



Appendices

**Response to the
Federal Government's
Green Paper on**

FINANCIAL SERVICES AND CREDIT REFORM

**Improving, Simplifying and Standardising Financial Services
and Credit Regulation**

June 2008

Appendix 1: Cash Advance

Cash Converters short term loan product, *Cash Advance*, is:

- **short term** — average loan period is one-month
- **fixed cost** — one set fee of \$35 in the \$100, not rolled over, no compounding of fees and charges
- **small amount** – average loan is \$250
- **widely used** — 220,000 users nationally
- **used well** — 97% of loans are repaid in full

Key points in regard to Cash Converters payday lending practices are:

- **We do not require security to be provided by our customers.**
This removes concerns regarding small loans requiring high value security, repossession tactics and excessive repossession fees. There is simply no commercial value in allowing our customers to over-commit. We do not support the practice of payday loans providers taking security over customer possessions. There is no security taken or lien on goods.
- **The scheduled period of a payday loan is 30 days.**
A customer can pay early with no additional costs. If a customer requires more time to repay their loan, there is no compounding of the initial fees over time and any “interest”, fees or charges are for the term of the loan, regardless of the time taken for consumers to meet their obligations.
- **Our system is internet based allowing stores across Australia to access records.**
Our operators can connect to the entire network of Cash Converters stores, which prevents customers entering a number of our stores and taking out multiple loans without our knowledge and becoming over committed.
- **We have a robust process for assessing a customers’ capacity to repay and do not allow customers to exceed this, thus preventing debt spiral.**
A new customer is loaned a maximum of 15% of their net monthly income, depending on their total commitments. Should a loan not be repaid in the month, Cash Converters will contact the borrower and discuss.

As far as we are aware Cash Converters has never been contacted by consumer affairs or fair trading agencies to discuss a complaint about a *Cash Advance* product.

Appendix 2: Summary of Policis/Synovate Research

2.1 Consumer Profile

Of payday customers across Australia;

- more than half (51%) have incomes of more than \$34,000; and
- almost a quarter (23%) have incomes of more than \$50,000.

However, the research report referenced in this paper and compiled by *Policis* is only concerned with reporting the findings of those on incomes of less than \$35,000 pa.

8.2 Credit Profile

8.2.1 The Role of Credit

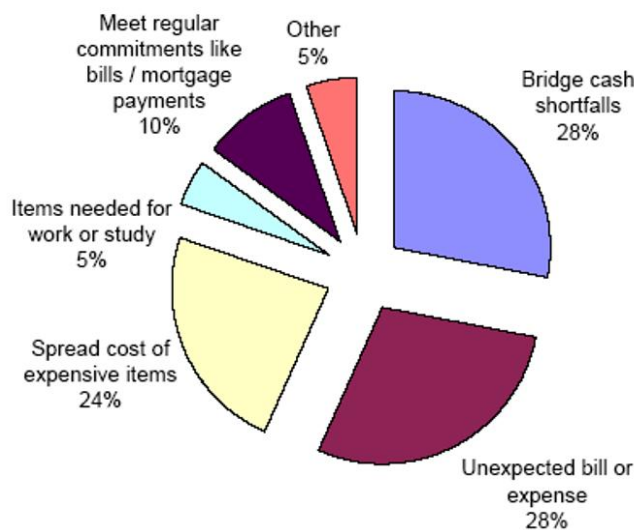
Consistent with international experience, credit in Australia plays a role in facilitating cash flow, managing peaks of expenditure, spreading the cost of large purchases and enabling the leverage of income to acquire assets. Credit has become an essential lubricant for household finances for many Australians.

Rapid growth of products specifically designed to meet the need for short term credit, such as payday lending, may in part have resulted from the consumer experience of revolving credit. The majority of those who use payday lending are making an active choice over other credit options.

Not being able to borrow from mainstream lenders came last in a list of twelve reasons given by the users of payday lending for using this type of credit, however, three in ten borrowers (29%) use payday because they cannot get credit from other lender types.

