Factors Affecting Credit Card Debt Payment in Malaysia

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Abstract

Credit card proliferation could bring adverse consequences to cardholders and financial institutions if the credit risk is not managed prudently. The objective of this study is to identify the factors affecting timely repayment of credit card loan in East Malaysia. Attitude towards credit, dependability, image consciousness and financial planning were found to have a significant impact on timely payment of credit card outstanding balance.

Key words: credit card debt

JEL classification: D14; D31; G21

1. Introduction

Risk associated with the mismanagement of credit risk can be far reaching. The outbreak of the global financial crisis 2008 and the collapse of the Greece economy in 2010 are both attributed to excessive leverage and poor credit risk management. Just as the world is starting to see some light at the end of the tunnel towards a full economic recovery, the Bank of International Settlement warned that debt ratios have reached a level significantly higher than they were before the onset of the 2008 financial crisis and this time it involves all major regions of the global economy (Evans-Pritchard, 2015). Among these massive credit build-up, credit card debt has been a major contributor (Chan, 2016; Silver-Greenberg, 2008). Financial experts predicted that the financial world is on the verge of experiencing a credit card debt crisis (Business Week, 2011). Credit card companies' aggressive marketing efforts have successfully lured more consumers from both the advanced and emerging nations. People own credit cards for different reasons, some used credit cards for convenience while others treat credit card loans as their "another source of income" (Dean et al., 2013; Khare and Varshneya, 2015; Shen et al., 2014). Since credit cards hearten dependability by allowing cardholders to spend their future income in advance; this fact pulls indiscipline cardholders into a debt trap. Debt trap generally leads to high level of toxic debt that erodes household financial health and

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subsequently jeopardizes the resilience of the financial institutions and the country's economy.

In Malaysia, the outstanding debt of credit card holders surged a staggering 230% (from MYR14.5 to MYR33.5 billion) for the past ten years, and credit card debt represents the second highest debt among young Malaysians (Central Bank Malaysia, 2016; Mail, 2014). According to Nielson Global Survey (2012), 18% of Malaysian paid the minimum 5% payment every month while 15% repaid more than the minimum payment. Overall, Malaysia is the second worse re-payer in the Asia-Pacific region and is one of the countries with the highest credit card outstanding debt among the developing markets surveyed. As quipped by economist Paul Krugman (2009), "Borrowed money is inherently likely to produce moral hazard" (p.63). Debt can cause both physical and mental health problems if it was not prudently managed.

Credit cards were first introduced to wealthy Malaysians in the mid-70s (Loke, 2007). During that time, owning a credit card was considered prestigious and reflecting high social status. Infatuated with the lucrative fee-based income from credit card loans, major card providers such as VISA and MASTER have relaxed the criteria required for obtaining a credit card loan for three decades since its inception. As a result, the total number of cards in circulation has surged to nearly 8.7 million in 2015 (Central Bank Malaysia, 2016). Malaysia Department of Insolvency statistics shows that around sixty people aged between 35 to 44 years old in Malaysia were declared bankrupt each day and about 5% of them declared bankrupt due to credit card debt defaults (The Star, 2013)

Against this backdrop, the objective of this study is to identify factors affecting credit cards loan payment. The empirical results could provide some useful insights to policy makers, credit card providers as well as credit cardholder in formulating a better credit card credit risk management framework.

2 . The Credit Card Market in Malaysia

Referring to Table 1, the total number of credit cards in circulation increased steadily from the 70s until 2009. A 21% drop in card numbers was reported in 2010, when an annual fee was made mandatory on all credit cards issued. This no 'free' card policy was imposed to curb high default rate and deter over-indebtedness. Nonetheless, the total credit line extended has been progressively increased over the years. Total outstanding balances and overdue amounts within three months also reported an undisrupted growth in the past decade despite interventions such as increasing income requirements for applicants and making annual fees mandatory for all cards owned.

As at the end of December 2015, the total amount of credit card debt owed by Malaysians was MYR33.5 billion. Out of these total outstanding balances, about 7% had a three-month delinquency. In Malaysia, any outstanding balances where the minimum balance has not been paid for three months are considered to be non-performing. With that in mind, initiatives from credit card holders and financial

institutions to curb the level of indebtedness and to avoid bankruptcy are crucial. The statistics exhibited in Table 1 show an alarming growth rate of the credit card overdue amounts. Therefore, it would be beneficial if some of the factors affecting the intensification of this phenomenon could be identified and monitored.

