THE
INVESTMENT
ASSOCIATION

Response to consultation

FCA DP22/5: THE POTENTIAL COMPETITION IMPACTS OF BIG TECH ENTRY AND EXPANSION IN RETAIL FINANCIAL SERVICES

About the Investment Association

The IA champions UK investment management, supporting British savers, investors and businesses. Our 250 members range from smaller, specialist UK firms to European and global investment managers with a UK base and manage £10 trillion of assets. The investment management industry supports 122,000 jobs across the UK. Our mission is to make investment better. Better for clients, so they achieve their financial goals. Better for companies, so they get the capital they need to grow. And better for the economy, so everyone prospers.

Our purpose is to ensure investment managers are in the best possible position to:

- Build people's resilience to financial adversity
- Help people achieve their financial aspirations
- Enable people to maintain a decent standard of living as they grow older
- Contribute to economic growth through the efficient allocation of capital

The money our members manage is in a wide variety of investment vehicles including authorised investment funds, pension funds and stocks and shares ISAs. The UK is the second largest investment management centre in the world, after the US and manages over a third (37%) of all assets managed in Europe.

Executive summary

New entrants to any market, regardless of their background, can be an important source of innovative ideas. However, there are areas in which some Big Tech firms may be able to act that is not necessarily in the best interest of consumers or would uphold a healthily competitive environment and so the regulatory authorities must be prepared to intervene where required.

The investment management sector is not one of those the FCA chose to analyse in its discussion paper, but nevertheless there are considerations and implications that arise from our analysis of how a Big Tech firm may seek to enter this particular market.

We find that the FCA's proposed analytical approach to assessing Big Tech entry and competition across financial services is broadly fit for purpose and that regulators should apply the following principles to its

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ongoing work in this area: continue to regulate the activity rather than the firm; be technology-neutral; apply a level playing field to all market participants.

The UK has become steadily less attractive for investment management, particularly as a location for domiciling funds, over recent years. This environment could either mean that Big Tech firms look elsewhere for easier market entrance opportunities, or conversely, it may mean that the scale they can offer may provide an opportunity for gaining market share quicker due to a lack of large competition.

General comments

Big Tech[1] firms play an important role in the investment management sector already from a service provision perspective, for example, in the provision of cloud services and other IT infrastructure. As we previously commented in our recent response to the PRA, Bank and FCA proposals[2], we are broadly supportive of the plans to enable regulators to designate some firms as 'critical third parties' (CTPs). In order to manage the international resilience of CTPs operating in multiple jurisdictions, international regulatory coordination is fundamental[3].

The involvement of Big Tech in devising and providing products and services to retail consumers is a different question however, and requires more careful consideration in allowing the market to develop fairly and with regard to consumer protection. Although the investment management sector was not one that you chose to analyse in your discussion, it is our view that the potential for paths similar to those you explored in the four selected sectors are likely to also apply to investment management.

In particular, we can see that Big Tech firms may want to utilise their extensive datasets, of both UK consumers and products, to play an indirect role via the distribution of funds through their networks and platforms. Over time, perhaps via a partnership or acquisition, they may wish to directly enter the product manufacturer route and offer some investment funds of a simple nature, perhaps index trackers.

It is important that the FCA works closely with the CMA and that both organisations are adequately resourced and knowledgeable on this subject. Equally it will be important to co-operate internationally with peers given the global nature and reach of Big Tech firms, and the possibility of regulatory arbitrage. There is effectively a live international experiment in progress as jurisdictions across the globe seek to establish effective protection mechanisms to their own markets and their consumers in different ways. We in the UK need to work with international partners, monitor developments in these locations and be able to adapt quickly to learn lessons of where and how bad outcomes arise, adopting others' approaches that work.

Answers to selected questions

Q1: In your opinion, will Big Tech firms in UK financial services follow a similar path to other countries? What factors would make the UK experience similar? Or what reasons may exist for Big Tech firms to look for new approaches in the UK?

Big Tech firms play an important role in the investment management sector already from a service provision perspective, and it is likely that they will, at some point, play a more direct role in future. The development of this role is likely to take an evolutionary route, starting perhaps with a role within the product distribution market before they would be able to play a more direct role of product manufacturer.

It is our view that the potential for paths similar to those you explored in the four selected sectors are likely to apply to investment management. This is due to the well-established nature of the sector and its highly regulated nature, as well as the various roles that a firm can play along the value chain. Aside from direct entry into the portfolio management services, there are areas of the industry that may be more suited to a Big Tech firm, such as utilising their datasets to help distribute, or compare products to consumers likely to

[1] We adopt the FCA's definition of this term throughout this response

[2] Bank of England, Prudential Regulation Authority and Financial Conduct Authority: *DP22/3 - Operational resilience-critical third parties to the UK financial sector* July 2022

[3] Investment Association: *Response to DP3/22* December 2022

want them. In time, there may be options for Big Tech firms to play a more direct role, but this will likely only occur as a result of an acquisition or significant partnership.

