TheCityUK

A roadmap for economic recovery

The role of financial and related professional services

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About TheCityUK

TheCityUK is the industry-led body representing UK-based financial and related professional services. We champion and support the success of the ecosystem, and thereby our members, promoting policies in the UK, across Europe and internationally that drive competitiveness, support job creation and ensure long-term economic growth. The industry contributes over 10% of the UK's total economic output and employs more than 2.3 million people, with two thirds of these jobs outside London. It is the largest tax payer, the biggest exporting industry and generates a trade surplus exceeding that of all other net exporting industries combined. It also makes a real difference to people in their daily lives, helping them save for the future, buy a home, invest in a business and protect and manage risk.

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Foreword

Covid-19 has unleashed an unprecedented public health emergency across the world, the economic aftershocks of which will shape the global economy for decades to come.

While uncertainty, flux and change have been mainstays across the past year, the successful vaccination drive across the country has bought a renewed sense of optimism. This is the backdrop against which we are publishing this report. It sets out how the UK-based financial and related professional services industry can play its role in the nation's post-Covid-19 economic recovery, supporting customers, businesses and communities up and down the country.

Just over a decade ago, TheCityUK was set up in the wake of a different global economic crisis. At that time, it was actions from within some parts of the industry that were the problem. In this crisis, the industry has acted as a shock absorber, protecting jobs and providing a safety net for customers and businesses. As a result, it is well placed and determined to continue to be part of the solution and support the recovery.

It is the case that after every economic crisis there is a period of economic renewal. But given the deep economic disparity across the country, there will need to be a concerted effort by all stakeholders to ensure that this economic renewal and the opportunities it will bring are realised in all areas of the UK.

As a truly national industry and one that is a major economic contributor, financial and related professional services will be central to driving economic recovery and making stronger all the UK's regions and nations. Some of the measures we propose in this report can be taken forward by the industry itself, while others will require collaboration with government, regulators and other stakeholders.

While the sense of optimism is palpable, the path ahead remains unpredictable and policy prescriptions will need to evolve as the fog further lifts. There is, however, one thing of which we are certain: that our industry is committed to continuing to adapt and playing its part in helping deliver jobs, prosperity and growth for communities and economies across every part of our country.

Miles Celic
Chief Executive Officer, TheCityUK

Executive summary

Charting a course through the many challenges we face

Covid-19 has had a huge impact on the UK, but it is not the only challenge our country faces as we progress through the phased approach to ending restrictions and driving economic recovery. The pandemic has accelerated or accentuated many existing trends: the international slide towards protectionism and isolationism; the changing relationship between the UK and its largest single market; regional disparities of wealth, investment and opportunity; the need for greater diversity, inclusion and equality at all levels – especially at senior levels and in the boardroom; climate change and technological transformation. These are unquestionable challenges. But there are also substantial opportunities. Our industry is ready to play its role in helping the UK to seize them.

The international slide towards protectionism and isolationism

The pandemic has exacerbated existing geopolitical tensions. It has also put the nation state centre stage, in sharp contrast to the international collaboration seen during the global financial crisis. This means the benefits of globalisation and open markets to consumers and businesses need to be restated with clarity and purpose. The UK is uniquely well positioned to make this case. As we make clear in the section on international trade and investment, the British government and our industry should continue to advocate for open markets and guard against protectionism.

The changing relationship between the UK and its largest trading partner

We stand ready to support the UK to thrive outside the European Union (EU), and ensuring that our industry is at the heart of future Free Trade Agreements (FTAs) will be crucial to achieving that goal. As we set out in the section on international trade and investment, the global economy is increasingly driven by data and recent trends towards digital protectionism could limit growth. The government should work with like-minded trade partners to create a gold standard of digital free trade agreement chapters that cater for technology-enhanced services businesses, limit data localisation, and position the UK globally as a critical digital trade hub.

Regional disparity of wealth, investment and opportunity

Prior to Covid-19, the UK was one of the most regionally unequal and most centralised countries in the developed world. This framed the backdrop of the Conservative Party's central 2019 general election promise to spread opportunity and growth to left-behind areas – its commitment to 'level up' the country. In the levelling-up section, we set out how our own ongoing programme of activity can help empower local leaders to build and promote the strength and opportunity of financial and related professional services in the many thriving industry hubs across the UK's regions and nations.

The need for greater diversity, inclusion and equality at all levels – especially at senior levels and in the boardroom

Just as regional inequality is holding Britain back, so is gender, racial and social inequality, among others. In the section on industry skills and talent, we recognise the need to add greater impetus to the industry's own approach to diversity and inclusion and the crucial need to attract a more diverse workforce.

Climate change

When the Covid-19 pandemic struck, many feared that the issue of climate change would move down the agenda. However, with the UK hosting COP26 this year, it has rightly remained centre stage. Our industry remains focused on the need to advance sustainability goals and in the sustainability section we set out our thinking on how it can work in partnership with government to do so.

Technological transformation

The acceleration of digital adoption for customers and employees brings with it the need to do more on digital literacy, reskilling and upskilling. In the technology section, we detail some of the ways that technology can be put at the centre of the UK's economic recovery.

Moving forward on stable economic foundations

All these challenges share important characteristics while differing in their immediacy. This report seeks to balance near-term action with long-term vision. It is written on the assumption that those longer-term goals are harder to achieve without decisive action to bring some stability in the near-term.

For financial and related professional services, much of its contribution will build on the central role it has played in the crisis so far: acting as a shock absorber to support people, businesses and communities. Banks have worked closely with government to deliver government-backed loans to more than 1.6 million companies at pace. Customers have been offered holidays on mortgage and loan repayments. Call centres have continued to operate, and firms have maintained access and support for customers.

Legal and professional services have continued to give crucial advice to businesses and people up and down the country, many dealing with existential issues they have never encountered before. Essential employees have come into offices to ensure markets can operate efficiently and seamlessly. And the industry is providing long-term finance so that, ultimately, savers' and pensioners' money can continue to grow.

Beyond that, in the regulation section, we look at the potential for regulation – including through some changes that are enabled by our exit from the EU – to focus on pro-recovery and pro-investment measures. These include enabling the industry to find new, sustainable ways to support small and medium-sized businesses (SMEs). To help achieve this we set out in the tax section how the UK can stimulate investment through the tax system. In the international trade and investment section, we outline the necessary action to ensure businesses in the UK can make the most of the digital and data-led opportunities the government helps to create through its global trade deals.

The power of the industry and the road ahead

Financial and related professional services make a real difference to people in their everyday lives, helping them to save for the future, buy a home, invest in a business, and protect and manage risk.

The industry is a key engine of the UK economy and a major national strategic asset. It contributes around £10 in every £100 of economic output. It is the nation's largest taxpayer, biggest exporting industry and employer of over 2.3 million people – two thirds of them outside London. The industry's trade surplus is greater than all other net exporting industries combined.

The strength and resilience of the industry stems from its ability to adapt to change and transform. This is at the heart of how it has remained globally competitive and world leading for centuries. Fundamental to that is its continued ability to attract the best talent from home and overseas who together develop better products and services for customers and markets.

The UK is at a crossroads and the financial and related professional services industry can help steer it in the right direction. As we emerge from this health and economic crisis, our role is to be part of the solution: acting as an engine for economic recovery in the near term while driving forward industry change that will help us make the country stronger in the decades ahead. The industry cannot do it alone but, in partnership with government and regulators, it is determined to play its full part, supporting jobs and growth now and into the future. This report sets out our roadmap.

Summary of recommendations

Levelling-up

Levelling-up as a concept needs to be given further rigour and must be measured by clear metrics

Levelling-up needs to be hardwired into government thinking, and a national strategy of this scale must have effective measures of success. Sub-national data sets can inform decision making within government and chart progress against key aims, and wider indicators of policy success should be established to better judge the economic and societal value of efforts to rebalance and redistribute.

Levelling-up requires a national focus with a ministerial champion and dedicated delivery team

A Cabinet-level ministerial champion should be appointed to join up government activity at the centre and align it with regional strategies across the UK. That minister should also lead a dedicated delivery team with a cross-cutting departmental brief to drive policy programmes, engage the private sector and local stakeholders and measure delivery against key indicators.

Local and regional leaders must ensure place-based strategies are informed with industry insight

Local leaders should look to formally include industry insight into their plans and strategies. By creating dedicated forums for industry representatives, channels can be established to identify where financial and related professional services leaders can support the delivery of local initiatives. This is an even greater priority given the economic recovery challenge that we face.

Industry skills and talent

Increase action on diversity and inclusion

The industry will work to identify the structural issues that impact underrepresented groups and promote best practice and collaboration. Firms should accelerate efforts to collect data, report and make public commitments to increase workforce diversity.

A commitment to youth and mobility schemes

The industry should double-down on commitments to sustain young people in apprenticeships, paid internships, graduate programmes and underpin this with mentoring and social mobility schemes.

Focus on upskilling and reskilling

The industry should upskill staff to build creativity, adaptability, emotional intelligence, and reskill in areas of technology, data, sustainability and remote and digital tooling.

Align training to industry needs and future skills

Government investment in skills and training needs to be aligned with the skills needs of business and accessible to ensure that training opportunities deliver the greatest possible impact.

Technology

Accelerate development of resilient digital systems and infrastructure to enable all parts of the UK to benefit from the future of financial and related professional services

Technology must be placed front and centre of the UK's approach to driving economic recovery. High-quality, resilient infrastructure will enable the industry to support its customers however they choose to access services and allow firms to recruit and operate across the UK's regions and nations.

Prioritise the development of digital identity in the UK

Digital identity infrastructure has the potential to deliver inclusive economic growth by providing greater access to services, reducing fraud, delivering efficiencies and increasing transparency. Government should take a leading role in coordinating cross-industry and public-private sector efforts to bring about digital identity in the UK.

Create a diverse public-private forum to consider how to drive greater digital adoption and literacy among UK consumers

More needs to be done to improve digital literacy and encourage consumers to make use of technological developments that could enhance their financial resilience during challenging economic circumstances. Government and industry should consider what could be done in the short term to accelerate digital consumer capability and adoption so that people can make use of the tools available to them.

Regulation

Prioritisation of the regulatory pipeline to focus on pro-recovery and investment measures

The regulatory agenda should fundamentally change its focus in the short term, with a greater emphasis on identifying measures concentrated on investment for the recovery.

Consult on proposals to unlock capital through regulatory reform

UK regulators should consult with industry to identify and take forward proposals to unlock capital through regulatory reform.

Interventions to mitigate impacts of economic cycles

Central banks and regulators should continue to enhance their focus on procyclicality and take forward interventions that mitigate the negative impacts of economic cycles.

International trade and investment

Encourage countries to coordinate Covid-19 economic policy measures

The UK should work with other countries to coordinate Covid-19 economic policy measures in two key areas:

- Cooperation on trade-related aspects of Covid-19 recovery plans. Play a leading role in coordinated discussions on recovery strategies on the international stage.
- Coordination of strategies around Covid-19 related investment protection laws. These efforts should be focused on avoiding protectionism against foreign direct investment.

Put digital trade in services at the heart of ambitious FTAs

The government should aim to put digital trade facilitation at the heart of new FTAs and work with like-minded trade partners to create a gold standard of digital trade chapters that cater for technology-enhanced services businesses, limit data localisation, and help position the UK globally as a critical digital trade hub.

Prioritise building coalitions of supporters of open trade

Together, government and industry should continue to build coalitions of countries favouring open trade to support the global trading system.

Closer coordination between industry and government to promote greater liberalisation of trade

Working together to advance international standard setting would help reinvigorate global trade and maintain a global environment which supports foreign investment.

Related professional services

Maintain and build the global competitiveness of the UK's related professional services sectors

Government must focus on this through its policy on developing future trade agreements and the domestic business environment to ensure the professional services sectors can fully play their role in facilitating economic growth.

Acknowledge and promote the importance of English law, the rule of law and UK legal services

Maintaining and further developing a strong, competitive and well-regulated legal services sector remains essential for the sustainable growth of the UK economy. Certainty and stability are key to the international attractiveness of this globally-leading sector and the UK's role as a leading centre for dispute resolution.

Focus on talent, mobility, and data

The development and retention of domestic talent and securing access to international talent are critical in knowledge-based services. Ensuring that practitioners can access their clients' markets, including through recognition of their professional qualifications, and the cross-border flow of data must all be prioritised in the government's drive to build new trade agreements.

Sustainability

Government and industry must work in partnership to advance sustainability goals

While governments set long-term policy frameworks, it is the actions of private-sector firms that will help meet targets, including the UK's commitment to bringing net greenhouse gas emissions to net zero by 2050.

Government should ensure that the right incentive structures are in place

This includes identifying incentive structures that can help promote sustainable investments over non-sustainable ones and considering how the tax system could, in the future, be used to incentivise sustainable finance.

Government and industry should continue to encourage international collaboration, including by leveraging the UK presidency of COP26

International cooperation will be critical to tackling what is fundamentally an international challenge. Such cooperation can help maximise the effectiveness of various national initiatives, and also ensure that best practice and innovative solutions are shared more widely. Government should also aim to show global leadership in this area, and leverage the UK's Presidency of COP26, now due to be held in November 2021, to demonstrate such leadership.

Tax

The UK tax system should support long-term, sustainable economic growth to maximise the financial and related professional services industry's contribution to economic recovery

The government should focus on stimulating long-term, sustainable economic growth and consider carefully the impact that new tax measures and action to rebuild public finances could have on investment.

Tax policy changes should be clear, consistent and developed through consultation to continue to attract businesses to the UK

A stable, consistent and simplified approach to tax policy will have a positive impact on inward investment and the overall attractiveness of the UK's business environment. The government should use this opportunity to develop a long-term, strategic approach to taxation in the UK which aligns to its broader policy objectives by producing a 'Tax Roadmap' to help businesses plan for upcoming changes.

Consider how the international nature of the UK-based financial and related professional services industry can be maximised for the benefit of the UK's economic recovery

It is vital that government continues to prioritise international competitiveness to ensure that the UK can continue to attract inward investment in financial and related professional services and other industries as well as focusing on international cooperation to minimise complexity arising from market fragmentation.

1. Economic analysis*

*Economic analysis is based on data available and assumptions prevailing as of 23 March 2021

The impact of the pandemic on the UK economy

Due to the simultaneous demand and supply shock caused by Covid-19, the public policy responses to contain its spread, and the prolonged nature of the crisis, the economic impact of the disease has proved to be far worse than that of the global financial crisis of 2008-09.

In the broadest terms, the effects in the UK arose from the very sharp reduction of household income and expenditure and the hit to business profits and cashflow, plus the ongoing uncertainty in the business environment, leading to reduced investment.

These factors were evident in the most recent official data, which showed that GDP declined by 9.9% year on year in 2020,[1] and by 2.9% month on month in January 2021.[2] Given that consumer spending is the main driver of the UK economy, representing two-thirds of GDP, the ongoing impact of pandemic-related policy on household income as well as spending opportunities will have significant consequences for the UK economy.

The policy response has encompassed strong monetary as well as fiscal elements. While the benchmark interest rate had been close to zero even before the emergency rate cuts implemented in March 2020 (when the benchmark rate was cut from 0.75% to 0.25% and then further to 0.1%), the market signalling around these rate reductions and the additional quantitative easing boosted confidence by increasing liquidity, which in turn helped maintain stability in domestic capital markets.

The future state of the UK economy

The consensus view regarding the UK economy is that after experiencing a deep recession (GDP contraction of 9.9%) in 2020, the economy will rebound in the next two years, with average (median) forecasts of 4.7% for 2021 and 5.9% for 2022.[3] A summary of consensus forecasts is presented below:

Figure 1: UK GDP forecasts, % change year on year, consensus* March 2021
Source: HM Treasury

	2021	2022
Median	**4.7**	**5.9**
Lowest	2.1	3.3
Highest	6.1	8.7

*Consensus forecasts are drawn from 34 forecasters split between 'City' forecasters (primarily banks) and independent forecasters (both private-sector firms and multilateral institutions)

The rebound in GDP in 2021 is expected to be driven mainly by government consumption, which is expected to grow by 7%, followed by fixed investment and private consumption. In 2022, private consumption is finally expected to experience the strongest growth among GDP components, with a growth rate of 6.8%, followed by fixed investment. The consensus expectation is that government consumption growth falls back significantly in 2022, to 2.5%. A summary of consensus forecasts for GDP components is presented below:

1 TheCityUK calculations based on the Office for National Statistics, 'Gross Domestic Product: chain volume measures: seasonally adjusted £m', (12 February 2021), available at: https://www.ons.gov.uk/economy/grossdomesticproductgdp/timeseries/abmi/pn2

2 Office for National Statistics, 'GDP monthly estimate, UK: January 2021', (12 March 2021), available at: https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/gdpmonthlyestimateuk/january2021

3 HM Treasury, 'Forecasts for the UK economy: a comparison of independent forecasts', (March 2021), available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/970101/Forecomp_March_2021.pdf

Figure 2: UK GDP components forecasts, % change year on year, median, consensus* March 2021

Source: HM Treasury

	2021	2022
Private consumption	5.1	6.8
Government consumption	7.0	2.5
Fixed investment	6.1	6.1
Inventories (contribution to GDP growth, ppt)	0.6	0.1
Net trade (contribution to GDP growth, ppt)	-1.8	-0.1

*Consensus forecasts are drawn from 34 forecasters split between 'City' forecasters (primarily banks) and independent forecasters (both private-sector firms and multilateral institutions)

However, these forecasts are highly uncertain; downside economic risks are still abundant, and much remains unpredictable both with regard to the trajectory of the pandemic and to business and consumer behaviour. Forecast uncertainty is particularly high for 2022: the 2021 forecasts included in the consensus sample range from 2.1% to 6.1% (a 4 percentage point spread) while the 2022 forecasts show a 5.4 percentage point spread, ranging from 3.3% to 8.7% and indicating materially differing views of the pace and profile of the recovery.

