THE INDIVIDUAL'S SAVING DECISION

BUILDING SOCIETIES ASSOCIATION

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The Building Societies Association
is the trade association for the UK's building societies. There are 60 building societies in the UK with total assets of over £305 billion. Building Societies have over 22 million investing members and over two and a half million adults are currently buying their own homes with the help of building society loans.

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BUILDING SOCIETIES ASSOCIATION

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Executive Summary

The BSA commissioned GfK NOP to conduct research into what causes people in seemingly similar situations to come to different saving decisions. The main points and key conclusions from this research are set out below.

- The decision to start to save or to save more is made in advance of and separately to the choice of saving product
- More than half the people who currently save said a better return would encourage more saving
- Nothing could persuade about a third of people who currently did not save to start to save
- Some change in circumstances (excluding a rise in income) would be most important for a significant proportion of people to increase or start saving
- Almost half of savers thought high rates of return were the most important product feature. Flexible products were also important

Further analysis by the BSA - drawing on other published research - helps put these results in context:

- Behavioural economics helps us understand why people do not always approach the saving decision rationally. For example they lack self control, weigh losses as more important than gains, and make inconsistent choices over time. Viewing the saving decision as a trade off between the benefits and behavioural impediments of saving enables us to postulate as to why saving is such an individual decision. For example;
  - Differing responsibilities due to changing circumstances can alter how costs and benefits are perceived in this trade off
  - Financial capability entails a long-term outlook that enables better valuation to be given to future needs. The less financially capable someone is, the more relevant behavioural factors are to their decision and the more they rely on trust and word of mouth and proceed by trial and error. As financial capability rises, savers become more like "traditional" interest rate sensitive consumers
  - Alternatives to saving in deposit accounts, such as investing in housing or the use of credit, also impinge on the saving decision
- Effective saving products are likely to be simple and easily adaptable, requiring minimum effort from the saver. Desirable behaviour, such as setting up a standing order, could be encouraged via cash rewards or utilising savers' procrastination
- Financial education in schools should be made compulsory to try to instil some forward looking component in the financial decision making of future generations. The Child Trust Fund also represents an excellent opportunity to enliven this teaching
- Some sort of public awareness campaign is likely to be required to make adults stop and re-examine their current saving behaviour
- Regulation should be imposed on the saving market only where the benefit to the consumer is greater than the disincentive effect on saving behaviour.

Introduction

Existing research frequently comes to the conclusion that people fail to save because of limitations to their income. In savings research the instinctive response is often "*I can't afford to save more*" or "*I would if I had more money*".

However, some people save more and others save less, even if they are in similar circumstances and have comparable resources at their disposal. Therefore, it is a very individual decision. Rather than simply accepting a stated inability to afford to save as justification for low saving, this research aims to find out how and why people have come to that decision.

The BSA commissioned GfK NOP to conduct research into what motivates people to save. This incorporated interviews, workshops and survey questions. The research shows that the decision to save or to save more is made before the range of available products is even considered. Higher returns are the most important incentive for more than half of existing savers to save more, but for less than a quarter of non-savers. Many other factors are also important. Some change in circumstances (excluding higher income) is often required to make saving more of a priority. However, the greatest number of non-savers stated that none of the proposed factors could persuade them to start to save. When choosing a saving account, higher interest rates, as well as more flexible and easy to understand products are likely to be popular.

Models based solely on rational economics assume full, complete knowledge, with agents giving consideration to all relevant factors. In practice, this is likely to be too strong an assumption, especially in complex and uncertain areas like personal finance. Behavioural economics takes insights from psychology to give a more practical explanation of behaviour. By treating the barriers to saving proposed by behavioural economics as a cost in the saving decision, we can consider the saving decision as one of weighing the relative costs and benefits over time. These trade-offs may be judged with imperfect understanding, possibly subconsciously, and decisions may be inconsistent over time.

The numerous different influences on these variables help explain why the decision to save results in such diverse saving decisions. By looking at how these decisions are arrived at, it may be possible to influence the perceptions of the pros and cons of saving, in order to encourage a more adequate level of personal saving. Financial capability is found to be crucial to attitudes to saving, making people less reliant on trust, word of mouth and learning by trial and error.

Research Findings

The BSA commissioned GfK NOP to carry out interviews and workshops to explore the process people go through in deciding to save and the product features they value. From these discussions, questions were placed in an omnibus survey in October 2006 to try to determine which factors were most important to people.

What would make people save more or start to save?

We tried to find out what could encourage people to save more if they already saved, or to start to save if they did not. They were asked to rank which of the following factors would make them most likely to encourage them to save or save more in the future:

- Advice or recommendation
- A greater understanding or awareness of the benefits of saving
- A better rate of interest or return
- Simpler, easy to set up savings products and accounts
- A reward for commitment
- A change in needs or personal circumstances, for example, children, retirement, but excluding salary increases
- Or, None of the above

The table above right shows the factors favoured by savers and non-savers. Over half the savers ranked a higher rate of interest as most important, and this was the most important factor for almost a quarter of non-savers.

A change in circumstances was thought to be the most important factor to over one in five non-savers and almost one in six savers.

30% of non-savers said that none of the factors could persuade them to start saving. This was the first choice for the largest proportion of non-savers. A high proportion of these are effectively 'hard-core' non-savers. As noted in the discussion of the Saving Gateway pilots below, nearly a fifth of people cannot be persuaded to save, even when the government promises to double their money. The other choices all received relatively few votes as the most important factor. However, rewards for commitment and simplicity attracted substantial votes for second and third rankings.

Factor most likely to encourage more saving - % voting first choice

Rank	Savers		Non Savers	
1	Better Interest Rate/Return	**56%**	None of these factors	**30%**
2	Change in Circumstances	**16%**	Better Interest Rate/Return	**23%**
3	Simpler Products	**7%**	Change in Circumstances	**22%**
4	None of these factors	**7%**	Reward for Commitment	**6%**
5	Reward for Commitment	**5%**	Simpler Products	**4%**
6	Advice or Recommendation	**5%**	Advice or Recommendation	**4%**
7	Understanding Benefits of Saving	**3%**	Understanding Benefits of Saving	**3%**
8	Don't Know	**1%**	Don't Know	**8%**

A higher rate of interest is less important for young age groups compared to old age groups. A change in circumstance is relatively more important for younger age groups, as are rewards for commitment. Younger age groups are also less likely than older groups to state that none of these factors will encourage saving.[1]

A much greater proportion of the higher socio-economic groups ranked interest rate as most important compared to lower groups. For lower socio-economic groups a change in circumstances (excluding a rise in income) was important, but for the lowest socio-economic group the most common response (attracting 40% of first choices) was that none of these factors could encourage saving, not even a change in circumstances.

What are the most important product attributes?

The interviews and workshops indicated that it is only once the decision to save has been made that the product design is considered. The research tried to determine which product attributes are most important when choosing a savings account. Respondents were asked to rank in order of importance the following features:

- Flexibility
- Conditions on making withdrawals *(Note: This is partially the flipside of flexibility)*
- Easy to understand products
- Brand
- Better interest rate or return
- Advice or recommendation
- Or, None of these factors.

[1] See Appendix 1 for the full demographic breakdown of these results.

Almost half the savers ranked a better interest rate as the most important product feature, as did almost 3 in 10 non-savers. Flexibility and ease of understanding were also important to relatively high proportions of respondents, both savers and non-savers. Again a significant proportion (17%) of non-savers said that none of the product features would attract their attention.

