

UK FINANCIAL AND RELATED PROFESSIONAL SERVICES: MEETING THE CHALLENGES AND DELIVERING OPPORTUNITIES

August 2016



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I. THE UK FRPS INDUSTRY IS A NATIONAL ASSET 12

The FRPS industry is a key driver of the UK economy. The industry is the biggest single generator of tax revenues, contributes 12 percent of economic output and employs nearly 2.2 million people. It plays an essential role in helping companies raise finance, supports global business, and provides a range of investment opportunities for institutions and individuals.

II. OUR SUCCESS AND PROSPERITY ARE AT RISK 15

The highly-skilled FRPS industry is globally mobile and intensely competitive and the UK must work hard to maintain its leading position, particularly in light of the uncertainty and opportunity caused by the recent vote to leave the European Union. The industry continues to be transformed by automation and technology, and this is likely to lead to reduced employment levels in some areas if the UK does not seize new growth opportunities.

III. WE NEED TO ACT NOW 19

To maintain our leading role, we must be prepared to adapt and innovate, drawing on the FRPS industry's historic strength and resilience to support existing relationships and create new opportunities. We discuss five priority actions for policy makers and stakeholders: connect globally; drive national growth; expand our services; innovate, disrupt and scale; and foster skills and talent.

IV. CONCLUSION: OUR VISION FOR FRPS IN THE UK 51

The actions we take now, alongside our commitment to the UK's stable business and regulatory environment, deep and diverse client networks, and inclusive culture, should help us continue to lead the world in FRPS in the years ahead.

FOREWORD

John McFarlane, Chairman, TheCityUK

The UK has firmly established its reputation as the leading international financial centre. Only the US matches the scale and diversity of the UK based financial and related professional services (FRPS) industry, but that is based on a larger domestic economy. Yet despite the UK's clear competitive advantages, we cannot afford to be complacent or we will lose out to other financial centres that are vying to win the race to attract more business. Decisive action is required to sustain the industry's competitive advantages.

The FRPS industry is becoming increasingly global, competitive and technology fuelled. Emerging markets are strengthening, jobs are under threat from automation and off-shoring, and many businesses have been challenged since the financial crisis. The US is capitalising on a leading position in fast growing areas such as investment management and cyber insurance, and regional centres in Asia are benefiting from local rapid GDP growth. The capabilities that will drive tomorrow's growth and success will be very different from those of today. Staying the same simply will not cut it.

Getting the response right to meet these challenges is essential. We need to act now not only to maintain the global strength of our industry, but also to ensure the UK's continued attractiveness. How we respond to a future outside of the European Union following the recent referendum will also have significant bearing on the UK's economic growth and prosperity.

Our changing relationship with the EU is critical, and the new terms of trade will be of fundamental importance – to our industry and to the long-term attractiveness of the UK. This report is not a look at the detailed implications of different Brexit scenarios; these are covered in our other work. Instead, it focuses on the structural industry challenges that remain relevant despite the Brexit decision. What the referendum outcome has done is magnify the impact and urgency of addressing these challenges and delivering new opportunities that relate to them.

Unlike in the wake of the 2008 financial crisis, our industry has acquitted itself well in ensuring that the financial system works following the decision to leave the EU. We have played a positive role and wish to continue to do so. We must now speak confidently and with one voice to policymakers to help inform them about the deal we want to see from the upcoming negotiations. It is vital that the needs of FRPS are prioritised. Our industry is a national asset – one that employs nearly 2.2 million people across the UK; pays more tax than any other sector (£66bn in 2014); generates a significant trade surplus (£72bn in 2014) that helps to offset the trade deficit; and touches our everyday lives in many ways, helping us save for the future, protect ourselves against risk, and provide the finance and services for the businesses we all rely on. A robust and globally competitive FRPS industry helps to build a strong and thriving economy.

Our vision is to secure future prosperity, retain and strengthen the UK's position as the leading international financial centre, and be globally recognised as the home for worldwide expertise and innovation.

This report focuses on how we can drive innovation and be more resilient and better skilled to succeed. The UK's attractiveness is built on some long-standing bases of competitive advantage, time zone, rule of law, being open to investment and a society where hard-working and talented people can succeed. Given the impact of the vote to leave the EU, now is the time to act in concert with policymakers and regulators to bring forward policies that support and drive growth in the UK's most important and globally competitive sector. These focus on an attractive tax environment for companies and people, a regulatory environment that promotes innovation and investment, labour laws that promote flexible modern working practices and greater investment in digital as well as transport infrastructure. In short, it means making the UK the best place in which and from which to do business.

I must extend my personal thanks to the team at McKinsey & Company for contributing their research and analysis to this work, the Steering Group of members for overseeing its development, the Board and Advisory Council for its guidance, members for participating and TheCityUK team for producing such an important report. The views from the interviewees that contributed to this report were gathered before the EU referendum, but some of them include perspectives about the Brexit scenario.

We know there are very strong, unique foundations from which to build, but ensuring we secure the best possible deal for our industry and the UK in the upcoming negotiations with the EU and delivering the core areas for growth outlined in this report will absolutely require energy and partnership. Ultimately, we want to be in the position to better serve clients and customers in the UK, across Europe and around the world and continue to rebuild trust in the industry. This is a prize that we believe is worth fighting for and which will deliver stability and confidence in our future.

EXECUTIVE SUMMARY

FRPS serves the nation's needs

The UK is the leading centre for financial and related professional services (FRPS), exporting more financial services than any other country and hosting the highest number of FRPS headquarters. The country leads across a diverse range of businesses, from international arbitration to fixed income trading and specialty commercial insurance.

London is also a leading global FRPS cluster due to its network of interconnected businesses, suppliers, and associates. This “cluster effect” – which encompasses the full range of FRPS – provides the UK's FRPS businesses with better efficiencies, productivity, access to talent, and more rapid innovation than other international locations.

Consequently, the UK FRPS industry is a core driver of the economy, responsible for 12 percent of economic output and employing nearly 2.2 million people.¹ Our reach extends far beyond the City of London, with two-thirds of employment outside the capital. Professional services employment outstrips financial services employment.² The industry is also an enabler for the rest of the economy, providing financing for businesses and a wide range of products and services to individuals.

Sustaining and growing the FRPS industry is critical for the future of the UK economy.

However, growth is not guaranteed and action is required to secure new opportunities

Jobs (particularly outside London) are under threat from automation and off-shoring. Profitability is down, with many businesses seeing large declines in return on equity since the 2008 financial crisis. At the same time, the competitive environment is hardening. Some Asian regional centres are benefiting from rapid local GDP growth, and the US is capitalising on a leading position in fast-growing sectors such as investment management and cyber insurance. The capabilities required to power tomorrow's success in a more global, competitive and technology-fuelled FRPS industry are changing.

The vote to leave the EU in the recent referendum amplifies the challenges we face and creates additional ones, including the potential loss of the current level of access to the EU single market. It also creates opportunities that must be made a reality.

We should focus on five priorities

Securing the industry's pre-eminent position is not only important for FRPS. It is because of UK leadership in FRPS that global companies invest in our country. The depth of talent in banking, insurance, asset management, law, consulting and accounting creates jobs through the value chain.

To overcome the outlined challenges, sustain our competitive advantage as the leading global FRPS cluster and continue to lead in global FRPS expertise and innovation, we should focus on five priorities (Exhibit 1):

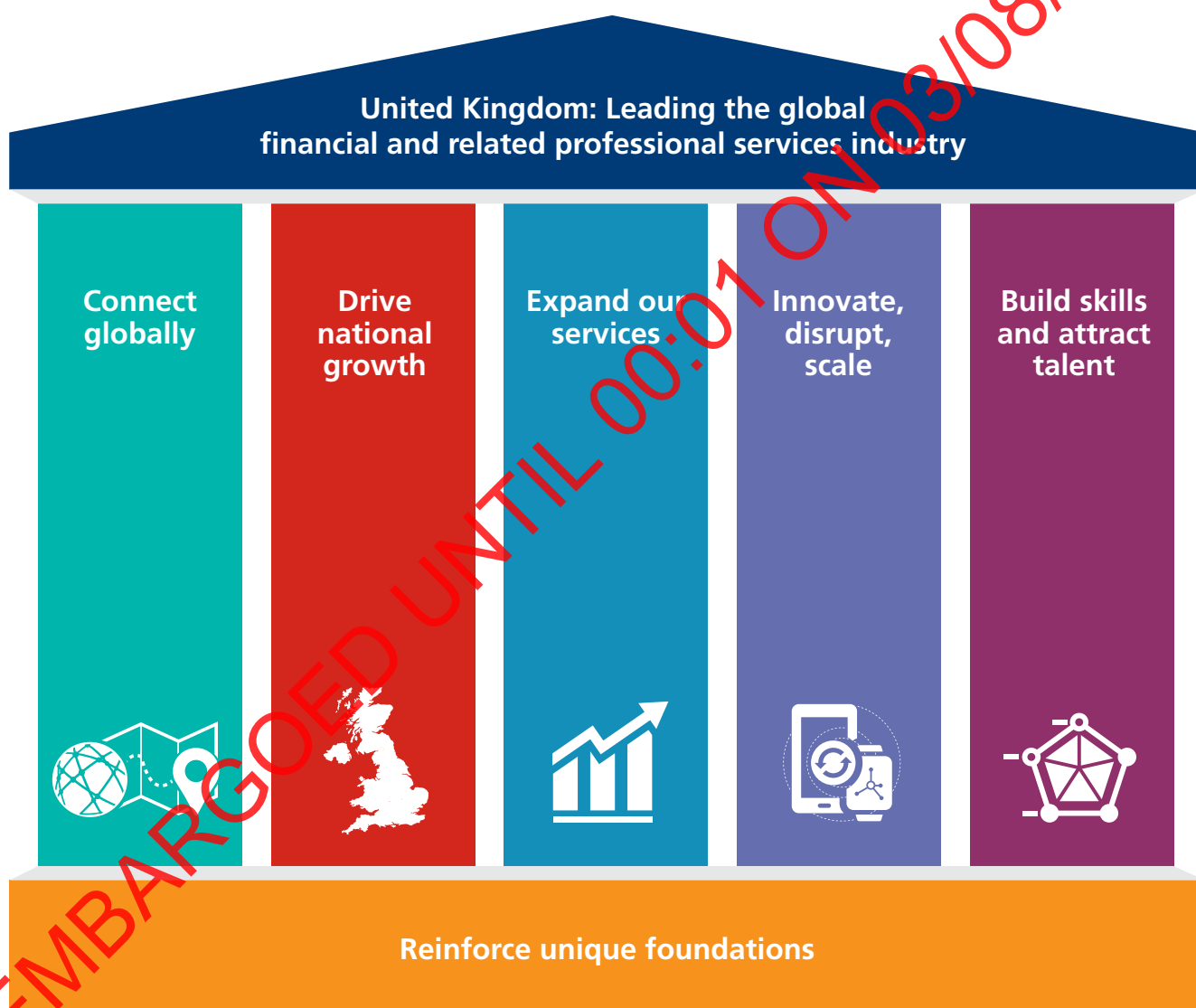
- **Connect globally**
- **Drive national growth**
- **Expand our services**
- **Innovate, disrupt, scale**
- **Build skills and attract talent**

¹ Office for National Statistics (ONS), as quoted in TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

² ONS Balance of Payments Yearbook, as quoted in TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

EXHIBIT 1

Five areas for partnership to secure future growth for UK FRPS





1. CONNECT GLOBALLY

The UK is a global FRPS centre, and international trade and investment drive the UK's profile and performance. However, global markets offer untapped opportunities. To realise these in a post-Brexit scenario, we should:

- **Maintain an effective UK/ EU relationship and sustain access to the single market for FRPS.** European companies look to London to raise capital and for complex professional advice, and it is in the interests of Europe and the UK to maintain market access. To do that, three principles should guide our initial response to the Brexit vote: i) map an effective relationship with the EU that maintains mutual market access, ii) prize clarity and stability, essential to markets, investors, customers and employees, and iii) defend the UK's pre-eminent position in FRPS.
- **Enhance FRPS trade and investment with developed markets including the US and Japan.** To strengthen the relationship with the US, there should be efforts to grow FRPS exports and inward investment, and coordinate bilateral policy and regulatory coherence across FRPS and business more broadly. Similarly, Japan is a leading trade and investment destination which we should regard as a partner for more cooperation and investment.
- **Continue growing links with emerging markets.** The UK's expertise (e.g. in capital markets and Islamic finance), relationships (through exporting qualifications and standards) and regulatory frameworks (through appropriate mutual recognition of services and products) should be promoted in emerging markets. The UK should seek to boost cooperation and mentoring, helping emerging markets develop as financial centres linked to our country.

56%

OF UK PROFESSIONAL
SERVICES EXPORTS
GO TO EUROPE



THE US ACCOUNTS

FOR
49%

OF UK FINANCIAL
SERVICES FDI STOCK

AND 19%

OF UK PROFESSIONAL
SERVICES FDI STOCK



LONDON
ACCOUNTS

FOR
AROUND
TWO-
THIRDS

OF ALL RENMINBI
PAYMENTS OUTSIDE
OF MAINLAND CHINA
AND HONG KONG



2. DRIVE NATIONAL GROWTH

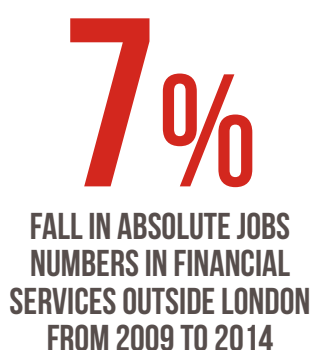
More than two-thirds of FRPS jobs are outside London. However, increased automation is leading to declines in financial services employment in some regions and uncertainty surrounding the terms of Brexit could amplify that trend. Attracting and retaining the next wave of off-shoring activities will be critical to supporting jobs in the UK.

We should be more aggressive about building the skills that FRPS firms are looking for, and create strong, connected regional centres with clear specialist capabilities and expertise:

- **Reinforce the value proposition of UK regional clusters.**

Educational institutions such as universities and colleges, as well as Local Enterprise Partnerships and firms, must co-operate at scale to identify and act on the next wave of opportunities to grow regional employment. A clearer UK-wide proposition for FRPS firms should be a priority, as should identifying regional expertise, particularly in relation to technology.

- **Accelerate efforts to build a local capabilities pipeline to support UK regional clusters, growth and jobs outside London.** Regional centres need local capabilities to support innovation, growth and job creation. Collaboration with colleges and universities should be scaled up to develop local talent pipelines for specialist skills.





3. EXPAND OUR SERVICES

The FRPS profit pool is changing. Fixed income, currencies and commodities (FICC) business, for example, has seen a rapid decline in employment and profitability, whilst cyber insurance and infrastructure financing are growing at double digit rates. The prospect of Brexit might impact some businesses (e.g. euro clearing) and strengthen others (e.g. legal services). We must position ourselves as the natural home for growth businesses and aim to:

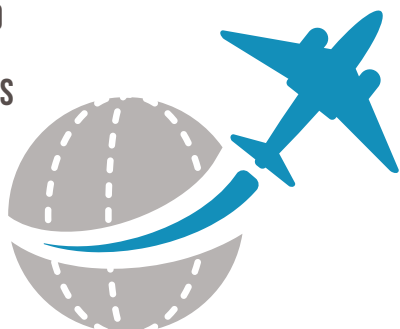
- **Strengthen UK capital markets and market infrastructure.** Targeted improvements would enable the UK to capture economic growth as activity shifts to digital, and emerging markets grow. In the primary market, efforts should be made to scale up promotion and improve research quality and availability. In the secondary market, market infrastructure must be modernised (e.g. clearing and settlement facilities for emerging market currencies) and should support electronification of front and back office processes.
- **Accelerate insurance product innovation.** As the world's largest hub for specialty commercial insurance, the London Market can help businesses better manage emerging risks, such as cyber, longevity, corporate liability, giga lofs and reputational damage. New capabilities and more robust data and analytics should be a priority.

- **Revitalise the global market for infrastructure financing.** The UK can lead infrastructure financing and advisory, and establish consistent legal, financial and management standards, develop new financing instruments, provide project pipeline transparency and foster a secondary market in infrastructure-related securities.
- **Preserve the UK's global leadership in investment management.** The UK can strengthen its domestic investment management market through skills development, robo-advice and pension fund consolidation and enhance the sector's international standing through greater product expertise and market liberalisation.
- **Secure the UK's position as the world's legal capital.** To strengthen the UK's distinctive legal offering and maintain the primacy of English law in commercial contracts and disputes, we should make efforts to increase harmonisation and develop contacts in emerging markets. In dispute resolution, cost and efficiency improvements will be key drivers of competitiveness.

OVERSEAS CLIENTS PROVIDE

30-40%

OF FUNDS MANAGED
BY UK INVESTMENT
MANAGEMENT FIRMS



THE LONDON MARKET IS THE

#1 HUB

FOR SPECIALTY
COMMERCIAL RISKS





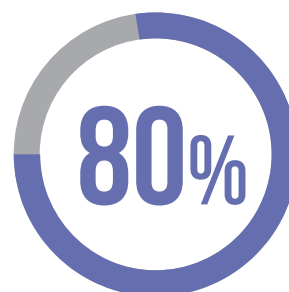
4. INNOVATE, DISRUPT, SCALE

Technology continues to disrupt the FRPS industry, from creating new ways to engage with customers to reinventing back-office processes. We should seek to build on our strength in FinTech through initiatives that may include:

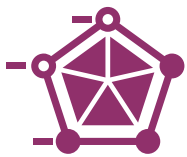
- **Diversifying and scaling up the UK FinTech scene** by embracing the next generation of start-ups and scale-ups in RegTech, insurance, legal services, regulation and accounting. The potential Brexit impact on FinTech funding availability in the UK could be addressed by encouraging venture capital activity, increasing investment thresholds in existing tax initiatives, and promoting (and potentially simplifying) AIM listings. Scaling must be supported by a clearer industry playbook to help young FRPS technology firms engage with established institutions.
- **Promote industry utilities**, primarily in financial services but potentially also in some areas of legal services and accounting. Shared services reduce costs and help firms implement regulation more efficiently.
- **Ensure the UK has appropriate capabilities, networks and regulations in areas that could disrupt the industry.** There should be a collective effort to encourage and invest in major industry disruptions, including blockchain, Internet of Things (IoT), cyber, data, cognitive analytics and telematics. There is an opportunity to link industry more closely with government initiatives (e.g. PETRAS IoT Research Hub run in collaboration with nine leading UK universities) and regulatory involvement (similar to the FCA's Project Innovate on FinTech).

