

## 4 Responsible lending and borrowing?

The credit market has become very competitive, and in a highly competitive market the most profitable customers can also be the most risky. In the words of the credit risk department head of a leading lender '*The accounts that are headed for delinquency will look like your most profitable*' (Bailey 2002<sup>1</sup>).

A number of marketing practices have led to concerns, raised at the DTI's Task Force, that they may be contributing to the problem of over-indebtedness. At the same time, there is an awareness that irresponsible borrowing also plays an important part in adding to the problem of indebtedness and that consumer awareness of the terms of the commitments they take on is too low. This chapter examines each of these areas in turn.

Before we do so, however, it is important to return to the term 'over-indebtedness'. Although it is widely used, there is no generally agreed definition. Indeed, various commentators have interpreted it quite in different ways (Betti et al, 2001). Following discussion by the Task Force it was decided to adopt a pragmatic approach and to use:

- a measure of the extent of current financial difficulties, including arrears (20 per cent of all households)

and two definitions of heavy credit use, both of which are strongly associated with reported levels of financial problems:

- spending more than 25 per cent of gross income on consumer credit (5 per cent of all households) and
- spending more than 50 per cent of gross income on consumer credit and mortgages (6 per cent of all households).

In doing so, we are not saying that a household is only over-indebted if their spending is above these levels – it is merely an analytical tool that accords with a common sense view of experts on consumer borrowing.

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<sup>1</sup> This article was based on interviews with a number of credit risk department heads, four of whom agreed to have their quotations attributed to them.

## 4.1 Irresponsible lending?

A number of marketing strategies were of concern to some members of the Over-indebtedness Taskforce and the research found evidence that they are potentially problematic. These strategies include:

- The automatic raising of credit limits on credit and store cards and on overdraft facilities
- Encouraging people to transfer balances on credit cards, by offering low initial interest rates and higher credit limits
- Reducing the minimum payment on credit cards
- Issuing cheques that can be used to draw on credit card accounts

None of these practices affected large numbers of people and it would be wrong to claim that they *caused* financial difficulties or over-borrowing. They do, however, disproportionately attract people who face these situations and can potentially make a bad situation worse.

### *4.1.1 Automatic increases in credit limits*

Automatic rises in credit limits are quite common - as a credit risk manager has put it 'You can't afford not to do it because all your competitors are doing it' (Bailey, 2002). There are, however, concerns that they are also raised without adequate checks on the customer's credit risk.

Indeed, when asked directly, 83 per cent of the people interviewed for this study thought that credit limits should only be increased at the customer's request and not increased automatically. In practice, this was still seldom the case.

#### *Credit cards*

Three in ten of all households with a credit card had had a credit limit increase on at least one of their cards in the past 12 months (Table 4.1). (This is equivalent to 15 per cent of all households). In most cases the limit had been raised automatically and not at the customer's request; fewer than one in ten people had asked for the increase. A similar proportion had used some or all of the increase granted. About two in ten receiving an increase had been close to or over the limit at the time it was raised. This accords with earlier research on credit cards (Berthoud and Kempson, 1992; Rowlingson and Kempson, 1994).

There was evidence of a link between raised limits on credit cards and financial difficulties. Households that were in financial difficulties at the time of the interview were more likely to have had an increase in the limit on their credit card in the past 12 months than other card-holders - even though the number of cards held by these two groups was almost identical (Table 4.1). Consequently, six in ten of those who were

close to or over their limit at the time it was raised were in financial difficulty, as were half of those who had used some or all of the increase.

Indeed, some credit risk managers in credit card companies have acknowledged that they raise limits in the knowledge that the highest risk customers are also the ones that need and will use the increase.

