

Strategic Skills Needs in the Financial Services Sector

A report for the National Strategic
Skills Audit for England 2010

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Foreword

Launched on 1st April 2008, the UK Commission for Employment and Skills is a key recommendation in Lord Leitch's 2006 review of skills Prosperity for All in the Global Economy: World Class Skills. The UK Commission aims to raise UK prosperity and opportunity by improving employment and skills. Its ambition is to benefit individuals, employers, government and society by providing independent advice to the highest levels of the UK Government and Devolved Administrations on how improved employment and skills systems can help the UK become a world class leader in productivity, in employment and in having a fair and inclusive society.

Research and policy analysis plays a fundamental role in the work of the UK Commission and is central to its advisory function. In fulfilling this role, the Research and Policy Directorate of the UK Commission is charged with delivering a number of the core activities of the UK Commission and has a crucial role to play in:

- Assessing progress towards making the UK a world-class leader in employment and skills by 2020;
- Advising Ministers on the strategies and policies needed to increase employment, skills and productivity;
- Examining how employment and skills services can be improved to increase employment retention and progression, skills and productivities.
- Promoting employer investment in people and the better use of skills.

We will produce research of the highest quality to provide an authoritative evidence base; we will review best practice and offer policy innovations to the system; we will undertake international benchmarking and analysis and we will draw on panels of experts, in the UK and internationally, to inform our analysis.

Sharing the findings of our research and policy analysis and engaging with our audience is very important to the UK Commission. Our Evidence Reports are our chief means of reporting our detailed analytical work. Our other products include Summaries of these reports; Briefing Papers; Thinkpieces, seminars and an annual Research and Policy Convention. All our outputs are accessible in the Research and Policy pages at www.ukces.org.uk

This report was commissioned by the UK Commission to contribute to the evidence base for Skills for Jobs: Today and Tomorrow, the National Strategic Skills Audit for England 2010. A further two reports were commissioned to identify the strategic skills needs in the Bio-medical and Low Carbon Energy Generation sectors and a fourth, Horizon Scanning and Scenario Building: Scenarios for Skills 2020, investigated the potential implications for skills of future national and global scenarios. We hope you find the report useful and informative in building the evidence we need to achieve a more prosperous and inclusive society.



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Executive Summary

Introduction

The aim of this study is to provide an assessment of the skills needs in the financial services sector to 2020 in support of the National Strategic Skills Audit for England 2010, undertaken by the UK Commission for Employment and Skills. This report presents the findings of the assessment which, while discussed in further detail below, are that;

- Between 1998 and 2007 industry output doubled, but employment increased by only 2.2 per cent. Since then total employment in financial services is estimated to have declined between 5 per cent and 10 per cent;
- In the coming decade all the drivers of change, such as increasing levels of regulation, the need for efficiency, consumer demand and globalisation are pointing downwards. In our view, overall employment is unlikely to return to 2007 levels in the next decade and could remain significantly lower;
- Historically there have been certain skills gaps and shortages in particular in retail banking, and in retail and wholesale insurance. While some of these gaps and shortages may persist, others such as risk management and compliance skills and actuaries will come to the fore;
- Regulation could limit the freedom of banks to innovate. This could result in polarised banking business models, with some banks focusing on core retail banking services, generating lower but more stable returns, while other niche providers serve clients willing to take greater risks;
- Efficiency will be paramount in retail financial services as companies look towards recovery and the need to restore margins and profitability. There will be continuing job losses due to branch closures and moves towards more efficient distribution channels, and;
- As emerging economies become more important, client-facing front-office functions in wholesale markets will need to be established close to international clients. As emerging economies grow in importance and develop their infrastructure, further middle-office activities may follow.

The impetus for the Audit came from the policy document, “New Industry, New Jobs”, published by the then Department for Business, Enterprise and Regulatory Reform in April 2009.

“New Industry, New Jobs” identified professional and financial services as one of six priority sectors for development as together they comprise a strong and important sector in the UK economy and there is a need to secure the country’s position as a leading centre of global finance given the current economic crisis. Given the importance of this sector to the economy, this report provides a timely response to the current debate into the UK’s strategic skills needs.

Our study is part of a wider exercise designed to contribute towards the UK Commission's overall response to strategic skills, the National Strategic Skills Audit. This Audit, which is supporting current government-led developments around industrial and skills activism, is comprised of a number of strands, including:

- **A national assessment:** to provide a strategic national overview and assessment of immediate and emerging priority skills needs in both existing and emerging industries. This will also include a regional assessment, providing a consistent and comparable skills assessment across the UK;
- **Priority sector assessments:** to provide an assessment of the skills needs of selected priority sectors; and
- **Horizon scanning:** to provide an assessment of what the future may hold by scanning the horizon, exploring important emerging issues and developments and bridging policy-making in the short and long term.

Scope of research

The scope of this research is the financial services sector, which is comprised of retail and wholesale banking, insurance and asset management. The sector was selected for analysis on the basis of its importance to the UK economy.

These activities are covered by section K of the UK's 2007 Standard Industrial Classification (SIC) of Economic Activities, "Financial and insurance activities." This is also the area of activity covered by Financial Services Skills Council (FSSC) data. In addition to the segments above, these data sources also cover "Other financial intermediation not elsewhere classified," "Administration of financial markets" and "Activities auxiliary to other financial intermediation not elsewhere classified." However, we have not focused on these segments in this report due to the diversity of activities they cover and the relatively small share of employment they comprise (13 per cent in 2008).

Financial services are normally segmented along the three main activities of banking, insurance and asset management. We have used a further cross-cutting segmentation by customer type of retail vs. wholesale, as there are a different set of drivers relevant to each. For retail, we define customers as individuals and small and medium enterprises; for wholesale, we define customers as large corporations (typically international in profile), financial services companies themselves and government/public sector organisations.

Professional services, including those linked to financial services, such as accountancy, are not within the scope of this report.

The research has also taken into consideration relevant international trends and regional implications within the UK.

Objectives of this study

The objectives of this study into financial services can be summarised as follows:

- develop an overview of the economic, social and technical drivers of change for the chosen sectors and a discussion of why the sector is so important to the economy;
- develop an in-depth analysis of global and national trends in skills and employment within a selected sector; including skills insight and foresight and labour market impact. This needs to give consideration to the priority skills within the sector; and
- consider future challenges and trends for the sector, outline possible alternative sector scenarios and implications and consider how they impact on the labour market and skills requirements.

Our approach

Our study is based on in-depth desk research, interviews with industry stakeholders, analysis and scenario development to help the UK Commission understand the future skills needs of the financial services sector. It provides both a qualitative and quantitative view of these requirements and how they may evolve in the long-term. In conducting our analysis, we have drawn on the existing literature and national data on skills in the financial services sector. We have also consulted with the FSSC, trade associations, employers and PwC's Financial Services team.

Key findings on current employment and skills

Different sources indicate that the financial services industry employs between 1m and 1.2m people. This represents c.4 per cent of the total UK workforce. Employment is weighted towards the banking segment (51 per cent of total financial services), followed by insurance (30 per cent), then asset management (6 per cent). The majority of employment falls within retail (63 per cent of total financial services) and retail banking as an individual segment employs 38 per cent of the financial services workforce. The sector is highly productive, generating GVA per head in excess of £100,000 and awarding average remuneration of over £40,000. Between 1998 and 2007, industry output doubled, but employment increased by only 2.2 per cent as productivity rose significantly. This was mostly due to wholesale activities, centred on London, and a reduction in the number of low value-adding support roles, either through technology or offshoring.

More than any other sector, employment in financial services has come under pressure in the recession. Anecdotal evidence suggests that total employment may have declined between 5 per cent and 10 per cent since it peaked in 2007. It is unlikely that the full impact of the financial crisis has yet been felt, so there may be more job losses to come. As this report is being written, the UK is the midst of a debate about banking remuneration and the behaviours it should be designed to encourage.

Financial services employees are generally educated to a higher level than the national average, with many positions requiring National Qualifications Framework (NQF) Level 4 or above. However, there are persistent skills deficits in financial services, although these are more pronounced in certain subsectors than others.

- Retail financial services generally suffer greater skills gaps and shortages than wholesale financial services. Retail financial services, which generally requires lower level qualifications and where a significant share of employees are school-leavers, is less attractive compared to competing sectors such as high-street retail. Financial services companies providing wholesale services have historically offered very generous remuneration packages, enabling them to attract the brightest people;
- Furthermore, insurance, in both the retail and wholesale markets, is less attractive to high-quality candidates than banking. In the wholesale market, there is a remuneration disparity with other financial services companies, in particular investment banks;
- There are shortages and gaps in both generic and sector-specific skills, as outlined in Table 1. It is worth noting that entry-level candidates for retail financial services jobs often lack the basic numeracy, problem-solving and people skills required, as well as basic industry and product knowledge;
- Skills relating to risk management and risk assessment are weak. Due to a lack of investment in this area, there is a current shortage of experienced and qualified risk managers and the shortage has been exacerbated by the need to respond to the financial crisis;
- There is a shortage of management and leadership skills across the sector;
- UK candidates for wholesale financial services positions have weaker language and cultural awareness skills than their non-UK counterparts;
- There are also sector-specific shortages, even for highly-skilled, well-paid jobs. For instance, there is an acute shortage of actuaries in the insurance industry. Investment banks have also noted a difficulty in recruiting UK graduates with sufficiently advanced mathematics skills, although they are generally able to source appropriate people from abroad.

Table 1: Summary of identified skills gaps and shortages in the financial services sectors

	Banking		Insurance		Asset Management
Subsector	Retail	Wholesale	Retail	Wholesale	Retail & Wholesale
Estimated direct employment in 2007	398,000	136,000	267,000	50,000	67,000
GVA (2008)	£62.1bn		£15.4bn		£9.6bn
Specific skills gaps and shortages	Sales and customer service roles (National Qualifications Framework (NQF) Level 1 - 3) Retail Bank Managers (NQF Level 4)	Professional & technical staff (NQF Level 5) - time lag between new specialisms being created and individuals having the necessary skills. Managers and Senior Officials (NQF Level 6)	Actuaries (NQF Level 5) Specialist underwriters (NQF Level 5) Compliance Staff (NQF Level 5) Claims professionals (NQF Level 3) Information technology (IT) and Legal Staff (NQF Level 3)	Actuaries (NQF Level 5) Risk managers (NQF Level 5) Capital modelling (NQF Level 5) Accountants (NQF Level 7) Internal auditors (NQF Level 7) Price reserving Lloyd's Exam Brokers	Professional and technical staff (NQF Level 6) Compliance roles (NQF Level 5) Experience of derivatives and structured products Back office roles
Generic skills gaps and shortages	Management and leadership skills Self motivation and direction Industry knowledge Numeracy & literacy Understanding client needs	Product and industry knowledge Managerial 'soft skills' - ability to cope with stress and positive management of staff relationships. Complex mathematics / statistics	Industry and product knowledge Self motivation and direction Management and leadership skills	Management and leadership skills IT skills Numeracy Business language	Technical and product knowledge Management and leadership skills IT skills Positive management of staff relationships

Note: See Annex B for the NQF framework
Source: PwC analysis

Future outlook for employment and skills

The outlook for the financial services sector has changed significantly as a result of the financial crisis. Future levels of employment in the sector will depend on the government's response on regulation, the need for efficiency, consumer demand and globalisation.

We have developed a series of scenarios which illustrate a set of possible future states of the retail and wholesale financial services sectors. In five of our six scenarios, employment in financial services declines due to tighter regulation, a shift in consumer demand towards saving rather than credit and a gradual loss of wholesale market share relative to other international financial centres. Most of the scenarios, supported by our research and interviews, suggest that overall employment is unlikely to return to 2007 levels in the next decade, and could remain significantly lower. Specifically:

- wholesale financial services employment is the most volatile, particularly in investment banking and asset management. Employment is dependent on London's position as a global financial centre and there is an argument that this will be gradually eroded between now and 2020 as trade and capital shift to emerging economies; and
- employment in retail banking and insurance is less volatile, but as these sectors comprise the majority of financial services employment, a small percentage decline would still result in materially lower employment.

Overall, our view tends towards the more pessimistic of our scenarios. Whichever scenario emerges, it is likely that the distribution of jobs along the financial services value chain¹ will change. We expect the shift towards higher-value, higher-skilled jobs we have seen in the UK to continue as certain functions are moved abroad or automated.

- Efficiency will be paramount in retail financial services as companies look towards recovery and the need to restore margins and profitability. There will be continuing job losses due to branch closures and moves towards more efficient distribution channels (phone and internet), negatively impacting front-office employment;
- Regulation could potentially limit the freedom of banks to innovate and result in polarised banking business models, with some banks focusing on core retail banking services, generating lower but more stable returns, and niche providers serving clients willing to take greater risk. Utility banks will seek to regain the trust of their customers, with positive implications for customer services employment. Recent marketing by banks such as NatWest, for instance, showcases the personal relationships financial advisers build with clients;
- As emerging economies become more important, client-facing front-office functions in wholesale markets will need to be established close to international clients. However, London-based clients will still need to be serviced from London;

¹ The value chain comprises the front office (customer-facing) and middle and back offices (support)

- Globalisation and technology advances have enabled financial services companies to fragment their activities geographically to achieve cost savings. Significant proportions of the back-office have been exported to developing economies such as India and we expect this trend to continue and extend towards some middle-office monitoring and control functions, although some of these will need to remain close to the main financial exchanges.

There is likely to be a significant change in the provision of personal financial advice as a result of the Retail Distribution Review (RDR). New regulations will mean many independent financial advisers (IFAs) leave the market and encourage insurance and asset management companies to develop alternative sales channels.

In the next decade, there are likely to be many changes in the type of skills needed by the financial services industry. New roles will be created and existing roles modified or expanded. Most of the impact will be on the jobs that already exist; employees working at all levels in financial services organisations will need these skills in the new environment.

- Risk management and compliance skills, driven by greater regulation of financial services companies (both wholesale and retail) and demand for transparency among stakeholders. The need will be strongest in banks, which are likely to experience the greatest change in regulation, but insurance companies will not be exempt. Whatever the extent of increased regulation, there will be a greater need for accountants, actuaries and other professionals capable of assessing and monitoring financial risk. A new attitude towards and greater awareness of risk will also need to permeate financial services companies;
- Product knowledge and advice skills. The Thoresen review recommends establishing a free generic financial advice service targeted at less affluent customers which would impact the need for these skills in the third sector;
- In the wholesale sector, it is widely recognised that many financial services companies did not understand the risks associated with the complicated products they were buying and selling. While the effect will be most strongly felt by front-office staff, the need for better understanding will span all areas of financial services companies – middle-office staff and board members cannot control and assess the risk of front-office activities without fully understanding the products;
- Cultural and language skills will become more important as more business originates from emerging markets.

The government has a critical role to play in managing the sector in the medium-term and is currently formulating its response to the crisis, both in terms of regulation and remuneration and in terms of its role in supporting banks as a shareholder or a lender of last resort. The government's response will shape not only the structure of the sector and its competitiveness, but ultimately will impact upon levels of employment and the types of skills that will be required.

Six possible scenarios for the financial services sector

We have developed a set of scenarios illustrating potential future states for the financial services industry in 2020, based on analysis of the findings from desk research and interviews with industry stakeholders relating to the drivers for change in the industry.

Due to differing industry drivers, we have developed a separate set of scenarios for retail financial services and wholesale financial services. The primary drivers of retail financial services are regulation and consumer demand. For wholesale financial services, these drivers are regulation (relative to other jurisdictions) and the pace of globalisation.

The retail scenarios are:

- Scenario R1: "Laissez faire," characterised by light regulation and consumer appetite for credit – a scenario that is similar to the last decade;
- Scenario R2: "Sustainable consumer finance," characterised by moderate regulation and more balanced consumer attitudes; and
- Scenario R3: "Utility financial services," in which restrictive regulation constrains innovation and consumers have cautious attitudes to credit and a greater appetite for savings.

The wholesale scenarios are:

- Scenario W1: "Business as usual," in which the UK retains a light-touch regulation and the pace of globalisation is relatively slow, favouring London's position as a global financial centre;
- Scenario W2: "Sustainable global finance," characterised by moderate regulation that is consistent with other jurisdictions. The pace of globalisation means the UK, centred on the City of London, loses some share as a financial centre, but its position remains supported by strong infrastructure; and

- Scenario W3: “Shift to the East,” in which the UK regulatory environment is more restrictive than other jurisdictions and the pace of globalisation accelerates a shift of wholesale business to other financial centres in emerging markets.

In five of our six scenarios, employment in financial services declines due to tighter regulation, a shift in consumer demand towards saving rather than credit and a gradual loss of wholesale market share relative to other global financial centres. Most of the scenarios, supported by our research and interviews, suggest that overall employment is unlikely to return to 2007 levels in the next decade and could remain significantly lower.

The remainder of the executive summary is drawn from the chapter summaries and includes our more detailed findings about the current state of the banking sector, the insurance sector and the asset management sector.

Industry insight: banking

The banking sub-sector is the largest within financial services, with a workforce of c.534,000 people. Retail banking employs nearly three times as many people as wholesale banking, with c.398,000 workers, compared to c.136,000 in wholesale. There is a distinct concentration of employment in London and this is particularly prevalent in wholesale banking, with c.42 per cent of this workforce located in the capital. Wholesale employment levels have fallen significantly in the last two years as many banks have laid-off staff.

Retail banking occupations can be split generally into front-office positions and back- and middle-office positions. Front-office roles are those typically found in branches and customer support centres, such as clerks and sales, marketing and telephone support staff. Back- and middle-office functions include credit control managers, risk analysts, information technology (IT) support and compliance staff. Employees in this sector tend to have lower qualification levels.

Retail banking appears to have significant skills shortages and gaps. Retail banking does not enjoy the same attractiveness as wholesale banking relative to the sectors it competes with for candidates and as a result, recruitment is more difficult. 77 per cent of banks and building societies responded that they suffered from skills shortages. Retail banks also suffer from skills gaps, mainly in the areas of product and sector knowledge, as well as general motivation and “job readiness”.

Wholesale banking follows a similar structure to retail banking, although front-office roles reflect the corporate and institutional nature of wholesale banking and include corporate relationship managers, finance analysts, finance and mergers & acquisitions (M&A) advisors and product design staff. Support roles are similar to those in retail banking and include staff working in risk analysis, compliance, IT support and credit control, although there is generally a larger product control division as well as finance settling function.

Skills deficits in wholesale banking are less pronounced than in retail banking. It has historically been a destination of choice for graduates of all qualification levels and is able to attract talented staff, often with Level 5 qualifications or sector-specific training from bodies such as the CFA (Chartered Financial Analyst) Institute or the Chartered Institute for Securities & Investment. Furthermore, once these high-calibre individuals are hired, significant investment in training ensure that they are developed further.

As a result, wholesale banking employers generally do not suffer from significant skills gaps and shortages. Where deficits have been identified, these relate to quantitative analytical skills and a general lag in understanding as staff become acquainted with new financial products. However, much of the responsibility for the financial crisis in this sub-sector has been attributed to poor management and leadership in the sector, as well as a lack of understanding of risk.

Industry insight: insurance

The insurance sub-sector is a large component of financial services, with a workforce of c.317,000. For the purposes of this report, we have broken it down into three main segments:

- life and pensions;
- general insurance (also called non-life); and
- reinsurance.

While life and pensions generates the largest annual premiums, general insurance is the largest segment by employment, with approximately a third of insurance workers involved directly in the sector (c.106,000), compared to c.72,000 directly employed in life and pensions. The wholesale insurance sector employs c.50,000 people, of which 80 per cent are located in London. The remaining c.89,000 workers in insurance are employed in various support functions, including agency, brokerage and risk assessment.

The segments are affected by different drivers: life and pensions businesses have been strongly affected by the financial crisis because of falling interest rates driving up liabilities and poor investment performance; general insurance tends to be more resilient.

There are different skills needs for the different segments. Most positions in retail insurance require basic quantitative skills and experience tends to be more important than qualifications. However, in wholesale insurance, strong quantitative analysis skills are more valued and qualifications from bodies such as the Chartered Insurance Institute (CII) are important.

There has been a historical trend of outsourcing non-core functions, with some of these moved offshore. Along with general improvements in efficiency, this has resulted in a decline in total employment in the sector.

Insurance has traditionally had difficulties in attracting the most highly qualified candidates to the industry as the industry lacks the appeal and financial rewards of other financial services careers such as wholesale banking or asset management. Senior roles in the sector tend to be occupied by middle-aged, white middle-class men. As the industry is largely based on experience rather than qualifications, it is difficult for people to transfer into the industry.

There are several key skills shortages apparent, due to a lack of applicants and the ageing workforce. There are particular shortages of actuaries, which will intensify as demand increases while supply is held back by long training periods, low pass rates and low industry attractiveness. There are also likely to be shortages of risk management, IT and operations staff in the near- to medium-term future.

The key skills gaps are found in entry-level positions, typically filled by school leavers and graduates, who lack basic industry and technical knowledge. It is reported that some senior staff can lack appropriate management skills.

Industry insight: asset management

The asset management sub-sector is the smallest within financial services, employing c.67,000 people. Asset management can also be segmented into retail and wholesale, with retail asset management servicing individuals and wholesale asset management looking after funds for institutions². Hedge funds and other alternative investment funds are a niche sector of wholesale asset management. Retail investors account for a small share of total assets funds and many products (e.g. mutual funds) are managed in the same way as products for wholesale customers.

The core asset management activity – including investment research, management of investment portfolios, trading and broker liaison – accounts for approximately a quarter of all employees. Marketing and distribution functions, including sales and business development, make up a further 21 per cent of employment. The remaining 54 per cent comprises middle- and back-office functions.

Asset management is a geographically concentrated segment, with 74 per cent of employment in London, although Edinburgh is also an important centre.

Front-office asset management roles are generally filled by individuals with graduate or post-graduate qualifications and employers expect entrants to be numerate and possess a good degree. Those looking for roles in asset management are required to have a strong quantitative reasoning ability to develop strong investment and risk analysis skills. Junior roles do not have to be registered with

² Wholesale investment management can also be defined as white-label products. However, for the purposes of this report, we have split asset management between retail and wholesale in the same way as for the other financial services sectors

the Financial Services Authority (FSA). However, senior asset managers with responsibility for funds have to be registered with the FSA and pass appropriate exams.

There are skill shortages in the industry, with a shortfall of people with qualifications directly relevant to the sector's needs. A lack of experience and technical knowledge is the most common shortage. Back office and support functions are historically difficult to recruit for, as highly skilled applicants are put off by a lack of clear career paths and the impression that the roles are under-rewarded.

School leavers and graduates and administrative staff are the most likely to have skills gaps, while professionals and technical staff are less likely to lack skills. Industry and product knowledge was found to be lacking by 30 per cent of employers, while 28 per cent reported a lack of technical knowledge. It has been reported that even senior staff can lack an understanding of the investments that they manage. Soft skills such as relationship management also need to be developed at many companies.

1 Introduction

1.1 Background to research

PricewaterhouseCoopers LLP (PwC) was commissioned by the UK Commission for Employment and Skills (the UK Commission) in September 2009 to provide an assessment of the skills needs in the low carbon energy generation sector to support its work on the National Strategic Skills Audit for England, 2010. The impetus for the Audit came from the policy document, “New Industry, New Jobs”, published by the then Department for Business, Enterprise and Regulatory Reform in April 2009. In it, the authors emphasise the importance of a more strategic approach to skills in the changing economy:

“... the government also has to do more to help equip high potential British firms. We need to take a range of actions. We must improve the skills of our people and adapt them to the specialist demands of a modern economy; strengthen our capabilities in research and development; innovate further in science and technology, and industrialise this innovation in commercially successful ways. These actions are the bridges to our economic future.”

“New Industry, New Jobs” identified professional and financial services as one of six priority sectors for development as together they comprise a strong and important sector in UK economy and there is a need to secure the country’s position as a leading centre of global finance given the current economic crisis. Given the importance of this sector to the economy, this report provides a timely response to the current debate into the UK’s strategic skills needs.

Our study is part of a wider exercise designed to contribute towards the UK Commission’s overall response to strategic skills, the National Strategic Skills Audit. This Audit, which will support current government-led developments around industrial and skills activism, comprises a number of strands, including:

- **A national assessment:** to provide a strategic national overview and assessment of immediate and emerging priority skills needs in both existing and emerging industries. This will also include a regional assessment, providing a consistent and comparable skills assessment across the English regions;
- **Priority sector assessments:** to provide an assessment of the skills needs of selected priority sectors; and
- **Horizon scanning:** to provide an assessment of what the future may hold by scanning the horizon, exploring important emerging issues and developments and bridging policy-making in the short and long term.

- The 25 employer-led Sector Skills Councils are, at the same time, reporting to the UK Commission on their individual sectoral skills priorities while also working in 'clusters' examining the skills needs in six key areas to enable the UK Commission to triangulate the overall skills needs of the UK economy to 2020 and to help inform the planning of higher and further education provision in the years to come.

1.2 Scope of research

The scope of this research is financial services, which is comprised of wholesale and retail banking, insurance and asset management. This sector was selected for analysis on the basis of its importance to the UK economy. This research includes:

- banking;
- insurance; and
- asset management.

These activities are covered by section K of the UK's 2007 Standard Industrial Classification (SIC) of Economic Activities, "Financial and insurance activities." This is also the area of activity covered by FSSC data. In addition to the segments above, these data sources also cover "Other financial intermediation not elsewhere classified," "Administration of financial markets" and "Activities auxiliary to other financial intermediation not elsewhere classified." However, we have not focused on these segments in this report due to the diversity of activities they cover and the relatively small share of employment they comprise (13 per cent in 2007).

Within each of these sub-sectors, we have considered different customer types, including:

- individuals;
- businesses/corporations;
- financial services companies; and
- government and public sector organisations.

Segmentation of financial services is considered in Section 2.

Professional services, including those linked to financial services, such as accountancy, are not within the scope of this report.

The research has also taken into consideration relevant international trends and regional implications within the UK.

1.3 Objectives of this study

The objectives of this study into financial services can be summarised as follows:

- develop an overview of the economic, social and technical drivers of change for the sector and a discussion of why the sector is so important to the economy;
- develop an in-depth analysis of global and national trends in skills and employment within the sector, including skills insight and foresight and labour market impact. Consider the priority skills within the sector; and
- consider future challenges and trends for the sector, outline possible alternative sector scenarios and implications and consider how they impact on the labour market and skills.

1.4 Methodology

Our study is based on in-depth research, analysis and scenario development to help the UK Commission understand the future skills needs of the financial services sector. It provides both a qualitative and quantitative view of these requirements, and how they may evolve in the long-term. We have drawn on the existing literature and national data on skills in the financial services sector and consulted the FSSC, trade associations, employers and PwC's financial services team.

The remainder of this report is structured as follows:

- Industry insight: Overview;
- Industry insight: Banking;
- Industry insight: Insurance;
- Industry insight: Asset management;
- Industry foresight;
- Scenarios; and
- Conclusions.

It also contains four annexes:

- Annex A: Occupations in the financial services sector;
- Annex B: The National Qualifications Framework;
- Annex C: Glossary; and
- Annex D: Bibliography.

2 Industry insight: Overview

Chapter summary

The financial services sector is a major part of the UK economy and its wide range of sub-sectors and activities makes pinpointing an exact employment number difficult. Different sources indicate that the financial services industry employs between 1m and 1.2m people. This represents c.4 per cent of the total UK workforce. The sector is highly productive and generates 8 per cent of total UK output, as measured by GVA. The industry average GVA per head is in excess of £100,000 and average remuneration is over £40,000.

Employment is weighted towards the banking segment (51 per cent of total financial services), followed by insurance (30 per cent), then asset management (6 per cent). The majority of workers fall within retail (63 per cent of total financial services) and retail banking as an individual segment employs 38 per cent of the financial services workforce. However, the wholesale segment, centred in the City of London that is the more productive.

Employment levels have remained largely stable between 2002 and 2008, although this masks a shift in employment levels between sectors. Employment in insurance declined by 14 per cent between 2000 and 2006, driven by corporate losses sustained subsequent to 11 September 2001, consolidation within the market and market reforms. This has been largely offset by increases in the wholesale financial services industry. However, the recent financial crisis has caused high levels of retrenchment amongst financial services companies and while no firm figures on total job losses are currently available, anecdotal evidence would suggest total financial services employment has fallen between 5 per cent and 10 per cent.

Within the financial services value chain, there are a wide range of jobs, although managerial, technical and professional occupations are the most prevalent. Employment in supporting back-office functions is higher than the national average, reflecting the importance of administration, paperwork and record-keeping in the sector and the degree of regulation. Financial services employees are generally educated to a higher level than the national average, with many positions requiring National Qualifications Framework (NQF) Level 4 or above. However, for many financial services companies, there are no set qualifications required for employment.

The main identified technical skills deficits within the industry were:

- the ability to perform complex quantitative reasoning;
- skills relating to risk management and risk assessment (due to a lack of investment in this area, there is a current shortage of experienced and qualified risk managers);
- a thorough and balanced set of soft skills, with many industry surveys finding that new hires often lacked simple skills related to customer handling, communication and problem solving;
- language skills and cultural awareness among UK workers compared with foreign workers in some sub-sectors; and
- basic industry and product knowledge among school leavers and graduates.

2.1 Introduction

Financial services are a key part of the UK economy, making up over 8 per cent of total UK output³. The financial services sector is subject to high levels of scrutiny due to the importance of the sector to the UK economy and the recent financial crisis has focused national and international attention on the regulation and governance of the sector⁴.

The Office for National Statistics (ONS) describes financial corporations as those primarily engaged in financial activities and subdivides them into monetary financial institutions; other financial intermediaries and financial auxiliaries; and insurance corporations and pension funds⁵. In practice, financial services can be broken down along two dimensions – the type of activity carried out (banking, insurance or asset management) and the target customer group.

The main providers within UK financial services are high-street names and most individuals in the country have some form of interaction with a financial services provider, whether through the provision of a current account; the funding of a major purchase such as a house or car; insuring day-to-day or long-term risks; or through managing their savings and assets.

This chapter describes the financial services market in the UK, with more detailed insights into each of the subsectors within financial services in subsequent chapters. This will provide a backdrop to our research and to the scenarios for financial services to 2020. This chapter will cover at a high level:

- Current state of the UK market;
- Current employment;
- Characteristics of employees;
- Occupations;
- Current skills profile and provision; and
- Unfulfilled skills needs.

³ ONS

⁴ Various media; Factiva

⁵ ONS (2009) The Blue Book

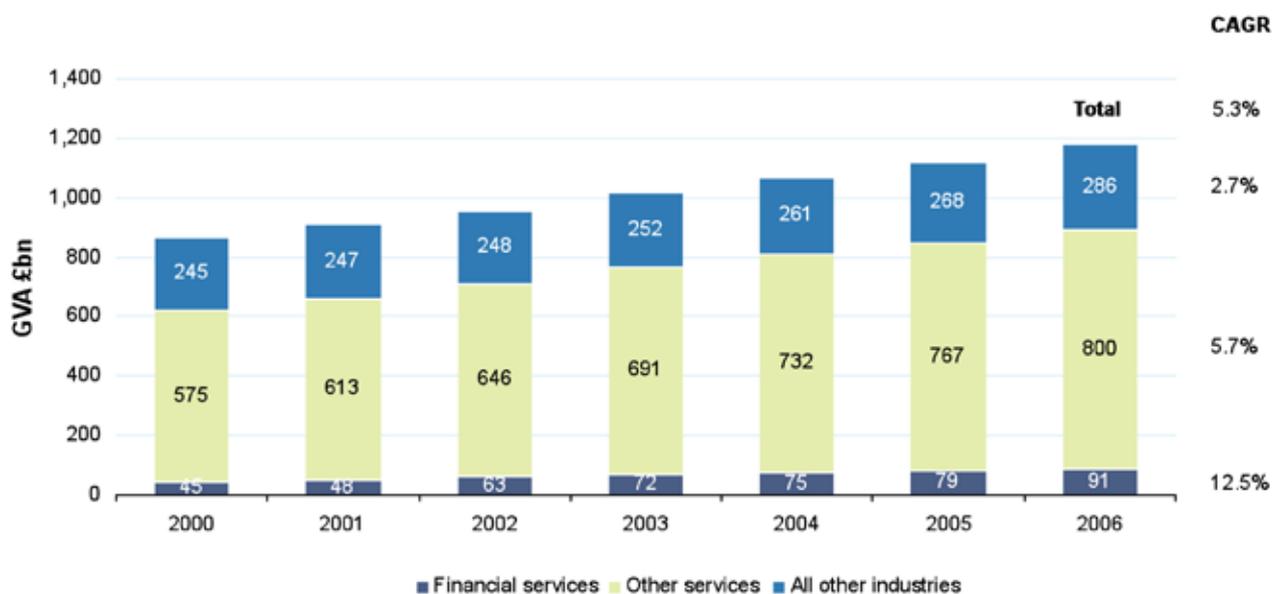
2.2 Current state of the UK market

This section of the report considers the current state of the UK financial services market, in terms of its importance to the UK economy; market segmentation; growth in the sector in recent years; the regional distribution of the sector across the UK; market supply; and regulation of financial services, particularly in the context of the current economic crisis.

2.2.1 Importance to the UK economy

In order to capture the importance of financial services relative to the other sectors of the economy, and to draw comparisons between banking, insurance and asset management, we have used gross value added (GVA)⁶ as a key measure. Financial services comprise one of the most important sectors in the UK economy and, historically, one of the most productive, with average GVA per head in excess of £100,000 and average remuneration in excess of £40,000⁷. Figure 1 shows the relative importance of financial services in the broader economy and its relative growth since 2000. Growth in GVA during the boom market that ended in 2008 was over twice that of the UK economy as a whole.

Figure 1: GVA of financial services as part of the total UK economy, 2000-2006



Source: Office for National Statistics (QTPR, QTPZ, ABML)

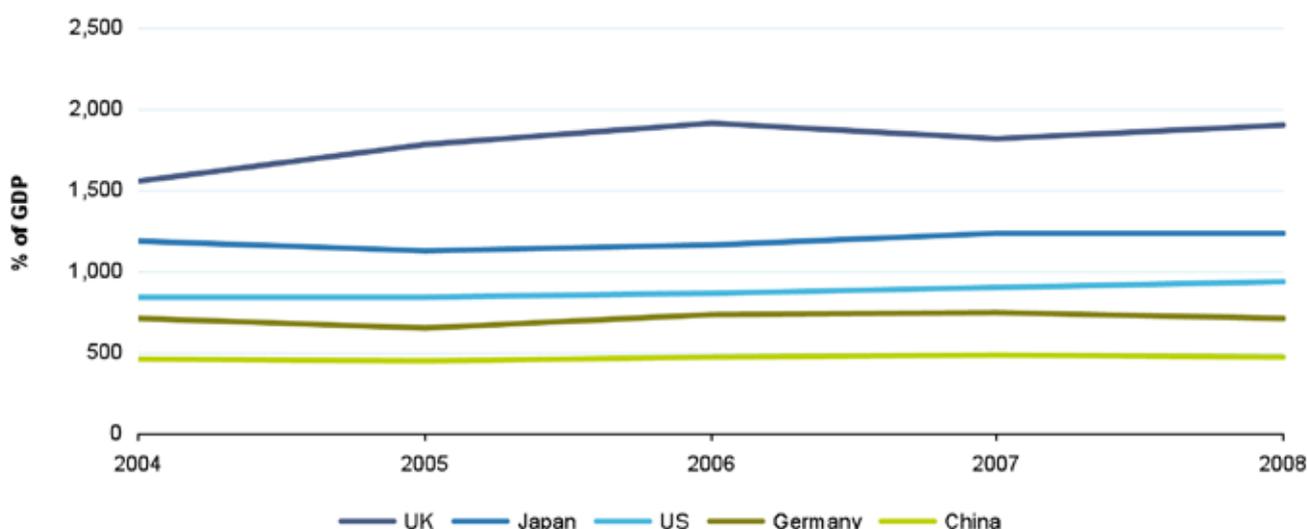
⁶ The Office for National Statistics defines GVA as: GVA (at current basic prices; available by industry only) plus taxes on products available at whole economy level only) less subsidies on products (available at whole economy level only) equals GDP (at current market prices; available at whole economy level only).

⁷ ONS (2009) The Blue Book

The sector is one of substantial employment, with over 1m people employed in the financial services activities and support functions. Workers in financial services are generally highly skilled and have higher levels of attainment at Levels 3 and above than the wider UK economy⁸.

The majority of the UK’s international financial services activity is carried out in London. The volume of activity, particularly in wholesale financial activities, has made London one of the world’s most important financial centres. Compared with other countries, financial services are more important to the UK than elsewhere, particularly in the years immediately preceding the financial crisis. This is evidenced by the ratio between financial assets (non-physical assets such as securities, bank deposits and loans) and gross domestic product (GDP) of a selection of leading economies (Figure 2).

Figure 2: Financial assets in selected major economies as a per cent of GDP, 2004-2008



Source: Economist Intelligence Unit (2008)

At the peak of the boom in 2007, the UK had established itself as the leading global financial market. In spite of the current financial crisis, and the growing importance of emerging financial centres in Asia, London has maintained its premier position in the latest Global Financial Centres Index (GFCI), a ranking study commissioned by the Corporation of London (Table 2)⁹.

⁸ ONS (2008) LFS/IER

⁹ City of London Z/Yen Group (2009) Global Financial Centres Index 6, September 2009

Table 2: GFCI Ranking, September 2009

Centre	GFCI 6 Rating (September 2009)	GFCI Rank	Change in Rating since GFCI 5 (March 2009)	Change in Rank since GFCI 5
London	790	1	9	0
New York	774	2	6	0
Hong Kong	729	3	45	+1
Singapore	719	4	32	-1

Source: City of London and Z/Yen Group (2009)

When it was last published in 2008, the MasterCard Worldwide Centres of Commerce Index – another ranking of financial centres – also ranked London first¹⁰. The city is recognised as having a business environment that is conducive to financial services, with excellent support services and strong infrastructure. London is also ideally located between the American and Asian time zones and has close proximity to continental Europe.

2.2.2 Market segmentation

Financial services are normally segmented along the three main activities of banking, insurance and asset management. We have used a further cross-cutting segmentation by customer type of retail vs. wholesale, as there are a different set of drivers for these customer types. For retail, we define customers as individuals and small and medium enterprises; for wholesale, we define customers as large corporations (typically international in profile), financial services companies and government and public sector organisations. Within the wholesale segment, London is the dominant UK region in all three areas of banking, insurance and asset management.

- **Banking:** the majority of the financial services market is occupied by banking activities. This includes high-street banking, personal and business lending; debt and equity instruments for capital-raising; and the trading of equity, debt, fixed income assets, currencies and commodities. Banking advisory services are also included in this segment.
- **Insurance:** the act of providing a guarantee to compensate consumers should a risk become realised. There are two main aspects to the insurance market: the actual provision of the insurance and underwriting of risk; and the investment management of the funds received from insurance premiums.

¹⁰ http://www.mastercard.com/us/company/en/insights/pdfs/2008/MCWW_WCoC-Report_2008.pdf

- **Asset Management:** a much smaller segment of financial services, but with some of the largest profit margins and returns in any industry. Asset managers either actively manage the investment components of a fund based on experience, knowledge and insight, or passively manage a pool of assets by tracking the fund to a set index (such as the FTSE 100). The majority of the sector is made up of institutional investment managers of pension and mutual funds.

These activities can also be divided into retail and wholesale:

- **Retail:** the provision of financial services to individuals and small & medium enterprises (SMEs), which is characterised by high volume, low value activity. It is almost exclusively confined to the domestic market;
- **Wholesale:** the provision of financial services to large business or corporations, typically with international operations; financial services companies; and government and public sector organisations.

Within the resultant segments there are a range of products and services that are offered by banks, insurance companies and asset managers. These are illustrated in Table 3.

Table 3: Financial services products, segmented by activity and customer type

Customer	Retail		Wholesale		Government
	Individuals	Businesses / Corporations	Small & Medium Enterprises (SMEs)	Large Corporations	
Banking	<ul style="list-style-type: none"> •High street banking •Banking to individuals via telephone and internet •Products include current and savings accounts, loans, credit cards and mortgages 	<ul style="list-style-type: none"> •Banking to SMEs via high street branches, telephone and internet •Products include business accounts, business loans, payroll services and so on. 	<ul style="list-style-type: none"> •Banking to large corporations often with international operations •Products include the issuing of commercial bonds and stock, capital raising, corporate finance / M&A advice and foreign exchange 	<ul style="list-style-type: none"> •Banking between banks, typically large banks with international operations •Products include inter-bank trading, capital markets activity, proprietary trading, and foreign exchange. 	<ul style="list-style-type: none"> •Bond issuances •Asset disposals •Project financing
Insurance	Life and Pensions	<ul style="list-style-type: none"> •Life insurance, pensions and long-term investment products for individual customers 	<ul style="list-style-type: none"> •Group pension schemes for groups of individuals / employees, typically for large employers (corporations and financial services companies) 		
	General	<ul style="list-style-type: none"> •Personal products for individuals including home, motor and health insurance 	<ul style="list-style-type: none"> •Commercial products for businesses including commercial and professional indemnity, property and buildings insurance, business continuity, disaster/emergency insurance •Commercial products often referred to as wholesale business 		
	Reinsurance	<ul style="list-style-type: none"> •n.a. 	<ul style="list-style-type: none"> •n.a. 	<ul style="list-style-type: none"> •Reinsurance of a wide range of specialist risks, typically international in nature, including aviation, marine, life and financial risks* 	
Asset Management	<ul style="list-style-type: none"> •The asset management market for individuals is small and dedicated to a relatively small number of high net-worth individuals 	<ul style="list-style-type: none"> •n.a. 	<ul style="list-style-type: none"> •The majority of asset management activities are carried out on behalf of large corporate clients, financial services companies or public sector organisations Includes pension, insurance or mutual fund management, private equity and venture capital, hedge funds or sovereign wealth funds. 		

Source: PwC analysis

2.2.3 Industry growth

Banking accounts for 59 per cent¹¹ of total financial services GVA and has been the primary source of growth in the sector over the last 15 years. The insurance market, which accounts for 15 per cent of financial services GVA, is relatively mature in the UK and has grown only modestly over the same period. Asset management accounts for 9 per cent of GVA and has grown strongly on the back of buoyant financial markets. Other financial services, including the administration of financial markets, risk and damage evaluation, and financial consulting, account for the remaining 17 per cent of output. Figure 3 presents the growth in the sector from 1994 to the present.

Figure 3: Growth by financial services sub-sector - GVA (1994-2008)



Source: Office for National Statistics (DPIN, DUYN, DUZX, YBFR) and PwC analysis

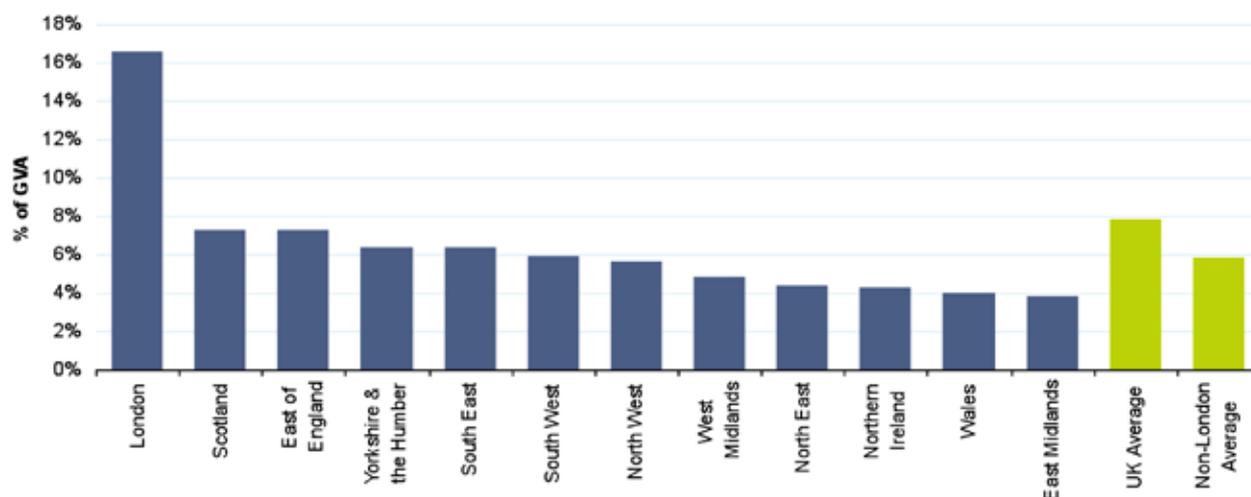
Financial services growth has historically moved in cycles and the industry has recognised several distinct periods of “boom and bust”. Financial services have historically tracked above the wider UK economy in terms of growth rates, although “bust” cycles also tend to cause deeper industry recession. Over the period of 1974-2008, financial services grew over twice as fast as the UK economy, taking into account any shrinkage, to achieve a compound annual growth rate (CAGR) of 4.9 per cent. This is almost 2.5 times as fast as the wider UK economy, which grew at 2.1 per cent p.a.

