What is the potential impact of Open Finance?

The Building Societies Association commissioned economics consultancy Frontier Economics to look into the effects of the introduction of Open Finance.

The research modelled the potential impacts of Open Finance on the UK savings market and the knock-on effect on mortgages.

It also identified ways to implement Open Finance that would benefit consumers, while reducing adverse consequences and minimising risks to financial stability.

"We welcome developments that aim to deliver better value to consumers, and Open Finance could do just that in the savings market. On average building societies pay higher savings rates than those offered by the banks, and so it's likely that our sector could benefit overall from the changes.

"However, we are mindful that with any well-intended changes, there can be unintended consequences. In the case of Open Finance, this could be reduced availability of easy-access accounts, which are often relied upon by some of the most vulnerable savers in our society. Also, if overall savings rates rise, there is likely to be a corresponding rise in mortgage rates. The Frontier Economics report is a useful guide on how these risks can be reduced, which we hope the regulators will consider carefully."

Robin Fieth,
Chief Executive
of the BSA

"Open Finance has the potential to change the UK savings market. Many customers could benefit from new services helping them to manage their savings. But there are also risks: for both building societies and banks, there is a risk to financial stability from deposits being transferred more quickly. To reduce these risks, there should be limits on the flow of deposits that can be moved by Open Finance services. We hope our analysis will help the industry and regulators decide how to proceed with the next phase of Open Finance."

Kristine Appleton,
Economist, Frontier Economics

This is a summary of the full report, The impact of Open Finance on mutuals' business models, published April 2024.

Building Societies Association

frontier economics

Open Finance will enable data sharing, similar to Open Banking, but for a wider range of financial services, including savings.

In the savings market, a personal finance app could use Open Finance data to give personalised information, or potentially move a customers' savings automatically to earn the highest available interest rates, or automatically transfer them to their current account to meet upcoming bills.

How big and how rapid a change Open Finance brings depends on:

- the extent to which consumers take up Open Finance
- the level of access and control that the regulator allows for providers using Open Finance

The impact if take-up is high

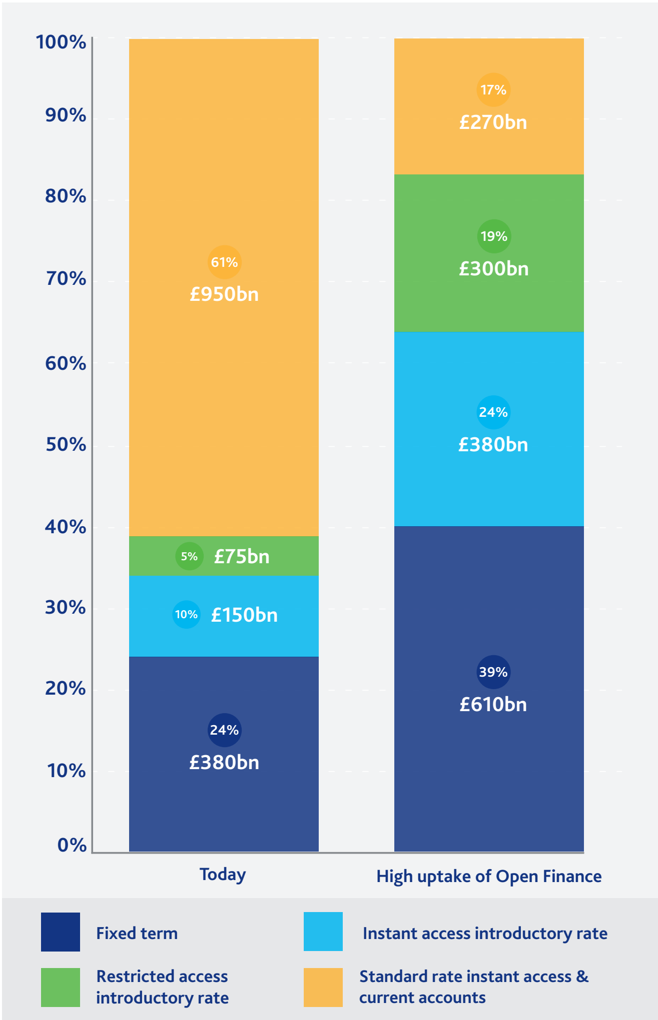
In a scenario where there is **high take-up** of Open Finance by consumers, Frontier Economics' analysis suggests there could be substantial changes to the structure of the savings market.

Using the example of a personal finance app that had the ability to access data, make payments and even open new accounts, account balances that are not fixed or locked away could be easily switched to a new savings provider.

This would have major consequences for the market.

