COMPETITION AND MARKETS AUTHORITY
PAYDAY LENDING MARKET INVESTIGATION

SUBMISSION ON BEHALF OF MEM CONSUMER FINANCE LIMITED, INSTANT CASH LOANS LTD AND EXPRESS FINANCE (BROMLEY) LTD IN RESPONSE TO WORKING PAPERS PUBLISHED ON 9 APRIL 2014

1. Introduction

1.1 This submission is made by DFC Global Corp ("DFC") on behalf of MEM Consumer Finance Limited ("MEM"), Express Finance (Bromley) Limited ("Express Finance") and Instant Cash Loans Limited ("ICL") in response to the Repeat borrowing and customers' use of multiple lenders working paper (the "Working Paper") and two presentations – Customers' use of multiple payday lenders ("Multiple payday lenders use presentation") and Use of other credit products by payday loan customers ("Other credit products presentation"), all published by the Competition and Markets Authority ("CMA") on 9 April 2014. References to DFC in this document should be taken to refer to MEM, Express Finance and ICL collectively as well as to DFC Global Corp.

1.2 This submission is in addition to the submission made by DFC dated 19 March 2014 in response to the Annotated issues statement (the "AIS") and all working papers published by the (then) Competition Commission[1] on or before 24 February 2014 (the "AIS Response").

1.3 DFC understands that the purpose of the Other credit products presentation is to complement the CMA's existing analysis in relation to market definition and that the purpose of the Working Paper and the Multiple payday lenders use presentation is to expand the CMA's analysis in relation to the first theory of harm namely, the existence of impediments to customers' ability to shop around and switch suppliers. DFC addresses each of these issues below.

2. The use of other credit products presentation – Market definition

2.1 In the AIS, the CMA's initial analysis in relation to market definition suggests that providers of other forms of credit will provide little competitive constraint on payday lenders.[2] As set out in DFC's AIS Response, DFC continues to submit

[1] For ease of reference, the Competition Commission is generally referred to as the CMA throughout the remainder of this submission.

[2] Annotated issues statement, paragraphs 52-55.

that payday loans have faced and still face competitive pressure from other credit products.[3]

2.2 In its Other credit products presentation, the CMA considers, based on its analysis of transaction and CRA data, the extent to which payday loan customers use other credit products and have other forms of credit available to them when taking out a payday loan. The analysis is based on a random sample of over 3000 payday loans made by the principal 11 payday lenders, the identification of the customers to whom those loans were made and consideration of credit record information held in relation to those customers.[4]

2.3 The CMA's analysis finds that in 2012, 71% of payday loan customers also used either a credit card or overdraft; but that, at the time of a payday loan being obtained, in 85% of cases customers had less than £200 of credit available on their credit cards, and in 81% of cases[5] customers had less than £100 of credit available.[6]

2.4 It is not clear what, if any, inference the CMA intends to draw from its findings in relation to available credit card balances. If the CMA intends to infer that a majority of payday loan customers do not have recourse to forms of credit other than payday loans and therefore other credit products do not impose a competitive constraint on payday loans, DFC does not accept such inferences and submits as follows:

(i) the payday loan customer data analysed by the CMA implicitly excludes borrowers who have considered a credit card, overdraft or other form of credit to be a substitute for a payday loan and have opted to use that other form of credit instead of taking out a payday loan;

(ii) the CMA's analysis does not take into account the fact that even those payday loan customers who have less than £100 or £200 of credit remaining on their credit cards at the point of taking out the payday loan in question may previously have chosen to obtain funds by the use of a credit card instead of taking out a payday loan. It follows that the CMA's analysis is likely to understate the extent to which payday

3 DFC's response to Annotated issues statement, paragraphs 4.8-4.15

4 CMA, Use of other credit products by payday loan customers presentation, 9 April 2014, slide 4

5 CMA, Use of other credit products by payday loan customers presentation, 9 April 2014, slide 3

6 CMA, Use of other credit products by payday loan customers presentation, 9 April 2014, slide 3

loan customers have previously chosen to obtain alternative forms of credit and, in so doing, have taken out a reduced loan;