GLOBAL FINTECH FINANCING HAS RISEN SEVEN-FOLD OVER THE PAST THREE YEARS TO

~\$20 BN FOR 2015



80% OF FINANCIAL SERVICES PROFESSIONALS CITE
**MANAGING
REGULATORY CHANGE**
AS A SIGNIFICANT DRIVER OF UTILITIES UPTAKE



5. BUILD SKILLS AND ATTRACT TALENT

A global financial centre requires access to the best talent in the world if it is to retain its leading position. The FRPS industry must develop a talent pipeline in the skills of the future, including data science, artificial intelligence, cyber security, interface design and software engineering. Brexit could increase the challenge by making it harder to attract international talent and because much research funding for universities comes from EU sources, an area where the UK had outperformed its peer group.³

Stakeholders should:

- **Agree an approach to retention, sourcing and movement of high quality FRPS talent between the EU and the UK.** The economic contribution of European immigrants is significant. Between 1995 and 2011, migrants from the EU made a net positive contribution to British public finances of over £4 billion.⁴ Free movement of high quality FRPS talent across the EU is essential to the UK remaining a leading financial centre.

- **Broaden skilled immigration channels.** Limits on skilled immigration are holding FRPS businesses back, particularly in respect of expertise in new technologies and international markets. The industry and government must continue to address bottlenecks, for example by ensuring technology talent is on the Shortage Occupation list for Tier 2 visas.

- **Partner with schools and universities to build the next generation of technology skills.** Technology expertise is necessary to support FRPS innovation. Educational institutions specialising in emerging technology clusters or technology-related initiatives should be offered FRPS modules and apprenticeships, and there should be industry-specific qualifications curricula and apprenticeships. School and university curricula should encourage digital and mathematics skills.

- **Promote diversity,** to attract and retain talent from the broadest possible pool. Barriers to career progression must be addressed and diversity schemes supported. The industry should support research on diversity gaps.



UK COMPANIES WITH 10 PERCENT HIGHER
GENDER AND ETHNIC/RACIAL DIVERSITY ON
MANAGEMENT TEAMS AND BOARDS HAVE

5.8%

HIGHER EBIT
ON AVERAGE



³ The Royal Society, How much research funding does the UK get from the EU and how does this compare with other countries?, December 2015

⁴ The Economist. What have the immigrants ever done for us? November 2014

REINFORCE UNIQUE FOUNDATIONS

Underlying the five pillars is a need to **maintain secure foundations** for the industry. Without a stable political, business and regulatory environment, a diverse and global client base and effective stakeholder engagement, progress already made on the five pillars could be wasted.

These foundations include the need to:

- Retain and expand existing UK operations of foreign corporates through proactive outreach campaigns and use of incentives
- Launch a proactive campaign to attract new FDI to the UK, using a range of incentives
- Foster a new level of dialogue between industry, Government and regulators

- Recast the current approach to Government and regulatory policy design and implementation to be more mindful of international competitiveness
- Maintain and improve the UK's physical infrastructure and digital connectivity
- Guarantee a competitive taxation scheme for both businesses and individuals.

We see a dynamic scenario in which the UK becomes an FRPS hub for developed and emerging markets, with strong connected regional centres. The UK should strive to become a leader in growth areas, with a strong technology proposition and diverse, skilled workforce (Exhibit 2).

EXHIBIT 2

Our vision

United Kingdom: Leading the global financial and related professional services industry

From



Leading global and European FRPS centre, but emerging market centres strengthening their positions



A growing industry overall, but employment at risk in parts of the UK as offshoring and automation continue



Broad product portfolio, but lagging behind the US in growth areas like investment management



Strong innovation centre in banking, but funding gaps remain versus the US



First for financial and professional talent, but shortages in diverse profiles and next-generation skills

To

FRPS hub for the developed and emerging world, FRPS capital for Europe

Strong, connected regional centres with clear specialist capabilities and expertise

Leader in growth areas, including investment management, emerging risks and infrastructure financing and advisory

Dynamic technology centre across the whole FRPS industry, where innovation happens at scale

Diverse workforce that leads the world in combining financial, professional and technology skills

Solid foundations on trust, future-proof client base, dialogue and cooperation with policymakers

I. THE UK FRPS INDUSTRY IS A NATIONAL ASSET

A. The UK FRPS industry is a core driver of the UK economy and a national asset

The FRPS industry is critical to the UK economy. It provides 12 percent of output and employs nearly 2.2 million people.⁵ The FRPS industry plays a bigger role in our economy than other comparable countries.⁶ It generates the UK's largest industry-specific trade surplus (around 4 percent of output) and contributes more in net exports than all other net exporting industries combined.⁷ The FRPS industry is the country's biggest source of inward investment⁸ and the financial services sector generates 11 percent of tax revenue.⁹

The industry has helped raise regional and national living standards by providing high productivity and high value employment around the country. The average output per FRPS worker is close to £87,000, compared to the £52,000 UK average for other industries.¹⁰ Every region has FRPS output per worker higher than £61,000.

The FRPS industry is also an enabler for the wider economy. It provides finance and services that keep businesses working, including high-growth companies and SMEs. Nearly 40% of the £429 billion outstanding loans made available by major banks to UK businesses in 2015 were lent to SMEs. High-growth companies from across the UK also enjoy access to the largest share market for small companies in Europe, with over 1,000 companies quoted on the AIM. And nearly 1 million people have qualifications administered by the UK's legal, accounting and related professional bodies, providing a training ground for the next generation of business leaders.¹¹

The FRPS industry also improves people's everyday lives. It provides bank finance (including mortgage finance), protects against risks through insurance, and advances financial inclusion. In the UK today, there are 9.3 million basic bank accounts, a rise of 2.9 million since 2005.¹² The industry also safeguards savings and manages investments for the future. The UK has the second largest pension sector worldwide,¹³ despite having the world's fifth largest economy.¹⁴ And the FRPS industry continuously enhances its consumer proposition by embracing technological innovation – 56% of UK adults use online banking today, up from 30% in 2007.¹⁵

B. The industry goes beyond “the City”

The UK FRPS industry extends across the country, with diverse and interlinking businesses operating far beyond the City of London. Two thirds of the industry's employment and output contribution occurs outside London, and related professional services firms employ more people than the financial services industry does directly (Exhibit 3).

At a high level, the following FRPS industry segments can be found across the UK:

- UK-focused financial services industry across the country
- World-leading internationally-oriented financial services industry centred on London
- Flourishing consulting and accounting sectors, growing output at 8 percent a year, amid rising demand for (increasingly specialist) business advisory services
- Strong legal services sector with a world-leading position in dispute resolution and transaction management

⁵ Office for National Statistics (ONS), as quoted in TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

⁶ In 2014, World Industry Service IHS estimates financial and professional services GVA as a share of total GVA at 19% for the UK, compared to 16% for the US, 16% for France, 14% for Germany, 12% for Japan, 10% for India, 8% for China. Definition of professional services includes activities that are not directly covered by this report: architectural, engineering and other technical activities; advertising; and other business services.

⁷ TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

⁸ Office for National Statistics (ONS), UNCTAD FDI statistics

⁹ ONS Balance of Payments Yearbook, as quoted in TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

¹⁰ TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

¹¹ TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

¹² British Bankers' Association, as quoted in TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

¹³ TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

¹⁴ The World Bank, Gross domestic product ranking table, 11 April 2016

¹⁵ Office for National Statistics (ONS)

C. The UK competes against the US as a global centre for FRPS, despite its smaller domestic market

The UK exports more financial services than any other economy, including the US, and is one of the most open economies for foreign capital.

The UK is the second largest exporter of professional services after the US, and hosts the global headquarters for four of the world's top 10 law firms¹⁶ and six of the world's top 10 accounting firms in terms of fee income.¹⁷ English law is used in 27 percent of the world's 320 legal jurisdictions and is the governing law in 40 percent of global corporate arbitrations. London is the leading centre for international arbitration, ahead of second-placed Paris, and is four times more frequently used than New York.¹⁸

In financial services, the UK, powered by London, is the global leader in FICC trading, cross-border lending and specialty commercial insurance, and consistently occupies a top three position across other major globally mobile business lines (Exhibits 4 and 5).

EXHIBIT 3

Over two-thirds of FRPS jobs are located outside of the capital, and over 50 percent of jobs are in professional services



SOURCE: ONS Business Register

¹⁶ The American Lawyer, 2015 Global 100: Top-Grossing Law Firms in the World, 28 September 2015; company websites; press search

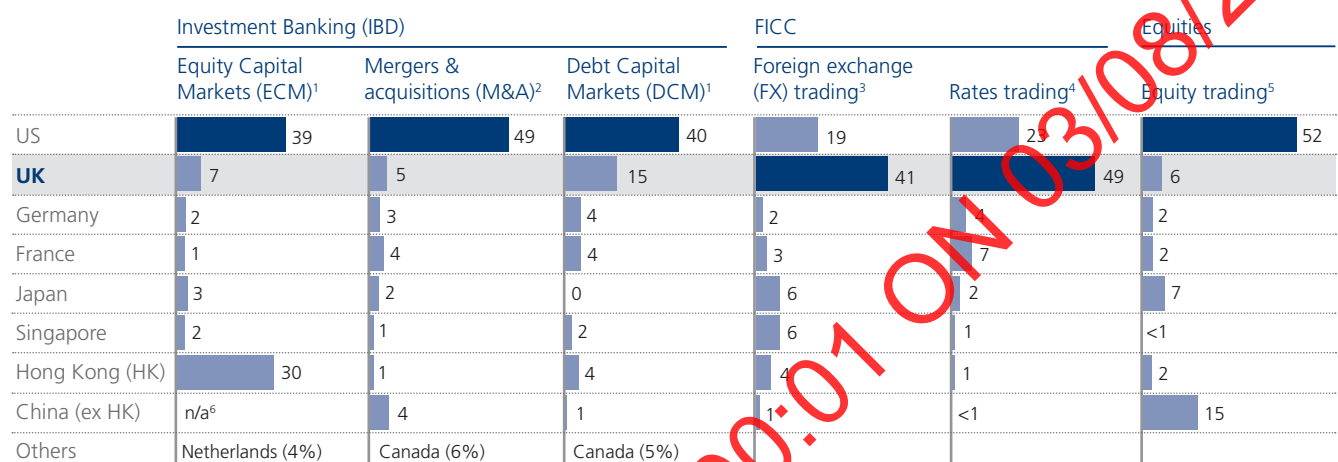
¹⁷ Accountancy Live, Top 25 survey, July 2015; company websites; press search

¹⁸ Queen Mary University of London, 2015 International Arbitration Survey: Improvements and Innovations in International arbitration 2015

EXHIBIT 4

The UK has a leading position across a broad range of globally mobile financial services businesses (1/2)

Share of the global market, %



1 % of aggregate non-domestic revenues from ECM / DCM deals between 2012 and 2014 (Dealogic, Windinfo, Thomson Reuters, Prime)

2 % of gross worldwide M&A revenues in 2013 where the locations are either target or acquirer for a deal (Dealogic)

3 % of Over The Counter (OTC) global turnover for foreign exchange in 2013 (BIS)

4 % of Over The Counter (OTC) global turnover for single-currency interest rate derivatives in 2013 (BIS)

5 % of value of share trading in 2014 in the equity exchanges in each location e.g. NYSE and NASDAQ for US (London Stock Exchange, World Federation of Exchanges)

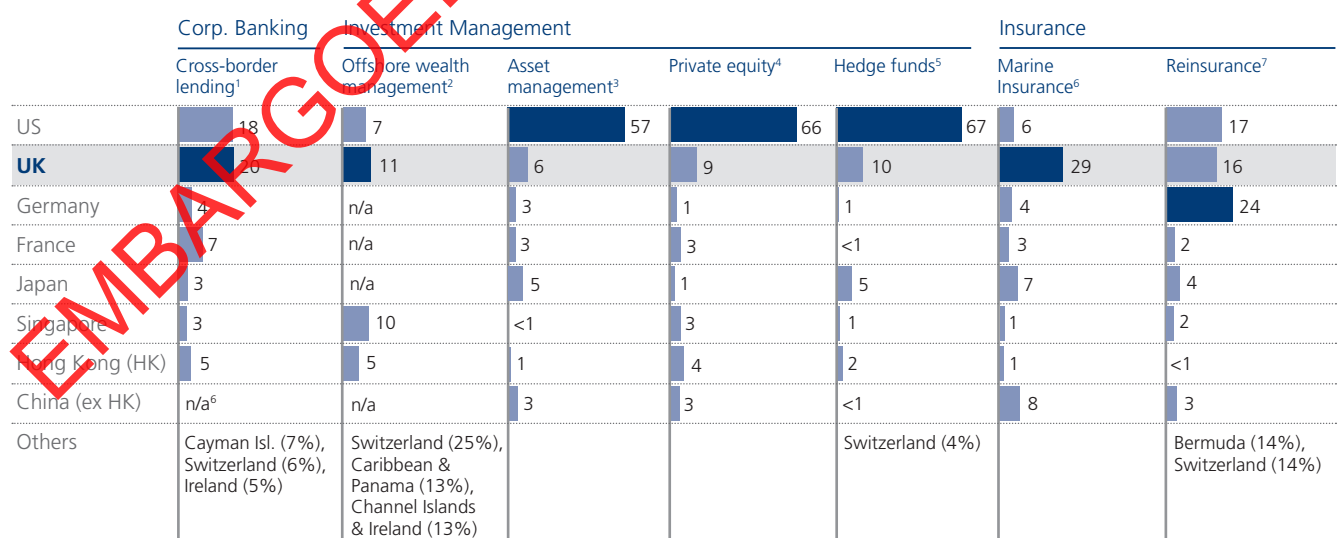
6 The China Securities Regulatory Commission did not allow foreign IPOs between 2012 and 2014 (data period for ECM figures)

Market leader

EXHIBIT 5

The UK has a leading position across a broad range of globally mobile financial services businesses (2/2)

Share of the global market, %



1 % of cross border liabilities as of Q2 2015 (BIS)

2 % of offshore wealth as of 2014 (BCG Global Wealth report)

3 % of global asset management revenue pools in 2014 (McKinsey Global Banking Pools)

4 % of aggregate capital raised in 2015 (Preqin)

5 % of global hedge funds Assets under management (AUM) in 2014 (McKinsey Global GrowthCube database)

6 % of gross marine insurance premiums written globally in 2014 (International Union of Marine Insurance IUMI)

7 % of gross reinsurance premiums written globally in 2014 (London Matters 2014 report by London Market Group (LMG) and BCG)

8 Data not available – China does not report cross-border lending figures to BIS

Market leader

II. OUR SUCCESS AND PROSPERITY ARE AT RISK

UK FRPS employment growth faces significant headwinds, and new sources of FRPS employment will be required to compensate for likely job losses from automation and off-shoring, particularly outside London. Growth has also been affected by the tough post-crisis operating environment, particularly in areas where the UK is a global leader (e.g. FICC). Additionally, technology is radically changing the capabilities required to succeed in FRPS, creating significant talent gaps.

Internationally, the UK's continued leadership position is not guaranteed. Regional centres in emerging markets are getting stronger, and the US is leading the global market in key growing business lines, including investment management and FinTech.

The vote to leave the EU amplifies some of the challenges and creates additional ones. It is likely to strengthen other European FRPS hubs (Frankfurt, Paris or Dublin) as firms or investors seek to guarantee access to the single market.

A. Jobs are threatened by automation and off-shoring, particularly outside London

Automation and off-shoring threaten a significant number of UK FRPS jobs, particularly in the middle and back-offices. It is estimated that around 40 percent of financial services activities and 35 percent of professional services activities can be automated by adapting existing technology.¹⁹

Job losses are likely to hit areas outside London hardest. Banking and insurance employment across the UK has declined since 2010, with areas outside London experiencing a drop of around 7 percent per year.

In the past, declines in banking and insurance employment have been offset by growth in related professional services, but this could be undermined as the wave of post-crisis "re-setting" of financial institutions comes to an end. Over time, the same technology forces driving the jobs decline in financial services will likely impact professional service employment trends.

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¹⁹ McKinsey Global Institute [NOTE: Similar trends are at work in the US, where ~43% of financial services activities and ~35% of professional services activities can be automated by adapting existing technology. More details available at <https://public.tableau.com/profile/mckinsey.analytics#!/vizhome/AutomationandUSjobs/Technicalpotentialforautomation>]

B. The operating environment has been tough post-crisis

Financial services firms have been under significant cost pressure in recent years, driven by regulation, restructuring, fines, litigation and large non-core operations. For example, the UK banking sector's return on equity (RoE) has fallen from 25 percent in 2006 to under 9 percent in 2015,²⁰ and could drop further once the latest round of regulation has been implemented. The insurance sector is facing similar challenges due to Solvency II regulations.

As a result, the majority of financial services firms have focused on risk mitigation, including reductions in cost and risk-weighted assets (RWA), and portfolio reshaping and repricing. UK banks divested \$138 billion in international assets between 2007 and 2015, making them less global (Exhibit 6).

