

CAPCO

OPEN FINANCE

CURRENT STATE OF PLAY & LESSONS FROM OPEN BANKING



OPEN FINANCE: BACKGROUND

Open Finance will see the extension of the core Open Banking concept of making customer payment and bank account data safely available to share with regulated institutions, into the realm of consumer credit and investments, pensions, general insurance, and mortgages. Open Finance will therefore extend the impacts of open APIs in finance, to customers who employ any of these services and beyond banks, building societies and customer credit firms to the following financial services providers:

- mortgage lenders and intermediaries
- financial advisors
- general insurers and insurance intermediaries
- investment managers
- life insurers and pension providers
- Fintechs and innovative third parties in the wider financial arena e.g. pensions, insurance.

The Financial Conduct Authority in the UK has made a clear commitment to supporting the expansion of open APIs in the Financial ecosystem, through its 'Call for Input'¹ issued in December 2019. The FCA was due to publish a paper based on responses to the Call for Input in March but this is now due in October 2020.

As we await the FCA's feedback, we consider the outcomes and lessons learned from Open Banking and look ahead to the potential of Open Finance (OF) to share insights including: benefits and use cases, the projected course for Open Finance in the UK, thoughts on how institutions will need to prepare to participate, and the likely timelines for roll-out.

WHAT ARE THE POTENTIAL BENEFITS OF OPEN FINANCE TO CUSTOMERS?

We have identified five key benefits of Open Finance for customers:

1. More suitable products & services offered

- Tailored products and services offered that suit a customer's overall profile and requirements
- Improved suitability assessments based on a holistic picture of a customer's financial position
- Previously inaccessible products unlocked for some customers
- More accurate creditworthiness assessments, access to cheaper finance, better credit options for consumers struggling to access credit, restricted access to credit that is fair and more readily available debt finance.

2. Easier to compare and switch providers

- Open Finance can automate switching and renewals so encouraging shopping around for alternative service providers. This will help consumers get more value from their provider and combat scenarios where customers are unaware that they are overpaying for a product or service
- Open Finance could make it easier to compare price and product features
- It has the potential to improve competition among financial services providers.

3. Improved financial management

- Individual / SME account financial management dashboards would enable a better understanding of, and more opportunity to improve, a customer's overall financial position (cash flow, insurance, investments, spending, goals all in one place), in turn improving their overall financial wellbeing

- Potential to help a consumer understand whether to put an additional £100 into a savings account, mortgage overpayment, or pension – and execute that payment on the consumer's behalf²

- More informed choices and better financial opportunities available for consumers that could in turn raise demand for products and services.

4. Fairer pricing & more financial inclusion

- Price quotations for products could be more competitive, with products more tailored to a client's needs rather than being generic
- Improving customer access to product offerings and financial advice that is relevant but has not so far been accessed (either due to price, ease of access).

5. Loyalty & rewards programs

- Some of the most popular features for Open Finance identified by consumers are loyalty and rewards³
- Providing more rewarding loyalty points collection systems will incentivize consumers to buy and use more insurance products
- Programs will also provide more transparency around consumer spending habits, helping them to earn more loyalty advantage points.

WHAT DOES OPEN FINANCE MEAN FOR PROVIDERS OF BROADER FINANCIAL SERVICES?

Open Finance will benefit financial services providers, enabling them to deliver improved customer experiences and optimize their service offerings. It will also introduce fiercer competition, widen the marketplace with new and disruptive entrants and encourage more innovation amongst traditional players. Here are the benefits to the industry at-a-glance:

1. Deliver an improved personalized customer experience

- Information can be more easily shared with financial advisors, making the customer experience more streamlined and efficient
- PSD2 & Open Banking have driven high standards of secure access to banking systems. We are likely to see the trend towards multi-factor authentication (often including biometrics) extend to other financial products, meaning both more secure and more efficient access & onboarding experiences for customers
- Institutions will be able to make transactions or changes on a client's behalf, e.g. payments, switching accounts or making investments.

2. Increase customer account oversight

- Account managers will have access to a holistic view of customer account data, and for example across their savings, pensions, investment accounts and mortgage position
- There will be a better understanding of a customer's overall financial circumstances, enabling improved and more informed advice.
- Firms will minimise risk and gain a better understanding of a customer's requirements.

3. Improve service offerings

- Increased transparency and aggregated views of accounts will enable firms to develop existing and build new services and offerings, meaning new revenue streams for providers
- Competition between existing firms will be increased, encouraging enhanced capabilities and innovation.

