THE POVERTY PREMIUM: A CUSTOMER PERSPECTIVE

A REPORT FROM THE PERSONAL FINANCE RESEARCH CENTRE

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ABOUT THIS REPORT

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CONTENTS

1. Introduction 3
2. Efforts to tackle the poverty premium... 6
3. Calculating the poverty premium 13
4. Barriers to the best deal 18
5. The impact of the poverty premium 33
6. What would help remove the poverty premium 42
7. Recommendations.. 48
References and appendices 52

1.
INTRODUCTION

The poverty premium – the concept that people who are poor pay more for essential goods and services – was first introduced in the 1960s (Capowitz 1963) but continues to resonate today. On the eve of the global financial crisis, a report by Save the Children (2007) identified the main ways in which people in poverty in the UK paid more. When this research was conducted in 2019, it was against the backdrop of a substantially reduced system of social welfare and wage stagnation, however, nothing has emphasised quite how keenly those on low incomes are impacted by structural unfairness than the Covid-19 pandemic and the policy response to it.

In response to COVID-19, the UK government implemented a lockdown from the evening of Monday 23rd March, closing all non-essential retail businesses, asking those who were able to work from home to do so, and expecting those in essential retail to implement COVID-19 safety guidelines in their workplace. Key workers (e.g. in health or social care) continued working and were able to send their children to school to facilitate this.

It was immediately clear that low-income workers would be hit hardest; the industries affected, such as restaurants, leisure facilities – including cinemas or sports centres – and non-essential shops are low paid industries, and in fact, one third of employees in the bottom tenth of the earnings distribution work in shut-down sectors, compared with just 5 per cent of those in the top 10 per cent (Joyce and Xu, 2020). The UK Government put in place several financial support measures including the Coronavirus Job Retention Scheme (employee furlough),[1] and the Self-Employment Income Support Scheme (a grant for self-employed people).[2] designed to support businesses struggling as a consequence of the lockdown, by covering the majority of wages of employees, or replacing income of those self-employed. Nonetheless, for those on low wages any drop in income may not be sustainable.

Even as we emerged from the lockdown, low-income workers remained nearly twice as likely to have been furloughed, to have lost hours or pay, or to have lost their jobs altogether than higher paid workers.[3] Any economic recovery will be slow, and for those whose jobs have been impacted in these ways, a difficult time lies ahead; Around a third of such households were already experiencing financial difficulties, four or five times the level of working households who had not been affected[4]. The situation is even more stark for those who were self-employed or working in the gig economy, as many did not qualify for any support.

It is therefore more important than ever to make sure that people in poverty can make the most of the income they have. This research explores the barriers to paying less for exactly the type of low income households who have suffered most in 2020: those insecurely employed in higher risk industries; mothers, whose capacity to work will have been impacted through the closure of schools and childcare, and those who have experienced serious financial difficulty.

[1] https://www.gov.uk/guidance/claim-for-wage-costs-through-the-coronavirus-job-retention-scheme
[2] https://www.gov.uk/guidance/claim-a-grant-through-the-coronavirus-COVID-19-self-employment-income-support-scheme
[3] https://www.resolutionfoundation.org/app/uploads/2020/09/Low-Pay-Britain-2020.pdf
[4] https://www.standardlifefoundation.org.uk/__data/assets/pdf_file/0022/61852/Emerging-From-Lockdown.pdf

Recent research has taken a fresh approach to understanding and measuring the poverty premium in the UK (Davies et al 2016, Corfe and Keohane 2018a/b, Whitham 2018). As a result, we have a much better understanding of different poverty premium pathways and the types of people likely to be affected by them (Hirsch 2013, Davies and Finney 2017).

UK government and regulators also increasingly recognise the pressing need to eradicate the poverty premium. Some recent regulatory changes have explicitly aimed to address unfair market practices that can feed the poverty premium. Technological changes may quickly impact on the way in which the poverty premium is felt, whether positively or negatively. There is a new generation of innovators that are expressly designing products to help people on low and uneven incomes by tackling the poverty premium, including those funded by the Fair By Design Venture Fund.[5]

Fair By Design and Turn2Us commissioned this research to explore recent changes in the poverty premium landscape, to understand if they are having any impact on the cost of premiums, or the number of people who pay them. Importantly, we did this through the lens of the low-income customer in order to hear first-hand how they experience these extra costs; how they see the problems with the current system; how they respond to initiatives and interventions designed to reduce poverty premiums; and the changes they feel would make the most difference to them and their household.

This research report:

- Describes recent initiatives to reduce the poverty premium and reviews any evidence of what works.
- Re-calculates the level and types of poverty premiums paid by low-income households in 2019. We focus on high-cost credit use, energy tariffs and insurance (specifically home contents, car and specific item insurance) because our previous work identified these as potentially the most harmful to low-income households (Davies et al, 2016; Davies and Finney, 2017).
- Looks in detail at the financial difficulties experienced by low-income households, their impact on individuals and families, and the things that prevent low-income households from getting a better deal.
- Sets out 'user-led' solutions and ideas that people living in poverty feel could help to reduce the extra costs they pay.

1.1 RESEARCH DESIGN

This research report is based on a three-stage, mixed-methods study.

1. **A review of the evidence**. We looked at recent evidence about interventions (such as new regulation or innovative business practices) designed to reduce or eradicate the poverty premium and any evidence about their effectiveness.

[5] For details see https://fairbydesign.com/

2. **A survey of people living in low-income households**. We collected survey data from 1,000 people living in low-income households[6] who had contacted Turn2Us for help. They either completed an online survey on the Turn2Us website or over the phone with Turn2Us helpline staff. The survey asked about the costs they paid in domestic energy, insurance and consumer credit.
3. **Four focus groups with people in low-income households in London and Plymouth.** Each group examined a different dimension of poverty: one group was with older people aged 55+; one with working age people who were unemployed or insecurely employed; one with people who had sought advice about their financial difficulties; and one with mothers of young children. In the groups we heard about the different poverty premiums that participants experienced; the impact of these poverty premiums on them and their households; and their ideas about what would help them to access better value services.

[6] Low-income households were defined in the survey as those below 70% median income when equivalised for household size. This meant we could compare the findings with our earlier research which used the same definition.

2.
EFFORTS TO TACKLE THE POVERTY PREMIUM

What is being done to reduce the poverty premium and do we know whether these strategies are working?

This chapter explores what has been done in recent years in the UK to address the poverty premium in the domestic energy, insurance and consumer credit markets. We reviewed evidence of interventions, regulation and changes in business practices which aim to reduce or remove the premium.

2.1 WHAT IS BEING DONE TO ADDRESS THE DOMESTIC ENERGY POVERTY PREMIUM?

The domestic energy market has seen the most significant innovation and regulation in the past few years of any of the sectors we investigated, and the pace and breadth of change has been substantive. Regulatory intervention has introduced price caps to protect consumers using prepayment meters (PPM) and those on standard variable tariffs. Recent evidence is suggestive of a positive impact from using collective switching schemes when partnered with behavioural science insight.

However, all of these interventions – with the potential exception of the PPM cap – continue to place the responsibility for accessing the best deals with the individual, which only benefits active consumers who are willing *and* able to shop around. Our literature search highlighted a number of key reports exploring the impact of poverty upon decision making, which suggest that poverty frames decisions differently and can reduce people's mental 'bandwidth'.

This evidence appears to be influencing regulators' thinking around the poverty premium. The CMA response to the Super-Complaint made by Citizens Advice (2018) states that people should not be required to spend significant lengths of time negotiating a good deal – or feel that they must be 'on guard' against being ripped off (CMA 2018, p.5). It is of specific note that the CMA states 'in the past too much has been asked and expected of consumers and not enough from businesses' with regard to tackling the loyalty penalty (CMA 2018, p.8). While domestic energy is not one of the five markets under specific scrutiny, it is clear that unless businesses take responsibility for addressing loyalty penalties/pricing practises, longer-term regulatory solutions will be needed.

Regulatory changes

Substantive, wide-ranging regulatory changes have been introduced in the UK energy sector in the past few years. In 2017, Ofgem introduced the Prepayment Meter (PPM) Price Cap, limiting the price charged to customers and aiming to reduce the difference in energy charges between prepayment customers and those paying by other methods. For the 4 million customers in the UK using prepayment meters this cap has resulted in lower unit prices.

The PPM cap saw prices fall below that for some Standard Variable Rate (SVR) Tariffs in 2017[7]. However, the October 2019 review found an increase for the first time due to a change in how the cap is calculated. We did not find any evidence about how this cap has impacted upon consumers; however, the decision by Ofgem to extend the period of the cap past the original 2020 deadline is evidence in itself that continued regulation is necessary in order to protect consumers.

Concern regarding the prices of SVR tariffs led to a 'safeguard tariff' being introduced between February 2018 and January 2019 for customers on a standard variable or default energy tariff who received the government's Warm Home Discount. They were price protected at the level of the prepayment meter price cap. Subsequent to dealing with these very high SVR tariffs, a cap was introduced limiting the cost of standard variable tariffs via the Domestic Gas and Electricity (Tariff cap) Act 2018. It took effect from 1 January 2019, aiming to protect the 11 million customers not actively engaging in the switching process and paying considerably higher costs than the best deals available.

Prior to and following on from the introduction of the cap, concerns have been raised that this form of regulation may result in consumers paying higher prices as energy providers 'race to the top', with prices converging around the cap price. Ensuing price increases, limiting competition and causing consumers to further disengage with the market are feared (Ioannidou and Mantzari 2018[8]; Dodsworth and Bispring 2019[9]). Notably, price variance between suppliers in the prepayment meter sector has decreased, which may reduce the incentives for prepayment customers to switch because cost savings are the main reason to switch (unless they change to a different payment method whereby saving could still be made). In the longer term, when the cap is removed disengagement from the market could become detrimental to customers. Alternative forms of regulation have been suggested, such as issuing a price cap upon the standing charge (Osmon 2018)[10].

As the default tariff is a very recent regulatory change it is not yet clear what the longer-term consequences will be and whether the caps will indeed protect and benefit customers, or if in fact prices will rise and competition decrease over the longer term. Currently the default tariff cap is due to remain until the end of 2020. Therefore, continued focus is needed to ensure that at the end of the price cap period pricing practises take account of the needs of low-income and vulnerable consumers.

Collective switching utilising behavioural science

Building on already detailed knowledge of barriers to switching for low-income consumers, Ofgem explored ways of increasing consumer engagement in the domestic retail energy

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[7] Ofgem (2017) https://www.ofgem.gov.uk/publications-and-updates/standard-variable-tariffs-latest-trends-september-2017

[8] Ioannidou, M and Mantzari, D (2018) The UK Domestic Gas Electricity (Tariff Cap) Act: Re-Regulating the Retail Energy Market (September 24, 2018). Modern Law Review, Forthcoming. Available at: https://ssrn.com/abstract=3266371

[9] Timothy J Dodsworth, Christopher Bisping, 'Energy Price Cap – a Disservice to Consumers' (2019) 8 *Journal of European Consumer and Market Law*, Issue 2, pp. 53–64

[10] Osmon, D (2018) The case for a cap on the standing charge in energy bills. London: Ideal Economics. Available at: https://www.ofgem.gov.uk/ofgem-publications/141606

market offering a collective switch to vulnerable consumers in a series of five randomised control trials (Ofgem 2018b)[11]. Evidence of collective switching as a potential tool for engaging vulnerable consumers and to promote switching in the energy market has existed for some time (London Councils 2013)[12]. Ofgem (2018b) found that offering a collective switch tariff alongside 'applying behavioural science to remove as many steps from the switching process as possible' was most effective in raising switching rates (ibid, p.7). It resulted in 22% of customers switching energy supplier; more than eight times the level of switching in the control group (Ofgem 2018a).

As a result of this study Ofgem are considering 'what future role collective switching may play in the energy market' and considering how to take this forward (2018b, p.9).

Innovation

Youtility and websites such as lookaftermybills are examples of innovation in the energy sector, namely around automatic switching to better tariffs. However, these innovations presume digital capability and trust in online technology which we know are lower among households most likely to pay the poverty premium.

2.2 WHAT IS BEING DONE TO ADDRESS THE INSURANCE POVERTY PREMIUM?

Based on our earlier findings (Davies et al 2016; Davies and Finney 2017), in the insurance market we focus on home contents insurance, car insurance and insuring specific items as key areas where the poverty premium is acutely experienced by low income consumers.

