Canada is woefully unprepared for the FinTech tsunami[1]

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Our financial sector is navigating monster waves of disruption as it fights to remain a global industry leader. So why isn't Ottawa captaining a strategic course?

The buzz word *FinTech* covers a range of financial technologies that enable consumers to access financial services over their mobile phone or the internet. Through the many FinTech innovations introduced over the past five years, retail customers can take out a loan, make a payment, transfer money overseas, or invest their savings electronically. Customers enjoy a better experience at a lower cost by transacting via a simple interface that is easier to navigate than traditional brick-and-mortar businesses. And for many of these services, customers bypass traditional financial intermediaries who have profited from this activity, such as banks, mutual fund dealers, and money transfer companies.

While the FinTech wave arguably started decades ago before the term FinTech was coined, the global financial crisis turned this swell into a tsunami, as many consumers lost trust in traditional financial intermediaries. Technology, the loss of trust, and the arrival of mobile-first millennials are driving this paradigm shift in financial services.

Over the past year, the pace of FinTech innovations has accelerated as the first-generation of technologies that enabled this digital transformation – such as mobile phones, cloud computing, and peer-to-peer networks – have been combined with newer technologies such as blockchain, machine learning, and artificial intelligence. These technologies not only lower the barriers to entry into banking, they have opened the doors to non-traditional players ranging in size from small start-ups to giant technology companies. The question is how much of the disruption witnessed in other traditional consumer businesses – think of book and music stores, video rentals, hotels, and taxis – will be seen in the financial sector? And what will happen to the incumbents that currently dominate this sector and our economy?

As a country, you would think Canada should be well-positioned to benefit from the FinTech tsunami due to our leading financial services sector, our highly-educated workforce, our diverse and

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spread-out population, and our pool of talented entrepreneurs and investors. You would be wrong. Rather than leading in the development and adoption of FinTech innovations, Canada is lagging countries such as the United Kingdom, the United States, Hong Kong and Singapore who have been quicker to seize on the opportunities presented by this technological disruption. Canada is being held back by the lack of a national strategy and the absence of a FinTech champion to provide leadership in this vital sector.

What should Canada be doing? Let's take the example of Australia, a parliamentary democracy of 24 million inhabitants with a stable, concentrated financial system and an economy dominated by services (70% of 2016 GDP) and the export of natural resources, energy, and food. Sound familiar? Much like Canada, the Australian banking sector came through the crisis largely unscathed, owing to the same prudent policies, conservative risk-taking, and strong leadership seen in Canada. But when it comes to the FinTech tsunami hitting our economies, the similarities end there. Australia has an "emergency preparedness" plan, Canada does not.

In March 2016 Australia's Treasurer – the equivalent of Canada's Finance Minister – published their national strategy in a document titled "*Backing Australian FinTech"*[2]. The report outlined commitments and initiatives being undertaken by the government and other bodies to support and promote Australia's FinTech sector, including: creating a FinTech Advisory Group; introducing funding and tax incentives; reforming insolvency laws to encourage angel investment; promoting FinTech exports and partnerships; addressing data accessibility and cybersecurity issues; and encouraging government procurement of FinTech. The report even has a dedicated website to track progress towards this goal. [3]

The catalyst for the Australian government's response was perhaps the threat of losing talent abroad. In September 2015, the UK government invited nine leading Australian fintechs on an all-expenses paid trip to London, England, to convince them to relocate. This followed several years of lobbying by the private sector and regional and city governments. In October 2014 the Committee for Sydney and the government of New South Wales commissioned a critical report on Australia's FinTech sector.[4] In May 2015 these parties established a FinTech hub and co-working space in Sydney called Stone & Chalk, modelled on Level39 in London. They then formed a new industry body, Fintech Australia, who outlined in a manifesto how the federal government could build a thriving FinTech ecosystem.

[2] The report is available at: http://fintech.treasury.gov.au/files/2016/03/Fintech-March-2016-v3.pdf, accessed January 9, 2018.
[3] The Australian government's dedicated website is: http://fintech.treasury.gov.au/, accessed January 9, 2018.
[4] KPMG, "Unlocking the Potential: The Fintech Opportunity for Sydney", October 2014.

The message was received. In February 2016, Australia's Prime Minister established an expert FinTech advisory panel with a mandate of making Australia a leading player in Asia. The panel's 13 members drawn from banks, venture capital firms, and FinTech start-ups published its top three obstacles to achieving Australia's ambitions, namely: a lack of government procurement, the over-regulation of equity crowdfunding, and the absence of a regulatory sandbox to help start-ups navigate the regulatory system.[5] This input led to Australia's FinTech strategy published in March 2016. Several months later, Treasurer Morrison backed up these promises by announcing financial support in Australia's budget. Finally in December 2016, Australia's securities regulator launched its regulatory sandbox and innovation hub while pursuing outreach to securities regulators in Europe, Singapore, and the United States.