*'It's remarkable how many times you see a situation where written-off accounts have had significant automatic credit limit increases, based on behavioural scoring strategies, less than 12 months before the account becomes delinquent.'*  
(Bailey, 2002)

**Table 4.1 Credit limit increases on credit cards, overdrafts and store cards/accounts**

*Cell percentages*

	All with an account	Financial difficulties	25% of income on credit	50% of income on credit/m'gage
Percentage of account-holders with limits raised on:				
Credit card	28	37	40	37
store card/account	10	18	..	..
agreed overdraft facility	16	26	22	29

*.. numbers too small for analysis*

There was also a link with high levels of repayment on borrowing. Households that repaid a high proportion of their gross income either on credit alone or on credit and a mortgage were also more likely to have had the limit increased on one of their credit cards than were other card holders (Table 4.1). They were also more likely to have used the increase. They also accounted for three in ten of the card-holders who were over or near their credit limit when it was raised.

In this case, people with high levels of repayment on borrowing, held slightly more credit cards than the average for all card-holders (1.9 compared with 1.6).

#### *Store cards and accounts*

Credit limit increases on store cards/accounts were less common (Table 4.1) but again fewer than one in ten customers had requested the increase. Only a small number of card holders were over or close to their credit limit when it was raised. As the number of people involved was quite small it is not possible to report on any link with over-indebtedness, save for the fact that raised limits were more common among people who were in financial difficulties (Table 4.1).

#### *Overdrafts*

Overdraft limit increases were also more common among people with financial difficulties or paying a high proportion of their income to service their borrowing (Table 4.1). But they were somewhat different from credit and store cards in that half of the people whose credit limit was increased had requested it and this rose to three quarters of households in financial difficulties.

Reflecting this, four in ten households whose overdraft limit was increased had been close to or over the limit at the time. Again this was associated with financial difficulties; six in ten households at or over the limit when it was raised had financial problems. There was a similar link with higher levels of repayment on borrowing but it was less pronounced.

*The need for checks on risk*

Taken together, this evidence lends weight to the proposal that credit limits should only be increased following a check on account-holders' credit worthiness. The information relating to overdrafts shows that this will be more effective in preventing over-indebtedness than seeking prior authorisation from customers, as households in financial difficulty are especially likely to agree to an increase. This concurs with the experience of credit risk managers (Bailey 2002).

Some in the industry have argued the case for improved behavioural scoring (CCRG 2002a); others that a more holistic approach is needed.

*The truth is that each credit card operator is looking at a very small world. You won't pick up someone paying off one card with another. You have to look at the customer at customer level, not just account level. I would like to see all issuers using behaviour scores via the credit [reference] bureaux.' (Bailey 2002)*

Research has shown that a check with credit reference bureaux would identify a high proportion of the most risky customers (Tingay and Wilkinson, 2002).

#### **4.1.2 Transfer of credit card balances**

Recent years have seen a considerable growth in offers of low initial interest rates on balances transferred from one credit card to another. For many people it would be a rational decision to move balances in this way, but concerns relate to people who transfer because they are facing financial difficulties and may not have made plans for meeting the interest charges when the initial low rate ends. In particular, there have been concerns that some people are unaware of when the period of low interest will end and what the charges will be afterwards.

One in twenty (5 per cent) households with credit cards had opened a new account in the past 12 months and transferred balances from other cards. Almost all of them had been offered a low rate of interest on the transferred balance and four in ten had also been offered a higher credit limit than they had on their old card. (This is equivalent to 3 per cent of all households).

Switching credit card provider to pay off other cards was quite strongly associated with financial problems (Table 4.2); half of those transferring balances in this way were in financial difficulties. The proportions were higher still for those who not only transferred

balances but were also offered a higher credit limit. Two thirds of these people had financial problems.

**Table 4.2 Credit cards: balance transfers, minimum payment and receipt of credit card cheques**

	<i>Cell percentages</i>			
	<b>All with an account</b>	<b>Financial difficulties</b>	<b>25% of income on credit</b>	<b>50% of income on credit/m'gage</b>
Percentage of account-holders:				
Transferring balance from another card	5	15	10	9
Regularly making minimum payment	7	23	29	20
Receiving credit card cheques	16	24	23	23
<i>Base: all with a credit card</i>	<i>856</i>	<i>99</i>	<i>51</i>	<i>76</i>

The link with the amounts households spent repaying money borrowed was not quite so marked. In part this is explained by the fact that card-holders who had transferred balances had been given a lower minimum payment – and in our calculation of the proportion of income spent on credit repayments we included the minimum payment for credit cards. Even so, they included twice the average proportion of households who had also been given an increased credit limit.

