ignition house

Structured Products

Qualitative Research with Consumers

Prepared by Ignition House for the Financial Conduct Authority (FCA)

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Acknowledgements

This document reports the findings of a research project carried out for the Financial Conduct Authority (FCA) by Ignition House from August 2013 to October 2013.

Tim Burrell and Victoria McLoughlin from the FCA managed the project. At the FCA, several colleagues contributed to the design of the interviewing materials and to the research plan overall, and we thank them collectively.

We would like to thank our regional qualitative recruitment specialists for meeting the challenging requirements of this project and the 100 individuals who gave up their time to be interviewed with such good will and patience.

Janette Weir of Ignition House authored the report, with support from Edward Ripley.

Any errors in the report are the responsibility of the authors.

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Glossary

This report contains a number of industry terms and specific descriptions of participants.

Term	Meaning
CAP	The maximum return that is payable on a Structured Product in the event of a stock market rise.
Cliquet	A structured product whose return is calculated on the performance of its underlying index, in a given number of sub periods over the overall term of the product.
Endowment Policy	A life insurance contract designed to pay a lump sum after a specified term.
Equity ISA	An Individual Savings Account which enables the holder to invest in a wide range of financial products such as unit trusts, stocks and shares and open ended investment companies, in a tax efficient manner.
Execution Only	When an individual takes his or her investment decisions facilitated by an intermediary without seeking or obtaining financial advice.
Financially Capability	A gauge of a person's financial sophistication and understanding.
Fixed Term Deposit	A savings account or deposit which pays a fixed rate of interest over its designated term.
Kick Out	When a Structured Product matures early due to the underlying index it is linked to, having risen to a specified level.
Lock in	The time period, usually a minimum, which an investment is tied up before an investor can withdraw.
Unit trust	An investment fund that issues units for public sale.

Abbreviations

Abbreviation	Definition
BS	Building Society
FCA	Financial Conduct Authority
FR Bond	Fixed Rate Bond
FSCS	Financial Services Compensation Scheme
FTSE	Financial Times Stock Exchange
IFA	Independent Financial Adviser
S&I	Savings and Investments
SCARP	Structured Capital At Risk Product
SP	Structured Product

Reporting Conventions

The report makes use of two types of illustration to support the findings:

Verbatim comments

These are respondent quotations, based on interview recordings, with only minor editing. They are labelled by:

- Whether the consumer holds a structured product or not;
- Which of the three financial capability segments (low, medium or high) the consumer was allocated to;
- Whether the consumer took their product out via a bank of building society, IFA or direct.

The respondent quotations demonstrate their own views and perceptions and may not always be factually correct.

Graphical representations/ counts

The number of consumers giving a particular response is shown in some report sections as the (n). Counts are provided to indicate the spread and balance of different behaviours or views among consumers who participated in the research. Typically, they are based on interviewer interpretation of qualitative responses given by respondents. **These are indicative only and should not be regarded as statistical measures. The research is not necessarily representative of all structured product customers. Quotas were imposed to achieve sufficient cell sizes for analysis rather than to be representative.**

1. Executive Summary

1.1 Research objectives and methodology

The FCA recently gathered information which led it to question whether consumers are able to effectively assess the value of structured deposits or capital protected structured investment products and decide whether these products are an appropriate investment solution to meet their needs.

The FCA commissioned this research to explore:

- the reasons why consumers choose to invest in structured products and what they perceive to be ‘valuable’ or ‘useful’ about the product class;
- the factors that motivate consumers to purchase structured products when compared to alternatives;
- what customers understand about these product and their features, and whether this matches reality; and
- how well consumers can assess likely product performance.

This research is based on the findings from 100 qualitative interviews with consumers; 88 held a structured product and 12 would be open to doing so in the future. Interviews lasted 60 to 90 minutes and were conducted across eight locations around the UK. We used a range of stimulus materials to test consumers’ ability to understand common product features and how they assess the value in products against product substitutes.

Structured capital at risk products (“**SCARPS**”) were out of scope for this research.

1.2 Key findings

1.2.1 At face value, structured products appear to be meeting the key underlying financial need of customers, in that they guarantee to return their capital and offer potential for upside

Respondents in our research overwhelmingly said that structured products are a good match to their fundamental financial needs because they offer security of initial capital with the chance to earn better returns than a savings account. These were the key sales themes used.

The research also suggests that, while not necessarily a valued feature by all, the lock-in period is well understood by consumers, as is the fact that they may not get back all of their initial investment if they exit early.

1.2.2 Respondents had very limited background knowledge about structured products and were usually introduced to the product

Prior to taking out their product, few respondents were aware of structured products and those that were knew little about their features. Respondents were typically introduced to their product by an advisor or by bank or building society staff. Most felt that advice was definitely needed to feel comfortable investing and structured products were generally perceived to be more complicated than other savings products, both in terms of how they work and in terms of understanding what they will get at the end.

The sales process, therefore, has a strong influence on consumers' propensity to purchase structured products. Respondents almost unanimously described bank and building society sales staff in a positive light – often describing them as experts and knowledgeable – and placed a lot of weight on their recommendations. However, despite the prevalence of fact finds in the sales process, there is limited evidence that products other than the structured product were discussed as a solution to meet the needs of the consumer.

1.2.3 The 'push' nature of the sales process coupled with the relatively short decision-making timescales means that, left to their own devices, some consumers will not actively seek to make comparisons themselves

Few respondents thought very deeply about purchasing their structured product, typically discussing the product for less than 30 minutes. There is very little evidence to suggest they did any follow-up research or compared structured products to alternative investments.

Because respondents see the product as low risk (due to the capital protection), many were confident to go ahead with the investment without much thought or further exploration, despite a low baseline knowledge.

1.2.4 Structured products are expected to outperform alternative savings products, and product holders will be disappointed if they do not do so

Despite not knowing much about the product, most respondents had expectations of returns in the range of 4% to 7% per year, which the current investment climate may struggle to deliver without dividend income.

Most dismissed out of hand the possibility that they could earn more from an instant-access savings account or long-term, fixed-interest deposit account. Indeed, respondents said they would be very disappointed if their structured product delivers no returns (simply the return of their capital), or a return that is lower than what would have been achievable in a bank savings account or cash ISA.

That said, few could give a good explanation of what would need to happen over the term of their investment (for example, to interest rates or the FTSE 100/underlying reference index) to achieve these returns.

1.2.5 There are significant failings in consumers' abilities to assess potential product outcomes or performance, particularly when compared to fixed-interest savings products

Most respondents could not accurately assess the likely performance of their product because they did not know what their investment return is based on.

The majority could recall seeing examples of potential returns prior to taking out their product, but these either consisted of an adviser talking them through past performance or a comparison of what returns they would get under different economic scenarios. Not everyone found these easy to understand.

Furthermore, when asked to talk about the return they hoped to receive, there was often a discrepancy between annual rates of return and the cash sums they would want to get at the end, suggesting that consumers struggle with the calculations and particularly with compounding.

Most could not give a coherent explanation of when they might be better or worse off investing in structured products rather than putting their money into deposits or equity-based investments.

1.2.6 Few respondents had a good understanding of the underlying factors driving potential returns and did not consider likely market levels when making investment decisions

A large proportion of the less financially-capable respondents could not make reasoned decisions on the likely outcomes of structured products, because they do not understand the underlying factors driving returns. In particular, many could not explain what the FTSE 100 is or what factors might affect it.

Respondents rarely make any attempts to consider likely FTSE performance or market levels when making their investment decisions and the majority did not understand the impact of market timing on the potential payouts, regularly saying that they would invest only when markets are high or rising and would not invest when the markets were low or falling.

While most had some understanding of what inflation is and could say why inflation is important when thinking about savings at a conceptual level, many failed to explicitly link inflation to the return they can get on their investment and failed to make the connection that a simple capital return or low return would actually result in a loss in real terms. So, although consumers believe that structured products are meeting their underlying financial need to guarantee their initial capital, many overlook the impact inflation could have on capital erosion.

1.2.7 When consumers are given more information about the potential outcomes associated with structured products, they make different decisions

We created an exercise to test how consumers assess value in structured products against product substitutes and where this notion of value comes from. Respondents were asked to look at four different hypothetical structured products. Each product had a range of potential outcomes that could be achieved on maturity and a probability attached to that return being triggered. Respondents were then asked to assess whether each was attractive to them and whether they felt it was offering good value for money. After reviewing each structured product, respondents were then shown the returns from a five year Fixed-Rate Savings Bond and were asked to revisit their original assessments and say whether they would choose to invest in the structured product or the alternative.

When presented with the range of potential outcomes, a significant minority (around one quarter) of structured product holders would choose not to invest in **any** of the structured products on offer. Furthermore, when shown the return from the alternative savings bond, well over half preferred the certainty of the fixed-interest rate to the payouts on offer for each structured product.

This exercise also highlighted that there are significant failings in consumers' abilities to assess whether a product is going to deliver value for money, even when presented with information on possible outcomes. The issues ranged from respondents not knowing what a probability is and failing to understand percentages, to struggling to convert five year returns back to an annual figure or making realistic comparisons between a five year return and an annual interest rates.

Ultimately, consumers are likely to need encouragement to make such comparisons, and the comparison vehicle will need to be very clearly explained, with like-for-like returns in cash terms and percentages.

1.2.8 Respondents had a good understanding of basic product features and where structured products fit in the investment landscape, but struggled with the details

At a basic level, respondents understood how structured products differ to a direct investment in an index or a fixed-term deposit. Respondents could also easily identify some possible benefits of structured products over these alternatives, but the less financially capable struggled to identify any risks.

Unprompted, a number of structured product features were regularly misinterpreted (in particular, 'kick out' features and the 'cliquet' product), but, if explained, most respondents could understand them.

However, many struggled to physically calculate the returns structured products would deliver, typically due to poor mathematical abilities (e.g. working with percentages) or due to misinterpretations of the wording in the example documentation (e.g. misunderstanding the phrase 'the greater of 100% and a minimum return of 10% in total').

Respondents also struggled where products had more than two complex features in combination. For this reason, providers will need to be mindful when constructing products to consider the consumer's ability to take on board multiple features, and such products will need careful explanation and wording.

1.3 Overall Conclusions

Structured products appear, at face value, to be a good match for consumers seeking a relatively low risk product with a capital guarantee and the potential for upside. However, this research suggests that many consumers – particularly those with lower financial capability - are not able to accurately assess whether their product will deliver value for money. The least financially capable have a limited understanding of the underlying drivers of performance and there appears to be evidence across all segments that consumers are under-estimating what could be achieved from alternatives (mostly due to confusion over the effect of compound interest) and over-estimating the returns their product is likely to deliver in the current climate.

Our findings suggest that, left to their own devices, few customers actively make meaningful comparisons between substitute products and that, for many, this type of analysis is outside of their comfort zone. We found little evidence that this type of exercise systematically forms part of the sales process today, suggesting that a more formal comparison process may be needed at the point of sale to help customers make more informed decisions.

Our research indicates that explicit comparisons of potential product outcomes and comparisons of the returns from structured products with common product alternatives would appear to have powerful impacts on consumer behaviour. Such information will need to be delivered in a careful way to cater for all levels of ability. Comparison vehicles will need to be clearly explained, and include like-for-like returns in both cash terms and percentages.

Structured products often have a combination of features that impact upon the potential payout, such as kick outs, caps, averaging and reference indexes. Our research shows that there is a critical mass of features beyond which consumers will start to switch off. Providers will need to be mindful when constructing products to consider consumers' ability to take on board multiple features.

2. Project Scope and Aims

2.1 Project introduction and scope

Structured products are investments or deposits that aim to deliver a return based on the performance of an underlying investment. This return is usually based on the performance of a specific market, such as the FTSE 100, and delivered at a defined date, known as the maturity date.

There are broadly three types of structured product:

- **Structured deposits**: these are essentially fixed-term deposit accounts where, instead of earning interest at a set or variable rate, the return is dependent upon the performance of the underlying stock market index or another defined underlying measurement. While some are available in the IFA space, they are typically sold by banks and building societies and are designed to return at least the original capital in full at maturity;
- **Capital 'protected' structured products:** Like structured deposits, these are designed to return the original capital regardless of the performance of the underlying measure. However, unlike deposits, they do not usually benefit from FSCS protection if the counterparty defaults. These products can often offer higher returns as a result.
- **Structured capital at risk products ("SCARPS")**: These products put a customer's initial capital at risk and as a result usually have the potential to produce higher returns, but also to give rise to a loss at maturity. Many incorporate a barrier that protects the capital until the stock market falls by a certain amount, often 50 per cent.

Structured deposits and *capital 'protected' structured products* were in scope for this research. These terms cover a broad range of investment and deposit products, but are typically 'structured' by investing the majority of an investment into a note or deposit account which is designed to return capital at the end of the product term. The remaining proportion of the investment is invested in derivatives that are used to generate the returns needed to deliver the defined capital growth or income.

Products typically have the following common characteristics:

- a fixed investment term (often five or six years);
- structured to offer capital protection at a minimum on product maturity provided that the underlying counterparty does not default;
- penalties for early redemption or exit;
- interest or growth payments calculated using a pre-determined formula that is linked to the performance of a separate reference measure (e.g. an index, or basket of equities);
- potential for investors to receive no growth or interest on the investment at the end of the product term.

Structured capital at risk products ("SCARPS") were out of scope for this research.

2.2 Research aims

The FCA recently gathered information which led it to question whether consumers are able to effectively assess the value of structured deposits or capital protected structured investment products and decide whether these products are an appropriate investment solution to meet their needs.

The FCA commissioned this research to explore:

- the reasons why consumers choose to invest in structured products and what they perceive to be 'valuable' or 'useful' about the product class;
- the factors that motivate consumers to purchase structured products when compared to alternatives;
- what customers understand about these product and their features, and whether this matches reality; and
- how well consumers can assess likely product performance.

