Inside FCA Podcast: Interview with Debbie Gupta on the consumer investments strategy

OI: Hello and welcome to the Inside FCA Podcast. I'm Ozge Ibrahim and today I'll be speaking to the director in the FCA's Supervision - Investment, Wholesale and Specialists Division, Debbie Gupta about the new consumer investments strategy.

Earlier this year, I spoke to the FCA's campaigns team about their research in this area, which revealed the trend towards self-directed investors making high-risk investment decisions. Today, we'll be talking about the work to tackle these issues and understand the thinking behind the newly released investment harm strategy.

Welcome, Debbie.

DG: Thank you.

OI: I'd like to start by talking about the current investment landscape. What are the areas of concern the FCA has identified in this market?

DG: What I'm going to talk about is the consumer investment market. So we're talking about people like you and I, not institutional investors or people for whom this is their day-to-day job or their profession. But people like you and I invest in this market in order to make our savings go further. And we at the FCA don't believe that that market is working as well as it should for people like you and I.

I think there are 3 reasons, probably, why that's happening. The first is consumers are having to make really complex decisions in a way that they've never had to before, about how to invest and where to invest their hard earned cash. The second is that government policy has changed in recent years. For example, the pension freedoms that were introduced a few years ago give people much greater choice, not just about how they invest their money for retirement but also what to do with the money and the cash they've earned for retirement.

And that means we're having to make complex decisions with more choices than ever before. And on the flip side, I think the market that we regulate is dominated by lots and lots of small firms. So it makes it really difficult for people like you and I to navigate. 6,000 firms and over 27,000 individuals provide services in this space to help us understand where we might invest, how we might invest, and providing advice to consumers.

And that means that it's really difficult for us to understand what good looks like, it's really difficult to find trusted firms that do their work well. But also, for the regulator, it's really easy for bad actors to hide in this market because there are so many of them. And so those 3 things combined mean that we are really clear that this market isn't working for consumers in the way that we want it to.

OI: And you've recently published an update on your work over the past year to tackle harm in this market. What does this cover and why?

DG: Well, it's interesting, because in this market, we do lots and lots of work through our supervision, through how we authorise firms at the gateway and we give them licences to operate. And, indeed, enforcement action that we take when firms do the wrong thing or breach our regulations. But we don't often tell people how much work we are doing in this area. We do through ad hoc means, you know, through MPs' letters or freedom of information requests. Or a journalist might phone us up and we'll provide some data there.

So we thought we would pull together all of the activity that we do as a regulator in this market to demonstrate and explain the sort of activity we do and the scale of activity that we carry out. And in it, it shows things like the fact that since March, we've stopped 1 in 5 applications from new firms who are trying to enter this market but where we're not convinced that they've got the consumer's interest at heart or they have potential for causing consumer harm.

There are firms that offer higher risk investments to the wrong kinds of consumers, for whom that kind of investment just isn't right. Or potential scams and reports of scams. And we've got 1,700 cases open against firms in that sort of territory. And of course, we are a source of advice and intelligence for consumers, and we try to help consumers navigate this market as best we can. And since March, we've had over 19,000 consumer calls and emails about pensions and investments in this market.

So, clearly, there's a lot of work that we are doing. We want to be in line with the ambitions of the FCA of the future. We want to be really transparent about that. But more importantly, we are really clear about the outcomes we're looking for, that we hope the industry will also support us on achieving and therefore, allowing ourselves to be held to account, both by consumers and wider opinion formers.

OI: And in addition to this, how does the recently published consumer investment strategy address some of the issues you've outlined?

DG: Well, we published last September what we call a call for input, which was to set out our vision on what we thought was wrong in this market and invite industry and consumers and other academics and other interested parties to help us figure out A, whether they agreed with our analysis of the market; and B, what they would do or what they might suggest on how we can improve it. And so this consumer strategy takes account of all of that input. We had fantastic input, really detailed reflections from right across this sector. And this strategy then sets out what it is we're going to do.

And there are essentially 4 ambitions that we set out. The first is where people have funds to invest, we want to make sure they are doing so confidently and safely, so that they can benefit from investment returns. Investment is a good thing, and we know that over 8 million people have more than £10,000 in cash in investible assets that's just not earning any interest or earning any return because it's just held in cash.

So, the first ambition is to help more people save with confidence and understand what they're doing. And we want to reduce that 8 million by 20% over the coming period. The second is, for those who do invest, we want to make sure that they are investing in suitable investments and we're particularly targeting those consumers who invest in investments that are higher risk than they should. And we want to reduce this number.

