011, McLeod joined the Chartered Banker Institute as Curriculum Support and Accreditation Manager, a qualifications development role. In her current role as Head of Learning and Assessment, she is responsible for leading and developing the Institute's newly formed learning and assessment hub.

“The Chartered Banker Institute has been extremely important throughout my career,” McLeod says. “I've been a member of the Institute since 1985, when I signed up to do my bank exams. I qualified in 1989, and in 2000 I received my Fellowship from the Institute.

“Between 1996 and 2011, when I joined the Institute as an employee, I worked with the Institute in a variety of ways. I was an examiner, verifier, tutor and author. I ran revision days for students and designed and delivered personal and professional development workshops for members' continuing professional development. I was also a volunteer for the Institute's Financial Education Partnership [an initiative promoting financial education and employability skills].”

McLeod's passion for learning has led to a string of qualifications, including an Advanced Certificate in Executive Coaching and an MSc in coaching from Edinburgh Napier University.

How important is education and training in banking?

“It's absolutely critical,” McLeod says. “Being professionally qualified and a member of a professional body helps us develop and demonstrate the high standards of professional competence that our organisations, customers and regulators expect.”

McLeod's message to future Young Banker of the Year entrants is: “Go for it! The world of banking needs people like you and your amazing, innovative ideas!”

CAREER OVERVIEW

1984	Bachelor of Education, University of Edinburgh and qualified teacher
1993	Centrebank Training Officer, Training and Staff Development Department, Bank of Scotland
1994	Winner, Young Banker of the Year
2000	Associate Director, Human Resources, Bank of Scotland
2000	Fellow, Chartered Banker Institute
2002	Leadership Development Consultant, HBOS
2010	Manager, National Qualifications, Scottish Qualifications Authority
2019	Head of Learning and Assessment, Chartered Banker Institute

YOUNG BANKER OF THE YEAR

2005 YOUNG BANKER OF THE YEAR

Audrey Connolly, now Head of PPI Programme, Lloyds Banking Group

Collaboration and co-operation across different banking areas has been an enduring theme of Audrey Connolly's career and was at the heart of her winning Young Banker of the Year pitch in 2005.

"It was, in essence, about how you could use the power and the strength of the whole organisation working collaboratively to support customers, rather than people working in silos," says Connolly, who is now Head of Payment Protection Insurance (PPI) Programme at Lloyds Banking Group.

"I recognised these big organisations have lots of different departments and front and back offices that don't generally talk to each other. For example, a customer might talk to someone in a branch who doesn't know anything about their insurance relationship with the business. So the organisation's not working at its full power and the customers aren't getting that cohesive sense of relationship with the bank. It was about how you would get better at doing that in the future, and how that would bring power to the relationship."

Managing change

Connolly has spent much of her career solving problems and was Programme Director for a change project at National Australia Group when she entered the competition.

"I've worked in retail, commercial, projects and strategy and I've run operations, so I've had a unique career journey that's allowed me to cross boundaries," she says. "That meant I was able to reach across the water to other departments and use my network, bring people together, have those joint conversations and get better outcomes, because I had seen all these areas in action."

After using her Young Banker of the Year prize money for a transatlantic flight to run in the 2006 New York Marathon, Connolly moved to Halifax Bank of Scotland as head of its commercial real estate business. After the merger with Lloyds Banking Group, she took on potentially the biggest challenge of her career, as Head of PPI Operations.

"I was responsible for effectively building the PPI operation that dealt with the PPI crisis in 2011," Connolly explains. "At one point I was looking after 3,000-plus people and dealing with a very difficult challenge, with lots of customer expectations and a lot of regulatory scrutiny. So it was a massive learning curve, and a huge development opportunity for me to do that. I'm now working in the programme that is going to turn off the lights on PPI at some point in the future, which is brilliant, because I get to see it from beginning to end."

Diversity and inclusion

Connolly is also a diversity champion and runs the bank's Rainbow Network, which looks after LGBT+ colleagues. Diversity and inclusion has been a key theme for the Chartered Banker Institute, she adds, alongside green finance and ethical banking.

"It shows you're committed to your development and your career – and it gives you exposure to wider industry thinking."

Audrey Connolly

"I love the way the Institute is at that bleeding edge of thinking," she says. "It's not just about numbers and pound signs, it's actually about that cultural journey, which is fantastic.

"Giving back to the younger generation coming into the industry is also important and is something the Institute supports."

Her message to future Young Bankers?

"I think it's a great learning experience. It shows you're committed to your development and your career – and it gives you exposure to wider industry thinking."

CAREER OVERVIEW

1990	Master of Arts, University of Glasgow
1993	Qualifies as Chartered Banker
1999	Business Development Manager, Group Collections, National Australia Group
2005	Winner, Young Banker of the Year
2019	Head of PPI Programme, Lloyds Banking Group

2014 YOUNG BANKER OF THE YEAR

Jamie Broadbent, now Head of Digital and Innovation, RBS International

For Jamie Broadbent, winning the 2014 Young Banker of the Year competition immediately showcased him as a rising star within RBS.

"Literally the day after the competition, I was getting emails from some of the great and the good of RBS to congratulate me and invite me to come in and talk them through what I'd done and what my plans were for the next step in my career," says Broadbent, who was a Customer Proposition Manager at the time in the bank's UK business banking operation.

"After I won, I had the opportunity to share my winning entry with our then Chief Executive, Ross McEwan, and also the chief executive of both the retail and the commercial banks. That was Les Matheson and Alison Rose, respectively, at the time. What it did almost immediately was open a lot of doors with our senior executives, which was really quite an awesome experience."

Future challenge

The theme of the 2014 competition was: How would you shape the future of banking? Proposals had to be aimed at improving outcomes for customers, colleagues, communities or the company they worked for.

Broadbent's idea involved creating an online portal to help businesses find funding after being turned down for lending by banks. His proposal involved connecting small businesses with funding needs to local crowdfunding communities that he called Local Investment Opportunity Networks (LIONs).

"My idea was effectively a peer-to-peer lending platform that looked at how to deliver much-needed capital to small businesses, but funded by people in their local community," Broadbent explains. "It was the opportunity to support businesses both financially, but also by getting its funders to become customers and advocates of that business.

"At the time I was working in our business banking segment and was familiar with the challenges that early-stage businesses have with accessing funding. The bank isn't always well placed to lend to early-stage businesses, and so this was a proposition to potentially help plug some of that gap."

Getting noticed

In the audience at the 2014 Young Banker of the Year Awards was RBS Director of Communications and Chief Economist Dr Andrew McLaughlin. He was shortly after appointed CEO of RBS International, the bank's international division. Following a meeting with Broadbent, he offered him a job.

"That was game-changing in terms of giving me the next steps on the career ladder," Broadbent says. "My role today is heading up both digital and innovation for the international part of the bank. Effectively, I'm the business owner for all of our customer-facing digital channels – mobile banking, online banking and our corporate banking platform. I have the responsibility for driving the innovation agenda of RBS International, which means being an enabler for colleagues to become more innovative, using new and different technology to do better things for customers."

Moving to Jersey from Edinburgh has also been life-changing for Broadbent and his family.

"I have a young family and they absolutely love it here," he says. "You're never more than 10 minutes away from a beach. It's safe. The schools are good. You can see France on a clear day. It's just a really great place to live and to have this next chapter of my career."