The use of high cost credit such as payday lending is undertaken to maintain commitments on mortgages and bills and to avoid default charges on loan and credit agreements, reconnection fees on utilities and overdrafts.

Figure 2a: Application of Borrowed Funds for Low Income Users in Selected Income Ranges and Payday Loan Users



8.2.2 The Demand for Credit

International comparisons indicate an irreducible need for credit with levels of demand strikingly consistent among low income households.

Low income households are likely to need credit more than affluent householders with savings safety nets. Significantly, of households with incomes of less than \$35,000 pa:

- almost half indicated they would be unable to raise between \$500 and \$700 in an emergency;
- nearly six in ten would find it difficult to manage a cash emergency without borrowing;
- 55% would be unable to renew or repair essential equipment without borrowing; and
- four in ten (42%) say they find it difficult to deal with unanticipated expenses or cash crises without borrowing.

Remember also that three in ten borrowers (29%) use payday because they cannot get credit from other lender types.

In a situation where the short term loan industry was eradicated from the credit market, the volume of consumers referred to above would rely on social credit to bridge their financial gaps. This would significantly impact on governments through increased access to Centrelink and other State agencies and similarly on not-for-profit welfare agencies within the community.

Any resulting credit vacuum would likely be challenging for the Government, and resource, time and cost intensive to fill with any sort of social lending alternative.

8.2.3 The Profile of Credit Use

Revolving credit clearly dominates patterns of credit use even amongst the lowest income groups and users of payday lending.

Consumers using payday lending include those for whom the key driver appears to be less a lack of any alternative means of borrowing, and more the product offering being a good fit with the demand for small sum instant credit borrowed over the short term – a service not always readily available from mainstream sources.

Although credit use is dominated by credit cards, low income households appear to be using a diverse range of credit products to meet a variety of needs. For those using higher cost credit, there is also a high degree of cross-over between mainstream and other credit types.

The following observations about credit use behaviours were drawn from the *Policis* research:

- Payment irregularity on mainstream credit and loan agreements is lower among payday loan users, at 2.4 missed payments per year, than among other low income credit users.
- Users of payday lending miss 20% fewer payments than all low income credit users and 30% fewer payments than those raising cash advances on credit cards.
- The average total debt for all low income credit users (households with less than \$35,000 pa) is \$7,745. For credit card users as a whole, the average total debt is \$5,175 rising to a little short of \$7,300 for credit card revolvers.
- The total value of outstanding debt is highest for the low income borrowers who are taking cash advances on credit cards, averaging \$9,600 - some 20% higher than for low income credit users.
- The total debt owed by those using payday lenders at \$7,900, is broadly in line with that for all low income credit users.

In summary, the [Policis](#) research shows that low income credit users appear better able to manage credit and have a better sense of duty for repaying debt than high income earning Australians.

8.2.4 The Concern Over Debt Spiral

In Cash Converters case, requirements for customers who take a *Cash Advance* loan are that they must be on a regular income and, as a new customer, will not be lent more than 15% of their net monthly income.

A *Cash Advance* loan does not attract escalating fees and charges and is for a set one-month period. If the loan is not repaid in the month, we will contact the borrower to discuss repayment. The loan attracts a fixed charge of \$35 per \$100 agreed by the borrower and that charge does not increase if the borrower fails to repay within the agreed period.

8.3 Credit Exclusion

As previously mentioned, the impact of credit exclusion is clearly highlighted in international research. In markets where access to credit is reduced or eliminated for those who need it most, research shows that a credit vacuum leads to:

- credit, and ultimately social, exclusion;
- a rise in indebtedness;
- a rise in the level of default including utilities; and
- the rapid rise of an illegal lending industry.

The most obvious group of borrowers likely to be impacted by credit exclusion are those that currently rely solely on high cost lenders. These borrowers, amongst the most disadvantaged, have the greatest need for credit and may suffer considerable hardship as a result.

The more likely scenario is that the industry would become filled with unlicensed and unregulated lenders likely to not only lend at significantly higher prices, but also to exhibit a series of behaviours damaging and exploitative of vulnerable low income consumers.