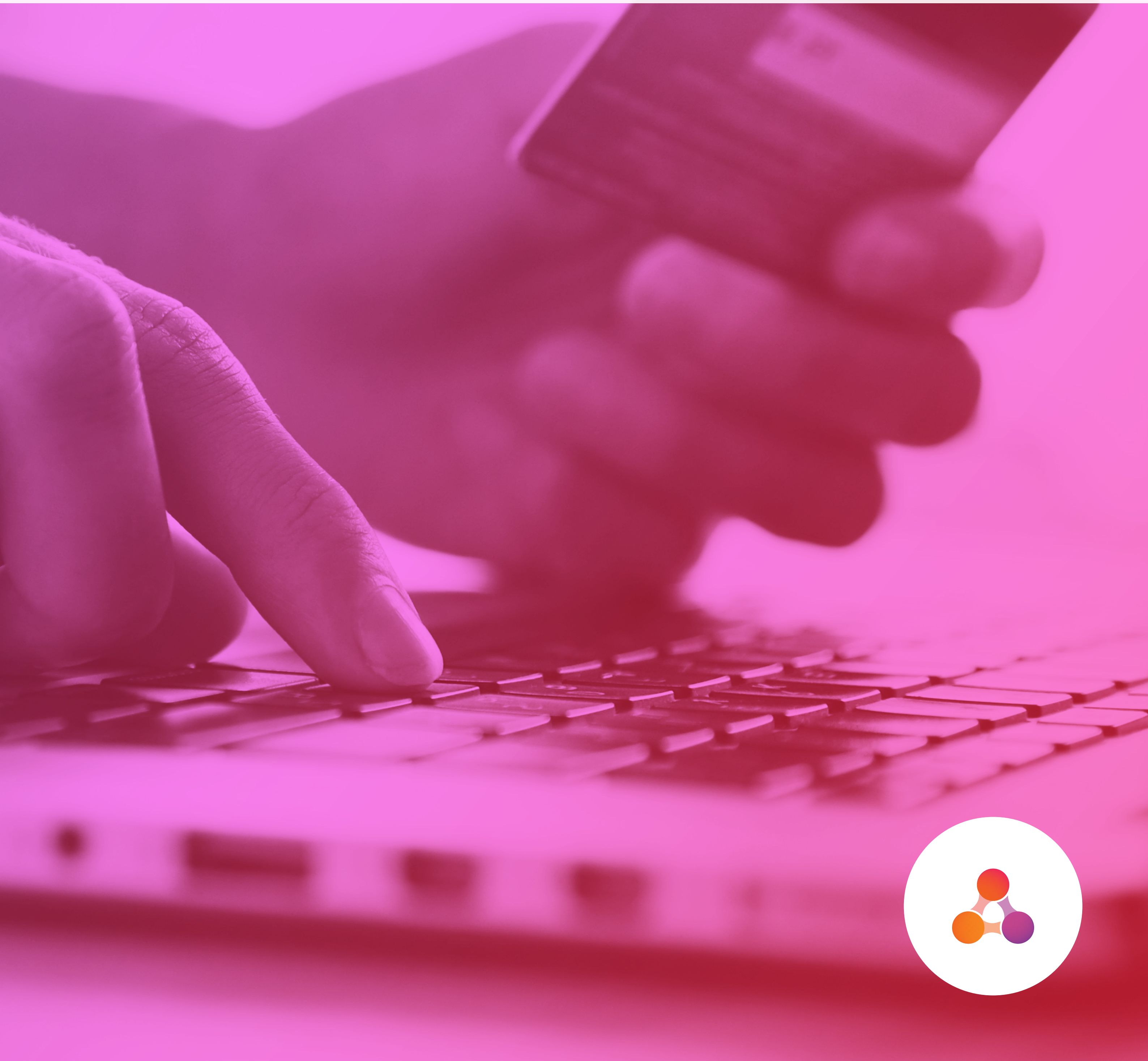
Second report

July 2019

Credit Card Nation 2

Good still good, but bad get worse



Executive Summary

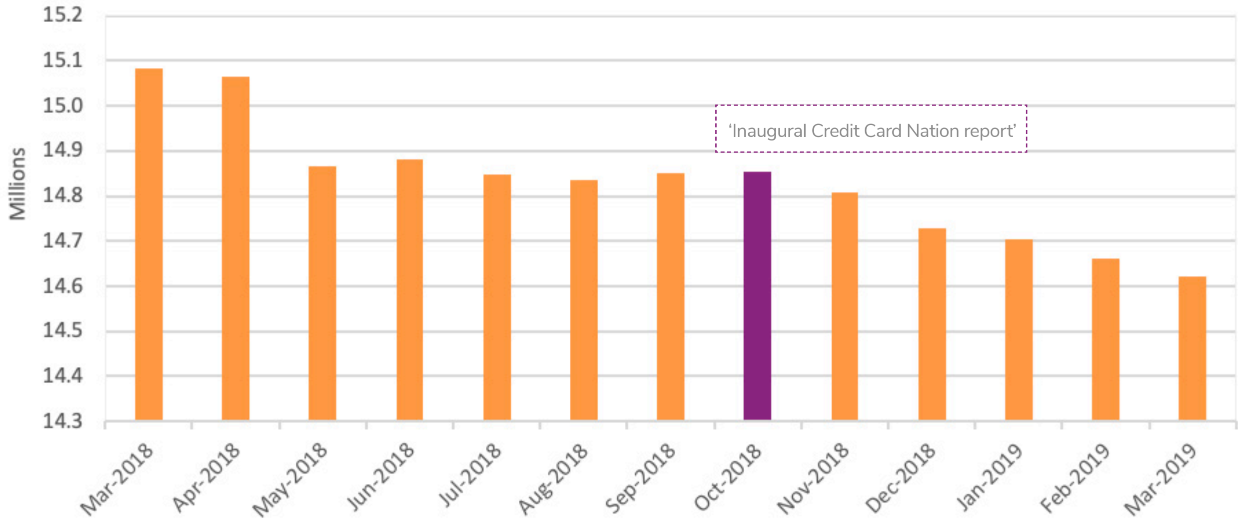
About this report

Almost half a million Australians have cut up their credit cards in the last 12 months, despite the Reserve Bank of Australia (RBA) dropping the official cash rate to an historic low of 1 per cent, and suggesting further cuts may be just around the corner.

illion's 2nd Credit Card Nation report highlights that there were 14.6 million credit cards in Australia in March 2019, down an extraordinary 462,000 cards, or 3.1 per cent from 12 months earlier[1].

Collectively, Australia's credit card limit stands at $137.3 billion , or an average $9,390 per card , down from $141.6 billion[4], in March 2018. The average per card remains unchanged.

Number of credit cards in Australia



Source: RBA, April 2019

The findings of this report confirm that Australia has surpassed 'peak card' and is on a long-term trend downwards.

While it is difficult to explain why, one reason may be that credit cards directly impact how much home-buyers can borrow from banks for their mortgage. Tighter APRA guidelines imposed on banks in the last 18 months could be forcing prospective home-buyers to abandon their credit cards – especially what they see as secondary cards - in order to qualify for tighter mortgage approvals.

[1] RBA C1.2 Credit and Charge cards – Original Series – Personal and Commercial Cards April 2019 CELL B218
[2] Official Reserve Bank figures of total market - Cell C28 in Marketshare tab
[3] Official Reserve Bank figures of total market - Cell D28 in Marketshare tab
[4] RBA C1.2 Credit and Charge cards – Original Series – Personal and Commercial Cards April 2019 CELL S218