(iii) the CMA's analysis considers unused credit on a credit card only. Importantly, it does not take into account unused overdraft limits or other forms of credit and it fails to take into account the extent to which customers might use an (unauthorised*)* overdraft as a substitute to a payday loan;

(iv) DFC questions the appropriateness of any analysis that does not take account of the actual amount borrowed by the payday loan customer in question. Whilst £260 is the (mean) average amount of a loan, there is wide dispersion in the amount borrowed. Notably, the CMA itself opted to use the (modal) average of £100 in its previous pricing analysis.[7] DFC believes the CMA's analysis should not be conducted in terms of average (mean) borrowing amounts. Rather the CMA should consider the extent to which actual amounts borrowed by an individual payday loan customer could have been taken out on a credit card, by way of an unauthorized overdraft or indeed a combination of the two. The CMA's analysis also takes no account of a customers' ability to request increases in credit card limits if and when the need arises.

(v) the analysis is based on a loan sample constructed from an underlying random sample of over 3000 payday loans over a one year period (2012). In addition, credit record information for the sample customers was obtained, representing approximately 90%[8] of the customers in the original sample. The CMA notes that to the extent that a customer's credit history is not fully documented, "*the result may underestimate customers' usage of other credit products*". No indication or analysis is undertaken as to the extent to which customers' use of other credit products may have been underestimated. The sample of over 3000 loans represents approximately 0.03% of the total amount of loans for the same

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[7] CMA, Payday lender pricing working paper, 19 February 2014, Annex 2, paragraph 2

[8] We refer to the CMA statement at slide 4 of the Use of other credit products by payday loan customers presentation, 9 April 2014, in which it is stated that "it covers over 90% of the customers in our original sample". In addition, while the number of customers actually included in the CMA's analysis using the CRA dataset is not entirely clear from the two working papers (Use of other credit products by payday loan customers and Customers' use of multiple payday lenders, 9 April 2014), the CMA recognises on slide 4 of Customers' use of multiple payday lenders presentation that "the sample is likely to contain a larger number of heavier borrowers than the population", so the number of consumers in the CMA's sample is presumably less than 3,250 out of the 2.6million customers served by the industry during 2012.

period[9]. Even if, in the unlikely event, each one of those loans corresponded to a different customer, the CMA's analysis would consider the borrowing behaviour of less than 0.12%[10] of customers for 2012. While sampling from a population will usually involve drawing inferences from a small fraction of the population, it is important to note that the sample of customers obtained by the CMA is not only small but it is also not a random sample of payday lending customers. On the contrary, the CMA's sample is constructively "*selected*" in a specific way – with a bias towards oversampling high loan volume (and hence, for example, presumably repeated use) consumers. DFC submits therefore that the sample data does not therefore represent a robust basis for drawing any conclusions in relation to the use of other forms of credit by payday loan customers in general;

(vi) DFC further submits the CMA must ensure that the "*selected*" nature of its sample does not artificially drive or lead to unsustainable or unwarranted conclusions. In this regard, DFC notes that the CMA provides no detail on the use of "*reweighting*" where this is used in its analysis[11] and does not, for example, compare the demographics and borrowing profiles of the customers which appear in the loan sample (as matched to CRA data) for the purpose of the Other credit products presentation with those of the wider 2012 transaction dataset available to the CMA. DFC submits that an analysis to compare the properties of a sample with that of the population (here the customer characteristics of the transaction dataset) should typically be undertaken and may reveal that significant adjustments to the sample weighting used in the analysis would be required.

3. First Theory of harm: impediments to customers' ability to shop around and switch supplier

3.1 The CMA's first theory of harm relates to the existence of impediments to customers' ability to search and identify the best value product and to switch

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9 CMA, Customers and their loans presentation based on analysis of the transaction data, 14 February 2014, in which the total numbers of loans for 2012 is given as 8,807,573, slide 5

10 CMA, Repeat customers presentation based on analysis of the transaction data, 14 February 2014, calculated as 100*(3,250)/2,614,620 = 0.124% where the denominator is obtained from slide 42

11 CMA, Customers' use of multiple payday lenders working paper, 9 April 2014, slide 4.

supplier. In the Working Paper and the Multiple payday lenders use presentation, the CMA considers the following issues:

(i) the extent to which customers take out multiple loans from the same lender;

(ii) the extent to which customers use multiple lenders;

(iii) the reasons why customers may choose to switch suppliers or not; and

(iv) the existence of any factors or mechanisms that might prevent existing customers from switching suppliers.

