FCA Future Scenarios Conference

The changing face and nature of products and services - Do Keep Up...

Introduction

Around forty five years ago my Mum and Dad bought their first house. As a recently married couple, both with relatively well paid jobs, they discussed the matter of a Mortgage with the manager of the Building Society in town where they had managed to save a deposit. No doubt questions were asked, plans were considered and an offer was made, in person, with triplicate forms and an oversize accountant's calculator. The Newbury Building Society is still with us today - one of a small and dwindling number of building societies, branding itself as the 'local' mortgage and savings experts.

Jump forward to Sheffield 2002, a youngish civil servant, single, with a very modest pot of savings, partly reliant on the Bank of Mum and Dad for a little bit of help. Knowing that prices are going up and up, decides to jump on the bandwagon and is signposted to a mortgage broker by an estate agent through which he wants to buy. A few very basic questions asked (no documentation as I recall) and after a bit of tapping into a computer the broker prints out three or four different options. I select the one with the cheapest monthly repayments and stick with that mortgage provider for the next 10 years.

And so to twenty years hence - my kids in their mid-late twenties may also be wanting to buy a house. What will their journey be? Will people be involved in scrutinising their finances? Will that happen in person? Over the phone? Online? Will they ask any questions at all? Will some super-computer making use of AI have already monitored their money and offer them a bespoke set of credit solutions, filled the form in and just be waiting for confirmation with a retinal scan through a mobile device embedded in their finger?

Who knows?
Who cares?
Well - I do.
My kids will (hopefully)...
And for that matter, so will all of the next generation - whoever they are and whatever their skills, capabilities, incomes and wealth
And so should the FCA

Technological Change

I am not a technology geek
I do well to turn on my computer each day - sort out my emails, write a report, analyse numbers in spreadsheets, put together a presentation, surf the web for news and sports updates. Occasionally I might stream some music, tweet, manage my online bank account. In short, I am probably much like you. Average.

As an averagely techy person, I am both amazed and sometimes a bit confused by the pace of change in technology over the last twenty years. When I started work in the civil service in 1999, my PC had the numbers 386 (admittedly as the new boy, I had a particularly old machine). The internet made those noises that you will only remember if you are over 30 and you had dial up. I didn't get a computer at home for some time after that. I got my first mobile phone in the year 2000 which could hold 10 text messages in its memory and the most entertaining thing you could do on it was play the game 'snake'. The year before I started work a company called Google was founded.

Today, Google is my homepage. It also happens to support my email, documents, spreadsheets and more. It also pops up on my mobile phone (my phone, I think it is more or less average these days, but apparently it is as powerful as the mid 80's supercomputers that enabled NASA to send people and satellites into space). Technology allows me to conduct the majority of my financial affairs online. I no longer receive paper bank statements or energy bills. Other than my nieces' birthday presents, I can't remember the last time I wrote a cheque. I pay for things with contactless, including my commute.

I could trade stocks and shares through apps on my phone. I could rearrange my pension portfolio. I could gamble on sport, politics or just casino type games hosted somewhere in a cloud. I could at a press of a couple of buttons take out hundreds of pounds in high cost credit. I could then spend it seconds later on whatever advert has popped up my social media account.

Averages and Distributions

I am (for now) an average man. There are some things I do with technology. There are some things I don't do, because I don't understand or trust how it works online. (I am not a pioneer, nor an early adopter). There are some things I don't do because they are not in my interest.

Economists are notorious for using averages and totals. There are some things that these terms are useful for. The total number of people employed is… The Government debt is… But there are sometimes when averages or totals don't let us understand the distribution. The average regular weekly pay in the UK is now £475. I bet you don't earn precisely that. The average house price is £216,750. How much is yours worth? Or the one you are looking to /

dreaming of buying? 80% of the population have ‘adequate’ digital skills, including presumably me. What about the other 20%?

Digital Capability

Technological change is not benefiting everyone. This is also true when it comes to financial services. 20% of the UK adult population don’t have adequate digital skills. 10% have never used the internet. Despite good progress recently with Basic Bank Accounts, there are still millions who are unbanked.

At Citizens Advice we serve over 20 million unique visitors each year with help and support through our website. But we also help 2 million people through our network of local offices and over dedicated phone numbers. The clients we help face to face can be vulnerable, poor and disadvantaged. Almost 3 in 4 are below the poverty line. They are more likely to be in debt, be out of work, be disabled or have a long-term health condition, have a mental health problem, live in private or social rented accommodation. Usually, and by the very nature that they are seeking help, support and advice, they are in a vulnerable situation, sometimes temporarily, sometimes for a long period of time.

Last year (2016) we conducted a survey of 3,000 of our face to face clients to assess digital capabilities. We followed an established framework to test capability in five areas: Managing Information; Communicating; Transacting; Problem Solving, and; Creating.

