Can innovation in financial services tackle financial exclusion?

Notes of a discussion roundtable hosted by the Community Investment Coalition

Attendees

Lord Griffiths of Fforestfach (Chair)

Callum Anderson (Community Investment Coalition)

Jennifer Tankard (Community Investment Coalition)

Professor Sharon Collard (Open University and the Financial Inclusion Commission)

James Crump (Which?)

Jake Eliot (Money Advice Service)

Matthew Ford (Pariti)

Niamh Goggin (Small Change Ltd)

Joseph Henson (Centre for Social Justice)

Ben Hughes (Community Development Finance Association)

Alex Letts (Ffrees)

Fiach Maguire (My Community Bank)

Dame Mary Marsh (The Clore Social Leadership Programme and the Financial Inclusion Commission)

Frank Mukahanana (Quid Cycle)

Mutaz Qubbaj (Squirrel)

Andrew Robinson (CCLA)

Sureena Santos (Fairbanking Foundation)

Alison Seabrooke (Community Development Foundation)

Andy Walton (Centre for Theology and Community)

Ellie Ward (Pioneers Post)

Opening remarks from Lord Griffiths of Fforestfach

- Interest in this area began while a lecturer in the 1960s: researched money creation and competition and regulation in banking.

- Found that all markets within financial services were cartels.

- Explored the social; cost of a cartel – should cartels exist?

- Concluded that cartels were bad for competition and consumers, as well as hampering innovation in the industry.

- Bear in mind that, at the time, consumer credit was controlled. Working class consumers' credit products were predominantly hire purchase products, while the middle classes had a broader array of options.

- Democratisation of credit did not arrive in the UK until the 1970s.

- In 2003: on the request of Oliver Letwin and the Conservative Party, begun to explore the relationship low income families had with debt. This research was conducted through a non-partisan commission and was published shortly prior to the 2005 General Election.

- Reality is that low income families need credit just as much as middle and high income families.

- When considering the provision of financial services to communities, there are five main questions:

    1) What is the role of the public sector?
    2) What is the role of local and central government?
    3) What is the role of (social) enterprise?
    4) What is the role of regulations and regulators?
    5) What is the role of innovation and technology in supporting this?

- Technology is changing the fabric of financial service provision and will continue to do so in the future.

Alex Letts, Ffrees

- What is the percentage of UK households earning more than £28,000 per year? [21.2%]. Therefore 78.8% of UK households earning below £28,000.

- 65% of people can last only one month until they face significant financial distress.

- Percentage of customers that banks make a profit from via a current account **only**? [30%].

- Banks are dependent on overdrafts and other fees to make a profit form current accounts.

- This reality has led to a banking model that drivers people to debt: society cannot afford it.

- Retail banking is not yet democratised.

- ***Bill Gates: "Banking is essential, banks are not."***

- **Ffrees:**

    - A digital current account
    - Everything is transparently charged.
    - Customers are actively encouraged to save.
    - Ffrees gained 60,000 accounts in its first 18 months with revenue of £80k per month.
    - By September, Ffrees will offer a full suite of transactional current accounts. But will **not** drive people into debt.

Mutaz Qubbaj, Squirrel Financial Services

- Average UK household has £240 of disposable income a month after essentials are taken into account.

- 1 in 4 UK households have £50 of disposable income after essentials are taken into account.

- 1 in 10 UK households have no disposable income after essentials are taken into account.

- The payday loan market has grown significantly (into a £3-4 billion market).

- Main banks charging £5 per day to customers who have unauthorised overdrafts – an extortionate amount of interest paid.

- **Squirrel:**

    - A financial wellbeing platform that partners with employers to provide simple and intuitive tools to help their employees to save, budget and manage their bills directly from their payroll.
    - Offers employees the ability to save directly from payroll for targeted expenditure (such as Christmas).
    - Incentive for employers: by addressing financial distress of employees; raises productivity (can increase by as much as 20%); reduced staff turnover; reduces absenteeism; reduces fraud.

Frank Mukahanana, QuidCycle

- Banks: ultimate aim is for profitability from their credit/debt products.

- **QuidCycle**

    - Tackles middle income financial capability.

- Focus on households who have taken on more debt than they would ideally like and suffer form a lack of knowledge of financial products.
- Aim is to out-compete traditional financial service providers by helping families out of debt (predominantly through consolidating multiple debts).
- Refinances debt by closing accounts (i.e. at credit card companies). Although this costs money we feel it is the right thing to do by our customers.
- Uses a peer-to-peer platform to raise capital.
- Works with every borrower until they are debt free (regardless of time horizon).
- Offers incentives such as cash back of up to 4%.
- Each customer's target is to reduce the level of debt each year.
- Each customer is offered 2 hours of financial education (delivered online) each year.
- Customers meet with a financial advisor to discuss their financial situation/goals. (QuidCycle pays for this to enhance financial capability of customers).
- Technology is an important element in successfully delivering services.
- Financial exclusion can affect people on middle incomes just as much as those on low incomes.

