The rise of consumer credit in Latin America

June 28, 2012

In their paper, Mario Capizzani, Felipe Javier Ramirez Huerta and Paulo Rocha e Oliveira investigate the trends and prospects for consumer credit growth in Latin America.

Emerging consumers in Latin America often depend on consumer credit to obtain essential items and services.

In their paper, "Consumer Credit in Latin America: Trends and Opportunities in Credit and Store Cards," Mario Capizzani, Felipe Javier Ramirez Huerta and Paulo Rocha e Oliveira analyze the current trends in the region's consumer credit market and the prospects for growth in the sector.

Types of consumer credit

There are broadly three types of consumer credit identified in the authors' study.

- *The Virtual Wallet.* Small-scale retailers can offer emerging consumers a "virtual wallet," or informal credit, by allowing regular customers to make up differences on their next shopping trip. This is critical for low-income consumers, as it can help avoid the embarrassment of having payments declined at the point of sale.
- *Credit Cards*. Credit cards allow for purchases against a set credit limit, which can then be paid back in full or in monthly installments. They can include affinity cards and reward cards. Cobranded retailer cards, issued by retailers acting as financial institutions and without usage restrictions, also count as credit cards in this study.
- *Store Cards.* Also known as a retailer or private label card, store cards offer a "pay later" component similar to that of credit cards, but with a direct association with a

©IESE Business School

particular store or retail group.

Post-crisis recovery

The 2007-08 economic crisis adversely affected all Latin American economies to some degree. One of the immediate effects of the downturn was a tighter credit environment across the region. In Mexico, for example, pre-crisis borrowing levels are not expected to be reached until later in 2012.

Crucially, economic stability is an essential driver of consumer credit. Take, for example, the region's strongest economy, Brazil, where higher employment rates, improved income levels and a housing deficit of 6.5 million have provoked an unprecedented expansion in the construction industry.

As a result, mortgages and housing represent significant growth areas in the country.

Likewise, interest rate stability and long-term finance options have boosted growth in auto lending, despite the Brazilian government's removal of tax incentives.

Greater access

Across Latin America as a whole, much of the population has traditionally been "unbanked," making it all but impossible to access consumer credit.

However, this has started to change, and not just in Brazil. Argentina, for example, has witnessed a flourishing of longer-term financing and discounted rates, allowing those previously unable to access credit to do so.

This, coupled with aggressive marketing, produced a 38 percent increase in card lending in 2010 alone. Much of this marketing took place during the 2010 FIFA World Cup, when long-term finance options on LCD TVs were offered through credit cards.

Likewise, Peru, Mexico and Chile have sought to tap the potential of lower-income consumers by relaxing requirements to obtain credit.

The Peruvian department store, Estilos, recently began offering two months of interest-free payments and discounts at other stores, restaurants, book stores and even oral health-care clinics.

In Colombia, Colpatria introduced reward points schemes on the purchase of consumer

©IESE Business School

goods.

From retailer to banking institution

In Brazil, the retailers were the first to bring consumer credit to the masses, with their "carnês de loja" — store booklets that recorded payment dates and amounts due, which eventually progressed into the modern store card.

However, as the population has gained greater access to banking, the proportionate use of store cards has dwindled somewhat.

Across the continent, retailers have made the switch to cobranded cards in partnership with banks. For example, Banco Walmart launched a credit card in Mexico, offering a 3 percent savings on purchases at Walmart-affiliated stores.

It is likely that many store cards across Latin America will be converted into credit cards that retain the previous benefits but are more widely accepted.

Many retailers are also diversifying into other financial offerings, such as insurance and loans.

In Chile, for instance, there is an increasing trend toward allowing store cards to be used in other stores, while offering consumers extras, such as the opportunity to top up their mobile phone credit.

A bright future in store?

Despite this diversification toward cobranded cards and credit cards, store cards are still expected to grow. In Brazil, there is expected to be a 90 percent increase between 2011 and 2015.

In Mexico, store cards are expected to stage a recovery. Although this is likely to be in the low-income segment of the population and the average amount per transaction is likely to go down, transaction volumes are forecast to grow by 8 percent.

In sum, while there may be a drive toward banking-based models in consumer credit, for the emerging consumer in Latin America the store card is likely to remain a more realistic and attractive option.

©IESE Business School

©IESE Business School