Consumer Research

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Financial Services Authority

Measuring financial capability: an exploratory study

Prepared for the
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by Personal Finance Research Centre,
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FSA®

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Ethnos Research and Consultancy undertook a separate study to test an early draft of the questionnaire with people from black and ethnic minority communities. This has been invaluable in ensuring the cultural sensitivity of both the questionnaire and its analysis.

BMRB has assisted with the refinement of the questionnaire, including the final two rounds of testing. We are grateful to both their research staff and the interviewers for the improvements they have identified.

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1. Executive summary

In 2004 the Financial Services Authority (FSA) announced that it would commission a "*comprehensive baseline survey to establish the current state of financial capability in the UK*". The FSA subsequently asked the Personal Finance Research Centre to carry out an exploratory qualitative study to design a questionnaire that could be used to measure levels of financial capability. Within this overall aim, the study had three specific objectives:

- To identify the components of financial capability with input from consumers and experts, and to explore whether the components vary in different circumstances.
- To design a questionnaire that can capture these components of financial capability in a large-scale quantitative survey.
- To design a scale against which individuals' financial capability can be measured, taking into account their circumstances and 'need to know'.

The study has been carried out in five stages:

- A literature and research review, to help develop a model of financial capability and to review questions used in other surveys.
- Eight focus groups held in three different areas to explore people's perceptions of financial capability, and to identify ways of capturing it in a survey.
- A first wave of depth interviews with people who had participated in the focus groups to develop the content of the questionnaire.
- A second wave of semi-structured interviews to provide a cognitive test of the structured questionnaire.
- Two further waves of interviews to test the questionnaire.

A separate, but linked, study was carried out by Ethnos Research and Consultancy who tested the questionnaire for cultural sensitivity.

1.1. A model of financial capability

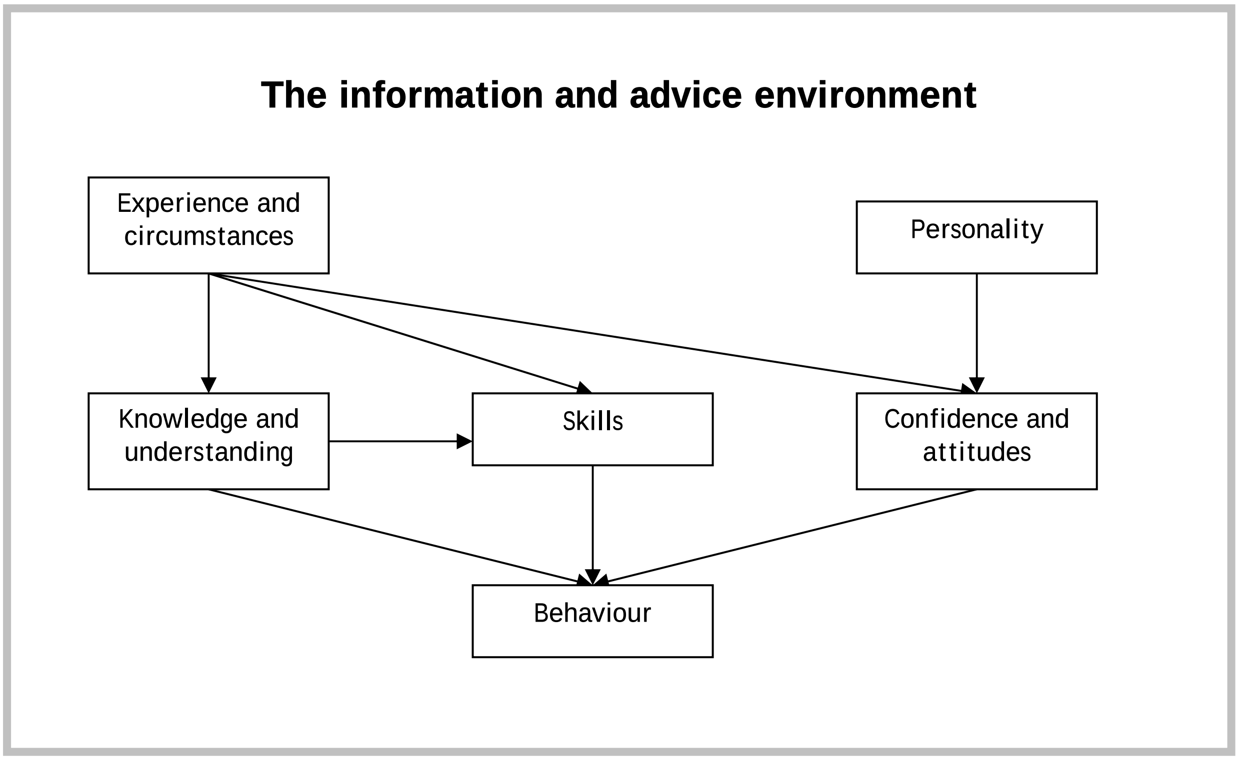
The model of financial capability drew on the *Adult financial capability framework* which was developed by the FSA and the Basic Skills Agency (Basic Skills Agency, 2004), supplemented by a considerable body of other research and literature.

The model that emerged identifies three key elements that determine financial capability. These were:

- knowledge and understanding;
- skills; and
- confidence and attitudes.

These are influenced by a person's experience and circumstances, and by their personality. The extent of a person's financial capability can be measured by examining their behaviour.

In diagrammatic form, these relationships look something like this.



In essence, this was the conceptual model that was tested in the focus groups.

1.2. Capturing financial capability in a survey

Discussions in the focus groups revealed that people thought about financial capability in behavioural terms, suggesting that the baseline survey should be structured accordingly. Overall, they felt that financial capability had four discrete aspects:

- **Managing money -** which was primarily concerned with being able to live within one's means.
- **Planning ahead -** which was required to cope with unexpected events and to make provision for the long term.
- **Making choices -** which involved being aware of the financial products that were on offer, and being able to choose those that were most appropriate to an individual's circumstances.
- **Getting help -** which had two dimensions: self-reliance and using third parties.

1.3. Designing and testing the questionnaire

The questionnaire was developed through two waves of interviews with 33 people: a wave of depth interviews to refine the content of the questionnaire and a wave of cognitive testing interviews using the structured questionnaire. The questionnaire was also tested with 15 people from black and ethnic minority communities. The draft questionnaire was refined by two further waves of testing, each involving 100 people.

It was not easy to measure individuals' financial capability in the kind of structured questionnaire that is required by a quantitative survey. First, the survey needs to address a wide range of factors that are not amenable to simple measures. Secondly, the survey needs to collect information from people who live in widely different circumstances. Designing a questionnaire for the majority of people was relatively straightforward; ensuring that it was capable of distinguishing levels of capability at the income extremes was far more difficult.

Another key challenge was to capture the financial capability of people who rely on someone else to make most of the financial decisions for them. The questionnaire also needed to be culturally sensitive.

1.3.1. Structure

The topic guide used in the first wave of interviews was divided into four sections, one for each of the four domains being studied: managing money, planning ahead, making choices and getting help. Testing showed however, that this was not always the most helpful structure for respondents to the interviews, and the resultant questionnaire does not exactly mirror the four sections.

1.3.2. Managing money

This section, more than any other, illustrates the problems associated with a one-size-fits-all approach. Considerable time was spent to ensure that it included questions that were appropriate to people at the income extremes, that it identified and accommodated people with limited responsibility for money management and that, as far as possible, it took account of the complexities of money management in extended families that are common in some South Asian communities.

The questionnaire covers:

- record keeping and knowing where you are with your finances;
- planning for 'lumpy' expenditure, such as quarterly or annual bills; and
- living within one's means.

1.3.3. Planning ahead

This section demonstrates the importance of distinguishing among better-off people between those who have planned for such eventualities and those who have adequate provision by default rather than by design. Likewise it shows the importance of being able to identify people on low incomes who would plan if they had enough money, and those who would not.

The questionnaire covers how people would deal with:

- an unexpected drop in income;
- an unexpected expense;
- anticipated expenses; and
- retirement.

1.3.4. Making choices about financial products

This part of the questionnaire begins with a general section which assesses basic knowledge about financial products, attitudes to risk, confidence about selecting appropriate financial products, and the extent of trust of financial advisers. The questions are tailored to accommodate different levels of involvement with the financial services market.

The questionnaire collects information about how people:

- monitor the products that they hold; and
- choose products.

1.3.5. Getting help

The section covers the steps that people take to ensure that they are well-informed as well as their use of advisers. It explores how people:

- keep abreast of changes;
- use information and advice; and
- deal with complaints.

1.4. Developing a scoring system

Most of the work associated with developing a scoring system can only take place when sufficient data becomes available from the main survey. We can, however, set out the broad approach that will be adopted.

First, it is clear from the development work that there cannot be an overall scale across the whole questionnaire. Secondly, it is clear that it would be inappropriate to have a 'pass mark', above which people are considered capable and below which they are not.

We have adopted five broad criteria in selecting the scoring system to use:

- **Reliability** – it should produce accurate output and have internal consistency.
- **Validity** – it should measure what it is intended to measure.
- **Relevance** – it should relate to the outcome being evaluated, with no bias for different income or ethnic groups.
- **Comprehensible** – it should be possible to explain the outcomes to a non-technical audience.
- **Longitudinal** – it should be possible to repeat the process in future surveys and compare the outcomes.

Three approaches have been considered, all of which meet these criteria. The first is a 'simple count', would involve assigning a score to each question and adding these up to give an overall score for each respondent. This can then be converted to percentages from 0 (worst financial capability) to 100 (best financial capability). This is the approach used in the *Skills for Life* survey (DfES, 2003).

The second approach is more complex and similar to the ones used for predicting longevity of individuals, or for credit scoring to predict individuals' likelihood of falling into arrears. It is based on regression analysis.

The third approach is one that is used for the Index of Multiple Deprivation and Health indices. This is also fairly complex and uses factor analysis. This method, like the other two, is robust and well-tested. It is, however, complex and rather less easy to explain. It is based on factor analysis of the data with the results for each domain transformed to a normal distribution.

At this stage, the third approach seems best suited to the types of inter-related behavioural questions that are being used to assess financial capability in the survey. Building on this approach, further analysis can be undertaken to combine the assessments of the four separate domains for individuals. In this way it will be possible to build a typology of consumer financial capability that describes individuals' strengths and weaknesses. This could then be used to inform policy and practice for raising levels of financial capability.

2. Introduction

It is now widely recognised in the UK that consumer financial capability goes hand in hand with regulation and competition in ensuring that we have an efficient financial services market. Indeed, a recent report by the National Association of Citizens Advice Bureaux shows the consumer detriment that can arise through low levels of consumer financial capability (NACAB, 2001). Financially incapable consumers find it difficult to identify products and services that are appropriate to their needs; they are unsure about how best to access and evaluate independent advice; they make inappropriate financial decisions; and they fall victim to abusive practices and mis-selling.

The establishment of the FSA marked the first time a financial services regulator was given a statutory responsibility to promote public understanding of the financial system in the UK. From the outset, the FSA has played an active role in the area of financial capability, issuing a consultation paper on how it should undertake this role soon after it was set up. Since then the FSA has commissioned a large body of research and developed a framework for adult financial capability that draws on earlier work in schools (FSA, 2002b).

In 2003, the FSA launched a new initiative to develop and implement a national strategy for financial capability (FSA, 2003). This included the establishment of a Financial Capability Steering Group, which identified seven priorities that are being explored by specially convened working groups. These priorities cover: schools, young adults, families, work, retirement, borrowing and advice (FSA, 2004a). In the 2004 progress report, it was noted that the FSA would commission a "*comprehensive baseline survey to establish the current state of financial capability in the UK",* which would also be used to inform the evaluation of individual pilot projects that will be set up within the strategy (FSA, 2004a).

The FSA subsequently commissioned the Personal Finance Research Centre to carry out an exploratory qualitative study and to design a baseline questionnaire to measure levels of financial capability in the UK. Within this overall aim, the study had three specific objectives:

- To identify the components of financial capability using input from both consumers and experts, and explore whether the components vary in different circumstances.
- To design a questionnaire that can capture these components of financial capability in a large-scale quantitative survey.
- To design a scale against which individuals' financial capability can be measured, taking into account their circumstances and 'need to know'.

2.1. Previous research measuring levels of financial capability in the UK

A number of research studies have identified relatively low levels of financial capability among consumers in the UK, and show that they encounter difficulties in dealing with the growing complexity and diversity of financial services provision. Some of these studies are quantitative, others are qualitative, and between them they have used a variety of methods to capture this information. We give an overview of a selection of the key studies below, drawing out some lessons in terms of methodology.

The *Better informed consumers* quantitative survey undertaken for the FSA in 2000 used an administered questionnaire to capture consumer reports of their behaviour and information needs when they bought products they had acquired in the past five years. This looked particularly at where people had gone for information or advice as well as their willingness to use different sources of information and advice. It also covered a number of attitude statements that were used to assess the level of interest in financial matters, consumers' own assessments of their skills in selecting the right financial product and approaches to money management and saving. There was a parallel qualitative study as well.

This survey found that around nine in ten consumers who had considered taking out or had taken out a financial product in the past five years said they felt confident that they had enough information and that they had made the right decision. But related qualitative research showed that this confidence was often misplaced. (In fact, one in eight had bought a financial product in the past five years that they had later regretted.) It also found that about eight in ten consumers said that they tended to shop around, but in practice hardly any of them had actually done so (FSA, 2000a).

