Should switch, don't switch

Overcoming consumer inertia

Ben Richards

FIRST PUBLISHED BY

The Social Market Foundation, October 2015
ISBN: 978-1-910683-05-7

11 Tufton Street, London SW1P 3QB

THE SOCIAL MARKET FOUNDATION

The Foundation's main activity is to commission and publish original papers by independent academic and other experts on key topics in the economic and social fields, with a view to stimulating public discussion on the performance of markets and the social framework within which they operate. The Foundation is a registered charity and a company limited by guarantee. It is independent of any political party or group and is funded predominantly through sponsorship of research and public policy debates. The views expressed in this publication are those of the authors, and these do not necessarily reflect the views of the sponsors or the Social Market Foundation.

DESIGN AND PRODUCTION
Pistachio Design
www.pistachiodesign.com

PRINTED BY
Diversified Global Graphics Group
www.dg3.com

CONTENTS

ACKNOWLEDGEMENTS

This research and publication have been made possible by the generous support of comparethemarket.com. I would like to thank the group of experts that offered advice and feedback during the project: Tom Webb, Simon McCulloch, Katy King, Anne Pardoe, Alistair Thompson, Will Mosseri-Marlio, Caroline Fletcher, Jake Eliot, and Paul Worthington. At the SMF, special thanks go to Nigel Keohane, Katie Evans, Emran Mian, Nida Broughton, and Matt Oakley for their intellectual input and guidance. The views expressed in this paper are those of the author, and not those of comparethemarket.com.

ABOUT THE AUTHOR

Ben Richards is a Researcher at the SMF, where he works on projects in a range of areas including policy and regulation in consumer markets, the impact of taxes, tax credits and benefits for low income households, and immigration policy. Ben recently completed a Ph.D. in Social Policy at the London School of Economics. He has previously worked as a Researcher at the Centre for Analysis of Social Exclusion, LSE, where his work included projects on cash transfers, poverty and inequality. He has also conducted research for charities including Oxfam and the Child Poverty Action Group.

EXECUTIVE SUMMARY

After several years of falling real wages, household finances are still tight for many. Strains on Government budgets and further cuts to come will leave some households under even more pressure, despite welcome improvements in wages in recent months. Yet things can be done to help households: many can save hundreds of pounds each year by shopping around for everyday items such as energy, broadband, and car insurance. An average household can save £200 by switching their energy provider, £160 by choosing a more suitable mobile tariff, and £288 by switching their broadband. Even bigger savings can be made by getting the right car insurance and mortgage deals. However, rates of switching are low, with many consumers missing out on these savings. 62% of consumers have never switched energy provider; and a majority have had their main current account for more than 10 years. There is substantial untapped potential for savings for UK households.

Why do so few consumers take advantage of better value deals? Traditional economic theory suggests they should. But insights can be found from social psychology and behavioural economics that give reasons for consumer inertia, and can provide a better understanding of how to overcome it. Using these insights we can design policy and regulation to help consumers engage, save substantial sums of money, and receive products and services that are better tailored to their needs. This also creates a virtuous circle: as consumer engagement increases, firms are pressured to lower prices, provide innovative new products, and respond to consumers' demands. A more competitive market provides even more choice and even better value.

This report therefore asks why so many consumers remain inert, how inertia varies between markets, and how we can best design policy and regulation to overcome it.

CONSUMER INERTIA VARIES CONSIDERABLY ACROSS MARKETS

We consider most of the markets in which households spend a considerable proportion of their money, including the markets where regulators have

noted past challenges with consumer engagement. Consumer inertia varies considerably between different markets. The car insurance market has particularly high rates of switching and consumer engagement. At the other end of the scale, the current account market is characterised by very low rates of switching, with many consumers remaining with their provider for 20 years or more. Figure E1 below demonstrates differences in consumer inertia between different markets. It shows switching rates in each market (including 'internal' switching to a different tariff with the same provider), along with some key market characteristics in each case. Switching is highest in the vehicle insurance market, with 32% of consumers having switched in the previous 12 months; and lowest in the current account market, with just 7% having switched (2013 data).

We find particular characteristics of markets that explain some of the variation in inertia. The car insurance market operates predominantly with fixed one-year insurance contracts. At the end of the contract, there is no 'roll-over' – customers must purchase another product. This creates a 'window' of time in which consumers must make a decision, and is one reason why switching rates for car insurance are relatively high. In contrast, the broadband, landline and mobile phone markets operate predominantly with minimum contract terms, but monthly payments are allowed to roll-over after the contract ends, often leaving consumers that do not switch on poor value deals. The absence of a window in which consumers must make a decision makes it more likely that consumers will allow their contract to roll-over.

Another practice that can in some cases create inertia is 'bundling', where several products are sold together in the same package. Examples include selling mobile phone handsets and tariffs as part of one contract; and banks making mortgage and insurance deals dependent on also having a current account with them. Bundling can have several effects. First, it can make comparability between the products of different firms difficult by obscuring the true price of each part of the bundle. Second, it can increase barriers to switching. If each part of the bundle was sold separately, a customer may wish to switch one or other product. When each part is sold together, consumers may not wish to switch all of the bundled products to a different provider. In some cases bundling can provide genuine value to consumers; but in other cases – where there is not a clear mechanism by which it increases value – it can increase consumer inertia.

Figure E1: Inertia across different markets, together with switching rates, and key features of each market

ENGAGED

INERT

Vehicle insurance	Mobile phones	Broadband	Energy	Digital TV	Credit cards	Mortgages	Current accounts
32%	21%	21%	17%	16%	11%	10%	7%
High rates of searching and switching	Consumers motivated by desirable handsets	High incidence of bundling	Fairly low switching despite big savings available	Most switching is 'internal' (same provider)	Higher rates of switching than other banking products	Perceptions of poor choice and low satisfaction	Many customers have never switched
Yearly policies with a 'window' to renew	Poor value when contracts are left to roll over	Often linked to landline contracts – increase in charges	Little difference in product quality	Historically a lack of choice – Sky main provider	Complex features of cards make comparison difficult	Choice deteriorated after financial crisis	Customers can remain 'loyal' for 20 years or more
Big savings for shopping around	Often 'bundled' with other telecoms deals	Can also be linked to digital TV and mobile	Market regulated to restrict number of tariffs	Choice is increasing with BT and Virgin	Credit score determines which deal consumers can get	But choice and switching increasing since then	Switching low despite '7 day switch' process

BEHAVIOURAL BIASES CAN AFFECT THE DECISION-MAKING PROCESSES OF CONSUMERS

How does consumer decision-making interact with the characteristics of different markets to affect inertia? Consumer decision-making can be understood in terms of four stages. We understand a fully engaged consumer as one that can effectively go through each of the four stages when making a decision. Consumers can exhibit inertia by failing to fulfil any one or more of these four stages:

1. **Motivate**: consumers must be motivated to identify their best value tariff and provider.
2. **Access**: consumers must be able to access information about the various offers available in the market.
3. **Assess**: consumers must be able to assess these offers in a well-reasoned way.
4. **Act**: consumers must be able to act on this information and analysis by purchasing the good or service that offers the best value to the customer.

Behavioural biases can create difficulties for consumers' decision-making, and different biases can affect different stages of the decision-making process. The key types of behavioural biases relevant to consumer decision-making are as follows.

Too much information. There is a limit to the amount of information consumers can process, particularly when the information is complex. A social psychology experiment investigated how consumers behaved when presented with a choice of jams to taste and purchase. Those offered a smaller selection were more likely both to purchase some jam after the tasting, and crucially also to be happy with their purchase. This suggests that consumers can make better decisions when confronted with less information. But it also suggests that some consumers may be put off entirely if confronted with an overload of information.

Framing. Consumers are sensitive to the way information is presented. For example, consumers might be attracted by a deal that is presented as 'half price', despite the fact that the 'full' price of the item is double what the product would cost elsewhere. Retirees' decisions over whether or not to purchase an annuity can also be affected by the way in which the decision is framed. Those seeing it as an investment decision are more likely to focus on the short-term loss of their capital and are less likely to purchase an annuity. Those framing it in terms of future consumption, by contrast, are more likely to consider the long term benefit of an income and are more likely to purchase an annuity.

Habits. Rather than continually making active decisions about how to perform day-to-day tasks, humans form habits that guide much of their behaviour. These habits are extremely useful in allowing our brains to think about the bigger issues. Everyday tasks are completed without having to do too much information processing. But they can create problems for making good decisions as consumers. Where behaviour is habitual, our intentions are not good predictors of our behaviour. This means that, even if consumers access and assess information to come to a well-reasoned decision, if they are behaving habitually they may not act on this decision.

Biased beliefs and inconsistent preferences. People are bad at predicting their own future preferences and needs. We might, for instance, over-estimate how much we will go to the gym, or how much we will use our mobile in future. But people can also suffer from 'time inconsistency', where their preferences change over time. Yesterday's decision to start the search for a new energy supplier might be less appealing today when the time comes to actually go out and do it.

POLICY RECOMMENDATIONS

Understanding how behavioural biases can affect the decision-making processes of consumers can help us understand how policy and regulation can be designed to reduce inertia. Our analysis of how inertia differs between markets can also guide the extent to which our recommendations are appropriate to each market. We have four key recommendations for policy and regulation.

1. Nudge consumers away from the practice of 'rolling over' their tariffs after contract expiry.

The way contracts are structured differs substantially between markets. In the car insurance market, for instance, contracts typically last for one year, and are not 'rolled over'. After the year ends, the contract finishes. At this point, consumers must purchase a new yearly insurance contract. In the mobile phone market, by contrast, contracts are typically 'rolled over' on a monthly basis after the contract ends. Consumers continue paying the same rate and are on the same tariff until they cancel the contract. This gives the opportunity for procrastination when the contract ends: rather than consumers having to enter a new contract, it is possible for them to do nothing. Almost half of mobile customers do in fact allow their contract to roll over after it expires, leaving them with a poor value deal in which they are still paying for a handset they already fully own.

