

## Credit Consumption and Debt Accumulation among Low-Income Consumers: Key Consequences and Intervention Strategies

### An Exploratory Study

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## Outline of Presentation

- Review of Literature and Policy
- Methodology
- Analysis of Agency/Supply-Side Research
- Analysis of Consumer-Focused Research
- Conclusions, Recommendations and Limitations
- Q&A

## Defining Credit and Indebtedness

### Definitions:

- Credit is "the provision of money to facilitate a purchase, which will have to be repaid at a later date, along with interest and other stated charges e.g. loans, overdrafts, credit cards, credit sales, charge cards, in-store cards, hire purchase, leasing (consumer hire), housing, loans/mortgages, moneylending and pawnbroking" ([www.odca.ie](http://www.odca.ie))
- Indebtedness is the "frequent use of credit which is now part of the common currency of society, whereas over-indebtedness relates to the imbalance or shortfall between income and expenditure" (Joyce, 2003)

## Poverty, Low Income and Indebtedness in Ireland

- Lack of Irish research
- Indebtedness is a major social problem in Ireland, linked to income inadequacy for low-income families (NAPS, 2003-2005)
- Low-income households were most likely to find their debts to be a heavy burden (Hughes and Duffy, 2005)
- EU SILC, 2004 - 8.7% experiencing debt problems to meet ordinary living expenses (CSO, 2005)

## Nature of Debt Among Low- Income Groups

- Rent and Mortgage arrears are priority (MABS, 2004)
- Utility arrears (Massey, 2004)
- Food poverty (Friel and Conlon, 2004)
- Consumption related to events, celebrations e.g. First Communion, Weddings, Bereavements
- Changes in circumstances: drop in income, job loss, lifestyle interruptions (McKay, 2005)
- MABS client (2005):
  - 36-40 majority age group
  - 20% hold mortgage
  - 31% are employed
  - 55% of debt owed to banks/financial institutions

## Access and Use of Credit Among Low-Income Groups

- The Sub-prime Market
  - Main providers of small value loans (Datamonitor, 2004)
  - Moneylenders
    - 50 traders serving 150,000 people (Conroy and O'Leary, 2005)
    - 72% borrow from moneylenders (Byrne *et al.*, 2005)
  - Goods on Credit Providers (21 week period)
  - Pawnbrokers
- The Prime Market
  - Banks
    - Access widening but 2-tiered system exists (Conroy and O'Leary, 2005)
  - Credit Unions
    - Valuable source of affordable credit (Slattery, 2005)
    - Small loan amounts and geographic proximity (Byrne *et al.*, 2005)

## Initiatives to Tackle Indebtedness

- Widening Access to Credit and Promoting Financial Inclusion
  - Lone parents (Conroy and O'Leary, 2005);
  - Travelling community (Quinn and Ni Ghabhann, 2004)
  - Credit Union recommended to increase marketing & education initiatives, offer EFT service, small loans (Byrne *et al.*, 2005)
- Encouraging Saving among Lower-Income Consumers
  - Small amounts, short term saving
  - UK Gateway Saving Scheme
- Money Advice and Support
  - MABS/Credit Union Special Budget A/C
  - MABS Social Lending Scheme
  - FLAC

## Initiatives to Tackle Indebtedness

- Improving Financial Literacy and Capability
  - NALA (2004)
  - [www.itsyourmoney.ie](http://www.itsyourmoney.ie)
- Increasing Consumer Protection and Legislation
  - Role of Financial Regulator
  - Consumer Protection Codes

## Research Methodology

### Research Objectives

- Types of credit available to and used by low-income people and nature of underlying consumption
- Nature and extent of low-income indebtedness and current attitudes and behaviours
- Adequacy and appropriateness of access and provision, advice, support and regulation
- Intervention strategies to be developed and augmented

## Research Methodology

- **Secondary Research**
  - Irish & international academic sources, administrative data, survey data
- **Primary Research**
  - 5 Interviews with range of supply/agency-side informants
    - CEO, Irish League of Credit Unions (ILCU)
    - Head of Sales, Marlboro Trust (Moneylender)
    - National Development Officer, Money Advice and Budgeting Service (MABS)
    - Head of Research and Policy, Combat Poverty Agency (CPA)
    - National Social Policy Officer, St Vincent de Paul (SVP)
  - 5 Interviews with MABS clients/ advisors
    - Client 1 (Female, Married/Children, Unemployed, Urban, 45-54)
    - Client 2 (Female, Married/Children, Recently Employed, Rural, 35-44)
    - Client 3 (Female, Lone Parent, Part-time Employed, Urban, 25-34)
    - MABS Advisor 1 (Mid West Region A)
    - MABS Advisor 2 (Mid West Region B)

