Llais Defnyddwyr Cymru
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Consumer Focus Wales
The new Consumer Council for Wales

The cost of cash

Lindsey Kearton

About us

Consumer Focus Wales is a statutory organisation campaigning for a fair deal for consumers, established through the Consumers, Estate Agents and Redress Act 2007.

Our structure reflects the devolved nature of the UK. Consumer Focus Wales looks at issues that affect consumers in Wales whilst, at the same time, feeding into and drawing on work done at a GB, UK and European level. We were created through the merger of three consumer organisations – energywatch, Postwatch and the Welsh Consumer Council. This approach allows for more joined-up consumer advocacy, with a single organisation speaking with a powerful voice and able to more readily bring cross-sector expertise to issues of concern.

In advocating for consumers, we aim to influence change and shape policy to better reflect the needs of consumers. We do this in an informed way owing to the evidence we gather through research and our unique knowledge of consumer issues. We have a specific focus on vulnerable consumers, particularly those on low incomes, people with disabilities, people living in rural areas and older people. In addition, we also seek to identify where other consumers may be disproportionately disadvantaged by an issue or policy.

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www.consumerfocus-wales.org.uk

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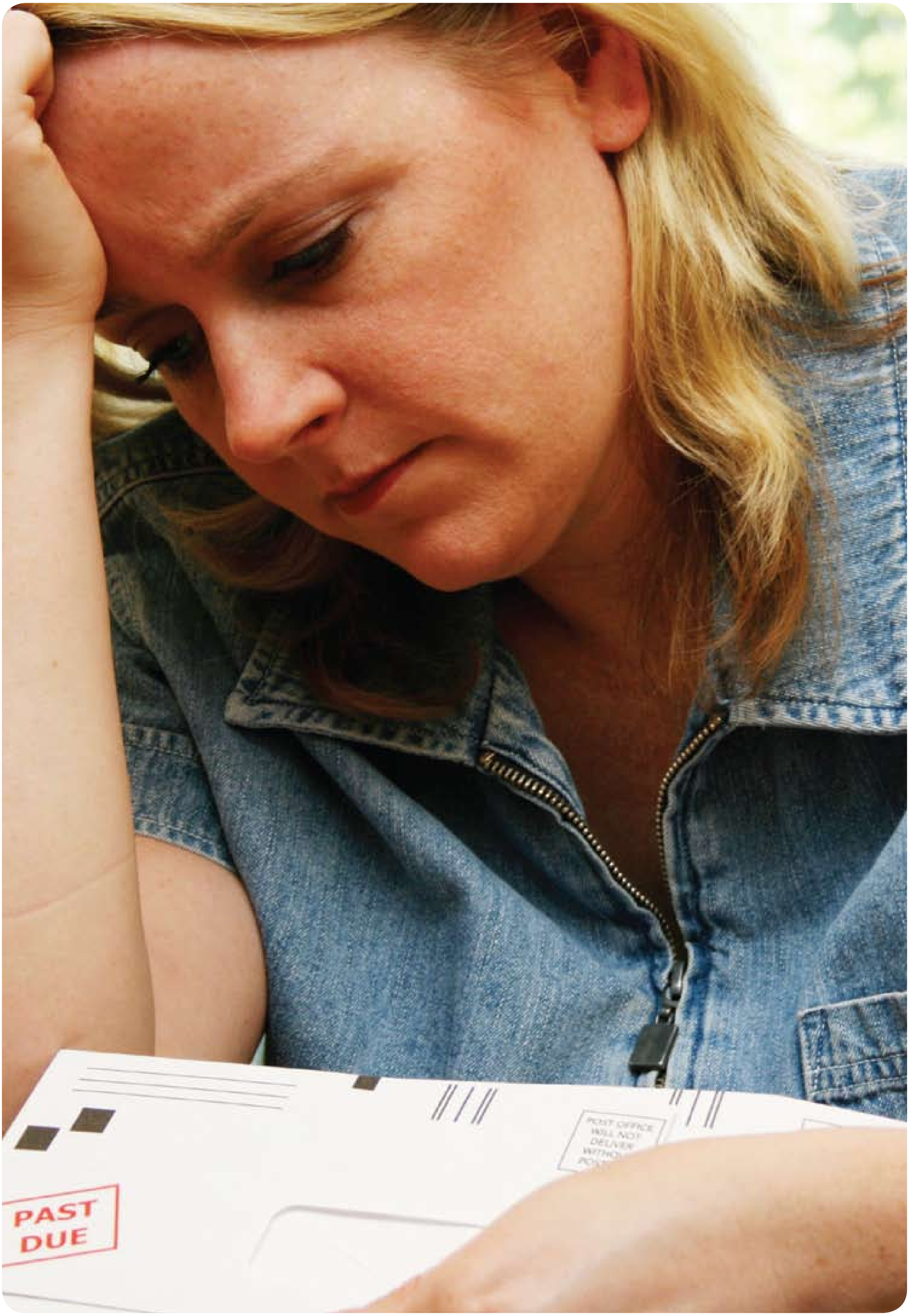
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Summary

This report highlights some of the daily experiences of low income families in Wales who largely live on a cash budget, including how they manage their money, their general attitudes to wider money issues and who they turn to if they need additional finance.

It shows how people without bank accounts, those who prefer to manage their budgets in cash, or those who are denied access to mainstream credit facilities often end up paying more for everyday essential goods and services because of how they pay.

Our research highlights the complexities that surround the interaction of many low-income consumers with financial products and services and how their financial behaviours are influenced by a range of factors.

It was apparent that most participants had a very 'sensible' attitude to money management. The need to maintain control over their finances, a general aversion to going into debt and feelings of trust (or mistrust) towards different financial services providers were all key drivers for choosing to use cash. Nobody in our study had been refused a bank account or felt they could not open one if they wanted to, showing that self-exclusion is commonplace when it comes to using bank accounts to their full potential.

However, more critically, in other areas, such as accessing reasonably-priced credit, a sense of enforced exclusion is evident. In such circumstances the critical supporting role of other family members is clear. For other financial products such as insurance and savings affordability is a real issue, with potentially devastating consequences.

Developing financial products and services that are better suited to the needs and circumstances of low income consumers is a critical part of the financial inclusion agenda. There are now a range of products available that have been designed to help satisfy these needs: basic bank accounts, Credit Union Current Accounts and loans, insurance with-rent schemes and the Saving Gateway[1] (due to be rolled out nationally in 2010) to name but a few. However, each of these products has experienced varying levels of success both in terms of take-up and levels of usage.