¹¹ ONS (2008)

2.2.4 Regional distribution in the UK

London has the largest financial services economy, comprising 39 per cent of the national financial services GVA; taken together, London and the South East comprise over half of the UK's total financial services output. The capital has also experienced the highest growth rate of any region since 2000, with an annual increase of c.17 per cent. The higher GVA contribution of London is largely down to the profitability of its wholesale banking segment, made of which is international in nature

Figure 4: Share of GVA generated by financial services, by region/country, 2



Source: Office for National Statistics (DPIN, DUYN, DUZX, YBFR) and PwC analysis

Financial services in Scotland were also growing strongly until the financial crisis. Between 2000 and 2007, the industry grew by c.14 per cent p.a. to £7.6bn¹². This growth was over twice that of the wider Scottish economy¹³. As a result of the crisis, both the Royal Bank of Scotland (RBS) and HBOS suffered heavy losses and were forced to scale down their operations, resulting in a fall in financial services output of over 8 per cent in Scotland in 2008¹⁴. The financial services industry is an important contributor to regional economies across the UK: Edinburgh, Glasgow, Leeds, Manchester, Birmingham and Bristol are also important national centres¹⁵.

2.2.5 Market supply

Financial services in the UK is relatively concentrated, particularly in the banking and insurance sectors.

¹² ONS Statistical Bulletin: Regional, sub-regional and local gross value added 2009 <http://www.statistics.gov.uk/pdfdir/gva1209.pdf>

¹³ ONS Statistical Bulletin: Regional, sub-regional and local gross value added 2009 <http://www.statistics.gov.uk/pdfdir/gva1209.pdf>

¹⁴ Scottish Executive (2009) The Strategy for the Financial Services Industry in Scotland, 2009 Annual Report.

¹⁵ IFSL (2009) International Financial Markets in the UK

In banking, the “big four” high street banks (Barclays, HSBC, Lloyds Banking Group and RBS) have significant presence across both retail and wholesale banking, due to their full-service propositions.¹⁶ In the retail banking sector, some smaller banks and national building societies also have a significant market share. The total market share for the top 10 retail banks in 2008, prior to the crisis, was 84.6 per cent.¹⁷ There has since been some consolidation in the retail banking sector, notably the acquisition of HBOS by Lloyds TSB.

While the “big four” high street banks have some market share in wholesale banking, there is a larger representation from dedicated international banks, such as JPMorgan, Goldman Sachs, Deutsche Bank and UBS. Standard Chartered, a British bank but without any retail banking operations in the UK, also has market share in wholesale banking.¹⁸

There are 336¹⁹ authorised banks in the UK, of which 254 are from outside the UK.²⁰ The internet is increasingly used as a sales and distribution channel for retail banks, as evidenced by the growth of First Direct, an internet and telephone-only bank.²¹ As of 2005, there were 10,300 bank branches in the UK.²²

The insurance sector has companies present in life and pensions, general insurance, and reinsurance.²³ There were 647 insurance companies authorised in the UK in 2008, of which 489 were general insurers, 133 were life insurers and 25 operated across both market segments. A fifth (21 per cent) of insurers were foreign-owned.²⁴ The five largest companies in the general insurance industry account for 53 per cent of total net written premiums, while the largest 20 companies wrote 83 per cent of total net premiums. In the life insurance sector, the top five companies were responsible for 48 per cent of premiums, while the top 20 took 95 per cent of the market.²⁵ Insurers sell their products through independent financial advisors, intermediaries tied to one or more companies, direct to customers or in conjunction with banking products.²⁶

Asset management has a small number of large companies (as measured by assets under management), although the “tail” for smaller companies is long. The biggest funds hold over £250bn in assets under management.²⁷ Many asset managers are extensions of banks or insurers, with only 32 per cent of assets under management managed by dedicated fund managers.²⁸ The remainder is managed by fund managers within insurance companies, banks and pension funds.

¹⁶ IFSL (2008) Banking

¹⁷ Mintel (2008) Retail Banking Overview

¹⁸ Thomson Deals Intelligence (see: <http://online.thomsonreuters.com/dealsintelligence>)

¹⁹ European Banking Federation (2008) Banking Sector Statistics

²⁰ IFSL (2008) Banking

²¹ first direct results (see: <http://www.firstdirect.com/index.shtml>)

²² European Banking Federation (2008) Banking Sector Statistics

²³ Lloyd's Members 2009

²⁴ IFSL (2008) Insurance

²⁵ Association of British Insurers Rankings 2008

²⁶ Mintel (2009) Life and Protection, Mintel (2008) General Insurance Overview - UK

²⁷ IFSL (2009)

²⁸ IFSL (2009)

2.2.6 Regulation

The division of responsibilities for financial regulation in relation to financial stability is set out in statute as well as in the Memorandum of Understanding between the Tripartite Authorities (HM Treasury, the FSA and the Bank of England). The original Memorandum of Understanding between the Treasury, FSA and Bank of England was published in October 1997 and amended in 2006. The Memorandum outlines the responsibilities of each authority in relation to financial stability and is the key source for the current Tripartite framework.

Financial services in the UK are directly regulated by the FSA, under the Financial Services and Markets Act (2000). Prior to the crisis, the FSA maintained a “light-touch” regulatory model that favoured principles-based regulation rather than stricter rules-based regulation. The FSA is also responsible for promoting the resilience of regulated institutions against operational disruption and for working with regulated institutions to resolve any problems that may prevent them from operating normally. The Bank of England is responsible for the stability of the financial system as a whole and monetary stability. The Treasury has less direct influence over the financial services industry or the wider financial environment, but has responsibility in overseeing the legislative basis of the tripartite regulatory structure and for authorising any support operation in the event of a financial crisis.

2.2.7 The current financial crisis

The financial crisis was the result of a number of factors and circumstances combining to eventually undermine market faith in financial capital adequacy and counterparty trust. The resulting lack of liquidity and capital access meant that many companies were unable to function.²⁹ A broad explanation on the cause and origin of the financial crisis was put forward in a speech by Adair Turner, the chairman of the FSA, in early 2009³⁰. Using this explanation and a variety of other sources, the following points explain the causes of the crisis:

- with low interest rates across the board, banks and other financial institutions found lending money to be extremely profitable and began lending to customers of all profiles and risk groups, fuelling an economic boom, with rising house prices and increased household debt;
- investors and banks were unable to generate satisfactory returns on lower-risk investments such as index-linked government bonds, so increasingly turned to higher profit generating investment vehicles;

²⁹ PwC The Day After Tomorrow Series (available at: <http://www.pwc.com/gx/en/financial-services/day-after-tomorrow/index.jhtml>)

³⁰ Speech by Adair Turner, FSA Chairman; The Economist's Inaugural City Lecture, 21 January 2009

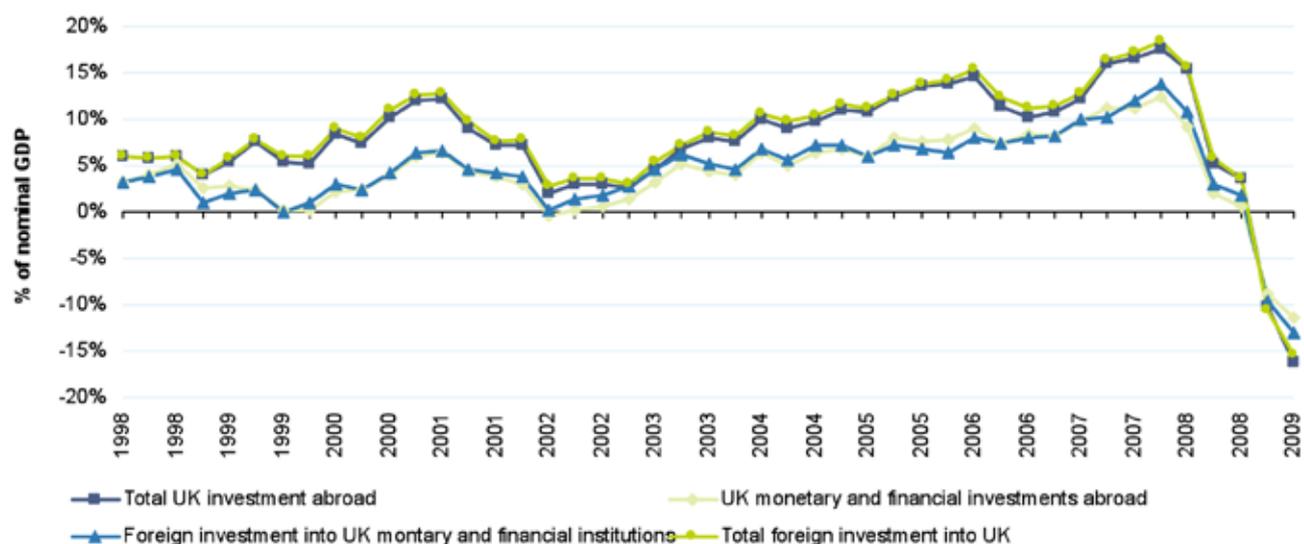
- the consequence was a situation where bankers were generating profit from increasingly sophisticated “securitised” products where the risk of the underlying assets was not fully understood. Rewarded for the increasing profits generated, bankers continued to innovate and trade, thus exacerbating the situation; and
- poor governance and risk assessment meant that banks did not trace the ultimate risk and were unable to manage their exposures.

Overall, trading of securitisation products in the UK grew by 800 per cent between 2000 and 2007.

As a result of the financial crisis, Northern Rock and Bradford & Bingley (the latter now part of Spain’s Santander Group), were completely nationalised, while two of the UK’s largest banks, RBS and Lloyds TSB, received significant government injections to remain solvent. Measures to address imbalances and also to protect against future recurrences have included proposed regulatory reform, shifts in cultural thinking and practice, as well as direct government intervention to rescue companies from bankruptcy.³¹

Since the crisis began, capital flows through London have shrunk abruptly and severely, as global capital flows halted and investors exercised caution in their activities (see Figure 5).³²

Figure 5: UK international capital flows



Source: Bank of England Quarterly Bulletin, Q3 2009

³¹ PwC The Day After Tomorrow Series (available at: <http://www.pwc.com/gx/en/financial-services/day-after-tomorrow/index.jhtml>)

³² World Economic Forum (2009) The future of the global financial system

London's pre-eminence on the international financial scene and the UK's reliance upon financial services as an income-generator have led the country to suffer disproportionately due to the financial crisis. As of the third quarter of 2009, the UK had experienced the longest period of recession since records began in 1955³³. However, the outlook for the financial services sector has recently started to improve.

2.3 Current employment

In order to determine employment figures at an overall financial services level, we have used data from the UK Employment and Skills Almanac (2009) that draws on data from the Labour Force Survey (LFS), the National Employer Skills Survey (NESS) and the Annual Business Inquiry. In the absence of comparative sub-sector data, we have drawn segmented data from other sources including Working Futures, HM Treasury reports and the Annual Business Inquiry itself.³⁴

Table 4: Comparison of financial services employment data sources

Source	Date of publication	Size of financial services workforce (year)	Geographic coverage	Use of data
UK Commission for Employment and Skills Almanac https://almanac09.ukces.org.uk/default.aspx	November 2009	1,229,930 (2008) All jobs covered by the FSSC	UK	Overall financial services employment Historic growth, overall and by region
Annual Business Inquiry	2008	1,054,084 (2007)	Great Britain (excludes Northern Ireland)	Historic growth of financial services by SIC codes (banking, insurance, asset management) and by country/region Excludes self-employed and unpaid workers
Working Futures 2007-2017 (UK Commission for Employment and Skills)	2008	1,107,000 (2007)	UK	Historic and future growth of employment, overall and by job type; historic and future output and productivity
UK international financial services – the future (published by HM Treasury)	May 2009	1,021,000 (no date given)	UK	Cross-segmentation of employment by detailed segment (Wholesale banking, retail banking, insurance, asset management) and by country/region

Source: PwC analysis

³³ National Statistics

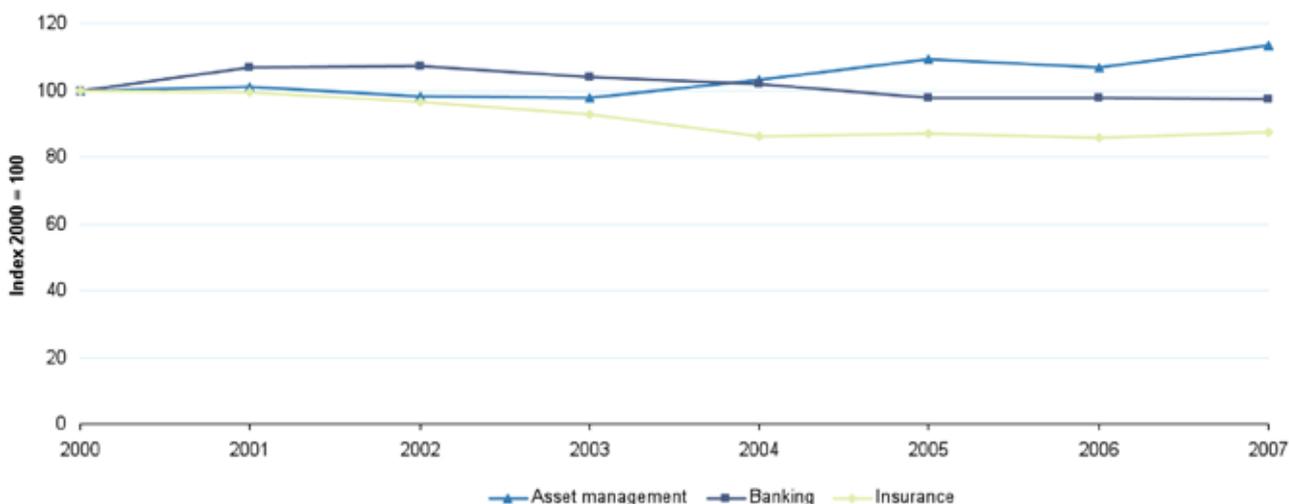
³⁴ Sub-sector level data are for 2006.

According to the UK Commission’s Almanac, financial services employed more than 1.2 million people in 2008, or 4 per cent of the UK workforce.³⁵ In employment terms, the most important sector is retail banking (38 per cent of workers), followed by retail insurance and pensions (25 per cent of workers), corporate and institutional banking (13 per cent of workers) and asset management (6 per cent of workers) and wholesale insurance (5 per cent of workers), with the remaining small percentage working in other segments of the industry.³⁶

Although the economic importance of financial services has increased significantly in the last ten years, increased productivity has kept the number of people employed in the sector relatively stable. In the four years between 2002 and 2005, financial services employment grew by 0.8 per cent per year and decreased by 0.4 per cent per year between 2005 and 2008 (Figure 6). The financial crisis – which is not captured by this historic data – has had a significant impact on employment and is discussed in more detail later in this section.

There has been a shift in the levels of employment within the subsectors, with the number of employees in insurance and the number in banking both declining by 6 per cent between 2003 and 2007. London insurers have downsized as a result of substantial losses in 2001 and 2005, industry consolidation and market reform.³⁷ Banking numbers have been reduced as a result of cost cutting by banks and increasing automation. However, asset management employment numbers have increased over the same period by 16 per cent.

Figure 6: Financial services employment by sector, 2000-2007



Source: ONS (2008) Annual Business Inquiry

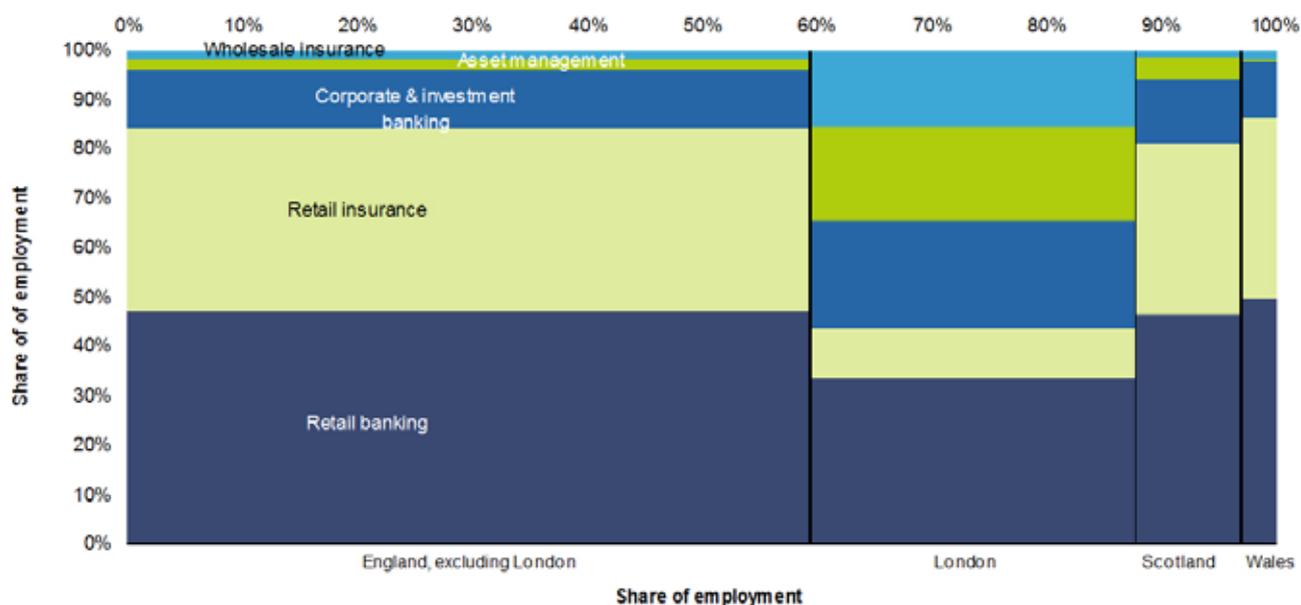
³⁵ ONS (2008) LFS/IER - Employment by Financial Services Sector Skills Council

³⁶ ONS Annual Business Inquiry; HM Treasury; PwC Analysis

³⁷ FSSC (2008) London Market Skills Review

A quarter of the workforce is in London, where financial services accounts for 25 per cent of total employment³⁸ and where, as we have noted in the previous section, the wholesale market is relatively more important than elsewhere in the UK.³⁹ Figure 7 segments the UK’s financial services workforce by sub-sector and region.

Figure 7: Financial services employment by sector and country/region, 2007



Source: ONS (2008) Annual Business Inquiry (excludes Northern Ireland); HM Treasury; PwC Analysis

English regions are not shown individually, although the most important region is the South East, accounting for c.21 per cent of financial services in employment in England outside London, followed by the North West, which accounts for c.16 per cent.⁴⁰

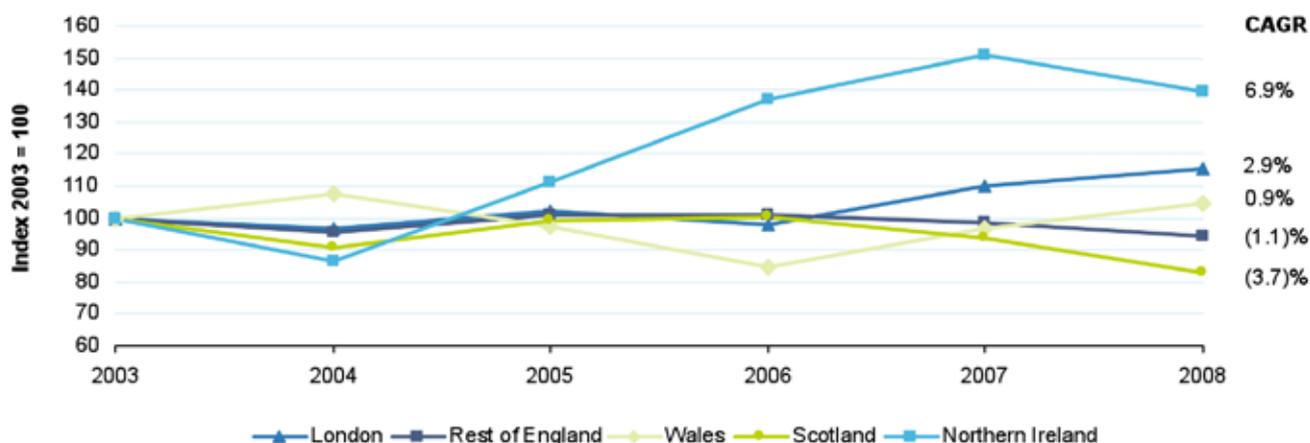
In the period between 2003 and 2008, financial services employment in the capital grew by 15 per cent, compared to the rest of England, where it contracted by almost 6 per cent (Figure 8). This is mostly due to the growth in corporate and investment banking activity in London, centred in the City and Canary Wharf.⁴¹ Northern Ireland grew strongly from a very small base during this period.

³⁸ ONS (2008) LFS/IER

³⁹ ONS (2008) LFS/IER

⁴⁰ LFS/IER 2008

⁴¹ IFSL (2009) International Financial Markets in the UK

Figure 8: Change in UK financial services employment by country/region, 2003 – 2008

Source: ONS (2008) in UKCES Almanac (2009) <https://almanac09.ukces.org.uk/default.aspx>

The financial crisis has had a dramatic impact on employment in financial services, particularly in the wholesale sector. In September 2009, London Economics estimated that the UK would lose 35,000 wholesale financial services jobs, out of 84,000 losses across Europe.⁴² This follows an estimated 28,000 job losses in wholesale financial services in 2008.⁴³

Anecdotal evidence indicates the scale of the impact on the retail sector. In November 2009, three of the UK's four major banking groups announced job losses:

- Lloyds Banking Group announced a net loss of 2,600 jobs, mostly from its group operations, insurance and mortgage businesses;⁴⁴
- HSBC announced it would shed 1,700 jobs in back-office functions, affecting collections and credit cards and equivalent to 4 per cent of its workforce. However, it said it would create 500 new jobs; and⁴⁵
- RBS said it would cut 3,700 jobs in its retail business.⁴⁶

There are signals, however, that the overall outlook is improving. Although employment is likely to continue to decline, the Confederation of British Industry (CBI)/PwC Financial Services Survey (September 2009) found that the number of financial services firms expecting to reduce their headcount in the next three months fell in the third quarter of 2009.

⁴² London Economics (2009) The importance of wholesale financial services to the EU economy 2009

⁴³ Financial Times, 20 April 2009 (see: http://www.ft.com/cms/s/3/7bfc44de-2da7-11de-9eba-00144feabdc0,dwp_uuid=504a1f30-1518-11dd-996c-0000779fd2ac.html)

⁴⁴ Financial Times, 10 November 2009 (see: http://www.ft.com/cms/s/0/1a9c750a-cdee-11de-95e7-00144feabdc0,dwp_uuid=504a1f30-1518-11dd-996c-0000779fd2ac.html)

⁴⁵ Financial Times, 3 November 2009 (see: http://www.ft.com/cms/s/0/8ae2be70-c8c9-11de-8f9d-00144feabdc0,dwp_uuid=504a1f30-1518-11dd-996c-0000779fd2ac.html)

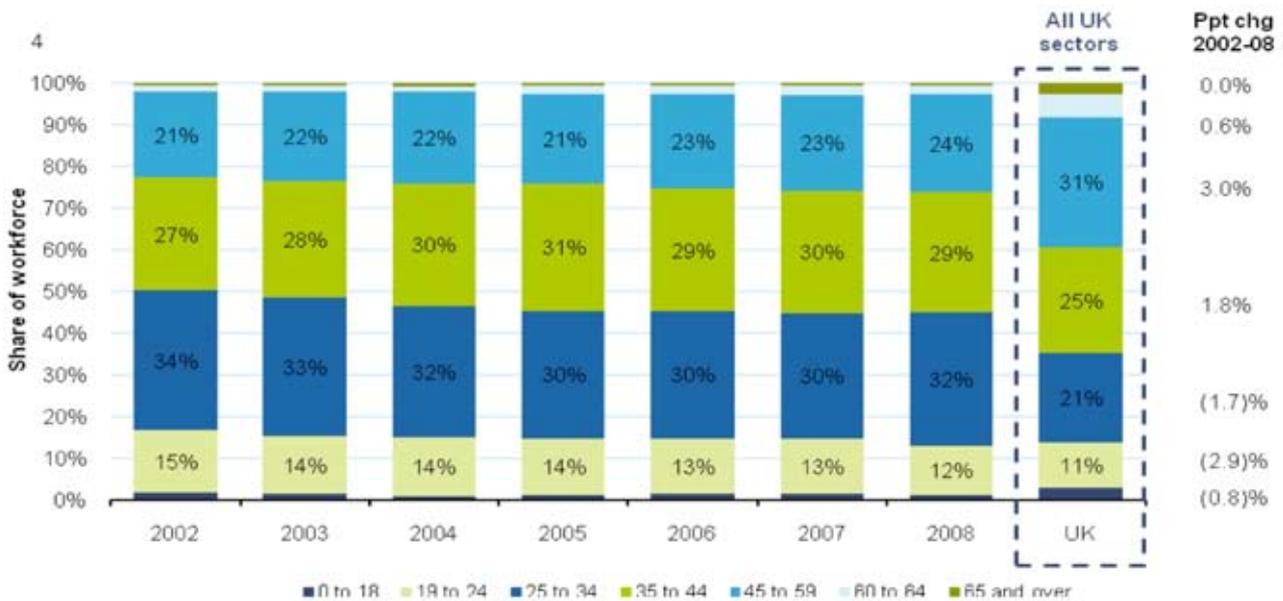
⁴⁶ Ibid.

In October 2009, London’s financial services hiring market showed some signs of improvement as the volume of new job vacancies reached the highest number recorded in any one month so far that year. New job opportunities rose by 15 per cent compared with the previous month (from 3,843 to 4,410).⁴⁷

2.4 Characteristics of employees

Financial services employees are less likely to be part-time than employees in other sectors – only c.15 per cent of workers are part-time, compared with c.25 per cent in the general workforce.⁴⁸ Self-employment is slightly more common than average, with c.16 per cent of workers working for themselves, vs. 13 per cent in the broader economy. The industry’s workforce is skewed towards males, which account for c.52 per cent of workers, compared with c.48 per cent in 2002.⁴⁹ The workforce is also ageing, although it is younger than the overall UK workforce – the average age is 38 years, 1 month, compared with an overall average age of 41 years, 11 months.⁵⁰ Figure 9 shows the age split of the financial services workforce.

Figure 9: UK financial services workforce by age, 2002-2008



Source: ONS (2008) in UKCES Almanac (2009) <https://almanac09.ukces.org.uk/default.aspx>

⁴⁷ Morgan McKinley (2009) London Employment Monitor, October 2009

⁴⁸ ONS (2008) LFS/IER

⁴⁹ ONS (2008) LFS/IER

⁵⁰ ONS (2008) LFS/IER

2.5 Occupations

Financial services careers include a broad range of occupations with varying skill requirements. The financial services value chain typically splits into front, middle and back office. The front office consists of chart facing revenue generating activities; the middle-office consists of monitoring and control industries such as managing risk; and the back office consists of support functions, such as compliance, IT and accounting. Figure 10 illustrates the functions along the value chain:

Figure 10: Activities along the financial services value chain, by sector

	Back office	Middle office	Front office	
	<i>Non-core support functions</i>	<i>Non-customer facing core functions; monitoring and control functions</i>	<i>Customer-facing functions</i>	
Example functions	<ul style="list-style-type: none"> • IT • Compliance • Human resources • Accounting • Record keeping and reporting • Clearance and settlement • Facilities management • Call centres 	<ul style="list-style-type: none"> • Service and product design • Position keeping – calculation of profit and loss • Risk management • Product control • Actuarial (insurance) • Claims handling (insurance) 	<ul style="list-style-type: none"> • Sales and marketing • Customer relationship management • Customer service • Product and service delivery 	Banking
			<ul style="list-style-type: none"> • Sales and marketing • Customer service • Underwriting • Broking 	Insurance
			<ul style="list-style-type: none"> • Trading • Broking • Portfolio management 	Asset management

Source: PwC interviews & analysis

Job types are found across the value chain, although administrative jobs are more likely to be in the back office. Managers and senior officials, professionals and associate professional/technical staff account for more than 62 per cent of employment in financial services. Growth in the number of managers and senior officials, professionals, associate professional/technical staff and sales and customer service staff has been offset by a sharp decline in the administrative, clerical and secretarial occupations, which in 2008 accounted for almost 9 per cent less of the workforce than in 2002 (Figure 11). However, these jobs remain the most common, held by almost three of every ten people (27 per cent) in the workforce - compared with the UK average of 11 per cent.

Figure 11: Financial services employment in the UK by occupation, 2002-2008⁵¹



Source: ONS (2008) in UKCES Almanac (2009) <https://almanac09.ukces.org.uk/default.aspx>

Occupations and their position in the value chain are described in more detailed below.

Managers and senior officials

Managers and senior official roles account for 28 per cent of the workforce. Managers in financial services companies usually have a professional or technical background and management and leadership are their followed by the conception and articulation of strategy. Occupations include directors, chief executive officers (CEOs), chief risk officers, marketing and sales managers, quality assurance managers and personnel managers. These occupations span across all segments of the value chain, from back office to front office.

⁵¹ Presents the types of occupations that can be found in the financial services industry as classified by the 2000 Standard Occupational Classification (SOC). Some occupations have been excluded from the analysis due to their irrelevance to the financial services industry including, skilled trades, personal service, process, plant and machine operatives and elementary occupations.

Professional and technical staff

Professional and technical staff are the primary producers and “caretakers” of the industry’s expertise. They are instrumental to the development of new products and services, the management of risk and the allocation of assets.⁵² Typically they are highly numerate, hold professional or other high-level qualifications, sought-after for their specialist skills and rewarded well for their services.⁵³ Professional and technical staff, including associates, account for 35 per cent of the UK financial services workforce. Professional occupations within financial services include actuaries, chartered accountants, chartered insurance practitioners/brokers and fund managers. Associate professional occupations include actuarial students, underwriters, trainee fund managers, brokers and investment banking analysts. These occupations are primarily front-office jobs.

Administrative and secretarial staff

Financial services have a much larger administrative and secretarial workforce compared to other industries, due to the amount of administrative work relating to managing data and information, conducting and tracking transactions, facilitating communications and regulatory compliance. Administrative work is a driver of cost and is often the target of efficiency drives, including outsourcing and offshoring. Administrative and secretarial work is primarily a back-office function and includes occupations such as credit controllers, counter clerks and personal assistants.

Sales and customer service staff

Sales and customer service occupations are held by 9 per cent of the UK financial services workforce. In the wholesale markets, customer service is a more technical front office discipline of managing client accounts and professionals performing these activities would not describe themselves as customer service staff. The occupations outlined in Figure 11 are further defined in Annex A.

2.6 Current skills profile and provision

The FSSC segments the skills required in the sector between industry and technical skills (specific skills), and business and interpersonal skills (generic skills).⁵⁴

⁵² FSSC (2007) Analysis of skills needs in UK financial services.

⁵³ FSSC (2007) Analysis of skills needs in UK financial services.

⁵⁴ FSSC (2007) The Skills Bill: Analysis of skills needs in UK financial services.

Industry and technical skills include those competences particular to financial services that have a clear knowledge component (e.g. knowing how to model a particular type of risk or price an instrument). Industry and technical skills are important in the hiring of professional and technical staff, but also play a part in the selection of managers and senior managers, who are themselves usually selected from among the former.⁵⁵ The level of industry and technical skills required varies across the value chain. Numeracy skills differ from basic manipulation of figures at an administrative and secretarial level to sophisticated mathematical analysis at an experienced professional level. Those in sales and customer service occupations are required to have deep product knowledge.

Business and interpersonal skills are transferable across industries and include non-technical competences such as relationship management, communication and problem-solving skills. These skills are required across all segments of the value chain, but are more prominent in managerial, sales and customer service roles.

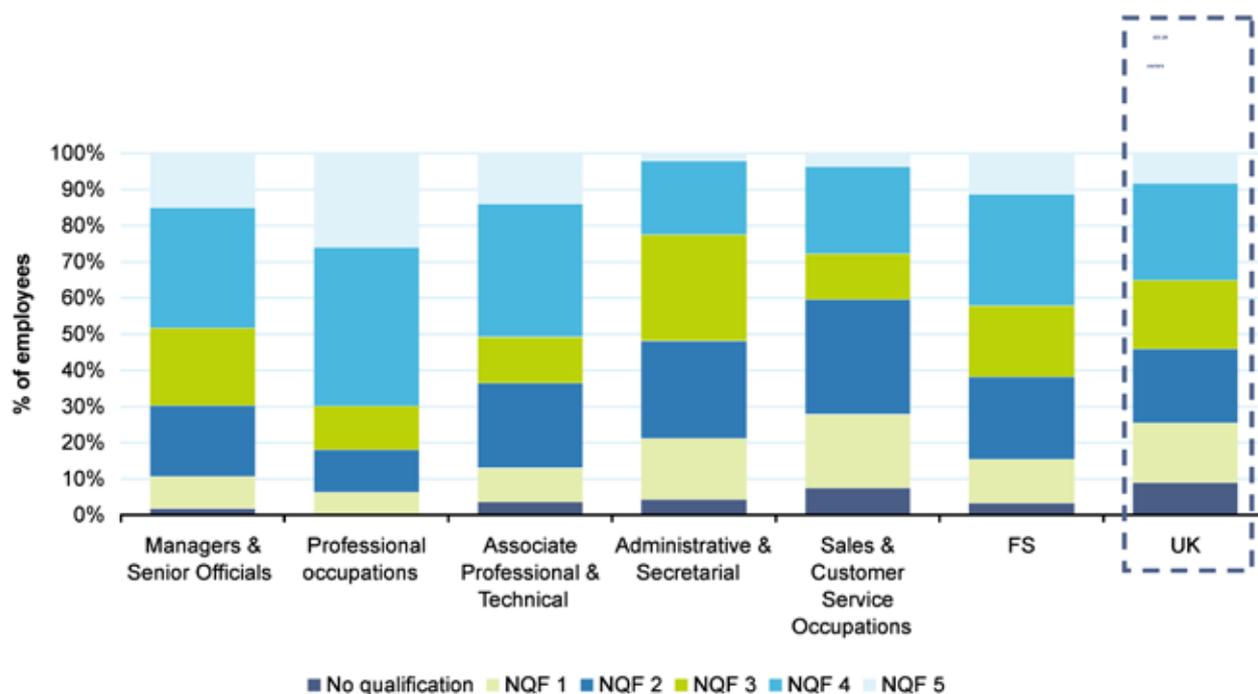
Skills requirements not only differ along the value chain, but also between the different sub-sectors within financial services. Employers in wholesale financial services, for instance, report an increasing premium on quantitative skills for both front and back office functions, due to increasing demand for complex products and an insufficient supply of individuals with quantitative skills.

Figure 12 provides an overview of the qualification level of the UK financial services workforce by job category.⁵⁶ As would be expected, given the relative weighting of managerial and professional occupations in financial services, the average level of qualification in the sector is higher than in the economy as a whole. The percentage of the financial sector workforce holding qualifications at NQF Level 3 (e.g. A-Levels) and above is c.62 per cent, eight percentage points higher than the average for the broader UK labour force.

Those in professional occupations hold the highest levels of qualifications, with 26 per cent qualified to NQF Level 5 (e.g. Doctorate/Masters level) and a further 44 per cent qualified to NQF Level 4 (degree level). In contrast, only 15 per cent of managers and senior officials are qualified to NQF Level 5 and a further 33 per cent are qualified to NQF Level 4. This suggests that some managerial positions are occupied by people who entered the industry with lower level qualifications (e.g. NQF Level 2 or 3) and then progressed to their managerial position with experience.

⁵⁵ Ibid.

⁵⁶ See Annex 2 for further details of the National Qualifications Framework (NQF) levels in England, Wales and Northern Ireland.

Figure 12: Qualification level of the UK financial services sector

Source ONS (2008) in UKCES Almanac (2009) <https://almanac09.ukces.org.uk/default.aspx>

Many people in customer service and administration enter directly from school. This accounts for the lower level of educational attainment in these occupations, with over 70 per cent of the workforce in administration and secretarial and sales and customer service educated to NQF Level 3 or below.

Employees' external qualifications come from general education, work-based learning, higher education and professional training. Formal and informal internal training provision is also important.

General education

Approximately 85 per cent of the workforce in 2008 possessed GCSEs or equivalent qualifications. The retail banking and general insurance sectors employ the highest proportion of individuals with Level 2 qualifications as their highest qualification.⁵⁷ This most likely reflects the large share of secretarial and administrative roles in these sectors.

Vocational qualifications

The take-up rate of apprenticeships is generally low in financial services. In 2006, only 1 per cent of the workforce completed an apprenticeship programme and these apprenticeships tended to be in insurance and broking and fund management.⁵⁸

⁵⁷ FSSC (2007) The Skills Bill: Assessment of education and training provision in UK financial services.

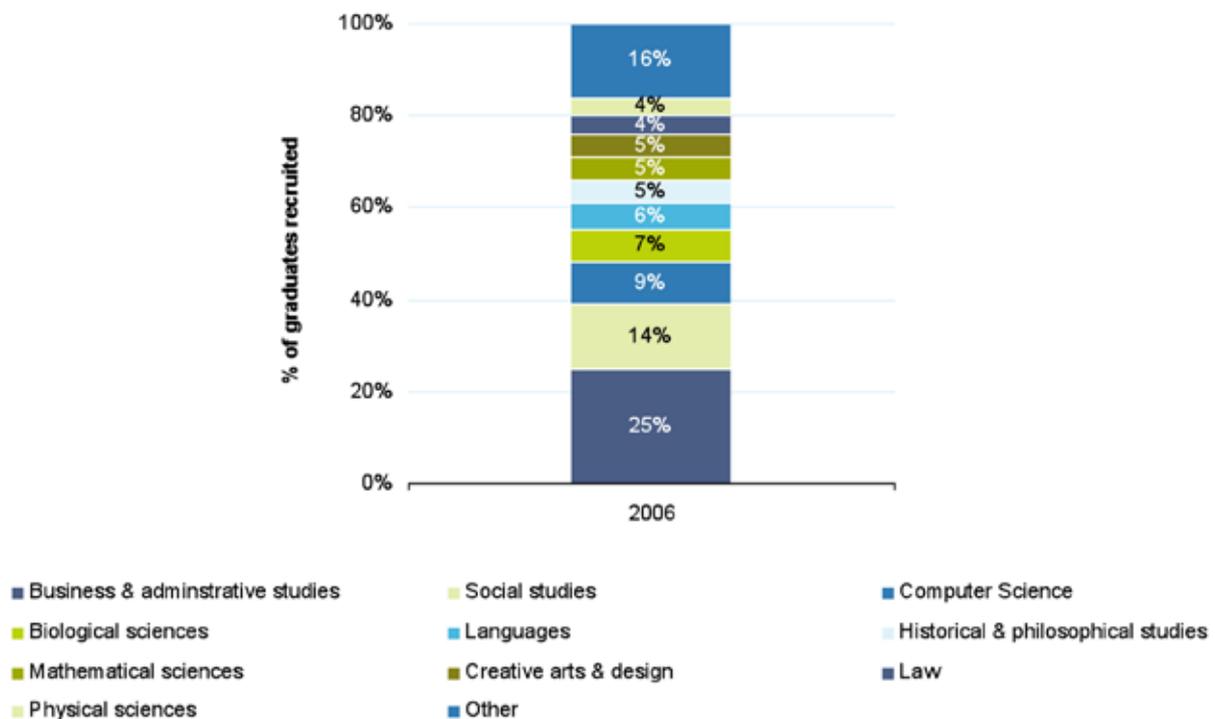
⁵⁸ LFS (2006)

The majority of employers and training providers surveyed in the 2006 FSSC Employer Survey considered vocational qualifications not particularly relevant to certain financial services occupations.⁵⁹ This is due to the industry’s regulatory nature and somewhat negative perceptions of national vocational qualifications (NVQs) in some quarters. The FSSC has developed apprenticeships in Providing Financial Services, and the Advanced Apprenticeship in Providing Financial Services. The requirements for the apprenticeships are a technical certificate (e.g. from the CII, the Institute of Financial Services, the Chartered Institute for Securities & Investment), a competence qualification (NVQ) and possession of key skills (literacy, numeracy, communications, IT and team work).⁶⁰

Higher education qualifications

Over 40 per cent of financial services employees were educated to NQF Level 4 (bachelor’s degrees, graduate certificates and diplomas) in 2008. Lucrative careers in some areas of financial services – particularly wholesale banking – have enabled the industry to attract graduates from a broad variety of disciplines, as shown in Figure 13.

Figure 13: Analysis of non-specific industry degrees contribution to total UK financial services graduate recruitment (2004/05)



Source: HESA 2006

⁵⁹ Ibid.

⁶⁰ FSSC website (see: http://www.fssc.org.uk/147_13.html?i=5)

The talent pool for wholesale financial services is also very international, with employees drawn (to London in particular) from across Europe and farther afield. A significant proportion comes from France, Germany, Eastern Europe and the Far East.⁶¹

The majority of graduates entering the financial services industry occupy junior management, associate professional and sales roles. Many move quickly from this initial role, either as part of a training programme or internal promotion. The low level of recent graduates occupying professional roles (e.g. compliance, financial advice) compared with other industries is attributable to the industry's high degree of regulation.⁶²

Employers increasingly demand post-graduate qualifications. In some parts of the industry, particularly within wholesale financial services, they are required for entry-level jobs. The proportion of employees holding a post-graduate qualification grew from 4 per cent in 2003 to 11 per cent in 2008.⁶³

Professional training

Some jobs within financial services, such as fund managers (asset management) and financial advisors (insurance), are regulated by the FSA and require practitioners to have a specific qualification before undertaking the job without supervision. These qualifications are issued by the relevant awarding bodies, including the CFA Institute, the CII and the International Compliance Association. Training for these qualifications may be funded by employers.

Internal training

In addition to formal qualifications, internal training is also an important tool for developing employees. Regulatory compliance is the most common type of training undertaken. In addition, different types of employees receive different types of training:

- managers are most often given management development training;
- professional and technical staff take courses in regulatory compliance and non-regulatory, technical subjects;
- secretarial and administrative staff are more likely to take communication courses;
- sales and customer services staff take role-specific training to facilitate sales; and
- new entrants and graduates are trained extensively, with an emphasis on non-regulatory technical skills.⁶⁴

⁶¹ | FSSC (2007) Skills Review: UK wholesale financial services

⁶² FSSC (2007) The Skills Bill: Assessment of education and training provision in UK financial services

⁶³ FSSC (2007) Skills Review: UK wholesale financial services

⁶⁴ FSSC (2007) The Skills Bill: Assessment of education and training provision in UK financial services

The 2008 LFS found that 33 per cent of financial services employees have received some sort of training (including in-house and outside training) in the previous 13 weeks, compared with 31 per cent of employees across all sectors.⁶⁵ These figures have declined somewhat in recent years – in 2002, the equivalent figure was 40 per cent for financial services and 34 per cent for all sectors. This trend is likely to be exacerbated by the current economic climate, which has put pressure on training budgets. Recent findings from the CBI/PwC Financial Services survey suggest that employers' expenditure on training in the last six months has declined; however, this trend is improving from the previous quarter.⁶⁶

In-house training is often not recognised or accredited. This can make it difficult for people to transfer their skills to other areas of the industry.

Experience

While qualification and training are useful indicators of the workforce's skill level, they are not the sole indicator. Many positions require skills which are mostly developed through experience (or even innate). Relationship skills, for instance can only be developed to a limited extent through training, but these are often cited as the most important skill for many financial service jobs.

2.7 Unfulfilled skills needs

The financial services sector is impacted by significant skills deficits, particularly among “home-grown” talent in the UK. Skills deficits fall into two categories:

- skills shortages: skills which cannot be filled from the available pool of job applicants; and
- skills gaps: skills lacked by employees already in the industry.

Although job losses in the recession will have undoubtedly alleviated the shortage of skills, a survey of senior human resource managers (covering all sectors of the economy) by King's College London in 2009 found that management roles are still affected by skills shortages in the recession.⁶⁷ Despite organisations continuing to reduce headcount, the report found that a third of senior HR professionals reported skills and staff shortages as a continuing problem. Pay freezes, bonus pool reductions, ongoing redundancies and shelved training plans have made it more difficult for companies to attract and retain skilled employees. In the current economic climate, companies may rely on the threat of job insecurity and limited external opportunities to ensure remaining employees meet performance requirements.