We know from our survey and research that 6% of adults, that's nearly 4 million, have held higher risk investments, more so than they should and the losses that they can tolerate. And that's really increased over the course of the pandemic. So, we really want to tackle that and reduce the number of people that are just investing in the wrong kind of product. The third ambition here is fraud and scams and this is a really, really big area for us.

In the last year, people lost £570 million to investment fraud and scams and that has got to come down. It's tripled since 2018. And so we're going to use all of the tools available to us to really get tough at the gateway, really supervise and regulate the firms that are operating in this market and take enforcement action where that is appropriate. So we want to tackle fraud and scams more robustly than we've ever done before.

And the last bit is really about what happens when things go wrong and how do we make sure that consumers get the compensation that they deserve when things go wrong. Because things will go wrong. And at the moment, the cost of paying that compensation is falling too much on the FSCS [Financial Services Compensation Scheme], and that means that all of the industry, the good and the bad, are paying for the small number of bad actors that are operating in this market.

So we really want to tackle that issue of how do we get, as we call it, the polluter to pay, rather than the good guys to pay. So those are our 4 ambitions, we want to bring down the FSCS bill, we want to make sure that we are tackling fraud and scams more robustly than before, we want to make sure that people who are investing, are investing in the right products rather than higher risk products that they shouldn't be in. And for those who aren't investing, we want to make sure that they are doing so safely and confidently.

OI: You've mentioned 4 million higher risk investments there, and there's generally more people making higher risk investments, especially during this pandemic, and they don't necessarily understand the risks that they're getting into. Can you give me some examples of what these investments are?

DG: Yeah, I mean it's interesting, because the pandemic has changed the profile of people who are investing. And what we notice is that there are more younger people investing in these kind of products, often prompted by online approaches. So, you know, I mean the basic thing is, if an offer is too good to be true, it probably is not right for you. Because I know that in our research, we found that, we tested, what do consumers think is too good to be true? At what point do they go, 'hang on a minute, that can't be right'?

And it's something like 30% rate of return, which is extraordinary in a low interest environment, that that is the threshold at which people start to go, 'hang on a minute, there might be something wrong with this'. So we need to do a lot more to help consumers navigate this landscape, recognise what risks they are taking, make sure they know how to absorb the losses and that they understand that that money might all go and can they afford to lose that.

But we see things like speculation in foreign currency trading, we see lots more investment in crypto. And these things aren't bad in and of themselves, but they need to be investments that people are making knowingly and with a really clear understanding of what the risks are that they're taking. Investing in crypto in order to pay off your mortgage probably isn't the right thing to be doing.

OI: And what impact are websites and social media having on the accessibility of these high-risk investments, do you think?

DG: Well, I think it's really interesting because online marketing and what we call financial promotions, the way in which investments are marketed to people has really, really changed over the last few years. You know for example, you get celebrity endorsements or you get things dropped into your social media feeds. Or you get prompts from influencers online that, in a sense, aren't your traditional marketing brochure that you might have got some years ago.

For example, Katie Price recently promoted foreign exchange trading through a guy called Josh Chandler. You know, she's sort of endorsing that. 2.6 million followers of hers see that on Instagram. And that's really, really difficult to kind of navigate and control. But it's an area where we are seeing increasing activity from people like you and I. You know, there's a story I think, of a nurse whose hard earned savings, she got one of these endorsements from Katie Price and lost nearly a month's wages, relying on the fact that Katie Price's endorsement must have been a safe thing to do.

So, how do we tackle that sort of behaviour? Younger people just kind of having a go online, it's really easy, it's a couple of clicks of a button. It makes you feel good. It's sort of more like gambling and gaming than it is investing. And that's really one of the areas we've got to tackle, which is to ensure that when people are doing that, when they're having a go and playing with this activity online, they're really clear about the risks they're taking.

OI: And there are also concerns about poor advice, both for consumers and for other firms across the market. What are some of the examples of poor advice and the implications?

DG: We did a study some time ago about financial advice. And what we found is that financial advice generally for most people on straightforward investments is pretty good. We define good as advice that is suitable for that particular person, suitable in terms of their income, their assets, their ambitions, their aspirations, and their needs in retirement. Where we see real harm occurring, is often in the place where people are being advised to invest in pensions and particularly, where people have, for example, final salary pension schemes, really valuable things that are not available to most people nowadays. And they're being advised to cash out their final salary scheme and invest in something else.