We therefore recommend a number of steps to nudge consumers away from the practice of 'rollover'. However, the extent to which this is feasible depends on the market in question. There are three main options.

Option 1. Where consumers allow their contract to rollover, ensure firms improve communication with their customers to nudge them towards the best deal. In particular, firms would be obliged to contact consumers to inform them that their contract is ending, and to inform them of their options for getting a good value deal – including the possibility of purchasing from a different provider. Customers would also be sent an annual usage statement – similar to existing annual statements for credit cards – to help them make a better decision on their new contract.

Option 2. Introduce a regulated 'emergency tariff' for those failing to renew their contract before it ends. We believe this emergency tariff would be a way of making it clear to consumers that they are unlikely to be on the best deal once their contract ends. Providers would have the same obligations for communication with customers as in Option 1, but with the additional requirement that they repeatedly contact customers on the emergency tariff to discuss their options for contract renewal. The emergency tariff would be regulated to ensure it offers reasonable value. This option would

work well with the gas and electricity markets, since it would encourage consumers reaching the end of a good value tariff to find a new one.

Option 3. Restrict the practice of rollover contracts in specific markets in which this is feasible. This is currently the norm in the car insurance market; other markets could follow its example. This option could work well for the mobile phone, broadband, landline and digital TV markets, since the consequences of a consumer's tariff expiring are not as severe as for the energy market.

2. Greater transparency over the costs of 'bundled' products.

In many markets products are 'bundled' together. Customers may be sold a broadband contract, landline and TV service as part of the same package. Banks offer current accounts that include insurance and credit card deals at the same time.

In some cases the bundling of products offers genuine value to consumers, particularly where there is a clear cost saving for the firm. In these cases there may be a justification for bundling. In other cases, however, it can make it difficult for consumers to compare the prices of each of the products sold as part of their bundle with those of other providers. There are clear benefits to consumers being aware of the cost of each of these products.

We therefore recommend that, in cases where bundling does not offer any clear consumer benefit, firms should be obliged to break down the cost of each component part of a bundled product and clearly state each price on consumer bills. If there is a saving from having purchased the bundle, this should also be included. This practice is already the norm in the energy market, where prices for dual fuel energy tariffs are broken down to show separate gas and electricity costs. Savings associated with being on a dual fuel tariff are also shown separately.

In addition, we recommend that regulators consult on whether or not they can identify products that appear to be bundled together without justification. If there are no genuine cost savings to be made in bundling products together, the practice can be used simply to confuse consumers and make comparability difficult. A good place to start would be for Ofcom to consult on the consequences of restricting bundling of mobile handsets and mobile tariffs.

3. Implement an Active Consumer Week.

Evidence consistently suggests a significant proportion of the UK population are not motivated to engage with achieving better value in many consumer markets. There would be considerable benefits to a policy that could overcome some of the motivational barriers to consumer engagement. To do this, we recommend implementing a national Active Consumer Week (ACW) to be held once a year.

Regulators should co-ordinate with one another to decide upon the most appropriate week. A good possibility would be to use the first week in January – a time when typically many people are making New Year's resolutions and planning for the year ahead. Each regulator would be responsible for liaising with the firms within its remit to ensure they comply. Firms should be encouraged to offer fixed contracts of one or two years that start and end in ACW. Once a 'critical mass' of consumers were signed up to yearly or bi-yearly contracts that ended in ACW, this would become a regular time of year for switching. Because of the number of potential new customers firms would be incentivised to advertise their products at this time of year.

In addition, there should be a requirement for firms to write to all customers on 'rolling' tariffs to inform them they are likely to be overpaying and to give examples of ways they could achieve better value. This should be done in the run up to ACW to encourage consumers to shop around during this time.

An ACW would have considerable benefits. It would activate consumers that have never switched or don't switch often. Consumers would only have to engage with the switching process once a year, saving them time and hassle. Furthermore, those who switch several products at once would enjoy substantial savings in the same week. Given evidence suggests the size of savings is a key driver of engagement, this is important.

4. Expand and speed up the Midata initiative, and implement a consultation on encouraging people to make better use of their consumer data.

The Midata initiative is intended to give consumers greater access to their own personal data. The initiative has already made significant progress and, when rolled out fully, it should enable consumers to compare prices of different tariffs – based on their own usage data – and to switch simply and easily. However, more can be done.

One key problem is the fact that consumers' data is in several different places – consumers have to contact each of the providers of the products and services they use to access it all. Furthermore, providers have a vested interest in consumers failing to use this data, and may not wish to advertise its existence. It would be advantageous for consumers to be able to access this data from a third party, and it would also be advantageous if the data could be unified in one place for ease of use.

We therefore recommend several measures to expand and speed up the Midata initiative.

First, to speed up the full implementation of Midata by giving firms deadlines by which they must start providing relevant Midata information for consumers. A timeline should be drawn up of when the Midata initiative could be completed in all of its target markets. Regulators would need to assess the appropriate deadlines for each market, but there should be penalties for failing to comply.

Second, to implement a consultation on ways to encourage consumers to make better use of their usage data, including the possibility of introducing a Unified Data Portal (UDP). Such a portal would enable consumers to choose a third party to hold their usage information. Once permission had been granted by the consumer, firms would be required to send updated data to the portal provider on a monthly basis. Consumers would then be able to log into their account to access their data in one place. Consumers would be able to electronically share their data with a price comparison site of their choice, and to receive quotes from a variety of markets personalised to their own usage data. This would reduce the hassle of switching and make the products consumers are offered better tailored to their needs.

Provision of the UDP would not necessarily be a role for Government alone. There may be advantages to having a choice of providers. For example, consumers could choose to allow HMRC to hold their data, or Citizens Advice, or an appropriately regulated private company of their choice. However, we recognise that there are privacy risks and important technical barriers to be overcome to implement a UDP. This is why it is important to set up a consultation – including regulators, industry representatives and data protection experts – to examine the feasibility of a UDP, the risks involved, and to ensure that any risks identified are properly managed.

CHAPTER 1: INTRODUCTION

Following the global financial crisis household finances are still difficult. The UK has been through a period of declining real wages for several years. Although average wages are now starting to rise, there are further Government cuts to come and finances are still tight for many. The current climate gives little room for increased Government spending to improve standards of living.

Despite these pressures, there are routes to helping households improve their standards of living. Substantial amounts can be saved by getting better value deals on many consumer products, including energy, telecommunications, and financial products including bank accounts and insurance. In energy markets alone, Ofgem estimates that £2.7bn could be saved if consumers shopped around more, with the average household able to save £200 a year.[1] Evidence suggests that over 70% of consumers can save an average of £160 a year by choosing a more suitable mobile tariff,[2] and nearly half of consumers can save a further £92 a year on average by switching immediately after their mobile contract ends, rather than continuing to be charged for a handset they have already paid for.[3] Furthermore, consumers switching from a standard broadband tariff to a better value tariff can save £288 a year.[4]

Even bigger savings can be made by getting the right deals for car and home insurance, current accounts, credit cards, and mortgages. The median household with mortgage debt owes around £80,000. For this household, switching from a mortgage paying the average Standard Variable Rate to a better deal can save over £450 a year, even after fees and charges.[5] When savings from each of these markets are added together they represent a substantial improvement in a household's standard of living.

Yet many consumers do not shop around to take advantage of better deals – instead they remain inert and fail to take up better value products. Evidence suggests that a majority of consumers have been with their current account provider for more than 10 years;[6] and that 62% of domestic energy customers do not recall having ever switched supplier.[7]

Given the savings that can be made from taking up better value products, why do so many consumers remain inert? Explanations are difficult to find from within traditional economics – theoretically consumers should always behave such as to achieve maximum value. In recent years policymakers and regulators have instead started turning to behavioural economics and social psychology to uncover insights into and explanations for consumer behaviour. But much more can be done. Using these disciplines we can gain an improved understanding of consumer behaviour and create policy that is better tailored to what consumers actually do, and that is more effective in ensuring consumers get better value from the markets in which they spend money.

Overcoming consumer inertia creates a further important benefit. As consumer engagement increases, a virtuous circle is created: firms are pressured to lower prices, provide innovative new products, and respond more closely to consumers' demands. Consumer engagement drives a more competitive market, and a more competitive market provides even more choice and even better value for everyone.

The aim of this report, therefore, is to explore ways in which policy and regulation can be improved – in the light of evidence from behavioural economics and social psychology – in order to reduce consumer inertia, increase the value consumers get from the products and services they buy, and improve household finances. The key research questions are as follows:

- Why do many consumers remain inert?
- In which markets is inertia the most significant problem, and why?
- What innovative, practical and affordable solutions for policy and regulation can help consumers engage more effectively, thereby driving competition, increasing consumer value, and improving household finances?

Chapter 2 explores consumer engagement and inertia across each of the markets we consider. It demonstrates the great variation in inertia across different markets and highlights key characteristics of markets with high and low levels of inertia. Chapter 3 discusses explanations for consumer inertia from behavioural economics and social psychology. It identifies key behavioural biases that affect consumer inertia, and considers at which point in the four-stage consumer decision-making process each bias operates. Chapter 4 highlights the importance of getting policy and regulatory reforms right, before detailing our four key policy recommendations to help overcome consumer inertia.

CHAPTER 2: CONSUMER ENGAGEMENT AND INERTIA ACROSS DIFFERENT MARKETS

This chapter looks at the evidence on consumer engagement and inertia in key areas of household spending, and investigates how this varies across different markets. Are there certain markets in which consumers exhibit less inertia, and what are the key characteristics of these markets? Conversely, what are the characteristics of markets in which consumers exhibit most inertia?

