Leading on Investments and Savings

Response to the Treasury Committee's Inquiry into Household Finances

January 2018

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About TISA

TISA is a unique, consumer focused, financial services membership organisation. Our aim is to improve financial wellbeing by aligning the interests of UK consumers, the financial services industry and the economy. We achieve this with evidence-based proposals to government, policy makers and regulators.

TISA's membership comprises over 170 firms representing all sectors of the financial services industry: asset managers, insurance companies, fund managers, distributors, building societies, investment managers, third party administrators, FinTech, consultants and advisers, software providers, financial advisers, pension providers, banks and stockbrokers.

TISA also supports a range of operational and technical initiatives targeted at improving infrastructure and processes, standards of practice and the implementation of new rules and regulations.

TISA has a successful track record in working with government and regulators to enhance customer outcomes and improve industry effectiveness.

Executive Summary

TISA is pleased to submit our thoughts and evidence on the state of household finances for consideration by the Treasury Committee. At the heart of our work is the view that everyone should be able to make the most of their money throughout their lives, which is far from the case at present.

In November 2017, TISA launched a new biannual Savings Index providing a unique view of the total savings of UK households by region and age. The TISA/KPMG Savings Index is designed to encourage and monitor long term saving. We would be delighted to expand on the insights we believe it will deliver for the Committee in person.

The first TISA & KPMG Savings Index found:

- Median average savings of households in Great Britain (including property, pensions and financial assets) is £233,000;
- There is a huge disparity between those who own a house (£421,000) and those who do not (£4,000);
- Although the North-South divide on property values remains wide, it is narrower on pensions

Enabling people to benchmark their savings against peers should help nudge to greater saving. We hope it will help households set long-term goals and plan for their future financial wellbeing.

We believe some straightforward policy solutions could incentivise and enhance household savings. These are explained more fully below, but briefly we'd ask the Treasury Select Committee to recommend:

- Amending the statutory objectives of the Financial Conduct Authority to include increasing the median level of household saving (in addition to fair treatment of individuals and market integrity);
- Establishing a regime for public and private sector provision of free financial guidance that provides meaningful support for households seeking to save and invest;
- Ensuring the Single Financial Guidance Body (SFGB) has measurable accountability to increase median savings levels and that it collaborates with the financial services industry to achieve this aim;
- Enhancing financial education in schools by including this within the primary school curriculum, and providing funding for teacher training at both primary and secondary schools;
- Reviewing the taxation regime for pensions, including making this more effective in encouraging consumers to save adequately for retirement;
- Giving a single government department responsibility for creating and implementing strategic policy to enhance median levels of savings;
- Supporting the development of a Digital ID that helps consumers engage with their finances and makes saving and investing easy and secure.

Household Savings: the state of the nation

1. TISA has produced several reports[1] that evidence low levels of saving in the UK and has developed a Savings Index to track the national savings median and have used key findings to substantiate our recommendations below.

2. A third of UK households have no spare income to save. Another 20% have less than £1,500 to cope with an unexpected event[2]. Propensity to save is down to the individual as well as their financial situation.

3. A savings culture has been replaced by easy access to debt to finance consumption[3]. Furthermore, whilst relative salaries have increased since the 1940s, successive generations have spent more and saved less, reducing household financial security.

4. Property-price growth has resulted in a major share of national wealth now being held by the aged. 80% of over 65 year-olds are owner-occupiers of their home. This wealth is likely to be released to subsequent generations as a windfall, but may be used to make up the significant shortfall in retirement savings for those aged over 50 years-old today.

[1] TISA - Our Financial Future, Saving Our Financial Future, Strengthening the Incentive to Save, Financial Advice Market Review, Can Housing Wealth Save the Day?

[2] TISA – Our Financial Future

[3] TISA Our Financial Future

5. Both state and employers have reduced pension payments[4] substantially, meaning individuals must save more to achieve adequate retirement incomes. Whereas previously, a major proportion of retiree needs were met by well-funded workplace pensions, the cost is now borne to a much greater extent by individuals. Society has not yet adapted to this new paradigm.

6. ISA savings are increasingly positioned as an alternative to pension saving. However, this creates a situation where fewer people pay income tax in later life (when they represent the heaviest burden on the state). Promoting ISA usage for retirement saving provides government with higher tax revenues today, but creates a higher tax burden on future generations.