The FRPS industry and the Government are working together to support growth, and should redouble efforts as the regulatory outlook continues to become clearer. The industry must also continue to rebuild trust, building on progress in recent years in modifying cultures and behaviours.

EXHIBIT 6

UK banks have divested the biggest share of international assets since 2007

BANKING EXAMPLE

Since 2007, Western banks have divested significant assets outside of their home markets

Bank divestitures 2007-15, USD billions

Nationality	Example	Cumulative deal value USD billions	Cross-border percentage of cumulative deal value
United States	JPMorgan Chase, citi, Bank of America	306	45%
United Kingdom	RBS, BARCLAYS, HSBC	187	74%
Spain	BBVA, Santander	117	68%
Belgium	KBC, DEXIA	70	70%
Italy	INTESA, SANPAOLO, UniCredit	69	37%
France	BNP PARIBAS, SOCIETE GENERALE	48	50%
Germany	COMMERZBANK, Deutsche Bank	47	65%
Rest of World		417	55%

SOURCE: Dealogic

This trend continues today

RBS

The bank will...fully exit its markets businesses in Central and Eastern Europe, the Middle East and Africa.

– The Guardian 03/03/15

BARCLAYS

Barclays...to cut up to 1,200 jobs by closing many operations in Asia, Russia and Brazil and exiting precious metals trading.

– FT.com 21/01/16

HSBC

HSBC Holdings Plc is shutting its private banking unit in India.

– The Independent 28/11/15

²⁰ Redburn Ideas, quoted in GAM, Are European banks a buy?, August 2015

C. Alternative FRPS hubs are getting stronger

The UK's location, language and culture have made it a natural home for an FRPS industry that straddles Europe and North America. This is likely to remain the case for some time. But FRPS profit pools are migrating to emerging markets, particularly China. The Chinese market for retail and wholesale banking and asset management grew 19 percent a year between 2007 and 2014 (Exhibit 7).

Hong Kong and Singapore are building depth and breadth on the back of regional GDP growth, and are credible alternative centres for many FRPS. For example, Hong Kong already has

a ~75 percent share of mainland Chinese IPOs and Singapore saw 10 percent annual growth in gross written premiums in reinsurance between 2010 and 2013, compared with 1 percent for the London Market.²¹

Increased fragmentation of global regulatory requirements makes acting as a global "one-stop-shop" for financial services more challenging. People and resources need to be employed in local markets to manage local regulations, risking a trickle of jobs away from established global centres.

Additionally, depending on the precise arrangements, Brexit may exacerbate the challenge. Access to the single market will be crucial to maintain the UK's competitive position.

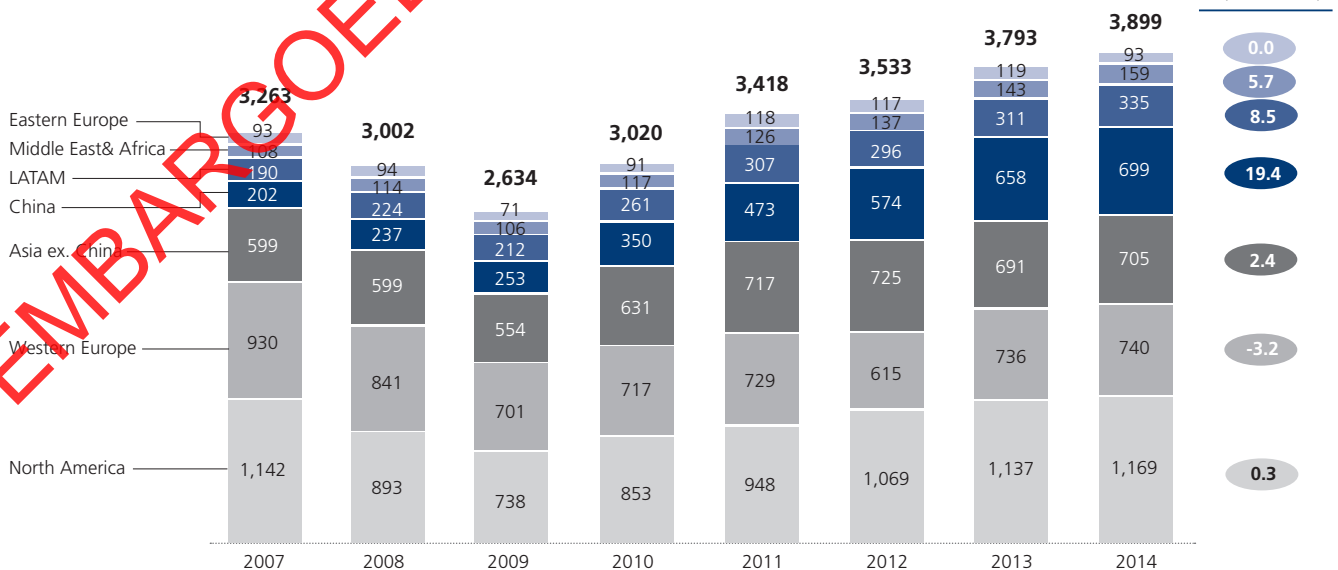
EXHIBIT 7

Global financial services revenue pools are shifting to emerging markets, especially China

Global retail banking, wholesale banking and asset management revenues

Bank divestitures 2007-15, USD billions

CAGR,
% (2007-2014)



SOURCE: McKinsey Panorama – Global Banking Pools, McKinsey CMIB Revenue Pools

²¹ London Market Group and Boston Consulting Group, London Matters: The competitive position of the London insurance market, November 2014

D. The US is better positioned to ride the next wave of FRPS growth

The UK's strongest position across financial services business lines is in FICC trading. Post-crisis, FICC has suffered from increasingly challenged economics, with returns falling below the cost of capital.²²

By contrast, the US leads in a number of key growth sectors, particularly investment management and FinTech (Exhibit 8). While this partly reflects the size of the US domestic market, it leaves the UK in a weaker position to ride the next wave of growth.

Today's growth trends reinforce the picture – the UK tends to focus on existing strength areas, rather than building its position where the US leads.

E. Different capabilities will be required to fuel future growth in FRPS

Technology is radically changing the capabilities needed to win in FRPS. New skills areas, including digital technology, big data, artificial intelligence, machine learning and telematics, increasingly occupy centre stage. Consequently, the FRPS ecosystem includes an ever-wider range of companies – with start-ups, established technology companies, market infrastructure players and utility providers operating alongside traditional FRPS firms.

Companies need talent that is in short supply, i.e. expertise in both financial services and technology. The shortage of technology skills is not just felt in FRPS – over 90 percent of global companies say they lack digital skills.²³ Further, millennials increasingly look to entrepreneurial opportunities and the technology industry rather than FRPS for careers.

EXHIBIT 8

The US currently leads in higher growth areas

CAGR, %

Businesses where the US is the global leader

Businesses where the UK is the global leader



¹ Number of FinTech firms raising venture capital and private equity funding between 2010-15 (Pitchbook) ² Aggregate capital raised in PE between 2010-15 (Preqin)

³ Hedge fund Assets under management between 2010-14 (Global GrowthCube) ⁴ AM revenue pools between 2010-15 (McKinsey Global Banking Pools) ⁵ Includes ECM, DCM, securitisation and M&A; revenue after risk cost between 2011-15 (McKinsey Global Banking Pools) ⁶ Equities trading revenue after risk cost between 2011-15 (McKinsey Global Banking Pools) ⁷ Rates revenue after risk cost between 2010-13 (McKinsey Global Banking Pools) ⁸ Cross border liabilities to non-financial corporations between 2010-15 (BIS) ⁹ Gross marine insurance premiums written globally between 2010-14 (International Union of Marine Insurance) ¹⁰ FX revenue after risk cost between 2010-13 (McKinsey Global Banking Pools)

²² Coalition, as quoted in Financial Times, Investment banks' return on equity declines, 21 February 2016

²³ Capgemini, The Digital Talent Gap: Developing Skills for Today's Digital Organizations, 2013

III. WE NEED TO ACT NOW

The UK has an exceptional starting position in FRPS. However, the industry is changing fast and the country faces ever-stronger competition. Growth, particularly in jobs, is not guaranteed, and Brexit is a major geopolitical event that will create additional headwinds. Despite the challenges, we believe that the UK can continue to lead the global FRPS industry. This report identifies a series of priority actions to achieve faster growth in jobs and output.

Priority actions should be based on three strategic imperatives:

a. Actions that will drive growth

We have focused on actions the industry, policymakers and regulators should take to drive growth in FRPS and the wider economy. These include nurturing existing areas of strength, adding high growth businesses and attracting additional international investment. The recommendations are based on our analysis of how industry profit pools are likely to shift, geographically and by business line, and which locations and sectors are likely to compete successfully for growth opportunities.

b. Actions that enhance partnership

A significant driver of FRPS growth will be the actions of individual firms, driving their own performance and profit. We have gone beyond what individual firms should do to maximise their own growth, and have focused on opportunities for the industry. Government and regulators to work collaboratively and with international policymaking bodies to drive industry-level growth, prioritising the opportunities that appear achievable.

c. Actions specific to the FRPS industry

We have deliberately focused on FRPS-specific areas for immediate attention, rather than on the UK's broader attractiveness, but it is recognised that there are many areas of overlap between FRPS and other industries.

These criteria lead to the prioritisation of five key pillars to help secure the UK's global leadership in FRPS:

- Connect globally
- Drive national growth
- Expand services
- Innovate, disrupt, scale
- Build skills and attract talent

These pillars should be supported by secure foundations comprising a stable political, business and regulatory environment, a diverse and global client base and stakeholder cooperation (Exhibit 9).

EXHIBIT 9

Proposed areas for action

Areas for action	
Connect globally	<ul style="list-style-type: none"> • 1.1. Maintain an effective UK/ EU relationship and sustain access to the single market for FRPS • 1.2. Refocus strategic intentions on key non-EU partners (e.g. US, Canada, Japan, Australia and other Commonwealth countries) by pursuing bilateral trade and investment agreements and regulatory coherence • 1.3. Dramatically accelerate efforts to broaden the industry's links with emerging markets, particularly building on progress with China and India and intensifying bilateral economic and financial dialogues
Drive national growth	<ul style="list-style-type: none"> • 2.1. Reinforce the value proposition and marketing of complementary regional clusters across the UK • 2.2. Accelerate efforts to build a robust pipeline of domestic financial and related professional services talent and strengthen local capabilities to support specialist cluster growth in cooperation with universities and regional bodies
Expand our services	<ul style="list-style-type: none"> • 3.1. Strengthen UK capital markets and market infrastructure to capture growth in debt and equity financing, foreign exchange and electronic trading • 3.2. Accelerate innovation in the London insurance markets, focusing on new risks (e.g. cyber) and embracing new market segments • 3.3. Revitalise the market for infrastructure finance and advisory services through new standards, partnerships and structures • 3.4. Preserve UK leadership in investment management and encourage new forms of advice (e.g. robo-advice), despite the uncertain outlook • 3.5. Secure London's position as the world's legal capital, and maintain English law as first choice for commercial contracts and disputes as interactions between English and EU law are unwound
Innovate, disrupt, scale	<ul style="list-style-type: none"> • 4.1. Diversify and scale FinTech, broadening the UK's leadership position into insurance and related professional services and securing EU market access for high-growth firms • 4.2. Develop large-scale innovation ecosystems across FRPS (e.g. blockchain, IoT, data, telematics, cognitive analytics, cyber) • 4.3. Foster cooperation and create the regulatory framework for the next wave of industry utilities (e.g. cyber risk, AML, market and reference data) in the UK and attract participation from EU financial and related professional services firms
Build skills and attract talent	<ul style="list-style-type: none"> • 5.1. Agree approach to retention, sourcing and movement between the EU and the UK of high quality talent working in FRPS • 5.2. Ensure that the UK immigration system facilitates access to top global FRPS talent for next-generation skills (e.g. data science, artificial intelligence, cyber security) and strategically important partners (e.g. US, China, India) • 5.3. Build next-generation skills, particularly in technology, through industry collaboration, apprenticeships and schools and universities • 5.4. Collectively promote diversity through industry-sponsored schemes
Reinforce unique foundations	<ul style="list-style-type: none"> • 6.1. Retain and expand existing UK operations of foreign corporates through proactive outreach campaigns and use of financial and operational incentives • 6.2. Launch a proactive campaign to attract new FDI to the UK, using a range of incentives • 6.3. Foster a new level of dialogue between industry, government and regulators • 6.4. Recast the current approach to government and regulatory policy design and implementation to be more mindful of international competitiveness • 6.5. Maintain and improve the UK's physical infrastructure and digital connectivity • 6.6. Provide a competitive taxation scheme for both businesses and individuals



1. CONNECT GLOBALLY

The UK is a global FRPS centre, and international trade and investment drive its profile and performance.

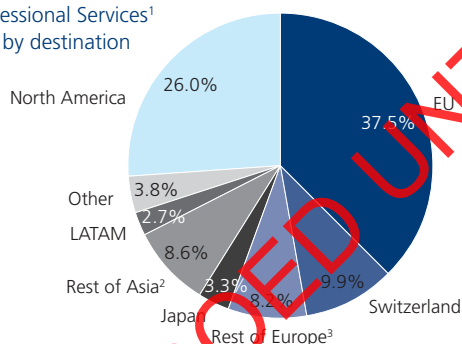
Europe and North America account for over 80 percent of UK professional services exports, and over 85 percent of FDI stock in the UK across FRPS (Exhibits 10 and 11).

However, the greatest competitive threats to the UK's position comes from emerging markets, and the uncertainty created by the Brexit vote. In response, the UK should take initiatives to become the primary FRPS hub for both developed and emerging markets, and to reinforce its position as the FRPS capital of Europe.

EXHIBIT 10

Europe and North America account for over 80% of UK professional services exports

UK Professional Services¹ exports by destination



¹ Defined here as 'professional, management consulting & R&D services'

² Includes: China (ex. Hong Kong) 0.6%, India 0.6%, Hong Kong 0.9%, Singapore 1.3%

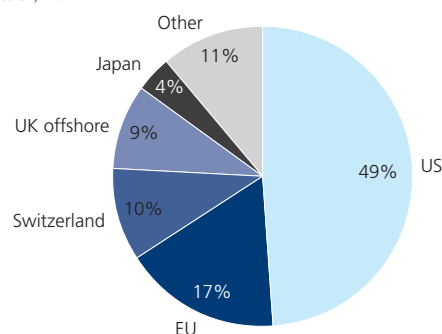
³ Includes: Channel Islands 1.3%, Norway 1.1%, Isle of Man 1.0%

SOURCE: Office for National Statistics

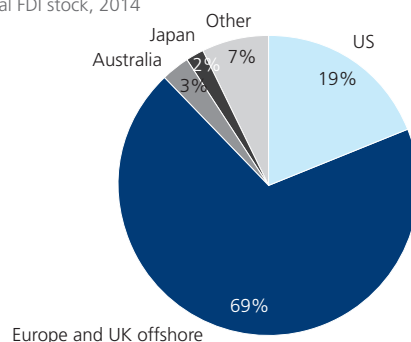
EXHIBIT 11

Most foreign direct investment in UK financial and professional services comes from Europe and the US

Financial services FDI stock in the UK by geographical origin
% total FDI stock, 2014



Professional services FDI stock in the UK by geographical origin
% total FDI stock, 2014



SOURCE: Office for National Statistics; UNCTAD FDI statistics

1.1 Maintain an effective UK/EU relationship and sustain access to the single market for FRPS

To reinforce London's role as Europe's financial centre, we must maintain an effective UK/ EU relationship. European companies look to London to raise capital and for complex professional advice, and it is in the interests of Europe and the UK to maintain joint market access. In order to do that, three principles should guide an initial response to the Brexit vote:

1. Map an effective relationship with the EU which maintains mutual market access.

It is of utmost importance that UK and EU firms continue to trade freely under broadly similar conditions and that any transition is managed effectively.

It will be important to ensure that UK access to the single market remains, as far as possible, in place, to ensure that:

- UK-based FRPS businesses continue to trade freely with the EU-27 and vice-versa.
- Mechanisms approximating single market passporting remain.
- Transitional agreements act as effective stepping stones to the new relationship.

2. Prize clarity and stability; essential to markets, investors, customers and employees.

The exit process must be orderly, with a clear view of the UK withdrawal agreement and framework for the UK's future relationship with the EU.

- An orderly exit is essential for financial stability in both the UK, the EU-27 and internationally.
- There is a significant global dimension; cooperation with international bodies and institutions is important.
- Combining exit negotiations and a new relationship agreement is the best way to address issues and move forward.

3. Defend the UK's pre-eminent position in FRPS

To maintain London's international competitiveness, a renewed focus on global regulatory coherence and opening up global markets is crucial. Additionally, UK policymakers and regulators must communicate consistently with EU regulators.

The following initiatives can contribute to safeguarding international competitiveness:

- A renewed focus on reasserting the UK's voice in promoting global regulatory coherence.
- Addressing the question about the future status of EU branches via inter-governmental and inter-regulator discussions and clarifying any grandfathered status or acquired rights that UK-based FRPS businesses may enjoy in the EU under past or present EU legislation.
- Highlighting the potential relatively better long-term economic outlook for the UK and thereby promoting financial stability.

