IDEAS FOR LEADERS | **JUNE 2016**

# banking insight

PP 17327/05/2013(032407)

HARVESTING THE
**WISDOM OF THE CROWD**

**BLOCKCHAIN ASCENDING**

Banking for Sustainability:
The Policy, Regulatory and
Financial Case for Action

BANKING ON FULL RESERVES

## THE STATE OF BASEL III

Although regulators are turning the heat up on compliance with Basel III, ASEAN banks are staying ahead of the regulatory curve.

ISSN 2231-8267

A PUBLICATION OF
ASIAN INSTITUTE OF CHARTERED BANKERS

Editor's Note

# REBUILDING TRUST THROUGH REFORM

**THERE'S NO REST** for the weary in the global financial sector, as the relentless pace of reform marches on.

Regulatory reform continues in full swing; this issue takes a sweeping look at Basel III, which marks the most concerted global effort by regulators, policymakers and financial players to reduce systemic risk in their bid to avert a repeat of 2008's financial crisis. Although the timeline for full compliance is by 2019, the majority of jurisdictions are currently well into the implementation phase, with the Basel Committee on Banking Supervision (BCBS) coordinating member states at the global level and monitoring non-member states at regular intervals. Attesting to the state of regulatory flux, Basel IV is already waiting in the wings even though Basel III is still underway. We offer some insights into Basel IV as well to keep readers abreast of what's key in the fourth round.

Ever evolving, fintech continues to disrupt banking and will fundamentally change the way financial institutions conduct their businesses. One of the newest trends which banks are fervently investigating is blockchain, the architecture underpinning cryptocurrency Bitcoin which has been hailed as a game-changer and revolution. At its simplest, the blockchain can be described as the register of all bitcoin transactions, one which is completely decentralised, public, transparent and verifiable. Indeed, author and journalist John Lanchester in the *London Review of Books*, said this in an essay on blockchain: "A decentralised, anonymous, self-verifying and completely reliable register of this sort is the biggest potential change to the money system since the Medici. It's banking without banks, and money without money." Like the internet in the early days, the blockchain story and its potential uses are still unfolding. But we've attempted to give readers an introduction and update on what's happening in the blockchain space, especially with regards to ASEAN.

Speaking of changes that date back to the earliest days of finance, might there be prospective reforms in the fundamental system of banking as we know it? Check out our update on the campaign to replace fractional reserve banking with full reserve banking, which has gained interest and supporters in Switzerland, Finland and Iceland. We consider viewpoints emerging from the Bank of England to Frosti Sigurjónsson, Icelandic lawmaker and writer of the 'Monetary Reform: A Better Monetary System for Iceland' report to assess if full reserve banking can really be a panacea to address the fundamental failings of the current financial system: "the ability of banks to create credit, money and purchasing power, and the instability which inevitably follows", as Sigurjónsson put it.

While identifying key new developments is a paramount objective every issue, we also want to offer pragmatic strategies and insights into managing change. Among a slew of diverse subjects, this issue explores how chief risk officers as the fulcrums of their organisation can enhance risk culture from top to bottom, and how banks might want to strengthen their information gathering and data analytics competencies to make better decisions and improve their competitiveness.

Nevertheless, while we might be preoccupied by trying to best manage change and the parallel opportunities and risks, we mustn't lose sight of the real reason and goals behind these shiny new reforms – which is to achieve better business and better governance. In everything that we do and in all the reforms that we implement, we have to place the public interest at the core of our strategies and initiatives. Only then can we reinvent ourselves positively to achieve sustainability and legitimacy, and regain public confidence and trust in a world that seems intent on bypassing old-school banks, that demands "banking without banks." ✱

*Hope you have a fruitful read.*

**The Editor**

**+ Fintech continues to disrupt banking as we used to know it. One of the newest trends which banks are fervently investigating is blockchain, the architecture underpinning cryptocurrency Bitcoin which has been hailed as a game-changer and revolution.**

