The financial position of British households: evidence from the 2016 NMG Consulting survey

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- The improvement in mortgagors' balance sheets that has taken place since the financial crisis has not continued. But debt servicing costs remain relatively low by historical standards.
- The 25 basis point cut in Bank Rate that was announced in August has been passed through to lower mortgage costs for many variable-rate borrowers.
- There has been a small deterioration in households' expectations for future income and spending growth.

Overview

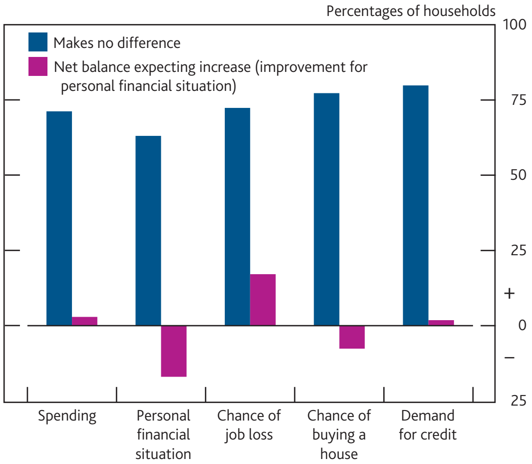
In June 2016, the United Kingdom voted to leave the European Union. This was followed in August by the Monetary Policy Committee's decision to cut Bank Rate by 25 basis points to 0.25% and to introduce a further package of policy-easing measures. Evidence from the latest NMG survey of households, collected over the first three weeks of September, can provide an insight into how households have been affected by these events.

How households react to these developments will, in part, depend on the state of their balance sheets. Households' balance sheets have improved since the financial crisis, and while evidence from the latest survey suggests that this improvement may have come to an end, the share of households with high mortgage debt servicing costs is low by historical standards.

The survey suggests that the August cut in Bank Rate had already been passed through to lower mortgage costs for many borrowers. But when asked about how they might respond to a hypothetical further fall in mortgage payments, households reported that paying off debt and saving more were likely to be a more common response than increasing spending.

Households reported that the EU referendum result had only had a modest impact on their finances (**summary chart**). There had been little sign of a change in credit demand and no large rise in uncertainty. But there had been some softening in households' expectations for their personal financial situation and income. Consistent with that, households had revised down their expectations for house price growth.

Summary chart The impact of the vote to leave the European Union on households[(a)]



Source: NMG Consulting survey.

(a) All questions refer to the next twelve months. See footnotes to **Charts 10**, **12**, **14** and **16** for more details on the questions.

Introduction

The outcome of the referendum on EU membership in June 2016 is likely to be associated with a period of significant uncertainty about the UK economy. Immediately following the vote, economic activity was expected to weaken. In light of that, the Monetary Policy Committee (MPC) introduced a package of policy measures in August 2016. Since then indicators of activity and business sentiment have generally recovered from post-referendum lows. The latest household survey carried out for the Bank by NMG Consulting was focused on assessing the impact of both the referendum outcome and monetary policy stimulus on the household sector.

Household-level data provide information about people's perceptions of the impact of these events and allow analysis of how different groups have been affected and how they may respond.

Assessing the impact of the referendum is important for both monetary and financial stability. From a monetary policy perspective it is important to understand if and how aggregate spending might be affected by households' expectations of future income, credit conditions, inflation and interest rates. For financial stability, changes in indebtedness and income can alter the resilience of households' balance sheets, affecting the likelihood that shocks are amplified through, for example, arrears on debt or sharp contractions in spending.

The NMG survey is a now biannual household survey commissioned by the Bank. The motivation for the survey is to gather timely microdata on households' finances and to investigate topical policy issues where there is limited information available from other sources. The latest survey was conducted between 31 August and 19 September. It covered approximately 6,000 households and was carried out online. This article analyses the results. The box on pages 194–195 provides more detail on the survey method.

The survey contained questions on a number of topics. These included: the latest developments in balance sheet positions, the impact of lower interest rates, credit conditions, and households' views on the housing market, uncertainty and expectations for spending.

The article begins by providing an overview of the latest developments in household balance sheets and a summary of indicators of financial distress. This sets the backdrop for an assessment of the extent to which households had been affected or expected to be affected by the recent cut in Bank Rate. Next, it investigates how households viewed the outlook for credit conditions and house prices. Finally, it reviews measures of household uncertainty and what these may mean for consumer spending.

Developments in balance sheets

In the aggregate National Accounts data, household debt grew broadly in line with income over the year to 2016 Q2, with unsecured debt growing more rapidly than secured credit. In the NMG survey average income rose by 1.4% compared to the 2015 H2 survey, but the average outstanding mortgage, for those that had one, was broadly flat at around £85,000, while the average unsecured balance remained in the region of £8,000. The main discrepancy between the latest survey and aggregate data is that the NMG survey does not appear to pick up the recent strength of unsecured lending, which has been growing at close to 10% a year in the aggregate data. Any analysis of the survey data relating to unsecured debt must be considered with that in mind.

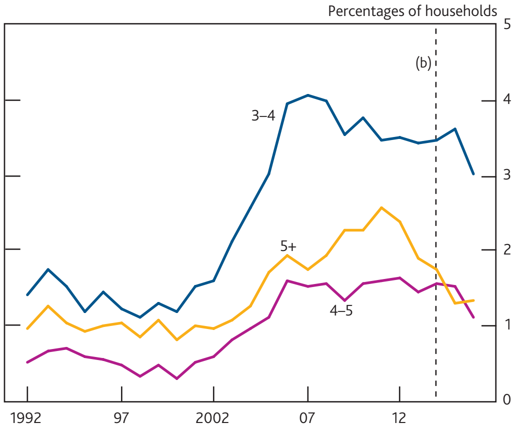
Two of the key indicators for assessing the sustainability of balance sheets for households are the debt to income (DTI) ratio and the debt-servicing ratio (DSR), which is the proportion of income spent on loan repayments (both capital and interest). For both indicators, a higher ratio is typically associated with an increased risk of financial distress, particularly if incomes were to fall or repayment costs were to rise.

