Payday lending market investigation

Final report

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The Competition and Markets Authority has excluded from this published version of the report information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. Some numbers have been replaced by a range. These are shown in square brackets. Non-sensitive wording is also indicated in square brackets.

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Background and context to our investigation

1. On 27 June 2013 the Office of Fair Trading (OFT), in exercise of its powers under sections 131 and 133 of the Enterprise Act 2002 (the Act), made a reference to the Competition Commission (CC) for an investigation into the supply of payday lending in the UK. On 1 April 2014, the Competition and Markets Authority (CMA) took over many of the functions and responsibilities of the CC and the OFT, including in relation to this investigation.

2. This report sets out our findings on whether any feature or combination of features in this market prevents, restricts or distorts competition, thus constituting an adverse effect on competition (AEC) along with our decisions on the remedies necessary to address any AEC.

3. The questions that we have considered in this investigation – of whether competition is working well in this sector and what should be done if it is not – are important ones. Effective competition benefits consumers. In a well-functioning market, the competitive process encourages suppliers to keep their prices low, to innovate and to improve the service they provide to consumers. We have found that there is a clear demand for short-term, small-sum credit, which many customers are currently meeting by taking out a payday loan. As with any other market, shortcomings in the competitive process can lead to customers paying more than they need to for their loans.

4. Payday lending has been, and continues to be, an issue which attracts a large amount of political and media attention. In conducting our investigation, we have been aware of the wide range of concerns that regulators, consumer groups, debt-advice charities and other interested parties have expressed about the operation of the payday lending sector. These concerns have centred on a variety of issues, including the cost of borrowing, whether lenders are acting responsibly when assessing whether customers can afford to meet the repayments due on a loan, whether advertisements for payday loans are misleading or inappropriate and whether sufficient forbearance is shown to customers that get into difficulties in meeting repayments.

5. It is clear to us that a number of these important issues go wider than the question of competition in the provision of payday loans which we are required to consider under the market investigation regime. We have been aware of the work undertaken in parallel by the Financial Conduct Authority (FCA) and the other bodies responsible for other aspects of public policy in relation to payday lending, including the introduction by the FCA of its new rules and guidance contained in the Consumer Credit sourcebook (CONC), to

tackle a number of the problems that have arisen in this sector in recent years and which had been identified by the OFT in March 2013 in its review of compliance by payday lenders. In addition to the normal benefits of a competition review, our in-depth market investigation has informed the work of the FCA and of the other stakeholders with an interest in payday lending, by providing detailed evidence and analysis of the way the market operates. We have kept closely in touch with the FCA during our investigation and have shared information and data with the FCA, in response to its requests, in accordance with our own statutory responsibilities in relation to the information we collect.

6. Our investigation has also taken place against the background of substantial changes to the regulation of the sector. The FCA assumed responsibility for consumer credit regulation from 1 April 2014. In October 2013, it published its detailed proposals for the regulation of consumer credit, including payday lending which formed the basis of its new CONC rules that are now in force. As part of this new regime, the FCA has made new rules to address two issues which had been the subject of much public concern – namely the number of times that a loan might be 'rolled over' and the extensive use by lenders of continuous payment authorities (CPAs) to recover debt from a borrower's bank account. Also, following an announcement in November 2013, Parliament passed legislation which placed a duty on the FCA to impose a price cap on the cost of payday loans. The FCA published its consultation paper on its proposals in July 2014 and its final decision on 11 November 2014. The price cap came into force on 2 January 2015. Furthermore, on 1 December 2014 the FCA published a Policy Statement which set out its concerns about the practices of some credit brokers which charge upfront fees to consumers. It introduced new rules targeted at ensuring that key features of brokers' relationships with consumers are transparent, which came into effect on 2 January 2015. The FCA stated it would consult on whether to retain or modify these new rules, and whether to introduce additional rules.

7. In carrying out our work, we have been mindful of the implications of changes to the way that payday lending is regulated and the evolution of the market. The evidence base underpinning our assessment of competition is, by necessity, based on how competition has been working over recent years. In reaching our final conclusions about whether any features of the market lead to an AEC, we have sought to take into account the impact on competition of regulatory changes and other market developments. Similarly, in considering possible remedies, we have considered whether regulatory changes or other market developments are likely to remove the need for remedial action and/or affect the rationale for introducing specific measures.

An overview of the payday lending sector

8. Payday loans are short-term, unsecured credit products, which are generally taken out for 12 months or less. The average loan size in our data set was £260 and nearly all payday loans are for £1,000 or less. Within this broad definition a variety of products are offered, including ‘traditional’ payday loans repayable in a single instalment within one month or less and longer-term loans where the loan is repaid in a number of instalments over several months. The average duration of a payday loan is just over three weeks.

9. The payday loan market grew rapidly between 2008 and 2012, at which point total payday loan revenue was around £1.1 billion, with lenders issuing approximately 10.2 million payday loans, worth £2.8 billion. These figures represented a 35 to 50% increase on the preceding financial year – depending on the way in which the size of the market is measured. Since the peak of 2012 growth rates reduced significantly. Revenue growth was around 5% in 2013. In 2014 the market contracted, and both payday lending revenue and the volume of new loans issued fell year on year by around 27% for the period January to September 2014. Four of the 11 major lenders identified at the start of our investigation, as well as some smaller ones, decided to stop issuing payday loans during 2014.

10. We estimate that there were around 1.8 million payday loan customers in 2012. Customers often take out multiple loans over time and many use more than one lender – we estimate that an average payday loan customer took out around six loans in a 12-month period, and that approximately four in ten payday loan customers used more than one lender in 2012.

11. Payday loans may be taken out online or on the high street. Most payday loan customers borrow online. We found that 83% of payday loan customers have taken out a loan online and 29% of customers have taken out a payday loan on the high street. There is some overlap, with 12% of customers having used both channels. The average amount borrowed on the high street (£180) was significantly lower than that borrowed online (£290).

12. As part of the application process, payday lenders will carry out an assessment of a customer’s creditworthiness and their likelihood of successfully repaying the loan. Most lenders have developed their own automated risk models, of varying degrees of sophistication, to help them make decisions about the creditworthiness of potential applicants, developed using historical customer information. The rate of loan applications that were turned down was well above 50% for many of the 11 major lenders in 2012 and has risen for some operators in the period January to September 2014 as lenders

adjusted their decision criteria to accommodate new FCA rules regarding rollovers and CPA use.

Payday loan customers and their use of payday loans

13. We found that the median net income of an online payday loan customer was £16,500 – broadly similar to that of the wider UK population (£17,500) and significantly more than high street borrowers (£13,400). Overall, the distribution of payday loan customers' incomes was somewhat narrower than that for the UK population – with fewer individuals with particularly low or particularly high incomes. Payday loan customers were more likely to be male and in full-time work than the population as a whole, to be younger than average and to live in larger households.

14. We investigated whether payday loan customers had experienced any credit or financial problems within the past five years. 38% of customers reported that they had experienced a bad credit rating, 35% had made arrangements with creditors to pay off arrears, 11% had experienced a county court judgment and 10% had been visited by a bailiff or debt collector. In total, 52% of customers reported having experienced one or more of these debt problems in the last five years.

15. We asked customers what they had used their most recent payday loan for. Just over half (53%) of customers told us that they had used the money for living expenses (such as groceries and utility bills), 10% said the money related to a car or vehicle expense and 7% said general shopping such as clothes or household items. When asked why they needed to take out a payday loan, 52% of customers said that the loan was linked to an unexpected increase in expenses or outgoings and 19% said the need was due to an unexpected decrease in income. 93% of those who said their need was due to a change in financial circumstances thought this change was temporary whereas 5% expected the change to be permanent. Payday loans are particularly likely to be taken out on Fridays and are somewhat more likely to be taken out at the beginning and end of the month.

16. 64% of payday loans issued in 2012 were repaid in full, either early or on time. 22% of loans were repaid in full, but after the originally agreed repayment date (including loans that were refinanced or 'rolled over'). 14% of loans issued in 2012 had still not been repaid in full by October 2013. Online customers are more likely to repay loans in full on time than high street borrowers and the proportion of customers repaying in full on time varies significantly by lender. Customers who have previously taken out a loan with a particular lender are significantly more likely to repay a subsequent loan with

the same lender in full and on time than are customers taking out their first loan with a lender.

17. When taking out their loan, customers were usually confident about their ability to repay it by the agreed date. However, a significant minority of customers (17%) reported having found getting money to repay their loan to be more difficult than they had expected. This proportion is significantly higher for those customers who: *(a)* had previously taken out payday loans in order to pay off debts to other payday lenders; *(b)* had a poor understanding of financial terms and conditions; *(c)* had been refused loans before; *(d)* had experienced debt problems in the last five years; and *(e)* said that they had taken out a payday loan as a last resort.

Repeat borrowing

18. Customers' demand for payday loans is typically recurring. Our analysis of loan-level data suggests that around three-quarters of customers take out more than one loan in a year, and that on average a customer takes out around six loans per year. These findings are broadly consistent with the results of our customer survey.

19. Furthermore, repeat custom typically accounts for a large proportion of lenders' business. More than 80% of all new loans in our data set that were issued in 2012 were made to customers who had previously borrowed from the lender. On average, payday loan customers took out a further 3.6 loans from the same lender within a year of their first loan from that lender. Around 40% of customers had a borrowing relationship with their lender of more than one year.

20. Many customers also borrow from more than one lender. We estimate that around four in ten payday loan customers borrowed from more than one payday lender in 2012, and that on average a customer used 1.9 lenders. In line with this, 45% of respondents to our customer survey reported having used more than one lender. Much of the use of multiple lenders that we observed took place concurrently – ie while a loan was outstanding with another lender – or following a repayment problem with a previous loan.

21. In addition to taking out new loans, borrowers have been able to extend the duration of their credit with their current lender by rolling over an existing loan. In 2012, around 20% of the loans in our data set were subsequently rolled over – with 16% of online loans and 26% of high street loans rolled over. On average, loans which were being rolled over were extended 2.5 times. The incidence of this practice is likely to have fallen significantly since 2012 in light

of new regulations limiting the number of occasions on which a loan can be rolled over (see paragraph 27).

Payday lenders and other market participants

22. There were at least 90 payday lenders offering loans to UK customers as of October 2013. However, the market has been more concentrated than this figure might suggest, with the three largest lenders (CashEuroNet, Dollar and Wonga) accounting for around 70% of total revenue generated from payday lending in the UK in the 2012 financial year and the ten largest lenders accounting for more than 90%. We also note that a number of providers have stopped issuing payday loans since October 2013.

23. Around 40% of payday loan customers in our data set taking out loans with online lenders applied via the website of a lead generator. Lead generators are companies that contract with payday lenders to provide potential customer applications (or 'leads') in return for a fee for each lead provided. Online customers who do not apply via a lead generator may access lenders' websites directly, or by other means including using a search engine such as Google, via the websites of associated marketing companies and, to a lesser extent historically, by using price comparison websites (PCWs).

24. Most payday lenders purchase information from credit reference agencies (CRAs) regarding applicants when carrying out a credit risk assessment. These CRAs hold large databases of individuals' personal information, past credit history and current credit commitments. This shared data is available on commercial terms to lenders. Historically, lenders have tended to provide information to the largest CRAs on a monthly basis; however, CRAs have made significant progress recently in developing systems to allow lenders to provide and access information in real time or near real time.

The regulation of payday lending

25. As part of its response to the financial crisis of 2008, the Government made important changes to the regulation of financial services and banking in the Financial Services Act 2012. This resulted in the abolition of the Financial Services Authority and the transfer of its functions to two new bodies: the FCA and the Prudential Regulation Authority. That Act also enabled the transfer of regulation of consumer credit from the OFT to the FCA.

26. Payday lenders, like any other consumer credit providers, are subject to a variety of regulatory obligations, most of which are now overseen by the FCA. As such, for example, payday lenders are required to give borrowers specified information before entering into a consumer credit agreement, to conduct a

reasonable assessment of affordability, to monitor repayments and to show forbearance in resolving customers' repayment problems. Now that consumer credit is regulated by the FCA, no person may issue a payday loan, or offer any other form of consumer credit, unless that person holds either an interim permission from the FCA, or has been authorised by the FCA. Over the next two years, payday lenders and other credit providers will be invited to apply for full authorisation. Like other firms regulated by the FCA, all firms providing consumer credit loans will have to comply with the high-level Principles in the FCA's Handbook, for instance with regard to treating customers fairly and cooperating with the regulator.

27. In addition, a number of further FCA rules apply specifically to high-cost short-term credit (HCSTC) lenders (essentially payday lenders). The rationale for these stems from widely expressed concerns about the operation of the payday lending market, including a review by the OFT of compliance by payday lenders which it published in March 2013. This pointed to a significant degree of non-compliance with consumer credit legislation and regulatory requirements. In particular, the FCA's CONC rules and guidance now prohibit lenders from rolling over payday loans more than twice and provide that from 1 July 2014 no more than two unsuccessful attempts to take a payment with a CPA can be made and a CPA must not be used to take part payment.

28. Following an announcement in November 2013, Parliament adopted legislation to impose a duty on the FCA to place a cap on the charges which may be imposed in relation to payday loans. Following consultation by the FCA, the price cap came into force on 2 January 2015 (see paragraph 6).

Assessment of competition in the UK payday lending market

29. In assessing whether competition has been working well for payday loan customers, we looked first at evidence on pricing and other outcomes of the competitive process. We then considered the causes of these market outcomes by examining the adequacy of the competitive constraints acting on payday lenders from other forms of credit, the need to attract and retain customers and the threat of new entry and expansion.

Evidence of market outcomes

30. Prior to the introduction of the price cap, payday lenders have used a variety of pricing structures, such that the amount that a customer pays for a loan usually consisted of several distinct charges or fees. Among other factors, the cost of a loan has typically depended on the desired loan amount, duration and instalment structure; whether the loan is repaid on time, extended or topped up; and whether the customer opts to pay an additional fee in order to

receive the sum borrowed more quickly. Lenders are still able to levy a range of charges and fees but the price cap has imposed constraints on the structure and level of prices that may be charged.

31. We found that the prices of payday loans tended to cluster around a headline price of £30 for a £100, month-long loan. The lenders charging monthly interest around this level included some of the largest providers. In addition, several products with prices that are above £30 for a £100 month-long loan nevertheless carried headline interest rates of approximately 30% a month or 1% per day. This clustering in headline prices emerged over time as increasing numbers of lenders have increased their prices to this level.

32. Nevertheless, we observed some significant variation in the prices that different lenders charged in a number of representative borrowing scenarios. For example, the difference between the cost of borrowing £100 for 28 days using the cheapest product included in our review and the most expensive alternative was £39. The extent of price dispersion was even greater in the event that a customer repaid their loan late.

33. Headline price changes have been infrequent, and prior to the introduction of the price cap, which necessitated a change in lenders' pricing, many lenders have made at most one change to their products' headline rate since 2008. Aside from a small number of developments towards the end of the review period, price reductions, whether by reducing the price of existing products or via the introduction of new products, have been particularly uncommon. There was some evidence of competition between lenders taking place via the use of price promotions, but the coverage of the price promotions used by payday lenders was usually limited.

34. We found that customer demand responded weakly to prices. Where lenders changed their prices, this did not generally result in a significant customer response. Lenders that offered substantially lower rates have not been particularly successful in attracting new business. The submissions of lenders and patterns of price dispersion that we observed suggested that customers were particularly unresponsive to changes in late fees and other charges incurred if a customer did not repay their loan in full and on time. We observed a significant proportion of customers taking out loans that were significantly more expensive for their given borrowing requirements than other payday loan products potentially available to them at the time.

35. We concluded that our analysis of pricing behaviour indicated significant limitations in the effectiveness of competition between payday lenders on prices, and that the competitive constraints that lenders faced when setting their prices were weak.

36. This conclusion is consistent with our profitability assessment, which showed that the average annual return on capital employed of the 11 major lenders included in our analysis ranged between 17 and 44% during the period 2009 to 2013. There was some variation in the profitability of larger and smaller lenders: the three largest lenders achieved high and in some cases exceptional returns which were substantially above our consideration of the cost of capital over the majority of the past five years. Six of the smaller lenders achieved returns in excess of our consideration of the cost of capital for periods ranging from between one and five years. Two of the smaller lenders did not generate a profit during the period. There was some evidence that future profitability may be lower than recent levels, both because of a slowing down in market growth compared with historic rates and due to regulatory changes which may increase costs and/or reduce revenues.

37. In contrast to the evidence on pricing, our analysis suggested that lenders have competed on certain non-price aspects of the product offering – including launching new products and introducing faster payment services and other product features – and lenders told us that they sought to provide good customer service in order to retain borrowers. To some extent, this was supported by reported levels of customer satisfaction, which were high for some lenders. We were also aware, however, that the serious problems identified by the OFT, the FCA and others about irresponsible lending and compliance with lenders' regulatory obligations clearly indicate that not all payday loan customers have benefited from good customer service. While noting this evidence of non-price competition, we took the view that lenders in a well-functioning market would also be expected to compete on prices to a greater degree than we had observed.

Market definition and competition from other forms of credit

38. The characteristics of payday loans differentiate them from many other credit products, which often do not allow customers to borrow such small amounts for short periods, access funds as quickly, or require some security. With the exception of unauthorised overdrafts, borrowing using alternative credit products is generally significantly cheaper than using a payday loan (borrowing a similar amount for a similar duration using an unauthorised overdraft can be substantially more expensive).

39. We noted that it was relatively common for payday loan customers to use other forms of credit. However, a significant proportion of payday loan customers have experienced credit repayment problems in the past, and the evidence that we saw suggested that many customers would be constrained

in the extent to which credit would be available using alternative products at the point at which they take out a payday loan.

40. Customer research suggests that customers taking out a payday loan do not generally consider other credit products to be a close substitute – only 6% of respondents to a survey commissioned by us into the payday lending market reported that they would have used another credit product had they been unable to take out a payday loan. Partly this is due to the fact that many payday loan customers do not have credit alternatives available to them when taking out their payday loan. In addition, some customers may prefer payday loans because of the convenience, speed or discretion associated with these products, or because of a negative perception of alternatives such as a concern that spending on credit cards could more easily get out of control. We saw no substantive evidence of payday lenders taking developments in the pricing of other credit products into account when setting payday loan prices.

41. Given this evidence and the market outcomes that we observed, we reached the view that competition from other credit products was likely to impose only a weak competitive constraint on payday lenders, and in particular on their pricing.

42. We considered whether it was necessary to define separate markets for online and high street lending and/or to identify distinct geographic markets within the UK. We found that, while some customers may have a preference for particular distribution channels, the level of segmentation was not sufficiently great to require us to define separate markets for online and high street payday loans. We noted, in particular, that the possibility of substituting to online lenders was likely to impose a significant constraint on high street lenders. Given this, the lack of local variation in high street lenders' offering and the relative ease with which lenders have been able to open new stores in different local areas, we did not consider that competitive conditions would differ across local areas such that it was necessary for our competition analysis to define separate local geographic markets for high street lending. We did not consider it necessary to define separate local geographic markets for online lending.

43. We therefore concluded that the market relevant to our assessment of competition is the provision of payday loans in the UK.

Competition for payday loan customers

44. We reviewed patterns of shopping around and switching among payday loan customers. Our customer survey indicated that more than half of all payday loan customers do not shop around at all prior to taking out a loan. High street

customers are particularly unlikely to compare different lenders' products before taking out a loan. Where customers do shop around prior to taking out their loan, they most commonly report doing so using information on lenders' websites.

45. Around four in ten payday loan customers have used more than one lender, and so will have some direct experience of the loan terms offered by different suppliers. However, we found that much – though not all – of this use of multiple lenders takes place in situations where customers are constrained in their ability to borrow further amounts from an existing lender – for example, where they already have a loan outstanding with a lender, or have experienced a repayment problem with a previous loan. Where customers are able to access credit from an existing lender and are happy with the level of service provided by that lender, they often do not consider alternative lenders when looking for a subsequent loan.

46. We identified the following combination of market features which have given rise to the limited responsiveness of customer demand to prices that we have observed in the UK payday lending market, and which reduce the pressure for lenders to compete to attract customers by lowering their prices. These features act in combination to deter customers from comparing the different loans available, to impede their ability to do so effectively, and to discourage repeat customers from considering and/or selecting a new lender that offers a better value loan for their needs:

(a) The context in which customers take out payday loans is often not conducive to customers shopping around to find a good-value loan and may amplify the adverse effects of other barriers to shopping around and switching lender. Customers often perceive the need for their loan to be urgent, and attach considerable importance to the speed with which they are able to access credit. Many payday loan customers are also uncertain, often with good reason, about whether, and from whom, they will be granted credit to meet their borrowing requirements. These aspects of the decision-making environment can tend to make customers reluctant to spend time shopping around for the best deal available, and can cause customers to focus on which lender is willing to lend to them (or, for a repeat borrower, to stay with a lender that they previously used) rather than which lender offers the best-value product.

(b) It can often be difficult for customers to identify the best-value loan product on offer given their borrowing requirements. Despite information on headline rates generally being available on lenders' websites or in the shops of high street lenders, customers' ability to use this information to identify the best-value payday loan is impeded by the complexity

associated with making effective price comparisons given variation in product specifications and pricing structures across lenders, and the limited usefulness of the annual percentage rate in facilitating comparisons between payday loans of different durations. Existing PCWs, which might otherwise help customers compare loans, suffer from a number of limitations and are infrequently used.

(c) Customer demand is particularly insensitive to fees and charges incurred if customers do not repay their loan in full on time. Customers tend to be less aware of these potential costs of borrowing than they are of the headline interest rate when choosing a payday loan provider. This is in part because over-confidence about their ability to repay the loan on time can cause some customers to pay only limited attention to these costs when taking out their loan. Even where customers seek to anticipate the costs associated with late repayment, the information generally provided about such costs is significantly less complete, less easy to understand and/or less prominent than information on headline rates. It can therefore be difficult for customers to estimate, and so make effective comparisons about, the likely cost of borrowing if they do not repay their loan in full on time.

(d) Many online customers take out payday loans via a lead generator's website. Lead generators typically promote their ability to find customers a lender willing to offer them a loan within a short period of time. The value for money represented by different lenders' loan offerings is not taken into account in the auction process operated by lead generators. Lead generators instead generally sell customer applications on the most favourable commercial terms for the lead generator – often to the highest bidder. Furthermore, there is often a lack of transparency in how the service that lead generators provide is described in their websites – particularly the basis on which applications are directed to lenders – and many customers do not understand the nature of the service offered by lead generators. An implication of the operation of this distribution channel is that lenders acquiring customers through lead generators are unlikely to have a strong incentive to lower their prices. The lead generator model may also create an incentive for lenders to increase prices to customers, as lenders offering cheaper loans would find it harder to bid high prices in lead auctions and hence acquire valuable leads.

(e) Where their choice of lender is not dictated by concerns about credit availability, customers can be dissuaded from looking at alternative suppliers by the perceived risks associated with using a new lender (ie one they had not used previously), particularly in light of the negative reputation of the payday lending sector. Customers may perceive a loss

of convenience associated with applying to a new lender, particularly if the alternatives are rolling over or topping up an existing loan with an existing lender. These factors further reduce the constraint placed on lenders by the threat that existing customers will switch to another lender offering a better-value product.

47. We concluded that the barriers that we have identified as serving to reduce customers' sensitivity to prices would generally continue to restrict competition between lenders in the presence of the price cap. Although the price cap may lead to some standardisation of payday lending products and may also reduce the risk perceived by customers who are considering switching lender, we did not consider that these effects would increase customers' sensitivity to prices such that the threat of losing business would cause lenders to compete effectively on prices. We considered that this loss of competition would be material (see paragraph 58).

Entry and expansion

48. We noted that the first UK payday lenders began offering loans over ten years ago. Since then, we have observed firms employing a variety of different entry strategies, including start-ups, firms entering by acquisition, entry by North-American-based lenders, and diversification by lenders originally offering non-payday credit products. The payday lending sector as a whole (high street and online) expanded rapidly over the past decade, with growth particularly strong between 2010 and 2012, although this trend has not continued in 2014. Wonga expanded particularly rapidly since its entry in 2008 and CashEuroNet has also increased its share of supply significantly. Entry by companies into the payday lending sector has been observed regularly since 2008, at a rate of at least two to five new entrants per quarter. These patterns indicate that, historically, large numbers of lenders have managed to enter the market, and that a few lenders have been very successful in growing their businesses.

49. Notwithstanding these historic patterns, and as indicated by the evidence on market outcomes, entry by new firms into the payday lending market does not appear to have resulted in existing lenders facing an effective constraint when setting their prices.

50. One reason for this is the factors described above which reduce payday customers' sensitivity to prices, and weaken price competition between lenders. For example, on many occasions where we have observed new providers entering payday lending, these lenders have relied to a large extent on lead generators for new customers. Lead generators have a number of advantages from the perspective of a new entrant or a smaller lender. In particular, they are accessible to all lenders, irrespective of size, and allow

lenders to exercise close control over the volume and profile of customers that they want to attract. Lead generators allow a new entrant to build up a loan book quickly, in loan-by-loan increments, and to their own specification. The use of lead generators by new entrants may also reflect the strength of the well-established brands that already exist in the market and the costs associated with advertising on a sufficient scale to acquire sufficient new customers. As noted in paragraph (d) however, lenders acquiring customers through lead generators are unlikely to have a strong incentive to lower their prices since lenders would have to bid high prices in lead auctions to acquire valuable leads. Therefore a lender sourcing new customers via a lead generator is likely to have little or no incentive to compete on price.

51. In addition, the competitive constraint that might otherwise be imposed on payday lenders' prices by the prospect of new entry or expansion is further weakened by the following market features:

(a) New entrants will face certain disadvantages relative to more established lenders, in particular:

(i) The ability of new entrants to expand and establish themselves as effective competitors is likely to be obstructed by the difficulties associated with raising customers' awareness of their product in the face of the barriers to shopping around and switching summarised in paragraph 46, the strength of the well-established brands that already exist in the market and the costs associated with advertising on a sufficient scale to be effective in overcoming these obstacles.

(ii) While the ability to assess credit risk accurately is a necessary requirement for any provider of personal credit, it is likely to be a particularly important determinant of a provider's success in the payday lending sector, because of the relatively high credit risk profile of payday loan customers and the significant limitations associated with the information available to lenders about these customers from CRAs. Because of their greater reliance on new customers and the role of learning in the credit risk assessment process, new entrants are likely to face some disadvantages in their ability to assess credit risk for a period, which would put them at an initial cost disadvantage relative to more established providers.

(b) The history of non-compliance and irresponsible lending by some payday lenders and the resulting negative reputation of the sector are likely to reduce the constraint imposed on payday lenders' pricing by the prospect of new entry. In particular, the reputation of payday lending is likely to deter some businesses with established reputations in other sectors –

such as mainstream credit suppliers – from entering the market. This reduces the likelihood of entry by parties with the capability to transform the nature of competition in the market. Potential entrants may also be dissuaded from entering payday lending by the difficulty – itself linked to the current reputation of the sector – in establishing banking relationships, and the very small number of suppliers currently willing to provide banking services to payday lenders.

52. We took the view that the recent regulatory developments in the payday lending market were likely to create market conditions that would be less favourable to entry and expansion than those observed historically, and so would reduce the extent of any competitive constraint which the prospect of new entry or expansion might otherwise impose on incumbent lenders. Cumulatively the changes detailed in paragraphs 25 to 28 have made the payday lending market less profitable and could not be expected to address barriers to entry and/or expansion to any material extent.

Findings

53. For the reasons set out above, we have found, pursuant to section 134(1) of the Act, that there are a number of features in the provision of payday loans in the UK which contribute to, and help to explain, the failure by many payday lenders to compete on price and which either alone or in combination give rise to an AEC within the meaning of section 134(2) of the Act. These features are:

(a) The structural and conduct features set out in paragraph 46, which limit the extent to which customer demand is responsive to the price of payday loans, and so reduce the pressure for lenders to compete to attract customers by lowering their prices. These features relate to: (i) the context in which customers take out payday loans; (ii) difficulties customers face in identifying the best-value loan for them; (iii) customer insensitivity to fees and charges incurred if they do not repay their loan in full on time, itself linked to the difficulty of finding out the relevant information; (iv) the operation of the lead generator distribution channel; and (v) the perceived risks and loss of convenience of switching lender.

(b) The structural features summarised in paragraph 51 which weaken the competitive constraint that might otherwise be imposed on payday lenders' prices by the prospect of new entry or expansion by smaller lenders. These features relate to: (i) disadvantages faced by new entrants in raising customers' awareness of their product (partly because of the features described above in subparagraph *(a))* and in assessing credit

risk; and (ii) the impact of the reputation of the payday lending sector in deterring potential entrants.

54. We identified two sources of customer detriment which are likely to arise as a result of the AEC. We have identified that:

(a) Some customers currently pay more for their loans than they would if price competition were more effective.

(b) There may be less innovation on pricing (eg in relation to the introduction of risk-based pricing or flexible pricing models) than we would observe in a market in which price competition were more effective.

55. We considered the extent to which the AEC has given rise to customer detriment to date and may be expected to give rise to customer detriment in future.

56. Looking at the period to the end of 2014, the AEC is likely to have led to customers paying higher prices for payday loans – and to have resulted in reduced innovation in pricing structures (eg in relation to the introduction of risk-based pricing or flexible pricing models) among payday lenders – than we would have expected to observe in a well-functioning market. Lower-risk customers, borrowers repaying their loan late, borrowers paying upfront fees and borrowers using 'traditional' 30-day payday lending products to borrow for relatively short periods are likely to have overpaid by a particularly significant amount.

57. The extent to which customers have paid more for their payday loans than in a well-functioning market – and hence the scale of this aspect of the customer detriment caused by the AEC – is likely to have been material. On the basis of different plausible assumptions about the level of prices that might be observed in a market in which price competition were more effective, we estimated that, in our mid-price case, the lack of effective price competition has meant that, on average, borrowers have overpaid for their loans by an amount in the order of magnitude of around £5 to £10 per loan. The extent of historic overcharging could be higher still (up to £14 per loan) relative to scenarios that reflected the lower prices that had been on offer in the market – our low-price case. This is relative to a typical loan of £260 taken out for just over three weeks, and with a total cost of credit for a customer that repays in full and on time of around £75. Applying these savings to the total number of loans issued in 2012 that were repaid in full would imply, in the mid-price case, a total potential overpayment for these loans of around £48–£85 million in that year. The total potential overpayment in that year could have been as

high as £74–£127 million relative to scenarios in which the competitive price was closer to the low-price case.

58. We note the price cap has now capped payday loan prices below the mid-price case, but the cap is still above the low-price case which we considered to be more relevant to assess the forward looking detriment in light of the downwards trend in many categories of lenders' costs (see below). By forcing down the prices of payday loans, the price cap will mitigate some of the harm to customers that has arisen from high prices. Nevertheless, we considered that even in the presence of the price cap, significant scope for price competition between payday lenders to further improve customer outcomes would be achievable in the absence of the market features that we have identified. This implies that a material customer detriment would arise from the AEC if it were left unaddressed, and the gains of effective competition were foregone. In particular:

(a) There is a risk that the price cap may become the benchmark for the pricing of payday loans. Even in the short term, some lenders' costs are likely to allow them to price beneath the level of the price cap for their products. As such there is likely to be some scope for these lenders to undercut their rivals in the event that competition became more effective.

(b) More effective competition is likely to increase the pressure on lenders to compete for lower-cost customer groups – for example, through increased innovation in pricing structure. Such customers might be offered prices significantly beneath the price cap.

(c) In the longer term we would expect to observe a downwards trend in many categories of lenders' costs including, for example, cost reductions from cost efficiencies, lower lead prices and a reduction in impairment costs for lenders participating in real-time data sharing (RTDS). Without effective price competition, there will be no pressure for lenders to pass any cost reductions of this type on to customers.

59. Put another way, in the absence of effective price competition, there will be no incentive for lenders to reflect their costs in the prices charged to customers in the future, irrespective of technological developments, evolution in the products on offer, or changes in market structure. For this reason, we concluded that the scale of the customer detriment caused by the AEC was likely to continue to be material, notwithstanding the reduction in prices brought about by the cap.

Remedies

60. To remedy the AEC which we have found we have decided to introduce a package of remedies comprising the following elements:

(a) Measures to promote the use of effective PCWs.

(b) A recommendation to the FCA to take steps to improve the disclosure of late fees and other additional charges.

(c) A recommendation to the FCA to work with lenders and other market participants to help customers shop around without unduly affecting their ability to access credit.

(d) A recommendation to the FCA to take further steps to promote RTDS between lenders.

(e) A requirement for lenders to provide existing customers with a summary of the cost of borrowing.

(f) A recommendation to the FCA to take steps to increase transparency around the role of lead generators.

Measures to promote the use of effective PCWs

61. Our principal remedy is the promotion of greater use of PCWs by customers and an improvement in the quality of the PCWs used by customers to enable customers to shop around more effectively when choosing a payday loan. We considered that this would be likely to lead to greater price competition between payday lenders and would improve the ability of customers to find the most appropriate payday loan for their needs. This remedy would also make it easier for new entrants with attractive products to enter the market.

62. This remedy will address the difficulty faced by customers in identifying the best-value or most appropriate loan product on offer for them. Making comparisons across products which differ in their duration and/or other characteristics can be difficult and existing PCWs suffer from a number of limitations.

63. We considered that commercial providers of comparison services would be best placed to develop payday lending comparison tools capable of evolving as the payday lending market itself develops. However, we considered there was also value in ensuring that these commercial operators would provide the core functionality on their sites that we identified was necessary to allow customers to make accurate comparisons.

64. We further considered that a stronger competitive dynamic would be fostered by allowing multiple website operators to compete to innovate to service borrowers' needs. In our provisional decision on remedies (PDR) we provisionally decided that an accreditation scheme, which allowed for the accreditation of multiple PCWs which met defined criteria, would be a practical way of achieving this objective. This is consistent with existing accreditation schemes operated in the energy and telecommunications sectors. We considered that the FCA would be the best placed body to accredit PCWs that offered payday loan price comparison services.

65. In response to the PDR the FCA told us that operators of PCWs were already likely to require its permission to act as credit brokers. The FCA said it was concerned that accreditation would lead to a two-tiered regulatory system and requested that we consider amending our recommendation so that the FCA uses the tools at its disposal to raise the standards of all PCWs. We consulted on this change and, based on the views of parties, we have decided to recommend to the FCA to introduce standards for payday loan PCWs through its existing legal framework.

66. In our PDR we provisionally decided that, to encourage the development of a dynamic, high-quality price comparison sector for payday loans, we would issue an Order specifying that all payday lenders would be prohibited from supplying payday loans unless details of their prices and products were published on at least one accredited PCW, a link to which would be included on their own website. After publication of the PDR a number of PCW operators told us that they had little experience of providing comparison services for products which were not available online and raised concerns about the difficulties associated with listing high street lenders on their website.

67. In view of these concerns, we decided that high street lenders might encounter difficulties in agreeing commercial terms with PCWs and this might discourage PCWs from comparing payday loan products if the PCWs perceived that they would be obliged to include high street lenders on the PCW and believed that this was unviable. We therefore decided that lenders who only offer loans on the high street should not be obliged to have the details of their loans published on an authorised payday loan PCW but may nonetheless seek to be listed. We note that high street lenders would still be required to include on the summary of borrowing (see paragraphs 81 to 83) the web address of an authorised payday loan PCW or (if created) of a portal listing all authorised payday loan PCWs.

68. In response to concerns raised by lenders we noted that there was a risk that an authorised payday loan PCW might not allow a given lender to appear on

its listing. We acknowledge this risk and have introduced protections for lenders where they are unreasonably excluded from all authorised payday loan PCWs and have recommended to the FCA that consideration is given as to how to encourage authorised payday loan PCWs to be open to all lenders to better facilitate comparisons.

69. We have therefore decided to revise the Order that we had proposed so that online lenders will be prohibited from supplying payday loans to customers in the UK unless details of their payday loan products are published on at least one payday loan PCW which is operated by an FCA-authorised person following the FCA's implementation of additional standards. Where an online lender can demonstrate that it has been unreasonably excluded from all authorised payday loan PCWs, this prohibition will not apply.

70. Where no authorised payday loan PCW exists within the later of 12 months after the FCA publishes its decision or the date the FCA's new standards become effective and no applications for authorisation of a payday loan PCW are being considered by the FCA, online lenders individually or collectively will be given a further period of 6 months to commission a payday loan PCW and apply for authorisation. Where good progress can be demonstrated a further period of up to six months will be allowed by the CMA. Details of lenders' payday loan products must appear on the PCW within 3 months of it being authorised.

71. To address identified shortcomings of existing payday loan PCWs, the CMA further recommends that the FCA reviews its requirements for payday loan PCWs and uses its regulatory tools to raise the standards which apply to payday loan PCWs. We decided that the FCA is the best-placed body to perform this function and that operating the authorisation process would have synergies with the FCA's ongoing regulatory role. If the FCA accepts our recommendation, it would be for it to determine the precise standards to consider as part of this authorisation process, but on the basis of the evidence and the AEC we have found we have proposed a number of high-level standards for authorisation. We recommend that:

(a) The FCA seeks to ensure that authorised payday loan PCWs enable customers to view loans ranked on the basis of objective criteria and the default ranking should be the total amount payable, presenting loan product information/results of the customer's searches in ascending order of total amount payable (the cost of the loan plus interest and other charges) unless the borrower requests a different presentation. In the event of different products having the same price, any secondary ranking should be on the basis of objective factors that are of benefit to customers and not be linked to the commercial interests of the PCW or of any lender.

(b) Advertising on an authorised payday loan PCW should be clearly differentiated from the ranking of loan products so that customers are not drawn away from the objective ranking of products by banner advertisements.

(c) The authorised payday loan PCW should provide a search function that returns results that reflect the key features of the loan the customer is seeking. Such functionality could include, for example, the ability to specify a desired loan amount, term (or repayment date) and repayment structure (eg the number of instalments).

(d) The authorised payday loan PCW should be as transparent as possible about all features of the loan, including the consequences of late or non-payment. We consider that customers would particularly benefit if they were presented with information about late fees and charges as well as the effect of early repayment on the price of the loan.

(e) The FCA seeks to ensure that authorised payday loan PCWs include only loan products in their loan comparison tables and do not include brokers or other intermediaries in their loan comparison tables.

(f) The FCA seeks to ensure that authorised payday loan PCWs disclose to customers the number of lenders the PCW covers.

(g) The FCA considers how to ensure that authorised payday loan PCWs comply with all relevant laws and regulations since the effectiveness of this remedy will be enhanced if customers have confidence that they are transacting with a reputable provider.

72. This measure is the central element of our remedy package, which is supported by a number of our other remedies.

Increased transparency on late fees and charges

73. We have decided to recommend that the FCA take the necessary steps to ensure that payday lenders improve their disclosure of these fees and charges. This is an area already subject to FCA regulation, and is covered by the provisions of the Consumer Credit Directive (CCD). Further action taken by the FCA in this area will be supported by other elements of the remedy package, including the authorisation of payday loan PCWs and the disclosure of late fees and other charges incurred on previous loans as part of our requirement for lenders to provide a summary of the cost of borrowing.

74. This remedy will address the shortcomings in information provided about fees and charges by lenders (despite existing rules which require disclosure of this

information) which mean that it can be difficult for customers to estimate, and so make effective comparisons about, the likely cost of borrowing if they do not repay their loan in full and on time.

Measures to help borrowers shop around without unduly affecting their access to credit

75. We expect that our remedy to promote the use of good-quality PCWs will encourage borrowers to shop around when searching for a payday loan. In support of these measures, we wish to ensure that customers are not discouraged from doing so by the risk of obtaining a poor credit rating by appearing to be taking out multiple loans simultaneously.

76. Customers are in general not currently able to assess their eligibility for a loan without undergoing a full credit check and they may not be aware of when such a check is taking place. We also found that the presence of multiple credit searches on a customer credit record is a factor that may negatively influence a lender's decision to issue a loan. This is because a customer who is shopping around can leave a similar record on their credit file to a customer who is very 'credit-hungry'. Customers may therefore perceive a risk that multiple credit checks could adversely affect their ability to borrow in the future and may be therefore discouraged from shopping around.

77. We therefore recommend that the FCA works with payday lenders, CRAs and authorised payday loan PCWs to improve the ability of customers to search the market without adversely affecting their credit history.

78. We recognised the potential costs (both the cost of additional searches and the costs of amending lending systems) of requiring all payday lenders to offer quotation searches which do not leave a record that is visible to other potential lenders. We have therefore decided not to mandate the use of such searches using our own formal powers. However, should it decide to take forward our recommendation, we would expect the FCA to encourage lenders and other market participants to take practical steps to help improve the ability of customers to shop around for loans without damaging their credit score.

Measures to encourage development of real-time data sharing

79. We have also found that there are benefits to both lenders and borrowers if lenders are able to access credit information that is updated in real time, principally:

(a) We would expect that greater use of RTDS would enable new entrants to the payday lending market and smaller lenders to gain access to better quality credit data more easily.

(b) We would expect further developments in RTDS to work in support of our recommendation to promote greater use of quotation searches and other measures to encourage borrowers to shop around as it will improve lenders' ability to differentiate these borrowers from those who are seeking to access multiple sources of credit simultaneously.

80. We are therefore also recommending to the FCA that it continues to work closely with lenders and CRAs to encourage the development and use of real-time data.

Summary of the cost of borrowing

81. Payday loan customers may be unaware of, or unwilling to consider, the total costs caused by their use of payday loans. We found that repeat borrowers can be dissuaded from looking at alternative suppliers by the perceived risks associated with using an unknown lender. Borrowers may also perceive a loss of convenience associated with applying to a new lender, particularly if the alternative is rolling over or topping up an existing loan with an existing lender. Our investigation has also indicated that the cumulative cost of taking out payday loans can be considerable – with customers taking out around six loans per year on average – and that payday loan customers can be unaware of, or unwilling to consider, the total costs of using payday loans over time.

82. Requiring payday lenders to provide a clear summary of the actual costs that a borrower has incurred at the end of a loan period would encourage borrowers to consider and search for lower-cost alternatives. We would expect that information on the actual cost of a recent loan would also encourage some borrowers to anticipate the likely future costs of a loan more realistically.

83. We have therefore decided to issue an Order requiring payday lenders to provide their borrowers with details of the charges that the borrower has paid on both the most recent loan and also over the last 12 months and the web address of one or more authorised payday loan PCWs or a portal listing all authorised payday loan PCWs. This would be available from when a loan has been repaid. Lenders should take all reasonable steps to bring the summary to borrowers' attention. To demonstrate this, before an existing borrower commences a further loan application process with a lender, the lender should request that a borrower confirms that they are aware that they have had the opportunity to access the summary issued following the conclusion of the

borrower’s most recent loan with that lender. At the point of this confirmation, a link should be available for the borrower to access the summary, or, for high street lenders, borrowers should be reminded of the availability of the summary.

Transparency regarding the role of lead generators

84. We have found that the role of lead generators (including pingtree operators, fee-charging brokers and the affiliates and marketing companies that collect borrower details) contributes materially to the AEC and, in particular:

(a) many borrowers that use a lead generator’s website to find a loan are unaware of the fact that they are using a lead generator and believe they applied directly to a lender; and

(b) there is a lack of transparency in how lead generators describe the service they provide and the commercial relationship that the lead generator has with lenders on their websites. Applicants are typically referred to the lender that offers the lead generator the best commercial deal rather than to the lender that offers the most suitable loan for the customer’s needs.

85. We have therefore decided to recommend that the FCA take the steps necessary to address both dimensions of this lack of transparency.

86. We expect this to lead to a reduction in the number of instances where customers confuse lead generators with lenders, or use lead generators in the erroneous expectation that these intermediaries will match them with the best loan for their requirements. This is likely to induce some customers to engage in more research, for example, by using an authorised payday loan PCW.

87. We also expect this remedy to increase the likelihood that customers will make an informed decision to use a lead generator as an active choice, rather than as a result of a misunderstanding or by chance, and it will thereby play a part in improving the reputation of the market.

88. Given wider concerns about customer detriment in this sector, in particular relating to fee-charging brokers and the subsequent use of data provided to lead generators by potential borrowers, we also recommend that the FCA continues to prioritise its review of the operation of this sector. On 1 December 2014 the FCA published a policy statement introducing new rules, which were targeted at ensuring that key features of brokers’ relationships with consumers are transparent. The rules came into effect on 2 January 2015. The FCA is consulting on the rules. We considered that if they are retained post consultation, the rules would make it clearer that a lead

generator is not a lender but do not address our concern about lead generators selling leads to lenders. We recommend that lead generators should be required to state that application details are referred to the lender that offers the lead generator the best commercial deal rather than to the lender that offers the most suitable loan for the customer's needs.

Assessment of effectiveness and proportionality

89. We have decided that the remedy package represents a comprehensive and effective solution to the AEC that we found.

90. We have further decided that:

(a) Each of the remedy measures that forms part of our package of remedies is capable of effective implementation, monitoring and enforcement.

(b) The ongoing monitoring and compliance costs of the package of remedies are likely to be reasonable. Based on the cost estimates provided by parties, we consider that the remedies package in total is likely to cost less than £2.5 million to implement and to have ongoing costs of less than £1 million per year.

(c) We would expect to be able to put in place an order within six months of publishing our final report in relation to those measures that the CMA will implement (ie the prohibition on lenders from supplying payday loans unless details of their prices and products are published on at least one authorised payday loan PCW and the obligation on payday lenders to provide customers with a summary of their borrowing history). The timescale for implementing the measures that we recommend the FCA to implement will depend upon the time required for the FCA to consult on the measures and the time allowed for their implementation. We expect that all remedies would be implemented and have a beneficial impact on market outcomes within around two years following the publication of our final report.

91. In relation to the proportionality of our package of remedies, we decided that, having evaluated the potential benefits and costs of these measures, the beneficial effects that would flow from addressing the AEC are likely to outweigh significantly the costs of introducing our remedies. Having considered various alternatives, we were unable to identify a less onerous package of measures that would be similarly effective. We decided that our package of remedies represented a proportionate solution to the AEC and the resulting customer detriment.

92. Therefore we have decided that this package of remedies represents as comprehensive a solution as is reasonable and practicable to the AEC and the resulting customer detriment which we have found.

Findings

1. Introduction

The reference and statutory task

1.1 On 27 June 2013 the OFT, in exercise of its powers under sections 131 and 133 of the Enterprise Act 2002 (the Act), made a reference to the CC for an investigation into the supply of payday lending in the UK. The terms of reference for our investigation are provided in Appendix 1.1.[1] This document sets out our findings from this investigation.

1.2 On 1 April 2014, the CMA took over many of the functions and responsibilities of the CC and the OFT.[2] Accordingly, the functions of the CC in relation to the reference were transferred to the CMA.[3] These findings are now published by the CMA in exercise of its functions under section 136(1) of the Act, read with paragraph 2 of the Schedule to the Order.

1.3 The CMA is required by section 134(1) of the Act to determine whether any feature or combination of features in this market prevents, restricts or distorts competition in connection with the supply or acquisition of any goods or services in the UK or a part of the UK, thus constituting an AEC.[4]

1.4 Under section 131(2) of the Act, a 'feature' of the market can refer to: *(a)* the structure of the market concerned or any aspect of that structure; *(b)* any conduct (whether or not in the market concerned) of one or more than one person who supplies or acquires goods or services in the market concerned; or *(c)* any conduct relating to the market concerned of customers of any person who supplies or acquires goods or services.

1.5 If the CMA finds that there is an AEC, it is required under section 134(4) of the Act to decide whether action should be taken by it, or whether it should recommend the taking of action by others, for the purpose of remedying,

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[1] In the course of our investigation we found the operation of the lead generator channel contributed materially to the AEC we had provisionally identified. As a result we consulted on amending our terms of reference in June 2014. The CMA board considered the responses to the consultation and approved the Group's request. See the Notice of a variation in the terms of reference, 22 July 2014 (Appendix 1.1).
[2] The CMA works to promote competition for the benefit of consumers, both within and outside the UK. It aims to make markets work well for consumers, businesses and the economy.
[3] This transfer was under Schedule 5 to the Enterprise and Regulatory Reform Act 2013 and the Schedule to the Enterprise and Regulatory Reform Act 2013 (Commencement No. 6, Transitional Provisions and Savings) Order 2014 (the Order).
[4] Our guidelines state: 'A market investigation may examine any competition problem and identify the feature causing the problem. It aims only to see if competition within the particular market under review is working well or can be improved and is not seeking to establish general rules and obligations for firms.' (*Guidelines for market investigations: Their role, procedures, assessment and remedies, CC3* (the Guidelines), paragraphs 18–21.)

mitigating or preventing the AEC, or any detrimental effect on customers[5] so far as it has resulted from, or may be expected to result from, the AEC; and, if so, what action should be taken and what is to be remedied, mitigated or prevented. The Act requires the CMA 'to achieve as comprehensive a solution as is reasonable and practicable to the AEC and any detrimental effects on customers so far as resulting from the AEC'.[6] In considering remedies, the CMA may take into account any relevant customer benefits (RCBs), as defined in the Act, arising from the feature or features of the market.[7]

1.6 This section provides the context of the investigation, an overview of the conduct of the investigation, and the structure of the remainder of the report.

Context of the investigation

1.7 The questions that we have considered in this investigation – of whether competition is working well in this sector and what should be done if it is not – are important ones. Effective competition benefits consumers. In a well-functioning market, the competitive process encourages suppliers to keep their prices low, to innovate and to improve the service they provide to consumers. We have found that there is a clear demand for short-term, small-sum credit, which many customers are currently meeting by taking out a payday loan. As with any other market, shortcomings in the competitive process can lead to customers paying more than they need to for their loans.

