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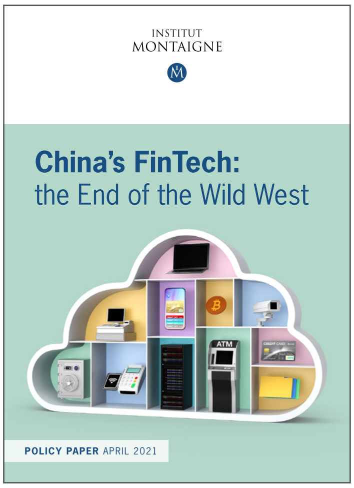

Executive Summary

"To build the national competitive strengths, China will establish and improve the platform economy governance system, giving equal importance to development and regulation, amid efforts to boost fair competition, fight monopoly and prevent the disorderly expansion of capital." Xi Jinping, March 15, 2021

The years 2020 and 2021 mark a critical turning point in the history of the FinTech sector in China. The drama around Ant Group and Jack Ma is only the tip of the iceberg. The issuing of a new set of regulations shows that **the Chinese government is seeking to strike a new balance between FinTech innovation and regulation**. After a long period of hands-off approach, China is now tipping the scale towards regulation. However, this shift did not happen overnight. There has been a series of events that brought the FinTech sector where it is, step by step.

This study provides an overview of the development of FinTech in China, and how the Chinese government has navigated between the needs of innovation and regulation. The general analysis of the sector is complemented by a dive into the country's "big five" – **the five largest Chinese FinTech players**, namely, Ant Group, Tencent, Ping An Group, JD Technology, and Du Xiaoman Financial – including their **international expansion**. Finally, the paper raises a number of important questions from the angle of **European data management** issues, to anticipate a possible expansion of Chinese fintech platforms in Europe.

FinTech, an umbrella term

"FinTech", or "financial technology", is used to describe technologies and innovations that transform the provision of financial services and **compete with the traditional financial establishments**. The notion encompasses **a set of innovative technology-enabled financial services**, such as mobile payment, digital banking, insurance, wealth management, as well as cryptocurrency and cross-border payment.

The global FinTech market was valued at about USD 111 billion in 2019, and is expected to grow to USD 158 billion by 2023. China has one of the most dynamic FinTech markets in the world. In 2018, China's FinTech investments reached USD 25.5 billion, ranking first in the world and amounting to about half of the global total of FinTech investments that year.

The take-off of FinTech in China

A lack of proper financial services and a protective domestic environment in China in the early 2000s provided a fertile environment for the **growth of non-bank payment systems**. Furthermore, the absence of regulations around non-bank mobile payment systems enabled companies like Ant Group or Tencent to grow and reach a critical size to **withstand both competition and compliance costs**. Regulations regarding online payment systems were only issued by the Central Bank in 2010. In addition, to support its domestic players, the **Chinese government strategically delayed opening its financial sector to foreign companies**.

In parallel, the **democratization of smartphones, mobile internet access** and the growing importance of **e-commerce in retail** further boosted the growth of the mobile payment sector. In 2010, China passed the bar of 450 million people connected to the internet, among which 66% used mobile devices.

China's giant platforms have extended their services into the financial sector, leading to **the creation of cross-sector big techs that encompass financial and technology activities under one roof**. The participation of non-traditional financial players has brought challenges and changes to the Chinese financial industry, which has eventually led to visible regulatory efforts in the past few years.

From the Wild West to the "Party leads everything"

The evolution of China's FinTech regulatory environment over the past 20 years can be roughly broken down into **three phases**:

- for the first ten years, **from 2000 to 2010**, the sector went largely unchecked;
- **between 2010 and 2015**, attempts were made at introducing regulations;
- and **since 2015**, there has clearly been a ramping-up of efforts, with 2020 & 2021 reaching the peak.

In the FinTech sector, China has long placed **development before regulation (先发展后监管)** to provide sufficient space and freedom for growth of the industry. This has been the feature of the first phase of FinTech development (2000-2010), providing a relatively lenient environment for companies to explore and experiment.

Attempts to regulate the industry started from 2010, when regulations for specific areas started being introduced. During this second phase, however, the FinTech sector remained extremely unregulated. It led to several high amount **Ponzi schemes in the P2P lending segment**, contributing to the change of mind of China's financial regulators and top leaders. Adding to this is the 2015 stock market crash. It was not only perceived as politically embarrassing, showing the weakness of China's financial system and the failure of the government to prevent it, but also raised the alarm on the risk of capital outflow. Since then, Chinese authorities have clearly expressed their will to regulate the FinTech sector.

In 2015, ten high-level Chinese state regulatory agencies jointly issued the "Guiding Opinions on Promoting the Healthy Development of Internet Finance 2015 (关于促进互联网金融健康发展的指导意见)", **setting legal parameters for Internet finance**. Nonetheless, in order to leave room and space for innovation, the document offered general guidance and advised the formulation of loose regulatory policies.

However, as Guo Shuqing, chairman of the China Banking Regulatory Commission, explains, **"FinTech is a winner-take-all industry"**, and **"with advantage of data monopoly, big tech firms tend to hinder fair competition and seek excessive profits."** As time passed, the state voiced some concerns that resulted in the end of China's hands-off approach in the FinTech sector. These concerns can be summarized as follows:

- Big FinTech companies have **outgrown state-owned banks**.
- Big FinTech companies have **accumulated too much strength**, including political power.
- **Jack Ma provoked policy makers and regulators** by criticizing China's financial regulation at the Bund Summit in October 2020.
- FinTech companies have contributed to **the promotion of irrational spending** through overlending.