Repeat borrowing

3.2 The CMA concludes that repeat borrowing is relatively common in the payday lending sector.[12] DFC accepts that it is important for DFC companies (and indeed other payday lenders) to compete to retain its customers such that when a customer requires additional loan facilities, that customer chooses to return to DFC, its existing supplier. DFC submits, however, that the importance of repeat custom is no different for payday lenders than for any other service provider. In common with all such businesses, it is important for payday lenders to maintain and grow their customer base by winning new custom and working hard to retain their existing customers.

3.3 From a DFC perspective, the means by which DFC attempts to ensure repeat custom is by [CONFIDENTIAL]. On this point, DFC welcomes the acknowledgement by the CMA that "*Customers who have always used the same lender typically reported doing so because they were happy with the service provided by their existing lender*". Such an analysis holds true whether looking at customers who have considered switching or those who have not.[13]

3.4 DFC submits that, insofar as there are high levels of repeat lending to the same customer in the payday lending sector, such a feature, when considered together with the high levels of customer satisfaction seen in the industry as well as the levels of switching considered below at paragraphs 3.23 and 3.15, is not indicative of any competition issue but is supportive of an industry in which all

12 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 14

13 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraphs 5(b) (ii) and 40

parties compete vigorously in relation to their service offering in order to retain as well as attract customers.

3.5 DFC also submits that any analysis of repeat lending in the sector should be considered in the context of the short duration of a typical payday loan and the constant customer churn in the sector. As previously noted by DFC[14], DFC estimates that [CONFIDENTIAL]. DFC's position is supported by Cash Euro Net who have informed the CMA that customers "*tended to stay with a payday lender only for around 12 to 18 months, which resulted in a continual churn of customers who were taking out payday loans*".[15] The CMA's analysis of its full transaction dataset by total value of loans and by cohort supports such an analysis.[16]

Use of multiple lenders

3.6 In relation to the Working Paper and the multiple payday lenders presentation, it is also important to note that the CMA's analysis is based on a random selection of 3,250 loans issued in 2012 from the transaction databases submitted by the 11 principal lenders (the "limited sample data"). The limited sample data represents 0.03% of the total amount of loans for the same period[17] . For the reasons set out at paragraph 2.4 (v) above, DFC does not consider that the limited sample data is random and therefore representative of payday lending customers generally. The CMA itself recognises that the probability of a customer being included in the CRA sample is proportionate to the number of loans issued to that customer (and adjusts its results for such sample selection for just one slide, slide 8, of its presentation).[18]

3.7 However, sample selection is more important in a more general sense. For example, the limited sample data over-selects customers who are heavier payday loan users and so may well be more likely than the general population of

14 DFC's response to Annotated issues statement, paragraph 4.6

15 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 29(b).

16 CMA, Repeat customers – presentation based on analysis of the transaction data, 14 February 2014, for example, slide 9 notes "*customers who started borrowing from a particular lender in 2010 or earlier took out between 1% and 28% of loans in 2012 (by value).* The CMA's analysis shows that between 99% and 72% of loans by value in 2012 were taken out by customers who had not been customers of the same lender in 2010.

17 CMA, Customers and their loans – presentation based on analysis of the transaction data, 14 February 2014, in which the total numbers of loans for 2012 is given as 8,807,573, slide 5. Even if the extended sample of 36,073 loans referred to in CMA, Customers' use of multiple payday lenders (slide 13) were used in this calculation, it would still only increase the proportion of loans in the sample to 0.4% of loans. Most importantly, the CMA need to be suitably deliberate in interpreting its analysis since: (i) the 36,073 sample of loans is not a random sample of all loans (by construction) and (ii) the set of customers' in the CMA sample is not a random sample of the population of payday lending customers. These observations may mean that important biases affect the CMA's calculations.

