Is competitiveness an appropriate statutory objective for a conduct regulator?
Roundtable discussion - Summary
Tuesday 22nd February 2022 11am - 12pm

Attendees

- **Chair:** Marloes Nicholls - Head of Policy and Advocacy at the Finance Innovation Lab
- Heather Buchanan - Director of Policy at the APPG on Fair Business Banking
- Matthew Conway - Director of Strategic Policy at UK Finance
- Jon Dennis - Sustainable Finance Manager at WWF
- Kevin Hollinrake MP - Co-Chair of the APPG on Fair Business Banking
- Peter Gibson MP – Co-Chair of the APPG Personal Banking and Fairer Financial Services
- Tina McKenzie - Incoming Policy and Advocacy Chair at the Federation of Small Businesses
- Nick Shaxson - Co-Founder of the Balanced Economy Project
- Martin Wolf - Chief Economics Commentator at the Financial Times
- Simon Youel - Influencing Money Lead at Positive Money
- Carl Packman - Head of Corporate Engagement, Fair By Design Campaign at Barrow Cadbury Trust
- (Observer: Ben Guerin - Senior Policy Analyst, Prudential Policy, Future Regulatory Framework team, Prudential Regulatory Authority, Bank of England)

Background

- HM Treasury has published major new proposals for the Future Regulatory Framework for the UK's financial services sector post-Brexit.
- The flagship proposal is to introduce a new (secondary) statutory objective for regulators – the Financial Conduct Authority ('FCA') and the Prudential Regulation Authority ('PRA') – to promote "the long-term growth and international competitiveness of the UK economy, including the financial-services sector." In the case of the FCA, this would be added to its existing (primary) objectives to promote market integrity, consumer protection, and competition.
- This proposal has sparked an important debate. For example, some industry representatives (such as UK Finance) have called for the new objective be restricted to the growth and competitiveness of the financial-services sector only. Civil society organisations, on the other hand, have warned that asking regulators to promote international competitiveness risks repeating the mistakes of the past: just a decade ago, HMT and parliamentarians identified regulators' excessive concern for competitiveness as one of the key causes of the global financial crisis 2007/08. (The Finance Innovation Lab has published an MP briefing on these issues: Why 'competitiveness' objectives for regulators risk UK finance success.)

Summary of participant views

- Roundtable participants were unanimous that the 'international competitiveness' of the finance sector should not be a primary objective of financial regulation, as has been proposed by some.
- There was also agreement that the proposal would significantly affect financial regulation, because statutory objectives shape everything regulators do, including the allocation of their resources, the research they undertake, and the basis upon which they make their decisions and are held to account.
- However, there were different opinions on whether it should become a secondary objective, as the government has proposed, or remain as it is – namely, a factor that regulators should 'have regard to' when pursuing their objectives (as has been the case since March 2021). **The remainder of this note summarises the key points of debate.**

Definitions

- A number of participants raised that 'international competitiveness' is not well-defined or well-understood (in the FRF and other forums), and this ambiguity makes it hard to assess the implications of the government's proposal. Is it about attracting businesses to domicile or do business in the UK? Is it about promoting the UK financial sector relative to other financial centres? Or something else? (We note that the Financial Services Act 2021 defines it as 'relative standing of the UK as a place for firms to be based or carry on activities'.)
- In particular, it is important to note that international competitiveness is distinct from competition within a market (the promotion of which already is a statutory objective of regulators) – though the two often get mixed up. In fact, the pursuit of an internationally competitive sector may reduce competition when it is interpreted as promoting large winners.
- Attendees welcomed an offer from the proposal's advocates to help to meaningfully define 'international competitiveness'.

Purpose of financial regulation

- Participants broadly agreed that the government is right to consider how regulators can maximise financial services' contribution to the UK's economic, social, and environmental goals.
- However, there was some disagreement over which goals should be prioritised over others. It was said, for example, that financial services exports should not "wag the dog" and be prioritised over ensuring that people and businesses have access to financial services. Another view was that UK financial regulators had to take due account of international competitiveness because regulators in other jurisdictions, including the EU, do so. But it was also argued that we should not simply follow the EU because it's the status quo (its approach to the Irish border and the consequential impacts for SMEs being a case in point).

Regulatory independence

- It was argued that the proposal risked eroding the ability of regulators to act independently in the public interest if it requires regulators to act as a cheerleader for firms. This could also exacerbate the undue influence of industry lobbyists.

Financial stability and consumer protection

- A number of participants worry that the proposal conflicts with primary objectives to promote stability and consumer protection, although it was also noted that regulators already manage tensions between existing objectives.
- It was argued that a focus on competitiveness risks sparking a 'race to the bottom' in standards. For example, we could expect to see a watering-down of key post-GFC measures to raise capital requirements in the banking and insurance sectors as a result.
- Participants quoted Andrew Bailey (then CEO of the FCA, today Governor of the Bank of England) who said in 2019 that the regulator "was required to consider the UK's competitiveness, and it didn't end well, for anyone." It was argued that the 'have regard to' competitiveness duty that regulators were issued by the Chancellor in 2021 is already very close to what the Financial Services Authority had in place before the GFC, and which HMT and parliament went on to remove post-crisis.
- It was noted that Sheldon Mills of the FCA described the new trade-off the proposal would introduce when he gave evidence to the Treasury Select Committee in February 2022. He said that FCA regulators would be hindered in their ability to take action to protect consumers (or meet their other objectives) where it could be argued that such measures impede competitiveness. However, others argued that as a secondary objective, international competitiveness could not make a regulator do what a primary objective would preclude it from doing. So, if an action that promotes international competitiveness did not promote any primary objective, the action would not be carried through.

Economic growth vs. international competitiveness

- Participants broadly welcomed moves to strengthen the regulators' mandate to promote long-term economic growth.
- Some thought HM Treasury could do more to clearly set out what the Future Regulatory Framework means for SMEs and the real economy.
- A number of participants highlighted that the proposed new objective could be contradictory, arguing that promoting the international competitiveness of UK finance could undermine economic growth. They pointed to academic evidence, such as by the Bank for International Settlements, that has found that a country can have 'Too Much Finance' and act as a drag on economic growth. This can happen, for example, as a result of a domestic 'brain drain' whereby high pay in finance draws talent from other, more productive sectors.

Levelling up

- While it is estimated that two thirds of the UK's financial sector employees are based outside of London, London remains the UK's financial hub.
- It was argued that asking regulators to promote international competitiveness could undermine the government's 'levelling up' agenda. This could happen, for example, if rising net foreign inflows into UK finance raise the real exchange rate, making other sectors that are

disproportionately based elsewhere in the UK (e.g. manufacturing) less competitive against exports (the so-called "Dutch Disease").

Net zero

- Another important area, it was stated, that the introduction of a secondary international competitiveness objective could undermine and/or directly conflict with is the government's commitment to develop the world's first 'net zero aligned finance centre'. Currently, regulators must 'have regard to' net zero. Since this sits lower down in their hierarchy of duties, concerns concerns were raised that a new competitiveness objective would detract from this.

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