4. Innovation and wider marketplace

- New market entrants and third-party providers (TPPs) will drive innovation and increase the quantity and quality of application-based offerings in the market
- Market differentiation in areas such as pensions, currently dominated by a few major players with similar offerings
- Opportunities for partnerships with fintechs and TPPs, allowing existing smaller providers an opportunity to form alliances and cross-sell products and services to consumers

Case Study 1: UK Pensions

The UK pensions market is dominated by a relatively small number of players and has traditionally been considered an area of financial services where there is low competition, a trend towards consolidation, limited transparency around both product investment decisions and fees data and characterized by very low levels of customer engagement.

Our review of the potential for Open Finance in the pensions space has identified the following themes:

- **Inclusion for those not in a traditional workplace/self-employed:** By making choices easier and pensions more visible, there is an opportunity to incentivise pension saving amongst those in the non-traditional job market.

- **Better security of information:** By moving to digital communications – customers are currently required to sign and send paper forms for almost all pension related correspondence.⁴
- **Increased “ownership”:** Individuals with defined pension contributions will have the ability for more hands-on management and forecasting for retirement from their aggregated pension pot and in the context of their other investment accounts. Open Finance (along with initiatives such as the Pension Finder Service) will help consumers reclaim occupational pension schemes that have been forgotten and aggregate all pension pots in once place.
- **More transparency & pro-active investment selection:** More visibility of pension investments will encourage more proactive engagement from customers: Are my investments sustainable and ethical? What is the impact of x/y/z on my portfolio? What has been the impact of recent stock market movements on my returns?
- **Improved modelling of future retirement provision:** there is the opportunity for incumbents and TPPs to provide lifetime/retirement forecasting tools due to improved data, which will help customers to understand the impacts of their decisions on future pension provision. TPPs like Intelliflo are already leveraging Open Banking capabilities to enhance advisory offerings to clients.
- **Transparent fee structures:** exposing historic fees, AMCs, trail commissions charged to customers by pension providers will enable them to easily compare providers and thus we are likely to see more switching which will in turn drive more competitive pricing amongst providers. It will also likely see providers upselling to customers that they merge their various pension pots; they will be able to model the benefits of lower overheads of a single pension pot in the long-run in comparison to fees being paid today. We will therefore likely see more consolidation, as well as more switching of providers.

- **Automated pension top-ups:** Enablement of automatic pension top-ups, e.g. if your cash savings account reaches x threshold it is moved across to your pension account. This has potential to assist reversing the under-provisioning currently in pensions and should result in an overall increase in savings.

Case Study 2: General insurance

The UK general insurance market is highly competitive, fragmented, and diverse, offering a broad range of products. Whilst the industry has been characterized by stability it has a limited record when it comes to innovation with consumers who fail to shop around, thus often penalized by rates that are less attractive than those offered to new customers.

Our review of the potential for Open Finance in the general insurance market has identified the following themes:

- **Risk-based pricing:** Better risk-based pricing on insurance products based on more visibility of customer’s financial and historic data around spending, and claims history etc.
- **Direct customer interface:** Insurance carriers and customers can have a direct interface, where previously traditional intermediaries have owned customer interactions enabling insurers to improve their customer engagement⁵.
- **Optimised claims management & fighting fraud:** OF will give insurers the ability to view a customer’s bank account and reconcile event costs with insurance owed, ensuring correct amount is reimbursed, and enabling insurers to combat fraud.
- **Personalised advice & alerts:** Customers will receive more personalized insurance advice, claims renewal alerts, advice on switching.
- **Automation of operational processes:** OF will help facilitate the movement away from paper heavy communications to digital methods, it will enable swifter processes for e.g. through the ability to reconcile an insurance claim with an account debit, etc.

HOW SHOULD IN-SCOPE SERVICE PROVIDERS PREPARE FOR OPEN FINANCE?

Consider the timelines...

The timelines for Open Finance should become clearer with the next FCA publication, however we envisage a phased approach. Firstly, we expect an expansion into other homogenous retail banking offerings (outside payments), e.g. savings, loans, and mortgages. This will be relatively low effort with minor changes to current OB standards and regulatory framework required. Pensions are likely to be the next priority given the OF initiative can run in parallel with efforts already underway to develop a pension finder service and dashboards in this space.⁶ OF for insurance, investment accounts and other complex and less standardized products will likely take longer to implement, as much preliminary work will be required to cleanse and standardize data first.

Look at the lessons learned from Open Banking...