### Agency/Supply-side Findings:

## Changes in Low-Income Debt & Debtor

- Changes in Nature of Low-Income Debt
  - Expectations, Lifestyle-driven consumption e.g. HIFIs, clothes, mobile phones, cars and children-related expenses
  - Some low-income debt related to mortgages and credit cards (ILCU)
- Change in Profile of Debtor
  - Gender – “women own the problem” (MABS)
  - Geographic background – urban vs. rural
  - Income – “working poor, newly indebted” (CPA)
  - Age/Lifecycle – young families, single parents (Marlboro Trust) change in expectations among young people

### Agency/Supply-side Findings:

## Financial Exclusion

- Low frills banking/basic bank account
- MABS/Credit Union pilot initiative for lone parents
- Asset transfer:

*The only way that people get out of poverty is through the accumulation of assets ... asset transfer doesn't mean money necessarily. It means education, it means health, it means access to financial services ... you don't have enough money to save, not enough money even for today ... just talking about access to credit, it's just not enough (Michael Culloty, MABS)*

## Agency/Supply-side Findings: Role of Financial Service Providers

- Mainstream Banks
  - Not interested in Low-Income groups as not profit-making, inaccessible, marginalised
  - BUT social finance initiative being developed (CPA)
- Credit Unions
  - 45% of loans for €1,000 or less (ILCU)
  - BUT more "middle-class" in focus
  - Need to more actively target low-income groups
- Moneylenders
  - Legitimate role: convenience, immediate need (MABS)
  - Lack of awareness of APR (100-200%)
  - Self-sufficiency of person encouraged (SVP)

## Agency/Supply-side Findings: Saving

- Saving possible but not widely practiced
- UK Savings Gateway (SVP)
- Dedicated Low-Income Savings Account:

*... the [savings] product has to be quite different ... the ones that strike me are having some place where they can store and manage their money, a kind of low-cost facility. The second one would be then short term loans which again are at a very modest cost ... the third one is a kind of savings facility that ... offers some level of flexibility (Jim Walsh, CPA).*

## Agency/Supply-side Findings: Financial Capability and Literacy

- Financial Capability, Budgeting and Planning Ahead
  - Mix of financial capability
    - "excellent money managers...others lack money and budgeting skills" (SVP)
  - Income inadequacy
    - "living on the borderline" (CPA), "barely surviving" (MABS)
  - Mitigating factors
    - Health-related issues, pressure from society, child-related spending
- Financial Literacy, Education and Confidence
  - Low level of literacy and knowledge of financial options
  - "Educational promotion in disadvantaged communities" (ILCU)
  - Need for "life skills" and empowerment (CPA)

## Agency/Supply-side Findings: Debt Management, Support, Protection (1)

- Effectiveness of System in Managing People in Debt
  - Certain kinds of debt "harder to detect" e.g. credit cards (SVP)
  - 3 to 4 years training to identify people in debt (Marlboro Trust)
  - MABS - "single most important state intervention" (ILCU) but "self diagnosing" key due to limited resources (MABS)
  - FLAC key but legal system needs to be modernised
- Responsibility of Financial Providers in Debt Issue
  - "laissez-faire approach" (ILCU)
  - "lack of pro-activity" "non-discrimination" (CPA)
  - "Incentivised through community re-investment tax" (SVP)
- Governmental and Societal Responsibility
  - "mainstreaming social inclusion" (CPA)

## Agency/Supply-side Findings: Debt Management, Support, Protection (2)

- Debt-Coping Strategies
  - Lack of adequate income and savings mechanism
  - Varying debt situations - Chronic debt, "bad but manageable" debt (CPA)
  - Psychological issues "feeling powerless", "chronic hopelessness" (SVP)

*...they may go without food ... they may go without light and heat ... Others would try and borrow their way out of it by getting a loan to pay off a loan. Some people would have two or three moneylenders. And again it's like the credit card, borrowing from one to pay off the other (MABS).*

