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HELPING HOUSEHOLDS IN DEBT

Anna Round, Shreya Nanda, and **Lesley Rankin**

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SUMMARY

Household debt is increasing in the UK. Non-mortgage borrowing, excluding student loans, stood at £87 billion in 2016–18. Well-managed consumer debt can be a useful part of a household budget. But when repayments become difficult or unaffordable, or the sums owed outstrip disposable income, debt becomes a problem with severe impacts for wellbeing and mental health, as well as local economies and community life. In 2016/18, 4 per cent of households had 'problem debt', while 44 per cent of adults with non-property debt felt that this was 'a heavy burden' or 'somewhat of a burden'.

The Covid-19 pandemic has created precisely the kind of shock that turns manageable debt into problem debt, and forces people to enter into debt, or increase their borrowing. **27 per cent** of people entered the pandemic holding consumer debt, and **10 per cent** were behind on their bills. On average, people **anticipated a one in seven chance** of not being able to meet their usual outgoings during the Covid-19 crisis.

In this report we examine how the financial impacts of Covid-19 may affect people in different demographic groups and regions and explore experiences of debt and household finance before and during the pandemic. Across the UK, certain demographic groups are more vulnerable to financial difficulties as a result of the Covid-19 crisis. This includes people who were *already* worse off before Covid-19, showing another way in which the pandemic has deepened existing inequalities. We found that:

- young people aged 16 to 29 were more likely than those in other age groups to have lost their jobs or otherwise left the labour market (11 per cent compared to 5 per cent of all age groups), and therefore to have experienced an 'income shock'
- people from black, Asian and other minority ethnic groups were more likely to report that they had been struggling financially before Covid-19, and were more likely to anticipate further financial difficulties as a result of the pandemic
- people who rent (rather than own) their homes were more likely to anticipate struggling financially during the pandemic, and to be at risk of problem debt
- people on lower incomes, who were more likely to be struggling financially before the crisis, are more likely to anticipate financial difficulty during the pandemic and to have lost their jobs or otherwise left the labour market – making it *more* difficult to turn around their situation.

We also found variations between UK regions in levels of pre-pandemic indebtedness and vulnerability to problem debt. Between 2016 and 2019:

- people in the north east of England were more likely to hold consumer debt
- debt-to-income ratios were highest in Scotland and Northern Ireland, with Yorkshire and the Humber and the North East not far behind
- people in London were more likely than those in other areas to report struggling financially pre-pandemic (housing costs are likely to be a major factor); they are also significantly more likely to live in households that are in arrears with priority bills. This reflects high levels of inequality in London, where high levels of financial insecurity sit alongside high *average* wages.

The likelihood of experiencing problem debt during the pandemic varies between regions. For example:

- people in London and Wales are more likely to expect financial difficulties during the pandemic, with the North East and West Midlands not far behind
- people in the North East and East Midlands are most at risk of problem debt.

The Covid-19 crisis represents a significant shock to incomes, especially for those who have lost their jobs or are likely to, or who could not access government support. Our interviews with debt advisers confirm that Covid-19 has pushed some people who were 'just about managing' on a tight budget to a point where they are 'just not managing'. Without action on household finances, we risk a vicious spiral of debt and job losses, with impacts concentrated on those who are already most vulnerable.

RECOMMENDATIONS

The underlying causes of problem debt are multiple and complex. The evidence suggests that low incomes are a key issue, both before and during the Covid-19 pandemic. Here, our recommendations focus on actions to mitigate the impacts of the pandemic and to help people manage their finances. These should be read in the context of a view that the government needs to support adequate incomes through job protection and creation, and strengthening the social safety net.

Recommendation 1: Government should take urgent action to address the impact of the Covid-19 pandemic on household debt, working with key stakeholders such as the major debt charities to identify effective responses.

Stakeholder organisations, including major debt charities, agree that the government must provide a package of support to mitigate debt issues associated with Covid-19. Their proposals share several common themes, including targeted support for people unable to access government help and for those on very low incomes, action on priority debt and help for renters, and gradual rather than 'cliff edge' cessation of forbearance schemes.

Recommendation 2: Communication about debt and affordability should be clear and accessible, designed to encourage budgeting, proactive engagement with debt support, and better understanding of credit and debt.

We recommend collaboration between multiple stakeholders to improve communication about debt, including development of a defined set of 'plain English' principles, specifically designed for this purpose.

Recommendation 3: The government should increase support for partnership working to address problem debt and encourage engagement with debt advice, through early intervention and collaboration between business, civil society and government departments. Some elements of this should be designed and delivered locally, reflecting emerging issues in local communities and economies (including Covid-19 impacts).

This recommendation relates to *both* the short-term response to Covid-19 *and* a longer-term approach to support early interventions, and includes additional funding for local authorities to establish wide-ranging local partnerships.

Recommendation 4: Technological and social innovation to facilitate wider use of 'open banking' should be supported through investment and collaboration. This should include working with stakeholders to identify ways to engage people who are *not* currently tech enabled or who are digitally excluded.

Used effectively, open banking could support improved financial literacy and facilitate high quality debt advice and early interventions to reduce problem debt. We recommend further work following the principles of 'open banking for good' (Collard and Evans 2019), and urgent action on improving access to these technologies.

Recommendation 5: Improve access to affordable and sustainable credit.

For many households, debt is an unavoidable part of everyday life – and that experience will become more common in the wake of Covid-19. For this reason, we recommend urgent action by government and other stakeholders to widen access to affordable and sustainable credit.

Recommendation 6: Improvements to debt collection practices to support engagement and avoid harms to mental health.

How debt collection is handled can have a marked impact on people's mental health and wellbeing, and affect how they engage with the immediate remedies and longer-term actions to improve their financial wellbeing. We support the recommendations of specialist stakeholders for improved format and content of communications with people facing debt collections action, and recommend that debt enforcement including bailiff action should be enacted only at a late stage in the debt journey; alternatives should be proactively sought at earlier points.

1.
HOUSEHOLD DEBT IN THE UK

Household debt is increasing in the UK. Compared to 10 years ago, more people owe more money through more different kinds of credit, and more of them are identified as 'over indebted'. Problem debt has severe impacts for wellbeing and for physical and mental health, as well as for local economies and community life.

This issue is more urgent in the context of Covid-19. The pandemic has created precisely the kind of shock that turns manageable debt into problem debt, and forces people to enter into debt or increase their borrowing. In this report, we examine how the financial impacts of Covid-19 may affect people in different demographic groups and regions.

Our focus is primarily on problems problem debt such as loans, credit cards, hire purchases, arrears on rent, bills and other payments, and informal lending. We have not included mortgage or student loan debt, except where otherwise noted.

1.1 THE EXTENT OF HOUSEHOLD DEBT IN THE UK

Debt can be a useful part of a household budget (Sparkes and Wood 2020). It helps people respond to economic shocks, improve their standard of living, and invest in goods and services for the long-term (Hood, Joyce and Sturrock 2018). However, debt is problematic when repayments become hard to afford, when it is used to pay for day-to-day costs of living, or when people pay one debt by taking on another.

Household debt in the UK has risen over recent years. Non-mortgage borrowing,[1] excluding student loans, rose from around £80 billion in July 2010/June 2012 to £87 billion in April 2016/June 2018 (ONS 2019a). This increase was driven by increases *both* in the overall sum borrowed, and the number of households with financial[2] debt; the latter rose from 12.4 million to 12.7 million households (ibid). Estimates for the total stock of stock of consumer debt (mostly unsecured) place the figure at over £200 billion[3] (Ahmed and Henehan 2020; Linares-Zegarra and Wilson 2017).

At the aggregate level, the three major sources of consumer credit are formal loans, credit and store cards, and hire purchase accounts. At the individual level, there is a fourth major source: current account overdrafts. Credit and store cards and overdrafts play a greater role at the individual level, suggesting that they are disproportionately consumed by borrowers with lower absolute levels of debt. The reverse is true for formal loans and hire purchase accounts.

1 These figures are derived from the Wealth and Assets Survey. They include the use of credit, store and charge cards, mail order purchases, hire purchase agreements, loans and current account overdrafts.

2 'Financial debt' refers to debts *other than property debt* that are included in the Wealth and Assets survey.

3 Ahmed and Henehan (2020) estimate total consumer debt at £203 billion; Linares-Zegarra and Wilson 2017 give a figure of £239 billion.

TABLE 1.1: CREDIT CARD DEBT IS THE MOST COMMONLY HELD FORM OF CONSUMER DEBT

Consumer debt by category, Great Britain 2016–18

	Share of aggregate consumer debt (%)	Share of individual-level consumer debt (%)
Formal loans	35	16
Credit & store cards	29	45
Hire purchase agreements	27	20
Overdrafts	3	10
Informal loans	3	1
Arrears	2	4
Mail order	1	3

Source: IPPR analysis of ONS (2020a)

In July 2020, the average total unsecured debt per UK adult was £3,947,[4] of which an average of £1,182 is accounted for by credit card debt (Money Charity 2020). Households, however, are not averages, and "the vast majority of debt is held by a small number of households" (Lane 2018). About half of households hold some unsecured debt, but around 70 per cent of that debt is held by just 10 per cent of households (Hood, Joyce and Sturrock 2018). For many, this will be unproblematic. But especially for those on low incomes, debt servicing may be hard to afford, and any 'income shock' may lead to more debt, through extra costs and missed payments.

1.2 WHEN DEBT BECOMES A PROBLEM

For some people, *any* use of debt is a source of shame. The (mis)quotation, "neither a borrower nor a lender be", is still presented as sage financial advice in a world where few people on an average income can buy a home or complete a degree without incurring some debt. Every generation coins new euphemisms for owing money.

As discussed above, well-managed consumer debt that a household can afford to service is *not* problematic in financial terms – although in personal, cultural, or emotional ones it may be. The impact of debt depends on the overall financial position of a household, as well as the ways in which its members take decisions about money and communicate with one another about these (Anderson et al 2016).

Debt creates difficulties when it is unaffordable. Factors in problem debt include:

- spending a high proportion (the Wealth and Assets Survey definition is 'more than 25 per cent') of monthly disposable net income on debt repayments
- falling behind with bills or credit commitments for two or more months
- having household debt that represents a high proportion (Wealth and Assets Survey specifies 20 per cent) of annual disposable net income
- the feeling that debt is a 'heavy burden'.

(ONS 2019a)

Many people who struggle with debt do so only for a short period, following a temporary income loss or unexpected cost. However, around half of indebted households may be in difficulties for a year or more, and for those already in debt

4 Including mortgages, the figure was £60,403 – around 114 per cent of average earnings.

a further income shock or debt increase can be disastrous (Thompson et al 2017). Lower income homeowners may have high levels of unsecured debt and be at risk of losing their homes (Wallace 2016). And debt takes a heavy toll on mental and physical health (MMHPI 2019).

In the period April 2016 to March 2018, 14 per cent of UK adults with financial debt considered this to be 'a heavy burden', and a further 30 per cent felt that their debt constituted 'somewhat of a burden'. 4 per cent of households in the UK were identified as having 'problem debt' (ONS 2019a).

Poorer households are much less likely to have property debt than wealthier ones, but they are more likely to have financial debt and to borrow more as a proportion of their income. In turn, living on a low income makes it difficult to build up a 'cushion' of savings against income shocks (Hardy and Lane 2018).

Of the poorest 10 per cent of households (by income) in the UK:

- around 61 per cent have financial debt, compared to 33 per cent in the highest 10 per cent
- around 35 per cent have debts worth more than the total of their assets
- around 25 per cent of people spend more than a quarter of their income on servicing debts or are in arrears, compared to just 6 per cent in the highest 10 per cent
- around 13 per cent have debt repayments greater than 20 per cent of their household income, compared to 3 per cent of those in the highest 10 per cent.

