Consumer Stress Barometer

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Australia
December 2024

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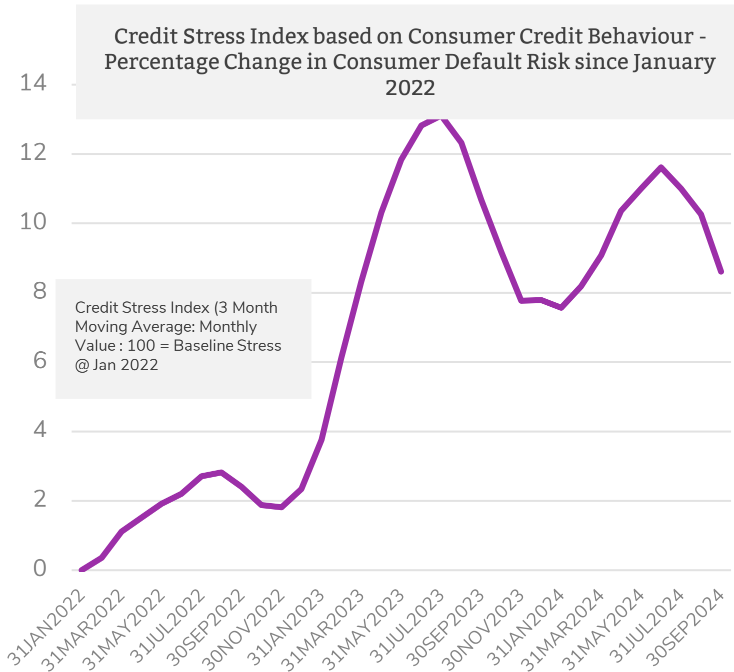
Credit Stress Barometer @ September 2024 – The barometer is generally stable, showing no underlying trend in the last year; overall risk remains around 9% higher than in early 2022.



The illion Credit Stress Barometer for September 2024 indicates that the consumer credit default risk of Australians may be stabilising. The overall trend over the last 18 months is now looking broadly harmonic, with deterioration occurring in H1 and improvement in H2 in both 2023 and 2024.

There is no evidence that the trend into 2025 will change, suggesting that the default risk of consumers will remain around 9% higher than in early 2022. This does show that conditions for borrowers are harder today than 3 years ago but also, that borrowers may have begun to adapt to their new economic conditions. Higher risk may be 'here to stay' until interest rates start falling but may at least, not deteriorate further.

By following a seasonal trend, credit stress appeared to deteriorate in the early part of the year (as incomes did not keep pace with rising expenses around Xmas), then improved in the latter part of the year as debts were progressively repaid and costs contained.,

Householders were better able to control their budgets in Q3, being buoyed by wage increases and tax refunds and especially, by the additional financial support received from the enacted tax-cuts for FY24/25. While the effect of these tax-cuts is not yet conclusive, our data may suggest that they have helped to mitigate default risk.

However, while the tax-cuts may have helped many households service their debts, they don't yet appear to have materially helped more vulnerable groups, including those with higher debts to income, nor with promoting greater consumption and broader economic activity. As such, economic stresses are still evident, especially amongst 30-something Mortgage holders. The outlook for lower income, mortgage-belt Australia and for the small business sector is therefore still uncertain.

Specific observations for the September quarter are as follows:

- The default risk of Credit holders decreased, this being most notable amongst Personal Loan and Mortgage holders. The overall improvement amongst Mortgage holders reversed the deterioration seen over FY23/24.
- All major Australian states saw this improvement in Mortgage holder risk, reversing the trend seen in the June quarter; even Victoria saw a turnaround.
- Interest rate relief appears to be necessary in Australia's mortgage-belt, where we have seen a materially lower improvement in risk even as incomes have been supplemented by tax relief (i.e. 2% lower amongst 30-somethings compared to the average fall of over 4% amongst people over 40-years-old).
- There was a marked drop in credit demand, especially for new Home Loans and Personal Loans, while demand for Credit Cards was flat.
- Consumer optimism floundered somewhat, as savings levels remained quite low and real Retail and Grocery spending growth was at or below CPI levels.