#### ***4.1.3 Reducing the minimum payment on credit cards***

A further practice that is gaining momentum is a reduction in the minimum monthly repayment on credit cards. For most cards the minimum payment has been 5 per cent of the outstanding balance, but an increasing number of card suppliers have reduced the limit to 3 per cent or even 2 per cent. This has raised criticisms that someone making only the minimum payment will take decades to clear a large balance. Writing in *Money Mail*, the former director of the Credit Card Research Group has calculated the length of time it would take to clear a £3,000 balance on a card with a monthly interest rate of 1.313 %, if only the minimum payment were made each month. She estimates that it would take nine and a half years to clear if the minimum payment were 5 per cent. Reducing the minimum payment to 3 per cent almost doubles the time to clear the balance (18 years) and reducing it further to 2 per cent quadruples it (37 years) (Phillips, 2001).

A minority (7 per cent) of households with credit cards regularly made only the minimum repayment on at least one card (equivalent to 4 per cent of all households). Again there was a strong link with our measures of over-indebtedness (Table 4.2). So households that were in financial difficulties were three times more likely to be making only the minimum payment, as also were those spending half or more of their income on consumer credit and mortgage repayments. It was higher still (four times the average) among households spending a quarter or more of their income just on consumer credit commitments.

These will, of course, be the very people who are attracted to cards with low minimum payments and with repayment levels as low as 2 or 3 per cent they will be unlikely to reduce the balance on the cards that they have.

#### ***4.1.4 Credit card cheques***

Credit card cheques are a fairly recent development. These are cheques that are issued to credit card holders that can be used in the same ways as other personal cheques except that the money spent is debited from the credit card account. Unlike payments made with the card itself, payments made with the cheques incur interest immediately, in the same way as cash withdrawals using a credit card.

One in six (16 per cent) of households with credit cards had been sent cheques by their card supplier in the past 12 months. (This is equivalent to 8 per cent of all households in Britain.) In almost all cases these were sent unsolicited. Only a minority (13 per cent) of cheque recipients had used any of them, so the numbers are small and the following analysis needs to be treated with caution. A third of them had used the cheques either to pay bills or to pay off debts. Only a third of cheque users knew that they paid interest on the money straight away.

Interestingly, credit card cheques had been sent to above average proportions of card holders who were either in financial difficulty or spending a high proportion of their income on repaying the money they had borrowed (Table 4.2).

## **4.2 Irresponsible borrowing?**

A responsible credit agreement can depend just as much on responsible borrowing as it does on responsible lending. Here there are three main areas of particular concern:

- Borrowing to re-finance other credit or to pay off arrears on bills and other commitments. There is evidence that not only has this become more common, but it is a strategy used disproportionately by people who are either in financial difficulties or have borrowed substantial amounts.
- Households who take on credit agreements, despite knowing that they will struggle to repay the money.
- Unplanned purchases and credit use, which is also linked to financial difficulties and heavy borrowing.

### ***4.2.1 Re-financing and borrowing to pay bills***

Although re-financing can reduce the repayments that households have to make on their total credit commitments, there are concerns that it is often only a short-term solution and that many of these households would do better to seek advice from a free money advice centre. An added concern is that refinancing is often secured on the borrower's home.

Indeed, a survey of consumer credit providers by the Finance and Leasing Association shows that debt consolidation was the main reason for their customers taking out a loan and that the proportion was higher for secured than for unsecured loans. In 2000, 58 per cent of the £1.8bn new secured lending was used by consumers to pay off existing debts – an increase from 1999 when it was 50 per cent. The proportion of the £9.4bn unsecured lending used for debt consolidation was lower, at 38 per cent, and this had fallen from 42 per cent in the previous year (Finance and Leasing Association, 2001).