Most important product feature - % voting first choice

Rank	Savers		Non Savers	
1	Better Interest Rate/Return	**48%**	Better Interest Rate/Return	**29%**
2	Flexibility	**17%**	None of these	**17%**
3	Easy to understand	**11%**	Flexibility	**16%**
4	None of these	**7%**	Easy to understand	**16%**
5	Conditions on withdrawals	**6%**	Brand	**4%**
6	Advice or Recommendation	**5%**	Conditions on withdrawals	**3%**
7	Brand	**3%**	Advice or Recommendation	**3%**
8	Don't Know	**4%**	Don't Know	**11%**

Flexibility attracted the greatest proportion of second place votes with 25% of savers opting for this, but conversely conditions on making withdrawals also attracted 17% of savers' second choices.

Flexibility was the most important attribute to a relatively large proportion in the middle age groups. Compared to older age groups, the young were more likely to rank ease of understanding and brand as the most important factor. None of the factors was the first choice for nearly 40% of the oldest age group, more than in any other age group.[2]

A better rate of interest was most important for a greater proportion in higher socio-economic groups, as was flexibility, except for socio-economic group AB where flexibility was relatively less important but advice was valued by a larger proportion than in other groups. Ease of understanding and brand were less important for higher socio-economic groups. Also, a greater proportion in lower socio-economic groups chose none of these factors above all others.

Discussions in the workshops revealed that safety of deposits was taken as given in saving products. Consumers disliked the impression that the institution was doing things with "their money" and preferred the saving side to be distinct from other operations. Simple products and easy to understand literature were appreciated. Respondents valued flexibility, but disliked too much choice with minor variations between the options. Some also favour being denied instant access to their money, but do want to be able to view the balance easily. Savers did not want ATM cards for their savings account, nor did they want the ability to withdraw from their savings account online, fearing they would make whimsical withdrawals. Rather than talking about earning a rate of return, many participants said they preferred the idea of being granted a reward for desirable behaviour, such as reaching a savings target or setting up a standing order.

A hierarchy of savers?

The BSA research reveals a possible split within those who save, with participants falling into two broad attitudinal categories.

Firstly, there were those saving for relatively short-term, functional ends. These people were saving for a specific purpose such as a holiday, wedding or house purchase. The short-term goal gives saving real value and purpose, making the trade-off between saving and consumption easier to negate. Indeed, the end objective is so valuable that these savers are very averse to making withdrawals along the way.

These savers tend to save irregularly, with the amounts varying considerably. They tended to be younger and more impulsive, and may stop saving after the objective is reached. This type of saving could be seen as a bridging point between not saving at all and regular saving for the longer term. As young, functional savers see that in practice saving need not have a radical impact on their lifestyle, saving without a specific target becomes more acceptable.

The second group save more for a rainy day or just the future in general, rather than a particular purpose. These people acknowledge the importance of saving. To a certain extent, saving becomes accepted as part of life, and the notion that it leads to missing out on other things is not considered. These savers tend to be older, or at least more mature in their outlook. These "committed" savers tend to save more regularly, in a more organised way.

[2] See Appendix 1 for the full demographic breakdown of these results.

An Internal Cost Benefit Analysis

The above results may be better analysed with reference to insights from behavioural economics. By considering the individual's decision as a trade off between the perceived benefits and costs of saving over time, our findings may help determine what causes one individual to weigh these factors differently from others.

The benefits of saving

Saving provides the individual with security and the ability to recover from shocks and emergencies. It allows individuals to plan future consumption with more certainty, and enables people to take advantage of a greater number of opportunities by loosening financial constraints. People can also afford luxuries, or at least afford more than the bare necessities. The roles for which saving is needed are likely to vary over a person's life. Attitudinally, participants in our research also reported a sense of achievement when they looked at the pot of savings they had accumulated.

These are broad benefits that arise whether saving takes place formally (such as in a saving account with a building society) or informally (in a jam jar, for example). Formal saving is also usually safer than informal saving, as in the latter the money could be stolen, get damaged or lost. Formal saving often provides the possibility of earning a return on savings. There is always the risk that deposits will not grow at a rate greater than inflation, but in a savings account paying interest, this is unambiguously better than informal saving that loses purchasing power over time.

Wider benefits of saving include the reduced cost to society as people rely less on state support in hard times. The government's provision of support has been scaled back in recent decades, and there is now a greater emphasis on people to save for themselves. Saving adds to the nation's capital stock and supports capital markets. The government has identified the benefits of individuals owning a financial asset, and this has prompted the development of schemes such as the Child Trust Fund and the Saving Gateway trials (see, for example, HM Treasury 2001).

Many government initiatives have attempted to influence incentives by increasing the benefit of saving, particularly by increasing the return on savings, but these are blunt tools that are difficult to target towards specific groups without distorting other behaviour.

SAVERS

> "It's quite worthwhile, I feel proud of myself. It's just a good feeling when you've got that amount there, as opposed to having to worry." **MALE, 22**

Savers feel that saving is rewarding, giving them a sense of accomplishment - admittedly not the strongest of positive emotions! Saving is seen as a priority, whether saving for something specific or just for the future.

NON-SAVERS

> "I just can't be bothered because so many other things are more important." **FEMALE, 38**

While it was seen to be commendable to have savings, saving was often a low priority or not even considered. Saving is seen as the preserve of the responsible, whereas non-savers considered themselves to be fun-lovers who lived for today.

In the first trial of the Saving Gateway the generous 100% return on savings did not persuade some of the 31% of people who previously did not save to start making deposits; more than half (18%) still did not make any deposits. Of course, this could be because they were in such poverty that any sacrifice would have been too great, or they were at some stage of life (unemployed, pensioner, etc) where it is more reasonable to draw down assets rather than try to accumulate them. But some of this 18% may have wanted to save, but never got round to it. Or they may have actively chosen not to make any cutbacks in their standard of living. And this was for 100% return. (In comparison, at the time of writing, the rate of interest on the best buy Cash ISA was 5.8% (incidentally this was at a building society, as were five of the top six best buys)). For 18% of people to turn down such a high rate of return, there must be some other factors that prevent them from saving, something that outweighs this significant benefit. It is to the impediments that impose a cost on the act of saving to which we now turn.

Impediments to saving

Looking at the inadequacy of personal saving in pensions, the Pensions Commission (2004) found that people were not rational or well informed, especially when there are complex decisions to be taken and long term consequences, as is the case with saving. In such settings, traditional economic assumptions of fully rational agents acting with complete information do not adequately reflect actual behaviour. However, developments in behavioural economics suggest a number of reasons why it can be difficult to save. These may apply to differing extents to different people, but any one person could be affected by several or all of these interlinked factors.

SAVERS

"I've got into a habit of being able to work it out; what's coming out,... where I get paid." **MALE, 22**

Although savers still admit they are confused by many terms and products, they have less fear and less of a sense of hopelessness than non-savers.

"I think with time you get more astute... you make yourself do things more and try and understand things more." **MALE, 48**

NON-SAVERS

"I've not really thought about it [saving] and I wouldn't know about where to start because there's that many different ways to save." **FEMALE, 38**

Many other non-savers stated that they never get round to saving as it is too complicated and time consuming. It is perceived as difficult and boring, so many do not ever seriously contemplate saving.

Lack of understanding

The FSA's Baseline Survey on financial capability (FSA, 2006) indicates the low level of understanding that exists in the UK today. This broadly-based survey looks at all socio-economic and age groups, and shows that people take on risks without realising it, do not compare products and do not appreciate the problems of failing to plan ahead.