Over recent years, the number of households with high mortgage DTIs and high mortgage DSRs has been gradually falling (**Charts 1** and **2**). The latest NMG survey suggests that, on some measures, this improvement has come to an end. The proportion of mortgagors with debt to income ratios above 5 was broadly unchanged on the year, having roughly halved since 2011 (**Chart 1**). But there was a fall in the share of households with a mortgage debt to income ratio between 3 and 5. The share of households with mortgage DSRs above 40% rose slightly in the latest survey while the share with DSRs between 30% and 40% was broadly flat (**Chart 2**). Stepping back from the changes over the past year, the share of households with high mortgage DSRs is low in historical terms, although that should be viewed in the context of interest rates being at historically low levels.

Taking into account unsecured loans, where balances are typically small relative to mortgages but repayments can still be sizable, there has been a fall in the share of households with a total DSR above 40% (**Chart 2**). But this must be interpreted with some caution given that the latest NMG survey appears to underrecord the recent growth in unsecured credit.(1)

(1) There is additional uncertainty around unsecured credit data from the 2016 H2 survey due to a change in the phrasing of a question on credit cards — see the box on pages 194–195 for more details.

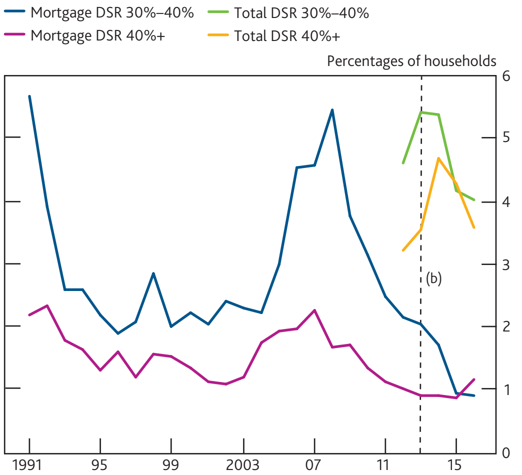
Chart 1 Distribution of mortgage DTIs(a)



Sources: Living Costs and Food (LCF) Survey, NMG Consulting survey and Bank calculations.

(a) Ratio of outstanding mortgage debt to pre-tax annual income.
(b) Data up to 2014 are based on responses to the LCF Survey. Data from 2015 onwards are based on responses to the NMG Consulting survey and have been spliced onto the earlier LCF Survey data series in 2014. NMG data are from the H2 surveys only. NMG data before 2015 have been adjusted for a change in the income definition.

Chart 2 Distribution of DSRs(a)

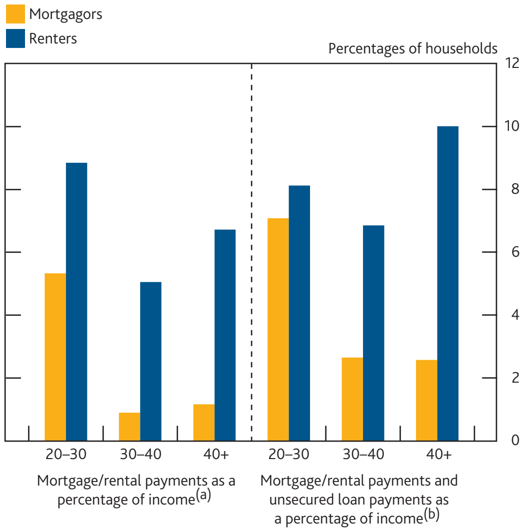


Sources: British Household Panel Survey/Understanding Society (BHPS/US), NMG Consulting survey and Bank calculations.

(a) The mortgage DSR is calculated as total mortgage payments (including principal repayments) as a percentage of pre-tax income. The total DSR is calculated as total mortgage and unsecured debt payments (including principal repayments) as a percentage of pre-tax income. Reported repayments may not account for endowment mortgage premia.
(b) Mortgage DSR data up to 2013 are based on responses to the BHPS/US survey. Data from 2014 onwards are based on responses to the NMG Consulting survey and have been spliced onto the earlier BHPS/US survey data series in 2013. NMG data are from the H2 surveys only. All total DSR data are from the NMG survey. NMG data before 2015 have been adjusted for a change in the income definition.

Households who rent their accommodation currently spend considerably more of their income on accommodation payments than mortgagors. A new question on rental payments that has been introduced into the survey means that a rental service ratio (RSR) — the proportion of income spent on rental payments — can now be constructed. Consequently, it is possible to draw comparisons with mortgage DSRs, although the metrics are not completely equivalent. Rents should reflect the full value of the property and will factor in costs to landlords such as maintenance costs, whereas a mortgage will only capture the cost of the part of the property that was financed by borrowing. Renters and mortgagors constitute 36% and 30% of all households respectively. But renters with an RSR above 30% make up 12% of all households, while only 2% of households are mortgagors with a mortgage DSR greater than 30% (**Chart 3**). When repayments for unsecured loans are factored in, 17% of all households are renters spending more than 30% of their income meeting accommodation and debt costs, compared with 5% for mortgagors.

Chart 3 Housing costs and DSRs



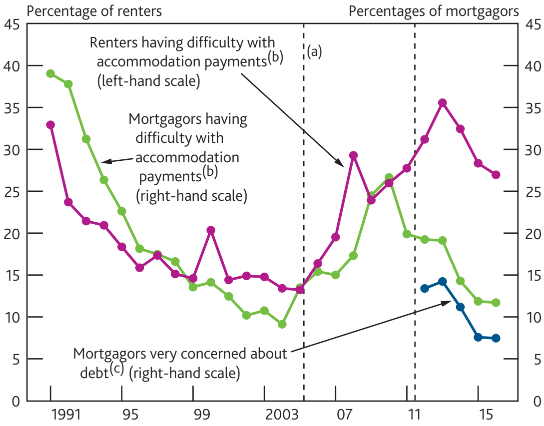
Sources: NMG Consulting survey and Bank calculations.

(a) Calculated as mortgage DSR for mortgagors, as described in the footnote to **Chart 2**. RSR for renters is calculated as total rental payments as a percentage of pre-tax income.
(b) Calculated as total DSR for mortgagors, as described in the footnote to **Chart 2**. Ratio for renters is calculated as rent plus unsecured debt payments (including principal repayments) as a percentage of pre-tax income.

