

Financial inclusion in the UK: Review of policy and practice

Findings
Informing change

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Financial exclusion is the inability, difficulty or reluctance to access appropriate, so-called mainstream, financial services. The reduction of financial exclusion is a priority for the present government because it can lead to social exclusion. This study was a review of current policies and practices aimed at reducing financial exclusion. The financial services covered included money and debt advice, financial capability, banking, affordable credit and insurance.

Key points

- People outside the mainstream financial services suffer financial disadvantages including: higher-interest credit; lack of insurance; no account into which income can be paid; and higher-cost utilities.
- Even those with bank accounts may barely use them, preferring to withdraw all their money each week and manage it as cash.
- Those particularly vulnerable to financial exclusion include: housing association tenants; young people not in employment, education or training; those leaving care; lone parents and divorced people; disabled people, those with mental health problems and carers; people living in isolated or disadvantaged areas; prisoners, ex-offenders and families of prisoners; members of ethnic minorities; migrants; asylum seekers and refugees; homeless people; older people; women; people with a Post Office Card Account or basic bank account; people with low incomes.
- The number of adults in the UK without a bank account fell from 2.8 million in the financial year 2002–03 to 2 million in 2005–6. Despite this progress, there will continue to be people who cannot take full advantage of bank accounts and other financial services. The reasons for this depend on the different characteristics of vulnerable groups; all are exacerbated by low income.
- Much financial exclusion is caused by a complex set of factors. Consequently, financial exclusion initiatives must address many different issues. These include: geographical exclusion e.g. resulting from branch closures; failure to qualify because of poor credit history or problems in supplying identity document requirements; the relative cost of financial products and services e.g. charges for unauthorised overdrafts; and cultural and psychological barriers.
- In an increasingly cashless future economy the consequences of not holding a bank account are ever more exclusionary.

The research

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Background

Financial inclusion has two elements: good financial decision-making (the 'demand side' of the equation) and access to suitable products and services (the 'supply side').

Good financial decision-making requires:

- Financial literacy, or a basic understanding of financial concepts.
- Financial capability, or the ability and motivation to plan finances, seek out information and advice, and apply these to personal circumstances. Financial capability is increasingly important, as the range of financial products becomes more complex. The need for financial education is continuous through people's lives as the market and personal circumstances change.

Poor financial decision-making can, of course, affect people not on low incomes. However, those most affected are those who will suffer a greater loss of welfare as a consequence of poor decisions. Better-off people are more likely to have a cushion of financial assets or access to affordable credit and so may be able to get by with only a rough knowledge of how much they earn and how much things cost: they are not financially excluded.

Implications of financial exclusion

Financial exclusion is a current policy concern because it creates financial problems in the following ways:

- Exclusion from affordable loans leaves people who need to borrow money with no option but to use high-interest credit.
- A lack of insurance and savings makes families vulnerable to financial crises following unexpected events such as burglary or flooding. A lack of savings can lead to poverty in old age.
- Many employers will only pay wages into a bank account.
- Cheque cashing agencies may charge 7 to 9 per cent of the value of the cheque plus a fee for the transaction.
- Not having a bank account with a direct debit facility excludes people from this method of paying bills. Most utility suppliers charge more for using other methods of payment, such as pre-payment meters, pay-point cards in convenience stores, postal orders or cash.

Financial exclusion reinforces social exclusion. It is not just an individual problem: a whole community can suffer from under-investment in financial services. Conversely, financial inclusion significantly contributes to a route out of poverty.

Policy context

In the last ten years, financial exclusion has emerged as a policy concern and funding has been made available at both national and local levels. There are many different initiatives under the auspices of different government departments and statutory bodies. In addition there is divergence between the policies in England and the devolved administrations. The voluntary and private sectors also play a crucial role in providing services to financially excluded groups.

There is currently a push for financial advice to be more widely available. The aim is to ensure that there is greater access to high-quality, affordable and 'sales-free' financial advice for those who are most vulnerable to the consequences of poor financial decision-making. The Thoresen Review feasibility study of 'generic financial advice' – also referred to as 'money guidance' – published its final report in March 2008 (Thoresen Review of Generic Financial Advice: Final Report, HM Treasury).

Aims of the study

The aims of this study were:

- to identify which groups appear likely to remain financially excluded in the future;
- to identify the strengths and weakness of current financial inclusion initiatives;
- to look at how policy makers and practitioners can address the needs of the financially excluded.

The research was complicated by the very many financial inclusion initiatives currently taking place and the fast-moving nature of this field. In addition, because government investment in financial inclusion is relatively recent, many initiatives remain at the early stages or are short term and so few have, as yet, been properly evaluated.

