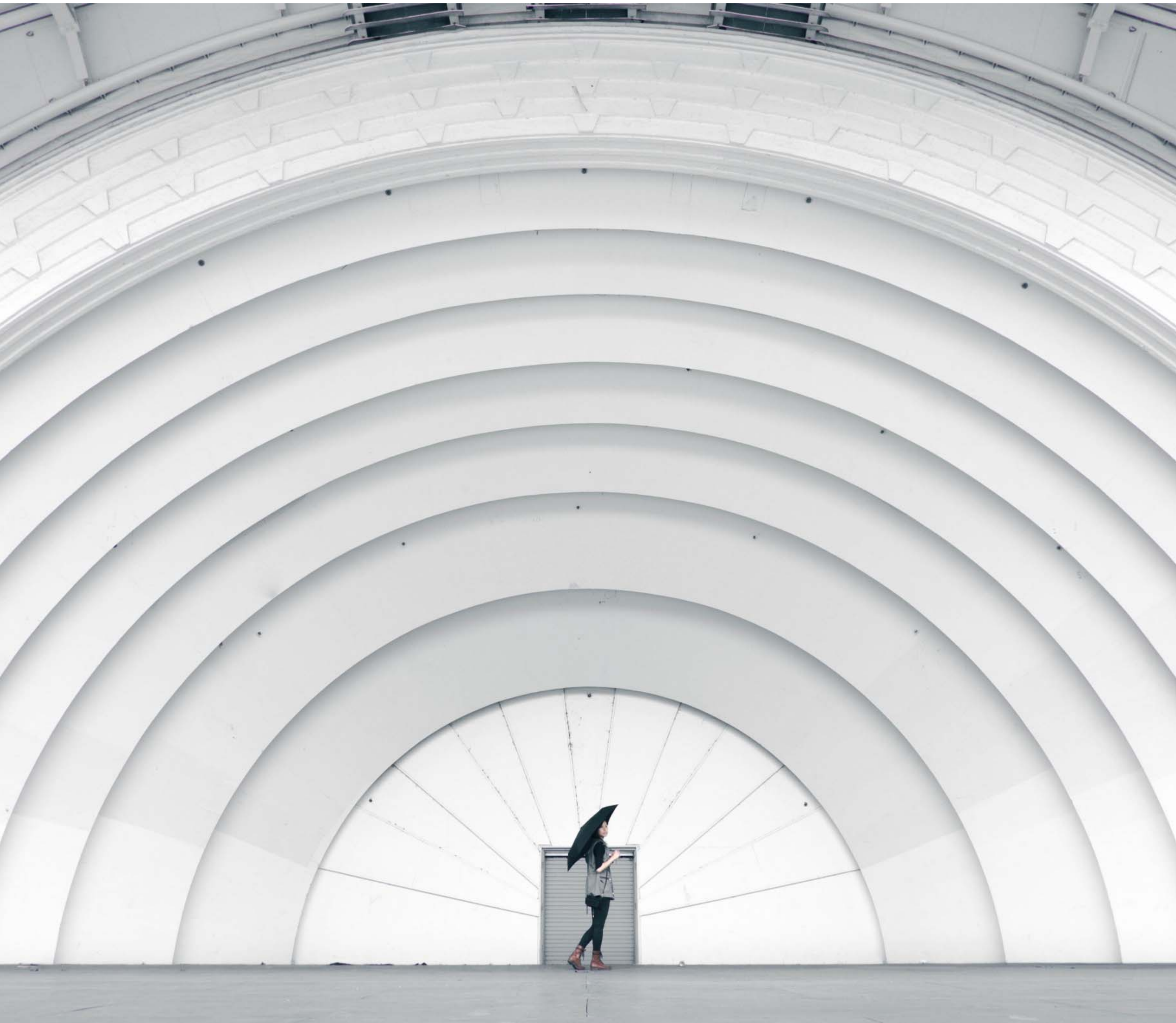
NO CUSTOMER LEFT BEHIND

REACHING 2.5 MILLION NEW CUSTOMERS THROUGH FINANCIAL INCLUSION IN THE UK



NO CUSTOMER LEFT BEHIND: REACHING 2.5 MILLION NEW CUSTOMERS THROUGH FINANCIAL INCLUSION IN THE UK

HUMANISING BANKING THROUGH MORE APPROPRIATE, MORE EFFECTIVE AND MORE INCLUSIVE CONSUMER ENGAGEMENT AND DIGITAL APPROACHES.