Supporting evidence from illion includes the 'mortgage generation' aged 35-50 being the most likely age-group to be chronically behind in their credit card repayments. This group represents 38 per cent of all those two months or more in arrears, suggesting that financial stress is highest for those households with large mortgages. For context, however, it is important to remember that this group represents the highest number of credit card accounts.

Credit cards are most popular with young baby-boomers aged in their 50s, who own about one card each, compared with only 0.2 cards for each Australian adult under 25 years of age. This is a key economic group, and as card penetration is reduced in this group, it has the potential to impact on the broader credit provider market.

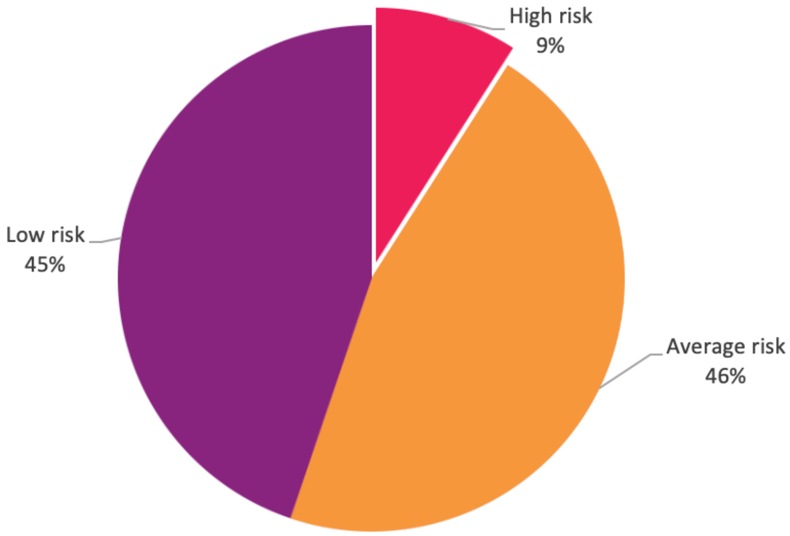
A slippery slope

illion holds detailed data on 95 per cent of all Australian credit card holders, making it amongst the most accurate sources for predicting consumer and business trends in the market.

Our data shows that almost $12 billion worth of credit card liability is sitting with 1.4 million high-risk accounts, creating a potential financial time bomb for banks.

High-risk borrowers are more likely to default on their debts than others and they represent 9 per cent of the entire market.

Percentage of credit card limits at risk of default over next 12 months



Defaulting on their debts may have an effect on bank profitability and subsequently a flow-on impact to the property market if banks become more cautious with their lending.

Despite the Reserve Bank of Australia's 0.25% cut to the cash rate in July 2019, which follows an extended period of historically low rates, the property market continues to be weighed down by tepid consumer demand, with prices down 7.3% nationally over the last year . The falls have been more pronounced in Sydney and Melbourne, which have dropped 17.2% and 9.9% respectively.

Impact of the Federal election

The research for our second Credit Card Nation report was completed a few weeks after Australia's 2019 Federal election.

