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TRANSFORMATION IN FINANCIAL SERVICES

Digital disruption in financial services, from local, regional and global perspectives

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Good morning, ladies and gentlemen. I'm delighted to have the opportunity to speak to you this morning and grateful to the Banker Middle East and CPI Financial for this opportunity.

INTRODUCTION

Innovation, Challengers, Disruptors, Transformation.

Whatever you call it, there is a lot going on in the financial services sector at the moment. You can't go very far without hearing about digitalisation projects, about better customer experiences, about engaging with millennials.

But why? Changing customer expectations, more competition in the sector from new entrants, technology providing the opportunity to simplify what can be a complex business, the pressure to streamline operations, and other factors, are pushing the drive for reinvention and innovation.

This means different things to different businesses. We have seen some firms focus solely on improving their back office capabilities, while others are focused entirely on customer engagement and enhancing the customer journey. Many are creating new and improved digital platforms.

Technology is not new in financial services, but no firms appear to be immune from the pressure for change. Centuries old banks, insurance providers with legacy systems, household names - none remain unaffected either locally or globally.

The transformation journey can be challenging. Some firms have technology and adaptation in their DNA, many do not. Those that do not will need to shed old habits, update cultural norms, upskill their employees, and adjust their way of thinking to become a digital business. Learning to connect the dots between digital initiatives, strategy, and business enablement will be critical.

1. Technology in the financial services sector

When we talk about digital transformation, what technology are we talking about? We know that many in the sector are looking at using Artificial Intelligence (AI), Distributed Ledger Technology, or blockchain, as well as cloud computing, advanced analytics, robotic process

automation, and so on. You have sessions today looking at many of these topics. Some of this technology is genuinely new, some is not. The ongoing development of multiple delivery channels is also not new, but has been accelerated by change in technology and in customer demands.

From a regulatory point of view, we aim to be technology neutral, both in the requirements we place on firms and in how we supervise. We want firms to have the right staff with the right skills to work in this area and for firms to make sure that digital transformations and upgrades are carried out effectively. For example, if using AI, we will ask whether you really understand how the AI solution is delivering the outcomes it was intended to deliver? We want you to be on top of everything that is happening. One of the drivers of the 2007/8 financial crisis was that only a small subset of people understood some of the complex products in the market and that company boards, in

particular, were not able to challenge what management told them, as they did not understand enough about what was going on. We all have a responsibility to make sure that the same does not happen with technology deployment.

Regulators are also using new types of technology, as we ourselves look to become more efficient, to manage risk more effectively, and to engage in better ways with our stakeholders. For example, the DFSA has introduced a digital application process, branded as 'Forms Online', for many of our applicants. Of course, we haven't just taken the paper forms and put them online – we have looked to revise the way we capture information, to facilitate automation and analysis, and re-engineered our processes around applications. As you all know, using technology and becoming more digital is not simply a matter of doing the same things as before, but with different tools. Instead, it is about doing things differently and better.

We are also looking at digital KYC/AML and the solutions that may be available in this area. Firms in the DIFC are using digital solutions in this area, to provide digital on-boarding to their prospective clients, and we are happy to discuss how firms might want to do this.

We are also looking at how we might make our rules machine readable - digitising and automating the interpretation of regulations. The end product will tell the user exactly what regulatory standards need to be followed based on the activities being undertaken by the firm. Globally, regulators are also looking at how they can become "more digital" with many initiatives under way.

2. The speed of change

As I suggested earlier, speed of adoption and change varies. A report from Gartner¹ earlier this year stated that almost half of global financial services organisations are still in a very early or

¹ <https://www.gartner.com/smarterwithgartner/the-5-digital-transformation-identities-of-financial-services-organizations/>

even immature stage of their digital transformation journey. Of course, that means that many are more advanced than that.

I think there are a few reasons for the varying pace of change:

First – as I have already mentioned in relation to our own experiences, financial services firms have realised that digital transformation is not achieved by simply adding or replacing technology systems without changes to underlying business processes. Rather, a wider transformational change is required to keep up with and leverage the success of the disruption that is being seen. This takes time.

Second - legacy issues. Many financial institutions have to deal with old IT systems. For many global or large players, these systems have grown through merger and acquisition, without adequate systems integration, and the number of people who understand how things fit together, and so how change can be facilitated (if indeed the systems can cope with this), is small.

Third – cost. These sort of changes are not cheap and the changes often required are complex. The right people need to believe this is the right thing to do and put resource into it; they also need the right expertise to drive these projects.

Fourth – culture. Many firms recognise that they are not agile – their scale often prevents this. Decision making processes can be slow. They also see that radical change is not part of their corporate culture. Often, firms try to address this by separating, or somehow carving out, teams to be more entrepreneurial and agile, and to develop the firm's new digital identity, for example, in parallel with the existing business. Separate branding can lead to cannibalisation of the legacy business, but perhaps it is better to cannibalise your own business than be eaten by someone else.

Lastly – regulation. While many regulators, including the DFSA, support and want to facilitate technological change in financial services firms, there is no doubt that actual regulation of some areas can be slow to change, which can slow down adoption of new and disruptive technology or business models.

While these points may explain the varying pace of change, what is clear is that all are changing. There are many examples in Dubai, the UAE and the region of such change. But this isn't limited to the financial services sector. For example, in Dubai, there is a commitment that all government services will be effectively paperless by 2021. The UAE government has launched the Emirates blockchain strategy 2021, which aims to have 50% of government transactions delivered using DLT by 2021.