This could include:

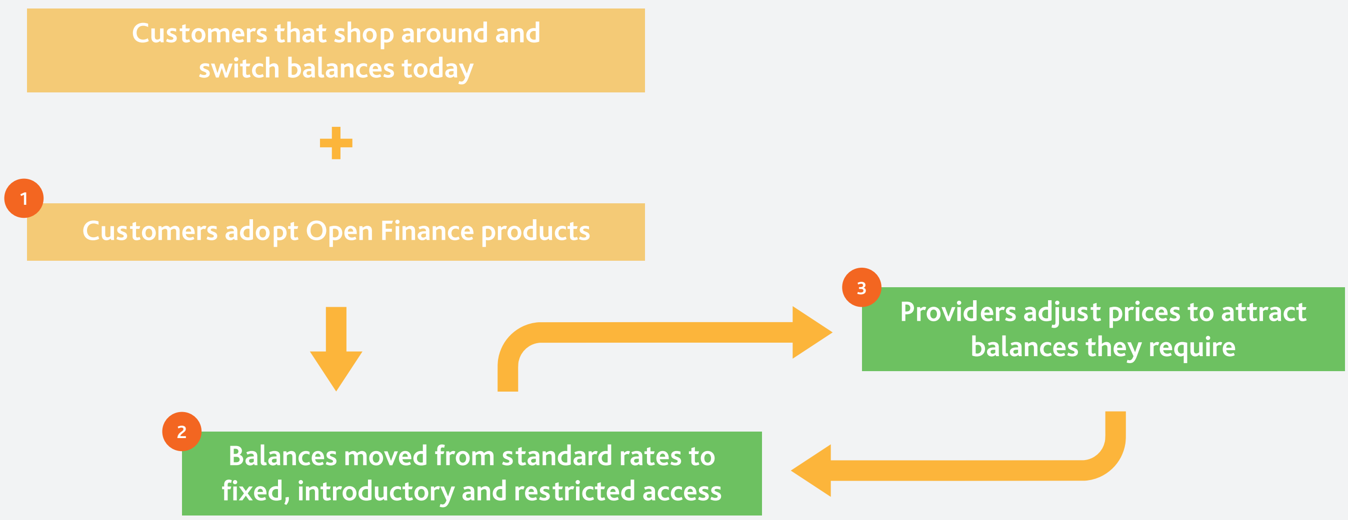
- **Large scale, rapid switching of savings between providers**. £950 billion currently in standard instant access rates could reduce to £270 billion.
- **A greater proportion of savings moving to fixed term and restricted access deposits** as Open Finance based services could identify more savings that are unlikely to be needed instantly, and so could be locked away and earn higher rates.
- **Lower introductory rates on new instant access accounts**, as the deposits are less likely to remain with the provider long-term, and on higher rates, so providers are less keen to attract them in the first place.
- Frontier Economics estimate that overall **average savings rates earned could increase by 0.39-0.77 percentage points** in this scenario.
- This could have a knock-on impact on other markets if providers seek to offset these increased costs.For example, the impact in the mortgage market could be **an increase in mortgage rates by approximately 0.21-0.41 percentage points,** or about **£90 a month** more on an average mortgage[1].



[1]Mortgage pricing calculated on the basis of a 2-year fixed rate mortgage at 90% LTV, using the Money Saving Expert Mortgage Calculator, an average 2-year fixed rate in February 2024 of 5.71%, as calculated by USwitch and the average house price of Nationwide Building Societies February 2024 HPI of £260,420.

"The emergence of such Open Finance enabled... solutions in the savings market has the potential to have a significant impact on how the savings market operates, with potential knock-on impacts on the mortgage market."

Frontier Economics' full report, page 4



The impact on savings providers

Exactly how **Open Finance affects existing providers** will depend on their existing business models, particularly:

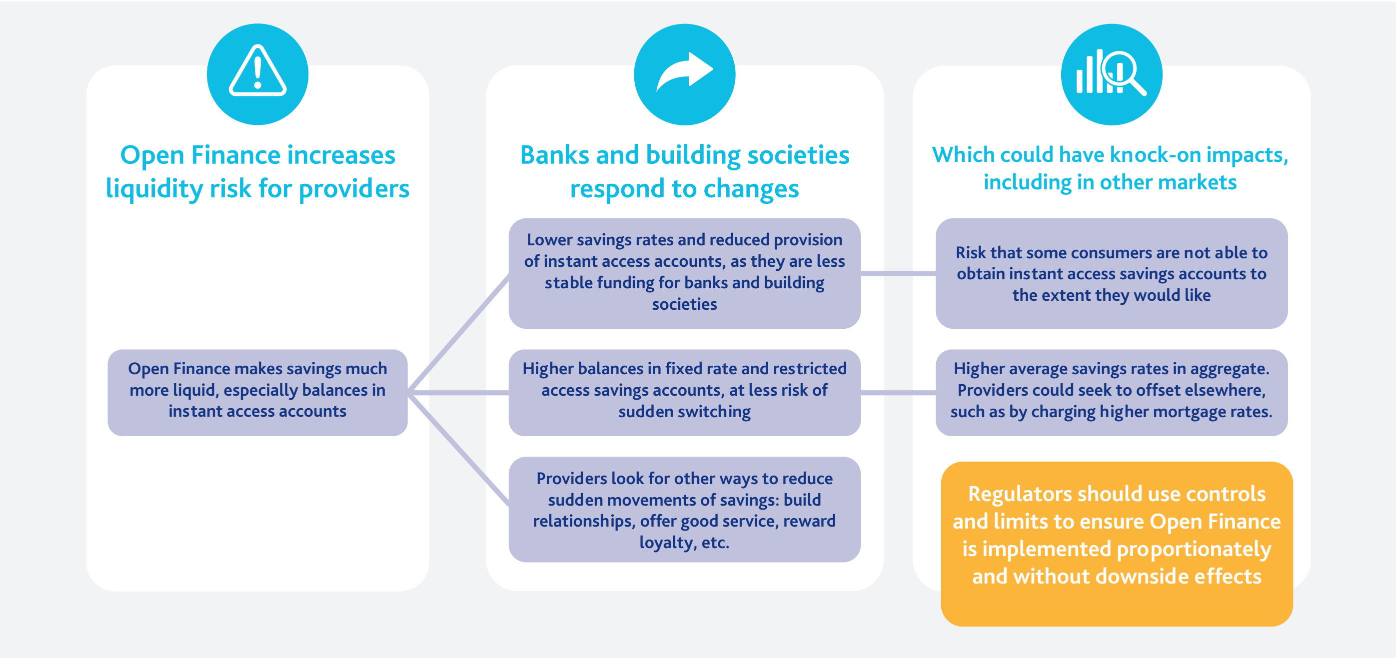
- A provider’s funding structure: whether they currently rely on instant access accounts or fixed rate and notice accounts.
- How it prices its savings accounts: do they have flat rates, or do they offer introductory or bonus rates to new customers?

Providers with high volumes of instant access savings are likely to see the average rates they have to pay increase. Providers with a small proportion of instant access accounts and that already pay high introductory rates could see the rates they offer reduce, as increased switching means they don’t need to pay as much to attract customers.

There would be **significant costs to implement the regulations** and systems to manage the data and payments, especially for smaller providers, which includes many building societies and credit unions. Providers may also need to invest in their internal capabilities to manage a more dynamic balance sheet, liquidity needs and pricing movements, and adopt more sophisticated hedging strategies.

"Open Finance may affect the entire savings market, but mutuals hold on average fewer balances in standard rate instant access products than the rest of the market and offer higher average rates on their savings products. This means that the emergence of... solutions in cash savings may present a number of opportunities for mutuals."

Frontier Economics' full report, page 6



Implications: mitigating the downside risks

As savings balances are moved automatically by Open Finance services, some savers will benefit from higher savings rates, but banks and building societies would face increased liquidity risks from less stable instant access deposits.

Frontier Economics' assessment suggests that savings providers are likely to need to develop safeguards to manage the heightened liquidity risk. For example, providers may find it necessary to introduce restrictions, such as notice periods, to reduce automatic outflows and improve the stability of deposits. This could lead to a reduction in the availability of instant access accounts. In addition, interest rates offered on instant access products may fall to reflect the higher risks borne by providers.

There is therefore **a risk of financial exclusion, particularly for some vulnerable groups** that rely on instant access accounts.

However, there are a number of approaches regulators could take to develop Open Finance without having an unforeseen impact on savings product pricing and availability, mortgage pricing and wider digital exclusion caused by forcing unrestricted digital services on organisations and their customers.

For the instant access accounts that remain, there may be other ways to support savings providers **managing the liquidity risks** of savings suddenly moving into or out of the business.

These may involve requirements on app providers with access to accounts via Open Finance, for example:

For providers:

1. **Limits on the value of savings that can be transferred out per day** from any single savings provider, which could apply at a savings account level or be set by the savings provider.
2. **Setting clear obligations and responsibilities** on both the app provider and the savings provider to prevent liquidity shocks, such as requiring **agreement** between the app provider and the bank or building society prior to transfer of any funds and intended flows of customers and balances.
3. **Information sharing** to help account providers to understand whether savings are being transferred at the customer's request or automatically by an app.

For regulators:

4. Regulators need to ensure that existing **regulations are flexible** enough to allow deposit takers to respond to shifts in markets and consumer behaviour as Open Finance is adopted.
5. Policymakers also need to be **proportionate** in implementing Open Finance, basing its roll-out on specific uses where consumers or businesses clearly benefit.

**Scan here to read Frontier Economics' full report:
The impact of Open Finance on mutuals' business models**