The reasons behind this are likely to be many and varied. Although this was just a small study, there are indications that some of these products may not be fully meeting consumer needs. For other products or services, such as credit unions and insurance with-rent schemes, there appears to be a lack of understanding as to how they work, or a general lack of awareness that they even exist.

[1] The Saving Gateway is a new Government supported cash savings scheme to encourage working-age people on lower incomes (i.e. people who are either eligible for, or in receipt of, certain DWP benefits or tax credits) to start saving small amounts of money (up to £25/month). Savers can withdraw their money at any time. The incentive to save is provided through a government contribution of 50 pence for each pound saved. This will be based on the highest balance in the account at any point over the 2 years (not necessarily the final balance).

Many consumers prefer to use cash to pay for goods and services and maintaining that choice should remain an important element of the financial inclusion agenda. However, progress in reducing financial exclusion could be improved by gaining a better understanding of what influences financial behaviours. In addition, addressing consumer concerns about certain products, raising awareness of less costly alternatives and developing the capacity of alternative trusted providers to offer additional financial services will all be critical if a shift in long-established behaviours is to be achieved.

There have been a number of significant and very welcome developments to promote financial inclusion in Wales over the last 12 months. To help take forward this work a number of policy recommendations have been included at the end of this report.

Introduction

For most people, having a bank account is part of everyday life. There is no need to carry too much cash around as we can pay for the majority of things with a debit card and many of our household bills are covered by monthly direct debit payments. If we do need cash, we can generally access it readily at any number of free-to-use ATMs or by using the cash-back facility on our debit card. The times when we may need a little extra help financially are covered by access to an agreed overdraft facility with our bank or building society, or we may choose to take out a personal loan or use a credit card.

Having a bank account also enables us to take advantage of online deals and to spread the cost of buying certain, more costly items, such as furniture, large electrical goods and insurance, over several months if we so wish, making them generally more affordable.

However, the situation is very different for people with limited or no interaction with financial products or services, many of whom will already be living on a low or limited income. More often than not people, without bank accounts, those who prefer to manage their budgets in cash, or those who are denied access to mainstream credit facilities will end up paying more to have that new TV or sofa, more to borrow money for those little emergencies and more to access their cash because they have to travel further to find a free-to-use ATM or have to rely on expensive cheque-cashing facilities.

Cash remains an important payment method for many of us. In a recent survey, two-thirds of the population in Wales (67%) said that they prefer paying for things in cash as it gives them greater control over their money[2]. However, the link between income and a preference for using cash was very clear. More than eight out of ten people from social grades DE[3] (82%) expressed a preference for using cash compared to less than half of those from social grades AB[4] (44%).

This report highlights some of the daily experiences of low-income families in Wales who largely live on a cash budget, including how they manage their money, their general attitudes to wider money issues and who they turn to if they need additional finance.

It is based on the outcome of four focus group discussions conducted at locations across Wales in March 2009. The focus of the research was people with children under 16 living in the household[5].

This research also forms part of a wider study into what is often called 'the poverty premium'[6] and how it affects families in Wales. The latter study covers issues such as the costs of education, financial services and fuel and is being led by the Bevan Foundation, in partnership with Consumer Focus Wales, NEA Cymru and Save the Children.

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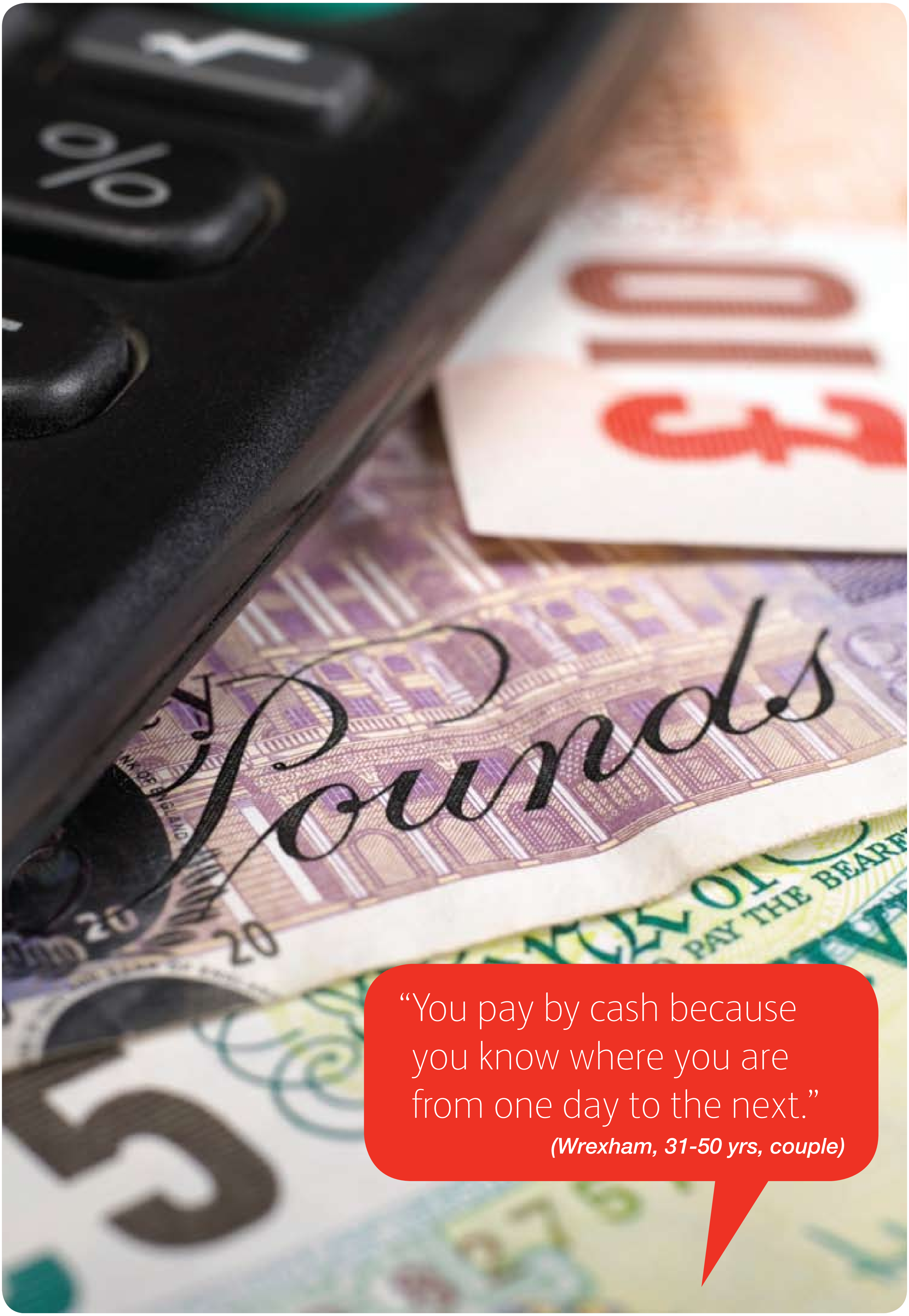
[2] 'Access to Cash', Welsh Consumer Council (August 2008)
[3] Semi-skilled/unskilled manual workers; those at the lowest level of subsistence
[4] Higher/intermediate managerial, administrative, or professional positions
[5] Further details of the research methodology can be found in the Annex. Due to the qualitative nature of the research the results should be treated as indicative rather than definitive.
[6] The 'poverty premium' is a term frequently used to describe the costs people on lower incomes have to bear to gain access to cash and credit, and pay for essential goods and services. Work undertaken by Save the Children and the Family Welfare Association in 2007 estimated the value of the 'poverty premium' to be around £1,000 a year.


