Fairer Finance

Creating a fairer financial services market for consumers and the businesses that serve them

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Fairer Finance

Meeting the Fair Value test

Fairer Finance Talks The Consumer Duty Series

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About Fairer Finance

Fairer Finance is a ratings agency, consultancy, and consumer group with a mission to create a fairer financial services market.

We do this by publishing our unique ratings – and by working with companies who want our help and expertise to do better.

What we'll cover today

- Informing decisions
- Benchmarking fair value
- Win-win business models
- Discussion with Q&A

Who we are

James Daley,
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Financial Conduct
Authority

Graeme Reynolds,
Director of Competition, FCA

The fair value test

The competitive market test

Are customer outcomes in line with what we would see in a well-functioning, competitive market?

- Customers make informed decisions.
- There is a reasonable relationship between your product features, service quality, and price.
- Win-win business models. Profitability is not reliant on poor customer outcomes.

Customers make informed decisions

- You understand the information you need to make an informed decision. This means you understand how the product compares to competitors on service and features, and what you might pay for a similar product elsewhere.

or…

- You do not understand how the product compares on service and price, or what you might pay elsewhere. However, the product is sufficiently strong across price, product features, and service. So, you're still getting value – despite being less well-informed.

Informing decisions...

Some firms are very open about what the product does, and does not do.

Feature comparison

We believe in transparent banking, and we want to be clear on what you will, and won't, get with a Triodos Current Account.

We offer:

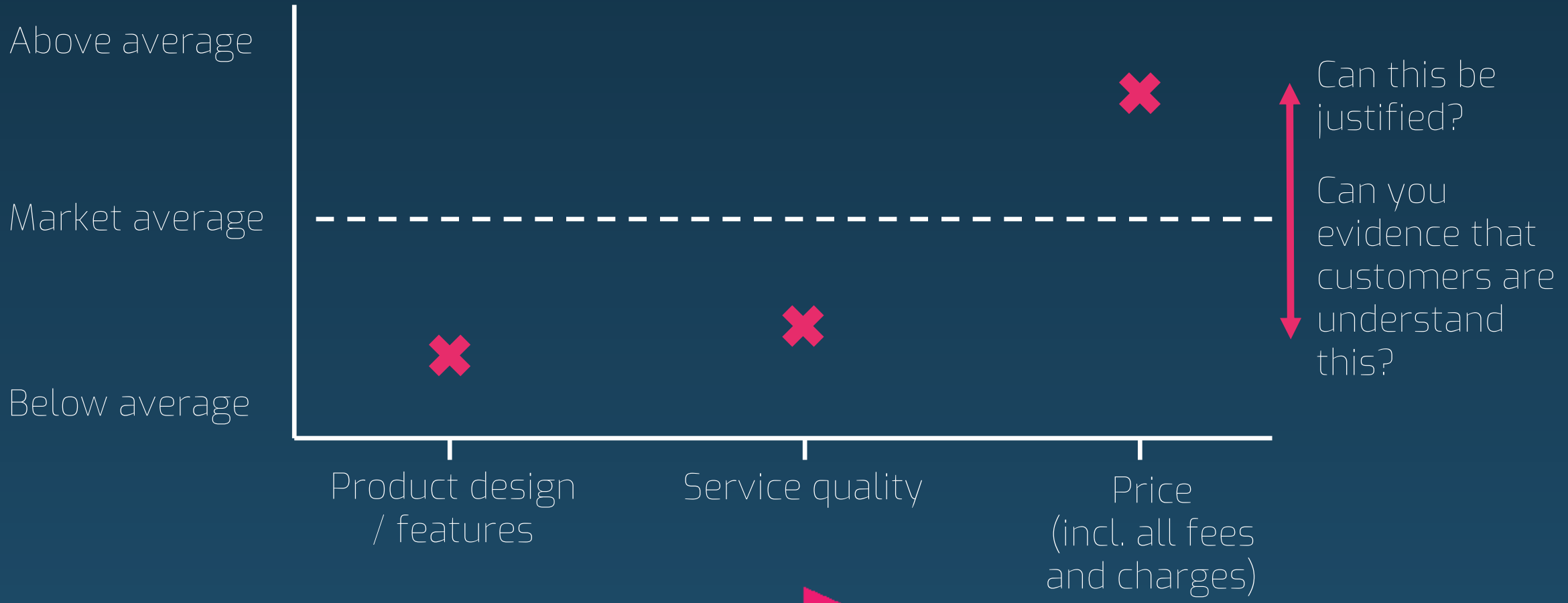
- ✓ Contactless Debit Mastercard.
- ✓ Online banking through internet banking and our mobile banking app.
- ✓ Online statements.
- ✓ Text message alerts to help manage your money.
- ✓ Secure messaging in Internet Banking.
- ✓ Securely access Internet Banking with the Triodos App (using a second device to scan the QR code on the login screen).
- ✓ Overdraft of up to £2,000 for a specific purpose, available on request. Subject to affordability and credit checks.
- ✓ Cheque book available on request.
- ✓ Telephone support available Mon to Fri: 8am-6pm, except Thu: 9am-6pm (out of hours card services provided 24/7).

