Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry

Some Features of Car Financing in Australia

Background Paper 3

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1. Purpose of the Paper

This background paper provides information about car financing in Australia, including the range of participants and their relationship to car dealers, the relative market share of various participants, the size of the sector and the profitability of the sector. This paper has been prepared (and charts have been constructed) using public information.

This paper illustrates the following key points.

a) Indicatively, 90% of all car sales are arranged through finance, of which around 39% are financed through a dealership and around 61% are financed from other sources.
b) In the December quarter 2017, car loan payments were the largest vehicle-related expense for the ‘hypothetical household’ in both capital cities and regional areas, with repayments larger than weekly fuel costs.
c) In 2017, new finance commitments for motor vehicles were around $35.7 billion, equivalent to around 4.2% of all new finance commitments in 2017.
d) In 2017, finance commitments for motor vehicles were the equivalent of around 2.0% of nominal GDP, similar to its share in 2007.
e) Over the past 10 years there has been an increase in financing for new motor vehicles and a decrease in financing for used motor vehicles.
f) Profit margins for car dealers rely not only on car sales, but on ancillary services, including the sale of finance and insurance.
g) Delinquency rates for motor vehicle loans have increased since 2012, but remain at low levels.

2. Introduction

A car is one of the largest purchases a consumer is likely to make,[1] its significance typically second only to the purchase of a home.[2] The Australian Securities and Investments Commission ('ASIC') indicates that 90% of all car sales are arranged through finance. Of these sales, around 39% are financed through a dealership and around 61% are financed from other sources.[3,4]

According to the Australian Automobile Association (AAA)'s *Transport Affordability Index*, as at the December quarter 2017, car loan payments were the largest vehicle-related expense for the 'hypothetical household' in both capital cities and regional areas, with repayments larger than weekly fuel costs (see section 4.6).[5,6]

A 'car loan' in this paper generally refers to a personal loan with the specific purpose of buying a new or used motor vehicle. A personal loan is a low-value loan for personal use. These loans are usually payable over two to seven years.[7] There are, however, other methods of obtaining finance for a motor vehicle, including obtaining a line of credit or signing a lease agreement, which are also discussed in this paper.

3. Size of the car financing sector

According to the Australian Bureau of Statistics ('ABS'), new finance commitments for motor vehicles totalled around $2.8 billion in the month of December 2017.[8] A 'finance commitment' is a firm offer of finance from a lender that has been, or is normally expected to be, accepted by a borrower.[9]

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1 ASIC, *Car Loans*, Moneysmart (20 June 2017) <https://www.moneysmart.gov.au/borrowing-and-credit/car-loans>

2 ACCC, *New Car Retailing Industry: A Market Study by the ACCC, Final Report* (December 2017), 27 <www.accc.gov.au/system/files/New%20car%20retailing%20industry%20final%20report_0.pdf>.

3 ASIC does not provide a source for these statistics.

4 ASIC, *Regulation Impact Statement: Flex commission arrangements in the car finance market*, Attachment 2 to CP 279 (March 2017), 6 <http://download.asic.gov.au/media/4172129/attachment-2-to-cp279-published-3-march-2017.pdf>.

5 Note that the AAA's 'hypothetical household' is assumed to own a near-new vehicle financed with a car loan. See section 4.6 for further details.

6 AAA, *Transport Affordability Index* (December 2017), 7, 10, 11 <https://www.aaa.asn.au/storage/aaa-affordability-index-q4-2017.pdf>.

7 ASIC, *Car Loans*, Moneysmart (20 June 2017) <www.moneysmart.gov.au/borrowing-and-credit/car-loans>.

8 ABS, *5671.0 Lending Finance, Australia*, *December 2017* (13 February 2018) Table 9 – Finance Commitments, for Motor Vehicles: Australia, Original ($000) <http://www.abs.gov.au/ausstats/abs@.nsf/mf/5671.0>.

9 ABS, *Glossary – Commitment: 5671.0 Lending Finance, Australia*, *December 2017* (13 February 2018) <http://www.abs.gov.au/ausstats/abs@.nsf/glossary/5671.0>.

For calendar year 2017, new finance commitments for motor vehicles totalled around $35.7 billion, equivalent to around 4.2% of total new finance commitments in 2017.[10]

3.1 Share of new finance commitments

Car loans make up a very small proportion of new finance commitments, making up 4.2% of total new finance commitments in calendar year 2017, an increase from 2.7% in calendar year 2007.[11] In 2017, motor vehicle finance commitments made up around one-fifth (22%) of new personal (consumer) finance commitments, but only 3% of commercial finance commitments.[12]

