Centre for Policy Studies

Retail Therapy

Making the case for wider share ownership

BY NICK KING

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Executive Summary

It is received wisdom that owning your own home is a good thing. Indeed, home ownership and the foundational pillar of a property-owning democracy have taken on near-mythical status in the UK's political discourse.

Underpinning this support for home ownership is the idea that having a stake in the property market counts for something. This is predicated on the idea that ownership matters for individuals, for communities and for our country as a whole – and has positive consequences on both an economic and social level.

It is absolutely right for politicians to focus on home ownership. But it is remarkable that they pay so little attention to ownership of other kinds and, in particular, the ownership of shares.

> **'Over the last 30 years, the proportion of UK shares held by UK residents has fallen consistently. The most recent statistics told us that the proportion of shares held by UK residents was just 12%, compared to more than 50% in the 1960s'**

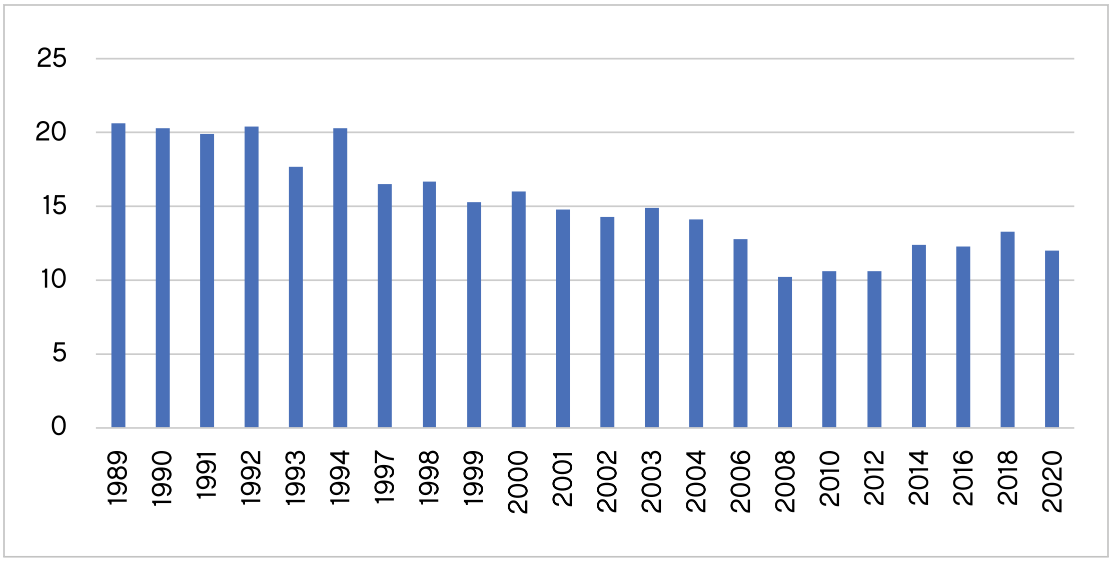
It is of course true that many of us own shares via institutional investors, in particular pension funds. The automatic enrolment of most employees into workplace pension schemes has seen a big increase in the number of UK citizens who have some exposure to the UK stock market.

But when it comes to retail investing – individuals actively choosing to invest their savings in the stock market – we are falling woefully short. And this has huge implications: for the financing of UK businesses, for the personal finances of the individuals concerned, and for public understanding and the wider reputation of the free-market system.

Over the last 30 years, the proportion of UK shares held by UK residents has fallen consistently. The most recent statistics told us that the proportion of shares held by UK residents was just 12%, compared to more than 50% in the 1960s.[1]

1 ONS, 'Ownership of UK Quoted Shares: 2020' (March 2022). Link

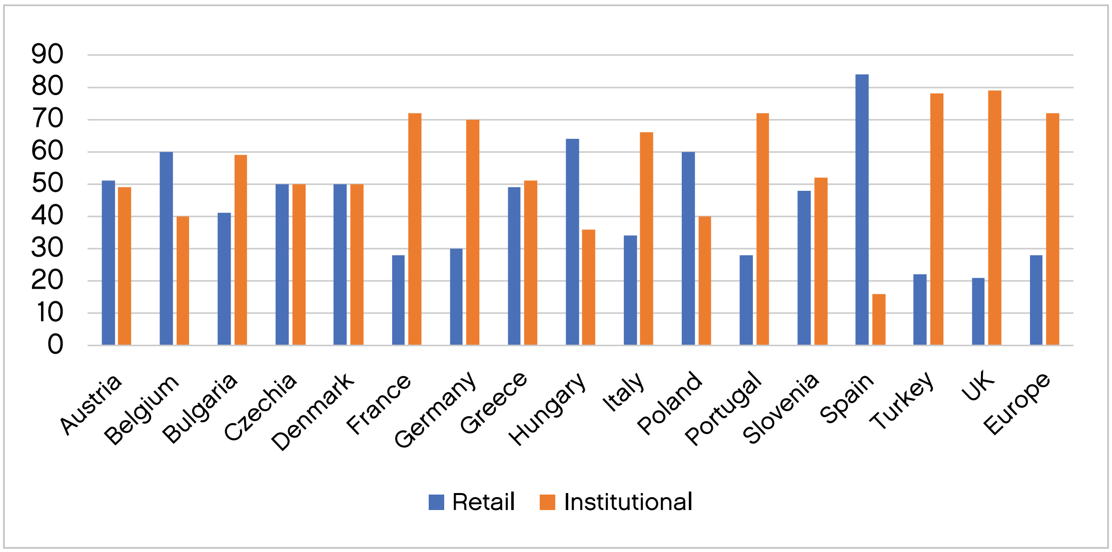
The percentage of UK equities owned by UK residents has fallen over recent decades



Source: ONS

Although international statistics are notoriously difficult to compare, the numbers suggest that the UK also has the lowest percentage of retail client money (compared to institutional client money) as 'assets under management' (AuM) of any European country. Whereas in Spain, retail investors make up 84% of AuM, in the UK it is just 21% (though the total under management is far higher in the UK).[2] Shares also make up a much smaller percentage of household assets.

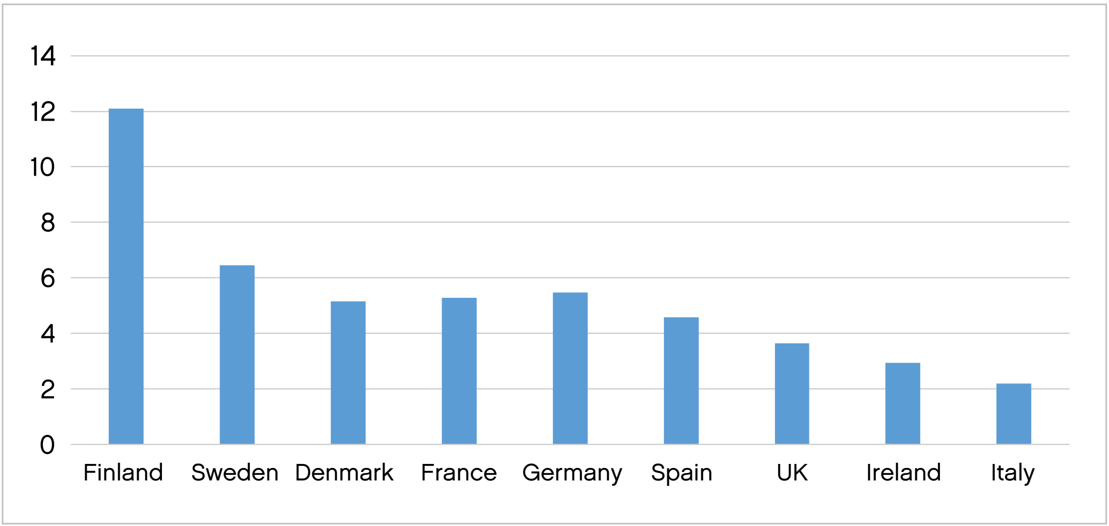
Retail vs institutional capital as a percentage of assets under management (end of 2022)



Source: EMAFA

2 EFAMA, 'Asset Management in Europe: An overview of the asset management industry' (December 2021). Link

Listed shares as a percentage of total household financial assets (2019)



Source: Eurostat

You might say that this doesn't matter much – surely it is better for people to entrust their cash to savvy investors who know what they are doing? But that is not what is happening.

The Financial Conduct Authority (FCA) believe that there are 9.7 million people with investable assets of over £10,000 in the UK, mostly or entirely in cash.[3] Of these, more than four million want to take some form of investment risk – but at the moment, due to high inflation, they are in fact losing money hand over fist.

At the moment, there is more than £200 billion invested in cash in National Savings and Investment Products.[4] More broadly, there is estimated to be £1.8 trillion of cash in savings accounts up and down the country.[5] Extraordinarily, the total sum of these savings is roughly equivalent to the total current market capitalisation of the FTSE 100, which at the end of June 2023 was just over £1.9 trillion.

Even among those taking advantage of the Individual Savings Account (ISA) scheme – who you might think would be savvier investors – the vast majority are parking their assets in cash, not shares. In fact, for each of the last 13 years bar one, there have been at least eight million Cash ISA subscriptions, and sometimes as many as 12 million. Taken together, the total holdings in Cash ISAs in the UK comes to just shy of £300 billion.[6] And the pattern of saving is hugely unequal. Those with the smallest savings are the most likely to take out Cash ISAs, and get the lowest returns – increasing wealth inequality significantly.

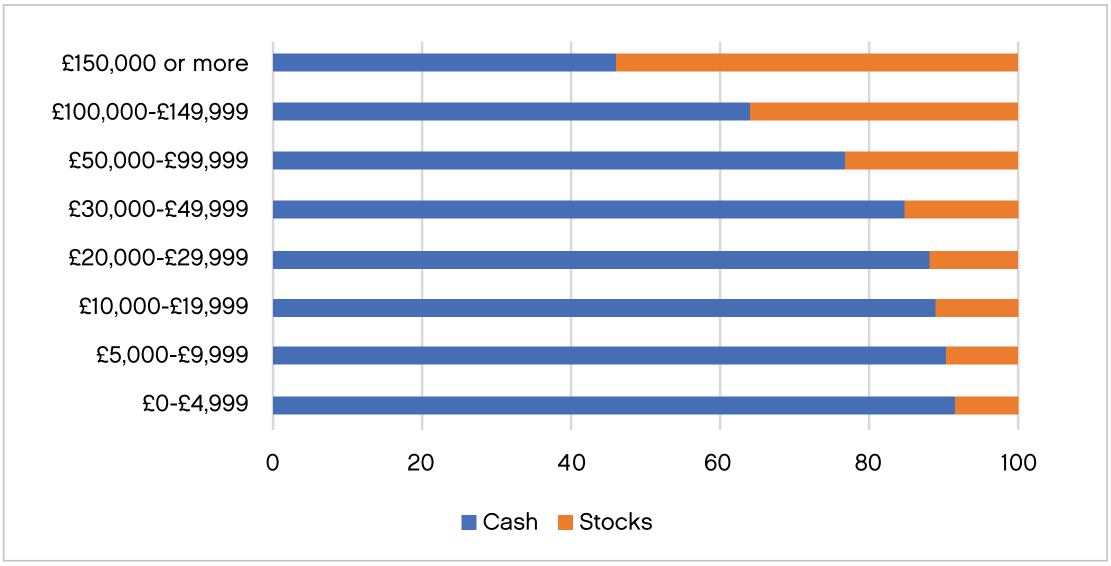
3 Financial Conduct Authority, 'Financial Lives survey 2022: insights on the vulnerability and financial resilience relevant to the rising cost of living' (October 2022). Link

4 National Savings & Investment, 'NS&I Provisional Q3 2022-23 Results and 2023-24 Net Financing Target, (March 2023)'. Link

5 Jim Armitage, The Times, 'Middle England is rolling in cash – but will people spend it?' (February 2023). Link

6 HMRC, 'Annual Savings Statistics 2022' (June 2022). Link

ISA type as percentage of total, by income bracket (2021)



Source: HMRC

Britain's neglect of retail investing is surprising in both practical and ideological terms.

In practical terms, incentivising more retail investors, and encouraging more retail investment, should increase the amount of deployable capital available across the UK economy. It should help individual companies achieve their full potential, support economic growth at a national level and, in turn and in time, reward those who have made those investments. In a 2017 paper for the Centre for Policy Studies (CPS) on the retail bond market, Rishi Sunak pointed out that 55% of the US population was then invested in the stock market, vs just 19% of Britons. 'That division,' he said, 'represents a vast store of underworked capital.'[7] Little has changed since then; recent statistics from UK Finance suggest that 10.6% of UK household financial assets are currently held in equity, compared to 36.2% of US households.

