NBB Conference 2022: Household Heterogeneity and Policy Relevance Session 3 – Household Finance

Brussels, 21st October 2022

Over-indebtedness and poverty: patterns across household types and policy effects

(by Sarah Kuypers and Gerlinde Verbist, Universiteit Antwerpen)

Discussant: Olga Cantó (Universidad de Alcalá & EQUALITAS)

MAIN AIM OF THE PAPER & CONTRIBUTIONS TO THE LITERATURE

Main objective of the paper

Propose measure over-indebtedness + study relationship with poverty in Belgium, using data from the HFCS

Main contributions of the paper

- 1) What is the relevance of debt repayments in the measurement of living standards?
- 2) How important is it to consider potential leverage through the ownership of assets?

Using more dimensions of poverty: incidence, intensity and inequality

Accounting for wealth heterogeneity across households

Evaluate two potential policy reforms in Belgium that include debt repayments in social policy design

WHY SHOULD WE BE WORRIED ABOUT OVER-INDEBTEDNESS?





- IT, JPN, NL, NO, SVN, ES, SÉ, CH, USĂ, LVA.
- Most developed countries have increased household debt substantially (peaking 2007/2008) and remaining high afterwards (OECD, 2017) : 53% GDP in EU and 65% GDP in Belgium
- At the micro level: financial difficulties lower current standard of living, debt payment default risk, psychological health impact (increasing levels of stress, depression and anxiety in population), physical health impact (postponement of health treatments)
- At the macro level: financial system instability (weakening banks' balance sheets), tightening margin and conditions new loans, reduction in credit accessibility, reduction of aggregate demand (fall in employment and growth prospects).

MEASURING OVER-INDEBTEDNESS: RELEVANT ISSUES

- No scientific consensus in its measurement: not just the "inability to meet financial obligations" (economic dimension)
- Is it a multidimensional phenomenon?
 - Dimensions: economic, temporal (long-term structural problem), social (financial and social exclusion), psychological (severe stress)
- A variety of indicators:
 - Administrative (number of people on debt settlement)
 - O Objective indicators: **capacity to repay** (debt-to-income ratio, debt-to-asset ratio, debt-service-to-income, number of loans)
 - Subjective indicators (debt repayments a heavy burden, difficulties to make ends meet, unable to face unexpected expenses)

C The authors propose objective indicators that aim to measure "capacity to repay" by measuring the gap between household disposable income after debt repayments and the poverty line. Authors also consider the role of asset ownership in possible leverage (joint income-wealth). They extend previous approaches for Belgium (Carpentier and Van der Bosch, 2008) by considering over-indebtedness intensity and inequality within the over-indebted

MEASURING OVER-INDEBTEDNESS: QUESTIONS & COMMENTS (I)

- If over-indebtedness is a multidimensional phenomenon, why stick to the strictly economic dimension? Why not consider a multidimensional approach to measurement similar to economic insecurity literature? Should be not look into both objective and subjective issues (implies changes attitudes so affects aggregate demand and economic instability)?
- Not clear if mortgage debt repayments are included within debt repayments. If included, a discussion on the comparative treatment of renters is due
- Very relevant within objective indicators is how to undertake additional methodological choices :
 - Thresholds: 60% of median income? 30-40%-50% of household total income? Why not use income and annualized wealth? when does indebtedness become a problem?
 - Income concepts included (related to life risks): expected social security (pensions) income? expected unemployment transfers? expected coverage of risks?
 - Time period measure of all variables: monthly? yearly? longer?
- Not considering asset ownership ignores household heterogeneity, but during recessions converting real assets into liquid is difficult and asset value generally falls
- Not clear how asset (different from main residence) buffer works: is it a one shot compensation of one year of debt repayment or does is consider a wider time period to compensate debt repayments?

MEASURING OVER-INDEBTEDNESS: QUESTIONS & COMMENTS (II)

- The use of FGT indices to measure over-indebtedness in three dimensions: incidence, intensity and inequality is very interesting and is one of the clear advantages of the approach proposed, however, it is not clear what authors mean by "poverty intensity" in the interpretation of the FGT(2)
- It would be very interesting to decompose these indices into incidence H, mean intensity I and inequality over the overindebted CV². Moreover, a TIP curve to analyse over-indebtedness could also be constructed
- It is very difficult to understand the different specifications of "capacity to repay" considered (a to g), a clearer explanation is due here
- Over-indebted households are:
 - those over the poverty line (60% median income) that become poor when subtracting debt payments and considering assets as leverage
 - those below the poverty line (60% median income) but who increase their poverty gap when subtracting debt payments and considering assets as leverage
- Problem: individuals with small debt payments may be considered as over-indebted if they cross the poverty line. The threshold to determine over-indebtedness may be better if taking an individual perspective, not in a social one. In fact, debt-to-income and debt-service-to-income are individually referenced indicators

OVER-INDEBTEDNESS AND POVERTY & POLICY SIMULATIONS: QUESTIONS & COMMENTS

- Poverty-based over-indebtedness indicators proposed use a social threshold (60% median income) to determine who belongs to the group, this is essentially different from any other over-indebtedness indicator that considers an individual threshold, maybe a double threshold approach would be interesting in this context
- Why not consider first over-indebtedness and poverty (considering debt repayment and asset leverage) as separate risks and analyse the classification of individuals in these two related risks (cause and consequence of each other)?
- In the first reform, when including debt repayments in the means-test of social assistance benefits: we are assuming that any household can turn assets into liquid easily? May this be also heterogeneous (e.g. by urban/rural areas)?
- O In the first reform it would be interesting to consider what would the implications be of a double threshold: an income one and an asset one instead of a change in the means-test. Does the change in the means-test not promote further debt increases?
- In the second reform, may transfers related to payments of non-mortgage debt or arrears promote more debt? moral hazard? Is there any conditionality in receiving these transfers? Why are mortgage payments excluded?

NBB Conference 2022: Household Heterogeneity and Policy Relevance Session 3 – Household Finance

Brussels, 21st October 2022

Over-indebtedness and poverty: patterns across household types and policy effects

(by Sarah Kuypers and Gerlinde Verbist, Universiteit Antwerpen)

Discussant: Olga Cantó (Universidad de Alcalá & EQUALITAS)