The Federal election has positively impacted consumer sentiment, which had been generally weak in the months leading into polling day. This coincided with sluggishness in spending, credit growth and credit card usage.

There has been a 'post-election bounce' in consumer sentiment, although hard data on growth in credit and spending will not be available until late-July and early-August when the June private credit and ABS retail sales data are released. Indeed, it is likely that several more months of data will be needed to confirm whether any pick up has been sustained. This will feed into our Credit Card Nation 3 report.

There was been some easing from the 'credit crunch' in the period after the election, with the RBA cutting official interest rates and APRA relaxing the qualifications for new mortgages. These changes will take some time to show up in new data on credit growth and the economy more generally, but they are designed to underpin an increase in credit and spending.

That said, banks are still cautious in their new lending, partly in response to the current slump in house prices, but also partly in response to potential changes in lending rules and regulations following the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

[5] https://www.bloomberg.com/news/articles/2019-06-03/australia-property-prices-fall-least-in-a-year-as-slide-eases
[6] https://www.dailymail.co.uk/news/article-7105507/From-Byron-Bay-Gold-Coast-Great-Ocean-Road-house-prices-fell-past-year.html
[7] https://www.realestate.com.au/news/melbourne-property-price-falls-slowing-corelogic-finds/

Key Facts:

Consumers

illion's 2nd Credit Card Nation report shows there were 14.6 million credit cards in Australia in March 2019, down 462,000 cards from 12 months earlier[8].

Almost $12 billion is held by 1.4 million high-risk accounts, creating a potential financial time-bomb for the Australian banking system.

More than 35,000 Australians have five or more credit cards, making them five times more likely to default on their debts than those with fewer cards to manage.

350,000 accounts in Australia have some form of risk. This could be a bankruptcy, summons, judgement or default unknown by the lender.

Australia's total credit card limit is now worth a collective $137.3 billion, or an average $9,390 per card, down from $141.7 billion[9] 12 months earlier. Note the average limit remains the same.

Credit card limits vary significantly by capital city and regional area. Sydneysiders borrow the most, followed by Canberrans.

Businesses

In a further sign of the credit crunch, commercial credit card debt accruing interest grew by an astounding 47 per cent, from $1.4 billion to $2.0 billion, in the 12 months to March 2019[10].

This was partly off the back of companies using their credit cards more often, rather than cash. Businesses spent a cumulative $5.0 billion on their credit cards in March this year, compared to $4.6 billion 12 months earlier[11].

[8] RBA C1.2 Credit and Charge cards – Original Series – Personal and Commercial Cards April 2019 CELL B218
[9] RBA C1.2 Credit and Charge cards – Original Series – Personal and Commercial Cards April 2019 CELL S206
[10] RBA C1.2 Credit and Charge cards – Original Series – Personal and Commercial Cards April 2019 CELL AI221
[11] RBA C1.2 Credit and Charge cards – Original Series – Personal and Commercial Cards April 2019 CELL AB206

Conclusions

- While it is difficult to explain the fall in ownership of credit cards in Australia, one reason may be that credit cards directly impact how much home-buyers can borrow from banks for their mortgage. Tighter APRA guidelines imposed on banks in the last 18 months could be forcing prospective home-buyers to abandon their credit cards – especially what they see as secondary cards - in order to qualify for tighter mortgage approvals.
- With the addition of CCR account data in credit reports, credit providers are now able to identify existing liabilities more effectively, and may even ask an applicant to close an existing account before they will extend additional credit.
- While the number of credit cards overall is falling, those who have them are using them more often. Australians made 222 million credit and debit card transactions in March this year, up by 3.6% from 214 million 12 months earlier . This suggests some consumers are struggling to manage their cash-flow and are opting to drift into debt rather than pay off their bills immediately.
- Young people under 25 pose the greatest risk of failing to pay back their debts, as they are 5.8 times more likely to be two months behind in their repayments than Australians over the age of 50.
- Millennial men own just 5 per cent of all credit cards but represent 12 per cent of all those with debts exceeding 60 days. Why are they the only age group who are showing growth? The answer could simply be one of 'market forces' in play...that as card volumes continue to fall, financial institutions and credit providers may be taking on more risk to prop up the numbers.
- Over the years, the method of paying for goods and services has evolved from predominantly cash to credit cards, which gave the benefit to the consumer of allowing for 'borrowed money' or credit to bring forward purchases. Direct debit has evolved, along with the internet, and innovative payment methods such as what is now on offer through Facebook and buy now pay later. As we have seen in our inaugural Credit Card Nation Report, card transactions are likely to fade as other methods increase in popularity.
- It is likely that the reduction in credit cards has less to do with consumers abandoning credit cards altogether, but rather that they are closing superfluous credit cards as these may affect the ability to take on additional credit.
- Ownership of credit cards is now higher in regional Australia than metropolitan Australia (against the national average), with regional volumes increasing by 180,000 since October 2018. This is in sharp contrast to metropolitan card ownership figures, which have fallen by more than 400,000.

Balance and transparency will benefit everyone

By Steven Brown, illion's Director of Bureau Engagement

A more competitive credit environment will offer consumers pricing benefits as well as the capacity to show recovery from a negative credit experience sooner than what is possible under a 'negative only' credit reporting regime.

illion is a strong advocate for the expansion of Australia's credit reporting (CCR) system and mandating an environment that allows CCR data to be available to credit providers.