Moreover, thanks to modern technology and the growth of investment apps the barriers to entry are historically low – certainly when compared to buying property.

The ideological arguments are equally strong. Retail investing can be rewarding on an individual level, in terms of self-actualisation and self-worth. But it also gives people an opportunity to shape the companies they invest in – to literally become an owner, which includes the right to vote on corporate pay, environmental issues and governance. More retail investment gives people a stake in the society and the economy of which they are part.

That opportunity and potential were firmly understood by Margaret Thatcher and her fellow ministers (encouraged by CPS authors of the time).[8] Their push for privatisation was principally about efficiency and good governance – but it also provided an opportunity to widen ownership of well-known British companies to the public.

Through initiatives like the 'Tell Sid' campaign, a new cadre of retail investors was born – with the ambition to create a share-owning democracy existing alongside a

7 Rishi Sunak MP, 'A New Era for Retail Bonds', Centre for Policy Studies (November 2017). Link

8 E.g. See Shirley Robin Letwin and William Letwin, 'Every Adult A Share Owner: The Case for Universal Share Ownership' (1986), and Sir Nicholas Goodison, 'Shares for All: Steps Towards a Share-owning Society' (1986)

property-owning one. In 1979, when Thatcher came into office, about three million people owned shares; by 1987 that had risen to eight million. The sale of British Gas alone resulted in an estimated two million people buying shares for the first time.[9]

However, the last 30 years have seen a huge decline in our ambitions around retail investing. Small tweaks have been made, for example turning Personal Equity Plans (PEPs) into Individual Savings Accounts (ISAs) or the reduction of the stamp duty payable on the trading of shares. But there has been no concerted effort made to encourage more individual investors by any of the political parties. No campaigns have been run, no major initiatives launched, no landmark new systems or structures created. Xavier Rolet, the former CEO of the London Stock Exchange, recently pointed out that: ‘At present, we have dividend tax, capital gains tax, income tax, and a transaction tax via stamp duty, of which the UK has the highest rate in all of Europe. The same pound of income from equities is taxed four times.’[10]

‘In 1979, when Thatcher came into office, about three million people owned shares; by 1987 that had risen to eight million’

And obvious opportunities to redress this have been missed. In recent years, the Government has been selling down its stake in NatWest (formerly the Royal Bank of Scotland), which it took on during the financial crisis. The sale of six blocks of shares since 2008 has reduced the Government’s stake from around 84% at its peak to 38.6% at the time of writing – yet none of those have been allocated for retail investors.[11]

There have, admittedly, been some attempts to recognise and address this situation of late. Lord Hill’s UK Listing Review had a chapter dedicated to retail investing.[12] Mark Austin’s Secondary Capital Raising Review was unapologetically on the side of the retail investor, calling for individual investors to be treated more equitably.[13]

Both of these reviews were warmly welcomed by the Treasury. The current Chancellor, Jeremy Hunt, announced the Edinburgh Reforms in December 2022, which were broad in range but included a consultation on an alternative, more retail investor friendly, framework for retail disclosure in the UK.[14]

The private sector is also doing its bit, with organisations like PrimaryBid and Peel Hunt’s REX platform looking to give individual investors new opportunities in an investing environment primarily designed by, and for, institutional players.

There has, in short, been a recognition that the pendulum has swung too far in favour of institutional investment and against the interests of individual investors. But more needs to be done. We need both to create more retail investors and unleash more retail investment – not least by ensuring retail investors are not put at a disadvantage compared to institutional investors.

9 House of Commons, ‘Research Paper 14/61: Privatisation’ (2014). Link
10 Interview with the Daily Telegraph (June 2023). Link
11 HM Treasury, ‘Government sells £1.26 billion of NatWest shares…’ (May 2023). Link
12 Lord Jonathan Hill, ‘UK Listing Review’ (March 2021). Link
13 Mark Austin, ‘UK Secondary Capital Raising Review’(July 2022). Link
14 HM Treasury, ‘PRIIPs and UK Retail Disclosure, A Consultation’ (December 2022). Link

There are obviously many routes to doing this – such as encouraging more retail access to corporate bonds (as recommended by the current Prime Minister in his CPS paper) and to private markets, especially in terms of exposure to private equity and venture capital opportunities. There is also a strong case for more employee share ownership. But this paper will focus on the opportunities presented by the public markets, and on making the case for more retail investing from first principles.

We will show that retail investing brings both economic and social benefits for individuals, for businesses and for the UK economy as a whole. We will then move on to consider what steps policymakers should take to encourage more retail investment. In particular, we will look at two broad areas which require particular attention.

‘We need both to create more retail investors and unleash more retail investment – not least by ensuring retail investors are not put at a disadvantage compared to institutional investors’

The first is around attitudes and awareness. As this report explain, current rules mean that many people don’t receive the advice or guidance they should when it comes to investment opportunities. But there is a more fundamental problem, which is that far too few people appreciate the investment opportunities which exist in the first place. For a multitude of reasons – including the opaque language of financial services and a lack of financial literacy on the part of many potential investors – many people think investing ‘is not for them’.

Some of these problems are linked to a wider issue around the risk tolerance of policymakers in this country – or rather, what they perceive to be an acceptable level of risk for its population. Too often, especially when compared to the property market, retail investment is considered to be a high-risk activity from which people might need protecting. The advice/guidance rules reflect this.

The second area which requires attention is around our systems and structures. Mark Austin pointed to some of the most egregious structural issues in his recent report into Secondary Capital Raising.[15] These obstacles should be dismantled as soon as possible. But the process around primary capital raising also needs reform so that Initial Public Offerings (IPOs) are actually worthy of their name. Far too many IPOs are not offered to members of the public – a trend which has been getting worse of late.

This report goes further in making two more ambitious recommendations.

The first is around ISA reform. Although there is a lot to be said for streamlining the number of ISAs on offer, the real opportunities lie in helping those who have Cash ISAs understand the opportunities which exist through Stocks and Shares ISAs. The report therefore calls for Cash ISAs and Stocks and Shares ISAs to be amalgamated. If the ISA holder wants to keep their money in cash, they can, but this conversion would help bring investment opportunities much closer to the millions of people who only hold Cash ISAs at the moment.

The second idea is around the creation of a new Government-backed fund which would either invest in a diversified portfolio of UK equities or track the FTSE index.

15 Mark Austin, ‘UK Secondary Capital Raising Review’ (July 2022). Link

Investment vehicles already exist to provide this function, of course - but they are clearly failing to reassure many would-be investors who are staying away from the market.

With Government both establishing and promoting this fund, it is hoped it will appeal to the millions of people with investable capital who hold most or all of it in cash and who are not tempted by the market solutions currently available.

There will be some who are not convinced of the economic case for more retail investors. Many institutional investors will argue that the investment impact – even if there are millions of new retail investors – cannot come close to their own.

But the key point here is that there are hundreds of billions of pounds of investable assets sitting in cash which could be put to better use. If invested into UK equities, that is money that could benefit individual investors, the companies they invest in and the economy as a whole. That would mean a material improvement in the economic lot of millions of people living in the UK.

But ultimately, retail investment is not just about economic impact. It is about the sort of economy we want to build, the sort of society we want to be part of – and the sorts of opportunities which ought to be the preserve of every man and woman in the land.

Summary of Recommendations:

1.	The Government should commission or produce a new Retail Investment Strategy. This Strategy should make the creation of more retail investors and unlocking more retail investment its explicit aim, looking to put retail investors on an equal footing with institutional investors. It should consider in particular how to encourage more private capital into public markets, given the economic and social benefits which this would unlock. And it should examine the tax treatment of retail investing and how it can be made more attractive.
2.	The Government and regulators should rethink the disclaimers around retail investing – and, more fundamentally, take a more realistic, and positive, attitude towards risk. The concept of personal responsibility in investing should be recognised and embraced, and the positive role which can be played by risk capital should be more readily supported.
3.	As part of this, rules around financial advice should be amended to avoid the disproportionate 'suitability requirements' which prevent many people from accessing advice from which they would benefit. The rules around financial advisers' liability should also be reconsidered in respect of the provision of 'bad advice' reflecting the wider emphasis on personal responsibility, and the dangers of simply leaving assets in cash.
4.	The Government, regulators, the London Stock Exchange and other interested parties should support a modern version of a 'Tell Sid' campaign, raising awareness of the opportunities provided by retail investing and helping to tackle the relatively low levels of retail investing from the UK public.

5.	A proportion of new equity offered through Initial Public Offerings should always be made available to retail investors. Companies should consider the most appropriate way to achieve this, which might well be through the use of new technology platforms. The Government should also continue to overhaul the listings regime and regulatory burden to make the public markets in the UK more attractive for companies to list and operate.
6.	Those with Cash ISAs should be made more aware of the potential returns available via Stocks and Shares ISAs, and the harm they are doing themselves by leaving their assets in cash. This could be done via correspondence or by amalgamating Cash ISAs and Stocks and Shares ISAs into a single product.
7.	A new national fund should be created, which might invest directly in a diversified portfolio of UK equities or operate as an index tracker for the main FTSE index. The new fund should be explicitly backed by Government to instil confidence in new investors and established by an organisation which would give potential investors confidence about the prospects of investing in UK equities – such as NS&I.

1. The Case for Retail Investing

Introduction

The ambition to own the whole, or part, of an enterprise is hardly a modern one, though the rules and structures surrounding joint endeavours have come a long way since The Code of Hammurabi set out some of the earliest known provisions relating to commerce, trade and investment.[16]

Traders and commercial activity have existed for centuries, as has the idea of joint endeavours. The first known example of an investment which pooled risk was the Moulin du Bazacle scheme in southern France in the 14th century, established to support a series of flour mills (extraordinarily, a shared commercial interest which lasted until the late 19th century).[17] Venetian moneylenders sold bonds in the 14th century, Belgian brokers dealt in promissory notes in the 16th century and in the 17th century, stock exchanges started to emerge.[18]

> **‘Figures from the Office for National Statistics show that the proportion of UK shares held by UK residents has been falling from over 20% some 30 years ago to just over 10% now’**

Share ownership and investment activity, however, typically remained the preserve of a wealthy few. It was not until the 19th and 20th centuries that company law came to look more like the system we have today, especially by moving to a system where the liability of owners was curtailed through ‘limited liability’ laws. This, combined with the spreading of wealth beyond the elites, slowly gave more and more people the opportunity to invest and own their own share in companies.

This shift towards a more enfranchised and empowered population has been of huge significance to both the economy and the society of the UK (and other countries). Yet in recent decades, the shift towards greater individual ownership has effectively stalled.

In fact, figures from the Office for National Statistics show that the proportion of UK shares held by UK residents has been falling, from over 20% some 30 years ago to just over 10% now.[19] This is not principally due to a decline in the total amount of household wealth in the UK, but the allocation of that wealth – a point that becomes

16 The Code is probably the best-preserved legal text from the ancient Near East and is widely regarded as being the first known document in the history of investing and investment.

17 Merryn Somerset Webb, ‘Share Power’ (2022), p. 22.

18 The Amsterdam Exchange was founded in 1602 and the London Stock Exchange, emerged from John Castaing’s list of currency, stock and commodity prices, first published at Jonathan’s Coffee House in the City of London in 1698

19 ONS, ‘Ownership of UK Quoted Shares: 2020’ (March 2022). Link

clear when comparing the UK's proportion of total household assets invested in listed shares to other European nations.

Part of this, of course, is about a shift towards institutional investment, and in particular pension savings. But it is also the case that the UK lacks a culture of popular share ownership. And it is not just that we are all parking our savings into property instead. Particularly concerning is how much money is being held in the form of cash – with official figures and wider estimates suggesting that the total sum might add up to more than £2 trillion across the UK economy.[20]

This is money which will have its value eroded thanks to inflation, meaning the individual investor loses out, but which is not being invested in companies which can build and grow – meaning the wider economy loses out.

> **'Particularly concerning is how much money is being held in the form of cash – with official figures and wider estimates suggesting that the total sum might add up to more than £2 trillion across the UK economy'**

Later in this report we will consider some of the reasons why people might not be investing in the public markets, including rules and regulations, systems and structures, attitudes and apathy. But we will start by explaining why this is a matter of concern.