Lasting support

Broadbent received his Professional Banker Diploma in 2014 from the Chartered Banker Institute, which he says has been a lasting source of both support and friendships.

"People look to the Institute as a recognised standard within our industry," he adds. "It's great to be able to point to your qualification and say, 'Look, I'm a professional within my industry who can demonstrate having met certain standards.' For me, that's been really important.

"I would definitely encourage anybody to enter Young Banker of the Year competition. It's a great platform for you to develop the skill of taking an idea from inception, through to a robust concept that you can pitch and present.

"It's also a great opportunity to raise your personal profile and gain exposure to a very senior audience within your organisation – and across the wider industry." CB

> **"Literally the day after the competition, I was getting emails from the great and the good."**
> Jamie Broadbent

CAREER OVERVIEW

2008	BA (Hons) International Business, Sheffield Hallam University
2008	Joins RBS Business Leadership Graduate Programme
2014	Winner, Young Banker of the Year
2014	Professional Banker Diploma, Chartered Banker Institute
2017	Head of Customer Experience and Digital, RBS International
2019	Head of Digital and Innovation, RBS International

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NEGATIVE RATES

The perils of dropping below zero

Negative interest rates have been introduced in Europe and Japan to stimulate flagging economies. But is the policy doing more harm than good?

Danish Jyske Bank became the first to offer a negative interest rate mortgage in August 2019, reducing individuals' debt each month by more than the amount they pay.

Weeks later, the bank also announced a negative deposit rate. But even with nominal rates, its mortgage customers are likely pay back a little more than they borrowed in the end, once fees and charges are accounted for.

Meanwhile, questions continue to grow about whether the downsides outweigh the positives, with critics arguing that the negative rate environment is discouraging Eurozone banks from lending and motivating them to hoard physical cash – the opposite of the policy's intended effect.

With the European Central Bank announcing a further 10 basis point cut in its deposit rate to a record low of minus 0.50% in September, what does this policy mean – and what potential long-term impacts could there be for individuals, banks and the economy?

Crisis response

"The history of negative interest rates is recent and stems from policymakers' attempts to boost stagnant economies after the global financial crisis of 2008-09," explains Professor Philip Molyneux, a banking research specialist and Dean of the College of Business Administration at the University of Sharjah in the United Arab Emirates and Emeritus Professor at Bangor University in Wales.

"In order to have an expansionary monetary policy, central banks initially reduced interest rates sharply. Lower policy rates trickle through the financial system, reducing lending rates and therefore encouraging borrowing and spending. Lower rates are also expected to boost investment.

"However, when rates approached zero without there being the hoped-for recovery, various central banks experimented with a range of unconventional monetary policies to provide further stimulus. These included large-scale asset purchases to raise asset prices and increase the supply of bank reserves; targeted asset purchases to alter the relative prices of different assets, and forward guidance to communicate about future policy rate paths."

The effectiveness of these policies in boosting economies was also somewhat limited, Molyneux says. As such, since 2012, six European economies – Denmark, the Eurozone, Hungary, Norway, Sweden and Switzerland – and Japan have taken monetary policy a step further by introducing a negative interest rate policy.

How negative rates work – and the risks

"What this means is that banks are charged interest for holding excess reserves at the central bank – the aim is to encourage banks not to hold these excess reserves and to take these back onto their balance sheets and lend out," Molyneux explains.

> **"Ultimately the aim is to force banks to lend more than they otherwise would do if rates were zero or slightly positive."**

"Ultimately the aim is to force banks to lend more than they otherwise would do if rates were zero or slightly positive. Also, lower lending rates should encourage customers to borrow more. From a broader economic perspective, the main policy aims are to support economic growth and stabilise inflation expectations. In Denmark and Switzerland, the policy was also aimed at discouraging capital inflows to reduce exchange rate appreciation pressures."

Support for the real economy was expected to come from a greater supply and demand for loans, with loan supply increasing as banks ran down their (large) excess reserve balances, and loan demand increasing in response to falls in lending rates.

NEGATIVE RATES

Negative rate policy fuelled debate on the likelihood of its success in boosting growth and, also, how it would impact on bank behaviour.

Trouble ahead

“Sceptics at the time pointed to several possible complications,” Molyneux continues. “One possible restriction relates to the limited pass-through of negative rates to lending and deposit rates. Banks may be reluctant to charge negative rates on deposits, as this may encourage significant deposit withdrawals – if customers are effectively charged for holding deposits in a bank.

“And if deposit rates for bank customers are capped at zero, the negative policy rate likely will encourage loan rates to fall more than the deposit rate. This will squeeze margins – making it less attractive for banks to lend and reducing their overall performance.

“Negative loan rates would mean that banks would have to pay borrowers to take on credit – hardly an attractive commercial proposition for bankers. Negative rates can have other associated distortions in asset valuations that can create asset price bubbles, threatening stability.”

Voting with their feet

For bank customers, negative policy rates are expected to feed through into lower lending and deposit rates. But banks don’t want to start charging their customers, for fear of withdrawals and other linked reputational factors – and this is what has happened.

“Negative loan rates would mean that banks would have to pay borrowers to take on credit – hardly an attractive commercial proposition for bankers.”

“Banks can’t depend on the loyalty of their depositors if they start asking them to pay for the privilege of holding their deposits,” Molyneux says. “As a result, banks don’t reduce their lending rates as much as they probably should, because they want to do their best to maintain margins. So lending rates to customers don’t fall as much as policymakers believed would be the case.

“Also, if margins are squeezed, banks look to do their best to maintain profits by increasing fees (non-interest income). There is evidence that this has also occurred. The low interest rate environment in general also encourages bank customers to look to minimise deposit holdings and to seek higher returns from elsewhere – either in the stock market, housing or other forms of investment.”

What happens when deposit and loan rates go negative?

When Jyske Bank’s mortgage tracker went negative, it was in response to the official Danish rate dropping to minus 0.75%. Customers will still pay fees. The Danish bank also announced it would charge negative rates to its corporate and private clients – those with more than DKK750,000 (at the time US$11,100) – from 1 September 2019.

“It had initially said it would charge minus 0.6%, but the rate increased after an official policy rate change,” Molyneux explains. “Interestingly, Jyske Bank’s main competitor [Den Danske] announced at the same time it had no intention of introducing negative deposit rates.

“A similar move has recently been announced by the Swiss bank, UBS, which has said it will introduce a negative rate on deposits of more than CHF2m [around US$2m]. The main expectation is these negative rates on deposits are being targeted at wealthier clients, many of whom will move their funds to other banks that charge no negative rates.

“One can see that banks are implementing negative deposit rates selectively and not applying this to their overall depositor base, for fear of mass withdrawals.”

In such a challenging market, this does mean that banks have to become more dependent on revenue from non-interest sources, Molyneux says. Consequently, fees and commission on banking and other financial services will increase.

“This will range from increased fees on accounts, transaction services, insurance products and so on – across the board,” he adds. “The extent to which prices can be increased of course depends on the economics of particular fee and service-based markets, some being more competitive than others. But banks operating in a negative rate, or very low rate, will have to do something to maintain profits, and increasing fees will be an important feature.”

Long-term impact for individuals, banks and the economy

Individuals have long been used to a low interest rate environment, characterised by historically low borrowing and deposit rates. Typically deposit rates are ‘stickier’ downwards than borrowing rates and up until very recently, as in the Danish and Swiss cases noted earlier, negative rates have not been imposed on retail banking products.