The markets considered here are: gas and electricity; vehicle and home insurance products; banking products (current accounts, credit cards and mortgages); and telecommunications products (mobile phones, landlines, broadband, and TV). These represent significant areas of expenditure for consumers and are markets where regulators have noted past challenges with consumer engagement.

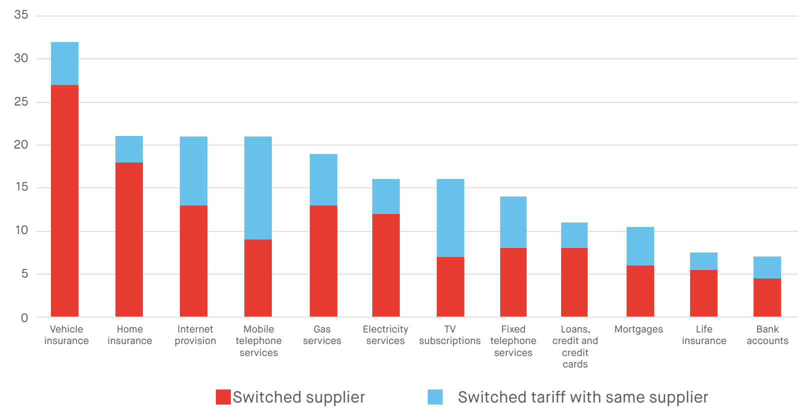
I. OVERVIEW OF INDICATORS OF INERTIA ACROSS KEY MARKETS

Below we examine evidence of consumer inertia across consumer markets. One useful indicator is the rate of consumer switching in that market. A high rate of switching should indicate lower levels of consumer inertia, particularly in markets in which providers offer good value deals to tempt new customers (implying that most consumers would have something to gain by switching). However, rates of switching do not tell the full story. A market may have a low rate of switching because many customers are very happy with their existing product or service. In this case, consumers may extract little or no value from switching. Switching figures also do not capture 'internal switching', where consumers take a different product from their existing provider. Alternatively there may simply not be much choice in the market, so consumers have few options to switch to and from. In what follows, therefore, we consider switching rates in each of our core markets, but interpret them in light of other indicators, such as rates of customer satisfaction and levels of choice. Where relevant we also consider recent policy and regulatory developments in each market to give an understanding of the main advantages and problems in that market, along with potential drivers of consumer inertia.

Rates of switching

Switching rates vary significantly across different markets. As Figure 1 illustrates, the highest switching rates are recorded in car insurance, whilst lower rates are evident in some financial services such as life insurance and bank accounts. The disparity between switching between providers compared with switching between plans (sticking with the provider) is also noticeable. For instance, a very low proportion of consumers switch between providers of TV subscriptions, but most of those who switch home insurance policies do so with a new provider.

Figure 1: Proportion of the UK population that have switched tariff plan or supplier in previous 12 months (%)



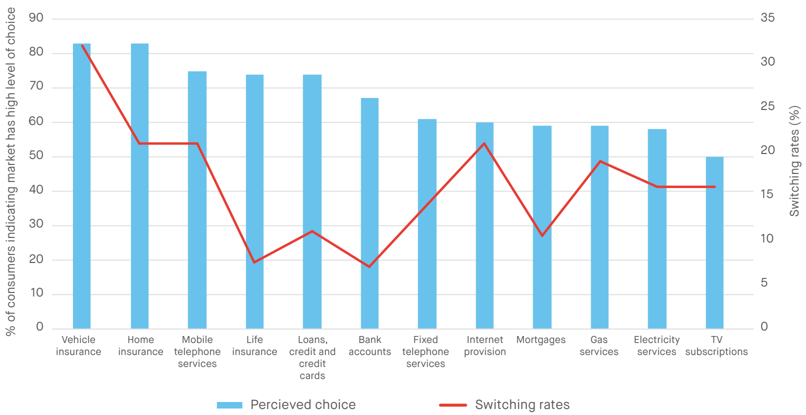
Source: EUROPA consumer dashboard, 2013 data.[8] The EUROPA data used in this report refer to the UK only.

Choice between different providers

Could low rates of switching indicate insufficient choice in a market? Figure 2 illustrates responses to a question asking consumers: 'On a scale of 0 to 10, would you say there are enough different retailers / providers you can choose from?' Insurance markets – and particularly vehicle and home insurance – score highly, indicating a high level of perceived consumer choice. With the exception of mobile phone services, telecommunications and energy markets score most poorly, with choice in TV subscriptions deemed to be particularly poor. Most financial products and services are rated somewhere in between, with the exception of mortgages, which are also rated poorly.

There appears to be some relationship between perceptions of choice and actual switching rates, but the relationship does not hold for all markets. The vehicle insurance market has both high rates of switching and high perceived choice. The TV subscription market has both a fairly low rate of switching and perceptions of poor choice. Yet for some of the other markets the relationship is less clear: the loans and credit market, for instance, has low switching rates and high perceptions of choice. Perceptions of choice alone, therefore, cannot fully explain differences in switching rates.

Figure 2: Consumer perceptions of choice in different markets (% of consumers indicating market has a high level of choice)



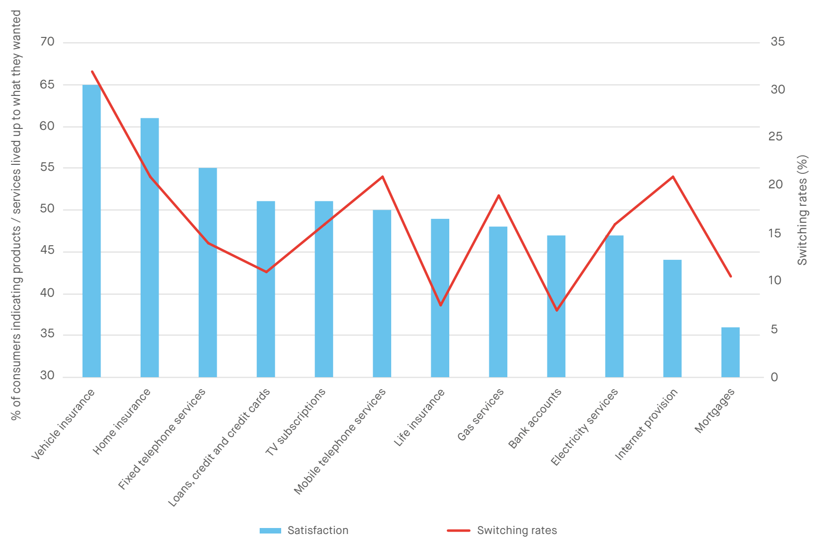
Source: EUROPA consumer dashboard, 2013 data

Consumer satisfaction with providers

Alternatively, low levels of switching could be an indicator that customers are satisfied with the products they currently have. Figure 3 illustrates levels of consumer satisfaction with their providers in a range of consumer markets. Vehicle and home insurance products again score well, with mortgage products scoring particularly poorly, and the other markets somewhere in between.

If low levels of switching were explained by customer satisfaction, one would in theory expect to find low levels of switching in markets with high levels of satisfaction. In some markets – particularly financial services – there appears to be a link, with loans and bank accounts both combining low levels of switching with reasonable rates of satisfaction. However, in many markets there appears not to be a link. Vehicle insurance, home insurance and mobile services have both high levels of satisfaction and relatively high rates of switching – the opposite of what one would expect. Again, it appears that levels of satisfaction cannot alone explain the variation in rates of switching between markets.

Figure 3: Consumer satisfaction with products and services across different markets (% indicating products/services lived up to what they wanted)



Source: EUROPA consumer dashboard, 2013 data

II. IN-DEPTH ANALYSIS OF KEY MARKETS

Gas and electricity

Household spending on gas and electricity makes up a significant part of household budgets. In a recent estimate, Ofgem calculated that households spent an average of £1,225 on gas and electricity in 2013.[9] Although some households use alternative fuels for heating, around 90% of UK households are connected to the gas network,[10] so spending in these markets constitutes an important expenditure for a very large number of UK consumers.

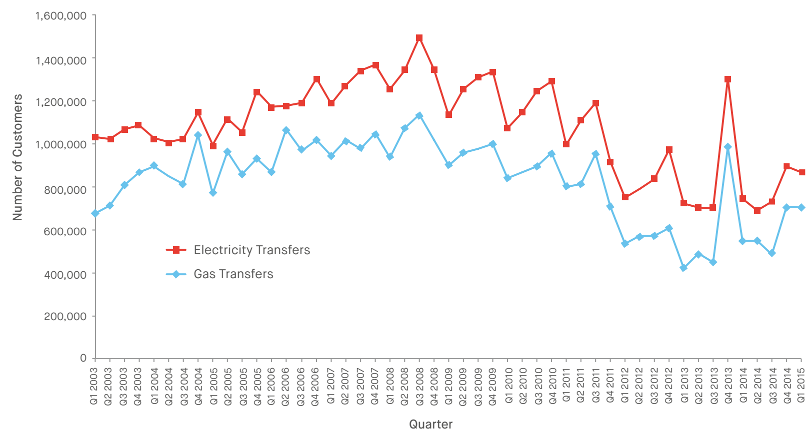
Energy market policy in recent years has been dominated by concerns about affordability. Domestic prices have frequently increased faster than inflation in recent years, and there is evidence that standards of service have dropped.[11]

A key method by which policymakers and regulators have sought to drive competition and lower prices in the gas and electricity markets is by encouraging consumers to switch providers, yet rates of switching remain low in both markets, with recent data suggesting only around 12% of domestic gas and electricity customers switched supplier over a 12 month period.[12] Survey evidence suggests that 62% of domestic energy customers do not recall having ever switched supplier.[13]

Furthermore, switching rates have fallen in recent years. Between 2008 and 2013 there was a gradual decline in switching (see Figure 4), although with a large spike in switching towards the end of 2013, which has been attributed to widespread media coverage of the large price hikes of the main energy retailers in 2013.[14] In 2014 and early 2015 switching rates have been relatively low, and it remains to be seen whether the spike seen in late 2013 has halted or reversed the downward trend.