To do this, we will ask why retail investment matters. We will look at what it means in economic terms to the individual, to the businesses who receive investment and what investment can do for the economy as a whole – as well as the wider implications of retail investment for our capitalist system and wider society.

The Economic Case

This might feel like an odd time to publish a report making the case for more retail investing and a larger number of retail investors. Even those with little interest in financial markets will be aware of the turmoil that affected stock exchanges throughout the Covid-19 pandemic and the precipitous falls which befell various companies in different sectors last year. Given that the FTSE 250 was down by almost 10% over the course of 2022 (and at one point was down by over 20%) it is self-evident that many people's ISAs, SIPPs or personal trading accounts are likely to have taken a hit.[21]

Yet the economic case for more retail investing is not about the returns generated in any single year, but about the long-term growth potential of investing in public markets – and the benefits which will accrue to individuals, businesses and the economy as a result.

Now, perhaps more than at any point in the last 30 years, it is easy to explain to people why keeping most of your money in cash is not a particularly sensible idea. With inflation rampant, running at double figures during late 2022 and in early 2023, people recognise that the money 'in their pocket' is starting to be worth less and less. Interest rates have, of course, gone up – but by nowhere near the rate of inflation.

20 See Jim Armitage, The Times, 'Middle England is rolling in cash – but will people spend it?' (February 2023). Link
21 London Stock Exchange, 'Indices: FTSE 250' (accessed 2023). Link

The eroding effect which inflation has on cash holdings is all too clear – yet the latest official statistics suggest that there is almost £300 billion worth of money sitting in individual cash ISAs. That figure pales into insignificance when compared to the amount of cash held in savings accounts, however, which leading economists at NatWest recently estimated to be £1.8 trillion across all the major banks.[22]

The Financial Conduct Authority's (FCA's) Financial Lives Survey 2022 revealed that 9.7 million UK adults had investible assets of more than £10,000 which were held mostly or entirely in cash.[23] As the FCA themselves have made clear, this is money which could be put to far better use.[24] Deploying this money into property, gilts or – ideally – equities would all be likely to offer better returns than holding it in cash at a time of high inflation.

Many people, as this report has already pointed out, consider property their default option for investment activity, with a far smaller proportion looking to buy bonds or gilts. But, based on historic returns, few of these asset classes offer anything like as positive a long-term yield as equities.

'The Financial Conduct Authority's (FCA's) Financial Lives Survey 2022 revealed that 9.7 million UK adults had investible assets of more than £10,000 which were held mostly or entirely in cash'

In 2019 the Financial Times compared a £100 investment made in 1900 into either Government gilts or a broad range of shares. They showed that the real return (i.e. adjusted for inflation) of the investment into gilts, with returns reinvested, would be £876 after 119 years. The real return on the investment into equities over the same period would be almost £55,000.[25] The situation with the property market is more nuanced, but analysis by Schroders shows that excluding taxes and costs, the global stock market has reliably beaten the UK property market over a range of recent time periods, even in regions such as London.[26]

When individuals buy into a company (ideally via equity holdings in a number of companies, as part of a diversified portfolio) they buy into the potential for future growth in the market valuation of that company. But they also buy into the potential to unlock income through company dividends.

Such dividends can provide valuable funding for individuals to spend as they see fit – but it is when those dividends are reinvested that the value of equity holdings really comes to life, with the gains subject to compound effects.[27]

There is clearly risk attached to holding shares – something we will consider in more depth later in the report – but the average returns of equities compared to other asset classes over decades and decades is undeniable, and why it makes sense for as many people as possible to have exposure to equities.[28]

22 Jim Armitage, The Times, 'Middle England is rolling in cash – but will people spend it?' (February 2023). Link

23 Financial Conduct Authority, 'Financial Lives survey 2022: insights on the vulnerability and financial resilience relevant to the rising cost of living' (October 2022). Link

24 See, for example, FCA, 'Evaluation of the impact of the Retail Distribution Review and the Financial Advice Market Review' 2020. Link

25 Glen Arnold, 'Financial Times Guide to Investing: The Definitive Companion to Investment and the Financial Markets' (2019), p.22.

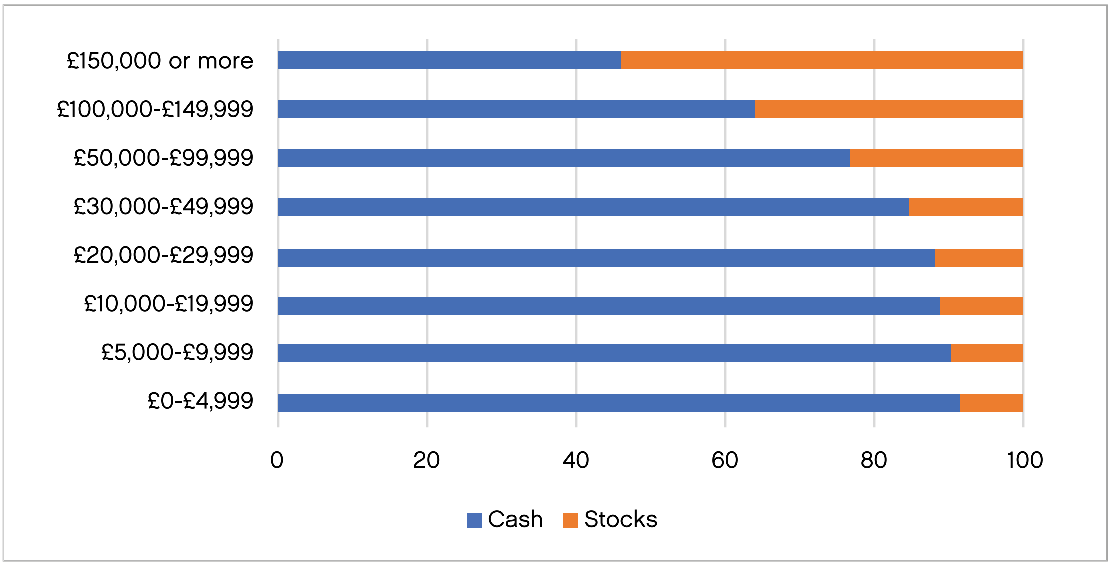
26 Schroders, 'What 175 years of data tells us about house price affordability in the UK' (Feb 2023). Link

27 Ibid.

28 See Barclays Equity Gilt Studies for more information

This is also an essential task if we are to tackle the inequality gaps in the UK, which were exacerbated during the Covid-19 pandemic. The ONS has shown that in 2021 median income for the poorest fifth of the population decreased by double the rate that it did for the richest fifth[29] – yet HMRC statistics make it clear that those on the lowest incomes are far more likely to invest in Cash ISAs than in Stocks and Shares ISAs.[30]

ISA type as % of total (by income bracket)



Source: HMRC

Helping those on lower incomes to understand, and take advantage of, the opportunities to invest in companies via public markets is likely to enhance their own wealth, as well as that of the country as a whole.

And attracting more investment from individuals into UK companies is likely to be good news for those companies too, especially given the UK's historically poor performance when it comes to business investment.

Few people would look at the UK's economic record since the financial crisis and describe it as an unparalleled success. Moreover, performance since the Covid-19 pandemic has been even worse than historic trend rates. Growth has stalled, productivity flatlined and the wealth gap has widened.

The relatively low levels of business investment by UK companies are well recognised, not least in previous CPS publications, as are the issues that some companies have in attracting the finance they need to invest and grow. It seems reasonable to think these phenomena might be linked.

There is also a specific issue around attracting equity finance in the UK, especially compared to other advanced economies. The tax treatment of equity finance compared to debt finance – or investments in property and real estate – is, many suggest, one of the reasons why comparatively little capital is invested in the more productive parts of our economy.

29 ONS, 'Average household income, UK: financial year ending 2021' (March 2022). Link
30 HMRC, 'Commentary for Annual saving statistics' (June 2022). Link

Encouraging more 'productive finance' has been a key Government priority in recent years, as is clear from the establishment of the Productive Finance Working Group[31] and Rishi Sunak's explicit instructions to the Bank of England just a month after becoming Chancellor.[32]

Ultimately, if we are to be successful in securing future growth, we will have to rely on the hard work of the private sector. That, in turn, relies upon the private sector's ability to attract the capital it requires to invest in people, ideas, land, property and kit.

'Those companies that took steps to actively engage with their retail investors, especially through holding investor events, reportedly saw liquidity increase by more than 20% on average'

If more money was to be invested in companies with a realistic prospect of growth, i.e. if they were able to attract the capital needed to make good on their ambitions, then we could expect those companies to expand, make more money and invest more in their future growth.

Some people we spoke to while researching this report claimed that, for most companies, marketing to individual investors is not worth the hassle. It is easier, more efficient and more effective to appeal to institutions. This is especially true, it was claimed, for those companies which are not 'business to consumer' in nature – and therefore do not have to worry about wider public recognition and appeal.

The argument goes that by talking to investment banks and those who they represent, you can have a smaller number of conversations and convince a more expert audience of your company's valuation and future potential.

But that misses out the benefits which retail customers can offer to companies listed on public markets – such as having a more diverse share register, a more stable share register and, perhaps most importantly, providing more opportunities to raise capital and increasing liquidity.

In terms of capital, there are hundreds of billions of pounds of retail investor money sitting in Stocks & Shares ISAs as well as in more typical share trading accounts. And if the various proposals in this report are taken forward, there could be plenty of extra investment coming down the track.

A key point here is that companies with a large and engaged retail investor base also tend to benefit from increased liquidity – something recently demonstrated through research conducted for the Quoted Companies Alliance.[33] Those companies that took steps to actively engage with their retail investors, especially through holding investor events, reportedly saw liquidity increase by more than 20% on average. This helped reduce not just their cost of capital, but also price volatility, resulting in fairer valuations.

31 Bank of England, 'Productive Finance Working Group' (accessed 2023). Link

32 Rishi Sunak and HM Treasury, 'Remit and Recommendations for the Financial Policy Committee (March 2020). Link

33 Quoted Companies Alliance, 'Quoted Companies Discover the Power of Retail Investors' (November 2022). Link

Separate research carried out by Barclays and by Capita Asset Services has shown that retail investors are often more loyal to companies. According to this research, of the private investors who invest via IPOs, 76% are still invested after the first year, and 42% are still shareholders after three years. This compares to institutional and foreign investors typically holding on to their UK equity investments for less than two years.[34]

In other words, increased retail investment would benefit companies as well as individual investors – but it would also lead to macro-economic benefits, through a combination of GDP and GVA growth, development of capital stock and wider economic spillover effects.

As those companies are able to grow, they can pay more taxes and fund more public services. But this virtuous circle starts and finishes with the ability for these companies to attract investment.

That investment could come from the millions of would-be investors in the UK.

Beyond the Economics

The economic arguments for retail investment are clear-cut for individual investors, for businesses and for the economy as a whole. But the case for encouraging more retail investor activity goes beyond pure numbers. It is about the type of economy, society and country that we want the UK to be.

The market-based, capitalist system which exists in many liberal economies has brought about huge advances in living standards in those countries – and around the world. The statistics in terms of access to education and healthcare, poverty reduction and life expectancy speak for themselves.

‘Of the private investors who invest via IPOs, 76% are still invested after the first year, and 42% are still shareholders after three years’

Yet the capitalist system which has brought about so many of those advances – which includes the successful deployment of capital, freely exchanged between investors and companies, as one of its key features – continues to have its detractors. In fact, those detractors are seemingly increasing in both number and hostility towards the capitalist system – as various polls (and certain elections) conducted over recent years make clear.[35]

The Centre for Policy Studies, and its sister organisation CapX, have looked closely at this topic. In 2018, CapX, working with Number Cruncher Politics, asked survey respondents if they agreed that ‘Communism could have worked if it had been better executed’. Within the group aged under 35, almost 40% of respondents agreed with the statement – and it also had a net positive response from those aged 35-44.[36]

34 Barclays Stockbrokers and Capita Asset Services as quoted by Swen Lorenz, ‘The importance of retail investor’ (accessed 2023). Link

35 See, for example, YouGov, ‘Do you have a favourable or an unfavourable opinion of capitalism?’ (2016). Link; Gideon Skinner, ‘World divided on socialism, 200 years after birth of Marx’ (2018). Link; and More in Common, ‘Britain’s Choice: Common Ground and Division in 2020s Britain’ (October 2020). Link

36 Number Cruncher Politics, ‘CapX Ideologies Poll’ (2018). Link

Moreover, when Dr Frank Luntz recently conducted a landmark survey on behalf of the Centre for Policy Studies, looking at the British public's attitudes towards certain values, his results suggested widespread disillusionment with the 'British system', including in terms of how business and enterprise operated. When people were asked what phrases they thought of when asked about British companies, the top two answers were 'profit over people' and that 'they put shareholders first, not ordinary people.'[37]

Such results suggest that many people feel increasingly disconnected from the system – a feeling which is exacerbated by left-wing populists who try to point to high corporate profits or examples of individual wealth as evidence of a 'them and us' world, which is unfair, loaded and demands reform.

