

Towards a national strategy for financial capability



The FSA would welcome any comments on issues raised in this document. It would be particularly helpful if at least initial comments could reach us by Friday 12 December, so that they can help to inform our early work. You can send your response by e-mail:

Email: financial.capability@fsa.gov.uk

Alternatively, please send comments in writing to the following address:

Marie Calnan
Financial Capability Team
The Financial Services Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Telephone: 020 7066 0832

Fax: 020 7066 9713

It is the FSA's policy to make all responses to consultation available for public inspection unless the respondent requests otherwise.

Contents

1	Foreword	3
2	The problem	6
3	The consequences of the problem	8
4	What's the solution?	10
5	Scope of the strategy	12
6	How will the strategy be developed, funded and implemented?	13
7	What will success look like?	16
8	How we will engage with our partners	17

1 Foreword



I explain in this paper that, under FSA leadership and working in partnership with other organisations, we propose to develop and implement a national strategy for financial capability.

The Strategy for Financial Capability is about providing consumers with the education, information and generic advice needed to make their financial decisions with confidence.

Never has the need been so great or so urgent. Consumers are grappling with worries about their pensions and savings, insurance protection and build-up of debt. There remain high risks to consumers from inadequate understanding of financial concepts and products, and this at a time when consumers are increasingly being asked to take on more responsibility for their long-term financial planning.

I have set up a Financial Capability Steering Group to develop the national strategy and oversee its implementation. I will chair the group, which comprises senior representatives of our core partners – government, firms, employers, not-for-profit organisations, consumer representatives and the media. The members of the group are listed at the end of this foreword.

We consider that the strategy should be based around consumers' needs, recognising that these change as consumers' circumstances change. To optimise speed and impact, we need to be clear about how content preparation and content delivery can best be allocated across partner organisations. I should emphasise that this is not about centralisation, but about a co-ordinated approach, getting better value for the money currently spent, drawing in new money and implementing with a high degree of flexibility and autonomy.

Our statutory objective of promoting public understanding of the financial system, together with the ability to raise finance from the industry for this purpose, gives us a clear remit to lead the development of this strategy.

We have discussed our thinking with a range of stakeholders and potential partners. They all agree that there is currently a lack of a UK strategy to improve financial capability, that this gap should be filled and that the FSA should take on the leadership role.

The strategy is the second phase of our public awareness work. Over the past five years we have taken forward our original consumer education proposals, published in November 1998. We have, from a standing start, increased year on year the scale, range and topicality of our public awareness work. We have fostered initiatives on financial literacy (including in the education system) and have provided independent information and guidance to consumers through a variety of channels, both directly and in collaboration with others. However, our experience (and that of others) has shown that much more needs to be done. And further that we need to engage with a much wider range of organisations, so as to make the most of each others' contributions, knowledge and experience.

We have also increasingly come to see the interdependence between our regulatory measures for consumer protection and our public awareness work. The effectiveness of the information and advice delivered to consumers by firms is critically dependent not only on the quality of the information for its purpose but also on the capacity of the consumer to understand and to benefit from it at the time and place of its delivery. Consumer understanding and awareness influence both the nature and the intensity of the regulation needed for consumer protection and also whether consumers derive benefit from competition in the market place. However, improving financial capability is complementary to, not a substitute for, firms treating their customers fairly – and there are some firms which have still not embedded this principle into their management culture and which now need to do so.

The FSA will, later this year, publish our high level objectives and plans for the future regulation of the retail market. This will bring together and take forward the consumer- and industry-facing elements of our work under a common set of core objectives that I made public in the summer:

- consumers' needs are well understood by themselves, firms and the FSA;
- consumers are financially aware, can take responsibility for their financial affairs, and (as a group) are able to influence the market;
- there is an economically sustainable distribution system that operates to standards that provide appropriate levels of advice and disclosure tailored to the needs of the consumer and complexity of the product;
- there is a choice of competitively priced products suitable to meet the financial needs of all types of consumer; and
- coherent and proportionate regulatory requirements are aligned to the risk of consumer detriment.