Of the four sectors looked at in detail in the discussion paper, the most relevant complementarities for investment management are deposit taking, insurance and payments. In the first case, deposit taking, as an extension of providing wallets or savings accounts, firms may offer investments into money-market or bond funds for longer-term deposits searching for higher yield (although this might not be such an opportunity in a high(er) interest rate environment than the recent past). In the second, insurance, there may be future opportunities to facilitate access to products that cater for an individual's long-term savings needs based upon the dataset that the firm had available, perhaps utilising the opportunities of open finance. In the third case, payments, firms with retail product distribution capabilities handle large volumes of payments and are likely to continue to see evolutions in payment options, again, most likely through partnership with fintech or other organisations.

Q2: Have we identified the right analytical approach to assessing Big Tech entry and competition?

We broadly agree that the analytical approach identified is fit for purpose. We agree with the FCA's previous, and consistent, assertion[4] that challenger firms are an important source of new ideas and innovation in existing markets. Disruption can bring benefits to established firms who otherwise may tend to be less attentive and innovative.

We have provided further specific feedback relating to our sector in other questions.

Q8: If Big Tech firms enter and expand in financial services, will they create new complementarities between markets or their activities that we have not identified?

The wide range of functions within the investment sector, outside of portfolio management, provide further opportunities for Big Tech firms to play an indirect role. They have significant access to a wide range of datapoints, specifically on individuals but also on investment products such as investment funds, that they will likely be able to use in distribution functions. This will only increase over time as the volume of available data, such as that able to be used in behavioural analytics, marketing and sales trends continues to grow.

In China a decade ago, Alibaba was able to utilise its retail client data by developing a money market fund that very quickly became the largest fund in the world. The Tianhong Yu'ebao Money Market Fund[5] (a joint venture between Tianhong Asset Management and Alibaba) amassed $211bn in assets under management and 370 million account holders[6] within four years as a result of the client base of Alipay (now Ant Financial Services Group), something that traditional firms could not effectively compete with. In response to risk concerns, the Chinese regulators imposed a cut in the links with the super app and major capital requirements which resulted in a subsequent drop in AUM. The super app now provides access to 28 other money market funds[7].

The potential rise of super apps is likely to become a key route for Big Tech firms to enter into new markets in providing a wide range of services across multiple sectors. There are potential issues that may arise from this and it will be important to evaluate app design features which may facilitate consumer harm in a similar way to the issues associated to the 'gamification' of trading via apps that the FCA has recently identified[8].

[4] FCA: *Approach to Competition* October 2018
[5] Tianhong Asset Management: *Yu'ebao Money Market Fund* Accessed December 2022
[6] Wall Street Journal: *Meet the Earth's Largest Money-Market Fund* 13 September 2017
[7] Fitch: *Regulatory Cap on Yu'e Bao May Affect Other Chinese Funds* 25 April 2021
[8] FCA: *Gaming trading: how trading apps could be engaging consumers for the worse* November 2022

Similarly, as open finance develops, it will be important to ensure that data sharing is reciprocated so that newly-participating financial services sectors are able to gain access to non-financial firms' data as well as vice-versa.

Q9: Will the ways in which Big Tech firms enter and compete in the UK financial services markets be significantly influenced by regulatory boundaries? Does this differ across the four sectors we have studied?

The UK has become steadily less attractive for investment management, particularly as a location for domiciling funds, over recent years. The UK remains the second largest investment management centre in the world, and it is the most outward facing, meaning that relative international competitiveness is a critical factor. Currently, existing UK-based investment firms are more likely to place business in other jurisdictions than towards a domestic market. The regulatory environment has a role to play in the assessment of the relative merits of the jurisdictions in which global firms seek to locate business. Looking solely at our sector, and in keeping with this trend, it may be more likely that Big Tech firms will choose to enter other markets sooner. Aside from other effects, this would have two highly relevant impacts for this discussion: it places UK consumers at a disadvantage and deprives them of potentially helpful products and services, and makes the UK a less innovative and competitive location.

On the other hand, it could be argued that the general lack of attractiveness described above, and rising levels of barriers to entry may come to favour larger firms. While it may be less attractive to set up in the UK as a new business, if you are a company with scale (or scale obtained via partnership or acquisition), you might be at a distinct advantage. There is a risk in this scenario that a firm may be able to scale up to a dominant market position or a monopoly relatively quickly. Similarly, regulatory developments such as the introduction of an open finance data-sharing framework, and the introduction of greater flexibility on financial advice services[9] may provide opportunities for Big Tech firms, in particular, to play facilitative roles in the investment management sector.

Ends

[9] FCA: *CP22/24: Broadening access to financial advice for mainstream investments* November 2022