Taking the four-step roadmap out of lockdown introduced by the government in February 2021[4] as our baseline assumption, and assuming that social and mobility restrictions are gradually eased throughout the second quarter of the year, and also assuming that no restrictions are reintroduced in the second half of 2021 or in 2022, TheCityUK's view is broadly in line with this consensus. We expect a rebound in economic output in 2021, and for the recovery to then gather pace in 2022 — although, given the high level of uncertainty, our expectations for 2022 are more tempered than the consensus. Our analysis also assumes that the pandemic does not trigger sustained behavioural changes relative to the pre-pandemic period (for example, a permanent shift to more arts consumption at home rather than in cinemas and theatres).

Although there are not yet sufficient data to be able to draw firm conclusions, it is possible that the effects of the pandemic could worsen existing UK regional inequalities. Loss of income associated with lost or reduced employment will naturally have varying effects depending on (among other things) the level of pre-pandemic household income — which differs widely across the UK's regions, ranging from £29,362 per head in London to £16,995 in the North East.[5] Meanwhile, our analysis of pre-pandemic and current unemployment rates by region and nation shows that the unemployment rate increased in all regions and nations between January and December 2020 — but the increase in the unemployment rate varied significantly, ranging from 0.3 percentage points in Scotland to 2.2 percentage points in London.[6]

Fiscal policy has been and will remain critical in light of the limits of monetary policy in supporting demand. Given the reduction of household income and expenditure and of business investment, the unprecedented policies to support private sector income have been welcome, despite the fact that they and other support measures have taken the public finances into uncharted territory.

4 Further detail is available at https://www.gov.uk/government/publications/covid-19-response-spring-2021/covid-19-response-spring-2021-summary#step-2---not-before-12-april

5 Office for National Statistics, 'Regional gross disposable household income: all NUTS level regions', (4 June 2020), available at: https://www.ons.gov.uk/economy/regionalaccounts/grossdisposablehouseholdincome/datasets/regionalgrossdisposablehouseholdincomegdhi

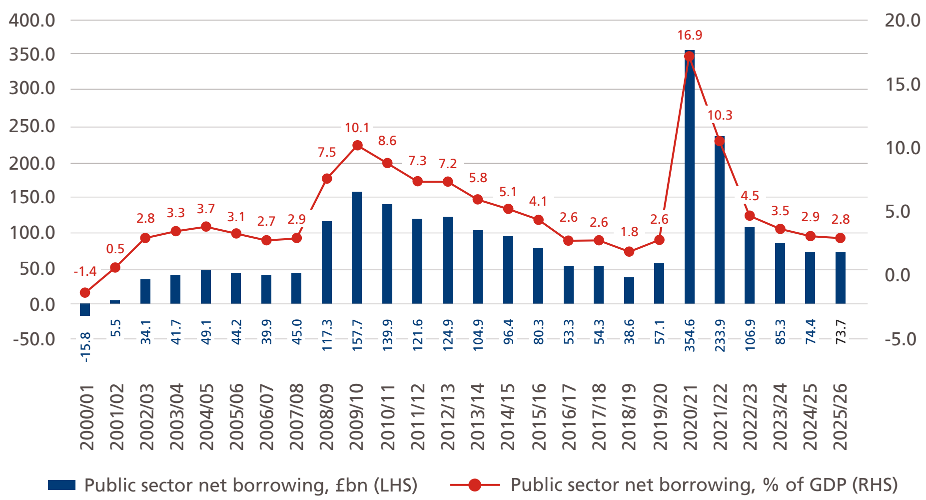
6 Office for National Statistics, 'HI00 Regional labour market: Headline labour force survey indicators for all regions', (23 February 2021), available at: https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/datasets/headlinelabourforcesurveyindicatorsforallregionshi00

The implications of near-to medium-term fiscal policy are profound given the scale of the costs of fiscal measures in response to Covid-19. According to the latest data from the Office for National Statistics (ONS), public sector net debt reached £2.1trn at the end of February 2021, equivalent to 97.5% of GDP. Public sector net borrowing was £278.8bn during the period April 2020–February 2021, compared to £50.6bn in the year-earlier period.[7]

In February 2021, the Institute for Fiscal Studies forecast that government borrowing will reach around £400bn and £160bn in 2020/21 and 2021/22, respectively. The amount of borrowing will then gradually reduce over the next few years to around £130bn in 2024/25.[8] The Office for Budget Responsibility (OBR) estimated in March 2021 that in its central scenario public sector net borrowing will be £354.6bn and net debt will be £2.2trn in 2020/21. The OBR also forecasts that public sector net debt will rise to the equivalent of 109.7% of GDP in 2023/24 before falling gradually thereafter (although remaining above 100% of GDP in 2025/26).[9] The expected increase in public sector debt and borrowing is far larger than that of the post-financial crisis period, as seen in the charts below.

Figure 3: Public sector net borrowing

Source: Office for Budget Responsibility



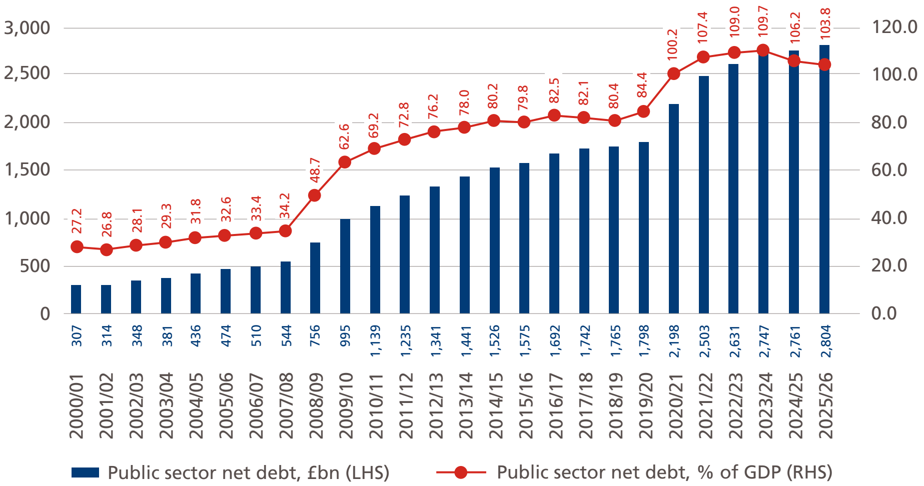
7 Office for National Statistics, 'Public sector finances, UK: February 2021', (19 March 2021), available at: https://www.ons.gov.uk/economy/governmentpublicsectorandtaxes/publicsectorfinance/bulletins/publicsectorfinances/february2021

8 Institute for Fiscal Studies, 'Through a glass, darkly: Uncertain outlook for the public finances', (16 February 2021), available at: https://ifs.org.uk/uploads/Through-a-glass-darkly.pdf

9 Office for Budget Responsibility, 'Public finance databank – March 2021', (3 March 2021), available at: https://obr.uk/data/

Figure 4: Public sector net debt

Source: Office for Budget Responsibility



Combined with the reduction in tax revenue because of the collapse of private sector income and spending, this increased government spending will most likely require a heavier tax burden on individuals and businesses over the next few years. We suggest recommendations for the development of tax policy on pages 54 and 55, and note that the government should be mindful not to attempt to rebuild public finances too quickly by disincentivising investment with new tax measures. Nevertheless, revenue increases are unlikely to match the scale of increased expenditure, and the government is likely to have to issue additional debt. This increase in the government debt level may have implications for the UK's sovereign risk rating.

Total goods and services exports from the UK increased by an average of 5.5% annually over the past decade, reaching £690.8bn in 2019, 54% of which was goods exports and the remaining 46% of which was services exports. Inward foreign direct investment (FDI) flows averaged £61bn annually over the past decade. TheCityUK expects that UK exports and inward FDI will increase in 2021 and 2022 compared to 2020 as the global economic recovery boosts external demand.

The role of financial and related professional services in the economy and the economic recovery

The financial and related professional services industry is—and will remain, post-pandemic—a key contributor to the UK economy. Unlike the economic recession of Q2 2008 – Q2 2009, which was triggered by a collapse in financial-sector activity, the current recession originated outside the financial services sector. The UK-based industry is far more robust today than it was in the aftermath of the 2008-09 global financial crisis. For example, according to data from the World Bank, banks' capital-to-assets ratio in the UK was 6.8% in 2018 (the latest available data), compared with 4.4% in 2008 and 5.4% in 2009.[10] The ratio of bank non-performing loans to total gross loans was 1.1% in 2018 (latest available data) compared with 1.6% in 2008 and 3.5% in 2009.[11] According to the Bank of England's latest Financial Stability Report, at the end of September 2020, UK banks and building societies had common equity Tier 1 (CET1) capital holdings more than

10 World Bank, 'Bank capital to assets ratio (%)', (March 2021), available at: https://data.worldbank.org/indicator/FB.BNK.CAPA.ZS

11 World Bank, 'Bank nonperforming loans to total gross loans (%)', (March 2021), available at: https://data.worldbank.org/indicator/FB.AST.NPER.ZS

three times higher than in 2007, pre financial crisis.[12]

The industry is among the UK's largest industries as measured by GVA. Across their domestic and international activities, financial and related professional services contributed £194.2 to UK gross value added (GVA) in 2020, representing 10.3% of total UK GVA.

Financial services productivity remains almost twice as high as whole-economy productivity in terms of output per hour. Output per hour for the financial services sector was £62.9 in 2020, compared with the average for all industries of £36.4.[13]

Over 2.3 million people work across the country in financial and related professional services, accounting for 7.4% of total UK employment. Financial services have almost 1.1 million people in employment and related professional services comprising legal services, accounting services and management consultancy have over 1.2 million people in employment.

The industry provides important support to the UK's fiscal position and balance-of-payments position, in part by attracting FDI. Inward FDI is a volatile indicator that can show significant changes from year to year (for example, in any given year the figure may be distorted by a particularly large deal). In 2019, the latest year for which data are available, the financial services sector attracted £2.5bn in FDI; the previous year's figure had been negative (indicating that direct investment interests were sold, and/or reinvested earnings were negative). Over the past four years (2016-19), cumulative inflows of financial services FDI totalled £35.5bn, equivalent to 10.9% of overall FDI. The professional, scientific and technical services sector that includes TheCityUK's defined related professional services attracted the most FDI (19.7% of the total during the same period).[14]

UK financial services are also a vital source of tax receipts, contributing £75.6bn in tax revenue in 2019/20. This accounted for 10.1% of total UK tax revenue.

Based on data from the ONS, TheCityUK estimates UK-based financial and related professional services generated a trade surplus of £77.9bn in 2019. The industry's trade surplus is more than the combined surplus of all other industries in the UK that register trade surpluses (it is the UK's biggest net exporter). This helps to partly offset the UK's trade-in-goods deficit of £130.9bn.

A strong financial and related professional services industry is therefore a driving force for overall economic growth, and the industry is well-placed to help facilitate the UK's economic recovery post-Covid-19. Its contribution can take various forms: it can make a direct contribution to the economy, but also an indirect contribution through, for example, investment platforms and business and personal loans. In other words, the relatively strong position of the industry means it is well placed to continue to supply finance to the economy to facilitate growth.

12 Bank of England, 'Financial stability report', (December 2020), available at: https://www.bankofengland.co.uk/-/media/boe/files/financial-stability-report/2020/december-2020.pdf?la=en&hash=876D253A7E169E6462692A41101AA698E7897EA1

13 Office for National Statistics, 'Breakdown of contributions, whole economy and sectors', (19 February 2021), available at: https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/labourproductivity/datasets/annualbreakdownofcontribution-swholeeconomyandsectors

14 TheCityUK calculations based on Office for National Statistics, 'Foreign direct investment involving UK companies (assets and liabilities): liabilities', (21 December 2020), available at: https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/datasets/ foreigndirectinvestmentinvolvingukcompaniesassetandliabilityinward

2. Impact of Covid-19 on key trends and policies driving industry change

In our report 'A vision for a transformed, world-leading industry' in collaboration with PwC, we discussed some of the big challenges facing the industry – geopolitical tensions, technological transformation, changing terms with major trading partners, and an imperative to rebuild trust, to name but a few – and its readiness to transform to meet those challenges. The unprecedented circumstances that have stemmed from the onset of the Covid-19 pandemic have further accelerated some of those trends and highlighted others that are driving change across the financial and related professional services ecosystem. There are also policy changes that should be made to keep the UK a competitive and thriving international financial centre into the future. How the industry, government and regulators should respond to these changes is considered below.

Analysis and recommendations

Levelling-up

ANALYSIS

The government's stated ambition is to 'level up' the UK. This is shorthand for a wide-ranging domestic policy programme aimed at improving productivity, infrastructure and wellbeing across all our country's regions and nations. Reaffirmed by ministers, it has the potential to be an even greater, defining tenet of government policy and a guiding principle of the UK's recovery.

The economic impact of the pandemic has the potential to hit left-behind areas hardest, and to exacerbate existing UK regional inequalities. Industry clusters across the UK are, however, well-placed to act as the engines for restarting and rebuilding the economy. Major UK centres which each have more than 30,000 financial and related professional services industry jobs include Birmingham, Bristol, Edinburgh, Glasgow, Leeds and Manchester.

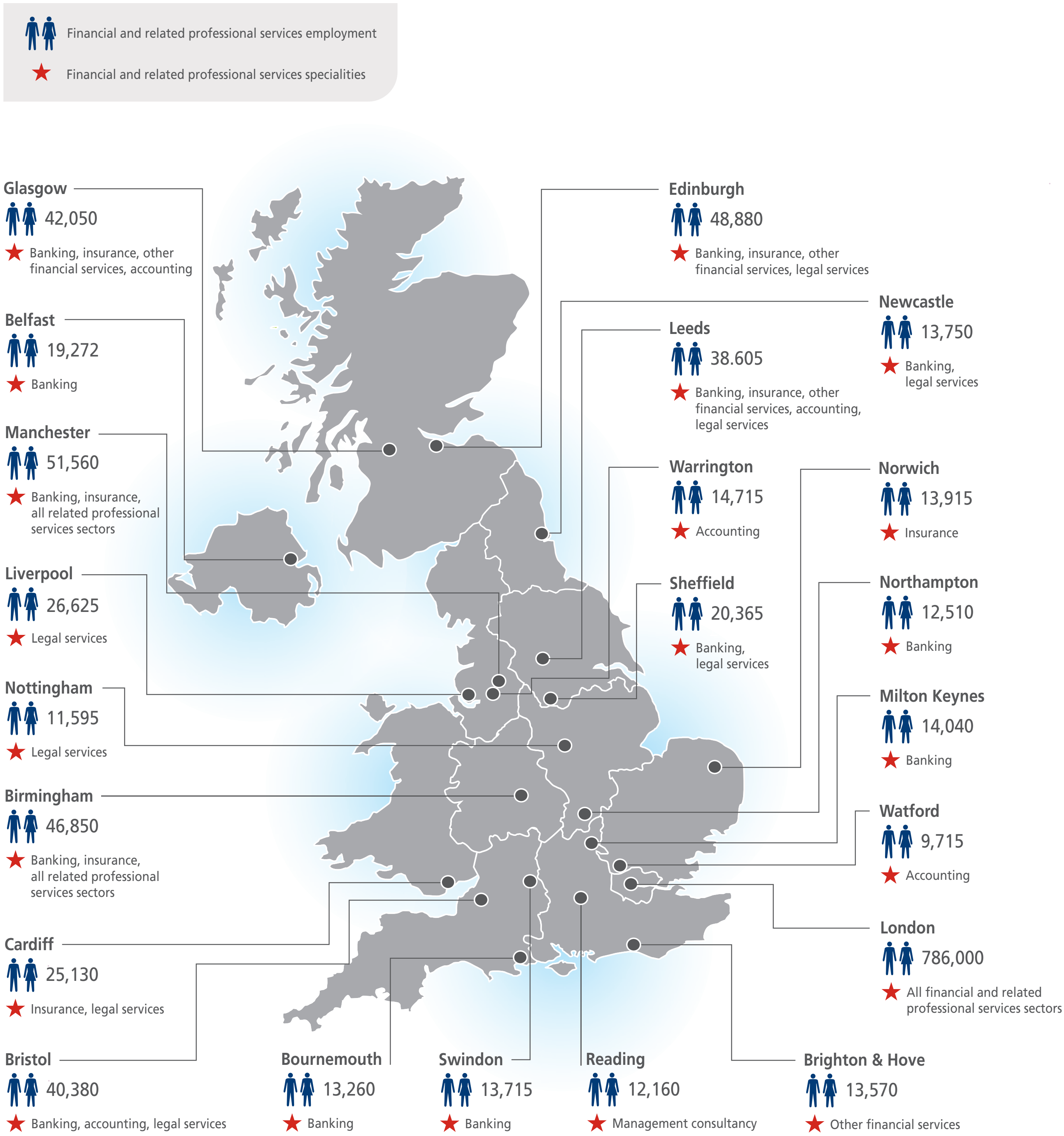
Overall, 21 towns and cities across the country each have more than 10,000 people in employment in the industry. Levelling-up must therefore harness the regional footprint of the industry, which is ready to support the delivery of the agenda across our towns, cities and regions.

