**Plastic over paper**

# China's consumers embrace credit cards as regulators rebuff new industry entrants

Thursday, July 23, 2015

**Share:**


Image: ImagineChina

Chinese consumers' credit card debt hit a record high of RMB2.55 trillion (about US$411.1 billion) in the first quarter this year according to a report from the People's Bank of China—up 35.49% over the same period in 2014.



That may fall short of America's credit card debt for the same period of US$684 billion as tallied by the Federal Reserve Bank of New York. But thanks in part to the slowing growth of China's economy, total debt from credit card borrowing was actually equivalent to 18.1% of Q1 gross domestic product, compared to only 3.8% of Q1 GDP in America.

"The jump in credit is tied to issuers feeling more comfortable with their risk management systems as well as consumer demand," said David Robertson, publisher of the Nilson Report. However, Robertson was quick to note that "100% of all credit card transactions are loans, even if the consumer pays off the entire balance when due. So, you can't assume that the great rise in credit outstanding means that the entire amount outstanding is subject to finance charges."

Even so, such a sizable boost in credit card use seems to suggest the historic reluctance among Chinese consumers to borrow might soon become a thing of the past—a likely necessity if the country is going to transition away from export dependency and high savings toward a

## DAILY NEWSBRIEFS

more

IMF calls for more financial reforms as Beijing seeks reserve currency status Friday, July 24, 2015

Wal-Mart buys remainder of online retailer Yihaodian after co-founders' departure Friday, July 24, 2015

Close to 90% of China's 668mn Internet users get online via smartphone Friday, July 24, 2015

Beijing asks for return of 153 loggers given life sentence by Myanmar court Friday, July 24, 2015

Postal Savings Bank of China ordered to accelerate pre-IPO fundraising Friday, July 24, 2015

## LATEST ARTICLES

China's consumers embrace credit cards as regulators rebuff new industry entrants
Jul 23 2015


What China-Vietnam trade balance figures miss, misstate and mask
Jul 21 2015

consumption-based growth model, per the current administration's economic blueprint. But the most recent annual figures from the People's Bank of China showed credit card payments overdue by six months or more had risen by almost 42% to RMB35.76 billion at the end of 2014, accounting for 1.53% of total outstanding credit.

That kind of growth might be why authorities put the kibosh on virtual (but very real) credit cards planned by Chinese e-commerce conglomerates Alibaba and Tencent only a week before they were set to launch last year. Since then online credit has grown slowly as companies like Alibaba, Tencent and Suning push to expand their financing capabilities in the face of ongoing opposition.

"It's the cautiousness of the regulators," said Brian Mercurio, an expert in international economic law who has studied China's credit system regulations. "China sees that if they allow essentially private companies [to become] banks without being subject to the regulations, this would lead to a bubble that would inevitably burst."

That might also help explain the unexpected hurdles thrown up in front of MYbank, an Alibaba-affiliated online bank, just before it launched in June. But the fact remains that the Beijing-backed domestic payment system operator UnionPay retains a virtual monopoly over credit cards as a result—including online transactions that use its cards. If every opportunity for efficient credit allocation beyond established brick-and-mortar venues is shot down, it could be decades, perhaps even centuries before China's consumer dream is realized.

### Risk and reward

There is no disputing that China's consumer credit has been growing: It has averaged more than 27% year-on-year growth since the financial crisis; data from the National Bureau of Statistics show that short term consumer loans had expanded to RMB3.24 trillion as of last year. Yet that may not be enough.

A policy memorandum published this year by the Paulson Institute lays out the conflict in simple terms: If private consumption continues growing at its current pace it will take another fourteen decades before it contributes as much to China's GDP as in Japan—and nearly 200 years to reach the share of GDP it provides in America.

Credit cards are one possible solution Beijing could pull from the capitalist playbook. Currently major purchases or emergency expenses require Chinese consumers to store up large amounts of money that typically get put to little productive use. Granting households easier access to credit as an alternative to precautionary savings could help disabuse China's famously high savers of their current spendthrift.

Credit cards would empower Chinese consumers as never before, allowing them to decide for themselves – without any middlemen or loan officers to get in the way – which goods and services they actually want. Who gets to skim profit off the top of all those transactions is a far more contentions question, but the latest figures from China's credit card sector show that the pot is only getting bigger.

### Debit devotees

Thanks to UnionPay's virtual monopoly on yuan-denominated card transactions in mainland China, the statistics it provides – as published by The Nilson Report in its overview of global card figures for 2014 – represent practically the entirety of the mainland's card-carrying cohort. While the state-run firm accounted for only about 10% of purchase transactions worldwide in 2014, its total transactions grew 52.3% over the previous year, and its cards accounted for 52% of the global total for credit and debit cards in circulation last year.

