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When Times are Tough

Tracking household spending and debt through diaries – interim findings

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Challenging ideas – Changing policy

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ippr, 30-32 Southampton Street, London WC2E 7RA. Tel: +44 (0)20 7470 6100 E: info@ippr.org www.ippr.org. Registered Charity No. 800065

About the contributors

This briefing was written by Dalia Ben-Galim with Tess Lanning and contributions from Lucia Durante and Rachel Seal-Jones.

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Introduction

The financial crisis and recession have highlighted the unsustainable nature of the economic growth that went before. While there is much discussion around the recession, global capitalism and what principles will underpin economic recovery, ippr has been exploring the particular impacts on families as part of a ground-breaking project on consumer spending and debt. Through this innovative research – which looks at households' circumstances in great detail – we are gaining an understanding of people's daily expenditure.

This briefing presents the interim findings from our research, undertaken over four months with low-income families across the UK, which aims to produce in-depth understanding of the dynamics between spending, saving and debt. It provides fresh insight into the impact of the recession on the daily realities of people's lives.

The next stage of the project will analyse the findings in more detail to offer insight into how families – specifically those on low incomes – are coping in the recession. It will also look at the savings and assets agenda and how people are coping with debt, with policy recommendations presented based on this analysis.

This briefing provides an opportunity to reflect on some of the emerging themes being generated from rich data collection and analysis. The findings here are illustrative.

Background: changes in consumption

Consumption is a key driver of economic growth and increasing consumption has been a feature of the significant rises in living standards in the UK over recent decades. However, this has created problems at the national and household level. Outstanding household debt has more than doubled since 2000 and has now reached £1.4 trillion; and the Citizens Advice Bureau reports that on average its debt clients owe £16,971, which is two thirds higher than in 2001 (Aznar 2009).

Changes in consumption affect different socio-economic groups in different ways. Based on a minimum income measure that the Joseph Rowntree Foundation has published, the minimum cost of living has increased by about 5 per cent over the last year for most families (Hirsch *et al* 2009). This is disproportionately skewed: families on low incomes spend a larger proportion of their household budgets on items such as food, fuel and public transport, all of which have increased in price, than higher-income households. Income inequality has also grown (Brewer *et al* 2009), with those at the bottom of the income scale not seeing their incomes rise as much as people further up the scale. Many households are becoming poorer and the combination of increased levels of debt, rising costs and income levels remaining fixed or falling presents significant challenges.

Research methodology

ippr's research employed an innovative methodology whereby low-income[1] families with children below working-age, located in London, Newcastle, Nottingham and Glasgow, took part in interviews and then completed a weekly diary for a month, thus providing a very detailed picture of spending and saving[2]. Furthermore, by working with families over a four-month period, we are able to look beyond a particular point in time, and understand the decisions that families make around spending and saving in more depth.

Profile of the sample

The sample was purposively selected to include men and women, a range of household sizes and types, ethnicity and employment status.

- There were 34 two-parent households, 22 with one parent, and two families living in extended households (with family or friends).
- The families have between one and five dependent children.
- The participants were largely female. Forty-five heads of household (self-selected to answer the questions on family finances), were female. The age of the participants ranged from 21 to 50 years old. There were 14 respondents aged between 21 and 30 years old,19 aged 31 to 40 and 25 were 41 to 50.
- Fifty households were white British, four were British Asian, two respondents were mixed race (West Indian/White British) and two were non-UK-nationals, both from Sri Lanka.
- Reflecting the prevalence of carers and the disabled among low-income households and benefit claimants in the UK, 16 of the households included someone with a disability.
- 22 households (16 of them couples) had mortgages. Two single mothers and one couple owned their house outright. Of the 33 renters, 15 had their rent paid by housing benefits (11 of them single mothers).

During the course of the project, the employment status changed in several households, creating fluctuations in levels of income and expenditure. This captures the sometimes fluid nature of employment for many families – particularly in a recession.

- At the start of the project, there were ten households with two adults in employment, 29 households with one adult in employment and 17 households with no employed adult. Additionally, two participants lived with extended family, and there were at least two working adults in both these households. One single mother lived with friends and one couple.
- By the end of the research period (four months later) many changes had occurred including in employment status in some cases, and in hours worked. For example, one participant, a single mother, became unemployed and moved in with her partner; a couple of participants lost their businesses and became unemployed; and several had their hours reduced by their employers.