What explains these low rates of switching? There is little evidence of widespread satisfaction with providers: only 51% of customers said they were satisfied, with customer complaints increasing 50% between 2011 and 2014.[15] There are also substantial gains to be made for consumers that do switch: dual customers of the six largest firms can expect to save an average of 14% - or around £160 per year – by switching; and some types of customer can expect to save more than 20%.[16] However, many consumers are either not aware of these price differences, or do not consider them to be large enough to motivate them to switch: around 45% of energy customers agree that ‘there is no real difference in the prices that energy suppliers charge’.[17] This perception is important since there is evidence that the expectation of gains from switching is the strongest driver of consumer activity in the electricity market.[18]

Figure 4: Quarterly rates of switching for domestic energy customers



Source: Quarterly domestic energy switching statistics, Department for Energy and Climate Change.[19] *Note, in Q1 2015 there were 28.065 million domestic electricity customers; and 22.089 million domestic gas customers.*

Insurance products

The UK vehicle insurance market has relatively high rates of switching compared to other consumer markets. In 2013, 27% of consumers had switched provider over the previous 12 months, compared with an average of just 13% across all consumer markets surveyed by EUROPA. A further 5% of consumers had changed products with the same vehicle insurance provider.[20]

However, these figures should be interpreted in the context of some other features of the car insurance market. Consumer trust in car insurance providers – in common with many other providers of private insurance – is particularly low. Indeed, trust in UK insurance companies is lower than trust in providers in any other market surveyed by EY, including trust in pharmaceutical companies and banks.[21] Consumers may therefore be less inclined to stay with their existing provider through feelings of loyalty.

Second, there is evidence of substantial choice in the vehicle insurance market. Respondents to a EUROPA consumer survey were much more likely than in other markets to feel they had sufficient choice of vehicle insurance provider.[22] There is also evidence that the way in which the timing of car insurance purchases are structured is beneficial for consumer engagement. Insurance policies are typically sold for the duration of one year, and rather than the policy 'rolling over' each month after that year ends, there is a requirement for the customer to actively purchase another policy before their existing one expires. Customers therefore face the prospect of a reasonably large annual bill about which they have to make an active decision. This decision is made more pressing by the fact that it is illegal for their car to remain on the road without insurance. The presence of a specific 'decision-making window' each year may have a role in reducing inertia, and may contribute to the relatively high rates of consumer engagement in the car insurance market.

The UK home insurance market has similarities to vehicle insurance in that consumers also have low trust in UK home insurance providers, and feel that the market gives a high level of choice of providers. However, this market differs from the vehicle insurance market in that there are substantially lower rates of switching, with only 18% of consumers having switched supplier in the last 12 months, and only a further 3% having changed products from their existing provider (2013 data).[23] It is unclear what drives this difference, although it may be attributable to higher costs in vehicle insurance or the triggers to seek out deals on contract renewal.

Banking products and financial services

The personal current account (PCA) market has relatively low levels of switching. Figure 1 above shows bank account switching rates to be one of the lowest. The FCA found that there were 80 million PCAs in the UK, of which 50 million had incoming monthly payments of more than £500 (2014 data). The number of PCAs opened annually remained broadly constant at around 6 million – approximately 7.5% of all PCAs in 2014.[24]

While choice for consumers is widening, it remains limited compared to many other markets. The share of the four largest UK banks has been decreasing since 2011, but still remains very large at 70%. Furthermore, there is evidence that price comparison websites – a key switching tool for many consumers – are used less frequently than in other industries.[25]

There is evidence that many customers stay with their PCA provider for a considerable period of time. Survey evidence found more than half of all respondents had been with their main PCA provider for more than 10 years, with 37% having been with their provider for over 20 years. 73% of customers had not shopped around in the last 3 years.[26]

There is little evidence that low rates of switching are driven by satisfaction alone. Figure 3 above indicates satisfaction with bank account providers is average relative to other markets – considerably higher than satisfaction with mortgage providers, but much lower than vehicle and home insurance providers. Furthermore, the FCA has identified excellent offers and clear benefits to switching for some segments of the PCA market, opportunities which are not yet being exploited.[27]

Various attributes of the PCA market may make it difficult for consumers to switch providers: comparability between products can be difficult because of the range of overdraft charges incorporated in products; information on service quality is also not always easily available or comparable. Other evidence suggests that a significant proportion of consumers believe it is complex and risky to switch accounts.[28] Recently a 7 day switching service has been implemented in an attempt to overcome some of these difficulties and boost rates of switching, but as yet evidence suggests there have been only modest improvements in consumer engagement. The Payments Council reported a 22% increase in switching volumes in the 12 months after the new switching service was implemented, although this improvement was from a very low base.[29]

The UK's credit card market has some similarities, although with somewhat higher switching rates than the PCA market. According to the FCA the market is working well for many consumers, but with significant concerns for some. Competition between providers focuses on particular card features that may not represent long-term value or sustainability, and some consumers may not be choosing a credit card that best meets their needs. Additionally, there is evidence of excessive profit making from higher risk borrowers and of cross-subsidisation across customer groups.[30]

Many consumers purchase products without comparing the options available. An OFT survey found that around 70% of consumers who took out a credit card in the previous three years did not shop around for it at all.[31]

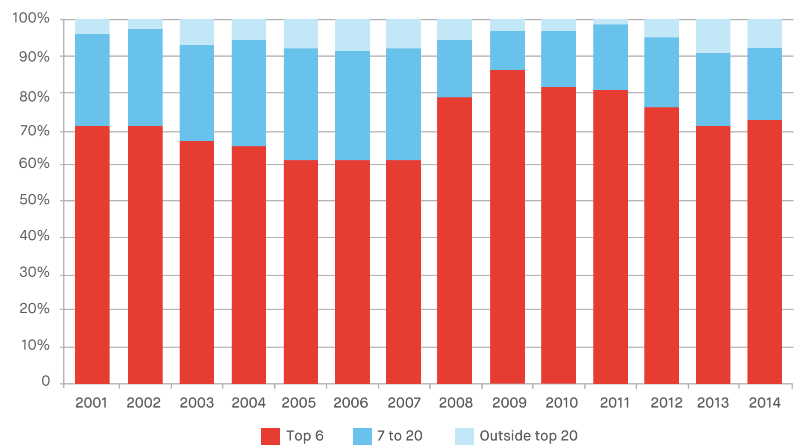
Credit cards being sold as bundled deals with bank accounts can sometimes represent poor value for certain consumers and also discourage consumers from shopping around. There is evidence that, of those consumers that do shop around, many focus on only one feature of a card – such as a 0% balance transfer or the APR rate – and so do not have a broad view of value for money. This problem is compounded by the fact that different cards have many different types of features, making comparability difficult. For instance, cards can have several different interest rates applying to different types of balance – such as spending and cash withdrawals – with promotional rates and cashback rewards creating additional complexity.[32]

A particular concern relating to credit markets is the fact that an individual's credit score and personal circumstances determine the product they are offered.[33] A consequence of this is that consumers do not know which product they are eligible for – or the exact terms of the product – until they have applied, making comparisons between products extremely difficult. In theory a consumer would need to apply for every product in order find the best available – a process that would not only be extremely time consuming, but would also adversely affect that consumer's credit score. This latter feature of the credit application process can also discourage consumers from shopping around because of a concern that multiple applications could affect their credit score.[34]

Mortgages

Due to their cost, mortgages are a crucial element of household finances. Historically, the mortgage market was one of the more competitive markets in financial services. Prior to the financial crisis, switching rates were relatively high and products spread across a somewhat wider range of providers. Following the crash, market concentration increased and switching rates plummeted.[35] In addition, the spread between the Bank of England base rate and mortgage interest rates increased, suggesting that consumers were getting poorer value. Evidence suggests this spread increased by more than would be justified by an increase in costs.[36] Switching rates have since risen from this low point, but levels of satisfaction remain low, as do perceptions of choice.

Figure 5: Lending in the mortgage market – proportion of lending going to top providers



Source: CML Regulated Mortgage Survey [37]

Higher levels of regulation – and the impact of this regulation on the role of intermediaries and advice in mortgage decision-making - may have helped sustain higher levels of switching. The high and tangible cost of a mortgage facility is also likely to drive higher switching rates than for personal banking where the gains are lower and less tangible.

Lower switching rates are partly attributed to lower bank base rates and therefore low mortgage interest rates. But, some have noted concern that the low levels of switching coexist with significant gains to be made between the best and worst deals on the market.[38]

Telecommunications and media

Many telecommunications services are characterised by low rates of switching between providers, with switching plans with the same provider being a more common practice than in many other consumer markets.

One factor explaining this may simply be unusually high levels of consumer satisfaction. However, there is evidence of limited choice in the TV services market, with a small number of providers historically being dominant.[39]

Telecommunication services and products have been affected strongly by 'bundling'. This practice sees consumers offered a range of associated services and products for one single fee under a single contract. A recent survey found that 63% of consumers reported having bought communications services in a bundle.[40] This trend has been driven by market deregulation and by increased convergence between technologies. A recent academic study has analysed consumer survey data. It concluded that 'when services are bundled the probability of switching those services decreases significantly'.[41]

Potential explanations for low switching rates also include the low expected financial gains from switching, which are lower in telecoms and TV than in other services.[42]

The future may see improvements. From summer 2015, landline and broadband providers who use the Openreach network have introduced a new 'one touch' process. This will place the responsibility for the switch in the hands of the company the customer is moving to and reduce the risks to the consumer.[43]

Switching rates and perceptions of choice are somewhat better in the mobile phone market than for other telecommunications products. However, switching between mobile tariffs is more common than switching provider (see Figure 1). Ofcom has plans to improve the ease with which consumers can change mobile providers, with the intention of increasing switching rates between mobile networks in future.[44]

CHAPTER 3: WHY DO CONSUMERS REMAIN INERT? LESSONS FROM BEHAVIOURAL ECONOMICS AND SOCIAL PSYCHOLOGY

I. BUILDING ECONOMICS AROUND BEHAVIOUR

We can see from the switching figures in Chapter 2 that across a wide range of markets, relatively few customers change providers, and only slightly more even take the time to look around for a better deal. Across a wide range of household bills, consumers just keep paying the same company for the same service, without engaging with the market at all. This is costing consumers substantial sums – we would all be better off if we could find the motivation to switch.