The fact that rents tend to account for a higher proportion of incomes than mortgage payments does not necessarily translate into bigger risks to financial stability. Renters do not pose direct credit risk to banks if they struggle to pay their rent, although indirectly, rental arrears may impact on landlords' ability to service buy-to-let mortgages.

Indicators of current financial distress from the NMG survey also point to a mixed picture for household balance sheets over the past year. The survey contains a number of subjective questions asking whether accommodation or debt-servicing costs are manageable. The share of households reporting difficulties in servicing their mortgage debts appear to have levelled off in the latest survey having fallen in recent years (**Chart 4**). The proportion of renters reporting difficulties in meeting accommodation costs has fallen a little, but in line with the new data on RSRs this figure is significantly higher than for mortgagors. The characteristics of renters are likely to influence this result: for example, both private and social renters tend to have lower incomes than mortgagors and they may have more limited opportunities to save.

Chart 4 Measures of financial distress



Sources: NMG Consulting survey and Bank calculations.

(a) Data from 2011 onwards are from the online NMG survey. NMG data are from the H2 surveys only. Data from 2005 to 2010 are from the face-to-face NMG survey. Data from 1991 to 2004 are from the BHPS. Data from the BHPS and face-to-face NMG surveys have been spliced to match the online NMG survey results.
(b) Question: 'Many people these days are finding it difficult to keep up with their housing payments. In the past twelve months would you say you have had any difficulties paying for your accommodation?'.
(c) Question: 'How concerned are you about your current level of debt?'.

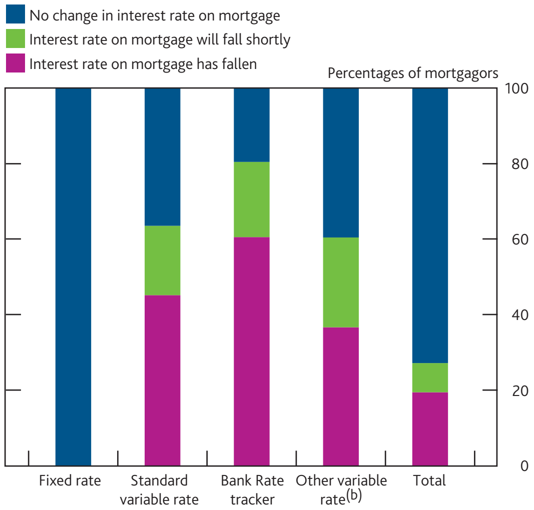
Impact of lower interest rates

At its August policy meeting, the MPC announced a package of policy-easing measures designed to provide additional support to growth and to achieve a sustainable return of inflation to the target. This package comprised: a 25 basis point cut in Bank Rate to 0.25%; a new Term Funding Scheme to reinforce the pass-through of the cut in Bank Rate; the purchase of up to £10 billion of UK corporate bonds; and an expansion of the asset purchase scheme for UK government bonds of £60 billion, taking the total stock of these asset purchases to £435 billion.

The cut in Bank Rate is likely to have affected many households with floating-rate mortgages relatively quickly. In the latest NMG survey, around 40% of mortgagors reported that they had floating-rate contracts. Roughly half of those households said that their payments had already fallen when the survey was conducted in the first three weeks of September, with a further 20% having been notified of a change to come. Taking into account households on fixed-rate mortgages too, who would only see their payments change once they refinance, around a quarter of all mortgagors had or were about to see their mortgage payments fall at the time of the survey (**Chart 5**).

Households have also revised down their expectations for Bank Rate (**Chart 6**). These expectations continue to track financial market expectations closely. At the time of the survey, the median household expected no increase in Bank Rate over the next year and a rise of only 0.25 basis points by September 2018.

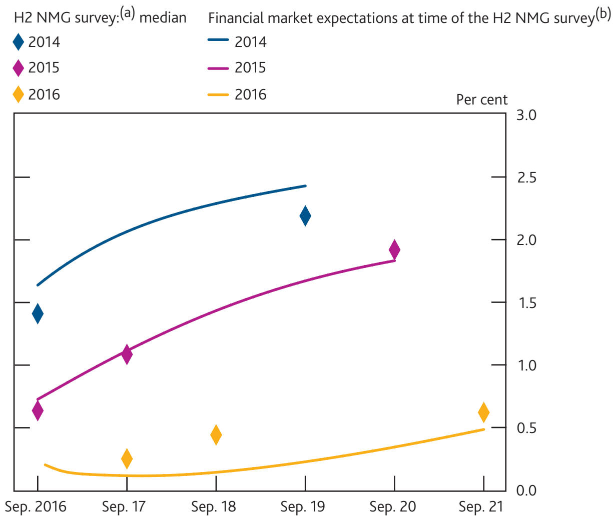
Chart 5 Households affected by lower Bank Rate[(a)]



Sources: NMG Consulting survey and Bank calculations.

(a) Question: 'The Bank of England Base Rate was lowered in August from 0.5% to 0.25%. Has the interest rate you pay on your mortgage fallen as a result or have you been notified that it will fall shortly?'.
(b) Mortgages where the interest rate is discounted or capped.

Chart 6 Households' expectations for Bank Rate

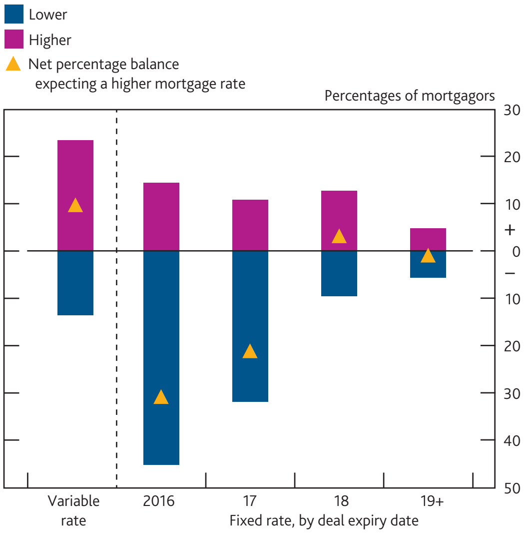


Sources: Bloomberg, NMG Consulting survey and Bank calculations.