One cost of saving is investing the time to understand the saving decision and the products on offer. This cost is considerable due to the complexity and long term nature of the saving decision, meaning that a large amount of time and effort must be spent to understand the personal value of saving and investigate the various options available. Also, as the decision is often a long term one, it is made only infrequently and it is not worthwhile to maintain more than a low level of awareness of the savings market and the options available. Therefore, each time the decision is made from a low base. Against this low level of understanding, some products are inherently complex.

People have great difficulty understanding risks, giving much greater weighting to a scenario they can envisage rather than weighting the likelihood and size of possible gains and losses.

The way in which information is presented can affect understanding because this influences how that information is absorbed, and so what action is then taken.

Loss aversion

People weigh losses much more heavily than gains, and will go to great efforts to avoid making a loss, but will exert much less effort to make a gain of the same magnitude. In combination with a misunderstanding of risk, people would often prefer to take a considerably lower return rather than a much higher likely return because there is also a (relatively small) chance of making a loss. If saving requires cutting back on consumption, this may be treated as a loss by the individual, who may then be expected to resist saving and prefer to continue to consume at current levels.

Lack of self control

People cannot trust themselves to save. One theory for this considers that the decision is made by different versions of the same self (Schelling, 1984): one who makes the initial decision, and the other who must act on the resolution. For example, the future self can desire a level of saving to support future consumption, but the current self must then forego some consumption now. This leads to the theory of "internalities" where one self can inflict harm on the other self and does not take this into account in its consumption decision. So the current self can over-consume and under-save now to the detriment of the future self. People can therefore make decisions at one point in time that are unwise even according to their own longer term values and preferences.

The individual's awareness of their own lack of self control can mitigate or exacerbate the problem (O'Donoghue and Rabin, 2001). For example, if they are aware that they will fail to save they can create some mechanism for committing to saving, or they may conclude that there is no point in saving at all, as at some later date they will yield to their whimsical demands anyway.

SAVERS

"I still had the life that I liked, did what I wanted to do, I still enjoyed myself ... I just cut down on a few of the little things, and all the little things added up." **FEMALE, 19**

Savers become accustomed to saving a certain amount, so do not feel like they are sacrificing anything.

NON-SAVERS

"We've got a holiday booked for January. If I was saving I wouldn't be able to afford that, I'd miss out on that experience of going on holiday with some friends and enjoying myself there." **FEMALE, 19**

Non-savers often have the perception that the choice is between saving and having an active life.

SAVERS

"If there is money [left] over then we'll put it away because there's always the temptation that if you, say, go out shopping or something and you think, 'Oh well that's lying there,'... you can end up spending it." **MALE, 34**

"That money, you know it's there, you know you can spend it, but what would you rather do at the end of the day, save it up for what you want or blow it?" **FEMALE, 19**

NON SAVERS

"I might think, 'Oh, I've got 50 quid in my purse, I'll go and open a savings account'. And then I'll... walk past a shop and I'll think, 'Stuff it, I'm having that'." **FEMALE, 34**

SAVERS FALL INTO THE ROUTINE OR HABIT OF SAVING, SUCH THAT IT BECOMES SECOND NATURE FOR SOME.

SAVERS

"I'm fortunate enough to... set up a direct debit and it's all dealt with for me, and if I've got anything left over and I don't need it then I'll invest that as well." **MALE, 35**

NON-SAVERS

"At present saving doesn't bother me that much because I know I've got like 60 years left ahead of me, in which case I can do it all then." **FEMALE, 19**

MANY, ESPECIALLY THE YOUNG, BELIEVE THEY CAN AFFORD TO ENJOY LIFE TODAY AND NOT SAVE. SOME SUGGEST THAT IN THE FUTURE THEY WILL BE MORE RESPONSIBLE, BUT OLDER NON-SAVERS CLAIM THAT OTHER PRIORITIES OFTEN SEEM TO "GET IN THE WAY" OF SAVING.

SAVERS TENDED TO ACKNOWLEDGE THE LONG TERM VALUE OF SAVING.

SAVERS

"In the future, if I was to ever have kids, or a family or anything like that, I'd like to have some money back and if I can get into a routine now, then hopefully it'll just stick, and they'll have the quality of life that I've had, and I can still do it now as well." **MALE, 22**

NON-SAVERS

"I think, 'Oh, next month, next month', and just never really get there... I'd rather have my nights out and not have the money at the end of the month." **FEMALE, 19**

THE IMMEDIATE BENEFITS OF A NIGHT OUT, FOR EXAMPLE, OUTWEIGH FUTURE CONSIDERATIONS. VIRTUALLY ALL NON-SAVERS STATED INITIALLY THAT THEY COULD NOT AFFORD TO SAVE. HOWEVER, WHEN PLACED IN CONTEXT, THE MAJORITY ACKNOWLEDGED THAT THEY COULD; NONE WOULD MISS £30-£50 TAKEN FROM THEIR ACCOUNT STRAIGHT AFTER PAYDAY. THEREFORE, OTHER ATTITUDINAL BARRIERS TO SAVING MUST BE PREVENTING SAVING.

Procrastination and inertia

People often put off the difficult and complex saving decision. There is some small cost in terms of time and effort to research, choose and apply for a savings account. Also putting off acting until next month as opposed to today has very little impact on the final value of the saved asset. However, next month when the decision is broached again, the same line of reasoning leads to saving being delayed until the following month, and so the procrastination continues indefinitely.

Schemes such as Save More Tomorrow (see Box 1) and the National Pension Saving Scheme in the Pensions Bill introduced to Parliament in 2006, use people's inertia to make them save by enrolling them automatically into the saving scheme. People then have to act to exempt themselves; many will not, so will be enrolled by default. Also, people will have to act if they would prefer parameters other than the default arrangements, and again, many will fail to act, even if they initially intended to do so (Madrian, B and Shea, D, 2001).

Inconsistency in impatience

The immediacy of the costs of the saving decision, compared to the distant benefits of saving are exacerbated when the individual's time preference is incorporated into the decision. People tend to place a greater value on things that they have now rather than things they will have in the future, so the value presently of something expected in the future is discounted. Traditionally the discount rate has been assumed to be constant: it is the same between period 1 and 2 as it is between period 101 and 102. Crucially, however, people are not consistent in the weighting they give to different time periods. The near term is valued very much more than the longer term, some estimate by as much as ten times greater (Laibson et al, 2005). For example, if people could have £100 in a year's time or £101 in a year and one day, most would opt for the higher amount. However if the choice was more immediate, such as £100 today or £101 tomorrow, many people would opt to receive the money today, and would get the smaller amount. This is the inconsistency of choices over time.

BOX 1
SAVE MORE TOMORROW (THALER AND BERNARTZI, 2004)

"Save More Tomorrow" is a saving scheme designed with the prescriptions of behavioural economics in mind. Under the scheme, employees at participating US companies commit themselves now to increase their savings rate at some point in the future. The extra saving comes out of an individual's future pay increase before it is passed on into take home pay. This builds on the various strands of behavioural costs outlined above, overcoming individual's improvidence. The structure of the Save More Tomorrow scheme is set out below.

1. Employees are approached about increasing saving well in advance of a pay increase. This avoids impatient time preferences.
2. If they join, part of the next pay increase goes to increase saving. This avoids loss aversion from cuts in current take-home pay.
3. Continues with future pay increases up until some preset maximum. This uses people's inertia to keep them in the plan.
4. Employees can opt out at any time. The increased flexibility makes people more comfortable to join.