ALTHOUGH SERVICES MAKE UP
70% OF EUROPE'S OUTPUT AND
MORE THAN 90%
OF JOBS, THEY ACCOUNT FOR
ONLY 20% OF INTRA-EU TRADE



56%
OF UK PROFESSIONAL
SERVICES EXPORTS
GO TO EUROPE



1.2 Refocus strategic intentions on key non-EU partners (e.g. US, Canada, Japan, Australia and other Commonwealth countries) by pursuing bilateral trade and investment agreements and regulatory coherence

The UK would benefit from even closer economic integration with the US, which is the single biggest contributor of FDI to UK financial services and the biggest non-European contributor of FDI in UK professional services, accounting for 49 percent and 19 percent respectively.²⁴ The US also accounts for 25 percent of UK professional services exports.²⁵

Similarly, Japan is a key trade and investment partner, accounting for more than a third of FDI stock from outside Europe and North America.²⁶ Financial services account for more than a quarter of UK exports to Japan.²⁷

Specific actions to enhance UK FRPS trade and investment with the US and Japan may include:

- **Promoting targeted efforts to grow FRPS exports** (e.g. infrastructure financing) and inward investment (UK infrastructure projects, FinTech) with the US.
- **Coordinating bilateral policy and regulatory coherence with the US** across financial services (bank capital and liquidity measures, OTC derivatives reform), professional services (Investor-State Dispute Settlement instrument linking with UK international arbitration capabilities, issues surrounding US GAAP and IFRS accounting standards) and business more broadly (data privacy and security).²⁸
- **Promoting targeted efforts to grow FRPS exports** (investment management, life insurance, infrastructure financing, M&A advisory, professional services) and wider commercial investment (UK subsidiaries, infrastructure projects) with Japan.
- **Working with Japan** in third countries where the UK and Japan have complementary strengths (e.g. ASEAN on FinTech).



²⁴ UNCTAD FDI statistics

²⁵ ONS International Trade in Services statistics

²⁶ UNCTAD FDI statistics

²⁷ UKTI, Doing business in Japan: Japan trade and export guide, May 2015

²⁸ Atlantic Council, TheCityUK & Thomson Reuters, The Danger of Divergence: Transatlantic Financial Reform & the G20 Agenda, 2013

In addition, we should pursue rapid advances in trade and investment relationships with the rest of the world by prioritising services (especially FRPS) in newly negotiated free trade agreements by:

- **Building a renewed and independent UK approach** across economic, trade and investment policy, supported by government.
- **Developing a UK approach to agreements** with key trade partners on market-openness to:
 - replicate advantages currently available to the UK as an EU member.
 - modernise and expand those advantages.
- **Exploring scope for using international law principles** to enable the benefits of EU trade agreements to continue to apply to the UK.
- **Prioritising key resources** for trade agreements with key trade partners:
 - establish a priority list of trade partners, by value and volume of financial and related professional services business
 - rapid development of resources to ensure the UK is equipped to manage a full-service trade and investment policy, including conducting trade and investment negotiations.
- Preparing to engage early in trade policy activities requiring little preparation, for example TISA negotiations or the multilateral procedures for implementing the recent WTO Trade Facilitation Agreement

1.3 Dramatically accelerate efforts to broaden the industry's links with emerging markets, particularly building on progress with China and India and intensifying bilateral economic and financial dialogues

As the world's leading exporter of financial services and second biggest exporter of professional services,²⁹ the UK is well-positioned to significantly increase FRPS trade and investment with emerging markets, which remain big importers of FRPS. For example, China and India import \$26 billion and \$11.5 billion respectively in financial services annually.³⁰ The UK is also well positioned to share expertise and cooperation with emerging markets in financial centre development, regulation and professional qualifications. That includes building on the successful Chinese Pilot Free Trade Zones (PFZ) and UK-India Financial Partnership initiatives. In addition, growing FRPS trade and investment, and sharing UK expertise in emerging markets will help drive economic growth in these markets and strengthen economic links with the UK. This includes markets in Asia-Pacific, Eurasia, Latin America, the Middle East and Africa, as well as through targeted International Financial Centre initiatives.

THE UK HAS FALLEN FROM INDIA'S
**#3 TRADING
PARTNER TO #12**
OVER THE PAST 15 YEARS



THE UK ACCOUNTS FOR
JUST 1%
OF CHINA FDI STOCK



²⁹ IMF Balance of Payments statistics, World Bank Indicator statistics
³⁰ UNCTAD statistics

The Government, industry representative organisations, the City of London Corporation and individual firms are strengthening links with China, India, and emerging markets, and the importance of those efforts is increased following the referendum outcome. Specific steps may include:

- **Developing an action plan centred on products the UK can offer to emerging markets to help create jobs and growth** (e.g. investment management, infrastructure financing, FinTech, legal services) and identifying potential trade barriers and regulatory obstacles in priority markets in light of the referendum vote.
- **Exporting UK regulatory, legal and professional standards** (e.g. investment advisory and asset management, accounting standards) and professional qualifications (including skills training) to emerging markets.
- **Supporting government efforts to advance FRPS priorities internationally** through Economic and Financial Dialogues (EFDs), Joint Economic and Trade Committees (JETCOs), taskforces and other bilateral contacts.
- **Facilitating links between the UK's devolved administrations and FRPS clusters in emerging markets** (e.g. China's City Clusters and Pilot Free Trade Zones, India's Smart Cities).

- Actions with China may be designed to build on progress made in the 7th China-UK Economic and Financial Dialogue in 2015:³¹

- **Strengthening London's position as a global centre for investment in China** by improving market access for UK firms and facilitating investment from international investors into China.
- **Attracting investment from Chinese FRPS firms** into the UK.
- **Promoting expertise-sharing and regulatory coherence with China**, building on recent agreements to collaborate in priority areas (e.g. technological innovation, peer-to-peer lending, consumer protection, alternative dispute resolution).³²

- Actions with India may build on progress made in the 8th UK-India Economic and Financial Dialogue in 2016:³³

- **Supporting implementation of the recommendations of the India-UK Financial Partnership** on corporate bond market development, pension policy, financial insolvency regulation and infrastructure financing, as well as future areas of work.³⁴
- **Promoting trade and investment with India** by encouraging Indian firms to list and raise finance in London.

The UK's position in emerging markets will also benefit from actions outlined elsewhere in this document, including growing debt and equity issuance by emerging markets corporates, promoting internationalisation of emerging market currencies and attracting emerging market companies to the UK.

³¹ HM Treasury, Combined Policy Outcomes of the 7th China-U.K. Economic and Financial Dialogue, 21 September 2015

³² HM Treasury, Combined Policy Outcomes of the 7th China-U.K. Economic and Financial Dialogue, 21 September 2015

³³ HM Treasury, UK-India 8th Economic and Financial Dialogue: Joint statement, 19 January 2016

³⁴ TheCityUK & Kotak Mahindra Bank, India-UK Financial Partnership: Progress Report, January 2016



2. DRIVE NATIONAL GROWTH

Although employment in UK FRPS is growing overall, off-shoring and automation are putting jobs at risk, with regions outside London and the South East most likely to be impacted. The trend could be more pronounced due to the Brexit outcome. However, the FRPS industry can respond by creating strong, connected regional centres with clear specialist capabilities and expertise.

2.1 Reinforce the value proposition and marketing of complementary regional clusters across the UK

Regional FRPS centres typically develop on the back of the needs of investors (e.g. Citigroup investment in software development talent in Northern Ireland has expanded into IT and operations more broadly over time) and strengths of local universities (e.g. FinTech in Manchester due to strong technology programmes). Building on those strengths, the UK FRPS industry can work with the Government to promote regional centres, highlighting their expertise to potential investors and positioning them as complementary to each other rather than competitors.

Further, there is uncertainty regarding the future of EU investment at the sub-national level (for example in the regions and local universities). There is also room to ensure that the structures supporting investment promotion are working well for all regions, as part of the devolution agenda. UKTI operates on a “UK-first approach” whereby FDI enquiries are channelled to partner organisations in the devolved administrations and LEPs. This structure seeks to present a consistent and coherent offering to investors.

An important factor will be a clear nationwide view on how to build specialist expertise in priority areas, including emerging technology skills like cyber and analytics, where the FRPS industry will need to strengthen links with emerging technology hubs across the country (Exhibit 12). This entails building on broader enablers for innovative sectors, such as addressing the relative lack of venture capital (VC) presence outside London.



Other specialist areas include more traditional middle and back-office activities, where the UK could position itself to capture the ‘next wave’ of near-shoring that would otherwise be at risk of off-shoring (e.g. risk operations, compliance operations, finance). These activities have relatively high skill requirements, particularly in conjunction with automation.

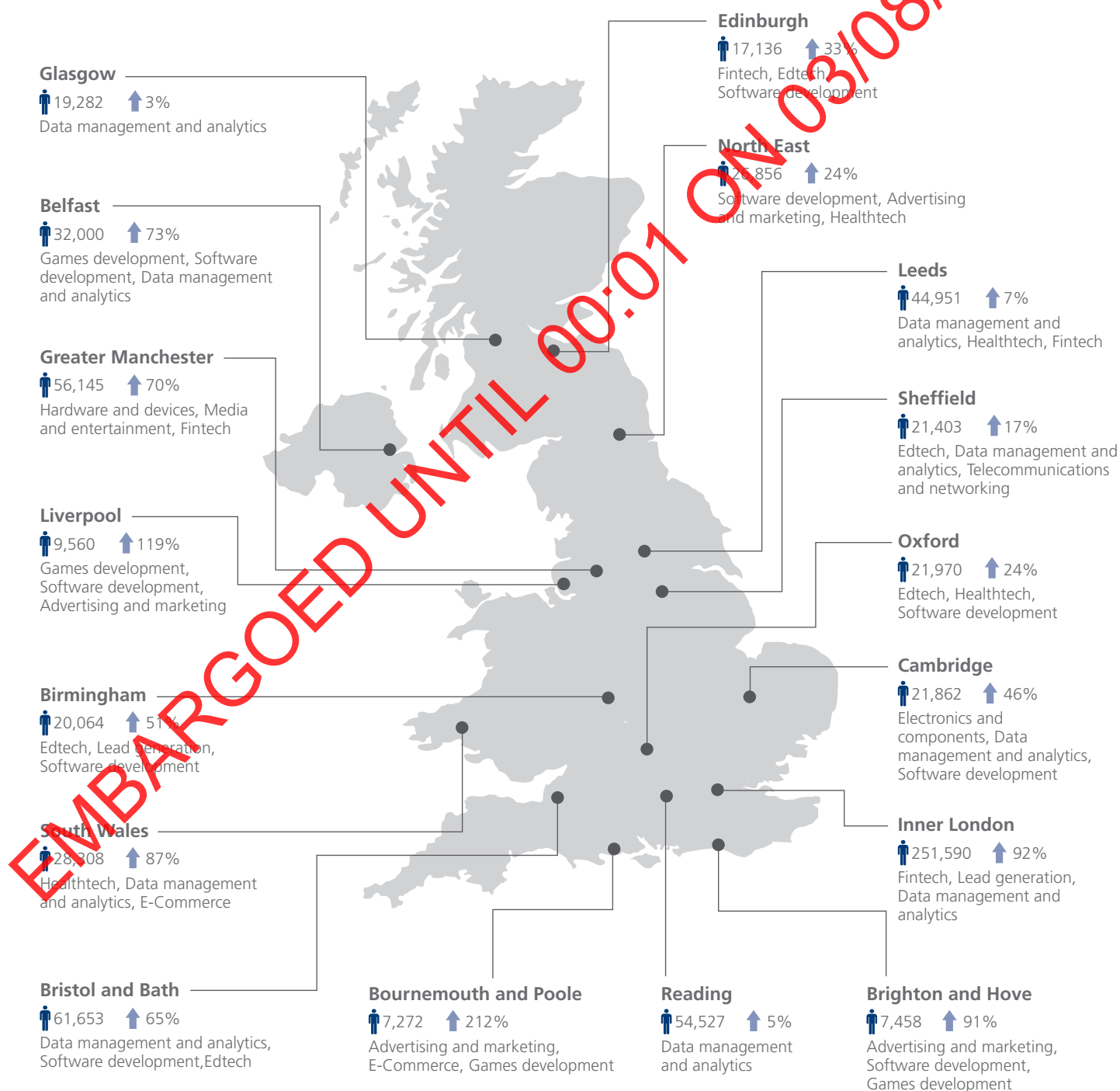
Specific actions to sharpen the value proposition and marketing of UK regional clusters include:

- **Aligning on key specialist needs and identifying regional centres with existing capabilities and ecosystems**, building on the Financial Centres of Excellence programme.
- Following the outcome of the referendum, we welcome the **review of the UK’s promotional machinery** to ensure it is fit for the new circumstances. Additionally, **strengthening the identities of specialist clusters** through single contact points for prospective investors, distinctive names and selling points for each regional centre, promotional materials presenting the UK’s regional centres as complementary parts of a coherent narrative and developing a value proposition for investor firms.
- **Cooperating more with central government and regional promotional bodies to promote the UK’s specialist clusters domestically and globally**, aiming to win new and incremental investment and to showcase political support for regionalisation.
- **Contributing to the broader agenda of regional economic development** by supporting better regional economic data and improved regional infrastructure, and by continuing to support the nationwide devolution agenda.

EXHIBIT 12

Technology hubs are emerging across the UK

 Digital employment
 Growth of digital companies (2014-15)



SOURCE: ONS Business Register; Tech City UK, Powering the digital economy, 2015

2.2 Accelerate efforts to build a robust pipeline of domestic financial and related professional services talent and strengthen local capabilities to support specialist cluster growth in cooperation with universities and regional bodies

Regional FRPS centres will rely on local capabilities to support specialist cluster growth. Specialist industry clusters will also need to improve investment marketing activities.

In Scotland, Northern Ireland and Wales, industry players, universities and regional bodies have successfully collaborated to strengthen regional clusters. Scotland has recently launched CodeClan, a digital skills academy that develops a talent pipeline of software developers for Scottish industry. Capital markets firms in Northern Ireland have developed collaboration platforms with local universities, whereby PhD students conduct and commercialise research jointly with the industry. Wales has successfully involved senior industry leaders in regional development activities.

Specific actions to further strengthen local capabilities to support specialist cluster growth include:

- **Reviewing and potentially expanding successful strategies to generate inward investment** in Scotland, Wales and Northern Ireland (e.g. local FRPS councils led by senior representatives from the industry and universities, senior industry champions) **to England's cities and LEPs** in line with the City Deals' expanded mandate.
- **Developing local talent pipelines in specialist skills areas in partnership with universities** by updating curricula to address future skills requirements, developing local career paths linked to apprenticeships and graduate programmes and promoting careers in specialist areas.
- **Strengthening links between industry, universities and regional bodies in specialist clusters**, by commercialising university researchers' innovations, joint appointments in industry and academia, initiatives to provide start-ups and SMEs with access to technical expertise, and events and mentorship programmes linking start-ups with investors and industry leaders.

THERE ARE
22
UNIVERSITIES
WITHIN AN HOUR'S DRIVE OF
GREATER MANCHESTER




WALES CREATED OVER
2,000
NEW JOBS
IN FINANCIAL AND
PROFESSIONAL SERVICES
IN 2014-15 ALONE



3. EXPAND OUR SERVICES

The UK FRPS industry lags the US in growth areas including investment management and cyber insurance. However, there is no reason why our country can't become the leader in key growth areas, including insurance products for emerging risks, investment management and infrastructure financing.

Brexit might impact some services and/or products, with the specialty insurance market particularly exposed due to its exports to the EU. In this regard, maintaining access to the single market will be important.

We have identified a sub-set of substantial, high-growth businesses where there is a clear opportunity for partnership across industry, Government and regulators to strengthen the UK's global position. While these are not the only fast growing businesses in the industry, they are the ones where joint action could make a real difference.³⁵

3.1 Strengthen UK capital markets and market infrastructure to capture growth in debt and equity financing, foreign exchange and electronic trading

The UK leads in a broad range of capital markets businesses. In the primary market, the UK is the second largest centre for

debt financing globally (after the US) and one of the leading locations for international IPOs.³⁶ In the secondary market, the UK is the global leader in FICC trading, with over 40 percent of the market in foreign exchange and OTC interest rate derivatives.³⁷ The position is supported by a distinctive capital markets infrastructure across the entire value chain – trade facilitation and execution, clearing, custody and settlement and information and technology services.

To maintain and improve its position, the UK must capture pockets of growth in global capital markets, whether they arise from the largely unmet financing needs of international corporates or business shifts to emerging markets and to digital.

In the primary market, the UK has witnessed a fall of around 60 percent in IPO activity since the crisis, while US stock exchanges have maintained pre-crisis activity levels and overtaken UK issuances by a factor of 2.5 to 1. During the same period, Hong Kong has seen 50 percent growth in IPOs

THE UK IS THE
GLOBAL LEADER
FOR FIXED INCOME, CURRENCIES AND
COMMODITIES TRADING



THE UK HAS WITNESSED

**A FALL OF
AROUND 60%**
IN IPO ACTIVITY SINCE THE CRISIS



³⁵ NOTE: Islamic finance, another fast growing business, is covered in 1.3.

³⁶ Dealogic

³⁷ Bank for International Settlements, Triennial Central Bank Survey of foreign exchange and derivatives market activity, 2013

(fuelled by Chinese corporates) and overtaken the UK as an IPO hub (Exhibit 13).

This decline in the UK's position is not just driven by sector mix. It is observed across all geographic regions and most major industries, including technology (UK share of offshore IPOs declined from 31 percent from 2004-09 to 14 percent from 2010-15), financial services (61 percent to 34 percent), healthcare (41 percent to 13 percent), and mining (65 percent to 28 percent).³⁸

Similar forces are at play in debt financing. The UK has yet to strengthen its proposition as a centre for debt financing for emerging markets – Hong Kong, Singapore and the US are all ahead in offshore bond issuance by Chinese corporates.³⁹ Closer to home, European corporates (including SMEs) remain reliant on bank lending for funding, presenting an opportunity to grow debt financing.

More broadly, steps to grow equity and debt financing for Europe (assuming the UK retains a similar level of access to the European market as pre-Brexit) and emerging markets corporates will reduce reliance on bank lending and facilitate a transition to a capital market financing model.