International and supranational organisations are supporting innovation. In late 2018, the IMF and World Bank launched the "Bali FinTech Agenda." This sets out a framework of 12 elements that IMF member countries should consider in their domestic policy discussions when developing their approach to innovative products and services in the financial sector. The framework aims to ensure the sector is resilient, that risks created by the use of various technologies are addressed, and to

promote international cooperation. This Agenda is something the DFSA strongly supports.

3. Embracing transformation and disruption

Much of the transformation we have seen has been driven by those seeking to challenge and disrupt the sector. Some challengers compete with established firms to try and take market share; others are looking to engage and collaborate; there are many models.

Change has also been driven by demand for improved customer experiences, which is more than just customer service these days. From what we see, customer experience refers to a customer's overall journey from start to finish, including every touchpoint and interaction along the way; this is evolving rapidly with technology being used to enhance every step along this journey. Today, a good customer experience may include anything from being able to carry out all your account activities on your mobile phone, to getting a question immediately answered by a chatbot, to having information pushed to you to help you manage your finances. Tomorrow – well, the technology is the limit, rather than the sky.

We believe the tone is set from the top; in the UAE the tone was established by the National Innovation Strategy, which was set out by His Highness Sheikh Mohammed Bin Rashid Al Maktoum, UAE Vice President and Prime Minister and Ruler of Dubai, in 2014, with the aim of creating an innovation-friendly ecosystem. This has been critical to support digital transformation in the UAE. One major goal was to establish a stimulating environment for innovation, in the form of supportive institutions and laws, and there are many examples of this being done. This has gone a long way to supporting industries and their desire for digital transformation.

In the DIFC we have embraced this Strategy and there is a strong focus on supporting innovation, including via DIFC FinTech Hive. The Hive was established in 2017 to support the innovation ecosystem in the DIFC, and was the region's first financial services incubator/accelerator programme. The Hive programme gives all types of technology firms access to accelerator programmes, mentorship from leading global and local financial institutions, a dedicated "cost-effective" space to work, and a community of like-minded individuals, as well as access to products and services in front of the region's largest financial community. There are currently more than 80 firms registered in DIFC Fintech Hive, from over 30 countries, with over 40 start-ups having been through their accelerator programmes. The fourth accelerator programme has just commenced with 31 innovative firms from all over the globe participating.

It is not only programmes like this that help support the digital transformation in financial services, regulators play their part. In 2017, the DFSA established the Innovation Testing Licence (ITL) – a licensed regulatory sandbox. This allows firms to test and develop innovative business models, products and services in or from the DIFC, with the full regulatory requirements applicable at the point they are ready to leave the sandbox, not when they enter it.

Other regulators in the region are also supporting the digital transformation in finance. For example, in Saudi Arabia this year, SAMA has launched a regulatory sandbox to understand and assess the impact of new technologies in the market, allowing local and international firms to enter the Kingdom to do so.

At the global level, the Global Financial Innovation Network (or GFIN) was set up in 2018 as a way for financial services regulators across the globe to collaborate, promote consistent regulatory engagement, and increase the speed of cross-border

adoption of emerging technologies. In order to assist innovative firms in scaling new technologies across multiple jurisdictions, a cross-border testing pilot was announced in early 2019. Demand for this cross-border testing was high and regulators are working with firms in the pilot to try and improve the inefficiencies of working between multiple markets.

4. The increasing use of data

Financial firms are starting to find ways to unlock the value of the vast amount of data they hold and to use it to gain insights into their customers to anticipate their needs, and – recognising reality - use those insights to develop more products, cross-sell products and services and understand customer purchasing behaviours.

Many countries have introduced Open Banking requirements, so that other firms can also make use of these data, to analyse and identify market opportunities. We think it is only a matter of time until similar access to data is available in the UAE and in the region.

With the increased use of data there is now a growing amount of regulation in this area; firms need to think about data privacy and security in a new way. This presents firms with challenges in how to meet these additional requirements. This can be problematic, for example, when a firm wants to analyse all its data, but data localisation rules mean that certain data sets cannot move outside, or across, national boundaries. But appropriate protection of individuals' personal data is essential.

5. Cyber

I have focused on the positives of digital transformation in the sector, and the benefits it can present to both the firm and their consumers, but there are threats. The financial

and reputational risks resulting from cyber-attacks and incidents are now one of the biggest threats to the sector. This concern is understandable given the surge in high-profile cyber incidents in 2017 and 2018.

So what can financial services firms do? Clearly the priority is to prevent a cyber-incident from occurring, but many have said that it is a question of “when”, rather than “if”, a breach will occur. It is vital to have an effective response strategy so that attacks can be quickly and effectively detected, analysed and responded to. Knowledge sharing and industry collaboration is also important to stay ahead of the threat.

At the DFSA we are increasing our focus on cyber risk and, in particular, we are focusing on firm resilience to cyber incidents. The DFSA is in the process of launching the region's first regulator-hosted cyber threat intelligence platform. The platform will be available to all companies (regulated and non-regulated) operating in or from the DIFC, and the objective of the



platform is to facilitate the development of a community of information sharing. The DFSA will host the platform on its infrastructure and will outsource management of the platform to a third party cyber security specialist firm.

CONCLUSION

In conclusion, everyone is having to run faster to keep up with the pace of change in the industry, and to make effective use of technology both to protect existing markets and to develop new ones. We, and many other regulators, are supportive of this trend, but recognise that there are challenges and that risks need to be well-managed.

I've talked at a fairly high level about the changes we see, locally, regionally, and more broadly. I hope the rest of the day is useful for you as you think about how you can best be part of the opportunities and challenges that technology brings.