HOUSE OF LORDS

Select Committee on Financial Exclusion

Corrected oral evidence: Financial Exclusion

Tuesday 15 November 2016

10.40 am

Listen to the meeting

Members present: Baroness Tyler of Enfield (Chairman); Bishop of Birmingham; Lord Harrison; Lord Haskel; Lord Kirkwood of Kirkhope; Lord McKenzie of Luton; Lord Northbrook; Baroness Primarolo; Lord Shinkwin.

Evidence Session No. 16 Heard in Public Questions 159 - 167

Witnesses

I: Virraj Jatania, Co-founder and CEO, Pockit; Monica Kalia, Co-Founder and Chief Strategy Officer, Neyber.

USE OF THE TRANSCRIPT

1. This is a corrected transcript of evidence taken in public and webcast on www.parliamentlive.tv.

Examination of witnesses

Virraj Jatania and Monica Kalia.

Q159 **The Chairman:** Welcome, and thank you for coming. Do make yourselves comfortable, and I will go through one or two of the formalities. Welcome to this evidence session of the Select Committee on Financial Exclusion. You have in front of you a list of interests that have been declared by members of the Committee. The meeting is being broadcast live via the parliamentary website. A transcript of the meeting will be taken and published on the Committee website, and you will have an opportunity to make any corrections to it, as necessary.

On the subject of interests, Lord Kirkwood will not ask any questions during this session. Lord Kirkwood, would you like to explain why?

Lord Kirkwood of Kirkhope: Yes. For the record, I am looking forward to joining Neyber as a member of its advisory board. I have not yet had the pleasure of attending a meeting, and I am looking forward to that. In order to stay within the rules, I shall be a mere observer of this session, if that is okay with you.

The Chairman: Fine, thank you. I will start by asking you both to introduce yourselves and to explain briefly the nature of your company and the work you do.

Monica Kalia: My name is Monica Kalia and I am the founder of Neyber. The business was started two years ago. Prior to Neyber I worked in investment banking, at Goldman Sachs, as one of the lead analysts, responsible for covering the European bank sector during the sovereign crisis and the sub-prime crisis. That gave me a front-row seat in terms of the challenges caused by the banking crisis, such as depositor protection, and a good window on the crisis's impact on the provision of credit to the consumer and to SMEs. That was one of the reasons why I decided to found Neyber.

We are a consumer lender, so we operate exclusively in the consumer credit space. We lend money to individuals for a range of reasons—debt consolidation, home improvements, car purchases—and we fulfil a range of consumer credit needs. We have a unique route to market: rather than lending to individuals directly, we partner through the employer and offer our solution as an employee benefit. The advantage for us is that we lower our customer acquisition costs, so we can originate loans more cheaply. We can be far more inclusive about who we lend to, because we know more about the individual borrower characteristics—we know who they work for, and we can verify salary et cetera. In addition, we have security of repayment, because we take all the repayments of loan and interest directly from an individual's salary. Essentially, it is a salary-deducted lending model that we think gets around a lot of the issues associated with data and risk that existing incumbent banks are unable to resolve.

In our two-year history, we have managed to secure a unique partnership with an organisation called Police Mutual, and we are now lending to 43 police forces across the UK. We have launched in the last six weeks to four NHS trusts, so we are lending to NHS employees and a range of private sector organisations, including Anglian Water, UK Power Networks and DHL—marquee names that recognise that the financial well-being of their employees is important. Therefore, they are looking to address financial inclusion but also financial education.

The Chairman: Thank you. That is very helpful.

Virraj Jatania: Good morning. I am the founder and CEO of Pockit, which I decided to found about three years ago after a number of years growing up in emerging markets. I moved around quite a lot when I was younger, and from my experiences I had always noticed the inefficiencies of cash-based communities and the problem that leads to for consumers when they are outside the banking system. I built Pockit to solve a problem for unbanked and underserved consumers specifically involving the most basic banking products. It is a place to deposit your money, pay bills and transact in the way that conventional consumers and all of us would be accustomed to.

We are therefore an alternative current account provider in the UK. We provide our customers with a bank account into which they can have their salary or government benefit paid. We also provide 28,000 locations across the UK through a partnership with a company called PayPoint, at which our customers can deposit cash into our accounts. We then allow customers to pay bills through direct debit through our accounts, and to transfer funds to other UK bank accounts. We also provide them with a MasterCard, so that they can transact on the high street and online, and we give them an app with which they can manage their money and stay on top of their finances at all times.