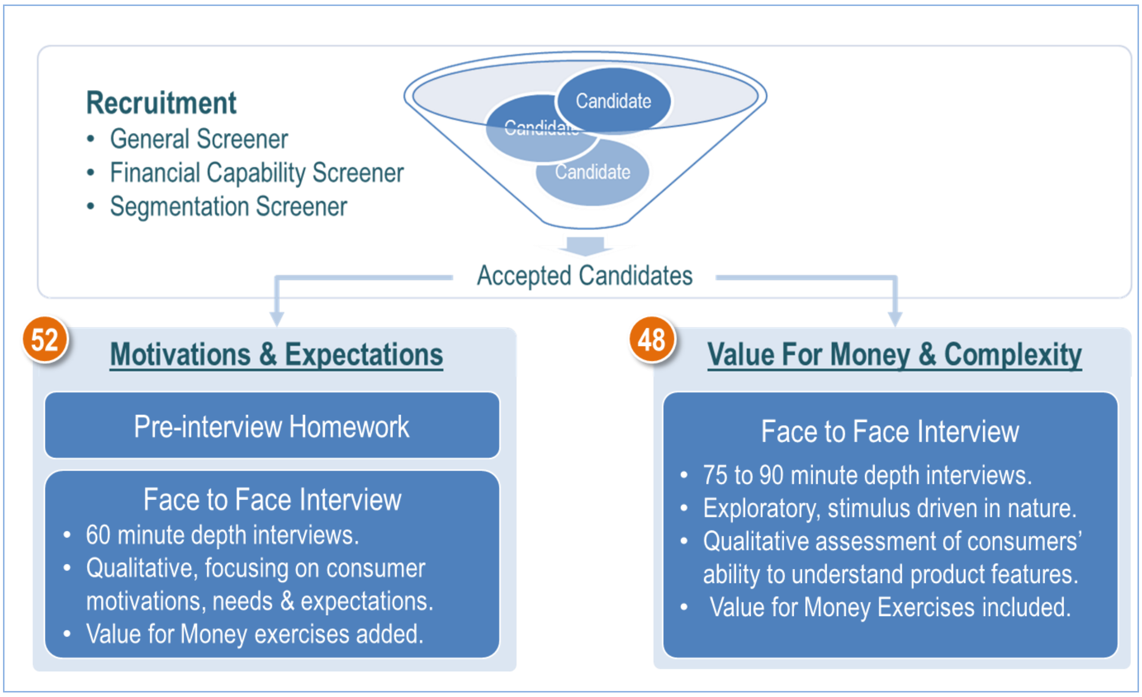
3. Research Methodology

This research involved 100 face-to-face in-depth interviews with consumers. Interviews were qualitative in nature, lasted between 60 and 90 minutes, and were held in eight locations across the UK. All interviews were conducted between the 19th August and 12th September 2013 by one of our senior Research Directors familiar with structured products.

Due to the breadth of insights required, the research was split into two parts, with each part focused on providing different insights into the 'customer utility function' of structured products:

- In Part 1 ***'Motivations, Needs & Expectations'*** we spoke with 52 consumers who had taken out a structured product in the last 18 months to examine their motivations for purchasing their product, what financial needs they had prior to purchase, and how they expected their product to perform.
- In Part 2 '***Value for Money & Complexity***' we spoke to 36 product holders and 12 non-product holders to assess their ability to understand common product features and understand how they assess the value in products (vs. product substitutes) and where this notion of value comes from.

Figure 1: Research methodology summary



One of our key methodological challenges was to find suitable respondents who had recently taken out a structured product, as structured products are marketed under a plethora of names including “Savings Accounts”, “Protected Capital Accounts” and “Index Bonds”. They have historically also been called “Guaranteed Equity Bonds”, although this practice has been restricted by the FCA. Certain types of products can be placed within a Cash ISA wrapper which adds an extra layer of complexity. To overcome this issue we used a multi-staged recruitment process which included a rigorous quality control processes to ensure that respondent’s structured product holding was genuine.

Screeners were also used to ensure the research is representative of the consumer demographic that actually invests in such products, and therefore that the study reflects “real-life” preferences and decisions. This included setting quotas by distribution channel, type of structured product, level of financial capability, and so on.

A range of stimulus material was development by Ignition House in partnership with the FCA team, including exercises to test product-feature complexity and assessment of value for money (vs. product substitutes).

Please refer to the *Technical Appendix* for further details related to the research methodology, including sample quotas, discussion guides, and stimulus materials.

4. Financial Needs & Motivations for Purchase

This chapter provides some background to the respondents in our study and explores the thought processes that they went through when purchasing a structured product and what other products they considered. In doing so it considers the financial needs that respondents had prior to purchase and the factors that influenced them to make their purchase. It draws on the findings from Part 1 (***'Motivations, Needs & Expectations')*** of the research; based on interviews with consumers who had recently taken out a structured product via a range of advised and non-advised channels.

4.1 Key findings

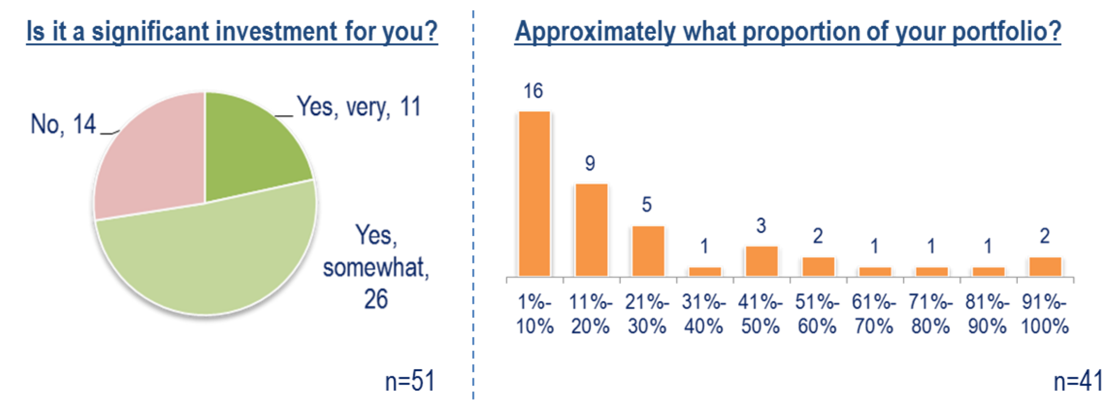
- Prior to purchasing their structured product, respondents were often looking to invest a significant part of their portfolio, but had limited experience of investing lump sums.
- Many did not have a specific use or timeframe in mind for the money.
- Respondents were looking for a product to deliver security of capital protection with the potential for upside. Structured products were felt to offer "the best of both worlds".
- The vast majority of respondents knew very little or nothing about structured products prior to taking out their product.
- Most respondents were introduced to their product by a bank or building society 'adviser' or their IFA. Around half of those that purchased from a bank or building society said that the sales discussion was instigated by their bank or building society because they had 'money sitting around in their account'. Respondents spoke positively about the bank or building society sales process and described sales staff in a positive light. Sales through the IFA channel were more likely to stem from a regular review than a one-off meeting.
- There was poor recall of any alternatives discussed, particularly as part of the bank/ building society sales process.
- Because respondents see the product as low risk (due to the capital protection), many were confident to go ahead with the investment without much thought or further exploration, despite a low baseline knowledge.

4.2 Respondents were often looking to invest a significant part of their portfolio, but had limited experience of investing lump sums

We asked respondents to talk about their financial situation prior to their recent investment in a structured product and to consider what their investment needs were for this pot of money at the time that they made their decision to invest.

Most respondents in our research were very much mass-market customers. Some said they were investing a significant proportion of their savings. The typical sums available for investment were £10,000-£25,000, which accounted for up to 25% of their overall portfolio.

Figure 2: Respondents were often looking to invest significant sums



Base: All respondents taking part in Part 1 of the Research (n=51/41).

Across all respondents, around half reported that the money available for their investment was new money for them (i.e. it had not previously been invested) and had come from a one-off windfall such as pension lump sum, an inheritance or equity from a house sale.

Many respondents, particularly those buying their structured product through a bank or building society, reported that it was unusual for them to have such lump sums to invest and that the process was not familiar to them.

> *"I never had savings before in my life, until my inheritance."*
>
> **Product holder, Low financial capability, IFA channel**

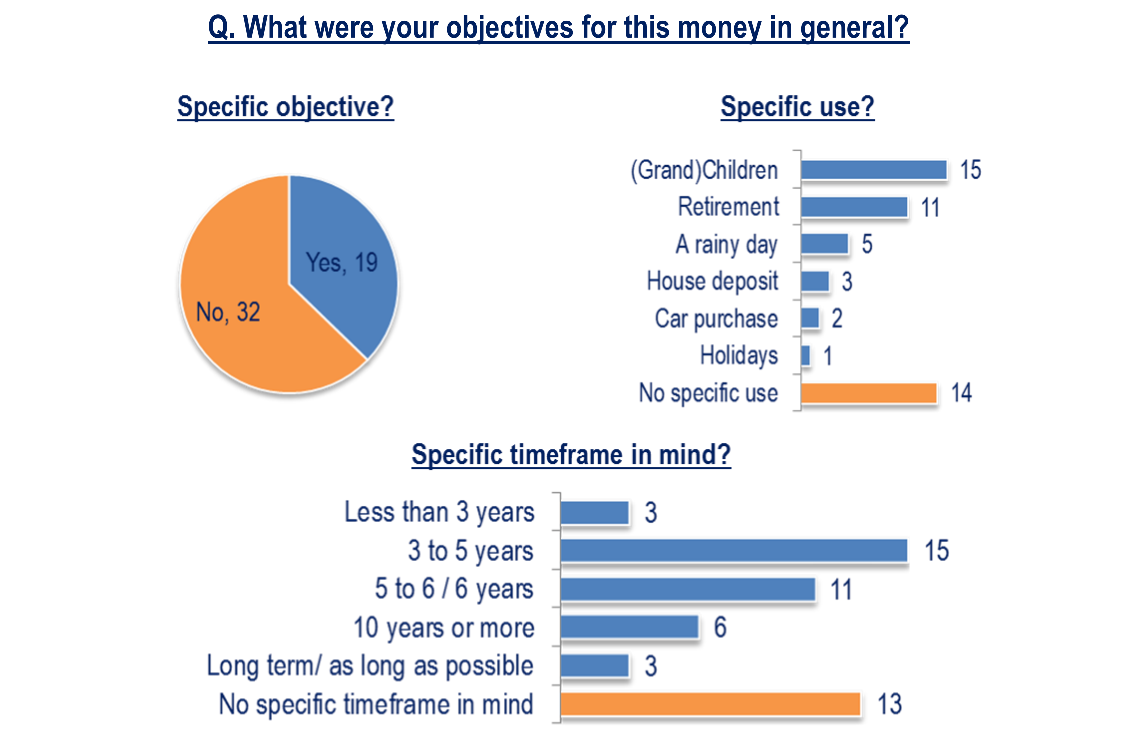
> *"I don't really know about investments, I get nervous talking about them."*
>
> **Product holder, Medium financial capability, Bank/BS channel**

4.3 The majority had no specific use or timeframe in mind for the money

As structured products are held for a fixed term, typically three to six years, we probed respondents about their objectives and timeframes to determine whether the product chimed with their financial needs.

Over half of the respondents in our study did not have a clear idea what the money would be used for, and when they might need to access it. The money was simply seen as a safety net for the future.

Figure 3: Many had no specific objective or timeframe in mind



Base: All respondents taking part in Part 1 of the Research (n=51).

As there was no immediate need for the money, respondents reported they were open to products that required them to lock their money away for a short to medium length of time, particularly as they were aware that this would probably be required in order to generate the potential for higher returns.

> *"If I had had it in an instant-access ISA it's hardly doing anything, it's rubbish, I wasn't bothered about drawing on it. I wasn't going to touch it for five years anyway."*
>
> **Product holder, Low financial capability, Bank/BS channel**

With the vast majority of respondents looking to invest for more than three years, the medium term nature typical of most structured products fits well with their investment time horizons. The vast majority of respondents (all bar six) were also aware that there would be penalties if they tried to access their money early, but recollection of what these penalties would be in practice were somewhat hazy.

4.4 Respondents were looking for a product to deliver security of initial capital with the potential for upside

When asked to recall the investment needs they had for the money, by far the most important objective was that they did not want to experience any capital loss. Respondents described themselves as 'not big risk takers' and were looking for somewhere 'safe' to put their money. Structured products were often described as offering the 'best of both worlds' – and some acknowledged that this had been a message used in the sales process.

> *"We don't work anymore; we can't replace money that we lose. It's not life and death, but that is why we went for the safety net I suppose."*
>
> **Product holder, Low financial capability, Bank/BS channel**

Figure 4: Respondents' financial needs centred on security of initial capital, locking their money away for a set period of time, and doing 'something different'

Base: All respondents taking part in Part 1 of the Research (n=51).

Note: Multiple answers given to this unprompted question. * Other responses included: some risk, linked to the FTSE, short term, protected, reliable, tax advantageous, not passive, element of fun, guaranteed return, long term, access to funds.

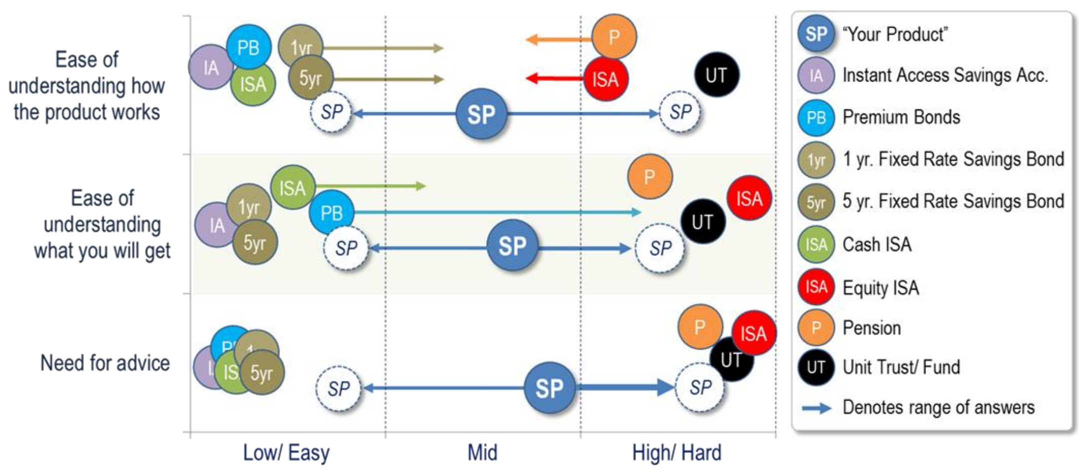
4.5 Most were introduced to their structured product by an 'adviser'

Most respondents were introduced to their structured product by their IFA, bank or building society. Many felt that structured products are more complicated than other savings products, both in terms of how these products work and in terms of understanding what they will get at the end. As such, most felt that 'advice' was definitely needed to feel comfortable to make an investment.

This finding was confirmed by the 'product sort' exercise that we conducted in the sessions. In this exercise, we asked respondents to sort their structured product and eight other savings investments products into three categories (high, medium, low) based on: ease of understanding how the product works; ease of understanding the return they will get; and the need for advice. The results of this exercise, which are depicted below, highlight how respondents view their structured product as sitting somewhere between equity-based investments and savings deposit products in terms of complexity and the need for advice.

Figure 5: For many, structured products are perceived to be more complicated than other savings products, both in terms of how the product works and in terms of understanding what they will get at the end

Q. Please rank these products on the following categories (low, mid, high)



Base: All respondents taking part in Part 1 of the Research (n=51).

Note: Respondents were asked to sort their structured product and eight other savings or investment products into three categories (high, medium, low) based on: ease of understanding how the product works; ease of understanding the return they will get; and the need for advice. Refer to the Technical Appendix for further methodological details.

Note: Arrows denote the range of responses given.

