UK FINANCE

FINANCIAL SERVICES: Growth, Levelling up and Skills

Briefing paper

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FOREWORD

Laying the foundations for sustainable and inclusive economic growth across all the nations and regions is rightly central to the Government's policy aims. A thriving banking and finance sector will be integral to achieving this. In this briefing note, we outline six key recommendations to support the levelling up and skills policy agendas in order to encourage regional growth.

Strong economic growth is essential to securing a better future for the UK. A growing economy gives households a better standard of living, allows local businesses to flourish and British companies to compete internationally. It also generates the revenues needed to fund the public services we all rely on, as well as being key to the UK realising its net-zero and sustainability goals.

In its own right, the sector accounts for 10 percent of GDP, employs over a million people in high quality, well-paid jobs, and contributes tens of billions in tax each year. But just as importantly, it delivers essential services to the rest of the economy – from providing scale-up financing to promising AI and life sciences start-ups, to helping family businesses manage their cash flow and ensuring established FTSE 100 companies can effectively manage complex risks.

There is, however, the potential to do more. *The Skills for Future Success* report from the Financial Services Skills Commission (developed with PwC and the Professional Business Services Council) shows that tackling the skills challenge across financial and professional services sectors could boost UK economic output by £38bn by 2038, a growth of 12 per cent in the size of the sector.

By tackling the skills challenge and supporting the levelling up agenda, the sector can help to channel investment into the major infrastructure projects of tomorrow, such as wind farms, expanding rail capacity and building more homes. Doing this now will help grow the economy and improve the lives of people across the country.

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Recommendations

Financial services are an engine for growth and prosperity across the UK. Touching almost every aspect of the economy and society, the industry is playing a critical role in delivering the missions identified in the Levelling Up White Paper and contributing to the UK's skills agenda.

UK Finance has identified seven areas where financial services are already having a significant impact in regions around the country and where government action can help take this further:

Jobs and skills

1. **Creating highly paid, highly productive jobs across the UK** – by giving employers greater flexibility in spending their Apprenticeship Levy contributions
2. **Developing people's skills** – by working with the industry to deliver improved adult numeracy, including extending Maths provision to 18
3. **Greening the housing stock** – by training the hundreds of thousands of skilled workers needed across the country to improve the energy efficiency of homes

Businesses

4. **Supporting small business growth and encouraging lending** – by reforming regulations on MREL and capital concentration to allow greater competition in the banking sector and unlock up to £62 billion of new investment
5. **Boosting access to growth funding through the UK's capital markets** – by widening the scope of investment schemes, championing success and entrepreneurship, and fostering a culture of equity ownership in the UK

Consumers

6. **Empowering and protecting consumers** – by bringing forward reforms to the Consumer Credit Act in this Parliament

Regional growth

7. **Driving regional investment** – by giving private sector investment a greater role in future devolution deals

Current impact

Financial services make a huge contribution to the regions and nations of the UK as:

- One of the country's largest employers - providing highly paid, highly skilled jobs for more than 2.2 million people, with around two-thirds of these roles based outside of London.
- An investor and lender – delivering tens of billions of pounds in investment to help turbocharge regional economies – from tech start-ups in Manchester to transformative green energy projects in Teesside.
- A trusted source of finance and advice for consumers - empowering people by improving their financial independence, skills and confidence, and strengthening their communities in turn.
- Financial Services is one of the UK's most productive industries, generating £115,000 in output for every job in 2019.

Public support

Recent polling by Public First for the APPG for Financial Markets and Services shows the public recognise the importance of financial services for levelling up:

- 93% of people believe financial services are important or very important for the UK economy.
- 78% believe financial services are important or very important for the economy of their region.
- 81% think the industry has an important or very important role to play in levelling up.

The polling also reveals the public's desire for financial services to be given a bigger role in levelling up. In particular, they want to see the industry increase investment in companies outside of London, boost investment in SMEs and create more well-paid jobs across the country.

Jobs and skills

1. Creating highly paid, highly productive jobs

In every region of the UK, jobs in financial services are on average more productive and offer higher median salaries than those in other sectors.