This growth was confirmed by a comparison between the present survey and the one carried out in 1989. In 1989, 17 per cent of commercial loans were used to pay other creditors or to make ends meet (Berthoud and Kempson, 1992). An identical question in the 2002 survey showed that it had risen to 30 per cent.

Altogether 15 per cent of households had borrowed money in the past 12 months to repay other creditors or to make ends meet (Table 4.3). They had borrowed this money in one of three of ways:

- On credit cards (12 per cent of all households – excluding those who had transferred balances from one card to another)
- Taking out loans (5 per cent of all households)
- Mortgage extensions (1 per cent of households)

Most commonly people said they had borrowed ‘to pay bills’ and this was equally true for all three types of credit agreement. While it is plausible that someone might routinely pay bills on a credit card it is highly unlikely that they would take out a loan or re-mortgage their home to do so. In such cases, at least, it is very likely that they had fallen into arrears. For much the same reason, it is improbable that people would take out a loan or re-mortgage ‘to make ends meet’.

**Table 4.3 Extent of refinancing**

	<i>Column percentages</i>				
	<b>All</b>	<b>Arrears in past 12 months</b>	<b>Financial difficulties now</b>	<b>25% of income on credit</b>	<b>50% of income on credit/m'gage</b>
To pay bills	9	16	14	22	17
To refinance other borrowing	2	3	4	6	7
To pay off other debts	4	13	13	20	15
To make ends meet	3	9	10	10	10
None of these	85	70	71	63	68
<i>Base: all householders</i>	<i>1,647</i>	<i>305</i>	<i>325</i>	<i>79</i>	<i>102</i>

Quite clearly, borrowing money to pay other creditors or to make ends meet was associated both with being in financial difficulties and also with spending a high proportion of income either on consumer credit alone or on consumer credit and a mortgage (Table 4.3).

In other words, borrowing for any of these reasons is almost certainly an indication of financial stress. This was borne out by the fact that four in ten of the households who had re-financed said that they had been in financial difficulties at some time in the past year and six in ten said it was a struggle to make ends meet some or all of the time. Whether this is seen as irresponsible borrowing or irresponsible lending is a matter for debate. To some degree it is almost certainly both.

#### 4.2.2 Doubts about ability to repay money borrowed

Credit screening ought to ensure that people are not lent money if they are already in financial difficulty or have borrowed large amounts of money relative to their income. In practice, though, this does happen and not all of the blame can be laid at the doors of lenders.

In the survey, households who had arranged a mortgage, a loan or other fixed term credit were asked how easy they expected it to be to keep up with the repayments when they took on the commitment. On the whole, most of them said that they expected to be able to pay without difficulty. A minority had either anticipated some problems or had not thought about the matter at all (Table 4.4). It is important to keep in mind that this was people's own assessment of their ability to repay and not an objective measure of it. Indeed, some people may have been deluding themselves that they would be able to keep up with the repayments.

**Table 4.4 Expectations regarding ability to repay loans and hire purchase agreements**

	<i>Column percentages</i>		
	Hire purchase/ credit sale	Loans	Mortgages
Expected to pay without difficulty	82	75	70
Thought it would sometimes be hard to find the money	12	15	23
Thought it would always be hard to find the money	1	2	2
Did not think about it	6	8	5
<i>Base: all HP, loan or mortgage</i>	<i>221</i>	<i>251</i>	<i>629</i>

In general, households that were in financial difficulties were much more likely to have anticipated problems keeping up with the repayments at least some of the time: three in ten (29 per cent) on loans; a third (36 per cent) on hire purchase agreements and nearly half (46 per cent) on their mortgages. In fact, two thirds (67 per cent) of the people who had any reservations about their ability to make the repayments on their loans or hire purchase agreements were in financial difficulty at the time of the survey. So, too, were a third (32 per cent) of the people with similar reservations when they took out their mortgage, even though many of them would have taken out their mortgages a number of years previously.