You will see that implementing the strategy for financial capability is critical to achieving these outcomes, in particular for ensuring that consumers are financially aware, can take responsibility for their financial affairs, and are able to influence the market. However no-one should be under any misapprehension about the scale of the problem that needs tackling or about the time it will take to make a significant impact.

The FSA will have a part to play within the strategy, in addition to its leadership role, but so will others working in the field. We hope that a broad range of players will join under the strategic umbrella. This paper does not set out to offer detailed measures. At this stage, our purpose is to offer for comment the main elements on which a strategy could be built.

We look forward to working with our partners in developing the strategy and ensuring a successful outcome.

A handwritten signature in black ink, appearing to read 'John Tiner', with a horizontal line underneath.

John Tiner
Chief Executive, FSA
November 2003

The Steering Group members are:

John Tiner, Chief Executive, Financial Services Authority (Chairman)
Luqman Arnold, Chief Executive, Abbey National plc;
David Clementi, Chairman, Prudential plc;
John Gummer MP, Chairman, Association of Independent Financial Advisers;
David Harker, Chief Executive, Citizens Advice;
Deirdre Hutton, Chair, National Consumer Council;
Digby Jones, Director General, Confederation of British Industry;
Ruth Kelly MP, Financial Secretary to the Treasury;
Ron Sandler, Chairman, Personal Finance Education Group.

A media representative will be announced shortly.

2 The problem

A growing body of consumer research suggests that consumers are far from confident in the decisions they make about their financial future. As a result, many people do not manage their financial affairs effectively and do not provide adequately for emergencies, life changes and eventual retirement.

Consumer research highlights low levels of consumer understanding, confidence and engagement across a range of financial needs.

There are low levels of **understanding** and **confidence**:

- Research for the Financial Services Consumer Panel shows that many consumers do not understand which products are linked to the stock market, and what the term ‘equity’ means.
- Two-thirds of consumers think that financial matters are ‘too complicated for them’ and that they do not know enough to choose suitable financial products.

Not surprisingly, **engagement** with personal finance is relatively low:

- Only 33% of consumers regularly review their financial situation. The research for the Financial Services Consumer Panel further concludes that across most life-stages and across a range of income/debt levels, there is considerable evidence of reactive rather than proactive financial management.
- 7% of the overall population remains completely outside the financial services market, having no mainstream financial products. In families where household income is between £150-£200 per week, this figure rises to 14%, and to 25% where the head of the household is a lone person. While some of these consumers may have made a rational decision not to engage in the market, our concern is that others may not be engaged due to their lack of understanding and confidence.

Changing behaviours is a difficult task under any circumstance

Efforts to improve financial capability must be rooted in an understanding of how to change consumers' behaviour. Our discussions with leading brand and marketing specialists confirm that repetition of key messages is important to ensure they are being heard, understood, agreed with and decisions are acted upon. A pre-requisite of success is co-ordinated and common messages. However, in the financial services sector, the sheer volume and variety of material consumers receive is a turn-off and consumers face message overload.

Factors which make this task more difficult

Among the factors which make the task more difficult are that a significant proportion of the population have poor literacy or numeracy skills. For example, 25% of adults have 'very low' numeracy, meaning they are unlikely to be able to perform even the simplest calculation.

Changes in society which give rise to an increasing need for the strategy

Factors which emphasise the importance of the strategy include demographics, employment trends and changing attitudes towards ways of managing money:

- The population is ageing. By 2021 there will be 48 pensioners for every 100 people of working age, compared to 30 per 100 in the mid-1990s. And more people live at distance from their elderly parents, increasing the need to provide for long-term care.
- Employment trends are changing. Having a consistent income over a long period of time is less common and there has been an increase in the number of temporary contracts. Two-fifths of employees are receiving significant amounts of their annual pay in the form of variable, discretionary bonuses. In addition, fewer companies are offering final salary pension schemes and, in those that do, fewer staff will benefit from long service.
- The ageing population and changing employment trends combine with changes to state pension provision to increase the need for individuals to take responsibility for providing for their retirement.
- Debt has become a common (and socially acceptable) means of managing personal finances. However, some people become over-indebted.

