momentum | UNISA university of south africa

Purposeful collaboration towards Financial Wellness in South Africa

Momentum/Unisa Household Financial Wellness Index

2017 Summary Report

Overall Financial Wellness score

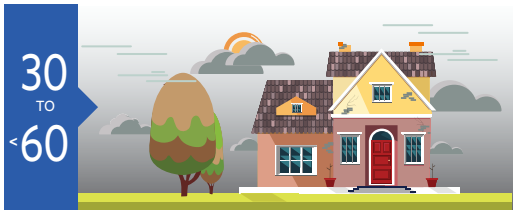
The average overall financial wellness score increased from 64.1 points in 2011 to 67.7 points in 2017. However, the improvement was marginal between 2016 and 2017 - as the score increased by only 0.4 points. The small improvement can be attributed to a mixed bag of factors at the national economic (macro), community (meso) and household and consumer (micro) level. The said factors include inter alia:

- **Macro-level:** Low but improved economic growth rate compared to 2016, low employment growth, high unemployment, low consumer and business confidence, lower consumer price inflation, lower growth in gross income per worker, stagnating real GDP per capita growth and low private consumption growth.
- **Meso-level:** Low growth in early stage entrepreneurial growth, high levels of inequality within and between communities, high levels of poverty in many communities and widely differing levels of service provision in communities.
- **Micro-level:** Low levels of subjective well-being experienced by consumers, low household balance sheet growth, low levels of financial literacy among consumers, strong growth in the number of secondary school finishers (although there are many concerns about the quality of school education) and high levels of financial vulnerability among the low and lower middle income groups.

Financial Wellness categories defined

Financially Distressed

The household is deeply rooted in a financially distressed position. Major outside assistance is required for improvement. These are the people most at risk of missing fixed payments and resorting to high-cost credit.



Financially Unstable

The household is not entrenched in a financially distressed position, but remains in an unwell situation. Adverse events and wrong decisions can easily change its position to Financially Distressed. However, some opportunities are available to become Financially Exposed.

Financially Exposed

The household has more opportunities to improve its Financial Wellness. Although the financial situation is not unwell, negative/positive changes will cause households to become either Financially Unstable/ Financially Well.

Financially Well

The household is Financially Well in the current political/economic/ social climate. However, negative developments may cause the household to become Financially Exposed.

Figure 1

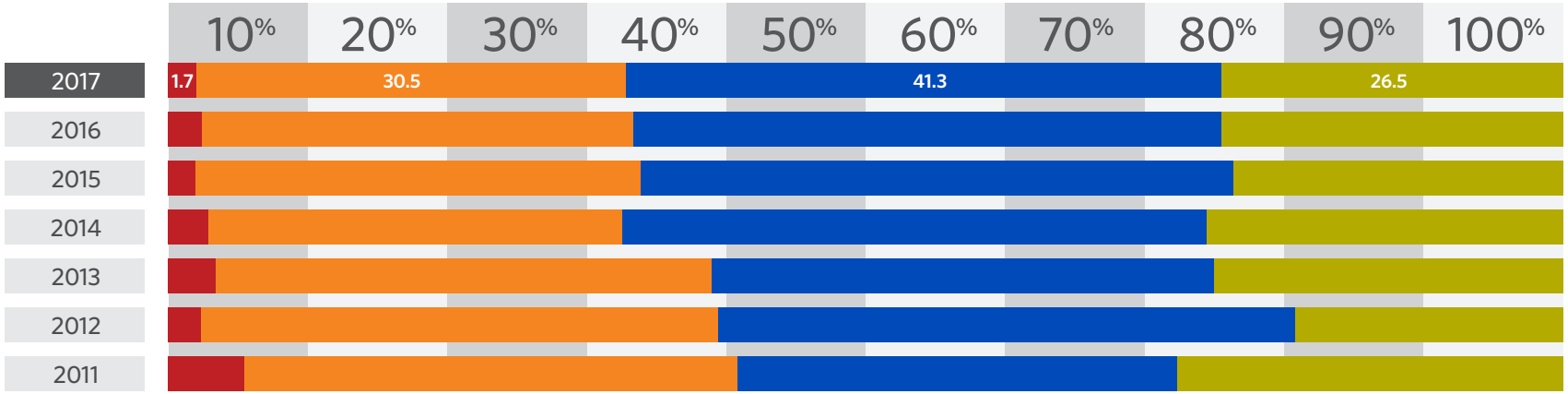


Figure 1 shows that the proportion of financially well households was virtually unchanged between 2016 and 2017. Only 26.5% of households are considered financially well during 2017, implying that 73.5% of households were financially unwell during this period.

More concerning is that the proportion of financially well households was virtually unchanged since 2011. The biggest change was the movement from financially unstable to financially exposed. This means that although a larger proportion of households are still financially unwell, they are not "as financially unwell" as before. Put differently, their degree of financial unwellness softened.