In one trial over 80% stayed in the plan throughout four pay rises, the typical amount of time to reach the maximum contribution. Those in the plan ended up with much higher saving rates than other employees, more than tripling their saving rates in just over two years. Financial advice did boost the participation in the scheme, but was very costly. Save More Tomorrow works better than people outside the scheme who class themselves "eager to save", because these people suffer inertia and procrastination, and often do not get round to actually taking the steps to increase their savings, despite their good intentions. In contrast, Save More Tomorrow uses individuals' powerful inertia to commit to increase savings rates.

Such "hyperbolic discounting" can result in individuals making different choices depending on when the payback is expected to be received. Specifically, when people have to delay immediate consumption in order to save, or spend time investigating options, the discounted value applied to this sacrifice is very high. However, if they had to delay this consumption in some future period, the present value of the sacrifice would be much lower. Myopic decisions are made when the sacrifice must be made today.

The individual's decision

An individual computes the costs and benefits of saving, and discounts them to some present value internally, whether consciously or not. Whenever income is consumed or saved, the costs and benefits have been weighed and a decision has been made. We can interpret the research results in light of this, then look at how these perceptions might be altered so that more individuals come to the decision, preferably of their own volition, to save more and on a more regular basis.

There are risks in attempting to influence such decisions through universal policies (Whitman, 2006). Some people are already making the "preferred" decision and saving adequate amounts without any centralised attempt to adjust their incentives. Market-wide policies risk distorting the decisions of these individuals. Central policies may also overlook or misinterpret some of these internalised incentives and the policy would not have the desired effect. Finally, the heterogeneity of individuals means that a "one size fits all" policy may incentivise some to save too much and others too little.

Interpretation of Research Findings

We can now interpret the findings of the research from the perspective of a trade-off of the benefits of saving against the behavioural impediments, as outlined in the previous section.

Interest rate or rate of return

Over half, 56%, of savers (compared to 23% of non-savers) ranked a higher rate of return the foremost factor that could persuade them to save more. Existing savers are likely to respond to a higher rate as they have already overcome the behavioural impediments to save, so an increased benefit would be expected to be the most important factor, as it increases the benefit at the margin.

This is what "traditional" economic theory would suggest is most important – that people would respond to a greater monetary return. However, we know this is not the whole story. There are currently some very attractive interest rates on the high street and many people still do not save, and nearly one in five turned down a 100% return in the first Saving Gateway trial. Besides, the FSA's survey of financial capability (FSA, 2006) shows that 49% of savings account holders could not estimate the current rate of interest on their account. Interviews in the BSA-commissioned survey also indicate that many people do not know what rate of interest their savings earn. If people don't know what interest rate their savings are earning, it is difficult to see how they can distinguish what is a "good" rate of interest. By ranking a better rate of return first it could be that people are saying "The reward I can get for more saving is not enough to compensate me for the sacrifices I would have to make", as opposed to requiring a extra few basis points onto the best buys. That other factors were also chosen first shows the prevalence of behavioural factors in the saving decision.

In terms of encouraging more saving, rate of return was considerably more important for those in socio-economic group AB (54% compared to 36% across the other groups on average), who may be expected to have higher incomes. This is likely to be because as income rises, financial constraints become looser, in particular those around necessities bite less often and it is easier to overcome behavioural impediments. Also, on a small savings balance, even a high rate of interest yields a small absolute return. Therefore, lower socio-economic groups might be expected to be less responsive to higher interest rates than those who might be assumed to have saved larger amounts.

Change of circumstance

A change in circumstance could be relevant if people really are living on limited resources. For example, for those in unemployment a new job might lead to significant changes. However, as this category explicitly ruled out a change in income as the change in circumstance, this factor would not alter financial constraints so would not have been chosen by most for this reason. Choosing a change in circumstances as a factor to make you save more indicates that these people do ultimately acknowledge the benefit of saving. In their present lifestyle, they have chosen to prioritise other things above saving but accept this might change in the future. The demographic splits show this was a high ranking factor for the young and for non-savers (for whom it was almost as popular a first choice as interest rate).

This is because a change in circumstances such as buying a house or having children could make an individual reappraise their responsibilities. In our interviews, young people tended to focus on their own current situation and lack of responsibility, and saving was unimportant. People who were married or had children often thought less personally. According to GfK NOP's Financial Research Survey data, young couples and families save more, on average, than young singles (FRS 12 months ending June 2006). Older people often looked ahead to their preparations for retirement. Saving then became a higher priority.

"Well if I had £50 I could think, I'll put that away or I can go out, I'd just go out because that's more fun" SINGLE FEMALE, 34

"But obviously since having a child, that makes you put things into more perspective because you've got to look at their future and where they are going to go and what they are going to do." MALE WITH FAMILY, 35

"I think it's much more of a necessity now, especially with the way forecast financial climates are, you've got to think about tomorrow" SINGLE MALE, 48

Saving is often mentioned in similar terms to stopping smoking or going on a diet. Everybody knows it would be good for them to stop smoking, eat less and save more, but all of these things are often difficult to do. To give up smoking, for example, the motivation must ultimately come from the individual themselves. Often a change in personal circumstance forces individuals to reappraise their responsibilities, and look at the various choices they make in a different light. For example, becoming a parent can radically alter the perceived cost of smoking in the home as the smoke will also affect the new child.

The term "savings habit" is often used as something desirable to acquire. In fact, it might be more accurate to refer to a "consumption habit" that people should try to kick. Like eating too much or smoking, it is far more enjoyable to indulge now than abstain for the benefit of the future. The common comment that "I cannot afford to save" actually reflects the outcome of an internal mental analysis. When a person's situation changes through their life, the relative costs and benefits of saving can alter, sometimes radically. Approaching retirement, for example, can bring home that in a few years' time income will fall, and encourage action. Saving then becomes more important, and is valued more than some other area of consumption, where a sacrifice is then made.

The different weighting people give to the costs and benefits of saving is exacerbated by differing reactions to changes in responsibilities. Some people decide now is the time for them to start saving, just as some people decide now is the time to go on a diet or to stop smoking. Only when an individual's mind is fully convinced of the benefit of saving, or the harm of failing to save, will behaviour change.

Psychological factors

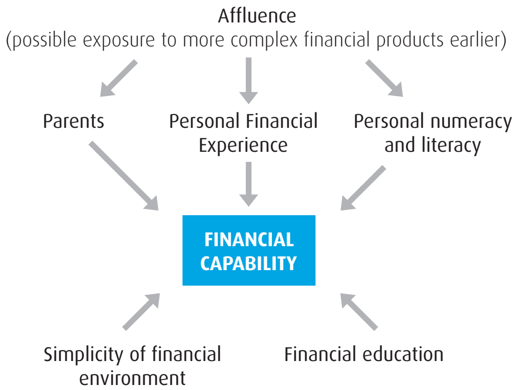
A recent paper looking at a case study in a South African credit market examined the effectiveness of product attributes that could be described as operating on the take-up of products at a "psychological" level (See Box 2). The authors state that preferences are constructed, not merely revealed, during their elicitation. That is, the context in which the financial decision is made, the way information is presented, and the actual options available all influence the outcome of the decision.

The results from the survey show those that may be reasonably assumed to be less financially capable, such as the lower socio-economic groups and younger age groups, place greater weight on factors such as ease of understanding, brand, advice, face to face contact[3] and so on, which corresponds with this research on psychological factors. The authors propose that psychological manipulations weaken the price sensitivity of demand either because they make an individual less price (interest rate) sensitive, or they attract a higher proportion of people who are less price sensitive into taking up the product. Our results would seem to suggest the latter. The less financially capable reach the limits of their financial comprehension, and fall back to trust and trial and error, and are therefore more susceptible to psychological attributes. The more financial experience, and the more financial capability people have, the more they are like "traditional" interest rate sensitive consumers.