1.8 Payday lending has been, and continues to be, an issue which attracts a large amount of political and media attention. In conducting our investigation, we have been aware of the wide range of concerns that regulators, consumer groups, debt-advice charities and other interested parties have expressed about the operation of the payday lending sector. These concerns have centred on a variety of issues, including the cost of borrowing, whether lenders are acting responsibly when assessing whether customers can afford to meet the repayments due on a loan, whether advertisements for payday loans are misleading or inappropriate and whether sufficient forbearance is shown to customers that get into difficulties in meeting repayments.

1.9 It is clear to us that a number of these important issues go wider than the question of competition in the provision of payday loans which we are required to consider under the market investigation regime. We have been aware of the work undertaken in parallel by the FCA and the other bodies

[5] A detrimental effect on customers is defined in section 134(5) of the Act as one taking the form of: *(a)* higher prices, lower quality or less choice of goods or services in any market in the UK (whether or not the market to which the feature or features concerned relate); or *(b)* less innovation in relation to such goods or services.
[6] Section 134(6) of the Act.
[7] Section 134(7) of the Act.

responsible for other aspects of public policy in relation to payday lending, including the introduction by the FCA of its new CONC rules, to tackle a number of the problems that have arisen in this sector in recent years and which had been identified by the OFT in March 2013 in its review of compliance by payday lenders. In addition to the normal benefits of a competition review, our in-depth market investigation has informed the work of the FCA and of the other stakeholders with an interest in payday lending, by providing detailed evidence and analysis of the way the market operates. We have kept closely in touch with FCA during our investigation and have shared information and data with the FCA, in response to its requests, in accordance with our own statutory responsibilities in relation to the information we collect.

1.10 Our investigation has also taken place against the background of substantial changes to the regulation of the sector.[8] The FCA assumed responsibility for consumer credit regulation from 1 April 2014. In October 2013, it published its detailed proposals for the regulation for consumer credit, including payday lending which formed the basis of its new CONC rules that are now in force. As part of this new regime, the FCA made new rules to address two issues which had been the subject of much public concern – namely the number of times that a loan might be 'rolled over' and the extensive use by lenders of CPAs to recover debt from a borrower's bank account. Also, following an announcement in November 2013, Parliament passed legislation which placed a duty on the FCA to impose a price cap on the cost of payday loans. The FCA published its consultation paper on its proposals in July 2014[9] and it published its final decision on 11 November 2014.[10] The price cap came into force on 2 January 2015.

1.11 In carrying out our work, we have been mindful of the implications of changes to the way that payday lending is regulated and the evolution of the market. The evidence base underpinning our assessment of competition is, by necessity, based on how competition has been working over recent years. In reaching our final conclusions set out in Section 8 about whether any features of the market lead to an AEC, we have sought to take into account the impact on competition of regulatory changes and other market developments. In considering possible remedies in Section 9, we have considered whether regulatory changes or other market developments are likely to remove the need for remedial action and/or affect the rationale for introducing specific measures.

[8] We summarise the legislative framework governing payday lending and how this has changed in Section 3 and Appendix 3.1.
[9] FCA, CP14/10 Proposals for a cap on high-cost short-term credit.
[10] FCA, PS14/16: Detailed rules for the price cap on high-cost short-term credit.

Conduct of the investigation

1.12 During our investigation, we have published a considerable number of documents (including the issues statement, the annotated issues statement, our provisional findings, notice of possible remedies, addendum to our provisional findings, provisional decision on remedies, amendments to proposed remedies consultation and various working papers and other evidence gathered) on the CMA webpages. We describe in Appendix 1.1 the process we followed in our investigation and how we utilised the evidence, data and information we received.

Structure of final report

1.13 This document, together with its appendices, constitutes our final report. It refers, where appropriate, to material published separately on the CMA webpages. The report, however, is self-contained and is designed to provide all material necessary for an understanding of our findings.

1.14 The remainder of this report is set out as follows:

- Section 2 describes the background to the payday lending sector, including information about customers and their use of payday loans.

- Section 3 provides information on the relevant policy frameworks and regulation of the industry.

- Section 4 sets out our analysis of market outcomes, including prices, profitability and various indicators of non-price competition.

- Section 5 considers market definition including the constraints from other forms of credit.

- Section 6 considers the extent and nature of rivalry between payday lenders, with a particular focus on the role played by payday loan customers in driving competition, and assesses whether there are any barriers to effective competition arising on the demand side of the market.

- Section 7 considers entry conditions and assesses whether there are barriers to entry and/or expansion in the market.

- Section 8 presents our findings in relation to whether there are features of any relevant market that give rise to an AEC and result in customer detriment.

- Section 9 sets out our decisions on remedies.

1.15 Appendices supporting each section are numbered according to the first section where they are relevant and are listed in full in the table of contents at the beginning of this report.

2. Background to the payday lending sector

Introduction

2.1 In this section we provide background information on the payday lending sector. It describes:

(a) the main characteristics of payday loans (paragraphs 2.2 to 2.16);

(b) some of the main characteristics of payday loan customers (paragraphs 2.17 to 2.24);

(c) the way in which customers use payday loans (paragraphs 2.25 to 2.56);

(d) the high street and online distribution channels and the characteristics of customers who use each channel (paragraphs 2.57 to 2.63);

(e) the application and approval process for payday loans (paragraphs 2.64 to 2.73);

(f) the size and structure of the payday loan sector (paragraphs 2.74 to 2.80);

(g) the main providers of payday loans (paragraphs 2.81 to 2.124);

(h) the role of lead generators in the payday loan sector; (paragraphs 2.129 to 2.154); and

(i) other participants in the sector such PCWs (paragraphs 2.155 to 2.170).

Basic characteristics of a payday loan

2.2 We considered the basic characteristics of payday loans and how we should define a payday loan for the purpose of this investigation.

2.3 Payday lending is defined in our terms of reference 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 customer's next payday or at the end of the month, and specifically excluding home credit loan agreements, credit cards, credit unions and overdrafts'.[11] The term 'payday loans' is not used exclusively to refer to loans linked to the borrower's payday.

2.4 In its rules and guidance contained in the Consumer Credit sourcebook (CONC), the FCA has adopted a similarly broad definition so as to capture the

[11] See Appendix 1.1.

range of different short-term unsecured loan products on offer in the payday lending sector. It uses the term 'high-cost short-term credit', to reflect the fact that loans are not necessarily paid back on the borrower's payday, and to capture longer-term products that are repaid over several months. It defines HCSTC as regulated credit agreements:

(a) which are borrower–lender or P2P[12] agreements; and

(b) in relation to which the annual percentage rate (APR) is equal to or exceeds 100%, either:

  (i) in relation to which a financial promotion indicates that the credit is to be provided for any period up to a maximum of 12 months or otherwise indicates that the credit is to be provided in the short term; or

  (ii) under which the credit is due to be repaid or substantially repaid within a maximum of 12 months of the date on which the credit is advanced;

(c) which is not secured by a mortgage charge or pledge; and

(d) which is not:

  (i) a credit agreement in relation to which the lender is a community finance organisation; or

  (ii) a home credit loan agreement, a bill of sale loan agreement or a borrower–lender agreement enabling a borrower to overdraw on a current account or arising where the holder of a current account overdraws on the account without a prearranged overdraft or exceeds a prearranged overdraft limit.[13]

2.5 A range of different types of product are captured within these definitions, with variation in terms of how long money can be borrowed for (ranging from a day up to a year or more) and how much can be borrowed (from small, fixed amounts to larger amounts that are repaid in instalments). A notable recent trend has been the development of instalment loans to replace, or be offered alongside, more 'traditional' fixed term payday loan products that require the

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[12] Peer-to-peer lending (abbreviated frequently as P2P lending) is the practice of lending money to unrelated individuals, without going through a traditional financial intermediary such as a bank or other traditional financial institution. This lending takes place online on peer-to-peer lending companies' websites using various different lending platforms and credit checking tools.
[13] Glossary of Definitions, *FCA Handbook*; FCA 2014/12 Consumer Credit (Consequential and Supplementary Amendments) Instrument 2014, Annex A, Amendments to the Glossary of Definitions.

loan to be repaid in a single repayment on a borrower's payday, generally within 30 days or fewer.

2.6 Building on the approach taken by the OFT and FCA, and in light of our own analysis described below (see paragraphs 2.7 to 2.16), we have defined payday loans for the purpose of this investigation as being short-term, unsecured credit products which are generally taken out for 12 months or less, and where the amount borrowed is generally £1,000 or less. In line with our terms of reference, home credit loan agreements, credit cards, overdrafts, credit union loans and retail credit are all excluded from the scope of this investigation, though we consider the competitive constraint from these and other forms of credit in Section 5.

2.7 In this report we discuss two lending channels through which lenders can issue loans to customers. The first channel requires customers to visit a lender's (or intermediary's) website in the first instance, which we refer to as 'online' and the second channel requires customers to visit a retail store which we refer to as 'high street'.[14] We discuss the differences in these channels (and the customers who use them) in greater detail in paragraphs 2.57 to 2.63.

2.8 We describe the different types of payday loan products offered by the major payday lenders and their characteristics in greater depth in Appendix 2.1.

2.9 Notwithstanding this variation between products, there are some common characteristics, particularly in terms of the size and duration of loans which help differentiate payday lending from other forms of credit. We used transaction data provided by 11 of the largest lenders[15,16] in order to identify and analyse the common characteristics of payday loans – see Appendix 2.2 for further details of the data set and how it was prepared.

2.10 Payday loans are typically for relatively small amounts. In terms of loan size, the minimum value of payday loans offered by suppliers is usually £100 or less. For shorter-term products, the maximum amount that can be borrowed by a new customer generally lies between £100 and £500. Repeat customers

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[14] Some lenders offer a 'text message loan' service, which allows customers to request a loan by sending a short message service (SMS) text message to a lender. However, these services require customers to create an account online.
[15] These lenders were identified on the basis of various criteria (see Appendix 2.5 for further details), including their size in 2012. Since then some of these lenders have either temporarily or permanently ceased issuing payday loans (see paragraph 2.74). Nonetheless the information provided by these 11 lenders during the investigation has been key to inform our assessment of the functioning of the payday lending sector and, for simplicity, we will refer to them as 'the 11 major lenders' throughout the final report.
[16] The 11 major lenders comprise Ariste, CashEuroNet, CFO Lending, Cheque Centres, Dollar, Global Analytics, H&T, MYJAR, SRC, The Cash Store and Wonga.

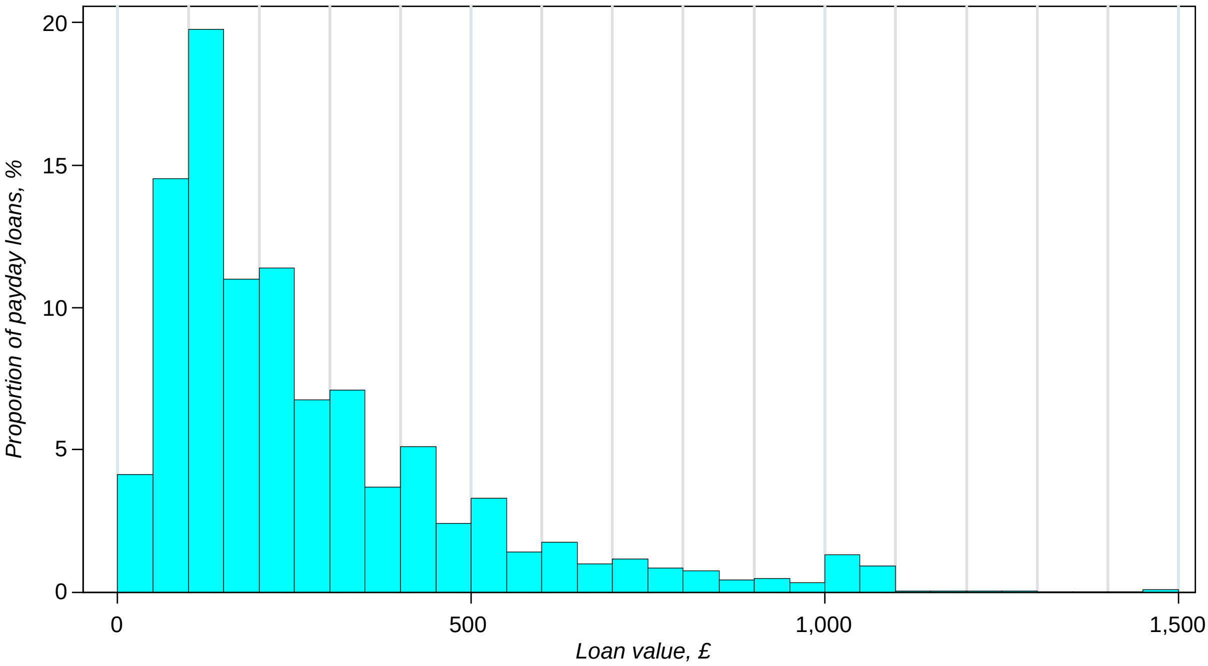
and those using longer-term products are often able to borrow higher amounts, although rarely more than £1,000.

2.11 Our analysis of transaction data[17] found the average size of a payday loan to be £260. The single most common amount borrowed was £100: amounts of £50, £150, £200 and £300 were also relatively common.[18] Around 25% of all payday loans were for £100 or less, half were for £200 or less, and 90% were for £570 or less. The average value of a payday loan varies substantially across lenders, from £163 for [✂], up to £326 for [✂].[19] Figure 2.1 shows the overall distribution of loan values in our transaction database.

2.12 Responses to our customer survey suggested that high-income customers, older customers, those in full-time employment and those who owned their own house all took out larger than average loans. Unemployed customers were the customer group found to have the lowest average loan value.

FIGURE 2.1

Distribution of loan values



Source: CMA analysis of transaction data.
Notes:
1. Analysis covers the 12 months to 31 August 2013.
2. Loan value includes top-ups made on the original loan but excludes any fees deducted from the sum advanced.

[17] For loans issued between September 2012 and August 2013.
[18] Source: Customer and transaction level descriptive presentation, slide 21.
[19] We describe the structure and operations of some of the largest lenders from paragraph 2.82.

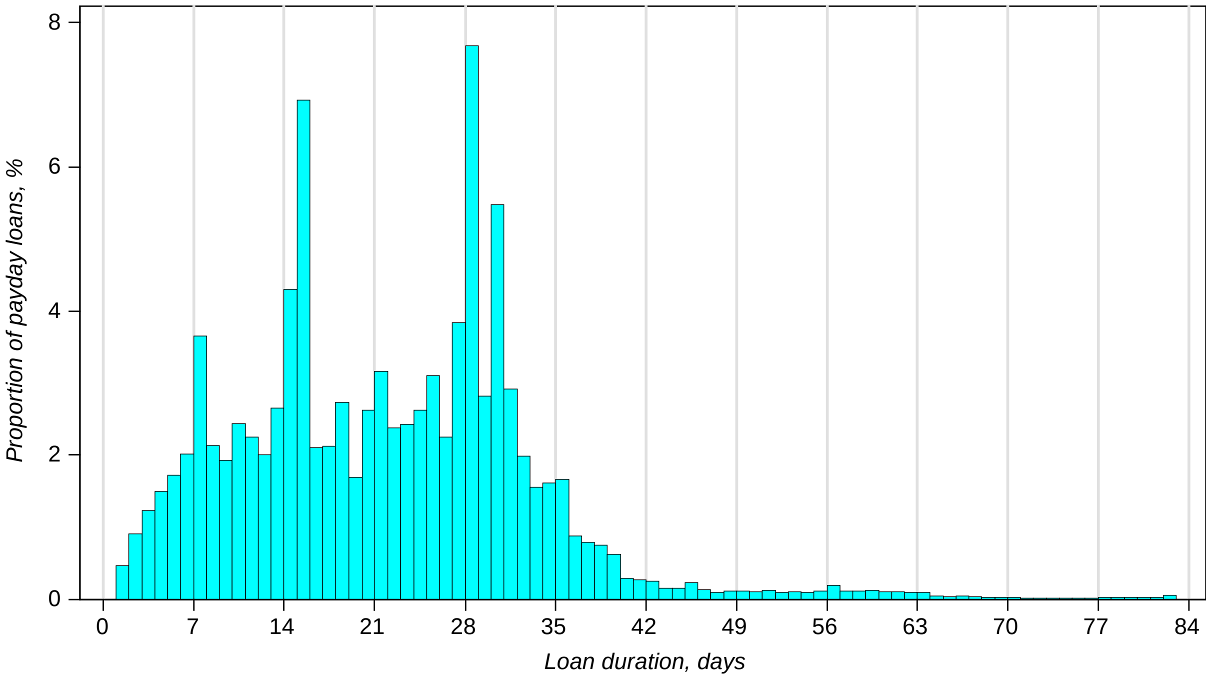
2.13 Payday loans are also typically issued for relatively short durations. Although some loans issued by the lenders from which we collected data were for a year or more, an overwhelming majority of loans in our data set were shorter term. In particular, over 80% of loans in our data set had durations of 31 days or less, and over 95% had a duration of 90 days or less.[20] Longer-term products generally allow customers to repay in several instalments, whereas shorter-term products are usually repaid in a single instalment.[21]

2.14 If we exclude longer-term instalment products[22] from our data set (accounting for around 4.5% of all loans), the average duration of a payday loan was 22 days. 10% of customers borrowed for a week or less, 90% for 34 days or less, and within this distribution we observe that loan durations of around a month (ie 28 to 31 days) and around a fortnight (ie 13 to 15 days) were particularly common. The average duration of a loan was slightly shorter online (21 days) than for high street customers (24 days).[23] Figure 2.2 shows the distribution of loan durations among the shorter-term products in our data set.

[20] For loans issued between September 2012 and August 2013.
[21] See paragraphs 2.52 & 2.53 on the use of rollovers in the recent past.
[22] Longer term instalment products refers to those products in our data set which are taken for periods longer than 30 days and are usually repaid in instalments.
[23] Customer and transaction level descriptive presentation, slide 27.

FIGURE 2.2

Distribution of loan durations



Source: CMA analysis of transaction data.
Note: Analysis covers the 12 months to 31 August 2013.

2.15 In contrast, instalment loans which some payday lenders offer are by their nature issued and repaid over a longer period. The duration of instalment loans varies by lender and product but typically last between two months and a year, though both longer and shorter loans may be payable in monthly or weekly instalments.

2.16 Payday loan products falling within the above definitions also vary in terms of the flexibility that they offer customers who want to borrow additional amounts. For example, some lenders allow customers to extend – or 'roll over' – an existing loan for an additional period if they pay off outstanding fees and interest. Historically different lenders have set different restrictions on how many times a loan can be extended: following new rules introduced by the FCA, no lender is able to roll over a loan more than twice. In addition to roll-overs, some products allow customers to borrow further amounts – or 'top up' – during the course of a loan (see Section 3 for changes in the regulation of rollovers).

Characteristics of payday loan customers

2.17 We next briefly outline some of the characteristics of the people who use payday loans. We first summarise some demographic characteristics before discussing customers' incomes and their experience of credit and debt problems.[24]

Demographics

2.18 In our survey of customers, we asked about their background. We found that customers were disproportionately likely to be male and that customers were younger than the UK population as a whole (71% of customers were aged 18 to 44 compared with 46% of the population). Customers are also more likely to be working full-time than the population as a whole, and to live in larger households (as a result of having children), but this reflects the fact that customers are predominantly of working age.

2.19 We discuss these characteristics in greater depth in Appendix 2.3.

Income

2.20 Both our survey and our analysis of lenders' transaction data suggested that the median income of an online payday loan customer was broadly similar to that of the wider UK population. High street borrowers typically had incomes below the UK average.

2.21 In our survey we found that 36% of all payday loan customers[25] had a net household income of less than £18,000, 37% of customers had a net household income of £18,000 to £36,000 and 28% of customers had a net household income of greater than £36,000. However, 21% of customers responded that they did not know what their household income was and are not included in these figures. 23% of customers stated that they had a variable income. The distribution of payday loan customers' incomes was somewhat narrower than that for the UK population – with fewer individuals with particularly low or particularly high incomes.

2.22 Table 2.1 shows the distribution of yearly net personal income for the UK population and payday loan customers based on our transaction data, analysed further by borrowing channel. Median net individual income for all payday loan customers (£15,600) was lower than the national median

[24] This subsection is based upon two principal sources of information, which we use throughout this final report. The first is the customer research that we commissioned from TNS BMRB, and which was carried out between September and December 2013. This research included a telephone survey of 1,560 payday loan customers, and 37 depth interviews carried out face to face with payday borrowers. The second source is the transaction data, discussed in paragraph 2.9 above and Appendix 2.2, which provides detail on each payday loan issued by the 11 major lenders in the period January 2012 to August 2013, and the customers to whom these loans were issued.
[25] That is, of the 72% who were able or willing to state their income.

(£17,100). However, the median net individual income of online customers (£16,500) was only slightly less than the national median whereas the median net income of high street customers (£13,400) was significantly less than the national median.[26]

TABLE 2.1 **Distribution of net annual income**

	Net annual income – percentile (£)				
	10th	*25th*	*Median*	*75th*	*90th*
UK*	8,800	11,700	17,100	26,300	39,000
All payday	9,200	12,000	15,600	21,600	28,800
Online	9,600	12,400	16,500	21,600	29,400
High street	7,000	10,200	13,400	17,900	23,200

Source: CMA analysis of transaction data (September 2012 to August 2013); HMRC, Survey of Personal Incomes (2010/11).

Extent of previous credit or financial problems

2.23 We investigated whether payday loan customers had experienced any previous credit or financial problems within the last five years. 38% of customers had experienced a bad credit rating, 35% had made arrangements with creditors to pay off arrears, 11% of customers had experienced a county court judgment and 10% had been visited by a bailiff or debt collector. In total, 52% of customers had experienced one or more of these debt problems in the last five years. Customers over 45 years old and owner-occupiers were the most likely to have experienced financial problems.[27]

2.24 Customers who had used both high street and online lenders were more likely to have been turned down for credit (44% compared with 29% for all customers) in the last 12 months. This group of customers were also slightly more likely to have had no alternative form of credit available to them at the time of taking out their most recent payday loan (43% compared with 39% of all customers).[28]

How customers use payday loans

2.25 We next consider how customers use payday loans. We look at the following aspects of customer behaviour:

[26] In the survey we similarly noted a significant difference between online and high street customers with respect to income. Whereas 60% of high street customers had a household income of less than £18,000 a year, only 28% of online borrowers fell into this category. 34% of online customers had a household income greater than £36,000 a year.
[27] TNS BMRB Survey Report, p30.
[28] ibid, p59.

(a) We look first at the circumstances in which customers take out payday loans, including the reasons given for taking out a loan and the timing of loan applications (paragraphs 2.26 to 2.32).

(b) In paragraphs 2.33 to 2.41, we consider evidence on customers' repayment behaviour, including the extent to which customers repay payday loans in full on time, repay late, or roll over the loan. We go on to note the implications for customers of defaulting on repayments.

(c) In paragraphs 2.42 to 2.54 we consider whether customers' use of payday loans may be characterised as a 'one-off' event and examine the extent of repeat borrowing and customers' use of multiple lenders.

Circumstances in which customers take out payday loans

2.26 We asked customers what they had used their most recent payday loan for. 53% of customers told us that they had used the money for living expenses (such as groceries and utility bills), 10% of customers said the money related to a car or vehicle expense and 7% said general shopping such as clothes or household items.[29]

2.27 59% of customers told us that the expenditure funded by their payday loan was for something that they could not have gone without. Had a payday loan not been available, 31% of all customers said they would have borrowed from friends or family and 29% would have gone without. Of those 59% of customers who told us they could not have gone without the expenditure incurred, 24% said that had payday loans not been available they would have gone without.[30] The qualitative research suggests that customers' mindsets at the time of taking out a loan tended to push their perception towards apparent need, exaggerating their need for a loan, but in retrospect, customers thought that the expenditure could have been forgone or delayed.[31,32]

2.28 When asked what the money was used for in an open question, only 2% told us that it was to pay off another payday loan, though 25% of all customers

[29] ibid, p68. Other less common types of expenditure (where 4% or less of those surveyed made reference to them) included holidays, paying off other loans (both payday and non-payday), rent and mortgage payments, presents and gifts, replacing broken household items and socialising.
[30] ibid, p72.
[31] ibid, p73.
[32] The qualitative research suggests an explanation that the apparent contradiction between the necessity of the expenditure the loan funded and the customer's likely action had credit not been available can be understood that a customers' initial claim that they could not go without could reflect a customer's mindset at the time of taking out the loan. The research suggested that customers may be justifying their need for a loan to themselves at the time of taking it out, and therefore repeat this rationalisation later when asked about their reasons for getting a loan. TNS BMRB Survey Report, p74.

(and 36% of those who had previously had a loan) had paid off a payday loan in the previous month.

2.29 We asked customers why they had needed to take out a payday loan. 52% said the loan was linked to an unexpected increase in expenses or outgoings and 19% said the need was due to an unexpected decrease in income.[33] 93% of those who said their need was due to a change in financial circumstances thought this change was temporary, whereas 5% expected the change to be permanent.[34]

2.30 We considered whether repeat borrowers used payday loans for different purposes than other customers who used payday loans only once. Our qualitative research suggested that once a customer had taken out their first loan, the reasons for taking out subsequent loans evolved over time, shifting from paying for necessities to satisfying more general wants and desires.[35] We also noted that customers who had used three or more lenders and those who had taken out both online and high street loans were more likely to have needed to repay a previous loan in the month before. We discuss repeat borrowing in greater depth in paragraphs 2.42 to 2.54.

When are loans taken out?

2.31 Our analysis of the transaction data for the 12 months to August 2013 found that the number of loans taken out on a Friday was around three times greater than the number of loans taken out on a Sunday, and around 50% more than for other days of the week. The distribution of loans by the day on which they were issued is shown in Figure 2.3.

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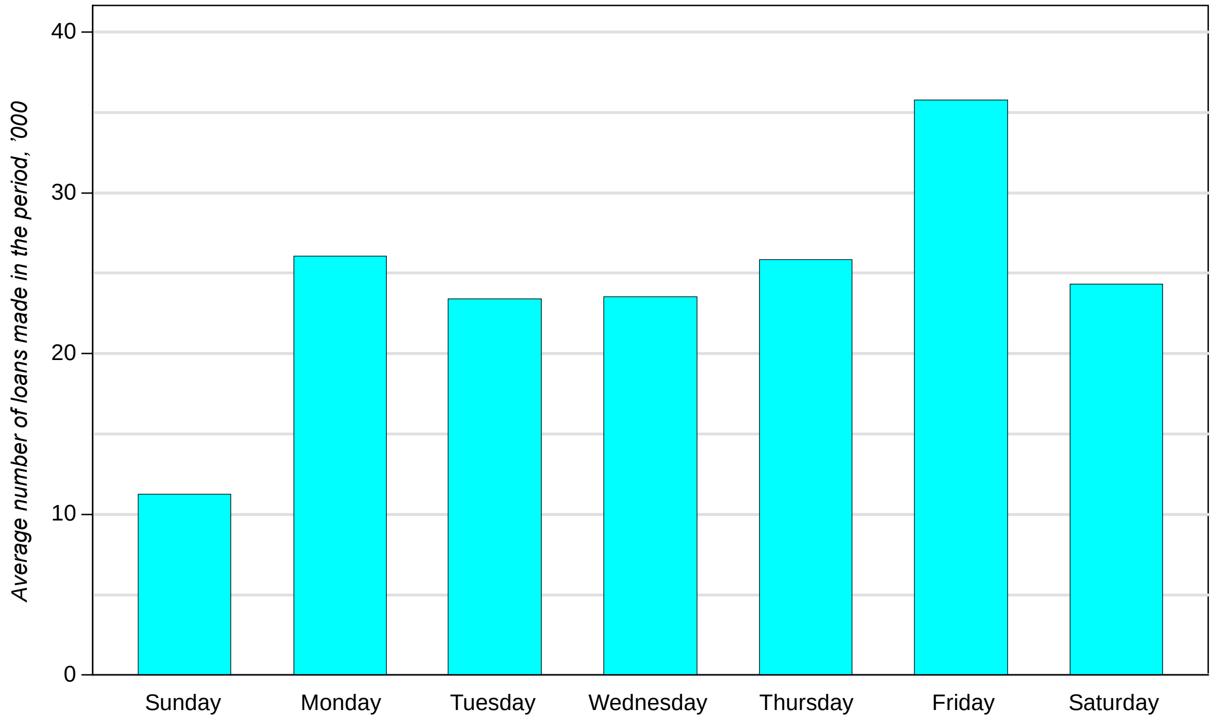
[33] ibid, p70. 31% said that their need was not linked to unexpected changes in income or expense.
[34] ibid, p70. The remaining 2% did not know.
[35] ibid, p75

FIGURE 2.3

Number of loans taken out by day of the week

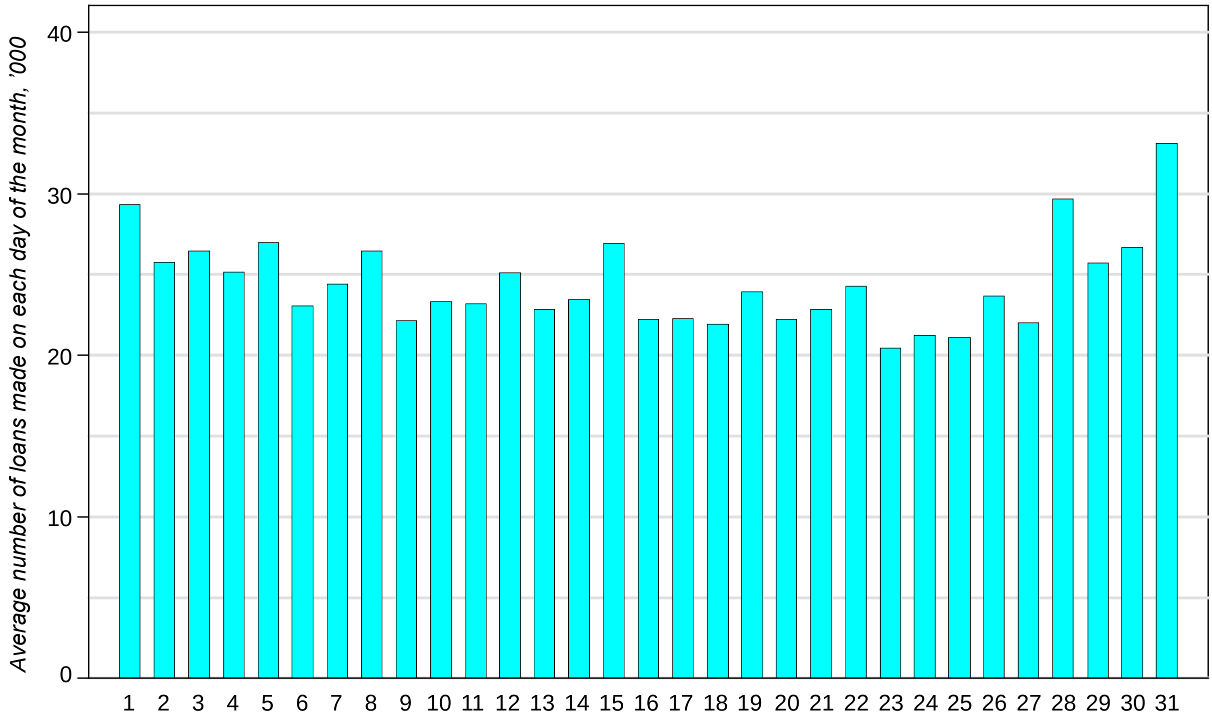


Source: CMA analysis of transaction data.
Note: Analysis covers the 12 months to 31 August 2013.

2.32 We also considered the distribution of loans by the day of the month, which is shown in Figure 2.4. Although slightly more loans were taken out at the beginning and end of a month, significant amounts of borrowing occur throughout the month.

FIGURE 2.4

Number of loans issued by day of the month



Source: CMA analysis of transaction data.
Note: Analysis covers the 12 months to 31 August 2013.

Repayment

2.33 Our analysis of the transaction data found that 64% of payday loans issued in calendar year 2012 were repaid in full either early or on time. 22% of loans were repaid in full late (ie after the originally agreed repayment date) – often as a result of having been rolled over. 14% of these loans had not been repaid in full as at October 2013.[36]

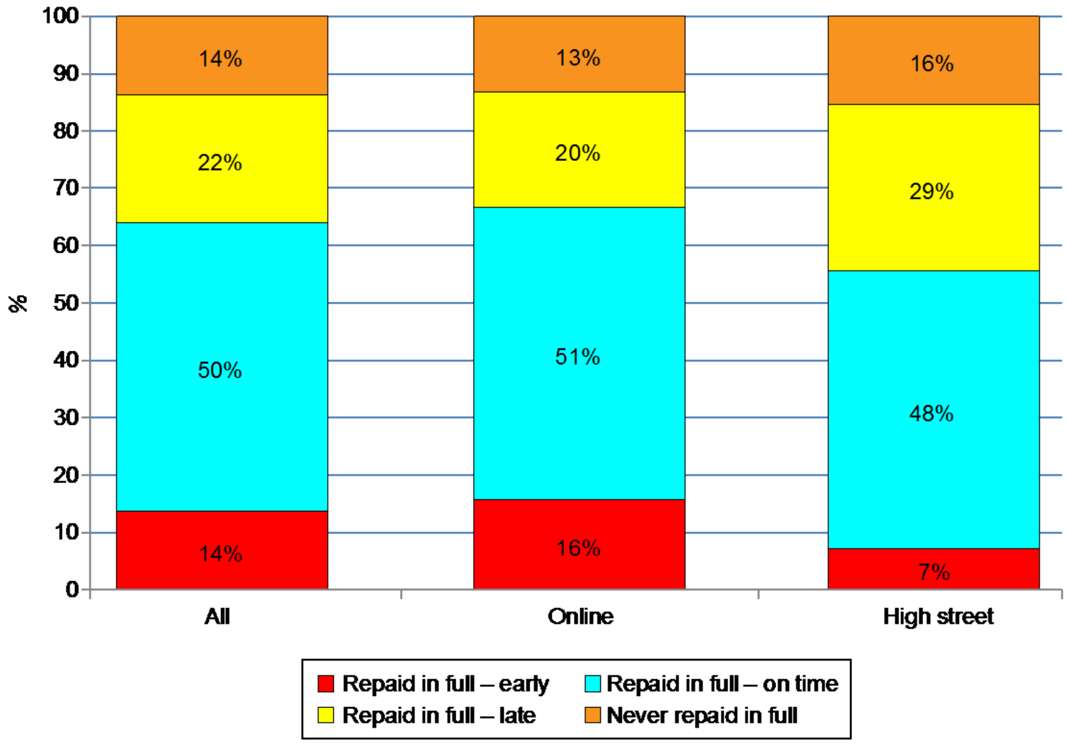
2.34 Figure 2.5 shows that 55% of high street loans were repaid in full on time compared with 67% for online loans.[37] Figure 2.6 shows that repayment rates also varied significantly by lender, with the proportion of loans being paid in full either early or on time varying from around 20% ([✂]) to 80% ([✂]).[38] 67% of repeat loans (loans taken by customers who have previously taken a loan with the same lender) were repaid in full either early or on time, which compared to 50% of new loans.[39]

[36] This will include loans where customers had either defaulted or rolled over.
[37] Customer and transaction level descriptive presentation, slide 31.
[38] ibid, slide 32.
[39] ibid, slide 33.

FIGURE 2.5

Repayment status of loans

All loans issued in 2012, status as of 1/10/2013

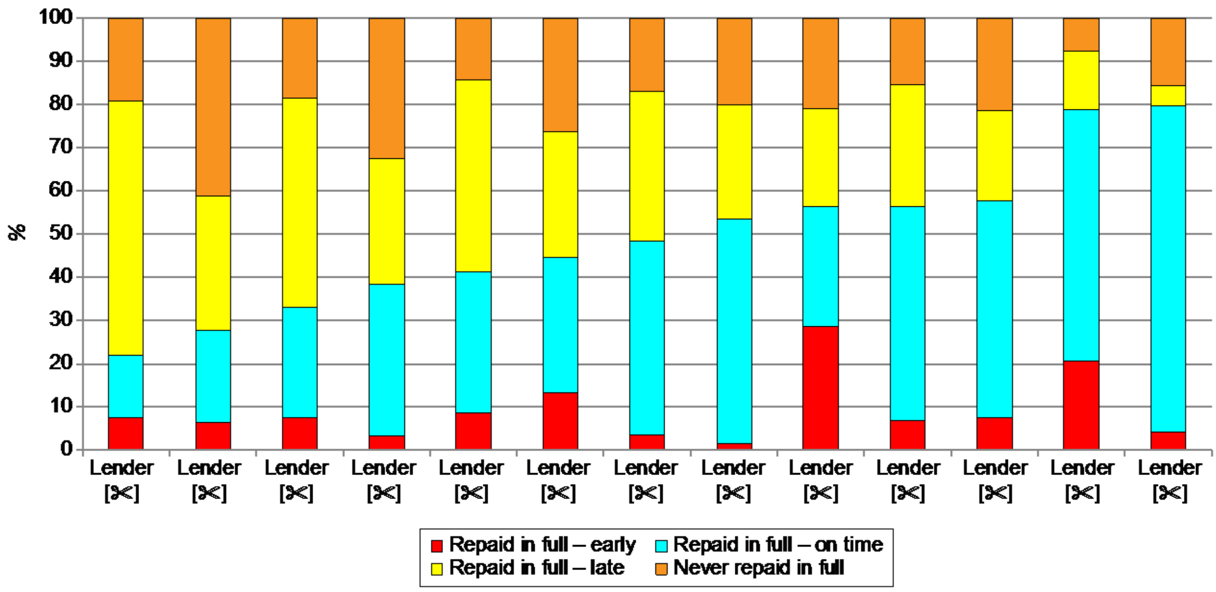


Source: CMA analysis of transaction data.

FIGURE 2.6

Repayment status by lender

Loans issued in 2012, repayment status as of 1/10/2013



Source: CMA analysis of transaction data.

2.35 Our survey found that the following groups of customers were less likely to have repaid their loan in full on or before the scheduled repayment date:

(a) customers who felt themselves not to have a good understanding of financial conditions and terms;

(b) customers with past financial problems (including having previously been refused for payday loans); and

(c) customers who had used a greater number of payday lenders.[40]

Expectation and ability to repay

2.36 When asked how confident they were when taking out the loan that they would be able to repay it by the agreed date, 80% of customers responding to our survey reported having been very confident and 15% having been fairly confident.[41]

2.37 Just over half (52%[42]) of the 18%[43] of customers who had failed to repay their loan on time stated that the total repayment amount had been more than they had expected, which contrasted with 13% of those customers who had repaid their loan in full and on time. This may suggest that either the customers most likely not to repay their loan were those customers who were not able to calculate, or misunderstood the repayment amount, or alternatively that those customers which had not repaid in full had not anticipated additional late charges (for example, as a result of not anticipating being unable to repay the loan in full on time).[44]

2.38 17% of customers reported having found getting money to repay their loan to be more difficult than expected. Certain groups of customers were more likely to find getting the money more difficult than they expected, including customers: (i) who had previously taken out payday loans in order to pay off debts to other payday lenders; (ii) with a poor understanding of financial terms and conditions; (iii) who had been refused loans previously; (iv) who had experienced debt problems in the last five years and (v) who said they took out a payday loan as a last resort.[45]

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[40] TNS BMRB Survey Report, p117.
[41] ibid, p95.
[42] ibid, p120.
[43] ibid, p117.
[44] ibid, p120.
[45] ibid, p121.

Defaulting on payments

2.39 In the payday lending sector, the implications of late payment vary from lender to lender. Typically a customer could be charged a late payment fee and would accrue interest on the outstanding balance.[46] Prior to the introduction of restrictions on the use of CPAs a lender would make further attempts to collect money owed from the customer in either one payment or in several part payments.[47]

2.40 Information in relation to failed payments may affect the customer's ability to obtain credit in the future as a result of lenders informing CRAs of the default. The Consumer Credit Act 1974 (CCA), as amended by the Consumer Credit Act 2006, sets out additional requirements in relation to default:

(a) A creditor must give the borrower a notice of sums in arrears, plus an arrears information sheet at intervals of six months until the borrower is no longer in arrears, or until a judgement is made regarding the amount owed.

(b) A creditor cannot enforce an agreement during the time it fails to comply with this requirement and the borrower would not be liable to pay interest during this time.

2.41 Under the Consumer Credit Act sections 87 and 88, as amended by the Consumer Credit Act 2006 section 14, it is necessary for the lender to serve a Default Notice and give the customer 14 days to remedy the breach of the agreement specified in it. This applies to all notices served after this date, regardless of when the agreement was made or the default occurred. The lender must set out what action it intends to take if the borrower fails to make the payment.

Repeat borrowing

2.42 Our analysis suggests that customers' demand for payday loans is typically recurring, and that a large proportion of customers return to the same lender for further credit after taking out their first loan. We consider first repeated borrowing with the same lender before considering borrowing across multiple lenders.

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[46] See Appendix 4.1, Tables 3 & 4, for details of additional charges.
[47] Lenders are now restricted from taking part payment by CPA but may make arrangements with borrowers to reschedule payments. CONC 7.6.14 R.

Repeat borrowing with a single lender

2.43 Looking at repeat borrowing from a single lender, our analysis suggests that more than 80% of all loans (excluding rollovers) issued by the 11 major lenders in 2012 were to customers who had previously borrowed from them. Considering a customer taking out a loan with a lender for the first time in the first 8 months of 2012:[48]

(a) 60% took out at least one further loan from the same lender during the subsequent year;

(b) 21% took out more than five additional loans from the same lender during the subsequent year; and

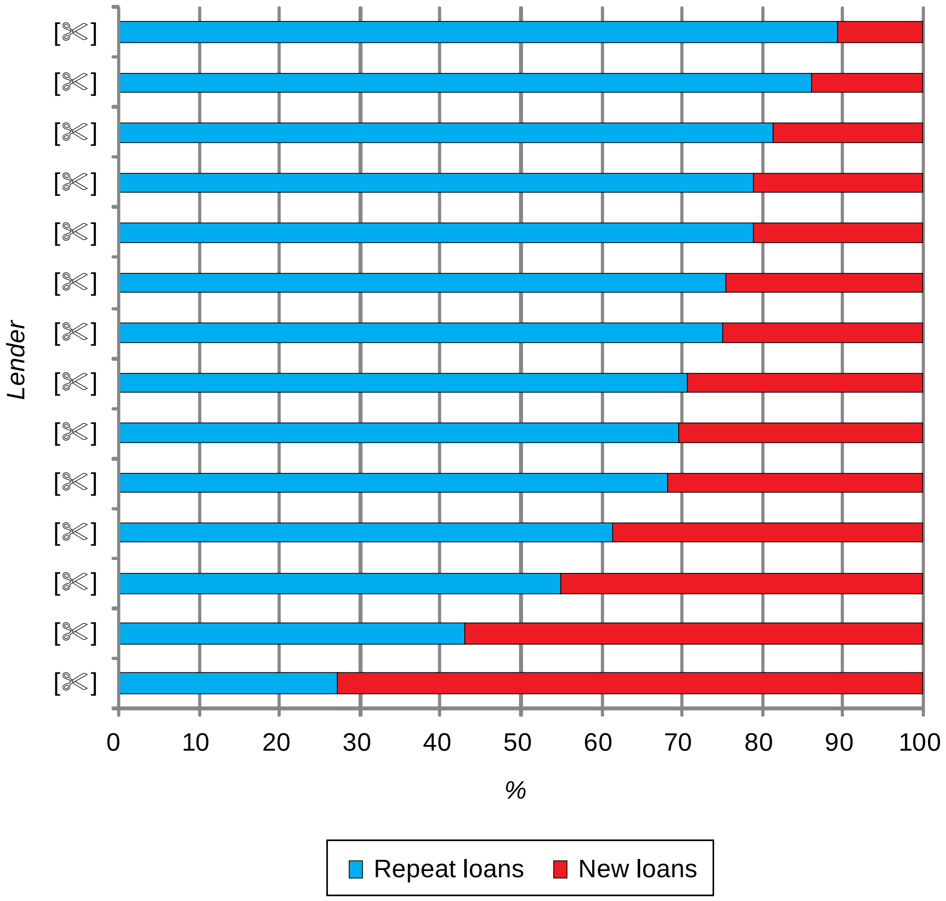
(c) the average number of additional loans that a customer went on to take out from the same lender within a year of the first was 3.6.

2.44 Furthermore, we found that around 40%[49] of customers of the 11 major lenders had a borrowing relationship with that lender of more than one year.[50] The extent to which customers return to a lender for further loans varies considerably across lenders. Figure 2.7 shows the proportion of each of the 11 major lender's loans in 2012 which were to repeat customers. This proportion ranged between 27% ([✂]) and 89% ([✂]). Notwithstanding this variation, it is worth noting that for most lenders more than half of all loans were to repeat customers – and for many lenders the proportion was much greater than this.

[48] See 'Repeat customers—presentation based on analysis of the transaction data' for further details.
[49] As of August 2013.
[50] We discuss this in more detail in Section 7.

FIGURE 2.7

New customers vs repeat customers – number of loans (2012)



Source: CMA's analysis on lenders' transaction data.

2.45 Some of the repeat borrowing that we observed in the payday market took the form of 'top-ups' (where lenders[51] offered customers the ability to borrow additional amounts by topping up an outstanding loan to a predefined credit limit – see Appendix 2.1 for further details). For example, looking at [✂]% of [✂] loans and [✂]% of [✂] loans were topped up in the period September 2012 to August 2013. Together these loans accounted for [✂]% of all loans issued by the 11 major lenders.[52]

Borrowing across multiple lenders

2.46 Many payday loan customers borrowed from more than one lender, suggesting that the extent of repeat borrowing among payday loan customers

[51] Facilities of this type were offered by Wonga, CashEuroNet (Pounds to Pocket and QuikQuid Flexicredit), Dollar (Payday Express and Instant Cash Loans), SRC, The Cash Store, Pay Day Loans and KwikLoan (H&T) and SRC (SpeedyCash Flex Loan).
[52] On average, each such loan was topped up [✂] times.

is greater than indicated by our analysis of an individual lender's transaction data.

2.47 To estimate the extent to which customers borrowed from multiple lenders, we selected a sample of over three thousand loans at random from the transaction database (see Appendix 6.2 for further details of this sample). Each customer identified within our sample was matched across lenders using a combination of their surname, postcode and date of birth. Information on the loans issued to these customers by smaller lenders was then added by matching in data provided by a number of CRAs.

2.48 A reweighting exercise was then carried out so that the sample was representative of payday loan customers in 2012.[53] Using this reweighted sample, we estimated that 76% of payday loan customers took out more than one loan in 2012 either with the same lender or with different lenders. 41% took out 2 to 5 loans, 20% took out 6 to 10 loans and 15% took out more than 10 loans. On average, a payday loan customer took out 5.7 loans in 2012.

2.49 Around four in ten customers (38%) in the sample borrowed from at least two different lenders during the year. 27% of customers borrowed from two or three lenders and 11% borrowed from more than three lenders. On average, a customer borrowed from 1.9 lenders.

2.50 These findings are broadly consistent with the results of our customer survey (as well as the submissions of various lenders[54]) which found that 45% of all customers interviewed had used more than one lender; 79% had taken out more than one loan and around a third had taken out more than five loans.[55]

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[53] Reweighting was required because the sample was constructed by selecting loans issued in 2012 at random, rather than customers, and so borrowers taking out relatively few loans in the period would otherwise have been relatively unrepresented. Each customer was assigned a weight according to their probability of being included within the original sample. These weights were generated using the ratio of the total number of customers who took out a given number of loans in the population, divided by the number of such customers in the sample. So, for example, if customers taking out one loan in the period made up 5% of the population but 1% of the sample, then these individuals would receive a weight of 5. Note that the weights applied differ to those underpinning the analysis reported in the presentation on *Customers' use of multiple lenders*, publish 9 April 2014, explaining the difference in the estimates presented in that paper and those reported here.
[54] For example, Wonga told us that [✂] of its inactive customers were using other payday lenders (see Wonga's response to the annotated issues statement, paragraph 1.16). CashEuroNet submitted the results of a survey (conducted on [✂]) which asked respondents about the lender that customers had used before taking out their loan with QuickQuid. [✂]% of respondents reported having used another payday lender, higher than the proportion of customers who reported having previously taken out a loan from QuickQuid itself. Dollar submitted that the evidence resulting from the analysis of transaction data and customer survey suggested high rates of churn (See Dollar's response to the annotated issues statement, paragraph 7.13).
[55] Broadly similar results were also found when, instead of sampling, we simply matched all loans in the transaction database on the basis of the customer's surname, date of birth and postcode. Although a lower proportion of customers were found to have used more than one lender (30%) and on average customers were estimated to have taken out fewer loans (5.2) using this approach, this would be expected given that the transaction data does not include any loans issued by smaller lenders.

