The Financial Health Check

Helping People Build a Stronger Future

Summary

For many of us, saving money is a lot harder in practice than in theory. At the end of every month, after bills and the expenses of daily life, it can often seem like there's very little left to put aside for a rainy day. In fact, only a minority of Americans - 40% according to a recent survey - have the funds in reserve to support themselves for a minimum of three months. While this endemic lack of saving can be seen in all sections of society, the consequences of not having a financial buffer most strongly affects those with low incomes, who often don't have as much access to credit and traditional banking services. In the event of unforeseen financial shocks like a medical emergency, car accident, or loss of employment, they're often forced to cut back on other essentials, or take out high-interest loans that can trap them in debt cycles.

Ongoing attempts to drive an increase in savings have resulted in the widespread use of 'financial literacy' and coaching programs as a means to increase financial capability. However, evaluations of these information-based training programs have shown mixed results when it comes to actually increasing savings rates.

That shouldn't come as a surprise - insights from behavioral science show that providing more information doesn't always translate to taking action. With this in mind, ideas42 partnered with the Financial Literacy Center and the Social Security Administration to design and pilot-test a comprehensive, in-person "financial health check" (FHC) program as an alternative to traditional classroom-style training.

Previous research has demonstrated that common behavioral limitations such as forgetfulness and limited self-control play important roles in determining our financial behaviors. So rather than give clients a bevy of financial information and a list of steps to be completed after the coaching session, we encouraged recipients to take positive actions - such as signing up for automatic transfers and text message reminders - while still in the coaching session. We hypothesized that this would be a more effective way to deliver financial advice and could lead to increased savings rates.

After a small, initial experiment with a credit union in the Pacific Northwest of the US, using a population of members who opted-in to the new program, we found that FHC recipients with no savings at the credit union had 21% more savings at the end of the study period than the control group. Our results demonstrate the potential of the FHC as a supplement to traditional counseling programs, as well as the potential to develop an even more effective financial-coaching approach that incorporates behavioral enhancements into financial education programs around the world.

Defining the Problem

People of all income levels have trouble saving money, but the potential fallout from financial emergencies and unforeseen expenses disproportionately harms middle- and low-income individuals. A recent report from the Pew Charitable Trusts found that the majority of American households (55%) can replace less than one month of their income through liquid savings. The situation is even worse among low-income families, where a typical household has the equivalent of less than two weeks' worth of income in checking accounts, savings accounts and cash at home.

Managing day-to-day finances in a manner that could enable better savings behaviors is complex, and often outside the reach of most people without some form of support or instruction. For the wealthy, this typically comes in the form of expensive money management professionals. Low- and middle-income households ought to have at least the same level of banking services as the rich; they may even need more, but what they commonly have access to is nothing like the private banking services available to the wealthy.

In recent years, there has been substantial work in developing financial capability training for low- and middle-income households through the form of classes, workshops and counseling sessions. But research on what actually happens after these sessions shows little to no behavior change (Lynch & Netemeyer, 2014). Studies have found evidence that people do learn in these classes, and a few even suggest that they do their "homework" (O'Rourke, 2010). However, many other experiments show that financial education has no ultimate effect on financial behavior (Saez, 2003; Mandell & Klein, 2003).

Problem Diagnosis

In financial literacy programs, educators teach concepts and may help consumers make a budget, but most activities take place after the class. Consumers must then leave to open savings accounts, pay off debts, or cut up credit cards: actions that can be complex, daunting, and often tedious. Some credit counseling agencies offer full financial service, but only if consumers need remedial help digging out from under a mountain of debt. The rest of the financial advice available to them is just that—advice.

People may forget to act when they have only a vague plan and no reminders to take their intended action at the end of a financial literacy session. Small hassles, such as physical distance from the bank, difficulty in accessing their account, or other similar situations may deter them from action. Furthermore, temptation or more pressing daily stresses may divert their attention from their longer-term financial wellbeing.

