

THE IMPACT OF OPEN FINANCE ON MUTUALS' BUSINESS MODELS

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Contents

1	Executive summary	4
2	Introduction	10
3	Qualitative assessment of impacts	12
3.1	Impact 1: Emergence of third-party provider solutions in savings	14
3.1.1	Disintermediation in the savings market	14
3.1.2	Changes in the savings product market	23
3.1.3	Changes in lending markets	26
3.2	Impact 2: Increased access to financial data and improved customer data via Smart Data	30
3.3	Impact 3: Changes to the regulatory requirements in the savings market	34
4	Quantitative assessment of impacts	37
4.1	Summary of the quantitative model	37
4.2	An illustrative view of the market today	38
4.2.1	Market	38
4.2.2	Representative mutuals	40
4.2.3	Balances that could switch because of Open Finance	42
4.3	Open Finance take-up scenarios	44
4.3.1	Proportion of customers on standard products that are able to engage with Open Finance	44
4.3.2	Proportion of balances on standard rates	46
4.3.3	The proportion of balances that actually switch	49
4.4	Open Finance equilibrium	52
4.4.1	Balances in the Open Finance equilibrium	52
4.4.2	Prices in the Open Finance equilibrium	54
4.4.3	Combined balance and price impacts in the Open Finance equilibrium	57
4.4.4	Strategic choices for firms and impact on lending markets	60
4.5	Liquidity risk	61
4.5.1	Balances theoretically exposed to automated sweeping	62

4.5.2	Impact of sweeping services on market outcomes	62
5	Conclusions	64
5.1	Summary of impacts from Open Finance	64
5.2	Implications for developing Open Finance	65
	Annex A Sensitivity analysis	69
A.1	Variation in type of product that customer balances switch to from instant access standard rate products	69
A.2	Relative pricing strategies of mutuals and the rest of the market	71
A.3	Distribution of balances on standard rates across age groups	72
	Annex B Case study: Open Finance and Smart Data in other jurisdictions	76

1 Executive summary

The introduction of current account data sharing and “read and write” access to third parties through Open Banking was the result of regulatory intervention in UK financial services to promote competition in retail banking. Open Finance would enable the sharing of data and “read and write” access to more financial services and potentially other industries via Smart Data. This may include providing third-party access to savings and mortgages products. The FCA has asked the cash savings industry to explore the potential to bring cash savings into Open Banking.¹

This paper sets out the potential impacts on the business models of the Building Societies Association (BSA) members that could result from the introduction of Open Finance and Smart Data in the UK cash savings market.

Open Finance impacts on the market

The main impact that the market may expect to face as a result of the introduction of Open Finance and Smart Data in the UK would be the emergence of third-party provider (TPP) solutions in the savings market. These solutions may use data from cash savings providers to help customers manage their cash savings. Depending on the functionality enabled through Open Finance, TPPs may provide services ranging from personalised notifications about savings rates and products through to automatic movement of balances to achieve the highest available interest rates.

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

Changes in customer behaviour

- **More customer switching between cash savings providers.** If customers adopt Open Finance solutions, more savings balances may move more frequently between providers than today, in particular for those balances on instant access standard rate products.² This may lead to a reduction in customer tenures on instant access products.
- **Movement of balances to fixed term, restricted access and instant access introductory rate products.** TPPs may help customers identify where they can optimally reduce access to some of their savings balances in return for higher interest rates, leading

¹ FCA Cash Savings Market Review 2023, p6.

² We define standard rate instant access products as products that customer funds move to after the expiration of the introductory rate they initially signed up to. Customers are able to withdraw funds from these accounts at any point without penalty. These products are not available to new customers to open an account and are sometimes referred to as the “back book”.

to an increase in balances held in fixed term and restricted access deposits. TPPs may also help customers identify introductory bonus rates on instant access products.

Market response to changes in customer behaviour

- **Reduction in bonus rates.** There may be a reduction in the size of the introductory bonus rates firms can offer to attract customers and balances on to instant access products as customer switching on standard rates increases.
- **Increases in average savings rates.** As a result of balances moving to higher interest products from standard rate products, average rates are likely to increase. At the market level, we estimate an increase in average savings rates of up to 25 – 48 bps in some scenarios where customer adoption of Open Finance is high.
- **Increased deposit stability for providers.** If customers optimise their savings towards fixed term deposits to secure higher rates, there may be a reduction in liquidity risk.³
- **More active management of savings balance sheet and pricing.** The increase in switching and price movements may require providers to change their hedging strategies and adopt a more active approach to managing their balance sheet and pricing.
- **An increased use of restrictions for accessing savings balances.** Providers may introduce restrictions to prevent large-scale automatic switching triggered by TPPs, which would reduce the availability of instant access products. If such restrictions are not effective, then there is a risk that interest rates offered for instant access are reduced to reflect the increased liquidity risk relative to fixed term products.⁴

Knock-on impacts on the mortgage market

- **Increasing mortgage rates.** The changes in the savings market, such as changes in the average rates, improved deposit stability and increased switching from standard rate products may lead to changes in the mortgage market. The increase in average market savings rates alone may lead to an increase in mortgage rates by up to approximately 21 – 41 bps if Open Finance adoption in the savings market is very high.

Open Finance impacts on mutual organisations

The extent to which mutual organisations are affected by the emergence of TPP solutions in the savings market may depend on their business model. Mutual business models differ in terms of the proportion of balances they hold on standard instant access rates and whether or

³ There may be a countering effect of an increase in liquidity risk on instant access products, which are more prone to switching.

⁴ In this scenario, there may be differences in the impact of Open Finance for different customer groups, depending on customer engagement and ability to lock away savings. Customers that engage with Open Finance solutions would obtain higher rates by switching to fixed term or restricted access products, if they are able to lock away some of their savings. Customers that do not engage with Open Finance solutions, or are unable to lock away savings, may face lower rates or lack of access to instant access products.

not they use introductory bonus rates to attract customer balances. Both of these factors may affect mutuals' exposure to disintermediation via Open Finance.

We estimate the changes to mutuals' average savings rate paid and, by implication, margin, under a plausible set of scenarios for the uptake of Open Finance enabled solutions and increased switching on standard rate instant access products for each type of mutual.⁵ Table 1 below summarises the modelling results.

Table 1 Impact of emergence of TPP solutions on mutual savings rates by type of mutual business model

	<u>Minority</u> of balances on standard instant access rates	<u>Majority</u> of balances on standard instant access rates
Bonus rate pricing model	Average savings rate decreases by 50 – 61 bps	Average savings rate increases by 19 – 29 bps
Flat rate pricing model	Average savings rate increases by 10 – 43 bps	

Based on our modelling, mutuals with a bonus rate pricing model that hold less than half of their balances in standard products may see a decrease in the average rates paid on their savings products and an increase in their net interest margin as customers adopt TPP solutions in the savings market. For other types of mutuals, there may be an increase in the average savings rate paid and a decrease in net interest margin.⁶

Mutuals that experience an increase in average savings interest rates may be able to pass the impact through to their mortgage pricing in line with the expected changes in mortgage pricing at the market level.

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

- Mutuals currently offer higher savings rates than the market average for instant access products. Mutuals may be less exposed to switching from instant access standard rate products due to Open Finance.

⁵ We use an economic model that shows the impact on average savings rates if customer balances increasingly switch from standard rate products to fixed term and introductory instant access and restricted access products and estimates the change in introductory and standard rates across the market and for mutuals by assuming that the Net Present Value of the savings business remains unchanged at the market level.

⁶ The modelling focuses on six types of “representative mutual” which are informed by data submitted by seven building societies (see section 4.2.2). Due to data limitations, credit unions are not considered as a separate business model, but grouped together with building societies in the “representative mutuals”.

- Depending on business model, some mutuals may see a reduction in cash savings interest rates as the increase in switching across the market means that they need to invest less in attracting customers.
- As mutuals have fewer financing options available to them than major banks, the increase in customer deposits held in fixed and restricted access savings accounts may generate a greater benefit to mutuals than for other market participants through the reduction in liquidity risk.
- Better customer data through Open Finance and Smart Data may improve risk pricing for mutuals in the lending market and may help to extend credit to previously underserved customers, but we expect this impact to be small.

The emergence of TPP solutions in savings may also present some **risks for mutuals**. Adapting to a savings market with more frequent and rapid price and balance movements may be relatively more challenging for mutuals than for other firms due to their smaller size, lower capability and restricted funding options.

- Changing market dynamics may require the development of new systems to handle the additional data, new product pricing and hedging strategies and may involve the automation of many processes around balance sheet management. Mutuals, in particular smaller firms, may lack the resources and capability to adjust to these changes as well as the rest of the market.
- The cost burden of implementing Open Finance regulation has the potential to be much more significant for mutual organisations than for other businesses due to their small size and relatively lower levels of digitisation.
- Building societies are less able than banks to raise funds from alternative sources such as wholesale funding markets, as they are required by law to raise the majority of their funds from saving members. In addition, building society-specific regulation restricts the proportion of a building society's balance sheet that can be funded by fixed rate products. These restrictions may limit mutuals ability to adapt their funding in response to market changes.

Implications for developing Open Finance

If UK regulators and policy makers decide to move forward with Open Finance, then it should be developed to minimise the potential risks that we have identified above. We recommend further consideration of the following:

1. If Open Finance was to enable the automatic transfer of deposits by a TPP on behalf of customers (e.g. "write" functionality), then the **TPPs that operate Open Finance enabled services in cash savings should face obligations** to help manage risks to the stability of institutions. This may include:
 - a. Notifying and confirming that the savings provider that is to receive a transfer of balances is willing to accept them, if the transfer meets certain criteria, such as if it above a certain transaction value.

- b. Limiting the value of transfers out of any single savings provider, such as setting limits for the total value that can be transferred out of an institution per day and requiring the TPP to provide a schedule for future payments to the savings provider.
2. **Cash savings providers should be permitted to:**
 - a. Choose the level and type of customer balances they wish to accept when a TPP requests a transfer, including choosing not to accept some or all balances. This may include not accepting any TPP transfers at any time. This should be facilitated by the TPP providing information about intended flows of customers and balances.
 - b. Introduce products that require notice for withdrawal
 - c. Reduce the availability of instant access products to TPP-managed cash savings.
3. **Regulators should ensure that:**
 - a. The costs of complying with Open Finance regulation are not excessive relative to the size of mutuals.
 - b. Funding rules imposed on building societies are flexible enough to respond to potential shifts in the structure of funding markets brought about by Open Finance.

Conclusion

In this report, we have considered the impacts on mutual business models from an Open Finance rollout into the savings market and other financial services. We have also considered how Open Finance could be designed to limit some of these risks.

However, we have not conducted an overall cost benefit analysis for expanding Open Finance to the savings market. In deciding whether to take Open Finance forward, regulators should consider:

- the potential benefits for some customers in terms of being able to earn higher savings rates as set out in this report;
- the unintended consequences of liquidity risk for some customers, such as potentially reducing the availability and interest rates offered for instant access products;
- the potential pass on of higher savings rates into higher mortgage rates;
- the likely adoption of Open Finance, which will determine the scale of impacts and benefits;
- the implementation costs for mutuals in relation to these benefits, especially for smaller firms;
- the funding restrictions imposed on mutuals; and
- the practicalities of implementing Open Finance, such as requirements to connect mutuals to Faster Payments to initiate balance transfers through Open Banking, or the feasibility of automated account opening.

The work that the UK Financial Conduct Authority (FCA) has proposed to explore the scope and opportunities for Open Banking capabilities to help customers make their money work harder in the cash savings market may provide a further analysis of these considerations.⁷

This analysis has been informed by Frontier research, discussions with BSA members and data provided by the BSA members. In the remainder of this paper, we summarise the background to this research and provide a qualitative assessment of the potential impacts and the key drivers behind them. We then report on quantitative analysis and economic modelling of the most significant impacts from Open Finance on the savings and mortgage markets and mutual organisations. The final section summarises our findings on how Open Finance would affect mutual organisations and discusses implications for developing Open Finance further.

⁷ FCA Cash Savings Market Review 2023, p44

2 Introduction

In 2016, the Competition and Markets Authority (CMA) completed an investigation of the retail banking market. Its findings highlighted a need for increased innovation and competition in the market.⁸ The CMA set out a series of remedies to address its concerns. As part of these remedies, the CMA mandated the nine largest current account providers (the “CMA9”) to create and fund the “Open Banking Implementation Entity” (OBIE), which oversaw the development of Open Banking.⁹ Open Banking was designed to improve competition and innovation in the banking and payment services markets, while giving customers more control over their financial data and improving customer protections.¹⁰

More recently, the FCA conducted its “Cash Savings Market Review 2023” assessing competition in the cash saving market and the actions needed to achieve better consumer outcomes – namely fair and competitive interest rates across all savings products. The FCA concluded that progress is still needed in the cash savings market, with the following outcomes expected in the near term:

- **A narrowing of the difference in rates applied to new and existing products:** More is needed to remove unfair differences in the pricing of products which are currently on sale to new customers, and those that are no longer on sale, but are applied to existing customers.
- **A reduction in balances earning low or no interest:** There should be a reduction in the proportion of easy access accounts with very low interest and the proportion of balances held in non-interest-bearing accounts.
- **An improvement in customer engagement with their savings:** firms need to be more effective at helping customers engage with their savings, for example by making it clear when customers could switch and access higher paying accounts or by encouraging regular savings”.¹¹

The next stages of Open Banking and data sharing, if taken forward, would be to go a step further and enable the sharing of data and “read and write” access from other types of financial

⁸ The CMA identified two broad issues in the retail banking sector. Firstly, they found a general lack of competition, with established, larger banks dominating the market and barriers to entry for new, smaller providers. Secondly, they found that complicated current account charging structures and lack of transparency made it difficult for customers to understand the value of services and to switch providers.

⁹ See: <https://www.gov.uk/government/news/millions-of-customers-benefit-as-open-banking-reaches-milestone#:~:text=Open%20Banking%20enables%20consumers%20and,save%20them%20time%20and%20money>.

¹⁰ Combined with the revised Payment Services Directive (PSD2), Open Banking grants third-party providers “read and write” access to customer payment account information. This enables third-party providers to access account information (such as transaction history) and initiate payments from those accounts on customers’ behalf. Third parties can then provide innovative services helping customers manage their spending, consolidate their finances and enabling super-fast payments. New services and entrants in the payments market then stimulate competition and further innovation.

¹¹ FCA Savings Market Review 2023, p6

services products (Open Finance) and other industries (Smart Data). This may include providing third-party access to savings and mortgages products. The FCA recognises how Open Finance has the potential to improve outcomes in the cash savings market by improving the information available to customers and encouraging switching to better rates.¹²

For the purposes of this report, we define Open Finance as the extension of Open Banking to include all retail financial products, such as savings, mortgages, insurance, unsecured lending, investments and pensions. When we refer to Smart Data, we mean customer data sharing (with customer's consent) to third-party providers in other sectors, including: utilities, telecoms providers, transport providers, social media and shopping platforms.¹³

Open Finance initiatives could potentially expose Building Societies Association (BSA) members' business models to increased disintermediation from third-party providers (TPPs). At the same time, the ability to access enhanced customer data on a range of financial services products via Open Banking and from other sectors via Smart Data provides new opportunities for mutual organisations. Changes to mutual business models may also have a knock-on impact on other financial services markets, such as mortgages, and to overall financial stability.

This paper sets out the potential impacts on BSA members that may result from the introduction of Open Finance and Smart Data in the UK. The paper first provides a qualitative assessment of the key factors driving each impact in section 3. Section 4 provides a quantitative assessment based on economic modelling of the most significant impacts on the market and building societies. We then set out our conclusions on how the savings market would change with the introduction of Open Finance and suggest how to safeguard against any unintended consequences in section 5.

This analysis has been informed by Frontier research, discussions with BSA members and data provided by the BSA members.

¹² FCA Cash Savings Market Review 2023, p30.

¹³ This definition is consistent with the sectors represented in the UK Smart Data working group.

3 Qualitative assessment of impacts

In this section we provide a qualitative assessment of the likely impacts that may affect mutual organisations as a result of the introduction of Open Finance and Smart Data in the UK.

For each impact, we first describe how the cash savings market, and other related markets such as lending, may change in response to the identified impact and how this would affect mutual organisations. We then describe the key factors that may drive the impact and the available evidence about the likely scale of each factor. We provide a qualitative assessment of the level of uncertainty about the final scale of the factor and the potential severity of the impact that this factor would have on mutuals.

We identify three main impacts that may affect mutual organisations as a result of the introduction of Open Finance and Smart Data in the UK. The impacts and the factors behind them are briefly summarised below.

Impact 1: Emergence of third-party provider (TPP) solutions in savings

1.1. Disintermediation in the savings market

- New players may enter the market as intermediaries that facilitate customer switching, mutuals may lose customer relationships, face increased competition and find it more difficult to compete in an increasingly price-driven market.
- Mutuals would have the opportunity to attract new customers via intermediaries reducing the costs of acquisition.
- Mutuals would have the opportunity to act as TPPs, provide new services and attract new customers.

1.2 Changes in the savings product market

- As a result of changes in customer switching, price levels and customer demand for deposits in the market may change.
- Mutuals may respond by adjusting prices, adjusting balances or changing product design.

1.3 Changes in lending markets

- Mutuals' cost of funds and available lending may have changed due to changes in market dynamics.
- Mutuals would change their amount of lending in the mortgage market, change the prices at which they lend out mortgages or lose market share.

Impact 2: Increased access to financial data and improved customer data via Smart Data

- Better customer data could increase profitability for mutuals in the lending market by improving risk pricing and extending the market to previously underserved customers.

Impact 3: Changes to the regulatory requirements in the savings market

- Regulatory requirements may create additional costs for mutuals via requirements to invest in Open Finance or by exposing them to payment fraud through Faster Payments. But there may also be savings from improved efficiency of regulatory reporting.

We identify 16 factors that drive the impacts summarised above.

In the table below, we provide a summary of these factors in terms of how they may impact mutuals, the level of uncertainty around their scale and the potential severity of impact on mutuals if the factor did play out in its most impactful form.

Greatest impact on mutuals if	Level of uncertainty about final scale of factor	Potential severity of impact on mutuals	Explored in quantitative analysis
1.1 Disintermediation in the savings market			
A High customer engagement with Open Finance enabled services	Medium – Open Banking provides a starting point	High	✓
B Final scope of Open Finance regulation includes read, write and account opening	High – still under discussion	High	✓
C Third-party providers able to offer good Open Finance solutions	Low – UK fintech market seen as thriving	Medium	✓
D High value of customer balances at risk of switching	Medium – further analysis required	High	✓
1.2 Changes in the savings product market			
E Rate differentials for mutuals are high	Medium – further analysis required	High	✓
F Regulatory restrictions on product design are introduced	Low – unlikely to be implemented	Medium	
G Mutuals' ability to differentiate their offer is limited	Low – BSA view of own business capabilities	Medium	
1.3 Changes in lending markets			
H Extent to which other savings providers are affected by Open Finance is limited	Medium – further analysis required	High	✓
I Competition in the mortgage market works well	Low – market is competitive	High	✓

THE IMPACT OF OPEN FINANCE ON MUTUALS' BUSINESS MODELS

Greatest impact on mutuals if	Level of uncertainty about final scale of factor	Potential severity of impact on mutuals	Explored in quantitative analysis
J Availability and cost of wholesale funding for mutuals is limited	Medium – unclear impact of Open Finance on wholesale funding costs	Low	
2 Increased access to financial data and improved customer data via Smart Data			
K Customer willingness to share data is high	Low – likely to be similar to Open Banking	Low	
L Size of the unserved market is large	Low – well researched	Low	
M Smart Data is high quality and well standardised		High	Low
3 Changes to the regulatory requirements in the savings market			
O Mutuals are required to make significant investments in Open Finance	Low – unlikely to be required disproportionate investment		High
P Mutuals are able to achieve significant savings from improved efficiency of regulatory reporting		Medium	Low

The uncertainty about the final scale of several of the factors is further explored in our quantitative analysis in section 4.