We don't offer:

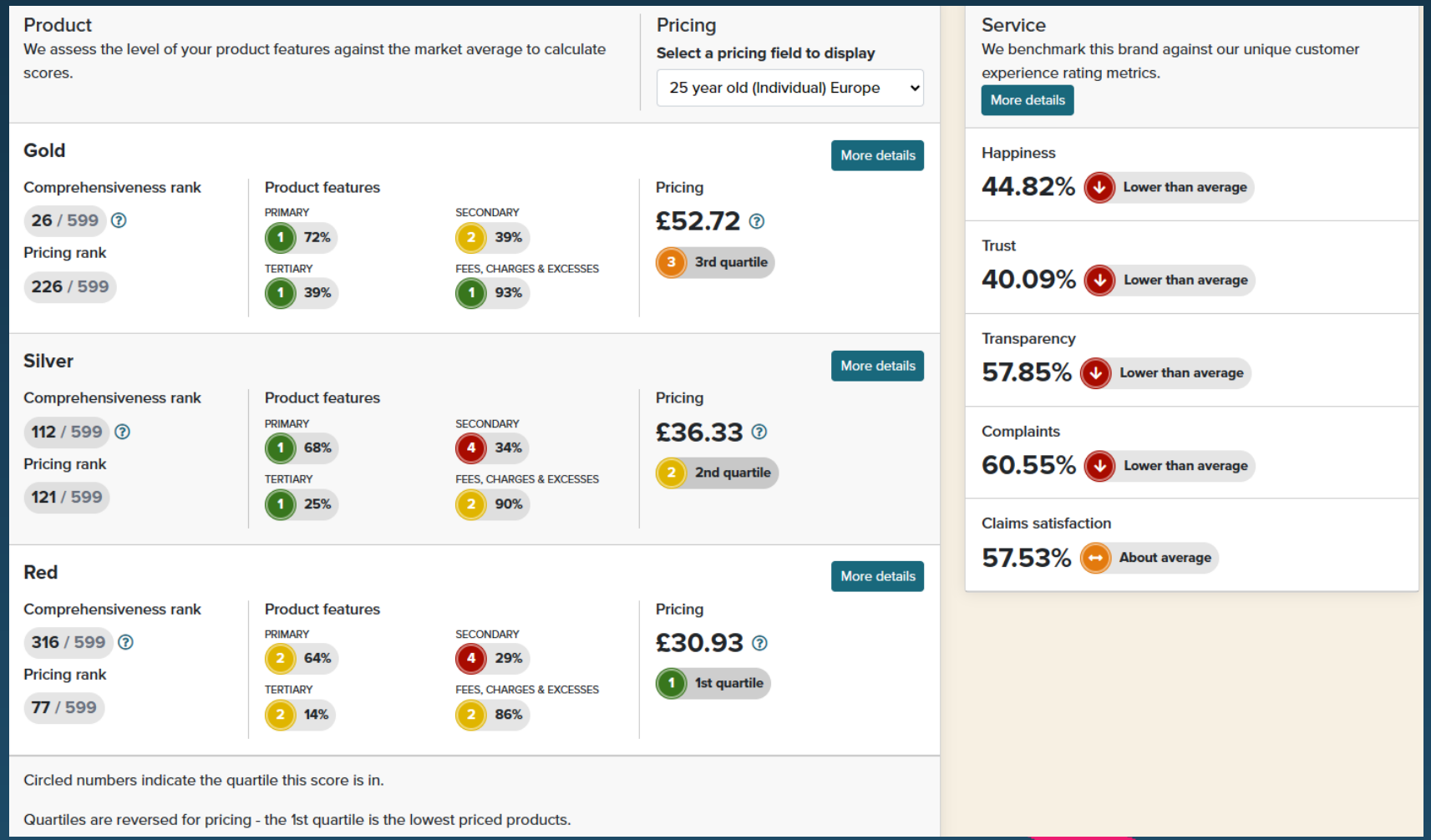
- ✗ Apple Pay or Google Wallet (Google Pay, Android Pay). **Find out why**.
- ✗ Interest on balances held in your current account.
- ✗ A unique IBAN. **Find out how to receive an international payment**.
- ✗ In-app messaging or live chat for customer support.
- ✗ Paying cash into your account with over-the-counter services, like the Post Office or PayPoint.
- ✗ Immediate Faster Payments. Please see our payment timescales below.