18 CMA, Customers' use of multiple payday lenders, 9 April 2014, see the note on slide 4

payday loan customers to take out multiple concurrent loans (multi-sourcing) and indeed may well have more limited access to other sources of credit. By way of example, the CMA states that according to its limited sample data "*On average a payday customer took out 7.9 loans in 2012.*"[19] However, the CMA's transaction database[20] in 2012 reports that in the full sample there were a total of 8,782,969 loans taken out by 2,614,620 customers in 2012, which amounts to an average of only 3.4 loans per customer.[21]

3.8 In light of the real issues concerning the representative nature of the limited sample data, DFC inevitably has concerns in relation to the reliability or accuracy of any conclusions based on such data and, in particular, whether that data provides a robust basis for drawing any conclusions in relation to the use of multiple lenders and levels of switching between lenders by payday lending customers. It is not readily apparent to DFC why the CMA is not using the full transaction dataset for at least parts of its analysis rather than what appears to be a very small non-random sample of customers.[22]

3.9 In particular, in relation to the switching issue, DFC notes that the CMA has concluded that of the customers in the limited sample data who used more than one payday lender in 2012, a significant proportion of these may be multi-sourcing. The CMA goes on to conclude that if a customer uses multiple lenders simultaneously, "*there will typically be constraints on customers' ability to return to the previous lender for further credit*".[23] [24] DFC does not accept, however, that the multi-sourcing levels identified by the CMA in the limited sample data are representative of the wider payday lending customer base given that the limited sample data is weighted to heavier payday loan users. Insofar as the CMA's estimates in relation to multi-sourcing is likely to be an over-estimate, this may lead to levels of switching, in the absence of multi-sourcing, being understated.

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19 CMA, Customers' use of multiple payday lenders working paper, 9 April 2014, slide 8

20 CMA, Repeat customers - presentation based on analysis of the transaction data, 14 February 2014, slide 42

21 Calculated as 8,782,969/2,614,620=3.4. It is noted that according to the CMA, Customers' use of multiple payday lenders, 9 April 2014, slide 13, the CMA's sample involves a total of 3,094 customers who have a total of 36,073 loans which means an average of 11.66 loans per customer in the sample. Thus the "re-weighting" reported to have been undertaken on slide 8 appears to reduce 11.66 to 7.9 loans per customer but that does not appear to be correctly reweighting this number to be representative of the transaction database which instead reports an average of 3.4 loans per customer in 2012. Finally, the CMA, Customers' use of multiple payday lenders, 9 April 2014, slide 21, reports the results from a sample with somewhat different numbers of observations in, namely 3,228 customers and 37,333 loans in 2012.

22 To the extent that the CMA can undertake the customer matching across lenders' transaction databases for those customers in its sample (in the manner described in the CMA, Customers' use of multiple payday lenders, 9 April 2014, slide 5) by using a combination of last-name, postcode and date of birth, it should be able to undertake an analogous exercise to match the full transaction database or at least large parts of it.

23 CMA, Customers' use of multiple payday lenders, 9 April 2014, slide 12

24 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 24

3.10 DFC notes that the CMA's position is not supported by the evidence from the transaction dataset. Specifically, when the CMA considers the amount of the loan taken as a proportion of the maximum amount available to be borrowed it concludes that: "*Just over 20% of customers take out the maximum [loan] amount possible - a half take out less than half the amount originally available.*"[25] The CMA's survey reports that a minority of those customers (only 34%) who did change lender could not go to their existing lender because of an outstanding loan or as a result of not being granted a higher or further loan.[26]

3.11 In addition, DFC questions the CMA's approach to exclude instances of switching where a customer changes lender following a 'repayment problem' with the previous supplier.[27] No information is provided about the nature of any potential repayment problem which might encompass any number of issues which would not entail the need to switch suppliers. The assumption that all customers who had had an unspecified 'repayment problem' are unable to return to their original lenders is not supported by any robust evidence and is likely to have the effect of under-stating switching rates.