What is Financial Inclusion?

"Financial Inclusion is about ensuring that every adult in the United Kingdom is connected to the financial 'mains', just as he or she is connected to mains electricity or mains water." Financial Inclusion Commission, 2015

On 24 May, 2016, the Financial Conduct Authority (FCA) launched Occasional Paper 17 on Access to Finance. The paper clearly signals that Financial Inclusion must now take its place on the senior management agenda. And it needs to be considered in the context of consumer vulnerability, an ageing population and the creation of a fairer market for financial products and services. The key points from the launch event sum up the issues that can and must be addressed:

- **Exclusion is not demographically restricted**. Any of us can potentially be financially excluded at some point in our lives. (For more detail, see Appendix 1 – The demographics of financial exclusion.)
- **Financial products should fit the consumer and not the other way around**. Consumers need to have access to products that are right for them and that offer useful features and easy-to-understand functionality.
- **The poorest should not pay the most for financial access**. There is much work to be done to eliminate the 'poverty premium' that sees the least advantaged in society paying the most for basic financial services.
- **Technology is not always a door opener**. Technology is both an enabler of and a barrier to Financial Inclusion. Its rapid pace of development and the changes it triggers can exclude some consumers from mainstream financial services.
- **Financial Inclusion is a social fundamental**. Financial Inclusion can provide the first step towards meaningful employment, decent housing and basic self-respect. In these aspects, nobody should be left behind.
- **People need financial education**. We need to boost financial education, particularly for younger people.
- **People need IT skills**. We need to build basic IT skills, particularly for older people.
- **Financial knowledge is a skill for life**. We need to recognise that knowledge of how to use basic financial products – bank accounts, insurance, responsible credit – is a fundamental life skill and should be taught effectively to all.

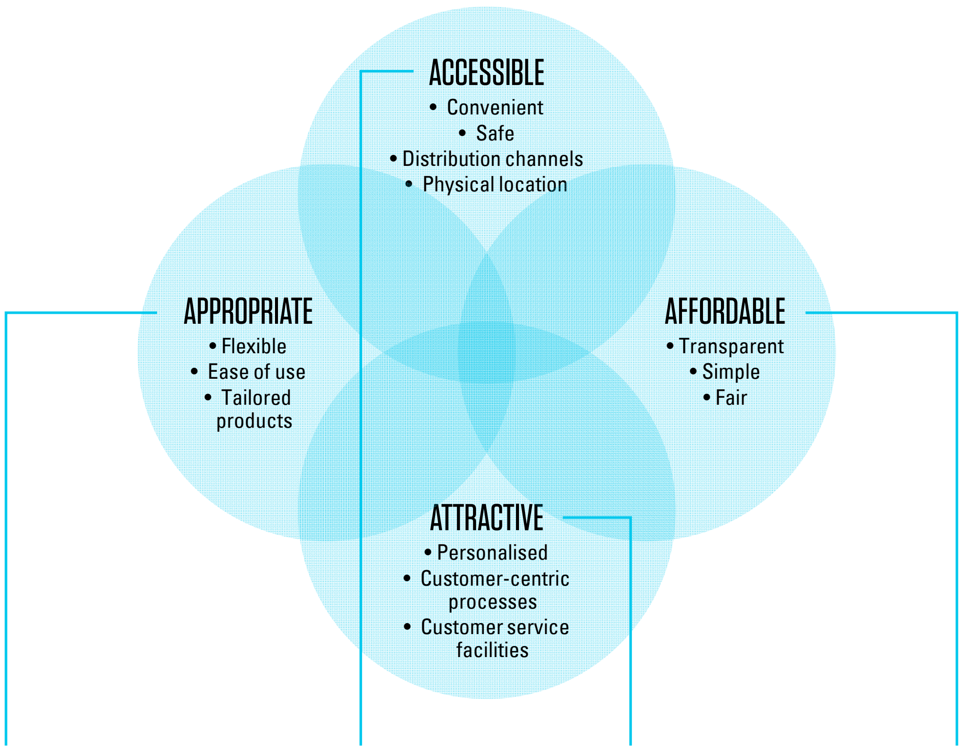
The reality today is that banks don't always treat all retail customers as individuals, with individual needs. Regulations introduced with the best of intentions, such as anti-money laundering rules or mandatory creditworthiness checks, have created a land of unintended consequences. They often inhibit providers from offering flexibility and Financial Inclusion where it is most pressingly required. The financial industry needs to re-set its thinking and its practices around Financial Inclusion. In this paper, we briefly examine the current market context. Then we address the practical steps that C-suite management needs to take in order to make Financial Inclusion a delivered reality.