Chart 1: Share of finance commitments for motor vehicles, 2007

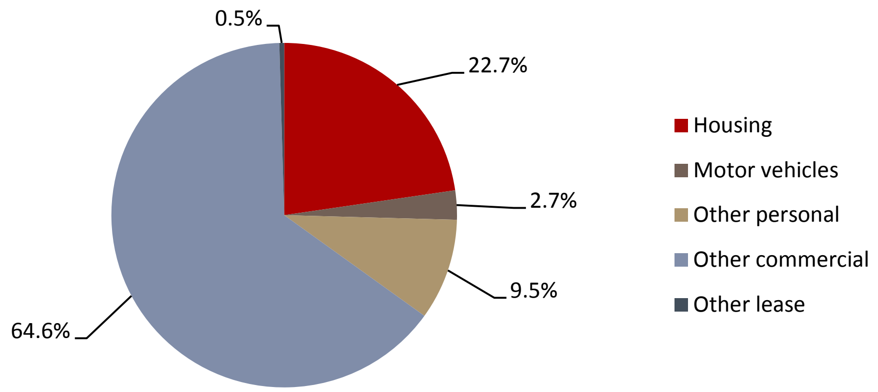
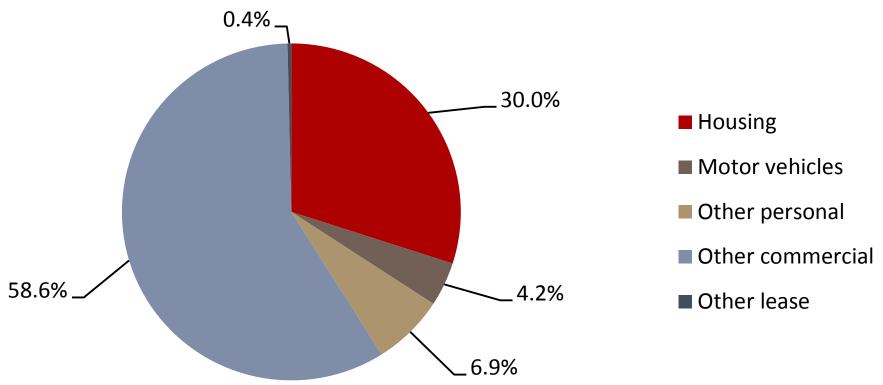


Chart 2: Share of finance commitments for motor vehicles, 2017



Source: *ABS*[13]

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10 ABS, *5671.0 Lending Finance, Australia*, *December 2017* (13 February 2018) Table 9 – Finance Commitments, for Motor Vehicles: Australia, Original ($000); Table 1 – Finance Commitments, Summary, Australia ($000) (original data) <http://www.abs.gov.au/ausstats/abs@.nsf/mf/5671.0>.

11 Ibid.

12 Ibid.

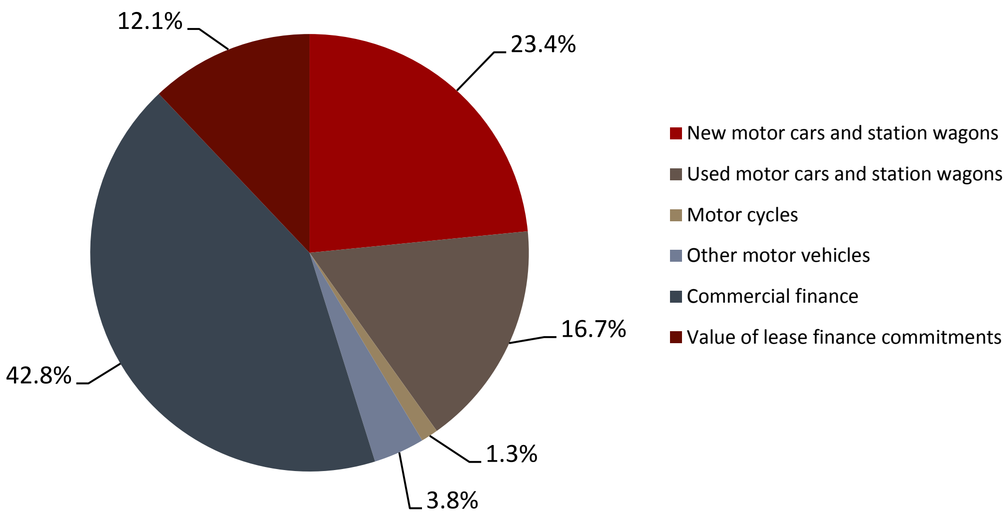
13 Ibid.

When considering the share of motor vehicle finance commitments, it is worthy of note that ABS data on new finance commitments for motor vehicles does not include commitments of revolving credit.[14] An aggregate revolving credit figure is published by the ABS but not attributed to a purpose (such as the purchase of motor vehicles). In particular, revolving credit may include dealer 'floor plan' financing arrangements, which allows a car dealer to settle a liability with a financier simultaneously with, or soon after, the sale of the vehicle to a customer.[15]

3.2 Types of vehicles financed

In calendar year 2017, almost one quarter of motor vehicle finance commitments were for new motor cars and station wagons for personal use, with around a further 17% for used motor cars and station wagons for personal use. Around 43% of new motor vehicle finance commitments in calendar year 2017 were for commercial finance.[16]

Chart 3: Shares of finance commitments for motor vehicles, 2017



Source: *ABS*[17]

14 See comments to spreadsheet in ABS, *5671.0 Lending Finance, Australia*, *December 2017* (13 February 2018) Table 9 – Finance Commitments, for Motor Vehicles: Australia, Original ($000) <http://www.abs.gov.au/ausstats/abs@.nsf/mf/5671.0>;