## Agency/Supply-side Findings: Regulation

- Appropriateness of Current Level of Regulation
  - "inadequate" "inappropriate" for low-income groups
  - "may not have enough information to make rational choices" (CPA)
  - "improved awareness of negative effects of spending" (SVP)
- Regulation of Moneylenders
  - Consumers dislike completing loan documentation (Marlboro Trust)
  - No cap on interest rates
  - Discourage "illegal's" (unlicensed moneylenders) to enter market (MABS)
  - Need for improved customer protection (CPA)

### Consumer-focused Findings: Living on a Low Income

- Traditional expenses e.g. rent/mortgage, utility bills etc
- Lumpy expenditure e.g. Christmas, Confirmation, child-related expenses etc
- Luxury expenses e.g. holidays, cars, house improvement, luxuries like TV/DVD systems and mobile phones
- Difficulty in budgeting and managing on low-income
  - "It goes in one hand on a Thursday and out the other" (Client 3)
  - "I couldn't tell you the last time I was outside the door" (Client 2)

### Consumer-focused Findings: Access to and Use of Credit

- Banks - Access has increased (particularly if employed) but only until client defaults e.g. small loans, credit cards
- Credit Unions – Flexible, supportive, low-cost credit
  - *The Credit Union is the only place I can get money ... They will actually negotiate how much do you think you could pay back weekly ... They're the best option for me anyway* (Client 1).
  - **BUJ** "huge fluctuation in increase in debt to credit unions" (Advisor 1)
- Moneylenders – Flexibility, tradition, costly, intimidation
  - *... I got an X box off him, I got a carpet off him ... I was paying it back, to be honest with you I was afraid of my life not to pay it, he would sit outside my door for over an hour, and he would bang and bang ... I was afraid to go out to him, because he would disgrace me out in the front of the neighbours ... at one stage he came to the door for money and the abuse he threw at me in front of them! Oh I actually cried here over him... I owed him very little and he disgraced me* (Client 3).

### Consumer-focused Findings: Access to and Use of Credit

- Credit Cards
  - "easy access", "increased limit" but high risk of default:
    - *She had two MBNA credit cards and a Bank of Ireland credit card and they're all in bad debt now ... they would have allowed her credit up to €4,500 on one of those credit cards. MBNA...because she was a good payer in the beginning and they increase your limit* (Advisor 1).
  - Credit cards were "handed to you on a plate" but had "learned my lesson" (Client 2)
- Other sources
  - Non-mainstream financial institutions
  - Target consumers with adverse credit rating

### Consumer-focused Findings: Saving and Financial Exclusion

- Saving – "difficult" and sometimes "impossible"
  - *... we just want to clear off everything first, get on an even footing and then we would be able to start saving. That's our main goal at the moment anyway* (Client 2).
- Financial Exclusion
  - Increased need for access to bank accounts for "employers, FAS schemes, even social welfare" (Advisor 1)
  - Vicious circle - access to mainstream lenders results in increased borrowing and potentially default resulting in financial exclusion
  - "I had to go to Provident. They helped me out with my daughter's Confirmation. I had no other choice" (Client 3).

### Consumer-focused Findings: Financial Capability and Literacy

- Money Management & Budgeting Skills varied
  - "some can't manage money" vs. "would teach us" (Advisor 1)
  - *I have always done my Christmas planning in September, the minute they are gone back to school ... that's the way I have always worked it ... I could do with a new suite of furniture ... but I was passing a shop and they were closing down and I got fantastic throws for €10. It made all the difference* (Client 2).
  - More acceptable to have money problems and seek advice (Advisor 2)
- Financial literacy and awareness of cost of credit low
  - Banks "don't give a hoot" (Client 1);
  - They "did not make it clear" "badly caught", "very very wary" (Client 2)

### Consumer-focused Findings: Nature of Debt

- MABS - 20% of clients experiencing utility debt; 80% of debt through credit cards, mobile phones (Advisor 2)
- Low-income consumption driving debt (e.g. cars, holidays)
  - *I took out a loan to buy my car which was €5,000. I took out a loan just to have a nice life ... didn't go on anything too extravagant ... a car ... I'd pay off bills and stuff like that. Go on a holiday to England you know ...* (Client 1).
- Low-income credit driving debt (e.g. bank/supermarket loans, top-ups, moneylenders)
  - *I borrowed €3,500 in a Tesco loan and then I got a loan a few years ago from the Ulster bank to go on a holiday and then I topped that up to €3,000 ... When I went for a loan to the bank to clear off the Tesco loan and the Ulster Bank loan she told me I would have to clear off €4,500 ... Then with the moneylender is €500-600 ... or nearly €700 ...* (Client 3).