Additional premiums paid by low-income consumers purchasing car or home contents insurance are accrued because of where they live, how they pay and the loyalty penalty. Unfair pricing relating both to risk (e.g. where someone lives) and the loyalty penalty have been addressed, at least in part by recent regulatory clarification. Potential innovation or new business practices have been evaluated by recent research on behalf of the FCA and suggest that in the next three to five years new technology and business models have the potential to be impacting this sector (Deloitte, 2019)[13].

In this section we will consider the regulatory input from the FCA in the general insurance market and the ban on the sale of extended warranties at the point of sale in RTO stores (a form of specific item insurance), before considering innovation in this sector.

[11] Ofgem (2018b) Ofgem's collective switch trials report. Available at https://www.ofgem.gov.uk/ofgem-publications/156461

[12] London Councils (2013) Big London Energy Switch Evaluation: Key Lessons for Boroughs. Available at: https://www.londoncouncils.gov.uk/node/1648

[13] Deloitte - Annex 6 (2019) Trends in general insurance pricing: Final report for the FCA. Available at: https://www.fca.org.uk/publication/market-studies/ms18-1-2-annex-6.pdf

Regulation

Clarification of General Insurance Pricing Practises

Whilst the FCA have currently stopped short of implementing new regulation, general insurance – home contents and car – has received recent scrutiny; an interim report published in October 2019 clarifies current regulations and responsibilities for insurance firms (FCA, 2019g)[14]. The FCA found firms were failing to assess and evidence that they were treating customers fairly with regards to pricing. Differential pricing led to some customers paying substantially more than others, despite similar risks and costs being associated with each customer profile.

Cross-subsidy of some consumers to others was also highlighted as a concern. The FCA note that this additional cost often fell on long-standing customers who do not switch – effectively a loyalty penalty.

Acknowledgement from the FCA that vulnerable and low-income customers are currently being disadvantaged is positive in terms of reducing the poverty premium in this sector. Their final Market Study is due to be published early in 2020 and will set out potential remedies. The report will also take account of stakeholder feedback regarding the challenges and innovations of potential remedies to unfair pricing in general insurance. It will be interesting to note if amelioration is made for paying monthly rather than paying an annual renewal.

Ban on Rent-to-Own extended warranty purchase at point of sale

Direct regulation has been introduced by the FCA to prohibit the sale of extended warranty on Rent-to-Own goods at the point of sale, in order to minimise pressure on consumers to take this expensive form of insurance (FCA, 2019f[15]). Low-income households show a greater propensity to purchase specific item insurance (Corfe and Keohane 2018b) and therefore this regulation change is expected to reduce the number of lower-income consumers taking out this type of expensive policy (10-20% reduction expected, FCA 2019e[16]) and specifically consumers becoming over-insured.

This regulation assumes that taking specific item insurance is an inappropriate and expensive form of insurance, however in the light of potentially unsuitable home contents policies it will be important to conduct research to explore the impact of this change, as it may also leave consumers under-insured.

Innovation

Within three to five years a number of innovations are likely to impact upon the general insurance sector. Developments in technology and data sharing (open insurance) are expected to enable intelligent, flexible products (Deloitte 2019). While some innovative products may seek to challenge the current pricing structures, many are based upon the

[14] FCA (2019g) MS18/1.2 General insurance pricing practices interim report. Available at: https://www.fca.org.uk/publication/market-studies/ms18-1-2-interim-report.pdf
[15] FCA (2018) https://www.fca.org.uk/publication/consultation/cp18-35.pdf
[16] FCA (2019e) https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/815022/RPC-4372-HMT-FCA_-_Rent-to-own_Extended_warranties.pdf

same pricing framework. This may proliferate the same unequal pricing causing detriment to those who do not switch, suggesting there may still need to be further regulatory intervention in this sector for the poverty premium to be addressed (Deloitte 2019).

Other innovative potential options for designing out the poverty premium in the insurance sector focus upon creating home contents policies suited to the needs of low-income households; smaller insured sums, a focus on household essentials and low weekly payments. In order to overcome the many potential exit points on the customer journey to taking out insurance, research has suggested using intermediaries – social landlords, employers or via benefits payments – to allow low-cost policies to be paid (WPI Economics 2019). Creative innovations such as auto-enrolment schemes or home contents insurance as a 'benefit' provided by other services, such as a current account or employer, are also being explored as methods of overcoming the insurance poverty premium.

2.3 WHAT IS BEING DONE TO ADDRESS THE CREDIT POVERTY PREMIUM?

Since 2014, wide-ranging and substantive FCA intervention and regulation has changed the high-cost credit (HCC) and consumer credit sector in the UK. Price caps have been introduced for high-cost short-term credit (HCSTC) products (i.e. payday loans) and rent-to-own products (offered by firms such as BrightHouse). Tighter business restrictions have been enforced across other high-cost credit products, and affordability requirements have also been tightened.

There remains a need for access to affordable credit by low-income households in order to manage unstable incomes, unexpected expense or a reduction in income (Citizens Advice 2018), as well as creative methods of reducing the demand by addressing specific drivers of credit need (FCA 2019c). Recent FCA focus upon potential low-cost and non-credit alternatives to HCC has highlighted areas for development and innovation within the sector and from outside intermediaries, such as registered social landlords, credit unions and charities (FCA 2019c).

In this section we will consider the specific regulations that have been introduced and evidence of their impact, beginning in 2015 with the HCSTC cap.

Cap on high-cost short-term credit (HCSTC, i.e. payday loans)

In January 2015 a price cap was introduced which limited the total cost that a consumer could be charged for a HCSTC loan at 100% of the total loan value, capping the daily interest charge at a maximum of 0.8% of the amount borrowed and limiting default charges at £15 (FCA 2014).[17]

The evidence indicates that consumers who are no longer able to access payday lending as a result of tighter affordability criteria are not being pushed towards loan sharks or suffering substantial hardship as a result of restricted access to this type of credit (Critical Research

[17] FCA (2014) PS 14/16 Detailed rules for the price cap on high-cost short-term credit Including feedback on CP14/10 and final rules. Available at: https://www.fca.org.uk/publication/policy/ps14-16.pdf

2017). Informal lending from friends or family, going without (including missing a payment or falling into arrears) are found to be the most likely outcomes (unless changed circumstances mean that credit is no longer needed). Some consumers reported it was a 'wake-up call' to address their difficult financial circumstances.

Concern has however been raised about the implications of informal borrowing and going without (Appleyard, Packman, and Lazell 2018; Citizens Advice 2018[18]). Borrowing from friends and family may cause pressure and distress, especially when family or friends are themselves in financially vulnerable positions. Going without in some instances may be an appropriate option, however when households are going without essentials such as food or heating, or are falling into arrears on priority bills, it indicates a need for an alternative form of credit.

Wider high-cost credit regulation, 2018 onwards

As well as a price cap in the payday lending market, the FCA has intervened in several other credit sectors to address significant consumer detriment – demonstrating that high cost is not limited to the high-cost credit market:

- Regulatory intervention in the credit card market has included action to address persistent credit card debt, a requirement for credit card firms to use their data to identify customers at risk of financial difficulties and a voluntary code to ensure credit limits are not increased without customer agreement.
- Home collected credit has been subjected to tighter rules around repeat borrowing and more transparent information for consumers.
- Catalogue and store card regulation has outlined requirements for transparent information regarding products and tightened responsibilities of firms to customers in long-term debt.
- The FCA has introduced rules regarding overdrafts which requires simpler pricing in order to allow customers to more easily compare overdraft costs and increased transparency, making overdrafts fairer and easier to manage.
- The rent-to-own sector has seen a price cap imposed to control both 'the cost of product and the charge for credit'[19]. (As discussed in the insurance section of this literature review, a ban has been introduced on point of sale RTO extended warranties.)

[18] Citizens Advice (2018) Walking on thin ice: The cost of financial insecurity. Citizens Advice. Available at: https://www.citizensadvice.org.uk/Global/CitizensAdvice/Debt%20and%20Money%20Publications/Walking%20on%20thin%20ice%20-%20full%20report.pdf

[19] FCA website (https://www.fca.org.uk/firms/high-cost-credit-and-consumer-credit/summary-key-publications Accessed: 7/12/19)

3. CALCULATING THE POVERTY PREMIUM

This chapter sets out the poverty premium paid by low-income households in 2019

3.1 HOW MUCH IS THE POVERTY PREMIUM IN 2019?

To calculate the cost of the poverty premium in 2019, we replicated the methodology used in our earlier study (Davies, Finney and Hartfree 2016). This time around, we surveyed low-income households who had contacted Turn2us for benefits help and asked them about how they paid for gas, electricity, and any insurances they held; levels of switching in essential services; and what form of consumer credit (if any) they had used in the last 12 months.

Using the same assumptions and examples as 2016, we then attributed a cost to each type of premium (for a full explanation of the assumptions see the Appendix). This enabled us to measure any changes to each poverty premium component between 2016 and 2019. The table below summarises the poverty premiums that have risen or fallen.

Table 3.1 Poverty premiums that have risen or fallen

Premium area	Change in costs from 2016 to 2019
Use of prepayment meters	↓
Non-standard billing methods	↑
Not switched to best fuel tariff	↓
Area-based premiums	↑
Insurance for individual items	↑
Access to money	↑
Higher-cost credit	↑ ↓

(Green=lower in 2019, red= higher. Darker shade=bigger difference)

Broadly speaking, the premiums related to domestic energy have dropped, whereas those relating to insurance have risen. The premiums relating to the cost of credit differ depending on the type of credit used, with some rising but some dropping.

A full breakdown of the 2019 poverty premium and the changes from 2016 are shown in Table 3.2, along with the proportion of households that incur different premiums. This shows that, on average, in 2019 low-income households incur **£478** of extra costs through poverty premiums. The equivalent figure for these premiums only in 2016 was £432 (see appendix for full list of comparable premiums in 2016). This is a slight increase overall, however, by comparing the current costs of the elements of the poverty premium with those from 2016, we can begin to understand the changing nature of the poverty premium.

Table 3.2 A breakdown of the average poverty premium in 2019, with comparison costs for 2016

Premium	**Households incurring premium**	**Cost of poverty premium 2019**	**Average poverty premium 2019**	***Cost of poverty premium (2016)***
	%	**£ / year**	**£ / year**	***£ / year***
		-	**£478**	-
Use of prepayment meters	**31**	-	**£28**	-
Prepayment meter - electricity	28	£29	£8	*£35*
Prepayment meter - gas	25	£29	£7	*£35*
On best prepayment meter tariff	10	£131	£13	*£227*
Non-standard billing methods			**£64**	-
Payment on receipt of bill - electricity	9	£54	£5	*£38*
Payment on receipt of bill - gas	8	£54	£4	*£38*
On best payment on receipt of bill tariff	5	£143	£7	*£43*
Home contents - monthly payments	29	£10	£3	*£9*
Car insurance - monthly payments	28	£161	£45	*£81*
Not switched to best fuel tariff	**53**	**£213**	**£113**	***£317***
Area-based premiums		-	**£133**	-
Home contents insurance - deprived area	44	£5	£2	*£14*
Car insurance - deprived area	44	£298	£131	*£74*
Insurance for individual items			**£23**	-
Household appliance insurance	8	£176	£14	*£132*
Mobile phone insurance	11	£81	£9	*£60*
Access to money			**£10**	-
Fee-charging ATM	35	£25	£9	*£25*
Pre-paid card fees	4	£33	£1	*£25*
Higher-cost credit	**28**		**£107**	-
Rent-to-own	2	£182	£4	*£315*
Short term loan*	4	£237	£9	*£120*
Home collected loan	4	£644	£26	*£540*
Pawnbroking loan	2	£152	£3	*£50*
Subprime personal loan	6	£557	£33	*£520*
Subprime credit card	12	£207	£25	*£194*
Mail order catalogues	10	£60	£6	*£178*
Christmas hamper scheme	1	£47	£0	*£47*

* *short term (three month) loans were used as substitute for payday loans in 2016*

Area-based poverty premiums

In 2019, the area-based premiums, particularly car insurance, were the largest contributor to the overall premium. This contributed almost one third of the overall total, as it is both a costly, as well as a commonly-incurred premium. Just under half of the Turn2Us clients we surveyed (44 per cent) incurred this cost. Respondents who lived in a high-risk area (20th percentile IMD area[20]) paid nearly £300 per year more on average, if they had insurance, than those who lived in a lower-risk area (50th percentile IMD). In 2016, this figure was only £74, which is striking increase.