(ONS 2019a and Hood, Joyce and Sturrock 2018)

People get into problem debt for different reasons. Overspending, inability to resist temptation, and relatively relaxed attitudes to borrowing money are all cited as contributing factors (Frigerio, Ottavani and Vendone 2018; LSE 2015; Edwards 2006), alongside poor money management skills.

However, recent research shows that an increasing number of people simply do not receive enough income to cover the costs of daily life, even when it is lived very frugally. For people on a 'negative budget' (Martin and Lane 2020), simply paying for essentials (such as housing, utilities, and food) is unaffordable, despite careful budgeting. Contributing factors include low incomes and high fixed costs for basic items. Of Citizens Advice clients with negative budgets, 28 per cent are in full time work, and the sums spent are very similar amounts to people with 'positive' budgets. The difference is the proportion of income accounted for by fixed outgoings, which stands at 90 per cent of income compared to 62 per cent (ibid).

1.3 THE IMPACT OF COVID-19 ON HOUSEHOLD DEBT

The long-term impact of Covid-19 on household debt is as yet unknown. The furlough scheme is still in place, protecting many workers and businesses against the worst effects of lockdown on the economy. Some people have saved money while working from home or on furlough, and may have used this to pay debts or build up savings.

But many face a bleak future as unemployment rises and the industries where they have gained skills, knowledge and contacts suffer in a profoundly changed world. People whose situation was already problematic or precarious have been pushed into debt, or deeper into debt. Others who were not in financial difficulty have found themselves needing to borrow or in danger of missing payments. This has grave implications for individuals and families, as well as for the economic recovery ('every pound spent on debt repayments is a pound not spent consuming goods and services') and for creditors, including local government and essential service providers (Citizens Advice 2020c).

IN THE THREE WEEKS FOLLOWING THE MARCH 'LOCKDOWN', OF ALL UK HOUSEHOLDS:

- **one-quarter** had lost all or a substantial part of their earned income as a result of the pandemic (around 7 million households)
- **11 per cent** were in serious financial difficulty
- **almost 20 per cent** were struggling to make ends meet
- **around 16 per cent** had struggled to pay bills such as food or energy, and **22 per cent** reported that they either could not afford some essential items or were very sure they would not be able to during the Covid-19 crisis
- **two-fifths** thought their financial position would worsen during the crisis (Kempson and Poppe 2020; MPS 2020).

By late May 2020:

- an estimated **28 per cent of adults (14 million people)** had experienced a direct negative effect on their income due to Covid-19
- an estimated **4.6 million people** affected had accumulated a total of **£6.1 billion** in arrears and debt, averaging **£1,076** in arrears and **£997** in debt each
- **4.2 million people** had borrowed to make ends meet, using a credit card (1.7 million), an overdraft (1.6 million) or a high cost credit product (980,000)
- other common financial coping strategies included **using savings**, asking **family and friends** for help, applying for **universal credit**, and **selling possessions**
- of those who had fallen behind on essentials, **two-thirds** (67 per cent) had also borrowed to make ends meet (StepChange 2020a).

Citizens Advice estimate 6 million people have fallen behind on a household bill due to Covid-19 (Citizens Advice 2020a). In addition, 3.9 million people have fallen behind on their credit card repayments or overdraft. Mobile phone and broadband bills are the most common areas of arrears, perhaps because they are seen as a relative 'inessential' (3.4 million people are likely to be in arrears). But 2.8 million people are behind on energy bills, the same number on council tax, and 1.2 million people are in rent arrears (ibid). In April–May, one in eight new clients of (StepChange 2020a).

As with so much else, experiences of debt in the crisis will depend on circumstances going into it. Of households who were in serious financial difficulty as a result of Covid-19, 41 per cent had financial problems *before* the crisis; many included low-paid and/or 'precarious' workers in the private sector, with minimal levels of savings (Kempson and Poppe 2020). Bank of England research from July showed that households with incomes below £35,000 per year had on average run down their savings, while households with incomes above £35,000 had on average built them up (Bank of England 2020).

Compared to the 2008, households with low to middle incomes entered the present crisis more likely to be facing problem debt and struggling to pay for essentials. In December 2019, 3.2 million people in the UK were in severe problem debt and 9.8 million were showing signs of financial distress (StepChange 2020a). 2.2 million households were *already* behind on their bills going into the crisis, owing an estimated £3 billion (Citizens Advice/Money Advice Trust/StepChange 2020).

In a cruel irony, people who have been particularly vulnerable to the health effects of the pandemic are more likely to have experienced financial hardship. People who are in arrears with one or more bills include:

- **one in five key workers**, compared to 7 per cent of other workers.
- **one-quarter of carers**, compared to 6 per cent of people without caring responsibilities
- **one in three Black people**, compared to one in eight white people
- **20 per cent** of people who were shielding.

(Citizens Advice 2020b)

Insecure income is also a risk factor; 43 per cent of zero hours contract workers have fallen behind on bills, compared to 9 per cent of other workers, and 30 per cent of people whose working hours have fallen are in arrears (ibid).

The impacts are already stark in human terms. Of people who have fallen behind with bills, 9 per cent have been unable to afford food at some point, and one-third have run down their savings. Of debt clients, 72 per cent had under £100 left for the rest of the month after paying for essentials, and 40 per cent were now in a negative budget (ibid 2020a). There are potentially severe knock-on effects for creditors, not least local authorities which have had to spend extensively to mitigate the effects of Covid-19, and may now face diminished council tax income (ibid 2020b).

2.
DEMOGRAPHIC AND REGIONAL VARIATIONS IN DEBT

2.1 APPROACH

This chapter presents an analysis of data from the Understanding Society survey,[5] exploring experiences of debt and household finance before and during the Covid-19 crisis. We have looked at seven variables to give a picture of individuals' financial situations and debt.

TABLE 2.1: VARIABLES

Variable name	Description	Time period covered
Share with debt	The share of people who hold consumer debt. This includes (but is not limited to) formal and informal loans, hire purchase agreements, mail order purchase agreements, overdrafts, and DWP budgeting loans. It does not include student loan debt or mortgage debt.	**January 2016 to June 2018**
Median debt-to-income ratio among borrowers	Here we compare total debt and gross annual income among borrowers.[6] This variable measures the median ratio of total debt to annual income among borrowers in a given demographic group. In the original survey data, total debt includes student loan debt. Where possible, we have excluded individuals who hold student loan debt, and looked at debt-to-income ratios among the subsection of the population who do not hold student loan debt. However, for some demographic groups, the share of the group with student loan debt was too high to allow us to do this and still obtain a meaningful result.[7] For these demographic variables (age and ethnicity) we have looked at total debt across the population, including those with student loan debt.	**January 2016 to June 2018**
Share reporting struggling financially	Survey participants were asked: "How well would you say you yourself are managing financially these days? Would you say you are: - living comfortably - doing alright - just about getting by - finding it quite difficult - finding it very difficult." This variable measures the share of participants who responded that they were finding it quite or very difficult to manage financially.	**January 2017 to June 2019**

5 'Understanding Society' is a major UK household panel survey. Data for the period pre-Covid-19 is taken from waves 8 and 9, which cover the period January 2016 to June 2019 (University of Essex 2020a). Data for the period during Covid-19 is taken from waves 2 and 3 of the Understanding Society Covid-19 survey, a special survey taken during the pandemic (University of Essex 2020b). These cover the period May to June 2020, and were the latest dataset for the survey available at the time when the research was conducted.

6 'Borrowers' here is used to refer to holders of consumer debt.

7 Where the percentage of comsumer debt holders with student loan debt was above 15 per cent, we have chosen not to exclude individuals holding student loan debt from the sample. On average, 11 per cent of the population hold some student loan debt (IPPR analysis of University of Essex 2020a).

Share in households that are behind on bills	The share of people living in households that report being behind on bills currently, or having been behind on rent, mortgage, or council tax payments in the last twelve months.	**January 2017 to June 2019**
Expected likelihood of experiencing financial difficulty during the pandemic	Survey participants were asked: “On a scale of 0–100% how likely do you think it is that you will have difficulty paying your usual bills and expenses in the next three months?” This variable measures the average response given – ie the average self-reported expectation of experiencing financial difficulty over the three months from May 2020.	**May 2020**
Share at risk of experiencing problem debt	The share of people who both held consumer debt before the crisis, *and* who put their likelihood of experiencing financial difficulty during the crisis at or above 10 per cent. This is used as a proxy for the risk of experiencing problem debt during the crisis.	**May 2020**
Share of the working population who have lost their jobs or otherwise left the labour market during the pandemic	Out of those who *were* employed or self-employed in January–February 2020, this variable measures the share who have now lost their jobs or otherwise left the labour market by June 2020. It does not include those who have been placed on furlough – these employees are still counted as in work for the purposes of this analysis.	**June 2020**

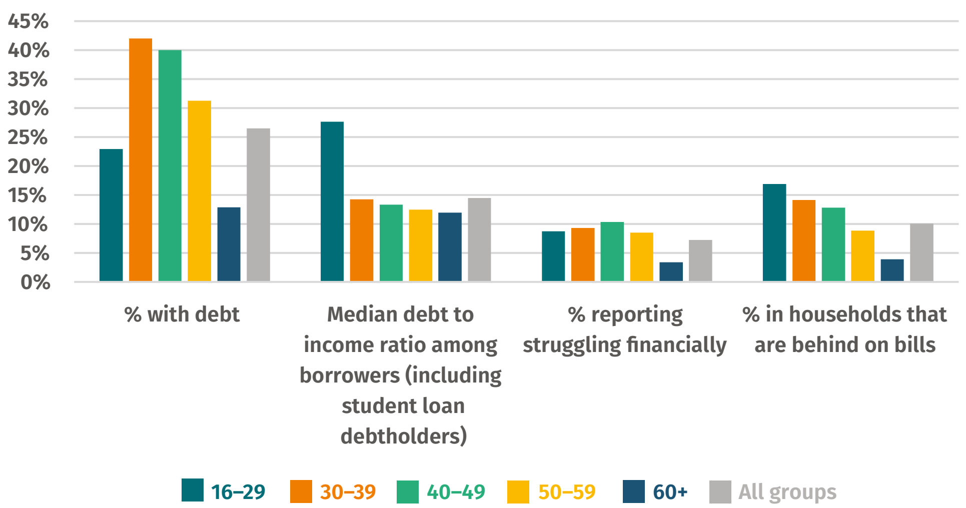
Source: Authors’ analysis

2.2 DEMOGRAPHIC VARIATION

Age

FIGURE 2.1: 30–39-YEAR-OLDS WERE THE AGE GROUP MOST LIKELY TO BE IN DEBT PRE-PANDEMIC

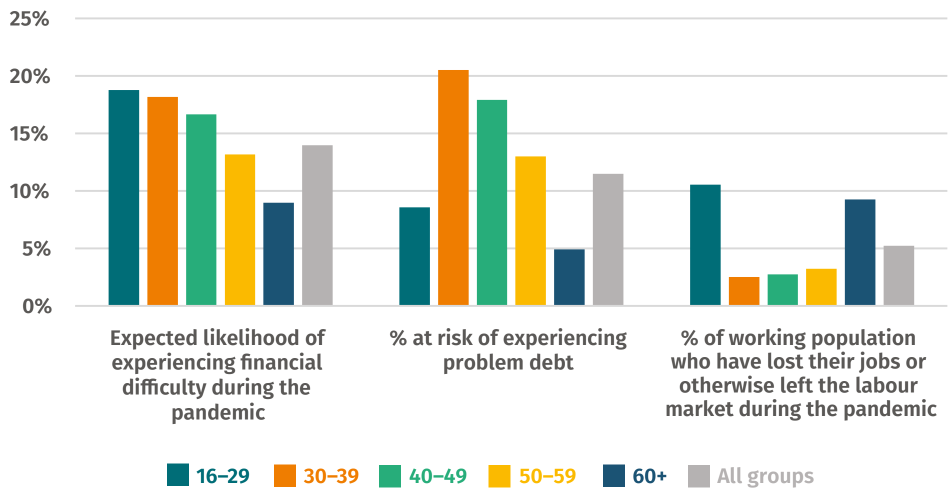
Individual financial situations pre-Covid-19, by age



