CHASM | Centre on Household Assets and Savings Management

Briefing Paper BP4/2015

Financial Inclusion: Review of Coalition Government Policies 2010-2015

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May 2015

Introduction

The aim of this review is to outline the key financial inclusion policies of the UK Conservative-Liberal Democrat Coalition government between 2010-2015. Since 2010 there has not been a clear financial inclusion strategy. However there have been policies introduced or abandoned which give a sense of where the Coalition government's financial inclusion agenda lies. Drawing on Rowlingson and McKay's (2015) Financial Inclusion Annual Monitoring Report, I review Coalition policies on household budgets, bank accounts, savings, pensions and borrowing before concluding the paper.

When the Coalition took office in 2010, New Labour's Financial Inclusion Taskforce (FIT) was still in operation but scheduled to finish its work in 2011. Whilst the Taskforce had achieved some success in improving access to appropriate and affordable financial products and services, the 2008 financial crisis meant that it became increasingly difficult for individuals to manage financially with increased levels of unemployment and insecure employment, reduced incomes and increased living costs. The demise of the taskforce came at a time when it was needed most.

The Coalition government's plan to reduce public debt through austerity included reforming the welfare system through the introduction of Universal Credit to simplify the benefits system and with the intention of getting people back into employment. The austerity drive coupled with wider economic instability created a financially unstable environment for many households and individuals both in and out of work. This has had a major impact on financial inclusion.

The continuing squeeze on household budgets

It is difficult for people to manage on their incomes (a vital part of financial inclusion) when their incomes are going down and their expenses are going up. By 2014, there were more people in low-paid jobs than ever before (Corlett and Whittaker, 2014): 5.2 million people,

or one in five workers, earned less than £7.69 an hour and were more likely to be female, young, working in part-time or temporary employment in retail, hospitality and care sectors of the economy. The squeeze on living standards has increased calls for a rise in the minimum wage to a living wage (Hirsch and Valadez, 2014). Many social housing tenants have also found it difficult to manage financially with the shift to universal credit (Power, et al., 2014). Therefore there is evidence to suggest that a growing number of people are experiencing financial difficulties both in and out of work.

Bank accounts

The number of people with a bank account has increased year on year since the Coalition government took office (Rowlingson and McKay, 2014). Basic bank accounts have recently been re-launched with the support of nine high street banks and building societies. Basic bank accounts are for those currently without a bank account or for those that are ineligible for a full service account. There are no fees or penalties with the basic bank account so if a Direct Debit or Standing Order fails there are no charges but there is also no overdraft facility. Basic bank accounts can be used at any ATM, bank or Post Office which means that access is geographically widespread.

Savings

Saving is one way the government believes that individuals can protect themselves from income shocks and rising costs. However, 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 from Government. For each £1 saved, it would be matched by 50 pence from the government with a maximum of £300 paid in from government after two years. When the scheme was piloted, it was regarded favourably by its users. Instead, the government increased the amount an individual can save in a tax free ISA to just over £15,000 in 2015/16. ISAs favour middle and higher income earners because those whose income falls below the income tax rate do not benefit from tax-free savings. And those on the highest incomes, who therefore pay the highest rates of income tax, benefit most (Rowlingson and McKay, 2014). However, Bank of England interest rates have plummeted and remained at a historical low for the past six years, so savers are gaining little interest.

The Coalition also withdrew support from the Child Trust Fund (CTF), a universal savings scheme for all babies and therefore fully inclusive. Each child was given a £250 (or £500 for those families on a lower income) grant to each child born from September 2002. These grants had to be invested in special accounts until the child reached 18 and up to £1200 could be saved into the account each year. The account was topped up on the child's 7th birthday. The Coalition government phased out the CTF for all but the poorest families and

the CTF was replaced by Junior ISA in January 2011 which allowed families to invest up to £3,600 tax-free each year without any government investment.

Pensions

Government pension reforms to encourage more people to save for retirement via auto enrolment into workplace pensions appear to be working, with low opt out rates (Rowlingson and McKay, 2015). However, levels of pension saving are low and so people still need to save more than they are currently doing but not everyone can afford to do so.

From April 2015, people aged over 55 will have the freedom to make a number of choices with their pension pot. For example, they will be able to take their pension as cash (with 25% tax free), put it into an annuity or drawdown an income. This will enable people to pay off debts or their mortgage but needs to ensure that this money will last throughout their retirement and provide for all their needs during this time.