These roles are found not just in internationally significant financial services hubs outside of London, such as Belfast and Glasgow, but also in places that are central to the levelling up agenda. From Stockton to Swansea, over 20 towns and cities have more than 10,000 people employed in the industry. 71% of parliamentary constituencies have more than 1,000 local people employed in financial services.

Jobs in the industry are increasingly moving to the regions. For example, HSBC has relocated the UK headquarters of its ring-fenced operations to Birmingham, moving 1,000 roles to the city. This has helped encourage other firms such as Deutsche Bank to also create 1,000 roles in the city, while Goldman Sachs has moved its engineering division there and agreed a £4bn partnership with Legal & General for new housing and urban regeneration.

Whilst the sector continues to expand across the UK, a lack of access to skills remains a significant barrier to more jobs being created outside of London. Roles in the regions are also much more likely to be affected by automation, meaning there is an increasing need to retrain the existing workforce to prevent this having a negative impact.

Greater flexibility over how employers can spend their Apprenticeship Levy contributions would allow financial services hubs to grow further – by boosting retraining and enabling large firms to pool resources with Combined Authorities and SMEs to target skills gaps.

Recommendation: The Government should give employers greater flexibility in spending their Apprenticeship Levy contributions, so that they can build a strong pipeline of skills in regions outside London.

2. Developing people's skills

Whether it's saving up a deposit for a first home, planning for retirement or applying for a loan to start a business, millions of people rely on the financial services industry for advice and support. Firms within the industry deliver some of the largest skills and employability programmes in the country, such as Barclays' Life Skills initiative, which has reached over 15 million people since 2013 and NatWest's MoneySense which has reached 11.5 million children and young people since 1994. Many others offer practical help for their vulnerable customers, for example, through Yorkshire Building Society's partnership with Citizens Advice, which provides free independent advice to customers through its branch network and HSBC's No Fixed Abode and Survivor Bank propositions which support the homeless and victims of modern slavery to obtain access to a Basic Bank Account.

These initiatives have the potential to support the Government to deliver on its Levelling Up agenda, given the large disparities in basic financial literacy skills held by people in different regions of the UK, with those outside London and the South East significantly less likely to feel confident with numbers. Furthermore, the Money and Pensions Service provision mapping exercise found that young people from lower socio-economic groups have lower baseline financial capability scores and schools with the highest proportion of pupils eligible for Free School Meals were less likely to teach pupils about managing money.

An All-Party Parliamentary Group (APPG) on Financial Education for Young People report found that two fifths of teachers, who have a statutory duty to deliver financial education, were not aware that it is a national curriculum requirement. Building financial literacy and practical maths skills needs to start early, as attitudes to money are well developed by the age of seven. Financial literacy is important at every stage of life and the new government programmes 'Multiply' and 'Maths to 18' need to form part of a holistic approach which delivers age-appropriate content at the right time. Above all, teachers need to be given appropriate support so that they have the skills, knowledge and confidence to deliver the training.

As a trusted source of advice with a far reach, financial services firms are in a strong position to where possible help plug the gaps in knowledge, helping to boost basic numeracy skills and increase financial confidence. The financial services sector provided meaningful, quality assured financial education to over 4.3 million children in a school or community setting in 2022, and is therefore an ideal partner to help deliver improved provision.

Recommendation: The Government should work closely with the financial services industry to ensure that the Multiply and Maths to 18 provisions complement and leverage existing programmes available through the financial services sector. This would deliver a holistic financial literacy approach that provides a platform for financial wellbeing, social mobility and economic growth.

3. Greening the housing stock

The industry is committed to playing its part in tackling climate change, protecting nature and meeting the net zero target by 2050. Greening the UK's housing stock will be essential to meeting our net zero target. As we set out in our **Net Zero Homes Report 2022**, the UK's homes are currently among the least energy efficient in Europe, with heating of its 28 million homes representing 14 per cent of total carbon emissions.

This presents significant challenges, but also opportunities to stimulate economic activity across the UK. As demand for retrofitting increases, supply chains will have to scale-up to keep pace. This will involve the creation of hundreds of thousand of well-paid, high-skilled jobs across the UK; the Climate Change Committee (CCC) estimates that an additional 200,000 workers will be required.