On the whole, it was not possible to study the links with the proportion of gross income spent on credit or mortgage repayments, as the numbers were too small. The one exception was mortgages, and here there was a clear link. Four in ten (41 per cent) of households spending half or more of their gross income on their mortgage and credit commitments had reservations about their ability to keep up with their mortgage repayments, when they borrowed the money.

This same question was also asked of households who had borrowed money in 1989. This earlier survey found that 83 per cent of households with hire purchase agreements and 77 per cent of those with loans had expected to keep up with the repayments without difficulty. It also found a strong link between arrears and anticipation of problems repaying (Berthoud and Kempson, 1992).

In other words, the situation in 1989 was much as it is now. So, although households have borrowed far larger amounts currently than their counterparts in 1989 most expect to find the repayments manageable because they are paying much lower rates of interest.

#### ***4.2.3 Impulsive spending and unplanned purchases on credit***

Previous research has identified a clear link between compulsive shopping, over-borrowing and financial difficulties. The people who were most affected had a tendency towards other addictions too. This research was undertaken across four European countries, including Dumfries and Galloway in Scotland. It classified a third (33 per cent) of the adult population as ‘addictive spenders’: with 12 per cent having a considerable addiction to shopping and 3 per cent reaching levels that were ‘pathological’. Although overall scores did not vary a great deal between the four participating countries, there were some subtle differences in the make-up of their scores. Compared with others in Europe, people in Scotland were more likely to acknowledge buying on impulse and to think that they used credit cards too much (Junta de Comunidades de Castilla-La Mancha 2000).

As we noted in Chapter 2, two attitudes to shopping and spending were strongly associated with heavy credit use:

*I am impulsive and tend to buy things even though I can't always afford them.*  
and  
*I am a saver, not a spender*

As Table 4.5 shows, there was also a very strong link with being in financial difficulties, and especially so with being in arrears with consumer credit commitments. So, although only 5 per cent of the householders interviewed agreed strongly that they tended to buy things on impulse it was three times higher (15 per cent) among those that were currently in arrears with consumer credit repayments. Similarly, while 7 per cent of householders disagreed strongly with the proposition that they were a saver not a spender, 24 per cent of those with consumer credit arrears said the same.

**Table 4.5 Attitudes to shopping and spending**

		<i>Column percentages</i>			
	All	Financial difficulties now	Consumer credit arrears now	25% of income on credit	50% of income on credit/m'gage
<b>I am an impulsive shopper</b>					
Agree strongly	5	10	15	6	6
Agree	13	22	30	27	22
Neither agree nor disagree	8	10	6	9	7
Disagree	33	32	30	35	34
Disagree strongly	41	26	20	25	31
<b>I'm a saver, not a spender</b>					
Agree strongly	15	7	4	6	10
Agree	30	18	13	13	17
Neither agree nor disagree	30	27	22	35	37
Disagree	18	32	36	32	24
Disagree strongly	7	16	24	14	11
<i>Base: all householders</i>	<i>1,647</i>	<i>325</i>	<i>103</i>	<i>79</i>	<i>102</i>

The other measure of impulsive purchases came from questions relating to the loan and hire purchase agreements people had. Most households making purchases on credit had planned them all along and less than one in twenty had made completely spur of the moment decisions (Table 4.6). Emergency purchases were, however, slightly more common. Earlier research showed that unplanned purchases – whether emergencies or spur of the moment decisions - were associated with a higher than average risk of arrears (Berthoud and Kempson, 1992).

Results from the present survey lend some support to this earlier finding. Hire purchase agreements were more often taken on in an emergency by those who were in financial difficulties; while their loans were more often associated with impulse purchases (Table 4.6).