“It’s important to note that the spectre of negative rates in the UK has diminished as the official base rate has increased from the 0.25% between 2009 and 2017 to 0.75% today,” Molyneux continues. “In 2016, according to the Bank of England, you could get a two-year fixed-rate mortgage with a 65% loan to value from HSBC with an interest rate of 0.99%. But now, with the increase in base rate, it’s around 1.79%. So interest rates are – as monetary economists say – normalising in the UK.

"The spectre of negative rates in the UK has diminished as the official base rate has increased from 0.25% between 2009 and 2017 to 0.75% today."

"A similar pattern has been occurring in the US, where rates have increased from historically low levels in 2016 [although they have fallen from 2.25% in December 2018 to 1.75% today].

"In the euro area, Denmark, Switzerland and Japan, rates are still at record low levels and plunging into negative territory with no strong signs of 'normalisation'. In these countries and regions, the likelihood of negative rates on banking products is looking more likely – unless growth turns around quite rapidly. It is much less likely in the UK."

More studies needed

Evidence on the impact of a negative interest rate policy on banks and the economy has up until recently been somewhat scant, Molyneux adds. Two recent papers by academics at the universities of Bangor, Bath and Sharjah provide a telling insight into the influence of negative rates on bank performance and lending behaviour.

One study investigates the influence of negative interest rate policy on bank margins and profitability, and identifies country- and bank-specific features that amplify or ease the effect of the negative rate policy on bank performance.

"Using a sample comprising 7,352 banks from 33 OECD member countries between 2012-2016, they find that bank margins and profits fell in countries that adopted the negative rate policy, compared to those negative rates," Molyneux explains. "This adverse effect appears to have been stronger for small banks as well as for those with limited fee income business, and also for mortgage specialists.

"The adverse impact on bank performance was also greater in countries where floating – as opposed to fixed – lending rates predominate."

In a follow-up paper, the authors use a similar large sample of banks and countries to investigate if lending increased – a main aim of the negative rate policy. They conclude that bank lending fared worse in negative rate countries.

"Specifically, countries where central banks implemented negative interest rate policy experienced a decline in total bank lending relative to those countries in which central banks did not follow this policy," Molyneux explains. "This result holds for total bank lending as well as for mortgage and commercial lending. In fact, the study finds that other forms of monetary policy actions, like quantitative easing, are better at boosting lending than the negative rate policy. The results also confirm that various factors, such as the capital strength and interest rate exposure of banks, reduce the willingness of banks to lend in a negative interest rate setting."

Overall, negative interest rate policy is unlikely to have a positive impact on banks and the economy, Molyneux concludes. It may have a positive impact on borrowers though, if banks have to pay borrowers to take on credit.

"But here the benefits likely will be very small, as banks will increase fees and commissions to make up for squeezed margins," he adds. "Overall, the authorities should look to alternative monetary policy to help boost failing economies – such as large-scale asset purchases and other liquidity injections – if they wish to boost lending in the future. It seems nobody really wins from a negative rate policy." CB

BANGOR BUSINESS SCHOOL

Has investment in regulation paid off?

Since the global financial crisis began to appear in 2007, there have been widespread public calls to strengthen the regulation of financial markets. John Ashton, Professor of Banking at Bangor University, analyses whether the resulting abundance of fresh directives went far enough.

The financial crisis triggered a colossal increase in spending on financial regulation across the globe. For example, the net costs of the UK's principal financial regulator – the Financial Services Authority until 2013, and then the Financial Conduct Authority (FCA) – rose impressively from £115m in 1999 to around £588m in 2019.

This heightened spending has been aligned with greater, and often stricter, regulatory activity. The level of fines levied on firms has sharply escalated in the past 20 years, particularly after the financial crisis. Between 2011 and 2014 alone, more than £38bn was raised in fines and remediation in the UK, a figure that equates to more than half of all bank profits.

A wide range of regulatory punishments, from variations of regulatory permissions to public sanctions, have also been liberally imposed. This has caused concerns because this level of regulatory activity can clearly reduce firm valuations and place an inordinate and unfair cost on shareholders rather than on those persons responsible for sub-optimal behaviours.

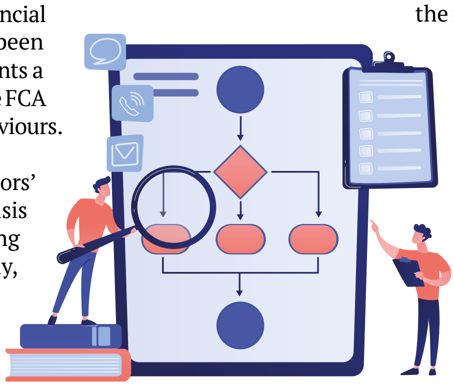
An improved environment?

After such sweeping changes to financial regulation, it is important to ask whether this increase in the costs, severity and frequency, and the associated rise in punishments, has improved the conduct of financial services firms.

Critically, it's important to ask whether all this fresh regulation is reducing the number of offences committed by financial firms in an effective manner, and whether it's deterring future offending. Answering these questions is not as easy as one would think.

While we know the proportion of regulated financial firms brought to book by the regulator has been dropping since 2010, it is unclear if this represents a decline in the number of firms offending or if the FCA is simply catching fewer firms for aberrant behaviours.

On the one hand, it could be argued that regulators' actions in the immediate years following the crisis has deterred future offending, thereby reducing the number of transgressing firms. Alternatively, others would contend that the diminishing proportion of offenders is because of a weaker enforcement environment. Both explanations are plausible, but whereas the former outcome would attract wide-ranging praise, the latter would be highly undesirable.



The increased enforcement of financial regulation can be, and previously has been, interpreted as evidence both of more active and successful regulators and also of their failure for 'allowing' more transgressions to occur. Clearly, this creates a paradox of criticism faced by regulators – they're either undertaking too little or too much action simultaneously, and it requires further investigation.

Central to solving such a problem and comprehending the extent and scope of all financial wrongdoing is the 'partial observability' problem', whereby one only ever observes the wrongdoers who are detected by the regulators and other apposite authorities. Headline figures of the number of firms and individuals caught, prosecuted or issued with final regulatory notices therefore tells us little about the actual number of offenders.

Detecting the undetected

Our work at Bangor University, through a collaboration with colleagues from the University of East Anglia, Warwick University and the University of Otago in New Zealand, has been trying to untangle these two effects of detection and deterrence. This is a non-trivial exercise because we're trying to measure something that is partially unobserved – i.e. the level of offending that is not observed or caught.

To do this, we used a simple logic. We observe that the proportion of offenders is declining. If we can establish that the rate of detection has not dropped, this would be a sign of increased deterrence. As a simple example, if you know that you always detain at least 20% of all offenders, but the numbers of caught offenders' drops from 30 to 20, then it must mean fewer offenders exist. Estimating how and if the rate of detection has changed, is however, not an obvious undertaking.

To do this, we summon an unorthodox capture-recapture method. This technique is both frequently used and well established in ecology to estimate population parameters of various species.

When wildlife researchers want to estimate the population size of a given species, they don't need to capture all the existing animals. It is sufficient to tag a proportion of this animal population and release them back into the wild. This process is repeated with a second, third and fourth sample of captured animals tagged and released. In this recurring process the proportion of tagged animals which are recaptured provides an estimator from which the proportion of all tagged animals within the whole population can be derived.

