

Measuring financial capability – identifying the building blocks

Understanding what drives or inhibits consumers' financial wellbeing and resilience

An in-depth analysis of the UK Financial Capability Survey



Foreword

Financial capability in the UK has remained stubbornly low with nearly half the working age population having savings of less than £100, one in six of the population over-indebted and one in five unable to read a bank statement.

It is for that reason that we launched the UK Financial Capability Strategy just over a year ago, designed to harness the collective efforts of financial services firms, the advice sector and public sector bodies to drive up the levels of capability in the UK.

But financial capability is a complex topic encompassing behaviour, attitudes, motivations, skills and knowledge across a range of areas: saving, spending, credit use, budgeting, planning and protection. It is essential that we understand these factors and how they inter-relate so that we can target and design the most effective interventions.

We believe that this is a major piece of work that significantly advances our knowledge and will help drive forward financial capability initiatives in the UK. We would like to thank the working group of Andrea Finney of Social Research and Statistics, Professor Elaine Kempson, Antony Elliott of the The Fairbanking Foundation and our own Insight and Evaluation team, in particular Nick Watkins, Helen Pitman and Chris Phillips.



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More information on the Financial Capability Survey, this analysis and all our research is available on the Money Advice Service website: moneyadvice.service.org.uk/en/corporate/research

More information on the UK Financial Capability Strategy and our tools for supporting the sector are available on the Financial Capability website: fincap.org.uk

Introduction

In 2015 the Money Advice Service ran the Adult Financial Capability Survey for the UK. This was a major piece of research involving over 3,500 interviews with a representative sample of the UK population, supplemented by additional interviews in the devolved nations and amongst younger consumers aged 18-24.

The questionnaire built on the findings from several earlier studies, as well as including new questions developed from qualitative work and extensively tested prior to use. The interviews were conducted online or face to face and lasted an average of 27 minutes. More detail on the design of the survey is available on our website moneyadviceservice.org.uk/en/corporate_categories/research

The survey generated a wealth of data about the financial capability of the UK adult population but we were keen to mine the data more deeply in order to ensure that our conceptual map of financial capability, and our choice and interpretation of the key measures, were fully grounded in the data. We also wanted to understand in much more detail the relationships between the various components of financial capability. Using a variety of statistical techniques we were able to refine our conceptual model, identify the key drivers or inhibitors of capability, and profile groups within the population according to their levels of wellbeing and resilience.

This piece of work has therefore enabled us to identify both the key building blocks of financial capability and the barriers to their implementation. We will be tracking these key measures in the UK population via subsequent surveys.

This document summarises the key findings from the analysis and the implications for interventions. A full technical report of this work is also available on our website.

The broad dimensions of financial capability

In order to make sense of the data, and help us interpret the output, we classified each of the survey variables into one of four categories. The input from Professor Elaine Kempson was particularly valuable in the development of this categorisation.