## Consumer-focused Findings: Nature of Indebted Client and Debt Triggers

- Indebted Client
  - 80% of MABS clients are younger of which 'half would be working' (Advisor 2).
  - Middle-class people had become MABS 'more traditional client' where there are 'both couples working' (Advisor 1)
  - Low-income, social welfare are still a priority for MABS
- Triggers of Debt
  - Change in circumstances "maternity leave, an accident" (Advisor 2)
  - Consumerist society – pressure to "buy buy buy" (Client 1)
  - Lifestyle and child-related expenditure:
    - My daughter 'wants to be up to date' and 'constantly needs money for this and that' (Client 3).

## Consumer-focused Findings: Coping with Debt

- Mental and Physical Implications of Debt
  - "awful pressure" not able to cope" "just hanging in there"
  - *... I could be 6 under because at one stage as ... I was in the habit of taking tablets ... and 40 is well the highest within 3 days whereas you're supposed to go into hospital after if you take 10 together ... I continued that route you know. Then I was doing self-harm to myself. Three little rusty nails I found at home ... swallowed them ... I was hoping it would bust the lung or something, d'you know (Client 1).*
- Not Confiding in Family or Friends
  - "would be shot if family knew" (Client 3)
  - MABS provides key counselling service "someone to listen to outside of their family" (Advisor 1)

## Consumer-focused Findings: Debt Support Services

- Debt Support offered by MABS
  - "brilliant" "they fight your case" (Client 1)
  - "only for MABS I would be lost, MABS is the best thing that ever happened to me" (Client 3)
  - Empowerment and "capacity to help themselves" (Advisor 1)
  - MABS perceived by financial providers as key intermediaries
- MABS Outreach Education and Support
  - Communities and schools targeted
  - "prevention more than cure" (Advisor 1)

## Consumer-focused Findings: Regulation

- Access
  - "easy to get money" (Client 2) "just a matter of a phone call" (Client 3)
- Credit Limits
  - "they just kept building up the credit limit" (Client 1)
- Lender Practices and Responsibility
  - "lack of analysis of client financial situation" (Advisor 1)
  - Multiple accounts with credit unions
  - Need for credit scoring
- Borrower Responsibility
  - *There's the lender's responsibilities and there's the borrower's responsibilities ... And they [the bank] don't check because they're just relying on the person to tell them ... and these are people who are desperate for money (Advisor 1).*

## Conclusions: Secondary Research-Based

- Direct Link between poverty and indebtedness
- Change in nature of low-income debt and debtor
- Access to credit widening but not always appropriate to low-income groups
- Further low-income intervention and support required

## Conclusions: Agency/ Supply Research-Based

- Higher expectations – aggressive marketing, heightened pressure of consumerist society
- New MABS client -working/newly indebted
- Low-income consumers incurring middle-class, luxury-based debt e.g. cars, mobile phones, luxury child-related expenses
- Acquired through middle-class credit e.g. credit card, personal loans, overdrafts
- Access to prime credit is widening but banks and credit union deemed "middle-class" in focus
- Current low-income intervention strategies regarding regulation and support are inadequate

## Conclusions: Consumer Research-Based

- Difficulties in budgeting and in relation to “lumpy expenditure”
- Increased access to credit but higher level of default
- Low level of saving and financial capability creating cycle of indebtedness
- Low-income debt and debtor have evolved driven by pressure from society and desire to attain desired lifestyle
- Psychological and physical repercussions of debt
- Augmented debt support services & increased regulation and protection needed e.g. credit scoring & stricter limit controls
- Current intervention strategies regarding regulation and support are inadequate

## Key Recommendations

- Addressing Financial Exclusion
  - Asset Banking
- Augmenting Money Advice and Support Services
  - MABS
- Heightened Regulation and Consumer Protection
  - Lender Responsibility and Pro-activity
- Strategic Priority of Low-Income Credit and Debt at National Policy Level
  - “Mainstreaming” of low-income issues in government policy
  - State-funded research

## Other Recommendations

- Providing Low-Income Saving Opportunities
- Continued Improvement of Financial Literacy and Capability
- Enhanced Debt Management and Support

## Limitations and Future Research Directions

- Exploratory Study – Small Samples Sizes
- Not generalisable but indicative of key themes warranting further investigation
- Further larger-scale qualitative and/or quantitative research with agency/supplier informants and low-income consumers called for

Thank Your for your Attention

Questions?