2.51 Our survey also suggested that there may be some relationship between a customer's financial behaviour and the extent to which they take out more than one loan and/or use multiple lenders (see Figure 2.8 below):

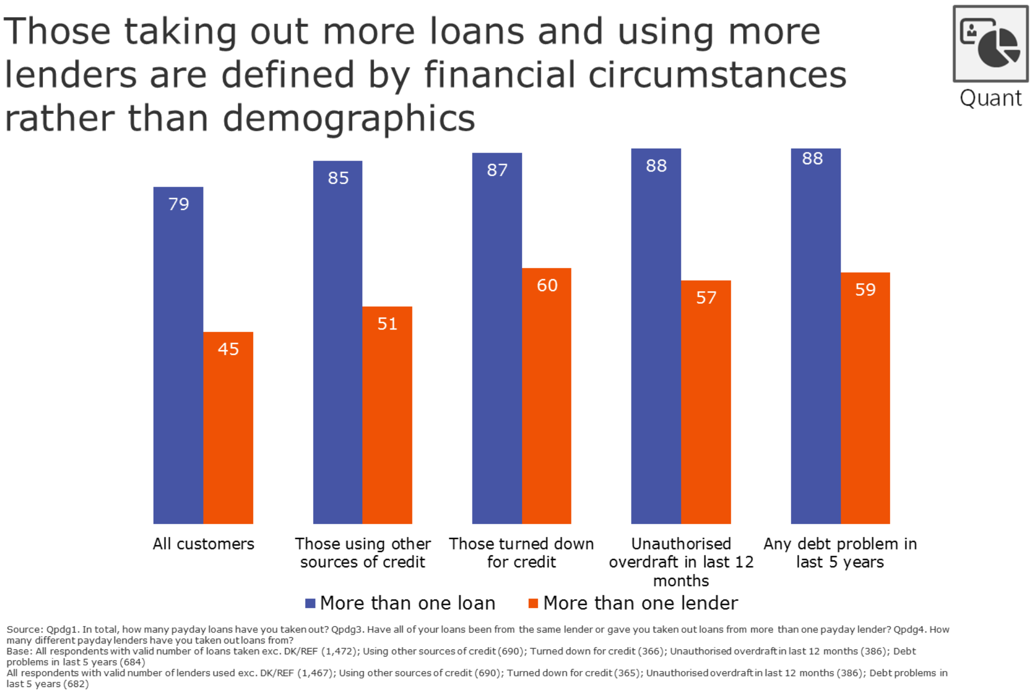
(a) 85% of payday loan customers who had used sources of credit other than payday loans in the last 12 months had taken out more than one loan compared with 73% of customers who had not used other sources of credit in this period.

(b) Customers who experienced credit or debt problems[56] were more likely than average to have had more than one payday loan and were also more likely than average to have used more than one payday lender.

(c) Customers with an unauthorised overdraft, who had been turned down for credit in the last year, or who had a debt problem in the last five years, had used an average (median) of two payday lenders whereas the average (median) number of lenders used across all customers was one.

FIGURE 2.8

Customers' financial behaviour and use of multiple lenders – CMA customer survey



Source: CMA customer survey.

[56] Customers who had been turned down for credit, who had an unauthorised overdraft in the last 12 months, and / or who had a debt problem in the last five years.

Rollovers

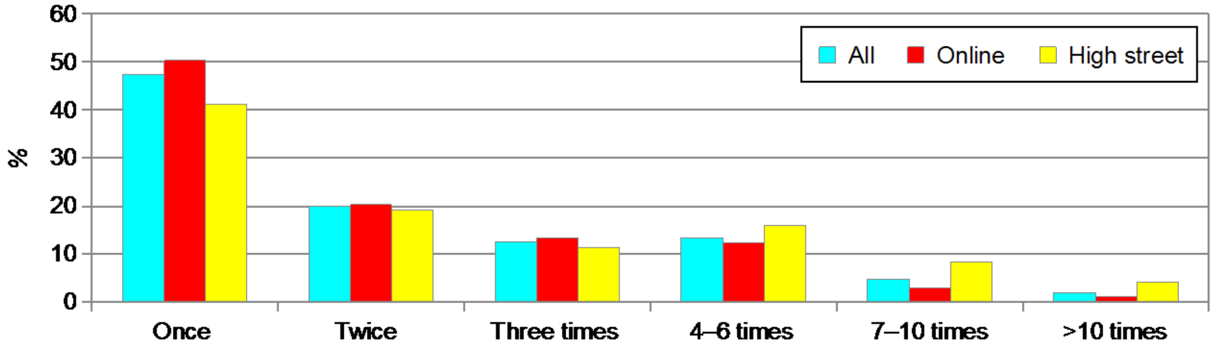
2.52 In addition to taking out new loans, many borrowers extend the duration of their credit from their current lender by rolling over an existing loan (see paragraph 2.16).[57] Our analysis of the transaction data found that in 2012, around 20% of the loans taken from the 11 major lenders were subsequently rolled over – with 16% of online loans and 26% of high street loans rolled over.[58]

2.53 Figure 2.9 shows that of those loans that were rolled over, about 50% of online loans were rolled over more than once, compared with around 60% of high street loans.[59] On average, loans which were rolled over were rolled over 2.5 times. Rules introduced by the FCA in April 2014 now limit the number of rollovers to two.[60]

FIGURE 2.9

Distribution of the number of times a loan is rolled over

Number of times loans have been rolled over (% of all loans that have been rolled over)



Source: CMA analysis of transaction data.
Note: Analysis covers the period January 2012 to December 2012.

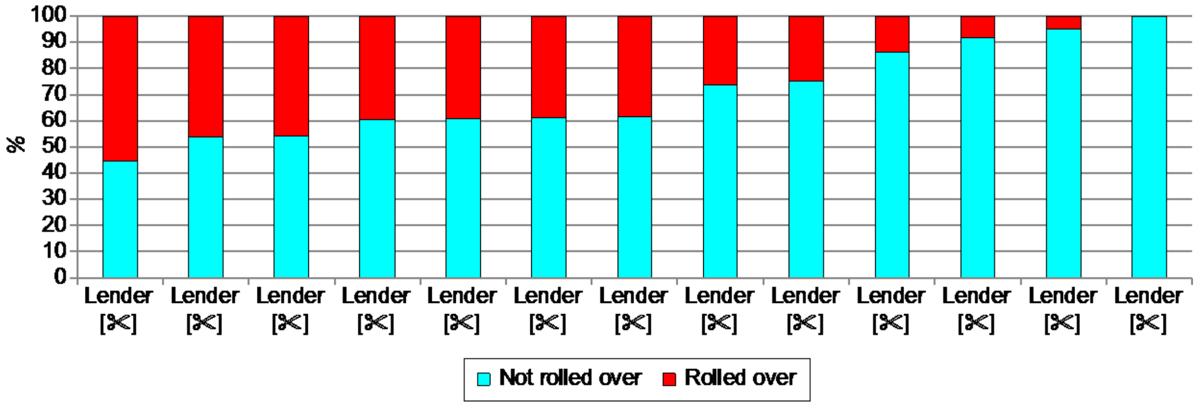
2.54 Again, the extent to which customers rolled over their loans varied significantly across lenders. Figure 2.10 shows the proportion of loans that had been rolled over by lender. The proportion of loans rolled over varied from 0 to 55%.

[57] Some lenders charge a fee for rolling over a loan; however, interest rates remain the same as during the original term of the loan.
[58] Customer and transaction level descriptive presentation, slide 42.
[59] ibid, slide 44.
[60] CONC 6.7.23 R.

FIGURE 2.10

Proportion of loans rolled over by lender

Proportion of loans issued in 2012 that have/have not been rolled over



Source: CMA analysis of transaction data.
Note: Analysis covers the period January 2012 to December 2012.

2.55 We considered the significance of rollovers to payday lenders’ revenue. To do this, we took all loans issued by the 11 major lenders in 2012, estimated the total value of fees and interest charged on those loans (with certain exceptions due to data limitations – see footnote), and calculated the proportion of these charges that was accounted for by rollover fees and interest.[61] We estimated that this proportion was 32% for online lenders, and 40% for high street lenders.

2.56 One limitation of this approach is that it reflects revenues contracted for, rather than revenues received by a lender, and so does not take into account differences in the extent to which customers that rollover their loan actually repay the amount owed. To allow for this, we adjusted the estimates to take into account the difference between the proportion of rolled-over loans which were never repaid in full compared with the proportion of loans that were not rolled over which were never repaid in full. This resulted in slightly lower estimates of the importance of rollover fees and interest: 29% for online lenders and 36% for high street lenders.[62]

[61] This estimate excluded late fees and interest, top-up charges and some discounts (eg for early repayment), because complete and consistent information on these charges/discounts were not available in our data set.
[62] These estimates were derived by deflating the proportion of charges accounted for by rollovers using the difference in the proportion of loans which were rolled over which were never repaid in full, and the proportion of loans which were not rolled over which were never repaid in full.

High street and online distribution channels

2.57 Payday loans can be taken out either from an online lender or on the high street. Payday loans issued online are taken out by customers visiting a lender's website[63] having accessed the site directly or through an internet search, or through intermediaries such as lead-generators or other advertisers: each of these routes is considered in paragraphs 2.129 to 2.164 below. Customers applying online then complete an application form, though the process may differ if the customer is directed to a lender through an intermediary. High street customers visit retail premises where a member of staff may lead the customer through the application process and customers may be required to provide documentary evidence of income and identity. The nature of the loans issued by the two channels do not differ, but the ways in which lenders attract customers and process customer applications do. These are discussed in greater detail in the following section.

2.58 Most payday loan customers borrow online. Our survey found that 83% of payday loan customers have taken out a loan online and 29% of customers have taken out a payday loan on the high street.[64] There is some overlap, with 12%[65] of customers having used both channels. Of those individuals who have used both channels, a clear majority (78%) mainly use online loans. [66] The average amount borrowed on the high street (£180) was lower than that borrowed online (£290).[67]

2.59 Our survey found that 78% of customers used online lenders either exclusively or as their main payday loan provider. We found that a higher proportion of men,[68] younger customers, those in full-time work, those educated to degree level or above, and those on middle or higher incomes were likely to have used online lenders as their main or only payday loan provider.[69] The extent of these groups' use of online lenders is shown in Table 2.2.

[63] Either using a PC, tablet or a smartphone.
[64] TNS BMRB Survey Report, p41.
[65] 71% of customers only used online and 17% only used high street.
[66] TNS BMRB Survey Report, p42.
[67] Customer and transaction level descriptive presentation, slide 21.
[68] This difference was relatively small, and our analysis of lenders' transaction data did not find a difference in the gender balance of high street and online customers (weighted by the number of loans) – see customer and transaction level descriptive presentation, slide 8. Gender information is missing from the transaction data for around one-third of all records.
[69] TNS BMRB Survey Report, p48.

TABLE 2.2 **Customer groups more likely to use online lenders**

Customer group	*% of that group using online lenders*
All customers	78
Gender	
Men	82
Age:	
18–24	88
25–34	86
Employment status	
Full-time worker	84
Level of education	
Higher	84
Income	
Middle	83
Higher income	90

Source: TNS BMRB Survey Report, p48.

2.60 Customer groups which were significantly more likely to have used high street lenders exclusively or as their main payday loan provider included: women; older customers; social renters; those in part-time work or unemployed; lone parents; those with no academic qualifications; and those on low incomes. The extent of these groups' use of high street lenders is shown in Table 2.3.

TABLE 2.3 **Customer groups more likely to use high street lenders**

Customer group	*% of that group using high street lenders*
All customers	20
Gender	
Women	23
Age	
45+	26
Housing tenure	
Social Renters	29
Employment status	
Part time worker	26
Unemployed	29
Household composition	
Lone parents	24
Level of education	
No qualifications	37
Income	
Low	31
Access to banking facilities	
No bank account	30

Source: TNS BMRB Survey Report, p49.

2.61 As set out in paragraph 2.22, high street customers generally had lower incomes than online customers or the population as a whole. Our analysis of lenders' transaction data found that the median net individual income of a high street borrower was £13,400, some £3,100 lower than for online borrowers (£16,500).[70]

[70] Customer and transaction level descriptive presentation, slide 10.

2.62 Coding of respondents' residential postcodes using the ACORN classification system indicated that high street customers are more likely than online customers to come from areas classed as 'urban adversity' or 'financially stretched'.[71]

2.63 More detailed comparisons of the characteristics of users of different channels are included in the Survey Report and in the underlying tables.[72] We discuss customers' perceptions of different distribution channels in Section 5.

The process of applying for and taking out a payday loan

2.64 In Appendix 2.4, we describe the loan application and approval processes of online and high street lenders.

2.65 The nature of the application process is necessarily different for online and high street lenders, although both collect similar types of information during the application process. There is also some variation in the approach taken by different lenders within each distribution channel. For example, some online lenders (such as Wonga) operate an almost exclusively automated process for verifying customer details and assessing customers' creditworthiness, whereas others (such as WageDay) will use a combination of automated and manual techniques.

2.66 Generally lenders collect the following information from an applicant:

(a) the amount of the loan requested;

(b) personal details, including name, address, residential status, date of birth, email address and telephone number;

(c) income details, such as employment type, net monthly pay, pay frequency, pay date, employment sector and time at current job;

(d) personal expenditure details (discussed further in paragraph 2.68);

(e) bank details, ie account name, sort code, account number; and

(f) debit card details, including card type, card number, expiry date and security code.

[71] In addition, the use of high street lenders is particularly prevalent in London, which accounts for 24% of customers of high street lenders, as compared with 14% on online customers. Source: TNS BMRB Survey Report, p57.
[72] www.gov.uk/cma-cases/payday-lending-market-investigation#cc-commissioned-research.

2.67 For verification purposes, high street lenders usually require sight of a customer's ID and proof of address while online lenders require a customer's mobile phone number.

2.68 We found that there was generally greater diversity in the nature and quantity of information required about a customer's expenditure (including credit commitments and existing debt balances) than in the other types of information requested. Some lenders do not require applicants to provide any information on expenditure or existing commitments.

2.69 The minimum eligibility criteria applied by all lenders are that a customer must be a UK resident and over 18 years of age. Individual lenders specify different additional requirements. An assessment of eligibility is included in the application process.

2.70 Having collected information from an applicant and established their eligibility, lenders will consider the individual's creditworthiness and their likelihood of successfully repaying the loan. To perform credit risk assessments, lenders typically analyse information collected during the loan application process, any information held about the applicant internally (eg their repayment history if they are a returning customer), and relevant third party information sources (eg information purchased from CRAs). Most lenders have developed their own automated risk models, of varying degrees of sophistication, to help them make decisions about the creditworthiness of potential applicants, developed using historical customer information. These models may support, or in some cases largely replace, manual assessments of a customer's creditworthiness.

2.71 For online customers an application form generally takes 5 to 10 minutes to complete. Once submitted, the lender verifies customer details and completes affordability and risk assessments. The time taken to do this may be determined partly by the extent to which manual checks are also required (eg confirming the customer's employment details). The customer will then either be approved or declined.

2.72 Once a customer's application has been approved, the funds will be transferred to the customer's bank account. In most cases this takes place on the same day, often in a couple of hours, though some lenders offer a basic service using a BACS transfer which may take up to two to three days (typically these lenders also offer a same-day transfer, for which they charge an additional fee).

2.73 We discuss the loan application and approval process in greater depth in Appendix 2.4.

Market size and structure

2.74 We collected information about the size and structure of the payday loan market by issuing detailed questionnaires to 11 major payday lenders and a further shorter questionnaire to 213 parties which had been identified as possible payday lenders.[73] Further details of this exercise and our analysis are set out in Appendix 2.5. Based on this analysis, we estimated that there were at least 90 payday lenders offering loans to UK customers as of October 2013.[74] We are aware that since then a number of lenders have either temporarily or permanently ceased issuing payday loans.[75] Four[76] of the 11 major lenders have either exited the market or announced a decision to exit the market (see paragraphs 2.81 to 2.124 for details of individual lenders). The trade associations have also provided evidence that a number of lenders terminated their membership and either exited the market over the course of 2014 or ceased issuing loans until the FCA price cap proposals were known. Data provided by the trade associations indicated that in the region of at least 50 lenders had exited the market since late 2013.[77]

2.75 We discuss current and future market developments at paragraphs 4.161 to 4.175 including the expected impact of the FCA's price cap.

Size of the market

2.76 As shown in Table 2.4, during the 2012 financial year, total payday loan revenue was around £1.1 billion, with lenders issuing approximately 10.2 million payday loans (excluding rollovers), worth £2.8 billion.[78] Online lenders issued £2.3 billion of loans, which was around 81% of all loans by

[73] The list was drawn up from a range of sources including: companies in a list of lenders compiled by the OFT, members of the BCCA, Consumer Credit Trade Association (CCTA) and the Consumer Finance Association (CFA) trade associations, a desktop review; and lists of competitors provided by lenders in response to our initial letter.
[74] This figure may underestimate the total number of lenders to the extent that not all lenders responded to our questionnaire, or we were unable to identify all relevant potential lenders. However, we would expect any lenders that were missing from this list to be limited to firms with very small-scale lending activities, such that their omission would not materially affect our assessment of the market size or structure.
[75] Although, on the basis of a review of their websites, as at November 2014 at least half of these 90 lenders appeared to still be operating in the payday loan market.
[76] Namely Ariste, CFO Lending, Cheque Centres and The Cash Store.
[77] The CFA told us that since late 2013 three of its members had left the payday loan market, with one new entrant. BCCA told us that [✂] online lenders and [✂] high street lenders ([✂]) had terminated membership, which was an indication that they had left the market (although it was not able to be precise in the number of members that previously issued payday loans). Almost all of those lenders terminating BCCA membership did so in the first quarter of 2014. The CCTA reported that 25 members classified as payday lenders had terminated membership.
[78] The figures for revenue, volume and value may not always correspond because not all lenders could provide full information on all these metrics.

value, with high street lenders issuing the remaining £0.5 billion of loans.[79] We estimate that there were around 1.8 million payday loan customers in 2012.[80]

TABLE 2.4 **Total revenue, value and number of payday loans issued, financial years* 2011 and 2012**

Totals	*2011*	*2012*	*Growth %*
Number of loans (million)	7.4	10.2	37
Value of loans advanced (£m)	1,926	2,810	46
Revenue earned (£m)	755	1,091	44

Source: CMA analysis.

*See Appendix 2.5 for a description of how different lenders' financial years have been treated. For each lender in each financial year, payday loan revenue refers to the total income generated by each lender's payday lending operations, payday loan volume refers to the number of new loans issued by each lender and payday loan value refers to the total loan amount issued by each lender.

2.77 The revenue and lending figures for 2012 represented a 35 to 50% increase on the preceding financial year (depending on the way in which the size of the market is measured).

2.78 More recent financial data indicates that the rate of market growth has reduced substantially. Our analysis indicates that in 2013 revenue growth for the 11 major lenders was around 5%. Data for the first nine months of 2014 showed that revenue and new lending for the seven[81] major lenders for which we have data was down year on year by 27% and 26% respectively.

Shares of supply

2.79 Table 2.5 reports estimated total payday revenue and shares of supply for the ten largest payday lenders in 2012. Wonga—the largest payday lender—had a [20–30]% share of total payday revenue, a [30–40]% share of all loans (excluding rollovers) by volume and a [40–50]% share of all loans (excluding rollovers) by value.[82] The three largest lenders by revenue had a share of just under 70% of total payday revenue, over 65% of payday loans issued and over 75% of loan value; the ten largest lenders by payday revenue accounted for more than 90% of total payday revenue, 85% of loans issued and just under 95% of loan value.

[79] Online lenders also accounted for similar proportions (70 to 80%) of total loan revenue and volume of payday loans. These proportions did not change significantly relative to the previous financial year though there has been a longer-term trend towards online lending.
[80] We derived this estimate by dividing the total number of loans issued in 2012 in Table 2.4 (10.2 million) by our estimate of the average number of loans held by a payday loan customer in a 12-month period as set out in paragraph 2.48.
[81] Ariste, CashEuroNet, Dollar, Global Analytics, MYJAR, SRC (including Speedy Cash and WageDayAdvance) and Wonga. Data from H&T was not available. Three major lenders had exited the market (CFO Lending, Cheque Centres and The Cash Store).
[82] Wonga's share of revenue relative to its share of the value and volume of loans issued appears to be driven by the payment behaviour of its customers. The possible causes for disparities in shares of revenue, value and volume are discussed further in paragraph 2.80.

2.80 We note that the different characteristics of lenders' products may drive differences between a lender's share of revenue, value and volume. For example, all else equal, a lender offering an instalment product might be expected to issue higher-value loans on average compared with a lender offering a 30-day fixed term product – and hence have a higher share of total loan value and revenue, relative to the total number of loans issued – because of the longer repayment period.

TABLE 2.5 **Shares of supply of the ten largest lenders, financial year* 2012**

%

Lender	*Share of 2012 total loan revenue*	*Share of 2012 total loan value (excl rollovers)*	*Share of 2012 total loans issued (excl rollovers)*
CashEuroNet†	[10–20]	[10–20]	[5–10]
CFO Lending Limited (CFO Lending)	[0–5]	[0–5]	[0–5]
Cheque Centres Group Limited‡	[0–5]	[5–10]	[5–10]
Dollar	[20–30]	[10–20]	[20–30]
Global Analytics	[0–5]	[0–5]	[0–5]
MYJAR	[0–5]	[0–5]	[0–5]
Oakam	[0–5]	[0–5]	[0–5]
PDL Finance	[0–5]	[0–5]	[0–5]
SRC	[0–5]	[0–5]	[0–5]
Wonga§	[20–30]	[40–50]	[30–40]
Other lenders	[5–10]	[5–10]	[10–20]
Total	100.00	100.00	100.00

Source: CMA analysis.

*See Appendix 2.5 for a description of how different lenders' financial years have been treated.
†Pounds to Pocket instalment loans are included in CashEuroNet's total figures.
‡Cheque Centres instalment loans are included in Cheque Centres total figures.
§Wonga has undergone a corporate restructuring which may affect the extent to which its year-on-year figures are comparable with other lenders.

Payday loan providers

2.81 All payday loan providers seek to attract potential customers and issue loans. However, in addition to the choice of whether to issue loans online or on the high street, the methods that lenders use to attract customers (which are described below in paragraphs 2.118 to 2.164 in other market participants), and the profile of those customers may vary across lenders. We discuss price and non-price competition and profitability of lenders in Section 4. Further, each lender will experience different levels of default (see Section 7), rollovers (paragraphs 2.52 to 2.54) and repeat borrowing (paragraphs 2.42 to 2.45).

2.82 In this subsection, we set out information on 14 payday loan providers arranged broadly by size into three groups:

(a) First, we set out detailed descriptions of the top three payday lenders:

(i) CashEuroNet UK, LLC (CashEuroNet);

(ii) DFC Global Corporation (DFC), trading in the UK as Dollar; and

(iii) Wonga (WDFC UK Ltd, formerly Wonga.com Limited).

(b) Secondly, we describe eight other payday lenders to which we sent detailed market and financial questionnaires. These companies offered a range of single repayment and instalment loans which as at October 2013 fell within our definition of a payday loan and included the largest online and high street brands outside the top three companies referred to above:

(i) Ariste Holding Limited (Ariste);

(ii) The Cash Store (UK) (The Cash Store);

(iii) CFO Lending Limited (CFO Lending);

(iv) Cheque Centres Group Limited (Cheque Centres);

(v) Global Analytics Holdings, Inc (Global Analytics);

(vi) Harvey and Thompson Limited (H&T);

(vii) MYJAR; and

(viii) SRC Transatlantic Limited (SRC).

(c) Finally, we provide details of three further lenders with annual payday lending revenue over £10 million:[83]

(i) Oakam Limited (Oakam);

(ii) PDL Finance Limited (PDL Finance); and

(iii) Elevate Credit International Ltd, formerly Think Finance (UK) Limited (Elevate).[84]

2.83 The three groups of companies are presented below in alphabetical order. We estimate that the 11 lenders which comprise the first two groups (the 11 major lenders) accounted for around 90% of revenue generated from payday lending in the UK in financial year 2012. Diagrams of the corporate structures of the largest three lenders are set out in Appendix 2.6. As at November 2014 three of the major 11 lenders had exited the market (CFO Lending, Cheque

[83] Based on 2012 data.
[84] Think Finance press release.

Centres and The Cash Store) and Ariste had announced its intention to exit the market.[85]

CashEuroNet

2.84 CashEuroNet is one of the UK operating subsidiaries of Enova, a US finance company offering unsecured short term loans (including payday loans), instalment loans, and line of credit accounts within the USA, UK, Australia and Canada. Until November 2014 CashEuroNet sat within the group structure of Cash America International Inc (Cash America) in a holding company Enova International Inc (Enova). Established in 1984, Cash America is listed on the New York Stock Exchange and has a market capitalisation of approximately $650 million. It operates within the USA offering a variety of loan products including pawnbroking loans, unsecured short-term loans (including payday loans) and instalment loans. On 13 November 2014 Cash America completed a spin out of Enova, which is now listed on the New York Stock Exchange as a separate company with a market capitalisation of approximately $700 million. The restructuring created two separate entities with Cash America operating a high street business in the USA and Enova trading solely online.

2.85 Enova offers three online lending products to UK customers through its subsidiary CashEuroNet: QuickQuid, a payday loan service launched in July 2007; Pounds to Pocket, an instalment loan product launched in September 2010; and FlexCredit, a running account credit facility[86] launched in March 2013.[87] [✂]. In 2014 Enova opened a UK office having previously had no physical presence in the UK. Enova has no high street stores and previously all online operations were managed from Chicago.

2.86 CashEuroNet generated total revenue of £[✂] million in 2012 from UK payday lending activities. Net profit for the same period was £[✂] million. In 2013 CashEuroNet's UK payday lending revenue increased by [✂]% to £[✂] million, with strong growth of [✂]% from its instalment payday loan Pounds to Pocket and additional sales generated from the launch of

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[85] H&T withdrew from single-payment one-month payday lending products in June 2013 and withdrew its online payday lending product in January 2014. H&T's personal loan product, introduced in September 2013, offers up to £1,000 repayable over up to 24 months. H&T personal loans granted for durations of 12 months or less are included in our terms of reference.
[86] With this type of product, a customer applies for a credit facility of a given value. The customer can then request any amount of money up to the value of the approved facility to be transferred to their bank account. Customers then repay over ten months but are able to repay earlier and reduce the outstanding balance. Interest is charged on the outstanding balance. However, if customers have made repayments according to their payment schedule they can request another transfer of money to increase the balance outstanding up to the original value of the facility.
[87] Another Enova subsidiary offers the 'On Stride' loan in the UK, which was launched in April 2014 and offers customers £1,000 to £5,000 from one year to three years at APRs ranging from 29% to 89%.

FlexCredit. In the first nine months of 2014 CashEuroNet's payday lending revenue decreased year on year by [✂]%; net profit increased [✂]%.

DFC/Dollar

2.87 DFC Global Corp (DFC) was sold to private equity firm Lone Star in June 2014 for $1.3 billion.[88] Prior to this DFC had been a NASDAQ-listed company with its headquarters in the USA. DFC operates throughout Europe and North America, including the UK, USA, Canada and Spain, offering a variety of short-term lending products.[89]

2.88 The UK operations of DFC are collectively known as Dollar. These include three subsidiaries offering payday loans and other credit products within the UK:[90,91]

(a) Instant Cash Loans Ltd (ICL), trading as The Money Shop, is a high street outlet. ICL was purchased by Dollar Financial UK Limited (Dollar) in February 1999, at which time it was operating 11 stores. Since then it has opened more than 500 stores throughout the UK, offering cheque cashing, pawnbroking, prepaid debit cards, foreign exchange and overseas money transfers. In 2013 the company generated total revenue of £[✂] million, [✂], and a net profit of £[✂] million.

(b) MEM Consumer Finance Limited (MEM), trading as PaydayUK, is an online operation. The original MEM business was founded in 2003 and acquired by DFC in 2011 for $195 million.[92] It offers a payday lending product through the website www.paydayuk.co.uk, and launched its Multi Payment Loan in August 2014. Total revenue for 2013 was £[✂] million and net profit £[✂] million.

(c) Express Finance (Bromley) Limited (EFL), trading as Payday Express, is an online operation. EFL began operating in 1999 and was purchased by DFC in 2009 for $[✂] million. Lending through its website www.paydayexpress.co.uk, EFL had total revenue of £[✂] million in 2013 and net profit of £[✂] million.

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[88] *The Guardian*, 2 April 2014, 'Money Shop owner Dollar Financial to be sold to Lone Star for $1.3bn'.
[89] Source: 10K.
[90] DFC also owns several pawnbroking shops in Scotland and England, including Suttons and Robertsons.
[91] Dollar introduced Ladderloans in 2012, an instalment product offering £500–£1,500 from 6 months to 18 months.
[92] 2012 DFC Global Corporation 10K.

2.89 In the financial year to June 2014 Dollar's UK performance deteriorated. Revenue from payday lending was down [✂]% to £[✂] million from £[✂] million the prior year. Dollar's payday lending activities generated [✂].[93]

2.90 In July 2014 Dollar announced a voluntary £0.7 million refund to customers after an FCA review found that Dollar had exceeded its own lending criteria in giving loans to certain customers. It also announced the appointment of a 'skilled person'[94] to review lending decisions.[95]

Wonga

2.91 Wonga was founded in October 2006 by Errol Damelin[96] and Jonathan Hurwitz[97] and launched its short-term consumer loans product, 'Little Loans', in 2007. As an online-only business, without any high street stores, it has developed its own loan approval technology.

2.92 Wonga is a subsidiary of Wonga Group Limited, itself a privately-held company registered in the UK. Since 2006 it has completed several rounds of equity financing and currently has three key shareholders: Balderton Capital (21%), Accel London II LP (14%) and Greylock Partners (12%).[98] Wonga Group Limited is thus the parent company and UK payday loans are made through its subsidiary WDFC UK Ltd (Wonga – formerly Wonga.com Limited).

2.93 The majority of Wonga's business is in the UK; it also provides consumer loans in Canada, Poland, South Africa and Spain. To promote this growth, subsidiaries for support services such as customer service and technology development have been opened in the Republic of Ireland, South Africa, Switzerland and Israel.[99]

2.94 Wonga offered three credit products in the UK as at August 2013: its main product was Little Loans, a short-term loan falling within our definition of a payday loan product; PayLater, a credit offering for online shopping; and Everline, a loan for small businesses.[100] In March 2014 Wonga announced

[93] [✂]
[94] A 'skilled person' is appointed under section 166 of the Financial Services and Markets Act 2000.
[95] See FCA press release.
[96] Errol Damelin resigned as a Director of Wonga Group Limited on 12 June 2014.
[97] Jonathan Hurwitz resigned as a Director of Wonga Group Limited on 5 November 2013.
[98] 31 December 2013 figures provided by Wonga.
[99] Note 8 to the consolidated financial statements for the year ended 31 December 2013.
[100] PayLater and Everline were launched in 2012, therefore the majority of Wonga's 2012 revenue of £305 million relates to Little Loans.

that it was trialling six-month instalment loans and withdrawing the PayLater product.[101]

2.95 Wonga generated revenue of £[✂] million from payday lending in 2013, [✂]. Revenue [✂] by [✂]% for the first nine months of 2014 against the equivalent period in 2013.

2.96 For the year ending December 2013 Wonga's UK business including non-payday activities reported a loss before income tax of £5 million after £18.8 million of costs relating to the remediation and settlement of historic debt collection and interest calculation issues, and further costs for complying with new regulatory standards.[102] Net profit for the prior year (ending December 2012) was £59 million.[103] Before exceptional costs and adjusted for the revised cost allocation set out in Appendix 4.5, Wonga's UK payday lending activities generated a profit before interest and tax of £[✂] million in 2013, [✂] on the prior year. For the first nine months of 2014 Wonga's net profit [✂].

2.97 Since April 2014 Wonga has made several announcements regarding changes to its business resulting from regulatory developments.

(a) In April 2014 reported to the FCA that it had discovered system errors relating to the calculation of the amount owing on customer accounts where fees, balance adjustments or the timing used to calculate interest were not consistently applied.

(b) On 25 June 2014 Wonga agreed to repay £2.6 million to customers following an OFT/FCA investigation into its debt collection practices. The investigation found that Wonga had sent letters to customers from non-existent law firms threatening legal action over uncollected loan amounts. A 'skilled person' was appointed to oversee the process.[104,105]

(c) On 2 October 2014 the FCA announced that Wonga had entered into an agreement, known as a voluntary requirement (VREQ). The VREQ required Wonga to undertake remedial redress for customers who were affected by inadequate affordability assessments. The FCA indicated that approximately 330,000 customers in excess of 30 days in arrears will have the balance of their loan written off and will owe Wonga nothing; and

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[101] *The Guardian*, 26 March 2014, 'Wonga looks beyond payday to try out longer loans'.
[102] Report and Financial Statements. Wonga Group Limited generated a profit before tax of £31 million.
[103] Wonga Group Limited Annual Report, 2012. Wonga Group Limited reported net profit of £62 million.
[104] FCA press release.
[105] On 30 September 2014 Wonga Group announced results for the year to December 2013 which included a charge of £18.8 million for remediation relating to historic debt collection and systems issues.

that approximately 45,000 customers between 0 and 29 days in arrears will be asked to repay their debt without interest and charges and will be given an option of paying off their debt over an extended period of four months.[106]

Other major lenders

Ariste

2.98 EZCORP is a NASDAQ listed company with a $550 million market capitalisation as at 5 February 2015. It is based in Austin, Texas, and operates throughout the world in the consumer lending industry. In the UK, it had a significant investment[107] in Albemarle & Bond Holdings Plc.[108] It currently still has significant investment in Cash Converters UK Limited.[109] Its primary UK payday lending operation is a wholly-owned subsidiary, Ariste, trading as Cash Genie.

2.99 Cash Genie began offering payday loans in October 2009 and was partly acquired by EZCORP in 2012 and fully in 2013 for a total of $43.5 million. Cash Genie is an online business providing payday loans. Total revenues for the 2012 financial year were £12.8 million with a net profit of £1 million. Total revenues for the financial year ending September 2013 were £16 million with a net loss of £4.6 million.

2.100 In October 2014 EZCORP announced a plan to exit the online lending business in the UK[110] and said that it expected to have completed its exit, whether by wind-down or sale, before the end of the second quarter of fiscal 2015.[111]

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[106] FCA press release.
[107] ezcorp.com (accessed 29 October 2013).
[108] In early December 2013 Albemarle & Bond commenced a formal sales process for the company. Operating primarily in the gold-buying and pawn loan industries, profitability and net debt have been significantly impacted by the unexpected fall in gold prices, increased competition and lower supply of gold for sale. Refinancing is required in order not to breach loan covenants; a rights issue was unable to proceed after discussions between EZCORP and other related parties, and the company failed. (Albemarle & Bond Annual Report.) On 25 March 2014 administrators were appointed to Albemarle & Bond Holdings Plc. The administrators announced on 15 April 2014 that the majority of the business and assets had been sold to Promethean Investments LLP. See PwC website.
[109] EZ Corp annual report 2013 indicated ownership of one-third of Albemarle & Bond Limited and one-third of Cash Converters UK.
[110] [✂]
[111] On 6 October 2014 EZCORP, Inc, the parent company of Ariste (trading as Cash Genie), issued a press release announcing a plan to exit the online lending business in the UK. EZCORP stated that recent changes in the UK regulatory environment relating to HCSTC had created challenges for the Cash Genie business. These changes included *(a)* the transfer of regulatory authority from the OFT to the FCA in April 2014; *(b)* the enactment by the FCA of regulations that focused on the affordability of the credit extended (ie the customer's ability to repay), the use of CPA to collect repayments, and sustained use of short-term credit products; and *(c)* the publication in July 2014 of the FCA's proposal for rate caps on HCSTC products scheduled to become effective

The Cash Store

2.101 Until April 2014 The Cash Store Financial Services Inc was a Canadian company which was listed on both the New York Stock Exchange and the Toronto Stock Exchange, with a market capitalization of CAD 34 million.[112] In 2010 it began operating in the UK through its subsidiary The Cash Store Financial Limited, the parent company of The Cash Store.

2.102 As at August 2013 The Cash Store had 29 stores in the UK through which it offered payday loans and a small amount of cheque cashing. The company generated total revenue of £6.2 million in 2012 and a net loss of £5.2 million.

2.103 In April 2014 the Cash Store's Canadian parent company, Cash Store Financial, entered administration.[113] The UK subsidiary followed in August 2014.[114]

CFO Lending

2.104 CFO Lending is a privately-held company registered in the UK. Founded in 2008 as Capital Finance One, it offered payday loans online through the brands CFO Lending and Payday First until May 2014. The company generated total revenue of £19.6 million in 2012, with a net profit of £0.1 million. The company generated total revenue of £23.6 million in the financial year ending August 2013, with a net profit of £0.8 million. CFO ceased lending in May 2014 and in August 2014 the FCA appointed a 'skilled person' to review its collection practices).[115]

Cheque Centres

2.105 Cheque Centres is a wholly-owned subsidiary of Axcess Financial Services Limited (Axcess) (which in turn is part of CNG Financial Corporation), a privately-registered US company which also operates as a payday lender in the USA. As at June 2013 Cheque Centres offered payday loans through two companies in the UK: Cheque Centres (high street) and Cheque Centre (online) (formerly The Loan Store).

2.106 Cheque Centres (high street) was established in 1996 by a small group of Edinburgh business people and sold to Axcess/CNG Financial Corporation

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in January 2015. In light of these changes in the regulatory environment, and in the context of the refinement in company strategy, the company had decided to exit the Cash Genie business as soon as practicable.

[112] In April 2014 it announced that its shares would be delisted from the Toronto Stock Exchange effective on 23 May 2014 as a result of failing to meet the exchange's listing requirements.

[113] See CCAA information.

[114] See *The Independent*, 12.8.2014.

[115] See FCA Requirement Notice.

group in 2006. As at June 2013 its 433 stores throughout the UK offered a variety of services including payday loans, cheque cashing, foreign exchange and gold buying. With total revenues of £356 million, £[✂] million from payday loans, the company recorded a net [✂] in the 2012 financial year. In the financial year ending December 2013 Cheque Centres generated total revenue of £[✂] million, £[✂] million from payday loans and a net [✂]

2.107 Founded in 2008, Cheque Centre (online) entered the payday loan market in 2011 to provide online short-term loans. [✂] of its revenue, however, has been derived from its other activities of foreign exchange and gold. Revenue from payday lending was £[✂] million in 2012 with total company turnover of £12 million. The company generated net [✂] in 2012. Revenue from payday lending was £[✂] million in 2013 with total company turnover of £[✂] million. The company generated £[✂] million in 2013. Cheque Centre (online) stopped offering payday loans in January 2014 and, following an agreement with the FCA, Cheque Centres (high street) have now ceased offering single instalment payday loans.[116]

2.108 Cheque Centres withdrew from UK payday lending in May 2014 following a review by the OFT/FCA. Instalment lending and pawnbroking were also temporarily suspended while changes were made to collection policies and staff retrained.[117]

Global Analytics

2.109 Global Analytics is a privately-held company based in San Diego, California (USA). It operates in the UK through its wholly-owned subsidiary Lending Stream LLC (Lending Stream), which began offering payday loans in 2008.

2.110 Lending Stream LLC trades using the brand Lending Stream. It previously also traded as Zebit between 2012 and 2014. Zebit loans are no longer offered, although customers can apply for six-month loans via the Lending Stream brand. For this investigation both were considered payday loan products. Total Global Analytics revenue attributable to Lending Stream LLC was £49 million and £64 million in 2012 and 2013 respectively. In 2013, after five years of consecutive losses, Global Analytics reported a net profit of £4.6 million related to Lending Stream LLC.

[116] For more details refer to Voluntary Application for Imposition of Requirement: Cheque Centres Limited.
[117] See FCA document.

H&T

2.111 As at June 2013 H&T Group plc offered payday loans through its subsidiary H&T, which operated 194 stores throughout the UK. H&T Group plc has been listed on AIM since 2006 and as at 5 February 2015 had a market capitalization of £64 million. It was previously owned by Cash America, which founded H&T's payday lending operation.

2.112 H&T's core business is pawnbroking and gold buying, with a small amount of payday and instalment lending historically performed in-store and online. Total revenue for the company for 2012 was £130 million, of which payday lending contributed £[✂] million. Net profit for the same period was £12.9 million. Total revenue for the company for 2013 was £99 million, of which payday lending contributed £[✂] million. Net profit for the same period was £4.9 million. H&T withdrew from single-payment one-month payday lending products in June 2013 and withdrew its online payday lending product in January 2014. H&T's personal loan product, introduced in September 2013, offers up to £1,000 repayable over up to 24 months. H&T personal loans granted for durations of 12 months or less are included in our terms of reference.

MYJAR

2.113 MYJAR, formerly known as TxtLoan Limited, provides online payday loans. Founded in 2008, it began lending in March 2009, offering open-ended loans with a minimum term of 18 days. As at June 2013 it has provided over 1 million loans to customers throughout the UK. Total revenue grew over the prior four years, reaching £[✂] million in 2013; [✂]. Total revenue for 2014 was £[✂] million; [✂].

2.114 From October 2010 MYJAR has been part of Txt Holdings Ltd, a privately-held holding company based in Jersey. MYJAR operates solely in the UK and has headquarters in London with an internal technology and support team in Estonia. The company is funded through intercompany and shareholder loans.

SRC

2.115 SRC is a wholly-owned subsidiary of Speedy Cash Intermediate Holdings Corp. This is itself a wholly-owned subsidiary of Speedy Group Holdings Corp, a privately-held US company.

2.116 SRC operates two payday companies within the UK: high street and online business Speedy Cash; and the online-only WageDayAdvance Limited (WageDayAdvance).

2.117 SRC and its online lending operation WageDayAdvance share a compliance function. Following an FCA review in June 2014, an independent person was voluntarily appointed to review compliance for both companies.[118]

- *Speedy Cash (SRC's high street business)*

2.118 The high street lending operations of SRC, trading as Speedy Cash, was opened by its parent company in November 2010 and has since grown to 23 branches throughout the UK.

2.119 As at June 2013 Speedy Cash offered three payday loan products: a flex account, an instalment-based 'flex loan' and a single-payment payday loan. SRC ceased offering its open-ended flex account in June 2014 and ceased online lending in December 2014. SRC generated payday lending revenue of £[✂] million (total revenue of £12.2 million) in 2012. The net loss for Speedy Cash for the same period was £9.4 million. SRC generated payday lending revenue of £[✂] million (total revenue of £16.6 million) in 2013 in the financial year ending December 2013 and a net loss of £4.9 million.

- *WageDayAdvance Limited (SRC's online business)*

2.120 WageDayAdvance, SRC's online business, began offering payday loans in December 2006 as Cash 4 Compensation Ltd. Changing its name to WageDayAdvance in February 2008, it was one of the first online payday lenders. Offering one payday loan product, and a small cheque-cashing operation, WageDayAdvance had total revenues of £39 million and a net profit of £15 million in 2012. WageDayAdvance had total revenues of £35 million and a net profit of £9.3 million in the financial year ending December 2013.

2.121 In February 2013, WageDayAdvance was acquired by SRC, becoming a fully-owned subsidiary. Prior to this the company had been privately held by six equal shareholders who provided the majority of funding.

2.122 In February 2014 WageDayAdvance introduced FlexAdvance, an instalment loan of between £80 and £750 payable over up to 18 months. In January 2015 FlexAdvance was replaced with the WageDayAdvance payday loan.

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[118] See FCA Requirement Notice.

Other lenders

Elevate

2.123 Elevate (previously Think Finance UK) offers credit products under the name of Sunny. It previously offered (but has since ceased) loans under the product quid.co.uk. Elevate Credit International is a subsidiary of US firm, Elevate (previously Think Finance, Inc), which is privately held and backed by venture capitalist firms Sequoia Capital and Technology Crossover Ventures. In 2012 Think Finance (UK) Limited generated total revenue of £14 million, making a £3 million net loss.[119] In 2013 Think Finance (UK) Limited generated total revenue of £13.7 million, making a £17.4 million net loss.

2.124 Elevate entered the UK payday lending market in 2011 with the acquisition of Fortress Capital, a UK-based provider of one-month loans. Fortress Capital had one product, 1 Month Loan, and after the acquisition, the company then launched quid.co.uk. In 2013, Elevate withdrew its 1 Month Loan product. In May 2014, it withdrew its quid.co.uk product. Until 2 January 2015 Elevate offered just Sunny, a line of credit product where customers could borrow up to £1,000 and repay within five months through instalments. On the 2 January 2015, Elevate withdrew its Sunny line of credit product. It said that the introduction by the FCA of its new rules and guidance (contained in the CONC) had made such a product unprofitable. Elevate now offers a range of instalment products under the brand Sunny with terms and rates varying by the amount borrowed.

Oakam

2.125 Oakam launched in 2007 and offers payday loans both online and through high street stores with a call centre serving the whole of the UK.[120] As at January 2015 it operated 21 stores across London and the Midlands. It currently offers two loan products: ‘The Bonus Loan’ for periods between three and six months; and ‘The Big Plus Loan’ for 6 to 36 months. Both products are eligible for cashback rewards for on-time repayments.

2.126 The company is privately held and registered in the UK. It has one major shareholder, CS Capital Partners III LLP,[121] which also provides funding for the business. The majority of its total revenue for 2012 of £19.9 million and net profit of £2 million was generated by The Bonus Loan product.[122] In the

[119] Think Finance annual report 2012.
[120] Annual report 2012.
[121] ibid.
[122] ibid.

financial year ending December 2013 the company generated total revenue of £21 million and net profit of £0.3 million.

PDL Finance

2.127 PDL Finance is a privately-held UK company offering payday loans via its online service 'Mr Lender'. As at June 2014, a payday loan product was the only loan product offered with customers able to borrow between £80 and £500 for up to 30 days. As at January 2015, PDL Finance offered a payday loan with customers able to borrow between £100 and £1,000 for up to 6 months.

2.128 SDJ Enterprises Ltd is the parent company and primary funder of PDL Finance; it is also registered in the UK. PDL Finance generated total revenue of £17.5 million in 2012, with net profit of £2.4 million.[123] PDL Finance generated total revenue of £36 million and net profit of £6 million in the financial year ending December 2013.

Lead generators operating in the payday lending sector

2.129 In this section we outline the role of lead generators operating in the payday lending sector.

2.130 As well as approaching a payday lender directly, customers may also be directed to online payday lenders by one or more intermediaries such as lead generators which contract with payday lenders to provide potential customer applications (or 'leads') in return for a fee for each lead provided. Like credit brokers more generally, lead generators are required to hold a consumer credit licence (as they 'introduce individuals seeking credit to businesses that provide credit').[124]

2.131 Lead generators include:

(a) Pingtree operators, which are lead generators providing technology platforms[125] to auction the details of prospective borrowers applying for payday loans.[126] Pingtree operators may operate websites themselves which collect details from applicants, or process applications submitted by marketing affiliates (see *(c)* below).

[123] PDL Finance annual report 2012.
[124] See Appendix 3.1 for a discussion of relevant regulation.
[125] Technology platforms may work in conjunction with telephone call centres.
[126] See paragraphs 2.146-2.147 for further details on the operation of the Pingtree.

(b) Directory listings or database lead generators, which list payday loan lenders and lead generators in tabular format, or offer a search function, as a means to collect details of prospective borrowers searching for payday loans for onward sale to pingtree operators or processing in their own pingtree.

(c) Affiliates,[127] which are generally marketing companies collecting customer data via a lead form (which is then passed to pingtree operators or lenders), or using lead forms on websites run by pingtree operators.

(d) Fee-charging brokers offering a service to manage an application for the user and potentially finding a payday lender for them for an upfront fee. Fee-charging brokers may contract separately with lenders for additional payment from the lender to the broker.

2.132 Lenders may also use affiliates to generate traffic using, for example, banner advertisements or a PCW.

2.133 We discuss first the size and structure of the lead generator channel and then the role of lead generators in the payday lending market. In Section 6 we discuss customers' use of lead generators and the transparency of lead generators' websites. In Section 7 we set out the expenditure across the market on different acquisition channels (Table 7.2) and how this varies between lenders (Figure 7.3) with some larger lenders focusing their customer acquisition expenditure more heavily on television and non-digital advertising ([✂]) which contrasts with the greater use of lead generators by other smaller lenders [✂].[128]

Size and structure of lead generator channel

2.134 Many lead generators operate in the UK payday loan sector. Our analysis of payments made by payday lenders to lead generators showed that 130 lead generators were operating in 2012. Most of these companies were very small – only 45 lead generators accounted for more than 0.05% of total payments made by lenders to lead generators in 2012.

2.135 The lead generators we analysed[129] dealt with more than 43 million leads[130] in 2013 and sold more than 9 million of these applications to payday lenders.

[127] The use of the term affiliate relates to 'affiliate marketing', whereby an 'affiliate' receives commission for directing traffic to a supplier (or additionally on conversion of that traffic to a sale) and does not indicate any control or shared ownership by a parent entity.
[128] However, the cost per customer acquired will vary by both lender and by channel employed.
[129] For details of our sample see Appendix 2.7, Annex B.
[130] Includes leads sold by pingtree operators and leads sold by lead generators directly to lenders only to avoid multiple counting of affiliate leads.

Leads may fail to sell to payday lenders for reasons including: poor data integrity such as missing digits in mobile phone numbers; affiliates specifying a minimum commission which is too high for lenders; and lead data not meeting the requirements of payday lenders such as the age of the applicant. If payday lenders choose not to buy leads such leads may be sold to non-lenders such as other lead generators including fee-charging brokers, debt management firms and marketing companies.

2.136 The lead generators in our sample generated combined revenue of £[✂] million in 2013 from UK payday lead generation activities. Aggregate 2013 net profit from all activities (including in some cases operations in overseas markets and non-payday markets), was £[✂] million.

2.137 Table 2.6 shows UK revenue generated from the sale of leads to payday lenders in 2013.[131] [✂] was the largest lead generator in our sample and reported turnover of £[✂] million from the sale of leads to payday lenders in 2013, almost [✂] the size of [✂] and [✂], which generated turnover of £[✂]million and £[✂] million respectively. The three largest lead generators accounted for [50–60]% of our total sample's 2013 revenue. All three large lead generators operate pingtrees.

TABLE 2.6 UK **revenue of lead generators from sale of leads to payday lenders for the year ending 31 December 2013**

Lead generator	*Revenue (£m)*
9Global	[✂]
Cannon Finance	[✂]
D&D/T3 Leads	[✂]
EPL	[✂]
Eudore	[✂]
Interfinancial	[✂]
Knight Creative	[✂]
Lead Tree	[✂]
Lending Metrics	[✂]
Loan Machine	[✂]
Loan Partners	[✂]
Market Genomics	[✂]
Money Gap	[✂]
New Wisdom Solutions	[✂]
Nouveau Finance	[✂]
Pingtree Ltd	[✂]
Quiddi	[✂]
RevUp Media	[✂]
Sandhurst Associates	[✂]
Sigma	[✂]
Stop Go Networks	[✂]

Source: CMA analysis of lead generator template.