Although this is an extreme simplification of what has been performed in our work, we analogously apply a variation of capture-recapture methods for financial firms. The regulator catching offending financial firms is the equivalent of trapping animals and each year considered to be a new trapping event. The proportion of firms caught repeatedly is akin to animals being captured and tagged, providing a basis to estimate the overall proportion of firms breaching financial regulations. From this we can infer the probability of catching offenders in each year.

Of course, financial firms might be expected to be even more astute than wildlife when it comes to avoiding traps. Subsequently, these sampling procedures are unlikely to be random and the samples taken each year will probably not be independent. We also account for these issues by using multiple variations of capture-recapture methods to show that detection rates have not dropped, implying (because the number of cases declined) that relatively fewer offences are committed.

From this assessment it is recorded that around only a quarter of UK financial offenders seem ever to be caught. While this may appear to be a low figure, this indicates there has been a significant enhancement of detection rates in the UK. This improvement in detection is associated with both the improved ability to detect mis-selling and fraudulent behaviour and the increased punishments and costs of committing financial crimes.

In summary, we provide evidence that the UK financial regulatory system is not doing badly. The increase in regulatory deterrence observed indicates that some of the many changes seen in the past decade have had a positive influence in constraining financial offending. Of course, moving beyond detection and determining why UK financial firms choose to offend less is an important area for future research. CB

About the author

John Ashton is a Professor of Banking at Bangor University, the Programme Director of the Chartered Banker MBA, Editor of the Journal of Financial Regulation and Compliance *and acts as Chair of the British Accounting and Finance Association group on Financial Markets and Institutions. John has published widely on banking and regulatory matters, has undertaken work for regulators in the UK and internationally and is currently a member of the Competition and Markets Authority academic panel.*

Reference: Working paper: John Kevin Ashton, Tim Burnett, Ivan Diaz-Rainey and Peter L. Ormosi, (2018). *Has the Financial Regulatory Environment Improved in the UK? A Capture-Recapture Approach to Estimate Detection and Deterrence*, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3176993

PERSONAL DEVELOPMENT

Scepticism – a positive or negative quality?

A small business has a strong set of figures and proven revenue potential, so surely an approved lending application is a given. But there is far more to consider than just a healthy bottom line.

The scenario

Samantha is a bright young entrepreneur. She formed a limited company three years ago, offering IT services to small and medium-sized enterprises as well as some large companies. Having been employed by a major multinational company for 10 years, she was confident she could make a success of her new business.

She spent much of her first year visiting potential clients and securing consulting work. The first year yielded a small profit, but in the second year her commercial turnover increased significantly, with profits growing by 80%. Her third year was even better, as her turnover doubled and the company profits increased by 40%. Much of her company's business came from three big IT project contracts.

Aware that nothing lasts indefinitely, Samantha felt she needed to invest in marketing to generate future business. She produced a business plan and projections and applied to her bank for working capital to fund a marketing campaign. Samantha had banked with them since leaving university and had an impeccable credit history, so she believed her application for credit would be successful.

To her dismay, Samantha's detailed proposal was declined. She was told that while the growth and profitability of the business was impressive, there was simply not enough evidence that the business was sustainable in anything but the short term.

"In carrying out their roles as professionals, bankers have to be sceptical."

Samantha was disappointed. She had invested a lot of time in preparing her proposal. She had also provided two years' accounts prepared by a qualified accountant and had obtained confirmation from HMRC that her income tax and corporation tax liabilities were paid in full and on time in each of the previous accounting periods. Samantha also provided evidence from her two main clients that they could guarantee income from them for at least the next 18 months. She believed this was as good a guarantee of future income as anything that could be provided by an employed person.

The bank's small business adviser explained it was quite common for the bank to take a conservative attitude to credit applications from small businesses, due to their high failure rate. The adviser added the bank had evidence that more than 70% of new businesses failed in the first five years, although many entrepreneurs didn't become insolvent and merely returned to the salaried workforce instead.

Samantha felt bitter that the bank would not support her aspirations. Her father had told her that his business had survived its early difficult years in the 1980s by being able to rely on an unsecured overdraft, which the bank increased several times without being asked. Samantha concluded that the only way forward was to apply for funding from elsewhere. She secured a loan from a finance company, reluctantly paying a significantly higher rate of interest than her bank would have charged.

What fundamental ethical principles are demonstrated by this case? By working through this scenario and developing your own solution before reading the author's analysis, you may claim up to one hour towards the professionalism and ethics component of the Institute's CPD scheme.

The analysis

Samantha's story is a common one that could be retold by many small business entrepreneurs in the wake of the global financial crisis. At that time, banks became more risk averse. As a result individuals and businesses, once able to routinely secure new lines of credit or increase borrowings, now found it difficult or even impossible to obtain new funding. There are several ethical implications of this.

The bank has been honest. Lending is a risk business and experienced bankers will confirm there is no such thing as a good loan, only a good risk. Every bank has experienced defaults on loans that were considered to be very low risk, often taken out by people and businesses of the highest integrity. Conversely, the same banks will be able to recall instances when their lending officials have gone 'out on a limb' to sanction higher-risk loans, but the borrowers have gone on to become millionaires. This writer was once a member of a credit committee which declined an application to fund the development of a 'teabag squeezer' because it was considered to be too eccentric and too high a risk, only to find that the applicant borrowed from elsewhere and sold his invention to three multinational teabag producers.

Samantha has every right to be disappointed, but the bank has explained its reasons and if it has taken the decision objectively, based on the evidence before it, then it has acted correctly.

Scepticism is rarely included in a list of fundamental principles, but is now increasingly recognised as an essential quality of a professional person. At face value, scepticism appears to be a quality that is negative in nature. It implies adopting a questioning mind, or a disbelieving attitude. By being sceptical, a banker is not prepared to take information at face value. Samantha's projections, for example, are little more than a 'wish list', and may be based on assumptions, however well formulated, rather than concrete facts. But is there a contradiction here? To be regarded as ethical, we are encouraged to trust and respect others. So if we are not prepared to trust their word or the information and supporting evidence provided, does this not suggest that we are mistrustful of others, or worse still, not showing them the appropriate respect?

In carrying out their roles as professionals, bankers have to be sceptical. Successful business people, and a good many unsuccessful ones, will have supreme confidence in their own ability. To many of those with a new vision or concept, their idea is the 'child of their mind', to be nurtured and developed for their own benefit and often for that of society. However, Samantha's adviser is right. Many businesses do fail, sometimes despite the incredible amount of time and energy invested in them.

One of the keys to this case scenario is the fact that Samantha is involved in projects for clients, and by definition, projects have a beginning, a middle and an end. She relied heavily on a few large clients, which, while appreciating her efforts, could decide not to renew their contracts with her. Concentration of business risk is a major reason why small businesses fail.

"Every bank has experienced defaults on loans that were considered to be very low risk, often taken out by people and businesses of the highest integrity."

It is right for a banker to exercise scepticism when dealing with commercial propositions, and it is nothing to do with trust, or even mistrust. When a banker sanctions a loan but a default subsequently occurs, this rarely reflects the intent of either party. But it does no favours to clients to provide credit if their interests are not best served by the decision. CB

Bob Souster is a Module Director, Professional Ethics, Chartered Banker MBA at Bangor University. Share your views on Bob's verdict about this ethical dilemma by joining the Chartered Banker LinkedIn discussion forum.