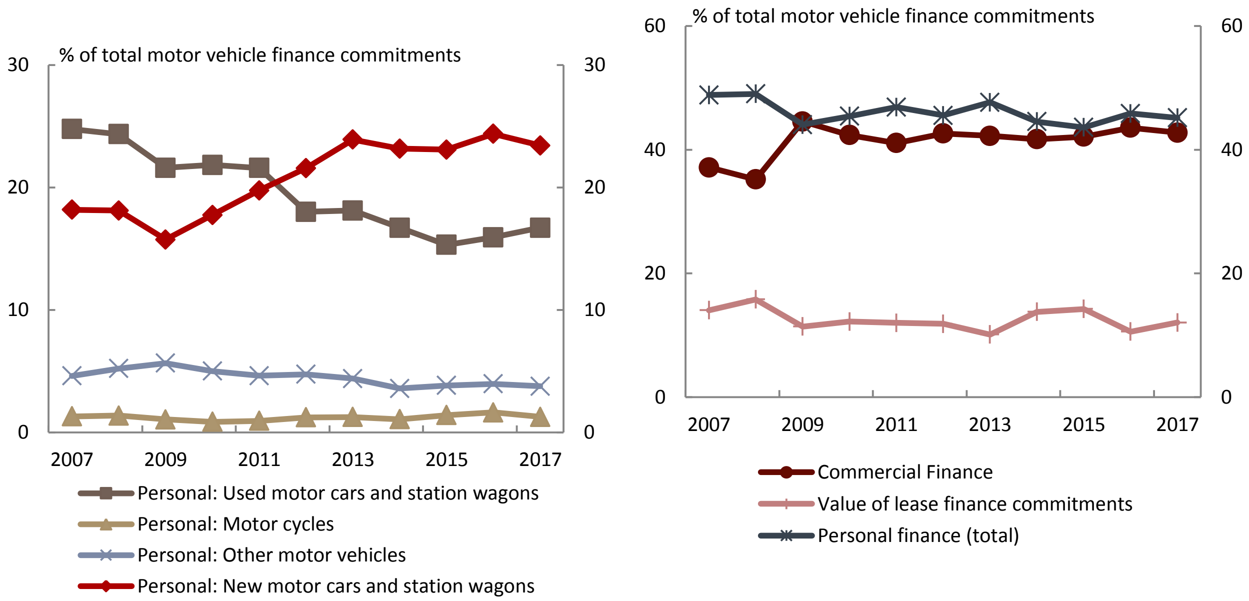
15 Australian Automotive Dealer Association Ltd., *Australian Automotive Dealer Association (AADA) new car retailing industry – a market study by the ACCC*, letter to ACCC in response to Issues Paper (21 November 2016), <https://www.accc.gov.au/system/files/Australian%2520Automotive%2520Dealer%2520Association.pdf>.

16 ABS, *5671.0 Lending Finance, Australia*, *December 2017* (13 February 2018) Table 9 – Finance Commitments, for Motor Vehicles: Australia, Original ($000) <http://www.abs.gov.au/ausstats/abs@.nsf/mf/5671.0>.

17 Ibid.

Over the past 10 years, there has been an increase in the share of finance commitments for new motor vehicles for personal use (up from around 18% in calendar year 2007 to around 23% in calendar year 2017) and a decrease in financing for used motor vehicles for personal use (down from around 25% in 2007 to around 17% in 2017).[18]

Chart 4: change in share of new finance commitments for motor vehicles, 2007-2017



Source: *ABS*[19]

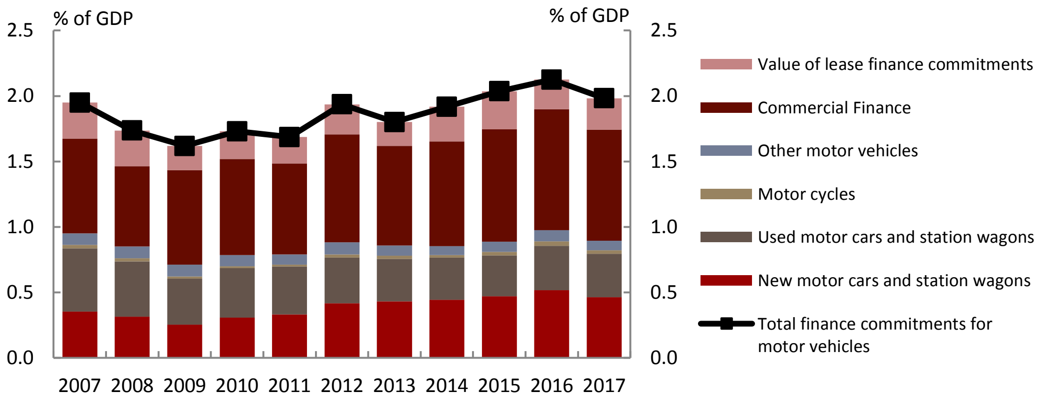
18 Ibid.

