COMPETITION COMMISSION PAYDAY LENDING MARKET INVESTIGATION

INITIAL SUBMISSION OF WONGA GROUP LIMITED

12 JULY 2013

PAYDAY LENDING MARKET INVESTIGATION: INITIAL SUBMISSION OF WONGA GROUP LIMITED TO THE COMPETITION COMMISSION

CONTENTS

SECTION **PAGE**

ANNEXES

PAYDAY LENDING MARKET INVESTIGATION: INITIAL SUBMISSION OF WONGA GROUP LIMITED TO THE COMPETITION COMMISSION

1. EXECUTIVE SUMMARY

1.1 This is Wonga Group Limited's ("**Wonga**") response to the Competition Commission's ("**CC**") invitation in the first day letter dated 28 June 2013 for Wonga to make an initial submission with comments on the reasons for the reference of the case.

The market for short-term credit is a dynamic market which is growing and evolving rapidly

1.2 Unlike other, more mature, financial services markets reviewed by the CC, the market for short-term credit is changing rapidly with the emergence of new products and entrepreneurial business models such as Wonga's. This will be an important aspect of the CC's investigation for the following reasons:

(a) in markets such as short-term credit which have seen rapid developments and innovation in recent years, current market features and firm performance may be a poor indicator of the likely outcomes going forward;

(b) innovation is more likely where there is a level regulatory compliance playing field; and

(c) the evaluation of any further consumer protection initiatives must be undertaken holistically taking into account all consumer welfare impacts including those relating to innovation.

Wonga is a consumer focused provider

1.3 Wonga is seeking to challenge the established UK consumer credit providers on the basis that many consumers are poorly served by traditional products, which are not transparent, leading to customers making mistakes, misunderstanding terms or using them irresponsibly. The founding principles for Wonga are therefore:

(a) transparency – Wonga's aim to transform financial services is focused on offering services which are clear, simple to understand and where charges are not hidden. Moreover, Wonga considers that being able to compare and contrast different forms of credit is vital for consumer choice and facilitates competition;

(b) flexibility - Wonga has differentiated itself from its competitors by placing customers in control. Wonga's home page sliders let customers choose exactly how much they want to borrow and for how long, with no charges for early repayment if they change their mind;

(c) selectivity – Wonga is successful when its customers repay on the due date, not by continually extending a growing line of credit. Wonga has no interest in offering loans or providing extensions in circumstances which are likely to result in a customer experiencing financial difficulties. This is reflected in: (i) Wonga's policies, for example, a self imposed credit cap[1] and a limit on rollovers to a maximum of three; (ii) Wonga's highly sophisticated automated and real-time systems for assessing affordability; and (iii) key performance indicators, in particular, the very low proportion of loans which are extended (8.5 per cent in 2012), and low default rates at around [✂] per cent of principal lent in 2012.

---

1 First time borrowers are never allowed to borrow in excess of £400, while existing customers are eventually limited to a maximum of £1,000.

1.4 Wonga considers that its success in expanding in recent years is attributable to this customer-focused business model coupled with a very innovative technological solution which has given Wonga a competitive advantage. Importantly, Wonga does not perceive that it is significantly disadvantaged in undertaking proper affordability checks and by being compliant more generally because of the risk of losing business to those who are less compliant. Moreover, Wonga does not rely on the recoupment of costs through rollovers or the use of continuous payment authority ("CPA") to mitigate the risks of poor lending decisions – these risks are mitigated through Wonga's investments in technology to ensure rigorous and accurate upfront and ongoing assessments.

Wonga welcomes a process which will allow practices in the industry to be scrutinised leading to greater consistency and providing a better platform for innovation

1.5 Wonga is aware that other business models exist which place less emphasis on consumer protection. Wonga considers that more consistent compliance with the regulatory framework is needed to provide a stronger platform for competition and innovation by Wonga and others by levelling the playing field. The investigation could play a useful part in steering the industry towards this outcome and Wonga will engage actively with the CC to assist in this regard.

The investigation should encompass how consumers use and access all forms of short-term credit including overdrafts and credit cards

1.6 Wonga welcomes a rigorous, evidence-based approach to market definition by the CC. Wonga does not consider that the OFT has carried out sufficient empirical work to support its market definition conclusions. In particular, Wonga considers that there is substantial evidence that many customers do see alternative sources of credit as genuine substitutes to payday loans. Moreover, there is clear scope for supply-side substitution as well as evidence of actual entry, which also supports a wider market definition which covers a range of short-term consumer loan products.

2. OVERVIEW OF THE MARKET FOR SHORT TERM CREDIT

2.1 The supply of short-term credit is a dynamic market which is growing and evolving rapidly. Customer protection is enshrined in Wonga's policies but Wonga is aware that other business models which place less emphasis on consumer protection exist. This section considers:

(a) the dynamic nature of the short-term credit market as evidenced by the emergence of new products and entrepreneurial business models such as Wonga's which couples commercial success with strong consumer protection policies;

(b) Wonga's commitment to responsible lending; and

(c) the need for an effective regulatory framework through better compliance.

Dynamic market

<u>A dynamic market with significant growth and new entry</u>

2.2 The short-term credit market is growing and evolving rapidly. The CC has commented on the growth of certain forms of specialist non-standard credit lending (including payday loans, pawnbroking and credit unions) in its evaluation of the remedies introduced following the home credit market investigation.[2] The OFT also acknowledges "*a very large*

[2] "*Some of the decline in non-standard lending by mainstream providers has been replaced by growth in other forms of specialist non-standard credit lending – payday loans, pawnbroking and credit unions*", Understanding past market investigation remedies, Home Credit, CC, February 2013, page 15, para 65.

increase in the volume and value of payday loans in the UK" following significant new entry in recent years.[3]

A response to demand from consumers poorly served by traditional lenders

2.3 Forms of non-standard credit lending have emerged to meet demand from consumers who, in many cases, are poorly served by traditional lenders. Wonga offers small, short-term loans (online and via smartphones only) in competition with a range of alternative short-term credit products offered by banks, high street lenders, other cash advance websites and other sources of short-term credit.

2.4 A founding principle for Wonga is that its products are transparent, in contrast to many traditional financial products (such as bank accounts) which are ostensibly "free" or have low headline rates but where revenue is generated through charges which are not transparent and by keeping consumers in long-term debt. Wonga's code of practice states as its mission the following:

> "*Our mission is to solve consumers' occasional, urgent and short-term cash flow problems with an equally short-term solution. We base our commitment to responsible lending on transparency, flexibility and extreme selectivity - believing it's possible to provide credit in a way that suits consumers, not lenders.*
>
> *We feel that for too long traditional lenders have been devising and marketing products with low headline rates, whilst generating most of their revenue by keeping consumers in long-term debt, or through charges hidden in the small print. Such is the lack of transparency that many financial products, including free bank accounts, would not be commercially viable without a significant portion of customers making mistakes, misunderstanding terms or using them irresponsibly.*"[4]

2.5 Wonga has sought to differentiate itself from its competitors by placing customers in control. For example:

(a) unlike payday lenders, Wonga offers short-term loans which are not tied to payday or pay cheques;

(b) Wonga charges daily interest rather than fixed fees-per-hundred charged; and

(c) Wonga's home page sliders let customers choose exactly how much they want to borrow and how long for, with no charges for early repayment if they change their mind.

Entrepreneurial business models and ongoing innovation

2.6 Wonga's backers have taken significant risks in supporting an entity which is using data and technology to revolutionise financial services, and which seeks to challenge the established UK consumer credit and business credit providers. When Wonga launched its online offering in 2007, it was the first fully-automated risk, ID and decision system in the world. Wonga's founders were unable, initially, to raise finance in the UK and their first line of credit was from the [✂]. Since then Wonga has grown but remains an entirely equity funded business. As noted by Robert Peston "*It is, for example, funded exclusively with equity capital, or £100m genuinely at risk of being lost if things go wrong.*"[5]

---

3 Payday lending, Final decision on making a market investigation reference ("OFT's decision document"), OFT, June 2013, para 3.102

4 http://www.wonga.com/money/downloads/code-of-practice.pdf at Annex 1.

5 http://www.bbc.co.uk/news/business-23078746 at Annex 2.