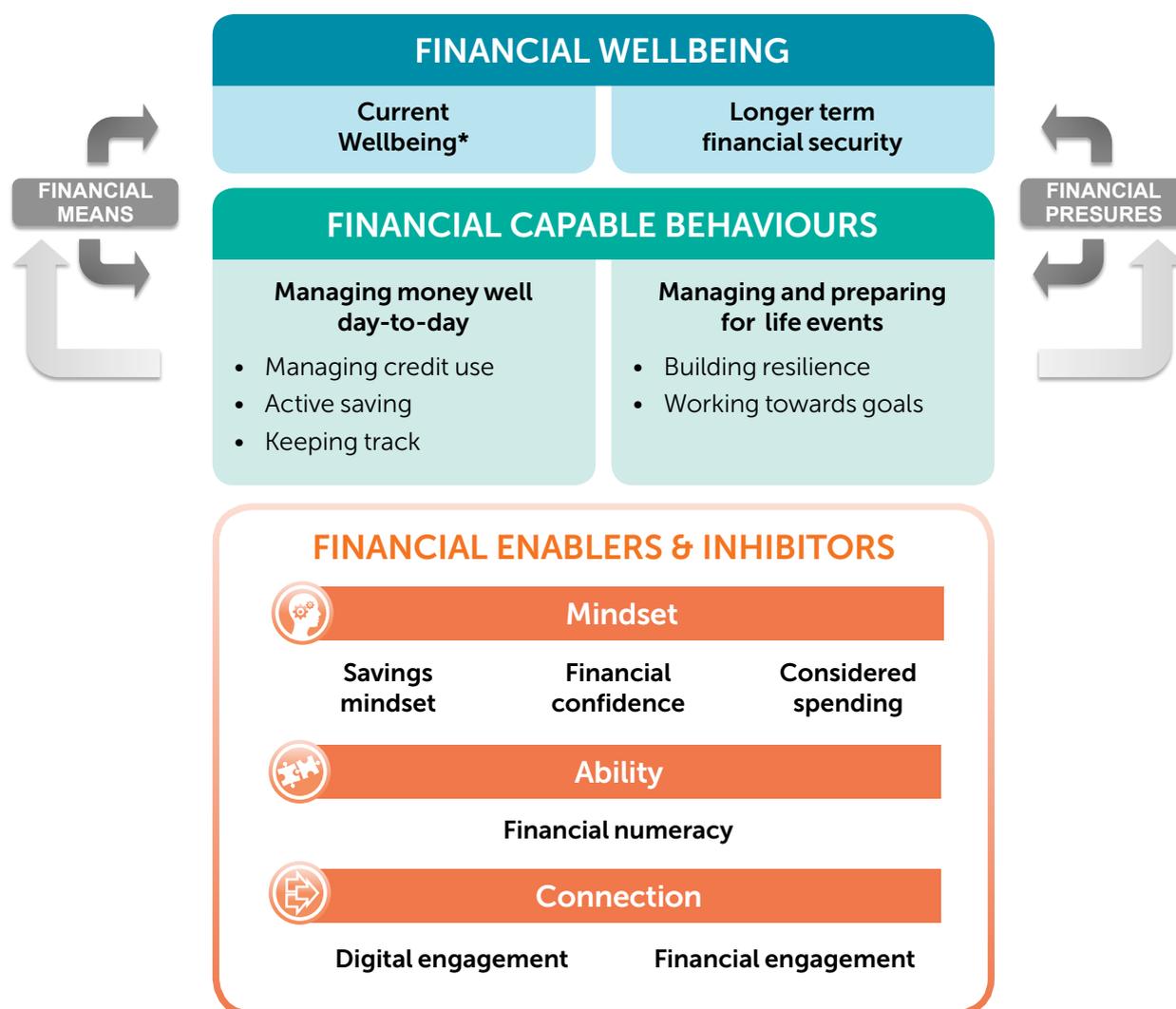
- **Financial wellbeing measures** – these are best defined as what we would like people to be able to achieve in their financial lives, either day to day or in the future. As such, wellbeing measures comprise dimensions such as satisfaction, being able to cope with household bills including unexpected ones, not being anxious, or having savings for the future.
- **Financially capable behaviours** – these are the behaviours that people exhibit or the actions they take, for example saving regularly, keeping track of their finances, working towards longer-term goals, or how they use credit. Many interventions will be focused on behaviours – to help consumers save more or keep a budget for example.
- **Financial enablers and inhibitors** – these are the things that make behaviours or financial wellbeing either easier or more difficult for people to achieve. They are therefore the levers that we need to pull, or the barriers that we need to overcome. They encompass attitudes and motivations, skills and knowledge as well as aspects of how easy or difficult it is for people to access the financial services system. Many interventions will focus on these variables – improving literacy or building digital confidence for example. Critically, we need to understand exactly how the various enablers and inhibitors influence behaviour and how this differs across the population.
- **Demographics and other characteristics** – critically these include the economic ‘means and pressures’ that make capable behaviours or financial wellbeing easier or more difficult to achieve. Income is critical but so too is the presence of dependent children and whether or not the individual has a partner. It is important to understand just how much influence these have when thinking about targets for interventions. In other words, the extent to which people can save, or how satisfied they are with their financial circumstances, will necessarily be impacted by their wages or benefits, and by the tax regime or cost of living.

