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The City will win again in Brexit Bang

Fears that leaving the EU will put London's bankers out in the cold are misplaced. Across the capital, tech innovators are preparing to disrupt finance again — to our profit, says Iain Martin

Few areas of economic activity are more ripe for disruption than banking and finance, and the City is well placed to cope with the changes beginning to sweep through the sectorGETTY

The City of London has had a lot thrown at it in the past four centuries. The Square Mile burnt down in the great fire of 1666 and was bombed by the Luftwaffe in the 1940s and by the IRA in the 1990s. As the nation's financial centre, the crowded patch of ground between Fleet Street and the Tower of London has hosted terrible scandals throughout its history, caused by a colourful cast of visionaries, rascals and even outright swindlers. Yet it has survived and for the most part prospered because, love it or hate it, the place is a remarkable generator of jobs, voraciously sucking in talent.

But for how much longer? Once again, this time because of the Brexit vote in June, the talk is of the City facing an existential crisis. Its status as one of two premier global centres, the other being Wall Street in New York, is in doubt.

Relegation would put into reverse the Square Mile's renaissance that has its origins in the Big Bang of 1986. It was 30 years ago that Margaret Thatcher's government bust open the old cartel at the stock exchange and encouraged big foreign firms to move in.

Since then it has mainly boomed, the financial crisis of 2008 aside, to Britain's benefit. The contribution made to the exchequer by the UK's financial services industry last year was £66.5bn, according to the City of London Corporation.

Before the EU referendum, many leading financiers and spokesmen for those big foreign and British banks — encouraged by the Treasury and No 10 — claimed that this bounty was at risk. But is it? Some bankers said that if the British dared to vote to leave the EU, then tens of thousands of jobs would be lost as they would consider moving operations to

Dublin, Paris or Frankfurt. To find that believable one must ignore the question of whether any of those financiers had tried to hire or fire staff under France's ridiculously uncompetitive labour laws, or attempted to persuade their employees to move their families to the outskirts of Frankfurt.

There is genuine concern that the UK will lose its special status, in which it sits outside the euro while dominating European finance to an extraordinary extent. British-based institutions have a so-called passport that allows them to operate across the EU, but arguably much more important is the arrangement by which London is allowed to handle transactions in euros in which hundreds of billions and even trillions are at stake.

By 2013 London's lead in Europe on all manner of measures was gigantic: 78% of all foreign exchange trading in the EU took place in London; 85% of all hedge fund assets were in the UK and 50% of fund management; 23% of all insurance premiums and 19% of all money lent by banks in the EU were organised in London. Even if the euro became a troubled currency, it still represented a tremendous opportunity to move around debt and trade financial instruments, which London has long been good at.

If that trade goes, and the eurozone countries make it difficult for their banks to use London, then the commuter trains coming in from the capital's suburbs and the home counties every weekday morning will soon be a lot less crowded. Tens of thousands could lose their jobs.

In this bleak scenario the UK will also find itself shut out of the important but seemingly arcane discussions undertaken by bureaucrats in Brussels and banking regulators in Basel, where the international rules that govern banking and the flow of money in Europe and beyond are decided. Britain post-Brexit will apparently be reduced to a pathetic rump, receiving orders from distant regulators over whose decisions it has sacrificed all influence.

What a counsel of despair. Perhaps we should just close the City after Brexit and be done with it. But no, because there is a much more positive way of looking at the prospects, and not just because EU countries will continue to need London's expertise in financing deals and trading.

It is only 14 years since the death of the City was last predicted wrongly, during the invention of the euro and Britain's (fortunate) refusal to join. Smart opinion agreed that it would leave London isolated and put Frankfurt on course to become Europe's money capital. Yet London did not decline. It did the opposite. It boomed, and even the 2008 financial crisis did not interrupt its progress for long.

Today, boring old Frankfurt remains a relative sideshow in terms of financial firepower. It could never compete with the unique cocktail that entices foreign financiers and the gifted and greedy to London. The Square Mile is a true 21st-century international hub, thanks to time zone, language, history, experience, law and English schools to which foreign bankers want to send their children.

In the Square Mile traditional methods of trading work seamlessly with new technologyBLOOMBERG/GETTY

Of course, just because the pessimists were wrong about the euro's impact on London does not mean all will go well this time. Indeed, there is a warning from history about potential decline that is worth taking seriously. The City's worst experience in the modern period came with the outbreak of the First World War, which shut the gloriously open cross-border markets of the Victorian and Edwardian era, when money flowed across continents, largely unimpeded by government intervention. Capital controls, which were introduced in the Second World War and continued after it, restricted businesses and individuals who wanted to move money around the world. It meant the healthy and normal flow of investment in and out of the country was curtailed.