7. The TISA Savings Index shows that when it comes to savings, UK households are far from homogenous. Effective responses should recognise certain consumer segments face more challenges than others. Baby boomers (aged 53-71) tend to have more wealth than subsequent generations. The cohort aged 45-55 are poised to receive pensions 30% lower than baby boomers, with those who have under-saved, finding auto-enrolment is too little too late. However, many will benefit from inheritances resulting from high levels of home ownership in their parents' generation. People aged 35-45-have grown up in a credit-driven world of large mortgages and high house prices and often do not appreciate retirement costs. Young adults (18-34) are affected most by expensive housing and less generous pensions. They must save more than previous generations to fund extended lifespans, but do have the advantage that saving today has longer to grow.

8. Under-saving cannot be separated from the issue of wealth inequality. The bottom 20% of consumers own less than 1% of the wealth, the bottom half just 9%, whilst the top 20% owns 62% of the wealth[5]. TISA believes regulatory and legislative efforts must focus on the financial well-being of the low and middle-income households.

Obstacles to progress

9. TISA is disappointed with the outcome of the FCA's Financial Advice Market Review (FAMR) of Advice and Guidance, which focussed on less than 10% of the population[6], largely ignoring the majority of households who do not have money and need free guidance to make informed decisions about how to save in their particular circumstances. Over the course of the review, attention shifted to focus primarily on financial advice, despite FCA research showing that financial advice was only affordable or attractive to 3 million people (6% of households) in the last twelve months. The FCA believes a further 6 million people might pay for financial advice if the cost was £500 or less.

10. This leaves 42 – 48 million people who will rely upon financial guidance to make key decisions. The SFGB alone will not be able to support this group and financial services firms are currently not allowed to provide anything more than generic information, without it becoming regulated and charged advice. TISA continues to work with the FCA to identify where regulations might

[4] TISA – Our Financial Future

[5] TISA – Our Financial Future

[6] FCA – FAMR baseline Report 2017

allow financial services firms to provide more helpful guidance to customers and support the SFGB in addressing the guidance gap.

11. This situation has occurred partially because the Retail Distribution Review has combined with MiFID, so that anything that might be considered a personal recommendation is regulated advice, for which fees must be charged. The FCA has proceeded with a solution to improve the quality of advice, without a parallel solution (in the original scope of RDR and FAMR) to increase consumer access, despite concerns that an advice versus guidance gap would inevitably result.

Solutions

12. We believe the financial services industry has a major role to play in encouraging household savings. This is best done by supporting focused government-sponsored initiatives rather than through introducing new products, or the notion that improved value and transparency (however desirable and important) would deliver a sea change in consumer culture.

13. Solutions should consider the ‘nudging’ approach that has made auto-enrolment a success and how it could be applied to a high percentage of the population.

14. The provision of free financial guidance for everyone is critical and TISA remains supportive of the creation of the SFGB. However, we caution that there will be a gulf between the SFGB resources and the required capacity to deliver to the 42 million people who need support in managing their money[7].

15. The SFGB needs to work with financial services to leverage the industry’s unparalleled reach, capacity, data, experience, and available product solutions. TISA recognises the genuine concerns held in some quarters about industry participation in delivering financial guidance, and there would need to be effective governance. However, the alternative is to continue along a failing path, leaving millions without the right support to make informed choices for themselves.

16. TISA believes that the FCA will not take assertive action on under-saving as its statutory objectives do not include the financial well-being of the population at large. It focuses on the potential detriment to small numbers of active consumers rather than encouraging greater savings and investment for the mass market. TISA believes the FCA should be given a responsibility to improve the median level of household savings, concentrating on consumers in the lower quartile of earnings.

17. We encourage government to consider specific measures as part of a concerted effort to get the nation saving again. For the long-term welfare of our society and economy, we need a national strategy for saving. Policy needs to address the transfer of financial risk and responsibility from state and employer to individuals, the shift of financial dependence from saving to debt, and of financial wealth from young to old. We need to encourage greater financial capability and engagement, counter inequality, reduce social instability, and manage threats to the future of our economy.

[7] FCA – FAMR Baseline Report 2017

18. Government and industry also need to facilitate greater consumer engagement with their savings through technology. Government has a key role to play in supporting the development of a Digital ID that helps consumers manage their finances and makes saving and investing easy and secure. TISA is piloting a Digital ID in Q1 2018 plus working with Government Digital Services and other key players to agree a way forward that can be adopted by the mass market.

