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# Feedback on Everyone Needs a Savings Buffer

Good Shepherd Microfinance welcomes the opportunity to respond to the Everyone Needs a Savings Buffer consultation paper. As leaders in promoting financial inclusion and resilience in Australia, we are committed to our purpose of enabling economic wellbeing for people with low incomes, especially women and girls. Global research clearly demonstrates that having a savings buffer is an important prerequisite for the ability to cope with financial shocks/developing financial resilience - we therefore look forward to further discussion on this important topic.

Our feedback detailed below responds to the questions laid out in the consultation paper.

**Section 3.2**

1. **Are there other changes or other elements that would support take-up of a savings buffer option amongst target consumers?**

It is our view that the take-up of a savings buffer option amongst our target consumers would be increased when it is supported with both a financial conversation and a supportive pathway enabling individuals to translate the intent to save into positive and ongoing savings behaviour.

Good Shepherd Microfinance sees financial conversations as a means of providing support, relevant information and positive reinforcement for our clients. The financial conversation generally takes place when an applicant attends an interview for a No Interest Loan Scheme (NILS) loan or a low interest loan (StepUP). It can also apply for applicants of our other programs, including AddsUP, our matched savings program delivered in partnership with NAB, and Debt Deduct, a pilot program offering no interest debt consolidation loans to people on low incomes with the support of financial counsellors. Research recently published by Good Shepherd Microfinance on the impact of the NILS financial conversation has found that these conversations have a positive immediate impact on each component of the applicants' financial capability, and that ~~that~~ applicants leave the financial conversation with increased confidence and fresh strategies for managing their finances[1].

We also believe that that consumers seeking support for debt repayments, particularly those on low incomes, would equally benefit from this type of financial conversation. This view is supported by a

[1] Randrianarisoa, A., & Eccles, K., (2016) Pathways to resilience: The impact of financial conversations on the financial capability of NILS applicants, Good Shepherd Microfinance, Melbourne

program evaluation of the Victorian pilot of Debt Deduct, which we undertook 2014. A Debt Deduct loan is only available to clients who have first received assistance from a financial counsellor to ensure they have a financial conversation catering to their specific requirements around credit and debt matters with people qualified to discuss and negotiate debt on their behalf. A number of clients in our Victorian pilot reported a vast improvement in financial wellbeing indicators and financial capability and we are now piloting the program in South Australia. Based on this research, it is our view that discussing the importance of a savings buffer during the financial conversations could lead to an increase in the up-take of a savings buffer option, particularly for people on low incomes.

Building financial capability and resilience, in addition to providing knowledge and enhancing skills also requires behavioural change. We support the recognition in the discussion paper that consumers are more receptive to behavioural prompts at specific life events, such as when they are evaluating their financial situation. It is therefore important to ensure that a simple, easy and streamlined process is in place to ensure that those consumers who wish to take up the savings buffer are supported in making this intention to save into a reality. This may include support in setting up an appropriate no-fee, interest bearing savings account and also setting up a regular direct transfer, allowing clients to 'set and forget' their savings buffer until they need it. Uptake of a savings buffer may also be increased through offering some form of reward or incentive, such as a higher interest if savings are deposited on a regular basis.

**Section 3.3**

2. **Is 10% or $20 a reasonable amount?**

We would welcome more information on the foundations for establishing a savings amount of 10% or $20 per month including how these were calculated and if the 10% is considered to apply to disposable or total income.

The Money and Advice Service in the UK responsible for improving debt advice services suggests that 'some advisors, particularly those working with very low income and benefit dependent clients questioned the feasibility of their clients being able to save 10 pound per month, or 10% of the available income[2]. We are concerned that this could be equally true in Australia where people who are already in debt, and in a position where their income is less than their outgoings, may struggle to have excess cash to spare each month. We suspect this would be particularly true for those in debt who are receiving the Newstart allowance of $263.80 a week, which we believe is insufficient to cover the costs of living.