2.7 Wonga's commitment to innovation and its success in this regard is demonstrated by the following:

(a) Wonga has won several awards relating to its technical innovation. For example, Wonga is the only business to date to have featured in the Top 3 of the Sunday Times Tech Track in consecutive years. It was also the Digital Entrepreneur winner at the 2011 Media Guardian Innovation Awards and Credit Risk Team of the Year in 2009;[6]

(b) a significant proportion of Wonga's staff of 500 are devoted to developing new products and new markets;

(c) Wonga has diversified into new business lines, for example, a business loan product and an e-commerce product; and

(d) Wonga has expanded internationally and now provides short-term loans in South Africa, Canada, Poland and Spain.

2.8 Wonga's incentives to innovate are strong because other key players in the industry are also innovative (particularly in relation to flexible loan products which place customers in control), and therefore innovation is a key element of competition. For example, QuickQuid has recently launched an unsecured loan product which allows customers to choose both the loan amount (up to a personalised credit limit) and the payment timescale (up to a maximum repayment term of 10 months).[7]

<u>The need for a regulatory framework which encourages, not stifles further innovation</u>

2.9 The OFT suspects that irresponsible lending has "*its roots in the way competition works*".[8] Wonga, however, couples strong consumer protection policies with competitive success because, by dealing fairly and transparently with customers, it delivers a service which is valued and which engenders loyalty. Wonga provides a counter-example, therefore, to the OFT's assertion that "*those firms which invest more time and effort in complying may be placed at a competitive disadvantage to those which invest less*".[9]

2.10 Business models are evolving in light of improved understanding of consumers' needs. Wonga considers that more firms will seek to emulate Wonga's successful pro-consumer business model such that dynamic competition will deliver better outcomes for consumers. More consistent compliance with the regulatory framework is needed to provide a stronger platform for competition and innovation by Wonga and others by levelling the playing field.

Wonga's commitment to responsible lending

2.11 Wonga is a customer-focused business which has given careful consideration to many of the issues identified by the OFT as reflected in strong consumer protection policies which distinguish Wonga from many traditional payday lenders. For example:

(a) as regards <u>transparency</u>, the simplicity and transparency of the product offered by Wonga is of central importance to customers and Wonga considers itself to be an industry leader in terms of transparency. The website makes it clear to customers on the very first page how much a customer will pay back (i.e. the total cost of borrowing) before they commence the application process and information is

---

6 Wonga's various awards are listed on its website at http://www.wonga.com/money/wonga-awards/.

7 https://www.quickquid.co.uk/mediaroom/new-quickquid-flexcredit-provides-customers-more-credit-flexibility-and-control/

8 OFT's decision document, para 3.23.

9 OFT's decision document, para 1.14.

available a click away from the home page on what happens in the event that the customer does not have sufficient funds to repay on the due date. Wonga's customer survey shows that 95 per cent consider that information is conveyed by Wonga well or very well. Only 2 per cent of customers consider that Wonga does a poor (or very poor) job of conveying information (less than a tenth of the proportion who feel this way about their high street banks);[10]

(b) as regards checking affordability, Wonga has developed highly innovative digital systems for performing these checks (which are described below). This has allowed Wonga to meet its twin objectives of being a responsible lender (which also makes business sense because Wonga is only successful by lending to customers who can afford to pay it back), and giving customers the speed and convenience that they demand. For Wonga, there is no trade-off or inconsistency between these objectives; and

(c) as regards loan extensions (which Wonga limits to three), Wonga aims to achieve an appropriate balance between customer benefits from the ability to rollover/refinance where necessary, and responsible lending. Wonga has no interest in providing extensions in circumstances where they are likely to result in financial difficulties, and Wonga's policies and results are consistent with this aim. In particular, Wonga has a policy of undertaking a thorough re-assessment of affordability before the term of the loan is extended. Wonga provides the information customers require when considering whether to apply for an extension, highlighting any risks they may face, the costs associated with extension and the requirement that customers must pay the interest and fees on the original loan. Only 8.5 per cent of Wonga's loans in 2012 were extended and Wonga does not pro-actively encourages extensions.

2.12 Wonga welcomes a process which will allow practices in the industry to be scrutinised leading to greater consistency and providing a better platform for innovation. This should encompass how consumers use and access all forms of short-term credit including overdrafts and credit cards (as discussed in the market definition section below).

The need for an effective regulatory framework

2.13 Wonga acknowledges that business models exist which are non-compliant with the regulatory framework (and are yet sustainable) and there is a need for enforcement action to address this.

2.14 The OFT's enforcement action (following the compliance review) will continue in parallel with the CC's investigation. Wonga is aware, for example, that lenders inspected by the OFT were given 12 weeks from receiving notification from the OFT to demonstrate that any non-compliance in policies and procedures has been addressed. The OFT has received responses from 19 of the 50 lenders, including two that have surrendered their consumer credit licences and three others that are no longer offering payday loans. The impact on the short term credit market of the "shake out" of non-compliant lenders and improvements in conduct among the remainder will need to be closely monitored.

2.15 From April 2014, when the FCA assumes responsibility for consumer credit regulation, Wonga expects to see stricter enforcement of the current standards enshrined in consumer credit and consumer protection legislation as well as the OFT guidance documents. The FCA regime will also place more stringent requirements on firms in terms of compliance, systems and controls and Wonga anticipates that the FCA will take a more pro-active role than the OFT in monitoring the activities of regulated firms.

[10] Populus Customer Survey, March 2013, slide 13 at Annex 3.

2.16 Whilst market exits and a lower rate of entry are consistent with a regulatory regime which is enforced more effectively, this is a benefit from a consumer protection perspective and does not preclude competition amongst the remaining compliant players; as noted above, Wonga anticipates greater competition where the regulatory compliance playing field is levelled.

3. MARKET DEFINITION

3.1 Wonga believes that a wider market definition, encompassing a range of short-term credit options, is required for the CC's investigation. Currently, the OFT has defined the market as:

> "*the provision of small-sum cash loans marketed on a short-term basis, not secured against collateral, including (but not limited to) loans repayable on the consumer's next payday or at the end of the month and specifically excluding home credit loan agreements, credit cards, credit unions and overdrafts*".[11]

3.2 Wonga welcomes a more rigorous, evidence-based approach to market definition by the CC, and notes that the OFT has not carried out any empirical work to support its market definition conclusions:

(a) The OFT cites a few research sources in evaluating the demand-side substitutability between payday loans and other forms of unsecured small-sum credit, but fails to take into account evidence demonstrating that: (i) many alternative sources of credit are available to online payday loan customers; (ii) customers do see these alternatives as substitutes; and (iii) the effects of switching in response to a small but significant non-transitory increase in price ("SSNIP")[12] could be significant.

(b) The OFT acknowledges that there is scope for supply-side substitution[13], but has not widened its proposed market definition accordingly.

3.3 Given these points, Wonga believes that there are risks in defining the scope of the reference too narrowly. These point are outlined in more detail below.

Many alternative sources of credit are available to online payday loan customers

3.4 The OFT acknowledges that there are many alternative small-sum credit products,[14] and that "some" consumers may use one or more of these other products.[15] In fact, the Bristol University study found that 76 per cent i.e. a large majority of online payday customers also used at least one type of mainstream credit.[16] This is confirmed by Wonga's own customer research, which found that [✂] per cent of its customers have access to bank overdrafts, [✂] per cent to credit cards and [✂] per cent to each of traditional payday lenders, bank loans and other forms of credit.[17]

3.5 However, the OFT claims that these alternatives may not be available at the time of borrowing (for example, because they have been exhausted), citing the Bristol University

---

11 OFT's decision document, para 1.2.

12 Based on using a hypothetical monopolist test, as per OFT and CC guidance. OFT (2004), Market Definition, Competition Guideline 403; CC (Apr 2013), Guidelines for market investigations: Their role, procedures, assessment and remedies, CC3 (revised), para 138.

13 OFT's decision document, B18.

14 See for example the list at para B5 of the OFT's decision document.

15 OFT's decision document, para B6.

16 The impact on business and consumers of a cap on the total cost of credit ("the Bristol University Research"), Personal Finance Research Centre University of Bristol, 2013, Table 4.4.

17 Populus Customer Survey, March 2013, slide 21 at Annex 3.

finding that 30 per cent of online payday customers were unable to access alternatives at the time of applying.[18] This ignores evidence from the same study that a sizeable 24 per cent of online payday customers did have the option to tap unused mainstream borrowing capacity,[19] where the proportion would be expected to be even higher if all alternatives had been examined by the study.