It should also be noted that the proportion of planned purchases is now much higher than it was in 1989, when only 56 per cent of hire purchase agreements and 61 per cent of loans were used for things that people had planned to buy all along. But the explanation for this difference lies in the higher proportion of emergency purchases in 1989, not to a higher level of impulse buying – which was more or less the same as now (Berthoud and Kempson, 1992).

**Table 4.5 Unplanned purchases and credit use**

	<i>Cell percentages*</i>		
	<b>All with HP or loan</b>	<b>Financial difficulties now</b>	<b>25% of income on credit</b>
<b>Hire purchase</b>			
Had planned purchase all along	70	67	64
Planned purchase but decided at last minute	17	17	13
Decided on spur of the moment	7	6	9
Emergency purchase	12	17	16
<i>Base</i>	<i>221</i>	<i>78</i>	<i>45</i>
Planned to use credit from retailer	81	83	76
Planned to borrow, decided source at last minute	13	13	9
Did not plan to use credit	8	7	13
<i>Base</i>	<i>221</i>	<i>78</i>	<i>46</i>
<b>Loans used for purchases</b>			
Had planned purchase all along	79	65	-
Planned purchase but decided at last minute	11	16	-
Decided on spur of the moment	5	11	-
Emergency purchase	14	16	-
<i>Base</i>	<i>138</i>	<i>55</i>	<i>-</i>

- numbers too small for analysis

\* numbers do not total 100 per cent because some people had more than one hire purchase agreement or more than one loan

The European study noted that compulsive shopping was more prevalent among young people, with nearly half of 14 to 18 year olds (46 per cent) being classified as ‘addictive shoppers’. This found some resonance in our own survey. Young people aged between 18 and 24 were far more likely to agree that they bought things on impulse (17 per cent agreed strongly; 29 per cent agreed). And many more of them disagreed that they were a saver, not a spender (21 per cent disagreed strongly; 32 per cent disagreed).

The number of young people who had bought things on hire purchase or loans was too small to assess how many of them had been unplanned.

### **4.3 Consumer awareness**

In its first report the DTI Task Force on Over-indebtedness highlighted the need for greater consumer awareness of the terms and conditions of the agreements they sign. This is reinforced by a report from the National Association of Citizens Advice Bureaux, which found that lack of financial literacy was an important factor among individuals experiencing difficulties with repaying credit. This manifested itself mainly in their choice of particular types of consumer credit (National Association of Citizens Advice Bureaux, 2001).

The survey specifically investigated two areas: awareness of cancellation rights and awareness of interest rates on fixed term credit.

#### ***4.3.1 Awareness of cancellation rights***

As fewer credit agreements are now arranged face-to-face in the lenders office, there is some concern that consumers taking on credit commitments over the telephone or internet or in their own home are unaware of their cancellation rights.

Almost nine in ten (86 per cent) of households with hire purchase/credit sale agreements had made them face-to-face in the lender's office and almost all of the rest knew about their cancellation rights.

On the other hand, nearly half (47 per cent) of households with loans were *not* confirmed in the lender's office in this way. Two in ten (22 per cent) were agreed on the telephone and just over one in ten were either agreed by post (14 per cent) or in the customer's home (11 per cent). Only a handful (2 per cent) had been agreed over the Internet.

At the time they signed their agreement, almost four in ten (37 per cent) of the people who had confirmed their loan agreements somewhere other than the lender's office did not know what their cancellation rights were. Again this needs to be set in context - it means that over the course of a year around 3 per cent of all households in Britain sign loan agreements without being aware of their cancellation rights. Although they were a very small minority, over half of these households were facing financial difficulties.

#### ***4.3.2 Knowledge of interest rates***

There has long been concern that most consumers do not know the interest rate even on their fixed-term credit agreements. In 1989, half of people with fixed term credit agreements said they did not know what rate of interest they were paying on them (Berthoud and Kempson, 1992). Disturbingly, our present survey shows that the situation was even worse in 2002. Three quarters (75 per cent) of households with hire purchase agreements and two thirds (63 per cent) of those with loans did not know the rate of interest being charged.

