A NEED FOR PRODUCT INNOVATION TO HELP LMI CONSUMERS MANAGE FINANCIAL EMERGENCIES

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I. INTRODUCTION

The current recession in the United States emphasizes the financial vulnerability of many American households. While families experience emergencies, such as car breakdowns, household repairs and medical illnesses, today's uncertain economy makes families even more vulnerable to these financial shocks. Without the right tools to manage these emergencies, families can experience hardships - less food on the table, increased levels of debt, deeper depths of poverty – that can be short-term or ever-lasting. For low to moderate income (LMI) households, the size of the shock might be small but the relative impact large, long-lasting and potentially forever damaging.

Saving is already difficult for many working Americans, with limited and volatile income, high and often fluctuating monthly expenses and limited discretionary funds. These challenges make saving for both unexpected and planned large expenses difficult. Much research provides insight on the prevalence of emergencies, the need for rainy day funds and hardships experienced as a result of the lack of emergency savings and other available coping mechanisms.[1] However, little research has focused on highlighting tools to keep households prepared and safe. This creates a need for more in-depth understanding and testing of products and design features that can make savings easier and more accessible to LMI consumers and reduce the gap between the need for and the access to emergency funds.

With this in mind, Doorways to Dreams (D2D) Fund designed a survey to understand LMI consumers' perceptions of and experiences with emergencies and their insights into product design features that will help their households cope. The survey was conducted by the RAND Corporation and respondents were drawn from a sample of RAND's American Life Panel members. The sample comprised 632 participants with household income between $20,000 and $60,000.

This paper details the survey findings, focusing on the a) Need for Rainy Day Funds, b) Opportunity for Innovation and c) Design Insights for Product Innovation. The *key findings,* detailed in these sections of the paper, are:

- Financial emergencies are a salient concern for households. Not only are they worried about their ability to manage financial shocks, but they are vulnerable to experiencing them.

- LMI households without emergency savings have limited savings overall. The positive correlation between lack of overall savings and vulnerability to shocks suggests that households might not need a specific emergency savings product but a more general savings product that serves as a cushion for short and long-term needs.

- Consumers have a desire to protect their families from emergencies and hardships. Marketing and designing products that emotionally connect to this need can help motivate consumers to take action.

- Given the lack of emergency funds by a majority of households, even a small reserve would help them feel more confident in their ability to cope with emergencies.

1 *Summary of research in Chase et al. Coming Up with Cash in a Pinch: Emergency Savings and Its Alternatives. Center for Financial Security (June 2011)*

- Connecting savings to a pre-existing behavior might be an effective way to get households started with saving for emergencies.

- With limited amounts to save each month, the most effective way to help households build an emergency reserve is with a product that allows them to set a little bit aside at a time.

- To deter use of alternative financial services when an emergency hits requires easy access to funds when needed; but to deter the use of funds for non-emergent purposes requires a design with some barriers to access.

II. SURVEY METHODOLOGY

In 2011, Doorways to Dreams Fund contracted with the RAND Corporation to survey a representative sample of their American Life Panel (ALP). The ALP is an Internet based panel of respondents who are at least 18 years old, but the technology makes it accessible to participants without internet access at home. To target the sample to more financially vulnerable Americans, D2D limited the survey to ALP participants with household income between $20,000 and $60,000. The ALP panel provides demographic data of panelists and the actual survey asked participants questions to gauge insight into their experiences with emergencies as well as their preferences for product design.

Table A: Demographics of survey participants

					632 Respondents
Gender			*Family Income*		
Male	*241*	*38%*	*$20,000 to 29,999*	*140*	*22%*
Female	*391*	*62%*	*$30,000 to 39,999*	*165*	*26%*
			$40,000 to 49,999	*175*	*28%*
Age			*$50,000 to 59,999*	*152*	*24%*
<25	*18*	*3%*			
25-39	*135*	*21%*	*Race*		
40-59	*253*	*40%*	*White/Caucasian*	*550*	*87%*
60+	*226*	*36%*	*Black/African American*	*40*	*6%*
			American Indian or Alaskan Native	*6*	*1%*
Current Living Situation			*Asian or Pacific Islander*	*9*	*1%*
Married or living with a partner	*384*	*61%*	*Other*	*27*	*4%*
Separated or Divorced	*109*	*17%*			
Widowed	*40*	*6%*	*Current Job Status (Select all that apply)*		
Never married	*99*	*16%*	*Working Now*	*354*	*56%*
			Unemployed and looking for work	*48*	*8%*
Education			*Temporarily laid off, on sick or other leave*	*8*	*1%*
Less than High School	*17*	*3%*	*Disabled*	*36*	*6%*
High School Graduate	*134*	*21%*	*Retired*	*166*	*26%*
Some college but no degree	*198*	*31%*	*Homemaker*	*83*	*13%*
Associate degree	*89*	*14%*	*Other*	*21*	*3%*
Bachelors degree	*122*	*19%*			
Masters degree	*57*	*9%*			
Professional School or Doctorate Degree	*15*	*2%*			