Technology is both an enabler of and a barrier to Financial Inclusion.

Financial Inclusion – an opportunity for everybody

Financial Inclusion is good for the financial industry too. The FCA has identified that 1.5 million people in the UK have no bank account. The Financial Inclusion Commission (FIC) estimates that **£5bn worth** of demand for responsible lending is going unmet every year. This is a major opportunity to refresh and grow the customer base and to develop sustainable demand for a new generation of products and services. In addition, the specific inclusion opportunity does not take into account the potential value of increased demand from existing customers, if they too were better engaged.

So what is required for truly effective access to finance? At Capco, we define Financial Inclusion as **appropriate, affordable, accessible and attractive** financial products and services, made available to the entire population by creating a differentiated, engaging and customer-led experience through a robust framework (see figure 1).



EXAMPLES	APPROPRIATE	ACCESSIBLE	ATTRACTIVE	AFFORDABLE
	• Basic bank accounts with no minimum deposits or credit facilities • SME lending • Responsible selling • Responsible credit	• Branch access in rural areas • Voice activated functionality • Selfie identification and payments • Supervision and advice for those that need it	• Personalised offers and rewards • Loyalty programmes • Easy to use budgeting tools	• Transparent and simple interest rates • Home contents insurance for social housing • Affordable credit facilities

FIGURE 1. FINANCIAL INCLUSION PRINCIPLES – THE 4 A'S

What are the obstacles to satisfying the key criteria of Financial Inclusion?

There are three substantial obstacles to achieving the standards of Financial Inclusion advocated by the FCA. The first is **Financial Crime and Fraud Prevention**. Many potential customers are unable to meet the exacting requirements for identification and proof of address. Secondly, there is the issue of **Automated Systems**. The problem of exclusion through automation is best summed up in the now iconic "computer says 'no.'" Thirdly, we have the downside of **Digital Transformation**. Many people are still unable or unwilling to engage with online banking or other products. (For more detail, see Appendix 2 – Key Financial Inclusion obstacles: Scale and associated risk factors.)

What can the financial services industry do?

The FCA's Occasional Paper 17 encourages all stakeholders to create a retail market where fairness to consumers, clarity of information and consistent delivery against initial expectations are the cornerstones of normal practice. (For more detail of the relevant Paper highlights, see Appendix 3 – Best practice in Financial Inclusion creation: Issues and imperatives). In this 'new normal' market, the technology phenomenon of the so-called 'digital revolution' deserves special mention.

The digital revolution is in fact a great Financial Inclusion opportunity for those who can practically engage with it. Thoughtfully designed and trustworthy mobile and online platforms can very effectively connect previously excluded customers with responsible, fair and attractive products. The greater the level of digital inclusion, the better the means by which all people can make informed choices and best meet their financial product needs. This is because digital technologies provide improved access to more of the information that allows people to choose and manage the products they use more successfully.

We can go further: digital interfaces that are appropriate, attractive and accessible have **exceptional** potential for reducing financial exclusion. However, research shows that customers do continue to prefer combining purely digital, automated channels with human interaction. The personal touch is far from dead. And far from being the 'enemy' of human interaction, well-configured digital technologies can enable more effective human-based customer relationships. One example of this is facilitating fellow human being contact via webchat or video calls. Text-based human interaction is also perceived by some as less intimidating than face to face or telephone channels. As digital skills improve throughout the population, there will be more and more opportunity to engage the financially excluded through digitally delivered services.

