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WHITE PAPER

Can FinTechs solve Financial Exclusion?

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Lack of access to mainstream banking and financial services, both appropriate and affordable to an individual's needs still remains a key social issue.

Through technological and product innovation, the FinTech community is increasingly cited as offering potential solutions to solving financial exclusion. However, FinTech that is specifically targeted at financially excluded customers remains at the early stages of development while 1.5 million people in the UK continue to be unbanked.[1] Many more are reliant on "sub-(optimal) prime" financial products for day-to-day living needs; the FCA's Financial Lives Survey 2017 noted that "at least 4.5 million adults say they have been declined a financial product in last two years".[2]

Financial exclusion can affect people across a wide range of demographics and social groups including the unemployed, low paid, the elderly, young people, people with disability or poor physical and mental health, and those in poverty. This paper focuses on how FinTech could address financial exclusion where all such groups are represented by applying a set of criteria focused on the individual in the wider social context.

Why does Financial Exclusion matter?

People who are locked out of "mainstream" banking are penalised by having to incur a "poverty premium" for everyday services and products because, for example, they cannot access (cheaper) online pricing. This in turn may lead to over-indebtedness. The FCA's Financial Lives Survey reported 3.1 million UK adults have one or more high cost loans and 4.1 million are "in difficulty" in paying domestic bills or credit commitments.[3] Of increasing concern is the wider negative health impact that financial exclusion perpetuates through an individual's persistent financial "un"wellbeing. There is a clear link (and business case) between what FinTechs can seek to solve in financial exclusion which in turn delivers significant effects in improving health and wellbeing.

1 *Rowlingson, K. & McKay, S. (2017). Financial Inclusion Annual Monitoring Report 2017. University of Birmingham. [online]*
2 *Financial Conduct Authority (2017). Understanding the financial lives of UK adults. [online]*
3 *Ibid.*

Is Policy and Regulation making a difference?

Policy, regulatory and legislative reforms currently seeking to address financial exclusion comprise a variety of approaches, including the FCA's focus on high-cost credit products and in understanding consumer behaviours to inform regulatory interventions. Other initiatives include consideration of a duty of care for the provision of financial products, a possible effect of which might be to align the banking sector more closely to regulated utilities in ensuring universal access to financial products. Open Banking and GDPR are further avenues to drive product innovation through greater access, transfer and control of data by consumers. However, not all of these initiatives may ultimately assist people who are digitally or financially excluded.

There also needs to be a constant balance between seeking to facilitate safer, affordable products suited to individuals in their context and the necessity for financial providers to operate secure markets by applying uniform risk criteria, a key outcome of which may be the continued exacerbation of financial exclusion of the individual.

Is Policy and Regulation making a difference?

The FinTech market is well positioned to deliver alternatives to the incumbent landscape. By utilising newer technologies and digital innovation, it can capture comprehensive customer data (and contextualised experience) as to product utilisation across different exclusion situations in relevant social and environmental contexts. Armed with such data, it is arguable that FinTechs can offer a far more holistic and measured approach to assessing customer risk than currently exists. Through lower operational costs delivered through technology - and the ability to "test and see" product approaches – FinTech has a market opportunity to properly serve this underserved population by being responsive and tailoring products to their needs. But how can FinTech best optimise such a pivotal opportunity?

Optimising your product development approach to address financial exclusion customer needs

1 Understanding a customer's lived experience of financial exclusion

The design and innovation of retail financial products requires a bottom up perspective and insight to connect to a customer's needs and wants that reflect their life reality. The "one size fits all" approach does not work because individual circumstances vary significantly in community and across social contexts. Evidenced based research can inform a human centred design (HCD) approach to product development that utilises qualitative and quantitative research to specifically understand the needs and wants of the individual and how products can be designed to be responsive. Through a process of "listen, learn and act" the FinTech sector has considerable advantage in being able to implement, amend and update products and services in a swift, responsive and dynamic process. The FinTech sector can look to the health sector for HCD innovation and prototyping.

2 Understanding the social, cultural and community context

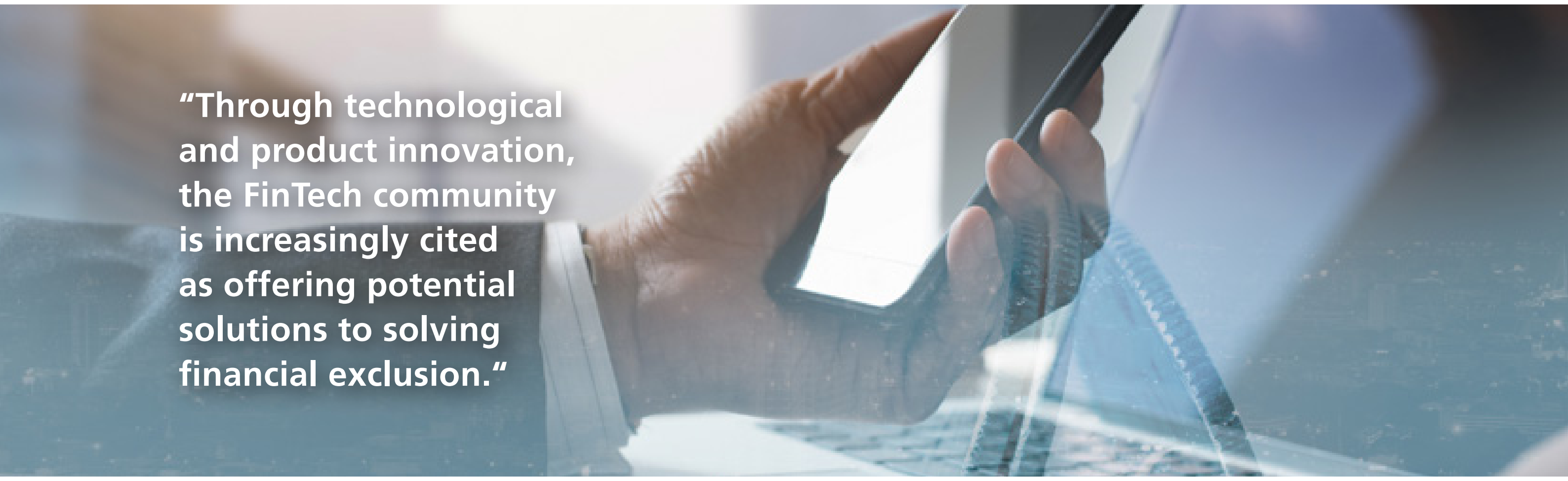
Financial products and services vary significantly in their usage depending on the needs of individuals in their social, cultural or community context. Within communities of poverty or social isolation, the ability to physically interact and engage at frequent touch points with a provider is key in establishing a strong (and mutual) trust relationship, such as is evident in the Credit Union and Responsible Lending sectors. The FinTech sector could utilise such an approach by incorporating habitual interaction points (e.g. through field agents, and mobile and PC applications) that are designed to be responsive to customer behaviours in their specific settings. Physical interaction with a provider will remain a priority to achieving an understanding and empathy toward cultural context which, over time, enables a more sustainable perspective of how products are utilised in communities and importantly, what matters most.