Usually, the low impact of these financial literacy programs is diagnosed as arising either from a lack of interest and motivation from attendees, or from a shortcoming of the material being covered in sessions. Curriculums are then retooled with an aim to increase the number of sessions people attend or to make the material more comprehensive. But when we make financial literacy curricula more comprehensive and rigorous, we are implicitly assuming that people will be able to process large amounts of complex information quickly and effortlessly. Research in behavioral science has shown this is not true, and that a person's cognitive resources at any given moment are finite and exhaustible—particularly in situations of financial stress. Increasing the cognitive demands of financial literacy programs may in fact make them less effective and unlikely to help people act on their intentions.

Instead, building financial literacy programs around taking concrete actions that will tangibly improve financial lives, rather than simply providing more information, may be a more effective route to promoting financial literacy and responsibility. We set out to design a coaching approach that would help credit union members have more tangible impact on their financial health and take action to build savings, while being cost-effective and sustainable for providers.

Intervention Design and Testing

The Financial Health Check program was conducted during a personalized hour-long, in-person meeting. In the treatment session, a financial coach helped participants pay down credit card debt, identify and meet their savings goals, and schedule on-time bill pay to reduce late fees and penalties. Just as in a traditional financial coaching session, time was devoted to understanding and using a monthly budget, balance sheet, and credit report. However, in the FHC session, the informational portion was completed quickly with approximate figures instead of taking the entirety of the hour. At the end of the initial informational assessment, the coach asked the client about their goals for saving and debt management and recorded them in a worksheet.

Depending on the client's situation, the coach also made specific recommendations such as suggesting clients with little savings take steps to build up an emergency fund.

After the financial review and goal-setting exercise was completed, the coach used the rest of the session to set up various transactions and action steps to help clients actually reach their goals. For clients who wanted to save more, the coach helped them set up automatic savings transfers.

The most intuitive barrier to following through on our intentions is forgetting. If participants were not prepared to sign up for automatic savings transfers or payments during the session, the coach provided them with the option to receive regularly scheduled email or text message reminders to save or pay their bills throughout the coming months. In doing this, the coach asked the client to make a verbal commitment to save a specific amount. Additionally, clients experiencing difficulty managing their credit card use were given the option to leave their cards at the credit union - to be returned to them upon request - as a physical barrier to future spending.

The FHC was tested at a credit union in the Pacific Northwest of the US. Operational and randomization challenges within the existing infrastructure of the credit unions prevented a fully randomized evaluation. However, the results of the initial pilot were promising. Two years after it was rolled out, individuals who received the FHC were nearly twice as likely to have accumulated savings of $500 or more compared with similar individuals who did not receive the FHC. Within the treatment group, 28% had saved $500, while only 16% of the control group had saved $500. Similarly, 19% of the treatment group had saved $1,000 or more, compared to 13% of the similar group of individuals who did not receive the FHC. This suggests that the FHC may have prompted more people to follow through on their intention to save, or encouraged them to save a larger amount.

Lessons for the Future

The Financial Health Check demonstrated the potential of using small, inexpensive behavioral interventions to increase financial capability. Three important insights gained from the initial phase of the FHC are important for informing future work in the financial inclusion space.

Firstly, we saw a low uptake of automatic savings transfers (just 5%), which we believe stemmed from discomfort among clients about losing even a small amount of control over their financial affairs. This contrasts with the nearly one in five who signed up for automatic savings reminders, which allowed them to retain control. Second, uptake of the FHC treatment session was limited by the ability of clients to attend an in-person meeting. During the course of the FHC, we experimented with other potential delivery channels, such as conducting the session over the phone. This appeared to be effective, and could provide a pathway to scale the FHC in future work. Finally, building in more checkpoints to monitor the randomization process with future partners could prevent limitations on data and results analysis.

Among the other takeaways from this project, an increase in savings balances among participants in the initial Financial Health Check pilot demonstrated that we have the potential to multiply the impact of financial counseling and education with just a few, simple changes to existing programs. Using behavioral insights aimed at bridging the action-intention gap, we can ensure that consumers follow through on all the good advice they get from counselors and instructors, and achieve measurable improvements in their financial health. .