Table 1. Credit Card Statistics Malaysia

Year	Number of cards in circulation (million)	Credit line (million)	Total outstanding balance (million)	Overdue > three months (million)
2005	7.8	57130.3	14569.8	1399.4
2006	8.8	71335.8	17216.8	1905.2
2007	9.9	87980.4	20954.4	1928.2
2008	10.8	101853.1	22810.2	1996.1
2009	10.8	115080.0	24282.0	1880.6
2010	8.5	115627.5	28174.5	2067.9
2011	8.3	124109.7	30862.8	2070.6
2012	8.2	125598.1	31564.6	2028.1
2013	8.1	130449.5	32882.6	2178.0
2014	8.0	123886.2	32841.4	2493.9
2015	8.7	128753.3	33521.8	2350.9

Source: Central Bank of Malaysia (2016)

Literature Review

According to the life-cycle hypothesis, it is advantageous to borrow at a younger age to invest in human capital development like education or training instead of incurring debt for material wants. However, Dean et al. (2013) posit that Americans are prone to incur credit card debt in undesirable forms of credit despite the fact that these practices are at the expense of their future financial wellbeing. Due to this negative money attitude and spending habit, increasing portion of household incomes are dedicated to debt repayment, and households also tend to carry or revolve their outstanding debts for a longer period of time. A similar study by Rutherford and DeVaney (2009) contend that customer's attitude toward credit is inversely related to repayment default. Consumers who did not perceive or use a credit card as convenience are less likely to view credit as bad, more likely to think it is acceptable to use credit for luxury goods such as vacations and have a higher default rate. Dean et al. (2013) report that negative credit card behaviors also serve as a positive predictor for other forms of consumer indebtedness such as auto, installment, and personal loans.

In a study on Singapore credit card holders, Gan et al. (2008) contend that in addition to age and income level, credit card ownership also represents social status and self-image. This finding is confirmed by Khare and Varshneya (2015) and Wickramasinghe and Gurugamage (2009) in similar studies conducted on Indian and Sri Lankan consumers respectively. Variables such as perception of credit card,

lifestyles, credit card interest levels, consumption and saving orientations are also found to be related to credit card debt levels (Confer & Cyrnak, 1986; Hawes, 1987; Paquin and Squire-Weiss, 1998).

Park and Burns (2005) posit that credit card usage and compulsive buying is highly correlated. Compulsive shoppers are consumers who buy an excessive number of items which they do not need and cannot afford most of the time (Hoyer and MacInnis, 2001). Some compulsive shoppers demonstrate chronic and repetitive purchasing in responding to negative events in life (O'Guinn and Faber,1989). Khan, Khanam, and Imran (2009) suggest that compulsive buying is affected by self-esteem and materialism. Cardholders with negative consumer behaviors such as compulsive buying and materialism tend to exhibit dependability on the usage of credit cards as it provides a convenient way for them to spend beyond their means; treating credit card loan as their source of income.

On the other hand, studies also reported that credit attitude, i.e. preferred mode of payment, also influence credit card overdue balances. Soman (2001) discovers that comparing those who prefer to use cash or check for shopping, consumers using credit as a mode of payment are more willing to overspend and purchase high-value items. The fact that cardholders are generally stimulated to spend more compared to those who prefer to pay by cash also leads to a greater probability of accumulating higher debt and declaring bankruptcy (Pirog and Roberts, 2007; Szmigin and O'Loughlin, 2010).

In a related study conducted by Lee and Hogarthe (2000), credit cardholders are divided into those who use credit cards for convenience and the revolvers who use their credit cards as a mode of financing. A revolver is a credit card holder that pays the minimum amount on their credit card loan and carry outstanding balances for months or years. The authors found that the revolvers who used credit cards for debt payments of other loans tend to pay only the interest charges on the unpaid credit card dues. Their practices make them pay high interest on outstanding balance every month and have a much higher chance of falling into a debt trap. Revolvers also tend to carry more credit cards.