PROFESSIONAL BANKER CERTIFICATE

Professional and Responsible Banking in a Digital Age

Our Professional Banker Certificate has been updated. Lynn McLeod, Head of Learning and Assessment, Chartered Banker Institute, explains what has changed and why...

What is the Professional Banker Certificate?

The Professional Banker Certificate is the Institute's flagship introductory banking qualification. It was originally launched in 2009.

What is its aim?

The Certificate was designed primarily for those who are new to banking with a view to providing them with an overview of the banking profession and to develop their understanding of the banking business.

The updated Professional Banker Certificate was launched on 31 October 2019.

It aims to develop the learner's knowledge, understanding and skills relating to banking in a digital age. Study of core banking principles and practice is combined with learning about the forces that are transforming the way we bank, and how banks are responding to meet the changing expectations of customers in an increasingly competitive environment. Key themes include responsible and sustainable banking, and what it means to be a professional in banking in the current environment. By applying these principles, learners will be able to help their bank deliver its strategy, perform well at work, and serve customers, communities, and the wider environment well.

Who is it for?

The Professional Banker Certificate is for all bank employees in the UK and internationally. Particularly those new to banking, regardless of their own specialism, who want to expand their knowledge and understanding of the business they are in – the business of banking – and have that knowledge and understanding recognised through the award of a professional banking qualification.

How has it changed – and why?

The qualification has changed because digital innovations in technology have transformed the way we bank today, and will continue to affect the way we bank in future. Yet the core principles of professional and responsible banking remain fundamental to our banking practice. So we've kept the certificate's main topics unchanged – these cover what banks do and their role in the economy and society, products, services and distribution channels, lending, risk, legislation and regulation, and professionalism and ethics. But we've updated the content supporting these topics to reflect the way we bank today and trends for the future.

The learning programme that leads to the award of the Professional Banker Certificate has changed from 'Professional Banker' to 'Professional and Responsible Banking in a Digital Age'. We chose this title because the programme aims to enhance understanding of what is meant by professional and responsible banking, and what it means to be a professional in banking today. It also has more of an international feel, with more focus on sound banking principles that apply globally and more examples of developments outside the UK.

What's different about the mode of study?
The method of delivery has been changed with a view to enhancing students' learning experience.

The programme is delivered online through our Learning Management System. The study text has been replaced by an interactive study guide, or 'workbook', that includes information about the programme, tips for effective learning, bite-sized chunks of core reading, learning activities, case studies, links to online resources, including videos, recommendations for further reading, and questions for review and reflection.

Interactive e-learning modules and online knowledge checks, with feedback given on responses, are included to help students revise key topics and prepare for the exam.

How have you updated the tone and style?
The tone and style of the study guide is less formal than a traditional study text – more conversational and student-focused. We did it this way because we wanted to help students engage more with the content and include activities that would help them learn – and think about how they might apply what they have learned in their role at work.

We also want students to enjoy learning about banking, reinforcing its significance and the critical role banks play in the economy, society and the wider environment. We want them to realise that they can make a difference, contributing not only to their bank's success, but also to the achievement of society's goals.

As Simon Thompson, Chief Executive, Chartered Banker Institute, says in his foreword to the programme "…there has probably never been such an exciting time to work in banking. Not just because of the exciting opportunities opened up by digital and data-driven innovation, but also because of the key role banking plays in tackling some of our world's greatest challenges".

What kind of course content has been added?
All content has been updated. New content includes:
- The digital and data revolution
- Digital innovations in banking
- Bank stakeholders, strategy and purpose
- Sustainability and the UN Sustainable Development Goals
- UN Principles for Responsible Banking
- New distribution channels and ways of banking
- What customers look for when choosing a bank
- Segmenting customers in a digital age
- The customer experience
- Responsible lending
- More on the types of risk banks face, including algorithms and machine learning risk, cyber crime and cyber risk, and climate-related risk
- Enterprise Risk Management
- Operational resilience

"We want students to realise that they can make a difference, contributing not only to their bank's success, but also to the achievement of society's goals."

- Open Banking
- Regulation technology
- Banking as a profession and what it means to be a 'professional banker' – future knowledge, skills and roles required
- More content about understanding and applying the principles of the Chartered Banker Code of Professional Conduct
- More about ethical dilemmas and ethical decision-making
- Ethics and technology
- Banks' moral obligations towards the environment.

What skills and capabilities does it enhance?
The programme has been designed to enhance the learner's ability to:
- Understand and articulate what banks do, how they do it, and the significance of their role in the economy, society and the wider environment
- Match bank products and services to customers' needs, treat customers fairly, and contribute to a good customer experience
- Support vulnerable customers and customers in financial difficulty
- Apply a sound and responsible approach to lending
- Identify and be aware of different types of risk, regulation and legislation that apply to banking
- Understand and apply the values and principles of the Chartered Banker Code of Professional Conduct
- Recognise when they have an ethical dilemma, apply an ethical-decision model, and exercise ethical and professional judgement when making decisions on how to act.

We have also included content to help learners:
- Study effectively
- Set personal goals and outcomes
- Plan their own development. CB

To find out more about the updated Certificate, please visit: www.charteredbanker.com/routes-to-chartered-banker/our-qualifications/professional-banker-certificate.html

INSTITUTE ADVOCATES

Safety. Belonging. Mattering.

A strong sense of belonging and eagerness to make a difference are helping Institute members influence the future of their industry, says Institute Advocate and Chair of the Membership Forum David May.

An opportunity to shape the future of banking through encouraging and broadening engagement has been fundamental to David May's long involvement with the Institute. At a time when the degree of change facing the financial services sector is unprecedented, and the pace of learning is exponential, May believes the role of the Institute and its core purpose are as relevant as ever.

Leading the debate

"The Institute has demonstrated tremendous forethought and placed itself ahead of the curve on current and future issues, such as sustainability, green finance and ethics," says May.

"Ethics has always been a part of the Institute's ethos; a core part of our purpose, which is to serve the public interest. After the events of 2008, that purpose became even more prominent. The complex world we now all live and work in intensifies the need for a framework to help people debate issues, manage that complexity and navigate the decision-making process. The Institute provides that framework, promoting transparency and rigorous decision-making, providing an anchor for its members against which complex and challenging decisions can be made."

"We should not underestimate the influence of a collective band of professionals."

An evolving purpose

As one of the first members of the Institute Advocates programme, May is passionate about the initiative, which enables the Institute to share insight on what it means to be an ethical, sustainable and future banker – and to highlight the Institute's role in promoting professionalism in banking.

"In my personal experience, the Institute has evolved from a membership association with a predominant focus on examinations, to one that promotes professionalism in the broadest sense and explores and shapes discussions that are of key importance to the industry and its professionals," he explains.

May was encouraged to join the Institute in 1981 when starting his career at NatWest. After completing the prescribed examinations, May became a revision course tutor for the Institute and took up a role in the bank's Insolvency Department, where his senior manager was a champion of the Institute. That enthusiasm for all the Institute had to offer obviously rubbed off. Following a stint as a divisional HR Director, May took up the position of Director of Learning and Development at RBS, where he became an avid Institute advocate and the professionalism it embodied himself.

Professional community

May's connection with the Institute continued to develop. He became a Fellow and a Member of the Council, taking his place on the Board of Trustees.