Low financial capability means reliance on a greater number of personal beliefs and rules as people can only be rational to the extent that their cognitive capabilities allow. As a result, it is no surprise that savings decisions made under identical circumstances can yield such diverse results, as people revert to personal values and heuristics, where people learn by a process of trial and error.

Influences on an individual's financial capability

It is difficult to examine the determinants of personal financial capability without making substantial generalisations. However, it can be reasonably assumed that financial capability is broadly improved the more experience an individual has in dealing with financial products and financial institutions. The FSA's baseline survey states that "*Experience counts in choosing financial products: the number of different types of products people have bought is by far the best indicator of how well they choose, and much stronger than income, for example.*" (FSA, 2006). The FSA also finds that the young are much worse at choosing financial products. How quickly this experience is absorbed depends to some extent on the individual's own numeracy and literacy. Much research highlights the important role of parental attitudes to finance and saving in shaping the saving behaviour of their offspring (see for example Kempson et al, 2006). All of these factors could be expected to be affected by the individual's background. If the individual's parents were well off, the parents are more likely to have saved, and their offspring are more likely to have higher degrees of numeracy. If the individual is well off they are more likely to get exposure to a wider variety of financial products earlier, so gaining valuable experience.



Education specifically in financial matters should also raise capability. The level of financial capability that is necessary is determined by the simplicity of the financial environment. This also works the other way - developments in financial capability enable a market to evolve for saving product features that are more useful yet more innovative or complex.

As financial capability increases, the costs of the saving decision identified by behavioural economics and psychology reduce. The need for trust and reliance on trial and error and rules of thumb diminishes. Procrastination, inertia and hyperbolic discounting become less accurate descriptions of financial behaviour as people give greater consideration to their long term future, and better analyse their own behaviour.

[3] GfKNOP's FRS data shows that 80% of 16-20 year olds save via face-to-face contact in branches. This compares to 63% of 25-34 year olds and an average of 68% across all ages. (GB, 12 months ending June 2006)

BOX 2
WHAT IS PSYCHOLOGY WORTH? (BERTRAND ET AL, 2005)

Although based on a trial with a loan product, the insights from this case are also likely to be applicable in savings markets. The features of the trial are set out below.

A South African micro-lender lending to the working poor (so likely to be financially illiterate) sent direct mail solicitations to former clients with product offers that differed along a number of characteristics:

1. Rates ranged from 3.25% to 11.75% per month – The cheaper loans were more popular.
2. Example repayment options were presented describing single monthly repayment or a menu of repayment options - The simpler descriptions were found to have a strongly positive effect on take up.
3. Comparison of offered rates, stating the gain or loss using different representative units – Framing the loss is powerful when expressed in terms with which people are familiar (eg. Pounds per month rather than percentage points).
4. Subtle demographic features such as photos which deliberately matched or mismatched the recipient in terms of race and gender - Race had no effect, a female photo had a positive effect on male recipients.
5. Promotional giveaway (unrelated product, eg free clock radio) – Counterproductive; thought to be a trick or costly gimmick.
6. Suggestion effects (suggested uses for the loan, pre-letter phone calls) – Suggested uses did alter the use of the loan, and pre-letter phone calls a had positive impact.
7. Mentioning that they spoke Zulu had no effect
8. Merely describing the rate as "special" had no effect

The results showed that on average, any successful psychological manipulation had an effect on product take up equivalent to half a percentage point reduction in the monthly interest rate charged on the loan. This is therefore a very significant influence on take up. Positive psychological attributes have an additive effect, so two factors are twice as strong as one.

The psychological features appear to have a larger effect when used with less favourable offers. Indeed, worse offers attract customers who are relatively less savvy financially, but these customers cannot be distinguished in terms of income or education. New product features and departures from the status quo require more psychological justification.

The authors acknowledge that the impact of psychological effects is very context specific.

Conversely, the collapse of the Christmas savings company Farepak shows how the dependence of those with low financial capability on psychological factors can have dire results. This scheme relied on trust as it was often close friends or family who introduced the scheme to the savers and collected the regular contributions. These savers were not aware that saving schemes like Farepak are not subject to the stringent regulation that applies to building societies and banks, so they were in fact taking a greater risk with their money.

Alternatives to saving in savings accounts

The decision to save in a savings account is not made in isolation. The individual weighs up the relative costs and benefits of other forms of saving and investment, such as equities and property. Also, some will see credit as a solution to their short term consumption demands, when historically people may have saved in advance.

i) Housing

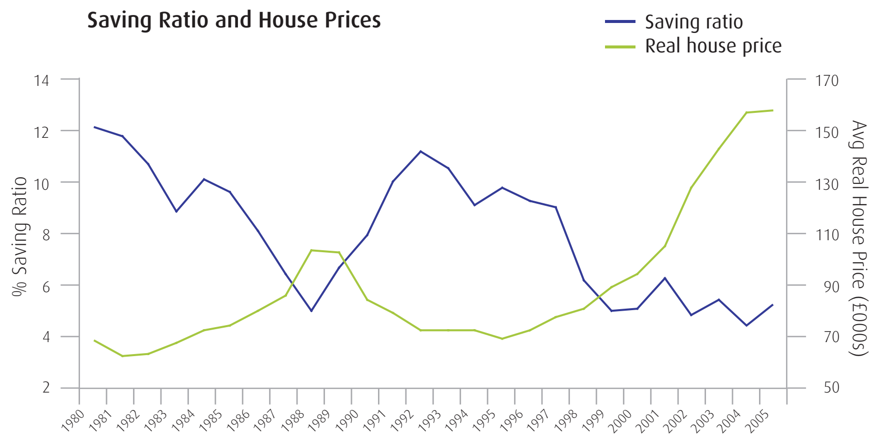
House prices have risen continuously for over ten years. For some, this has become accepted as the nature of the housing market. As such, investment in housing, including paying off the mortgage, is a form of saving. A survey by the Association of British Insurers (2006) showed that 70% of those interviewed thought property was the best long-term investment. The wealth effect from rising house prices means people may deem that they need not engage in other forms of saving. Research looking at household saving when house prices fell in the early 1990s compared to the period of house price growth at the end of that decade found that yearly household saving reduced by £28 for every £1,000 rise in real house prices (Henley & Disney, 2002). Young homeowners in particular reduced saving as house prices rose, consuming an extra £105 for every £1,000 extra of housing wealth.

The chart below shows how as real house prices have risen in the UK, and therefore housing wealth has increased, the saving ratio has been depressed. There are, however, a number of other important influences on the saving ratio including consumer confidence when inflation and unemployment are expected to be low, easier access to credit, and the wealth effect stemming from rises in the value of shares.

Wealth effects with housing are believed to be stronger than with equities (see for example Case et al, 2005). In terms of the internal saving decision, the benefits of saving can be realised by remortgaging or moving house to release the equity. The behavioural impediments are then of secondary importance. The costs of saving in this way then include the risk that prices will fall, or the risk that the lack of liquidity of the asset should hinder a response to a short-term emergency.

ii) Credit

A decline in savings penetration in the last five years has been mirrored by a substantial rise in the debt to income ratio. Greater availability of credit diminishes the perceived role of saving. Readily available credit



might be particularly attractive to the short-term "functional" savers identified earlier. Rather than save up in advance for a specific goal, such as a holiday or a car, it is now easy to buy this on credit. If this functional saving is a stage which some people go through to become more committed savers, the availability of credit may be hindering this progress.

Credit accentuates the problems from hyperbolic discounting as it enables the lure of immediate consumption to be satisfied using credit. The repayment of this loan is in the future, so is valued much less than the immediate consumption. In our research, many people complained about the ubiquitous advertising for loans and credit cards that fuel this culture.