(a) Question: 'The level of interest rates set by the Bank of England (Bank Rate) is currently 0.25% (0.5% in 2014 and 2015 surveys). At what level do you expect that interest rate to be in each of the following time periods? One year from now/two years from now/five years from now?'.
(b) Forward curve estimated using overnight index swap rates during the period which the respective surveys were conducted over. Forward curves constructed in this way are likely to reflect a measure close to the mean expectation of financial market participants.

There were also some interesting differences in expectations for their own mortgage rates among households. While a majority expected no change over the next year, those with a fixed-rate mortgage (around 60% of mortgagors), particularly those whose current deal expires in 2016 or 2017, expected their mortgage rate to be lower in a year's time than it was when they completed the survey. As many of the households with floating-rate mortgages had already seen a fall in their mortgage repayments, most of them expected no change in the next twelve months, but a small net balance expected an increase (**Chart 7**).

Chart 7 Households' expectations for their own mortgage rates in a year's time[a]



Sources: NMG Consulting survey and Bank calculations.

(a) Question: 'In 12 months' time do you think the interest rate you pay on your mortgage will be higher or lower than it is now/the rate you have been notified you are about to pay? Please assume everything else about the mortgage will stay the same — ie the amount borrowed, the length of the mortgage'.

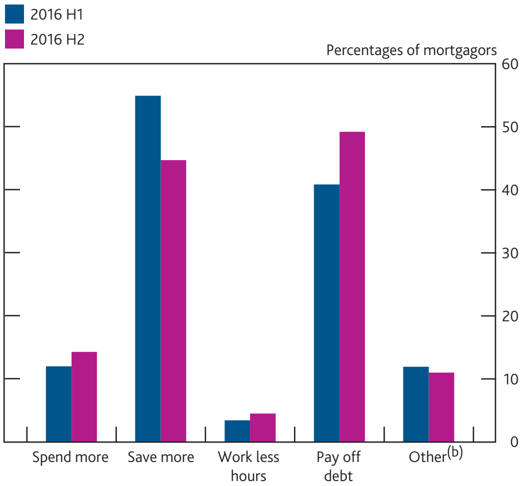
Economic theory suggests that a fall in interest rates should lead to higher household spending: because lower returns on savings decrease the amount of future consumption that can be achieved by sacrificing a given amount of spending today, lower rates make spending more today more attractive. Higher spending in the economy also has a second-round effect of raising incomes, for example by reducing unemployment and boosting wages, which supports spending further.[1]

In addition, falls in interest rates redistribute money from savers to borrowers. If borrowers increase spending by more than savers reduce it in response to lower interest payment and receipts, that also boosts spending via a cash-flow effect.

The survey did not specifically ask households how they had responded to the recent cut in Bank Rate. But it did ask mortgagors with a current mortgage rate above 1% how they would respond to a hypothetical further 1 percentage point reduction in mortgage rates, where they were told by how much their own mortgage payment would fall in cash terms, based on responses to earlier questions in the survey.

Respondents reported that paying off debt and saving more were likely to be a more common response to lower mortgage payments than increasing spending (**Chart 8**). Just over 10% of mortgagors said that they would increase spending in response to lower mortgages rates. Around 50% indicated that they would use the money to pay off debt with 45% planning to save more (multiple responses were allowed). These are similar to the responses given to the same question in the April survey.

Chart 8 Mortgagors' expected responses to lower interest rates[a]



Sources: NMG Consulting survey and Bank calculations.

(a) Question: 'Mortgage rates on new loans have fallen recently. If your monthly mortgage payments were to fall by £x [which is calculated automatically from software as the payment decrease under a 1 percentage point fall in interest rates] for a sustained period from tomorrow, how do you think you would respond? Please assume your income would not change unless you take action to change it'. Households were allowed to select up to three options.
(b) Includes leave paid employment myself, someone else in my household would leave paid employment, give financial help to family/relatives, move to a more expensive property and other.

Households who stated that they would increase their spending in response to lower mortgage rates were asked by how much they would raise spending. This allows a marginal propensity to consume (mpc) to be calculated. When weighted by their net borrowing, the average mpc of borrowers from lower rates was 0.15, implying that they would increase spending by 15 pence for every pound that mortgage payments fell. This is lower than the mpc of around 0.5 estimated from previous surveys of how borrowers would adjust spending in response to *higher interest rates*.[2] This asymmetry in mpcs is consistent with responses to questions on how households say that they have responded to more general income shocks in previous surveys, although it could also reflect how the question was framed or a desire from households to appear financially responsible in their answers.[3]

One possible explanation for the relatively low reported mpc of mortgagors in response to *lower rates* is that, for some households, a reduction in interest payments would only work to offset other factors that are holding back spending; that is lower mortgage payments might lead some households to reduce spending by less than they *otherwise would*, but they still would not increase it in absolute terms. There is some tentative evidence to support this, with mortgagors who were expecting to increase spending over the next year reporting higher mpcs, in the region of 0.25, larger than for those who planned to decrease spending (**Table A**).

(1) See Cloyne, Ferreira and Surico (2016) for more detail.
(2) For more detail on the survey questions on higher interest rates see Anderson *et al* (2014) and Bunn *et al* (2015).
(3) See Bunn *et al* (2012) for more information on spending responses to income shocks.

Survey method

Introduction and method

The latest NMG survey was carried out online between 31 August and 19 September, covering 6,011 UK households. The survey has been carried out bi-annually since 2014, with the field work taking place in April and September every year. The survey was conducted annually, usually during September, between 2004 and 2013. The survey has been run online since 2012, following pilots in 2010 and 2011. Before that, the survey was conducted face-to-face.

Moving the NMG survey online facilitated the introduction of a panel element where the same households were asked to respond to successive surveys. Around 65% of the respondents to the latest survey had completed a previous survey. Unless otherwise stated, this article reports results from the full set of cross-sectional data and not just the panel element.

The NMG survey has a number of advantages relative to other household surveys. It is more timely than other surveys, such as the Wealth and Assets Survey, where results are typically available only around two years after the completion of the field work; it may be better at measuring financial distress by virtue of being conducted online where respondents are more willing to disclose sensitive information about their finances; and it contains questions on topical policy issues that are not often available in other surveys.