We founded the company about three years ago but launched officially in September 2014. We have just over 100,000 customers as of today, and we are solving quite a large problem for a lot of our customers who have not been provided with bank accounts by major high street banks. Our vision for the future is to build out the services that we provide to our customers. We know that they are underserved across the spectrum of financial services. Their first problem comes with depositing money and paying bills, but they also have no access to low-cost remittances or lending, they have no credit profile, and they have never even thought about savings and insurance products. Our vision is therefore to build an inclusive bank so that we can provide them with all those services.

Q160 **The Chairman:** Thank you. Those are two very helpful explanations. We will start with the first question. What are the principal ways in which fintech, in your view, could help to address financial exclusion? I know that you have already started to tell us that, but could you develop that a little and tell the Committee about the notable successes that you have had, or indeed about any things that have not worked? I would ask that in this session you speak in layman's language and not assume that we are familiar with jargon that might be your everyday parlance but is not ours.

Monica Kalia: It may be helpful to start by explaining how the definition of financial exclusion might have evolved. My perception is that in many ways the definition of exclusion, say 10 or 20 years ago, was used solely in relation to people who were poor—it was really a poverty issue—and potentially to people who lived in remote areas.

To my mind, the definition of exclusion has changed quite significantly over the past few years. That could be because of the make-up of the workforce. Foreign workers have moved into the UK and they lack a credit footprint and data, so they are obviously excluded in that respect. Virraj and I have spoken about this session, and his experience has been of people who cannot get basic access to financial services such as a bank account.

Exclusion also has an impact where people are declined access to things like bank loans. We commissioned a 10,000-employee survey across the UK, which we submitted to the session. Some of its findings point to aspects of exclusion. One data point is that 40% of people between the ages of 25 and 35 have been turned down for access to bank credit in the past year. Some 15% of those people have no idea why. This speaks to the fact that people are excluded from access either to a bank account or to a loan, often because they do not have the basic education or understanding of complex financial products even to get access in the first place. So it is important in the first place to set the scene by setting out the issues and what exclusion consists of.

To answer the question more directly, we see fintech as being in the fortunate position in the UK of having a constructive regulatory background. Also, it does not have a lot of the challenges and legacy that the existing financial-services incumbents face: old technology, which they are having to grapple with; and legacy branch networks that nobody really goes into. Obviously that is a generalisation, but a vast proportion of the population no longer goes into branches. They are grappling with that legacy. Fintech can be much more agile and nimble when servicing customers' needs and in a low-cost way. That means that huge swathes of the population who are not profitable from the perspective of incumbent banks can be served much more readily by fintech, because their cost of acquisition is that much lower. Fintech can be and has been a huge part of the financial inclusion solution.

The Chairman: May I interrupt you on that point? What you say about the impact of bank branch closures is very interesting. Quite a lot of the evidence that the Committee has received has suggested that that in itself can, for some people who like that form of banking, be a cause of exclusion. Can you just respond to that point?

Monica Kalia: That is definitely a valid point. At the end of the day we are dealing with a diverse demographic, and for people living in remote areas who rely on their post office or their bank branch and are used to physical transactions—it could be the older population—cutting bank branches aggressively can obviously exacerbate the problem.

At the other end of the spectrum, fintech has been instrumental in driving broader acceptance and inclusion in financial services through the use of things like smartphones and tablets. Our evidence is that 70% of our transactions are done on a smartphone or a tablet. You have to have that two-pronged approach. Some people want to rely on the physical; they want that face-to-face contact and the bricks and mortar, because at the end of the day they still perceive banking to be a trust business. Then you have people who do not need that infrastructure. They want to use social media, and the trust is driven by their social media connection with their peers and who they are banking with. They also want to be able to transact online, and they want a loan or a bank account to be approved within 24 hours. Fintech can jump to those demands, and it is increasingly what people are demanding these days.

Virraj Jatania: Monica has raised an extremely interesting couple of points. I will give you our definition of financial exclusion in relation to our customer base. A lot of people come to us because: they have had some form of debt in the past so a bank is not willing to provide them with an account or with one that has the functionality that they require; they are new to the country; or they do not have the prerequisite ID and verification documents that banks require in order to open a bank account. That is why we see a lot of people falling into the category of consumer we serve.

Fintech has enabled smaller organisations, at a much lower cost, to disrupt the financial services space and to get access to the banking or financial services infrastructure in the United Kingdom. That has enabled us, for example, to provide access to direct debits and to faster payments such as instant transfers. These are services that five or 10 years ago companies would not have been able to access. Fintech has enabled that.

The point about branches is also extremely interesting. We see very interesting feedback on branches from our customer base. A large proportion of customers feel what in our industry is called branch inertia. Going into bank branches is quite a scary experience because they feel that they might be scrutinised to extreme levels by banks, or that, because they do not have the documentation, they might be viewed differently from somebody else who is in the queue.