The following sections contain our qualitative assessment of the impacts and evidence behind the factors driving them.

3.1 Impact 1: Emergence of third-party provider solutions in savings

In this section, we provide a qualitative assessment of this impact. Section 4 below provides a more detailed quantitative assessment of this impact.

3.1.1 Disintermediation in the savings market

Market impacts

Open Finance would grant third-party providers (TPPs) access to customer data in savings. Access may be on a read basis, read-write basis or potentially read-write with account opening

features.¹⁴ This access would allow TPPs to provide a range of tailored products and services within the savings market, such as:

- financial management and optimisation services that better enable customers to understand and optimise their finances. Customers may become more aware of the performance of their savings and investments, and may rebalance their portfolios accordingly;
- tailored price comparison services that compare the rates available on different savings products and highlight the best rates available to the customer. Customers may be encouraged to switch if better rates are available, but have to conduct the switching themselves; or
- automatic switching services that build upon price comparison tools by undertaking the transfer of savings balances to products with better rates on behalf of the customer (with prior consent).

Moving money between accounts (“sweeping”) is already available under Open Banking, with nearly all of the CMA9 banks offering sweeping APIs.¹⁵ For example, through a TPP, consumers could set up a sweeping instruction to move excess funds to another account in their name without authenticating each time. Sweeping services could therefore be used for savings optimisation (between cash savings accounts), managing loan repayments or protecting against overdrafts.

Variable recurring payments (VRPs)¹⁶ are also possible under Open Banking and propositions are currently being developed. This alternative payment method will allow customer to connect authorised payment service providers to their bank account to make variable payments on the customer’s behalf (within agreed parameters) to a specified end point.¹⁷ VRPs can expand on sweeping services, allowing the automatic payment into savings or investment accounts with high interest.¹⁸

¹⁴ With read access, TPPs can only read or retrieve data without modifying it. With read-write access, they have both reading and writing capabilities, enabling them to make payments and transfers out of the account. Account opening functionality brings the ability to open new accounts on a customer’s behalf.

¹⁵ For example, HSBC were the first bank to complete the rollout of Sweeping APIs with variable recurring payments. See: <https://develop.hsbc.com/news/sweeping-vrp-open-banking-0>

¹⁶ Sweeping payments are one type of VRP. See here: <https://www.openbanking.org.uk/insights/variable-recurring-payments-what-are-they-and-how-can-they-help-smes/>

¹⁷ VRPs are therefore more flexible than existing recurring payments such as direct debits of card payment authority. VRPs have additional transparency and security advantages.

¹⁸ See: <https://truelayer.com/blog/recurring-payments/variable-recurring-payments-and-sweeping/#:~:text=Investments%3A%20while%20this%20currently%20falls,automatically%20into%20higher%20interest%20investments.>

This functionality is currently offered by a small number of Open Banking enabled TPPs.¹⁹ However, whilst sweeping and VRPs allow the movement of funds from current accounts to savings accounts, the reverse channel is not currently available. Information on wider savings portfolios is also unavailable to TPPs. Open Finance could therefore expand the scope of sweeping services by giving TPPs full sight over the savings held by consumers and enabling movement of balances between savings products. TPPs could then reallocate funds across a larger number of savings accounts to maximise returns for savers.

Open Finance services may be provided by new entrants into the savings market, such as fintechs, neo-banks or Big Tech.

The introduction of these disintermediation services would result in an increase in customer switching in the savings market and the loss of some customer relationships that are currently held by savings providers. But established banks and mutuals would also be able to take the role of a TPP and offer their customers services to optimise their savings balances. This would present mutuals with the opportunity to provide new solutions to customers, deepen relationships with their existing customers and acquire new customers.

Open Finance enabled services are likely to be more focussed on price than any other product features. This means that the nature of competition in the market may therefore become more price-driven than it is today. This may make it more difficult for mutuals that differentiate their products based on non-price factors to compete in the savings market. However, mutuals would have new opportunities to attract digitally active customers at lower cost via these intermediaries.

Switching services may also encourage the movement of balances from current accounts to savings accounts. This could increase demand for savings products if excess current account balances were moved towards interest-bearing savings accounts.²⁰

In summary, the impact on mutuals from these changes in the market would be:

- As TPPs enter the market as intermediaries and customer switching increases, mutuals may lose customer relationships, face increased competition and find it more difficult to compete in an increasingly price-driven market.
- Mutuals would have the opportunity to attract new customers via TPPs.
- Mutuals would have the opportunity to act as TPPs, provide new services and attract new customers.

¹⁹ Fintechs Chip, Cleo and Plumb use Open Banking to monitor transactions and balances in a connected bank account before automatically moving funds to a savings account depending on recent. In some cases, savings providers are able to connect with TPPs to provide connected savings accounts. For example, OakNorth, Alicia Bank and Clear Bank savings products are available through Chip.

²⁰ See: <https://www.openbanking.org.uk/wp-content/uploads/OBIE-Sweeping-Evaluation.pdf> table 1 for potential use cases of "sweeping"

Key factors

There are a number of customer, regulatory and market factors that will affect how likely the impacts are to be realised.

A. Customer engagement with Open Finance enabled services

Open Finance will make it easier for customers to be engaged with their savings and easier for financially engaged customers to switch. If there is greater engagement with Open Finance enabled services, then there is likely to be more switching and larger impacts on the savings market. We have reviewed some of the available evidence on likely customer engagement.

- Customer engagement with Open Banking enabled services in the UK is perhaps the best evidence for the likely potential engagement with Open Finance enabled services. Consumer engagement with Open Banking enabled services in the UK is currently fairly low but growing. In its most recent Open Banking impact report, it is estimated that about 11% of digitally enabled consumers and 17% of digitally enabled small businesses used Open Banking enabled services in mid-2023.²¹ It also shows gradual growth in Open Banking service use year-on-year, with 21% growth in the number of consumers and 11% of businesses between June 2022 and June 2023. The growth in use of Open Banking enabled services has primarily been driven by growth in Open Banking enabled payments, rather than data access.
- Open Finance would require customers to share their data with TPPs. Consumer attitudes to data sharing would therefore have a large impact on the take-up of Open Finance enabled services. In the UK, the BSA's Digital attitudes survey shows that 24% of customers were comfortable sharing their data with third parties for financial purposes in 2023.
- Data from the EU shows that currently only 20% of respondents across 12 European countries are willing to share financial data with banks or third-party providers as part of PSD2. Purchase discounts, free banking services, or automated tax returns are the most effective incentives to encourage customers to share their data. Data shows that 17% of customers trust in traditional banks and card providers, but this has decreased by four percentage points since 2018. Only a small percentage of customers trust payment service providers (9%) and retailers (8%), and an even lower percentage trust neo-banks and fintechs (3%).²²
- Demographic characteristics are also likely to be a relevant factor for engagement with Open Finance, as younger generations tend to be more digitally active. BSA's Digital attitudes survey shows that the age group 25-34 have the highest levels of willingness to share data to help with managing their finances (39%). 31% of people aged 18-24 and

²¹ See: <https://openbanking.foleon.com/live-publications/the-open-banking-impact-report-october-2023/>

²² See <https://www.strategyand.pwc.com/de/en/industries/financial-services/open-banking-and-payments-survey.html>

35-44 are willing to share their data, but only about 20% of those aged 45-64 and 10% or less of those aged over 65 are comfortable with data sharing.

- However, older customers are becoming increasingly digitally engaged. For example, the adoption of digital banking services has seen the most significant increase among individuals aged 55 and over during the pandemic.²³

Qualitative assessment: Customer engagement with Open Finance enabled services

Level of uncertainty: medium. Initial customer engagement with Open Finance enabled services is likely to be similar to engagement with Open Banking enabled services, which is well studied, but there is scope for it to be different depending on the services offered.

Severity of potential impact: high. Greater customer engagement with Open Finance enabled services could make impacts on mutual business models much more significant.

We model different levels of customer engagement with Open Finance enabled services in section 4.3.1.

B. Final scope of Open Finance regulation

The scope of Open Finance would have a significant impact on the types of services TPPs are able to offer and their attractiveness to customers.

- If TPPs are only able to use “read” functionality, the services that Open Finance would enable would be limited to enhanced information about the customer’s finances and the deals available on the market (e.g. personalised, rather than generic, prompts for customers if their savings interest rate is lower than they could get elsewhere). While this may have some positive impact on switching, it is likely to be fairly limited.
- If TPPs are able to “read” and “write”, Open Finance would allow TPPs to move customers’ money between their own accounts to optimise it for the best value. These propositions may generate more value to customers than a “read” service and lead to more switching of customer balances among their existing savings providers.
- If TPPs were able to “read”, “write” and also provide a largely automated “account opening” service (such as where the customer would be able to switch with a single click and the app ‘takes care of the rest’), Open Finance could have a more significant impact on the savings market. With automated switching, Open Finance could lead to rapid

²³ For all, see <https://missive.co.uk/insights/effective-audience-segmentation-for-open-banking-could-be-the-key-to-unlocking-growth/>

THE IMPACT OF OPEN FINANCE ON MUTUALS' BUSINESS MODELS

switching of customer balances between providers in response to price differentials in the market.

TPP Functionality	Pre-Open Banking	Open Banking	Open Finance "Read"	Open Finance "Read-Write"	Open Finance "Read-Write-Open"
Generic information about best current accounts available in the market	✓	✓	✓	✓	✓
Personalised information and prompts about best current accounts available in the market		✓	✓	✓	✓
Move customer current account balances between existing accounts to optimise value		✓	✓	✓	✓
Generic information about best savings rates available in the market	✓	✓	✓	✓	✓
Personalised information and prompts about best savings rates in the market			✓	✓	✓
Move all customer balances between all existing accounts to optimise value				✓	✓
Open new accounts on customers' behalf to move balances to the best deal on the market and optimise value					✓

The extent to which regulation ensures data standardisation and enables smooth customer journeys may also have a significant impact on the success of Open Finance and the resulting scale of impact on the savings market.

- API standardisation could result in greater adoption of Open Finance. For instance, the OECD considers that standardised APIs could provide more aligned incentives between different market participants in the Open Finance ecosystem such as banks and TPPs, as well as promoting more efficient investment in appropriate technology.²⁴ In the European Commission's PSD2 implementation study, 36 out of 62 stakeholders strongly

²⁴ Shifting from Open Banking to Open Finance. Results from the 2022 OECD survey on data sharing frameworks <https://www.oecd.org/finance/shifting-from-open-banking-to-open-finance-9f881c0c-en.htm>

advocated for a single global API standard to facilitate payments. Some mentioned that standardizing APIs could further harmonize the EU, reducing market uncertainty, complexity, and costs.²⁵

- The more that regulation allows for a smooth customer experience using Open Finance products, the higher adoption is likely to be. For example, under Open Banking customers were originally required to re-authenticate for any TPP services that they were using every 90 days to ensure their continuous consent of sharing their data. This rule was later identified to create friction in the customer experience and potentially limit the growth in Open Banking. The FCA changed the rules in 2022 to allow for a more seamless customer journey.²⁶

Qualitative assessment: Final scope of Open Finance regulation

Level of uncertainty: high. Regulation still under discussion.

Severity of potential impact: high. Types of services that TPPs are able to offer would have a significant impact on how much switching may increase in the market and therefore the scale of impact on mutuals.

We model different types of Open Finance regulation in section 4.3.3.

C. Third-party provider capabilities

The existence of a thriving financial services ecosystem is likely to contribute to the success of Open Finance. The more TPPs are able to react to customer demand and capitalise on new regulation, the greater customer engagement with Open Finance and switching in the savings market is likely to be.

- Since the implementation of Open Banking, the UK has experienced significant growth and diversity in new fintech third-party providers. Nearly 300 unique firms operate in this sector, and market analysts anticipate it will double in size by 2026, exceeding a total market value of £31bn.²⁷
- The UK is seen as a hub for innovation in financial services. Most recent data for the FCA regulatory sandbox shows that more than 600 firms applied to the program and 188 were

²⁵ A study on the application and impact of Directive (EU) 2015/2366 on Payment Services (PSD2)
<https://op.europa.eu/en/publication-detail/-/publication/f6f80336-a3aa-11ed-b508-01aa75ed71a1/language-en>

²⁶ <https://www.fca.org.uk/firms/strong-customer-authentication>

²⁷ Shifting from Open Banking to Open Finance. Results from the 2022 OECD survey on data sharing frameworks
<https://www.oecd.org/finance/shifting-from-open-banking-to-open-finance-9f881c0c-en.htm> .

successfully accepted since its launch.²⁸ Moreover, financial intermediation presented the highest share (50%) of innovation by active business within the distribution and services sector during the period 2018-2020.²⁹

- The FCA's analysis of the savings rates available to UK customers has highlighted that challenger banks offer customers better value than those of traditional banks: in January 2022 major banks offered a median instant access rate close to the 0.25% base rate, while challenger banks provided 0.4%. By July 2023, with the base rate at 5%, digital challengers offered a median of 3.7%, while major banks had a median of 2%. Despite this, challenger banks may still lack the ability to attract a significant number of customers. Data on market share shows that digital challengers were only able to increase their savings market share in terms of customers from 3.7% to 3.9% between January 2022 and March 2023 while the nine largest lenders grew from 48.3% to 49.7%.³⁰

Qualitative assessment: Third-party provider capabilities

Level of uncertainty: low. The UK fintech market is seen as thriving, with significant growth and diversity in new fintech third-party providers since the implementation of Open Banking.

Severity of potential impact: medium. Better TPP capabilities are likely to increase customer engagement with Open Finance, which could make impacts on mutual business models more significant.

We model different levels of third-party provider capabilities in section 4.3.3.

D. The value of switching balances

The relative value of balances held by the customers that switch savings provider as a result of Open Finance will also affect the scale of the impact that Open Finance is likely to have on the savings market.

- Half of all UK savings balances are currently held in Individual Savings Accounts (ISAs).³¹ Due to their tax status, balances in non-ISA accounts are easier for customers to switch to a different provider than ISA balances. For Non-ISA accounts, customers can simply open an account and move any part of their savings balance over to the new account

²⁸ Regulatory Sandbox accepted firms <https://www.fca.org.uk/firms/innovation/regulatory-sandbox/accepted-firms> .

²⁹ UK innovation survey 2021: report (Figure 4.1) <https://www.gov.uk/government/statistics/uk-innovation-survey-2021-report> .

³⁰ For all, see <https://www.fca.org.uk/publication/multi-firm-reviews/cash-savings-market-review-2023.pdf>.

³¹ According to the 'Annual savings statistics', at the end of 2021 to 2022 the market value of Adult ISA holdings stood at £741.6 billion. FCA data show that consumers collectively hold around £1.5 trillion in savings accounts. Hence, ISA share is 49.8%. <https://www.gov.uk/government/statistics/annual-savings-statistics-2023/commentary-for-annual-savings-statistics-june-2023>

(other than any savings in a fixed term account). For ISA accounts, there is an additional step for customers as they need to fill out an ISA transfer form and wait for the transfer to take place (up to 15 working days for cash ISAs). Open Finance may have different impacts on ISA and non-ISA savings accounts as the steps involved in switching balances are different.

- When considering the deposits of the nine largest banks and building societies, the Bank of England finds that 16% are non-interest-bearing and 60% are low-interest instant access savings.³² The FCA's Financial Lives Survey finds that nearly 30% UK adults do not have a savings account of any kind.³³ Open Finance could move these low-interest balances towards interest-bearing saving accounts, accelerating recent trends.³⁴
- FCA research finds that only 23% of savers switched savings account in the last 6 months to get a better interest rate. Earlier research from the CMA suggests switchers tend to be younger with greater use of the internet and multi-banking.³⁵ While not observed in the CMA study, there is some evidence that those with higher incomes are more likely to switch bank accounts.³⁶ As younger savers age and their savings balances grow, switching could naturally increase. Open Finance could further increase the rate of switching.

Qualitative assessment: The value of switching balances

Level of uncertainty: medium. The share of savings in lower interest rate products gives some indication of the value of balances that are most prone to switching. However, to better understand the value of switching balances, further analysis is required on customer demographics and switching behaviour. This is provided in the quantitative assessment part of the report.

Severity of potential impact: high. Greater switching balances could make impacts on mutual business models much more significant.

We model the value of switching balances under Open Finance in section 4.3.2.

³² See Figure 1 in <https://www.fca.org.uk/publication/multi-firm-reviews/cash-savings-market-review-2023.pdf>.

³³ FCA Cash Savings Market Review 2023, p11

³⁴ From January 2022 to May 2023, deposits held within the CMA9 have gradually moved away from instant access accounts and towards fixed term accounts. Specifically, there has been a 4% reduction in instant access deposits and a 3% increase in fixed term deposits. See the FCA Cash Savings Market Review 2023, p11.

³⁵ CMA. Retail banking market investigation. Quantitative analysis of searching and switching in personal current accounts p4.
https://assets.publishing.service.gov.uk/media/55d459a540f0b609ff000003/Quantitative_analysis_of_searching_and_switching_in_personal_current_accounts.pdf

³⁶ Account holders who switched or did not switch bank accounts in the last year in the United Kingdom (UK) in 2015, by income <https://www.statista.com/statistics/467295/switching-bank-accounts-income-profile-uk/>

3.1.2 Changes in the savings product market

Before considering the changes that Open Finance may have on the savings market, we briefly summarise the key drivers of prices in the market below.

- Fixed term savings products are priced competitively - reflecting the current demand and supply of deposits from financial institutions and savers respectively.³⁷ A “liquidity premium” is needed to compensate savers for locking away funds for an extended period of time. Financial institutions are willing to offer a higher rate on fixed term products as they grant certainty of available funds and the date of withdrawal.
- Instant access products are also priced competitively, reflecting changes in supply and demand factors. However, rates tend to be lower than fixed rate products due to the liquidity risk that financial institutions take when allowing instant withdrawals, making them less attractive to financial institutions than fixed rate products. Interest rates also reflect the cost of providing the account.
- Instant access products may also offer introductory bonus rates for time limited periods to attract new customers. The size of the bonus reflects an expectation that some balances will be retained at the end of the introductory period. The greater the expected retention at the end of the introductory period, the higher is the introductory bonus that financial institutions are able to offer for these balances.

Market impacts

When customers switch more frequently, easy-access deposits will reduce in value to financial institutions relative to longer-term, fixed deposits.