A broadly similar approach was adopted by the Financial Services Consumer Panel Survey. Here, though, consumers were asked about the most recent savings or investment product they had bought. They were also asked whether this had been bought in the past 12 months, one to five years ago, or more than five years ago. This survey asked a number of questions designed to capture consumer attitudes and reported behaviour, which were used to develop scores of levels of financial literacy, confidence and risk aversion. The Personal Finance Research Centre undertook this analysis, but had not been involved in the design of the original questionnaire. We consider that it offers a starting point but that the questionnaire could be greatly improved, especially with regard to the measure of financial literacy.

The Financial Services Consumer Panel survey showed that around four in ten consumers reported feeling confident about making their own financial decisions, and a third were confident that they had a clear idea of the sorts of products they need. But these were rather different types of people; the first group were more likely to be people with limited holdings of financial products than the second. Around half of the people surveyed were judged to be risk averse, and these people held below-average numbers of financial products. Around a third said they reviewed their finances regularly. The extent to which people did so differed according to life stage, economic well-being, level of product holding and confidence about financial decisions. Turning to information and advice, seeking pre-purchase advice was considered important for all products, but especially so for 'investment products', pensions and mortgages. About half of those who had bought pensions, life assurance policies or investment products said that they found it difficult to understand the charges levied on them, and six in ten of those who had taken out a mortgage said that it was difficult to compare the costs of different products (Financial Services Consumer Panel, 2001).

Follow-up qualitative research for the Financial Services Consumer Panel in 2003 however, showed that, regardless of age and social class, people were generally prepared to admit to being fairly uninformed and unsophisticated with regard to financial products. Only a minority regarded themselves as 'financially astute' and prepared to shop around. These spanned all social classes, although there was evidence that some people in social classes D and E might be particularly vulnerable. The research identified 'customer relations concerns', with consumers saying that providers fail to give them the full picture. In particular, they identified a failure to draw attention to key terms and conditions; to advise on performance of long-term products; and to notify changes in savings account interest rates. The study also identified 'product related concerns', such as small print, problems comparing like-for-like, and limited understanding of life assurance, pensions and investment products (Financial Services Consumer Panel, 2003a).

Other qualitative research undertaken for the Consumer Panel at much the same time explored the way that consumers manage their own finances, as well as their overall understanding and interpretation of the financial world around them. This showed that most consumers undertook little long-term planning or budgeting. Most decisions were reactive rather than proactive. There was a general misunderstanding of the so-called 'more sophisticated' financial products – although many could identify ones they considered risky, they could not say why they thought this was the case. Like many other studies, it also found that when people want advice they turn first to their family and friends (Financial Services Consumer Panel, 2003b).

A study of young people (aged 15-18) showed that parents were the main source of information about financial matters. It was, however, parental behaviour rather than their advice which had the greatest impact on young people's decisions. Levels of shopping around for financial products were very low, in contrast to their behaviour when buying clothing or mobile phones (FSA, 2004b).

To inform its investigation into changes that might be made to liberalise the polarisation regime, the FSA commissioned six independent consumer studies: some quantitative, others qualitative. These showed that over a quarter of consumers had obtained financial advice in the past 12 months; around one in five people had sought advice from a bank, building society or insurance company; and one in eight had consulted an independent financial adviser. Most had done so because they felt that they lacked the knowledge they needed to make a financial decision. Regardless of their financial sophistication, consumers clearly differentiate between 'information' and 'advice', which they saw as guidance on the most suitable product given their needs and circumstances. Tied advisers tended to be selected on the basis of trust; independent advisers on their status. However, consumers in general were sceptical about whether there is such a thing as independent advice (FSA, 2002a).

Drawing this together, it seems that the qualitative research elicited a more realistic picture of people's financial capability than most of the quantitative studies have done to date. And, within the quantitative surveys, different approaches have been used to assess financial capability, with varying degrees of success. Some rely on consumers' own assessments of their knowledge and confidence, and how they tend to manage their finances and make decisions about financial products. This approach was used in a recent Australian survey of financial literacy (Roy Morgan Research, 2003).

Others try to obtain more objective measures through questions designed to assess consumer knowledge, and consumer accounts of their behaviour when they last purchased a financial product. Overall, this approach seems to be more fruitful.

None of the research studies that have been carried out to date, however, provides a robust means of measuring and monitoring levels of financial capability in the population as a whole. The FSA, therefore, commissioned the Personal Finance Research Centre to undertake this exploratory, methodological study to design a baseline questionnaire that could be used to measure levels of financial capability in the UK.

2.2. Research methods

The study has been carried out in five stages:

- A literature and research review, to help develop a model of financial capability and to review questions used in other surveys.
- Eight focus groups held in three different areas to explore people's perceptions of financial capability, and to identify ways of capturing financial capability in a survey.
- A first wave of depth interviews with people who had participated in the focus groups to develop the content of the questionnaire.
- A second wave of semi-structured interviews, to provide a cognitive test of the questionnaire.
- Two further waves of interviews to test the questionnaire.

Further testing was undertaken with people from black and ethnic minority communities in a separate, but linked study, undertaken by Ethnos Research and Consultancy. The results have been incorporated into this report, and the study is described in more detail in Appendix A.

2.2.1. Literature and research review

The first stage of the qualitative study was to develop a detailed conceptual model of financial capability, in order to provide a basis for measurement in a quantitative survey. This involved a wide-ranging review of existing literature and research, the findings of which are reported in Chapter 2.

At the same time, we reviewed a large number of earlier studies that sought to assess levels of financial capability. This included studies carried out in the UK, many of which are described above, but also extended to work carried out in the US, Australia and other parts of the world. These studies are listed in the bibliography. They were reviewed in detail to identify the most appropriate and accurate ways of capturing the level of financial capability of consumers.

In total, we reviewed the methods used in 37 surveys from eight countries. The main areas covered by these surveys were knowledge of financial products, behaviour and attitudes. Hardly any attempted to capture skills or experience.

In terms of the topics included in these surveys, most asked questions about the financial products that people had (currently and/or in the past). Some included questions about money management behaviour; knowledge of sources of information and advice; and people's behaviour in terms of seeking information and advice.

There was little or no coverage in these surveys of people's attitudes, knowledge or skills in relation to money management. Financial planning was rarely touched upon, and very few asked about people's skills and attitudes with respect to seeking information and advice.

Moreover, none of the studies we looked at attempted to relate financial capability to consumers' circumstances. This is something we have tried to address in the fieldwork. In particular, we have aimed to assess the impact on financial capability of the financial world in which people operate and how this changes over the life cycle.

2.2.2. Focus groups

Eight focus groups were held in three different areas and with people in different age groups. Two groups took place in a low-income neighbourhood, one with people aged 18 to 39, the other with people aged 40 or over. Three groups were held in a middle-income neighbourhood and three in a high-income neighbourhood. In each of these neighbourhoods, one group was held with young people aged 18 to 24, the second with people aged between 25 and 39, and the third with people aged 40 or over.

The aim of these focus groups was to find out what people considered to be the main elements of financial capability, in order to test the conceptual model and to provide a basis for the development of a questionnaire. The findings are reported in detail in Chapter 3.

2.2.3. Interviews

In order to develop the questionnaire, two waves of interviews were held, involving 33 people in total. The first wave of depth interviews was used to develop the content of the questionnaire. A second wave of cognitive testing interviews was then held, using a more structured questionnaire. The interviews comprised a balanced mix of people at different income levels and from different age groups.

All but four of the people who were interviewed in these two waves had taken part in the focus groups. It was decided to interview the focus group participants because they already had a clear idea of what the survey was trying to achieve and, as a consequence, we could discuss with them at the end of the interview how successfully they felt we had captured their own financial capability. In addition, four extra people were recruited, who were living on state benefits with low levels of product holding. The development of the questionnaire is discussed in detail in Chapter 4.

3. A conceptual approach to financial capability

Financial capability is a relatively new concept and we lack a strong, established consensus about what it entails. However, much valuable work has been undertaken recently, not least in the development, by the Basic Skills Agency and the FSA, of the *Adult Financial Capability Framework* (Basic Skills Agency, 2004).

The Framework was designed "to support the creation of learning programmes and resources around adult financial capability". However, its essentially pedagogic basis means that it is not necessarily a suitable tool for measuring the extent of financial capability within the adult population. We therefore sought to develop a conceptual approach that would provide a more appropriate starting point for the development of a questionnaire.

We began with a review of existing definitions and concepts. The results gave us the basis for the initial discussions in the focus groups, after which we were able to develop and refine questionnaires that were consistent with the conceptual model but which used approaches that were rooted in people's understanding of what financial capability is all about.

3.1. Defining financial capability

At first, attention focused on the need to define financial capability, or financial *literacy* as it was initially conceived. The National Foundation for Educational Research, for example, defined financial literacy as "*the ability to make informed judgements and take effective decisions regarding the use and management of money*" (Noctor et al, 1992). This succinct definition has been widely accepted and built on in the context of personal finance education in schools.

The draft guidance on personal finance within personal, social and health education in schools expanded the National Foundation for Educational Research definition to spell out more precisely the types of judgements and decisions a financially capable person should be able to undertake.

> *"Financially capable people are able to make informed financial decisions. They are numerate and can budget and manage money effectively. They understand how to manage credit and debt. They are able to assess needs for insurance and protection. They can assess the different risks and returns involved in different saving and investment options. They have an understanding of the wider ethical, social, political and environmental dimensions of finances."*

These two definitions were considered to provide a *“base starting point for a broader definition of adult financial capability”* by the Adult Financial Literacy Advisory Group (AdFLAG), which reported in December 2000.

At much the same time, Carolynne Mason and Richard Wilson from the Business School at Loughborough University reviewed a substantial body of literature in their attempt to conceptualise financial literacy. They concluded that it was a *process* leading to desired *outcomes*.

> *“Financial literacy could therefore be defined as an individual’s ability to obtain, understand and evaluate the relevant information necessary to make decisions with an awareness of the likely financial consequences” (Mason and Wilson, 2000).*

3.2. From definition to concept

The Adult Financial Capability Framework, developed by the Basic Skills Agency and the FSA, reflects the process model outlined by Mason and Wilson. It identifies three broad elements of financial capability and, in so doing, begins to specify what it is that financial capability enables individuals to do.

- **Financial knowledge and understanding**
  This is the ability to make sense of and manipulate money in its different forms, uses and functions. Financial knowledge and understanding allows people to acquire the skills they need to deal with everyday financial matters and make the right choices for their needs.

- **Financial skills and competence**
  This is the ability to apply knowledge and understanding across a range of contexts including both predictable and unexpected situations. Financial skills and competence makes available to people the necessary skills to allow them to plan, monitor, manage and resolve any financial problems or opportunities.

- **Financial responsibility**
  This is the ability to appreciate the wider impact of financial decisions on personal circumstances, the family and the broader community, and to consider the social and ethical issues. Financial responsibility enables people to understand and appreciate their rights and responsibilities. They understand the need and have the right skills and attitudes to plan, analyse, decide, evaluate and monitor financial decisions and choices. They understand the various sources of advice and guidance available (Basic Skills Agency, 2004).

The Framework goes on to specify three levels of capability:

- **Basic understanding and developing confidence**
  Aimed at those adults who have a low level of understanding and who require the skills to make informed judgements concerning their finances, and the ability to use appropriate financial services.

- **Developing competence and confidence**
  Aimed at those adults who have a basic understanding and competence in handling financial services, and who require more knowledge and skills to meet their needs.

- **Extending competence and confidence**
  Aimed at adults who require the skills and knowledge to understand the wider range of services and the ability to make informed decisions regarding their own personal circumstances (Basic Skills Agency, 2004).

The clear implication is that an individual can progress from the basic to the extended level through formal or informal learning or, possibly, through experience, if that met their needs.

The Framework is, essentially, a curriculum document, and does not explicitly address the fact that consumers are a heterogeneous group. The nature of the capability required will be determined, to a great extent, by the individual's financial circumstances - the knowledge and skills required by a young lone parent living on a low income, for example, will be very different from those required by a high-income professional who is nearing retirement.

People also differ in the extent to which they choose to use financial products and whether they need advice to do so. Moreover, an individual's use of financial services and their need for advice will almost certainly change over their lifetime.

It is, therefore, necessary to take into account the wider context within which the individual is operating, in particular the individual's circumstances and needs. Here we can draw on work on information literacy and citizenship that was undertaken by Ana Maria Correia on behalf of Unesco. She emphasised both the need to take account of context and the role of information providers when assessing an individual's information literacy.

> *"If the citizen stays within his or her sphere of expertise, then there should be no problem with [basic information literacy skills]. Once outside that sphere, the average citizen should not be expected to have the knowledge required to understand the information ... unless the information is given in a form which is designed for general consumption. Here it is the responsibility of the information provider to ensure that the information provided is suitable for the average citizen, whatever his or her calling" (Correia, 2002).*

This suggests that, to understand financial capability fully, one needs to take account of the *context* within which the individual is operating or, in Correia's terms, the individual's sphere of understanding.

The context will be determined, to a great extent, by the individual's financial circumstances. As we noted above, the capability required by a poor person will be very different from that needed by a rich person.

The context might also be determined by the individual's life stage and any association with the triggers that determine the need for financial products (FSA, 2005).

Other factors that might need to be taken into account include the degree to which an individual interacts with the financial services sector and an individual's ethnicity or faith, and possible limitations that these might place on their use of financial services.

Correia also points to the importance of the information environment – the availability and quality of information and the providers' consequent responsibility to provide information that can easily be used. We also need to include information made available through other channels, such as the mass media.

Further, the role of intermediaries, such as independent financial advisers or friends and family, is important as they can play a key role in the decision-making process.

The nature of this information and advice environment is important as it will condition the level of financial capability required at any one time. If information or advice is generally misleading or not readily available, individuals will need a higher level of skill to gather and interpret the information they need for effective decision making.