These skills represent the minimum level of digital literacy that is considered necessary to use and benefit from digital technologies. In this framework, people have ‘basic digital skills’ if they can complete at least one task in all five skill areas. This framework has been used to assess levels of digital literacy across the UK, so using this common approach in our survey has allowed us to understand the needs and capability of our clients against this benchmark. We also asked our clients about their access to the internet. Whether they had access at home, only on a smartphone, through friends, family or public places, or had no access at all.

Only 54% of these clients said they could complete a digital task in each of the 5 skill areas, well below the 77% national benchmark. These findings show us that many of our clients are those who are most in need of support to navigate online service delivery and avoid being excluded.

We compared the number of clients who had access to the internet with the number of households with an internet connection in Britain. 61% of our clients had access to the internet at home. 11% had access only on a smart-phone. Our findings suggest our face-to-face clients are twice as likely to lack access to the internet compared with people in Britain.

Many people benefit from the opportunities afforded by well designed digital services. Digital service provision presents opportunities for those using services and also those delivering them. However, this research reinforces the importance of being responsive to the needs of people who are not digitally capable. Our survey was general digital capability, but you can see how the results and the conclusions read across to financial services, products and of course the FCA.

The Internet and Consumer Behaviour

The internet is an amazing phenomenon. I read a blog the other day which presented what I think is a very astute point. The internet presents a paradox. It allows you to know pretty much anything, but at the same time it prevents you from knowing everything.

At Citizens Advice we have done a lot of work recently on consumer behaviour. For decades economists, Government and regulators have adopted a model of rational consumer behaviour, or 'Homo Economicus'. We absorb information regarding the decisions we have to make, we investigate the market to find the right product at the right price for us. We therefore maximise our utility (or happiness). Producers compete, they align their products and services to consumers demands. The market reaches some sort of equilibrium. It clears. We all go home... relatively happy.

It's an inconvenient truth to say it doesn't really work like that. The majority of us haven't switched energy supplier over the last two years and we are stuck on their Standard Variable Tariff - often paying several hundred pounds more than next door who switched to the same supplier as us last week. That's worth £1.4 billion each year.

The majority of us have no need for the very latest mobile phone (apparently mine could send someone to space) but we are regularly upsold gadgets which we barely use, let alone understand. When all we really need are a certain amount of minutes, texts and data megabytes. I guess a camera is a nice to have too. That's another xx million gone.

About half of payday loan customers could have got cheaper credit from their bank. (Much of the other half really should be getting help, support and advice on their debts, welfare benefits and managing their money). The majority of those customers didn't want the bother of arranging a loan or overdraft with their bank, and prefer the feeling of anonymity and convenience through arranging something on their mobile. That, together with the cash landing in their account in a matter of moments.

The internet together with the way markets have evolved, has brought us more choice. But as the blogger said it is impossible to know everything. We just don't have the time.

Time is a precious resource for consumers, but policymakers can be too quick to propose solutions that demand more of it, without thinking through what the implications will be.
More engagement in markets is often proposed as the solution to the fact that consumers experience considerable problems. This increased engagement will of course take up more of

consumers' time. We conducted research to find out what 'good' consumer engagement would look like, how much time it would take compared to decision-making that comes more naturally, and what impact it would have on consumers. To make our study manageable, we limited it to the pre-sale, decision-making process only. To make it realistic, we invited consumers to contribute to designing the 'good' engagement process we would eventually test. The findings of this research show that:

- Following a 'good' decision-making process takes longer than following a natural process (an average of 107 vs 76 minutes per week). This difference is particularly stark in regulated markets
- Following a 'good' decision-making process leaves consumers feeling less satisfied with their decision than when they decide naturally. Again, this is worse in regulated markets
- In regulated markets, consumers are even less satisfied when they take the time to read terms and conditions, than if they don't bother to do so.

So if we don't have the time, and we aren't able or willing to find out everything we need to know about consumer decisions, then what? We do what we have always done. Behavioural economists call it heuristics, which broadly means following a process that won't necessarily lead to the optimal outcome. In everyday speak, we make short cuts. We go with the flow. We ask our friends. We respond to the adverts. We take the introductory offer. We end up on the default option.

The internet has moved the discussion about rational consumer behaviour further on. What does it mean to be rational when we shop online? When choice has expanded further still? When google presents us with seemingly endless options? When at a click of a button we can access new credit, spend thousands instantly, accept reams of pages of terms and conditions without reading them. Can consumers really be protected by even more information? Can the regulator keep up with new markets, products and services?

The Internet and Firm Behaviour

That blogger had a second paradox too. The internet allows you to be heard, but how does anyone else hear you?

This presents some challenges for all parties in the financial services market. First of all there has been an explosion of companies in financial services over the last decade or so. That can't be a bad thing, economists would much rather be down towards the perfectly competitive market end of the spectrum, rather than towards a handful of monopolies dominating. Secondly the internet has also allowed new products and innovation to spring up. Again as an economist, this must be a positive sign on the whole. The internet has also evolved how firms communicate and market themselves, away from traditional mainstream advertising, towards sponsored links, pop ups and social media.