- If instant access deposits are more prone to switching and more responsive to relative interest rates, then the tenure of deposits would fall and the persistency of balances may become more uncertain. This exposes financial institutions to increased liquidity risk making it harder for financial institutions to manage liquidity effectively. Increased liquidity risk will, in turn, constrain maturity transformation, as financial institutions may need to limit the value of assets tied up in longer-term investments, to meet any large-scale deposit withdrawals.³⁸
- Longer tenure deposits (such as deposits in fixed savings products) would therefore become relatively more valuable to financial institutions, as these present a more predictable and stable deposit base to lend against.

³⁷ See the FCA's update on the cash savings market here: <https://www.fca.org.uk/news/statements/fca-publishes-update-cash-savings-market>

³⁸ Bank and capital liquidity. Quarterly Bulletin of the Bank of England <https://www.bankofengland.co.uk/-/media/boe/files/quarterly-bulletin/2013/bank-capital-and-liquidity.pdf>

It is unclear what the net effect of increased customer switching and potential liquidity risk would be on interest rates. Open Finance may lead to a reduction in rates offered on easy-access deposits relative to fixed deposits.

Another possible market dynamic is a change in the differential between introductory and standard rates. Currently, providers tend to offer a higher rate for a set period which then reverts to a lower rate at the end of the period. If switching in the savings market increases as a result of Open Finance, the expected retention of balances at the standard rate after the end of the introductory period would be lower. Firms would be less willing to offer the same introductory bonus if retention of standard rate balances is lower. Firms may reduce the introductory rates offered to account for lower retention on standard rates, or they may increase the standard rates in order to improve retention of customers on these rates. As a result, a possible impact from Open Finance would be a narrowing of the price differential between the introductory and standard rates in the savings market.

Mutuals would be able to react to the increase in customer switching and changes in savings rates in different ways. At a high level, mutuals would have a choice between flexing rates, changing product balances and changing product design and non-rate features in response to the changing market conditions.

- **Flex rates:** mutuals could respond to changes in the market wide price dynamics by changing their interest rates, including the rate differentials between fixed term and instant access products and between their introductory and standard rate products.
- **Change balances:** mutuals could adapt to the changes in market rates by changing the distribution of balances held between different types of savings products.
- **Adapt product design:** mutuals could change their product features in order to offset some of the customer switching dynamics. For example, they may introduce restrictions on access and/or withdrawal penalties for instant access products to lock in deposits for longer time periods and increase tenure, or stop offering instant access products altogether. Mutuals could also introduce fixed term products with shorter terms (e.g. 1-6 months), to guarantee deposits over shorter time horizons.
- **Non-rate financial incentives** such as one-off payments or loyalty rewards, could be used to increase demand for certain products (for example, fixed term savings).
- **Differentiate based on non-price factors:** mutuals could focus on attracting and retaining customers by differentiating their offer in terms of the service provided, such as personalised advice and a physical branch network.

In summary, as a result of changes in customer switching, the price levels, demand for and supply of deposits in the market may change. Mutuals may respond by adjusting prices, adjusting balances or changing product design.

Key factors

The key factors that would determine the extent to which the savings market changes as a result of customer switching are the level of rate differentials in the market and the mutuals' ability to adapt their savings product offer.

E. Rate differentials in the savings market

- The differential between the savings rates offered by mutuals and the **rest of the market** will affect the extent to which increased switching would impact mutual organisations. If the rates offered by mutuals are currently relatively low compared to the rest of the market (for example, because mutuals offers are stronger on non-price factors), mutuals may be more exposed to losing balances when customer switching increases as a result of Open Finance. If instead the rates offered by mutuals are on average higher than those offered by the rest of the market, mutuals may experience an increase in demand for balances.
- The rate differentials between mutuals' **fixed term and instant access products** and between **introductory and standard rates** would also affect how impacted mutuals are by Open Finance. The greater the differentials in the prices offered by mutuals, the greater the impact of Open Finance may be as these differentials contract due to customer switching.

Qualitative assessment: Rate differentials in the savings market

Level of uncertainty: medium. Further analysis is required to understand the level of rate differentials for different products between mutuals and the rest of the market. This is included as part of the quantitative assessment.

Severity of potential impact: high. Greater differentials will encourage greater switching which could make the impacts on mutuals business models much more significant.

We model the rate differentials in the savings market in section 4.2.2.

F. Regulatory restrictions on product design

One of the key changes to product design that mutuals may want to introduce in response to the increased customer switching driven by Open Finance is the ability to introduce notice periods and limit access to accounts that are currently instant access. There is currently no regulation that restricts firms' ability to introduce these product features.³⁹ If such regulation

³⁹ While there is no regulation specifically limiting changes to product design, any product restrictions would have to take into account the fair treatment of vulnerable customers (see [Guidance for firms on the fair treatment of vulnerable customers | FCA](#)).

were to emerge in the future, this could have an impact on mutuals' ability to respond to market changes as a result of Open Finance.

Qualitative assessment: Regulatory restrictions on product design

Level of uncertainty: low. Regulatory restrictions on product design are unlikely to be implemented.

Severity of potential impact: medium. Restrictions on product design could reduce mutuals' ability to offset customer switching.

G. Mutuals' ability to differentiate their offer

Mutuals may be able to limit the impact of Open Finance on their business models by differentiating their offer on a non-price basis. The extent to which they are able to do so would depend on how well they are able to serve customers in an increasingly digitally enabled, price-focussed landscape of competition in the savings market.

BSA members vary in terms of their digital capabilities and many are currently undergoing digital transformation programmes. The overall assessment of the BSA members on their own capabilities is that they are somewhat less digitally capable and agile than other market players and need to improve their technology offer. Being less well positioned to adjust their offering in a more digital marketplace may lead to a greater impact from Open Finance on mutual business models.

Qualitative assessment: Mutuals' ability to differentiate their offer

Level of uncertainty: low. The assessment of the BSA members on their own capabilities is that they are less digitally capable and agile than other market players.

Severity of potential impact: medium. Being less well positioned to adjust their offering in a more digital marketplace may lead to a greater impact from Open Finance on mutual business models.

3.1.3 Changes in lending markets

Market impacts

The changes in total stock of deposits and the tenure of these deposits available to mutuals in the savings market would impact the balances available for the lending side of the business and the price mutuals are able to offer on their loans.

Additionally, the lower tenure of deposits would create potential liquidity risks for mutuals that would need to be managed. At the extreme, rapid switching facilitated by third-party intermediaries would substantially increase liquidity risk of withdrawn deposits not being covered by existing assets (either interest payments on loans or the sale of other assets). Managing this liquidity risk could create high additional costs for mutuals. The increased costs from the liquidity risks would have similar implications to the changes in available deposits and price changes in the market.

- 1 **Mutuals may keep the amount of lending in the mortgage market unchanged** and look for alternative sources of funds to provide loans. Other funding sources, such as debt and other wholesale financing, are typically more expensive than deposits and would likely reduce profitability.
- 2 **Mutuals may reduce the amount of lending in the mortgage market** in line with the deposits available to them. This would keep the overall profitability level for a given amount of deposits the same, but reduce the overall profits of firms.
- 3 **Mutuals may increase the prices they charge for mortgage lending** in order to offset the cost increases for savings deposits.
- 4 If the changes in deposits available and costs are significant enough, **some mutuals may not be able to sufficiently adjust the lending side of their business and lose market share or be forced to exit the market.**

In summary, mutuals' cost of funds and available lending may change due to changes in savings market dynamics. Mutuals may change their amount of lending in the mortgage market, change the prices at which they lend out mortgages or lose market share.

Key factors

H. Extent to which other savings providers are affected by Open Finance

Mutuals would not be the only financial institutions affected by Open Finance. The increase in average prices of deposits and liquidity risk would affect other savings providers such as mainstream banks as well.

As these providers also make up the majority of the lending in the mortgage market, the impact that Open Finance has on mainstream banks' savings business will affect their lending in the mortgage business and ultimately the competitive dynamics of the mortgage market as a whole.

The business model of mainstream banks is different to building societies: they have access to more varied sources of funding such as current account deposits, as well as a greater range of lending options such as unsecured credit. This means that mainstream banks would likely have a greater ability to mitigate any impact that Open Finance would have on prices and deposit tenure on their savings business across the rest of their product portfolio. As Open Finance creates changes in the savings market, the prices in the wider mortgage market may increase, but likely to a lesser extent than the cost increases faced by mutuals. The full extent of the changes in mortgage market pricing would depend on the extent to which mainstream banks are able to mitigate the changes in the savings market via their wider product portfolio relative to their mortgage products.

Qualitative assessment: Extent to which other savings providers are affected by Open Finance

Level of uncertainty: medium. Further analysis is required to understand the effects of Open Finance on the wider savings and mortgage markets. This is provided in the quantitative assessment part of the report.

Severity of potential impact: high. The prices in the wider mortgage market may increase, but likely to a lesser extent than the cost increases faced by mutuals, this limits mutuals ability to recover cost increases.

We model the extent the rest of the savings market is affected by Open Finance in section 4.4.

I. Competition in the mortgage market

In addition to the extent to which other providers are affected by Open Finance, the level of competition in the mortgage market would be a key factor determining the extent to which mutuals are able to pass on any cost increases in the savings side of the business onto the lending side of the business.

The FCA's Mortgage market review in 2019 found that the UK mortgage market works well and that the majority of customers are able to shop around and get a good deal. Switching in the mortgage market has been steadily increasing. According to the FCA, the number of mortgage borrowers not switching to a better deal and missing potential savings has dropped

significantly since 2016. In 2022 it was estimated that only 370,000 mortgage holders could save money by switching, down from 800,000 in 2016.⁴⁰

Mutuals account for 23% of all UK mortgage lending.⁴¹ In a competitive market with many providers such as the UK mortgage market, mutuals are likely to be price takers and therefore have limited ability to unilaterally raise prices.

Qualitative assessment: Competition in the mortgage market

Level of uncertainty: low. The mortgage market is considered to be competitive overall with high levels of disintermediation.

Severity of potential impact: high. Mutuals may have a limited ability to offset cost increases in the rest of their business by unilaterally increasing prices charged for mortgage lending.

We model the impact on the mortgage market in section 4.4.4.

J. Availability and cost of wholesale funding for mutuals

If mutuals faced a change in the customer deposits available to them for lending activities, they could potentially use wholesale funding instead. If wholesale funding was cheap and easily available, this could limit any potential negative profitability impacts from emergence of TPP solutions in savings.

However, mutuals are subject to “the funding limit” in the Building Societies Act (1986) which requires that at least 50% of funding is from members’ deposits in savings accounts. This would mean that in practice the mutuals ability to raise wholesale funds may be very limited compared to other financial institutions such as banks.

Other savings providers such as mainstream banks would also be affected by Open Finance, and may adjust their funding portfolios accordingly. More broadly, other market changes taking place while Open Finance is rolled out could have an impact on availability and cost of wholesale funding. It is therefore unclear how changes to the cost and availability of wholesale funding would affect mutuals.

⁴⁰ FCA switching in the mortgage market – an update <https://www.fca.org.uk/news/news-stories/fca-issues-update-switching-mortgage-market>.

⁴¹ According to the BSA, total mortgages from building societies amounts to £375 billion, representing 23% of total mortgage balances outstanding in the UK <https://www.bsa.org.uk/media-centre/press-releases/building-society-sector-performs-strongly-in-first-nine-months-of-2023>.

In practice, mutuals' own assessment is that they would not be able to increase their wholesale funding significantly beyond their current levels even before they approach the Building Societies Act limit as this could create a risk of a loss of credibility in credit markets and increase the cost of borrowing.

Qualitative assessment: Availability and cost of wholesale funding for mutuals

Level of uncertainty: medium. It is unclear how wider demand for wholesale funding will impact the availability and cost of wholesale funding for mutuals.

Severity of potential impact: low. Mutuals are unlikely to be able to rely on significantly increasing wholesale funding to offset any potential negative profitability impacts from increased switching in savings.

3.2 Impact 2: Increased access to financial data and improved customer data via Smart Data

Market Impacts

Open Finance would provide lenders with additional financial data on their customers, covering information on savings, investments, pensions, loans and any other financial services used. Smart Data can add to this by providing non-financial data which could give an indication of creditworthiness,⁴² such as energy use, utility bills and social media data.⁴³ Additional data can improve the accuracy of credit scoring and risk assessments by providing a more comprehensive and granular view of customers' finances than exists currently.⁴⁴

Improved risk assessments would translate into improved risk pricing, which can directly improve the profitability of loans. Profitability can increase by better matching loans' terms to a borrower's risk (rather than grouping within customer groups). This could also result in credit being extended to new customers that previously would not be served – opening another channel of demand and profits.⁴⁵ Relatedly, adverse selection can be mitigated by filtering out unprofitable, higher risk customers that were served previously.

⁴² See: <https://seon.io/resources/social-media-credit-scoring/#:-:text=Social%20media%20credit%20scoring%20uses,of%20borrower%20you%20could%20be>.

⁴³ See: <https://www.openbanking.org.uk/open-finance/#:-:text=Open%20finance%20will%20extend%20these,lead%20to%20'open%20everything'>.

⁴⁴ Simple credit scores often only focus on a limited set of information such as credit history and income. See: <https://www.equifax.com/personal/education/credit/score/articles/-/learn/how-is-credit-score-calculated/>

⁴⁵ See: <https://www.f5.com/glossary/open-banking/#:-:text=Evolution%20of%20Open%20Banking%20Technology,and%20enabling%20innovative%20financial%20services>.

While this additional data could improve the accuracy of credit scoring and risk assessments, its impact is likely to be small as the most relevant financial information for lending decisions is already accessible through Open Banking, such as salary and spending patterns.

There may be other, smaller, benefits from improved customer data and analytics which also increase profitability. Enhanced data analytics can improve the speed and automation of loan applications and approvals, saving costs for creditors and improving the customer experience.⁴⁶ Data-driven advice may help mitigate default risk by providing borrowers with budgeting tips and payment reminders. Additional data can also lead to improved advertising on lending products, increasing demand for those products.

In summary, expanded customer data could increase profitability for mutuals in the lending market by improving risk pricing and extending the market to previously underserved customers, but improvements are expected to be small given the most relevant financial information for lending decisions is already accessible through Open Banking.

Key factors

The key factors that would determine the extent of any profitability improvement in the lending market are customers' willingness to share data, the quality of shared data and mutuals' data capabilities compared to competitors.

K. Customer willingness to share data

A significant challenge from Open Banking has been the low proportion of customers that are willing to share their financial data with third parties (as described in section A). If individuals are unwilling to share non-financial data or additional financial data⁴⁷, the potential to expand the customer base or improve risk modelling on existing customers is reduced. This factor would be particularly important for the customers that are currently underserved or financially excluded. They are likely to be lacking financial data or credit histories, and in order to be able to participate in lending markets they would need to grant access to alternative, potentially more personal data sources.

⁴⁶ A Smart Data discussion paper by DESNZ (then BEIS) highlights how automation has been beneficial in cutting costs for Credit Unions. See: <https://assets.publishing.service.gov.uk/media/64ac1728b504f7000ccdb88c/smart-data-phase-1-discussion-paper.pdf>

⁴⁷ In addition to information provided by Open Banking.

Qualitative assessment: customer willingness to share data

Level of uncertainty: low. Customer willingness to share data is likely to be similar to Open Banking.

Severity of potential impact: low. Greater financial and non-financial data sharing could increase the potential benefits to risk modelling and lending profitability, but the impact is expected to be small given the most useful data for lending is already available from Open Banking.

L. Size of the unserved market

Survey evidence suggests that a large proportion of the UK population is currently underserved by financial institutions. For example, a 2022 FCA study finds that 1.1m UK adults (c.2% of the population) do not have a current account.⁴⁸ These people are likely to be completely excluded from accessing credit from mainstream lenders. A 2022 PWC survey concludes that over a third of adults, while technically eligible for credit, have difficulty in accessing credit from mainstream lenders.⁴⁹ Enhanced data on these underserved customers could therefore have a large impact on expanding the credit market.

The PWC survey also finds that the underserved tend to be younger with lower incomes and lower savings, and are generally higher risk.

Qualitative assessment: Size of the unserved market

Level of uncertainty: low. The size of the unserved market is well researched.

Severity of potential impact: low. Currently underserved customers have lower incomes and are unlikely to contribute significant improvements in profitability if lending was expanded to this group.

M. Quality and standardisation of Smart Data

High quality data would be directly usable in lending decisions, providing valuable information on customers' risk rather than irrelevant noise. The general expectation is that additional data on investments, pensions, loans, as well as from other industries such as energy and telecoms

⁴⁸ See p47: [Financial Lives 2022: Key findings from the FCA's Financial Lives May 2022 survey](#)

⁴⁹ See: <https://www.pwc.co.uk/industries/assets/financially-under-served-report-2022.pdf>

can complement existing financial data and improve risk modelling. However, without knowing specifically what types of data would be available under Smart Data, the magnitude of improvements in risk modelling is unclear, and Open Banking already provides the most useful data for lending decisions.

The completeness of data will also affect its usefulness. The standards around Smart Data sharing should be set up in a way that ensures that data is available on the majority of customers. Incomplete data could be significantly less useful in risk modelling. If a phased approach⁵⁰ to Open Finance is used (for example, with investment, insurance and pension data not initially available), then the benefits to risk modelling may take a longer time to materialise.

The lack of standardised data formats and definitions was identified as a key challenge faced by firms when sharing Open Banking data.⁵¹ Unclean or unformatted data reduces its usefulness in any modelling, or adds processing costs to get the data into a useable format. If not addressed, additional data from Open Finance could exacerbate this challenge and limit any benefits. Clear API standards will also be crucial to ensure data is shared in a consistent format between TPPs and API providers.

Qualitative assessment: Quality and standardisation of Smart Data

Level of uncertainty: high. The quality of Smart Data is currently unknown and will depend on regulatory standards on data sharing and APIs, stakeholders' data capabilities and the total amount of customer data available.

Severity of potential impact: low. Higher quality Smart Data could increase the potential benefits to risk modelling and lending profitability, but the impact is expected to be small given the most useful data for lending is already available from Open Banking.

N. Mutuals' capabilities to capitalise on the data

For a given level of quantity and quality of data, the impact of Smart Data of mutuals would depend on their ability to integrate and use customer data compared to competitors. If mutuals gain a competitive advantage in risk pricing, then they would likely see a greater positive effect on profitability. Conversely, if mutuals fall behind in this aspect, their profits could suffer relative to competitors.

⁵⁰ See section B for a discussion of a phased rollout of Open Finance.

⁵¹ See: FCA Feedback Statement 3.42

Current data capabilities vary across mutuals, with some offering more digital services and having an established digital strategy, whilst others are further behind in digital offerings. However, the assessment of BSA members is that they are generally behind competitors in terms of digitalisation and data use. For example, most mutuals have not been directly involved in Open Banking, so may have a disadvantage compared to larger banks (CMA9) that already have Open Banking capabilities.

Competitors and their offerings in the lending market would evolve with Open Finance too. For example, Big Tech may enter the lending market and gain a competitive advantage by combining data from Open Finance and Smart Data with their own customer insight, therefore reducing the mutuals' relative ability to capitalise on Smart Data in the lending market.⁵²

Qualitative assessment: Mutuals' capabilities to capitalise on the data

Level of uncertainty: low. The assessment of BSA members is that they are generally behind competitors in terms of digitalisation and data use.