"You pay by cash because you know where you are from one day to the next."
(Wrexham, 31-50 yrs, couple)

Why live on a cash budget?

The harsh realities of managing on a low income became very evident during our research. People spoke of a constant struggle to make ends meet and provide for their families.

Paying by cash was an active choice for the majority of consumers in our study[7] and not just a default position. Nobody had been refused a bank account or felt they could not open one if they wanted to. Many people did, in fact, hold an account of one form or another (e.g. current accounts, basic bank accounts, Post Office Card Accounts) but generally withdrew cash for the week as soon as money was paid into their accounts.

This allowed them to budget more easily by putting money aside for essentials, such as bills and food, and assess how much was left for other expenses.

Maintaining control over their finances was the critical factor, and, for the majority, young and old, this was the primary motivation for using cash.

"You pay by cash because you know where you are from one day to the next." *(Wrexham, 31-50 yrs, couple)*

"Oh, it's better. I know where I am, it's easier. You know what you have to spend." *(Merthyr Tydfil, 18-30 yrs, single parent)*

Knowing they could only spend what they physically had in their purse/pockets also helped to alleviate fears of knowingly or unwittingly going into debt – something frequently linked with using a bank account. These feelings had often been compounded by particular debt problems associated with unauthorised overdraft charges and subsequent repayment difficulties. The fact that the Post Office Card Account (POCA)[8] offered no overdraft or direct debit facilities appeared to be viewed positively as it stopped them having to worry about charges or being tempted to overspend.

Younger people in particular also appeared to have a general mistrust or suspicion of banks, especially how they administer direct debits. The current economic climate and high profile publicity surrounding the stability of many banking institutions had only served to amplify these feelings for some people.

[7] It should be noted that respondents were recruited on the basis that they tended to manage on cash budgets
[8] The POCA is an ultra-simple account that can only be used to receive benefit, state pensions and tax credit payments. No other payments, such as Housing Benefit, occupational pensions, or wages can be paid into it. Holders are issued with a plastic card and PIN, which allows them to withdraw cash for free or request a balance enquiry but only at a Post Office branch.

"I have a building society account. I won't have a bank account. I got into a mess with it before. I won't do that again." *(Cwmbran, 31-50 yrs, couple)*

"If you go 1p or 2p over, they charge you £40 when the direct debit has gone out." *(Merthyr Tydfil, 18-30 yrs, single parent)*

Some people had opened their bank account when they started work so that wages could be paid in. Households with at least one wage earner (mainly those with two adults) were more likely to hold standard current accounts. However, young single parents (who were largely dependent on benefits) tended to have a basic type of account and appeared to be more trusting and satisfied with the services provided by the Post Office than a bank. The limited functionality of the POCA (as a repository for receiving benefits) and the perceived control it gave them were felt to be more appropriate to their needs than a standard current account.

Many people had used direct debits at some point, and several continued to use them to pay for certain services, particularly when there was no other payment option (e.g. satellite and cable TV subscriptions). However, levels of distrust and confusion as to how the scheme worked were evident. There was a view that people had little control over direct debit payments (particularly payment dates), with limited awareness of their rights under the Direct Debit Guarantee, which includes the need for the person receiving the payment (e.g. the service supplier) to notify the customer in advance of any change in the amount to be paid or the payment date (excluding changes due to weekends or public holidays). The uncertainty around dates had led some respondents to go overdrawn and as a consequence, to incur significant penalty charges.

"With cash you know it's been paid. If you pay through a bank you can't guarantee that they are going to receive it when they should."

(Wrexham, 31-50 yrs, couple)

"I don't do direct debits. They give you a date and they either take it out a week before or a week after, never the time they say, and you get bank charges." *(Rhyl, 18-30 yrs, single parent)*

"With some of the services if you don't use direct debit they charge you another £5 … you think, 'I've got to do that because I'm saving £5 a month' which adds up." ***(Cwmbran, 31-50 yrs, couple)***

As a result, while people were aware of the higher costs for using cash rather than direct debits to pay certain bills, the advantages were felt to outweigh the extra cost. Participants did question the fairness of this, especially when in some instances they were paying in advance for the service. For example, prepayment meters or pay-as-you-go mobile phone services.

Table 1 below shows the differences paid annually by gas and electricity prepayment meter (PPM) customers, those who pay their bills quarterly (i.e. Standard Credit, SC) and those who pay by direct debit (DD). From the table, it is clear that customers who choose to pay by cash or cheque can pay around £100 more than those who pay by direct debit.

Table 1: Wales average energy prices (prices include VAT)

Medium user / Std rate	Gas	Electricity	Dual Fuel
DD	£749	£431	£1,148
SC	£798	£462	£1,245
PPM	£805	£454	£1,255
Difference PPM – DD (Wales)	£56	£23	£107
Difference PPM – DD (GB)	£47	£25	£99

NB: *The average price for electricity is cheaper for PPM than paying by quarterly bills. This is because all of the main suppliers apart from Scottish Power have equalised their electricity tariffs for these payment methods, and Scottish Power charge their PPM customers less than those who pay by quarterly bills.*

Source: Consumer Focus Wales (as at 19th August 2009)

"I know I'm paying more, I don't like it but I know what I'm paying and when." ***(Wrexham, 31-50 yrs, couple)***

"When you run out you, don't use [a mobile phone]. I had a contract and the bills just mounted up so I changed back. Now I know what I spend."