4.5.1 Around half of the bank/ building society sales were not instigated by the customer

Around half of those that purchased from a bank or building society said that the sales discussion was instigated by their bank or building society because they had 'money sitting around in their account'. Some received referrals from tellers within the branch, while others reported that they received a phone call at home asking whether they would be interested in making their money 'work harder'. A large number of these respondents were not actively engaged in thinking about making an investment with their money when referred for such a discussion.

> *"I went in (to the bank) for a totally different reason. I was setting up a couple of accounts for my children, but I had this money which I wanted to put it in a high rate instant savings account or even a notice account, because it had been recommended by the Daily Mail… The lady at the counter, her ears perked up when I talked about what I wanted to do, and she said 'have a word with Mr Smith', and I went to see him about the savings account but then they coerced me into this (the Structured Product)."*
>
> **Product holder, Low financial capability, Bank/BS channel**

4.5.2 A significant number of respondents went to find out what savings products the bank/ building society had to offer

There a significant number of respondents who reported they had specifically gone to the branch to ask for advice on what they could do with their savings. They had mentioned to staff that they had money to invest and were referred for a 'financial health check'.

In a few cases, word-of-mouth recommendations from friends or colleagues triggered a visit to a bank or building society to find out more.

> *"It was mentioned to me by a friend. He knew about different products in different areas, because he was a Financial Adviser. The biggie was when we met with the person at NatWest, we had a lot of confidence in him, if we hadn't it could have been a bit different. I would say we were there for an hour and a half and then 3 weeks later we went for another meeting and signed up for it then."*
>
> **Product holder, Low financial capability, Bank/BS channel**

4.5.3 Advertised headline rates of return sparked interest

Some respondents also reported that in-branch point-of-sale literature played a key role in sparking their interest in structured products. They were attracted by headline rates, and this motivated them to make further queries to the branch staff.

> *"When I went into the branch to have a regular meeting, I saw a flyer on the counter and I enquired about it. That's how it started. I didn't want to lose my money and I knew this was definitely going to be guaranteed, so I thought, well why not?"*
>
> **Product holder, Low financial capability, Bank/ BS channel**

Similarly, adverts in national newspapers were also a driver for interest for a few.

> *"I saw an advert in the Sunday Times for it and thought it sounded quite good. I phoned them up and I went for it because I knew what was roughly around and it sounded quite good. I had been in another one before, which was quite good."*
>
> **Product holder, Medium financial capability, Execution only channel**

4.5.4 Sales through the IFA channel were more likely to stem from a regular review

Most of the respondents who purchased via an IFA reported a long-standing relationship with their adviser. As such, sales through this channel predominately came about from regular reviews or meetings. A couple of IFA sales were driven by the consumer themselves simply using the IFA to validate or verify their thinking.

> *"I had my annual meeting with IFA. He introduced the product. It didn't take long to decide on product, and we glanced through the information. He pointed out the main points of product - the guarantee of capital return appealed to me".*
>
> **Product holder, Medium financial capability, IFA channel**

4.6 Respondents gave positive feedback on the sales experience

Respondents purchasing through the bank/ building society channel were usually referred to a 'financial adviser' for a discussion about their financial circumstances and needs. Such meetings usually lasted an hour or so and included a review of attitude to risk and financial objectives as well as an introduction to the structured product. There was a high level of awareness that bank/building society staff were promoting their own products rather than conducting an independent whole of market review.

Respondents were positive about the interactions they had had with these member of staff, describing them as "knowledgeable", "friendly", "expert", and "professional". They did not feel that the staff had employed any high-pressure sales techniques and the vast majority of respondents were very comfortable with the purchase process they had been through.

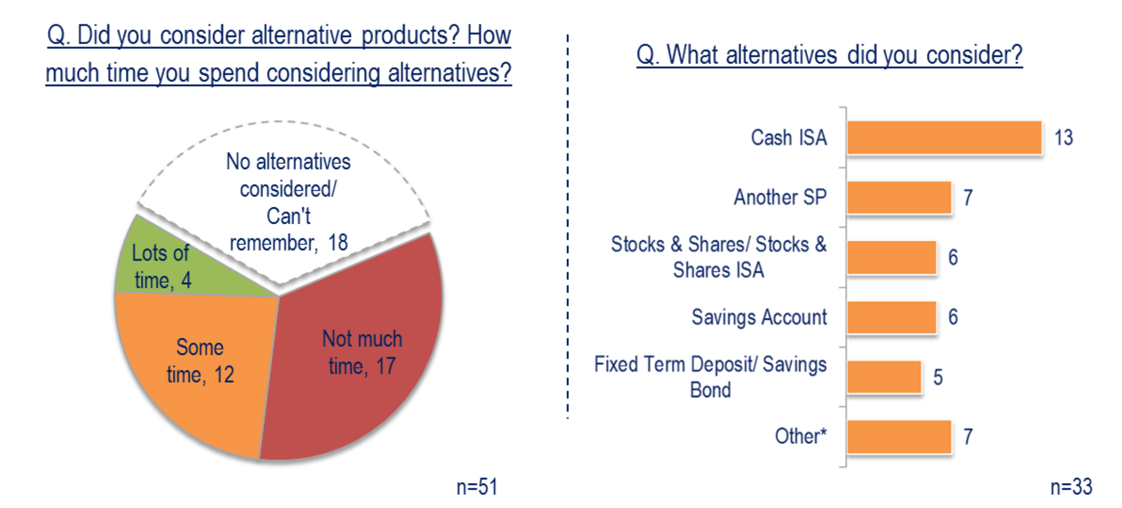
> *"He was very professional, sensible, and put us at ease. Not pushy. He had a nice manner, very knowledgeable, experienced, expert."*
>
> ***Product holder, Medium financial capability, Bank/ BS channel***

Those purchasing through the IFA channel in our research typically had a long-standing, trust-based relationship with their adviser and consequently felt their adviser was acting in their best interests. As such, they placed a great deal of weight on their recommendations.

4.7 Few spent much time assessing whether the product recommendation they received was right for them

Despite the investment often accounting for a significant proportion of their portfolio, only a handful of respondents said they spent a lot of time thinking about and researching alternative products. Just a couple explicitly compared the potential returns from their structured products with alternative savings products.

Figure 6: Just a quarter of our respondents spent 'some time' or 'lots of time' considering alternative products



Base: All respondents taking part in Part 1 of the Research (n=51).

* Other includes: premium bonds (2), property, 'paying off my mortgage', investment trusts, 'VCT/ EIS', 'business deals', unit trusts

Few respondents could recall alternative products being discussed as part of the bank/ building society sales process. Rather, they simply recalled the structured product being presented as the best and only solution to their financial needs.

> *"In the discussion they asked what do I want to do with the money? Would I want low, medium or high risk? He said "I've just got this new product which is a guaranteed return". He was friendly, but forceful about the product. He did not offer anything else."*
>
> **Product holder, Medium financial capability, Bank/ BS channel**

The IFA channel experience was a little different as this formed part of a wider review of finances. Here, respondents were also more likely to split their investment across several vehicles such as equity ISAs and bonds in addition to the structured product. Nevertheless, there were a couple of cases where the structured product was the only investment vehicle presented.

Respondents were very receptive to structured products, firmly believing that they will meet their financial needs of a capital guarantee plus the potential for upside. They view structured products as 'low risk', categorising them in the same risk bracket as instant-access savings accounts, premium bonds, fixed term deposit accounts and cash ISAs. Because they see the product as low risk, many felt they did not need to conduct much research.

5. Expectations of Performance

In this chapter we explore respondents' expectations for how well their structured product will perform, either in terms of the returns they expect to receive upon maturity or in relation to an alternative savings product such as a fixed-rate savings bond, and how they reached their conclusions. These insights come from Part 1 of the research, based on in-depth interviews with 52 consumers who had recently taken out a structured product.

5.1 Key findings

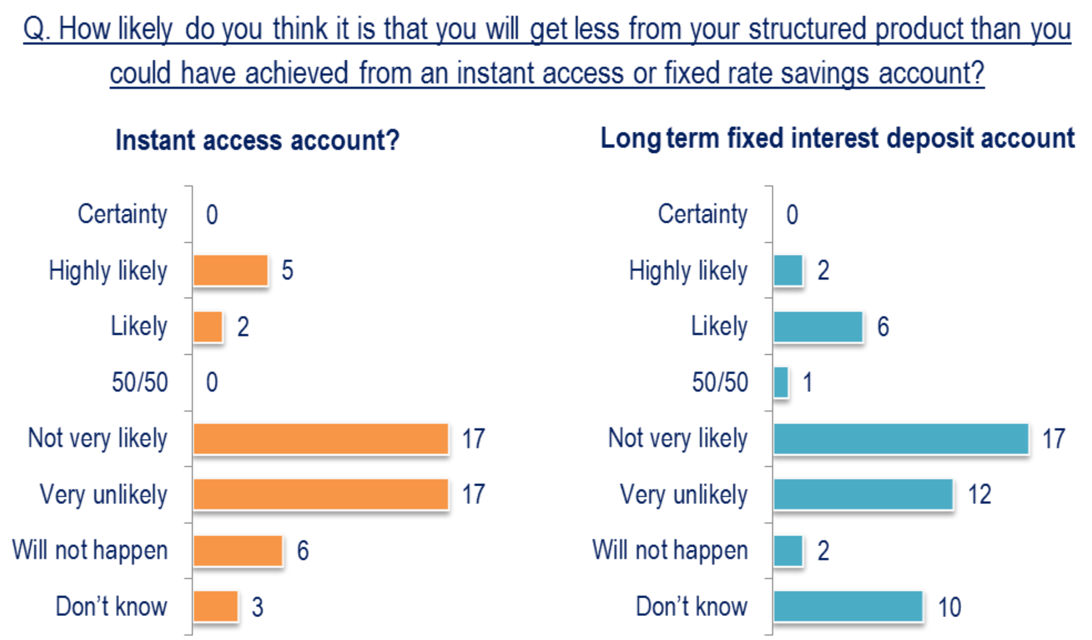
- Respondents expect their structured product to outperform alternative savings products, and would be disappointed if it did not do so. Of particular note, structured products were perceived to offer the potential for higher returns than fixed-term savings bonds, yet with no additional risk to their capital.
- Respondents generally had expectations of returns of around 4%-7% per year for their product, which the current investment climate may struggle to deliver (without dividend income).
- Should structured products fail to deliver more than alternative savings products, our research suggests there could be a large number of structured product holders who would be disappointed.

5.2 Respondents expect their structured products to outperform alternative savings products, and would be disappointed if they did not do so

Despite spending little time evaluating what alternative savings products could offer, structured products were regularly perceived as 'offering the best of both worlds'; the safety of a deposit account but with 'medium' to 'high' potential returns.

The vast majority of respondents dismissed out of hand the possibility that they could earn more from an instant-access savings account than their structured product. Structured products were also deemed to offer the potential for higher returns than longer-term fixed-rate deposits, but respondents were less sure about this assessment as many were not confident in their knowledge of the interest rates on these products or how they will move over the next five to six years.

Figure 7: Most respondents dismissed out of hand the possibility that they could earn more from an instant-access savings account or long-term fixed-interest deposit account



Base: All respondents taking part in Part 1 of the Research (n=50).

These assessments were rarely based on a direct comparison of the relative returns at the time of purchase, but rather on their perception that interest rates on these accounts are "awful" and are unlikely to improve, and that 'stock markets are likely to increase'. Indeed, just nine respondents could give a reasonable explanation of what would need to happen for their product to outperform these alternatives.

> *"I would like to think I'd get another £3,000 to £4,000 on top of the £30,000 I put in. I'm not expecting mega money any more. Looking at what I could get from a bank at the moment, it is nothing near the 10% return I get on my product. 2.5% in a deposit account is rubbish. 10% is much better."*
>
> **Product holder, medium financial capability, Bank/ BS channel**

5.3 Respondents expected returns of c. 4%-7% per year, which the current investment climate may struggle to deliver (without dividend income)

Respondents generally had expectations of returns in the range of c. 4%-7% per year, but few had a firm sum in mind as to what they would expect at the end of their term. Respondents tended to reference what they would expect to earn in a Cash ISA or on deposit account and add a little extra on to that. Just a handful specifically referred to their recollection of their product's features when making this assessment.

> *"I'd like to think I would get more than sticking it in a Building Society, so let's say 6% or 7% in five or seven years. I think I would be disappointed if I got back only what I would have done in a Building Society, as you invest it in stocks and shares to hopefully get something better than you would on the high street."*
>
> **Product holder, Low financial capability, IFA channel**

Most recognised that that the low-risk nature of the product meant that they would not be able to get very high returns, but a small number of respondents had expectations of getting more than 20% return and anything less than this would disappoint. These expectations appear to have stemmed from headline maximum rates that they had seen in the product literature.

> *"I would be hoping for the full 6% per annum on the sum invested. I think 24% is relatively realistic, 30% is what I would hope for and 36% would be the icing on the cake."*
>
> **Product holder, High financial capability, Execution-only channel**

6. Assessing Value for Money

In this chapter, we formally explore how well respondents understand the underlying factors driving potential returns from structured products, and how well consumers understand when they might be better or worse off investing in a structured product versus near substitutes.

6.1 Key findings

- Few respondents had a good understanding of the underlying factors driving potential returns and did not consider likely market levels when making investment decisions.
- The least financially capable do not understand what the FTSE 100 index is, and understanding of volatility is patchy. While respondents did not necessarily have unrealistic expectations for future performance of the FTSE 100 over the next 3-6 years, few were making educated decisions.
- Most respondents understood inflation, but failed to link the impact of inflation on money-back guarantees.
- There were significant failings in consumers' abilities to use their knowledge to assess potential product outcomes or performance. Based on these findings, consumers are likely to need encouragement to make meaningful comparisons.
- When presented with the range of potential outcomes, a significant minority (around one quarter) of structured product holders would choose not invest in any of the structured products on offer. Furthermore, when shown the return from the alternative savings bond, well over half preferred the certainty of the fixed interest rate to the payouts on offer for each structured product.
- Ultimately, consumers are likely to need encouragement to make such comparisons, and the comparison vehicle will need to be very clearly explained, with like-for-like returns in cash terms and percentages.