There is an important time dimension to financial capability. We want people to be able to manage their money day to day and have a high level of current financial wellbeing. But we also want them to be able to prepare for and manage life events, which can be positive or negative, and develop longer-term financial security. Research consistently shows that planning for tomorrow is much more difficult than managing today.

The financial capability model

Before we look at the analysis in detail, an overview of our model of financial capability is shown below.

Within each category, or domain, there are a number of elements which have been identified by the data analysis as the most important and distinct. For example, managing money well day to day is made up of three components: managing credit use; active saving; and keeping track. These in turn are made up of a number of survey variables – for example, ‘managing credit use’ comprises questions on total value of unsecured borrowing, method of credit card repayment (where owned) and plan for paying down debts. A full listing of all the components and their constituent questions is provided in the technical report available on our website.



* Note that ‘Current wellbeing’ includes the Money Advice Service measures of over-indebtedness (debts as a heavy burden or recent experience of missing payments)

The next sections of this report identify which components have the greatest influence on current financial wellbeing or longer-term financial security.

The drivers of current financial wellbeing

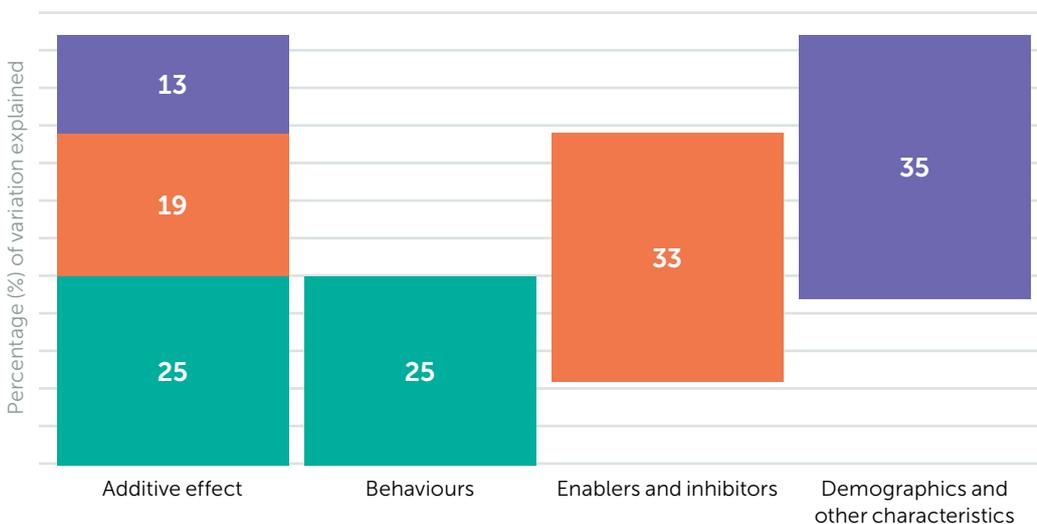
Ultimately, we want to see the current financial wellbeing of the UK improving. We would like more people to be satisfied with their financial circumstances, more keeping up with their bills and credit commitments or able to pay unexpected bills, and fewer feeling anxious about their finances.

In order to try and achieve this we need to understand where we can have the greatest effect – to identify the key building blocks and the main barriers.

At an aggregate level the chart below shows us that the 'demographic and other characteristics' have the single largest influence on current financial wellbeing – accounting for one-third (35%) of the variation in our measure. In other words, financial wellbeing is most definitely correlated with factors such as income, household composition, housing tenure or work status. As in all consumer research, there is necessarily some variation, in this case 43%, that we can't explain with the questions in the survey and compared to many studies this model is relatively successful.