This positive future, driven both by digital and many other developments, should not be viewed merely as desirable in theory. There is much to be gained from the effective pursuit of Financial Inclusion, not least commercially.

What now are the key considerations, including the business drivers? And how, from the perspective of management, up to and including the CCO, CRO, CXO and CMO, can banks most effectively address the key strategic directions, service style implications and delivery technology demands of Financial Inclusion?

> **Thoughtfully designed and trustworthy mobile and online platforms can very effectively connect previously excluded customers with responsible, fair and attractive products.**

Across the C-suite, what are the key issues to recognise?

REGULATION & COMPLIANCE: CCO (CHIEF COMPLIANCE OFFICER)

Financial Inclusion represents a complex compliance challenge. Financial services providers will be expected to follow the new FCA guidance while still adhering to existing anti-money laundering and cross-subsidy requirements. The role of the CCO will be to navigate a path between these potentially conflicting regulations.

Key business drivers

- Prevention of new mandatory pricing or payments conditions being imposed as a result of new regulations or the ongoing cost of legacy remediation.
- Imperative to ensure that the organisation is compliant and future-proof on a continuous basis.

CCO checklist

- Do your policy and procedures align with the FCA expectations and good practice around Financial Inclusion and financially vulnerable customers?
- How can you onboard higher risk customers, without undermining existing AML (anti-money laundering) or ABC (activity based costing) management systems?
- Can you identify people at risk of exclusion and give them the individual attention they need?
- How does your organisation gather, understand and respond to individual needs?
- How do you respond to the challenges created by the fact that one approach does not fit all?
- How does your organisation manage complaints from excluded customers?
- What safeguards does your organisation have against mis-selling or up-selling to vulnerable customers?
- How do you ensure that customers are not offered products that they do not understand?
- What makes a person within your organisation qualified to decide matters of vulnerability?
- Does your staff have sufficient training and awareness to identify and meet individual needs?
- How do you balance an individual judgement-led approach with a consistent basis for assessment?
- Are your product terms and conditions fair and unambiguous? Do they describe features, benefits and risks in an understandable way to all intended audiences?
- How do you ensure that your Financial Inclusion initiatives are compliant with competition and cross-subsidy regulations and guidelines?

RISK: CRO (CHIEF RISK OFFICER)

Financial Inclusion will present an important regulatory, conduct and operational risk challenge for the CRO office. Given the emotive nature of the subject, it also poses a potential reputation issue.

Key business drivers

- Risk of ongoing costs of litigation and of remediation cases for the unfair treatment of customers.
- Risk of reputational damage resulting in substantial business losses.
- Challenges of embedding Financial Inclusion into the risk framework of the organisation, including policies, procedures and practices.
- Possible further regulatory scrutiny through supervision and the chance of more formal regulatory sanction, through a (potentially very costly) s166 procedure.
- Need to monitor ongoing organisational performance in the area of Financial Inclusion.

CRO checklist

- What level of Management Information - MI - is available to the Board to allow effective Financial Inclusion oversight by senior management?
- Does your organisation implement flexible, pragmatic and mature risk measures that allow the effective application of judgement? (For example, when making decisions around credit sanctioning and loan covenants.)
- Do your profitability and risk techniques ensure that consumers will not effectively be priced out of the market, or denied access to financial services and products?
- How robustly constructed is your current risk framework for detecting and preventing financial exclusion?
- Have you considered partnering with third parties/fintechs to provide alternative methods of credit decision-making or delinquency management?
- Do you have supporting processes in place for customers experiencing changes in their circumstances, to aid them in rebuilding their credit worthiness?

CUSTOMER EXPERIENCE: CHIEF OF CUSTOMER EXPERIENCE (CXO)

Previous negative experience of customer service in the retail financial services industry is one of the most common reasons given by the financially excluded for not engaging with legitimate, fair and mainstream financial products. Potential customers who feel unable to access appropriate products will very likely be pushed towards irresponsible, anti-social, exploitative and even illegal providers.