A drawback of the NMG survey is that there may be a greater risk of selection into the survey based on unobservable characteristics than is the case for some other household surveys. The survey is weighted to be representative of the age, gender, region, housing tenure and employment status distributions of Great Britain. However, because the sample is drawn from the Research Now panel used by the survey provider rather than the population as whole (which is typically the case for surveys conducted by the ONS) there may be a risk that certain types of people are more likely to respond to online surveys and be part of that panel, which could bias the results. However, even when the probability of being invited to complete the survey is known, certain types of households may still be more or less likely to respond. The NMG survey data do follow broadly similar trends to the aggregate data and other surveys in most respects and so are still likely to be a useful source of information on distributional issues given the advantages described above.[(1)]

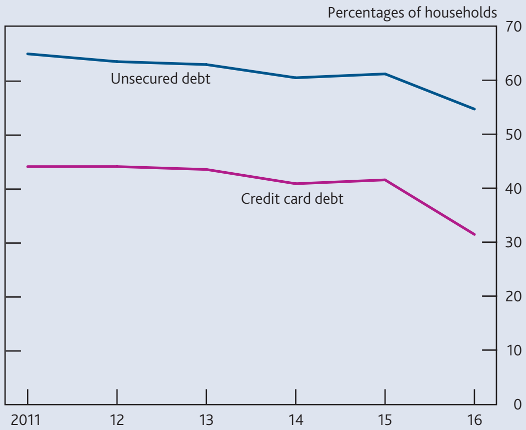
Different approaches to asking about household income

The main methodological change introduced in the latest survey was around how households were asked to report their incomes. This year, all respondents were asked about the income of each household member separately instead of being asked for just the total household income. This followed a successful test for half of the sample in 2015.[(2)] While this change should help to improve the accuracy of the survey over the longer term, it does introduce some difficulty when making year-on-year comparisons. Where possible, this article uses data from the 2015 survey — that had both versions of the income question — to adjust back-data to make comparisons more consistent with results from the latest survey.

Different approaches to asking about consumer credit

A smaller change in the latest survey was around how households were asked about their balances of consumer credit. The wording of the questions in relation to unsecured debt was changed to try to ensure that the responses did not capture credit card balances that were paid in full at the end of every payment period. Previous surveys asked households to exclude these balances as well, but analysis of extra questions on credit cards introduced in the 2015 survey revealed that some respondents may be misreading the questions and reporting that they used credit cards as a source of credit even if they paid the balances off in full at the end of every payment period. The wording in the September 2016 survey was made more explicit and additional pop-up boxes were introduced to help ensure the correct interpretation of the question.[(3)]

Chart A Percentage of households with unsecured debt and credit card debt[(a)]



Sources: NMG Consulting survey and Bank calculations.

(a) Data are from H2 surveys only.

(1) For further details see Anderson *et al* (2016).
(2) For a more detailed discussion of this change see Bunn *et al* (2015).
(3) When being asked what types of unsecured debt they hold, respondents were previously told 'For credit and store cards, please exclude any balances that you expect to repay in full on the next payment date'. But in the latest survey those who reported that they had this type of debt were then shown a pop-up box saying 'If you have credit card borrowing which you do not expect to pay off in full (for example if you only pay off the minimum each month) then leave the box ticked', and were asked to confirm whether their original answer was correct.

This change to the question wording has reduced the proportion of households who reported that they have credit card debt. This fell to around 30% of households in the September 2016 survey from around 40% in April (**Chart A**). Consequently, the share of households reporting any type of unsecured debt also fell, from 61% to 55%. This should help to improve the accuracy of the survey but does need to be taken into consideration when making year-on-year comparisons with these data. It may be contributing to the NMG survey underrecording the growth of unsecured debt over the past year relative to aggregate data, but is unlikely to be able to account for all of that discrepancy.

Table A Mortgagors' marginal propensities to consume out of lower interest rates by spending intention for next year[(a)]

Spending intention for next year	Estimated marginal propensity to consume
Increase a lot	0.22
Increase a little	0.26
About the same	0.13
Decrease a little	0.09
Decrease a lot	0.01
All mortgagors	0.15

Sources: NMG Consulting survey and Bank calculations.

(a) Calculation is based on the question described in the footnote to **Chart 8** and the following question that was asked to respondents who reported they would increase spending, 'How much would you increase your monthly spending by in this situation?'. The marginal propensity to consume is calculated as the reported change in spending as a share of the change in interest payments. Respondents who reported that they would not change spending were given an mpc of zero. Results are weighted by net debt (outstanding mortgage and unsecured debt less deposits). Data from 2016 H2 survey only.

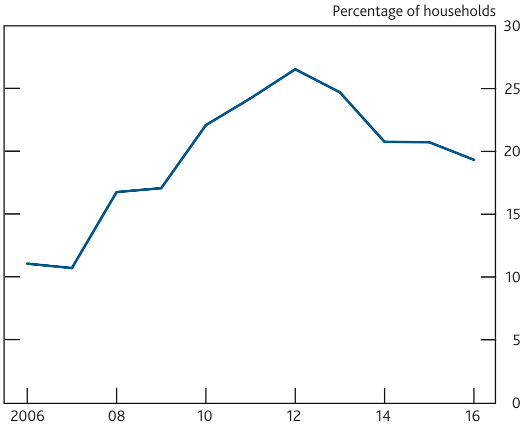
Savers were not asked how they would respond to lower interest rates. That was because the survey does not collect data on the interest rates on savings accounts and because many of those interest rates are likely already to be very low. Not having data on how savers would respond to *lower rates* means that an estimate of the cash-flow effect on aggregate spending from lower interest rates cannot easily be calculated. But if the mpc for savers were similar to the 0.1 estimated from previous surveys on their response to *higher rates*, that would mean that the cash-flow effects from *lower rates* implied by this hypothetical exercise would be relatively modest. Although, as was discussed above, this is only one of a number of ways in which changes in interest rates can affect spending.