Note: Four lead generators did not provide revenue figures.

2.138 We identified two broad strategies operating in the lead generation sector for payday loans. Some lead generators work to build online brands to attract

[131] For company descriptions see Appendix 2.7 Annex A.

applications from customers, for example: Beeloans.co.uk (operated by Knight Creative); paydaypig.co.uk, (operated by Stop Go); purplepayday.co.uk, (operated by Pingtree) and Cash Lady (operated by Money Gap).[132] Money Gap told us that its two largest websites generated the great majority of its leads.

2.139 Other lead generators seek to attract leads from affiliates (a type of lead generator themselves, see paragraph 2.131*(c)*), for example D&D generates all its traffic from affiliates, and both Loan Machine and Quiddi told us that around 90% of total leads collected were generated by affiliates.

2.140 We were told that there were more than 1,500 affiliates operating in the payday lead generation channel in the UK. Many affiliates are very small companies and may use the services of an affiliate network to pass leads to pingtree operators. We identified New Wisdom, Swift Money and Sandhurst Associates as three affiliate companies operating widely in the sector.

2.141 Lenders generally rely on affiliates to a lesser degree than lead generators. In particular, we note that affiliates account for only 2.2% of all advertising spending by lenders; around one-third of all advertising spending in the market is on lead generators (see Figure 7.2 for an analysis of all customer acquisition channels). As noted above in paragraph 2.133, the relative expenditure of different lenders on the various acquisition channels varies significantly.

The role of lead generators in the payday lending market

2.142 A significant proportion of customers applying for a payday loan online do so via the website of a lead generator.

2.143 Lead generators market their services in various ways including: *(a)* purchasing key words on search engines; *(b)* hosting or operating websites (including landing pages, directory listings and lead forms); *(c)* placing traditional online banner advertisements, including for example, on PCWs such as money.co.uk;[133] *(d)* inserting advertising material into contextually relevant websites such as internet fora, blogs, social media and newsletters; *(e)* search engine optimisation techniques such as embedding metadata in

[132] We noted that Money Gap had used television advertising to create customer awareness of the Cash Lady brand.
[133] Including banner ads in comparison sites, for example [✂] told us that it had generated [✂]% of leads collected in the last 12 months from [✂].

webpages or designing webpages to rank highly on search engines; *(f)* email marketing campaigns;[134] and *(g)* SMS messages.

2.144 Online search is the main means by which most lead generators attract applicants to their websites. Swift Money, Market Genomics and Knight Creative told us that 100% of traffic to their websites was generated by search engine marketing. Pingtree told us that more than 50% of traffic to its own websites was generated by paid search and organic search marketing, with the remaining activity coming from a mix of display, email, returning customers and SMS marketing.

2.145 As noted in paragraph 2.135, lead generators generate income by selling customer details to lenders. To do this, lead generators operate websites which ask customers to complete a form that captures information needed by lenders to make an 'in principle' lending decision. Where a lead generator supplies details to multiple lenders, customer details are then sold through an auction mechanism referred to as a 'pingtree'.

2.146 At a high level, the pingtree operates as follows:

(a) lenders specifying the characteristics[135] of potential customers which they wish to buy 'leads' on (that is, have the opportunity to offer credit to directly) and the number of leads that they wish to purchase;

(b) in most instances the lender which bids the most for a certain type of customer will be offered matching leads first; and

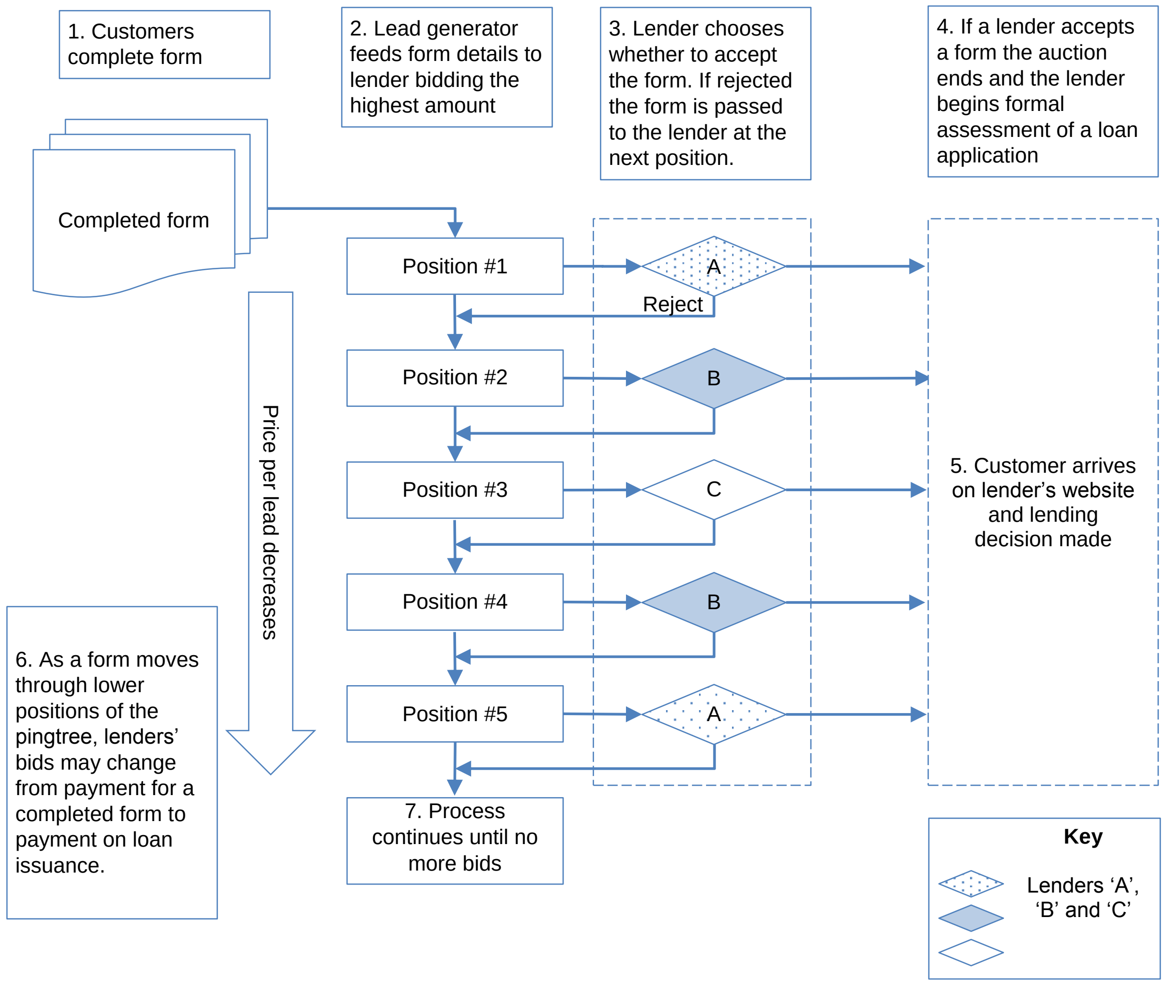
(c) the lender then undertakes a risk assessment and must decide whether to purchase the lead at the bid price. If the lender chooses not to purchase the lead, the lender with the next highest bid is offered the lead.[136]

2.147 The operation of the pingtree is shown diagrammatically (with three lenders, A, B and C)[137] in Figure 2.11. When a lead is offered to a lender, the lender has a short window of a few seconds to undertake its initial risk assessment to decide on whether to accept the lead. This restriction is imposed by the lead generator to ensure that a customer is passed to a lender before the customer decides to abort the process.

[134] For example, [✂] told us that 15% of its leads were supplied by affiliates, most of which did not have websites but promoted by email marketing.
[135] Also known as 'qualifying criteria'.
[136] Passing on leads in this way is known as going down towards the bottom of the pingtree.
[137] Our analysis indicated that pingtrees typically operate with between 20 and 40 payday lenders.

FIGURE 2.11

Diagrammatic representation of the pingtree



Source: CMA analysis.
Note: In this example there are three lenders: 'A', 'B' and 'C'. Both lenders 'A' and 'B' occupy two positions each and the placing of these positions is based on the bid price for that customer's form. Our analysis indicated that pingtrees typically operate with between 20 and 40 payday lenders.

2.148 Money Gap, one of the largest lead generators, told us that lenders may occupy three to five pricing points on the pingtree.[138] For the best-quality leads, payment is on the basis of any lead purchased; lower-quality leads, sold lower down the pingtree, are bid for on the basis of whether a customer ultimately takes out a loan.

2.149 Money Gap told us that on average approximately 20 to 25% of leads entering the pingtree were ultimately purchased by any lender on a 'cost per accepted lead' basis. The top lenders generally accepted 1 to 2% of the customers they were offered. These lenders were relatively stable in their activity in the

[138] That is, a lender may target three to five different types of customer and bid accordingly.

pingtree. They typically operated towards the top of the tree and paid per accepted lead. [✂].

2.150 Leads are generally sold on the most favourable commercial terms for the lead generator. In most cases it appeared that leads are sold to the highest bidder in the auction process, although three parties submitted that there were circumstances in which this would not be the case: Credit Benefit Services indicated that a lender bidding for a higher volume of leads at a set price might be offered a lead in preference to a lender seeking a lower volume at a higher price. Stop Go Networks told us that it might choose to sell leads to a lender rather than a broker bidding a higher price in order to maintain good relationships with lenders. SGE Loans told us that in cases where its call centre employees discussed a number of loan offers with borrowers, the product chosen by the customer might be the 'best match' for the borrower, as discussed with the call centre employee.

2.151 Table 2.7 shows that data collected on lead prices was consistent with evidence from lenders, for example CashEuroNet said that the price of the most expensive leads was close to £[✂] in 2013.

TABLE 2.7 **Lead prices, 2013**

£

	Cost per funded leads	*Cost per application leads*
Range	2–280	0.35–70
Average maximum	70	30
Average	25	8

Source: CMA analysis of lead generator template.

2.152 Leads are sold on a cost-per-application basis – where the lead generator receives payment from the lender on sale of the lead; or on a cost-per-funded (CPF) basis – where payment is dependent on the applicant taking out a loan with the lender which has bought the lead. In 2013 lead generators in our sample sold around 90% of leads on a cost-per-application basis.

2.153 Affiliates are typically paid a percentage representing the majority (generally ranging from 70 to 95%) of the amount that a pingtree operator receives from the party that purchases the lead. In some instances affiliates are paid on a 'per lead', 'per application' or 'per click' basis.

Fees charged by lead generators

2.154 Where fees are charged to borrowers by lead generators, these fees can take several forms including: membership fees, administration fees, application processing fees, brokerage fees, and service fees. SGE Loans charges a

£99.99 'Premium Service' fee which gives borrowers access to a 'VIP' customer service telephone number and email address, vouchers and discount codes for retailers and restaurants. SGE Loans told us that [✂]% of its customers chose to pay the premium service fee in addition to the administration fee of £5. Premier Net told us that it charged applicants a one-off fee of £69.99 for a six-month period.[139] We noted that fees set out on the websites of other fee-charging brokers[140] ranged from around £45[141] to £70.[142]

Other market participants

2.155 In this section we outline briefly the role of a number of third parties active in the payday lending sector. In turn we consider PCWs, search engines and CRAs.

Price comparison websites

2.156 In many online markets for financial products, PCWs play a key role in helping customers to compare the offering of different suppliers. A number of websites exist (or existed previously) allowing visitors to carry out some comparison of the terms of different payday lenders, although the traffic generated by these websites (and lenders' reliance on them for new customers) is very limited. One of the largest financial services PCWs, moneysupermaket.com, operated a payday loan comparison site until spring 2013. This service was withdrawn in response to the increasing level of media and political scrutiny into payday lender practices, and the perception of non-compliance in the sector.

2.157 The range and selection of 'lenders' listed and the functionality of these sites may affect their utility to customers. For example, some such as money.co.uk and whichwaytopay.com include brokers/lead generators as well as lenders, whereas others such as allthelenders.co.uk include only lenders. In each case only a relatively limited subset of lenders is included. Typically these sites will provide basic information on the loan products such as the representative APR, the loan amount, the possible duration and the total amount repayable for a £100 loan for a given lending period (which could vary by lender[143]) but do not allow a customer to input their specific loan requirements.

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139 Premier Net told us that it offered an auto loan facility that could be used to place further loans.
140 Not included in our sample.
141 Midlandcash.com.
142 Mymoneyfinder.co.uk.
143 For example, the cost for a month-long loan is calculated by different lenders using a period of 28, 30 or 31 days on some comparison sites.

2.158 We discuss some limitations of the PCWs currently operating in the payday lending sector in greater detail in Section 6.

Search engines

2.159 Customers can research and identify payday lenders using web search engines such as Google, Yahoo! and Bing.

2.160 An individual using Google to search for a payday lending related term will be presented with links to the websites of a number of lenders in the organic search results, as well as a number of pay-per-click advertisements for payday lenders and brokers. In 2013, the term 'payday loans' was searched for between 200,000 and 300,000 times a month on Google. Customers also search for individual lenders, with searches specific to the products of Wonga and CashEuroNet being searched for more times each month than the more generic term 'payday loans'.

2.161 Our analysis of search results on Google's first page for a number of payday-loan-related terms[144] on a number of dates in 2013 and 2014[145] found that of the top 10 organic search results generated by each of these searches on each of these dates, 39% were lenders' websites, 15% were comparison websites, 5% brokers'/lead generators' websites and the remaining 41% included news websites, advice websites and editorial content.[146]

2.162 Our analysis of pay-per-click advertisements[147] found that lenders' websites were the most common links presented alongside payday related search terms (67% of the advertisements), followed by lead generators (26%[148]) and comparison websites (4%).[149]

2.163 The proportion of each lender's customers that reach that lender's website by using a search engine varies significantly,[150] and this may in part relate to each lender's expenditure on pay per click.[151]

2.164 Search engines may require lenders who use pay-per-click advertising to comply with specific requirements on the content and presentation of financial

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[144] Namely: compare payday, payday, payday lenders, payday loan direct, payday loan lenders, payday loans and payday UK.
[145] Specifically on 4, 6, 8, 11, 13, 15 and 18 November 2013, and 29, 30 and 31 January 2014.
[146] Lenders' website appeared more frequently (49%) in January 2014's search results than in November 2013's (35%) whilst links to 'others' were more common in November 2013 (47%) than in January 2014 (28%).
[147] Both those placed at the top and those placed on the side of Google's page.
[148] Which is considerably greater than their presence in organic search results.
[149] These figures are roughly similar in November 2013 and January 2014. The remaining 2% related mostly to financial products other than payday loans.
[150] We discuss this further in Section 6.
[151] We discuss expenditure on customer acquisition by different channels in Section 7.

information on lenders' websites. Advertising that is found not to comply with these requirements could then be excluded from appearing on search results pages. In addition, search engines may limit the range of search terms which payday lenders are permitted to advertise their products alongside – for example, Google limits payday lenders to advertising alongside search terms specific to payday loans.[152]

Credit reference agencies

2.165 Most payday lenders – both online and high street – purchase information from CRAs regarding applicants when carrying out a credit risk assessment. The three largest CRAs are Experian, Equifax and Callcredit. These CRAs hold large databases of individuals' personal information, past credit history and current credit commitments. This shared data is available on commercial terms to lenders.

2.166 Lenders are not required to use information from CRAs in making a lending decision but should do so 'where necessary'.[153] Different lenders purchase information from (and share information with) different CRAs, and so no single CRA will hold complete records of borrowers' use of payday loans. Many lenders will purchase information from more than one CRA when making credit-risk assessments.

2.167 Lenders commonly used to provide information to the largest CRAs on a monthly basis, with CRAs making the information available to other customers shortly after its receipt and validation.[154]

2.168 In February 2014 the FCA stated that it would like the industry to identify and remove any blockages to RTDS as a matter of urgency but that if the industry cannot overcome the obstacles, and the FCA is best placed to bring about data sharing, the FCA would not hesitate to act.[155] Since then, two of the three largest CRAs (Callcredit and Experian) publicly announced that they were developing systems to allow lenders to provide and access information in real time or near real time. In its subsequent Policy Statement on introducing a price cap, published on 11 November 2014, the FCA concluded that significant progress had been made in this area with the vast majority of the HCSTC market (around 90%) now participating in RTDS. In view of this significant progress, and likely impact on the HCSTC market following the

[152] For example, ensuring that any only search terms relating directly to payday lending and not credit in general can be used.
[153] CONC 5.2.1 (3) R.
[154] Although smaller CRAs exist – for example, LendingMetrics – whose records are updated in real time.
[155] FCA, Policy Statement PS14/3, February 2014.

introduction of the price cap, the FCA chose not to consult on introducing mandatory RTDS requirements. FCA stated that it expected further improvements in coverage in the near future following the recent launch of real time services by the larger CRAs and that it would continue to press the industry to make progress on RTDS.[156]

2.169 CRA data is available (on commercial terms) to lenders under the Principles of Reciprocity (developed and administered by the Steering Committee on Reciprocity whose membership includes lenders and CRAs). The Principles (at a high level) require lenders to share with CRAs the same categories of data to those which they receive from the CRA, which maintains the accuracy of customer credit information. We discuss lenders' views on the utility of CRA data in Section 7.

2.170 We discuss lenders' use of CRA data in the application process in Appendix 2.4.[157]

[156] FCA, PS 14/16.
[157] We also consider the design issues in improving the use and availability of CRA data and credit searches in remedying the AEC we have found in Appendix 9.3.

3. The regulation of payday lending

3.1 In this section we describe the regulatory framework that applies to the payday lending sector. The regulation of this sector has evolved significantly over recent years, so we first describe the background to the development of the regulatory framework, before describing the current regulatory regime including recent and forthcoming changes to regulations, and then the specific requirements applicable to payday lenders.

Background to the development of the current regulatory framework

3.2 As part of its response to the financial crisis of 2008, the Government made important changes to the regulation of financial services and banking in the Financial Services Act 2012. This resulted in the abolition of the Financial Services Authority and the transfer of the majority of its functions to two new bodies: the FCA and the Prudential Regulation Authority. That Act also provided for the transfer of regulation of consumer credit from the OFT to the FCA (see paragraph 3.6).

3.3 In December 2012 the National Audit Office (NAO) published its report on regulation of consumer credit by the OFT,[158] drawing attention to the plight of the poorest borrowers in particular and highlighting concerns about the impact of payday lending on some of these borrowers. It also expressed concern about the effectiveness of the enforcement regime in driving better behaviour from market participants due to a lack of sufficient resource focused on enforcement. At the same time there were concerns being expressed by debt charities, such as Citizens Advice and StepChange, about how the rapid expansion of payday lending appeared to be fuelling debt problems for some borrowers.

3.4 The OFT undertook a review of compliance by payday lenders, publishing an Interim Report in November 2012 and its Final Report in March 2013. This highlighted a significant degree of non-compliance with consumer credit legislation and OFT regulatory requirements. A key passage of the OFT's conclusions is quoted below:

> Our evidence paints a general picture of poor compliance with the law and guidance across the market and throughout the lifecycle of payday loans, from advertising of loans to debt collection:

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[158] www.nao.org.uk/report/office-of-fair-trading-regulating-consumer-credit/.

- Lenders compete by emphasising speed and easy access to loans, but borrowers are not getting a balanced picture of the costs and risks of taking out a payday loan.

- Across the sector, there is evidence that the majority of lenders are not conducting adequate affordability assessments and their revenue streams rely heavily on rolling over or refinancing loans. Around one in three loans is repaid late or not repaid at all.

- Many lenders are not treating borrowers in financial difficulty with understanding or forbearance. Many are promoting rollovers when borrowers would be better served by a repayment plan. Continuous payment authorities are poorly explained to consumers and their misuse is causing distress to a considerable minority of consumers, in some cases leaving them with insufficient funds to cover their most basic needs.

- A number of firms are using aggressive debt collection practices which fall far below the standards we have set out in our Debt Collection Guidance.

- Across the industry we have seen evidence of poor internal procedures and processes, including a failure to put in place effective complaints handling systems.

This is causing real harm and the problem has grown. In the first quarter of 2009/10 only one per cent of Citizens Advice Bureau debt casework clients had at least one payday loan – in the same quarter of 2012, 10 per cent had at least one payday loan. In November 2012 StepChange Debt Charity reported that the proportion of their clients with payday loan debts had increased from 3.7 per cent in 2009 to 17 per cent in 2012.[159]

3.5 The further developments to the regulation of payday lending described below arose out of these concerns and similar concerns expressed by other bodies about the operation of the payday lending market.

3.6 In addition, as part of the Government's changes to the arrangements for competition, consumer protection and consumer credit regulation, on 1 April 2014, the competition and certain consumer functions of the OFT and CC

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[159] OFT, *Payday Lending: Compliance Review Final Report*, March 2013.

merged to become the CMA while the FCA became the regulator for consumer credit markets. The CMA is now the principal enforcer of the Unfair Terms in Consumer Contracts Regulations 1999.[160]

3.7 In this section we consider the current regulation of payday lending. We first describe the key elements of the regulatory framework that is now in place, and then discuss the main regulatory requirements applicable to credit agreements. Further details of the regulatory framework may be found in Appendix 3.1.

The regulatory framework

3.8 We consider below the key aspects of the regulatory framework of payday lending, namely:

(a) the Consumer Credit Act 1974 (CCA) and the Consumer Credit Directive 2008 (CCD);[161]

(b) the FCA's Consumer Credit sourcebook (CONC);

(c) the Irresponsible Lending Guidance, published by the OFT in 2010;

(d) the Financial Services and Markets Act 2000 (FSMA) as amended by the Financial Services Act 2012;

(e) the Financial Services (Banking Reform) Act 2013; and

(f) the role of self-regulation in the payday lending sector.

The Consumer Credit Act 1974 and the Consumer Credit Directive 2008

3.9 The CCA is the principal piece of legislation regulating lending and credit-related activities in the UK and since 1 April 2014 it has been partially replaced and supplemented by FSMA and FCA rules. The CCA lays down rules requiring information to be given to borrowers before entry into a consumer credit agreement. New regulations requiring information to be given to borrowers before entry into a credit agreement came fully into force on 1 February 2011, implementing provisions of the CCD.[162]

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[160] See Appendix 3.1 for further details.
[161] Directive 2008/48/EC.
[162] Directive 2008/48/EC.

3.10 For the purposes of the CCA, payday loans are either ‘fixed-sum’[163] or ‘running-account’[164] credit agreements (see Appendix 3.1).

3.11 The aim of the CCD was to increase the harmonisation of EU rules on consumer credit across EU Member States and increase consumer protection. It is a maximum harmonisation directive meaning that national authorities cannot, within the scope of the Directive, introduce national rules that exceed or contradict the provisions of the directive, unless expressly permitted. The CCD contains provisions specifying the standard information to be included in advertisements[165] and the requirements relating to the provision of pre-contractual information to enable borrowers to compare different offers and take informed decisions before the borrower is bound by any credit agreement[166] and to provide borrowers with adequate explanations to enable them to assess whether a product is suited to them and their financial situation.[167]

The FCA’s Consumer Credit sourcebook

3.12 The transfer of regulation for the consumer credit regime from the OFT to the FCA gave the FCA responsibility for firms that carry on consumer credit business.

3.13 In addition to the CCA, the FCA has made further rules for high-cost short-term credit lenders (including payday lenders) and debt management firms (see Appendix 3.1 for further details). These new CONC rules and guidance have applied to firms carrying on a consumer-credit-related regulated activity since 1 April 2014.[168]

3.14 Key elements of these rules are as follows:

(a) The CONC replicates pre-existing OFT wording with minor changes, but some of the material in the Irresponsible Lending Guidance and other

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[163] Fixed-sum credit is any other facility under a consumer credit agreement whereby the borrower is enabled to receive credit (whether in one amount or by instalments).
[164] Running-account credit is a facility under a credit agreement whereby the borrower is enabled to receive from time to time, from the lender, cash to an amount or value such that, taking into account payments made by the borrower (or payments to be credited to the borrower), the credit limit stipulated in the agreement (if any) is not at any time exceeded.
[165] Article 4.
[166] Article 5(1). This information must be presented using the Standard European Consumer Credit Information form and include the ‘interest rate applicable in the case of late payments and the arrangements for its adjustment, and, where applicable, any charges payable for default’ as well as a warning regarding the consequences of missing payments’. See CCD, Article 5(1) (l and m).
[167] Article 5(6).
[168] In order to allow firms time to become familiar with the new structure and style of rules and guidance, the FCA allowed a six-month transitional period. During this time, if a firm was able to demonstrate that it had acted in accordance with CCA requirements and OFT guidance, the FCA would not take action against it in relation to the equivalent new rules.

guidance has been rendered as Rules and the remainder has been reproduced largely as Guidance.

(b) Irresponsible lending – new Rules and Guidance in CONC cover the verification of creditworthiness and affordability and impose post-contract requirements.

(c) Credit brokers and intermediaries – references to requirements to assess affordability have been removed.

(d) Rollovers – since 1 July 2014, lenders may not refinance, or roll over, loans more than twice so that charges do not continue to escalate. When a loan can no longer be refinanced, instead the lender may pursue collection of the amount due and consider forbearance where customers are in default or arrears difficulties. The definition of 'refinance' in CONC reflects the language used in the FCA's earlier Consultation Paper of October 2013 in respect of rollovers.[169]

(e) CPAs – when taking out a payday loan, it is common for the lender to request the borrower to grant a CPA. Once agreed, a CPA allows the lender to take a series of payments from a customer's payment account without having to seek express authorisation for every payment. FCA rules provide that from 1 July 2014 no more than two unsuccessful attempts to take a payment with a CPA can be made, and a CPA must not be used to take part-payment.[170]

(f) Risk warnings – the FCA, in conjunction with the Money Advice Service (MAS), has revised the risk warning to be included by firms promoting a high-cost short-term loan, and has created an information sheet to guide consumers in financial difficulty to free debt advice.

3.15 All firms regulated by the FCA also have to comply with high-level Principles contained in the FCA Handbook. These include requirements to treat customers fairly and to deal with regulators in an open and cooperative way.[171]

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[169] In its policy statement, the FCA considers that:

> a loan is rolled over if the period over which loan repayments are to be made has been extended, or if the due date for any loan repayment has been moved to a later date, whether by means of an agreement that replaces, varies or supplements an earlier loan or otherwise (excluding any forbearance by the lender where the firm does not receive any consideration in connection with the rollover and the effect is that no interest or other charges (other than where a charge is a reasonable estimate of the cost of the additional administration required as a result of the customer having rolled over the agreement) accrue from the date of the rollover). See also CONC 6.7.18R.

[170] Apart from in the limited situation set out in CONC 7.6.14R (2).

[171] These Principles are contained in rule PRIN 2.1.1R of the FCA Handbook.

The Irresponsible Lending Guidance

3.16 Under section 25 of the CCA, the OFT had a duty to ensure that licences were held only by businesses that were fit to hold them (known as the 'Section 25 Test'). In March 2010, the OFT published its Irresponsible Lending Guidance.[172] The foreword of the Irresponsible Lending Guidance states:

> The primary purpose in producing this guidance is to provide greater clarity for businesses and consumer representatives as to the business practices that the [OFT] considers may constitute irresponsible lending practices for the purposes of section 25(2B) of the CCA. It indicates types of deceitful or oppressive or otherwise unfair or improper business practices which, if engaged in by a consumer credit business, could call into consideration its fitness to hold a consumer credit licence.

3.17 This guidance sets out the expectation that lenders will conduct a reasonable assessment of affordability and monitor repayments. If customers fall into difficulties with their repayments, the lender is expected to show forbearance in resolving the problem. These principles and the accompanying expectations of firms have been brought forward into the new regulatory framework.

The Financial Services and Markets Act 2000 and the Financial Services Act 2012

3.18 Consumer credit lending is now a regulated activity under section 22 of the FSMA. Firms with existing consumer credit licences must have applied to the FCA for an interim permission before 31 March 2014. Consequently no person may carry on that activity in the UK by way of business unless that person holds either an interim permission (firms which held an OFT consumer credit licence were invited to notify the FCA to obtain interim permission) or has been authorised by the FCA. The FCA has invited firms holding interim permission to apply for full authorisation during designated periods between 1 October 2014 and 31 March 2016.[173]

3.19 Like other firms regulated by the FCA, all firms providing consumer credit loans will have to comply with the Principles for Businesses in the FCA's

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[172] OFT, *Irresponsible lending – OFT guidance for creditors*, March 2010 (updated February 2011), OFT 1107.
[173] Firms with an interim permission are listed on the FCA's Consumer Credit Register. This register is a public record that contains information including a firm's basic details, a list of the regulated activities it has permission to carry on and its disciplinary history. If the FCA approves a firm's application for authorisation, these details will move to the Financial Services Register. The FCA also maintains a list of firms that were previously licensed by the OFT but do not have an interim permission.

Handbook, for instance with regard to treating customers fairly and cooperating with the regulator.

The Financial Services (Banking Reform) Act 2013

3.20 In December 2013, the Government imposed a duty on the FCA to make specified rules[174] in relation to one or more specified descriptions of regulated credit agreement appearing to the FCA to involve the provision of high-cost short-term credit with a view to securing an appropriate degree of protection for borrowers from excessive charges. The Financial Services (Banking Reform) Act 2013 amended the FSMA to place a duty on the FCA to implement this price cap no later than 2 January 2015.[175] The FCA published its final decision on the price cap on 11 November 2014 and these rules came into force on 2 January 2015.

Self-regulation

3.21 Self-regulation has also played a role in the payday lending sector. Following discussions between the Department for Business, Innovation & Skills (BIS), and four trade associations representing over 90% of the payday and short-term loan industry, a Good Practice Customer Charter[176] was published by the four trade associations representing payday lenders in July 2012: CCTA, CFA, BCCA and the Finance and Leasing Association (FLA)[177] (together, 'the trade associations').

3.22 The trade associations have committed their members to explaining how loans work and the costs involved; increasing transparency about loan repayments so that consumers can make informed decisions and are not surprised by hidden payments; providing help for customers in financial difficulty by freezing charges and interest; undertaking robust credit and affordability assessments to ensure that loans are suitable for the customer's situation; and effective compliance monitoring by the trade associations to root out poor practice in the industry. The CFA's Code of Practice required its members to operate a limit of three rollovers per customer.[178] This practice has since been limited to a maximum of two rollovers by the FCA.[179]

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174 See section 137C(1A) of the FSMA 2000.
175 Section 137C(1A) of the FSMA 2000, inserted by section 131 if the Financial Services (Banking Reform) Act 2013.
176 www.cfa-uk.co.uk/assets/files/PD&STL_Charter.pdf.
177 FLA has only one member in this sector, which is Wonga.
178 Consumer Finance Association: Lending Code for Small Cash Advances. Point 4.6.4 of the Code of Practice: 'Members shall not allow customers to extend a short term loan on more than three occasions'.
179 See Appendix 3.1.

3.23 Under the Good Practice Charter, the trade associations require their members to provide an annual statement of compliance and to be subject to periodic independent compliance visits. Failure to comply with the Charter could result in firms being subject to written warnings, recommendations as to future conduct and expulsion from the trade association for more serious breaches.

3.24 In relation to BCCA, any issues of non-compliance are raised with the lender to take action. If agreement cannot be reached members can face disciplinary action. The CCTA's[180] and the CFA's[181] Codes of Practice state that they may expel any of their members who failed to comply with the code.

The requirements applicable to credit agreements

3.25 A number of regulatory requirements currently apply to payday loan agreements. These may be considered under the following headings:

(a) existing provisions of the CCA which have been replicated as FCA rules;

(b) obligations under distance marketing regulations;

(c) new rules put in place by the FCA as discussed above; and

(d) from 2 January 2015, a price cap on the TCC.

CCA provisions replicated as FCA rules

3.26 Most of the conduct-related provisions in the CCA and its secondary legislation remained in place after 1 April 2014.

3.27 The provisions that were repealed are 'replicated' as FCA rules and guidance without being 'substantially changed'. These include the CCA provisions on:

(a) pre-contractual explanations (section 55A of the CCA);

(b) assessment of creditworthiness (section 55B of the CCA);

(c) assignment of creditor's rights to a third party (section 82A of the CCA);

(d) the method of calculating APR;

(e) credit intermediaries (section160A of the CCA);

[180] BIS, Government response to the consultation on proposals to ban the use of bills of sale for consumer lending, January 2011, Annex C: Code of Practice for bills of sale lenders (paragraphs 2.4 & 2.5).
[181] Consumer Finance Association: Lending Code for Small Cash Advances.

(f) procedures relating to events of default, termination or early settlement; and

(g) credit advertising.

Distance marketing regulations

3.28 The Financial Services (Distance Marketing) Regulations[182] apply where the borrower enters into a distance contract. From 1 April 2014 the key parts of the Financial Services (Distance Marketing) Regulations are dis-applied for firms that are authorised persons. CONC 2.7 and CONC 11 sets out the equivalent provisions for authorised persons etc. The Rules require the lender to provide the following information:

(a) name and address of the creditor;

(b) description of the main characteristics of the credit agreement;

(c) total price payable for the credit;

(d) arrangements for payment and performance; and

(e) information regarding a right to cancel.[183]

Price cap on the total cost of credit

3.29 As mentioned above, in December 2013, the Government imposed a duty on the FCA to make specified rules in relation to one or more specified descriptions of regulated credit agreement appearing to the FCA to involve the provision of high-cost short-term credit with a view to securing an appropriate degree of protection for borrowers from excessive charges by no later than 2 January 2015.[184] On 11 November 2014, the FCA published its final decision on the cap and these rules came into force on 2 January 2015.

3.30 The price cap has three key elements:

(a) The initial cost cap of 0.8% of the outstanding principal per day, on all interest and fees charged during the agreed loan duration and when refinancing. This covers all the charges and fees associated with a loan repaid on time (this includes interest charges, but also charges for any

[182] SI 2004/2095 Financial Services (Distance Marketing) Regulations 2004.
[183] See regulations 9–11. The customer has a right to cancel within 14 days after conclusion of the contract and if the rights are exercised is liable only for charges in respect of the service actually provided.
[184] Section 137C(1A) of the FSMA 2000, inserted by section 131 of the Financial Services (Banking Reform) Act 2013.

ancillary services, such as loan agreement charges, faster payment charges, insurance charges etc). Where a loan is repaid in instalments, the cap dictates the amount that can be charged on the outstanding balance.

(b) The cap for those in default of a total of (i) £15 on fixed charges and (ii) interest at the same rate as provided for in the agreement (subject to the 0.8% maximum per day) on outstanding principal and on fixed default charges.

(c) The total cost cap of 100% of the total amount borrowed applying to all interest, fees and charges.[185]

3.31 We consider the implications of the price cap where relevant in Sections 5, 6, 7 and 8.

[185] See CONC 5A.2.6R etc which sets out the total cost cap is the lesser of the amount of credit that the lender actually advances or the credit limit (where the agreement is for running account credit).

4. Market outcomes

Introduction

4.1 In this section, we consider market outcomes in the payday lending sector.

4.2 Outcomes of the competitive process in a market – eg prices and profitability, levels of innovation, product range and quality (including levels of customer service) – can provide evidence about its functioning. Evaluating these outcomes helps the CMA determine whether there is an AEC and, if so, the extent to which customers may be harmed by it, ie the degree and nature of 'customer detriment'.[186]

4.3 The remainder of this section is structured as follows:

(a) In paragraphs 4.4 to 4.109, we consider evidence about the pricing of payday loans.

(b) In paragraphs 4.110 to 4.190, we consider the profitability of payday lending companies.

(c) In paragraphs 4.191 to 4.217, we consider evidence of non-price competition between payday lenders.

(d) In paragraphs 4.218 to 4.221, we set out our conclusions on outcomes in the payday lending market.

Pricing of payday loans

4.4 In markets subject to effective competition, firms will be constrained to keep their prices down in order to win new business and retain existing customers. Pricing patterns can therefore help us to understand the effectiveness of competition in a market. In this subsection, we:

(a) consider the evidence on:

(i) the different components of payday loan prices, and the amounts that different lenders charge for their loans (paragraphs 4.5 to 4.42);

(ii) indicators of the extent of price competition between payday lenders (paragraphs 4.43 to 4.73); and

[186] The Guidelines, paragraph 103.

(iii) customer sensitivity to variation in prices (paragraphs 4.74 to 4.103); and

(b) describe our conclusions relating to the pricing of payday loans (paragraphs 4.104 to 4.109).

The price of borrowing using a payday loan

4.5 We begin with a description of the main pricing structures used by payday lenders, and a comparison of the prices at which payday loans are offered to customers.

The structure of payday loan pricing

4.6 The price paid for a payday loan has typically consisted of several distinct charges or fees, which may include some or all of the following:

(a) an interest or finance charge, calculated based on the agreed principal and duration of the loan;

(b) a compulsory flat fee;

(c) optional fees paid at the borrower's discretion in return for services such as faster transfer of the principal;

(d) top-up fees, charged when a borrower chooses to 'top up' their loan during its originally agreed term;

(e) 'rollover' fees and/or additional rollover interest charges when the loan is extended, with agreement by the lender, beyond the originally agreed repayment date; and/or

(f) fixed late payment, default or termination fees and/or late interest charges, incurred by the borrower when a repayment is missed and/or an outstanding balance remains overdue beyond certain thresholds defined by the lender.

4.7 Prices in the payday lending sector are now influenced by the FCA's price cap, which is discussed in greater detail in paragraphs 4.62 to 4.73. Paragraphs 4.8 to 4.13 below provide a brief summary of the most common and important aspects of payday loan pricing structures as observed in the period prior to the introduction of the price cap. A detailed account of the individual charges, their levels and structures is provided in Appendix 4.1.

4.8 The interest or finance charges of payday loans are typically based on simple interest rates charged per day or per month. For most products that charge a monthly rate, the borrower incurs the interest or finance charge for the full month even if the loan is repaid within a shorter period (for example, at the time of our review a borrower taking out a ‘chequeless’ payday loan with The Money Shop (Dollar) will pay monthly interest of £29.99 per £100 borrowed, irrespective of whether the loan is taken out 10 days or 20 days before their payday). Products with daily interest rates are often flexible around the issue of a customer’s repayment date (for instance, allowing early repayment without a penalty).

4.9 Some lenders charge compulsory flat fees at the point at which a loan is taken out (for example, at the time of our review borrowers taking out a loan with Wonga pay a £5.50 ‘transmission fee’). Such fees are typically included in (and subtracted from) the issued principal and are therefore themselves subject to interest charges. Additional optional fees are also applied to many products, for example in some cases where the loan is extended or ‘topped up’, or the borrower opts for the lender to transfer the loan principal using Faster Payments Service.

4.10 While it has not historically been common practice for lenders to vary their prices for different customers with the same borrowing requirements, there are some exceptions to this: most notably via the use of risk-based pricing or price promotions. Under risk-based pricing, the interest rate paid by a borrower depends on their risk of default as assessed by the lender, with less risky customers paying lower interest rates. For example, one lender in our review – CashEuroNet – classifies customers of its QuickQuid Payday product into three risk tiers: ‘average’, ‘good’ and ‘excellent’. Customers assigned to the highest-risk tier are charged the highest finance charge of £29.50 per £100 borrowed, while the lowest-risk customers pay £20 per £100 borrowed.[187] Elevate similarly offers reduced rates to lower-risk borrowers who make successive timely repayments, or participate in training on financial awareness.

4.11 None of the other payday lenders that we spoke to charge different prices to borrowers of different risk. However, several of the major lenders indicated that they either had considered or were considering introducing some type of risk-based pricing.[188] One potential drawback associated with risk-based

[187] Risk-based pricing is not currently available for borrowers using CashEuroNet’s FlexCredit product, which now represents over [✂]% of CashEuroNet’s issued loans to new customers. [✂]
[188] For example, [✂]. SRC told us that it might be able to develop a risk-based product in the future but that the customer response to its previous experiments with risk-based pricing had not been strong enough for it to be profitable.

pricing which was highlighted by some lenders is the resulting increase in the complexity of prices.[189]

4.12 In addition to some providers offering lower rates to lower-risk customers, sometimes lenders offer certain customers promotional interest rates, or waive certain fees. The discounts offered, which are used to varying degrees by different lenders, have often been for substantial amounts. These promotions are targeted at various different customer groups, although broadly speaking, the coverage of the price promotions used by payday lenders is limited, and in many cases most customers will either be unaware or unable to avail themselves of these discounts. To give an example of a promotion used by a large lender, Wonga has in the past waived its transmission fee to [✂] and – until June 2013 – customers referred by moneysupermarket.com. Further details of the price promotions used by payday lenders – and in particular the size of these discounts and the targeted customer groups – are provided in paragraphs 4.55 to 4.61.

4.13 Late payment fees refer to flat fees and/or interest or finance charges incurred by the borrower when they fail to make a repayment by the previously agreed time and/or date, without having agreed an extension. For example, at the time of our review The Cash Store charged customers £25 where a loan is not repaid on its due date. Almost all products carry flat late payment fees. In addition, many products also charge late interest that is calculated based on the amount of the outstanding loan. The pricing structure of late interest charges tends to vary across lenders, and these charges:

(a) may be calculated at the same or a different rate to the original loan;

(b) may apply to the principal only or to the full outstanding balance;

(c) may or may not be subject to a limit in terms of days, after which additional interest is frozen;

(d) may be subject to forbearance, whereby lenders waive their late fees and/or late interest under certain conditions such as the customer's agreement to a repayment plan; and

(e) may be avoided where the borrower requests a loan extension or rollover that is approved by the lender. This can be a cheaper option depending

[189] For example, Dollar told us that its customers appreciated the transparency of its pricing model. Wonga highlighted the fact that risk-based pricing could come at the cost of being less simple for the customer if it was structured in such a way that it meant they could no longer see upfront exactly how much the loan would cost.

on the level and structure of late charges on a particular product and the length of time the borrower expects their final repayment to be overdue.

Analysis of lenders' prices – methodology

4.14 We considered the distribution of prices charged by payday lenders.

4.15 Given the differing pricing structures outlined in paragraphs 4.6 to 4.13, the cost to a payday customer of taking out a payday loan can depend on several factors, including:

(a) the desired loan amount, duration and instalment structure;

(b) whether the borrower expects to repay their loan on time, extend their loan and/or top up their loan;

(c) whether the borrower decides to avail themselves of optional services such as faster payment;

(d) the borrower's risk profile, as assessed by the lender; and

(e) the availability of discounts and price promotions.

4.16 The large number of possible combinations of these characteristics means that it is not possible to calculate prices for every possible combination. On the other hand, only calculating an 'average price' would not allow for the identification of price patterns that are specific to particular borrowing scenarios.

4.17 Instead, in order to understand the prices of payday lenders, we consider the cost of borrowing using different lenders' products in a number of 'representative customer scenarios'. The idea behind this approach is to:

(a) select specific scenarios that are representative of the different types of borrowing scenarios in which payday loans are taken out;

(b) analyse different lenders' prices, and the extent of variation in these prices in each of those scenarios; and, thereby,

(c) generate an understanding of pricing and price variation in the payday lending sector.

4.18 The process used to determine the representative scenarios used for our analysis is described in Appendix 4.2. We identified four scenarios which we consider to be representative of key patterns of borrowing behaviour among payday customers,[190] namely:

(a) a customer takes out a £100 loan for 28 days, which is repaid in full on time;

(b) a customer takes out a £100 loan for 14 days, which is repaid in full on time;

(c) a customer takes out a £100 loan for 28 days, which is rolled over for an additional 28 days before being repaid in full; and

(d) a customer takes out a £100 loan for 28 days, which is repaid in full 11 days late (the median overdue period among loans repaid late).

4.19 In each of these scenarios, we make the assumption that where they are given the option, customers opt to pay for faster payment, as opt-in rates for faster payment are high across the products considered in our analysis. We do not include any promotional rates in our analysis, as these discounts are generally available only to limited groups of customers (the extent of price promotions in payday lending is discussed in greater detail in paragraphs 4.55 to 4.61).

4.20 The measure we use for price in all four of these scenarios is the total cost of credit (TCC). The TCC is the total amount in pounds that a customer would pay if they took out and repaid a loan under the circumstances described in the relevant scenario.

4.21 We examined the pricing of the payday lending products offered by 11 major payday loan companies as of October 2013. A list of these products is provided in Appendix 2.1, Table 4.1. For ease of analysis and comparability, we have grouped certain products that are offered by these lenders together, and excluded others from our review (although these exclusions do not have a material impact on our overall findings). These steps are explained in Appendix 4.1.

[190] Loans that are equivalent to one of these four borrowing scenarios account for around 6% of all loans in our transaction data set. We consider that these examples allow us to understand the pricing of lenders in a much larger proportion of short-term borrowing scenarios, however, given that the prices of different lenders will typically vary linearly with the amount and duration of a loan. Further details of the sensitivity of our findings to variation in these parameters are provided in paragraph 4.33.

Analysis of lenders' prices – findings

4.22 In this subsection, we set out our key findings on the level and dispersion of different lenders' prices across different borrowing scenarios.

4.23 Table 4.1 summarises the prices of the different products of the 11 major lenders in each of the four scenarios in our review.[191] Figures 4.1 and 4.2 illustrate at a more granular level the prices of each lender for a £100 loan repaid on time after 28 and 14 days respectively. Similar charts corresponding to Scenarios 3 and 4 are shown in Appendix 4.2.

TABLE 4.1 **Descriptive statistics for TCCs* of £100 loans across representative borrowing scenarios**

£

Scenario	*Median*	*Mean*	*Minimum*	*Maximum*	*Range*	*Median deviation from median*
Scenario 1 – 28 days repaid on time	30	33	18	56	39	7
Scenario 2 – 14 days repaid on time	30	29	11	56	45	10
Scenario 3 – 28 days, 28-day rollover	60	62	35	92	57	14
Scenario 4 – 28 days, 11 days late	59	61	32	107	75	19

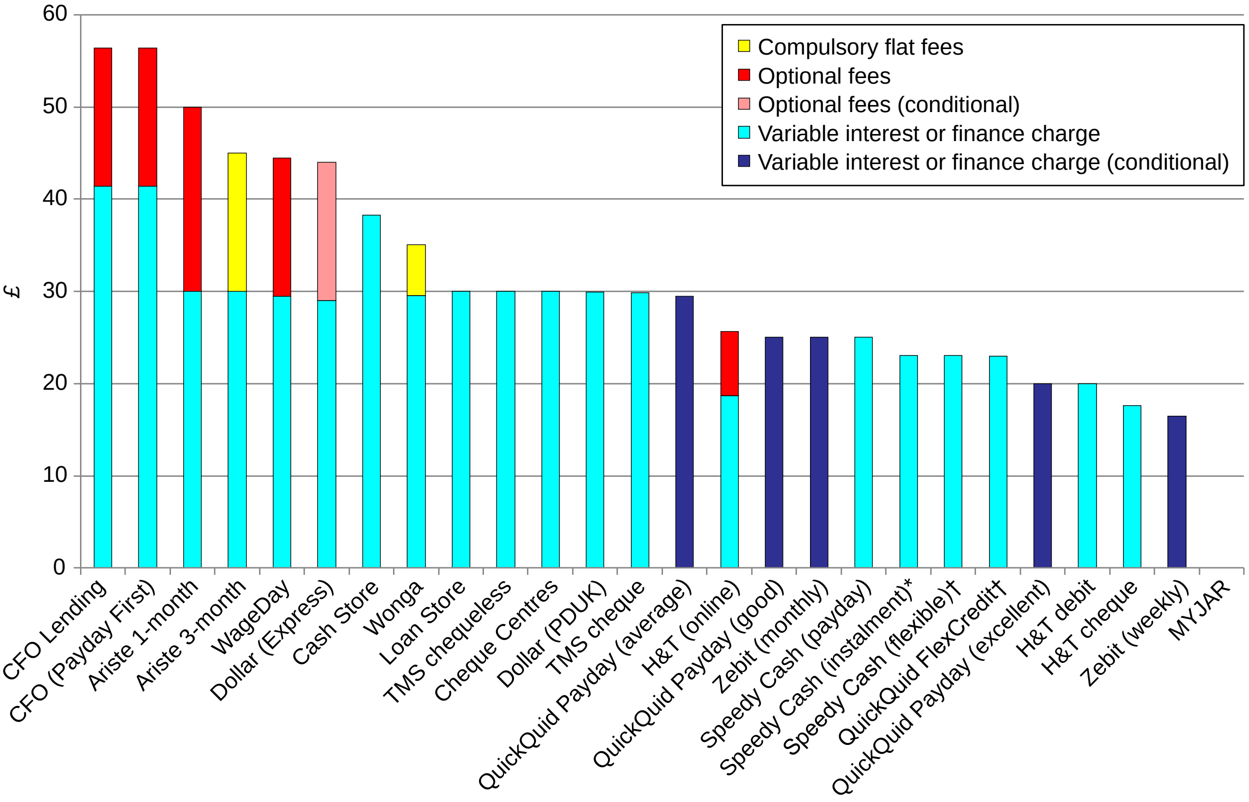
Source: CMA analysis.

*Values rounded to nearest £.
Note: Where products' prices depended on customers' characteristics, the price used for those products in calculating these descriptive statistics is the weighted average price, with weights derived from data on the proportion of customers with the relevant characteristic. The 'median deviation from median' measure is explained in paragraph 4.30. We include the mean and the median to show that the average prices are not excessively driven by outlying values.

[191] This exercise was conducted by reference to lenders prices as at October 2013. Some of these lenders have either exited the market or have temporarily ceased issuing loans since we carried out our review (see paragraph 2.74).

