Speech

Speech by SFST at Thomson Reuters 6th Annual Pan Asian Regulatory Summit (English only)

Wednesday, October 14, 2015

Following is the speech by the Secretary for Financial Services and the Treasury, Professor K C Chan, at the Thomson Reuters 6th Annual Pan Asian Regulatory Summit today (October 14):

Distinguished guests, ladies and gentlemen,

Good morning. It is my pleasure to return to the Summit after joining the event last year and a warm welcome to those who have flown in to Hong Kong.

As a prelude to the next panel discussion, I would like to spend the next 10 minutes or so to discuss financial technologies, or Fintech, and regulation.

Fintech generally refers to utilising technology to upgrade the operation of financial services and enhance the interface with customers. I should first mention that our host today is among the pioneers in Fintech. I also know that Thomson Reuters has a Data Innovation Lab in Boston that hosts a data science team to provide novel data-driven insights with big data analytics and visualisation. And congratulations as well to Thomson Reuters Labs, which has just launched a new operation in Waterloo, Canada.

But is regulation friend or foe of financial innovation? To answer this question, let's look at the forces that help create the Fintech sector.

First, there is a push factor of a changing customer culture under the on-demand economy that is disrupting financial services. Clients these days desire to initiate, sometimes spontaneous, interactions anytime, anywhere and not confined by the model of bricks-and-mortar branches with fixed opening hours. The new generations of clients of the financial services industry are those who grew up with the Internet and smart phones. They tend to obtain and share information and recommendations with other netizens. The crowd-sourced development has not only revolutionised the software industry, but is now changing our way of living and the landscape of many sectors, financial services being one of them.

Second, there is a pull factor of technological advancement and "hyper-connectivity" that lowers the entry barriers to provide finance-related products and services via alternative channels. Made possible by the revolution of information and communication technology, they enable us to devise technical solutions that are intuitive for customers, secure for financial institutions and cost-effective for everyone.

So we have seen that telecommunication firms, Internet search engines and e-commerce companies are moving into the space of financial services. Their natural advantage is that they are a node of information flow in the Internet age. It helps them amass huge amounts of data about the behaviour and preferences of customers. With big data analytics and cloud computing, they have the first-mover advantage of turning what used to be number crunching into treasure hunting.

IT experts and data scientists are no longer geeks and nerds. Their skills and insights are sought after for improving existing processes, enhancing consumer experiences and developing new products. In short, new species of financial services providers have evolved in our ecosystem and they compete fiercely with the existing inhabitants.

Many financial institutions are equally active in taking advantage of Fintech in enhancing their operations. For instance, financial institutions can leverage their incumbent status and apply big data techniques to customise products and solutions for clients. Some banks are also open to working with startups that provide credit analytics solutions for short-term unsecured business loans to enhance their credit risk management.

There is no doubt that Fintech will change the way financial services are offered. But what remains the same is that financial services are about pooling capital into more gainful use, pricing risk, and pushing through transactions more efficiently to serve the real economy.

An efficient and trustworthy financial services industry must be underpinned by a regulatory regime that makes customer protection one of its pillars. Maintaining robust customer protection measures will give investors confidence in the financial system and enhance systemic resilience. This should be a consistent message across all places and ages. At the same time, regulation should avoid being the hurdle to bringing genuine innovation to the financial services industry that benefits firms and customers.

The emergence of new players and stakeholders on the horizon may subject these golden rules to many practical challenges. For instance, there are companies coming from outside the financial services industry like internet portals and telecommunications companies now actively engaging in the provision of payment services. Successful ones obviously offer local services that are low in cost and high in efficacy, and some could amass significant funds from their users along the way. When the payment platforms are turned into de facto deposit institutions, this could raise prudential and systemic concerns as well as conduct risks like frauds and cybercrimes. How to welcome these new neighbours into the house of financial regulations that was originally built for financial institutions is no small matter.

Then there are the lean startups which, same as their more financially equipped counterparts, bring about novel ideas in delivering financial services. When striking the right balance between protecting consumers and promoting innovation, we have to acknowledge that some of the small Fintech startups may not have the same resources to deal with regulatory and compliance matters compared with established financial institutions. Therefore, a conducive Fintech ecology must provide an effective communication channel for the new kids on the block to understand the sometimes complicated regulatory landscape. A number of jurisdictions like Australia and the UK are making admirable attempts to help bridge this gap, and we will no doubt closely look at how Hong Kong can benefit from their experience.