We are also concerned that $20 per month (i.e. $240 per year) may not be sufficient to build a savings buffer large enough to cover unexpected expenses. Recent research commissioned by Good Shepherd Microfinance into the use of payday loans indicated that the average loan size was per household was $611, with approximately 30% of those with payday loans having more than one concurrent loan within the year[3]. We recognise that whilst saving $20 per month would have a positive impact in building financial resilience and capability, it would likely not be enough to cover the unexpected costs that drives people to predatory lending services.

[2] The Money Advice Service. (2015) The Standard Financial Statement: Emerging Themes from Responses to the Consultation, Money Advice Service, London
[3] Digital Financial Analytics (2016) Women and Payday Lending, Good Shepherd Microfinance, Melbourne

Recognising the complex issues involved, we do see the importance of developing innovative ways to support people on low incomes to overcome of these challenges and the benefits in developing a savings buffer and positive savings habits. Therefore setting a target of 10% could be a reasonable starting point provided there was evidence to support this. In addition, it would be important to allow flexibility to adapt this allocation depending on individual circumstances and monitor the impacts of the savings-buffer approach to better understand ways that people can build their financial capability and become more financially resilient.

3. **Should there be a limit to the amount that consumers repaying debts can save?**

In most cases there will be an interest rate charge on debt that the customer is repaying. Therefore we would suggest that economic modelling is conducted to understand the tipping point at which someone is better paying off more on their debt than having increased money in savings. Although we have not conducted research into this optimum level we believe it could be linked to research requirements for access to emergency savings and noting that the ABS uses a benchmark of $2,000.

A clear understanding from the client's perspective would be required for them to make an informed decision around delaying debt repayment in favour of building a savings buffer. People need to be aware that paying back their debt while adding money to savings will increase the length and cost of their debt.

If it is possible to evaluate people's behaviours we would suggest not setting a fixed limit in the first phase of amending the financial statements, instead evaluating what actions consumers have made during a trial period. Likewise, it will be important to note any psychological outcomes that occur as a result of changed behaviour, specifically if people feel positively or negatively about having a savings buffer relative to paying off their debts quicker.

4. **Should there be controls on when and how the consumer can withdraw funds from the savings account and on how they can be spent? If so, who should oversee these controls?**

Without having conducted any study on this topics, we would be inclined not to support establishing controls on accessing the funds. The very premise of encouraging people to establish a rainy day fund involves the understanding that the needs and circumstances that people may experience, which might prompt them to access the funds, will be varied and uncontrollable. However, it would be useful as part of an evaluation to understand why people choose to access the funds to determine if facilitating and supporting the establishment of a savings buffer assists people better manage financial shocks.

One of the top savings purposes of our AddsUP matched savings program, delivered in partnership with NAB, is the establishment of a safety net, or rainy day fund[4]. If there was an opportunity for the savings to be held in a 'reward' type account, such as one earning higher interest rates or matched savings, it may be a way of encouraging people to keep their savings buffer intact and encourage the funds to only be used in an emergency.

[4] Good Shepherd Microfinance, (2016) 'AddsUP Savings Plan passes key milestone. $1 million saved and $1 million matched', http://www.goodshepherdmicrofinance.org.au/blog/addsup-savings-plan-passes-key-milestone-1-million-saved-and-1-million-matched

5. **Should a savings target be set and once reached, should funds be redirected towards paying off debt? If so, what should the target be?**

Our response to this question is very similar to that in question 3 above. In most cases there will be an interest rate charged on debt that the consumer is repaying. Therefore we would suggest that economic modelling is conducted to understand the tipping point at which someone is better paying off more on their debt than having increased money in savings. Although we have not conducted research into this optimum level we believe it could be linked to research requirements for access to emergency savings and noting that the ABS uses a benchmark of $2,000.

A clear understanding from the client's perspective will be required for them to make an informed decision around delaying debt repayment in favour of building a savings buffer. People need to be aware that paying back their debt while adding money to savings, will increase the length and cost of their debt. We feel the important aspect of setting a target should be focused around education and understanding of trade-offs rather than an enforced target.

