Chapter 1

Introduction and overview of the Australian credit card market

1.1 On 24 June 2015, the Senate referred matters relating to the economic effects of credit card interest rates to the Senate Economics References Committee for inquiry and report by 24 November 2015. The committee was asked to give particular reference to:

a. the Reserve Bank of Australia's cash rate announcement and associated changes in credit card interest rates;

b. the costs to banks, credit providers, and payments systems, including those related to:

   i. borrowings,

   ii. credit risk and default rates, and credit risk pricing,

   iii. various credit card loyalty programs, and

   iv. consumer protection measures, including reforms introduced following the global financial crisis,

c. transaction costs, including interchange fees, on the payments industry;

d. the costs to consumers, including those related to:

   i. how and when interest is applied,

   ii. minimum monthly payment levels,

   iii. various credit card loyalty programs of other users, and

   iv. card fees, including ATM and POS fees;

e. what impact competition and price signals have on the credit card market;

f. how the enforcement of responsible lending laws and the national consumer credit regime affect consumer costs;

g. how consumer choice of credit card products can be improved, with reference to practices in other jurisdictions; and

h. any other related matters.

1.2 On 23 November 2015, the Senate extended the reporting date to 3 December 2015, and on 30 November 2015 the Senate again extended the reporting date to 16 December 2015.

Conduct of inquiry

1.3 The committee advertised the inquiry on its website and called for written submissions. The committee also wrote directly to a range of government departments and agencies, companies, industry bodies, consumer groups and academics with an interest in matters relating to credit cards, drawing their attention to the inquiry and inviting them to make written submissions.

1.4 The committee received 37 submissions, which have been published on the committee's website. The committee held five public hearings: two in Sydney (27 August and 16 October 2015), one in Melbourne (3 September 2015), and two in Canberra (22 September and 9 November 2015).

1.5 The committee thanks all those who assisted with the inquiry, especially individuals and organisations that made written submissions and the witnesses who put in the time and effort to appear before the committee.

Background to inquiry

1.6 In part, the committee's interest in regard to credit card interest rates and the credit card market more broadly was stimulated by a discussion about these subjects during Senate Estimates in June 2015. In this discussion, the Secretary to the Treasury, Mr John Fraser, indicated that Treasury had recently considered the gap between the cash rate and credit card interest rates, and believed more work might be required in this space. Mr Fraser told the committee:

> My personal view is that it is an issue well worth further and deeper investigation and consideration. I am driven partly by the fact that it does seem that the people who pay these credit-card interest rates—those who do not fully pay off the amounts—tend to be people, perhaps, less capable of servicing that debt, and that worries me. I think it is something well worth considering, and we will give some further thought to it.[1]

1.7 During the same Senate Estimates hearings, officials from the Reserve Bank of Australia (RBA) were also asked about the 'stickiness' of credit card interest rates ('stickiness' meaning that credit card interest rates had not fallen in line with the fall in the RBA cash rate in recent years). Dr Malcolm Edey, RBA Assistant Governor (Financial Systems), noted that there were several factors that might help explain why credit card interest rates had not responded to a falling cash rate, including higher costs of funding (independent of the cash rate) and a repricing of risk in the post-Global Financial Crisis (GFC) period. However, Dr Edey acknowledged that the 'gap seems high and it is hard to explain why it is as large as it is'.[2]

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1 Mr John Fraser, Secretary, Department of the Treasury, *Official Committee Hansard*, 1 June 2015, p. 42. Subsequent to Senate Estimates, Treasury released a March 2015 ministerial brief and slide presentation on credit card interest rates in response to a Freedom of Information (FOI) request. Treasury, 'Briefing documents on matters relating to credit cards provided to the Treasurer and referred to in June 2015 Budget Estimates', http://www.treasury.gov.au/Access-to-Information/DisclosureLog/2015/1746.

2 Dr Malcolm Edey, Assistant Governor, Financial Systems, Reserve Bank of Australia, *Official Committee Hansard*, 1 June 2015, p. 62.

1.8 Dr Edey quite rightly made the point that Australia does not regulate interest rates, and, as such, there is no interest rate regulator. He told the committee that Australia does have 'an ACCC [Australian Competition and Consumer Commission] that can investigate uncompetitive conduct if they see it, but they clearly have not seen it in this market'.[3] It was put to Dr Edey that the issue was not so much whether there was uncompetitive conduct in the market, but whether regulatory settings were conducive to the promotion of sufficient competition to put downward pressure on credit card interest rates.[4] In part, the committee's inquiry has been directed at understanding whether existing regulatory settings in relation to credit cards are appropriate in this respect. More broadly, the committee has sought to determine what might be done to improve competition in the credit card market or otherwise put downward pressure on credit card interest rates.

Structure of report

1.9 Chapter two of this report provides a contextual overview of the Australian credit card market, with a particular focus on interest rate settings within that market. A brief overview is also provided of the responsible lending obligations as they operate in relation to credit card lending.

1.10 In turn, chapter three explores the reasons for the apparent 'stickiness' of credit card interest rates in the context of a falling RBA cash rate. In doing so, the chapter considers the extent to which apparent consumer inattention to credit card interest rates might be inhibiting downward pressure on those rates. Chapter three also assesses the explanations provided by the banks and other card providers for the continued prevalence of high interest rates despite a falling cash rate.

1.11 Chapter four examines the competitive dynamics of the credit card market and the capacity of consumers to exercise choice in that market. A key focus of the chapter is how consumers might be empowered to better value and compare credit cards and switch to a product that best suits their needs and circumstances. The potential of peer-to-peer lending as an alternative form of consumer credit is also briefly considered.

1.12 Chapter five explains how credit cards often become a 'debt trap', and suggests reforms that might help consumers better manage their credit card debt or, better still, avoid accruing it in the first place. Specific consideration is given to the efficacy of existing responsible lending obligations as they operate in relation to the credit card market, whether there is merit in requiring higher minimum repayments on credit card debt, and the role played by balance transfer offers in shaping consumer decisions about credit card debt. Chapter five also looks at financial literacy programs

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3 Dr Malcolm Edey, Assistant Governor, Financial Systems, Reserve Bank of Australia, *Official Committee Hansard*, 1 June 2015, p. 67.

4 Acting Chair (Senator Dastyari), *Official Committee Hansard*, 1 June 2015, pp. 67–68.

and tools in relation to credit card debt, and evaluates the adequacy of existing support for people experiencing financial hardship due to credit card debt.

1.13 Chapter six considers the related matters of interchange fees, surcharging and the competitive neutrality of the regulation of credit cards.