PAYDAY LENDING MARKET INVESTIGATION

Summary of hearing with CashEuroNet held on Wednesday 26 February 2014

Background

1. CashEuroNet said that when QuickQuid was launched in 2007 the UK payday lending market was fairly small and consumers were not aware that payday loans were available via the Internet. The market had grown substantially from 2009 to 2010 as consumers had become aware that payday loans could be obtained online. There were now more products available to consumers, including longer-term products.

2. CashEuroNet did not consider there to be any correlation between the state of the economy and the number of payday loans taken out by consumers based on CashEuroNet's direct observations of payday loan demand in the USA during the 'great recession'. There had always been a certain number of customers who were unable to secure finance from the banks. CashEuroNet believed that some consumers preferred the anonymity of applying for loans online as opposed to walking into a store.

3. CashEuroNet was constantly seeking to innovate and to provide newer, better and cheaper products. It was working towards improving its data collection and the analysis of that data to improve its credit decisions. The first loan to any new customer always had [✂]. The same was also true for instalment loans. There were a certain number of customers who would not repay their loan (known as 'won't pay customers') no matter how good the payday lender's credit model and there was no way to identify them.

4. The market had now reached maturity and any future growth would be likely to be in [✂]. Tougher market conditions would mean that competition would intensify and companies would have to compete on price and service and would have to market their products more efficiently. This would result in cheaper products and better service. CashEuroNet was planning on launching a much cheaper product in the next two to three months [✂]. As payday customers tended to stay with lenders for only 12 to 18 months, [✂].

Barriers to entry

5. The market was quite different from some of the other markets in financial services in that barriers to entry [✂]. With a small staff including two or three analysts, it was possible to develop a good credit model in six months. It was then possible to build good lead buying and pay-per-click (PPC) analytics in a further [✂] months.

6. New entrants also had access to a service provided by Experian called Bank Wizard Absolute which was able to confirm a customer's bank account details in near real time. Payday loans were typically short-term products and so a new entrant would know within 30 days whether its credit model worked and whether it required any fine tuning. CashEuroNet thought it was easier to set up a payday lending company now than when it entered the market, although it was hard to establish a brand. Wonga had been able to do so by television advertising, bus and tube advertisements and other creative publicity-generating events. Television commercials were effective in attracting new customers until they became stale. [✂]

The market

7. CashEuroNet did not agree with the proposition that consumers seeking loans were desperate for funds and took the first available loan. The results of its own survey of QuickQuid customers, which were consistent with the results of the Competition and Markets Authority's (CMA's) consumer survey, indicated that around [✂]% of people shopped around and a significant proportion of those had done so for previous loans. CashEuroNet noted that only a very small percentage ([✂]%) of the consumers viewing its PPC products took out a loan and that customers dropped out at every stage of its loan application process. A lot of its customers were taking out smaller loans than for which they qualified. CashEuroNet considered that unauthorised overdraft facilities were a substitute to payday loans. The results of its own survey indicated that consumers were using unauthorised overdraft facilities and payday loans as substitute products. It was very concerned about [✂].

8. CashEuroNet thought that the initiative by Callcredit to share real time data (including details of the loan duration and whether it was repaid on time) would benefit the entire credit market as it would enable payday lenders to make more informed decisions on credit because companies would have access to customer data. Companies would be able to see whether a customer had applied for multiple loans. CashEuroNet did not want customers to have multiple loans with other lenders because this reduced the chances of it being paid back but would consider lending to them subject to outstanding obligations and affordability constraints. CashEuroNet had recently changed

its credit search processes so that a customer could obtain a quote without leaving a footprint on its credit report.

9. Marketing costs had increased significantly between 2010 and 2013. A lender might need to issue [✂] loans to the same customer to cover its acquisition costs. However, CashEuroNet's product portfolio enabled it to recover its costs over a longer period of time. Television advertising was [✂], while lead generators could cost [✂]. If lead generators increased their prices, payday lenders had to pass on the cost in the form of increased prices to their customers. PPC cost around £[✂] for branded loans and less for non-branded products, although both had very low conversion rates [✂]. The cost of PPC was being driven by competition from lead providers and other lenders on Google.

10. QuickQuid operated promotions (using codes obtained from affiliate websites) and discounts. If a customer had performed well in servicing their loan they might be offered a discount on their next loan. However, [✂].