Three of the five sub-components that comprise the financial wellness score improved during 2017, while two sub-components deteriorated. ***Figure 2*** shows that that the lowest sub-index score of 4.7 (out of 10) was registered by the asset capital component (households' assets, liabilities and net wealth, reflecting their balance sheet). This decline from 5.0 points in 2016 can be attributed to a number of reasons. The FNB House Price Index suggests that house prices declined by 1.1% in real terms between 2016 and 2017. At the same time real investments in residential property increased by less than 1% compared to 2016. As for financial assets, the real value thereof was lower during the first half of 2017 compared to the same time a year before. However, households who remained invested in shares via among others their retirement funds reaped the fruits during the latter part of 2017 when share prices increased. However, these improvements, as well as a decline in the debt to disposable income ratio from 74.1% in 2016 to 72.0% in 2017 were not sufficient to prevent the net wealth to disposable income ratio from declining to 372.7% in 2017 from 376.0% in 2016.

When analysing the sub-index scores as illustrated in ***Figure 3***, some household financial wellness trends over the period 2011 to 2017 become evident. It should firstly be noted that during this period, human capital scores increased due to a growth in the pool of household members with completed secondary and tertiary qualifications, while environmental capital grew because of the improved housing conditions of people. While these two forms of capital generally saw positive growth over the period 2011 to 2017, the growth patterns in physical and asset capital were fickle due to volatility in the levels of real household income and net wealth growth. Social capital levels remained low due to feelings of disempowerment, low levels of subjective wellbeing, financial vulnerability and low consumer confidence in the economy.

Figure 2: Capital 2016 vs 2017

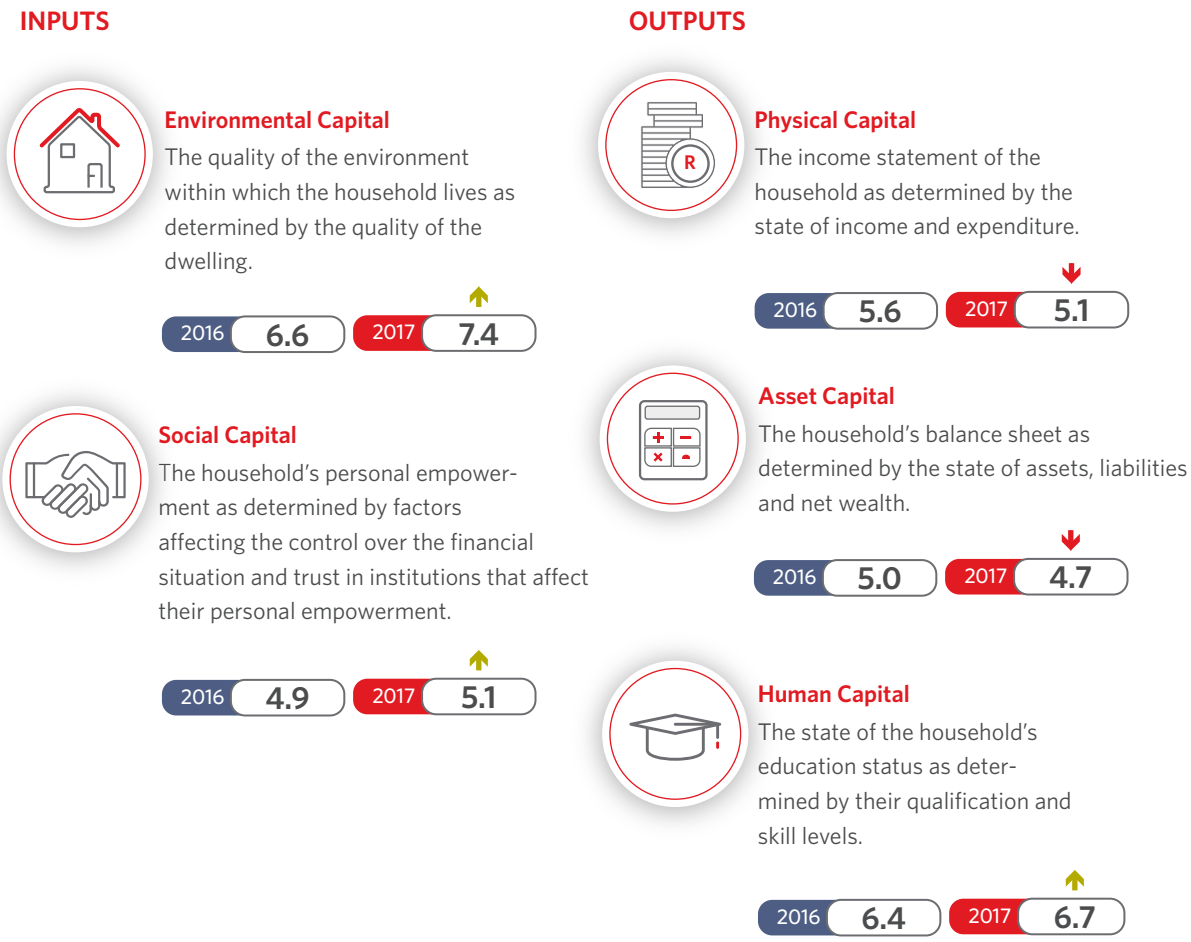
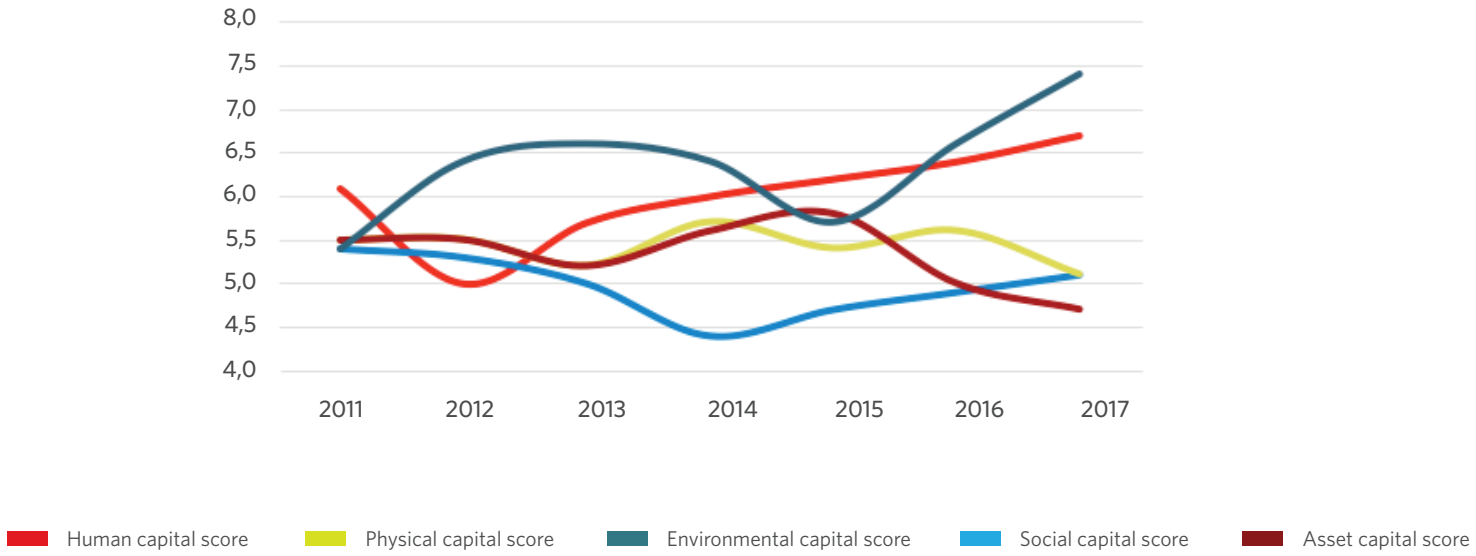


