FCA
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Sector Views
2017

Sector Views
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Sector Views
Introduction

The Financial Conduct Authority is the conduct regulator for 56,000 financial services firms and financial markets in the UK and the prudential regulator for over 18,000 of those firms. As such, it is vital that we understand how the financial markets are working, how they are evolving and the needs they are seeking to meet. To regulate effectively we need a view of how the system is working as a whole – as well as within its component sectors and markets. To develop this view, we divide the system into sectors and monitor them continuously using a wide range of data and intelligence.

Sector Views play an important part in our work... each Sector View helps determine our priorities for a sector, our resourcing decisions and our operational plans

The picture evolves almost daily, but once a year we bring our collective intelligence together into documents called Sector Views. These give us a picture – an FCA view – of how a sector is performing. Sector Views describe the sector, the need it seeks to fulfil, the issues and developments we are seeing and the impact of change.

By their nature Sector Views are a snapshot of a sector at a given time, based on the information available at that time. They set out what we already know but, just as importantly, they tell us where we need to know more. We regularly update the Sector Views internally with any significant developments to reflect the changing dynamics in the sectors.

Sector Views play an important part in our work. Once our Board has approved the content, each Sector View helps determine our priorities for a sector, our resourcing decisions and our operational plans. Once we have identified an area as a priority, we use an intervention framework to establish what is causing the harm. We analyse its scale and impact and we assess how effective different remedies could be. Our Business Plan then sets out which areas we are prioritising and how we plan to tackle them. This all takes place in the context of our Mission, which provides a framework for our decisions and the approach we take to delivering our objectives.

This year, for the first time, we are publishing our Sector Views alongside our Business Plan. These Sector Views were presented to our Board between June 2015 and November 2016 and contain information that was up to date at that point. In the future we will publish individual Sector Views on our website once a year, three months after they are approved by our Board.

We would welcome your feedback on our observations. Please send your comments to SectorViews@fca.org.uk

Our methodology

Sector Views draw on the wide range of information, research and insight held across the FCA. We supplement this with information from external sources, ranging from independent economic forecasts to MPs' correspondence, social media and the views of our Statutory Panels.

Sector Views are developed in four stages:

Understanding the sector
We define the scope of a sector. Our definition includes consumers, their needs, the products and services offered and the firms that supply them.

Monitoring intelligence
As well as FCA intelligence, we gather qualitative and quantitative information to show what is happening in markets. We consider this in the context of outside factors that might influence the sectors, such as macro-economic, technological, social and policy changes. We also consider the relationship between the sector under review and other sectors. This gives us as full a picture as possible of the key developments.

Assessing how the sector is performing
We analyse what the data and intelligence are telling us. We look at how the sector is performing for consumers and firms, the effectiveness of competition, whether markets operate fairly and cleanly, and the impact of market-wide forces.

Identifying the key issues for consumers, firms and the sector more widely
Finally, based on our assessment, we identify the key areas of focus for the sector and begin to prioritise them based on the actual or potential harm they cause. The areas we identify then inform our planned activity in the sectors.

We also assess how sectors are interacting with each other as part of the wider financial landscape. We identify cross-cutting issues that are relevant to a number of sectors, or that begin in one sector and affect another.

Consumer segmentation
In some of the Sector Views we refer to groups of consumers such as 'Retired with Resources' or 'Hard Pressed'. These refer to the categories set out in our consumer segmentation tool, Consumer Spotlight, which was developed jointly with The Futures Company, TNS BMRB and Experian. Consumer Spotlight helps us better understand consumers by dividing the UK population into 10 distinct segments. It shows how the groups have different financial needs, behaviour, capability and vulnerability, and identifies the groups where the risk and impact of potential detriment is greatest. Consumer Spotlight helps us identify the types of consumers who are active in a particular financial market and helps support a range of activities including policy development, risk identification and consumer communication.

The Sector Views cover all the markets we regulate, grouped into seven sectors:

- Retail banking
- Retail lending
- General insurance and protection
- Pensions and retirement income
- Retail investments
- Investment management
- Wholesale financial markets

Introduction
Methodology

We look at the sector through 13 lenses. This approach helps us assess where markets are working well, and where they are not.

Consumer journey

Taking actions on decisions
What prevents consumers from acting on their decisions or choices?

Assessing product/ service information
Can consumers assess what the best options are for their needs?

Accessing product/ service information
Is key information about products and services available that consumers can access without difficulty?

Assessing own needs
Do consumers suffer harm as a result of their lack of understanding of their needs, now and in the future?

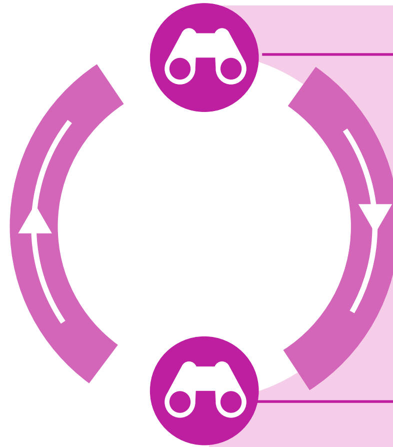
Market wide drivers

Barriers to entry or expansion
Are there factors which prevent new or existing firms from taking advantage of attractive business opportunities?

Consequences of regulatory or government intervention
Has regulatory or government action led to adverse impacts on competition between firms or poor outcomes for consumers?

Side effects on other parties
Do firms or consumers within the market take action which could have or has had side effects on other parties?

Consumers are empowered and buy products/services offering the best value for money



Firms compete vigorously to offer consumers a fair deal

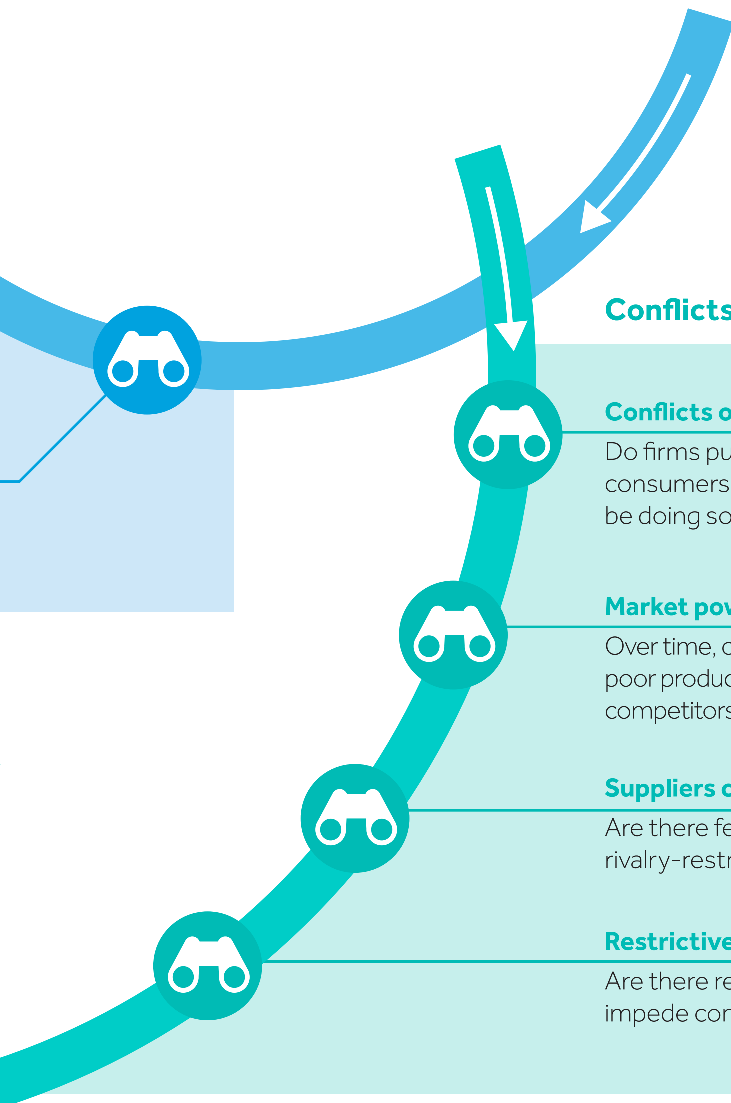
Firms' intent and behaviour

Firm-specific incentives

Are firms' policies, processes, procedures and culture focused on ensuring good consumer outcomes?

Firm specific behaviours

Do firms act in a way which results in good consumer outcomes?



Conflicts of interest and competition

Conflicts of interest

Do firms pursue gains for themselves by not acting in consumers' interest when they are obliged or perceived to be doing so?

Market power

Over time, can one or more firms maintain high prices or sustain poor product/service offerings without losing business to their competitors offering better deals?

Suppliers coordinating

Are there features within the market which mean that harmful, rivalry-restricting coordinated behaviour by firms is likely to occur?

Restrictive agreements within supply chain

Are there restrictive relationships within the supply chain that impede competitive rivalry within the market?

Retail banking and payments
Sector View

The retail banking and payments sector is the gateway into financial services for most consumers. It enables consumers to:

- make fast and secure payments
- hold funds securely (usually on deposit and possibly earning interest)
- have a credit buffer to smooth cash flow
- put money aside as savings both for the short and the long term

The sector serves consumers, including small and medium-sized enterprises (SMEs).[1]

We have divided the sector into three sub-sectors:

- transactional banking – personal and business current accounts, including overdrafts, which are provided by banks, building societies and credit unions (known collectively as deposit-takers)
- cash savings – personal and business savings accounts, which are also provided by deposit-takers
- payment services – defined as those payment services provided by firms other than deposit-takers such as money transmission firms, merchant acquirers and e-money providers

In practice, the distinction between the sub-sectors is not clear-cut, but it serves a useful purpose in framing our analysis.

This sector is closely linked to the retail lending sector. Overdrafts are inseparable from current accounts and we have considered them in both our Sector Views. Credit and charge cards are sometimes tied to a current account, although they are also offered as standalone products.

Transactional banking

Consumers

Although 97% of adults in Great Britain have a current account,[2] not all groups are equally likely to have one. The consumers least likely to hold a current account are the 'Hard Pressed' segment (15% of whom do not have an account). In 2014, personal current accounts generated revenues of approximately £8.7 billion.[3]

There are over 5.2 million SMEs in the UK, which make up over 99% of all UK businesses by number. 84% of SMEs use a business bank account[4] while others rely on a personal current account for their business needs.

Products

Until recently, consumers have not typically incurred fees for holding a personal current account or making and receiving payments. Most accounts still operate on this basis. In recent years, however, packaged bank accounts, which provide additional products and services (such as insurance or motor breakdown cover) for an additional fee, have become increasingly popular. Reward accounts, which typically offer higher rates of interest and cashback on certain

1. The Bank of England defines SMEs as those (non-financial) businesses with an annual debit account turnover on the main business account of up to £25 million. The FCA does not regulate all lending to SMEs, but most of the five million plus small and medium-sized enterprises in the UK need access to credit and lending products.

2. GFK Financial Research Survey, six months ending March 2015 data.

3. CMA Retail banking market investigation provisional findings report, 22 October 2015,

4. SME Finance Monitor Q2 2015, BDRC Continental.

transactions in exchange for a monthly fee, have also increased in popularity. Reward accounts are blurring the distinction between personal current accounts and savings accounts, often offering higher interest rates than some savings products. Unlike personal current accounts, business bank accounts usually incur fees for holding and using an account.

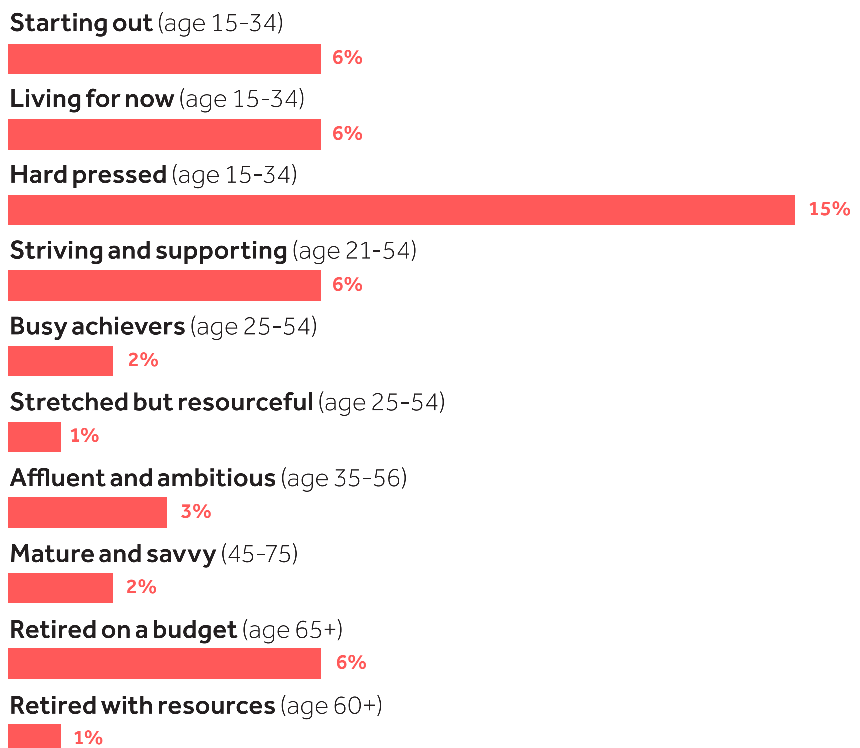
In a survey of 4,500 consumers in 2015, nearly two thirds of personal current account holders said they had an overdraft facility.[5] In 2014, providers derived 34% of their total income from personal current accounts from overdrafts.[6]

Firms

At the time of our review there were 38 providers of personal current accounts and 31 providers of business current accounts, which between them offered 387 different products.[7] Although there is a wide range of providers and products available, consumers and businesses overwhelmingly hold accounts with the six largest providers. At the time of our review, these banking groups accounted for 86% of the personal current account market.[8] The five largest banking groups accounted for 89% of the business current account market.[9]

Although transactional banking is dominated by the largest banking groups, there are established smaller providers and challengers in the market. For the purposes of this report we have defined challengers as new entrants to the banking market, or smaller banks seeking to challenge incumbents' business models. In recent years a number of new firms have entered the market and established strong brand identities. Although this has given

Figure 1: Consumer Spotlight
% least likely to have a personal current account



Range of ages are most prevalent ages.
For more information on our Consumer Spotlight model:
fca.org.uk/publications/research/consumer-spotlight

5. GFK, 'Personal Current Account Investigation: A Report for the Competition and Markets Authority' by GFK NOP, (April 2015).
6. Arranged and unarranged overdrafts. CMA Retail banking investigation provisional findings report, table 5.6 (October 2015).
7. Data from Moneyfacts as at 31 March 2016. Figures include student and graduate current accounts.
8. GFK Financial Research Survey, data six months ending March 2015.
9. Mintel Small Business Banking (June 2015).

86%

of personal current accounts are held with the six largest providers

66%

of consumers with a cash savings account hold them with their main current account provider

GFK Financial Research Survey, data six months ending March 2015

consumers more choice, challenger banks' market share remains low and none has yet gained a market share above 5% – the share the Independent Commission on Banking deemed that a challenger would need to provide a competitive constraint on larger incumbents.

How services are provided and accessed
Consumers and businesses have a direct relationship with the banks and building societies that provide their accounts. Although most consumers continue to go straight to a provider, price comparison websites allow consumers to compare features of different accounts and may also facilitate account opening through their sites.

Consumers can access and manage their accounts through a range of channels. At the time of our review, 25 million consumers used online or mobile channels and 13.9 million consumers relied on branches. The use of mobile channels in particular has grown, with 2.5 million consumers accessing their current account solely through mobile channels.[10]

The 'gateway' nature of a current account provides opportunities for firms to cross-sell additional products to individuals and businesses. 28% of individual consumers held all their banking products with their main bank.[11] According to data collected for the Competition and Markets Authority (CMA), SMEs also tend to obtain a wide range of banking products from their main bank. 88% of those with a company credit card obtained it from the same provider as their business current account, while 72% of those with a business mortgage purchased it from the same provider as their business current account.[12]

Cash savings

Consumers
At the time of our review around 55% of British adults had a cash savings account.[13] Our data showed that the propensity to hold an account rose both with age and affluence. Our Cash Savings Market Study showed there are 69 million easy access accounts in operation holding £354 billion of savings.[14] There are also 4 million fixed-term savings accounts in operation, holding £145 billion in assets. Over 66% of consumers with a cash savings account held it with their main current account provider.[15]

Consumers' use of digital channels to open and manage accounts has increased in recent years, and the number of bank branches has declined. Retired consumers are less likely to use the internet to manage their accounts, and are more likely to use branches. At the time of our review, SMEs held £67 billion in business savings accounts.[16]

Products
Compared with the transactional banking market, the cash savings market has a large number of providers offering a larger range of products. At the time of our review there were 117 providers of products offering 1,737 different products.[17] These accounts include easy access savings accounts, fixed-term products with penalties for access before maturity, and tax-efficient ISAs. While we observed significantly more providers and products in the cash savings market than in transactional banking, at the time of our review, 73% of the market share by volume[18] was held by the six largest bank account providers.[19]

Payment services

Consumers
Consumers can make and receive payments in a variety of ways using cash, credit and debit cards, automated payments and money remittance. Although standing orders and Direct Debits continue to make up around three quarters of the volume of regular payments, such as mortgages, utility

10. GFK Financial Research Survey (FRS), six months ending March 2015 data.
11. GFK, 'Personal Current Account Investigation: A Report for the Competition and Markets Authority' by GfK NOP, (April 2015).
12. Charterhouse Q3 2013, Banking services to small and medium-size enterprises: A CMA and FCA market study (July 2014).
13. GFK Financial Research Survey (FRS), six months ending March 2015 data.
14. Based on data for 2013, covering the 21 largest providers.
15. GFK, 'Personal Current Account Investigation: A Report for the Competition and Markets Authority' by GfK NOP, (April 2015).
16. BBA Bank support for SMEs, Q2 2015.
17. Moneyfacts Treasury Report, UK Savings Trends (November 2015).
18. GFK Financial Research Survey, six months ending March 2015 data.
19. Lloyds Banking Group, HSBC Group, Barclays, RBS Group, Santander UK) and Nationwide.

bills and subscriptions, the way non-regular or spontaneous payments are made has changed over the last few years. According to data from Payments UK[20] while cash remains the most popular method for spontaneous payments,[21] between 2009 and 2014 its use fell from 63% to 52% of volume for all spontaneous payments. During the same period, the volume of debit card transactions for spontaneous payments increased by 56%.

Automated payments (Direct Debit, Bacs, Faster Payments, CHAPS and remote banking) accounted for 20% of all payment transactions in 2014 and accounted for 79% of their total value. Credit card transactions remained steady at 6% of all transactions.[22]

Firms
Traditionally, banks and building societies have dominated the payment services market. However, in recent years we have seen an increasing number of non-bank firms, including technology firms, entering the market and leveraging technology to deliver services. Although most payment transactions are carried out by banks and building societies, we are seeing a growing challenge from these new entrants.

Payment systems

Designated payment systems are regulated by the Payment Systems Regulator. Payment systems underpin the payment services that enable funds to be transferred between people and institutions. Payment systems transfer huge sums of money every day, and trillions of pounds annually.