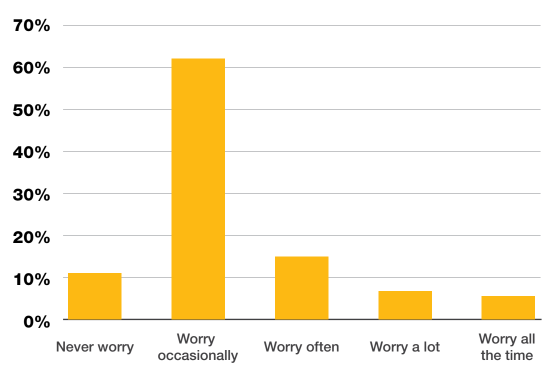
III. THE NEED FOR RAINY DAY FUNDS

While households are vulnerable to facing shocks, the severity of this vulnerability is important to understanding the need for emergency savings and to gain insight for the marketing and design of products. To understand the need, the survey looked at households' perceptions of their vulnerability and experiences, including the number of emergencies faced, their preparedness for managing shocks and the coping strategies used. Similar to other consumer finance research, D2D found that households are worried about their ability to manage shocks and this fear correlates with their experience with emergencies. The following summary of findings illustrates the need for innovative financial tools to help households better manage emergencies.

Do households worry about emergencies?

Yes, the majority of participants are worried about facing emergencies and their household's ability to handle an emergency. Only 11% of respondents surveyed do not worry about their household's ability to cope with a financial shock, while the remaining 89% worry. Overall, the majority of respondents who worry about their ability to cope responded that they only worry occasionally. While consumers' response to the degree of worry is subjective, competing household concerns and needs along with limited discretionary income for savings probably make it difficult for households to prioritize this worry and ensure preparedness for financial emergencies.

Chart 1: Do households worry about their ability to deal with emergencies?



The survey also finds that worry is correlated with household experience. Sixty-two percent of all respondents experienced at least one financial emergency in the last twelve months. The fear of not being able to effectively cope with an emergency aligns with the experience faced by LMI households. Of all households that reported experiencing an emergency, 60% faced more than one showing the extent of their vulnerability to financial shocks. Those experiencing more emergencies, unsurprisingly, are also more worried about their household's ability to handle an emergency if faced with one.

Chart 2: Number of household emergencies experienced in the last 12 months

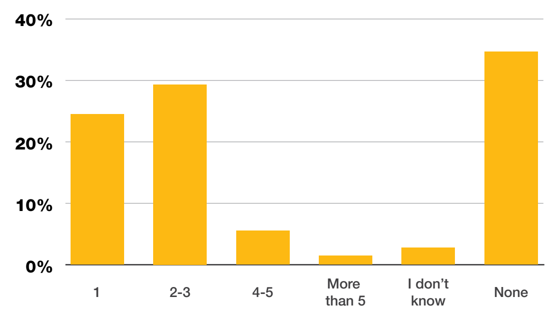
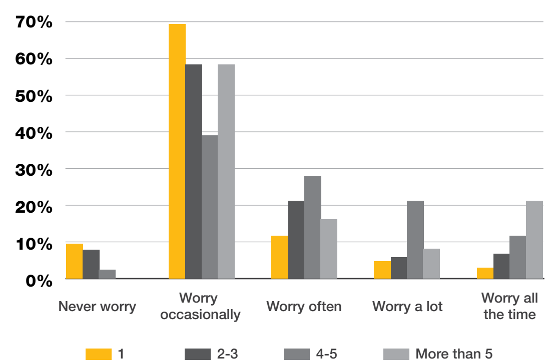