These substantial public interest benefits are wholly reliant on the comprehensive information being available and utilised. Until the recent broad-based adoption of CCR by Australia's major banks, CCR information has not been widely shared despite the enabling legislation being in place since 2014 - a real missed opportunity from a responsible lending perspective.

The breadth of positive reporting data available in Australia falls well short of information available in other jurisdictions such as the United States, Canada, South Africa and the United Kingdom.

illion is therefore of the view that while lenders must be obliged to make use of CCR data as part of their responsible lending obligations, account balance information must be included as a key data element.

The inclusion of balance in a credit report ensures that lenders get visibility of the level of utilisation that an applicant is making of their credit facilities and how they can best interpret the Repayment History Information (RHI) that is included for each line of credit.

Take the example of Susan for instance, who has two credit cards each with a $5,000 limit, one that is used regularly and is paid off each month in full, and another that is only kept for emergencies and has not been used in the last two years. Susan has a blemish free track record on her credit report and shows all payments made on time. It is important to note that when no payments are due, they will be reported by the credit provider to the credit bureau in the same way as a payment that is made on time.

Frank also has two credit cards, each with a $5000 limit. In his case he has been having some difficulties managing his spending and does not pay off the full balance of either card each month. In fact his balance on each card has been steadily increasing over the last two years to the point where both cards are now at their limit. Frank has however, managed to make the minimum monthly payments on both cards each month.

Now imagine a potential credit provider receiving credit applications from both individuals for a personal loan for a holiday. In both cases the credit files that they receive would show the same $10,000 limit spread across two cards and a blemish free repayment history. In fact their credit worthiness would appear almost identical in both credit reports.

Clearly however their actual circumstances couldn't be more different. By including a balance in the credit report it would become immediately clear to the credit provider that the circumstances of both individuals are quite different. The additional account balance information can be used by the credit provider to make the most informed decision possible about the extension of additional credit to the applicant.

Section 1: Age comparison

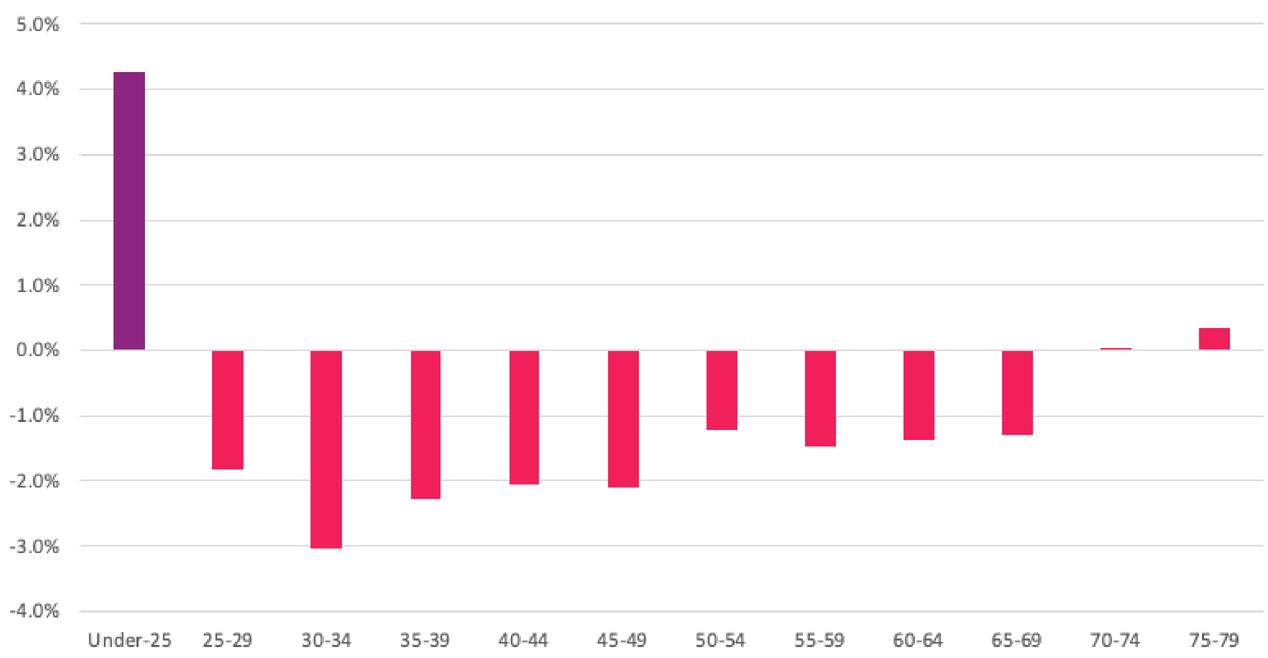
Over 25s continue to cut up cards

Since we conducted our first Credit Card Nation research in October 2018, we have found there are 320,000 less credit card accounts in the over 25 groups. Conversely, around 10,000 accounts have been opened by millennials.

While the increase in millennial credit card ownership may at first appear to be something of a silver lining in a cloudy world, we should remember that this is one of the groups with the highest risk profiles, which tempers any good news.

It is likely that the rise in millennial credit card ownership can be explained by young Australians getting their first job and getting a credit card. As we found in our inaugural Credit Card Nation report[12], this group tend to be users of both credit cards and buy now pay later services, having a slight preference for credit card ownership over buy now pay later (55 per cent to 45 per cent).