The UK is innovating in capital markets and has issued renminbi and rupee denominated bonds as part of the agenda for renminbi and rupee internationalisation (see 1.3.). Additionally, the UK has abolished stamp duty on AIM shares and the FCA has recently recommended revising prospectus timelines and rules to make it easier for firms to list on the London Stock Exchange.⁴⁰

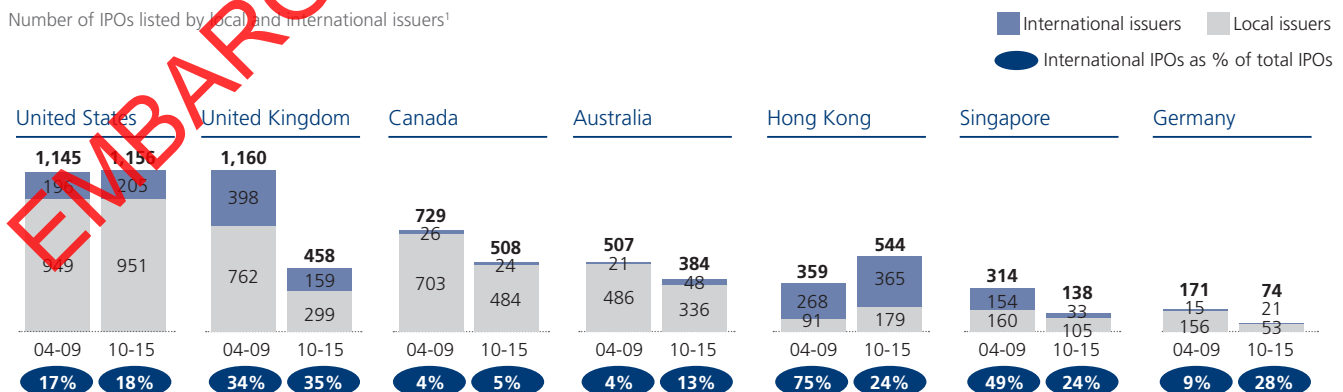
In the secondary market, the UK should build on its leadership position in foreign exchange to capture emerging markets growth. The UK is the largest centre for trading diverse currencies (Exhibit 14). In future, the biggest trading opportunities are likely to be in the renminbi and the rupee (see 1.3.).

The UK industry needs to lead the ongoing electronification of capital markets activities. Previous waves of digitisation have significantly impacted product value chains (over 90 percent of trading in futures, cash equities and G10 spot FX markets is now electronic). Shifts to electronic trading have typically compressed costs by four to five times and have led to volume increases, which have sometimes compensated for margin compression. Electronification is expected to continue, aided by the rise of FinTech firms. Taking an active role in this transformation will also reinforce the UK's position as an investment management centre (see 3.4.) and can positively impact the sell-side business model.

EXHIBIT 13

The UK's global position in IPOs has declined dramatically since the crisis

Number of IPOs listed by local and international issuers¹



¹ Numbers may be under-reported due to criteria used by Dealogic to classify a deal as an IPO issuance (e.g., deal should come from the ECM desk of the company in question, there should be sale of stake/ownership transfer, there should be a sale to market)

SOURCE: Dealogic

³⁸ Dealogic

³⁹ Dealogic

⁴⁰ Financial Conduct Authority, Availability of information in the UK Equity IPO process, April 2016

Specific actions to strengthen UK capital markets and market infrastructure include:

• **Growing debt and equity issuance from emerging markets:**

- Scaling up targeted efforts to attract issuance from growing industries (e.g. consumer technology, biotech) and markets with notable international issuance activity (e.g. China, Israel, Poland).
- Improving quality of research and information for potential investors in emerging markets' debt and equity.

• **Revising listing requirements to stimulate equity financing,** building on FCA recommendations:⁴¹

- Improving information availability and quality (e.g. no blackout period, more non-connected research).⁴²
- Reviewing disclosure requirements for follow-on issuance.⁴³
- Incentivising investment in high-growth companies and SMEs.⁴⁴

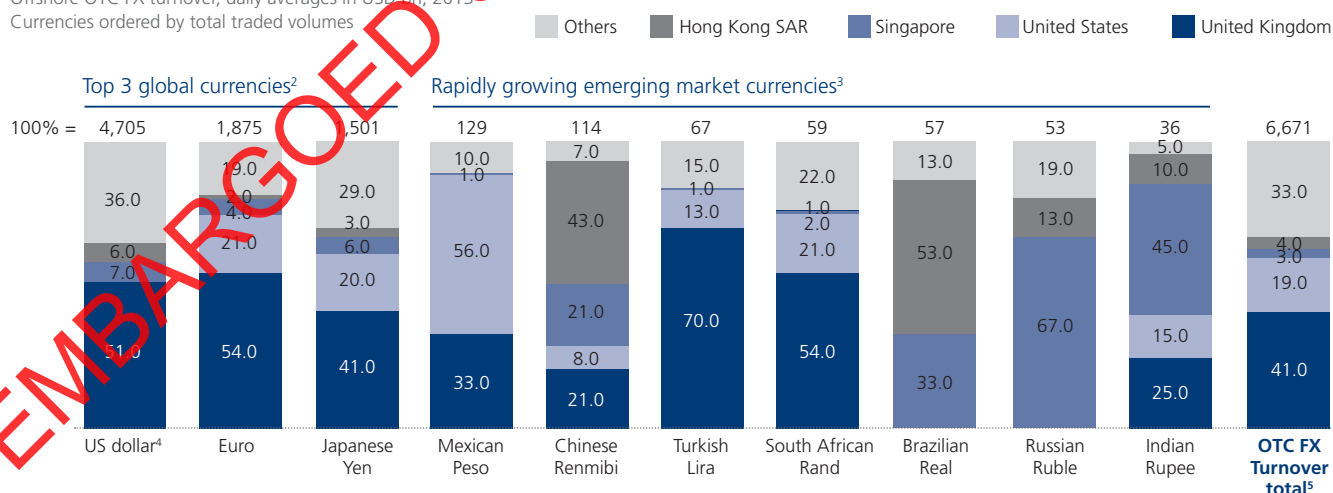
• **Promoting internationalisation of emerging market currencies** and strengthening the London offshore FX markets:

- Deepening offshore markets for foreign currency-linked products (e.g. trade finance, interest rate swaps, fixed income indices, ETFs).
- Upgrading market infrastructure (e.g. clearing banks, real-time settlement).
- Targeting investor groups with more limited exposure (e.g. sovereign wealth funds).
- Supporting electrification of capital markets activities:
 - Cooperating to adapt processes to digital (e.g. clearing and settlement, risk management).
 - Helping regulators clarify operational risk requirements and supervisory process.
 - Encouraging innovation by incumbent and FinTech firms in technologies that could transform capital markets operations (e.g. blockchain).

EXHIBIT 14

The UK has a very strong position in OTC trading across a broad range of currencies

Offshore OTC FX turnover, daily averages in USD bn, 2013
Currencies ordered by total traded volumes



¹ Spot transactions, outright forwards, FX swaps, currency swaps, options and other products; adjusted for local inter-dealer double-counting (i.e., "net-gross" basis)

² Account for 72% of total OTC FX turnover globally (offshore and onshore)

³ Top 10 emerging market currencies with >10% annual CAGR of OTC turnover between 2010-13

⁴ UK remains market leader (41% of global turnover) even if onshore USD trading is included

⁵ Includes both offshore and onshore volumes of major currencies traded globally. OTC FX turnover total appears lower in value than turnover of individual currencies because it counts each trade of a currency against another currency as a singular event (e.g., USD-CNY trading reflected once in total figures vs. twice, i.e., once each in US Dollar and Chinese Renminbi figures)

SOURCE: BIS triennial central bank survey 2013

⁴¹ Financial Conduct Authority, Availability of information in the UK Equity IPO process, April 2016

⁴² TheCityUK & King & Wood Mallesons, Capital Markets for Growing Companies: A review of the European listings regime, August 2015

⁴³ TheCityUK & King & Wood Mallesons, Capital Markets for Growing Companies: A review of the European listings regime, August 2015

⁴⁴ TheCityUK & King & Wood Mallesons, Capital Markets for Growing Companies: A review of the European listings regime, August 2015

3.2 Accelerate innovation in the London insurance markets, focusing on new risks (e.g. cyber) and embracing new market segments

London is the largest global hub for commercial and specialty insurance, over twice the size of California, its nearest competitor. The London Market is the global leader for marine, energy and aviation insurance, and one of the largest hubs for reinsurance.⁴⁵ The market comprises a unique ecosystem of carriers, brokers and related professional services, all located within a 400 metre radius of Lloyd's of London.

However, London faces long-term challenges to its historic position and additional uncertainty from Brexit. Increasing underwriting locally in emerging market centres could put 30 to 40 percent of London premiums at risk, particularly as London is a relatively high-cost location with expense ratios as much as nine percentage points higher than its peers.⁴⁶ In addition, the rise of alternative capital could disintermediate parts of the London Market – alternative sources already supply ~\$70 billion of capital to the reinsurance industry.⁴⁷

The UK needs to place itself at the forefront of insurance innovation. The London Market must develop insurance

products that enable corporates to better manage emerging risks, including cyber, longevity, corporate liability, gig economy, reputation, brand and climate and weather-related risks (Exhibit 16). The opportunity is significant and will address a large unmet need – the share of corporate risks covered by insurance has shrunk to as little as 10 percent.⁴⁸

In addition, emerging market segments (for example, Islamic insurance) offer potential.

Concerns about cyber risk are driving demand for insurance. Another significant driver is disclosure policy. The US has required companies to disclose breaches to regulators and affected consumers since 2002,⁴⁹ leading to the development of a cyber insurance market, and the EU is expected to enact a similar law in 2018.⁵⁰ Today, US companies purchase 90 percent of cyber insurance, while just 10 percent of cyber insurance is underwritten on the Lloyd's platform. The London Market must take action if it is to become a leader in the field.⁵¹

The UK government is taking steps and its Cyber Essentials scheme outlines cyber security standards for businesses.⁵² Moreover, a proposed board-level Cyber Check-List will raise awareness and boost demand for insurance. Some 50 percent of CEOs believe they have insurance cover for cyber attack, but only 10 percent actually do.⁵³

THE LONDON MARKET IS THE
#1 HUB
FOR SPECIALTY
COMMERCIAL RISKS



THE LONDON MARKET'S COSTS ARE
**9 PERCENTAGE
POINTS**
HIGHER THAN ITS PEERS



⁴⁵ London Market Group and Boston Consulting Group, London Matters: The competitive position of the London insurance market, November 2014

⁴⁶ London Market Group and Boston Consulting Group, London Matters: The competitive position of the London insurance market, November 2014

⁴⁷ Aon Benfield, Reinsurance Market Outlook, January 2016

⁴⁸ Risk Management Association, as quoted in London Market Group and Boston Consulting Group, London Matters: The Competitive position of the London insurance market, November 2014

⁴⁹ California Civil Code S.B. 1386

⁵⁰ Financial Times, Beazley and Munich Re join up in cyber push, 11 April 2106

⁵¹ Fortune, Lloyd's CEO: Cyber attacks cost companies \$400 billion every year, 23 January 2015

⁵² HM Government & Marsh, UK Cyber Security: The role of Insurance in Managing and Mitigating the Risk, March 2015

⁵³ TheCityUK & Marsh, Cyber and the City: Making the UK financial and professional services sector more resilient to cyber attack, May 2016

Longevity risk is another growing concern for governments, pension funds and annuity writers, amid estimates that the aggregate expenses of the elderly will double between 2010 and 2050.⁵⁴

At the same time, the UK is strengthening insurer capital. The Insurance Linked Securities (ILS) Taskforce is devising a strategy to attract more ILS vehicles to the UK. We encourage ongoing efforts to structure a tax and regulatory regime for ILS and assess the potential of a secondary market.⁵⁵

The UK should build on this positive momentum to accelerate insurance market innovation and sharpen its value proposition for emerging risks. Specific actions to accelerate innovation in the London insurance markets include:

• **Building capabilities in non-life insurance to enable corporates to better address emerging risks:**

- Building on existing initiatives to raise awareness of cyber risk by making the completion of Cyber Essentials a standard procurement requirement for industry and Government, encouraging the adoption of cyber standards in credit and investment decisions⁵⁶ and promoting reporting of cyber breaches.
- Taking the lead in developing products for other emerging risks (e.g. indemnification for reputation loss, corporate giga liability loss, catastrophe bonds for climate and weather-related risks) through enhanced data and analytics capabilities.

• **Improving the cost competitiveness of the London Market** building on existing measures (e.g. shared services, improved market infrastructure for claims payment and speed of placement).⁵⁷

- **Developing expertise in managing global longevity risk** by establishing a “Lloyds-like” specialist centre and creating public datasets to support advanced models (e.g. anonymised health records including lifespan and genetic information).
- **Identifying and shaping market expertise to develop innovative products in new market segments** (e.g. Islamic insurance).

EXHIBIT 16

Overview of insurable corporate risks



SOURCE: Aon Benfield, Global Insurance Market Opportunities: Insurance risk study, Tenth edition, 2015; interviews

⁵⁴ United Nations statistics, as quoted in Guy Carpenter, A clearer view of emerging risks, September 2015

⁵⁵ Financial Times, London seeks insurance-linked securities business, 1 March 2016

⁵⁶ TheCityUK & Marsh, Cyber and the City: Making the UK financial and professional services sector more resilient to cyber attack, May 2016

⁵⁷ London Market Group and Boston Consulting Group, London Matters: The competitive position of the London insurance market, November 2014

3.3 Revitalise the market for infrastructure finance and advisory services through new standards, partnerships and structures

Global demand for infrastructure is projected to reach over \$90 trillion by 2030, almost doubling the estimated \$50 trillion value of existing infrastructure globally.⁵⁸ This includes the investment premium for green infrastructure in support of global targets for low-carbon growth.⁵⁹ Green finance itself is an example of an area in which the UK can capitalise on its clusters of FRPS expertise to enhance its leading global role. Since the financial crisis it has become more difficult for the public sector to provide financing. Government's ability to invest in infrastructure has been restricted by rising debt levels and pressure on spending. Similarly, public utilities have less capacity to raise financing. European utilities have lost \$500 billion of market capitalisation since the crisis.⁶⁰

Infrastructure investment offers stable and predictable long-term returns that make it a natural fit for pension liabilities. Further, returns from infrastructure may involve inflation protection and exhibit low sensitivity to swings in the broader economy and capital markets.⁶¹

However, structural obstacles limit the potential of infrastructure financing:

- **Shortage of bankable projects.** Many infrastructure projects do not offer sufficient risk-adjusted returns.⁶² The most accessible lever to address that issue is better project preparation to ensure financial, legal, technical and environmental feasibility.⁶³
- **High development and transaction costs.** There are no international or consistent standards for infrastructure project development. Standardising legal, financing and project planning would significantly reduce costs and improve access.
- **Lack of readily available data.** There is a lack of high-quality data on infrastructure investments, even in developed markets such as the EU.⁶⁴ Global datasets on infrastructure projects and their historical performance would address the issue and reduce reliance on sovereign risk ratings, which tend to restrict access to debt financing for projects in emerging markets.

GLOBAL DEMAND FOR INFRASTRUCTURE
IS PROJECTED TO REACH

**OVER \$90
TRILLION**

BETWEEN NOW AND 2030



SPENDING ON INFRASTRUCTURE CURRENTLY
AMOUNTS TO \$2.7 TRILLION A YEAR, YET

\$3.7 TRILLION
IS NEEDED



⁵⁸ McKinsey Center for Business and Environment, Financing change: How to mobilize private-sector financing for sustainable infrastructure, January 2016; New Climate Economy, Better Growth, Better Climate, 2014

⁵⁹ Global Commission on the Economy and Climate, as quoted in McKinsey Center for Business and Environment, Financing change: How to mobilize private-sector financing for sustainable infrastructure, January 2016

⁶⁰ World Economic Forum, How can we close the green infrastructure gap?, 6 May 2015

⁶¹ Bank for International Settlements, Understanding the challenges for infrastructure finance, August 2014

⁶² Preqin Investor Interviews, as quoted in UK Department for International Development (DFID), International Capital Flows to Infrastructure in Sub-Saharan Africa and South Asia, August 2015

⁶³ World Economic Forum & Boston Consulting Group, Africa Strategic Infrastructure Initiative: A Principled Approach to Infrastructure Project Preparation Facilities, June 2015

⁶⁴ UK Department for International Development (DFID), International Capital Flows to Infrastructure in Sub-Saharan Africa and South Asia, August 2015

- **Lack of transparency on existing projects.** Governments either do not have long-term infrastructure plans, or do not clearly communicate project pipelines – only half of the major economies in the G20 publish infrastructure pipelines.⁶⁵ A global pipeline for infrastructure projects would enable greater investor participation and help position the UK FRPS industry at the centre of the activity.

