Financial inclusion

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Introduction – What is financial inclusion?

The OECD define financial inclusion as:

> 'the process of promoting affordable, timely and adequate access to a wide range of regulated financial products and services and broadening their use by all segments of society through the implementation of tailored existing and innovative approaches, including financial awareness and education with a view to promote financial well-being as well as economic and social inclusion' (OECD, 2014: 26).

In the UK, Kempson and Collard (2012) have suggested that people who are financially included have the ability to: manage day-to-day financial transactions via a transactional (bank) account; save to meet one-off expenses; manage a loss of earned income; invest in a pension; access insurance; and avoid/reduce problem debt.

Financial inclusion first emerged on the UK social policy agenda in response to bank branch closures in the early 1990s. From then on, this issue was championed by New Labour who set up the Financial Inclusion Taskforce in 2005 to help improve access to appropriate and affordable financial products and services. The Financial Inclusion Taskforce made some progress but since the global financial crisis, household incomes have become increasingly squeezed, making it difficult for people to achieve financial inclusion, as defined above. This paper explores current levels of financial inclusion and briefly reviews recent government policy before considering the future of financial inclusion.

Current levels of financial inclusion

There is no single measure of financial inclusion but one of its most fundamental elements is to have a sufficient and secure level of income with which to meet basic needs. Since the economic crash of 2007, however, unemployment has gone up and incomes have been squeezed still further. With wages stagnating and benefit cuts biting, it has become increasingly difficult for people to manage financially. In fact, survey findings suggest that in order to make ends meet, the majority of the population (57%) were cutting back on their spending in 2014. Much of this economising was on non-essentials such as eating out and luxury food but one in ten manual workers had cut back on basic food items (Rowlingson and McKay, 2014).

One of the key components of financial inclusion is to have sufficient savings to meet one-off expenses and/or shortfalls in income. Whilst many people recognise the significance of saving, only 41% of people said they were actively saving in 2010-11 (Rowlingson and McKay, 2014). It is unsurprising that those with the highest income were more likely to save than those on the lowest incomes and that those with the highest incomes were also able to save significantly more (half of the top 10% were saving a mean average of £526 whereas half of those at the bottom half of the income distribution were saving £50 per month) (Rowlingson and McKay, 2014). In 2010-11, 45% of households had less than £1,500 in savings, 28% had between £1,500 and £20,000, and 20% had over £20,000 (Rowlingson and McKay, 2014).

It is therefore not surprising that people have very little capacity to meet unexpected expenses, even relatively small ones. When asked whether or not they could find £200 at short notice, 16% of the population in 2014 said they would have to borrow money – either through a formal loan (credit card, overdraft, loan etc.) or through an informal loan from family/friends. A further 16% said they would not be able to meet this

expense or preferred not to answer the question (Rowlingson and McKay, 2014).

An early focus of the financial inclusion agenda was to increase the number of people in the mainstream financial system through opening a bank account. Whilst increasing numbers of households now have a bank account, around 1.87 million adults remain unbanked in 2011-12 (Rowlingson and McKay, 2014). The majority of those without a transactional bank account are between the ages of 18-29 (15%) (Rowlingson and McKay, 2014). Not having a bank account (or a credit history) also has implications for accessing other financial products and services such as affordable credit, and to meet other needs such as private rented accommodation. However, it is not known how many people have a bank account but do not use it and the reasons for doing so (perhaps for fear of becoming overdrawn and the cost associated with it). Further research would be welcomed in this area.

Given the lack of savings, it is also no surprise that the number of households with unsecured credit or a form of credit commitment is high (64% and 75% respectively) (Rowlingson and McKay, 2014). This further suggests that household incomes are not meeting the needs of households and that these finances are under increasing pressure.