6.2 Few respondents had a good understanding of the underlying factors driving potential returns and did not consider likely market levels when making investment decisions

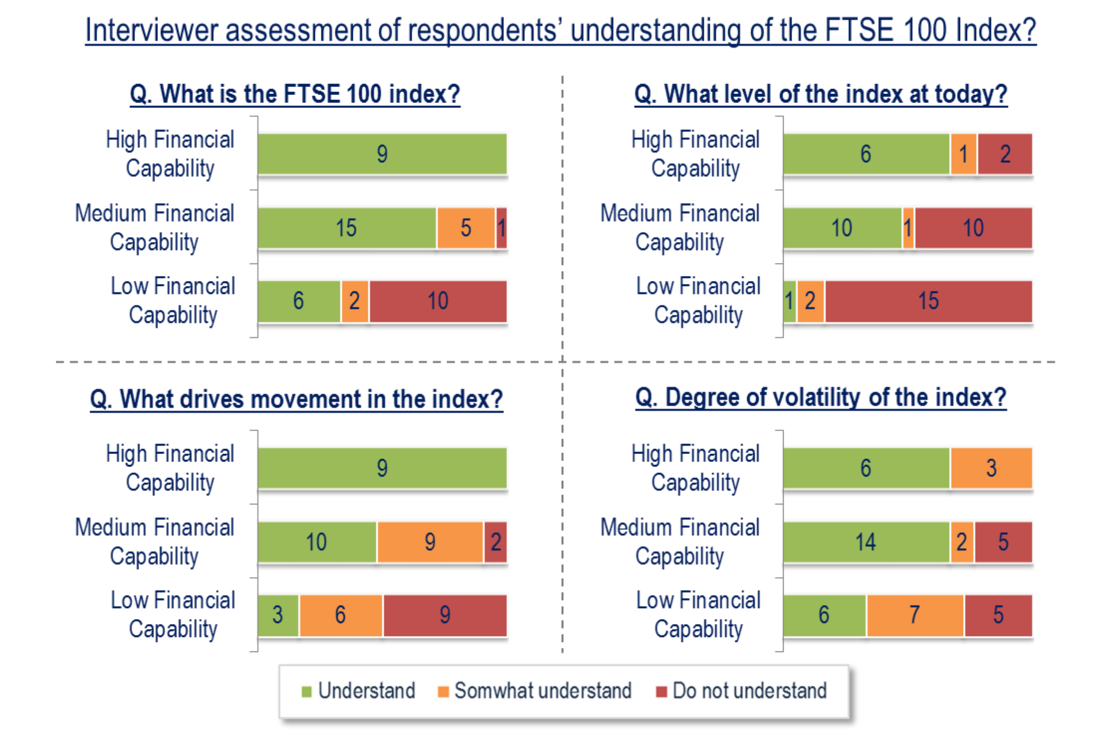
To assess respondents' level of understanding on the underlying factors driving returns, we used a series of open questions and exercises with the 48 respondents who participated in Part 2 of the research, 36 of whom were product holders and 12 were non-product holders who were open to investing in structured products. We evaluated the extent to which consumers understood:

- The FTSE 100 index: as this is usually the underlying index for the most popular structured products on the market;
- Interest rates on instant-access and on five year fixed-term deposits: as these are near substitutes for structured products;
- Inflation: to test whether consumers understand there is an opportunity cost of simply getting their money back and no additional return.

6.2.1 The least financially capable do not understand what the FTSE 100 index is, and their understanding of volatility is patchy

We used a series of questions and exercises to test whether respondents understood what the FTSE 100 index is, whether they take an active interest in the index and whether they understand the volatility that is associated with the index. Our assessment of their understanding is depicted in the graphic over page.

Figure 8: A significant number of respondents did not know what the FTSE 100 index is, let alone be able to talk more broadly about the movements in the index



Base: All respondents taking part in Part 2 of the Research (n=48).

When asked to describe what they think the FTSE 100 index is, one fifth could not give any explanation at all. The vast majority of these were in the low financial capability segment.

> *"I'm not really sure what the FTSE is. I couldn't explain it to you. I have heard of it. Something to do with the percentage you will get back on something."*
>
> **Product holder, Low financial capability, Bank/ BS channel**

Those with medium financial capability were generally able to say that the FTSE 100 index is based on the performance of large UK companies and that it is driven by the economy, but had limited knowledge beyond that. They, too, had some difficulty saying what level the FTSE 100 index is today, but had a much better understanding of volatility.

> *"The FTSE is worked out on how the top 100 companies are doing, that's how I understood it when I was sold the product. I see it on the news, but I don't really pay much attention to it... I wouldn't have a clue what the current level is!"*
>
> **Product Holder, Medium financial capability, Execution-only channel**

Those with a good understanding of the FTSE 100 were typically able to roughly quote its level at the time, but even in this group there were a couple who did not fully understand volatility.

6.2.2 Respondents did not necessarily have unrealistic expectations for future performance of the FTSE 100 over the next 3-6 years, but few were making educated decisions

When we asked respondents to indicate what they expect to happen to the level of the FTSE 100 index over the next three and six years given today's starting point (see Technical Appendix for the research materials used), we found that they did not necessarily have unrealistic expectations. Respondents favoured 7,000 for the value of the FTSE 100 in 3 years (given a starting point of 6,400 at the time of field) and around 7,500 to 8,000 for the FTSE in 6 years, but many respondents reported that making such predictions was way outside their comfort zone and admitted that they were simply making guesses.

"*The exercise is quite difficult, because I do not pay much attention to it and I don't know what the highest point of the FTSE has been.*"

Non product holder, Low financial capability

6.2.3 Few understand the impact of market timing on the potential payouts

When asked to give examples of when might be a good time to invest in a structured product, respondents regularly said that they would invest only when markets had been rising and would not invest when the markets were low or falling.

Few structured product holders taking part in these exercises said that they had actively been thinking about how the FTSE 100 index would perform when taking out their product.

6.2.4 Most respondents failed to link the impact of inflation on money-back guarantees

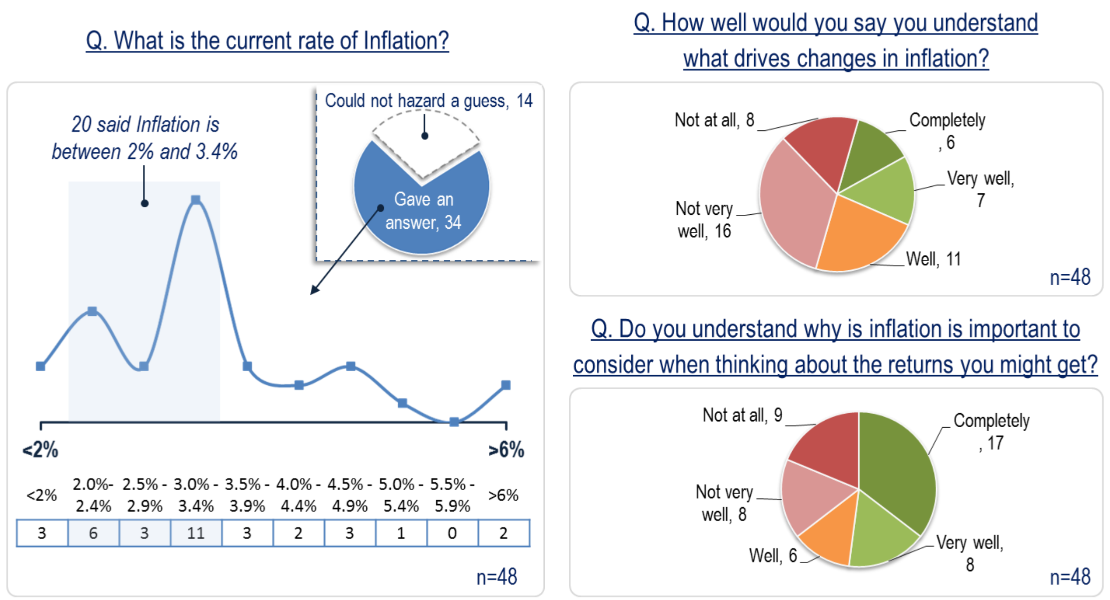
Most respondents had some understanding of what inflation is and could say why inflation is important when thinking about savings at a conceptual level, but a significant minority (just under a third) could not give a good explanation.

However, many more failed to explicitly link inflation to the return they can get on their investment and failed to make the connection that a simple capital return or low return would actually result in a loss in real terms and admitted that this was not something they had factored in to their decision making.

> *"I don't take the inflation rate into account, one should factor in, but I don't think people do."*
>
> **Product holder, Medium financial capability, IFA channel**

This suggests that, while structured products are meeting respondents' underlying financial priority by guaranteeing their initial capital, respondents are often overlooking the impact that inflation could have on capital erosion and, therefore, overestimating the value of the capital guarantee.

Figure 9: While most respondents had some understanding of what inflation is and could say why inflation is important when thinking about savings at a conceptual level, they often overlooked the impact that inflation could have on capital erosion



Base: All respondents taking part in Part 2 of the Research (n=48).

6.2.5 Respondents had a good grasp of current interest rates and were much more comfortable making predictions about future rates

Respondents had a much better grasp of current interest rates available in the market, with most giving reasonable estimates of what they could get on both instant-access and fixed-term savings accounts. Indeed, poor interest rates were one of the key drivers for looking to do something different with their money.

Interest rates for instant-access savings accounts were typically described in derogatory terms (such as 'rubbish', 'next to nothing', and 'peanuts') and five year savings bonds were seen as not much better. When thinking about these levels, respondents often recalled past returns on savings of 6% to 7%, and some referred to the 1980's when notional interest rates were double digit. When asked about their expectations for interest rates in the future, the consensus was that base rate would stay the same for the next couple of years at least and then "creep up" to around 3%.

6.3 There are significant failings in consumers' abilities to assess potential product outcomes or performance, particularly when compared to fixed-interest savings products

Respondents were asked to describe situations when they might be better or worse off investing in structured products rather than putting their money into fixed-term fixed-interest saving products. Most respondents could not accurately assess the likely performance of their product because they did not know what their investment return is based on. While most were optimistic they will get back more than their original investment, many of the less financial capable respondents did not understand what would need to happen for this to occur.

The majority could recall seeing examples of potential returns prior to taking out their product, but these either consisted of an adviser talking them through past performance or a comparison of what returns they would get under different economic scenarios. Not everyone found these easy to understand.

Respondents in our research could not give very coherent responses to when they might be better or worse off investing in structured products rather than putting their money into deposits or equity-based investments. This again suggests that there are significant failings in consumers' abilities to assess potential product outcomes or performance.

6.4 A significant minority may not have taken out their structured product if presented with the potential outcomes they could achieve

6.4.1 Research methodology

We created an exercise to test how consumers' assess value in structured products against product substitutes and where this notion of value comes from. Respondents were asked to imagine they had £10,000 to invest and were looking to invest for a five year period. They were asked to look at four different hypothetical structured products in turn. Each product had a different range of potential outcomes that could be achieved on maturity and a probability attached to that return being triggered. Respondents were reminded that all four products guarantee to return at least their initial capital at the end (i.e. no risk of capital loss). We then asked respondents to rate each of the products and say how likely they would be to invest a small, medium or large amount of their own money into the product, if it was available in the market today.

Figure 10: Value for Money Exercise showcards: 4 (hypothetical) Structured Products

Part 1 Value for Money Showcards (Scenario Set 2)

You have £10,000 to invest and you are looking to make an investment for 5 years. There is no risk of capital loss. The columns show the different levels of interest that could be triggered on maturity, the probability of the return being triggered, and what this equates to in cash terms.

Scenario 1

Total amount of interest	Total amount paid back on maturity	Probability
10%	£11,000	5 out of 10
11 – 15%	£11,100 - £11,500	3 out of 10
16 - 20%	£11,600 - £12,000	2 out of 10

Scenario 2

Total amount of interest	Total amount paid back on maturity	Probability
0%	£10,000	2 out of 10
10%	£11,000	3 out of 10
15%	£11,500	2 out of 10
20%	£12,000	2 out of 10
25%	£12,500	1 out of 10

Scenario 3

Total amount of interest	Total amount paid back on maturity	Probability
0%	£10,000	4 out of 10
1 – 10%	£10,100 - £11,000	2 out of 10
11 – 20%	£11,100 - £12,000	1 out of 10
21 – 30%	£12,100 - £13,000	1 out of 10
31 – 42%	£13,100 – £14,200	2 out of 10

Scenario 4

Total amount of interest	Total amount paid back on maturity	Probability
0%	£10,000	5 out of 10
25%	£12,500	5 out of 10

The four hypothetical products were constructed to give roughly the same average payback, but each had a different payback shape. These outcomes (the range of potential outcomes and probability attached to them) were provided by the FCA's technical team and full details can be found in the Technical Appendix. As a summary:

- *Product Scenario 1* offered a minimum guaranteed return of 10% and a maximum return of 20%, with a 2 in 10 chance of achieving this.
- *Product Scenario 2* introduced the possibility of no payback at the end of the five years (which would happen 2 in 10 times), but a maximum return of 25%, with a 1 in 10 chance of achieving this.

- *Product Scenario 3* increased the chance of that no payback would be achieved at the end of the five years (4 in 10 chance of this happening) and increased the maximum return possible to 42%, with a 2 in 10 chance of achieving this.
- *Product Scenario 4* offered a 5 in 10 chance of making a 25% return, and a 5 in 10 chance of no return at the end of five years.

After reviewing the four hypothetical structured products in detail, respondents were then shown the compounded returns from a five year Fixed-Rate Savings Bond. Respondents were asked to revisit their original assessments to say whether they would choose to invest in the structured products or the alternative savings bond.

Figure 11: Value for Money Exercise showcards: Alternative Savings Bond

Part 2: Alternative Savings Bond Showcards (Scenario Set 2)

(Revealed at the end of the exercise)

Alternative: 2.35% interest per year

During your discussion with the adviser, they talk to you about an alternative savings product that could be suitable for you.

This product is a fixed term fixed interest savings bond. Again, you have to invest for 5 years.

You will be paid an interest rate of 2.35% each year.

As an alternative you could invest in:

A 5 year term fixed interest savings bond paying 2.35% interest per year.

WHICH EQUATES TO A PAYOUT OF:

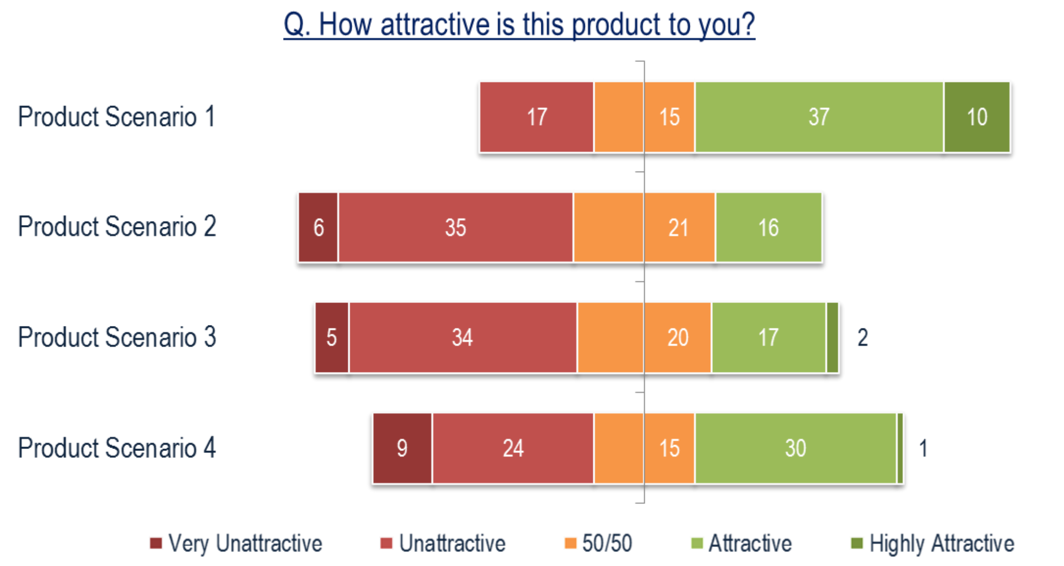
Total amount of interest	Total amount paid back on maturity	Probability
12.3%	£11,231	10 out of 10

6.4.2 A significant number of respondents found all of the structured product scenarios unattractive, and were surprised by what they deemed to be poor payouts

The Value for Money Exercise suggests that a significant minority of structured product holders may not have selected their product if presented with the potential outcomes they could achieve. Indeed, when first presented with these potential outcomes (prior to the reveal of the alternative savings bond), many said they were unattractive and some were surprised by what they deemed to be poor payouts.