19 Ibid.

3.3 Share of the Australian economy

Finance commitments for motor vehicles as a share of nominal GDP in calendar year 2017 were similar to their share of GDP in calendar year 2007. In 2017, finance commitments for motor vehicles were the equivalent of around 2.0% of nominal GDP, compared to around 1.9% in 2007.[20]

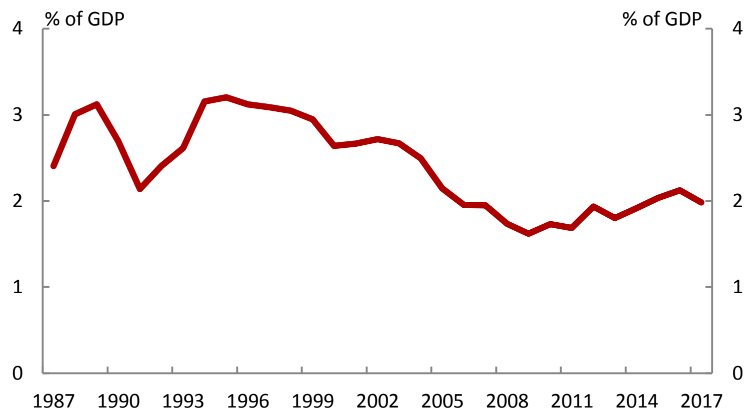
Chart 5: Finance commitments for motor vehicles, per cent of GDP, 2007 to 2017



Source: *ABS*[21]

Over a longer time period, finance commitments for motor vehicles declined as a share of GDP over the mid-1990s to late-2000s, and have broadly increased since 2010.[22]

Chart 6: Finance commitments for motor vehicles, per cent of GDP, 1987 to 2017



Source: *ABS*[23]

20 ABS, *5671.0 Lending Finance, Australia*, *December 2017* (13 February 2018) Table 9 – Finance Commitments, for Motor Vehicles: Australia, Original ($000) <http://www.abs.gov.au/ausstats/abs@.nsf/mf/5671.0>; ABS, *5206.0 Australian National Accounts: National Income, Expenditure and Product, Dec 2017* (7 March 2018), Table 1 – Key National Accounts Aggregates, GDP, current prices, original <http://www.abs.gov.au/ausstats/abs@.nsf/mf/5206.0>.

21 Ibid.

22 Ibid.

23 Ibid.

4. Participants in car financing

Participants in car financing include car dealers, dealer finance companies, lenders, finance brokers and borrowers.

Car dealers are persons or entities that sell cars to customers. A car dealer must have a licence from the relevant state government.[24] As well as selling a car to a consumer, car dealers may offer ancillary services, such as the sale of finance or insurance, for which they earn a commission on the sale of the ancillary service.[25]

Dealer finance companies have a direct relationship with car dealers, offering personal loans to customers to finance a vehicle purchase from the car dealership.[26]

Lenders provide the funds for a car loan. They can be either authorised deposit-taking institutions (‘ADIs’), such as banks, building societies, credit unions and other ADIs,[27] or other non-ADI lenders, such as money market corporations, securitisers and finance companies.[28,29]

Finance brokers act as an intermediary by matching borrowers to lenders and their loan products, assisting and advising borrowers on the loan application process and negotiating interest rates on loans, including car loans.[30]

Borrowers are persons or entities that incur a debt to a lender on agreed terms.[31]

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24 See, e.g. Consumer Affairs Victoria, *Apply for a motor car trader’s licence* (25 February 2018), <https://www.consumer.vic.gov.au/licensing-and-registration/motor-car-traders/licensing/apply-for-a-licence>.

25 ASIC, *Regulation Impact Statement: Flex commission arrangements in the car finance market*, Attachment 2 to CP 279 (March 2017), 7 <http://download.asic.gov.au/media/4172129/attachment-2-to-cp279-published-3-march-2017.pdf>.

26 See generally Stratton Finance, *Newsroom: Dealer finance vs. car loan* <https://www.strattonfinance.com.au/newsroom/dealer-finance-vs-car-loan-what-s-the-best-option>.

27 See generally Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, *Background Paper 1: Some Features of the Australian Banking Industry* (2018), 21 <https://financialservices.royalcommission.gov.au/publications/Documents/some-features-of-the-australian-banking-industry-background-paper-1.pdf>.

28 ‘Finance companies’ provide loans but cannot accept deposits. They raise funds from wholesale markets using debentures and unsecured notes from retail investors.

29 Reserve Bank of Australia, *Main types of Financial Institutions* (June 2017) <https://www.rba.gov.au/fin-stability/fin-inst/main-types-of-financial-institutions.html>.

30 See ASIC, *Glossary — finance broker* <https://www.moneysmart.gov.au/glossary/f/finance-broker>; see also generally Productivity Commission, *Draft Report: Competition in the Australian Financial System* (January 2018), 214–16 <https://www.pc.gov.au/inquiries/current/financial-system/draft/financial-system-draft.pdf>.

31 RBA, *Glossary: Borrower*, <http://www.rba.gov.au/glossary/index.html?search=borrower>.

4.1 Number of car loan providers and brokers

A complete list of car loan providers and brokers operating in Australia is not publicly available, although comparison websites such as RateCity[32] and Canstar[33] provide comparisons of car loans offered by various lenders. As there are no publicly available lists of the number or car loan providers and brokers, changes in their numbers over time are also not publicly available.