Source: Authors’ analysis of University of Essex (2020a)

FIGURE 2.2: YOUNGER AGE GROUPS HAVE HIGHER EXPECTATIONS OF EXPERIENCING FINANCIAL DIFFICULTY DURING THE PANDEMIC

Individual financial situations during Covid-19, by age



Source: Authors' analysis of University of Essex (2020a, 2020b)

People aged 16 to 29 have by far the highest debt-to-income ratios. However, this includes student loan debt. For context, an estimated 33 per cent of young borrowers hold some student loan debt, compared to 11 per cent across all age groups (IPPR analysis of University of Essex 2020a). Of the total debt held by borrowers aged 15 to 29,[8] 52 per cent is student loan debt, compared to 20 per cent across all age groups; and for the average young borrower, student loan debt makes up 19 per cent of their total debt, compared to 5 per cent across all age groups (IPPR analysis of ONS 2020a).

People aged 30 to 49 are generally more likely to hold consumer debt; the lower figure for the 16 to 29 age group may reflect weaker access to credit. Younger age groups are more likely to live in households that are behind on bills, and have higher expectations of experiencing financial insecurity during the crisis. This is consistent with the fact that young people tend to earn less than older age groups (with the exception of the 60+ age group) (ONS 2019a), are more likely to live in cities with high living costs, and are more likely to rent (MHCLG 2020a).

16 to 59-year-olds reported similar levels of financial difficulty pre-Covid-19, but levels were marginally highest among 40 to 49-year-olds at 10 per cent – possibly partly driven by caring responsibilities for children and elderly parents, which tend to be concentrated around this age group (ONS 2019b). Relatively high levels of risk, both pre- and post-Covid-19, among the 30-49 age group are concerning because this group are likely to live in households with dependent children – and most were already in the workforce during the 2008 recession.

Young people aged 16 to 29 are most likely to have lost their jobs or otherwise left the labour market during the pandemic. This is in line with analysis suggesting that they tend to have jobs with the highest risk of unemployment due to coronavirus – in particular, 'accommodation and food' and 'arts, entertainment and recreation' (TUC 2020). However, those in the 60+ age group are also more likely than average to have stopped working

8 Including consumer debt and student loan debt and excluding mortgage debt.

during the crisis. This may in part be driven by workers retiring and so leaving the workforce.

Ethnicity

The picture on indebtedness by ethnicity is mixed – black people were slightly more likely to hold consumer debt than the population as a whole, while Asian people were substantially less likely. Black people had the highest debt-to-income ratios, but this includes student loan debt. For context, 21 per cent of black people hold student debt, the highest of any ethnic group (IPPR analysis of University of Essex 2020a). Across all groups, 11 per cent hold student loan debt.

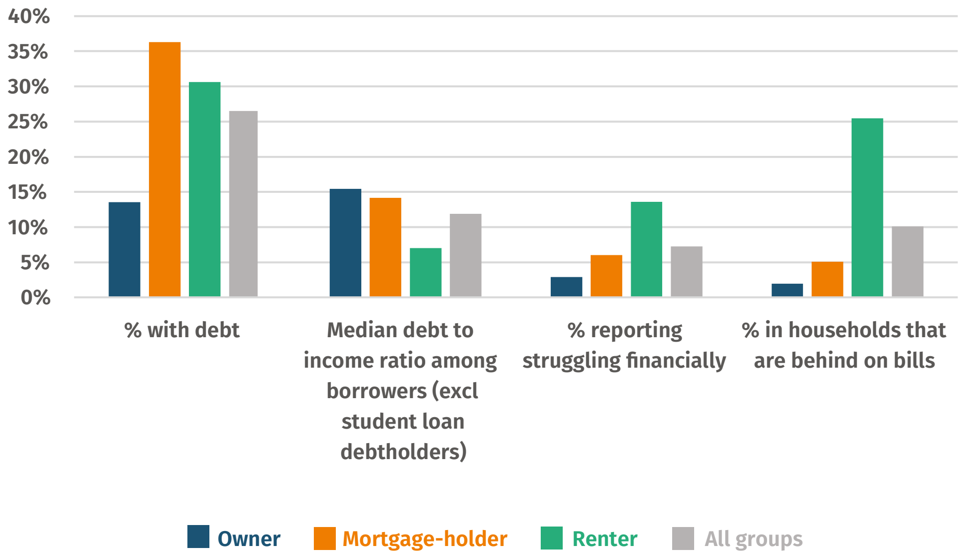
People from black, Asian and other ethnic minority groups were more likely to report struggling financially and being behind on bills before the crisis, and had higher expectations of experiencing financial difficulty during the crisis – with averages of between 27 and 34 per cent, compared to 14 per cent across all groups. This is likely in part driven by the fact that people from ethnic minority groups are more likely to be renters than the population as a whole (ibid).

People from mixed and Asian groups are more likely to have lost their jobs or otherwise left the labour market during the pandemic, while black people are less likely to have done so. The former is consistent with the finding that ethnic minority workers are more likely to be in insecure or temporary work (TUC 2019).

Housing tenure

FIGURE 2.3: RENTERS WERE MOST LIKELY TO BE STRUGGLING FINANCIALLY AND BEHIND ON BILLS PRE-PANDEMIC

Individual financial situations pre-Covid-19, by housing tenure

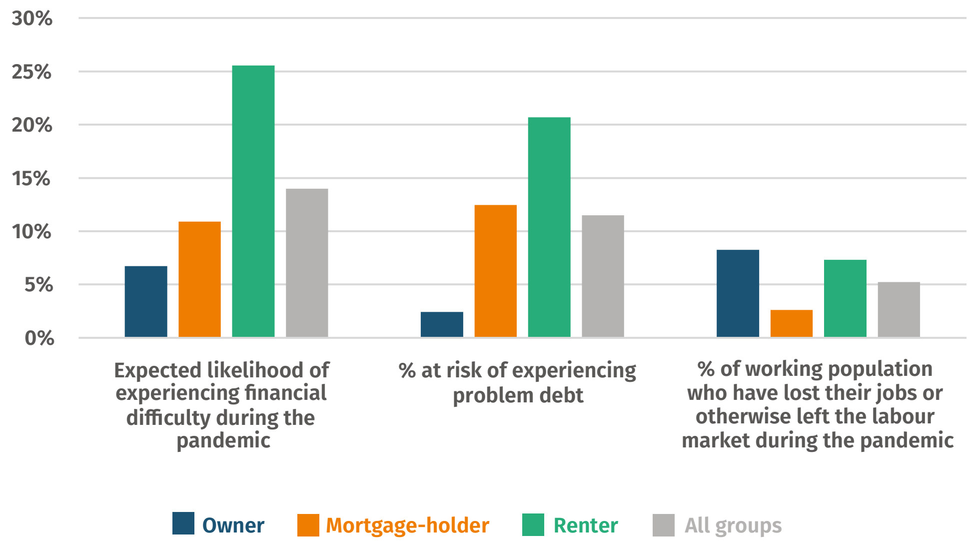


Source: Authors' analysis of University of Essex (2020a)
Note: 'Owner' includes both owner-occupiers and those who live rent-free.

As we might expect, renters and mortgage-holders are more likely to hold debt, more likely to be struggling financially and behind on bills, and more likely to expect financial difficulty and be at risk of problem debt during Covid-19. However, among borrowers, renters have lower levels of debt relative to their incomes – possibly due to weaker access to credit. And, while renters are more likely to have lost their jobs or otherwise left the labour market during Covid, owner-occupiers are too. Again, this may partly be driven by owner occupiers simply retiring and leaving the workforce – 68 per cent of homeowners are in the 60+ age group, compared to 27 per cent of renters and just 10 per cent of mortgage-holders (IPPR analysis of University of Essex 2020a).

FIGURE 2.4: RENTERS ALSO HAVE THE HIGHEST EXPECTATIONS OF EXPERIENCING FINANCIAL DIFFICULTY DURING THE PANDEMIC

Individual financial situations during Covid-19, by housing tenure



Source: Authors' analysis of University of Essex (2020a and 2020b)

Long-term health

Differences between those with a long-term illness or disability and those without were relatively modest, with the exception of financial situation – those with long-term health conditions were twice as likely to report experiencing financial difficulty pre-pandemic. Those with long-term health conditions were also more likely to live in households behind on bills, and had higher expectations of experiencing financial difficulty during the pandemic.[9] However, they were slightly less likely to be indebted, and those working were marginally less likely to have lost their jobs or otherwise left the labour market during the pandemic.

Sex

Although women earn, on average, significantly less than men – £24,000 per year compared to £38,000 (ONS 2019c) – there was little significant difference between men and women for any of the variables analysed. Transfers within households help to make up at least some of this difference. Men were slightly more likely to have a high debt-to-income ratio, while women were slightly more likely to expect to experience financial difficulty during the pandemic.

Income

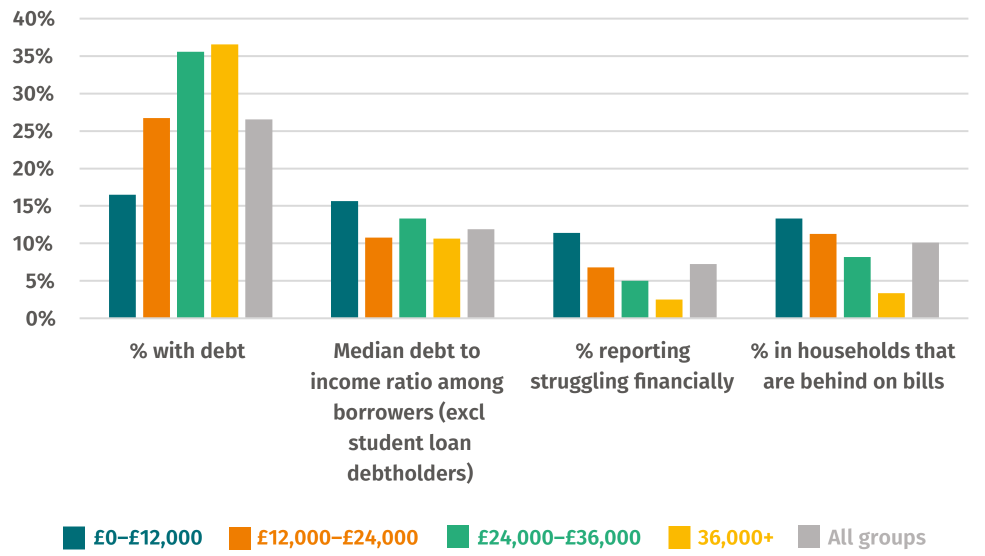
People on higher incomes are more likely to hold consumer debt – potentially because higher incomes make it easier to access credit. However, as we would expect, those on lower incomes were more likely to report struggling financially pre-crisis, to live in households that were behind on bills, to anticipate financial

9 For context, those with long-term health conditions make up an estimated 37 per cent of the UK population (IPPR analysis of University of Essex 2020a).

difficulty during the pandemic, and to have lost their jobs or otherwise left the labour market. The accommodation and food services sector is both one of the lowest paid sectors, and one of the hardest-hit in terms of job losses by coronavirus (Autonomy 2020).