Having said that, we have also seen that they need some form of offline network to give them the credibility and the support that they might need. For us, that is things like the way we do customer service, and the places where we acquire customers are quite offline-driven in order to give them the support and help that they need.

The Chairman: Can you explain what you mean by offline?

Virraj Jatania: I mean more face-to-face interactions with customers. We have a network of 28,000 locations across the UK where our customers can deposit cash, which is very important for our customer base. We also work with employers to provide our accounts to their employees. We work with a large employer of temporary labour in the UK, and we provide our account instead of their employees being paid in cheques which they then take to a Money Shop or a Cash Converters to convert from cheques into cash. We work through more face-to-face channels as opposed to purely online channels and being quite obscure, so customers have a person to interact with, get feedback from and have more of a dialogue with.

The Chairman: Can I check that that is a face-to-face conversation, not a telephone conversation.

Virraj Jatania: Yes. It could also be a telephone conversation, but we see face to face as one of the most popular means.

Bishop of Birmingham: Could I ask about the 40% who get turned down for loans? I have not read the survey yet, but are either of your products looking at that age range, and are people getting access through you who might be turned down by the other systems?

Monica Kalia: Yes. That is an interesting question. Some of the alternative lenders that have emerged over the last few years have a decline rate of about 80%, so they approve about 20% of applications. A traditional high street lender like a Barclays—this is a Barclays statistic —turns down 60%, so six in 10 applications for bank credit are declined. In our current offering, across the police force for example, we approve around 65% to 70% of applications. That is all across the board; some of it is people who are in that millennial group, but it is across all age ranges and salary levels. The reason why we can be more inclusive about who we lend to goes again to the risk data point. If we are lending to a police officer, we can verify that they work for the Met and their tenure and salary, so we are privy to a lot more information, which allows us to make a risk-based decision in a much more definite environment. And because we are taking repayments directly from a salary, we are also solving risk, so that lack of willingness to repay aspect is removed.

Fintech tries to be disruptive by using technology but also by offering a genuine consumer benefit. I view consumer benefit as more affordable lending. We can lend more affordably, because most people consolidate credit card debt and pay rates of around 20%-plus. Neyber charges between 5% and 10%, so they can borrow more affordably, which is a genuine consumer benefit. The other aspect is access, which is basically your approval rate. The ability to lend to much more of the population is where fintech can be more disruptive.

Baroness Primarolo: I have a quick question about your using salary deduction. Do employees mind that their employers therefore know their credit history or at least that they are borrowing?

Monica Kalia: The way the relationship works is that Neyber is the provider and the employer very much facilitates. It is similar to providing access to private medical care, for example. The data in relation to your credit history and the size of your loan, and so on, is information that is passed to Neyber, not to the employer. That is an important point, because obviously employees see a stigma in their employer knowing about their financial situation. If they are seen to be in debt and not coping financially, that might cast aspersions on their professional capabilities, so preserving anonymity is key. The interaction with the employer is via the payroll. The employer will be passed a schedule of repayments and deductions that have to be made on a monthly basis, but that is only the monthly deduction as opposed to the size of the loan that has been taken. Next year we will also introduce a savings product, and the schedule will not specify whether it is a loan deduction or a savings deduction. We are there to protect the anonymity of the borrower.

Q161 **Lord Shinkwin:** I am delighted to hear that you both recognise that there is a need for balance in how you engage with customers, whether it is face to face, on the phone, or online. I am interested to know whether you think it will be possible for the fintech sector to produce solutions that help to address the needs of all groups who might be at risk of financial exclusion. How do we ensure that digital exclusion, coupled with increased use of new technologies, does not exacerbate financial exclusion, for example among older people or disabled people?

Virraj Jatania: Fintech is definitely capable of solving a large portion of the problems. It cannot be the sole solution to all these problems; it will need the support of regulators, government, and the general financial services space and for everyone to partner up and solve these problems. Therefore, to look at it as the sole problem-solver would not be right.

When it comes to digital exclusion, we do not see a huge amount of our product with regard to the customers who sign up with us. That does not mean that it does not exist; we know that it does. That is why it is important that the more face-to-face or telephone-based solutions are coupled with the online solutions. Anyone who is looking at this as a purely online play has got the wrong end of the stick. From our perspective, it is a three-pronged approach: telephone, face-to-face and online. If you provide across that spectrum, you can address the challenges that digitally excluded customers face.

