BAKER & MCKENZIE

For further details please contact:

Yuko Mishima
Public Relations Assistant Manger
Phone + 81 3 6271 9408
yuko.mishima@bakermckenzie.com

Press Release

Artificial Intelligence to increase market competitiveness in financial services but regulators struggling to keep pace; new report

- Artificial Intelligence (AI) predicted to bring about dramatic changes in financial services
- Financial industry predicts AI will have a positive impact on competitiveness but questions remain around regulators' ability to keep pace with changes
- Risk of market instability with the advent of AI; Asia Pacific lagging behind other regions in AI investment
- However, Hong Kong, Singapore, Sydney and Tokyo still key hubs of fintech in Asia Pacific

Singapore/Tokyo, April 26 2016 - Artificial Intelligence (AI) is predicted to bring about dramatic changes to the way financial markets operate, increasing the competitiveness of the sector, but with the possibility of a rise in market instability, according to a new report, *Ghost in the Machine: Artificial intelligence, risks and regulation*, by global law firm Baker & McKenzie.

AI, or technology that 'learns' from patterns and behaviours and can act accordingly, is one of the fastest growing areas in fintech. In a survey of 424 finance executives, run in conjunction with *Euromoney Thought Leadership*, including 67 from across Asia Pacific, it emerged that AI is largely seen as a major opportunity for the sector, although not one without inherent risks.

Over the next three years, the most dramatic changes brought about by AI will be felt in the areas of trading, financial analysis and IT, according to 64%, 60% and 60% of respondents respectively. Large numbers also expect machine learning to materially affect risk assessment (59%), credit assessment (57%) and investment portfolio management (52%).

Indeed, risk assessment and financial research are the areas where companies are most likely to invest and experiment with machine learning applications in the next three years; half of all financial services companies surveyed globally expect smart tech to be introduced in the next three years in their risk assessment functions, although in Asia this drops to just 38%.

Asia Pacific again risks being slightly behind the curve, as globally 42% of financial institution (FI) respondents say their organisations are investing in in-house AI research and development, which jumps to 47% in North America. Meanwhile only 33% of those FI executives surveyed in Asia Pacific say their workplace is investing in this space. Cost of development remains the number one obstacle for the building of AI/machine learning within financial institutions, followed by a shortage of skills to develop and maintain AI systems.

Tokyo-based Gavin Raftery, Banking and Finance Partner at Baker & McKenzie, and a leading legal expert in fintech in Asia Pacific, said:
"AI is here to stay, and while industry solutions and standards are far from settled, financial institutions delay AI investment at their peril. New entrants to the market, harnessing AI for platforms as diverse as investment research and risk management, will have the ability to disrupt the financial services sector significantly, and that is why we see many FIs actively involved in incubator and accelerator programs; to stay abreast of change, identify investment opportunities and to tap into top talent."

Survey respondents believe AI will encourage market diversity, with more start ups and SMEs entering the market. In fact 56% of those in the financial services sector globally see new entrants spurred on by AI. However, this is also predicted to impact market stability, with 38% of those surveyed predicting a negative impact on market stability, compared with just 27% that see a positive impact from AI.

Looking further ahead, within 15 years, more than two thirds of those surveyed said their own roles in financial services would be substantially or completely changed by AI and machine learning.

The findings also identified a challenge for regulators, with more than three quarters of those companies surveyed believing that financial regulators' knowledge is not keeping pace with advances in technology.

When asked how regulators should therefore be managing the impacts of this emerging technology, the leading response was to encourage collaboration between regulators and fintech adopters, while in Asia Pacific, the top ask was to co-ordinate regulatory efforts across markets, in a systematic global fashion.

Gavin Raftery continued:
"This is a call to action for all of those with a stake in fintech, including start-ups, FIs, regulators and consultants such as those in the legal profession. At a minimum, new technologies need to be understood as they come on stream, and information sharing and collaboration needs to be embraced to keep pace with this rapidly changing sector."

According to the report, technology will not be able to remove the risks inherent in some financial activities. These are likely to persist, regardless of whether humans or algorithms do the work.

As Arun Srivastava, Partner, Baker & McKenzie argues, “Financial institutions have been fined billions of dollars because of illegality and compliances breaches by traders. A logical response by banks is to automate as much decision-making as possible, hence the number of banks enthusiastically embracing AI and automation. But while conduct risk may be reduced, the unknown risks inherent in aspects of AI have not been eliminated."

- Ends -