



St Vincent de Paul Society
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Submission on Matters Relating to Credit Card Interest Rates

The St Vincent de Paul Society (the Society) is a respected lay Catholic charitable organisation operating in 149 countries around the world. Our work in Australia covers every state and territory, and is carried out by more than 65,000 members, volunteers, and employees. Our people are deeply committed to social assistance and social justice, and our mission is to provide help for those who are marginalised by structures of exclusion. Our programs assist millions of Australians each year, including people living with mental illness, people who are homeless and insecurely housed, migrants and refugees, and people experiencing poverty.

Background

On 24 June 2015, the Senate referred an inquiry into matters relating to credit card interest rates to the Senate Economics References Committee, and the Society was invited to make a submission on 14 July 2015.

The call by the Senate to investigate the widening gap between the Reserve Bank of Australia's (RBA) official low cash rate and the high interest charged on credit card purchases by financial institutions is long overdue, particularly for people living on low incomes. Families and individuals on income support payments have reported that they have unsustainable levels of personal debt and owe more than they can afford; primarily those on Newstart, Youth Allowance, the Disability Support Pension and, to a lesser extent, those on the Aged Pension.¹ In our work every day, we see these economically vulnerable families and individuals resort to borrowing money, selling items of value, taking out short-term pay day loans, and seeking the assistance of welfare services in addition to increasing the limit or taking out new credit cards when the offer is made available.²

This submission sets out the main ways in which credit card rates impact the most on those Australians on low incomes, before making several recommendations to ameliorate the current situation. The National Council of St Vincent de Paul Society wishes to thank the Senate Committee for the opportunity to make this contribution and welcomes further engagement regarding its content.

The Necessity of Credit for those on Low Incomes

Although the proportion of Australian households with credit card debt has declined from 57% in 2003 – 2004 to 53% in 2011 – 2012³ there has been a steady increase in the use of credit cards as a preferred payment method for most goods and services. In a society where credit card use is rapidly becoming the preferred method of payment for many goods and services⁴,

¹ National Network of Councils of Social Service, *Payment Adequacy: a view from those relying on social security payments* (2015) 20 at

http://www.acoss.org.au/images/uploads/COSS_Network_Payment_Adequacy_Report.pdf.

² Ibid.

³ Australian Bureau of Statistics (ABS), *What Types Of Debts Do Households Have? Australian Social Trends* (2014) at

<http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/4102.0main+features402014#creditcard>.

⁴ John Simon, Kylie Smith and Tim West, *Reserve Bank of Australia: Price Incentives and Consumer Payment Behaviour* (June 2009) at <http://www.rba.gov.au/publications/rdp/2009/pdf/rdp2009-04.pdf>

having a credit card equates to being able to participate in the very structure of society for those who are financially disadvantaged and marginalised.

Case Study: A Volunteer with St Vincent de Paul Society met Grace* – a sole parent who had fled a violent marriage – and her two children aged 4 and 14.

Grace felt pressured to hold on to her credit cards, even though she couldn't afford to pay much more than the minimum amount each month. Grace had been offered the cards whilst working and married, and wasn't sure if the banks would reissue her new cards now that she was a sole parent. Grace felt as though keeping her old credit cards kept her safe, allowing her to cope when the big bills came in or when the children's school had an unexpected excursion that she couldn't afford. Grace held on to her credit cards as she felt most places now require credit card payments and she needed them to survive.

*not her real name

This contributes to a form of socio-economic pressure, where low income earners are torn between holding on to the security that credit cards offer in terms of being able to manage unexpected costs, such as excessive winter bills, and struggling with excessive credit card debt and interest payments on their low incomes.

With an unemployment rate of 6% in June this year,⁵ and with many low income earners already experiencing underemployment,⁶ it is likely that more financially vulnerable people will be using credit cards to tide them over in-between periods of employment. It is ironic that, in an era where banks are still reporting growth in profits,⁷ some of the banks' most profitable customers are those on low incomes caught in the spiral of credit card debt.⁸

Different Banking Behaviours

Moreover, people on low incomes typically have banking behaviours that differ markedly to high income earners. These behaviours include making numerous withdrawals of small sums of cash in each pay-period and using cash transactions more often.⁹ As such, low income earners with savings or deposit accounts are charged multiple transaction fees and monthly account keeping fees for these withdrawals by their financial institution.