Australia is not alone in publishing a national FinTech strategy championed at the highest levels of government. The UK, Hong Kong, and Singapore have each published strategies, and in each case the head of the Finance ministry was behind it. What these four countries have in common are their small size relative to their neighbours, their large financial sectors as a share of GDP, their dependence on exports particularly of financial services, and their vulnerability to shocks from abroad. Canada shares these features, but lacks their leadership and strategy for the future.

What's at stake if Canada does not get its act together? In 2016, Canada's financial sector represented 7.0 percent of GDP and 4.4 percent of all jobs in Canada. This important sector is at risk of disruption from abroad, enabled by technologies that eliminate borders and other barriers to entry. It does not cost any more to access a foreign website than a Canadian one. And as shown with the growth of Netflix, Canadians are happy to pay for foreign over domestic content even in a so-called protected industry. While the entry of foreign players may lead to better service for Canadians at a lower cost, it would be infinitely better for Canadians if we developed these FinTech abilities domestically and exported them abroad, particularly to the US market.

To accomplish this goal, Canada needs a national strategy. Regional initiatives by provincial governments or municipalities like Toronto and Montreal – while positive – will not suffice to develop a world-class industry. The elements of Canada's strategy can be drawn from the plans of other countries such as Australia. All Canada needs is a national champion, and the evidence from other countries points squarely at our Finance Minister. Mr. Morneau, it is time to take the wheel and steer Canada through the Fintech tsunami.

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[5] See: http://fintech.treasury.gov.au/working-with-australias-fintech-industry/, accessed January 9, 2018.

Exhibit 1: Key Elements of Australia's FinTech Strategy

Define a FinTech Strategy: Australia has set out a clear strategy and agenda for the FinTech sector in collaboration with the industry and other key stakeholders.

Set Up FinTech Advisory Group: The Australian government has established a FinTech Advisory Group to advise the Treasurer directly on issues important to Australia's FinTech industry.

Support for Innovation: The Australian government launched the National Innovation and Science Agenda to improve funding for start-ups. The government created a new independent statutory board, Innovation and Science Australia (ISA), with responsibility for providing strategic advice to the Government on all innovation matters. The Australian government is investing $36 million over five years in a Global Innovation Strategy and establishing five 'landing pads' (in Tel Aviv, San Francisco, Shanghai and two other locations).

Funding and Tax Incentives: Australia introduced tax incentives for investments in early-stage innovation companies. These incentives include a 20 per cent non-refundable tax offset on investment capped at $200,000 per investor per year and a new 10 year capital gains tax exemption for investments held for 12 months.

Develop and Attract Talent: Starting in 2016–17, Australia is committing $112 million to equip its future workforce with STEM skills. Australia also introduced a new Entrepreneur Visa.

Support for Incubators: Australia is committing $8 million to an Incubator Support Program and will offer matched funding to support development of new incubators and accelerators.

Reform Insolvency Laws: Australia is reducing the current default bankruptcy period from 3 years to 1 year; introducing a 'safe harbour' for directors from personal liability for insolvent trading; and making ipso facto clauses that allow contracts to be terminated solely due to an insolvency event unenforceable if a company is undertaking a restructure.

Promote FinTech Exports: Australia is working with regional partners to develop the Asia Region Funds Passport that will waive or diminish key regulatory impediments to trade. Australia's securities regulator has signed formal Cooperation Agreements with the UK and Singapore.

Data Accessibility: The Australian government has tasked the Productivity Commission with considerating the up-take of comprehensive credit reporting data as part of its inquiry of data accessibility. Non-sensitive government data will be open by default and available for free.

Address Cybersecurity: Australia is providing $30 million through to 2019–20 to establish a new industry-led Cyber Security Growth Centre to grow and strengthen Australia's cyber security industry.

Regulatory Sandbox and Innovation Hub: Australia's national securities regulator has launched a 'regulatory sandbox' and an Innovation Hub to help FinTech start-ups get set-up and navigate the regulatory system.

Technology Neutrality Principle: Australia committed to amending priority areas of existing financial regulation to ensure they are technology neutral, and will embed this principle into future legislation.

Government Procurement of FinTech: Australia is looking for ways to use FinTech for government procurement and service delivery needs, and supports the uptake of FinTech services by public agencies.

Source: *Backing Australian FinTech* (2016) by Commonwealth of Australia