



# Focus on *over-indebtedness*

## DEBT, BORROWING AND OVER-INDEBTEDNESS: A COUNTRY-LEVEL MONITORING FRAMEWORK

### LIVING ON CREDIT: THE NEW NORM?

Until the recent financial crisis, debt didn't feature in economic discussions, despite the rise in over-indebtedness over the past three decades. Debt is a double-edged sword: it can lead to both economic growth, and crisis and over-indebtedness. The thin line dividing these two outcomes is difficult to define, and measures to detect when precisely the tipping point occurs are imperfect. Indebtedness is a complex social and economic phenomenon that affects large numbers of people on a very personal level, and impacts their well-being and ability to contribute to society.

### PATHWAYS INTO OVER-INDEBTEDNESS

Getting into debt is easy, getting out of debt can prove difficult for many – and impossible to some. The many reasons why people become seriously indebted include:

- Reduced income while maintaining the same expenses, and spending beyond one's means
- Major negative life events such as divorce or death of the breadwinner
- Poor money management
- Underemployment
- Low savings levels
- Misleading marketing and toxic financial products
- Unsubstantiated optimism and irrational decision-making.

Whatever the reason, there are real consequences for households and society alike.

### LEVELS OF INDEBTEDNESS

Falling into over-indebtedness is a gradual process; individuals and households may be in and out of debt at various times, or fall deeper into debt until they become insolvent. These stages can be defined by look at an individual's financial situation, or at the ratio of debt repayments to overall income.

	Stage	Indicator
1	Financial constraint	Sense of debt burden, high debt-to-income ratio
2	Inability to make timely debt repayments	Mortgage arrears, using hire-purchase and other loans to keep afloat
3	Inability to cover living expenses	Arrears on rent or utility bills
4	Personal bankruptcy	Level of debt exceeds assets

The **Microfinance Centre (MFC)**, based in Warsaw, Poland, is a regional microfinance resource center and network. It brings together 103 organizations (including 78 microfinance institutions, or MFIs) in 27 countries of Central Europe and Asia, serving over 800,000 low-income clients. MFC's goal is to promote balanced MFI performance, create informed and capable financial consumers, and build strong institutions. To that end, it conducts research and analysis, contributing to thought-leadership, provides technical assistance on best practice, and collaborates with NGOs, private, bilateral and unilateral funders, and policymakers. For more information, visit [www.mfc.org.pl](http://www.mfc.org.pl) or contact us at [microfinance@mfc.org.pl](mailto:microfinance@mfc.org.pl).

It is nearly impossible to live debt-free, and the majority of people take on short-term debt, repaying it in a regular, predictable and timely fashion. Some people incur debt only occasionally, becoming “intermittent debtors” – while others (a minority) are permanently in debt, often living on the edge of personal bankruptcy and insolvency.

## WHY THE RIGHT MONITORING IS IMPORTANT

The need to monitor indebtedness in its various forms stems from the fact that debt has become a permanent feature of our economic lives. Rising debt levels partly reflect the reality that it often the only means to manage our finances. But more importantly, debt is a complex issue that permeates all aspects of our lives, and has profound consequences on our well-being and ability to function in society. It is fundamentally a human issue that impacts on our mental and physical condition, so we need to look beyond “impersonal statistics” and “hard numbers” to understand the impact of debt on society.

When we do so, we can consider debt not just in terms of the individual financial debt burden, and macro-level debt burden, but also as a broader social and economic condition. Beyond measures and analysis of the size, scope and incidence of excessive debt, we can achieve a deeper analysis of the wider consequences of over-indebtedness and impoverishment, especially for low-income people who more prone to falling into the debt trap.

## WHAT IS “DEBT WATCH”?

A proposed new “Debt Watch” could systematically review policies, actions and gaps in addressing over-indebtedness. This will be an independent and impartial body, ensuring that it provides an objective point of view, and maintains the autonomy to voice concerns that may politically unacceptable or socially unpopular within a particular context.

## WHO

Debt Watch could be managed either by an independent consumer rights organization, or as a separate body – either formally organized, (for example as an EU-wide body), or as an ad-hoc body that is evoked to conduct the annual watchdog

function. Either way, its credibility and success will depend on both its independence and political neutrality.

## WHAT

The scope of the Watch should be comprehensive, covering all aspects of the indebtedness issue:

- Policies
- Definitions and measures
- Data on indebtedness
- Financial products and services
- Market conduct of lenders
- Education and advocacy
- Public information
- Economic and social consequences of debt.

## HOW

Monitoring would involve various techniques, including policy assessment, surveys and research studies, as well as social media analysis to understand the full scope of the problem of indebtedness in a society. It should be a cross-disciplinary body: uniting lawyers, economists, sociologists, educators, and advocacy experts to create a comprehensive map of indebtedness. Its findings should be widely communicated through the media, and used by policy makers to inform the development of social programs.

## EU-WIDE COLLABORATION

Once established on a country level, Debt Watch could become an EU-wide collaborative platform to encourage professional cooperation, as well as the exchange of methodologies, research experience, and results. Doing so would enrich our knowledge and understanding of indebtedness issues, especially in relation to the most vulnerable groups, and help us improve the effectiveness of policies and activities designed to mitigate the negative consequences of over-indebtedness.



*This publication has been produced with financial support from the European Union. The contents of this publication are the sole responsibility of the Microfinance Centre and can in no way be taken to reflect the views of the European Union.*