FIGURE 2.5: HIGHER INCOME GROUPS ARE MORE LIKELY TO BE IN DEBT

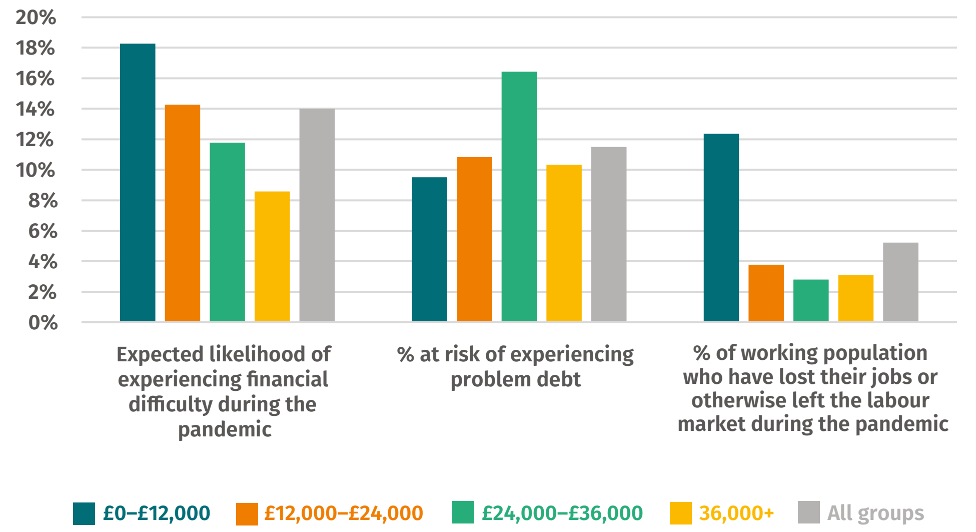
Individual financial situations pre-Covid-19, by income (pre-Covid-19)



Source: Authors' analysis of University of Essex (2020a)

FIGURE 2.6: PEOPLE ON LOW INCOMES ARE FAR MORE LIKELY TO HAVE LOST THEIR JOBS OR OTHERWISE LOST THEIR JOBS OR OTHERWISE LEFT THE LABOUR MARKET DURING THE PANDEMIC

Individual financial situations during Covid-19, by income (pre-Covid-19)



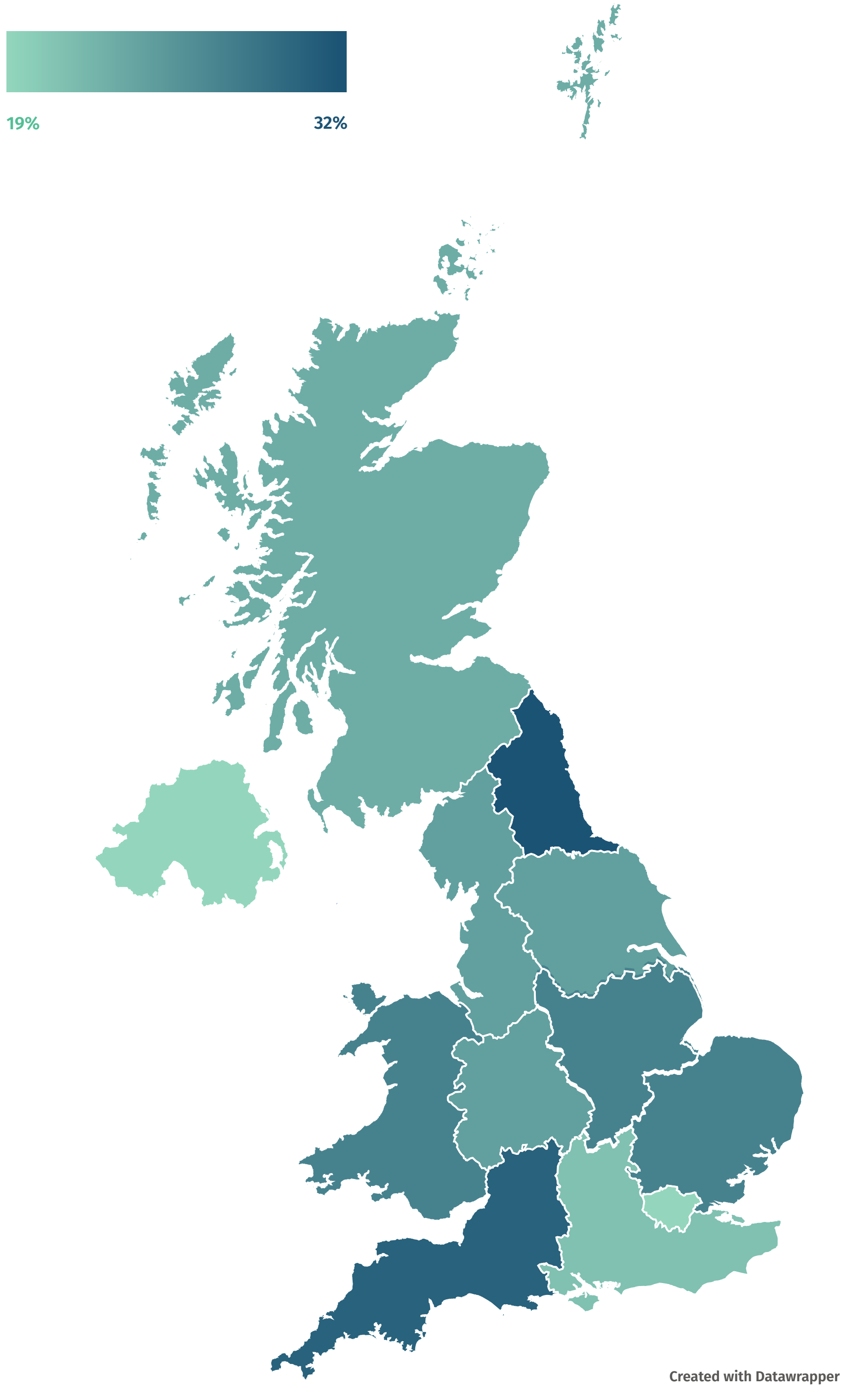
Source: Authors' analysis of University of Essex (2020a and 2020b)

2.3 REGIONAL VARIATION

People in the North East were most likely to hold consumer debt pre-Covid-19; 32 per cent have debt of some kind, compared to 27 per cent across all regions. The North East also had the highest rate of unemployment prior to the crisis (ONS 2020a), and the third-lowest levels of average earnings (ONS 2019c).

FIGURE 2.7: PEOPLE LIVING IN THE NORTH EAST WERE MOST LIKELY TO HOLD CONSUMER DEBT PRE-PANDEMIC

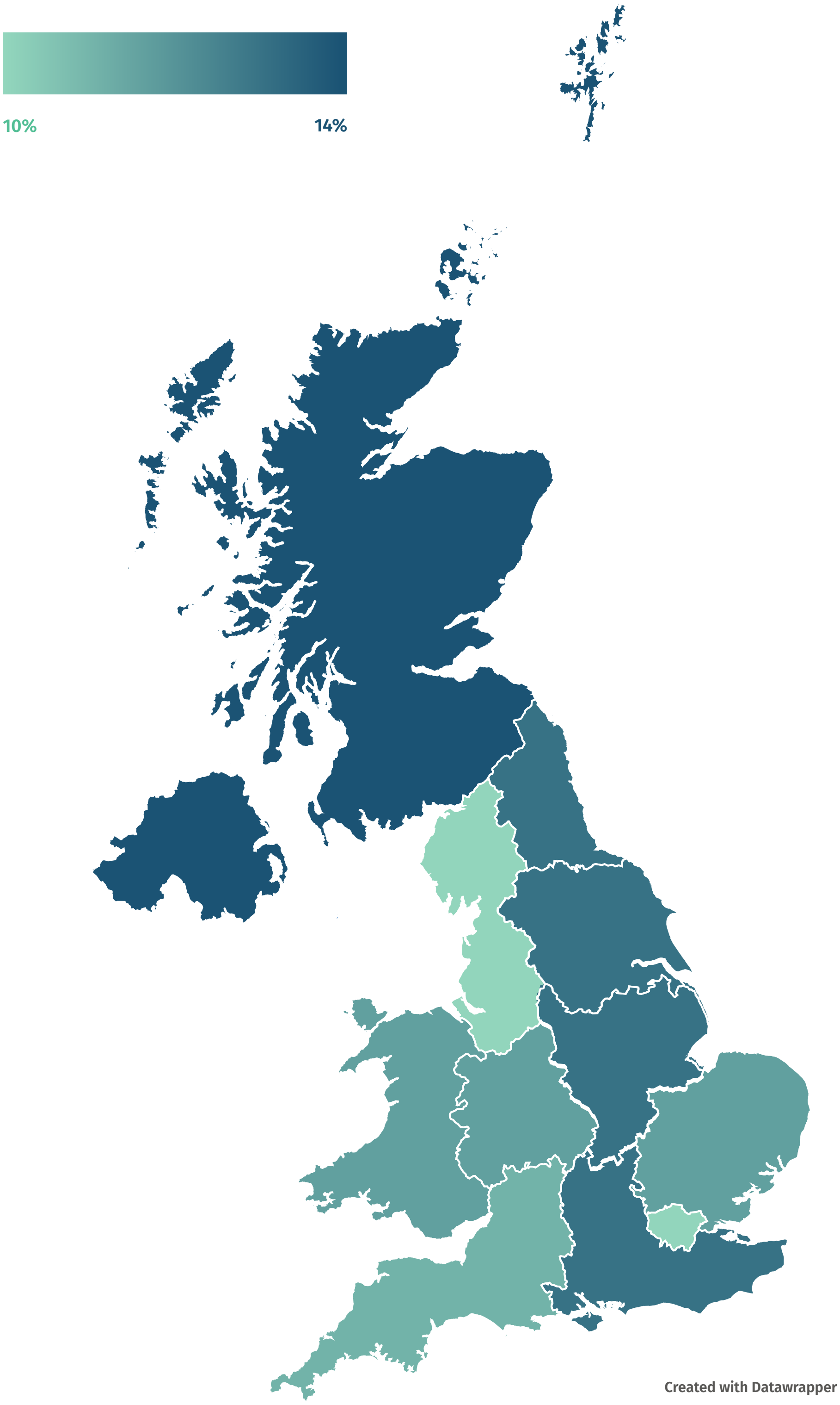
Share of population with debt pre-Covid-19, by region



Source: Authors' analysis of University of Essex (2020a)

FIGURE 2.8: DEBT-TO-INCOME RATIOS AMONG BORROWERS WERE RELATIVELY SIMILAR ACROSS THE COUNTRY PRE-PANDEMIC

Median debt-to-income ratio among borrowers (excluding student loan debtholders) pre-Covid-19, by region