The next section discusses generally the ways consumers can receive finance for a car purchase and the entities that offer car loans.

4.2 Relationship between car dealers, brokers and lenders

Broadly, there are four channels by which a consumer can obtain finance to purchase a car:

a) through an authorised deposit-taking institution (ADI) or non-ADI lender;
b) through a finance broker;
c) through a car dealership; or
d) through a lease or similar arrangement.

Providers of car loans or their intermediaries engage in ‘credit activities’ (which includes giving credit assistance to a consumer)[34] and/or ‘acting as an intermediary between a credit provider (the lender) and a consumer’.[35] As a result, car loan providers are regulated by ASIC under the *National Consumer Credit Protection Act 2009* (Cth) and must hold an ACL or be an authorised credit representative of another entity that holds an ACL.[36]

Under the *National Consumer Credit Protection Act 2009* (Cth), credit providers, including car loan providers or intermediaries, must not enter into a contract with a consumer that is unsuitable for the consumer, such as a loan the consumer cannot repay without suffering hardship or a contract that does not meet the consumer’s requirements and objectives.[37]

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32 See generally RateCity, *All Car Loan Companies*, <http://www.ratecity.com.au/car-loans/companies>.

33 See generally Canstar, *Compare Car Loans,* <https://www.canstar.com.au/car-loans/>.

34 ASIC, *Regulatory Guide 203: Do I need a credit licence?* (October 2017), 18–25 <http://www.asic.gov.au/media/4511533/rg203-published-12-october-2017.pdf>.

35 See generally ibid.

36 Ibid 4.

37 ASIC, *Consumer Credit Regulation,* Moneysmart (20 June 2017) <https://www.moneysmart.gov.au/borrowing-and-credit/consumer-credit-regulation>. See also Australian Government, *National Consumer Credit Protection Act 2009*, s118 <https://www.legislation.gov.au/Details/C2017C00196>.

4.2.1 Finance through an ADI or non-ADI lender

Consumers can obtain personal loans to finance a car purchase from ADIs or non-ADI financial institutions. There were 147 ADIs operating in Australia as at the September quarter 2017[38], and 121 non-ADI financial institutions with assets above $50 million, including 112 finance companies, as at June 2017. The number of non-ADI financial institutions with assets below $50 million is not publicly available.[39]

4.2.2 Finance through a broker or credit intermediary

Car loans can be offered through finance brokers and credit intermediaries. Some brokers provide non-specific lending products, while others specialise in personal loans for car financing.

According to the most recent public information from ASIC, there are a total of 4,861 credit intermediaries with 36,149 credit representatives for the year 2017–18.[40] From information on credit representatives made publicly available by ASIC,[41] it is not possible to determine the corresponding figures for car loan financing specifically.

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38 APRA, Statistics: *Quarterly ADI Performance* (September 2017), Quarterly Authorised Deposit-taking Institution Performance, <http://www.apra.gov.au/adi/Publications/Documents/0512-QADIPS-Sep-2017.xlsx>.

39 Reserve Bank of Australia, *Main types of Financial Institutions* <https://www.rba.gov.au/fin-stability/fin-inst/main-types-of-financial-institutions.html>.

40 ASIC, *Cost Recovery Implementation Statement: Levies for ASIC Industry Funding (2017–18)* (October 2017), 47 < http://download.asic.gov.au/media/4506901/cris-levies-for-asic-industry-funding-2017-18-published-6-october-2017.pdf>.

41 See Australian Government, *ASIC — Credit Representative Dataset* (1 February 2018), <https://data.gov.au/dataset/asic-credit-representative>.

4.2.3 Finance through a dealer

ASIC notes that there are over 1,500 new car dealers in Australia, which operate around 2,600 outlets.[42] Car dealers can have three different roles under the *National Consumer Credit Protection Act 2009* (Cth). These are:

- holding an Australian Credit Licence (ACL);
- being appointed as a credit representative; or
- being exempt from the credit licencing regime as a 'supplier of goods and services' under regulation 23 of the *National Consumer Credit Protection Regulations 2010* (Cth).[43]

ASIC indicates that the majority of car dealers engage in credit activities by relying on the supplier of goods and services exemption, rather than as credit licensees or as credit representatives.[44] In these cases, the obligation rests on the ACL holder, rather than the car dealer, to ensure it complies with the *National Consumer Credit Protection Act 2009* (Cth).[45]

Car dealers may be associated with a branded financing company. Examples include Toyota Finance Australia Limited, MyFord Finance, Holden Financial Services and Nissan Financial Services Pty Ltd. Alternatively, car dealers may form an arrangement with a finance broker or finance aggregator, such as the arrangement between Car City and Money Now Pty Ltd.[46]

4.2.4 Finance through a lease or similar arrangement

Cars can be purchased through various types of lease or similar arrangements, as described in the table below. Often a lease or similar arrangement is most suitable for a business borrower as a result of the payment structure and/or tax arrangements. Depending on the type of arrangement, a borrower may not necessarily have the right to purchase the car at the end of the period.