"My first experience of the Institute was through the examinations, which ensured I was well-versed in the technical skills I needed. Over time, however, I have come to value the professionalism the Institute promotes, the community it creates and the value of its member services. My role now is to support the Institute as it progresses the future of banking and promotes the value of financial services to a healthy economic society."

May has recently taken up the position of Chair of the Institute's new Membership Forum, designed to give members a greater say in the governance and direction of the Institute and, as May pointed out at the inaugural meeting in Summer 2019, "work together to help the Institute and its members become the best they can be".

The Membership Forum brings together members from all over the world, from all levels of membership and experience, in a panel of 30 members. As well as consulting on membership matters, the Forum will help develop the Institute's strategic plans as it continues to evolve to meet the challenges and opportunities the industry faces.

Insight and experience

"The Membership Forum is a fantastic new initiative that is representative of the diversity of the Institute's 33,000 members. It offers the Board huge insight into the kind of things that members are looking to acquire from the Institute and what really matters in terms of helping members fulfil their objectives of serving the public interest in different geographies, networks and departments. The Forum also helps disseminate messages from the Institute to the wider membership base, so its role is both educational and informative.

"In essence, the Membership Forum is a massive vehicle for insight, which we haven't had before. At the inaugural and subsequent meeting, the level of engagement of those involved was stunning."

As the Membership Forum develops, May hopes it will increase the extent to which the voice of the Institute's members is heard both within the industry, in the media and with the industry's regulators, creating a dialogue between members and the public they serve.

Embracing change

Looking to the future, May considers the importance of the Institute in promoting lifelong learning, a cause he has championed throughout his career. "Lifelong learning is a fundamental driver of professionalism and the Institute enables members to achieve that. It also builds a more open mindset, one that can see the importance of anticipating change, preparing for it and embracing change – and that is something that is going to continue to be vital for our industry."

The changes he foresees having an impact on banking in the future include the increasing importance of data and digital experience, particularly in altering the focus from products to the customer journey. "I think consumer awareness more generally, but particularly in respect of their economic and environmental footprint, will be crucial to the way we interact with customers and our priorities. Sustainability, for example, is now of strategic importance. Increasingly, decisions on funding and investments are being taken for the long term, with sustainability in mind."

Enduring relevance

Calling out the Institute's flagship event, the Young Banker of the Year Award, for its focus on the future of banking and contemporary issues, May says that the recent emphasis on sustainability highlights the continued relevance of the Institute to bankers and the industry.

"The award gives us the ability to look through the eyes of the young banker, to anticipate the future and what society and consumers will expect from banks, banking and bankers. It engages younger bankers and the organisations supporting and sponsoring them and helps us all to engage more deeply with what is important to the industry, regulators, society and the economy – now and in the future."

"The Institute has placed itself ahead of the curve on many of the key issues facing the industry."

May sums up why being a part of the Institute is so important in just three words: safety, belonging and mattering. The Institute, he says, offers all three. "It provides safety in terms of employability and the knowledge and skills members need. It offers a sense of belonging to something that's bigger than you, your team and your employer. And it matters, because professionalism really matters to society and Institute members on the whole want to make a difference. We should not underestimate the influence of a collective band of professionals." CB

If you would like to contribute your views as an Institute Advocate, please contact Matthew Ball, Head of Public Affairs, Policy & Communications, the Chartered Banker Institute: matthew.ball@charteredbanker.com

PROFESSIONAL FINANCIAL ADVICE

Gut instinct?

Mitigating customers' bad decisions and poor judgements to ensure positive outcomes could be seen as the holy grail for bankers across the sector. Institute member Jim Coke explains how behavioural economics can help 'nudge' better decision-making.

Behavioural economics is a cross between economics and psychology and it holds the view that people are irrational actors when making financial decisions. In other words, people make decisions based on limited and simplified knowledge, often resulting in compromised choices rather than optimised strategies. For want of a better term, people use their 'gut' to make significant economic and financial decisions.

Only in the past 50 years has behavioural economics entered the forefront of our understanding. Adam Smith, in *The Wealth of Nations*, first postulated the idea of the "invisible hand" and people acting in their self-interests in order to create an efficient allocation of resources for the whole society. Notwithstanding his invisible hand concept, classical economists since the late 18th century have held that economic actors are rational because they weigh all the options against a well-defined set of preferences to choose the one which makes them happiest (Homo economicus).

However, it was Herbert Simon (1956) who introduced the idea that we are irrational when making economic decisions because we act through a sense of 'bounded rationality' – our thinking is bounded by the information we have, cognitive biases and time constraints.

Beginning with Simon's Bounded Rationality and Satisficing Theory (1956) and Kahneman and Tversky's (1979) Prospect Theory, economists and psychologists have popularised behavioural economics as a subject. However, Richard Thaler's 2017 Nobel Prize for his work in behavioural economics is considered the critical point at which the subject entered the mainstream consciousness. It was generally acknowledged that human beings rarely make rational economic choices, because they're motivated by cognitive biases.

Cognitive biases

So, what are cognitive biases and how important are they when we make decisions? The truth is that we make an average of 3,000 judgements and decisions every day, and we often think that most of them are objective and logical. Unfortunately, that could not be further from the truth because we make systematic errors in the way we process information, often leading to poor decisions and bad judgements.

Such errors are relatively predictable, and we refer to them as cognitive biases. Research in this subject is still evolving; some researchers have recorded more than 300 cognitive biases! In theory, more will be discovered as culture, technology and society changes.

For example, one new bias that has been recognised in the past five years is the Google Effect. This is when a person shows a trend for forgetting information/facts that they can easily Google online, preferring to retain information that is unique and cannot easily be Googled. A consequence is that people rely less on facts they can recall through memory (which they leave to Google) but more on heuristics (rules of thumb). Without a mobile device, people are then more likely to be ill-informed and more prone to making decisions based on personal experiences, anecdotal evidence or preconceived ideas.

A possible solution to the Google Effect is to caveat information with very trusted (e.g. government) sources on Google, the argument being that if people have a natural disposition to refer to Google, then any effort that facilitates such a behaviour will be well received.

Debiasing (Cognitive bias mitigation)

Banks and financial institutions are starting to seriously consider modifying their customers' behaviour in order to avoid the common mistakes and poor choices they see all the time. When one considers the overall costs emanating from customers making poor decisions, institutions now see a financial upside with engaging early with customer behaviour.

An area that seems to produce the most tangible set of results comes from debiasing – methods used to reduce or eliminate cognitive biases. Do they work? Well, quite a few are already being used in financial apps produced by the growing number of FinTechs dominating the industry. Figure 1 has a short list of cognitive biases, mitigation strategies and examples in the long-term savings and pensions sector.

Conclusion

What evidence is there that debiasing works? With an increasing number of financial services and products being sold online, user experience (UX) and user interface (UI) researchers and designers can use analytics to show changes in behaviour. Even the Cabinet Office now co-owns a Behavioural Insights Team (BIT) that is specifically tasked with using behavioural psychology to change habits and actions.

A few of the major high street banks now employ behavioural economists to sit alongside UX/UI designers to change or modify behaviour. One conclusion that can be drawn from this is that it seems financial institutions are now getting to the root of their customers' relationship with money; their attitudes, biases and behaviours instead of just focusing on their age, income and assets. CB

The views and opinions expressed in this article are those of the author and do not necessarily reflect the official policy or position of any other agency, organisation, employer or company. Assumptions made in the analysis are not reflective of the position of any entity other than the author.