However, there is currently a shortage of skilled workers to fill these jobs. In Q2 2022, the Federation of Master Builders (FMB) reported that 61 per cent of members had delayed hires due to a shortage of skilled tradespeople in that quarter; 42 per cent found it difficult to hire bricklayers and carpenters and joiners, with 81 per cent of experienced builders increasing their prices for work.

Another obstacle to scaling up the supply chain is a lack of certainty among construction and housing SMEs as to the policy environment they are operating in. Our Net Zero Homes Report showed that uncertainty as to the available finance, applicable regulations, incentives and subsidies available is deterring existing SMEs from investing to expand their retrofitting capabilities, and making it less attractive for new businesses to enter the market.

Recommendation: We believe government intervention is needed to help overcome these obstacles and unlock new green jobs across the UK. Specifically:

- the Government should offer grants and subsidies to train new and upskill existing tradespeople to achieve the qualifications required to perform the various roles involved in retrofitting. We estimate that it could cost up to £110 million to train the CCC's predicted 200,000 additional workers.
- the Government should design long-term policies that give SMEs a clear signal of the direction of the market. These policies should be clearly communicated, with the conditions and timelines made explicitly clear from the outset.
- the financing available to SMEs in the supply chain should be increased via initiatives that mobilise both private and public funding sources. This could include the use of credit guarantees for lenders (to reduce the risk of lending to supply chain companies) and the mobilisation of finance from the UK Infrastructure Bank (to provide low-interest loans to supply chain companies).

Businesses

4. Supporting small business growth

Financial services also support levelling up by backing small businesses around the UK.

For example, HSBC have a commitment to invest £12 billion in SMEs outside of London, whilst NatWest have established regional boards to drive greater impact at a local level.

Challenger banks and Fintechs play a particularly important role in enabling SMEs to find new investment. A 2020 Bank of England report found that since 2017, all of the net growth in SME lending had come from smaller banks or from alternative sources, such as peer-to-peer lending. This includes lenders such as Funding Circle, whose lending is over-represented in regions with the largest investment gaps, and Paragon Bank, who make around 70 per cent of new lending outside London and the South-East.

However, challenger banks are being held back by regulations such as MREL, which require them to hold capital at the same levels as major banks and well above the thresholds found in other countries – preventing some £62 billion of potential investment into the UK economy.

Creating a more dynamic, competitive banking sector and unlocking investment across the regions will therefore be key to driving the levelling-up agenda. Reforming rules for challenger banks would help close regional lending gaps - estimated to be around £2-3 billion each year – and make it easier for businesses outside of London to grow.

Recommendation: The Government should bring MREL thresholds down to levels seen in similar economies and relax rules which penalise banks for only lending in the UK.

5. Accessing funding and investors through the capital markets

The UK's capital markets are fundamental to growing and supporting the businesses of the future.

The UK creates the greatest number of new businesses per capita in Europe (one per 12.5 versus one per 17 in France and one per 25 in Germany). However, the survival rate of newly-founded businesses after five years is only 38 per cent, below that of other comparable markets. Coupled with this, UK households hold just 10.6 per cent of their financial assets in equity, compared with 36.2 per cent for US households and 22.7 per cent for French households.

As explored in greater detail in UK Finance's recent **UK capital markets: Building on strong foundations** report, the above trends form part of a wider landscape of challenges facing UK capital markets and access to funding for growing businesses – in particular the need to address the structural barriers hindering UK growth companies and reboot the nation's culture towards financial empowerment and equity ownership.

To continue to support small businesses and growth companies throughout the UK, we must ensure our capital markets ecosystem provides access to funding to businesses of any size, at any stage in their growth journey. At the same time, steps should be taken to foster a dynamic and supportive investor base in the UK by empowering individuals to take personal ownership of their financial futures. Everyone should have the opportunity to own a piece of UK plc and back the businesses which they use every day.