Key business drivers

- Opportunity to enhance customer experience through financial innovation and the use of new technology.
- Opportunity to compete with emerging fintechs - providing more personalised and tailored experiences to those target markets that traditional financial institutions have been unable to address.

CXO checklist

- Do you clearly understand each customer's current degree of financial exclusion?
- Are you able to tailor individual customer journeys, based on that understanding?
- How do your frontline staff capture specialised service delivery needs in branch or over the telephone?
- How does your online offer capture specialised needs?
- Are your staff trained to identify key financial vulnerability triggers and then respond appropriately?
- Do you make appropriate complaints processes accessible to all profiles of vulnerable customer?
- Do you have a clear idea of any new delivery channels needed for your products and services, especially in areas of restricted access to financial facilities?
- How can you help your customers improve financial management skills, thereby helping existing and potential customers achieve long-term financial viability?
- Are you considering measures to improve physical access as part of your customer experience?

MARKETING: CHIEF MARKETING OFFICER (CMO)

The release of the FCA paper, as well as other related government, charity and business initiatives, indicate that the topic of Financial Inclusion is gaining high profile momentum. Financial institutions that incorporate inclusive finance into their brand purpose, and successfully promote FI initiatives in their markets, will enjoy considerable advantages when it comes to positive perception of their brand.

Key business drivers

- There should be a vision – held and supported at C-suite level - to rebuild trust and respect amongst new and existing customers, by providing consistent and affordable financial services through every stage of their lives.

CMO checklist

- How do you communicate your offer to the vulnerable and excluded who need your support most?
- Do you have safeguards to prevent pressure on vulnerable customers to choose inappropriate products?
- Do you have a clearly defined Financial Inclusion marketing strategy?
- Do you make a clear distinction between promotional material and essential account-related information?
- Is your marketing communication on pricing clear and simple? Does it comply with CMA (Competition and Markets Authority) best practice?
- Do you tailor offers and recommendations to fit the needs of financially excluded customers?
- Do you make all new product and service offerings clear to all profiles of customer?
- How are you positively different from your competitors when it comes to Financial Inclusion?
- Are your positive differences clear to your staff and customers?

Why and how – practically - should senior executives be addressing Financial Inclusion?

Financial Inclusion is emphatically not limited to ticking the box of Corporate Social Responsibility and satisfying the regulators. It is important for banks - and all financial institutions - to recognise the challenges and the opportunities. They must do this across all areas of the business, from regulation and compliance, through risk and marketing, to customer experience.

Nor should financial institutions only be looking at how they can change their primary products and services at the point of access. They should also consider preventative measures to boost inclusion, along with driving effectiveness at managing delinquency. In figure 2 we offer a high level Financial Inclusion Management Framework as a practical route to identifying and managing key initiatives effectively.

Conclusion

Senior executives across the business, from regulation and compliance to customer experience and marketing, should become aware of the issues identified by the checklists in this paper. They must then address these issues, in the context of the guidance from the regulator, to ensure their products and services are not only accessible but affordable, attractive and appropriate to the entire population.

Those who do take action will be better able to maintain and grow market share. They will achieve this by delivering customer-led experiences that - far from being 'one size fits all' – are personally tailored to the needs of ALL customers, including the financially vulnerable and those who are currently financially excluded.

It is ethically desirable, operationally feasible and, not least, commercially rewarding to achieve a retail financial services environment where no customer and no potential customer is left behind (and no sustainable opportunity for revenue and market share growth is left unrealised). The time to act is now.

BANK'S FI INITIATIVES	EXAMPLES
PRIMARY How could you adapt your primary products and services to fit individual needs of customers?	• flexible credit • no minimum deposits • branch design
PREVENTATIVE What processes and tools can you implement to prevent exclusion?	• financial education • budgeting and saving tools
DELINQUENCY How can you better support customers experiencing financial difficulties?	• managing repayment deadlines • resetting credit instalments

FIGURE 2. FINANCIAL INCLUSION MANAGEMENT FRAMEWORK

Appendix 1 – The demographics of financial exclusion

Financial exclusion is a relative rather than an absolute concept. Each and every one of us will at some point experience degrees of exclusion across different products or channels, according to our life circumstances. Exclusion is certainly not limited to vulnerable customers. There are many indicators however that may suggest specifically increased risk of financial exclusion. These include, but are not limited to, the following profiles of people:

- Social housing tenants
- People with poor maths and basic literacy skills
- People not in employment, education or training
- Current and former military personnel
- Anyone who has experienced a relationship break-up
- Those with mental health problems
- People living in isolated or disadvantaged areas
- The disabled
- Migrants
- Homeless people
- The elderly
- Post office card account holders
- Carers
- People with low IT skills
- Those in sheltered, temporary or emergency accommodation
- People in care or having recently been in care
- Lone parents
- Ex-offenders and families of prisoners
- Those with unconventional or poor credit histories
- Prisoners
- Ethnic minorities
- Asylum seekers and refugees
- The under-30s
- People on low income
- Those who have a first language other than English
- Students

THE UK PERSPECTIVE – WHAT ARE THE FINANCIAL EXCLUSION NUMBERS?

- **1.5 million** people in the UK do not have a bank account.
- Almost **8.8 million** people are over-indebted, often as a consequence of being offered inappropriate products, or of being excluded from fair and responsible credit.
- **7.8 million** people are unable to access mainstream credit.
- **3 million** households in social housing lack basic contents insurance.
- The Department of Work and Pensions currently pays an average of **£50 per person per year in transaction costs alone** delivering benefits to the **2.5 million** benefit recipients who have no bank account.
- People on benefits borrow an estimated **£330 million** a year on home credit, paying **£140 million in interest** due to inflated and irresponsible home credit interest rates. Many people do not understand how the loan and associated repayments work when they take on the credit agreement.

Appendix 2 – Key Financial Inclusion obstacles: scale and associated risk factors

FINANCIAL CRIME AND FRAUD PREVENTION

Regulations associated with anti-money laundering, anti-terrorism, anti-tax evasion and fraud prevention increase the “Know your Customer” imperative acting on all financial institutions. Many potential customers are unable to meet the exacting requirements for identification and proof of address. Even basic bank accounts, specifically designed for the excluded, still require a check with a credit-referencing agency. This is for the sole purpose of identification but the thought of a credit check deters many vulnerable people. Again, this is not a marginal issue affecting a limited number. As the figures below make clear, significant numbers of the UK population risk financial exclusion through ‘identity crisis’.

Identity-related financial exclusion risk factors

- 9.5 million UK residents have no passport.
- 25% have no driving licence.
- 154,000 regular members of the armed forces (who are relatively well paid) frequently move between temporary addresses; BFPO (British Forces Post Office) overseas addresses in particular may not be recognised by financial institutions.
- 112,000 people apply for homelessness assistance each year.
- 70,000 households are in temporary or emergency accommodation.

AUTOMATED SYSTEMS

The problem of exclusion through automation is best summed up in the now iconic "computer says 'no'". Automated processes within customer relationship management, creditworthiness checks and pricing have led to a tendency to categorise potential customers in an over-simplified way. Being placed in a category perceived as 'risky' can mean that a customer is by default not accepted, or is faced with extortionate charges. This can happen regardless of their other circumstances, circumstances that ironically may make them very attractive to a financial services provider.

There arguably needs to be a more judgement-led and less automation-dictated approach to specific personal circumstances. At base here, there is a broader social policy aspect: holding a bank account often becomes a key component in enabling wider social access. Not least, there is also a regulatory dimension. Automated practices (unmonitored) put the provider at risk of contravening the Equality Act, 2010. They potentially inhibit providers' ability to identify customer vulnerability and further dissuade vulnerable customers, who have more complex needs, from asking for greater support.

As before, it must be stressed that this form of financial exclusion (or potential exclusion) is not restricted to the margins of society. Very large numbers of people encounter 'automated exclusion'.