Income and wealth gaps have fanned the flames of this discontent, encouraging some on the left to argue that the situation is stacked against the little guy, with greedy shareholders exploiting workers for their own benefit.

> **When the CPS asked people what they thought of British companies, the top two answers were 'profit over people' and that 'they put shareholders first, not ordinary people'**

Their crude characterisation is, of course, wide of the mark. The innovation, hard work, creativity and determination of the private sector is what has led to a greater number of opportunities and the huge advances in living conditions which we now take for granted – not to mention providing the lion's share of employment and opportunity in the country. But, nevertheless, a gauntlet has been thrown down which it is necessary to respond to.

If more people get an active stake in the economic model in which they operate, then they are more likely to understand the benefits they, and society as a whole, gain from the capitalist system. More people being exposed to businesses, and having a stake in their success, is likely to lead to a greater understanding of the fundamental role and purpose of business – and more support for the private sector.

If lots of people think that capitalism is a broken system, which isn't for them and is fundamentally unfair, then the answer is not to reform capitalism – but to ensure that as many people as possible are exposed to it and are in a position to benefit from it. This, ultimately, is about the democratisation of capital – and ensuring that the proceeds of growth are shared more widely. We need to help people to understand the opportunities that exist and give them more of a stake in the system at the same time.

Increasing polarisation in terms of income, wealth and opportunity is not only likely to weaken the UK economically, but also politically and societally. Ultimately, we run the risk of undermining our cohesiveness as a nation and the social contract which exists between us.

Looking to increase the number of retail investors is as much a moral imperative as it is an economic one, therefore. People need to be empowered and to be given a greater, and more obvious, stake in the system in which they operate.

37 CPS, 'CPS publishes landmark survey by Dr Frank Luntz on politics, economics and culture wars' (July 2021). Link

Having a stake in the system also means having the ability to change it from within – rather than tearing it down from without. In the context of a population which is increasingly conscious of Environmental, Social and Governance (ESG) issues, that represents an opportunity for people to exercise their legitimate rights as shareholders, but also an opportunity to encourage people to invest in public markets.

This latter opportunity is one which organisations like Share Action have recognised and are trying to promote – by, in their words, 'using the power of the financial system to tackle the biggest environmental and social challenges we face'.[38] Research by the European Capital Markets Institute has shown how 'responsible investing' is drawing investors into public markets, with ESG preferences being of particular importance.[39]

As well as considering stewardship in ESG terms, having a share in a company also gives the shareholder a wider interest in and responsibility towards the good health and financial returns of the company – and the ability to influence it. As literal owners of companies, investors can vote on key decisions, including around remuneration policy and Board positions – or at least they can when intermediaries allow them to.

'If people do not understand – or cannot exercise – their rights as part owners of a company, then they will not get the opportunities which are their due through ownership'

Some organisations work hard to ensure the voice of retail investors is heard. Tumelo and Tulipshare have been established with that exact purpose in mind and both ISS (Institutional Shareholder Services) and Glass Lewis work hard to bring companies closer to their individual retail investors. Too much intermediation remains in the system, however – an issue which Mark Austin looked at in depth and which continues to defray the wider benefits of investing for individuals.

This is a matter of concern because if people do not understand – or cannot exercise – their rights as part owners of a company, then they will not get the opportunities which are their due through ownership.

That is not to say owning shares through funds and trackers isn't a perfectly legitimate option. For many people, it makes overwhelming sense – and is definitely preferable to cash holdings or other asset forms. But the potential engagement which comes through direct equity holdings is self-evidently more likely to foster a sense of ownership and empowerment on the part of retail investors – and to lead more people to both understand and participate in our economic system.

Retail investing, in other words, is not just about the economic opportunities which might accrue to an individual, to businesses and to the country at large, but also about the opportunity for individuals to develop, for businesses to gain from a wider pool of owners and for the system in which we operate to be more widely understood and appreciated.

38 Share Action (accessed 2023). Link

39 Marie Brière and Stefano Ramelli, 'Can responsible investing encourage retail investors to invest in equities?' (March 2021). Link

In recent years we have seen a welcome democratisation of share ownership and of interest in the public markets, via the growth of investing apps and forums. There has been much coverage recently of the rise of 'fininfluencers' (financial influencers) on platforms such as Instagram and Tiktok. There has been some concern over the potential lack of sophistication of these investors, particularly given the rise of meme stocks, crypto, NFTs and other novel investment classes. But the surge in interest of retail investing, and the accompanying surge in the number of retail orders, is ultimately a welcome phenomenon, and one that needs to be built on.[40]

As well as serving to reduce the economic inequalities which exist in the UK, making retail investing a genuinely mass market phenomenon would help to break down perceived barriers around opportunities which some consider to be the preserve of the wealthy few. As much as anything, then, this is about the defence of capitalism.

Right now it is clear that this country is facing a crisis of confidence in capitalism – particularly when it comes to younger groups who don't feel like the system offers them anything worth defending. Encouraging more retail investing offers an antidote to that problem. If we don't promote it deliberately, assertively and consistently, we will not just be faced with a crisis of confidence in capitalism, but a crisis in capitalism itself.

That is why we need government to explicitly embrace and promote retail investing. While many documents or strategies can be pointed to which demonstrate the Government's commitment to property ownership, employee ownership or other policy priorities, no such document exists with regards retail investment. It is time that was put right.

It is true that the FCA produced a consumer investment strategy in 2021 – but encouraging retail investing was just one element of it, and has received far less attention since publication than other component parts. Moreover, it should be the Government which recognises the economic and social benefits which are to be gained by encouraging more retail investing and acting accordingly.

Recommendation

> The Government should commission or produce a new Retail Investment Strategy. This Strategy should make the creation of more retail investors and unlocking more retail investment its explicit aim, looking to put retail investors on an equal footing with institutional investors. It should consider in particular how to encourage more private capital into public markets, given the economic and social benefits which this would unlock. And it should examine the tax treatment of retail investing and how it can be made more attractive.

40 Financial Times, 'Meteoric rise of 'finfluencers' sparks concerns' (May 2023). Link

2. Attitudes and Awareness

Introduction

The previous chapter aimed to explain why retail investing matters and what the benefits might be if there was more investor activity. In summary, individual businesses, our economy and our society would all gain. Most importantly, so would individual investors.

But given the potential gains for individual investors – and the fact that many UK citizens clearly want to avail themselves of opportunities to increase their personal or household wealth – why aren't there more retail investors?

In some respects it's never been easier for the individual investor to access equity markets. Trading accounts can be set up easily, advertisements for retail investor products are commonplace and the business pages continue to be full of market commentary and share tips. That's before you get into the profusion of investing apps, forums and social media accounts appealing to the younger generation. So why might people be steering clear?

'The FCA's 2017 survey of perceptions towards finance in the UK found that only 29% of adults think they know enough about investments to choose ones that are suitable for their circumstances'

Clearly there are structural and systemic issues. The UK does have an extremely attractive tax-free wrapper for share investment, in the form of the ISA. But as Xavier Rolet has recently highlighted, it also imposes higher transaction taxes on share trading than any of its major rivals – not to mention the wider regime of dividend taxes, income taxes and capital gains taxes which grows ever more extractive. That is why the strategy proposed in the previous chapter needs to take account of investment incentives and transaction taxes, with a view to mirroring best practice elsewhere.

But within the world of investing, too, it feels as if the balance has shifted too far towards institutional investors, to the detriment of individuals, making accessing opportunities – which historically might have been taken for granted – much harder. Exposure to Initial Public Offerings (IPOs) is one example of how retail investors are often frozen out, despite the name suggesting these are targeted at members of the public.

Yet the evidence suggests that the most fundamental challenge may be around people's understanding of finance and their self-perceived ability to deal with financial matters. The FCA's 2017 survey of perceptions towards finance in the UK found that only 29% of adults think they know enough about investments to choose ones that are suitable for their circumstances. Moreover, only 16% considered themselves highly knowledgeable about financial matters.[41]

In many respects, this isn't particularly surprising. The language of investing and investment opportunities is hardly accessible, with the interchangeable terms stocks, shares and equities confusing people from the off, before they even start to grapple with alpha, price-to-earnings ratios and fill or kill trade orders. By the time you've reached acronyms (who can tell their KIDS from their KIIDS?), most people have either decided that they need advice – or that investing is not for them.

The problem is that those who reach the second conclusion – who clearly number millions and millions – are being cut adrift from opportunities which are clearly in their best financial interests. Opening up these opportunities means helping those people understand, appreciate and navigate the investment landscape. That, in turn, relies on increasing their awareness of, and ensuring they're better educated about, the world of investments. A senior executive at one of the UK's largest banks bemoaned to us that at present, they are effectively forbidden from suggesting to the many customers with significant amounts in cash that they might like to think about the stock market or tracker funds.

‘Perversely, much of what the Government and its regulators do actually serves to put people off investment opportunities’

As well as ensuring people are aware of the opportunities which exist, it should also be incumbent upon policymakers to ensure that no artificial or unhelpful impediments are put in the way of investment activity. The first of the two likely conclusions mentioned above – i.e. people who might want to seek advice – falls into that category. It's far harder for people to access appropriate, tailored advice than it should be – a topic which is considered in more depth below.

Yet there is an even more obvious issue which acts as an impediment to investor activity – the UK's attitude towards risk, particularly with regards investment activity.

Being Realistic about Risk

Given the Government's support for ISAs in particular, one might assume the state already wants people to engage in more investment activity. After all, why create a tax-efficient vehicle for people to buy and sell shares if you don't want more people investing in public markets?

But perversely, much of what the Government and its regulators do actually serves to put people off investment opportunities. From regulatory disclaimers screaming about the chances of investors losing money through to the barriers which need to be jumped over for individual investors to be able to access certain investment opportunities (typically unlisted securities), the regulatory requirements around the promotion of financial products self-evidently have a stultifying effect.

41 FCA, ‘Understanding the financial lives of UK adults: Findings from the FCA's Financial Lives Survey’ (October 2017). Link

Certain protections and regulations are required, of course. But where the line has been drawn in respect of investment opportunities goes far beyond what is required. The stance we are taking is unsuitable for a market economy and liberal democracy which, in theory at least, wants to support investment activity and in which robust protections already exist against fraudulent behaviour.

This is perhaps most obvious when investing in stocks and shares is compared with investing in crypto-assets or placing a bet online or in your local bookmakers. All platforms which allow people to trade shares or which point people towards funds or other investment opportunities declare that 'your capital is at risk', as they are required to do by the Financial Conduct Authority (FCA). But if someone wants to invest in crypto, no such warning is required, because this sort of activity is currently unregulated by the FCA. Equally, there are no similarly prominent regulatory warnings when you place a bet, despite the fact that there is a far greater chance of losing your stake if you put £100 on a horse in the 3.15 at Carlisle than a firm in the FTSE 100.

If you walked into a restaurant and on the top of the menu it said that all the food served within the restaurant might give you food poisoning, people would walk out. But that, in effect, is the approach being taken with investing, given that every webpage and every trading form says 'your capital is at risk'. In effect, we are putting people off before they even get through the door.

‘Our current approach to investing defaults towards regulations, restrictions and an abundance of caution – flying in the face of personal responsibility’

Instinctively, it feels beyond much doubt that people understand that there is a risk to any capital invested in a company, because people have a basic understanding of the fact that value can go up as well as down. These disclaimers do not enhance anyone's understanding of the fundamental principles.

This is not, by the way, a call to add further regulatory strictures to, say, the gambling industry. On the contrary, there is something to be learnt from the way that policymakers and regulators recognise that it is down to individuals to decide what their risk appetite is and to do with their money as they see fit.

Our current approach to investing, by contrast, defaults towards regulations, restrictions and an abundance of caution – flying in the face of personal responsibility and the idea that individuals are best placed to determine what they consider to be in their personal interests. Moreover, the throttling effect of heavy-handed regulation will actually reduce the potential upside for investors across the board, burdening companies with extra costs and compliance requirements and distracting them from the activities which most shareholders would most want them to focus on: making profits and creating shareholder value. It is also worth pointing out that if you want to invest in a public company, it is already overseen by company law and corporate governance codes, with regular reporting requirements – and the right to resort to the law if you have been misled.