- Bacs is the interbank system that processes payments through two main electronic payment schemes: Direct Debit, which is used by individuals and businesses to pay bills, and Bacs Direct Credits, which are used by the Government and businesses to pay benefits, pension payments, bill and supplier payments and employee salaries and wages. Bacs Payment Schemes Ltd operates the Bacs payment system. In 2014 it enabled 5.8 billion transactions with a total value of £4.4 trillion.[23]
- The Faster Payments Scheme (FPS) provides near real-time payments as well as standing orders. Almost all internet and telephone banking payments in the UK are now processed through FPS. It is also used by payment service providers to process other services. Faster Payments Scheme Ltd operates the FPS payment system. Faster Payments made 1.1 billion transactions in 2014 at a value of £904 billion, but we expect to see this grow as the system becomes more established.[24]
- CHAPS is the UK's real-time, high-value sterling interbank payment system, where payments are settled over the Bank of England's Real Time Gross Settlement (RTGS) infrastructure. CHAPS processes both wholesale (eg international payments) and retail payments (eg house purchases). CHAPS Clearing Company Ltd operates the CHAPS payment system. CHAPS is the smallest payment system in terms of volume, but the largest by value at £67.9 trillion in 2014.[26]
- LINK allows consumers to withdraw cash using the LINK network of ATMs in the UK. LINK Scheme operates the LINK payment system.
- Cheque and Credit (C&C) is the interbank payment system in England, Scotland and Wales that processes cheques and other paper instruments. The Cheque and Credit Clearing Company Ltd manages the systems used for making payments by cheque.
- Visa and MasterCard also have their own payment systems to underpin payments made by the cards they provide. These account for the largest volume of transactions, but the lowest value per transaction.

20. UK Consumer Payments 2015, Payments UK.
21. Spontaneous payments are all non-regular payments
22. UK Payments Market 2015, Payments UK.
23. UK Payments Market 2015, Payments UK.
24. UK Payment Statistics 2015, Payments UK.
25. UK Payment Statistics 2015, Payments UK.

25 million
consumers access and manage their bank accounts using online or mobile channels

GFK Financial Research Survey, data six months ending March 2015

x3
Between 2013 and 2014 contactless payments trebled in value

Payments UK (2015)

Consumer needs are becoming increasingly diverse... older consumers are less inclined to use emerging technology as their primary means of accessing banking, while younger consumers prefer to engage digitally, although income and education levels also determine consumers' behaviour

Drivers of change

The retail banking sector is subject to a complex regulatory structure. It is subject to European and UK legislation, and regulation by the Bank of England, the Prudential Regulation Authority and the FCA. The European Banking Authority also provides technical standards and guidance on European legislation. In addition, the CMA has recently undertaken a study into retail banking, which will have a significant influence over the way the market develops.

The immediate post-crisis focus on re-capitalisation of banks and significant prudential regulatory change has begun to give way to policy and regulation that promotes competition and innovation, as well as improving market integrity. The sector continues to be subject to a large mandatory regulatory change agenda with multiple objectives. This includes ring-fencing and the revised EU Payment Services Directive (PSD2). This is taking place against a backdrop of uncertainty over the consequences of the UK's decision to leave the EU.

The low interest rate environment is putting pressure on firms' net interest margins. Coupled with the increasing costs of regulatory capital requirements, this is having an impact of firms' financial performance and is driving the need to cut costs (with digital innovation a key driver of cost-cutting).

Existing firms are beginning to use new technologies. We are seeing that technology is a key driver of change in the sector, with many new entrants using technology to launch new offerings.

Consumer needs are becoming increasingly diverse. In general, older consumers are less inclined to use emerging technology as their primary means of accessing banking, while younger consumers prefer to engage digitally, although income and education levels also determine consumers' behaviour. This means that firms need to invest both in physical and digital services to satisfy consumer demand. Stagnating real incomes, low interest rates and greater uncertainty are having an impact on consumers' desire and ability to save.

Our assessment

Consumers' interaction with retail banking

The sector is characterised by loyalty to brands and firms, but also by inertia – with many consumers paying relatively little attention to the way they are using their account. Overall, levels of switching are low. With an increasingly diverse population, we are concerned that there may be diminishing access to products for some groups of consumers.

Technology is changing the way consumers access information and interact with their provider, but this does not always translate into consumers taking action.

Firms' intent and behaviour

We found that banks are setting a strong 'tone from the top' around culture and intended good consumer outcomes, but competing objectives can lead to mixed actual outcomes for consumers. Commercial pressures to reduce the cost to serve, technology and evolving demand are accelerating a shift towards digital channels. This may improve profitability but may lead to some consumers being excluded. We are not seeing firms compete for these excluded consumers.

Competition

The sector remains concentrated, with continued low levels of switching. Firms have entered the sector but have not yet gained significant market share. Since the CMA concluded its retail banking Market Investigation in August 2016, we have been working with them to introduce remedies to increase competition.

Market-wide drivers

The largest firms face a significant challenge to adapt their business models in response to regulatory developments such as ring-fencing, capital requirements and the Senior Managers Regime. The scale of change may increase the risk of poor consumer outcomes and adverse impacts on firms. Firms also remain concerned about regulatory, political and economic developments outside the UK.

Areas of focus

Ring-fencing

By 2019 the largest banking groups must separate their retail and wholesale operations into two separate banks. We are concerned that the complexity of the undertaking will lead to increased operational risks for affected banks and unintended consequences for consumers. We are particularly focused on the continuity of banking services for consumers, the impact on pricing and availability of services, and the layering effect of these changes alongside other political and regulatory change.

Non-bank payment firms

A significant number of new and innovative non-bank payment firms have been entering the market, which present consumers with opportunities to make payments in new ways – often at lower headline cost to traditional banks. Non-bank firms operate within a different regulatory framework to traditional banking firms, with different (and sometimes fewer) consumer protections, which are not always clear to consumers. We will be monitoring how the market develops, with a particular focus on the evolving technology, marketing and consumer adoption of these new services.

Competition

New entrants and innovation have led to some increased competition in recent years. In spite of this, retail banking is characterised by low consumer engagement and low levels of switching. Consumer inertia means that incumbents retain their position and have limited incentives to innovate and improve quality and price, while new firms struggle to grow and gain market share. We will continue to monitor how the market develops as a result of intervention activity such as ring-fencing, CMA remedies and the growth in non-bank payment firms.

IT stability and security

The largest banking groups are long-established and tend to have extensive, complex legacy IT systems supporting their operations. Firms must deliver extensive programmes of regulatory and business change into these systems, which are complex and costly. They can also present significant operational risks to firms and the risk of disruption in service to consumers. Firms are also seeking to innovate to compete, offering new digital banking services, which add to the volume of change and exacerbate the risks identified above.

In addition, there has been a significant increase in cyber-threat to firms and we are focused both on firms' preparedness for, and response to, cyber-attacks.

Financial crime and anti-money laundering

We are seeing general improvements in firms' systems and controls in relation to financial crime and anti-money laundering as a result of increased effort over recent years. However, a significant number of banks (and retail banks in particular) continue to have poor controls over high-risk customers and we will be monitoring to ensure firms continue to improve these controls. We are seeing an increase in reports of payment fraud and will continue to focus on firms' controls to identify and prevent it.

Access and vulnerability

We observe that efforts to de-risk, shed unprofitable business and standardise operations may leave some consumers and SMEs unable to access services they had used previously. In addition, firms find it difficult to identify and respond to vulnerable consumers' needs within existing business processes.

Culture

In recent years we have undertaken a lot of work with firms to improve culture. We will be monitoring carefully as this work continues to embed – ensuring that firms develop their culture and continue to prioritise the fair treatment of consumers.

Business models

Firms are reconsidering their business models to adapt to structural reform, an economic environment in which interest rates are staying lower for longer than many had expected, the UK's exit from the EU, and changing technology and consumer demand. The consequences of these changes for consumer outcomes, competition and market integrity are not yet clear, and we will continue to monitor and assess the implications of firms' business model changes in the future.

Retail lending
Sector View

The retail lending sector exists to meet the borrowing needs of individual consumers and small-to medium-sized enterprises (SMEs). The sector provides secured and unsecured borrowing that covers everything from day-to-day expenses through to buying a property.

At the heart of retail lending is consumers' need to fund spending or to refinance debt by drawing on future income to meet current needs. The sector allows consumers to manage their budgets more flexibly and make financial commitments they might otherwise not be able to make (or to make them more quickly) by providing them with a loan or credit. As an alternative to buying on credit or through a loan, some consumers choose to hire products, in which case their arrangements may be regulated as a consumer hire agreement.

Retail lending is a key driver of economic activity. At the end of 2015 UK households owed £1.27 trillion in mortgages and £179 billion in consumer credit.[1]

Consumers

Different consumer segments use lending in different ways. A consumer's access to products depends on their circumstances, their individual risk profile and their ability to repay. The circumstances and behaviour of individuals drive credit risk and therefore the cost at which lenders are prepared to lend to them – if at all. Many consumers have more than one lending product.

In general, consumers with a good track record of using financial products, and whose circumstances suggest a degree of stability, will be able to access credit at attractive rates. In contrast, consumers whose circumstances are more transient or less well-documented, or who have a history of missed payments, may have to approach specialist lenders and may need to pay more to access credit. Consumers who struggle with their debt may use specialist debt advice services.

While access to credit can be beneficial (and in some cases essential) for some consumers, those who are most reliant on credit are often those most at risk of taking on unsustainable repayments. Changes in circumstances can also make borrowing unaffordable and force consumers to default on their loan. If their debt becomes unmanageable, consumers may seek advice from firms, or firms may proactively seek out consumers in debt to offer them a solution.

Products

We divide the sector into five broad sub-sectors, each defined by its product structure and the way consumers use it.

Mortgages

Mortgages are loans secured on a property,[2] which are used mainly to fund or refinance the purchase of a property. They can also be used to release equity accumulated in a

1. Bank of England Statistics, Bankstats (Monetary & Financial Statistics), Money and Lending table A5.2 (January 2016). Bank of England data (balances outstanding) are updated each month and may be subject to adjustment due to changes in the reporting population, classification changes reflecting any updated sectoral classification guidance produced by ONS, foreign currency revaluation effects, write-offs, or miscellaneous other causes such as adjustments made on the basis of information provided by reporting institutions. A full explanation can be found here: http://www.bankofengland.co.uk/statistics/Pages/iadb/notesiadb/Changes_flows_growth_rates.aspx

2. A regulated mortgage contract is one under which the borrower is an individual or trustees and the obligation of the borrower to repay is secured against land in the EEA as a first or second charge, provided that at least 40% of the land is used or is intended to be used as or in connection with a dwelling. For more information, see section 4.4 of our Perimeter Guidance manual.

property, which can be an alternative to borrowing using other forms of credit, or to consolidate existing debts. Buy-to-let mortgages are generally not regulated.[3]

When arranging a mortgage, consumers either access the market through their chosen lender, or through an intermediary firm (such as a broker) that has access to a range of mortgage providers. The Mortgage Market Review led to a significant increase in advised sales, where a recommendation is made based on a consumer's circumstances. Advised sales increased from 75% of mortgage sales in 2012 to 97% in 2015.[4]

According to Moneyfacts data, there are around 6,000 different mortgage products (including buy-to-let mortgages) available to new consumers.[5] Mortgage rates may be fixed or variable. Variable rates can either be the lender's standard variable rate, or a rate fixed by reference to another index such as the Bank of England Bank Rate. Rates are typically higher for mortgages with higher loan-to-value ratios.

Secured consumer credit
Secured consumer credit loans are secured against an asset of the borrower, or secured by a guarantee or indemnity provided by a third party. Products include pawnbroking and logbook loans.

Pawnbrokers provide loans secured against the value of a pledged item. Over two million items are pawned each year, and in 2013 there were over 2,000 pawnbrokers in the UK. Loans typically last for six months and annual percentage rates charged range between 70% and 130%.[6] In 2015 gross annual lending was £520 million.[7]

The logbook loan market is small and niche. Loans are secured against a borrower's vehicle, and are generally aimed at consumers with a poor credit history who need a relatively large amount of credit quickly. They tend to be short to medium-term loans (typically between 6 and 18 months). Interest varies, but APR is usually around 400%.[8] Logbook loans are generally secured by a bill of sale. In 2016, the Law Commission recommended that the Bills of Sale Acts 1878 and 1882 be replaced by more modern legislation to improve consumer protections for borrowers taking out logbook loans.

Running account unsecured consumer credit
A significant amount of unsecured borrowing in the UK takes place on a running account credit basis. These products allow consumers to borrow flexibility within an agreed limit. Products include credit cards, overdrafts and catalogue credit.

Credit cards
Credit cards are the most commonly used and widely held lending product in the UK. In 2014, 60% of consumers[9] and 48% of SMEs were active users of credit cards.[10] In total, over 30 million consumers had over £63 billion in outstanding debt.[11]

Our Credit Card Market Study's final report stated that although competition was working fairly well for most consumers, we were concerned about the scale of potentially problematic credit card debt. We estimated that in 2014, 6.9% of cardholders (2.1 million) were in arrears or default, a further 6.6% of cardholders (2 million) had an average credit limit utilisation of 90% or more

At the end of 2015 UK households owed:

£1.27tn
in mortgages

£179bn
in consumer credit

3. The exception is a consumer buy-to-let (CBTL) mortgage, which is subject to the legislative framework set out in the Mortgage Credit Directive Order 2015.

4. FCA Product Sales Data Q4 2015.

5. Moneyfacts Monthly Treasury Report (January 2016).

6. Based on FCA analysis and information from National Pawnbrokers Association (2013).

7. Pawnbrokers & High-Street Loan Stores: Apex Insight Report (August 2015).

8. Based on FCA analysis of Citizen Advice and BIS data (2015).

9. FCA Credit Card Market Study Interim Report - Market Overview (November 2015).

10. CMA Retail Banking Market Investigation Report (November 2015).

11. FCA Credit Card Market Study Final Findings report (July 2016).

63.3 million

total number of credit cards in issue at the end of 2014 (there are around 30 million card holders)

FCA Credit Card Market Study Interim report (November 2015)

42%

of credit card balances are paid off in full each month therefore accrue no interest

UK Cards Association (Q4 2014)

during a calendar year, and another 1.6 million repeatedly made minimum repayments. Furthermore, we found that 650,000 people had an average credit limit utilisation of 90% or more for three consecutive calendar years or more, and a further 750,000 people had been making systemic minimum repayments for that time.

Credit card firms have been competing to offer longer interest-free periods for balance transfers and purchases. In mid-2014 over 25% of outstanding balances were on 0% balance transfers.[12] It was widely anticipated that the reduction in interchange fee revenue for credit card firms would lead to some reduction in rewards or increase in the price paid by consumers. The market appears to be adjusting along those lines, although it is too early to say what the long-term impact will be.

Overdrafts

Overdrafts are a credit facility attached to current accounts. They allow consumers whose account balance reaches zero to continue drawing and spending money. They are either 'arranged' (within a limit already agreed with the financial institution) or 'unarranged' (in excess of any overdraft limit previously agreed).

They are provided by current account providers, and the market is dominated by the biggest banks and building societies. In recent years, some banks have moved away from charging overdraft fees based on a percentage of the amount borrowed, and have moved instead to flat fees and charges.[13] 45% of personal current account customers and 43% of SMEs are overdraft users,[14] with outstanding balances of £7 billion.[15]

Fixed-sum unsecured consumer credit

Fixed-sum unsecured consumer credit covers a wide range of credit products including:

- personal and business loans
- peer-to-peer lending
- motor finance
- high-cost short-term credit (payday loans)
- home-collected credit

Personal loans are prominent in the fixed-sum market, with £36 billion in outstanding balances.[16] The largest banking groups are the major providers of personal and business loans in the UK, with 66% of the market.[17] Smaller banks and building societies and specialist personal loan companies make up the rest of the market.

Motor finance has grown rapidly in recent years; the value of advances for cars bought on finance by consumers reached £32.7 billion in 2014.[18] Personal contract purchase (PCP) is prominent in the private car finance market. Key providers of car finance plans are car manufacturers' finance arms and specialist lenders, including some banks.

12. FCA Credit Card Market Study Final Findings Report (July 2016).

13. Firms typically charge different rates for arranged and unarranged overdrafts.

14. CMA Retail Banking Market Investigation Report (November 2015).

15. BBA High Street Banking Statistics (December 2015). Note: this data only covers the main high street banks.

16. BBA High Street Banking Statistics (December 2015). Note: this data only cover the main high street banks.

17. Mintel 'Unsecured Loans - UK' (January 2016).

18. FLA Annual Review (2015).

Peer-to-peer loans are a small market that has grown rapidly in recent years. Peer-to-peer platforms do not lend directly, but facilitate agreements between borrowers and lenders. The nature of the borrower and the lender will determine whether the loan and/or the platform's activity is regulated. In the fourth quarter of 2015, £2.1 billion was outstanding (£0.91 billion to individuals and £1.2 billion to businesses).[19] Dedicated peer-to-peer platforms form marketplaces for borrowers and lenders, with some specialising in business lending.[20]

The high-cost short-term credit sector is relatively small. At its 2013 peak, it was estimated at roughly £2.5 billion, with 10 million payday loans made to 1.6 million consumers.[21] The FCA has strengthened regulation in this sector and imposed a price cap on the sector in January 2015. As regulation has become firmer, the market has reduced in size. More recently, there have been signs that the market for high-cost short-term credit is increasing, though lending levels overall remain much lower than before the imposition of the cap.

In the home-collected credit market, relatively small amounts are lent through agents, and payments are typically collected on a weekly basis. There were just under £1.2 billion in loans outstanding in October 2015. In 2015 there were an estimated 2.3 million home-collected credit customers in the UK.[22] The average length of these loans is usually between 26 and 52 weeks and loan values are typically between £250 and £750.

Credit and debt services

Credit reference agencies

Credit reference agencies collect a range of information about potential borrowers and make it available to lenders. Lenders use this information to make decisions about a consumer's creditworthiness (ie their likelihood of making repayments). There are three major credit reference agencies and a number of smaller agencies who specialise in credit checks for more niche products. Some credit reference agencies also sell information services to customers, particularly on their credit history.

Debt collection and purchase

Debt collection is the provision of services such as attempted tracing, phone and written contact with a debtor, on behalf of a creditor. Around £20 billion is passed from lenders to debt collectors every year.[23] In debt purchase, specialist firms buy performing, semi-performing or non-performing debt accounts. The price paid for the debt varies, but for semi or non-performing debt it tends to be significantly lower than the face value of the debt. The new owners of the debt then attempt to obtain repayment from the debtor.