1. A broad definition of low-income was used to reflect a range of households. The selection criteria were based on a measure of equivalised income (for example, a couple and one child: £226 per week or less and £11,752 per year or less). Other criteria such as household size, ethnicity and employment status were also considered.
2. Primary research was undertaken between December 2008 and May 2009 with 58 low-income families in Glasgow, London, Newcastle and Nottingham. Face-to-face interviews were conducted between December and January. Families were then asked to complete a weekly diary for a month. Between February and May, researchers contacted participants at regular intervals to understand whether there had been any significant changes to income and/or expenditure. Final interviews were undertaken in April and May with 52 families. Six families did not complete the research, but there are data from the early stages.

The sample was also purposively selected to expose the diversity of income among low-income families. This range has allowed for comparison across different social and economic circumstances. Over a third of the families in this sample were living below or just above the poverty line (Figures 1 and 2).[3]

Figure 1: Household weekly income before housing costs (BHC)

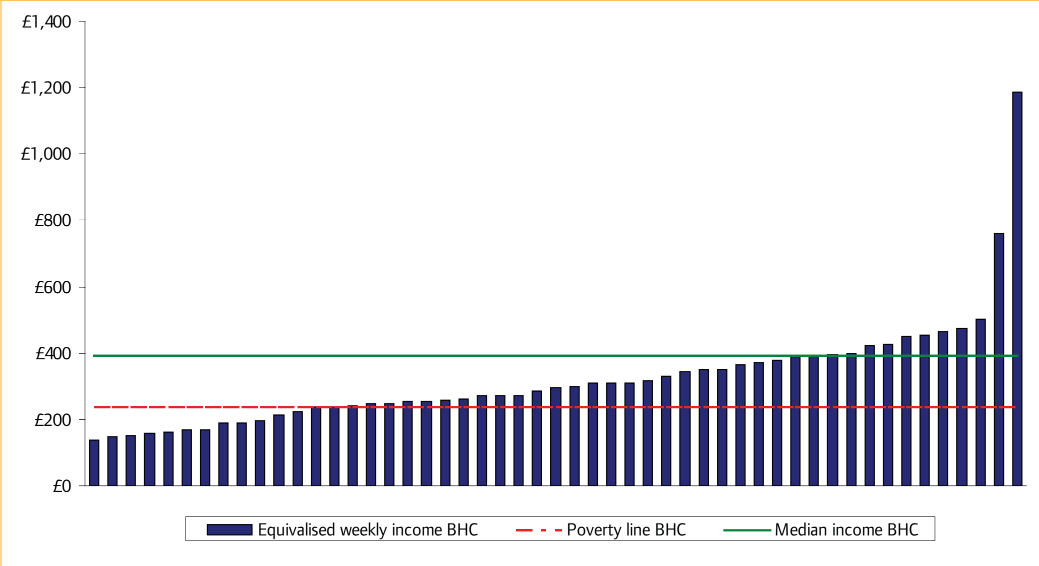
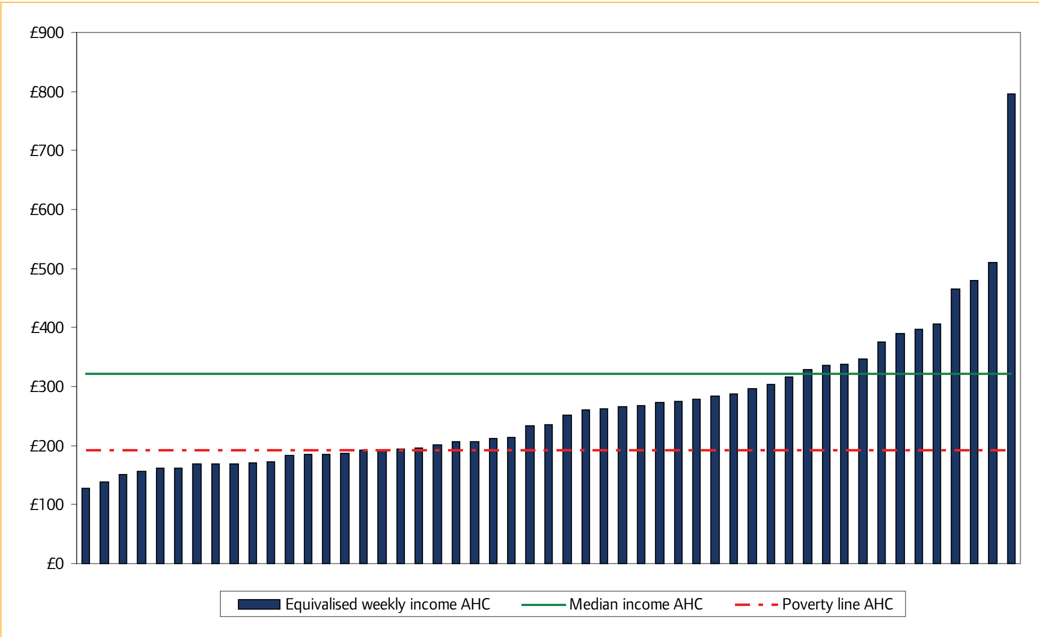