Source: Triodos Bank, https://www.triodos.co.uk/current-accounts/current-account

Benchmarking features, service, and price



Benchmarking fair value



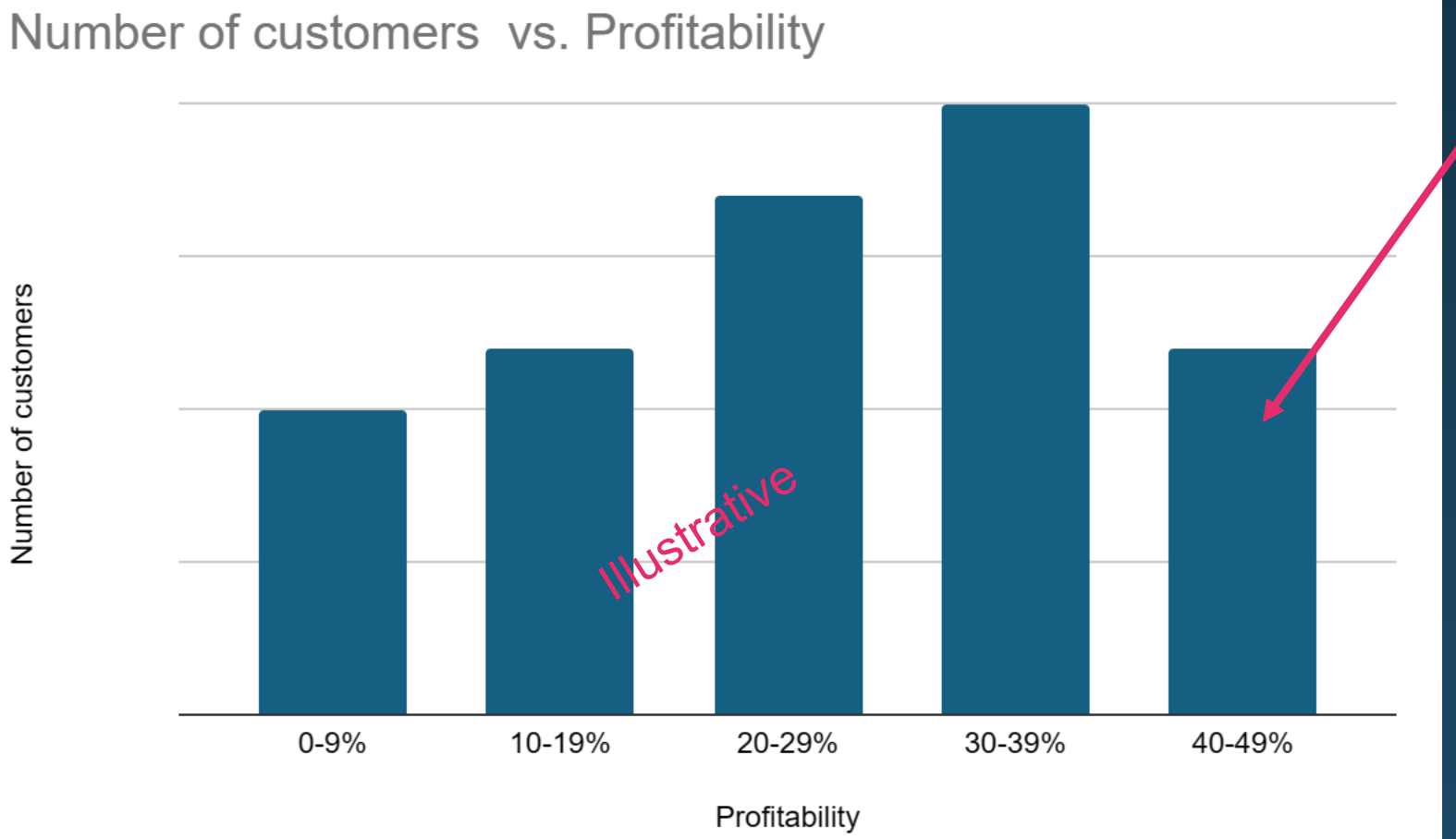
Source: Fairer Finance, Fair Value tool, https://www.fairerfinance.com/the-fair-value-report-tool

Win-win business models

Follow the money…

- Analyse the full distribution of customer outcomes.
- Is your business model reliant on a group of customers who are receiving poor outcomes? Or do you have a win-win business model?
- Do you generate cross-subsidies? If so, have you quantified these, and then justified the extent of the cross-subsidy?
- Is the profitability of products in-line with what we would see in a competitive market?