3 The consequences of the problem

Lack of financial capability has consequences for consumers, the industry, other service providers and, indeed, society as a whole. Few would dispute that it is a significant contributor to all of the following.

For Consumers:

Losing money

Our research shows that lack of understanding of how to shop around (or in some cases, such as for pension annuities, awareness that it can be done at all) leads to consumers losing out.

Not understanding or meeting needs

Lack of financial capability increases the risk that consumers will mis-buy financial products, that is they will make unsuitable purchases. For example, certain investment vehicles linked to equities may not be suitable for a consumer who may need to realise the investment in the relatively near future.

Lack of financial understanding also increases the risk that consumers may fail to buy products which would meet their needs or may fail to make sufficient provision to meet those needs.

Feelings of helplessness

Two in three consumers surveyed by the Financial Services Consumer Panel felt that financial matters were too complicated for them. This feeling of helplessness can lead to consumers not taking actions they need to take. Evidence from Citizens Advice Bureaux also suggests that fear and helplessness exacerbate problems in financial wellbeing, particularly in relation to debt.

For the Financial Services Industry:

Lack of consumer confidence in markets and in firms

Consumers who do not understand products or who feel that they have bought, or been sold, something unsuitable will lose confidence in the individual firms with which they deal and possibly with the market as a whole. This may mean that firms are losing customers or potential customers.

Increased costs

Inadequate understanding on the part of consumers, leading to mis-buying and increased vulnerability to mis-selling, means higher costs for the industry. Substantial costs have been incurred by firms responsible for past mis-selling and the costs of handling complaints when consumers have bought something which does not meet their needs are also considerable.

Stronger regulatory intervention

The FSA has a statutory objective to secure the ‘appropriate’ degree of protection for consumers. But what is appropriate will differ according to the level of general financial awareness consumers may have. Lack of financial capability has meant relatively high levels of regulatory intervention to protect consumers. Therefore, raising awareness has the potential, in the medium to longer term, to change the nature of regulation and possibly to reduce the burden on firms.

For other service providers:

More effort on reactive services

Lack of financial capability produces a greater need for reactive, problem-solving services, such as those offered by Citizens Advice Bureaux and other agencies. This results in limited resources being devoted to cure problems, rather than preventing them.

4 What's the solution?

It will be neither easy nor quick to make significant progress towards resolving these issues. However, we believe that the solution will need to have the following features:

A shared sense of purpose

There are already many participants who are actively involved in some aspects of developing financial capability. Some are focusing on helping put things right, such as specialist advice agencies; others on helping consumers to understand financial needs, such as educators; and others, such as financial companies and their trade associations, on helping to explain choices and options.

Our aim is to make more of the work we are all doing. To facilitate this, we need to agree a common set of goals or objectives to which we can all sign up and contribute. We all need to be pointing in the same direction to be effective.

Based around consumer needs

In order to engage with consumers, the strategy must be based on an understanding of those we want to reach. Many consumers don't recognise they have needs for financial services at all: they will often only identify a financial need in the context of some other event in their life. Understanding the financial needs of consumers, and the way that consumers identify these needs and seek to address them, will be key to finding the right approach for raising financial capability. In other words, we have to speak the language consumers speak.

The FSA is doing research to understand what drives consumers when it comes to financial services. We plan to use the outcome of this work to help to shape this strategy. Early findings will be set out in the forthcoming paper on the regulation of the retail market.