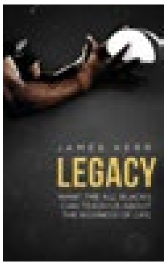
"It seems financial institutions are now getting to the root of their customers' relationship with money."

Cognitive bias	Description	Mitigation strategy	Examples
Ambiguity effect	This is when a customer's decision making is negatively affected because of incomplete and ambiguous information.	Customers should always have access to additional information.	Always ask customers if they would like more information before they finally commit to any product, process or service. This could be a useful and free tool for collecting additional information and insights for further development of the product, process or service without needing to do additional research.
			For every journey, create help buttons, guides, call back features etc. Links to information will be useful and will also help mitigate Digital Amnesia (Google Effect).
Actor-observer bias	A customer is more likely to judge their own behaviour and blame circumstances around them. However, when they judge other people's behaviour, they are more likely to blame those people's attitudes and personalities.	Customers should be encouraged to see as many retirement journeys of other people as much as possible so that they see themselves in others.	Use positive case studies at specific points of a retirement journey to make it personable and relatable. The more people see their personal situations in others, the less actor-observer bias you get.
			Showcase a pensioner by doing "Interview of the Month" so that a pensioner's lifestyle can be demystified thus reducing actor-observer bias.
			Create an online pension forum or discussion board where people can discuss pension issues and bank staff can offer answers and suggestions. This will reduce actor-observer bias.
Gambler's Fallacy	This is when a customer believes that a frequently occurring event is likely to be less frequent in the future or a less frequent event is likely to increase in frequency. In short, the customer ignores the probability of events.	Customers should be reminded of statistical facts regarding retirement; both good and bad.	Customers should be asked to list the top five events that have affected their payment contributions and the top five that will likely affect their payment contributions in the future. In theory, the lists should be the same and this exercise is where Gambler's Fallacy tends to show up.
Authority bias	This is when a customer attributes more authority or puts more weight to the opinions of an individual in an authoritative position.	Information to customers should always be supported with research or citations were possible.	Female customers should be advised to save more than men because according to the Pension Policy Institute, *"To draw the same pension income throughout their retirement, women would need to have saved around 5% – 7% more than men by retirement age to allow for living longer."*
Automation bias	This is when a customer shows a positive bias towards automated decisions than from decisions made by other people even when the decisions contradict the automated decision and is correct.	Customers should be advised that decisions are made by algorithms, which are continuously reviewed.	Customers should be advised that the retirement journey automatically and disproportionately targets women in their 60s because pension wealth for men reduces by a third but half for women, signifying a greater impact of divorce for women than men.
Functional fixedness	This is when a customer has a mental block in that they can use an object only for what it was intended, traditional used or designed for.	Customers should be advised of different ways to look at their pensions.	Most customers are told to follow the pension rule of thumb: whatever age they start contributing towards their pension, they should divide that by half and invest that amount of their salary until they retire. Customers should consider looking at alternatives such as starting from how they want to live in their retirement and working backwards from that figure.
Focalism	This is when a customer makes decisions based on an initial piece of information received and almost discounts any further information.	In a retirement journey, customers should be frequently reminded of information given.	In a pension journey, each page or screen should offer the customer a summary of the last three-to-five screens.

BOOK BANK

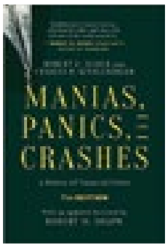
Pick of 2019

Two Fellows from the Chartered Banker Institute's Membership Forum share their must-reads from 2019.



Legacy, James Kerr
Recommended by David Roberts, TSB

Legacy is all about what the All Blacks can teach us about the 'business of life'. This is described as "unputdownable" by Bloomberg and they aren't wrong. It's all about how the best in the world stay the best by learning from the culture of the New Zealand's national rugby union team. It doesn't matter if you are a sports fan or not, as it covers many good habits that turn vision into action, purpose into practice – and pressure into results. Only 200 pages in paperback, so very easy to put in your travel pack to read on the commute to work.

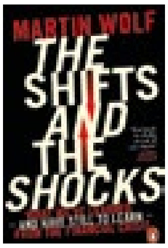


Manias, Panics and Crashes, Charles Kindleberger (and Robert Z. Aliber, in newer editions)
Recommended by Dr Alan Brener, Queen Mary University of London

This is a classic description of how financial panics occur and why. Kindleberger's style is very clear and the book easy to read as it examines a series of financial crises from the South Sea Bubble onwards. It is now a standard work for anyone interested in the fragility of financial services and why we have prudential regulation.

For me, a key element of the book is the lack of mathematical formulae. Kindleberger shows how it's possible to describe market behaviour in lucid English, and the psychological pressures on bankers, depositors and investors.

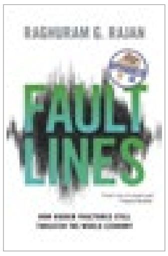
> **"This is described as 'unputdownable' by Bloomberg and they aren't wrong."**



The Shifts and the Shocks, Martin Wolf
Recommended by Dr Alan Brener, Queen Mary University of London

The Shifts and the Shocks examines the reasons for the 2007/8 financial crisis and its aftermath in global economic terms – and is one of a small number of books that I recommend to my students. Once read, all becomes much clearer, although the author is quick to point out that there are no easy and painless solutions.

Wolf highlights the fact that there are strong economic and political reasons behind banking crises; these develop over time. He quotes with approval the late German economist Rudiger Dornbusch, who said that a financial crisis takes a much longer time coming than you think, and then it happens much faster than you would have thought. There are lessons in this for all bankers, regulators and politicians.



Fault Lines, Raghuram Rajan
Recommended by Dr Alan Brener, Queen Mary University of London

Raghuram Rajan is a professor at Chicago University and was recently governor of the Reserve Bank of India. He was one of a small band of economists who predicted the 2007/8 financial crisis. His major concern was, and remains, the high level of debt in society and the threat that this posed, and continues to pose, to financial stability. He blames much of this on politicians failing to take hard tax and expenditure decisions, preferring to encourage people to borrow. This is summed up in Rajan's prescient phrase that, in the face of societal financial hardship and inequality, the political response was 'let them eat credit'.

Rajan uses his succinct turn of phrase and clarity of writing to communicate both complex issues and his proposed solutions. He is an important commentator and deserves to be heard. CB

LESSONS LEARNED

When will challenger banks come of age?

Many of the new banking brands, from Metro to Monzo, are still younger than 10 years old, and every one of them seems to be going through their own growing pains. Ian Henderson examines what's stopping them joining the big boys.

The UK banking sector is the largest in Europe and the fourth largest in the world. It is also one of the world's most competitive and technology-driven – only the US and China have more billion-dollar 'unicorn' FinTech start-ups. So, it's not surprising the big four high street brands – Barclays, HSBC, Lloyds and RBS – have been feeling the pressure from digital 'neobanks' such as Monzo, Starling, Revolut and N24 as well as the more conventional newcomers like Metro and Atom.

However, the rise of these challengers seems to be stalling. The Big Four still control more than 70% of personal bank accounts, down from 92% a decade ago, and 85% of business accounts, while their dominance is even more solid in the lending market. Despite optimistic forecasts from the new banks, they continue to make significant losses, which have spooked investors. While analysts have not forecast outright collapses, they have predicted a period of consolidation with mergers and takeovers by the bigger firms.

