HELD BACK BY DEBT:

HOW BRITAIN'S LACK OF FINANCIAL RESILIENCE IS TIPPING PEOPLE INTO A DEBT TRAP

People will always face ups and downs that they have to adjust to, but recent trends in the jobs market, with fewer working people in traditional permanent, full-time, steady-wage jobs, mean more people experience more frequent shocks and changes as part of everyday life.

Almost 14 million Britons faced an income shock or a change to their circumstances in the last year. But those working zero hours contracts, fixed term jobs and the self-employed were twice as likely to see a drop or an interruption in their income.

This means that more than ever, people need safety nets to weather shocks and changes. Safety nets are effective options for managing falls and interruptions in income – and include welfare benefits, savings and insurance.

Welfare benefits are being reformed to incentivise work, by mirroring work – a welcome principle. But these reforms need to be balanced to ensure that welfare benefits also act effectively as a responsive safety net to the ups and downs of modern working life, in a world where fewer and fewer people have savings to fall back on.

Savings and welfare benefit gaps mean that in the last year 6.5 million people used credit to keep up with their outgoings after a change in their circumstances.

So many people fall into severe problem debt when they use credit in an emergency, because credit commitments build up as people struggle to pay next month's bills, plus last month's, plus interest.

Once in debt, people face additional barriers to regaining work, are less productive when they are in work, and lose confidence in their ability to progress in their career. Severe problem debt turns everyday obstacles into long term problems, and acts as a major roadblock to key government objectives.

To avoid unnecessary barriers to work and drags on productivity, Government must ensure that people working hard and doing their best in the modern labour market have safety nets that help people cope with everyday ups and downs and avoid falling into the debt trap.

How a lack of financial resilience to shocks and changes can lead people into problem debt

14 MILLION people faced a shock to their income or a change in their circumstances in the last 12 months

People working zero hour and fixed term contracts were **twice as likely** to face an income shock as those with permanent work

5.5 MILLION people could cope without credit or benefits
→ (1%) **55,000** people ended up in severe problem debt

2 MILLION people coped just using benefits
→ (4%) **80,000** people ended up in severe problem debt

2.5 MILLION people coped by using credit and benefits
→ (28%) **700,000** people ended up in severe problem debt

4 MILLION people coped by using credit
→ (20%) **1 MILLION** people ended up in severe problem debt

In total 1.7 million people who kept up with credit fell into severe problem debt

DEBT is a drag on productivity

15% say that their debt worries led to them arriving late for work or taking more time off

43% say that being in debt has led to them being unable to concentrate at work

DEBT holds people back from regaining work

68% say they have tried hard but struggled to get a better paid job

76% worry about taking an insecure job in case it makes their income unreliable

48% of people out of work were worried about higher debt repayments if they took a new job

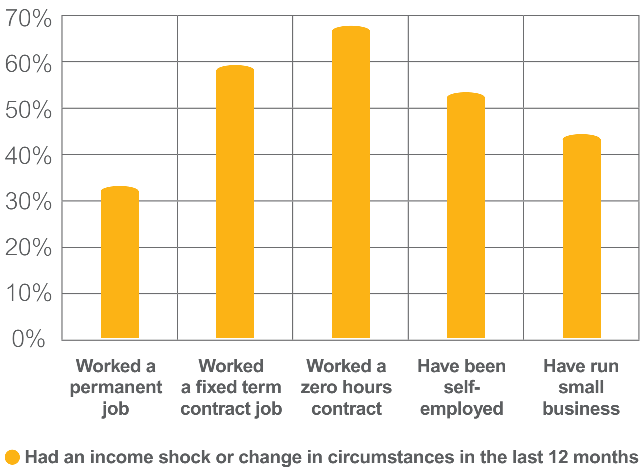
Everyday ups and downs

Despite a recovering economy, millions of people every year have to adjust to significant changes to their circumstances. 28% of all adults in Britain - almost 14 million people - faced at least one income shock or significant change to their circumstances.