⁶⁵ ONS (2008) LFS/IER

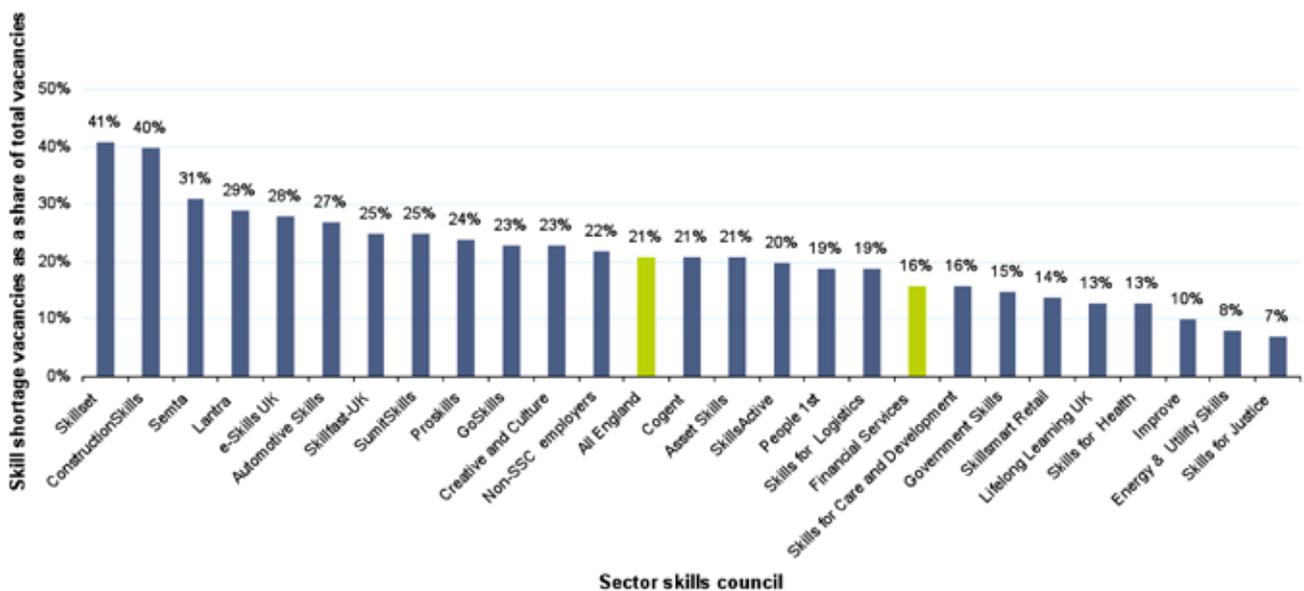
⁶⁶ PwC/CBI Financial Services Quarterly Survey (September 2009)

⁶⁷ Kings College London (2009) Riding the recession? The state of HR in the current economic downturn.

2.7.1 Skills shortages

According to NESS 2007, skills shortages are slightly less pronounced in Financial Services than many other sectors. As shown in Figure 14, the share of vacancies unfulfilled due to skills shortages was 16 per cent, five percentage points below the average for England. The occurrence of skills shortage vacancies per 1,000 employees stood at five in financial services, compared with an English average of six.⁶⁸

Figure 14: Summary of skill-shortage vacancies by sector skills council

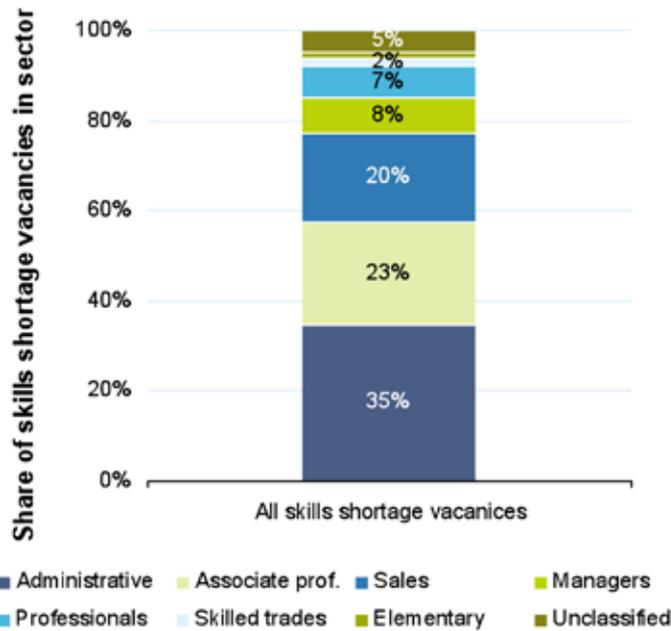


Source: NESS 2007

According to NESS 2007, skills shortages in financial services are most commonly for administrative, associate professional and sales jobs, as demonstrated in Figure 15.

⁶⁸ NESS (2007)

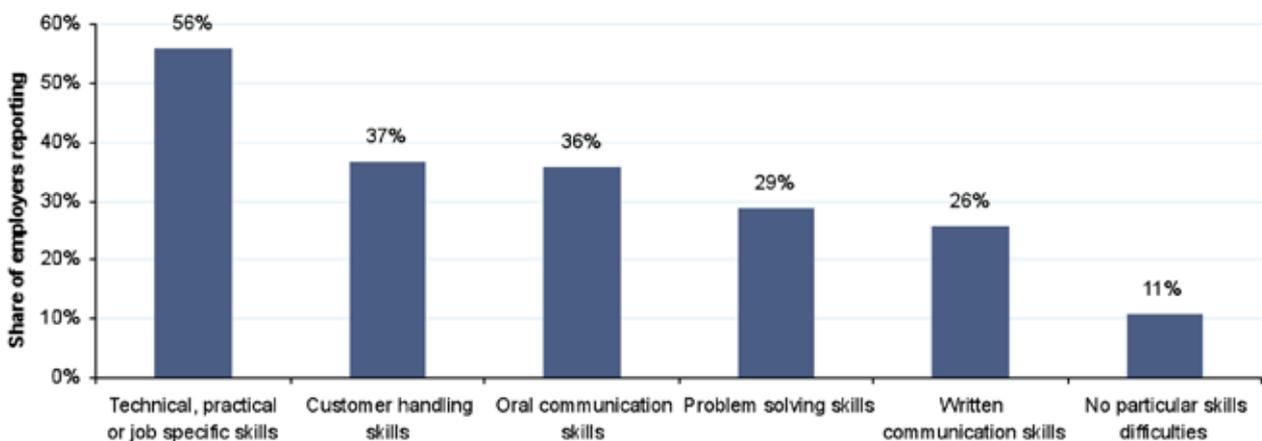
Figure 15: Distribution of skill-shortage vacancies in financial services, by occupation



Source: NESS 2007

NESS also found that a majority of participating financial services employers had difficulty finding applicants with the right technical or job-specific skills (often specialist quantitative skills such as modelling risk or pricing instruments and/or deep product knowledge). A significant number also said there was a shortage of “soft” skills in customer handling, oral/written communication and problem solving.⁶⁹

Figure 16: Skills responsible for skill shortage vacancies in financial services



Source: NESS (2007)

⁶⁹ NESS (2007)

Three quarters of financial services employers interviewed by the CII in its 2009 Annual Skills Survey⁷⁰ reported shortages of technical skills, a 5 per cent increase on 2007. The issue has become so critical that it is now on the agenda of four out of five financial services employers, compared with three in five in 2007.⁷¹

The technical skills that are found lacking are often quantitative skills. In 2007, wholesale financial services employers reported an increasing premium on, and an acute shortage of, quantitative skills for both back and front office roles, especially in newly emerging areas driving growth.⁷² According to the FSSC, the industry needs people with “sophisticated maths” who are trained in probability.⁷³ However, these skills alone are not sufficient: the Turner Review of financial regulation identified a “misplaced reliance on sophisticated mathematics” as one cause of the market’s inability to identify and assess risk.⁷⁴

2.7.2 Skills gaps

Data from skills surveys around the UK suggests that as of 2007, c.7 per cent of all financial services employees may not have been fully proficient at their roles.⁷⁵ In absolute terms, around 80,000 people were reported to lack some skills necessary to carry out their duties proficiently.⁷⁶ Compared with other sectors, the incidence of skills gaps is in line with the average, though they impact a higher share of companies, as shown in figure 17.

⁷⁰ CII (2009) CII Group Skills Survey. Covers all aspects of financial services.

⁷¹ Ibid.

⁷² FSSC (2007) Skills Review: UK wholesale financial services.

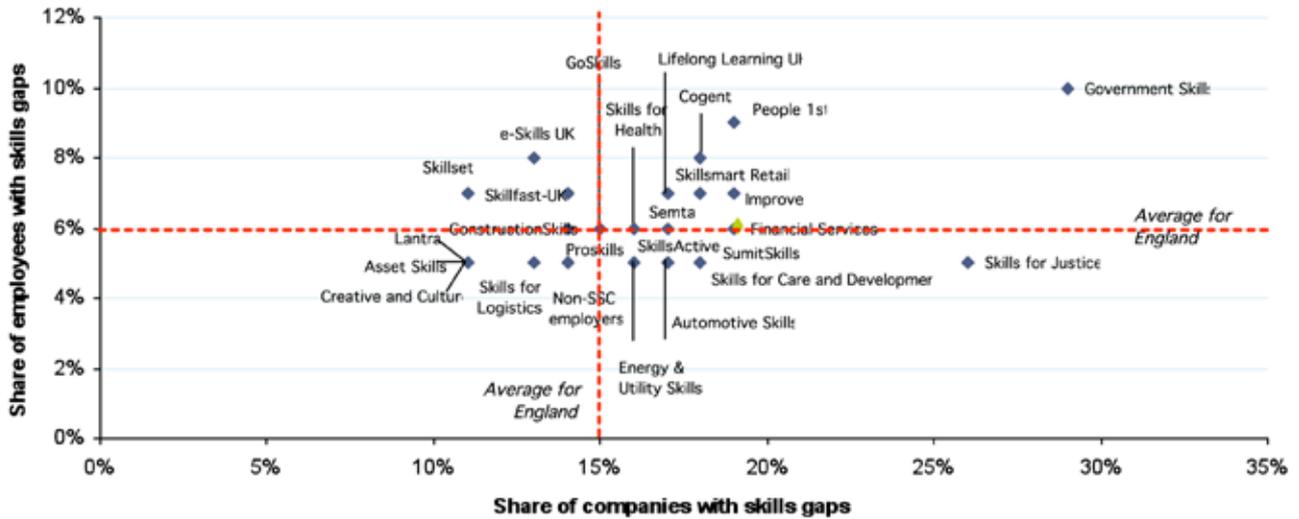
⁷³ FT Advisor website, 30 April 2009 (see: <http://www.ftadviser.com/FinancialAdviser/Advisers/Industry/TrainingAndCompetence/Supplements/article/20090430/3364ec56-2e5d-11de-8da9-00144f2af8e8/Doing-the-maths.jsp>)

⁷⁴ FSA (2009) The Turner Review: A regulatory response to the global banking crisis.

⁷⁵ Sources: ONS, NESS, Future Skills Scotland, Future Skills Wales, Northern Ireland Skills Monitoring Survey and FSSC calculations.

⁷⁶ FSSC (2007) The Skills Bill: Analysis of skills needs in UK financial services.

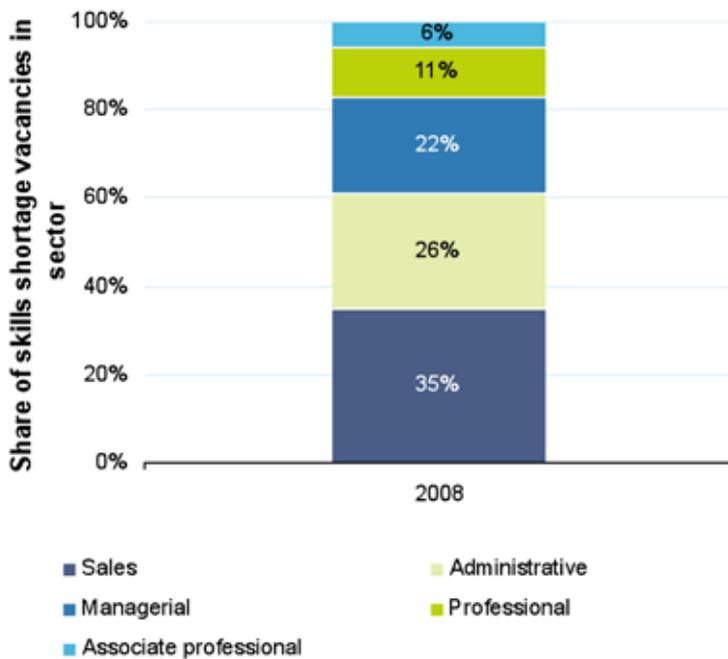
Figure 17: Incidence and number of skills gaps by sector skills council



Source: NESS 2007

Staff working in sales and customer service occupations accounted for 35 per cent of the skills gaps in financial services, followed by administrative and secretarial workers (26 per cent) and managers and senior officials (22 per cent), as shown in Figure 18.

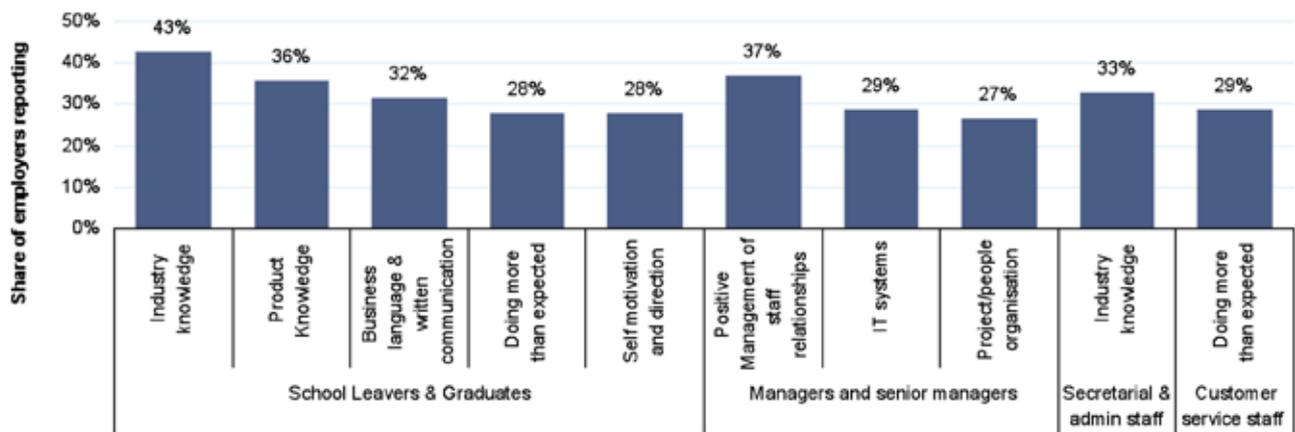
Figure 18: Skills gaps in UK financial services by occupation



Source: NESS (2007)

Figure 19 identifies the skills gaps by type of employee identified by the 2006 FSSC Employer Survey. School leavers and graduates were most likely to have skills gaps. They often lacked appropriate industry and product knowledge – although much of this would be acquired on the job, they would be expected to have a basic level of understanding before starting work. Secretarial and administrative staff also lack industry knowledge, while the largest skills gap among managers related to people management.

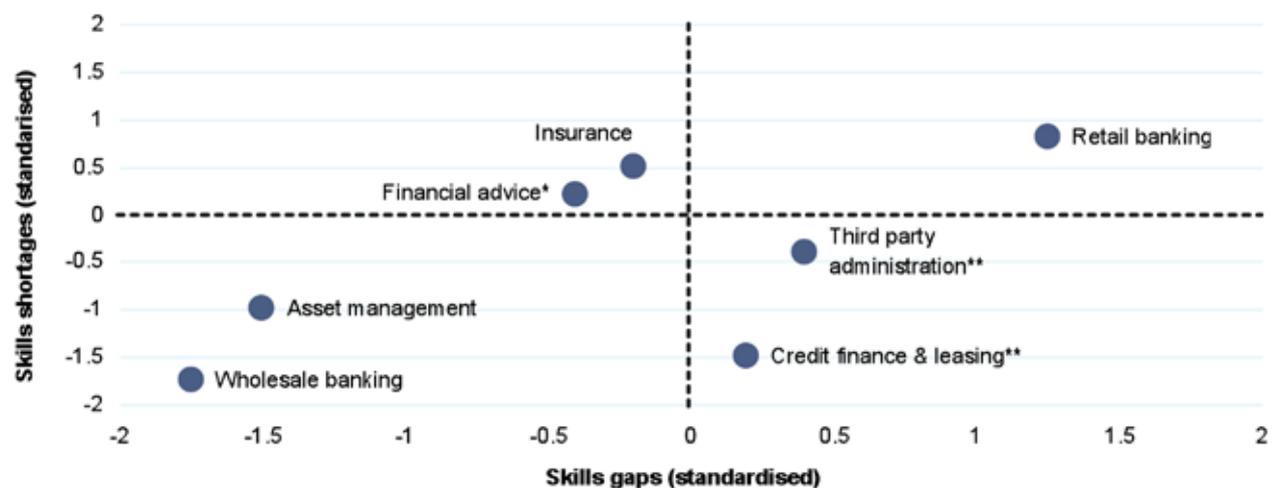
Figure 19: Top ten skills gaps in financial services, by employee type



Source: FSSC (2007)

Figure 20 presents a map of skills deficits across sectors based on standardised differences from the UK average. The scale of skills deficits varies significantly between financial services sectors, and is less pronounced in the more “prestigious” wholesale sectors.

Figure 20: Sector skills deficit grid⁷⁷



* considered part of Insurance for the purposes of this report

** “Other” categories not considered in detail in this report

Source: FSSC (2007)

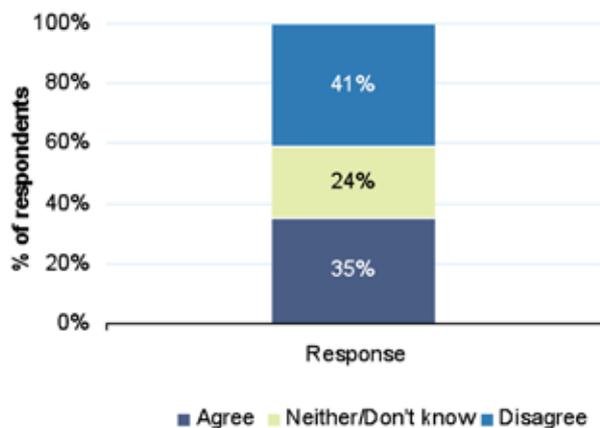
⁷⁷ Segmentation used by FSSC different from that used in this report

This analysis shows that:

- retail banks appear to experience the most acute skills deficits. Insurance is threatened by skills shortages, although the current workforce does not lack the necessary skills or qualifications. However, there may be a problem sourcing the skills needed in the future; and
- wholesale banking and asset management have a relatively small proportion of employers reporting skills deficits of either type. This is due, in part, to the fact that these sectors do not depend exclusively on the domestic labour market as they have access to a global pool of professionals who are attracted to London.⁷⁸ Compensation is also generally very competitive in these sectors.

The CII Annual Skills Survey (2009) found that more than 40 per cent of members felt that the education system did not prepare them for a career in the financial services industry, suggesting that schooling may be at the root of some skills shortages and gaps.

Figure 21: “Our education system has prepared me well for a career in the financial services industry”



Source: CII (2009)

Over half the employers responding to the CII survey (57 per cent) said the education system failed to meet the needs of the industry, with only 3 per cent describing basic levels of education as “more than adequate”. In addition, a large proportion of employers who participated in this research believed that many graduates struggle with basic literacy and numeracy skills.

⁷⁸ FSSC (2007) The Skills Bill: Analysis of skills needs in UK financial services

According to the FSSC, the gap between the numeracy and quantitative skills of UK students and their overseas counterparts has resulted in increased recruitment of foreign candidates into wholesale financial services over time.⁷⁹ French and German mathematicians are particularly common in the City. According to one academic, their training in probability is much more rigorous than that offered by the British system, and only a minority of British mathematicians is taught with the same statistical basis.⁸⁰ Employers have also identified language skills, cultural awareness and a superior work ethic among overseas candidates as advantages over their UK counterparts in the recruitment process.⁸¹

⁷⁹ FSSC (2007) Skills Review: UK wholesale financial services.

⁸⁰ FT Advisor website, 30 April 2009 (see: <http://www.ftadviser.com/FinancialAdviser/Advisers/Industry/TrainingAndCompetence/Supplements/article/20090430/3364ec56-2e5d-11de-8da9-00144f2af8e8/Doing-the-maths.jsp>)

⁸¹ FSSC (2007) Skills Review: UK wholesale financial services.

3. Industry insight: Banking

Chapter summary

The banking sub-sector is the largest within financial services, with a workforce of c.534,000 people. Retail banking employs nearly three times as many people as wholesale banking, with c.398,000 workers, compared to c.136,000 in wholesale. There is a distinct concentration of employment in London and this is particularly prevalent in wholesale banking, with c.42 per cent of this workforce located in the capital. Wholesale employment levels have fallen significantly in the last two years as many banks have laid-off staff.

Retail banking occupations can be split generally into front-office positions and back- and middle-office positions. Front-office roles are those typically found in branches and customer support centres, such as clerks and sales, marketing and telephone support staff. Back- and middle-office functions include credit control managers, risk analysts, information technology (IT) support and compliance staff. Employees in this sector tend to have lower qualification levels.

Retail banking appears to have significant skills shortages and gaps. Retail banking does not enjoy the same attractiveness as wholesale banking relative to the sectors it competes with for candidates and as a result, recruitment is more difficult. 77 per cent of banks and building societies responded that they suffered from skills shortages. Retail banks also suffer from skills gaps, mainly in the areas of product and sector knowledge, as well as general motivation and “job readiness”.

Wholesale banking follows a similar structure to retail banking, although front-office roles reflect the corporate and institutional nature of wholesale banking and include corporate relationship managers, finance analysts, finance and mergers & acquisitions (M&A) advisors and product design staff. Support roles are similar to those in retail banking and include staff working in risk analysis, compliance, IT support and credit control, although there is generally a larger product control division as well as finance settling function.

Skills deficits in wholesale banking are less pronounced than in retail banking. It has historically been a destination of choice for graduates of all qualification levels and is able to attract talented staff, often with Level 5 qualifications or sector-specific training from bodies such as the CFA (Chartered Financial Analyst) Institute or the Chartered Institute for Securities & Investment. Furthermore, once these high-calibre individuals are hired, significant investment in training ensure that they are developed further.

As a result, wholesale banking employers generally do not suffer from significant skills gaps and shortages. Where deficits have been identified, these relate to quantitative analytical skills and a general lag in understanding as staff become acquainted with new financial products. However, much of the responsibility for the financial crisis in this sub-sector has been attributed to poor management and leadership in the sector, as well as a lack of understanding of risk.

3.1 Introduction

The banking sub-sector is the largest sector in the UK financial services. This chapter of our report describes the banking market in the UK and the current status of employment and skills in the sector. It covers the following topics:

- Current state of the UK market;
- Current employment;
- Occupations;
- Current skills profile and provision; and
- Unfulfilled skills needs.

3.2 Current state of the UK market

3.2.1 Importance to the UK economy

“The banking system provides two crucial services to the rest of the economy: providing companies and households a ready means by which they can make payments for goods and services and intermediating flows of savings to finance investment.” Mervyn King, Governor of the Bank of England⁸²

The UK has a mature and highly developed banking sector that accounts for 62 per cent of total UK financial services GVA, and employs c.534,000 people.⁸³ It has become, in recent years, one of the UK’s largest and most productive sectors, but is currently going through a period of considerable turmoil and volatility, evidenced by the collapse of Northern Rock, Lehman Brothers and other banks, and the bailouts from the UK government.

⁸² Speech by Mervyn King, Governor of the Bank of England to Scottish business organisations, Edinburgh, 20 October 2009 (see: <http://www.bankofengland.co.uk/publications/speeches/2009/speech406.pdf>)

⁸³ ONS (2008) Annual Business Inquiry

In 2008, there were 336 authorised banks in the UK,⁸⁴ of which 254⁸⁵ were foreign, and 10,300 bank branches.⁸⁶ The number of banks has been declining over the last decade, primarily as a result of mergers and closures of small institutions as the market reached over-capacity. The number of UK-owned banks has also declined sharply, while the number of foreign-owned banks has increased. This reflects the wider globalisation trends evident in the financial services sector as a whole as well as the effects of the European single currency, as European banks consolidate and use their new critical mass to expand into the UK.⁸⁷

Prior to the crisis, banks enjoyed very high profitability levels, with net income reaching £20bn for the first time in 2008. The boom period just prior to the financial crisis saw profits increase at rates of up to 89 per cent as banks took advantage of economic conditions and financial innovation to generate returns on capital of over 20 per cent.

3.2.2 Market segmentation

In order to understand the drivers of different parts of the banking sector, and to identify different employment dynamics, we are using the segmentation described in Chapter 2 (retail banking and wholesale banking).

- **Retail banking** covers the banking activities of individuals and SMEs. Services provided under retail banking includes current accounts, savings accounts, credit cards, personal loans, mortgages, and small business banking and associated ancillary services;
- **Wholesale banking** is the provision of services to large business or corporations, typically with international operations; financial services companies; and government and public sector organisations. These services include access to money and capital markets; corporate finance; securities and derivatives trading; fixed income investments; and commodity and currency trading.

Due to the nature of their activities, retail banking tends to be domestically focused, while wholesale banking is more international.

⁸⁴ European Banking Federation (2008) Banking Sector Statistics as of 31.12.2008

⁸⁵ IFSL (2008) Banking

⁸⁶ European Banking Federation (2008) Banking Sector Statistics as of 31.12.2008

⁸⁷ Europe's World website (see: http://www.europesworld.org/NewEnglish/Home_old/Article/tabid/191/ArticleType/ArticleView/ArticleID/20668/Default.aspx)

Retail banking

Retail banking is a relatively stable sector and one that is mature in the UK with deep penetration. In 2007, there were:

- 75.9m current accounts in the UK, with only 6.4 per cent of the population estimated to be without a current account;⁸⁸
- over 62m credit cards in issue; and⁸⁹
- 11.8m mortgages outstanding⁹⁰.

While retail banking is generally stable, the financial crisis has impacted many activities in the sector. Lending activities have suffered from lack of liquidity and banks' unwillingness to issue credit, although current accounts are more immune as the population still requires access to basic banking facilities.⁹¹

Credit card lending stagnated in 2009 and balances fell 3 per cent over the year, as consumers attempt to reduce their levels of debt. The number of cards in issue has declined by 8 per cent to a level not seen since 2003.⁹²

Total gross mortgage advances are estimated to have fallen by a third from 2007, a result of tightening credit conditions. As well as an increase in caution regarding the credit-worthiness of consumers, a cooling housing market has reduced demand for mortgages.⁹³

As Figure 22 shows, retail banking deposits in the UK grew strongly in recent years, doubling between 2003 and 2008. This was largely driven by growth in the deposits of private financial corporations, which were very profitable throughout the boom period.

⁸⁸ Mintel (2008) Retail Banking Overview UK

⁸⁹ PwC (2009) Precious Plastic 2010

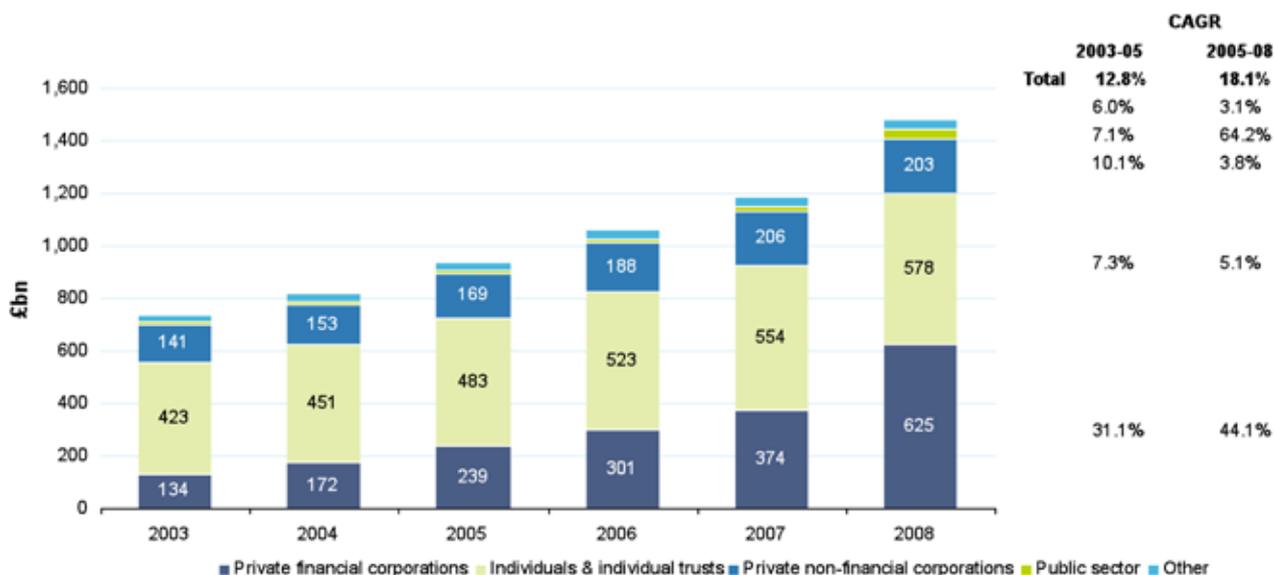
⁹⁰ Mintel (2008) Retail Banking Overview UK (relates to 2007 data)

⁹¹ Mintel (2008) Retail Banking Re-forecast UK

⁹² PwC Precious Plastic

⁹³ Mintel (2009) Retail Banking Re-forecast UK

Figure 22: Retail banking deposits 2003-2008



Source: BBA Abstract of Statistics (2008)

Private banking has been one of the fastest growing areas of the banking industry over the past decade, with many high net-worth individuals relocating to London. However, the UK has been particularly hard hit by falling equity and property values and the number of people considered high net-worth individuals⁹⁴ fell by 26 per cent in 2008.⁹⁵

Retail banking customers are typically individuals and small businesses. The main products are simple depositing and borrowing facilities. Prior to the financial crisis, approval criteria for many retail banking products were relaxed, leading to an overabundance of cheap consumer credit and ultimately contributing to the financial crisis itself.⁹⁶ Since the crisis, retail banks have retrenched many of their assets and credit has become scarce to both individuals and corporate customers.⁹⁷ The government has subsequently made attempts both to constrict capital to higher-risk customer segments⁹⁸ and encourage lending to credit-worthy customers and businesses which might otherwise struggle without it.⁹⁹

⁹⁴ Defined as those with investable assets of US\$1m or more, excluding primary residence, collectibles, consumables and consumer durables

⁹⁵ Capgemini (2009) World Wealth Report

⁹⁶ PwC The Day After Tomorrow Series (available at: <http://www.pwc.com/gx/en/financial-services/day-after-tomorrow/index.jhtml>)

⁹⁷ PwC (2009) 10 Minutes, February 2009

⁹⁸ FSA website (see: <http://www.fsa.gov.uk/pages/Library/Communication/PR/2009/140.shtml>)

⁹⁹ HM Treasury website (see: http://www.hm-treasury.gov.uk/press_05_09.htm)

The concentration of the retail banking industry is very apparent in the retail sector, with the top six brands (Barclays, Lloyds TSB, HSBC, NatWest, Halifax and Nationwide) accounting for over 60 per cent of the market, and the top ten providers acting as the primary financial services provider for 85 per cent of the banked population.¹⁰⁰ However, it should be noted that individuals typically have services from different financial providers as significant cross-selling is not common in the UK market.¹⁰¹

The distribution of retail banking products generally relies upon two channels: branches and distance channels such as telephone or internet banking. As already noted, the number of bank branches overall has declined as more people adopt telephone and internet banking. The continued consolidation of the market also leads to branch closures as recently-merged banks reduce duplication in their networks.

Wholesale banking

The UK has a strong global presence across all major wholesale banking activities, with activity conducted predominantly in London. While the largest retail banks in the UK often have a wholesale banking division as part of their full-service offering, there are many international and specialist wholesale banks operating in the UK. Wholesale banks usually undertake a wide variety of activities, although some do specialise in certain niches. The main activities undertaken by wholesale banks include:

- capital raising, either through issuing bonds (debt) or shares (equity);
- M&A advisory;
- corporate finance;
- foreign currency exchange;
- large-scale lending and international/cross-border lending;
- money markets (short term financing);
- trading of financial instruments (either on behalf of clients or proprietary); and
- securities and derivative trading.

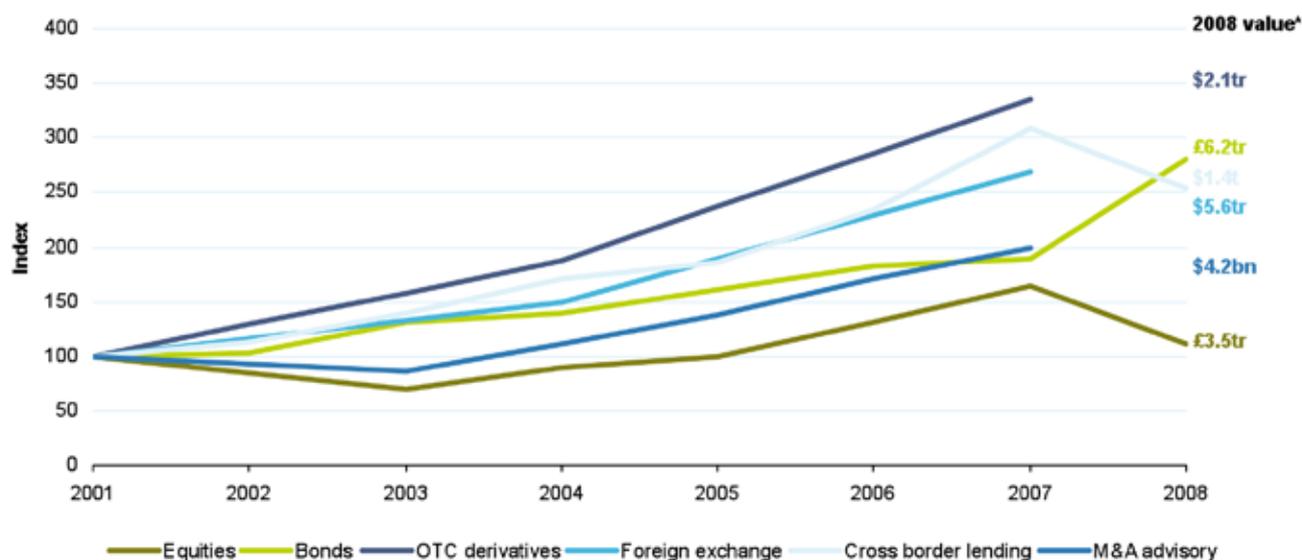
¹⁰⁰ Mintel 2009

¹⁰¹ Expert interviews

Wholesale banking is a multi-billion pound sector, responsible for a significant part of the financial services sector’s overall GVA. Cross-border lending, foreign exchange services and over-the-counter (OTC) derivatives remain three of largest financial services activities carried out in London, and all three experienced strong growth between 2001 and 2008.¹⁰² The UK is an established destination for international finance and is one of the main financial hubs in Europe. Over 23 per cent of European investment banking revenue was sourced from the UK in 2008.¹⁰³

As Figure 23 highlights, the UK’s main wholesale banking activities have generally been increasing since 2001, with all markets except equities two or three times larger in 2008 than they were in 2001. The total equities market stood at £3.5tr in 2008, following a 32 per cent drop as a result of the credit crunch and subsequent financial crisis. However, London is still responsible for one-fifth of global foreign equity trading and a similar proportion of global capital-raising through equities.¹⁰⁴

Figure 23: Indexed value of wholesale banking markets, 2001–2008 (2001=100)



Source: Bank of International Settlements, World Federation of Exchanges, PwC analysis.¹⁰⁵

¹⁰² Ibid.

¹⁰³ IFSL (2009) International Financial Markets in the UK

¹⁰⁴ IFSL (2009) International Financial Markets in the UK

¹⁰⁵ Equities is the total value of all share trading and new capital raised through shares; Bonds is the total value of bonds listed, bond trading and new capital raised by bonds; OTC derivatives is the average daily turnover; Foreign exchange is the daily average foreign exchange market.

London continues to lead the European market of initial public offerings (IPOs)¹⁰⁶, with a 35 per cent share of all European IPOs by volume (58 per cent by value) in 2008.¹⁰⁷ London has international appeal for companies seeking a stock exchange listing and tends to attract larger deals, as evidenced by a significantly larger market share of IPO value than volume. However, since the financial crisis, IPO numbers have fallen to almost zero due to low appetite among investors looking to consolidate their existing portfolios instead of extending their investments.

London is a leading global banking centre and has maintained this position in the financial crisis¹⁰⁸ - the city has 264 foreign banks, more than any other city in the world,¹⁰⁹ with over £7.9tr in assets.¹¹⁰ The global nature of UK banking is also evident in the changing composition and control of its assets: in 2007, foreign banks were responsible for 58 per cent of total UK banking sector assets.¹¹¹

Customers of wholesale banks are generally large companies requiring complex banking services; banks and financial services companies; and government and public sector organisations. The nature of some wholesale banking activities means that some relationships are short-term - for example, where short-term financing or a one-off transaction is required. However, most wholesale banks have long-term relationships that are built either from large-scale projects, such as the underwriting of an IPO or capital raised through a long-yield bond, or from recurring transactions, such as foreign-exchange trading.

M&A has historically been a key revenue earner in the UK wholesale banking segment, accounting for 61 per cent of revenue in 2007 and 2008. However, it has been severely impacted by the financial crisis, and accounted for just 28 per cent of revenue in 2009.¹¹² Just over half of wholesale banking's 2009 revenue was generated by equity products and 21 per cent came from fixed income products.¹¹³ Table 5 lists the top wholesale banks globally for M&A activity.

¹⁰⁶ Initial Public Offering

¹⁰⁷ PwC (2008) IPO Watch Europe – Review of the year 2008

¹⁰⁸ City of London(2009) The Global Financial Centres Index (GFCI 6)

¹⁰⁹ IFSL (2008) Banking (relates to March 2005 figures)

¹¹⁰ European Banking Federation (2008) Banking Sector Statistics as of 31.12.2008

¹¹¹ Bank of England (2008)

¹¹² IFSL (2010)

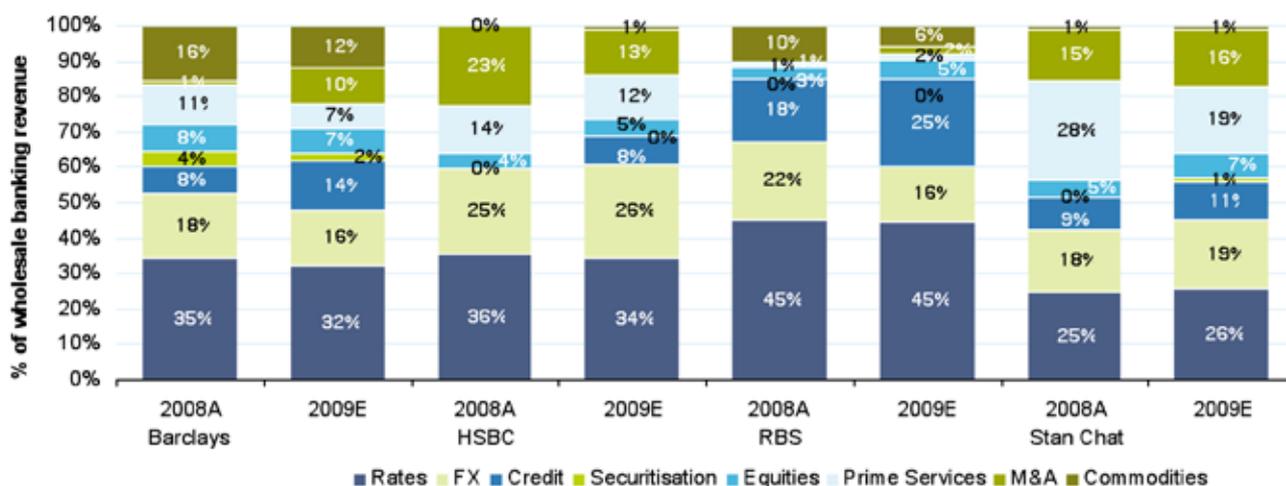
¹¹³ IFSL (2010)

Table 5: Selected wholesale banks with announced and completed M&A deals with any UK involvement, September 2009 year-to-date

Financial advisor	Announced		Completed	
	Value US\$bn	Number of deals	Value US\$bn	Number of deals
Bank of America Merrill Lynch	32.1	15	62.2	13
Citi	116.5	25	72.5	21
Credit Suisse	87.1	23	63.0	15
Goldman Sachs & Co.	144.8	31	18.0	19
Lazard	143.7	31	39.9	26
UBS	146.6	46	62.2	27
Total (with financial advisor)	283.6	540	129.3	451

Source: Thomson Reuters Deals Intelligence: Global M&A Financial Advisory, Third Quarter 2009

This list does not include any of the four main UK-based wholesale banks (Barclays, HSBC, RBS and Standard Chartered). For these banks, M&A accounted for no more than 16 per cent of revenue in 2009 (Standard Chartered), as shown in Figure 24. For all four banks, interest rate charges on bonds issued was the largest segment of revenue, followed in most cases by charges for foreign exchange services, one of banks' most profitable activities.¹¹⁴ This reflects the UK's strong international position for capital raising activities and foreign exchange services.

Figure 24: Revenue share breakdown of the main UK-based wholesale banks, 2008/09


Source: JPMorgan (2009)

¹¹⁴ JPMorgan (2009) The Return of UK Investment Banking

3.2.3 Regulation

The banking industry is regulated directly by the FSA as part of the Tripartite Agreement with the Treasury and the Bank of England. The Basel II Accord, first published in 2004, is the most important regulatory instrument governing the capital requirements of banks. It is made up of three pillars: the minimum Tier 1 capital that a bank should maintain based on its risk profile (Pillar 1); the tools which regulators have available to respond to risk profiles generated in Pillar 1 (Pillar 2); and market discipline, including a disclosure requirement from banks (Pillar 3).¹¹⁵ Since the financial crisis, there have been proposals and revisions to ensure that the Basel II Accord is more robust and more likely to prevent a recurrence of the circumstances that led to the financial crisis.¹¹⁶

The Treasury has identified four main reasons for the failure of the financial markets. While these apply to other financial services subsectors as well, the impact has been most acute in the banking sector. These factors include: excessive leverage and risk taking; an over-reliance upon wholesale funding; an overdependence on particularly risky product streams, such as derivatives; and poor management decisions in respect of acquisitions.

The difficulties of the banking sector have resulted in unprecedented levels of intervention by the government. Direct funding from the government has now reached £80bn¹¹⁷, and the government is responsible for over £1tr¹¹⁸ in realised and potential bailouts.

“If we had not dealt with this problem, this would have had the effect of further exacerbating the downturn and compounding the financial crisis. It was clear that we had to act to clean up banks’ balance sheets.” Paul Myners, Financial Services Secretary to the Treasury¹¹⁹

As a response to the financial crisis, Parliament passed the Banking Act 2009¹²⁰, to strengthen the UK’s statutory framework for financial stability and depositor protection. The Act implements a new permanent special resolution regime, which provides the Tripartite Authorities with tools to deal with failing banks and building societies.

As a result of the financial crisis, retail banks have had to change certain aspects of their operating models. Bank lending has become much tighter and certain products (such as 100 per cent+ and self-certification mortgages) have disappeared from the market.

¹¹⁵ Basel Committee on Banking Supervision, Bank of International Settlements;

¹¹⁶ Basel Committee on Banking Supervision, Revisions to the Basel II market risk framework, January 2009; Enhancements to the Basel II framework, July 2009

¹¹⁷ HM Treasury, Factiva, PwC analysis

¹¹⁸ The Guardian website, 25 November 2009 (see: <http://www.guardian.co.uk/news/datablog/2009/nov/03/bank-bailouts-uk-credit-crunch>)

¹¹⁹ Speech by the Financial Services Secretary to the Treasury, Paul Myners to the Association of Foreign Banks, 11 June 2009 (see http://www.hm-treasury.gov.uk/press_54_09.htm)

¹²⁰ The Banking Act (2009) (see: http://www.opsi.gov.uk/acts/acts2009/ukpga_20090001_en_1)

Wholesale banking is considered to be an originator of the financial crisis,¹²¹ with wholesale trading of derivatives and sub-prime housing loan securities identified as critical factors. As a result, wholesale banking has been severely affected by the crisis. During the credit crunch period of 2007-2008, banks heavily involved in wholesale banking were forced to announce significant write-downs to their investment assets and once Lehman Brothers declared bankruptcy, the wholesale banking landscape changed significantly.¹²²

Initial reactions to the crisis were understandably short-term in nature and in many cases driven by the need for survival. These included a temporary ban on short-selling of financial stocks by the government and an evaporation of trust between banks for counterparty risks, causing global liquidity flows to dry up.¹²³ The government rescued five UK banks as a result of imprudent wholesale banking activities:

- Northern Rock and Bradford & Bingley were heavily involved in securities trading that resulted in very high losses and were completely nationalised,¹²⁴
- RBS and HBOS were likewise heavily involved in derivatives, securities and loans that became toxic and RBS was given the largest bailout of any bank in the world¹²⁵, while HBOS was merged with Lloyds to create a stronger balance sheet;
- however, the resultant Lloyds HBOS entity has struggled to cope with market conditions and also received significant government support¹²⁶.