This pattern of behaviour belies traditional economics, which states that consumers should always take the best deal available to them, using all the information they can access. In theory, active and well-informed consumers force firms to offer good value or face losing out to competition. If their provider isn't offering a good deal, consumers should switch. In real life, this just doesn't seem to happen; the perfectly rational consumer at the heart of traditional economic theory just doesn't exist. The conundrum is all the more puzzling when we know people want to make good financial decisions and find the best deals.[45]

In response to these realisations, we have begun to bring people back into economics, combining market insights with psychology to understand how consumers actually behave in markets, and why they make choices that don't lead them to the best results. In this chapter we explore the ways behavioural economics and social psychology explain the fact that consumers don't engage with the market, and the ways in which this relates to decision-making processes in consumer markets.

II. WHY DON'T PEOPLE MAKE CHANGES?

Behavioural economics points to several biases that mean consumers fail to get the best deal in markets. These can take many forms:

1. **Cognitive limitations.** There's a limit to the amount of data we can process, and the amount of information we can take in. Behavioural responses include being more likely to go for the first object on a list than to look down. Choice overload is a problem in some circumstances – with too many options to choose from where products differ in only minute ways, consumers lose patience with more choices.

2. **Framing.** We're vulnerable to the way things are framed – the way price and quality is presented. For example, pricing with special offers and multiple rates can make it hard to compare prices. Something which is labelled at half price is often perceived as being better value, even if it is no better than a product originally priced at the cut-down cost – which would originally have been a better deal. Contracts which offer "months free" or limited-term deals can evoke an emotional response in the customer and distract from clear comparison of value.

3. **Humans tend to form habits** – we have routines and when a pattern of behaviour is established, we tend to stick to it. Lots of the time this is a perfectly reasonable way to behave – you wouldn't get far in life if you actively considered what type of milk to put on your cereal every day! But making changes to these habits is often difficult, and can create problems for well-reasoned consumer decision-making.

4. **Biased beliefs.** Consumers aren't always good at predicting their own needs in the future or at accounting for the probabilities of different events. Firms can take advantage of this. For example, a consumer might not have a clear idea of how much they will use their mobile phone in future. A firm may use this to sell a more costly contract than is needed. Consumers also often underestimate the amount that they use an overdraft, meaning they don't pay that much attention to the fees charged when choosing a current account, allowing firms to make substantial profits.

5. **Inconsistent preferences.** People can want a better value product most of the time, but at the point in which effort is needed to search for a new deal they put too much weight on short term search costs, and fail to switch.

But how do these behavioural biases relate to different parts of the consumer decision-making process? How can these insights help us understand consumer decision-making in a way that offers potential policy and regulatory solutions?

Here we use the (now disbanded) Office of Fair Trading's consumer decision-making framework, and consider how each behavioural bias relates to this decision-making framework. In the light of insights from the behavioural economics and social psychology literatures, we modify the framework and introduce a new, fourth part of the process, coming before each of the other three. One of the key insights of the literature on inertia is that, in order to 'access' information in the first place, a consumer must be motivated to do so. The new four-stage decision-making process, therefore, is as follows.

In order for consumers to drive competition they need to:

1. Be motivated to identify their best value tariff and provider;
2. Access information about the various offers available in the market;
3. Assess these offers in a well-reasoned way;
4. Act on this information and analysis by purchasing the good or service that offers the best value to the customer.[46]

Figure 6 demonstrates how each of the behavioural biases we identify as potentially important for inertia relates to this four-stage consumer decision-making process. Each of the types of behavioural bias, and their implications for consumer inertia, is discussed below.

Figure 6: Behavioural biases that can cause inertia

Type	Examples	Motivate	Access	Assess	Act
Too much information	Limit to amount we can process	■	■	■	
	Coping strategies include going for first object on a list			■	
	Ostrich problem – don't want to know getting bad deal	■			
Framing	Vulnerable to presentation of information			■	
	Incomparable pricing			■	
	Loss aversion – regret more than missing out on gains			■	
Habits	We use routines to avoid having to make irrelevant decisions	■			■
	We delay decisions unless prompted	■			■
	Tend to take default option, rather than making active choice			■	
Biased beliefs	Probability of future needs – e.g. mobile, gym, overdraft usage			■	
	Endowment effect – value things we own more	■		■	
Inconsistent preferences	Time inconsistency – preferences change when effort needed	■			
	Time inconsistency – too much weight on present 'teaser' deals			■	

Source: author's analysis

Too much information

Biases can relate to the way in which consumers use information, and can take several forms. There is a limit to the amount of information it is possible for consumers to process, which can be a particular problem where the information is complex – they are, in behavioural economics, 'boundedly rational', rather than fully rational beings capable of making use of infinite information. There are many examples of this. For instance, an attempt was made to boost participation by increasing the number of pension fund options savers could choose from. However, instead of the increased choice being viewed in a positive light, the increased complexity put customers off and was linked to a decrease in participation rates.

Psychology experiments uncovered similar findings when investigating how people responded to a simpler or more complex set of choices in purchasing gourmet jams and chocolates. People were more likely to purchase gourmet jams or chocolates when offered only 6 choices rather than 24 to 30 choices. Furthermore, those offered the more limited choice of 6 options reported greater satisfaction with their selection afterwards.[47] These studies clearly highlight that, in consumer decision-making, more information – even when of good quality – is not necessarily better, and can in many situations be counter-productive.

In the face of complex information consumers can adopt several approaches to decision-making that are at odds with traditional concept of the 'rational economic consumer'. One approach is to opt for the first item on a list rather than compare each item systematically. Other options include adopting rules of thumb, or looking only at a subset of the information to make decision-making less complex.[48]

Another problem is known as the 'Ostrich problem'. Often consumers don't want to know that they're getting a bad deal. Instead, they 'bury their heads in the sand' and avoid thinking about the extent to which their energy or insurance provider is giving them good value. In many instances people avoid or reject information that would help them to monitor their progress.[49] People are often defensive to information that contradicts their views.[50] Experimental evidence suggests that in cases where participants expect they have performed poorly, they don't wish to have this confirmed.[51]

Biases in the way choices are framed

Consumers are vulnerable to the way in which information is presented. Comparison may be difficult; alternatively some options may be favoured by their setting or positioning. Consumers may find an offer presented as 'half price' attractive despite the fact that the previous price was double what it could be bought for elsewhere.[52] Presenting a bundle of two items – such as an online and print subscription together – alongside an option of one only and for the same price – can influence decision-making, and give the impression of better value compared to providing one single price alone.

The framing of the costs, losses or gains may also affect the motivation of some to engage in a market and indeed the decisions they ultimately take. For example, there is evidence that retirees may be put off buying an annuity because of an excessive focus on the immediate and tangible loss of the capital sum, rather than the prospect of income spread out over many decades. Consumers framing an annuity in terms of an investment can be overly concerned with their short-term loss. Consumers who frame the decision to annuitise in terms of a 'consumption frame', in which the focus is on the end result of what can be spent over time, were more inclined to purchase an annuity.[53] Loss aversion may also deter people from switching because they notice the downside risks of switching more than they do any similar upsides.

Habits and consumer inattention

The habits that we form can aid or undermine decision-making. Routines and patterns of behaviour enable us to shortcut decision-making processes where these are basic and where repeating a full market analysis may not be worth the time (for instance buying milk or a newspaper each morning). Making such shortcuts should allow us to devote more time to bigger choices in life.[54]

However, these habits can create problems for making good decisions as consumers. Making changes to habits can be difficult.[55] And, evidence from social psychology shows that, where behaviour is habitual, people's stated intentions are not good predictors of their behaviour. This can mean that a consumer's conscious assessment of the best product or service for them may not correspond to their actual consumer behaviour because the routine of past acts may determine what they do in practice.[56] This can affect the 'motivate' stage of the consumer decision-making process if consumers simply act habitually without being motivated to consider their options. Alternatively, it can affect the 'act' stage if consumers are motivated to consider their options, access information and assess it in a reasoned way, but simply fail to act on their conscious decision.

Habitual behaviour could be one reason why, for instance, almost half of mobile customers do not switch immediately after their contract ends, but instead continue paying for a handset they have already bought.[57]

Biased beliefs

An important example of how people can have biased beliefs is in their judgement of their future needs and preferences. Evidence suggests people are likely to expect their current tastes and preferences to continue into the future and underestimate the possibility of change. In consumer markets this can manifest itself by consumers tying themselves into long and expensive mobile phone contracts on a tariff that they no longer need, and by overestimating their future potential to pay back credit card debt.[58] These tendencies predominantly affect the 'assess' part of the decision-making process, as people are unable to accurately weigh up their present and future needs.

Biased beliefs can also take the form of the 'endowment effect', whereby people attribute extra value to a good or service they already have.[59] This encourages people to retain their current good or service even when a better alternative is available, simply because of the fact they currently own or use that product. The endowment effect clearly creates a barrier to switching provider, and can affect the 'motivate' part of the decision-making process, since people do not want to look for alternatives as they value their existing product or service more. It can also affect the 'assess' part by inhibiting a well-reasoned evaluation of the different available products.