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42 ASIC, *Regulation Impact Statement: Flex commission arrangements in the car finance market*, Attachment 2 to CP 279 (March 2017), 6, <http://download.asic.gov.au/media/4172129/attachment-2-to-cp279-published-3-march-2017.pdf>.

43 ASIC, *Regulation Impact Statement: Flex commission arrangements in the car finance market*, Attachment 2 to CP 279 (March 2017), 9 <http://download.asic.gov.au/media/4172129/attachment-2-to-cp279-published-3-march-2017.pdf>.

44 Ibid.

45 Ibid.

46 See generally Car City, *Finance With Money Now*, <http://www.carcity.com.au/2-pages/2-home>.

Table 1: Types of motor vehicle leases

Lease type	Description
Personal lease	Fixed rental period, often with monthly payments. At the end of the agreed rental period, the car may be purchased or the finance company may sell it as a used car.
Hire-purchase	Rental for a given period with an obligation to buy the car by making a final 'balloon payment' at the end of the agreed hire purchase period. This often suits small businesses as they can design the payments to suit the business' cash flow. The balloon payment can also be adjusted to reduce the rental payments.
Operating lease	Financing company retains ownership of the vehicle and provides the customer with exclusive use of the vehicle in return for lease payments. The finance company bears the risk of losing money on the resale of the vehicle.
Chattel mortgage	Similar to hire-purchase, the customer, usually a business, makes a series of payments and a final balloon payment. Designed for a business that uses cash accounting to allow a business to claim back GST at once, rather than gradually over the life of the lease.
Novated lease	Lease payments are paid by the borrower's employer via salary packaging, through pre-tax income. The borrower has the option of either trading in the car for another model on a new lease or paying a pre-determined buy-out balloon payment to purchase the vehicle outright.

Source: *Drive*[47]

4.3 Number of car loan providers and brokers owned by or authorised representatives of Australian Financial Services Licensees (AFSLs) that are ADIs

While there is no comprehensive list of the number of car loan providers and brokers owned by or who are authorised representatives of AFSLs that are ADIs, some finance brokers owned by ADIs are providers of car loans and leases. Some illustrative examples are provided below.

Esanda, a provider of motor vehicle financing, is a division of the Australia and New Zealand Banking Group Limited ('ANZ'). In October 2015, ANZ agreed to the sale of the Esanda Dealer Finance portfolio to Macquarie Group Limited. The sale affected finance arranged through a car dealership, rather than financing arranged with Esanda directly or through a finance broker.[48]

47 Drive, *Different Finance Types Explained* <https://www.drive.com.au/car-finance/different-finance-types-explained-20150730-ginjrk.html?trackLink=articleResultsHero>.

48 Esanda, *Sales of Esanda Dealer Portfolio to Macquarie,* <https://www.esanda.com/auxiliary/esanda-sale-announcement/>.

As at the announcement date (8 October 2015), the sale of the retail Dealer Finance portfolio was expected to be complete by 31 October 2015 and the wholesale Dealer Finance portfolio by 31 March 2016.[49]

Macquarie notes on its website that it is 'one of Australia's largest motor financiers', with car finance, sourcing and other services provided by Macquarie Leasing Pty Ltd.[50] MyFord Finance is a registered business name of Macquarie Leasing Pty Ltd.[51] ACA Research, which publishes an annual Automotive Finance Insight Report based on a survey of nearly 800 automotive finance customers throughout Australia, notes in an article from December 2016 that 'ANZ and Macquarie Bank (including Esanda) are currently the greatest beneficiaries of the broker channel'.[52]

Holden Financial Services is a registered trademark of General Motors LLC and is used under sub-licence by St George Bank, a division of Westpac Banking Corporation Limited.[53]

4.4 Profitability of the sector

ASIC notes that profit margins for car dealers relies 'not only on car sales, but on ancillary services, including the sale of spare parts, after-sale services (such as ongoing servicing) and the sale of finance and insurance'.[54] This profit margin is 'generally considered on a whole of transaction basis, rather than on individual components'.[55]

For new cars, the offer of finance as an 'after-sales' purchase is often a key part of the sales process. The Australian Competition and Consumer Commission ('ACCC'), in its 2017 market study of the New Car Retailing Industry, notes that car manufacturers 'through their own activities and those of their subsidiary distributors in Australia, earn revenues and profits from a range of activities including … the wholesale of car finance'.[56]

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49 ANZ, *ANZ agrees to sell Esanda Dealer Finance portfolio to Macquarie*, Press Release (8 October 2015) <http://news.iguana2.com/anz/ASX/ANZ/431228>.

50 Macquarie, *Welcome to Macquarie Car Loans* <https://www.macquarie.com/au/corporate/asset-finance/motor-vehicles/transferring-esanda-customers/>.

51 MyFord Finance, *myFord FINANCE,*<https://www.ford.com.au/content/dam/Ford/website-assets/ap/au/shopping/myford-finance/0369ml_caf_myFord_Finance_flyer.pdf>.

52 Nuttal, Steve, *Digital Disruption Changing Landscape of Automotive* Finance, ACA Research (6 December 2016), <http://www.acaresearch.com.au/australian-market-research-blog/digital-disruption-changing-landscape-of-automotive-finance>.