Chart 3: Worry by number of emergencies experienced in the last 12 months



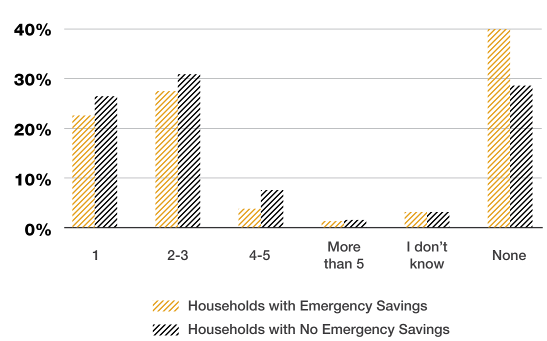
While the findings show that household worry aligns with experience, it also highlights that households might be underreporting the extent of their worry (based on their experience). The responses could be influenced by the ordering of the questions (had we asked about experiences before worry, we might have seen a higher degree of reported worry amongst participants), the recentness of experiences or the severity of other household concerns. However, effectively coping with emergencies is a salient concern given that the majority of respondents are worried and have experienced emergencies in the recent past. However, to capture consumers' attention, product designs and marketing need to creatively remind consumers of their experiences and concern in order to motivate use.

Do families have a cushion to help them cope with emergencies?

A majority of households responded that they have no emergency savings. Of all respondents, 51% do not have any emergency savings set aside. Of these respondents, 41% used to have emergency funds set aside but have not been able to replenish those funds. In contrast, a majority of those with emergency savings have a good savings cushion in place, with 68% having at least $1000 in funds (and 42% having more than $2000 set aside).

Households without emergency savings were slightly more likely to experience financial shocks than households with emergency savings, showing those less prepared might also be more vulnerable to facing shocks and struggle more to replenish funds once used. Sixty-eight percent of households without emergency savings experienced at least one shock compared to 56% with emergency savings.

Chart 4: Number of household emergencies experienced in the last 12 months



Our findings show that households without emergency savings are in general more financially vulnerable, with slightly lower income levels[2], less savings overall and more limited use of savings products to prepare for both short and long-term savings needs. Households without emergency savings are 15 percentage points less likely to have a general savings account, 16 percentage points less likely to have a certificate of deposit and 22 percentage points less likely to have an individual retirement account than households with emergency savings.

Chart 5: What savings products do households have?

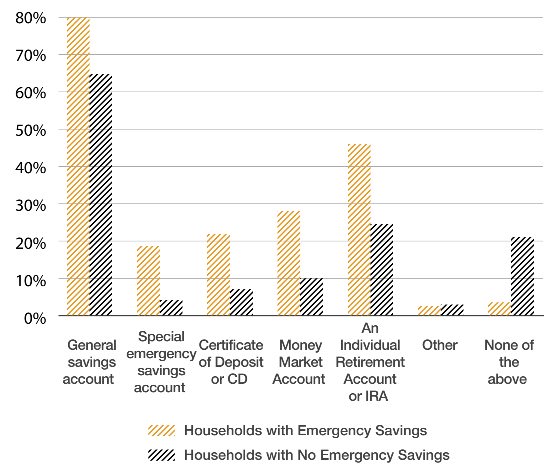
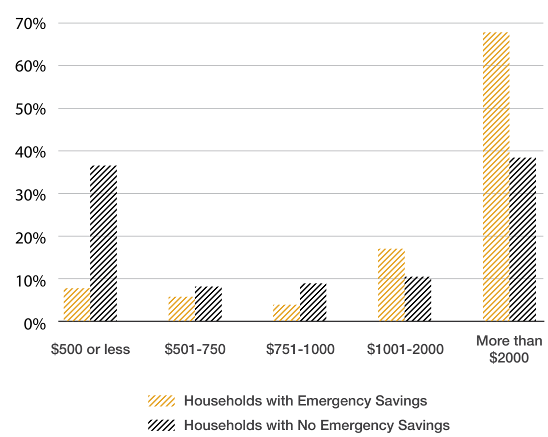


Chart 6: How much do households have saved in these savings products?