FIGURE 4.1

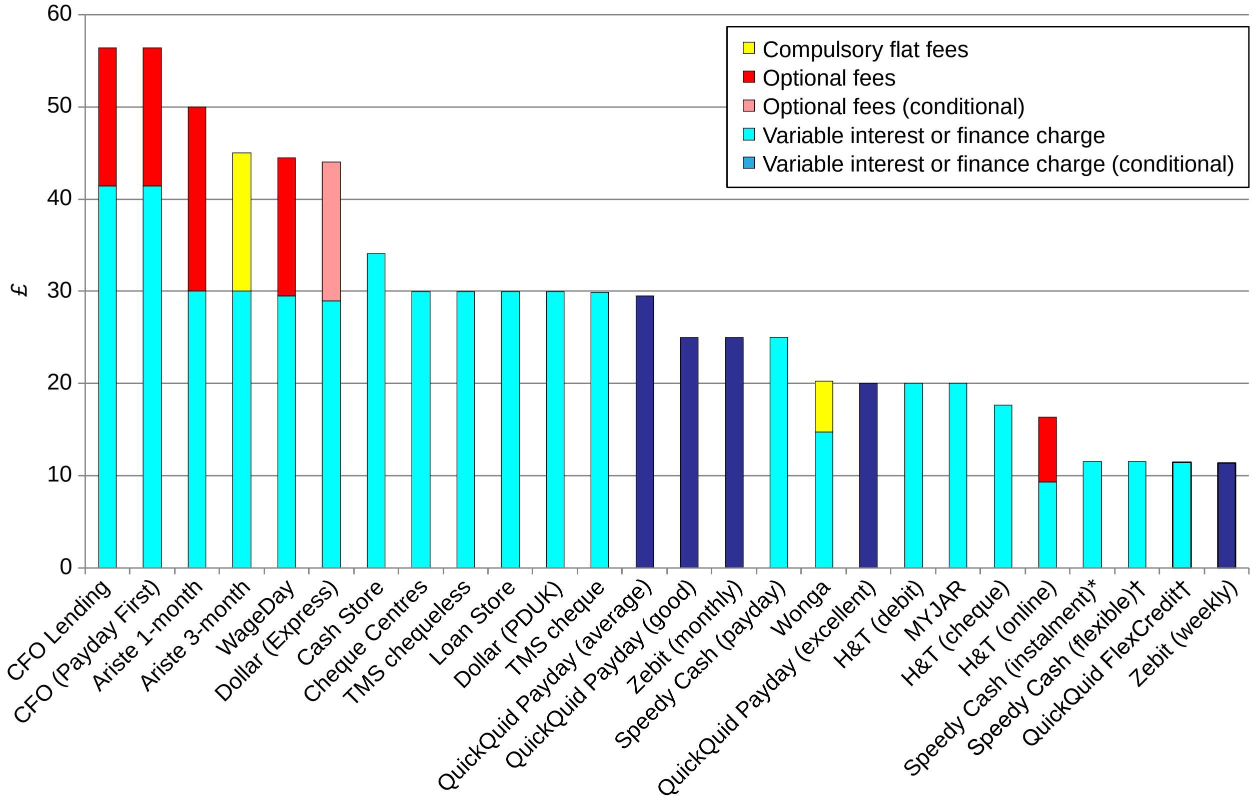
TCC for a £100 loan over 28 days (Scenario 1)



Source: CMA analysis of lenders' responses to the market questionnaire, October 2013.
*Long-term instalment products for which this scenario implies prepayment by the customer – see Appendix 4.1.
†Flexible open-ended credit agreements with a flexible draw-down structure.
Note: The maximum duration of MYJAR's product is 18 days and was therefore excluded from this analysis. Products whose prices varied depending on customer are shaded lighter red, namely Payday Express (whose faster payment fee did not apply to new customers), and darker blue, namely QuickQuid Payday (for which the price depended on the customer's risk tier) and Zebit (for which the repayment structure, and therefore price, was determined by the customer's pay cycle).

FIGURE 4.2

TCC for a £100 loan over 14 days (Scenario 2)



Source: CMA analysis of lenders' responses to the market questionnaire, October 2013.
*Long-term instalment products for which this scenario implies prepayment by the customer, see Appendix 4.1.
†Flexible open-ended credit agreements with a flexible draw-down structure.
Note: Products whose prices varied depending by customer are shaded lighter red, namely Payday Express (whose faster payment fee did not apply to new customers), and darker blue, namely QuickQuid Payday (for which the price depended on the customer's risk tier) and Zebit (for which the repayment structure, and therefore price, was determined by the customer's pay cycle).

4.24 Looking across the products of the 11 major lenders, we observe that the prices of many products were the same whether a customer borrowed for 14 or 28 days due to their 'per month or part-month' interest rate structure. The products that were cheaper in the 14-day scenario than in the 28-day scenario were products with daily interest rates.

4.25 There was a degree of clustering around a headline price of £30 for a £100 loan for customers borrowing for a month or less (further commentary on how this pattern emerged is provided in paragraph 4.47). In both the 28- and 14-day scenarios, the average price of a £100 loan among the products in our review was close to £30. In addition, several different lenders charged monthly interest around this price, including some of the largest lenders in the market: Dollar (for both its online and high street products), Cheque Centres and CashEuroNet (for customers using its QuickQuid Payday product and falling into the 'average' risk tier).

4.26 Several products that had TCCs that were above £30 for a £100, 28-day loan nevertheless also carried headline interest rates of approximately 30% a month or 1% per day. For example, excluding the £5.50 compulsory fee, Wonga's product was priced at 1% per day; MYJAR's interest charge for its 18-day fixed-term loan worked out at 1.11% per day; and excluding optional faster payment fees, WageDayAdvance charged 29.5% and Ariste charged 30% interest per month or part-month.

4.27 Wonga told us that pricing must generate sufficient revenue to allow for a reasonable profit margin above the level of costs and risk borne by the lender and that this might lead to a £30 price point (taking into account 30-day loan lengths for many payday lenders). CashEuroNet told us their pricing reflected the risk of their customers and their operating model.

4.28 Dollar told us that price clustering had been driven to £30 per £100 by customer demand and response. It also highlighted [✂]. SRC similarly told us that the market had identified a price that customers were willing to bear, that reducing prices would eventually cause lenders to lose margin and that lenders instead competed on customer service, convenience and speed. MYJAR told us that customer feedback suggested that £1 per £100 per day was a price that was acceptable to customers.

4.29 Despite a number of lenders charging amounts close to these averages, we observe some significant variation in the TCC incurred by customers borrowing from different lenders, with products available which cost customers substantially more or substantially less to borrow the same amount for the same period. This is illustrated by the large difference between the cheapest and most expensive alternatives available on the market – a gap of £39 in the price of borrowing £100 for 28 days, and £45 when borrowing £100 for 14 days.

4.30 The significant price dispersion was not solely driven by outliers. We calculated the median price deviation across all products from the median price. We used the median as our measure of the average price as the mean is susceptible to being disproportionately affected by a small number of extreme prices. For a 28-day, £100 loan we found the median price to be around £30, but half of all products in the market were £7 or more away from this price. For a 14-day, £100 loan, the median price was also £30, but half of all products in the market were £10 or more away from this price.

4.31 Turning to the other borrowing scenarios, most lenders' interest charges did not change when a loan is rolled over, and so we find that the average price for a 28-day, £100 loan was around £60 when extended for an additional 28 days – twice the average of the on-time borrowing scenario.[192] Looking across the different products, the average price of taking out a £100 payday loan for 28 days and then repaying 11 days late was around £59.

4.32 We found that there was again significant price dispersion in the event that a customer rolled over their loan or repaid late. The difference between the price of the most expensive and cheapest products in our review was £57 for a 28-day, £100 loan rolled over for 28 days, and the gap was £75 for a 28-day loan repaid 11 days late. In the 28-day rollover scenario the median deviation is £14 from the median price of £60. The late repayment scenario showed the most significant dispersion (in absolute terms) of all of the scenarios: half of all products were at least £19 away from the median price of £59 for a £100, 28-day loan repaid 11 days late.

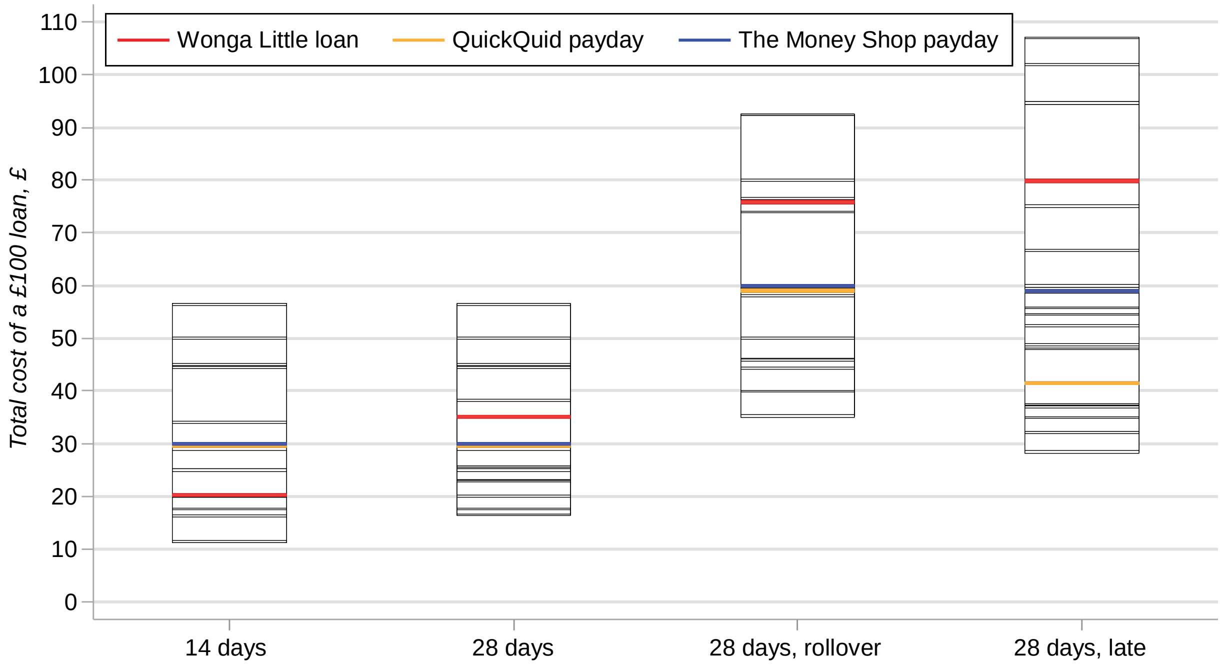
4.33 We also observe variation in the relative prices of different lenders' products across scenarios. That is, a product that was relatively cheap in one scenario could be relatively expensive in another. This was driven by some lenders' use of daily interest rates (which caused their products to be relatively cheap at shorter loan durations, more expensive at longer durations), as well as by variation in the size of the late and other fees charged by different lenders.

4.34 To illustrate this variation in relative prices, Figure 4.3 shows the price of borrowing £100 as at October 2013, using products of three of the largest lenders – Wonga, CashEuroNet and The Money Shop – under each of the four borrowing scenarios. The cost of borrowing using each of these products (indicated by the coloured lines) was shown in the context of the range of prices observed across the products of all 11 of the major lenders (the grey bars). The figure shows that borrowing with Wonga was considerably cheaper when taking out a 14-day loan, but more expensive for a 28-day loan or if the loan was rolled over. If the loan was repaid late, CashEuroNet's QuickQuid Payday product became significantly cheaper than the other two alternatives.

[192] However, it should be noted that lenders generally required part payment of the outstanding balance before approving a rollover. The components that must be repaid varied across products.

FIGURE 4.3

The relative price of borrowing £100 using the products of Wonga, QuickQuid and The Money Shop, under four borrowing scenarios



Source: CMA analysis.
Note: The black bars show the range of prices offered by the 11 major lenders, the black lines show the prices of other lenders.

4.35 We considered the extent to which our findings regarding lenders' prices were sensitive to the parameters of the representative scenarios chosen. We found that:

(a) Price dispersion tended to be higher when considering loans with shorter durations. This is because the TCCs of products with daily interest rates – which tended to be relatively cheap – become cheaper for shorter loans, while the TCCs of traditional 'monthly' products did not change when the duration was less than one month. The pattern of clustering around a price of £30 per £100 was not sensitive to duration, as most of the products priced at this level were traditional 'monthly' products.

(b) The scale of price dispersion tended to fall in relative terms when considering larger loans. This is because where flat fees applied (affecting eight of the products in our review), these fees become smaller in relative terms for larger-value loans.

(c) The TCC of a loan repaid late was likely, for some lenders, to vary significantly depending on the length of the overdue period due to both daily late interest, and flat late fees which were incurred after a specific

number of days. Nevertheless, because of the wide range of different late interest fees and charges used by lenders (see Appendix 4.1), we would expect to continue to observe significant dispersion in the TCCs of late loans under alternative assumptions regarding how late a loan was repaid.

Analysis of lenders' prices – the role of risk in explaining price dispersion

4.36 We considered the extent to which the differences in prices that we observed might reflect variation in the credit risk of the customer groups targeted by different lenders.[193]

4.37 We began by noting that payday lenders generally did not explicitly target their products at high- or low-risk payday customers in their marketing materials or on their websites. Nevertheless, it is possible that lenders might have targeted different risk groups in deciding their thresholds for which applications to accept or reject.

4.38 We considered the strength of the relationship between different lenders' default risk and their prices. A strong, positive correlation between lenders' average default costs and average prices would support the hypothesis that dispersion in lenders' prices reflected variation in the risk profile of their borrowers. On the other hand, a weak correlation may suggest that default costs were not the primary driver of lenders' prices.

4.39 When considering lenders' prices, rather than selecting any single borrowing scenario, we computed each lender's average revenue across all loans issued in financial year 2012, and then compared this with the lender's average default rate.[194] We sought to control for differences in lenders' loan profiles, by dividing each lender's revenue by the average loan value, and the total duration of all loans issued by that lender.[195]

4.40 Figure 4.4 sets out the results of our analysis. It shows that there was significant dispersion both in lenders' average prices and in principal loss rates. However, we did not find a clear correlation between the two. In particular, some lenders with relatively high average daily revenues enjoyed

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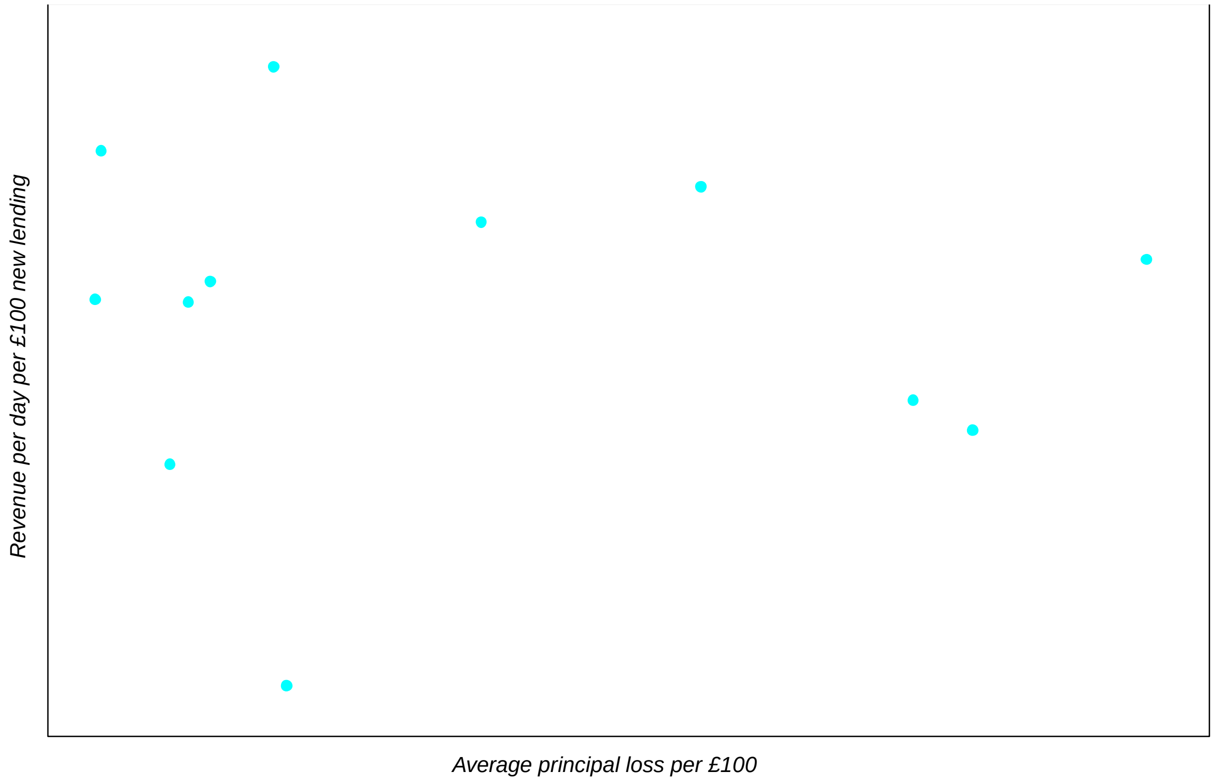
[193] CashEuroNet said in paragraph 4.3 of its response to the annotated issues statement that 'wide price dispersion may simply reflect payday lenders to some extent serving different types of customers (by risk profile)'.
[194] As the financial years of lenders do not always coincide, so the revenue and default rates that we calculate for each lender relate to overlapping but not identical periods.
[195] For a given lender, the average revenue earned per day per £100 lent is given by its total accounting revenue divided by its total value of new principal lent, all divided by the average duration of its loans. Total accounting revenue includes all revenue earned from interest income, origination fees, optional fees and penalty fees. Average duration is calculated as the average difference between the date of the loan agreement and the date of the final repayment. This measure of average revenue effectively describes the amount of revenue, on average, that a lender generates for every day £100 of principal has been issued and remains outstanding.

relatively low default rates, and there were substantial differences in average daily revenues among lenders with similar default rates.

FIGURE 4.4

Price versus default costs



Source: CMA analysis.

Note: Revenue includes all finance charges payable on single payment loans. Multi-period loans have been excluded due to differences in the revenue recognition policies for finance charges due but unpaid because of default. The average revenue data for one of the points relates to revenue from instalment products, which may not be comparable to the other data due to differences in revenue recognition. The exclusion of this point would not affect the conclusions drawn from this analysis.

4.41 One potential limitation of this approach is that there may be other cost factors which also affected lenders' prices, and that any relationship between prices and default costs would only emerge when controlling for these other factors. However, in this respect we note that the pattern of weak correlation remains when we consider Figure 4.4 and restrict our attention to:

(a) traditional payday loan products with no instalment or flexible line-of-credit structure;

(b) payday loan products that do not offer short durations and/or daily interest rates; and

(c) online products.

4.42 Our full analysis of the relationship between lenders' revenues and their costs is set out in the subsection on profitability, starting from paragraph 4.110.

Price competition between payday lenders

4.43 We next considered the extent to which payday lenders compete with each other on prices. We first discuss the way in which prices have evolved during the past seven years. We then discuss lenders' use of pricing promotions. Finally, we consider some recent developments in payday lenders' pricing.

Evolution of prices in the period 2007 to 2013

4.44 This subsection discusses our findings based on evidence from the historical evolution of prices. We first discuss our findings in relation to headline prices (paragraphs 4.45 to 4.50) before separately describing the evolution of late fees (paragraphs 4.51 and 4.52). These findings are drawn from our analysis of the payday loan prices of each of the major lenders over the period 2007 to 2013, which is presented in detail in Appendix 4.3.

4.45 Headline price changes were infrequent. Many lenders either made one change to their products' headline rate since 2008, or never changed their prices. For example, following some early adjustments to its transmission fee, the price of borrowing with Wonga for loans repaid on time did not materially change in the period from 2009 to 2013.[196]

4.46 Where price changes took place, they tended to be price increases and, correspondingly, the trend was for the average price for a loan repaid on time to increase over the period.

4.47 Many of the price increases that we observe reflected lenders adjusting their prices from a lower level up to an interest rate of approximately 30% per month, giving rise to the cluster of prices around 30% per month (or 1% per day) described in paragraphs 4.25 and 4.26. This 'cluster' emerged over a number of years, as follows:[197]

(a) In 2008, Wonga launched its product with an interest rate of around 1% per day. It introduced a transmission fee of £5.50 in mid-2008. At the point

[196] The only change was made in 2013, when Wonga changed its daily interest rate by a very small amount, from [✂]% to 1.0% per day [✂].
[197] We are aware that price changes towards a TCC of £30 for a £100, one-month loan have also taken place since the period considered in our review. For example, in 2014, SRC increased the interest rate of its payday loan products to 29% per month and the daily interest rate on its Flex Loan product to 0.95% per day.

of Wonga’s entry, all other payday lenders in our review charged monthly interest rates below the 30% level.

(b) In 2009, CashEuroNet increased the interest rate on loans to its highest-risk customers – [✂] – to 29.5% per month. At the end of this year, Ariste entered the market with a headline interest rate – excluding optional fees – of 30% per month on four different products.

(c) In 2011, WageDayAdvance increased its headline interest rate, excluding optional fees, to 30%. In the same year, Cheque Centres introduced its online Loan Store product with an interest rate of 29%. It also began increasing the interest rate on its high street product – this rate reached 30% in 2013.

(d) In late 2011 and early 2012, Dollar increased the headline rates of its online products, Payday Express and PaydayUK, to 29% and 30% per month respectively.

(e) In 2013, Dollar also increased the interest rate on its high street products to close to 30% per month.

4.48 There were very few instances of headline price reductions in the period. Since 2007, reductions in the TCCs of loans that are paid on time – ie reductions in interest charges, compulsory fees and/or optional fees – were only observed on six of the products considered in our review.[198] All but one of these reductions applied to products whose prices were already relatively high – ie costing at least £33 for a £100, 28-day loan – and none took the lenders’ prices materially below the £30 mark.

4.49 The other price reduction was associated with the introduction of risk-based pricing by CashEuroNet in 2009, albeit this price reduction applied only to the subset of its customers qualifying for its lowest-risk price tier. In particular, this represented a price reduction from £25 to £20 per £100 for these customers, while at the same time, prices were increased from £25 to £29.50 for customers in the highest-risk tier. For comparison, the lowest-risk tier accounted for [✂]% of new customers and [✂]% of repeat customers using this product in July 2013, while the highest-risk tier represented [✂]% of new customers and [✂]% of repeat customers.

[198] Dollar’s Payday Express, CashEuroNet’s QuickQuid Payday, Cheque Centres’ Loan Store product, CFO Lending’s two payday loan products and the Cash Store’s payday loan.

4.50 We saw two examples in the period where existing lenders introduced new products with low prices relative to other payday lenders, namely Speedy Cash's Flex Loan and Flex Account, and CashEuroNet's FlexCredit product.

(a) Since 2011, Speedy Cash introduced two new products:

(i) The first of these was 'Flex Loan', a 12-month instalment product with a price of around £21 for a 28-day, £100 loan. In 2013, the Flex Loan was changed to an 18-month instalment product with a higher price of £23. Recent information on the Speedy Cash website indicates that the price of the Flex Loan for a one-month, £100 loan has increased to £29. SRC told us that more than 90% of its customers now chose the Flex Loan.

(ii) The second of these was the 'Flex Account', an open-ended credit agreement with a price of around £23 for a 28-day, £100 loan. SRC suspended this product in July 2013 as the take-up rate was low.

(b) Towards the end of the period, CashEuroNet introduced QuickQuid FlexCredit. This product was priced at a relatively low level of around £23 for a £100, 28-day loan repaid on time. We consider the introduction of FlexCredit alongside other recent developments in payday lenders' pricing in paragraphs 4.62 to 4.73.

4.51 We also considered how charges on loans that are repaid late had changed in the period. We found that changes to late fees and interest are similarly uncommon: 6 of the 11 lenders we considered had kept their charges unchanged during the period. This includes one of the three largest lenders, CashEuroNet.

4.52 Where lenders have changed their late charges, those changes have been infrequent, rarely occurring more than once per year, and are almost always substantial increases. To summarise the changes in the period:[199]

(a) Two lenders introduced new late charges during the period, PaydayUK (a £15 flat late fee) and H&T (which introduced a daily late interest charge for its high street products equivalent to the monthly interest rate).

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[199] SRC also introduced a late fee of £10 for each missed instalment on its Speedy Cash Flex Loan product and a £25 default fee on its Speedy Cash payday loan product in November 2013.

(b) WageDayAdvance's late interest rate increased in 2011. While the daily rate was decreased in 2013, the flat fee of £12 has recently been increased to £20.

(c) Wonga increased its 'day one' late fees on a number of occasions over the period, trebling its charges from a £10 flat fee in October 2007 to a £30 flat fee in August 2013.[200]

(d) The Money Shop reduced the late fee on its cheque-based loan from £25 to £16 in 2012, but then increased this fee to £29 in August 2013. The late fee on its 'chequeless' loan was increased from £25 to £29 in 2012.[201]

(e) CFO Lending's late interest rate has fluctuated over the period in line with its product's headline interest rate, while its flat late fee of £25 has not been changed.

4.53 We also considered lenders' commentary on their price changes. Several lenders told us that they adjusted their prices or products' characteristics to win customers from other payday loan providers. In general, we saw little evidence to support this, although there were a small number of relevant examples, which are discussed elsewhere in this sub-section. Notably, four lenders[202] told us that they did not adjust their prices or products' characteristics to win customers from other payday loan providers:

(a) Cheque Centres told us that it was not aware of how other payday loan providers affected its business and that it had not responded to other lenders' activity by changing the features of its product. It also told us that its Loan Store business did not overtly compete with other payday lenders, that it did not track their pricing or changes to their offering and that other competitors' stances did not drive its own activity, pricing or profitability.

(b) MYJAR told us that other lenders' prices were not a key factor in its pricing and that it set its price at a level that customers saw as fair and that gave it an economic return. It also indicated that it took no actions to win customers from individual competitors, except to adjust the criteria for leads and the price it paid to 'introducers'.

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[200] Wonga reduced this late fee to £20 in April 2014.
[201] The Money Shop reduced this late fee to £15 and changed its overdraft balance interest to 0.769% per day in November 2014.
[202] Three of them have either temporarily or permanently ceased issuing payday loans (Ariste, Cheque Centres and The Cash Store), see paragraph 2.74.

(c) Ariste told us that it had not taken any actions to win customers from, or reacted to the competitive actions of, its competitors, but that it would not rule out this approach in the future.

(d) The Cash Store told us that it had not been in a position where it needed to react to specific competitive actions of other lenders.

4.54 Wonga argued that we had failed to adequately explore price competition which occurred through the interaction of price structure, rather than headline prices.[203] However, while we acknowledge the variation in pricing structures that existed in the market (as described in paragraphs 4.6 to 4.13), we noted that there was very little evidence of lenders changing their pricing structures in the period since 2008 to make the price of their products more attractive. Wonga also said that insufficient weight had been given to competition relating to charges for optional services such as faster payments, which affect the cost to a payday customer of taking out a payday loan.[204] As we discuss in paragraph 4.203, most lenders have introduced fees for the use of faster payment services in the period since 2008. However, we noted that only two of these lenders removed this fee later.

Use of price promotions

4.55 In this subsection, we discuss the extent to which payday lenders discount their headline rates for specific groups of customers.

4.56 Price promotions were used to varying degrees by all three of the largest lenders. Where offered, these promotions typically involve a substantial discount – for a £100, 28-day loan repaid on time, the discounts offered by these lenders ranged in value from around £4 to around £10. In particular:

(a) Wonga’s discounts typically consisted of waiving its £5.50 transmission fee (and, therefore, also the additional interest charges that applied when this amount is included in the principal). This reduced the price of a £100, 28-day loan by £7.04.

(b) CashEuroNet told us that the average discount from its promotions given to new customers was 32% during the period June to August 2013. Depending on the customer’s price tier, this average discount corresponded to a discount of £6.40, £8.00 or £9.44 on a £100, one-month loan repaid on time.

[203] Wonga's response to the provisional findings, paragraph 2.2.
[204] ibid, paragraph 2.6(b).

(c) Dollar's PaydayUK and Payday Express businesses both offered a discounted 25% interest rate to some customers, amounting to a saving of £4 and £5 respectively on a £100, one-month loan repaid on time.

(d) Dollar's Money Shop has offered promotional interest rate reductions of between [30–40]% and [50–60]% to some new customers of its cheque-based loan product between 2010 and 2013. However, no such discount has applied since the price increase to £29.95 per £100 in 2013.

4.57 These promotions were targeted at a number of different customer groups, commonly including:

(a) repeat/existing borrowers;

(b) customers referred by comparison websites; and

(c) customers responding to specific advertising campaigns.

4.58 The coverage of these promotions – ie the proportion of loans sold at the relevant promotional price – was generally quite small. In particular, promotional prices applied to [✂]% of Wonga's loans and [✂]% of cheque-based loans provided by The Money Shop. In August 2013, the proportion of new customers paying discounted interest rates [✂] was [✂]% for PaydayUK and [✂]% for Payday Express (although these figures averaged [✂]% and [✂]% respectively in the months after the discount began but before the closure of the payday loans section of moneysupermarket.com).

4.59 However, two of the promotions offered by the largest lenders had a broader coverage. In particular:

(a) CashEuroNet told us that its promotional discounts applied to [✂]% of loans issued to new customers in the period June to August 2013. These price promotions generally required applicants to enter a discount code advertised via affiliate websites, direct emails to customers, and pay-per-click and television advertisements.[205]

(b) Dollar's discounted interest rate of 25% (described in paragraph 4.56*(c)*) was applied to around [✂]% of the loans made by PaydayUK to existing customers in August 2013, and around [✂]% of the loans made to existing customers by Payday Express. This 'discount' is a legacy of the price increases introduced by Dollar's online subsidiaries in December

[205] CashEuroNet also clarified that it offered discounts when customers indicated that they had shopped around and were considering switching to a cheaper product from another lender.

2011 to March 2012, which were applied to new customers only, such that existing customers continued to be offered the pre-2012 interest rate.

4.60 Apart from the largest lenders, CFO Lending, Cheque Centres, H&T and WageDayAdvance all told us that they did not use price promotions. Ariste, The Cash Store, Global Analytics and MYJAR all offered price promotions that were small in terms of the coverage of loans.

4.61 SRC offered a substantial price promotion which applied to a large proportion of loans issued through its 'Speedy Cash' high street chain. This promotion offered zero interest on the first £200 borrowed by new customers and applied to over [✂]% of loans to new customers in August 2013. SRC told us that its interest-free loan offer had only led to a marginal pick-up in volume, see paragraph 4.76*(d)*.

Recent developments in pricing

4.62 In this subsection we discuss some particularly significant recent develop-ments in payday lenders' prices. In particular, we consider the introduction by CashEuroNet – the second largest online lender – of the FlexCredit product in June 2013, and then go on to discuss developments in the market subsequent to the launch of that product. We also briefly discuss possible impacts of the price cap that came into force in January 2015 on the pricing structures used by lenders, on loans of different duration, and on running account products.

4.63 CashEuroNet introduced FlexCredit in June 2013. This is an open-ended, revolving credit product, which charges a daily interest rate of 0.82% and has no compulsory fees or faster payment fees. The price of a 28-day, £100 loan repaid on time is therefore around £23.The introduction of FlexCredit warrants particular consideration because it is one of very few (perhaps the only) examples of one of the largest lenders significantly reducing the prices that borrowers are charged for their loans.[206] Available data suggests that the product has, since its introduction, [✂].

4.64 CashEuroNet told us that its decision to launch FlexCredit arose from its loss of customers for loans with durations of around 15 to 17 days, because QuickQuid Payday was expensive relative to [✂] over this duration. It also told us that the decision to introduce FlexCredit was informed by market

[206] In each of the four scenarios considered in our analysis, FlexCredit was among the cheapest products, and was cheaper than all of the products offered by the three largest lenders.

research, which showed that its ‘target audience’ ranked loan cost, flexibility and perceived chance of approval as key drivers of payday loan choice.

4.65 Where other payday loan products have previously been offered with a head-line interest rate significantly below 30% per month or 1% per day, there is evidence to suggest that these lenders have been unsuccessful in attracting customers through these low prices (see paragraphs 4.76 and 4.80), and in many cases the price of the relatively cheap products have subsequently been increased, or the products have been withdrawn.[207]

4.66 Generally speaking, the introduction of the FlexCredit product does not to date appear to have resulted in the other major payday lenders responding by reducing their prices. For example, Speedy Cash has increased the price of its traditional payday loan and Flex Loan[208] since the introduction of FlexCredit. While Dollar has introduced a £5 promotional discount applying to all loans repaid on time, this offer was only open between October 2013 and April 2014. WageDayAdvance has introduced ‘FlexAdvance’, a new instalment loan product. However, this is priced significantly above CashEuroNet’s FlexCredit product: borrowers are typically charged 0.97% per day with a £15 optional faster payment fee (implying a 28-day, £100 loan repaid in one instalment would cost around £42 including the faster payment fee).

4.67 [✂]

4.68 [✂][209]

4.69 Figure 4.5 presents [✂]. Figure 4.6 compares [✂].

FIGURE 4.5

[✂]

Source: [✂]
Note: [✂]

FIGURE 4.6

[✂]

Source: CMA analysis.

[207] For example, Speedy Cash’s Flex Loan had an interest rate of 0.72% per day, but this was increased to 0.82% per day (equalling FlexCredit) in July 2013 and most recently to 0.95% per day. H&T withdrew its high street products for new customers in June 2013.
[208] See paragraph 4.50*(a)(i)*.
[209] [✂]

4.70 [✂]

4.71 [✂]

4.72 [✂]

4.73 The price cap is likely to influence the characteristics of the loan products that lenders offer, by affecting the relative profitability of different types of product or by making it more difficult to structure certain types of product in ways that comply with the structure of the cap. It is possible that certain types of product (and in particular certain combinations of loan duration and repayment structure) may no longer be viable as a result of the cap, and so the range of products on offer in the market may be reduced. Some examples of how lenders' product offering might be affected by the cap might include an increase in the use of daily interest rates,[210] a simplification of late fee structures,[211] a reduced incentive for lenders to offer very short-term loans[212] or loans of longer durations,[213] and a reduction in the use of running account products.[214]

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[210] Because the cap is applied per day of the loan, lenders may be discouraged from using traditional monthly interest rates which do not vary depending on whether a customer borrows for a full month or for just part of it. Instead, it may become more common to observe lenders imposing restrictions on minimum loan durations, or quoting customers daily interest rates. The FCA noted, however, that the lenders that remained in the market would still have sufficient flexibility to adopt their pricing and products (see the FCA, final decision the price cap, p20).

[211] Some lenders currently charge a number of different types of late fees, triggered by different defaulting behaviour (for example, immediate fees for missing a payment, further fees after a fixed period if the loan still has not been repaid, trace fees). By limiting the total fees that can be charged to £15, the scope for lenders to use multiple late charges will be greatly reduced.

[212] This could be the case if significant costs are incurred in making a loan, irrespective of the loan's size and duration (and so its expected revenue). For example, the costs of acquiring a customer via an affiliate, the administration costs associated with processing a loan and the cost of carrying out credit checks are all likely to be the same irrespective of the value or length of the loan. Because the cap level is set as a fixed proportion of loan amount and varies linearly with duration, lenders may find it difficult to recoup the disproportionately high costs incurred by relatively small loans within the bounds of the cap, and so may be disincentivised from offering such loans. There are, however, reasons to consider that an incentive will nevertheless exist for lenders to continue to offer small or short-duration loans. Specifically, this could be the case if there are marketing benefits associated with the simplicity or flexibility of a product offering that allows customers greater control over how much they borrow and how long for. Moreover, the possibility of customers returning to a lender for further loans implies that the expected revenue associated with a customer taking out a loan of limited value or duration may extend beyond that single transaction. We also note that the FCA found that 70% of customers who initially took out short loans subsequently took out longer loans, and that short and small loans are typically used by borrowers with better credit scores and are less likely to be paid late or to remain unpaid than longer and larger loans. The FCA concluded that its analysis showed that issuing short and small loans will still be profitable under the cap once it took into account that customers often return to the lender for longer and larger loans, and that customers currently getting short and small loans are more creditworthy (see FCA, final decision the price cap, p27).

[213] The viability of some longer duration loans may be affected by the cap on the TCC (ie the element that requires that lenders cannot charge customers more than 100% of the initial loan principal). In particular, the cap may make longer-term loans on which borrowers make little or no contribution to the loan principal until the end of the loan agreement unviable. Relating to this, the FCA commented in its consultation document that the incentive for lenders to offer loans of duration longer than six months was particularly likely to be reduced by the cap (See FCA 'Technical annexes, Supplement to CP14/10', p116).

[214] Customers with running account products that are making multiple drawdowns within the scope of the same running account agreement may be particularly likely to come up against the limit that the amount charged cannot exceed 100% of the credit limit or the maximum amount outstanding under the agreement. The cap may

Customer sensitivity to prices

4.74 We next discuss evidence on the extent to which payday customers have in the past appeared sensitive to differences in price between lenders, or movements in prices over time. We begin by setting out evidence from lenders' submissions on how customers have responded on those occasions where they have changed their prices in the past. We then discuss the extent to which the products that customers choose appear to reflect the relative prices of the different alternatives on offer.

Evidence from lenders' submissions on customers' responsiveness to price changes

4.75 We begin this subsection by considering evidence on customers' responsiveness to changes in headline prices, before separately considering responsiveness to late fees.

4.76 Several lenders' commentaries indicated that customers were not responsive to changes to headline prices, and that lenders charging relatively low prices had not been particularly successful in attracting new business. For example:

(a) [✂] told us that it increased its [✂] interest charge from [✂]% to [✂]%, in order 'to increase revenue as [it was] getting no appreciable marketing benefit by undercutting competitors on price'. It said that there were two main reasons for the weak response by customers to that change: [✂].

(b) Furthermore, [✂] told us that it increased its [✂] price after it 'looked at the market and … determined that [it] wanted to be competitive in that market but that there was room for some increase in price'.

(c) Similarly, H&T told us that media coverage suggested that all payday lenders were 'as bad as each other' and, therefore, customers did not understand the potential savings from shopping around. It told us that its efforts at being cheaper failed to 'gain any traction', despite charging significantly lower prices than some competitors.

(d) SRC told us that it did not think price was a key factor in customers' choice of product, mainly because of the relative urgency with which they required a loan. It did not believe it would get more volume if it lowered prices and that its interest-free loan offer had only led to a marginal pick-

therefore encourage lenders to move away from running accounts, or to place restrictions on the minimum value of the initial loan advance or the number of drawdowns that can be made. Relating to this, Elevate told us that the way that the total cost element of the cap was structured would force it to change its product from a running account into a multi-instalment product.

up in volume (despite the size of the discount that was offered, see paragraph 4.61).

(e) SRC also said that the absence of risk-based pricing arose partly because the lower rate offered to low-risk customers would not result in sufficient retention of customers to make the price reduction profitable. It said that this may be the result of relatively poor availability of price comparisons, compared with other financial products such as credit cards and auto loans.

(f) [✂] told us that it did not consider that 'the evidence is overwhelming that [price promotions have] an enormous impact' and that price promotions were therefore not a primary driver of its business. It told us that this was 'one of the reasons why [✂]'.

4.77 There was some indication that customers may be more responsive to increases in monthly interest rates above 30%. In particular, Dollar told us that the increase in Payday Express interest rates from 30 to 33% per month or part-month in September 2013 was reversed because [✂]. It told us that [✂]. It said that [✂].

4.78 Wonga told us that its internal analysis showed a relatively sensitive response by customers to an increase in its price from [✂] to 1% in June 2013. [✂]. It interpreted this price response as implying a price elasticity of [✂].[215] We noted the potential for variation in Wonga's applications over time for reasons unrelated to its own prices, which was not controlled for, and therefore did not consider that this estimate could be relied upon. Moreover, the price was advertised as 1% per day both before and after the price change, ie even when Wonga charged the slightly lower price of [✂]% per day. In addition, the price change was accompanied by a substantial increase in the representative APR (from 4,214 to 5,853%) which reflected not just the price change but also changes in Wonga's representative loan amount and duration. As such, any customer response that did take place may have been driven by a large perceived change in price despite the actual change being marginal.

4.79 In its response to our provisional findings, Wonga also pointed to evidence that [✂].[216,217] However, we did not consider that this provided evidence of customer sensitivity to price, or a willingness among customers to switch lenders in search of a better deal. This is because [✂].

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[215] [✂]
[216] [✂]
[217] Wonga's response to the provisional findings, paragraph 5.10.

4.80 We also consider evidence from lenders' submissions on the extent of customer responsiveness to late fees. Again the evidence that we saw suggested that customers were insensitive to changes. In particular:

(a) Wonga told us that it did not notice any difference in the take-up of loans following the increase in its late loan fee from £20 to £30, although it also told us that it did not track the response closely.

(b) [✄] said in an internal document that it [✄]. It told us that [✄].

(c) [✄].

(d) SRC, which increased its late payment fee substantially for both its Speedy Cash and WageDayAdvance products in November 2013, did not mention any significant impact on its volume following the price increase.

4.81 Finally, there was some evidence from the way that pricing promotions were used by payday lenders to suggest that certain groups of customers may be perceived as being more sensitive to prices than others. In particular, Dollar told us that when it increased its monthly interest rate from 25 to 29%, it applied the increase to new customers coming through lead generator or organic search channels, while excluding existing customers and customers coming from the moneysupermarket.com website, because that [✄]. We also observed a number of other lenders targeting discounts at customers using PCWs. Further, CashEuroNet told us that it offered coupons to customers when they indicated at point of purchase that they were considering a competitor's product (see paragraph 4.56*(b)*).

Analysis of customers' responsiveness to headline prices

4.82 In this subsection we consider the correlation between lenders' shares of supply and their prices in different borrowing scenarios, so as to understand the extent to which customers' choice of payday loan product in different scenarios at a particular point in time reflects the relative prices of the loans that are available.

4.83 We begin by examining lenders' shares of loan volume within our two main scenarios – a £100 loan taken out for 14 or 28 days and repaid on time.[218] For each scenario, we examine all loans in the transaction data that were taken out for the relevant amount and duration (or similar) and calculate the shares of total loan volume in the period 1 April to 9 June 2013 achieved by each

[218] See Appendix 4.2 for a discussion of the representativeness of these two borrowing scenarios.

product. This is then compared with the relevant price of the product. Appendix 4.4 provides further details of our methodology.

4.84 Figures 4.7 and 4.8 show the results of our analysis. There is some evidence to suggest that those products which were relatively low-cost in a scenario accounted for a greater share of the market – in particular, the proportion of loans of around 14 days which were accounted for by products with pricing structures which made them cheaper for short loan durations (such as those of Wonga and MYJAR) was greater than the shares of longer-duration loans accounted for by such products.

4.85 Nevertheless, in both scenarios we find that a substantial proportion of customers took out relatively expensive products despite the presence of cheaper alternatives. For instance, during the period, while customers seeking a loan of £100 for 14 days could pay £17 when borrowing from MYJAR, around half of all customers taking out a loan of similar amount and duration chose a product with a TCC of around £20 or more, and around a quarter of all customers chose a product with a TCC of £25 or more. Similarly, while the price of a £100 loan for 28 days lay between £16 and £25 for the seven cheapest products, a large majority (over [✄]%) of customers chose products with a TCC of more than £25, and more than a fifth of customers chose products with a TCC of over £35.

FIGURE 4.7

Price by market share for loans of £100 for 14 days (and similar)

[✄]

Source: CMA analysis.
Notes: [✄]

FIGURE 4.8

Price by market share for loans of £100 for 28 days (and similar)

[✄]

Source: CMA analysis.
Note: [✄]

4.86 One possible explanation for the observation that a substantial proportion of customers took out loans where cheaper alternatives were available is that some customers were unable to identify the best-value product for themselves. We discuss possible barriers to shopping around and switching which may lead to this result in detail in Section 6.

4.87 There are, however, other possible explanations, including:[219]

(a) Customers may be unable to choose cheaper products, because of the credit constraints that they face.

(b) Certain customers may prefer more expensive products because of the non-price features of those products, such as a lender's level of customer service, and whether the lender is an online or high street lender.

4.88 We consider each of these other possible explanations in turn below.

- *Customer responsiveness and credit constraints*

4.89 We considered the extent to which customers may choose more expensive products because they are unable to take out better-value loans, given their credit histories.

4.90 In order to test the extent to which credit availability may be driving the patterns that we observed in paragraph 4.84, we analysed variation in [✂] risk scores of different lenders' customers. These scores were available for customers of [✂]. Table 4.3 sets out statistics describing the distribution of [✂] scores for accepted loans for each of these products during the period January 2012 to August 2013.

TABLE 4.3 [✂] **risk scores for accepted loans by product, January 2012 to August 2013**

Lender	*Product*	*Mean*	*Median*	*Standard deviation*	*Minimum*	*Maximum*	*Range*	*Inter-quartile range*
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: CMA analysis.

Note: The interquartile range describes the range of all values excluding the top and bottom quartiles. This measure is useful when considering differences in the distributions of risk scores without the potential for those differences to be driven by a small number of outliers.

4.91 [✂].

4.92 We then assessed the relationship between different lenders' prices and their market shares for a subset of low-risk customers (defined as customers within the top decile of [✂] risk scores in the sample, corresponding to all customers with a score of at least [✂]). In general, we would not expect these low-risk customers to be constrained in the lenders that they could borrow from (or at least, we would expect a smaller proportion of these customers to be

[219] In principle, customers may also prefer products with higher headline rates if they anticipate a risk that they will default on their loan, and the products that they choose have lower fees in this eventuality. However, we note that this is unlikely given the limited extent to which customers appear to base their loan decision on late fees (see Section 6).

constrained in their choice of lender). The top panel of Figure 4.9 illustrates each lender's share of customers taking out loans for £100 for 14 days across all customers for whom [✄] scores are available, while the bottom panel shows those shares among only the top decile of low-risk customers. Figure 4.10 does the same for loans of around 28 days.

FIGURE 4.9

Prices by market share for loans of £100 for 14 days (and similar) among customers of all risk ratings (top panel) and low-risk customers (bottom panel)

[✄]

Source: CMA analysis.
Note: [✄]

FIGURE 4.10

Prices by market share for loans of £100 for 28 days (and similar) among customers of all risk ratings (top panel) and low-risk customers (bottom panel)

[✄]

Source: CMA analysis.
Note: [✄]

4.93 These charts show that a material proportion of customers continued to take out products that were significantly more expensive than others available on the market when we restrict our attention to low-risk customers (ie customers with high [✄] scores) that were unlikely to be constrained in their choice of lender. For example, Figure 4.8 shows that [✄] of these customers used [✄] when taking out a loan [✄], even though [✄] offered [✄] interest that is much cheaper. Figure 4.9 shows that [✄]% of low-risk customers taking out a loan for around a month took out a loan with [✄], even though [✄] offer products that were £[✄] cheaper for a £100 loan. This strongly suggests that the patterns that we observe cannot be fully explained by the credit constraints faced by customers.

- *Customer responsiveness and non-price characteristics*

4.94 We also considered the extent to which differences in the non-price characteristics of different lenders' products might drive the patterns that we observe. Specifically, certain customers may prefer more expensive products because of the non-price features of those products, such as the degree to which the product offers repayment flexibility, or a lender's quality of customer service.

4.95 Testing the extent to which this is the case is difficult, given that each lender's service will be unique in some way, and the difficulty in both quantifying the extent of any non-price differences that do exist and their value to customers. Notwithstanding this, we note that at their core, payday loans are a relatively homogeneous product (in that the underlying service received by all online customers is exactly the same – a deposit in the applicant's bank account).

4.96 One of the key dimensions across which payday loans differ is in terms of customers' ability to repay in instalments. However, we considered that a willingness among customers to pay more for the ability to repay in instalments was not likely to explain the substantial proportion of customers found in our analysis to choose relatively expensive products (as presented in paragraphs 4.84 and 4.85, and Figures 4.7 and 4.8), based on the following observations:

(a) For most products offering repayment by instalment, those instalments occurred at monthly intervals (eg QuickQuid Payday, the monthly Lending Stream Loan and Ariste's three-month Cash Genie Loan). Therefore, these products did not offer additional repayment flexibility relative to traditional payday loan products when the customer's borrowing requirements were for durations of one month or less, as was the case in the analysed scenarios.

(b) Those products that did allow for relatively flexible repayment on short-term loans (ie by offering either instalments that could be made more frequently than once a month, or at the discretion of the borrower[220]) had [✄] small market shares in the analysed scenarios.

(c) Those products that were relatively expensive but nevertheless had substantial shares of loan volume (eg [✄]) did not offer repayment by instalment, although we note that [✄].

4.97 Another key difference between the products of different lenders is whether they are offered online or on the high street. In order to assess the extent to which this might be driving the patterns that we observe, we replicated the analysis previously presented in Figures 4.7 and 4.8 for online products only in Figure 4.11.

[220] eg Speedy Cash Flex Account and Flex Loan, and the weekly Lending Stream Loan.

FIGURE 4.11

Prices by market share for loans of £100 (and similar)—online products only

[✂]

Source: CMA analysis.
Note: [✂]

4.98 We find a similar pattern to that observed previously: a material proportion of customers taking out online loans used products that were significantly more expensive than others that were also available online. For example, while the price of a £100 loan for 14 days from MYJAR was £17, [✂]% of online customers with similar borrowing requirements borrowed using a product with a TCC of around £20 or more (a relative difference in prices of over 18% for a £100 loan), and [✂]% of customers chose a product with a TCC of £25 or more (a relative difference in prices of over 47% for a £100 loan). Similarly, while a number of online lenders offered loans for 28 days with TCCs ranging from £20 to £30, [✂]% of customers chose products with TCCs of £35 or more and [✂]% of customers chose products with TCCs of over £45, between 1.5 and 2 times the price of some other online loans.