Severity of potential impact: medium. If mutuals are less capable than their competitors in using data to improve risk pricing, their profits may suffer.

3.3 Impact 3: Changes to the regulatory requirements in the savings market

Market Impacts

Implementing open data sharing rules in any market would come with new regulation and the potential requirement for providers in the market to comply with the regulation. Depending on the final regulatory framework, the introduction of Open Finance in the savings market could result in mutuals being required to comply with certain levels of data sharing across the industry.

The regulation would likely be associated with some costs for the mutuals to implement the rules. Likely costs include investment in technology to meet data sharing standards, compliance and legal costs, regulatory fees and reporting costs. The higher the incremental cost faced by mutuals, the more significant the impact of Open Finance would be on mutuals' profitability.

⁵² The FCA is investigating the possible competitive effects and harms of data asymmetries between big tech and financial services firms. It is considering intervention that may be needed such as facilitating access to Big Tech firms' data to remove asymmetries. Any competitive advantages to Big Tech will therefore be influenced by the regulatory environment. See: <https://www.fca.org.uk/publication/call-for-input/potential-competition-impacts-data-asymmetry-between-big-tech-firms-and-firms-financial-services.pdf>

Open Finance regulation may also require all UK savings accounts to become part of the UK Faster Payments System network. Payment providers using Faster Payments are exposed to relatively high payment fraud (annual losses of £485m in 2022) and high costs associated with fraud prevention and customer reimbursement.⁵³ Becoming part of Faster Payments may result in mutuals facing additional costs due to potential for payment fraud in the system.

At the same time, the introduction of Open Finance also has the potential to lower mutuals' regulatory costs. Access to more diverse, higher quality and more standardised data could reduce the costs of regulatory reporting and therefore have a positive impact on the mutuals' profitability.

In summary, regulatory requirements may create additional costs for mutuals via requirements to invest in Open Finance or by exposing them to payment fraud in Faster Payments. But there may also be savings from improved efficiency of regulatory reporting.

Key factors

O. The extent to which mutuals are required to invest in Open Finance

The regulatory framework for Open Finance is still being deliberated by the FCA, and therefore, the full extent of regulation on mutuals are uncertain. However, the FCA's current view is that the regulatory framework for Open Finance could have a "phased approach", starting as an extension of the regulatory framework applied to Open Banking to cover non-payment accounts and other banking products, before expanding to cover pensions, investments and insurance etc.

Delivering the implementation entity for Open Banking (the OBIE) in the UK has cost an estimated of more than £150m in the time period from its inception to 2020.⁵⁴ This is significantly higher than the £20m initially estimated by the Competition and Markets Authority when it was introduced.⁵⁵ This cost has been borne by the nine largest UK banks, known as CMA9.

The total cost of implementing Open Banking is significantly higher. While UK specific costs are not available, costs to the EU provide a sense of the total scale (while noting that the scope of PSD2 is different to the scope of Open Banking and therefore the two are not directly comparable). The European Commission estimates a total cost of Open Banking and API development of €2.2 billion in the EU.⁵⁶ ⁵⁷ According to the same report, the median cost of

⁵³ UK Finance, Annual fraud report 2023

⁵⁴ See <https://www.gov.uk/government/publications/open-banking-limited-independent-investigation-report>

⁵⁵ Paragraph 13.86 of the CMA's Final Report
<https://assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf>

⁵⁶ See figure 14 here: <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=SWD:2023:0231:FIN:EN:PDF>

⁵⁷ For small and medium Account Servicing Payment Service Providers (ASPSPs) the estimated value is EUR 0.43m, while for large ASPSPs is EUR 14,8m.

adoption of the PSD2 is estimated to be between EUR 50m and EUR 100m per financial institution, with 45% of the firms indicating that their budgets exceeded EUR 100m.

The FCA has implied that mandated development of Open Finance solutions (data sharing and APIs) is unlikely for two reasons. Firstly, the significant investment costs needed could disproportionately impact smaller firms and risk market exit – reducing competition and choice for consumers. Secondly, the FCA (and stakeholders) believe that Open Finance will be most effective if its development is driven by consumer propositions and commercial incentives, rather than through regulatory action. This means that mutuals are unlikely to be mandated to bear disproportional costs to comply with Open Finance regulation.

Qualitative assessment: Extent to which mutuals are required to invest in Open Finance

Level of uncertainty: low. The FCA has implied that significant investment is unlikely to be mandated.

Severity of potential impact: high. Evidence from Open Banking suggests that costs could be very high if mutuals were mandated to invest in Open Finance.

P. The extent to which mutuals are able to improve efficiency of regulatory reporting

Open Finance has the potential to give mutuals access to more diverse, higher quality and more standardised data on their customers which could in turn lead to efficiencies in regulatory reporting and compliance costs. The greater the efficiencies that Open Finance can provide, the greater the impact would be on mutuals. Similarly, Open Finance might provide benefits by improving efficiency in some back office processes.

Most mutuals are small organisations with relatively simple reporting and back office processes. As such, the scope for any improvements is likely to be fairly limited.

Qualitative assessment: Extent to which mutuals are able to improve efficiency of regulatory reporting

Level of uncertainty: low. Nature of mutuals' businesses means that there is limited scope for cost savings in regulatory reporting.

Severity of potential impact: low. Savings likely to be small.

4 Quantitative assessment of impacts

In this section we provide a quantitative analysis of Impact 1: Emergence of TPP solutions in the savings market. The objective of this analysis is to estimate the impact that increased switching of savings customer balances due to Open Finance enabled TPP tools may have on mutual prices and margins, and the wider market impacts in cash savings and mortgage markets.

4.1 Summary of the quantitative model

There are four main steps to the quantitative model.



1. Mutual organisations operate a range of different business models. We therefore consider the impact of Open Finance for different types of “representative mutuals”. We first develop a view of the mutual business models in the savings market today. We define six “representative mutuals” that capture the different types of business models, in terms of customer balances by type of savings product and average prices. The mutual business model options capture different types of balance sheets and different types of pricing models. This allows us to identify the customer balances that could be exposed to Open Finance. This is described in section 4.2.
2. We then develop a range of plausible scenarios for the level of Open Finance uptake, in terms of savings balances affected. We do this by combining data on the proportion of customers that are able to theoretically engage with Open Finance by age, the proportion of balances on standard rate products by age and different plausible levels of Open Finance take-up. This allows us to estimate the savings balances that may switch due to Open Finance. This is described in section 4.3.
3. Next we model market outcomes in equilibrium following the introduction of Open Finance. We estimate the balance composition by type of product for different types of mutuals and for the market as a whole in this equilibrium. We then estimate the impact that these balance movements would have on market prices and prices for mutual products. This is described in section 4.4.2. We discuss the strategic choices and impact on lending markets in section 4.4.4.
4. We finally consider the potential liquidity risk arising from automated switching services that may instantaneously “sweep” savings accounts and move balances to the best rates

on the market. We set out the balances potentially at risk from “sweeping” and the likely market outcomes. This is covered in section 4.5.

4.2 An illustrative view of the market today

4.2.1 Market

There are about £1.5 trillion of savings deposits held in a range of products in the UK savings market today.⁵⁸ The product range can be grouped into four high level categories:

- fixed term deposits;⁵⁹
- deposits on instant access introductory rate products;⁶⁰
- deposits on restricted access introductory rate products;⁶¹ and
- standard rate deposits.^{62,63}

For the purposes of modelling, we group ISA and non-ISA products together and use total balances and average interest rates across both types of products.

There is approximately £300bn of further customer deposits held in personal current accounts (PCAs). While PCAs are generally not interest-bearing, many consumers use PCAs for holding balances that could otherwise be deposited in a savings product.⁶⁴

⁵⁸ FCA Cash Savings Market Review 2023, p11

⁵⁹ Deposits that are unavailable to the depositor to access for a fixed period of time without penalties, usually earning a fixed rate of interest.

⁶⁰ Deposits in products offering immediate access to the customer's funds, at an introductory or promotional interest rate for a period of time (typically offered for 12 months), after which the introductory rate expires.

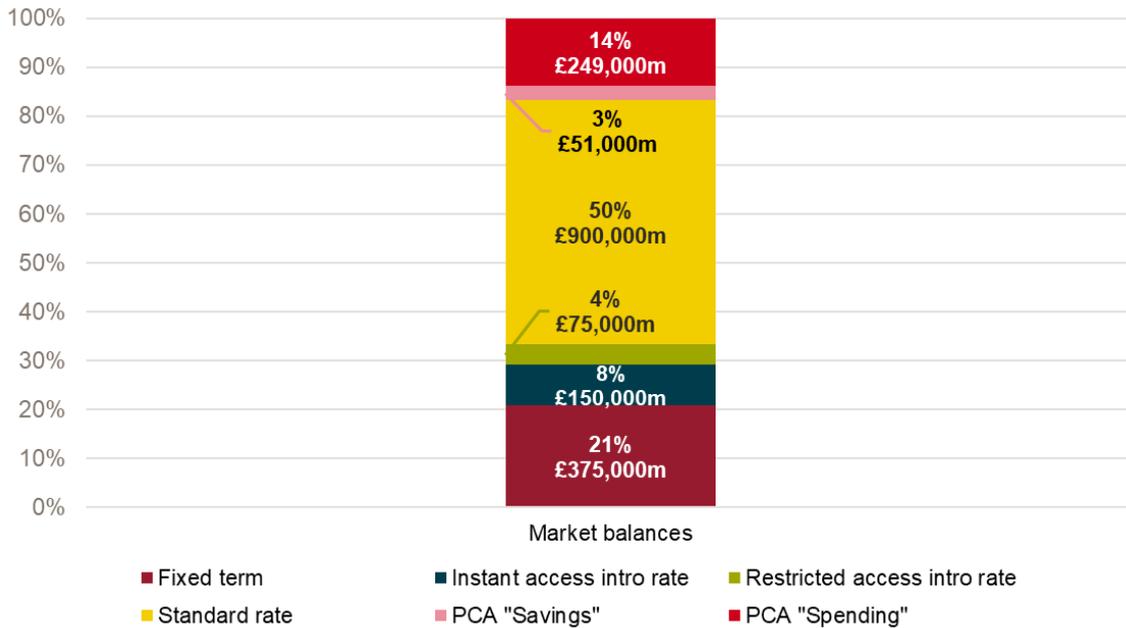
⁶¹ Deposits in products that impose restrictions or limitations on the frequency or method of accessing the funds, offered at an introductory or promotional interest rate for a period of time (typically offered for 12 months), after which the introductory rate expires. Customers withdrawal options may be limited to a maximum number of withdrawals per month, or they may need to provide notice before withdrawing funds.

⁶² Deposits in products that customer funds move to after the introductory rate product expires.

⁶³ We exclude Regular saver, Junior, Childrens, Business and Community products from our analysis.

⁶⁴ According to the FCA, 17% of people choose to use their current account for savings (FCA Cash Savings Market Review 2023, p12).

Figure 1 Balances distribution for the market



Source: Frontier analysis of data from the FCA and Frontier commercial insight

The data shows that £900bn or 50% of balances across the market are currently held in instant access standard rate products. A further £375bn (21%) of balances are held in fixed term deposits, £150bn (8%) are in instant access introductory products, and £75m (4%) are in restricted access introductory products. Finally, £300bn (17%) of balances are held in PCAs, with £249bn (14%) used for spending and £51bn (3%) used for saving.

We use data from Moneyfacts to develop a view of the average savings rates offered in the market. As we are looking to represent the weighted average rate paid across all market balances, rather than a simple average of products available on the market, we use data from CMA9 banks to represent the rates paid on the majority of deposits in the market.

Table 2 Average savings rates offered in the market

Product	Current Market rates
Fixed term products	4.8%
Instant access introductory rate	3.3%
Restricted access product introductory rate	3.7%
Standard rate	1.8%
Intro rate bonus	1.5%

Source: Frontier analysis of data collected from Moneyfacts, January 2024

4.2.2 Representative mutuals

Mutuals operate a variety of different business models. In order to capture the impact that Open Finance may have on different types of mutuals, we develop six types of “representative mutual”, based on:

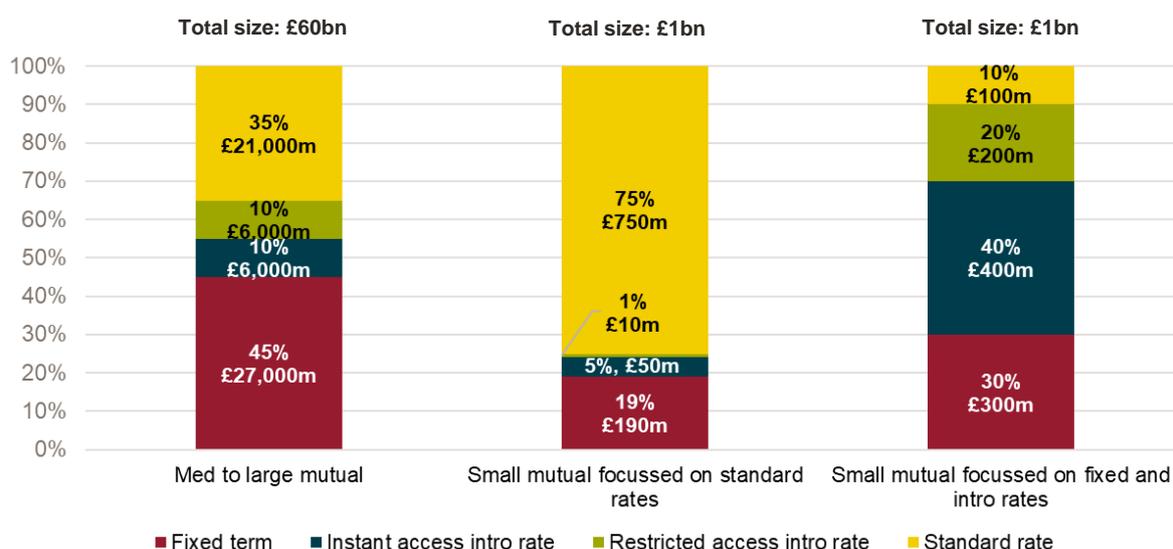
- three different types of balance distributions that we observe across mutuals; and
- two types of pricing models that we observe across mutuals.

Mutual balance sheet models

Data submitted to us by 7 building societies (which together cover 87% of total building society market by asset size) reveals three types of balance sheet composition.⁶⁵

5. Medium to large building societies hold close to half of their deposits in fixed term products. Deposits on standard rate products are the second largest group.
6. Small mutuals with a focus on standard rates are characterised by the majority (about 75%) of their savings book being held in standard rate products, with the remainder of balances largely in fixed term products.
7. Small mutuals with a focus on fixed and introductory rates hold about 40% of their deposits in introductory rate instant access products and 30% of their deposits in fixed term products. Only 10% of their deposits in instant access standard rate products.

Figure 2 Balance distribution for mutuals



Source: Frontier analysis of data submitted by BSA members. Data covers period Q1 2023 or the closest available date

⁶⁵ Due to data limitations, credit unions are not considered as a separate business model, but individual credit unions should be reasonably aligned to one of the representative mutuals included in this analysis.

Mutuals vary greatly by asset size, ranging from £270bn to less than £500m. We allocate a “size” to the representative mutuals to give a sense of scale for the Open Finance impacts modelled, but the conclusions for each type of business model hold for any mutual size.

The actual shape of balance sheet for each individual mutual will be slightly different, but based on the evidence available to us we consider these three models to be broadly representative of most building society balance sheets at a high level.

Mutual pricing models

We draw on data submitted to us by building societies and desk research of Moneyfacts data to develop two representative building society pricing models⁶⁶.

- **Model A: Bonus rate based pricing model** is characterised by offering an instant access product with a bonus rate for an introductory period (typically 12 months), followed by a lower standard rate after the introductory period. The current average instant access bonus rate offered by mutuals is approximately 1.5% above the standard rate.
- **Model B: Flat rate pricing model** does not offer an introductory bonus rate. The rate on instant access products is the same standard rate for all accounts of all tenures.

Table 3 Market and mutuals rates by pricing model

Product	Current market rates	Representative mutual current rate	
		Model A: Bonus rate based pricing model	Model B: Flat rate pricing model
Fixed term products	4.8%	3.7%	3.7%
Instant access introductory rate	3.3%	4.5%	3.0%
Standard rate	1.8%	3.0%	3.0%
Intro rate bonus	1.5%	1.5%	0.0%

Source: Frontier analysis of Moneyfacts data and data submitted by members, January 2024.

The three types of balance sheet distributions and two types of pricing models together yield six representative mutuals that we use to model impacts of Open Finance.

⁶⁶ We test the impact of alternative pricing strategies in Annex A.2.Implications for developing Open Finance

Figure 3 Representative mutuals

<i>Balance sheet model</i>			
<i>Pricing model</i>	1: Medium to large	2: Small mutual with focus on standard rates	3: Small mutual with focus on fixed and intro rates
<i>Model A: Bonus rate based pricing model</i>	Representative mutual 1A	Representative mutual 2A	Representative mutual 3A
<i>Model B: Flat rate based pricing model</i>	Representative mutual 1B	Representative mutual 2B	Representative mutual 3B

Source: Frontier analysis

4.2.3 Balances that could switch because of Open Finance

For the market and each of the representative mutual business models above, we estimate the value of balances that may switch because of Open Finance that would not otherwise be expected to switch.

Many customers already shop around for the best savings rate based on the type of product they need. According to the FCA, around 23% of savers had recently switched their savings account to get a better rate.⁶⁷ The FCA has also observed balances moving towards higher interest accounts in recent months. In the first half of 2023, easy access account balances decreased by £52 billion while fixed term or notice account balances increased by £38 billion across the nine largest banks, representing 4% and 3% of total balances respectively.

Across the market, the rates on fixed term deposits, instant access introductory rate products and on restricted access introductory rate products are significantly higher than rates on standard rate products. Customers holding their deposits in fixed term and introductory rate products have typically made an active choice to “optimise” their savings by either giving up a level of access to their funds (with fixed term or restricted access products) or by switching to a new savings product with a new or existing provider (for introductory rate products). We expect that Open Finance would not have a significant impact on the switching levels for savings balances held in these products by these customers, although Open Finance may change the way that currently optimising customers practically engage with their savings (such as using a TPP-enabled tool to find their savings product instead of a price comparison website).