2 *Fifty-eight percent of households with emergency savings reported household incomes of $40-60K, whereas 54% of households without emergency savings reported household incomes of $20-$40K.*

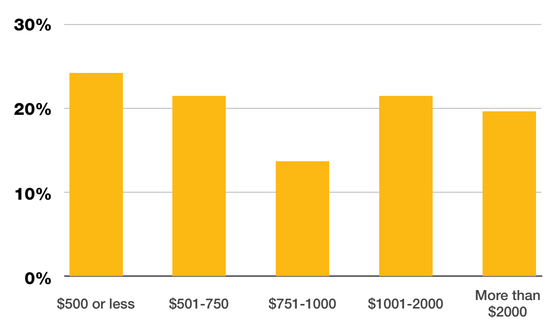
Similarly, households without emergency savings have less saved in these savings products than those with emergency savings. Fifty-two percent of households without emergency savings have $1000 or less saved in these products, and of these, 69% have $500 or less saved. However, those with emergency savings are much more financially prepared, with 84% having over $1000 saved in these savings products.

Households without emergency savings are less prepared and more vulnerable to the impact of financial shocks. Their limited savings overall highlights a need for products that help households prepare for emergencies but also the importance of products that help them meet other savings needs. The positive correlation between lack of overall savings and vulnerability to shocks also suggests that households might not need a specific emergency savings product to reduce their vulnerability to shocks, but a more general savings product that can serve as a cushion for short and long-term needs.

How are families coping with emergencies?

When households experience shocks, they need tools to cope. Of respondents that experienced a shock in the last 12 months, 41% reported that their most expensive emergency exceeded $1,000, showing a need for a large amount of funds to manage emergencies. While families cope differently, those without emergency savings are slightly more likely to rely on more than one coping mechanism and more likely to use alternatives to savings.

Chart 7: **Largest household emergency in the last 12 months**

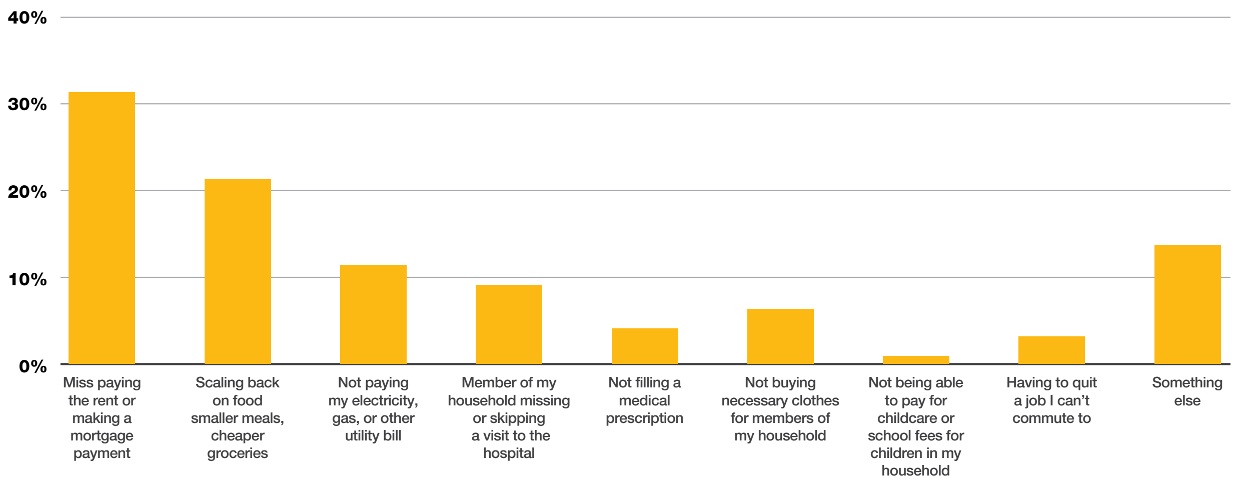


Compared to households with emergency savings, households without emergency savings were 28 percentage points less likely to use savings to cope with their largest household emergency (42% versus 70%). When asked how they handled the largest emergency faced, those without emergency savings were 15 percentage points more likely to borrow from family and friends, 9 percentage points more likely to charge it to their credit card and 10 percentage points more likely to spend less on things they did not need. Compared to those with emergency savings, those without emergency savings were also slightly more likely to rely on more than one source to cope (76% vs. 68%), implying that when they do rely on an alternative to savings, such as their social networks and their credit card, they are relying heavily on them. The fact that 27% of households without emergency savings spent less on things they absolutely did not need to manage their largest emergency provides an opportunity to capture some of their discretionary funds (though limited) into savings.