Domestic energy poverty premium

The costs of the premiums related to energy costs, whether through switching, or use of prepayment meters have mostly reduced. The changes between 2019 and 2016 were:

- The gap between the standard variable direct debit tariff and the best online one has reduced from £317 in 2016, to £213 in 2019, a reduction of over £100.
- There were higher levels of switching in this survey of low-income households, than in the one conducted in 2016. In 2016, only 27 per cent of those surveyed had switched gas or electricity supplier in the last 2 years, whereas in the survey of Turn2Us clients 47 per cent had. However, this is most likely to reflect the engaged nature of the sample
- The gap between the best PPM tariff and the best online only one had almost halved, dropping from £227 in 2016 to £131 in 2019.
- The only energy-related premium that was higher in 2019 was for those who paid for energy on receipt of their bill. The best tariff available for those who paid in this way was £143 higher than the best tariff for those who pay by direct debit and managed their account online. This had increased from only £43 in 2016.

The nature of the changes to energy tariffs suggest that the 2017 prepayment meter tariff cap and the subsequent 2018 default tariff cap have narrowed the gaps between different tariffs, and by doing so, reduced the poverty premium.

Consumer credit poverty premium

The premiums for insurance, and those for gas and electric supply are 'broad' premiums, that is they are incurred by a significant proportion of low-income households. The remaining premiums were mostly less frequent, although in the case of High Cost Credit, individually the most expensive premiums to bear.

As in 2016, the costs for use of High Cost Credit vary depending on the type of credit used, ranging from £644 for home collected credit to £42 for those who used catalogues. In comparison with 2016:

- The costs of buying goods on credit from a rent-to-own store has decreased, dropping from £315 on average to £182.
- The cost of using mail order catalogues has also dropped since 2016, in the case of catalogues by £118 pa on average.

[20] Index of Multiple Derivation; DCLG, 2015

- Conversely, the costs of loan finance, whether subprime loans, short-term loans (payday substitute) and home-collected loans have all increased.
- The costs of subprime credit card use were also slightly higher than in 2016.

These changes in credit costs suggest that the recent cap on the cost of Rent-to-Own contracts may indeed be having a positive impact on how much customers pay for their goods. In general, however, higher-cost credit is more costly than in 2016, and this brings into question the impact that the cap on total cost of credit is having in the long run.

Having calculated the current average poverty premium, we now move on to explore in more depth some of the reasons why those in low-income households are still experiencing them.

4.

BARRIERS TO THE BEST DEAL

We explore the factors that may prevent low-income households from paying less for essential services

We explore in this chapter the reasons why a low income may prevent people from accessing the best deal in the energy, insurance and credit sectors, using our survey data and information from four focus group discussions. We consider:

- choice of payment methods;
- switching behaviour;
- external barriers – issues around poor credit ratings and housing tenure;
- the barriers to affordable credit use;
- the barriers to the use of insurance,

and look at how these factors interact with the challenges of living on a low income.

4.1 CHOICE OF PAYMENT METHODS

Our survey of Turn2Us clients shows that a significant proportion paid their regular bills by what might be considered non-standard methods that incur extra costs.

Table 4.1 Level of non-standard payment method use

Non-standard payment method	% of sample
Prepayment meters for gas or electric	31
Pay on receipt of bill for gas or electric	11
Home contents - monthly payments	29
Car insurance - monthly payments	28

(base: 1,000)

Among our focus group participants, payment methods for domestic energy bills were the most varied, divided between monthly direct debits, standing orders, online payments, and Prepayment Meter. Monthly direct debits were the most common method of payment for insurances, although a smaller number did report paying an annual premium.

Choice of payment method was often pragmatic; those who spread the cost of insurances across the year were fully aware that it was more costly in this manner but were not able to pay the lump sum in one go. We found few who purchased white goods or furniture outright, but many were able to spread these costs without incurring interest, through buying from shops that offered interest-free credit. Generally, payment schedules were chosen to fit into the budget cycle of the household, and few worked to a budget that had any large sums coming in at any point during the year.

Gas and electricity were notable in that, unlike many other bills, the amount owed varied considerably over the course of the year. For those who had choice over the way they paid, their preferred method was generally driven by feeling in control over their money. However, this manifested in different payment and billing methods for different people. The cheapest tariffs remain those that are paid by direct debit and administered online, yet a considerable proportion of low-income households do not pay in this way as seen in Table 4.1 above.

Control over the accuracy of billing

Many participants raised concerns over the accuracy of the bills they received, and this was a strong motivation for paying on receipt of the bill – so they are able to check before they pay. There were enough examples of inaccuracies given to suggest it was a reasonable concern. One woman had received inaccurate bills previously, which justified her continued choice of paying on receipt of bill:

> *"I like to see what I have used... And what I haven't used ... I match the meter reading on the paperwork to my meter and for the last three quarters it has been wrong... They sent a £600 bill when I was away for 5 weeks, so they refunded me... if someone didn't know how to read their bills properly would have actually just paid the £600." (Working age group, London)*

In this example, the loss of £600 would have been far more costly than any savings that she may have made from being on a better tariff.

This was a particular concern over the use – actual or potential – of direct debits. Unless the household has a smart meter, it was hard to gauge if the full amount owed for gas and electricity was being covered. A woman using direct debits noted the extra effort that was needed:

> *"I think if you're on direct debit you've got to be really savvy and like check how much you are using each month... I have had that before where the payment has not come out for the right amount or one month's bill has been higher than what you pay and then you end up with a huge bill... my husband thinks I am obsessed but I'm just like, I don't want a huge bill, I can't pay a huge bill." (Young family group, Plymouth)*

Other respondents noted occasions when direct debits had not been taken, particularly when starting a new contract, which resulted in arrears. Overall, for those with no slack in their budgets, direct debits were seen as a risky option, and help explain why many chose other payment options. The reluctance of those in low-income households to use direct debits is well known, but carries an even greater risk when paying for gas and electricity. For many, therefore, the fear of losing money was a stronger driver than the desire to save some.

For others, particularly those on a steady income, use of direct debit was a budgeting tool, allowing them to spread the fluctuating costs of gas and electricity over the year. Rather than giving frequent meter readings one participant explained:

> *"...it works for us because most of the time you're not using, you're not using the same amount of energy throughout the year, in summer you're not using, so it does fluctuate, but it works in your credit so at the end of the year you're actually, usually you get something back, it's quite helpful." (Working age group, London)*

However, when income fluctuates it can make using a fixed method like direct debit problematic:

> *"[We pay] quarterly because of our income, we can't pay with direct debit... Because we don't have the same income every month." (Working age group, London)*

One man explained why he chose to pay some bills quarterly, some monthly and some via a prepayment meter:

> *"The reason why I do that, if I paid by direct debit and something goes wrong and they take the running of it, you owe them money out of your next pension if you go overboard." (Older group, London)*

Finally, prepayment meters were also about keeping control of usage as well as payment for gas and electricity. Prepayment meters and smart meters gave clear information about energy consumption and allowed those who had them control over their usage. For many, rationing heating in order to pay other bills was a routine method of balancing household finances.

> *"Yes that would be the worry wouldn't it, like making sure your bills will get paid because some months is tighter than others, so like you might think right okay just don't have the heating on for that week because I need to pay my bills…" (Young family group, Plymouth)*

Payment methods are therefore a vital way to budget or juggle household expenses by maintaining control of when and how payments are made, accommodating the need for cash flow in households where incomes are constrained. Unsurprisingly, there is significant caution relating to any payment method that risks an unexpectedly large bill and equally, a strong draw towards payment methods that reduce risk and increase security.

4.2 SWITCHING BEHAVIOUR

This section explores the barriers that can prevent those in low-income households from switching to the best deals and tariffs, as well as the factors that have persuaded others to do so. Table 4.2 shows that among our survey respondents, the pattern was one of low levels of switching across both services and products.

Table 4.2 Level of switching

Services or products switched in the last 12 months	% of sample
Gas or electricity provider	31%
Broadband/ TV package	22%
Vehicle (car or motorbike) insurance	17%
Building or Contents insurance	14%
Mobile phone provider	13%
Bank account	7%

(base: 1000)

In the focus groups, we identified three groups with different types of switching behaviour: firstly, the households who embraced switching, investing substantial time and energy into shopping around and ensuring they negotiated good tariffs for energy, telecoms and insurance. These were often those with youngish families. The second group were those who had previously switched, in at least two services or on more than one occasion, but had not continued to do so, and thirdly households who had not engaged in switching at all. This third group tended to be those who were older, or perhaps had English as an additional language.

For all groups, however, issues of trust permeated through the discussion around switching and revealed substantial dissatisfaction with the current consumer environment, whereby responsibility for getting a good deal falls to the consumer, regardless of their age, capacity, digital skills or ability to invest time in this area. It was considered unreasonable to require all consumers to actively engage in these markets in order to pay a fair price.

Why do people switch?

Among our focus group participants, the main reason to switch was the perception that the money saved is substantial. Unless there had been an active problem with the existing supplier, this was essentially the only reason to do so, and this was recognised by most participants, whether they switched or not. Broadly speaking, it was felt that there were considerable savings to be made by switching supplier, although a few believed that potential savings were minimal.

> *"he did switch recently but I can't remember who it was with, he was with British Gas and he's moved to someone new and he's saved about £200 a year in gas and electric." (Young family group, Plymouth)*

Throughout all the groups, there was a tacit acceptance that there was a need to switch in order to get the best deal; that loyal customers frequently faced high tariffs and were penalised rather than rewarded by companies. Again, this was the case whether people had switched or not, and it was not viewed in a positive light.

> *"That's a travesty, that is, I mean customer loyalty is getting exploited… they laugh at people with customer loyalty… Because you get the worst deal…" (Older group, London)*

Those that switched were engaged with the idea of the market, that it was just what you needed to do to save money. In this group, they had the capacity to shop around, and were comfortable with doing so. Within the focus groups, or in their daily lives, they were generally positive about the idea of switching, and encouraged others to do so. However, language such as 'game' and 'tactics' was used when talking about how to get the best deal, suggesting that as consumers, they felt manipulated with the choice only to either engage or pay more than other consumers

Even those that did switch noted that the gains were less with each switch. One mother claimed to save each year, but on reflection changed this to "I haven't gone up, if that makes sense". Switching becomes a way of maintaining rather than improving the household financial position.

Why don't people switch?

While Table 4.2 above finds that rates of switching among low-income households are higher than previously recorded, the focus groups highlighted a range of complex and often interlinked reasons why many chose not to engage.

As noted above, the strongest benefit of switching came from the initial move away from the standard tariff, and subsequent moves were to avoid going back to the higher rate. Not surprisingly, many resented the need to constantly monitor and switch in order to maintain a reasonable price for a service. Price rises meant that consumers quickly felt they were no longer saving, and that the process of comparing prices and switching had produced only short-lived benefits. As a result, trust in providers was lost.

> *"And a lot of these tactics are used with energy providers… the first 6 months we'll charge you half price on the low tariff and then it's going to go to a standard tariff, not many people understand… Eventually they're taking back exactly what they wanted to in the beginning but showing, making you go around the maze eventually to come back to the same spot." (Working age group, London)*

This disillusionment was particularly noticeable in the second groups of switchers (who had switched previously), leading them to disengage with the market. In the insurance market, however, there was an expectation that annual renewals might require consumers to shop around, and this appeared to be acceptable. This may reflect that the car owners in our group were more likely to be both younger and working.

Most felt that this current system, requiring constant reviewing and switching, was unfair and stressful. It took an unwanted level of effort to participate in this market, and was particularly unfair on the older generation, and those who struggle with the internet.

> *I'm always checking, whether I switch or not but I'm always looking to see if I can get a better deal out of it and all that, but it is a game that you have to invest a lot of time in and it is very, they make it very difficult for you as well, you know." (Older group, London)*

Some of the older participants, who were really struggling financially, saved money by cutting back, and were understandably cynical that they could in fact make the sorts of monetary savings that were advertised by providers.