> *"Well, that's only slightly better than a savings account…"*
>
> **Product holder, Low financial capability, Bank/BS channel**

Figure 12: Many respondents rated the hypothetical structured products in our Value for Money Exercise as unattractive or very unattractive



Base: Structured product holders (n=79).

6.4.3 *Product Scenario 1* was favoured as it offered a minimum guaranteed return

Of the four products presented, *Product Scenario 1* was favoured as it offered a minimum guaranteed return, with the potential to earn a little bit more. This is perhaps not surprising given the majority of respondents were generally very risk adverse. Those that liked *Product Scenario 1* focused on the fact that they would get something more than their original investment back and 10% seemed quite reasonable as a minimum, which a couple worked out to be roughly equal to 2% a year.

> *"Very attractive, even if I just made a grand I would be happy and it would be a bonus if I was one of the three out of ten people… yes very attractive."*
>
> **Product holder, Low financial capability, Bank/BS channel**

In contrast, those that found *Product Scenario 1* unattractive were typically scathing about the low rate of return on offer for tying their money up for 5 years. Some had expectations of a return of 5% to 6% per year annum on their product and were surprised by the low rates of return on offer in our hypothetical exercise.

"Well that's only slightly better than a savings account, (where) you are probably only getting 1% - maybe a bit more if you shop around. After 5 years you could maybe compound to 10.5%. So, a 20% chance for £2,000 over 5 years, it's not a big enough (return). If that figure was higher, I might take a gamble."

Product holder, Low financial capability, Bank/ BS channel

Product Scenario 2 and *Product Scenario 3* were less well liked overall as they introduced a possibility of making no return and most respondents felt that the increased upside was not enough to outweigh the risk of making no return at the end of the five year period. Yet these payback shapes are commonly seen in the market.

"So, I have a 20% chance of gaining zero and the same chance of gaining 15% or 20% and a 30% chance of gaining 10%. And this is over 5 years? That's going to be lower than a bank (account) at 2% a year. If I was going to get the highest probability it would work out at 2% a year, but there is an equal chance of me getting nothing back as there is for getting 15% or 20%... I don't really see that as fun!"

Product holder, Medium financial capability, IFA channel

"Well, it's riskier this, a bit too risky. I have been thinking that I'd be one of the 4 out of 10 (that gets no return), so that's not attractive."

Product Holder, Low financial capability, Bank/BS channel

In contrast, those that like these two products focused exclusively on the upside potential. In particular the 42% maximum payout on offer in *Product Scenario 3* caught their eye.

"A 40% chance of not getting anything at all is not very attractive. Then again, I am interested in the 42% (maximum payout). That does look quite attractive over the term."

Product Holder, High financial capability, IFA channel

Product Scenario 4 was seen as a "gamble" and appealed to the more risk loving respondents, saying "it's a red or black moment", "I'd do it just for fun", or "it's safer than a lot of things I do". Risk adverse respondents typically reactive negatively to this product, although it was often favoured over *Scenarios 2* and *3* as the outcomes were "easier to understand".

"It isn't really me - a 50% chance of getting nothing and 50% chance of getting a decent return. I might as well have a bet with you on it! It does depend on where you got the money, if you got it from a bonus then you might as well have a go on it or I would be more inclined to do it, given that it is an inheritance then I would be less inclined to do it, so I'm going to say very unattractive - very unlikely to do it."

Product Holder, High financial capability, IFA channel

"Well, it's red or black at the casino, nice and straight forward, nice and simple. It's probably my favourite of them as it is nice and simple."

Product holder, High financial capability, IFA channel

6.4.4 A large proportion of respondents preferred the returns from the fixed-rate bond in each scenario rather than the structured product

When shown the alternative of putting their money in a fixed-rate fixed-term savings bond paying 2.35% per year, many respondents were surprised that 2.35% - seen as a 'pittance' in the earlier discussion - would deliver returns of 12.3% once compounded over the five years.

"Not bad is it. With my limited knowledge of interest rates and compounding and things like that (it is a surprise). It does seem a lot more attractive when you are quoting figures like that."

Product Holder, Bank Channel, Mid Savviness

Once they saw the counterfactual returns from the savings bond, a significant minority preferred the certainty of the fixed-interest rate that the bond offered to any of the four structured products.

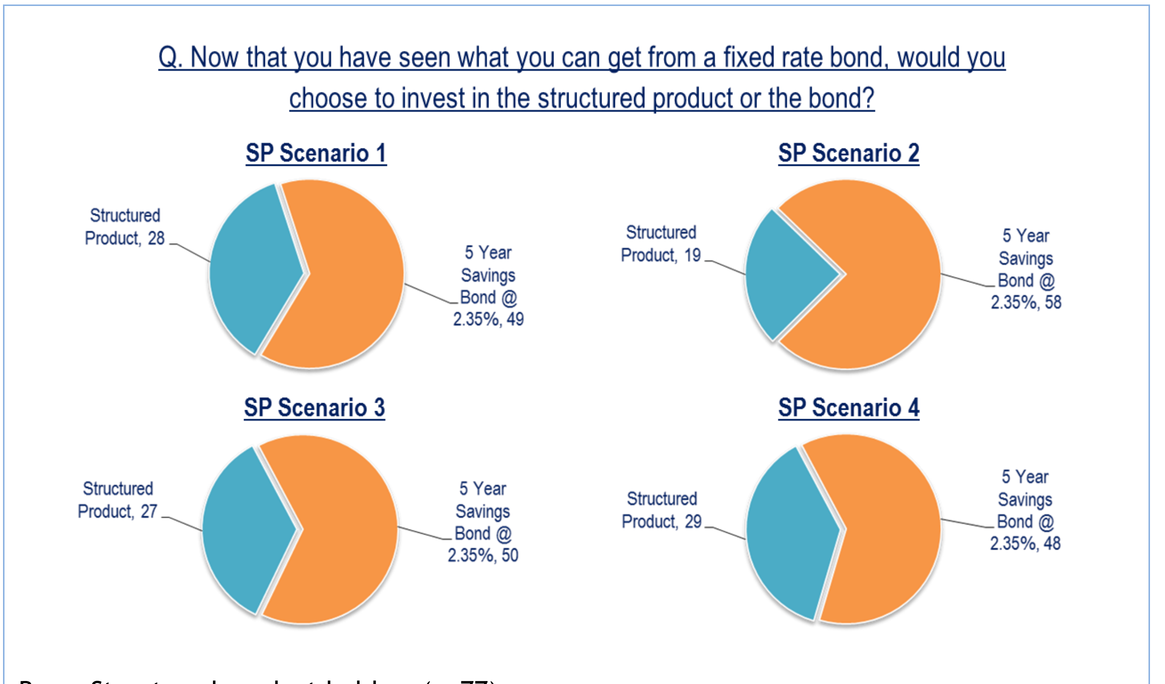
Of the four structured product scenarios, *Product Scenario 1* held up relatively well with a third saying they would choose to invest in it over the savings bond. Some felt that the minimum 10% return it offered was sufficient to take the chance of getting a higher return, even if that higher return was unlikely to be significantly better. Others felt the 'reveal' had simply reinforced their perceptions of the poor interest rates available on savings products in general, and many were also pretty dismissive of the our structured product payback scenarios too. These respondents were willing to take a chance for a higher return.

Three quarters said they would choose to invest in the savings bond over *Product Scenario 2*. Respondents liked the certainty of the payback offered by the bond and felt that the difference between what they could get at the upper end of the distribution in *Product Scenario 2* was not high enough to compensate for the risk of making no return.

Despite initially being the least popular, the structured product in *Product Scenario 3* actually performed slightly better against the savings bond, with one in three saying they would choose to invest in it rather than the savings bond. In fact, some respondents who had previously said the product did not offer value for money subsequently opted for it over the bond. Here respondents were almost solely focused on the top end return of 42%.

Four in ten said they would choose to invest in the *Product Scenario 4* over the savings bond despite it being seen as a "gamble". While it tended to appeal to the less risk adverse respondents, there were also some real outliers where very risk adverse respondents chose the structured product because the outcomes were easier to understand.

Figure 13: A significant minority may not have selected their structured product if presented with the potential outcomes they could achieve and the outcomes associated with an alternative product



Base: Structured product holders (n=77)

6.5 Information will be required at the point of sale, but will need to be carefully presented and explained

Our findings suggest that, left to their own devices, few structured product customers actively make meaningful comparisons between substitute products and that, for many, this type of analysis is outside of their comfort zone. We found little evidence that this type of exercise systematically forms part of the sales process today, suggesting that a more formal comparison process may be needed at the point of sale to help customers make more informed decisions.

We also found that when consumers are given explicit comparisons of potential product outcomes with common product alternatives they make different decisions. However, our research highlighted that there are significant failings in consumers' abilities to assess whether a product is going to deliver value for money. As a result, such information will need to be delivered in a careful way to cater for all levels of ability. Comparison vehicles will need to be clearly explained, and include like-for-like returns in both cash terms and percentages.

Common misunderstandings that came to light in our research included:

- Not knowing what a probability is, or failing to understanding percentages.
- Choosing a single outcome, rather than understanding that there are a range of outcomes possible.
- Discounting the set probabilities attached to the outcomes, either for emotive reasons (e.g. 'knowing my luck, I would be the person who would get x%') or due to their own beliefs on how the markets will perform (e.g. 'what with the markets at the moment, you will most likely end up with x%).
- Struggling to convert five year returns back to an annual figure or making realistic comparisons between a five year return and an annual interest rate. For example, many respondents said that a guaranteed return of 10% was attractive, but earlier discussed 'pitiful' interest rates of 2% to 3% per year on savings accounts.
- Focusing on the upper limit when presented with an outcome expressed as a range (such as 30% to 42%), rather than the range of outcomes possible or the lower limit.
- Gravitating towards *Product Scenarios* that had fewer outcomes, because they were easier to understand rather than because they offered better outcomes.
- Being unable to perform percentage calculations when thinking about expected returns, resulting in a discrepancy between the annual rates of return and the cash sums they would want to get at maturity.

7. Product Complexity

Structured products often have a combination of features that impact upon the potential payout, such as kick outs, caps, averaging and reference indexes. The FCA is concerned that customers may be unable to understand individual product features and that there may be a critical mass of features that, when combined, mean understanding is not achievable.

In order to explore these concerns, respondents were asked to read showcards describing five hypothetical structured products. Each structured product included a different combination of features available in the market, building from a plain vanilla product to one containing multiple features:

- Product 1: Basic Deposit Product, based on FTSE 100 Index, 100% of FTSE upside, no cap.
- Product 2: Basic Deposit Product, based on FTSE 100 Index, 100% of FTSE upside, capped at 30%.
- Product 3: Basic Deposit Product, based on FTSE 100 Index, with Kick Out.
- Product 4: Basic Deposit Product, based on FTSE 100 Index, with capped upside of 30% and a minimum return of 10%, calculating the final Index using averaging over a year.
- Product 5: Cliquet product based on FTSE 100 Index.

Respondents were asked to complete a number of exercises to test comprehension and moderators corrected any misconceptions to replicate an advised sale.

7.1 Key findings

- Respondents had a good understanding of basic product features and where structured products fit in the investment landscape.
- Many struggled to physically calculate the returns structured products would deliver, typically due to poor mathematical abilities.
- The Kick Out feature was commonly misinterpreted.
- The averaging feature was generally well understood.
- The basic concept of a Cliquet product was understood, but many missed that gains could be offset by the losses to deliver a zero return.
- Respondents struggled where products had more than two complex features.

7.2 Respondents had a good understanding of basic product features and where structured products fit in the investment landscape

At a basic level, respondents understood how structured products differ to a direct investment in an index or fixed-term deposit. In our exercise, the features set out in the basic deposit products (*Product 1* and *Product 2*) were felt to be straightforward to understand. However, even here, there were areas of difficulty. In particular, respondents struggled to physically calculate the returns these structured products would deliver under different FTSE 100 growth scenarios, typically due to poor mathematical abilities, especially when working with percentages. Across all respondents asked, almost half made at least one error calculating the returns.

Figure 14: The features set out in the basic structured deposit products were felt to be straightforward to understand, however, even here there were areas of difficulty

Q. How does a Structured Product differ to a direct investment in an index (equity ISA)?

What they understood

- ✓ SPs guarantee to return your initial capital.
- ✓ SPs require you to lock your money away for a set period of time and are harder to exit.
- ✓ Equity ISAs can go up or down.
- ✓ ISA are more flexible as you pick how risky you want it to be – SP is given to you.

What they did not understand

- x How the returns would be calculated.
- x No dividends paid on SP (only mentioned by 2).
- x How an equity ISA works (5 did not know what an equity/ stocks and shares ISA is).

Q. How does a Structured Product differ to a fixed term deposit account?

What they understood

- ✓ SPs do not pay a fixed interest rate per year (and as such could there is an element of risk).
- ✓ Both guaranteed to give you at least your money back and both lock money away for a set period.
- ✓ Both are usually lump sums.
- ✓ You could do better in a SP.

What they did not understand

- x Impact of inflation.
- x Return might be less on SP than the deposit.
- x Costs.
- x Deposit rates can change during the fixed term.

Base: All respondents taking part in Part 2 of the research (n=48)

Respondents could easily identify some possible benefits of structured products over alternatives, such as that they guaranteed to return their initial capital whereas equity investments do not, or that they offer the potential for greater upside compared to a savings account. While most could identify some risks associated with structured products, such as the potential to realise poor returns or that there may be a penalty if they exit early, the less financially capable struggled to identify any risks, often referring to structured products as offering the "best of both worlds".

Figure 15: While most could identify some benefits of structured products, the less financially capable struggled to identify any risks

Q. What are the benefits of Structured Products?

- Safe – initial capital protected (18 mentions).
- Better returns than a savings account (14 mentions).
- Good returns potential (11 mentions).
- Lock money away for a set time (7 mentions).
- Linked to the stock market (7 mentions).
- Easy to calculate what you will get (3 mentions).
- Wrappable in an ISA (3 mentions).
- "You can't lose" (2 mentions).