Demographics, however, are outside the scope of any intervention. We cannot affect them and so we cannot use them to improve wellbeing. Instead, interventions must be directed at behaviours or enablers and inhibitors. The former account for 25% of the variation in wellbeing; the figure for the latter is 33%. However, there is overlap between these two such that if we 'fix' the behaviours, which in this case we have assumed we would do first, the 'additive effect' of enablers and inhibitors is reduced to 19%. In the case of demographics, the 'additive effect' is only 13% after the impact of the other types of variable. Therefore, and reassuringly, interventions focussing on behaviours and enablers and inhibitors can be successful in improving current wellbeing. Taken together, behaviours and enablers and inhibitors – which we can influence – explain over 40% of the observed variation in wellbeing.

The influence of different component types on current financial wellbeing

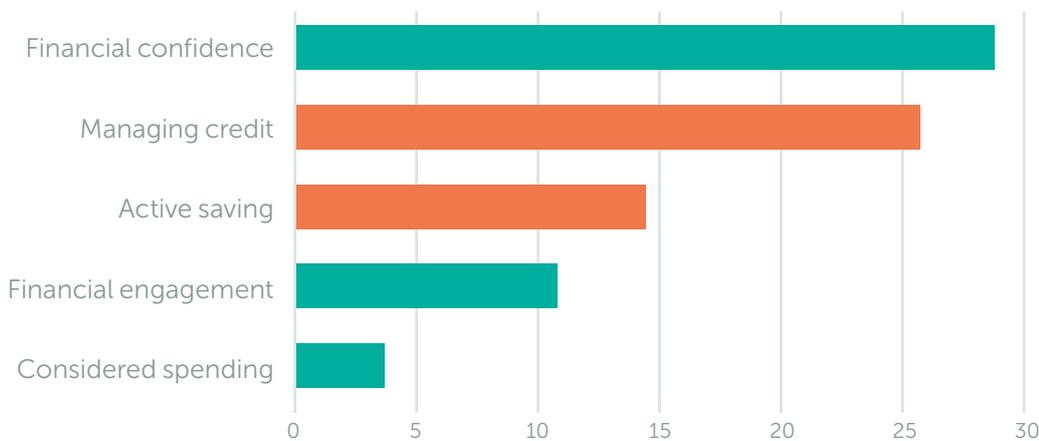


We can then look at the relative influence of individual components on current financial wellbeing. As can be seen from the chart below, **managing credit use** is the behaviour with the greatest impact on current financial wellbeing, followed by **active saving**. Whilst keeping track is an important component of managing money day-to-day there is less of a direct relationship with wellbeing. We believe that it is important that people keep track of their money and there is plenty of research evidence to show that it is a key step to managing money and being able to save more.

Turning to ‘enablers and inhibitors’ by far the most important dimension is **financial confidence** (comprising both confidence managing money day to day and the confidence to make financial decisions). The second most important is **financial engagement** (which includes measures of making time for one’s finances, not just living for today and believing that you can make a difference to your own financial situation). Both these dimensions have more impact on current financial wellbeing than the financial numeracy questions. This is not to say that numeracy is not important and other work that the Money Advice Service has done shows the linkage between numeracy and confidence, keeping track and setting goals. Taken together, this analysis suggests that it is an individual’s confidence in applying their basic numeracy skills that is important.

The other component that features in this analysis is considered spending, which is built from negative responses to the questions on whether people buy things on impulse or feel under pressure to spend like their friends.

The individual components with the greatest influence on current financial wellbeing



Note: Analysis based on behaviours and enablers and inhibitors only and shows the relative coefficients from the regression (x100).