Figure 3



The gap between human capital and social capital as depicted in Figure 3 over the period 2014 to 2017 is concerning. This gap can to a large extent be attributed to insufficient skills delivered by the educational system. Although the educational system delivers a growing number of matriculants and graduates, the students predominantly acquire academic knowledge and not the high-level cognitive, social and communication skills that are required. The latter "missing" skills requirements prevented matriculants and graduates from obtaining better 'adaptable' skills which would have enabled them to live more empowered lives.

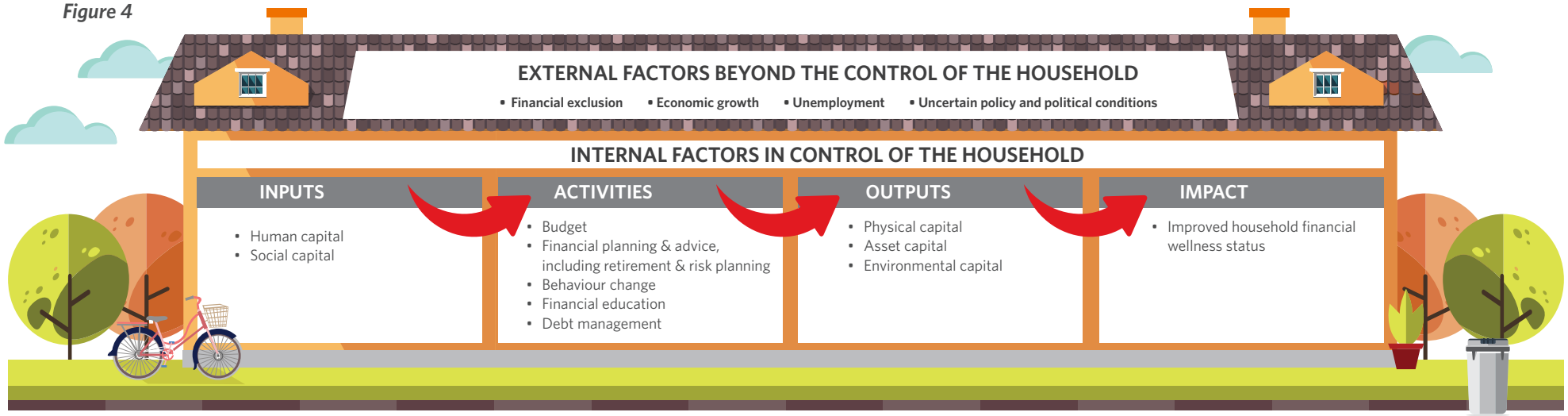
It is also important to note that although the human capital index has shown strong growth during the 2012 to 2017 period, the physical capital index did not experience the same improvement as one would have expected. In fact, the physical capital index has been fluctuating at nearly the same level over this period. This disconnect between the human capital and physical capital index scores can to a large extent be explained by the low production elasticity of employment which stems from a skills mismatch in the economy. The skills provided by the South African labour supply are to a large extent out of kilter with the skills demanded by current and prospective employers. This phenomenon also explains a considerable part of the high levels of unemployment, poverty and income inequality – the so-called 'triple challenge' – found in South Africa.