- 11% said their income varied from month to month
- 5% experienced a reduction in income / hours at work involuntarily
- 5% had an illness/accident that affected household income
- 4% said they involuntarily lost their job or were made redundant
- 3% of self-employed people and small business owners saw a business downturn
- 2% people experienced a relationship breakdown[1].

No matter how hard they work, people will always face shocks and changes to their circumstances. **But the increase in insecure jobs – with 19% more people working a zero hour contract in 12 months[2] and steady numbers involuntarily in temporary or part time work[3] – means an increased likelihood that people will face shocks more frequently.**

JOB INSECURITY CAN DOUBLE THE RISK OF INCOME SHOCKS AND CHANGES



Source: StepChange Debt Charity commissioned online survey from YouGov PLC. Weighted sample: 4,771 GB adults. Fieldwork: 10th-12th August 2015. Figures based on StepChange Debt Charity analysis of the data.

People who worked zero hour contracts, fixed term contracts, and were self-employed in the last 12 months were around twice as likely as those with permanent jobs to experience an income shock or a change in their circumstances[4].

Everyday ups and downs are tipping millions of people into problem debt.

Nationally, people who face an income shock or change in their circumstances are more than four times as likely to be in severe problem debt in the next 12 months as people who don't[5].

7 in 10 StepChange Debt Charity clients cite a shock to their income or a change in their circumstances as the chief factor that led to them falling into problem debt[6].

How people cope

Millions of people lack the financial resilience to keep up with demands on their finances when they face shocks to their income and changes in their circumstances.

People's financial resilience is determined by the tools they have to weather shocks and changes. Such tools might include savings, spare income, insurance, benefits and tax credits.

In practice, a substantial number of people don't have access to many of the tools above. They lack savings, income and insurance, and do not find their needs met by the benefits system. In these cases, credit can seem like the only option to plug the gap.

In new research, we identified four distinct coping strategies used by almost 14 million people who faced a drop in their income or change in their circumstances in the last 12 months:

- 5.5 million (40%) coped without using credit or benefits
- 4 million (29%) coped by using credit to keep up
- 2.5 million (18%) coped by using benefits and credit to keep up
- 2 million (13%) coped by using benefits to keep up[7].

In total 47% of those who faced a change in their circumstances in the last 12 months – equivalent to 6.5 million people - used credit to keep up with their essential costs.

What factors influence the coping strategies people adopt?

Coping strategy	Characteristics of people adopting the coping strategy
Coping without credit or benefits	• Most likely to be on a higher income (£35,000+) • People who own their homes outright were most likely to adopt this strategy (50% more likely than average) • 22% of do not have a month's savings • 18% said it was hard to adjust their finances quickly to a change in their circumstances • 48% thought that the benefits and tax credits system is too complicated and slow to use
Coping with credit	• Most likely to be on a middle income (£25 - £35,000) • People with mortgages and renting privately were most likely to adopt this strategy (18% more likely than average) • 48% do not have a month's savings • 28% said it was hard to adjust their finances quickly to a change in their circumstances • 56% thought that the benefits and tax credits system is too complicated and slow to use
Coping with credit and benefits	• Most likely to be on a low-middle income (£15 - £25,000) • People in social housing were most likely to adopt this strategy (more than twice as likely than average) • 63% do not have a month's savings • 40% said it was hard to adjust their finances quickly to a change in their circumstances • 63% thought that the benefits and tax credits system is too complicated and slow to use
Coping with benefits	• Most likely to be on a low income (Under £15,000) • People in social housing were most likely to adopt this strategy (77% more likely than average) • 43% do not have a month's savings • 30% said it was hard to adjust their finances quickly to a change in their circumstances • 56% thought that the benefits and tax credits system is too complicated and slow to use

Source: StepChange Debt Charity commissioned online survey from YouGov PLC. Weighted sample: 4,771 GB adults. Fieldwork: 10th-12th August 2015. Figures based on StepChange Debt Charity analysis of the data