Some types of borrowing can be helpful to smooth the peaks and troughs of income and consumption but if people cannot afford their repayments they may get into 'problem debt'. 'Problem debt' also occurs when people fall behind with bill payments. Whilst it is difficult to access reliable data on 'problem debt', the evidence suggests that increasing numbers of households are experiencing difficulties in repaying unsecured credit and consider it to be a 'heavy burden' (18% in 2008-10) (Rowlingson and McKay, 2014). Furthermore, there were 34,000 mortgage repossessions in 2012, a fall from the peak in 2009 of 50,000 but still signalling major difficulties for people in repaying mortgages (Rowlingson and McKay, 2014). While mortgage repossessions have fallen in the last few years, evictions from rented accommodation have been increasing since 2010 (Rowlingson and McKay, 2014). Early evidence suggests that the impact of welfare reform and the so-called bedroom tax is exacerbating this trend. The government clearly has a responsibility to ensure that people have access to appropriate housing and greater forbearance is required particularly during financial hardship.

Coalition policy on financial inclusion

The Coalition has rarely used the term 'financial inclusion'. It has certainly not had a 'financial inclusion strategy' and it went ahead with the disbandment of the Financial Inclusion Taskforce in 2011. It had always been the intention for the Taskforce to be temporary but, given the economic situation, a government committed to financial inclusion might have considered extending its life for a few more years.

One of the first acts of the Coalition was to stop the introduction of the Saving Gateway. This was a financial inclusion policy designed to encourage low-income savers to save through matched saving. When piloted, the scheme was well regarded by its users. Instead, the government increased the amount an individual can save in a tax free ISA which caters for middle and higher income earners, people who already have access to appropriate financial services.

The Coalition also withdrew support from the Child Trust Fund, a universal savings scheme for all babies and was therefore fully inclusive.

Some elements of Coalition government policy have been more positive in relation to financial inclusion. For example, in 2013 the government have provided £38 million worth of financial support to Credit Unions to modernise under the 'Credit Union Expansion Project' and expand their operations for low income households, but this alone will not enable them to meet the potential market demand and many Credit Unions are unwilling to do so.

The government has also introduced various reforms of 'high cost, short term' credit including an interest rate cap on payday lending to reduce the cost and risk of this form of high-cost credit to individuals. From January 2015, the interest

rate cap will be set at 0.8% per day, or 1,270% APR. More significant perhaps is that there is a 100% borrowing limitation, meaning that consumers will never have to pay back more than double the cost of their initial loan if they are experiencing difficulties with repayment.

Finally, the government's pension reforms around auto enrolment into workplace pensions looks set to include many more people than before into pension schemes.

Conclusions and recommendations

With the loss of the Financial Inclusion Taskforce in 2011 and in lieu of a clear financial inclusion strategy, recent financial inclusion policies have been fragmented and tokenistic. These policies alone do not go far enough to ensure that people are financially included, particularly around supporting those on the lowest incomes. And broader Coalition policies around welfare reform are causing levels of financial exclusion to rise still further in relation to low levels of income, problem debt and lack of savings.

UK household finances are under significant pressure. Many may have weathered the storm so far yet remain in an extremely precarious position. There is evidence of blue sky amongst the grey clouds in the UK economic outlook yet the Coalition plan to continue the drive for austerity and Welfare Reform. This suggests that the majority of households (particularly at the lower end of the income distribution) will experience financial challenges both in the short and longer term. It is fundamental that the work of the Financial Inclusion Taskforce is not diminished. The evidence presented here suggests that the reduction (in real terms) in household incomes is having the greatest impact on financial exclusion. This is also where government financial inclusion strategy could have the greatest impact. This could be achieved through instituting a minimum income standard via the minimum wage and through means tested benefit increases, progressive taxation and a reduction in VAT (as poorer households pay a disproportionate amount of VAT compared to wealthier households). Alongside this, savings schemes designed to support and reward low income savers that match regular small sums such as the Saving Gateway could offer a starting point for an effective financial inclusion agenda to be relaunched.

References

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