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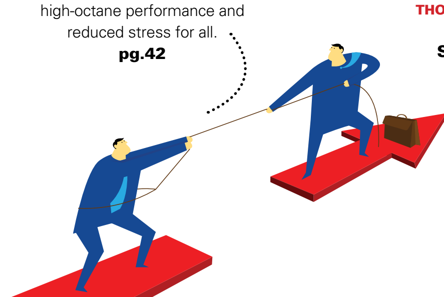



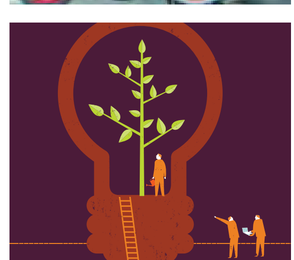

### THE PANAMA PAPERS

The Panama Papers, an unprecedented investigation by the International Consortium of Investigative Journalists (ICIJ) together with other media partners, is the largest leak in offshore history. ICIJ's data and research unit indexed, organised and analysed the 2.6 terabytes of data that make up the leak. The leak includes 11.5 million records, dating back nearly 40 years, and contains details on more than 214,000 offshore entities connected to people in more than 200 countries and territories.
Interestingly, the leak also shows how major banks have driven the creation of hard-to-trace companies in offshore havens, said the ICIJ. More than 500 banks, their subsidiaries and their branches – including HSBC, UBS and Société Générale – created more than 15,000 offshore companies for their customers through Mossack Fonseca, the law firm at the heart of the leak. ✱


## BLOCKCHAIN: THE NEXT EVOLUTION

PwC's report, "**Blurred Lines: How Fintech is shaping Financial Services**" says blockchain, a distributed ledger technology, represents the next evolutionary jump in business process optimisation technology, which could result in a radically different competitive future in the FS industry. Blockchain could disrupt and redistribute current profit pools towards the owners of new, highly efficient blockchain platforms. Huge gains in transparency and costs savings are possible.
However, the survey of 544 CEOs, Heads of Innovation, CIOs and top management involved in digital and technological transformation across the FS industry in 46 countries, found that while the majority (56%) recognise blockchain's importance, 57% say they are unsure or unlikely to respond to this trend.
Apathy could cost them. PwC's Global Blockchain team has identified over 700 companies entering this space, 150 of whom it says are "ones to watch" and 25 of which it expects will likely emerge as leaders. ✱

"FINTECH is changing the FS industry from the outside. PwC estimates within the next 3-5 years, cumulative investment in Fintech globally could well exceed USD150 billion" - Steve Davies, EMEA Fintech Leader at PwC commenting on PwC survey, 'Blurred Lines: How Fintech is Shaping Financial Services'.

83%
the percentage of respondents from traditional FS firms who believe PART OF THEIR BUSINESS IS AT RISK of being lost to standalone Fintech companies - PwC report 'Blurred Lines: How Fintech is Shaping Financial Services'.

## INADEQUATE LIVING WILLS

*The New York Times* in April 2016 reported that the Federal Reserve and the Federal Deposit Insurance Corporation (FDIC) rated the "living wills" of five of the eight largest banks in the US as not being credible. The living wills are a requirement of the 2010 Dodd-Frank financial overhaul, intended to assuage the risks to the broader economy of large financial institutions which are "too big to fail".
The Fed and the FDIC., which jointly oversee the largest banks, agreed that the plans put forward by five of the big banks, JPMorgan, Bank of America, Wells Fargo, State Street and Bank of New York Mellon, were "not credible or would not facilitate an orderly resolution under the US Bankruptcy Code," reported the NYT. ✱

## STOCKS SHOCK

**THE DOW INDUSTRIALS** and the S&P 500 may be heading toward record highs, but Americans – especially middle-class adults and those below 35 years of age - appear hesitant to buy into the rally. According to Gallup, only 52% say they currently have money invested in the stock market, matching the lowest ownership rate in the poll's 19-year history. In 2007, just before the markets were crushed in the Global Financial Crisis, ownership hit a high of 65%. ✱