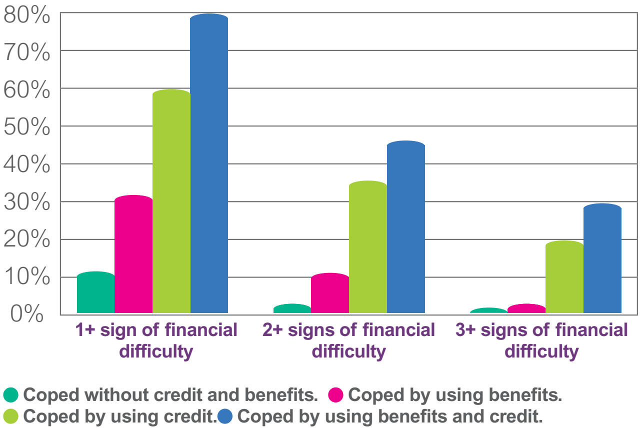
People on the highest incomes were most able to cope with shocks and changes by using their own resources, and a significant number of those on the lowest incomes were able to adjust to income shocks with help from tax credits and benefits.

Those on low and middle incomes were most likely to rely on credit to keep up, were least likely to have savings, and tended to be less confident that the benefits system would help them adjust. They are more likely to be private renters or have a mortgage, and therefore have the highest housing costs. Despite earning more, they are more exposed to shocks and changes.

Why is using credit to cope a problem?

Credit can help people meet their essential costs in the short term, but people who used it are subsequently much more likely to fall into severe financial difficulty than people who just relied on benefits or were able to cope without benefits or credit.

THE IMPACT OF USING CREDIT ON SUBSEQUENT FINANCIAL DIFFICULTY



Source: StepChange Debt Charity commissioned online survey from YouGov PLC Weighted sample: 4,771 GB adults. Fieldwork: 10th-12th August 2015. Figures based on StepChange Debt Charity analysis of the data.

A significant proportion of all people who had faced a shock to their income or a change in their circumstances were showing at least one of six recognised signs of financial difficulty[8]. People who used credit were significantly more likely to be in moderate problem debt (2+ signs of financial difficulty) or severe problem debt (3+ signs of financial difficulty).

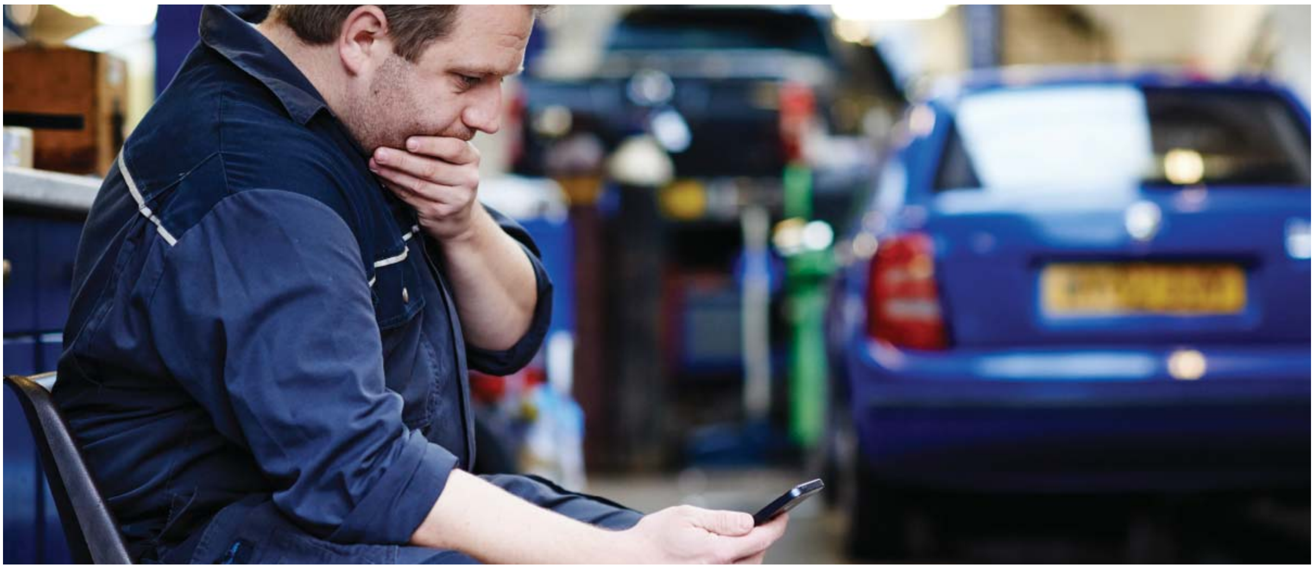
4 million people who solely relied on credit to keep up after a change in circumstances are 20 times as likely to fall into severe problem debt as people who did not use credit or benefits.