3.12 The CMA considers that the "*possibility that a significant proportion of the instances of borrowers changing lenders ... is being driven by borrowers being unable to go back to the original lender*"[28] is also supported by additional evidence. However, DFC submits that none of the evidence relied upon is directly relevant to this proposition. For example, the CMA considers the tendency for borrowers not to repay or repay their 'last loan' late is relevant to the issue of switching. However, a significant number of 'last loans' will also be first and only loans and so the relevance of the numbers reported in Figure 5 is far from obvious.[29]

3.13 In addition, DFC notes that the CMA seeks to rely upon a customer's decision not to repay a last loan as one which causes customers to switch provider thereby supporting the hypothesis that a significant proportion of customers are forced to switch. DFC notes, however, that an alternative (and equally credible) interpretation would involve consumers deciding to switch provider and, since they are switching, making a decision not to repay their last loan from their current provider.[30] DFC notes therefore that a tendency not to repay a last loan

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25 CMA, Customers and their loans—presentation based on analysis of the transaction data, 14 February 2014, slide 25

26 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 32, Figure 4

27 CMA, Customers' use of multiple payday lenders, 9 April 2014, slides 17 and 26

28 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 35

29 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, Figure 5

30 [CONFIDENTIAL]

may sometimes be a consequence of a customer's decision to switch provider rather than the cause for that customer to switch.

3.14 DFC notes also the CMA's reliance on its survey to establish that customers' financial circumstances tend to affect their borrowing behaviour in that customers with greater need tend to access more loans and also other types of credit.[31] DFC agrees that demand for financial services is likely to be associated with greater use of financial services but also submits that such a relationship is not of itself evidence of an inability to switch between lenders. In addition, such a relationship between need and consumption would not ordinarily be deemed to indicate a competition problem.

Switching

3.15 Notwithstanding DFC's concerns about any conclusions reached on the basis of the limited sample data and its belief that levels of switching are likely to be under-stated, DFC notes that the following observations emerge from the CMA's analysis in relation to switching between multiple lenders by payday lending customers:

(i) the majority of customers in the CMA's sample (55%) used more than one payday lender in 2012 and those customers accounted for 69% of all loans in 2012;[32]

(ii) 27% of customers in the sample used different lenders for consecutive loans on at least one occasion. Excluding customers who, according to the CMA, have experienced 'repayment' problems with a previous lender, the proportion that have switched suppliers is at a minimum of 16% (and may well be higher)[33];

(iii) In DFC's submission, the switching rates of 27% or 16% referred to above are significant and notably higher than levels of switching found in relation to many other financial products, as considered further below at paragraph 3.18.

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31 See in particular the observations at paragraph 22 and Figure 3 of CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014

32 CMA, Customers' use of multiple payday lenders, 9 April 2014, slide 9

This is in fact even higher than the percentage indicated by the CMA customer survey. The CMA customer survey, pages 33 and 132, indicates that, when looking at customers who have taken out multiple loans, 57% have used more than one lender; and when looking at all customers including those who have only ever taken out one loan, 45% have used more than one lender.

33 CMA, Customers' use of multiple payday lenders, 9 April 2014, slides 17 and 26

3.16 DFC is unclear as to what, if any, inference the CMA intends to draw from its hypothesis that a proportion of the customers who use multiple lenders may be constrained from returning to their previous lender. DFC notes however that whether customers opt to switch or whether the assumption of the CMA is correct (which is not accepted) namely that some or all only do so because they are constrained from returning to their previous lender, they are nonetheless switching suppliers. Therefore the majority of customers in the CMA's sample switched lender in 2012 and of that majority, a significant proportion switched suppliers in the absence of any evidence of any constraint in the ability to borrow from an existing lender.

3.17 DFC submits that the CMA's own evidence which, as noted above, is likely to understate switching levels, clearly supports the conclusion that customer behaviour imposes a strong competitive constraint on payday lenders in that:

(i) payday lenders must compete to win new customers. On this point, it is notable that the CMA's analysis suggests that payday lenders had an average of 20% of loans that were new customers to that lender in 2012;[34]

(ii) they must compete to retain existing customers; given the high proportion of customers who not only use more than one lender, but who use three or more lenders[35], there can be no assurance that a customer who borrows simultaneously or consecutively from a second (third, etc) lender will return to any given lender. Regardless of whether an existing lender has any incumbency advantage over a new lender (see further below), in this situation the existing lenders can clearly expect to face vigorous competition at least from one another as well as from other forms of credit; and

(iii) even excluding customers who change lenders because of repayment problems, as noted above, there remains 16% of customers who use different lenders for consecutive loans.