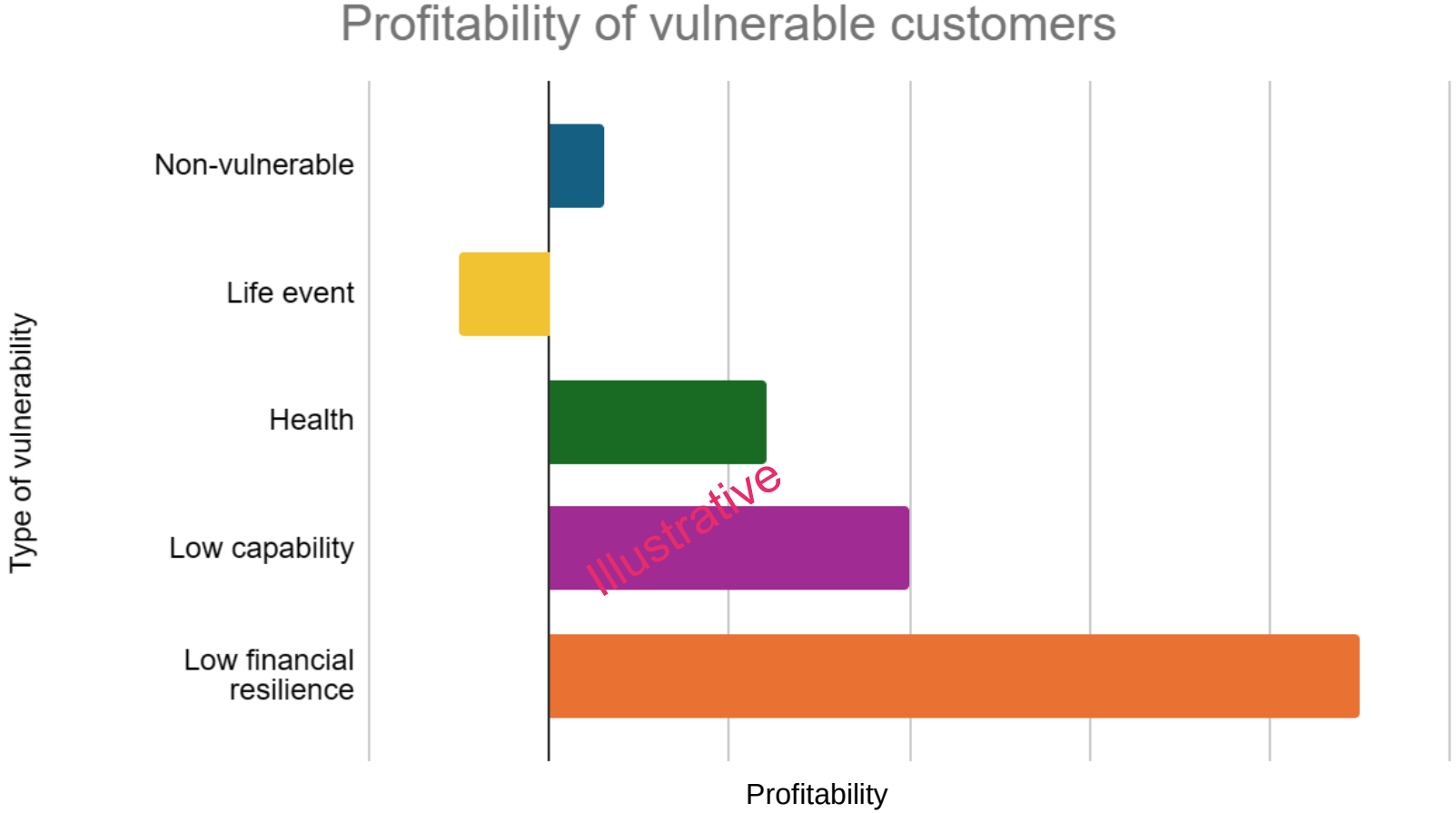
Who are the most profitable customers, and why?



What customer behaviours / characteristics drive profitable outcomes for the business?

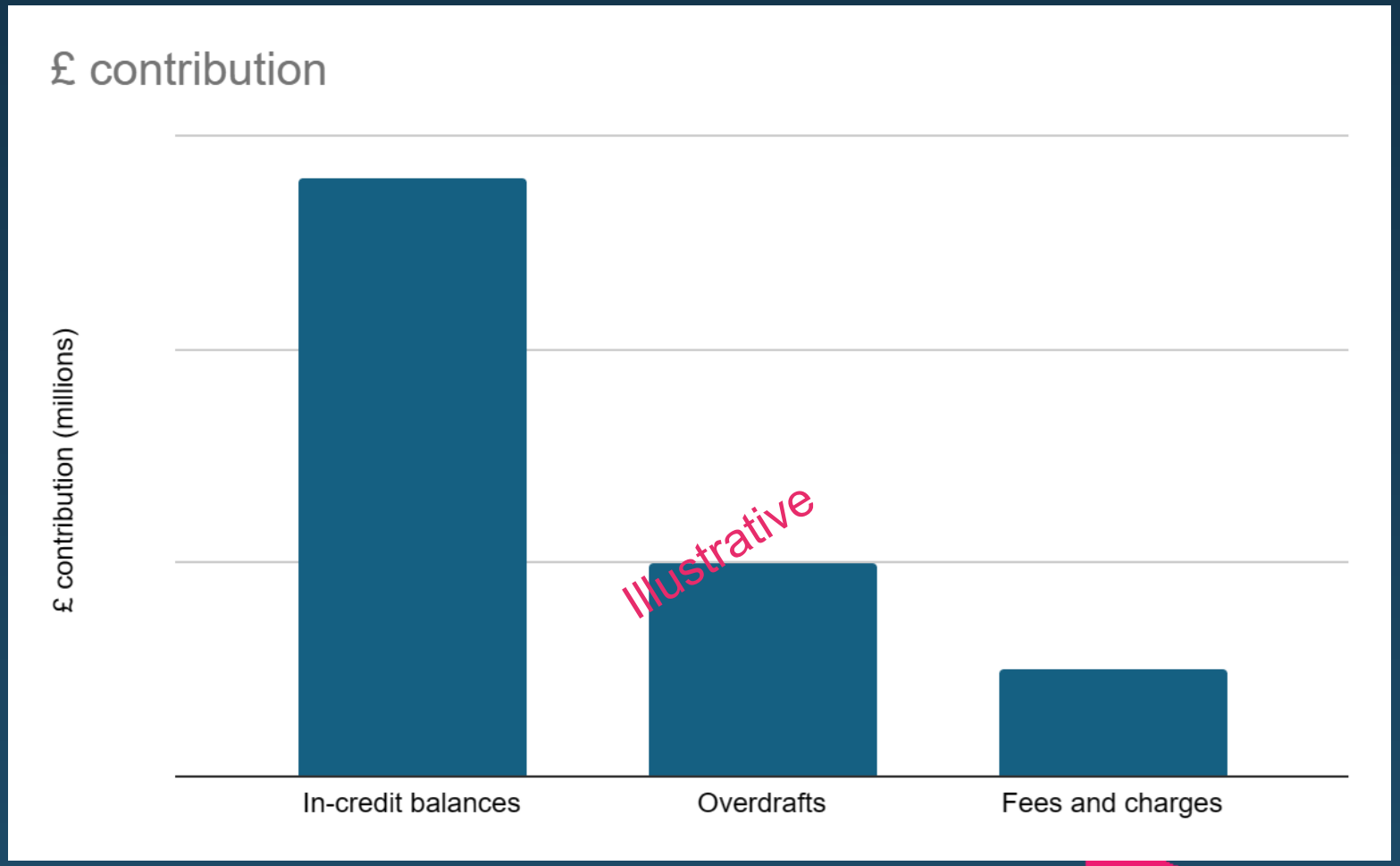
Get to the heart of the business model by analysing the distribution of outcomes (cohorts, individuals).