The vast majority of China's plastic by volume is still dedicated to debit: UnionPay credit cards totaled only 455 million out of the firm's total 4.936 billion cards, with debit cards occupying the remaining 91%. But despite making up just 9% of the total card share, credit card purchases grew 43.3% in 2014 over the previous year to a total of more than US$2.3 trillion. That's a

**Beijing's latest round of SOE reforms on track to bolster China's corporate colossi**

Jul 17 2015

**China's tech start-up sector is big on cash but short on experience**

Jul 16 2015

**China's long-dormant geothermal energy sector may soon wake up**

Jul 14 2015

respectable 34% of the country's $6.8 trillion in annual card-based purchases.

"I would say that age of the consumer matters most with credit versus debit preference," Robertson said. "Younger consumers will be more favorably disposed to credit cards and any rewards tied to their usage. Middle-aged consumers will be more comfortable with debit cards."

At just over a third, though, credit's share in China's total purchases still falls well short of the ratio for America-based Visa and MasterCard, which together saw credit account for about 56% of all purchases last year.

But those are global figures, whereas UnionPay's dominance is domestic—and the gap is slowly shrinking. Last year in China debit card transactions' share of the total fell 2.4% from 2013. Individual card use rose as well by 33.6% to just over 23 purchases per annum. And while average purchase amount fell 7.8%, at $219 UnionPay users bought well above their weight class. Visa and MasterCard purchases averaged just $83 and $84, respectively.

### Virtual plastic

Thus far China's central bank has rebuffed efforts by UnionPay's international rivals to enter the Chinese credit card market, as in 2013 when MasterCard attempted to partner with Chinese online payment platform EPayLinks to issue virtual credit cards. The cards would have allowed users to buy products online in deals settled using offshore renminbi, processed via MasterCard's own payments system.

The People's Bank of China squashed the endeavor like a mosquito before it could take off, declaring that, "no payment institution is allowed to co-operate with foreign card companies in developing cross-border payment businesses involving renminbi bank accounts or renminbi payment accounts."

Yet where regulators may oblige to block out foreign challenges, the tech sector has seen fit to begin undermining UnionPay's monopoly—and this threat is domestic. Figures from the China E-Commerce Research Center indicate that last year online commerce in China grew by 31.4% to reach a total market value of RMB13.4 trillion (roughly US$2.1 trillion). Leading the online payment services charge are Alibaba's Alipay and Tencent's Tenpay, whose online payment systems siphon a growing stream of yuan from UnionPay's landline-only outfit.

These young Turks of Chinese finance, flush with cash, have begun pushing beyond their roles as online clearing houses, one-upping one another in a competitive race the likes of which UnionPay has never had to run. In 2014 Alibaba announced it would partner with Citic Bank to offer 1 million virtual credit cards as part of its Alipay Wallet app. Less than 24 hours later Tencent boasted it would offer the exact same service in the exact same amount with the exact same bank through its WeChat social messaging app.

The People's Bank of China seized on a technical issue to delay the cards' launch. Bank officials said the bar code-like "quick response" codes that would be used to ID customers weren't secure enough. But while the bank's move favored UnionPay, Mercurio said the sudden effective ban wasn't another protective measure akin to that pulled on Mastercard.

"I do think that was probably a signal to slow down for Alibaba and Tencent," he said, noting that online finance was a new frontier for the generally cautious People's Bank of China. But said central bank has remained reluctant to embrace online financing, as when it pulled the rug out from under the Alibaba-affiliated MYbank just days before the new online venture was set to debut.

In announcing it was unsure about the face-recognition tech MYbank wanted to verify account applicants with, the central bank left the new financing outfit hamstrung. MYbank launched anyways, but without the ability to take on any customers.

### Liquidity traps

Yet even if the central bank's concerns are legitimate, the effective ongoing ban on experimentation with online credit card provision in China may be overly harsh. Both Tencent and Alibaba have said they would use customers' financial history culled from their own databases to vet card applicants. In fact, Tencent was going to give final say to its partner Citic Bank, which intended to run another, traditional credit check on all users by using the (imperfect and incomplete) credit information system run by the central bank itself.

Regulators' misgivings are not entirely without reason: Last year three members of a Shanghai family committed suicide when they couldn't find the funds to pay RMB2.4 million in credit card debt, according to state media, which labeled the phenomenon “credit card slavery.”

Even if most Chinese consumers aren't slaves to debt, they are still unwitting underwriters of the profits of UnionPay and the risk-averse financial establishment that currently decides how, and how slowly, China's available credit gets portioned out. But that kind of control may become more difficult to maintain as China's financial system internationalizes.

"E-commerce is a global matter," said Robertson, at Nilson, adding that merchants in China need to prepare for sales coming from foreign countries—especially now that the State Council has announced it will allow foreign firms like Visa and MasterCard to set up their own clearing companies in China.

"The world is getting smaller owing to the ease of online purchases. The PBOC is getting educated along with every other regulatory body worldwide," Robertson said. "Alibaba in particular has global aspirations and sellers worldwide must give consumers worldwide every payment option they desire or they will be at a competitive disadvantage." ♦

---

Author: Hudson Lockett (@KangHexin)

Banking & Finance
Business
Economics & Trade
Law & Regulation
Politics & Society
Tech, Media & Telecom