Fiach Maguire, MyCommunityBank

- **My Community Bank**

  - Grew out of a credit union called Brent Shrine Credit Union, formed in 1979.
  - Initially to serve people living or working in the London Borough of Brent.
  - In 2013, common bond was extended to include members and supporters of The South Asian Community across the UK.
  - Raises capital privately (no public subsidy).
  - Addresses needs of the underbanked population.
  - Works with innovators to produce a suite of financial products.

Open discussion: What changes do we need to see from regulators, the Government, investors and others to encourage innovation that benefits low income communities?

1. How do the featured enterprises make money to survive?

2. Are these enterprises scalable?

3. Can we solve financial exclusion without public subsidy?

4. On innovation:
    i. How do we reduce the costs of payment mechanisms?
    ii. How do we increase financial capability, education and planning?

Mutaz Qubbaj (MQ):

- Employers are a key stakeholder for Squirrel.
- Squirrel's services costs employers between £5 and £10 per employee per year.
- Whilst there is no need for public subsidy, there could be scope for us to work with Department of Work and Pensions to assist benefit claimants.
- We provide a financial platform for employees.

Alex Letts (AL):

- Banks do not understand the concept of 'digital'. To them, it simply means a [mobile] app, use of social media and cutting backroom staff.
- In fact, it means changing the banking business model.

Ben Hughes (BH):

- CDFA – trade body of Community Development Finance Association (CDFA), who lend £200 million to individuals and businesses.

- Public subsidies aren't the answer. It is about determining new financial instruments to meet different needs.

- There is a clear case for the commercial market failure of the mainstream banking sector. It is nigh on impossible to lend to people who are constructs of this market failure.

- It is also clear that alternative providers of financial products/services exist – but they are underdeveloped.

- There is a distinct lack of poltical leadership on this issue. Yet, leadership is key if we are to have effective legislation, regulation and a new flow of capital into alternative providers of finance.

- Q: How financially excluded are the customers (of Ffrees, Squirrel, QuidCycle and My Community Bank)?

Lord Griffiths:

- Is there a need to recreate savings institutions akin to that of the Post Office Savings Bank and Trustee Savings Bank (similar to those seen in Germany)?

- Acknowledged that the privatisation Post Office Savings Bank and Trustee Savings Bank was wrong.

- Surely a political consensus exists to tackle this issue (as shown by the £38m Department of Work and Pensions investment in the credit union sector).

Alison Seabrooke (AS):

- Key point – financial literacy of civil servants and politicians is low. This significantly inhibits their ability to challenge the status quo in the financial services industry.

- Q: How do you engage with communities, linking the technology that they have at their disposal (i.e. smart phones, the internet etc.), and connect that with the financial products/services they seek?

AL:

- Fair to conclude that older people will not be our customers. Thus we target those who actively use smart phones, have access to the internet etc.

Andy Walton (AW):

- Centre for Theology and Community worked with Citizens UK to propose Community Finance Foundation: a proposal to use £200 million of fines on banks and payday lenders levied in the next Parliament (2015-20) to support community finance organisations.

- The venture would help 500,000 people avoid high-cost credit, saving them over £200 million per year in interest and fees and reducing the cost of problem debt on wider society by £1.4 billion.

- A proportion of the money could go towards building infrastructure (of which technological advances could play a key role).

- However, political will at the moment has been lukewarm towards this idea.

AL:

- There are also signs that there is will within the private sector to invest in the area of fintech, especially in the field of building infrastructure.

- But key point: venture capitalists (i.e. the investors in fintech companies) do want a quick return on their investments.

- We can't rely on a handout from the state to build and maintain a sustainable sector that tackles financial exclusion.

Niamh Goggin (NG):

- There has always been an assumption in the developed world that we are more advanced in the area of fintech. But, as has been shown numerous times in Africa, this is simply not the case.

- A key element of fintech companies retaining their customers is combining their technology with fostering basic trust from their customers.

- There is a need to develop an investment driven approach towards financial service provision.

- A long term support programme is needed, embodied by a partnership between the public and private sector with experienced people needed, in order to develop a sustainable sector.

- Also vital that there are no 'poor people's products'.

Matthew Ford (MF):

- Pariti – provides tools, guidance and access to low cost loans to help customers out of high-interest debt.

- Another factor: the opaque credit assessment methodology employed.

- There are a very small number of credit assessors.

- Pariti is seeking new ways in addressing people's credit worthiness.

- Difference between Pariti and Experian: actually trying to inform people how they can improve their credit rating.

Frank Mukahanana (FM):

- Challenge: Delivering social benefit whilst still being commercial sustainable.