6. **Should there be a ceiling for monthly contributions?**

It is our view that there should not be a ceiling for monthly contributions due to the fact that all consumers have unique circumstances. It is often the case that income fluctuates and this is particularly true for the casualised workforce. It is therefore unlikely to be appropriate to attempt to control how someone may choose to allocate their savings on a monthly basis. It should be at their discretion to put in extra savings when they have the capacity to do so and also allowing the freedom to not contribute to their savings when they cannot afford it.

**Section 3.4**

7. **Do you agree that the savings buffer amount should be pre-entered by pre-filling an income and expenditure statement where possible?**

While we acknowledge that pre-filling the savings buffer amount would harness the power of defaults, we question whether pre-filling the amount of a savings buffer would allow consumers to make arrangements appropriate to their individual circumstances. Anchoring people to a specific amount may have some negative unintended consequences. Anchoring describes the way that elements of situational context can suggest reference points that guide our behaviour—especially when it comes to numbers[5]. Pre-filling a standard amount may anchor people to a specific savings amount when they are actually capable of saving more. Alternatively, some consumers may suffer negative psychological impacts if they are not able to put aside the pre-filled amount of savings. We suggest that reviewing the savings buffer amount on an annual basis could ensure that the amount an individual is setting aside as a savings buffer is appropriate to their individual circumstances, acknowledging that people's circumstances can change over time.

**Section 3.5**

8. **Do you agree that participation by consumers in setting aside some savings should be voluntary? Alternatively, should there be a mandatory requirement in relation to debt repayment arrangements so that some amount is set aside for savings (even if below the minimum amount)?**

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[5] Fiorillo, A., Potok, L., Wright, J., Peachey, J., & Davies, K. (2014). Applying behavioral economics to improve microsavings outcomes. New York, NY: Ideas42 Report.

Based on current research and understanding, it is our view that participation by consumers in setting aside some savings should be voluntary. As research is conducted to evaluate the benefits of the saving buffer, there may be more evidence to support this as a mandatory requirement, which may change this stance. We would also be interested in understanding how a mandatory savings requirement could be enforced and monitored.

One option rather than making it mandatory could be an option to 'opt out' to encourage positive savings behaviour, people are more likely to take it up. Individuals have unique circumstances so our view at present is that you should not force savings if someone would prefer to pay their debt off faster and cheaper.

**Section 3.6**

9. **Where should savings be deposited?**

In a separate bank-owned, no-fee, interest bearing savings account

10. **Do you agree that creditors have a role in helping people in financially difficulty set up accounts and mechanisms to deposit savings?**

Yes, we do agree that creditors have a role in helping people in financial difficulty set up accounts and mechanisms to deposit savings. It is our view that the extent of this role would vary according to creditors as not all creditors may be in the best position to fulfil this task, and we would want to avoid creditors from coercing consumers into an option that is not in their best interest. Where a creditor does not have the ability to set up such an account, such as a utility company, we believe they should provide appropriate referrals to services that are able to assist the consumer when required. It would be important to evaluate the impact of the savings-buffer approach and share this with creditors, particularly if the results indicate that customers are more resilient and better able to manage their debt repayments.

11. **What role could Centrelink play in assisting consumers set aside a savings buffer?**

We are supportive of Centrelink's recent announcement to include savings paid to microfinance savings plans as eligible Centrepay services, which enables people receiving government support to easily set up direct transfers from their Centrepay account to their microfinance savings account and ultimately build their financial resilience. We encourage Centrelink to continue to support this service and continue to work with organisations like Good Shepherd Microfinance as we work to develop appropriate products and systems that will enable us to extend this offering to microfinance clients. We also believe it would be valuable to explore if there is the opportunity to extend this offering to people on low incomes who are building a savings buffer while managing debt repayments.

**Section 3.7**

12. **Do you agree that this measure should be evaluated? If so, we would welcome support from financial institutions that may wish to be involved in doing this.**

Yes! It will be important to understand if changes to the statements actually result in changes to people's savings behaviours and their ability to cope with financial shocks. It will be necessary to gain access to de-identified consumer account data for analysis and there will likely be privacy issues. A banking partner who could assist in establishing the savings account for a nominated group to pilot these changes and could then analyse and summarise this data would be advantageous.

