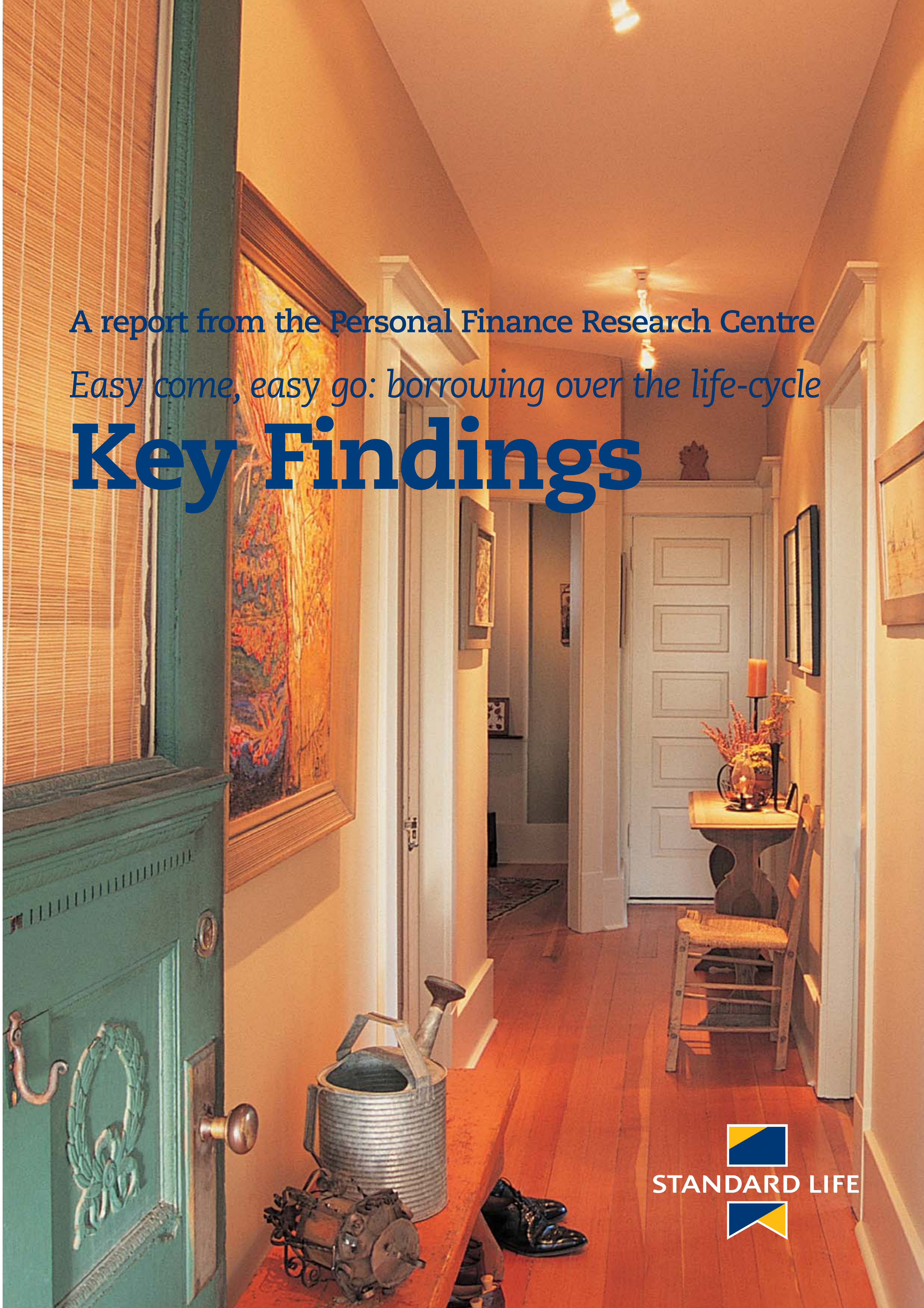

A report from the Personal Finance Research Centre

Easy come, easy go: borrowing over the life-cycle

Key Findings

STANDARD LIFE

A marked increase in wealth in recent years has been matched by a similarly marked increase in borrowing in the UK. With total outstanding consumer borrowing now exceeding £1.35 trillion the UK is seeing the highest levels of unsecured credit supplementing the highest ever levels of mortgage borrowing. This research project was undertaken to understand better why people borrow, and how borrowing may be mitigated and even avoided at different life-stages. It shows that:

- The amounts owed by credit-users have increased in recent years, although heavy credit use remains concentrated among a tiny minority.
- Borrowing was most common among people aged between 20 and 50, starting when people are young and continuing in the family years when demands on the family budget are high.
- There was a clear connection between consumption and borrowing and credit use often reflected the rising expectations of standards of living and wealth.
- The perceived ready availability and cheapness of borrowing made it attractive. Among credit users there was little desire or perceived need to seek alternatives to using credit. Some felt they couldn't save quickly enough to keep up with rising prices, despite the low inflation of recent years.
- Young adults seemed especially susceptible to strong pressures to consume, and were prepared to borrow to do so. The use of credit to meet everyday expenditure was a way of life. For some the line between needs and wants was virtually indistinguishable.
- Some parents felt pressured to borrow to provide for all their children's needs and wants.
- Housing equity was seen as the solution to all future financial needs, especially among those in or approaching the family years. A belief that property is the best investment was compounded by a belief that mortgage borrowing is itself a form of investment, having been quite cheap recently.
- The increase in demands on finances for large expenses such as home ownership and higher education, which were seen as legitimate and inevitable, was central to a shift in norms among younger generations. However, some people were borrowing far more than strictly required for these purposes.
- A disconnect between the perceptions and reality of 'debt solutions' was apparent among some young adults. A core minority were circumscribing personal responsibility for their credit use and saw debt consolidation and insolvency as easy ways out of 'problem debt'.

The research concludes that policy responses need to focus on providing a counterbalance to the 'want it now' consumer culture, promoting financial capability through a coordinated approach. This needs to centre on the positive message of 'making money work for you', which should be delivered consistently and repeatedly.

About this study

This study was undertaken by Andrea Finney, Sharon Collard, and Elaine Kempson of the Personal Finance Research Centre (University of Bristol). The research involved primary analysis of eight focus groups of people at three life-stages – young adults, people in the family years, and people in their post-family years – and was supported by a review of the existing literature, secondary analysis of national survey data and a workshop with experts in the field.

The extent and nature of borrowing in the UK

About three-quarters of the population have some form of credit facility, although only a half are active credit users. Although this proportion has remained relatively stable in recent years, the amounts owed by credit-users have increased; there has also been a shift away from the use of credit tied to a particular purchase in favour of sources, like credit cards, that can be used more widely.

Heavy credit use is concentrated among a tiny minority of the population. Credit use can be a direct cause of financial difficulties both following a drop in income, and in the absence of an earned income.

Who borrows

Borrowing was most common among people aged between 20 and 50, when demands on the family budget are greatest. Compared with others, unsecured borrowing was more common among people with a mortgage, even when all their other circumstances were the same.

A change in income – particularly following job loss – was related to credit use and had a stronger effect than income itself.

Credit use was common among people with modest levels of savings – of between £3,000 and £5,000 – even once the influence of other factors such as income was taken into account. Far from being irrational, borrowing serves to protect the "safety net" that modest savings provide.

Attitudes towards spending, saving and borrowing were important for explaining who was likely to be a credit user, and especially a heavy credit user. People were much more likely to be credit users if they were impulsive, preferred to use credit rather than to save, or lived for the day.

Reasons why people borrow

The essential function of borrowing is to smooth the ebbs and flows of income and expenditure throughout life. Previous research has distinguished borrowing to alleviate financial hardship and borrowing to augment a consumer lifestyle.

In the current strong economic climate there was little evidence of borrowing purely to relieve financial difficulties. However, for many heavy credit users, discretionary borrowing was contributing to a need to borrow in order to get by.

The current research provides new evidence that the distinction between consumers' needs and wants is not clear cut. Among young adults in particular there was clear evidence of routine borrowing for everyday spending for discretionary purposes, although it may not have been perceived as such. For them, borrowing for wants and needs were virtually indistinguishable.