A number of takeaways from the roll-out of Open Banking will be applicable for Open Finance and companies should invest time in exploring key themes that emerged, including:

- The complexity in implementing open sources in large banks with legacy infrastructure will see the increasing preference to deploy new technology on a modular basis rather than wholesale system upgrades and complex migrations
- Open Banking used the ISO 20022 standard for financial data as the basis of the APIs. This forced banks to represent their data in a standardized form for easy comparison and interoperability across providers. Open Finance will push similar standards forward on the industry more broadly. This will likely lead to providers modifying their core platform to closer align with industry standards. Businesses with no clear API strategy or unreliable APIs will limit the benefits and critical mass of Open Finance overall

- Open Banking defined robust security standards for banking APIs – more advanced than banks had typically used previously. This prompted upgrades of security standards across the banking API ecosystem in the UK. The industry now has a much higher bar for API security. API availability, developer ecosystem and general quality and interoperability standards have also been driven forwards. These upgrades in higher standards have made the ecosystem much more usable for integrators allowing many more players with new ideas and platforms to get involved. We are likely to see similar ecosystem improvements in Open Finance
- The emergence and customer adoption of new, tech-enabled market entrants in the payments and retail banking space, such as Monzo and Starling, has shown that digital-only money propositions are not only possible but popular; this is a likely trend for Open Finance too
- Expect the unexpected – Open Banking has shown that openness and transparency of data can lead to unexpected benefits. For example, TrueLayer using Open Banking as part of the response to COVID-19.⁷

We recommend firms now focus on the following nine activities:

1. Confirm the scope of your Open Finance initiative so the objectives and priorities are clearly understood by all.
2. Adopt a digital first mindset and consider the target operating model required to support Open Finance, e.g. strategy to standardize and digitize data.
3. Re-learn the lessons of Open Banking. Getting into a cycle of building new platforms, release incrementally, learn from early integrators and improve services. Develop APIs with a product mindset and focus on improvement of current API performance.

4. Define the right environments to build and deploy these services, how integrated are they to the core systems, what security controls protect the core systems.
5. Embed good development practices into your new service builds, logging, auditability, health monitoring etc.
6. Build an open relationship with the regulator.
7. Develop relationships and testing opportunities with TPPs.
8. Develop carefully prioritized implementation roadmaps.
9. Look to Australia, Brazil, the US, and Canada (Financial Data Exchange) to understand and learn from their Open Finance journeys.

HOW CAN CAPCO HELP CLIENTS?

Our proven experience acting as the delivery partner for Open Banking programs in tier one banks, along with our core capabilities in relevant disciplines to any OF initiative (as outlined below), make us a reliable choice to support clients on their Open Finance journey.



TPP Assessment & Onboarding

- Baseline assessment / gap analysis of TPP's registration journey
- Future state journey options & quick wins
- Analysis of industry trends / competitors
- Advisory on ways to expand value proposition through integrations with strategic partners



Project Mobilisation & Execution Oversight

- Resource Management
- Planning
- Financials
- RAID Management
- Change analysis and planning
- KPI Management & Tracking



API Test Assurance

- Gap analysis & recommendations
- Documentation of test scenarios and accompanying journeys that could be leveraged across all environments
- Automation & integration into test suite
- Exploratory testing and testing of customer redirect journeys



Compliance Advisory

- General advisory and implementation strategy of regulatory standards
- Proven experience on topics such as standing orders / scheduled payments, dynamic client registration, customer authentication and ops requirements



Architecture Reviews & Solution Design

- Detailed current state assessments & Research, detailed guidance and support in sourcing or design
- Options appraisal (build vs. buy) for future state solutions e.g. certificate management and verification services



TOM Design & Delivery

- Analysis of open data requirements
- Assessment of AISP/PISP journeys
- Scoping operating model impacts on core business areas
- Design of new customer journeys (both traditional and TPP focused)
- Regulation advisory support
- Third-party operating model delivery

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ABOUT CAPCO

Capco is a global technology and management consultancy dedicated to the financial services industry. Our professionals combine innovative thinking with unrivalled industry knowledge to offer our clients consulting expertise, complex technology and package integration, transformation delivery, and managed services, to move their organizations forward.

Through our collaborative and efficient approach, we help our clients successfully innovate, increase revenue, manage risk and regulatory change, reduce costs, and enhance controls. We specialize primarily in banking, capital markets, wealth and asset management and insurance. We also have an energy consulting practice in the US. We serve our clients from offices in leading financial centers across the Americas, Europe, and Asia Pacific.

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