Figure 2: Household weekly income after housing costs (AHC)



Note to Figures 1 and 2: The data for seven households were incomplete and are therefore not included. The data were equivalised before and after housing costs, using the McClements Equivalence Scale that applies a weight to each household member, allowing for comparison between households. Poverty line and median income 2007/2008 levels from Households Below Average Income (DWP 2009)

The graphs show household equivalised income for families before and after housing against the median income levels and the poverty line. In both graphs, about a quarter of families were living below the poverty line, with approximately 80 per cent living below the median income levels.

3. During the project it became clear that two of these households fell outside the initial criteria for participation, with relatively high ratios of household income to the number of people in the households. One of these lost the only source of household income towards the end of the project and both adults in the second household were being threatened with redundancy. Both households were uncertain how they would cover outgoings.

Spending, saving and debt: emerging themes

While the analysis is ongoing, our interim findings highlight the different ways in which people budget, save, spend, earn and prioritise. They illustrate the dynamics of each of these in the context of household finances and the way that different families plan, cope and respond to changes.

Below we outline our findings in relation to:

- **Planning ahead** – how families plan for events and how they cope when there are unforeseen and unexpected increases in expenditure or decreases in income
- **Managing budgets** – methods that households use to manage tight budgets
- **Saving** – some of the ways that households save and some of the main barriers to short-term and longer-term saving
- **Borrowing and debt** – attitudes and methods towards borrowing and debt.

Planning ahead

Many families reported that they felt less financially secure compared with the same time last year and are concerned about their future financial stability as unemployment continues to rise.

All of the households in this research were particularly vulnerable to changes to their financial situation, including anticipated changes that could be planned for such as additional spending at Christmas and birthdays, and less foreseeable changes such as job losses. Some households seemed to feel protected by their level of income but as they became more vulnerable they found planning more difficult. Some families were more fearful than others about future spending demands and felt they would be unable to cope with any additional expenditure.

In particular, Christmas and summer holidays were acknowledged as being difficult times of the year because of their associated expense. But the amount that families spent on Christmas varied enormously and was only loosely correlated with levels of income. Certainly many families struggled through the Christmas period and it seemed to cause increased levels of stress and anxiety.

> 'Christmas is … just another bill… My brother and sister are very good to them [my children], they bought [my daughter] tickets to a big show last year that cost nearly £50, something I couldn't do… I mean my poor daughter, I've barely even bought her a stitch, she has all hand-me-downs from her friends, her wardrobes [are] full of Next but they are nothing that I've bought, 'cause I couldn't afford to.' (Male, Newcastle, two-parent household, two children)

The winter months bring additional financial pressures due to increased costs for electricity and gas, which disproportionately affect low-income families as a higher proportion of household budgets are spent on utilities:

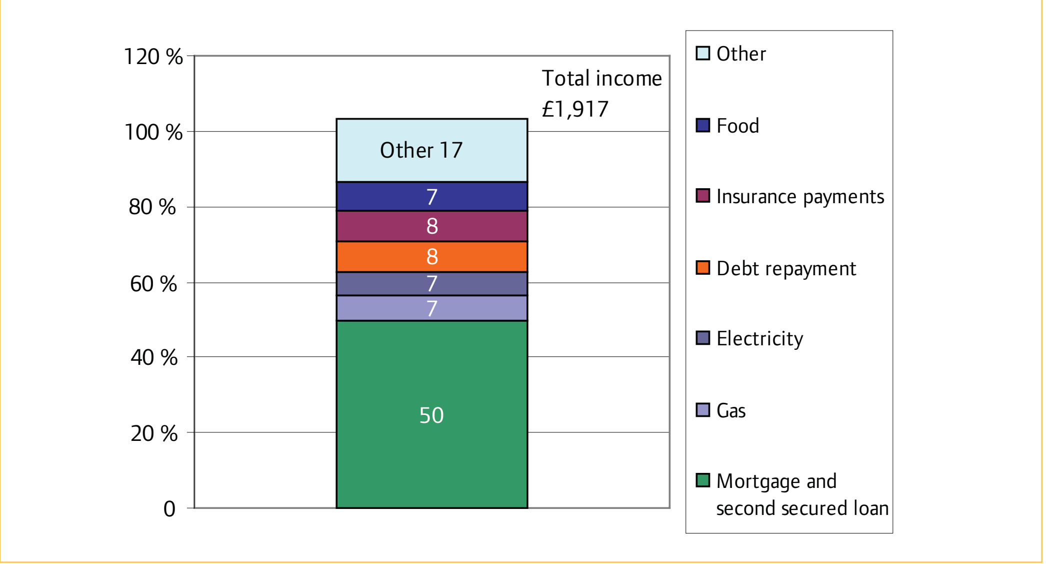
> 'This time of year … it's colder, your electrics are dearer. You've got your gas central heating on a lot more, you tend to buy in more food, comfort food, all these kinds of things.' (Female, 49, Glasgow, one-parent household, three children)

Living on tight budgets, with limited savings and disposable income makes unexpected shocks – such as the breakdown of a household item, divorce, illness, an accident or sudden job loss – all the more distressing.

Figure 3 illustrates the situation of a family in Glasgow where the only earner was made redundant just as the research began. The mortgage was covered by insurance, but the household's financial situation deteriorated over the course of the project. The couple were getting into debt to cover the basic cost of living. Several months after becoming unemployed their bank told them they were no longer entitled to an overdraft and they had to pay it back. They had relied on the overdraft to juggle payment priorities, and were concerned they would not meet household expenses. The family was spending a slightly higher proportion of their income on debt (excluding mortgage payments) than on food.

Figure 3: Couple with three children, unemployed, Glasgow

Expenditure as a percentage of income, November–December 2008



Managing budgets

Many low-income families have to manage very tight budgets. The example below (Figure 4) presents the income and expenditure of a single mother with one child, not currently in employment. Her monthly income totalled about £480. Increases in living costs were the most difficult to budget for and absorb: she told us how food and fuel costs were increasingly eating into her budget. To cope, she had begun shopping around more and reducing costs in other areas. She found that she was able to prioritise and budget to accommodate rising costs due to the stability of her income from benefits. As she knew exactly how much money was coming in each week and her housing was covered by Housing Benefit, she was able to spend within her means. She did not want access to mainstream credit, but preferred to borrow from family or from the Social Fund – a Government fund to which people can apply for help in emergencies.