Financial planning also plays a crucial role in debt management. The Organization of Economic Cooperation and Development (2009) suggests that developing countries establish financial literacy hand in hand with the growth of the financial industries. According to the Manulife Investor Sentiment Index (2016) research, the lack of financial planning among Malaysians has resulted in them having the highest proportion of debt among the eight Asia markets surveyed. The average debt of Malaysians was about ten times that of their monthly personal income. Norvilities and Santa Maria (2002) posit that college students with poor financial literacy are associated with negative financial behaviors and higher credit card debt. Chong et al. (2010) confirm that borrowers with a monthly budget displayed better money attitude and have a lower chance of falling into a debt trap.

3. Methodology

Information required for analysis was obtained via a field survey using a structured questionnaire. The questionnaire consists of questions on demographic profile and components related to credit card usage and repayment practice. Based on the literature review, five constructs were identified: attitude towards credit, status, dependability, financial planning, and debt spiral. All these variables are measured using a five-point Likert scale where 1 = strongly disagree, 2 = disagree, 3 = neutral, 4 = agree, and 5 = strongly agree. Data was collected from Kuching and Kota Kinabalu, two of the largest cities in East Malaysia. All the respondents were credit card users. A total of 310 questionnaires were distributed, and 238 completed questionnaires were used for analysis.

For the constructs included in the survey instrument, attitude towards credit refers to the extent to which a respondent prefers to use cash (or direct debit) rather than a credit card and whether the credit card is only used for emergency purposes. The power and prestige a credit card brings to the cardholder was represented by Status/Image. Dependability refers to the extent to which a cardholder relies on credit cards as a "source of income" to pay for their expenses. On the other hand, financial planning proxies whether cardholders are rational shoppers who have a budget before carrying out purchases. Lastly, debt spiral refers to whether cardholders are revolvers who did not pay the full outstanding credit amount and would use one debt to settle other debt obligations. The dependent variable used in this study is the timely payment of outstanding credit card debt balances.

The mathematical version of the equation used in this study is stated as below:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_{5+}\mu. \tag{1}$$

Whereby, Y = Timely payment

X_1 = Attitude towards credit

X_2 = Status

X_3 = Dependability

X_4 = Availability of financial planning

X_5 = Debt spiral

4. Analysis

4.1 Descriptive Statistics

In this survey, the gender distribution of the respondents is 61.2% male and 38.8% female. About 75% of the respondents were aged between 26 to 40. Regarding educational level, respondents with secondary education predominated (59.6%), while university-educated individuals accounted for 22% of the sample.

4.2 Factor Analysis

To identify and confirm hypothetical constructs, a factor analysis was performed. Reliability and validity of the final measurement model were also assessed. From the procedure, as shown in Table 2, the Cronbach's alphas of all the constructs used in this study are found to meet the minimum requirement of 0.70 (Molina et al., 2007; Nunnally and Bernstein, 1994). This shows high internal consistency of all the constructs used in this study. In addition, scale composite reliability (SCR) that concentrates on standardized loadings and error measurement for every item also exceed the proposed values of 0.7 recommended by Nunnally (1978). The average variance extracted (AVE) were also calculated and are within the acceptable range (exceed 0.5).

Table 2. Factor Analysis and Reliability Analysis

Constructs	Indicator	Standardized loadings	Reliability [CA, AVE, SCR]
Attitude towards credit	A2	0.858	Cronbach's α =0.816
	A4	0.795	AVE = 0.627
	A1	0.753	SCR = 0.870
	A5	0.756	
Image / Status	S2	0.850	Cronbach's α = 0.812
	S1	0.829	AVE = 0.623
	S3	0.700	SCR = 0.831
Dependability	D1	0.776	Cronbach's α = 0.702
	D2	0.709	AVE = 0.529
	D3	0.703	SCR = 0.771
Financial planning	F2	0.883	Cronbach's α =0.722
	F1	0.851	AVE = 0.587
	F3	0.504	SCR = 0.801
Debt spiral	R1	0.836	Cronbach's α = 0.713
	R2	0.657	AVE = 0.558
			SCR = 0.712

4.3 Multiple Regression Analysis

After confirming on the hypothetical constructs, multiple regression analysis were performed on the model proposed to assess the relationship between the predictors and the "on time payment rate". From the analysis, 75% of the respondents indicated that they pay their credit card installment on time, while 10.5% indicated that they did not pay the minimum payment required on time. The remaining was indifferent in terms of timely payment. On the other hand, only 30.7% of the respondents stated that they have no outstanding credit card balance.