Credit conditions

One of the purposes of the policy package announced on 4 August 2016 was to ensure that credit conditions remained supportive of economic growth. In the latest NMG survey, the proportion of households who perceive that credit availability has been a constraint on spending was marginally lower than a year ago at just under 20% (**Chart 9**). That is consistent with the results of the Bank's *Credit Conditions Survey*, where lenders reported they expected credit availability to remain broadly unchanged.[(1)]

The survey also included direct questions about the perceived impact of the vote to leave the European Union on credit availability and the demand for credit. Most respondents

Chart 9 Credit availability as a constraint on spending[(a)]



Sources: NMG Consulting survey and Bank calculations.

(a) Question: 'Have you been put off spending because you are concerned that you will not be able to get further credit when you need it, say because you are close to your credit limit or you think your loan application would be turned down?'. Data from H2 surveys only. Results from 2006 to 2010 are from the face-to-face survey. Results from 2011 onwards are from the online survey.

thought that the Leave vote would not have an impact on credit availability, although at the margin slightly more respondents thought that credit conditions would become tighter. Around 80% of respondents also thought that the Leave vote would not change their intention to borrow (**Chart 10**).

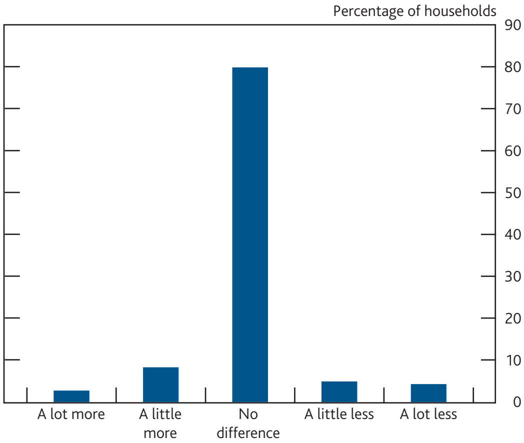
Housing market expectations

Immediately following the EU referendum, aggregate data on the housing market continued to soften. Mortgage approvals, a leading indicator of housing transactions, fell back relative to the first half of the year and annualised growth in the average of the Halifax and Nationwide house price indices slowed to 2.5% in the three months to September from 4.6% in the three months to June.

Evidence from the NMG survey suggests that households' expectations for house price growth over the next year have fallen (**Chart 11**). The mean expectation for house price inflation over the next twelve months fell to 0.7% in the latest survey, down from 2.2% in the first half of the year. That fall in expectations for house price inflation is consistent with

(1) For more detail see *Credit Conditions Survey 2016 Q3* available at www.bankofengland.co.uk/publications/Documents/other/monetary/ccs/2016/16q3.pdf; and *Credit Conditions Review 2016 Q3* available at www.bankofengland.co.uk/publications/Documents/creditconditionsreview/2016/ccrq316.pdf.

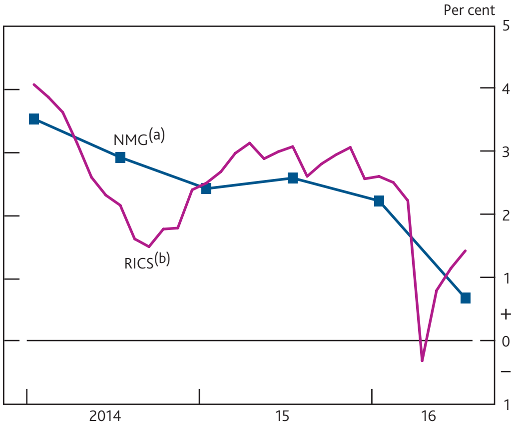
Chart 10 Changes in credit demand as a result of the vote to leave the European Union[(a)]



Sources: NMG Consulting survey and Bank calculations.

(a) Question: 'Has the overall amount of money you would like to borrow over the next 12 months been affected by the vote for Brexit?'. Percentages are calculated excluding those who stated 'don't know' or 'prefer not to state'.

Chart 11 Expectations for annual house price inflation



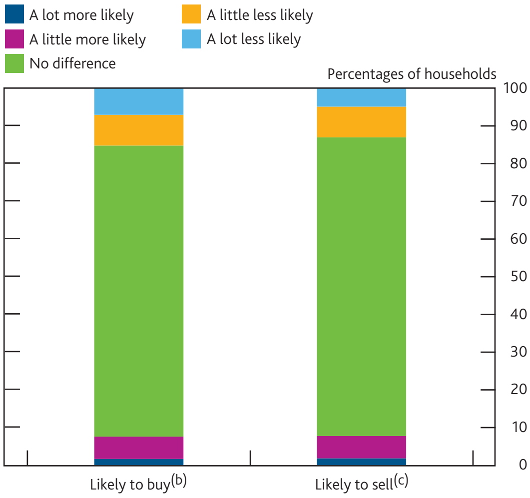
Sources: NMG Consulting survey and RICS residential market survey.

(a) Question: 'How much would you expect house prices in your region to change over the next twelve months?'.
(b) RICS survey expectations for house price inflation twelve months ahead.

surveyors' expectations from the Royal Institution of Chartered Surveyors (RICS) at the time of the NMG survey. According to both the NMG and RICS surveys, expectations fell most sharply in London.

The NMG survey results suggest that the vote to leave the European Union is likely to only have a small effect on housing transactions. The vast majority of survey respondents reported that the referendum result had not affected the likelihood that they would sell their main residence or purchase a new one (**Chart 12**). For those that did think that the vote to leave the European Union would have an impact, a net balance of around 5% of households said that the vote had made them less rather than more likely to buy/sell property.

Chart 12 Impact of the vote to leave the European Union on the likelihood of buying or selling home[(a)]



Sources: NMG Consulting survey and Bank calculations.

(a) Percentages are calculated excluding those who stated 'don't know' or 'prefer not to state'.
(b) Question: 'How do you think the vote for Brexit has affected how likely you are to buy a new main residential home over the next 12 months (whether moving or buying for the first time)?'.
(c) Question: 'How do you think the vote for Brexit has affected how likely you are to sell your main residential home over the next 12 months (either to buy another property to live in or move in to other accommodation)?'. Question asked to homeowners only.