Figure 4: Single mother, aged 24, one child, London

a) Expenditure as a percentage of income, November–December 2008

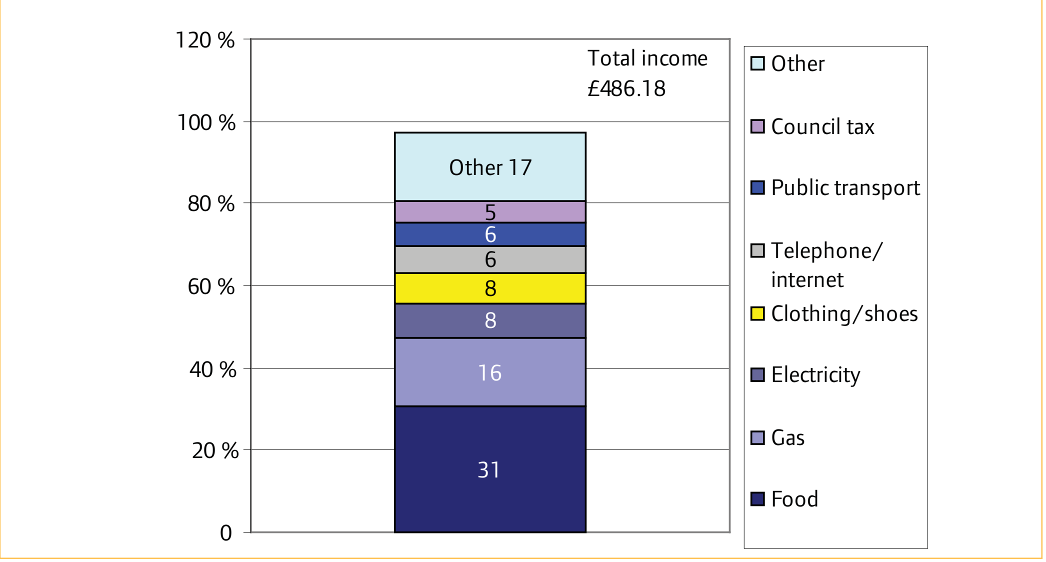
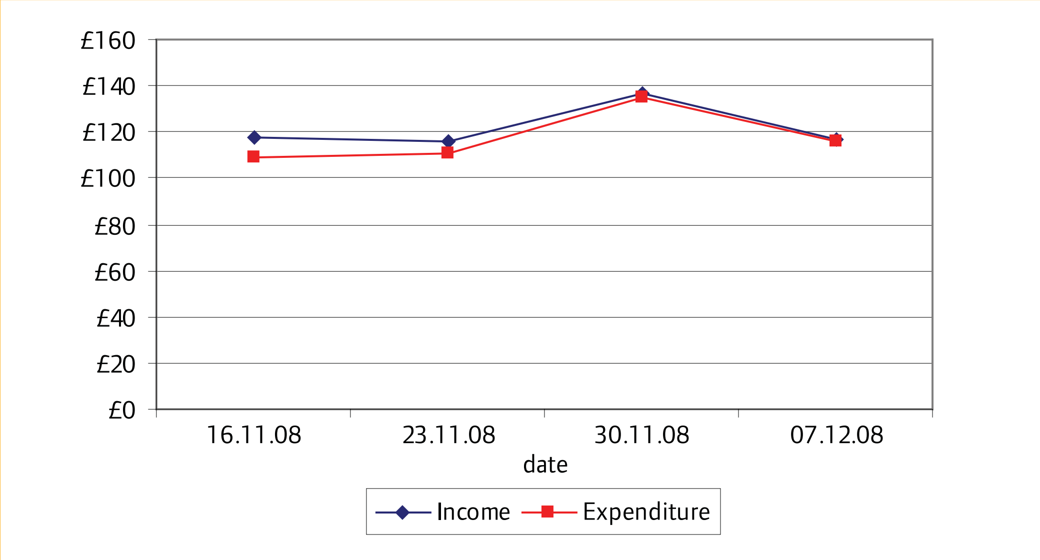


Figure 4: Single mother, aged 24, one child, London

b) Expenditure as a percentage of income, November–December 2008



The coping mechanisms that households employ to manage their budgets vary. Living within one's means has been found to be a mechanism in itself for families living on low incomes (Hills et al 2006). Increases in prices – particularly food and utilities – as well the impact of the recession meant that many families in our research were pragmatic about only buying what they could afford. Many talked about sacrificing certain luxuries like socialising, holidays and entertainment for their children. And many families compared their current situation with the past, when they considered themselves to have a better lifestyle:

> 'You know [before] we were able to do wee luxuries, take the kids to the cinema, get the train into Glasgow and go for a McDonalds...' (Female 38, Glasgow, two-parent household, three children)

Managing with a very tight budget has an emotional impact on families, with many feeling guilty about depriving their children, particularly around Christmas time:

> 'We're not going to the cinema any more. We tend to rent a DVD and we don't go mad or anything but we'll have a bag of chips. We're just not spendthrifts, we don't go out drinking. Christmas will be very tight, it's my grandson's first Christmas and I'm feeling very guilty that I can't spend what I want to spend on him.' (Male, 42, Nottingham, two-parent household, two children)

There is a strong evidence base highlighting how parents on low incomes prioritise their children's needs even as income levels fall (Bennett 2008). In particular, mothers in low-income households often use sophisticated budgeting plans to maximise their money. Among ippr's participants, the majority of finances were managed by women (although in some cases finances were managed by the male partner or both). This is common as women are often responsible for the management of household finances (Goode *et al* 1998). Many families had also changed their behaviour in order to budget more effectively. Doing more cooking from scratch, shopping around for cheaper deals and changing energy suppliers were all examples of how savings were being made.