Theory of Change

The Theory of Change (ToC) is an excellent conceptual, analytical and modelling tool that can be applied to determine how the input variables (i.e. human and social capital) in conjunction with activity variables (e.g. financial planning) impact the output variables (physical, asset and environmental capital), from where the financial wellness outcome can be derived. So, the Theory of Change postulates that the baseline conditions for a household to proceed on their household's financial wellness journey will be determined by their level of human and social capital. As can be seen from the graphical depiction of the Theory of Change, a broad range of financial activities are the vital link between the baseline conditions and the generation of financial wellness outputs (physical and asset capital).

If higher levels of human and social capital are absent, or not used and applied actively and effectively via conducting the necessary financial activities aimed at building physical-, asset- and environmental capital, such human and social capital will have little positive impact on household financial wellness outcomes. However, it is not just a case of conducting certain activities but conducting such activities correctly. Such activities in the personal finance sphere include, inter alia, continuously conducting comprehensive financial planning such as saving sufficiently for retirement, planning for resilience against financial risks and – emergencies, as well as not incurring too much debt. The research shows that if a household has highly skilled members (human capital) who are socially empowered (social capital) and regularly conduct detailed and continuous financial planning and good debt management and stay informed on financial matters, the household will be in a better position to produce favourable outputs (physical, asset and environmental capital) and also tend to be more financially well.

Figure 4



Analysis

A comparative analysis of the theory of change applied to financially well and unwell households, 2017

Table 1

		Financially Unwell **73.5%**	Financially Well **26.5%**
INPUTS	**Human capital score (out of 100)**	63.16	78.50
	Social capital score (out of 100)	44.03	71.69
	Completed secondary or tertiary qualification	71.4%	96.8%
	Completed tertiary qualification	11.2%	39.2%
	Able to calculate compound interest	25.1%	31.4%
	Able to determine risk in portfolio decisions	26.1%	35.0%
ACTIVITIES	Percentage that don't have a financial plan	57.6%	35.9%
	Percentage that have a comprehensive plan that includes providing for emergencies and unplanned expenses"	6.5%	17.0%
	Percentage that will be able to cope with an emergency requiring R20 000	33.0%	60.5%
	Percentage that agree that they have a written budget	40.4%	53.4%
	Percentage that agree that they have an institutional/professional financial adviser	5.3%	15.6%
	Percentage that agree that they have enough for retirement	23.4%	40.8%
	Percentage conducting planning on portfolio composition	15.2%	22.5%
	Percentage that continuously review their financial plan	28.9%	42.1%
	Percentage that change their budget or financial plan continuously to reflect changes in prices, taxes and debt repayments	26.5%	42.2%
	Percentage indicating that they have provided for the event of their own death or the death of a household member in their financial plan	37.1%	57.0%
	Percentage for which a combination of short and long-term periods are important in their financial planning	8.7%	20.2%
OUTPUTS	**Physical capital score (out of 100)**	40.32	79.89
	Asset capital score (out of 100)	35.71	79.75
	Environmental capital score (out of 100)	66.94	92.64
IMPACT	**Financial Wellness score (out of 100)**	60.2	88.7

A Theory of Change profile of the households classified as financially well and financially unwell (the sum of financially distressed, financially unstable and financially exposed) is provided in ***Table 1***.

This table reveals that when financially well households are compared to financially unwell households, the financially well households have a big head start as they possess higher human capital scores, as well as much higher social capital scores. They also engage more actively in financial activities, which contributed to their output scores being higher than their input scores, making them financially well.

Tertiary qualifications stand out as a strong predictor of household financial wellness outcomes (i.e. a larger percentage of households in the financially well category have tertiary qualifications, namely 39.2% vs 11.2%). The financial literacy levels of the financially well are also higher than that of the financially unwell, but in both cases the level of financial literacy is concerningly low. However, the financially well are more likely to overcome this deficit as they (on a larger scale) make use of professional financial advice. The proportion of households who do make use of professional financial advice is however disproportionately low.

The social capital scores coupled with low financial literacy levels appear to be the Achilles heel of many South African households. This may explain the general lack of comprehensive financial planning among financially well and financially unwell households, not understanding the usefulness of skilled financial advisers and not conducting effective debt management. The cumulative impact of low skills, low levels of social empowerment as well as the relative absence of planning and good financial management in such households result in low incomes and excessive expenditures (physical capital), low levels of wealth accumulation (asset capital) and adverse living conditions (environmental capital).