IV. THE OPPORTUNITY FOR INNOVATION

The experience of LMI households with financial emergencies, their fear of not being able to manage them as well as their lack of sufficient savings present a need and opportunity to help households build a savings cushion. While households experience challenges to setting money aside for emergencies, a product with the right design features has the potential to help households close the gap between need for and access to emergency savings. The findings from the survey show this opportunity for innovation, with consumers wanting to protect their households and set a little bit aside each month.

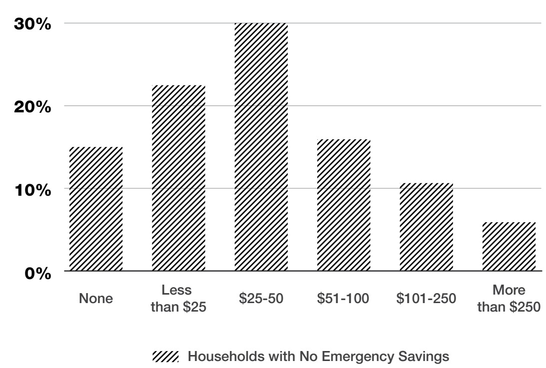
Chart 8: In case of an emergency, what would consumers most like to protect their families from?



Desire to protect their households

Consumers are interested in the emotional and physical protection of their families from the hardships faced when they cannot effectively cope with emergencies. For households surveyed, their top priorities are to protect their family from missing a payment on rent or mortgage (31%) and scaling back on food (21%). So, while households worry about coping with an emergency, the most salient worry and concern might be the ability to cope in the aftermath of one. In the context of product design, this presents an opportunity to emotionally connect the product to the consumer to motivate take-up and use.

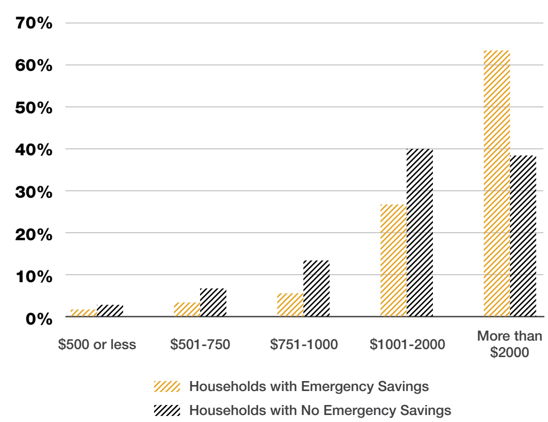
Chart 9: How much do households with no emergency savings think they can save each month for emergencies?



Ability to set a little bit aside for emergency savings

While households without emergency savings struggle monthly to manage their income and expenses, there is an interest in saving for emergencies and a willingness to forego some discretionary spending to save. Households, without emergency savings and with limited savings overall, reported that the largest impediment to saving each month is the difficulty faced in covering their monthly expenses. However, 62% of these households said they could set aside at least $25 a month for emergency savings. With the right product design, individuals could begin saving a little each month and are willing to cut discretionary spending such as eating out, family vacations and gifts to save.

Chart 10: How much would households like to have set aside to feel better able to face emergencies?



Households need emergency savings and want the opportunity to protect their families from hardships. However, households do vary in how much emergency savings they need to feel comfortable in their ability to effectively cope. For many, just having access to some funds (rather than none) is important to feel more confident in their ability to manage emergencies.

V. DESIGN INSIGHTS FOR PRODUCT INNOVATION

For an emergency savings product to be successful, the product should have features that make saving easy, accessible and rewarding. At the same time, connecting the product to consumer desire to protect their families from emergencies and hardships has the potential to enhance take-up of it. With the right product design, there is potential to help households overcome many of the challenges to saving, from taking up the product and starting to save, building and motivating savings, to maintaining savings for emergency purposes.

Reaching consumers with emergency savings products

One of the biggest challenges to saving is just getting started. Often the easiest way to help consumers start is by meeting them where they are with products that build off of an existing behavior, connect savings to an emotional need that resonates with them or address competing financial needs, making the decision to act easier.