3.6 As the CC is aware, the relevant analysis in assessing demand substitutability is of marginal customers (i.e. the one quarter of online payday customers with unused mainstream borrowing options), where these customers are more likely than others to see other products as substitutes and to switch in face of a SSNIP or be willing to stop consuming the product without substituting. In focusing on the infra-marginal customers who may not switch, the OFT has understated the availability and importance to payday customers of many alternative credit sources.

Customers do see alternative sources of credit as substitutes

3.7 There is also substantial evidence that customers with access to alternative sources of credit do see these as genuine substitutes to payday loans. The OFT doubts that payday loans are functionally similar to other alternatives and are thus perceived by many customers as substitutes (citing an observation in a Policis study,[20] general features of payday loans[21] and anecdotal comments from meetings with payday lenders[22]). In doing so, the OFT appears to ignore considerable evidence to the contrary, for example:

(a) the Bristol University study found that 18 per cent, i.e. almost one fifth of online payday customers, compare the costs of loans from non-payday providers before choosing to take out their loan.[23] A SSNIP (e.g. 5-10 per cent price rise) is likely to induce further search and switching by some customers who indicated they would not find this worthwhile at current prices;

(b) customers do seem to perceive payday loans as functionally similar to other types of short-term credit. For example, the Bristol University study shows that customers of payday lenders and pawnbrokers used their funds for similar activities.[24] Furthermore, customer responses to questions such as whether the form of short-term credit is "*a good way to raise cash quickly*" and "*it makes it easier for me to manage when money is tight*" were very similar across the different short-term credit products surveyed (home credit, pawn broking, and retail and online payday loans);[25]

(c) in responding to customers' demands, payday lenders perceive themselves to be competing against mainstream and other credit products. For example, Wonga's own consumer research actively compares the performance of its lending product to mainstream and other credit products such as credit cards, overdrafts, bank loans and traditional payday lenders;[26]

(d) it is clear that industry commentators treat payday loans as an alternative to unauthorised overdrafts. Many reports and articles directly compare the charges

---

18 OFT's decision document, para B8.

19 The Bristol Research, page 24.

20 OFT's decision document, para B9.

21 OFT's decision document, para B11.

22 OFT's decision document, para B13.

23 The Bristol University Research, Table 5.1.

24 The Bristol University Research, Table 4.1.

25 The Bristol University Research, Table 4.2.

26 Populus Customer Survey, March 2013 at Annex 3.

that customers would incur when taking out these two products. For example, the Chartered Institute for Securities & Investment has undertaken research which compares the cost of taking out a £200 unauthorised short-term overdraft from a typical payday lender, Lloyds Bank and Nat West;[27] and

(e) the above evidence is consistent with how Wonga views its business. For example, in a presentation of the Wonga business to journalists in early 2013, Niall Wass (Chief Operating Officer of Wonga) included a comparison of Wonga's charges for a given loan to that of its competitors. This included the details of the charges associated with use of unauthorised overdrafts based on calculations from Money Saving Expert.[28]

The effects of switching in response to a SSNIP could be significant

3.8 Payday customers appear to be highly price sensitive, contrary to the OFT's interpretation of the available evidence. The OFT cites the Bristol University study finding that "only" 46 per cent, or almost half, of online payday customers compared the costs of borrowing before taking out their loan.[29] Furthermore, the OFT ignores evidence in the same study that a majority (55 per cent) of payday customers would not have been likely to take out their loan in the event that the price was higher.[30]

3.9 In addition to the evidence referred to above that customers do perceive alternative sources of credit as substitutes, there is also a real prospect of price sensitive customers switching, given that the costs of payday loans and forms of mainstream credit such as unauthorised overdrafts or credit cards can be comparable. As noted above, the Chartered Institute for Securities & Investment identified that £200 borrowed from a payday lender would cost £66 compared to a charge for borrowing the same amount by way of an unauthorised overdraft of £84.22 for Lloyds and £110 for Nat West.

3.10 Combining price sensitivity with the many alternatives to which payday customers have access, the cumulative exposure of payday lenders to lost customers in the event of price increases above the competitive level could be significant, even if switching to any one product may appear low.

3.11 Moreover, even modest switching by customers is likely to render a SSNIP unprofitable.[31] This is because the structure of the payday lending business is likely to include a high proportion of fixed costs, such as those relating to overheads, IT, premises, regulatory functions and brand investments, which payday loan revenues must cover. This implies a low proportion of variable costs in the business, so that even a modest loss in customers would render a price rise unprofitable.[32]

3.12 Given this evidence, other short-term credit products are considered to pose an effective constraint on payday lenders, and should be included within the relevant product market.

---

27 http://www.cisi.org/bookmark/genericform.aspx?form=29848780&URL=87925819 at Annex 4.

28 'Introducing Wonga', presentation to journalists, Niall Wass, early 2013 at Annex 5, slide 13.

29 OFT's decision document, para 3.69.

30 The Bristol University Research, Figure 5.1.

31 A key step in applying the hypothetical monopolist test is to carry out a critical loss assessment i.e. determine the percentage of customers that would need to be lost following a SSNIP in order to render that price rise unprofitable (the "critical loss"). This can then be compared with evidence on likely consumer responses e.g. from survey evidence to help assess the extent of substitutability across products, and thus how widely the market should be defined.

32 As an illustration, with a gross profit margin (leaving aside fixed costs) of around 75 per cent of revenue, a hypothetical monopolist would need to lose only around 12 per cent of its customers in the face of a 10 per cent rise in prices to suffer a fall in profit.

The scope for supply-side substitution supports a wider market definition

3.13 The OFT acknowledges that there is scope for supply-side substitution, although it does comment that the most significant barrier to entry appears to be establishing brand recognition in a primarily online-based industry and generating website "hits".[33]

3.14 Wonga considers that the evidence of actual supply side substitution is clear:

(a) as noted by the Bristol University research, most retail lenders offer pawnbroking and payday lending, as well as other services such as the purchase and sale of gold, cheque cashing, foreign exchange, money transfer, and buying and selling second-hand goods.[34] Of the ten retail lenders surveyed for this report, all provide payday loans, nine out of the ten provide pawnbroking services and five offer unsecured instalment loans;[35]

(b) some pawnbrokers have moved into the provision of online payday loans. A recent example is H&T pawnbrokers;[36]

(c) US traditional payday lenders have begun both traditional and online operations in the UK,[37] demonstrating that entry barriers to the UK market are not significant;

(d) a successful online business can be applied in a number of related product areas. Wonga itself is seeking to diversify into new business lines, for example, a business loan product and an e-commerce product. Further, some online firms offer a range of products including instalment loans or are considering doing so.[38] As noted above, QuickQuid has recently launched a product called "FlexCredit" which is essentially a running credit account.[39] Equally, a growing source of finance for consumers and businesses is peer to peer lending (offered by providers including Zopa, Ratesetter and Funding Circle).[40] While this market is developing rapidly and currently tends to focus on longer-term loans, it is plausible that such a model could be developed for short-term loans as well;[41]

(e) as noted by DeutscheBank in its analysis of the UK Retail Banking sector, payday loan companies could face competition from intermediaries and payment processors such as Google[42] and Paypal.[43] The same note characterises payday loans within the wider unsecured lending segment (which also includes overdrafts, student loans, car finance); and

---

33 OFT's decision document, para B17.

34 The Bristol University Research, page 6.

35 The Bristol University Research, page 7.

36 Mail On Sunday, April 7, 2013, p.71 at Annex 6.

37 The Bristol University Research, page 6 and page 8.

38 The Bristol University Research, 2013, page 8.

39 The product offers flexibility to the customer as to when and how to pay off the loan. One of the payment options is to make instalment payments over a period of up to 10 months, though early repayment in full is also an option. https://www.quickquid.co.uk/how-it-works.html

40 The P2P Finance Association indicates that Zopa, Ratesetter and Funding Circle have facilitated over £500m of loans between their lenders and their borrowers, of which over £100m has been facilitated in the first 5 months of 2013. http://www.p2pfinanceassociation.org.uk/

41 Peer to peer lenders connect investors with people seeking credit after screening the credit histories of potential borrowers.

42 Google has existing interests in the financial sector. In March 2013, Google invested $125m in Lending Club, a peer to peer lender.