Spending and uncertainty

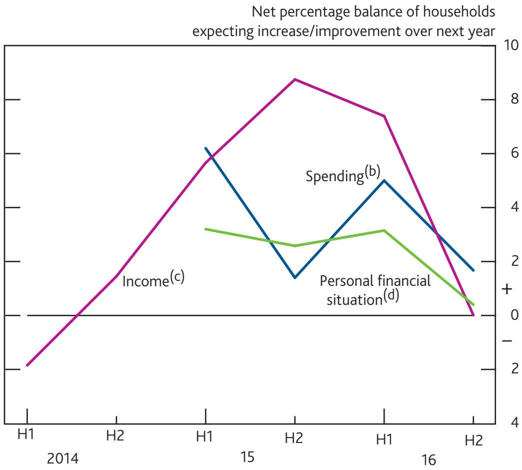
Households' view of the outlook for their incomes and financial situation more widely are likely to be an important influence on their spending decisions. Following the EU referendum, aggregate measures of consumer confidence deteriorated slightly but generally held up well.[(1)] Data from the latest NMG survey are consistent with a modest weakening in households' expectations.

The net balance of households expecting to increase spending over the coming year fell back a little in the latest survey (**Chart 13**). That is likely to be, in part, due to households becoming a little more pessimistic about their financial situation and a fall in income expectations (**Chart 13**).[(2)] To assess how this related to the vote to leave the European Union, households were also asked how the referendum result had affected their personal financial position and spending plans. Although it had no impact for most, a small net balance of households thought that the vote had worsened their personal financial positions (**Chart 14**). Conversely, the proportions of respondents who thought the referendum result would lead to an increase and decrease in spending were similar.

The vote to leave the European Union does not appear to have led to a large increase in uncertainty among households.

(1) For example, see Chart 2.6 from the November 2016 *Inflation Report* for data on consumer confidence; www.bankofengland.co.uk/publications/Documents/inflationreport/2016/nov.pdf.
(2) Two thirds of the fall in the net balance of households expecting an increase in income was due to fewer households expecting income to increase, with one third reflecting more households expecting income to fall.

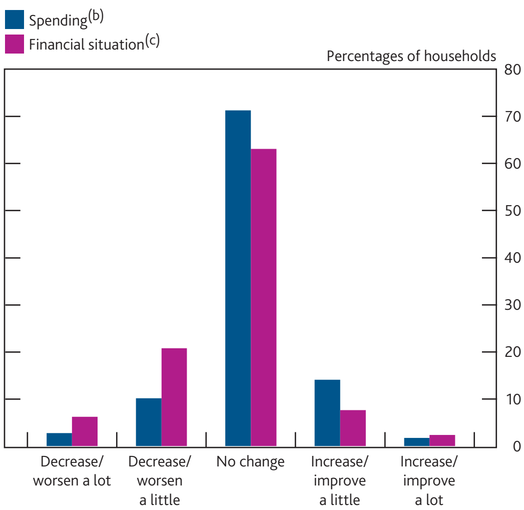
Chart 13 Expectations for spending, income and financial situation(a)



Sources: NMG Consulting survey and Bank calculations.

(a) The net balance for each question is calculated as the difference between the percentage of respondents expecting an improvement/increase over the next twelve months and those expecting a deterioration/fall. Percentages are calculated excluding those who stated 'prefer not to state'.
(b) Question: 'How do you expect your household to change its spending over the next 12 months? Please exclude money put into savings and repayment of bank loans'.
(c) Question: 'Over the next twelve months, how do you expect your total household income (before anything is deducted for tax, National Insurance, pension schemes etc.) to change?'.
(d) Question: 'How do you expect the financial position of your household to change over the next 12 months?'.

Chart 14 Impact of the vote to leave the European Union on spending intentions and financial situation expectations(a)

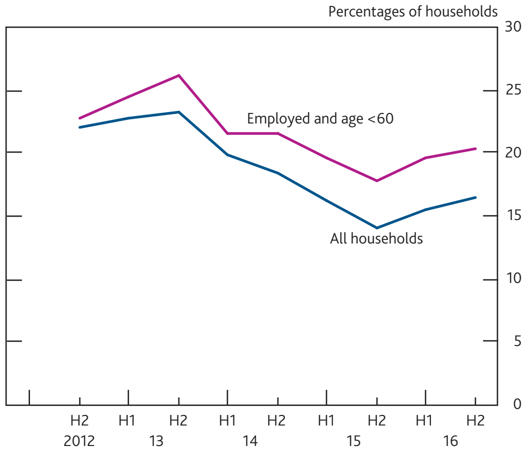


Sources: NMG Consulting survey and Bank calculations.

(a) Percentages are calculated excluding those who stated 'don't know' or 'prefer not to state'.
(b) Question: 'How do you expect the vote for Brexit to affect your household's spending over the next 12 months? Please exclude money put into savings and repayment of bank loans'.
(c) Question: 'How do you expect the vote for Brexit to affect the financial position of your household over the next 12 months?'.

There was only a slight increase in the proportion of households who thought that their income could fall sharply over the next year (**Chart 15**). A potential cause of sharp falls in income is job loss, and households' perceived probability of unemployment over the next year has risen slightly relative to when the question was last asked 18 months ago. The vote to leave the European Union may have had an impact on this: around 20% of households thought this had increased the probability of job loss slightly over the next year, although for 70% it had no impact (**Chart 16**).

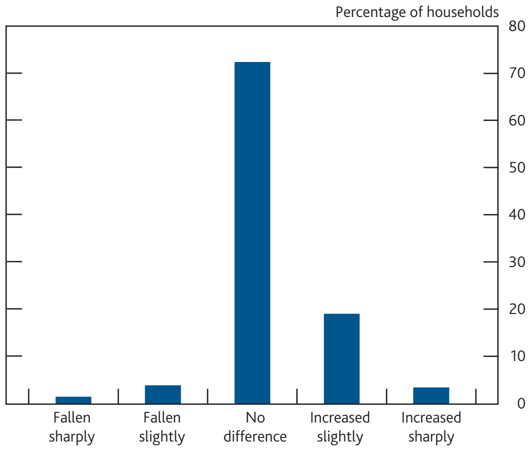
Chart 15 Share of households who think that income could fall sharply over the coming year(a)



Sources: NMG Consulting survey and Bank calculations.