Credit Default Risk has improved in the September quarter as consumers prioritise debt servicing over consumption

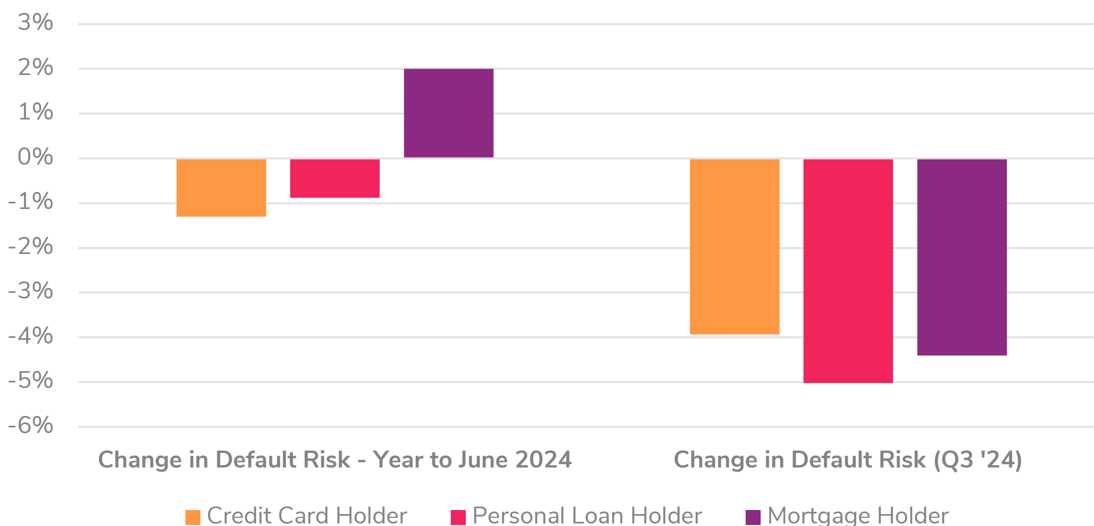
The FY24/25 tax-cuts, tax refunds and wage increases appear to have reduced the financial stress on borrowers, at least in the short-term. This is shown by improving credit default risk across products and in all major states.

After seeing Mortgage holder risk rise by 2% in FY2023/24, the September quarter saw credit risk falling by 4%, as shown in the diagram below. This substantially reversed the 3% deterioration seen in the June quarter and led to an overall improvement of 2% in Mortgage holder risk nationally over the 15 months since June 2022. While this improvement offers some optimism, it also implies that Mortgage holder risk is volatile at present and highly sensitive to any events that impact on household finances.

To illustrate this sensitivity, we note that the improvement in Mortgage holder risk has coincided with five events that may have benefitted consumers (some being unique to FY24/25) - 1) more stable and lower CPI compared to the previous 2 years, 2) stable interest rates over the last 12 months, 3) FY2024/25 wage increase reviews, 4) FY23/24 tax-refunds and especially, 5) FY24/25 tax-cuts. Some of these events will have had an enduring impact on consumers while others may have offered short-term relief.

Personal Loan and Cardholder risk have also fallen (5% and 4% lower), meaning that Australians have used their improved financial standing to pay down all types of debt. That said, the extent to which these better conditions will continue to benefit consumers is unclear.

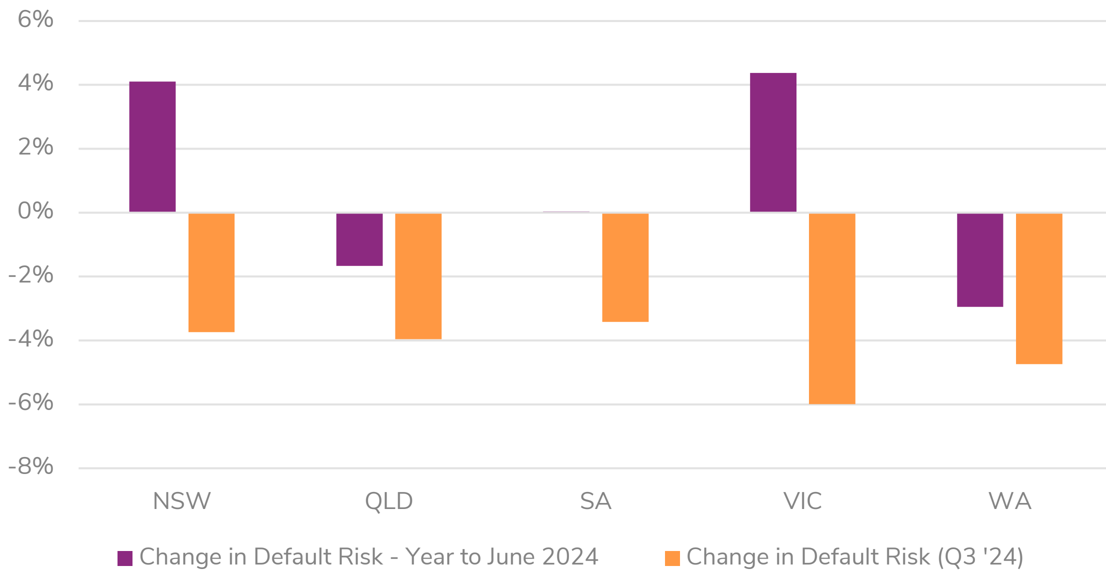
Percentage Change in Credit Default Risk since June 2023