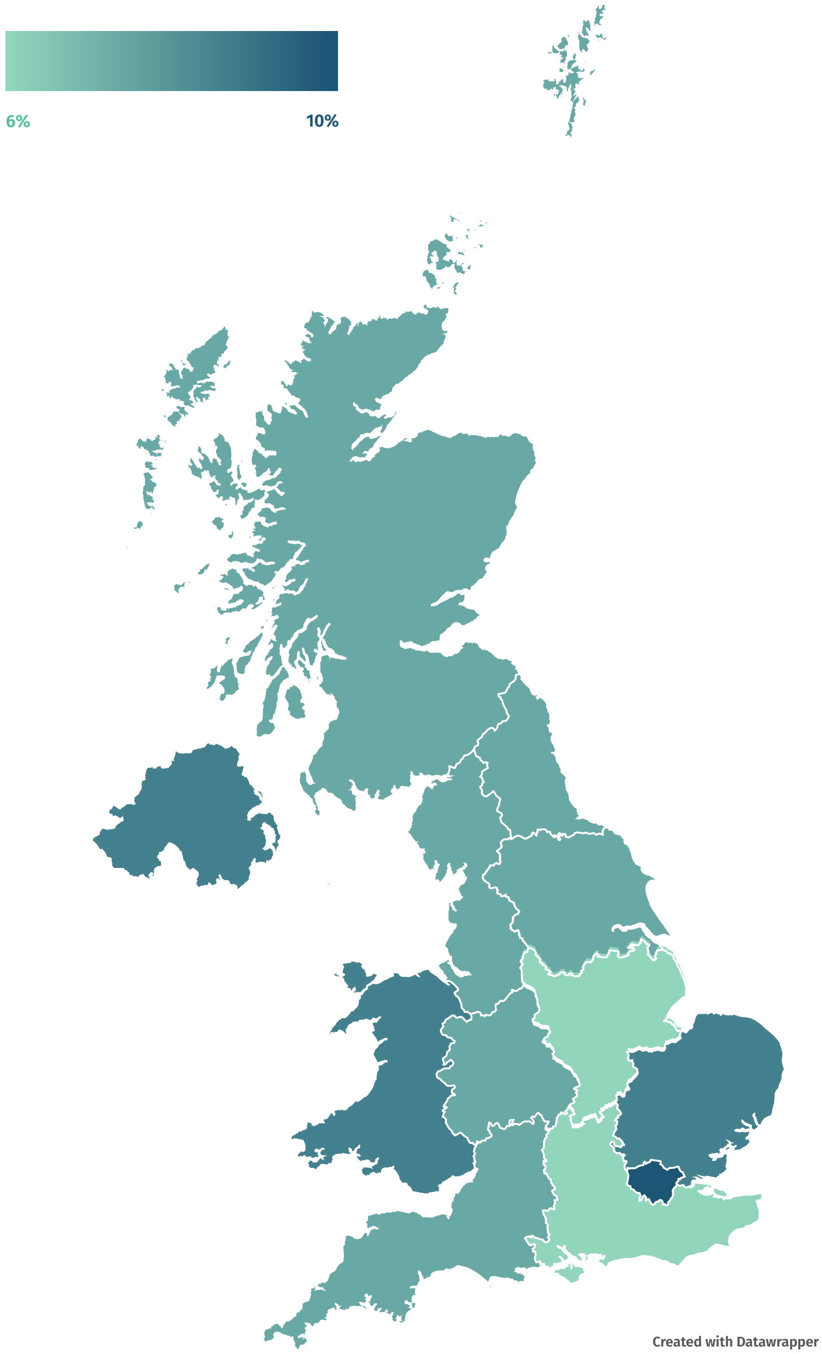


Source: Authors' analysis of University of Essex (2020a)

Median total debt to annual income ratios among borrowers were highest in Scotland and Northern Ireland, though Yorkshire and the North East were close behind. Consumers in Northern Ireland were found by the Financial Conduct Authority to have significantly lower levels of confidence regarding financial matters compared to the rest of the UK (FCA 2018), while Experian found that Glasgow and Edinburgh were both in the top five areas for credit card debt in the UK (Experian 2017).

FIGURE 2.9: PEOPLE IN LONDON WERE MOST LIKELY TO REPORT STRUGGLING FINANCIALLY BEFORE THE PANDEMIC

Share of population reporting struggling financially pre-pandemic, by region

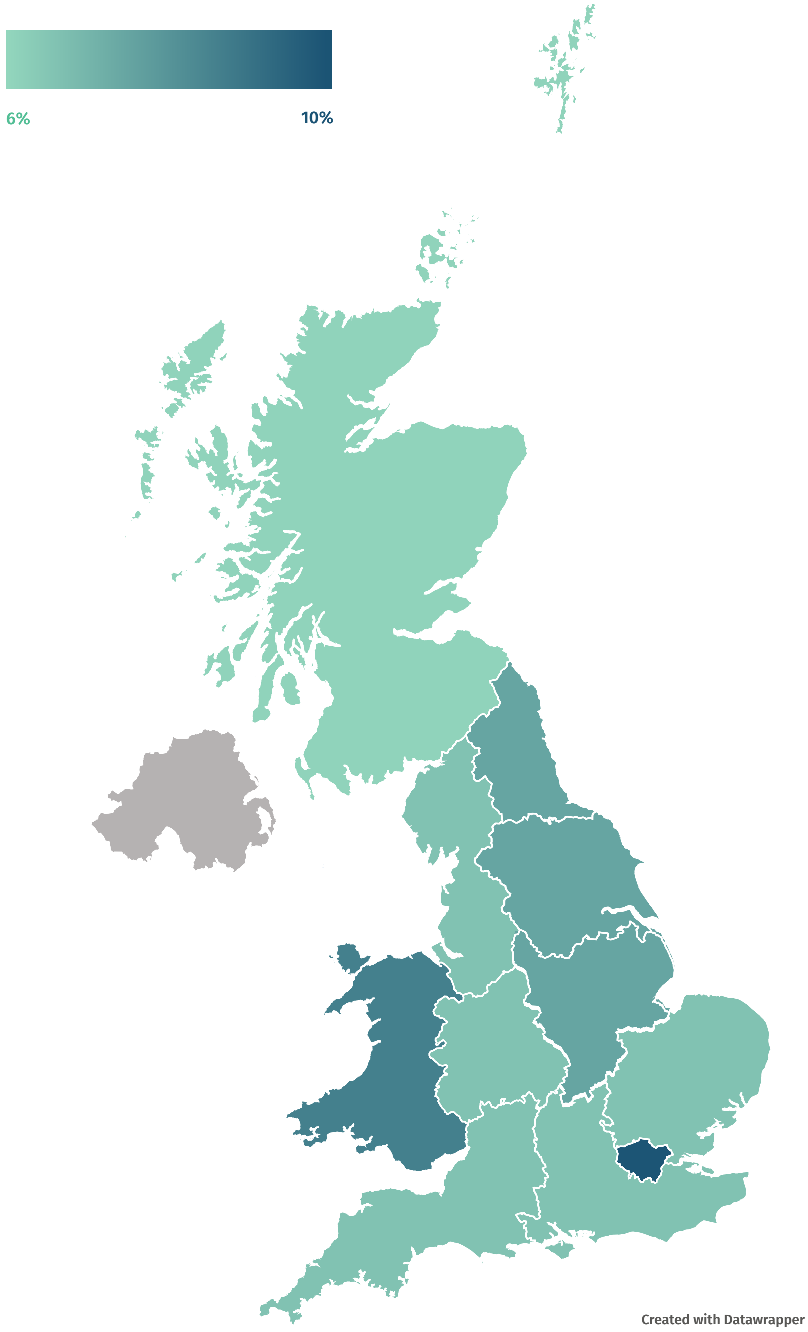


Source: Authors' analysis of University of Essex (2020a)

Despite lower levels of indebtedness, people in London were more likely to report struggling financially before the pandemic – potentially linked to higher housing costs. People in the South East and East Midlands were least likely to report struggling financially.

FIGURE 2.10: PEOPLE IN LONDON WERE ALSO MOST LIKELY TO LIVE IN HOUSEHOLDS BEHIND ON BILLS PRE-PANDEMIC

Share of population in households behind on bills pre-pandemic, by region

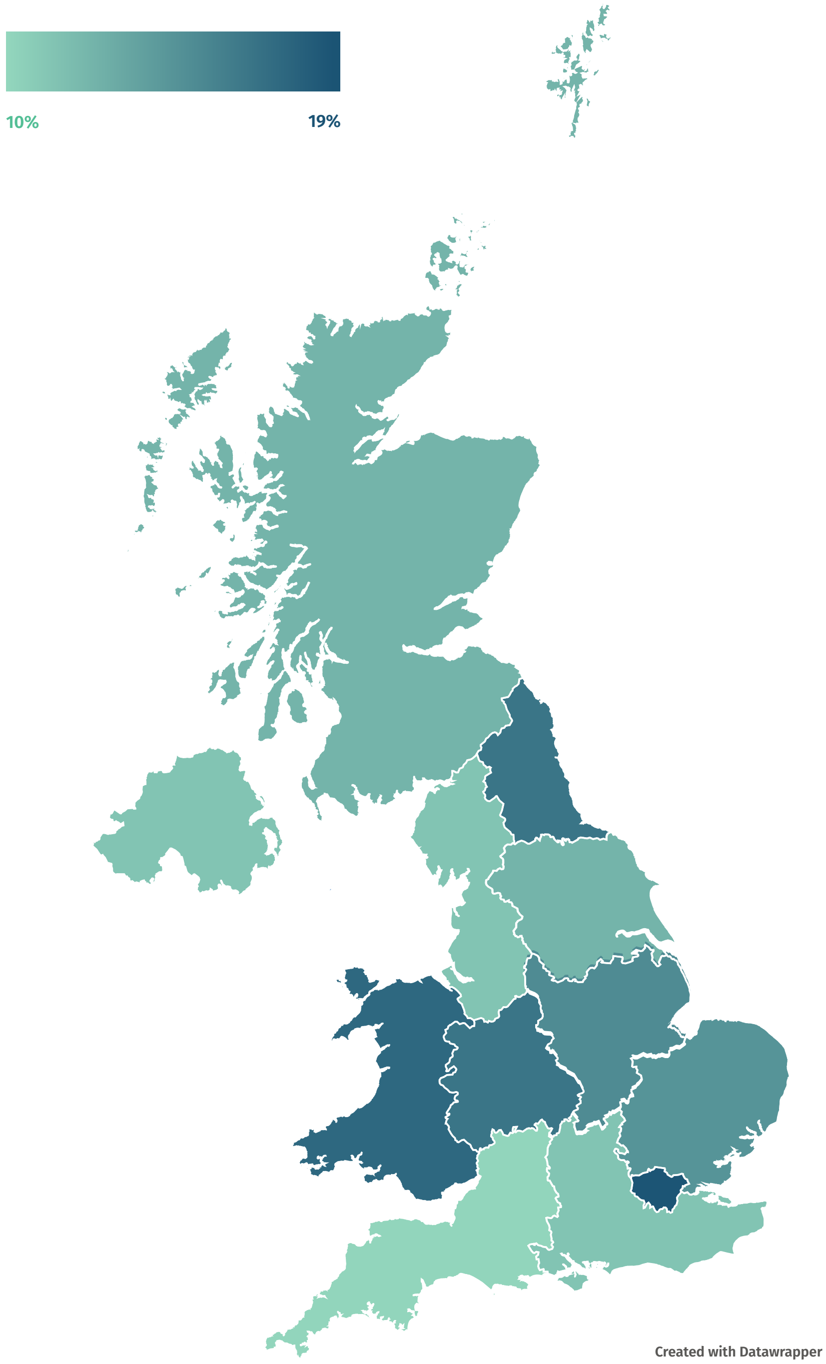


Source: Authors' analysis of University of Essex (2020a)
Note: Data for Northern Ireland is excluded from this figure due to low response rates for the survey questions used to construct this variable.