In terms of a conceptual approach to financial capability, the information and advice environment can be considered to be an external factor, in the sense that it is fixed – it does not vary from individual to individual, although of course each individual will choose which parts of the information environment they use. The information environment may well change over time, however, and it will also vary geographically, some areas being better provided with sources of advice than others.

3.3. Our conceptual model

The first point to be made is that financial capability is a relative, not an absolute concept. It might be possible to define a basic level of financial capability that is required by everyone in a given society. Beyond that level, the degree and nature of the financial capability required by any given individual will depend on their circumstances.

We, thus, have a universal basic level, or floor, which all individuals need in order to survive and to develop the capability which corresponds to their needs and circumstances. In an ideal world, 100% of the population would attain this basic level of capability.

Beyond this basic level, the nature of the financial capability required by any individual will be determined by their financial circumstances. With this proviso, we initially felt that financial capability consisted of three interrelated elements: knowledge, skills and attitude. This approach was consistent with the results of our literature review.

3.3.1. Knowledge

People require a basic body of knowledge and understanding, upon which they can draw when managing their financial affairs. This knowledge will be acquired in different ways: through experience; through education and training; and through passive receipt of information from different sources such as family and friends, the media and information materials produced by the financial sector.

This basic knowledge and understanding will be supplemented from time to time by information gathered for specific purposes. The additional information will be assimilated and understood in the context of an individual's existing body of knowledge. Some of the information will be forgotten; what is not forgotten will add to the individual's knowledge and understanding.

It follows, therefore, that the body of knowledge will tend to increase through a person's life. Parts of it, however, can become redundant or inaccurate as circumstances change.

The Adult Financial Capability Framework identifies three areas of knowledge and understanding:

- Different types of money or payments.
- Income generation.
- Income disposal.

To this could be added knowledge and understanding of the following:

- Concepts, such as risk, interest, inflation and probability.
- Financial products.
- Institutions, including sources of information, advice and redress.

3.3.2. Skills

People also need the ability to apply their knowledge and understanding in order to manage their money and to make appropriate financial decisions. This calls for a range of specific skills, which need to be underpinned by basic levels of literacy and numeracy. The Framework identifies two sets of skills:

- Gathering financial information and record keeping.
- Financial planning – saving, spending and budgeting.

The Framework lists a third set of skills. 'risk and return', but this concerns understanding the concept of risk and should, we felt, be included as an element of knowledge and understanding rather than an element of skills.

There is, however, another set of skills that should be included. These are the skills required to evaluate information and to make comparisons between different products or courses of action.

3.3.3. Attitudes

Knowledge and skill alone are not enough to ensure that people manage their financial affairs appropriately. They must be prepared to take whatever steps are necessary to apply their knowledge and to exercise their skill. This is largely a question of attitude.

It is possible to identify three elements of a person's attitude towards financial capability. They must be:

- willing to invest the time and other resources required to apply their knowledge and to exercise their skill;
- able to gain access to information, advice and other resources; and
- confident enough to exercise their skills and to act on the results.

The strength of these attitudes can be measured by assessing the extent to which the willingness, ability and confidence is reflected in a person's behaviour.

It might also be useful to take account of people's attitudes towards things, such as their attitude towards salesmen, risk or mutually-owned providers.

We began, therefore, with a conceptual model that was built around three elements: knowledge, skills and attitudes. The validity of this model was first tested at a seminar held by the FSA and held on 4 November 2004. At the seminar, a speaker identified nine factors that influenced financial capability.

- Knowledge
- Understanding
- Basic skills
- Behaviour
- Experience
- Attitudes
- Confidence
- Circumstances
- Personality

Each of these can be further sub-divided. Equally, a case can be made for grouping some together. In our thinking, for example, we had tended to group knowledge and understanding; it also seemed possible to group experience and circumstances, as well as confidence and attitudes. Approached this way, we were able to specify a rather more manageable group of factors.

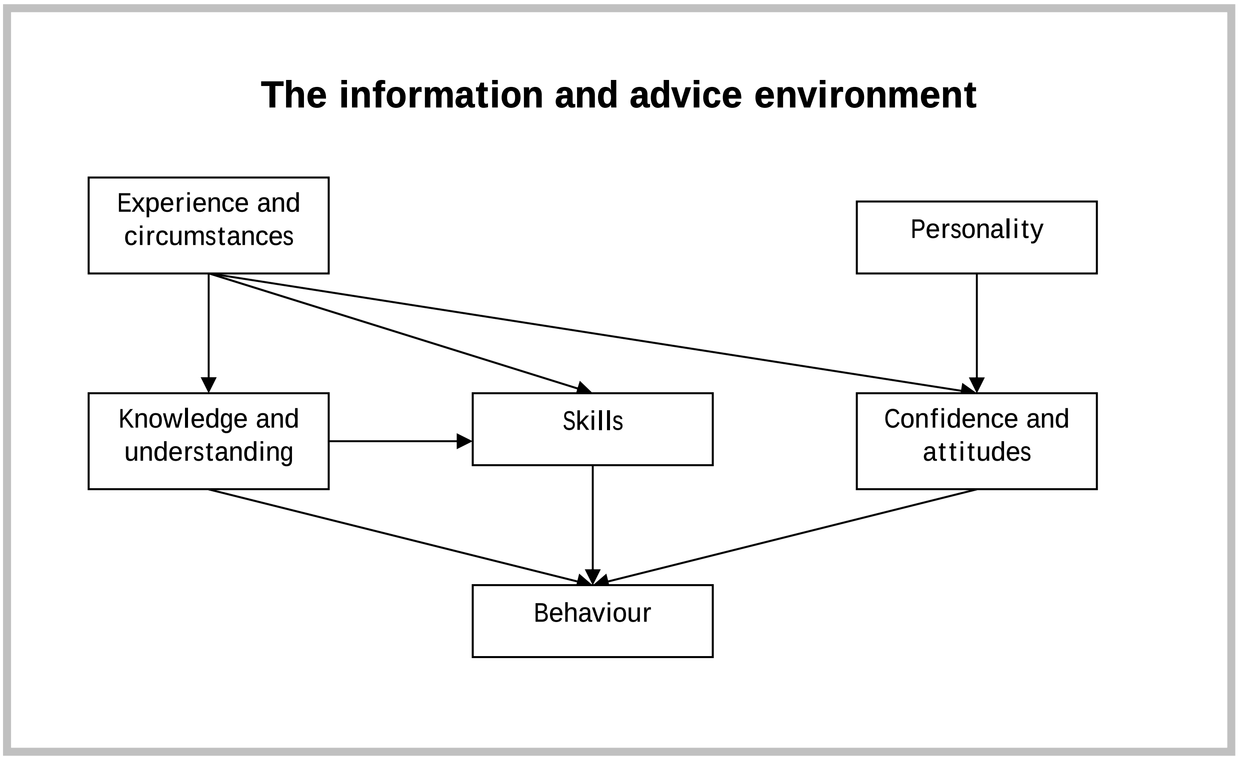
- Knowledge and understanding
- Skills
- Experience and circumstances
- Confidence and attitudes
- Personality
- Behaviour

It now became easier to chart the interrelationships between these factors.

- Knowledge and understanding are influenced by experience and circumstances.
- Skills are also influenced by experience and circumstances. In turn, basic financial skills are shaped, or at least, constrained by knowledge and understanding.
- Confidence and attitudes are influenced by experience and circumstances. They are also influenced by personality.
- Patterns of behaviour are influenced by all the above factors, indeed behaviour can be perceived as evidence of financial capability.

All these factors operate within an information and advice environment that is effectively fixed at any one time.

In diagrammatic form, these relationships look something like this.



In essence, this was the conceptual model that we tested in the focus groups.

3.4. Lessons from the focus groups

We held eight focus groups to explore consumers' own perceptions of what financial capability means, and whether these perceptions varied according to their circumstances. The detailed results of these focus groups are discussed in the next chapter, so for now we will simply outline the main conclusions.

It became clear in all of the groups that people's perceptions of financial capability were rather different from our conceptual model. Perhaps most significant was the fact that they found it very difficult to distinguish between knowledge and understanding, and skills.

Indeed, members of the focus groups perceived financial capability in behavioural terms. They were able to specify quite clearly the characteristics of financially capable people, although the actual specifications varied slightly between groups. Overall, they felt that financial capability had four discrete aspects:

- Managing money.
- Planning ahead.
- Making choices.
- Getting help.

People discussed the issues about knowledge, understanding, skills, attitudes, confidence and personality in the context of their behaviour in relation to these four activities. They felt that personality, confidence and attitudes were inextricably bound up with knowledge and skills, with the outcomes reflected in behaviour.

Managing money

This was primarily concerned with being able to live within one's means. Financially capable people needed to be well organised, particularly when it came to paying bills, and keeping and using financial records. Staying within one's means involved developing strategies to make ends meet and resisting pressures to spend or to borrow money. It also involved accepting responsibility for one's actions. Financially capable people budgeted for lumpy or unexpected expenditure.

Planning ahead

This is required for two purposes: to cope with unexpected events and to make provision for the long term. Unexpected events can upset budgets and financial plans. Financially capable people are able to deal with a large fall in income. They have a plan for meeting expenditure in such circumstances; they have a clear idea of the help that they can expect from the state and from others, such as employers; and they know about, and understand, insurance. They also know how to cope with large, unforeseen expenses. They have made some provision for such unexpected events and they are aware of possible sources of financial help.

Planning for the long term is also important. Here discussion focused on retirement and pensions, possibly because the issue was very topical at the time. They felt that a financially capable person would have made adequate provision or have firm plans to do so; they would know what sort of help would be forthcoming from the state; they would know about appropriate financial products; and they would know how and where to seek advice.

Making choices

Given the array of financial products available, being aware of what was on offer and being able to choose those that were most appropriate to an individual's circumstances were important aspects of financial capability. People needed a good general awareness of the types of product that were available but a constant preoccupation with financial matters was 'sad' and did not indicate confidence.

Consumers should be able to choose the products that were right for them. This required an ability to compare costs and returns; an ability to assess risk and to identify risky products; and an ability to look at products holistically. The financially capable person was also able, and confident enough, to say 'no' in the face of assertive selling or seductive advertising. Some felt that a financially capable person would be able to work the system, getting, for example, the most advantageous interest rates by switching between products. They would certainly know the key features of the products that they had bought, even though they might have struggled with the small print to understand the terms and conditions.

Getting help

This had two dimensions: self-reliance and using third parties. First, people should be able to gather information for themselves. This involved both general environmental scanning, which kept them up to date with what was going on, as well as the ability to find and compare information about different products. Secondly, a financially capable person would know where and when to turn for advice and help from a third party. They would also be able to judge how much trust to place in the information and advice provided.

Interestingly, the ability to complain and seek redress was not seen as being an important aspect of financial capability. In this context, there was a high degree of fatalism.

3.5. The model and reality

Superficially, there does not seem to be a close correspondence between the conceptual model of financial capability and the reality, as perceived by the focus groups. A closer examination, however, shows that the differences are not marked.

The most striking difference was the fact that the focus groups thought about financial capability in behavioural terms. They related it to the four activities described above.

Within each activity, however, they could identify requirements for the conceptual model's three key elements: knowledge and understanding, skills, and confidence and attitudes. More particularly, they were quite sure about the importance of individuals' experience and circumstances. There was a clear recognition that income in particular, and life stage more generally, shaped and constrained financial capability. They emphasised the fact that you cannot judge everyone by the same yardstick.

Personality was also seen to be an important factor. It had a bearing on confidence, shaping people's ability to say 'no', and on their propensity to take action. It also conditioned the way they behaved: whether or not, for example, they were well organised.

In essence, they took our conceptual model and applied it to the four different, but related, sets of activity.

While we, and others who have gone before us, found it relatively easy to distinguish between knowledge and skills, it is clear that consumers do not make the distinction so readily. They perceive financial capability in terms of behaviour: what people do and what they should be capable of doing. This behaviour, however, involves knowledge, understanding, skills of various kinds, and the confidence to use them as and when required.

We feel, therefore, that the focus groups did not invalidate the basic model, indeed they served to endorse it. The groups did, however, provide a clear indication of how best to ask members of the public meaningful questions that would measure financial capability as we have conceptualised it.

4. Developing the framework for the questionnaire

Having developed our conceptual model of financial capability, we held a series of focus groups to test the assumptions underlying the model and to provide a basis for the development of the questionnaire.

4.1. The focus groups

We held eight focus groups that were attended by a total of 68 people. The groups were selected to provide a good spread of both ages and financial circumstances.

Two groups were drawn from a low-income neighbourhood: one with people aged 18 to 39, the other with people aged 40 or over. These people held a relatively low level of financial products. We held three groups in a middle-income neighbourhood, one with young people aged between 18 and 24, the second with people aged 25 to 39 and the third with people aged 40 or over. These participants held a wider range of products, including some investments. The final three groups were in a high-income neighbourhood, the first with young people aged 18 to 24, the second with people aged 25 to 39 and the third with people aged 40 or over. Participants in these groups held a wide range of financial products, including a number of investment products.

Each focus group lasted between 60 and 105 minutes. The discussions were recorded and transcribed in full for analysis using thematic grids. To provide a structure for the discussions, we developed a topic guide which was deliberately kept very open (see Appendix B). The topic guide began by asking participants to describe the characteristics of a person who is *not* financially capable, and then to describe someone who is. It then sought to open up the discussion to consider the knowledge, understanding and skills that people require. Participants were asked to identify other factors that might influence financial capability. The groups finished by considering three different scenarios to explore whether they considered the people concerned to be capable or not.