Profitability by cohort



Let your thinking on potential customer harms guide your thinking on customer segmentation in your fair value assessment.

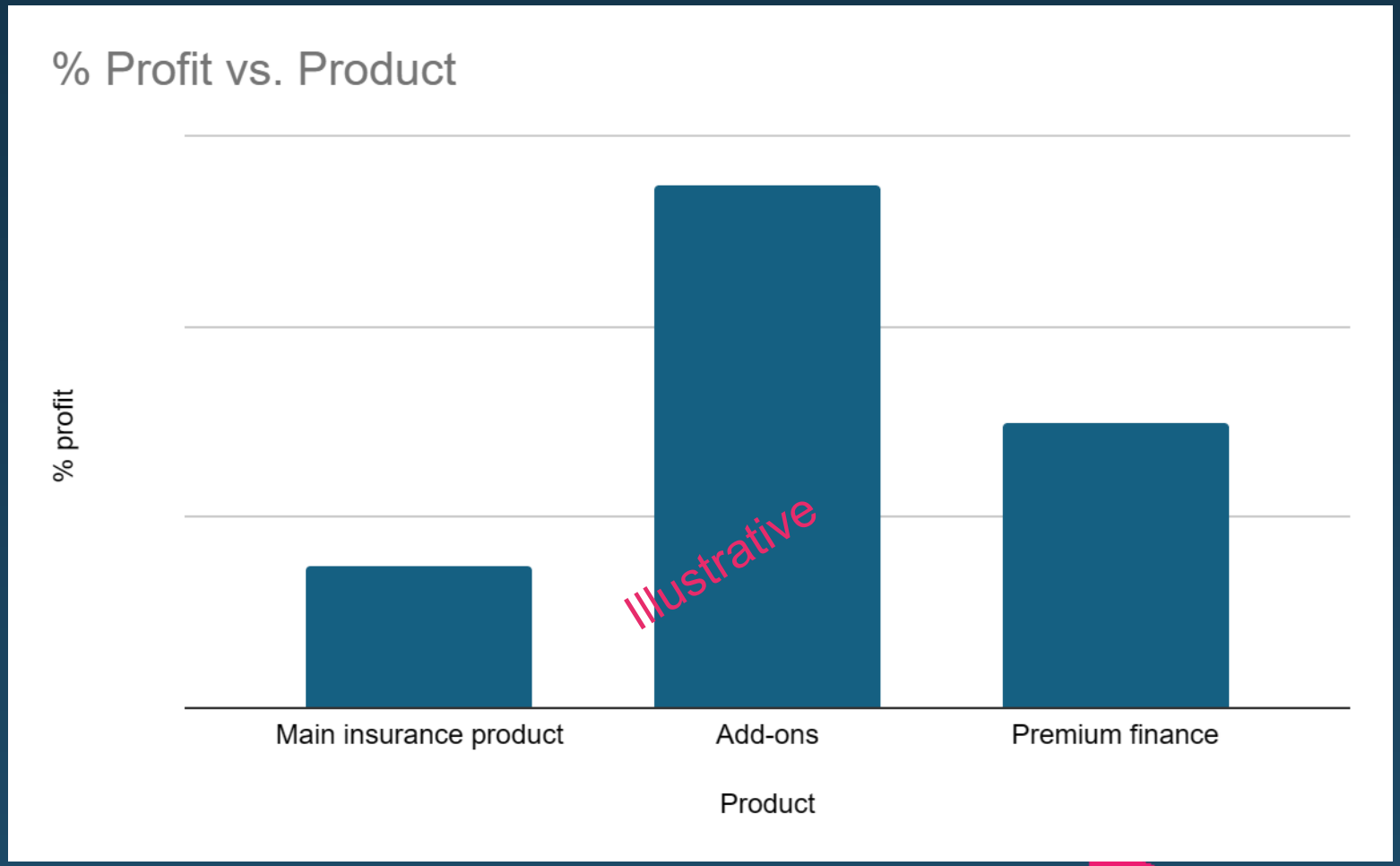
Profitability by product (I)



