Exploring the new frontier: open banking

By Sindiswa Makhubalo

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The concept of open banking is forcing banks to rethink financial services as it's understood today. Realising that this is the new frontier, the Financial Sector Conduct Authority (FSCA) is far advanced in its research into open banking, including its challenges and the opportunities it presents.

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We are actively exploring ways to bring the concept to life, to help both customers and service providers – a task that will require collaboration between regulators and industry players, to ensure that advancements in open banking meet market needs and that regulators can manage the risks without stifling innovation.

Digital innovation has disrupted financial services significantly in the last five to 10 years – but of the array of advances and pioneering new solutions and products that have made their mark and served to streamline the sector, open banking is the one considered by many to be the game changer.

Also known as open bank data, this is a secure way to give financial service providers, access to customers financial information using application programming interfaces. This will allow the networking of accounts and data across institutions, opening a new and competitive way of delivering various product and service offerings, that can be used by customers and small-to-medium sized businesses.

As the conduct regulator, and as a member of the Intergovernmental Fintech Working Group (IFWG), we are investigating how best to regulate open banking innovation, as we see it as an important means of fostering competition, developing the financial services ecosystem, and improving access. We believe that as banks modernise their infrastructure and increasingly adopt cloud-based solutions, their ability to partner, connect and share data will improve. And, for fintech start-ups, their agility will improve the customer experience and solve for ever-evolving needs.

However, as much as open banking is encouraged, several barriers exist which undermine the prospects for open banking in South Africa, and the FSCA has the responsibility to facilitate and enable elements of an open banking framework, such as:

- Customer protection: we need to ensure that customers understand the risks of consenting to the sharing of their data. There needs to be more consideration around data, who owns it and how it is used. For example, aggregated data to demonstrate a trend has different ethical considerations to using a customer's individual data to cross-sell products or services. Coupled with this is the need to ensure customers are treated fairly, their money is protected, and there is transparency.
- Licencing: evaluating the business models of fintechs and other third-party service providers to understand the risks and opportunities they bring to the financial system.
- Establishing the parameters: agreeing on common standards on how the industry would work together. Lessons from international markets show that the costs for open banking can be crippling to the banking industry, therefore it's imperative for regulators to follow a phased or targeted approach, focusing on the areas that can add value to customers.

At the heart of open banking is the concept of customer control over data, and its protection by the recipient organisation. This is achieved through robust technical standards, revised consumer contracts, cybersecurity requirements and granular consent mechanisms.

Open banking is a boon for service providers and customers alike because it gives providers secure access to their customers' financial information, enabling them to create and introduce more effective and efficient products and services to meet customer needs. It also gives customers greater control of their finances and data by offering a comprehensive view of all their accounts on online or mobile platforms.

Further benefits include:

1. Easy sharing of transactional data with third-party providers;
2. Easier account comparison and switching;
3. Better savings decisions through more transparent savings account terms;
4. Easier and quicker access to credit for FinTech companies and small businesses;
5. More secure and safe infrastructure by moving away from screen scraping and credential sharing.

To truly benefit from these opportunities, we will need to overcome the obstacles they present. The major hurdles include a lack of regulations to govern the concept, risks associated with data, data sharing and privacy, a lack of maturity and knowledge in banks and financial services providers about how to implement open banking, and market readiness and competition issues within the sector.

Because data sharing has been identified as a major risk, there are concerns that open banking will bring more risks than benefits. These concerns include users not understanding that the service is not free and that the cost of the service is payment with their personal data; not being able to control who their data is shared with; and not knowing which party or provider is responsible for the loss of their data if a breach occurs. Regulatory changes will need to happen and the risks associated with data and privacy need to be addressed to unlock its benefits.

Open banking is already gaining traction because of the possibilities it unlocks. More than 22 countries around the world have developed and implemented frameworks around it and are already seeing its value, because of the opportunity to make the financial infrastructures more efficient, and its ability to serve more people - a goal that has not yet been achieved by the commercial sector alone.

Findings of the inaugural Fintech Landscaping Report, looked at the fintech issues that have the potential to reshape South Africa's financial services industry. The report was put together by the IFWG.

Encouraging innovation and competition in banking

Open banking was one of the six main themes that the report identified – and the four key findings around open banking were:

- "Banking is necessary. Banks are not." And banks need to shift their thinking and approach to stay relevant as the industry evolves, moving away from traditional capabilities and infrastructure.
- Open banking could solve for competition in an industry that has traditionally been dominated by large incumbent banks.
- Fintech innovations linked to open banking in South Africa have benefitted large banks, as well as start-ups and have helped drive financial inclusion, but issues surrounding data ownership and privacy do present a risk.
- Regulators can support an open banking environment by providing guidelines for licencing and consumer protection.

The growth of open banking will also allow for greater collaboration between traditional banks and fintech start-ups – enabling innovations such as the ability to provide customers with loans at the point-of-sale (POS) and the development of solutions such as screen-scraping, which allows direct EFT payments to merchants.

This is particularly important in South Africa, where micro, small and medium enterprises (MSMEs) are the backbones of economic growth. These businesses often face challenges like lack of access to capital, credit and critical financial services products. Solutions introduced through open banking could potentially help solve these concerns.

Ultimately, regulators together with the financial services sector will continue engagements to carve a clear understanding of what an open banking framework is trying to solve for in a South African context, and how it should be shaped around the unique needs of the South African market.

ABOUT THE AUTHOR

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