The economic impact of the pandemic and the risk it poses to regional inequalities, combined with the political requirement to rebalance the economy, means levelling-up is a necessity. The challenge, presented by the acceleration of change post-Covid-19, and the wider pressures on the public finances, may also mean that we need to rethink long-standing approaches to investment, partnerships and decision making, if we are to be successful in meeting it.

Place-based plans, devolved settlements, and regional coalitions will continue to set a direction of travel for improving skills, supporting businesses and boosting infrastructure and connectivity; and all of these themes have long been industry priorities that echo across the regional ecosystem. This chapter, however, aims to define a specific role for the financial and related professional services industry in supporting the delivery of the levelling-up agenda with a partnership-led approach.

Figure 5: Financial and related professional services clusters across the UK, 2019

Source: Office for National Statistics, Nomis, Northern Ireland Department for the Economy and TheCityUK estimates



Recovering and rebalancing across the regions and nations

TheCityUK established a dedicated Regions & Nations programme in 2017, aimed at promoting the strength and opportunity of industry hubs and clusters. A network of City Chairs – senior industry leaders representing Belfast, Birmingham, Bristol, Cardiff, Leeds, Greater Manchester and Newcastle – were appointed to lead our work locally, and in Scotland we work alongside Scottish Financial Enterprise. The City Chairs, and our wider UK member network, provide invaluable perspectives on the industry's capacity for delivering inclusive, local growth. Below, we explore the local contribution of financial and related professional services, and how this can support levelling-up.

Building regional talent pipelines and equipping the regional workforce for the future

Preconceptions of the industry providing predominantly 'City jobs' are misguided. The two thirds of industry employees that are based outside London support major operations of some of the largest companies in the world; these jobs are high quality and highly-skilled. The industry has taken a leadership role in forging partnerships, particularly with education providers and local leaders in equipping the workforce with skill sets for the future.

Courses such as the University of the West of England's MSc in Financial Technology, supported by Bloomberg and Deloitte, show how the industry is collaborating with higher education institutions to develop a leading-edge offer for students in burgeoning innovation hubs like Bristol.

This example highlights the active involvement of the industry in designing and developing entry routes into the industry. For regional leaders, they offer a template for levelling-up that can be applied more widely. They also pose a question about the retention of local talent and how firms look to ensure that the entry-level jobs or training schemes they provide lead to second and third jobs, and local career paths. Covid-19 may also have a significant bearing on the dispersal of leadership talent across UK hubs, and further regional opportunities at a more senior level if home working trends continue. We must ensure, however, that local talent is nurtured by equipping employees with the skills needed for progression into leadership positions, whether that is in the office or across virtual platforms.

Rewiring government to level up

The UK government has set about reconfiguring its machinery and mindset in order to meet the levelling-up challenge. Significant parts of the Whitehall estate are being re-located or repurposed across the UK regions, with the ultimate aim of moving 22,000 civil servants out of London.[15]

This agenda will see: the Ministry for Housing, Communities and Local Government occupying a ministerial office outside of the capital; the UK Infrastructure Bank being established in Leeds and the 'Treasury North' campus bringing 750 civil servants to Darlington. Additionally, approaches to economic policymaking could be radically rethought, following the HM Treasury review of the Green Book formula.[16]

These are significant changes and the government has shown a commendable ambition to move major elements of central Whitehall departments beyond the M25. It should seek to do so with regulators, too, in order to drive the growth of challenger institutions and regional clusters. Yet we urge the government to ensure that these moves are not merely symbolic gestures, and instead represent a wider, and more comprehensive reconfiguration aimed at achieving economic rebalancing across the UK.

As a starting point, this new geography for UK policymaking presents prime opportunities for fostering greater understanding of local industry activity, and collaboration with local agendas.

Strengthening regional hubs with sustainable investments

Levelling-up will require a focus on investment that extends beyond the built environment and hard infrastructure. It requires finding answers to key questions of how regional clusters can be better linked, home workers and start-up firms better connected, and basic services extended to all.

Before Covid-19, transformational changes were in progress. High-speed rail construction had started; the West Midlands had acted as testbed for 5G roll-out; regional airports provided domestic and international gateways with dedicated, point-to-point services. Furthermore, financial and related professional services had acted as an enabler for such major projects. The way in which the pandemic has changed behaviours over a short space of time – through more remote working, a greater reliance on technology, and social distancing – could have far-reaching consequences. The extent to which these behavioural shifts are permanent is unclear, but the industry must have them in view as it considers future, long-term investments across the regions and nations.

The financial and related professional services industry should therefore present itself to local and central government as an enabler that can support the delivery of forward-looking projects in the regions and nations. Digital connectivity is a given, and transportation will remain critical. But it might also look at how it can support sustainable agendas, for example in the race to net-zero, where local strategies – such as the West Midlands' #WM2041 initiative – will be just as critical, if not more so, than top-down plans led from the centre.

The government's Levelling-up Fund Prospectus highlights transport schemes that reduce carbon emissions, as well as regeneration and investment into town centre areas, as

15 HM Government, Budget Speech 2020, (March 2020), available at: https://www.gov.uk/government/speeches/budget-speech-2020
16 HM Government, Final Report of the 2020 Green Book Review, (November 2020), available at: https://www.gov.uk/government/publications/final-report-of-the-2020-green-book-review

particular priorities.[17] It also sets out a role for the private sector in supporting major projects. As such, there may be opportunities for working in partnership to better connect left behind or isolated areas in a sustainable way, and the industry is well positioned to enable this progress.

Supporting the SME economy

Access to finance, workspace and expertise are key components of the contribution of financial and related professional services to businesses operating in the wider economy and the 5.8 million SMEs across the UK. The industry can have an important role in supporting SMEs with finance at every stage, yet this is perhaps most critical when they are starting-up.

Across the UK's regions and nations there are examples of the industry supporting emerging companies with a more holistic offer. Companies can support burgeoning start-up communities with regional programmes aimed at delivering shared workspace, incubation for high growth projects, and events, networking opportunities and mentoring services for new companies. Innovation – and FinTech specifically – is a key area in which the industry can impart expertise and practical support for start-ups.

Place-based strategies

Encompassing many of the themes above are the place-based strategies that set out blueprints for the growth of areas across the regions and nations. Approaches to rebalancing the UK has taken different forms in the past involving, for example, the creation of metropolitan counties, the prominence of the now-defunct Regional Development Agencies, and the direct election of metro mayors. Levelling-up was an ambition set out at Cabinet-level and is an agenda that could define this government's domestic policy agenda. The progress we have seen so far suggests that it will be driven, partly at least, by central government initiatives. Efforts must, however, supplement and augment the role of local leaders in driving local economic growth.

As a starting point, levelling-up may mean different things to different areas, and our City Chairs have convened leaders across the UK to gather insights on local priorities and challenges. In some cases, local leaders need more power to harness growth and innovation, in others, more fundamental support in reducing inequality, or improving productivity is required.

Metro mayors and combined authorities have set a template for growth across city regions. Budgetary levers related to housing, transport and skills, as well as wider business support services, provide local leaders with the means by which they can deliver inclusive growth. Their soft power, deployed when bringing together local leaders, can be just as influential in ensuring that the government does not lose sight of its ambitions to level up the UK. Additionally, Covid-19 has seen many regional leaders using their roles to establish recovery committees and groups, some of which have incorporated a sectoral focus, aimed at highlighting and coordinating local interventions, as areas confront the challenge of post-pandemic economic recovery and renewal.

For its part, the financial and related professional services industry has the capacity to support the delivery of a virtuous circle of high-quality jobs, improved skills, efficient

17 HM Government, Levelling Up Fund: Prospectus, (March 2021), available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/966138/Levelling_Up_prospectus.pdf

connections and new infrastructure; but it should effectively demonstrate how it can integrate with local leaders' aims and objectives.

National and local leaders can make place-based strategies more accessible by ensuring they are more consistent in structure, and clear in focus. Measurement of success is also an important aspect; local electorates and potential industry partners need clear indicators of how far local strategies have delivered on achieving local economic growth.

RECOMMENDATIONS

The concept of levelling-up needs to be given further rigour, and must be measured by clear metrics

Regional rebalancing is a challenge that transcends a government's term in office, and as such, `levelling-up' needs to be hardwired into the UK's policymaking machinery. Moreover, a national strategy of this scale - which depends on the success of the UK's constituent parts - must have an effective measure of success.

Sub-national data sets can inform decision making and chart progress and TheCityUK has been supportive of the work that the Office for National Statistics has done in making this information more readily available. Improving the access to and availability of localised statistics can enhance policymaking and present a clearer line of sight on regional priorities, and this is work that must continue.

Additionally, wider indicators of policy success should be established - in consultation with the public, regional leaders and industry stakeholders - to ensure that the levelling-up agenda has rigour. These could include metrics focused on personal wellbeing, environmental impact and lifestyle indicators, for example.

In addition, key government departments - in particular, the economic ministries with a focus on driving national growth - should look to refresh their business plans with key performance indicators specific to levelling-up, to ensure this remains a cross-government priority.

Levelling-up requires a national focus, with a ministerial champion and a dedicated delivery team

Levelling-up was an ambition set out by the Prime Minister within days of taking office. It has given regional rebalancing a national significance, though it is an agenda that is ultimately local in its focus. To meet the challenge, central government must work hand in glove with local leaders.

Despite various policy announcements and a redeployment of government resources across the UK regions, `levelling-up' lacks an institutional framework with clear lines of accountability.

A Cabinet-level ministerial champion - potentially within one of the key, economic central departments - should be appointed, with a focus on joining up government activity at the centre. That minister should also lead a dedicated delivery team with a brief to: align policy programmes with key local initiatives; engage the private sector and local stakeholders; and measure departmental delivery and outputs against key indicators.

Local and regional leaders must ensure place-based strategies are informed with industry insight

The financial and related professional services industry, through the work of TheCityUK's City Chair network, has been active in identifying where it can meet and support local leaders in tackling local challenges and priorities. However, local leaders should look to formally include industry insight into their plans and strategies.

There are best practice examples of where local and national governments have collaborated in creating such forums: the Scottish Government's Financial Services Advisory Board, reporting directly to the First Minister is one; another, in the Covid-19 context, is the West of England Combined Authority's Professional Services Recovery Taskforce.

By creating dedicated forums for sectoral leaders, channels can be established to identify where financial and related professional services can support the delivery of a local plan or major project, and help develop local skills offerings.

In order to support this recommendation, TheCityUK will take its Regions and Nations Programme to the next stage, deepening our focus on meeting local policy challenges and using industry perspectives to help empower local leaders to effectively build and promote the strength and opportunity of financial and related professional services across the country.

Levelling-up skills

Firms have embraced flexible approaches to accommodating a remote workforce, operating at a distance from office bases. We explore this trend further in a 'future of work and offices' case study on page 27. Employees are – for the moment at least – less reliant on geography as a factor determining their ability to work. While it may be too early to predict the permanence of these changes, which have been accelerated by the pandemic, shifts in the future of work need to be considered as part of the levelling-up agenda.

Beyond investment in hard infrastructure, government-led efforts to level up should take a wider and softer approach that incorporates a focus on skills development and unlocking regional talent pools, including through the targeted use of mentoring. Flexible working arrangements increase the potential for firms to reach a wider labour market which is less restricted by transport networks, distance and other local barriers. However, this could also mean there will be greater onus on firms to develop and upskill their workforce in new ways, potentially in a virtual setting. In policy terms, and in line with these shifts, central and local government should consider how it can support the day-to-day fundamentals of living and working at home, for example by prioritising universal, high speed broadband connectivity.

As the industry continues to adapt, and the horizon becomes clearer, a priority for financial and related professional services is striking a balance that works from an operations – and an employee – perspective. Hubs across the UK will continue to extend the industry's reach across the UK's regions and nations and ensure that central operations are accessible and within reach of the wider workforce.

Industry talent and skills

ANALYSIS

Covid-19 has reframed our perceptions of what is possible. Financial and related professional services employers have been at the heart of that response showing their resilience and ability to adapt to remote working, ensuring people can access the products and services they need as well as implementing various loan schemes and mortgage holidays, and supporting customers and clients to navigate the rapidly evolving landscape.

In January 2020, the Financial Services Skills Taskforce, launched by the then Chancellor Philip Hammond and convened by TheCityUK, highlighted the impact of megatrends such as digitisation, demographic change and globalisation on the industry. Covid-19 has further accelerated these trends with customers adapting to digitised products and automated services, and with firms moving to near 100% remote-working practices in a matter of days.

The disruption is framing new ways of working for the long term that the industry needs to embrace and prepare for. Half of financial services workers have indicated that they want to work more flexibly following the pandemic.[18] This will support the industry's efforts to build more inclusive career paths, increase productivity and retain qualified employees. The advantages for employers and employees are too important to ignore.

Covid-19 has led to over nine million people being furloughed in the UK with a disproportionate impact on the youngest and oldest in society.[19] Overwhelmingly, our industry continues to retain talent and provide opportunities with well-paid jobs that people can do from home, with government research showing that at its peak 4% of financial services staff were furloughed.[20]

However, the industry must not be complacent. Despite functioning well in response to the crisis, it will not be immune from the restructuring affecting other parts of the economy. Reskilling and upskilling our current workforce in areas such as technology, digitisation, empathy and adaptability is critical to overcoming existing skills gaps and will help ensure the industry, and wider UK economy, has the right skills needed for the future.

By ensuring our employees are equipped to work from home effectively and moving towards a greater use of blended teams and digital tools, productivity can be protected and enhanced. By doubling down on efforts to ensure outreach schemes are accessible across the UK and enhance diversity, the industry will be better placed to bolster the economy by building home-grown talent. A highly-skilled, productive workforce is key to the UK's future success.

The Financial Services Skills Commission (FSSC), borne out of the recommendations from the Financial Services Skills Taskforce, will play a major role in understanding these Covid-19 related issues. The FSSC began the debate in this area with the publication of 'The Future of Work: Lessons from a pandemic' and will continue to work with industry and policymakers to address the impact of the pandemic on people in financial services.[21]

18 Financial Services Skills Commission & KPMG 'The future of work: Lessons from a pandemic' (October 2020), available at: https://wp.financialservicesskills.org/wp-content/uploads/2020/10/WEB_Future-of-FS-workforce_KPMG-FSSC_October-2020.pdf

19 Office for National Statistics 'Labour market overview, UK: August 2020' (August 2020), available at : https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/bulletins/uklabourmarket/august2020

20 HM Revenue & Customs 'Coronavirus Job Retention Scheme statistics, (October 2020), available at: https://www.gov.uk/government/publications/coronavirus-job-retention-scheme-statistics-october-2020/coronavirus-job-retention-scheme-statistics-october-2020

21 Financial Services Skills Commission 'The Future of Work: Lessons from a pandemic' October 2020, available at: https://financialservicesskills.org/research/

Diversity and inclusion

Following calls across society for greater diversity, inclusion and equality, these issues have been underscored as pressing priorities. This has added greater impetus to financial and related professional services' own approach to diversity and inclusion. It has shone a spotlight on the need for greater inclusivity and equality at all levels of the workforce and accelerated the need for action to ensure the industry can attract a more diverse workforce and improve the working experience for employees who are currently underrepresented.

