



RICH MAN, POOR MAN

How does income affect debt?

CCCS counsels clients from across the income spectrum; but all have debts beyond their control. In this investigation, two sets of clients are compared: those with a take home pay of less than £10,000 a year; and those with a take home pay of more than £30,000 a year – the “middle class” debtors.

The average take-home pay of a CCCS client in 2005 was about £16,500. Accepted wisdom suggests that a take-home income of £30,000 per year is enough to allow most families to be able to manage the demands on their incomes. But large mortgages, rising school fees, “keeping up with the Joneses” and the increasing availability of credit have made debt a normal part of life for many of the middle class.

Those at the other end of the spectrum are beset by different problems. Earning less than £10,000 a year means that virtually all income is spent on essentials – housing, utilities, clothing and food. Credit is used as a way of bridging the gap between income and essential expenditure.

Rich man, poor man: two different ways of life. How do the debts of these two groups compare?

Debt and indebtedness

Indebtedness can be measured in several different ways. The most direct is to examine the average unsecured debts for all clients from the two income categories. From this, we see that middle-class debtors are more than three times as indebted, with almost £70,000 as an average debt, compared with £20,000 for the low-income earners.

| | Debt |
|---------------|---------|
| Under £10,000 | £20,316 |
| Over £30,000 | £69,737 |

The picture changes, however, when we examine the ratio of debt to income for the different income brackets. The lower the debt to income ratio, the easier it should be to pay the debt off. Someone with an income of £30,000 a year is likely to find a debt of £15,000

much easier to pay off than someone who is earning £10,000 a year. How do the debt:income ratios of the two groups compare?

| | D:I ratio |
|---------------|-----------|
| Under £10,000 | 3.30 |
| Over £30,000 | 1.90 |

Clients earning more than £30,000 have a much lower average debt to income ratio than clients earning less than £10,000 a year, despite their debts being so much greater.

Clients on low incomes have often suffered a job loss or some long-term injury which means they can no longer work. Their earnings drop to low levels, but their outgoings are usually unable to be reduced quickly to the same level. Many turn to credit to bridge the gap between income and outgoings, and this is where the problems begin. Others find that, whereas they could manage repayments on their credit commitments well when they were earning full salary, the debt burden is now too much. What was originally a sensible debt level is now an unsustainably high debt to income ratio.

Credit is more easily available to people with higher incomes. A lender sees less risk in lending to someone with a high income than to someone whose income is low. Clients who earn more have a substantially higher number of credit commitments.

| | Number of debts |
|---------------|-----------------|
| Under £10,000 | 7.44 |
| Over £30,000 | 12.62 |

Social factors

What social and demographic factors distinguish the two income groups?

Unsurprisingly, age is the most telling factor. Clients in the 40 to 59 age group are the most likely to earn higher incomes while those under 25 are the most likely to have incomes of less than £10,000. The table shows the distribution of the two income brackets across the age groups.

| | 18-24 | 25-39 | 40-59 | 60+ |
|---------------|-------|-------|-------|------|
| Under £10,000 | 12.6% | 44.1% | 38.2% | 5.1% |
| Over £30,000 | 0.4% | 37.1% | 60.0% | 2.5% |

Clients earning more than £30,000 are more likely to be married and more likely to have children (the table shows the proportion of clients in each income group with the number of children):

| | 0 | 1 | 2 | 3 | 4 | 5+ |
|---------------|-------|-------|-------|-------|------|------|
| Under £10,000 | 53.3% | 21.5% | 16.6% | 6.4% | 1.8% | 0.4% |
| Over £30,000 | 32.6% | 22.0% | 29.8% | 11.8% | 2.9% | 0.9% |

It is probable, therefore, from this that households with an income of more than £30,000 a year will be older, and in a family unit – essential outgoings are likely to be high. Households with an income of less than £10,000 a year are likely to be younger, single people with no children. Essential outgoings will consequently be lower than for the over £30,000 income group.

Counselling solutions

After a counselling session, a CCCS counsellor will recommend the best debt solution for the client’s circumstances. About half of the people who come for in depth counselling find that a debt management plan is the best way to begin repaying their debts. These plans are developed and administered by CCCS.

In the other cases, other solutions are offered; the term financial counselling encompasses such solutions as bankruptcy, token payments to creditors and IVAs.

The third option is that the client’s debt problem is too complex to be dealt with in one counselling session, or that the counsellor requires further information about the client’s financial situation before being able to make a fully-informed recommendation – in these cases, clients have second appointments – and more if necessary.

| | DMP | Financial counselling | Second appointment |
|---------------|-------|-----------------------|--------------------|
| Under £10,000 | 48.0% | 43.2% | 8.8% |
| Over £30,000 | 54.7% | 31.8% | 13.5% |

Clients with an income of more than £30,000 a year are slightly more likely to be suitable for a Debt Management Plan, making fixed monthly repayments to their creditors through CCCS. They are also more likely to need a second appointment, probably because their financial affairs are more complicated.