As shown in the following graph, the September quarter also saw the default risk of mortgage holders falling in all major states. In NSW, this improvement reversed the 4% deterioration seen in FY23/24, while in WA, QLD and SA, it added further to the stability already seen in FY23/24. Therefore, while the NSW result suggests some volatility in terms of credit stress, the QLD, WA, SA result appears to show a sustainable improvement since mid-2023.

Victoria saw the largest improvement (6%) in the September quarter; reversing the 4% deterioration seen in FY23/24. However, the overall improvement since June 2023 is still significantly lower when compared to QLD, WA and SA. Mortgage holders in Victoria and NSW have therefore been slower to recover from credit stress, however the result seen in the September quarter has, at least, shown that their improved finances have helped to pay down overdue debt. Although smaller regions are not included in the diagram, there has been a deterioration in Mortgage stress in Tasmania and the Northern Territory. This is most likely due to the steep and delayed rise in house prices in these markets (relative to income), which have over-stretched consumers.

Change in Credit Default Risk of Mortgage-holders (by State)

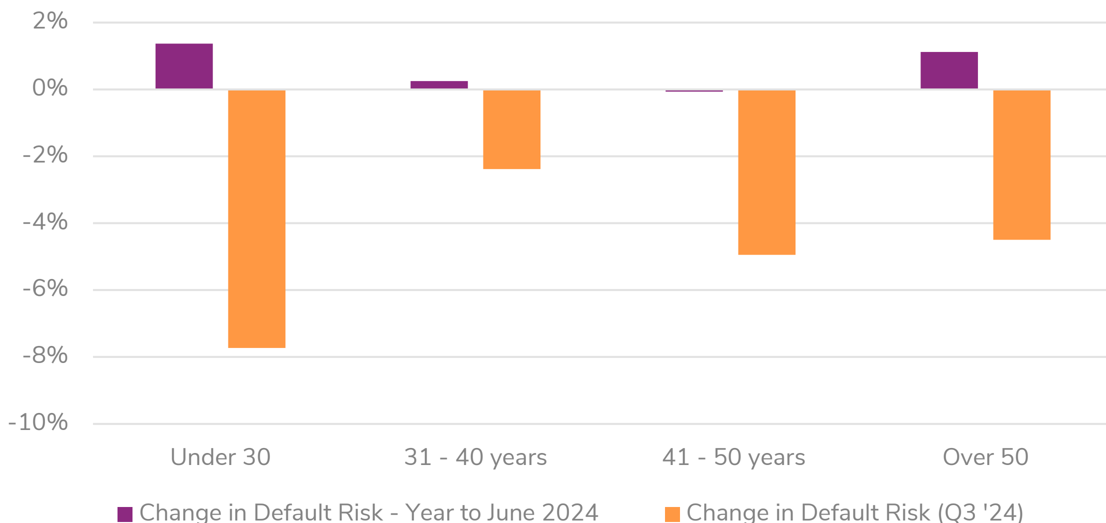


While the September quarter saw a significant improvement in mortgage holder stress, this was not consistent across all age-groups. The risk of older Australians (over 40's) and the young (under 30's) improved substantially (4% and 8% respectively), whereas the risk of 30-something Australians only improved mildly (2%) (this is shown in the following diagram). One possible reason for this is that the savings levels of older Australians benefitted most from the tax-cuts and tax-refunds (given that their outgoings may have been lower than other age groups). With greater savings, the 'Bank of Mum and Dad' effect may have consequently benefitted young mortgage holders.