A co-ordinated approach

It will not be enough to agree common objectives. A more coherent, integrated, long-term effort is required. This will imply some agreement on priorities and co-ordination of related work programmes to ensure that the whole adds up to more than the sum of the parts. We will need to map what provision exists currently (and what is spent on it), to evaluate how effective this is, to identify gaps and to agree to fill them where appropriate.

With sufficient autonomy

Although we need to work together, we recognise that every organisation will have its own reasons for contributing to the strategy and will need to be confident that the work it is doing is in pursuit of its own objectives, in its own way. This will require a difficult balancing act.

Using targeted communications

Communication is not just a matter of providing information. A message that is not properly targeted to meet the needs of its audience is unlikely to be effective. In fact, evidence suggests that information overload is one of the reasons people switch off. The strategy must deliver simple, clear messages to specific target groups. It needs to be innovative in its approach, using both traditional forms of communication and developing creative options to deliver messages that people relate to.

We can learn from the FSA's experience and even more from that of others, particularly from financial services firms, about what works and what results we can expect to achieve with different communication methods and channels. And outside of financial services there is a wealth of experience of seeking to change behaviours, including the area of health education. We shall also want to use this experience to help to determine what works best.

One of the benefits of working together is to ensure we get the best from everyone's knowledge and learning. It is vital to tailor an action or message to the interests, needs and preferences of the target group so it can most effectively be delivered.

5 Scope of the strategy

The strategy covers the following:

- **Financial education:** improving financial capability will require clear, well-targeted and readily accessible financial education for children, young people and adults. The aim is to help people to get to the point where they recognise the importance of financial matters and where they know how to set about identifying and addressing their own financial needs and where to go for help.
- **Information:** in order to be fit for purpose, the information provided to consumers must address the questions which they have, be provided in a style with which they feel comfortable and be made available at a time and place which is convenient to them.
- **Generic advice:** the FSA will explore the scope for developing interactive generic advice service(s) (using people or technology or both). The aim is to help consumers identify their needs and to provide them with generic solutions: it is not about providing product-specific recommendations. It may be possible to build on advisory services and other facilities which are already available.

The strategy is **not** about encouraging people to buy specific products, nor about delivering information on specific products from specific providers. However, the strategy is likely to result in more people buying products. The strategy does not cover regulated advice, nor regulated information. However, the strategy may lead more people to use them. The strategy is not about teaching consumers basic numeracy skills, which is better led by government. However, the degree of success the government achieves here will influence the success of the strategy. Nor is it directly about tackling over-indebtedness. However, as a result of the strategy, people should be better able to manage their financial affairs.

6 How will the strategy be developed, funded and implemented?

We recognise that those working with us will want to be able to influence the strategic direction of the development and implementation of the strategy for financial capability. We have therefore set up the Financial Capability Steering Group, to be chaired by John Tiner, which comprises senior representatives of our core partners. Members of the Steering Group are:

John Tiner, Chief Executive, Financial Services Authority (Chairman)
Luqman Arnold, Chief Executive, Abbey National plc;
David Clementi, Chairman, Prudential plc;
John Gummer MP, Chairman, Association of Independent Financial Advisers;
David Harker, Chief Executive, Citizens Advice;
Deirdre Hutton, Chair, National Consumer Council;
Digby Jones, Director General, Confederation of British Industry;
Ruth Kelly MP, Financial Secretary to the Treasury;
Ron Sandler, Chairman, Personal Finance Education Group.
A media representative will be announced shortly.

In the first instance, the Steering Group will be asked to address the following:

- What should be the objectives of the strategy?
- What should be the priorities for action, including which consumers should we look to reach and with what messages?
- How should we look to achieve the objectives?
- How should we measure the success of the strategy and over what time periods?

The conclusions reached by the Steering Group on the above questions will, taken together, form the basis for the strategy. We are aiming to publish this by the end of March 2004.

To help support the work of the Steering Group, we will be setting up a Working Group. This will be chaired by the FSA Consumer Director, Anna Bradley, and will consist of working level representatives of similar organisations to those represented on the Steering Group.