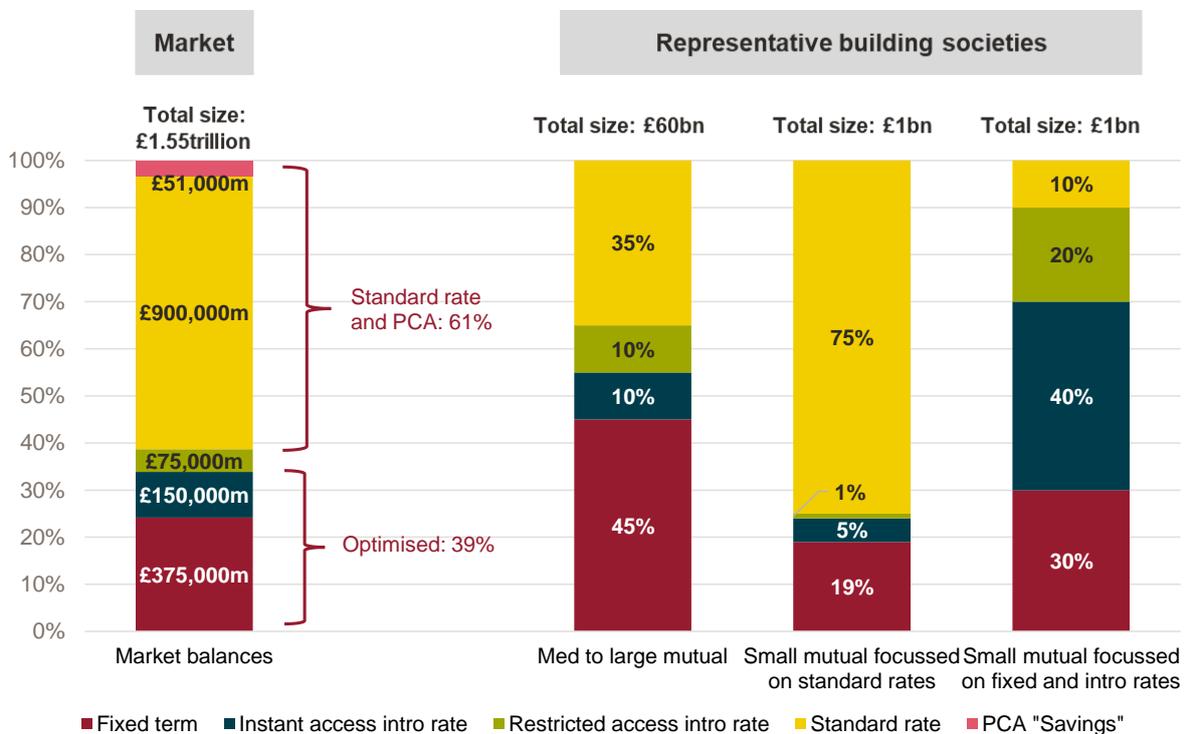
⁶⁷ FCA Cash Savings Market Review 2023, p5

Conversely, customers who hold their balances in instant access standard rate products may not have selected or reviewed their savings product. These customers' balances typically transition to a standard rate product after the introductory bonus ends, and these products are usually not on sale. Balances on standard rate products are likely to be exposed to TPPs seeking to switch balances to higher interest rates.

Savings balances held in PCAs are also not actively optimised and the majority do not earn interest.⁶⁸ A portion of PCA balances are therefore also exposed to TPPs seeking to switch balances through Open Finance.

Across the market, around 60% of all customer deposit balances are on standard rates or in PCAs for saving purposes and could therefore be impacted by Open Finance. The proportion of balances that are exposed to potential Open Finance impacts for mutuals therefore depends on the business model. For small mutuals that focus on standard rate products, up to 75% of balances could be affected by Open Finance. For medium to large mutuals, this percentage is about 35% and for small mutuals that focus on fixed and introductory rate products, this percentage is only 10%.

Figure 4 Proportion of all savings balances that could be impacted by Open Finance



Source: Frontier analysis of FCA data and data submitted by BSA members

Note: Of the £300,000m balances held in PCAs, 17% are assumed to be used for savings purposes (FCA Cash Savings Market Review 2023, p12) which amounts to £51,000m or 3% of total savings balances in the market.

⁶⁸ Balances held in PCAs for spending purposes are not exposed to Open Finance.

4.3 Open Finance take-up scenarios

Not all of the balances that could potentially be exposed to Open Finance impacts set out in section 4.2.3 above may actually switch. Any impact that Open Finance may have on businesses would depend on the extent to which Open Finance is adopted, and which customers adopt it. We use three types of data input to model the savings balances that may be affected by Open Finance, which are:

- the proportion of customers on standard products that are able to engage with Open Finance;
- the proportion of balances on standard rates; and
- the level of customer uptake of Open Finance.

4.3.1 Proportion of customers on standard products that are able to engage with Open Finance

As Open Finance gives access to customer data to largely digital TPPs, any new solutions or tools for customers can be expected to be primarily digital. Only customers that are able to use digital tools would be expected to be able to engage with Open Finance solutions.

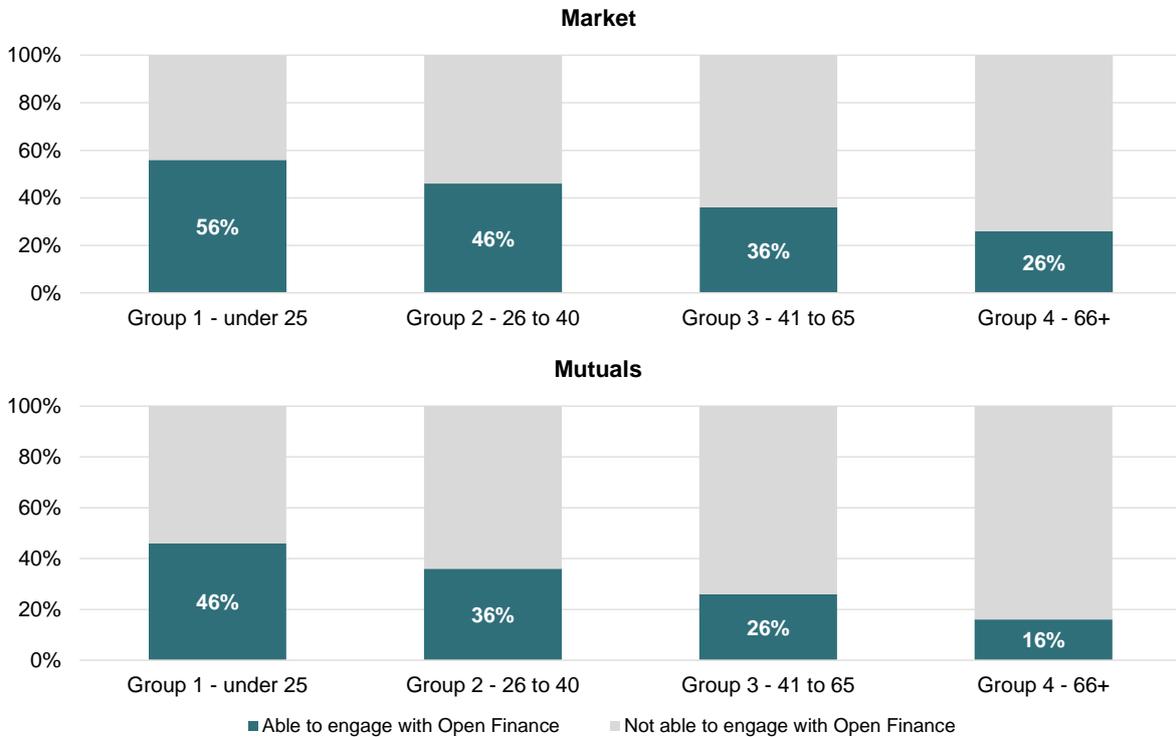
We construct two scenarios for the potential level of digital engagement of savings customers.

- **Low digital engagement:** in this scenario, we assume that only customers that currently use digital banking are able to use Open Finance.
- **High digital engagement:** in this scenario, we assume that everyone who owns a smartphone is able to use Open Finance.

Digital engagement differs depending on customer age. In the “low digital engagement scenario”, 56% to 26% of customers market wide would be able to engage with Open Finance. This proportion is lower for customers of mutual organisations where 46% to 16% of customers would be able to use Open Finance.

We expect that in a given age group the proportion of customers that own a smartphone is similar between mutual organisations and the market as a whole. The proportion of customers that would be able to use Open Finance in the “high digital engagement” scenario ranges from 99% in the younger age groups to 71% in the highest age group. This scenario shows the theoretical maximum proportion of customers that could engage with Open Finance.

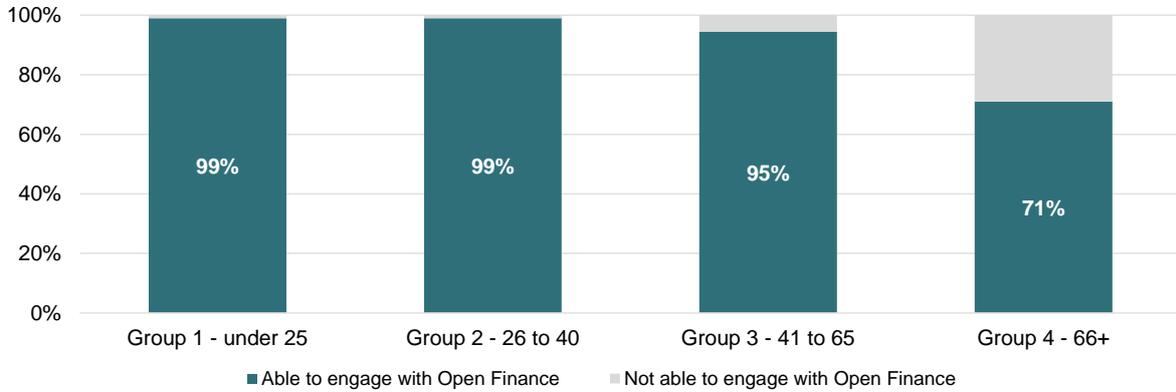
Figure 5 Proportion of customers on standard products that are able to engage with Open Finance – low engagement



Source: Frontier analysis of data submitted by BSA members and the BSA Digital attitudes survey (2024).

Note: Digital engagement for mutuals is based on the proportion of mutual customers that currently use digital banking. Data from the BSA Digital attitudes survey questions on digital engagement suggests that customers of large banks are 10% more likely to feel positive towards using digital solutions to manage their savings than customers of mutuals. We therefore apply a 10% uplift to mutual digital engagement figures to estimate the customer digital engagement at the market level.

Figure 6 Proportion of customers on standard products that are able to engage with Open Finance – high engagement



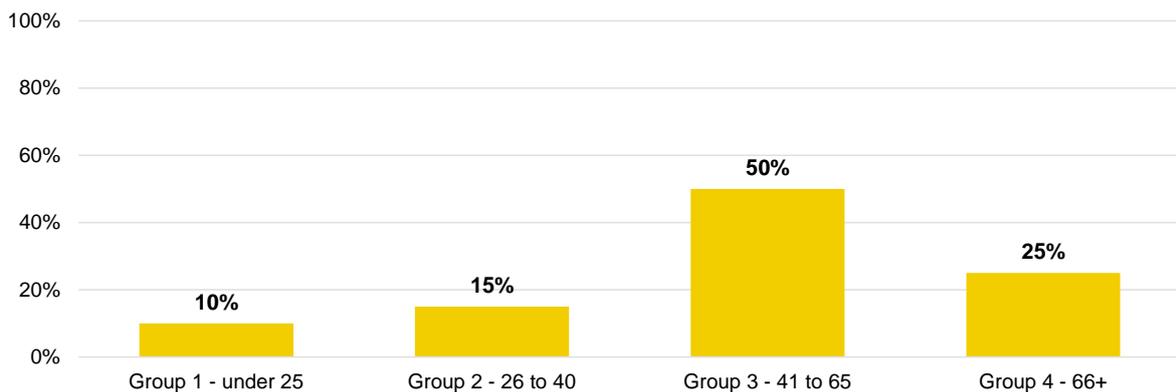
Source: Frontier analysis of Statista data.⁶⁹

Note: Data represents the share of smartphone users in the United Kingdom (2023) by age group.

4.3.2 Proportion of balances on standard rates

Customer deposit balances are not uniformly distributed by age. While young people are more likely to use digital channels than older customers, young people also have a lot less savings than older age groups. We use data from members to estimate the proportion of total standard rate savings balances held by each group.⁷⁰

Figure 7 Proportion of balances on standard rates by age



Source: Frontier analysis of data provided by BSA members.

⁶⁹ See: <https://www.statista.com/statistics/300402/smartphone-usage-in-the-uk-by-age/>

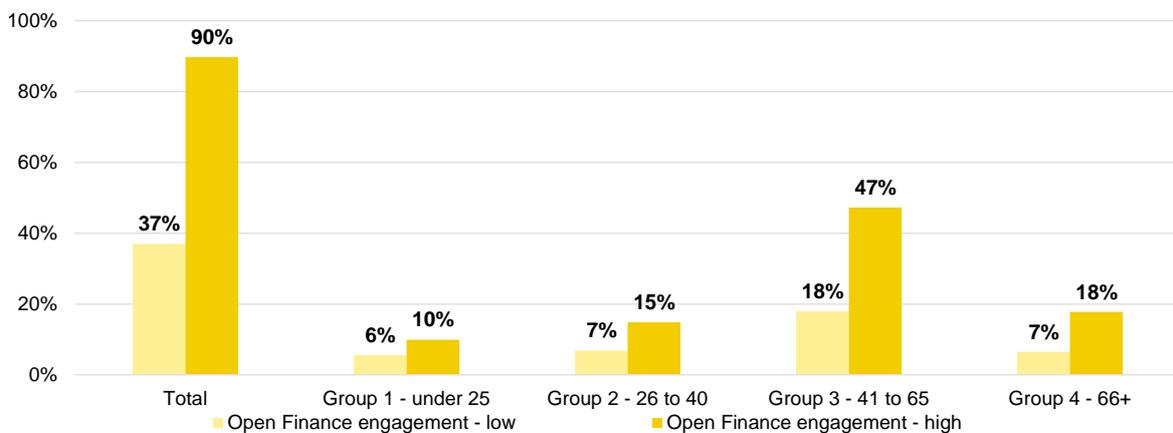
⁷⁰ We test the impact of varying the proportion of balances on standard rates by age in Annex A.3.

Combining the proportion of customers that are able to engage with Open Finance from section 4.3.1 and the standard rate product balance distribution by age gives the total proportion of savings balances that could be impacted by Open Finance.

Open Finance could impact a significant portion of standard rate balances, particularly in the high engagement scenario, as shown in the Figure below. For mutuals, 27% of standard rate balances could be impacted by Open Finance in the low engagement scenario, increasing to 90% in the high engagement scenario. The market as a whole has a higher proportion of balances that could be impacted by Open Finance, due to a relatively higher proportion of digitally engaged savers. In the low engagement scenario, 37% of standard rate balances in the market could be impacted by Open Finance, rising to 90% in the high engagement scenario.

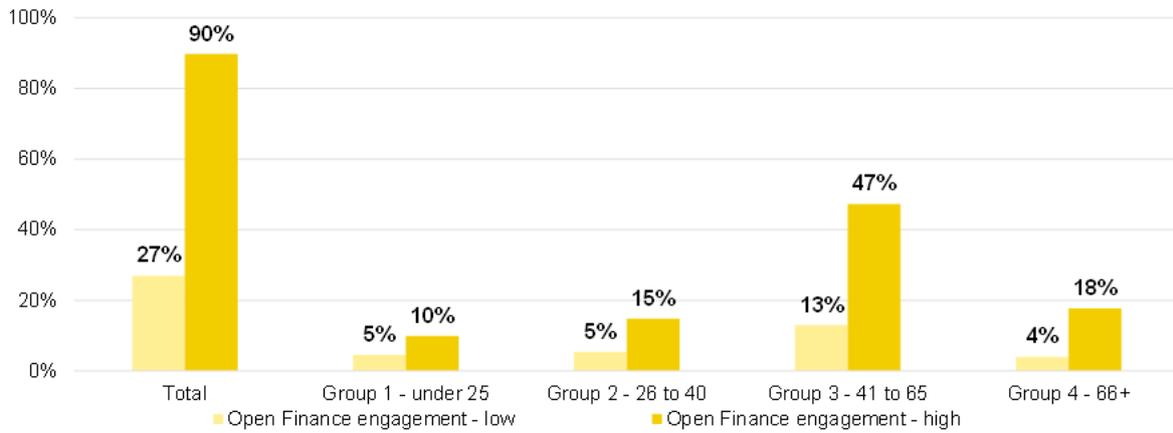
The age group between 41 to 65 years old holds the largest portion of balances at risk, both within mutuals and across the market. This is primarily because they hold the highest proportion of standard rate balances. Under 25s generally have the lowest proportion of standard balances at risk despite having the highest digital engagement, on account of a low share of standard rate balances.

Figure 8 Proportion of standard rate balances at risk – Market



Source: Frontier analysis

Figure 9 Proportion of standard rate balances at risk – Mutuals



Source: Frontier analysis

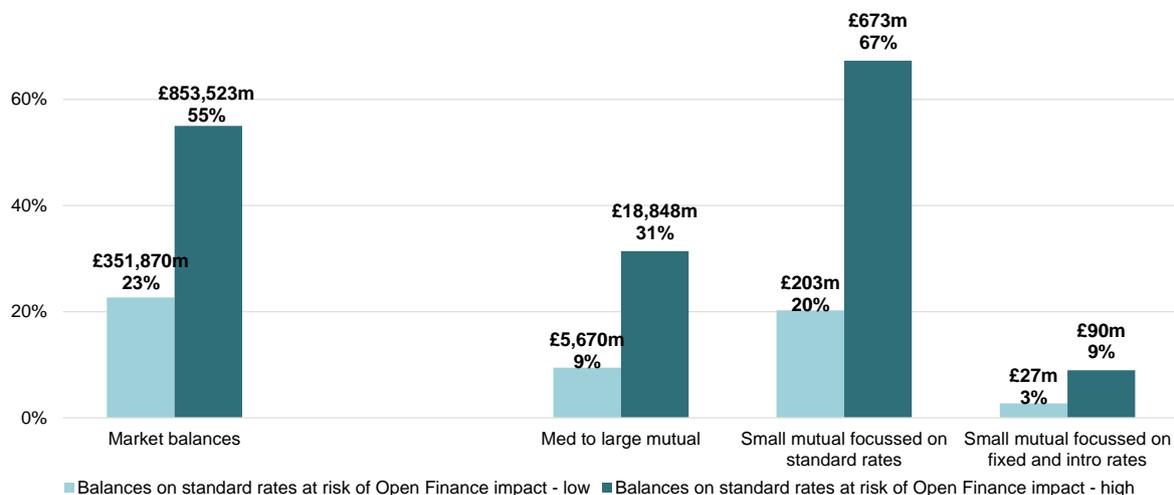
Applying the proportion of standard rate balances at risk to the standard rate balances held gives the proportion of balances that could be impacted by Open Finance.

Across the market, 25% of all savings balances could be at risk of switching due to Open Finance in the low digital engagement scenario and 60% of balances in the high engagement scenario, as shown in the Figure below.

Building society exposure to switching due to Open Finance will vary greatly depending on their business model:

- Small mutuals with high fixed and introductory rate balances have a small share of balances on standard rate products, and therefore only 3%-9% of total balances are exposed to switching from Open Finance.
- Medium to large mutuals could face between 9% and 31% of balances switching from Open Finance.
- Small mutuals with high standard rate balances could in theory face significant outflow of balances depending on how digitally engaged their customers are: from 20% to 67% of their total balances.

