COVID-19 & Debt

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We are all in this together

WHERE WE WERE

Stable economic times.

Regulators established a stable set of rules for debt collection and hardship that balanced customer protections with industry cost.

Effective management of debt was a source of competitive advantage under price deregulation.

Retailers' historical collection and write-off rates were a reasonable indicator of future performance.

Overdue payments triggered recognition of doubtful debts in retailers' financial accounts.

WHERE WE ARE

First recession in thirty years.

Regulators change expectations and disrupt the balance between customers and retailers on engagement and debt collection.

Effective management of debt now more critical than ever to retailers survival.

Rapid change in the economic and regulatory environment makes the past a poor guide to the future.

Accounting standards (AASB 9) now require *immediate* recognition of *expected future* credit losses.

AASB 9 & AER share a common objective

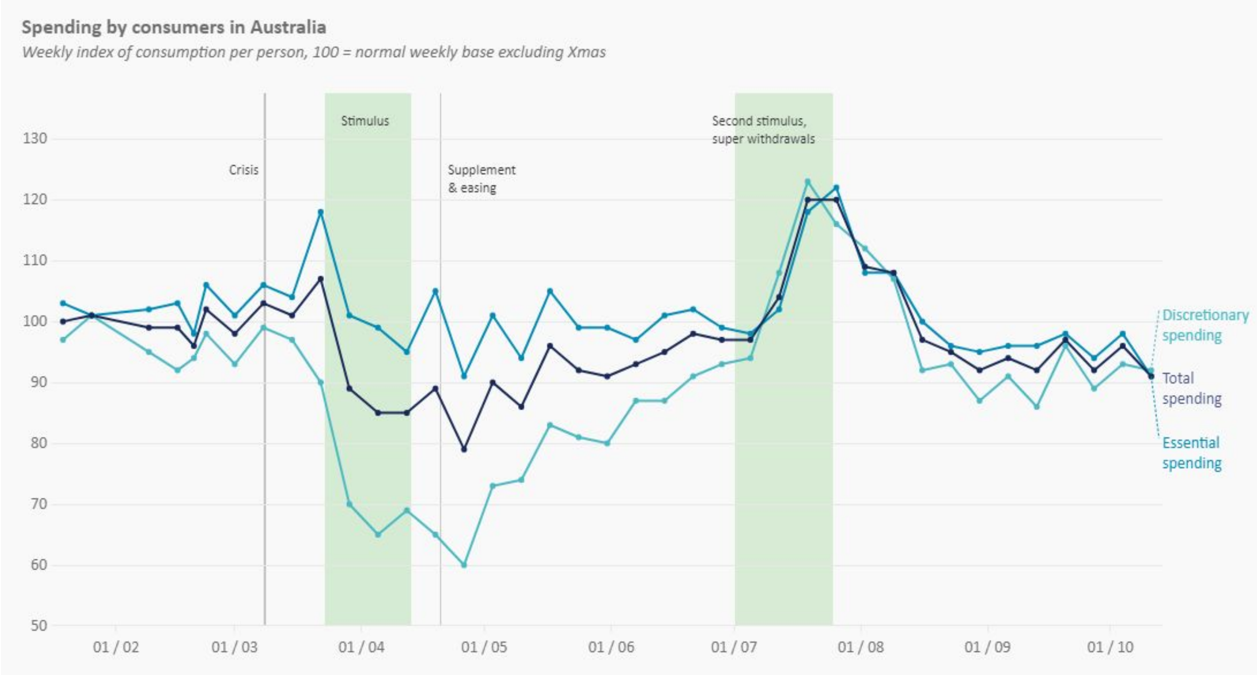
"Lifetime expected credit losses are generally expected to be recognised before a [debt] becomes past due. Typically, credit risk increases significantly before [it] is past due …. Consequently when reasonable and supportable information that is more forward-looking … is available .., it must be used to assess changes in credit risk"
Australian Accounting Standards, AASB 9

Under AASB 9 Retailers must forecast and recognise the costs of expected *future* write offs under the new accounting standards.

Similarly, the AER needs to forecast changes in expected *future* write offs for the DMO.

Retailer's assessment of expected credit losses can help inform the AER of reasonable adjustments for rising debt in the DMO.