(Merthyr Tydfil, 18-30 yrs, single parent)

The direct payment of benefits into bank accounts has helped to reduce the number of 'unbanked' individuals across the UK. However, our research has confirmed that simply having a bank account is not enough for many consumers on low incomes to start using the full range of facilities on offer. The need to maintain control over their finances and the fear of going into debt are two of the primary drivers for living on a cash budget.

Confusion and suspicion surround direct debit payments and until these issues are effectively addressed many consumers will continue to use cash as their preferred payment method, regardless of the fact that, in some situations, they pay more as a consequence.

Some consumers may be more willing to use bank accounts if they are provided by alternative third-sector providers, such as credit unions or Community Development Finance Institutions, or other trusted organisations, such as the Post Office.

Recommendations:

- Banks, building societies and credit unions who provide current account facilities should:
  - provide face-to-face support to those opening a bank account for the first time to improve their understanding of how direct debits work, setting payment dates and the Direct Debit Guarantee;
  - include a free £10 'buffer zone' on their basic bank accounts to allow for some overlap between money going in and out of the account without incurring charges (currently less than one in three banks and building societies offer this facility);
  - develop innovative ways of keeping people up-to-date with their account transactions (such as text alerts) to help overcome fears of losing control;
  - explore alternative arrangements for electronic payments to alleviate some of the fears associated with direct debit payments (e.g. setting up a sub-account solely for bill payments, as suggested under the 'Saving from Poverty' proposition[9]).
- The Welsh Assembly and UK Governments should work with the banking industry to develop the capacity of alternative financial services providers, such as credit unions, Community Development Finance Institutions and the Post Office, so that they are able to offer bank account services that are appropriate to the needs and circumstances of people living on a low income.

[9] Effectively having two linked accounts: one for bill payments and one for cash/other expenses. For further information see www.savingfrompoverty.org.uk

The cost of accessing cash

Generally none of the people who took part in our research had difficulty accessing their cash, which they mostly did via a free-to-use ATM or directly from the Post Office.

For some the most convenient machine to where they lived was a fee-charging machine. If they had to use this facility they generally took out less money than planned in order to cover the charge and ensure that they did not go unexpectedly overdrawn. However, most of the time, they would travel further to use a machine that did not charge.

"It's just the charges on some of them. With some of the shops, you pay £1.50 or £1.75. I don't use them. I just go down town." ***(Cwmbran, 31-50 yrs, couple)***

"You have to take out less because they charge you."

(Merthyr Tydfil, 18-30 yrs, single parent)

Other Consumer Focus Wales research[10] shows that for some communities across Wales the impact of the recent Post Office closure programme[11] means that those who rely on the Post Office to access their cash (or pay bills) are either having to travel further to reach an alternative post office or have become more reliant on the goodwill of family or neighbours to reach these services.

Free access to cash can also be particularly difficult in rural areas. A recent survey of rural residents across Wales found that 8% of those on a low income said they had difficulty accessing an ATM[12].

Most participants in our research felt that having to pay for the privilege of accessing your own money was extremely unfair.

The demise of the cheque is gathering speed, with most major retailers now refusing to accept cheque payments. Very few people we spoke to said they personally wrote cheques these days (many had accounts without chequebooks). However, some had had direct experience of using cheque-cashing facilities. The cost of getting instant cheque clearance using these services is generally around 10% although it can be higher. Those who were aware of such services generally knew that they were expensive to use. However, users were prepared to pay the charge if it meant gaining access to their money more quickly.

[10] To be published shortly

[11] The recent Network Change Programme saw 150 Post Offices closing in Wales, with an additional 50 being replaced by outreach services (these could be in the form of a service provided in another outlet such as a village shop or community hall, or a mobile van)

[12] 'Coping with Access to Services: Research Report 12', Wales Rural Observatory (2007)

“They are OK if you need the money straight away and can’t wait five days for the cheque to clear.” *(Cwmbran, 31-50 yrs, couple)*

Mobility or transport problems were not an issue for anyone in this research. However, the additional cost and logistics associated with travelling to a free-to-use machine should not be underestimated and need to be considered as part of the wider social implications of the location of such machines. This can have a significant impact on those with limited budgets or restricted mobility.

We welcome the work that is currently underway by the Welsh Assembly Government, LINK (the ATM network provider) and the Bank of Ireland/Post Office Ltd to improve access to ‘free-to-use’ ATMs in some of the most deprived areas of Wales. Under the LINK Strategy, almost 200 new machines are planned in 37 areas across Wales[13] although the rural areas of Gwynedd, Ceredigion and Monmouthshire are not covered by this scheme.

According to the latest figures from LINK, as of August 2009, 113 machines have gone ‘live’, 5 are under contract and 80 remain outstanding. While these developments are very welcome, there is still considerable work to be done to ensure that everyone in Wales is easily able to access their cash for free. Both planning difficulties and community-safety concerns have been cited as barriers to implementation in some areas. For example, there may be local opposition due to pedestrian walkways being obstructed or concerns that the machine and/or its users would be a target for anti-social behaviour or theft. Such issues need to be urgently addressed.

Recommendations:

- The Welsh Assembly Government should:
  - ensure local planning and police authorities better understand the need for free-to-use ATMs in identified communities as suitable locations still need to be identified for 40% of the machines proposed under the LINK Strategy;
  - review how well rural communities are served under the current programmes in order to increase access to free-to-use ATMs, particularly following the Post Office closure programme.
- Local authorities, local police and Community Safety Partnerships should work constructively with community-based organisations, local retailers and others hoping to house a machine, in order to help them overcome, as far as practicable, any potential barriers to locating a machine in their area.

[13] Following consultation with the UK Government, consumer groups and the Treasury Select Committee LINK and its Members have devised a programme to support the installation of free cash machines in areas where there is limited free access to cash. Of the 600 ATMs required across England and Wales, 198 are due to be installed in Wales if suitable sites can be found. Target areas have been identified using the Welsh Index of Multiple Deprivation (2005).

To borrow or not to borrow?

A preference for using cash and related concerns of going into debt highlighted the importance that many participants in our study placed on living within their means.

Nearly all of the people who took part in our research felt that it was important to budget although many admitted that this was hard to do at times. Several respondents, mainly the younger single parents, felt that they would benefit from more advice on how to budget effectively.