Other mentions include: 'less of a gamble than an equity ISA', 'easy access', 'long term opportunity', 'something a bit different', 'low risk', 'guaranteed return', 'a gamble', 'none'.

Q. What are the risks?

- Potential to get poor returns or just your initial capital back (14 mentions).
- No access to your money/ hard to exit/ possible penalty should you exit early (11 mentions).
- No risks – 'you can't lose' (10 mentions).
- Inflation risk (6 mentions).
- Product risk – opportunity cost of doing something else (4 mentions).
- What would happen if the provider went bust? Are you guaranteed to get your money back? (4 mentions).
- Your returns are unknown until the product matures (3 mentions).

Base: All respondents taking part in Part 2 of the research (n=48)

7.3 The kick-out feature was commonly misinterpreted with consumers generally over-estimating the likelihood that it would reach maturity

The kick-out feature in *Product 3* was initially not well understood. Half of all respondents did not understand this product when they first read it, commonly believing that it would give them a percentage return each year, and/or that it was their choice to stay in the product if the kick-out event occurred. Respondents also failed to pick up how little the FTSE 100 index needed to grow by for them to be kicked out.

As a result the product was often described in very positive terms, with respondents overestimating the likelihood that it would run to maturity and deliver maximum returns (which in our example was 50% at the end of 5 years).

> *"I like it. It pays you if the FTSE stays same. If it is higher, you get 50% and a 'kick-back' at years two, three, and four. It is definitely attractive."*
>
> **Product holder, Medium financial capability, IFA channel**

Once the kick-out feature was explained in detail by the interviewer, a number of respondents expressed surprise that the FTSE 100 only had to grow a little for them to be kicked out. Most now said that it was likely they would be kicked out at year two or three. Attractiveness scores fell considerably as a result.

7.4 The averaging feature was generally understood, but consumers failed to recognise that there could be downsides

The principle of averaging in example *Product 4* was generally understood by respondents of all financial capability levels. Occasionally, respondents thought that the averaging would be carried out over the whole five year period rather than the last 12 months, but this was the exception rather than the rule.

When thinking about the potential impact of averaging, respondents recognized how averaging could cushion them from a fall at the end of the product's term, but did not necessary identify circumstances where averaging could make them worse off, such as in a rapidly rising market.

7.5 The basic concept of a cliquet product was understood, but many missed that gains could be offset by the losses to deliver a zero return and could not give a good assessment of the possible payout

From the description alone, respondents understood many of the basic features in example *Product 5*, in particular that it is a three year investment, there are six periods when the FTSE 100 index is recorded, there is a cap on the total rise and fall in the FTSE 100 index in each period, that they might only get their money back, and that there is a maximum 42% payout. However, many misunderstood how the calculation is made, and how the cap works.

Unprompted, the vast majority did not recognise that the netting process could lead to them getting just their money back. Once explained, this feature was quite well understood, but even after explanation, few could articulate why this netting process was in place, and under what circumstances this could be beneficial for them.

Given a range of possible payouts from 0% to 42% in this product example, most respondents simply hazarded a guess somewhere around the midpoint. Few were able to think deeply about likely payouts. Despite the attraction of the headline maximum figure, none said that they thought it was likely they would achieve this payout.

7.6 Respondents started to struggle where products had more than two complex features in combination

The combination of features in *Product 4* often required at least five minutes of explanation by the moderator to get respondents to a reasonable level of understanding. In particular the wording of the 10% minimum was very confusing and respondents took a little time to work out how the averaging would work in practice. As a result, many missed the cap altogether as they had got so tied up in trying to understand the previous two features.

A significant number (just under a third) reported that the combination of features was now starting to get too much, and that they had switched off at this point. These tended to be those with low to moderate levels of financial capability.

From this exercise, it appears that there is a critical mass of features that when combined mean understanding is not achievable. For this reason, providers will need to be mindful when constructing products to consider the consumer's ability to take on board multiple features, and such products will need careful explanation and wording.

8. Technical Appendix

8.1 Achieved Sample

Figure 16: Research sample

		Structured Deposit	Structured Investment	Non Product Holder	TOTAL
Number of F2F interviews		**54**	**33[2]**	**12**	**99[3]**
Distribution Channel	IFA	20	12	-	32
	Bank[1]	26	17	-	43
	Execution Only	8	4	-	12
Age	<45	8	7	-	15
	45-54	13	26	3	42
	55-64	14	9	5	28
	>64	6	4	4	14
Financial Capability	High	10	9	-	19
	Medium	27	13	3	43
	Low	17	11	9	37
Gender	Male	33	19	5	57
	Female	21	14	7	42

[1]Bank includes banks, building societies and direct salesforce.

[2] Includes 3 SCARP product holders.

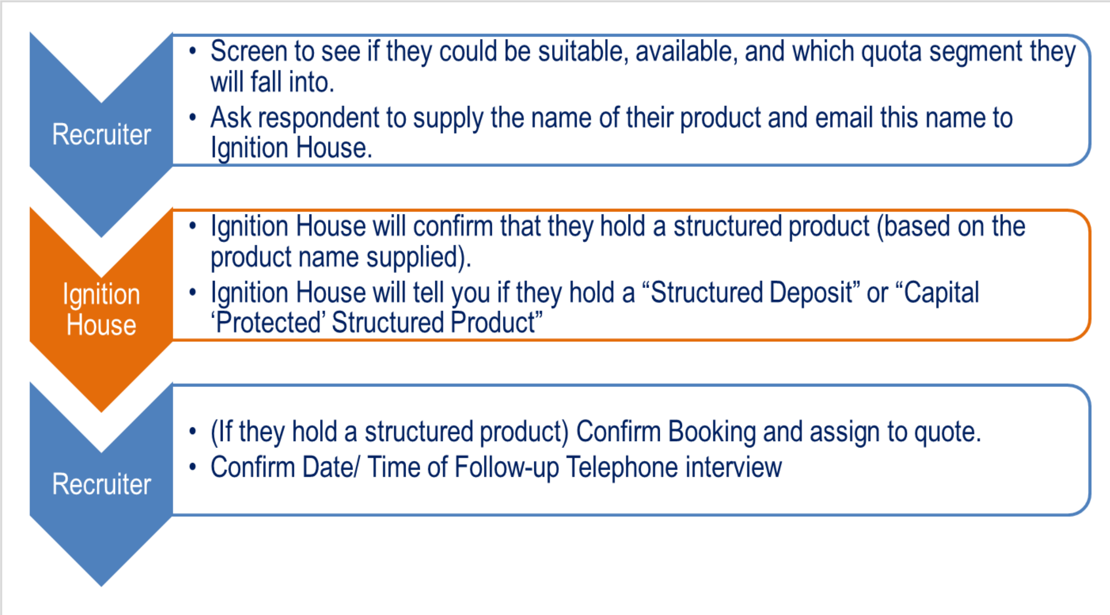
[3] One interview discounted from the analysis.

8.2 Recruitment Screener

For Product Holders we are following a 3 Step Recruitment Process

We are following a 3 step process for this project. This is depicted in the graphic below. The rationale for this 3 step process is as follows:

- Respondents may not be sure if they hold the product we require for this project (structured products are typically not called structured products).
- Further, if we recruited only those respondents that knew the product they had was a structured product, we risk skewing the research towards more financially savvy consumers.



Potential respondents who do not fit the criteria for Part 1 (Customer Journey Research) may be suitable to take part in Part 2 (Exercise Research), subject to quota.

STEP 1 - SCREENER

1.1 Introduction/ General Screener

I am working on behalf of Ignition House, an independent research company. We are carrying out some research on behalf of a large financial services organisation. The research involves talking to customers like you about the decision-making process surrounding a certain type of savings product.

The interview will last for around an hour. We will ask that you complete a short (no more than 20 minutes) exercise at home before the session. In addition, one of the Ignition House directors or senior interviewers **may** call you after the interview to ask about your thoughts once you have had time to reflect on what was discussed in the interview.

If you are able to help with the research, we would arrange for you to come to {LOCATION} where one of the directors or senior interviewers at Ignition House will conduct the interview at a time that is convenient for you.

{INSERT LOCATION & DAYS}

Ignition House is completely independent and the research is confidential.

IF WILLING, PROCEED TO CHECK CRITERIA

Q.1 Screening out people who work for a FSI or work in journalism/media/PR.

a) **Please could you tell me do you currently work or have worked in journalism/media/PR? (IF Yes - CLOSE)**

b) **DO NOT ASK IF INDIVIDUAL ALREADY EXCLUDED at Q1a: Does your partner/spouse/any other close relative work in journalism/media/PR or have they done so in the past? (IF Yes - CLOSE)**

c) **Do you work currently for any financial services institution?**

- IF WORK IN FSI: Are you a financial adviser or involved in selling financial services and investments? **(IF Yes - CLOSE)**
- IF WORK IN FSI: Do you work for a financial services provider, such as a bank or building society? (IF YES – check whether this is a general insurance company, if NOT EXCLUDE).

Q.2 Screening out non-financial decision makers

When you are thinking about choosing financial products and services such as pensions and investments, which of the following statements best describes how you normally go about deciding which product to take out? **READ OUT**

1. I am the sole decision maker (IF MENTIONED CAN BE WITH SUPPORT OF FINANCIAL ADVISER].
2. I discuss things with my partner, but I tend to make the final decision (IF MENTIONED CAN BE WITH SUPPORT OF FINANCIAL ADVISER].

3. I make decisions jointly with my partner (IF MENTIONED CAN BE WITH SUPPORT OF FINANCIAL ADVISER]
4. I discuss things with my partner but they tend to make the final decision. (CLOSE)
5. I leave it all up to my partner/someone else (CLOSE – BUT ENSURE ANY 'CLOSE' HERE IS NOT BECAUSE THE 'SOMEONE ELSE' IS A FINANCIAL ADVISER)

ALL RESPONDENTS MUST BE FINANCIAL DECISION-MAKERS TAKING RESPONSIBILITY FOR THE DECISION I.E. ALL MUST CODE 1, 2 or 3.

Q3 Can I just check, which of the following would you usually do:

a) **Manage your own money**

b) **Manage household finances (either individual or jointly)**

c) **Pay some household bills**

ALL REPONDENTS MUST ANSWER YES TO ALL QUESTIONS

1.2 Product Holding Screener

I'm now going to read out a description of a financial product: READ OUT

There are certain types of products in the market which are taken out for a set period of time (usually 5 or 6 years) and have the following features:

- Capital is protected, so at a minimum investors will receive back the money that they have invested at maturity
- The return on the investment is calculated using a set formula which investors are told in advance. This formula is usually linked to the performance of a separate measure like the FTSE 100, inflation or Halifax House Price Index.
- The final amount of interest paid at the end of the product is not fixed. There may be a chance of getting no return, or a minimum return at the end of the product.

Products are supposed to be held for the fixed term and it is not easy to exit them early.

Q4. Do you think you have an investment product the meets this description?

[Note to recruiters: These products are sold under many different marketing names, including: Structured Cash ISAs, Growth Deposit plans, Guaranteed Capital Plans, Guaranteed Stock Market Bonds, Protected Investment Funds, Guaranteed Income Bonds, Index Bonds, Guaranteed Equity Bonds. The main product providers are: Investec; Barclays; L&G; Morgan Stanley; RBS; Santander; Meteor Asset Management; Gilliat Investor Solutions; Credit Suisse. Building Societies also distribute the products including – Nationwide, Yorkshire BS, Barnsley BS, Newcastle BS, Leeds BS etc.]

Q4a. Can I just check, when did you take this product out roughly?

Q5. Can I just check, which financial services company is this with?

Q5a. Is it through National Savings and Investments?

- IF YES TO Q4 AND NO TO Q5a: POTENTIALLY ELIGIBLE FOR PART 1 OF THE RESEARCH – CONTINUE SCREENER
- IF RESPONDENT HOLDS PRODUCT BUT HAS HAD IT FOR MORE THAN ONE YEAR CONTINUE SCREENER AND ALLOCATE TO PART 2 OF THE RESEARCH (CHECK PRODUCT HOLDER QUOTA)
- IF NS&I PRODUCT HOLDER CONTINUE SCREENER AND ALLOCATE TO PART 2 OF THE RESEARCH (PRODUCT HOLDER)
- IF NOT A PRODUCT HOLDER, GO TO Q9 (QUOTA NON PRODUCT HOLDERS PART 2)

ASK PRODUCT HOLDERS ONLY (PART 1 QUOTA OR PART 2: PRODUCT HOLDER QUOTA)

Q6. How did you take out this product?

1. A member of staff at a bank or building society told me about the product and its features and I took it out straight away.
2. I had a longer conversation with a member of staff at a bank or building society about the product, my personal circumstances and other products that I held. I was told the product was suitable for my needs.
3. It was recommended to me by an IFA.
4. I bought it myself without any advice from anyone (e.g. by post, from the internet, responded to an advert, other (please specify).
5. I have a discretionary fund manager, and they arranged it on my behalf (SCREEN INTO PART 2: PRODUCT HODLER QUOTA)

6. Don't know, can't remember (SCREEN INTO PART 2: PRODUCT HOLDER QUOTA).

Q7. Can I just check, did the money for this investment come from a similar product that had recently matured, or was about to mature? Yes/No

Q8. And does this investment product account for a small, medium or significant part of your savings and investments portfolio?

1. Small part of my savings and investments portfolio
2. Medium part of my savings and investments portfolio
3. Large/ significant part of my savings and investments portfolio

ASK NON PRODUCT HOLDERS ONLY

Q9. How would you feel about this type of product - would you consider investing in something like this (conceptually)?

ASK AS AN OPEN QUESTION. EXCLUDE RESPONDENTS WHO ARE VERY NEGATIVE AND WOULD NEVER CONSIDER INVESTING

1.3 Financial Capability Questions

Q10. To start, I am now going to read some statements and I'd like you to tell me how much you agree or disagree with them, where 5 means strongly agree and 1 means disagree strongly?

	Disagree strongly	Disagree slightly	Neither agree nor disagree	Agree slightly	Agree strongly
Q10a: I regularly check out financial information in newspapers, magazines or on the internet.	1	2	3	4	5
Q10b: I feel confident handling my own financial affairs.	1	2	3	4	5
Q10C: I think I am knowledge about financial issues and products.	1	2	3	4	5

- If they score ‘1’ on any question – code as LOW FINANCIALLY SOPHISTICATED
- If they score ‘1’ or ‘2’ on all questions – code as LOW
- If they score ‘4’ or ‘5’ on all questions – code as HIGH
- All others code as MEDIUM

Q11. Which of the following best describes your attitude to risk?

1. You are not comfortable with the thought of investing in the stock market and would rather keep your money in the bank.
2. You are prepared to take only a small amount of investment risk and it is important to you that your capital is protected
3. You are prepared to take a limited investment risk in order to increase the chances of achieving a positive return but you do not want to risk your capital to achieve this.
4. You are prepared to take a moderate amount of investment risk in order to increase the chance of achieving a positive return. Capital protection is less important to you than achieving a better return on the investment.
5. You are prepared to take a substantial degree of risk with your investment in return for the prospect of the highest possible longer term investment performance.