People in London were significantly more likely to live in households behind on bills, rent, mortgage payments or council tax payments, at 16 per cent, compared to averages of 8 to 11 per cent across other regions. Again, this is likely linked to higher housing costs and a higher proportion of renters. It also reflects high levels of inequality – high levels of financial insecurity exist in the region alongside high average wages.

FIGURE 2.11: PEOPLE IN THE SOUTH WEST HAD THE LOWEST EXPECTATIONS OF EXPERIENCING FINANCIAL DIFFICULTY DURING THE PANDEMIC

Expected likelihood of experiencing financial difficulty during the pandemic, by region



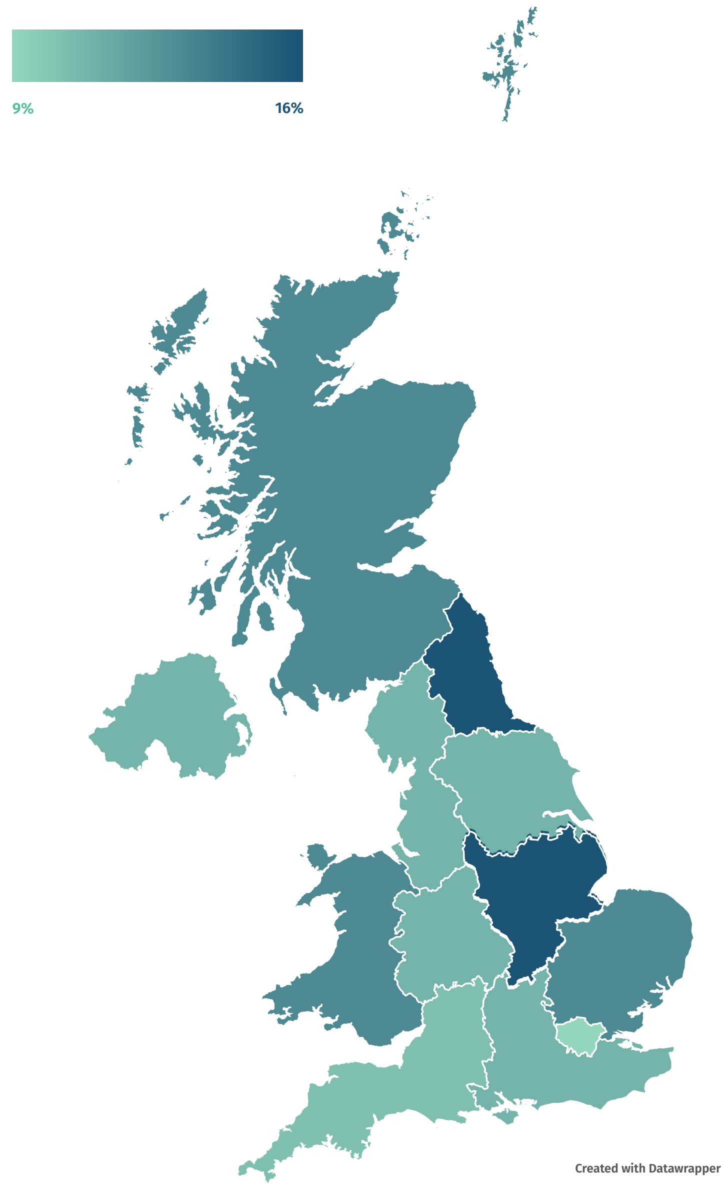
Source: Authors' analysis of University of Essex (2020a, 2020b)

People in the South West put their chances of experiencing financial difficulty during the three months from May 2020 at 10 per cent, compared to 19 per cent in London and 17 per cent in Wales. There are some similarities to the statistics on job losses in figure 2.13 (London and Wales are particularly badly affected), but also some differences (the North West is not). Part of this may be down to the different time periods covered – the data shown here was collected in May 2020, whereas the data in figure 2.13 covers jobs lost by June 2020.

Part of it may also be down to the experiences of those who are still working, but who have been financially hit by the pandemic – for example, those on furlough who have taken a pay cut; workers who have seen their hours cut; or business owners whose profits are down.

FIGURE 2.12: PEOPLE IN THE NORTH EAST AND THE EAST MIDLANDS ARE MOST AT RISK OF EXPERIENCING PROBLEM DEBT

Share of population at risk of experiencing problem debt, by region

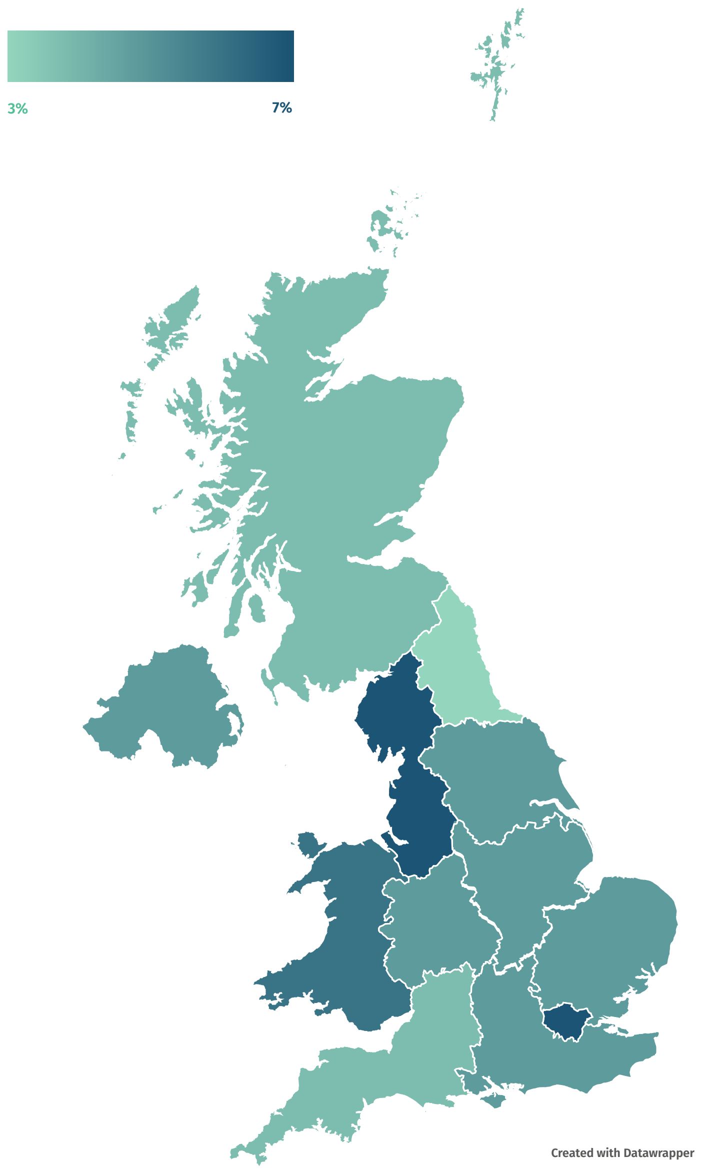


Source: Authors' analysis of University of Essex (2020a and 2020b)

People in the North East and the East Midlands are estimated to be most at risk of experiencing problem debt, while people in London are the least at risk. This variable captures the share of the population who both hold consumer debt, and anticipate a 10 per cent or more chance of experiencing financial difficulty during the pandemic. For the North East and for London, this is not surprising – as in figure 2.7, the North East has the highest levels of consumer debt, while London has the second lowest. The East Midlands does not have an exceptionally high incidence of either consumer debt or expectations of financial difficulty, but does have a disproportionately high percentage of people who fall into both groups.

FIGURE 2.13: WORKING PEOPLE IN THE NORTH EAST ARE LEAST LIKELY TO HAVE LOST THEIR JOBS OR OTHERWISE LOST THEIR JOBS OR OTHERWISE LEFT THE LABOUR MARKET DURING THE PANDEMIC

Share of the working population who have lost their jobs or otherwise left the labour market during the pandemic, by region



Source: Authors' analysis of University of Essex (2020a and 2020b)
Note: 'Lost their jobs or otherwise left the labour market' does not include employees placed on the furlough scheme

An estimated 7 per cent of workers in London and the North West lost their jobs or otherwise left the labour market during the pandemic, compared to just 3 per cent in the North East. As of July 2020, furlough take-up rates were very similar across regions, so this cannot account for these differences (HMRC 2020).

The Centre for Cities found that the largest behaviour changes as a result of the virus were found in large cities, and largest of all in London, with sharp falls in the number of workers travelling into the city centre in March 2020 (Centre for Cities 2020). While working from home has helped to save many jobs, this shift has also had knock-on effects on the businesses that normally serve city-centre workers. This has likely contributed to the higher levels of job losses in London.

Self-employed people are also disproportionately vulnerable to economic shocks, and have received disproportionately little in terms of government support. The Centre for Cities also found that London had high rates of self-employment; while the self-employed in cities in the North West were disproportionately precarious – in other words, reliant on self-employment as their sole source of income (Centre for Cities 2019).

> Across the UK,
> **27% of people**
> entered the pandemic with consumer debt.
> **During the crisis, people expect a**
> **1 in 7 chance**
> of not being able to pay their usual bills.

Meanwhile, the North East has a disproportionately low concentration of jobs in construction and arts, entertainment, and recreation, two of the sectors most affected by Covid-19 (Autonomy 2020).

2.4 SUMMARY

There is striking variation in levels of indebtedness and financial difficulties across age groups, ethnic groups, housing tenures, regions, and income groups. For most of these groups, the relationship between demographics and financial difficulty is fairly straightforward – young people, ethnic minorities, renters, Londoners, and people on low incomes are all more likely to have been struggling financially before and during the crisis. The picture on indebtedness is more mixed, with people on higher incomes, people in their thirties and mortgage-holders the most likely to hold consumer debt; and low levels of variation in debt-to-income ratios across housing tenures, regions, and income groups.

Across the UK, 27 per cent entered the pandemic holding consumer debt; 10 per cent behind on their bills. And on average, during the crisis, people expect a one in seven chance of not being able to pay their usual bills. The Covid-19 crisis represents a significant shock to incomes, as job losses inevitably rise, workers on furlough face reduced incomes, and the economic outlook remains highly uncertain. Without action on household finances, we risk entering a vicious spiral of debt and job losses, with impacts concentrated on those who are already most vulnerable.

3. EXPERIENCES OF PROBLEM DEBT

In this chapter, we discuss findings from interviews with ten experienced advisers at two debt charities, conducted in August and September 2020. All our interviewees had worked in debt advice both before and during the pandemic.

These findings, of course, relate to a subset of a subset of people with debt in the UK. The clients of these debt charities are all experiencing *problem* debt, rather than debt which is manageable, and they are among the group of people with problem debt who have decided to seek help and advice. The observations of debt advisers on their clients' situation reflect the experiences of this group, rather than of the wider UK population. Nevertheless, they almost certainly apply to many people who have problem debt but have not yet engaged with an advice service.

3.1 WHEN AND WHY DO PEOPLE SEEK ADVICE ABOUT THEIR DEBT?

People typically contact debt charities fairly late in their debt journey, after they have missed numerous payments on multiple accounts. Prompts for seeking help include repeatedly receiving letters from creditors; where these include contact details for a debt charity, this can direct a request for help. However some people delay getting in touch until they are threatened with bailiff action, or a county court judgement.