It became apparent early on that the focus group participants found it difficult to discuss the concepts of knowledge, skills, understanding, personality, confidence and attitudes in the abstract. They were much more comfortable discussing these concepts in relation to different kinds of activity or behaviour. Four particular activities emerged: money management; planning ahead; choosing and using products; and seeking information and advice. Within each of the different activities, participants were able to identify the knowledge, skills and understanding that were required, and were able to consider the ways in which factors like personality, confidence and attitudes would affect behaviour.

4.2. Financial capability

We began each discussion by asking participants to describe the characteristics of someone who they would consider to not be financially incapable and, conversely, those of someone who was financially capable.

All the groups agreed that the key characteristic of a financially capable person was that they were able to manage their money. This enabled them to live within their means and 'keep their head above water'. Money management involved being well organised and keeping control over financial resources. A financially capable person budgeted so that they were able to balance their income and expenditure.

These characteristics were identified by all the groups: young and old, rich and poor. Beyond this, there was some variation by age and by income in what people thought financial capability encompassed – we discuss these variations below.

Most people agreed that planning ahead was an important characteristic. A financially capable person would make long-term provision for expected events and for their retirement. They would also have a strategy for coping with the unexpected.

Financially capable people would be aware of the range of products that were available to them, and would take care to shop around and select the ones that were most suitable. Finally, a financially capable person would make sure that they were generally well informed, and would know where to go for further information and advice. Their financial capability would be influenced by their personality, upbringing and experience.

It seemed, therefore, that financial capability was a function of money management; planning ahead; choosing and using financial products; and accessing and using information and advice. Within this broad framework, however, there were some differences according to age and income level.

For poor people, capability did not extend much beyond day-to-day money management. Their ability to plan for the future was constrained by their lack of spare cash. They used a limited range of products, mostly those involving borrowing, and they used a limited range of sources of information and advice. Young people had very similar views and patterns of behaviour.

On the other hand, better-off people faced fewer money management problems and, because they generally had spare cash, they often did not find it necessary to plan for expected or unexpected events. They did, however, use a much wider range of financial products, and drew on a wider range of information and advice.

Young people, as we have noted, had a fairly constrained view of financial capability. In contrast, middle-aged people, while retaining the emphasis on money management, identified a greater need for forward planning, and for pensions in particular. They chose and used a fairly wide range of products, drawing on a range of sources of information and advice.

Older people reflected generational differences in attitudes towards money and, particularly, the use of credit. They arguably had the most balanced view of financial capability, although the emphasis on money management remained.

4.3. Managing money

All the groups thought that managing one's money was very important, indeed there was a strong sense that this held the key to financial capability: if a person was not able to manage their money day to day, then no matter how good they were at planning ahead, choosing and using products, or seeking advice, they would not be able to make best use of their financial resources.

4.3.1. Budgeting

For most people, money management involved being in control of one's financial resources, monitoring income and keeping some kind of record of expenditure. Critically, it required someone to be aware of regular outgoings and to ensure that they would always be able to meet these commitments. To do this successfully required someone to be both quite organised and be prepared to spend some time working out budgets, keeping records and checking statements.

'Lumpy' expenditure, or commitments that fell outside the normal weekly or monthly pattern, presented a particular difficulty that had to be taken into account when budgeting. This highlighted the differences between people on different incomes. People on low incomes found that 'lumpy' expenditure caused them real problems, and they sometimes had to borrow in order to meet the commitment. In contrast, people in the high-income focus groups said that they were able to meet such expenditure out of their regular surplus income.

The purpose of all this budgeting and control activity was to enable people to live within their means or, as many people put it, to "*keep their heads above water*". There was a general recognition that inadequate or low incomes made the process of money management more difficult. This view was emphasised, unsurprisingly, by those on low incomes: they commented that some of the most skilful money managers were the people who had to exist on state benefits. It was also a view that was stressed by the younger people, many of whom had incomes that they felt were low relative to their requirements. That said, a minority of older people on higher incomes recognised that people living on state benefits long term should not be judged incapable if they sometimes failed to make ends meet.

4.3.2. Pressure to spend or borrow

People were very conscious of the ways that money management and budgets could be upset by pressures encouraging people to spend. These pressures were thought to be growing, and came from advertising, the desire to keep up with one's peers and, particularly, from children. Resisting such pressures was considered to be a mark of capability. Young people seemed to find it hardest to resist such enticements to spend.

People also felt that they were being tempted to borrow money. They felt that they were constantly being offered credit, particularly through direct mail advertising, and that getting credit, or extending credit limits, was easy – some said it was too easy.

The ability to resist the pressure to spend and the temptation to borrow was seen by all groups as a characteristic of a financially capable person.

4.3.3. Borrowing and credit

There was a general wariness of credit. Most of the participants, particularly in the younger and middle-aged groups, were using credit of some kind. They felt, however, that a financially capable person would avoid using credit if they could or, if they could not, that they would make sure that they were able to repay what they owed. Reckless use of credit was regarded as a mark of financial incapability.

The people on middle incomes felt that the use of credit should be kept under control and that a financially capable person would not 'overborrow' to the extent that they found it difficult to keep up with the payments. They also felt that a financially capable person would not borrow to meet regular commitments or to buy things like food. The experience of poor people was different. They felt that it was sometimes necessary to borrow in order to cover lumpy expenditure, pressing commitments, and unforeseen events.

The people with high incomes used credit quite extensively. This group felt that a capable person would be able to borrow cheaply and to 'play the system'.

Younger people had the most relaxed views on the use of credit. Many had, or were contemplating taking out, loans to cover major expenditure like the purchase of a car. For this kind of borrowing, the important thing for them was to ensure that they would be able to meet the repayments. Most also used credit cards quite extensively but they were critical of people who built up large credit card balances and who only made the minimum repayments each month.

People in the middle-aged groups drew a similar distinction between types of credit. Mortgages and loans to buy cars were accepted as necessary and it was a matter of simply making sure that the repayments could be managed within the family budget. There was, however, a wariness of credit cards and a feeling that their use should be restrained.

The older people were more likely to comment on the overuse of credit and were particularly wary of the overuse of credit cards. These attitudes seem to be associated with the view that financially capable people were those who were able to defer gratification and so put off a purchase until it could be afforded.

4.3.4. Group characteristics

Somewhat alarmingly, people on high incomes appeared almost automatically to associate a lack of financial capability with broad social groups. The 18 to 24 year olds among them thought that unemployed people and students were financially incapable; the 25 to 39 year olds thought that young people, lone mothers and people on state benefits were financially incapable; while those aged 40 or over identified benefit recipients and 'artistic people' as financially incapable. In each case, the criterion seemed simply to be the level of income that the groups were assumed to receive. In their minds, someone was financially incapable if they lived on a low income, as a more capable person would make sure that they earned more. These did not, however, seem to be strongly held views.

4.3.5. Enjoyment

Interestingly, only the older groups commented on the need to balance the management of one's financial affairs with the need to enjoy one's money, suggesting that excessive amounts of time spent gathering information or shopping around indicated a person who was 'sad' rather than financially capable. The younger groups also seemed to think that the enjoyment of money came with spending it, but they were aware that unrestricted spending carried with it the consequence of losing control, overcommitment and excessive borrowing, all things that a financially capable person would avoid.

4.4. Planning ahead

Making financial provision for the future was something that everyone thought was important. There were two aspects to this: making long-term provision for expected commitments and requirements, and providing what some described as a safety net, to cover the unexpected.

4.4.1. Saving

The ability to save was strongly associated with planning ahead. This could involve saving money for expected events and for specific purposes: for example many of the young people mentioned the need to save for a car or for a deposit on a house. Or it involved saving for emergencies; the middle-aged and older people, in particular, saved in order to build up a safety net to cover emergencies or unexpected expenditure – in other words they were saving for a rainy day.

Saving behaviour clearly differed with income. For people on low incomes, saving was difficult. Indeed, for some it seemed a hopeless aspiration and, consequently, they did not spontaneously identify saving with financial capability. For people on high incomes, though, saving was an aspect of regular budgeting, suggesting that a financially capable person would budget for regular expenditure and would then decide how much of their surplus income to save.

4.4.2. Planning for the long term

Everyone thought that making long-term provision for expected events was an important part of financial capability. There was a considerable range of things that people were planning for, including buying a car, buying a home, helping children to buy a home, paying for children’s higher education, pensions and long-term care. The older that people were, the more conscious they seemed to be of the need to make such provision early in life.

Both age and income level seemed to have a bearing on people’s views about planning for the long term. Young people recognised the importance of making provision but few were actually doing so. Poor people were in a similar position.

Middle-aged people were aware that they could use a range of financial products in order to make long-term provision. They were also most aware of some of the complexities; some, for example, were conscious of the fact that having savings might mean the loss of entitlement to some means-tested benefits. There were also some who were content to leave matters to the government, believing that, at the end of the day, the state would provide. A number of the middle-aged people stressed the importance of getting the balance right between saving for the future and using one’s money to enjoy life.

Older people were more likely to say that they had little incentive to save for the long term, many because they were already retired and, for them, the long term had arrived.

The lack of incentives to save was also mentioned by the people on high incomes, although here the lack of incentive was more closely associated with low interest rates and investment returns.

Much of the discussion focused on pensions. In part this might be a reflection of the fact that pension reform was a very topical issue at the time the focus groups were held. The majority of people recognised that they had to make some provision over and above their entitlement to a state pension. There was, however, little agreement on what was the best strategy. Some people, as we have noted, were prepared to leave things to the government, believing that the state would provide them with an adequate pension. There seemed, however, to be a generally low level of trust in the government, in pension providers or in firms that ran their own pension schemes. Perhaps as a consequence, a number of people were exploring alternatives to conventional pensions. Some were investing in stocks and shares. A larger number, particularly among those who were better off, were investing in property. Indeed, there seemed to be a fairly widespread belief in the long-term value of property.

4.4.3. Planning for the unexpected

People recognised that they might face the need to cope with unexpected events like a sudden drop in income, a significant increase in expenditure, a major one-off expense, the loss of possessions or damage to one's dwelling.

The extent to which people made provision for these possible events varied considerably according to their income. People with low incomes faced the biggest problems. They lacked the spare cash that would be needed to build up a safety net and they found it difficult to justify expenditure on insurance. In contrast, for people with high incomes, unexpected events of this kind presented less of a problem as many of the unexpected expenses could be managed within existing budgets. Even the loss of income did not seem to be a concern as most of the people on high incomes believed that they would simply get another well-paid job.

Insurance clearly provides for events of this kind. People with low incomes were more likely to mention taking out payment protection insurance to guard against financial difficulties arising from the loss of income. There was, however, a degree of scepticism about other forms of insurance, particularly insurance against the breakdown of things like white goods. People generally seemed to balance the cost of insurance against the risk of being uninsured.

The other safety net is provided by the benefits system. Knowledge of the way the system works varied considerably, although nearly all people commented on its complexity and the difficulties one faced if claiming for the first time. Among the middle- and high-income groups there were considerable misconceptions about eligibility and the amounts that one would receive if one were eligible. The people on high incomes, in particular, over-estimated the amounts that people would receive and underestimated their entitlement: they seemed to believe that people who were dependent on state benefits lived on comfortable incomes, while they themselves would not be entitled.

4.5. Making choices

The types of financial products that people held varied according to their age. Middle-aged people tended to have the widest range. Young people most commonly just had credit, in the form of credit cards, loans and overdrafts, while older people tended to have pensions and investments.

4.5.1. Shopping around

With the exception of the older groups, people thought that a financially capable person would take the trouble to shop around to get the best value – both generally and in relation to financial products. They would also be concerned to get the products that were most suitable for them. This required three things: a good general understanding of what was available; shopping around before purchase; and monitoring during the life of the product.

Attitudes towards background knowledge differed. Some people felt that it was best to build up a general understanding regardless of whether one had an immediate need. Others felt that it was better only to gather such information in response to need. This dichotomy arose in all the groups.

Most people, however, admitted that, when they were planning to buy a product, they did not shop around as assiduously as they felt they should. The main reason for this seemed to be that people found it difficult to compare products. They found the products themselves complex and were not at all sure what criteria they should use to compare one against another. In this context, there was a widespread lack of understanding of interest rates in general, and APR in particular. Faced with this, many people seemed either simply to choose the lowest-priced products, or they chose products offered by big firms on the grounds that they felt that the firms were more likely to be trustworthy.

They also did not monitor their products, once purchased, so that they could switch to others that offered more favourable terms. The exceptions here were credit cards and mortgages; people seemed ready to switch providers of these products to take advantage of more favourable offers.

4.5.2. Risk

People's attitudes towards the risk associated with financial products seemed to vary considerably. The younger people did not associate the ability to assess risk with financial capability, indeed many participants did not fully understand the concept of risk. The middle-aged people thought that a capable person would be prepared to take risks in order to make money. The older people, however, seemed a little more cautious, and emphasised the importance of taking risks within one's limits.

A similar variation seemed to apply to the different income groups. Some people in the low-income groups perceived risk almost exclusively in terms of being able to keep up with commitments. The middle-income people tended to associate risk with making money, while those on high incomes took a rather more measured view and said that a financially capable person would assess risk in relation to the amount they could afford to lose.

4.5.3. Small print

Choice and comparison were made more difficult by the fact that people perceived that the products' terms and conditions were usually set out in small print. People usually did not read these terms and conditions, although they felt they should. This was felt to be particularly critical when buying things like equity-based products that carried a degree of risk. Awareness of such risks appeared to be low, particularly among young people and those with low incomes. Most people said that they would like to see the terms and conditions expressed in simple, clear, easily understood language, and printed with a type size that was easy to read.