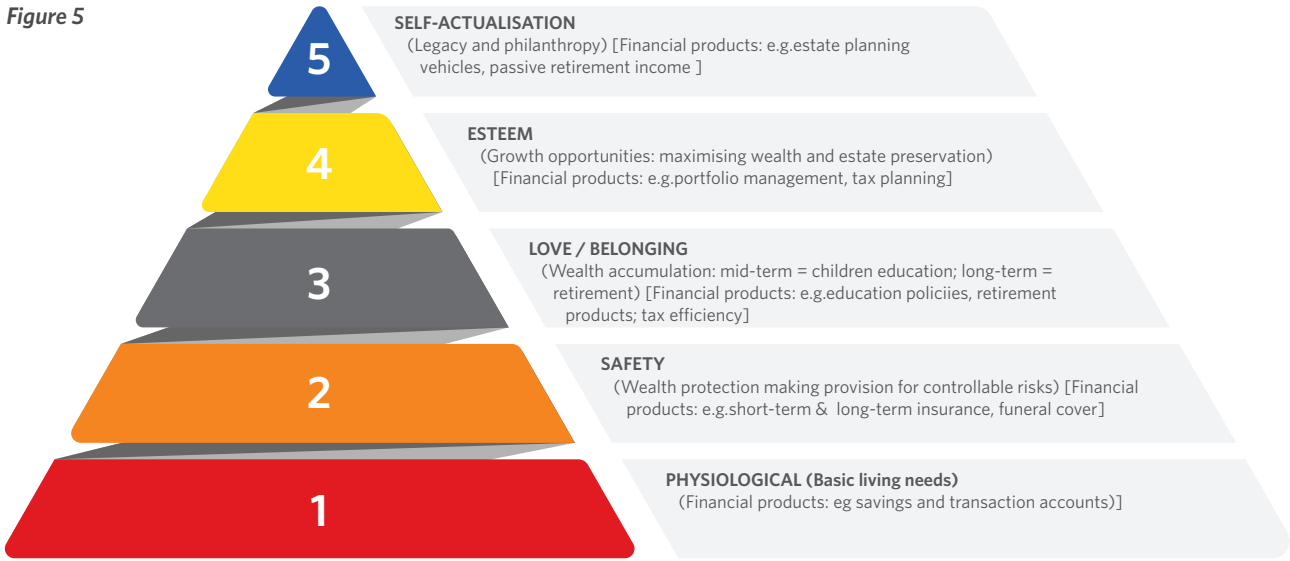
The results from the Theory of Change exercise show that a comprehensive intervention is needed for financially unwell households to become financially well. Such a comprehensive intervention is more multi-faceted than merely providing social grants, social housing, free services and financial products. The said grants, housing and services do, however, prevent financially unwell households from becoming even more financially unwell. But putting households on a path of financial wellness growth will necessitate job creation, high quality education, enhancement of households' financial literacy and financial capabilities, improving their understanding of the need and role of financial advisers, -planning and -products in their quality of life, making such planning and products accessible and affordable while also customising it to their needs, and programmes to improve their social empowerment (to take control of their own lives and financial situations).

Hierachy of needs in terms of financial wellness

The importance of having a comprehensive financial plan and adjusting their budgets to achieve financial goals was also presented as one of the distinguishing factors between the two financial wellness groups as it was established that a positive relationship exists between goals and desired outcomes. As such, a financial plan that includes an active pursuance of specific financial wellness goals will contribute to progress on the financial wellness journey of households.

However, a better understanding of households' emotional and financial needs is critical for better financial planning and long-term financial wellness success. According to Anthony and Walker (2006), the real challenge for financial advisers is to change the client conversation from a 'money conversation' to a 'lifestyle conversation'. Once this change has occurred, the conversation is about how to pay for the lifestyle the household desires – moving the conversation away from a grudge relationship to a financial coaching partnership.

Figure 5



To gain a better understanding of the essentials of this 'lifestyle conversation', Maslow's (1954) hierarchy of needs can be applied. Although prior research might differ on the number of levels in the hierarchy of financial needs, the consensus view is that short-term basic financial needs are considered lower level savings goals; financial security needs are middle level; and self-actualisation are at the top of the human needs pyramid. Parallel to the increase in financial needs is also the rise in sophistication of the products utilised to fulfil those financial needs. For example, lower level financial needs could be satisfied by the utilisation of a transaction or savings account, but shares or exchange traded funds can be utilised to provide growth at the higher end of the human needs pyramid. Financial goals based on Maslow's theory can therefore be depicted as in ***Figure 5***.

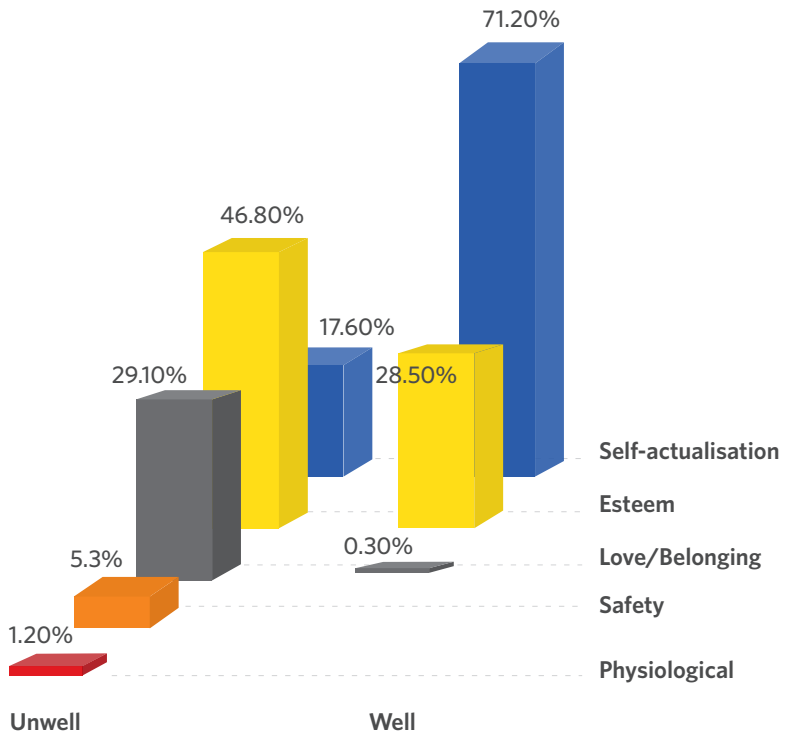
In order to determine the placement of South African households on the financial needs hierarchy based on their financial wellness capitals, the following assumptions were made in line with Maslow's original hierarchy of human needs:

- A lower order need has to be relatively satisfied before a higher order need becomes predominant.
- Household members generally first try to satisfy physiological needs (using human and physical capital) before moving towards safety needs (using physical and environmental capital) before they start satisfying social and esteem needs (social capital) as well as self-actualisation needs (asset capital).
- Higher respective capital scores indicate a transition from basic needs to higher order needs.

Based on the fulfilment of their financial needs, it is evident from ***Figure 6*** that the financially well households have been successful in servicing their physiological, safety and belonging needs (i.e basic living needs, wealth protection and wealth creation) and are on their way towards fulfilling their higher-order needs. In contrast, financially unwell households are still addressing some safety needs and they are predominantly focused on their wealth accumulation needs, such as saving for retirement and investing in the education of their children.

The hierarchy of needs picture is supported by ***Table 2*** which shows that financially well households spend proportionately less on physiological needs such as groceries and clothing (than financially unwell households). They therefore can fulfil other needs such as insurance and medical cover and saving more money. Financially well households succeed in ensuring that their safety needs are sufficiently addressed by among others obtaining short-term insurance, life and disability insurance. Financially well households are also good at addressing their social needs via financial behaviour aimed at ensuring that they are financially well, i.e. they formulate financial plans, set the correct financial goals, update the plans and goals regularly and monitor the financial outcomes forthcoming from such plans.

Figure 6



A comparative analysis of financial needs hierarchy applied to financially well and unwell households, 2017

Table 2

		Financially Unwell	Financially Well
PHYSIOLOGICAL (basic living needs)	Groceries (eg food, alcoholic and non-alcoholic beverages, tobacco and consumer products such as cleaning products) (% of total expenditure)	24.8	18.9
	Clothing, footwear and accessories (% of total expenditure)	10.7	8.3
	Taxi, bus and train fares, parking and garage fees, tolls, etc. (% of total expenditure)	6.7	3.6
	Expenditure on other essentials (% of total expenditure)	22.6	27.6
	Total expenditure on essentials (% of total expenditure)	64.8	58.4
SAFETY (wealth protection making provision for controllable risks)	I have sufficient insurance, savings or access to money to cope with unexpected costing more than two weeks of salary (% agree)	16.4	31.5
	I can rely on assistance from others, when facing financial difficulties (% agree)	29.4	27.2
	I have enough insurance or savings to cover the theft of or damage to my vehicle (% agree)	18.0	39.3
	I have enough insurance or savings to replace my belongings lost owning to fire, floods or theft (% agree)	13.8	37.8
	My financial plan makes provision for the possibility that I might become disabled (% agree)	17.0	36.6
	I provided for the event of my own death or the death of a household member in my financial plan (% agree)	37.1	57.0
	My financial plan provides for earning an income should I lose my job (% agree)	20.0	38.1
	High level of risk tolerance regarding investments and savings (mean score out of 10)	7.0	8.7
LOVE/BELONGING (wealth accumulation: mid-term = children education; long-term + retirement)	I monitor my budget, actual expenses, financial plan continuously (% agree)	28.1	42.6
	I review my financial plan continuously (% agree)	28.9	42.1
	I change my budget or financial plan continuously to reflect changes in prices, taxes and debt repayments (% agree)	26.5	42.2
	Taxation has a positive impact on my life (% agree)	35.7	31.7
	I never skip payments of bills and accounts (% agree)	30.7	49.2
	The amount of tax people pay is too high (% agree)	49.1	55.4
	People with high incomes should pay a larger share of their income on taxes than those with low incomes (% agree)	48.3	43.3
	Have a written budget (% agree)	40.4	53.4
	It is highly likely that a person will be punished by SARS if he/she avoids paying the required taxes (% agree)	33.0	60.5
	When planning your household's finances you plan for a year or more (% agree)	46.5	52.6
	Should there be a need for taxes to be increase, I would prefer an increas in income tax to an increase in VAT (% agree)	27.8	20.8
		33.9	31.0
ESTEEM (growth opportunities: maximising wealth and estate preservation)	My financial knowledge is extensive (% agree)	26.7	35.1
	During the past year my household planned our portfolio composition thoroughly (% agree)	15.2	22.5
SELF ACTUALISATION (legacy and philanthropy)	I am on track to achieve my long-term financial golas (ie for retirement) (% agree)	23.4	40.8

Figure 6 and ***Table 2*** reveal that households who have a predominant focus on the satisfaction of their higher order needs tend to have higher financial wellness scores. This suggests that the economically active members of such households should possess highly developed financial literacy skills and that they are on track to achieve their long-term financial goals. However, ***Table 3*** shows that it is not the case as both the financially well and financially unwell don't possess sufficient financial literacy skills. Possible reasons for such low financial skills and inadequate financial portfolio planning are insufficient development and inculcation of financial literacy skills on household and school levels, conspicuous consumption being the order of the day and the absence of a true savings culture in South Africa.