4.99 Next, we noted that if the reason that a relatively expensive product holds market share in one scenario is because it has a non-price characteristic (for example customer service, access to the product in the form of mobile apps and website functionality, ability to repay early, faster payment services, etc) that causes the product to be generally preferred by customers, we would not then expect to see that product 'lose' market share to other, considerably more expensive products in a scenario where it is relatively cheap.

4.100 However, the evidence suggests that this is not the case. In particular, Figure 4.10 shows that Wonga held [✂]% of total online loan volume in the 28-day scenario, while cheaper products PaydayUK and QuickQuid Payday held a combined share of online volume of [✂]%, [✂]. If demand is being driven by superior non-price dimensions of Wonga's product, then we would expect that in the 14-day scenario, customers would prefer Wonga (which would have both better non-price characteristics, and would be considerably cheaper) to these alternatives. However, we find that in the 14-day scenario PaydayUK and QuickQuid Payday continued to have a considerable share of online volume around [✄]% [✄].[221,222]

4.101 We also examined the relationship between market shares and price, restricting the sample to customers taking out their first loan from a given lender, to examine whether the patterns that we observed might be driven by customers deciding to go back to a more expensive lender on the basis of a previous positive experience. However, Figure 4.12 shows that relatively expensive products captured a share of first-time loans that was at least as high as when considering new and repeat customers together, suggesting that the patterns that we observe cannot be explained by customers' previous experience with a lender.

FIGURE 4.12

Prices by market share for loans of £100 (and similar) – borrowers who are new to the lender

[✄]

Source: CMA analysis.
Note: [✄]

4.102 Although we cannot discount the possibility entirely, taken together the evidence presented above suggests that the price dispersion we have observed is unlikely to be driven primarily by any differences that exist in the non-price characteristics of different payday loan products.

4.103 Wonga told us that even if the proportion of price-sensitive customers was limited, we had not considered if this might be sufficient to create a competitive constraint.[223] However, we draw our conclusions on the overall strength of the competitive constraint in the round, taking into account not just the proportion of customers which are price-sensitive, but also evidence on lenders' pricing behaviour, profitability and other factors in reaching our conclusions. The balance of evidence set out in Sections 4 to 8 clearly indicates that the competitive constraint on lenders' pricing is weak.

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[221] Conversely, if PaydayUK or QuickQuid had superior non-price characteristics we would expect them to have substantially higher shares in the 28-day scenario than they have.
[222] Wonga suggested an alternative explanation for this finding, ie that different customers would value different aspects of a particular product offering (Wonga's response to the provisional findings, paragraph 2.11(b)(iv)) and this may explain why PaydayUK and QuickQuid Payday continued to capture a significant share in the 14-day scenario when they are relatively expensive. While possible in theory, we considered it unlikely – and saw no evidence to support – that payday loans were horizontally differentiated in the way proposed by Wonga, and that heterogeneous customer preferences existed which could explain the findings. Instead, as set out earlier, we noted that at their core payday loans are a relatively homogenous product, and that the most significant differences between products (such as online/high street availability, and single/instalment repayment options) could not explain the patterns that we observed.
[223] Wonga's response to the provisional findings, paragraph 2.11(d).

Conclusions on pricing

4.104 Payday lenders have historically used a variety of different pricing structures, and the amount that a customer pays for a loan will usually consist of several distinct charges or fees. Among other factors, prices will typically depend on the desired loan amount, duration and instalment structure; whether the loan is repaid on time, extended or topped up; and whether the customer opts for faster payment.

4.105 Reviewing the price of a payday loan in the period prior to the introduction of the price cap, we found that there was a degree of clustering around a headline price of £30 for a £100, month-long loan. The lenders charging monthly interest around this level included some of the largest in the market. In addition, several products with prices that were above £30 for a £100 month-long loan nevertheless carried headline interest rates of approximately 30% a month or 1% per day. This clustering in prices has emerged over time as increasing numbers of lenders have increased their prices to this level.

4.106 Despite a number of lenders charging headline prices close to this average amount, we observe some significant variation in the prices that different lenders charged in a number of representative borrowing scenarios. For example, the difference between the cost of borrowing £100 for 28 days using the cheapest product included in our review and the most expensive alternative was £39. The extent of price dispersion was even greater in the event that a customer repaid their loan late.

4.107 Headline price changes were infrequent, and many lenders had either made only one change to their products' headline rate since 2008, or had never changed their prices. Price reductions were particularly uncommon. The most notable exception is CashEuroNet's introduction of its FlexCredit product (in 2013), which was priced significantly below £30 per £100. We have not seen other lenders responding by similarly reducing their own prices, and we note that in the past lenders which have offered headline interest rates significantly below 30% per month or 1% per day have generally been unsuccessful in attracting large volumes of new customers and have in many cases subsequently increased their price or withdrawn their product.

4.108 There is some evidence of competition between lenders taking place via the use of price promotions. However, the coverage of the price promotions used by payday lenders was generally limited. Among the largest lenders, the main exception to this is again CashEuroNet, for whom a higher proportion of customers (around a [✂] of new customers) benefited from significant discounts. In addition, before it closed its payday service, a significant number of customers searching for a loan via the PCW moneysupermarket.com were offered discounts by several lenders.

4.109 Customer demand appears unresponsive to variations in prices. Where lenders have changed their prices, this does not generally appear to have resulted in a significant customer response, and lenders that have offered substantially lower rates have not been particularly successful in attracting new business. There is evidence to suggest that customers may be particularly unresponsive to changes in late fees. In addition, we observe a material proportion of customers taking out loans that were significantly more expensive for their given borrowing requirements than similar payday loan products available on the market. The evidence suggests that the substantial shares of loan volume captured by relatively expensive products is not simply driven by the credit constraints faced by customers, or by any differences in the non-price characteristics of the different products on offer.

Profitability

Introduction

4.110 Having considered the evidence on pricing behaviour, we now consider the profitability of the 11 major payday lenders.[224]

4.111 By combining evidence on lenders' revenues and their costs, profitability analysis complements our assessment of lenders' pricing, helping us to form a view of whether an effective competitive process is driving prices down towards the costs of provision, or whether there are indications of shortcomings in the competitive process. Profitability analysis also provides one way of assessing whether prices are high compared with a competitive benchmark. We consider whether prices of payday loans are high relative to other forms of borrowing in Section 5.

The Guidelines

4.112 The Guidelines[225] set out how consideration of the economic profitability of the business activity being investigated may be used as an indicator of competitive conditions in the market.

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[224] For the reasons set out in paragraph 4.135 it has been necessary to exclude Cheque Centres from this analysis. At the start of our investigation the 11 major lenders included Ariste, CashEuroNet, CFO Lending, Dollar, Cheque Centres, Global Analytics, H&T, MYJAR, SRC, The Cash Store and Wonga. As at December 2014, three lenders (Cheque Centres, CFO Lending and The Cash Store) had left the market and one lender (Ariste) had announced its intention to exit.
[225] The Guidelines, paragraphs 114–120.

4.113 In practice, a competitive market would be expected to generate significant variations in profit between firms and over time as supply and demand conditions change, but with an overall tendency towards levels commensurate with the cost of capital of the firms involved. Firms in a competitive market would generally earn no more than a 'normal' rate of profit where the rate of return on capital employed (ROCE) for a particular business activity would be equal to the opportunity cost of capital for that activity. In competitive markets, characterised by free entry and exit, companies are expected in the long run to make profits that equal the minimum returns required by investors (the opportunity cost of capital). Hence returns that are persistently in excess of the cost of capital can be an indication of market power or a lack of competition in a market.

4.114 Differences between returns and the cost of capital may sometimes be explained by innovation and successful risk-taking by firms. Our Guidelines recognise that at particular points in time the profitability of some firms may exceed what might be termed the 'normal' level. There could be several reasons for this, including cyclical factors, transitory price or other marketing initiatives, and some firms earning higher profits as a result of past innovation, or superior efficiency.[226]

4.115 In measuring profitability, the Guidelines refer to the use of a meaningful measure of profitability, usually in terms of rates of return on capital, and refer to both return on equity (ROE) and ROCE.[227]

4.116 Our consideration of the profitability of payday lending comprises four sub-sections as follows:

(a) Market-specific factors: we begin by considering market-specific factors affecting the methodology adopted for analysing profitability in payday lending (see paragraphs 4.117 to 4.135).

(b) ROCE estimates: we then consider the treatment of asset values within the ROCE framework and set out our estimates of historic ROCE after adjustments for intangible assets (see paragraphs 4.136 to 4.147).

(c) Interpretation of ROCE estimates: next we consider the issues associated with interpreting the levels of profitability observed, and the estimation of the relevant cost of capital for payday lenders for use as a benchmark for assessing profitability (see paragraphs 4.148 to 4.185).

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[226] The Guidelines, paragraph 117.
[227] The Guidelines, paragraph 9.

(d) Finally, we set out our conclusions on profitability (see paragraphs 4.186 to 4.190).

Market-specific considerations for conducting profitability analysis in payday lending

4.117 In addition to the general considerations normally associated with conducting profitability analysis in market investigations, we sought to assess any industry-specific aspects of the payday lending market relevant to conducting such analysis. We identified four areas: *(a)* the time period analysed and how this relates to the industry life cycle; *(b)* the choice of profitability metric adopted; (*c*) the relevance of different business models to the analysis of profitability in payday lending; and *(d)* cost issues, in particular relating to measuring doubtful debt expenses.[228]

Time period analysed and industry life cycle

4.118 We analysed detailed information from the 11 major lenders and estimated levels of ROCE for the period 2008 to 2013.[229] Our approach to profitability analysis is set out in detail in Appendix 4.5.

4.119 Most lenders made no submissions regarding this approach. Wonga, Dollar and CashEuroNet raised concerns regarding the time period chosen and the developmental stage of the industry under review, which we discuss below.

- *Parties' views on the time period analysed and industry life cycle*

4.120 Wonga submitted that 'the significant competitive and regulatory changes which have occurred since 2012 mean that financial performance over the period 2008 to 2012 provides no meaningful insight as to the current state of competition in the market'.[230] Wonga commissioned a report from its economic consultants, AlixPartners UK LLP (AlixPartners), which examined the profitability of Wonga and the industry. AlixPartners stated that many aspects of Wonga's business model were novel or unproven at the outset and the performance of the business could have turned out very differently. AlixPartners said that we should therefore be more cautious about interpreting

[228] The doubtful debt expense is an item in the profit and loss statement for the relevant financial year that reflects the expected (and actual) value of debt that will not be recovered. The name and method of calculation of this expense can vary depending on the accounting framework used. For details on how this expense is calculated, see Appendix 4.5.
[229] Aggregated data for 2013 is based on the financial years ended July to December 2013 and January to June 2014.
[230] These comments were submitted in Wonga's response to our preliminary profitability analysis (Wonga response to the profitability of payday lending companies working paper, paragraph 1.1.9).

the results of profitability analysis in this sector compared with the more mature markets typically investigated.[231]

4.121 Dollar told us that historic levels of profitability achieved at a time when the industry was relatively immature were not likely to give an accurate picture of future profitability or to provide any meaningful indicator of whether such profits were high or exceptional.[232]

4.122 CashEuroNet said that in a new and rapidly developing sector, subject to fierce competition, one would expect to see both businesses failing and businesses making substantial profits. It told us that it would be very difficult to draw any meaningful conclusions about the state of competition in such a market based on such a wide distribution of outcomes (over a relatively short period of time).[233]

- *Our position on time period analysed and industry life cycle*

4.123 We considered these views in the context of the time period that we had analysed. Whilst the short-term credit sector – including payday loans – has been established in some form for many years, there are several elements of the payday lending business model which have been introduced more recently, including: the ability for customers to apply online, automated risk processing, rapid funding of customer accounts and collection via CPA. We recognised that the time period analysed may not incorporate either the full business cycle[234] relevant to these industry changes and/or the long-term effect of more recent regulatory changes (see Section 3). There was, however, clear evidence that the time period that we reviewed covered the full life cycle of the largest underlying asset of the business – a payday lender's loan book. We therefore took the view that the time period we had considered – from 2008 to 2013 – provided relevant insight into the functioning of the market.

4.124 We further considered that uncertainty over the likely outcome of investment did not prohibit effective profitability analysis. In a competitive market, innovative and efficient firms may earn superior returns on investments for a period of time. However, we would normally expect excess returns to be competed away as rivals introduce competing innovations and/or improve efficiency. We agreed with AlixPartners and Wonga that there had been uncertainty in the early part of the period over the likelihood of future success.

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[231] AlixPartners report, paragraph 3.1.11.
[232] Dollar's response to the provisional findings, paragraph 2.6.2(iii).
[233] CashEuroNet response to the profitability of payday lending companies working paper, paragraph 1.5.
[234] We noted that a full business cycle can be measured as either from peak to trough, or from initiation to ex-growth steady state (which is sometimes regarded as indicative of industry maturity).

This situation did not differ, however, from any other new project in any other industry subject to uncertain demand and/or supply conditions. We therefore took the view that the analysis undertaken provided relevant insight into the functioning of the market. We have sought to take into account issues relating to the relevance of innovation, successful risk-taking and the relative immaturity or maturity of the industry when interpreting the level of profitability observed (see paragraphs 4.148 to 4.175).

4.125 We therefore concluded that the period chosen and our overall approach to profitability analysis was valid. We note further that we have considered as full a time period as practicable by including data from financial years up to 30 June 2014. We have also considered trends in revenue, new lending and net profit for the nine months to September 2014.

Choice of profitability metric adopted

4.126 Dollar instructed economic and accounting firm FTI Consulting (FTI) to review the data that it had previously submitted to us.[235,236]

4.127 FTI said that it did not consider ROCE and ROE to be appropriate measures of assessing profitability in this investigation. FTI said these measures were only appropriate for capital intensive industries, and it considered that Dollar was not. It told us that [✂].[237]

4.128 Dollar argued that earnings before interest and tax (EBIT) was a more appropriate measure to use to evaluate profitability than ROCE[238] and submitted analysis from FTI comparing Dollar's EBIT margin on revised costs with the payday lending comparator companies used in our beta analysis (see Appendix 4.5, Table 71).

4.129 We found the use of EBIT margin as a basis for comparing lenders to be problematic for the purpose of our profitability analysis as we did not have a suitable benchmark for comparison. Without a suitable benchmark for levels of EBIT margin it was not possible to make meaningful comparisons with other markets, or to exclude the possibility that margin levels observed in the market as a whole might be the result of high prices, and might therefore include any 'abnormally high returns'. By contrast the examination of levels of ROCE is a well-established approach in profitability analysis and does not

[235] Our profitability analysis took place in a number of stages. Dollar's initial submission was in response to our financial questionnaire. For further details of our approach to profitability analysis see Appendix 4.5.
[236] Dollar's response to the provisional findings, paragraph 2.6.2.
[237] Dollar's response to the annotated issues statement and working papers, paragraph 6.3(iii-iv) and Appendix 9; Dollar's response to the provisional findings, paragraph 2.6.2(i).
[238] Dollar response to annotated issues statement and working papers, paragraph 6.3(iv-v).

suffer from this problem. In adopting a ROCE approach we recognised that it was important to accurately establish the inputs of returns calculations and be careful estimating the components of the weighted average cost of capital (WACC) benchmark so that subsequent comparisons could be made with confidence and provide valid insights into competition. Finally we observed that Dollar included ROCE calculations for its subsidiary MEM as a key performance indicator for reporting the performance of this business.[239,240] For further discussion of profitability metrics see Appendix 4.5.

Different business models

4.130 In evaluating the profitability of payday lenders, we have taken account of the different business models operating in the industry. The range of business models include: organic start-ups funded by venture capital (VC); organic start-ups with publically listed equity/public debt funding; and acquisition of established lenders, either by UK or international parent companies (which may or may not have been active in the payday lending or other credit markets in the UK or overseas). Where relevant, we have considered the implications of parent company charges levied by international parent companies on UK subsidiaries.[241]

4.131 We have also noted that some of the major lenders also offer 'non-payday' products such as pawnbroking, buying and selling gold, foreign exchange services and money transfer. Where appropriate, we have examined revenues and costs of payday lending disaggregated from overall levels of firm profitability.

Cost issues

- *Repeat lending*

4.132 There was evidence that levels of repeat lending were monitored by management using, for example, retention curve metrics,[242] and we recognised that the profitability of payday lenders was driven by a combination of initial loans to first-time customers and repeat lending to existing customers. Initial loans

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[239] Although Dollar noted that ROCE is not generally used internally by its business for assessing its performance/profitability.
[240] Dollar subsidiary MEM reported ROCE of 26% for the year to 30 June 2013 down from 105% the prior year. Report and Financial Statements 30 June 2013, page 2.
[241] We also noted that two of the three largest lenders and four of the smaller lenders originated from the USA/ Canada. The decision by an overseas lender to enter the UK market may have been undertaken to diversify the geographic risk faced by parent companies. The process undertaken for investment evaluation and hurdle rates for a strategy designed to diversify geographic risk may have differed from those used by a UK operator entering the market from scratch.
[242] Retention curves illustrate the extent to which borrowers are retained as repeat customers over time.

to first-time customers will not be profitable unless the high levels of customer acquisition costs observed for many lenders (see Section 7) are exceeded by interest and fee revenue received from the first-time borrower concerned. If a customer's initial loan with a lender is unprofitable due to high customer acquisition costs, the overall profitability of a lender will be dependent on the extent of repeat loans for which there is no (or a much reduced level of) customer acquisition cost.

4.133 We considered conducting profitability analysis which sought to assess the profitability of repeat lending as a subset of corporate profitability; however, we took the view that corporate profitability was the more relevant measure for our analysis. This was partly because corporate profitability could be calculated consistently for all of the major lenders. In addition, corporate profitability could be compared with the cost of capital for payday lending in aggregate and did not require the estimation of a separate benchmark against which to compare the profitability of repeat lending. Finally, on the basis of the information available to us, we noted that analysing the profitability of repeat lending would have required us to make a significant number of further, judgemental assumptions to split costs between new and repeat lending.

- *Doubtful debt costs*

4.134 We also considered issues in relation to the cost of default. Our analysis of lenders' costs showed that the doubtful debt expense was the most significant category of costs faced by lenders, and represented around 45% of total costs for all lenders in both 2012 and 2011. We were therefore careful to examine the extent to which provisioning policies were comparable between lenders. We looked in detail at the underlying assumptions and calculations of the doubtful debt expense for 2012 for the 11 major lenders. To aid our comparison of the policies used by lenders, we created an illustrative hypothetical loan book based on the combined loan books of the 11 major lenders at the end of their respective last reported financial years.[243] Our review of provisions policies indicated that in general terms the majority of lenders followed similar methodologies with the exception of four smaller lenders. We therefore made no adjustment to bad and doubtful debt costs contained in lenders' financial statements.

4.135 It was not possible to separate specific costs relating to payday operations from other costs in the case of Cheque Centres. Cheque Centres' submission included only doubtful debt expenses for its payday loan products. Other significant operating costs were therefore excluded, and figures for Cheque

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[243] Up to December 2012.

Centres were not comparable with other lenders in our analysis. We have excluded this lender from our analysis to avoid overestimating profitability levels for the major payday lenders.

ROCE estimates

4.136 We now consider the ROCEs of the major payday lenders. As part of this assessment, we consider the case for making adjustments relating to the replacement cost of assets and the potential value of intangible assets, before reaching our estimates of the economic ROCE. We set out the adjustments made to accounting data prior to adjustments for intangible assets in Appendix 4.5, paragraphs 62 to 109.

Treatment of assets within the ROCE framework

4.137 Our Guidelines recognise that evaluating profitability under a return on capital approach requires an economically meaningful value for the capital base which may not accord with the value ascribed in the financial records.[244] Hence it may be necessary to make adjustments to accounting data produced in line with UK GAAP if the historic cost of assets differs substantially from the 'replacement cost' or 'Modern Equivalent Asset Value',[245] which is a more economically meaningful measure for our purposes in most cases. In situations where the difference between historic cost and replacement cost would be likely to have a material effect on profitability calculations, our Guidelines state that we will consider whether replacement cost values can be derived reliably.

4.138 In the case of payday lending, we did not consider that adjustments to the book value of tangible assets were necessary. This was because fixed asset intensity is low due to the high contribution of IT assets with short asset lives, and the predominant use of leasehold sites by high street lending firms. Additionally the loan book, which is typically the largest asset on a lender's balance sheet, is characterised by a very high level of asset turnover and frequent revaluations via the provision for doubtful debt, both of which factors are likely to eliminate any material valuation distortion. Moreover, evidence

[244] The Guidelines, paragraph 13.
[245] These terms are used interchangeably to mean the current cost of acquiring assets which yield equivalent services to those currently used by the firm, based on the most efficient technology and optimal configuration. Source: The Guidelines, Annex A, footnote 5.

presented by lenders on asset values indicated a reduction over time in the price of IT systems in particular.[246]

4.139 Although evidence indicating that IT costs have fallen during the period might suggest that asset values could plausibly be revalued downwards, we have not made an adjustment and our ROCE analysis, which is based on the book value of tangible assets, can therefore be seen as conservative in this regard.

- *Treatment of intangible assets*

4.140 The second adjustment to accounting data provided for in the Guidelines[247] concerns the possible inclusion of intangible assets where the following criteria are met:

(a) The cost associated with creating the asset must comprise a cost that has been incurred primarily to obtain earnings in the future.

(b) This cost must be additional to costs necessarily incurred at the time in running the business.

(c) It must be identifiable as creating such an asset separate from any arising from the general running of the business.

4.141 We considered carefully parties' views on intangible asset categories and values relating to: customer acquisition costs; knowledge of the customer base; staff recruitment and training; regulatory costs; pre-incorporation costs; start-up losses; technology; channel relationships and 'know how'.[248]

4.142 Wonga, Dollar and CashEuroNet submitted views on the value of assets, as set out in Appendix 4.5. Having assessed possible intangible assets to include in our analysis on the basis of paragraph 4.140, we recognised and took account of costs relating to staff recruitment and training. Our detailed reasons for this approach are set out in Appendix 4.5. We conducted sensitivity analysis to assess the effect on ROCE of changing our approach to include additional intangible asset categories. Additional categories considered were: potential assets relating to customer acquisition costs; and potential assets

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[246] For example, Wonga told us that 'recent developments (for example, in relation to the quality of CRA data and the availability of loan management software) also serve to reduce certain entry and expansion costs compared with 2007 when Wonga entered (and the subsequent period of significant growth)'. Source: Response to annotated issues statement, paragraphs 7.29 & 7.37*(b)*.
[247] Criteria originally set down in the CC report *The supply of banking services by clearing banks to small and medium-sized enterprises*, March 2002.
[248] CashEuroNet told us that it had acquired an intangible asset of payday lending business 'know-how' from CashNetUSA for no charge in 2007. It told us that it believed this intangible asset would have been costly to develop and should not be excluded from calculations (CashEuroNet's response to the provisional findings, paragraph 6.5).

relating to knowledge of customer creditworthiness, which we assessed using the CRA data costs incurred by lenders. The levels of ROCE indicated by this sensitivity analysis were not sufficiently different to change our conclusions on profitability (see also paragraph 4.147).

Estimates of ROCE including intangible assets

4.143 Table 4.5 shows our estimates of adjusted ROCE for the major lenders based on capital employed including the intangible assets we have identified.

TABLE 4.5 **Adjusted ROCE including intangible assets, 2009 to 2013**

%

	2009	*2010*	*2011*	*2012*	*2013**
Ariste	[✂]	[✂]	[✂]	[✂]	[✂]
CashEuroNet	[✂]	[✂]	[✂]	[✂]	[✂]
CFO	[✂]	[✂]	[✂]	[✂]	[✂]
Dollar	[✂]	[✂]	[✂]	[✂]	[✂]
Global Analytics	[✂]	[✂]	[✂]	[✂]	[✂]
H&T‡	[✂]	[✂]	[✂]	[✂]	[✂]
MYJAR	[✂]	[✂]	[✂]	[✂]	[✂]
SRC§	[✂]	[✂]	[✂]	[✂]	[✂]
The Cash Store	[✂]	[✂]	[✂]	[✂]	[✂]
WageDayAdvance§	[✂]	[✂]	[✂]	[✂]	[✂]
Wonga†	[✂]	[✂]	[✂]	[✂]	[✂]
Weighted average ROCE	33	38	44	33	17

Source: CMA analysis.

*2013 includes financial years ended July to December 2013 and January to June 2014.
‡Based on Group figures.
†Includes AlixPartners fixed asset adjustment to group accounts.
§SRC and WageDayAdvance constitute one major lender.

4.144 Our analysis indicated that the weighted average annual ROCE of the major lenders in Table 4.5 ranged between 17 and 44% during the period 2009 to 2013.[249] The annual firm-level ROCE has varied between lenders and across the period from –175% to over 170%. The highest levels of returns for these major lenders were achieved in 2011. Profitability for the largest three lenders has generally been higher than smaller lenders and was also subject to less variation at between –18% and over 90% during the period 2009 to 2013. In 2013, of the nine major lenders for which we have data,[250] three[251] lenders were not profitable.[252]

4.145 Returns in 2013 were generally lower than in previous years, with seven lenders generating lower returns year on year and ROCE for 2013 averaging 17% compared with 33% in 2012. Factors contributing to lower levels of

[249] The lenders in Table 4.5 accounted for a share of supply of 80–85% of 2012 loan revenue, loan value and total loans issued (excluding rollovers). See Table 2.5.
[250] SRC and WageDayAdvance constitute one major lender.
[251] [✂]
[252] [✂]

ROCE in 2013 included: *(a)* a slowdown in lending growth (revenue growth in 2013 was around 5% compared with historic growth rates of 40% to over 100% a year for the period 2009 to 2012), *(b)* cost increases and *(c)* an increase in retained profits at most lenders. We also noted that the average level of 17% in 2013 was depressed by a large change in the performance of [✄]. Excluding [✄], the average ROCE for 2013 was 24%. We considered that the decline observed for [✄] was due to internal factors relevant to the company rather than indicative of an increase in competition from rivals. We noted in particular management comments regarding the [✄],[253] which indicated, in our opinion, a slower and less responsive operational approach than competitors.

4.146 Examining the trends in returns at a company level, our analysis indicated that:

(a) Ariste generated a ROCE of [✄]% in 2011, having entered the market in late 2009. Profitability [✄] in 2012, however remained [✄]%. In 2013 the company reported [✄] £[✄] million due to [✄]. In October 2014 Ariste announced a plan to exit the online lending business in the UK citing recent changes in the UK regulatory environment (see paragraph 2.100).

(b) CashEuroNet's ROCE averaged [✄]% between 2009 and 2013. The lowest ROCE achieved by CashEuroNet during the period was [✄]% in 2011 and ROCE [✄] in both 2012 and 2013. Our analysis of the most recent level of profitability indicates that CashEuroNet's ROCE in 2013 was supported by a strong increase in reported EBIT of around [✄]%. In spite of a [✄] of [✄]% in loan applications in 2013, CashEuroNet's 2013 revenue [✄]% as [✄].

(c) CFO Lending generated a ROCE of [✄]% in 2012.[254] Profitability was [✄] in 2013 at [✄]%, [✄] than the weighted average of the major lenders. CFO ceased lending in May 2014 and in August 2014 the FCA appointed a skilled person to review its collection practices (see paragraph 2.104).

(d) Dollar's combined ROCE averaged [✄]% for the period 2009 to 2013 (year to June 2014), with [✄] returns of around [✄]% for the first [✄] years of the period followed by [✄] in both 2011 and 2012. In 2013 (year

[253] [✄]
[254] The first year for which data was available due to negative equity balances in 2010 and 2011.

to June 2014) Dollar reported [✂]. The deterioration in Dollar's performance was due primarily to [✂] reduction in revenue from payday lending activities, which fell [✂]% year on year.

(e) Global Analytics delivered a [✂] trend in profitability and in 2013 generated [✂] ROCE, which at [✂]% was [✂] the average of lenders analysed.

(f) H&T generated ROCE levels of around [✂]% for the first [✂] years of the period, after which profitability [✂] and in 2013 ROCE reached [✂]%.[255]

(g) MYJAR generated [✂] ROCE levels of [✂]% in 2010 and 2011 after which profitability [✂] and the company reported [✂].

(h) There was [✂] of SRC's high street business and its online operation. SRC's Speedy Cash stores made a [✂] 2012, the second full year of operation, and while [✂] in 2013 ROCE was [✂]%. We attributed the [✂] of SRC's high street business to a lack of scale and to an inefficiently large average store size. [✂] WageDayAdvance generated ROCE levels of [✂]% for the four year period 2009 to 2012 and [✂] in 2013, to [✂]%, profitability [✂] the average for the major lenders. The company told us that the change in profitability in 2013 at WageDayAdvance was the result of complying with new regulations concerning rollover loans and CPAs.[256]

(i) The Cash Store entered the UK market in 2010 and generated [✂] of ROCE in both 2011 and 2012. We attributed the [✂] generated by The Cash Store to a [✂]. As at August 2013 the company operated 29 stores in the UK. The Cash Store entered administration in August 2014.

(j) Wonga's ROCE averaged [✂]% during the period 2009 to 2013. Wonga's returns were [✂] in the early part of the period before [✂] for both 2011 and 2012. Wonga's profitability was [✂] in 2013 with ROCE of [✂]% due to [✂]. The [✂] appeared to have been driven by [✂].[257]

- *ROCE sensitivity analysis*

4.147 We performed ROCE sensitivity analysis to explore the effect of including intangible assets in addition to the intangible assets we had identified deriving

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[255] H&T withdrew from single-payment one-month payday lending products in June 2013 and withdrew its online payday lending product in January 2014. H&T's personal loan product, introduced in September 2013, offers up to £1,000 repayable over up to 24 months. H&T personal loans granted for durations of 12 months or less are included in our terms of reference.
[256] Hearing summary, paragraph 20.
[257] Wonga response to the profitability of payday lending companies working paper, paragraph 2.3.11.

from staff training and staff recruitment costs. The results of our sensitivity analysis indicated that ROCE ranged from 16 to 47% during the period 2009 to 2013 based on a capital base including 100% of customer acquisition costs and costs relating to knowledge of customer creditworthiness.[258] The weighted average ROCE for the period was 32% including the additional intangible assets considered. The results of our sensitivity analysis were therefore not sufficiently different to change our conclusions on the levels of profitability observed.[259,260]

Interpreting the level of observed returns

4.148 We now consider the interpretation of the observed levels of returns by first discussing issues relating to the variation between lenders. We then consider the relevance of innovation to interpreting levels of observed profitability. Next we consider the relevance of successful risk-taking to observed profitability. We then discuss the outlook for profitability and the extent to which it is possible to conclude whether current levels of returns will persist. Finally, we discuss the benchmarks which we consider relevant when interpreting levels of profitability.

Variation in returns

4.149 In its response to our provisional findings, CashEuroNet raised concerns that comparing the ex-post profits of the three most successful entrants to the market with ex-ante required returns of investors reflected a survivorship bias.[261]

[258] Based on total CRA data costs incurred by lenders in the period.
[259] We noted that our use of CRA data costs in our sensitivity analysis rather than bad debt costs (as the basis on which to take account of intangible assets that might be associated with knowledge of customer creditworthiness) was consistent with the methodology adopted in the Home Credit market investigation. Final profitability analysis in the Home Credit market investigation included an intangible asset for 'knowledge of the customer base'. Our reasons for considering this category of intangible assets in sensitivity analysis, rather than our final ROCE analysis, are set out in Appendix 4.5.
[260] We noted the results of analysis by AlixPartners which indicated the average economic ROCE of 20 companies (comprising 17 lenders) operating a payday lending business was between [✄] and [✄]% for the period 2007 to 2012 (AlixPartners report Table 6.7 MEA 1 basis). The range estimated by AlixPartners was therefore slightly lower than the range we estimated in our sensitivity analysis. We noted two factors relevant for considering AlixPartners' analysis. Firstly AlixPartners' analysis incorporated additional intangible asset categories not included in our sensitivity analysis (including marketing costs and regulatory compliance and business continuity costs) and a higher value for the knowledge of customer creditworthiness intangible asset. Secondly AlixPartners' analysis did not include a capitalisation and amortisation adjustment and therefore understated profitability for the purposes of our analysis (AlixPartners report, p51, footnote 48). We noted overall that despite the incorporation of higher intangible assets and lower profits, the ROCE levels calculated by AlixPartners were above our consideration of the minimum level of returns required by investors.
[261] CashEuroNet's response to the provisional findings, paragraph 6.1.

4.150 Wonga argued that 'even where overall financial performance may be strong, variation between lenders is a strong indicator of vigorous competition'[262] and that the variation in ROCE performance was 'consistent with a competitive sector'. Additionally, Wonga said that 'the dispersion of financial performance is consistent with a market where firms are competing to develop the best business model to serve the customer'.[263]

4.151 We considered these views. We acknowledged that the aggregate profitability of all lenders under consideration was more reflective of the profitability of payday lending than a subset of the large three lenders. In this context we noted that our analysis was based on the weighted average ROCE for the 11 major lenders (see paragraph 4.144). We further noted that these lenders accounted for the majority of the number of loans issued by all the payday lenders included in Figure 7.1.

4.152 We noted that our estimation of the weighted average ROCE for the major lenders included companies which had either exited the market or announced an intention to exit, including Ariste, CFO Lending and The Cash Store.[264] As such our ROCE estimates included companies which had failed, in addition to the most successful companies. We therefore considered that we had taken the steps necessary to avoid the introduction of survivorship bias by examining the returns delivered by both successful and unsuccessful companies with the minimum level of return expected by investors.

4.153 We agreed that the variability of returns was a relevant consideration. Our analysis indicated that whilst there was a range of financial performance across the sector as a whole, the extent of variation among the largest operators was more limited, and levels observed for these operators were above our estimate of WACC[265] across the period, except for one lender in one year. We also noted that overall returns were higher than our estimate of the minimum level required by investors despite the reduction in the weighted average ROCE in 2013 relative to prior years. We considered that the presence of a very limited number of unprofitable lenders during the period did not indicate that the competitive process was working well.[266] Rather we concluded that the unprofitable lenders observed were earning negative returns because these firms either continued to lack scale as new entrants, or had experienced cost or strategic issues including IT problems or 'oversizing'

[262] Wonga response to the profitability of payday lending companies working paper, paragraph 1.1.8.
[263] ibid, paragraph 1.1.10.
[264] Cheque Centres has also exited the market but was not included in our ROCE calculations due to the reasons set out in paragraph 4.135.
[265] And in Wonga's case we also examined the level of returns delivered in comparison with VC targeted returns (see paragraph 4.182).
[266] We also noted that in 2013 one lender had moved into profit having historically generated negative returns.

the store base (building too many and/or excessively large stores). See Section 7 for further discussion of the conditions faced by new entrants.

4.154 We also noted that if there were a lack of competitive pressure on payday lenders, we might expect some of the resulting profitability to be dissipated through increased expenditure by lenders in customer acquisition channels (for example, in lead generator auctions). In this context, we noted the fierce competition (and consequentially high prices) observed to acquire leads and in pay-per-click advertisement auctions for payday-related search terms (see Section 7), and the high proportion of online lenders' costs accounted for by customer acquisition expenditure (see paragraph 7.44). Total expenditure on customer acquisition per new loan issued has increased substantially over the period, as the number of lenders active in the market has increased.[267,268]

Rewards for innovation

4.155 We considered that an element of Wonga's [✂] levels of ROCE in 2011 and 2012 might be explained by its position as an innovative early mover offering differentiated flexibility to customers in the growing online sales channel. During the early part of Wonga's existence it innovated via its website 'slider', daily pricing, the speed of lending decisions and mobile access. Wonga introduced its faster payment service to expedite the transfer of money to customers in October 2008.[269] CashEuroNet, Payday Express, PaydayUK and CFO Lending had all introduced this facility by April 2012. Wonga was the first lender to introduce mobile access to loans in January 2010. We did not consider, however, that the extent of innovation was sufficient to explain the full extent of the [✂] levels of ROCE observed for Wonga in 2011 and 2012.

4.156 We considered that market-changing innovation had not been a factor in driving the high returns observed for other major lenders:

(a) In Dollar's case, UK market entry was achieved via the purchase of established firms operating with traditional high street credit-scoring methods or the online distribution of traditional 'monthly' single payment loans.

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[267] It would also be logical for lenders to increase their spend on acquisition costs, at least for a time, if the overall rate of growth in the market was slowing yet the evidence was unclear and lenders were not achieving their volume objectives.
[268] In its response to our provisional findings (paragraph 3.25), Wonga told us that it considered that increasing customer acquisition costs were due to the intensification of competition (reflecting new entry and expansion).
[269] MYJAR offered expedited funds transfer from inception and began lending in March 2009.

(b) CashEuroNet established its UK business using proven operational methods from the USA and initially offered QuickQuid loans repayable in either one or two monthly instalments.[270]

4.157 Additionally we noted that other major lenders including Ariste, Global Analytics, SRC and The Cash Store established businesses in the UK having operated previously in markets outside the UK.

Successful risk-taking

4.158 We also considered whether the high returns observed for the largest lenders were compensation for downside risks taken at the time of investment in significant innovations. We did not, however, consider that this applied to the payday lending industry because:

(a) Investments have been incremental so that whilst initial investments may have involved relatively high risks, subsequent investments could be made conditional on the success of the first. The result of this approach was that less capital was at risk in the initial, more risky stage of significant innovation. There was evidence that the initial finance provided to Wonga was relatively modest and supplemented in later years as the business matured.[271]

(b) Lenders have typically invested in short-lived assets and there was no evidence that lenders have faced significant demand risk over the life of assets in which investment has been made.

(c) The expectation that returns would converge over time towards the cost of capital applies equally to innovative markets since high ex-post returns would provide an incentive for other companies to enter the market.

(d) The relatively low asset intensity[272] of the payday lending industry means that investment is scalable to changes in demand.

4.159 Taken together, we took the view that these factors suggested that high ex-post returns were not compensation for downside risks taken at the time of

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[270] CashEuroNet's Pounds to Pocket 12-month instalment product was launched in 2010. QuickQuid Flexcredit, a revolving credit facility, was launched in June 2013.
[271] AlixPartners report, paragraph 7.1.3(c).
[272] In its response to the provisional findings (paragraph 3.23(b)), Wonga argued that its low asset intensity reflected its high velocity of credit, relying on its ability to 'revolve' the credit to provide more loans. Wonga told us that even if we did not adjust benchmarks for the higher risk resulting from high velocity of credit, we should at least take this into account in our interpretation of the results. Wonga compared the provision of £100 loans of around or less than one month totalling £1,200 of capital at risk with an annual personal loan of £100. We noted, however, that personal loans typically had a minimum amount of £1,000 (see Appendix 5.1, Table 1) and that there would be circumstances in which the risk of a one-month loan would be less than the risk of an annual loan due to the time value of money.

investment, but rather indicated that prices were higher than could be explained by the level of costs observed, including the cost of capital for the major lenders.

4.160 We also considered that whilst investments made by the lenders under consideration had enabled a significant change to the dominant sales channel, the extent to which this investment had created a new market was open to debate. As such, conclusions about whether the industry was in steady state were of less relevance in this instance, unlike in markets where innovation had required high-risk large-scale, 'all or nothing' investment, which in turn could be clearly be considered to have created a new market (such as Movies on Pay TV).

Outlook for profitability

4.161 Several lenders submitted views on the outlook for profitability:

(a) In its response to our provisional findings, CashEuroNet told us that the FCA rules on rollovers and CPA would further negatively impact lenders' profits and returns on investment.[273]

(b) In its response to our provisional findings, Wonga stated that payday lending was in the growth phase of the industry cycle during the period 2009 to 2013 and that Wonga was an innovator, which indicated that greater weight should be placed on forward-looking profitability analysis.[274]

(c) In its response to our provisional findings, Dollar told us that we had not taken into account a number of current FCA initiatives and the potential consequences of those initiatives[275] and submitted that these matters were likely to mean that profitability levels in the industry were likely to decline further.[276]

4.162 We considered these views by *(a)* examining cost data for 2013; *(b)* analysing the trend in revenue and net profit for the period July to September 2014 (Q3 14); and *(c)* reviewing the internal profit projections for 2014 and 2015 of the six major lenders which were in a position to provide forecasts.[277]

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[273] CashEuroNet's response to the provisional findings, paragraph 7.1.
[274] Wonga's response to the provisional findings, paragraph 3.19.
[275] Including the impact on lenders' costs resulting from the FCA's announced thematic review on arrears and collection and the review of the significant use of s166 Skilled Person for numerous players in the industry, and the announcement by several providers (most notably Cheque Centres) that it was restricting its operations as a result of moving towards FCA supervision. (Dollar's response to the provisional findings paragraph 2.6.2 (iv).)
[276] ibid, paragraph 2.6.3.
[277] [✄]

4.163 From our review of 2013 data it appeared that there had not been a significant increase in regulatory costs in the context of the overall cost base of lenders. It appeared that if lenders had anticipated the introduction of the FCA's detailed rules on affordability and creditworthiness in April 2014, and the introduction of rules limiting rollovers and the use of CPAs in July 2014, any action taken had not significantly affected costs in 2013. We noted that three lenders ([✂]) had increased profits in 2013 compared with 2012.

4.164 Our analysis of the trend in the most recent financial data available indicated that the performance of the lenders under consideration was weaker than in previous years. A comparison of Q3 14 with Q3 13 for seven[278] of the major lenders showed that:

(a) whilst aggregate revenue and new lending was around 40% lower year-on-year, combined net profit for the period had dropped by around 30%;

(b) the Q3 14 aggregate net margin rose to 31% from 25% as a result of the different relative rates of decline in revenue and profit; and

(c) Profitability was likely to have been supported by an increase in the proportion of lending generated from repeat borrowing, which rose to 86% from 81% in Q3 14. We noted that further increases in profitability would not be possible if the proportion of repeat borrowing reached 100%, and that a strategy centred on increasing the incidence of repeat borrowing would not be a sustainable one.

4.165 We considered lenders' views regarding trends in the most recent financial performance:

(a) Wonga told us that the main reasons for the decline in net profit performance were higher costs and lower revenue due to a combination of regulatory measures and greater competition.

(b) By contrast, other parties did not cite competitive factors as having influenced performance, and noted the effect of regulatory changes:

(i) CashEuroNet told us that the factors affecting its financial performance were regulatory in nature [✂].

(ii) Dollar told us that changes had occurred as a result of new regulations imposed by the FCA which were mandatory across the industry. Additionally, changes had been implemented by Dollar in

278 Ariste, CashEuroNet, Dollar, Global Analytics, MYJAR, SRC (including Speedy Cash and WageDayAdvance) and Wonga.

response to ongoing dialogue with the FCA designed [✄], a key metric the FCA used to assess whether lending was affordable for the customer.

(iii) Global Analytics told us that the addressable market for its product was being reduced by the CPA limits and affordability measures.

(iv) MYJAR told us that factors affecting its performance in 2014 included [✄]

(v) SRC stated that the [✄] was due to the cap on the number of deferrals allowed and the CPA restrictions which had been in place from July 2014.

4.166 In the absence of any observed reductions in headline prices of products during the period (see paragraph 4.45) we took the view that relevant competitive factors were likely to relate to the introduction of new products, such as CashEuroNet's instalment product. Our review of data submitted by CashEuroNet indicated that whilst its revolving credit product, Flexcredit, may have taken market share from other lenders, it was also possible that growth in this product had been at the expense of CashEuroNet's single payment QuickQuid loan.[279] Additionally we considered that the decision by Wonga to cease television advertising on 21 June 2014 was likely to have contributed to reduction in new lending reported by Wonga. We therefore concluded that regulatory changes were likely to have been the major determinant of the observed trend, and that reduced financial performance did not indicate that the market was operating competitively.

4.167 Our review of lenders' 2015 forecasts indicated that there was a very high level of uncertainty among lenders over the level of future financial performance. Three lenders ([✄]) did not submit forecasts. [✄] told us it was unable to provide an estimate of profitability for 2015 [✄]. [✄] told us that its projections were subject to significant unknown factors and estimated that its forecasts could vary significantly in practice, by as much as 50%. Internal planning documents from [✄] indicated it expected to gain market share in 2015.

4.168 Considering the likely evolution of future profitability we acknowledged that revenue and returns were likely to fall following the price cap which was introduced on 2 January 2015. We considered three reasons for this.

[279] [✄]

4.169 Firstly, those lenders which had previously priced above the cap would now be operating with reduced prices and (unless they were to achieve a sufficient compensating increase in lending volumes) revenues would fall.

4.170 Secondly, the cap is likely to cause lenders which previously charged above the cap to tighten their risk thresholds, granting fewer loans to relatively high-risk customers. This is because the expected gains from lending to the highest-risk customers are unlikely to continue to exceed the expected costs (given the risk that they do not repay). This effect is likely to reinforce the increased regulatory focus on conducting effective affordability assessments. Modelling carried out by the FCA suggested that the cap could have a significant impact on the size of the market as a result. The FCA estimated that 7% of customers will no longer be able to obtain a loan from any lender.[280]

4.171 Thirdly, we considered that lower levels of revenue with the price cap in place might mean that some less efficient and/or less well-resourced lenders would exit the market. Based on the FCA's static modelling which assumed that firms would not change their business practices to operate profitably under the cap, the FCA had initially estimated in its Consultation Paper that five out of the eight larger firms for which it carried out its modelling exercise would be at risk of exiting the market in the presence of the proposed price cap.

4.172 The FCA subsequently revised its estimates in light of recent changes to lending volumes and estimated that more lenders may become unprofitable as a result of the price cap than previously estimated.[281] However, the FCA outlined several reasons why the static modelling is not reflective of the actual situation in terms of market participants[282] and that a higher number of lenders were likely to remain in this market than the model indicated. This was consistent with lenders' views collected during our investigation: while lenders in general supported the view that a number of less-efficient firms were likely to exit the market as a result of the cap, most lenders expected that a variety

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[280] See FCA 'Technical annexes, Supplement to CP14/10' p68, Table 7.
[281] See FCA, PS14/16: Detailed rules for the price cap on high-cost short-term credit, Box 1, pp67-68.
[282] The FCA pointed to five different reasons. First, the static model does not fully reflect firms dynamically changing their business to remain viable. Second, consultation responses, public announcements and discussion with lenders indicate that a significantly higher number of lenders are likely to remain in the market than the model indicates. Third, the model is based on the assumption the reduced level of lending at August 2014 will continue but the FCA considers that lending volumes will likely recover to some extent. Fourth, the model under a 'no price cap' scenario indicates that only four firms are at low risk of being unviable but the FCA noted that all eight of firms in its model are continuing to operate at present. Fifth, one high-street lender has stated publicly that it expects to continue to operate under the cap and has acquired several stores recently. (See Box 1, Annex 2 of Detailed rules for the price cap on high-cost short-term credit.)

of suppliers – large and small – would remain in the market following the introduction of the cap.[283]

4.173 Notwithstanding the reasons set out in paragraphs 4.169 to 4.172, we took the view that there could be scope for further cost reductions as lenders responded to the end of the period of exceptional market expansion and the effect of regulatory changes, including the price cap introduced on 2 January 2015. We noted in particular three areas where cost reductions could be possible. Firstly we considered that lenders had the option to examine efficiencies in internal costs in the light of market developments driving lower lending volumes. Secondly we noted the expectation that external costs, such as the cost of purchasing leads, could fall with the price cap in place.[284] Finally we considered that it was likely that one benefit of RTDS would be a reduction in impairment costs for participating lenders.

4.174 Additionally we noted that as well as the reduction in the number of loans granted the tightening of risk thresholds would be likely to lead to a reduction in the overall riskiness of the population of payday loan customers that continue to be approved for loans. The FCA noted that the price cap 'provides a 'bright line' backstop to ensure that it is economically unviable for firms to lend to customers with a high risk of non-payment'.[285] This effect might be expected to increase profitability, albeit relative to a smaller loan volume.

4.175 We concluded that whilst the price cap was likely to result in a fall in some lenders' revenues, there could also be some countervailing reductions in costs. Moreover, to the extent that profits do fall with the price cap in place, this would not demonstrate that the market was operating competitively.

Benchmark for profitability

4.176 In order to interpret levels of observed returns, it is necessary to compare profitability with an appropriate benchmark. Our Guidelines state that in assessing levels of profitability the CMA will have regard to its view of firms'

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[283] For instance, CashEuroNet told us that a number of small firms currently offered products priced below the cap, and that it was therefore unlikely that only three firms would remain in the market. It said that the key determinant of whether a lender survived would be the effectiveness of its credit models rather than its size (CashEuroNet response hearing summary, paragraph 9). Dollar said that it expected more than three or four lenders to remain in the market, because lenders' products would respond to the cap (Dollar response hearing summary, paragraph 4). Global Analytics said that it would [✂] (Global Analytics response hearing summary). Two of the smaller lenders that we spoke to (Elevate and Provident) told us that they intended to stay in the payday lending market in the presence of the cap (though Elevate said that the cap would cause it to change the rate of progression within its product, and would possibly cause it to eliminate some of the lower risk tiers – see paragraph 4.10) (Elevate response hearing summary; Provident response hearing summary).
[284] See paragraph 6.122.
[285] See FCA, PS14/16: Detailed rules for the price cap on high-cost short-term credit, page 70.

cost of capital. The CMA will generally look to the capital asset pricing model (CAPM) when considering the cost of capital, since this is a widely understood technique with strong theoretical foundations. However, the CMA will have regard to alternative models where appropriate.[286] In the light of views expressed regarding the appropriate approach to determining the cost of capital for payday lending, we considered both CAPM WACC and other potential benchmarks associated with VC financing.