Individual actions may also be determined by conceptions of self-proficiency. If consumers don't expect switching to be successful they may be unready to summon the energy to start.

Inconsistent preferences

Inconsistent preferences can frequently take the form of 'time inconsistency', whereby people's preferences change from one moment to another. In consumer markets time inconsistency can explain, for instance, why people prefer 'teaser rate' credit cards, then fail to switch when borrowing lasts longer than first thought. The immediate reward of a 0% card outweighs the longer-term gains of choosing a different product.[60] Consumers may also put too much weight on present searching costs, compared to the payoff of lower bills in future. This leads them to spend less time searching than would be optimal.[61] Time inconsistency can affect the 'motivate' part of decision-making when they put too much weight on search costs; and can affect the 'assess' part of decision-making when immediate rewards are preferred over long-term gains.

III.IMPLICATIONS FOR POLICY AND REGULATION

Each of these behavioural biases impact on different stages of the consumer decision-making process. This can guide the most appropriate policy response to overcoming each bias, reduce consumer inertia, and ensure consumers get better value for the products and services they purchase. The next chapter builds on the key insights from behavioural economics and social psychology for each of the four stages of the consumer decision-making process; considers which markets each insight is more relevant to; and proposes concrete solutions for policy and regulation that could help to reduce consumer inertia.

CHAPTER 4: OVERCOMING CONSUMER INERTIA – RECOMMENDATIONS FOR POLICY AND REGULATION

This chapter combines the insights of Chapters 2 and 3 in establishing the key barriers to engagement – and causes of inertia – in each of the four stages of the consumer decision-making process across UK markets. It proposes recommendations for policy and regulation that can overcome these barriers and reduce consumer inertia.

I. THE NEED FOR CAREFUL POLICY DESIGN: WHEN REFORMS GO WRONG

First, however, it is informative to consider some examples of previous policies intended to remedy behavioural biases. Although policy and regulation has increasingly been building on the insights provided by the behavioural economics and social psychology literatures, there have been recent examples of well-intentioned policies that have had adverse consequences. Examples of such policies can highlight the importance of getting policy right by understanding markets and consumer behaviour in the fullest possible way, and provide context for the policy recommendations that follow.

Consumer responses to cooling off periods

Cooling-off periods are often considered to be an appropriate policy measure in situations where consumer decision-making is motivated by excitement, fear or impulse. A cooling-off period can allow consumers time to reflect on their purchase when their decision-making is motivated by other, more 'rational', factors. In part for these reasons, consumers in the UK are legally entitled to cooling-off periods for several types of purchase, including when purchasing goods and services online.

However, although they are well-intentioned, there is evidence that cooling-off periods can – in some situations – have unintended consequences. Other behavioural biases can be introduced into the decision-making process, such as consumers being less reflective at the point of sale since they know they are able to reverse the decision later. Yet subsequently consumers may be inert and fail to cancel or return the product and service within the allocated timeframe. Moreover, there is evidence that the length of the cooling off period is related to the likelihood of cancellation, with longer timeframes associated with lower chances of cancellation.[62]

Unintended consequences of 'non-discrimination clauses'

In the late 2000s energy companies in the UK adopted a practice of offering discounts to new customers joining them in parts of the country in which they were not yet established. The result was that they offered prices that were around 10% lower in areas in which they were new entrants into the market, compared with their 'home area'. One effect of this was that those who switched paid around 10% less than those who didn't. This concerned Ofgem, particularly because those failing to switch were more likely to belong to vulnerable groups.

In 2009 Ofgem responded to these practices by introducing a 'non-discrimination clause' to prevent companies from offering different deals in different areas of the country. As a result, however, the average amount saved from switching reduced by more than 50%; and many companies withdrew from the new areas they had gone into, retreating into their home areas. This resulted in a dampening of competition, with evidence of increases in the profits of energy firms and price rises for many consumers. Ofgem subsequently declined to renew the non-discrimination clauses when they expired.[63]

II. POLICY RECOMMENDATIONS

With these warnings in mind, and in the light of insights from Chapters 2 and 3, our recommendations for policy and regulation are as follows.

1. Nudge consumers away from the practice of 'rolling over' their tariffs after contract expiry.

The way that contracts are structured differs substantially between different markets. Car insurance gives us an example of a market that operates predominantly with one year fixed contracts. After the contract ends it is necessary to actively renew the contract. This gives several advantages. It provides a particular 'window' of time in which a decision must be made, or the contract will lapse. Evidence from the car insurance market suggests that the existence of this 'window' reduces the level of consumer inertia by providing a point of time in which a decision must be made. This is likely to be one reason why switching rates in car insurance are higher than other markets.

In addition, structuring a contract in this way gives no option for the contract to 'rollover' on the same tariff after the end date, in contrast to many telecommunications contracts. By rollover we mean that the contract is allowed to continue on a running monthly basis after the end of the contract. The crucial distinction is whether a contract finishes after its set end date, or whether the contract is allowed to continue after this date.

By contrast, mobile phone contracts are typically 'rolled over' on a monthly basis after a contract ends. Tariffs that combine a tariff and a handset typically offer poor value for those who let the contract rollover after its end date, as after this point they are effectively paying extra for a handset they already own.

We therefore recommend a number of steps to nudge consumers away from the practice of 'rollover contracts'. However, this is likely to be easier in some markets than others. Exact solutions will therefore depend on the market in question.

Mobile contracts could easily be structured such that a customer paying for both a handset and tariff in a two year contract would no longer be left on the same rolled over contract after the two years had elapsed. Instead, the provider could contact the customer asking whether or not they wished to enter into another contract or not. If not, consumers could move over to a SIM-only deal. It would be more problematic, however, to structure energy contracts in this way, since it would be undesirable for consumers forgetting to renew their contract to have an interruption of their gas or electricity supply.

We recommend one of the following three options for each market. Regulators should consider the pros and cons of each, and decide which would be most appropriate for the market in question. However, we indicate below the markets in which each of the options has the potential to work well.

Option 1. Where consumers allow their contract to rollover, ensure firms improve communication with their customers to nudge them towards the best deal. In particular, providers would be obliged to contact consumers to inform them that their contract is ending, and to inform them of their options to get a good value deal – including options of purchasing from a different provider. Depending on the extent to which privacy issues are of concern, it may also be beneficial for other providers – or comparison sites – to contact consumers as well. This option would work well with credit card and current account markets, since it would require providers to contact consumers when the value part of their deal – for instance an introductory 'teaser' offer – had expired.

Option 2. Introduce a regulated 'emergency tariff' for those failing to renew their contract before it ends. Customers failing to renew would go onto an 'emergency tariff', which would be designed as a way of making it clear to consumers that they are unlikely to be on the best deal. The provider would have an obligation to repeatedly contact the customer to discuss options for renewing a contract and moving off the emergency tariff. Providers would also be obliged to inform them of their right to search for a new contract from another supplier. The emergency tariff would be regulated to ensure it offers reasonable value. This option could work well with gas and electricity markets, since it would encourage consumers reaching the end of a good value tariff to find a new one.

Option 3. Restrict the practice of rollover contracts in specific markets in which this is feasible. This is currently the norm in the car insurance market; other markets could follow its example. This option could work well for the mobile phone, broadband, landline and digital TV markets, since the consequences of a consumer's tariff expiring are not as severe as for the energy market. However, in 2011 Ofcom banned Automatically Renewable

Contracts, in which landline and broadband providers automatically committed customers to long term deals on the expiry of their current deal.[64] If implemented, Option 3 would therefore also need to ban auto-renewal practices, other than with the customer's explicit permission, in order to avoid the problems experienced prior to 2011.

2. Greater transparency over the costs of 'bundled' products.

In many markets products are 'bundled' together. A telecommunications company might sell a consumer a broadband contract, but include a landline, mobile phone tariff, and TV tariff at the same time. Banks frequently offer their customers current accounts that include several other items 'packaged' with it – often including insurance or credit card products.

In some cases the 'bundling' of products can allow firms to offer better value deals than would have been the case had they sold their products separately. In these cases there may be a justification for bundling. This could particularly be the case where there are cost savings to be made by providing two or more products at the same time. A possible example would be the installation costs associated with landlines, broadband and TV. If carried out at the same time by one engineer from a single company, costs may be lower than three separate companies carrying out the work independently.

In other cases, however, these deals can be confusing and create difficulties in comparing similar products. For example, combining mobile tariff and handset charges into one contract makes it difficult to compare these contracts against the cost of SIM-only deals. Bundling in this case seems less justified: costs for mobile handsets are not directly related to costs of mobile tariffs. There is a concern that some firms can use these deals to reduce the clarity of information around their products, stopping customers from making direct comparisons.

There are clear benefits to ensuring firms break the costs of bundled products down by each component part. Charges for combined gas and electricity tariffs, for instance, already do this. Electricity charges are

reported separately from gas charges on consumer bills, and any applicable savings from being on a dual fuel tariff are deducted in a transparent way. Mobile contracts could easily do the same by separating handset and tariff charges. This would make comparability with other tariffs and handset retailers much easier. This would help overcome significant behavioural biases with regard to processing complex information, and with regard to framing information in a comparable way.

We therefore recommend that, in cases where bundling does not offer any clear consumer benefit, firms should be obliged to provide individual costs for component parts of a bundled product. This would allow for direct comparison between each of the component parts and the costs of other providers. Savings that derive from having purchased a bundle should also be clearly shown, so that consumers are aware of the value they get from buying products together.

In addition, we recommend that regulators consult on whether they can identify products that appeared to be bundled together without justification. If there are no genuine cost savings to be made by bundling products together, the practice can be used simply to confuse customers and make comparability difficult. A consultation on the bundling of mobile tariffs and handsets would be a good place to start. Ofcom could establish whether there are genuine cost savings in this practice, or whether it mainly serves to reduce comparability. Lessons could be taken that would inform the consultation into bundling in other markets.