The UK can take global leadership in infrastructure financing and advisory services. We have decades of experience structuring, financing and advising complex infrastructure projects, and our National Infrastructure Plan is exemplary.⁶⁶ The opportunity is supported, among others, by the consolidation of local authority pension funds.⁶⁷

Infrastructure financing and advisory services are global markets, with around 60 percent of demand expected to come from emerging markets between now and 2030.⁶⁸

Other countries are taking steps. Most notably, Canada and Australia have established private capital markets for infrastructure investment. Four of the five pension funds with the largest unlisted infrastructure equity are Canadian and Australian.⁶⁹ Canada has also recently established Convergence, a blended finance platform that matches private sector investors with infrastructure projects in emerging markets.⁷⁰

Specific actions to revitalise the global market for infrastructure financing and advisory services include:

- **Fostering industry cooperation** (e.g. establishing an industry-wide body, supporting international bodies like the B20, Global Infrastructure Hub and International Infrastructure Support System) **to export UK infrastructure expertise and grow the global pipeline of bankable infrastructure projects**, including:
 - Exploring cost-efficient ways to provide legal, financial, management and technical expertise (e.g. infrastructure centre of excellence in collaboration with universities) to projects in the preparation phase, particularly in emerging markets.
 - Establishing legal, financial, management and technical standards for infrastructure projects that could be replicated across geographies.
 - Developing advanced risk assessment techniques for infrastructure projects globally, utilising comprehensive datasets and analytics.
 - Publishing a global pipeline of infrastructure projects.
- **Encouraging innovation in financing markets** (similar to yieldcos)⁷¹ that address the illiquidity and risks of infrastructure investments and encourage greater investor participation, especially from smaller funds and other institutional investors with low exposure to infrastructure assets.
- **Exploring the potential for a secondary market for infrastructure-related securities** to improve liquidity, reduce transaction costs and increase familiarity with the asset class.
- **Continuing to work with policymakers to engage with other public sector bodies in infrastructure globally.**

⁶⁵ McKinsey Center for Business and Environment, Financing change: How to mobilize private-sector financing for sustainable infrastructure, January 2016

⁶⁶ British Bankers' Association & KPMG, Financing the UK's infrastructure needs, February 2015

⁶⁷ Financial Times, Seven British wealth funds planned, 21 February 2016

⁶⁸ McKinsey Global Institute, as quoted in McKinsey & Company, The infrastructure conundrum: Improving productivity, July 2015

⁶⁹ OECD, Annual Survey of Large Pension Funds and Public Pension Reserve Funds, 2015

⁷⁰ KPMG, Public Private Partnerships: Emerging global trends and the implications for future infrastructure development in Australia, June 2015; The Economist, Trending: blending, 23 April 2016

⁷¹ Yieldcos separate operating assets with stable cash flows (e.g. operating wind farm) from higher-risk activities (e.g. construction) and pool projects to allow institutions to diversify their investments

3.4 Preserve UK leadership in investment management and encourage new forms of advice (e.g. robo-advice), despite the uncertain outlook

The investment management sector globally is forecast to grow 6 percent annually over the next five years, driven by an ageing population and the rise of the middle class in emerging markets.⁷² The UK is the second largest source of conventional funds globally (behind the US), and the leading global centre for fund management on behalf of overseas clients, who provide 30 to 40 percent of funds.⁷³ Significant work has also been done to increase the UK's attractiveness as a fund domicile (e.g. abolition of Schedule 19 stamp duty, launch of Tax Transparent Fund) and consolidate the £200 billion local authority pension system, combining 89 local authority pension plans in England and Wales into eight.⁷⁴

Brexit is likely to have less of an impact on investment management than on some other financial services sub-sectors. Many investment managers who operate across the EU have a UK fund range for sale to UK domestic investors and a fund range based elsewhere in the EU for sale to other EU investors. EU law also has a range of provisions which allow

managers from outside the EU to manage the assets of funds and other clients.

For investment advisers in the retail space, evolution of business models to provide consumers with affordable financial advice could be a consideration. The Financial Advice Market Review acknowledged a substantial advice gap; around half of consumers find pensions difficult to understand⁷⁵ and only 14 percent are confident planning and investing for retirement,⁷⁶ yet less than a third obtain financial advice.⁷⁷ Affordability is a key driver, with 43 percent of advisers turning away clients due to high cost-to-serve.⁷⁸ Robo-advice can potentially help address the gap; in the US, there are 200 such platforms.⁷⁹

Specific actions to deepen UK leadership in investment management include:

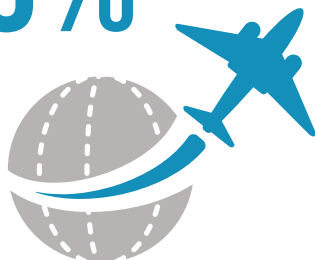
Enhancing the international standing of the UK's investment management sector:

- Working with regulators in other countries to promote UK structures, addressing the FATCA 30 percent withholding tax that limits access to the US and promoting fund recognition in emerging markets.

OVERSEAS CLIENTS PROVIDE

30-40%

OF FUNDS MANAGED BY
UK INVESTMENT
MANAGEMENT FIRMS



THE ASSET MANAGEMENT
INDUSTRY GLOBALLY
IS SET TO GROW AT

6%
ANNUALLY
OVER THE NEXT 5 YEARS



⁷² PwC, Asset Management 2020: A Brave New World, 2014

⁷³ TheCityUK, UK Fund Management 2014, September 2014

⁷⁴ Institutional Investor, Britain's Public Pension Plans Hope Bigger Is Better, 7 April 2016

⁷⁵ FCA Consumer Insight Survey & GfK research, as quoted in HM Treasury & Financial Conduct Authority, Financial Advice Market Review: Final report, March 2016

⁷⁶ Aegon research, as quoted in HM Treasury & Financial Conduct Authority, Financial Advice Market Review: Final report, March 2016

⁷⁷ YouGov research, as quoted in HM Treasury & Financial Conduct Authority, Financial Advice Market Review: Final report, March 2016

⁷⁸ Association of Professional Financial Advisers, as quoted in HM Treasury & Financial Conduct Authority, Financial Advice Market Review: Final report, March 2016

⁷⁹ A.T. Kearney, as quoted in Wealth Wizards, Is the UK ready for investment advice given by robots? Robo-advice set to transform how people save, 6 January 2016

– Continuing the Government's strategy to attract significant investors in funds from overseas markets, especially Asia and the Americas.⁸⁰

• **Improving the sector's proposition for UK consumers,** building on consumer protection priorities:

– Developing a 'pensions dashboard'⁸¹ to increase transparency and customer insight.

• **Enabling UK customers to save and invest by accelerating the development of robo-advice solutions,** building on Financial Advice Market Review recommendations.⁸²

– Clarifying regulatory expectations in respect of financial guidance versus advice, particularly in the context of technology solutions.

– Developing a business and regulatory framework to deliver streamlined advice.

– Establishing an Advice Unit within the FCA to help firms develop automated advice models.

• **Establishing ongoing dialogue with the Government and regulators** to develop and maintain an optimal product suite in terms of fund architecture and investment capability.

3.5 Secure London's position as the world's legal capital, and maintain English law as first choice for commercial contracts and disputes as interactions between English and EU law are unwound

The UK legal services sector (second in size only to the US) is the most international legal sector in the world,⁸³ driven by the primacy of English law. Over a quarter of the world's 320 legal jurisdictions are founded on English Common Law principles and 40 percent of governing law in global corporate arbitrations is English law.⁸⁴ The choice of English law for global contracting is partly driven by the UK's reputation as a leading centre for dispute resolution, whether through litigation or arbitration.

In addition to continuously improving the UK's legal infrastructure, the industry and the Government should work together to maintain the primacy of English law as the choice for commercial contracts globally. As part of this effort, the UK should ensure that English law is highly interoperable with other legal jurisdictions. This is especially relevant for emerging markets, where there is the opportunity to cooperate with legal systems as they evolve and become more international.

Specific actions include:

- Focusing innovation and infrastructure investment in areas that would reduce the cost and improve the speed of dispute resolution (e.g. utilising world-class IT systems and paperless processes, including around low-cost automated disclosure), court structures and processes.
- Exploring collaboration between arbitral organisations and the judiciary.
- Partnering with Government to export UK legal and regulatory standards to emerging markets, which will also facilitate trade and investment.
- Ensuring a focus on legal services in key opportunities to reduce overseas barriers to trade, including in TiSA, developed and emerging market negotiations.

⁸⁰ HM Treasury, Financial Services Trade and Investment Board: Annual report 2014-2015, March 2015

⁸¹ HM Treasury & Financial Conduct Authority, Financial Advice Market Review: Final report, March 2016

⁸² HM Treasury & Financial Conduct Authority, Financial Advice Market Review: Final report, March 2016

⁸³ TheCityUK, UK Legal Services 2016: Legal Excellence, Internationally Renowned, July 2016

⁸⁴ Queen Mary University of London, 2015 International Arbitration Survey: Improvements and Innovations in International Arbitration, 2015



4. INNOVATE, DISRUPT, SCALE

The UK is an innovation centre in banking, but FinTech funding gaps remain versus the US. More worryingly, Brexit may have an impact on the growth of FinTech.

Still, the UK has the potential to become a dynamic technology centre across the FRPS industry, fostering technologies that will open up opportunities to engage differently with customers and employees, radically reduce costs, and enable entirely new business models.

4.1 Diversify and scale FinTech, broadening the UK's leadership position into insurance and professional services and securing EU market access for high-growth firms

Recognising the role of HM Treasury and the FCA in fostering a favourable environment for technological innovation, the UK is well-positioned in FinTech. It has more people working in the sector than New York and more than Singapore, Hong Kong and Australia combined, being home to six of the 31 FinTech 'unicorns' (i.e. FinTechs valued over \$1 billion).⁸⁵ The UK has a receptive policy environment (e.g. FCA's Project Innovate and regulatory sandbox initiatives), attracting early stage funding (through the Enterprise Investment Scheme) and building a

rich FinTech ecosystem. These measures, combined with the UK's traditional strength in financial services, have enabled the UK to grow into the world's largest FinTech market, with a greater market size than each of the leading US FinTech hubs of California and New York (Exhibits 17 and 18).

Scaling could be supported by a clearer industry "playbook" to help young technology firms in FRPS engage with incumbent firms. Most technology firms (around 80 percent in corporate and investment banking) are seeking to collaborate with incumbents rather than disrupt business models.⁸⁶

There is clear potential for the UK to lead innovation beyond the core banking areas of payments, lending and investments. For example, the UK could encourage start-up innovation in areas such as RegTech, insurance (none of the world's leading

EXHIBIT 17

Comparative snapshot of major FinTech markets globally

NOT EXHAUSTIVE

	Market size £ billion	Investment £ billion ¹	FinTech staff Number of people
United Kingdom	6.6	524	61,000
New York	5.6	1,400	57,000
California	4.7	3,600	74,000
Germany	1.8	388	13,000
Australia	0.7	198	10,000
Hong Kong	0.6	46	8,000
Singapore	0.6	44	7,000

¹ Investment refers to the period from October 2014 to September 2015
SOURCE: HM Treasury & EY, UK FinTech: On the cutting edge, 2016

⁸⁵ HM Treasury & EY, UK FinTech: On the cutting edge, 2016

⁸⁶ McKinsey Panorama FinTech

"InsurTechs" are based in the UK),⁸⁷ or in legal services (only 10 percent of the world's ~400 "LegalTech" start-ups are based in the UK).⁸⁸

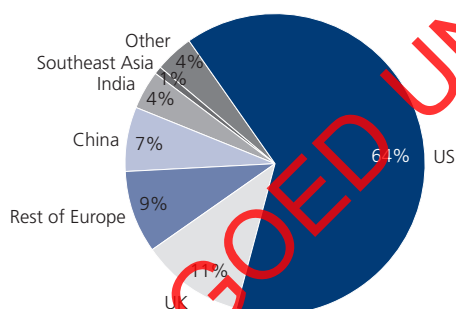
Specific actions to diversify and scale up the UK FinTech industry include:

- **Increasing "growth capital" funding** (i.e., £5-100 million) by:
 - Building UK capabilities in VC and encouraging corporate VC activity.
 - Increasing investment thresholds in existing tax initiatives, such as the Enterprise Investment Schemes and Venture Capital Trusts.
 - Promoting (and potentially simplifying) AIM listings on the London Stock Exchange.

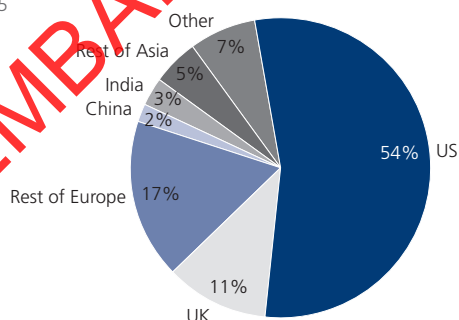
EXHIBIT 18

The UK accounts for ~11% of global Fintech investment activity

Share of global FinTech investment
Cumulative investment, 2010-mid 2015¹



Total number of FinTech deals globally
2015



¹ Measures cumulative FinTech investment between January 2010 and June 2015, as presented at FinTech Week London (14-20 September 2015)
SOURCE: IC Dowson and William Garrity Associates, Pitchbook

- Conducting further research to identify gaps and measures to embed potential investors in the FinTech ecosystem.

• **Building on the FCA's reputation as one of the most progressive regulatory environments for FinTech:**

- Ensuring equal access and scalable regulatory approaches.
- Adding resources to Project Innovate and the regulatory sandbox.
- Exploring options to expand the regulatory sandbox mandate to provide a 'safe harbour'⁸⁹ for innovative firms.
- Simplifying the authorisations process.
- Supporting the development of RegTech start-ups by clarifying standards and supporting a service framework that would facilitate adoption of RegTech solutions.

• **Expanding opportunities overseas for UK-based companies:**

- Building trade and investment opportunities with priority markets.
- Creating a college of international regulators to explore best practice and promote regulatory coherence across borders.

• **Increasing support for technological innovation in FRPS more broadly** (e.g., insurance, legal services, accounting) through dedicated outreach by Government and industry, including a clear "interoperability playbook", with a focus on customer access and consideration of the Government as a customer.

• **Working with Government and Office for National Statistics to improve data availability** for start-ups and firms developing innovative products.

GLOBAL FINTECH FINANCING HAS RISEN SEVEN-FOLD OVER THE PAST THREE YEARS TO

**~\$20_{BN}
FOR 2015**



⁸⁷ KPMG & H2 Ventures, FinTech 100: Leading Global FinTech Innovators Report 2015, 2015

⁸⁸ The Law Society Gazette, Legal tech: easing the pain-points, 15 February 2016

⁸⁹ NOTE: 'Safe harbour' would shield innovative firms from non-compliance penalties for a period of time.

4.2 Develop large-scale innovation ecosystems across financial and professional services (e.g., blockchain, IoT, data, telematics, cognitive analytics, cyber)

In addition to facilitating the kind of “bottom-up” innovation that is often driven by smaller FinTech firms, the UK FRPS industry can act collectively on major industry disruptions. Blockchain, the Internet of Things, and telematics are examples, but there is a broader need to identify and respond to industry-shaping waves of innovation.

The UK industry and Government should develop joint action plans to encourage innovation and link industry experimentation with existing Government initiatives.

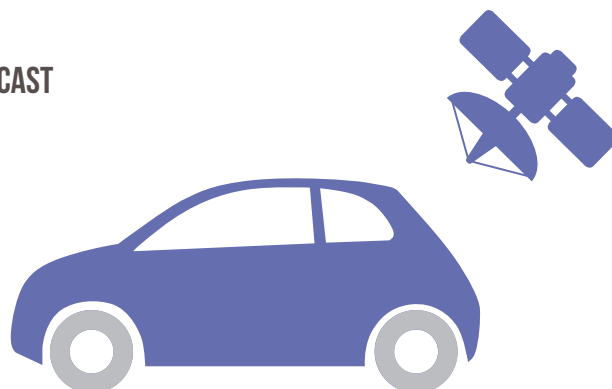
Specific actions to strengthen the UK’s innovation platforms in blockchain, IoT and telematics include:

- **Building on existing efforts to support distributed ledger experimentation** through industry sponsored research, joint Government and industry pilots, developing a legal and regulatory framework, address ambiguities around security and privacy and cultivate talent (particularly in trading, administration and legal treatment of distributed ledgers).
- **Commercialising the Internet of Things for FRPS firms** by facilitating the adoption of IoT technologies and services, exploring how IoT enables improved underwriting and pricing in insurance (including through shared or public datasets, industry pilots and sponsored research) and elevating cyber security standards to address potential risks.
- **Fostering industry cooperation to grow the UK telematics insurance market** by promoting telematics equipment, testing sensor and transmission technology to collect customer data, and exploring partnerships with digital players to develop interfaces.

TELEMATICS EQUIPMENT IS FORECAST
TO REACH PENETRATION OF

98%

OF NEW VEHICLES IN
EUROPE BY 2020



4.3 Foster cooperation and create the regulatory framework for the next wave of industry utilities (e.g., cyber risk, anti-money laundering (AML), market and reference data) in the UK and attract participation from EU FRPS firms

Industry utilities pool costs, and enable greater economies of scale, helping firms switch from a capital expenditure model to pay-as-you-go, and creating greater flexibility in scaling up and down.

Post-crisis, many FRPS firms have squeezed efficiency levers (especially in financial services). Utilities can provide an additional wave of cost savings (conservatively estimated at 20 to 30 percent depending)⁹⁰ and improvements in agility.

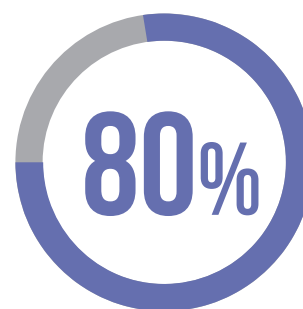
In addition, just under 80 percent of financial services professionals cite managing regulatory change as a significant driver of utility uptake.⁹¹ In a world in which regulatory change receives a large share of industry investment, utilities could drive consistency in service delivery, improve service quality and reduce operational failures and exceptions. That would in turn reduce the risk of fines, minimise reputational damage and enable sharing of regulatory compliance costs.

The UK can establish itself as home for future services of this type, enabling it to capture business opportunities and have greater influence over the industry's future "building blocks". Establishing global industry utilities could sharpen the value proposition of regional FRPS centres and provide additional sources of FRPS employment.