Building savings off of an existing behavior: Even though consumers in the survey report a willingness to forego consumption today to save for tomorrow, saving is challenging especially for households with limited access to disposable income and savings products that help automate the decision to save. With consumption a more immediately gratifying decision, the behavior of buying can potentially be used to engage consumers in the act of saving. For instance, a majority of American consumers are familiar and comfortable with both giving and receiving gift cards for many occasions, especially holidays and birthdays. From D2D's work on savings bonds at tax time, we know gifting savings sells, with consumers motivated to buy savings for their loved ones. In three years of D2D pilot studies, 65% of savings bond purchasers gifted bonds to loved ones and saved, on average, 73% more when saving for others.[3] An emergency savings gift card, a product designed with these insights from tax time, a well adopted consumer habit of gifting cards and the more impulsive and gratifying decision to consume, has the potential to use an existing behavior to help consumers begin to save for emergencies.

Motivating savings by emotionally linking it to consumers: Reaching consumers also requires offering a product that is salient to their needs and speaks to their emotional desire to save. From the survey findings, consumers are worried about emergencies and have a desire to protect their families from hardships that are often experienced as a consequence of their inability to cope. Households are also worried about specific emergencies that they mostly experience, with the top three being medical expenses, car repair or maintenance and home repair or maintenance.[4] To engage consumers to take-up a new savings product requires marketing it around this desire to protect themselves and their households from emergencies and linking it to the experiences that resonate with them. From D2D's work with savings bonds, we learned the importance of linking savings bonds to children to motivate consumers to gift them.[5] This link resonated with consumers and their desire to help their children achieve their dreams and have a more financially secure future. Insights from the survey and D2D's experience indicate that similar marketing would be effective in helping drive take-up of an emergency savings product.

3 *2011 Savings Bond Report.* *Doorways to Dreams Fund (June 2011)*

4 *In the survey, the top three emergencies households were worried about experiencing were medical expenses (29%), car maintenance or repair (17%) and home repair or maintenance (17%)*

5 *2011 Savings Bond Report.*

Bundling savings with other products to address competing needs: Competing saving needs and tension between short-term access and long-term security means that a product might be more effective in attracting consumers if it is designed to help them build a savings cushion for both long-term and short-term, emergent needs. Given the competing needs of households, bundling emergency savings with another product that is either currently used by consumers (e.g. prepaid cards) or wanted by consumers (e.g. insurance) can also be an effective way of reaching them with emergency savings and making it easy to begin taking action. In D2D's survey, 53% of consumers showed interest in life insurance rewards linked to an emergency savings product, showing that bundling of two different but important needs can be an effective way to reach consumers with emergency savings.

Driving use of emergency savings products

Ensuring use of a product requires that it is simple, easy to use and rewarding. Designing a product with features such as automated savings, incremental savings, incentives and reminders can help drive use of it.

Making the act of saving more accessible: Survey results indicate that households differ in how much they can set aside each month, but a majority of households said they are able to save at least $25. This indicates the need for a product with low minimums to start and accessible increments to build savings. Households indicate a willingness to forego some consumption each month to save, so the product could be designed with a commitment to forego some spending, such as a family restaurant night a month or a coffee twice a week to save.

Making the act of saving easy: Products designed with automatic features have also shown to be effective because individuals don't have to think about the action once the automation has been set up. While some households worry about automation due to monthly fluctuations in income and expenses, the ability to automate saving small amounts, such as $5, could help households build a good cushion without a significant, noticeable amount disappearing each month. In the survey, respondents expressed interest in product designs with automatic features that make it easier to build emergency savings. Thirty percent like an automatic transfer from their paycheck into an emergency account and 29% an automatic transfer from a bank account into an emergency account. For unbanked and underbanked consumers, this design feature can be structured into financial products that are already accessible to and used by them. For instance, the prepaid card industry reaches 32% of Americans[6], many who are unbanked and underbanked. As an accessible financial tool for many LMI consumers, prepaid cards have the potential to be a good savings instrument, with saving pockets that allow for automation of a percentage of loads into them.

Where automation is not possible, reminder messages can be an effective way to help consumers save. In the survey, one-third of participants responded positively to the use of regular reminders to help them set savings aside for emergencies. The effectiveness of reminders will be based on the ability to ensure their timeliness (e.g. to their paycheck, tax refund, government benefit check time) and how well the reminder message resonates with consumers.

Rewarding savings behavior: Making saving as easy and accessible as possible is important to help households build savings by removing many barriers to access, but it's also important to make saving a rewarding decision with more immediate gratification. This has the potential to help consumers become more active in saving, turning an often mundane (though needed) activity into one tied to enjoyment.