4.6. Getting help

People considered that information and advice were important aspects of financial capability. A financially capable person would, they felt, get help from passive information sources, such as newspapers, the broadcast media and the Internet. This would help them to become well informed. They would also know where to go for specific advice and assistance from third parties. They would know their rights and they would be able to seek redress when things went wrong.

4.6.1. Background information

As we noted above, people were divided over when it was useful to gather background information. There was, however, much more agreement on the sources of information they used. They gathered information from broadcast media (television and radio), newspapers and magazines. The Internet was used for background information by some, but people more commonly turned to the Internet when seeking information about a specific product.

People sought information on a wide variety of topics, ranging from general issues like the state of the economy or the housing market, through to new product developments and special offers.

While nearly everyone felt that it was important to keep up to date in this way, there was a recognition that it could be taken too far; people who spent all their time reading the money pages of the Sunday newspapers were, generally, considered to be rather 'sad'.

4.6.2. Specific issues

Everyone agreed that the important thing was to know where to go for advice. When people needed information or advice on specific issues they, unsurprisingly, turned to a different range of sources. Some relied on family and friends. Young people, in particular, said that they would turn first to their parents. Other potential sources of advice were the Internet, banks (popular with young people and those on low incomes) and employers (used mostly by low-income, middle-aged people). Independent financial advisers were used by everyone other than people with low incomes. They were used most heavily by people on high incomes, one of whom suggested consulting three and comparing the results.

The choice of which source of advice to use clearly depended on the degree to which they were trusted. People recognised that family and friends might not know very much but they felt that they could be trusted. In contrast, independent financial advisers were regarded with a considerable degree of scepticism as people felt that they would be inclined to advise someone to have the product that generated the largest commission for the adviser rather than one that best suited the consumer. There was also a belief that if a person sought advice, it was almost inevitable that they would be put under pressure to buy a financial product.

Notwithstanding people's scepticism about the objectivity of the advice provided by professionals, there was a clear feeling that being mis-sold a product by a professional adviser did not necessarily mean that a person was financially incapable.

4.6.3. Rights, complaints and redress

People generally felt that it was important to know about one's rights and how to assert them. Most people, however, were aware that their knowledge was patchy. Perhaps because of this, people were fatalistic about their rights and their ability to complain successfully. In part, this related to the terms and conditions embedded in the small print on contracts. People seemed to feel that when things went wrong the firms would be able to point to something in the small print that exonerated them. Even if right was on the side of the consumer, people felt that embarking on a complaint was tantamount to starting a 'war of attrition', in which the firm would continue to make life difficult in an attempt to force the consumer to drop the complaint. Faced with this gloomy prognosis, it is perhaps not surprising that many people seemed happy to call upon the local Citizens Advice Bureau to help them get redress.

4.7. The X-factors

Throughout the discussions, people referred to a range of additional factors that would determine the extent of a person's financial capability. The key was the individual's personality: whether they were organised; able to resist temptation; likely to plan for the future; prepared to shop around; likely to keep themselves well informed; and prepared to assert their rights. Knowledge, understanding and skills alone were not enough – one had to be prepared to act on them.

People differed in their views about what it was that determined one's personality. Many mentioned upbringing and parental example, but in nearly every group someone was able to point to siblings they knew who differed widely in their financial capability. One participant also pointed out that her parents provided dreadful role models. Despite this, there was a general feeling, particularly among older people, that parents should do more to instil a sense of financial capability in their children.

Experience was felt by many to be important, particularly as one learned from one's mistakes, and there was a general view that a person became more financially capable as they got older.

4.8. Important issues

A number of other issues arose during the focus-group discussions that are important when developing a framework to measure financial capability.

The first is the need to take levels of income into account. Managing money was clearly felt to be more difficult when financial resources were tight. The scope for planning ahead, and the strategies that could be used, were largely determined by a person's income. The range of financial products that a person would use was also, to a great extent, determined by income level. And, to a lesser extent, the range of sources of advice was constrained by a person's disposable income.

The effect is most marked at the extremes. A poor person could still be considered to be financially capable even though they were unable to make ends meet on an inadequate income. Equally, the simple fact of being rich should not be equated to financial capability.

It is also clear that different generations have different attitudes towards things like the use of credit. Just as the needs of older generations differ from those of younger people, and the range of products used differs, so too do people's attitudes. Behaviour that is not considered to be reckless by a 20 year old might appear so to someone in their sixties.

People in most of the groups commented that financial capability meant more that simply knowing what to do. If a person knew what the right course of action was but failed to do it (shopping around for products was a frequently mentioned example), then they could not be considered to be financially capable.

Related to this, the older people and those on high incomes thought that leaving one's financial affairs to others, whether another family member or a professional adviser, was a mark of financial incapability.

This also has a bearing on the need to test financial, or applied, literacy and numeracy. Basic literacy and numeracy skills are required for financial capability, and for almost all other human endeavours in a modern society. We considered, therefore, whether we should include questions to test literacy and numeracy. What is important, however, is not whether a person has the skill, but whether they use it. Someone who lacks literacy and numeracy skills, or who has not developed coping strategies to overcome their deficiency, would not be able to manage money, plan ahead, make choices or, probably, get help when they need it. By measuring their behaviour we are therefore, implicitly, testing their literacy and numeracy.

Finally, being canny should not be confused with financial capability. People thought that someone who, for example, constantly switched between credit card companies to take advantage of zero per cent interest on balance transfers while failing to reduce the level of the balances was more likely to be reckless than capable.

The literature review and our initial discussions enabled us to develop a conceptual approach to financial capability. We tested the model in the focus groups and found that the model itself was sound. However, people found it easier to discuss financial capability in behavioural, as distinct from conceptual terms. We therefore needed to use a pragmatic approach when designing a questionnaire to test. This questionnaire, which is discussed in detail in the next chapter, is grounded in the four behavioural domains of: managing money, planning ahead, making choices and getting help.

5. Designing and testing the questionnaire

The questionnaire was developed through two waves of interviews with 33 people: a wave of depth interviews to refine the content of the questionnaire and a wave of cognitive testing interviews using a more structured questionnaire. All but four of the participants had taken part in the focus groups, and were drawn in equal numbers from people of different income levels and ages. Four additional people were recruited, all of whom were living on state benefits with minimal levels of product holding (such as a basic bank account and a Social Fund Loan) because people in these circumstances present a particular challenge for the survey (as we describe below) and we needed a booster sample.

The ‘managing money’ and ‘planning ahead’ sections of the structured questionnaire were also tested to identify any cultural or religious factors specific to certain ethnic or religious groups that needed to be taken into account. This included 17 interviews with four Indian, five Pakistani, four Bangladeshi, and four Black Caribbean respondents. In addition, 15 interviews were conducted with ‘experts’ who could provide information about the religious, cultural and social factors likely to have an impact on financial capability. This work was undertaken independently by Ethnos Research and Consultancy. The results are incorporated into this chapter, and the work is described more fully in Appendix A.

Two further waves of interviews to fine tune the questionnaire are in progress at the time of writing. Both are being undertaken by BMRB, with interviewers being accompanied by members of the research team. Each wave is made up of 100 people.

5.1. General points

Without doubt, it was easier to capture an individual’s level of financial capability in the depth interviews; translating this into a questionnaire for a quantitative survey was much less straightforward. This is in keeping with previous research, as we have noted in Chapter 1. It became clear very early in the interviews that assessing financial capability is a complex process, which needs to be tailored to specific circumstances and cannot be captured in a short interview. None of the exploratory interviews lasted less than an hour, while a number took more than two hours to complete.

As we have discussed in Chapters 2 and 3, financial capability is considered, by both experts and the general public, to encompass a wide range of factors that do not conform to simple measures. To assess these in more than a superficial way will require an interview of some length (averaging in excess of 30 minutes).

5.1.1. Inappropriateness of a one-size-fits-all approach

It was also apparent that a one-size-fits-all approach would be inappropriate. At one extreme, people living on very low incomes with little or no opportunity to save or plan for the future and limited engagement with financial service products need to be assessed primarily in terms of their ability to manage their finances day to day. They need to be asked about plans that are realistic in their circumstances and products that they have experienced. At the other extreme, someone with an income far in excess of their needs, who has money to invest and experience of a wide range of financial products including some complex investment ones, needs to be assessed quite differently. In this case, greater weight has to be given to their ability to plan for the future, and to choose and use appropriate products wisely.

Failure to modify the interview in this way could lead to the false conclusion that poor people are financially incapable and that financial capability increases with income. This has proved a considerable challenge. Designing a questionnaire for the majority of people was relatively straightforward. Ensuring that it was capable of distinguishing levels of capability at the income extremes has been far more difficult.

Another key challenge was to capture the financial capability of people who rely on someone else to make most of their financial decisions for them. This includes people who rely on their partner to manage the household finances and people who rely on a financial adviser for most of their financial planning and choice of financial products. It is particularly acute in some ethnic groups as we discuss below. This, too, has proved very difficult as, ideally, we need to find out what they would be capable of if they had to do it themselves. At the very least, one needs to know if they are wise to leave everything to someone else, and whether or not they are able to judge whether that person is handling their affairs in a capable way.

Throughout the questionnaire we have, therefore, asked questions to ascertain who is mainly responsible for different aspects of the household finances – including managing money, planning ahead and making choices about financial products. And, although most questions relate to the individual's behaviour, questions on income, saving and borrowing, and the ability to make ends meet are asked about the family as a whole.

Couples tend to pool resources, and often hold savings, investments, mortgages and consumer credit commitments in their joint names. For this reason it is usual to assess these in relation to the family income to arrive at estimates of people's gearing. Moreover, for individuals who rely on their partner to manage the family budget or make financial provision for the future it is important to assess the outcome at the family level to assess whether or not they are wise to rely on their partner in this way.

A third challenge was to make the questionnaire culturally sensitive. In particular, it needs to take account of ways that specific ethnic groups might handle their affairs that differ from others at their age or income level. The most obvious example is that of Muslims, whose religion could influence the ways they make provision both for the future and for unexpected events, as well as the types of products they would find acceptable. But there are other areas of cultural sensitivity too. These include language and literacy difficulties, the extent to which there is gender segmentation in financial responsibilities, and the need to take account of the complexities of money management and planning ahead in extended families. As noted above, the questionnaire was tested separately for these cultural differences.

Many of these points are returned to in the sections below, which discuss the design and testing of specific sections of the questionnaire in more detail. It is, however, important to note that strong gender divisions of responsibility in some South Asian and Black African cultures mean that women may be incapable of answering large sections of the questionnaire.

5.1.2. Format of questions

The topic guide and questionnaire included a mix of questions covering the individuals' circumstances, behaviour, attitudes, knowledge and applied financial numeracy. Wherever possible, questions used and tested in previous surveys were deployed in the draft questionnaire. At key points in the interview, participants were asked for their views of the questions they had been asked and how well they felt these had captured their financial capability. They were also asked to identify any areas they felt had been omitted, or ones that they felt should not have been included. No radical suggestions of this kind were made, although participants did make valuable comments on the detail of the interview and questions they had been asked.

Attitude statements

The attitude questions proved especially valuable and participants often commented that, taken together, the statements in the individual sections of the interview gave a fairly accurate picture of their capability. That said, questions in the first wave of interviews that related to the individual such as: "*I am impulsive and tend to buy things even though I can't really afford them*" worked far better than those that were more general, for example: "*Most financial firms treat their customers fairly*". The non-personalised questions more often elicited equivocal responses like: "*Well, it depends*". As a result, only personalised statements were included in the questionnaire for the second wave of interviews.

Incomes, saving and borrowing

It was decided that accurate information should be obtained about incomes, amounts held in savings and investments, equity in properties owned and amounts borrowed. A number of people queried why this level of detail was required and would have preferred to assign their reply to a banded amount. Most were, however, willing to provide the information when the interviewer explained why it was needed, how it would be used (i.e. in aggregate for groups of people) and the confidentiality of the information they gave. It will clearly not be possible to collect this information at the level of detail of, for example, the *Family Resources Survey* (DWP). At the same time, figures are needed that can be used to calculate ratios of, for example, borrowing to income, so banding has to be avoided.

The testing for ethnic sensitivity identified two particular problems in relation to information about incomes. Many people from South Asian and Chinese communities work in small family businesses, alongside other members of their family. The amounts withdrawn from the business vary from week to week, and are often taken out to meet extended family rather than individual needs. Capturing income from self-employment is complex in any survey, and this adds a further level of complexity. It was decided, therefore, to use the full set of harmonised questions used on all Government surveys to capture income from self-employment. The second problem arises where people in receipt of benefits also have jobs. Experts suggested that it is relatively common for Bangladeshis, Pakistanis and refugees to work informally in this way. This has two implications for this survey: the need to try and record these informal earnings, and the low level of engagement with the financial services sector that this can result in. Both have been taken into account in the design of the survey.

Testing and past experience have shown that respondents often do not know how much their partner may have in savings, or how much they owe on mortgages or credit commitments when these are in their own name only. Because we need fairly accurate information for the family as a whole, we decided to ask respondents for details of commitments held in their own name or jointly, and to use a statistical technique, known as ‘hot decking’, to impute values for their partner’s saving and borrowing.

Language and literacy

The ethnic sensitivity testing showed that some people (and South Asians in particular) found parts of the questionnaire difficult because of a combination of:

- a lack of ease with conversing in the English language;
- literacy problems; and
- a lack of familiarity with financial services and financial services terminology.