Regulators of course want to protect consumers from harm – but the irony is that their approach is often harmful in and of itself. For example, the first draft of the 2014 Markets in Financial Instruments Directive (MIFID II) legislation actually tried to prevent anyone trading as an individual investor without taking regulated investment advice.

Although this ludicrous regulation was avoided, MIFID II and countless other regulations put in place in the UK have served to stifle the market and reduce investor interest and investor opportunities. We will deal with the topic of advice later in this report. But notoriously, the decision (inspired by EU rules) to ban firms from taking commission in exchange for offering financial advice helped to create a yawning and much-publicised 'advice gap': because people now had to pay for investment advice, many of them decided not to get it at all.[42]

The FCA's most recent Financial Lives Survey revealed that there were 9.7 million people with investable assets of over £10,000 mostly or entirely held in cash. Of those, they said, 44% (4.2 million) had some appetite to take 'investment risk'. But how many of those 9.7 million might want to take 'investment risk' if they weren't served a barrage of off-putting messages?[43] Or if they had access to the kind of advice they need?

As a first step, the current approach towards risk needs to be turned on its head, with the Government, regulators and other policymakers embracing a more positive attitude. A recent consultation looking at Packaged Retail and Insurance-based Investment Products (PRIIPs) and UK Retail Disclosure suggested the Government is alive to the need to address some of the most excessive requirements, but there is much further to go.[44] The Government and regulators need to rebalance their approach, recognising that some risk is not just inevitable but actually necessary and worthwhile.

> **'The FCA's most recent Financial Lives Survey revealed that there were 9.7 million people with investable assets of over £10,000 mostly or entirely held in cash'**

There would, of course, be a chance that some people would lose money if this new approach was adopted – people who would not lose money if the status quo is maintained. But it is not the job of Government to stop people from losing money, but simply to ensure they are not taken advantage of, defrauded or otherwise ripped off. And we should remember that by keeping their assets in cash, those people are already losing money with every day that passes – all the more so with inflation at the sort of levels seen thus far in 2023.

What we need to do, in other words, is draw a distinction between criminal behaviour and bad investments. Where criminal activity takes place, the perpetrators should be punished and, if possible, customers refunded (and obviously regulators should do everything in their power to stop this activity in the first place). But we should be more relaxed about people making certain investments which lead to an increased chance of them losing money – that is the price that is paid for other, or even the same, investors having a greater chance of making money.

Back in the 1980s, a decade where the Government put its full weight behind the ambition to encourage more retail investing, Professor Laurence Gower was asked to publish a review on investor protection. He argued that the level of supervision

42 FT Adviser, 'What is the legacy of the RDR 10 years on?' (Dec 2022). Link. See also Royal London, 'Exploring the advice gap' (2021). Link

43 Financial Conduct Authority, 'Financial Lives survey 2022: insights on the vulnerability and financial resilience relevant to the rising cost of living' (October 2022). Link

44 HM Treasury, 'PRIIPs and UK Retail Disclosure, A Consultation' (December 2022). Link

should not 'seek to achieve the impossible task of protecting fools from their own folly', but should rather 'be no greater than is necessary to protect reasonable people from being made fools of'.[45]

Gower's Review actually attracted some criticism at the time for being too heavy-handed – showing just how far we have come regarding our attitude to risk in recent decades.[46] As our risk appetite has dulled as a country, with much of the blame lying with politicians who refuse to speak up for personal responsibility and the limits of appropriate Government intervention, the deleterious effects on our economy have been all too obvious.

If we are to thrive economically, we need to put our capital to work as effectively as possible – and that means not putting people off investment opportunities from the outset.

Recommendation

The Government and regulators should rethink the disclaimers around retail investing – and, more fundamentally, take a more realistic, and positive, attitude towards risk. The concept of personal responsibility in investing should be recognised and embraced, and the positive role which can be played by risk capital should be more readily supported.

Accessing Appropriate Advice

Some might argue that there is an inherent contradiction in what has already been said in this chapter. We have moved from pointing out how small a percentage of the British public claim to have a solid understanding of financial matters to recommending that disclaimers are dispensed with and risk more readily embraced. Surely, the critic might argue, this self-diagnosed gap in knowledge and understanding is just cause to maintain – or perhaps even further enhance – risk warnings and the wider regulatory approach?

But the main reason to call for a reduction in regulation is not because of the absence of risk. Indeed, risk is inherent in the act of investing. Rather, our argument is that people self-evidently understand the potential for share prices to fall – but the current warnings are disproportionate and can deter investments that might be in an individual's best interests. Ultimately, risk can actually be a good thing; it is an essential part of the equation which can lead to higher returns when capital is deployed.

Moreover, there is an easy fix if people are worried about their own understanding of the stock market: to consult an expert. Yet there too the Government has made it far, far harder than it should be for people to gain access to guidance and advice.

Although these terms may sound interchangeable, and clearly both are targeted at helping people understand options that might be available to them, they actually have very different technical definitions. This distinction is reflected in who can offer each, what processes those who offer them have to undertake, how valuable they are for consumers and what the risks are for those who provide such services.

45 Nigel Lawson, Financial Times, 'We must not take London's success for granted' (October 2006). Link
46 See, for example, Len Ross, 'Investor Protection – Why Gower is Wrong' (1984). Link

In broad terms, guidance means providing people with general information about options that might be available – for example about different pension products or types of ISAs. Indeed this report might itself count as guidance given the topics which it covers.

Advice, however, is tailored to an individual's specific circumstances – for example their personal finances, what their financial goals are and their attitude towards risk. Whereas guidance can be offered without regulation (a relief in the context of writing this report), financial advice can only be offered by financial advisers or wealth managers who are regulated by the Financial Conduct Authority (FCA).

So far, so good. Most people would want those who offer financial advice to be properly authorised and regulated.

But the nature and burdens of the current regulatory approach causes issues which, like the regulators' attitude towards risk and the stifling nature of constant risk warnings, actually end up causing harm to consumers.

'The FCA believe that 38 million people do not use any formal support to help them with their finances – small wonder when the average 'fact find' before offering advice costs £750'

The first and most obvious issue is around the disproportionate and bloated requirements imposed upon an adviser if they are going to offer advice which is in any way tailored to someone. As soon as any type of 'personalised' service (reflecting an individual's personal circumstances or preferred approach) is introduced, then 'suitability requirements' kick in. These require the adviser or wealth manager to ask a huge number of questions, and offer a set of options and recommendations which might go way beyond what the prospective investors wants or needs. This actually stops them from being able to offer the sort of low-cost, light-touch advice which most people are looking for – and which might catalyse millions more people to invest in the stock market.

The FCA believe that 38 million people do not use any formal support to help them with their finances – small wonder when the average 'fact find' before offering advice costs £750.[47] This is all the more absurd when the basics of advice, for the overwhelmingly majority of people, can be expressed via a few universal commandments.

As we have said, financial services can be inherently complex to understand, and many people don't feel equipped to decide for themselves what a good investment option might be. But the current situation means that financial advice is too often the preserve of the older and the wealthier. This means that they are more likely to get wealthier still, well advised as they are, while younger people and the less well off are unable to afford the tailored advice which might make a huge difference to their prospects. Unsurprisingly, the wealth gap continues to grow.

The FCA have, to their credit, acknowledged that this issue exists. In November last year, they issued a consultation looking at what might be done to broaden access to financial advice.[48] The consultation announced an intention to introduce

47 Patrick Hosking, 'The Times, Personal Guidance to Help With Personal Finances' (28 November 2022). Link

48 Financial Conduct Authority, 'CP22/24: Broadening access to financial services for mainstream investments' (November 2022). Link

'a new streamlined regulatory regime to increase firms' confidence and commercial willingness to provide financial advice proportionate to the needs of the consumer' and said that, following reforms, 'firms should find it cheaper and easier to provide… advice to consumers who need it.'[49]

A key part of their suggested approach was 'reframing the existing suitability requirements' – but it remains to be seen how bold their approach will actually be. (We would argue that it should be very bold indeed.)

The consultation closed at the end of February 2023, but no response has been published at the time of writing. And nothing within the consultation suggested that the FCA intend to do anything at all about one of the biggest failings of all, highlighted above – the fact that high street banks are either forbidden or very strongly discouraged from approaching customers with a high level of cash savings and talking to them about other investment options.

'The current situation means that financial advice is too often the preserve of the older and wealthier. This means they are more likely to get wealthier still'

Even in terms of the reforms that are expected, concerns remain that the 'fact find' requirements for financial advisers or wealth managers concerning each possible investor will remain far too onerous.

At the simplest level, it doesn't seem unreasonable that an adviser should just ask an individual how much they have to invest, whether they have any debt, what their risk appetite is and whether they have some sense of the sorts of products they want to invest in – before offering them some advice, which can be taken or left as the individual prefers.

Instead, when advice is given, not only do suitability requirements come into play, as outlined above, but there is also a wider issue of liability which then applies. Indeed, part of the reason that there are such stringent requirements at the moment is because the adviser is considered to be liable for the advice that they have offered – and that liability hangs over them if investments don't work out.

Because advice is regulated by the FCA, those who receive it are protected by the Financial Ombudsman Service and the Financial Services Compensation Scheme. As the advice provided on the Citizens Advice website points out: 'If you have lost money because of bad advice… you can complain to the adviser who originally gave you the advice', before going on to explain how complaints might be escalated.

But, on a point of principle, it seems unreasonable to be able to hold a financial adviser liable just because the advice they gave was bad – just as you should not be able to hold a racing tipster liable because their 'sure fire' tip in the 3.15 at Carlisle was actually an old nag who came dead last.

This, again, comes back to a question of where the line should be drawn in terms of personal responsibility. Advice, ultimately is just that – and it should fall on individuals to decide whether or not they want to act on that advice.

49 Ibid.

More reasonably, a financial adviser could be considered liable if they provide wrong or misleading information, or have a hidden financial incentive to make a particular recommendation. The issue is not with any form of liability, but with the proportionality and appropriateness of the current set of regulations. Equally, the issue is not around the need to ask personalised questions before offering advice, but around the proportionality and appropriateness of the current set of regulations around suitability requirements. Just to hammer the point home: the alternative to investing is not keeping your money safe, but seeing it relentlessly lose its value if kept in cash.

Something can easily be done about this. Most of the regulatory backdrop to these regulations is provided by MiFID II, mentioned above – the Markets in Financial Instruments Directive (2014), which was the enhanced regulatory framework imposed by the European Union around the financial service industries of its member states. Repealing the legislation in question presents a genuine Brexit opportunity – one which will also be an opportunity for millions of people up and down the country.

Recommendation

Rules around financial advice should be amended to avoid the disproportionate 'suitability requirements' which actually prevent many people from accessing the advice from which they would benefit. The rules around financial advisers' liability should also be reconsidered in respect of the provision of 'bad advice' reflecting the wider emphasis on personal responsibility.

Promoting Public Markets

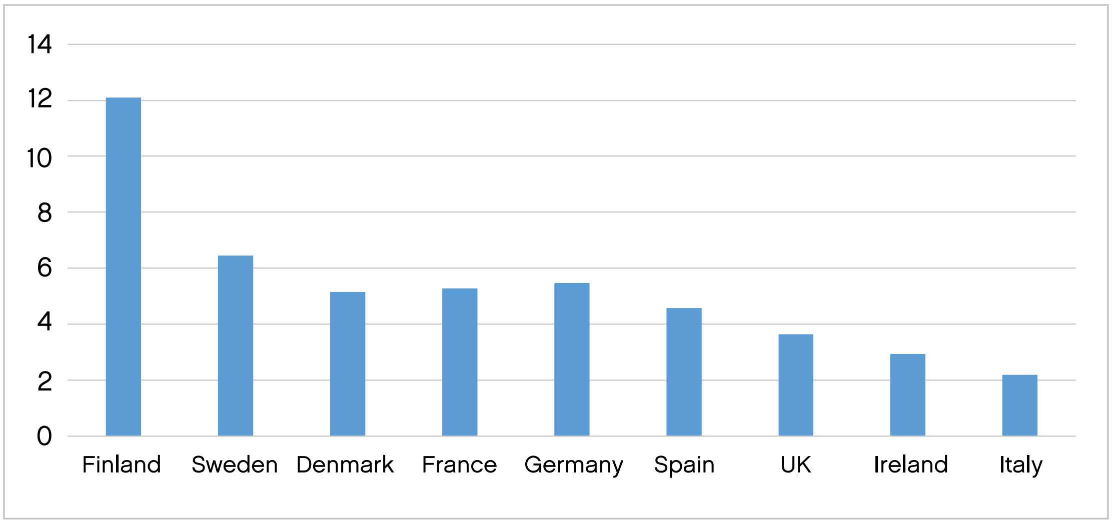
With easier, and more affordable, access to advice, one could reasonably expect there to be an increase in the number of individual investors – and the number of people who invest well. Making advice more readily accessible would be a hugely welcome step forward, therefore. But it would do little to address the huge numbers of people who are not investing in public markets, who would probably benefit if they did so.