Overall savings levels and balance sheets

1. **What determines the aggregate level of household net saving and the saving ratio in the macro-economy? Can policy affect the aggregate level of household saving?**

19. Factors that underpin the savings ratio correlate to a diverse number of elements including consumer confidence in employment security, wage inflation and ability to service debt.

20. With the increased access to credit, a higher savings ratio does not necessarily result in more cash in the bank, rather a reduction in debt. The savings ratio rose from just over 4% in 2008 to over 11% in 2010, dropping to 7% in 2012[8] post the financial crisis. This was offset by a reduction in consumer credit from £249bn in 2008 to £170bn in 2012[9].

21. Take up of ISAs and auto-enrolment show that policy can affect savings. However, there is a lack of policy co-ordination across general and retirement savings – there is no consumer saving strategy nor a single department owning this objective. TISA also believes the FCA's current mandate is a barrier to encouraging greater savings as outlined above.

2. **What is the "right" level of saving for households and the UK economy more widely, in view of prevailing and potential future economic conditions? To what extent does the UK have a "savings gap"?**

22. Appropriate saving levels depend on individual circumstances, but should be sufficient to offer 'rainy day' resilience, and retirement provision. FAMR recommended that 'Rules of Thumb' be developed as benchmarks for consumer savings. This has been passed to the Money Advice Service (MAS) to progress and determine the right levels of savings for consumer segments. We would encourage the Treasury Committee to recommend additional budget to complete this work to a high standard.

23. The scale of the savings gap depends on what levels of savings are deemed appropriate. However, we can point to evidence that suggest consumers are under-saving.
    - 30% of households have no savings at all [10]
    - A further 20% have less than £1,500 in savings[11]

[8] Source ONS
[9] Source BoE
[10] TISA – Our Financial Future
[11] TISA Our Financial Future

- In 1996, around half the private sector were saving into a pension, which reduced progressively to around 35% by 2012[12]
- Two thirds of people retiring in the next 15 years have under-saved in terms of meeting the DWP target income levels[13]

3. How do household balance sheets vary across generations?

24. There are significant progressive reductions in household wealth across generations. We have identified some examples below:

    a) **Housing wealth**. The average age of a first-time buyer has risen from 24 in 1970 to 30 in 2016[14]. The percentage of people aged 25-34 who were owner occupiers has slipped from around two thirds for those born 1950-1970, to one third for those born in 1980 and later.[15]

    b) **Pension savings**. Increased longevity means whilst the generations born in the 1950's worked 3 years for every one year in retirement, those born in the 1990's and later can expect to work only two years for every year in retirement. This makes saving for retirement more challenging.

    c) **Student Debt**. Around half of young adults now go to university, incurring an average level of debt of £50,000[16], making saving for a deposit for a house, retirement and for general purposes even more challenging.

25. Comparing the need to save, with changes in pensions, we see younger generations facing a big squeeze in retirement. Generous Defined Benefit (DB) schemes have been declining in the private sector since the mid 1990's. Whereas the median value of a DB scheme for 55 to 64 year-olds is £184,000, those aged 55-64 in Defined Contribution schemes have a median value of only £17,000, and for women £8,500[17]. Auto enrolment helps those currently aged between 20 and 35, but has less benefit for those aged 35 to 50 and is too little too late for the six million people aged 50 plus who have under-saved.[18]

Household lifetime saving and financial planning

4. What policies could support households in achieving appropriate levels of saving in cash and pensions? Are current policy interventions (e.g. ISAs) well targeted?

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[12] ONS

[13] TISA – Can Housing Wealth Save the Day?

[14] TISA – Our Financial Future

[15] English Housing Survey

[16] IFS

[17] TISA - Can Housing Wealth Save the Day?

[18] TISA – Can Housing Wealth Save the Day?

26. Whilst cash savings are an important 'rainy day' buffer, too large a proportion of household savings are held in cash as opposed to other investments offering better growth. Measures to encourage the public to invest money in bonds and equities will boost the economy through more productive use of capital, but requires greater education and guidance on the options available.