- *CAPM weighted average cost of capital*

4.177 We have derived a pre-tax nominal WACC of 7.9 to 12.7% for the UK payday lenders under consideration using CAPM (see Appendix 4.5 for details). Most lenders made no submissions regarding this approach, though some lenders expressed concerns:

(a) [✂] said: 'we consider that the CAPM may not be appropriate to estimate the industry WACC due to the riskiness of the business'.[287]

(b) CashEuroNet observed that its US-based pre-tax WACC would be [✂]% using our UK tax rate assumption of 25% and argued that the WACC estimate should also include Advance America.[288]

4.178 We considered [✂]'s view (see paragraph 4.177*(a)*) that CAPM might not be appropriate due to the riskiness of payday lending business. We noted, however, that the cost of capital calculated under CAPM compensates investors for market risk, rather than the specific risk of a particular business activity. Since investors are free to diversify away specific risk by holding a balanced portfolio, it follows that investments should earn a return which compensates for their degree of market (systematic) risk.[289] We therefore concluded that CAPM was appropriate for calculating the cost of capital for payday lending and noted further that [✂] had historically undertaken [✂]. Separately we also noted that several other lenders had submitted WACC calculations used within their businesses, albeit these estimates overstated the cost of capital for our purposes due to the incorporation of factors to cover specific risks, including forecast risk and regulatory/legislative risk (see Appendix 4.5).

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[286] The Guidelines, Annex A, paragraph 16.
[287] [✂]
[288] Advance America, a US financial services company, was acquired by Grupo Elektra on 23 April 2012. See www.gruposalinas.com/News.
[289] Some shares/investments are more affected by market risk than others and this aspect of risk is captured by beta.

4.179 We recognised that including additional companies in the beta analysis could increase the accuracy of WACC estimates. Our review of beta data for Advance America indicated that our estimate of the median beta for our analysis was unchanged having included this comparator.

- *Consideration of other benchmarks*

4.180 We noted that there were differing views on the applicability of alternative benchmarks.

(a) Wonga argued that we must adjust for the risk of 'survivorship bias' and stated that this could be done by 'looking at the returns that venture capitalists require[290] on their successful investments so as to deliver overall returns for their portfolio consistent with the high risks they bear'.[291]

(b) CashEuroNet raised concerns over the use of a benchmark based on the long-term returns of VC funds, as these funds will include both successful and unsuccessful businesses.[292]

4.181 We noted that VC firms raise funds from external sources including institutional investors such as pension funds and insurance companies.[293] The cost of capital for these external investors would reflect the combined opportunity cost of not having invested in other asset classes such as equities, bonds, property and other alternative investments. The decision to undertake VC investment was likely to reflect a wish on the part of investors to introduce a further level of diversity and variance into their portfolios.[294] Just as equity investors were free to diversify holdings across equity markets, VC investors were free to diversify across different asset classes. We acknowledged, however, that to the extent VC assets were less marketable and divisible than

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[290] AlixPartners told us that it understood from Wonga management involved in the early development of the company that 'early-stage venture capital investment often stipulates a required return on equity investment assuming the business is successful, rather than modelling all cash flow scenarios that may materialise' and that 'this is consistent with initial finance being relatively modest and then supplemented a few years later as the business matures (which is what happened with Wonga, where significant fund raising took place in 2009)'. AlixPartners also submitted that 'Wonga itself does not have direct evidence on such expectations'. AlixPartners report, paragraph 7.1.3(c).
[291] Wonga response to the profitability of payday lending companies working paper, paragraph 1.1.13.
[292] CashEuroNet's response to the provisional findings, paragraphs 6.1–6.2.
[293] BVCA, *A Guide to Private Equity*, p16.
[294] We also noted that a portfolio approach is also often adopted by VC firms themselves in that those undertaking seed capital investment are typically multi-stage investors and the extraordinarily high risk/return ratio of seed capital deals are attenuated in being amortised across the total range of activities of the fund. See Dimov and Murray, *An examination of the determinants of the incidence and scale of seed capital investments by venture capital firms 1962-2002*, 2007.

listed equity, the required returns of VC investors might be expected to include a liquidity premium.

4.182 In order to consider the effect of any liquidity premium that might apply we examined evidence on internal rates of return (IRRs) targeted by the VC investors which had provided funding to Wonga.[295] Table 4.10 shows targeted returns of [✄]% for very high-risk early 'seed capital' dropping to [✄]% for aggregate, more substantive investment.[296] A comparison of these IRRs with our analysis of Wonga's achieved returns indicated that Wonga's profitability substantially exceeded targeted returns for the seven-year period 2007 to 2013.

4.183 We noted that Accel Partners had told us it historically had to wait an average of [✄] before it saw any return from an investment. It therefore seemed reasonable to consider how [✄] profitability might be expected to affect the weighted average ROCE for Wonga for the period 2009 to [✄]. Our analysis incorporating Wonga's projected [✄] profitability,[297] however, did not reduce the weighted average for the [✄] to below the targeted IRR benchmarks on which we had evidence.[298] Wonga was [✄]. It was not possible, therefore, to extend this analysis to analyse at what point in the future returns might be expected to fall, such that the weighted average reached Accel's IRR targets.

TABLE 4.10 **Comparison of Wonga's historic ROCE with VC targeted returns**

%

	Seed capital	*Aggregate investment*
VC money multiple targeted	[✄]	[✄]
Time period	[✄]	[✄]
VC target IRR (A)	[✄]	[✄]
Wonga's ROCE 2007 to 2013 % (B)	[✄]	[✄]
Difference % (B minus A)	[✄]	[✄]

Source: CMA calculations.

[295] The IRRs targeted by VC investors include a liquidity premium associated with the risk that VC assets might be less marketable and divisible than publically listed equity.
[296] For reasons set out in Appendix 4.5 paragraph 62 we considered that the lower benchmark was likely to be applicable to investment in Wonga from 2010 onwards.
[297] In its response to the provisional findings (paragraph 7.14), Wonga told us that it expected to generate an economic ROCE of [✄]%. Incorporating this figure into our analysis (albeit we considered that it underestimated profitability for the purposes of our analysis (see Appendix 4.5) suggested that the weighted average ROCE for 2009–2014 would be in the region of [✄]%, equivalent to [✄]% above the highest IRR target for which we have evidence. See Appendix 4.5 for further detail.
[298] In its response to the provisional findings (paragraph 3.17(c)), Wonga told us that VC investors typically sought to generate multiples of 5 or 10 times invested capital over a five- to seven-year time frame, resulting in a target for IRR for successful individual companies within the portfolio in excess of 100%. We noted that Wonga's view related to VC investors in general, rather than the specific investors which had provided early-stage funding to Wonga (AlixPartners report, paragraph 7.1.3c). We therefore took the view that the specific target IRRs on which we had evidence were the more appropriate metric to consider. This was because the evidence submitted by VCs that had provided funds to Wonga and the associated IRR targets were likely to take into account the anticipated risks and an evaluation of the specific returns opportunity presented by an investment in Wonga. By contrast, IRR targets relating to more general investment opportunities would be likely to include a range of anticipated risks and different contractual arrangements between VC investors and portfolio companies.

4.184 Turning to the overall funding of the lenders under consideration, whilst VC investors had participated in the industry, it was also the case that VC-funded lenders were in the minority. Two of the largest lenders (CashEuroNet and Dollar) and three of the other major lenders (Ariste, H&T and the Cash Store) were publically listed companies or were owned by listed parent companies. Given that VC investors were not the only investors in the companies under consideration, we considered that an approach which sought to factor in any significant imperfections of equity capital market funding was not warranted.

4.185 We therefore concluded that CAPM was an appropriate benchmark against which to compare the observed levels of ROCE generated by publically funded major lenders over the period. To the extent that a cost of capital calculated using CAPM did not incorporate the liquidity premium associated with VC assets, this could be taken into account by considering the IRRs targeted by VC investors. It did not appear, however, that if we were to increase the cost of capital to incorporate the higher hurdle rates[299] used by VC investors this would explain the levels of profitability observed.

Conclusions on profitability

4.186 The average annual ROCE of the major lenders included in our analysis ranged between 17 and 44% during the period 2009 to 2013. The average economic ROCE peaked in 2011 and has declined in subsequent years, although at 17% in 2013 remains above our consideration of the minimum level required by investors.

4.187 There was some variation in the profitability of larger and smaller lenders included within the major lenders analysed. The three largest lenders have earned high and in some cases exceptional returns over a significant part of the period 2009 to 2013. The profitability of the smaller lenders has been more variable, however six of the smaller lenders achieved returns in excess of the cost of capital for periods ranging from between one and five years. Two of the smaller lenders did not generate a profit during the period. We attributed the negative returns of these lenders to a lack of scale and to strategic issues rather than evidence that the competitive process was working well.

[299] We use the term ‘hurdle rate’ in a general sense to describe total IRRs targeted by VC investors rather than a specific rate which may be included in the contractual compensation arrangements for funds including: the negotiated management fee, terms relating to carried interest payments (performance related compensation which may be triggered by a company meeting a specific contractual hurdle rate) and capital contributions from managing partners.

4.188 There was some evidence that future profitability may be lower than recent levels, both because of a further contraction in revenues and new lending compared with historic rates, and due to regulatory changes which may increase costs and/or reduce revenues. We noted, however, that the most recent trend in net profit for the six major lenders for which data was available indicated that the aggregate net margin for the lenders analysed had increased by six percentage points to 31%.

4.189 We noted that Q3 14 profitability was supported by an increase in the proportion of lending made to repeat borrowers and a reduction in impairment costs. We took the view that there could be scope for further cost reductions if lenders responded to ex-growth market conditions and the constraint of the new price cap by seeking efficiencies in internal costs. We also noted the expectation that the cost of purchasing leads could fall with the price cap in place, and it was likely that the benefit of RTDS would be a reduction in impairment costs for participating lenders. Moreover, we concluded that should profits fall with the price cap in place, this would not demonstrate that the market was operating competitively.

4.190 We noted that profitability analysis in isolation may be insufficient to draw firm conclusions on the extent of competition in a market and should be considered in conjunction with other evidence on market outcomes.[300] We judged that the profitability analysis conducted, combined with the evidence of price stability despite new entry (see paragraph 4.45), and the observed high price of leads (see Section 7) indicated that observed levels of profitability were consistent with a lack of competitive pressure. We considered that our interpretation of the profitability analysis undertaken gave sufficient weight to factors which can result in returns above the cost of capital (even in a competitive market) including innovation and successful risk-taking. We therefore concluded that the levels of profitability observed were indicative of shortcomings in the competitive process.

Non-price competition and innovation in payday lending

4.191 Payday lenders' products differ not only in terms of prices but also with respect to other dimensions. As set out in the Guidelines,[301] 'prices and costs are not the sole indicators of the level of competition in a market. Poor quality, lack of innovation, or limited product ranges are prominent among other indicators of weak competition in a market'. In this subsection we discuss the extent to which we observe lenders competing for customers using non-price

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300 See also Section 6 in which we assess the extent and nature of rivalry between payday lenders, with a particular focus on the role played by payday loan customers in driving competition.
301 The Guidelines, paragraph 127.

variables. We begin by setting out evidence on the importance of different non-price product characteristics to customers. We then look at evidence of competition between lenders in terms of access to credit, repayment flexibility and customer service, in the period 2008 to early 2014.

The importance of different non-price product features to borrowers

4.192 As a guide to identifying which non-price characteristics of payday loans lenders are important to customers, we reviewed the following evidence:

(a) customer surveys investigating the factors that influence customers' decisions about which payday loan provider to choose;

(b) lenders' submissions on the non-price factors that are important to customers; and

(c) lenders' marketing and advertising strategies.

4.193 As part of our customer survey, we asked respondents to indicate the importance of various product characteristics in the choice of payday loan. 'Speed of getting the money' was cited as very or extremely important by 74% of the respondents, followed by 'being able to apply for the loan online' (for online customers) or 'in a store' (for high street customers) (67%) and 'ease of the application process' (63%). Other factors, such as the reputation of the lender, the total cost of the loan, repayment flexibility and the amount that customers could take out, were considered very or extremely important by a smaller (though still significant) proportion of the respondents.[302]

4.194 Consumer research carried out by lenders[303] similarly highlighted the importance to customers of speed, as well as flexibility and ease/convenience. One lender, CashEuroNet, submitted that because rapid availability of money was now provided by all the main payday lenders, it was 'not a driver of choice between different online payday loan options', citing a more recent survey (August 2013) which it said suggested that different factors (especially interest

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[302] TNS BMRB survey report, p91.
[303] For example, a survey commissioned by Wonga in March 2013 found that [✂]% of its customers indicated the most appealing feature of Wonga's products 'that it is faster than other lenders'. Simplicity and flexibility (ie short-term product) were indicated by respectively 39% and 38% of the customers. Similarly, research commissioned by [✂] in 2012 found that, together with the cost of loan, speed of process, ease and convenience and flexibility of the loan terms play an important role in influencing customers' choice. [✂]% of [✂] customers indicated speed of process as the most important driver of the provider choice (more than the customers who indicated the cost of loan as the most relevant factor, [✂]%). Ease and convenience and flexibility were the most important drivers chosen by, respectively, [✂]% and [✂]% of [✂] customers. Finally, research commissioned by the CFA also suggested that the speed with which the money is available is the most important attribute to customers (22% of customers), followed by clear explanations of charges and fee (16%), and being treated with dignity and respect (16%).

rate [✂]) were now more important drivers of product choice than speed within the UK payday loan market.

4.195 In its submissions, Wonga highlighted customers' responsiveness to the ability to control the level of debt, access the product around the clock on various devices, the speed of lending decisions and ability to manage the loans. Similarly, MYJAR submitted that the ease with which customers could access their account, the simplicity of its offering and the way the customers were treated when they needed help were the most significant factors that customers took into account.

4.196 We also reviewed lenders' responses to our market questionnaire in relation to their marketing and advertising strategies (see also Appendix 6.3):

(a) Wonga told us that the key messages emphasised in its advertising were control, flexibility, speed and the fact that Wonga always showed the TCC upfront. Some examples of texts used by Wonga in its advertising include: 'Cash loans you control', 'Short term loans on your terms', 'How much? How long? You decide', 'No hidden charges'.

(b) In its promotions, CashEuroNet has presented side-by-side comparisons with rivals' products. For example, Figure 4.13 shows QuickQuid's Pay Per Click campaign (May 2013)[304] which contained a comparison with Wonga's Little Loans. In addition to the representative APR, the comparison also stressed the differences between the two payday loan products in relation to: the fee for fast funding, the maximum amount of loan that new (and repeat) customers can borrow and the offering of a loyalty programme.

[304] This campaign was run during the OFT's consultation on referring the payday lending market to the CC.

FIGURE 4.13

QuickQuid's (CashEuroNet) May 2013 Pay Per Click campaign, with Wonga comparison

Source: Global Analytics.

(c) Zebit (Global Analytics) submitted some examples of its online pay-per-click marketing campaigns. Speed of process ('A Zebit cash loan is initiated in 4 minutes') and long-term repayment in instalments ('A Zebit cash loan ... allows flexible repayments up to 7 months') were key messages contained in those campaigns.

4.197 Finally, we considered the product characteristics recorded for each payday product on money.co.uk – the largest comparison website (at the time of our review) providing information on payday loans (see Section 2 for further details). In addition to the cost (APR), the website compared products in respect of the minimum and maximum amount of loan that could be taken out, and the maximum duration of the loan.

4.198 On the basis of this review, we identified three key areas which appeared particularly important to customers, and where non-price competition may take place: *(a)* access to credit; *(b)* repayment flexibility; and *(c)* customer service. Below we discuss the extent to which we have observed innovation or competition in these product dimensions in recent years.

Access to credit

4.199 Much of the innovation that we have observed in the payday lending sector involves providers facilitating customers' access to credit. The changes have taken various forms: *(a)* increased flexibility in the amount that can be borrowed; *(b)* faster access by speeding up the process to obtain the loan; or *(c)* making it easier for customers to access their credit.

4.200 A number of lenders have increased the maximum amount that customers can borrow using their products in the past five years. Lending Stream increased the maximum loan amount from £600 to £1,000 in November 2008. The Money Shop (Dollar) progressively increased the maximum loan size of its products, moving from £200–£250 to around £1,000 for new customers and from £350–£450 to around £1,000 for existing customers. Wonga also increased the maximum loan amount (in November 2009) for new customers from £200 to £400 and for existing customers from £750 to £1,000.[305] Wonga told us that this was a 'direct result of competition and customer demand' as at the time of the change other competitors were offering loans up to a maximum of £1,000.[306] Similarly, Dollar told us that it had modified its maximum loan to respond to the 'market advertising larger loan sizes' and to offer 'a maximum loan value in line with the competition'.

4.201 Increased flexibility has also been achieved through the introduction of facilities that allow customers incrementally to increase the loan amount up to some limit (for example, top-up facilities). There are examples of these facilities being made available both for standard-duration payday loans and for longer-term instalment products. This type of facility has been introduced in the period by Wonga,[307] CashEuroNet, Dollar, The Cash Store,[308] H&T and SRC. Some lenders ([✂]) told us that they were also considering offering a product with such characteristics. Wonga and CashEuroNet submitted that these facilities were launched in response to competition.

4.202 Innovations have also been introduced to expedite the process of approving and transferring money to customers.[309] The majority of lenders, including Wonga,[310] CashEuroNet, Payday Express, PaydayUK, CFO Lending,[311]

305 We have also observed one example of a lender increasing the flexibility of its loans by reducing the minimum amount that customers can take out. Specifically, in December 2009 Wonga told us that it reduced the minimum loan from £50 to £1 with the scope of giving customers increased flexibility and providing 'a more competitive offering'. An internal analysis carried out by [✂] suggested that one of the reasons explaining Wonga's high customer turnover was indeed its offer of smaller loan sizes.
306 Wonga also submitted that the increase in the maximum amount of loan was made possible by the improved capability of its lending platform which enabled it to risk-assess customers at higher loan amounts with improved confidence as to the customers' ability to repay the loan on time. This was evidenced by the reduction in the principal loss rates for existing customers which Wonga achieved by early 2009.
307 Wonga launched this facility in July 2009.
308 These facilities were available to customers who pay back at least 50% of the outstanding principal on an existing loan. Such loans are subject to The Cash Store's overall lending limits.
309 CashEuroNet submitted that speed of service was one of the main innovative features of online payday loans (p11 of its initial submission).
310 Since October 2008.
311 Since April 2012.

Global Analytics, Ariste, MYJAR, SRC[312] and The Cash Store, currently use Faster Payment Services (FPS)[313] to process funds transfer. CFO Lending told us that faster payments to customers became a key factor in the customers' decision on provider and that it began offering cash transfer through FPS in order to compete with other online services.

4.203 Among the nine major lenders offering online products in 2013, six introduced fees for the use of FPS in the period since 2008, namely Ariste, CFO Lending, Cheque Centres, H&T, WageDayAdvance and Dollar (for repeat customers of its Payday Express product). Three of these – Dollar, [✂] and Ariste[314] – later removed this fee. The three remaining online lenders introduced FPS without introducing a corresponding optional fee. For example, MYJAR told us that it had never charged a fee for this service since its inception in 2008. CashEuroNet told us that it introduced free expedited funding in 2010 and that this action was intended to provide a competitive advantage to attract both new and existing customers.

4.204 We have also seen various examples of lenders implementing changes intended to make it easier to access their payday loans. In particular, many lenders have introduced mobile access to payday loans,[315] have improved their website functionality[316] or have extended store hours/begun offering 24/7 availability.[317] SRC told us that in its view there was a significant migration from high street to online borrowing in the UK and that it was driven largely by mobile. It added that 50% of the people on its website were on a mobile device and, in this respect, the UK market seemed to be much further ahead than the USA.

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[312] Since June 2011.
[313] FPS is a payment service that reduces clearing time and enables payments made via electronic telephone banking, internet banking and standing order to be completed quickly.
[314] Ariste removed the fee from its Cash Genie product only recently (in late May 2014).
[315] TxtLoan has offered the possibility to apply for loans through SMS since its inception in 2008. Wonga introduced mobile apps in January 2010, followed by CashEuroNet [✂]. Wonga and CashEuroNet told us that mobile app use showed significant growth since their launch (for example, Wonga submitted that currently [✂]% of its loans were taken out via a mobile device).
[316] Wonga told us that it had initially launched a 'My account' section on its website which was limited to reviewing loan details and updating customer details. Greater functionality was subsequently added. This included, among others: checking eligibility to apply for additional credit or to extend loan, online early repayment and using online self-service tools to create repayment plan when customers are experiencing difficulties repaying.
[317] In 2011 CashEuroNet introduced the possibility for customers to apply for loans at weekends and bank holidays with no extra costs. CashEuroNet submitted that the weekend service was a competitive necessity, suggesting that other lenders already offered weekend funding and that the CashEuroNet offer was driven by the need to catch up with the competitors. Similarly, Dollar told us that in response to competitors' action it modified store hours to be open at times more convenient to customers, including weekends (Dollar told us that opening hours for individual stores changed on an as-required basis. A central decision was made in summer 2012 to open approximately 40 stores on Sundays from 10am to 4pm).

Repayment flexibility

4.205 Flexibility in repayment terms is another area where we have observed significant changes being made by payday lenders in the past few years. A key development has been the introduction by many lenders of the ability for borrowers to repay loans in instalments. Some of the instalment products – such as Pounds to Pocket (CashEuroNet), Lending Stream (Global Analytics) and KwikLoan (H&T) – were loans specifically designed to be repaid in instalments. Others – such as QuickQuid Payday Loan (CashEuroNet), FlexCredit (CashEuroNet), Speedy Cash Flex Account (SRC), Zebit Short Term Cash Loan (Global Analytics), Cash Genie/Cash Genie Loans – three-month loan (Ariste)[318] – allowed customers some flexibility in deciding whether to repay the loan in a single payment or in multiple instalments.[319]

4.206 Table 4.9 shows the date on which various instalment products have been introduced. H&T was the first to launch an instalment loan in 2003. CashEuroNet's QuickQuid product was launched in 2007 (initially allowing customers to repay in either one or two monthly instalments) and Global Analytics' Lending Stream two-month instalment loan (which could be extended to eight months) in 2008, followed by CashEuroNet's Pounds to Pocket 12-month instalment product in 2010, Speedy Cash Flex Account (SRC) in 2011 and Global Analytics' Zebit instalment product, Ariste's Cash Genie/Cash Genie Loans (three-month loan), Sunny (Think Finance) and FlexCredit (CashEuroNet) in 2013.

TABLE 4.9 **Instalment products – timeline of entry into the market**

2003	*2004*	*2005*	*2006*	*2007*	*2008*	*2009*	*2010*	*2011*	*2012*	*2013*
KwikLoan				QuickQuid Payday	Lending Stream		Pounds to Pocket's Instalment Loan	Speedy Cash Flex Account		Zebit's Instalment Cash Genie/Cash Genie Loans (3-month loan) FlexCredit Sunny

Source: Responses to CMA's market questionnaire.

4.207 Further changes were made to some of these products after their introduction, for example CashEuroNet's QuickQuid product was extended in November 2012 to allow customers to elect to repay over up to three monthly instalments, and the repayment term of the Lending Stream product was increased

[318] Launched in June 2013.
[319] QuickQuid Flexicredit and Speedy Cash Flex Account were both revolving credit facilities. While they cannot really be explained as instalment loans as the drawdowns and repayments could be numerous and varied throughout the time the customer has the account, they allowed customers to make periodic repayments.

from two repayments to four, five or six repayments (depending on loan amount) in March 2009.

4.208 CashEuroNet told us that the launch of its three-period loan option was triggered by the fact that a number of competitors ([✄]) already offered longer-term products and this suggested that 'a longer term loan would be favoured by some customers'. Similarly, Ariste indicated that following the strategy adopted by competitors was part of the rationale for the launch of its instalment product. Global Analytics submitted that its Zebit instalment product was launched (in June 2013) because it saw the market opportunity as there were relatively few established competitors offering instalment products.

4.209 A number of other lenders told us that they intended to launch instalment loans or focus their strategy on this type of product:

(a) Wonga told us that [✄].[320] [✄].[321]

(b) [✄].

(c) Elevate said that its intention was to withdraw the payday-like products and to market only instalment loans and lines of credit products, as it did in the USA.

4.210 SRC told us that the US market had evolved towards instalment products in recent years. While five years ago the majority of its business in the USA was generated by traditional payday loans (more precisely, two-week loans because people were paid biweekly in the USA), currently most of the loans issued by SRC are instalment loans of varying terms.

4.211 Maximum and minimum loan durations represent another important dimension across which lenders' offerings differ. MYJAR increased its loan duration from 7 to 15 days in February 2011, and later in July 2013 from 15 to 18 days. It told us that these changes were driven by the analysis of customer repayment patterns which indicated that a longer-term product would suit customers' need better and allow more flexibility in ensuring that they would be able to repay on time. WageDayAdvance told us that it was considering the possibility of extending the loan term and providing customers with longer-term repayment options.[322] We also observed examples of lenders reducing the loan minimum duration, eg Wonga decreased the minimum loan term from

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[320] Wonga has recently launched an instalment product in pilot.
[321] [✄]
[322] It told us that WageDayAdvance would offer the same loan terms as SRC did.

five days to one day (in November 2009),[323,324] and Payday UK (Dollar) and Payday Express (Dollar) reduced the minimum loan duration to seven days ([✂]).

Customer service

4.212 Our customer research suggests that existing payday loan customers are likely to attribute importance to their 'experience' with a particular lender, especially given concerns about the reputation of the market (see paragraph 6.42). This is likely to create an incentive for lenders to invest in customer service, given the importance to most payday lenders' business models of repeat custom.

4.213 We saw evidence that lenders invested in customer service as a means to enhance the customer experience and retain customers with a good repayment record. For example:

(a) Wonga told us that it had taken several actions in order to improve the quality of its customer service since it had launched its Little Loans product. It mentioned, for example, an increased number of customer staff, live online customer services and improved customer contact numbers (more clarity and removal of expensive 0871 numbers).

(b) CashEuroNet said that it was the first company to have 24/7 customer service and considered the customer service it provided through a call centre to be better than that offered by other lenders.

(c) Other lenders, such as [✂],[325] The Cash Store,[326] SRC[327] and MYJAR,[328] emphasised that they continuously invested in customer service as this was an important factor of differentiation between lenders.

4.214 Related to this, we were aware of some evidence to suggest that many customers were happy with the service that they received from payday

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[323] In discussing the rationale for this change, Wonga said in an internal document that: 'In order to prove to journalists, regulators and customers that we are completely flexible we want to be able to offer £1/1 Day loans'.
[324] [✂]
[325] [✂]
[326] The Cash Store told us that it tried to differentiate itself from other payday lenders through superior customer service and 'the open and welcoming environment'. It also said that it believed that the overall experience it offered its customers was superior to the competitors'.
[327] SRC told us that customer service was a key competitive dimension and its customers were paying a premium because they acknowledged the high-quality service provided by SRC.
[328] MYJAR told us that it focused its investment 'around service and treating the customer right'. It added that its business culture and approach was to try and 'give consumers an experience that they would not ordinarily expect from a financial services company, let alone something that is perceived as a payday lender, and see how they respond. And basically, through the service proposition, as opposed to the price proposition, see if we can actually build scale.'

lenders. For example, the consumer survey carried out by the University of Bristol's Personal Finance Research Centre found high levels of satisfaction among payday borrowers with the customer service received from lenders. Wonga highlighted the relatively high net promoter scores that it achieved compared with those of other financial services providers. A significant proportion of customers responding to our survey who had taken out multiple loans, but had only ever used one lender, reported having done so because they were happy with the service provided.

4.215 We were also aware, however, that the serious problems identified by the OFT in its compliance review[329] and others about irresponsible lending, and a lack of compliance with lenders' regulatory obligations, clearly indicate that not all payday loan customers have benefited from good customer service (see Section 3).

4.216 As discussed in Section 3, under section 25 of the CCA, the OFT had a duty to ensure that licences were held only by businesses that were fit to hold them (known as the 'Section 25 Test'). In March 2010, the OFT published its Irresponsible Lending Guidance.[330] This guidance set out the expectation that lenders will conduct a reasonable assessment of affordability and monitor repayments. If customers fall into difficulties with their repayments, the lender is expected to show forbearance in resolving the problem. These principles and the accompanying expectations of firms have been brought forward into the new regulatory framework under the FCA. In addition to the CCA, the FCA has made further rules for high-cost short-term credit lenders (including payday lenders) and debt management firms (see Appendix 3.1 for further details). These new CONC rules and guidance have applied to firms carrying on a consumer-credit-related regulated activity since 1 April 2014.[331]

Conclusions on non-price competition

4.217 The evidence we discussed above suggests that lenders have on a number of occasions introduced new products or made changes/innovations to their products in recent years. We noted in particular that:

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[329] The OFT undertook a review of compliance by payday lenders, publishing its Final Report in March 2013. This highlighted a significant degree of non-compliance with consumer credit legislation and OFT regulatory requirements.
[330] www.oft.gov.uk/shared_oft/business_leaflets/general/oft1107.pdf
[331] In order to allow firms time to become familiar with the new structure and style of rules and guidance, the FCA allowed a six-month transitional period. During this time, if a firm was able to demonstrate that it had acted in accordance with CCA requirements and OFT guidance, the FCA would not take action against it in relation to the equivalent new rules.

(a) A number of lenders launched credit products or introduced features that allow customers to draw down further funds during the term of a loan.

(b) Over the years lenders introduced faster payment services, and these are now offered by the majority of providers. Some who charged an optional fee for this service have since removed it.

(c) Instalment loans became increasingly available through the period reviewed, and a number of lenders introduced either loans specifically designed to be repaid in instalments or the option to do so.

(d) Lenders invested and took actions to ensure compliance with the new regulatory framework and improve their customer service. Many payday customers reported being happy with their experience with their lender, although this must be set in the context of the findings of the OFT in its 2013 compliance review mentioned above and discussed further in Section 3 and Appendix 3.1.

Conclusions on market outcomes

4.218 There is evidence from the outcomes that we have observed in the payday lending sector to suggest that lenders compete on certain non-price aspects of the product offering, and that some lenders seek to provide good customer service in order to retain borrowers. Related to this, reported levels of satisfaction among borrowers with the service provided by some payday lenders are relatively high, though these should be considered in the context of the serious problems identified by the OFT in its 2013 compliance review (see Section 3).

4.219 In a well-functioning market, as well as seeking to offer customers good customer service and to improve the non-price dimensions of their products, we would also expect lenders to compete on prices.[332] However, our analysis of lenders' pricing behaviour indicates that there are significant limitations in how effective competition between payday lenders on prices has been, and that the competitive constraint that lenders face when setting their prices is weak.

4.220 In particular, payday loan customers can face a wide range of possible prices (particularly if they settle late) and many customers take out loans that are significantly more expensive for their requirements than others potentially

[332] Despite some differences in the non-price features of lenders' products, we note that at their core, payday loans are a relatively homogeneous product (see paragraph 4.95) and prices should be therefore an important dimension along which lenders compete.

available to them at the time. Aside from a small number of relatively recent developments, there is little evidence of lenders actively using the price of their loans to attract customers over the past six years, and in general customers appear insensitive where lenders have offered lower prices. The apparent weakness in the constraint that lenders face when setting their prices is consistent with our profitability assessment, which shows that the largest lenders have earned profits significantly above the cost of capital over much of the past five years, although we have observed significant variation in the level of profitability, both between lenders and over time.

4.221 In the next three sections, we seek to understand the causes of these market outcomes, by examining the potential constraints on payday lenders' pricing and any factors that may be inhibiting the effectiveness of these constraints:

(a) In Section 5, we consider the constraint on payday lenders' pricing from competition from other forms of credit, as well as setting out our definition of the relevant market.

(b) In Section 6, we examine the extent to which payday lenders' prices are constrained by customers shopping around for a better deal, or switching to a lender with a superior product offering.

(c) In Section 7, we consider the competitive constraint on established lenders from the prospect of new entry, or expansion by smaller lenders.

5. Market definition and the constraint from other forms of credit

Introduction

5.1 In this section we set out our analysis of *(a)* the competitive constraint that payday lenders face from providers of other forms of credit, and *(b)* whether competitive conditions vary for different groups of customers. In light of this assessment, we set out our conclusions regarding the 'relevant market' – a task that flows from the statutory questions that this investigation is required to address.[333]

5.2 As set out in the Guidelines, defining the market helps to focus on the sources of any market power and provides a framework for the assessment of the effects on competition of features of a market. It facilitates our understanding of the key competitive constraints which may be faced by suppliers within the market.

5.3 We take as our starting point the definition of payday loans that is set out in Section 2: short-term, unsecured credit products which are generally taken out for 12 months or less, and where the amount borrowed is generally £1,000 or less. The first question that we then assess in this section is the extent to which payday lenders are constrained by the threat that customers will use other types of credit that fall outside this definition (such as credit cards or overdrafts) instead of payday loans. This assessment allows us to draw some conclusions on whether these other products should be included within the relevant market.

5.4 We then look at whether distinct groups of payday loan customers exist such that different classes of payday lenders face different competitive conditions. Specifically, we discuss competition between online and high street lenders, before looking at whether the competitive constraints facing lenders vary materially between different local areas. Understanding any market segmentation of this type sets the context for our examination of the effectiveness of competition between existing payday lenders to attract customers in Section 6, and the competitive constraint exerted by new or expanding providers in Section 7.

[333] The 'relevant market' is defined in the Act to mean the market for the goods or services described in the terms of reference given to the CC for investigation. The market definition(s) used by the CC need not correspond with the 'relevant market(s)' as used in the Act (see the Guidelines). In this section, we discuss the appropriate market definition for this investigation.

Competition from other credit products

5.5 We begin by assessing the extent to which providers of other types of credit product are likely to impose a competitive constraint on payday lenders. We discuss:

(a) how the main characteristics of payday loans compare to the characteristics of other credit products;

(b) evidence on the extent to which payday loan customers have access to other credit products and, if they have some access, the extent to which credit is available via these alternatives when they take out a payday loan;

(c) evidence from payday loan customers on their perception of payday loans and alternatives, and whether they had considered (or would consider) using other credit products instead of taking out a payday loan; and

(d) evidence of payday lenders and other credit providers competing with each other for customers.

5.6 We recognise that the consumer credit sector, like many we consider, is dynamic with new products being regularly introduced, each with its own particular characteristics. At the edges, this may lead to a degree of blurring between product definitions. However, in the light of the evidence that we have seen, we are satisfied that the broad distinctions that we have drawn between different classes of credit product allow us to capture the spectrum of credit alternatives that are on offer to customers, and to understand the competitive constraint that different classes of credit products impose upon each other.

Product characteristics

5.7 Although not conclusive, significant differences between the characteristics of a payday loan and another credit product may suggest that customers would be less likely to consider that other product to be a suitable alternative to a payday loan, in turn making it less likely that the other product would impose a competitive constraint on payday lenders. For example, our survey showed that speed of access is an important aspect in customers' decisions to use payday loans.[334] Given this, other credit products which do not offer similarly

[334] Research into the payday lending market report – results of quantitative and qualitative research undertaken by TNS BMRB, p90.

rapid access to funds are unlikely to be seen by many customers as an attractive alternative to payday loans.

5.8 Based on our review of the products on offer, we identified the following as being some key observable characteristics of payday loans:[335]

(a) Amount of loan – this is typically less than £1,000.

(b) Loan duration – this is typically a month or less, but can be up to a year for some products, particularly instalment products.[336]

(c) No need to provide security – payday loans are unsecured loans.

(d) Payment and repayment method – when customers take out a payday loan online the loan amount is deposited in their bank account, making the money available for paying bills and withdrawing as cash. With high street payday loans customers can receive the funds in cash or as a credit to their bank account. Loans are often repaid through the use of CPAs and customers of some high street lenders (eg the Money Shop) can repay loans in cash in-store.[337]

(e) Speed of application, approval and transfer – successful applicants generally receive the funds on the same day, often within an hour (or less) of their application. Customers using high street payday lenders can receive the cash immediately after approval.

(f) Ability to roll over loans – many payday loan products allow customers to roll over their loan. The exact terms on which these facilities are offered, and the terms used to describe them, vary, but the common effect is to allow the customer to extend the duration of their loan beyond the originally agreed repayment date. This characteristic of payday loans has become less pronounced in light of the FCA's decision to limit the number of rollovers on an individual loan to two (see paragraph 3.14*(d)*).

(g) Top-up facilities – some payday loan products allow the borrower to increase or top up their loan before the end of the loan term.

5.9 We then investigated the extent to which other credit products shared these characteristics, looking at credit cards, overdrafts (authorised and unauthorised), credit union loans, home credit, logbook loans, pawnbroking,

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[335] This list is not exhaustive, and will not reflect every characteristic of payday loans that customers might find important. Nevertheless, we consider that it serves as a useful basis on which to compare the key attributes of payday loans to other credit products.
[336] Rollovers and refinancing may also result in the extension of the effective loan period of shorter-term loans.
[337] www.moneyshop.tv/short-term-loan-FAQ/.

peer-to-peer lending, personal loans and retailer credit. Full details of this analysis are presented in Appendix 5.1.

5.10 Our review showed that credit cards and overdrafts shared a number of characteristics with payday loans. Credit cards and overdrafts could be used to borrow similar amounts, had similar payment and repayment methods and were also unsecured. They could also provide facilities similar to rollovers and top-ups, so long as the customer was able to borrow more within agreed credit limits. Customers with an existing credit card or overdraft facility could also access funds immediately (eg by making a purchase by card, or by withdrawing cash from an ATM).

5.11 Credit cards and overdrafts differed from payday loans in terms of the period over which credit is paid back to the lender. With credit cards, customers are only required to pay back a minimum amount every month, rather than the whole outstanding debt. Authorised overdrafts typically run over an extended period and can extend indefinitely. Unauthorised overdrafts typically cover a significantly shorter period – for example, Santander told us that the average time a customer spent in unauthorised overdraft was three days.

5.12 Other credit alternatives shared fewer characteristics with payday loans. Of the other products we considered, credit union loans and retailer credit appeared to share the most similarities. Credit union loans involved similar small, unsecured loans which are paid and repaid through bank accounts, offered top-up facilities and are available for shorter terms (including in some cases one-month loans). However, they sometimes could not be obtained quickly and did not offer the ability to roll over/refinance the credit. In addition, a customer would need to meet the membership criteria of a particular credit union in order to be able to borrow from them. Retailer credit could involve borrowing similar unsecured small amounts and the funds could be made available quickly. However, the credit had to be spent with a specific retailer and the payback period could be longer than for payday lending, as repayment generally operates in a broadly similar way to a credit card.

5.13 We also considered the characteristics of guarantor loans, such as those offered by Amigo Loans and UK Credit Limited. We found that these products differed from payday loans in some key respects – the amount of a guarantor loan is typically much higher (an average of £[✄] for Amigo Loans), the duration is longer (a minimum of 12 months,[338] although it could be possible to repay early), they are not paid as quickly (typically the application process

[338] Amigo Loans told us that the average loan duration was over three years.

can last a few days)[339,340] and the loan is paid to the guarantor, rather than the borrower.

5.14 We also looked at the relative cost of borrowing using a payday loan compared with borrowing using other credit products. We considered that the larger were any price differences between payday loans and other types of credit, the more likely there were to be significant differences in the characteristics of those products.

5.15 Our analysis, set out in Appendix 5.2, compared the prices of payday loans with other credit products in the following four scenarios:[341]

(a) A customer takes out a £100 loan for 28 days and pays back the loan on time.

(b) A customer takes out a £100 loan for 14 days and pays back the loan on time.

(c) A customer takes out a £100 loan for 28 days and then rolls over the loan for 28 days.

(d) A customer takes out a £100 loan for 28 days and pays back the loan 11 days late.

5.16 We found that borrowing using a payday loan was typically significantly cheaper than using an unauthorised overdraft (for example, a median cost of £29.25 per £100 for a 14 day payday loan compared with £72.50 for an unauthorised overdraft of similar duration and amount).[342] Payday loans were, however, generally substantially more expensive than the other forms of credit considered under all scenarios, apart from home credit. Borrowing using a payday loan was typically cheaper than using home credit in Scenarios 1 and 2 (the shorter-term scenarios), but more expensive than using home credit in Scenarios 3 and 4 (the longer-term scenarios). This was influenced by the minimum loan term for Provident's home credit products, which was significantly longer than 28 days.[343]

5.17 Finally, we considered other, non-commercial alternatives that were potentially open to some borrowers, including borrowing from friends and

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[339] Amigo Loans said that on average loans took around 36–48 hours to pay out.
[340] UKCredit told us that the average loan took 6.6 days between receipt of enquiry and payment to guarantor.
[341] These scenarios were also used in our comparative pricing analysis of payday loans in Section 4.
[342] The full results are set out in Appendix 5.2, Table 1.
[343] Although we noted that, in principle, a customer might borrow from Provident on a longer, cheaper term and then get a rebate within 28 days, which would cause the relative price of using home credit to decline somewhat relative to the price of a payday loan.

family. Wonga submitted that friends and family should be considered a competitive constraint, and that the non-financial costs associated with this type of borrowing would be a relevant consideration to customers when considering the price of a payday loan.[344]

5.18 These informal credit options, where available, may have some characteristics similar to a commercial payday loan, such as the speed of access to funds (assuming family or friends have ready access to the funds), but may differ in other characteristics such as customers' ability to borrow more or extend the loan. Moreover, since borrowing from friends or family is based on a personal rather than a commercial relationship, this form of borrowing is inherently different, as a much wider set of social and other factors are likely to be involved in any request to borrow money. Its availability as an alternative and the range of factors that would be involved in practice are likely to differ considerably between potential borrowers. Further, friends and family will not normally be driven by the profit-seeking incentives of commercial credit providers when lending. We have not seen any evidence to suggest that lenders take into account funds sourced from friends or family when setting their prices. Taken together, this suggests that the risk that customers might otherwise borrow from friends or family is unlikely to impose an effective competitive constraint on payday lenders' pricing.

Access to, and availability of, other types of credit

5.19 Alternative sources of credit will only provide a viable alternative to a payday loan if payday loan customers have access to other credit products, and are able to use those alternatives to borrow the required amount given their credit histories. To assess the extent to which payday loan customers are able to use other forms of credit to borrow, we reviewed:

(a) customer research, including our survey of payday loan customers, and the work carried out as part of the Bristol Report;

(b) CRA data on payday loan customers' use of other credit products; and

(c) evidence on the acceptance criteria of non-payday lenders.

Customer research

5.20 Our survey showed that use of other forms of credit was relatively common among payday loan customers, although not universal. Specifically, when asked about their use of other credit products, we found that 49% of payday

[344] Wonga response to the annotated issues statement, 28 February 2014.

loan customers had used an alternative form of credit (excluding an overdraft) in the last 12 months. Credit cards were the most commonly used credit product (31% of payday loan customers). The others were retail credit (13%), bank/building society loans (8%), home credit (6%), pawnbroker (4%), Department for Work and Pensions (DWP) Crisis Loan (5%) and credit union (2%).[345] Moreover, of customers with a bank account, 56% had been overdrawn in the previous 12 months,[346] around half of whom had used an unauthorised overdraft.[347]

5.21 While many payday loan customers use other credit products, there was also evidence to suggest that a significant proportion had experienced credit repayment problems in the past (see paragraphs 2.23). We considered evidence on the extent to which payday loan customers have credit available to them from alternative credit sources at the point in time at which they take out their payday loan. Respondents to our survey were asked whether – instead of taking out a payday loan – they could have borrowed using another credit product.[348] We found that a significant proportion of customers – 39% – reported that they could not have used any alternative credit product to borrow the money. However, some customers did have credit alternatives available to them: 18% of all customers said that they could have used a credit card to borrow the money instead of a payday loan, 20% said that they could have used an overdraft and 30% said that they could have used at least one of these two alternatives.

5.22 The customer research produced for the Bristol Report[349] derived a measure of credit access from survey data, based on whether customers reported having unused balances on their overdraft or credit card or said that they were most likely to have used mainstream credit if they could not have borrowed from a short-term lender. On this measure, the report estimated that mainstream credit was a feasible alternative to short-term credit for 14% of high street payday loan customers and 24% of online payday loan customers. In most cases this would have meant using a credit card or overdraft.

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345 Research into the payday lending market report – results of quantitative and qualitative research undertaken by TNS BMRB, response to QFCA1.
346 ibid, response to QFC2. 96% of respondents said they had a bank, building society or credit union account.
347 ibid, response to QFC3.
348 ibid, response to QPDSB3. TNS expressed concerns regarding the possible limitations of this question, noting that some people may have answered in terms of what they would have done, rather than what they could have done, and that it may be difficult to judge whether one could use some of the alternatives, eg unlicensed lenders. This may result in the responses underestimating the availability of other sources of credit.
349 The impact on business and consumers of a cap on the total cost of credit, Personal Finance Research Centre, University of Bristol, 2013.

5.23 The Bristol Report also investigated customers' perceptions of the alternative credit products that were available to them. For online payday loan customers, 50% agreed that they used payday loans because they did not have access to anything else. For high street payday loan customers the figure was 57%.

5.24 Other customer research that we reviewed provided additional evidence of the extent to which payday loan customers could have used other forms of credit to borrow instead of a payday loan.[350] In all cases these surveys showed a significant proportion of payday loan customers reporting not having access to any credit alternatives, although estimates of the proportion of customers this applied to varied significantly (from around a quarter, up to more than half), depending on the sample used and the precise question asked.

Credit reference agency data

5.25 To explore further the degree to which payday loan customers are able to access other credit products – and the amount of credit available to payday customers using those products – we analysed information relating to a sample of payday borrowers' credit records. The detailed analysis is in Appendix 5.3.

5.26 We began by selecting a sample of payday loan customers from the transaction databases of 11 major payday lenders, as discussed in 2.48. CRAs were then asked to provide information on the payday loans and any other credit products used by each customer in the sample in the period 1 January 2012 to 31 August 2013. Our sampling methodology was based on randomly selecting loans, rather than customers, so will tend to give extra prominence to heavier borrowers who account for a greater share of payday loans.

5.27 Using this sample, we estimated that 52% of payday loan customers in our sample had an active credit card during 2012 and 55% had an overdraft balance greater than £20. A smaller proportion of customers used other credit products, such as personal loans. Around 25% of customers were not recorded in our data set as having used any other credit product.

5.28 Our results suggest that a significant proportion of payday loan customers use (or have used) credit cards. We considered the extent to which customers

[350] This included research by the CFA; Which?; Dollar; [✂]; YouGov; Friend Provident/JMU/Policis. In addition, Think Finance submitted survey results of 1,016 short-term borrowers, which asked why they had not considered products other than payday loans. 70% said that it was because they had a bad credit score or were rejected by mainstream lenders.

actually had credit available on their credit card accounts when taking out a payday loan. We did this by taking each payday loan in the sample that was issued in the period from 1 April 2012 to 31 March 2013, and for those customers with credit cards, seeking to estimate the total amount of available credit on all of their credit cards at the point at which the loan was taken.[351]

5.29 We estimated that in 82% of cases customers either did not have a credit card, or had less credit available than the amount that was ultimately borrowed using the payday loan. This finding, which is broadly in line with the results of our customer survey, suggests that although use of credit cards is relatively high, many payday loan customers with credit cards would not be able to use these cards to borrow further amounts as an alternative to a payday loan.

Evidence from non-payday lenders

5.30 Some non-payday lenders provided information on the likely availability of their credit products to payday loan customers.

5.31 A number of banks[352] told us that payday loan customers tended to represent higher credit risk than their typical customers, for example:

(a) Lloyds Banking Group (LBG) told us that it monitored the proportion of lending to customers with payday loans as these customers tended to have worse repayment behaviour overall than customers who did not use payday loans. LBG internal research from April 2012 suggested that of the Lloyds Bank customers who used payday loans, [✂]% would be rejected if they applied for a personal loan. For HBOS customers using payday loans, the figure was [✂]%. Follow-up research in July 2012 gave rejection figures of [✂]% for Lloyds Bank and [✂]% for Halifax.

(b) Another large bank ([✂]) told us that 4.4% of its retail customers had evidence of an active payday loan facility or had taken or applied for a payday loan facility in the last 12 months. Of those customers, 80% were currently in arrears on other credit facilities, with 73% having a registered default, county court judgment or insolvency marker. It told us that customers with recent payday loan activity had default rates up to ten times higher than those customers without payday loan activity.

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[351] It was not possible to carry out a similar assessment for overdrafts, because of limitations in the data available for these products.
[352] [✂]

5.32 In addition, a number of other credit providers[353] said that they were using or considering using information on payday lending as part of their credit checking process.

Summary of findings on access to and availability of alternative credit products

5.33 We found that use of other forms of credit was relatively common among payday loan customers, although not universal. We estimated that up to a half of all payday loan customers had used a credit card in the previous 12 months, and around a half had used an overdraft facility.

5.34 However, a significant proportion of payday loan customers have experienced repayment problems with credit in the past, and the evidence suggested that many customers would be constrained in terms of the alternative credit products available to them at the point of taking out a payday loan. In particular, we found that a significant proportion of borrowers would be unlikely to have *any* credit alternatives available to them when taking out a payday loan (our survey suggested that this applied to around 40% of all customers). In addition, despite relatively high usage of credit cards and overdrafts among payday customers, our survey suggests that only around 30% of customers could have used a credit card or overdraft to borrow the money instead of a payday loan. Our analysis of data provided by a CRA similarly indicates that many customers are likely to have only limited credit available on their credit cards at the point at which they take out a payday loan.

Payday loan customers' perceptions of other credit products

5.35 We next reviewed evidence on payday loan customers' perceptions of other credit products, and their willingness to use these products instead of payday loans.