3. Implement a national 'Active Consumer Week'.

Evidence consistently suggests a significant proportion of the UK population are not motivated to engage with achieving better value in many consumer markets. This can be for a variety of reasons: a minority are simply not aware that they have the option of exercising choice in energy supplier and communications provider; many consumers are demotivated by a perceived lack of choice and differentiation between providers; and others can be put off by perceived hassle or risks of switching, compared to a perception that the benefits of switching provider would be low.[65]

There would, therefore, be considerable benefits to implementing policies that can mitigate some of the barriers to consumers being motivated to engage with consumer markets, to raise awareness of the benefits of changing provider or tariff, and to assuage fears of the hassle and risks of doing so. For these reasons we recommend implementing a national Active Consumer Week (ACW) to be held once a year.

Active Consumer Week would involve several policies. First, there would need to be co-ordination by regulators of different markets to pick a week in which to implement Active Consumer Week. The first week in January could be a good possibility – a time when typically many people are making New Year's resolutions and planning for the year ahead. Each regulator would then need to work with firms in its jurisdiction to ensure they implement fixed contracts of one or two years that start and end in ACW. Once a 'critical mass' of consumers were signed up to yearly or bi-yearly contracts that ended in ACW, this would become a regular time of year for switching. Firms would be incentivised to advertise their products at this time of year by the large number of potential new customers.

Second, there should be a requirement for firms to write to all customers on 'rolling' tariffs – such as mobile customers on an old tariff and so still effectively paying for a handset they already own – to inform them they are likely to be overpaying and to give examples of ways they could achieve better value. This should be done in the run up to ACW to encourage consumers to shop around during this time.

A benefit of ACW would be that consumers are activated that have never switched or don't switch very often. This makes it a particularly advantageous policy to implement alongside others that tend to provide benefits for customers who are already engaged. An additional benefit is that consumers would not have to think about switching for most of the year, but only engage once a year. This would provide some of the advantages currently enjoyed by the car insurance market because of the way contracts are structured yearly, and with no rollover. Furthermore, they could switch several providers on the same day, giving them substantial gains across several markets, and potentially lowering perceived switching costs. Given that evidence suggests perceived gains are a key driver of switching in some markets this would be a very important tool to reduce inertia.

4. Expand and speed up the Midata initiative, and implement a consultation on encouraging people to make better use of their consumer data.

The Midata initiative is intended to give consumers greater access to their own personal data. This includes their own usage data and is available in a portable, electronic format. The intention is to enable consumers to gain insights into their own behaviour so they can make more informed choices about the products and services they purchase.[66] Consumers' bank account usage data, for instance, can currently be downloaded in spreadsheet-compatible format when they log into their online banking. The initiative has already made significant progress and, when implemented fully, should enable consumers to compare prices of different tariffs – based on their own usage data – and to switch simply and easily, by providing a link to their own usage data, and without the need to provide complex information.

The Midata initiative has the potential to make comparing providers and tariffs and completing switches much simpler and more effective. It also has the potential to motivate more consumers to engage, for those consumers previously put off by the complexity of information and the complications and hassle involved in accessing and assessing information. However, much more can be done both to expand the Midata initiative, and to speed up its development.

One current problem stems from the fact that the providers of consumer data have a vested interest in consumers not using it. Data on bank account usage, for instance, is currently given by existing bank account providers, who may not wish to advertise its existence to consumers. It would be advantageous for consumers to be able to access this information from a third party. Furthermore, it would also be advantageous for consumers to be able to access all of their data – across the different markets in which purchase goods and services – in one place.

We therefore recommend several measures to expand and speed up the Midata initiative.

First, to speed up the full implementation of Midata by giving firms deadlines by which they must start providing relevant Midata information for consumers. A timeline should be drawn up of when the Midata initiative could be completed in all of its target markets. Regulators would need to assess the appropriate deadlines for each market, but there should be penalties for failing to comply.

Second, to implement a consultation on ways to encourage consumers to make better use of their usage data, including the possibility of introducing a Unified Data Portal (UDP). Such a portal would enable consumers to choose a third party to hold their usage information. Once permission had been granted by the consumer, firms would be required to send updated data to the portal provider on a monthly basis. Consumers would then be able to log into their account to access their data in one place. Consumers would be able to electronically share their data with a price comparison site of their choice, and to receive quotes from a variety of markets personalised to their own usage data. This would reduce the hassle of switching and make the products consumers are offered better tailored to their needs.

Consumers could be allocated a Consumer Number (similar in concept to a National Insurance number) to use when comparing products and services. This Consumer Number could then be linked to an individual's UDP account. When using a price comparison website, for instance, consumers would simply be able to enter their Consumer Number – this would link to their UDP account, and products and services from a variety of markets could be compared, based on their actual usage data. This would have the dual advantage of providing products best suited to a consumer's actual behaviour, and prevent the consumer from having to go through the time consuming process of repeatedly entering information such as their address and date of birth. In addition, the ability to easily compare products across several markets at once using a price comparison website has the potential to increase the total gains a consumer could make from switching, and so could provide additional motivation that can prevent consumer inertia.

Provision of the UDP would not necessarily be a role for Government alone. There may be advantages to having a choice of providers. For example, consumers could choose to allow HMRC to hold their data, or Citizens Advice, or an appropriately regulated private company of their choice. However, we recognise that there are privacy risks and important technical barriers to be overcome to implement a UDP. This is why it is important to set up a consultation – including regulators, industry representatives and data protection experts – to examine the feasibility of a UDP, the risks involved, and to ensure that any risks identified are properly managed.

ENDNOTES

1. Department for Energy and Climate Change, *'Switch to save', 2015.* https://www.gov.uk/government/news/switch-to-save-27-billion-up-for-grabs-by-switching-energy-supplier
2. Which?, *'Mobile customers losing out on billions of pounds by being on wrong contract', 2015.* http://press.which.co.uk/whichpressreleases/mobile-customers-losing-out-on-billions-of-pounds-by-being-on-wrong-contract/
3. Which?, *'Millions of pounds wasted paying for mobiles people already own', 2015.* http://press.which.co.uk/whichpressreleases/millions-of-pounds-wasted-paying-for-mobiles-people-already-own/
4. MoneySavingExpert, *'Switching broadband can save £100s', accessed 16/09/2015.* http://www.moneysavingexpert.com/phones/cheap-broadband#switchsave
5. Standard Variable Rate (SVR) data taken from Bank of England average for July 2015. Median property debt data are from ONS, *'The Burden of Financial and Property Debt, Great Britain, 2010 to 2012', 2015,* http://www.ons.gov.uk/ons/dcp171776_412308.pdf. Savings are based on author's calculations, using mortgage offers from www.moneysavingexpert.com, accessed 16/09/2015.
6. CMA, *'Retail banking market investigation: Updated issues statement', 2015.* https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/428973/Updated_Issues_Statement_2015.pdf
7. Ofgem, *'State of the Market Assessment', 2014.* https://www.ofgem.gov.uk/ofgem-publications/86804/assessmentdocumentpublished.pdf
8. Note: *Switching period in Europa data is 24 months for life insurance, bank accounts, mortgages and loans, credit and credit cards.* For these products the Europa data was divided by 2 to give comparable switching data in a 12 month period. See Europa, page 16: http://ec.europa.eu/consumers/archive/consumer_research/editions/docs/monitoring_consumer_markets_eu_2012_en.pdf
9. Ofgem, 'Infographic: Bills, prices and profits', 2015. Average dual fuel household bill. 2013 data and prices. https://www.ofgem.gov.uk/publications-and-updates/infographic-bills-prices-and-profits
10. Department for Energy & Climate Change, *'LSOA estimates of households not connected to the gas network', 2015.* https://www.gov.uk/government/statistics/lsoa-estimates-of-households-not-connected-to-the-gas-network
11. CMA, *'Energy market investigation: Summary of provisional findings report', 2015.* https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/442500/EMI_PFs_Summary.pdf
12. UKRN, *'Consumer engagement and switching', 2014.* http://www.ukrn.org.uk/wp-content/uploads/2014/12/Statement-Consumer-engagement-and-switching.pdf
13. Ofgem, *'State of the Market Assessment', 2014.* https://www.ofgem.gov.uk/ofgem-publications/86804/assessmentdocumentpublished.pdf
14. Ofgem, *'State of the Market Assessment', 2014.* https://www.ofgem.gov.uk/ofgem-publications/86804/assessmentdocumentpublished.pdf
15. Ofgem, *'State of the Market Assessment', 2014.* https://www.ofgem.gov.uk/ofgem-publications/86804/assessmentdocumentpublished.pdf
16. CMA, *'Energy market investigation: Summary of provisional findings report', 2015. Data are from 2012 – 2014.* https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/442500/EMI_PFs_Summary.pdf