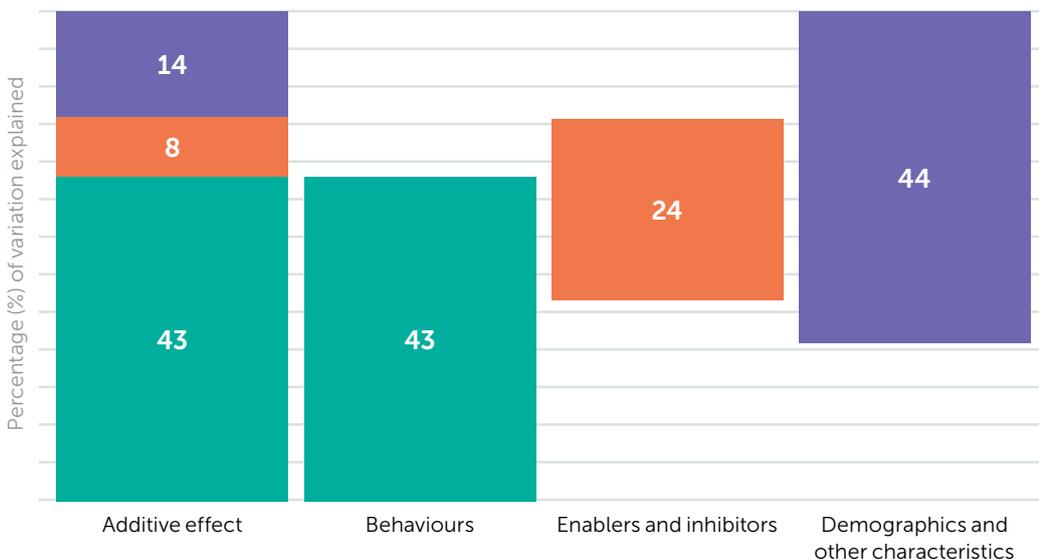
The drivers of longer-term financial security

Finding the best measures for the longer-term component of financial wellbeing was considerably more difficult than for the current dimension and is an area we will address further in future surveys.

For these purposes, longer-term financial security comprises the savings-to-income ratio; the number of protection products and longer-term savings products held; and the biggest unexpected bill that could be covered.

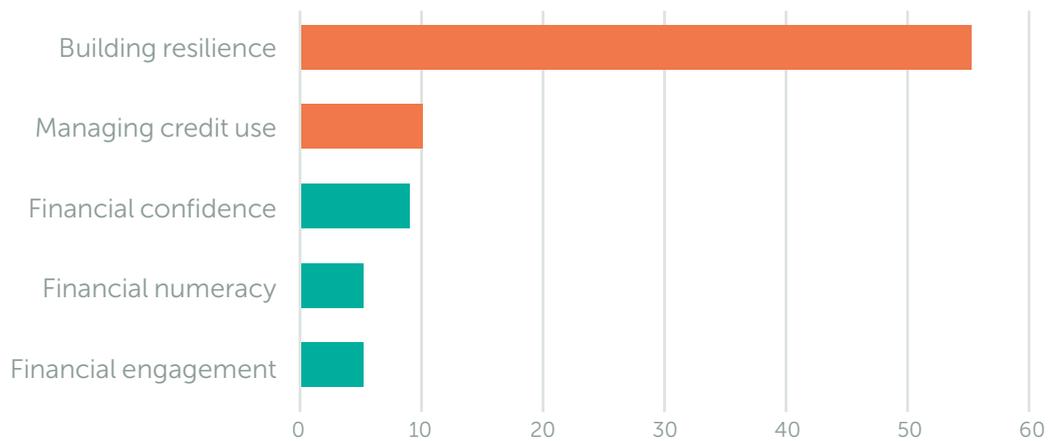
The chart below, which repeats the analysis in the previous section, shows quite clearly that whilst the ‘demographic and other characteristics’ again have the biggest influence on our wellbeing measure, in this case behaviours have a stronger relationship than previously, alone accounting for over 40% of the variation in longer-term financial security.