Figure 10 Proportion of all savings balances that could be impacted by Open Finance



Source: Frontier analysis

4.3.3 The proportion of balances that actually switch

Not all customer deposits that are theoretically exposed to switching due to Open Finance may actually switch. In reality, the proportion of customer balances that actually switch due to Open Finance solutions would be at some level below 100% of the theoretical maximum. There are three key factors that are likely to drive this:

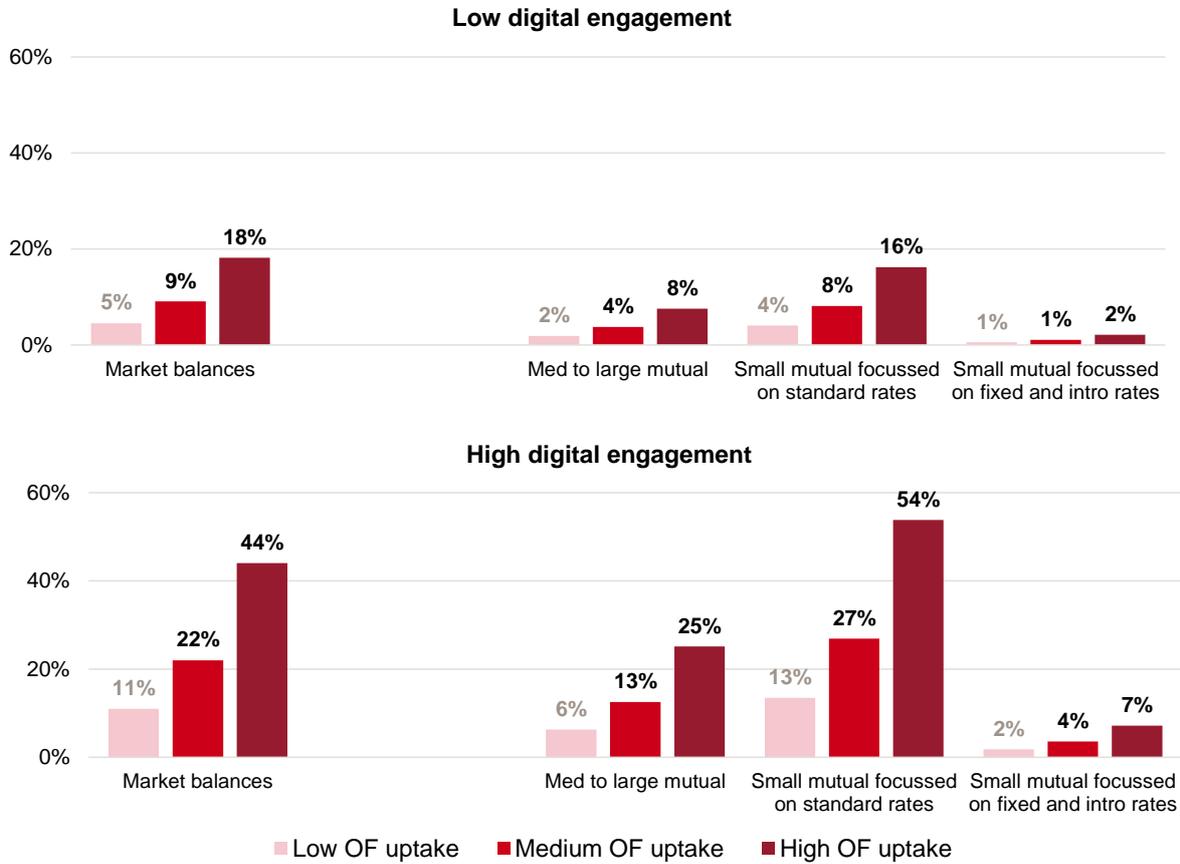
1. **Final scope of Open Finance regulation.** The types of services that TPPs are able to offer would have a significant impact on how much switching may increase in the market. If TPPs are only able to use “read” functionality, the proportion of balances that actually move is likely to be low. If they can “read” and “write”, or “read”, “write” and also provide a largely automated “account opening” service, the proportion of balances that switch would be much higher (see section 3.1.1).
2. **The quality of Open Finance propositions.** The better the range and quality of the Open Finance tools available to customers, the higher actual switching will be. This will be driven by both TPP capabilities (see section 3.1.1) and by regulation ensuring a smooth customer journey (see section 3.3).
3. **The extent to which customers wish to engage with Open Finance services.** Not all customers that are able to engage with Open Finance would choose to do so. Reasons such as reluctance to share their data or lack of interest in optimising their finances could lead to limited customer take-up.

All of these factors would have to be fully realised so that the majority of balances that could theoretically switch due to Open Finance would actually do so: Open Finance regulation would need to allow or “read”, “write” and also provide a largely automated “account opening” service; the solutions available on the market would have to be high quality and easy to use; and customers would need to be willing to share their data and engage with these products. We define this as the **“high” Open Finance uptake scenario** and assume that 80% of all balances that could theoretically switch do so. A scenario where a Big Tech company launches a successful Open Finance proposition may fall into this category.

If only some of these factors are fully realised, then a smaller proportion of balances would switch. We define this as the **“medium” Open Finance uptake scenarios** and assume that 40% of all balances that could theoretically switch to do.

Finally, if only one of these factors is fully realised, such as quality of TPP products being very high, but regulation only allowing “read” access and customers not being engaged with the services, the **uptake of Open Finance would be “low”**. This is modelled as 20% of all balances that could theoretically switch actually doing so.

Figure 11 Proportion of balances that actually switch due to Open Finance



Source: Frontier analysis

The low digital engagement scenario shows that, under medium Open Finance take-up, only 9% of overall balances in the market would switch due to Open Finance, and 18% would switch if Open Finance uptake was very high. Depending on mutual type, 2% to 16% of their balances would switch if Open Finance was very successful.

The high digital engagement scenario shows a larger range of possible effects. Between 22% and 44% of savings balances across the market would switch if Open Finance uptake was medium or high. Mutuals' balances that would switch if Open Finance uptake was medium to high vary depending on the composition of their balance sheet model:

- Small mutuals focussed on fixed and introductory rates have a low proportion of their balances held in standard rate products and only 4%-7% of their balances would switch.
- Medium to large mutuals could have between 13% and 25% of their balances switching.
- Small mutuals focussed on standard rates would have the largest proportion of balances switching due to Open Finance, between 27% and 54% of all balances.

4.4 Open Finance equilibrium

In section 4.3.3 above, we set out the proportion of balances that may switch away from standard rate and PCA products as a result of Open Finance in different scenarios of digital engagement and Open Finance uptake. As these customers look to optimise their savings, they would move their balances from standard and PCA products to fixed term products, instant access introductory rate products and restricted access introductory products depending on their needs. This switching may happen to a greater or a lesser extent, depending on the Open Finance uptake scenario.

As these switches take place across the market, in addition to the customers that shop around and switch their balances today, savings providers would react by adjusting their prices in order to attract the level of balances that they require. This process would be gradual over several years as customers begin to adopt Open Finance tools, and providers would be able to respond by gradually adjusting their prices. This gradual adjustment would continue until the market reaches a new equilibrium point.

This section describes the modelled adjustment to the new Open Finance equilibrium in the high digital engagement scenario for both balances and prices.⁷¹

4.4.1 Balances in the Open Finance equilibrium

We assume that, all else being equal, the overall savings balances in the market would be no different in the Open Finance equilibrium than they are today.⁷² The product composition of savings providers would be different, with increased balances on fixed rate, instant access introductory and restricted access introductory rate products, and fewer balances on instant access standard rate and PCA products.⁷³

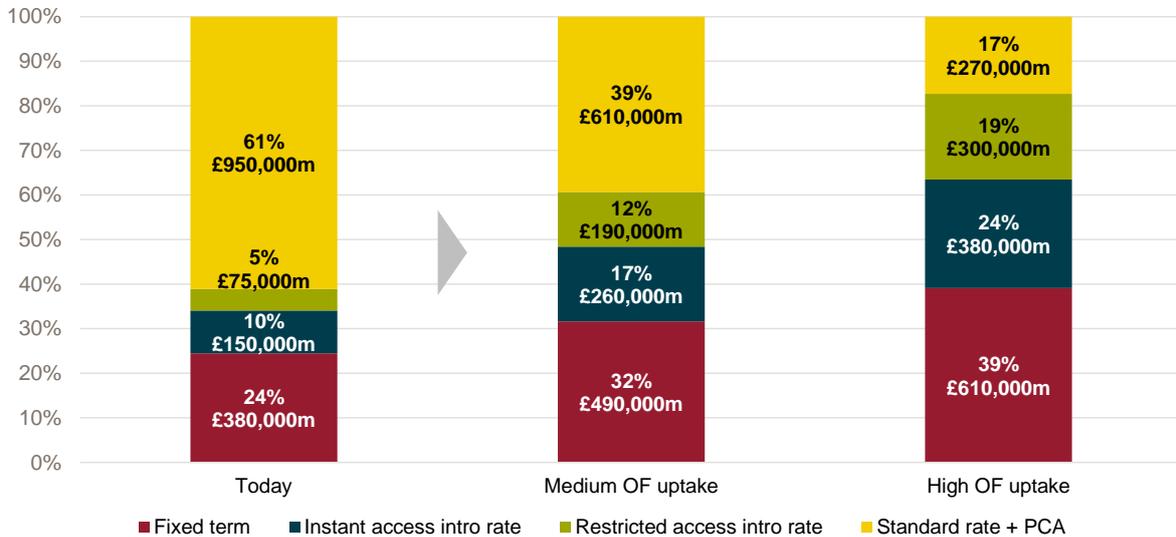
At the market level, we would expect a significant shift of balances away from standard rates in the new equilibrium. Standard rate balances and savings balances held in PCAs fall from 66% of balances to 43% and 19% in the medium and high Open Finance take-up scenarios respectively. The balances on introductory, restricted and fixed rate products would increase at the same time.

⁷¹ The high digital engagement scenario shows a more conservative range of possible results. Results from the low digital engagement scenario have the same directional impacts as the high digital engagement scenario, but with a lower magnitude.

⁷² There is no reason to believe that Open Finance would significantly alter the total size of the balance sheet for providers on average. Instead, prices will adjust in the new equilibrium to maintain total balances at the required level. Individual providers' balances may change due to their strategy or other factors in the market changing, but this would not be a result of Open Finance.

⁷³ For the purposes of modelling, we have assumed that customers on standard rate and PCA products would be evenly split between switching to fixed term, instant access introductory rate and restricted access introductory rate products. We test alternative switching behaviour in Annex A.1.

Figure 12 Distribution of savings balances at the market level

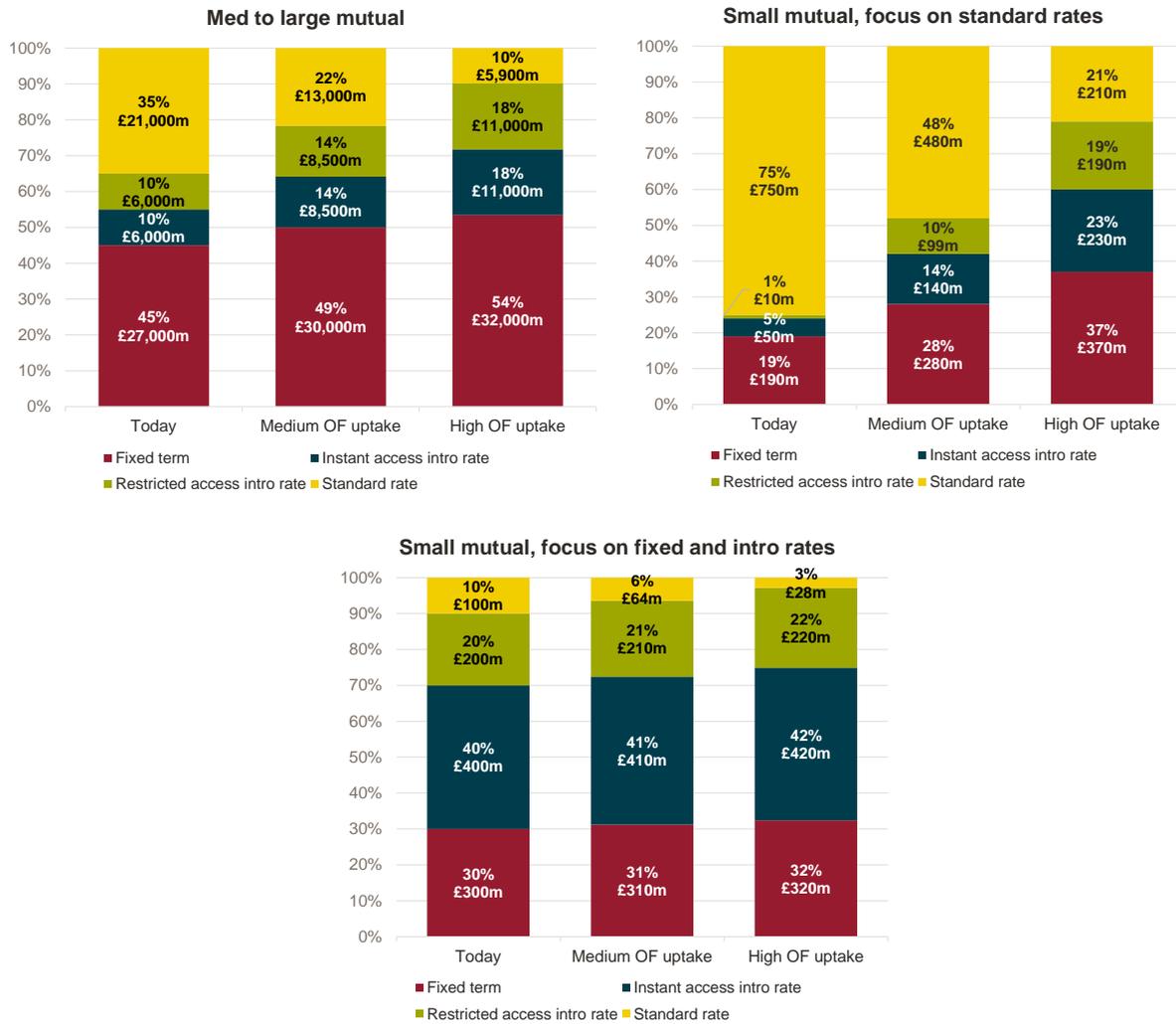


Source: Frontier analysis

After the introduction of Open Finance, mutuals would have less balances on standard rates than currently, but the impact would vary by business model.

- Small mutuals focussed on fixed and introductory rates experience a fall in standard rate balances from 10% of balances to 6% or 3% depending on Open Finance take-up. This means there is only a small increase in balances held in introductory, restricted and fixed products, and the distribution of balances appears largely unchanged.
- Medium to large mutuals have a larger fall in standard rate balances, from 35% to 22% or 6% depending on Open Finance take-up. This leads to a noticeable change in balances held on introductory, restricted and fixed products.
- Small mutuals focussed on standard rates have the largest fall in standard rate balances, from 75% to 48% or 21%. Given this movement of balances, there is a large increase in the proportion of balances held on introductory, restricted and fixed products.

Figure 13 Distribution of savings balances at the mutual level



Source: Frontier analysis

4.4.2 Prices in the Open Finance equilibrium

We use an economic model to estimate the impact that the changes in savings balances between different products due to Open Finance may have on prices across the market, keeping all else equal.⁷⁴ We then model mutuals' reaction to market prices.

⁷⁴ The economic model assumes that the market is competitive today, and continues to be so in the Open Finance equilibrium. An implication of this assumption is that at the market level, the net present value (NPV) of providing savings products would remain unchanged in the Open Finance equilibrium. We solve for market prices using this condition and the customer demand for savings products as set out in section 4.3.2 above. As balances move from standard rates to other products under Open Finance, retention on standard product balances decreases. This leads to a shorter duration

In reality, price levels in the market will be affected by a number of different factors, such as the interest rate environment, the strategic choices of market participants, the wider regulatory environment, customer behaviour and others. The results of this modelling give an indication of the direction and the relative scale of the impacts arising from Open Finance in isolation, keeping all other factors constant.

The price impacts at the **market level** are as follows.

- **The differential between introductory and standard rates decreases.** As standard rate balances are more likely to switch in the Open Finance equilibrium compared with today, providers are willing to invest less in introductory bonuses to attract balances (both in instant access and restricted access products). At the same time, providers are also willing to pay more for standard rate balances to increase retention. The greater the increase in switching due to Open Finance, the more the differential between introductory and standard rates would shrink.
- **The price for fixed term products remains constant.** There is an increase in customer demand for fixed term products as TPPs help customers to manage their savings. This could lead to a reduction in the rates offered on fixed term products. At the same time, as switching on standard rate savings products has increased, providers would value the certainty of fixed term deposits more than they currently do, leading to an increase in the rates that providers would be willing to offer for fixed term products. We assume that these two effects would broadly balance each other out.
- **The differential between restricted access and instant access products remains constant.** As with fixed rate products, we assume that the increase in customer demand for restricted products balances with the increased certainty of restricted deposits.

Mutuals make up about 20% of the savings market and are therefore price takers in the savings market. The price impacts for **mutuals** are as follows.

- **The differential between mutual introductory and standard rates decreases in proportion to the market change in the differential.** Mutuals retain their relative pricing position in the market.
- **The price for fixed term products remains constant.** In line with the rest of the market, customer demand for mutual fixed term products increases, but the value to mutuals from offering fixed term products also increases at the same time. We assume that the two effects balance each other out and the price of fixed term products remains unchanged.

over which the lower standard interest rate is applied for instant access products and thus higher total interest paid for instant access products. At the same time, interest paid on other product balances also increases as more balances sit on higher rate products. To counteract the potential rise in interest payments and maintain competitiveness, prices on instant access and restricted access products must adjust. These price adjustments are modelled to precisely offset each other and hold NPV constant.

Mutuals with a flat rate pricing model do not offer a bonus on introductory rates to attract new customers. These mutuals have therefore adopted a different pricing strategy to the market (where introductory bonuses are common) and we cannot predict how their strategy may evolve in response to new market prices.⁷⁵ As such, we have assumed that these mutuals continue with the same flat rate strategy, maintaining flat rates at pre-Open Finance levels. The effects of prices in the market and for each mutual is summarised in Tables 4 to 6 below. Market rates on introductory products (both instant and limited access) fall by 88 bps in the medium Open Finance uptake scenario and 109 bps in the high uptake scenario. Standard rates also increase slightly, by 11 – 24 bps depending on uptake. Fixed rates remain constant.

Table 4 Market prices in the Open Finance equilibrium

Product	Current rates	Medium Open Finance uptake scenario		High Open Finance uptake scenario	
		Open Finance equilibrium rates	Change in rates	Open Finance equilibrium rates	Change in rates
Fixed-term	4.81%	4.81%	0.00%	4.81%	0.00%
Instant access introductory rate	3.31%	2.43%	-0.88%	2.22%	-1.09%
Limited access introductory rate	3.66%	2.78%	-0.88%	2.57%	-1.09%
Instant access standard rate	1.81%	1.92%	0.11%	2.05%	0.24%

Source: Frontier analysis

Mutuals with a bonus rate pricing model adjust prices in line with the adjustment in the market, to maintain their relative pricing position, and mutuals with a flat rate pricing model do not change their pricing strategy.

⁷⁵ For example, these mutuals could decide to reduce costs by lowering rates in response to lower introductory rates in the market, or they could reward members and attract new balances by keeping rates high, or a middle ground. Alternatively, these mutuals could change to a bonus rate pricing model and realign to the market's pricing structure.