"I could do with help with budgeting as I'm not good with money."

(Merthyr Tydfil, 18-30 yrs, single parent)

"I do it on a Monday night because I get paid on a Tuesday. I make a list of what has to be paid, what I've got for shopping. I never stick to it but I do it with good intention. " *(Rhyl, 18-30 yrs, single parent)*

Paying for essentials, such as food, rent, gas and electricity, tended to take priority. Pressures to provide for their children and to try to give them what they want and need were also evident. A number of people said that they would rather go without themselves than say 'No' to their children.

Most people in our groups had an aversion to going into debt and worried about not being able to keep up with repayments. A number had struggled with problem debt in the past and one or two had been declared bankrupt as a consequence.

In spite of this, the majority said that they still have no option but to borrow occasionally, even to pay for utility bills, due to the realities of living on a low income, cash-flow problems and unexpected expenses. On the whole most people borrowed for more everyday essential items (washing machines, furniture and cars were all mentioned) than perceived 'frivolous' reasons, such as holidays or going out.

"I'd borrow if I needed to for gas and electricity but I wouldn't borrow to go out." *(Merthyr Tydfil, 18-30 yrs, single parent)*

"I borrowed for my car, I did it on my credit card. I don't know how I'll pay it."

(Cwmbran, 31-50 yrs, couple)

"Mine are always coming demanding this and that... you have sleepless nights over finances."

(Cwmbran, 31-50 yrs, couple)

In terms of who they would turn to if they needed some extra cash to pay for a major item such as a TV or washing machine, it was noticeable that, in the first instance, many relied heavily on other members of their family for credit, especially the younger single parents.

The main reasons were to avoid paying interest and the ability to pay the money back in smaller, weekly instalments. They also felt that they were less likely to default on these payments. We are planning to explore the impact this subsequently has on the wider family and their ability to manage their own everyday living costs in future research.

"I had to borrow from my mum for a washing machine but I still had to pay it back. It was my mum's holiday money." ***(Wrexham, 31-50 yrs, couple)***

"If you borrow off your mum and dad, there is no interest, and if you can only afford to pay back £5 a week, they would accept that." ***(Rhyl, 18-30 yrs, single parent)***

Rather than borrow, a couple of people said that they would try to save up if they needed to buy such items in order that they could pay in cash, but, if all else failed, several others said that they would buy the item from a catalogue or credit retailer (such as Brighthouse or Buy as you View). This was particularly true of the younger respondents.

In addition, a number of people in our study found it difficult to get credit from mainstream sources such as banks and building societies (largely due to their level of income or poor credit histories). However, the fact that the majority of loans provided by these firms require monthly repayments means that, even if access was not a problem, having to pay back the loan at monthly intervals would prove unaffordable.

"The amount of money I'm on, I'd not be able to borrow from a bank. I wouldn't be able to afford to pay it back." ***(Merthyr Tydfil, 18-30 yrs, single parent)***

Only a couple of people (mostly older participants) had used credit cards or gone to a bank for a loan. For this minority, credit was relatively easy to come by although they felt more often than not that lenders encouraged people to borrow more than they could afford to repay.

"I keep struggling, but they say, 'Have a loan, have a loan', but how do I pay it back?" ***(Cwmbran, 31-50 yrs, couple)***

As already mentioned many people had personal experience of using home credit companies, credit shops and coin-meter retail services (e.g. Provident, Brighthouse, Buy As You View). Participants were shown examples of the differences in cost between paying for particular goods and services using different payment methods or retailers. For example, buying a £159.99 cooker from Argos would typically cost £405 from Brighthouse (if paid for over 125 weeks) – a difference of £245.01, or 153%[14].

No one was at all surprised at how much more expensive high-cost credit providers were – words such as 'extortionate' and 'rip-off' had already been used spontaneously to describe some companies. However, before being shown, many found it hard to assess the extent of the difference between these and more mainstream forms of credit.

Many of those who took part in our study severely criticised companies such as these. Some went as far as to say that they should not be allowed to charge the interest rates they do. But most believed that people in their situation often had little choice but to use this form of credit due to a perceived lack of affordable alternatives, combined with the fact that some of these providers do not run credit checks[15].

"What you pay back is nearer double what you borrow. They [a well-known home credit company] come round at Christmas when you're most likely to say 'Yes'." ***(Rhyl, 18-30 yrs, single parent)***

"My missus went and had a three piece suite off them [a well-known credit shop]. It cost me five grand." ***(Cwmbran, 31-50 yrs, couple)***

"If your washing machine breaks down, you need one there and then. You can't wait to save. If you are in that predicament, you will go there [a well-known credit shop] and get it." ***(Merthyr Tydfil, 18-30 yrs, single parent)***

14 This example was taken from 'The Poverty Premium: How poor households pay more for essential goods and services', a briefing paper prepared by Save the Children and the Family Welfare Association (2007)

15 This study mainly focussed on people's attitudes to and experience of commercial lenders. Third-sector lenders were discussed as potentially affordable alternatives, but no Credit Union members took part in the research. Government grants/loans, such as the Social Fund, were also outside the scope of this study.

Not surprisingly, all were aware of unlicensed lenders ('loan sharks'), but only a couple had personal experience of using them. The majority felt that they should be avoided at all costs and their reputation for intimidation was clear.

"I want to keep my home! You get involved with them and you've had it."

(Wrexham, 31-50 yrs, couple)

"I won't even go there. I know people who have though."

(Rhyl, 18-30 yrs, single parent)

There is growing concern from consumer organisations (such as ourselves) and others that as the impact of the economic downturn kicks in and credit providers (including home credit companies) start to tighten their lending criteria, more people will be forced to use illegal lenders.

The current legislative framework for consumer credit in the UK is largely governed by the Consumer Credit Act 1974. Reforms to the Act in 2006 have since allowed for the Office of Fair Trading (OFT) - the regulator for consumer credit - to take appropriate action if a consumer credit business is deemed to be lending irresponsibly. Their proposed guidance for creditors on this issue is very welcome and helps to clarify business practices which will not be considered acceptable by the OFT. The guidelines include expectations on creditors not to encourage borrowers to increase their existing debt when they may face difficulties clearing their debts, not to target borrowers who may be particularly vulnerable with inappropriate credit products, and to ensure that all information/documentation provided to borrowers is written in plain and intelligible language. These requirements are likely to be strengthened when the Consumer Credit Directive comes into force in June 2010. While such developments should hopefully benefit consumers there is a concern that they may further restrict access to affordable credit for some.