Debt advice and debt management

The market for consumer debt services is made up of two main groups: fee-charging and free-to-consumer. The debt services offered by these groups include debt counselling (advice) and debt adjusting (debt negotiation). Many firms offer both, while some only offer advice. If any of these activities is carried out with a view to an individual entering into a particular debt solution, this constitutes debt management activity. Almost half a million consumers hold debt management plans with the top ten providers.[24]

Credit broking

Credit broking is the introduction of a potential borrower (looking to enter into a consumer credit agreement or a consumer hire agreement) to a lender or provider of goods on hire. Credit broking activity includes preparatory work and presenting or offering a regulated credit agreement. It also includes brokers introducing potential borrowers to other brokers. A large part of the credit broking sector is occupied by retailers who offer finance terms for their goods or services, on behalf of a third-party lender. The broker may be acting primarily for the consumer (for a fee) or the lender/owner (for commission) or both. There are approximately 29,000 credit brokers in the UK.[25]

19. P2P Finance Association data for Q4 2015 (January 2016).

20. The FCA is undertaking a post-implementation review of the peer-to-peer market, and a call for input was published in July 2016.

21. FCA CP14/10: Proposals for a price cap on high-cost short-term credit (July 2014).

22. 'The impact on business and consumers of a cap on the total cost of credit', Personal Finance Research Centre, University of Bristol (2013).

23. NOCN Level 2 Award for Working in the Debt Collection Industry (QCF) - 2014 Overview.

24. FCA Consumer Credit Authorisations (August 2015).

25. FCA permissions data (August 2016).

Firms

A wide range of firms operate in this sector, from the largest banks in the UK to high street retailers offering secondary credit-broking services relating to the goods or services they offer.

During the third quarter of 2015 there were 127 providers of new mortgage products.[26] However, most mortgage lending is concentrated among the UK's largest banks, with the top six lenders accounting for 77% of regulated mortgage balances market share.[27] Smaller lenders and building societies generally compete in more specialist or niche product areas.

The large banks, supermarkets and monoline[28] card issuers have a large presence in the unsecured running-account and fixed-credit markets. The top nine card-issuing groups account for an estimated 81% of the credit card market.[29]

The largest five banks are the main providers of personal and business loans in the UK, as well as overdrafts.[30] Smaller banks, building societies and specialist personal loan companies make up the rest of the market.

In other credit markets, a small number of firms have a large presence. For example, in the peer-to-peer loan market three firms have an 83% share[31] and three firms account for around 70% of the high-cost short-term credit market.[32]

Drivers of change

Technology is driving innovation in the sector, giving rise to new firms, business models and products. It is improving functionality and convenience through mobile and digital interactions, and more use of real-time data sharing and predictive analytics is driving lending decisions in the supply side. However, technology can also lead to financial exclusion for less tech-savvy consumers or for those who have limited internet access, and to increased security and resilience risks.

Recent policy and regulation such as the price cap on high-cost short-term credit, has focused on improving the market by encouraging affordable and responsible lending. The regulation of consumer credit was passed to the FCA on 1 April 2014. The Government gave two reasons for this decision: to give

26. FCA Product Sales Data (PSD), Q3 2015.
27. FCA Mortgage lending statistics (MLAR) Q4 2015.
28. A monoline provider is a firm that focuses on one specific financial product.
29. Mintel Credit Card Study (May 2015).
30. CMA Retail Banking Market Investigation Report (November 2015).
31. P2PFA quarterly data release for Q4 2015 (January 2016).
32. CMA Payday lending market investigation (February 2015).

consumers better protection; and to ensure that the regulatory regime is proportionate to the types of firms and the risks posed by them. The transfer has led to changes in the provision of credit and debt services, which may have reduced access to mainstream lenders for more indebted and lower income consumers. It may also have led firms to diversify their business models (eg payday lenders offering instalment loans), which may pose different risks. Many of these policies and regulations were introduced recently, so we must continue to monitor their impact on the market.

Socio-economic trends suggest that the retail lending sector will remain a key driver of economic activity over the coming years. Household finances have been under pressure from low wage growth and changing labour market conditions, including a rise in less secure forms of employment and zero hour contracts. Household debt has remained relatively high, with an overall ratio of household debt-to-income of 142%. This is forecast by the Office for Budget Responsibility to rise to 149% by 2021, which, although high, is still below the pre-crisis peak of 160%. In the mortgage market, lending figures have been more subdued since the crisis.[33]

Increasing demand for consumer credit, particularly in the sub-prime sector, has seen growth concentrated in specialist lenders. Low interest rates have kept the costs of consumer borrowing low, but may put more indebted households (and those who have become accustomed to low rates) under pressure if interest rates rise.

Wider economic and regulatory factors have put continued pressure on firms' revenue, and many have responded by cutting costs and outsourcing.

Our assessment

Consumers
Some consumers struggle to assess product and service information (and to take action) because of complexity, a lack of transparency, and the number and variety of products and services available to them. This is compounded by the fact that some consumers also misjudge their needs. They can be over-optimistic and place their immediate needs over longer term considerations – for example, by focusing on initial monthly mortgage payments or introductory rates on credit cards. This issue is most acute where consumers are distressed or are focused on a pressing need.

Consumers and SMEs tend to give their options less consideration when buying or renewing a financial product from their existing lender, using an existing line of credit, or obtaining credit at the point of sale. This is particularly acute for vulnerable consumers and consumers in financial difficulty.

Conflicts of interest and competition
In consumer credit, some firms exploit demand-side weaknesses and we observed some unmanaged conflicts of interest. There are risks that motor and retail finance consumers pay too much for credit at point of sale, and that fee-charging debt management firms may not give impartial advice and may sell unsuitable plans.

Although technology and innovation can be beneficial, they may fail to address (and/or exacerbate) weaknesses in the way consumers make decisions. Price comparison sites facilitate shopping around, although they do not always display the full range of products available. There are a small number of lenders with a large market concentration in the SME banking market.

Firms' intent and behaviour
In consumer credit, evidence from our recent Credit Card Market Study showed that some credit

Average household debt-to-income

142%

By 2021, this is forecast to rise to

149%

33. Economic and Fiscal Outlook, Office for Budget Responsibility (November 2016).

card providers allow 'performing' consumers to stay in long-term debt and pay interest and fees over a prolonged period, putting them at risk of building up unsustainable debt.

There is a risk that where firms have an additional route to limit losses (such as the security of the vehicle for logbook loans or the guarantee for guarantor loans), they may have less incentive to conduct stringent affordability assessments at the outset. It follows that these firms will need to have effective systems and controls in place to mitigate this risk.

A small interest rate rise could affect mortgage borrowers significantly, either directly if their rate is variable or indirectly if their rate is fixed (through a general impact on household finances). A rate rise, alongside government welfare reforms, is likely to increase demand for debt advice – at the same time as capacity in debt advice services may be adjusting to the transfer to FCA regulation and a reduction in public spending on advice.

A rate rise or deteriorating economic conditions may increase the risk that borrowers in financial difficulty are shown inappropriate or inadequate forbearance (eg lenders change their forbearance practices and move more quickly to enforce the payment of a debt), not treated fairly, or put under undue pressure to make repayments through inappropriate debt collection practices.

In response to the transfer to FCA regulation, some consumer credit firms are changing their business models rather than be regulated by the FCA (eg debt management firms switching to offering Individual Voluntary Arrangements). This may lead to poorer consumer outcomes from unregulated or more weakly regulated firms.

Areas of focus

Treatment of consumers in financial difficulty
Our assessment highlighted a number of areas where consumers in financial difficulty were not being treated appropriately. In the mortgage market we have seen examples of overforbearance, where borrowers with little potential to recover are kept in forbearance too long. In debt services, some consumers are put under pressure to repay. We have also seen instances of consumers being sold debt management products that are not cost-effective and that do not meet their needs sufficiently. We will continue to pay particular attention to the treatment of consumers in financial difficulty. A deterioration in household finances would exacerbate these issues, which makes continued monitoring even more important.

Treatment of existing customers
We observed changes in the market that mean some mortgage borrowers (such as interest-only customers) may suffer financial detriment from difficulties in remortgaging.

Restricted access to credit and services
Our assessment highlighted how external drivers of change had a direct impact on consumers (through changing risk appetites among lenders, or their responses to regulatory change). This may lead to consumers who could once afford credit having trouble accessing products and services they need. Consumers who are new to credit may also struggle. We are also concerned that changes in the provision of consumer credit and debt services (following the transfer of regulation to the FCA) may have resulted in reduced access to the less mainstream consumer credit products, and to debt services for some consumers. We will continue to monitor the way these markets develop as FCA regulation embeds.

Lending practices
We continued to see instances of some consumer credit firms not conducting adequate affordability assessments, which can lead to consumers taking on unsustainable financial commitments. This will continue to be an area of focus and action for us.

Complexity and lack of transparency
We are concerned that the complexity and a lack of clear information may mislead consumers about the nature or value of products, services and add-ons. This makes it more difficult for consumers to compare products and services – and so weakens the impetus for firms to compete in improving the quality and nature of the products and services consumers need, or in the prices at which they offer those goods and services. This is a particular issue where products have different target markets, loan terms, routes to market, and fees and charges. Given the possible implications for consumer harm and market integrity, we will continue to focus on the importance of firms providing clear information that does not mislead.

Conflicts of interest and misaligned incentives
We have seen instances where firms' remuneration models and/or their financial arrangements with third parties do not always place enough importance on positive consumer outcomes. This may lead to firms not acting in consumers' interests.
We are concerned that some firms do not have adequate controls in place – or an appropriate culture to mitigate conflicts of interest or the risk of such conflicts arising.

Firms' business models
Our assessment highlighted instances of consumer credit firms employing aggressive strategies focused on short-term profitability without taking account of the risks to consumers. This is driven largely by poor culture and inappropriate business models.

This can lead to business models that are designed to exploit demand-side weaknesses and/or to work around regulation, and we will be paying close attention to developments in this area.

We continued to see instances of some consumer credit firms not conducting adequate affordability assessments, which can lead to consumers taking on unsustainable financial commitments. This will continue to be an area of focus and action for us

General insurance and protection
Sector View

The general insurance and protection sector provides cover for individuals and businesses against the cost of uncertain and unpredictable events. The sector underwrites over £80 billion a year in the UK and overseas.[1] The UK is a significant market both in Europe and globally.[2]

We divide the sector into three sub-sectors: retail, commercial and wholesale. The retail sub-sector provides insurance to individuals and households. Commercial serves smaller businesses (sole traders, micro-businesses and SMEs), and wholesale meets the insurance needs of the largest and most complex businesses, including multinationals. The sub-sectors are interconnected, although each has a distinct market built around the consumers it serves and the products and services it provides.

The sector as a whole meets five core needs:

- protection of assets against loss and damage
- protection from loss from harm to the person (injury, death, ill health, medical, dental)
- protection from other financial loss (including reinsurance)
- liability insurance (ie indemnity for civil action, defence costs etc)
- compliance with public policy (compulsory insurance for protecting the general public and employees)

The retail sub-sectors

Consumers
Almost all consumers hold some form of insurance at some stage of their lives. Older, more affluent consumers are the most likely to have insurance cover; 87% of these consumers have home insurance compared with just 26% of consumers in the 'Hard Pressed' segment of our Spotlight Model.[3]

Products
Motor and home insurance are the most widely held retail products in the UK. Over 20 million drivers have motor insurance policies,[4] 90% of which are for comprehensive cover.[5] The average cost of a comprehensive policy fell between 2012 and 2014 (from £442 to £398) but began to rise again in 2015, when the average cost of a policy was £427.[6]

Home insurance is the second largest market. Of the 26.7 million households in the UK in 2013, over 17 million had buildings insurance and 20 million had contents insurance.[7] The market remained broadly static between 2011 and 2014. In 2016, the ABI estimated the average annual premium for buildings insurance was £254, contents £138, and combined policies £309.[8]

1. Total Market Statistics, ABI (2015).
2. Key Facts, ABI (2016). The UK is the fourth largest insurance and the largest long-term savings industry in the world.
3. Consumer insight data, FCA (2013).
4. Key Facts, ABI (2016).
5. Motor Insurance UK, Mintel (March 2016).
6. Average motor insurance premium tracker, ABI (Q1 2016) .
7. Key Facts, ABI (2016).
8. Average household insurance premium tracker, ABI (Q2 2016).

Protection insurance protects consumers and their families against the impact of events such as illness, accident, unemployment and death. Over 15 million policyholders have whole life policies (which pay out on death).[9] Slightly fewer consumers (11.6 million) have term assurance, which typically covers outstanding mortgage debt in the event of early death.[10] Other forms of protection, such as income and critical illness cover, are less widely held, with 3.2 million and 0.8 million policies in force respectively.[11] Accident and health is another major part of the retail sub-sector, providing cover in the event of ill health, injury and death. This includes 5.1 million consumers with private medical insurance.[12]

Speciality insurance such as pet, gadget and travel insurance is not held in the same volumes. However, pet insurance is a growing market, with over 3.4 million policyholders. [13]

How retail consumers access products and services

Consumers can choose from a range of channels through which to buy their insurance. Although price comparison websites play a major role in new sales of motor insurance, around half of policy renewals are retained by existing insurers. Price comparison websites also feature prominently in home insurance, although to a slightly lesser extent. Around 25% of new business comes directly from these websites, with a similar proportion sold by retail banks and by insurers directly.[14] In both motor and home, the direct channel is seeing a resurgence, driven largely by auto-renewals and lower premiums in recent years. Consumers tend not to seek advice when buying these products.

Advice plays a more significant role in the protection market. Independent advice is the largest distribution channel, accounting for just under half of new mortgage-related term assurance sales and two thirds of other term assurance products. By contrast, 84% of whole life policies are sold through non-advised channels.[15] Restricted (non-independent) advice is another significant channel, particularly in mortgage-related term assurance.

Firms

There are 340 authorised providers of general insurance (with an additional 563 headquartered in Europe and passporting in under Solvency II).[16] Despite the presence of several big, well-known brands, these markets are highly fragmented. A number of firms have both an insurer and an intermediary within their group, and some price comparison websites are owned or part-owned by insurers. The intermediary market is also fragmented.

In the private medical insurance market one provider holds a market share of over 40% [17], while two firms dominate the income protection[18] and term assurance markets.[19] Pressure on market share has led firms to consolidate, expand their offerings or leverage other non-insurance propositions. Others have changed their distribution models by, for example, removing branch-advised sales and investing in online platforms.

9. Business in Force – Full Results, ABI (2015).
10. Business in Force – Full Results, ABI (2015).
11. Business in Force – Full Results, ABI (2015).
12. Key Facts, ABI (2015).
13. Key Facts ABI (2015)
14. UK Personal Lines Insurance: Distribution and Marketing, GlobalData (2016).
15. Protection Overview Tables, ABI (Q3 2016).
16. Key Facts, ABI (2016).
17. Private Medical Insurance UK, Mintel (October 2016).
18. Income Protection UK, Mintel (February 2017).
19. Term Assurance UK, Mintel (June 2015).

There are 340 authorised providers of general insurance (with an additional 563 headquartered in Europe and passporting in under Solvency II)

The commercial and wholesale sub-sectors

Consumers

Business consumers are particularly diverse, ranging from sole traders and SMEs through to the largest corporates and multinational businesses. The commercial sub-sector serves the UK's 4.1 million sole traders, 1 million micro businesses and 240,000 SMEs.[20] These smaller businesses are engaged in a wide variety of activities, from online businesses through to agriculture, manufacturing and financial services.

The wholesale sub-sector has global significance, serving the needs of the largest and most complex multinational businesses around the world. The sector underpins the functioning of global aviation, marine and energy markets, and provides alternative and reinsurance cover to international markets.

Products

Commercial products protect firms from financial loss, including their liabilities to third parties and employees. The most widely held commercial products are property insurance and employers' liability insurance (both of which are held by around two thirds of SMEs) and public and product liability insurance.[21] Smaller firms tend to buy generic packaged products or products that are designed for a particular trade (such as hairdressing).

Larger corporates tend to require bespoke contracts tailored to their needs, and the wholesale sub-sector offers multiple classes of businesses with thousands of sub-classes. Each sub-class operates as its own separate market with its own dynamics and legislative, technological and macro-economic drivers. Cyber-insurance is increasingly prominent as firms face growing liability to their consumers for data loss and other losses caused by hacking.

Reinsurers essentially provide 'insurance for insurers'. They enable insurers to limit their exposure to a large individual claim (or series of claims) and provide capital and support of growth in risk. Virtually all reinsurance business in the UK is carried out in London because of its concentration of expertise in the broker and (re)insurer markets.

How business consumers access products and services

The size of a business and its activities determines its buying patterns and its access to the market. Most commercial insurance is sold through intermediaries.[22] Although the phone remains the most popular way for SMEs to access insurance products, a growing proportion (just over a third in 2015) are choosing to buy online.[23]

Commercial insurance supply chains often involve multiple parties with overlapping boundaries. This

20. Business Population Estimates for the UK and Regions, Department for Business Innovation & Skills (2016).

21. Detailed Premium Analysis, ABI (2013).

22. Product Distribution, ABI (2015).

23. UK SME Insurance Survey, GlobalData (2015).

Figure 2: UK general insurance and protection: total commercial and wholesale sub-sector GWP:

	Commercial motor	Commercial property	Liability	Commercial pecuniary loss	Reinsurance	Marine, aviation and transport
2014	**£4.7bn**	**£14.1bn**	**£15.8bn**	**£1.1bn**	**£16.0bn**	**£8.7bn**
2013	£4.8bn	£14.5bn	£15.8bn	£1.0bn	£16.2bn	£9.6bn
2012	£5.1bn	£13.4bn	£14.1bn	£0.9bn	£16.1bn	£9.5bn
2011	£4.7bn	£12.7bn	£13.4bn	£0.9bn	£13.8bn	£9.0bn

Source: FCA estimates of the size of the sector based on PRA returns, published ABI data, Lloyd's of London annual report, including EEA branch income and FCA estimates.

complexity may not be apparent to the consumers, whose business may pass through a long chain of intermediaries before it is underwritten.

Commercial distribution channels have undergone significant change in recent years. Insurers have sought to automate the underwriting of more generalised parts of their business, using automatic-rating models, to deliver quotes electronically without the need for human intervention. In some instances the whole transaction can be completed online.

There has also been innovation from new web-based brokers and direct insurance models aimed primarily at micro-SMEs, and some retail insurers have begun to offer more commercial products, such as commercial van insurance, through price comparison websites.

Managing general agents (MGAs) are becoming an increasingly important part of the commercial supply chain. Insurers delegate underwriting responsibilities to MGAs in return for a fee and/or profit share. Traditionally, MGAs provided niche products but have recently been set up to offer more generalised products. MGAs are not subject to the same regulatory requirements as insurers.

Firms

The largest commercial insurers offer products that cover the vast majority of business needs, and are therefore in a position to provide either packaged or standalone products to consumers. Outside these largest firms, however, the complexity of consumer needs leads many insurers to specialise in particular trades or professions. There has been extensive mergers and acquisitions activity
in the insurance sector in recent years, as firms have sought to gain economies of scale and diversify their insurance risks.

The wholesale market is fragmented, although the larger firms dominate the market. There are nine key global firms (based in London) in the pure reinsurance market. Certain sub-classes or speciality lines may be fairly concentrated due to the specialised underwriting they require, such as specialised marine insurance. The top insurers derive a significant part of their income from the Lloyd's market.

Lloyd's houses 106 syndicates which, in 2015, wrote £26.7 billion of gross written premiums, with profits of £2.1 billion on behalf of their (largely corporate), members who provide the capital to support the underwriting.[24] Most business placed at Lloyd's is placed through brokers who facilitate the risk-transfer process between clients (policyholders) and underwriters.