> *"I can't save £200 a year… they say my bill's £523 with gas and electric, but it must be 250 now, so I can't save 250, I can't get it for free." (Debt advice group, Plymouth)*

In the context of the drop in the real value of benefits and incomes, as one woman receiving benefits noted, *"me saving £5 here and there really doesn't cut* it". For those struggling with other – often multiple – issues like ill-health, caring responsibilities or debt, switching energy supplier tends to be lower down their list of priorities, particularly for those we spoke to who were battling with government agencies over entitlement to benefits.

Additionally, many were concerned that they may incur additional costs as a result of switching. One woman had switched energy supplier and ended up accruing a large bill because both suppliers billed for usage during the process. While it was resolved eventually, overall there was a significant level of concern about the financial detriment that may be caused by switching. This anxiety was discussed in relation to telecoms as well as energy providers.

> *"Yeah I'd like to go to Tesco's but that would involve something else, possibly racking up £20 in between and I can't afford to do it." (Young family group, Plymouth)*

These concerns reflected how tightly household budgets were managed and how little room there was for additional costs or even minor financial shocks.

Trust in providers

A lack of confidence and trust in the provider emerged as key underlying factor in many of the barriers to switching – and could result in more consumer effort in order to validate that a provider was 'legit'. One woman had recently switched to a newer provider and she explained how she verified that the company was legitimate:

> *"Because I was a bit dubious about the company I'm with but then I did a lot of research and finding out reviews and what they're like and then rang them a few times… to make sure they were actually there, I bet they thought oh god I'm stalking them." (Young family group, Plymouth)*

The context of the recent demise of a number of the newer energy companies made this fear of unknown companies feel very real to many. There was comfort and security of dealing with familiar, large company brands.

> *"you get the best prices from the small ones, but the small ones can go bust… So what happens then? What if they've taken, you know, £600, £700 and then they go bust and then what happens to your utility, you know, what happens?" (Working age group, London)*

It is understandable that many of those in poverty will not switch to a company that they do not trust, as the consequences of making an error and losing money are so severe. Whether the lack of trust is justified or not, this a considerable barrier to encouraging those who may benefit from the savings, to risk switching to get them. The fear of the unknown was strongest amongst those who were unemployed or of an older age.

> *"I might go into changing or looking into changing my energy provider, but other than that I don't think one would make that leap because it's too scary, there's so much fraud out there …it's true for me and my mum, we don't trust nobody, you know, I've been caught out myself a couple of times … I just don't trust people." (Working age group, London)*

There was also a feeling of powerlessness in the relationship with providers. The language of coercion was used in several contexts when discussing getting the best deal. Consumers talked of the 'tactics' that companies used, that its's a 'game', and that loyal or vulnerable customers were 'prey'. Those who either lacked the choice to switch or who are not able to actively participate in the switching process were felt to 'not have a voice'. Many felt significant pressure to use online services whether they wanted to or not.

Skills and information needed to make the right choice

The levels and types of capability, both digital and financial, required by consumers to find the best deal for energy, insurance and telecoms tariffs was explored in detail the older age group and the financial difficulties group who had received debt advice. The challenges of negotiating a complex marketplace for older consumers or for those with a learning difficulty, health condition or other difficult situation, was overall deemed to be unfair and unrealistic.

Even for participants without any particular limitations, the information required to determine the best deal was seen as complex and difficult to navigate. Many believed that companies deliberately made information complex in order to make offers appear better than they really were, raising levels of mistrust in these companies.

> *"..they're getting very good at, you know, blinding you with fake science basically..." (Older group, London)*

So while some could clearly articulate how to compare deals using unit prices and standing charges, others felt this was unfamiliar to them. This lack of trust in the good faith of companies made it even harder to know what to believe.

Digital barriers

Digital capability was a particular issue for the older focus group participants. While some older participants were confident about keeping safe and interacting online, many others, of all age groups, were not. Some did not access digital services at all, while others were happy with online communication or listening to music online, but would not undertake online transactions. Building digital skills and confidence takes time and significant effort on the part of the consumer. One older woman explained that it requires a trusted intermediary to 'hold your hand' through the process; it isn't something that can merely be told. With the help of a community advisor, she had been able to acquire the skills and confidence to shop online and was now supporting others to do the same. However, others remained unconvinced and believed it should be a choice whether to be online or not.

However, in terms of digital access, across all groups, security was the biggest issue. Fear of potential online fraud was a very real concern for many we spoke to. With a number of reports from the focus groups that people had been victims of fraud or scams and one participant admitting that they wrote down passwords, there is a real concern that the pressure to be online may also lead to consumers becoming vulnerable because of poor digital security.

> *"I'm just scared...some people might get my information or something and it might be something I do wrong." (Older group, London)*

This concern about the risk of fraud when using digital platforms is a clear barrier for some consumers, preventing them from easily comparing prices or accessing information about switching.

Customer relationships and loyalty.

Apart from the energy that it took to keep switching providers, there emerged a real wish for a relationship with service providers that went beyond the transactional. We found a tacit rejection of the values underpinning the market; that cost was the only factor by which people should or do choose an energy supplier, for example. Many that we spoke to actively wanted a positive relationship with service providers, to demonstrate relationship loyalty and receive the benefits for being loyal. As already discussed, trust was primary, and trust is built over time.

A surprisingly high number believed that they were currently rewarded for loyalty, particularly among telecom companies.

> *"…because if you build up a relationship with the company… I don't know of any other provider but I know Sky they're very good at looking at how long you've been with them and how faithful you have been with them and then the adjust the tariff." (Older group, London)*

Whether this results in the best tariff for the customer is not known, but the perception of being rewarded is real. Often customers negotiated with their current suppliers, and felt that their loyalty was recognised. In general, there was more enthusiasm for negotiating a better deal with an existing company than there was for constantly switching between providers.

Conversely, there was a lot of criticism for the practise of increasing tariffs or prices, which resulting in existing 'loyal' customers paying more.

> *"It should be the other way around, they should be trying to want to keep you but they don't, it doesn't seem like they have loyalty and they're not worried, as long as they have some customers they're not worried." (Young family group, Plymouth)*

Again, this demonstrated how current business practises are often perceived as untrustworthy by customers.

For some, however, they admitted that the longevity of the relationship with some providers stemmed from a form of inertia, albeit one that showed loyalty, and that they were happy with.

> *"I stayed with mine for 14 years because you get comfortable with the company and you know how the customer service is." (Working age group, London)*

4.3 EXTERNAL BARRIERS TO GETTING THE BEST DEAL

Credit rating/debt or banking facilities

As well as impacting on the ability to access affordable or any credit, poor credit scores and current debt were clear barriers to switching for some participants in our focus groups. This was particularly noticeable when discussing telecoms contracts, as poor credit ratings were felt to effectively remove the option of switching. In some instances, knowledge of their bad credit rating put people off even trying to switch to a better deal:

> *"..if you've got some sort of like problem with your bank, credit, you can't switch anyway....which is where we've found the problem is it's completely out of the question....So even if it's cheaper we can't do it." (Debt Advice group, Plymouth)*

Housing tenure

Those who were in rental accommodation often had less control over choice of provider than homeowners. Some reported that they were unable to choose their energy provider because of arrangements made between landlords and providers. One woman, who had recently moved into a new housing association flat, would have preferred to remain with her previous provider. Her landlord set her up with their choice of provider, and she is now tied to this one for a year. Another told of how electricity charges are included in their rent, but when the amount doubled, was unable to do anything to reduce the costs.

One private tenant was told that she was not allowed to change providers for any services, under threat of a £3,000 fine, and it was only with encouragement from her family that she had the courage to change anyway. It quickly became clear that this threat was baseless, and may have indicated a financial agreement between the provider and the landlord.

The extent to which tenants are able to switch providers to get a better deal, therefore, is hampered by contracts signed on their behalf, and by a worrying level of misinformation.

4.4 BARRIERS TO AFFORDABLE CREDIT USE

Table 4.3 Level of credit use

Credit usage in the last 12 months	Any form	HCC
None	48%	73%
One type	25%	18%
Two types	15%	6%
Three types of credit	7%	2%
Four or more types of credit	5%	1%

(base=1,000)

Our survey of Turn2Us clients found that overall, 52 per cent had used some form of credit in the last 12 months, with 27 per cent using a form of high cost credit. Fewer than one in ten had used more than one form of high cost credit in the last few months. Mainstream credit was considerably more prevalent than high cost credit; only subprime credit cards were more common than the three types of mainstream credit used. The most common form of credit, use of an overdraft facility, is not necessarily cheaper than use of high cost credit, depending on the charges levelled and the how often the facility is drawn on.

Table 4.4 Type of credit used

Types of credit used	% of sample
Overdraft	26%
Credit card from mainstream lender	24%
A credit card from a subprime lender	12%
Personal loan from bank, BS, or CU	10%
Mail order catalogues	10%
A personal loan from a subprime lender	6%
Home collected loan	4%
Payday loan	4%
Pawnbroking loan	2%
Rent to own store	2%
Christmas food hamper scheme	1%

(base=1,000)

Why use credit at all?

As would be expected from the survey, as well as previous research finding (for example Collard et al 2013), there was relatively little current use of high cost credit across the focus groups, although some did have previous experience. Overall, most avoided using credit as far as they could, particularly for day-to-day items. When needing to buy bigger items, such as furniture or white goods, interest-free credit was sought out. Some bought furniture from DFS, or from IKEA in this way:

> *"You just need something then you can go to the interest free option, because you are not paying anything extra, you're just paying the money." (Working age group, London)*

The most common response to enquiry about credit use, however, was that they had just learned to manage without it, particularly those whose previous experience of credit had led to financial difficulties. Where there was use of interest paying credit, whether on a credit card, or through catalogue usage, as with interest free credit, it was mostly to buy essential white goods, or furniture, although there were a few instances of people using home credit loans to pay for Christmas. Given the struggle that many had to manage on their incomes alone, it is not surprising that there was a need to borrow to cover the bigger costs, and generally most people used the cheapest credit open to them.

The importance of white goods to the functioning of many households is reflected in the costs that are incurred to purchase them. It is also reflected in the high levels of appliance insurance among low-income groups, discussed in the next section. These costs of buying and running the appliances are weighed up against the detriment of not having one, even for a short period, and this can result in choices that are more costly than they may need to be.

> *"When my tumble dryer went [partner] took out a credit card because it was, you just cannot physically dry your washing indoors in this weather and we were still paying, we're still paying the credit card off now even though that tumble blew and we've had to buy a second hand one." (Young family, Plymouth)*

It isn't necessarily a lack of understanding of the costs incurred, but that the costs were accepted as the price to keep their households running.

In general, there was little evidence of any misunderstanding around the costs of the different types of borrowing; those who had used higher-cost credit were fully aware of how much it cost, and many were clear that they used this through lack of other options at the time. For some, it was because their credit rating excluded them from better value credit, and for others, the immediacy of their needs, or the emotional pressure they are under may make it difficult to make rational choices.

> *"even though I have experience and I do, but because I was in such a desperate situation at that time I just went with the price, I didn't look at the interest rate and usually I'm so savvy like that." (Working age group, London)*

Lack of awareness of sources of affordable credit did not appear to be a great barrier to accessing it. Overall, there was knowledge of the different types of affordable credit available, although individually it varied. As already noted, most were aware of sources of interest-free credit and Credit Unions were mentioned in all groups, and discussed in detail by one man in the older group, and by a respondent in the debt advice group.

However, in these instances, both men had applied for a loan from a Credit Union, but were refused because of their high risk and bad credit rating. In one instance, the man found a costly alternative:

> *"They give people loans when you're on benefits and not working and I was really surprised by that, I got 500 quid out of them. It's not exactly cheap is it, I mean they still want 300 quid back on top of it but it's only like 30 quid a month paying back, so..." (Older group, London)*

This perhaps highlights the limitations of affordable credit as a way of reducing the credit poverty premium; those who feel they need to access credit will only be left with high-cost lenders. One mother in the group, who had been refused a loan from a credit union remarking *"it was a big fat no"*, had used home credit loans to pay for their Christmas spending last year. She reported that she was practically paying back double the amount she had borrowed.

> *"They prey on people they know that have got low credit scores and the only way they can get credit or can get money is through these companies because they charge so extortionate rates." (Young family group, Plymouth)*

Others were aware of the predatory practices of some lenders that can lead people into financial difficulties. The potential for financial detriment that was inherent in an overdraft facility was noted, along with the practices where banks automatically give them to people who didn't request them and possibly shouldn't have them.

