Policy Brief:
Fintech and the Future of Finance

Fintech, the application of digital technology to financial services, is reshaping the future of finance. Digital technologies are revolutionizing payments, lending, investment, insurance, and other financial products and services – a process that the COVID-19 pandemic has accelerated. The World Bank Group and the IMF launched the Bali Fintech Agenda in 2018, recognizing the need for regulators and policy makers to actively engage as technology transforms finance, to take advantage of new efficiencies and opportunities to improve financial inclusion, while safeguarding financial stability and consumer protection.

Digitalization of financial services and money is helping to bridge gaps in access to financial services for households and firms and promoting economic development

Access to basic financial services such as savings, insurance and credit translates into better firm productivity and growth for micro and small businesses, as well as higher incomes and resilience to improve the lives of the poor. Technology can lower transaction costs by overcoming geographical access barriers; increasing the speed, security, and transparency of transactions; and allow for more tailored financial services that better serve consumers, including the poor. Women can especially benefit.

The latest World Bank Findex data show global financial account ownership grew to 76 percent from 51 percent between 2011 and 2021 and the share of adults making or receiving digital payments grew to 57 percent in 2021 from 35 percent in 2014.

Yet too many people and firms still lack access to essential financial services that could help them thrive. Therefore, countries should embrace fintech opportunities and implement policies that enable and encourage safe financial innovation and adoption.

Fintech is transforming the financial sector landscape rapidly and has profound policy implications

Fintech is making an impact in many countries. Examples include the rapid ascent of mobile money, bank apps, financial services provided by bigtechs and neobanks, and crypto-assets and central bank digital currencies. New infrastructures, providers, products and business models are reshaping market structures in profound ways. These technological advances are blurring the boundaries of both financial firms and the financial sector. For example, financial firms more often rely on third parties to offer their products and services and non-financial firms are increasingly embedding financial services into their products.

In addition to inclusion, core policy objectives for a well-functioning financial system comprise: financial stability and integrity; efficiency--which is linked to fair competition; cyber and operational soundness and security; data privacy; and consumer and investor protection. Allowing fintech developments to be driven solely by market forces could compromise these objectives. For example, economies of scale and scope could lead to market concentration, with adverse consequences for competition, innovation and financial stability.

Policy makers need to adapt as fintech adoption continues and policy tradeoffs evolve.

It is important to ensure that market outcomes remain aligned with core policy objectives. Several policy implications emerge:

- **Manage risks, while fostering beneficial innovation and competition.** Given the fast-evolving landscape and rapid spread of innovation, a regulatory approach that supports responsible fintech innovation and adoption is critical. Prudential supervision, market conduct and consumer protection agencies should coordinate extensively as fintech issues cut across their mandates. Regulators should strive to promote trust and investment and minimize exposing consumers, particularly the poor, to undue risks. This will require regulators to be proactive, pragmatic, and clear in their decisions.

- **Broaden monitoring horizons and reassess regulatory perimeters.** Financial services are increasingly provided by a wide variety of entities and are even embedded into commercial transactions and social interactions. This blurs the boundaries of the financial sector. It is essential to proactively monitor the comprehensive financial sector value chain and reshape the regulatory perimeter accordingly.
- **Review regulatory, supervisory, and oversight frameworks.** The range of new products and providers, the use of new technologies and a wider range of data, and the inclusion of new customer segments in increasingly complex markets has made existing regulatory and supervisory mandates and approaches insufficient. Principles that help underpin policies include: pursuing an approach that is proportional to risks; maintaining a level playing field by treating the same activities and risks similarly, looking through technology and focusing on underlying economic functions; and ensuring the primacy of core policy objectives. This may call for bespoke approaches.
- **Be mindful of evolving policy tradeoffs as fintech adoption deepens.** Policy tradeoffs will evolve as fintech continues to permeate the financial sector. This calls for proper safeguards to maintain financial stability, fair competition, ensure data and consumer protection, and to prevent the abuse of market power. Regulators can take various actions to better balance the tradeoffs between stability, competition, concentration, efficiency, and inclusion through various actions, including:
    - formulating data collection principles and proactively monitoring market conduct;
    - establishing frameworks for open banking and data ownership; and
    - revisiting restrictions on product tying and linkages between banking and commerce.
- **Monitor market structure and conduct to maintain competition.** While the initial focus of many regulators has been on facilitating entry to markets and the momentum of innovation has been from small startups and new entrants, the industry is rapidly boomeranging towards concentration of players and platforms, due to economies of scale and the massive amounts of data held by big-tech companies. This may deliver inclusion and efficiency, particularly in developing economies, which may lack a robust, competitive, and inclusive banking sector. However, regulators will need to proactively monitor markets and dynamically balance tradeoffs between competition, concentration, efficiency, data protection, and inclusion.
- **Modernize and open financial infrastructures.** Financial infrastructure may need upgrading to enable digital products and services. Infrastructure should be interoperable and open to both new and traditional players. The increasing role of fintech companies, embedded finance by big tech companies, digital money, and cross-border financial flows will put pressure on regulators to ensure that the access policies of financial infrastructures are fair and transparent. Moreover, with the entry of new market-level services that take on characteristics of financial infrastructures, regulators will need to assess whether and how to bring them within the regulatory perimeter.
- **Ensure public money remains fit for the digital world.** Reduced reliance on public money could impede authorities from shaping and safeguarding financial sector and economic development. The ongoing digitalization of the economy and payments, the world of crypto-assets, and the influence of big tech firms in payments and user data, over time, could challenge the role of public money, competition, and privacy. Public authorities might consider distinct, public alternatives to crypto-assets, such as central bank digital currencies (CBDCs), in addition to strengthening policy frameworks regarding crypto-assets and big tech firms. Countries that consider a CBDC should carefully evaluate the wide-ranging implications and design options in consultation with public and private stakeholders.
- **Pursue strong cross-border coordination and sharing of information and best practices.** Fintech developments enable providers to reach a wide set of customers across borders and provide services without necessarily being subject to regulation in the customer's jurisdiction. Regulators and public authorities need to collaborate and coordinate with their peers to safeguard their respective financial systems and customers.