43 Deutsche Bank Markets Research (2012), FITT for investors, Retail banking 012: past, present and future, September 7, page 61, to be provided in response to the CC's request for off-the-shelf material (CC's First Day Letter to Wonga, 28 June 2013).

(f) the CC's evaluation of remedies imposed following its Home Credit market investigation demonstrates that in response to market conditions, home credit suppliers have sought to innovate and develop new products such as shorter-term loans (of around 14 weeks duration) and online arrangements to facilitate lending.[44]

3.15 Based on this evidence, many suppliers operate across a number of consumer credit products, suggesting there may be significant synergies in doing so. The evidence also suggests the absence of any significant barriers to entry. The fast-moving nature of the sector, including the development of new types of products, suggests that there would be significant risks associated with defining a market too narrowly.

3.16 Furthermore, the potential for future entry should also be considered in any analysis of supply-side substitution, since the scope for entry in response to a hypothetical SSNIP may otherwise be understated. There are a number of established businesses that may be interested in, and capable of, entering, including: banks, where, in the US, a number of deposit-taking institutions are offering an "advance deposit" products; online gaming or commercial entities, which already have in-house access to the requisite technical expertise, a strong online presence and funding to set up an online payday business; and peer-to-peer lenders, which are a growing source of finance for both consumers and small businesses.

3.17 Given the clear scope for supply-side substitution as well as evidence of actual entry, the market definition should be widened to cover a range of short-term consumer loan products.

There are risks of defining the scope of the reference too narrowly

3.18 Given the evidence above, Wonga would urge the CC to bear in mind the possible need to request a variation to its terms of reference in order to extend the reference to other forms of short-term credit. Wonga is concerned that the overly-narrow scope of reference as currently defined could result in partial remedies focused on the narrow set of products which have been referred, which would risk distorting competition between the referred products and the wider set of products with which they actually compete.

4. FEATURES OF THE MARKET IDENTIFIED BY THE OFT

4.1 The CC invites comments on the reasons provided by the OFT for the market investigation reference. Wonga outlines in brief where it does not agree with the OFT's characterisation of the market, highlighting where the OFT's concerns have already been addressed by Wonga or are simply not applicable to Wonga given the nature of its customer offer and the customer protections already enshrined in Wonga's policies and practices.

Competition to approve loans quickly leads to widespread but variable non-compliance with regulatory requirements

4.2 The OFT has identified that irresponsible lending (and, in particular, a lack of incentive to undertake adequate affordability assessments) might have its roots in the way competition works through lenders' reliance on speed of approval, reliance on revenues from rollovers and excessive use of CPA. The OFT has also identified a risk that bad practices drive out good practices. There is an acknowledgement, however, that some lenders are conducting more adequate affordability assessments than others.[45]

---

[44] Competition Commission (2013), Understanding past market investigation remedies, Home Credit, February, pp.11-12.

[45] OFT's decision document, para 3.4.

Wonga has strong commercial incentives to undertake rigorous affordability checks

4.3 Wonga is successful when its customers repay on the due date, not by continually extending a growing line of credit. Wonga has no interest in offering loans or providing extensions in circumstances which are likely to result in a customer experiencing financial difficulties. This position is reflected in:

(a) Wonga's **policies**, for example:

(i) self imposed credit caps – first time borrowers are never allowed to borrow in excess of £400, while existing customers are eventually limited to a maximum of £1,000. The average first-time customer borrows £180 and the average across all loans is £257, with average length of loan being 17 days; and

(ii) limits on extensions to a maximum of three (in accordance with the FLA Lending Code 2012) as well as a requirement that the customer must pay off all outstanding fees and charges prior to any extension;

(b) Wonga's systems for assessing **affordability** (which are described below); and

(c) **key performance indicators**, in particular, the very low proportion of loans which are extended (8.5 per cent in 2012), and low default rates at around [✂] per cent of principal lent in 2012[46] which is significantly lower than approximately the level of [✂] per cent which applied in 2008 due, in large part, to Wonga's investment in data and affordability assessment models.

4.4 Whilst the OFT sees the revenue derived from loans which are not repaid on time as a significant competitive driver of the payday lending market[47], this perspective fails to recognise that the key driver of Wonga's business model is to use digital technology together with constructive debt management policies[48] (where loans are approved but subsequently become difficult to repay) to minimise default rates.

4.5 For this reason, affordability assessments are central to Wonga's business model. Wonga undertakes rigorous upfront and ongoing checks which aim to identify and accept only those individuals who Wonga believes (with a reasonable degree of certainty) will be able to repay the loan on the due date given their financial circumstances (including the level of indebtedness). Wonga determines a customer's immediate and future credit limit based on an in-depth credit and status check, including (where the information is available) how a customer has used Wonga's service in the past. These fully automated checks are undertaken (very quickly) before granting any loan, including any loan extensions.

4.6 Wonga accesses a range of data (including data on disposable income and financial commitments) [✂]. Wonga invests considerable time, effort and resource to ensure that its risk-based affordability decisions are based on the widest range of available data which is updated on a regular basis. [✂] All relevant publicly available data is also used to make the best possible lending decisions.

4.7 These digital, real-time risk-based systems are fully automated and, most importantly, very fast (reflecting the advanced technology that Wonga develops and utilises):

---

46 Approximately [✂] per cent of principal lent is not repaid on the due date and is not subject to an agreed extension with the customer. However Wonga's collection policies results in the recovery of just over [✂] of this within [✂] days.

47 OFT's decision document, para 3.12.

48 For example, Wonga treats borrowers in financial difficulty with forbearance by seeking to agree a repayment plan on revised terms and by freezing interest on both the original loan and any default charges after 60 days.

(a) as regards automation, the checks do not typically require manual verification checks (such as contacting employers) or validating documentary evidence[49] which seems to be the OFT's view of what constitutes a thorough affordability check[50] – but are no less rigorous or less accurate (as evidenced by Wonga's low arrears rates);[51] and

(b) as regards speed, there is no trade-off or inconsistency for Wonga between undertaking systematic and rigorous assessments of affordability, and processing loan requests as quickly as possible in order to give customers the speed and convenience that they demand as would be expected in a competitive market which is responsive to consumer preferences. Wonga has built sophisticated systems which allow it to do both because they are both important to the success of its business. Wonga does not perceive any disadvantage to undertaking affordability checks because of the risk of losing customers due to delay (as suggested by the OFT).[52] More generally, Wonga considers that speed of approval and convenience are valid bases (amongst others) upon which to compete for customers who are familiar, and comfortable, with real-time online interactions and who expect a speedy service in this context (as discussed at paragraph 4.30 below). Wonga's practices show that this can be compatible with regulatory compliance. Where firms are not complying with requirements to undertake adequate affordability checks, however, in order to be competitive on speed of approval, this should be addressed.

4.8 Wonga does not consider that this significant investment in affordability assessment places it at a competitive disadvantage. Whilst it certainly limits the number of customers to which Wonga is prepared to lend – Wonga rejects over 60 per cent of first loan applications – Wonga benefits from low default rates as noted above. More generally, Wonga considers that its success in expanding in recent years is attributable to a customer focused business model (based on transparency, flexibility but also selectivity) coupled with a very innovative technological solution which has given Wonga a competitive advantage.

4.9 Finally, Wonga does not consider that it emphasises the easy availability of loans and speed of arrangement rather than giving equal weighting to potential costs or risks, which the OFT suggests is a common theme across websites:[53]

(a) Wonga emphasises speed of application processing but this is not given precedence over the total cost of borrowing. Wonga states on the first page of its website the time by which money can be sent to customers, but it also makes the total cost of every loan clear and transparent on the same page, as well as providing a representative example (as shown in the screen shot in Annex 7);

(b) there is no undue emphasis on the speed of approval – although this information appears at the top of the page, the information on the total cost of borrowing is in larger font and forms part of the highlighted box which includes Wonga's "sliders", and therefore has more prominence. The representative example appears directly below the highlighted box and is also in larger font; and

---

49 Manual verification is undertaken by Wonga only very rarely (less than [✂] per cent of cases) where there is a high level of uncertainty as regards a customer's risk assessment.

50 OFT's decision document, para 3.25-3.26

51 A further advantage of an automated online checking process is that fraudulent behaviour, for example falsified document submission, is largely mitigated.