The influence of different component types on longer-term financial security



The chart overleaf shows the relative influence of the individual components on longer-term financial security and reveals ‘**building resilience**’ as by far the most important component. This encompasses both the total level of savings and the number and types of expenses for which people are saving. Given that savings is a key feature of longer-term financial security this is not surprising. However, it also shows that if we want people to have the benefit of financial security, to help them to prepare for and manage life events, then we need to focus on establishing savings behaviours.

The individual components with the greatest influence on longer-term financial security



Note: analysis based on behaviours and enablers and inhibitors only. The chart shows the relative coefficients from the regression (x100).

There is some relationship between managing money behaviours and longer-term financial security, with **managing credit** having the largest effect. Other research that we have conducted has shown how the servicing of historic debt can significantly impair people’s ability to save and to improve their future financial resilience. Given the importance of this component for both dimensions of wellbeing it clearly needs to be an area of focus.

Whilst the effect of enablers and inhibitors on longer-term financial security is comparatively small, it is worth noting that **financial confidence** is again the most important individual dimension. Also there is more of a relationship with financial numeracy than was the case with current financial wellbeing.

The attitudinal dimension of financial engagement also has some effect. The willingness to use the internet for banking and the time spent online, not shown in the chart, also has a very weak relationship.

Where to focus interventions

We have been able to measure survey respondents on all the dimensions from wellbeing measures to behaviours and enablers and inhibitors. These scores range from 0 to 10 and are applied on a consistent basis, such that zero is always the lowest possible score and ten the highest, regardless of the actual survey responses.

When we compare the current measures for current financial wellbeing with those for longer-term financial security, the analysis clearly shows that managing money today is easier to achieve than planning for tomorrow – a finding reflected in most other studies. Looking at the average for all adults the measurement is almost exactly twice as high:

- Average score for current financial wellbeing 7.5
- Average score for longer-term financial security 3.8

As has already been identified, demographics and other characteristics have a major influence on people’s wellbeing. The scores on the two wellbeing measures are closely related with the same demographic groups generally scoring higher – or lower – on both measures as shown below. The only slight exceptions are that people aged 75 and over have a lower score for future wellbeing than those aged 55–74; and social tenants have an equally low score for future wellbeing as their private-sector peers.

High and low Financial Wellbeing measures by demographics

Lower/lowest scoring group (on current)	Current	Future	Higher/highest scoring group (on current)	Current	Future
Unemployed	5.8	1.9	Retired	8.6	4.7
Private tenants	6.6	2.4	Own outright	8.6	5.1
Single parents	6.2	3.2	Couples with no children	8.0	4.4
Youngest (18 -24)	7.1	2.4	Oldest	8.8	4.2
Lowest income	7.2	3.0	Highest income	8.2	5.3
BME	6.9	2.6	White	7.6	3.9
Full-time self-employed	7.0	3.6	Full-time permanent	7.5	3.8
Women	7.4	3.6	Men	7.7	3.9

If we wish to design interventions to raise the current financial wellbeing of those with the lowest scores, we then need to look at how they perform on the key behaviours and enablers and inhibitors that we have identified. Specifically, these are managing credit, active saving, building resilience by accumulating savings and holding appropriate protection products, financial confidence and engaging with one’s finances. The last of these includes being willing to make the time, believing it is possible to make a difference and planning for tomorrow rather than just living for today.