53 Holden Financial Services, *Holden Financial* Services, < http://www.holden.com.au/complete-care/finance>.

54 ASIC, *Regulation Impact Statement: Flex commission arrangements in the car finance market*, Attachment 2 to CP 279 (March 2017), 6, <http://download.asic.gov.au/media/4172129/attachment-2-to-cp279-published-3-march-2017.pdf>.

55 Ibid.

56 ACCC, *New Car Retailing Industry: A Market Study by the ACCC, Final Report* (December 2017), 29 <www.accc.gov.au/system/files/New%20car%20retailing%20industry%20final%20report_0.pdf>.

The Victorian Automobile Chamber of Commerce (VACC) notes that finance operations are considered 'an intrinsic part of the new car supply chain'.[57]

According to ASIC, car dealers have two main sources of finance-related income from a sale. Either they receive 'a range of financial benefits from lenders, including upfront commissions for individual loans, volume bonuses according to the level of business arranged with a lender, and soft dollar benefits'.[58] 'Soft-dollar' benefits are benefits received other than a basic cash commission or direct client fee.[59] Alternatively, dealers 'can charge the consumer a dealer origination fee for assisting in the provision of finance'.[60]

The ACCC notes that after-market services can often 'contribute significantly to manufacturers' and dealers' overall profitability', noting that 'dealers will be willing to sell some goods and services with a lower mark-up (including new cars) if this means they can sell more high mark-up services (such as parts, insurance and finance)'.[61]

On 7 September 2017, ASIC banned 'flex commissions' in the car finance market. Flex commissions are paid by lenders to car finance brokers (typically car dealers), allowing the dealers to set the interest rate on the car loan. The legislative instrument set by ASIC operates so that the lender not the car dealer has responsibility for determining the interest rate that applies to a particular loan. Lenders and dealerships have until November 2018 to implement new commission arrangements that comply with the new law.[62]

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57 VACC, *VACC Submission: ACCC Market Study into New Car Retailing* (14 November 2016), 4 <https://www.accc.gov.au/system/files/Victorian%2520Automobile%2520Chamber%2520of%2520Commerce.pdf>.

58 ASIC, *Regulation Impact Statement: Flex commission arrangements in the car finance market*, Attachment 2 to CP 279 (March 2017), 7 http://download.asic.gov.au/media/4172129/attachment-2-to-cp279-published-3-march-2017.pdf>.

59 ASIC, *REP 30 Disclosure of soft dollar benefits* (June 2004), 1 <http://download.asic.gov.au/media/2243023/rep30-published-june-2004.pdf>.

60 ASIC, *Regulation Impact Statement: Flex commission arrangements in the car finance market*, Attachment 2 to CP 279 (March 2017), 7, <http://download.asic.gov.au/media/4172129/attachment-2-to-cp279-published-3-march-2017.pdf>.

61 ACCC, *New Car Retailing Industry: A Market Study by the ACCC, Final Report* (December 2017), 30, 142 <www.accc.gov.au/system/files/New%20car%20retailing%20industry%20final%20report_0.pdf>.

62 ASIC, *17-301MR ASIC bans flex commissions in car finance market* (7 September 2017) <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-301mr-asic-bans-flex-commissions-in-car-finance-market/>.

4.5 Loan types

Car loans can be secured or unsecured, fixed or variable, obtained through a line of credit, from peer-to-peer ('P2P') financing or through a dealership. Each of these loan types have different characteristics, as described below.[63]

Secured car loans are secured by an asset, such as the car being purchased. As a result, the loan may have a lower interest rate. However, the lender has the right to repossess and sell the car if the borrower fails to repay the loan.

Unsecured car loans are those where the lender does not have the car or another asset as security against the money borrowed and instead relies on the borrower's creditworthiness. An unsecured car loan may be harder to be approved and generally have higher interest rates.

Either of these loans can have a **fixed** or **variable interest rate**. A variable interest rate on a car loan is less common than a fixed rate. A fixed rate loan makes it easier to calculate repayments over the relatively short timeframe of the loan.

Redraw facility/line of credit facilities may be available to consumers who already have a home loan with a lender. A redraw facility allows a borrower to withdraw funds within a set credit limit (for example, to finance a car purchase) and only pay interest on withdrawn funds.[64] However, if the borrower does not make extra repayments to cover the extra debt, this may result in higher interest payments.

Peer-to-peer (P2P) lending involves borrowing from individual investors who are seeking a return on their cash. Major P2P lenders in Australia include SocietyOne and RateSetter, which both offer personal loans which can be used to purchase a car.

Car dealership financing involves car dealers offering on-site financing for the cars they sell. Sometimes dealers will offer interest rates lower than other lenders and will manage the paperwork of the loan on behalf of the borrower.

The Australian Automotive Dealer Association (AADA) notes that 'the point of sale interest rates available on finance offered to customers by dealers as agents for the financiers compares very favourably to alternative sources of finance available to the customers'.[65]

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63 The loan types referred to in this section are summarised from Canstar, *What Type of Car Loan Should You Get?* (4 August 2016) <https://www.canstar.com.au/car-loans/car-loans-what-are-your-borrowing-options/>.