When a fintech company that is solving a problem for financially excluded customers is building its product set, it is extremely important to think about the digitally excluded customer as well. Therefore there is a big piece around product design; whenever you think about any changes or any introduction of new products in your product set, you need to make sure that you are thinking about providing the simplest, most transparent and convenient product to the customer. If you can do that, you will not exacerbate the problem with digitally excluded customers.

Monica Kalia: I would add only to your question of whether fintech will be able to serve all the needs. While I echo Virraj's point about it not being a one-size-fits-all or a cure-all, I would go back to my original statistic: alternative providers turn down 80% of applications; we currently turn down 35%. Arguably, therefore, we are doing a much better job, but we are not perfect. We have been able to support the 35% who we cannot lend to through financial education and working with debt advice charities.

Generally speaking, when we cannot lend to an individual, it is because of affordability. That individual should not take on additional debt and they need to have better education, or they might just have made some bad decisions; they are not aware that renting and moving address year after year is compromising their credit history, for example, or that not being on the electoral register also has an impact. We have been able to fill that void with financial education, which is received incredibly well through the employer channel. We can be inclusive by identifying the body of people who we cannot lend to because of either of those reasons, and by providing financial education we can improve financial capability. At least that provides them with the building blocks to get there on that journey. All this has to be married with education, which is another important role for fintech.

The Chairman: Can either of you directly address Lord Shinkwin's point about the impact of this on older people—perhaps those who no longer have an employer—and people with disabilities, both physical and mental?

Monica Kalia: We work with retired police officers, so the offering already resonates with the retired population. We also have a very strict approach towards vulnerable customers. To that extent, in effect we have a customer service operation in London where we deal with those customers on the phone to make sure that there is adequate provision. Obviously part of the FCA's requirements is identifying people who have a vulnerability because of mental health issues, age, or whatever, so that is an important part of the proposition. But I take the point that largely digital propositions may be deemed not to serve the direct needs of that population. That is a valid point. However, supplementing it with the right level of customer service is something that both our organisations are very focused on.

Virraj Jatania: I echo what Monica has said. In the same vein, a large proportion of our customers are ex-Army veterans. A large proportion of people who have served in the Army have lived abroad for a number of years, so when they come back to the UK it is difficult for them to get access to banking services. Again, a large proportion of these customers will be above the age of 50 or 60; we see that they can interact with the product and find it easy to get access to it. We also provide a telephone sign-up process. All our account sign-up processes take about two minutes and we have 100% guaranteed acceptance—unless there are some technicalities whereby someone cannot get an account, but there are very few such cases. We require an email address for somebody to sign up, and if a customer does not have an email address we will help them to sign up for a Gmail or a Hotmail account and get them up and running. Again, as Monica was saying, we will take different approaches through our customer service channels to address the problem of digital exclusion when we see it. It is sometimes hard to address every problem that you might find. Often, someone who is digitally excluded may not actively look for the product, so it is a matter of finding the problem and then trying to find a solution at that point.

Lord McKenzie of Luton: I am trying to get my mind around this. I can understand the circumstances where your client base is the police force and members have retired or are still in employment; because they get a regular salary, they are likely to have a decent pension. The same applies, or perhaps less so, to Army veterans. But how does it work for someone who is on a zero-hours contract? How many of those people are you routinely able to serve? What is the magic that enables you to do that?

Monica Kalia: We have done a lot of our own risk work, looking at different employee groups across the UK, and there are some quite clear trends. The most creditworthy are employees in, for example, education organisations and the police force. At the other end of the spectrum, you have retail and NHS employees, and employees in cyclical sectors such as construction. The difference in creditworthiness and their ability to repay is really quite marked, often by the nature of their contracts and the fact that there may be more foreign workers in health and retail. Obviously from our perspective we have to look at affordability, as any lender would. We have to be able to map that individual’s ability to repay that debt, which is where lenders got into problems during the last financial crisis. It is much more difficult for us to lend to people without a regular income, but we can offer our other services, such as financial education.

There are retail workers who are paid weekly and may have a less regular income, and in that respect we have managed to solve the risk aspect, because ultimately it comes down to risk. We have created a product for them called a salary advance loan, which allows them to borrow up to 80% of their net monthly salary. If they leave employment, we can take the residual loan from their last pay cheque. We have tried to come up with solutions that are more inclusive, regardless of what type of employee you work with. But making sure that we can keep up with the demands, based on the different employment and payment trends in the UK, is a work in progress.

Virraj Jatania: To follow on from Monica’s point, given that our product is not a lending product, we are not bound by some of the criteria and requirements that Monica has in her business. We are providing the first step on the ladder to enable people to deposit their money safely and to pay bills. A large proportion of our customers are people on zero-hours contracts. Our vision is to build up enough of a dataset on these customers so that we can analyse it and show that although they might be in temporary work or working sporadically, they have built up enough of a track record over a six, nine or 12-month period for us to say that they can afford lending up to X amount, and then we try to provide a very tailored product for that customer.