BOX 3
THE HOUSEHOLD BALANCE SHEET (ONS BLUE BOOK 2006)

Looking at the aggregate household balance sheet highlights the importance of housing to household wealth.

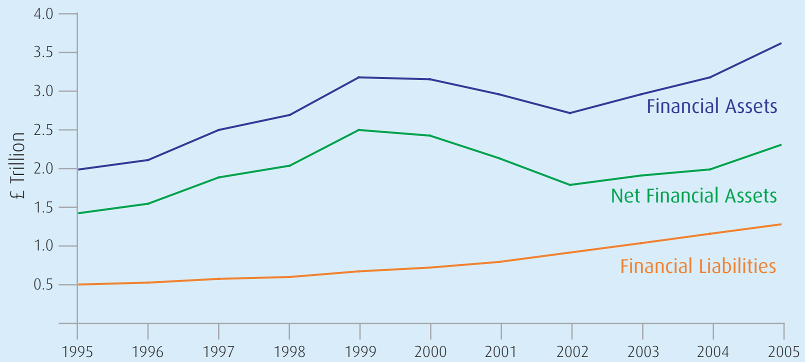
Financial Assets

Since the end of 1995 financial assets (excluding tangible items such as housing) have grown by 82% to over £3.5 trillion by the end of 2005. Deposits held with building societies and banks have become relatively more important in recent years, accounting for a quarter of household financial assets in 2005, compared to 18% in 1999.

Liabilities

Borrowing by households has also increased since 1995, growing by 141% to almost £1.3 trillion by the end of 2005. Over three quarters of this relates to mortgages and most of the remainder was short-term unsecured borrowing. Net financial assets represents all households' saving less all their borrowing. This grew by 60% in the ten years to the end of 2005, or an average of 4.8% per year. Therefore, despite a rise in borrowing, households were considerably wealthier in 2005 than ten years previously. This is also despite falls in the value of equities reducing the value of net financial asset holdings from 2000 to 2002.

Financial Assets and Liabilities 1995 - 2005

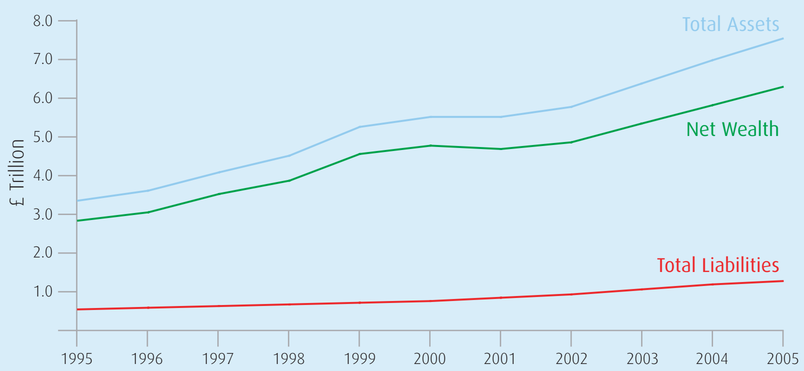


BOX 3 Continues over leaf...

Housing Assets

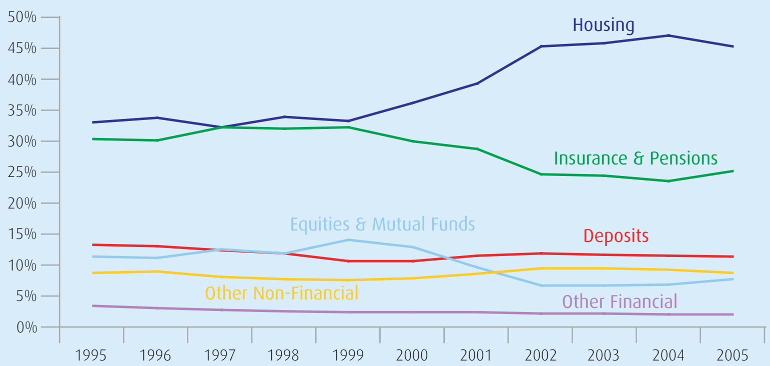
The value of housing held by households has more than tripled since the end of 1995 to £3.4 trillion by the end of 2005, a rate of increase much greater than the growth in the value of mortgage debt. Including housing assets in the calculation of household net wealth (Financial and non-financial assets less all liabilities) shows further how household wealth has increased in the decade after 1995.

Household Wealth 1995 - 2005



Housing has therefore become a much more important part in a household's portfolio of assets. Whereas it accounted for only around a third of assets (32%) at the end of 1995, by the end of 2005 this had grown to 44%. This change is shown in the chart below.

Components of Total Household Assets 1995 - 2005
% proportions



Therefore, in aggregate UK households are considerably more wealthy than ten years ago, even though borrowing has increased substantially over the period. This would suggest the media attention on household indebtedness may be overstated at the aggregate level, although a number of individual households could be in this situation. However, research by the Bank of England (BoE, 2006) showed that it is those with the largest asset holdings who also hold the greatest proportion of debt.

Liquidity versus commitment

We saw from the preferred product features that after interest rates, flexibility was a popular product feature. This is likely to reflect a desire for savings that are easy to access. In addition, conditions on withdrawals was a relatively popular second and third choice. While it is not possible to determine from our results whether these are different groups of people or the same individuals choosing apparently conflicting product attributes, other evidence suggests that the trade off between liquidity and commitment is a difficult one to balance, especially for the poor.

Without problems of self control, it would be optimal to have fully liquid and flexible savings deposits so people can easily react to shocks, but would not react to temptation. Commitment products will also only ever be a sub-set of savings products because they appeal mainly to people who are aware that they have little self control. Many people will not have consciously considered whether they do or not.

MicroSave is an organisation that studies microfinance schemes that assist saving in some of the poorest people in the world. It finds that in many cases the poor exhibit strong "illiquidity preference", valuing the structured commitment saving mechanisms that prohibit them from withdrawing in response to trivial needs and allow them to fend off demands from relatives (Wright, 2001). This enables them to make longer term savings. However, the poor are also more likely to need to access their savings in emergencies, as they are more likely to suffer income shocks, become ill, get divorced, and so on.

MicroSave suggests that products to meet the needs of the poor would allow small, variable amounts to be deposited with quick access to funds, but also have a contractual component for planned large expenditures.

Ashraf et al (2006) conducted a trial of a commitment saving product in a Philippines bank. The commitment is not to withdraw until an agreed date or an agreed total has been reached, as opposed to a commitment to regular saving. Those who chose the product tended to exhibit hyperbolic discounting and were aware of their self control problem. Over a twelve month period, the balances in the commitment accounts grew considerably more than the control group (by an extra 81 percentage points).

Commitment mechanisms necessarily require conditions to be added on to the terms of the accounts. This needs to be balanced not only against flexibility, but also against simplicity and ease of understanding.

The prevalence of "None of these factors"

In the survey, when people were asked what would be most likely to persuade them to save more, the choice of "None of these factors" was chosen by around 1 in every 5 respondents, implying that factors such as a higher rate of return or simpler products had no persuasive effect on their saving. There are of course some people who really do not have the resources to save, but it is unlikely to be as a high a proportion as a fifth of the people in the UK. This result suggests a deep rooted apathy with regards to saving. This raises the same question as the 18% who did not participate in the first Saving Gateway trial and passed over the very generous pound for pound match, a 100% return. Either people do not understand what they are turning down, or they perceive the value from their current saving behaviour to outweigh the rejected return. Choi et al (2005) attempt to understand why people do not take "free money". As well as liquidity constraints (which could include those in retirement and students who we may not expect to save) or the disincentive of early withdrawal penalties, they also state that there are significant behavioural reasons, such as procrastination, as discussed in the earlier section, and these "costs" tend to be stronger in the less financially literate. Such people do not respond to the provision of advice either. Educational and monetary incentives alone will not be effective in increasing saving, especially in those who are less financially capable. A wider range of factors need to be considered.