3.3 Current employment

Banking employs c.534,000 people, with retail banking accounting for 38 per cent (c.398,000 employees) of overall financial services employment and corporate and institutional banking accounting for 13 per cent (c.136,000 employees). London accounts for 22 per cent of employment in retail banking (c.88,000 employees), with a further 10 per cent (c.39,000 employees) located in Scotland.¹²⁷ London also dominates the wholesale banking sector, with 42 per cent of the sector's employment (c.57,000 employees) located in the capital.

3.4 Occupations

The banking value chain is similar to that presented earlier for the entire financial services industry. The activities along it are shown in Figure 25.

¹²¹ PwC The Day After Tomorrow Series (available at: <http://www.pwc.com/gx/en/financial-services/day-after-tomorrow/index.jhtml>)

¹²² Ibid.

¹²³ Ibid.

¹²⁴ HM Treasury website (see: http://www.hm-treasury.gov.uk/press_16_08.htm and http://www.hm-treasury.gov.uk/press_97_08.htm)

¹²⁵ Bloomberg website, 2 November, 2009 (see: <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=ahcxjNVrDXyk>)

¹²⁶ Financial Times website, 3 November 2009 (see: <http://www.ft.com/cms/s/0/f66eea44-c84a-11de-a69e-00144feabdc0.html>)

¹²⁷ Data from HM Treasury

Figure 25: Activities along the banking value chain

	Back office	Middle office	Front office	
	<i>Non-core support functions</i>	<i>Non-customer facing core functions; monitoring and control functions</i>	<i>Customer-facing functions</i>	
Example functions	<ul style="list-style-type: none"> • IT • Compliance • Human resources • Accounting • Record keeping and reporting • Clearance and settlement • Facilities management • Call centres 	<ul style="list-style-type: none"> • Service and product design • Position keeping – calculation of profit and loss • Risk management • Product control • Actuarial (insurance) • Claims handling (insurance) 	<ul style="list-style-type: none"> • Sales and marketing • Customer relationship management • Customer service • Product and service delivery 	Banking
			<ul style="list-style-type: none"> • Sales and marketing • Customer service • Underwriting • Broking 	Insurance
			<ul style="list-style-type: none"> • Trading • Broking • Portfolio management 	Asset management

Source: PwC interviews & analysis

In retail banking, the front-office employees include cashier/counter clerks, sales and marketing staff, branch managers, and contact centre staff. Middle and back-office employees include credit control managers, risk analysts and compliance staff.

In wholesale banking, front-office employees include corporate relationship managers, corporate finance analysts, financial advisors and M&A analysts and advisors. Middle and back-office employees include risk analysts, compliance and product control.

3.5 Current skills profile and provision

Common skills and qualities needed for retail and wholesale banking roles include good numeracy skills, good interpersonal skills and sales skills.

Wholesale banking employees will have technical expertise in areas like international trade, importing and exporting, M&A and foreign exchange.¹²⁸ Additional skills required in wholesale banking include commercial awareness, analytical skills, lateral thinking and initiative.¹²⁹

Retail banking

Entry requirements to retail banking vary. Some banks may ask for four GCSEs or equivalent when recruiting customer service clerks, with IT skills also in demand.¹³⁰ Experience of cash handling and customer care is an advantage, therefore there is potential for transfer into banking from other industries, such as retail.

¹²⁸ FSSC website (see: http://www.fssc.org.uk/corporate_business_to_business_banking.pdf)

¹²⁹ FSSC website (see: http://www.fssc.org.uk/corporate_business_to_business_banking.pdf)

¹³⁰ FSSC website (see: <http://www.fssc.org.uk/cashier.pdf>)

For people aiming to reach higher positions in retail banking, such as branch management and customer relationship management, there are typically three main routes into the industry:

- joining a mainstream retail banking graduate training programme;
- working up from branch operations, usually joining a fast-track in-house training programme; or
- via a retail banking apprenticeship and joining an accelerated training programme.¹³¹

As with many occupations in financial services, those working up from retail banking operational roles to branch management roles can enter with a vocational qualification. This could be a general vocational qualification such as a BTEC, NVQ/Scottish Vocational Qualification or a specialist diploma, for example, the Diploma in Business, Administration and Finance.¹³²

Employers often provide comprehensive in-house training, which is usually complemented by a wide selection of professional customer service and financial retail qualifications, from introductory level upwards. Professional qualifications vary depending on the level of entry. Those working their way up the career ladder may undertake one of the following qualifications: an Institute for Fiscal Studies (IFS) Foundation Certificate in Personal Finance (Level 1); an NVQ in Retail Financial Services (Level 2); or the IFS Diploma in Financial Studies (Level 3).

Graduate trainees usually join a training programme at a higher level and professional qualifications undertaken reflect this. These may include: the Professional Diploma in Financial Services Management (Professional DFMS); the Applied Diploma in Retailing Financial Services (Applied DFMS Retail); or the Applied Diploma in Corporate Banking (Applied DFMS Corporate).

Retail banking branch managers may also study towards technical qualifications for regulated financial products, including but not limited to: the Level 3 IFS Certificate in Mortgage Advice and Practice (CeMAP); the Level 3 IFS Certificate for Financial Advisers (CeFA); the SCQF Level 8 CIOBS (Chartered Institute of Bankers in Scotland) Certificate in Investment Planning; or the SCQF Level 8 CIOBS Mortgage Advice and Practice Certificate.

Wholesale banking

For mainstream wholesale banking positions, applications are encouraged from graduates in a wide range of disciplines, and there is demand for trained specialists with additional qualifications such as law, accountancy or business management. Opportunities are also available in most firms for those seeking a career in IT. Investment banking can offer an excellent career to very motivated school leavers, but with ever more competition, graduate and professional qualifications are increasingly regarded as a minimum.¹³³

¹³¹ FSSC website (see: http://www.fssc.org.uk/branch_management.pdf)

¹³² FSSC website (see: http://www.fssc.org.uk/branch_management.pdf)

¹³³ Courses & Careers UK website (see: <http://www.ca.courses-careers.com/banking.htm>)

The usual minimum entry requirement to wholesale banking is an upper-second class honours degree or a professional qualification in law or accounting. There is no particular preference for any specific degree subject, although a numerate discipline or subject such as economics, law or business studies can prove to be particularly useful. Graduates commence as trainees and can progress rapidly to senior managerial appointments, depending on their performance and the potential they show.¹³⁴

Inter-personal skills are of great importance, as are imagination, application and adaptability. Fluency in foreign languages is also considered an asset.¹³⁵

Wholesale banking is a complex area and there are many generic as well as more specialist qualifications. During training and once in post, wholesale banking employees are usually encouraged to work towards one of the following: the IFS Applied Diploma in Corporate Banking (Applied DFMSM Corporate); the CIOBS Advanced Diploma in Business and Corporate Banking; the SII Certificate in Corporate Finance; or the CFA qualification.¹³⁶

Investment firms regulated by the FSA are required to employ staff who are “competent,” as defined by the FSA.¹³⁷ A major component of competence is knowledge of the services and products of the relevant industry sector. For many job functions, staff are expected to hold a qualification which appears on one of the lists published by the FSSC.¹³⁸ The Appropriate Exams list applies to staff dealing with retail clients and the Recommended Exams lists applies to staff dealing with wholesale clients.¹³⁹

3.6 Unfulfilled skills needs

3.6.1 Retail skills shortages

Retail banking is one of the sectors most affected by skills deficits. As shown in Figure 26, 70 per cent of bank and building societies who responded to the FSSC employer survey (2006) reported difficulties in recruitment due to competition from other employers and 69 per cent reported difficulty due to a lack of skilled and experienced or qualified people. The occupations which are creating the greatest challenges for participating recruiters, with three quarters reporting difficulties, are professional and technical roles and sales and customer service roles.

¹³⁴ London Investment Banking Association website (see: <http://www.liba.org.uk/>)

¹³⁵ London Investment Banking Association website (see: <http://www.liba.org.uk/>)

¹³⁶ FSSC website (see: http://www.fssc.org.uk/corporate_business_to_business_banking.pdf)

¹³⁷ FSA Handbook SYSC 3.1.6R

¹³⁸ http://www.fssc.org.uk/appropriate_exam_list_15.html?i=1&l1=true

¹³⁹ Securities and Investment Institute website (see: <http://www.secinst.co.uk/bookmark/genericform.aspx?form=29848780&URL=qualifications>)

Retail banking is not an attractive sector for the majority of younger people as the retail segment does not have the prestige or favourable compensation relative to competing sectors (e.g. retail sales) which is enjoyed by the wholesale financial sector (which competes with professions such as law, accountancy and similar careers).

“There is fundamentally a big mismatch between the client facing profile/responsibility of branch employees and what the industry pays – notably less than other retail companies,, such as mobile phone companies, which are competing for the same talent pool.” PwC financial services team

Figure 26: Key causes of recruitment difficulties for retail banking



Source: FSSC (2007)

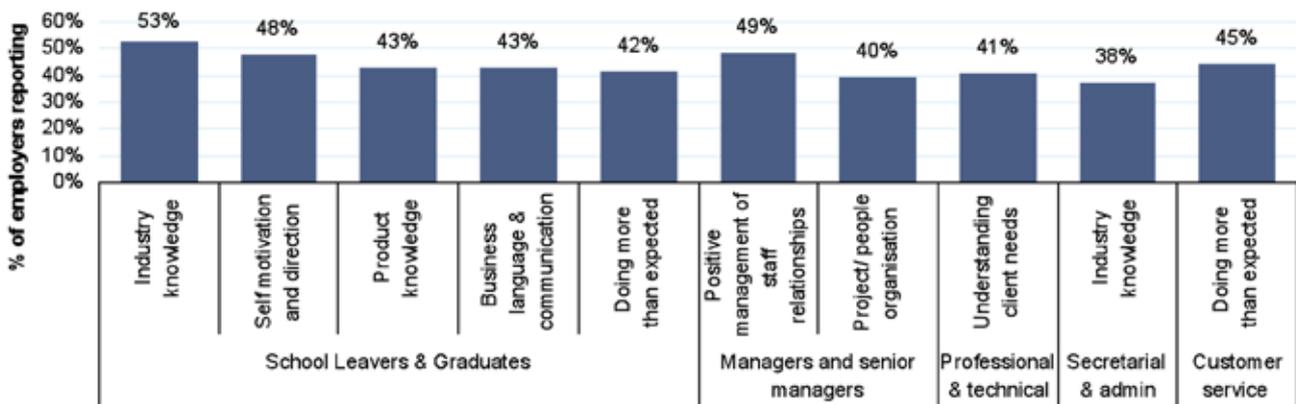
Competition for employees is an issue both at the junior level and for middle management roles. At the graduate level, retail banking employers struggle to attract graduates when faced with strong competition from prestigious employers in other financial services sectors, and at the managerial level, the relatively uncompetitive salary in retail banking means employers are frequently outbid for well qualified professionals.

3.6.2 Retail skills gaps

The challenges in the retail banking sector are further compounded by retail banking having the most significant skills gaps in the financial services sector. The sector’s skills shortages and skills gaps are inherently linked: the large proportion of the skills gaps identified among the school leavers and graduates group is likely to be a result of employers having to hire candidates who don’t have the necessary skills at the outset, simply because there is insufficient supply of qualified individuals. Nearly 70 per cent of participating employers in the 2006 FSSC study reported skills gaps in the school leavers and graduates group.

Figure 27 highlights that the most frequently reported skills gap amongst school leavers and graduates is knowledge of the retail banking sector; however, a large proportion of the skills gaps in this group are general attitudinal/motivational issues, including a lack of self direction, lack of motivation and a lack of drive to do more than is explicitly asked.

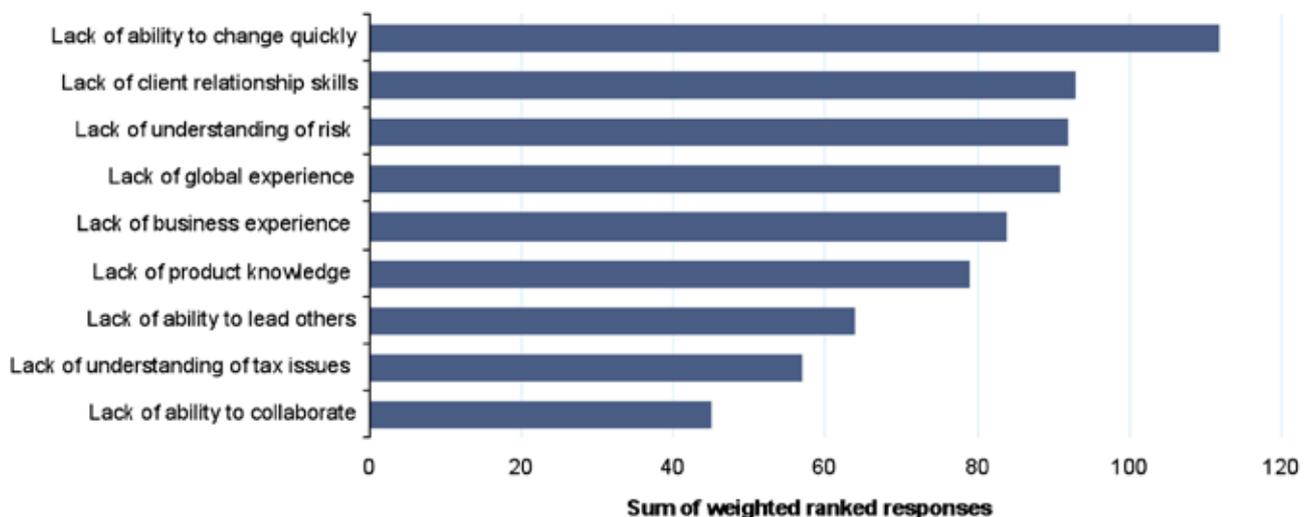
Figure 27: Top skills gaps identified in retail banking, by employee type



Source: FSSC (2007)

In private banking, the economic crisis has presented challenges for which client relationship managers (CRMs) have neither the experience nor the training.¹⁴⁰ In PwC’s Global Private Banking and Wealth Management Survey, respondents identified a lack of ability to adjust to change quickly as the greatest area of weakness for CRMs, followed by a lack of client relationship skills and a lack of understanding of risk (Figure 28).

Figure 28: Greatest areas of weakness identified among CRMs



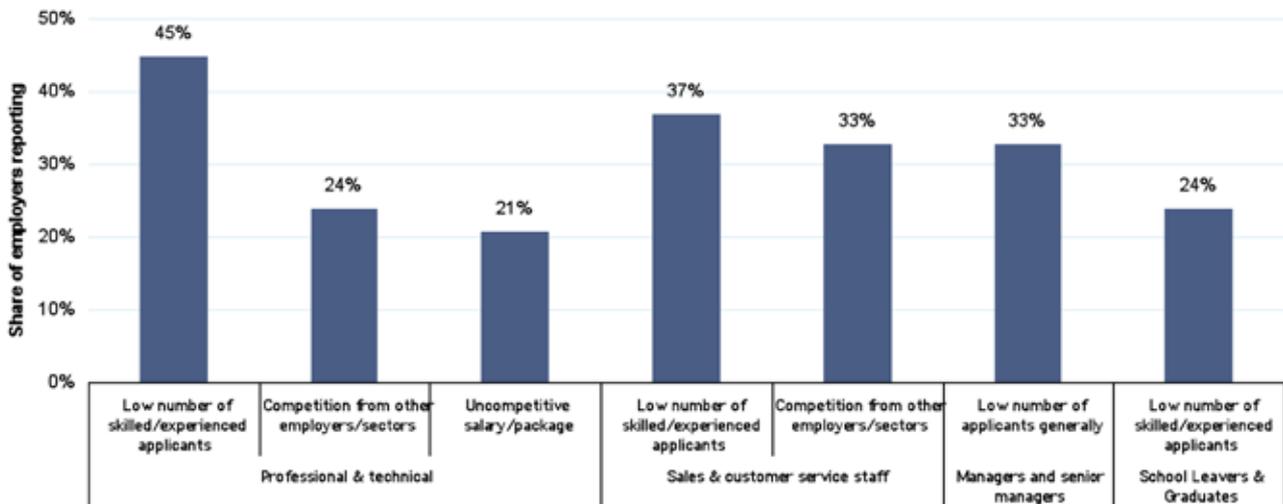
Source: PwC (2009) Global Private Banking and Wealth Management Survey

¹⁴⁰ PricewaterhouseCoopers (2009) Global Private Banking and Wealth Management Survey.

3.6.3 Wholesale skills shortages

Within the financial services sector, wholesale banking has the lowest level of skills shortages. The prestigious reputation and attractive remuneration packages in the sector means employers are able to draw the best people from across the UK and around the world. However, despite London ranking as one of the leading places internationally in terms of availability of skills for the financial and business sectors, employers have still experienced a shortfall of skilled candidates in this sector as the labour pool struggles to keep pace with the cyclical demand in the sector (although at present, shortages have been eased by economic conditions). The key shortfall is in the professional and technical groups because new specialisms are created when new products are launched and there may be a lag before individuals have the necessary skills. The FSSC suggests there is also a shortage at the managerial level because “some professionals in the sector have little desire to become managers: in some areas it is seen as tantamount to a loss of technical edge”. Figure 29 outlines the key causes of recruitment difficulties in wholesale banking by employee type.

Figure 29: Causes of recruitment difficulties for wholesale banks, by employee type



Source: FSSC (2007)

3.6.4 Wholesale skills gaps

The significant resources available for internal training, combined with a culture of retaining only the best employees means that, relative to other sectors, there are fewer skills gaps in wholesale banking. On the technical side, gaps tend to be relatively short-term and related to new skills requirements, generated, for example, by a new product launch. These short-term gaps are often solved through internal training. The key skills gaps in the sub-sector, as shown in Figure 30, are product and industry knowledge across different employee groups and managerial ‘soft skills’, including ability to cope with stress and positive management of staff relationships.

Figure 30: Top skills gaps identified in wholesale banking, by employee type



Source: Source: FSSC (2007)

4. Industry insight: Insurance

Chapter summary

The insurance sub-sector is a large component of financial services, with a workforce of c.317,000. For the purposes of this report, we have broken it down into three main segments:

- life and pensions;
- general insurance (also called non-life); and
- reinsurance.

While life and pensions generates the largest annual premiums, general insurance is the largest segment by employment, with approximately a third of insurance workers involved directly in the sector (c.106,000), compared to c.72,000 directly employed in life and pensions. The wholesale insurance sector employs c.50,000 people, of which 80 per cent are located in London. The remaining c.89,000 workers in insurance are employed in various support functions, including agency, brokerage and risk assessment.

The segments are affected by different drivers: life and pensions business has been strongly affected by the financial crisis; general insurance tends to be more resilient.

There are different skills needs for the different segments. Most positions in retail insurance require basic quantitative skills and experience tends to be more important than qualifications. However, in wholesale insurance, strong quantitative analysis skills are more valued and qualifications from bodies such as the Chartered Insurance Institute (CII) are important.

There has been a historical trend of outsourcing non-core functions, with some of these moved offshore. Along with general improvements in efficiency, this has resulted in a decline in total employment in the sector.

Insurance has traditionally had difficulties in attracting the most highly qualified candidates to the industry as the industry lacks the appeal and financial rewards of other financial services careers such as wholesale banking or asset management. Senior roles in the sector tend to be occupied by middle-aged, white middle-class men. As the industry is largely based on experience rather than qualifications, it is difficult for people to transfer into the industry.

There are several key skills shortages apparent, due to a lack of applicants and the ageing workforce. There are particular shortages of actuaries, which will intensify as demand increases while supply is held back by long training periods, low pass rates and low industry attractiveness. There are also likely to be shortages of risk management, IT and operations staff in the near- to medium-term future.

The key skills gaps are found in entry-level positions, typically filled by school leavers and graduates, who lack basic industry and technical knowledge. It is reported that some senior staff can lack appropriate management skills.

4.1 Introduction

The insurance sector is the second major sector in the UK financial services after banking, contributing c.£22bn to the economy, or 1.6 per cent of GVA.¹⁴¹ This chapter of our report describes the insurance market in the UK, and the current status of employment and skills in the sector. It is structured as follows:

- Current state of the UK market;
- Current employment;
- Occupations;
- Skills profile and provision; and
- Unfulfilled skills needs.

4.2 Current state of the UK market

This section of the report considers the current state of the UK insurance market, in terms of its importance to the UK economy; market segmentation; growth in the sector in recent years; the regional distribution of the sector across the UK; market supply; and regulation of insurance, particularly in the context of the current economic crisis.

¹⁴¹ IFSL Insurance Update 2009; excludes brokers and other auxiliary professions

4.2.1 Importance to the UK economy

The UK insurance industry is the largest in Europe and the second largest in the world.¹⁴² Insurance in the UK accounts for 11 per cent of total worldwide premium income¹⁴³, and the UK has an almost 60 per cent higher rate of premium paid per head than the US and France, and over double that of Japan, Germany and Italy.¹⁴⁴ Furthermore, the UK's total insurance premiums as a percentage of GDP are far higher than any of the other major insurance markets.

Table 6: Comparison of international insurance market

	Total \$bn	Gross insurance premiums of which (%)			Premium per head (\$)	Premiums as a % of GDP
		Life	Non-life	% of share of world		
US	1,230	47	53	30	4,087	8.9
UK	464	75	25	11	7,114	15.7
Japan	425	78	22	10	3,320	9.6
France	269	70	30	7	4,148	10.3
Germany	223	46	54	5	2,662	6.6
Italy	142	62	38	3	2,322	6.4
South Korea	117	69	31	3	2,384	11.8
Others	1,191	57	43	29		
World	4,061	59	41	100	608	7.5

Source: International Financial Services, London (IFSL) (2008) Insurance Update (from SwissRe)

The relative importance of insurance in the UK is due not only to the relatively high penetration of insurance products in the UK, but also the global orientation of the country's wholesale insurance business, which is centred predominantly in London.

4.2.2 Market segmentation

In order to understand the drivers of different parts of the insurance sector and to identify different employment dynamics, we are using the segmentation described in Chapter 2, which splits insurance by type (life and pensions, general and reinsurance) and customer type (retail and wholesale). This is laid out again in Table 7.

¹⁴² Association of British Insurers – UK Insurance - Key Facts 2009

¹⁴³ Association of British Insurers, UK Insurance – Key Facts 2009

¹⁴⁴ IFSL Insurance Update 2008

Table 7: Insurance activity, segmented by activity and customer type

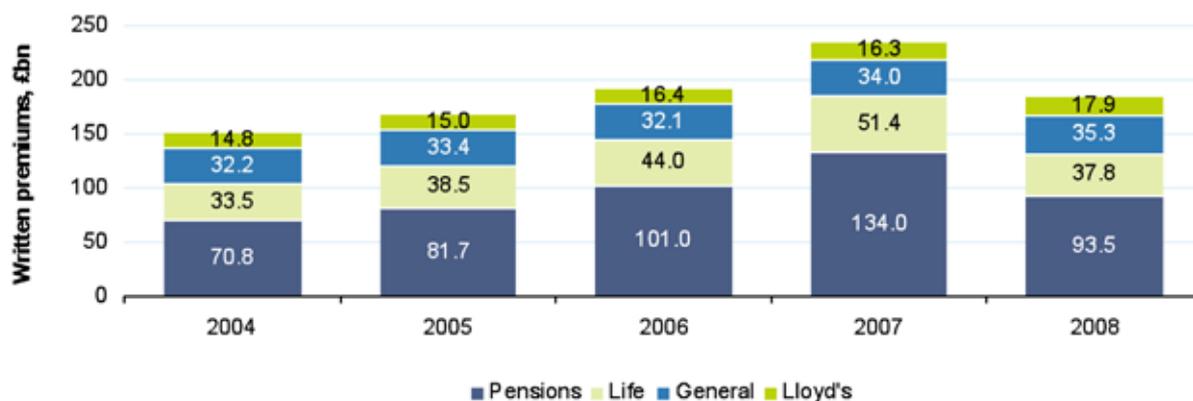
Customer		Retail	Wholesale			
Activity		Individuals	Businesses / Corporations		Financial Services Companies	Government
Insurance	Life and Pensions		Small & Medium Enterprises (SMEs)	Large Corporations		
	General	•Life insurance, pensions and long-term investment products for individual customers	•Group pension schemes for groups of individuals / employees, typically for large employers (corporations and financial services companies)			
	General	•Personal products for individuals including home, motor and health insurance	•Commercial products for businesses including commercial and professional indemnity, property and buildings insurance, business continuity, disaster / emergency insurance •Commercial products often referred to as wholesale business			
	Reinsurance	•n.a.		•n.a.	•Reinsurance of a wide range of specialist risks, typically international in nature, including aviation, marine, life and financial risks*	

Source: PwC Analysis

The segments shaded dark grey comprise the London Market, which is a market for reinsurance and general insurance (both personal and commercial) business. The London Market is defined as Lloyd's plus the London companies market. Reinsurance is primarily carried out in the London Market, but also by a number of large foreign reinsurance companies based in the UK, but outside of the London Market.

The size of the insurance industry is typically measured by the value of the premiums written in a year. The industry grew strongly up until 2007, with total net premiums increasing 16.0 per cent p.a. between 2004 and 2007 to £235.8bn.¹⁴⁵ However, the sector has been impacted since 2008 by the financial crisis, with the written premiums income of pensions and life business declining significantly, as shown in Figure 31.

¹⁴⁵ IFSL (2008) Insurance Update. Total net premiums include written premium less reinsurance premiums paid by the insurer

Figure 31: Total written premiums for insurance sub-sectors 2004-2008

Source: Association of British Insurers statistics, Lloyd's of London Annual Report¹⁴⁶

Premiums for life and pensions, which account for more than half of the total market, fell 29 per cent to £131.2bn for Association of British Insurers (ABI) members in 2008,¹⁴⁷ largely as a result of the financial crisis. Companies hit by the recession have contributed less to pension funds and have looked for ways to move away from defined-benefit pension schemes.¹⁴⁸ General insurance premiums collected by ABI members however increased by 3.8 per cent in 2008, amounting to £35.3bn. Lloyd's premium income has behaved counter-cyclically, with a 35 per cent increase in gross written premiums in the first half of 2009 compared to the same period in 2008,¹⁴⁹ but this has been driven predominantly by foreign exchange movements.¹⁵⁰

Pensions

Pensions comprise the largest and arguably most important sub-segment of the UK insurance market. Pensions fall into two categories: occupational pensions and personal pensions.

Table 8 provides an indication of the distribution of pensions between these two categories, broken down further by whether or not pensions are defined benefit or defined contribution.

¹⁴⁶ Data set includes all Association of British Insurers members (covering 90 per cent of market), some non-Association of British Insurers members and Lloyd's of London

¹⁴⁷ Association of British Insurers (2009) UK insurance - key facts. (Association of British Insurers members represent around 90 per cent of insurance companies in the UK, the main exception being Lloyd's of London)

¹⁴⁸ Mintel (2009) Personal and Stakeholder Pensions UK, Mintel (2009) Life and Protection UK

¹⁴⁹ Lloyd's of London Interim report 30 June 2009

¹⁵⁰ 78 per cent of Lloyd's business originates from outside the UK

Table 8: Pension schemes in the UK, 2008

Pension type	Occupational Pensions			Personal Pensions	
	Defined benefit (DB) pension	Defined contribution (DC) pension	Hybrid DB/DC pension	Defined contribution (DC) Group	Defined contribution (DC) Retail
Pension scheme's primary contributor	Employer (individual may contribute)	Employer (individual may contribute)	Employer (individual may contribute)	Individual, (employer may contribute) ¹⁵¹	Individual only
Number of members	8.8m	1.5m	6.3m	3.2m ¹⁵²	14m ¹⁵³

Source: The Pensions Regulator; Mintel

Based on total premium income, the pensions market grew at an average of 11 per cent p.a. between 1998 and 2007 and by 24 per cent p.a. between 2004 and 2007. By 2007, net premium income totalled £134bn.¹⁵⁴ Growth was largely fuelled by strong growth in occupational pensions – total premium income for these pensions grew by 28 per cent p.a. between 2004 and 2007, double the growth rate of personal pensions.

Figure 32: Premium breakdown of pensions, 1998-2008

Source: Association of British Insurers

Over the course of 2008, however, total pension premiums fell 30 per cent to £93.5bn. This was driven by a 36 per cent fall in net premium income from occupational pensions, while net premium for personal pensions fell by 13 per cent.¹⁵⁵ The fall in occupational pensions was likely to have been driven predominantly by the closure of defined benefit schemes.

¹⁵¹ Defined contribution group pensions are pensions arranged with the assistance of an employer, even though the contract is between an individual/employee and a pension provider. The employer may have to contribute alongside the employee for a group personal pension order to secure a contract with a pension provider

¹⁵² Based on Annual Survey of Hours and Earnings conducted by the ONS. Would include all group personal pensions and stakeholder group pensions that are contracted through the employer

¹⁵³ Based on pension scheme returns from pension providers received by the Pensions Regulator. This will refer to the number of 'memberships' that have been purchased from a pension provider by an individual. An individual can purchase multiple 'memberships', and so 14m does not refer to the number of individual members but rather the number of individual memberships

¹⁵⁴ Association of British Insurers (2009) UK insurance - key facts (based on Association of British Insurers members)

¹⁵⁵ Association of British Insurers (2009) UK insurance - key facts (based on Association of British Insurers members)

The financial crisis has also impacted defined contribution schemes, particularly within the personal pensions market. In the current climate, some members may be unable to contribute to their scheme due to unemployment, some may forgo increasing their contributions due to personal financial circumstances, and new members are less likely to join.

The pensions market continues to shift away from defined benefit schemes run by employers to defined contribution schemes, mainly run by insurers and it is likely that the financial crisis will accelerate this trend. Longer employee life expectancy and uncertain investment returns have left many defined benefit schemes with a significant deficit. As a result, the number of members in open private sector schemes dropped from a peak of 6.5m in the early 1990s to 3.6m in 2007.¹⁵⁶ As companies move away from defined benefit towards defined contribution, there is likely to be a greater demand for pension managers and investment specialists, as well as advisory roles to ensure that customers purchase products suited to them and that their pensions are managed in the best possible way.

“There are different skillsets required for administering defined contribution and defined benefit schemes; there are more rules to defined benefits.” National Association of Pension Funds

Overall take-up of pensions is low in the UK and government is acting to address this issue. The Pensions Act 2008 aims to ensure that, from 2012, all employers automatically enrol jobholders into good quality workplace pension schemes and make a minimum contribution. The Act will also bring into effect a personal accounts scheme in 2012, aimed at median to low earners.¹⁵⁷ The Pensions Regulator currently estimates that around seven million people have no pension provision whatsoever. The state retirement age for women is also set to increase gradually from 60 to 65 between 2010 and 2020. Between 2024 and 2046, the State Pension retirement age will rise further, from 65 to 68.

The market for personal contract-based pensions is fragmented. The main providers include Aviva plc, Lloyd’s Group, Legal & General Insurance, AXA Insurance and Aegon. Occupational pensions generally are managed by a separate entity that is created by the company providing the pension. The main insurers for occupational trust-based pensions are Prudential Insurance, Standard Life, Aegon, Legal & General and Canada Life.¹⁵⁸

¹⁵⁶ Ibid

¹⁵⁷ DWP website (see: www.dwp.gov.uk)

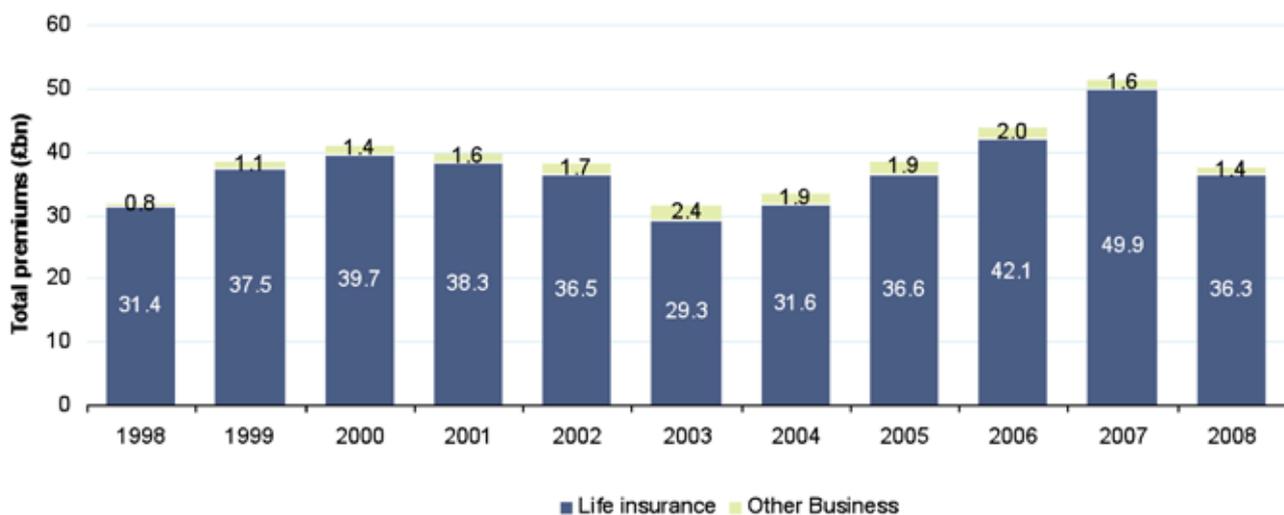
¹⁵⁸ Association of British Insurers. Occupational Pension Business will include occupational pensions, EPPs, SASSs, AVCs, TIPs, and Bulk Buyouts. Managed fund business has been excluded.

Life insurance

There are three generic types of life insurance protection: term assurance, whole-of-life and endowment insurance. Term assurance only pays out if death occurs within a fixed term and usually covers mortgage debt. Whole-of-life insurance has a smaller scope of coverage, such as inheritance tax or funeral expenses. Endowment life assurance policies are essentially long-term savings schemes that have life assurance attached, often used to repay the capital on interest-only mortgages.¹⁵⁹ Life insurance can also be segmented between pure protection policies or investment policies. Pure protection policies are designed to provide a benefit in the event of death, while investment policies aim to facilitate the growth of capital and were commonly viewed as the ideal investment for saving for school fees, inheritance tax or mortgage debt.

The life insurance market grew at an average of 2.2 per cent p.a. in total premium income from 1998 to 2007 and at a rate of 16.4 per cent p.a. from 2004 to 2007, reaching a total of £51.4bn in total premium income in 2007. This was driven by life insurance (including annuities), which increased at a rate of 16 per cent p.a. from 2004 to 2007, while other business (including income protection) declined in total premiums by 7 per cent p.a. over the same period.¹⁶⁰

Figure 33: Premium breakdown of life insurance, 1998-2008



Source: Association of British Insurers

In 2008, there was a significant drop in the value of total premiums for life insurance. Total premiums declined by 27 per cent compared to 2007, driven mainly by life and annuities.

¹⁵⁹ Mintel (2009) Life and Protection UK

¹⁶⁰ Association of British Insurers (2009) UK insurance - key facts (based on Association of British Insurers members)

During the recession, consumers cut back on their life insurance. In the fourth quarter of 2007, consumers spent net £5.6 billion on life insurance (seasonally adjusted), but by the first quarter of 2009, this figure had declined to £4.8 billion.¹⁶¹ However, the number of new policies sold rose, reflecting the rapid growth in particular policies such as low-value whole-of-life cover for over-50s. Mortgage-related term assurance and endowments have also been affected by the downturn in the housing market. These types of life insurance are reliant upon mortgage issuance and are closely linked to the performance of the housing market.¹⁶²

Market penetration is relatively low, with 26.1m adults holding no life cover in 2009. Mintel research indicates that there is relatively low market penetration due to consumer attitudes towards products related to death, a misunderstanding of the costs and general financial ignorance. Consumer attitudes have begun to be addressed by protection schemes and the government through the industry-backed Consumer Protection Insurance Engagement Campaign, the FSA's actions following the Thoresen review and by regulatory and industry action to reduce consumer complaints.¹⁶³

The Retail Distribution Review (RDR), initiated by the FSA in 2006, sought to address customer service issues within the industry, and in June 2009 the FSA issued its consultation paper on delivering the RDR, with responses due by 30 October 2009.¹⁶⁴

Of the £758m of new life insurance products sold in 2008, £367m (48 per cent) were sold through an IFA or distributor offering products from the whole of the market. £286m (38 per cent) was sold through a single-tie or multi-tie distributor (distributors who sell products from one or more providers exclusively) and £105m (14 per cent) was sold directly without an intermediary. Bancassurance (insurance products attached to a banking product such as a mortgage) are a key source of revenue and are mainly distributed via banks selling the products of an insurance subsidiary. Between 2006 and 2008, these products accounted for between 27 per cent and 29 per cent of premiums.¹⁶⁵

¹⁶¹ Mintel (2009) Life and Protection UK

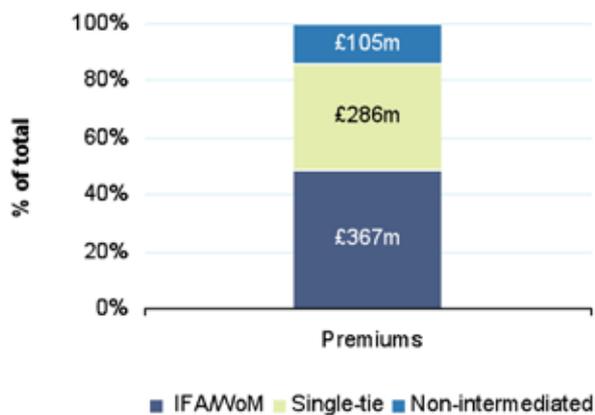
¹⁶² Ibid.

¹⁶³ Mintel (2009) Life and Protection UK

¹⁶⁴ FSA website (see: www.fsa.gov.uk)

¹⁶⁵ Mintel (2009) Life and Protection UK

Figure 34: Breakdown of distribution method for life insurance premiums sold



Source: Mintel (2009)

The main providers of life assurance are Legal & General; Aviva; Aegon Scottish Equitable; HSBC; and Skandia Life.¹⁶⁶

Non-life insurance

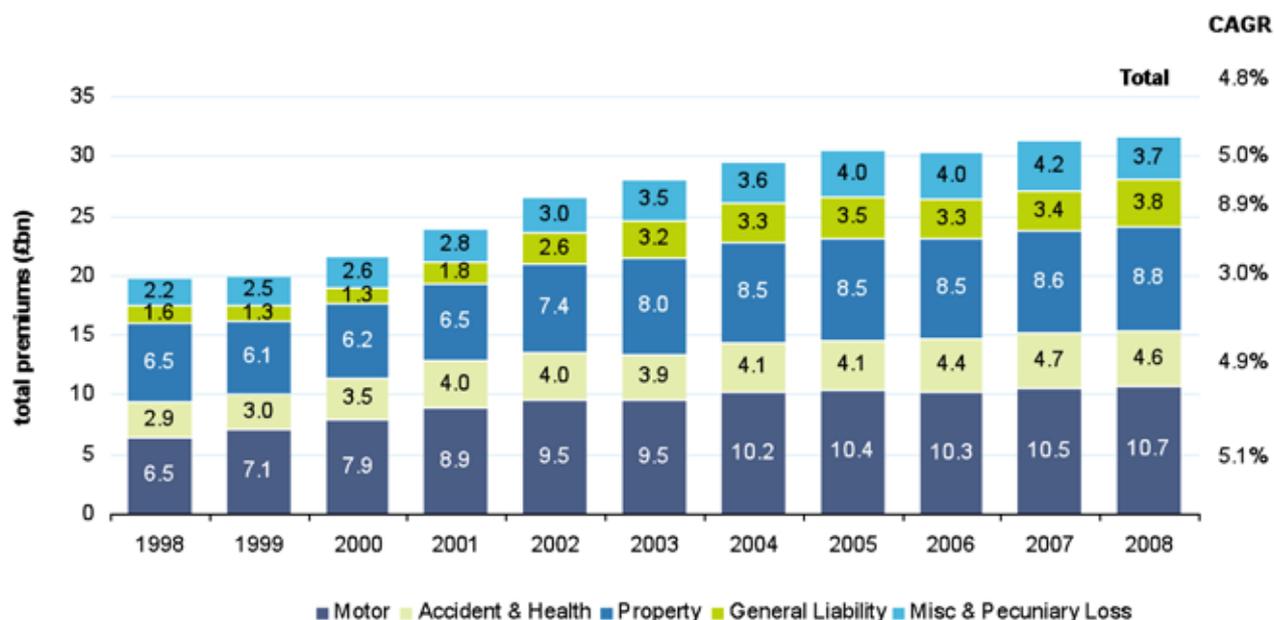
The supply of general (or non-life) insurance may also be segmented by customer type: personal products sold to private individuals and, commercial products sold to businesses. General insurance is dominated mainly by motor and property insurance, followed by accident and health, general liability and pecuniary loss.¹⁶⁷ All sub-sectors have remained broadly stable in terms of market share and gross written premium over the past five years, as shown in Figure 35.¹⁶⁸ The general insurance industry is fundamentally mature and stable and premiums are resilient to recession. Between 2007 and 2008, total general insurance premiums grew 1.1 per cent to reach £31.7bn.

¹⁶⁶ Association of British Insurers

¹⁶⁷ Pecuniary loss are financial losses that may have occurred, for example consequential loss and mortgage indemnity policies

¹⁶⁸ Mintel (2008) General Insurance Overview UK

Figure 35: Non-life premiums by type of insurance



Source: Association of British Insurers¹⁶⁹

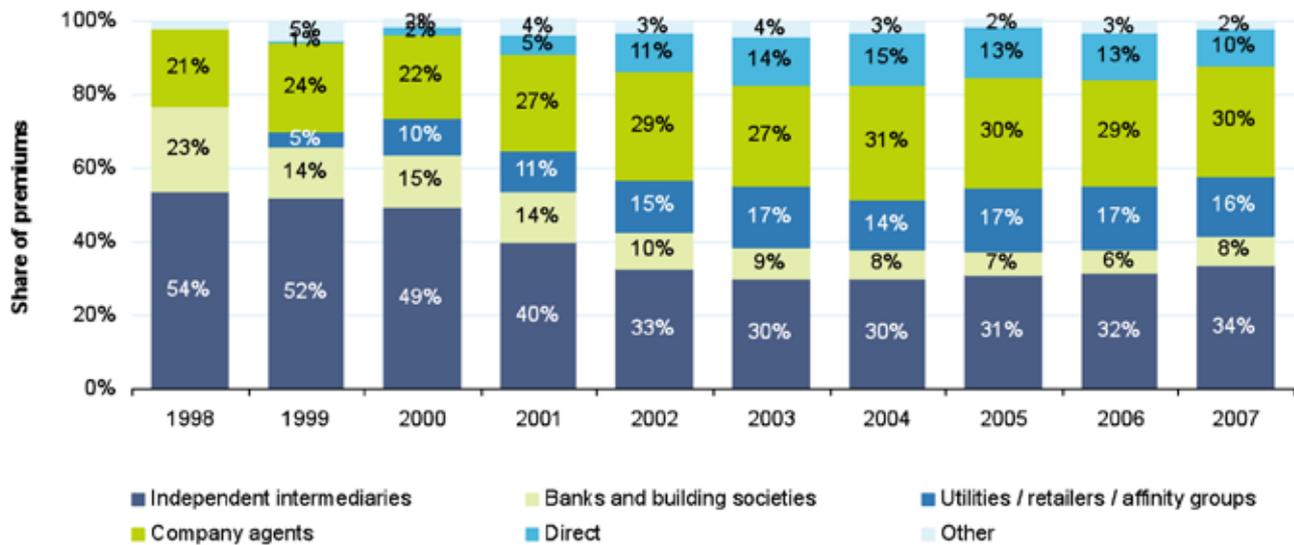
Retail insurance accounts for more than half the general insurance market. The largest sub-segments are private motor insurance and domestic property insurance, both of which are part of retail. These products are either required by law (e.g. third party motor insurance), or made mandatory through other contracts (e.g. mortgages requiring building insurance). Other products, such as household contents insurance, are discretionary.

The penetration of personal insurance products in the UK is high. In September 2008, a consumer review of the penetration of insurance products in the UK found that 82 per cent of adults aged over 18 had at least one insurance product. Private motor and domestic property insurance were the most widely held, with 65 per cent and 68 per cent of adults holding them respectively.