Pre-requisite borrowing to buy a home or to fund further or higher education was seen as a legitimate form of financial investment. However, some people were borrowing far more than they strictly needed for these purposes.

Drivers of borrowing

In the context of a highly competitive credit market, it is perhaps not surprising that factors associated with the supply of credit – such as the perceived ready availability and cheapness of borrowing – made borrowing attractive.

Among a small core of young adults, the availability and benefits of debt solutions – such as debt consolidation, Individual Voluntary Arrangements and bankruptcy – outweighed the drawbacks of over-borrowing, even to the extent that they made borrowing beyond one's means all the more desirable.

Across the life-stages, borrowing behaviour often reflected the rising expectations of living standards and wealth born out of increased prosperity in the UK in recent years, as well as the social pressures of a 'want it now' society.

Among young adults in particular, credit use was a way of life and seen as socially acceptable. The increase in demands on finances for large and legitimate expenses, such as home ownership and higher education, were central to a shift in norms for young adults and people in the family years compared to older generations.

There was both a sense of inevitability around borrowing large sums to support higher education and home ownership and that borrowing for these purposes was a form of investment. In particular, a belief that property is the best investment was compounded by a belief that mortgage borrowing is itself a form of investment, having been relatively cheap in recent years.

Among young adults, the perception of credit as 'money' predominated. Higher education students tended to see credit as seen as a legitimate form of income; that they had a 'right' to this money as their own. Among a minority of other young adults, a perception that credit was someone else's responsibility seemed to underlie a feeling that it could be spent frivolously.

Mitigating borrowing

Against a backdrop of widely available credit and a pervasive consumer culture, there was clearly little desire or perceived need among borrowers to cut back on spending or go without, nor was there a motivation to reduce levels of borrowing. There was also a sense of impatience: people did not want to wait and save up. It was, however, accepted that avoiding credit use would be difficult among lower-income families.

Some people – younger and older people alike – felt it was impossible to save quickly enough to keep up with rising prices. This seemed counter-intuitive given low inflation in the UK at the time of the study, but related specifically to new technologies. There was a feeling that by the time you had saved up for something, there would be a newer, higher specification, more expensive version on the market.

Across all life-stages, problem debt was seen predominantly as arising through irresponsible spending and borrowing behaviour by the individual, although concerns about irresponsible lending were also expressed in some groups.

People in the family and post-family years tended to identify internal definitions and warning signs of problem debt, such as worry about money and losing track of spending; young adults referred more to external warning signs such as final demands for payment and threatened court action, and perceived the fewest personal negative consequences of problem debt.

Stricter lending criteria, financial education in schools, and advice at the point of need were among the diverse solutions perceived as being needed to prevent problem debt.

Whilst the need for people to take more personal responsibility was discussed by people in their family years, some young adults seemed to circumscribe personal responsibility for their spending and borrowing behaviour.

Conclusions and policy implications

Young adults seemed especially susceptible to strong societal pressures to consume and were prepared to borrow to do so. A core minority were circumscribing personal responsibility for their credit use and saw debt consolidation and insolvency as an easy way out.

There were two key routes to over-commitment among the family years groups: the pressures to provide for all their children's needs and wants; and a belief that housing equity can provide for all future financial needs.

People in the post-family years had generally cautious attitudes towards borrowing, and were willing to borrow for only a narrow range of purposes.

Three important policy issues emerge which raise questions about greater risks of payment default and the implications for longer-term financial planning. These are:

- The apparent connection between consumption and borrowing;
- A belief in housing equity as the solution to all future financial needs;
- A disconnect between the perceptions and reality of 'debt solutions'.

In discussion with a panel of experts, the research concluded that policy responses need to focus on providing a counterbalance to the 'want it now' consumer culture, promoting financial capability through a coordinated approach. This should centre on the positive message of 'making money work for you', which must be delivered consistently and repeatedly to all age groups to be effective.

For more information on this report please call us on this number or go to the website below:

0131 245 0102

www.standardlife.co.uk

P f R C
PERSONAL • FINANCE • RESEARCH • CENTRE