Table 3: Financially well and unwell households classified on the two top tiers, 2017

		Financially Unwell	Financially Well
ESTEEM	My financial knowledge is extensive (% agree)	26.9	30.9
	During the past year my household planned our portfolio composition thoroughly (% agree)	14.0	14.3
SELF-ACTUALISATION	I am on track to achieve my long-term financial golas (ie for retirement) (% agree)	35.8	42.3

TEN BEHAVIOUR CHECKS TO ASSIST IN THE JOURNEY TO FINANCIAL WELLNESS

Based on the findings of this research project, as well as discussions based on the findings of this project, ten behaviour checks were identified by the Unisa research team that could assist households on their financial wellness journeys, namely:

1. Actionable high quality market-related skills: In research conducted by the Federal Reserve of St Louis (2017) in the United States, a very strong correlation between educational attainment and incomes were found. It was found that families with household heads who possess an advanced degree earned on average 52% more than households headed by a person with a first degree and 182% more than households headed by people with a high school diploma. Analyses of the 2017 Household Financial Wellness data provided the following comparable South African data: Households with post-graduate degree as highest degree in the house-hold earn only 26% more than house holds with a first degree as highest degree in the household but 329% higher than households with matric as highest qualification in the household. This provides a clear indication of the value of tertiary education in South Africa and the lower value of a matric compared to the United States.

2. Continuous growth in personal (i.e. cognitive, communication and social) skills: In a 2006 firm-level study conducted by the Development Policy Research Unit (DPRU) at the University of Cape Town, it emerged that South African firms were very critical of the quality of primary and secondary education in South Africa. Such firms were especially concerned by the low level of functional illiteracy, lack of 'soft'-, entrepreneurial and communication skills among school leavers. According to the firms this could be addressed by bridging courses presented at tertiary institutions. Having obtained a certain level of personal skills, however, does not mean that consumers are now set for life in using such skills to ensure success on their financial wellness journeys. It is clear from the DPRU results that skills need to be continuously practised and updated.

3. Personal empowerment and self-efficacy: According to the journal Entrepreneur (2017) there are eight steps to personal empowerment, namely (1) being open to possibilities, (2) focusing on who you are, (3) running your own race, (4) trusting yourself, (5) being able to build personal networks, (6) loving what you do, (7) holding yourself with grace, and (8) embracing imperfect moments (failures). Although

these eight steps to personal empowerment appear to be self-evident and that everybody applies them, the 2017 social capital results show that this is not the case at all. Some 34.2% of respondents indicated that they are seldom or never able to solve their problems, 33.7% felt that there is little that they can do to change important things in their lives and 24.0% indicated that they are helpless in dealing with problems of life.

4. Financial literacy: Respondents were generally of the opinion that their financially knowledge is limited (71.0% described it as not extensive at all). Three financial literacy questions asked during the survey show that such assessments by respondents were correct. Financial literacy across income and household financial wellness groups were very low showing a generally low level of financial literacy in South Africa. Financial advisers who provide a comprehensive service can play a very important role to nudge, guide and coach households towards higher levels of financial literacy and making better financial decisions.

5. Financial capability: The 2017 results indicate that financial capability (not literacy) levels differ greatly between financially well and financially unwell households. Global financial capability research has shown that financial planning tools can make a world of difference to consumers wanting to plan, budget, etc., but the assistance value is diminished by them not knowing how such tools should be used and how the results should be interpreted. In this regard, a tax planning tool such as TaxTim is a great example of a knowledge and planning instrument which makes the optimal completion of tax returns possible for taxpayers.

6. Full financial inclusion: Databases such as FinScope and the All Media and Product Survey clearly show that financial inclusion rates are fairly high with respect to basic transactional accounts. However, financial inclusion rates for savings and investment, insurance, medical schemes and secured debt products are still fairly low. Fortunately, the development of a new generation of innovative financial sector products contributed to higher levels of financial inclusion in recent years.

7. Financial planning by making use of qualified financial advisers: Research conducted some years ago by Unisa's Taxation Department has shown that the use of financial advisers is generally low. This was mainly because such advisors are often not trusted by consumers due to the belief that financial advisers do not provide financial advice and products that are in the best interest of consumers, but rather in the financial interest of the advisers themselves. Qualified financial advisers that have the best interests of their clients at heart, considers them holistically and who are financially well-informed could play a large role in ensuring improvements in household's financial wellness.

8. Assisted and informed portfolio composition including financial coaching: Investment advisers and portfolio managers could play a very important role in coaching and guiding investors in making good investment and asset allocation decisions.

