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# China Needs More Fintech Regulation, America Needs Less

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Now is the time to re-energise America's payment system.

In a recent episode of Professor Scott Galloway's podcast, he talked with one of my favourite writers: the eminent historian and Hoover Institution senior fellow Niall Ferguson. The subject of the conversation was the relationship between the United States and China. Their fascinating discussion ranged across many fields, including financial services and fintech. As the author of one of the best books on the history of finance, The Ascent of Money, Ferguson has a very wide and well-informed perspective on the future of money in the context of Sino-American competition and I quote him more than once in my book on the topic, "The Currency Cold War".

Ferguson touched on a particular aspect of what he referred to as "Cold War 2", saying that American regulators "have allowed the fintech revolution to happen everywhere else". I took this to mean that the nature of financial regulation in America has been to preserve the status quo and allow the promulgation of entrenched interests while the costs of financial intermediation have not be reduced by competition. In which case, he has a good point. He went on to say that "China has established an important lead in, for example, payments", clearly referring to the dominance of mobile payments in China and the role of (in particular) Alipay in bringing financial services.

(As an aside, if you want to understand some of the big picture around the coronavirus, currency and Ferguson's "Cold War 2", then you might want to also listen this podcast from CoinDesk. It is a conversation between Ferguson and the author Michael Casey about our disrupted world, inevitable crisis and what it could mean for money. )

At a time when America is finally beginning to at least think about opening up financial services to allow real competition, China is heading in the opposite direction by clamping down on fintechs.

Ferguson's point about payments is particularly interesting to me. One way to provide more fintech competition to the incumbents would be to provide a more relaxed environment for payments. America lacks a regulatory construct equivalent to the EU's "Payment Institution" or India's "Payment Bank" and it really needs one. One place to look for new regulation might be the OCC, which has developed the concept of the Special Purpose National Bank (SPNB) charter. I don't want to sidetrack into the controversy around this charter, except to note that the OCC expects a fintech company with such a charter to comply with capital and other requirements that seem unlikely to generate the innovation that America wants. It seems to make that it is therefore unlikely to generate more competition, as was obvious from the comments on the original proposals when fintechs made it clear they would be reluctant to invest in such an OCC license unless such a licence would require the Federal Reserve to give them access to the payments system. This is because they do not want to have to depend on banks to intermediate and route money for them, largely because the fees associated with such intermediation are a significant (ie, top five) operating cost for many fintechs.

**Competition Via Access**

However, the idea of another kind of OCC federal charter that would allow regulated institutions access to payment systems, but would not allow them to provide credit, seems rather appealing to me. Such a charter would separate the systemically risky provision of credit from the less risky provision of payment services, a very different concept to the SPNB charter. The economist George Selgin, Senior Fellow and Director of the Cato Institute's Center for Monetary and Financial Alternatives, recently posted a similar point on Twitter, arguing for the Federal Reserve to give fintechs direct access to payment systems (instead of having to go through banks).

This was the approach taken in the UK when the Bank of England decided to give settlement accounts to fintechs, where examples of fintechs who took advantage of this opportunity to deliver a better and cheaper service to customers range from the $5 billion+ Transferwise money transfer business (which has just obtained a “restricted banking licence” to gain direct access to the Australian payment system) to the open banking startup Modulr (which just received a $9 million investment from PayPal Ventures). Interestingly, Singapore has just announced that it will go this way as well, so that non-banks that are licenced as payment institutions will be allowed access to the instant payment infrastructure from February 2021.

My good friend Chris Skinner was right to say that many US fintechs will follow the likes of Varo, apply for new licenses and become more and more like traditional banks, but that’s because the traditional bank licence is all that is on offer to them. The situation has arisen because of an accident of history that jumbles together money creation, deposit taking and payments. It’s time to disentangle them and to stop, as Jack Ma (the billionaire behind Alibaba and Ant Group) recently said, regulating airports the way we regulate train stations.

Mr. Ma made these comments shortly before Chinese regulators halted his IPO, following more comments questioning financial regulation, clearly signalling that their relaxed attitude toward the growth of China's financial giants is coming to an end. Whereas China was happy to see its techfins grow in order to help them scale while American enterprises were kept at bay, it is now beginning to set some bounds. The issues around the Alipay IPO were related to lending, not payments, and concerns about leverage. Although heading towards half of Ant's revenues came from the lending, facilitated by their vast quantities of data, but they only came up with 2% themselves (if they were were a bank, they would be required to provide something like a third) passing the rest of the exposure onto banks.

Where is the right balance for fintech? I think it is clear. China needs to regulate lending more, the US needs to regulate payments less. America needs more competition in the core of financial services and now is a good time for fresh thinking. With the Biden administration on the way, they can tackle this core issue that, as The Hill says, the U.S. government has "ignored and neglected" the need for a regulatory framework that will support American technological innovation around money, setting aside what I agree is an embarrassing and "outdated regulatory approach to fintech". Separating payments and lending would be a great place to start.