This was especially the case with older people and more recent migrants. It should also be noted that the second and third problems were also identified in relation to some people on low incomes in the general testing. Where possible, the questionnaire has been simplified to remove technical language; this is being tested to see if further simplification is needed. The interview relies on the use of show cards and show screens, some of which are, through necessity, quite long. Future testing will identify any remaining problems with these. There is, however, an inherent tension between designing a questionnaire that is efficient for the majority of people while not creating insurmountable problems for a minority of people. In cases where respondents cannot cope with show cards or show screens, it is standard practice for the interviewer to read them out.

It has been decided that, to deal with English language difficulties, interviewers will carry information in appropriate languages to tell people that they can request an interview in their mother tongue. A second interviewer will then conduct the interview in that language. Unlike other surveys, conducting an interview using a family member as an interpreter is not appropriate in a survey that is assessing an individual's financial capability.

Applied financial numeracy

The applied financial numeracy questions were designed by staff at the FSA. They included questions intended to show whether people could extract information from bank statements, tables or graphs, and those questions that sought to capture their ability to make calculations, such as working out the monthly instalments on a Council Tax bill paid over 10 months rather than 12 months. On the whole, the first group of questions worked better than the second.

A number of people commented that 'calculation' questions altered the tone of the interview and made them feel like they were being tested by a school teacher. Some objected quite strongly to this, especially those younger people who were fazed by these calculations. These questions also often took some time to administer, and people were torn between giving a quick response and working out an accurate one. Many people needed to have the questions read out to them several times or were given them to read on paper. This suggests that a self-completion format might be preferable, although if people have limited literacy skills it will not be clear what is being tested. In real life, people would have access to pens and paper or calculators, and there is a strong argument to be made for mirroring this in the interview. The FSA has, subsequently, decided to drop the calculation questions from the questionnaire.

For the final rounds of testing, the remaining applied financial numeracy questions were placed towards the end of the interview and introduced as "like a quiz. But don't worry – it's not an exam."

We also tested the applied financial numeracy questions by asking first for a free response and then by giving people a multiple choice response. In both formats, a number of people were clearly guessing with no attempt to work out the response. This was more apparent with the free responses than with the multiple choice ones, where they usually had a one in three chance of being right. It would be possible to ask people how they arrived at their answer although this would complicate the analysis. Undoubtedly, quicker responses are elicited by multiple choice questions, but at the cost of a lack of accuracy of measurement.

5.1.3. Structure of the interview

The topic guide used in the first wave of interviews was divided into four sections, one for each of the four domains being studied – managing money, planning ahead, making choices and getting help.

Testing showed, however, that this is not always the most helpful structure for respondents. For example, information about levels of saving and borrowing (needed to assess ability to manage money) are better asked in a section dealing with product holding. Likewise questions on information seeking and use of financial advisers (part of the 'getting help' domain) are better dealt with when asking about recent product purchases. As a consequence, although the final questionnaire is still broadly structured around the four domains, these are no longer as self-contained as they were originally. In the sections that follow on the four main domains, we describe not only what information is being collected, but also indicate where in the questionnaire it is located.

5.2. Managing money

This section, more than any other, illustrated the general issues highlighted in the one-size-fits-all approach. Considerable time was spent to ensure that it included questions that were appropriate to people at the income extremes; identified and accommodated people with limited responsibility for money management; and, as far as possible, took account of the complexities of money management in extended families that are common in some South Asian communities.

In the first wave of depth interviews, most people had no difficulty at all in talking the interviewer through how they managed their day-to-day finances and, with some probing and prompting, it was possible to elicit details of the strategies they used. This generally gave a clear picture of the things that distinguished both very capable and less capable people from the rest. These included keeping account of money spent, knowing fairly accurately how much money is available to cover future spending, planning to deal with 'lumpy' expenditure, and living within one's means. Capturing the same information in a structured questionnaire was much more of a challenge.

5.2.1. Record keeping and knowing where you are with your finances

Individuals differed in the extent to which they kept an eye on their finances. Regardless of income, some knew accurately to within a pound or two how much money they had at any one time, others had only the vaguest idea. Some checked to make sure sufficient money was in their account before withdrawing cash or making a big payment; others did not. Some kept records and checked statements on their bank accounts to make sure that no errors had been made by the bank and to make sure that all payments had been processed; others merely skimmed statements or did not look at them at all.

On the whole, the questions in the questionnaire for the second wave of interviews gave an accurate picture of the extent to which people had control over their finances. Further refinement was, however, needed to ensure that this is also the case where people make little use of banking facilities, or rely on another member of the family to manage the money.

5.2.2. Planning for 'lumpy' expenditure

This area also clearly marked out the more capable people, who tended to plan and budget to ensure that they always had enough to cover regular expenses that were normally billed quarterly, annually or half yearly. The strategies used were very varied and this needed to be captured in a question with pre-coded responses. The least capable strategies involved borrowing (including using credit cards and overdrafts) and falling into arrears with regular commitments.

A complication arose with people who had high incomes and did not need to plan ahead, as they could absorb large occasional expenses, perhaps with a little pruning of non-essential spending. This has been addressed by adding extra pre-codes.

Again we have included a question to ascertain the extent to which the respondent is responsible for ensuring that money is available to meet this type of expenditure.

5.2.3. Living within one's means

As we have noted, the focus groups indicated clearly that someone should be judged capable if they balanced the books and incapable if they didn't, and either fell into arrears or routinely borrowed to make ends meet. But the focus groups recognised that this needed a caveat - that people living on benefits for extended periods of time may well have insufficient income to cover their basic needs.

Previous surveys have included a variety of questions to capture people's ability to live within their means, and all worked well. It was decided to approach this in a variety of ways, asking people about going overdrawn, running short of money and the strategies used to manage when this happens, as well as the total amounts owed in relation to income. It also included questions (in the 'making choices' section) about using credit cards to buy food and pay bills, but not settling the balance in full.

Again people on higher incomes posed a challenge as they should be able to meet all essential expenditure with a large margin. The distinction here was more subtle, with the least capable people regularly spending all their income and having none left over at the end of the month. In this context, it was also important to identify if people had taken on heavy expenditure on mortgages and discretionary commitments such as school fees. A question has been included towards the end of the questionnaire to capture this type of expenditure.

Information is also collected in the 'making choices' section to allow calculations to be made of total borrowing (in relation to both annual income and to savings and investments) and of repayments on mortgages and other credit commitments (in relation to monthly income). Finally, information is collected in the 'making choices' section on amounts saved, invested or paid off the capital on mortgages in the past 12 months.

5.2.4. Areas dropped following the depth interviews

A number of other areas were covered in the initial depth interviews but subsequently dropped from the questionnaire.

The initial interviews included questions about spending priorities and methods of bill payment, but the wide use of direct debits meant that this approach was not particularly useful as people were unable to assign a priority to bills paid in this way. And while a conscious decision to pay by direct debit could indicate a careful approach to money management, in other circumstances it was imposed by creditors after someone had fallen behind with bills. A further complication was the fact that direct debits were eschewed by careful money managers who had low incomes, who preferred the greater control offered by cash payments. And among cash budgeters, use of prepayment meters, like direct debits, resulted both from careful money management and from past financial difficulties.

The timing of bill payment (soon after receipt of income) was generally a good indicator of careful money management, but individual idiosyncrasies meant that it was difficult to capture in a quantitative survey. In any case, the timing was much less important for people who routinely had a large surplus income. It was, therefore, excluded.

The initial interviews also asked people how often they reviewed their levels of both saving and borrowing. But neither question elicited responses that added usefully to the assessment of their capability. The people interviewed did not operate their finances in this way and found the questions too abstract. For example, people were either minded to save and did so when they could, or they didn't. Many avoided borrowing altogether while others considered their level of borrowing in an ad hoc way when a purchase or house move was contemplated.

5.2.5. People with limited responsibility for finances

People who lived with a partner and relied on them to manage the joint finances posed a particular problem. As we have already noted, this was most acute in South Asian and Black African families where women often played no role at all in managing finances. It was possible to include questions to identify who these people were and the extent to which they relied on their partner. It was, however, more difficult to assess how capable they were personally the less financial responsibility they had. To some extent, the attitude statements helped to make this assessment.

5.3. Planning ahead

The initial depth interviews asked about a range of situations for which people might be expected to make financial provision. These included the following:

- Unexpected events (how people dealt with any they had experienced, and how they would deal with any in the future) such as:
  - an unexpected drop in income;
  - an unexpected rise in expenditure (tailored to their circumstances);
  - an unexpected major expense (also tailored to their circumstances); and/or
  - lost or damaged possessions.
- Anticipated events or major expenditure.
- Retirement.

This proved to be too long and repetitive and so for the questionnaire for the second wave of interviews it was reduced to four areas that provided the most useful information:

- An unexpected drop in income.
- An unexpected expense of £1,000 or more.
- Any areas of major anticipated expenditure.
- Retirement.

5.3.1. General points

Both waves of interviews demonstrated the importance of distinguishing between better-off people who have planned for such eventualities and those who have adequate provision by default rather than by design. Likewise the interviews showed the importance of being able to identify people on low incomes who would plan if they had enough money, and those who would not (and not penalise the first group for failing to make adequate provision). The questionnaire for the second wave of interviews needed further revision to capture this information more fully.

It was also clear from the replies people gave that it will, ideally, be important to check whether the same provision has been earmarked for a number of purposes, and whether or not it would be adequate to cover them all.

The ethnic sensitivity testing confirmed the need to take account of the fact that in some ethnic groups (and especially those where extended family households are common) the cultural norm is for families to support one another, obviating the need for specific financial provision for retirement or a drop in income. It is important that this is captured in the replies to questions, and just as important that it is taken into account in the analysis.

5.3.2. Unexpected drop in income

On the whole, few people had consciously considered what they might do if they had a large fall in income. More people could relate to becoming unable to work through ill health or disability than through redundancy. People with higher levels of qualifications or who worked in jobs where there was a skills shortage could not envisage being out of work for long, except through ill health.

With the general caveats already noted, it was possible to capture what provision people had made or considered and, if they had none, how they would manage to make ends meet. To assess its adequacy, we have added a question asking people how long they think they would be able to manage to make ends meet on the provision they have made.

5.3.3. Unexpected expense

In the first wave of interviews we tried to tailor the unexpected expense to people's circumstances, asking home owners about needing to replace the roof on their home, and tenants about needing to replace a washing machine and fridge at the same time. Non-householders were asked about needing to set up home at short notice. In the second wave of interviews we tried a different approach, asking instead about an unexpected expense of £1,000 or more.

On the whole, the second approach worked better, but would be better still if the sum were adjusted to take people's incomes into account. Accordingly, we have amended the question to ask about an expense 'equivalent to a month's income'.

Because the second wave interviews took a good deal more than an hour to complete, we decided to reduce this section quite considerably, and merely ask how people would manage to cover an expense of this amount.

5.3.4. Anticipated expense

The questionnaire captured expenses that people anticipated and any plans they had for meeting these. In the first two waves of interviews the questions were, however, more open-ended than those asked about other areas of financial planning. The information collected has enabled us to design pre-coded questions.

Following the second wave, questions were included that identify whether the provision made will cover all the cost and, if not, how any shortfall will be met. The ethnic sensitivity testing identified the need to include within the anticipated expenses those related to travel overseas for an extended period of time.

To reduce the length of the interview, it was decided only to ask about the provision that had been made for the expense that was likely to occur first.

5.3.5. Retirement

People were asked a different set of questions depending on whether they were retired or had yet to retire. For most of those interviewed this routing was unproblematic. It was, however, less clear-cut when people had either retired early or passed retirement age but continued to work. Where people had continued in the same job after the age of retirement they generally described themselves as still working, and for these the section for people who had yet to retire worked best. On the other hand, people who had retired (sometimes early) but had found another job variously described themselves as working, retired and retired but still working. Generally speaking, the section for people who had retired worked best in these circumstances. The questionnaire needed to identify and route these people appropriately.

People who had already retired were asked about the sources and adequacy of their income and, if inadequate, the reasons for this and how they had managed.

Those yet to retire were asked about private and occupational pensions, and other potential retirement income from investments, property etc. They were asked how confident they were that these would give them the standard of living they would like, although it was clear that a question in this format needed a lower age limit, which we have decided to set at 50.

The second wave of interviews identified the need to include questions on the number of years people had paid into personal pensions and any additional contributions they had made.

Women who relied on their husband's provision for retirement also presented a problem. We have decided to concentrate on the provision they have made personally, but to include questions to ascertain whether their partner has any pension provision and the role this has played in their own decision about pensions. We have also added a question to ascertain who, in the family, has mainly been responsible for ensuring they have an adequate income in retirement.

5.4. Making choices about financial products

This part of the questionnaire begins with a general section, to assess basic knowledge about financial products, attitudes to risk, confidence about selecting appropriate financial products, and the extent of trust of financial advisers. This section has remained largely unchanged from wave one. The second wave of interviews also included a module of questions on applied financial numeracy, many of which have since been dropped following the testing. As discussed earlier, the remainder have been moved to the end of the questionnaire.

It was decided early in the design that the bulk of this section needed to be tailored to the extent of people's involvement with the financial services market. For example, it would be inappropriate to ask someone on a very low income about complex investment products, or strict Muslims about credit or insurance. At the same time, it became clear that the interview could be very lengthy indeed for people who held a large number of products and we would need to find some way of restricting the ones that they were asked about.

Most previous surveys have solved this dilemma by asking people either about the product they took out most recently or about any they have taken out in the past 12 months. However, these surveys tended to concentrate on savings and investment products (including pensions and mortgages) whereas the present survey covers products of all kinds. Widening the coverage in this way meant that a high proportion of people would be asked about general insurance policies that were renewed annually. Moreover, we generally wanted to collect some information about each type of product held, as well as asking about purchases in some detail.