So an example was an individual who had worked for an employer for a very long period of time, probably didn't earn much more than £30,000 a year. And when the employer looked like it was at risk of going bust, a financial advisor told him that his pension might be at risk because of that and advised him that he should move all of his defined benefit pension scheme with this employer into a different investment. And as a result, that individual, who did what the advisor had advised, but wasn't aware that in doing so, he would lose protections from the Pension Protection Fund, and that he would be giving up guaranteed benefits that he wouldn't get anywhere else.

Now, in the grand scheme of things, in terms of the economy, yeah, it was £135,000 that this person lost as a result of that advice. £135,000 in the grand scheme of things is probably not a lot, when the economy is dealing in trillions and billions of pounds. But to that individual, earning £30,000 a year, that's 3 or 4 times their annual salary. That's a huge amount. And at a time in their lives when they're not going to have the earnings to recover that investment. And that's the sort of thing we absolutely have to crack down on, because it has a devastating impact on those individuals.

OI: And so, what do you plan to do to reduce the cost and impact of poor advice like that?

DG: Well, we are really, really tackling particularly the advisors who operate in this market and we have raised standards over the course of the last few years. And we have increased our supervisory oversight, our regulatory oversight on these firms. So for example, we've been doing things like extracting more data from these firms to understand what the volume of activity is that they are doing in this space. We are looking to ensure that they don't charge individuals in a contingent way, so we've banned contingent charging.

We've accessed advice from them, we've accessed data from them about what insurance cover they have and what capital they hold, so that if things do go wrong, they're able to repay the consumers who have lost out as a result of the poor advice that they've given. And, as a result of that, in 2018 there were over 3,000 firms that gave DB transfer advice. But because we have been cleaning up the market and raising regulatory standards, there are now around just over 1,200 firms that are operating in that market.

And while that is not great for the firms that are no longer operating in the market, it's a much better outcome for consumers because they are now able to feel more confident about the firms that they need to go to for that kind of advice.

OI: And are there any barriers for you in this space and challenges to doing this?

DG: I think there is. You see, the market is operating as the market operates. And what we see in this market, and I think we in the UK are probably a bit different to other jurisdictions and other countries, but it only costs about £20,000 to set up an advice firm, in terms of holding capital for providing that kind of service. And then when you look at the Financial Services Compensation Scheme, which is essentially where consumers end up going if a firm can't pay compensation that's due, the average compensation pay out from the FCSC is about £30,000. So you can see already that the structure of the market doesn't quite work in the way we would expect it to do, or the way we see it working in the banking sector, for example.

So I think there is a big debate to be had about how we make sure that firms giving advice in this market are able to put things right when things go wrong. Insurance is another way in which smaller firms cover their costs, if they're not holding the capital, then maybe they hold insurance to cover any of these mis-selling or poor advice cases. But actually, what we've seen over recent years is that the insurance market is also hardening. And it's excluding some of this higher risk advice activity from being eligible for any pay outs if things go wrong.

So it's a really big question for the market as a whole but also for the regulator, about how we get the balance right between wanting to nurture a market that's competitive and responsive to the evolution of consumer behaviour and the needs of consumers. But balancing that with ensuring that they provide services that are appropriate, that are robust, and are safe.

OI: Investment scam activity has also grown significantly in the last few years. How do you plan to tackle this?

DG: You're absolutely right. We have seen a rapid increase in investment and pension scam activity and, actually, through the pandemic, we've seen an acceleration of the reports that we are getting. Some of that involves the foreign exchange stuff that I was talking about. There were quite high profile examples I think in the media during the pandemic of people sat at home in their bedrooms, particularly younger people, just like gaming and gambling, just playing online with trading and foreign exchange trading.

What we've seen is an increase in scams, because of course, when you think about the online platforms and the online noise that people are exposed to every day, it's easy to see how firms and particularly scammers and fraudsters can set up a fake website, entice you in, persuade you to hand over your money, and then disappear. And they are outside, often operating outside the UK, sometimes operating outside, they're not regulated firms, they're not authorised firms. So we don't have a very big grip on who these firms are and how they're operating.

But that doesn't mean we're not doing lots in this space to help tackle this particular problem. You'll know that the Online Harms Bill is going through Parliament and there's been lots of calls for the Government to include financial fraud and financial scams in the Online Harms Bill. We have certainly made our position clear about that, but lots in the industry are advocating similar inclusion. We've been working really hard with all of the online service platforms like Google and others who, in a sense, provide the kind of vehicle through which those scammers can operate.