Nonetheless, there was a general agreement that for most people nowadays, there would be occasions when they had to access money that they didn't have saved.

> *"you have to have a credit card sometimes to bail you out because else you're gonna be like a month where you're sorry you're not gonna have anything to eat this month because I've just had a whole load of bills to pay." (Young family group, Plymouth)*

Credit, therefore, was used primarily to cope as a last resort, and the cost of that credit generally reflected the choices that the lenders made, rather than the preference of the borrower.

Given the paucity of income, Government grants or charitable funds were considered the best alternative to borrowing for those who qualified for them. Focus group participants whose income was too high to qualify for the grants, but who were nonetheless in poverty, were understandably resentful about the fact that their needs were not recognised. Those who were able to borrow from family or friends discussed this as a preferable option to taking out formal credit. However, not everyone had the choice and this type of borrowing can lead to additional pressures.

4.5 BARRIERS TO USE OF INSURANCE

Table 4.5 Levels and types of insurance held

Insurance used	% of sample
Motor vehicle insurance	44
Home Contents insurance	44
Building cover insurance	27
Mobile phone insurance	11
Household appliance insurance	8
Critical illness/ income protection	4
None of the above insurances	34

base=1,000

Fewer than half of all Turn2Us clients in our survey had home contents cover, and around one third had no insurance at all. Over half of those who were under 35 were completely uninsured (52%) on the types of policy we asked about, significantly higher the older respondents. Age was also a significant factor in likelihood to hold home contents insurance, with likelihood to hold it rising with age, and homeowners were significantly more likely to have contents insurance than those who rented, whether privately or through social housing (81% cf. 27% and 29% respectively)

In some respects, insurance is the flipside of credit; the purpose was mostly to enable those who couldn't afford to spend a lump sum from savings or incomes to access the goods that they considered to be essential. In the focus groups, this emerged strongly as the motivation for having individual appliance insurance or mobile phone insurance.

> *"I do cover everything [appliances]...Because my appliances they work hard, you know, with a lot of children they're constantly on the go, fridge constantly opening and shutting, hungry children and all that, so yeah they've gone several times and if I had to replace them..." (Working age group, London)*

While the value of the appliance insurance to those who held it justified the cost, it also negated the need for broader contents insurance for some people. One woman was reluctant to take out contents insurance, as her appliance insurance covered the key items that she needed, resulting in the contents insurance then appearing to be an 'extra' cost. In general, contents insurance policies do not cover the breakdown of white goods, unless the damage comes from an external factor such as a flood, or possibly if accidental damage cover is included. As this will not cover breakdown outside of the warranty period, it may not in fact be the most appropriate product for many in low-income households. Individual appliance insurance often seems the more suitable protection under the circumstances.

> *"... it was only a few pound a month but when I worked it out I thought well if that goes wrong after my 12 month guarantee I can't afford to buy another one so I worked it out and it works out good." (Young family group, Plymouth)*

Some people avoided insurance completely, particularly contents insurance, because of a lack of trust that the insurance company would pay up in the event of a claim. Stories were told of boiler cover that did not actually cover breakdown, only servicing, and furniture insurance that only covered the sofa for fire and theft. Another participant had realised that her microwave cover cost 50 per cent of the price that she paid for the microwave, and as such did not represent good value. All these stories contributed to a general feeling of mistrust around insurers, and insurance products, and perhaps deterred some from looking seriously into taking it on. The exception to this was car insurance, which was perceived as a necessity, as well as an insurance that was easy to understand, and to compare different benefits.

However, it was also clear that increasing pressures on income meant that some people lacked insurances because they did not have the money to pay for it. As with many areas of spending, it was accepted that their ideal standards were lower than they had been 10 years ago; when talking about the lack of mobile phone insurance, one woman noted "I think we've all just learned to live with broken screens."

However, the potentially disastrous consequences of not having insurance when needed were recognised, but talked of in a fatalistic way:

"See I don't have any but I do want to get some, because my friend had a fire last year and she didn't have anything and lost everything…yeah that's the sort of stories that makes me think ooh…But then everyone always thinks it won't happen to me." (Young family groups, Plymouth)

Those who couldn't afford to take out appliance insurance had to either borrow from friends or family or take credit to replace an item.

5.
THE IMPACT OF THE POVERTY PREMIUM

How are financial difficulties felt in low-income households, and what is their impact?

In this chapter we use our survey and focus group data to consider the factors causing financial difficulty, the impact this has on low-income households, and how these are reflected through the poverty premium. Two broad themes emerge: the effect of having an increasingly constrained income combined with rising living costs, and the challenges of making optimal decisions when stressed or under significant time pressures.

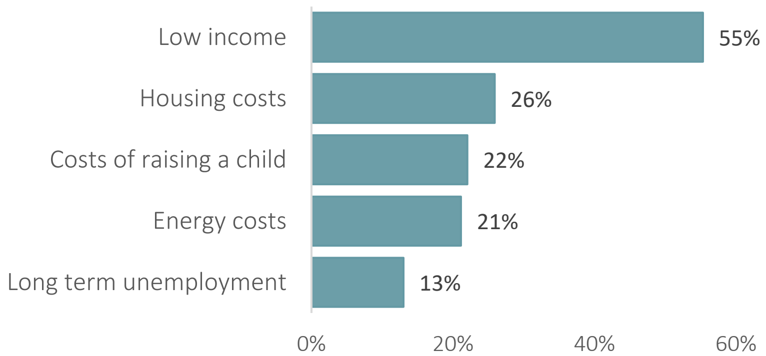
We specifically explore the impact of the poverty premium on:

- people who are unemployed or in insecure work;
- those with young families;
- those who have sought advice about financial difficulty; and
- older people.

5.1 WHAT FACTORS WERE CAUSING FINANCIAL DIFFICULTY?

As well as looking at how people were accessing and paying for services, we asked survey respondents about the factors that had had a negative impact on their financial situation over the last 12 months. The following figures explore the key factors.

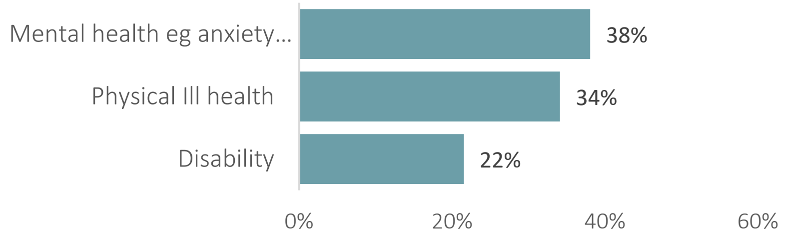
Figure 5.1 Percentage of households where general income/outgoings had a negative impact on financial situation



As Figure 5.1 shows, the most common factors that had negatively impacted on the financial situation of our survey respondents was, essentially, the fact that they were on a low income. It was the general costs of life along with not enough money that was the biggest cause of financial hardship in the last 12 months.

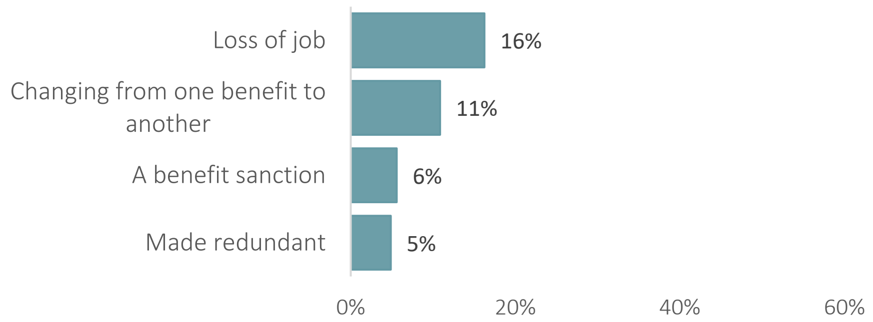
Those of working age, under 55, were significantly more likely to say that low income was negatively impacting on their life than older respondents, as were those in private or social rented accommodation. In terms of working situation, it was those who were insecurely employed, those who worked part-time, self-employed or on a casual contract for whom low incomes were significantly more negative. Households in private rentals were more likely than home owners to struggle with costs overall, and more likely than any other form of tenancy to suffer hardship due to housing costs (40 per cent).

Figure 5.2 Percentage of households where health had a negative impact on financial situation



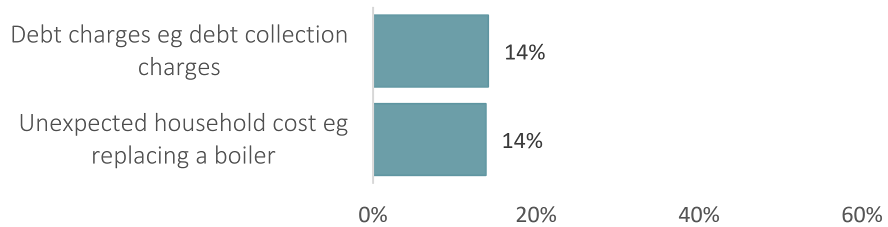
Survey respondents who were unable to work, as well as those who had a disability were, unsurprisingly, significantly more likely to have suffered financially as a result of health-related factors than others. Single people were more likely than those who were partnered to have mental health issues impact on their financial situation, but the opposite was true for the financial impact of a disability. Those of retirement age were less likely to have suffered financially as a result of mental health issues than those of working age. Those who were nearing retirement age (55-64) were the most likely to have been affected by physical ill health.

Figure 5.3 Percentage of households where an income drop had a negative impact on financial situation



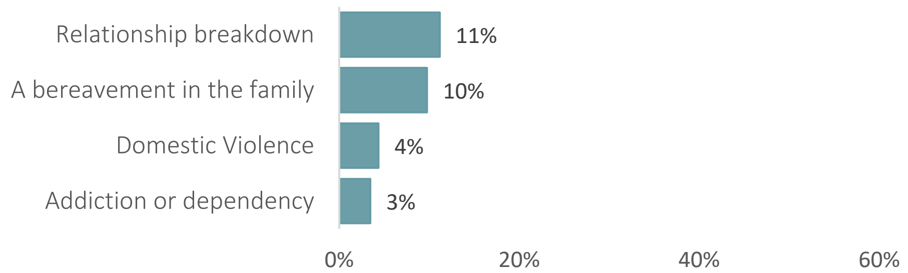
Job loss was three times as common as redundancy among the households in our survey, suggesting a high level of insecure work. Those who were actively seeking work were most likely to have suffered as a result of a drop-in income, with 41 per cent impacted through a loss of job in the last 12 months, and 14 per cent impacted through redundancy, far higher than the numbers shown in Figure 5.3 above. Homeowners were significantly less likely to have been impacted by benefit sanctions than those who rented. Couples were more likely than those who were divorced or widowed to have suffered through job loss or redundancy, although this may be as there are more adults in the households to be impacted.

Figure 5.4 Percentage of households where unexpected costs had a negative impact on financial situation



As seen in Figure 5.4, approximately one in seven low-income households in our survey had been negatively impacted by an unexpected cost. Homeowners were more likely than any other form of tenant to have incurred unexpected household costs, but debt charges were most common in those aged under 35, with nearly one quarter (23 per cent) suffering financially as result of them. Those who had some form of disability were also more likely to have been impacted by debt charges (17 per cent).