For the people in our groups the ability to borrow money instantly and pay back loans in small weekly instalments were common factors for all of the preferred sources of credit, be it borrowing from family, through a catalogue, or credit retailer. This approach was overwhelmingly viewed as being more affordable in the short-term even if (in the case of high cost credit providers) they would ultimately end up paying more for the item in question. This type of consumer behaviour is not uncommon in financial markets when the current benefit of an action is perceived as being greater than any future costs.

While the majority realised using home credit companies or credit retailers were expensive, there was a general lack of awareness as to the extent of the cost differential between paying for goods in this way and other methods of payment, including borrowing from more affordable third-sector lenders.

Maintaining control over their finances and being able to live within their means were also recurring themes throughout the discussions. Whilst we have seen significant developments to improve financial capability over recent years, both at the Wales and UK level, any additional support to help better manage their money would be welcomed by many participants.

Recommendations:

- Funders of financial capability work, including the Welsh Assembly and UK Governments, the Financial Services Authority, the financial services industry and others, should ensure that there is sufficient, sustainable funding for financial capability work to continue at the community level, particularly during such uncertain financial times;

- Community based organisations such as credit unions, citizens advice bureaux and housing associations, should explore opportunities to extend their financial capability work through the national rollout of the Financial Services Authority's Money Guidance service, 'Moneymadeclear', which is due to begin in spring 2010;
  - efforts should initially be targeted at specific groups (eg. single parents, low income families) who are likely to benefit most from free, impartial, face-to-face advice and support on money issues (including budgeting, the advantages/disadvantages of different payment methods and types of borrowing).

- The Welsh Assembly Government and the Financial Services Authority should work together to ensure that Wales gets its fair share of the funding available under the 'Moneymadeclear' programme.

- As part of their financial inclusion policies the Welsh Assembly and UK Governments should carefully monitor the impact the implementation of the Consumer Credit Directive has on consumers' ability to access affordable credit, particularly those on a low or limited income where access can already be a problem.

An affordable alternative

For many people on lower incomes access to affordable credit can be difficult, especially when they often need to borrow small amounts over a short period of time.

The British Banking Association (BBA) has acknowledged that banks are never likely to provide mainstream finance to this group of consumers[16]. Therefore third sector lenders, such as credit unions and Community Development Finance Institutions (CDFIs), are currently the main solution for extending affordable credit to low-income consumers.

Both types of organisations are not-for-profit and have similar aims but while credit unions are financial co-operatives, CDFIs are generally set up as community interest companies.

Credit unions are legally restricted in the amount of interest they can charge on their loans (a maximum APR of 26.8%). However, a CDFI has greater flexibility in setting interest rates. Typical APRs can be nearer 50% meaning that their ability to offer loans to slightly 'higher risk' customers is increased, although, as with any lending, careful consideration still needs to be given to the creditworthiness of any potential borrowers.

While interest rates of 45-50% may seem relatively expensive, Table 2 below shows that the total amount a CDFI customer would have to repay is still considerably lower than for a typical home credit loan.

Table 2: Comparison costs of £300 loan (August 2009)

Credit provider	Amount repaid
Typical Credit Union (at least 8 weeks saving required beforehand) *12.7% APR, paid over 52 weeks*	£318.64
Credit Unions (offering instant loans) *26.8% APR, paid over 52 weeks*	£337.99
Community Development Finance Institution (offering instant loans) 47.75% APR, paid over 50 weeks	£357.50
Typical home credit company (home collection) *254.5% APR, paid over 50 weeks*	£525
Difference (cheapest and most expensive)	£206.36 or 64.8%

There are currently 29 Credit Unions in Wales covering all local authority areas, and 2 CDFIs are under development – one in Powys (as part of the Robert Owen Community Banking Partnership) and 'Moneyline Cymru' (being set-up through Community Housing Cymru)[17], with pilot outlets in Bridgend, Cardiff, Newport, Rhondda Cynon Taff and Torfaen.

[16] 'Financial Inclusion: Access to advice, banking & credit', BBA & APACS (November 2005)
[17] Due to launch in October 2009

Credit unions across Wales have been trying for many years to break the cycle of reliance on home credit that exists in many deprived communities, but this is not an easy task. We heard during this study that representatives from home credit companies are often well-known in the local community, with long-standing relationships that have developed over generations. Changing this culture of money management is therefore a considerable challenge. The risk of being unable to pay back the loan is also much higher amongst people whose weekly income is low or limited. In the home credit market if customers pay six out of ten repayments on time they are regarded as 'good payers'. The degree to which third sector lenders can absorb bad debt is severely limited, which means that, in many communities competing on the same basis as the home credit industry is near impossible and, at best, unsustainable.

To put this into context, a recent report commissioned by the Joseph Rowntree Foundation[18] found that a not-for-profit home credit business would need to charge APRs of 123% to compete on the same basis as commercial home credit companies. The proposed business model would also need an £18 million investment (via public subsidy or social business investment) to make the service financially sustainable – rising to a £90 million subsidy over ten years if the APR were reduced to 100%.

Our research also found that awareness of credit unions was generally low[19] and that overall knowledge of how they worked was somewhat limited. Those participants who had heard of them (mostly through word of mouth) had generally positive impressions i.e. they were perceived as trustworthy and usually offered a good deal 'to people like them' once you had saved for a while.

When the idea of credit unions was explained to them, many were interested in finding out more, especially as a means of saving for Christmas and special occasions.

"I want to do that. It's supposed to be good. My nan told me about it."

(Merthyr Tydfil, 18-30 yrs, single parent)

"There is one just across the road. I've heard of them but not used them. I was thinking of using it before Christmas, but just didn't get round to it. They've got a savings club." *(Rhyl, 18-30 yrs, single parent)*

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[18] 'Is a not-for-profit home credit business feasible?', Joseph Rowntree Foundation (March 2009)
[19] It should be noted that members of Credit unions were screened out at the recruitment stage

> “It depends on how low the interest is. It’s paying it back.”
>
> *(Wrexham, 31-50 yrs, couple)*

The current recession, combined with policy and legislative changes, is likely to mean that the credit landscape will change quite significantly over the coming years. In the immediate future more consumers are likely to struggle to keep up with their credit commitments, and the chances, of defaulting on loans is likely to increase. This poses a particular challenge to third sector lenders, particularly credit unions as they are restricted in the amount of interest they can charge on their loans. However, the changes also mean that there is a real opportunity for these lenders to capitalise on the evident interest in their services through improved promotional activity and by building stronger links with other organisations.