Table 5 Prices in the Open Finance equilibrium for mutuals with a bonus rate based pricing model

Product	Current rates	Medium Open Finance uptake scenario		High Open Finance uptake scenario	
		Open Finance equilibrium rates	Change in rates	Open Finance equilibrium rates	Change in rates
Fixed term	3.70%	3.70%	0.00%	3.70%	0.00%
Instant access introductory rate	4.50%	3.62%	-0.88%	3.41%	-1.09%
Limited access introductory rate	4.70%	3.82%	-0.88%	3.61%	-1.09%
Instant access standard rate	3.00%	3.11%	0.11%	3.24%	0.24%

Source: Frontier analysis

Table 6 Prices in the Open Finance equilibrium for mutuals with a flat rate based pricing model

Product	Current rates	Medium Open Finance uptake scenario		High Open Finance uptake scenario	
		OF equilibrium rates	Change in rates	OF equilibrium rates	Change in rates
Fixed term	3.70%	3.70%	0.00%	3.70%	0.00%
Instant access introductory rate	3.00%	3.00%	0.00%	3.00%	0.00%
Limited access introductory rate	4.70%	4.70%	0.00%	4.70%	0.00%
Instant access standard rate	3.00%	3.00%	0.00%	3.00%	0.00%

Source: Frontier analysis

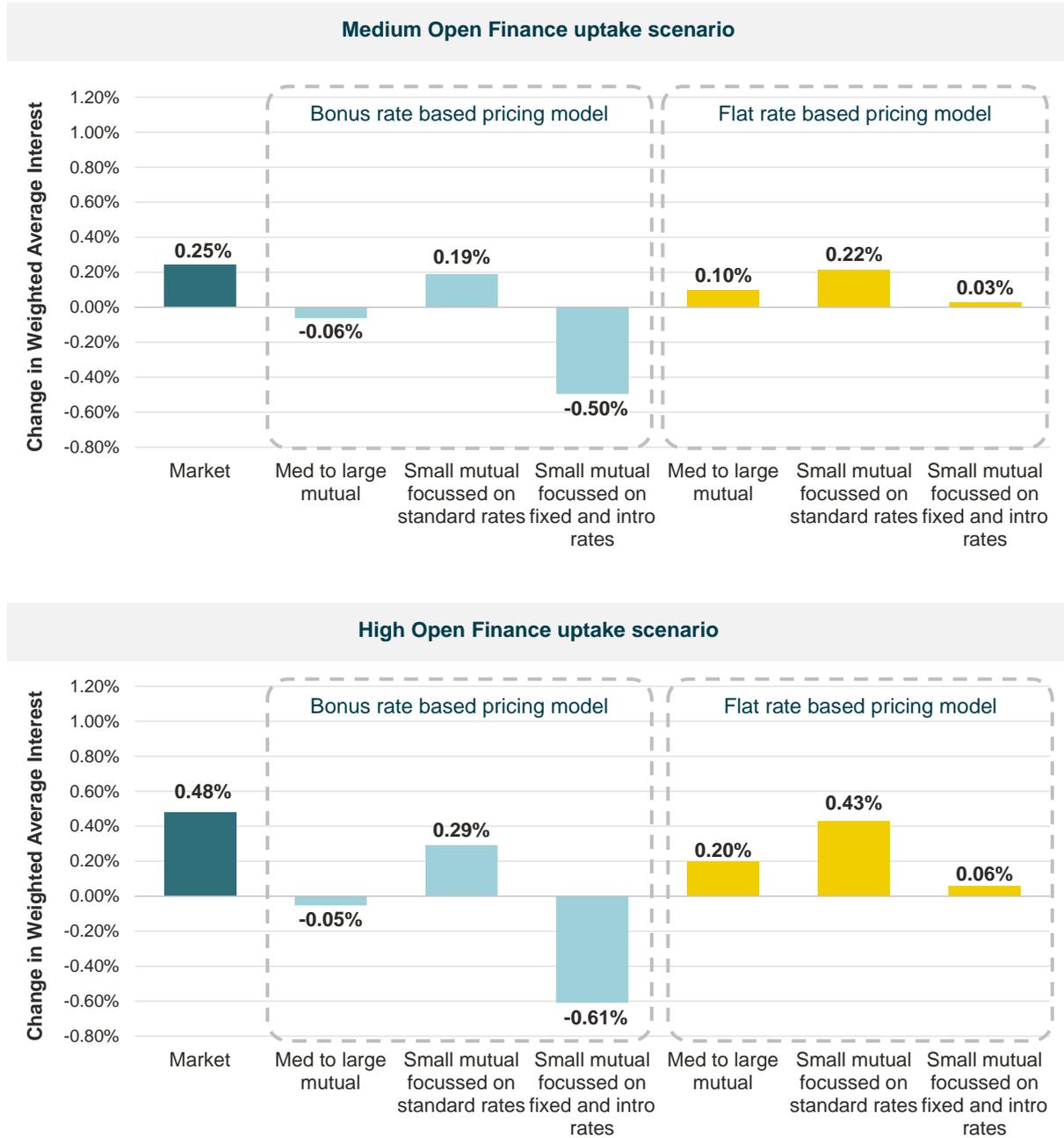
4.4.3 Combined balance and price impacts in the Open Finance equilibrium

The overall impacts of Open Finance on the market equilibrium would be a combination of the changes in the balance distribution between different products and the changes in the price levels of the different products.

- Balances effect:** As balances shift towards higher interest products (fixed term, restricted access and instant access introductory rate products), the average rate paid on savings would increase, all else being equal.
- Rates effect:** As introductory rates on instant and restricted access products reduce and standard rates increase (but by a smaller extent), the average rate paid on savings would decrease, all else being equal.

The overall impact on each market participants' average savings rate would depend on the relative effect of each of these two factors. This impact is different for providers with different business models.

Figure 14 Weighted average interest rate changes



Source: Frontier analysis

Note: Percentage point change in weighted average interest rate between the Open Finance equilibrium and current rates. Weighted average calculated across instant access, fixed and restricted products.

Across the market: As the majority of balances across the market as a whole are currently in standard rate and PCA products, the balances effect would dominate. The average savings rate across the market would increase by an estimated 25 – 48 bps.

Mutuals with a bonus rate based pricing model: these providers currently offer introductory and standard rates above those in the market and therefore the rates paid on these products would decrease (the price effect). The overall effect would depend on the balance sheet type.

- **Medium to large mutuals (representative mutual 1A).** As these mutuals have the minority of their book on standard rate products, the balance effect and the price effect would broadly balance out and the impact on their average savings rate would be close to 0.
- **Small mutuals focussed on standard rates (representative mutual 2A).** These mutuals have the majority of balances on standard rate products. The balance effect would be somewhat offset by the price effect, but this group would see an estimated increase in their average interest rate paid by 19 – 29 bps.
- **Small mutuals focussed on fixed and introductory rates (representative mutual 3A).** Only a small minority of these mutuals' balances are on standard rates. The price effect would therefore dominate and their average savings rate paid would decrease by an estimated 50 – 61 bps.

Mutuals with a flat rate pricing model: these mutuals currently do not have a differential between their introductory and standard rates. It follows that if these providers keep their current strategy of flat prices at above-market rates, there would be no price response to the increased switching of standard rate balances in the Open Finance equilibrium. For these mutuals, there would be no price effect and their average savings rate paid would be determined by the balance effect.⁷⁶

- **Medium to large mutuals (representative mutual 1B).** As these mutuals have the minority of their book on standard rate products, the balance effect would be limited and rates would be expected to increase by 10 – 20 bps due to the balances effect.
- **Small mutuals focussed on standard rates (representative mutual 2B).** These mutuals have the majority of balances on standard rate products and would experience a significant balance effect of 22 – 43 bps.
- **Small mutuals focussed on fixed and introductory rates (representative mutual 3B).** As only a small minority of these mutuals' balances are on standard rates, there would be no meaningful impact on savings rates in this group.

⁷⁶ In reality, these firms may respond to the balance effect by reducing the rates that they offer on introductory and standard products. However, our model is based on providers maximising their profits and it cannot predict the Open Finance equilibrium strategy of a provider that is not maximising its profits in the current market equilibrium (by setting current rates flat above the market prices).

4.4.4 Strategic choices for firms and impact on lending markets

Market wide impacts

As set out in section 4.4.3 above, the market savings rates may increase approximately 25 – 48 bps with Open Finance due to the increased concentration of balances in fixed rate and introductory rate products. This is equivalent to 8% - 15% of the current average net interest margin (NIM) for large retail UK banks of 3.2%.⁷⁷

Each bank would face a strategic choice in terms of how it responds to this increase and the reaction may depend on the bank's business model and options available to it. Some of the considerations include:

- The extent to which the bank is reliant on savings deposits for funding – the overall funding impact may be diluted for banks that have access to a broader range of funding options.
- The extent to which the bank is able to improve its hedging strategy given that in the Open Finance equilibrium more balances are in fixed term and restricted access products, increasing the overall deposit stability and increasing profitability as a result.
- The proportion of mortgage lending in the bank's assets.
- The extent to which a bank is willing to accept lower profits if it means being able to keep prices low in lending markets.

With savings deposits making up the majority of retail banks' customer liabilities and mortgage lending making up the majority of customer assets, we expect that at least some of the change in savings prices would be passed on to the mortgage market. The plausible range of this impact is from 0 up to 21 – 41 bps.⁷⁸ This is just over 8% of the current average mortgage rate of approximately 5% for a 2 year fixed rate mortgage.

Mutual impacts

Savings and mortgage lending is more closely linked on mutuals' balance sheets than they are for large retail banks. At the same time, being member-owned means that mutual organisations think differently about profitability than other businesses: profit is generally distributed to members rather than given to shareholders and can therefore be used to absorb profitability impacts in different parts of the business. Mutuals that would see a change in their profitability would effectively face a choice of one of the three options:

- changing the amount of member benefit they give to savings customers via the relatively higher instant access standard rates compared with the market;

⁷⁷ Speech by Andrew Bailey on 12 February 2024 – see <https://www.bankofengland.co.uk/speech/2024/february/andrew-bailey-lecture-at-loughborough-university>.

⁷⁸ Our analysis shows that on average for large UK retail banks mortgage lending makes up about 85% of total customer lending.

- changing the amount of member benefit they give to mortgage customers via relatively lower mortgage rates compared with the market; and
- the amount they give to members in other ways (e.g. investment in branches, digital tools, member cash benefit and others).

Representative mutuals 2A, 1B, 2B, 3B would see an increase in the average savings rate paid and a decrease in their margin of up to 3 – 43 bps depending on business model:

- These firms would likely have scope to pass the price increase through to the mortgage market where prices may increase up to 21 – 41 bps and maintain their level of profitability unchanged. This would keep the member benefit distributed in the same way that it is today.
- Mutuals that are currently distributing member benefit to savings customers via a flat savings pricing model could change their current pricing strategy and lower the rates paid on standard savings products, thus keeping mortgage prices and profitability the same. This would mean taking some member benefit away from savings customers and transferring it to mortgage customers (who would be getting lower rates than the market level).
- Alternatively, mutuals could accept higher savings rates and lower profitability and keep mortgage rates as they are. This would be equivalent to taking member benefit away from where it is currently being invested and giving some of it to mortgage customers

Mutuals that would see a decrease in the average savings rate paid and an increase in their profitability (representative mutuals 1A and 3A) would see their savings margin improve by 5 to 61 bps. They would have the opportunity to give more member benefit to customers and a choice of where to invest it.

- If these firms passed the decrease in savings rates through to mortgage prices and kept their profitability constant, they would be increasing the member benefit given to mortgage customers.
- Mutuals could offer higher savings rates than the competitive level predicted in the modelling and keep profitability unchanged. This would give the increased member benefit to savings customers.
- Finally, mutuals could accept an increase in profitability and distribute the profits to customers in another way.

4.5 Liquidity risk

One of the potential services that TPPs may offer under Open Finance may be an automatic “sweeping” of balances: a tool that instantaneously and regularly moves eligible balances to the best rate available on the market. From the point of view of a savings provider, this means that at any given point in time they could theoretically be exposed to a significant liquidity shock if another product on the market offered a better rate and a significant proportion of their balances were automatically and quickly swept away.

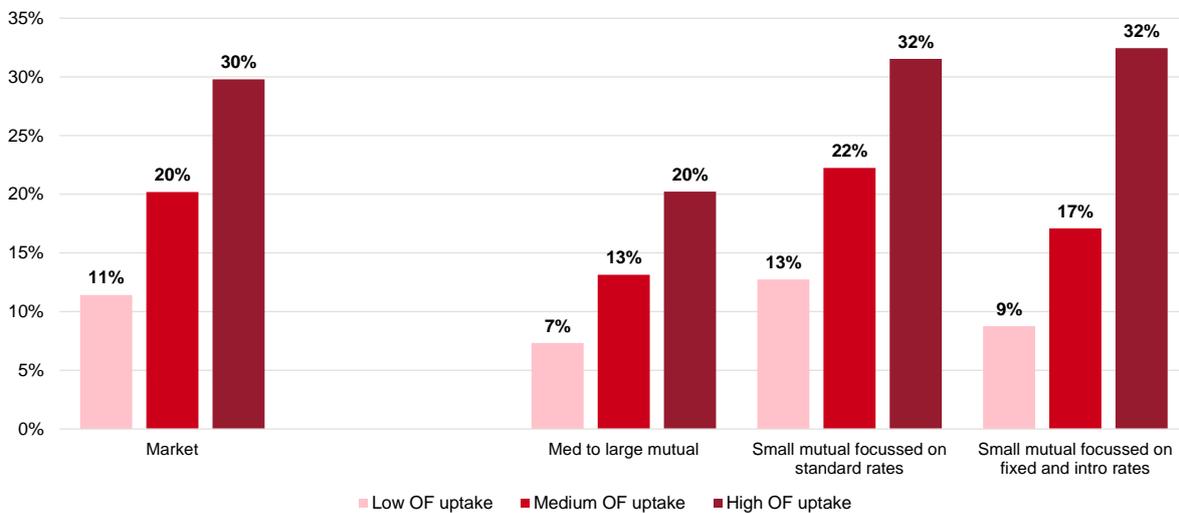
4.5.1 Balances theoretically exposed to automated sweeping

As more customers adopt these Open Finance services, a greater proportion of balances may be at risk of automatic sweeping at any given time. At the same time, a greater proportion of savings balances are likely to be held in fixed term and restricted access products as people seek to optimise their savings, as set out in section 4.4.1. This would reduce the proportion of balances that may be at risk of automatic sweeping.

Figure 15 below shows the combined impact of these two effects. The total balances that could theoretically be at risk of automated sweeping in the Open Finance equilibrium would be the total amount of balances on instant access products (introductory and standard rates) held by customers that are engaged with Open Finance. It shows that in the central scenario across the market about 20% of balances could be at risk of automated sweeping. For mutuals, this percentage is between 13% and 22% depending on the business model.

If Open Finance take-up was very high, these percentages may be about 32% for most provider types.

Figure 15 Balances on instant access products (introductory and standard rate) held by customers that are engaged with Open Finance



Source: Frontier analysis

4.5.2 Impact of sweeping services on market outcomes

The take-off of Open Finance would ultimately be driven by customer adoption. Customers would need to sign up to any new service that TPPs offer. Even if customer adoption of Open Finance is quick, the technology would necessarily be adopted gradually, rather than overnight. This means that any automated sweeping of savings balances, if it were to emerge, would do so gradually.

As providers observe the growth of balances that are automatically switched between providers, they would have an opportunity to respond through changes to products and pricing. We would expect two main types of provider response.

- Providers may react by changing how prices are managed on a day-to-day basis to avoid rate differentials that may trigger balance sweeping.
- Providers may react by introducing restrictions or penalties on the acceptance of and access to balances in order to reduce the potential for instantaneous automatic switching in the first place.

We describe further in section 5 how these changes may be implemented and how Open Finance could be developed to reduce the potential for increased liquidity risk.

The increase in liquidity risk for mutuals (if adoption of automatic switching was sufficiently high) will depend on the implementation of these safeguards by firms and regulators. If these safeguards are fully effective, then there may not be an increase in liquidity risk, although there may be other consequences, such as a reduction in the availability of instant access products. In this case, we would expect the market to develop towards the equilibrium outcomes that we have modelled above.

If liquidity risk cannot be managed through such safeguards, then we would expect to see an impact on the pricing of instant access products. Providers may offer lower interest rates on instant access balances that are subject to automatic sweeping as they would not be able to rely on the stability of these deposits on a day-to-day basis. The equilibrium outcomes we have modelled above would need to be adjusted to reflect this effect.

We have not estimated the scale of this effect on market outcomes as we assume that sufficient safeguards can be put in place to prevent this outcome as we describe in section 5.

5 Conclusions

In this section we summarise the impacts that Open Finance may have on mutual organisation business models and the market as a whole and discuss the implications for developing Open Finance further.

5.1 Summary of impacts from Open Finance

The main market impact as a result of the introduction of Open Finance and Smart Data in the UK would be the emergence of third-party provider (TPP) solutions in the savings market. This may lead to a new equilibrium distribution of balances and price levels and to increased liquidity risk in the market.

New market equilibrium

Open Finance enabled TPP solutions have the potential to increase the switching of customer balances that are currently held on standard rate instant access products towards higher interest rate products, which may be fixed term or restricted access products. This switching may lead to interest rate changes and an increase in the stability of deposits for financial institutions. Cash savings providers may also have to adjust their balance sheet management and pricing strategies in response to this increased switching.

These impacts are likely to be gradual as customers take time to adopt TPP products. Cash savings providers would therefore have the opportunity to respond and adjust their business models over time as the market moves towards a new equilibrium. The changes to business models required to compete in the new equilibrium are likely to be less significant than some of the recent rapid market changes that firms have responded to, such as the Covid-19 pandemic or the interest rate rises of the last two years.

The extent to which mutuals may be exposed to increased switching that results from Open Finance depends on their business model today. Based on our modelling of scenarios of Open Finance uptake, the negative impacts on mutuals' net interest margins would be smaller than for the rest of the market and may even be positive for some types of business model.

Adapting to a savings market with more frequent price and balance movements may be relatively more challenging for mutuals than for larger firms. The changing market dynamics are likely to require new investment to increase the speed of balance sheet management. Mutuals, in particularly smaller firms, may lack the resources and capability to adjust to these changes compared with the rest of the market.

Liquidity risk from automated switching

If Open Finance was to enable the automatic transfer of deposits by a TPP on behalf of customers (e.g. "write" functionality), this could lead to the development of automated switching services that "sweep" balances to the best rate available on the market at any given

time. This could potentially expose savings providers to the prospect of a significant liquidity shock if another product on the market offered a better rate and a significant proportion of their balances were automatically and quickly swept away.

Firms may introduce product restrictions to prevent large-scale automatic switching triggered by TPPs (e.g. withdrawal notice periods). This would reduce the availability of instant access products. If such restrictions are not effective, then interest rates offered for instant access products may be reduced to reflect the increased liquidity risk relative to fixed term products. This highlights an important trade-off that needs to be fully considered and approached strategically by both regulators and the industry.

Cost of implementing Open Finance

The requirements on firms to support Open Finance need to be developed, and therefore the extent of such requirements is uncertain. However, evidence from Open Banking suggests that costs of introducing Open Finance could be significant.