Specific actions to establish the next wave of industry utilities include:

- **Taking the lead globally to define regulatory standards promoting the use of industry utilities**, addressing process and service standardisation, data privacy and security, accountability and reporting and supervision models.
- **Mobilising UK-based FRPS firms to jointly explore opportunities for industry utilities** in areas with significant cost reduction potential and utility maturity, such as market and reference data, cloud services, IT applications, reconciliation and exception management.⁹²
- **Partnering with the Government and regulators** to establish industry utilities in priority areas of regulatory compliance, such as cyber risk, anti-money laundering and financial crime.

73%
OF BANKING PROFESSIONALS ARE
CONSIDERING OR PLANNING ADOPTION OF A
MARKET AND REFERENCE DATA UTILITY

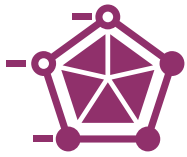


**80% OF FINANCIAL SERVICES
PROFESSIONALS CITE
MANAGING
REGULATORY CHANGE
AS A SIGNIFICANT DRIVER OF UTILITIES UPTAKE**

⁹¹ Capco & Finextra, What Makes Utilities Useful?, February 2016

⁹² Capco & Finextra, What Makes Utilities Useful?, February 2016

⁹³ Capco & Finextra, What Makes Utilities Useful?, February 2016



5. BUILD SKILLS AND ATTRACT TALENT

The UK is first for financial and related professional talent globally,⁹³ but faces shortages in diverse profiles and next-generation skills, with Brexit potentially amplifying the trend. The UK can therefore nurture a more diverse workforce that leads the world in combining financial, professional and technology skills.

5.1 Agree approach to retention, sourcing and movement between the EU and the UK of high quality talent working in FRPS

The economic contribution of European immigrants is significant. Between 1995 and 2011, migrants from the EU made a net positive contribution to the British public finances of over £4 billion.⁹⁴ That contribution continued even during the worst years of the financial crisis. Free movement of high quality talent is important to London's prospect of maintaining and improving its position as a leading financial centre.

5.2 Ensure that the UK immigration system facilitates access to top global FRPS talent for next-generation skills (e.g. data science, artificial intelligence, cyber security) and strategically important partners (e.g. US, China, India)

To maintain the UK's pre-eminence in FRPS and deliver on strategic priorities we must access the world's best talent.

As an example, over 40 percent of Silicon Valley technology workers are born overseas, and 44 percent of Silicon Valley start-up founders between 2005 and 2012 came from overseas; nearly half from India and China.⁹⁵

The UK has started to address barriers to accessing highly skilled talent:

- The Tech Nation Visa Scheme provides 200 Tier 1 Exceptional Talent visas per year to technology experts, entrepreneurs

UK COMPANIES WITH 10 PERCENT HIGHER GENDER AND ETHNIC/RACIAL DIVERSITY ON MANAGEMENT TEAMS AND BOARDS HAVE

5.8%
HIGHER EBIT ON AVERAGE



WOMEN MAKE UP
ONLY 14%
OF EXECUTIVE COMMITTEES
AND 23 PERCENT OF BOARDS
IN THE UK FINANCIAL
SERVICES INDUSTRY



⁹³ Deloitte, London Futures – Globaltown: Winning London's crucial battle for talent, November 2013

⁹⁴ The Economist. What have the immigrants ever done for us? November 2014

⁹⁵ Vivek Wadhwa, AnnaLee Saxenian, Francis Daniel Siciliano II and Ewing Marion Kauffman Foundation, Then and Now: America's New Immigrant Entrepreneurs, Part VII, 1 October 2012

and start-up employees (although concerns remain that the scheme applies only to a subset of digitally skilled workers).⁹⁶

- The Graduate Entrepreneur visa allows graduates from outside the EU to pursue business ideas in the UK.
- Government has simplified documentation requirements for Graduate Entrepreneur visa applicants using funds provided by authorised public sources (e.g. UK government, devolved Government departments, seed funding competitions).⁹⁷
- The Government has left visa grants under the Tier 2 Intra Company Transfer route uncapped.
- The Government has revised monthly caps of restricted certificates of sponsorship to better reflect seasonal demand for visas and address the large number of refusals in June–October 2015 (Exhibit 19).

Immigration policy must take account of a wide range of complex factors. However, there are opportunities to help the industry attract the world's best talent and address skills gaps. Currently, start-ups, SMEs and firms outside the capital are more heavily impacted by immigration restrictions:

- Start-ups and SMEs are expected to face increasing difficulties recruiting talent due to the rise in the salary threshold for experienced workers under Tier 2 General visas to £25,000 and the new £35,000 salary requirement to remain in the UK indefinitely.⁹⁸ FinTech start-ups are also

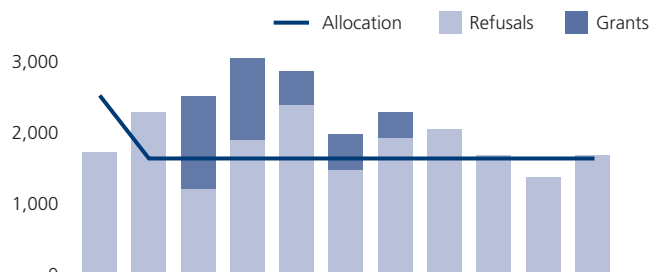
calling for the inclusion of technology talent on the Shortage Occupation List for Tier 2 visas and a foreign technology students' visa scheme to enable UK-qualified graduates to join the UK workforce.⁹⁹

- FRPS firms outside London and the South East are likely to find it increasingly difficult to recruit migrant talent as a result of the announced salary threshold increases. There are significant differences in salaries between London and the rest of the country – the average salary for skilled jobs

EXHIBIT 19

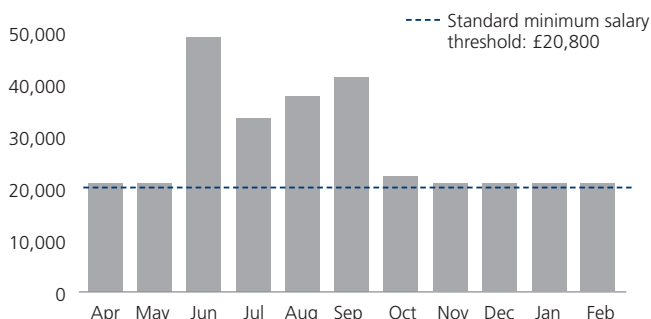
Allocations, grants and refusals of restricted certificates of sponsorship between June–October 2015

Monthly allocation, grants and refusals¹ of Restricted Certificates of Sponsorship for Tier 2 (General) visas, 2015/16



Minimum salary needed for a successful Tier 2 (General) visa application, 2015/16

(GBP)



¹ The number of grants and refusals in a given month may be above or below the initial allocation due to the balance from the previous month carrying over to the next
SOURCE: Gov.uk; Migration Advisory Committee

**MIGRANTS FROM THE EU MADE
A NET POSITIVE CONTRIBUTION
TO BRITISH PUBLIC FINANCE OF
MORE THAN
£4 BILLION
BETWEEN 1995 AND 2011**



⁹⁶ HM Treasury & EY, UK FinTech: On the cutting edge, 2016

⁹⁷ UK Visas & Immigration, Tier 1 (Entrepreneur) of the Points Based System – Policy Guidance, April 2016

⁹⁸ Institute of Directors submission to Migration Advisory Committee, Call for evidence: Tier 2 route, 17 August 2015; Universities UK submission to Migration Advisory Committee, Call for Evidence on Minimum Salary Thresholds for Tier 2, 3 July 2015; Forbes, Thanks For The Taxes, Now Leave: £35k Salary Requirement Hurting UK Startups, 28 March 2016

⁹⁹ HM Treasury & EY, UK FinTech: On the cutting edge, 2016

in London is over £15,000 above the average in Wales and Northern Ireland (Exhibit 20).

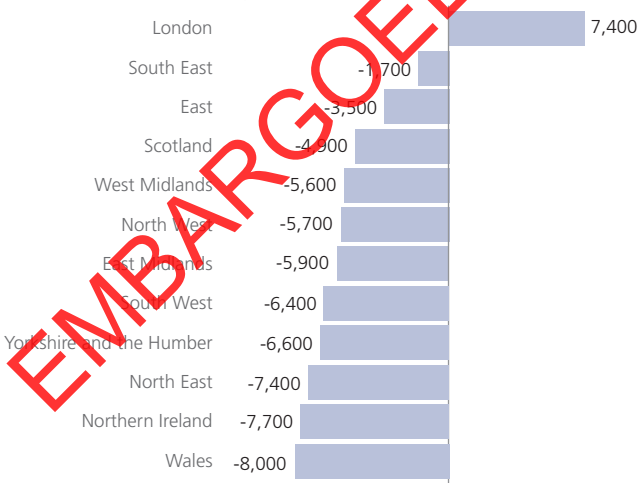
Specific actions to increase the use and usability of skilled immigration channels include:

- **Ensuring the industry fully uses the current system**, including taking better advantage of the uncapped Intra Company Transfer visa route.
- **Pursuing targeted immigration reforms to stimulate growth sectors:**
 - Including technology talent, such as coders and software developers, on the Shortage Occupation List for Tier 2 visas.¹⁰⁰
 - Reducing visa restrictions for entrepreneurs and foreign STEM and ICT students, (e.g. by allocating additional points in the skilled migration test).¹⁰¹
 - Revising salary thresholds for start-ups¹⁰² and firms outside London and the South East.¹⁰³
 - Enabling Local Enterprise Partnerships and Venture Capital Trusts to become Tier 2 visa sponsors.

EXHIBIT 20

Average salaries for skilled jobs in London are significantly higher than elsewhere in the UK

Regional differences in the mean wage for MQ6+ occupations
Difference from mean UK wage



SOURCE: Migration Advisory Committee

5.3 Build next-generation skills, particularly in technology, through industry collaboration, apprenticeships and schools and universities

The challenge of nurturing next-generation digital skills goes beyond the FRPS industry, and work is underway in the form of new institutions like the National College for Digital Skills and youth programmes like coding clubs (e.g. CodeClan in Scotland). Activities are taking place at Government, regional, local and third sector levels (Exhibit 21).

The FRPS industry needs to be at the forefront of these efforts. The shortage of technologically skilled workers is likely to hit the industry particularly acutely, given the rapid pace and broad impact of technological innovation in FRPS. Also, the industry needs to ensure that talent sees FRPS as a natural place to apply and hone technology skills.

The FRPS industry can partner with schools, universities and other educational institutions to develop next-generation skills by:

1. *Broadening its offering of apprenticeships and research projects* (e.g. with data scientists in PhD programmes). We start from a position of strength. Six of the top 10 apprenticeship employers in the UK today are FRPS firms, and FRPS is likely to remain a key participant in the new apprenticeship scheme set to be introduced next year.¹⁰⁴ FRPS can also build on recent Government efforts to increase the number of quality digital apprenticeships by clarifying standards for digital roles and expanding the Tech Industry Gold Apprenticeship scheme.¹⁰⁵
2. *Developing industry-specific qualifications and curricula* in collaboration with universities and higher education providers. Developing qualifications for emerging FRPS areas of competence (e.g. digital banking, conduct risk, regulatory compliance) will enable FRPS firms to secure the right talent more easily and allow the UK to export standards. The launch of a new postgraduate qualification in Central Banking and Financial Regulation at Warwick Business School, developed in partnership with the Bank of England, is a step in the right direction.¹⁰⁶

¹⁰⁰ HM Treasury & EY, UK FinTech: On the cutting edge, 2016

¹⁰¹ HM Treasury & EY, UK FinTech: On the cutting edge, 2016

¹⁰² Kingsley Napley, Kingsley Napley LLP's Response to Migration Advisory Committee's Call for Evidence on the Review of the Tier 2 Minimum Salary Thresholds, July 2015

¹⁰³ Migration Advisory Committee, Review of Tier 2: Balancing migrant selectivity, investment in skills and impacts on UK productivity and competitiveness, December 2015

¹⁰⁴ RateMyApprenticeship.co.uk, Top 60 employers 2015-2016 (Note: EY, Fidelity, J.P.Morgan, Lloyds Banking Group, M&G Investments and PWC are the 6 FRPS employers in the top 10)

¹⁰⁵ Department for Business Innovation & Skills and Department for Culture Media & Sport, Digital Skills for the UK Economy, January 2016

¹⁰⁶ Bank of England, News Release – The Central Banking Qualification: training the central bankers of the future, 12 February 2016

Successful delivery will require a step change in focus and resourcing, as well as a preparedness to act collectively. Specific actions to build next-generation skills include:

- **Forging links with educational institutions in emerging technology clusters** (e.g. Manchester for computing) or **technology-related initiatives** (e.g. National College for Digital Skills, Tech Partnerships, Digital Catapult Centre) to ensure educational programmes offer FRPS modules and apprenticeships.
- **Partnering with universities and higher education providers to develop industry-specific qualifications and curricula paired with apprenticeship training**, focusing on technology areas (e.g. cyber security, data sciences) and emerging FRPS themes (e.g. digital banking, conduct risk).
- **Developing apprenticeships and on-the-job-training for secondary school graduates**, as an alternative to university degrees where appropriate.
- **Ensuring that primary and secondary school curricula help students develop digital and mathematics skills** required for FRPS degree programmes, apprenticeships and on-the-job training.
- **Working with technology-led institutions** (e.g. Tech City UK, Coadec) to understand and address FRPS-specific issues that impact skills shortages.
- **Fostering industry cooperation to improve the industry's employee value proposition for millennial talent**

EXHIBIT 21

Examples of existing initiatives to build digital skills across the UK

Government initiatives

- **Degree apprenticeships:** Over 300 degrees launched across 9 universities to enable young people to obtain integrated computer science degrees and job training
- **National College for Digital Skills:** Newly established sixth form college that will provide programming training and higher level apprenticeships
- **Digital Business Academy:** Free online training platform designed to teach digital business skills (e.g. establishing a start-up, developing digital products)
- **Small Business Digital Capability Programme:** Initiative to help SMEs acquire digital skills

Regional initiatives

- **CodeClan:** Digital skills academy to develop a talent pipeline of qualified software developers for Scottish businesses
- **Manchester Digital:** Initiatives supporting businesses to develop digital skills (e.g. apprenticeship matching service, continuous professional development)
- **Dynamo North East:** Initiatives supporting employers and talent in promoting digital apprenticeships, running coding clubs, and supporting digital programmes in educational institutions

Digital skills building initiatives

Local initiatives

- **North East Tech Skills Hub:** Sunderland-based collaboration between schools and small businesses to improve teachers' digital skills and introduce students to career opportunities in digital
- **Better Broadband for Oxfordshire:** Project helping women who are running small businesses or returning to the workforce to improve digital skills
- **Software Cornwall:** Programme to nurture talented developers and attract new skilled digital workers to the region

Third sector initiatives

- **School and Business Partnership:** Initiative to encourage more girls to study STEM subjects
- **X-Forces:** Social enterprise supporting military personnel leaving the armed forces to acquire digital skills upon reentry to the labour market
- **Digital Outreach:** Capability building programme offering digital skills training and support to micro- to medium-sized voluntary and community organisations

5.4 Collectively promote diversity through industry-sponsored schemes

Better diversity across FRPS is a vital component of expanding the talent pool and improving perceptions of FRPS.

Research shows that companies that commit to enhancing diversity are more successful, and a diverse and inclusive workplace is an important part of attracting and retaining talent.¹⁰⁷ UK companies with 10 percent higher gender, ethnic and socio-economic diversity on management teams and boards have EBIT¹⁰⁸ that is close to 6 percent higher on average.¹⁰⁹ The Government estimates that female professional equality could add ~£600 billion to the UK economy.¹¹⁰

Given the growing body of evidence suggesting a strong link between diversity and performance, there is a clear opportunity for the UK FRPS industry:

- Women make up 14 percent of executive committees and 23 percent of boards in the UK financial services industry.¹¹¹ Only one in five partners in top 20 UK law firms is female, despite more women now entering the profession than men.¹¹²
- Black, Asian, and minority ethnic groups hold less than a quarter of management positions in financial services.¹¹³ Less than 6 percent of UK law firm partners are from an ethnic minority background.¹¹⁴
- People from disadvantaged socioeconomic backgrounds are a small subset of employees in FRPS firms. Up to 70 percent of job offers by leading accountancy firms are made to graduates educated at selective state or fee-paying schools, which educate only 11 percent of the population. Similarly, in legal services, close to 40 percent of graduate trainees are educated at fee-paying schools, which educate only 7 percent of the population.¹¹⁵

The industry faces perception issues that may hurt its credibility with women and minorities – two-thirds of banking-oriented students globally do not associate banking with acceptance towards minorities, and only 38 percent think that banks support gender equality.¹¹⁶

Acknowledging these challenges, the UK FRPS industry has been at the forefront of efforts to improve diversity in the workplace. For example, the 30% Club has helped grow the share of women on FTSE 100 boards from 12.5 percent in 2010 to 26 percent (and rising).¹¹⁷ The recent launch of HM Treasury's 'Women in Finance Charter' aims to address the industry's gender imbalance.¹¹⁸

There has also been successful sector-specific work. Leading UK law firms set up PRIME, a diversity access scheme providing state school children aged 14-18 from disadvantaged backgrounds with legal work experience.¹¹⁹ Investment 2020 is an established programme that offers traineeships in investment management to people from diverse educational and social backgrounds.