Downward pressure on premium rates and low investment returns have had an impact on Lloyd's results. However, the focus on underwriting discipline remains a priority, along with the need to respond to new risks and pressure brought by rapid advances in technology. Lloyd's is currently undertaking a range of market modernisation efforts, including the updating of its operating model to make it easier and quicker for firms to conduct business.

Within the commercial sub-sector, the role of intermediaries is evolving. Although a handful of brokers dominate the distribution channel, larger wholesale brokers are targeting certain products (such as cyber) to penetrate the sub-sector and diversify their business models. As competition for traditional wholesale business intensifies, some wholesale brokers are acquiring commercial brokers to gain market share. New entrants and intermediaries backed by private equity are challenging established firms for a share of the value chain.

Drivers of change

Technological advances are bringing new opportunities to the sector, giving firms access to an unprecedented amount of consumer data. In retail, car-telematics are giving insurers increasingly sophisticated data on their customers' driving behaviour and risk profiles. In the protection market, insurers can use Big Data to predict life

Lloyd's houses 106 syndicates which, in 2015, wrote £26.7 billion of gross written premiums, with profits of £2.1 billion on behalf of their (largely corporate), members who provide the capital to support the underwriting

24. Lloyd's of London website (2016).

expectancy and income security with more accuracy. This is likely to have an impact on premiums for consumers, introducing more marked price differences based on the risk a consumer presents.

Access to data is enabling commercial insurers to carry out more sophisticated analytical modelling, capturing risks that had been 'unknowable' and therefore pricing more accurately. In some cases this is enabling insurers to increase their product range.

Technological change also brings risks. Firms are becoming more exposed to cyber-attacks, and new mechanical products and processes – such as 3D printing and driverless cars – may transform the liability potential for reinsurers. These new risks will challenge the wholesale industry as it gains experience in managing these new exposures.

As well as creating opportunities for existing firms, new entrants to the sector with innovative business models ('InsurTech') have the potential to disrupt traditional businesses models.

Developments in policy and regulation are also having an impact on the sector. New conduct regulation has aimed to address consumer detriment in some areas by introducing additional requirements – particularly in general insurance add-ons and disclosure requirements at renewal. The European Insurance Distribution Directive (IDD), which aims to introduce cross-border standards for insurance across the EU, will bring further change to the sector and impose significantly higher standards. Other developments include the Government's plans to tackle 'compensation culture', measures aimed at improving consumers' access to insurance (eg Flood Re), addressing late payment of claims handling and strengthening the legal framework underpinning the sector.

Consumers' buying patterns are changing, which poses challenges to firms' underwriting. Increasingly, consumers are researching and comparing products and firms online, giving them information to make more informed choices. However, variations in wealth and financial capability may mean that some consumers are less well-equipped to assess their needs or access affordable products. This is particularly relevant in light of our findings that people on lower incomes are more likely to renew with the same provider. An ageing population and millennials interacting with the sector is bringing further complexity.

The challenging economic environment has affected demand for non-compulsory insurance, which has put pressure on insurers' margins. Firms continue to adapt and diversify their business models in response. Some insurers are also increasing the risks taken in their asset portfolios to generate further income (and reserves) for future claims. Insurers' income in the wholesale sub-sector is sensitive to cyclical and structural changes in the economy, including the volume and value of goods traded internationally.

In recent years the (re)insurance market has seen premiums driven down by a major influx of new capital. This 'alternative capital' has been brought largely by hedge funds and pensions funds investing in the sector. Their investment has been driven partly by the introduction of a new framework for insurance-linked securities (ILS) business. The Government is aiming to make London a global ILS hub, competing directly with other global hubs (such as Bermuda, Guernsey and Gibraltar).

Increasingly, climate change and the accompanying risks are crystallising for the sector. In response, insurance providers are enhancing risk models in the light of the uncertainty that environmental change brings.

In retail insurance, price comparison websites have become central to the distribution of core products. It is now harder for insurers to reach consumers in the motor and home insurance markets without paying to list on price comparison websites

Our assessment

Consumers
Across the sub-sectors, a number of factors can leave consumers vulnerable to buying products that do not meet their needs, or to renewing at above-market rates. Low engagement with insurance (particularly at renewal) and limited understanding of complex products can lead to inertia or to retail (and some SME) consumers focusing on the headline price of products without giving enough consideration to whether the products meet their needs. We continue to be concerned with fairness, access and pricing for retail consumers who are vulnerable or who have health-related or other needs. This could be exacerbated through technological changes (such as the use of Big Data).

Large commercial and wholesale consumers generally have more sophisticated needs and capabilities. However, increasingly complex products mean they are still highly reliant on brokers to access the product and service information they need to make decisions.

Firms' intent and behaviour
Insurers across the sector have experienced a squeeze on profit margins. This has been caused by intense competition around headline price for new business, competition from intermediaries for parts of the value chain and adverse market conditions (including low interest rates). Providers have tried to increase profitability by reducing service levels or by introducing dual pricing, administration charges and the sale of add-ons. For intermediaries, commission from insurance providers is still a common element of the remuneration structure which, if not handled appropriately, could provide an incentive for mis-selling.

Across the sector, we have seen some evidence of poor oversight of delegated or outsourced activities, as well as of the activities of Appointed Representatives.

Competition and conflicts of interest
In retail, price comparison websites have become central to the distribution of core products. It is now harder for insurers to reach consumers in the motor and home insurance markets without paying to list on price comparison websites.

Parts of the insurance sector have vertically integrated value chains (where one company owns every part of the supply chain), including arrangements between brokers and MGAs. In commercial and wholesale in particular, horizontal and vertical integration of intermediaries has concentrated their position in the value chain. In particular, the largest brokers hold a large proportion of business accessing the London Market.

Further technological changes could affect competition by, for example, increasing risk segmentation or non-risk price discrimination.

Market-wide drivers
The wholesale insurance market is global in nature, sometimes involving

Consumers at the end of long distribution chains may not understand the roles of different parties and what each of them provides

lengthy and complex distribution chains. This presents challenges to the firms involved, as their insurance activities must comply with UK and local legislation on sanctions, bribery, corruption, terrorism and money laundering.

The general complexity of systems and the existence of legacy systems means that IT resilience and security is an issue across the general insurance sector. The functioning of the London Market is critical to the global economy and could be jeopardised by outages and cyber-attacks.

Recent failures of two EEA firms had an impact on consumers and resulted in significant compensation being paid by the Financial Services Compensation Scheme. Solvency II aims to reduce the incidence of prudential failure and its adverse impact on consumers.

Areas of focus

Across the sector

Operational resilience
Technology is changing the way insurers and other parts of the insurance market work and interact with customers. Firms' operational resilience must remain a critical part of our monitoring activities.

Firms' reliance on complex systems increases their vulnerability to outages and cyber-attack. This can be exacerbated by their reliance on legacy systems, which are often the result of mergers and acquisitions, The outsourcing of functions (such as claims administration) or IT systems can lead to poor oversight of the outsourced activities. This could lead to consumer data being compromised, leading to detriment and reputational risks. We will continue to monitor the way firms are addressing these risks.

Governance and oversight of distribution chains
Insurance is distributed in a range of different ways and can involve numerous (regulated and unregulated) parties across the distribution chain and customer sale/post-sale journeys. Product underwriting, distribution and claims management can all be handled by different parties. Firms may have weak oversight of these complex, fragmented distribution chains, of Appointed Representatives and outsourced activities, and of activities carried out by unregulated third parties (eg claims fulfilment). Consumers at the end of long distribution chains may not understand the roles of different parties and what each of them provides. We will continue to monitor the risks presented by this complexity.

Regulatory arbitrage
Products that perform a similar function to insurance, but which fall wholly or partly outside our regulatory perimeter, can leave a gap in protection or redress at the point of claim. Such products do not carry the equivalents of Financial Ombudsman Service rights or Financial Services Compensation Scheme protection, and this is not always clear to consumers.

In the retail sub-sector

Pricing, suitability of sales and consumer choice
If the sales journey focuses unduly on headline price without the consumer giving due consideration to suitability, a gap in expectations may only be discovered at the point of claim.

New data sources increase the range of factors that can be used for pricing and underwriting of business. Our recent Call for Inputs on Big Data in Retail General Insurance found that pricing based on non-risk factors could disadvantage certain individuals or groups.[25]

Competition dynamics
A dual pricing model where insurers quote lower rates for new business exists in some parts of the sub-sector. Insurers cross-subsidise low premiums for new customers by raising renewal prices for more inert existing consumers.

In some retail markets, particularly motor insurance, the separation of cost liability and cost control means that insurers, brokers or claims management companies representing the 'non-fault' party have no incentive to control costs, and may in fact have incentives to inflate them. Insurers are

25. FS 16/5 feedback Statement - Call for Inputs on Big Data in Retail General Insurance (September 2016).

at a disadvantage unless they do the same, driving a competitive dynamic that can lead to claims inflation and higher premiums for consumers. However, insurers have recently been setting up bilateral agreements to reduce the costs of no-fault claims.

Fairness of access for vulnerable or high-risk customers
Vulnerable customers, or those who present an underwriting risk to insurers, may find it more difficult to identify suitable products or to switch between providers. However, some technological developments (such as more widely available data analytics) may help by enabling firms to develop and sell new products more efficiently to specific groups of consumers.

In the commercial sub-sector

Suitability and advice for SME customers
Sole traders and micro-businesses can behave in similar ways to individual consumers. Increasing standardisation and packaged products can lead to smaller businesses buying cover that does not meet their needs, and to underestimating the levels of cover or sums insured. This leads to a risk that their expectations would not be met when claims are made.

Conflicts of interest
The growth in vertically integrated business models, such as broker-owned MGAs, could increase the risk of conflicts of interest if it results in more suitable or better value solutions being excluded. Vertical integration and opaque remuneration structures can also restrict choice if it leads to business being given to insurers who are willing to pay for services, rather than to those offering greater suitability or value.

In the wholesale sub-sector

Inducements
Relationships and remuneration structures within the London Market can lack transparency. Development of products and services could favour particular providers, rather than those offering the best suitability and value.

Market developments
Market modernisation has the potential to transform market efficiency. It may also improve customer outcomes in terms of placement and claims processing. However, it could give rise to operational resilience challenges particularly where it creates single points of failure. It could also make market entry more challenging for those not able to meet market standards.

Financial crime
Complex relationships with multiple parties gives scope for firms to breach financial crime or sanctions requirements, and makes compliance oversight challenging. Firms can be susceptible to pressure from counterparties outside the UK to weaken their financial crime controls. The current political environment, trade and economic sanctions and increasing threat of terrorism will exacerbate these risks.

Pensions, retail investments and investment management
Introduction and context

Between March and September 2016, the FCA Board approved three connected Sector Views covering the long-term savings and investment landscape. These included Retail Investments, Pensions and Retirement Income and Investment Management.

Since then, we have carried out extensive work across the long-term savings and investments landscape. This includes the Asset Management Market Study, the Assessing Suitability Project, gathering and publishing retirement income data and the Retirement Outcome Review. The breadth and depth of this work has further developed our knowledge base across these sectors.

The Sector Views included here build on this latest intelligence. We have enhanced key data points in Pensions and Retirement Income, updated Retail Investments to reflect the findings of the Assessing Suitability Project, and included the conclusions from the Asset Management Study in the Investment Management Sector View.

Pensions and retirement income
Sector view

The pensions and retirement income sector offers UK consumers a wide range of products and services to help them grow financial assets, and, if they want to take an income, to convert these assets to fund their desired lifestyle during retirement.

Understanding the sector

The sector serves over 34 million consumers and manages around £2.1 trillion of assets and savings. 66% of the working population is enrolled in a workplace pension scheme. 7.8 million retired consumers are taking a regular income, of which 0.6 million consumers are in a drawdown product.[1]

A wide range of Government policy has an impact on the sector, including policies from the Treasury, HM Revenue and Customs and the Department for Work and Pensions. Regulation from the Prudential Regulation Authority (PRA), the FCA, the Pensions Regulator and the European Commission also has an impact on the way the sector operates.

We split the sector into two sub-sectors:

Accumulation
The accumulation sub-sector covers the activities to amass financial assets to provide an income during retirement. There are over 20 million consumers with over £500 billion of assets in defined contribution schemes[2] and £1.3 trillion of assets in defined benefit schemes.[3]

With the introduction of auto-enrolment, the decision to pay into a pension has become more passive as many employees are enrolled into their employer's pension scheme. Other consumers (particularly the self- employed) need to make a more active choice to invest in a pension plan. Some consumers choose self-invested pension plans (SIPPs), which allow them to take a more active role in deciding what their pension is invested in. Some SIPPs allow a broader range of investments such as property and alternative asset classes.

1. FCA Retirement Income Data Request (September 2016).

2. FCA Retirement Income Data Request (September 2016).

3. The Pensions Regulator, The Purple Book (March 2016).

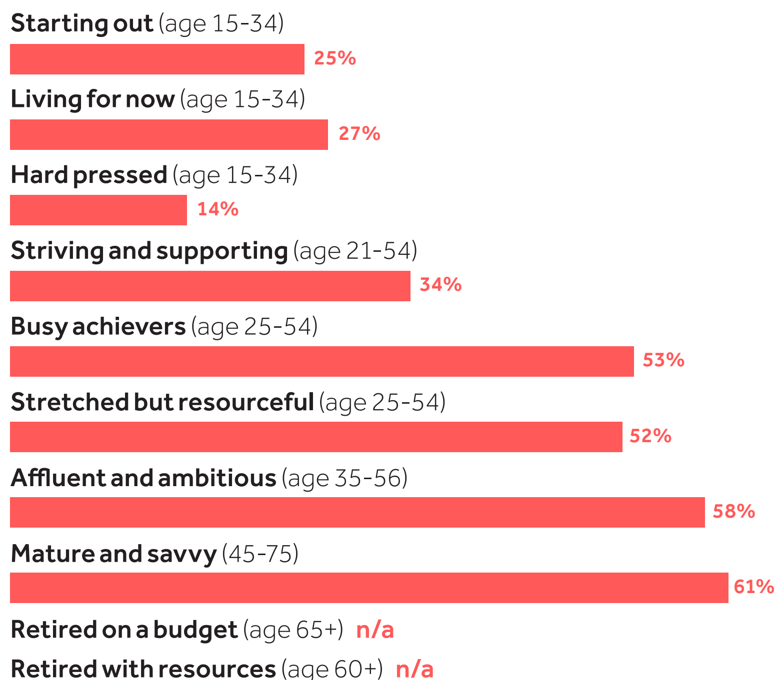
Decumulation

The decumulation sub-sectorfacilitates the conversion of accumulated financial assets into a form that enables consumers to fund their desired lifestyle. There are over 7 million consumers drawing an income in retirement, either from an annuity or through withdrawals from income drawdown. There is over £80 billion of assets in drawdown products[4] and over £300 billion invested in annuities.[5] Since the introduction of the Government's pension reforms, consumers have been free to choose from a wider range of options to take their money.

Consumers

The sector serves a wide range of retail consumers. The chart opposite shows the varying participation and contribution levels of the consumer groups within the FCA Spotlight Model.

Figure 3: Consumer Spotlight
% currently paying into an occupational or personal pension



Retired on a budget (age 65+) n/a
Retired with resources (age 60+) n/a

Range of ages are most prevalent ages.
For more information on our Consumer Spotlight model:
fca.org.uk/publications/research/consumer-spotlight

4. FCA Retirement Income Data Request (September 2016).

5. Synthesys Insurance Returns (December 2015).

Firms

The sector is served by a range of firms including financial advisers, life insurers and asset managers, SIPP providers and platform firms. In accumulation, the top five firms offering employer-based defined contribution schemes had a 68% share[6] of the market in terms of assets under management.

The top five firms providing personal and stakeholder pensions had a 67% share of the market in terms of gross written premiums.[7] In decumulation there were 17 firms offering annuities with the top five having a 68% share of the market by value of income paid out to existing annuities in payment.[8] For drawdown, the top five had a 43% share of the market of assets available.[9]

Products and services

In the accumulation phase there are two main pension regimes: defined benefit and defined contribution. The FCA regulates part of the defined contributions market, which includes providers of, and sales and advice relating to, contract-based personal/stakeholder pensions and SIPPS. Defined benefit schemes are regulated by the Pensions Regulator.

In the past, many private sector employers offered defined benefit schemes, which ensured members had a guaranteed retirement income. However, due to a wide range of factors including increasing life expectancy and low gilt yields, these schemes have proven increasingly expensive to fund and many have been closed to new members.

There are currently 11.5 million members of private sector defined benefit schemes, with 1.4 million active members in accumulation, 5.5 million deferred members (not paying in) and 4.6 million retired members in these schemes. The number of active members accumulating a defined benefit pension in the private sector has fallen by 50% since 2006.[10] This illustrates the declining role of defined benefit schemes for consumers accumulating a pension.

Market share: accumulation

67% The top five firms providing personal and stakeholder pensions had a 67% share of the market in terms of gross written premiums

Market share: decumulation

68% The top five firms offering annuities had a 68% share of the market by value of income paid out to existing annuities

43% The top five firms offering drawdown had a 43% share of the market of assets available

6. OFT Defined Contribution Workplace Pensions Market Study (September 2013).

7. Mintel, Personal and Stakeholder Pensions - UK (April 2015).

8. FCA Retirement Income Data Request (September 2016).

9. FCA Retirement Income Data Request (September 2016).

10. The Pensions Regulator, The Purple Book (March 2016).

Membership of workplace pension schemes increased from 59% in 2014 to 66% in 2016. Although the Department for Work and Pensions had predicted an opt-out rate of 15%, rates have been closer to 10%. Auto-enrolment rollout is now in its third phase and is being introduced to up to 1.5 million small employers in 2017/18.[11] We are therefore likely to see continued growth in the market.

At decumulation, there are six main options that may be open to consumers when they want to access their defined contribution savings: flexi-access drawdown, annuities, hybrid products, blended solutions, full cash withdrawal, and partial cash withdrawal using the UFPLS option.

In the immediate aftermath of the Government's pension reforms, we saw a surge in full cash withdrawals. However, subsequent periods have shown a fairly consistent pattern in consumers' choices of retirement income options.

Consumers' choices appear to be driven in part by their age and the size of their pension pot. Around 90% of full cash withdrawals are made by consumers with a pension pot of less than £30,000, and around 97% have less than £50,000. Consumer demand for annuities appears to increase up to pot sizes of £100,000, where around 30% of consumers purchase an annuity, but then declines as the size of pension pot increases further. Demand for flexi-access drawdown increases with pot size across the board. While drawdown is a more popular choice overall, a higher proportion of consumers aged 65-69 chose an annuity in each of the past four quarters.[12]

Consumers may have multiple defined contribution pots and additional sources of pension income from defined benefit schemes, the state pension and a partner's pension. They may also have other income at retirement including, for example, income from equity release, buy-to-let investments, inheritance and savings in ISAs and other investments.

Drivers of change

Firms are able to use technology to reduce costs and to improve functionality for customers. This may be attractive for some customers. However, others may be unable or unwilling to interact digitally, which means they will miss out on the benefits.