Many participants were well aware of their weekly and often daily income and expenditure:

> 'I get my money every Wednesday in cash from the post office. So the income support and the child benefit both go in, and then I go and draw it all out in one lump. And then I just sit down and divide my money. I go straight to the supermarket and do my shopping so that comes first… and then I put petrol in on the way home … And then I get some money and put that in my

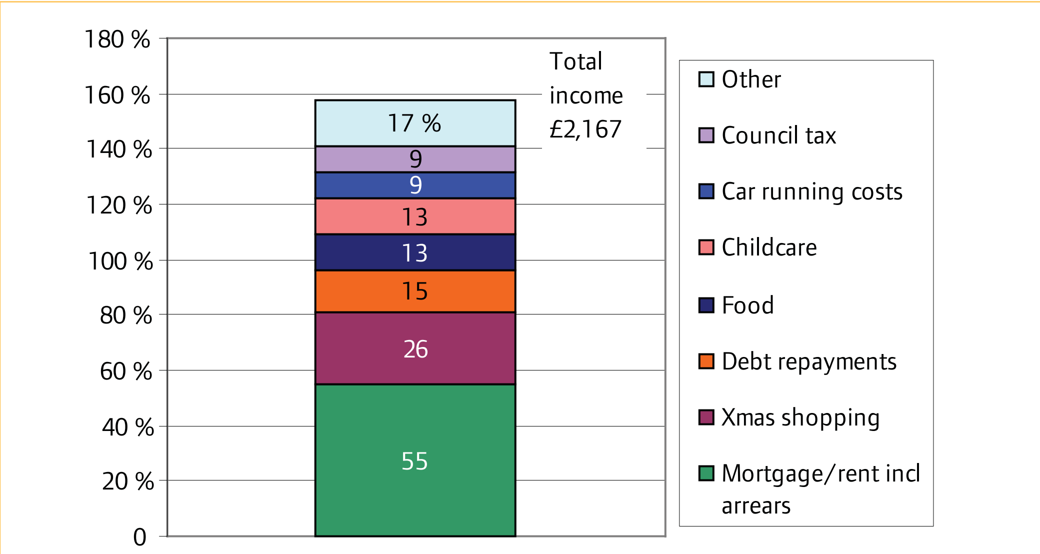
> children's building society, so I take that £5 out and then I get my tithes out which I [give] to the church … whatever is left is mine to spend' (laughs). (Female, 43, Nottingham, one-parent household, three children)

Despite these techniques to manage tight budgets, and coping mechanisms to limit the impact, some families fell behind on payments for bills, rent and debt.

