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Thoughts regarding the delivery of European financial products in the Digital Era

The pace of technological change continues to rise and as a result the impact of technology on people's lives is getting greater. The pandemic has clearly brought technology further to the forefront of our minds and is accelerating changes in consumer behaviour.

As new operators and business models emerge, it is essential to consider all of the new and different players in the financial ecosystem from the end user's perspective. For instance, as a broader range of firms from a diverse range of sectors seek to offer retail and potentially wholesale financial products, there is a need to ensure that consumers are provided with the same level of protections, and that all those participants who offer the same service, undertake the same activity, or expose consumers to the same risk are subject to equivalent regulatory requirements on a proportionate basis. Without this, consumers will face an inconsistent experience, with the potential customer

detriment counteracting the benefits of greater competition and creating potential risks for market integrity and potentially also financial stability.

Despite the rapid technological changes and the emergence of new digital players, large and small, regulation has developed to respond to the traditional 20th century business model, which regulates based upon product, manufacturer and issuing or distributing entity. This creates a narrow regulatory perimeter applicable to these industries. However, a 21st century "platform company" does not need to create the underlying financial product or service to become a leading digital aggregator and distributor of those products and services. This can – in the case of financial services – create a substantial financial marketplace to complement a non-financial services marketplace. In other words, in the connected economy, a position of strength in one market, led by data, can readily be used to access another very different product market.

Looking forward, as the number and type of business able to access consumer spend data increases due to Open Banking and PSD2 this is likely to have further transformational effects on the composition of the new financial ecosystem and therefore critical components of financial markets infrastructure. The increase in competition for consumers is to be welcome, but there is a need to address how we collectively provide for the protection of consumers and clients and also to ensure a fair playing field for all market participants. Looking at the ecosystem from a consumer perspective, it will be increasingly difficult for consumers to understand the risk profiles of products attached to different entities and the associated protection they may or may not enjoy without further assistance from regulators. Understandably, a consumer sees products that are interchangeable for their needs, rather than considering in detail their regulatory regimes. There is a significant risk that an industry defined approach to regulation will fail to recognize emerging risks posed by the market changes noted above, and result in customer detriment.

In addition, a key barrier to innovation for firms is the lack of regulatory clarity regarding how 'new' and 'emerging' technologies, such as distributed ledger technology (DLT) and artificial intelligence (AI) may apply to financial sector use-cases. The current regulatory

frameworks across the globe were not written with these technologies and the wider ecosystem in mind, and therefore they may not be fit for purpose. Whilst the principle of technology neutrality is important it is also essential that regulations consider the technologies where relevant. In addition, with global regulatory and supervisory direction constantly evolving, one of the main barriers results from some of the inconsistencies from one jurisdiction to another and resulting fragmentation.

Quite apart from this, there is a lack of consistent regulation of underlying products, with some at a more advanced stage unified regulation at the European level (e.g. the UCITS directive, which creates a harmonised framework for investment funds that can be sold to retail investors throughout the EU using a passporting mechanism), and other, substantial areas such as mortgages remain mostly regulated at the national level. Similarly, investments and trading have been tackled effectively at the European level, with the creation of ESMA; but while such "asset-side" regulation has been advancing, the "liability-side" (borrowing and lending) has yet to achieve the same level of harmonisation. This creates a further gap in safeguarding customers' interests at the European level and in completing the single market.

These issues are recognised by the regulatory community. Steps such as the European Commission's Digital Finance Strategy, which aims to amend the regulatory framework to make it fit for the digital era and achieve a level playing field across entity types, will be crucial in helping solve these challenges. Further, given the cross-border nature of innovation, collaboration by policymakers in different jurisdictions is essential. Regarding underlying product areas, the European Commission recognises the continuing fragmentation of credit markets, and while the Mortgage Credit Directive was a good first step towards an EU-wide mortgage credit market with a high level of consumer protection, it needs to act as a foundation and not an end-point. This is all the more important in an age of digital delivery of financial services.