Although consumers are being encouraged to save at the accumulation stage (through automatic enrolment), changes to the tax treatment of pension contributions for higher earners (including the reduction in the lifetime allowance) may lead to alternative investment strategies becoming more attractive to these consumers or removing the incentive to save long-term. On the supply side, we have seen some providers exit the annuity market because of a variety of factors included increased capital requirements, move to asset management business models and falling demand following the Government's pension reforms. At decumulation, there is an increasing need for advice and guidance following the introduction of the Government's pension reforms. Changes to the Pension Wise offering and recommendations from the Financial Advice Market Review (FAMR) may help address this gap.

Continued low interest rates and poor earnings growth (compared with historic norms) pose longer term challenges for consumers' interactions with the sector. These factors influence consumers' ability to save for the long term, and constrain the returns generated on investments.

The distinction between accumulation and decumulation is becoming increasingly blurred by changes in the labour market (the growth of more flexible and less stable forms of employment), and the decline of traditional cultural norms in retirement. Retirement is no longer necessarily the sole trigger for accessing pension savings, and more consumers may begin to access pension pots while they are still working.

11. Automatic enrolment: commentary and analysis 2016, the Pensions Regulator (March 2016).

12. FCA Retirement Income Data Request (September 2016).

Given the value of assets under management in this sector, and the recent changes which give consumers over 55 access to their pension savings, there is scope for significant side effects to be felt outside the pensions sector

With rising life expectancy and increased consumer exposure to longevity risk, the need to accumulate sufficient pension wealth is becoming increasingly important, particularly given the decline in defined benefits schemes. Continued labour market challenges are likely to lead to difficulties participating in the sector and providing for retirement for those who are less well off.

Our assessment

Consumers

Faced with an increasing range of options and a market undergoing continued change, making decisions about retirement income can be daunting and challenging for many consumers. Many still find it difficult to balance longevity and investment risks, and to work out how much they need to save during accumulation to fund their desired lifestyle in retirement. However, we are seeing some positive signs of increasing consumer engagement.

Poor decision-making at decumulation may lead to consumers running out of funds, particularly given the trend to enter drawdown without advice. A combination of inertia and the need to make complex decisions at decumulation may discourage consumers from shopping around for the best available option.

The Government's pension reforms have increased the complexity of the decisions consumers need to make at retirement. This means that an increasing number of consumers will need support and guidance, but may not be willing or able to afford traditional forms of advice.

If demand for advice grows faster than supply, some of the most vulnerable market participants may be left without access to adequate advice. This is being addressed through Pension Wise and FAMR implementation work. Since the pension reforms came into effect, many more consumers have been looking for help to navigate the increasingly complex set of choices they need to make– although this may not always involve advice (shown by the increasing numbers of non-advised drawdown sales).

Firms' intent and behaviour

Firms' have adapted well to the introduction of the Government's pension reforms. However, given the degree of consumer inertia identified in our assessment, we would like to see good consumer outcomes feature more prominently in firms' decision-making.

We have observed that some firms are not giving sufficient consideration to consumer outcomes as they make changes to their business models, particularly since pension reforms came into effect.

Market-wide drivers

The blurring of the line between accumulation and decumulation means there is no single trigger point for challengers to target potential customers. This is making it harder for these challenger firms to attract consumers from existing providers, and particularly from large insurers. The growth in demand for income drawdown has the potential to encourage asset managers to enter the sector. Where there has been entry these providers focus mainly on the advised sector of the market.

Recent policy developments have had a significant impact both on demand and supply-side dynamics in the sector. These and any future developments could increase uncertainty among consumers.

Given the value of assets under management in this sector, and the recent changes which give consumers over 55 access to their pension savings, there is scope for significant side effects to be felt outside the pensions sector. For instance, if more retirees choose to invest in buy-to-let properties, this could affect the housing market.

Areas of focus

Sales and advice

Consumers may not have sufficient access to advice to enable them to choose the best option. This is driven by an absence of easily accessible and affordable advice, behavioural biases and the quality of the guidance provided by firms and government agencies. Less affluent consumers may be particularly vulnerable.

Value for money

Consumers may be unable to assess value for money because cost information is not disclosed, or is difficult to understand. It is vital that cost information is clear to consumers during accumulation and in decumulation.

Business model changes

Consumers may be affected by a transition to new business models, which could bring risks as well as benefits. There are two broad trends. Firstly, some insurers are shifting to capital-light asset management business models. In some cases this involves new online propositions and re-platforming. This may involve bulk transfers of customers to new propositions, which carries the risk that some customers may lose out as a result. Secondly, there is a trend towards more integrated supply chains, which may discourage customers from shopping around when they move from accumulation to decumulation. This may increase the risk of receiving poor value for money.

Scams and fraud

Complex decisions combined with limited financial capability may make some consumers susceptible to fraudulent products, which may lead to them losing their pension assets. Consumers' continued susceptibility makes continued monitoring necessary.

Sustainable retirement income

There is an increasing risk that consumers may not accumulate adequate funds to meet their needs in retirement. It is difficult to predict future lifestyle needs, and it may simply be difficult for some consumers to save more.

Consumer confidence in pensions

Consumers are less likely to save if they are uncertain and lack confidence. Sustained change in the pensions sector may lead to uncertainty, which could lead consumers (and particularly the self-employed) to seek out alternative savings products.

Reduced competitive pressure

In decumulation, consumer inertia and a limited number of new entrants may limit competitive pressure and reduce the pressure to innovate. As the market settles down after the implementation of the Government's pension reforms, firms may focus on customer retention at the expense of product innovation.

Retail investments
Sector view

The retail investments sector enables individuals to grow the value of their assets and, if they wish, to obtain an income through investing. Typically, investors seek higher returns than are available from cash savings, but unlike cash, investments do not normally provide a guaranteed return. The sector offers consumers exposure to a selection of investment opportunities and consumers bear the risk of the investment return not meeting their expectations.

Approximately 12.6 million British consumers have retail investments products,[1] equating to 25% of the British adult population. Retail investment products are worth approximately £1.8 trillion in the UK.[2] This compares to £1.5 trillion held in cash deposits and savings accounts.[3]

The sector is regulated by the FCA, the Competition and Markets Authority and the Prudential Regulation Authority, which implement a range of domestic and European regulations such as MiFID II, AIFMD, and UCITS IV. The Treasury and HM Revenue and Customs implement Government policy across the sector.

Consumers

Consumers tend to invest once they have met their needs through other savings and investment options, such as pensions and cash savings.

Consumers with retail investments tend to be older, male, have a higher educational status and be wealthier than average. Five specific Consumer Spotlight segments account for most of the demand for retail investment products: 'Retired with Resources', 'Affluent and Ambitious', 'Mature and Savvy', 'Stretched but Resourceful' and 'Busy Achievers'.

Consumers in these segments are more likely than other groups to seek out financial advice. Investments within the sector are concentrated in a small number of high net worth individuals; 32% of total savings and investments are held by 0.6% of the UK population.[4]

Evidence suggests that people often decide to invest following a change in disposable income or wealth, and a salary increase or bonus is likely to trigger an investment decision. However, our data shows that for a third of consumers, the most important factor is simply the decision to spend less and save more.

Firms

There are three distinct services provided in the sector: the provision of investment products; services (such as platforms) that provide access to, and ongoing administration of those products; and the provision of advice and guidance to help consumers select which products and services to buy. Advisers and discretionary investment managers also provide

1. GFK Financial Research Survey, six months ending June 2016 data. Retail investments definition: any investment product, any alternative investment (excluding property bought-to-let), unit linked endowment or Premium Bonds.

2. FCA calculation based on various sources: a) Nesta and University of Cambridge, Alternative Finance Report (2014); b) Datamonitor (2015); c) UK Government (2015); d) Investment Association (2015); e) NS&I website (Oct 2015); f) FCA returns data (2015); g) FCA Supervisory estimates (2015).

3. Bank of England data taken from Moneyfacts Treasury Report (October 2016).

4. 'Wealth in the UK: sizing the market opportunity', GlobalData (September 2015).

services that monitor or manage the ongoing suitability of the investments for consumers.

A wide variety of firms operate in the sector. The number of vertically integrated firms (firms within the same group that both manufacture and distribute their own investment products) is increasing as product providers seek direct relationships with consumers and intermediaries develop their own in-house investment solutions.

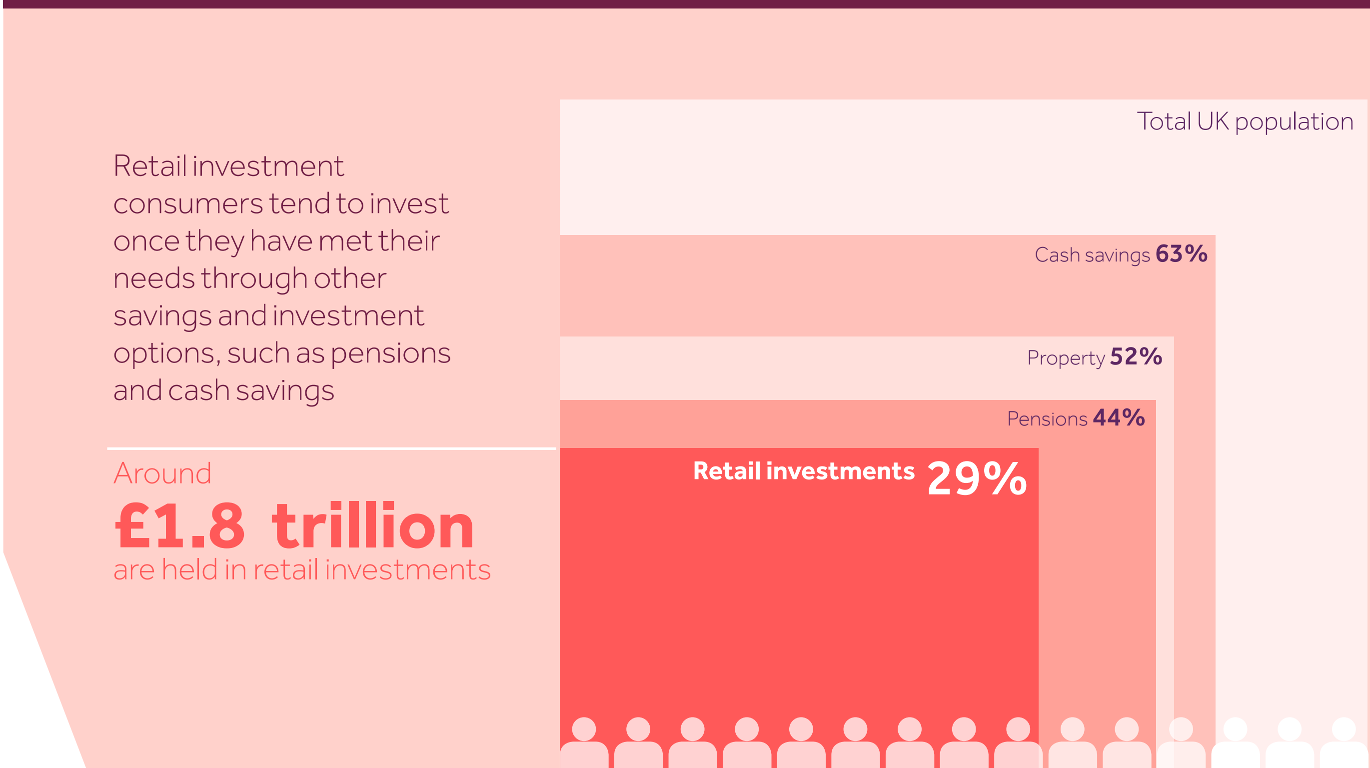
Firms offering advice services have a wide range of business models. They also vary significantly in size, with 11% of advisers operating as sole traders.[5] Some advice firms offer independent advice (providing unbiased advice based on a comprehensive analysis of the relevant market). Others offer restricted advice on a narrower range of products, and some recommend only in-house solutions.

Vertical integration may take different forms, which results in different business models. There may be an element of rational sequencing involved. For example, tax wrapper providers who offer in-house investments evolve their business models into wider retail investment and platform distribution.

32%
of total savings and investments are held by 0.6% of the UK population

5. The financial advice market in numbers 3.0, APFA (2015).

Figure 4: How consumers save



Source: FCA Consumer Spotlight Data 2015.

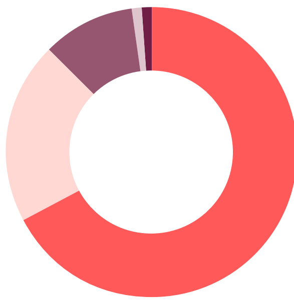


Figure 5: What consumers buy

Collective investment schemes	66%	(£1,061bn)
Direct holding in stocks or fixed income products	20%	(£324bn)
Investment bonds	10%	(£156bn)
CFD	>1%	(£2.8bn)
Crowdfunding	>1%	(£1.5bn)

Sources: UK Leveraged trading report, 2014. FCA Returns data. Investment Association, 2015. AltFi, 2015.

Vertical integration is not exclusive to the largest firms in the sector, with some smaller players also adopting this approach.

Products and services
Figure 5 shows the range of products and services offered by the sector, and their relative sizes.

Drivers of change

Technology is changing the way firms interact with consumers, improving analytical capabilities and transforming the way transactions are processed. The use of automated advice solutions has the potential to transform the market and establish itself as a mass-market proposition. Better technology is delivering more information and a wider choice of products to consumers and their advisers.

The growing availability of sophisticated analytical tools at low cost gives more opportunities for self-directed consumers to make decisions without using advice. Platforms often make these tools available for free to attract new clients or to encourage existing ones to invest more. Product providers may also use new analytical technology to develop more complex investment products and use platforms to market these directly to investors. However, greater use of technology also leads to increased exposure to cyber-crime, system outages and resilience issues.

Government policy exercises considerable influence over whether and how consumers save and invest. Tax incentives influence the relative attractiveness of pensions, property, ISAs and 'unwrapped' investments that consumers must navigate. Material changes to the relative tax treatment of retail investments may be a precondition of major growth in the sector.

The trend of Government policy and employer practice has been to transfer the responsibility for saving for retirement to individuals. In addition, welfare cuts, the closure of defined benefit pension schemes, the rise of auto-enrolment in defined contribution schemes and the Government's pension reforms signal a further transfer of responsibility to individuals. A large number of consumers will be accessing relatively small pension pots, for which getting regulated advice may be prohibitively expensive.

The transfer of responsibility to individuals, the complexity of the tax system and the Government's decision to broaden the scope of ISA eligibility to riskier assets mean that consumers' need for advice is likely to become more acute.

Socio-economic factors play a vital role in determining consumers' willingness to invest, and the amount of money they have available. It is estimated that 13% of the British population holds risk-based

investments (down from 21% in 2006).[6] A decline in real average earnings, combined with higher levels of indebtedness, may have left consumers with less surplus income to invest.

Alternative choices remain more popular with UK savers. High property prices may be encouraging younger savers to use cash products to save for a deposit on a property and then save for the long term through property ownership. Younger people are also leaving education with more debt than previous generations, which may delay their ability to participate in the sector. The changing balance between savers and retirees implies a broader shift towards the decumulation of wealth. The sustained increase in female labour-force participation, and the resulting increase in women's wealth, is expected to increase women's participation in the sector.

Yields on fixed-income investments have declined, which in turn has reduced yields on most other investments. The investment industry has responded by creating new products designed to enhance yield, the complexity of which may discourage retail investors or result in mis-selling or 'mis-buying'.

Our assessment

Consumers
Some consumers may find it difficult to assess their current needs, or may have a biased perception of what their future needs are likely to be. This can increase the likelihood of them buying unsuitable products. Although there is a wide range of comprehensive information available about products and distribution, some consumers may find this difficult to filter. The different charges linked to distributors can also make it difficult to assess products.

Consumers who buy regulated advice or wealth management services would normally be guided through the assessment of their needs. Many consumers, however, may be unaware that they could benefit from advice, or it may not be available to them.

It can be difficult for consumers to obtain information about the quality of advice. Such information is not available from published sources and can be difficult to verify even after purchase. This means that the total cost of the solutions (including advice) may only become apparent at a late stage of the sales process, when the consumer may have already made the decision to buy.

Costs and other barriers to switching mean that consumers can face a trade-off when considering changing their provider. These costs can take different forms, including entry and exit barriers (eg fees to transfer securities, transfer times), high search costs in the market for advice, or fiscal implications (such as capital gains) when selling products. Inertia and loss aversion also play a role in preventing consumers from switching between products and providers.

Entry fees are common, especially for consumers who take advice (either from advisers or wealth managers). More than 80% of advisers charge an upfront fee, which according to data collected by FAMR, is normally 3% (median value) of the assets.[7]

Competition
Despite the low levels of concentration and the absence of dominant players in the sector, providers of advice and products may have some room to maintain high prices or poor quality without losing business to their competitors. Firms offering face-to-face advice may have a degree of market power in geographical locations where the number of providers is extremely limited.

Platforms' increasing scale and influence over consumers' choices may allow them to negotiate better deals with product manufacturers (buyer power). However, the Asset

6. GFK Financial Research Survey, six months ending December 2006/16. Data based on adults 18+. Risk based investment includes any investment product, unit linked endowment or with profits endowment. 2016 percentage also including any alternative investment (excluding property) is 18%.

7. FAMR survey of firms providing financial advice (February 2016).

Management Market Study interim report found that although retail platforms can secure discounts on fund charges, this practice is not widespread. It is not clear that retail investors benefit fully from the economies of scale available to platforms.

Although prices in various areas of the sector seem to be clustered around certain levels, our analysis suggests that this is mostly the result of poor competitive pressures exercised by the demand side.

Implementation of the Retail Distribution Review (RDR) removed a significant cause of conflicts of interests by changing the way advisers and platforms are paid. However, increasing vertical integration between product manufacturers and distributors has the potential to reintroduce some of these risks.

Market-wide drivers
The importance of reputation and the high cost of client acquisition offer significant advantages to incumbents, and mean that entering into new markets (within the sector) is easier for firms with an established client base in a neighbouring market (eg a retail bank entering into the investment advice market, or an asset management firm setting up its own platform).

Policy and regulation is having a significant impact on the sector. The RDR facilitated price competition in some areas through increased transparency, and also increased entry requirements for advisers. The Government's pension reforms require consumers to make complex and difficult decisions about their pensions. While this might lead to better outcomes for some consumers, it may also increase the likelihood of some consumers making poor decisions.

Changes to the tax policy around property investment may increase consumers' appetite for retail investments. By seeking to increase consumers' protection, the Prospectus Directive has had the unintended consequence of limiting retail investors' access to equity and debt primary markets.

The implementation of FAMR's recommendations may significantly change the regulatory landscape for the provision of support, including regulated advice, with an aim of widening its accessibility and improving affordability.

Firms' intent and behaviour
Regulatory interventions have improved firms' policies and procedures. In the advice market, regulatory and industry efforts to improve professionalism and standards of qualification are driving improvements in the quality of the service provided. However, opaque and complex charging structures often make it difficult for consumers to compare providers, which can result in consumers being charged more than they had expected.