The cost burden of implementing Open Finance regulation has the potential to be much more significant for mutual organisations than for other businesses due to their small size and relatively lower levels of digitisation.

5.2 Implications for developing Open Finance

Safeguarding against liquidity shocks

If TPPs are enabled with “write” functionality under Open Finance regulation then they could develop tools that automatically switch customer balances towards better interest rates available on the market. This could lead to TPPs continuously searching the market for the best interest rates and automatically moving all eligible balances from customer accounts towards the market leading product. The movement could happen quickly with the TPP moving a high volume of balances across the market as soon as the price difference is identified.

For any individual savings provider, this could result in a large proportion of their book withdrawing funds simultaneously: a request they may not be able to meet if the amount of balances requesting to move is greater than the liquid funds that the firm holds. Conversely, if the savings rates available in the market are volatile, a provider could suddenly find it is offering a market leading rate, and rapidly receive larger inflows than it had intended.

Safeguarding options would need to be developed to slow down the potential flow of funds under Open Finance and ensure that the funds requesting to leave at any given point do not exceed the liquidity reserves available to a savings provider. A slower movement of funds would enable the provider to respond to the anticipated outflow of funds by acquiring new balances in the market or adjusting their prices to close the price differential between its product and the market leading rate to retain some of the funds that the TPP was looking to withdraw.

There are a number of different options for safeguarding against this risk and slowing the flow of funds in the market. We set out some options and how they might work at a high level below. We have not considered how each of these options would be introduced into specific regulation.

Limits on the maximum value of transactions per TPP

Introducing a cap on the amount of balances that a TPP can withdraw from any savings provider could effectively limit any providers' exposure to liquidity risk. The cap could be based on the value of balances withdrawn per customer or on the total withdrawals per provider. These caps may relate to various timeframes, for example, a daily, weekly and monthly maximum withdrawal amount. In response to a price differential, a TPP would then gradually switch its customers balances over several days, such that the pattern of withdrawals is similar to that under 'manual' switching today.

If such caps are in place, then savings providers could ensure that their reserves are aligned with their exposure to potential maximum TPP withdrawals alongside 'manual' withdrawals as in the market today. In the event of substantial TPP withdrawals, the cap would give time for savings providers to adjust pricing and better manage their liquidity.

The transaction limit for TPPs would need to be carefully considered. If the cap was set too low it may reduce the scope of benefits from switching to consumers and limit the impact of Open Finance.

TPPs to require agreement before transfer

TPPs could also be required to provide financial institutions with a schedule of the transactions that they plan to make over the following day, week or month, before the TPP can proceed with the transaction. This would give firms the ability to respond to the anticipated withdrawals by raising additional balances from the market or by adjusting their price to limit the anticipated withdrawals.

Obligations on TPPs to manage liquidity

The responsibility of ensuring that there are no liquidity shocks to savings providers arising from automated switching could also be passed on to TPPs as part of the requirements of holding an Open Finance TPP 'licence'. Under a "platform" model where a TPP aggregates the savings offers from multiple providers, it would have full control of movements between products and could manage liquidity independently. An alternative would be for the TPP to have pre-set limits in place with providers.

Unilateral control with information sharing

Open Finance regulation could also give financial institutions control over how they engage with TPP transfers based on information about incoming TPP-enabled transactions. Savings providers could set their own strategy over how they wish to respond when a TPP requests to

make a deposit, based on information encoded in the transfer request. This could include an indication of whether the transaction is automated or customer approved or initiated and allow savings providers to limit deposit inflows to much more similar levels to switching today.

Data sharing rules around Open Finance would need to be designed to ensure that the information that firms require to make decisions about whether or not to accept the transfer is shared in advance of any transaction, and give firms the permission to reject transfers.

Customer considerations

There may also be further customer considerations that would affect the market as a whole:

- In this paper, we model the average impact on savings prices, but there are likely to be winners and losers among different customer groups. Open Finance may further contribute to digital exclusion as Open Finance tools may allow digitally enabled customers to find better savings rates than today at the expense of lower savings rates for those who do not use digital tools.
- Open Finance may lead to greater restrictions on access to customers' savings balances in return for higher interest rates. This may benefit some customers, but could also lead to situations where customers are not able to access their funds when they need it in unexpected circumstances.
- The number of instant access products available on the market may reduce, potentially leading to financial exclusion.⁷⁹

The FCA has proposed to explore the scope and opportunities for Open Banking capabilities to help customers make their money work harder in the cash savings market.⁸⁰ This work would provide valuable insight into the overall costs and benefits from introducing Open Finance in the savings market to supplement the analysis presented in this paper.

Practical considerations

In this report, we have not considered the practicalities of implementing Open Finance, such as potentially connecting all savings providers to a real-time payment scheme like Faster Payments. There are likely to be a number of technical considerations that need to be addressed for this to be possible.

Further considerations for mutuals

If UK regulators and policy makers decide to move forward with Open Finance, then it should be developed being mindful of the potential scale and proportionality of costs that could arise for mutual organisations as they look to adapt their business systems and strategies to Open

⁷⁹ Firms would still need to take into account their obligations under the Financial Conduct Authority's new Consumer Duty when changing the provision of accounts.

⁸⁰ FCA Cash Savings Market Review 2023, p44

Finance. Regulators should ensure that the costs of complying with Open Finance regulation are not excessive relative to the size of mutuals.

While the market evolution towards a new Open Finance equilibrium would be gradual, giving mutuals time to adjust their business strategies and plan for anticipated expenditure, they may be affected significantly more than other businesses due to their small size and lower levels of digitisation. Building societies are also less able than banks to raise funds from alternative sources such as wholesale funding markets, as they are required by law to raise the majority of their funds from saving members.⁸¹

In addition, building society-specific regulation restricts the proportion of a building society's balance sheet that can be funded by fixed rate products. Regulators should ensure that this regulation is flexible enough for building societies to respond to potential shifts in the structure of funding markets brought about by Open Finance.⁸²

⁸¹ See: <https://commonslibrary.parliament.uk/research-briefings/cbp-9922/#:~:text=In%20accordance%20with%20this%20principal,like%20bonds%2C%20called%20wholesale%20funds.>

⁸² For example, the Prudential Regulatory Authority's Supervisory Statement 20/15 "Supervising building societies' treasury and lending activities" sets limits on the proportion of a building society's balance sheet that can be funded by fixed rate products. See: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2015/ss2015.pdf>.

Annex A Sensitivity analysis

In this section, we report the results of three types of sensitivity analysis of our modelling. This confirms that the results of the quantitative modelling are not driven by any modelling assumptions. We test three types of sensitivities:

- variation in the type of product that customer balances switch to in the Open Finance equilibrium;
- variation in the relative pricing strategies between mutuals and the rest of the market; and
- variation in the distribution of standard rate product balances held, by age.

We present the results of the sensitivity analysis for the “high” digital engagement and the “high” Open Finance take-up scenarios only, as these scenarios have the largest final impacts in our modelling.⁸³

A.1 Variation in type of product that customer balances switch to from instant access standard rate products

In Section 4.4 we model the switching of customer balances in the Open Finance equilibrium. As these customers look to optimise their savings, they would move their balances from standard and PCA products to fixed term products, instant access introductory rate products, and restricted access introductory products depending on their needs.

For the purposes of modelling, we have assumed that customers on standard rate and PCA products would be evenly split between switching to fixed term, instant access introductory rate, and restricted access introductory rate products. We test the sensitivity of results to this assumption.

We compare the baseline results to the results under the alternative assumption that the majority (60%) of switching balances move to one product, while the remaining switching balances are split equally (20%) between the other two products. We test this for fixed term products, instant access introductory rate products and restricted access introductory products.

Table 7 shows that average rates in the Open Finance equilibrium change according to the relative rates between fixed, introductory and restricted products, and where the majority of balances move. For example, a larger relative movement to fixed products increases the

⁸³ Other take-up and engagement scenarios were tested, but are not reported. These scenarios show the same directional impacts as the high Open Finance take-up and high digital engagement sensitivities, but with lower magnitudes. One exception (as discussed later in this section) is the effect of altering the distribution of standard rate balances across age groups, which has more pronounced effects in the low digital engagement case.

average rate for the market as market fixed rates are relatively high, but decreases the average rate for mutuals as mutual fixed rates are relatively low.⁸⁴

If more balances move into restricted products, this leads to a lower average rate for the market and a mixed effects for mutuals. Mutuals with a flat rate pricing model see an increase in average rates as restricted products have the highest rates and there are no countering rate adjustments. Mutuals with a bonus rate pricing model see limited changes in average rates since rates on introductory and restricted products adjust downwards to a greater degree than the baseline.

Lastly, if more balances move into introductory products there is a lower average rate for the market and mutuals. This is because introductory rates are low relative to the rates on fixed and restricted access products.

Table 7 Impact of a change in switching balances movements on prices

Market/Mutuals	Baseline	Mostly fixed	Mostly restricted	Mostly Instant Access
Market	0.48%	0.76%	0.36%	0.29%
Bonus Rate Pricing Model				
Medium to large	-0.05%	-0.03%	0.30%	-0.07%
Small mutuals with focus on standard rates	0.29%	0.32%	0.30%	0.25%
Small mutuals with focus on fixed and intro rates	-0.61%	-0.59%	-0.61%	-0.62%
Flat Rate Pricing Model				
Medium to large	0.20%	0.19%	0.29%	0.12%
Small mutuals with focus on standard rates	0.43%	0.41%	0.62%	0.26%
Small mutuals with focus on fixed and intro rates	0.06%	0.05%	0.08%	0.03%

Source: Frontier analysis

Note: Change in weighted average interest rate (% point change). Each 'Mostly X' scenario assumes that 60% of switching balances move to product X, while the remaining switching balances move to the other two products equally (20% each).

⁸⁴ There is a smaller, secondary effect on introductory rates. With more balances moving to fixed, there are relatively fewer balances moving into instant access introductory products. This creates less downwards pricing pressure and introductory and restricted access rates are marginally higher than the baseline scenario for the market and mutuals with bonus rate pricing models.

These results show that the product to which customer balances would move to in the Open Finance equilibrium has an impact on the weighted average interest rate for mutuals and for the market, but the direction and the relative size of the impacts between different types of firms remains similar to the baseline scenario.

A.2 Relative pricing strategies of mutuals and the rest of the market

In Section 4.2 we present an illustrative view of the relative pricing positions of mutuals and the rest of the market today. These positions represent a snapshot view of the market and are likely to change over time. We therefore test the sensitivity of the modelling results to different relative pricing positions of mutuals compared to the market. In particular, we test the following three scenarios:

1. average mutual rate for fixed term products is 100 bps higher than the average market rate;
2. average mutual differential between introductory and standard rates is 150 bps to 200 bps greater than the market; and
3. average mutual differential between introductory and standard rates is 150 bps to 200 bps smaller than the market.

Table 8 shows the modelling results in these scenarios. As in section A.2 above, the results of the sensitivity analysis are broadly consistent with the baseline, but the size of the impacts on the weighted average price for mutuals and the market is different under the different scenarios.

If mutuals offer higher fixed term rates than the market, then average savings interest rates for mutuals would be higher in the Open Banking equilibrium than in the baseline.

If the differential between introductory and standard rates is different than the baseline, for mutuals with a bonus rate pricing model the differential between introductory and standard rates decreases in proportion to the market's change in differential.⁸⁵ This means that if these mutuals offer a larger differential to begin with, then there is a greater reduction in rates for mutuals in the Open Finance equilibrium. There is a smaller reduction in rates if these mutuals have a smaller differential than the market to begin with. There is no change in the prices for mutuals with a flat rate based pricing model compared to the baseline as there is no pricing differential between their introductory and standard rates in the first place.

⁸⁵ As discussed in section 4.4.2.

Table 8 Impact of a change in pricing strategies on prices

Market/Mutuals	Baseline	Mutuals ahead on fixed	Mutuals bigger differential	Mutuals smaller differential
Market	0.48%	0.48%	0.48%	0.48%
Bonus Rate Pricing Model				
Medium to large mutuals	-0.05%	0.13%	-0.07%	-0.03%
Small mutuals with focus on standard rates	0.29%	0.67%	0.38%	0.20%
Small mutuals with focus on fixed and intro rates	-0.61%	-0.56%	-0.81%	-0.40%
Flat Rate Pricing Model				
Medium to large mutuals	0.20%	0.38%	0.20%	0.20%
Small mutuals with focus on standard rates	0.43%	0.81%	0.43%	0.43%
Small mutuals with focus on fixed and intro rates	0.06%	0.11%	0.06%	0.06%

Source: Frontier analysis

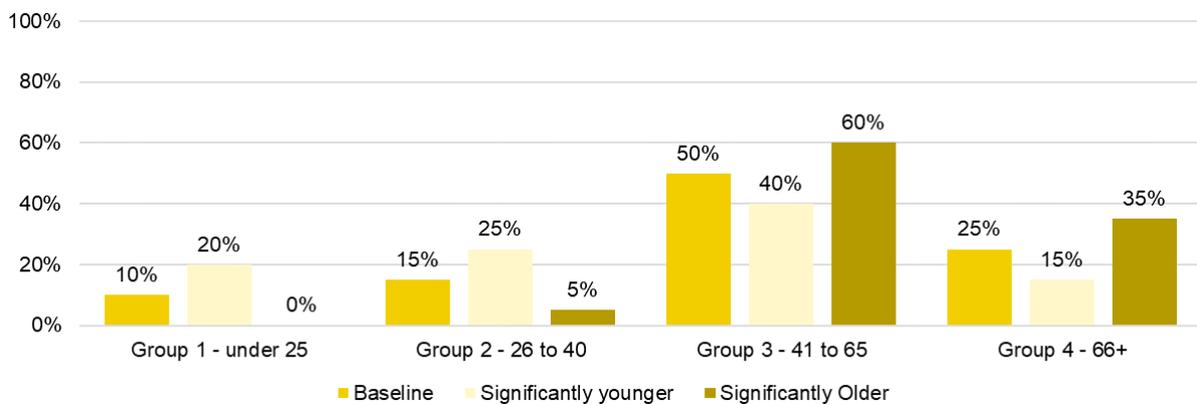
Note: Change in weighted average interest rate (% point change).

A.3 Distribution of balances on standard rates across age groups

In this section we test different scenarios for the distribution of balances on standard rates across age groups which is discussed in section 4.3.2. Exact data on this distribution was not readily available from mutuals who contributed to this work and the distribution was therefore derived from mutual data by applying a set of assumptions.

We consider two scenarios reflecting a generally younger and generally older distribution of standard rate balances, as shown in Figure 16 below.

Figure 16 Proportion of balances on standard rates by age - scenarios



Source: Frontier Analysis

Results of the sensitivity analysis are shown in Table 9 and Table 10 below.

The average savings interest rate in the “high” digital engagement Open Finance equilibrium is almost the same as the baseline, with only a few small variations across scenarios. This result is driven by the limited variation in digital engagement, where engagement is almost 100% for all but the oldest age group (see Figure 6). This means that in this scenario only the proportion of balances held by the oldest age group have a meaningful impact on the balances that actually switch, and the price effects thereafter.

Using a different age distribution of balances on standard rates has a relatively larger effect in the “low” digital engagement scenario. This is due to a greater variation in engagement across age groups affecting the balances that switch under each test case (see Figure 5).

If the distribution of balances on standard rates skewed significantly younger, the impact of the Open Finance equilibrium on average savings rates in the “low” digital engagement scenario would be slightly more pronounced than in the baseline. If the distribution of balances on standard rates skewed significantly older, the impact of the Open Finance equilibrium on average savings rates in the “low” digital engagement scenario would be slightly less pronounced than in the baseline. The overall scale of impact of these scenarios on our modelling results is very low.

Table 9 **Impact of a change in standard rate balances across age groups on prices – low digital engagement scenario**

Market/Mutuals	Baseline	Significantly younger	Significantly older
Market	0.20%	0.22%	0.18%
Bonus Rate Pricing Model			
Medium to large mutuals	-0.08%	-0.08%	-0.08%
Small mutuals with focus on standard rates	0.12%	0.14%	0.11%
Small mutuals with focus on fixed and intro rates	-0.46%	-0.48%	-0.44%
Flat Rate Pricing Model			
Medium to large mutuals	0.06%	0.07%	0.05%
Small mutuals with focus on standard rates	0.13%	0.15%	0.11%
Small mutuals with focus on fixed and intro rates	0.02%	0.02%	0.01%

Source: Frontier analysis

Note: Change in weighted average interest rate (% point change).

Table 10 Impact of a change in standard rate balances across age groups on prices – high digital engagement scenario

Market/Mutuals	Baseline	Significantly younger	Significantly older
Market	0.48%	0.49%	0.46%
Bonus Rate Pricing Model			
Medium to large mutuals	-0.05%	-0.05%	-0.05%
Small mutuals with focus on standard rates	0.29%	0.30%	0.29%
Small mutuals with focus on fixed and intro rates	-0.61%	-0.61%	-0.60%
Flat Rate Pricing Model			
Medium to large mutuals	0.20%	0.21%	0.19%
Small mutuals with focus on standard rates	0.43%	0.45%	0.41%
Small mutuals with focus on fixed and intro rates	0.06%	0.06%	0.06%

Source: Frontier analysis

Note: Change in weighted average interest rate (% point change).

Annex B Case study: Open Finance and Smart Data in other jurisdictions

A 2022 report from the OECD analyses different types of data sharing frameworks available in other jurisdictions, the impacts these have had on customers and financial markets and the common challenges with data sharing initiatives.

Existing data sharing frameworks

Most OECD countries have an established framework for Open Banking, but only some have extended frameworks to Open Finance.⁸⁶ For example:

- 1 The US and Switzerland have a market-led Open Finance approach. Switzerland's framework spans the entire financial sector, with standards extending beyond payments to areas like wealth management data. An association oversees API standards coordination through formal and informal forums involving regulators and market participants.
- 2 Australia has implemented the Consumer Data Right (CDR) which allows customers to securely share their financial data with accredited third parties. The CDR applies to the banking sector and is expanding to other sectors such as energy and telecommunications. Broader financial products are under consideration.
- 3 Brazil's Open Finance framework includes insurance, pension funds, investment, and foreign exchange.
- 4 In Israel, information sharing covers securities and deposits, with potential additions allowed by the Financial Information Service Act.

Market Effects

Various use cases have emerged within financial services. These primarily occur in the payment space (payment information and initiation served) with other services based on financial management, product comparison tools, account verification and balance checks.

Data sharing frameworks are reported to have positive impacts for both financial services and customers, through entry by fintechs, innovation, competition, lower costs and better customer experiences. For example, fees have reduced in several OECD countries across different financial services, and some consumers report improvements to financial management and budgeting. There is also some evidence of greater cooperation between banks and fintechs in the EU and Japan.

⁸⁶ See "Shifting from Open Banking to Open Finance" (2022) from the OECD. Available at: [Shifting from Open Banking to Open Finance \(oecd-ilibrary.org\)](https://oecd-ilibrary.org/open-finance)

Challenges

Numerous challenges in data sharing approaches are cited. These include ensuring responsible and safe data access, attributing liability and consumer safeguards, and promoting data interoperability.

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