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Interest rates set to bite as households prepare to take on more debt

The strength of the local economy has many Australians gearing up to take on more debt even as interest rates are expected to continue rising and as one in two households indicate that an increase in rates would negatively impact their finances. This behaviour is in stark contrast to other developed economies – whose debt to household income ratios are similar to Australia – where consumers are paying down their liabilities in response to recent global events.

The latest Dun & Bradstreet Consumer Credit Expectations Survey* – which focuses on Australians' expectations for savings, credit usage, spending and debt performance over the September 2010 quarter – reveals that one in five households expect their debt levels to increase in the coming months, 23 percent expect to apply for new credit and 13 percent intend to make an application for a limit increase on a current account. Meanwhile, 49 percent of households are indicating that an increase in interest rates would negatively impact household finances.

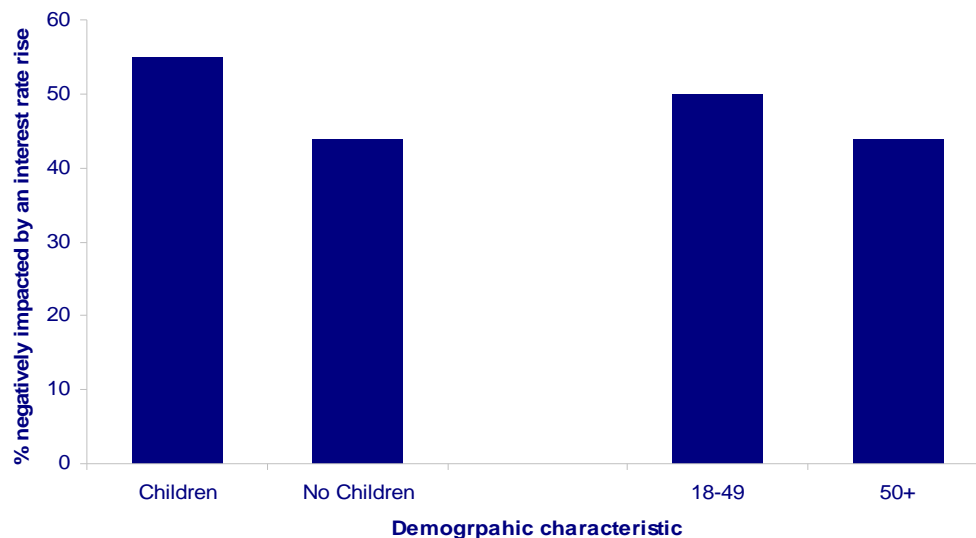
The survey found that certain demographics (18-49 years and those families with children) are more likely to experience financial stress, with these two groups having significantly higher proportions of people anticipating a need to use credit to pay for otherwise unaffordable expenses and indicating that another interest rate rise would negatively impact their household finances. Of concern, these are the same groups that are intending to make major purchases in the months ahead and they are more likely than others to fund their purchase using an interest free deal.

Close to 50 percent of households with dependents said they will use their credit card to pay for otherwise unaffordable expenses during the September quarter. This figure falls 15 percentage points to 31 percent for other households. In addition, one in four (23 percent) households with children expects their debt levels to increase in the coming months, while 17 percent of families without children have the same expectation.

Younger Australians are also demonstrating signs of potential financial stress, with 44 percent of people aged 49 and under indicating a need to turn to credit to pay for otherwise unaffordable expenses. This figure falls 19 percentage points to 25 percent for older Australians. These findings come on the back of figures from the Reserve Bank which show that average credit card balances are increasing. The average credit card balance is up five percent on a year ago – the fastest rate of increase in two years – and the latest Dun & Bradstreet survey indicates that balances may continue rising in the months ahead.

Despite showing signs of facing cash difficulties, significant numbers of families with children and younger Australians intend to apply for a new credit account in the coming months, with one in three younger Australians (18-34) intending to make an application for a new credit account. This figure falls seven percentage points for those aged 35-49 and a further 11 percentage points for those aged 50-64. This group (18-34 year olds) also has a higher proportion of people intending to apply for a limit increase on an existing account – 20 percent of 18-34 year olds have this intention, while 11 and eight percent respectively of the two older groups expect to apply for a limit increase. Meanwhile, one in three (28 percent) families with children at home intends to apply for a new credit account during the September quarter. This figure falls nine percentage points for households without dependents.