The industry has made good progress in this area through positive initiatives within firms and an increase in public commitments to diversity and inclusion, but more can still be done. At the senior leadership and board level, in particular, a lack of diversity remains an ongoing challenge and further tangible change must be made. The commercial benefits of making progress in this area are indisputable. Firms with increased ethnic or cultural diversity are 33% more likely to have increased profitability,[22] as are firms with better gender balance in their leadership. There is also a correlation between diverse leadership teams and increased performance and innovation, which will be crucial to driving economic growth. As outlined in the FSSC's report 'Diversity Data: The challenges of data collection and developing a culture of self-reporting' data measurement, analysis and reporting will be a major factor in improving diversity, inclusion and progression.[23]

Impact of Covid-19 on skills across the industry

Covid-19 has had a wide-ranging impact on skills for the industry and the wider UK economy alike. It has dramatically reframed perceptions of what is possible for the future of work, and has redoubled the appreciation of value, while demonstrating the resilience and agility of firms and their people.

Rapid shift towards different ways of working

Covid-19 has led businesses and managers to realise that physical proximity is not necessary to carry out duties or onboard talent. Work has become a thing that you do, rather than a place that you go.

As noted earlier in this report, the industry responded at pace to the crisis, investing significantly in equipment and technology to enable individuals to work remotely. This has decentralised working practices from London and other big UK cities to towns and suburbs across the country.

Questions remain around whether this will lead to a fall in demand for workspace over the longer term, but in the short term it may provide opportunities to build clusters of skills across the UK and equalise some of the regional imbalances currently seen between the South East and the rest of the UK. This will require improved broadband to support and facilitate flexible working which will also help to maintain productivity.

Remote working has been positively embraced by many workers. Nearly 80% of employees in financial services say they can perform most or all aspects of their work remotely, 50% have said that they want to see a continuation of remote and flexible working beyond Covid-19 and 26% said they want to work from home permanently.[24]

22 McKinsey & Company, 'Delivering through diversity', (January 2018), available at: https://www.mckinsey.com/~/media/McKinsey/Business%20Functions/Organization/Our%20Insights/Delivering%20through%20 diversity/Delivering-through-diversity_full-report.pdf?shouldIndex=false

23 Financial Services Skills Commission 'Diversity Data: The challenges of data collection and developing a culture of self-reporting' October 2020, available at: https://wp.financialservicesskills.org/wp-content/uploads/2020/10/Diversity-Data-the-challenges-of-data-collection.pdf

24 Financial Services Skills Commission & KPMG, 'The future of work: Lessons from a pandemic', (October 2020), available at: https://wp.financialservicesskills.org/wp-content/uploads/2020/10/WEB_Future-of-FS-workforce_KPMG-FSSC_October-2020.pdf

Workers said that they have achieved better work-life balance, increased productivity and better wellbeing. While some firms are looking to get back to the office and business as usual – albeit at reduced capacity – workers have expressed that they want to see flexibility and remote working retained and will judge potential employers on their approach to these.

Despite moving to a virtual world almost overnight, it is clear that not all will benefit from home working. Individuals starting internships, those early in their careers and those in client-facing roles will need the face-to-face exposure that comes from office working. Appetite for remote working also depends on the home situation; for many it is not an appealing or practical option. To remain attractive, firms will need to support flexible working and enhance employees' experience through equipping remote workers and installing well thought through employee wellbeing programmes.

It is too early to say what the long-term impact of working from home is, however, the industry must remain responsive to ensure the evolving workplace is fit for the future. This could include building collaborative spaces in the workplace and enhanced digital collaboration tools.

Globalisation of skills

Covid-19 has increased virtual working and slowed down the movement of people across borders. Virtual working means firms can truly access a global marketplace of skills. Securing and onboarding talent can be done virtually, and teams can be spread across the UK and other countries. However, this notion of globalisation has also been challenged by the fact that a global crisis has, thus far, been managed at a country level. Physical border closures and restrictive quarantines have reinforced the need for a pipeline of domestic home-grown talent. The UK should review the resilience of global supply chains, a theme discussed in the international trade and investment section, with firms considering reshoring and near-shoring roles. This talent will be crucial to build the UK's productivity.

Increased technology adoption and demand for revised skill set

The acceleration of technology and digital adoption for customers and employees has been particularly rapid and 30% of financial services workers have said[25] they need more digital and technological expertise to fulfil their roles as a result of the pandemic.[26]

Digital and data channels have shifted from secondary customer engagement options to being the only option for many. This has led to an increased demand for new capabilities, some of which cannot be filled by current skills in the system. Every participant in a recent survey said that the pandemic has changed the skills they need for their role.[27]

Those capabilities are not just confined to data and technology, but also 'human' skills and behaviours that have been utilised by the most resilient companies throughout the pandemic; adaptability, resilience, creativity and innovation and emotional intelligence. Sixty one per cent of financial services workers believe the pandemic has changed the skills needed for their role.[28]

The table overleaf shows how these skills and behaviours have been used by firms to mitigate the crisis. The industry should focus on building out these skills in their workforce.

25 Ibid

26 Ibid

27 KPMG & Financial Services Skills Commission 'The Future of Work: Lessons from a pandemic' October 2020 available at: https://wp.financialservicesskills.org/wp-content/uploads/2020/10/WEB_Future-of-FS-workforce_KPMG-FSSC_October-2020.pdf

28 Ibid

In doing so they will provide a pipeline of highly skilled, productive talent for the whole of the economy. A Future Skills Framework will be published by the FSSC later this year and will set out the skills and capabilities that are essential to the future success of the industry.

Skills and behaviours needs accelerated by Covid-19

Skills and behaviours	Rationale
Technology, data, cyber and digital	With the onset of homeworking, an increasing need for online marketing, web development and more data than ever before, skills in technology, data, cyber security and digital will be more important than ever.
Adaptability and resilience	Workers who adapt quickly to changing environments and work requirements and who can thrive when faced with rapid change will be vital. The ability of business to respond positively to change stems from the ability of its employees to adapt and consistently improve their skills.
Creativity	Covid-19 has shown the need for creative and innovative responses to problems. People who can think creatively and innovate will be crucial to the economy's success.
Emotional intelligence	Companies most likely to effectively navigate difficulties such as the Covid-19 crisis are those led by emotionally intelligent leaders. Empathy, self-awareness, motivation, self-regulation and social skills all lead to improved decision making, decreased occupational stress and increased personal and team performance. It has also been shown that businesses with higher numbers of people with high emotional intelligence have better bottom lines.

RECOMMENDATIONS

Increase action on diversity and inclusion

The industry will work to identify the structural issues that impact underrepresented groups and promote best practice and collaboration. Firms should accelerate efforts to collect data, report and make public commitments to increase workforce diversity.

A commitment to youth and mobility schemes

Given the pandemic's disproportionate effect on young workers,[29] the financial and related professional services industry should double-down on commitments to sustain young people in apprenticeships, graduate programmes, internships and underpin this with mentoring and social mobility schemes for this and future academic years. Industry should increase recruitment to these schemes from non-typical sources to support the drive towards diverse representation. Ensuring opportunities for the next generation of talent in financial and related professional services, while being mindful of the make-up of the industry's workforce, will be crucial to building back the economy and futureproofing against future crises.

While working from home practices continue, the financial and related professional services industry should expand new initiatives like online internships. This will increase the opportunities for work experience and deliver real benefits to individuals in

29 Office for National Statistics 'Labour market overview, UK: August 2020, (August 2020), available at : https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/bulletins/uklabourmarket/august2020

communities across the UK. The FSSC paper 'Keeping the pipeline of talent moving: making internships virtual' outlines the benefits of moving internships online and the hurdles to overcome.[30]

Focus on upskilling and reskilling

By reskilling employees to cater for roles created by an increasingly virtual world, the financial and related professional services industry can avoid adding to the unemployment figures across the UK. Industry should upskill employees to build creativity, adaptability, emotional intelligence, and reskill in areas of technology, data, sustainability and remote and digital tooling. This will futureproof the UK domestic workforce against future crises and strengthen the competitive position of the industry internationally. It is clear that with the move to shorter global supply chains due to Covid-19 and Brexit, the UK will need to build the skills in the current domestic workforce.

Align training to industry needs and future skills

Government investment in skills and training needs to be aligned with the skills needs of business and accessible to ensure that training opportunities deliver the greatest possible impact. Recent government announcements on investments in training and increased employer involvement in skills planning are welcome. The 'lifetime skills guarantee' for adults without an A-level or equivalent qualification has the potential to be transformative for the UK's financial services sector. Nearly 300,000 (24%)[31] employees, the majority of whom are based in the North East, North West and Yorkshire & the Humber, stand to benefit from this initiative, potentially boosting their skills and enhancing their current and future employability. The government should ensure that the skills provided through this initiative meet future skills needs. Recent announcements on increased flexibility around apprenticeships are welcome but can go further to boost investment in training by employers. The FSSC is working with industry to publish a 'Future Skills Framework' to define these future skills needs and encourage investment in training.

CASE STUDY: The future of work and offices

Firms and their employees have adapted quickly to the requirements of remote working and many have adopted more flexible working policies that are set to last beyond the pandemic.

The rise of remote and flexible working has called into question the future of offices and of the cities they are located in. With increasing proportions of employees across the UK likely to work from home on any given day there are signs that demand for office space will reduce. An increasing number of companies across the industry have made public statements about reducing their office space in the coming years as expectations of a different style of working are being translated into long-term decision making, including through statements in annual reports.

This may result in lower employee density in commercial hubs, with a knock-on impact on other supporting services like hospitality and retail. However, remote working does not work for everyone and early indications show that while more financial services

30 Financial Services Skills Commission 'Keeping the pipeline of talent moving: making internships virtual' January 2021, available at: https://wp.financialservicesskills.org/wp-content/uploads/2021/01/Keeping-the-pipeline-of-talent-moving-making-internships-virtual.pdf

31 Financial Services Skills Commission analysis based on ONS annual Population Survey, October 2017.

workers want to work more flexibly following the pandemic, there remains appetite for office-based working.[32]

The appetite for office-based working means that existing and future office space will be reconfigured to increase the quality of space available for employee and client collaboration, rather than maximising occupancy.

The financial and related professional services industry thrives on collaboration and firms have not yet found tools to replicate the value of face-to-face interactions in all circumstances. For example, it will be vital to ensure junior employees receive the training they need, particularly in professions such as law or for those completing apprenticeship programmes, where in-person training and mentorship is critical to career development.

Firms must take seriously the impact on employees' physical and mental wellbeing. Remote working can increase periods of isolation, and many don't have access to workplace equipment designed to minimise the risk of musculoskeletal health issues arising from sitting for long periods of time.

On the other hand, research shows that flexible working policies boost employee morale, reduce turnover and are more inclusive of those who need to balance work with other commitments and/or health conditions. It can also be an important factor for potential employees and is therefore a vital component of attracting and retaining talent.

These emerging shifts in office space and associated commercial real estate may also have a knock-on effect for investors and pension funds. Real estate holdings accounted for £45bn of the direct investments held by public and private sector employee pension schemes in December 2019.[33] While this represents just under 4% of the total amount of direct investments held, the performance of investments in real estate face an uncertain future as a result of the Covid-19 pandemic, particularly in retail and commercial property. This was illustrated by a report published in March 2021 which found that 2020 witnessed a record net decline of retail stores of nearly 10,000 in the UK, with the authors suggesting the real impact of the pandemic is yet to be felt and the situation may get worse before it gets better.[34] Cities were particularly hard hit, with larger declines in multiple/chain stores while local markets and retail parks performed more strongly.

Consumers continue to shift to online retail experiences, with the proportion of retail sales reaching a record high of 35.2% in January 2021 compared to 19.5% reported in January 2020.

The accompanying rise in data storage and processing as well as logistics real estate to support the growth of online retail activity has seen investors increase their exposure to these asset classes.

While the long-term trends are difficult to predict national and local administrations across the UK are focused on playing an active role in shaping their recoveries, including considering the future working environments needed to support economic growth. As we discuss in the levelling-up section of this report the industry can support this agenda through a partnership approach to delivering inclusive local growth.

32 KPMG & Financial Services Skills Commission ' The Future of Work: Lessons from a pandemic' October 2020 available at: https://wp.financialservicesskills.org/wp-content/uploads/2020/10/WEB_Future-of-FS-workforce_KPMG-FSSC_October-2020.pdf

33 ONS, 'UK pension surveys: redevelopment and 2019 results', (2020), available at: https://www.ons.gov.uk/economy/investmentspensionsandtrusts/articles/ukpensionsurveys/redevelopmentand2019results

34 PwC, 'Store Openings and Closures - 2020' (March 2021), avilable at: https://www.pwc.co.uk/industries/retail-consumer/insights/store-openings-and-closures-2020.html

Technology and innovation

ANALYSIS

Technology has kept the UK economy running in the face of Covid-19 related restrictions on the movement of people and the operation of businesses. There has been a surge in internet usage for remote working, services and retail, with increased corporate investment in digital technologies.[35] As discussed in the industry talent and skills section, financial and related professional services firms have transitioned quickly to remote working, relying on technology platforms and infrastructure to enable employees to do their job in a secure environment.

The surge in the uptake of digital finance, banking and payments has highlighted the need to address gaps in digital literacy and regional digital infrastructure, such as access to mobile and internet coverage. The publication of the Kalifa Review in February 2021, has provided a critical roadmap of recommendations in areas that the government must address to position the UK at the forefront of FinTech at an international level. It also includes a focus on recovery in ensuring FinTech can support citizens and small businesses to access more and better and cheaper financial services.

Contactless payments, mobile apps and online customer support services have enabled consumers and businesses to manage their finances and transact during an uncertain and challenging period. The use of cash continues to decrease, with ATM transaction volumes falling by 62% year-on-year at the start of the UK's lockdown in March 2020, while many businesses transitioned to cashless payment systems to minimise contact during transactions. This has also been facilitated by an increase in the contactless payment limit from £30 to £45 in April 2020, and then to £100 in March 2021.[36] Increased digitisation of payments has also led to a surge in the uptake of cryptoassets, for example, with Bitcoin reaching all-time market highs in early 2021. This increased popularity of cryptoassets has highlighted the importance of their underlying blockchain technology and its uses as well as a range of regulatory considerations as recognised by HM Treasury's recent consultation on the UK's regulatory approach to cryptoassets.

Others across the financial and related professional services ecosystem have had to adapt too. For example, the Business and Property Courts have continued operating remotely with 85% of the usual volume of business and property cases having been handled in the 12 weeks from the first lockdown in March 2020, setting the UK apart from other jurisdictions.[37]

The industry is no stranger to technological innovation, but the extent to which technology has been relied upon to continue providing vital services is like nothing we have seen before. The emergence of Covid-19 raises many new questions and increases the urgency of finding answers to existing ones. Can technology be used to enhance the financial resilience of UK consumers? How can we protect our industry and its consumers against the risk of cyber-attacks and online fraud? Can technology enable more parts of the UK to benefit from economic recovery? What are the implications of a cashless society? What kind of regulatory regime needs to be in place in order to drive innovation and competition?

These issues must be considered by policymakers to determine the shape of the UK's economic recovery with key challenges including digital infrastructure and improving consumer capability. The uptake in digitised services has heightened regulators' focus on

35 McKinsey and Company, 'How COVID-19 has pushed companies over the technology tipping point—and transformed business forever', (October 2020), available at: https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/how-covid-19-has-pushed-companies-over-the-technology-tipping-point-and-transformed-business-forever

36 FT, 'Coronavirus accelerates shift away from cash', (2020), available at: https://www.ft.com/content/430b8798-92e8-4b6a-946e-0cb49c24014a.

37 Sir Geoffrey Vos, 'Chancellor of the High Court speech to Chancery Bar Association', (June 2020), available at: https://www.judiciary.uk/wp-content/uploads/2020/06/ChBA.NewNormal.ff_.pdf

risks, particularly concerning cyber security, as well as consumer protection issues such as fraud and scams.[38]

Digital infrastructure

Digital infrastructure is a core requirement of a technologically-enabled financial and related professional services industry. Throughout the pandemic the industry has depended on public digital infrastructure such as mobile and fixed broadband infrastructure to keep the economy running, power remote working and manage digital interactions between firms and consumers.

Some questioned the resilience of networks to cope with the increased usage, but research conducted by Which? found that 70% of consumers said that their connections had met their needs during lockdown.[39]

The pandemic has also highlighted the 'digital divide' between those with access to high-quality mobile and fixed broadband networks and those without. The UK's broadband speed ranks as one of the slowest in Europe. Only 10% of UK households have access to next-generation full-fibre broadband, which greatly improves internet speeds.[40]

The government has already committed £1bn of funding to the roll out of gigabit-capable broadband[41] but it is vitally important it continues to prioritise investment in broadband networks so that digital infrastructure is not a barrier to the UK's economic recovery. Across the UK, broadband speeds are among the slowest in Europe and rural areas continue to struggle to access high quality speeds.[42] The government must get the basics right first, including by ensuring high quality coverage across the UK so households are not excluded from the benefits of digital financial services and remote working opportunities, as outlined in the industry talent and skills section of this report.