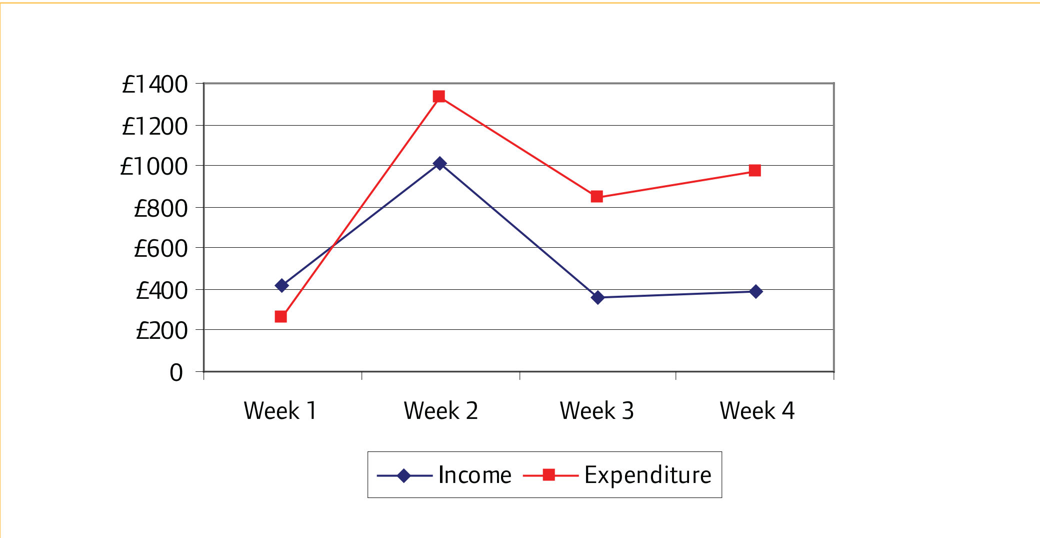
As an example, during the period covered by the diary research, expenditure in one household in Nottingham (by a couple with two children) was 158 per cent of their income (Figure 5). A significant proportion of this was accounted for by Christmas spending, but expenditure continued to exceed income from January, largely due to high housing costs and other long-term debt commitments. Their lack of ability to meet commitments was exacerbated when the main earner's business almost collapsed over January and February. The couple were using credit cards to meet costs but the situation came to a head in February when a graduate loan was called in. The couple sought help from National Debtline, and negotiated a consolidation loan. They were told their access to mainstream credit would be limited for at least six years. Again, their debt repayments were higher than expenditure on food and given that Christmas shopping took almost a quarter of the household budget, their situation was worrying.

Figure 5: Couple, both in work, two children, Nottingham

a) Expenditure as a percentage of income, November–December 2008



b) Expenditure and income, November–December 2008



This example illustrates the vulnerability of many households and the difficulties that many face in prioritising and juggling debts. Having to prioritise with limited cash flow can mean having to move money around, delaying additional payments and interest to pay more pressing ones. Of course, people prioritise in different ways.

> 'I prioritise things, I pay what needs to be paid, and if I can get away with leaving some for a couple of days then that's how I deal with it. I always seem to have to juggle it about, you know, rob Peter to pay Paul… my bills always get paid. I don't have any outstanding apart from your credit card and car and things like that, but you know, I just prioritise what is a must and then deal with the rest as it comes.' (Female, 38, Glasgow, two-parent household, three children)

In addition to often managing tight budgets, low-income families often pay a 'poverty premium' for many essential and non-essential items (Save the Children and Family Welfare Association 2007). It was common to use pre-payment electricity meters, catalogue shopping and door-step lenders – all of which are more expensive compared with other ways of getting the same good or service. While some consumers value the flexibility associated with making regular and small payments (see, for example, Kempson *et al* 2009), many do not have a choice. A number of households in our study told us about having to pay more for essential and non-essential items:

> 'I've had to order it … you have to pay a bit more for it … it's only £200 in the shops, now I am having to pay £300 … it's the only way I can afford to pay for it.' (Female 28, Newcastle, two-parent household, three children)

Saving

The difficulties faced by households living on low incomes – both anticipated and unanticipated – not only impact on how they prioritise spending and their vulnerability to debt, but also on their ability to save. Despite positive attitudes towards wanting to save, there is often simply not enough money to do that.

Data presented by the National Savings and Investments agency[4] shows that the ideal amount that people want to save represents over 15 per cent of total income. However, not surprisingly, there is a shortfall between ideal savings which amount to £210.26 per month on average, and actual savings at £90.12 per month (NS&I 2009). Although the latter marks an increase from £85.34 in autumn 2008, regular savers (currently 47 per cent of all savers) save significantly more than average (ibid). As the recession continues to be felt in the real economy, despite people's aspiration to save, many are less able to.

On the whole, the families we interviewed wanted to save but many simply could not as they were only just living within their means. A large proportion of households spoke about how they were more able to save in the past. Saving often means making a sacrifice somewhere else in the budget. Families spoke about not being able to spend any money on socialising in order to save for specific things like birthdays or Christmas.

> 'That's how else I've noticed that things have got worse because I always had £10-£20 in the bank before when I was really skint which is why mum did not have to send us anything. But now, I have never ever got anything in that savings account, never. I think it's got £1 or something in it. I don't think anything has gone in for months, simply because I cannot afford to leave it there.' (Female, 28, Newcastle, two-parent household, two children)

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4. The NS&I quarterly summary disaggregates data relating to savings and savings aspirations across various demographic indicators. These include location, gender, and age group but not socio-economic group or financial position.