As cautionary note however, these better conditions may have been due to seasonal and one-off effects. As such, default risk could deteriorate again if there is a return to higher inflation in 2025, where price increases and 'bracket-creep' negate the benefits attained from tax cuts and refunds.

More concerning is the change in the mortgage holder risk of 30-somethings. While they have also benefitted from tax-cuts and tax-refunds, their improvement has been more muted. This is because they represent a large segment of Australia's mortgage-belt and, as such, are in a more precarious financial situation than other groups; mainly due to having a higher ratio of debt to income, higher relative household expenses and a lesser ability to tap into other sources of funding (e.g. parents/family) when trying to weather the effects of inflation.

Change in Credit Default Risk of Mortgage-holders (by Age)



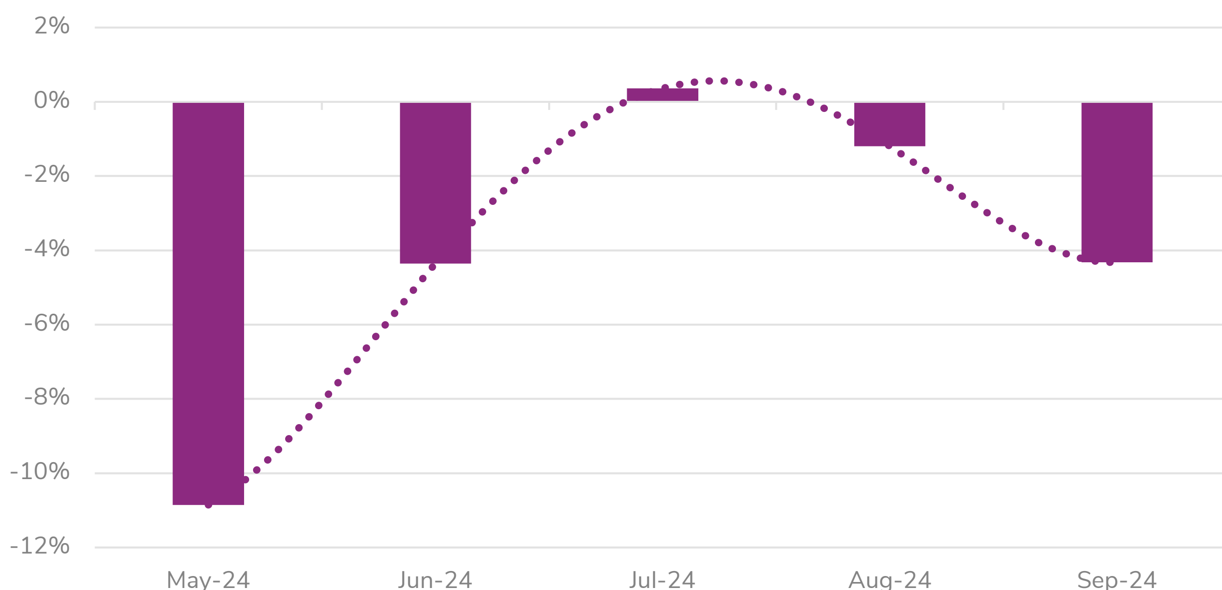
Consumer confidence is tentative as households 'stay in their shell' with spending while they prioritise loan repayments; although tax-cuts have offered some spark.

As tax-cuts and salary increases help budgets, Australians have opted to service debt rather than significantly increase consumption. The increase in spending is at, or below CPI, but the fall in household savings is slowing.

Although credit stress improved in the September quarter, Australians were still burdened by tight household budgets, affecting both their spending choices and their general mood. By September 2024, optimism was dropping again, as can be seen in the diagram below, which maps consumer confidence between May and September. Confidence did rise considerably in the last quarter of FY23/24, due mainly to more stable prices, as well as in anticipation of the FY24/25 tax-cuts. Therefore, while consumers were still strained by tight household budget, the prospect of greater spending power buoyed their confidence.

However, tracking forward to the September quarter, we can see that confidence, while not as low as in early 2024, fell again as the financial benefit from government policy was absorbed into household budgets and there was still no clear indication of the timing for interest rate relief. So, although credit stress was being managed, the broader problem of financial wellbeing remained unresolved.