- FOR PRODUCT HOLDERS (FOR EITHER PART 1 OR PART 2 OF THE RESEARCH) – JUST CAPTURE RESPONSE.
- FOR NON-PRODUCT HODLERS (FOR PART 2 OF THE RESEARCH) - IF THEY ANSWER 1 OR 5 THANK AND CLOSE.

1.4. Classification Details

Thank you, I would now like to ask you some classification questions.

Q.12 OCCUPATION OF HEAD OF HOUSEHOLD: ______________________________

HIGHEST QUALIFICATION LEVEL: ______________________________

TYPE OF INDUSTRY EMPLOYED IN: ______________________________

Q.13 WORKING STATUS OF RESPONDENT (IF NOT HEAD OF HOUSEHOLD):

1. FULL TIME
2. PART TIME
3. NON WORKING
4. STUDENT
5. RETIRED

Q.14 OCCUPATION (IF NOT HEAD OF HOUSEHOLD): ______________________

TYPE OF INDUSTRY EMPLOYED IN: ______________________

Q.15 SOCIAL CLASS:

1. A
2. B
3. C1
4. C2
5. D
6. E

Q.16 AGE OF RESPONDENT: _____

Q.17 MARITAL STATUS:

1. SINGLE
2. MARRIED
3. WIDOWED
4. DIVORCED
5. CO-HABITING

Q.18 CHILDREN:

1. LIVING AT HOME: ______ (AGES)
2. NOT AT HOME -______ (NUMBER)
3. NO CHILDREN -

Q.19 SEX OF RESPONDENT:

1. MALE
2. FEMALE

Q.20 ANNUAL HOUSEHOLD INCOME

1. < £10,000
2. £10,001-£20,000
3. £20.001 -£50,000
4. £50,001-£75,000
5. £75,001-£100,000
6. More than £100,000

Q.21 INVESTIBLE ASSETS (not including pensions or property)

1. <£10,000 (FOR PART 2: NON-PRODUCT HOLDERS – SCREEN OUT)
2. £10,000- £50,000
3. £50,001- £75,000
4. £75,001- £150,000
5. More than £150,000

ASK PRODUCT HOLDERS

Thank you. It sounds like you would be suitable to take part in the research, but before we can confirm the interview, I will need to check to make sure the product you have fits the requirements. Could you please find out the name of the product you have (it will be on any documents you have, or any statements) and who it is from, and I will call back [arrange time] to confirm the details with you.

STEP 2 - SUPPLY PRODUCT DETAILS TO IGNITION HOUSE

Recruiter: please capture product details & pass to Ignition House to confirm.

NAME OF PRODUCT ____

*PRODUCT PROVIDER*____

NAME OF IGNITION HOUSE PERSON WHO SIGNED OFF PRODUCT

____ DATE_______________

STEP 3 – ALLOCATE TO STAGE 1 OR STAGE 2, RE-CONTACT AND RECORD BOOKING DETAILS

Recruiter to re-contact respondent and schedule the time of the Face to Face interview. Say that they will receive a letter/ email of confirmation for the appointment. Stage 1 Respondents – say they will also receive a sheet with a few questions covering some things we would like them to think about before the interview. This should be completed before the interview and brought on the day.

NAME OF RESPONDENT: ____

RECTRUITED FOR: PART 1 - CUSTOMER JOURNEY/ PART 2 - EXERCISE RESERACH

POST CODE_________________

HOME TEL: _____________________ MOBILE TEL: ________________________

DATE OF F2F DEPTH: ____________________ TIME: __________________

DATE CONFIRMATION SENT ____

HOMEWORK EXERCISE SHEET SENT YES/NO/NOT APPLICABLE (PART 2 RESEARCH)

INTERVIEWER'S SIGNATURE: ________________________ DATE: _________

INTERVIEWER'S NAME: ____

8.3 Pre Interview Materials – Part 1: Motivations, Needs & Expectations

Homework Task

Thank you for agreeing to attend our discussion. During our meeting we would like you to talk to you about why you took out your investment product, and what you can recall about the process you went through to get it.

It would be helpful if you could take no more than **15-20 minutes** to answer the following questions which we hope will help to jog your memory.

If it would be helpful to you, please feel free to refresh your memory by reviewing any documentation you may have, **but please do not spend much time on this.** We are not expecting you have read your documents in detail, nor will we be asking any detailed technical questions about the literature in our discussion.

We very much look forward to meeting with you. Please remember to bring this answer sheet with you when you come.

Kind regards,

Ignition House

1. **What are your main objectives for your savings/ investments?**
2. **How would you describe you attitude to risk when it comes to your investments?**
3. **Where did the money come from for this specific investment?**
4. **What were your objectives for this money?** ***For example, did you have a specific use in mind, or were you looking to invest for a specific timeframe?***
5. **Did you consider doing anything else with the money?**
6. **Can you describe the process you went through to take out the product?**
   - Who was involved?
   - How did you hear about it?
   - How long did it take for you to decide the product was the right thing to do?
   - What were the key things that happened during that time? *For example, did you have any meetings or discussions?*
   - At what stages did you receive some literature about the product?

Thank you once again for your time. We look forward to meeting with you. **Please remember to bring this document with you when you come.**

8.4 Topic Guide - Part 1: Motivations, Needs & Expectations

Introduction

- Introduce self and Ignition House
- Interviews last 60 minutes
- Explain purpose and non-commercial nature of the research
- Explain confidentiality, audio and video recording

Warm up: Attitudes, Objectives & Needs for S&I

- Background about yourself, your occupation, and your family situation.
- What savings and investment products do you have at the moment?
- How knowledgeable do you feel about savings and investments in general?
- To what extent do you take an active interest in savings and investments?
- Do you feel confident in arranging your own savings and investments?
  - Where do you currently get your information and advice on savings and investments?
  - Do you do use the same approach for all the savings and investments that you hold?
  - What/ who is your first port of call if you need help?

Customer Journey: Purchasing their product

- Could you briefly talk me through the background to taking out this product?
  - How did you take it out? When was this? How long was the process? Who did you speak to? Would you say that is was as small or significant investment for you?
- Thinking back to before you took out this product:
  - Where did the money come from for this investment? Were you actively looking to do something different with this money at the time? What were your objectives for this money generally? What investment needs were you looking for the product to meet?
- Now looking at this set of features, can you say how closely each of the statements reflect the personal priorities and objectives that you had at the time that you invested in the product. (Please rate each statement using a scale of 1 to 10, where 10 means “it was essential” and 1 means “it was not at all important”.)

SHOWCARD 1

Get at least your money back at the end	A fixed return on your money	An easy to understand product
Lock money away for a set period of time	Some exposure to the markets	Brand name of the product issuer
Access money if needed it	Link to a particular market/reference measure	Need to spread money across different banks
Potential to do better than savings Account	Protection if the provider goes bust	Prefer to keep my savings and investments with a single provider
Beat inflation	Low charges	

- Thinking about structured products in general. Have you invested in similar types of products in the past? Why? What was your experience? Do you currently hold any others?
- When you first became aware of this product, could you describe to me how much you knew about these types of products and their features?
- Now thinking about how you became **aware** of this product. What made you aware of this particular product? Were you specifically looking for this type of product or did you come across it by other means? Was it your own decision/ idea or was it something prompted from a discussion with someone else?

ASK INTERACTIVE SALE (ADVISED)

- Now thinking about the **initial discussion** you had with the person who sold you it. Could you please describe to me what this initial discussion was like?
  - How would you describe the person (or people) that you dealt with?
  - How much weight did you place on their opinion when making a decision?
  - What can you recall was discussed about the product and its features… and about how it could meet your investment objectives and needs?

ASK EXECUTION ONLY

- So, now thinking about the **initial evaluation** that you did into the product:
  - What was the trigger for you to start to look for a product?
  - Where did you go to find out more about the product?
  - How long did you spend evaluating the product? What process did you go through?
  - And when you were researching it, what can you recall about the product and its features… and about how it could meet your investment objectives and needs?

ASK ALL

- Did you discuss/consider any other products at the time that could meet your needs?
  - How much time did you spend discussing/considering the alternatives? What products did you consider? How did you navigate through these alternatives? Did you make any specific comparisons? What sources did you use to gather information?
- During this discussion/evaluation, what was most attractive to you about your product? And what was attractive about the product in comparison to the alternatives?
- So, now thinking about **deciding** to opt for this product **and applying** for it. Could you please describe to me what your decision making process was like? What specific factors made you feel confident to take out this particular product/go ahead with the investment?

ASK INTERACTIVE SALE (ADVISED)

- To what extent did the discussion you had with [bank/ adviser] help you reach a decision to take this product out?

Mapping the Investment Landscape

I'd now like to do a quick exercise to get a sense for where you think your product fits compared to different investment products.

PRODUCT HIERARCHY EXERCISE – 9 PRODUCT SHOWCARDS

Your Product	Premium Bonds	Unit Trust/ Fund
5 year Fixed Rate Savings Bond	Cash ISA	Personal Pension or SIPP
1 year Fixed Rate Savings Bond	Stocks & Shares/ Equity ISA	Instant-Access Savings Account (bank/ building society)

- Are all of these familiar to you? (Provide a product explanation - exclude if no idea)
- Could you now please sort the products into three groups (high, medium, low) based on:
  - Ease of understanding how the product works
  - Ease of understanding what you will get at the end
  - Need for advice
  - Potential to get less than the value of the initial investment at the end
  - Potential returns/likely performance
  - Risk

- At the time you took out your [SP product], did you make any comparisons of what you would get in this product versus putting your money somewhere else, say in a fixed-interest bond or a deposit account?
    - What did you do? How did you go about making these comparisons? How easy was it? How confident are you in the assessment that you made? How important was this factor in your decision?
- Have you any idea how your product has performed so far against any of these alternative products? *(OR* if no comparisons raised) Have you any idea about how your product is currently performing?

Expectations

- Thinking now about when the fixed term comes to an end on your [SP product], what are your ***expectations*** of what you will get back from this product?
    - What is more important to you, return of capital or getting some investment growth?
    - How much more than your initial investment would you expect? (in both CASH terms and PERCENTAGES).
    - What would disappoint you? And what would delight you?
- How did you reach this conclusion? What did you base your thinking on? How confident are you in the assessment that you have made? (Probe fully)
- Do you remember seeing any examples of potential returns in the literature, or an adviser talking you through any examples? What are your thoughts on this?
- And how likely do you think it is that you will get more than your original investment back? Why do you say that?
    - Do you know what would need to happen for you to get more than your original investment back? Do you know what your investment return is based on?
- How likely do you think it is that you will get more than you could have got in an instant-access savings account? Why do you say that?
    - Do you know what would need to happen for you to get more than what you could get in a savings account? Do you know what the return on savings products is based on and how this differs to your product?
- How likely do you think it is that you will get more than you could have got in a longer term fixed interest deposit? Why do you say that?
    - Do you know what would need to happen for you to get more than what you could get in such a bond? Do you understand how your product differs?

- How likely do you think it is that you will get less than your original investment back? Under what circumstances could you get back less than you invested?
  - Do you know which provider is responsible for the ‘money back promise’ on your product?
  - What is your understanding of any protection you may have in the event the provider cannot meet its obligations?
  - In the event the provider cannot meet its obligations, is there anywhere you can go to get compensation? (**Deposits only** probe awareness of the FSCS)
- How would you describe your attitude to risk?
- If, for some reason, you were not able to get all your money back, what impact would this have?
- Are you aware of any other risks?
- Would you know what your product is worth today? How would you find out? Is there any way that you can track it?
- What would happen if you wanted to get your money out early?

Value for Money

We are now going to look at a range of scenarios about potential outcomes for a structured product, and ask you to tell me whether you think the product is giving good value for money. For each scenario, imagine you want to make an investment of £10,000 into the product and the product has a fixed five year term. There is no risk of capital loss. For each scenario we are going to show you different levels of interest that you could get on maturity, the probability of the return being triggered, and what this equates to in cash terms.

SHOWCARD PRODUCT SCENARIO 1 ***(Vary order shown)***

(EXPLAIN POSSIBLE RETURNS AND PROBABILITY OF THAT RETURN)

- What is your initial reaction of this product and the returns possible? How attractive do you find this product? \How likely would you be to invest in this product based on this payback and odds? Why?

(REPEAT FOR SCENARIOS 2, 3, 4)

SHOWCARD: ALTERNATIVE SAVINGS BOND

During your discussion with the adviser, they talk to you about an alternative savings product that could be suitable for you. This product is a fixed term fixed interest savings bond. Again, you have to invest for 5 years. You will be paid an interest rate of 2.35% on the account each year.

- What is your initial reaction to this rate of return?
- Tell them the return is £11,231 after five years) what is your impression of this return?

- Have you changed your view on how attractive this structured product is? Why?
- Which product do you think you would take out – the structured product with these payouts or the savings bond paying £11,231?

Wrap up

Reveal FCA.

Sign audio/ video release form.

THANK AND CLOSE.

8.5 Topic Guide - Part 2: Value for Money & Complexity

Introduction

- Introduce self and Ignition House
- Interviews last 90 minutes
- Explain purpose and non-commercial nature of the research
- Explain confidentiality, audio and video recording

Warm up: Attitudes, Objectives & Needs for S&I

- Background about yourself, your occupation, and your family situation.
- What savings and investment products do you have at the moment?
- How knowledgeable do you feel about savings and investments in general?
- To what extent do you take an active interest in savings and investments?
- Do you feel confident in arranging your own savings and investments?
  - Where do you currently get your information and advice on savings and investments?
  - Do you do use the same approach for all the savings and investments that you hold?
  - What/ who is your first port of call if you need help?
- How would you describe you attitude to risk when it comes to your investments?

Understanding Market Factors Driving Returns

<u>FTSE 100 Index</u>

- Could you describe to me what your understanding of the FTSE 100 index is?
- How well would you say you understood what drives movements in the FTSE100?
  - What level would you say the FTSE 100 is at today?
  - Could you describe what has happened to the FTSE 100 over the last year, 3,5 years?
  - What would you say is the typical annual change in the FTSE 100 over the long term?
  - How representative are current conditions would you say to the long term trend?

WORKBOOK - FTSE 100 VOLATILITY PATTERNS

- Which of these paths do you think best reflects movements in the FTSE 100 over 3 years? 5 years? Why? (probe: do they understand volatility).
- Are you aware of any other indices? (Probe for understanding)

WORKBOOK – FTSE 100 IN 3/6 YEARS

- We are now going to look at a series of statements about what could happen to the FTSE 100 in the next few years. Could you please say how likely you think each scenario is? (Range: *Certain, Highly Likely, Likely, 50/50, Unlikely, Very Unlikely, Impossible*)
- Now could you please put an actual percentage on that?
- For each scenario for the FTSE100, probe:
  - Please describe what you think the chances are of this happening?
  - What was your thinking behind this?
  - How confident do you feel with your answer?
- Were any aspects of this exercise particularly difficult for you to do? Why?