As mentioned earlier in this report, it many respects it's never been easier to invest in equity markets. Yet the statistics demonstrate that millions of people are leaving their money as cash holdings, despite the fact that inflation is eroding those savings and diminishing their capital pot. The FCA's Consumer Lives Survey from 2022, for example, showed that there were almost 10 million people with investable assets of more than £10,000 who had most or all of it in cash.[50]

Similar issues can be seen across the developed world, and organisations like the European Capital Markets Institute (ECMI) would be quick to point out that retail investing is not as developed as it might be right across European member states. But the fact is that UK citizens do, on the whole, have a low percentage of their household wealth invested in equities when compared to most European countries, especially those of an equivalent size.

50 Financial Conduct Authority, 'CP22/24: Broadening access to financial services for mainstream investments' (November 2022). Link

Listed shares as a percentage of total household financial assets



Source: Eurostat

The ECMI has shown that the most important factors in determining individuals' willingness to invest in public markets include risk aversion, education and financial literacy, trust (in the economic environment and in financial markets) as well as social preferences. In other words, culture matters hugely in terms of whether or not a country has an active retail investor base.[51] How else to explain the statistics cited by Rishi Sunak in his CPS report from 2017, showing that more than twice as many Americans held shares as Britons?

The American retail investor pool is in fact so deep compared to the UK's that it is estimated that increasing its value to the same percentage of GDP would mean almost a 300% increase in capital deployed.[52] Visit the US, and you will find that 401K savings pots are regular topics of conversation, in a way that ISAs simply aren't. Similarly, stock performance is apparently a staple of dinner table conversation in Australia, fuelled by interest in their own superannuation pension schemes and in the investor clubs in which many Australians participate.

This belies another important element of culture which was not mentioned by the ECMI – which is general awareness. It would hardly be surprising if large numbers of people steer clear of the public markets if they don't know what they are, or how attractive an option they might be. They are therefore cut off from opportunities which are clearly in their best financial interests.

To consider what we might do about this, it is illustrative to look again at the USA, widely regarded as one of the most retail investor friendly countries in the world, as well as the largest economy in the world (two facts which are probably not unrelated).

51 Marie Brière and Stefano Ramelli, 'Can responsible investing encourage retail investors to invest in equities?' (March 2021). Link

52 Panagiotis Asimakopoulos, Christopher Breen and William Wright, 'The Future of UK Banking and Finance' (April 2022). Link

You might think the United States has always offered a supportive environment for retail investing, from the place of Wall Street in the public imagination through to the appeal and popularity of penny stocks (sold directly to the public via nationwide intermediaries like Merrill Lynch). But in fact, Wall Street did not always care for retail investors. In the wake of the Wall Street Crash, the 1930s and 1940s saw a rearguard action by vested interests ('the Old Guard') to keep a stranglehold on who could trade freely within the New York Stock Exchange (NYSE).

> **'The American retail investor pool is so deep compared to the UK's that it is estimated that increasing its value to the same percentage of GDP would mean almost a 300% increase in capital deployed'**

This stranglehold was broken in the 1940s and the route was opened to more retail investment, encouraged and deployed via commission houses. But it wasn't just about the rules. To spur postwar growth, the NYSE subsequently did something far more important to drive awareness and the appeal of public markets: they launched a massive marketing campaign. The 'Own Your Own Share' campaign was couched in patriotic (i.e. anti-Communist) terms. But it also centred on the economic benefits for both the country and for individuals of partaking in public markets.[53]

This was an example followed, in part and somewhat belatedly, in the UK. Organisations like British Telecom and British Gas were household names due to their nationalised status. But when they were taken private in the 1980s, and floated on the London Stock Exchange (LSE), the opportunity for individual investors was pushed hard by the Thatcher Government. 'Tell Sid' is still regarded as one of the most successful UK advertising campaigns of all time – and its entire purpose was to make people aware of the benefits of retail investing.

A modern version of these campaigns is now needed to extol the virtues of retail investing to a new audience. Responsibility for this should rest with the Government, its regulators and with the LSE; individual companies who sit on the public markets might also be encouraged to be involved.

In some ways such a campaign should be easier than ever before. The accessibility of the stock market is more immediate thanks to various trading platforms. Auto-enrolment means many more people actually now do have money invested in the public markets, even if they don't know about it. And messages can be easily tailored to different audiences. Moreover, as outlined above, there is a new generation of people who are instinctively drawn to the idea of investing, as was demonstrated during the Covid-19 pandemic.

But the challenge is also harder. There is more competition for eyeballs and attention than ever before. There is greater suspicion of government. There are no obvious household names which are candidates for privatisation, and no flag around which to rally.

53 For the best exposition of the success of the campaign see: Janice M. Traflet 'A Nation of Small Shareholders: Marketing Wall Street after WWII' (2013). Link

But just because something is hard does not mean it is not worth doing. On the contrary, making people aware of the wealth-generating effect of investments in equities via public markets will not just allow them to grow their wealth, but also provide UK businesses with the capital to invest and grow – in turn, supporting the wider UK economy. That is a prize worth fighting for.

Recommendation

The Government, regulators, the London Stock Exchange and other interested parties should support a modern version of a 'Tell Sid' campaign, raising awareness of the opportunities provided by retail investing and helping to tackle the relatively low levels of retail investing from the UK public.

3. Systems and Structures

Introduction

It is all well and good extolling the virtues of the public markets and selling the vision of a shareholder democracy. But if would-be investors then find that they're unable to access the market in the way they might want, or if there remains confusion or concern about where they should invest their money, the effort will be for nothing.

One might think there should be no confusion on the part of investors if the above recommendations are taken onboard and they can access appropriate advice. But even if our recommendations are adopted, there will still be people who don't access advice, or who don't take time to understand the opportunities available to them.

This final chapter considers some of the other steps which we should take to ensure individual investors are able to capitalise on their enthusiasm to invest in the public markets, or which might help people to go down the path of retail investing.

'In truth, there are all manner of options for how the Government might tweak the structures within the investment landscape to encourage or permit more individual ownership'

In truth, there are all manner of options for how the Government might tweak the structures within the investment landscape to encourage or permit more individual ownership. Investor clubs (a far more common phenomenon in other countries) could be encouraged through preferential treatment of any dividends or capital gains. The Enterprise Investment Scheme (EIS) and Seed Enterprise Investment Scheme (SEIS) schemes could be made more flexible and more generous. Employee share ownership could be expanded with greater incentives. New ownership routes for venture capital and private equity could be opened up. The tax treatment of share transactions could be revisited. Novel ideas like being rewarded for the use of personal data by technology firms with shares in those companies could be considered.

However, we have chosen to focus this chapter on the two big areas. The first is the efficacy of the best known tax-efficient investment opportunity – the Individual Saving Account, or ISA. The second is the case for a new fund for would-be, but instinctively cautious, investors to help them dip their toe in the markets – in just the same way as Premium Bonds offer a state-sanctioned savings vehicle (though one, as outlined later, that offers extremely poor returns compared to the public markets). Reform in each of these areas would help secure our overarching objective – to have a more conducive and appealing environment for individual investors.

But before we look at the specifics, we should start with a more general consideration of the current place of the retail investor in the investment landscape.

Rebalancing Retail

The role of the retail investor is hugely important. But in recent decades it has been steadily eroded. Some of this is inevitable, as a natural result of the increased funding available within the financial services industry and the rise of low-cost institutional investment. The percentage of UK equities owned directly by UK resident individuals has come down a long way, for example – now sitting at something like 12% of the UK stock market, compared to the 54% owned by individuals in 1963.[54]

The balance has not just tilted away from retail investors because of shifts in capital flows and assets under management, however, but also because of some of the changes in rules and/or operating practices within the financial services sector.

> **'The percentage of UK equities owned directly by UK resident individuals has come down a long way – now sitting at something like 12% of the UK stock market, compared to the 54% owned by individuals in 1963'**

Some of these changes were unavoidable. During the pandemic, the Pre-Emption Group (PEG), the FCA, the Financial Reporting Council (FRC) and the Institute for Chartered Accountants of England and Wales (ICAEW) changed their rules to allow companies to raise funds for working capital at short notice, without the usual requirements around pre-emption (thereby putting retail investors at a disadvantage, but also making it easier for firms to navigate such a turbulent environment).

But the move towards an approach which systemically favours institutions over retail customers, particularly around pre-emption rights, has been going on for a long time, with much of the regulatory change coming as a result of decisions at a European level.

The fact that the current set of rules and regulations treat retail investment unfairly and put retail investors at a disadvantage has been acknowledged by Government-commissioned reviews such as Lord Hill's UK Listing Review[55] and Mark Austin's Secondary Capital Raising Review.[56] Both pointed to the potential for technology to help put the retail investor on an equal footing with institutions – or at least to try to rebalance the situation.

Lord Hill's review, for example, pointed to the success of capital raising models used in other jurisdictions such as Australia's Renounceable Accelerated Pro-rata Issue with Dual-bookbuild Structure (RAPIDS) and Accelerated Renounceable Entitlement Offer (AREO), which relied on technological advances to allow a quicker and more efficient process of raising capital for companies and more easily involve retail investors.

Mark Austin picked up the baton, arguing that it was 'important that retail investors are involved as fully as possible in all types of secondary fundraisings' and that companies should look to involve retail investors 'on the same terms and conditions' as institutional

54 ONS, 'Ownership of UK Quoted Shares: 2020' (March 2022). Link
55 Lord Jonathan Hill, 'UK Listing Review' (March 2021). Link
56 Mark Austin, 'UK Secondary Capital Raising Review – July 2022' (2022). Link

investors.[57] He pointed to the potential to use technology platforms, but noted that a company's approach was likely to depend on the use of their share register.

The varied nature of share registers (i.e. companies' actual record of who owns what part of a company) is indeed one of the most difficult issues to overcome for those who want to ensure retail investors are treated more fairly in secondary markets, whether in respect of the proper exercise of pre-emption rights or otherwise. Many individual investors are not registered shareholders themselves but instead hold shares through nominees, such as an investment manager; others still rely on paper share certificates. In both cases, the company of which they own a part won't necessarily have an accurate record of their shareholding, which makes including them in a corporate action, or the offering and granting of pre-emption rights, difficult.

The new Digitisation Taskforce, recommended by Austin in his review, was established by Government in July 2022 and is now chaired by Sir Douglas Flint. It is looking at how paper share certificates can be phased out and how the current intermediated system of share ownership could be improved.[58] This should help redress the balance in time.

'There are plenty of reasons why a company might be well advised to try to engage with the retail investor community, not least potentially higher valuations and increased liquidity as discussed earlier in this report'

But in the meantime, most companies on the public markets are likely to continue to consider it easier, cheaper and less resource-intensive to try to raise capital from institutions than from retail customers. Not least because the institutions have a clear interest in keeping it that way.

Sadly, this attitude is also being adopted by the Government. Since the financial crisis and the bail-out of certain UK banks, UK Government Investments (UKGI) has been gradually selling down the state's stake in NatWest (owned as a result of the bail-out of Royal Bank of Scotland). Yet these shares are all being sold to institutional investors, rather than the Government providing a means for individual investors to buy these shares.

There are plenty of reasons why a company might be well advised to try to engage with the retail investor community, not least potentially higher valuations and increased liquidity as discussed earlier in this report. But Austin's review tried to provide some stick to go along with the carrot. Specifically, he called on the FRC and the PEG to ensure that companies applied his recommendation that retail investors are involved 'as fully as possible' on capital raises and suggested the provision of a 'follow-on offer' for retail investors after an institutional raise takes place. He also recommended putting an obligation on investment platforms to pass on corporate actions to the beneficial holders.[59]

Austin also pointed out that Initial Public Offerings (IPOs) often put retail investors at a disadvantage – but this topic was outside the scope of his report, so he had little

57 Ibid, p. 37

58 HM Treasury, Digitisation Taskforce Policy Paper, (July 2022). Link

59 Mark Austin, 'UK Secondary Capital Raising Review – July 2022' (2022). Link

to say about what might be done to tackle this, beyond some considerations of the regime around prospectuses.