Conversely, credit card accounts attract a fixed annual fee, which at face value avoids the erosion of limited income through excess account keeping fees for small transactions. Credit cards also come with the added incentive of interest only being charged on any unpaid

⁵ ABS, *Australia's unemployment rate increased to 6.0 per cent in June 2015*, Media Release (June, 2015) at abs.gov.au/ausstats%5Cabs@.nsf/mediareleasesbyCatalogue/46DFE12FCDB783D9CA256B740082AA6C

⁶ See, eg, ABS, 'Underemployed Workers, Australia, September 2013' at <http://www.abs.gov.au/ausstats/abs@.nsf/mf/6265.0>.

⁷ See, eg, Michael Janda and Stephen Letts, 'Australian bank profits in pictures' *ABC News* (May 2015) at <http://www.abc.net.au/news/2015-05-08/australian-bank-profits-in-pictures/6454428>

⁸ The Australia Institute, *Money and Power: The case for better regulation in banking*, Institute Paper (August 2010) 9 at <http://www.tai.org.au/node/1650>.

⁹ Above n 4.

borrowings if the full amount is not paid by the due date.¹⁰ This, coupled with the various reward schemes offering bonus points for additional card holders or large purchases, makes credit card use for those on low incomes seemingly attractive.

However, the evidence suggests that in fact credit card debt is far from a cost-saving measure for most low income households. Low income earners tend to be less likely to pay off credit cards in full by the monthly due date, due to their limited incomes, and are then left paying high interest charges on debts with many obtaining additional credit cards just to make ends meet or accepting institutional offers to increase credit limits as they near their maximum credit limit.¹¹ These high interest rates, fees and penalties take a disproportionate slice of the limited budgets of low income earners. Often these financially vulnerable members of the community do not have the flexibility to change, pay-off or relinquish credit cards that were obtained during periods of employment, or through marital status, before negative changes in financial circumstances occurred.

Consumption debt

While credit card users on low incomes will use more of their income servicing that debt, it is also worth noting that this type of debt is significantly different to the debt incurred by high income earners.

Specifically, there is a marked difference between the consumption debt incurred through credit card spending (predominantly borne by those on lower incomes unable to pay off the debt) and investment debt (predominantly borne by those on higher incomes who borrow to invest), with the latter attracting lower interest rates as set by the RBA cash rate.¹² While investment debt offers the potential of future long term economic gains (for example, buying a house that will appreciate in value over time typically leaving the borrower significantly better off), credit card debt offers little in the form of increased economic opportunity, as it is a consumption debt used to purchase goods and services that are used immediately or depreciate in value immediately after purchase.¹³

As such, it is clear that the costs associated with credit card lending put pressure on everyday living, particularly for vulnerable members of the community.

Fees

In addition to Australians on low incomes being disadvantaged by credit card interest rates in this way, the consumption debt they bear isn't just limited to the direct use of credit for purchases. It includes merchant interchange fees charged by financial providers for the use

¹⁰ The Reserve Bank of Australia (RBA), *Review of Card Payments Regulation, Issues Paper* (March 2015) at <http://www.rba.gov.au/payments-system/reforms/review-of-card-payments-regulation/review-of-card-payments-regulation-issues-paper.html>

¹¹ Above n 4.

¹² Above n 10.

¹³ Australian Bureau of Statistics (ABS), *What Types Of Debts Do Households Have? Australian Social Trends* (2014) at <http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/4102.0main+features402014#creditcard>.

and convenience of credit card facilities in businesses, the costs of which are then passed on to consumers by way of increases in the purchasing price of goods and services. Research by the Society has shown that increases in the costs of basic goods and services (groceries, clothing, travel, utilities) are borne disproportionately by the poorest Australians.¹⁴

The paradox of choice

We have already outlined above how those on low incomes rely on credit cards to participate in society, and to make ends meet. A higher-level problem that Australians face is a lack of real choice over credit card providers.