We regularly, several times a day, scan the online services to try and identify scams, identify fraudsters, and take really rapid action, both to alert consumers to the risks here but also take down those websites that are causing the kind of harm that we are seeing. But of course you know, as anyone will know, it's pretty easy to set up a website. And of course, the minute you take one down, it's a matter of hours before it pops up again somewhere else slightly different, that enables them to continue operating in that way.

So it's a very, very difficult market. And a very, very difficult environment in which to take decisive, comprehensive action. What we are doing, as I say, the Online Harms Bill is one vehicle through which we can get a better grip on this. Working with online service platforms is another way in which we can get a better grip of this and we're making good progress on that front.

And we are making changes to the financial promotions regime. The financial promotions regime covers the way in which these investments are marketed to people like you and I. And that legislation is going to change. There will be more published later this year about how we are going to change that in order to make sure that we are extending the protections that consumers rightly deserve and often think they have when they don't.

OI: And we've talked about a wide range of areas where investment harm can potentially occur, in particular scams and fraud, what would you like partner organisations, including the Government, to do to help tackle these issues?

DG: Well, it's interesting because I think we can do quite a lot more and so one of the things we're doing is we are about to launch, in the next month or so, a really, really interesting, innovative way of helping consumers understand the risks they're taking and guide them to better advice and better information about what good or safe investment looks like. And, as I say, the online space is really where a lot of this activity is happening. And so our campaign in this area will be very much driven through social media and online platforms.

But I think the other thing is, as you've rightly identified, we can't do this alone. We are working very closely with industry to help tighten this up. So our sort of regulatory framework and our regulatory relationships with the industry are really important here. But there are other regulators and other enforcement agencies operating in this space and we need to work much more closely with them to ensure that our efforts here are coordinated and really impactful.

So the example I was giving you earlier, where there may be firms that are sort of on the margins of our regulatory reach, or indeed, completely outside our regulatory reach, who may be committing financial crime or who may be involved in fraud that's been conducted from outside the UK's borders. Well, we can work much more closely with enforcement agencies, intelligence agencies, to help tackle that. And I think that's one of the big ambitions of our consumer investment strategy.

OI: And you mentioned the upcoming FCA campaign, which is designed to help consumers make better informed investment decisions. Can you just give me some more detail about how your work will feed into this and what you actually want the campaign to do ultimately?

DG: Well, what we've done is we've looked very closely at consumer behaviour. And we've looked at what is it, what is the consumer journey? How do people like you and I get interested in online investments, offerings, how do we make our decisions? What is it that influences us? At what point do we go from speculation to action? So behavioural understanding of this type of investment activity is really key to making sure we can intervene at the right points in that journey, to just provide a note of caution that says, are you sure this is what you want to do? So, what we call sort of friction or disruption in that consumer journey.

And we will be providing interesting interventions in that consumer journey that might help guide them to a bit more information, might help guide them to the Register or to our warning lists, or to information that they could find that just helps them think twice before they act. So, disrupting that consumer journey online is a really new way for us to help educate consumers, support them in their investment decisions, and make sure they're making the right ones for themselves.

OI: And finally, how will you measure the success of the new strategy overall?

DG: Well, let me just go back to the 4 ambitions we've set for ourselves. And I have to say, for the FCA, we're being brave here in being clear about what we want to achieve over the next 5 years. Recognising that we're not in control of this market and things might happen that we haven't yet understood or can't predict.

But nevertheless, I think it's a really good thing to set out our ambitions. So, we said we wanted to help people invest, particularly where they have cash that is investible, and make sure they do so safely and with confidence. We know there are 8 million people who hold more than £10,000 in cash, who we think should be investing, and we want to reduce that number by 20% over the next 5 years.

The second thing we said we wanted to do, was we wanted to reduce the number of people who are investing in investments that are not suitable for them, that are too high risk for their needs. We know that there are 4 million people who do that and we want to reduce that number by half. In the third pillar, we said we wanted to tackle investment fraud and scams. That number has tripled over the last 3 years, it's now £570 million. We want to reduce that.

And the final thing we said was about the cost of compensating consumers when things go wrong. Those costs fall on the Financial Services Compensation Scheme. That bill currently this year is £800 million and we know that that is probably going to increase while we try and get the sort of harm that's already in the system crystallised and dealt with. But from 2025, we want that level to stabilise and reduce, year on year. Those are ambitious targets we've set ourselves for the first time.

OI: Thank you Debbie for your detailed insight and examples into the consumer investment market at this time. To find out more, go to our website to read the recently published strategy report. For now, stay safe and join us again soon on the next Inside FCA Podcast.

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