One way to do this is by finding ways to commoditize savings, as discussed above in the gift card example. Another way is to reward individuals for their saving behavior. In the survey, respondents were interested in rewards that could help motivate them to start and continue saving for emergencies with the most expressed interest in a 1% cash back feature

6 *Foster et al. The 2009 Survey of Consumer Payment Choice. Federal Reserve Bank at Boston. Public Policy Discussion Paper No 11-1 (April 2011).*

(71%), a life insurance reward (53%), an oil change reward (53%) and store reward points (50%). Over a quarter of respondents also like the idea of making savings into a game, with rewards for goals or milestones achieved. D2D's work in prize-linked savings, the concept of incentivizing the act of saving with rewards, has shown the potential of rewarding savings behavior to help consumers build a savings habit.[7] Consumers respond well to prizes and rewards that incent different actions and we can use this insight to motivate consumers to save for emergencies.

Maintaining savings for emergencies

A successful product for emergency savings also provides access to savings when an emergency hits but has some barriers that limit use for non-emergency purposes.

Ensuring easy access to savings: When an emergency hits, households need access to funds though their urgency in need varies; in the survey, 34% of households reported needing access immediately or within 24 hours, 32% within 1-5 days and 28% by the end of the month. This variability calls for a flexible product design to meet differing access requirements. Deterring consumers from relying on alternative financial services that are often more accessible than traditional financial services at these urgent moments (but can enhance the negative impact of the shock faced) might require a product that puts savings into the hands of consumers (e.g. a prepaid card with a savings pocket, an emergency savings debit card, an emergency savings gift card) so that a consumer can transact or cash out their savings when needed.

Creating barriers to limit use: However, to ensure funds are held for emergency purposes only, product designs must accommodate some barriers to access to limit use at other times. Forty percent of respondents like a product feature that reminds them of the purpose of the funds when they go to access them to limit their use for non-emergency purposes. A product in the hands of consumers but with some withdrawal barrier, such as a 1-800 number to release the funds, social commitments (e.g. the approval of two friends to access the funds), or a reminder message at withdrawal of their commitment to usage, has the potential to help consumers maintain their savings cushion for use when an emergency hits.

VI. CONCLUSION

The experiences of many low to moderate income consumers show the need for innovation to help households save for emergencies and protect their families from hardships faced as a consequence of being ill-prepared. Since financial emergencies are somewhat unique to each household, from what is considered an emergency to how quickly funds are needed, there is a need for both diversification of products and product features. With more vulnerable households lacking savings overall, products should also be designed to address the different and often competing saving needs that exist within households.

The survey findings provide insight into both the need for savings products and expressed design preferences of consumers. While understanding the expressed preferences is important and provides some insight for product design, innovations need to take into account the reality that expressed preferences do not always match the revealed preferences of consumers. As D2D tests product designs, we will test both to understand what products and product features drive take-up and use, improve a household's ability to cope and help reduce hardships.

7 *A Win-Win for All: Growth of Save to Win in Michigan.* *Doorways to Dreams Fund (October 2011)*

Table B: Design insights for product innovation

Challenge	*Opportunity*	*Product Designs and Design Features*
Reaching consumers with emergency savings products	*Building savings off of an existing behavior*	*- Emergency savings gift cards - Commoditizing savings*
	Motivating savings by emotionally linking it to consumers	*- Market the product around consumers' desire to protect their households from emergencies and hardships*
	Bundling savings with other prod-ucts to address competing needs	*- Bundle savings with an existing financial tool accessible to consumers (e.g. prepaid card) -Bundle savings with another financial need (e.g. insurance)*
Driving use of emergency savings products	*Making the act of saving more accessible*	*- Low barriers to entry - Ability to set aside small increments at a time*
	Making the act of saving easy	*- Automate savings, where possible - Set up reminder messages tied to cash inflows*
	Rewarding savings behavior	*- Incorporate reward features (e.g. cash back reward, oil change reward, store reward points) - Use the concept of prize-linked savings - Add a game layer to make savings fun*
Maintaining savings for emergencies	*Ensuring easy access to savings*	*- Put emergency savings in consumers' hands - Emergency savings gift card - Prepaid card with savings pocket - Emergency savings debit card*
	Creating barriers to limit use	*- Call 1-800 number to activate funds - Use social commitment (e.g. 2 friends to authorize release of funds) - Reminder of usage of funds when you go to withdraw*

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