Our assessment suggests that risks remain regarding the remuneration of individuals, especially within vertically integrated firms where customer-facing employees could be incentivised to sell in-house products and services.

Areas of focus

Suitable advice
Some firms may not be providing suitable investment advice consistently. Firms offering advice may make unsuitable recommendations because of conflicts of interest or insufficient competence. We have also identified the potential for unsuitable advice being given due to poorly managed or unrecognised conflicts of interest (for example, because of charging structures and vertical integration). We will continue to monitor the suitability of advice.

Awareness of advice
Consumers with small amounts of assets might not have access to, or awareness of, advice that could

benefit them. Our assessment, and the work that preceded FAMR, suggests that a large proportion of consumers lack awareness of, and access to, financial advice. We will continue to gather evidence to determine whether this is causing detriment to consumers.

Value for money
Consumers who take advice may not be getting value for money. Some advisers may not pay enough attention to value for money when they make personal recommendations to consumers.

Relatively few advisers are transparent about their pricing before they sell advice. This does not incentivise advisers to compete on price and may result in limited pressure on them to reduce their charges.

Self-directed consumers
Self-directed consumers may buy products that are not appropriate or that offer poor value for money. Limited comparability and ineffective disclosure can also lead to non-advised consumers buying products that are not appropriate for them, or that they do not fully understand. The risk can be heightened if firms present information in a way that does not help consumers make an assessment or that takes advantage of behavioural biases. Consumers may also end up paying more than they had expected because of limited means to compare products, and the complexity of some charging structures.

We also noted that consumers who trade products listed on exchanges pay high charges compared with those in other countries, and firms offering share dealing services often fail to deliver best execution. Clients of wealth managers and stockbrokers are likely to face similar issues.

Governance
Some firms may have poor product governance arrangements, which means consumers' interests are not properly addressed. Consumers' needs and outcomes may not be properly considered when firms are developing and reviewing products and distribution propositions. We have identified instances of poor product governance in structured products, crowdfunding and peer-to-peer markets. This can lead to firms marketing poorly designed products, or not taking sufficient steps to make sure products reach the right consumers.

Some firms charge legacy customers more than new or prospective customers, or allocate higher running costs to legacy products.

Client money
Consumers may be at risk of losing money both from scams or as a result of firms failing to meet our CASS (Client Assets Sourcebook) requirements.

Regulatory interventions have improved firms' policies and procedures. In the advice market, regulatory and industry efforts to improve professionalism and standards of qualification are driving improvements in the quality of the service provided

Investment management
Sector view

Our initial Sector View for investment management was presented to the FCA Board in May 2016. At this point, work was underway on our Market Study into Asset Management in the UK. The Market Study significantly enhanced our knowledge base and understanding of how the asset management market operates. Figure 6 shows the areas covered by the Market Study and the areas covered by the Sector View.

Our current Sector View therefore consists of the findings set out in the Interim Report for the Asset Management Market Study, together with our assessments in our original Sector View of the markets providing administration/ancillary services and third-party products and services to asset managers.

The Asset Management Market Study: interim report findings[1]

The UK's asset management industry manages nearly £7 trillion of institutional and individual assets. Over three quarters of UK households with occupational or personal pensions use the services offered by asset managers.

We undertook a Market Study to assess whether competition is working effectively. It looked at whether institutional and retail investors get good value for money when purchasing asset management services. Our interim findings were that:

- There is limited price competition for actively managed funds, meaning that investors often pay high charges. On average, these costs are not justified by higher returns.
- There is stronger competition on price for passively managed funds, though we did find some examples of poor value for money in this segment, fund objectives are not always clear, and performance is not always reported against an appropriate benchmark.

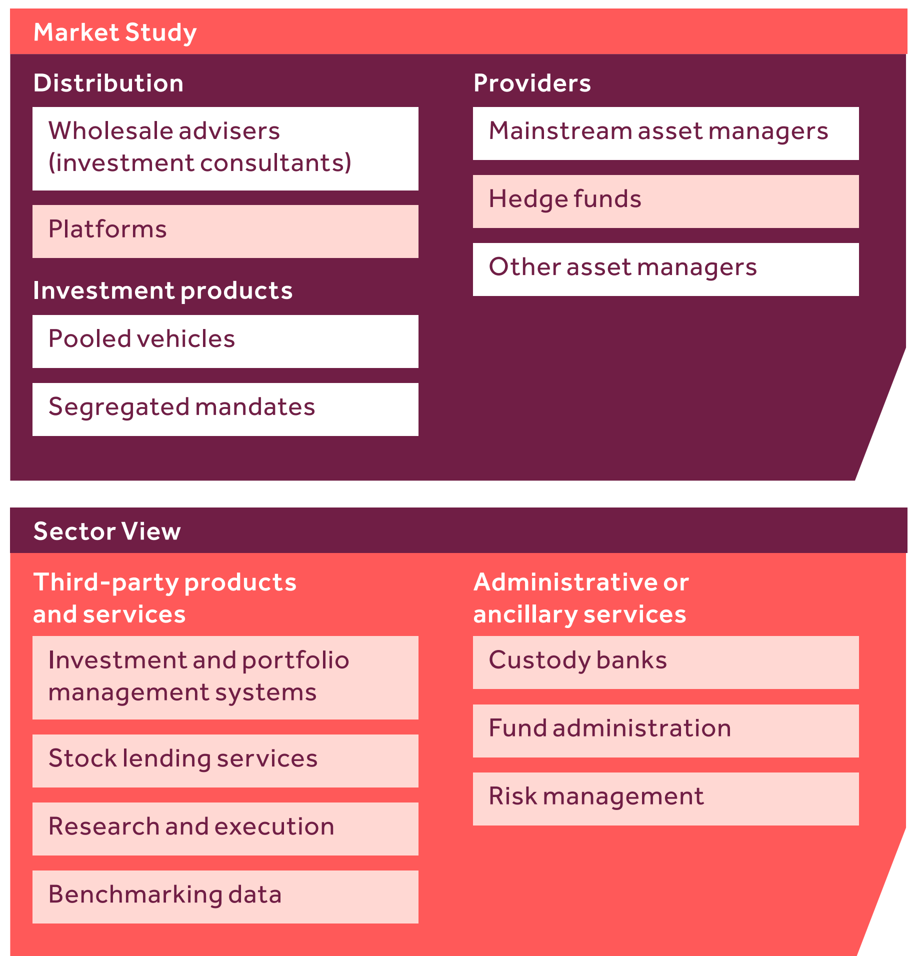
1. https://www.fca.org.uk/publications/market-studies/asset-management-market-study

- Despite a large number of firms operating in the market, based on our sample, we found evidence of sustained, high profits over a number of years.

- Investment consultants undertake valuable due diligence for pension funds but are not effective at identifying outperforming fund managers. There are also conflicts of interest in the investment consulting business model which require further scrutiny.

We consulted on the findings and proposed remedies in the interim report, and will publish the final report and any proposed rule changes later in the year.

Figure 6: Areas covered by the Market Study and by the Sector View



Administration and ancillary services

The administration of investment portfolios (fund administration) involves recording who owns the portfolio, safeguarding title to portfolio assets (custody), implementing transactions on behalf of portfolios and the valuation of portfolios.

To operate a portfolio, administrators must maintain a record of the interests of investors in the portfolio, and record cash inflows and outflows. Retail portfolios have multiple numbers of end-investors and recording their interests is known as transfer agency. Pension portfolios also have multiple numbers of investors and operators and maintain their own records or outsource the function to investment consultants.

Safeguarding title to the assets of the investment portfolio is undertaken principally by custody banks. All portfolios need to ensure their assets are kept safe from misappropriation or misuse and are properly segregated from those of service providers and other portfolios.

The bundling of custody banking services with other administration services raises an important competition question

The holdings of investment portfolios change constantly as a result of transactions or corporate actions (stock splits, takeovers), and portfolios must record and receive income from their holdings. Custody banks must record these changes and facilitate transaction settlement while ensuring each portfolio's title to assets is not endangered.

Almost all portfolios have to produce financial accounts, including valuations. Producing accounts for portfolios is known as fund accounting. Collective portfolios tend to use custody banks for fund accounting, whereas pension and institutional portfolios use a variety of service providers.

Our May 2016 assessment of the markets for custody and administration services concluded that:

- Information is generally available in the market explaining the services and is well understood by investment managers. We are concerned about contractual terms between custody banks and investment managers and there is evidence that terms are more beneficial for the banks.
- There is a small number of custody banks providing services in the market, but we do see evidence that firms compete on price for core custody services. Contracts are usually around 10 years in duration, creating barriers to switching providers.
- Because of low profit margins, many custody banks do not offer core custody as a single service. Instead, investment managers need to sign up for ancillary services such as FX trading and securities lending. There is some evidence that custody banks will charge low fees for core services. Additional revenue generation will be sought from ancillary services.
- The bundling of custody banking services with other administration services raises an important competition question, as it prevents investment managers from being able to shop around to obtain more competitive offers.
- Low profit margins also deter custody banks from investing in modern technology systems. We remain concerned that the failure to upgrade existing systems could negatively affect the sector, given the concentrated nature of suppliers and the reliance placed on custody banks by investment managers. The reliance on out-of-date systems could create an additional barrier, preventing asset managers from switching to other providers. Considering these switching barriers, the low number of suppliers and the lack of investment in new technologies, the prudential and operational risks associated with a significant service outage within the sector are high.

Third-party products and services

Investment managers gather assets from a range of investors, both retail and institutional, to invest in wholesale markets. Asset managers are major players in the wholesale markets where they both purchase research and execution services on behalf of portfolios and are responsible for the stewardship of portfolio assets invested in wholesale markets.

Investment managers purchase two key services on behalf of investors; third-party research to inform decisions, and execution services to implement decisions in the wholesale markets for their portfolios. Portfolios pay for these services through transaction costs on top of the annual management fee. These costs have an impact on returns to investors.

Our May 2016 assessment of research and execution services concluded that:

- Information on research and execution costs is limited and complex.

- There is a high number of suppliers of research. MiFID II could reduce the number of research providers but could also result in the growth of specialist providers.
- Some investment managers do not always take action to stop behaviours that lead to poor outcomes for end-investors due to conflicts.
- Research and execution costs are bundled together by the sell-side who cannot provide a clear price to the investment manager. The investment manager is therefore unable to value the services accurately.

Areas of focus

Topics covered by the Asset Management Market Study
The Asset Management Market Study interim report identified a number of areas for further work or potential remedies. We proposed a significant package of remedies that seek to make competition work better in this market, and protect those least able to engage actively with their asset manager. These include:

- a strengthened duty on asset managers to act in the best interests of investors, including reforms to hold asset managers to account for how they deliver value for money
- introducing an all-in fee so that investors in funds can easily see what is being taken from the fund
- a number of measures aimed at helping retail investors identify which fund is right for them, such as requiring asset managers to be clear about the objectives of the fund, clarifying and strengthening the use of benchmarks and providing tools for investors to identify persistent underperformance
- making it easier for retail investors to move into better value share classes
- requiring clearer communication of fund charges and their impact at the point of sale and in ongoing communication to retail investors
- requiring increased transparency and standardisation of costs and charges information for institutional investors
- exploring the potential benefits of greater pooling of pension scheme assets
- requiring greater and clearer disclosure of fiduciary management fees and performance

We also consulted on whether to make a market investigation reference to the CMA on the investment consultancy market, and have recommended that the Treasury consider bringing the provision of institutional investment advice within the FCA's regulatory perimeter.

In addition, we propose to undertake further competition work on the retail distribution of funds, particularly in relation to the impact financial advisers and platforms have on value for money.

Additional areas of focus identified in the Sector View

Overpayment of some investment management services
Some investment managers may pay too much for services on behalf of investors due to:

- lack of transparency of information regarding some fees and charges
- failure to consistently monitor, assess and deliver on 'best execution'

The ability of custody banks to meet current service standards or ensure continuity of service
Because of business model pressure and the relatively low margin nature of this business, the incentives to invest and replace legacy IT systems may not exist.

Product design and oversight of portfolios
Providers focus on designing investment products that are easy to manage, or suit advisers, rather than delivering products that meet end-investors' needs.

Disorderly failure of investment managers and/or their portfolios could disrupt the financial system
Market stability could be affected by the failure or disorderly wind-down of a very large asset manager or several asset management firms as end-investors attempt to redeem their holdings on demand, creating a downward selling spiral.

Wholesale financial markets
Sector view

Well-functioning wholesale financial markets are a critical part of the global economy. They fulfil a broad range of financial needs for corporates, governments and financial institutions including:

- making and receiving payments
- financing investment, innovation and growth
- financing operations and managing cash
- facilitating domestic and international trade
- providing opportunities to invest
- managing financial and other risks

In 2015, the total value of transactions in UK equity capital markets (ECM) was $63 billion, while $272 billion was raised through new debt issuance.[1] An estimated $50 trillion in equity and debt instruments were traded in the UK in 2014.[2] London is also an important centre for derivatives, commodities and FX. Around 40% of global daily volumes of both interest rate derivatives and global FX transactions are undertaken in the UK.[3]

Wholesale markets also directly affect many aspects of retail consumers' economic activity. The cost and availability of consumer credit (including mortgages) is determined partly by the cost to lenders of raising funding in the wholesale financial markets. The value (and return on) retail investments, including defined contribution pensions, is closely linked to asset prices set in wholesale financial markets. The price of foreign currency, energy and agricultural and industrial goods are determined in wholesale financial markets.

To manage the complexity and scope of the wholesale financial markets we have divided them into five distinct sectors. We have chosen to divide the markets based on the need each sector fulfils, which enables us to assess whether the markets are working well.

The scope of the five sectors is set out on the opposite page.

The sectors are closely interlinked and firms may offer services across a number of sectors. For example, lending and transactional business are typically supplied alongside capital markets services. The derivatives sector is clearly affected by developments in the underlying cash securities, commodities and FX markets, and equity, debt and lending are all ways in which corporates can raise capital.

Our work also takes account of the links between the regulated and unregulated elements of wholesale markets. Many of the activities in the wholesale lending, transaction services, and the FX and commodities sectors are not defined as regulated activities. However, they may fall under our broader regulatory remit, such as our competition powers.

1. Dealogic, includes financial and non-financial but not government debt.

2. FCA estimates based on Trax, a MarketAxess company, data for debt and Fidessa Fragulator data for equity.

3. FCA calculations based on BIS derivatives statistics.

We completed Sector Views for equity and debt markets, derivatives and FX and commodities markets in November 2016. This document reflects our work in these markets at that time. Sector Views for the two remaining sectors, wholesale lending and transaction services, were completed in February 2017.

Equity and debt primary and secondary markets
Equity and debt primary markets enable companies and public entities (issuers) to raise the finance they need to operate, invest and grow. They also provide savers and investors with opportunities to buy equity and debt instruments to make a financial return. Intermediaries play important roles in this sector, matching issuers and investors and providing services that facilitate capital market transactions including structuring, syndication, underwriting, sponsorship and rating, research and marketing. Intermediaries also provide advice on which form of finance is most suitable for the issuer and act as a go-between for listed companies and their shareholders.

The UK has traditionally been one of the largest international equity and debt capital markets (ECM and DCM). Over the past 10 years, the UK has consistently been one of the top five countries for equity and debt issuance. The market attracts both UK and International issuers and investors. In 2015, deal values of $63 billion (ECM) and $272 billion (DCM) generated gross fees of around $12 billion.[4]

Secondary markets exist so that investors can trade equity and debt instruments already issued on the primary market. This allows initial investors to exit their investment and gives other investors exposure to the instruments. Trading is generally facilitated by intermediaries and market infrastructure, eg trading venues.

4. FCA Investment and Corporate Banking Market Study MS15/1.2 (2016).

Overview of the five Wholesale Sector Views:

Transaction services

- Enables corporate treasurers to budget, save and invest their cash to optimise their cash flows
- Facilitates local and cross-border payments between corporates, customers and suppliers
- Provides tools and associated advice for domestic and international trade
- Provides short-term financing and risk management solutions to help mitigate credit risks involved in commercial transactions

Lending

- Provides financing solutions to wholesale market participants
- Corporates, financial institutions and public entities require funding for a variety of uses, including financing operations, refinancing, capital expenditures, and acquisitions

Equity and debt primary and secondary markets

- Enable companies and public entities to raise funds from investors by issuing and selling equity and debt instruments that are tradable in capital markets
- Facilitates the trading of debt and equity instruments and the associated financial risk between investors and traders acting to achieve a return on their investment

Derivatives (equity, rates, credit, FX, commodities)

- Facilitates the trading of risks associated with interest rates, credit, FX and commodities etc.
- May be used for hedging against changes in the values of assets or liabilities or to generate a synthetic investment position
- The majority of derivatives are traded over-the-counter (OTC) and their value is in most cases linked to one or more financial benchmarks

FX and cash commodities markets

- FX markets enable market participants to trade currencies in order to facilitate international financial activity
- The FX market is global and electronically linked but takes place over-the-counter (OTC)
- Commodities markets facilitate the buying and selling of raw materials such as metals, oil and gas and agricultural goods for consumption or processing, or as an investment

Well-functioning wholesale financial markets are a critical part of the global economy. They fulfil a broad range of financial needs for corporates, governments and financial institutions

Introduction
Methodology

We look at the sectors through 13 wholesale-specific lenses. This approach helps us assess where markets are working well, and where they are not.