Recommendations

Having considered the results from the survey in light of other relevant research into incentives to save enables recommendations to be made on the design of savings products and public policy more generally. This section suggests some ideas.

Product recommendations

Rate is important, but not everything

Marketing is often based on interest rate alone. While this is the attribute ranked first by the greatest proportion of people, it is not the only important factor. It attracts prospective savers' attention who then investigate, but who may then be put-off by the other features. Still, the most successful product design is likely to offer a competitive rate.

Given that a significant proportion of people are currently quite financially illiterate, building societies and other financial providers do need to make their products as simple and flexible as possible. This includes terms and conditions with minimal jargon, but also processes that are straightforward and well explained from the saver's point of view.

Many of those interviewed stated that they wanted products that could be tailored to their needs. Of course it would be very costly to produce products where every variable offered was altered for each individual saver. This request reflects a demand for products that are easy to adapt, enabling savers to respond easily to changes in their life. However, a large choice between minor variations is not valued by savers.

The more providers can do for their customers, and the more that can be automated without loss of flexibility, the better, as this negates consumers' procrastination. Processes need to be frequently reviewed to ensure there is no duplication of effort required of savers.

Encouraging desirable behaviour

Product design, including the whole process of setting up and making changes to accounts should bear in mind the importance of behavioural and psychological factors. For example, building societies could make it easy to set up standing orders. This could help mitigate the commitment and self control problem by encouraging regular saving. Many people in workshops suggested there should be some reward for desirable behaviour, such as setting up a standing order. This is likely to be because a reward helps overcome the procrastination. Furthermore, the results from the study into psychological factors mentioned above signify that the reward should be in terms that people understand. This implies the actual pound difference that it will make to the individual, rather than the additional basis points on the interest rate.

GET £10!

Simply set up a £20 standing order for 12 months and we'll give you £10!

Tick here for us to set up a standing order for £20 a month from your current account ☐

If you would prefer to pay in more, enter the monthly amount here: ____________________

If you don't have a current account with us, please give us the details for the account from which to draw the money:

ACCOUNT NO. ____________________

SORT CODE ☐☐ ☐☐ ☐☐

SIGNED ____________________

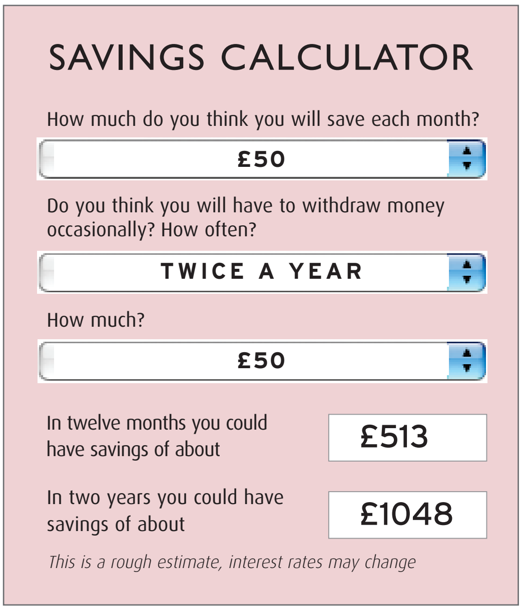
Inertia means that people are unlikely to prompt themselves to cancel or amend this standing order. People would tend to stick with a suggested amount (within reason). In fact, inertia may be so strong that with each annual statement, it may be possible to recommend that the amount collected by standing order be increased by 5% a year, for example. The account's annual statement could contain a tick box to return to the society. In a similar way to the enrolment in the Save More Tomorrow scheme described on page 11 that takes advantage of people's inertia and procrastination, the default on this option could be that the increase will take place unless the saver specifically takes the action not to increase the standing order amount.

Furthermore, to use people's loss aversion against them, rewards could be framed as an opportunity that could be missed rather than a bonus that can be earned.

Presenting the savings products on offer

Building societies should emphasise the security of savings deposits they hold and try to present savings operations separately from mortgage and lending operations to accentuate the distinction in the saver's mind.

In the same way that many mortgage providers provide online calculators to estimate the monthly mortgage cost for different loan terms, savings calculators could be used. These could make it simple for potential savers to judge realistically what they can expect after saving for a period and help them envisage a savings target. These should also emphasise the gains, and suggest uses to try to create some sort of goal in the saver's mind.



To encourage the "functional" saving where there is a specific purpose, people could be allowed to compartmentalise their savings. For example, part of the balance could be labelled "Holiday savings", and the account remains the same in all but name. This might be easiest to do with internet accounts. Research prior to the Saving Gateway trials also found that people engaged in this sort of compartmental saving (Kempson et al, 2005). Renaming accounts or parts of the balance may help engage savers as it helps them associate saving with their objective. Those engaging in "functional" sorts of saving may also value penalties on withdrawals as an added incentive not to touch their money. Conversely, more "committed" savers may appreciate occasionally being able to make a withdrawal without penalty.

Liquidity versus commitment

An alternative way round the liquidity-commitment problem discussed above would be to have an account with some sort of minimum deposit balance. As people start to save the account is fully flexible, allowing instant access to deposits. However, once some threshold value, say £500, is reached, £250 of the total balance can only be accessed with a notice period, such as 60 days. Balances above the £250 limit can still be obtained with instant access. As saving continues, and in moments when they are thinking of their long-term futures, savers could request that the threshold be raised, much like requesting an increased credit limit on a credit card.

Such a design has a short term element for dealing with emergencies, and a long term element that can be adjusted to help commitment to saving in the longer term. However, this design could easily get complicated. Increased financial capability is the only ultimate solution to complexity but, paradoxically, a more financially capable consumer relies less on product features to commit to saving.

Public policy recommendations

Simplicity alone is insufficient

Speaking at the 2006 BSA Annual Lecture, Peter Vicary-Smith, Chief Executive of the consumer body Which?, suggested that providers of financial products need to simplify their products so that they are more easily understood and compared. However, the extent to which product information can be simplified is subject to compliance with regulation. A side effect of money laundering regulations, for example, may be to burden prospective savers with a prohibitive amount of paper work, with loss aversion amplifying the value placed on the effort required. The introduction of new regulation in the UK is subject to cost benefit analysis, but it is important that in considering regulations that impact savings accounts, the full costs, including the added complexity that decentivises savers, are taken into account. Furthermore, the BSA's research shows that by itself, simplifying products is not enough to encourage more saving. The decision to start to save or to save more is taken before the range of available products is even considered.

Financial education

The government's role in welfare provision has been scaled back and there is greater reliance on individuals to provide for their own future. However, one reason that the government supported people in the past was that they could not be relied upon to provide adequately for their own future – they over consume now to the detriment of their future selves. The detriment also spreads wider, as personal under-provision also leads to a greater reliance on state support in hard times. Better informed consumers also lead to a better functioning market.

The government needs to tackle the low levels of financial capability in the country, educating individuals in what is required of them to fill a gap that they were previously deemed incapable of filling by themselves. Current work by the FSA's National Strategy for Financial Capability is in the correct direction, but financial education needs to be a compulsory part of school curriculum to have a real impact on capability in the longer term.

