



# Financial system rules vital even in face of technology progress

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I wish to commend Prof Samuel Seijaaka for the article he penned on the evolving banking industry, published in the *Saturday Monitor* of October 21 titled, 'Traditional Banking is Dead. Time to bury the corpse'. As usual Seijaaka was spot on. My task is to comment on the suggestion of the possible irrelevance of the "regulator" in the new normal.

Three things must be said about financial technology (FinTech) and the regulator in this new normal. First, this millennium is experiencing accelerated change in financial services propelled by FinTech. New service providers are entering the market for financial services which has led to a rise in automation, specialization and decentralisation.

As a result, financial firms are finding increasingly efficient mechanisms of leveraging vast quantities of consumer and firm data. Second, the regulator is likely to remain relevant. Third, the regulator will have to revamp his skill competencies and take on a changed mindset.

To start with, FinTech promises a number of benefits for the financial system. For example, we are already recording efficiency gains in a number of aspects - speed, convenience and cost - in delivery and use of financial services, thereby fostering

better access to, and inclusion for, financial services. FinTech could enable more transparency, consequently minimising information asymmetry and enabling more accurate assessment and pricing of risks.

Furthermore, there will be greater diversification and decentralisation of the financial system, as FinTech facilitates development of financial services and enables entry of more financial services providers.

It is, however, still too early to gauge the full impact of the current technological progress. What is clear is that there is potential for deep-seated change given the vast reach of FinTech. The increased competition is already forcing incumbents (banks and non-banks) to respond by adopting new technologies, improving services, altering business models and reducing costs.

It is important to be able to assess the impact that FinTech might have on the financial sector, and how regulation should respond.

To start with, the financial sector plays five broad functions: To make and receive payments, to save so as to be able to consume or invest, to borrow to be able to consume or invest now, to manage risks to income, savings, and transactions; and to provide advice. Irrespective of the function, technology can impact the

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attributes of the financial services. These attributes include speed, security and transparency.

In addition, technology can also impact on the organisation of service providers - the market structure. While the attributes and market structure are closely related, each can have an independent effect on regulation. Technology can promote the development and adoption of new services, especially when targeted at unmet user needs.

The bigger the unmet need, the greater the incentive for firms to improve services as permitted by technological advances and the faster the users' adoption of such service.

Technology can also affect the market structure of service providers. For example, it may reduce the need for financial intermediaries (specialized financial firms, banks and non-banks that facilitate transactions between parties), push in-

termediaries to change their internal structures or induce the entry of new intermediaries to compete with, or displace, old ones.

Finally, technology may affect factors that shape intermediaries. It can reduce asymmetric information, which underpins the need for trusted intermediaries, facilitate matching of parties to a transaction, and reduces transaction costs.

In this environment, financial regulation will have at least four important roles. First, it will seek to address vulnerabilities and imperfections in financial markets that undermine market efficiency, and expose consumers to risks. Second, regulation will help to ensure financial stability by providing incentives for institutions to take into account systemic risk.

Some emerging technologies could raise financial stability risks. It should be noted that the development of financial services outside the boundaries of the existing supervisory and regulatory framework may lead to the emergence of new risks.

Third, financial regulation will help to maintain trust in the financial system. Finance involves creating value through transferring assets and claims among entities as well as over time.

It requires trust in financial intermediaries and processes to ensure proper functioning of the financial markets. Emerging technologies that distribute information across networks, like distributed ledgers, raise questions about the right balance between privacy and transparency.

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