Change in Consumer Confidence – Monthly relative to 2 Years Earlier

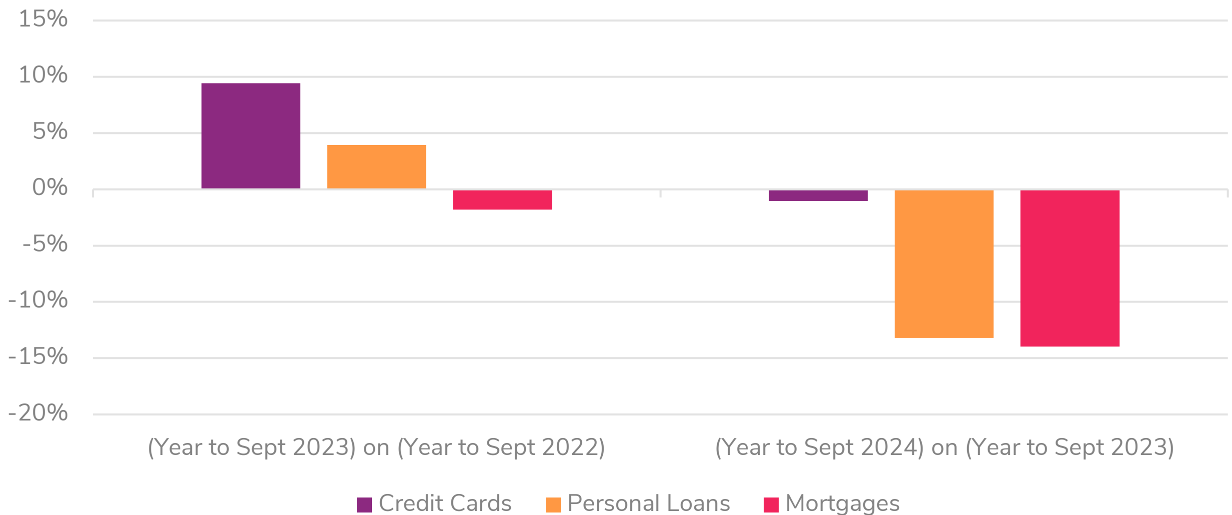


Source: ANZ-Roy Morgan Consumer Confidence Rating includes the five component questions on personal finance, the Australian economy and whether now is a 'good' or 'bad' time to buy.

While the prioritisation of credit obligations showed that households were managing their budgets in a tough economic environment, we uncovered aspects of consumer behaviour which may not augur well for the broader economy into 2025. These relate to the credit demand, savings rates and spending decisions of consumers. Solving these current economic problems will require delicate management of policies, to avoid either raising inflation or promoting a recession.

Firstly, as shown the next diagram, there is some suggestion that consumers have less desire or less financial capacity today to increased their demand for credit. When compared to the 12 months to September 2023, the year to September 2024 saw a near 15% fall in the number of Home Loan and Personal Loan accounts opened by consumers (and no growth in new Credit Cards opened), meaning that lending for personal consumption and home ownership is substantially lower today than in previous years. The financial support obtained by households is therefore being used conservatively – e.g. paying down existing debts and/or holding savings rather than taking on additional credit.