Percentage change of card ownership by generation since October 2018

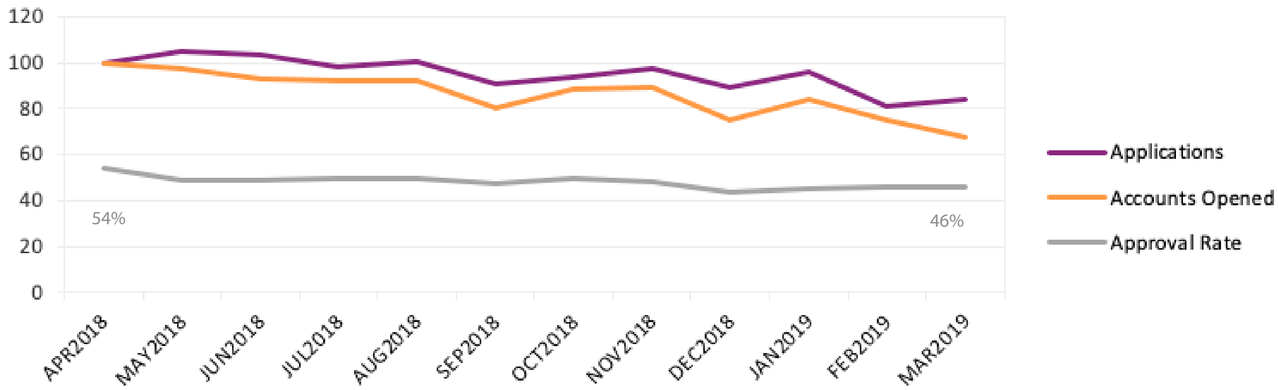


[12] https://www.illion.com.au/wp-content/uploads/2019/03/illion_CreditCardNationReport_2019.pdf, page 8

Credit cards are most popular with young baby-boomers, who own about one card each, compared with only 0.2 cards for millennials. However, illion data shows the 'mortgage generation' aged between 35-50 is the most likely to be chronically behind in their credit card repayments and represents 38 per cent of all those two months or more in arrears. This compares to 37 per cent of all younger Australians aged under 35, and only 20 per cent for pre-retirees aged between 50 and 65. These are the important revenue earning age groups, and large falls in demand are likely to become a major issue for credit providers with card products.

illion's data shows that mature credit users are dropping their credit cards – but the question is whether they are moving away altogether or simply closing their unnecessary credit cards and consolidating credit card debt.

Credit card applications, approval rates and new accounts



This graph shows that fewer applicants are being approved than ever, with 54 per cent approvals in April 2018 compared with 46% 12 months later.

Good still good, but bad get worse

By illion CEO Simon Bligh

In the last few years, lenders have adjusted their assessments of credit standards for consumers. This follows increasing pressure from the regulators as well as a sluggish economy, and anticipates potential changes to more rules as the findings of the Hayne Royal Commission come into force.

It has meant that low-risk, high-quality borrowers have maintained their strong credit scores, while marginal borrowers, or those with already problematic credit scores, have been further pressured and are finding it more difficult to obtain credit[13].

In simple terms, if you have a good credit score, you stay good. If you have a marginal or poor credit score, your ability to obtain credit is worse.

But here's where it gets interesting - our research this time around shows that millennials are now the only group that have increased ownership of credit cards. Granted the numbers are very small, and you may be asking why this is - especially as we know that young people under 25 pose the greatest risk of failing to pay back their debts and are almost six times more likely to be two months behind in their repayments than their parents.

In fact, we know from our inaugural Credit Card Nation research that millennial men own just 5 per cent of all credit cards but represent 12 per cent of all those with debts exceeding 60 days.

There are potentially two answers to this question: firstly, that millennial men are using both credit cards and buy now pay later services – and they get a card when they start their first job as a matter of course. Secondly, that we are simply seeing 'market forces' at play. That as card volumes continue to fall, financial institutions and credit providers may be taking on more risk to prop up the numbers?

Our society is in the early stages of moving towards a buy now pay later approach for many low-cost items, with this coming at the cost of a general decline in the usage of credit cards. Our young people are at the forefront of these changes and are using both at the moment – almost in equal measure. It will be fascinating to chart where it all goes in our future Credit Card Nation reports.

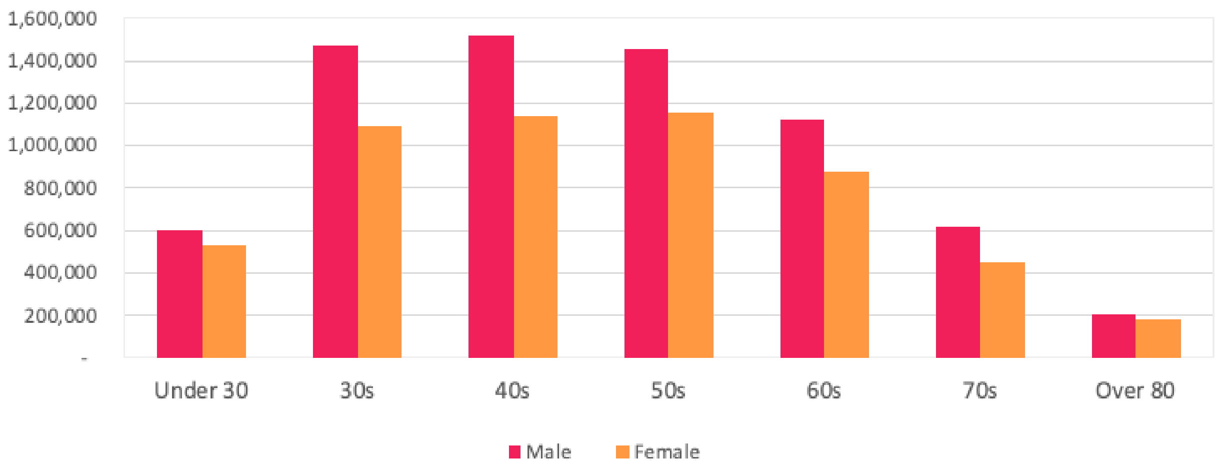
[13] https://www.smh.com.au/business/banking-and-finance/the-hayne-effect-home-loans-will-be-harder-to-get-and-take-longer-20180501-p4zco3.html