Improving consumer capability

The pandemic has prompted broader adoption of digital services such as mobile banking and cashless and online payments. Over one in three digital banking users say they have become more confident using technology during the Covid-19 pandemic and 83% intend to use digital banking in the same way or more frequently after lockdown. Almost half say they plan to reduce or stop their use of branches and in-person banking.[43]

While this is certainly an increase, these figures only consider those who already use digital financial services and point to an adoption rate that lags technological advancement. More needs to be done to encourage consumers to make use of newer developments that could deliver significant benefits.

Open banking is a prime example which has the potential to deliver improved consumer outcomes, including by enabling consumers to aggregate all their products in one place,

38 World Economic Forum, 'COVID-19 spurred a rise in FinTech', (October 2020), available at: https://www.weforum.org/agenda/2020/10/covid-19-financial-technology-fintech-regulation/

39 Verdict, 'Covid-19 highlights "crucial need" for digital infrastructure across the UK', (July 2020), available at: https://www.verdict.co.uk/uk-digital-infrastructure/

40 The Guardian, 'UK broadband speeds among slowest in Europe, study finds', (September 2020), available at: https://www.theguardian.com/technology/2020/sep/02/uk-broadband-speeds-among-slowest-in-europe-study-finds

41 Department for Digital, Culture, Media and Sport, 'Gigabit broadband rollout milestone reached', (August 2020), available at: https://www.gov.uk/government/news/gigabit-broadband-rollout-milestone-reached

42 Cable, 'Worldwide broadband speed league 2020', (March 2021), available at: https://www.cable.co.uk/broadband/speed/worldwide-speed-league/#highlights

43 Virgin Money UK, 'Confidence using online banking grows during lockdown as consumers embrace digital', (May 2020), available at: https://www.virginmoneyukplc.com/newsroom/news-and-releases/2020/confidence-using-online-banking-grows-during-lockdown

providing insights on their spending habits and automating decisions such as how much to save each month. But consumer adoption of services powered by open banking remains relatively low; only 11% of consumers use automated savings apps.[44]

Concerns about security and trust of third parties could be acting as a barrier to adoption.[45] Indeed, 59% of consumers worry about falling victim to fraud when using digital payments.[46]

While caution should be encouraged, particularly at a time when we are seeing increased levels of cybercrime, it is vital that concerns about online security do not unnecessarily hamper wider adoption of digital financial services that could bring substantial benefits to consumers.

To tackle this issue, efforts to progress innovation in financial services must be accompanied by businesses assuming responsible stewardship of data and providing more education and support, particularly for those consumers that lack the confidence and skills to access financial services online. If consumers have the skills to protect themselves from online fraud and they understand how businesses use their data, they may be more likely to take advantage of the services available.

RECOMMENDATIONS

Accelerate development of resilient digital systems and infrastructure to enable all parts of the UK to benefit from the future of financial and related professional services

Digital infrastructure is a core requirement of a technologically-enabled financial and related professional services industry. The existing speed and availability of key infrastructure in the UK, such as broadband, lags most other leading financial centres, putting at risk growth, attractiveness and ability to innovate. It is vital that the government provides access to high-quality digital infrastructure, so that individuals and households can benefit from digital financial services and more flexible, remote working opportunities, as set out in the industry talent and skills section of this report. It is also vital in maintaining the resilience of the UK's financial system, which is increasingly reliant on technology. Ensuring the UK has access to high-quality digital infrastructure means businesses can operate quickly and reliably.

The government should ensure commitment to the ambition that ultrafast broadband of at least 100Mbps is available to 95% of UK premises (as outlined in the National Infrastructure Delivery Plan 2016 – 2021). We would also advocate for the rollout of 5G connectivity more widely than the main urban areas in which it is already available. To improve on-the-go connectivity, the government should increase the minimum connectivity and quality standards for train operating companies to 4G-equivalent speeds.

Prioritise the development of digital identity in the UK

Digital identity is a key area which has been placed under the spotlight with the emergence of the Covid-19 pandemic. Digital identity infrastructure has the potential

44 Attest, 'UK Future of Finance Report 2020', (2020), available at: https://www.askattest.com/original-research/the-uk-future-of-finance-report-2020

45 Faith Reynolds, 'Open banking: a consumer perspective', (January 2017), available at: https://home.barclays/content/dam/home-barclays/documents/citizenship/access-to-financial-and-digital-empowerment/Open-Banking-A-Consumer-Perspective-Faith-Reynolds.pdf

46 Attest, 'UK Future of Finance Report 2020', (2020), available at: https://www.askattest.com/original-research/the-uk-future-of-finance-report-2020

to add 3% to UK GDP by 2030[47] and deliver inclusive economic growth by providing greater access to services, reducing fraud, delivering efficiencies and increasing transparency. It could also address challenges around digital adoption amongst the UK consumer base, while offering a more secure way for businesses and consumers to interact online.

In September 2020, the government outlined next steps for the UK's use of digital identity, which included the announcement of new principles to boost secure use of digital identity. This is a welcome development, but there is a real need for government, as recognised in the Kalifa Review, to take a leading role in coordinating cross-industry, public and private sector efforts to bring about digital identity in the UK.[48]

Create a diverse public-private forum to consider how to drive greater digital adoption and literacy among UK consumers

The pandemic has prompted broader adoption of digital services such as mobile banking and cashless and online payments. More needs to be done to improve digital literacy and encourage consumers to make use of technological developments that could enhance their financial resilience during a period of challenging economic conditions.

Government and industry should consider what could be done over the short-term to accelerate digital consumer capability and adoption so that people can make use of the tools available to them. As a first step, government should create a diverse public-private forum to establish the key consumer issues and consider what actions can be taken in the immediate term to drive adoption of solutions.

CASE STUDY: Financial resilience

The financial shock of Covid-19 has impacted many aspects of people's socio-economic wellbeing, and the ability to recover from this has underlined the importance of financial resilience for consumers and businesses alike.

According to the FCA,[49] the proportion of adults experiencing low financial resilience rose by 35% from 20% of UK adults in February 2020 to 27% in October 2020. The FCA also found that three in eight adults (38% or 20m) have seen their financial situation overall worsen because of Covid-19; 15% (7.7m) have seen it worsen a lot.

There are signs of increasing economic inequality with more people on lower personal incomes reporting reduced income.[50] Groups that have been particularly hard hit include: the self-employed, adults with a household income of less than £15,000 per year, those aged 18-54, and Black and Minority Ethnic (BAME) adults.[51]

As we note in the section on regulation, the UK regulatory authorities have taken decisive and welcome action to contribute to the capacity of the industry to support consumers and the real economy.

For customers and businesses with stressed finances, measures are being offered by banks and finance firms across the UK including mortgage holidays, payment deferrals,

47 Department for Digital, Culture, Media and Sport, 'Next steps outlined for UK's use of digital identity', (2020), available at: https://www.gov.uk/government/news/next-steps-outlined-for-uks-use-of-digital-identity

48 EY, 'UK FinTech: Moving mountains and moving mainstream', (2020), available at: https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/emeia-financial-services/ey-uk-fintech-2020-report.pdf

49 The FCA, 'Financial Lives 2020 survey: the impact of coronavirus', (February 2021), available at: https://www.fca.org.uk/publication/research/financial-lives-survey-2020.pdf

50 ONS, 'Personal and economic well-being in Great Britain', (January 2021), available at: https://www.ons.gov.uk/peoplepopulationandcommunity/wellbeing/bulletins/personalandeconomicwellbeingintheuk/january2021

51 The FCA, 'Financial Lives 2020 survey: the impact of coronavirus', (February 2021), available at: https://www.fca.org.uk/publication/research/financial-lives-survey-2020.pdf

the waiving of interest and late payments and facilities to increase credit limits and new credit lines.

Improving digital capability as we note in the technology section, is just one part of ensuring the industry can reach both businesses and consumers to help bolster their financial resilience.

Products and services designed to meet customer needs are critical. And this approach needs to recognise the fact that the UK has among the lowest saving levels of any developed nation. In a European context savings in the UK are on a long-term trend downwards. Among other economies in Europe, according to the Social Market Foundation, only Greece saves as little.[52]

A potential way to increase the rate of savings in the UK and bolster financial resilience is to address this through the enhancement of workplace saving schemes and their relationship with personal savings products, including ISAs, as well as both workplace and personal pensions.

Many businesses are considering savings tools for employees that strengthen their financial resilience and wellbeing. An example of this is the 'sidecar savings model,' a hybrid saving tool that combines an accessible emergency savings account with traditional defined contribution retirement saving. Other features may also include payroll deduction emergency saving tools with a pension saving rollover feature.[53]

The industry's contribution to these efforts should be matched by a focus on minimising financial exclusion. This includes offering products which are easier to understand, easier to access and give customers a clearer view of their financial situation than before, through various educational and information tools. For example, advice on how to manage cash flow, protect against cyber threats and develop new business models to counteract the effects of the pandemic will be critical for businesses.

This focus, coupled with the creation of a diverse public-private forum to establish key issues faced by customers, as recommended in this report, will enable the industry to play its part in enhancing financial education and resilience and supporting its customers through the challenges ahead.

52 Social Market Foundation, 'Barclays, Savings in the Balance Managing Risk in a Post-Crisis World', (December 2014), available at http://www.smf.co.uk/wp-content/uploads/2014/12/Social-Market-FoundationPublication-Savings-in-the-Balance-Managing-risk-in-a-post-crisis-world.pdf

53 Nest Insight, 'Supporting emergency saving', (October 2020), available at: https://www.nestinsight.org.uk/wp-content/uploads/2020/10/Supporting-emergency-saving-policy-considerations-and-questions-for-future-research.pdf

Regulation

ANALYSIS

The 2008 global financial crisis and the resultant recession have been the subject of much debate and spur for reform in the years since. At a headline level, and taken together, the post-2008 regulatory reforms of the financial sector meant that the UK entered 2020 with well-capitalised institutions, built from the bottom up to be resilient in the face of financial shock.

The post-financial crisis reforms mean the industry is well placed to contribute to the UK's economic recovery as we note in the economic analysis earlier in this report. However, the regulatory and structural responses that are necessary to maximise this contribution are, much like the overall response to the pandemic, multi-faceted and have different degrees of urgency and time horizons.

As we discuss in the section on international trade and investment, UK policymakers need to actively engage on the international front, both bilaterally and multilaterally, to mitigate the possible impacts of regulatory fragmentation on global liquidity. More international coordination would also help firms navigate the complex, diverse landscape of the varied ongoing and potentially conflicting national regulatory approaches to Covid-19.

UK regulatory responses

In addition to the fiscal and monetary responses which we discuss in the economic analysis, UK regulatory responses to the pandemic can be grouped into three main areas:

- New initiatives or requirements introduced directly in response to the crisis, with the aim of protecting markets from volatility and protecting consumers who face financial shocks.
- Regulatory forbearance in the application of existing rules, requirements and deadlines.
- Cancellations, delays (of varying timescales) and postponements to regulatory activities, including the implementation of new requirements that are not critical to consumer protection or market integrity and consultation response deadlines.

The nature and extent of regulatory reprioritisations was illustrated in the Regulatory Initiatives Grid[54] published by the Financial Services Regulatory Initiatives Forum in May 2020. This aggregated the pipeline of regulatory interventions envisaged by the Forum's members (comprising the Bank of England/Prudential Regulation Authority, Financial Conduct Authority, the Payment Systems Regulator and the Competition and Markets Authority, with HM Treasury as an observer member).

The foreword to the Grid stated "taken together the collective regulatory response contributes to the financial services industry's capacity to support consumers and the real economy through the impact of Covid-19."

Those actions were welcomed and helped firms across the industry to focus resources on responding to key areas such as the provision of strong support to customers, particularly those facing financial difficulties.

However, as 2020 progressed there was concern that the pipeline of financial services regulation would simply continue to grow, with new initiatives adding to those paused earlier in the year. This was recognised in the September 2020 edition of the Grid[55] which

54 Financial Conduct Authority, 'Regulatory Initiatives Grid', (7 May 2020), available at https://www.fca.org.uk/publication/corporate/regulatory-intitiatives-grid.pdf

55 Financial Services Regulatory Initiatives Forum, 'Regulatory Initiatives Grid', (September 2020), available at https://www.fca.org.uk/publication/corporate/regulatory-intitiatives-grid-september-2020.pdf

noted that the resumption of paused initiatives would occur in a carefully coordinated fashion, balancing the needs of industry with objectives including consumer protection and financial stability. The Grid also noted that the timing of many initiatives remains tentative and all initiatives are under continuous close review in light of the external environment facing the financial services sector and the economy as a whole.

In common with decisions to be taken on, for example, tax policy, it is essential that decisions taken to modify or reform the regulation of the industry in response to the Covid-19 crisis do not create unintended consequences for the future shape of policy and regulation and ultimately the UK's competitiveness.

Unlocking capital

Capital is held by financial institutions for good reason: to protect consumers and their savings and the overall safety and soundness of regulated firms. The principle that regulation should help firms safeguard people's savings and financial stability must not be weakened.

There are multiple reasons why private sector capital may be 'locked' and therefore not deployed in support of businesses and infrastructure investment across the UK. While not all of these relate to regulation (for example, investment mandates, liquidity requirements, tax and state-aid policy), there are some examples which we believe provide a useful starting point for a recommended consultative approach to identifying proposals to unlock capital.

In the UK, accessing funding through capital markets largely remains the preserve of larger corporates. However, the experience of regulatory responses to Covid-19 and the additional regulatory flexibility the UK has following the end of the transition period means there may be merit in exploring what regulatory burdens could be removed to facilitate the issuance of capital by small- and medium-sized businesses (SMEs) and measures that could encourage and foster greater appetite for investment in these assets (while safeguarding investors). Several recommendations on how this could be delivered have already been made in 2017 by Rishi Sunak (prior to his appointment as Chancellor) in a paper authored for the Centre for Policy Studies.

Furthermore, the publication of Lord Hill's Listing Review[56] is an opportunity to take forward areas such as ensuring that prospectus documentation is appropriately tailored to the type of transaction being undertaken and better suits the circumstances of capital issuance. The Review also noted that SME research provision should be a priority for the FCA. Improving the quantity and quality of SME research would help to improve visibility and financing opportunities of SME companies.

More broadly, we welcome the commitment from the UK authorities[57] to consider the regulation of the UK's wholesale financial markets, including a review of the Markets in Financial Instruments Directive (MiFID) framework to ensure it is effective and does not create unnecessary burdens for market participants. A proportionate regulatory framework which protects investors and market integrity will encourage activity to be undertaken in the UK and increase competition and liquidity in economically important markets.

There has been much debate on the UK's implementation of the EU's Solvency II regime for insurers. The Association of British Insurers (ABI) and others have called for a range of reforms to better enable insurers' role as long-term investors and address any regulatory barriers to the sector's ability to invest in socially useful assets such as infrastructure

56 HM Treasury, 'UK Listing Review', (March 2021), available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/966133/UK_Listing_Review_3_March.pdf

57 The FCA, 'A forward look at regulation of the UK's wholesale financial markets', (March 2020), available at: https://www.fca.org.uk/news/speeches/forward-look-regulation-uks-wholesale-financial-markets

projects. This was recognised in HM Treasury's call for evidence 'Review of Solvency II', published in October 2020. Going beyond infrastructure, this review will provide an opportunity to consider an enhanced role for insurers to invest in a whole range of real economy assets to support economic recovery (e.g. business debt/equity) that would not traditionally feature on an insurer's balance sheet due to existing regulatory constraints. In a similar vein the HM Treasury call for input on the UK Funds regime has the potential to help with the efficient allocation of this capital once it is unlocked.

In a report[58] published by the ScaleUp Institute, Innovate Finance and Deloitte, it was recommended that government and regulators accelerate the implementation of the Patient Capital recommendations including the enacting of regulatory changes needed in relation to Defined Contribution pensions.

The UK has a strong private equity and venture capital industry which invests across the UK, for example, the north west of England attracted nearly 10% of all private equity and venture capital investment in the UK in 2019.[59] The British Private Equity and Venture Capital Association (BVCA) reported that investment activity picked up in Q3 and Q4 2020 with around £37.4bn of aggregate deal value[60] and it is important that these sources of capital are considered as a key element of the broader ecosystem of funding throughout the stages of company development.

These examples of policy choices and considerations in relation to unlocking capital for growth across the UK economy illustrate the importance of a coordinated approach to industry consultation and regulatory reform as we recommend later in this section.

The impacts of economic cycles

In 2013, the Bank of England established a Procyclicality Working Group to examine the question of whether, and if so why, insurance companies and pension funds invest procyclically. In a discussion paper[61] the group defined procyclicality in the short- and medium-term as:

- **Short-term:** the tendency to invest in a way that exacerbates market movements and contributes to asset price volatility, which can in turn contribute to asset price feedback loops. Asset price volatility has the potential to affect participants across financial markets, as well as to have longer-term macroeconomic effects.
- **Medium-term:** a tendency to invest in line with asset price and economic cycles, so that willingness to bear risk diminishes in periods of stress and increases in upturns.