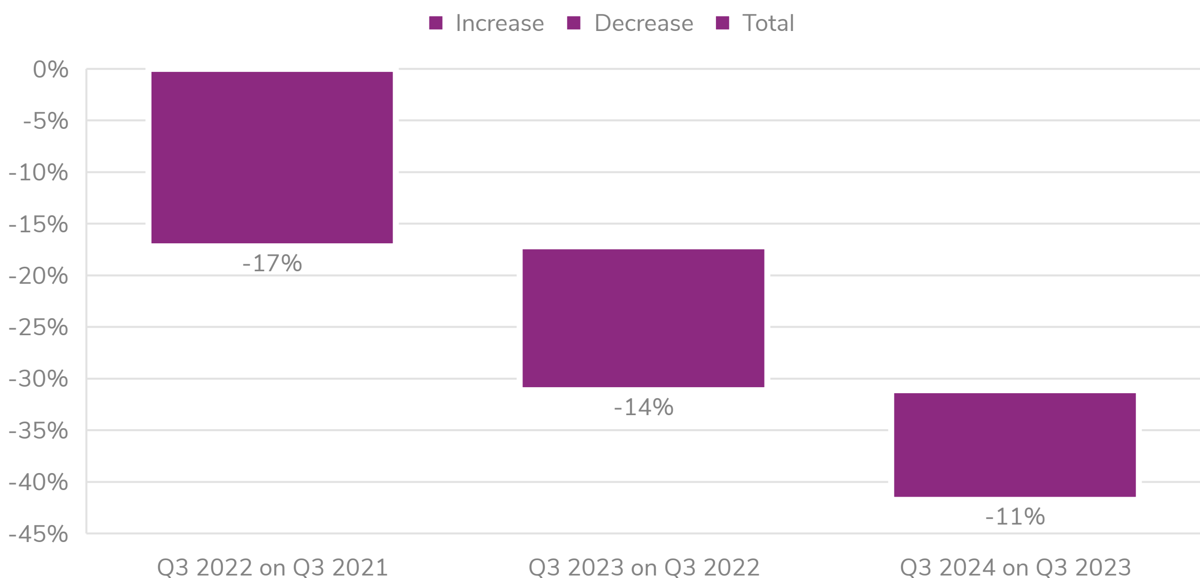
Change in the Number of New Accounts Opened



The delicate nature of household finances can also be seen in the savings patterns of Australians. While the additional money obtained through tax-cuts and other benefits has reduced credit stress, it has also influenced savings rates. From the diagram below, we can see that average household savings are now falling at a lower rate than in previous years; falling only 11% in the year to September 2024, down from 14% in the previous year and from 17% 2 years ago.

This result may indicate that - 1) Australian households are using surplus money to increase savings. If so, borrowing and spending for investment, for home ownership and for consumption is now 'taking a back-seat'. This speaks to the fragility of personal finances, where people are opting to keep money as a safety-net rather than using it to promote economic growth, which may have negative implications for the broader economy – 2) While slowly stabilising, savings rates have, on average, still fallen over the past year. This means that some households are continuing to tap into their safety-buffer, and while the September quarter saw a small rise in average savings, this may not be sustainable if it was due to one-off or seasonal events.

Change in Average Savings Balances of Australian Consumers – (YOY in September Quarter)