Figure 5.5 Percentage of households where life events had a negative impact on financial situation

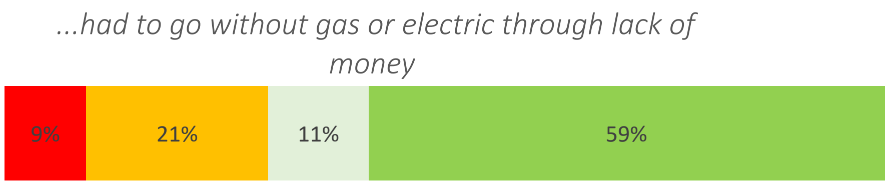


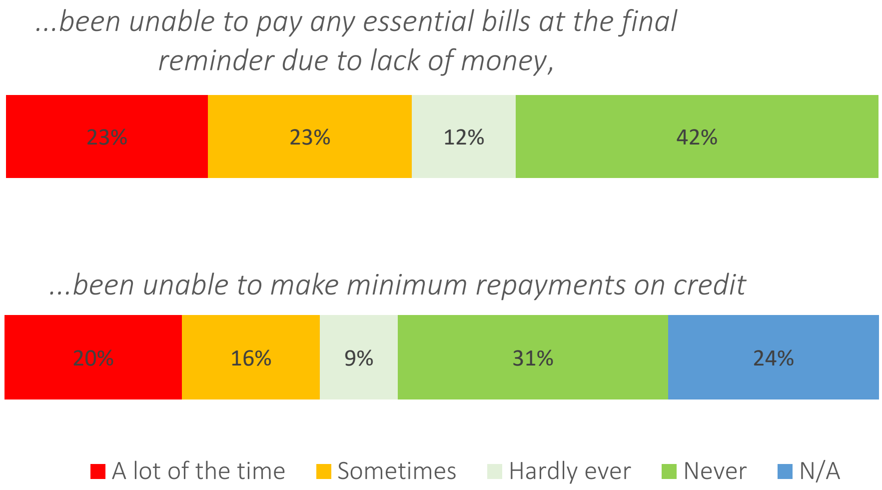
Older households, those aged 55+, were significantly less likely to have been impacted financially by a relationship breakdown than those in younger households. Single people were more vulnerable to financial difficultly through all types of life events than couples, although perhaps unsurprisingly, those who were divorced or separated had also been affected by relationship breakdown or domestic violence.

5.2 WHAT IS THE IMPACT OF FINANCIAL DIFFICULTY?

The impact of stagnating wages and benefits over the last 10 years on low-income households is clear in the findings from both the survey and the focus groups. From the survey, it was those under 35 who were struggling and the most likely to be falling behind on their commitments, or going without gas or electricity, and those over 65 – particularly those who were retired – who were the least likely to be. Perhaps unsurprisingly, homeowners were managing better than those who rented. Fifteen per cent of those in social housing were going without gas or electric a lot of the time, due to financial constraints. Those who were unable to work were also struggling, with nearly one third (30 per cent) falling behind on bills a lot of the time.

Figure 5.6 In the last 12 months, how often have you…





How do people in poverty experience the poverty premium?

There were varied experiences of poverty and financial struggles among our focus group participants, depending on their circumstances. As demonstrated in the survey findings, and as is more widely documented,[21] those who were retired were generally managing better than those of working age; they had a greater stability of both incomings and outgoings. Nonetheless, this older group found it hardest of all to get the best deal, and still struggled with constrained finances generally. The costs associated with bringing up children are a burden, even to those in working families.

Before we explore some of the specific ways in which poverty and the poverty premium can impact on different groups of people, there were two themes which appeared more broadly across the research: firstly, long-term, low incomes are fundamentally a problem. Persistent low-income levels make it hard to manage and impose constant short-term juggling of finances. Constrained budgets do not allow many households to access cheaper alternatives and over time this manifest as substantial risk aversion.

It was also evident that decision making during times of heightened stress or when substantial time pressure existed resulted in less well considered actions or sometimes a withdrawal from engaging with markets. For example, taking out expensive credit to buy essentials at the start of a tenancy or no longer switching supplier.

Unemployed or in insecure work

Our focus group participants with insecure work, or who were unemployed, faced very constrained budgets. There was a consistent message that people do not have enough income to live on and that rising living costs alongside changes to the welfare system are causing distress. It was acknowledged that switching and shopping around can save money, but do not address the underlying issue of inadequate incomes

[21] https://www.resolutionfoundation.org/publications/the-generation-of-poverty-poverty-over-the-life-course-for-different-generations/

"People's incomes are, have stagnated, there's no way even if you're a financial genius you can make...those sorts of amounts stretch to all the things that people need." (Older group, London)

Unsurprisingly, the system of Universal Credit was raised as a concern. A number of participants related how the amounts they are apparently entitled to were changed, and the financial difficulty that waiting for the first payment could cause.

"The worst thing is you get switched over without you being told, I didn't know I was on it... 3 weeks before they got me an appointment at the Job Centre, went in there and then they said oh we don't need to see you until May and then I had to wait another 2 weeks for them, so it was like 5 weeks of no money, borrowing off my mum." (Young family group, Plymouth)

Periods such as these are often the trigger for borrowing in desperation, or falling into arrears, which could have long-lasting consequences.

Irregular incomes more broadly could be a source of financial difficulty, and had implications for the ability to pay in the most cost-effective way. Many participants did find a way to account for times when budgets were tighter by restricting their usage of gas or electricity for a while, or by paying for larger items when their Universal Credit payment, or another larger amount, went into their account. However, this means that they are not able to benefit from the cheapest direct debit deals, or again, may need to borrow if they are unable to balance their budget efficiently enough.

Quite a few of those who were unemployed had accessed grants, budgeting loans or even white goods via charities which had helped them to manage. Foodbank use was also referenced as necessary and had been accessed by a number of working and non-working households. Additional benefits, such as free prescriptions or free school meals were mentioned by struggling families. However, those who were part of the 'working poor' focus group participants were unable to access these, and this was a source of resentment, particularly for those who had ended up relying on credit to manage instead.

"I can't get a grant, nobody will help me because even though I'm on low income. They look at it and think, your husband is working you've got 5 kids, we're not helping you." (Young family group, Plymouth)

Those who were working were also more likely to need car insurance, and as this is clearly an expensive item. Interestingly, few saw this as a particular burden, perhaps as they would be unaware of the costs that people in other areas paid, and in fact sometimes used this as a way of getting value through extra breakdown cover, or accessing otherwise unaffordable items like cinema tickets.

Young families

The poverty premium is often hardest on those who are participating most in all aspects of life, and as a result, parents with dependent children were particularly affected by the poverty premium in the energy, insurance and credit sectors. The overriding concern for parents was to do the best for their families and this resulted in a focus upon keeping control of spending on energy, the occasional use of credit for essentials like white goods and sometimes for social or cultural events like Christmas. Their outgoings in particular were very up and down, and the constant juggling of budgets was clearly a source of stress. As already noted, many families incurred the costs of appliance insurance, to ensure that they were covered if essential items were to break, avoiding unexpected costs where possible. The worry and anxiety of being without essential household items was evident in many of the discussions. For those who couldn't afford to insure their items, how they would cope in an emergency hung over them:

> *"I don't have a support network to borrow off anybody, so if something drastically went wrong I would have to go without until I could literally save up to buy it." (Young family group, Plymouth*

This was the group with the highest levels of borrowing. Home credit, credit cards, loans and overdrafts were discussed as formal credit options, but informal lending from family was also common. While this family support was invaluable to those who had it, those who didn't felt this left them with fewer options. While no one wanted to borrow, the pressure to provide secondary school-aged children with phones, clothes and costly uniforms clearly lay heavily on many, with hard choices to be made about what is and is not possible, and the extent to which they felt they needed to buy expensive goods for their children. While the discussion acknowledged that some children were happy with clothes that were cheaper, it was harder as children became teenagers.

> *"I think when they're in secondary and all their mates are wearing designer then they know…You're feeling more pressure then." (Young family group, Plymouth)*

Mothers did not want their children to miss out, and this did sometimes result in borrowing to pay for Christmas. Again, those with family support were lucky to be able to mitigate some of the pressures at this stage too.

> *"Once she gets older it's like just calling in favours from grandparents saying this is what she wants for Christmas so making sure she gets what she needs from other sources." (Young family group, Plymouth)*

However, this group was already doing all they could to minimise the energy-based premiums – switching levels were high, and parents spoke of monitoring heating costs very carefully – and when necessary going without or only using minimal heating at home in order to pay other household bills. This self-regulation of fuel appeared to be a normal occurrence for parents with primary aged children.

In financial difficulty

Those who had sought advice for previous and ongoing financial difficulties tended to have the most consistently constrained budgets. The margin of error was often so tight that the risk of even small unexpected costs was a barrier to switching. Participants discussed alternative strategies to save money including reducing consumption or going without rather than switching supplier. Similarly, payment methods that maximised control were favoured, prepayment meters and standing orders being mentioned specifically, meaning that again, the cheaper direct debit options were not considered because of the risk of additional or unexpected costs.

This group all had poor credit ratings, which further limited or removed the ability to switch or shop around for utilities, including mobile and broadband. The shame felt at having run up so much debt, meant that few even tried to switch providers (or applied for credit) in case they were turned down. Explaining that she hadn't tried to switch because of a poor credit rating one mother explained:

> *"No, I'm too embarrassed to, you know, if they went on that computer and did a credit search I would just die." (Debt advice group, Plymouth)*

This also meant that some were tied into particularly expensive mobile phone, or insurance contracts, that may not even be the most suitable service for them. One woman who explained she did little online, for example, had a 30GB data contract with a supplier she had been with for 17 years. She was unable to switch because of her credit rating and the large cost of her contract was suggestive of the long-term price creep for 'loyal consumers'.

Those experiencing financial difficulties often faced additional challenges including ill health, the challenges of navigating the benefits system and having caring responsibilities. Quite often, these were in fact the reason why their financial situation had ended up in the position it did. It was not always possible for them to find the mental 'bandwidth' available to navigate the complex and time-consuming process of 'getting a good deal' on top of substantial existing day-to-day demands.

One part-time worker, when she would run out of money before her pay date, would book annual leave from work for the end of the month, knowing she would run out of money before her pay date and couldn't afford to travel there. Clearly, in these circumstances, switching to the best deal is unlikely to be a high priority. Her income was far below her essential outgoings, and as such, no amount of 'savvy shopping' would have balanced the books. The issues of 'negative budgets' where monthly expenditure exceeds monthly income is becoming increasingly common among people seeking debt advice[22].

Older people

It was in the need to be an active consumer in the energy and insurance sector, switching and negotiating a good deal, where the elderly were most disadvantaged. Companies did not seem to account for the differing needs of consumers:

> *"how could you ask a 90 year old to go online, do online banking…?" (Older group, London)*

Younger people also recognised the difficulty that many older people had, and told stories of older sisters, grandparents, neighbours and friends who struggled to navigate the current system and were being disadvantaged as a result.

[22] https://www.stepchange.org/Portals/0/documents/Reports/2018-statistics-yearbook-stepchange-debt-charity.pdf

"I can get it a lot cheaper than that… but some [older] people don't have that support network and will just go okay I'll pay that because that's what it is." (Working age group, London)

However, many friends, family and advocacy organisations were attempting to disseminate information to the older population because messages about the benefits of switching suppliers, comparing prices or discounts that may be available are not reaching them.

This disadvantage was related primarily to digital capacity. It was clear that the older participants in our group were perfectly capable of understanding how to get the best deal in terms of grocery shopping, for example, or in other areas that they were familiar with. For those who weren't comfortable online, however, this resulted in exclusion from any number of savings or grants.

" We'll stay where we are, and we won't ask for all these things because it would be a lot of messing around. …. you might be entitled to like a bit of relief for your gas you know, like water, but my missus was saying, well it's probably too much trouble… I'm not computer literate and I'm sort of like dyslexic" (Older group, London)

Some older consumers had developed good digital skills, often explaining that a friend, relative or community organisation had 'held their hand' through a sometimes long process of learning how to use and trust online banking or navigate the internet. Nonetheless, there remains a substantial digital divide in relation to access, skills and trust.

It is concerning that older consumers are perhaps incurring the largest poverty premiums by not switching, even though the survey suggests they are managing better financially than younger people. It raises the question of what they may be going without in order to maintain their budget. Some appeared to be reducing food costs and removing social activities like eating out in order to minimise costs. Older consumers spoke at length specifically about restricting and reducing food costs, which may be reducing their ability to eat healthily.

"…although people said eat healthy food but you can only eat, you eat healthy food to the amount you can get. You can buy some healthy food and then you've got to look around to balance it…" (Older group, London)

Money was also saved through lack of social activities and removal of any other discretionary spending. Rationing heating was not discussed by older consumers, but it may also be prevalent. It seems that older consumers are making significant sacrifices in order to accommodate the additional costs of the poverty premium, even if this isn't always consciously acknowledged.

6.
WHAT WOULD HELP REMOVE THE POVERTY PREMIUM?

In this section we explore user-led solutions that may help people in poverty to pay less for essential goods and services

During the focus groups, we asked the participants about what kind of solutions they felt would help them to get a better deal, as well as asking them to respond to some potential solutions that we introduced to them. Below we discuss some of the key areas where there may be potential for cutting the poverty premiums that people pay, based on the views of people who pay them.