Still, there are specific actions that could promote talent diversity:

- **Investigating and addressing barriers to career progression** for women, minorities and other diverse profiles.
- **Sponsoring diversity schemes**, including increasing awareness about opportunities and an expansion of apprenticeships, temporary placements and sector-wide graduate programmes.
- **Reviewing recruitment criteria and strategies to appeal to a larger and more diverse graduate base** through collaboration with colleges, universities and other educational institutions.
- **Supporting research into underlying causes of shortfalls in diversity in the workplace.**

¹⁰⁷ Oliver Wyman, Women in financial services, December 2014

¹⁰⁸ Earnings before interest and taxes

¹⁰⁹ McKinsey & Company, Diversity Matters, 2 February 2015

¹¹⁰ Government Equalities Office, Government funds new speed mentoring events for female entrepreneurs to nurture talent across the nation, 17 August 2015

¹¹¹ HM Treasury & Virgin Money, Empowering Productivity: Harnessing the Talents of Women in Financial Services, March 2016

¹¹² LexisNexis Blog, Women in law: What needs to change, 22 February 2016

¹¹³ Business in the Community, Race to the Top: The place of ethnic minority groups within the UK workforce, 2009

¹¹⁴ 2014 BSN Diversity League Table, quoted in The Law Society Gazette, Diversity quotas in the law – the issues, 6 November 2014

¹¹⁵ Social Mobility & Child Poverty Commission, A qualitative evaluation of non-educational barriers to the elite professions, June 2015

¹¹⁶ Deloitte Talent in Banking Survey, Graduate recruitment in banking: Facing the credibility crunch, 2014

¹¹⁷ 30 percent Club website

¹¹⁸ HM Treasury, Women in Finance Charter: a pledge for gender balance across financial services, 8 April 2016

¹¹⁹ PRIME profile on LawCareers.net website

6. REINFORCE UNIQUE FOUNDATIONS

The five pillars must be built on the solid foundation of a future-proof client base and close dialogue and cooperation with policymakers under a post-Brexit reality.

6.1 Retain and expand existing UK operations of foreign corporates through proactive outreach campaigns and use of financial and operational incentives

A concrete indicator of the UK's global leadership as an international hub for business is that London has more projects by companies relocating and expanding overseas than any other city (Exhibit 22). London is also home to the second highest number of large corporate headquarters after Tokyo

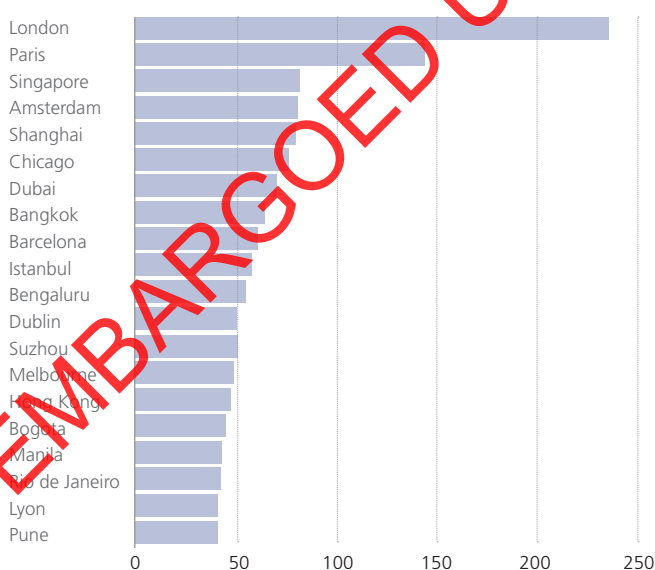
and significantly ahead of Paris, New York and other western centres.¹²⁰ London is the leading location for international company headquarters.

The UK is Europe's business capital. London hosts 40 percent of the 250 largest companies that have global or regional headquarters in Europe, significantly ahead of second place Paris with 8 percent.¹²¹ This strength is also reflected across the rest of the UK, which saw 344 foreign investment projects in 2014, with the South East, Yorkshire, West Midlands, Wales and Northern Ireland performing strongly.¹²² However, the UK's position could be undermined by Brexit arrangements.

EXHIBIT 22

London has more foreign investment projects than any other city globally

Top-ranking cities by projects, 2014



SOURCE: IBM Institute for Business Value, Global Locations Trends: 2015 Annual Report, 2015

6.2 Launch a proactive campaign to attract new FDI to the UK, using a range of incentives

There are huge opportunities for the UK if we can grow our status as a global hub for business in an increasingly globalised world. There will be another ~7,000 companies with \$1 billion revenue or more by 2025, two thirds of which are expected to be based in emerging markets.¹²³

Each of those companies may have a global or regional headquarters that the UK should seek to capture, leading to an associated cascade of FRPS demand. Even among the 50 largest emerging market corporates, there is an opportunity for the UK to grow inward investment – only 18 percent of those companies have their European hub in the UK and 40 percent have not expanded to Europe (Exhibit 23). Beyond headquarters, the UK can seek to capture specialist functions, such as R&D (where FDI has increased by 10 percent annually) or corporate treasuries.¹²⁴

¹²⁰ S&P Capital IQ [Note: Private and public companies with >\$1 billion revenue in 2014. Excludes subsidiaries.]

¹²¹ Deloitte, London Futures: London crowned business capital of Europe, 2014

¹²² EY, Another great year – but time to reflect on how the UK can stay ahead of the pack: EY's attractiveness survey, 2015

¹²³ McKinsey & Company, The family-business factor in emerging markets, December 2014

¹²⁴ UKTI, Inward Investment Report 2014/15, June 2015

Attracting inward investment is not the responsibility of the UK FRPS industry. However, it is a core driver of the industry's growth, and there is significant scope for greater partnership between the industry, Government and regional development bodies.

Specific actions to attract global client businesses to the UK include:

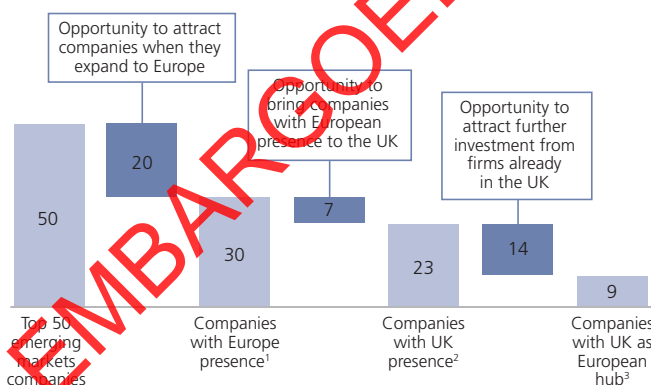
- **Supporting Government efforts to grow incremental inward investment** by firms already in the UK.
- **Supporting Government efforts to identify and attract leading international companies**, especially from emerging markets, to establish regional headquarters or specialised functions (e.g. R&D, corporate treasury) in the UK.
- **Improving the UK's intelligence base on global specialised functions of major corporates** (e.g. locations of biotech R&D and corporate treasury functions) and helping the Government identify additional target segments.

EXHIBIT 23

There is an opportunity for the UK to grow investment from the largest companies from emerging markets

Number of companies

UK presence of the top 50 on the FT Emerging 500 companies list



¹ Companies with at least one registered subsidiary that has its headquarters in Europe (incl. UK) and records positive revenue

² Companies with at least one registered subsidiary that has its headquarters in the UK and records positive revenue

³ Companies whose UK-headquartered subsidiaries record higher revenues than their subsidiaries in any other European country

SOURCE: FT Emerging 500 2015; S&P Capital IQ

6.3 Foster a new level of dialogue between industry, Government and regulators

Delivery of partnership opportunities we have outlined requires continued engagement between the industry, Government and regulators, building on recent positive momentum.

Recent steps include:

- The Financial Services Trade and Investment Board (FSTIB) helped coordinate industry and Government action that led to the UK's renminbi and sukuk bond issuances, advancing the industry's objectives on renminbi internationalisation and Islamic finance and working effectively with the India-UK Financial Partnership.¹²⁵ A renewed Board has identified key areas for future cooperation, with TheCityUK as a major private sector delivery partner – these areas are: insurance, capital markets, investment management, FinTech, China, India and the US.
- The insurance sector collaborated with the Government to launch Flood Re in April 2016, addressing the need for affordable household insurance in flood-prone areas.¹²⁶
- The legal services sector, supported by the Government, has engaged with legal bodies in emerging markets to liberalise laws governing market access for foreign law firms. Liberalisation of the Malaysian legal services sector is a recent example.¹²⁷
- The Bank of England has engaged with the industry in emerging areas of focus, such as cyber resilience.¹²⁸ Similar opportunities for cooperation may exist on stress-testing, as approaches evolve beyond impact on individual firms and towards overall system resilience.
- The FCA has engaged with the industry to stimulate FinTech innovation, most notably by establishing Project Innovate and the 'regulatory sandbox'.

Despite progress, there is a need for ongoing, consistent dialogue between industry, Government and regulators. Specific actions may include:

- **Developing a joint strategic vision** for a growing, stable and resilient UK FRPS industry.
- **Working with Government to pursue joint policy priorities and regulatory coherence in international dialogue**, including at EU and G20 levels.¹²⁹

¹²⁵ HM Treasury, Financial Services Trade and Investment Board: Annual report 2014-2015, March 2015

¹²⁶ The Daily Telegraph, Flood Re: Government insurance scheme launch confirmed for 2016, 8 June 2015

¹²⁷ Foreign & Commonwealth Office, How the UK has helped to liberalise the Malaysian Legal Services Sector for foreign firms, 22 June 2015

¹²⁸ Bank of England, Financial Stability Report, December 2015

¹²⁹ TheCityUK, Investing in Britain's Future, April 2015

6.4 Recast the current approach to Government and regulatory policy design and implementation to be more mindful of international competitiveness

The FRPS industry is emerging from a turbulent period, driven by regulatory change. However, there are continued risks and uncertainties, and increased complexity (e.g. the number of tax reliefs has risen from 1,042 in 2010 to 1,156 in 2016¹³⁰ while the number of new tax measures announced in annual budgets has grown threefold since 2010).¹³¹

The industry's ability to plan for the future has been challenged by an unpredictable policy outlook; recent examples include uncertainty around tax relief on pension contributions and the more restrictive interpretation of Solvency II in the UK than elsewhere.

A more stable and predictable policy environment will be a critical enabler of long term success. The industry can do its part by continuing to rebuild trust and confidence.

Specific actions to enable policy stability include:

- Ensuring efficient machinery of Government changes are made to respond to the Brexit dynamic. This should include drawing on resources and personnel across Government, as well as assessing how external support could help deliver national goals. The industry stands ready to help formulate and determine negotiation strategies, identify priorities and solutions and be active participants.
- **Help the Government and regulators conduct impact assessments,** compliance cost assessments, cost-benefit analyses and post-implementation reviews.¹³²
- **Promote Government consultations** to enable better understanding of potential consequences.¹³³

6.5 Maintain and improve the UK's physical infrastructure and digital connectivity

The UK FRPS industry is dependent on the success of UK business overall. With that in mind, infrastructure (physical and digital) is a critical driver of the UK's attractiveness.

Progress is being made on physical infrastructure, including projects such as HS2, HS3 and Crossrail, and the creation of the National Infrastructure Commission to drive strategy alongside the Infrastructure Projects Authority to oversee delivery. The UK can review EU regulations and directives, for example on procurement, to see how they can be improved, streamlined or scrapped. The Government should continue its push to consolidate local government pension schemes, enabling the new, stronger schemes to acquire the skills and expertise to invest in infrastructure. The pace needs to be maintained and accelerated, particularly on housing, road improvements (particularly in the Northern Powerhouse) and airports.

On the latter, delays to the expansion of air capacity in the South East are a pain point. Heathrow, the UK's busiest airport, is operating at 98 percent of capacity, much closer to capacity than other major European hubs,¹³⁴ while Gatwick, the country's second-busiest airport, is expected to be at capacity by 2020.¹³⁵ Britain trades up to 20 times more with countries with a direct air link and 40 percent of exports travel by air,¹³⁶ suggesting expansion of air capacity in the South East is critical.

Digital connectivity is still patchy, with gaps in fixed and mobile connections across the country (in London around 10 percent of premises lack high speed broadband).¹³⁷ Investment is required to deliver the government's ambition that ultrafast broadband of at least 100Mbps should be available to nearly all UK premises, and there is a risk that by the time that is achieved others will have moved ahead.

Hence, it will be critical to **support the Government's agenda to deliver world class physical infrastructure and digital connectivity across the UK**, as addressed in work by the City of London Corporation,¹³⁸ London First,¹³⁹ Tech City UK¹⁴⁰ and others.

¹³⁰ The Economist, Britain's tax code: Spaghetti junction, 13 February 2016

¹³¹ The Economist, The fiddler's charter, 19 March 2016

¹³² TheCityUK, EU Reform: Detailed proposals for a more competitive Europe, June 2015

¹³³ TheCityUK, Key Facts about UK Financial and Related Professional Services, March 2016

¹³⁴ BBC News, Airport expansion: What happens next?, 1 July 2015

¹³⁵ The Daily Telegraph, Graham Brady: 'Never mind Brexit, we need more runways', 14 February 2016

¹³⁶ Let Britain Fly

¹³⁷ Ofcom UK Fixed Broadband Data 2013, available at <http://maps.ofcom.org.uk/broadband/broadband-data/>

¹³⁸ City of London Corporation, Clusters and Connectivity: The City as a Place for SMEs, March 2016;

City of London Corporation, Future Workstyles and Future Workplaces in the City of London, March 2015

¹³⁹ London First, London 2036: An agenda for jobs and growth, January 2015

¹⁴⁰ Tech City UK, Tech Nation: Powering the Digital Economy, 2015

6.6 Provide a competitive taxation scheme for both businesses and individuals

The more attractive the UK is as a place for clients to locate, for top talent to live, and for businesses to invest, the more it is likely to support a successful FRPS industry. Interviewees highlighted the importance of taxation (both business and personal) as a critical driver of the UK's overall attractiveness to business.

In this regard, the industry has welcomed recent reductions in headline corporate and capital gains tax rates, improving the UK's competitiveness relative to other advanced economies (Exhibit 24). However, concern remains over increases in some non-headline rates of corporation taxation, such as the

announced apprenticeship levy and Immigration Skills Charge. Given that Brexit could add uncertainty to future taxation structures and rates, it is critical that any future tax changes balance fiscal-policy objectives with continued advancement of the UK's competitiveness as a world-leading business hub.

Specific actions to increase UK's taxation competitiveness include:

- Developing cross-sectoral strategic policy priorities on taxation and supporting ongoing Government efforts to simplify the tax code.
- Ensuring stable and predictable taxes despite current uncertainties for both business and individuals.

EXHIBIT 24

Illustrative comparison of top rates of tax across countries

Category	Tax	UK	US	Singapore	HK	France	Germany
Corporate taxes	Corporate tax	20% + 8% ^{2,3}	39% + 7.1% ⁸	17%	16.5%	33.5%	33% ¹²
	Capital gains	20%	39% + 7.1% ⁸	-	-	33.5%	15%
Personal taxes	Income tax (top rate)	45%	52% ⁶	20% ⁹	17%	45%	47.475% ¹³
	Capital gains	20% ⁵	20% ⁷	-	-	45%	26.375% ¹⁴
Consumption taxes	VAT/sales tax	20%	8.9% ⁴	7%	-	20%	19%
Bank-specific taxes	Bank levy	0.18% ¹	-	-	-	0.329% ¹¹	0.04%

1 The rate listed is for the 2016 calendar year. Levied on the total chargeable equity and liabilities. Half rates (0.09%) applies to long-term amounts. Gradual reduction to 0.10% by 2021.

2 Corporation tax main rate (for all profits except ring-fence profits) will be reduced to 17% by financial year 2020.

3 Additional 8% surcharge on banks. Came into effect January 2016.

4 State-level tax.

5 Capital gains tax on the sale of shares. 28% rate on gains from residential property.

6 Base rate of 39.6% + 8.82% state + 4% city.

7 Long term capital gains.

8 Federal rate of 39% + 7.1% state corporate income tax.

9 Top income tax rate will be increased to 22% from 2017 onwards.

10. Applies to branches of foreign banks only.

11. Applied over smaller perimeter than UK or German equivalents

12. Corporate income tax rate of 15% + 17% municipal + 15% solidarity surcharge

13. 45% top rate; 47.475% including solidarity surcharge

14. 25% flat rate; 26.375% including solidarity surcharge on privately held shares of less than 1%

SOURCE: British Bankers' Association & Oliver Wyman, Winning the Global Race, November 2015; Deloitte Tax GuidesHMRC; Inland Revenue Authority of Singapore; Impots.gouv.fr

¹⁴¹ TheCityUK, Tax Working Group Draft Terms of Reference, 2016

IV. CONCLUSION: OUR VISION FOR FRPS IN THE UK

Growing the FRPS industry will benefit the UK economy, create jobs and help stimulate inward investment. More UK trade and investment will also help create jobs and growth in the EU and other markets.

Competition to host the highly skilled and globally mobile FRPS industry is growing, and Brexit uncertainty will hamper the UK, which must now push harder and move faster to embrace opportunities, new technologies and specialist skills (Exhibit 25). The areas for growth identified in this report will require real energy from the industry, policymakers and regulators.

We at TheCityUK believe the prize is worth fighting for.

EXHIBIT 25

Our vision

United Kingdom: Leading the global financial and related professional services industry

From



Leading global and European FRPS centre, but emerging market centres strengthening their positions



A growing industry overall, but employment at risk in parts of the UK as off-shoring and automation continue



Broad product portfolio, but lagging behind the US in growth areas like investment management



Strong innovation centre in banking, but funding gaps remain versus the US



First for financial and professional talent, but shortages in diverse profiles and next-generation skills

To

FRPS hub for the developed and emerging world, FRPS capital for Europe

Strong, connected regional centres with clear specialist capabilities and expertise

Leader in growth areas, including investment management, emerging risks and infrastructure financing and advisory

Dynamic technology centre across the whole FRPS industry, where innovation happens at scale

Diverse workforce that leads the world in combining financial, professional and technology skills

Solid foundations on trust, future-proof client base, dialogue and cooperation with policymakers

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To supplement our research and develop the areas for partnership discussed in this report, we have spoken with a number of senior leaders across the industry, Government and regulators.

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