11. [✂]

12. [✂] It noted that some payday lenders had dropped the funding fee or had expanded their call centre hours in response to CashEuroNet's 24-hour service. Some lenders charged a funding fee, a default fee, an end-of-term collection fee and a post-default fee. CashEuroNet had no hidden fees.

13. There were a few comparison websites, although moneysupermarket.com had stopped offering a comparison website for payday loans. Some years ago, CashEuroNet discussed with the Office of Fair Trading (OFT) the idea of QuickQuid launching a payday loan price comparison website. The OFT had concerns about such a website being hosted by an entity that may not appear wholly unbiased.

14. Delays in payment were due to a variety of reasons, including bank errors and system crashes and problems with the customer's payroll. [✂] Banks Automated Clearance Service payments were accepted throughout the day. Loans were not considered past-due until after 11.59pm on the repayment date.

Competition

15. The cost of credit to a lender was dependent on the risk profile of the customer and was reflected in the price. CashEuroNet did not observe clustering around the £30 price point (as indicated in the CMA's pricing working paper). For example, CashEuroNet had introduced risk-based pricing with three specific price tiers in 2009 (£20, £25 and £29.50). Potential

customers completed an automated application form on its website and then received a price (following credit checks). [✂]% of its customers did not accept the offer. The introduction of price tiers was in response to competition. [✂] Prices in the market were dispersed across a spectrum and this might reflect to some extent differences in the risk profile of customers. Price competition was evident in the market, for example Wizzcash, Think Finance and Zebit had introduced cheaper finance, although the future Financial Conduct Authority (FCA) price cap might have an effect on price structures. Some companies such as Think Finance had developed risk-based pricing models which enabled them to separate customers by price, allowing them to serve both high- and low-risk customers. CashEuroNet thought more companies would offer risk-based pricing in the future in what would be a more competitive market (although this might be affected by the FCA price cap and other regulatory changes). CashEuroNet had started to add more services, adding same-day funding for no additional fee while keeping headline interest rates at the risk-based level.

16. CashEuroNet had introduced FlexCredit in response to its research, which indicated that its customers wanted flexible repayment. FlexCredit had a daily pricing structure and lower interest rates on short-term loans to compete with Wonga’s 20-day product. [✂] consumers were now using FlexCredit. Although QuickQuid’s longer-term loans were cheaper than similar loans offered by Wonga, some customers preferred Wonga products, which CashEuroNet attributed to certain features of the Wonga loan proposition. [✂] Peachy and Think Finance had also introduced flexible loans in the last year.

Regulation

17. CashEuroNet thought that the FCA would have a more rigorous and proactive approach than the OFT and this would have an impact on the market, as payday lenders were small companies with limited resources. However, CashEuroNet was used to regulation in the USA and so was well positioned to stay in the market, serve customers and eventually expand.

18. CashEuroNet acknowledged that some payday lending companies engaged in bad practices which were being addressed, and noted that the FCA consultation document referred to the lack of affordability assessments and the aggressive use of continuous payment authority (CPA). CashEuroNet thought that there might be some consolidation in the market because there would be some companies that would find it difficult to adapt to the FCA regime. CashEuroNet had received a lot of enquiries from companies seeking to sell their businesses. However, the acquisition of companies [✂] was not an attractive proposition, especially as CashEuroNet might not approve most of their customers.

19. The reduction in the number of rollovers to two by the FCA would not have much of an impact on CashEuroNet's business as it already had a rollover limit of two. It was aware that the FCA and OFT did not view rollovers favourably and so was trying to develop a business model in which they were not part of its future business.

20. The combination of the FCA regime, the rulebook changes and the rate cap would reduce [✂]. The FCA expected about 20 to 30% of firms to exit the market which CashEuroNet believed might be conservative pending rate-cap decisions by the FCA. It expected compliance costs to increase under the FCA regime and that some companies would be unable to adapt, notably those at the tail end of the market. CashEuroNet thought that removing the payday lenders at the lower end of the spectrum would result in a better, more orderly market. It would be interesting to see how the lead generators would adapt to the new regime. CashEuroNet expected that business practices would stabilise across the industry, ensuring that all companies were on a level playing field.

21. CashEuroNet thought that public perception of the industry would improve following the CMA's market investigation and under the FCA regime. While companies were currently deterred from entering the market, they would be more willing to invest once the reputation of the industry improved.