(a) Question: 'To the best of your knowledge, how likely is it that your household income will fall sharply over the next year or so (for example, because you or someone in your household is made redundant)?'. Percentages are calculated excluding those who stated 'don't know' or 'prefer not to state'. Question not asked in 2013 H1 and 2015 H1 surveys. These data points are interpolated.

Chart 16 Impact of the vote to leave the European Union on probability of job loss over next year(a)



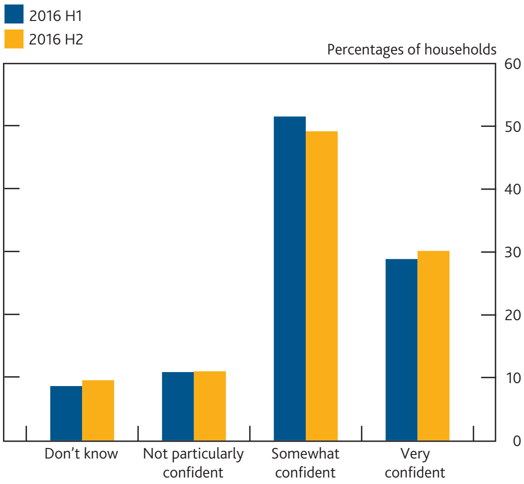
Sources: NMG Consulting survey and Bank calculations.

(a) Question: 'How do you think the vote for Brexit has affected the likelihood of you losing your job over the next 12 months?'. Percentages are calculated excluding those who stated 'don't know'.

In addition to questions relating to the chance of falls in income, the NMG survey also asked households how confident they were in their predictions for their own financial situation. There has been little change in uncertainty on this measure since the April survey (**Chart 17**).

Responses to the NMG survey suggest that if uncertainty were to increase more substantially, it could have a significant effect on spending. Those households who thought that there was a chance that their income could fall over the next year, and particularly those who thought that a fall was quite likely, had more pessimistic spending intentions than those who did

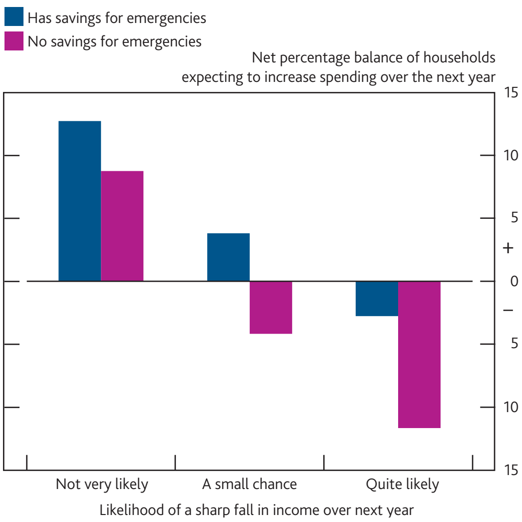
Chart 17 Households' confidence about their prediction for personal financial situation[(a)]



Sources: NMG Consulting survey and Bank calculations.

(a) Question: 'You mentioned earlier that you expect the financial position of your household to [get a lot better/.../get a lot worse] over the next 12 months. How confident are you that the financial position of your household will [get a lot better/.../get a lot worse] over the next 12 months?'.

Chart 18 Spending intentions and the chance of income falling sharply over the next year[(a)]



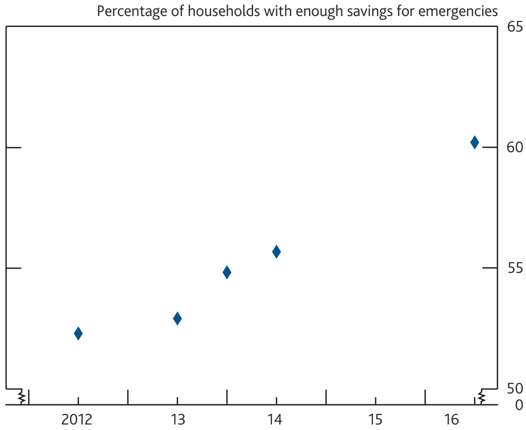
Sources: NMG Consulting survey and Bank calculations.

(a) Questions: 'How do you expect your household to change its spending over the next 12 months? Please exclude money put into savings and repayment of bank loans', 'Do you feel you have enough money set aside for emergencies?' and 'To the best of your knowledge, how likely is it that your household income will fall sharply over the next year or so (for example, because you or someone in your household is made redundant)?'. Only includes respondents who were in employment and under the age of 60.

not think it was very likely that their income was going to fall (**Chart 18**).

The extent to which higher uncertainty might affect spending may also depend on whether households already have a buffer of precautionary savings to fall back on in the event of emergencies. The share of households who felt that they had enough savings set aside for emergencies increased in the latest survey relative to when this question was last asked in 2014 (**Chart 19**). Households who do not have a sufficient buffer of savings were also more likely to plan on cutting back spending than those who do have a buffer if they thought that there was a chance of income falling (**Chart 18**).

Chart 19 Savings for emergencies[(a)]



Sources: NMG Consulting survey and Bank calculations.

(a) Question: 'Do you feel you have enough money set aside for emergencies?'. Percentages exclude those who stated 'don't know' or 'prefer not to state'. Question has only been asked in 2012 H2, 2013 H2, 2014 H1, 2014 H2 and 2016 H2 surveys.

Conclusion

Aggregate household debt remains high but has grown broadly in line with income over the past year. From a distributional perspective, data from the latest NMG survey show that on some measures the number of highly indebted households has stopped falling, having declined over recent years. The proportion of households with mortgage DSRs above 40% or DTIs above 5 was largely unchanged, while some indicators of current financial distress have also levelled off. However, the share of households with high mortgage DSRs is low by historical standards.

Following the MPC's August 2016 policy package, around half of mortgagors on floating-rate mortgages had already seen a cut in the interest rate at the time of the survey in the first three weeks of September. Households had also revised down their expectations for future Bank Rate. But mortgagors reported that paying off debt and saving more would be more common responses than an increase in spending in response to hypothetical further falls in mortgage payments.

The impact of the United Kingdom voting to leave the European Union appears only to have had a limited effect on households. Perceptions of credit conditions remained largely unchanged while there has not been much increase in measures of uncertainty. There was some weakening in households' expectations for future income, spending and house price growth, although these changes were relatively modest.

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