What is happening to household budgets?



https://www.alphabeta.com/illiontracking

1. Household spending up ~20% at its peak in July (Illion & AlphaBeta).
2. Superannuation Early Release reaches $34.3b (APRA, 11 October 2020).
3. Income tax cuts of $7b in 2020/21, plus $1.3b pension top up.
4. Housing loans deferred worth $160b (APRA, 30 September 2020).
5. Overseas holiday spend 5.6m trips at $43b in 2018/19 saved or diverted (AFR, June 2020).
6. Creditsavvy, Illion, FICO report higher household credit scores than before the crisis (Australian, October 2020).

Retailers Expected Credit Losses as at June

Expected credit losses published in FY2020 Financial Statements:

FY20 $ million	AGL	Origin	Red & Lumo
Expected Credit Losses	$196.0	$162.0	$40.1
Movement year on year	$21.0	$27.0	$11.5
COVID-19 Provisioning	$20.0	$40.0	$5.0

Customer Base	3,786,000	3,851,000	1,140,000
Expected credit loss per customer	$52	$42	$35
Movement per customer	$6	$7	$10
Covid provisioning impact	**$5**	**$10**	**$4**

Bad debts *were* expected to increase in FY2021 by $5-10 per customer.

The outlook was better in June:

- Record stimulus.
- 'Bridge to the other side' by September.
- Statement of Expectations was up for review at end July.

https://www.agl.com.au/-/media/aglmedia/documents/about-agl/asx-and-media-releases/2020/2097212_annualreport.pdf pg 114
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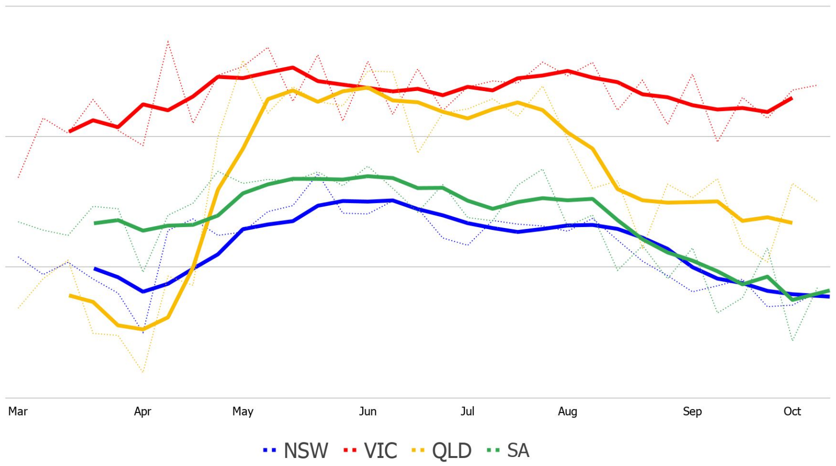
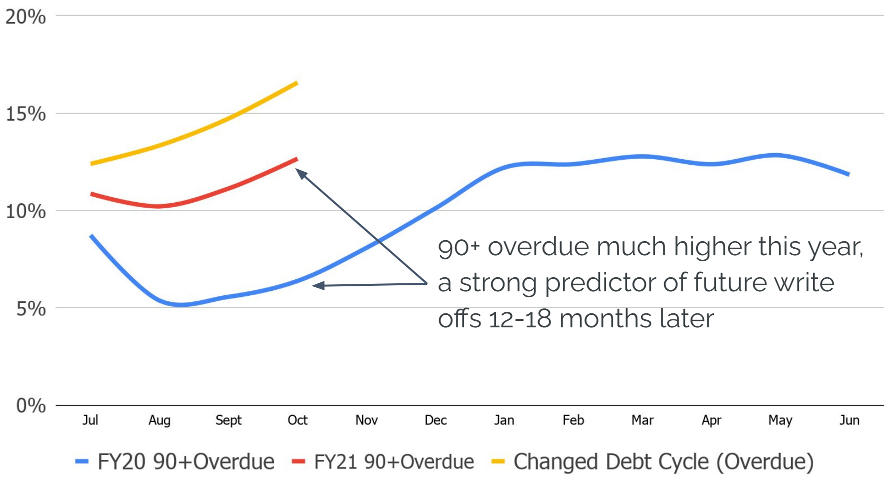
Deteriorating payment patterns since June

% Customers Paying Time



% Current Customer Receivables



- Most customers were paying as well as ever by June, but more have been missing their due date in recent months.
- Statement of Expectations (suspending disconnections) is contributing to increasing levels of debt with unengaged customers.
- Debts will continue to worsen without a return to normal processes.