Both of these groups have also indicated that any moves by the Reserve Bank to further increase interest rates will have a negative impact on household finances. More than half (55 percent) of households with dependents said an interest rate rise would have a negative impact, while 43 percent of households without children indicated the same. Similarly, 50 percent of those aged 18-49 indicated an interest rate rise would negatively impact their finances, while 44 percent of older Australians demonstrated the same concern.



Households impacted by rising interest rates

According to Christine Christian, Dun & Bradstreet's CEO, the apparent lack of concern about the consequences of unmanageable debt levels is worrying.

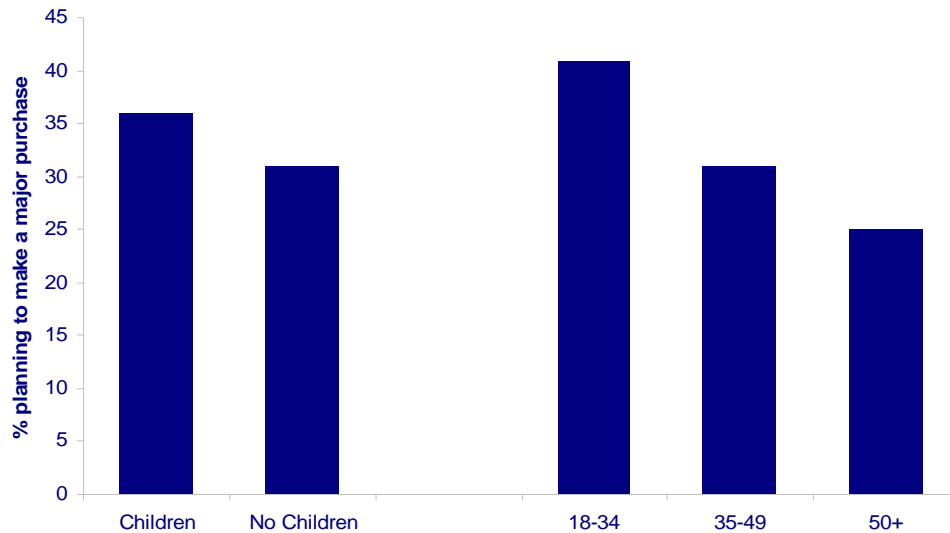
"Australia lived up to its reputation as the lucky country during recent global economic events however, our resilience as a nation and our relative lack of pain compared to other developed nations may have resulted in a failure to learn some important lessons," said Ms Christian.

"Dun & Bradstreet's latest research shows that consumers are concerned about the impact of rising interest rates on their finances. However, significant portions of Australians intend to take on more debt in the coming months and many are expecting a need to pay expenses on their credit card. These findings are supported by Reserve Bank figures which show that average balances on credit cards have edged higher in recent months.

"It is clear that some consumers are finding it tougher to make ends meet, which could in part be the result of rising home loan repayments, while for others, consumer conservatism has fallen by the wayside."

Further demonstrating the potential for younger Australians and those with dependents to experience cash pressures in the months ahead, both groups have relatively strong intentions to make a major purchase during the September quarter. Four in ten (41 percent) people aged 18-34 expect to make a significant purchase – this figure falls to 31 and 25 percent respectively for the two older groups. Meanwhile, 36 percent of families with children will make a major purchase, a figure that is five percentage points higher than households without dependents.

Savings and credit card are the most popular options for payment however, younger Australians and those with children show a greater propensity than other groups to use an interest free deal to fund their purchase. One in three younger Australians (18-34) and families with children indicated they would utilise an interest free deal – this figure compares to 11 percent for those aged 50+ and 22 percent for households without dependents.



Households planning to make a major purchase

"Australians are demonstrating significant intentions to spend in the months ahead," said Ms Christian.

"This bodes well for economic growth however, the groups with the greatest intent to spend are the groups that are demonstrating signs of potential financial stress.

"The study's findings also indicate that these demographics could find themselves in further trouble later in the year. Interest free deals and credit cards can be a trap for consumers if they aren't used correctly as consumers often find themselves unable to pay back the funds when the interest free period expires."

"Consequently, it is imperative that credit providers conduct the appropriate due diligence to ensure they provide appropriate levels of funding for each individual's situation. In addition, this process will ensure that lenders effectively manage their lending book as default risk will remain prominent in the months ahead."

**This Newspoll study was conducted online for Dun & Bradstreet in June 2010 among 1205 adults aged 18-64 years nationally.*

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