Less common reasons include the sense of being 'overwhelmed' by debt, or a personal crisis with financial ramifications (such as relationship breakdown). People who have managed to hide their debt from friends and family may seek advice when they fear that they will inevitably be 'found out'. More positively, doctors, care workers, or support workers can direct people to debt advice; these 'trusted' referrals can make it easier to engage with clients about their debt.

The majority of clients could benefit from seeking advice at an earlier stage, before the scale and number of their debts has increased to a point that is difficult to manage. Those who wait until they are the subject of a County Court judgement or liability order can no longer benefit from some of the services that charities can offer. Even where this is not the case, delay can cause stress and damage mental and physical health. Inevitably, it also means that people miss more payments and owe more interest.

Clients are often not aware of the benefits of debt advice. Many assume they will be *worse* off as a result, although life is often *more* affordable once a plan is in place. They may believe that because they don't have the money to pay off their debts, an adviser will not be able to help them. Or they may feel that approaching a charity is too intimidating or difficult. An additional problem is that when people use an internet search for debt advice, the first results they encounter may be for 'lead generators' for insolvency services rather than impartial and regulated advice services. As a result, they sometimes reach a debt advice charity having initially received advice which is not fully appropriate for their situation.

3.2 COMMON DRIVERS OF DEBT

Many clients live with the 'negative budgets' discussed above, where income is simply inadequate to cover the costs of even a modest lifestyle (see James 2020). The strain of this situation can be relentless.

Others have just enough regular income to cover their costs, but a short-term fall ('income shock'), or an unexpected cost, can push them into debt. This in turn can escalate if it is not repaid quickly or if the reduction in income drags on. Income shocks include redundancy, reduced working hours (especially for precarious or 'zero hours' workers), health problems and new caring responsibilities. All of these could be exacerbated by the Covid-19 pandemic.

People in this position can face endless complex calculations and 'trade offs'. For example, the decision to go into debt to buy a car that opens up new opportunities for work seems like a wise one – but if the car breaks down or the work dries up, the result can be mounting debt. Christmas, the return to school after the summer, and relationship breakdown can all trigger problems.

All the advisers we spoke to had met some clients for whom impulsive or excessive spending had led to debt, but this was by no means the main, or even the most important, factor. More often, clients "are cutting back as much as they can and they just can't get by". This is in line with the finding of Davies et al (2019) that economic and financial factors (including income) are more important than psychological ones in driving spending behaviours. People who are poor also face higher costs because of a 'poverty premium', when the costs of everyday goods and services are higher for the poorest families than for others (Davies, Finney, and Hartfree 2016).

Where spending on items other than basics had led to debt, this was often associated with social pressures and the need to maintain appearances. Advisers described clients who had carried a large burden of debt that they had built up when they were "young and stupid", or who had felt pressurised to maintain appearances. Spending on children was also a frequent issue.

Advisers noted that particular types of credit may be especially problematic for clients on low incomes.

- Short-term, high-interest loans, including 'payday loans' and home credit ('door to door lending'). These can be obtained quickly, making them an attractive option in response to income shocks. In addition, they may require only limited affordability checks. Several advisers described the marketing of these products as 'friendly', presenting them as meeting a need (which of course, they do) rather than creating a debt. Hire purchase agreements can also be very costly.
- Mobile phone contracts that last for one or more years or more can become unaffordable if people experience an income shock and a previously manageable payment can no longer be met.
- As identified in numerous studies, the practice of taking out more debt to pay off existing debts is almost always an indicator that debt is problematic. For example, people may get into debt using overdrafts or credit cards and then use more expensive credit to service these.
- Debt-related deductions from universal credit were a recurring theme. Advisers described the illogicality of a system that sets a minimum amount on which someone can be expected to live, and then regularly reduces this sum.

3.3 UNDERSTANDING OF DEBT AND 'FINANCIAL LITERACY'

Advisers reflected that many of their clients have a fairly good *general* understanding of their finances, but this may not be sufficiently detailed to facilitate careful budgeting. For example managing multiple payments and variable sums (such as grocery bills or precarious earnings) can be difficult. Very poor understanding (for example, simply not realising that debt must be paid back at some point) was rare although not unknown.

Attitudes to different kinds of debt vary, as can the *emotional* reality of different kinds of debt. For example, when debt servicing is affordable it may not actually *feel* like debt, even if it involves quite a high rate of interest; people may treat it more like a regular bill. Similarly, people can view overdrafts as fundamentally different from a loan – even though they can have high costs in fees and interest.

Many clients do not recognise which debts count as 'priorities', and in particular do not view rent and council tax as priority debts. Rather they tend to view the debt that is 'chased hardest' or seems 'most remote' or 'least friendly' as the most important, and will pay that off first. As a result, commercial creditors often get paid before utility providers, local authorities and even landlords. The credit card company seems a long way off and unlikely to respond to a request for flexibility, while landlords (especially social landlords) and the local council are considered more likely to be sympathetic.

These misunderstandings are made worse because utility providers (and some local authorities) may not 'chase' debts quickly. By the time people recognise the importance of these bills or receive urgent notices, they may be deep in arrears. Similarly, people are often not aware that it *is* possible to negotiate with commercial creditors, for example through an advice service.

Understanding of the finer details of debt processes and credit agreements is often vague among people with problem debt. Many credit products can be obtained easily, and it is possible to enter into a financial agreement without working through its full implications or actual sums that may need to be repaid over time. This is especially problematic when products are obtained online. Many people simply *don't* read the 'small print' of credit agreements ("We live in an age of just clicking the iTunes terms and conditions without looking at them", in the words of one adviser).

3.4 ATTITUDES TO DEBT

Guilt and shame about being in debt remains widespread, and all the advisers we met encountered these emotions in their clients on a regular basis. Some felt that they were more common among older people, but all agreed that they are common across the generations. For many clients, the debt adviser is often the first person to whom they have spoken to about their debt. Some hide their debts from their partner or their children, and as a result may have accumulated *more* debt.

The stigma of debt is a major reason why people delay seeking advice: "Aren't you going to tell me off?" is a question that advisers hear regularly. All described their efforts to reassure clients that there is no need to feel this way, and the profound sense of relief that comes with the realisation that 'they are not alone'. The taboo around talking about money contributes to poor understanding of debt and household finances. After all, where do people have the conversations from which they might learn?

A small number of clients *do* approach advice with the view that their debt is 'unfair', or that they want to avoid paying it altogether. And some hope that their adviser will take full responsibility for organising their repayments, allowing them to continue ignoring the problems. Remarkably few seem to be angry about having ended up in debt. For many, owing money is simply part of life.

3.5 IMPACTS OF COVID-19

The advisers we spoke to had seen a range of approaches to seeking advice about debts associated with Covid-19.

- Clients who were already in problem debt, which has been worsened by Covid-19. Covid-19 was often the 'shock' that prompted this group to get in touch.
- Clients who were in problem debt before Covid-19, but had benefited from the lack of bailiff and collections activity, or from payment deferrals on certain types of debt or (less frequently) mortgages. Towards the end of the summer, these clients were anxious about the need to make up payments or the threat that more aggressive debt recovery was about to resume.
- Clients who were not yet in problem debt (or even any debt) but who wanted to learn how they could avoid difficulties if they lost income due to the pandemic.
- Clients who had initially been able to cope with Covid-19-related debt, but who had begun to struggle.

Some people who were 'just about managing' have been tipped over the edge into debt. Moving to 80 per cent of a low wage itself constitutes an 'income shock', while some lower-income workers have lost their jobs altogether and others have found themselves unable to work because of caring responsibilities. Self-employed people were also more likely to have approached debt advice services for the first time.

Advisers described a *lower* caseload than usual over the summer, as approaches from 'new' client groups were balanced out by fewer enquiries from their regular client base. For example, a pause in enforcement actions, as well as deferred payments ('payment holidays') for certain bills, meant that these prompts for approaching a debt charity were not in place. Payment deferrals have helped many people to avoid problematic debt in the short-term. However, advisers were concerned that some people might find themselves in difficulty, or in greater difficulty, once the delayed instalments fall due. The transition from furlough to benefits when – inevitably – redundancies begin to rise was seen as another danger point for increased financial hardship and unmanageable debt.

A positive development has been the increase in universal credit amounts that was introduced in March 2020. For low-income households who lost earnings as a result of Covid-19, this has been important in allowing people to make ends meet.

As well as difficulties for people who had been in a precarious or problematic situation *before* Covid-19, advisers describe a 'new' group of clients who had lost well-paid jobs as a result of the pandemic. The majority had not previously experienced difficulties with debt, or used debt advice. Some did, in fact, carry a reasonably high level of debt but had been able to repay this regularly because their income matched their outgoings (including debt servicing). "I never missed a payment, and then Covid-19 came along", one had told their adviser. Less positively, some had simply not acknowledged that regular credit card bills counted as debt at all while they could still repay them.

These new clients may find it difficult to cut back on outgoings – especially if they have entered contracts and credit agreements that tie them into regular payments for long periods. They are often using their savings to pay regular bills and expenses, and need to take urgent action to make their position sustainable.

Concern is widespread over what will happen as enforcement action resumes, government furlough and job support schemes begin to wind down, payment deferrals end, redundancies mount up and – for better-off clients – savings run out. The picture will be particularly grim for certain regions and communities, as discussed in chapter 2. The final chapter sets out our short- and long-term recommendations.

4. RECOMMENDATIONS

The underlying causes of problem debt are multiple and complex. The evidence suggests that low incomes are a key issue, both before and during the Covid-19 pandemic. Here, our recommendations focus on actions to mitigate the impacts of the pandemic and to help people manage their finances. These should be read in the context of a view that the government needs to support adequate incomes through job protection and creation, and strengthening the social safety net.

IPPR has elsewhere made multiple recommendations in this vein, including: an increase in the local housing allowance, maintaining the increase in universal credit beyond March 2021, boosting payments to families with children and removing the two child limit for the child element of universal credit, and additional measures for job creation and protection (see Jung and Parkes 2020; McNeil, Jung, and Hochlaf 2020; Parkes, McNeil, and Jung 2020; Quilter-Pinner, Webster, and Parkes 2020; Webb and Murphy 2020).

The recommendations in this chapter address *both* the impacts of Covid-19, and the wider picture on household debt that was in place before the pandemic. In many cases, Covid-19 has simply brought greater urgency to problems that were already evident. However, it has also created and intensified new ones.

❯ Recommendation 1: Government should take urgent action to address the impact of the Covid-19 pandemic on household debt, working with key stakeholders such as the major debt charities to identify effective responses. This should recognise the ways in which Covid-19 has deepened established inequalities, and also new dimensions of vulnerability that have arisen as a result of the pandemic.

Stakeholder organisations, including major debt charities, broadly agree that the government must provide a package of support to mitigate debt issues associated with Covid-19 (see Citizens Advice 2020c, Andrew 2020, Brownfield 2020). Proposals for the form this might take share several common themes, which we in turn endorse in the light of our research. These include the following.

- Targeting of support to people who have experienced income shocks but received only limited or delayed support from income replacement schemes. This might include newly employed or self-employed people and people on short-term PAYE contracts or people in other kinds of precarious work. Targeting could also address the needs of workers in vulnerable sectors, such as hospitality, leisure, and culture. Our qualitative research established that all these groups included people who had been managing their finances successfully but faced hardship since the start of the Covid-19 crisis
- Additional support for people on very low incomes, especially those who have lost income or incurred additional costs due to the pandemic (Citizens Advice 2020d).
- Because of the specific problems associated with priority debts, local authorities should work with partners to manage the impact of council tax arrears and support people who have fallen behind, or are in danger

of falling behind. This could include a 'pre-action protocol' to avoid punitive action and encourage repayment, as proposed by Citizens Advice/StepChange/Money Advice Trust 2020), and flexibility on the requirement to pay arrears within the financial year, which may not be feasible given the continuation of Covid-19 restrictions into the winter. To minimize the impact on wider local government initiatives to support those affected by the pandemic, central government should compensate local government for the loss of council tax income as a result of Covid-19.