In the retail segment, insurance companies have increased their share of distribution in recent years by marketing directly to consumers. In the last three years, however, intermediated channels have begun to regain ground, due to the growing importance of price comparison websites such as www.confused.com and www.moneysupermarket.com. Intermediaries remain the most important channel for distribution of personal general insurance products, as shown in Figure 36.

¹⁶⁹ Data for ABI members operating in the London Market in these non-life sectors will also be captured in this analysis

Figure 36: Proportional distribution for retail general insurance, by value 1998-2007



Source: Association of British Insurers

The growing importance of comparison websites has made the general insurance market one of the most competitive segments in UK retail financial services. Price is one of the main purchase criteria when people buy motor or domestic property insurance, so the retention of existing customers has become the foundation of many general insurers’ retail strategies.¹⁷⁰

Almost all general commercial insurance is sold via a broker, because of the supplementary advice required. Some small and medium enterprises (SMEs) may however buy general commercial insurance directly. A limited number of very large companies operate their own captive insurance company, reinsuring only those risks deemed too large to self-insure.¹⁷¹

The main providers in the general insurance market for both retail and commercial insurance are Aviva, RBS Insurance, AXA Insurance, RSA and Zurich Insurance.¹⁷²

Wholesale market

We have defined the wholesale insurance market as shown earlier in Table 7. A major feature of the UK insurance market is the London Market (shaded grey in Table 7), which is defined as Lloyd’s plus the London Companies Market. The London Market is primarily wholesale insurance, including reinsurance, but also includes some retail insurance. Reinsurance is primarily carried out in the London Market, but also by a member of large foreign reinsurance companies based in the UK but outside the London Market.

¹⁷⁰ Mintel (2008) General Insurance Overview UK

¹⁷¹ PwC expert

¹⁷² Association of British Insurers

London is one of the world’s most important centres for wholesale insurance, due to the presence of specialist underwriting expertise and Lloyd’s. The City is the only place in the world where all 20 of the world’s largest insurers and reinsurers are represented.¹⁷³

Reinsurance is a method of passing on insurance risks, which enables insurers to take on larger risks than their capital would otherwise allow. Reinsurance serves to protect insurers against single large claims or a large aggregation of claims by spreading the risk between several reinsurance companies.

The London market generated c.£24.5bn in premiums in 2007, c.67 per cent of which was through the Lloyd’s market, 28 per cent through insurance companies and the remainder through protection and indemnity clubs (a form of mutual insurance). In 2008, premiums written through Lloyd’s increased a further 10 per cent, from £16.4bn to £18.0bn.¹⁷⁴ Lloyd’s underwrote £6.3bn in gross reinsurance premiums that year,¹⁷⁵ with Association of British Insurers member companies underwriting a further £1.2bn.¹⁷⁶ In the first half of 2009, Lloyd’s increased its total written premiums by 35 per cent compared to the first half of 2008, reporting total written premiums of £13.5bn.¹⁷⁷

Lloyd’s insures a wide variety of risks. The market is an international one, and only 22 per cent of its business originates from UK risks. As shown in Figure 38, the majority of risks are from North America (44 per cent) or Europe (38 per cent, including the UK), reflecting the relative sophistication of these markets.¹⁷⁸

Figure 37: Lloyd’s total business by class

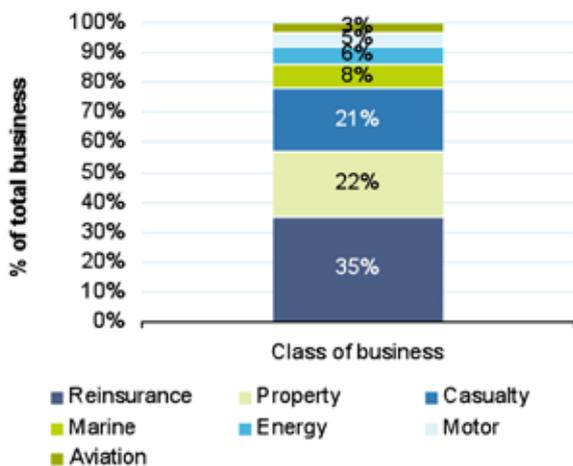
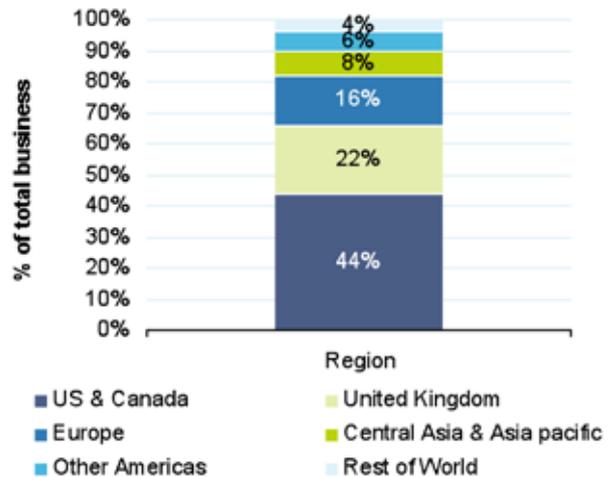


Figure 38: Lloyd’s total business by region



Source: Lloyd’s (2008) Annual Report 2008

¹⁷³ International Underwriting Association of London website (see: <http://www.iaa.co.uk/Content/NavigationMenu/About/IUASStandardPresentationSlides/default.htm>)

¹⁷⁴ Lloyd’s (2008) Annual Report 2008

¹⁷⁵ Lloyd’s (2008) Annual Report 2008

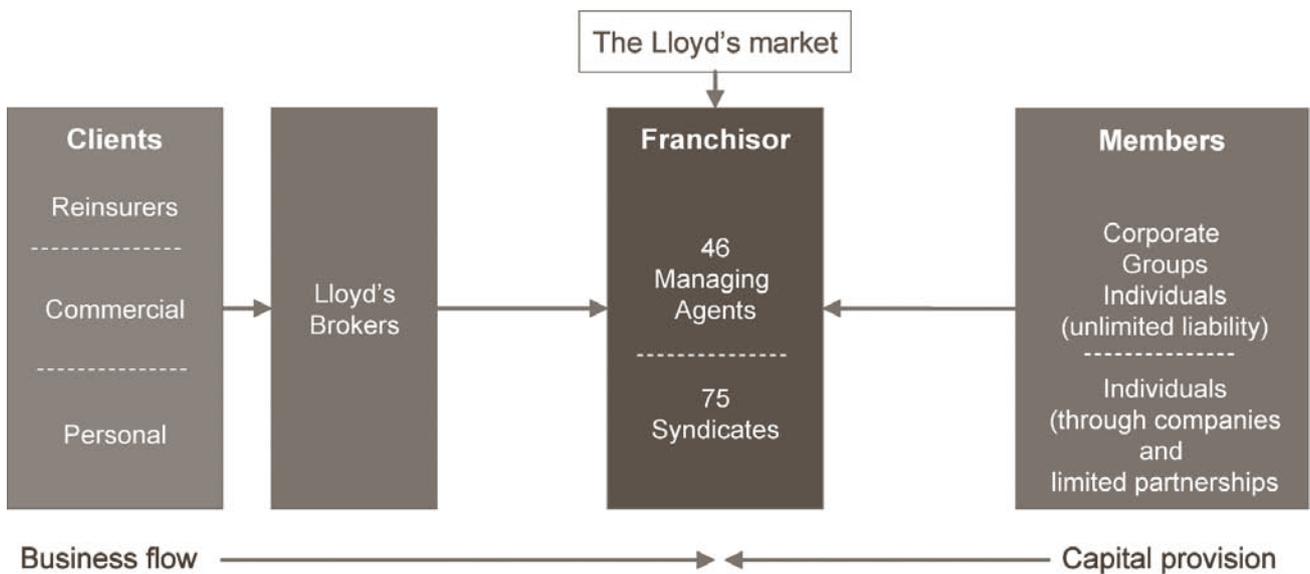
¹⁷⁶ Association of British Insurers

¹⁷⁷ Lloyd’s of London Interim report 30 June 2009

¹⁷⁸ Lloyd’s of London, Fact Sheet

Much of London Market is transacted at Lloyd's, which has been underwriting complex international risks for more than 300 years. Lloyd's typically insures complex wholesale risk by linking clients seeking insurance with syndicate members willing to underwrite those risks.¹⁷⁹ Reinsurance can be purchased either directly from the reinsurer or via a broker. Lloyd's supplies c.80 per cent of all reinsurance.¹⁸⁰

Figure 39: Lloyd's market structure



Source: Lloyd's 2008

Lloyd's is currently in a phase of modernisation, having implemented IT systems to replace dated paper-based deals and support processes. This modernisation program is still in progress, with upgraded communications platforms currently being tested.¹⁸¹

Aside from Lloyd's, which dominates the wholesale and reinsurance markets, wholesale insurance can be purchased directly or through a broker. The most important brokers include Marsh Inc. and AON Corp., both US multinationals, and Willis Group, which is headquartered in London.¹⁸²

4.2.3 Regulation

Most types of insurance products are regulated by the FSA. Certain types of pensions are also regulated by the Pensions Regulator.

¹⁷⁹ Lloyd's of London, About Us

¹⁸⁰ Lloyd's of London, Association of British Insurers. Excludes non Association of British Insurers that are not Lloyd's

¹⁸¹ Lloyd's (2008) Annual Report 2008, pg 25

¹⁸² Business Insurance magazine, 20 July 2009 (see: http://www.marsh.sk/documents/MMC_Ranking2009_000.pdf)

Life and pensions products have been the subject of numerous claims of mis-selling, both historically¹⁸³ and more recently in November 2008, when the FSA fined AWD Chase de Vere Wealth Management £1.1m for “serious failings in its pension transfer, pension annuity and income withdrawal business that resulted in mis-selling”.¹⁸⁴ Misleading advice was the largest cause of complaints to the FSA about life and pensions products in the second half of 2008, with 34 per cent of complaints related to mis-selling.¹⁸⁵ Continued review is likely to lead to further regulations on pension advice and more stringent requirements for compliance and risk assessment, as well as a need to better train sales and advice staff to ensure companies do not inadvertently mis-sell products.¹⁸⁶

General insurance underwent regulatory reform in 2005, when the FSA took responsibility for general insurance regulation in order to meet the EU’s Insurance Mediation Directive.¹⁸⁷ This led to significant compliance requirements on insurers. However, the regime that came into effect as of January 2008 included the removal of more detailed rules for insurance products (motor, home, pet insurance), which are regarded as posing less risk to the consumer than some protection products (term assurance, critical illness, income protection). As a result of these changes, it was anticipated that regulation would become easier to navigate and impose a smaller compliance burden.¹⁸⁸

As of 31 December 2008, all firms operating in the insurance sector needed to demonstrate their adherence to the FSA’s Treating Customers Fairly initiative. The FSA had estimated that around 80 per cent of firms were capable of meeting the December 2008 deadline, although only 13 per cent had met its interim deadline.¹⁸⁹

We discuss the RDR and Solvency II – two major regulatory developments for insurers – in the “Foresight” chapter.

¹⁸³ FSA website (see: <http://www.fsa.gov.uk/Pages/Library/Communication/PR/2002/010.shtml>) The Pensions Advisory Service website (see: <http://www.pensionsadvisoryservice.org.uk/dealing-with-complaints/pension-mis-selling>)

¹⁸⁴ FSA website, 11 November 2008 (see: <http://www.fsa.gov.uk/pages/Library/Communication/PR/2008/129.shtml>)

¹⁸⁵ FSA website (see: http://www.fsa.gov.uk/Pages/Library/Other_publications/complaints_data/index.shtml)

¹⁸⁶ FSA website, February 2009 (see: http://www.addleshawgoddard.com/asset_store/document/pension_mis-selling_briefing_154319.pdf)

¹⁸⁷ Eur-Lex website (see: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32002L0092:EN:HTML>)

¹⁸⁸ Mintel (2008) General Insurance Overview UK

¹⁸⁹ Ibid

4.2.4 The current financial crisis

Overall the extent of losses felt by the insurance industry has been limited. Insurers have been exposed to the credit crisis through investments of their assets and through insurance coverage provisions. On the whole, insurance companies had relatively minor exposure to mortgage-related assets, are typically less leveraged than banks so were better placed to avoid liquidity difficulties.¹⁹⁰ Losses on insurance coverage has been limited to specific lines of business, such as mortgage guaranty claims; directors and officers claims; and errors and omissions claims.¹⁹¹

The immediate impact of the financial crisis was the slowdown in M&A activity as liquidity dried up. In the medium-term however, some restructuring could encourage a rise in deal activity, with potentially significant implications for employment. There has been much speculation around the future of insurance brands owned by RBS and Lloyds Banking Group. RBS sold its 50 per cent stake in Tesco Personal Finance for £950m and according to Mintel, it is keen to offload its insurance arm (including Churchill and Direct Line) to rebuild its banking capital capacity.¹⁹² After the merger with HBOS, Lloyds Banking Group became the ninth-largest general insurer.¹⁹³ In November 2009 the company announced it would cut 5,500 jobs at group level, including 1,190 insurance jobs, to help eliminate overlap resulting from the merger.¹⁹⁴

The recent fall in overall consumer demand may have further impacted the sale of discretionary insurance products such as accident and health, as well as the sale of insurance alongside big ticket purchases, such as consumer durables and travel. A deflated housing market will have reduced the demand for insurance products that are reliant upon mortgage issuance such as mortgage-related term assurance and endowments.

Conversely, increased job insecurity has already led to an increase in demand for unemployment insurance and pensions may also be positively affected as people begin to more actively engage in their financial retirement plans. Record company losses and rising unemployment may encourage people and companies alike to consider personal contract-based pensions as opposed to trust-based occupational pension schemes in the future. In times of economic uncertainty, consumers are more inclined to mitigate risk by purchasing insurance products.¹⁹⁵

¹⁹⁰ IFSL (2008) Insurance Update

¹⁹¹ Ibid.

¹⁹² Mintel (2008) General Insurance Overview UK

¹⁹³ Ibid

¹⁹⁴ <http://www.broking.co.uk/insurance-age/news/1564028/lloyds-cut-190-insurance-jobs-hbos-takeover>

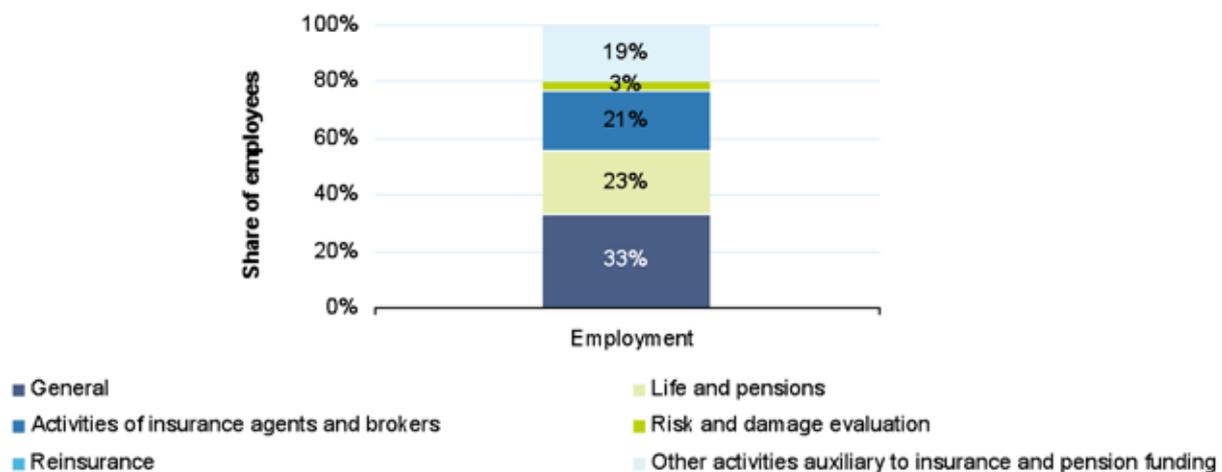
¹⁹⁵ Mintel focus group, September 2008

The London Market has also been impacted by the financial crisis. Lloyd’s suffered a 50 per cent decrease in pre-tax profits in 2008 due to the increase in attrition claims frequency, falling investment returns, the substantial markdown in equity values, as well as hurricanes Ike and Gustav. It is however possible that the recent financial turmoil will reap benefits for the reinsurance market and Lloyd’s, as illustrated by Lloyd’s performance in the first half of 2009.

4.3 Current employment

According to the Annual Business Inquiry (2007), c.317,000 people are employed in the insurance industry, including those who work indirectly for the industry.¹⁹⁶ 21 per cent of total insurance and pension employment is situated in London, with a further 10 per cent in Scotland.¹⁹⁷ 40,000 individuals are employed in the wholesale market in London, while a further 10,000 provide support for the sector in other parts of the UK.¹⁹⁸ Insurance employment by market segment is shown in Figure 40 (cross-segmented data with retail and wholesale is not available).

Figure 40: Insurance employment by market segment



Source: Annual Business Enquiry (2007)

4.4 Occupations

The insurance value chain is similar to that presented earlier for the entire financial services industry. The activities along it are shown in Figure 41.

¹⁹⁶ Annual Business Inquiry (2007)

¹⁹⁷ Annual Business Inquiry (2007)

¹⁹⁸ FSSC (2008) London Market Skills Review.

Figure 41: Activities along the insurance value chain

	Back office	Middle office	Front office
	<i>Non-core support functions</i>	<i>Non-customer facing core functions; monitoring and control functions</i>	<i>Customer-facing functions</i>
Example functions	<ul style="list-style-type: none"> • IT • Compliance • Human resources • Accounting • Record keeping and reporting • Clearance and settlement • Facilities management • Call centres 	<ul style="list-style-type: none"> • Service and product design • Position keeping – calculation of profit and loss • Risk management • Product control • Actuarial • Claims handling 	<ul style="list-style-type: none"> • Sales and marketing • Customer service • Underwriting • Broking

Source: PwC interviews & analysis

The back and middle-office segments of the value chain for both retail and wholesale typically involve risk and insurance analysis activities and claims handlers.

Retail insurance front-office job roles include insurance advisors and brokers, pension advisors and customer service and sales advisors who mostly deal with individuals and business customers. Wholesale insurance front-office job roles include underwriters, brokers, statisticians and analysts who deal with more sophisticated insurance customers. The London Market attracts a number of highly specialised service providers, such as claims and loss adjustors, actuaries, lawyers, accountants and consultants.¹⁹⁹

Given the relative difficulties disaggregating national data across the retail and wholesale value chain, we are unable to provide occupational breakdowns between retail and wholesale. A 2008 report into the wholesale insurance market in London provides projections of the demand for labour in the sector and we have used this data to estimate the occupational breakdown of the London wholesale insurance sector in 2008, as shown in Table 9.

Table 9: Employment in London's wholesale insurance sector by occupation, 2008

Occupation	Employment (2008)
Managers and senior officials	c.8,900
Professional	c.4,400
Associate professional and technical	c.8,300
Administrative, clerical and secretarial	c.13,500
Sales and customer service	c.4,900
TOTAL	c.40,000 ²⁰⁰

Source: Oxford Economics, Warwick Institute of Employment Research, FSSC analysis, PwC analysis

¹⁹⁹ FSSC (2008) London Market Skills Review.

²⁰⁰ Analysis excludes wholesale insurance employment outside London

4.5 Skills profile and provision

The skills and qualities needed in retail insurance include IT, numeracy, business communication and interpersonal skills. In addition to these skills, wholesale insurance employees require sound financial skills in relation to insurance contracts, excellent risk analysis skills and outstanding client relationship management skills. Understanding the London Market is important for positions in wholesale insurance.

The professional qualifications in retail and wholesale insurance often depend on employer's specific requirements, but quite often employees commence at the certificate level (equivalent to NQF level 3). If, however, an individual requires a lower level course or qualification (e.g. in retail insurance), it is possible to take the Foundation Insurance Test or the Award in Insurance first. The hierarchy of qualifications is as follows: entry level - Foundation Insurance Test; CII Award in Insurance; CII Certificate in Insurance; CII Diploma in Insurance; and CII Advanced Diploma in Insurance.

If a role in retail or wholesale insurance involves advising clients on life insurance, health insurance or pensions, an "Appropriate Exam"²⁰¹ is required, as giving financial advice is an FSA-regulated function. This means that in order to perform a function without supervision, specific professional qualifications are required. At the trainee level, an employer will often provide internal training and support the employee in gaining the qualification. Although there are no formal qualifications required to enter these roles and the associated training courses, good maths and English are considered essential. The minimum qualifications required to deliver advice include:

- CII Certificate in Financial Planning;
- CIOBS Certificate in Investment Planning; or
- IFS School of Finance CeFA.

Retail insurance

Entry into the retail insurance segment is usually through an administration role, and employees can progress with relevant experience and additional qualifications. Retail insurance roles require numeracy; good GCSEs or a diploma at Level 2 is thus a minimum requirement. Working as an insurance broker on general insurance products is not a regulated function, so an Appropriate Exam is not necessary. Once employed, retail insurance brokers generally aim to achieve industry-specific professional qualifications, choosing units of study that are relevant to the specific element of insurance in which they work.²⁰²

²⁰¹ List available at http://www.fssc.org.uk/appropriate_exam_list_15.html?i=1&l1=true

²⁰² FSSC website (see: http://www.fssc.org.uk/insurance_broking_retail.pdf)

“Skills are gained on the job rather than through qualifications.” National Association of Pension Funds

Apprenticeships in Providing Financial Services and Advising on Financial Products are also available.²⁰³

Wholesale insurance

In wholesale insurance, most employers now typically require new recruits to broking and underwriting to have a degree. Although often there is no subject requirement, degrees which have enabled candidates to demonstrate their communication and numerical abilities are welcomed.²⁰⁴

Underwriters working in the London Market also have to complete the Lloyd’s and London Market Introductory Test. This test tests basic knowledge of working in the London Market and covers the roles and working practices of brokers, Lloyd’s underwriters and insurance companies.²⁰⁵

In recognition of the need to recruit and train high-quality staff, Lloyd’s has implemented a number of initiatives both in-house and in cooperation with other employers, including the Graduate Programme and the Leadership Programme. The former is aimed at improving the quality of new recruits into Lloyd’s and other employers while the latter, run in conjunction with London Business School, seeks to develop future industry leaders. The Chartered Institute of Insurance has developed a number of initiatives to promote the skills agenda, including the Talent Initiative, which aims to improve university students’ knowledge of careers in the sector and entice high-quality entrants to the sector. The CII has also worked with apprenticeships providers and employers to bring together supply and demand and meet the needs of the profession.²⁰⁶

About one-third of the wholesale insurance workforce is qualified at or above degree level, a lower proportion than other financial service sectors in London. In wholesale insurance, many high value-added roles are occupied by experienced staff who have not historically had to pursue formal qualifications. The sector utilises a broad range of skills, both technical and general, that are not exclusively associated with academic study.²⁰⁷

4.6 Unfulfilled skills needs

The wholesale insurance workforce, particularly brokers, is ageing. Some small broking firms are composed almost entirely of staff with more than 20 years of experience in the London insurance market. As senior and experienced staff retire, replacing them will put pressure on the labour market.²⁰⁸

²⁰³ FSSC website (see: http://www.fssc.org.uk/317_14.html?i=4)

²⁰⁴ FSSC website (see: http://www.fssc.org.uk/insurance_broking_wholesale.pdf)

²⁰⁵ FSSC website (see: <http://www.fssc.org.uk/underwriting.pdf>)

²⁰⁶ CII (2009) Our view on: The Skills System in the UK

²⁰⁷ FSSC (2008) London Market Skills Review.

²⁰⁸ FSSC (2008) London Market Skills Review.

4.6.1 Skills shortages

Employers responding to the FSSC Employer Survey (2006) cited a lack of skilled or experienced applicants, including a shortage of specialist underwriters and compliance staff, as the most common obstacle to recruitment (65 per cent). This was followed by a lack of qualified applicants, such as accountants and internal auditors, and a lack of applicants in general. This is a concern for the future availability of skilled personnel as an increasing number of graduates and school leavers refuse to contemplate a career in the sector.²⁰⁹

At the moment, there is a very specific shortage of actuaries as demand for actuaries significantly exceeds supply.²¹⁰ Despite the recession, demand for actuaries continues to grow as insurance companies seek better means of managing and mitigating their risks. Some stakeholders expressed the view that the requirements of Solvency II (European regulation of insurers due to take effect in 2012) would exacerbate these shortages as it requires all insurance companies to have a risk management function and a chief actuarial officer.

Senior level operations staff, competent compliance, IT and legal staff, as well as risk management and claims professionals, are also in short supply.²¹¹

Table 10, drawn from the London Market Skills Review, provides an overview of the supply and demand of skills across the wholesale insurance value chain. It suggests that the supply of skills to the London Market is currently not keeping up with demand and, by automating underwriting processes, larger insurers could be eliminating a valuable source of new employees for both underwriting and broking positions.

Table 10: Roles in wholesale insurance – profiles and shortages

Roles	Skills at a premium: knowledge, ability, expertise, and personal attributes in demand			Demand: Cyclicity of demand for this role		
	Technical Skills	Other Skills	Experience	High	Medium	Low
Administrative staff						.
Brokers	ACII				.	
Statistician/Analyst		Strong IT Skills				.
Actuaries	Price reserving	Capital modelling				.
Underwriter	ACII, Lloyd's exam	Analytical	Relevant experience			.
Compliance						.
Risk						.
Claims Handler						.

Source: Hays Specialist Recruitment, Insurance and Financial Services, 2007

²⁰⁹ FSSC (2007) The Skills Bill: Analysis of skills needs in UK financial services.

²¹⁰ The Actuary website (see: <http://www.the-actuary.org.uk/694461>)

²¹¹ FSSC (2008) London Market Skills Review

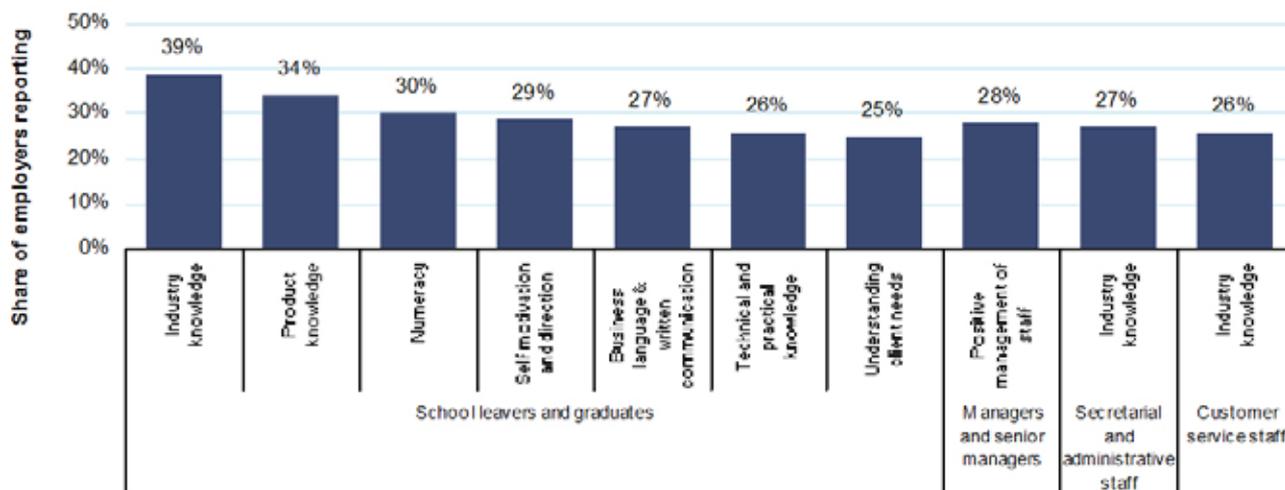
The FSSC suggests that these skills shortages are driven by the limited appeal and poor reputation of the industry. In research conducted by Lloyd’s, insurance is regularly ranked within the bottom few industry sectors in terms of reputation and 90 per cent of UK graduates say they would not consider insurance as a career²¹². The wholesale industry is also perceived to be dominated by white, middle-aged males, which is “driving away potentially valuable talent”.²¹³

Skills gaps

Skills gaps are not as widespread in insurance as they are in other financial services sectors, such as retail banking; nonetheless, employers report that skills are in need of improvement.

School leavers and graduates dominated the skills agenda for insurers in the FSSC Employer Survey (2006). Many participating employers stated that they lack basic industry knowledge, product knowledge, numeracy and a capacity for self-motivation and self-direction (Figure 42). Managers were found to be less than proficient at handling staff relationships, while industry knowledge was cited as a problem for administrative and customer service staff.

Figure 42: Top ten skills gaps in retail and wholesale insurance, by employee type



Source: FSSC (2007)

²¹² As cited in HM Treasury (2009) Vision for the insurance industry in 2020.

²¹³ FSSC (2008) London Market Skills Review

According to the London Market Skills Review (2008), employers in wholesale insurance have noted a lack of relationship management skills among senior staff. Table 11 highlights the most common types of skills gaps for each type of employee in the London Market.

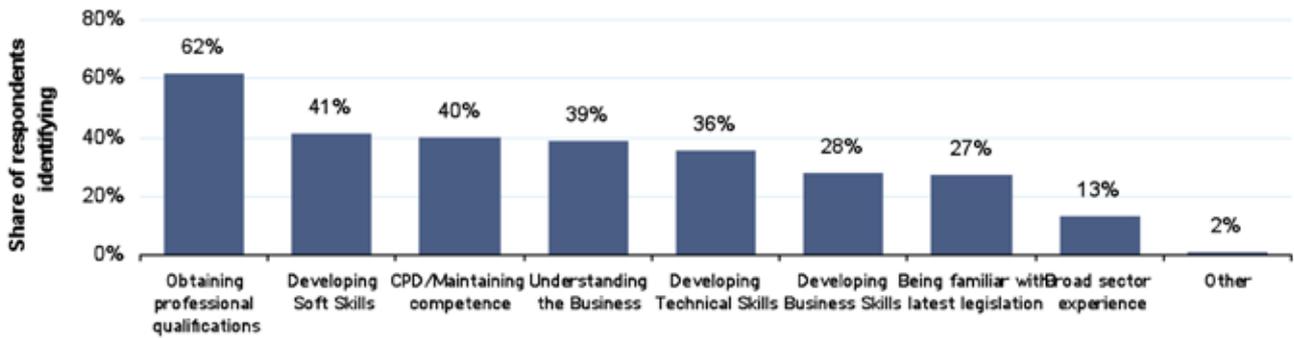
Table 11: Most common skills gaps in wholesale insurance by occupation

Managers & senior managers	Professional & technical	Administrative & secretarial
Positive management of staff relationships	Working effectively with others in a team	Industry knowledge
Coping with stress and pressure	Flexibility and co-operation	Self-motivation and direction
Project and people organisation	Industry knowledge	Ability to resolve issues/use initiative
Understanding client needs	Understanding client needs	Doing more than expected
Technical and practical knowledge	Ability to communicate clearly at various levels	Numeracy
Sales	Customer services	School leavers & graduates
Moving on from criticism and setbacks	Technical & practical knowledge	Technical & practical knowledge
Industry knowledge	Moving on from criticism and setbacks	Business language
Understanding client needs	Understanding client needs	Ability to resolve issues/use initiative
IT systems	Business language	Self-motivation and direction
Project and people organisation	Ability to communicate clearly at various levels	Understanding client needs

Note: Italicised text indicates the ten most cited skills gaps
Source: FSSC (2007)

The more recent CII Skills Group Survey (2009) found that obtaining professional qualifications, continuing professional development and developing soft skills were among the top three things that members felt were most important in skills training. CII members felt that developing business skills and broad sector experience were less important in skills training.

Figure 43: Skills identified as priorities for training in insurance



Note: Respondents were asked to identify what they thought to be the top three training priorities
Source: CII (2009)

The report found that 86 per cent of members felt that it is very important to get professional qualifications, while 64 per cent felt that the CII needed to broaden its range of training to reflect the increasing importance of soft skills.

5. Industry insight: Asset management

Chapter summary

The asset management sub-sector is the smallest within financial services, employing c.67,000 people. Asset management can also be segmented into retail and wholesale, with retail asset management servicing individuals and wholesale asset management looking after funds for institutions. Hedge funds and other alternative investment funds are a niche sector of wholesale asset management. Retail investors account for a small share of total assets funds and many products (e.g. mutual funds) are managed in the same way as products for wholesale customers.

The core asset management activity – including investment research, management of investment portfolios, trading and broker liaison – accounts for approximately a quarter of all employees. Marketing and distribution functions, including sales and business development, make up a further 21 per cent of employment. The remaining 54 per cent comprises middle- and back-office functions.

Asset management is a geographically concentrated segment, with 74 per cent of employment in London.

Front-office asset management roles are generally filled by individuals with graduate or post-graduate qualifications and employers expect entrants to be numerate and possess a good degree. Those looking for roles in asset management are required to have a strong quantitative reasoning ability to develop strong investment and risk analysis skills. Junior roles do not have to be registered with the Financial Services Authority (FSA). However, senior asset managers with responsibility for funds have to be registered with the FSA and pass appropriate exams.

There are skill shortages in the industry, with a shortfall of people with qualifications directly relevant to the sector's needs. A lack of experience and technical knowledge is the most common shortage. Back office and support functions are historically difficult to recruit for, as highly skilled applicants are put off by a lack of clear career paths and the impression that the roles are under-rewarded.

School leavers and graduates and administrative staff are the most likely to have skills gaps, while professionals and technical staff are less likely to lack skills. Industry and product knowledge was found to be lacking by 30 per cent of employers, while 28 per cent reported a lack of technical knowledge. It has been reported that even senior staff can lack an understanding of the investments that they manage. Soft skills such as relationship management also need to be developed at many companies.

5.1 Introduction

Asset management is the smallest of the three sectors we have reviewed within UK financial services. This chapter of our report describes the asset management market in the UK and the current state of employment and skills in the sector. It is structured as follows:

- Current state of the UK market;
- Current employment;
- Occupations;
- Skills profile and provision; and
- Unfulfilled skills needs.

5.2 Current state of the UK market

This section of the report considers the current state of the UK asset management market, in terms of its importance to the UK economy; market segmentation; and the regulation of asset management, particularly in the context of the current economic crisis.

5.2.1 Importance to the UK economy

Asset management accounted for 9 per cent of total financial services GVA (£9.6bn) in 2008.²¹⁴ The industry's revenues that year were c.1 per cent of GDP (c.£150bn), although funds under management were equivalent to 235 per cent of GDP.²¹⁵

The purpose of the asset management industry is to help clients achieve investment goals, which may vary widely in terms of ultimate investment objective and time horizon. The industry offers clients the ability to achieve a level of portfolio diversification and degree of access to a range of instruments and markets in a way and at a price that they could not achieve on their own. Money is managed for clients on both a pooled basis (i.e. co-mingled client assets in a collective vehicle) and segregated basis (managing client money in a distinct, separate account). A broader role fulfilled by the asset management sector is to act as a conduit for capital in the UK economy, by becoming a route through which those with capital to invest can distribute it to those with a need for investment.²¹⁶

²¹⁴ Office for National Statistics

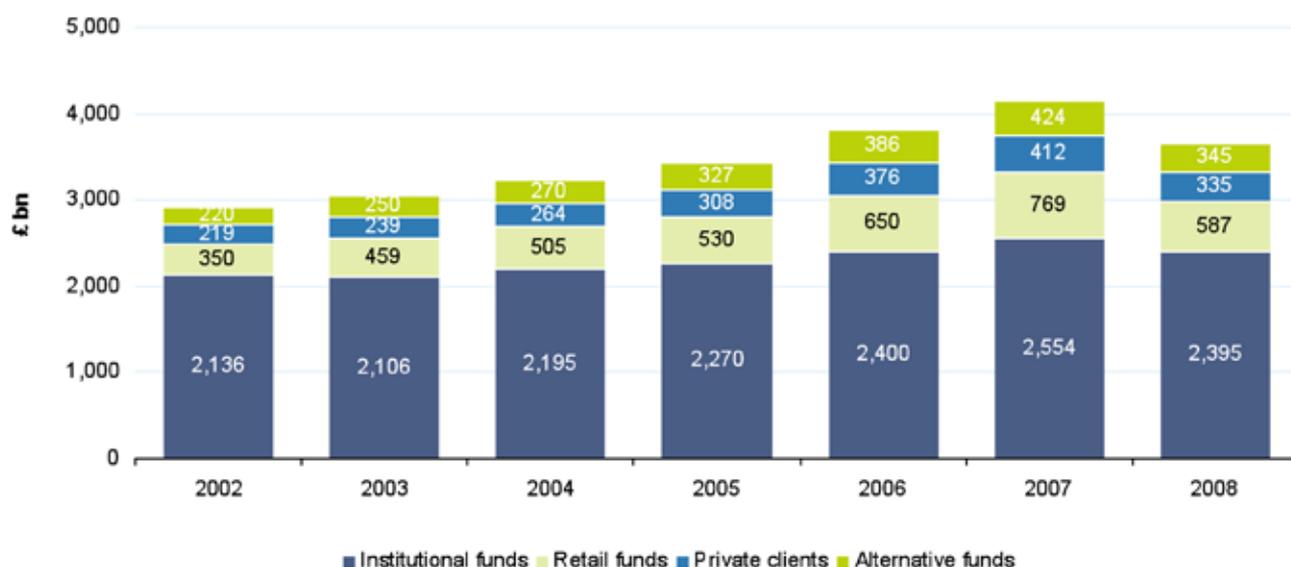
²¹⁵ HM Treasury (2009) Asset management: the UK as a global centre

²¹⁶ HM Treasury (2009) Asset management: the UK as a global centre

Figure 44 shows the total estimated funds under management in 2008 amounted to £3.7tr.²¹⁷ The majority of assets (65 per cent, £2.4tr) managed in the UK are held on behalf of institutional clients such as mutual funds, corporations, pension funds, insurance companies and smaller institutions such as charities, local authorities and sovereign funds. A significant portion (16 per cent, £587bn) is managed on behalf of individual investors who have assets in the form of exchange-traded fund (ETF) units, open-ended investment companies (OEIC) shares or individual savings accounts (ISA). The remaining 19 per cent of asset management funds are divided almost equally between high-net worth individuals and private clients (£335bn) and alternative funds (£345bn), which include hedge funds, real estate funds and private equity/venture capital.

The sector suffered a severe decline in funds under management in 2008, due to the financial crisis driving down the value of equities and assets.²¹⁸ The decline was felt across the entire industry, with all sectors experiencing contraction; however, institutional funds appeared to be more robust, with only a 6 per cent decline, compared to an average of 21 per cent across the other sectors.

Figure 44: Funds under management in the UK, 2002 – 2008



Source: IFSL (2009)

The UK is seen as having a competitive advantage over other countries as a destination for asset management. Key points which are specific to asset management include:

²¹⁷ FSL (2009) Fund management

²¹⁸ Charlie McCreevy, European Commissioner for Internal Market and Services European Asset Management, PwC European Asset Management Senior Executive Forum, November 2009

- an active and robust financial services industry with the necessary infrastructure for deals and trading. London-based asset managers had highly-sophisticated and innovative management styles, techniques and strategies. Prior to the financial crisis, the level of M&A activity was also high;
- a high level of liquidity;
- the skills, knowledge and experience to delivered tailored asset management strategies to clients; and
- strong individual asset management locations, each with different offerings and advantages. London (1st place), Jersey (7th), Guernsey (9th) and Edinburgh (15th) all featured highly on the GFCI 6 rankings of asset management locations.²¹⁹

5.2.2 Market segmentation

There are many different types of asset management products and channels, each catering to a separate niche of investor or financial goal. These can be broadly split into retail, targeted at individuals with assets to invest, including high net worth individuals, and wholesale, targeted at large corporate clients, financial services companies and public sector organisations.

Retail

Retail funds are offered to the general public and are subscribed to on an individual basis, usually through a distributor such as an IFA or bank. However, these will then be pooled into funds which are centrally managed. These funds tend to have a high turnover rate as individual investors typically subscribe to short-term (e.g. one-year) investments. As a result, they tend to adopt different strategies from institutional funds and structure themselves as companies with shareholdings to which each investor subscribes. Examples include:

- retail mutual funds, such as open-ended investment companies, which individuals invest into and have an established base capital which is invested. OEICs typically have stated investment objectives (such as high risk/high growth) to which individual investors are aligned. OEICs are typically owned by larger asset management entities; an
- exchange-traded funds are more liquid subscriptions which are sold and traded on stock exchange markets. These are similar to OEICs, except that the shares are easier to trade and thus can be used for short-term investments or for investors seeking less commitment.

²¹⁹ City of London (2009) The Global Financial Centres Index 6

Private asset management uniquely caters to high net worth individuals and provides a complete service offering that are client-driven and tailored to individual needs. Example services can include tax, retirement and inheritance planning; investment portfolio advice and management; trusts and estates; philanthropy arrangements; and even concierge services.

The ten largest retail fund managers in the UK managed £119.9bn of assets as of December 2008, representing 11.5 per cent of the retail and private client market (Table 12).

Table 12: Largest investment companies by total UK domiciled retail funds under management, December 2008

Rank	Company	£bn
1	Invesco Perpetual	£24.8
2	FIL Investment Management Limited	£15.4
3	Jupiter Unit Trust Managers Limited	£11.9
4	HBOS Investment Fund Managers Limited	£11.6
5	M & G Securities Limited	£11.4
6	SWIP Fund Management Ltd	£11.2
7	Threadneedle Investment Services Ltd	£9.9
8	Legal & General (Unit Trust) Managers Limited	£8.1
9	Capita Financial Managers Limited	£8.0
10	Schroder Investment Management Ltd	£7.6
	Other	£922.0
	Top 10 share of total	11.5%

Source: Investment Management Association (IMA) (2009)

Wholesale

Wholesale funds, also referred to as institutional funds, tend to be managed on behalf of large corporations, financial services companies, or public sector acquisitions. These typically include²²⁰:

- corporate funds. Companies with money to invest are almost exclusively liquidity-focused investors which use asset managers to help manage treasury efficiently. They look to grow their assets with minimal risk;
- insurance funds, which pool insurance premium income for insurance companies that is invested to generate growth and income;

²²⁰ PwC European Asset Management Conference, November 2009, HM Treasury (2009) Asset management: the UK as a global centre; IFSL (2009) Fund management

- pension funds. These include defined benefit and defined contribution schemes. Defined benefit schemes seek to match their assets with their liabilities. Defined contribution pension scheme funds are carefully managed according to the risk profile of subscribers, ranging from adventurous investors looking to maximise the growth of their pension to cautious investors looking to secure stable value. Most large companies have outsourced the management of their pension funds to dedicated fund managers²²¹; and
- funds of other institutions such as charities, local authorities or sovereign wealth funds. These are institutions that may find themselves with surplus assets which are not immediately required, such as charity endowments or a one-off income for local authorities. Countries that have surplus funds will often invest these funds to ensure long-term income generation to provide constant income over a long period of time. These will be invested into markets to achieve specific desired returns.

Alternative investment funds make up the remaining asset management sub-segments and include investment opportunities which tend to lie outside the mainstream. While small, this section of the industry is important as it attracts high levels of international interest and investment. These funds include:

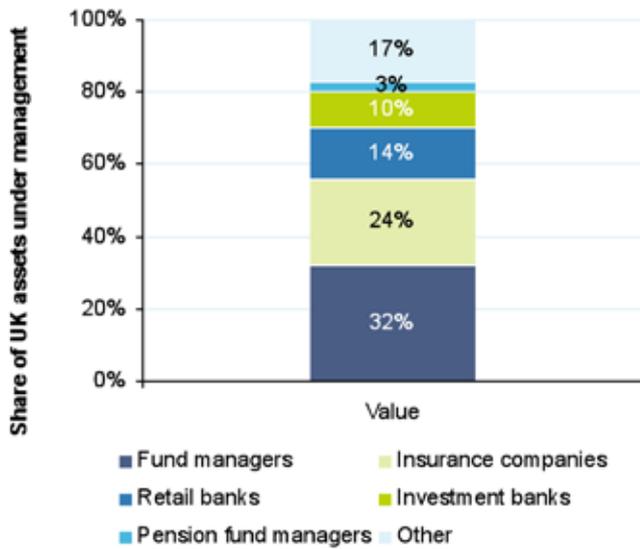
- hedge funds, which differentiate themselves from other investment funds by seeking to outperform the market by hedging against various investment positions. The funds use a wide range of alternative strategies and a combination of arbitrage, leverage and risk management to generate returns;
- real estate investment funds, which focus on property investment and pool investor's capital to purchase and manage property, either residential or commercial; and
- private equity and venture capital funds, which invest in companies and start-ups in which they see potential for growth.