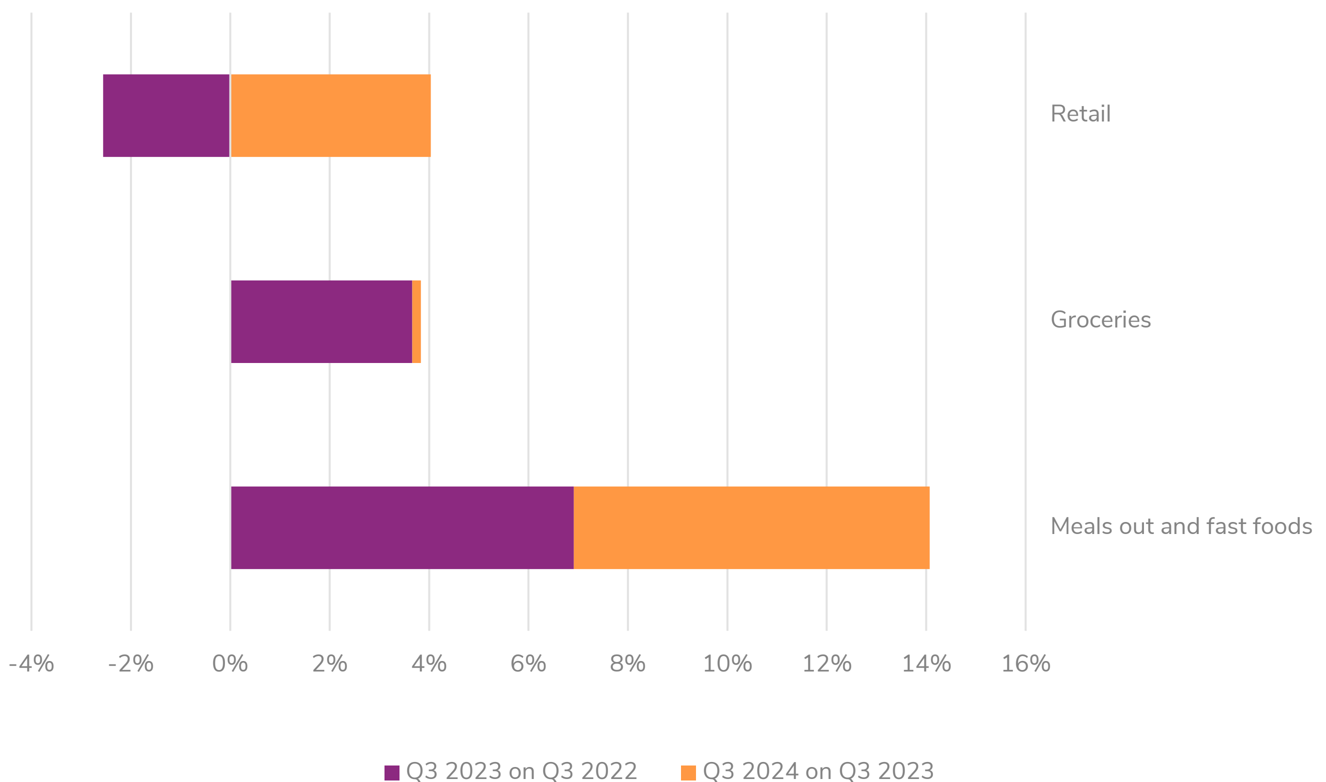


The fragility of Australians' personal finances is also shown by their regular consumptive spending (as opposed to incidental and one-off spending events). As depicted in the graph below, we observed that spending on several core categories struggled to keep up with inflation, meaning that real consumption either fell or remained flat.

For example, while eating out and take-away expenditure remained resilient, rising 7% in the quarter (or around 4% above CPI), retail spending only rose by 4% (barely above CPI) and grocery spending rose only marginally (less than 1% in gross terms and falling close to 3% in real terms). Though this may have been partly due to a lower inflation rate on grocery prices, the fall in real spending suggests that the level of consumption stagnated. Therefore, while consumers looked to increase their savings-buffer they also curtailed their regular spending.

The bottom line is that household budgets either appear to be fully stretched or geared to saving and/or paying down debt rather than consuming. By prioritising personal finances, this lower consumption may have consequences for economic growth into 2025 and may point to why we are seeing consumer confidence falling even though there is a moderate improvement in credit stress. Conversely, if tax-cuts were introduced to help households manage their finances but also 'keep a lid on consumption and inflation' then it can be argued that this has been achieved.

Change in Spending on Categories – (YOY in Sept Quarter)



Appendix: Definition of the Credit Stress Barometer

Background Notes: Basis of Credit Stress Barometer

illion's Credit Stress Barometer shows the risk of Australian Consumers defaulting on Consumer Credit contracts in the next 12 months. The barometer is a,

- metric, showing the percentage of consumers at risk of defaulting on their credit agreements
- forward looking prediction of this default risk
- trend-line, showing the changing nature of credit stress, both directionally and in magnitude.

The barometer is created by modelling the risk of credit default from a consumer's

- Current and historical credit performance – i.e.. trends in credit repayment performance across various types of credit contracts
- Current and historical credit demand – i.e.. the appetite for credit by considering application volumes and loan take-up; this is across different types of credit, including housing, investment and consumptive credit agreements.
- Financial exposure to different types of credit products – fixed loans, revolving loans, housing finance, car finance, investment loans
- Demand for credit in various industry risk sectors – e.g. the level of credit demand and repayment performance on borrowings from the Prime, Near Prime and Sub Prime lenders segments.

The Credit Stress Barometer is shown as the change in the percentage of consumers at risk of Credit Default, with the percentage calculated relative to a Baseline @ January 2022. This baseline has been chosen to a) remove the early biases/effects from COVID and to b) focus on current economic impacts from broad-based inflation and higher interest rates on borrowings.

In order to smooth monthly fluctuations, these trends are calculated as moving averages over a rolling 3-month period to the month shown in the trend diagram (Slide 2).

Additional insights into savings and expenditure patterns are incorporated in this Credit Stress Barometer pack to show financial trends that are likely to have an impact on the Credit Risk of Australian consumers.

The source data used in the creation of this report was derived from illion's proprietary credit and expenditure databases.

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