For the long term, the financial services landscape may further evolve given the technological revolution is not abating. It is helpful to remind ourselves to ensure that our rules have to meet both the need to protect consumers and fostering an environment for fair competition and relentless innovation.

For financial institutions that have been putting substantial resources to keep pace with the seemingly complex and ever-changing regulatory environment, I wonder how Fintech may potentially offer relief and mitigate some complaints about the shortage in compliance talent. Maybe our experts on conduct risk, cybercrime, KYC, anti-money laundering and fraud detection in the later panels could shed more light on this.

Last, but not least, regulators. They will make rules that apply to Fintech. They will enforce those rules. But will they benefit from Fintech? My answer is a resounding "yes". Many financial institutions are using technology to help them identify signs of fraud and risk early. Regulators are also looking into ways to explore the big data approach to streamline compliance process. The use of technology should enable regulators to conduct real-time transaction analysis and facilitate automated reporting by regulatees, so as to allow their market monitoring efforts to keep pace with financial transactions that nowadays can be completed within nanoseconds.

It is no coincidence that key international financial centres like London, New York and Hong Kong are among the major Fintech hubs around.

Our excellent information technology and communications infrastructure provides the conduits for innovative products and services to reach clients. Our regulatory regime is well respected and well understood, and is keeping pace with developments in the financial markets.

In addition, our large pool of financial experts provide a wealth of knowledge about customers' needs, locating the gaps in incumbents' services and the market segments that are currently being under-served. Some of them will share their domain knowledge with Fintech startups to improve their business models. Some will act as matchmakers between existing financial institutions and startups with brilliant ideas to explore how to improve customer experience and reach new clients. Some will even strike out on their own to start their own businesses to compete head to head with existing financial institutions.

I am pleased to note that the startup ecosystem in Hong Kong has been thriving. A government survey found that the list of co-work spaces, incubator and accelerator programmes located in Hong Kong has grown from three in 2010, to 35 in late last year, and further to 40 most recently. A poll on these spaces and programmes found that the number of startups registered has jumped 46 per cent to more than 1,500 in a space of less than a year. Around 90 of them are engaged in Fintech, and this figure could well be out of date even now. And they are a diverse bunch. Some are competing direct with financial institutions in securities trading, remittance and fund raising. Others are complementing existing players, with their brilliant banking and securities solutions to investment portfolio optimisation software.

The Fintech accelerator programmes that have been held in Hong Kong recently have not only been well received, their participants are coming from around the world, from Australia, India, Singapore, Israel, South Africa, Kenya and the UK.

In short, Hong Kong is embracing the challenge of Fintech by continuing to nurture a conducive ecology for the sector. One that attracts innovative Fintech talent and startups to use Hong Kong as their launch pad to establish and grow their presence here. One that actively engages existing financial institutions to bounce ideas with Fintech startups and keeps them abreast of the latest frontier in technological applications in financial services. One that represents a brand as the centre of excellence in Fintech for startups, financial institutions, and non-financial firms alike.

As our Fintech ecosystem is taking shape, there is much more that Hong Kong can offer as an ideal hub for Fintech companies to flourish. To further develop a set of policy measures to build Hong Kong into such a hub, I have been chairing a Steering Group on Fintech that was set up a few months ago in April. The Steering Group is a melting pot of views and ideas from the regulatory authorities and the industries, academia, and research and development institutions. We are working closely together to examine the economic and business opportunities provided by the development of Fintech for Hong Kong. We are putting focus on measures needed to promote Fintech in Hong Kong, especially to address any potential and existing gaps. And we hope to prepare a blueprint on the sector's development in the near future.

All these should prepare us well for the challenges posed by Fintech to traditional business models. And I believe there is definitely room for healthy competition between traditional players and startups to bring benefits to customers.

The above is just some food for thought early in the morning. I am sure that the upcoming panel will offer a hearty debate on whether and, if so, how

Fintech will change the regulatory environment. And I also look forward to the panel's in-depth look at how banks can respond to the disruption from Fintech and keep a grip on their client base.

I wish everyone a fruitful Day 2 at the Summit. For delegates flying in to join us here, a warm welcome and hope that you have the time to experience the culture and various kinds of offerings in Hong Kong.

Thank you very much.

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