Recommendations:

- In the development of their Credit Union Action Plan, the Welsh Assembly Government should:
  - work with the Wales Co-operative Centre, individual Credit Unions and trusted community representatives to develop a targeted, high-profile marketing campaign to promote the services offered by Credit Unions to those who would most benefit from their services;
  - include action to foster better links between credit unions and other local partners, including local employers, post offices, citizens advice bureaux and housing associations (particularly those involved with the new CDFI, ‘Moneyline Cymru’);
  - where beneficial, facilitate relationships between individual Credit Unions to enable them to share resources and thereby increase the range of financial services they are able to offer e.g. the Credit Union Current Account.
- Moneyline Cymru should similarly develop partnerships with credit unions and advice providers in the pilot areas in order to increase the range of financial services they are able to offer their customers, such as savings and debt advice.

"I used to have insurance but it began to work out expensive. I would definitely get it again."
(Rhyl, 18-30 yrs, single parent)

Having a financial safety net

The consequences of being burgled or the victim of a fire or flood without insurance cover can be devastating.

We also asked people about how they protect themselves financially for those times when things can and do go wrong. The majority of people who took part in our research agreed that it was important to have home contents insurance. For some, this was a direct result of having been burgled in the past, and they had since obtained cover. For others, the cost of insurance was the predominant barrier to take-up. Local crime rates, average property prices and the probability of flooding or subsidence can all have an impact on premium rates.

"Yes, I have insurance. I've seen it from the other side. I've not had it and lost everything." *(Merthyr Tydfil, 18-30 yrs, single parent)*

"No, I don't have insurance but I should do. I can't afford it at the moment,. If I could, I would." *(Wrexham, 31-50 yrs, couple)*

Many social housing providers now offer affordable insurance-with-rent schemes and, in some areas, regional premium rates have replaced more localised rates in order to help reduce the impact of living on an estate with higher crime levels. However, take-up remains low.

It would appear that, for many low income households, especially in such uncertain times, even when premiums have been reduced and weekly payment terms have been introduced, the additional cost of taking out insurance to protect their belongings against something which may or may not happen in the future still remains too much to bear compared with other priorities.

Similar views were apparent when discussing savings. The majority of people thought that it was important to try to save money whenever possible. Some tried to save for special occasions (e.g. Christmas) or to put money aside 'for a rainy day', but although promoting affordable, small-scale saving is an important element of the work of both credit unions and post offices, people tended to pass money to other family members to keep safe for them, rather than opening a formal savings account. Others just found that the realities of life and living on a low income made it impossible to save, although it was something they aspired to.

“I have my child benefit paid into my mother’s account not into mine, so I can’t spend it as it’s not in my account. It’s there if I need it. I use it for holidays and things.” *(Cwmbran, 31-50 yrs, couple)*

“If I could, I would. If I had the extra money.” *(Rhyl, 18-30 yrs, single parent)*

Our research shows that, while people recognise that having home-contents insurance and saving regularly are both important, for many people, their financial situation means that being able to benefit from such products is regarded as something of a ‘luxury’.

Products have been developed in these areas to try to meet the requirements of low-income consumers. However, clearly more needs to be done to make them more appealing and encourage take-up.

As trusted organisations, both credit unions and post offices are ideally placed to offer more formalised savings arrangements to low-income consumers, as well as providing a gateway to a range of other financial services. The UK Government has already stated that the Saving Gateway (due to be rolled out nationally in April 2010) will be available through the Post Office.

Recommendations:

- Social Housing Providers offering insurance-with-rent schemes should:
  - use peer educators more widely to relay information to existing tenants ensuring that they receive proper training and continuing access to appropriate support networks in order to avoid misinformation;
  - undertake specific work that focuses on the benefits of home contents insurance to encourage take-up of insurance with-rent schemes amongst new tenants as part of their ‘welcome pack’;
  - Those not currently offering insurance with-rent schemes should consider doing so as part of a wider financial inclusion strategy.
- Credit unions not currently offering Child Trust Fund accounts should consider offering this service as it provides an excellent opportunity for young people to be introduced to the benefits of formal saving.
- From April 2010, credit unions across Wales should also seek to be providers of the Saving Gateway as this incentivised savings account should help introduce more low income consumers to the benefits of formal saving.

Conclusion

This research has provided a snapshot of the experiences of managing on a cash budget and has highlighted the complexities that surround the interaction of many low-income consumers with financial products and services. In many situations, people actively choose to exclude themselves from taking up or using particular financial products, most notably bank accounts. However, more critically, in other areas, such as accessing reasonably-priced credit, a sense of enforced exclusion is evident, and, for products such as insurance and savings affordability is a real issue, with potentially devastating consequences.

Our research also shows how financial behaviours are influenced by a range of factors. The predominant reason for zero or restricted use of bank accounts centred on the need to maintain control over their finances. Whether out of necessity or desire, it was apparent that most participants had a very ‘sensible’ attitude to money management. Those who took part in our research, believe that paying by cash enables them to manage their money more effectively.

Other important drivers relate to a general aversion to going into debt, feelings of trust (or mistrust) towards different financial services providers and the crucial supporting role of other family members.

Developing financial products and services that are better suited to the needs and circumstances of low-income consumers is a critical part of the financial inclusion agenda. There are now a range of products available that have been designed to help satisfy these needs – basic bank accounts, Credit Union Current Accounts and loans, insurance with-rent schemes and the Saving Gateway to name but a few. However, each of these products has experienced varying levels of success both in terms of take-up and levels of usage.

The reasons behind this are likely to be many and varied. Although this was just a small study, there are indications that some of these products may not be fully meeting consumer needs while, for other products or services, there appears to be a lack of understanding as to how they work, or a general lack of awareness that they even exist.

If consumers are to be encouraged to make greater use of bank accounts and subsequently benefit from the reduced costs of paying by direct debit, the banking industry needs to show greater commitment to the promotion of basic bank accounts and the services they offer. While such accounts do not offer overdraft facilities, greater flexibility needs to be built into direct debit arrangements, supported by the right advice to improve understanding of how direct debits work and the benefits they can provide.

Banks and building societies are also not the only potential providers of such services. Some consumers may be more willing to use bank accounts if they are provided by alternative organisations, such as credit unions, post offices or a Community Development Finance Institution (once fully established in Wales). During our research the former two were perceived as trusted sources of information.