2.5 million people who used benefits and credit to keep up after a change of circumstance are 28 times as likely to fall into severe problem debt as people who did not use credit or benefits.

In total 1.7 million people who relied on credit wholly or in part to manage a change in their circumstances in the last 12 months are now in problem debt, compared to 135,000 people who did not use credit to keep up.

Using credit to meet essential costs can be a rational and appealing strategy, especially among those who, like our clients, have a tendency to self-reliance, a determination to seek new or better work, and to avoid dependency. But it can be destructive because life's costs mount up with the costs of borrowing. Essential costs recur each month, and previous month's costs, paid on credit, also need to be met – with interest. In contrast to sustainable, affordable credit used for smoothing larger expenses, using credit for everyday living costs tends to deepen financial difficulties and make debt problems harder to deal with. 97% of the people StepChange Debt Charity helps with severe problem debt say they used credit to keep up with essential costs after falling into financial difficulty[9].

Why is falling into problem debt bad for everyone?



Based on modelling by Baker Tilly, StepChange Debt Charity estimates that the total social cost of problem debt is £8.3 billion[10]. Problem debt costs so much because it impacts people's mental and physical health, and consequently:

People with problem debt may be less productive at work: research shows worries about debt lead to absenteeism and presenteeism – where people continue to attend work, but are less effective due to other concerns - in the workplace:

- 43% say that being in debt has led to them being unable to concentrate at work
- 15% say that their debt worries led to changes in attendance such as arriving late or taking more time off[11].

Debt affects people's work incentives by creating additional barriers to taking up new or better paid jobs. Of our clients:

- 61% feel less confident about getting a promotion at work
- 68% say they have tried hard but struggled to get a better paid job
- 76% say they would worry about taking on an insecure job in case it makes their income unreliable.
- 48% of those who had fallen out of work were worried about unaffordable debt repayments if they took a new job[12].

Problem debt undermines productivity, and blunts the incentives in the welfare benefits system to take work or take more work, and leaves people less well insulated against future shocks. Once in debt people end up further from the labour market with reduced chances of working their way out of financial difficulty.

Removing debt as a barrier to work, security and social mobility

Addressing problem debt means helping people adjust to income shocks and changes to their circumstances. People will always face ups and downs like illness and relationships breaking down. And despite unemployment standing at a record low, people still face losing their job, gaps between contracts and fluctuating hours – particularly the growing number of people in insecure work.

People with different incomes and costs need a range of safety nets to help them adjust and bounce back from difficulty.

People on higher incomes are more likely to cope with savings, and those on the lowest incomes with lower costs are more likely to be insulated from shocks by the welfare benefits system. But those working hard on low and middle incomes are most likely to resort to credit to keep up in emergencies when they face gaps in the safety nets at their disposal:

- They lack rainy day savings to cope with income shocks.
- They have limited ways of controlling their costs quickly.
- They have little confidence in the responsiveness of the welfare benefits system to their circumstances.
- They find that they are not eligible for enough support to help them meet their costs.

The economy, taxpayers and individuals benefit when people can weather life's ups and downs without falling into longer term financial difficulty. We want to see people be self-reliant and prosper through work. That's what our clients want too.

Policy does not focus enough on ensuring working families have the safety nets they need to avoid falling into longer term difficulty after facing a shock to their income or circumstances.