It was a mad approach ended by three uncoordinated innovations. In 1963 the German-Jewish refugee Siegmund Warburg and his team in London invented the Eurobond (nothing to do with the later euro), which created a new way for companies in Europe to borrow and tap into the vast pool of dollars outside America. It became a multitrillion-dollar market and attracted American and Japanese financiers to London.

Then, in 1979, the Conservative chancellor, Geoffrey Howe, scrapped exchange controls. Money could move around freely, a seemingly shocking innovation at the time that transformed the working of the economy. The Big Bang in 1986 completed what amounted to a lifting of the shutters, a reopening after a long shutdown from 1914 to 1963.

What all those innovations had in common was an openness to outside influences. The UK must not cut itself off. But then that is not what is being proposed by Theresa May's ministers or by most sensible Brexiteers, who seek free trade for the City. If sensible voices prevail it should be possible to arrive at a compromise with the EU in which co-operation and trade continue in return for some common standards.

The City's biggest advantage, however, is unrelated to the EU. It is simply this: London is brilliantly placed to benefit from the change that is already beginning to sweep through finance. Few areas of economic activity are more ripe for disruption than banking and finance in the West, with its long-established and over-large institutions, powerful central banks and closed networks of licensed operators, gaming regulation and political links.

Thirty years on from the Big Bang, finance is about to be blown apart again, this time by a digital revolution. Many big banks may be stuffed. It will be full-on creative destruction.

Digital disruption — in finance it is called fintech — is ready to destroy elements of the old system, and the City is a leader in that regard already. Three floors of the main tower at Canary Wharf are full of young coders and entrepreneurs launching start-ups, attempting to reinvent finance and London all over again. Elsewhere, in the clusters of tech developments in the East End, the fintech crowd is also a strong presence developing products for investment and retail banking.

Rival centres such as Silicon Valley on the US West Coast and tech-savvy Israel are in the race too, but only London and New York combine fintech with those traditional advantages of being hubs full of people who know about making money from money.

Some of the more obvious changes coming will be noticeable to us as consumers, in the form of new online banks that will make switching accounts so easy that it takes a matter of seconds to complete. New ways to pay (facial recognition instead of even a contactless card) are promised for customers who are already used to getting what they want from online streaming and delivery services.

The UK is particularly well placed partly because it has taken so enthusiastically to the internet and online shopping. Our internet economy has almost doubled in size since 2010. This year it is expected to provide 12.4% of the UK's GDP. In South Korea it is 8%, in China 6.9%, in the US 5.4% and in Germany 4%.

The British are making the transition to the future fast, creating an opportunity for the City to offer new products to retail customers. By combining new technology and apps with fresh thinking on how to sell shares to individual investors, we may even be able to revive the Thatcherite notion of a share-owning democracy. When interest rates are so ridiculously low and savings return nothing, it might appeal to millions of Britons.

But the biggest changes will be in the main, non-domestic business of the City, deep in the wiring of the international financial system and the giant debt and trading machine that props up our governments, which borrow from it.

The blockchain — digital technology that greatly increases the security of financial transactions — is the most audacious and fashionable fintech innovation of all. It has been invested in heavily by some of the old banks.

The underground digital currency bitcoin (a new form of money) is based on blockchain technology. All that underpins the virtual currency is code, a mathematical calculation that allows it to be produced and traded in a way both sides can see and have total trust in. No government or central bank controls it, and the transaction costs, unlike in traditional banking, are zero.

The best-known proponent of the blockchain is Blythe Masters, a British former JP Morgan financier now based in New York. The insight of the team that Masters runs was that it could be taken mainstream, so that main banks could use the underlying blockchain methodology to move dollars, pounds and euros and transact quickly at low or no cost.

Governments are worried about the potential loss of control involved, of not being able to see what is going on inside the financial system. That is one of the reasons the Bank of England has backed the work of a team of academics from University College London who have come up with RSCoin. It is claimed to be many times faster and more reliable than bitcoin, but the most important respect in which it differs is that it can be controlled directly by the Bank of England and the state, to manage the money supply and help the government ensure financial stability. Although this infuriates the original supporters of bitcoin, the libertarians who want a revolt and a new system entirely free from government interference, it is another example of London's innovation.

Whatever the outcome of these battles between the old and the insurgent new, it seems that how we pay, save, invest and even think about money is in the process of being transformed. In such a fast-moving situation, the very idea of worrying too much about a large regulatory bloc — such as the EU or the eurozone — handing down orders may soon look out of date, if it does not already.

Having maximum freedom of manoeuvre may be a post-Brexit asset that attracts rather than repels investors to the UK. Brexit is not without its difficulties, of course, but the Square Mile can work its strange magic again. All that one can say for sure is that the City will survive, and prosper. It usually does.

Crash Bang Wallop: The Inside Story of London's Big Bang and a Financial Revolution that Changed the World, by Iain Martin, is published by Sceptre on September 8