Q162 **Lord Haskel:** You have told us how fintech can provide credit for people with thin credit files or limited financial history, but there are dangers associated with new data and information sharing—and we had this episode with Tesco Bank. What are the risks associated with these technologies, and how might they be mitigated?

Monica Kalia: One of the questions is: is new data helpful in providing you with a better answer from a risk point of view? There are two different sides to this issue: is it right to use new data—and does it actually help you; and how do you protect that data? New data is helpful because it gives you supplementary information that provides you with the better answer. Traditionally, lenders would look at the scores of credit bureaux such as Experian and Equifax, and that would give you a "computer says yes" or "computer says no" answer. That is based largely on your past history, so if you defaulted on your student debt that could stay with you for years and years and impact on your ability to access credit on fair terms.

The use of supplementary data such as your social media score, your LinkedIn profile or your transaction history can act as an overlay, so the decision is no longer as binary. But the risk with using that data is that it is unproven. You cannot use it in isolation because this is a new technique; and you do not have a sufficient time series to go back through to provide proof, which results in a better risk outcome. In that context, there is a lot of "learn and see". We still use the bureaux scores as our mainstay, but we are trying to use incremental data to be more inclusive. But you cannot abandon credit bureaux data and say, "I am just going to look at this person's transaction history and social media footprint, and make my decision based on that".

Some of the US lenders have abandoned FICO scores and have gone quite aggressively in that direction, but I do not think that the UK fintech sector is at that point. So there are risks associated with using other data that are worth mentioning.

The other aspect is data security and data privacy. As we move into open banking standards and portability of data, it will be very important for us to protect that data. To be honest, the Tesco scandal and the scandals involving people being able to access data are what keep the founder of a fintech business awake at night. We can do everything possible to make sure that we have the ISO standards, that we are handling data carefully and that our controls and systems are robust, but the evidence from the situation with Tesco and others that have gone before is that as our controls get better, so people's ability to hack into systems becomes more sophisticated. It is a challenge for all of us.

Virraj Jatania: I would largely echo what Monica has said but would add a couple of points. The credit bureaux in the UK market are quite closed off at the moment, which makes access to building credit profiles for financially excluded customers quite difficult. A real effort is required to open up those companies and help provide them with the data that both Neyber and Pockit have, and help them create profiles for customers.

That is one thing we would like to see, and we are working with a lot of credit bureaux to make that happen.

There are new credit-scoring businesses such as Aire and Credit Kudos, which you may or may not have heard of. They are trying to use social media scoring and psychometric-based questions to make a decision on someone's credit profile. While they are extremely interesting and we are working closely with a number of those companies, the biggest problem is the adoption of those scores by utility providers such as mobile, broadband and energy and water companies. Until they start accepting those scores, unfortunately they will not have a lot of validity. We are in a bit of a chicken-and-egg situation whereby we need a bit more adoption before a lot of these new scoring methodologies can become mainstream.

As you pointed out with the Tesco example, there is a real issue with data security here. As Monica says, it is the one thing that keeps a founder up at night. My biggest concern is always how we continue to ensure that we are always as secure as possible from a data perspective and that we are in keeping with regulation and compliance requirements. One benefit that fintech businesses may have over some of the incumbents is that a lot of the technology that our platforms are built on is new, whereas a lot of the existing providers rely on legacy systems and you have data all over the place in the architecture of their platforms. That opens them up to being in a slightly more risky situation. That does not mean that fintechs will not be targeted—we will, 100%—but we have at least a slightly cleaner slate from which to build and make sure that we are as secure as possible.

Lord Haskel: Are you also kept awake at night by the personal risk to your customers—for instance, unscrupulous people getting hold of the data and using it? Do you feel that the National Cyber Security Centre has a role to play in this by setting standards and requiring people who use the internet in this way to have certain security standards in the same way in which, if you drive a car, you have to have some kind of insurance policy?

Virraj Jatania: I completely agree. There is definitely a role for the National Cyber Security Centre in this. I have just come back from a trip to Silicon Valley in San Francisco on the west coast of America. One of the talks we had was about cybersecurity and how the reality is that the internet was not built for what we use it for today but was built to share files and for simple needs. It is not the fault of anybody specifically, but we have built an entire world off this platform, although it was not built for that reason. A huge amount of work needs to happen to make the internet fit for purpose, because today, frankly, it is not. Hopefully new technology such as blockchain and some others will come out that will enable us to have a much more secure system.