During the 2017 National Financial Work Conference (NFWC), Xi Jinping had **urged financial regulators to "dare to" master their supervisory role (敢于监管)**, and highlighted the need to build "a serious regulatory atmosphere where failure to discover risks in a timely manner is a negligence, and failure to promptly address risks is a dereliction of duty (有风险没有及时发现就是失职、发现风险没有及时提示和处置就是渎职的严肃监管氛围)". The regulatory authorities are set to bring all financial activities under regulatory coverage, requiring licenses for all financial businesses following the so-called **"zero-tolerance (零容忍)"** policy in the future for all types of illegal or irregular conduct. The general policy direction for the FinTech industry had therefore been set, and regulations issued in the past few months provide a clear sign that such direction is being consolidated. **What was once considered engines of growth, is now seen as potential agents of chaos.**

China's FinTech conglomerates: The "Big Five"

To provide an overall analysis of the Chinese FinTech market, the study has chosen **the five most prominent and financially potent companies** in the sector, which we refer to as the "Big Five": Ant Group, Tencent, JD Technology, Ping An and Du Xiaoman Financial. These five companies can be classified as "integrated financial services", or FinTech conglomerates, as they offer a full range of services from mobile payment system to wealth management and credit scoring services. What differentiates them is the detail of their offers and the sector which they prioritize among their services, which reflects their background.

Ant Group (蚂蚁集团) and Tencent (腾讯) are the two leaders of the domestic FinTech market. Their respective mobile payment systems, **Alipay and WeChat Pay, maintain a duopoly in the domestic market**. "Latecomer" companies, such as Ping An (平安), Du Xiaoman Financial (度小满金融) and JD Technology (京东科技), have a strong emphasis on providing tech solution rather than competing for financial services with other FinTech companies and financial institutions head-on, even if they do offer such services to consumers. Ping An is the only "major" FinTech that does not come from the Internet and /or e-commerce sector.

As a broader trend, FinTech companies seem to be **moving away from the "fin"** aspect and **emphasizing the "tech"** aspect of their services in an attempt **to adjust to the increasingly harsh regulatory environment**. However, those appear to be just cosmetic changes. As later cases show, despite the change of emphasis and the attempts to project themselves as benevolent technology providers, these companies have remained under the purview of financial regulators – especially Ant Group, as financial regulators have not turned down the heat towards it.

International Expansion of Chinese FinTechs

Chinese FinTech companies have **ambitions to "go global"**, despite being at the early stages of the international expansion of their business activities. In 2016, Eric Jing, then chief executive of Ant Financial – as the group was then called – made 'going global' a core mission. Hoping to replicate its success in the domestic market, he set the goal of building a worldwide customer base of 2 billion users within ten years, of which 60% is supposed to be from outside of China.

A few years ago, having gained confidence through their domestic success, Chinese FinTech companies did draw an international blueprint which aimed to **replicate their domestic success abroad**, counting on their breadth to challenge existing overseas FinTech competitors and to occupy space where there is no competition yet. There have been some results: Ant Group and Tencent have provided **convenience abroad to their Chinese e-wallet users**. Ping An sells its financial services as "products" to foreign micro, small and medium enterprises (MSMEs). At home, they could grow with only limited outside competition, but this is not the case in the global market. Their actual presence in Europe remains minimal, especially compared to the relatively well-established American tech giants. Overall and despite a growing appetite for the global scale, **international expansion is currently not the priority of Chinese FinTech companies and their global footprint remains very limited**. But looking ahead, the possible expansion of Chinese FinTech platforms in Europe raises important questions.

Data transfers and flows between China and Europe

The most important policy question for Europeans to anticipate relates to **the possible implications of the expansion of Chinese FinTech giants for cross-border data transfers**. The question pertains to the **collection, use, storage, processing, and sharing of data of European data subjects**, i.e., European citizens and residents.

Looking into the operations of the main Chinese FinTech companies, as well as their parent Tech companies, it is apparent that their business models are even more **data-driven** than those of their global competitors. **They penetrate into their customers' life, which covers almost all aspects, gathering real-time data**. This is an advantage that non-Chinese companies find hard to compete with.

However, could the business models which ensured its success in the Chinese domestic market also provide a foundation for Chinese FinTech expansion in Europe? The arrival of Chinese FinTech companies, which built their empires based on an incomparable size and scale of data usage, raises various concerns. These concern **data privacy of users** as well as **the asymmetries of economic models** being leveraged by Chinese companies to gain market shares.

Europe's regulatory efforts to safeguard personal data are distinctive. The General Data Protection Regulation (GDPR) entered into force in May 2018. Chinese companies that collect and process data of EU citizens and residents are therefore subject to GDPR due to its extraterritorial effect. **The EU's own legal protection against data misuse creates a barrier for data-driven Chinese FinTech companies with an ambition to enter the European market**.

These Chinese companies are also likely going to be subject to **the proposed EU Digital Services Act (DSA) and the Digital Markets Act (DMA)**. Bearing in mind DMA's definition of "gatekeeper", the five FinTech giants examined in this study are likely to fall under these two new proposals should they wish to ramp up their European expansion. These regulatory proposals might restrain Chinese FinTech companies from becoming dominant players in the EU internal market once adopted.

Despite these limitations, the Chinese platforms still possess important assets for an international expansion in the FinTech sector. These include their **long experience in the field** and the **quality of their technologies** built on access to **limitless amounts of domestic data**. Although the international expansion is not Chinese FinTech giants' top priority at the moment – as it is being hindered by both external and internal factors –, **European banking and finance would do well to prepare for this competition in the near future**.