These two reviews were hugely valuable in drawing attention to the structural imbalance which negatively affects retail investors. For example Austin pointed to the absurd limit offered by way of exemption from the Prospectus Regime for retail investors, where there was an aggregate limit of £8 million which could be raised from individual investors, while the exemption was unlimited when applied to institutional investors.[60] Both reviews also highlighted the potential for technology to be used to overcome some of the issues which have developed in recent decades.

However, neither specifically called for reform of the system around primary markets – i.e. the means by which companies sell their stocks (or bonds) to the public for the first time.

To engage with the primary markets, a company typically goes through an IPO process. As the name suggests, this is meant to be an offering (O) to the public (P) for the first time (initially – the I).

Yet IPOs too often fail to live up to the 'public' part of their name. Between 2017 and 2020, there were 352 flotations on main market of the LSE and on its Alternative Investment Market (AIM). Retail investors were invited to participate in just 7% of these. The numbers between October 2020 and June 2022 were marginally better, with retail investors being able to access 21 of the 182 IPOs between those dates (i.e. 13%), but the proportion clearly falls a long way short of what might be expected.[61]

'PWC have found the length of the average FTSE 350 company report is now 64% longer than just five years ago, due to the extra reporting requirements'

There is a broader concern that the number of IPOs has been falling, not least because of the ever-increasing regulatory burden that becoming a public company involves, both initially and then on an ongoing basis – regulation which, like the rules referred to above, is having exactly the opposite effect from what the Government hopes. To give one simple example, PWC have found the length of the average FTSE 350 company report is now 64% longer than just five years ago, due to the extra reporting requirements.[62]

In terms of those IPOs that do take place, vested interests are again at play, with investment banks often pointing out to companies looking to list that it's going to be quicker, easier and cheaper for them to raise money from institutions than from individual customers. Again, this approach ignores some of the clear benefits from having a more diverse, and active, share register.

In their current form, in other words, IPOs are not really IPOs at all; they are IOs. They don't fall quite as far as short as the Holy Roman Empire, famously described by Voltaire being neither holy, nor Roman, nor an Empire – but still the nomenclature doesn't feel quite right.

60 Ibid.

61 Rick Steves, 'AJ Bell and Hargreaves Lansdown to bring IPOs to retail' (June 2022). Link

62 PWC, annual survey of FTSE350 company reports. Link

This should be addressed as part of a wider shift towards a more supportive environment for retail investment and retail investors – and indeed towards reviving the public markets by making listing more attractive, especially when compared to remaining private or choosing to list overseas.

For example, the Government or the regulators should insist that unless there are highly unusual mitigating circumstances, all IPOs can be accessed by individual investors and on the same terms as institutional investors. This could be through the compulsory use of technology platforms, where organisations like PrimaryBid – who have recently struck an agreement with the LSE – and Peel Hunt – whose REX platform is turning into RetailBook to increase retail participation – could have an important role to play.

But the means matters less than the ends and, indeed, the principle – which is that retail investors need to be given a fair crack of the whip.

Recent reviews and recent attempts to offer more rights to the everyday investor all implicitly acknowledge that the pendulum has swung too far in favour of institutional investment. Attempts to redress the balance are welcome on a point of principle but are also important in practical terms, as they can free up more capital for the public markets.[63]

Despite recent steps in the right direction, more needs to be done to support the interests of individual investors, and the most obvious area for reform is one where the supposed involvement of the public is reflected in the name. At the moment the public are not involved in Initial Public Offerings anywhere near as often as they should be. Nor are there as many IPOs as there should be, resulting in ordinary investors being denied the same kind of growth opportunities as those who already have assets. Neither of these is a good thing for investors, or for Britain.

Recommendation

Regulations should be amended so that a proportion of the new equity offered through Initial Public Offerings should always be made available to retail investors. Companies should consider the most appropriate way to achieve this, which might well be through the use of new technology platforms. The Government should also continue to overhaul the listings regime and regulatory burden to make the public markets in the UK more attractive for companies to list and operate.

Improving ISAs

It would be churlish, and inaccurate, to suggest that the Government does not care about retail investment. In fact, successive governments from both left and right have taken important and admirable steps to try to encourage more people into share ownership, from the public offerings around Thatcher's privatisations in the 1980s, through to the establishment of Personal Equity Plans (PEPs), replaced by Individual Savings Accounts (ISAs).

ISAs, in particular, replaced not just PEPs but Tax-Exempt Special Savings Accounts (TESSAs), with ISAs being available as a vehicle for both stocks and shares (the PEP

63 See, for example, the Economist Intelligence Unit, 'Untapped Capital: Understanding the Retail Investor Pool' (January 2020). Link

replacement) and to hold cash (the TESSA replacement). And the number opened and maintained since that point proves their popularity beyond much doubt.

In total, more than 10 million ISAs have been subscribed to every year since 2008 (the period covered by recent Government statistics), with around 12 million being subscribed to in 2020-21 alone (the last year for which figures are available). Encouragingly, from the point of view of this report, the 2020-21 year also saw a big increase in the number of Stocks and Shares ISA subscribers, which went up by 860,000 compared to the year before.[64] (This may well have been a side effect of people's greater spending and saving power during the pandemic.)

But there is a problem. Ever since the ISA was created, the number of Cash ISAs has dwarfed the number of Stocks and Shares ISAs, even though the latter is very clearly a better savings vehicle in the long term. The trend has been slowly shifting in the direction of shares recently, but in most years the number of Cash ISAs has been somewhere between three and four times as many as the number of Stocks and Shares ISAs.

Type of ISA (thousands)

Financial Year	Cash	Stocks and Shares	Innovative Finance	Lifetime	Total
2014/2015	10,288	2,711	[Not available]	[Not available]	12,999
2015/2016	10,118	2,539	[Not available]	[Not available]	12,657
2016/2017	8,480	2,589	5	[Not available]	11,074
2017/2018	7,018	2,869	49	154	10,090
2018/2019	8,476	2,424	38	223	11,161
2019/2020	9,703	2,727	34	545	13,009
2020/2021	8,059	3,589	16	553	12,217

Source: HMRC

On top of these two forms of ISA – by some distance the most popular – there are the Lifetime ISA and the Innovative Finance ISA, as well as variations on Cash ISAs, such as the 'Flexible ISA', and an ISA for those under 18 – the Junior ISA.

Such is the popularity of the Cash ISA that there have been between 8 million and 12.2 million subscriptions each year, ever year, for all but one of the last 13 years. Taken together, the total holdings in Cash ISAs in the UK comes to just shy of £300 billion.[65]

Given the plethora of different ISAs on offer, and the fact that many people feel uncertain and lacking in confidence when it comes to investment opportunities, it is no wonder some have called for a rationalisation of the number of ISAs on offer.

More important, however, is the need to get people out of cash and into shares. At the best of times, cash is not a particularly sensible way for people to hold their savings – and very definitely not in the high-inflation world which started to take hold in 2022 and into 2023.

64 HMRC, 'Annual Savings Statistics 2022' (June 2022). Link

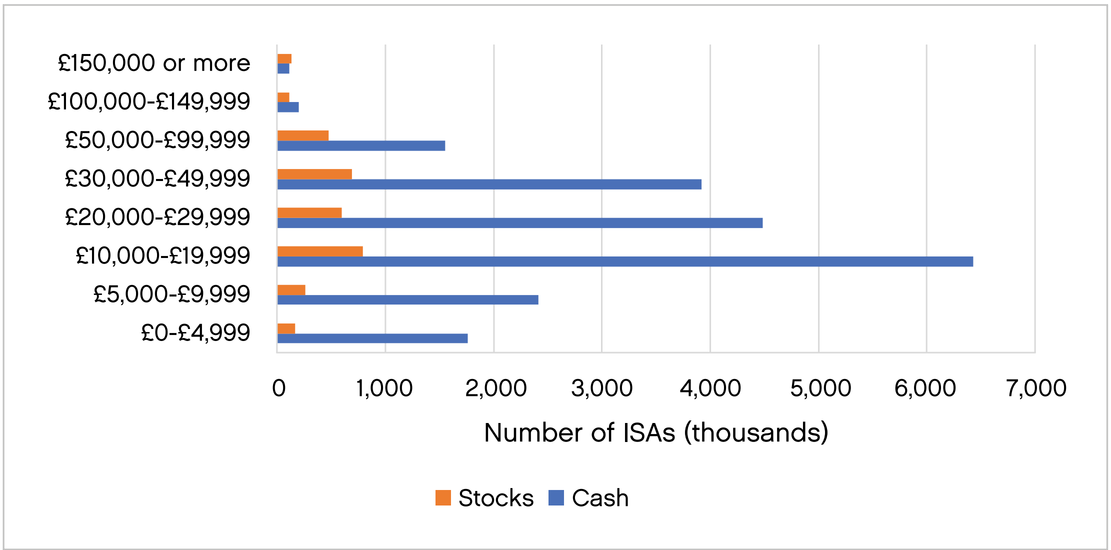
65 Ibid.

There are signs that people recognise this – especially the wealthy. Although there were far more Cash ISAs taken out in 2020-21 than Stocks and Shares ISAs, the percentage of the total market value of ISAs made up of Stocks and Shares ISAs went up from 49% to 58% in just one year. The market value of Stocks and Shares ISAs specifically went up by an astonishing 31%.

Of course, market values can go down as well – but the important point is that the historic performance of equities far exceeds that of cash holdings. This is something which has been explicitly recognised by the FCA who have said that 'over the longer-term people historically have seen better returns through investing excess savings for longer-term needs' and that those with cash holdings 'are missing out on the opportunity of potentially higher returns'.[66]

In that context it is particularly concerning that it is those on the lowest earnings who are most likely to get Cash ISAs. As the table below shows, as you go up the income brackets, people become increasingly likely to take out Stocks and Shares ISAs instead of or as well as Cash ISAs.[67]

Quantity of Stocks ISAs vs Cash ISAs by income bracket (2021)



Source: HMRC

This means that the wealth gap in the UK is only likely to get bigger and bigger – as those with more income accumulate more wealth, while those who are earning less have their holdings gradually reduced by inflation.

Some people might still be determined to hold their savings in cash, despite knowing that inflation will lead to a real-terms fall in their value. But as shown throughout this report, often people simply don't know, or haven't been well advised about, the options that are available to them.

66 FCA, 'Evaluation of the impact of the Retail Distribution Review and the Financial Advice Market Review' 2020. Link

67 HMRC, 'Commentary for Annual Saving Statistics: June 2022' (2022). Link

In the case of Cash ISAs, of which there are many more than there are Stocks and Shares ISAs, there was not a lot to be said for them even before inflation soared, given the record low interest rates that have been available over the last 10 years. But it is even harder to see the justification in this new high-inflation world.

The rational thing to do, therefore, is to push ISA investors towards Stocks and Shares ISAs. This is something that has been recognised by the FCA, who made it clear that they wanted to help those with significant cash holdings (and an appropriate risk appetite) move into shares via their Consumer Investments Strategy.[68] In November 2022 the FCA published a consultation paper which put forward their proposals for how to fulfil this ambition, with the principal means being via 'a new core investment advice regime'.[69]

This paper contained some good suggestions. But there are two bolder and more effective ways in which this goal could be better achieved.

The first, and more cautious, would be to encourage or compel all those firms who have customers with Cash ISAs to write to their customers to tell them about the availability of Stocks and Shares ISAs, point them in the direction of providers (if the original firm doesn't offer them) and confront them with some facts about the historic performance of equities. Crucially, this should also apply to high street banks, and those with large cash savings outside the ISA structure.

The bolder option would be to amalgamate Cash ISAs and Stocks and Shares ISAs into one single ISA wrapper, perhaps as part of the wider rationalisation of ISAs mentioned previously. This could be called a 'Cash and Shares ISA' – or simply 'an ISA'.

This would not be without implications: many Cash ISA providers cannot and would not want to offer share trading, and some Stocks and Shares ISA providers have rules about how much cash can he held. But bringing these two types together into a single tax-efficient wrapper would mean people would automatically get far closer to investment opportunities which might well benefit them far more than keeping their money in cash. And again, advice could be offered making clear the balance of rewards between the different options.