In the first two waves of interviews, the range of products held by respondents was assessed and respondents were routed to the sections of the questionnaire for the types of product they actually held, namely:

- current (including basic) bank accounts (but only if they had no other financial products);
- credit and store cards;
- loans and other fixed-term credit agreements;
- insurance;
- mortgages; and
- investments and savings.

In each section they were asked a small number of questions about the products they held and rather more questions about the most recent one they had purchased.

5.4.1. Monitoring products held

It became clear in the first wave of interviews that more searching questions were required about complex products such as investments, mortgages and protection insurance, as it was in this area that people on higher incomes would be likely to demonstrate their financial capability or lack of it. The questionnaire for the second wave of interviews therefore asked people holding these more complex products some more detailed questions: people with interest-only mortgages were asked what provision they had made for repaying the capital; those with protection insurance were asked whether and how often they assessed the adequacy of cover; while people with investments were asked how often they monitored their performance, whether they were likely to produce the return they wanted and, if not, whether they had increased the amount they had invested in the past three years. People who had invested in second properties were asked about their possible liability for Capital Gains Tax.

5.4.2. Choosing products

The early interviews showed that questions on purchases did not work for people who had not played an active role in selecting the product. This included people whose partners had taken a product out in joint names, young people whose parents had opened a savings account for them, people who had been given or inherited investments, and people whose employer had provided medical insurance. Consequently, the questionnaire was amended so that, in the second wave, people were only asked about purchases where they personally played a role in the decision making. No time limit was placed on purchases for the first wave in order to assess the most appropriate one to use. A five-year limit was subsequently used.

This was, however, one of the longest and most repetitive sections of the questionnaire, and ways were sought to reduce its length at each wave of interviews. So, in the second wave people were not asked about the purchase of savings products if they had bought an investment. Nor were they asked about the purchase of general insurance if they had bought some form of income or payment protection. Following the second wave of interviews it was decided to make further cuts and ask only about two purchases made in the past five years, and to ask about the most complex products people held. The order of priority used in the questionnaire is:

- investments;
- mortgages;
- payment or income protection;
- credit cards;
- unsecured credit;
- general insurance;
- savings accounts; and
- current accounts.

If further testing shows that the length of the interview needs to be cut even more then this may be reduced to asking about just one product.

For each product taken out recently, people were asked whether they had got any information or advice before selecting it, and the source of that information. This will almost certainly form part of the 'getting help' domain in the analysis.

They were asked who influenced their choice of product, and what features made them choose the particular one they did. They were also asked if they read the terms and conditions carefully before signing the agreement and, if they did not, whether someone else read them on their behalf. Questions were included in both of the first two waves of interviews to assess respondents' knowledge of key terms and conditions of products they had bought. There was some concern that we would not be able to verify the answers they gave to the questions on terms and conditions; however, the exploratory interviews indicated that people either knew the answer or (in the majority of cases) said they did not know. This was tested further, but the need to cut the length of the questionnaire meant that most of these questions were removed. Those remaining include questions about the interest rate on mortgages; unsecured credit and credit cards; whether, and how long, people would need to wait before claiming on protection insurance; and their assessment of the risk associated with investments (which will be compared with their earlier reply on the level of risk they are prepared to accept).

5.4.3. *Managing money*

This section also collected information about the amounts owed on mortgages, credit cards, loans and other credit agreements; the monthly repayments on these borrowing commitments; the amounts saved and invested; and the equity people had in any property they owned. These will be used to assess individuals' gearing and form part of the 'managing money' domain.

5.5. Getting help

Although the focus groups generally discussed information, advice, complaints and redress in the context of money management, planning ahead and choosing financial products, it was decided to create a separate domain that would bring this together. For short-hand this is called 'getting help'.

In the first wave of interviews this was included as a separate section at the end of the interview which covered:

- keeping an eye on changes in the economy and the financial services sector, how important this was considered to be, what was monitored and how, and any impact this information had on financial decisions;
- whether people had ever taken out a product and regretted it;
- what they would do if they made an unsuccessful claim on insurance, whether this had happened and what they did;
- what they would do if they were mis-sold a product, whether this had happened and what they did; and
- who they would contact for advice if their income fell and they got into financial difficulties.

5.5.1. *Keeping abreast of changes*

The section on keeping an eye on changes in the economy and the financial services sector has remained largely unchanged other than to turn open-ended questions into pre-coded ones. Respondents were asked how important they thought it was for people like them to keep up with financial matters generally, what they monitored personally, how they did this and how often. A question on any impact this information had had on their financial decision making was dropped as it proved to be too complex for a structured questionnaire.

This sub-section worked reasonably well, and showed that people monitored rather different things depending on their income and circumstances. This has been reflected in the pre-codes in the final questionnaire and needs to be taken into account in the scaling of replies.

5.5.2. Using information and advice

The first wave of interviews showed that some people on higher incomes had relied entirely on financial advisers and had not really made some of the decisions about their finances themselves. The topic guide had not captured this adequately and questions were added to the 'getting help' section of the questionnaire for the second wave of interviews. When tested these were found to be repetitive, and needed revising alongside questions on advice seeking in earlier parts of the questionnaire.

The questions used in the first two waves of interviews also failed to capture adequately the continuing relationships some people had with financial advisers, for example where they had an annual meeting which was initiated by the adviser. Nor did the questionnaire as a whole capture adequately people who relied on an adviser to manage their finances for them and played little active role in this.

Subsequently a small number of questions was added to the beginning of the 'making choices' section on more general use of financial advisers, supplemented by further questions on information seeking and the use of financial advisers linked to particular purchases.

5.5.3. Dealing with complaints

In the second wave of interviews, we were also asked to test a new set of questions on how people would deal with an error on a bank or credit card statement. This replaced the earlier questions on unsuccessful insurance claims.

So, the questionnaire for this second wave covered the following areas relating to complaints:

- Whether respondents had ever taken out a product and regretted it.
- What they would do if there was an error on a bank or credit card statement, whether this had happened and what they did.
- What they would do if they were mis-sold a product, whether this had happened and what they did.

These were rather repetitive, and the second wave of interviews indicated that they needed further revision and testing. Moreover, while the questions on what people did if they had experienced any of these problems worked, the more hypothetical ones on what they would do *if* they happened (or happened again) did not. Most people said that they would be willing to complain and to take things further if needed, while interviewers were left in some doubt that they would actually have done so.

The questions have, therefore, been revised to form a single section identifying whether, in the past three years, respondents have discovered:

- that they have been sold a financial product that is clearly unsuitable for their needs;
- an error involving £500 or more on a bank or credit card statement;
- an insurance policy claim for £500 or more that was turned down; or
- an error in the payment of state benefits or pension.

They are then only asked how they handled the first one in the list that they have experienced. This includes questions on whether they complained to the firm, whether they managed to resolve it with the firm, and, if not, whether they took the complaint further and who they contacted.

Everyone is then asked if they have experienced any financial difficulties in the past three years and, if so, whether and from whom they sought advice.

5.6. Developing a scoring system

Most of the work associated with developing a scoring system can only take place when sufficient data becomes available from the main survey. We can, however, set out the broad approach that will be adopted and the range of potential approaches that will be tested.

First, it is clear from the development work that there cannot be an overall scale across the whole questionnaire. When people discussed their self-assessment of their financial capability it was apparent that they did so in terms of the four main domains we have used. So people might think they were quite capable with regard to managing money but less so about choosing products. In view of this it seems appropriate to develop separate scores for each of the four domains.

Secondly, it would be inappropriate to have a 'pass mark', above which people are considered capable and below which they are not. This survey is not amenable to that sort of precise measurement as it is based on patterns of behaviour not individual questions with right and wrong answers. Moreover, the majority of people will almost certainly be judged to have very similar levels of capability, with only a small number of outliers - in particular at the least capable end of the spectrum. With such a flat distribution of replies, the differences between the mass of people who are clustered together are far too small to assess some as capable and others are not capable.

In determining the most appropriate approaches to test, we have adopted five broad criteria for the scoring system:

- **Reliability** – it should produce accurate output and have internal consistency.
- **Validity** – it should measure what it is intended to measure.
- **Relevance** – it should relate to the outcome being evaluated, with no bias for different income or ethnic groups.
- **Comprehensible** – it should be possible to explain the outcomes to a non-technical audience.
- **Longitudinal** – it should be possible to repeat the process in future surveys and compare the outcomes.

Turning now to the methods one might use to develop a score, three broad approaches have been used in other circumstances. The first approach would involve assigning a score to each question and adding these up to give an overall score for each respondent, which can be converted to percentages from 0 (worst financial capability) to 100 (best financial capability). This is the approach used in the *Skills for Life* survey (DfES, 2003). It has the advantage that it is simple and easily understood, but would be very difficult to apply to a questionnaire where the questions are mainly behavioural and few of them have a 'correct' answer.

The second approach is more complex, and similar to that used for predicting longevity of individuals, or for credit scoring to predict individuals' likelihood of falling into arrears. It would involve building models using regression analysis of the data to predict key outcomes, such as the ability to live within one's means, which would be used to develop a score measuring the risk of an individual failing to live within their means. This is a tried and tested approach, and one where the outcomes are well understood. Moreover it would be able to handle the behavioural questions used in the questionnaire. It would work well for some areas, where it is possible to identify an outcome that can be assessed, for example living within one's means. It is, however, more difficult to apply to other areas, such as information seeking, where it is difficult to identify a clear outcome that can be measured.

The third approach is similar to that used for the Index of Multiple Deprivation and Health indices. This method, like the other two, is robust and well tested. It is, however, complex and rather less easy to explain. It is based on factor analysis of the data with the results for each domain transformed to a normal distribution. The scores are then ranked from lowest to highest. At this stage, this approach seems best suited to the types of inter-related questions that are being used to assess financial capability in the survey. Building on this approach, further analysis can be undertaken to combine the assessments of the four separate domains for individuals. In this way it will be possible to build a typology of consumer financial capability that describes individuals' strengths and weaknesses. This could then be used to inform policy and practice for raising levels of financial capability.

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Appendix A: Testing for ethnic sensitivity

A1. Introduction

The development of the questionnaire was largely conducted amongst the majority white population. The FSA was concerned that the questionnaire may have an inherent cultural and religious bias, and could unwittingly 'downgrade' the financial capability of those from particular ethnic, religious or cultural groups. They therefore commissioned separate research to identify whether there are cultural and religious factors specific to certain ethnic or religious groups (or sub-sections of these groups) that should be taken into account either in the design of the questionnaire, in the management of the fieldwork, or in the analysis and interpretation of the data. This appendix reports on that research, namely on the pilot of the questionnaire amongst people from various black and minority ethnic (BME) communities, and on the adjustments that were made as a result.

This work was undertaken by Ethnos Research and Consultancy.

A2. Research design and methodology

The research was conducted in three stages:

- Literature review.
- Interviews with experts.
- Questionnaire testing with lay respondents.

A2.1. Literature review

A brief review of the literature on financial capability amongst people from ethnic minority backgrounds was conducted to identify the issues pertinent to the present study. In conformity with the work already carried out by the Personal Finance Research Centre at the University of Bristol on the key components of the concepts of financial capability, the literature review covered evidence in relation to managing money, planning ahead, making choices and getting help. Findings from the literature review were used as the basis for discussion in interviews with experts on ethnicity and financial capability.

A2.2. Interviews with experts

Fifteen interviews were conducted with people who had detailed knowledge and understanding of the different ethnic communities in the UK and who could provide information about the religious, cultural and social factors likely to impinge on their financial capability. The experts represented local voluntary sector organisations and Citizens Advice Bureaux, as well as financial institutions and financial advisers working specifically with ethnic minority clients.

A2.3. Questionnaire testing with lay respondents

The last stage of the research involved testing three sections of the questionnaire: introduction, money management and planning ahead. These sections were identified by the researchers conducting the main study with the general population as ones more likely to be problematic for BME respondents and in need of testing.

The approach employed to test the questionnaire was a “think aloud” procedure, whereby research participants were invited to comment on the questions in the very process of answering them. ‘Think aloud’ procedures are often used in questionnaire development to maximise the validity of the questionnaire. They help highlight difficulties in interpretation, misinterpretation, dissatisfaction with questions, and gaps, as well as cultural inaccuracies and insensitivities.

In testing for ethnic sensitivity, the ‘think aloud’ procedures focused specifically on the following:

- **Language and literacy** - whether respondents could read the questions in English.
- **Comprehension** - whether respondents could understand what the questions and response choices pertained to.
- **Relevance** - whether respondents thought the questions were pertinent to them.
- **Adequacy** - whether respondents felt the survey adequately captured ethnic, cultural or religious dimensions that may impact on financial capability.
- **Other issues** - whether there were any other issues that impacted on a respondent’s ability or willingness to answer specific questions.

As the development of the survey has been an ongoing process, we decided to divide the fieldwork with lay respondents into two stages. We first tested the questionnaire as it had been developed by the Personal Finance Research Centre for the general population. We then recommended some adjustments to the questionnaire to the Personal Finance Research Centre team. They incorporated our suggestions and we then tested the revised version.

Seventeen interviews were conducted with four Indian, five Pakistani, four Bangladeshi and four Black Caribbean respondents. Within each ethnic group, individuals were selected to represent those factors identified in the literature review and through expert interviews as likely to impact on people's financial capability. Thus, we had people who were recent migrants as well as those who were either born in the UK or had lived most of their lives here; people who were self-employed in a small family-owned business; people living in extended families; retired people; young people; and a mix of males and females.

Each interview lasted between 60 and 90 minutes. The interviews took place in areas where each ethnic group is concentrated. Thus, Indian people were interviewed in Leicester, Pakistani people in Bradford, Bangladeshi people in East London, and Black Caribbean people in South London.