- Help for renters, who have not benefitted from a standard system of deferred payments in the same way as mortgage holders (relying instead on the approaches of individual landlords). This might include emergency grants and loans for people who have been required to keep up regular rent repayments. For example, the Scottish Government have put in place a short-term emergency loan scheme that allows landlords with small portfolios to replace rental income lost due to Covid-19. Responses should include sensitivity to local housing markets and integrated with the measures proposed in recommendation 3.
- Grant (rather than loan or deferred payment) support to relieve debt for the hardest hit, for example people who were already on low incomes and who have experienced income and employment shocks during the pandemic. This recognises that Covid-19 has pushed some of the most vulnerable people in society into debt that they will not realistically be able to repay – especially during a severe recession. This support could be capped, effectively sharing the risk between government and creditors.
- The removal of the debt forbearance that has been put in place since March should be gradual, to avoid a 'cliff edge' of financial problems, and the extension of 'breathing space' schemes for people in problem debt that is associated with a specific issue or with short-term income reductions. This could involve protection from charges and enforcement for people who seek debt advice, allowing them time to get their finances in order (Thompson et al 2017). The FCA has issued additional guidance (in draft) on how commercial credit providers should manage payment deferrals associated with Covid-19 as restrictions continue (and in some areas, increase). We support recommendations for additional flexibility and forbearance to avoid undue escalation and enforcement action, and to prevent negative credit reporting, as recommended by debt charities (see, for example, StepChange 2020b).

Recommendation 2: Communication about consumer debt, credit agreements and affordability should be clear and accessible, designed to encourage budgeting, proactive engagement with debt support where this becomes necessary. better understanding of the implications of entering a credit agreement or missing payments.

The nature of communication from creditors is vital in determining whether and how people engage with debt advice and relief processes. Guilt, shame and fear are major barriers to seeking help with debt, as is the stigma associated with owing money. Messages that could reinforce these negative feelings are less likely to be effective than those which take into account the emotional state of debtors (Custers and Stephen 2019). Our interviewees reported that this is an ongoing issue among their clients, as does a lack of understanding about which debts constitute a 'priority' and what help is available with problem debt. Key issues include clear and straightforward messages, encouragement to seek support earlier rather than later with problematic debt, and specific advice about the priority nature of debts such as council tax. Action on these issues will involve collaboration between service providers and experts in debt. For that reason, our recommendations are addressed to multiple stakeholders and our main recommendation is for collaboration.

- Communication about consumer debt should follow a defined set of 'plain English' principles, specifically designed for this purpose. The principles should be developed through a partnership including experts from debt charities and other organisations to ensure that it is accessible and useful to customers. The FCA (building on its work on vulnerability) should collaborate with expert stakeholders to develop and disseminate best practice guidelines.
- This guidance should be tailored to include communications at different stages of the 'debt journey', for example when people start to use credit and at identified 'trigger points' that can signal that debt could become problematic (e.g. using identified patterns of financial behaviours that can signal the onset of 'problem debt', see StepChange 2017).
- Communication about the priority nature of certain payments (e.g. council tax, utility bills) should be proactive. The priority nature of these bills should be stressed when people first start to pay them, and on the payment of subsequent bills (while accounts are in credit).
- The Financial Conduct Authority (FCA) guidance on vulnerability (FCA 2020a) and other intelligence on financial vulnerability (see, for example, CMA 2019) should inform early and proactive interventions with people who are at risk of problem debt. Clear lines of accountability for implementing and embedding these frameworks should be set out and supported through advice, practical toolkits, partnership working etc (Fitch 2020). Financial services and services that have implications for household finance and debt should follow principles for inclusive design in essential services (Money Advice Trust 2020).
- Employers should be encouraged to provide tailored support and guidance on budgeting and debt for people in situations that could bring an income shock, such as redundancy, a reduction in hours or earnings, retirement, or time off work for ill-health.

Recommendation 3: The government should fund partnership working to address problem debt and encourage engagement with debt advice, through early intervention and collaboration between business, civil society, and government departments. Some elements of this should be designed and delivered locally, reflecting emerging issues in local communities and economies (including Covid-19 impacts).

Even before the Covid-19, demand for debt advice substantially outstripped supply (MPS 2019), despite evidence that investment in debt advice can bring substantial long-term savings (Tinelli et al 2019). Access to face-to-face advice services varied between locations and the online offer alone was not appropriate for many people (Collard, Kinloch and Little 2018). We found that experiences of debt vary for different demographic groups, and between local areas. Thus the need for support will also be different, reflecting communities characteristics and local economic conditions. For this reason, we recommend a strengthening of systems to make the most of opportunities for local working and provision tailored to the needs of particular demographic groups. In many parts of the UK examples of good practice are already in place (such as the initiatives supported by Leeds City Council's Financial Inclusion Steering Group and the Nottingham Financial Resilience Partnership). However, additional recognition and funding could help to extend work of this kind within and beyond current provision.

These recommendations relate to *both* the short-term response to Covid-19 *and* a longer-term approach to support early interventions.

- Government should support local authorities to work with stakeholders including debt charities, community groups, civil society and other partners to build local strategies for financial resilience, tailored to reflect local economies, communities, and wider social and economic conditions. This should include initiatives to promote early referrals to advice and support on debt and financial issues by health practitioners, mental health services, benefits advisers, housing providers and others, as well as preventative work to reduce over-indebtedness and improve financial literacy. Current good practice should be fostered and supported through wider funding that recognises the long-term savings and benefits associated with investment in projects of this kind.
- The government should empower the FCA to regulate online advertising by 'lead generators' for insolvency providers, and the Insolvency Service should ensure that the initial debt advice accessed through these advertisements is provided by an FCA-regulated debt advice firm (van Rooyen 2020).

Recommendation 4: Technological and social innovation to facilitate wider use of 'open banking' should be supported through investment and collaboration. This should include working with stakeholders to identify ways to engage people who are *not* currently tech enabled.

Our interviews highlighted the challenges of 'bringing together' all elements of a household budget in one place, in order to facilitate planning or to assess what is affordable. A clear and comprehensive picture of a customer's finances would also help providers of consumer credit to make a realistic assessment of what is affordable – and to be more accountable for the credit they offer.

Technology does not offer a 'silver bullet' but it could provide some solutions. For example, open banking legislation, introduced in 2018, allows consumers to give permission to their bank to share limited amounts of personal financial data with other banks for financial service providers. Coupled with digital innovation, this potentially opens up the opportunity for new applications that can help people to understand the 'full picture' of their finances, including income, outgoing, debt and affordability. Open banking underlies some online and technologically enabled solutions that are already in place, such as Newcastle Building Society's new service for customers who face financial difficulties or could benefit from additional support in understanding their financial position (Credit Connect 2019).

Challenges include the potential exclusion of people with poor levels of digital literacy or digital resources from open banking (Statham, Rankin and Sloan 2020, Stone 2020). Digital exclusion both exacerbates factors that lead to debt, such as poverty and high costs, and makes it harder to manage their impacts. It is estimated that 11.3 million people in the UK lack the basic digital skills that are necessary to thrive in modern Society (Good Things Foundation 2020).

Used effectively, open banking could support improved financial literacy and facilitate high quality debt advice and early interventions to reduce problem debt. Crucially open banking technologies can bring together all aspects of an individual's or a household's finances in one [digital] place, and see the 'big picture' of their income and outgoings. In this way, it can help people who need to 'smooth' irregular earnings from precarious or insecure work, help people to plan their finances or debt repayments, and support financial confidence and capability (Collard and Evans 2019). It also has the potential to improve affordability checks when people take on additional debt, or enter into financial arrangements.

- Following the principles of 'open banking for good' (Collard and Evans 2019), programmes to improve innovative tools for open banking and digital financial health services should be funded and developed. These should build on ongoing good practice, e.g. the work of the Inclusive Economy Partnership, Nesta's OpenUp challenge, and investments in innovative fintech by Fair by Design. Tools should be provided as a 'white labelled solution' for debt advice charities, driven by an organization such as the Money and Pensions Service or the Money Advice Liaison Group.
- A key consideration is potential for open banking to support rigorous affordability checks when people enter into financial agreements or take on debt.
- Access to digital services to improve financial health and wellbeing should be improved through programmes of funding and education.
- Legislation such as the 1974 Consumer Credit Act should be updated to extend the circumstances under which creditors can use digital channels to communicate with clients.

Recommendation 5: Improve access to affordable and sustainable credit.

Like the majority of research into household debt in recent years, we found that debt advice services increasingly see clients for whom debt is an unavoidable part of everyday life. Many live with 'negative budgets', where income does not meet even modest costs of living. And more people will face this situation in the wake of Covid-19; like other studies, our research shows that people who were *already* financially struggling are more vulnerable to the impacts of the pandemic. For this reason, we recommend urgent action by government and other stakeholders to widen access to affordable and sustainable credit. A growing literature (see, for example, CarnegieUK 2016) examines the practicalities of extending the affordable credit offer through diverse channels, and the diversity of need for affordable credit. However, we also recognize that debt is the symptom not the disease for many people who face ongoing financial hardship, and that the issue of 'negative budgets' can ultimately be resolved only through increases in wages and social security payments.

- Access to low-cost credit through credit unions, community finance and other low-cost options should be improved, through partnerships between providers and local authorities, community organisations, employers and social housing, as well as Post Office accounts (Collard and Kempson 2012). This should include government support for capacity building and scale-up funding to make the sector more sustainable and to improve the quality of offers to meet a variety of need (see Fair4All 2020). The government should revisit the issue of support for non-pension savings, concentrating on helping people with very low incomes to build a small 'cushion' (Hardy and Lane 2018).
- Providers should rigorously follow FCA guidance to do more to identify customers who show signs of financial strain or difficulty and implement strategies to reduce repeat use of overdrafts.
- Credit card providers should not offer unsolicited credit increases, and should require affordability checks before credit limits are increased (Citizens Advice 2017).
- High-cost credit options such as the 'home credit' (doorstep lending) market should be subject to further regulation, parallel to that applied to payday loans (see Hardy 2018). This should include rigorous affordability checks and a requirement for detailed information about repayment rates over time.

- The government should increase the availability of social fund grants for people who are unlikely to be in a position to repay any kind of commercial borrowing (StepChange 2018), alongside comprehensive support to build financial resilience following the use of a social fund grant.

Recommendation 6: Improvements to debt collection practices to support engagement and avoid harms to mental health.

Many of our recommendations address the *prevention* of problem debt. But once people are themselves in serious arrears and face the prospect of debt collection and enforcement action, the nature of these processes can have a marked impact on their mental health and wellbeing. It can also affect how they engage with the immediate remedies and longer-term actions to improve their financial wellbeing.

We support the recommendations for improved format and content of communications with people facing debt collections action, so that these are designed to encourage engagement and reduce potential harms, following principles such as those set out in Bond and Holkar (2018). These should be adopted across the sector, including in collections practices for debts to government (local or central) as well as commercial credit.

- We recommend that debt enforcement including bailiff action should be enacted only at a late stage in the debt journey. At earlier stages in the debt journey alternatives to enforcement should be sought proactively, including engagement with debt charities to work out affordable debt solution for clients. Creditors who use bailiffs should be required to set out their plan for this.

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