64 Canstar, *Line of Credit Personal Loans: What Are They?* (6 December 2017), <https://www.canstar.com.au/personal-loans/line-of-credit-personal-loans/>.

65 Australian Automotive Dealer Association Ltd., *Submission to ACCC New Car Retailing Industry Market Study* (21 November 2016), 17 <https://www.accc.gov.au/system/files/Australian%2520Automotive%2520Dealer%2520Association.pdf>.

However, depending on the structure of the financing contract, a 'balloon payment' may be required at the end of the loan period, which may or may not offset the savings made in interest payments over the loan period.

4.6 Types of customers that obtain car loans

While comprehensive information about consumers who obtain car loans is not publicly available, the AAA's *Transport Affordability Index* bases its estimates of the weekly costs of a car loan on a 'hypothetical household'. The AAA notes 'the characteristics of the household reflect the most common or average characteristics of the population'.[66]

The AAA's hypothetical household is:

- a couple, both employed, with children;
- the couple consisting of a 38 year old and a 36 year old;
- in a detached house;
- with two cars;
- living in a middle to outer ring suburb with a relatively high population density, good access to public transport and (where available) toll roads.[67]

Adjustments are made by the AAA for the hypothetical regional household. Largely the same as the city household, the AAA's regional hypothetical household:

- travels further than the city household;
- pays more for petrol in some locations;
- on average, earns less than their city counterparts;
- pays less for registration and insurance; and
- does not use public transport and tolls.[68]

The AAA's model assumes that one of the household's two motor vehicles is ten years old and owned outright. The other vehicle is assumed to be a near-new vehicle, financed with a car loan.[69]

According to the AAA, for the hypothetical household, average weekly car loan payments were estimated to be around $122 in both capital cities and regional areas within Australia, the largest vehicle-related expense for the household in both capital cities and regional areas, with repayments larger than weekly fuel costs.[70]

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66 AAA, *Transport Affordability Index* (December 2017), 6 <https://www.aaa.asn.au/storage/aaa-affordability-index-q4-2017.pdf>.
67 Ibid 7.
68 Ibid.
69 Ibid.
70 Ibid 7, 10, 11.

4.6.1 Familiarity of consumers with car financing

ACA Research has noted that, based on its survey data released in 2016, around 33% of buyers browsed a finance broker website and 16% of buyers used a broker to secure financing.[71] ACA Research results also showed that consumers who obtain car loans spend time considering their options before visiting a dealership. 81% of consumers researched finance options online, 76% of consumers considered their finance options prior to test driving a vehicle and 51% of consumers chose a lender prior to visiting a dealership.[72]

4.6.2 Average car loan size

Stratton Finance, a finance broker specialising in car financing, notes from its research that in 2017, the average car loan size was $39,445, the median loan size was $31,003 and the most popular loan size was $20,000. Stratton Finance also noted that men on average borrow around $5,000 more to finance a vehicle purchase than women. According to Stratton Finance, this was a result of women choosing to purchase smaller, more economical cars.[73]

4.6.3 Car loan delinquency rates

Ratings agency Fitch Ratings publishes the Fitch 'Dinkum' Automotive Asset Backed Securities (ABS) Index' – an index that approximates car loan delinquency rates based on car loans in Australia that have been securitised. Published series include an 'annualised net loss index', which gives an indication of the level of losses (or defaults) that are expected from car loans each year.[74] Fitch also measures as well as 30+ and 60+ day delinquency indices, which measure car loan payments that are 30+ days or 60+ days in arrears.[75]

The Fitch annualised net loss index, estimating the proportion of car loan defaults, has remained relatively stable since 2012, broadly fluctuating between 0.4% and 0.6%. The rate as at the June quarter 2017, of 0.44%, remained below the five-year average.[76]

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[71] ACA Research, *7 Auto Finance Insights You Need to Know: Insights from the new 2016 Automotive Finance Insights Report from ACA Research*, Automotive Insights (23 January 2017), <http://automotiveinsights.com.au/2017/01/23/7-auto-finance-insights-you-need-to-know/>.

[72] Ibid.

[73] Stratton Finance, *Who bought what? – A look at the numbers for 2017* (Insert date) <https://www.strattonfinance.com.au/newsroom/who-bought-what-a-look-at-the-numbers-for-2017>.

[74] Fitch Ratings, *Auto ABS Index – Australia: The Dinkum ABS Index, 2Q17* (11 September 2017), 7 <https://www.fitchratings.com/site/dam/investors/Auto-ABS-Index---Australia-The-Dinkum-ABS-Index.pdf>.

[75] Ibid 1.

[76] Ibid.

The delinquency indices for motor vehicle loans have increased since 2012, but remain at low levels in absolute terms. The 30+ days past due arrears rate has increased to 1.6% of loans by end June 2017 and the 60+ days past due arrears rate has increased to 0.8% of loans by end June 2017. Both indices, according to Fitch Ratings, have reached 'record quarter-end levels'. Fitch expects increased losses in the September quarter 2017, reflecting rising arrears over the past nine months. However, Fitch Ratings notes that 'losses remain low'.[77]

[77] Ibid.