Interest Rates

- Would you be able to say what interest rate you are likely to get on a 5 year fixed term savings bond today? And on an instant-access savings account?
- What are your expectations for the future?

Inflation rates

- Would you be able to say the current inflation rate is?
- How well would you say you understood what drives movements in the inflation rate?
- Why is inflation important to consider when thinking about what returns you might get back from your savings and inflation?
- How sustainable do you think current inflation rates are? What are your expectations for the future?

Introduction to the Product

SHOWCARD – SP DESCRIPTION

I would now like you to look at a description of the product, called a structured product, which we are going to be looking at for the rest of our discussion.

- What are your initial thoughts on this type of product?
  - (Moderator to correct any misperceptions)
- How do you think this product differs to:
  - a direct investment in the index (e.g. equity ISA)
  - a fixed term deposit account
- What are the benefits? And the risks?

Understanding Complexity: Building the Product Features

We are now going to look at some examples of structured products. These are typical of what is available in the market, but do not reflect any particular product. For each I will provide you with a description and then ask some questions about how well you can understand the product from what you have read.

Example 1: Basic deposit product, FTSE 100 index, no capped upside

SHOWCARD: SP 1

- Can you describe in your own words what this plan is doing?
- On a scale of 1 to 10, how well do you think you understood it?
- On a scale of 1 to 10, how complex do you think it is?
- What needs to happen for you to get **only** your money back? How likely do you think this is to happen? Why?
- What needs to happen for you to get **more than** your money back? How likely do you think this is to happen? Why?
- Imagine that you have £10,000 available to invest in this product for term of 5 years. When you invest in this product, the FTSE is at 6,400. If by the end of the 5 years, the FTSE had grown to **7,040** what do you think your [gross] return would be – **ignore any income tax**?
  - What was your thinking behind this? How confident are you in this answer? How likely you think you are to get this return?
- If by the end of the 5 years, the FTSE had grown to **7680**, what would your return be? (again gross - ignoring income tax)
  - What was your thinking behind this? How confident are you in this answer? How likely you think you are to get this return?
- If by the end of the 5 years, the FTSE had grown to **9,600** what would your return be? (again gross - ignoring income tax)
  - What was your thinking behind this? How confident are you in this answer? How likely you think you are to get this return?
- Under what circumstances would you be better off doing this than investing in a savings account paying you a fixed interest rate of, say 2.75%, per year? When might you be worse off?

Example 2: Basic deposit product, FTSE 100 index, with capped upside

SHOWCARD: SP 2

- Can you describe in your own words what this plan is doing?
- On a scale of 1 to 10, how well do you think you understood it?

- On a scale of 1 to 10, how complex do you think it is?
- What needs to happen for you to get only your money back? How likely do you think this is? Why?
- What needs to happen for you to get more than your money back? How likely do you think this is? Why?
- Why is this different to the previous example?
- Imagine that you have £10,000 available to invest in this product for term of 5 years. When you invest in this product, the FTSE is at 6,400. If by the end of the 5 years, the FTSE had grown to **7,040** what do you think your [gross] return would be – **ignore any income tax**?
  - What was your thinking behind this? How confident are you in this answer? How likely you think you are to get this return?
- If by the end of the 5 years, the FTSE had grown to **7680**, what would your return be? (again gross - ignoring income tax)
  - What was your thinking behind this? How confident are you in this answer? How likely you think you are to get this return?
- If by the end of the 5 years, the FTSE had grown to **9,600** what would your return be? (again gross - ignoring income tax)
  - What was your thinking behind this? How confident are you in this answer? How likely you think you are to get this return?
- Under what circumstances would you be better off doing this than investing in a savings account paying you a fixed interest rate of, say 2.75%, per year?
  - When might you be worse off?

Example 3: Basic deposit, FTSE 100 index with Kick Out.

SHOWCARD: SP 3

- Can you describe in your own words what this plan is doing?
- On a scale of 1 to 10, how well do you think you understood it?
- On a scale of 1 to 10, how complex do you think it is?
- What needs to happen for you to get **only** your money back? How likely do you think this is to happen? Why?
- What needs to happen for you to get **more** than your money back? How likely do you think this is to happen? Why?

- What is the Kick Out feature? When will it come into effect? Why might you want this option?
- What are your thoughts on the ‘headline’ payout rates?
- Under what circumstances would you be better off doing this than investing in a savings account paying you a fixed interest rate of, say 2.75%, per year? When might you be worse off?
- Please mark on the scale how likely you think these scenarios are to happen:
  - Kick out after Year 2
  - Kick out after Year 3
  - Kick out after Year 4
  - Plan runs to maturity
- Please describe what you think the chances of this happening are?
- What was your thinking behind this?
- How confident do you feel with your answer?
- Under what circumstances would you be better off doing this than investing in a savings account paying you a fixed interest rate of, say 2.75%, per year? When might you be worse off?

Example 4: Basic deposit product, FTSE 100 index, with capped upside of 30% and a minimum return of 10%, calculating the Final Index Using Averaging over a year

SHOWCARD: SP 4

- Can you describe in your own words what this plan is doing?

EXERCISE BOOK: p10

- On a scale of 1 to 10, how well do you think you understood it?
- On a scale of 1 to 10, how complex do you think it is?
- What needs to happen for you to get **only** your money back? How likely do you think this is to happen? Why?
- What needs to happen for you to get **more** than your money back? How likely do you think this is to happen? Why?
- What needs to happen for you to get back **the minimum return of 10%**?
- What is your understanding of averaging? When might this type of averaging work to your advantage? And when might you be worse off than if the performance was calculated based on what the FTSE is on the final day of the plan?

Example 5: Cliquet Product

SHOWCARD: SP 5

- Can you describe in your own words what this plan is doing?

EXERCISE BOOK: p11

- On a scale of 1 to 10, how well do you think you understood it?
- On a scale of 1 to 10, how complex do you think it is?
- What needs to happen for you to get **only** your money back? How likely do you think this is to happen? Why?
- What needs to happen for you to get **more** than your money back? How likely do you think this is to happen? Why?
- Why is the **upper limit 42%?** What do you make of this?
  – If you were thinking about this product, how much would the 42% headline rate influence your thinking on whether this was a good thing to do?
- When might this plan be attractive?
  – When might you do better than investing in a deposit account?
  – When might you do better investing in an equity ISA?
- Please mark on the scale (0%______________42%) what you think the likely payout will be?
  – Please describe what you think the chances of this happening are to me
  – What was your thinking behind this?
  – How confident do you feel with your answer?
- Please mark on the scale how likely you think the scenario is of:
  – 0% payout - so you just get back your initial investment
  – 42% payout - the maximum possible
- Please describe what you think the chances of this happening are to me
- What was your thinking behind this?
  – What needs to happen for you to get 42%?
  – What needs to happen for you to get 0%
- How confident do you feel with your answer?
- Under what circumstances would you be better off doing this than investing in a savings account paying you a fixed interest rate of, say 2.75%, per year? When might you be worse off?

Value for Money

We are now going to look at a range of scenarios about potential outcomes for a structured product, and ask you to tell me whether you think the product is giving good value for money. For each scenario, imagine you want to make an investment of £10,000 into the product and the product has a fixed five year term. There is no risk of capital loss. For each scenario we are going to show you different levels of interest that you could get on maturity, the probability of the return being triggered, and what this equates to in cash terms.

SHOWCARD PRODUCT SCENARIO 1 ***(Vary order shown)***

(EXPLAIN POSSIBLE RETURNS AND PROBABILITY OF THAT RETURN)

- What is your initial reaction of this product and the returns possible? How attractive do you find this product? \How likely would you be to invest in this product based on this payback and odds? Why?

(REPEAT FOR SCENARIOS 2, 3, 4)

SHOWCARD: ALTERNATIVE SAVINGS BOND

During your discussion with the adviser, they talk to you about an alternative savings product that could be suitable for you. This product is a fixed term fixed interest savings bond. Again, you have to invest for 5 years. You will be paid an interest rate of 2.35% on the account each year.

- What is your initial reaction to this rate of return?
- (Tell them return is £11,231 after five years) what is your impression of this return?
- Have you changed your view on how attractive this structured product is? Why?
- Which product do you think you would take out – the structured product with these payouts or the savings bond paying £11,231?

Wrap up

Reveal FCA.

Sign audio/ video release form.

THANK AND CLOSE.

8.6 Stimulus materials

8.6.1 Complexity Exercise Showcard: '*SP Description*'

SHOWCARD: STRUCTURED PRODUCT

Structured Products are taken out for a set period of time (usually 5 or 6 years) and have the following features:

- Capital is protected, so at a minimum investors will receive back the money that they have invested at maturity.
- The return on the investment is calculated using a set formula which investors are told in advance. This formula is usually linked to the performance of a separate measure like the FTSE 100, inflation or Halifax House Price Index.
- The final amount of interest paid at the end of the product is not fixed. There may be a chance of getting no return, or a minimum return at the end of the product.
- Products are supposed to be held for the fixed term and it is not easy to exit them early.

8.6.2 Complexity Exercise Showcard: '*SP1*'

Structured Product 1

The Plan is designed to repay your initial deposit and deliver an additional return linked to the FTSE 100 over a 5 year term.

If the FTSE 100 is equal to or lower than its starting level after 5 years, you will receive back only your initial deposit.

At the end of 5 years, the plan gives you 100% of any growth linked to the performance of the FTSE 100 Index.

Imagine that you have £10,000 available to invest in this product for term of 5 years. When you invest in this product, the FTSE is at 6,400.

8.6.3 Complexity Exercise Showcard: '*SP2*'

Structured Product 2

The Plan is designed to repay your initial deposit and deliver an additional return linked to the FTSE 100 over a 5 year term.

If the FTSE 100 is equal to or lower than its starting level after 5 years, you will receive back only your initial deposit.

At the end of 5 years, the plan gives you 100% of any growth linked to the performance of the FTSE 100 Index. The maximum growth you can get back is 30% gross of the money you invest.

Imagine that you have £10,000 available to invest in this product for term of 5 years. When you invest in this product, the FTSE is at 6,400.

3

8.6.4 Complexity Exercise Showcard: '*SP3*'

Structured Product 3

The Plan is designed to repay your initial deposit and deliver an additional return linked to the FTSE 100 over a 5 year term.

There is also potential for the Plan to 'Kick-Out' early depending on the performance of the FTSE 100. This means that if the FTSE is higher than its starting level on specific dates, the Plan automatically matures early, returning your initial deposit plus a specified return.

If the FTSE 100 is higher than its starting level on the anniversary of your investment in Years 2, 3, 4, the Plan will mature (Kick-Out) at that time, paying back your initial sum plus a fixed payment of:

10% of the amount initially invested if the plan kicks out at Year 2
20% of the amount initially invested if the plan kicks out in Year 3
30% of the amount initially invested if the plan kicks out in Year 4

If the FTSE 100 is higher than its starting level, at the end of the 5 years – at maturity - you will receive your initial sum back plus a fixed payment of 50%.

If the FTSE 100 is equal to or lower than its starting level at 5 years, you will receive back only your initial deposit.

Imagine that you have £10,000 available to invest in this product for term of 5 years. When you invest in this product, the FTSE is at 6,400.

4

8.6.5 Complexity Exercise Showcard: '*SP4*'

<u>Structured Product 4</u>

The Plan is designed to repay your initial deposit and deliver an additional return linked to the FTSE 100 over a 5 year term.

If the FTSE 100 is equal to or lower than its starting level after 5 years, you will receive back only your initial deposit.

At the end of 5 years, the plan gives you the greater of 100% of any growth linked to the performance of the FTSE 100 Index and a minimum return of 10% in total.

Performance is calculated using an average reading of the value of the FTSE 100 on the same day each month of the final year of the investment term, rather than a single date.

The maximum growth you can get back is 30% gross of the money you invest.

Imagine that you have £10,000 available to invest in this product for term of 5 years. When you invest in this product, the FTSE is at 6,400.

8.6.6 Complexity Exercise Showcard: '*SP5*'

<u>Structured Product 5</u>

The Plan is designed to repay your initial deposit and deliver an additional return linked to the FTSE 100 over a 3 year term.

The final return from the product is calculated as follows:

- Every six months during the three year term, the level of the FTSE100 index is observed and the performance over the preceding six months is recorded.
- Performance in any six month period is limited to a maximum 7% rise, or 7% fall.
- By the final maturity years, a total of 6 periods of performance will have been recorded.
- The return on your deposit is the sum total of all 6 performance measurements, subject to a maximum of 42%, and a minimum of 0%.

Imagine that you have £10,000 available to invest in this product for term of 3 years. When you invest in this product, the FTSE is at 6,400.

8.6.7 Value for Money Exercise Showcard: Scenario 1

You have £10,000 to invest and you are looking to make an investment for 5 years. There is no risk of capital loss.

The columns show the different levels of interest that could be triggered on maturity, the probability of the return being triggered, and what this equates to in cash terms.

Scenario 1

Total amount of interest	Total amount paid back on maturity	Probability
10%	£11,000	5 out of 10
11 – 15%	£11,100 - £11,500	3 out of 10
16 - 20%	£11,600 - £12,000	2 out of 10

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8.6.8 Value for Money Exercise Showcard: Scenario 2

Scenario 2

Total amount of interest	Total amount paid back on maturity	Probability
0%	£10,000	2 out of 10
10%	£11,000	3 out of 10
15%	£11,500	2 out of 10
20%	£12,000	2 out of 10
25%	£12,500	1 out of 10

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8.6.9 Value for Money Exercise Showcard: Scenario 3

Scenario 3

Total amount of interest	Total amount paid back on maturity	Probability
0%	£10,000	4 out of 10
1 – 10%	£10,100 - £11,000	2 out of 10
11 – 20%	£11,100 - £12,000	1 out of 10
21 – 30%	£12,100 - £13,000	1 out of 10
31 – 42%	£13,100 – £14,200	2 out of 10

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8.6.10 Value for Money Exercise Showcard: Scenario 4

Scenario 4

Total amount of interest	Total amount paid back on maturity	Probability
0%	£10,000	5 out of 10
25%	£12,500	5 out of 10

10

8.6.11 Value for Money Exercise Showcard: Alternative Product

<u>Alternative: 2.35% interest per year</u>

During your discussion with the adviser, they talk to you about an alternative savings product that could be suitable for you.

This product is a fixed term fixed interest savings bond.

Again, you have to invest for 5 years.

You will be paid an interest rate of <u>2.35% each year</u>.

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<u>As an alternative to this product you could invest in:</u>

A 5 year term fixed interest savings bond paying 2.35% interest per year.

WHICH EQUATES TO A PAYOUT OF:

Total amount of interest	Total amount paid back on maturity	Probability
12.3%	£11,231	10 out of 10

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