Q163 **Lord Northbrook:** We have had a number of submissions about the open banking standard, for instance from Barclays, the British Bankers' Association, the Financial Services Consumer Panel, the Money Advice Service and the Money and Mental Health Policy Institute, which said that this is a positive example of the benefits of fintech. How might this open banking standard, which I understand is due to be introduced by 2019, support the development of the fintech sector, how will it help to address financial exclusion, and could we also talk about the security aspect?

Monica Kalia: From our perspective, the open banking standard approach will allow portability of data. This will allow a lender such as Neyber or another fintech lender to get access to an individual's account history, their transaction profile, and will allow them to build up a much more composite picture of an individual's ability and willingness to repay. We have to make assumptions about those things now, so our underwriting decision by definition is based on those assumptions. If you no longer have to make those assumptions and you are in effect allowed to have access, because my file is my file, I can provide that to a lender and to a price comparison site, and I can get a better outcome with regard to making sure that I get a product that is tailored to my needs and a price that suits me.

In the past, we have seen the existing incumbents privy to a huge amount of current account and mortgage information, which lenders that do not have an existing relationship with customers are not privy to, so they are at a huge information advantage. With the open banking standard approach, through the use of APIs, which allows another lender to tap into an existing incumbent's database, you end up in a situation where you can make a much more informed decision, and that has to lead to better customer outcomes. It levels the playing field between fintech and incumbents, and that should be embraced.

Obviously, those open APIs and the way you access that data means that data security and privacy will need to be even more of a focus. For me, how we solve that will be the big question, because that is no small ask. Everybody needs to be aware of that. So I would expect open banking standards to lead to better customer outcomes and a fairer and more equitable system, but I would caveat that whole data piece.

Virraj Jatania: I will add a couple of points. The open banking standard has the potential to be game-changing. From the perspective of our customers who are unbanked and outside the system, it will not be as game-changing for us as a company in relation to the other data that we will be able to find on that customer from another financial services provider. However, it will allow us to build a much better set of products for our customers to interact with and will allow us to access some of the product sets of larger financial organisations and institutions, which will enable us to build a much better user journey and experience for our customers.

For companies that own the customer relationship, it will add a lot of benefit, and banks will to some degree become more providers of the pipes as opposed to owning the full relationship. That is where you will see some of the fintech businesses really benefit, as they will be able to build a direct relationship with the customer and then provide a lot of the services that banks have been providing. From that perspective, it is extremely interesting. We need to be a bit careful in that the aim is to have this by 2019 but the reality might be slightly different. It is a big undertaking. It is about two years away, and making it all happen in that short space of time will not be straightforward.

In addition, the implementation steering group for the open banking standard is being led by a large number of the banks. This will not be their best friend; it will be a big challenge for them. Therefore there is a question about how quickly all this will happen. I support that by pointing out that the adoption of email took about 15 years from when it first came out to when it became mainstream. Hopefully, it will not be as bad as that, but we will see a significant period of time before this becomes widespread.

Q164 **Bishop of Birmingham:** Can we move on to the Financial Conduct Authority for a moment? Can you reflect on its role in supporting fintech—project innovation, and so on? Can you also reflect on the balance it might provide between innovation and protection?

Virraj Jatania: We are very lucky that we have a very fintech-friendly regulator. The FCA has been extremely helpful to fintech businesses by providing advice and making them accessible and easy to speak to. It has a core role to play in the evolution of the fintech space in the United Kingdom. It has just announced the first batch of companies that have gone into their sandbox environment, which is an environment where there is a slightly lighter approach to regulation for businesses to prove the solution to a specific user case or a problem that a customer might be facing. That is a great initiative, and the fact that it has proactively taken those steps shows that it is really thinking about the fintech sector.

When it comes to financial exclusion, it might have been a little less focused. It has not necessarily been in its remit to solve that problem, and as a result it will require companies from the private sector, such as Neyber, Pockit and a number of others, to take that baton and really try to solve that problem and engage with the FCA as much as possible to get its support and help with that. So while it is doing a good job, when it comes down to our specific space it might not have been able to do as much as necessary.

On the balance between protection and innovation, the foremost focus for the FCA has to be protecting consumers and treating customers fairly—the types of initiatives that it does very well. I do not think that any of the innovations have been so extreme to date that it has had to prioritise innovation over its core focus of protecting consumers.

We are in a world where, interestingly, fintech is talked about a lot. What we are seeing in fintech today is innovation—more agile companies able to innovate on what exists today; it is not pure disruption. When things like blockchain and digital currencies become mainstream, they will become quite disruptive, which is when there will be a key role for the FCA to play in how it balances innovation with protection. As of now, I do not think that protection is being sacrificed.