3 Nudges and Behavioural Economics

Nudge theory and a growing systematic approach to utilising nudges to encourage "positive behaviours" in financial services, such as a regular savings or budgeting habit, is a key part of a FinTech armoury in alleviating financial exclusion. It is important that a consumer's specific goals or "wants and needs" are sufficiently understood prior to a nudge implementation and that the nudge is applied within context to become effective in the scope, desired impact and sustainability it seeks.[4] Nudges that are capable of being utilised alongside tailored products, in context, can offer a powerful and effective supplement. They may not provide a complete answer where financially focused and expert advice remains a prerogative (such as a physical interaction during a financial indebtedness crisis) or where individuals face constant economic trade-offs (scarcity) to manage everyday living.[5] In such situations, it is key for product designers to incorporate and be able to adapt to the need for physical interaction where a real human voice is available.

4 Financial capability and education

Financial capability and education are key components of tackling financial exclusion although how it is delivered and embedded, and the extent of its long-term effects continue to be assessed. FinTech can offer a valuable opportunity to deliver "teachable moments"[6] at important financial life episodes alongside active product use thus building self-confidence and motivation, where financial decisions are actioned in conjunction with learning points. It is equally important that financial capability programmes attribute greater recognition and value to intrinsic financial "nous" and capability that the lived experience of financial exclusion evidences. People in exclusion manage finances constantly and with significant cognitive effort, notwithstanding the frequent necessity of selecting expensive financial products that are frequently the only viable choice. Therefore, financial capability components of FinTech products must give credence and validity to the individual's own capability and agency in order for providers to better understand and appreciate customer motivations and behaviours in context. As Lisa Servon has so ably demonstrated in her research, the question should often be re-framed from positing "why a person has made a mistake in their finances?" to understanding more "why a person has made that decision in that context".[7]



4 *Sunstein, C. (2017). Nudges that fail. Behavioural Public Policy, 1(1), 4-25.*
5 *Mullainathan, S., & Shafir, E. (2013). Scarcity: The true cost of not having enough. Penguin*
6 *Center for Financial Inclusion (2016) Teachable Moments: Reach Consumers when they are making financial decisions [online]*
7 *Servon, L. (2017). The Unbanking of America: How the new middle class survives. Houghton Mifflin Harcourt.*

5 Stakeholder collaboration

Wider collaboration and knowledge-sharing among stakeholders is key to understanding the lived experience of financial exclusion, particularly among the not for profit, charity and public sector who may have deeper insight and understanding of the social and community contexts in which persons are situated. Such collaboration can reveal a deeper and holistic insight of how over-indebtedness, credit and other financial issues are managed within wider "life contexts" such as employment, social welfare benefit, housing or family situations. FinTechs are able to bring their technological advantage to combine with the expertise of other stakeholders in understanding the social psychological and behavioural contexts of persons and communities in financial exclusion. Through collaboration and a multi layered stakeholder engagement, a more sophisticated model and approach to developing products can be fostered. This lies in contrast to top down models which have inherent information asymmetries and which do not fully take account of the customer lived experience. The resulting data received from customers and wider stakeholder collaboration can produce a powerful data set.

6 Product differentiation

Until financial exclusion is eradicated, the importance of product differentiation will continue to increase with the desired effect of minimising - as far as possible - the negative outcomes of financial products that are unaffordable or "unsafe" for those using them. Initiatives taken by FinTech providers to seek wider inputs and validation of their products, as well as through the key customer voice and lived experience, can bring wider credibility to those seeking to address financial exclusion. In doing so and over time, such products will gain recognition as being fair, reasonable and meeting independent objective criteria.

Summary

FinTech is uniquely placed to challenge and modify the "one size fits all" approach to banking which has failed many by adopting the approaches described above. The FinTech community can combine technological innovation and physical interaction to deliver a more sustainable product from the customer's perspective. A FinTech provider that can successfully deliver measurable outcomes to solving financial exclusion may also benefit from social investment capital such as may achieved through social impact bonds. Wider society can benefit as we transition from a financial inclusion/exclusion policy to one where financial products and providers are primarily assessed (and trusted) on the extent to which they consistently meet customer needs and wants in context on a sustainable basis.

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