Why 'competitiveness' objectives for regulators risk UK finance success

THE FINANCE INNOVATION LAB

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HMT's Financial Services Future Regulatory Framework Review is a once in a generation opportunity to improve the rules that support the UK's world-leading finance sector. A hot debate is underway about how to uphold the success of the finance sector post-Brexit.

One proposal is to give financial regulators statutory objectives to promote the 'international competitiveness' of the industry. However, a large and growing number of voices – from regulation, academia, civil society, and industry – are raising the alarm that this would harm the long-term success of UK finance, and therefore the positive contribution it can make to economic growth, levelling up, and achieving net zero. Earlier this year, in January 2022, polling found that 91% of the British public are unconvinced by the proposal. This month, in February, 37 charities and public interest groups strongly opposed the proposal in a joint statement to HM Treasury. This briefing outlines three reasons why.

1. It will erode the independence of regulators to act in the public interest.

There are many organisations whose job it is to promote financial services, including industry associations and firms. Requiring regulators to take on this role too risks exacerbating the undue influence of industry lobbyists, when balanced input from a diversity of stakeholders leads to well-designed regulation that serves the public interest. Since regulatory quality is a determining factor in the success of a financial centre, the proposed objective could in fact work against the UK finance sector's international competitiveness.

2. It risks sowing the seeds of a financial crisis, thereby threatening long-term economic growth.

Asking regulators to promote international competitiveness is not a new idea. We know from painful experience that too great a focus on competitiveness risks putting regulators in a dangerous race to the bottom with regulators globally to water-down standards. In 2010, HM Treasury identified that one of the reasons for regulatory failure leading up to the global financial crisis of 2007/08 was "excessive concern for competitiveness". That cataclysmic event saw millions lose their savings, homes, businesses and jobs, and cost the UK an estimated £1.8 trillion in lost GDP.

As Andrew Bailey said in 2019 (then CEO of the FCA, today Governor of the Bank of England), the regulator "was required to consider the UK's competitiveness, and it didn't end well, for anyone."

3. It conflicts with existing regulator objectives to create fair markets by 'promoting effective competition' and 'protecting customers'.

The pursuit of competitiveness is distinct from competition; regulators already have an objective to promote competition between firms in order to drive better outcomes for consumers. International competitiveness typically refers to the ability of UK firms to compete for business overseas, and for the UK to remain an attractive location for globally active financial institutions. When large and international firms have a greater say over regulation, it can in fact damage competition at home. The proposal would also impede the FCA's ability to advance consumer protections where such measures might reduce the competitiveness of firms.

A way forward:

Since March 2021, regulators have been required to 'have regard to' the impact of their decisions on the competitiveness of industry when pursuing their objectives. Asking more than this risks undermining their effectiveness, and the success of the UK's critical finance sector. The government is right to consider how regulators can maximise financial services' contribution to the UK's economic, social, and environmental goals. To achieve this, it should prioritise upgrading tackling climate change, promoting financial inclusion, and driving long-term economic growth in the regulators' mandates.