An Evaluation of Policy Initiatives Designed to Aid Decision Making in Personal Finance in the UK

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Introduction

In the UK, policy makers are concerned that many consumers lack interest in, and understanding of, financial services, not least due to a high degree of product complexity and opacity in the marketplace (HM Treasury, 2002). Potentially detrimental outcomes of limited understanding and a lack of transparency in the marketplace include; "mis-buying" by consumers, as they choose products which are inappropriate for their needs (Johnson, 2000); and even a lack of adequate provision by consumers as they withdraw from the market (Noble and Knights, 2003). Under-provision, known in the UK as “the savings gap”, has been estimated at £27 billion per annum (Association of British Insurers, 2002) In such circumstances, mis-selling is also more likely to occur as firms and their agents exploit limited consumer understanding, with the result that public confidence in financial services markets may be undermined. To counter such problems, the UK Government has introduced policy initiatives (PI) (see Appendix for details) aimed at benchmarking or stipulating simplified financial services product specifications, with the objective of helping consumers make better, more informed decisions (HM Treasury, 2002; 2003). Policy makers have unambiguously indicated the primary target market for the PI outlined above: low to medium income consumers, those with little experience of financial services, those with limited savings and pension provision and those in a position of vulnerability or weakness due to low expertise and/or a lack of interest or involvement (HM Treasury, 1998; Johnson, 2000; HM Treasury, 2002; HM Treasury 2003).

Objectives

It is essential that the PI outlined above should appeal to the target market identified if the Government is to realize its core vision of providing better access to financial services markets for disadvantaged consumers, according to HM Treasury (2003). However, a number of interested parties have expressed reservations as to whether the PI introduced will impact in particular on the target market. Thus, the objectives of this study are to establish (a) the degree to which policy initiatives resonate with consumers generally and in particular with the target markets identified and (b) the relative contribution of measured consumer characteristics such as involvement, familiarity and expertise compared to relying exclusively on demographic variables such as income, age etc in trying to better understand potential responses to the PI and attendant lessons for policy makers

Methodology

The data used in the study were collected by means of a questionnaire administered by telephone. A total of 1002 telephone interviews were carried out in the UK in late summer of 2004, with the assistance of a professional market research agency. The sample was constructed to ensure representativeness of the UK population. For the measurement, a fully structured questionnaire was used, with the measurements required mainly taken from previous published research, with some scales developed by the researcher for the purposes of this study. Scales measured consumers’ preference for PI, involvement, familiarity, objective expertise and subjective expertise. Some manipulation of the objective and subjective expertise measures were carried out to allow a more sophisticated analysis of the data.

Results, Discussion and Implications

The results of the study suggest that the general level of acceptance of the PI under investigation appears reasonably high, with that data also indicating that consumers of financial services are positively disposed towards Government efforts to signal good value and minimum standards in the market place. Positive attitudes towards the PI initiatives are important if such changes are to help consumers overcome opacity in the marketplace, reduce instances of mis-selling and reduce the degree of under-provision on the part of consumers and potential consumers. Policy makers will be encouraged that their initiatives have, generally, been accepted reasonably enthusiastically and may well be assisting consumers in their choice process.

The results of the study further suggest that, to a large extent, the Government may be frustrated in its ambitions for the financial services market. The PI appeal more to those who are highly involved in financial services, as those who are already interested in and appreciate the personal relevance of financial services are more inclined to see merit in PI. Such individuals are less likely to be those that are confused, vulnerable and under-providing. Thus, a considerable amount of effort and expenditure is being invested in policy initiatives which will not appeal to the less involved. Policy makers would no doubt prefer that those with low levels of involvement and less engagement with financial services would view PI positively and respond accordingly, hence helping to correct problems of lack of understanding and provision amongst less involved consumers. The results pertaining to familiarity offer further evidence that the government may fail in its ambitions, with the PI appealing to those more familiar with financial services. The results with respect to knowledge are more mixed. Finally, there is no evidence to suggest that PI appeal particularly to low to medium income consumers, those from the lowest social classes or from ethnic minorities, all groups who may face particular challenges in engaging with financial services.

Appendix

The first policy initiative studied is the "CAT standard" scheme, whereby products which meet a Government stipulated set of criteria can be publicized as CAT standard approved. The CAT standard scheme covers one class of product, namely home loans, known in the UK as mortgages. However, as a recent estimate puts the value of home loans taken out annually in the UK at over £293 million (Council of Mortgage Lenders, 2004), this means that a significant element of the retail financial services market which could still potentially fall under the CAT standards scheme. In effect, the CAT standard is a benchmark against which firms can voluntarily measure their product specifications. The criteria covered concern **C**harges, **A**ccess and **T**erms, hence CAT, and CAT standards were initially designed to ensure that such products should always offer consumers a reasonable deal (Johnson, 2000). The Government has urged consumers to view CAT standards as a benchmark, or endorsement, of a minimum set of standards. The CAT standard scheme is voluntary, with firms left to choose whether or not they wish to design their products in accordance with the guidelines.

A more recent and more widespread initiative aimed at assisting consumers in making decisions more aligned to their interests is the introduction of the "Stakeholder" product suite. This suite of products is designed to offer simple, price-controlled and regulated products that can be provided through a simplified sales process (HM Treasury, 2003). Seemingly similar to the CAT standard scheme, in the case of Stakeholder products the Government sets standards for charges, access and terms, including a cap on charges of 1.5% annually. However, Johnson (2000) highlights important differences between the Stakeholder regime and CAT standards. The former represents a class of product and the standards set are compulsory for any product wishing to be designated as Stakeholder. The latter represents a voluntary benchmarking scheme in which it is entirely up to providers whether to design products that meet the criteria specified. The first stakeholder products, namely pensions, have been available since April 2001 and the concept has recently been extended to include a cash fund, a stock market based mutual fund, a "with-profits" (participating) life assurance fund and a child trust fund (a limited contribution tax free mutual fund or cash-based investment for each child).

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Endnotes

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[2]The author would like to acknowledge funding from the Financial Services Research Forum