How do you become heard? I don’t know how much money is spent on advertising strategy, but it must be worth the investment. I am a sports fan, I’ll watch almost anything, once I wrestle the flicker away from the kids. But what happens at half time? Half of the adverts are for sports betting companies, sometimes competing on prices or odds, but mostly on brand, on novelty new games, on introductory offers and free bets.

I do tweet, and if I open my twitter stream I can guarantee that I will have promoted tweets from PPI claims management companies. I work for Citizens Advice, yet I still get my fair share of cold calls about the accident I had in the last 24 months that wasn’t my fault.

In short companies have to make themselves heard. And they must spend a fair amount of money, time and resource in doing so. But therein is another paradox. It is relatively easy for a regulator to explore the market it knows - but what about those businesses that creep under the radar? That cross international borders? What about all the different products that now exist, can the regulator keep abreast of them all?

Our data

Linked to the internet is the issue of our data. We have had credit reference data for a long time, but our online footprint is growing and so are companies who deal in our data, make use of our data, sell our data, and customise products, messages and services because of our data.

We live in an age where we get personalised advertising aimed at us on line. Loan companies are fully aware of your repayment schedule and probably savvy enough to know whether you are likely to extend, roll over or want another loan. Insurers seem to have given up on my renewal dates - I now just get bombarded most weeks with questions about my home and car insurance.

Our data can be worked for good, to help us make the most of our decisions, to help save us time and money. However, as with new innovation and new products, our data can be abused and lead to detriment. It can be used with our consumer biases to push us further into debt, into detriment and into despair.

Mobile vs Desktop / Laptop

One interesting development over the past decade has been the emergence of the mobile internet. This isn’t so much a battle as we’ve seen with platforms and hardware, but a soft takeover. It also is complementary to the way we work. How many times have you used a mobile alongside your computer? To check or verify something? To explore other options? To read a review?

There are a couple of big advantages that mobile has over 'stationary'. One is that the amount of apps for mobile products now vastly outweighs what is available through your home desktop or laptop. The tech people are now mostly working on the next mobile platforms, apps and technology, rather than trying to update Windows 10. The other big thing is in the name, mobile. It's not about the fact it's on a phone, although gone are the days of small screens, everything now is becoming bigger and written for mobile phone content. It is that we as people are mobile, and we conduct much of our lives on the move. Commuting in the morning on the train, being able to work and connect pretty much anywhere, being able to access all that information from our pocket.

The two speed economy - and the dangers of cross subsidisation

One of the dangers of the future is the issue of bi-modal financial services. By that I mean a set of financial services for the digitally literate and included. Those savvy enough to keep up, make the most (or best they can) of new technologies, products and services. But there is another part of the population who won't have the confidence or capability or resources to conduct their affairs online. Those who want or need traditional services, on the phone and the high street, those who therefore might not get offered the best deals or most appropritate products.

In other markets we have seen that this comes with the dangers of cross-subsidisation. I no longer receive any paper communication about my energy bill. I get an e-mail and invited to submit my meter readings at least twice a year through an app. I switched to this deal as it was cheap. It's uncomfortable to admit that I am being subsidised because poorer people than me pay a lot more for their energy. Partly because they may not have switched, but also because those on pre-payment meters are too often stuck on tariffs that they can't afford and therefore find it very hard to switch out of. For the same energy usage, they are likely to be paying around £300 more than me.

One challenge the internet brings to financial services is that of cross-subsidisation. Although keeping up with the latest digital advancements costs money, so do the high street outlets and branches that many people depend on. Reflecting this in price can cause all sorts of issues and problems in the market, something the regulator needs to be acutely aware of as we progress

The future and the role of the regulator

I am not a technology geek. I am not about to predict the future, or imagine tomorrows world as yet another sci-fi movie. I don't know how things will evolve or how I or anyone else will make use of new technology in financial services or in any other market.

We are changing and evolving and that is a great thing. We all move at different speeds, we adopt sooner rather than later, but of course some of us will miss out, be left behind, be excluded.

The regulator must have the capability and capacity to keep up. It doesn't have to lead, it shouldn't lead, but it must have the skills and ambition to be not far behind, for that is where many consumers will be. But at the same time, it must also have the capacity and awareness to consider the market for those who are further back. And for those vulnerable consumers who may be exposed to greater risk through more choice, personalised advertising and new technologies. It must remember that no-one is average, not even me, but we are all part of a distribution, and the FCA must take care to serve every part of that distribution. That doesn't necessarily mean it must spend equal time on everyone, and indeed it should always look to the most vulnerable first.

Since the FCA came into being, I think there has been an encouraging start - to get the balance between the industry and consumers right. With the right investment and the right staff, it is well placed to see us into the next decade too.