Gender spending in Australia

Men still love their cards more than women

illion's inaugural Credit Card Nation Report[14] (March 2019) identified that men own more credit cards than women in Australia.

Gender breakdown - number of credit cards in Australia



Fast forward to our Credit Card Nation 2 report, and our research has confirmed that men continue to hold 56 per cent of all credit cards, with women holding 44 per cent.

The reasons for the differences in credit card ownership rates can be at least partly explained by what economists call 'macroeconomic issues in the labour market', or put simpler, gender differences in workforce participation rates and incomes.

According to the Australian Bureau of Statistics labour force data[15], slightly more than two-thirds of working age men (67.5 per cent) are in paid employment, compared with 57.5 per cent of women. Having a paid job is really important when it comes to getting a credit card, which likely accounts for more men than women having cards.

In terms of average annual incomes, the ABS data[16] also shows men earning $75,950, while women, on average, earn $51,850. These income levels are total income, and show a significant gender pay differential for many reasons. A person's level of income is also an important aspect in gaining approval to have a credit card.

The gender differences in paid employment ratios and incomes are evident across all age groups, and are consistent with men having more credit cards than women, again, across all age groups.

[14] Credit Card Nation: Page 10: https://www.illion.com.au/2019/03/10/an-inaugural-report-credit-card-nation-2019/[15] https://www.rba.gov.au/payments-and-infrastructure/resources/payments-data.html
[15] ABS employment to population ratio 2019: Table 1 https://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/6202.0May%202019?OpenDocument
[16] ABS wages data by gender 2019: Table 2 https://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/6302.0Nov%202018?OpenDocument

While this is the obvious reason, the less obvious reason may simply be that women are more financially conservative, given that both the number and proportion of defaults are lower for women than men[17].

Further evidence of the more responsible nature of female spending habits may be found in the exploding popularity of buy now pay later accounts. We know from our earlier research in our inaugural Credit Card Nation[18] report that women are more inclined to undertake such transactions by a factor of almost two to one.

We also know women are better at ensuring their credit card bills are paid on time, and are more likely to be financially prudent.

Getting on top of your finances

By David Scognamiglio, Credit Simple CEO

The Board of Australia's Reserve Bank meets at the start of each month, and in early July, it dropped the official cash rate to an historic low of just 1 per cent.

It was not the first drop, and in an environment where we have seen mortgage rates falling steadily, we should be seeing money going back into household coffers.

But it's not. Australians' spending patterns have been weak. Economists even have a name for it – they are calling it the 'era of the cautious consumer'. Household spending in recent years has been constrained by a combination of weak wage growth, high levels of mortgage debt and low rates of saving.

At Creditsimple.com.au, we believe that it's an imperative for homeowners to put a 3 in front of their mortgages – and potentially we will even start to see some 2s. You can have another month's income in your pocket each year simply by shopping around for a better mortgage rate. Low rates are introducing phenomenal competition on rates and we see consumers shopping their rates downward as a way of injecting funds into the retail sector or simply building consumer confidence by getting ahead on mortgage repayments.

If interest rate competition changes consumers behaviours to shop for better offers we see that as a positive effect. Other smart things to do include getting your credit card debt down with a balance transfer on a zero interest credit card or consolidating to lower rates to take stress off - just remember to close one of them afterwards.

Creditsimple.com.au is helping Australians get on top of their finances in a number of ways: we contribute to the publishing of reports like this one to help you understand the bigger picture, and how the credit system works. We give away credit scores for free on Credit Simple, allowing you to see for yourself the impact of missed payments on your credit score, as well as your standing with financial institutions.

We've also recently built Money Simple, which helps you easily categorise where consumers spend their money. This in turn helps people identify for instance, when you are paying too much interest on financial products or making small lifestyle payments that add up to large amounts of money - things like take out deliveries or too many coffees could be putting a drain on your coffers.