Customer numbers overall have plateaued. A number of high-profile reverses, such as controversial Metro founder Vernon Hill's ejection from the bank after a serious accounting error, Monzo's 'fluffed' (according to CEO Tom Blomfield) launch of its Plus premium card service and Virgin Money's profit warning from its owner CYBG following a 50% share price slump between April and October 2019 haven't reassured investors. And there's still the small matter of making money – almost all neobanks across the UK and across the world have yet to show a profit.

Loss-making is to be expected in today's new and highly competitive space; these rivals are competing for customer numbers before converting them to valuable account holders. This has produced plenty of experimentation with different models such as Nubank in Brazil, Revolut across Europe and, of course, Metro's contrarian branch-building extravaganza. It's led to some brilliant marketing, such as Monzo's 'movement-based' approach to building a loyal fanbase, and to levels of tech-enabled service that have transformed customer expectations.

The banking revolution this has created has been great for consumers. But in such an intensely competitive environment, the costs of customer acquisition are high. Additionally, at the current stage of development, more growth actually tends to mean bigger losses, which isn't especially helpful.

And while facing these many challenges, neobanks are having to contend with outside factors such as regulation, in which the UK leads the global banking sector. This may be good news for consumers but is less so for banking entrepreneurs. There are distinctly mixed messages from the Bank of England (BoE), which has been dishing out banking licences but, to quote the *Financial Times*, "...has also introduced uniquely stringent regulations that banks say make it difficult for them to grow".

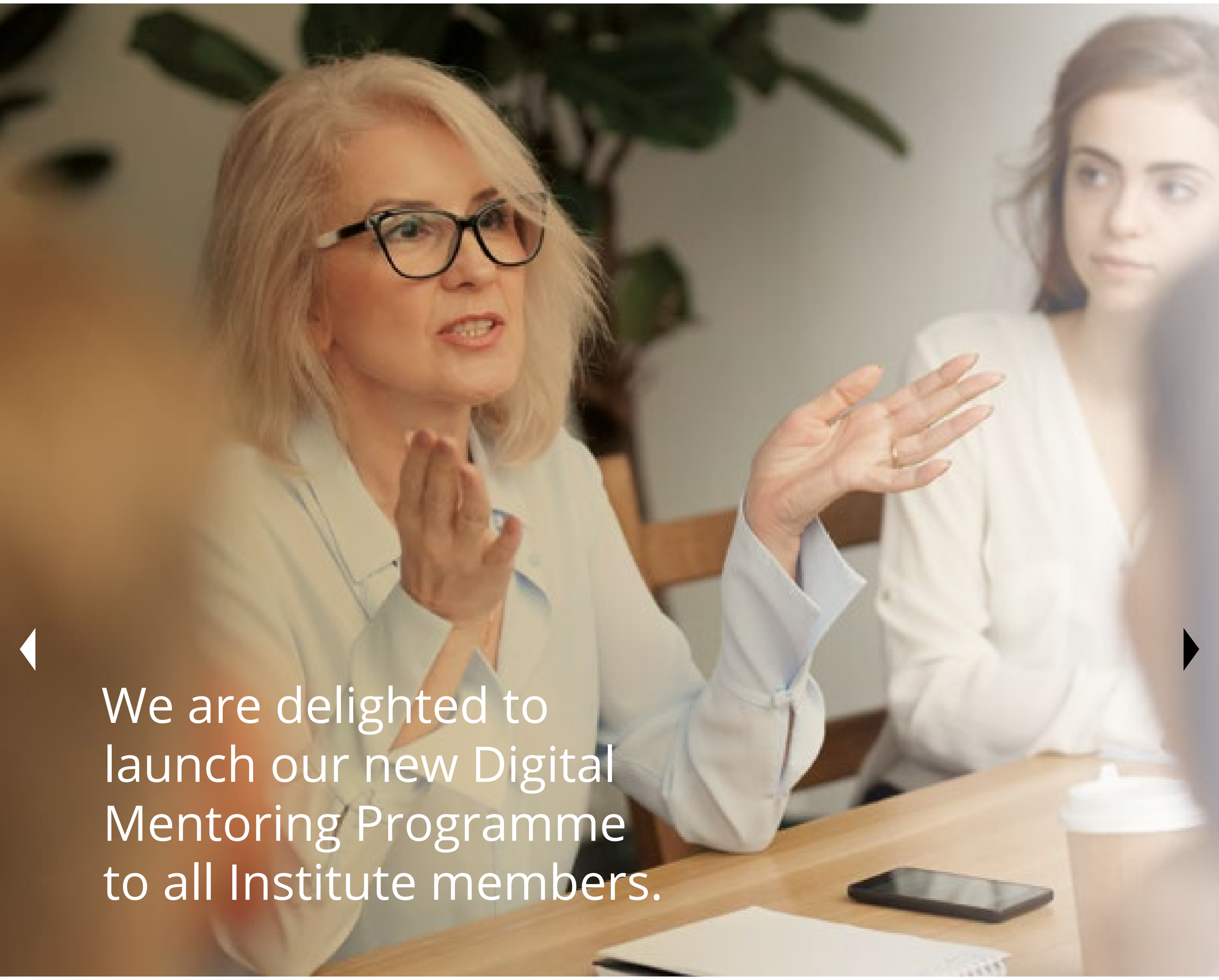
In the UK, one such self-imposed barrier to growth is minimum requirement for own funds and eligible liabilities (MREL), the BoE's requirement for banks to raise loss-absorbing debt when assets reach just £15bn – compare that to the Eurozone's much higher threshold of €100bn and the $250bn required in the US. Another hurdle is the ring-fencing of a financial organisation to protect against investment bank losses, which has hit larger market entrants such as Santander. And of course, political uncertainty has made investment decision-making as difficult for banks as for any other growth business.

"Can the challenger banks stand on their own feet and join the grown-ups?"

So, can the challenger banks stand on their own feet and join the grown-ups? Only some of them, seems to be the answer, and only the fittest will survive the coming cull. These survivors will only thrive – and continue to redefine the banking sector in ways that benefit the customer – if the UK business environment shifts in their favour. As well as a more certain political future, that means lighter-touch regulation and continued investment in growth. And of course, a steady stream of inventive, motivated and confident entrepreneurs. CB

Ian Henderson is CEO of AML Group
aml-group.com

Chartered Banker
MENTORING PROGRAMME



This platform has been designed to help members' professional development, expand their network and build their industry knowledge. The new digital platform allows mentees and mentors to easily manage their mentoring relationship online, and we hope members find this new service beneficial. As a valued member of the Chartered Banker Institute, we invite you to create a profile on the mentoring platform either as a mentor or mentee.

Discover the new platform, visit **www.charteredbanker.com/mentoring,** or please get in touch if you have any questions: **mentoring@charteredbanker.com**

"The Mentoring Programme has enabled great conversation with someone who has a lot of experience in the sector. I have received good advice on how to reach my career goals and have also been put in contact with others to discuss potential opportunities. I would strongly recommend the programme to others."

Institute Mentee

"Becoming a mentor has allowed me to give something back to the next generation of professional bankers; to pass on the experience I have acquired in the industry and to press home the importance of professionalism."

Institute Mentor