A3. Findings

The literature review and interviews with experts both highlighted differences in the ways in which financial capability may need to be measured amongst people from various BME backgrounds. They identified a range of factors which may make ethnic minority households seem less financially capable than their white counterparts, including:

- poverty, unemployment and self-employment as part of their economic circumstances;
- traditional gender roles;
- extended-family households;
- lack of knowledge of financial institutions;
- difficulties communicating in English;
- preferences for other sources of finances;
- perceived discrimination against poorer households and against BME households amongst financial institutions; and
- additional lumpy expenditures

We discuss these issues in detail and identify the implications they have for the survey. It should be noted that the issues identified have implications not only for the design of the questionnaire but, importantly, for the way in which the full survey data will be analysed.

A3.1. Socio-demographic diversity

Before we provide a detailed discussion of our findings, it is important to highlight the great diversity that exists both within and between the different ethnic minority communities. Some of the key factors that account for this diversity are:

- national and regional origins;
- patterns of migrations (economic and political reasons for migration);
- length of stay and generation (degree of acculturation in the UK);
- economic circumstances and modes of economic participation;
- educational achievements;
- ability to speak, read and write English;
- religion; and
- cultural traditions (sexual division of labour, household size and characteristics).

To capture the specific experiences of people from ethnic minority backgrounds, and to ensure that the statistical analysis can isolate factors directly linked to ethnicity in seeking to understand financial capability, the demographic section of the questionnaire was adjusted to include information on such factors as ethnicity, country of birth, length of stay in the UK and religion.

Household size and characteristics

The size and characteristics of ethnic minority households vary a great deal as a function of national and religious backgrounds. South Asian (Indian, Pakistani and Bangladeshi) households are much larger than either white, Black Caribbean, Chinese or Black African households. The vast majority of South Asian households also include both parents and dependent children, and a sizeable proportion live in extended three-generational households. This has implications for the financial capability of some South Asians and needed to be taken into account in questions about who takes responsibility for various aspects of financial management. The standard housing tenure question was amended to cover people living with family members other than parents.

By contrast, about half of Black Caribbean and Black African households are headed by single parents (usually women) and very few live in extended households, although complex family patterns are often found due to multiple relationships. This may have implications for the financial capability of Black Caribbean and Black African people, but no specific implications for the design of the questionnaire itself.

Gender roles

South Asian and some Black African cultures are characterised by a much stronger sexual division of labour than is common in most Western societies; men and women have very different social and economic roles, with men being the traditional breadwinners and women being in charge of the private sphere. This division is particularly sharp among Pakistanis and Bangladeshis. In these two groups, women are less likely to work and less likely to be knowledgeable about economic and financial matters than either Indian women or all South Asian men.

This has implications for the survey to the extent that many South Asian women may be incapable of answering large sections of the questionnaire, and may find very many questions and response choices not relevant to them.

Language and literacy

Many BME respondents (especially more recent migrants and older people) found it difficult to answer certain questions because of the combination of:

- a lack of ease with the English language;
- the length and cognitive demands made by the survey; and
- a lack of knowledge and experience of the mainstream financial sector.

South Asians in particular had very limited knowledge of mainstream financial institutions. All questions requiring experience of professional financial services, rather than descriptions of domestic financial management practices, were more liable to misinterpretations. The 'think aloud' procedure also revealed that generic words such as 'financial products', 'financial provision' and 'financial services' are not readily understood. Respondents found it easier to answer in relation to specific products, provisions and services, such as bank accounts or mortgages, than in conceptual terms. This was evident in the many requests for clarification or for question repetition before respondents answered.

Even for those who were functionally literate in English, completing a questionnaire with many technical terms was taxing. Show cards with long lists of response choices were particularly problematic because respondents struggled to remember the various options before having to choose one. They often lost track of the original question they were meant to answer. In some instances, respondents felt disempowered as they became aware of the range of possibilities, but also realised that very few categories actually applied to their circumstances.

Issues of language and literacy have many implications for the entire survey design. They strongly suggest avoiding technical language wherever possible and simplifying or reducing the number of options on show cards.

Religion

Islam is the only major religion to take a position on finance. Under Islamic law, the use of interest is prohibited. Muslims are not allowed to benefit from lending money to, or receiving money from, anyone. Wealth can only be generated through trade and investment in assets and where risk is involved for both parties in the transaction.

There is no robust evidence on the number of Muslims who adhere or wish to adhere to this principle. Financial products, such as bank accounts and mortgages, that are acceptable under Islamic law are only just beginning to appear in the UK. Islam also makes it obligatory for every Muslim man and woman to pay, each year, two and a half percent of their capital ('zakat') to support poorer members of the community. While not all Muslims follow this religious requirement, it does impact on people's involvement with financial services and, hence the nature of their financial planning.

The role of religion needs to be considered when assessing Muslims' financial capability. The testing confirmed that the two harmonised Government survey questions on religion should be included, one asking which religion people followed and the other assessing how actively people were practising their religion.

A3.2. Economic circumstances

Despite some pockets of relative prosperity, many ethnic minority households live on a low income. Their spending, saving and credit use is likely to be similar to impoverished groups in the general population. This is particularly the case with Black Caribbeans. However, ethnic minority communities also differ from the general population in the following ways: levels of self-employment, circumstances in retirement, involvement in the informal economy, and types of 'major' expenditures. These are discussed in turn.

Levels of self-employment

Many people from ethnic minority communities (especially South Asian and Chinese people) are self-employed and work as part of small family businesses. All or most family members find employment within that business unit, but they may not be formally salaried. Moreover, incomes are often related to the turnover of the business in any given week or month. Thus the amount withdrawn from the business is irregular and variable. Ownership of the business is often unclear as it is owned by 'the family' which can include parents, children and grandparents. As all work in the business there is no main earner; often husband and wife will have equal share.

Self-employed people may have a business partner who deals with the finances and may not be able to answer some of the questions related to self-employment in the survey. For instance, questions on tax might not apply as some people might have informal arrangements with their business partners. Government harmonised questions on self-employed income have been developed to deal with these sorts of circumstances and it was decided that these should be used in the questionnaire.

Self-employment also limits people's ability to seek credit from high street lenders. As a result, some people turn to family and friends, as well as informal community resources, to meet their financial commitments.

Retirement

Older BME respondents are very likely to be first generation migrants, to speak little or no English, and to have little knowledge of and contact with mainstream financial institutions. Many of them will have worked as manual labourers in unregulated businesses for which they will not have received work-related pensions. Many will have earned so little that they simply could not save for their retirement or otherwise plan for the future. In all such cases, money management practices were targeted towards meeting people's most immediate and pressing needs. This has implications for the questions related to 'planning ahead', highlighting the need to differentiate between those who would not plan even if they could and those who would have done so, had they had the resources.

Some older respondents also felt that there was no particular need for them to plan ahead for their retirement. In some cases, this was because they were used to living on such small incomes that they did not think any adjustment could or should be made for their retirement. In other cases, this was because respondents (especially amongst South Asian and Chinese people) expected that their family would look after them in old age. Finally, some ethnic minority people really did lack financial capability and felt that they would benefit from greater knowledge of pension schemes. It confirmed that, to account for those relying on family to support them during their retirement, the question on the sources of income people plan to use when they retire needed to include the option 'financial support from family'.

Informal economy

Some people in receipt of benefits also have informal jobs. Although it is difficult to assess just how widespread this practice is, experts suggested that it is relatively common for Bangladeshis, Pakistanis and refugees to work informally in the catering trade, as taxi drivers or in family-owned businesses. This practice may be more common amongst ethnic minority communities, both because community infrastructures facilitate informal working practices, and because many do not have skills required by the UK labour market, speak little or no English, and experience discrimination in employment.

As a result of working informally, however, many people are unlikely to save money in institutions such as banks or building societies in order to avoid losing benefit entitlements. They are more likely to be using cash than credit. They are also more likely to keep their money in the home rather than in dedicated savings accounts. Wherever possible this has been taken into account in the questionnaire. It may have consequences in terms of people's willingness to take part in the survey.

Ethnic-specific expenditures

BME communities have a number of expenses related to keeping in touch with family and friends 'back home'. They are likely to make trips abroad either to visit relatives or to attend family occasions (attending weddings or funerals, or contributing to expenses related to those). On the other hand, there is no tradition of annual holidays, except with the new generations.

Many first generation migrants also send money to relatives abroad, regardless of their income levels. This seems more common in some communities than others, but it is mainly dependent on generational status rather than ethnicity.

Some people also have investments abroad. Amongst first generation migrants, this is often in anticipation of a return to their homeland, either because people choose to retire in their native country or because people fear that they may be evicted from the UK and forced to return.

BME people also plan to help their children and grandchildren, not only for their education but also to provide them with a good standard of living. This is particularly important for people from Indian and Chinese backgrounds. These additional financial commitments impact on their overall financial capability and, in some cases, can be seen as 'major expenses'.

Such considerations led to adjustments to the questionnaire. For instance, additional response choices were suggested to take account of ethnic-specific expenditures.

A3.3. Alternative sources of financial support

Some people from ethnic minority backgrounds access different sources of financial support compared to the general population. This seems to be due to a combination of factors: lack of knowledge of mainstream financial institutions; exclusion from mainstream financial institutions; and high quality social capital within some ethnic minority communities. In response to a lack of access to mainstream finances, alternative financial sources may be turned to such as loan companies offering credit at high interest rates. Such loan companies often target areas of deprivation. Given the disproportionate location of BME people in these areas, loan companies will have a large impact upon these communities.

Other sources of financial support are informal ‘clubs’, where people come together and collectively save money in an informal community pot. These systems are called differently by the various BME groups: South Asians usually refer to them as ‘committees’, while Black Caribbeans call them ‘pardner’ systems. These informal arrangements provide alternative ways of saving large sums and make it possible for people to plan ahead for ‘major’ expenditures or to cover ‘lumpy’ expenditures.

As such community schemes are common across the different ethnic minority groups (except Chinese people), the questionnaire needs to reflect these specific ways of obtaining financial support.

A4. Conclusions

Findings from the literature review, the expert interviews and the ‘think aloud’ procedures with lay people all revealed that the survey was broadly appropriate to most ethnic minority respondents, and the flow of questions is adequate. However, a number of issues emerged in relation to the design of the survey itself which needed to be taken into account to ensure that the survey did not discriminate against people from ethnic minority backgrounds.

Where required, the questionnaire was revised to reflect the specific circumstances of ethnic minority households in relation to socio-demographic variables (gender roles, language and literacy and religion); economic circumstances (levels of self-employment, issues to do with retirement, participation in informal economic activities and ethnic-specific expenditures); and access to alternative sources of financial support.

It is hoped that these changes will make participation in the survey less taxing and disempowering for ethnic-minority respondents. It is also hoped that the research will enable the FSA to draw more valid conclusions from this survey.

Appendix B: Focus groups topic guide

- I am a researcher from the Personal Finance Research Centre, an independent research centre at Bristol University. I have done a lot of earlier research on people's use of financial services, such as bank accounts and credit cards.
- PFRC is not a commercial company. Nobody will try to sell you anything as a result of your involvement in this research.
- We have been asked to carry out this research by the Financial Services Authority (FSA), which regulates most financial firms in the UK.
- The FSA wants to find out what it means for people to be 'financially capable', and in the future they want to try and measure the level of financial capability in the population as a whole.
- There are lots of experts who think they know what being financially capable means, but we want to get the views of the general public.
- So the aim of this discussion is to find out what you think it means for someone to be 'financially capable'.
- We are interested in hearing everyone's views. You should not be afraid to say what you think - there are no right or wrong 'answers'.
- Completely confidential. No personal information will be passed to anyone else; nobody else will know who has taken part in the research. Tape recording only to facilitate report writing

B1. Introduction

To start off, please tell me your name, age, and who else lives with you.

And from this list, can you tell me if you currently have any of these financial products or have had any of them in the past? (SHOW CARDS A AND B).

Describe your picture of someone who is ***not*** financially capable.

Describe your picture of someone who is ***very*** capable financially.

B2. Knowledge, understanding and skills

What are the basic things you need to know and understand about money and finances?

PROMPTS:

- How to budget
- Types of products and product features (small print)
- How to choose financial products and services
- Financial terms and concepts, e.g. inflation, interest, risk
- Where/how to get information, help and advice
- How to plan for the longer term, e.g. retirement
- Your rights and how to complain
- Other things?

Which of these is the most/least important?

B3. Other factors

Are there other factors that influence how financially capable someone is?

PROMPTS:

- Attitudes, e.g. interested/not interested in personal finances
- Personality, e.g. risk taker, organiser
- Upbringing, e.g. parental influence
- Experience of financial products and services

What if someone had all the knowledge and skills they needed, but did not act upon them? Would you still describe them as being 'financially capable'?

B4. Scenarios

In each case, ask the group to discuss whether the person is financially capable or not.

1. Mr and Mrs Jones were sold an endowment mortgage through an independent financial adviser. Ten years on, they have been told that they are likely to have a shortfall on their mortgage of £16,000.

2. Mr Smith owes £10,000 on his credit card. He regularly switches providers to take advantage of their 0% balance-transfer offers. In the meantime, he continues using his credit card and usually only makes the minimum payment each month.

3. Miss Atkins has an accident in her car on the M6. When she tries to make a claim on her insurance, she finds out that she is not covered while driving on a toll road.

4. Mr and Mrs Gordon have mortgage arrears of £6,000 and are only paying part of their mortgage each month. They take out a £5,000 home improvement loan from a finance company they saw advertised on TV, with a view to selling their house and paying off their arrears.

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