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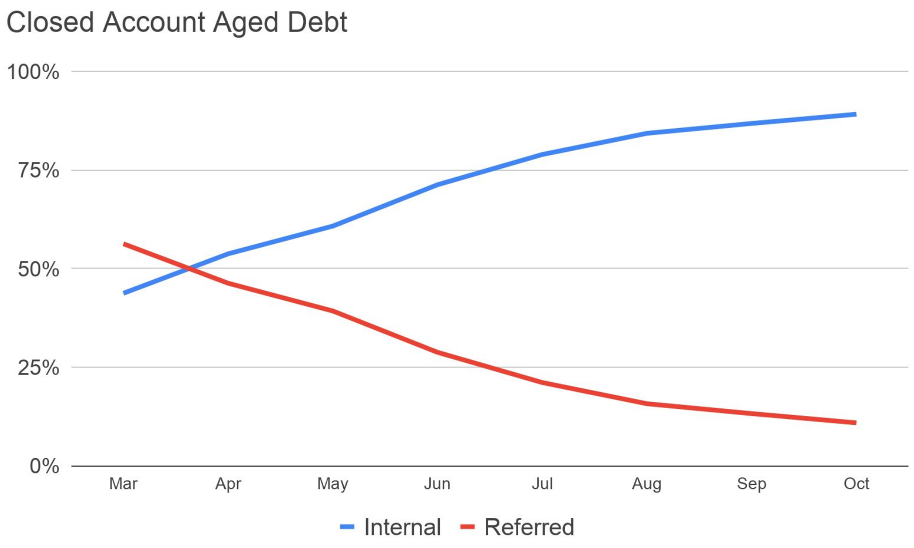
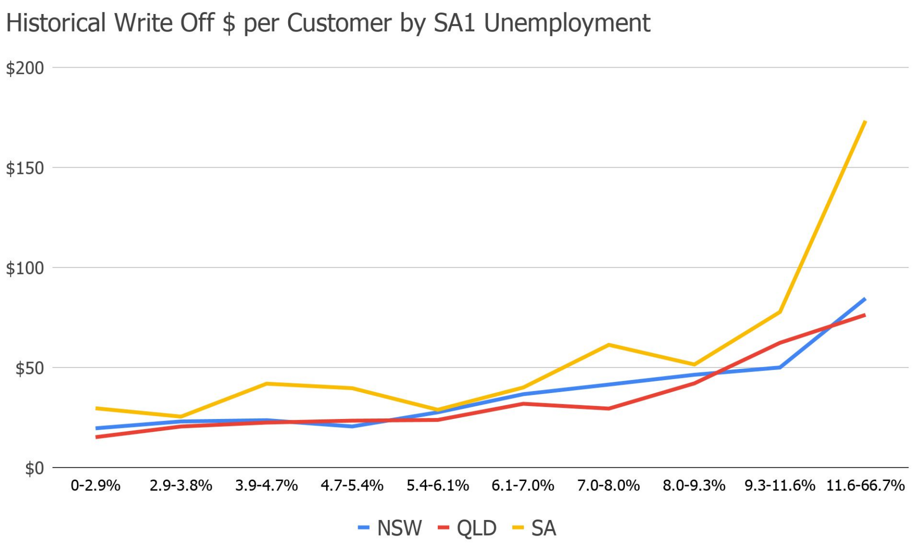
Debt and write offs will keep rising





- ❏ Customers leaving debt behind cannot be referred for collection under Statement of Expectations, driving up expected credit losses.
- ❏ This debt will continue to rise until a return to normal processes.

- ❏ Historical debt write offs correlate strongly with prevailing unemployment by SA1 region.
- ❏ Rising unemployment through 2021 will exacerbate the other worsening debt trends.

Retailers and AER need to be working together for better customer outcomes

The trend is not our friend - the Statement of Expectations is driving up customer debts faster than was expected at June.

Early engagement with customers in debt creates a win-win outcome.

Hardship programs are already in place and were working more effectively before the policy changes.

Higher debt is bad for customers, bad for retailers, and will increase prices and the DMO.

Our industry can't control the impact of rising unemployment on household debt, but retailers can help customers through challenging times given the right conditions.

Thank you