Recommendations: A range of complementary actions are set out in UK Finance's **UK capital markets: Building on strong foundations** report, including:

- The scope of investment under the Enterprise Investment Scheme (EIS) and the Seed Enterprise Investment Scheme (SEIS) should be extended into regulated entities (e.g. regulated fintech businesses). Enterprise management incentives (EMIs) should be included alongside the SEIS to eliminate an 'incentive cliff edge' for scaling companies.

- Develop ‘Why choose UK capital markets’ content to promote UK success stories, celebrate home-grown entrepreneurship, and encourage the public to back businesses using UK markets through targeted communications and engagement.
- Removing the 0.5 per cent stamp duty currently charged on share purchases. This would reduce the cost of investing and incentivise more investments in equities.

A holistic and collective approach from government, regulatory authorities, and industry is needed to take forward these actions and ensure our capital markets continue to drive growth and support the UK’s economic future.

Consumers

6. Empowering and protecting consumers

Financial services enable the consumer spending that drives our economy, from access to cash on the high street to the payment systems that integrate public transport across Combined Authorities.

The industry has responded to the changing way people manage their finances, especially the most vulnerable. The banking hubs programme is now being rolled out to ensure all communities have reasonable access to a bank branch or cash machine, whilst 7.2 million basic bank accounts have been created for vulnerable customers since 2016.
As the financial landscape changes further, it is crucial that regulation keeps pace so that consumers are protected and firms can deliver new solutions to meet their evolving needs. This is particularly important for levelling up, given large regional disparities in access to affordable credit and the concentration of financial vulnerability in communities that have been ‘left behind’.

The Government have made a welcome commitment to review the Consumer Credit Act, which is unfit for the digital age, and give full responsibility for regulating consumer credit to the Financial Conduct Authority. Given the current economic situation and the risk of more people being pushed into financial difficulty, the Government should accelerate these plans so they can be completed in this Parliament.

Regional Growth

7. Driving regional investment

As the government devolves power away from Whitehall, financial services are playing a critical role in helping Mayors and Combined Authorities to deliver growth for their areas.

Banks and others are investing billions in regional development projects outside London, for example through providing £5.5 billion in financing and support for the Dogger Bank offshore wind farm in Teesside, the largest project of its kind in the world. Other firms are lending their expertise to local government, including Mastercard who shared local spending data to help Hull, Belfast and other cities recover from the impact of Covid-19.

Securing investment relies on each region having a pipeline of ‘bankable’ projects into which private sector capital can flow. However, the visibility of these projects and the capability of local government to engage the private sector varies significantly between regions.

As devolution deals are extended across the country, a sharper focus on how they will unlock private sector investment would give the industry clearer signals about how it can best support growth. For example, future devolution deals could specify which projects will be a priority for private investment and make central government funding conditional on this being secured.

For example, empowering local authorities to make their own decisions to attract investment can support the Government to deliver on its private investment in nature target as outline in the Green Finance Strategy. The decision to provide four local authority areas with up to £1m each to build their capacity to attract private investment through the Local Investment in Natural Capital (LINC) programme is a welcome step, but needs to go further.

Recommendation: The Government should give private sector investment a greater role in future devolution deals by, for example, making it a condition of central government funding.

CONCLUSION

Supporting the levelling up and skills agendas by enacting the above recommendations will drive inclusive regional growth across the nations and regions of the UK.

Helping to strengthen initiatives like "Maths to 18" is vital to build a workforce and encourage talent that can more readily address future challenges. UK Finance recently made a similar assessment in its UK capital markets: Building on strong foundations report, where we called for financial literacy education programmes to help reboot the nation's culture towards financial empowerment and entrepreneurship. Such action could help to preserve our capital markets and financial services ecosystem – among the world's largest and most sophisticated, while securing our financial health and long-term economic growth.

Our recommendations also have the added benefit of helping the UK to achieve its wider net zero ambitions, an issue that is being keenly focused on following the Government's suite of announcements earlier this year, and set against a back drop of international progress in this area, which the UK needs to respond to.

Finally, taking action on both the levelling up and skills agenda through the above measures could help form the basis of an industrial strategy for the UK, aimed at improving both the long-term health and immediate growth potential of the economy.

FURTHER INFORMATION

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