17. Ofgem, *'Retail Market Review Baseline Survey', 2014.* https://www.ofgem.gov.uk/ofgem-publications/89113/ofgemrmrbaselinefinalpdf.pdf
18. Flores, M. & Price, C., *'Consumer behaviour in the British retail electricity market', 2013.* https://www.uea.ac.uk/mac/comm/media/press/2013/October/Switching+paper
19. Department of Energy & Climate Change, *'Quarterly domestic switching statistics', 2015.* https://www.gov.uk/government/statistical-data-sets/quarterly-domestic-energy-switching-statistics
20. EUROPA, *'Consumer Scoreboards Dashboard', 2015.* http://ec.europa.eu/consumers/consumer_evidence/consumer_scoreboards/market_monitoring/docs/dash3.swf
21. EY, *'Reimagining customer relationships: Key findings from the EY Global Consumer Insurance Survey 2014', 2014.* http://www.ey.com/Publication/vwLUAssets/ey-2014-global-customer-insurance-survey/$FILE/ey-global-customer-insurance-survey.pdf
22. EUROPA, *'Consumer Scoreboards Dashboard', 2015.* http://ec.europa.eu/consumers/consumer_evidence/consumer_scoreboards/market_monitoring/docs/dash3.swf
23. EUROPA, *'Consumer Scoreboards Dashboard', 2015.* http://ec.europa.eu/consumers/consumer_evidence/consumer_scoreboards/market_monitoring/docs/dash3.swf
24. CMA, *'Retail banking market investigation: Updated issues statement', 2015.* https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/428973/Updated_Issues_Statement_2015.pdf
25. CMA, *'Retail banking market investigation: Updated issues statement', 2015.* https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/428973/Updated_Issues_Statement_2015.pdf
26. CMA, *'Retail banking market investigation: Updated issues statement', 2015.* https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/428973/Updated_Issues_Statement_2015.pdf
27. CMA, *'Retail banking market investigation: Updated issues statement', 2015.* https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/428973/Updated_Issues_Statement_2015.pdf
28. Independent Commission on Banking, *'Final Report Recommendations', 2011.* http://webarchive.nationalarchives.gov.uk/20131003105424/https:/hmt-sanctions.s3.amazonaws.com/ICB%20final%20report/ICB%2520Final%2520Report%5B1%5D.pdf
29. FCA, *'Making current account switching easier: The effectiveness of the Current Account Switch Service (CASS) and evidence on account number portability', 2015.* https://www.fca.org.uk/static/documents/research/making-current-account-switching-easier.pdf
30. FCA, *'Credit card market study: terms of reference', 2014.* http://www.fca.org.uk/static/fca/documents/market-studies/ms14-6-1.pdf
31. Data are from 2008. OFT, Credit card comparisons, February 2008, OFT987.
32. FCA, *'Credit card market study: terms of reference', 2014.* http://www.fca.org.uk/static/fca/documents/market-studies/ms14-6-1.pdf
33. FCA, *'Credit card market study: terms of reference', 2014.* http://www.fca.org.uk/static/fca/documents/market-studies/ms14-6-1.pdf
34. FCA, *'Credit card market study: terms of reference', 2014.* http://www.fca.org.uk/static/fca/documents/market-studies/ms14-6-1.pdf

35. Independent Commission on Banking, *'Final Report Recommendations', 2011.* http://webarchive.nationalarchives.gov.uk/20131003105424/https:/hmt-sanctions.s3.amazonaws.com/ICB%20final%20report/ICB%2520Final%2520Report%5B1%5D.pdf
36. Independent Commission on Banking, *'Final Report Recommendations', 2011.* See page 348. http://webarchive.nationalarchives.gov.uk/20131003105424/https:/hmt-sanctions.s3.amazonaws.com/ICB%20final%20report/ICB%2520Final%2520Report%5B1%5D.pdf
37. Council of Mortgage Lenders, *'Largest lenders in 2014 reflect a competitive mortgage market', 2015.* https://www.cml.org.uk/news/largest-lenders-in-2014-reflect-a-competitive-mortgage-market/
38. Independent Commission on Banking, *'Final Report Recommendations', 2011.* See page 348. http://webarchive.nationalarchives.gov.uk/20131003105424/https:/hmt-sanctions.s3.amazonaws.com/ICB%20final%20report/ICB%2520Final%2520Report%5B1%5D.pdf
39. Oxera, *'BSkyB's profitability in the context of the Ofcom market investigation', 2010.* http://www.oxera.com/getmedia/46d48c44-ddbf-48ee-ac69-d89ebed5a96a/bskyb-s-profitability-in-context-of-ofcom-market-investigation-second-report.pdf.aspx
40. Ofcom, *'The Communications Market Report', 2015.* http://stakeholders.ofcom.org.uk/binaries/research/cmr/cmr15/CMR_UK_2015.pdf
41. Burnett, T., *'The Impact of Service Bundling on Consumer Switching Behaviour: Evidence from UK Communication Markets', 2014.* http://www.bristol.ac.uk/media-library/sites/cmpo/migrated/documents/wp321.pdf
42. Price, C. et al., *'Searching and Switching: Empirical estimates of consumer behaviour in regulated markets', 2013.* http://competitionpolicy.ac.uk/documents/8158338/8235394/CCP+Working+Paper+13-11.pdf/96adc02f-dd01-4d07-b5b0-f5e5404d07a1
43. Ofcom, *'Communications industry must serve customers better', 2015.* http://media.ofcom.org.uk/news/2015/communications-industry-serve-customers/
44. Ofcom, *'Communications industry must serve customers better', 2015.* http://media.ofcom.org.uk/news/2015/communications-industry-serve-customers/
45. Webb, T. & Sheeran, P., *'Does Changing Behavioral Intentions Engender Behavior Change? A Meta-Analysis of the Experimental Evidence', 2006.* http://www.communicationcache.com/uploads/1/0/8/8/10887248/does_changing_behavioral_intentions_engender_behavior_change-_a_meta-analysis_of_the_experimental_evidence.pdf
46. Adapted from: Office of Fair Trading, *'What does Behavioural Economics mean for Competition Policy?', 2010.* http://webarchive.nationalarchives.gov.uk/20140402142426/http:/www.oft.gov.uk/shared_oft/economic_research/oft1224.pdf
47. Iyengar, S. & Lepper, M., *'When Choice is Demotivating: Can One Desire Too Much of a Good Thing?', 2000.* https://faculty.washington.edu/jdb/345/345%20Articles/Iyengar%20%26%20Lepper%20(2000).pdf
48. Office of Fair Trading, *'What does Behavioural Economics mean for Competition Policy?', 2010.* http://webarchive.nationalarchives.gov.uk/20140402142426/http:/www.oft.gov.uk/shared_oft/economic_research/oft1224.pdf

49. Webb, T. et al., *'The Ostrich Problem: Motivated Avoidance or Rejection of Information About Goal Progress', 2013.* http://onlinelibrary.wiley.com/doi/10.1111/spc3.12071/epdf
50. Lundgren, S. & Prislin, R., *'Motivated Cognitive Processing and Attitude Change', 1998.* http://psp.sagepub.com/content/24/7/715.abstract
51. Webb, T. et al., *'The Ostrich Problem: Motivated Avoidance or Rejection of Information About Goal Progress', 2013.* http://onlinelibrary.wiley.com/doi/10.1111/spc3.12071/epdf
52. Centre for Competition Policy, *'Behavioural Economics in Competition and Consumer Policy', 2013.* http://competitionpolicy.ac.uk/documents/8158338/8193541/CCP+economics+book+Final+digital+version+-+colour.pdf/30214557-cace-4b0b-8aac-a801bbde87bc
53. MacDonald, B. et al., *'Research and Reality – A Literature Review on Drawing Down Retirement Financial Savings', 2013.* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2003891
54. Wood, W. et al., *'Habits in Everyday Life: Thought, Emotion, and Action', 2002.* https://dornsife.usc.edu/assets/sites/208/docs/Wood.Quinn.Kashy.2002.pdf
55. Gollwitzer, P. & Sheeran, P., *'Implementation Intentions and Goal Achievement: A Meta-Analysis of Effects and Processes', 2006.* http://www.researchgate.net/publication/37367696_Implementation_Intentions_and_Goal_Achievement_A_Meta-Analysis_of_Effects_and_Processes
56. Wood, W. et al., *'Habits in Everyday Life: Thought, Emotion, and Action', 2002.* https://dornsife.usc.edu/assets/sites/208/docs/Wood.Quinn.Kashy.2002.pdf
57. Which?, *'Millions of pounds wasted paying for mobiles people already own', 2015.* http://press.which.co.uk/whichpressreleases/millions-of-pounds-wasted-paying-for-mobiles-people-already-own/
58. FCA, *'Occassional paper No 1. Applying behavioural economics at the Financial Conduct Authority', 2013.* https://www.fca.org.uk/static/documents/occasional-papers/occasional-paper-1.pdf
59. Ofgem, *'What can behavioural economics say about GB energy consumers?', 2011.* https://www.ofgem.gov.uk/ofgem-publications/39711/behaviouraleconomicsgbenergy.pdf
60. Ofgem, *'What can behavioural economics say about GB energy consumers?', 2011.* https://www.ofgem.gov.uk/ofgem-publications/39711/behaviouraleconomicsgbenergy.pdf
61. Ofgem, *'What can behavioural economics say about GB energy consumers?', 2011.* https://www.ofgem.gov.uk/ofgem-publications/39711/behaviouraleconomicsgbenergy.pdf
62. Centre for Competition Policy, *'Behavioural Economics in Competition and Consumer Policy', 2013.* See page 101. http://competitionpolicy.ac.uk/documents/8158338/8193541/CCP+economics+book+Final+digital+version+-+colour.pdf/30214557-cace-4b0b-8aac-a801bbde87bc
63. Centre for Competition Policy, *'Behavioural Economics in Competition and Consumer Policy', 2013.* See page 77. http://competitionpolicy.ac.uk/documents/8158338/8193541/CCP+economics+book+Final+digital+version+-+colour.pdf/30214557-cace-4b0b-8aac-a801bbde87bc
64. Ofcom, *'Ofcom bans rollover contracts', 2011.* http://consumers.ofcom.org.uk/news/ofcom-bans-rollover-contracts/
65. UKRN, *'Consumer engagement and switching', 2014.* http://www.ukrn.org.uk/wp-content/uploads/2014/12/Statement-Consumer-engagement-and-switching.pdf
66. Department for Business, Innovation & Skills, *'The midata vision of consumer empowerment', 2011.* https://www.gov.uk/government/news/the-midata-vision-of-consumer-empowerment