52 OFT's decision document, para 3.26.

53 OFT's decision document, para 3.10.

(c) a box below the representative example on the home page is entitled "*Is a Wonga loan right for you*" and below this customers are informed "*Our loans are for short term use only. If you miss your repayment date a default fee is charged and it may impact your credit rating*".[54] A link is provided to a further page where customer can get more facts on how Wonga works including (as noted above) the consequences in the event that a customer is unable to repay their debt on the due date.

<u>Wonga does not use rollovers/CPA to shield it from the consequences of poor lending decisions thereby reducing incentives to lend responsibly</u>[55]

4.10 As described above, Wonga invests a significant amount of its resources in order to make lending decisions which are properly based on accurate and up-to-date information – Wonga is able to access up to [✂] data points to make each lending decision, and its success in this regard is demonstrated by its low arrears rates. Wonga does not, therefore, use CPA or the recoupment of costs through rollovers to mitigate the risks of poor lending decisions – these risks are mitigated through Wonga's investments in technology to ensure rigorous and accurate upfront and ongoing assessments. More specifically:

(a) as regards rollovers, Wonga has moved from a position where it previously declined to offer any extensions to a position where a limited number of extensions are available (subject to affordability checks at the point of each extension). Wonga changed its position in response to consumer demand and because it believes that it is in the interests of customers to be able to apply for a short extension at certain times (for example to avoid the costs associated with default after a single loan). Equally, a responsible approach to extensions can avoid the risk of customers getting into financial difficulties. These are the principles which inform Wonga's policy on extensions, as opposed to seeking to ensure the commercial viability of a business model which does not undertake assess affordability thoroughly;

(b) as regards CPA, Wonga (like other lenders) uses CPA to allow automatic recovery of the loan on the agreed repayment data. Whilst it helps to mitigate non-repayment risks and therefore increases incentives to supply short-term credit, it must be used in accordance with the OFT's Debt Collection Guidance which require that it is not used in a way which is "*unreasonable, disproportionate or excessive*". Wonga seeks to achieve transparency on the use of CPA by providing information on the way in which it operates at various points in the application process and during the loan term. CPA is not used by Wonga "*regardless of the financial position of the borrower*".[56] If a customer in financial difficulties contacts Wonga (or responds to the proactive attempts by Wonga to contact them) Wonga will agree a suitable repayment plan and suspend all collections activities.

4.11 Finally, Wonga envisages its approach becoming more widespread. As more lenders adopt this approach, the data will become richer and experience will deepen, thereby enabling firms which make the necessary investments to perform more accurate credit and affordability assessments.

---

54 This statement has been recently added to the front page by Wonga and is currently being tested with full implementation by the end of July 2013. See Annex 7.

55 OFT's decision document, para 3.17.

56 OFT's decision document, para 3.21.

Practices which make it difficult to identify or compare the full cost of payday loans, particularly when repayments are late or missed.

4.12 The OFT is concerned that transparency issues adversely affect competition by limiting the ability of consumers to compare loans effectively on price at the point of taking out the loan.[57]

4.13 Wonga considers that being able to compare and contrast different forms of credit is vital for consumer choice and facilitates competition. Transparency, flexibility and ease of use are central to Wonga's proposition and Wonga is consistently told by its customers that its service is easy to use and that information is communicated well. Wonga's aim to transform financial services is focused on offering services which are clear, simple to understand, where charges are not hidden and which are delivered without significant delay (by virtue of the underlying technology described above).

4.14 In this regard, Wonga's code of practice states the following on transparency:

- "*In addition to any regulatory requirements, we will always show you the total cost of repayment very clearly and prominently before you apply*
- *This calculation includes all potential costs involved, with no carve-outs, hidden fees or catches*
- *We also clearly explain the potential costs and consequences of late or non-payment*
- *We won't ever change the rate of interest or charge during the short life of your loan*"[58]

4.15 Wonga considers that the industry in general should aim to meet Wonga's level of transparency.

<u>It is straightforward for Wonga's new and repeat customers to get a clear idea of the full costs of a loan for comparison purposes before making an application, enabling them to shop around</u>

4.16 The most prominent features of Wonga's website (which are found on the front page) are the "sliders" which enable customers to choose the amount that they want to borrow for the amount of time that they need it. For any combination of loan amount and loan duration selected using the sliders, customers are informed on the front page of the website the total cost of the loan (including interest and fees) - it could not be more transparent. The cost of borrowing remains unchanged once the application process has commenced.

4.17 A representative example is also included on the front page of Wonga's website directly beneath the sliders which illustrates the cost of a representative loan (showing, separately, the amount of credit, interest cost, transmission fee, total repayment amount and representative APR).

4.18 One click from the main page provides information on what happens in the event that a customer does not have sufficient funds to repay on the due date, including the circumstances in which a missed payment charge will be levied (and how it can be avoided by contacting Wonga before 5pm on the due date), the way in which CPA works, the opportunity to discuss an arrangement with a professional collections team which might help a customer get back on their feet, the period over which interest will accrue if

---

57 OFT's decision document, para 3.59.

58 http://www.wonga.com/money/downloads/code-of-practice.pdf, at Annex 1.

a fair agreement is not reached (until it is frozen) and the risks beyond that point (i.e. the risk of the account being passed to an external partner and the consequences in the event that CRAs record the outstanding debt).

4.19 Wonga does not provide information on its home page on the costs associated with extensions as it does not wish to promote the availability of extensions but rather provides comprehensive information in the event that a customer applies for an extension. The website will, however, provide information on: (i) extension fees (in the section "*What it costs*"); and (ii) guidance on whether an extension is appropriate and the costs involved (in the section "*How do I manage the loan*"). The latter will include the warning "*If your circumstances have changed and you can't repay your original loan, please don't apply for an extension. We urge you to contact us instead. If you can repay but would prefer to repay later, a loan extension could be right for you. This will be a new application and we can't guarantee it'll be approved*."[59]

4.20 Wonga's customer research indicates that customers find the Wonga service to be easy to use, and a very high proportion (95 per cent) consider that information is communicated "well" or "very well".[60]

Customers are able to make meaningful comparisons

4.21 Research by Bristol University indicates that a significant proportion of customers do consider the total repayment amount when taking out a loan, and do make comparisons before taking out the loan. Further, the Citizens Advice survey (cited in the OFT's reference decision) suggests that this information is understood. More specifically:

(a) the Bristol University research indicates that 89 per cent of online payday lending customers considered the total repayment amount (i.e. the original loan amount plus interest) before they took out their loan, and 75 per cent considered the total amount of interest that would be charged.[61] The research also suggests that around half (46 per cent) of online payday customers compared the cost of their loan with similar or other types of lenders before taking out their loan.[62] This is consistent with Wonga's customer research which indicates that a significant proportion ([✂] per cent) of its first-time customers considered at least one other cash advance website before choosing Wonga and that an increasing proportion of these are looking at "lots" of cash advance websites;[63] and

(b) the OFT reports evidence from the Citizens Advice survey that 79 per cent of respondents felt that they were "clear" on the total repayment cost of their individual loan(s).[64]

4.22 As noted above, Wonga's sliders provide an instant indication of the cost of borrowing without requiring the customer to click through to any other pages. It is very easy, therefore, for online customers to take this quote and click to another website to compare with the quotes of other providers many of whom, for example Pocket Money Pay Day Loans,[65] also use a "slider" approach.

---

59 These amendments are currently being tested with full implementation by the end of July 2013.

60 Populus Customer Survey, March 2013, slides 10 and 13 at Annex 3.

61 The Bristol University Research, page 31, Table 5.3.

62 The Bristol University Research page 30, Table 5.1.

63 Populus Customer Survey, March 2013, slide 16 at Annex 3.

64 OFT's decision document, para 3.51. Figure 1 of the OFT's reference decision also suggests that a high proportion of survey respondents were clear on the "repayment method".