Embedded within free-market neoliberalism is an assumption that market forces will enable choice and control for consumers, including consumers of credit, through increased competition between providers and consumer pressure. However, while this may work in other markets, the high degree of market concentration between Australia's dominant financial institutions has led to a greater increase in growth and profitability for most banks. Specifically, last year, ANZ recorded a profit of \$7.2 billion (an increase of 15% over the prior year),¹⁵ the Commonwealth Bank of \$8.6 billion (a 13% increase),¹⁶ Westpac \$7.6 billion (12% increase),¹⁷ and National Australia Bank \$5.3 billion (a 1.1% decrease).¹⁸ This market dominance enables banks to charge a range of fees, including: credit card fees and interest, interchange fees, merchant fees, account-keeping fees, transaction fees and penalties for late payments with little pressure from opponents.¹⁹

Similarly, free market neoliberalism assumes that those on low incomes have the financial literacy and resources to interpret the implications of their choices upon their long-term financial situation in an economically rationalist manner. However, Australians in disadvantage are less likely to have more financial literacy than those on high incomes, and are certainly in a significant power deficit when it comes to the financial knowledge of banking providers offering credit.²⁰ In addition, studies show that too many choices, such as weighing up not paying credit cards off in full versus putting food on the table, can inhibit the decision maker's ability to make rational decisions, and can also detrimentally affect

¹⁴ Gavin Dufty and Ian Macmillan, *'The Relative Price Index: The CPI and the implications of changing cost pressures on various household groups'* St Vincent de Paul Society (December, 2012) at [http://www.vinnies.org.au/content/Document/RPI_Summary_Report_Aus_Dec_2012%20\(21%20August%202013\).pdf](http://www.vinnies.org.au/content/Document/RPI_Summary_Report_Aus_Dec_2012%20(21%20August%202013).pdf)

¹⁵ ANZ, *2014 Annual Report* (2014) at <https://www.shareholder.anz.com/sites/default/files/2014-ANZ-Annual-Report.pdf>

¹⁶ Commonwealth Bank of Australia, *Commonwealth Bank: Profit Announcement: for the full year ended 30 June, 2014* (2014) at <https://www.commbank.com.au/about-us/shareholders/financial-information/2014-results.html>

¹⁷ Westpac, *2014 A Year of Delivery: Annual Report* (2014) at <http://www.westpac.com.au/docs/pdf/aw/ic/2014WestpacGroupAnnualReport.pdf>.

¹⁸ National Australia Bank, *Annual Finance Report 2014* (2014) at <https://www.nab.com.au/content/dam/nab/about-us/shareholder-centre/annual-reports/pdf-reports/2014-annual-financial-report.pdf>.

¹⁹ Above n 10.

²⁰ Above n 8.

experiences of well-being after the choice is made.²¹ When given an increase in choices (or data to be analysed), including whether and how bills are to be paid, and what sacrifices to make to pay them, the cognitive cost of weighing up each option will increase to a point where rational decision making will be impaired, and the choices made will reflect preferences rather than logical analysis of available options.²² In these ways, banking fee structures impact upon the options available for low income earners whose limited budgets are more susceptible to the impact of credit card charges, and who have fewer options for choice or control over their financial circumstances.

Conclusion

For the range of reasons outlined above, credit card interest rates and fees have a disproportionate impact on those Australians living with the most disadvantage. They reflect just one of a range of structural barriers that continue to work in Australia to stop those who are struggling from getting ahead.

For these reasons, the Society recommends legislating that credit card interest rates align with changes in RBA cash rates, and bank fees are reduced to a sufficient level as so to be affordable to low income earners. The Society also recommends acknowledging the impact of credit card interest rates on the limited budgets of those receiving Newstart, or other social security payments, and we repeat our call for Newstart payments to be increased by at least \$50 per week.

The importance of credit card interest rates cannot be overstated: the financial system is one of the driving forces of the Australian economy, now and into the next 30 years, and consumption of goods – often on credit – is a primary method that Australians use to participate in our community. It is high time that we acknowledge the impact of credit card rates on the most vulnerable, and took action to remedy it.

²¹ See, eg, Botti and Iyengar, 'The Dark Side of Choice: When Choice Impairs Social Welfare', *Journal of Public Policy and Marketing* 25(1) 27 (2006).

²² Ibid.