Funding of the strategy

We need to understand how much money is currently being spent on increasing financial capability and try to get the best value from it. But we also consider that increased expenditure will be needed.

The FSA may well need to increase its own spending in this area. We would, of course, need to consult on any additional expenditure that may be required (as well as on any changes which may be needed to existing funding arrangements). We therefore expect that any additional FSA funding would not be available until the 2005/6 financial year.

We have thought about voluntary funding. Although such funding will doubtless continue to play a part in the resourcing of some partner organisations, it is not an option for the FSA. We have a duty to deliver a statutory public awareness objective and a power to levy the funds needed for the purpose. Delivery should not, in these circumstances, be conditioned by the levels of voluntary funding achieved. Moreover, there would be other difficult issues for the FSA: of compromise (or the appearance of it); and of accountability.

Money raised by the FSA will not be sufficient to fund the entire strategy: partners will need to play their part in generating the necessary funding, though there may be a role for the Steering Group and also the FSA more generally in supporting this. We expect that the very existence of a joined-up strategy will help to attract additional funds.

Implementation

To ensure the effective use of limited resources (money and people), we envisage that:

- work will be broken down into manageable initiatives;
- initiatives will be selected on the basis of whether they are likely to be effective and represent good value for money;

- some activities will be selected which will deliver fast, as well as some that are longer term; and
- we will be opportunistic and take advantage of existing initiatives, plans, relationships or arrangements to deliver the strategy's outcomes.

The FSA's role

The FSA will have two main roles:

- Leading and facilitating the development and, in due course, the implementation of the strategy. John Tiner explains in his Foreword the rationale for the FSA taking on this role.
- Taking responsibility for the delivery of specific elements of the strategy. The elements which the FSA takes forward will be determined according to where the FSA is best placed to make an effective contribution, having regard to the FSA's own priorities.

7 What will success look like?

We envisage that progress on delivering the strategy should be measured on three levels:

- how well we have **reached** target consumer groups;
- how **awareness, understanding and confidence** have changed; and
- how we have achieved **changes in specific behaviours** across the population.

We recognise that different partners may have different perspectives on what they would like the strategy to achieve. We will discuss with stakeholders what would be an appropriate set of outcomes for the strategy.

Over what kind of timescale?

In discussions with stakeholders, many have stressed the size of the task we are taking on. While it is important that the strategy produces some early results, the full impact of the strategy is likely to be seen over the next generation and beyond.

We recognise the need to tackle the problem in bite-sized chunks. We will identify, in collaboration with partners, a range of fairly immediate targets over specific periods of time. This should help us to assess whether we are heading towards our long-term goal of confident, better-informed consumers.

We expect to see some improvements in consumer understanding, engagement and confidence as a result of the strategy's initial priority actions by the end of 2007, significant improvements across a range of actions by 2010 and, in the longer term, a much more informed, educated and confident financial services consumer.

Ultimately, how much the strategy achieves depends on the extent of our ambition and on the nature and level of support we receive from our partners.

8 How we will engage with our partners

In addition to engaging with partners through the Steering Group and the Working Group:

- we now invite interested parties to e-mail us at *financial.capability@fsa.gov.uk* with their views on any of the issues raised by the document. It would be particularly helpful if at least initial comments could reach us by Friday 12 December, so that they can help to inform our early work;
- we will run workshops with different groups of stakeholders to help us in developing the strategy and in determining how success might be measured.

We will also participate in conferences and will consider arranging our own events to promote awareness of, and stimulate debate about, this initiative. In addition, we hope that the media will help to promote awareness and debate among a wider audience.

The Financial Services Authority
25 The North Colonnade Canary Wharf London E14 5HS
Telephone: +44 (0)20 7066 1000 Fax: +44 (0)20 7066 1099
Website: www.fsa.gov.uk

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