

# Discussion of "Open Banking..." by He, Huang and Zhou

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# The goal of Open Banking

- Long argued there is informational synergy between a bank's deposit-taking and lending businesses.
- Resultant market power might be reduced if banks were forced to share information with other potential lenders.

## Credit Information

Increases efficiency of lending (Nakamura 1993, Mester Nakamura Renault 2006, Parlour, Rajan, Zhu 2020)

## Marketing Information

Only increases ability to price discriminate (eg Garratt-van Oordt 2021 Chiu-Koepl 2022)

# The Idea, Formally

- Competition between two lenders with different information about borrower. (Common values auction: Broecker, 1990 but also Rajan, 1992 (see eg Kahn teaching notes))
- What are the effects of requiring one lender to share information with the other?
- What are the effects of giving the borrower the option to have the information released to the other lender?

The informed lender has a monopoly he exploits.  
Sharing the information has no social costs and increases competition

(if we ignore costs of information gathering—eg a free byproduct of account management)

It also increases the efficiency of lending by new lenders.  
Welfare of borrowers goes up.

The informed lender could price discriminate based on deposit information

e.g. use it to deduce borrower's cost of applying elsewhere

Without information release, protection from price discrimination by outside lender.

Information release reduces welfare of borrower

if price discrimination could be carried out efficiently,  
no further efficiency implications

it may discourage use of banks if privacy can't be trusted (Kahn McAndrews Roberds 2005))

Adverse selection: (individuals who are already informed of their type)

heterogeneous welfare effects: improved efficiency  
can hurt those who know themselves to be bad.

Is adverse selection important?

Yes. Seems to be a big problem for fintech lenders

- Strategic behavior in light of adverse selection (winner's curse).
- In Nash equilibrium of auction, second bidder's strategy sets the profits first bidder can achieve.
- Does the extra info make them closer in efficiency or does it push them apart?



- Borrowers would want to shield their information from fintechs
- At first glance giving them an option might solve the problem
- But then the choice of exercising the option itself becomes a signal

- How does competition among fintech change the story?
  - From pov of bidder, winner's curse even worse with multiple agents
  - But efficiency overall would generally improve
- What if existing banks hire data miners?
  - Banks seem genuinely worried about technologies
  - But perverse effects depend on leapfrogging skill
- Signals only false positives. (Better informed reject more)
  - Is this important for results or only for exposition
- Caveat: perverse results are possible, not inevitable

- Great topic and careful modeling
- Framework clarifies many of the real issues in open banking
- Right starting point for policy analysis