9. Long-term consumption smoothing, increased savings and preparation for retirement: Retirement planning and saving is vital in ensuring the long-term financial wellness of households, especially in light of the rapid growth in the life expectancies of people who reach retirement age. At the same time expensive and too much debt should be avoided as it has a negative impact on future consumption and saving smoothing.

10. Continuous monitoring and evaluation of financial outcomes: It is imperative that households not only conduct continuous financial planning but also monitor and evaluate their financial outcomes to determine whether they are on track to achieve their financial goals.

Realised sample description

TOTAL NUMBER OF HOUSEHOLDS POLLED

2 746

HOUSEHOLD INCOME GROUPS

52.3% LOW INCOME R0 - R94 500 pa

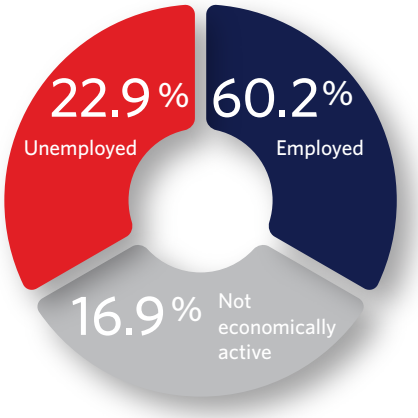
41.8% MIDDLE INCOME R94 501 - R757 000 pa

5.9% HIGH INCOME R757 001 + pa

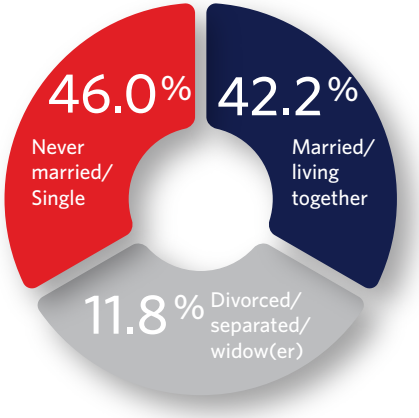
AGE GROUPS

18 - 24	25 - 34	35 - 44	45 - 54	55 - 64	65+
8.2%	31.8%	24.5%	17.5%	10.7%	7.3%

EMPLOYMENT



RELATIONSHIP STATUS



EDUCATIONAL

1.6%	Some primary	60.2%	Secondary completed
19.2%	Completed primary	19.0 %	Tertiary completed

Financial wellness groups

HOUSEHOLD FINANCIAL WELLNESS GROUPS

	DISTRESSED	UNSTABLE	EXPOSED	WELL	TOTAL
AGE CATEGORIES					
Younger than 18		17.8%	82.2%		100%
18 - 24		38.2%	44.9%	16.9%	100%
25 - 34	1.8%	30.2%	41.3%	26.7%	100%
35 - 44	2.3%	29.3%	39.7%	28.7%	100%
45 - 54	2.4%	25.6%	41.5%	30.5%	100%
55 - 64	0.9%	32.2%	42.7%	24.2%	100%
Older than 65	1.3%	35.7%	39.5%	23.5%	100%
RELATIONSHIP STATUS					
Never married / single	2.0%	34.0%	42.4%	21.6%	100%
Married / living together	1.7%	25.3%	40.3%	32.7%	100%
Single after marriage (widowed / separated / divorced)	0.7%	34.5%	40.7%	24.2%	100%
EDUCATION GROUP					
Some primary	17.8%	76.8%	5.4%		100%
Completed primary	4.3%	60.8%	30.7%	4.2%	100%
Completed secondary	0.9%	25.5%	48.0%	25.6%	100%
Tertiary	0.1%	9.0%	35.1%	55.8%	100%
EMPLOYMENT STATUS					
Employed	0,8%	22.8%	43.1%	33.3%	100%
Not economically active	1.4%	33.2%	41.9%	23.5%	100%
Unemployed	4.0%	45.8%	37.0%	13.2%	100%
INCOME GROUP					
Very low income (R0 - R21 500 pa)	6.2%	66.1%	27.7%		100%
Low income (R21 501 - R94 500 pa)	1.4%	39.0%	49.1%	10.5%	100%
Low emerging middle class (R94 501 - R215 000 pa)		14.5%	47.3%	38.2%	100%
Emerging middle class (R215 501 - R440 000 pa)		3.6%	34.3%	62.1%	100%
Realised middle class (R440 001 - R757 000 pa)		2.3%	22.4%	75.3%	100%
Emerging affluent (R757 001 - R1 600 000 pa)		1.0%	12.5%	86.5%	100%
Affluent and wealthy (R1 600 001 + pa)			12.1%	87.9%	100%
PROVINCE					
Gauteng	2.3%	26.7%	39.7%	31.3%	100%
Limpopo		41.4%	41.3%	17.3%	100%
Free State	0.5%	20.5%	55.2%	23.8%	100%
Western Cape	1.9%	28.0%	43.4%	26.7%	100%
Mpumalaga	1.1%	29.4%	43.7%	25.8%	100%
Northern Cape	0.7%	29.6%	42.2%	27.5%	100%
Eastern Cape	1.6%	37.5%	37.6%	23.3%	100%
KwaZulu-Natl	2.2%	30.7%	43.2%	23.9%	100%
North West	2.3%	32.9%	32.6%	32.2%	100%