- 'Ordinary citizens' act as lenders to QuidCycle's customers. They do so because, despite the higher risk, they are attracted to the prospect of having a bigger social impact.

- Technology enabled people to see how their money can make a difference.

- QuidCycle hopes to harness the pension reforms and the opening of the ISA markets to peer-to-peer platforms as a new source of capital.

Professor Sharon Collard (SC):

- Communities have diverse needs in the financial services space.

- A clear crossover between social policy and banking business models exists.

- An issue of an increasing demand for consumer credit in an environment where incomes are too low and demand from general goods and services is too high. Therefore it is vital that people with all incomes have access to credit.

- Also important to highlight that the needs of people on low incomes are different from those on benefits.

- Ultimately, people just want a system that works. It is a false to suggest that it is merely *banks vs non-banks*. People will use services that work in their interest, be that a mainstream bank, the post office, or a pre-paid meter (despite their high cost).

- Technology and innovation are not one and the same thing.

- There also needs to be a focus on building people's digital literacy and general capability.

Joseph Henson (JH):

- It is important that there is **no** top-down approach to this issue.
- Essential that there is solid understanding of the services people are demanding.
- Need to bridge the willingness of investors to finance the many fintech ideas that exist.

Fiach Maguire (FMag):

- Public subsidy of credit unions has not helped the sector grow and scale up within the last fifty years.
- In the credit union sector, there are more grant officers than marketing directors.
- Subsidies are distorting markets.
- Department of Work and Pensions' £38 million investment into the credit union sector is unlikely to have much of an impact.
- Definitely need to fix the payments system.

Dame Mary Marsh (MM):

- We must not forget the importance of financial literacy.
- The more that people are aware of the implications of financial decisions, the more likely that they will be able to exploit the benefits of financial technology services.

Lord Griffiths – Closing remarks and conclusions

- Ultimately: **yes** – innovation can help tackle financial exclusion.
- Evidence suggests that there has been poor regulation of the retail financial services, which have led to poor outcomes for consumers.
- Will innovation attract more private capital and private provision into this market? How can this be further encouraged?
- Will innovation help people to better change their finances? Can it help people out of debt?
- How do we ensure that innovation in financial services benefit the bottom two million Britons who are fundamentally excluded from the financial services industry, as well as low and middle income people?
- In addition to the practical need of providing basic financial services to communities how do we make financial exclusion a 'moral concern'? There could be more scope for the Church of England to extend its role in this.

For more information

For more information, please contact Jennifer Tankard, Community Development Foundation (CDF) on 020 7812 5430 or jennifer.tankard@cdf.org.uk.

About the Community Investment Coalition

The Community Investment Coalition is a partnership of national organisations including financial providers, charities, trade associations and academic bodies. Our mission is to promote access to affordable finance for families, businesses and communities.

CIC campaigns for:

- Increased transparency and public accountability of financial service providers to support consumer choice and allow effective intervention in under-served markets.

- Increasing diversity of providers and choice for consumers in the financial services sector, with more providers offering a wider range of fair and affordable products to households, individuals, communities and businesses.

- More innovation in the financial services sector so that affordable financial products are delivered accessibly to all communities.

- Sustainable local economic growth with a greater share of locally generated income remaining within communities.

- Improvements in financial literacy for all sections of the community.

We do this by:

- Collecting and sharing evidence and knowledge through research, conferences and dialogue;

- Campaigning for a regulatory system which helps not hinders community investment;
- Speaking with a unified voice on issues facing the sector; and

- Building the capacity of the Community Investment Sector through infrastructure and collaboration.

Partners include the following organisations:

The Centre for Responsible Credit (CfRC) is a dedicated unit established within the Centre for Economic and Social Inclusion to: monitor the development of credit markets; research models of responsible provision and promote policy responses which protect the long term interests of households.

CCLA manages money for more charities than any other fund manager in the UK and we are owned by our not-for-profit clients. We engage with the banking sector every day on behalf of our charity and local authority clients, who are concerned with issues that may affect shareholder value, but also wish to see account taken of their ethical investment concerns. CCLA is ranked top manager of ethical and responsible investment funds in the UK by assets under management.

Local Trust delivers the Big Local programme with an investment of over £200m from the Big Lottery Fund. Big Local is happening in 150 communities across England over the next 15 years. It provides residents in each community with at least £1m and a range of other support and funding to develop ways of making their areas even better places to live.

CDFA's mission is to support the development of thriving and sustainable community development finance (CDFI) sector that provides finance for disadvantaged and underserved communities and, as a consequence, contribute to the increasing prosperity of these communities.

The Community Development Foundation (CDF) is a social enterprise passionate about helping communities. We have unique expertise in using community development to strengthen local voices, improve people's lives and create better places to live. Our vision is for successful lives in flourishing communities.