What customer behaviours drive profitable outcomes for the business?

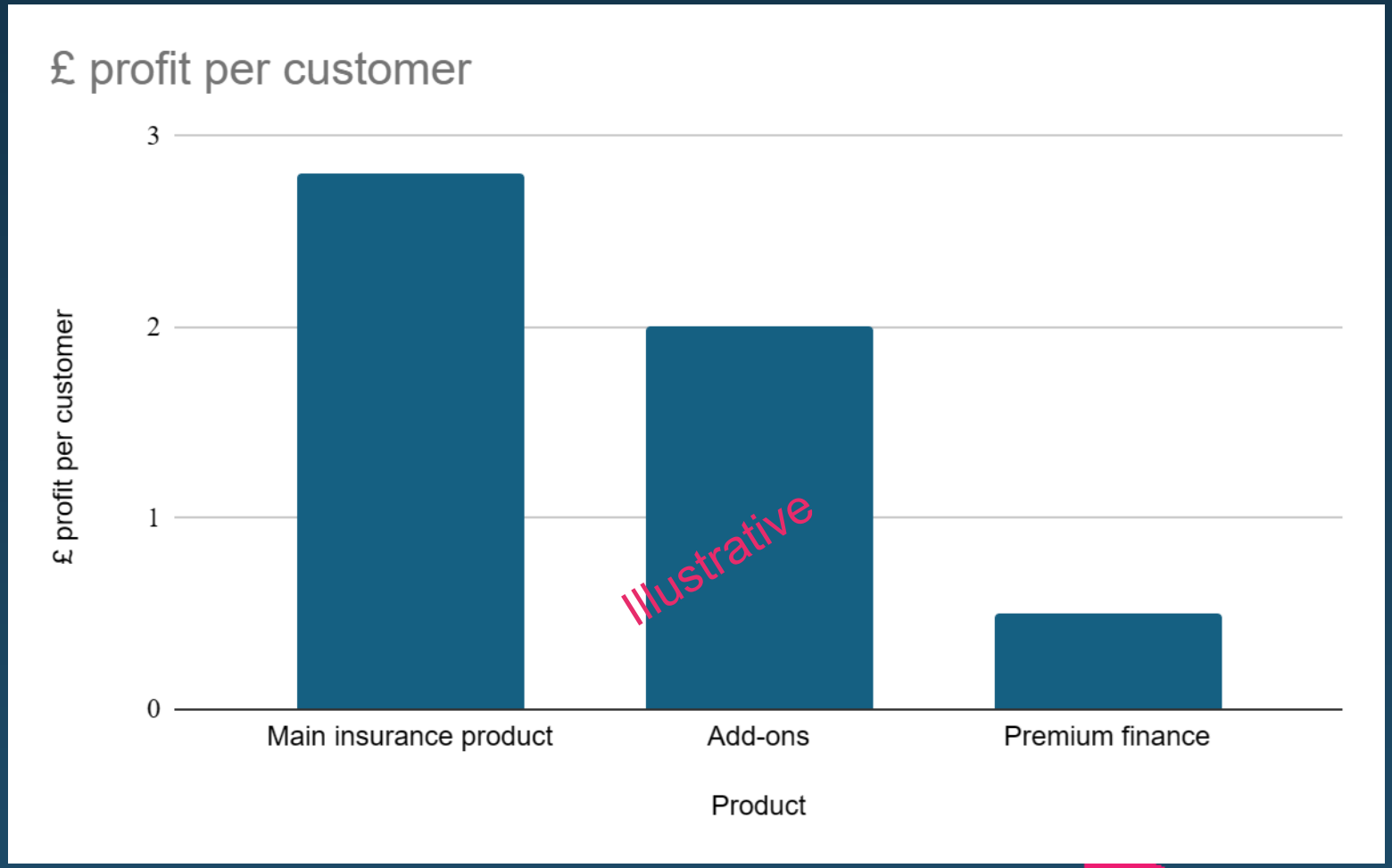
Have you stress-tested your fair value? What would profitability look like under different macroeconomic conditions?