**Section 4.1**

13. **Do you agree that creditors should include a savings buffer in income and expenditure statements when consumers apply for a loan?**

As advocates for financial inclusion, we are concerned that including the savings buffer in credit making decisions has the potential to further exclude some consumers and may force them to pursue credit from fringe lenders. We would not want to price people out of a loan if they can demonstrate a capacity to repay the loan, but do not have capacity to contribute to a savings buffer on a monthly basis at the time that they apply for the loan.

People who access a No Interest Loan Scheme (NILS) loans typically do not have the savings required to purchase the product upfront and are often excluded from mainstream credit options, with 92% of NILS clients living below the poverty line[6]. NILS lends a maximum of $1,200 to individuals over a 12-18 month term, requiring a minimum repayment amount $67 per month if they took out a loan for the full $1,200 (This minimum repayment may be lower if the client has taken a loan of less than $1,200 or has renegotiated their repayments due to financial difficulties). Our current budget does not include a line item for savings as consistent anecdotal feedback indicates that in many cases NILS client would not have the capacity to save in excess of $20 per month at the time they apply for the NILS loan.

We do however, acknowledge the importance of behavioural prompts at teachable moments and recognise that the financial conversations that occurs during the loan application can one of these moments. While many loan interviewers discuss savings with their clients during the loan interview, but it is our experience that the most valuable time encourage savings behavioural change is at the end of the loan when, having established positive repayment behaviours, many clients transfer their loan repayment amounts into savings at the completion of their loan. The AddsUP program assists and encourages clients in this process, as is demonstrated with 'the establishment of a safety net' being one of the top three savings goals of AddsUP clients.

Good Shepherd Microfinance is always interested in increasing our understanding of how our products and processes can assist people on low incomes to build financial capability and resilience and would be interested in gaining further insight into the possible impacts that the savings buffer on an income and expenditure statement could have for people on low incomes who are applying for a loan.

**Section 4.3**

14. **Is there any intersection between the responsible lending obligations in the credit law and a savings buffer in assessing capacity to repay?**

It is our current view that any intersection between responsible lending obligations and a savings buffer in assessing capacity to repay should only be used to positively highlight an applicant's capacity to repay, but should not negatively impact the assessment of the applicant's capacity to repay a loan. If an applicant can demonstrate that they actively maintain and regularly contribute to their savings buffer this could demonstrate their positive money management behaviours and be

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[6] Bennett, S. Georgouras, M. Hems, L. Marjolin, A. and Wong, J. (2013). Life Changing Loans at No Interest: An Outcomes Evaluation of the Good Shepherd Microfinance's No Interest Loan Scheme (NILS), Centre for Social Impact (CSI), University of New South Wales, for Good Shepherd Microfinance

used to favourably demonstrate their capacity to repay. However, through our NILS and StepUP programs we also find that many applicants who have not previously saved or established this kind of behaviour, but have been assessed as having the capacity to repay their loans, are able to do so, with our 94% repayment rate is indicative of this. We also find that NILS or StepUP loans can contribute to establishing positive money management behaviours which, once the loan is repaid, often continue with many clients transitioning the loan repayment amount into a savings account, such as AddsUP. We would be wearing of any intersection that restricted this process, but we would welcome research to analyse the intersection between responsible lending obligations and a savings buffer in assessing capacity to pay.

15. **Could the concept of a savings buffer be incorporated into lending assessment systems that use benchmarks for living expenses?**

We would welcome more information as to how a savings buffer would be calculated and incorporated into benchmarks for living expenses across the different household segments, including if the savings buffer would increase or decrease given the number of dependents in a household. We are concerned that incorporating a savings buffer into lending assessment systems that benchmark for living expenses could exclude people out of loans from the formal sector and force them towards predatory lenders, while at the same time we question its ability to support people in becoming more financially resilient. Our view is that adding a savings buffer into benchmarks would not lead to increased ability to deal with financial shocks because does not ensure that people are saving this money in practice. It is our view that without the appropriate mechanisms to support people in building a savings buffer, adding it into benchmarks for living expenses would more likely have unintended consequences of excluding people from products that they may actually assist them in managing their money and being financially resilient.