[17] Credit Card Nation: Page 10 https://www.illion.com.au/2019/03/10/an-inaugural-report-credit-card-nation-2019/
[18] Credit Card Nation: Page 3: https://www.illion.com.au/2019/03/10/an-inaugural-report-credit-card-nation-2019/

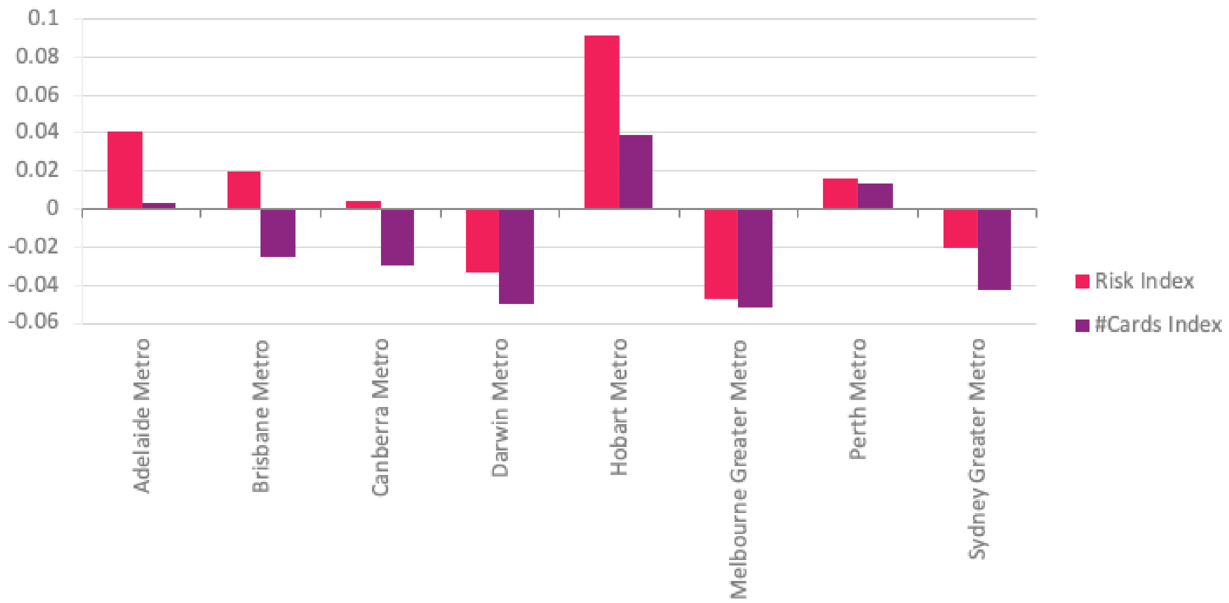
Geographic breakdown of ownership and payments

Analysis of credit card ownership has shown that residents in Hobart, Canberra and Perth have enjoyed the most growth in credit card ownership in Australia.

These capital cities now enjoy up to 10 per cent higher credit card ownership than the Australian average

Canberrans topped the credit card ownership leader board by a significant margin in our inaugural Credit Card Nation report. The nation's Capital has fallen slightly from October 2018, however, with 3,000 fewer card owners and 6,000 fewer cards. Canberra's credit card risk is 50 per cent lower than the Australian average.

Percentage difference in credit card ownership and risk since October 2018



Conversely, Hobart has seen moderate growth in credit cards, with 6,700 more people now with a card and 8,500 more credit cards since October 2018. This means Hobart now has the highest per person ownership amongst our capital cities (albeit the differences are slight).

Of all the capital cities, Hobart has also seen the largest improvement in risk since October 2018 – now being 8 per cent lower than in October 2018 - relative to the Australian Average change in risk.

Melbourne, Sydney and Darwin have all seen falls of around 5 per cent against the national average of card ownership. While Melbourne recorded an increase in the number of consumers with cards (19,852), Sydney showed a small drop (4,370), both cities have seen the number of credit cards in the market drop significantly by 182,000 and 184,000 respectively. This means that while there are new consumers taking on cards, there are many more existing consumers closing credit cards – especially 'non-core' credit cards.

Melbourne's Risk has deteriorated slightly since October 2018 – 5 per cent higher risk in March 2019 compared to our last survey in October 2018.

Brisbane is observed to be similar (on lower numbers), with a net increase of 25,000 new consumers with a credit card, but with 39,000 fewer credit cards in market.

While Sydney and Brisbane have a 10 per cent higher risk of late payment than the average, those in Darwin continue to have the lowest propensity to pay on time. Darwin was also the worst capital city performer by a significant margin (20 per cent higher than the national average).

Adelaide has seen a uniform loss in consumers owning a credit card as well as in the number of credit cards in market but maintains a much lower risk than average at 20 per cent.