Nearly a third (32 per cent) of assets in the UK are managed by dedicated fund managers investing on behalf of clients. About a quarter (24 per cent) are managed by insurance companies investing their premiums. Most of the remainder is managed by retail banks, investment banks and pension fund managers, as shown in Figure 45.²²²

²²¹ Economist Intelligence Unit (2009) Financial Services

²²² There is a possibility, due to the nature of the statistics, that some asset managers have also been counted into banking and insurance employment numbers as the IMA estimates employment levels differently to the Office for National Statistics

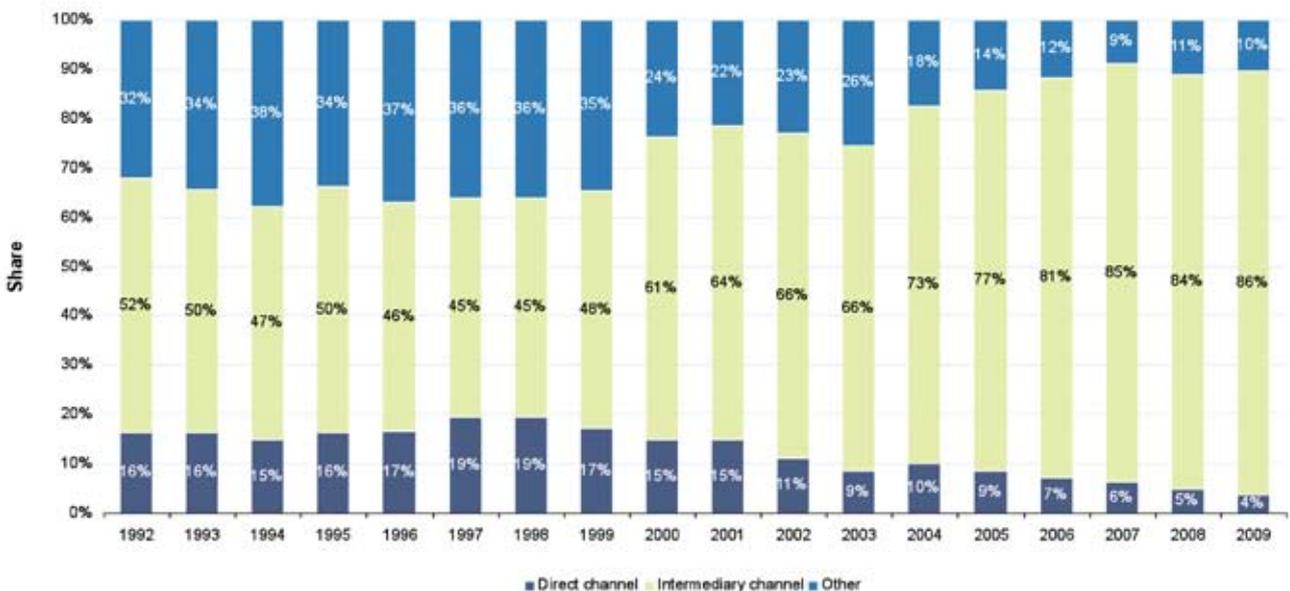
Figure 45: Percentage of UK funds managed by manager type, December 2008



Source: IFSL (2009)

Asset managers rely heavily on third parties such as IFAs to distribute their products. In the institutional pension fund market, clients tend to engage consultants to organise the commercial process and provide advice to trustees. As shown in Figure 46, intermediation is highly prevalent in the retail sector and direct sales have shown a marked decline.²²³

Figure 46: UK retail asset management sales channel trends, 1992 – 2009



Source: HM Treasury (2009)

²²³ HM Treasury (2009) Asset management: the UK as a global centre

5.2.3 Regulation

The asset management industry in the UK is regulated by the FSA. The FSA has recently implemented stronger liquidity standards, affecting all investment firms: asset managers will now be required to maintain stronger minimum capital to ensure that they are able to remain solvent in the event of external shocks.

“Fund management has historically been highly regulated and compliance is a very high cost for asset managers.” Investment Management Association (IMA)

Solvency II will also affect the asset management industry, given that a significant proportion of funds are either managed by captive fund managers within insurance companies or on behalf of insurers. Although the regulation is not likely to impact the value of assets under management, there could be some impact on the structure of investments. There is likely to be a greater focus on matching the risks of insurers’ assets and liabilities and counterparty risk of investments. This could result in tighter investment mandates and preference for investments such as more secure fixed-income products, rather than higher-risk equities.

The hedge fund industry benefited significantly from the 2001 European directive, Undertakings for Collective Investments in Transferable Securities (commonly known as UCITS) III, which allowed wider use of derivatives and leverage in retail funds. The industry is currently under review, with the draft Alternative Investment Fund Managers (AIFM) Directive moving through EC legislation.²²⁴ This directive is currently a subject of debate, with many alternative fund managers strongly opposed to its proposed measures. There is a possibility of the AIFM Directive having a significant effect on hedge funds in the UK, although this will not be confirmed until the directive is finalised. We discuss the AIFM in greater detail in the foresight section.

5.2.4 Impact of the financial crisis

The financial crisis has had a severe effect on asset management, with many funds losing large amounts of value in 2008. Total assets under management in the UK fell by 12 per cent.²²⁵ Alternative investments were particularly affected, with the UK hedge fund industry assets under management falling over 40 per cent in 2008.²²⁶ Although 2009 was a better year for stock markets, at the end of 2009, the FTSE 100 index was still at 2005 levels.²²⁷

²²⁴ Draft AIFM Directive proposal (see: http://ec.europa.eu/internal_market/investment/docs/alternative_investments/fund_managers_proposal_en.pdf)

²²⁵ IFSL (2009) Fund management

²²⁶ IFSL (2009) Hedge Funds

²²⁷ London Stock Exchange; Factiva

Despite widespread acceptance that activities within asset management were not contributing factors to the financial crisis, there are important reasons why regulators and politicians are ensuring that asset management regulations are tightened²²⁸:

- many regulators are reviewing the financial services industry’s ability to perform accurate diligence and valuation techniques on complex products and processes;
- there remain high levels of leverage within the sector, albeit isolated towards the alternative investment channels;
- counterparty risks (the risk that the other party in a deal may fail to meet their obligations) are being increasingly audited to assess the likelihood of default and investors are concerned about guarantees; and
- fraud remains a key concern, with recent high-profile examples such as the Madoff and Stanford frauds putting pressure on regulators to be more vigilant of the activities of investment managers.²²⁹

5.3 Current employment

According to the Annual Business Inquiry (2007), employment in the asset management industry in the UK is estimated to be c.67,000, accounting for 6 per cent of total financial services employment. London is the centre of the UK asset management industry, with 74 per cent of all employment in the sub sector.

5.4 Occupations

The asset management value chain is similar to that presented earlier for the entire financial services industry. The activities along it are shown in Figure 47.

Figure 47: Activities along the asset management value chain

	Back office	Middle office	Front office
	<i>Non-core support functions</i>	<i>Non-customer facing core functions; monitoring and control functions</i>	<i>Customer-facing functions</i>
Example functions	<ul style="list-style-type: none"> • IT • Compliance • Human resources • Accounting • Record keeping and reporting • Clearance and settlement • Facilities management 	<ul style="list-style-type: none"> • Service and product design • Position keeping – calculation of profit and loss • Risk management • Product control 	<ul style="list-style-type: none"> • Trading • Broking • Portfolio management • Sales and marketing

Source: PwC interviews & analysis

²²⁸ Charlie McCreedy, European Commissioner for Internal Market and Services European Asset Management, PwC European Asset Management Senior Executive Forum, November 2009

²²⁹ Reuters Hedgeworld News, ‘Madoff Documents Reveal Incredible, Unfocused SEC’; 02 November 2009; New York Times, ‘How Stanford Financial Dodged Regulators’, 20 June 2009.

Many asset management firms outsource a substantial amount of their activities, notably fund administration and accounting. Some assets are managed outside the UK and a number of firms domicile funds outside the UK and sell their products across Europe. Middle and back office employment is growing in other centres, particularly Dublin and Luxembourg.²³⁰ The Investment Management Association's Annual Survey (2009) provides some insight into the breakdown of asset management employment:

- middle and back-office functions account for the majority (54 per cent) of employment and include all support functions, such as transaction processing, settlement, custody and stock lending, IT support, investment accounting and compliance; and
- front office functions include core asset management (25 per cent of employment) and marketing and distribution (21 per cent of employment). Core asset management includes investment research, management of investment portfolios, buying/selling investments and pre-trade broker liaison. Marketing and distribution encompasses all activities relating to sales and business development.²³¹

Lower skilled middle-and and back-office functions may be outsourced:

“Much of the wider fund administration is outsourced, although not all funds pursue this route. ‘Supermarket’ platform retailers carry out a lot of the administration, distribution and record keeping of funds. Lower-skilled activities are offshored. This has historically been a major issue, with many jobs in the UK being moved abroad to remotely-controlled low-cost locations.” (AMA)

A breakdown of employment and occupations in each part of the value chain is shown in Table 13.

²³⁰ Investment Management Association (2009) Asset management in the UK 2008

²³¹ Oxera (2005) Future secure? Why asset managers locate in London.

Table 13: Distribution of asset management employment by activity

Value chain		Overall employment	Occupations
Core asset management	Fund management	c.16,800 (25%)	Fund management - strategic & operational c.11,400 (17%) Research/analysis c.4,000 (6%) Dealing c.1,300 (2%)
Marketing and distribution	Marketing, sales, business development and client services	c.14,100 (21%)	Marketing, sales, business development c.10,100 (15%) Client management c.4,000 (6%)
Middle and back office	Transaction processing	c.2,700 (4%)	Transaction processing, settlement c.2,000 (3%) Custody c.700 (1%)
	Fund accounting and administration	c.8,700 (13%)	Investment accounting, Performance measurement and client reporting c.4,700(7%) Other fund administration - including CIS administration c.4,000 (6%)
	Compliance, legal and audit	c.2,700 (4%)	Compliance c.1,300 (2%) Legal c.700 (1%) Audit c.700 (1%)
	Corporate finance and corporate administration	c.6,000 (9%)	Corporate finance c.2,700 (4%) HR and training c.1,300 (2%) Other administration c.2,000 (3%)
	IT systems	c.8,000 (12%)	-
	Other	c.8,000 (12%)	-
Total		c.67,000	

Note: Numbers may not reconcile due to rounding

Source: IMA (2009), Oxera (2005), PwC analysis

5.5 Skills profile and provision

Front-office asset management roles tend to require individuals with graduate or post-graduate qualifications. Employers require entrants to be numerate, but will typically accept graduates from any subject discipline, usually with at least a 2:1 degree. People entering front office asset management are required to have strong skills in investment and risk analysis, numerical reasoning and problem solving. Most people enter the front office in an investment analysis role. Junior employees in asset management are not required to be registered with the FSA, although employers often encourage and support employees in gaining professional qualifications relevant to the investment analysis role as they gain experience.²³² These qualifications include the CFA exam and the Certified International Investment Analyst designation.

Asset and fund management is a regulated function and therefore an Appropriate Exam²³³ is required if an individual is looking to carry out FSA regulated activity. Appropriate Exams include:

- CFA Society of the UK Investment Management Certificate;
- CISI Certificate in Investment Management; and
- CISI Diploma in Wealth Management.²³⁴

There are various levels of entry into back-office roles for people with different levels of qualifications, but many companies look for staff with A Levels or a degree. Whatever the level of qualification, back-office roles require people to have excellent communications skills and a good level of numeracy.

²³² FSSC website (see: http://www.fssc.org.uk/investment_analysis.pdf)

²³³ For some jobs within financial services a specific qualification is required before you are allowed to do the job unsupervised. These qualifications are called 'Appropriate Exams'.

²³⁴ FSSC website (see: http://www.fssc.org.uk/asset_mangement.pdf)

5.6 Unfulfilled skills needs

Asset management is another sector recording fewer skills deficits than the wider financial services industry. Skills levels are buoyed by access to global talent pools as well as stringent performance measures and controls. Competitive remuneration makes it an attractive sector and employees tend to be highly committed to their own personal development.²³⁵

Despite the fewer skills deficits reported by the sector, almost three-quarters (74 per cent) of all employers surveyed in the FSSC Employer Survey (2006) still reported some difficulty with recruiting and 64 per cent reported a shortage of skills.

5.6.1 Skills shortages

Skills shortages among professionals and technical staff – for instance, of specialist quantitative valuations skills – are at the top of the sector’s skills agenda and there is a shortage of people with qualifications directly relevant to the sector’s needs. In the FSSC’s 2006 Employer Survey, experience and technical knowledge was cited as more of an issue in this sector than in many others – even for new entrants. This is because employers find that professionals with experience of the full range of cyclical conditions or a profound understanding of multiple markets have a distinct advantage.²³⁶ There is also increasing demand for specific knowledge in company or other asset valuation, especially in the wake of the financial crisis, as asset managers seek to quantify more accurate precise values of assets and investments.

“There is a skill demand, particularly for valuation abilities. The ability to value illiquid, derivative or hard-to-value assets is becoming increasingly valuable.” PwC financial services team

It is more challenging to recruit into back-office and compliance roles. Attendees at the FSSC employer forum noted that beyond the highly-rewarded front-office roles, there is a definite skills shortage in the industry and skilled applicants for back office are scarce. Employers also reported that the lack of clear career paths between the different levels of occupations puts many people off back-office roles, believing they risk a poor return on their skills.²³⁷

Respondents to the FSSC Employer Survey (2006) reported that they ‘struggle to manage expectations’ among new recruits, who often come into administrative or technical roles with unrealistic aspirations of rapid personal development, even though they lack significant industry, product and practical knowledge.

²³⁵ FSSC (2007) The Skills Bill: Analysis of skills needs in UK financial services.

²³⁶ FSSC (2007) The Skills Bill: Analysis of skills needs in UK financial services.

²³⁷ FSSC (2007) The Skills Bill: Analysis of skills needs in UK financial services.

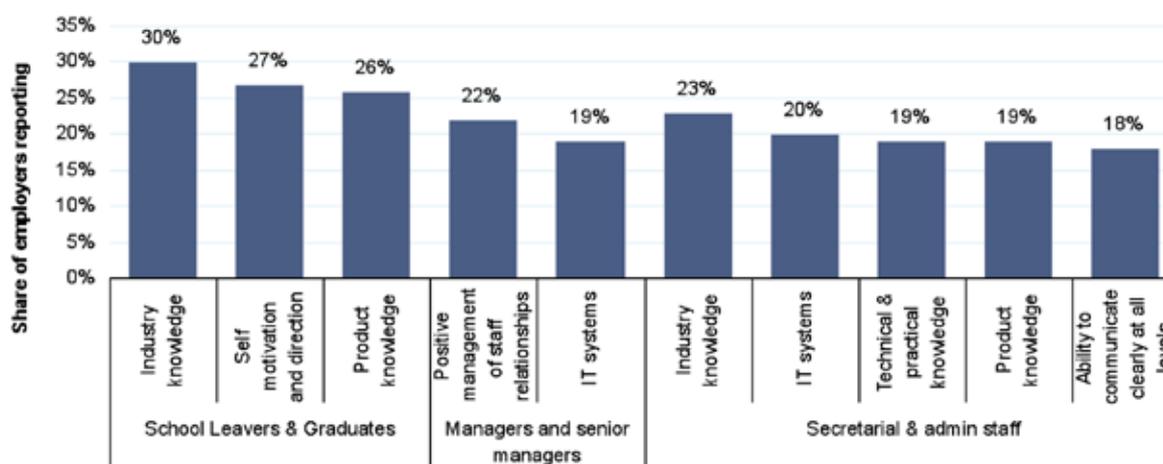
5.6.2 Skills gaps

Two thirds of sector employers (66 per cent) reported that employees' skills were in need of improvement. Skills in need of improvement were mostly of a sector-specific nature.

Most of the skills gaps identified in the FSSC Employer Survey concerned school leavers & graduates and secretarial & administrative staff, while professionals and technical staff were less likely to be reported as lacking skills. More than two out of five of the establishments surveyed said industry knowledge, as well as technical and practical knowledge, needed improvement among staff members. Gaps were also noted in softer areas such as self motivation and direction, staff relationships, project management and people organisation.

"Many asset managers have come from other sectors and lack deep technical skills. Many have come from custodial or valuations backgrounds." FSA

Figure 48: Top 10 skills gaps in asset management, by employee type



Source: FSSC (2007)

There is evidence that in light of the credit crisis, some aspects of fund management require urgent attention. A KPMG survey in 2008 found that the skills of staff have to some degree failed to keep up with growing sophistication in the industry. One in five fund managers that have invested in complex financial instruments, such as derivatives or structured products, admit to having no in-house specialists with relevant experience.²³⁸

For example, the Institute for Public Policy Research recently published research urging the government to take action to make the UK workforce 'climate ready'. The research explains that businesses will need a basic understanding of their contribution to climate change and in particular, investment fund managers will need to understand the impact that climate change schemes like the European Emissions Trading Scheme will have on the companies in their portfolios.²³⁹

²³⁸ KPMG (2008) Beyond the credit crisis: the impact and lessons learnt for investment managers.

²³⁹ Institute for Public Policy Research website, 2 November, 2009 (see: <http://www.ippr.org.uk/pressreleases/?id=3769>)

6. Industry foresight

Chapter summary

There are six primary drivers of future output for the financial services sector:

- regulation;
- globalisation;
- consumer demand;
- demographics;
- environmental change; and
- technology.

Regulation will be one of the most important factors in determining the future of the UK's financial services sector. Poor regulation and excessive risk taking are now seen as major contributors to the financial crisis. The Turner Review proposes stronger regulation, including stricter capital adequacy, risk management and governance, and remuneration policies. Tight regulation which is more onerous than elsewhere could have the effect of reducing overall employment. Whatever the extent of increased regulation, there will be a greater need for accountants, actuaries and other professionals capable of assessing and monitoring financial risk.

The increasing importance of emerging economies is expected to be a fundamental driver of change in UK financial services, particularly wholesale banking activities. Growth in emerging markets may, in the long-term, lead to London's leading position as a centre of international finance being challenged by Shanghai, Hong Kong, Singapore and other financial centres, with a potential reduction of certain roles in London. London, however, has many fundamental advantages in terms of a sound legal system, and an infrastructure of professional and legal services, that will help it to maintain a strong position in the next decade.

Consumer demand and attitudes will play a major role in retail banking. Whether consumers will recover their appetite for risk and for credit in the form of personal loans, mortgages and credit cards – or whether we are entering a decade of greater caution, with consumers increasing savings – will impact the level and nature of demand. Employees will require skills in new product development as well as analytical skills to quantify demand and price new savings products. They may also need stronger customer relationship skills to sell products to more sceptical consumers.

The demographics of the consumer base (and in particular, an ageing population) will similarly impact upon demand for different types of products (such as pensions, life assurance, or health insurance) which in turn brings with it the need to understand customer risk and the appropriate pricing model. It will also change the nature of the labour pool from which financial services draws – workers will be older and there will be a greater reliance on immigrant workers.

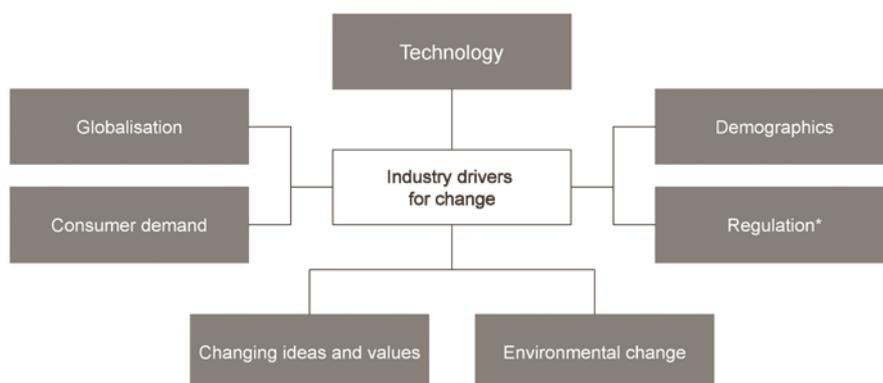
As with other sectors of the economy, environmental change will increasingly impact financial services. Examples include a greater need for accurate pricing of climate change-related risk, financing for renewable energy projects and carbon emissions trading. All of these activities require specific knowledge and additional skills.

6.1 Introduction

This section of our report presents our analysis of the key drivers for change in the financial services industry in the UK over the next 10 years and the likely implications for employment and skills.

In the context of the wider National Strategic Skills Audit work, a number of key industry drivers for change have been identified. These drivers, which are illustrated in the diagram below, have formed a framework for the basis of not just this study, but also the other UK Commission projects contributing to the Audit.

Figure 49: Drivers of change



Source: PwC analysis

Note: Broadly defined in the Audit as Multi level Governance and Regulation

This framework provides a useful means of comparing and contrasting the main drivers across different sectors to reflect the nature of the industry under scrutiny. For financial services, our research suggests that almost all of the drivers will be important, but that regulation, consumer demand and globalisation will be the drivers that will have most influence on the shape of the sector in the decade to 2020.

For each driver, we have identified the main aspects and discussed separately their impact on retail and wholesale financial services, and the implications for employment and skills. These implications are reflected in our scenarios in the next chapter, which are separated between retail and wholesale financial services. Table 14 summarises the impact of each driver on each segment.

Table 14: Summary impact of drivers

	Description	Implications for retail employment/skills	Implications for wholesale employment/skills
Regulation	More stringent risk management and transparency requirements Taxation and limits on remuneration RDR and Thoresen review impacting relationships with customers	Need for greater understanding of risk and compliance across organisations Reduction in number of IFAs, some of whom may work for insurers directly Increased demand for financial advisers for a free advice service	Need for greater understanding of risk and compliance across organisations Difficulties attracting and retaining internationally mobile employees Possible shrinking of some segments of the industry
Globalisation	More offshoring of back-office functions Growing importance of emerging economies Increasing job mobility	Lower demand for back-office roles which can be offshored	Lower demand for back-office roles which can be offshored Migration of jobs and employees to emerging economies Higher demand for language and cultural skills to deal with overseas clients
Consumer demand	More cautious consumers with demand for greater transparency and security Demand for more individualised products Demand for new types of products, such as ethical finance products and Islamic finance products	Improved understanding of financial products and associated risks, and ability to explain them to consumers Marketing and product development skills Better understanding of ethical finance, Islamic finance and other new product types	Better understanding of ethical finance, Islamic finance and other new product types Improved understanding of financial products and associated risks, and ability to explain them to clients
Demographics	Greater demand from the ageing and longer-living population for savings products to save for retirement Ageing of financial services workforce Migrants comprising a greater share of customer base and labour pool	Financial advice skills needed to deal with increased demand for retirement savings products Need to invest in skills of older workers Foreign language skills to deal with migrants Reliance on immigrant labour	Continued reliance on highly-skilled immigrant workers Cultural and language skills to identify opportunities in “younger” economies
Environment	More climate-related products, such as emissions trading, renewable energy project financing and insurance of climate-related risks	Understanding of climate risks and ability to model them Withdrawal of coverage could negatively impact some employment Increased need for experts in risk assessment and damage evaluation	Skills broadly the same, but understanding of climate change and associated products
Technology	New product innovation Greater automation More outsourcing Increased need for security	Need for greater IT understanding among all employees Increased need for specialist security skills Lower demand for low-skilled front-office roles Lower-demand for back-office roles which can be automated	Need for greater IT understanding among all employees Increased need for specialist security skills Increased need for specialists to develop systems capable of tracking complex derivatives Lower-demand for back-office roles which can be automated

Source: PwC analysis

6.2 Regulation

Regulation will be one of the most important factors in determining the future of the UK's financial services industry. Relatively light-touch regulation in recent years enabled the industry to innovate and grow at a fast pace, but proved inadequate in the financial crisis. However, increased regulation in the UK – which many consider inevitable – could arguably stifle the future potential of the UK's financial services sector.

“As we build this new global financial system, it is vital that we remain a world-class financial centre. It won't happen with a laissez-faire, hands-off, do-what-you-like approach any more than it would if governments try to micromanage the financial sector.” Alistair Darling, Chancellor of the Exchequer²⁴⁰

“There is no support in this country, and no case, for excessively bureaucratic regulation.” Mervyn King, Governor of the Bank of England²⁴¹

The main aspects of regulation impacting the retail sector are likely to be risk management rules and rules relating to consumer distribution. The wholesale sector will also be impacted by risk management regulations, as well as remuneration and taxation policies.

6.2.1 Retail

Risk management and transparency

Regulations relating to risk management and transparency are likely to impact all areas of financial services, but banking in particular. Poor regulation and excessive risk-taking is now seen as a major contributor to the banking market failure.²⁴⁰ In retail banking, risk-taking included extending mortgages to un-creditworthy borrowers, offering mortgages without confirming borrowers' ability to pay for them, and offering products such as 125 per cent mortgages which implicitly assumed that house prices would continue to rise.

Strong regulation has been proposed in the Turner Review which advocates stricter capital adequacy, risk management and governance, and remuneration policies.²⁴³ All banks will be significantly impacted as they will be required to hold increased amounts of capital to cover their liabilities. The FSA has already begun implementing some of these proposals, such as a ban on self-certified mortgages.²⁴⁴

²⁴⁰ Speech by the Chancellor of the Exchequer, the Rt Hon Alistair Darling MP, at the CBI Scotland Annual Dinner, Glasgow, 3 September 2009 (see: http://www.hm-treasury.gov.uk/press_78_09.htm)

²⁴¹ Speech by Mervyn King, Governor of the Bank of England at the Lord Mayor's Banquet for Bankers and Merchants of the City of London at the Mansion House, 17 June 2009 (see: <http://www.bankofengland.co.uk/publications/speeches/2009/speech394.pdf>)

²⁴² PwC The Day After Tomorrow Series (available at: <http://www.pwc.com/gx/en/financial-services/day-after-tomorrow/index.jhtml>)

²⁴³ FSA (2009) The Turner Review: A regulatory response to the global banking crisis.

²⁴⁴ HM Treasury (2009) Reforming financial markets

The government has advocated improved governance as a key strategy in ensuring that there is no repeat of the events that led up to the crisis. A recent HM Treasury report stated that improved risk management at board level, changes to the balance of skills, experience and independence, and a better approach to audit, risk and remuneration are required.²⁴⁵

Whatever the extent of increased regulation, there will be need for a greater awareness of compliance and risk among financial services staff across financial services organisations.²⁴⁶ There will also be a greater need for accountants, actuaries, credit officers and other staff capable of assessing and monitoring financial risk. Strong risk awareness instead of short-term profit maximisation has become a major focus and retraining in assessing investment risks from a long-term perspective will be required.

Insurers face significant regulatory changes in the medium term as Solvency II²⁴⁷ comes into force. Solvency II will impose stricter capital adequacy, enhanced risk management procedures and more transparent reporting requirements upon insurers, similar to the way Basel II regulation has impacted banks.²⁴⁸ This will drive a change to insurer strategy, as financial stability becomes a higher priority and profitability is reduced. Risk management and compliance will be the key areas of focus.

“Solvency II will force product and business management to change, with transparency and compliance skills the likely focus.” PwC financial services team

In response to Solvency II, many insurers have already established or expanded their governance and compliance functions to ensure that they are adequately prepared for the regulatory changes that are due to come into force in October 2012. There may be some changes to Solvency II before then as the industry lobbies for relaxation of “excessive conservatism”.²⁴⁹ However, the reverse may also be true if further systemic shocks occur or if major disasters occur and regulators will seek to ensure that insurers are adequately capitalised.

Solvency II could result in increased demand for staff similar to that resulting from the Sarbanes-Oxley Act of 2002 (US legislation affecting corporate governance).²⁵⁰ Solvency II will require every insurance firm to have an internal audit function and an actuarial function. For employers, this means that thought must be given to the required skills and experience necessary to achieve implementation which will create an increasing demand for actuaries, accountants, modellers and analysts. For example, Aviva has recently created the role of “Chief Actuary for Europe”, reporting directly to the chief financial officer for Europe.²⁵¹

²⁴⁵ HM Treasury (2009) Reforming financial markets

²⁴⁶ National Guidance Research Forum (NGRF), 2008

²⁴⁷ FSA website (see: <http://www.fsa.gov.uk/pages/About/What/International/solvency/index.shtml>)

²⁴⁸ FSA website (see: <http://www.fsa.gov.uk/pages/About/What/International/solvency/index.shtml>); FSA website (see: <http://www.fsa.gov.uk/Pages/About/What/International/basel/index.shtml>)

²⁴⁹ Financial Times website, 30 October 2009 (see: http://www.ft.com/cms/s/0/51852a0a-c57c-11de-9b3b-00144feab49a.html?nclick_check=1)

²⁵⁰ Blueport website (see: <http://www.blueport.co.uk/resources-news-item.php?id=21>)

²⁵¹ Aviva website, 23 June 2009 (see: <http://www.aviva.com/media/news/5000>)

“Following Solvency II, there will be a much higher need for financial modellers to run risk models and manage business lines; risk management consultants to mitigate risks, navigate compliance (e.g. “chief risk officer”); and actuaries to undertake underwriting and insurance sales in the new environment” PwC financial services team

Consumer advice & distribution

The RDR, launched by the FSA in 2006 and published in 2009, is likely to have a significant impact on the way financial products are distributed to consumers. The principal relevant recommendations of the review were that:

- financial services companies serving the retail market should no longer be able to pay commissions to IFAs to sell their products, with the aim of increasing the objectivity of financial advice. Instead, consumers should pay for IFA advice that they receive. This may encourage IFAs to target high net worth individuals as these are the types of consumers most likely to be able to afford IFA advice; and
- that IFAs should be qualified to at least QCF Level 4, to help ensure the advice consumers receive is sound.

If implemented, the recommendations are likely to have a particular impact on the insurance sector and, to a lesser extent, the asset management industry, which uses the IFA channel to sell products to retail customers. There are significant implications for employment: the proposal to raise professional standards in the RDR may cause some advisers, in particular older ones, to leave the market by retiring early, rather than studying to attain QCF Level 4. Consumer demand for IFAs is also likely to decline as their services are no longer free. Ernst & Young forecasts that the number of IFAs will fall by c.10,000 by 2013.

“As a result of the RDR, between four and twenty per cent of investment advisors will leave the industry.” RDR team manager, FSA

For the IFAs that remain, their skill set will need to change: as products are no longer sold on commission, product knowledge and advisory skills will become even more critical.

“The proposed RDR changes will likely result in many IFAs having to gain CII Level 4 qualification. Most IFAs will already have this qualification and those who do not will have to play catch-up.” AMA

Insurance companies and asset managers will need to market directly to their customers²⁵² and their demand may be met in part by former IFAs.²⁵³

The Thoresen Review of Generic Financial Advice, commissioned by the Treasury and published in 2008, is also likely to significantly impact distribution of financial products. There is a consensus in the literature and among industry stakeholders that participated in this study that financial education amongst the general public is lacking, which contributed to some of the causes of the financial crisis.

“The general financial education levels of the UK public will have to increase. There is a knowledge gap which has to close. The internet and the widespread availability of information (e.g. comparison websites) has helped in some retail products, but more needs to be done.” International Financial Services, London (IFSL)

The review recommends establishing a free generic financial advice service targeted at less affluent customers which would impact the need for appropriate skills.²⁵⁴ Indeed, demand for such a service could be expected to increase if IFAs begin charging for advice.

If the recommendations of the Thoresen Review are adopted, there will be strong demand for financial advice skills. As the level of advice is likely to be basic, the main qualifications for financial advisers will be numeracy and an understanding of the principal product types. These roles are unlikely to be filled by former IFAs.²⁵⁵

6.2.2 Wholesale

Regulation which impairs the ability of financial institutions to generate profit – particularly if the UK adopts more stringent regulation than other jurisdictions – have the potential to reduce overall employment in financial services, and this is particularly true in wholesale financial services. However, this depends on the extent of regulation and regulation certainly does create demands for certain types of employment and skills, as discussed in the retail section.

²⁵² PwC Interviews

²⁵³ Ernst & Young (2009) In shifting sands: UK life and pensions outlook.

²⁵⁴ HM Treasury (2009) Thoresen Review of Generic Financial Advice

²⁵⁵ National Guidance Research Forum (NGRF), 2008

Risk management and transparency

Regulations relating to risk management and transparency are likely to particularly impact wholesale banking. There have been proposals to limit the wholesale activities of retail banks and the proprietary trading functions of investment banks, as well as increase the capital requirements of banks. All of these restrictions could limit banks' profitability.

"Investment banking is likely to become a target of regulators and governments, particularly with the goal of reducing profitability." PwC financial services team

Across the wholesale industry, there will be increased demand for valuations abilities. The ability to value illiquid, derivative or hard-to-value assets will be very sought-after. There will be a stronger emphasis on due diligence prior to initial acquisition. This initial due diligence is also likely to remain ongoing as long as the asset remains in the portfolio of the fund.

"There is an intrinsic need to assess and analyse risks and the nature of products. However, this should not be the traders' job - there would be a conflict of interest in this case. It is down to RM and senior management to address risk and compliance." Director, Henley Business School, ICMA

Asset management is likely to be less affected by risk management regulations. There is a consensus that while regulatory changes will come to the asset management industry, these are likely to be procedural in nature rather than systemic upheavals. The result is that asset managers may have to adapt to new rules, but these will not be any more rigorous or difficult to comply with than previously.²⁵⁶

"Regulatory issues are not as applicable to asset management as it is to banking. It is an issue, but not as influential as in banking. Fund management has historically been highly regulated and compliance is a very high cost for asset managers. Business is unlikely to suffer due to regulatory burdens. Regulatory changes from Europe may occur, but this is likely to be merely changes, rather than tougher or increased regulation." AMA

However, there is a fear of increasing bureaucracy and trading restrictions due to local and European regulations.²⁵⁷ The AIFM Directive could significantly impact Europe's hedge fund industry, 80 per cent of which is based in London.²⁵⁸ The directive's proposals include debt restrictions and restricting the ability to market to EU investors to European-domiciled firms. Critics believe it will reduce choice for investors and deter investors from overseas. According to the British Venture Capital Association's chief executive, the directive could cut off the flow of private equity investment from outside the EU – the source of more than half the private equity capital in the UK.²⁵⁹

The directive has faced considerable opposition from the industry and the final form of the legislation remains undetermined.

²⁵⁶ PwC Interviews

²⁵⁷ IMA (2009) Asset Management Survey

²⁵⁸ <http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/privateequity/7079978/EU-hedge-fund-directive-hit-by-record-amendments.html>

²⁵⁹ http://uk.sitestat.com/pwc/uk/s?ukws_eng_publications.pdf.20_20_vision.2020_vision_future_of_financial_services&ns_type=pdf

“We understand that well over a thousand amendments have been tabled by MEPs – this is unprecedented in EU financial services regulation, and shows clearly that there’s a long way to go to get the directive into an acceptable shape, which will protect rather than damage Europe’s economies and competitiveness.” Secretary general of the European Venture Capital Association²⁶⁰

The FSA is also expanding its client assets (CASS) assessments and will become more proactive in ensuring compliance, with ARROW, audit and CASS reviews all likely to increase.²⁶¹ For captive asset managers, there is the risk that Solvency II regulations will be applied to asset managers as well, while fund managers investing insurance assets will find they have a limited pool of assets to invest.

Some fund managers have already left London for more attractive jurisdictions with lighter regulation.

“Historically, many fund managers have already left London for destinations such as Dublin and Luxemburg. They have not returned yet, despite crackdowns (e.g. by Obama) on certain financial centres” IMA

Remuneration and taxation

The remuneration of bankers and investment managers has become an important political issue in the context of the 2008-09 economic crisis. Considerable criticism has been expressed about the level of remuneration in the UK’s largest banks, particularly with regard to the payment of large bonuses.²⁶² The ‘bonus culture’ in the City of London, particularly amongst those involved in trading activities in investment banks, contributed to excessive risk-taking and short-termism and thereby played a contributory role in the banking crisis.²⁶³ Lord Turner has recommended that remuneration policies for top executives and traders should be designed to avoid incentives for undue risk-taking; and that risk management considerations should be closely integrated into remuneration decisions. New FSA rules stipulate that bankers earning more than £1m must take 60 per cent of their bonus in deferred shares, thereby linking remuneration to banks’ long-term performance.²⁶⁴

Taxation is another of the government’s main levers over the financial services industry and is a significant determinant of the UK’s attractiveness as a commercial jurisdiction. It impacts on all sectors of financial services and the wholesale market in particular, as its international client base (and often talent pool) makes it more mobile.

²⁶⁰ <http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/privateequity/7079978/EU-hedge-fund-directive-hit-by-record-amendments.html>

²⁶¹ CASS assessments are used to evaluate the adequateness of measures used by firms to protect their clients’ assets; ARROW (Advanced Risk Response Operating frameWork) is used by the FSA to appraise the risk profiles of firms and their ability to handle systemic shocks

²⁶² House of Commons (2009) Executive remuneration in UK banking.

²⁶³ Loughborough University (2009) The reform of UK regulation.

²⁶⁴ http://business.timesonline.co.uk/tol/business/industry_sectors/banking_and_finance/article7002329.ece

Seven in ten (71 per cent) of respondents in the Association of British Insurers' UK Competitiveness Survey (2009) stated that the current tax system is either very uncompetitive or fairly uncompetitive.²⁶⁵ However, the current state of public finances means it may be difficult for any government to lower taxes to make the UK a more attractive domicile for financial services companies.

As of the 2010/2011 tax year, the marginal rate of income tax for those earning over £150,000 p.a. will rise from 40 per cent to 50 per cent. A one-off 50 per cent levy on all bonuses of more than £25,000 has also been introduced (although many banks have absorbed this cost on behalf of their staff).

Changes to the tax regime could particularly impact the wholesale banking and asset management industries, due to the relatively high compensation in these sectors.

"The 50 per cent tax band will be very damaging to the UK, with many companies and executives moving as a result, and potential new entrants discouraged from relocation." IFSL

"Two senior bankers attending the World Economic Forum said yesterday that a substantial number of employees had asked to leave London. Some employees, particularly Americans who have been working in their London offices, are asking to go home. Others are apparently being seduced by the low taxes and high standard of living in Switzerland." The Times, 29 January 2010

Remuneration and taxation regulations could cause wholesale banks and asset managers to struggle to attract and retain talented staff, while many highly mobile top-earners would consider moving abroad to less constricting environments.²⁶⁶ This could negatively impact overall employment in the sector.

"People see that the government is now taking more than half of any extra income they earn. We've seen a number of our people asking can they work in other countries – and of course they could. Financial services companies and the people who work in them are very mobile – and I worry that Britain is going from being pretty competitive on a global scale to being pretty uncompetitive." Barry Bateman, Vice Chairman, Fidelity International²⁶⁷

There is also a possibility that remuneration regulations will make retention an issue for banks whose employees do not want to leave the UK.

"Retention will be more important than recruitment. If the economy begins to turn around and jobs become more readily available, many workers at banks who have suffered or been treated badly by their employer will seek to leave." PwC financial services team

²⁶⁵ UK Competitiveness Survey, September 2009 (see: http://www.abi.org.uk/Facts_and_Figures/43860.pdf)

²⁶⁶ As cited in HM Treasury (2009) Reforming Financial Markets

²⁶⁷ http://uk.sitestat.com/pwc/uk/s?ukws_eng_publications.pdf.20_20_vision.2020_vision_future_of_financial_services&ns_type=pdf

Corporate tax has already promoted many investment managers domicile outside the UK. Several hedge funds have relocated to more tax-efficient havens.²⁶⁸ Stamp duty at 0.5 per cent remains a barrier to growth with many investors preferring to invest into a fund that is domiciled in a jurisdiction without such a high penalty on transfers.²⁶⁹

There has also been discussion of a tax on banking transactions to safeguard the public purse in the event of a future financial crisis. However, such a tax would need to be adopted internationally and would have less of an impact on the UK's relative competitiveness as a jurisdiction. If adopted, it could still reduce the volume of transactions and limit overall employment in wholesale banking.

“Gordon Brown believes that there is growing international support for banks to be charged an insurance levy so that taxpayers would not be called on to bail them out in future.” The Times, 29 January 2010

6.3 Globalisation

Globalisation is a trend that will affect the operations of all banks, regardless of whether they have a local, regional or global strategy.²⁷⁰ Globalisation impacts demand for financial services (location of customers), as well as where financial services companies decide to locate their operations. The recent crisis has also highlighted the growing interdependency between financial institutions worldwide and the role of banks in financial transactions across national boundaries.

6.3.1 Retail

Although the impacts of globalisation are less numerous for the retail sector than the wholesale sector, its relative size means that the absolute impact of globalisation could be greater.

Shared service centres and off-shoring of back- and middle-office functions are becoming increasingly popular among retail financial services companies because there is a considerable amount of back-office administration which leaders consider to be a cost driver rather than delivering any added value. According to one industry stakeholder, “Business processing is increasing and outsourcing and off-shoring will continue, especially with recent needs for cost-cutting.” This trend may lead to a continued decline in employment in non-core functions at financial services companies.²⁷¹ However, the trend has been tempered somewhat by customer opposition to foreign call centres. NatWest's UK call centres are used as a key selling point in its advertising campaigns.

²⁶⁸ Financial Times website, 30 September 2009 (see: <http://www.ft.com/cms/s/0/2f6b9c88-add0-11de-87e7-00144feabdc0.html>)

²⁶⁹ HM Treasury (2009) Asset management: the UK as a global centre

²⁷⁰ IBM (2008), No bank is an island

²⁷¹ PwC Interviews

6.3.2 Wholesale

The impact of globalisation on employment and skills in the wholesale sector is more complicated than on the retail sector. Not only is there potential to offshore back- and middle-office functions to achieve cost savings, as in retail banking, but front office functions are also likely to be affected as London's role as a financial centre changes.

The UK has benefitted from globalisation in the financial sector and London has emerged as one of the leading centres. This is particularly evident in the wholesale banking sector, which has benefitted from capital flows through London. The UK emerged as a centre for financial services because of its stability, the availability of talented labour and because the supporting services, including accounting, legal and consulting services, are among the best in the world.

However, London's relatively strong international position could weaken over the next decade – with negative implications for employment in wholesale financial services. The UK may have overtaken the USA to rank first in the World Economic Forum's Financial Development Report 2009, but the report noted that “[the USA and UK's] significant drops in score show increasing weakness and imply their leadership may be in jeopardy”.²⁷² The same report ranked Britain's financial stability – which covers currency stability, banking system stability and the manageability of public and private debts – as very poor, with the country placing 37th out of 55 nations. Furthermore, the UK ranks only 13th in the WEF's Global Competitiveness Index.²⁷³ Accessing finance, inefficient government bureaucracy and tax were seen as the most problematic factors for doing business. Experts suggest regulatory transformation and cultural adjustments are required to restore confidence in London's banking and asset management reputation.²⁷⁴

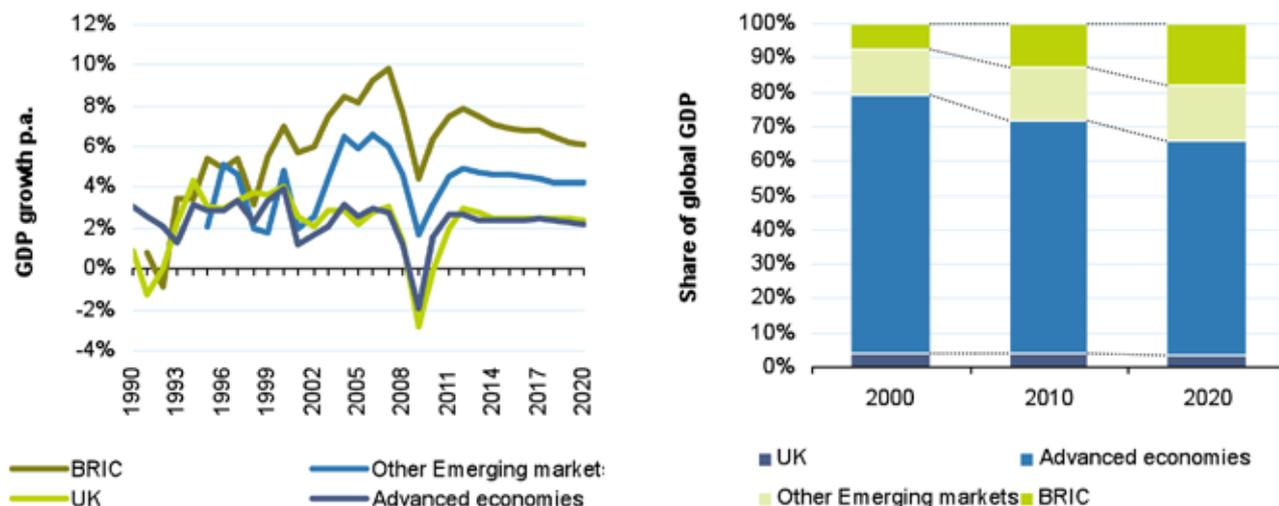
“London remains a leading financial centre, but will have to remain proactive in attracting clients and companies.” IMCA

The shift of wealth from advanced economies to emerging ones also has the potential to impact London's position as a financial centre as more business originates from these countries.