Borrowing

It is difficult to clearly capture levels of borrowing since 2010 given lack of good data in this field. On the one hand, some people seem to be paying down their credit commitments while others are adding to their current level of credit. The nature of access to credit has also changed somewhat since 2008 and even those who had previously been included in the financial system, for example, being able to secure mainstream credit in the form of overdrafts, mortgages, and loans were less able to secure the same levels of credit on similar terms. In the wake of the credit crunch, the nature of financial exclusion is changing. Payday lenders stepped in to fill the credit gap, and were particularly attractive for those unable to access mainstream credit from banks. However, the high rates of interest and repayment terms often meant that it was difficult for people to repay on time and in-full.

The Coalition government stepped in here to regulate short-term, high-cost credit in 2014 with the Financial Conduct Authority introducing various reforms 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 was set at 0.8% per day, or 1,270% APR. More significant perhaps is that consumers will never have to pay back more than double the cost of their initial loan if they are experiencing difficulties with repayment. However, capping the cost of credit does not address the issue of why people need to borrow and does not include home-collected credit which is targeted at lower income households.

The Coalition also invested £38 million into the Credit Union Expansion Project, in 2013 to modernise credit unions and expand their operations for low income households but this alone will not enable them to meet the potential market demand.

Less positive, from a financial inclusion perspective, was the introduction of local welfare assistance to replace the Social Fund in April 2013. The Social Fund allowed people to access a grant or a no-interest loan which was repaid through the benefits system. The local welfare assistance scheme has been devolved to Local Authorities which can offer grants, loans, vouchers, or in-kind support, for example, people can be referred to a food bank or receive grocery vouchers. Recent research has shown that Local Authorities offer different schemes (or none at all) and favour awarding grants and in-kind support to assist those in greatest need rather than provide loans which require greater administration costs (Gibbons, 2015).

Financial Inclusion Commission

Some have feared that the notion of financial inclusion and indeed the term itself has been lost in the last 5 years, but in recent months it has re-emerged with the establishment of the Financial Inclusion Commission (FIC). The FIC aimed to '*put financial inclusion back on the political agenda ahead of the 2015 General Election*' (FIC, 2015:1) to highlight the gaps in provision and what may be done to close the gaps. By drawing on evidence from experts working within the sector, the FIC set out its vision for a financial inclusive society in the UK by 2020.

The key recommendation of the FIC was to appoint a senior minister in the government to oversee responsibility for financial inclusion and financial capability with the title 'Minister for Financial Health'. The rationale for this is to ensure that there is a clear strategy and drive for financial inclusion which the UK has lacked since the FIT was disbanded in 2011. This would also enable government to respond to the changing needs of the financially excluded. However, it is what happens after the FIC disbands and the outcome of the 2015 general election that will be key to the future of financial inclusion in the UK.

Conclusions

Since the Coalition government came to power in 2010 and since the demise of the Financial Inclusion Taskforce in 2011, financial inclusion policies have lacked clarity. The Coalition financial inclusion policies are insufficient to ensure that people are financially included, particularly around supporting those on the lowest incomes. Indeed, the evidence suggests that 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.

Whilst recent figures show that levels of employment are increasing, these jobs tend to be insecure (i.e. part-time, low wage, temporary, self-employed) and wages are beginning to

increase, but those on the lowest and middle incomes are yet to significantly benefit. This is evident in the lack of savings amongst these groups. This suggests that the majority of the UK population is continuing to struggle financially. But it is difficult to give an accurate picture on the relationship between financial inclusion and related policies due to the lack of data. For example, further detailed research is needed on levels of problem debt where people are considered 'over-indebted', and the use of bank accounts (more people may have a bank account so are technically financially included but we do not know if they are actively using them).

The full extent of the austerity programme of the Coalition government has yet to be implemented if the Conservative- Liberal Democrats remain in power. We will see what happens in the next few weeks but in the meantime, Ricky Joseph's briefing paper outlines what the 2015 party general election manifestos say about financial inclusion to assess the outlook for financial inclusion policies in the future. Yet there is not a simple link between policy and impact because other factors are important (such as the labour market, inflation and austerity cuts more generally) and even if financial inclusion policies are implemented it will take time to assess their impact.

We would like to thank the Friends Provident Foundation for funding this work.

The views expressed in this briefing are the views of the author(s) and do not necessarily represent the views of CHASM as an organisation or other CHASM members.

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