Automated systems-related financial exclusion risk factors

- 2.5 million people are living with cancer or the aftermath of cancer. These people may be treated as a single, homogenised category when being considered for insurance or other products. (This happens despite the vast variation in profiles of risk, debility and health outlook associated with the disease).
- 3 million people have been turned down for insurance or charged an inflated premium due to disability, which in many cases has no relevance to the insurance policy itself.
- 10.5 million people in the UK have a criminal record of some kind. This may automatically preclude them from some financial products, regardless of the circumstances.
- 60% of mortgage providers impose an age limit to mortgage provision, again regardless of individual circumstances.

DIGITAL TRANSFORMATION

Many people are unable or unwilling to engage with online banking or other products. This can present a major obstacle in accessing the cheapest and most effective financial and non-financial products, which are to be found and chosen with increasing ease online. Lack of consumer interaction with online channels can also make administration of products more difficult, especially as banking and insurance branches and offices are becoming fewer.

A significant part of the challenge with digital transformation lies with the infrastructure enabling access to the digital world. UK mobile and broadband coverage is still far from having a uniform standard and can be prohibitively expensive for some. Those in rural areas are much more likely to be disadvantaged than those in cities.

Digital transformation-related financial exclusion risk factors

- 3.8 million UK households have no internet access.
- 13 million UK residents lack basic digital skills. This is more prevalent among older people.
- The rise in online banking is fuelling the closure of many bank branches. By 2020, one in four UK bank branches is likely to close without replacement.

Appendix 3 – Best practice in Financial Inclusion creation: issues and imperatives

The FCA's Occasional Paper 17 on Access to Finance provides clear direction on the values and practices that all financial institutions should now be embracing in order to drive Financial Inclusion. A satisfactory market context will be achieved when:

- Consumers can be confident they are dealing with firms where the fair treatment of customers is central to the corporate culture.
- Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.

- Consumers are provided with clear information and are kept appropriately informed before, during and after the sale.
- Where consumers receive advice, the advice is suitable and takes account of their circumstances.
- Consumers are provided with products that perform as firms have led them to expect, and the associated service is of an acceptable standard and also as they have been led to expect.
- Consumers do not face unreasonable post-sale barriers imposed by firms to inhibit change of product, switch of provider, submitting a claim or making a complaint.

Given the very wide range of financial exclusion issues, banks and other financial institutions now need to actively consider broadening their inclusion initiatives beyond vulnerable customers. They must examine how they can adjust their current business model to provide appropriate, affordable, accessible and attractive financial products and services to all. This obligation translates into the responsibility to identify each customer's current degree of financial exclusion, then to respond effectively through the right channels and at the right time.

Any assessment process must not be dehumanising. Customers need at all times, and in all situations, to be seen as individuals. Each has specific, personal needs. Badly administered, standardised operational processes and procedures can result in failure to address specific needs, as customers are inappropriately batched together. Nominated products must be right for the customer and their circumstances. The responsibility is considerable. Bad experiences can discourage participation in the mainstream financial system for life. So how can financial institutions work to get it right with the processes of inclusion?

Where appropriate banking products such as basic bank accounts already exist, banks need to engage with communities at risk of financial exclusion to build trust and encourage the use of beneficial products. Basic financial education and responsible marketing are an essential part of the journey to Financial Inclusion. Simple-to-operate financial products must be shown to be within the grasp of all sectors of the community and of benefit to all. Potential customers must be given the guidance they require to apply for and operate accounts for day-to-day requirements and savings provision.

A prevalent issue in the UK is the lack of a savings habit across all groups of the population. Only 41% of UK households are saving money for the future. This is less than almost every other country in the EU. Lack of savings has a direct impact on a person's ability to access credit, hence the significant recent growth in payday lenders (who have seen their loan books grow from £330m in 2006 to £3.7billion in 2012). Mainstream financial services providers could create a viable alternative, by identifying less aggressive and more sustainable ways to offer fair credit. The societal and commercial benefits are linked: by offering more attractive savings rates and appropriate budgeting tools, institutions have the opportunity to increase their deposit levels.

There is often a basic mismatch between people's needs and the products available to them. For instance, the high cost of contents insurance in unsafe areas makes cover unaffordable. One corollary is that 50% of the poorest households lack contents insurance, compared with just one fifth of households on average incomes. To compound the issue, households with no contents insurance are over three times more likely to be burgled compared with those with insurance.

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T1620-0616-01-EU

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