The government has a central role to play in the provision of financial education. State provision can ensure that all groups are included and attention is not focused on more profitable groups while others are excluded. This would also remove any problem of vested interests and the suspicion that information is allied to promotion. In the workshops, participants said that they would be cynical of information from providers and would be more likely to pay attention to the same information provided by the government.

Links with the Child Trust Fund (CTF) are likely to be a fruitful way of bringing this financial education to life. As the CTF develops over time, and children begin to use the accounts to make deposits themselves, there is a real opportunity to enhance understanding of basic financial products at an early and impressionable age. It is important that particular effort is made to involve the less well off.

Changing current perceptions

People need to be made to think seriously about their future. For current generations who do not save adequately, a public awareness campaign could be instigated. If consumption is a habit, and people are storing up harm for their own futures, they need to be made to reappraise the costly consumption in which they are now engaged. Higher consumption tax would be too extreme and hurt those who currently make adequate savings. In a similar way to stop smoking campaigns that use stark images of a harsh future, such as showing a person who has lung cancer after a lifetime of smoking, shock tactics could be used to make people take another look at the life they currently lead. Difficult or challenging imagery is needed to make people stop and think consciously about the decisions they are making that affect them in the medium to long term.

Positive imagery needs to be used carefully to promote the benefits of saving without reinforcing the "live for today" attitude that tempts people to opt for credit as a quick fix. As one participant in our research stated, "Pictures of new cars and holidays are not going to make me save, it's going to make me take out another loan".

The perceptions of those who currently don't save need to be challenged if their behaviour is to change. This is to show that saving is not difficult, it is important, and can be rewarding via the peace of mind it provides. Furthermore, it is not something only done by the affluent. The Saving Gateway can help to make this point to the less well-off, but the scheme needs to be carefully designed. This is discussed briefly in Box 4.

The provision of free financial advice announced by Ed Balls, the Economic Secretary to the Treasury, in January 2007 could help reduce some of the barriers to saving, but the impact may be limited. The scheme has been

BOX 4
THE SAVING GATEWAY

The Saving Gateway scheme aims to develop a savings habit in those who don't currently save. The main incentive is that every pound saved is "matched" by a contribution from the government, up to a limit. The results from the first trial are encouraging as they show that participants that were converted to saving came to understand the benefits, were more confident, and realised they could in fact afford to put money aside each month. However, the BSA research shows that more than a high rate of return is required to get non-savers to start saving.

The account needs to be as simple as possible to aid understanding. Reference to rewards should be in pound terms, as it has been in the trials. The pound for pound match has a simplicity that is advantageous in explaining the scheme.

The designs of the scheme being tested encourage commitment by allowing withdrawal of only one month's contribution before the match is irrecoverably reduced. It will be interesting to know whether greater flexibility in order to respond to emergencies is valued highly.

Marketing could focus on the total possible match, and what could be achieved with such an asset. Importantly, it should also represent this as a prize not to be missed, to maximize the incentive from loss aversion.

The choice of the product into which the balance transfers on maturity is important as inertia means that most will end up with the default option. The wrong default could undermine the positive effects from the Saving Gateway scheme.

More detailed recommendations on the scheme design can be made when the final results of the second trial are published in 2007.

allocated a relatively small budget and the information provided will have to be fairly generic. Crucially, however, it requires people to seek it out. It does not force them to stop and look again at their financial decisions, so will be valuable only to those who have already decided to take action.

The act of saving is itself never going to be "fun". In fact it is likely to be the very opposite as it requires the foregoing of current consumption, but also an investment of time and effort to understand and research the available options. But as long as individuals neglect the discomfort they are storing up for the future by not making adequate saving, the decision between current consumption and saving is incomplete. Individuals need to be persuaded to want to save more.

Conclusions

The decision to save is ultimately a very individual one. The challenge to increase the amount that is saved is to inspire people to actively want to save. At the most basic level this requires greater financial capability and a wider appreciation of the benefits of saving. For many people, this means challenging current misconceptions regarding the act of saving, such as it being the preserve of the rich and the boring. Saving need not mean radical lifestyle changes, but it does require a longer term outlook that is difficult to instill in individuals.

Given the levels of financial capability in the UK today, financial products should be made as simple as possible to ease understanding. While interest rate is the most important stated factor in terms of the amount of saving and product choice, it is not the only factor. Psychological and behavioural attributes are important impediments that should also be addressed in creating attractive saving products and policies. The less financial experience someone has, the more psychological factors such as trust and rules-of-thumb are important. Experienced savers tend to behave more like "traditional" interest rate-sensitive consumers.

As saving is influenced by so many factors that are a product of an individual's social and cultural context, any recommendation that is applied universally is likely to be a blunt tool. Coercing and enticing people to save is just as likely to distort behaviour, causing a rearrangement of assets rather than any new saving. The best long-term solution is likely to be educating people so that they want to save.

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Appendix 1 – Further Research Results

General saving behaviour

Most simply, approximately half (49%) of those questioned had made some deposit into a saving account in the last year. The demographic splits also yield unsurprising results. The proportion that save is the lowest in the youngest age group at 34%, rising steadily to around 60% in the 45-54 and 55-64 age groups. The proportion that saves in the 65+ group then drops off as more of these people can be expected to reduce their wealth in retirement. Again unsurprisingly, those in higher socio-economic groups save more, with 70% of those in the AB category having saved in the last year, compared to only 27% in the DE category.[4] Out of those in full or part time work, 55% had saved in the last year; 31% of those in unemployment had.

DEMOGRAPHIC BREAKDOWN: THE BREAKDOWN ACROSS AGE GROUPS AND SOCIO-ECONOMIC GROUPS FOR FACTORS TO ENCOURAGE MORE SAVING IS SHOWN BELOW:

Relationship with age:
%age voting first choice

Relationship with socio-economic group:
%age voting first choice

4 Socio-economic group AB includes people who are employed in higher and intermediate managerial, administrative and professional roles, DE includes semi-skilled and unskilled manual workers, low grade workers, the unemployed and those on state benefit.

THE BREAKDOWN ACROSS AGE GROUPS AND SOCIO-ECONOMIC GROUPS FOR DESIRABLE PRODUCT FEATURES IS SHOWN BELOW:

Relationship with age:
%age voting first choice

Relationship with socio-economic group:
%age voting first choice

Appendix 2 – Research Methodology

The research was carried out by GfK NOP Financial Research. The first stage of the research was a basic analysis of findings in GfK NOP's Financial Research Survey that interviews 60,000 respondants each year. The data was collected during the 12 months to June 2006. This informed hour-long in-depth discussions that were held with ten individuals by telephone. Two workshops were also held to generate a discussion about saving and product design. Half of the people recruited for these discussions and telephone interviews were savers, and half were non-savers. The age groups questioned were 16 to 34 and 35 to 55 years. There was also a split between those who had a family and those who were single or with a partner but had no children. Participants came from socio-economic groups C1, C2 and D.

The samples for the telephone discussions and workshops excluded those in groups where saving penetration tended to be greatest: the wealthy and those in the oldest age groups. This was to try to focus on those who are at the margins of the saving decision, so for whom the points raised in the questions resonated most strongly.

The telephone interviews and workshops were held over two weeks commencing the 25 September 2006.

Following the results of the interviews and workshops, three questions were submitted to the GfK NOP Omnibus survey. Interviews were conducted in respondents' homes with a (CAPI) laptop computer. 985 people took the survey between the 12 and 17 October 2006. Respondents were adults aged 15+, and were from all socio-economic groups. The answers were weighted to reflect the actual proportions in the UK population.

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