Mistakes that Marginalize
–
Financial Advice and Low-Income Households

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Utrecht, 11 March 2022

One balance sheet, many rules

- Financial consumer protection and excessive risk taking
  - Borrowing (consumers as debtors), and over-indebtedness
  - Investing (consumers as 'investors'; bank deposit), and exposure

Assets:		Liabilities:	
Description	Value	Description	Value
Condo	$140,000	Mortgage	$127,500
Car	$ 16,000	Car Loan	$ 11,250
Computer	$ 1,200	Credit Card	$ 800
Bike	$ 800	Line of Credit	$ 1,300
SmartPhone	$ 600	Student Loan	$ 12,500
TOTAL	$158,600	**TOTAL**	$153,350

Financial risk, and mistakes

- What's special with consumers on a tight budget?
  - Consequences of materialisation of financial risks may lead to social exclusion
  - In turn, reduced access to financial services:
    - Exclusion from certain market segments (not affordable)
    - Reduced ability to curb/manage financial risks
- Mistakes that marginalise:
  - Misallocation of assets and over-indebtedness harm resilience
  - Regulatory mistakes may exacerbate marginalisation

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A broad array of tools: advisory services

- *Balance sheet liability side* (CCD; MCD)
    - Mandatory assessment of creditworthiness
    - Non-mandatory advice
    - 'Debt advisory services' in proposal for new CCD (include legal counselling, money and debt management, as well as social and psychological assistance)

- *Balance sheet asset side* (MiFID II; ELTIF; BRRD; STS)
    - 'Suitability test' for investment advice
    - Made mandatory to buy certain assets

A broad array of tools: structural measures

- Product governance
  - Ex-ante filter based on 'target market'
- Product intervention
  - Ban based on overarching supervisory assessment
- Entry ticket
  - Excluding low-budget investors from risks (and returns…) (EuSEF; EuVECA)
  - Loan-to-value and loan-to-income ratios (national laws)
- Mandatory portfolio differentiation
  - One-size-fits-all approach to optimal risk management (ELTIF; BRRD; STS)

The importance of advice, and its limits

- ‘Adequate’ and ‘excessive’ risks are often consumer-specific
  - Case-by-case assessment reduce false positives and false negatives
- Ensuring quality is important – the case of inducements
  - No advice is better than tainted advice
- The advice gap
  - A problem inherent to any licensure system
  - Are we condemned to missing financial consumers on a tight budget? The UK experience

Fixing financial advice

1. Introducing a brand new service ('financial advice')?
   - Facilitates joint provision of all advisory services to enable general financial planning – particularly useful for low-income consumers
   - Should include broad array of services – 'debt advisory services' as a model
2. Subsidising its provision?
   - Not just a matter of welfare state: financial mistakes and stability concerns (externalities from subprime crisis)
   - Possibly avoiding cross-subsidization – a voucher system to:
     - Support independent advice
     - Nudge towards consumption of advice

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