Demographic group	Behaviours			Enablers		
	Managing credit	Active saving	Building resilience	Financial confidence	Financial engagement	Financial numeracy
Unemployed	7.7	1.5	0.8	5.9	5.4	5.4
Private tenants	7.1	2.8	1.7	6.6	5.8	6.3
Social tenants	7.7	2.0	1.1	7.1	5.3	4.9
Single parents	6.8	3.2	2.0	7.1	6.0	6.6
Youngest (18-24)	7.3	3.4	2.1	6.6	6.0	6.1
Lowest income (<£13,500)	7.7	2.4	1.5	7.0	5.6	5.5
BME	7.3	3.1	1.8	6.7	6.0	5.1
Full-time self-employed	7.3	3.3	2.2	7.0	6.3	7.2
Women	7.4	3.2	2.0	7.1	6.2	6.5
All adults	7.3	3.3	2.1	7.3	6.2	6.8

The table suggests that:

- The **unemployed** would benefit from support in almost every area other than using credit, although this in itself may be partly supply-side driven with the unemployed generally excluded from mainstream credit. Whilst survey data was collected on alternative sources of credit the overall incidence levels meant it did not feature in the analysis.
- **People living in rented accommodation** might benefit from interventions that encourage saving. Those in the private sector also lack confidence – possibly a feature of their younger age – whilst those in social housing need support or encouragement to engage with their finances. That being said it is also clear that social tenants are better than average at managing (mainstream) credit.
- As just mentioned the **18–24 year olds** lack confidence. Whilst their score for credit use is equal to the average they do less well on controlling their spending (not shown) and this fits with other research that we have conducted. As such, interventions targeted at spending and peer pressure may be beneficial.
- **Single parents** do relatively well on most measures other than credit use. Ensuring they can access affordable credit would seem to be a priority.
- Confidence would appear to be a particular issue for the **BME** population, although they tend to have slightly lower scores across the board. We must also recognise that there will be differences within this population but the base is insufficiently large to measure these variations.
- Gender differences are not large but **women** consistently score lower than men. Whilst they have a slightly more positive attitude towards savings they fare less well at building up a savings balance – correlated no doubt with income. There is a bigger difference between the sexes in terms of financial numeracy where women’s scores are lower; the same is also true of confidence, but the difference is less marked.

Conclusions

This analysis has highlighted a number of important issues around financial capability

- Interventions need to be targeted directly at aspects of financial behaviour and also at the enablers and inhibitors that facilitate or hinder that behaviour.
- Both consumer's wellbeing and financially capable behaviour have both a **current and longer-term** aspect. Consumers are considerably better at managing day-to-day than planning for the future – a consistent finding in our research.
- The three key dimensions of managing money well day-to-day have been identified by the research as
 - **managing credit**
 - active saving
 - keeping track of one's finances
- Preparing for and managing life events is best measured by:
 - **building resilience**
 - working towards goals
- **Managing credit** is the behaviour most highly correlated with financial wellbeing and second only to building resilience for the longer-term aspect of wellbeing. It is clear that helping consumers to manage their credit use – how they choose their credit instrument, how they repay and how they service historic debt – should be an area of focus for interventions. Managing credit is a particular issue for single parents.
- Financial enablers and inhibitors comprise attitudes and motivations, technical ability and engagement. Within these the 'mindset' variables of **financial confidence** and **financial engagement** are the most correlated with current financial wellbeing. **Financial numeracy** also features in the analysis of longer-term financial security.
- One of the key findings from this analysis is the importance of confidence generally and this is an area that we hope to explore further in subsequent research. It is a particular issue for the youngest consumers, who make up a significant proportion of private sector tenants, the unemployed and those from black and minority ethnic groups.
- Consumers' ability to save and build up their financial resilience is necessarily affected by their available income. We can see therefore that it is the unemployed, renters and those on a low income who fare less well on both these behaviours. However, there is plenty of evidence elsewhere that helping people to save even a modest amount has significant benefits, both emotional and practical. Resilience also includes the holding of appropriate protection products and this is an area that needs further exploration.
- A key conclusion therefore is that interventions targeting **active saving and through that building resilience** will contribute to improving consumers' current financial wellbeing and longer-term security respectively.
- This analysis has also highlighted a slight but consistent gender inequality with a possible need for interventions targeting at building financial numeracy and confidence amongst women.

All our research can be found on our website:
moneyadviceservice.org.uk/en/corporate/research



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November 2016

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