65 http://www.pocketmoneypaydayloans.co.uk/. Other lenders such as PaydayUK and Dosh Express also use a "slider" approach, albeit with only one slider for loan amount because these traditional payday lenders do not permit

4.23 There are many online sources of information on payday loans and alternative short-term credit options. For example, money.co.uk provides information to enable comparison across a range of financial products including credit cards, current accounts, personal loans, prepaid cards and mortgages;[66] paydayloanchecker.co.uk uses sliders like those used by Wonga enabling customers to choose a loan amount and a loan duration;[67] customers who need short-term credit but have no time or facility to arrange an overdraft extension, can compare the costs of a Wonga loan (using the Wonga sliders) against the likely costs of an unauthorised bank overdraft using a tool created by Moneysavingsexpert.com, which compares unauthorised bank overdraft charges.[68]

4.24 The OFT suggests that comparisons may be problematic (particularly amongst online lenders) because of differing calculation methodologies (for example between loans where interest is charged per day and those where fixed interest charges are levied irrespective of the duration of the loan).[69] Whilst there is some product differentiation as highlighted by the OFT, the products identified are still relatively simple and transparent compared to many other products (for example utility products where customers may be faced with multiple tariff structures and uncertainty as to their consumption profile). Moreover, product innovation by lenders such as Wonga to offer more flexible, short-term credit products which allow customers greater control (for example, by charging daily fees rather than fixed charges and allowing fee-free early repayment) is pro-consumer and pro-competitive. As noted above, the ability of customers to compare prices is also pro-competitive and should be encouraged, but this should not come at the expense of innovation.

Wonga's automated affordability assessment and upfront information on risks addresses subjective biases

4.25 Finally, Wonga notes the submission of Which? to the OFT that consumers are often over-optimistic about their ability to repay their debts, particularly when under financial pressure.[70] Wonga does not base its lending decisions on the judgment of individuals as regards their ability to repay but undertakes an objective assessment of the affordability of the loan using a myriad of data sources and sophisticated risk models. If over-optimism is a behavioural bias displayed by short-term credit customers, Wonga does not exploit this, but rather seeks to make a lending decision which is not influenced by customer perception and bias.

4.26 In addition, Wonga seeks to address any behavioural bias towards over estimation of the ability to repay by making clear on the website the consequences in the event a customer is unable to repay on the due date (as described at paragraph 4.18 above).

A significant proportion of payday borrowers have poor credit histories, limited access to other forms of credit and pressing needs and therefore may be less price-sensitive

4.27 The OFT identifies that a significant proportion of payday borrowers have poor credit histories, limited access to other forms of credit and/or a pressing need of money and, as

---

flexibility in the duration of the loan term but instead offer loans with a single payment typically due on a customer's payday.

66 http://paydayloans.money.co.uk/. Another website (http://www.whichpaydaylender.co.uk/) also provides price comparisons for various lenders by showing the total cost repayable for £100 over 30 days. Users are also provided with "reviews" for a number of lenders which highlights and explains any product differentiation so that customers can weigh this up in relation to the price information provided.

67 http://www.paydayloanchecker.co.uk/

68 http://www.moneysavingexpert.com/banking/bank-charges-compared

69 OFT's decision document, para 3.48.

70 OFT's decision document, para 3.52.

such, they may be more focused on speed and convenience rather than the price of a loan.

<u>There are significant differences in the profile of borrowers between firms</u>

4.28 The OFT indicates that price insensitivity among consumers is likely to weaken price competition.[71] The OFT accepts, however, that the profile of borrowers may vary significantly between firms, and that differences exist between retail and online payday borrowers on measures of vulnerability and shopping around (with the Bristol University research footnoted in respect of the retail / online customer differences).[72] The Bristol University research indicates:

(a) a lower proportion of online customers in financial difficulties – the Bristol University research found that only 13 per cent of online customers did not repay their most recent loan on the due date (i.e. half of the 26 per cent of retail customers who did not repay on time);[73] and

(b) a lower incidence of multiple and repeat borrowing amongst online borrowers – the Bristol University research found the number of online customers to have multiple loans to be 10 per cent (less than half the 22 per cent of retail customers with multiple loans) and the average number of loans in the past 12 months was 3 for online customers as compared to 5.1 for retail loans.[74]

4.29 Wonga has developed a customer base of well over [✂] online borrowers, all with bank accounts, debit cards and mobile phones – i.e. a customer base with characteristics which are notably different from the characteristics typically associated with vulnerable consumers.

4.30 Wonga considers that its customers, and online customers more generally, are more representative of a generation of people who have grown up with the internet and are familiar, and comfortable, with real-time online interactions (for example, from Amazon purchases, online banking and online grocery shopping). They understand the power of the internet in helping them to identify the right product and the right deal by using, for example, price comparison sites (which are heavily advertised), or through self-navigation using search tools such as Google. Moreover, these customers are younger, have higher incomes, have access to other mainstream credit options and are less likely to be in financial difficulties. They are very well placed, therefore, to deploy their knowledge and command of the internet environment to research and identify a short-term credit product which meets their requirements.

<u>A significant proportion of customers have access to alternative credit sources</u>

4.31 As regards the availability and use of other sources of credit, most of Wonga's customers are not forced to use Wonga as a last resort, but rather make an active choice in favour of Wonga's product primarily because it provides a clear and transparent repayment plan with no hidden charges or fees and is convenient and speedy.

4.32 Wonga's research indicates that the vast majority ([✂] per cent) of customers have access to alternative credit sources.[75] Moreover, when asked to rank their preferences for

---

[71] OFT's decision document, para 3.60 and 3.61.

[72] OFT's decision document, para 3.60 and 3.72.

[73] The Bristol University Research, section 14.5.3 and 14.5.4.

[74] The Bristol University Research, section 14.5.3 and 14.5.4.

[75] Populus Customer Survey, March 2013, slide 21 at Annex 3.

different sources of credit, Wonga comes [✂].[76] This suggests that Wonga customers do see bank overdrafts as a relevant alternative to consider.

4.33 This is consistent with evidence from third party research. The Friends Provident Foundation, Policis, and Liverpool John Moores University survey found that the majority of non-standard credit users (58 per cent) also use mainstream credit products and just three in ten (29 per cent) payday loan users are using payday loans because they could not borrow elsewhere.[77] A similar proportion was identified by the Bristol University research.[78]

<u>There is evidence of price sensitivity</u>

4.34 As regards price sensitivity, the Bristol University report indicates that 43 per cent of retail payday loan customers, and 55 per cent of online payday customers, would not have taken out the loan if the cost had been higher.[79] Furthermore, 29 per cent of online payday customers would have decided not to purchase the items they used the loan money for, had they not taken out their loan.[80]

<u>There is evidence suggesting that marginal customers may be able to drive down prices for customers more generally</u>

4.35 The OFT does not give sufficient consideration to the behaviour of marginal customers and the scope for marginal customers to drive down prices for customers more generally. The OFT dismisses this point on the basis that a lack of transparency combined with customers having few alternatives constrains the ability of consumers, even at the margin, to drive down prices.[81]

4.36 As outlined above, there is evidence of customers considering repayment costs before taking out a loan (with a significant proportion regarding this information as "clear") as well as evidence of shopping around. Moreover, Wonga's pricing strategy is significantly influenced by the fact that the majority of its customers have access to mainstream credit and many of its customers are shopping around. Wonga's products, therefore, must be attractive to customers who have the opportunity to choose alternative products. Equally, Wonga does not price discriminate – the same prices are available to all customers – and therefore the competitive pressure arising from the options available to marginal customers benefits all customers.

Barriers to switching at the point of rollover

4.37 The OFT has identified barriers to individuals switching between payday lenders to alternative products or options at the point of rollover. More specifically, the OFT suggests that: (i) the incumbent lender has a significant point of sale advantage; (ii) incumbent lenders actively encourage or pressurise borrowers to rollover debt; and (ii) this may restrict the ability of borrowers to switch to alternative lenders, and borrowers may also be unclear as to alternative ways of resolving their debt.[82]

---

76 Populus Customer Survey, March 2013, slide 20 at Annex 3.

77 Credit and low-income customer, A demand-side perspective on the issues for consumer protection, Friends Provident Foundation, Policis and Liverpool John Moores University, 2011, page 45-46.

78 The Bristol University Research, 2013, Figure 4.3 indicates that 30 per cent of online payday customers gave the reason "couldn't borrow from anywhere else" when asked directly why they had used an online payday loan on the most recent occasion. It is not clear why this is lower than the figure of 50 per cent identified in Table 4.2.

79 The Bristol University Research, Figure 5.1, page 29.

80 The Bristol University Research, Table 11.3, page 81.

81 OFT's decision document, para 3.73 to 3.74.

82 OFT's decision document, para 3.75.

4.38 The OFT acknowledges that "*switching to alternative providers may be a realistic possibility for some borrowers*"[83] but still considers there to be substantial barriers at the point of rollover. Wonga considers that these barriers are overstated:

(a) at the point a loan is due, customers may apply for loans from alternative suppliers (whether payday loans, or alternative sources of credit), comparing the costs of credit from each, and in the event of a successful application they may use the proceeds to settle their initial loan; and

(b) they would face very low switching costs. The time and effort involved in applying for a short-term credit product compares favourably with other credit products such as credit cards because of innovations such as real-time automated affordability checking. Moreover, Wonga customers who wish to switch before the end of their loan term because they have identified a better deal elsewhere can do so without a redemption penalty (23 per cent of Wonga's loans are repaid early).