6.1 USE OF TECHNOLOGY AND DATA TO REDUCE THE POVERTY PREMIUMS

In terms of the 'switching' poverty premium in particular, there is potential for technology to make it easier for people on low incomes to access the best deals. As with switching generally, the biggest barrier to consumers using technology in this way is a lack of trust.

Automatic switching to better energy and insurance deals

We introduced our focus group participants to Youtility[23], an app that uses open banking data to find out how much people are paying for their energy, telecoms and insurance, and then automatically switches the user to the cheapest tariff for them. Participants who were already comfortable with switching, particularly the mothers who switched regularly, could see a great benefit in having the hard work of comparing tariffs done for them:

> *"the amount of time I spend ringing up companies and trying to haggle prices and working out if I can save money here, there and everywhere, I spend hours beyond hours, it's unbelievable. But I usually have to do that all really late at night because I've got kids, I don't want to sit there on technology when I've got my children." (Young family group, Plymouth)*

There was some reluctance among participants to give companies access to their banking data, even among those who were comfortable with switching online. However, our survey found that switching is becoming more commonplace among low-income consumers, so we may also see the same trend with open banking over time.

While apps like Youtility may offer a clear benefit to those who already switch, or are considering switching, it is not clear if it can resolve issues such as overlapping payments, security, or the possible financial impact on the customer if the energy company they are switched to closes down.

Access to lower-cost credit

Open banking has the potential to reduce the credit poverty premium, because it offers credit reference agencies the opportunity to include a wider range of data when producing a credit score (Reynolds 2017). One such company is Credit Kudos[24], funded by Fair By Design, who are working with Credit Unions to help improve their ability to effectively judge the credit risk of potential borrowers. For potential borrowers with a limited credit history (often called a 'thin file') or those whose financial situation has improved since defaulting on

[23] https://youtility.co.uk/
[24] https://www.creditkudos.com/

payments in the past, this may help them pay less for credit. For example, the mothers in one of our focus groups who were using costly home credit as a result of a poor credit history could, in theory, benefit from this service. There was no indication that they were defaulting on their home credit loan payments, for example.

For others, such innovations are unlikely to have much impact. The evidence shows, for example, that use of home credit, or buying goods from Brighthouse are often not only about the cost of the credit; the use of mainstream credit such as overdrafts and credit cards is far more common than high-cost credit use, and for some, borrowing is simply not the answer. We also had examples of people in the focus groups turned down by affordable credit providers for what appeared to be good reasons.

Based on the present evidence, therefore, it is important to look at other ways of reducing the cost of credit premiums if more people are to benefit. The 2019 calculation of the poverty premium (Table 3.2) in fact showed a sharp increase in the costs associated with the use of high cost credit in comparison with 2016, notably for those who have taken out some form of loan. This may in part be explained by the fact that home credit is not subject to a price cap. It could also suggest that, as the payday market has evolved as a result of tighter regulation, low-income consumers are paying more to borrow over longer periods of time (e.g. three months rather than a month). To avoid the creation of new credit poverty premiums therefore requires more effective mitigation of these sorts of 'waterbed effects'.

Automatic entitlement to grants and preferential tariffs

Among our focus group participants, the use of data to facilitate automatic entitlement to any grants or preferential tariffs was perceived to be of great benefit. In each group, only some of those entitled to the Warm Home Discount (a discount of £140 from their electricity bills for people who receive certain income-based benefits) had heard of it, let alone received it. There was a strong belief that people who were entitled to it should receive it automatically, as it already relies on data sharing.

> *"Warm Homes Discount, it does state at the bottom you have to tick some boxes to say that you, you know, you're happy to give consent for them to access your data on the records," (Working age group, London)*

Participants were generally supportive of the idea of this type of data sharing where it was to their benefit, as long as they trusted the organisation that held the data.

Even simpler technology could play a role in helping people save money. Some focus group participants suggested that companies could use text messaging to notify customers when their fixed rate deal is coming to an end, as an alternative to automatic switching.

6.2 ENDING THE 'LOYALTY' PENALTY

As we saw in chapter five, many focus group participants did not want to switch providers and felt it unfair that many companies penalised loyalty. In this respect, the poverty premium reflects a clear mismatch between the needs of low-income customers and the way in which these markets function. The Citizens Advice super-complaint to the Competition and Markets

Authority[25] in 2018 highlighted the widespread detriment caused by the 'loyalty penalty', noting the particular vulnerabilities of low-income customers that prevent their effective engagement with markets. Our research reinforces these findings and lends weight to strategies such as principle-based regulation (Citizens Advice 2018, p.46), placing responsibility back on companies to ensure that their pricing is fair to customers, along with better targeting of vulnerable customers. Indeed, a fair few of our focus group participants said they would be happy to see 'everyone paying the same'.

6.3 FLEXIBLE OR PERSONALISED PAYMENT SCHEDULES

Our research clearly shows that timings, methods and amounts of payments can play a causal role in some key poverty premiums. The gap has grown between the cost of energy for those who pay by direct debit, and those who use other payment methods, not just in terms of the cost paid, but in terms of switching to the best tariffs. The gains are higher for those who pay by direct debit, and direct debit users have much higher rates of switching; 57 per cent of those who paid by direct debit had switched tariffs in the last two years compared with 40 per cent of those who paid on receipt of bills and only 31 per cent of those who used a prepayment meter. While the regulatory caps in tariffs has lowered the difference, the best direct debit tariff is still more than £130 cheaper than the best pre-payment meter tariff.

The benefit to low-income households of control over payment methods is already recognised (Ellison, Williams and Whyley 2015), yet there was little evidence that this has resulted in a change in practice from companies.

Allowing easy overpayments may help low-income households to budget in a manner that helps them to avoid 'pinch points'. One mother told us how her council tax bill was £27.22 weekly, but that she always paid £30. This meant that every few months, she was able to skip a week's payment without fear of arrears. Other focus group participants used lump sums to put towards bigger expenses when they could:

> *"I got a tax refund not long ago, £500 and I like put quite a lot on my Amazon account and put on gas and electric and it helped get [son's] bike." (Young family, Plymouth)*

However, these payments still need to be within the control of the payee rather than by direct debit because flexibility is so highly prized, as one of our older focus group participants explained:

> *"when we go to the Post Office they say why don't you go the cheaper one, but the only trouble is with BT they are good because a bill comes in and you pay in the middle of the week, they say right you can do half now and the other the end of the month and they do it." (Older man, London)*

[25] https://www.citizensadvice.org.uk/Global/CitizensAdvice/Consumer%20publications/Super-complaint%20-%20Excessive%20prices%20for%20disengaged%20consumers%20(1).pdf

Our focus group participants would welcome more opportunities for penalty-free ways of under- and over-paying, helping eliminate this particular pathway to the poverty premium.

6.4 TIMELY INFORMATION AND TRUSTED INTERMEDIARIES

It emerged that easy access to better information could make a difference to those focus group participants who were on expensive energy tariffs. Some of those we spoke to were reluctant to switch tariffs as they didn't know whether their tariff was a good deal or not. During the discussion it became clear that some people were paying high costs but hadn't realised how out of line their tariff was compared with the average. Comparative information could help let people know what fair or reasonable costs would look like.

> *"They should compile what it costs for each area, this is what it would cost you to heat your home, this is what you're paying, you know, you could actually save money, ...that way people could see ...hold on a minute I'm actually paying a lot more than I really needed to." (Working age London)*

This was most pertinent to the older age group, who appeared to be particularly vulnerable to a lack of knowledge. This chimes with low knowledge of eligibility for the Warm Home Discount reported earlier, which meant that households in need were losing out on £140 per year. All participants agreed that there must be better ways of making sure that individuals got the help they were entitled to. In fact, it was not clear how those who were not in touch with advice agencies, for example, would know to look for it. One family had been helped financially through access to Watersure[26], a scheme that caps the water bills for certain eligible households. They only knew of this scheme as they were signposted to it via an advice agency.

However, it is also important that information comes from a trusted source. When discussing how to present information about average or fair costs, one woman noted:

> *"You know these companies, the energy companies they try and make it look as good as they can on their part, and they take the best figures." (Young family groups, Plymouth)*

Utility or telecom companies could signpost their customers to trusted sources of information, such as regulatory or government websites, to ensure that they are receiving any grants or support that they are entitled to. There was also felt to be capacity for social housing providers or local authorities to take a more active role in promoting clear information on energy and credit.

Organisations such as Turn2us, Toynbee Hall and Plymouth Focus offer valuable support to those who need it. Many of those in poverty have multiple vulnerabilities that mean they need some help to absorb and act on information.

[26] https://www.ofwat.gov.uk/households/customer-assistance/watersure/

> *"for someone who's never changed it's a big leap, for them to take that leap they need somebody who they can trust to advise them." (Working age group, London)*

However, once the hurdle of doing something differently was overcome, be that switching providers, or using a different form of credit, many of those we spoke to were then happy to handle the issue themselves. It was often a matter of confidence and practice. The investment in helping someone could provide an ongoing financial benefit.

6.5 ADDRESSING INADEQUATE INCOMES: TARGETED SUPPORT AND PREFERENTIAL TARIFFS

Inadequate income was the root cause of financial difficulties for many of our research participants. Reducing or removing the poverty premium will help some people on low incomes; for others any number of money saving changes will not make a qualitative difference to their income or living standards. Consequently, our focus group participants felt that people on low incomes should receive targeted support (particularly related to energy costs and consumer credit), as well as expanding eligibility for grants.

Through the WaterSure scheme, one family's water bills were reduced to account for their circumstances, and this made a huge difference to their bills. Other participants felt that similar help with gas or electricity bills would make a real difference to people who were struggling.

> *"if they can work it for the water why can't they work it for the electric. What makes it so different between electric and water?" (Debt advice group, Plymouth)*

At the very least, there was a feeling that people on low incomes should automatically be put on their utility provider's most favourable tariff. One woman had received something similar:

> *"I hadn't changed my tariff I got a letter from my energy company saying that I'm going to be on the standard tariff, but because I'm a Warm Homes Discount customer they are going to change me to a tariff which is slightly cheaper than the standard tariff, which is their standard practice now." (Working age group, London)*

However, as with the cap on tariffs, any discount is usually relative to the standard tariff, and not the best value, online-only deals. Any genuine attempt to provide those who are struggling will need to reflect the cheapest tariffs.

Many focus group participants were interested to buy white goods from lenders that operated like BrightHouse – but without the high costs. Some participants with young families noted there were charities that offered interest-free help with white goods. They wondered if this type of help could be extended to a wider pool of people who aren't currently eligible, for example by charging affordable interest rates on the goods, which could help reduce the high cost credit premium.

> *"like the charities that the school uses like where they offer things, they'll buy a washing machine, not physically give you the money, buy the washing machine and*

7.
RECOMMENDATIONS

POLICY IMPLICATIONS AND RECOMMENDATIONS

The policies, practices and innovations aimed at removing the poverty premium need to take account of the heterogeneity of poverty, and make sure that consideration is given to the impacts of different policies on different groups.

Regulators must play a key role in poverty premium reduction

The capacity for regulation to play a role in poverty premium reduction is demonstrable. Our updated calculations find that the Tariff Cap regulations implemented in 2016 and 2018 by Ofgem have reduced the domestic energy poverty premium. The findings also suggest that the Rent-to-Own price cap (2019) may have reduced the costs of buying goods in this way. *Widening the remit of regulatory caps, therefore, is an essential part of the poverty premium reduction strategy.*

In the domestic energy market, implementing a price cap on standing charges may be of real benefit to those who limit usage as a means to save money. For many retired, and single person households, the standing charge will form a substantial part of their energy costs.

In terms of the credit market, while use of mainstream credit cards and overdrafts does not necessarily produce a poverty premium, they are the most common forms of credit used by those on low incomes, and the high cost of these will be having a detrimental impact on their financial situation. The evidence suggests that the caps on the cost of credit, and on rent to own borrowing have had a broadly positive impact, although it is clear that capping costs is more effective in a comparatively simple market, such as gas and electricity provision, with less chance of costs being displaced elsewhere. *Nonetheless, without some form of cap on the cost of credit extending more widely to more forms of credit, then it appears unlikely that costs will reduce, and it will be difficult to reduce the substantive credit poverty premium.*

More broadly, the CMA needs to consider ways in which regulation may be effective (and needed) in ending the loyalty penalty. Although domestic energy provision was not part of the super complaint that is currently under scrutiny, our research found that the loyalty penalty was an issue in this sector, and is still to be fully addressed without a longer-term regulatory solution.