> 'I have never managed to save a penny in my life [but] we live within our means…' (Female, 47, two-parent household, three children)

Despite the lack of saving capacity, some households are better at saving than others. Some participants saved even if it was a very small amount. Many said they try to pass these saving habits onto their children and a significant proportion of children in the sample have savings accounts.

> 'I guess it's a habit … you never know when you might need it so [we save] so we have a little.' (Female, 32, Newcastle, two-parent household, three children)

Very few of the households participating in this research did not save at all and even fewer expressed no desire to save. Saving did not necessarily correlate with levels of income, but the ability to save regularly was interrupted by changes in income.

Throughout the research it became clear that there are different goals and understandings about savings. Households were most inclined to save for a particular item or event. The most common targets people saved towards were Christmas, birthdays, holidays and home improvements. However, two thirds found they could not always save enough to cover the costs. Money saved was often used instead to cover unforeseen expenses, most commonly repairs of household appliances such as washing machines and fridge-freezers.

> 'We just try to save for a holiday, put a little bit extra away each month if we can so we've got something towards a holiday but it doesn't always work out that way.' (Female, 46, two-parent household, Newcastle, two children)

Fewer people were inclined or able to save for a 'rainy day' or an emergency and very few participants spoke about saving for the future. And there was virtually no reference to long-term savings such as for pensions.

Not surprisingly there is some hostility and lack of trust towards banks – particularly as guarantors of savings. Other financial institutions are viewed more positively, such as credit unions[5] (particularly in the case of participants from Glasgow) and local saving schemes. A household in Nottingham was part of a savings club where one neighbour would guard savings for everyone and release the money at Christmas.

Knowing and trusting the people who work in the credit union or run the savings scheme is seen to be important. These characteristics – an organisation being trusted as understanding people's circumstances and it having a local presence – are key in considering the way that financial products should be made accessible to respond to different families' needs.

Borrowing and debt

Throughout the research period, many families had to borrow money and/or were in some kind of debt. Attitudes to borrowing and debt varied. There are mixed views about borrowing from family and friends. Participants who did this preferred the informal nature of it – which included being able to make flexible payments and often with low or no interest. Some of the households in the research described themselves as being excluded from mainstream credit sources and there was general scepticism towards larger banks.

> 'Some days I have no money left and I am like, "what am I going to do?" and that's when I go around and see my dad and he has to help me…' (Female, 24, London, one-parent household, one child)

5. Credit unions are financial cooperatives owned and controlled by their members – see the Association for British Credit Unions Ltd at www.abcul.org/page/about/intro.cfm

Despite a preference for informal borrowing, some of the households did use formal credit. But as discussed earlier, many low-income families may only have access to high-interest credit, which incurs a 'poverty premium'. The Government's Social Fund (see above) was popular among a few participants because there is no interest charged. But many people are unaware of the options available, and the Social Fund can take some time to be administered and processed.

Levels and types of debt varied between families. Some were using formal borrowing as part of their day-to-day budget, others accessed credit to deal with emergencies, while others were completely against having any form of debt, no matter the circumstances.

> 'We've got a loan and I have my card … my store cards are paid off each month.' (Female, 46, two-parent household, Newcastle, two children)

> 'No – we never get into debt, that's one thing that we've always said that we'll never do.' (Female, 21, two-parent household, London, one child)

Conclusion

ippr's consumer spending and debt research is generating new evidence around the dynamics of spending, saving and consumption patterns for low-income families. It comes at a time where increases in energy and food prices have hit low-income families the hardest and the impact of the recession is being felt as unemployment increases. Many households are finding it difficult to plan ahead – particularly given their vulnerability to changes in income and expenditure. And it is clear that many families are facing significant challenges – the consequences of which are not only financial but also on their overall well-being.

The next stage of the research will provide more insight into the daily realities of people's lives and how their spending, saving and consumption are adapting and changing in response to the different economic climate. The focus will be on:

- Gaining a better understanding of why some families are not able to save and the relationship to poverty and other inequalities
- Understanding attitudes towards savings, spending and debt and how families cope with debt
- Analysing how consumption patterns may change in economic recovery and what type of consumer culture may emerge
- Unpacking the differences between the way people save for the short and longer term.

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