27. Policy solutions should include:-
    a) Greatly increased levels of financial education for all age groups;
    b) Increased access to financial guidance, currently the remit of the SFGB, whose proposed funding will not be of the scale needed for it to support the 42 million people unable to afford financial advice;
    c) Enabling the financial services sector to operate in support of the SFBG with free guidance that goes beyond the current limitation to neutral generic information;
    d) Adoption of financial rules of thumb to help consumers understand basic savings habits and outcomes (this work, currently with MAS, would benefit from significantly greater funding);
    e) Extending auto-enrolment to include auto-escalation, to increase savings levels from 8% to between 12% and 15% as recommended by the DWP;
    f) Undertaking a review of pension tax relief with a view to adopting a solution that can be easily understood by consumers, such as universal rate matching contributions, ideally at 33.3% which provides "Buy 2 get 1 free (from government)"
    g) Developing pension solutions for the self-employed and non-employed, who are currently left out of the auto-enrolment revolution and most vulnerable to under-provision in later life
    h) Simplifying the ISA regime.

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5. What actions can government take to improve levels of financial awareness and education, and what lessons can be learned in designing the successor to the Money Advice Service?

28. **Primary schools**. Research suggests children form their attitude to money between the ages of 7 and 11 years old. In 2016, TISA launched KickStart Money, funded by 20 financial services firms, delivering education on managing money in primary schools. We are working with the Money Advice Service (MAS) to evidence the benefits of this education and will share this with government over the next 3 years.

29. **Secondary schools**. Managing money is now part of the national curriculum However, there is no budget or programme for teacher training or for specialist resources in state schools. Managing money should be an essential part of the curriculum for all schools in the UK, and the committee should review whether the 'on paper' ambition is becoming an 'in classroom' reality or not.

30. Two key lessons to draw from MAS are:
    a) no public service will have the capacity to provide financial guidance to 42m people without the support of the financial services industry
    b) successful guidance can only be judged by the extent to which it causes people to act to save money. This action must be measured – requiring links between the SFGB and financial services.

6. How do high house prices and declining rates of property ownership among younger generations affect lifetime financial planning?

31. The average age of a first-time buyer has risen from 24 in 1970 to 30 in 2016[19]. The percentage of people aged 25-34 who were owner occupiers of a property slipped from around two thirds for those born between 1950 and 1970, to one third for those born in 1980 and later.[20]

7. What role can and should the state pension and triple lock have in supporting lifetime household finances?

32. The state pension is an essential underpinning of retirement income for much of the population, especially those in the lower income quartile. However, the lack of financial education results in consumers over-estimating the pension they will receive and under-estimating the saving required to meet adequate income in retirement.

33. Furthermore, the state pension system is unfunded and subject to demographic strain and intergenerational unfairness.

8. Are retiring households receiving adequate and appropriate financial advice following the implementation of pension freedoms?

34. PensionWise is a valuable resource for consumers but it does not provide a service that is immediately available at the point of decision. There are too many examples of individuals wanting to withdraw all their pension money, regardless of tax implications, and providers being prevented from counselling them to adopt more sensible approaches without it becoming fee-charged advice.

35. We advocate the idea of the Mid-Life 'MOT' with regards to pension savings as too often this is not given sufficient attention until it is too late to take effective action.

Household indebtedness and consumer credit and incomes

9. Is the overall level of UK household debt and consumer credit sustainable?

36. The extensive use of credit by consumers means that over their life, their consumption will be reduced by the cost of that credit. The cost of credit will vary according to the mechanism for borrowing and the borrower. Assuming an average of 10% means a household will consume 10% less goods over their lifetime than if they had made the purchases with cash.

37. Reliance on debt to finance daily living also results in the true cost of goods and services being significantly higher for those least able to afford to the cost of interest.

[19] TISA – Our Financial Future

[20] English Housing Survey

38. The most appropriate first step towards saving is often to reduce debt. TISA believes the two issues need to be tackled together – shifting people from the habit of debt-based consumption, to the discipline of saving up for things they want.

10. What is the scale of and trend in problematic debt and over-indebted households? To what extent is unmanageable debt being manifest in non-credit defaults (e.g. on utilities bills or council tax)?

Others are better placed than TISA to advise the Committee on this point.

11. Have household incomes become more variable as a result of more flexible labour markets and the "gig economy", and does this raise the need for new credit products?

Others are better placed than TISA to advise the Committee on this point, however the increase in labour market flexibility does exacerbate the current lack of adequate pension provision for the self-employed.

12. What are financial regulators doing to monitor the issues of problematic debt? Has the UK financial services market been effective in providing suitable credit products for low income households? What interventions can the Government make, including "breathing space" schemes?

39. TISA believes the broader problem with consumer debt is that access has been made very easy compared with access to savings products. Given the relative harm of debt products versus the benefits of savings products it is perverse that regulatory process weighs so heavily on the sale of savings plans, whilst credit can be obtained so easily.