Preventing longer term difficulty has only been an objective of recent and current welfare reforms insofar as reforms have sought to incentivise people to get back to work. This approach has not given enough priority to preventing people who were in work – especially insecure work – from falling into longer term difficulty when they face the inevitable ups and downs in their income.

An effective plan to boost families' resilience and self-reliance must have preventing people facing income shocks from falling into longer term financial difficulty as a key objective. An effective plan must address the following questions:

- **How to balance the role of welfare benefits as a preventative safety net against longer-term difficulty, with the need to remove barriers to work:**
  - **Considering the potential costs of longer term financial difficulty against the potential savings made by freezes and cuts to benefits in current and future welfare reforms.**
  - **Ensuring that all benefits and tax credits respond quickly to the dynamics of the modern, flexible – but less secure – job market.**
- **How to plug the gap between the welfare benefits that people are eligible for and their essential costs in the transitionary periods immediately after people have faced a change to their circumstances.**
- **How to boost people's self-reliance through an effective savings policy to ensure every low and middle income family has a rainy day savings pot.**
- **How to help people stop their commitments spiralling through a legal protection to pause interest, charges, enforcement action and unaffordable collections when people seek help with their debts.**
- **How the beneficiaries of more resilient, productive workers – government, employers and individuals - share responsibility for efforts to deliver an effective system of safety nets.**

1 StepChange Debt Charity commissioned an online survey from YouGov PLC. Total sample size is 4,771. Fieldwork was undertaken 10th-12th August 2015. The figures have been weighted and are representative of all GB adults (aged 18+). Estimates of the number of adults affected have been calculated by StepChange Debt Charity. These estimates are based on 2013 population estimates from the Office of National Statistics which indicate that there are 49,478,070 adults in Great Britain.

2 Office for National Statistics, 2015. Contracts with No Guaranteed Hours, Zero Hour Contracts, 2014.

3 Resolution Foundation, 2015. A steady job?

4 StepChange Debt Charity commissioned online survey from YouGov PLC. Weighted sample: 4,771 GB adults. Fieldwork: 10th-12th August 2015. Figures based on StepChange Debt Charity analysis of the data.

5 Ibid. Figures based on StepChange Debt Charity analysis of the data.

6 StepChange Debt Charity, 2015. Telephone helpline statistics Q1/2 2015. Sample: 87,956 people.

7 StepChange Debt Charity commissioned online survey from YouGov PLC. Weighted sample: 4,771 GB adults. Fieldwork: 10th-12th August 2015. Figures based on StepChange Debt Charity analysis of the data.

8 The signs of financial difficulty are: making just the minimum repayments on their debts for three or more months; using credit to make it through to payday; getting hit by late payment or overdraft charges on a regular basis; falling behind on essential household bills; using credit to pay essential household bills; using credit to keep up with existing credit commitments. These relate to indicators of financial difficulty devised by the University of Bristol's Personal Finance Centre.

9 StepChange Debt Charity client survey. Sample: 1,300 StepChange Debt Charity clients who sought advice in Q1/2 2015. Fieldwork conducted 15th July – 11th August 2015.

10 StepChange Debt Charity, 2014. Cutting the cost of problem debt.

11 StepChange Debt Charity client poll, 2014 (A). Fieldwork conducted 23 June – 14 July 2014. Sample: 923 StepChange Debt Charity clients who came for advice in 2013.

12 StepChange Debt Charity client survey. Sample: 1,300 StepChange Debt Charity clients who sought advice in Q1/2 2015. Fieldwork conducted 15th July – 11th August 2015.

StepChange Debt Charity London Office
6th floor, Lynton House
7-12 Tavistock Square
London WC1H 9LT

Email: policy@stepchange.org
Web: www.stepchange.org
Twitter: @stepchange

For help and advice with problem debts call
0800 138 1111 Monday to Friday 8am to 8pm
and Saturday 9am to 4pm

Registered office: Wade House, Merrion Centre, Leeds LS2 8NG
Registered in England No 2757055
Registered Charity No 1016630
Registered in Scotland No 162719
Scottish Charity No SC024413

StepChange Debt Charity