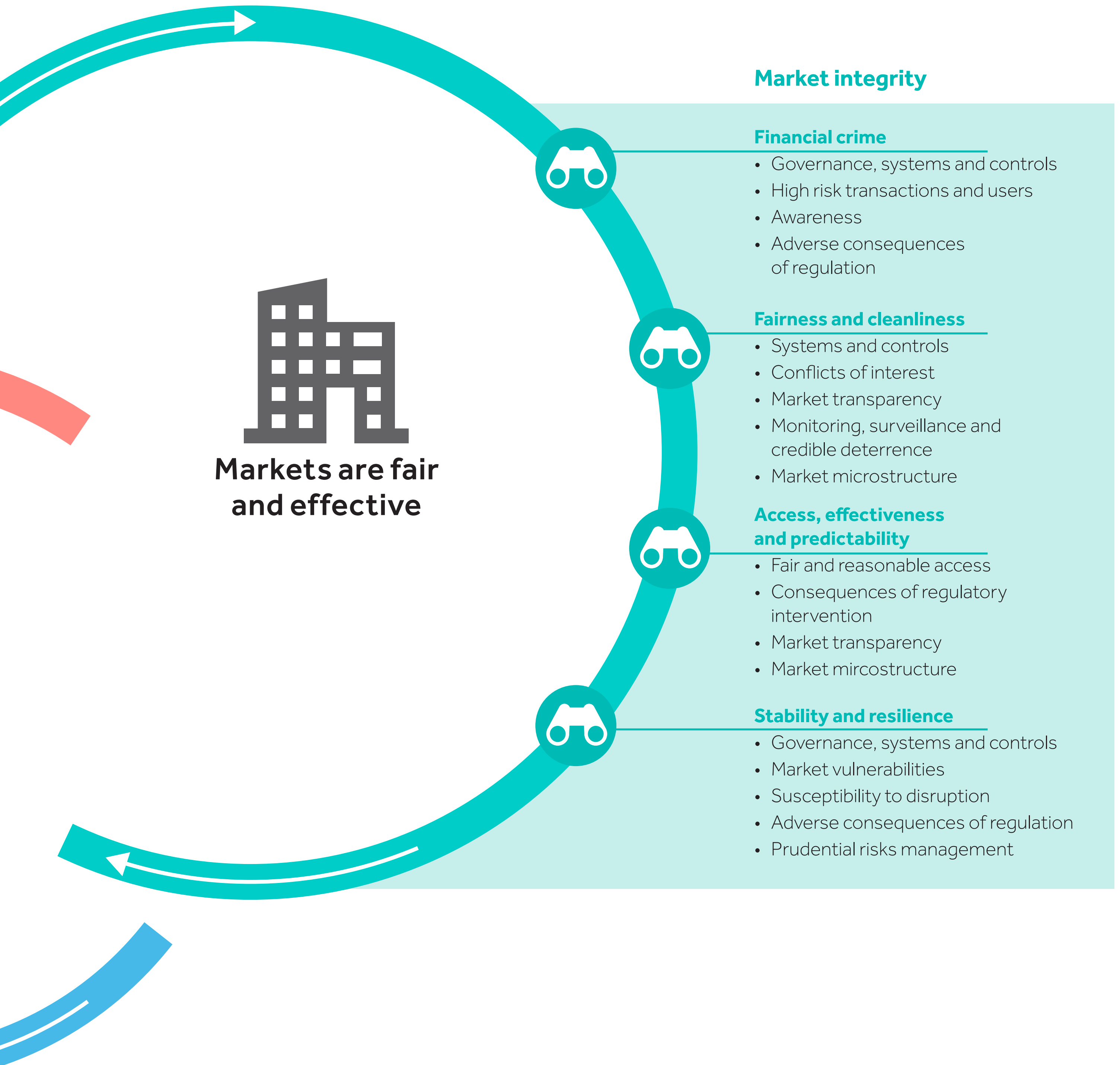
User protection

- Governance, systems and controls
- Adverse consequences of regulation
- Conflicts of interest
- User sophistication
- Information asymmetries

Markets work well, delivering for individuals, for businesses and for the economy as a whole

Effective competition

- Barriers to entry and innovation
- Anti-competitive behaviour
- Market power
- User ability to compare and switch provider
- Impact of innovation and regulatory intervention

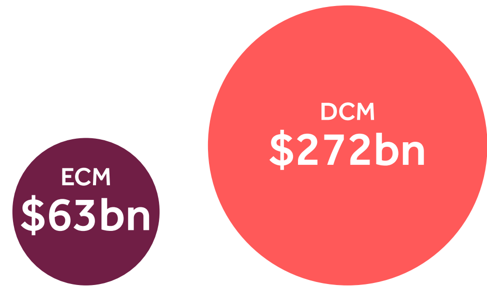

Markets are fair and effective
Market integrity
Financial crime
• Governance, systems and controls
• High risk transactions and users
• Awareness
• Adverse consequences of regulation
Fairness and cleanliness
• Systems and controls
• Conflicts of interest
• Market transparency
• Monitoring, surveillance and credible deterrence
• Market microstructure
Access, effectiveness and predictability
• Fair and reasonable access
• Consequences of regulatory intervention
• Market transparency
• Market mircostructure
Stability and resilience
• Governance, systems and controls
• Market vulnerabilities
• Susceptibility to disruption
• Adverse consequences of regulation
• Prudential risks management

$12bn

gross fees generated from UK ECM and DCM deal values (2015)

Source: FCA Investment and Corporate Banking Market Study (2016)

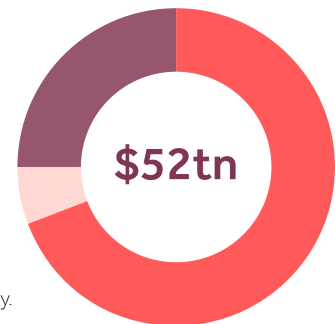
Figure 7: Equity and debt: UK deal values (USD, 2015)



Source: Dealogic - includes financial and non-financial but not government debt

Figure 8: Equity and debt: UK traded volumes (USD, 2014, estimates)

Debt (government)	69%	($37tn)
Debt (corporate)	6%	($2tn)
Equities	25%	($13tn)



Source: FCA estimates based on Trax, a MarketAxess company, data for debt and Fidessa Fragulator data for equity.

An estimated $50 trillion in equity and debt instruments were traded in the UK in 2014. Financial institutions are the largest users of secondary markets for both equity and debt. In recent years, High frequency traders (HFTs), who rely on speed of data analysis and trading execution, have increasingly established themselves as key participants in equity secondary markets. HFTs now account for an estimated 43% of the value traded on EU exchanges.[5]

Other participants in secondary markets include non-financial corporates, who may purchase equities to gain a stake in another company or to buy back their own shares. Central banks are heavily involved in the secondary market for government debt, often purchasing large volumes to meet their monetary policy objectives. More recently, central banks have also begun to buy corporate debt as part of their quantitative easing programmes. Retail investors may access these secondary markets through intermediaries.

The FCA has conduct, prudential and competition responsibilities across this sector, including oversight of secondary market trading infrastructure. It maintains the official list of publicly traded companies through the UK Listing Authority (UKLA). We work closely with the Bank of England, which oversees systemic infrastructure such as central counter parties (CCPs). The international nature of the firms and activities in this sector makes cooperation with our international counterparts particularly important.

Derivatives markets

Derivatives are contracts that derive their value from an underlying asset (such as equities or commodities) or from a reference price (such as interest rates or benchmarks). They serve a variety of needs, most notably to mitigate a range of financial risks. Deutsche Bank research found around 73% of participants in the OTC derivatives markets cite hedging as their motive to trade, 17% arbitrage and 10% speculation.[6] Financial counterparties account for the bulk of transactions. Non-financial

5. ESMA, High-frequency trading activity in EU equity markets (2014).

6. Deutsche Bank Research: Who are the end users in the OTC derivatives market? (2 Dec 2015).

counterparties account for 3%, 13% and 21% of notional outstanding interest rate, FX and commodity derivatives respectively.[7]

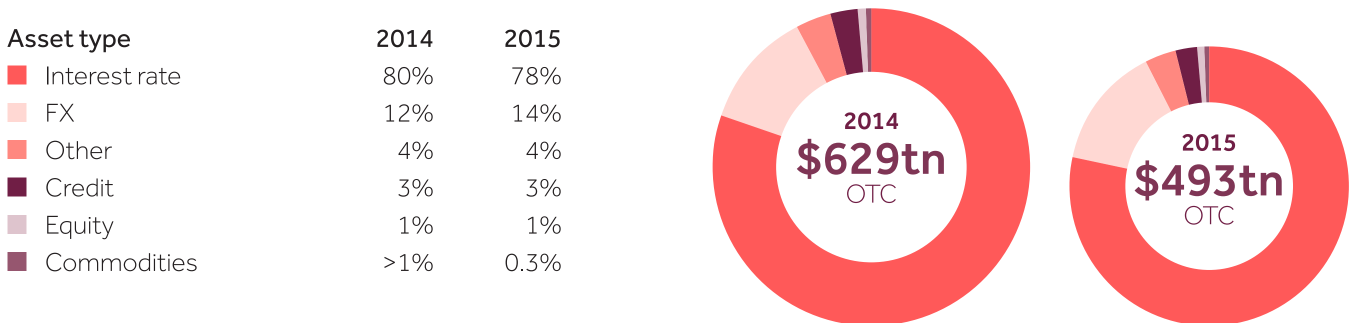
In 2015 the global derivatives market, measured by outstanding notional value, was approximately $490 trillion. Around 85% is traded OTC as opposed to exchange-traded derivatives (ETD). The UK plays a central role in the trading of these products. Almost 40% of the global daily volume in interest rate derivatives, and a similar percentage of FX derivative trading, occurs in the UK.

Interest-rate derivatives account for around 80% of the market and are used to manage risk and gain exposure to interest rate movements. FX derivatives are the next largest category and account for around 12%. Benchmarks such as LIBOR and ISDA Swap Rate often play an important role as reference points for pricing derivatives.

Traded volumes grew significantly during the run-up to the 2008 global financial crisis. Growth has slowed since then, caused largely by a trend towards de-risking among banks, and regulatory intervention aimed at reducing systemic risk. Following the crisis, there has been a general move towards increasing regulation for OTC derivatives, enhancing transparency and risk management through more exchange trading, and centralised clearing and reporting. This is enacted through the Markets in Financial Instruments Directive and Regulation (MiFID II) and the European Market Infrastructure Regulation (EMIR), which the FCA is largely responsible for enforcing. With the implementation of the EU benchmark regulation, more benchmarks will also fall within the FCA perimeter. These regulatory changes are driving significant structural changes in the markets, including a reduction in OTC derivatives.

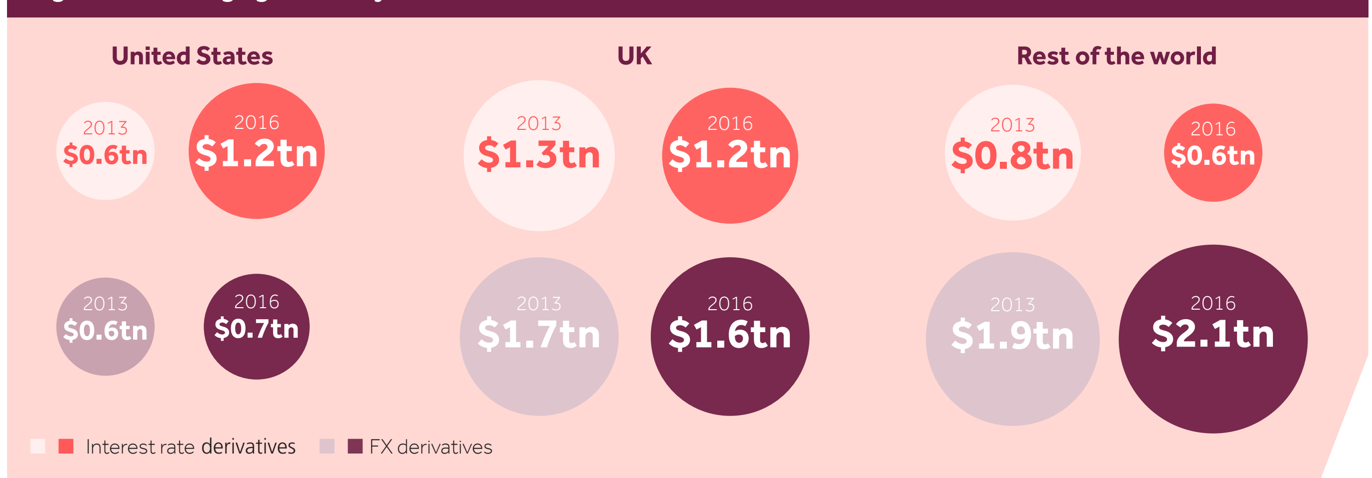
7. Calculation based on BIS data, detailed tables on semiannual OTC derivatives statistics at end-December 2014 (April 2015).

Figure 9: Derivatives: global OTC notional outstanding by asset class



Asset type	2014	2015
Interest rate	80%	78%
FX	12%	14%
Other	4%	4%
Credit	3%	3%
Equity	1%	1%
Commodities	>1%	0.3%

Figure 10: Average global daily turnover OTC derivatives:



Sources: Calculation based on BIS derivatives statistics.

FX and commodity cash markets
These markets enable users to buy, sell and trade the currencies or commodities they need for operations or investment. They are truly global and have significant influence on the 'real economy', including the price consumers pay for petrol and food. The UK is the world's largest spot FX market, accounting for 39% of global transactions. In April 2016, the UK's average reported daily spot FX turnover was $784 billion.[8]

The EU Commission has estimated that the global physical market for major commodities amounted to over $5 trillion in 2009/10.[9] The physical market is much smaller than the derivatives market. The notional value of exchange traded and OTC commodity derivatives is estimated to be forty times that traded on physical markets.

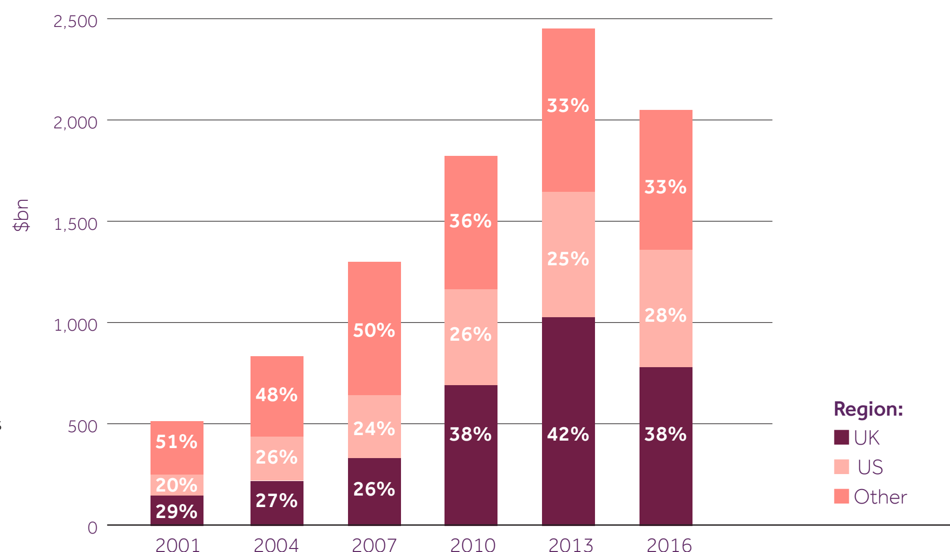
Dealing in cash FX or physical commodities is not a regulated activity. However, some associated activities are covered by our powers, such as maintaining controls associated with market abuse and financial crime. These markets may also be subject to our concurrent competition powers. Behaviour in the physical markets can affect the financial markets and vice versa, particularly given the direct link between physical commodities and their financial derivatives, or where firms operating in the physical market are regulated.

Transaction services

Transaction services are fundamental to the functioning of the economy. They enable corporates,[10] governments, local authorities, charities, and financial institutions to make and receive payments, manage cash flow, manage risk associated with trading, and fund short-term operations.

BCG estimate there was some $360 trillion in global wholesale payment transactions in 2015. Wholesale transaction services – including payments, cash management and trade finance – account for around 10% of global banking revenues.[11] Our analysis

Figure 11: FX cash markets
Global spot FX daily average turnover (April), $bn



Source: BIS derivatives statistics.

8. BIS derivatives statistics.

9. EU Commission, Impact Assessment of Benchmarks Regulation (2013).

10. For the purpose of this sector view, corporates includes all corporates other than small and medium-sized enterprises (SMEs). SMEs, i.e. firms with fewer than 250 employees and/or turnover lower than £25million, are covered within the Retail Banking sector.

11. Based on data from Global Payments 2016: Competing in Open Seas, The Boston Consulting Group 2016

suggests UK based wholesale banks earned over $13 billion from transaction services in 2015.[12] The majority of this, up to 80%, comes from payment services and cash management.[13] Transaction services revenue for wholesale banks has grown steadily since the crisis, in both real and percentage terms, and this is expected to continue.[14]

Transaction services are generally based around a corporate banking relationship, through which a suite of products and services are offered. Different transaction services are often cross-sold as a package with other banking services, particularly revolving credit facilities. Larger users tend to have relationships with numerous banks. This helps mitigate the risk of having a single supplier of banking services.

All banks worldwide offer transaction services. Supply of wholesale transaction services in the UK seems mildly concentrated with the top four banks accounting for around 70% of revenues.[15] Banks may specialise in certain markets, eg client groups, regions or certain product lines. There are non-bank players offering cash management and trade finance services, but these tend to focus on servicing SMEs and are therefore out of scope for this Sector View.

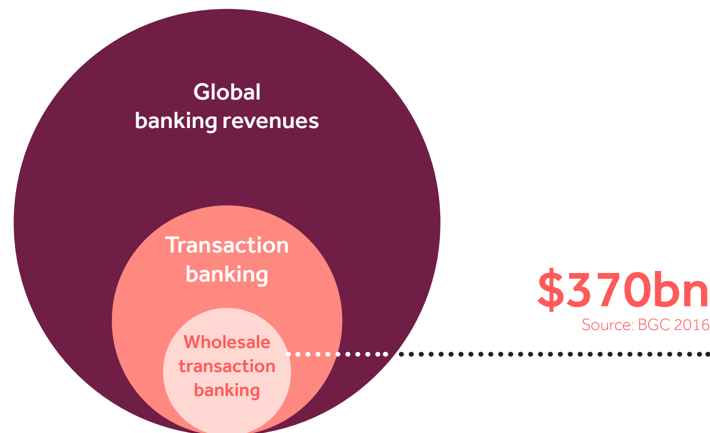
Wholesale lending

The wholesale lending sector is comprised of markets for bi-lateral and syndicated loans, as well as money markets.

Bi-lateral loans are made between a single lender (normally a bank) and a borrower. Syndicated loans are larger loans for which a single lender is normally unwilling to take the entire credit risk, so the loan is syndicated among a number of lenders.

Bi-lateral and syndicated loans provide borrowers with funding, either to support general or specific business needs, finance growth, projects or acquisitions. We do not have data showing the overall scale of wholesale

Figure 12: Wholesale transaction banking revenue[16]



lending in the UK; in particular, data for bi-lateral lending by UK firms to all corporate clients are not available. However, Bank of England data show all gross lending for UK based major financial corporations to UK corporations has grown steadily since 2012, reaching an estimated £480 billion in 2015.[17] In 2016 there was a reported €473 billion of UK syndicated lending to both UK and international clients.[18]

Both bi-lateral and syndicated loans can take the form of revolving credit facilities (where the borrower can drawdown and repay credit as needed), term loans (where the borrower will receive a lump sum and repay it in instalments) and other types of lending facilities, for example short-term swingline loans.

Money markets enable both financial and non-financial corporations to invest or borrow on a short-term basis (typically less than 30 days) to cover their short-term positions (in the case of financial corporations) or to fund other short-term needs. Money markets also enable businesses with excess capital to invest it in money market funds to generate a return.

Money markets include the issue of unsecured instruments like commercial paper and certificates of deposit, as well as secure instruments like repo agreements. In 2016 there were £78 billion in secured and £36 billion in unsecured money market transactions on an average daily basis.[19]

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12. Estimates based on analysis of FCA data and publically available data from firms' annual reports.