4.39 The balance of evidence cited by the OFT, however, seems more weighted towards a lack of awareness amongst vulnerable borrowers of alternative choices for resolving unpaid debt, and a failure by lenders to provide advice (or access to advice).

4.40 As noted above, Wonga believes that it is in the interests of customers to be able to apply for a short extension at particular times. For many customers, this simply provides additional flexibility where funds are available but a little later than anticipated. The alternatives in some cases (namely default after one loan or borrowing from less responsible/reputable sources) impose significant costs on vulnerable customers which can be avoided.

4.41 A responsible approach to extensions is required, however, to protect vulnerable borrowers and to ensure that they do not agree to rollover arrangements which, on their own, or if continued through further rollovers, would result in financial difficulties. Wonga agrees, therefore, that more effective enforcement of compliance with responsible policies relating to extensions would address many of the OFT's concerns.

4.42 Wonga's policies in this area reflect this position (and distinguish Wonga from many other short-term credit providers):

(a) Wonga will only ever extend the length of a loan when requested to do so by a customer. The term of a loan is never extended by default without the request of a customer, i.e. by "default rollover";

(b) customers can choose the duration for the loan extension (some other lenders insist on a 30 day rollover period);

(c) customers must significantly reduce the outstanding balance by paying off all fees and interest on the original loan;

(d) Wonga does not proactively encourage extensions;

(e) creditworthiness and affordability are re-assessed at the point of extension;

(f) the additional cost of extending the loan is clearly explained to customers; and

(g) Wonga limits rollovers to a maximum of three.

Market concentration and barriers to entry and expansion

---

[83] OFT's decision document, para 3.98.

4.43 The OFT identifies that three companies account for over 70 per cent of the UK payday market, measured by turnover, and that major increases in advertising spending by leading brands and new regulatory initiatives may have the effect of creating significant barriers to entry and expansion, although the OFT does not consider the evidence to be conclusive in this regard.[84]

<u>Wonga does not accept that there is relatively high concentration</u>

4.44 The OFT's view on market concentration is based on an arbitrary market definition and ignores the constraint from alternative sources of short-term credit (see Section 3 above which addresses market definition).

4.45 The OFT has not undertaken a dynamic analysis of how the market has evolved and provides no information on market shares over time. In markets such as short-term credit which have seen rapid developments in recent years, significant market shares are vulnerable and unlikely to persist and therefore information on current market concentration is likely to be of limited value. In this respect, the relevant market differs significantly from many other markets investigated by CC where persistence of market shares may have been a feature of the market.

4.46 There is a "long tail" of other players, many of which could expand and several have in the past year.

(a) Wonga's customer research indicates that, of the Wonga customers who have used a comparable service in the last six months (about [✂] per cent), [✂] have used [✂] and this percentage has [✂] from about [✂] per cent six months ago to just under [✂] per cent in March 2013);[85] and

(b) some competitors have also shown strong revenue growth in the last few quarters [✂];

(c) many of these players are driving competition through ongoing innovation and product development. [✂];

(d) other competitors such as DFC Global have stated that they are in the process of developing instalment products. Other varieties of unsecured loans that have shown strong growth by competitors recently include guarantor loans such as those offered by Amigo Loans; and

(e) peer to peer lenders such as Zopa, Ratesetter and Finding Circle have emerged in recent years and it is plausible that such a model could be developed for short-term loans as well as longer term lending.

<u>Entry barriers are demonstrably low as evidenced by the wave of entry in recent years</u>

4.47 In the online segment, growth has been particularly rapid suggesting that entry and expansion in the online environment can be readily achieved.

4.48 As regards the potential barriers identified by the OFT:

(a) brand awareness is a significant factor in driving any website business (short-term credit, or otherwise) but this does not mean that entry barriers are high:

(i) Wonga is still itself a relatively recent entrant (it launched in 2007) and does not have any significant first mover/incumbency advantages so new brands

---

84 OFT's decision document, para 3.99 and 3.114.

85 Populus Customer Survey, March 2013, slide 30 at Annex 3.

with competitive advantages could emerge and win market share from Wonga. Other brands such as QuickQuid have recently emerged and, as noted above, there is evidence of [✂] As indicated above, while many of Wonga's existing customers exhibit some degree of loyalty, this reflects very high customer satisfaction with the speed, simplicity, convenience and flexibility of the service. Without these high service levels, customers would find other providers – competition in the online environment is only a click away and there are very low switching costs. For example, [✂] per cent of Wonga customers have considered at least one other cash advance website before choosing Wonga. In these circumstances lenders must compete intensively to attract and retain customers by offering very good customer service;

(ii) brands do not need to be established from scratch. Indeed there are many strong existing online brands which could diversify into the provision of short-term credit, including entities such as mainstream credit providers or online gaming providers;

(b) Wonga does not see the costs of website development or advertising campaigns as a barrier to expansion. First, these costs are scalable to demand which significantly reduces the risks facing a new entrant. Secondly, it is likely that major advertising campaigns grow the overall market because they will tend to raise awareness of the product in general as well as specific brand awareness which will benefit new entrants to some extent; and

(c) Wonga does not see the need for lenders to build up a database of borrowers as a significant barrier to entry or expansion. Wonga considers that new entrants would have to invest in building up a database of borrowers, and they would not be guaranteed to succeed. However, this is the same as in any business, since it is only those companies with an effective business model, and the ability to win and retain customer and use the information arising from ongoing customer relationships, which can expect to be successful.

4.49 In summary, Wonga is not surprised that the OFT was unable to reach a definitive conclusion as to the effects of any market concentration because the market is evolving rapidly. What is clear, however, is that entry barriers are demonstrably low as evidenced by the wave of entry in recent years, and that existing players are expanding and diversifying as the market evolves.

12 July 2013

wonga.com

About us

Wonga is a leading short-term lender. We are based in London and provide credit to UK consumers via the internet and mobile. We launched our first website in October 2007 and offer flexible loans of £1 to £1,000, for between one and 31 days.

We have a consumer credit licence from the Office of Fair Trading (OFT) and are regulated by the Consumer Credit Act 2006. We are also a member of the Finance and Leasing Association (FLA) and abide by its Lending Code.

Our mission

Our mission is to solve consumers' occasional, urgent and short-term cash flow problems with an equally short-term solution. We base our commitment to responsible lending on **transparency**, **flexibility** and extreme **selectivity** - believing it's possible to provide credit in a way that suits consumers, not lenders.

We feel that for too long traditional lenders have been devising and marketing products with low headline rates, whilst generating most of their revenue by keeping consumers in long-term debt, or through charges hidden in the small print. Such is the lack of transparency that many financial products, including free bank accounts, would not be commercially viable without a significant portion of customers making mistakes, misunderstanding terms or using them irresponsibly.

We are taking a fresh approach to short-term credit and this is a relatively new market in the UK. Not everyone operating in this space is doing so scrupulously, so here we spell out exactly what consumers can expect when using our service. These principles are in addition to our strict adherence to UK law, regulatory requirements and the FLA's *Lending Code*.