²⁷² World Economic Forum (2009) Financial Development Report

²⁷³ World Economic Forum (2009) Global Competitiveness report 2009-2010

²⁷⁴ UK Economy: The Hangover, RBS

Figure 50: GDP of UK vs. other countries, historical and projected

Source: HM Treasury (2009)

Our stakeholder interviews suggested that growth in emerging markets may lead to London's position being eroded by places like Dubai, Shanghai, Hong Kong or Singapore. The need for London involvement in international business – for example, in transactions involving Chinese investors in African natural resources – is likely to decline as financial centres develop in, or closer to, these countries.

The wholesale financial services sector is considered to be very 'mobile' and operations can be relatively easily relocated to accommodate changing business needs. It is possible that London will experience a loss of employees and jobs to developing SAAAME markets as UK companies face growing competition from financial institutions in places like China, Singapore and the Middle East. Perhaps tellingly, HSBC has decided to relocate its head office operations to Hong Kong as a result of growth in Eastern markets.

"We can't get away from the fact that the East is growing at a faster rate than the UK, the US or Europe. In my time it will take over from the West as the most powerful part of the world economy." Group CEO, HSBC²⁷⁵

However, few financial centres in the world have the depth and breadth of experience and skills that is currently located in London. By maintaining a balanced regulatory framework, predictable and fair tax system and encouraging the supporting business services that underpin London's position in the global financial markets, some observers suggest it is possible for London to maintain a strong position in the financial services sector.²⁷⁵

²⁷⁵ The Times website, 26 September 2009 (see: http://business.timesonline.co.uk/tol/business/industry_sectors/banking_and_finance/article6850242.ece)

²⁷⁶ PwC interviews

“The UK has too many fundamental advantages to be completely cast aside by the global financial community.” PwC financial services team

There is optimism among interested industry observers that London can continue to build on its foundations as a global financial centre:

“While recovery in financial markets remains tentative, the UK has a broad and deep financial services market on which to build. The structural strengths - diversity of markets, strong skills base, global orientation and legal system - that underpin London’s status as a global financial centre remain in place. London’s instinctive internationalism and openness to global business provides a base for expanding markets, such as Islamic finance, carbon markets and sovereign wealth funds” Director, IFSL

In any case, the emergence of developing economies will impact the skills required for jobs in London as UK companies will need to adapt working practices to enable them to successfully work with businesses based in these economies. Languages and cultural awareness are expected to be increasingly important to ensure UK employees can communicate with overseas clients and are sensitive to cultural differences. Languages have been identified as a key development area for UK employees and the UK government is currently carrying out a review of languages. The government requirement for state schools to continue languages beyond the age of 14 came to an end in 2004, which has led to a decline in students taking languages at GCSE from 71 per cent in 1997 to 44 per cent in 2008, which in turn has led to a decline in students taking languages at degree level.²⁷⁷

Knowledge of international business law, accountancy rules and financial regulation are also likely to be important skills requirements in the medium term future (before 2020), which is likely to require significant re-skilling of the UK financial services workforce.

“Asia has become extremely important. Wide-ranging legal, regulatory and commercial expertise will be required; language and cultural education will be important.” PwC financial services team

6.4 Consumer demand and their changing ideas and values

Consumer demand is continuously changing, with particular implications for retail banks. In this section, we outline four key trends which are likely to impact financial services: cautious consumer attitudes; more demanding consumers; and new product types.

²⁷⁷ The Times website, 10 September 2009 (see: <http://www.timesonline.co.uk/tol/news/uk/education/article6828362.ece>)

6.4.1 Retail

Cautious consumer attitudes

Consumers have demonstrated greater caution with their finances in the current economic climate and reduced the size of their balance sheet. Net borrowing on credit cards, unsecured loans and overdrafts decreased for five consecutive months, between June and November 2009, as consumers paid off debts. There was a slight increase of £52m in consumer borrowing in December, but this was ascribed to consumers bringing forward purchases on credit cards before VAT increased from 15 per cent to 17.5 per cent in January 2010.²⁷⁸ Excluding credit card borrowing, repayments outstripped new borrowing by £143m.

“The credit figures were really as soft as one might have expected. There doesn’t seem to me very much change in the trend there. This will act as a continuing restraint on consumer spending over the next few months.”

The desire to repay debts has also impacted savings – building society customers withdrew £400m in savings in December “as people searched for better returns elsewhere, spent their savings on Christmas gifts or paid back debts.”²⁷⁹

The developments of 2008 and 2009 have resulted in an increased emphasis on safety for savings and investments.²⁸⁰ The collapse of Icelandic savings accounts and the nationalisation of Bradford & Bingley and Northern Rock highlighted many weaknesses in the retail banking model and prompted the surviving banks to promote their safety and stability.²⁸¹ A better understanding of the FSCS limit of £50,000 per authorised institution has also prompted wealthy customers to spread their savings across different banks. Building societies have benefitted from the perceived vulnerabilities in banks which also have large mortgage or wholesale portfolios, while the NS&I has experienced increased applications as customers see greater safety in state-owned institutions.²⁸²

The longevity of these trends and their impact on consumer behaviour remains to be seen. Greater consumer caution, should it last, will make it more challenging for financial services companies to sell certain products to consumers. As a result, they may have to adapt their product portfolios and improve their marketing capabilities. The need for greater transparency will require staff to have a solid understanding of products and be able to explain them to customers.

²⁷⁸ <http://news.bbc.co.uk/1/hi/business/8490810.stm>

²⁷⁹ <http://news.bbc.co.uk/1/hi/business/8490810.stm>

²⁸⁰ Mintel (2008) Retail banking overview UK

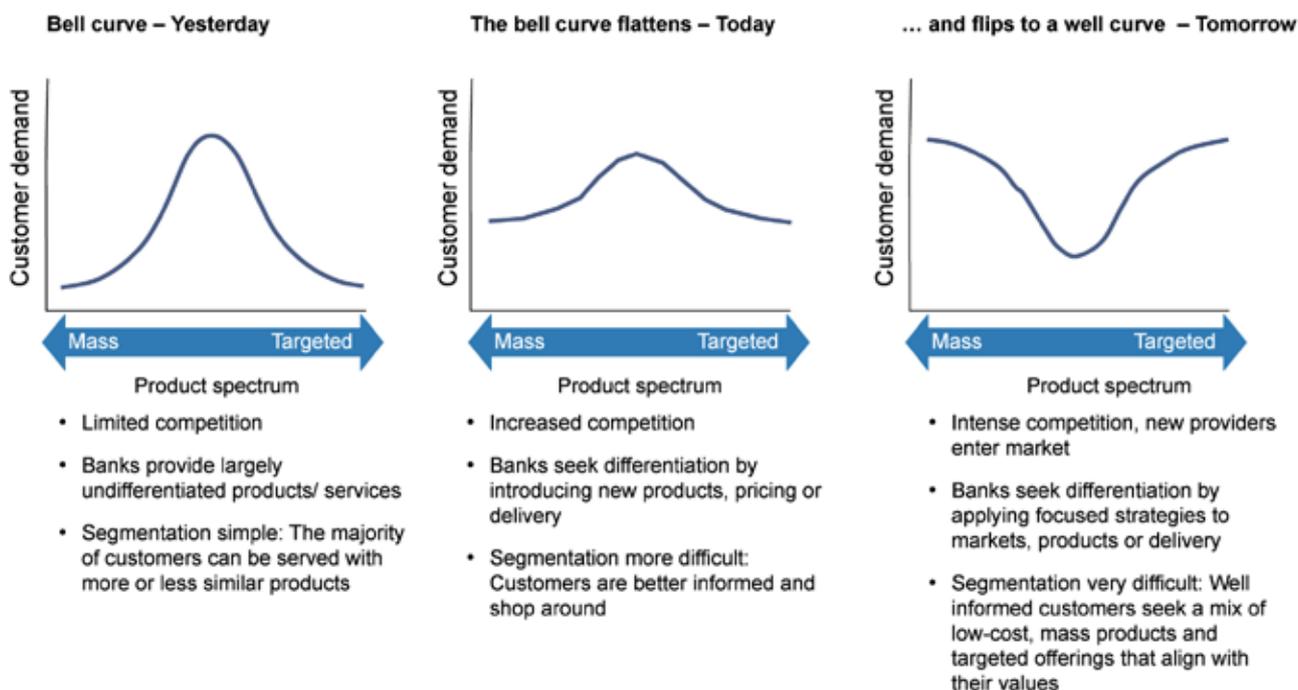
²⁸¹ PwC The Day After Tomorrow Series (available at: <http://www.pwc.com/gx/en/financial-services/day-after-tomorrow/index.jhtml>)

²⁸² Mintel (2008) Retail banking overview UK

More informed consumers

The internet and tools such as price comparison websites have increased the power of consumers and their expectations of financial institutions. A survey by Forrester Research found that as early as 2004, 60 per cent of US households were conducting their own research before buying financial services products.²⁸³ Customers are increasingly demanding low prices for basic goods, but willing to pay premiums for products and services that matter more to them personally. This is illustrated by “bell to well” in Figure 51, which shows a polarisation of consumer demand between mainstream and individualised products.²⁸⁴

Figure 51: From “bell curve” to “well curve” – polarisation of customer demand



Source: IBM

This is likely to have a number of implications for financial institutions and the skills required of employees. Banks will need to develop new products to meet new consumer demand and have staff with strong relationship and communication skills qualified to sell them to customers. The current shortage of these “soft” skills is therefore likely to become more pronounced.

²⁸³ IBM (2005)

²⁸⁴ IBM (2005) The Paradox of Banking 2015

Banks have started to borrow from the retail industry to develop the necessary techniques and skill sets to meet evolving customer demands. HSBC has introduced new branch designs based on retail concepts, with a focus on footfall and layout design to channel customers efficiently and increase opportunities to cross-sell products to them. In 2008, Barclays appointed Tesco's format and design director as the head of network development for its retail banking division. That same year, HBOS also hired a former director of Asda as its chief executive.²⁸⁵

The competitive pressure created by more knowledgeable customers is likely to be compounded by increased fragmentation in UK retail banking as RBS and Lloyds Banking Group sell off some branches and new players, such as Tesco and Virgin Money, enter the market.

Demand for new product types

Consumers are demanding new types of financial services products which will require financial institutions to have staff with an adequate understanding of them, although the skills requirement is unlikely to change. Here we discuss two examples: ethical finance and Islamic finance.

Ethical finance describes all types of financial activity which is not solely motivated by profit, but considers other implications as well. There is ethical banking, ethical insurance and ethical investments. Depending on the values and principles, ethical finance companies might refrain from doing business with tobacco or defence companies or religious organisations whose views they do not agree with. Ethical finance companies may also specifically cater certain "ethical" causes, such as environmental sustainability projects, low carbon developments and social investment.

These products are expected to gain traction in mainstream markets. According to the Ethical Consumerism Report 2009, published by Co-operative Financial Services (part of the world's largest consumer-owned organisation), spending on ethical finance nearly trebled from £5.2bn to £14.4bn between 1999 and 2009.²⁸⁶ Co-operative Financial Services' own profits increased by 11 per cent in 2009.²⁸⁷

There is also a growing market and demand for Islamic finance products, both in the UK and abroad. Islamic finance is based on principles taken from the tenants of the Islamic faith; the key principles are a prohibition on interest, conservative risk profiles and a universal sharing of profits or losses in a venture.²⁸⁸ The UK has a nascent Islamic finance presence²⁸⁹, with several Islamic banks locating in London and HSBC offering Islamic products through its Amanah brand.

²⁸⁵ Brand Republic, 6 November 2006 (see: <http://www.brandrepublic.com/News/602241/Barclays-hires-Tescos-Dodd-branch-redesign/?DCMP=ILC-SEARCH>)

²⁸⁶ <http://www.co-operativebank.co.uk/servlet/Satellite?c=Page&cid=1169627027939&pagename=Corp/Page/tplCorp>

²⁸⁷ <http://www.co-operative.coop/corporate/Press/Press-releases/Headline-news/Profits-up-17-at-The-Co-operative-Group/>

²⁸⁸ PwC (2008) Growing pains: Managing Islamic banking risks

²⁸⁹ PwC (2009) Shariah-compliant funds: A whole new world of investment

The changing nature of consumer demand will mainly impact jobs in retail financial services as these are more directly connected to consumers. Employees will primarily need a better understanding of the new types of products demanded by consumers.

6.4.2 Wholesale

The development of new products and ways of doing business to cater to evolving consumer attitudes will filter through to the wholesale financial sector. For jobs in the sector, the impact will be more on knowledge requirements than skill requirements. Islamic finance products, for instance, will require staff to understand the underlying principles to develop appropriate wholesale finance products and services, using the same skills as they would use for comparable non-Islamic products.

Caution among some investors, as well as a desire among some to regain the losses caused by the financial crisis, will influence the mandate of asset managers. Going forward, investors are likely to focus on safety and revert to investing in assets which are more likely to hold their value and return a steady income.²⁹⁰ As a result, bonds are showing a relative attractiveness over equities in the medium term, helping portfolios to meet longer term risk and return objectives.²⁹¹

With demand for transparency increasing, there will also be greater demand for valuation skills, as asset managers seek to quantify more accurately the precise values of assets and investments.

“There will be a skill demand, particularly for valuation abilities. The ability to value illiquid, derivative or hard-to-value assets is becoming increasingly valuable.” PwC financial services team

6.5 Demographics

There are two key components of the demographics driver: the ageing population of the UK and the growing migrant population. As the population ages and “baby boomers” move towards retirement, while at the same time living longer, there will be a profound impact on the financial services provision and demand within the UK, as well as the supply of labour. Simultaneously, a growing number of young and skilled migrants will ease the pressure on the UK’s ageing domestic population, bringing new skills and new financial services requirements to cater for their circumstances.

²⁹⁰ McKinsey (2009) The Asset Management Industry in 2010

²⁹¹ Barclays Global Investors (2009) BGI Insight Spring 2009

6.5.1 Retail

Aging population

The aging population is the single most important demographic change in the UK. Between 1983 and 2008, the percentage of the population aged 65 and over increased by a percentage point to 16 per cent of the population, an increase of 1.5 million people. This is anticipated to increase rapidly as the 'baby boom' generation reaches retirement. By 2033, 23 per cent of the population will be aged 65 and over. Furthermore, the fastest population increase has been in the number of people aged 85 and over, with an increase of over 100 per cent in the last 25 years, to 1.3 million in 2008. Healthier lifestyles and an improving healthcare service will encourage this trend, and the ONS predicts that by 2033 5 per cent of the population (3.2m people) will be over the age of 85.²⁹²

In conjunction with an aging population, fertility rates have been falling in the UK and are likely to continue doing so in the future. Over the last 25 years, the number of people aged 16 and under decreased from 21 per cent to 19 per cent, and it is anticipated that by 2033 this proportion will decrease to 18 per cent²⁹³.

An aging population will have significant implications for the financial sector. The current pension penetration in the UK is not sustainable for a large proportion of the aging population, particularly if some people spend 25 years or more in retirement, and is therefore likely to increase. Those who do save will also need to save (and therefore work) for longer to fund their retirement.

If individuals do start to engage more actively in their future investments, there will be an increasing demand for specialist advice in an expanding range of products, which will require specific vocational training. Furthermore, the growing proportion of people retiring, particularly those with limited or complex savings and investments, are likely to require individual affordable advice, if the UK's older population is to be able to sustain an extended period of retirement.

The ageing workforce will also require financial services, along with other industries, to invest in older workers so they can carry on working in evolving jobs.

Migration

The ONS projects that of the 10.2 million increase in UK population between 2008 and 2033, some 4.6 million (45 per cent) will be generated by the total number of net migrants.²⁹⁴ In addition, the other 5.6 million by natural increase (births minus deaths) is also partly dependent on the assumed level of net migration.

²⁹² ONS – Population

²⁹³ ONS – Population

²⁹⁴ ONS – Population. Net migration is immigrants less emigrants

The predicted rise in migration into the UK will require financial services to develop their product offerings to cater for this growing, geographically mobile, segment of the population, such as through remittance offerings or transferrable banking accounts. The sector may also need to adapt to cater for a growing number of migrants who join the over fifties group, and seek not only ‘traditional’ migrant financial services such as remittances, but also life and repatriation insurance too.²⁹⁵ As the migrant population becomes a larger more significant segment of the population, language skills also may become more important in the retail financial sector.

Given the ageing population in the UK and migration trends, we can also expect immigrant labour to account for a growing share of employment in retail financial services.

6.5.2 Wholesale

Asset management will be more impacted than other wholesale sectors by the UK’s aging population. Notably, the amount of assets to invest will grow as more people save more for retirement. However, as asset management is a scalable activity, there is unlikely to be a significant need for more asset managers – unless the growth encourages new competitors to enter the market, thereby increasing the need for asset managers.

However, global demographic trends may impact the skills requirements of asset managers. The Treasury anticipates that investment opportunities in ‘younger’ societies with an abundance of labour but a far more limited supply of capital, will become more attractive prospects for the UK financial services companies.²⁹⁶ This trend will have a similar impact on skills to globalisation, discussed earlier. There may be increasing demand for language skills and cultural understanding among UK asset managers with investments in these countries.

6.6 Environmental change

As their knowledge continues to evolve, scientists have issued stronger and more compelling warnings about the impacts of climate change and the steps that need to be taken in order to avoid the most catastrophic outcomes associated with these changes.

Climate change can alter the frequency and severity of many extreme weather events, such as floods, droughts and hurricanes. To avoid the risks of dangerous climate change, climate scientists predicted that global greenhouse gas emissions need to peak within the next fifteen years, and be halved relative to 1990 levels by 2050.

²⁹⁵ Insurance Age

²⁹⁶ HM Treasury (2005) The UK financial services sector: Rising to the challenges and opportunities of globalisation

In financial services, climate change is likely to have the most noticeable impact on the types of products and services which are sold to either counter climate change or deal with its consequences – including renewable energy project financing, emissions trading and insuring against climate risks. Across the industry, there will be a greater need for staff who understand renewable energy technologies and the science of climate change. However, the fundamental skills are required of staff are unlikely to change. The requirement is for knowledge, and this can be easily learned.

6.6.1 Retail

Insurance against climate risks

The greatest impact of climate change on insurers is likely to be the increased frequency and severity of weather-related property insurance claims. According to the Association of British Insurers, a 4°C global temperature rise and a 1.45° southward shift in storm track across the UK could result in a 14 per cent increase in average annual insured flood losses, to £633m, and a 25 per cent rise in average annual insured wind, to £827m.²⁹⁷ Changing weather patterns are likely to change demand for insurance products and may result in insurers withdrawing coverage for some risks which are deemed too high. This could negatively impact the size of the sector, as well as overall employment. However, the occupational mix could change: according to a report by the European Trade Union Confederation, there will be a particular need for experts in risk assessment and damage evaluation.²⁹⁸

Insurers will need to conduct further research to fully understand the likely impact of climate change. They will also need to enhance models to factor in newly available climate change data and review portfolios in the light of more sophisticated models and an improved understanding of the issues. This will require professionals with appropriate knowledge of climate change, though not necessarily new skills.

6.6.2 Wholesale

Renewable energy project financing

There will be significant demand for banks to provide or raise financing for renewable energy projects. These projects have high initial capital requirements and tend to have high risk profiles. Competition between technologies also means that providers of finance must make a significant investment in understanding the different technologies and the knowledge of their employees – although the skills requirements are not that different.

²⁹⁷ ABI website (see: <http://www.abi.org.uk/content/contentfilemanager.aspx?contentid=45255>)

²⁹⁸ GHK (2009) The Impacts of Climate Change on European Employment and Skills in the Short to Medium-Term: A Review of the Literature

Emissions trading

The emissions trading market is growing rapidly and there is strong evidence to suggest that there is significant room for growth. Although the market is relatively small compared with other energy markets, it is growing rapidly. Future growth is anticipated as emissions quotas are reduced in 2013, increasing demand for tradable permits. The emissions trading scheme may also be expanded to include airlines, which are expected to account for 4 per cent of global emissions by 2050. According to the FSA, this “would generate significantly increased demand” and increase market liquidity.²⁹⁹

The growth in emissions trading will increase employment associated with this activity, including trading and support functions. According to the FSA, “there is a keen market for experienced staff in both front and back office roles at authorised firms”³⁰⁰ trading emissions permits and this need is likely to grow with the market in the medium term. Firms will be required to develop a set of risk management tools for this type of trading as these are less developed than in other markets, due to the relatively short track record of pricing and trading history.³⁰¹ However, the skills required to provide these services are not significantly different from those required for providing similar services not linked to environmental issues.

6.7 Technology

Technological advances will be a key determinant of the future state of financial services. Technology has the potential to spur innovation, leading to new products or systems that could generate improved market share or penetration as well as better ways to limit risk or maximise profits, while also reducing costs on a large scale by automating processes and thus making job positions redundant or more efficient.³⁰² Greater reliance on more advanced technology also increases the need for security.

²⁹⁹ FSA website (see: http://www.fsa.gov.uk/pubs/other/emissions_trading.pdf)

³⁰⁰ FSA website (see: http://www.fsa.gov.uk/pubs/other/emissions_trading.pdf)

³⁰¹ FSA website (see: http://www.fsa.gov.uk/pubs/other/emissions_trading.pdf)

³⁰² European Financial Services Technology website (see: <http://www.fsteurope.com/article/Striving-for-new-technologies/>)

6.7.1 Retail

New products

Payments systems are developing quickly and offering financial services customers new products and platforms, with technologies such as contactless, mobile and micropayments all gaining penetration, as well as more streamlined and more secure internet payments all developing into major features.³⁰³ The technological basis behind peer-to-peer social finance (such as P2P banking) and microfinance has only been developed in recent years and has experienced strong growth. This growth is likely to continue and become an important niche in financial services.³⁰⁴

Increasing reliance on IT for product delivery may simultaneously increase the need for IT technicians and support staff.³⁰⁵ Training for staff members, even those not directly employed in an IT role, will become essential and employers will seek workers who are IT-literate and able to understand complex financial services applications. IT security training as well as dedicated IT security support teams are likely to be increasingly in demand.

Increasing automation

Automated banking, first via ATMs and later via the internet, has decreased demand for transactional services in branches. Online banking transactions have increased at an annual rate of 36.2 per cent between 2002 and 2007, and growth is likely to continue. This has resulted in a long-term trend of branch closures³⁰⁶ - for example, HSBC shut 31 branches in 2008, 54 in 2009 and planned to close a further 16 in January and February 2010 and as many as 100 over the course of the year.³⁰⁷ This trend is likely to continue as technology penetration increases and reduce demand for some customer-facing staff.

³⁰³ Accenture (2009) Harmonising payments – insights to progress on the European Payments Services Directive.

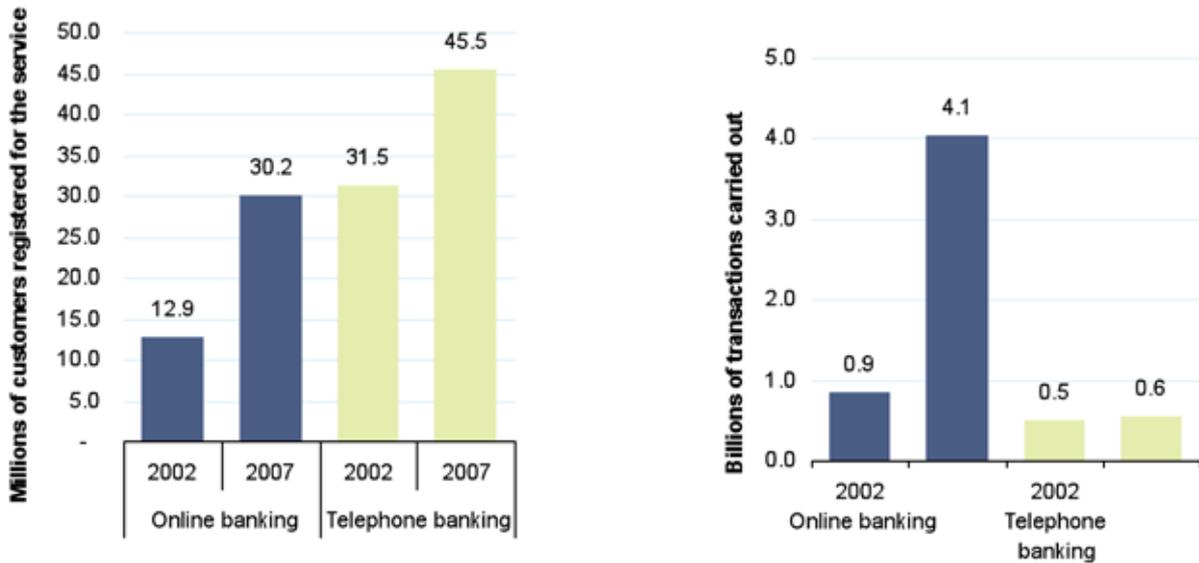
³⁰⁴ Capco Institute (2008) Zopa.com - Innovation in the UK Financial Services industry

³⁰⁵ European Financial Services Technology website (see: <http://www.fsteurope.com/article/IT-2012/>)

³⁰⁶ University of Nottingham (2006) The Changing Geography of British Bank and Building Society Branch Networks

³⁰⁷ http://www.thisismoney.co.uk/savings-and-banking/article.html?in_article_id=492656&in_page_id=7

Figure 52: Number of customers and transactions for remote banking, 2002-2007



Source: Mintel (2008)

Mobile telephone banking has not yet experienced significant growth in transaction volume, but the advent of smartphones could spur market growth and exacerbate the trends cause by online banking. The channel is expected to account for £6bn worth of transactions annually by 2012 and serve nearly half of mobile phone owners by 2014.³⁰⁸

Retail financial services aggregator websites have also reduced the need in some cases for IFAs and advisors in bank branches.³⁰⁹ The bancassurance channel has also been weakened by higher levels of independent consumer knowledge as a result of readily-available information on the internet.³¹⁰

IT efficiency is also likely to reduce the number of back and middle office staff required to process and support front office activities.

³⁰⁸ PwC – Mobile Banking; Javelin Strategy & Research, 2009 Mobile Banking Forecast

³⁰⁹ IBM (2006) Insurance 2020: Innovating beyond old models

³¹⁰ Mintel (2009) Life and Protection UK

Outsourcing and offshoring

Outsourcing technology, in particular core applications and systems, is set to grow. While financial services companies usually outsource secondary systems such as human resources and marketing applications, there is an increasingly trend towards trusting outsourcing firms to deliver on core applications.³¹¹ There will be a movement towards multi-sourcing as firms not only outsource more activities, but also use offshore providers more frequently to complement their domestic outsourcing arrangements. China as an outsourcing destination is growing in popularity, although India remains the top overseas destination.³¹²

However, not all financial services companies are prepared to outsource their functions and many have been reluctant to entrust their core functions to third parties:

“Banks have historically underinvested in IT and this trend could continue into the future. There is currently insufficient cash for banks to invest in transformation processes, although this could change with developments in the future” British Bankers Association

Security

As the dependency of financial services on technology increases, so too do the risks associated with using that technology. According to an IDC survey, data confidentiality and system integrity are considered the two most significant threats to organisations.³¹³ A January 2010 report by Forrester Research found that 36 per cent of all business planned to increase security spending in 2010 by 5 per cent or more.³¹⁴

However, there is already a wide gap between IT security skills supply and demand across industries. According to a 2008 worldwide survey by the Computing Technology Industry Association, security was identified by 73 per cent of organisations as the most important area for IT skills. However, just 57 per cent said their IT employees are proficient in security skills. This skills deficit is likely to become more pronounced as technology penetration increases. However, the deficit is difficult to address as security threats are constantly changing.³¹⁵

6.7.2 Wholesale

Wholesale financial services will be impacted by many of the same efficiency-driven developments in technology as retail banking. Offshoring and outsourcing will be important and the emphasis on data security will increase, with similar implications for skills and employment.

³¹¹ Accenture/Economist Intelligence Unit Global IT Outsourcing Survey

³¹² Accenture/Economist Intelligence Unit Global IT Outsourcing Survey

³¹³ IDC (2008) The next generation of web security

³¹⁴ <http://www.eweek.com/c/a/Security/IT-Security-Spending-Expected-to-Increase-for-Enterprises-SMBs-532369/>

³¹⁵ <http://www.scmagazineus.com/survey-it-security-employees-in-demand-but-skills-lack/article/107406/>

Wholesale financial services companies will also need to make significant investments in technology to catch up with the increasingly complex nature of the products they deal in. When Lehman Brothers collapsed in 2008, it had outstanding derivatives contracts with a face value of c.\$39tr with 8,000 different counterparties and recorded on 20 to 30 different systems³¹⁶ which will take several years to reconcile. This has made unwinding Lehman's liabilities extremely complex and illustrates the need for investment in technology.

“The main conclusion so far [...] is that the technology costs for derivatives have been underestimated. In addition, the answers that every regulator now wants and every investor should demand, in terms of levels of exposures and risks that banks hold, cannot be easily gleaned from the current multiple systems used to value and track positions.” Financial Times, 11 September 2009

RBS has already committed £6bn and made long-term drives to unify their technology systems and invest in applications and platforms that will lead to improved efficiencies.³¹⁷

6.8 Future skills requirements

Whichever way financial services evolves over the next 10 years – we discuss three potential scenarios in the next chapter – there will be a shift in the types of jobs in the sector and certain types of skills will be more in demand.

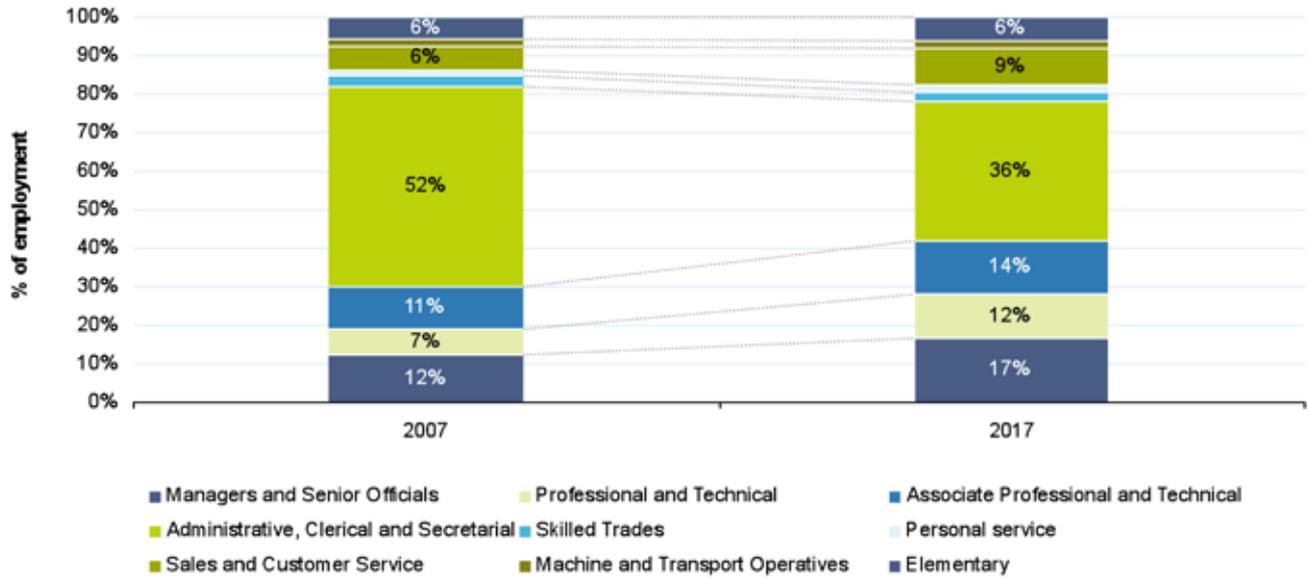
According to the Working Futures³¹⁸ forecast, administrative, clerical & secretarial occupations are expected to account for a smaller share of financial services jobs over the next decade. There have been significant job losses in this job category across all UK industries since the early 1990s due to the use of computers and IT systems. This trend is projected to continue at an even faster pace going forward. Meanwhile, managers and senior officials, professional and technical occupations and sales and customer service occupations are expected to account for a greater share of employment.

³¹⁶ <http://www.ft.com/cms/s/0/85c5dfec-9eff-11de-8013-00144feabdc0.html?SID=google>

³¹⁶ Bloomberg website (see: <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aBBgnijXTbdY>)

³¹⁶ We've used data from Working Futures because, although it may not fully reflect the recent financial crisis, the broad trends it shows are likely to remain true to varying degrees under all potential scenarios

Figure 53: Occupational mix for financial services, 2007-2017



Source: Warwick Institute for Employment Research: Working Futures II (2008)

However, when accounting for replacement demand and changes in overall employment together, the greatest demand for new workers will still be for administrative positions, as shown in the dark blue bar in Figure 54. This will be flowed by managers, associate professionals and professionals.

Figure 54: Requirement for new employees by occupation, 2007-2017



Source: Working Futures 2008

Skills shortages and gaps affecting administrative and managerial positions are therefore likely to remain an issue without action. Gaps are much less common among professionals and associate professionals.

We expect demand for certain specialist financial services skills to increase, however financial services evolves in the next decade. The most widespread impact will be on existing jobs; employees working at all levels will need new skills. Some new roles will be required, and some changes will be required to existing roles. The skills, discussed in more detail below, include:

- risk management skills;
- compliance skills;
- product knowledge and advice skills; and
- customer handling skills.

Risk management skills

Whatever the level of regulation imposed by government, there is likely to be greater emphasis on risk management among financial institutions. This will affect demand for risk management professionals who have an understanding of the products and services being sold and the risks that they involve. Risk management staff currently do not need to hold any specific qualifications, although accounting, finance and actuarial qualifications are all valuable. There is an acute shortage of these professionals and demand for them is likely to increase.

Depending on the extent of regulation, compliance and risk management will become embedded in roles across financial services organisations, in much the way it has in accountancy firms following the introduction of Sarbanes-Oxley. In its paper, “The shape of business: the next 10 years”, published in November 2009, the CBI predicted that:

“...the new business climate has made it more apparent that additional and/or more exhaustive checks and balances are needed. New policies to demonstrate integrity, manage risk and provide transparency will be the focus... Ultimately, everyone in the organisation will be clear on their governance roles and responsibilities, from the sales floor to the boardroom, with greater controls in place throughout.”³¹⁹

In retail banking, for example, this could mean loan officers taking a more subjective and thorough approach to assessing applications, rather than relying on automated computer systems to determine whether to approve a loan. The role will require stronger critical thinking and numerical skills than in the past, but also a higher degree of judgment.

In wholesale trading jobs this could mean traders more thoroughly identifying and quantifying risks associated with the financial instruments they trade, and operating within tighter risk tolerance parameters.

³¹⁹ CBI (2009): The shape of business: the next 10 years, p.29

Compliance skills

It is likely that reporting requirements will increase as governments demand greater transparency. This will affect demand for back-office administrative and managerial staff responsible for reporting and compliance. Some of these staff will have only basic qualifications but will be supervised by accountants and other professionals.

While the burden of policy-setting and reporting will fall to compliance professionals in the back-office, front-line staff will need to adhere to the policies and collect the information required for regulatory compliance. In the past, “know your customer” requirements made many front-line staff in retail and wholesale financial services responsible for verifying the identity of customers and obtaining appropriate documentation. We can expect increasingly rigorous compliance requirements in future and front-office staff will need to be familiar with them. In recent months, for instance, FSA rules mean mortgage lenders are checking applicants’ income more rigorously, and self certification mortgages may be phased out.

Product knowledge and advice skills

In the retail sector, a greater appetite for information about products from consumers will increase the need for client-facing staff with strong knowledge about the products they are selling and the advice skills to explain them properly. Staff will increasingly deal with customers who have “done their homework” online and will need to answer complicated queries from them. The supply of these skills is likely to come under pressure as a result of the RDR, which will encourage many IFAs to exit the market, restricting the supply of financial advice.

If the recommendations of the Thoresen review are adopted and generic financial advice is provided by the third sector, there will be greater demand for individuals with a breadth of knowledge about basic financial services and financial planning, as well as tax and benefits. While the Citizens Advice Bureau and others currently provide these services, capacity will need to be considerably increased.

There will also be a need for greater product knowledge in the wholesale sector, albeit at a more sophisticated level. After the crisis, many institutions were accused of trading products their employees didn’t fully understand. Insurance companies, for instance, will no longer have an appetite to invest in high-return instruments without fully understanding the risk implications. The need for understanding will extend to the highest levels of the organisation to enable proper accountability and control.

Customer handling skills

As more transactional work is carried out automatically online or on the phone, customer-facing roles in retail financial services will become more challenging and there will be a greater emphasis on customer service. School leavers formerly trained as cashiers to carry out simple transactions will need to be able to address more complicated customer needs. They will need strong interpersonal skills, including the ability to listen to customers, offer sound advice and solve problems. They will need to demonstrate greater empathy and maturity than before in order to help rebuild trust. They may need to be qualified to a higher standard, probably supplemented by structured development programmes.

Advisers in the third sector offering generic financial advice as a result of the Thoresen review recommendations will require specific skills to serve customers who will have historically had limited access to financial advice. They will need to be able to communicate with less well-educated customers, in a simple and easily understood way.

In the wholesale sector, the need for employees who can communicate effectively with international customers is likely to increase. There is already a recognised shortage of language skills among UK-educated candidates, and demand for these skills is only likely to grow. Employers will also increasingly seek candidates who really understand cultural differences, and the customs and nuances of conducting business with Chinese or Russian clients, for example.

As demand shifts towards these types of skills, other skills may become relatively less important. In particular, data entry and processing positions are likely to become less important as financial services are automated and the trend to offshoring continues.

6.9 Anticipated supply of skills

There are four principal sources of skills and labour for the financial services sector, or indeed any sector. Financial services will have to make the best use of these talent pools to minimise skills shortages and gaps. The sources are:

- the existing workforce;
- school leavers and graduates;
- experienced hires from other industries; and
- migrant labour.

Each source is considered in more detail below.

Up-skilling/training the current workforce

The majority of the financial services workforce in 2020 is already working in the sector. This is clearly the single most important source of skills and future employees. However, many of these people's jobs are likely to change as the emphasis on risk, transparency and customer service increases. Therefore, there is a significant need to train the workforce; responsibility for this will largely fall to companies, with some government support. While financial services companies have always invested heavily in the skills of their employees, the shift towards new types of skills may require greater investment than before.

The CBI expects businesses to refocus their approach to training and development, which could impact how these new skills needs are addressed:

*“Businesses will put additional effort into understanding their future skill needs and many will develop detailed skill roadmaps for their organisations... Businesses will collaborate more extensively with schools, colleges, universities and other education and training institutions to fund and design courses more closely aligned with their needs. Businesses will secure greater return on investment in training employees in a number of ways. Training to enhance business productivity will be the priority... across the board, funding for “non-essential” training and general career development training not directly aligned with corporate goals will be scaled down substantially or even stopped.”*³²⁰

There may be an opportunity to retrain many of the IFAs who are likely to leave this segment of the market as a result of the recommendations of the RDR. These people already have financial knowledge which could be deployed elsewhere in the industry – perhaps by working directly for financial services providers.

School leavers and graduates

There is a pressing need to improve the quality of school leavers so they are better equipped for employment in general, not just in financial services. This includes improving basic skills such as numeracy and literacy. In recent months, several major employers have criticised the state of the UK's education system.

“Sadly, despite all the money that has been spent, standards are still woefully low in too many schools. Employers like us... are often left to pick up the pieces.” Sir Terry Leahy, chief executive, Tesco³²¹

“[Some school leavers] cannot do reading. They cannot do arithmetic. They cannot do writing.” Sir Stuart Rose, chief executive, Marks & Spencer³²²

³²⁰ CBI (2009): The shape of business: the next 10 years, p.21

³²¹ The Guardian, 13 October 2009 (see: <http://www.guardian.co.uk/business/2009/oct/13/leahy-tesco-education-gordon-brown>)

³²² The Daily Telegraph, 24 November 2009 (see: <http://www.telegraph.co.uk/education/educationnews/6638699/Sir-Stuart-Rose-Schools-are-not-providing-workers-with-the-right-skills.html>)

Retail financial services suffer from low attractiveness among job-seekers which limits its ability to attract well-qualified candidates. The FSSC is currently assisting Higher Education Institutions in raising awareness amongst career advisors and HE teaching staff about the jobs the industry can offer and the skills required so that the industry can attract the most able graduates.

Experienced hires from other industries

Competitive remuneration has enabled the financial services sector, and the wholesale sector in particular, to poach employees from other sectors. This has been true for all types of role, whether core or non-core, front-office or back-office and roles within banks are generally better paid than similar roles in other industries.

As the type of skills demanded changes, this is likely to continue. The increasing emphasis on regulation and compliance means banks may seek to attract more professionals with risk management experience from other industries, such as professional services and law. Similarly, financial institutions' need for customer service expertise may be supplied in part by the retail sector. This has already happened already at very senior levels, as mentioned earlier in this report – in 2008, Barclays appointed Tesco's format and design director as the head of network development for its retail banking division. Earlier that year, HBOS hired a former director of Asda as its chief executive.³²³

However, if the profitability of wholesale financial services is lower in future and the ability of the industry to pay well is diminished, it may have greater difficulty attracting top-calibre candidates, from other industries or elsewhere.

Immigrant labour

Immigrant labour is likely to become more important in all areas of financial services, especially as the population ages. However, it could notably provide the complex mathematical and statistical reasoning that will be required to ensure adequate risk assessments moving forward. The gap between the numeracy and quantitative skills of UK graduates and their overseas counterparts has resulted in increased recruitment of foreign candidates into wholesale financial services over time. The extent to which the UK can attract and retain migrants will be influenced by its relative economic performance in comparison to immigrants' home countries and that of other countries competing to attract immigrants. However, we do not expect the industry's ability to draw candidates from abroad commensurate with its needs to diminish significantly in the medium term.

³²³ Brand Republic, 6 November 2006 (see: <http://www.brandrepublic.com/News/602241/Barclays-hires-Tescos-Dodd-branch-redesign/?DCMP=ILC-SEARCH>)

7. Scenarios

Chapter summary

We have developed a set of scenarios illustrating potential future states for the financial services industry in 2020, based on analysis of the findings from desk research and interviews with industry stakeholders relating to the drivers for change in the industry.

Due to differing industry drivers, we have developed a separate set of scenarios for retail financial services and wholesale financial services. The primary drivers of retail financial services are regulation and consumer demand. For wholesale financial services, these drivers are regulation (relative to other jurisdictions) and the pace of globalisation.

The retail scenarios are:

- Scenario R1: “Laissez faire,” characterised by light regulation and consumer appetite for credit – a scenario that is similar to the last decade;
- Scenario R2: “Sustainable consumer finance,” characterised by moderate regulation and more balanced consumer attitudes; and
- Scenario R3: “Utility financial services,” in which restrictive regulation constrains innovation and consumers have cautious attitudes to credit and a greater appetite for savings.

The wholesale scenarios are:

- Scenario W1: “Business as usual,” in which the UK retains a light-touch regulation and the pace of globalisation is relatively slow, favouring London’s position as a global financial centre;
- Scenario W2: “Sustainable global finance,” characterised by moderate regulation that is consistent with other jurisdictions. The pace of globalisation means the UK, centred on the City of London, loses some share as a financial centre, but its position remains supported by strong infrastructure; and
- Scenario W3: “Shift to the East,” in which the UK regulatory environment is more restrictive than other jurisdictions and the pace of globalisation accelerates a shift of wholesale business to other financial centres in emerging markets.

Scenarios R1 and W1 result in high but unstable growth in overall employment. Scenarios R2 and W2 result in some decline in overall employment. Scenarios R3 and W3 yield a more substantial decline.

In terms of sector impact, retail financial services employment is likely to be more stable overall than wholesale employment as investment banking and asset management are particularly volatile. Insurance does not always follow the same trends as the other sectors due to differing drivers of demand – for instance, increased caution could be favourable for insurance products.

7.1 Introduction

In order to establish our scenarios for the financial services industry in 2020, we considered the six drivers (in the foresight chapter) that are likely to drive change across the sector. We concluded regulation, consumer demand and globalisation will be the drivers that will have most influence on the shape of the sector in the decade to 2020. In particular these drivers will impact in different ways on retail and wholesale financial services, so as a consequence we have constructed retail and wholesale scenarios.

7.2 Existing projections

Working Futures projects modest employment growth in the sector, although forecasts may be somewhat out-of-date given the financial crisis. Between 2007 and 2017, the sector's workforce was anticipated to grow by 0.8 per cent p.a. to 1.2m employees.³²⁴ The forecast anticipates productivity to continue to grow, but at a slower pace than before – between 2.0 per cent and 2.1 per cent p.a. between 2007 and 2017, vs. 8.8 per cent p.a. between 2002 and 2007.³²⁵

Underlying the overall increase in employment forecast by Working Futures is a replacement demand rate of 37.3 per cent between 2007 and 2017 – in other words, 37.3 per cent of people working in financial services in 2007 are expected to leave the industry by 2017 and will need to be replaced. This is comparable to the overall forecast rate for all sectors of 36.8 per cent.³²⁶

Working Futures does not segment financial services employment data between activities (banking/insurance/asset management; retail/wholesale). Therefore, it is not possible to benchmark the individual retail and wholesale scenarios against it.

