Debt and social misery: the flipside of Britain's financial services boom

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Amid the hoopla, bonuses and champagne swigging that characterises Britain's booming financial services industry, a picture is emerging of the financial plight and social misery facing millions of families in thrall to the banks, credit agencies and loan sharks.

The burgeoning profits of the financial sector are bound up with the ever-increasing emiseration of workers and young people. Recently published reports and the BBC One TV series "The Whistleblower" testify to the growing problem of indebtedness and its impact on families.

According to a survey published by YouGov for the debt management agency Thomas Charles, more than one million people could be on the verge of bankruptcy. One in five adults—eight million people—has unsecured debts of more than £10,000 (US$17,000), and 1.7 million people often struggle to keep up with debt repayments, with more than half of them having problems meeting their obligations every month.

Young people are by far the worst affected, with under-25s representing 61 percent of those with debts of between £10,000 and £30,000. More than a third of those surveyed said that debt was having an adverse effect on their health or relationships, while 8 percent said that it had made them clinically depressed.

Home repossessions rose by 70 percent last year, as house prices soared and people borrowed more than they could afford.

Record numbers of people are ringing help lines. The Citizens Advice Bureau (CAB) said that the number seeking help with debt management had doubled in the last eight years, and accounted for three quarters of the 1.25 million new debt cases that the charity dealt with every year. Young people and the elderly are particularly vulnerable. Women over 60 are the fastest growing group seeking advice.

The CAB's David Harker said that people were condemned to a "lifetime of poverty" burdened by debt. With average debts of £13,153, it could take on average 77 years for people asking the charity for help to clear their debts, as they were stuck in a spiral of very low incomes and high debts. Most were simply too poor to afford the fees to file for personal bankruptcy. Most of those seeking advice were on only half the national income.

According to the financial groups Defacto and Money Expert, one in five people in 2005 paid a penalty fee or charge on their credit cards or other financial products, including bank overdrafts, loans and mortgages, with one in 20 racking up charges of £100. Some 7.8 million people paid out the astonishing sum of £538 million in penalty charges last year.

The situation was particularly desperate after the Christmas bills came in. A staggering 23,351 people filed for bankruptcy or insolvency in the first quarter of 2006 in England and Wales—up 73 percent on the corresponding period last year. It is the highest quarterly number since records began being kept in the 1960s.

All this follows hard on the heels of the Bank of England's announcement that personal debt topped one trillion pounds in 2004. This means that personal debt is more than Britain's GDP.

It is debt that has kept the economy afloat thus far. But while overall debt levels are as high as in the late 1980s, it will take much longer to repay debt because of low inflation. The burden of debt is likely to curtail growth in consumer expenditure, the main engine of growth in Britain's economy.

Most of the debt is the £917 billion of secured mortgage loans, up from £784 billion in February 2004. A further £190 billion is unsecured debt via credit and store cards. It is the latter that has particularly driven the increasing insolvency rate, even though unsecured debt has fallen slightly in the last 12 months.

Mortgages have risen for several interrelated reasons. House prices have soared since the Labour government came to power in 1997. The rising property market—itself the product of the orgy of financial speculation in the City of London and the role of British tax exiles who have put their money into bricks and mortar—has created an affordability crisis, as average mortgage payments reach an unsustainable proportion of household income.

The cost of housing has driven more and more people to rely on credit and store cards for daily necessities simply to make ends meet, while the constant barrage of advertising for "must have" goods finds a ready market in young people trapped in low-paid dead-end jobs.

Personal debt has shot up over the last decade. While 10 years ago the average household had £2,500 of unsecured debt, now it has £7,600. Over the last 12 months, unsecured debt has risen more than twice as fast as average incomes. But much of the increase in personal debt is "distressed borrowing," with some people taking on more credit to help them repay existing loans.

The financial institutions are only too ready to assist. According to the *Guardian*, a recent study has shown that 90 percent of credit cards borrowers were issued cards without the lender checking whether they could afford to repay their debts.

Others, unable to keep up with their credit card and other personal debts, have "consolidated their debt and taken out additional mortgages to pay off their unsecured debt, setting the scene for the calamitous repossession of their homes if they fail to make their mortgage repayments on time." The newspaper continued: "Indeed, the collapse of households under the weight of debt repayments is accompanied by the return of forms of usury associated with a bygone era. TV commercials for debt consolidation and advisory services have become the advertising agencies' latest and most rapidly expanding business."

The flipside of the ever-increasing debts and repayments that workers and their families must pay is the obscene level of pay and profits being made in the City of London.

Earlier this year, HSBC, the third largest bank in the world, reported profits for 2005 of more than $20 billion, while Royal Bank of Scotland reported £8 billion, Barclays £5.2 billion, HBOS £4.7 billion and Lloyds TSB £3.35 billion.

The combined profits of the nine stock market listed banks come to £35 billion. When the Spanish bank Santander took over the UK's Abbey

National bank in 2004, its CEO said that profits from UK banks were three times the amount made by French banks and seven times the amount made by German banks.

At the same time, repeated surveys have found the UK banks to be the worst in Europe in terms of customer satisfaction—lower even than for door step salesmen, according to the National Consumer Council.

Whereas once the banks relied on overdrafts and loans to generate profits, now much of their business is derived from their own low-paid staff hard-selling the banks' products—mortgages, insurance, investments and credit cards—to account holders. According to the BBC's "Whistleblower" series on debt, the banks give their customers names like "revolver" and "transactor," depending on their spending behaviour, and target them accordingly with sophisticated marketing techniques.

It is not just the high streets banks that have fuelled the expansion of consumer credit, but also the insurance companies, supermarkets and car companies, many of which make a higher return on their financial services than they do their traditional business.