The FCA insurance market study explicitly recognises the need to address the 'price walk' that comes from renewing with the same insurance companies, yet it is the level of risk attached to living in an area of deprivation that it is the biggest constituent of the insurance poverty premium. *The FCA needs to consider what would be a fair risk pricing strategy within insurance.*

It is also evident that those who struggle with energy costs may well struggle to purchase white goods without credit, for example, and therefore a cross sector approach to understanding the particular vulnerabilities of poverty will produce the most benefit. Indeed, the cross-cutting nature of the poverty premium requires an approach that both understands and addresses the issues in a more comprehensive manner. The CMA should take forward previous scoping work on the poverty premium to accurately measure detriment across markets so the most effective interventions can be created, and to help easily recognise when one sector is treating low income customers unfairly.

Entitlement to fair tariffs or grants should be automatic

Our research has highlighted that many do not have the time, energy or, in some cases, the capability to ensure that they are on the best tariff, or that they have claimed any discount or rebate they may be eligible for. More of the responsibility needs to be placed on companies to ensure that they are giving the best value to the customer, whether that is letting them know that they are on an expensive tariff, and could switch to cheaper one, or automatically giving them the warm homes discount (WHD). All energy providers should be able to give the WHD to eligible customers, and the provider should be able to identify those eligible through DWP data.

Improving access to frictionless switching

Group switching or auto enrolment could also play a role in reducing the parts of the poverty premium that arise from inertia. Evidence from the Big London Energy Switch[27], and Ofgem[28] finds that collective switching can increase the number of households on the best tariffs. There may be similar advantage for low income households through auto enrolment in basic home and contents insurance, perhaps as part of rental contract, or home contents insurance as a 'benefit' provided by other services, such as a current account or employer.

All customers should be able to pay flexibly without penalty

Low-income customers need to have more control over how and when they pay for goods or services, without penalty, and the ability to over- and under-pay easily will allow this. For example, a rent flexibility scheme is currently being trialled to allow tenants of Optivo Housing Association to set up a personalised schedule of rent payments, accounting for known financial pressure points throughout the year. A greater range of businesses could give consideration to how similar schemes might work for their customers. Benefit

Understanding of the insurance needs of low-Income households needs to improve

Insurance can be understood as a 'hidden' poverty premium; while it constituted a substantial proportion of the overall premium, it was not perceived as such by the low-income customers we spoke to. While the recent regulation to prohibit selling extended warranties at the point of sale may reduce their usage, it is also clear that many take out these products because they offer the type of coverage required. As Aviva have produced a home contents cover that is designed specifically with the needs of low-income households

[27] https://www.londoncouncils.gov.uk/node/1648
[28] https://www.ofgem.gov.uk/ofgem-publications/156461

in mind, a similar, and fair priced, product aimed at protecting white goods would reduce the poverty premium.

Increasing the availability of white goods could be of benefit

Enormous importance was placed on being able to access white goods, such as a reliable washing machine or cooker, at very short notice. Finding an easy way of distributing affordable white goods to those on low incomes, or increasing the availability and eligibility of grants to pay for them, would be of considerable benefit to low-income families

Improve access to affordable credit

While our findings highlight the limitations of credit, affordable or otherwise, to help those whose income is too low to support any type of borrowing, there was nonetheless scope for others to use lower cost credit when needed. Use of open banking to produce credit ratings, as done by companies such as Credit Kudos[29], for example, has the potential to reduce the credit poverty premium, and to help those whose credit file may not reflect their actual capacity to keep up with repayments. To avoid data sharing merely replicating existing inequalities, however, the findings of the data sharing review[30] by Fair4all finance need full consideration.

[29] https://www.creditkudos.com/

[30] https://fair4allfinance.org.uk/wp-content/uploads/2019/11/Project-summary-Data-Sharing-Review.pdf

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APPENDIX A

Table of relevant poverty premium elements from 2016

Premium	Households incurring premium %	Cost of poverty premium £ / year	Average poverty premium £ / year
Any	**99**	-	**£432**
Use of prepayment meters	**33**	-	**£38**
Prepayment meter - electricity	32	£35	£11
Prepayment meter - gas	27	£35	£9
On best prepayment meter tariff	8	£227	£18
Non-standard billing methods	**50**	-	**£34**
Payment on receipt of bill - electricity	7	£38	£3
Payment on receipt of bill - gas	7	£38	£3
On best payment on receipt of bill tariff	1	£43	£<1
Home contents - monthly payments	32	£9	£3
Car insurance - monthly payments	31	£81	£25
Not switched to best fuel tariff	**73**	**£317**	**£233**
Area-based premiums	**73**	-	**£45**
Home contents insurance - deprived area	52	£14	£7
Car insurance - deprived area	52	£74	£38
Insurance for individual items	**23**	-	**£27**
Household appliance insurance	13	£132	£17
Mobile phone insurance	16	£60	£10
Access to money	**29**	-	**£8**
Fee-charging ATM	27	£25	£7
Pre-paid card fees	3	£25	£1
Higher-cost credit	**16**	-	**£47**
Rent-to-own	2	£315	£7
Payday loan	1	£120	£2
Home collected loan	3	£540	£17
Pawnbroking loan	<1	£50	£<1
Subprime personal loan	1	£520	£7
Subprime credit card	4	£194	£9
Mail order catalogues	6	£178	£11
Christmas hamper scheme	3	£47	1

(from Davies et al 2016a)

APPENDIX B

Table 1. Calculating the Annual Poverty Premium - Summary 2019

Area	Benchmark	Poverty premium	Notes
Fuel:			
Payment method: Prepayment meter	dual fuel, Standard Variable Tariff paid by monthly direct debit	**Premium = £57.05 / year** Split between gas and electric payment	Average across big 6 suppliers and across household size (low, medium, high usage) Prepayment meter compared with Standard Variable Tariff average cost for dual fuel direct debit payment.
Payment method: Payment on receipt of bill e.g. quarterly billing	dual fuel, Standard Variable Tariff paid by monthly direct debit	**Premium = £107.50/ year** Split between gas and electric payment	Average across big 6 suppliers and across household size (low, medium, high usage) Quarterly billing compared with Standard Variable Tariff average cost for dual fuel direct debit payment.
Not switching premium for dual fuel monthly direct debit payment	switched to the best dual fuel deal - online only, payment by direct debit	**Premium = £212.94 / year**	Average difference in cost across the best 6 deals for dual fuel monthly direct debt payment and online account management, compared with average Standard Variable Tariff cost across the big 6 suppliers
Switching premium for dual fuel prepayment meter users	Prepayment meter user on the best prepayment meter deal	**Premium = £131.10 / year**	Average difference in cost across the best 6 deals for prepayment meter compared with average of best 6 deals for dual fuel monthly direct debt payment and online account management
Switching premium for dual fuel payment on receipt of bill	standard (1/4ly) billing user on the best standard billing deal	**Premium = £143.35 / year**	Average difference in cost across the best 6 deals for Standard billing compared with average of best 6 deals for dual fuel monthly direct debt payment and online account management

Area	Benchmark	Poverty premium	Notes
Insurance:			
Home contents insurance - premium for living in a deprived area	average area annual cost (average of lowest 6 quotes) = £79.01	**Premium = £4.47/ year** deprived area annual cost (average of lowest 6 quotes) = £83.59	Specification based on: 3 bed end of terrace, private rented, lone parent with 2 children. Policy cover for £15,000 incl. accidental damage and £100 excess. Cost is based on the average price of the 6 cheapest quotes from a price comparison site. Average area: Timperley, Trafford - 50th percentile on Index of Multiple Deprivation. Poor / deprived area: Ribbleton, Preston - 20th percentile on Index of Multiple Deprivation.
Home contents - premium for paying monthly in a deprived area	annual cost deprived area = £83.59	**Premium = £9.74 year** average cost when paid monthly = £93.33	Annual payment compared with total cost when paid monthly using quote for deprived area (above)
Car insurance - premium for living in a deprived area	average area annual cost (average of lowest 4 quotes) = £787.31	**Premium = £297.65 / year** deprived area annual cost (average of lowest 6 quotes) = £1,084.97	Spec based on Minimum Income Standard: Ford Focus 1.6l, petrol, manual, mileage, 5 years old Policy holder: single female, lone parent, age 40, licence for 15 years, no convictions or claims. Policy: comprehensive, £250 excess, social and commuting, 9,000 miles/yr, kept at home on street parking, 5 yrs no claims bonus - not protected, Cost is based on the average price of the 6 cheapest quotes from a price comparison site. Average area: Timperley, Trafford - 50th percentile on IMD. Poor / deprived area: Ribbleton, Preston - 20th percentile on IMD.

Area	Benchmark	Poverty premium	Notes
Car insurance - premium for paying monthly in a deprived area	annual cost (deprived area) = £1,084.97	**Premium = £161.88 / year*** total cost when paid monthly = £1,297.53	Annual cost compared with total cost when paid monthly using quote for deprived area (above) *(*NB: calculated only on the premium differences where pay monthly was an option)*
Individual items/ appliance insurance	not used / no charge	**Premium = £176.91 / year** £14.74 / month	Based on a typical cost - policy covers a number of kitchen appliances up to £1,000 in value
Mobile phone insurance	not used / no charge	**Premium = £81.37 / year** £5.42 / month x 12 x 1.25	Based on a quote from a leading provider. Spec based on Microsoft Experia L3 (closest model to Minimum Income Standard spec of Lumia 535) Converted to a household level premium by multiplying by 1.25 to account for households with more than one adult, with this insurance.
Accessing cash:			
Cash - ATMs	not used / no charge	**Premium = £25.35 / year** £1.69 x 12 x 1.25	Average charge per use = £1.69 Have assumed are used 1 / month. Converted to a household level premium by multiplying by 1.25 to account for households with more than one adult who uses a fee-charging ATM. *(no new data for charges to update in 2019)*
Pre-paid cards	not used / no charge	**Premium = £37 / year**	Based on a typical cost across range of cards Have assumed use of 10 withdrawal / top up fees per year + application fee.
Higher-cost credit:			
Rent-to-Own (TV)	retail price = £330	**Premium = £182 / year** rent-to-own price = £512	Most common item bought via rent-to-own from survey is a TV. 43" Smart 4K Ultra HD LED TV BrightHouse total cost paid over 12 months:££512

Area	Benchmark	Poverty premium	Notes
Short term loan (Payday loan substitute)	not used	**Premium = £237 / year** £200 loan x 2 x 1.25 @ £95 / loan	Based on a typical cost. Each loan is paid back over 3 months. ccost of credit per loan = £94.68 / loan. Converted to a household level premium by multiplying by 1.25 to account for households with more than one adult using payday loans.
Home collected credit	not used	**Premium = £644 / year** £450 loan x 2	Based on a quote from a leading provider. One loan is paid back over 26 weeks (535% APR), one overt 52 weeks (299% APR) Cost of credit = average £322 / loan
Pawnbroking loan	not used	**Premium = £152 / year** £130 loan x 2 @ 6 months	Based on a typical online pawnbroker cost of 154% APR Each loan is paid back over 6 months. Cost per loan = £106i.e. cost of credit = £76 / loan
Subprime personal loan	not used	**Premium = £557 / year** £450 x 2 @ 6 months	Based on a typical cost of £450 loan Each loan is paid back over 6 months Cost of credit £278.50 / loan.
Subprime credit card	not used	**Premium = £207.5 / year** £900 repaid over 12 months = £166 x 1.25	Based on a typical cost of APR of 37.65%. Cost based on opening balance of £900 repaid over 12 months. Converted to a household level premium by multiplying by 1.25 to account for households with more than one adult using subprime credit cards.

Area	Benchmark	Poverty premium	Notes
Mail order catalogue (washing machine)	retail price = £309	**Premium = £60.49 / year** catalogue price = £369.46	Minimum Income Standard washing machine spec = 7kg machine, 1400 Spin, A++ efficiency, bought from appliancesdirect.com. Compared to similar spec bought from a high cost catalogue: £309 paid over 52 weeks @39.9%APR = £369.46.
Christmas hamper	hamper items costed at supermarket prices = £207.56	**Premium = £46.68 / year** hamper price = £254.25	Based on a typical Christmas hamper costing £254.25. Compared to cost of buying the same hamper items at a supermarket.

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