Analysis of Consumer Payment Hierarchies

Authors: Michael Landgraf and Barrett Hasseldine

Organisation: illion

Abstract

Credit products are designed to attract consumers at various stages of their credit and financial life-stage and each, therefore has an intrinsic credit risk. At face value, this product level risk is generally well understood by lenders; being monitored to drive both loss provisioning and capital requirements.

However, at certain life-stages, consumers will interact with multiple credit products, and in some of these cases, they may be faced with the invidious choice to prioritise one credit product over another. This is especially likely when faced with financial difficulties, either through over-commitment or broader adverse economic conditions.

Knowing which credit products are coveted and which are sacrificed when there is competition for a consumer's available funds helps lenders forecast the near-term risks faced by their various credit portfolios.

Research into this topic for consumers in Australia and New Zealand was jointly undertaken by credit bureau illion and the University of Sydney. We examine the frequency of delinquency and default for pairs of credit products held by the same consumer. From this, we uncover the credit products that are most likely to be prioritised by considering both delinquency and default propensity of competing products when only one product is ultimately sacrificed as well as the priority order of delinquencies and default events when multiple products are ultimately sacrificed. We also consider the 'time to' an adverse event for each credit product in order to understand the period of time over which consumers will attempt to hold on to their competing credit products before they ultimately fail to meet the obligations.

As illion's Comprehensive Credit Reporting account information is used as the primary source of data, the products compared in this study are Home Loans, Revolving and Fixed Personal Loans, Automotive Loans, Overdrafts, Telecom services, and Utility bills.

As well as a product focused exploration, we also consider the impact to product default risk when a consumer has a shallow or deep credit relationship with a lender as well as when they hold multiple accounts or facilities of the same credit product, either with the same lender or across different lenders.