Lord Haskel: Do you find the rules of the FCA onerous?

Monica Kalia: Yes. That is the other thing that keeps us awake at night.

Virraj Jatania: I would say yes and no. That is probably the right way to answer that. Some rules are extremely onerous. If you suspect suspicious activity on an account, for example, you have to place a block on that account, but you cannot tell a customer why their account is blocked; you cannot speak to them, in effect. But if you have a customer who has some money in their account and they are calling you 10 times a day, it is quite difficult to keep saying that there are technical problems or that you cannot speak to them at that point. That is tipping off and is an FCA regulation. It is quite rigid, and it is quite hard to make sure that you always stay on the right side of it, but you have to.

On the flipside, we are servicing customers who have had no access before, and parts of the regulation allow us to given them that and to open a basic account for a customer who does not have much footprint or has no real data to prove that they should have one. There are pros and cons. Parts are onerous.

Lord Haskel: Does that help or hinder financial exclusion?

Monica Kalia: Having that rigorous framework is really important, because obviously you have to separate the companies that have the right operating infrastructure and approach and that are genuinely doing things for the consumer benefit. The alternative is to have a lax regulatory environment in which anyone can rock up and start a consumer lending business. Having the right level of infrastructure and regulatory framework is super-important. You have to have the appropriate approach and the right balance between having the infrastructure, and the guidance on what regulation needs to do to support those businesses, and fostering innovation at the same time.

We have engaged with the FCA Innovation Hub, which has been very constructive. It has taken a very pragmatic approach to legislation, but the standards on affordability, treating customers fairly and vulnerable customers, which we have to adhere to day to day, are significant. From an operations and a risk-in-compliance point of view, it is incredibly rigorous.

Q165 **Lord Harrison:** Good morning to you both. To what extent have larger banks and financial service providers supported your work? Across the wider fintech sector, what is the nature of the relationship between start-ups, SMEs and the major financial services? Do they ever blossom into beautiful relationships?

Virraj Jatania: Interestingly—and this relates a little to my point earlier about innovation as opposed to pure disruption—the large proportion of fintech companies today have to work with banks and larger financial services providers. For example, we work with Barclays, where our customer funds sit in ring-fenced accounts. We also access a large proportion of the payments infrastructure through Barclays. There are a number of examples of this.

There is a relationship between fintech and the banks and financial services institutions that exist today. This is a model of collaboration, not a model always of direct competition. Companies such as ours, Pockit and Neyber, are servicing consumers whom banks, for a variety of reasons, are not choosing to service and are not playing in that space, yet they are happy to provide their infrastructure to enable us to do that. We view this as a partnership with financial institutions and banks, and in that vein we are also in discussion with a number of the banks on servicing customers who they cannot provide accounts to, for example. That is just one example of how a fintech business is working with them. I think you will continue to see that trend; I do not think it will change overnight and that fintech banks will say, "We don't need anyone in the banking space to work with. We can do it all by ourselves".

Monica Kalia: I think the relationship has evolved. In the early stages of the fintech boom, the incumbents viewed fintech with suspicion, and fintech would have liked to have been seen as the new kids who would in effect be able to disrupt the banks and the banks would in effect dwindle over the time. We have had a bit of a reality check over the last year or two, and it is much more of a partnership. I think the incumbent banks recognise that fintech's advantage is that we can originate relationships far more cheaply, we are more cost-effective in how we win customer relationships, we are much more innovative in how we develop products and we have the technology that allows us to process loan applications or open accounts far faster than an incumbent operator.

There is a flipside to that. In my business, for example, we have to work with the banks because we do not take deposits, and the cheapest form of debt capital is deposits. Essentially, the access to debt capital, which is the most important part of the lending relationship, is owned by retail banks, and I cannot see that changing. Therefore there has to be this kind of symbiotic relationship between banks and fintech, which I think will prevail. Ultimately we need access to cheap deposit funding, and the banks own the deposits.

Q166 **Lord McKenzie of Luton:** Last year we heard from the Government about their ambitions for fintech. The then Economic Secretary to the Treasury said, "We are already a major player in financial technology; our ambition is now to be the major player—the leading FinTech centre in the world". To what extent have their actions and policies helped to deliver against that ambition?

Monica Kalia: From our perspective, the Government have fostered an innovative environment. We have a constructive regulator, a competitive corporate tax rate, and access to a diverse pool of human capital, so we can attract people from all over the world to work in fintech. All those are very significant, positive ingredients to reinforce the UK's status as a leading fintech centre. Obviously Brexit will unfold, and I have no crystal ball for what the impact will be.

