

Key Factors in Assessing How Fintech Applications Can Affect Financial Stability

DTCC has developed an original framework of nine key factors to assess how specific fintech applications can affect financial stability. The framework covers a wide range of critical factors including concentration and interconnectedness risk, fragmentation and substitutability of services and automated decision-making processes.

The provision of core banking functions by fintech firms

1

When it comes to diversifying credit and liquidity risk within the financial system, fintech companies that provide core banking functions could enhance financial stability but they could also create systemic vulnerabilities.

The level of fintech-related fragmentation

2

The unbundling of financial services that is associated with the rise of fintech may benefit clients through increased competition and lower fees and has the potential to fragment the creation and delivery of financial services across additional providers and platforms.

The impact of fintech on concentration risk

3

A small cluster of large players could create the potential for a concentration of operational risk.

The substitutability of fintech services

4

Substitutability is a key concept in assessing systemic risk. Financial services that are highly substitutable create less systemic risk than those that are not.

The effect of fintech on financial interconnectedness

5

The interconnectedness of financial service providers could have a significant impact on financial stability. Therefore, it is critical to analyze how fintech developments affect financial networks.

The degree of competition vs. cooperation between fintech firms and incumbents

6

An environment where fintech companies and incumbents cooperate in mutually beneficial arrangements is more likely to promote financial stability than an environment characterized by competition.

The degree of reliance on automated decision-making processes

7

Overreliance on purely data-driven algorithms may lead to errors that may not have occurred in an environment that involves more human judgement calls.

The sustained growth and adoption of fintech services

8

The impact of fintech depends on the extent to which the technology becomes a mainstream part of the financial ecosystem and to what extent it will ultimately be used for delivering critical financial services.

The evolution of the regulatory environment

9

Policy decisions and regulatory actions will directly determine to what extent fintech will ultimately impact financial stability for years to come.