Profitability by product (II)



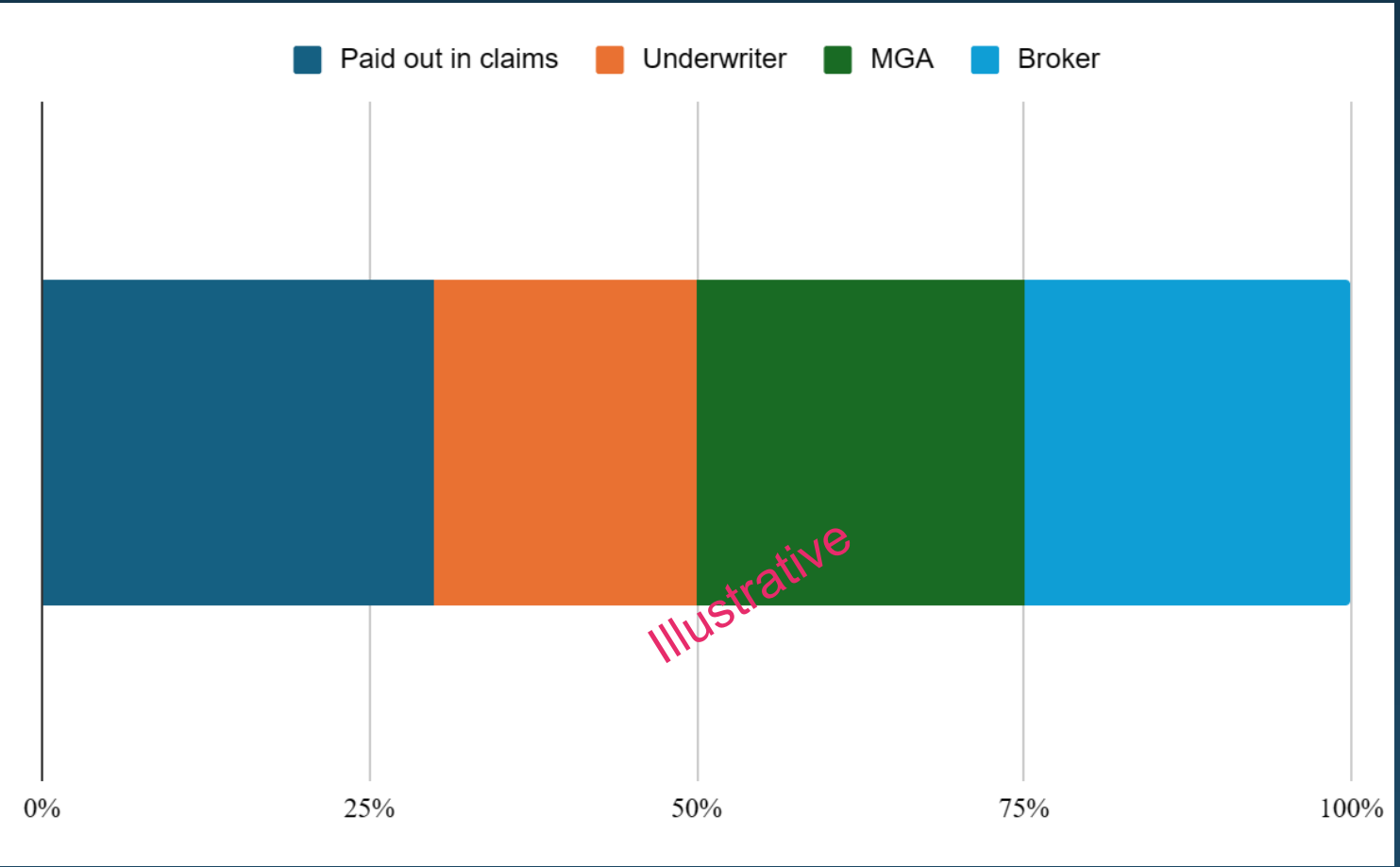
In general, larger margins require better evidence to justify that the value test is still fulfilled.

£ versus %



Add-ons may represent a high % profit margin – but a low £ contribution.

Value up and down the distribution chain



- Manufacturers must understand what cut distributors are taking and see the supporting evidence that this is reasonable.
- All commissions must be justified, individually and in aggregate.
- Distributors need to have sight of manufacturer's fair value assessments.

Key takeaways

Evidencing fair value: key questions to ask…

Is there a reasonable relationship between your product, service, and price, relative to the market?	Within your customer base, what is the distribution of outcomes?	Are your customers making informed decisions?
1. After adjusting for service quality and product features, are your prices in line with what customers would expect? If not, why not?	2. Who are your most profitable customers, and why? 3. Is your business model reliant on a group of customers who are receiving poor outcomes? Or do you have a 'win-win' business model? 4. Do you generate cross-subsidies? If so, have you quantified these, and justified the extent of the cross-subsidy? 5. Is the profitability of different products (including add-ons) in-line with what we would see in a competitive market?	6. Which are the key features, costs, risks, and limitations of the product about which a customer must understand to make an informed decision? 7. Can you demonstrate that your customers understand how their behaviour affects the value they enjoy? 8. Can you prove that the customers who enjoy the least value are making informed decisions about their product usage and behaviour? 9. Do your customers understand the value equation? For example, if prices appear out of line with product features and quality of service, can you prove that your customers are aware of this and choose to purchase the product anyway.