More broadly it has been shown that financial institutions' balance sheets expand and contract with the economic cycle,[62] as does their risk appetite. In part this is due to risk management tools used to measure and value risk being naturally procyclical, particularly when using short and uncertain data series, for example, data on the economic impact of Covid-19.

March 2020 saw extreme levels of market volatility and illiquidity even in the most liquid of markets. It is right that regulators in the UK, and at the global level through

58 ScaleUp Institute, Innovate Finance and Deloitte, 'The Future of Growth Capital', (August 2020), available at: https://growthcapital.report/

59 BVCA, 'New Horizons', (February 2021), available at: https://www.bvca.co.uk/Portals/0/Documents/Research/2021%20Reports/BVCA-New-Horizons-24-February-2021.pdf

60 Ibid

61 Bank of England and the Procyclicality Working Group, 'Procyclicality and structural trends in investment allocation by insurance companies and pension funds', (July 2014), available at: https://www.bankofengland.co.uk/-/media/boe/files/paper/2014/procyclicality-and-structural-trends-in-investment

62 Federal Reserve Bank of New York Staff Reports, no. 328, (December 2010), available at: https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr328.pdf

the Financial Stability Board (FSB), look at the causes and implications of this episode, including from a regulatory perspective.

We welcome the statement from the Bank of England in its August 2020 Financial Stability Report that an assessment of 'the extent to which risk controls and regulations contributed to constraining dealer capacity in March'[63] may be warranted. Equally, it will be important to understand the role that leveraged market participants played in the market turmoil in March 2020. However, as Nausicaa Delfas, Executive Director for International at the FCA, has said, any future regulatory initiatives in this area "must recognise that the non-bank sector will be critical in enabling recapitalisation to promote growth and recovery from the pandemic. So, the benefits of a vibrant market should be considered alongside the potential risks".[64]

The Chancellor set out the remit and recommendations for the Financial Policy Committee (FPC) in March 2021.[65] It noted that the publication of the FPC's detailed assessment of the adequacy of the risk oversight and mitigation systems for non-banks is expected to be published in the first half of 2021.

RECOMMENDATIONS

Prioritisation of the regulatory pipeline to focus on pro-recovery and investment measures

The Financial Services Regulatory Initiatives Forum should use the Regulatory Initiatives Grid to demonstrate explicitly that they have considered whether, and how, any regulatory interventions they are proposing may contribute to the UK's economic recovery.

This approach is grounded in the reality that the regulatory agenda should include a focus on enabling the industry to maximise its contribution to economic growth across the UK.

A rigorous approach to pro-recovery prioritisation would result in regulators being clear on whether initiatives should be reintroduced and if so, whether they should be revised to remain relevant given the economic landscape.

Consult on proposals to unlock capital through regulatory reform

The UK regulators should consult with industry to identify and take forward proposals to unlock capital through regulatory consultations coordinated through the Financial Services Regulatory Initiatives Forum.

This would enable any possible regulatory changes recommended by, for example, the Listing Review, the MiFID review and the Productive Finance Working Group convened by the Bank of England, HM Treasury and the FCA to be considered in one single setting, importantly allowing for consideration of the broader regulatory pipeline.

This activity should include engagement with HM Treasury and HM Revenue & Customs to consider whether the cumulative effect of both regulatory and tax policy changes – even if for a temporary period – can maximise the scope for lenders and investors to deploy capital.

63 Bank of England, `Financial Stability Report', (August 2020), available at: https://www.bankofengland.co.uk/-/media/boe/files/financial-stability-report/2020/august-2020.pdf

64 The FCA, `Building a financial regulatory system suitable for the UK in the new era', (July 2020), available at: https://www.fca.org.uk/news/speeches/building-financial-regulatory-system-suitable-uk-new-era

65 HM Treasury, 'Remit and recommendations for the Financial Policy Committee', (March 2021), available at: https://www.bankofengland.co.uk/-/media/boe/files/letter/2021/march/fpc-remit-and-recommendations-letter-2021

This approach should be complemented by a focus on proportionality of regulation, which is important in the context of how the industry can support businesses and consumers across the UK. For example, in banking it is important that specialists and mid-tier institutions can play their part in supporting customers with innovative and competitively priced products.

The UK's approach to proportionality could include factors such as entity size, or firms not being systemically important or internationally active. These issues were discussed by Sam Woods, Deputy Governor for Prudential Regulation and Chief Executive Officer of the Prudential Regulation Authority[66] who noted that early Bank of England research indicates the most sophisticated capital and liquidity requirements may not be as important, relative to sound governance, for small firms as they are for large ones.

Interventions to mitigate impacts of economic cycles

Central banks and regulators should continue to enhance their focus on procyclicality, for example, on risk weighting and capital buffers, including the potential for extensions to the temporary changes to the buffer framework (notably the UK countercyclical capital buffer and systemic risk buffer rates). Banks have consistently been encouraged to use their buffers, including through the Bank of England's Financial Stability Report (FSR) in both August and December 2020.

However, there is a general consensus that they have been reluctant to do so, in part because they have not yet needed to and in part because there is the potential for unintended consequences if a bank does so. For example, the reaction of the market (as noted in the August 2020 FSR) and potential impact on the bank's balance sheet and thereby its approach to risk and lending into the real economy. It is also worth noting that many banks are planning on the basis that they will need to raise additional capital to meet additional requirements as part of the finalisation of Basel III.

66 Bank of England, 'Strong and Simple', (November 2020), available at: https://www.bankofengland.co.uk/-/media/boe/files/speech/2020/strong-and-simple-speech-by-sam-woods

International trade and investment

ANALYSIS

Open trade and globalisation have brought benefits for UK businesses and consumers. Consumers have benefited from widely sourced, better quality products and services, with cheaper prices and more choice. UK businesses have been able to expand into foreign markets and specialise in their areas of strength in a global market. The UK's international connectivity, both outward and inward, has been critical to that expansion and the UK's ability to attract foreign direct investment.

Factors such as transport links with other cities internationally and ease of access to markets, clients and customers are important to corporate decision makers in determining company location decisions. The pandemic has had a catastrophic impact on international travel and opening up business travel needs to be a key priority for the government. Travel corridors with key markets such as the US will greatly assist the flow of global trade and investment. For example, according to York Aviation, business travel between the UK and US makes up 20% of air journeys and is a catalyst for the US's position as the largest foreign investor in the UK. The early introduction of the new Global Mobility Business Visa and improvements to the Global Talent Visa will significantly boost the ability of business to expand and further develop growth areas of the economy. The UK, with its longstanding strengths in financial and related professional services, has taken advantage of the open trading system which allows capital to flow freely across borders to become a global resource of funds and expertise.[67]

The UK's position as a leading international financial centre brings huge benefits. UK businesses stand to gain access to funds with which they can extend their reach worldwide. UK savers and pensioners have gained from access to a wider range of high-yielding investment opportunities.

The UK has also benefited from overseas investment and remains a key destination for financial services investment as we noted in the economic analysis earlier in this report. If the rules-based trading system which underpins globalisation stays strong, the industry will be better able to continue supporting UK growth. But if it starts to decline, both inward investment and domestic growth will be at risk.

The world pre-Covid-19: a return to protectionism

Well before the onset of Covid-19, the outlook for open and global trade deteriorated by signs of a return to protectionism, prompted by growing trade imbalances. Following a US-China trade war and other tensions, global trade declined by 3% in 2019.[68] Protectionist measures soared amid a return of nationalist agendas.[69]

Although most attention has focused on tariffs at the border, in today's increasingly services driven economy, protectionist measures are often 'behind-the-border' regulatory measures, driven by domestic pressures and prove harder to shift.

Digital trade – the ability of digitally-enabled businesses to trade cross-border without restrictions on data-movement – has been hit particularly badly: measures restricting data

67 Some illustrations of the UK's global strength in financial and related professional services, taken from Key Facts about the UK as an IFC (TheCityUK, 2019), are available at https://www.thecityuk.com/research/key-facts-about-the-uk-as-an-international-financial-centre-2019/ , pp4-5.

68 WTO, 'Highlights of world trade in 2019', (2020), available at: https://www.wto.org/english/res_e/statis_e/wts2020_e/wts2020chapter02_e.pdf p10

69 Between 2009-2012, an average of 279 discriminatory commercial policy measures affecting international trade had been taken by governments each year. From 2013-2016, this figure rose to 545 a year, and, between 2017-2019, to 908. See Going It Alone? Trade policy after Three Years of Populism (Global Trade Alert, December 2019) available at: https://www.globaltradealert.org/reports/48

flows have doubled over the last ten years.[70] This matters because about half of cross-border trade in services is now enabled by digital connectivity.[71]

Many governments have started imposing data localisation measures, forcing data to be stored on servers within a country's borders. Localisation measures make it harder for UK businesses to service clients and customers, weaken cyber security efforts and mean businesses face conflicting regulatory requirements. They also make it harder to share ideas, knowledge and experiences across borders, curbing opportunities for growth, discovery and innovation.

Even pre-Covid-19, these rising trade tensions had provoked disruptions in the governing institutions of the rules-based trading system, particularly in the World Trade Organization (WTO) and its Dispute Settlement mechanism. Tensions between trade blocs have produced disagreement on how these should function, so that it is now increasingly hard to enforce international trade law.

Covid-19 and globalisation

Covid-19 hit the global trading system at a vulnerable moment and exacerbated its tensions. The slow decline in trade risks becoming a rout: WTO economists report that world trade in commercial services fell by 24% year-on-year in the third quarter of 2020, following a record 30% drop in the second quarter of 2020.[72]

Nor is it just a matter of a fall in trade: the pattern of trade may be changing too. Covid-19 may have accelerated another existing trend that saw businesses in some markets, including the US, looking to shorten their supply chains and diversify their sources of supply to reduce exposure to future risk.

A crisis on this scale impacts all countries and calls for a joined-up international economic response. There is a good precedent for this. In 2008-2010, global leaders, led by the US, UK, EU and China, together developed a coordinated response to the global financial crisis by agreeing common crisis response measures through forums such as the G20.

But recent geopolitical strains make a repeat performance unlikely. Instead, many countries have responded to Covid-19 with a range of trade-restricting measures like export controls. Although they have gathered copious information about these, the WTO, G20 and other international bodies have struggled to facilitate a global response.

The contrast with attitudes after the global financial crisis is stark.[73] So far, Covid-19 seems to have accelerated the previous trends challenging globalisation. Up to now, a fragile consensus supporting open trade has been upheld. But the risk now is that countries could become locked in a vicious cycle of mutual distrust and respond to each other's initiatives accordingly, in a threatening downward spiral of protectionism. Countries now face a choice: either work together for a coordinated global economic recovery with all its potential gains, or pursue more nationalist paths.

70 VOX, Centre for Economic Policy Research (CEPR) Policy Portal, `The cost of data protectionism', (October 2018), available at: https://voxeu.org/article/cost-data-protectionism and ; World Economic Forum, `Exploring International Data Flow Governance', (December 2019), available at: https://www.weforum.org/whitepapers/exploring-international-data-flow-governance

71 World Economic Forum, `Data Free Flow with Trust (DFFT): Paths towards Free and Trusted Data Flows' (May 2020), p8 available at: http://www3.weforum.org/docs/WEF_Paths_Towards_Free_and_Trusted_Data%20_Flows_2020.pdf

72 World Trade Organization, `World Trade and GDP', (January 2021), available at: https://www.wto.org/english/res_e/statis_e/daily_update_e/serv_latest.pdf

73 An example of the sceptical attitude towards trade among some countries amidst Covid-19is that while the pandemic clearly revealed the importance of digital trade in areas like remote working, some WTO members pushed in March 2020 to review the WTO's long-standing Moratorium on Customs Duties on Electronic Transmissions, which keeps international data transmissions tax free.

RECOMMENDATIONS

Encourage countries to coordinate Covid-19 economic policy measures

The UK should work with other countries to coordinate the status of Covid-19 economic policy measures. This is true especially for two key areas:

- Cooperation on trade related aspects of Covid-19 recovery plans. Before the crisis, conflicts like the US-China trade war and US and EU trade tensions were sparked by debates about illegitimate forms of business support. These tensions could increase given Covid-19 related rescue measures. Governments have rightly had to be creative in stimulating their economies, but it will be important to encourage coordinated discussions on recovery strategies at bodies like the WTO, G20, International Monetary Fund, World Bank and Bank for International Settlements.
- Coordinate strategies around Covid-19 related investment protection laws. When the crisis hit, many countries took action to protect local businesses from being bought cheaply by foreign investors. Some temporarily changed their rules for reviewing foreign investment so that governments could monitor a far wider range of such investments; others made permanent changes to their investment screening mechanisms. The UK fast-tracked reforms of its own investment screening process in the proposed National Security and Investment Bill. Such investment screening measures can have protectionist effects. Here too, the UK should encourage international debate, and carefully consider the implications of enhanced UK investment review measures for foreign investment into the UK, including the impact on competitiveness and on the country's status as an international financial centre.

Government should put digital trade in services at the heart of ambitious FTAs

The WTO agreements set out essential ground rules. But regional and bilateral FTAs can provide deeper (WTO plus) trade advantages. For services (where WTO rules have limited reach) FTAs need to be developed and future-proofed to capture advanced benefits, particularly for high value-added services relying on global connectivity.

Before the pandemic, measures restricting data flows had doubled, even though digitalisation has expanded trade in services to a point where roughly half of cross-border trade in services depends on digital connectivity. Covid-19 and remote working has only served to reinforce this. Securing the right rules for digital trade is a key UK business priority.

The UK should aim to put digital trade facilitation at the heart of new FTAs. Many trading partners are already doing the same: the US, Mexico and Canada Agreement (USMCA) has an ambitious digital trade chapter, and the New Zealand, Chile and Singapore Digital Economy Partnership Agreement (DEPA) includes an innovative format for pursuing agreement on digital issues. The UK should work with like-minded trade partners to create a gold standard of digital trade chapters that cater for technology-enhanced services businesses, limit data localisation, and help position the UK globally as a critical digital trade hub. The UK-Japan Comprehensive Economic Partnership Agreement, signed in October 2020, marked an important first step in this process. The UK should also continue to take a leading role in WTO discussions to create a multilateral digital framework.

Prioritise building coalitions of supporters of open trade

The UK should take a leadership role in building coalitions of countries favouring open trade to support the global trading system, both in multilateral forums of many countries, such as the WTO, and through discussions on trade and regulatory cooperation with smaller groups of like-minded countries. Coalitions for open trade will need to develop positions and ideas that appeal not only to developed markets but also to emerging economies: both will have to be involved for a new consensus around open trade to emerge, and for the full strength of the WTO to be restored.

This is no easy task. A huge and diversified effort will be needed to forge viable coalitions for open trade, focusing both on diplomacy in international organisations and on persuading policymakers in national capitals. The UK has the means to advance this ambition through its impressive diplomatic network and other forms of soft power, including through its universities and professions. Industry representative bodies such as TheCityUK will work with counterpart bodies across the globe and assist them to advocate for open trade to be prioritised by their respective governments. Backed by a joined-up UK government approach, all these means should be exploited.

Closer coordination between industry and government to promote greater liberalisation of trade

While only governments have standing at international bodies like the WTO and in trade negotiations, the financial and related professional services industry can help the UK deliver on international economic policy initiatives. By working with industry and trade partners to advance international standard setting, the government should help reinvigorate global trade and maintain a global environment which supports foreign investment.

This may not be an easy task, but the size of the prize justifies making great efforts to attain it. HSBC and Boston Consulting Group research suggests that if G20 countries return to policies supporting market openness, global GDP could be $10trn higher by 2025 than under a status quo scenario.[74]

International business alliances already work together to make the case for open trade worldwide. As a member of the Global Services Coalition (GSC), TheCityUK works with other GSC members in Asia, the EU, North America and the Pacific Rim to push their respective governments towards deeper services liberalisation, including on digital trade related issues. Meanwhile, TheCityUK has developed strong links to the financial and related professional services industries of UK trading partners and can draw on these to build private sector coalitions for greater global and regional market integration and regulatory cooperation.

74 Boston Consulting Group, `The $10 Trillion Case for Open Trade', (September 2020) available at: https://www.bcg.com/ publications/2020/ten-trillion-dollar-case-for-open-trade

Related professional services

ANALYSIS

It can sometimes be overlooked that a major factor in the development of the UK's comparative advantage in financial services is the presence of a world-leading related professional services industry, including the legal services, accounting services and management consultancy sectors. UK-based related professional services businesses are some of the most prominent British businesses across the globe, contributing to UK soft power as well as economic and commercial success.

As highlighted in our `Key facts about UK financial and related professional services 2021' report, UK-based related professional services businesses have over 1.2 million people in employment divided among management consultancy (510,000), accountancy (404,000) and legal services (350,000). These three sectors contributed £14.9bn, £24.4bn and £29.1bn respectively to UK output in 2020.[75] The UK has the largest and most developed market in Europe for related professional services. This is heavily weighted towards SMEs, which make up 99.5% of legal firms and 99.7% of accounting firms in the UK. More than three quarters of legal firms and 81% of accounting firms are made up of fewer than four employees.

