

Study in focus: Competition issues in the Area of Financial Technology (FinTech)

BACKGROUND

Technology has created new opportunities to develop numerous financial services in recent years. The number of these so-called 'FinTech' services and their providers is constantly growing and still developing. Among the most relevant innovations are new banking and payment alternatives and financial tools such as mobile wallets, cryptocurrencies and crowdfunding. However, in spite of the infinite possibilities that technology provides to the market, the interaction between the traditional incumbent financial services providers, newcomers and technological companies combined with the lack of concreteness of the technological services nature can bring new competition and regulatory challenges to the market.



FOCUS OF THE STUDY

Against this background, the study aims to introduce the current and potential competition issues related to the boom of the financial technologies development. For this purpose, the current features of the FinTech ecosystem, including the services, the relevant market, the user's perception and the providers of such services are described. Potential anticompetitive factors and their impact on the relevant market and a selection of most developed FinTech services are discussed. In a further step the study analyses the detected competition challenges with view to the current competition instruments in order to reflect whether these instruments are able to cope with the anticompetitive issues.

KEY FINDINGS

The European financial context and the European FinTech market

The FinTech services are framed into the general digital transformation of businesses and have resulted in lower barriers to entry, disintermediation of the current value chain, new business models based on platforms and sharing economies and more efficient provision of services. The main actors involved in such technologies are newcomers, such as start-ups, traditional financial services providers and technological companies, which so far have not been active in providing financial services. They represent more than 3800 companies globally, of which 1020 are located in the EU. On the basis of a comprehensive description of the market, rather than specifying FinTech companies, the study names minimum criteria to define the services provided as FinTech and proposes a classification of seven key FinTech services by taking into account the currently offered FinTech services as well as those that are expected to be provided in the coming years. These services include: (1) banking; (2) payments, (2) transfers and Forex, Digital currencies, (4) Wealth and Asset management, (5) Personal financial management, (6) Insurance and (7) Enabling technologies and infrastructures, such as artificial intelligence and cybersecurity.

Competition issues in the FinTech sector

Many of the issues discussed, favoured by the expanded and abstract scenario created by the technology, are still hypothetical since most of them have not occurred so far. Multi-sided markets, such as FinTech platforms, make it difficult to define the relevant market with the traditional models used in competition. The study uses a matrix featuring the supply and demand perspective to explain at which instances competition issues could arise. Since FinTech services are constantly evolving, analysis is made along the dynamics within the new web-based business



models. From the **supply-side** the provision of services via online platforms and the intensive use of data are technology related reasons to explain competition issues. From the **demand-side**, competition challenges depend on access and operation of the technology by the user perception and behaviour. Independent from business models, common competition concerns include:

- the interoperability between technologies that may be used by incumbents as a market barrier for new entrants; however standardisation may lead to reduced ambitions to innovate;
- the definition of the relevant market and the question if services can be considered as substitutes depend from how users perceive and use the platform. If certain patterns are developed, the role of network effects has to be considered to assess where market power comes from;
- the use of data-intensive technologies brings along the issue of data portability and the ability to exclude certain users; access and use of data can lead to market power and if datasets are cross used and allow to leverage a market position gained in a different sector into the provision of FinTech services.

In **banking** for instance, the disparity in the approaches of national regulators could act as a barrier of entry for new players. Furthermore when lending services of digital platforms cannot be considered as pure P2P services, competition may be limited when these firms take advantage of their consolidated position in offline lending services to create their own digital platform to sell loans, avoiding investing in other platforms. Also, if big digital companies may decide to leverage their market power gained in finance related services such as e-commerce to start offering lending services taking advantage of customer data they already have allowing them to develop more accurate credit scoring tools or apply predatory pricing strategies.

Taking another example from the field of **cryptocurrencies**, issues of competition between different cryptocurrencies (intercryptocurrency market) may arise in the form of network effects. Given the dependence of a platform and a network, a large number of users and an increased use as payment causes substantial barriers to entry for new cryptocurrencies and give incumbents significant market power. There is a risk that at some point this may even lead to potential collusive agreements between members.

Assessment of the current competition instruments and conclusions

The study assesses that in **multi-sided markets**, such as FinTech services regularly provided via platforms, the definition of the relevant market faces difficulties when using the traditional concepts developed for business models where value is generated by the supplier of a product/service and then sold to a customer (pipeline). For instance, **network effects** have to be closely observed because they can enable large FinTech platforms to insulate from competition, however concerns do not arise in every case. The role and the use of **data** has to be taken into account, especially when assessing merger cases. Possession and access to data can mean a competitive advantage which may lead to anticompetitive effects if access is refused or use is limited to exclusive contracts. The explanatory matrix used in the study shows that some of the challenges for competition fall outside of the scope of competition tools and might be more adequately addressed by sector specific regulation.

Despite of anticompetitive factors FinTech have an important potential to disrupt markets by lowering barriers of entry. With view to the on-going market evolution **research** and **close monitoring** of developments should still receive preference. Any policy approach should depend on the type of service and the maturity of the relevant market. Any financial regulatory reform should consider competition issues from the beginning because it is working not only as one of the primary entry barriers for new service providers but also as a source of legal certainty for all market participants.

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