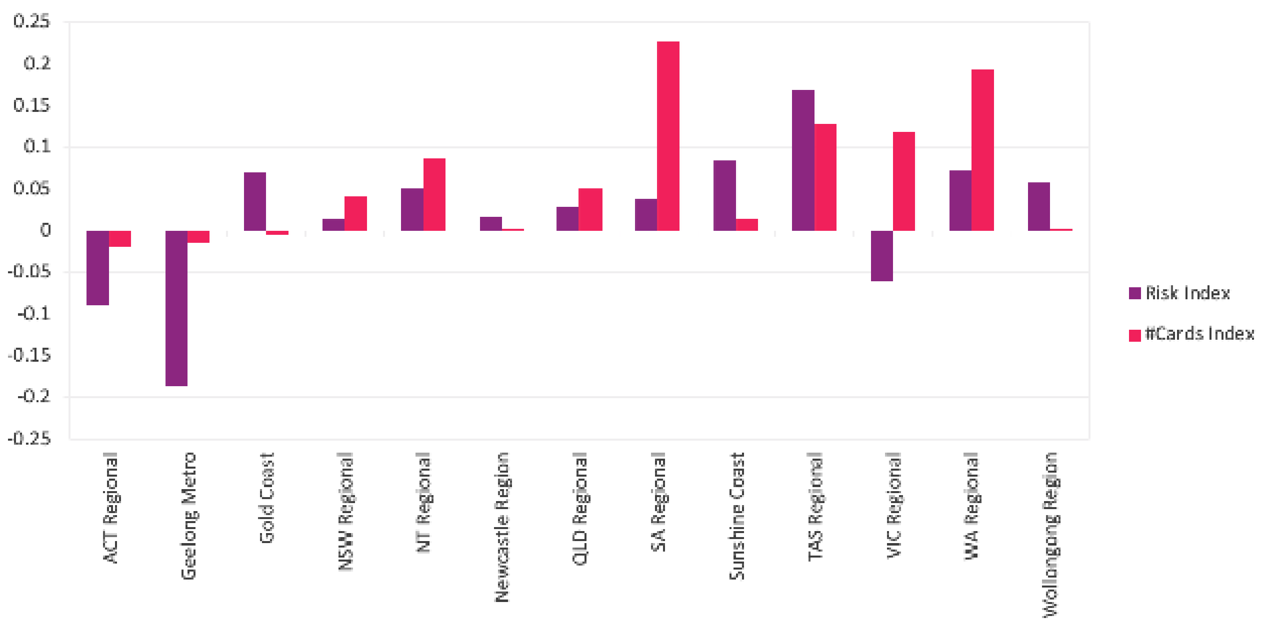
Findings in detail – by region

Our latest analysis of credit card ownership by region shows that most of regional Australia has seen growth in credit cards, which is countering the losses in capital cities.

Those living in regional ACT still love burning their plastic, with 20 per cent higher card ownership per person – consistent with our findings in our inaugural study. They are also 25 per cent less likely to miss a payment than the Australian average.

Sunshine Coast residents are not far behind those in the ACT, enjoying a 10 per cent higher card ownership rate per person. They are also 25 per cent less likely to miss a payment than the Australian average.

Percentage difference in credit card ownership and risk since October 2018



People in regional Tasmania and regional WA now also have a higher level of credit card ownership, at around 10 per cent more per person compared to our previous study. Significant improvements in risk have also been observed for regional Tasmania (15% lower than in October '18) and regional WA (8 per cent lower).

South Australia still has the lowest card ownership levels, but this has increased marginally since we undertook our inaugural Credit Card Nation study. Regional South Australians are also 25 per cent less likely to miss a payment than the Australian average.

The clear exceptions are the regional cities of Geelong and Wollongong which have seen 10 per cent falls in card ownership relative to the Australian average. Geelong has also seen its risk of default increase by 20 per cent, while Wollongong has recorded a 10 per cent lower risk of default.

Per person card penetration has increased the most in regional Victoria and the Northern Territory – by 10-20 per cent over the Australian average . This suggests that card growth has outweighed growth in card consumers in these regions, and indicates that people are potentially opening multiple cards.

Those living in the regional Northern Territory represent the highest risk in Australia – around 15% higher risk than the Australian average and consistent with Darwin's late payment rate of 20 lower than the average.

What's happening in regional Australia?

By illion's economic adviser, Stephen Koukoulas

Ownership of credit cards is now higher in regional Australia than metropolitan Australia (against the national average), with regional volumes increasing by 180,000 since October 2018. This is in sharp contrast to metropolitan card ownership figures, which have fallen by more than 400,000.

In some regions we have seen a growth in cards coinciding with a fall in consumers, suggesting both an increase in multi-card ownership and non-card ownership. It appears likely that people are now making choices around their preferred credit vehicle.

It is notable that the current slump in house prices has been concentrated in the capital cities, while the price falls in regional Australia have been more moderate. According to Corelogic[19], dwelling prices in the capital cities have fallen 10.2 per cent for their recent peak, while the drop in regional Australia is just 3.4 per cent.

These price trends may have influenced consumers in the cities to consolidate their financial position, including with credit cards.

The strength in credit card usage in regional areas has resulted in Geelong in particular moving from a significantly lower risk region to an average risk region.

Late payment risk rates are now lower in regional Australia compared with metropolitan areas, which could be due equally to a fall in delinquencies and/or a rise in new card volumes. This shift has continued to grow incrementally since October 2018.

It is likely that the loss in credit cards has less to do with consumers abandoning credit cards altogether, but rather that they are closing superfluous credit cards as these may affect the ability to take on additional credit.

It is too early to draw a conclusion that metropolitan areas have reacted to the new lending policies post-Banking Royal Commission. Likewise, whether perhaps regional Australia has become a desirable source of new credit to make up for shortfalls in other areas.

[19] https://www.corelogic.com.au/news/sydney-and-melbourne-housing-values-edge-higher-june-values-still-trending-lower-national

About illion

illion is the leading independent provider of trusted data and analytics products and services in Australasia, with the company's consumer and commercial registries representing a core element of Australia and New Zealand's financial infrastructure.

We leverage consumer and commercial credit registries, which comprise data on over 24 million individuals and over 2 million commercial entities, to provide end-to-end customer management solutions to clients in the financial services, telecommunications, utilities and government sectors.

Trusted Insights. Responsible Decisions.

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