7.3 Retail scenarios

The key drivers of retail financial services going forward, in our view, will be regulation and consumer demand. We have used these two dimensions as the scenario framework for the retail financial services sector.

Proposed regulations relating to capital, liquidity, transparency and risk management could dramatically impact the activities of retail financial services institutions in terms of the products and services they offer and the business models needed to deliver them. While some regulation such as Solvency II is now looming on the horizon other regulations that will result from government responses to the credit crisis are still at proposal stage.

³²⁴ Working Futures

³²⁵ Working Futures

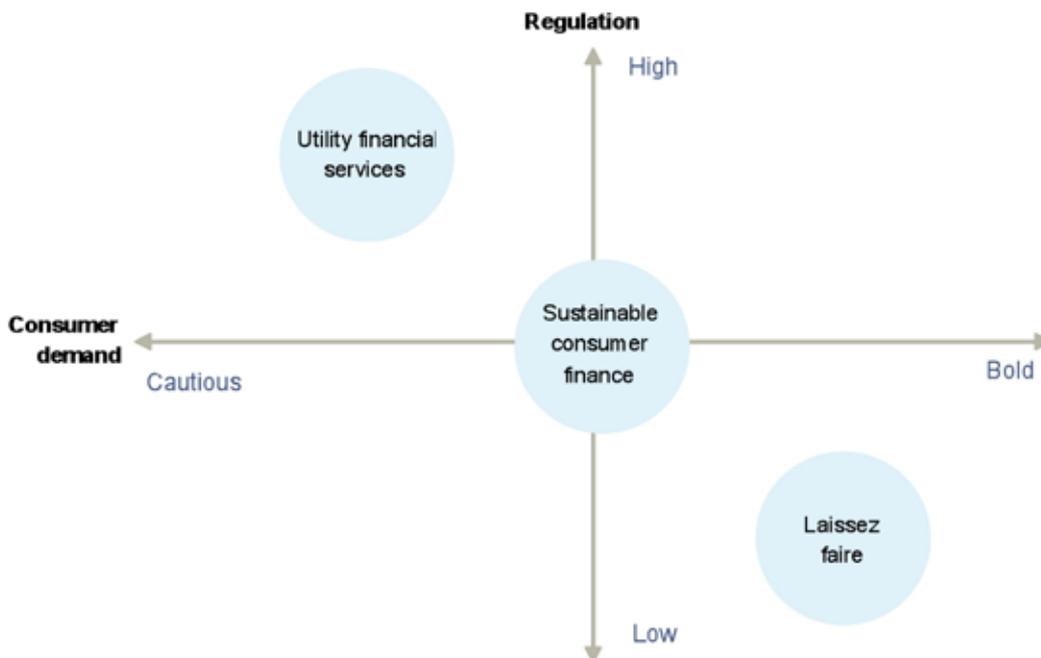
³²⁶ Working Futures

The future state of the retail financial services market will also be determined in large part by the nature of consumer demand. Depending on the economic environment and general consumer attitudes, consumer demand could be cautious, characterised by aversion to risk and debt and preference for savings products; or it could return to its more “pre-crisis” state and include a large appetite for risk and credit.

The chart below sets out three possible scenarios for retail financial services based on these drivers:

- Scenario R1: “Laissez faire,” characterised by light regulation and consumer appetite for credit; a scenario that is similar to the last decade;
- Scenario R2: “Sustainable consumer finance,” characterised by moderate regulation and more balanced consumer attitudes; and
- Scenario R3: “Utility financial services,” in which restrictive regulation constrains innovation and consumers have cautious attitudes to credit and a greater appetite for savings.

Figure 55: Summary of scenarios



Source: PwC analysis

7.3.1 Retail scenario 1: “Laissez faire”

Under this scenario, retail financial services return to their “pre-crisis” state. It is assumed that many of the proposed changes impacting retail financial services are not enacted or are watered down due to lobbying, political inertia or perhaps a change of government. There are few additional restrictions on the interactions between financial services and consumers, who recover their confidence and their appetite for debt – the combination of which results in high growth for retail financial services. Product penetration is high among consumers, as is their leverage. In this scenario, both regulators and financial services institutions fail to fully address their shortcomings.

Regulatory features of this scenario might include:

- light-touch regulation by the FSA;
- no increase in banks’ and insurers’ capital requirements;
- no new requirements for banks to do due diligence on their customers;
- weakening of Solvency II for insurers;
- only partial adoption of the RDR recommendations; and
- only partial adoption of the Thoresen Review recommendations.

This scenario results in high growth for the retail banking sector which benefits from high levels of consumer debt. Due to the maturity of the insurance market, its growth would be more moderate.

Table 15: Sector-specific implications of scenario

	Description	Industry output (Illustrative)
Banking	<ul style="list-style-type: none"> •Capital requirements remain relatively low and banks make heavy use of securitisation to fund loans •Return of high-risk products, such as sub-prime, 100% and self-certifying mortgages 	
Insurance	<ul style="list-style-type: none"> •Solvency II is continually challenged and amended, fails to achieve its original aspirations, and does not impact insurers as heavily as initially predicted •Focus on wealth-creation rather than wealth protection products. Life insurance performs less well than in other scenarios •Distribution remains commission based and largely dependent on the IFA channel 	

Source: PwC analysis

The emphasis on efficiency is somewhat lower in this scenario than the others as revenue growth means that profit margins are more easily restored and overall employment grows. The most important skills for the workforce are those which enable financial institutions to develop products and sell them to consumers. Quantitative skills are especially important. Client-facing staff (ranging from call-centre workers to private bankers) with good interpersonal and relationship skills are required, although less than in Scenario 2 as consumers possess a greater appetite for new financial products and are easier to sell to. IFAs, who continue to sell on a commission basis, remain an important distribution channel for financial products to the entire consumer market. Marketing and strategy professionals will be important to support sales.

7.3.2 Retail scenario 2: “Sustainable consumer finance”

Under this medium-growth scenario, retail financial services are subject to an increase in regulatory control and transparency. Many of the proposed regulatory changes, such as the RDR and the Thoresen Review, are enacted. An NHS Direct-style free financial advice service is launched, which helps increase consumers’ financial awareness. Consumers demonstrate a moderate appetite for credit and trust and transparency become key selection criteria for financial products. Personal debt levels remain moderate, also due in part to banks unwillingness to lend to uncreditworthy borrowers. The level of financial product innovation and personalisation is high, even higher than in Scenario 1 as financial institutions have to be creative in order to grow business given tighter regulations and consumers’ lower appetite for credit.

Regulatory features of this scenario might include:

- increased capital requirements for banks;
- Solvency II for insurers;
- IFAs selling on a fee rather than commission basis, per the RDR;
- adoption of the Thoresen review recommendations; and
- increased reporting requirements.

This scenario results in moderate and sustainable growth for both the banking and insurance sectors.

Table 16: Sector-specific implications of scenario

	Description	Industry output (Illustrative)
Banking	<ul style="list-style-type: none"> •Banks subject to higher capital requirements. Securitisation becomes a less important source of funding and the current retail banking business model becomes less profitable •Banks implement strict credit requirements and are less willing to issue credit cards and approve mortgages than before the financial crisis •Higher-service levels. Cross-selling required to extract greater revenues from individual customers 	↓
Insurance	<ul style="list-style-type: none"> •Solvency II requires insurers to develop alternative sales channels to the IFA market •IFAs focus on wealthier consumers who are able to pay for their advice •Lower-income consumers receive objective advice from government and the third sector •Life insurance products perform relatively well due to increased consumer focus on wealth protection. However, there is demand for greater transparency about the financial characteristics and benefits of products 	↑

Source: PwC analysis

Under this scenario, overall employment declines somewhat. Financial services institutions will still need more quantitative skills, but interpersonal and relationship skills are particularly important as they must overcome consumers' more conservative attitudes to sell new products. Consumer demand for high-quality advice also means customer-facing staff will need a sound knowledge of financial products. The development of a NHS Direct-style financial advice service would also require the government and/or third sector to employ a significant number of advisers with these skills. There will be a need for more employees focused on evaluating the risk of individual customers and complying with government reporting and risk management requirements.

7.3.3 Retail scenario 3: "Utility financial services"

Under this scenario, retail financial services return to a more traditional savings-oriented model. There is a high degree of regulatory control and transparency and extreme conservatism among financial institutions – due to heavy handed regulation, state ownership, or both – means products are highly standardised and the level of innovation is very low. Consumer attitudes about finance are very cautious – they retrench, de-leverage and focus on wealth preservation rather than creation. This is the least attractive scenario for financial institutions and results in low growth or contraction; banks in particular would be forced to rebuild trust with customers. The wider macroeconomic environment would remain depressed.

Regulatory features of this scenario might include:

- regulations at least as stringent as those in scenario R2;
- higher capital requirements; and

- stringent transparency regulations, resulting in a significant regulatory burden.

This scenario results in all sectors contracting, although retail banking is more severely impacted than insurance due to negative impact on debt products.

Table 17: Sector-specific implications of scenario

	Description	Industry output (Illustrative)
Banking	<ul style="list-style-type: none"> •Banks subject to higher capital requirements. Securitisation no longer a source of funding and the current retail banking business model becomes less profitable •Banks retain strict credit requirements and are less willing to issue credit cards and approve mortgages than before the financial crisis 	
Insurance	<ul style="list-style-type: none"> •Insurance premiums decline overall due to lower consumer demand for protection •However, life insurance products do not perform as poorly due to increased consumer focus on wealth protection 	

Source: PwC analysis

Under this scenario, employment declines significantly. Severely constrained revenues mean financial institutions need to drive down costs and there will be substantially less demand for salespeople and staff focused on new product development. The required skill set shifts markedly towards regulation and compliance, as the back and middle-offices become relatively more important. There will be a need for more employees focused on evaluating the risk of individual customers and complying with government reporting requirements. However, the development of an NHS Direct style financial advice service would require the government and/or third sector to employ a significant number of advisers with strong numeracy and interpersonal skills.

7.4 Wholesale scenarios

The key future drivers of wholesale financial services – and London’s position as a global financial centre – in our view will be regulation and globalisation. We have used these two dimensions as the scenario framework for the wholesale financial services sector.

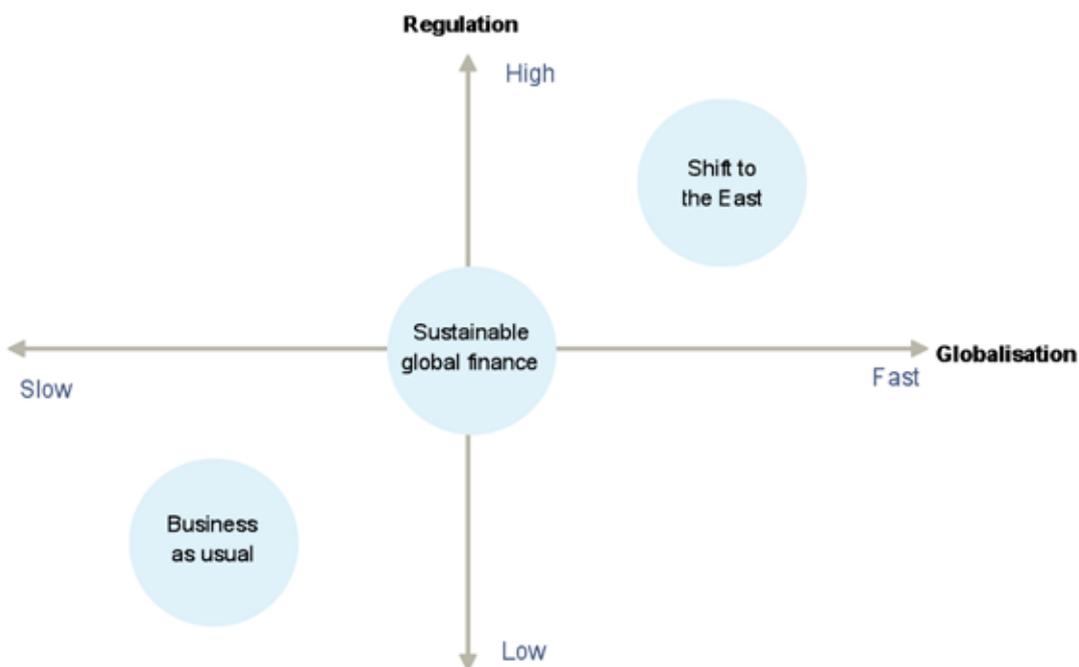
Proposed regulations relating to capital, liquidity, transparency, risk management and remuneration – and how these compare with those in the USA, Europe and other centres – could dramatically impact the activities of wholesale financial services institutions in terms of the products and services they offer and how they administer them. Again, many regulations remain at the proposal stage, so their probability of being implemented and their impact are uncertain.

By globalisation, we refer to the pace at which economic power shifts from mature Western economies to developing economies. A rapid shift of economic power to China, India, Russia, Brazil and the Middle Eastern countries could impact upon the UK’s role as an international financial centre.

The diagram below sets out three possible scenarios for retail financial services based on these drivers:

- Scenario W1: “Business as usual,” in which the UK remains a light-touch jurisdiction for regulation and the pace of globalisation is slow, maintaining London’s position as a global financial centre;
- Scenario W2: “Sustainable global finance,” characterised by moderate regulation that is at a level consistent with other jurisdictions. The pace of globalisation means London loses some market share as a financial centre, but its position remains supported by strong infrastructure;
- Scenario W3: “Shift to the East” in which regulations are more restrictive than other jurisdictions and the pace of globalisation accelerates a shift of wholesale business to financial centres in the developing economies.

Figure 56: Summary of wholesale scenarios



Source: PwC analysis

7.4.1 Wholesale scenario 1: “Business as usual”

Under this scenario – which offers the most positive growth of the wholesale scenarios – many proposed regulations are not introduced, or those that are introduced fail to keep up with product and service innovation. The pace at which economic power shifts to developing countries is such that UK wholesale financial services continue to benefit from globalisation and business does not shift to other jurisdictions. London remains pre-eminent as a global financial centre due to its light-touch regulation and there is a high degree of financial innovation, which leads to strong growth. The emphasis is on short-term profitability and the management of risk is considered subordinate to growth and profitability. Another market correction – if one hasn’t occurred already – is a real possibility.

Regulatory features of this scenario might include:

- failure by government to make proposed regulatory changes due to industry lobbying, resulting in relatively light-touch regulation compared with other jurisdictions;
- watering down of Solvency II and AIFM Directive;
- no increase in banks’ capital requirements;
- no changes to remuneration policy; and
- repeal of 50 per cent marginal income tax rate.

This scenario results in growth for all subsectors of financial services, but asset management in particular due to the high operational leverage and virtuous cycle it experiences when asset markets grow.

Table 18: Sector-specific implications of scenario

	Description	Industry output (Illustrative)
Banking	•Wholesale banks continue to develop innovative products as they did before the recession. While they might not return to the products which caused products in the past, their appetite for risk returns to high levels	
Insurance	•Solvency II is continually challenged and amended, fails to achieve its original aspirations, and does not impact insurers as heavily as initially predicted •Low levels of regulation allows insurers to pursue risky but profitable policies. Some insurers lose out when events strike due to insufficient capital protection, but others take the opportunity to charge even higher premiums •Lloyd’s remains the primary destination for institutions looking to insure against unusual or complex risks. It attracts risks from developing markets	
Asset management	•Light regulation, low taxes and flexible remuneration arrangements make London an attractive place to domicile •Asset managers are able to realise high growth through complex and innovative, but risky, products	

Source: PwC analysis

Under this scenario, employment is volatile due to the less stable nature of market growth. However, the emphasis on efficiency is somewhat lower in this scenario than the others as revenue growth means that profit margins are more easily restored. There is particular need for employees with advanced quantitative skills to develop and administer new products and employees with strong interpersonal and relationship skills to sell them. There is less need for risk and compliance staff than under higher-regulation scenarios.

7.4.2 Wholesale scenario 2: “Sustainable global finance”

Under this scenario, the Government institutes effective regulation which is considered appropriate and stabilises the sector and reduces what are irresponsible practices. This regulation is in line with that in other jurisdictions. There is greater government scrutiny of financial services institutions and communication between regulators and firms in the sector increases. Risk management becomes a key strategic priority as a result. Continued innovation by the industry enables growth to continue, albeit at a rate slower than before the financial crisis. The shift of economic power to the developing economies means that London loses some market share to emerging financial centres, but the regulatory framework and advanced infrastructure mean that London continues to benefit from increased global capital flows. Growth lies somewhere between the other wholesale scenarios, but is considered more sustainable. We consider this scenario to be the most likely approximation of the state of the industry in 2020.

Regulatory features of this scenario might include:

- regulation in line with that of other jurisdictions;
- increased capital requirements for banks and insurers;
- regulations, such as Solvency II for insurers, that require greater emphasis on risk management; and
- remuneration policies aligned with long-term institutional performance.

This scenario results in more modest growth than previously for most subsectors, although high-risk lines of business similar to those ones which induced the financial crisis do not return.

Table 19: Sector-specific implications of scenario

	Description	Industry output (Illustrative)
Banking	<ul style="list-style-type: none"> •Higher capital requirements reduce banks' profitability •Lower reliance on trading risky products, including certain types of derivatives •Significant investment in control systems to track sophisticated products 	↓
Insurance	<ul style="list-style-type: none"> •Higher capital requirements reduce insurers' profitability •The London market attracts business from developing markets 	↔
Asset management	<ul style="list-style-type: none"> •Traditional asset managers enjoy modest investment growth •Many Alternative investment managers continue to relocate to lighter-regulation jurisdictions, such as Switzerland 	↓

Source: PwC analysis

Under this scenario, employment is more stable and predictable due to the increased regulation. It is likely to be lower than 2007 levels. There is still a need for employees with advanced quantitative skills to develop and administer new products and employees with strong interpersonal and relationship skills to sell them, although the need is lower than in Scenario 1 due to the narrower portfolio of products on offer. Institutions invest in risk management and compliance employees, while improved control systems result in higher demand for specialist IT expertise. Finally, the shift of economic power to developing countries increases the need for foreign language skills in London more than in any other scenario.

7.4.3 Wholesale scenario 3: “Shift to the East”

Under this scenario, the wholesale financial sector contracts significantly. The combination of stricter regulation than elsewhere and a rapid shift of economic power to the developing world make this the most pessimistic scenario for employment. Mobile financial services companies leave the UK, while those that remain struggle to adapt. Strict regulation places limits on the products and services they can offer and growth through innovation becomes challenging. Meanwhile, other financial centres serving the needs of developing countries capture market share. London's position as a leading financial centre begins to decline and capacity develops rapidly in Asia and elsewhere.

Regulatory features of this scenario might include:

- regulations at least as stringent as those in Scenario W2 which are more onerous than those of other jurisdictions;
- limits on remuneration; and
- high taxes to fund government debt, including a tax on financial transactions and a 50 per cent marginal income tax rate for top earners.

This scenario is particularly detrimental to the UK asset management and wholesale banking sectors as companies are highly mobile, and are able to shift operations to other geographies. Insurance fares slightly better due to the less volatile nature of demand and the overwhelming advantage London already has in this industry in the form of Lloyd's (although its competitive advantage is eroded).

Table 20: Sector-specific implications of scenario

	Description	Industry output (Illustrative)
Banking	<ul style="list-style-type: none"> •New European directives such as new higher capital adequacy ratios and the regulations brought forward through Basel II Pillar 3, or possibly the introduction of a new Basel III accord, lead to significantly reduced profitability levels for banks •Withdrawal from derivatives trading and other risky activities •Investment banking activities severely curtailed •Remuneration policies prevent banks from offering the pay they once did and the sector becomes less attractive to top job candidates 	
Insurance	<ul style="list-style-type: none"> •Higher capital requirements reduce insurers' profitability •Insurance market is protected somewhat by presence of Lloyd's, but business is lost to other offshore centres as stringent regulations impair the markets' underwriting capabilities 	
Asset management	<ul style="list-style-type: none"> •Investment managers mostly relocate to other jurisdictions as the level of regulation makes London uncompetitive 	

Source: PwC analysis

Under this scenario, employment declines significantly, and wholesale financial service institutions must cut costs as much as possible. The required skill set shifts firmly towards regulation and compliance, as the back and middle-offices become relatively more important. Paradoxically, skills shortages may increase as financial services becomes a less attractive career option due to lower rewards and a decline in London's ability to attract the highest-quality candidates.

7.5 Overall implications for employment and skills in 2020

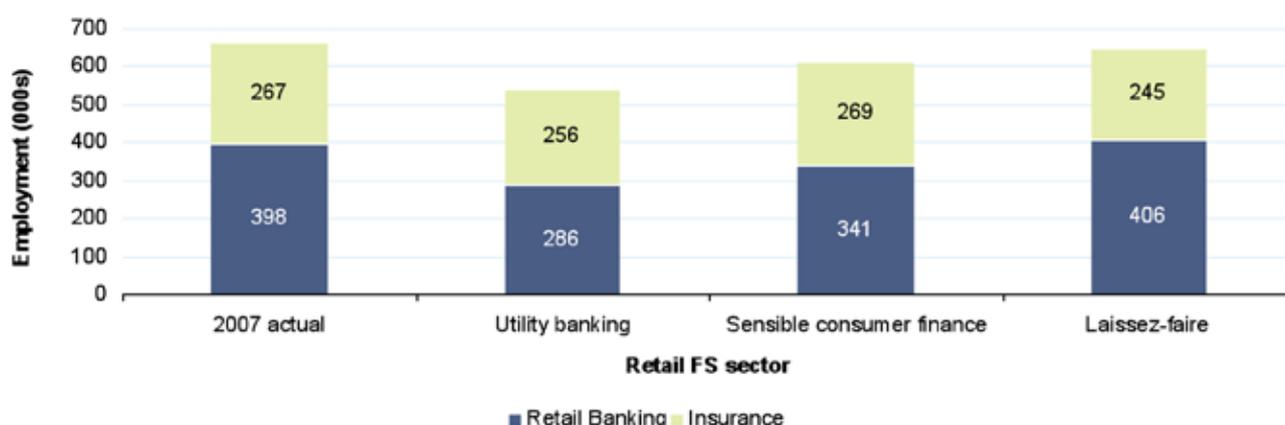
In this section we discuss the implications for employment and skills of the scenarios and our conclusions for employment and skills. Although we have considered the retail and wholesale scenarios separately, for the purposes of illustration, we have calculated the employment implications together: We have assumed that together, the worst case scenarios result in a 25 per cent contraction in overall employment (230,000 employees), the middle cases in a 10 per cent decline (94,000 employees) and the best cases in a 5 per cent increase (46,000 employees). We have then considered the relative volatility and size of the individual sectors to determine the change in sectoral employment.

In the scenarios where employment declines, we would expect general skills shortages and gaps to decline as employers face less competition as they draw from the talent pool. However, skills shortages and gaps are unlikely to disappear altogether.

7.5.1 Employment in retail financial services

In all our scenarios, employment declines compared to 2007, as shown in the chart below. The sustainable finance scenario is somewhat more favourable for insurance than the other two scenarios. Retail banking employment increases in the “Laissez Faire” scenario, but this assumes that the economy does not experience another downturn between now and 2020. Depending on if and when a downturn occurs, employment could actually be significantly lower than current employment under this scenario.

Figure 57: Retail financial services employment under 3 scenarios



Source: PwC analysis

Table 21 illustrates the impact on employment across the retail subsectors of the scenarios. Retail insurance does not always follow the same trends as retail banking due to differing drivers of demand and overall employment is more stable.

Table 21: Illustrative employment assumptions of retail scenarios

	2007	“Utility financial services”	“Sustainable consumer finance”	“Laissez faire”
Banking (000s)	398	286 Assume employment declines by c.28% due to need for aggressive cost cutting	341 Assume employment declines by c.14%, due to efficiency gains and reduced consumer demand for financial products	406 Employment falls for the next few years. By 2020, employment reaches 2007 levels, but this level is highly volatile. There is not the same impetus for efficiency improvements as under the other scenarios. However, retail banks are more reluctant than wholesale ones to put back costs taken out as a result of the crisis - hence little employment growth
Insurance (000s)	267	256 Employment is less volatile than banking. Assume employment declines by c.4%	269 Assume employment remains largely flat. Increased demand for insurance products due to fiscal conservatism among consumers is offset by efficiency gains	245 Assume employment continues to decline as it has historically. Employment is c.8% lower in 2020

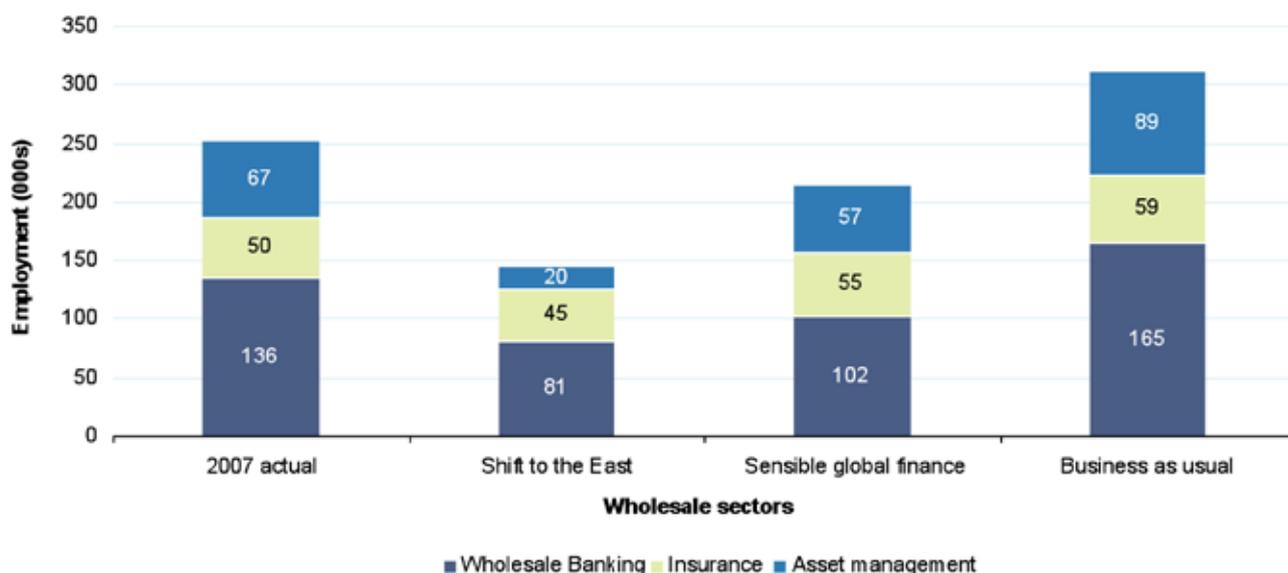
Source: PwC analysis

Note: Scenario employment numbers are rounded

7.5.2 Employment in wholesale financial services

The chart below shows that the wholesale sectors demonstrate more volatility in employment between the scenarios than the retail sectors. Employment increases in the “Business As Usual” scenario, but this assumes that the economy does not experience another downturn between now in 2020. Depending on if and when a downturn occurs, employment could actually be significantly lower than current employment under this scenario.

Figure 58: Wholesale financial services employment under 3 scenarios



Source: PwC analysis

Table 22 illustrates the impact on employment across the wholesale subsectors of each scenario. Employment in wholesale financial services is generally more volatile than retail financial services, with asset management generally the most volatile sector (output is dependent on stock market performance), followed by wholesale banking. Insurance does not always follow the same trends due to differing drivers of demand and overall employment is more stable.

Table 22: Illustrative employment assumptions of scenarios

	2007	“Utility financial services”	“Sustainable consumer finance”	“Laissez faire”
Banking (000s)	136	81 Assume 40% of employment is lost as significant proportions of wholesale banking disappear and there is another aggressive round of cost-cutting	102 Assume c.24% of employment is lost due to restrictions on products and innovation	165 Employment falls for the next few years. By 2020, employment is c.22% higher than in 2007, but this level is highly volatile.
Insurance (000s)	267	45 Assume employment falls by c.10% due to London’s decline as a financial centre	55 Assume employment grows by c.11% due to increased global demand for insurance products and London’s ability to service that demand	59 Employment not as dramatically impacted by crisis as other wholesale sectors. Assume employment grows by c.17% to 2020 due to increased global demand for insurance products and London’s ability to service that demand better than other markets
	67	20 Assume c.70% of employment is lost as most asset managers move abroad	57 Assume all hedge fund business is lost, but other businesses remain. Employment falls by 14%	89 Employment falls for the next few years. By 2020, employment is c.32% higher than in 2007, but this level is highly volatile

Source: PwC analysis

Note: Scenario employment numbers are rounded

7.6 Occupational impact of scenarios

We developed separate scenarios for the retail and wholesale sectors due to the differing drivers of these sectors. However, to understand change in the mix of employees within financial services, we have had to consolidate the retail and wholesale scenarios due to limitations with the occupational data, which is only available for the financial services sector as a whole and is not segmented by activity (banking/insurance/asset management) or market (retail/wholesale). We have paired retail scenario 1 with wholesale scenario 1 (Utility Financial Services and Shift to the East); retail scenario 2 with wholesale scenario 2 (Sustainable Consumer Finance and Sustainable Global Finance); and retail scenario 3 with wholesale scenario 3 (Laissez Faire and Business as Usual). These are illustrative and other combinations could of course exist.

Given the top-line changes in employment for each scenario, we have estimated the impact on the major job categories in financial services: managers and senior officials; professional occupations; association professional and technical occupations; administrative and secretarial occupations; sales and customer service occupations. Together, these occupational groupings account for the overwhelming majority of employment in financial services; a detailed list of the occupations included in these categories is available in Annex A.

The numbers emerging from this exercise, outlined in Table 23, tell only part of the employment and skills story. The occupational categories are necessarily broad and include employees from a wide range of functions within financial institutions. Therefore, overall trends will conceal some differences in the prospects for individual roles.

Table 23: Summary of occupational implications across all three scenarios

Scenario	Growth scenario ("Laissez faire" and "Business as usual")				Moderate scenario ("Sustainable con- sumer finance" and "Sustainable global finance"		Low growth/contraction ("Utility banking" and "Shift to the East")	
Occupations	Number of employees in 2008 (000s)	% of sector employment	Number of employees in 2020 (000s)	% of sector employment	Number of employ- ees in 2020 (000s)	% of sector employ- ment	Number of em- ployees in 2020 (000s)	% of sector employment
Managers and senior officials	344	28%	368	29%	328	30%	243	26%
Professional occupations	115	9%	123	10%	99	9%	92	10%
Associate professional and technical occupations	310	25%	355	28%	296	27%	220	24%
Administrative and secre- tarial occupa- tions	336	27%	287	22%	274	25%	281	30%
Sales and customer service oc- cupations	107	9%	138	11%	93	8%	72	8%
Other	19	2%	19	1%	19	2%	19	2%
Total	1,211		1,272		1,090		909	

Source: UKCES Almanac; PwC analysis

Managers and senior officials

This employment category includes managers across all functions within financial services in the front, middle and back office. Due to operational leverage – in which a manager is responsible for several more junior staff – we have assumed that demand for employees in this category is somewhat less volatile than it is for the other employment categories, although it is not as stable as the professional occupations category. This category of employees will be responsible for taking the lead in establishing a new culture of risk awareness and compliance.

Professional occupations

This group includes accountants, actuaries and IT professionals. Most of the people in this category work in back- and middle-office control and support positions. Therefore, the category is likely to be less volatile than the others as it includes many of the essential control functions which are difficult to dispense with. Under higher-regulation scenarios (“Utility Banking”/“Shift to the East” and “Sensible Consumer Finance”/“Sensible Global Finance”), we would expect employment in this category to perform relatively well as the need for risk management and compliance functions expands – there will be a greater requirement for actuaries in insurance companies and accountants in banks. However, if overall demand in some segments of financial services falls, it is likely that the need for these positions would decline as well (although their share of employment would increase).

Associate professionals and technical occupations

This segment includes people junior to the professional staff, but also many of the front-office workers in the wholesale financial services sector, including brokers, insurance underwriters, investment analysts, sales representative and marketing professionals. Although it is likely to include some risk management and compliance staff, the relative weighting towards front office means it is likely to be the most volatile of the five categories. In a low-growth or contracting environment (“Utility Banking”/“Shift to the East”), demand for these positions would fall dramatically; in an environment of heady growth, we would expect to see a significant share of employment gains here.

Administrative and secretarial occupations

This category includes lower-skilled employees, mostly in the back office. Back-office occupations include credit controllers, clerks, book keepers, record clerks and database assistants; front office positions include counter clerks and telephonists. This segment is likely to be less volatile than the rest, and could benefit from an increase in compliance and reporting. However, the overriding trend towards increasing automation and outsourcing means that this category of employment is likely to decline under all of the scenarios.

Sales and customer service occupations

This category mostly applies to retail financial services and includes call centre workers. We have assumed this occupational group to be volatile, second to associate professional and technical occupations because employment in retail financial services are generally less unstable than employment in wholesale financial services. In a future where financial products are tightly controlled and consumers have a low appetite for risk (“Utility Banking”/“Shift to the East”), it is likely that demand for these roles would decline. The category is also negatively impacted by increasing automation and technical advancements.

Employment in this category is likely to be significantly impacted by the RDR, which could encourage many IFAs to leave the market. However, demand for the financial advisers recommended by the Thoresen review would increase the number of these roles (although these workers may not be captured by official statistics as third-sector organisations are categorised separately from financial services by the Office for National Statistics).

Financial services employs c.4 per cent of the UK workforce, or between 1m and 1.2m people. The industry is highly productive, generating GVA per head in excess of £100,000, more than double the UK average. The sector is highly developed in the UK compared with other countries and London has become a leading centre for international finance, due in part to critical mass of trade, strong institutions and strong supporting infrastructure. However, the outlook for the sector has changed significantly as a result of the credit crunch and ensuing financial crisis; much debate is underway nationally and internationally regarding the right type of regulation for the sector, particularly in investment banking.

More than any other sector, employment in financial services has come under a great deal of pressure in the current difficult economic environment. Anecdotal evidence suggests that total employment may have declined between 5 per cent and 10 per cent since it peaked in 2007. It is unlikely that the full impact of the financial crisis has yet been felt, so there may be more job losses to come. As this report is being written, the UK is the midst of a debate about banking remuneration and the behaviours it should be designed to encourage.

Our research has shown that there are persistent skills deficits in financial services, although these are more pronounced in certain subsectors than others.

- Retail financial services generally suffer greater skills gaps and shortages than wholesale financial services. Financial services companies providing wholesale services have historically offered very generous remuneration packages, enabling them to attract the brightest people. Retail financial services, which generally require lower level qualifications and where a significant share of employees are school-leavers, does not enjoy the same attractiveness relative to competing sectors such as high-street retail;
- Insurance, in both the retail and wholesale markets, has been less attractive to high-quality candidates than banking. In the wholesale market, there is a remuneration disparity with other financial services companies, in particular investment banks.

There are shortages and gaps in both generic and sector-specific skills, as outlined in Table 24. It is worth noting that:

- entry-level candidates for retail financial services jobs often lack the basic numeracy and “people” skills required;
- there is a shortage of management and leadership skills across the sector; and
- there are also sector-specific shortages, even for highly-skilled, well-paid jobs. For instance, there is an acute shortage of actuaries in the insurance industry. Investment banks have also noted a difficulty in recruiting UK graduates with sufficiently advanced mathematics skills, although they are generally able to source appropriate people from abroad.

Table 24: Summary of identified skills gaps and shortages in financial services

Subsector	Retail Banking	Wholesale Bank- ing	Retail I nsurance	Wholesale Insurance	Asset Management
Estimated direct employment in 2007	398,000	136,000	267,000	50,000	67,000
Specific skills gaps and shortages	Sales and customer service roles (NQF Level 1 - 3) Retail Bank Managers (NQF Level 4)	Professional & technical staff (NQF Level 5) - time lag between new specialisms being created and individuals having the necessary skills. Managers and Senior Officials (NQF Level 6)	Actuaries (NQF Level 5) Specialist under-writers (NQF Level 5) Compliance Staff (NQF Level 5) Claims professionals (NQF Level 3) IT and Legal Staff (NQF Level 3)	Actuaries (NQF Level 5) Risk managers (NQF Level 5) Capital modelling (NQF Level 5) Accountants (NQF Level 7) Internal auditors (NQF Level 7) Price reserving Lloyd's Exam Brokers	Professional and technical staff (NQF Level 6) Compliance roles (NQF Level 5) Experience of derivatives and structured products Back office roles
Generic skills gaps and shortages	Management and leadership skills Self motivation and direction Industry knowledge Numeracy & literacy Understanding client needs	Product and industry knowledge Managerial 'soft skills' - ability to cope with stress and positive management of staff relationships. Complex mathematics / statistics	Industry and product knowledge Self motivation and direction Management and leadership skills	Management and leadership skills IT skills Numeracy Business language	Technical and product knowledge Management and leadership skills IT skills Positive management of staff relationships

Source: PwC analysis

8. Conclusions

We have developed a series of scenarios which illustrate a set of possible future states of the retail and wholesale financial services sectors. In most of our scenarios, employment in financial services declines due to tighter regulation, a shift in consumer demand towards saving rather than credit and a gradual loss of wholesale market share relative to other global financial centres. Most of the scenarios, supported by our research and interviews, suggest that overall employment is unlikely to return to 2007 levels in the next decade. Specifically:

- wholesale financial services positions are the most volatile, particularly those in investment banking and asset management. Employment is dependent on London's position as a global financial centre and there is an argument that this will be gradually eroded between now and 2020 as trade and capital shift to emerging economies;
- employment in retail banking and insurance is less volatile, but as these sectors comprise the majority of financial services employment, a small percentage decline would still result in significant job losses.

Whichever scenario emerges, it is likely that the distribution of jobs along the financial services value chain³²⁷ will change. We expect the shift towards higher-value, higher-skilled jobs we have seen in the UK to continue as certain functions are moved abroad or automated.

- Efficiency is likely to be paramount in retail financial services companies as they look towards recovery and the need to restore margins and profitability. There will be continuing job losses due to branch closures and a move towards more efficient distribution channels (phone and internet), negatively impacting front office employment;
- Globalisation and technology advances have enabled financial services companies to fragment their activities geographically to achieve cost savings. Significant proportions of the back office have been exported to developing economies such as India and we expect this trend to continue;
- Increasingly, client-facing front-office functions, for example in wholesale banking, will be established close to international clients, but there is likely to remain a significant body of clients in London who will need to be serviced from London. Middle-office functions such as product origination are also likely to remain close to the main financial exchanges, as are the associated monitoring and control functions;
- There is likely to be a significant change in the provision of personal financial advice as a result of the RDR. New regulations will mean many IFAs leave the market and encourage insurance and asset management companies to develop alternative sales channels.

³²⁷ The value chain comprises the front office (customer-facing) and middle and back offices (support)

In the next decade, there are likely to be many changes in the type of skills needed by the financial services industry. New roles will be created and existing roles modified or expanded. Most of the impact will be on the jobs that already exist; employees working at all levels in financial services organisations will need these skills in the new environment.

- Risk management and compliance skills, driven by greater regulation of financial services companies (both wholesale and retail) and demand for transparency among stakeholders. The need will be strongest in banks, which are likely to experience the greatest change in regulation, but insurance companies will not be exempt. While the number of risk management and compliance specialists may increase in the middle-office, a new attitude towards and greater awareness of risk will need to permeate financial services companies;
- Product knowledge and advice skills. The Thoresen review recommends establishing a free generic financial advice service targeted at less affluent customers which would impact the need for these skills in the third sector;
- In the wholesale sector, it is widely recognised that many financial services companies did not understand the risks associated with the complicated products they were buying and selling. While the effect will be most strongly felt by front-office staff, the need for better understanding will span all areas of financial services companies – middle-office staff and board members cannot control and assess the risk of front-office activities without fully understanding the products.

The government has a critical role to play in managing the sector in the medium-term and is currently formulating its response to the crisis, both in terms of regulation and remuneration and in terms of its role in supporting banks as a shareholder or a lender of last resort. The government's response will shape not only the structure of the sector and its competitiveness, but ultimately will impact upon levels of employment and the types of skills that will be required.

Annex A: Occupations in the financial services sector

Managers and Senior Officials	<ul style="list-style-type: none"> • Directors and chief executives of major [financial] organisations • Financial managers and chartered secretaries • Marketing and sales managers • Advertising and public relations managers • Personnel, training and industrial relations managers • Information and communication technology managers • Research & development managers • Quality assurance managers • Customer care managers • Financial institution managers • Office managers
Professional occupations	<ul style="list-style-type: none"> • Fund managers • IT strategy and planning professionals • Software professionals • Chartered and certified accountants • Management accountants • Management consultants, Actuaries, Economists and Statisticians
Associate professionals and technical occupations	<ul style="list-style-type: none"> • IT operations & user support technicians • Estimators, valuers and assessors • Brokers • Insurance underwriters • Finance and investment analysts/advisers • Taxation experts • Commodity importers/exporters • Financial and accounting technicians • Business and related associate professionals • Sales representatives • Marketing associate professionals
Administrative & secretarial occupations	<ul style="list-style-type: none"> • Credit controllers • Accounts and wage clerks, book-keepers, other financial clerks • Counter clerks • Personal assistants and other secretaries • Receptionists • Typists • Filing and other records assistants/clerks • Pensions and insurance clerks • Database assistants/clerks • Telephonists
Sales & customer service occupations	<ul style="list-style-type: none"> • Sales and retail assistants • Retail cashiers and check-out operators • Telephone salespersons • Collector salespersons and credit agents • Call centre agents/operators • Customer care occupations

Annex B: The National Qualifications Framework

National Qualifications Framework (NQF)		Framework for Higher Education Qualifications (FHEQ)
Previous levels (and examples)	Current levels (and examples)	
5 Level 5 NVQ in Construction Management	8 Specialist awards	D (doctoral) Doctorates
Level 5 Diploma in Translation	7 Level Diploma in Translation	M (masters) Masters degrees, postgraduate certificates and diplomas
4 Level 4 NVQ in Advice and Guidance (1)	6 Level 4 National Diploma in Professional Production Skills	H (honours) Bachelor degrees, graduate certificates and diplomas
Level 4 National Diploma in Professional Production Skills	5 Level 5 BTEC Higher National Diploma in 3D Design	I (intermediate) Diplomas of higher education and further education, foundation degrees and higher national diplomas
Level 4 BTEC Higher National Diploma 3D Design	4 Level 4 Certificate in Early Years	C (certificate) Certificated of higher education
Level 4 Certificate I Early Years		
3 Level 3 Certificate I Small Animal Care		
Level NVQ in Aeronautical Engineering		
A Levels		
2 Level 2 Diploma for Beauty Specialists		
Level 2 NVQ in Agriculture Crop Production		
GCSEs Grades A*-C		
1 Level 1 Certificate in Motor Vehicle Studies		
Level 1 NVQ in Bakery		
GCSEs Grades D-G		
Entry Entry Level Certificate in Adult Literacy		

Annex C: Glossary

Term	Definition
ABI	Association of British Insurers
AIFM	Alternative Investment Fund Managers (Directive)
APE	Annual premium equivalent
CAGR	Compound annual growth rate
CBI	Confederation of British Industry
CeFA	Certificate for Financial Advisers
CEO	Chief executive officer
CFA	Chartered Financial Analyst
CII	Chartered Insurance Institute
CIOBS	Chartered Institute of Bankers in Scotland
CISI	Chartered Institute for Securities & Investment
CRM	Client relationship manager
DFSM	Diploma in Financial Services Management
FSA	Financial Services Authority
FSSC	Financial Services Skills Council
GCSE	General Certificate of Secondary Education
GDP	Gross domestic product
GFCI	Global Financial Centres Index
GVA	Gross value added
IFA	Independent Financial Adviser
IFS	Institute for Fiscal Studies
IFSL	International Financial Services, London
IMA	Investment Management Association
IPO	Initial public offering
IT	Information technology
LFS	Labour Force Survey
Term	Definition
M&A	Mergers & acquisitions
NESS	National Employer Skills Survey
NQF	National Qualifications Framework
NVQ	National Vocational Qualification
OEIC	Open-ended investment company
ONS	Office for National Statistics
OTC	Over-the-counter (derivatives)
PwC	PricewaterhouseCoopers
RBS	Royal Bank of Scotland
RDR	Retail Distribution Review
SIC	Standard Industrial Classification
SII	Securities & Investment Institute (now CISI)
SME	Small and medium enterprise

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