The use of high cost lenders was commonplace for many of the people who took part in our research and there was a general perception that people in their situation had little choice but to use these providers. The challenges that third sector providers face in trying to compete with home credit companies are considerable, but, equally, there has probably never been a better time for them to capitalise on the evident interest and growing need for their services. Beyond loans, third sector providers are also ideally placed to offer a gateway into other financial services, including bank accounts, savings, and financial literacy advice.

There is currently a lot of good work going on across Wales to promote financial inclusion. It is hoped that both the Welsh Assembly Government's recently published financial inclusion strategy for Wales, 'Taking everyone into account', and the work being taken forward by the Financial Inclusion Champions team in Wales will help to provide a much-needed direction and focus for this work over the coming years.

Many consumers prefer to use cash to pay for goods and services and maintaining that choice should remain an important element of the financial inclusion agenda. However, progress in reducing financial exclusion could be improved by gaining a better understanding of what influences financial behaviours. In addition, addressing consumer concerns about certain products, raising awareness of less costly alternatives, and developing the capacity of alternative trusted providers to offer additional financial services will all be critical if a shift in long-established behaviours is to be achieved.

Recommendations

In light of these findings, Consumer Focus Wales makes the following recommendations.

The Welsh Assembly Government should:

- ensure local planning and police authorities better understand the need for free-to-use ATMs in the identified communities;
- review how well rural communities are served under the current programmes to increase access to free-to-use ATMs, particularly following the Post Office closure programme.
- in the development of their Credit Union Action Plan:
    - work with the Wales Co-operative Centre, individual Credit Unions and trusted community representatives to develop a targeted, high-profile marketing campaign to promote the services offered by credit unions to those who would most benefit from their services;
    - include action to foster better links between credit unions and other local partners, including local employers, post offices, citizens advice bureaux and housing associations (particularly those involved with the new CDFI, 'Moneyline Cymru');
    - where beneficial, facilitate relationships between individual Credit Unions to enable them to share resources and thereby increase the range of financial services that they are able to offer e.g. the Credit Union Current Account.

The Welsh Assembly Government and the Financial Services Authority should:

- ensure that Wales gets its fair share of the funding available under the 'Moneymadeclear' programme, with efforts being initially targeted at specific groups (e.g. single parents, low-income families) who are likely to benefit most.

The Welsh Assembly and UK Governments should:

- work with the banking industry to develop the capacity of alternative financial services providers, such as credit unions, Community Development Finance Institutions and the Post Office, so that they are able to offer bank account services that are appropriate to the needs and circumstances of people living on a low income;
- carefully monitor the impact that the implementation of the Consumer Credit Directive has on consumers' ability to access affordable credit, particularly those on a low or limited income where access can already be a problem.

Banks, building societies and credit unions who provide current account facilities should:

- provide face-to-face support to those opening a bank account for the first time in order to improve their understanding of how direct debits work, setting payment dates and the Direct Debit Guarantee;
- include a free £10 'buffer zone' on their basic bank accounts to allow for some overlap between money going in and out of the account without incurring charges (currently less than one in three banks and building societies offer this facility);
- develop innovative ways of keeping people up-to-date with their account transactions (such as text alerts) to help overcome fears of losing control;
- explore alternative arrangements for electronic payments to alleviate some of the fears associated with direct debit payments (e.g. setting up a sub-account solely for bill payments as suggested under the 'Saving from Poverty' proposition).

Funders of financial capability work (including the Welsh Assembly and UK Governments, the Financial Services Authority and the financial services industry) should:

- ensure there is sufficient, sustainable funding for financial capability work to continue at the community level, particularly during such uncertain financial times;

Local authorities, local police and Community Safety Partnerships should:

- work constructively with community-based organisations, local retailers and others hoping to house a free-to-use ATM, in order to help them overcome, as far as practicable, any potential barriers to locating a machine in their area.

Local authorities and housing associations offering insurance with-rent schemes should:

- use peer educators more widely to relay information to existing tenants ensuring they receive proper training and continuing access to appropriate support networks so as to avoid misinformation;
- undertake specific work that focuses on the benefits of home contents insurance in order to encourage take-up of insurance-with-rent schemes amongst new tenants as part of their 'welcome pack';
- those not currently offering insurance with-rent schemes should consider doing so as part of a wider financial inclusion strategy.

Community based organisations (e.g. credit unions, citizens advice bureaux) should:

- explore opportunities to extend their financial capability work through the national rollout of the Financial Services Authority's Money Guidance service, 'Moneymadeclear', which is due to begin in spring 2010;
- Credit unions not currently offering Child Trust Fund accounts should consider offering this service as it provides an excellent opportunity for young people to be introduced to the benefits of formal saving.
- from April 2010, credit unions across Wales should also seek to be providers of the Saving Gateway as this incentivised savings account should help introduce more low income consumers to the benefits of formal saving.

Moneyline Cymru should:

- develop partnerships with credit unions and advice providers in the pilot areas in order to increase the range of financial services that they are able to offer their customers, such as savings and debt advice.

Annex - Methodology

Consumer Focus Wales commissioned Beaufort Research Ltd to undertake four focus groups at locations across Wales. Locations were selected on the basis that they had been identified as amongst the most financially excluded/deprived parts of Wales, namely Merthyr Tydfil, Torfaen, Wrexham and Rhyl.

All those who took part in the study were living on a low income (defined as having a gross annual household income (before taxes and deductions) of £18,500 p.a. for single adult households and £29,000 for the two adult households. The emphasis of the research was on people tending to manage on cash budgets, so respondents were recruited to take part in the discussions on the basis that they always or usually paid household bills such as for gas, electricity and the telephone by cash.

In addition, a mix of genders and working / non-working people was sought across the discussions, and all had children aged 16 or under living at home.

The specification adopted for the groups is shown below:

Group	Location	Age	Household type	Gender
1	Merthyr Tydfil	18-30 years	Single parent	Mixed male / female
2	Wrexham	31-50 years	Couple with child / children	Mixed male / female
3	Torfaen - Cwmbran	31-50 years	Couple with child / children	Mixed male / female
4	Denbighshire - Rhyl	18-30 years	Single parent	Mixed male / female

Each of the four groups lasted up to 1½ hours, and was conducted in a convenient central location for the respondents. Three additional in-depth telephone interviews were also undertaken (with people who had agreed to attend but were unable to on the day) in order to supplement the findings of the groups. The research took place in March 2009.

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