Clients earning less than £10,000 a year are more likely to be offered one of the financial counselling solutions. This could be token payments, where the clients offer small monthly sums to their lender to show willingness to repay. Or it could be bankruptcy. Someone earning a small amount is unlikely to have assets which could be lost under bankruptcy, and this can often make bankruptcy an attractive option for those who see no other way of paying their debts.

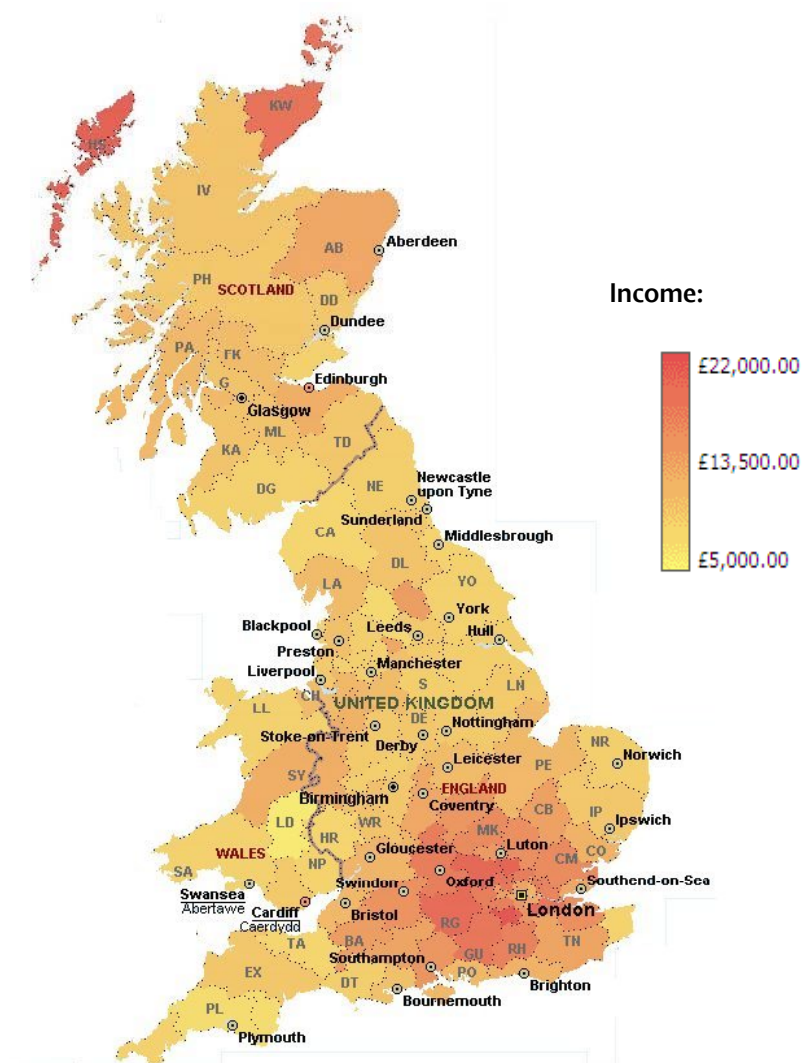
Where are the debt problems?

The map below shows the average incomes of clients who have been counselled by CCCS by their geographical location, grouped by postcode. The highest proportions of “middle class” debtors, where average incomes are highest, are almost exclusively found in the counties around London. The areas shaded in the darker oranges and reds are the postcode areas where clients’ average incomes are high.

The areas shaded in the lighter yellows are the postcode regions where clients’ average incomes are lower, as indicated by the key. These areas are primarily in the North of England, Wales, Scotland and the South West of England.

A possible explanation for the North-South divide seen in the map below could lie with house prices. While these have increased all over the UK, the increase has been most marked in the South. This may have led to people taking on mortgages which entailed large payments to be made each month, eating away at disposable income. People may have turned to credit to bridge the gap between their incomes and their outgoings.

In the yellow areas, average incomes are very low. Again, it is likely that credit is being used as a bridge between incomes and outgoings, but where incomes are low, this is more likely to be for essential subsistence needs than because the client has a large housing payment to make.



Summary

- Clients with incomes of more than £30,000 have average debts of £69,737
- 4.7 per cent of CCCS clients have a net household income of more than £30,000
- Only a third of clients with incomes over £30,000 have no children
- The average debt to income ratio for clients with incomes of more than £30,000 is 1.9
- The South East is the most common place for “middle class” debt

- Clients with incomes of less than £10,000 a year have average debts of £20,316
- 20 per cent of CCCS clients have a net household income of less than £10,000
- Over 50 per cent of clients earning less than £10,000 a year have no children
- The average debt to income ratio for clients with incomes of less than £10,000 is 3.3
- Clients with net incomes of less than £10,000 are likely to live in Wales, Southern Scotland, Northern and South West England