The role of related professional services in the UK's economy and economic recovery

Related professional services businesses have an enabling effect which underpins business growth and stability across the economy. The accountancy profession serves investors and facilitates the smooth operation of capital markets overall, as well as a significant number of parent and subsidiary undertakings and branches, joint ventures, mergers and acquisitions and listings across borders. In addition, it plays a key role in advising and facilitating the growth of SMEs, and guiding businesses to be more sustainable during the recovery and beyond. Insolvency practitioners, and the related area of restructuring law and practice, play key roles in periods of high economic growth but can assume even greater importance in periods of economic dislocation, as has been faced over the past year.

The UK-based legal sector also performs a crucial enabling role which provides a stable framework for all other sectors to flourish and for the UK to remain a world-leading international financial centre. The global primacy of English law as the law of choice for international business is core to this, alongside the UK's world class judicial and alternative dispute resolution mechanisms.

The swift, predictable and fair resolution of commercial disputes gives confidence to commercial parties from across the globe and the UK's strong and independent judiciary and reputation as a centre for legal excellence continues to draw business to the UK. Of the world's 320 jurisdictions, more than one quarter use a form of English common law, which continues to lead the way as the most widely used governing law for cross border contracts.

During the pandemic, the UK's related professional services businesses have played leading roles in the response for businesses and governments alike, helping them to negotiate the crisis, providing advice on issues as diverse as the management of supply chains, the construction of temporary hospitals, and the restructure of businesses. Management consultancy firms, for example, have been influential in helping both SMEs and larger companies adapt quickly to the needs of remote working as well as the acceleration of

75 TheCityUK, 'Key facts about UK-based financial and related professional services 2021', (March 2021), available at: https://www.thecityuk.com/assets/2021/Reports/4015f6e911/Key-facts-about-UK-based-financial-and-related-professional-services-2021-v2.pdf

the digitisation of business processes brought on by the pandemic. Related professional services firms have been particularly valuable in fulfilling the role of `trusted adviser', assisting clients to understand what financial support is available to them and enabling them to manage their businesses in the most efficient way possible.

This role in helping their clients to navigate the crisis has been undertaken at the same time as having to deal with the challenges which Covid-19 has presented to their own businesses and business models. Related professional services firms acted with agility on matters such as remote and flexible working to enable them to continue to serve their clients and guide them through the crisis.

However, at the smaller end of the market in the legal and accountancy sectors, the environment has been particularly difficult. With court hearings scaled back and the difficulties in continuing to facilitate procedures during lockdowns which would normally have to be conducted face-to-face, such as the execution of wills, some high street solicitors and self-employed junior barristers have struggled to remain afloat. Mandatory lockdowns and the resultant restricted commercial activity and difficulty in conducting audits have also placed smaller accountancy firms under severe strain during the crisis.

In parallel with other sectors, the onset of the pandemic also caused an immediate need for related professional services firms to focus on the wellbeing of their people, including both their employees and their clients. Leading UK-based related professional services firms have invested significantly in developing a culture within their respective firms and this crisis has provided a stern test of their ability to live up to the high standards they have set for themselves.

For example, the treatment and makeup of related professional services firms' workforces have been in the spotlight, with the Black Lives Matter movement serving to further elevate diversity and inclusion as a critical business priority.

As it has been essential in helping UK businesses to negotiate the immediate effects of the pandemic, the related professional services industry will also play a crucial role in facilitating the UK's economic recovery. As a further example, and in addition to the enabling examples outlined above, the industry is also a key source of tax revenue.

Research published by TheCityUK notes that the total tax contribution of the legal and accounting sector to the UK public finances in 2018 was £19.1bn and for every £100 of UK turnover that is made by UK legal and accountancy firms, an amount equivalent to £38.40 is paid in taxes.[76] However, in order to continue to play its successful enabling role during the economic recovery, the related professional services industry needs a competitive legal and regulatory environment in which to operate.

RECOMMENDATIONS

Maintain and build the global competitiveness of the UK-based related professional services industry

While the industry's relative strength and vital role in the ongoing success of the economy is clear, there is no room for complacency. If the UK is to remain a leading global centre for professional services, the government needs to carefully and continuously consider the implications for the competitiveness of the industry as it develops its future trading relationships and policy relating to the UK's business environment. Without such ongoing consideration of these factors, the extent to which the professional services sectors can play their important roles as facilitators and

76 'TheCityUK, 'Total tax contribution for UK legal and accounting activities' (July 2019), available at: https://www.thecityuk.com/assets/2019/Report-PDFs/070ca1ac22/Total-tax-contribution-for-UK-legal-and-accounting-services.pdf

enablers in terms of the UK economy's recovery may be unnecessarily constrained, to the detriment of UK PLC.

Acknowledge and promote the importance of English Law, the rule of law and UK legal services

Maintaining and further developing a strong, competitive and well-regulated legal services sector remains essential for the sustainable growth of the UK economy. As outlined above, the UK-based legal services sector forms an integral part of the financial and related professional services ecosystem that makes up the world's leading global financial centre.

It is also important that government positioning as well as legislative and regulatory changes do not (and are not seen to) undermine the certainty and stability provided by English law, the UK's ongoing commitment to the rule of law or the effectiveness and independence of the UK's courts and judiciary. While the UK is currently a world leader in legal services, the sector operates in a competitive global environment, and its reputation and standing, that has taken centuries to build, must not be taken for granted.

Focus on talent, mobility, and data

Two of the most critical assets for the professional and business services industry are people (talent) and knowledge. Access to the best global talent has been a critical factor in the success of UK professional services. The government must work with industry to address both current and future talent shortages, primarily via our education system but also by enabling our immigration system to address shortages of highly skilled labour where necessary.

In order to trade internationally, related professional services practitioners need to be able to share their knowledge with international clients. The UK's new trading arrangements must ensure that professional services practitioners are able to gain access to their clients' markets to facilitate the provision of services, both cross-border and in person, and that their professional qualifications are recognised in those markets.

Finally, the nature of business in the related professional services sectors makes them particularly dependent on the free flow of data and it is vital for international trade that our arrangements with trading partners limit disruption in data flows to an absolute minimum. The ongoing free flow of data is vital to further develop economies and create opportunities for growth as well as ensuring that related professional services businesses can continue to operate smoothly on a cross-border basis.

Sustainability

ANALYSIS

Sustainability had been rising up the priority agenda for national governments and private sector companies well before the outbreak of Covid-19. But the pandemic has clearly highlighted the importance of preparedness and mitigation strategies even for long-term issues such as climate change. Sustainable finance has now emerged as a far wider industry than its narrow beginnings, which were dominated by green finance transactions. As such, ESG (environmental, social and governance) concerns are now an important part of finance discussions and the relationships between corporates and their financers.

The role of financial and related professional services

The role of the financial and related professional services industry in driving a green and sustainable economic recovery is twofold, as summarised by the government's Green Finance Strategy of 2019:

- 'mainstreaming climate and environmental factors as a financial and strategic imperative ('greening finance')
- mobilising private finance for clean and resilient growth ('financing green')'.[77]

In November 2020, the prime minister set out a '10 point plan' for a 'green industrial revolution'. The plan includes 'advancing offshore wind, driving the growth of low carbon hydrogen, delivering new and advanced nuclear power, accelerating the shift to zero emission vehicles, green public transport, cycling and walking, 'jet zero' and green ships, greener buildings, investing in carbon capture, usage and storage, protecting our natural environment and green finance and innovation.'[78] The government is looking to invest £12bn and mobilise as much as £36bn in private investment in the plan.

The government has also specifically asked the Bank of England (BoE) to 'act with a view to building the resilience of the UK financial system to the risks from climate change and support the government's ambition of a greener industry, using innovation and finance to protect our environment and tackle climate change'.[79] Further action to build on existing climate change activity was announced in March 2021 when the Chancellor wrote[80] to the FCA and Prudential Regulation Committee (PRC), which supervise financial services firms, to set out that they should take into account the government's legally binding commitment to transition to a net zero economy by 2050. The letters set out the government's ambition to deliver a financial system which supports and enables a net zero economy, and mobilises private finance behind sustainable and resilient growth.

Previously, in May 2020, the Committee on Climate Change (an independent government-advisory body) had outlined six key principles that could form the foundation of a resilient recovery. These are:

- use climate investments to support economic recovery and jobs
- lead a shift towards positive, long-term behaviours

77 HM Government, 'Green Finance Strategy: transforming finance for a greener future', July 2019: available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/820284/190716_BEIS_Green_Finance_Strategy_Accessible_Final.pdf

78 HM Government, 'The ten point plan for a green industrial revolution', (18 November 2020), available at: https://www.gov.uk/government/publications/the-ten-point-plan-for-a-green-industrial-revolution

79 HM Treasury, letter from the Chancellor of the Exchequer to the Governor of the Bank of England, 3 March 2021; available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/965778/FPC_Remit_and_Recommendations_Letter_2021.pdf

80 HM Government, `Climate considerations now fully embedded across UK principal financial regulators', (March 2021), available at: https://www.gov.uk/government/news/climate-considerations-now-fully-embedded-across-uk-principal-financial-regulators

- tackle the wider 'resilience deficit' on climate change
- embed fairness as a core principle
- ensure the recovery does not lock-in greenhouse gas emissions or increased risk
- strengthen incentives to reduce emissions when considering tax changes.[81]

The financial and related professional services industry can play an important role in supporting public and private sector efforts to include these principles in post-pandemic recovery efforts. For example, through products like green bonds and green loans, the financial services sector matches 'sources of funding to new capital and operating expenditures that generate measurable progress towards the achievement of a well-recognised environmental goal'.[82] As one of the largest green finance segments, green bonds will inevitably play a key role in an environmentally sustainable post-pandemic economic recovery. The UK intends to issue its first sovereign green bond in 2021. These instruments have become highly successful green finance instruments in recent years, with many sovereign issues being oversubscribed.[83] In this context, the UK's planned issue is positive, although the overall impact will depend on the details of issue size and use of proceeds, which have yet to be published.

Individual financial services sub-sectors may be able to exploit specific growth opportunities in green finance. For example, some asset managers report having seen increased demand for ESG-aligned portfolios in recent years, although hard data remain limited. According to the European SRI Study 2018 published by Eurosif in November 2018 (the latest available), the UK's assets under management in six sustainable and responsible investment (SRI) strategies out of seven experienced positive growth rates between 2015 and 2017. The total growth of the seven strategies (Best-in-class, Thematic fund, Norms-based Screening, ESG Integration, Engagement and Voting, and Exclusions and Impact Investing) was 27% during the two years.[84] Asset managers may in future be able to continue capitalising on growing investor interest in such portfolios. For asset managers managing funds on behalf of High Net Worth Individuals or family offices — which are often, though not always, associated more closely with patient capital — long-term sustainability-focused financial instruments may present an opportunity.

The industry could also play an indirect role by addressing its own sustainability credentials. Financial and related professional services' carbon footprint is relatively low compared to other service sectors, and the room for improvement is therefore relatively small.[85] But as an industry that accounts for over 10% of GDP and employs more than 2.3 million people across the UK, demonstrable action to improve industry sustainability would set a positive example that might spur other industries and sectors to action as well as enhance the reputation of financial and related professional services. In the investment area, there is also a growing expectation from companies that responsible investors 'practice what they preach'.

Climate risk assessment is an area tangential to green finance that could present an additional opportunity for financial and related professional services institutions. Increased disclosure of climate risks will help advance efforts to meet the 2050 net-zero target. Accounting, management consulting and legal services can provide tax consulting and

81 Climate Change Committee, 'Take urgent action on six key principles for a resilient recovery', (6 May 2020), available at: https://www.theccc.org.uk/2020/05/06/take-urgent-action-on-six-key-principles-for-a-resilient-recovery/

82 TheCityUK and Imperial College Business School, `Growing green finance', (September 2017), available at: https://www.thecityuk.com/assets/2017/Reports-PDF/21ef6f5fef/Growing-Green-Finance.pdf

83 TheCityUK and Imperial College Business School, 'Understanding green bonds', (May 2018), available at: https://www.thecityuk.com/assets/2018/Reports-PDF/bf2095d362/Understanding-Green-Bonds.pdf

84 Eurosif, 'European SRI study 2018', (11 April 2018), available at: http://www.eurosif.org/wp-content/uploads/2018/11/European-SRI-2018-Study-LR.pdf

85 The CO2 emissions intensity of financial services in 2019 (latest available data) was nil; for professional and scientific services it was £0.01m tonnes of carbon dioxide per £1m of output (ONS, 'Atmospheric emissions: greenhouse gas emissions intensity by industry', 3 December 2020)

cost-benefit analysis services, and can advise on climate risk disclosure in ways that would encourage companies to reduce their carbon emissions or their holdings of conventional assets and allow them to access the full range of financial products that are now available. These services are likely to become even more important as the government set out a roadmap in December 2020 to promote better climate-related disclosures; the intention is that Taskforce on Climate-related Financial Disclosures (TCFD)-aligned disclosure will be mandatory by 2025. Other regulators are also encouraging the gradual adoption of TCFD-aligned disclosures. For example, the Department of Work and Pensions (DWP) completed its consultation on proposals to require trustees of larger occupational pension schemes and authorised schemes to have robust strategies in place to manage climate risk in January 2021 (although they have not yet indicated when they will publish results of the consultation). For its part, the Bank of England is demonstrating its commitment to climate risk preparedness and disclosure by dedicating its 2021 Climate Biennial Exploratory Scenario (CBES) to climate risk. The Bank plans to launch the CBES in June 2021; it will stress test the largest UK-based financial institutions with respect to financial risks posed by climate change.

Nevertheless, important challenges also remain. Perhaps foremost among these is the lack of commonly-agreed definitions and classification systems, which is a significant barrier to progressing sustainability further within financial markets. The challenge has been well documented for green finance; for example, research by TheCityUK and Imperial College Business School has addressed the ways that lack of standard definitions and benchmarks inhibit scale in green infrastructure investment. Significant work in this area has, of course, been undertaken — some systemic, and some relating to specific sub-sectors within green finance. For example, the EU Taxonomy has provided a strategy to reorient private capital towards more sustainable investments by providing a classification system. The green bond principles created by the International Capital Markets Association are a widely-accepted set of voluntary guidelines pertaining to that particular instrument. Meanwhile, the Partnership for Carbon Accounting Financials (PCAF) is an international initiative that seeks to measure and disclose the greenhouse gas emissions financed by financial institutions in a uniform and transparent way. The current (first) version of the standard includes six asset classes: listed equity and corporate bonds, business loans and unlisted equity, project finance, commercial real estate, mortgages, and motor vehicle loans. This demonstrates that — like all standards and frameworks in this area — PCAF should be considered a useful starting point, but an evolving work in progress.

In recognition of this, the UK government announced in November 2020 that it would develop its own green taxonomy. A green taxonomy is a framework that identifies which activities firms conduct can be defined as environmentally sustainable. The UK's taxonomy will be based on the EU taxonomy, and the metrics will be reviewed by a UK Green Technical Advisory Group to ensure they are suitable for the UK.

In areas that are even more difficult to quantify clearly, such as societal well-being, challenges around taxonomies and metrics will be even greater. Investors often turn to ratings agencies to assess the sustainability credentials of potential portfolio companies — but the methodologies of ratings agencies themselves are non-standardised and therefore highly subjective. This is not a criticism of ratings agencies: credit ratings can be comparable because they seek to answer a standard question consistently, whereas ESG ratings cannot be comparable as long as the questions being answered differ. For further detail, see below.

The 'Big 3' ratings agencies, as well as a host of smaller, specialised ratings agencies, have increasingly focused on ESG in recent years. Below is a summary of the approaches taken by the main credit-rating agencies, as well several specialised firms. The distinction between, on the one hand, incorporating ESG factors into credit ratings and, on the other hand, establishing separate ratings to assess ESG credentials, is important.

Fitch Ratings

In January 2019, Fitch Ratings launched a new scoring system: Environmental, Social, and Governance (ESG) Relevance Scores. The new scoring system takes ESG factors into account when Fitch makes its credit rating decisions. The ESG Relevance Scores are on sector-based and entity-specific bases. Fitch is the first credit rating agency that introduced how ESG factors affect credit ratings. When analysing the ESG impact, individual E, S and G are scored ranging from 5 (most relevant to credit ratings) to 1 (least relevant).