An unnamed senior banking executive told "The Whistleblower" that some banks had increased credit limits without customers' consent. She said, "Unsolicited increases in your credit limit can take place up to twice a year. In some cases, your credit limit could literally double in the space of two years."

In other cases, customers were invited into the bank to "review" their finances. This was often an excuse for a sales pitch. In the past two years, at least eight cases—almost certainly an underestimation of the real number—have been reported of people committing suicide when, due to their bank's irresponsible lending policy, their debts spiralled out of control.

The Thomas Charles study reported that more than 80 percent of those with debts of over £10,000 blamed the financial institutions for their indebtedness, feeling that the institutions had been irresponsible in making credit and loans available. Just this week, the *Financial Times* reported that the banks, after years of branch closures, are planning to open more branches on the high street. HSBC, for example, are planning to spend £100 million to open at least 50 new branches and refurbish a further 200. "Now, however, there is a realisation by banks that they need to become more like retailers and sell financial services products to customers," the FT said.

The new financial vultures that prey on the poor are now internationally well known names. According to Henry Palmer and Pat Conaty's report for the New Economics Foundation, *Profiting from Debt: Why Debt is Big Business in Britain*, there is a huge credit underground. This market was estimated to be worth £16 billion a year to the companies specialising in lending to the 8.3 million people systematically denied credit access to the mainstream banks, building societies and finance houses in 1999. It is far higher today.

The number of people exposed to "non-standard lenders" has risen in the last 10 years and is linked to the growth of "financial exclusion." A family resources survey found that three million British households had no access to a current account, a far higher rate than in other industrial countries.

In today's world, it is well nigh impossible to manage your financial affairs in a rational way without a bank account, a facility routinely denied to the poorest and most vulnerable in society. Financial exclusion has risen alongside the growth in the casualisation of the workforce, family and relationship breakdown, lone-parent households, and the legacy of the economic recession of the early 1990s that led to an increase in mortgage arrears, repossession actions and consumer credit debts, leaving hundreds of thousands of people facing court judgements.

The greatest levels of financial exclusion are to be found in Britain's former industrial centres: Glasgow, Newcastle, Manchester, Merseyside, Birmingham and South Wales.

Without access to mainstream credit, millions of people are condemned to a financial twilight zone, where interest rates on door step loans can be as high as 1000 percent, compared to the 5 and 17 percent APR (annual percent rate) on typical mainstream interest rates on credit cards or personal loans. Palmer and Conaty found effective interest rates as high as 1,834 percent.

These predatory lenders include the long-standing "alternative credit industry:" the licensed door step credit companies, also known as weekly collected credit or home credit, and pawnbrokers who operate virtually out of sight, as well as a host of new and virtually unregulated entrants onto the high street that employ a range of sophisticated and hard-sell tactics.

According to Datamonitor, the market research agency, the door step market is worth more than £3.3 billion a year, with customers borrowing an average of £1,000 a year. While a typical APR on a loan of £60 repayable over six weeks is 500 percent, much higher rates are not unusual. The worst problems arise when borrowers run into difficulties with repayments and are offered rollover loans to cover debts built up on their first loan.

The companies involved have enormous market power, as they have taken over their smaller rivals. Their financial rewards are correspondingly high. One company, Provident Financial, with 1.5 million customers, has more than 40 percent of the UK door step loans market and made £206 million in 2005.

Alongside all of this are the unlicensed and consequently illegal moneylenders. These are particularly rife in cities such as Glasgow, where poverty and social deprivation levels are high.

A new phenomenon is the rise of check cashing, where check cashers lend money to bridge the gap from one pay day to the next at an APR of about 400 percent.

Another is the spread of high street chains such as BrightHouse, formerly known as Crazy George's, which sell household goods and appliances on what appear to be competitive terms. But they set up shop in the poorest neighbourhoods, so that when many of their customers fail to pay up on time the rollover rates raise astronomically.

There has also been a huge rise in the number of "non-status lenders," who offer instant cash regardless of credit history for homes, cars and holidays. Such lenders will "consolidate" pre-existing debt against the borrowers' assets, typically their homes or cars, taking an ownership share in return. Having targeted people who will struggle to repay, they then seek a repossession order when the borrower, having paid heavy default penalties in effort to postpone the inevitable, fails to repay on time.

In the US, low-income homeowners are stripped of a staggering $9.1 billion a year through such tactics. While still new in the UK, court records show that the non-status lenders feature disproportionately high in repossessions. In east London, for example, 55-65 percent of repossessions are by such lenders.

The big financial institutions are not separate from all of this. Many well known corporations have been linked with the high-cost lenders, including Co-operative Insurance Services, the Thorn Group, Nomura Bank and Abbey National.

They have been aided by the Labour government, which has presided over and fostered the growth of the financial services industry at the expense of the vast majority of the population. Assisted by deregulation, in 2002 the financial services sector accounted for 5.3 percent of gross domestic product and the UK's surplus in financial services trade was £17.8 billion, the largest in the world and twice as high as Switzerland's, the next highest.

Britain has by far the highest rate of financial exclusion in northern Europe and by far the lowest standard of social protection. Despite this, the Labour government refused to place a statutory ceiling on interest rates in the recent Consumer Credit Act, preferring to consider instead only whether they might be "unfair."

Regulation through the courts and the Office of Fair Trading has been ineffectual. Despite hundreds of thousands of complaints lodged with the debt advisory services every year, only a handful of cases have come to court and even fewer have ended in convictions. The government has made no serious effort to widen access to affordable credit and has allowed the loan sharks to operate unchecked, making the UK one of the safest environments for predatory lending in the world.