Appendix

The Fairer Finance fair value framework

(1) Is there a reasonable relationship between your product, service, and price, relative to the market?

Can the differential between your prices and market prices be justified by differentials in product features and quality of service?

We benchmark your product features, pricing and quality of service to the market. We analyse Fairer Finance product ratings and customer experience polling; publicly available data; and your own data.

(2) Within your customer base, what is the distribution of outcomes?

Follow the money: which customers generate the most profitability? Why is this? Who are these customers? Does a certain type of customer drive the business model? (e.g. vulnerable customers) How does customer behaviour and product usage affect outcomes and profitability?

We analyse on your data on margins, costs, and revenues by customer.

(3) Are your customers making informed decisions?

Do customers understand the value equation? For example, if prices appear out of line with product features and quality of service, can you prove that your customers are aware of this and choose to purchase the product anyway.

Do customers understand how their behaviour affects the value they enjoy? Can you prove that the customers who enjoy the least value are making informed decisions about their product usage and behaviour? Or are customer decisions poorly influenced by the design of the choice architecture?

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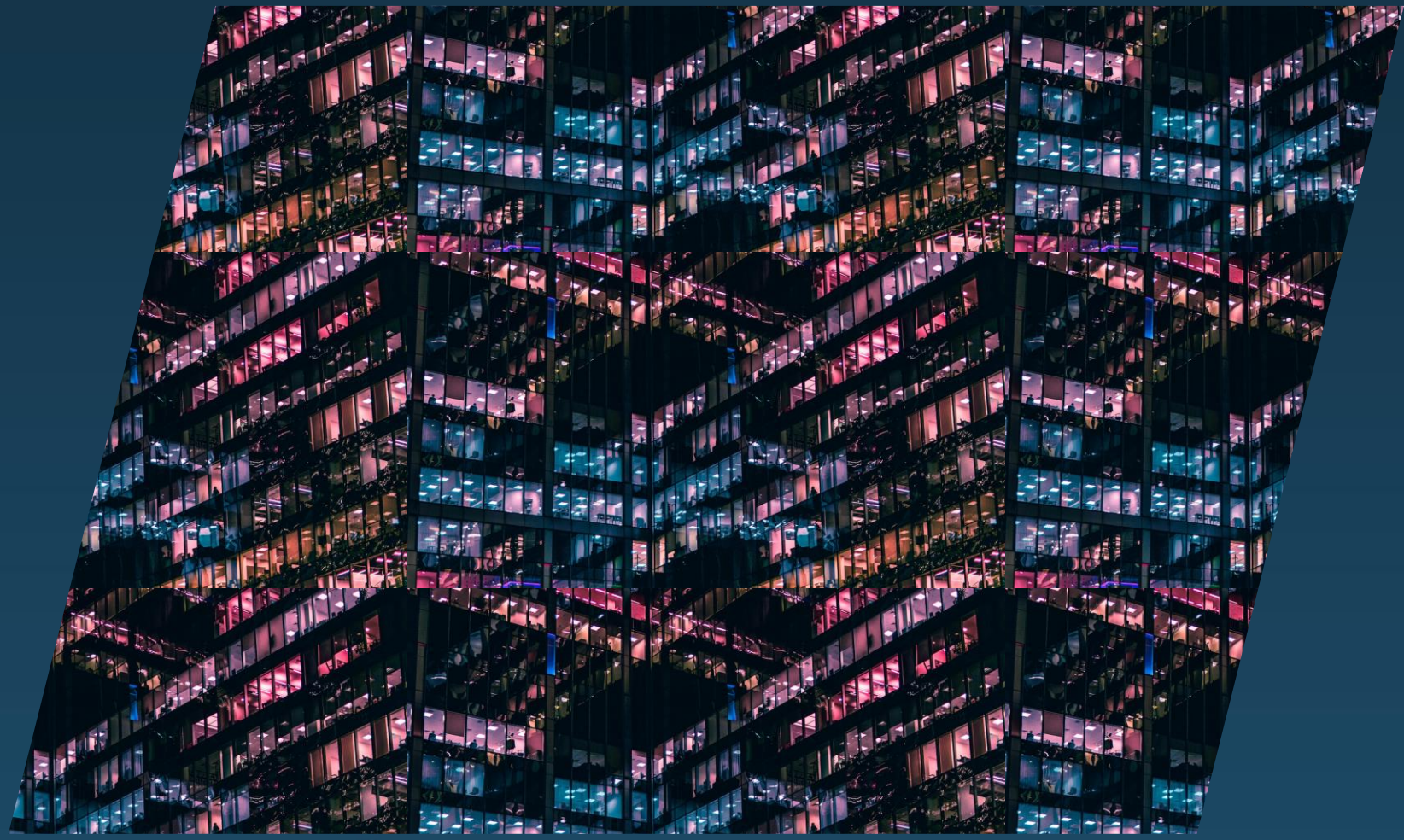

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