Should this happen, no one should be in any way forced into investing in equities – if people choose to keep holding cash, that should be their prerogative. But bringing information, options and opportunities closer to normal people is vital if we are to have more retail investment. And reform of the ISA system offers about as clear-cut an opportunity as it's possible to have.

Recommendation

Those with Cash ISAs should be made readily aware of the potential returns available via Stocks and Shares ISAs. This could be done via correspondence or by amalgamating Cash ISAs and Stocks and Shares ISAs into a single financial product – a Cash and Shares ISA, or simply an ISA.

68 FCA, 'Consumer Investments: Strategy and Feedback Statement' (September 2021). Link

69 FCA, 'CP 22/24: Broadening access to financial advice for mainstream investments' (November 2022), p 3. Link

Finding a Fund

The big reason why the FCA are right to encourage a shift away from cash and towards Stocks and Shares ISAs is because holding cash will likely lose people money. As the FCA themselves put it: 'We view this [holding cash] as a harm to consumers as, depending on individual circumstances, holding money will see its value eroded by inflation and will miss the historically higher returns available from investing.'[70]

That truth lies at the heart of much of this report and underpins many of our recommendations – including making people more aware of investment opportunities, rethinking our risk appetite as a nation, rebalancing the system in favour of retail investors and pushing people towards Stocks and Shares ISAs.

> **'Between December 2008 and the final quarter of 2022, the return offered by Premium Bonds never rose above 2%. For Direct Saver, the same was true from July 2010 – and for most of that period, the returns it offered were under 1%'**

As we have seen throughout this report, there are literally millions of people with money that could be put to better use by being invested. The most recent Financial Lives Survey suggested that there were 4.2 million people with investable assets of £10,000 or more mostly or entirely in cash, despite having some appetite to take investment risk. If a more realistic assessment of risk was provided, one could expect that figure to move higher, towards the overall figure of almost 10 million people who have that level of investable assets in cash.[71]

Millions of people also have money sitting in savings accounts, sitting in Cash ISAs or invested with National Savings and Investments (NS&I). This final figure is, perhaps the most extraordinary, given the historically poor rates of returns offered by NS&I on both its 'Direct Saver' product and via Premium Bonds. Between December 2008 and the final quarter of 2022, the return offered by the latter never rose above 2%. For Direct Saver, the same was true from July 2010 – and for most of that period, the returns it offered were under 1%.[72]

These poor rates may have something to do with the mandate NS&I has to return funds to the Government, which it is unsurprisingly well placed to do given the returns it offers savers. Its latest published figures revealed it delivered more than £2 billion to Government in just Q2 2022/23 – a sizable chunk of the £6.1 billion it was expected to return over the financial year.[73]

Some might think that is money that should actually be in investors' – i.e. UK residents' – hands rather than the Government's. And that it is something of a scandal that the Government is luring people towards investment vehicles that will leave them not much better off than if they had simply parked their money in cash.

70 Ibid.

71 Financial Conduct Authority, 'Financial Lives survey 2022: insights on the vulnerability and financial resilience relevant to the rising cost of living' (October 2022). Link

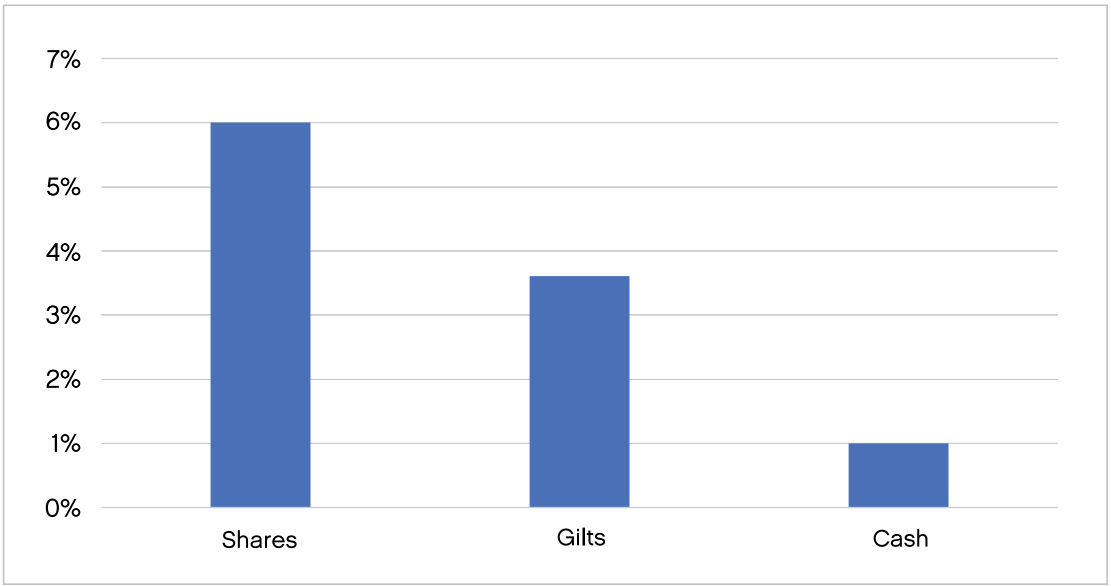
72 NS&I, 'Historical Rates' (accessed 2023). Link

73 National Savings & Investment, 'NS&I Provisional Q3 2022-23 Results and 2023-24 Net Financing Target, (March 2023)'. Link

Nevertheless, the investors keep coming, with NS&I's latest figures suggesting it has reached a record figure of £211.9 billion invested across its range of products.[74]

Whether we're talking about money sitting in Cash ISAs, saving accounts or NS&I, almost all of this money would be better off invested in a diversified portfolio of UK or global equities, a FTSE tracker fund, or any manner of income- or unit-trusts. By failing to invest that money in public markets, individual investors are failing to capture the returns they otherwise might – as this chart tracking average returns of different asset classes over the last 50 years demonstrates.

Annual average of real returns for shares, gilts and cash over the last 50 years



Source: Barclays Equity Gilt Study 2021

As we have said elsewhere in this report, this might be down to a lack of understanding about financial products, an inability to access advice or guidance, or people being put off by disproportionate risk warnings regarding investment opportunities which are actually in individuals' best interests. Clearly, in millions of people's cases, this is not, however, about a lack of investable assets.

Of course, as stated above, there are a huge variety of low-cost tracker funds out there – indeed, their growth has been one of the big stories in the financial markets in recent decades. We would normally be hesitant to suggest creating a state-sponsored rival. Yet the state is, via NS&I, already in the investment business – and it is offering the public a pretty raw deal.

Given people's reluctance to invest, or perhaps their ignorance of the investment markets, there is a case for the Government producing and promoting an investment opportunity which might appeal to those who have money to invest but have not yet chosen to put it in the public markets. Specifically, the Government ought to work to create a new fund or funds, which either invest in a diversified portfolio of UK equities or which operate as an index tracker for UK equities.

74 Ibid.

The Government cannot guarantee returns, of course – and it would not be appropriate to offer any sort of compensation scheme, along the lines of the Financial Services Compensation Scheme for savings, if money was lost. The whole point is that this is risk capital which *might* lose money, but the historical data suggests that in the long run it won't. And obviously the Government would not make investment recommendations itself, let alone of particular stocks.

But a fund of this sort would offer all sorts of benefits to individuals, to companies and to the economy at large.

Individuals would be able to access the higher returns which are more likely to come from equity investments and, through the diversified product on offer, would reduce the risk of being over-exposed to individual equity holdings.

> **‘Whether we're talking about money sitting in Cash ISAs, saving accounts or NS&I, almost all of it would be better off invested in a diversified portfolio of UK or global equities’**

Companies would have a new source of funding, which would both enhance their liquidity and provide them with patient capital – both important issues in the UK context.[75] [76]

The economy would benefit from those companies getting the funding they need to grow and through a growing investor community with more wealth and more confidence to invest in the future.

In other words, everyone would benefit. As the FCA have said: ‘The consumer investments market can help to improve people's lives. It performs a vital function in allowing people to provide for later life, to save for major expenses or for a home, and can help them deal with unexpected shocks. A well-functioning investment market also channels money to companies looking to grow and innovate, supporting the UK economy.’[77]

There are multiple different organisations which could take this idea forward. Ironically, NS&I might well be a suitable home for this fund, given people's familiarity with the brand and trust in its products. Alternatively, the British Business Bank might be well-placed to develop such an offering, given their close working relationship with the Government and regulators and their national reach.

Some will say there are market solutions which can supply this sort of product and therefore Government does not need to act. But the Government's involvement does not need to be either active, or even long-term. Having Government create and back this fund (or these funds) would provide confidence to would-be investors and show its support for investing in the public markets. It would be a natural, and helpful, extension of the earlier recommendation to promote the public markets through an

75 GOV.UK, ‘Patient Capital Review’ (October 2017). Link

76 To put London's lack of liquidity into perspective, the total daily volume traded on the London market in January 2023 was £3.7 billion. Tesla, the US's most traded stock, has more than £30 billion traded on an average day.

77 FCA, ‘Evaluation of the impact of the Retail Distribution Review and the Financial Advice Market Review’ (December 2020). Link

advertising campaign – both pointing out the opportunities and pointing the public towards an appropriate product. If at some point in the future the state wanted to sell off its interest, once the case has been made and millions of new investors have been created, it could of course do that.

The more fundamental point is that the private sector is currently failing to convince individual investors to invest in this sort of product, or indeed public markets more generally. That is why there are billions of pounds sitting in NS&I products, in Cash ISAs and in bank accounts and why (to repeat ourselves yet again) there are 9.7 million people with investable assets of £10,000 or more who hold most or all of that money in cash.

The creation of this fund would ensure that those figures were dramatically reduced. It would provide people with the confidence to invest and companies with capital to grow. In so doing it would help people increase their wealth, help businesses to fulfil their potential and, ultimately, help the UK economy thrive.

Recommendation

A new national fund should be created, which might invest directly in a diversified portfolio of UK equities or operate as an index tracker for the main FTSE index. The new fund should be explicitly backed by Government to instil confidence in new investors and established by an organisation which would give potential investors confidence about the prospects of investing in UK equities – such as NS&I.

Conclusion

Deep and liquid public markets are essential if the UK is going to forge the sort of dynamic economy which will create jobs, opportunities and the wealth of the future. Yet at the moment, these markets are not as deep as they should be – in part because retail investors invest nowhere near as much in the public markets as they could.

This is bad for individuals, for companies, and for Britain. A core part of the problem is that a huge amount of British citizens' savings is currently sitting in the form of cash, providing very limited returns, and not helping forge this dynamic economy.

There was a time when it was an explicit ambition of Government to encourage more retail investment and to develop a 'shareholder democracy'. The wind has, alas, gone out of those sails.

'By encouraging more retail investment not only would the Government be unlocking more funding for the most productive parts of our economy, but it would be helping people to help themselves, their communities, the economy and our society as a whole'

A retail investment strategy is now needed to make it easier and more obvious for consumers to invest in public markets. By encouraging more retail investment not only would the Government be unlocking more funding for the most productive parts of our economy, but it would be helping people to help themselves, their communities, the economy and our society as a whole.

Steps need to be taken in different areas.

First, there needs to be a recalibration in terms of attitude to risk. Friedrich Hayek once asked: 'Is there a greater tragedy imaginable than that in our endeavour consciously to shape our future in accordance with high ideals we should in fact unwittingly produce the very opposite of what we have been striving for?' At the moment, regulation is harming the very people that it is supposed to benefit. That needs to be addressed.

Second, more needs to be done around information and awareness – to sell retail investing as a concept. Too many people don't understand the wealth-generating opportunities available to them and are missing out on accruing wealth as a result. The Government and others need to help make it an obvious, almost default, option for people to consider.

Finally, we need to make it easy for people to invest. Whether by ensuring the odds aren't unfairly stacked against retail investors, through reforming products, or even creating new ones, we need to ensure retail investors can access opportunities on the public markets quickly and easily.

Giving more and more people a stake in the economic success of our country not only means that they can benefit as individuals, but that society as a whole benefits, as companies can grow faster, pay more taxes and fund more public services. This virtuous circle starts and finishes with individuals' access and exposure to investment opportunities.

'A society which has more retail investors is likely to be more prosperous, fairer and better governed. The need to encourage more retail investment is more urgent than ever before'

This harks back to points made earlier in this report about attitudes towards capitalism. The fact is we can only expect people to endorse and support capitalism if they feel like they have a stake in it – which is where share ownership comes in.

A society which has more retail investors is likely to be more prosperous, fairer and better governed. The need to encourage more retail investment is more urgent than ever before.

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