Table 3 shows the multiple regression analysis results. The independent variables in this model that are empirically proved to have a significant impact on the credit card's repayment performance are: attitude towards credit facilities, status/image, dependability, the availability of financial planning, and debt spiral. Overall, this model is significant and is able to explain 27.3 % of the variations in credit card repayment performance. A positive attitude towards credit management is seen where credit cards were used for emergency purposes and debt avoidance being positively associated with better credit card debt repayment. On the other hand, credit card users who link credit cards to self-esteem, image, and social status are associated to making payments on time to the credit card company. Those who treat credit card loan as their "source of income" tend to settle their credit card bills much earlier. Similar results are seen with cardholders who are revolvers and those who apply as many credit cards as possible to settle other debt obligations. Finally, the availability of financial planning is positively related to the timely payment of an outstanding balance.

Table 3. Multiple Regression Analysis on Variables Affecting Timely Credit Card Debt Repayment

Variables		β	t	*p*
Attitude towards credit		0.254	4.579**	0.000**
Image		0.295	5.319**	0.000**
Dependability		0.209	3.774**	0.000**
Financial planning		0.285	5.149**	0.000**
Debt spiral		0.110	1.989*	0.048*
R^2	0.288			
Adjusted R^2	0.273			
F -statistics	18.793**			
N	238			

Notes: * $p < 0.05$; **$p < 0.01$

From the results, this study concludes that a positive credit attitude (avoidance of credit) and the availability of financial planning are important factors which can be nurtured or inculcated to promote responsible credit card users. On the other hand, cardholders' dependency on credit cards as a source of spending, or revolvers, was also found to significantly affect repayment performance. A possible reason could be cardholders in debt spirals are afraid to face the consequences or the debt stress associated with failing to service minimum payments on time, thus supporting Pirog and Roberts (2007) and Szmigin and O'Loughlin (2010). Credit card holders who link credit card usage to image and status are also more conscious about meeting their payment commitments. This shows that cardholders are taking positive steps to control their social status and reinforce the self-fulling prophecy that credit card is positively linked to the well-off society. This is in-line with Khare and Varshneya's (2015) assertion that cardholders who associate credit cards to status tend to use

credit ownership in social comparison which allows them to differentiate from others.

5. Conclusion

This study examines factors related to the timely payment of credit card outstanding balances. Results show that debt avoidance attitude, image cautiousness, and adequate financial planning have a significant positive relationship with better repayment practices. While these results are expected, it was also surprising to find that cardholders who depend on credit card loans to finance their expenses and who use a credit card to settle other debts are also more inclined to pay their minimum balance or outstanding balance on time. Reasons for this group of credit card holders paying on time could be related to debt stress avoidance. This finding highlights the need for policymakers and credit card companies to formulate appropriate strategies to monitor revolvers and cardholders who exhibit high dependency to finance expenditures using credit cards. Reason being that if these cardholders were to be pulled into a debt spiral and file for bankruptcy, then the current problematic financial system would be further undermined. Furthermore, to find a better balance between profit and credit risk, credit card providers could adopt the framework of providing a higher credit limit to high-end customers and progressively take steps to reduce the credit limit of frequent revolvers. Since a correct attitude towards credit and practicing financial planning have a significant positive effect on repayment performance, society, and policy makers must endeavor to put more emphasis on financial education to curb the further souring of credit card debt.

Apart from providing an effective financial education to the public as suggested by OECD (2009), to curtail the rising credit card outstanding debt in Malaysia, the government could consider a more aggressive and comprehensive credit card reform policy with provisions to limit how credit card companies can market and charge consumers. In addition, the government could foster better product design so that information asymmetry could be reduced, especially among consumers with lower financial literacy. Future research could extend this study by introducing an objective measured dependent variable and including additional variables to advance more insights on the factors affecting credit card debt payment in Malaysia.

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