3.18 DFC notes that the CMA has given no indication as to what it would consider an appropriate level of switching. However, DFC submits that, even if the CMA considered the level of switching to be established at 16%, this level of switching is sufficient to ensure competition, and indeed is significantly higher than the

[34] CMA, Repeat customers – presentation based on analysis of the transaction data, 14 February 2014, slide 5

[35] CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 18

levels identified in other industries. For example, annual rates of switching in SME banking were 4% between 2002 and 2006, annual rates of switching in personal current accounts were between 2 – 3% between 2008 and 2012, annual rates of switching in pay TV service were 6% in 2010 and were considered low in comparison to annual switching rates cited (and implicitly approved) by the CC in 2010 of "*about 16-18% for electricity, 16-19% for gas, 29 to 34% for car insurance, 3 to 5% for bank accounts, 7 to 10% for fixed line telephones, 8 to 12% for mobile phones and 7 to 8 % for internet connection*".[36]

3.19 Moreover, the switching activity identified above takes place in the context of a high level of churn, [37] meaning that payday lenders constantly compete to win new customers.

3.20 DFC welcomes the acknowledgement by the CMA that overall, "*the evidence we have seen shows that a significant proportion of payday customers use more than one payday lender*." The CMA considers that "*much of this use of multiple lenders takes place as a result of customers being constrained in their ability to borrow further amounts from an existing lender*" but even if (which is not accepted by DFC) it is correct that a proportion of borrowers switch because they are constrained from borrowing further from their existing lender, the high level of switching and customer churn nonetheless operate as a significant competitive constraint on payday lenders and require them to ensure that their offering to both new and repeat customers is highly competitive.

3.21 In relation to the reasons why customers switch suppliers, DFC notes:

(i) the majority of customers who had taken out multiple loans but only used a single lender said that they had not considered switching because they were happy with their existing lender. As acknowledged by the CMA "*Customers who have always used the same lender typically reported doing so because they were happy with the service provided by their existing lender*".[38]

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36 Competition Commission, Movies on pay TV market investigation, paragraph 5.31

37 DFC's response to Annotated issues statement, paragraph 4.6

The CMA notes that, looking at new customers taking out a loan with a lender for the first time in the first part of 2012, 60% went to take out at least one further loan from the same lender during the subsequent year. However, as already noted in the DFC AIS Response, this means that a significant proportion, 40%, did not take out another loan during the subsequent year.

38 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraphs 5(b) (ii) and 40

(ii) an additional 4% of those customers who had taken out multiple loans but only used a single lender indicated that they had stayed with their existing lender because their current lender offered better terms.[39]

(iii) a significant proportion (30%) of those customers who have changed lender reported having done so because they prefer some aspect of the product and / or offering of the new lender such as the total cost of credit, repayment flexibility or the ease of application process.[40]

(iv) approximately 45% of those customers who had changed lenders cited positive reasons for switching to another lender including convenience and personal recommendations.[41]

(v) the CMA's survey found that "*44% of customers with more than one lender had switched at some point due to preferring an alternative loan or service*"[42].

Impediments to switching

3.22 The CMA has identified three possible mechanisms which impede switching by customers namely:

(i) the perceived inconvenience of switching

(ii) the uncertainty regarding other lenders' offering

(iii) lenders offering better loan terms

3.23 As regards whether perceived inconvenience or uncertainty as to loan approval may operate as a barrier to switching, DFC does not consider that they do and refers to the submissions previously made at paragraph 7.14 and 7.15 of its AIS Response. DFC notes the CMA's observations that there is '*some*' evidence to suggest that inconvenience may be a factor for some borrowers considering switching lenders and that there is '*limited*' evidence that uncertainty may deter borrowers from switching.[43] Both conclusions appear to be tentative which, in DFC's submission, reflect the fact that they are unsupported by any or any compelling evidence. The evidence confirms that the majority of payday loan

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39 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 40

40 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 33 (b)

