Sandboxes in the Sandpit: Fintech Evolution

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Recent years have seen a drastic increase in the funding of the Financial Technology ("Fintech") industry, which has allowed the industry to mature in many regions of the world. Fintech is still in a developmental state in the MENA region, with the region accounting for a miniscule percentage of global Fintech financing. However, there is significant potential as regional regulators are keen to create an environment that allows growth and innovation opportunity for existing and upcoming Fintech entities, with consumers eager to adopt innovative financial solutions. This article will explore the forces driving the growth of Fintech, the trends we can see developing, the regulatory response, and recommend actions that can expedite and aid the development of Fintech in the MENA region.

Forces driving the growth of Fintech

The two key elements that have stimulated the growth of Fintech are banks and Covid-19.

Most banks in the region view Fintech as an essential aspect of the evolving banking structure of the region, even if Fintech's exact role remains uncertain. The two most common approaches observed are banks developing in-house native Fintech capabilities or opting to monitor the development of independent Fintech companies, and partner with such companies to become first in line to provide the best and most innovative solutions to its customers. While enthusiasm is high, only a few banks have deployed Fintech in a targeted fashion, utilising Fintech in strategic projects to enhance the market's current product offerings and customer acquisition. Thus, although there is a strong desire from banks and consumers, the development of the Fintech industry remains nascent.

The pandemic and corresponding lockdowns in the region have fast-tracked digital payments and online retail growth. However, this positive outlook must be tempered to a degree as this rapid adoption of Fintech services is developing from a low base. Nonetheless, the outlook is optimistic. Covid-19 has also caused regulatory authorities to permit accelerated digital ID and e-KYC solutions to allow for digital on-boarding and identification of clients.

Key trends

The main reason behind the adoption of Fintech by consumers is to make banking and electronic transactions easier. Similarly, most consumers expect Fintech to support their banking needs and provide personalised service. However, certain categories of customers portray either lack of understanding of Fintech related products or hesitance to use such products to their advantage based on concerns relating to data security or their eligibility to use such products.

Whilst certain regulators in the MENA region have been quick to adopt payments or Fintech-related regulations to allow this industry to grow within certain acceptable legal and regulatory limits, other regulators are taking a more cautious approach before any such activities or products are formally regulated. Various regulatory authorities in the MENA region, and in particular the GCC countries have launched regulatory sandboxes that allow firms to test and develop their products in a limited and victual environment before such products are launched in the respective markets. The purpose of setting up regulatory sandboxes is to allow entities an opportunity to innovate and transform the digital and financial technology space with solutions to enhance customer experience and convenience.

In our experience, each regulator has adopted a different approach to regulatory testing with prime focus being to safeguard and protect the end user when the product or solution is launched in the market.

Especially during Covid-19, the central banks and financial institutions in the MENA region have encouraged customers to use technology as much as possible. Solutions such as tap and pay at points-of-sales (whether using tap cards, mobile phone or smart watches) are encouraged to keep physical contact to a minimum. Cashless transactions have been recommended. A significant boost to e-commerce since Covid-19 related lockdowns or restrictions has also led Fintech entities to develop applications and payment solutions to ease customer experience during the e-commerce checkout processes. Whilst mobile or e-wallets have been in the picture for some time now, its use has become more significant post-pandemic with government departments and ministries now allowing public to store, access and use official documents and cards such as identity cards, permits, drivers license etc. through e-wallets.

Regulatory response

Open banking provides a secure way for consumers to give providers access to their financial information. This allows independent Fintech companies to provide consumers with products and services that rely on information from their bank accounts. Regulators in the MENA countries are at different stages of introducing open banking. Some of the key factors influencing the adoption of open banking are the development of new regulatory policy, improved infrastructure, high internet and mobile usage rates, and

Covid-19. Bahrain is leading the way in the region, having introduced its Bahrain Open Banking Framework in October 2020. Regulators in UAE have shown support for open banking, with other key players pushing for its implementation. Adoption of open banking is also being discussed favourably in Saudi Arabia.

As part of its 2030 vision, Saudi Arabia is aiming to have majority of its transactions made through non-cash means. It has begun developing the KSA SARIE System, a network of digital rails that will allow secure real-time payments. The Qatar Central Bank has established a National Fintech Strategy that provides guidelines for new projects and enables them to establish operations in Qatar while working with international companies. Qatar has also launched Qatar Fintech Hub that runs incubator and accelerator programs in which Fintech start-ups can participate to test their prototypes or payments solutions and launch them in the market following requisite approvals from the Qatar Central Bank. Qatar aims to hold a cash-less FIFA World Cup in 2022. Egypt has also updated its banking laws, which for the first time address local payment service providers, digital banks, and cryptocurrencies. In 2020, it also launched the pilot phase of its new digital KYC service. In April 2020, the Arab Monetary Fund issued new guidelines for e-KYC, allowing for remote on-boarding of customers. Regulators across the MENA region are modernising their financial systems.

Recommendations

Regulatory frameworks for finance across the MENA region are disparate and at different stages of development. Achieving regulatory harmony would benefit the development of Fintech companies, many of which operate in multiple countries in MENA. Achieving such harmonisation is a challenge as the financial conditions in the nations are far from similar. A more realistic option would be to seek to achieve some degree of harmonisation within the GCC countries. Some progress can already be seen with KSA and UAE developing a common digital currency to facilitate cross border payments. Cooperation between the region’s sandboxes and Fintech hubs would also be advantageous. The collaboration would help in the creation of standard procedures for selection and development of Fintech solutions since a Fintech solution launched in one of the countries is the region is likely to expand to the other. It would also enable regulators and other key players to see developing trends, allowing them to forecast the growth and evolution of Fintech in the region.

Banks and Fintech companies also need to develop deeper relationships, with Fintech being integrated more holistically into the bank’s strategy, to cultivate longstanding partnerships. The demand from consumers is high, and such partnerships would benefit both banks and Fintech. Regulators can play a crucial role here by implementing benefits and exemptions for banks that form such partnerships. Ease of relevant approval and licensing processes would also encourage new Fintech companies to innovate and transform the payments industry.

There is a need to create awareness amongst public to encourage them to adopt Fintech solutions. While this could prove to be a challenge, it also represents a considerable opportunity especially in the post-pandemic era.

Conclusion

Although the development of the Fintech industry is still in the initial stages in the MENA region, there is much to be optimistic about. Regulators understand the importance of the industry and the critical role it will play in making their respective financial industries competitive at the global stage in the 21st century. There is a growing demand for innovative Fintech solutions from the younger tech-savvy population, which positively reflects the growth of Fintech in the region. While the adoption of Fintech remains limited in certain segments of the population, this represents a large market for Fintech, one that can be accessed with a greater focus on awareness.

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