Our operating principles

1) FLEXIBLE

- You will never be sold, encouraged or forced to borrow more credit than required
- We will let you control exactly how much you want to borrow, down to the last pound, and then determine the cost by deciding how many days you need it for (within defined parameters)
- If you haven't used Wonga before, we won't let you apply for more than £400
- We will determine your immediate and future credit limit based on in-depth credit and status checks, including how responsibly you have used our service in the past
- We deliver on our promises and describe our service honestly and accurately at all times - we will never make any misleading claims or hard-sell you credit

2) TRANSPARENT

- In addition to any regulatory requirements, we will always show you the total cost of repayment very clearly and prominently before you apply
- This calculation includes all potential costs involved, with no carve-outs, hidden fees or catches
- We also clearly explain the potential costs and consequences of late or non-payment
- We won't ever change the rate of interest or charge during the short life of your loan

3) SELECTIVE

- We use Credit Report Agencies and all the publicly-available data at our disposal to guard against fraud and make the best possible lending decisions based on your circumstances at the point of application. This includes evidence of your disposable income and financial commitments
- You will receive an instant, yet responsible decision on your screen
- If you are declined, we will give you as much information as possible about the reasons why, along with any relevant advice we can offer
- We recognise your circumstances can change so, if you return to use our service again, we will base every decision on a fresh review of your credit-worthiness, reserving the right to decline future applications even if you have repaid a previous loan on time
- Regardless of whether you apply via the website or an iPhone, our checks will be just as rigorous

4) SHORT-TERM

- You will always be encouraged to settle your debt quickly – either on time or early
- You will be able to compare interest accrued at any stage with the total cost of credit on the agreed repayment date - at any time. We will clearly show you how much you could save
- You can repay a loan early at any time and save money, paying only the interest accrued up to that point. We do not charge early repayment fees and there are no catches
- We will remind you of your responsibilities, the amount owed and the repayment date agreed during the short course of your loan
- We will automatically collect full repayment on the date agreed and never encourage you to roll your balance over for another term

5) FAIR

- We always provide clear warning about the serious nature of credit and explain the potential consequences of non-payment or late repayment
- If your circumstances change for the worse, you will be treated fairly and respectfully

- We abide by both the spirit and the word of the OFT's guidance on Debt Collection (OFT664) and subsequent associated guidance
- We ensure that any third parties we instruct on an agency basis maintain membership of the Credit Services Association (CSA) and comply with its Code of Practice
- We only recruit and employ experienced collections professionals whose objective is to reach a practical and positive solution for both you and Wonga
- We will only ever extend the length of your loan term when requested to do so by you - and if we believe it to be in your best interests. We will clearly explain the additional cost of extending your loan, require you to significantly reduce the outstanding balance to do so and limit the number of times you can move your repayment date
- We will never extend the term of your loan without your request, ie. by 'default rollover'
- We charge reasonable default fees (a one-off charge of £15 for a failed collection). This helps us cover some costs and dissuades people from late repayment, but nothing more
- We will freeze interest at the earliest possible stage – if a reasonable repayment plan can be commenced, or after **a maximum of 60 days** failing that

6) RESPONSIVE

- We make it easy to contact us during office hours: via the website, email, phone or instant chat
- If you have a complaint or concern you will receive a satisfactory response
- We will respond to your complaint and endeavour to resolve it within 48 working hours. If your complaint is particularly complex it may take longer to investigate but, in these cases, we will explain why there is a delay and tell you when we will contact you again
- If you are not satisfied with our response you can appeal the decision by writing to us again, stating your objections and providing any new information to be considered
- We are a member of the Finance and Leasing Association, so you can register a complaint via them if you have already contacted us and feel we have not responded to your concerns or resolved the matter fairly: www.fla.org.uk.

27 June 2013 Last updated at 09:31

Robert Peston
Business editor
More from Robert

The bad and good of Wonga

COMMENTS (536)

In many ways Wonga.com is an impressive, even admirable business (and please resist your temptation to send me hate mail - I am feeling delicate).

It is, for example, funded exclusively with equity capital, or £100m genuinely at risk of being lost if things go wrong.

So, unlike a bank, it has no depositors or creditors who can pull their money out in a panic and bankrupt it.

If all lenders were financed in this way, we wouldn't have had the banking crisis of 2007-8.

Also its technology, unlike our banks, is world class.

Wonga has written algorithms, computer programmes, which determine whether you deserve to be given a loan in seconds, from looking at details about you and your behaviour, such as what email service provider you use and whether you have bothered to look at the company's terms and conditions.

The proof of the robustness of this automated credit assessment is that it rejects 60% of applicants and has a default rate on its wholly unsecured personal loans of just 7.5% - which seems remarkably low, since Wonga is by definition lending to those who have exhausted their ability to get money from conventional sources.

Nor is it possible to say that what it charges for its per-day is hard to understand.

The interest rate is 1% a day, with a £5.50 transmission charge, for loans of up to £1000. Its typical loan is £200 for 15 days.

And if you go to its home page or mobile app (and in a way I would hope you haven't found the need to do that), it is staggeringly easy to see within seconds how much it will cost you to borrow what you want for the time period that suits you.

If only bank charges were so transparent.

So any criticism of Wonga would not be that it is a risky, or poorly managed business.

Arguably, given the way it is now expanding overseas and also getting into small business loans and creating a new product a bit like a credit card, it is impressively entrepreneurial.

The case against Wonga would be that there is something wrong with an economy that creates such huge demand for its very expensive money.

Its simple 1% per day interest rate equates to an annual percentage rate of interest a touch shy of 6000%. This is very, very, good business for Wonga and its venture capital backers - and a manifestation of the powerlessness of those who borrow from it.

If you hate Wonga, you are probably railing against a world in which millions of people find themselves desperate for money in the course of a year, and have nowhere to turn but a business charging an eye-wateringly high rate of interest.

Now there are so-called payday lenders (Wonga, by the way, insists it is a short-term lender, not a classic payday lenders) which are more rapacious and less transparent than Wonga.

And maybe the investigation into their practices by the Competition Commission, **which has been announced today**, will rein them in to an extent.

But if you hope that investigation, or indeed regulation and supervision by the newly created Financial Conduct Authority, will somehow eliminate the market for Wonga, or indeed destroy it as a business, well you may be guilty of an admirable but unrealistic naivete.

4 February 2013

It's as cheap or cheaper to borrow via a payday lender rather than a bank, CISI research shows

New research* undertaken by the Chartered Institute for Securities & Investment (CISI) has shown that customers looking to borrow money on a short-term basis might be better off going to a "pay day lender" rather than a high street bank.

The CISI, the 40,000 strong professional membership organisation for those working in the securities and investment industry, in the February edition of its magazine Securities & Investment Review, compares the cost of taking out a £200 unauthorised short-term overdraft from a typical payday lender, Lloyds Bank and Nat West.

The cost of borrowing £200 from the payday lender was £66.

However, from Lloyds Bank the charge for borrowing the same amount was £84.22, an APR of over 2,200%, and at Nat West the charge was £110, an APR in excess of 4,000%.

Simon Culhane, Chartered FCSI and CISI CEO said: "Late last December the Government, as part of the Financial Markets Act, undertook to introduce a cap on the amount of interest that can be charged on a loan. However, this legislation was aimed at payday lenders.

"The scandal isn't the rates charged by payday lenders but the rates charged by banks. The complete silence on rates being charged by banks for unauthorised borrowing is mystifying.

If the Government does legislate for a cap on interest we can expect to see the payday lenders focusing on charging fees, rather than interest, which will then allow some real comparison."

Ends

*Research document - **Example of APR rates**

Share this Press Release

Source: The Mail on Sunday {Main}
Edition:
Country: UK
Date: Sunday 7, April 2013
Page: 71
Area: 113 sq. cm
Circulation: ABC 169087 Weekly
Ad data: page rate £39,300.00, scc rate £230.00
Phone: 020 7938 6000
Keyword: Wonga

... as 150-year-old high street pawnbroker takes on Wonga

PAWNBROKER H&T is to take on payday lenders such as Wonga and Payday UK as it expands its online lending and traditional pawnbroker shops business.

The 150-year-old company, which has 192 stores and announced annual profits of £17million on turnover of £130million last month, claims to be a third cheaper than Payday UK and nearly half as cheap as Wonga, offering 35-day loans at rates of 820 per cent APR.

That is far higher than standard bank rates or for leading credit cards, but is less than the rates offered by many payday lenders, which are often equivalent to several thousand per cent a year.

H&T chairman Peter McNamara said 'given demand for alternative credit is unlikely to decline in the medium term, we believe that this presents a significant opportunity for the group to expand its asset base at attractive margins'.

McNamara said: 'An estimated ten million people in the UK have no access to traditional credit.'

He noted that payday lenders who did not follow best practice might be adversely affected by tightening of industry regulations.

H&T, which has just refinanced its debts with Lloyds TSB, recently became the first pawnbroker to record £50million of pledges on its books, and said it made more than £100 million of loans last year.

As well as offering traditional pawnbroking, whereby people borrow cash against valuable goods, jewellery or even cars as collateral and then have to buy back the items, H&T now has an online service by which borrowers can send in goods by post.

Sarah Bridge

Annex 7: Screenshot of www.wonga.com homepage