13. Coalition, referenced in Global Finance, 'The State Of Transaction Banking Today', 9 September 2016.

14. See McKinsey, Global Payments 2016 and The Boston Consulting Group, Global Payments 2016.

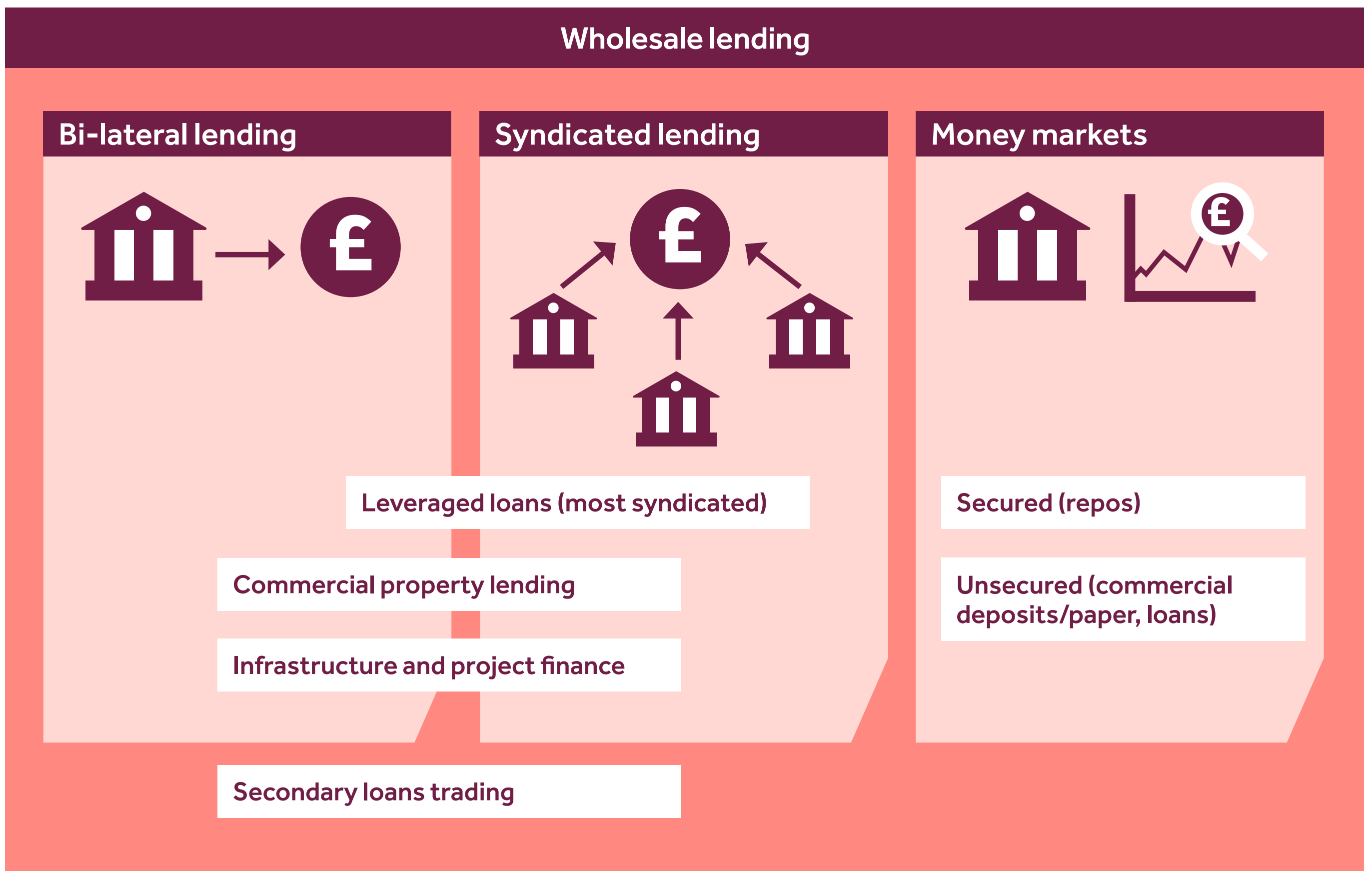
15. Estimates based on analysis of FCA data and publically available data from firms' annual reports.

16. Based on data from Global Payments 2016: Competing in Open Seas, The Boston Consulting Group 2016.

17. Bank of England, Bankstats. Lending to non-Financial Corporations from Table A8.1. Lending to Financial Corporations estimated based on outstanding loan ratios, calculated from BoE tables LPMVWMO and LPMVWMP.

18. Bloomberg syndicated loans data, UK, 2016.

19. Bank of England, Money Market Liaison Committee, Money Market Survey 2016 H1.



Drivers of change

The structure of wholesale markets and the roles of participants are changing rapidly as technology, regulation, economic and political factors influence the sector. The individual and cumulative impact of these developments is uncertain, though some trends can be identified.

Wholesale markets are increasingly interconnected globally. Firms have also become more complex and interconnected, operating across multiple jurisdictions.

High levels of indebtedness in the global economy, persistent low interest rates and weak global growth with lower international trade volumes, coupled with political uncertainty, including the UK's withdrawal from the EU, and new regulatory requirements, ie MiFID II, may drive significant change. This may include changes in firm business models, performance of asset classes, competition dynamics and trader, and investor behaviour.

Increased capital, liquidity and leverage requirements may lead to firms pulling back from more traditional roles as market makers, and market-making capacity being filled by non-bank participants such as asset managers and HFTs.

Technology is evolving rapidly in wholesale markets, increasing both the volume and speed of transactions and reliance on IT infrastructure. A search for efficiency is driving the harnessing of technology such as distributed ledger technology (DLT), increasing use of algorithms and machine learning. These may make markets harder to oversee and increase susceptibility to market shocks.

Our assessment of the sectors

In November 2016 we carried out a full assessment of three sectors: equity and debt markets, derivatives and FX and commodities markets. We followed this by assessing the transaction services and wholesale

lending markets, which we completed in February 2017. This was informed by a wide range of data and intelligence, and built on our understanding of the sector and the impact of external forces.

User protection
Our objectives and regulatory framework requires that users within relevant markets receive appropriate protection. Users in these markets are generally more sophisticated than retail markets and this is reflected in the graduated client classification and protection regime outlined in MiFID.

However, information asymmetries and conflicts of interest remain a feature of these markets and potential drivers of risks across these sectors. As such, monitoring firms' management of these risks needs to remain a priority. Areas of particular interest include:

- activities that are now, but have not previously been, subject to detailed regulation or oversight and may have less developed controls and culture to manage these risks
- where users are less sophisticated participants
- where a firm is acting both as a principal and agent in relation to a trade or service
- where products and services are bundled or cross-sold
- where firms are going through significant operational change or reorganisation, for example, as a result of the UK's withdrawal from the EU
- where firms are winding down to ensure protection of client assets

Effective competition
In assessing the effectiveness of competition across wholesale markets, which is difficult given the complexity, scope and international nature of the markets covered, we have not sought to carry out a full assessment. Rather, we have noted findings from recent work and, in some cases, identified some of the potential underlying issues and drivers of risk.

Indicators of effective competition include pricing, the number of competitors in a market, and market shares. Costs of trading have fallen over the past ten years, both in terms of trading fees and bid-ask spreads (analysis conducted by the FCA estimated that the contraction of spreads since 2012 could represent reduced trading costs of £46 million per annum[20]). However, we do not yet know whether there has been a similar reduction across the value chain or whether other costs may have increased (such as market data). In considering competition it is also important to recognise the potential role of innovation, including the possible development of disruptive technologies, which may threaten incumbents and improve competition in the sector.

In primary markets, there is a wide range of providers and market shares are usually not high (below 20% in most sub-sectors). However, we have found some issues that may hinder effective competition within ECM and DCM. We are seeking to address these through our remedies to the Investment and Corporate Banking Market Study on restrictive contractual clauses, the IPO allocation process, use of league tables, and availability of information during the IPO process.

In secondary markets, network effects and economies of scope and scale bring significant benefits to users – for example, in pooling liquidity. However, they create significant barriers to entry and (in some cases) switching. Firms in some areas of the secondary market may still retain large market shares, which may suggest some market power. Examples include equity trading, settlement, market data, credit ratings, indexes, and middleware, though it is not clear whether this is leading to an abuse of market power.

For market infrastructure providers, one of the key aims of MiFID was to introduce competition. This was

The increasing globalisation and accessibility of wholesale financial markets means the risk of financial crime is high

20. FCA Insight – UK equity trading costs continue to decline 02 November 2016.

achieved and led to a number of new entries – especially among trading venues (eg Multilateral Trading Facilities). Even so, the two largest trading venue operators still account for around 90% (in 2015) of the total traded value of UK equities and LCH accounts for around 95% of cleared global OTC interest rate swaps.[21] The MiFID II requirements relating to enhanced transparency and access across instruments and infrastructure may create a more level playing field for trading venues, benefiting competition.

There is some evidence of competition at work in the transaction services market. However, the time it takes and the operational risks involved in switching providers may reduce demand side pressure.

The wholesale lending market has low levels of concentration, suggesting market power is not an issue. However, in 2016, we sent 'on notice' letters to a number of firms involved in potential infringements of the competition rules relating to the treatment of competitively sensitive information relating to syndicated lending. In addition, the European Commission has recently commissioned some work to look in more detail at syndicated loans in six countries, one of which is the UK.

Financial crime

The scale of the sector and the complexity and opacity of certain areas (such as Direct Market Access chains) can lead to increased financial crime risk as well as difficulties in addressing financial crime. Transaction services are particularly relevant to our efforts to reduce financial crime. This is because the key anti money laundering (AML) and Know Your Customer (KTC) assessments often occur as part of the transaction services offerings. Recent regulatory action, including FCA supervision and enforcement activity, has triggered significant investment in systems and controls to tackle financial crime, and we have seen improvements in firms' ability to detect and prevent financial crime. Larger and smaller firms alike have made some improvements, and senior management engagement has increased significantly.

However, some firms may still present risks (particularly those with less resource to commit, less sophisticated systems and controls and fewer people with appropriate skills). Such firms may be seen as gateways into the financial systems, and targeted by criminals who go on to commit financial crime on a larger scale.

Furthermore, the increasing globalisation and accessibility of wholesale financial markets means the risk of financial crime is high. Global money laundering transactions are estimated to account for 2-5% of global GDP.[22]

Different standards across international jurisdictions pose challenges for firms operating cross-border and raise the risk of importing lower standards into the UK.

In terms of monitoring, the complexity and fragmented nature of financial crime regulations can make this difficult. The difficulties of detection are exacerbated by the pace of technology innovation, which continually presents new opportunities for criminals and thus requires ever-evolving modes of detection. However, technology may also help the detection and mitigation of financial crime risks by enhancing market-wide information sharing, and by making it easier to assess the risks posed by individuals and transactions.

Stability and resilience

The stability and resilience of certain wholesale infrastructure and transaction services is critical to the economy. We have seen change and improvements in both the regulatory regime and firms. Prudential and financial stability regulation has made firms and markets collectively more resilient – particularly from a systemic and counterparty risk perspective. Although the efficacy of the new regulatory framework remains untested in a highly stressed environment, the EU referendum was a positive example of successful

21. Fidessa and LCH Swapclear website.
22. PwC, Global Economic Crime Survey (2016).

mitigation of a known risk and evidenced how firms have improved the way they prepare themselves and their clients for risk events. Within market infrastructure firms, governance, systems and controls appear to have improved. Major exchanges also seem to have appropriate impact mitigation mechanisms.

In spite of these improvements, new and significant threats are emerging in relation to technology and cyber resilience. The number and sophistication of attacks continues to rise although there have been efforts to improve systems, controls, reporting and coordination such as CBEST testing. Increasing use of third parties and outsourcing (eg middleware providers) may also increase risk, where the supply chain becomes increasingly complicated and concentrated. A worsening economic situation and the UK's exit from the EU could lead firms to cut back on investment in IT, systems and controls, which would exacerbate some of these concerns.

We are also aware of the potential stability risks created by algorithmic trading. The inherent automation and speed may encourage herding behaviour and catalyse flash crashes, amplify market volatility and potential losses for firms and investors. This is in addition to risks associated with errant algorithms and the potential use of speed to manipulate markets.

Potential stability risks resulting from herding behaviour have also been raised in relation to passive funds.

Wholesale lending markets are generally resilient and stable. However, the Bank of England (including the Financial Policy Committee) have noted that repo market participants perceive (the market) to be 'functioning poorly' overall,[23] and is continuing to monitor and assess the performance of these markets.

Access, effectiveness and predictability

Although, technology and innovation has the potential to enhance access and effectiveness, such as blockchain clearing and settlement, we have a number of market-specific concerns relating to access, effectiveness and predictability across different markets.

In primary markets, while many clients, particularly large corporates, have good access, we recognise improvements could be made in some areas, such as the IPO share allocation process and availability of information during the IPO process.

In the derivatives market, concerns have been raised about the ability of some users to access hedging products. Concerns have also been raised about the impact of regulatory change on liquidity in some markets, such as corporate bonds. Market participants are worried that future regulations may reduce it further, especially in the debt markets.

More broadly, depending on how firms respond, the UK's withdrawal from the EU may reduce the services offered to UK clients in some markets raising additional access issues or hampering liquidity.

Fairness and cleanliness

High-profile enforcement cases have helped raise awareness of market abuse risks, and we have seen improvements in firms' conduct and culture.

Participants in the equity markets generally have sophisticated systems and controls to manage market abuse. However, ensuring the positive tone from the top reaches all levels, and that clear accountability is in place, remains a challenge. In addition, smaller firms may not have reached the same standards as bigger firms and may pose risks beyond their size. For example, a mid-range broker offering DMA services may not see the benefits of investing in sophisticated systems and controls, and may knowingly or unwittingly allow access

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Technology is evolving rapidly in wholesale markets, increasing both the volume and speed of transactions

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23. Bank of England, Money Market Liaison Committee, Money Market Survey 2016 H1.

High-profile enforcement cases have helped raise awareness of market abuse risks, and we have seen improvements in firms' conduct and culture

to the market to groups who pose a threat. This demonstrates the trade-off between increasing access and maintaining high standards.

Furthermore, areas that have not been subject to market abuse regulation may be less well prepared to mitigate the risks. For example, debt markets , spot FX, cash commodities and OTC derivatives markets may not have the same standards of governance and systems and controls as the equity markets.

Cross-venue and cross-asset market manipulation also may present particular monitoring challenges as does sophisticated and encrypted communication tools.

Bi-lateral and syndicated loan transactions give lenders access to confidential information which has the potential to be misused and may facilitate cross-market abuse or manipulation of the secondary loans market.

Areas of focus

Our assessment identified emerging priorities relating to IT and cyber-resilience. We highlighted risks, and drivers of risks, that are inherent to the sector, including the management of conflicts of interest, market abuse and financial crime. We also identified a number of areas where we believe ongoing monitoring is critical (such as the possible consequences of regulation and liquidity levels in some markets) and where we would benefit from a deeper understanding (such as competition dynamics in certain areas of the secondary markets).

Conflicts of interests and information asymmetries

The nature and structure of wholesale financial markets mean that conflicts of interest and information asymmetries remain inherent drivers of risk. High levels of horizontal and vertical integration give rise to numerous conflicts of interest, particularly where firms act both as principals and agents. Effective management of these conflicts is fundamental to firms meeting their regulatory requirements. In some cases, failure to do so may reflect deeper problems, such as an inappropriate culture.

Information asymmetries are driven by the complexity of products, services and pricing, a lack of transparency in OTC markets, and varying levels of user sophistication. These information asymmetries exacerbate conflicts of interests and impede users' ability to compare providers. Cross-selling and bundling add to the complexity, and further reduce the incentive and ability to shop around.

Market abuse and misuse of confidential information

There continue to be incentives for opportunists and participants in organised crime to undertake market abuse. Some markets are particularly illiquid, making them more prone to manipulation. Given the volume of transactions, increasing ease of access to markets and the lack of transparency, it can be difficult to identify instances of abuse.

Within some institutions, we have identified weaknesses in systems and controls and governance arrangements to mitigate the risks of market abuse. Poor culture may be a driver of risk, particularly in areas where there has previously been limited or no oversight. Given the difficulty of monitoring, cross-venue manipulation is also a significant concern. The increased demands on senior management resulting from the UK's withdrawal from the EU (and potential future market volatility) may increase these risks by diverting firms' focus away from controls, and making detection harder.

As noted above, loan transactions give lenders access to confidential information which has the potential to be misused. The issue is made more prevalent by investment banks' integration of their loan desks with capital markets activities (ie equity and debt). Misusing this information could also give rise to conflicts of interest for banks providing services to clients who are competitors.

Market power
Network effects across wholesale financial markets benefit market users, but may also raise competition issues. An example is secondary markets, where trading venues compete on a European and global basis to attract flows. This creates clear benefits for market users in terms of liquidity, but could lead to pockets of market power. Other areas include provision of benchmarks, post-trading services, market data and middleware – all markets where network effects are likely to play an important role. Abuse of market power can lead to sustained higher prices, or the ability to offer poor quality without losing business to competitors. Over time, consolidation in the industry could exacerbate market power issues.

Effective competition may also be undermined by structural barriers to entry, such as economies of scale, technology and the importance of reputation. Market user behaviours may also create risks to competition – for example, when firms are able to restrict access (or give access on unfavourable terms) to services that are necessary to participate in other markets, such as clearing in the derivatives trading markets. When considering competition it is important to recognise when providers are competing on a global scale to offer their services, and ensure any assessment reflects the appropriate geographical scale.

Financial crime
Inherent incentives to commit financial crime, globalisation of financial services and emerging technologies continue to drive financial crime risks which pose a threat to market integrity. This is of particular importance in the transaction services sector.

Specific risks may arise from lack of awareness or expertise within small firms, but also from failure to embed awareness across large global organisations. In addition, complex transactions and those that involve risky jurisdictions are a particular concern.

Anti-money laundering and Know Your Customer standards may come under pressure as firms and governments seek to reduce barriers to cross-border financial activity and to the growing speed of transactions.

Technology and IT systems
Technology and IT systems already play an important role in this sector, and in some areas they are integral. Technology developments are driving changes to market structures and market models which may transform the nature of the issues we are seeing. Increasing electronification (more venue-based electronic trading) and digitisation (use of strategies and tools such as algo-trading), high reliance on technology and the interconnectedness of markets at the European and global level mean that cyber-attacks or system glitches may cause widespread disruption. Firms often outsource IT services, but may fail to exercise appropriate oversight over the supplier. This can lead to risks in user protection, market stability and resilience.

Risks to stability and resilience may also arise from concentration risk, for example where unregulated middleware providers provide market infrastructure to secondary markets. This can be a particular issue where there is just a single supplier or a small number of suppliers. Some participants may struggle to deal with the demands of upgrading legacy systems.

Firms' management of technology and cyber risk resulting from their transaction services business including risks associated with interconnectedness and outsourcing, will remain a priority focus for us in promoting market integrity and stability.

The consequences of regulation
The wholesale financial markets have seen far-reaching regulatory change in recent years. This has focused on reducing systemic risk and increasing transparency and oversight. Regulation is also having an impact on market structure. Heightened capital requirements have seen banks withdraw from certain business lines, or offer more bespoke hedging arrangements to some clients. This could increase the risk of clients (both corporate and financials) having reduced access to services they need. Some interventions, either individually or cumulatively, may have a mixed (or adverse) impact on the effectiveness or predictability of the sector. It is important that we continue to monitor these developments.

Collusion in syndicated loans
There is evidence in other jurisdictions, and suspected cases in the UK, of lenders in the syndicated loans market colluding to set prices and/or manipulate benchmarks. This not only undermines the integrity of the syndicated loans market, but also leads to market participants paying an above market rate for loans.

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