My ask, I guess, from a human capital perspective, is that we continue to attract tech people not just from Europe but from all over the world, which we probably have not done so a good job on in the past. I am talking about a mix of people. For example, STEM graduates from Asian countries want to come to the UK, and we should encourage that.

The biggest impediment to fintech growth, from my perspective, goes back to access to debt and equity capital. The start-up culture in the UK is poles ahead of that in a number of other countries, but it is still way behind the US. Our culture of embracing entrepreneurship and risk appetite is still behind that of the US. If I could say what would make my life easier, it would be the ability to tap into capital so that people can have that view about how visionary models can be game-changing and to fund them more easily.

Lord McKenzie of Luton: What does it take to make that happen?

Virraj Jatania: I was in San Francisco and Silicon Valley last week. People out there think on a completely different level about innovation and building technology companies. That is supported by an incredible ecosystem that allows all this to happen. One interesting point is that that has been building for 50 years now, so to expect it to happen in five years in the UK will be difficult. We need to be scrappy. We need to build a few very successful businesses in the fintech space, with the hope that those entrepreneurs exit those businesses, bring in a lot of value and reinvest that into the fintech ecosystem here in the UK. If we can build a very attractive environment for something like that, we can achieve what Monica is alluding to. It will be difficult just to have government policies to enable that to happen; it will take a mixture of government policies and private sector thinking.

Monica Kalia: It comes down to the cost of capital. In the UK, the cost of capital is much higher than it is the US. That could just be because of your risk premium from your association with these investments. Ultimately, it comes down to risk tolerance, which is much higher in the US than it is the UK. In the US, people tend to take a portfolio approach towards investments and take it as a given that 90% of those will fail but that the 10% that flourish will be the unicorns. We have been less focused on that type of approach in the UK, where it is much harder.

The Chairman: We are almost at the end of the session. Baroness Primarolo has the last question.

Q167 **Baroness Primarolo:** It has been a fascinating session, so thank you very much. We have taken a lot of evidence from different groups. Perhaps, given the nature of your businesses, there is no simple answer to my question, but when the Committee draws up its recommendations, is there a particular recommendation that you would want us to consider, bearing in mind what you have said about ecosystems, innovation and how much government can do? Is there a piece of the jigsaw missing that could be put in place?

Monica Kalia: There is one that relates to my business specifically. We employ a facilitated provision of financial services. The benefit to the employee is that they get access to finance on fairer terms. Therefore, very much as we have had with auto-enrolment, which is the obligation to provide a pension, we could ask for an obligation on the employer to provide financial education for free to employees and access to financial services that can be taken from the payroll. This has been done in many countries where there are emerging markets.

Baroness Primarolo: You think that we could sell that to the employer by saying that there would be a benefit for them.

Monica Kalia: Yes.

Virraj Jatania: As you know, there are different natures to our business. The way the system works at the moment for consumers who are outside the banking system is that they try with a bank, and if the bank does not offer them the product or service they are almost left to figure it out by themselves. From my perspective, I would love there to be, especially at the Department for Work and Pensions and jobcentre level, a recommendation for an alternative provision of current accounts and financial services to consumers. At the moment, the Post Office is the only entity that is recommended outside the high street banks. It is quite an archaic provider of financial services. In effect, it is just a white-label version of what banks provide. It needs to be opened up to fintech business in order to be the solution to the problems that consumers are facing.

Lord Harrison: Perhaps you and Monica could provide us with examples of other countries that are already doing this and encouraging the employer to provide for it.

Monica Kalia: You could look at Brazil, for example, and a number of countries in Africa. This exists in those countries because they do not have credit bureaux data, so they deal with the risk by using a salary deduction model. My argument is that we have the data but we could be much more inclusive and offer a better deal to consumers if employees had the right to say, "Yes, I want to take this consumer loan but I want to take it from a provider who can deduct the repayments directly from my salary". There are a number of examples.

The Chairman: Would it be possible to let the Committee have a short note on some of those examples in other countries that you have talked about? We would find that very helpful.

Monica Kalia: Yes, absolutely.

The Chairman: Thank you very much indeed. It has been a very helpful session. Thank you for keeping the language straightforward. Finally, you both used the term "disruptive" on a number of occasions. Could you just say in one word whether, in the way you used that word, it is a good thing, a bad thing or a neutral thing?

Monica Kalia: I think it is a good thing, in the sense that—

The Chairman: That is enough, thank you.

Virraj Jatania: I think it is a good thing.

The Chairman: You are using it in a positive sense. Thank you.

Monica Kalia: Except when it comes to children, when it is less positive.

The Chairman: Thank you very much indeed.