Groups particularly vulnerable to financial exclusion

In identifying those 'vulnerable groups' which are being left out of current initiatives – either entirely or through inadequate or inappropriate provision – the study found that the need in this area is so great that all the groups looked at were likely to be vulnerable to financial exclusion into the future. Some groups are particularly vulnerable for reasons which are separate from, or interact with, having a low income, such as disabled people and older people. Nevertheless, low income is an exacerbating factor for all groups. In assessing vulnerable groups the research found that the gap between those making best use of financial services and those unable to do this looks likely to widen.

Money and debt advice services and financial capability initiatives

The study highlighted the huge diversity of financial inclusion work taking place. It was clear from the sheer number of initiatives identified that what helps one group of clients may not help another. The variety of advice being offered is not necessarily a problem because of the diversity of needs, and because of the way financial exclusion interlinks with the other problems a person may be facing. Nevertheless, considerable work remains to be done to identify what is effective for different types of client. It was impossible to fully evaluate the impact of this work within the time span of this study. However, data from the interviews suggests that successful initiatives shared the following features:

- Intervention occurred at the point when the client was ready to receive advice or was looking for financial help.
- They enjoyed continuity of funding, enabling an on-going service to be provided.
- They used trained staff. In some cases, money advisers were trained in the needs of vulnerable groups. In others, financial training was given to those already working with particular groups.
- The service was effectively marketed to potential clients.
- The service was seen as independent and trusted.
- Partnerships with other relevant organisations were developed.

The study's recommendations to money and debt advice services and financial capability initiatives were:

- To understand the specific needs of the target group in terms of where, when and how to deliver assistance, and the topics to be covered.
- To make cross-referrals, recognising that financial exclusion may be only one of several problems faced by an individual.

Recommendations for central, devolved and local government departments were:

- To provide more assured, long-term funding to money and debt advice and financial capability projects. This will ensure that experienced staff are not lost to the sector, and recognises the long-term nature of clients' needs.
- To continue to invest in the financial training of advice workers, particularly those working generally with a specific vulnerable client group.
- To ensure that the current government push for generic financial advice is sufficiently targeted, since the most successful projects are tailored to clients' circumstances.

The financial services industry

Recent changes in the financial services industry have increased the risk of financial exclusion for some groups, but have led to greater financial inclusion for others. The gap will widen further between those who stand to gain from being able to make the use of direct debits, online banking and text banking, and those whose main reason for financial exclusion is that their financial resources are stretched and who find it easier to use cash.

For those in danger of being left out, banks need to help customers on low incomes to control their finances by offering suitable financial products.

Credit unions (third-sector lenders) are an important means of tackling financial and social exclusion, but they cannot lend to the most high-risk customers. Therefore, the accessibility of the Social Fund should be monitored by the Department for Work and Pensions. So, for example, any difficulties in getting through on the phone to make a claim should be monitored.

Recommendations for the financial services industry were:

- When planning services, consult those groups who are likely to be financially excluded so as to understand their needs.
- Ensure that consumers receive clear, simple and understandable information.

Recommendations for central, devolved and local government departments were:

- Continue to monitor the impact of technological, macro-economic and demographic changes on access to financial services by the specific vulnerable groups identified in this report.

The roles of the different sectors

In terms of the balance of roles of the different sectors, the answer lies in a co-ordinated approach by the public, private and voluntary sectors. This will have to be led by government because people on low incomes are the least attractive customers to banks and other service providers. Credit unions are not widespread enough to be a single solution to high-cost lending, nor can they afford to take on the highest risk customers. The Financial Inclusion Taskforce will also have to continue to engage mainstream financial service providers who, otherwise, will be unlikely to make major changes to the services they offer to vulnerable groups.

Financial exclusion in the future

The study concluded that, overall, the number of those without access to banking services will continue to fall while the need to have a bank account will increase. Despite the impact of current policy and practice initiatives to combat financial exclusion, there will continue to be people who cannot take full advantage of banking and other financial services. There are many different reasons for this, depending on the different characteristics of particular vulnerable groups, but they are all exacerbated by low income.

About the project

The methods of the study included:

- Systematic searches of existing research studies and databases.
- An email survey sent to 233 organisations across the UK.
- Interviews with 11 umbrella organisations for background information
- Telephone interviews with representatives of 52 organisations, chosen to cover a range of types of project, target group, size and UK regions.
- The use of the database of Transact (a network for people interested in financial inclusion) as a source.
- Geographically, the interviews covered England, Northern Ireland, Scotland and Wales.

For more information

The full report, **Financial inclusion in the UK: Review of policy and practice** by Lavinia Mitton, is published by the Joseph Rowntree Foundation.

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