

Debates on Blockchain eclipse talk of Basel III at Davos

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When the World Economic Forum staged its flagship debate about the future of the financial services industry this week in Davos it sparked a disorderly scrum.

The Davos elites were not scrambling to listen to the debates that have dominated the WEF agenda in recent years, namely the financial crisis and regulatory reform; these are largely absent from the agenda this year. Instead the current hot issue is how financial technology or fintech could revolutionise the world of money; topics such as Blockchain have eclipsed discussions on Basel III.

Critics argue that the shift is a little premature. After all, the day-to-day life of most senior bankers is still dominated by regulatory reform issues and parts of the eurozone banking world are still grappling with legacy problems such as Italian bankers who have earnestly been downplaying concerns about bad loans.

Yet the bankers attending Davos insist that the sector is on its strongest footing than at any point since the financial crisis of 2008; capital reserves have increased, risk reduced, operations streamlined. Indeed, a survey from Edelman, the public relations firm, this week even showed that public trust in banks is rising.

“If you look at the amount of capital, oversight and approach to risk in the banking world today, I strongly believe that the banking system is a lot more solid than it was,” says Andrea Orcel, president of UBS investment bank.

This does not mean that the banks are out of the woods, however. “Trying to get the appropriate risk-adjusted returns from banks given the state of the economy, regulation, markets, and the necessary transformation of both business models and cost structures is a challenge — and competition is rising,” says Mr Orcel.

The most intense source of this competitive challenge comes from fintech, and its potential to upend the status quo. This is now affecting numerous aspects of finance, ranging from back office payments to investment advice and retail payments.

Indeed, the revolution is now so dramatic that the chief executive of one big European bank told the audience in Davos that cash might “cease to exist” in its current form in a decade.

Meanwhile, the International Monetary Fund issued its first white paper on virtual currencies this week. The report argued that while these new forms of money are still very small in scale — totalling a mere \$7bn in market value compared to the \$1.4tn value of US paper currency in circulation — they are exploding so fast that policymakers and bankers alike need to take note.

Many financial technology companies, who are out in force for the first time this year in Davos, hope to use this financial revolution to disrupt the incumbent banks. But the banks are trying to fight back by developing their own fintech capabilities, while also collaborating — and purchasing — tech start-ups. In the next few months, for example, senior officials at JPMorgan expect the bank to start settling loan trades using blockchain technology, the ledger that enables electronic payments, and operating in collaboration with one fintech start-up, Digital Assets Holdings (a group created by Blythe Masters, a former JPMorgan luminary.)

Many of the new entrants argue that the incumbent banks move too slowly to outwit the upstarts, while established financiers are apt to retort that the issue of fintech has been overhyped.

The issue of the blockchain, for example, is particularly problematic because of the controversy that surrounds the virtual currency, bitcoin. “We know that bitcoin itself is a complete failure and shows the number one law of programming and software: that anything that can be programmed can be hacked. So nothing is completely secure,” said Willem Buiter, Citi’s chief economist and former member of the Bank of England’s rate-setting committee. “The cyber boys . . . they believe that this is something that can just work on its own and allow a seamless web of costless transactions across the world. Forget it.”

Nevertheless, nobody expects this type of cynicism to undermine the enthusiasm for fintech at the WEF, particularly since the official theme for this year’s meeting is focused on technological revolutions.

The new battleground for the financial world is the issue of whether the new entrants will be subject to the same regulatory controls as incumbent banks — or whether these radical changes are simply concealing a new explosion of risk under the guise of “innovation.”

“If you’re going to be in the finance business, the finance regulation should be the same for everyone,” says Cathy Bessant, chief technology officer at Bank of America. Ms Bessant stresses that banks need to harness the power of technology and innovation, without reducing the capacity of the banking sector to absorb and deal with risk.

By this time next year that issue of “regulation” may be top of the agenda in the WEF finance debates again.