41 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 32, Figure 4

42 TNS BMRB survey report, Research into the payday lending market, 31 January 2014, page 135

43 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 54

customers who had not switched or changed lenders had not done so because they were happy with the service provided by their existing lender, and that only a minority of those questioned raised inconvenience or uncertainty as the reason for not switching.[44]

3.24 To the extent that the existence of material switching costs might give rise to incentives to exploit an existing customer base[45], the CMA has found no evidence of this. The CMA acknowledges that there is little evidence of price discrimination by payday lenders in favour of new customers.[46] [CONFIDENTIAL] As acknowledged by the CMA, even to the extent that lenders may wish to take advantage of existing customers by raising headline prices (and it is not accepted that payday lenders could price discriminate without risking losing existing customers), "*they may also have an incentive to reduce headline prices in order to compete for new customers…*".[47]

3.25 In relation to whether better terms being given to existing customers might constitute a barrier to switching, the CMA has conceded that it has found no evidence of the use of pricing discounts to retain repeat customers[48]. Equally the CMA has acknowledged that it is uncommon for customers to cite benefits to stay with incumbent lenders as a reason for not switching.[49] On the contrary, the CMA appears to be suggesting that a lack of access to credit from an existing supplier is driving customers to switch to other lenders.

3.26 In the absence of any evidence in relation to the use of promotions or pricing discounts or incentives to stay with an incumbent lender, the CMA has focused on the extent to which repeat customers are offered additional credit. DFC does not consider that increased lending limits for existing customers constitute a barrier to switching. [CONFIDENTIAL][50]

3.27 In addition, the bespoke payday lending credit databases currently being devised by CallCredit and Experian, [CONFIDENTIAL] are expected to provide lenders

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44 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 40- 42

45 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 48
"*Where material switching costs exist (and hence existing customers are 'captive' in some sense), then lenders are likely to have an incentive to exploit their existing customer base by increasing their prices, anticipating that the customer response will be weak.*"

46 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 50

47 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 49(b)

48 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 63

49 CMA, Repeat borrowing and customers' use of multiple lenders working paper, 9 April 2014, paragraph 69

50 [CONFIDENTIAL]

with more up-to-date credit information on borrowers and could in principle allow lenders to offer more similar credit limits to both new and repeat customers insofar as more comprehensive credit information is generally available.

3.28 DFC does not consider that the CMA has identified any evidence of any real impediments (whether or not imposed by payday lenders or as a result of customer behaviour) to customers' ability to switch lenders.

4. Conclusion

4.1 In conclusion, DFC submits as follows:

(i) for the reasons set out above, the CMA's analysis in relation to available credit card balances does not form a robust basis for any conclusions in relation to the use of other forms of credit by payday loan customers;

(ii) DFC accepts that repeat custom is important in the payday lending sector. This is no different from any other industry which provides services to customers. The importance of repeat customer incentivises payday lenders to compete in relation to their offers and levels of customer service. Notwithstanding the importance of repeat customers, it is important to note that repeat custom should be considered in the context of the short time period involved for any given loan and also the high levels of customer churn in the sector generally;

(iii) for the reasons set out above, the CMA analysis in relation to use of multiple lenders and switching rates does not provide a robust basis for its conclusions and may well over-state multi-sourcing and under-state switching rates;

(iv) the CMA's own analysis shows that there is in fact switching between lenders. Switching rates are estimated at between 16% - 27% depending on whether customers who, according to the CMA's analysis, are constrained from taking out further loans from an existing lender are excluded. The rates of switching (which are likely to be understated) in the payday lending sector are significant and compare favourably with rates of lending in other sectors, including those which have been previously cited by the CC as comparatively high;

(v) the CMA's own evidence shows that the principal reason most customers do not switch between lenders is due primarily to the borrowers' satisfaction with their suppliers and not as a result of any specific incentives or benefits offered by lenders to stay with them;

(vi) there are no barriers to customer switching raised by lenders. Factors such as perceived inconvenience and uncertainty which may discourage customers from switching are cited by a minority of customers as reasons for not switching. No or no compelling evidence has been produced by the CMA that either inconvenience or uncertainty are obstacles to payday loan customers switching suppliers.

29 April 2014