Households with financial difficulties and those with high levels of consumer borrowing were just as likely to know the interest rate they were paying as anyone else. If anything the heavy credit users were slightly *more* likely to know.

#### **4.4 Summary and overall conclusions**

Macro-economic statistics record a doubling in the amounts outstanding in consumer credit in the seven years between 1994 and 2001, even after allowing for inflation. Mortgage lending has also increased markedly over the same period.

In contrast, national figures indicate no increase in levels of arrears – on the contrary in most instances they seem to have fallen.

This survey has found that three quarters of all households had credit facilities of some kind, but only half of them owed money on them at the time they were interviewed. This points to a high level of un-drawn credit.

Most households used credit modestly, but a small minority were heavy credit users:

- 7 per cent had four or more credit commitments
- 5 per cent were spending a quarter or more of their gross income on consumer credit repayments
- 6 per cent were spending half or more of their gross income repaying their mortgage and other credit commitment.

Since the last comparable survey in 1989, the number of households with credit facilities has increased markedly, but the proportion currently repaying credit was about the same.

The amounts owed by credit users had, however, increased quite considerably – and especially on credit cards, loans and hire purchase agreements. It was this increase, plus the larger number of credit cards being settled in full each month, that seemed to account for the increase in borrowing recorded by official statistics. In other words, compared with 1989 more people would be at risk in an economic downturn.

Overall, about a quarter of households had been in arrears on one or more of their households commitments in the past year and around two in ten were in financial difficulties at the time of the survey. A small number (3 per cent) were currently behind with payments on three or more commitments. More were in arrears with their household bills (including mortgages) than had fallen behind with repayments on consumer credit agreements – but only because every household had to pay the main household bills; just half were repaying credit commitments.

It would seem that the situation is currently stable – over the last 12 months as many households got out of financial difficulties as saw them start. A considerable number of households, however, had been in financial difficulty for more than a year.

Financial difficulties were strongly associated with setting up home and having a family. The arrival of a new baby increased the risk of difficulties, as did relationship breakdown. Low and unstable incomes also increased the risk. Nearly half of households having financial problems attributed them to a loss of income and one in seven said it was because they were living on low incomes that were inadequate to meet their needs.

One in ten said that over-commitment was the cause of their financial difficulties. Using credit undoubtedly increased the risk of financial difficulties. So that the more credit commitments households had and the larger the proportion of their income that went on repaying borrowing, the more serious was their level of arrears on household commitments.

There is some evidence for the claims of both irresponsible lending and irresponsible borrowing. Lending practices that are associated both with financial difficulties and with high levels of spending on repaying money borrowed include:

- The automatic raising of credit limits on credit and store cards and on overdraft facilities.
- Encouraging people to transfer balances on credit cards, by offering low initial interest rates and higher credit limits.
- Reducing the minimum payment on credit cards.
- Issuing cheques that can be used to draw on credit card accounts.

These do, however, need to be set in context – each affects a relatively small number of high-risk households. But such practices do tend, quite disproportionately, to attract customers who are at a high risk of over-commitment.

At the same time there is clear evidence of borrowers acting irresponsibly:

- Borrowing money to re-finance other credit or to pay off arrears on bills and other commitments.
- Taking on credit agreements, despite knowing that they will struggle to repay the money.
- And impulsive shopping and credit use.

Each of these has a strong link both with financial difficulties and with high spending on credit repayments, although again each applies to only a small proportion of all households.

Of particular concern is the fact that, currently, more people are re-financing when they are having difficulty keeping up with payments than are either claiming on payment protection insurance or seeking advice from a free money advice service.

So, in conclusion, there is evidence that the historically high levels of borrowing are problematic for a only small number of people. But a far greater number would, potentially, be at risk of serious difficulties in an economic downturn or a period of sustained increased of interest rates. We need to find ways of minimising the risks, both by changes to lending practices and by educating consumers about the dangers of borrowing irresponsibly.