Moody's Investors Service

Moody's published its General Principles for Assessing Environmental, Social and Governance (ESG) Risks in January 2019. The company takes the impact of ESG factors into consideration in its rating analysis for all issuers, including corporates and sovereigns. For corporate credit ratings, Moody's assesses the ESG impact on corporates' product demand, reputation, cost of production and financial strength; the impact is incorporated into assessments about profitability, leverage, cash flow, business profile, financial policy and scale (revenue/assets). For sovereign credit ratings, Moody's considers the ESG impact on countries' economic competitiveness, government effectiveness, rule of law, political risk, control of corruption and revenue/spending needs; Moody's methodology scorecard then assesses the impact with regard to the countries' economic strength, institutional strength, fiscal strength and susceptibility to event risk.

S&P

S&P published its Environmental, Social, and Governance (ESG) Evaluation analytical approach in June 2020. S&P Global Ratings' ESG Evaluation analyses the ESG impact on an entity's stakeholders. An ESG score indicates the ability of an entity that mitigates ESG-related risks and capitalises on ESG-related opportunities. The ESG Evaluation is comprised of ESG Profile and Preparedness. Firstly, S&P establishes an ESG Profile to assess ESG-related risks and opportunities for a given entity. Secondly, S&P assesses an entity's ability to predict and prepare long-term ESG-related plausible disruptions, namely long-term preparedness. The ESG Evaluation is not a part of S&P's conventional credit ratings, but it provides information that can inform S&P's credit analysis.

Specialised agencies

Beyond the 'Big 3', a wide range of institutions specialising in sustainability ratings and analytics has emerged. Examples of some organisations doing prominent work in this area are:

Morgan Stanley Capital International (MSCI) is a global index and analysis tool provider. The company applies artificial intelligence and alternative data to measure companies' ESG ratings, aiming to test companies' resilience to ESG-related risks. In September 2019, MSCI published its ESG Ratings Methodology. The MSCI's ESG ratings method is to assess 37 ESG Key Issues through examining a company's core business and the industry issues. These are contained in three pillars and ten themes:

- Environment
  - Climate Change
  - Natural Resources
  - Pollution & Waste
  - Environmental Opportunities
- Social
  - Human Capital
  - Product Liability
  - Stakeholder Opposition
  - Social Opportunities
- Governance
  - Corporate Governance
  - Corporate Behaviour

After MSCI gives scores to each company, the companies are rated between the best (AAA) and the worst (CCC). The ratings are relative rather than absolute, with a company compared with industry peers.

The Institutional Shareholder Services group of companies (ISS) provides solutions to investors and businesses to support their long-term and sustainable growth. ISS's ESG ratings provide research and data on companies, countries and green bonds to help investors making their investment decisions. The aim of the ratings is to support investors to minimise the ESG risks they face. ISS's ESG ratings provides solutions in six areas:

- ESG Corporate ratings: analysing up to 100 rating criteria to assess a company's ESG issues;
- ESG Country ratings: sustainability issues for all countries in the EU, OECD, BRICS and other regions are assessed;
- Governance QualityScore: a company's governance risk is identified;
- E&S Disclosure QualityScore: a company's environmental and social risk are measured;
- Carbon Risk ratings: a company's climate-related issues are assessed;
- Custom ratings: allowing investors to establish their own view on ESG and manage their own ESG risk.

Sustainalytics, a Netherlands-based rating agency established in 1992 that provides ESG research and ratings to investors globally. The aim of the rating agency is to support investors to establish their responsible investment strategies. Sustainalytics conducts its ESG ratings through the areas of Corporate Governance, material ESG issues (MEIs), and idiosyncratic ESG issues.

Conclusion

The idea of ensuring a more green and sustainable post-Covid economy generally, and sustainability-linked conditionalities specifically, are generally very long-term goals. The CCC's Sixth Carbon Budget provides advice on meeting the net-zero target.[86] The analysis and recommendations are comprehensive and wide-ranging, but many individual businesses are likely to find committing to long-term targets abstract without an actionable, near-term, individually-tailored plan, and relatively few businesses have the internal resource necessary to align such goals with their business plans (although there are of course prominent exceptions to this, particularly among large firms).

To date, fundraising specific to the pandemic has generally been a subset of broader fundraising (for example, a proportion of funds earmarked for Covid-19 relief efforts as part of a larger Social bond issue).[87] The majority of Social bond issuance and almost the entirety of specialised Covid-19 bond issuance has been by sovereign and supranational issuers. But the financial and related professional services industry serves as a bridge in the case of such issues, linking suppliers (issuers) and demanders (investors) of the bonds and providing liquidity for the market. This financial intermediation function will be at the heart of the industry's contribution to a sustainable post-pandemic recovery — not just through Social bonds, but through the entire and still-growing range of green and sustainable products and services. Moreover, the industry's contribution to wider pressing debates around, for example, incentivisation of sustainable investment, sustainable investment metrics, and the reconciliation of long-term and short-term priorities will help advance the sustainable growth agenda more broadly.

It is therefore clear that the financial and related professional services industry has a role to play in securing a sustainable economic recovery for the UK. However, there remain barriers that were present before the pandemic and have become more acute as the economic environment became highly challenging. Below we set out three key recommendations that will help UK financial and related professional services firms contribute to a sustainable economic recovery.

RECOMMENDATIONS

Government, regulators and industry must work in partnership to advance sustainability goals

It is clear that sustainability is an area where the government, regulators and the private sector will have to work in close partnership in order to achieve long-term sustainability goals. Government policy will continue to be critical for setting the long-term framework within which private-sector firms must operate. The Paris Agreement carbon-emissions target represents an agreement between governments, but the attainment of this target will depend on the actions of private-sector firms. Moreover, the UN Climate Action Summit 2019 'confirmed finance as key for the transition to net-zero emissions climate resilient economies [and noted that] Public and private financial flows need to align with the objectives of the Paris Agreement and be accessible to actors on the ground…'.[88] The UK government set out the UK's contribution to this goal with legislation passed in June 2019 committing the UK to bringing net greenhouse gas emissions to net zero by 2050.

86 Climate Change Committee, 'The Sixth Carbon Budget: the UK's path to net zero' (December 2020), available at: https://www.theccc.org.uk/publication/sixth-carbon-budget/

87 A social bond is a fixed-income instrument whose repayment to investors depends on specified social outcomes.

88 United Nations, 'Report of the Secretary General on the 2019 Climate Action Summit and the way forward in 2020', (December 2019), available at: https://www.un.org/en/climatechange/assets/pdf/cas_report_11_dec.pdf

Government should ensure that the right incentive structures are in place

Incentive structures are often insufficient for businesses to promote sustainable investments over non-sustainable ones. Notwithstanding the fact that there are financial and reputational risks involved in not addressing sustainability issues, businesses are often deterred by the higher up-front investment costs associated with sustainable investments, and/or a lack of (real or perceived) higher returns associated with these investments. Government may also wish to consider how the tax system could in future be used to incentivise sustainable finance; in March 2021, for example, the Confederation of British Industry (CBI) published suggestions for using taxation to advance net-zero emissions.[89] Government policies in areas such as governance as well as tax could help incentivise businesses to adopt sustainability-focused practices. Policy and fiscal certainty around the necessary infrastructure investments will also be critical. Finally, reporting obligations combined with penalties for poor performance are likely to lead to more concrete results, in particular if coupled with support to help companies take practical steps to improve their output/performance in this area.

Government and industry should continue to encourage international collaboration, including by leveraging the UK presidency of COP26

International cooperation will be critical to tackle what is fundamentally an international challenge. Such cooperation can help maximise the effectiveness of various national initiatives, and also ensure that best practice and innovative solutions are shared more widely. Ultimately, international cooperation will be promoted both through the actions of individual businesses and through convening organisations like the Green Finance Institute. The government and industry should establish joint working groups to focus on international cooperation and agree consistent methodologies for measuring the effectiveness of national initiatives in addressing climate change. Government should also aim to show global leadership in this area and work closely with international partners, including other international financial centres. Leveraging the UK's Presidency of COP26, now due to be held in November 2021, should be a core component of demonstrating such leadership. For our part, the International Regulatory Strategy Group — a collaboration between TheCityUK and the City of London Corporation focused on helping to shape future regulatory developments in financial services — is currently examining issues around global standards for the Social aspect of ESG. Meanwhile, TheCityUK will publish research later this year which will provide evidence for the UK's role as a centre for green finance.

89 Confederation of British Industry, 'Greening the tax system: how tax policy could support net-zero', (March 2021), available at: https://www.cbi.org.uk/media/6332/2021-03-greening-the-tax-system.pdf

Tax

ANALYSIS

Tax policy is one of the levers government can use to balance their budgets in response to the huge fiscal interventions put in place since March 2020. As of January 2021 global fiscal actions amounted to $14trn[90] and global government debt was estimated to reach 98% of GDP at the end of 2020.

The OBR forecast that the UK's budget deficit in 2020/21 will be around £355 billion - equivalent to 17% of GDP. Around £250 billion of the forecast deficit arises from government steps to support public services (£106 billion), households (£82 billion) and businesses (£62 billion) during the pandemic.[91] The question of how to recoup the costs associated with the Covid-19 pandemic is incredibly challenging. However, the UK-based financial and related professional services industry has a vital role to play in securing economic recovery in a post-Covid and post-Brexit environment.

The financial and related professional services industry's contribution

A strong and dynamic financial and related professional services industry is in the interests of the UK. As well as providing products and services that meet the needs of consumers and businesses, the industry's activities generate substantial tax receipts that fund vital public services. It is therefore vitally important that the tax system is set up to encourage firms to do business in the UK.

The industry's tax contribution is significant, sitting above the headline rate of corporation tax and and in 2019/20 it accounted for 10.1% of total tax receipts and was equivalent to 3.4% of UK GDP.[92] The banking sector alone contributed £39.6bn in tax in 2020, comprised of corporation tax, business rates, employment taxes, irrecoverable VAT, the bank levy and the bank surcharge. The total tax rate for a bank operating in London is 46.5%, 13% points higher than the rate paid by a bank operating in New York.[93] Many of the taxes subject to UK firms are not dependent on profits, meaning that firms pay regardless of how well their business is doing.

Tax paid by firms is only one element of the total contribution of the financial and related professional services industry. The economic activity generated by the industry also raises significant levels of taxes. For example, the industry employs around 1 in 14 UK workers,[94] who contribute additional taxes in the form of Employee National Insurance Contributions (NICS) and income tax deducted under PAYE.

International firms also contribute a substantial share of the total tax paid by the UK-based financial and related professional services industry, demonstrating that UK attractiveness is vitally important in growing the industry's contribution to the public purse. The government must recognise the need to encourage businesses to operate in the UK, as doing so will increase investment and generate increased economic activity, which in turn will result in increased tax revenues.

90 IMF, `Fiscal Monitor Update, (January 2021), available at: https://www.imf.org/en/Publications/FM/Issues/2021/01/20/fiscal-monitor-update-january-2021

91 OBR, `Economic and fiscal outlook', (March 2021), available at: https://obr.uk/efo/economic-and-fiscal-outlook-march-2021/

92 TheCityUK, `Key facts about UK-based financial and related professional services 2021', (March 2021), available at: https://www.thecityuk.com/research/key-facts-about-uk-based-financial-and-related-professional-services-2021/

93 UK Finance, `2020 Total Tax Contribution of the UK banking sector', (January 2021), available at: https://www.ukfinance.org.uk/system/files/2020-UKF-TTC-for-the-UK-banking-sector.pdf

94 TheCityUK, `Key facts about UK-based financial and related professional services 2021', (March 2021), available at: https://www.thecityuk.com/research/key-facts-about-uk-based-financial-and-related-professional-services-2021/

RECOMMENDATIONS

The UK tax system should support long-term, sustainable economic growth to maximise the industry's contribution to economic recovery

The government should learn from the experience of the global financial crisis and be mindful not to attempt to rebuild public finances too quickly by disincentivising investment with new tax measures. Although the impetus and effects of the 2007-2009 financial crisis are quite different from the current pandemic, early estimates suggest the impact on tax revenues will be significant in the short-term and will likely take several years to return to pre-crisis levels.

Given this backdrop, the longer-term impact on tax revenue will depend on the effectiveness of policy responses taken to limit the economic impact of the crisis, and the extent to which these policies are focused on growth.[95]

The government should focus on stimulating long-term, sustainable economic growth, for example, by ensuring incentive structures are stimulating investment in the right way.

In 2015, a European Commission report investigated how tax incentive schemes can support the role of growth capital to drive job creation and economic growth, concluding that 'Venture capital and business angel investment has been shown to generate a number of positive macroeconomic effects such as job creation and productivity gains'. However, industry-level research estimated that external equity funding to fast-growing businesses fell by approximately 40% in Q2 2020 compared to Q2 2019 and predicted an overall drop of £6 billion of funding throughout 2020. In the post-Covid-19 world it has therefore become more important than ever to review tax incentive schemes such as the Enterprise Investment Scheme and rules related to Venture Capital Trusts, to ensure they are stimulating business angel and venture capital investment.

Growth must be factored into the government's policymaking agenda. This will encourage firms to continue operating in the UK, boost overall tax revenue in the long run, and enable the industry to contribute to the replenishment of public sector finances[96], which go towards funding the public services we all rely on.

Tax policy changes should be clear, consistent and developed through consultation to continue to attract businesses to the UK

The quality of a country's tax system encompasses more than the final output of tax policy; it is also important to consider the way in which tax policy is approached, from how it is decided that the policy objectives can be met, to the announcement of change, approaches to consultation and legislative drafting. A stable and consistent approach to tax policy will have a positive impact on inward investment and the overall attractiveness of the UK's business environment.

The government should use this opportunity to develop a long-term, strategic approach to taxation in the UK which aligns to its broader policy objectives, for example, by producing a 'Tax Roadmap' to help businesses plan for upcoming changes. The need for such a roadmap was recognised by the Treasury Select Committee's tax after

95 OECD, 'Tax and fiscal policy in response to the Coronavirus crisis', (2020), available at: https://www.oecd.org/coronavirus/policy-responses/tax-and-fiscal-policy-in-response-to-the-coronavirus-crisis-strengthening-confidence-and-resilience-60f640a8/

96 OECD, 'Fiscal policy in response to the Coronavirus crisis: Strengthening confidence and resilience', (2020), available at: https://www.oecd.org/coronavirus/policy-responses/tax-and-fiscal-policy-in-response-to-the-coronavirus-crisis-strengthening-confidence-and-resilience-60f640a8/

Coronavirus inquiry.[97] In doing so, the government should strongly consider the need for simplification, by rethinking certain taxes rather than applying short-term patches which create further complexity.

The UK's tax code has been widely reported to run at over 17,000 pages. In contrast, Hong Kong's tax code is less than 300 pages, allowing businesses to spend less of their resources interpreting and complying with complex regulation. While simplification itself may not drive additional tax revenues, clarity around the tax system may encourage businesses to operate in the UK, which would have the effect of increasing overall tax revenues.

Taking a consultative approach is vital. Newly designed taxes sometimes introduce unintended consequences that create further complexity. For example, recent changes to indexation relief on capital gains tax in December 2017 directly impacted returns to life insurance savings bond policy holders. The intended targets of this change were individuals as the government sought to bring the corporate tax system in line with personal capital gains tax, but the design of the policy meant that service providers and products were impacted. Estimates by the insurance industry calculated that up to £150 a year of extra tax would be levied on savings products sold by insurers, making their products less attractive.[98]

Consider how the international nature of the UK-based financial and related professional services industry can be maximised for the benefit of the UK's economic recovery

The size of a country's international tax treaty network is a key determinant of the overall competitiveness of its tax regime. The UK scores highly in this regard, and so it is vital that the government continues to prioritise international cooperation to ensure the UK can continue to attract inward investment, lead the fight against tax evasion and minimise complexity arising from market fragmentation.

This is particularly important in a post-Brexit context. The government needs to recognise the international nature of the financial and related professional services industry and seek to avoid unnecessary burden and complexity, for example, in cross-border travel and transfers, particularly given its stated focus on post-Brexit international trade and investment.

97 Treasury Select Committee, `Tax after Coronavirus', (February 2021), available at: https://committees.parliament.uk/publications/4865/documents/50796/default/
98 Financial Times, 'Savers face steep tax rise on insurance products', (2018), available at: https://www.ft.com/content/68faf940-fc45-11e7-a492-2c9be7f3120a.

3. Conclusion

While there is a renewed sense of optimism about the future, the challenges the UK faces to recover from Covid-19 are not to be underestimated. Setting out a clear path to recovery is essential, and at the heart of that is the need to make the most of the opportunities ahead. Among those is a focus on how we can build on the financial and related professional services industry's position as an engine for our country's growth.

Financial and related professional services are a national asset, with more than 2.3 million people in employment right across the country, two thirds of whom are outside London. This industry, already a major contributor to national and local economies, has played an important role in supporting customers through the pandemic so far and stands ready to continue that support and be part of the solution to this crisis.

Across the key areas explored in this report we have set out a range of recommendations and actions that can be taken forward to help drive the UK's economic recovery. We look forward to working with government, regulators and other key stakeholders to progress these, and ultimately make a difference to customers and communities across the UK.

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Financial Services
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