5.36 In our survey we found that only a very small proportion of all customers reported that they would have used another type of credit product, had a payday loan not been available. In particular, respondents to our customer survey were asked: 'If you had not been able to get a payday loan on this occasion, what do you think you would have done instead?'[354] 6% of respondents said that they would have borrowed from a different type of credit

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[353] [✂]
[354] In its response to the annotated issues statement, Wonga argued that answers to this question could not be relied upon because the question was unprompted and respondents could only choose one answer. However, if

provider.[355] These responses suggest that in general customers taking out a payday loan do not consider other credit products to be a close substitute. A similarly small proportion of those customers that might be considered more 'marginal' – ie more likely to have alternatives available to them if the price of payday loans were to increase – reported that they would have used a different type of credit had their payday loan not been available.[356]

5.37 Instead, most individuals stated that they would either have gone without the loan[357] or borrowed from friends or family. Of the minority of customers who said that they would have used an alternative product, and consistent with our review of product characteristics, a credit card was the most common option (21% of alternatives mentioned). Other options mentioned included overdrafts (15% of alternatives mentioned), bank/building society loan (12% of alternatives mentioned), pawnbroker loan (3% of alternatives mentioned) and home credit (1% of alternatives mentioned).[358] In total, around 2% of customers reported that they would have used a credit card or overdraft to borrow the money had their payday loan not been available. The proportion of customers who said that they would have used other credit products was lower still.[359]

5.38 Other survey evidence supported this finding. In particular, in the Bristol Report's customer survey payday loan customers were asked: 'What would you have done if you had been unable to obtain a payday loan?' 8% of respondents reported that they would have borrowed in some other way, which is close to our own figure of 6% (see paragraph 5.36).[360] In addition, we found that in total, only 14% of all payday loan customers reported having got

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payday loans and other forms of credit were close substitutes, we would expect this to be reflected in the responses of customers irrespective of whether the question was prompted and despite the fact that customers could only report their most favoured alternative.

[355] Research into the payday lending market report – results of quantitative and qualitative research undertaken by TNS BMRB, response to QPDSB1.

[356] Specifically, we looked at respondents to our customer survey who said that they had not experienced any debt problems in the last 12 months, and so may be expected to be more likely to have other credit products available. Among this group, 5% of customers reported that they would have borrowed using another credit product had their payday loan not been available.

[357] In its response to the annotated issues statement and working papers, Dollar said that this result was inconsistent with the fact that 59% of payday loan customers said that the loan was for something that 'they definitely could not have gone without'. However, as discussed in paragraph 2.27, the qualitative research suggested that customers' mindsets at the time of taking out a loan tended to push their perception towards apparent need, exaggerating their need for a loan, while in retrospect customers thought that the expenditure could have been forgone or delayed.

[358] Research into the payday lending market report – results of quantitative and qualitative research undertaken by TNS BMRB, response to QPDSB2.

[359] Since we did not ask consumers specifically about guarantor loans, we reviewed the quantitative and qualitative research to understand if there were any cases where consumers had used or considered a guarantor loan. None of those interviewed as part of the quantitative and qualitative survey work mentioned guarantor loans. Source: Review carried out by TNS at CC request.

[360] The impact on business and consumers of a cap on the total cost of credit, Personal Finance Research Centre, University of Bristol, 2013.

as far as finding out information to compare the pros and cons of alternative credit products with the pros and cons of a payday loan.[361]

5.39 Wonga told us that on the basis of the survey evidence discussed in paragraphs 5.21 and 5.23 a sizeable proportion of the payday loan customers could have used alternative forms of credit and that these customers in aggregate would be sufficient to constrain payday lenders.[362] We noted, however, that while a significant proportion of customers could have had access in theory to other types of credit providers, the evidence presented in the above paragraphs (5.36 to 5.38) indicates that a very small proportion would consider other credit products to be a close alternative.

5.40 As discussed in paragraphs 5.19 to 5.34, one reason why many payday customers may not consider other types of credit to be a close substitute is that they are *unable* to borrow using these other types of credit. For those individuals who are able to borrow using alternative types of credit, our customer research highlighted a number of other reasons why customers may prefer to use payday loans, either related to:

(a) the perceived attractions of payday loans; or

(b) the perceived disadvantages associated with the alternatives.

5.41 In terms of the perceived attractions of payday loans, discussions with customers as part of our qualitative research suggested that some customers were attracted to the practical benefits of payday loans, and in particular the speed, convenience and control. This was supported by the findings of the quantitative survey, in which we asked those payday customers who could have used an alternative source of credit why they did not do so. The main reasons given for favouring payday loans were that the alternatives were not as convenient (45%) and that they could not get the money as quickly (31%).[363]

5.42 The importance to customers of convenience was also highlighted in the customer survey of the Bristol Report, in response to which over 60% of online customers gave 'convenience' as the reason for using a payday loan rather than borrowing in some other way.

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[361] Consistent with this finding, Elevate provided the results of a survey in which 1,016 short-term borrowers were asked 'Thinking about the last time you used a payday loan, which, if any, of the following options did you also consider?' 58% said that they did not consider any other options or payday loans were the only option available to them. 15% said they considered borrowing from friends and family. 13% said they had considered using a credit card and 10% considered using their authorised overdraft.
[362] See Wonga's response to the provisional findings, paragraphs 4.5–4.7.
[363] Research into the payday lending market report – results of quantitative and qualitative research undertaken by TNS BMRB, response to QPDSB6.

5.43 In addition to these practical advantages of payday loans, some customers also referred to the perceived disadvantages associated with alternative credit products. In particular, our survey found that some customers wanted to distance themselves from the type of customer that uses home credit or pawnbroking. In contrast, online payday loans were seen to be a relatively discreet way of borrowing by many respondents. In addition, some customers reported disliking or distrusting mainstream credit providers. A third of respondents to our customer survey agreed with the statement 'I try to avoid banks as much as possible'.[364]

5.44 Responses to the Bristol Report's customer survey also highlighted negative perceptions among some payday loan customers about characteristics of other forms of credit, particularly credit cards or overdrafts, that are revolving rather than having a fixed end date, and/or can be used continuously. Around 63% of high street payday loan customers and 54% of online payday loan customers responding to the Bristol Report's customer survey agreed with the statement: 'I use this type of loan because I am less likely to get into difficulty using it compared with a credit card or overdraft.' Policis' payday loan customer survey[365] similarly found that 56% of payday loan users agreed that 'credit cards could trap you in long-term debt' while 43% believed that 'you are less likely to get into trouble with payday loans'.

Competitive interactions between payday lenders and other credit providers

5.45 We sought evidence of payday and non-payday lenders taking actions to compete with each other for customers, as well as lenders' views on the extent of competition between payday lenders and other credit providers. Further detail of respondents' views are set out in Appendix 5.4.

5.46 We began by noting that the market outcomes in payday lending, as set out in Section 4, suggest that lenders are not effectively constrained in setting their prices, although there is more evidence of lenders taking actions to improve the non-price dimensions of their loan offering.

5.47 A small number of payday lenders, including CFO Lending, Global Analytics and The Cash Store, told us that they did not see themselves as competing with other credit products. However, most payday lenders that we spoke to took the view that they did compete with providers of other forms of credit, including CashEuroNet, Cheque Centres, Dollar, MYJAR, Microlend, SRC, Think Finance and Wonga.

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[364] ibid, p84.
[365] Credit and low-income consumers, Policis.

5.48 When asked for examples of how they competed with providers of other credit, most payday lenders highlighted the role of competition between payday lenders and providers of other forms of credit in driving product innovation. For example, Wonga told us that there was evidence that other financial providers were responding to the innovation brought to the sector by companies like Wonga: for instance, banks were improving their online and mobile platforms; Provident, a home credit provider, was now providing an online short-term credit product; and some credit unions were increasing their efforts to offer an alternative to payday loans.[366] We saw no substantive evidence that suggested that the prices chosen by payday lenders were influenced by the prices of non-payday products.[367]

5.49 Many of the non-payday lenders that we contacted believed they did not compete directly with payday lenders and/or told us that they had not taken actions to respond to competition from payday lenders. These included: banks (Barclays, HSBC, LBG, RBS/NatWest and Santander); credit card providers (MBNA and SAV); home credit providers (Shopacheck); Logbook loan providers (CarcashPoint); pawnbrokers (Fish Brothers and Mays Pawnbrokers); peer-to-peer lenders (Ratesetter); retail credit providers (SDFC, Next and Arcadia Group); and guarantor loan providers (Amigo Loans and UKCredit).

5.50 However, some respondents provided details of some actions that they had taken as a result of the actions of payday lenders:

(a) Capital One told us that it had tested two credit card products as potential alternatives to, and partly in response to, the growth of payday lending.

(b) Leeds City Credit Union said that its business volumes had remained steady and therefore there was no evidence that it was losing customers to payday lenders. However, it was trying to win customers from payday lenders, working with local partners and media to raise its profile.

(c) Mobilemoney said that the growth of payday lending was adversely affecting its business for logbook loans of £200 to £1,000.

(d) Provident Financial, a home credit provider, told us that its home credit offer did compete at the margins with payday lenders. Provident Financial told us that it had sought to update and modernise its home credit offer in

[366] Wonga response to the annotated issues statement.
[367] Dollar told us that it had taken the price of authorised overdrafts into account when it had increased the price of the Money Shop payday product in 2013. Wonga referred to a presentation by [✄]. However, in neither case was any evidence provided showing how overdraft charges had actually affected the level of prices chosen by the lender, and there was no indication that the price of overdrafts (or indeed any other forms of credit) had driven either lender to keep their prices low for fear of losing customers.

response to the general trend in customer behaviour and preferences for greater convenience, speed and online interaction.

(e) S&U, a home credit provider, told us that it was competing for customer loan business, but did not compete directly online with payday loan companies.

5.51 Overall, despite a small number of examples of other credit providers – particularly non-mainstream lenders – taking steps to increase the flexibility of their products, most providers told us that they did not compete with payday lenders. Similarly, while we have observed some innovation in the payday lending sector (see Section 4), and it is possible that some of this innovation may be targeted at customers who had previously used other types of credit product, we saw no substantive evidence of payday lenders taking developments in the pricing of any non-payday products into account when setting the prices of their products.

Conclusions on competition from other credit products

5.52 Based on the evidence set out in paragraphs 5.5 to 5.49, and given the market outcomes that we observe as discussed in Section 4, we concluded that competition from other credit products was likely to impose only a weak competitive constraint on payday lenders, and in particular on their pricing. This was for the following reasons:

(a) The characteristics of payday loans differentiate them from many other credit products, which often do not allow customers to borrow such small amounts for short periods, access funds as quickly, or require some security. With the exception of unauthorised overdrafts, borrowing using other credit products is generally significantly cheaper than using a payday loan.

(b) It is relatively common for payday loan customers to use other forms of credit. However, a significant proportion of payday loan customers have experienced credit repayment problems in the past, and the evidence that we saw suggested that many customers would be constrained in the extent to which credit would be available using alternative products at the point at which they take out a payday loan. For example, only around 30% of respondents to our customer survey reported that, when taking out their most recent payday loan, they could have used a credit card or overdraft to borrow the money instead.

(c) Customer research suggests that in general customers taking out a payday loan do not consider other credit products to be a close substitute

– only 6% of respondents to our survey reported that they would have used another type of credit had they been unable to take out a payday loan. Partly this is likely to be due to the fact that many payday customers do not have credit alternatives available to them. In addition, some customers may prefer payday loans because of the convenience, speed or discretion associated with these products, or because of a negative perception of alternatives such as a perceived lack of control.

(d) In addition to this evidence of a lack of substitutability, we saw no substantive evidence of payday lenders taking developments in the pricing of any non-payday products into account when setting the prices of their products, although it is possible that some of the innovation that we have observed in the payday lending sector may be targeted at customers who had previously used other types of credit product.

Competition between online and high street lenders

5.53 We considered next the extent to which payday loans offered online and on the high street were perceived by borrowers to be substitutable, and whether online and high street lenders competed with each other for customers. First, we assessed the similarities and differences in product characteristics, prices and customer demographics between online and high street payday loans. Then we considered the extent to which customers had used both channels, and the reasons given for this. Finally, we considered lenders' submissions on whether online and high street lenders competed for customers.

Product characteristics and customer demographics

5.54 The clearest way in which high street and online payday loans differ is in the way in which customers apply for their loan – and whether this application takes place online or at a physical location. High street loans also differ in that borrowers are generally offered the ability to receive and repay credit in cash.

5.55 Putting these differences aside, however, we found that high street and online payday loans share many characteristics. For example, both online and high street payday lenders allow customers to take out loans for similar amounts and for similar short periods. Online and high street lenders both offer similar extension policies, generally allowing customers to roll loans over so long as they repay outstanding fees. For most lenders, whether online or high street, repayment dates are tied to a borrower's payday.

5.56 We also compared the prices (as of October 2013) of high street and online lenders. Table 5.1 provides the prices of the largest high street lenders under the different borrowing scenarios discussed in Section 4. It shows that the largest high street lenders (Cheque Centres and The Money Shop) charged prices close to the typical price of £30 per £100 for a one-month loan. The products of two other high street lenders, H&T and Speedy Cash, were relatively cheap, comparable to the cheapest online products available on the market.

TABLE 5.1 **TCC for a £100 loan for the largest high street lenders, under different borrowing scenarios**

£

Lender	*Product*	*Scenario 1*	*Scenario 2*	*Scenario 3*	*Scenario 4*
		Borrow for 28 days	*Borrow for 14 days*	*Borrow for 28 days, roll over for 28 days*	*Borrow for 28 days, repay 11 days late*
Cheque Centres	Payday loan	29.99	29.99	59.98	59.99
The Money Shop	Cheque-based loan	29.85	29.85	59.70	58.85
The Money Shop	Chequeless loan	29.99	29.99	59.98	58.99
H&T	Payday loan (cheque)	17.64	17.64	35.28	48.80
H&T	Payday loan (debit)	20.00	20.00	40.00	52.37
Speedy Cash	Payday loan	25.00	25.00	50.00	37.50
Speedy Cash	Flex Loan	23.01	11.51	46.03	32.05
Speedy Cash	Flex Account	23.01	11.51	45.92	32.05
The Cash Store	Payday loan	38.24	34.05	76.48	66.74

Source: CMA analysis.

5.57 We also considered the characteristics of high street and online payday loan customers. There was considerable overlap in the demographic profile of online and high street borrowers but, as discussed in paragraph 2.22, high street customers typically had lower incomes than online customers, and tended to be older.

Customer views of substituting between high street and online payday loans

5.58 We analysed survey evidence on the extent to which customers considered online and high street loans to be substitutes.

5.59 We found that in most cases, high street customers had heard of at least one online lender, and that similarly most online customers had heard of at least one high street lender.

5.60 Of the high street customers who had taken out more than one loan, half had only ever used high street lenders and half had borrowed both on the high street and online.[368] 26% of those who had never used an online lender (ie 13% of all high street customers who had taken out more than one loan) said that they had considered doing so.[369] Taken together, this suggests that 63% of high street customers who had taken out more than one loan had either

[368] Research into the payday lending market report, p43.
[369] ibid, p61.

used or considered using an online lender. These findings were broadly consistent with our analysis of data provided by the CRAs, as discussed in Appendix 6.2.

5.61 For those high street customers who had not considered using an online lender, the most common reasons given for not doing so were that they preferred to speak to someone face to face; they did not have internet access; and they did not like providing personal information online.[370]

5.62 Of the online customers who had taken out more than one loan, 82% had only used online lenders.[371] Only 11% of those who had only borrowed online (ie 9% of all online customers who had taken out more than one loan) said that they had considered using a high street lender. Taken together, this suggests that 27% of online customers who had taken out more than one loan had either used or considered using a high street lender. These findings were also broadly consistent with our analysis of data provided by the CRAs, as discussed in Appendix 6.2.

5.63 Of those online customers who had not considered using a high street lender, the most common reasons given for not doing so were that online customers preferred the convenience of online, and because borrowing online was considered quicker/easier.[372]

5.64 Our qualitative research provided further insight into the reasons why some customers may prefer high street lenders over online and vice versa. Reasons given for preferring high street lenders were: *(a)* it was perceived as safer; *(b)* customers preferred the face-to-face interaction and building relationships with the staff; *(c)* the convenience and visibility of the store; *(d)* customers' use of other services in the same store, like pawnbroking; and *(e)* a lack of knowledge and experience of the online market. Reasons given for preferring online lenders were: *(a)* a perception that the high street was less regulated; *(b)* the anonymity of online borrowing, especially if their credit application was rejected; *(c)* a lack of high street stores nearby, allied to the convenience of online; *(d)* convenience, as customers' finances were already dealt with online; *(e)* a feeling that high street lending was for the poor and dis-possessed; and *(f)* an expectation that high street lenders did not offer the same products as online lenders.[373]

[370] ibid, p61.
[371] ibid, p42.
[372] ibid, p61.
[373] ibid, p63.

5.65 The qualitative interviews also suggested that some of the movement from online to high street lenders was the result of serial borrowers being rejected by online lenders, with convenience also being a factor.[374] Recommendations from a friend could also play a part in the decision. Movement from high street to online was linked to marketing emails and texts after the initial loan, which could make borrowers aware of the online market.[375]

Lenders' views on competition between online and high street lenders

5.66 We also reviewed the submissions of lenders on the extent to which high street and online lenders competed with each other. CashEuroNet (an online lender) said that it competed with all payday lenders and SRC told us that the online sector was affecting the profitability of its high street stores. Other lenders' responses suggested that there was limited competitive interaction between high street and online lenders. For example, [✄] said that when setting prices it had peripheral awareness of the wider high street market and was not aware of how other providers affected its business, and The Cash Store said that the actions of other lenders did not affect its volumes or sales.

Conclusions on competition between online and high street payday lenders

5.67 The evidence we reviewed indicates that:

(a) There were some differences in the age and income profile of the customer groups served by online and high street lenders. Except for the channel through which they were sold, the products offered by the two types of lender were very similar.

(b) A significant proportion (63%) of high street customers had used or considered using an online lender. By contrast, fewer online customers had used or considered using a high street lender, though some had done so.

(c) Lenders' views on whether online and high street lenders competed for customers were mixed.

5.68 We concluded that while some high street customers may have a strong preference for borrowing face to face from a high street lender, the majority of customers were likely to consider online to be a viable alternative, such that online lenders were likely to compete with high street lenders. Any competitive constraint imposed on online lenders by high street lenders was likely to be

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[374] ibid, p64.
[375] ibid, p64.

weaker, given the relatively small proportion of online customers who had also used or considered taking out loans on the high street.

Competition in different local areas

5.69 We considered that the online payday lending sector was inherently national in scope, as customers in any part of the UK could apply to any online lender, regardless of where that lender was based. However, we recognised that there was scope for competition to have a local dimension in relation to high street lenders. We therefore reviewed the evidence on whether competition between high street lenders differed between different local areas. In particular, we considered:

(a) how far customers were willing to travel to their store, and the overlap between high street lenders' operations;

(b) the extent of local variation in lenders' payday loan offering and lenders' reactions to local competitive conditions; and

(c) the ease with which lenders are able to launch stores in new localities.

5.70 The evidence we collected showed that payday loan customers taking out loans on the high street generally travelled only a short distance to their store: 80% were located within 3.2 miles. Until the exit of Cheque Centres from payday lending in May 2014 (see paragraph 2.108), there was considerable overlap between the operations of high street lenders – largely as a result of the significant networks of stores operated by the two largest high street lenders, The Money Shop and Cheque Centres. Our detailed analysis of local overlap and concentration is set out in Appendix 5.5.

5.71 The evidence provided by high street payday lenders showed that there was very little local variation in their payday loan offering. Most of the larger high street lenders (including Cheque Centres, H&T, Oakam, SRC and The Cash Store) said that they did not vary their offer locally. Dollar (The Money Shop) said that it varied some aspects such as opening hours and marketing materials in response to competition, but not its price: when it had purchased existing operations it had gradually moved the prices in the acquired store to the uniform level. Most smaller high street lenders also reported not varying their offer locally – only three respondents to our smaller lender questionnaire said that there was any local variation in their offer.

5.72 We also asked high street lenders for examples of occasions where they had reacted to actions taken by other high street payday loan providers. In general, the commentary provided by lenders in their responses to our questionnaire yielded very little in the way of examples of lenders reacting to local competitive conditions.

5.73 We considered whether any localised barriers existed which would make it difficult for lenders to open stores in new local areas. To enter a new area, a high street payday lender would need to rent premises in a location with retail units available with the appropriate use class (A2 Financial and professional services).[376] In addition to this, high street lenders would need to fit out the locations for payday lending and hire staff.

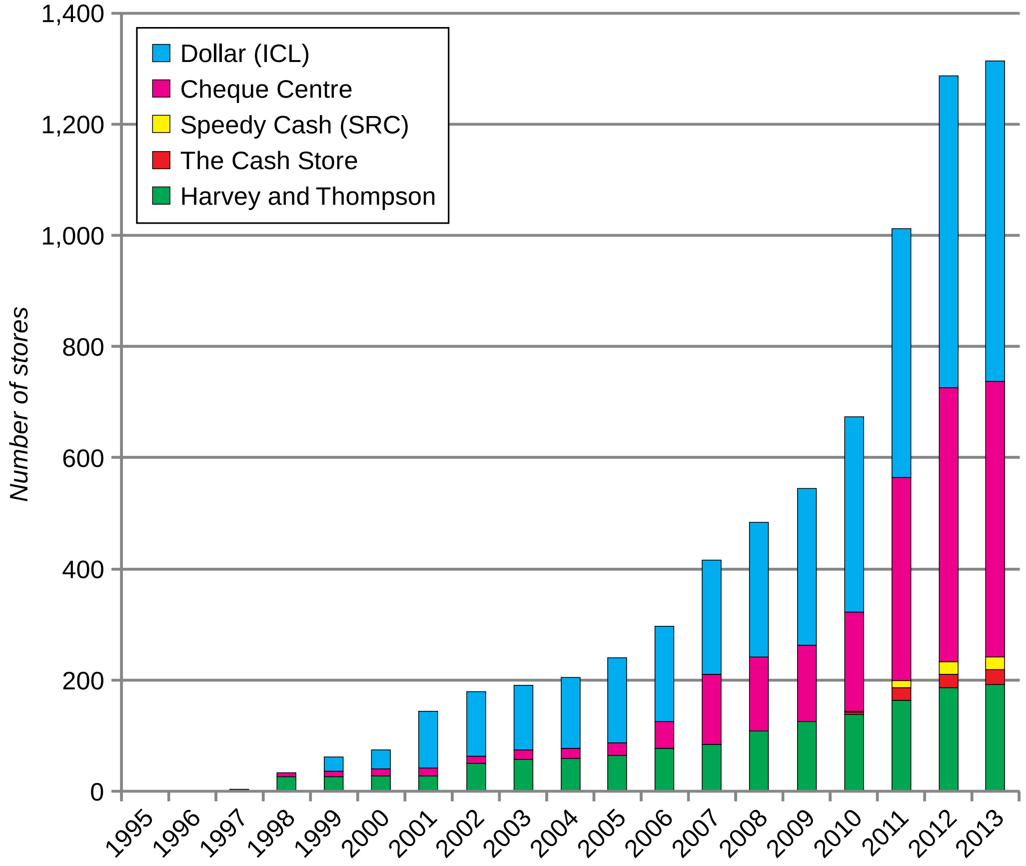
5.74 Dollar (The Money Shop) told us that costs of opening a store ranged from £[✄] to £[✄] per store. It said that a provider of only payday loans would incur much lower costs when opening a store because they would not need much of the safety/security equipment that The Money Shop required. SRC (Speedy Cash) said that its investment per store included £250,000 for construction and approximately £150,000 to fund receivables. SRC also invested in significant advertising, promotion and recruiting efforts. It took approximately 12 months from deciding to enter the market to starting to trade.

5.75 Figure 5.1 shows the evolution of the number of high street stores operated by the major lenders over time. It shows that these high street lenders have opened large numbers of stores in recent years, particularly between 2010 and 2012, although the rate of growth in store openings decreased in 2013, with a number of high street lenders exiting the payday lending market in 2014.[377]

[376] As set out in the Town and Country Planning (Use Classes) Order 1987 (as amended).
[377] See paragraph 2.74.

FIGURE 5.1

Number of high street payday lending stores over time



Source: CMA analysis.

5.76 This evidence suggests that existing high street lenders have been able to open stores in new localities with relative ease where they found there to be sufficient demand for payday loans.

Conclusions on local competition

5.77 We concluded that while high street lending had a local dimension (since most customers would be unwilling to travel more than a relatively short distance to their store), competitive conditions were unlikely to vary significantly by location. This is primarily because online lenders (who account for the majority of loans issued) are likely to constrain high street lenders in a similar way across the UK. In addition, we note that there has historically been a high degree of overlap between different high street lenders' stores and that existing high street lenders appear to have been able to open stores in new localities with relative ease. In line with this conclusion, we noted that lenders' prices and product offerings have generally been set at a national rather than a local level.

Conclusions on the relevant market

5.78 On the basis of the analysis set out in this section, we considered the relevant market definition for the purposes of our investigation.

5.79 We decided not to include products other than payday loans within our definition, due to the weak competitive constraint that other products impose on payday lenders. A combination of factors have informed our conclusion on the relevant product market, including the differences that exist between payday loans and other types of credit (which serve to limit customers' willingness to substitute between them), the limited extent to which many payday customers are able to borrow using other credit products, and the limited evidence of competitive interaction between payday and other lenders.

5.80 Regarding competition between online and high street lenders, we found that the products are similar and there is considerable overlap in the customer groups served by online and high street lenders. However, there is evidence to suggest that some customers may have a preference for particular channels, and we also noted an asymmetry, in that a higher proportion of high street customers used online lenders than vice versa. We did not, however, consider that the segmentation that we observed was sufficiently great that it was necessary to define separate markets for online and high street payday loans.

5.81 Finally, given our conclusions that the online payday lending sector was inherently national in scope (see paragraph 5.69) and that online lenders are likely to constrain high street lenders in a similar way across the UK (see paragraph 5.77), the lack of local variation in high street lenders' offering and the relative ease with which lenders are able to open new stores in different local areas, we did not consider that competitive conditions differed across local areas such that it was necessary for our competition analysis to define separate local geographic markets.

5.82 Given the above, we therefore concluded that the market relevant to our assessment of competition is the provision of payday loans in the UK.

6. Competition for payday loan customers

Introduction

6.1 In this section, we assess the extent and nature of rivalry between payday lenders, with a particular focus on the role played by payday loan customers in driving competition. In a market in which competition is working effectively, firms are incentivised to keep their prices down and the quality of their products high because if they do not do so, customers will choose an alternative supplier. If barriers exist that prevent customers from shopping around effectively for loans and/or switching supplier to obtain a better deal, then firms may be able to exploit these barriers and enjoy market power.[378]

6.2 Our assessment of competition between payday lenders, and the role of customers within this, is structured as follows.

6.3 We begin by reviewing evidence on the overall effectiveness of the constraint imposed on lenders by the threat that customers will choose an alternative supplier. We summarise the evidence regarding payday loan customers' sensitivity to variation in prices, and the impact this has had on the effectiveness of price competition between lenders.

6.4 We then present evidence we have gathered related to how customers choose their provider:

- *(a)* First, we provide a description of the extent to which payday loan customers compare the different products on offer prior to taking out a loan (ie shop around).
- *(b)* Second, we discuss the frequency with which customers switch lenders when returning for additional credit, and the reasons given for doing so.

6.5 Next, we discuss five characteristics of the payday lending market which may impede customers from effectively shopping around for a loan or switching lender to get a better deal, reducing their responsiveness to variation across lenders and so weakening the pressure for lenders to compete on prices. These are:

- *(a)* aspects of the context in which the decision to take out a payday loan is made;
- *(b)* the potential difficulties associated with identifying the best-value loan;

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[378] See the Guidelines, paragraph 295.

(c) additional factors limiting customers' awareness of and sensitivity to late payment fees and other fees and charges incurred if customers do not repay their loan in full and on time;

(d) the reliance of many customers on lead generators; and

(e) the perceived risk and loss of convenience associated with changing lender.

6.6 We then discuss the likely impact of the FCA's price cap – that came into force on 2 January 2015 – and other recent market developments on customers' sensitivity to prices, and on the constraint imposed on lenders by the threat that customers will choose an alternative provider if they fail to keep their prices low.

6.7 Finally, we present our conclusions on the constraint imposed on payday lenders by the need to price at a level to attract customers from other payday lenders and on whether there are any features of the UK payday lending market which restrict the effectiveness of this constraint.

The effectiveness of the competitive constraint imposed by the need to attract and retain payday loan customers

6.8 As set out in paragraphs 4.218 to 4.220, the outcomes that we have observed in the payday lending market suggest that while there is competition on certain non-price dimensions of payday loans, there has been a lack of effective price competition. This is consistent with our profitability assessment, which shows that the largest lenders have earned profits significantly above our consideration of the cost of capital during 2008 to 2013, although we observed significant variation in the level of profitability both between lenders and over time. While the volume of lending has fallen substantially in 2014, this appears to have been driven substantially by lenders adapting to and anticipating a tougher regulatory environment (see paragraphs 4.164 to 4.166). Although overall profits generated have fallen in 2014, profitability was supported by an increase in the proportion of lending that was repeat borrowing. Our analysis of the most recent trend in financial performance indicated that the aggregate net margin for lenders increased by six percentage points to 31%.

6.9 The evidence that we have reviewed suggests that customer demand has generally been unresponsive to differences in prices between providers. In particular, while price reductions are uncommon, where we do observe examples of lenders offering significantly lower rates, these lenders have generally not been particularly successful in attracting new business. For example, [✂] told us that it increased its [✂] interest charge from [✂]% to [✂]%, in order 'to increase revenue as [it was] getting no appreciable marketing benefit by undercutting competitors on price' (see paragraph 4.76*(a)*). Similarly, despite the size of the discount that was offered, Speedy Cash (SRC) told us that its interest-free loan offer had only led to a marginal pick-up in volume (see paragraph 4.61).

6.10 In many cases, we have observed cheaper products being withdrawn, or the prices of these products eventually being increased (see paragraphs 4.44 to 4.52). Nevertheless, despite this trend we continue to observe some significant differences between the price of the cheapest and most expensive products available on the market for a loan of a given value and duration (see paragraphs 4.29 to 4.35).[379] For example, comparing the products in our review of the prices charged by payday lenders as of October 2013, we found that a borrower seeking to take out a payday loan for £100 for 28 days could pay interest and fees of under £20, or more than £50, depending on which lender they chose. The extent of the variation in prices was greater still in the event that a customer repaid their loan late (see paragraph 4.32).

6.11 Moreover, lenders whose payday lending products are relatively expensive in different borrowing scenarios continue to capture a significant share of customers (see paragraphs 4.82 to 4.103). Although our data does not allow us to rule out the possibility entirely, the evidence does not suggest that this pattern can be explained by customers preferring certain lenders for reasons other than price, such as non-price aspects of their product offering, or by their relative willingness to grant credit to particular customers.

6.12 Despite this observed lack of price sensitivity, there is evidence to suggest that – as we would expect – customers care how much they pay for their payday loan. For example, in response to our survey, 55% said that the total cost of the loan was 'very' or 'extremely' important, and a further 30% said that this was 'fairly' important. This is especially likely to be the case given the tight financial constraints that payday loan customers often face when they take out a loan. This contrast between the importance that customers place on the cost of borrowing and the limited responsiveness of customer demand to differences in prices between providers suggests that some impediments exist which are preventing or deterring customers from responding to

[379] In its response to the provisional findings (paragraphs 2.1–2.9), CashEuroNet submitted estimates of price dispersion in various markets, arguing that the extent of price dispersion in payday lending was in line with the range observed in a number of other markets which it argued were broadly competitive. We noted, however, that it was likely that products in those other markets were likely to be somewhat heterogeneous in their attributes, which would drive dispersion in prices. In contrast, we considered a payday loan to be a relatively homogenous product (see paragraph 4.95). In addition, it was not clear the extent to which search and switching costs were absent in the markets cited by CashEuroNet, or how the markets chosen had been selected.

variations in the prices of payday lending products, as they would do in a well-functioning market. By reducing the responsiveness of customers to prices, these impediments are likely to be a primary reason why lenders are not driven to compete for customers by lowering their prices.

The extent and nature of shopping around

6.13 In order to be able to make effective comparisons between the value for money represented by different products – and so for lenders to face an effective competitive constraint – payday loan customers need to be aware of and willing to use other lenders' products that are available to them. In this subsection, we describe evidence of the extent to which customers carry out comparisons prior to taking out a loan and the nature of the comparisons that are carried out.

The extent to which customers shop around at all before taking out a loan

6.14 First, we considered the extent to which payday loan customers compare alternatives before taking out a loan.

6.15 The findings of our customer survey indicated that the majority of payday loan customers do not compare the pros and cons of different payday lenders at all prior to taking out a loan.[380] Seven out of ten customers reported that they had not done so for the most recent loan, and six out of ten customers reported never having done so.[381]

6.16 Other customer research also suggested that a significant proportion (ie at least a third) of payday loan customers do not carry out any comparisons

[380] The survey asked customers the question 'Did you shop around between payday lenders—for example, compare some of the pros and cons of different payday lenders—before you applied for your loan?'.
[381] CashEuroNet argued that the extent of shopping around was not low when compared with other financial products (and in particular the current CMA market investigation into private motor insurance (PMI) which found that two-fifths of PMI customers said that they last compared insurers or insurance policies less than a year ago). We note that there are substantial differences in the extent to which between private motor insurance (PMI) and payday loan customers compare products. Nearly all PMI customers (95%) had at some point compared insurers/policies. The majority of customers who had ever shopped around online used a PCW and of these, around 30% used more than one PCW to compare policies. In its response to the provisional findings (paragraphs 3.4–3.8), CashEuroNet argued that it would be more appropriate to compare the 'shop-around rate' of 45% (ie. the proportion of online payday loan customers who had ever shopped around) with what it considered to be the equivalent rates for PMI of 42% (customers who shopped around within the last 12 months) or 52% (customers who reported having shopped around within the last 18 months). CashEuroNet submitted that these were the relevant comparators because payday loan customers typically used loans for a period of 12 to 18 months while many motor drivers had been buying insurance for several years. We note, however, that payday loan customers typically take several loans over 12 to 18 months whilst motor drivers typically renew their motor insurance once a year. Therefore, over the same period motor drivers face a buying decision relatively less often than payday loan customers. While these considerations indicate the difficulties in making simple comparisons between markets given the different nature of the products, it appears indisputable that customers' use of PCWs currently plays a significantly greater role in competition to attract PMI customers than they do in relation to payday lending.

before choosing a payday loan, although the proportion of customers found not to have carried out any comparisons before taking out their loan were generally lower than found in our own customer survey:

(a) Research carried out as part of the Bristol Report found that 54% of online customers reported not having compared the cost before taking out their loan.[382]

(b) Wonga provided details of its own customer research which indicated that [✂]% of its first-time customers did not look at or consider an alternative lender's website before choosing Wonga.[383]

(c) An online survey conducted by CashEuroNet of approximately 2,000 of its own customers[384] found that [✂]% of respondents had neither shopped around for the most recent loan, nor for a previous payday loan.

6.17 We noted the variation between these results. One likely reason for this is the differences in methodology between the surveys. In terms of sampling approach, Wonga's and CashEuroNet's research included only their own customers, while our survey was able to draw on a market-wide sample using lenders' customer lists.[385] While the Bristol Report research was based on interviews with the customers of more than one lender, its coverage was more limited than that of our own survey, and – because of its focus on the broader high-cost credit sector – its sample of payday customers was smaller than our own. A second possible explanation is the variation in the precise questions that customers were asked. For example, while the question in our survey addressed the extent to which customers compared the pros and cons of different payday lenders before taking out their loan, Wonga's question asked about whether customers 'looked and considered' alternative lenders'

[382] University of Bristol (2013): 'The impact on business and consumers of a cap on the total cost of credit'. Customers were asked the following question 'Before you took this loan out from [name of lender], did you find out what it would cost to borrow the money you needed from any other payday lenders?'.
[383] According to customer research conducted in March 2013, [✂]% of Wonga's customers considered one or two other lenders before choosing Wonga, [✂]% considered 'lots', and [✂]% could not remember.
[384] CashEuroNet asked similar questions as in our customer survey.
[385] In its response to our provisional findings (paragraph 3.2), CashEuroNet submitted that although its survey consisted only of its own customers, it was still relevant as CashEuroNet was a significant player in the market. Our survey found similar results as those submitted by CashEuroNet in relation to customers who took out their most recent loan with CashEuroNet ([✂]% of CashEuroNet's customers had neither shopped around for the most recent loan, nor for a previous loan). However, the propensity on shopping around varies considerably between lenders. For example, the proportion of customers who had never shopped around is [✂]% and [✂]% for those who took out the most recent loan with, respectively, WageDayAdvance and Wonga. This further highlights the importance of drawing on a market-wide sample to gain an accurate view on the customers' average propensity on shopping around.

websites before choosing Wonga (an act which may not necessarily involve a comparison of products).[386]

6.18 While having regard to the different estimates of the proportion of customers who have shopped around, we placed greater reliance on the estimate from our own survey, because it was representative of the overall population of payday loan customers and because the question put to customers was the relevant one for the purpose of our assessment.[387]

6.19 We also considered how the extent to which customers reported having shopped around varies between the different customer groups represented in our customer survey. Our assessment included using an econometric analysis to estimate the relationship between different customers' characteristics and their likelihood of reporting having shopped around (see Appendix 6.1 for further details). We found that:

(a) There was little variation in the extent to which new and repeat customers reported having shopped around for their most recent loan.

(b) Online customers were significantly more likely to report having shopped around for their most recent loan (32%) compared with high street customers (13%).

(c) The financial literacy of customers (as indicated by their ability to calculate simple interest) and whether they had a higher education degree had a positive effect on the likelihood that they reported shopping around for their most recent loan.

(d) Customers who considered speed as the most important factor when taking out a loan were less likely to report having shopped around.

The nature of the comparisons carried out

6.20 We considered survey evidence on the nature of the comparisons that were carried out by the minority of customers who reported having shopped around.

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[386] Wonga asked the following question 'Before deciding to apply for your first Wonga loan, can you remember if you looked at and considered other cash advance websites too?' (see Populus Customer Survey, March 2013 – Annex 3 of Wonga's initial submission).
[387] In its response to our provisional findings (paragraph 3.9), CashEuroNet also emphasised that Pay-Per-Click conversion rates were [✂], and that drop-off rates (after visiting its website, after starting registration process, or after receiving an offer) were [✂]. It told us that this was evidence of customers shopping around. However, we noted that the fact that some customers did not follow through to complete an application does not indicate whether they switched to other lenders after dropping off, and the reasons for doing so.

6.21 Of the customers who reported having ever shopped around for a payday loan in our customer survey,[388] visiting lenders' websites was by far the most common source of information that customers reported having used (89% of these customers mentioned this source) followed by advertising (57%) and comparison websites (42%). Significantly less common were talking to friends and family (18%), speaking to lenders over the phone (16%) and visiting high street shops (14%).[389]

6.22 Of those customers who reported using lenders' websites to shop around,[390] around half reported visiting the websites of four or more lenders. Of those customers who reported visiting lenders' stores to shop around,[391] most reported having visited the shops of two or fewer lenders.

6.23 Nearly all (91%) of the customers who said that they had shopped around for any loan[392] reported having found out how much it would cost to borrow the amount needed from another lender. Most also reported having found out how quickly the other loan would be granted (84%) and the amount that they could take out (80%). Around two-thirds of customers who had shopped around reported having found out the cost of borrowing with another lender if they did not pay back on time.

6.24 Dollar told us that it was beginning to observe a change in the factors that customers shopped around on, as the market started to mature. Whereas in the past shopping around had focused mainly on speed, ease and convenience, Dollar considered that price and some of the other product features were becoming more important.

6.25 The results of our qualitative research indicated that in some cases customer search activities relating to different lenders' prices may not be particularly thorough, and that, in general, shopping around appeared to be a 'very cursory experience'.[393] For example, for some customers shopping around consisted of typing payday-loan-related terms (eg 'short-term loan' or 'fastest way to get a loan') into a search engine and clicking on the first two or three results, picking a site whose look appealed to them or where the loan application appeared very clear, and applying (and if rejected, trying the next site in the list). If during the application process there were some aspects that

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[388] 40% of the total sample. See TNS BMRB survey report, p96.
[389] For those customers who shopped around and took out a payday loan on the high street (a small minority of the survey sample of the high street customers, ie 13%, reported having shopped around for the most recent loan), visiting a shop was, however, a relatively important source of information (see TNS BMRB survey report, p101).
[390] 35% of all respondents.
[391] 17% of all respondents.
[392] 40% of the total sample.
[393] See TNS BMRB survey report, p95.

the customer did not like, such as having to provide evidence of income, they would search again.[394]

6.26 Our qualitative research also suggested that even when they tried to shop around, customers encountered various difficulties: eg they were unaware of PCWs that could assist in searching,[395] the borrowing terms on such comparison sites were for different amounts and/or time periods and so they could not be easily compared, they found it difficult to compare financial concepts such as APRs, they intentionally limited the number of lenders to which they sent their details due to privacy concerns, and they had a perception that lenders' charges were very similar.[396] Due to these difficulties, some customers were unable to identify the best deal for them.[397] We discuss in paragraphs 6.69 to 6.92 characteristics of the payday market which are likely to impede customers' ability effectively to identify and choose the best-value loan.

Conclusions on patterns of shopping around

6.27 The evidence that we have reviewed on patterns of shopping around shows that:

(a) The majority of payday loan customers do not shop around at all prior to taking out a loan. High street customers are particularly unlikely to compare different lenders' products before taking out a loan.

(b) Those comparisons that do take place are typically carried out using lenders' websites, and most customers who have shopped around report

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[394]Similarly, the further qualitative customer research we undertook as part of our remedies process found that the process of choosing a loan typically was relatively short (both in terms of the number of web pages visited and the time spent reading them) and simple, and consisted of very little comparison of loans and lenders. Some customers, particularly those who had taken out loans in the past, navigated directly to lender sites, or typed a particular lender's name into a search engine and clicked through to the lender without paying much attention to the other results. Customers in this research also said they would not scroll very far down a results page, often only looking at the top five results. The research found that such searching behaviour was driven by a desire to access the money quickly, and a belief that all loans cost around the same amount, See TNS BMRB remedies customer research, pp11–14.
[395] The customer research found similarly that customers had a low awareness of the existence of PCWs (see p12).
[396] See TNS BMRB survey report, p104.
[397] TNS BMRB told us that respondents to the qualitative research revealed their inability actually to identify the best deal in two ways:

- Respondents explained that since taking out loans with a certain lender, they had taken out subsequent loans with different lenders, with lower interest rates, fees and/or better terms. Respondents reported that they had been unable to identify these loans as a 'better deal' until they had experience of both lenders, for example due to unexpected charges.
- During the interview, respondents showed the interviewer the lenders that they had compared, and explained their decision-making process. Based on a comparison of the headline price, fees and administration charges, between two and three loans with similar repayment, the interviewer noticed when customers made an incorrect judgement. This, however, occurred in a very limited number of interviews.

finding out how much it would cost to borrow the amount needed from another lender. There is some evidence from our qualitative survey to suggest that comparisons may often be a 'very cursory experience', and that customers may face difficulties when trying to compare loans. Factors affecting customers' ability effectively to shop around for their loan are discussed in greater detail below.

6.28 These findings are consistent with the observation that lenders do not face a strong competitive constraint when setting their prices, and that this may be driven by the lack of responsiveness of customers to lenders' prices.

6.29 In response to our provisional findings, Wonga submitted that this 'does not necessarily support the conclusion that there is reduced pressure on lenders to compete to attract and retain customers. This constraint requires that a sufficient proportion of marginal customers might respond to a deterioration in competitive conditions by switching (to other products and/or other lenders)'.[398] We considered this argument carefully. Even assuming that the proportion of marginal customers willing to consider alternatives in response to a deterioration in competitive conditions (eg those who reported to have shopped around) would be sufficient to constrain lenders' strategies, the evidence (see paragraphs 6.26 and 6.69 to 6.92) indicates that when they try to shop around, customers encounter various difficulties which impede them from effectively identifying the best-value loan. We have seen no evidence suggesting that the factors limiting customer responsiveness to the price of payday loans – which we discuss in paragraph 6.46 onwards – do not apply to 'marginal' customers (ie those borrowers who are most likely to switch if lenders were to deteriorate their offer). Therefore we consider it unlikely that competition to attract marginal customers currently has an effective disciplining influence on lenders' pricing and product offerings, as suggested by Wonga.

The extent to which customers change lenders, and their reasons for doing so

6.30 As discussed in Section 2,[399] repeat lending to the same customer – whether in the form of taking out completely new loans, rolling over existing loans, or topping up – is pervasive, and accounts for a substantial proportion of the loans issued by payday lenders.

6.31 We also found that it is relatively common for customers to borrow from more than one lender (see paragraphs 2.46 to 2.50). Using information on a sample of customers selected from our transaction data set (see Appendix 2.2), we

[398] See Wonga's response to our provisional findings, paragraph 5.1.
[399] See paragraphs 2.43–2.45 and 2.52–2.56.

estimated that around four in ten payday loan customers borrowed from at least two different lenders during 2012, and that on average a customer borrowed from 1.9 lenders in a year. These findings were broadly consistent with the results of our customer survey.

6.32 This suggests that a substantial proportion of payday loan customers will have had some direct experience of the loan terms offered by more than one provider. In this section, we consider the factors underlying these patterns, and what drives payday loan customers to either change supplier or remain with the same lender.

Reasons for changing loan provider

6.33 Our analysis of borrowing patterns and our customer survey suggested that the use of multiple lenders by payday loan customers often takes place as a result of customers being constrained in their ability to borrow further amounts from an existing lender (see Appendix 6.2 for further details). We reached this view for the following reasons:

(a) First, we found that customers often use multiple lenders concurrently, ie taking out a new loan while an existing loan was outstanding with a different lender. Nearly all customers who used more than one lender 'multisourced' in this way on at least one occasion, and for many customers a large proportion of their loans were taken out concurrently. Typically, where a customer has a loan outstanding with a lender, we would expect their ability to borrow further amounts from that lender to be constrained. In particular, most lenders will not issue a customer a new loan if they already have a loan outstanding. Although in some cases customers who multisource their loan may have been able to meet their credit requirements via an existing lender by topping up a previous loan, this was unlikely to be the case for most occasions of multisourcing that we observed (see Appendix 6.2, paragraph 35, for further details).

(b) Secondly, we noted that customers may be constrained in their ability to return to a lender that they had previously used if they had experienced repayment problems with the previous loan. We found that the last loan a customer takes out with a lender is around ten times as likely never to be repaid compared with other loans.[400] In addition, responses to our customer survey suggested that about 70% of customers who had used

[400] Around two-thirds of 'last loans' are never repaid in full, compared with around 6% of loans that are not a customer's last loans.

multiple lenders had also experienced some form of financial problem[401] in the previous 12 months (compared with 42% of customers who had used only one lender).

6.34 Given this evidence, we took the view that the credit constraints facing borrowers are likely to be responsible for a significant part of the use of multiple lenders that we observe. We found that more than 95% of those occasions where customers used a different lender to the provider used for the previous loan occurred either *(a)* while a loan to an existing lender was being repaid and no further credit was available with the existing lender(s) or *(b)* following a repayment problem on a previous loan.[402] We estimated that less than 10% of customers in our sample had used different lenders for consecutive loans at least once during the course of a year where neither of these conditions applied and so where the customer was unlikely to have been constrained in their ability to borrow further from their previous lender.

6.35 The importance of credit constraints in driving borrowers to change lenders was also highlighted by our customer survey, although responses suggested that issues with credit availability accounted for a smaller proportion of the switching that we observed than was suggested by our analysis of borrowing patterns. In particular, when we asked those customers who had taken out loans from more than one lender in the past[403] what had caused them to go to another payday lender rather than borrow more from the same lender, a third of customers reported that they had not been able to go back to the same lender either because they already had an outstanding loan or because they would not be granted a higher/further loan by that lender.

6.36 At the same time, our customer survey also suggested that some customers had changed lender because they had a preference for a loan or service offered by another lender (30%). Other reasons, such as having had a bad experience with the previous lender, convenience or a personal recommendation, were cited less frequently.[404] Wonga told us [✂].[405,406]

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[401] Financial problems were defined as either *(a)* having been overdrawn on any of the customer's bank accounts, *(b)* having gone over the agreed limit on any of the customer's accounts, or *(c)* having been turned down for any types of credit.

[402] Wonga submitted that customers who did not repay loans were likely to encounter difficulties in taking out subsequent loans from any lender because their CRA credit record would include information indicating the unpaid loan. We note, however, that: *(a)* different lenders may have different strategies in relation to the customer risk profiles that they are willing to accept, and *(b)* the information available via CRAs suffers from a number of limitations (see paragraphs 7.103–7.107), which means that an alternative lender will generally not have as good visibility of a customer's repayment history as their previous lender.

[403] We did not ask whether the loans from different lenders were taken out simultaneously (ie multisourced), or one after another.

[404] Although not captured in the quantitative survey, the qualitative research suggests that sometimes customers use a new lender to repay other loans and avoid late payment fees.

[405] [✂]

[406] See Wonga response to the provisional findings, paragraph 5.10.

Reasons given for not changing lender

6.37 A significant proportion of customers in both our analysis of borrowing behaviour and our customer survey had taken out multiple loans, but had only ever used the same lender. We considered the reasons given by customers for remaining with the same provider.

6.38 Customers interviewed as part of our qualitative research indicated six key reasons for not switching lenders:

(a) they were generally pleased with the service they had received from the lender;

(b) a perception that lenders offered essentially the same deals;

(c) a reluctance to provide more information about themselves or proof of income;

(d) a concern that another lender might not accept their application and this might affect future loan applications;

(e) a concern that by being accepted by another lender they might be tempted to take out more loans than they could afford; and

(f) inertia brought on by having an account with a lender that made it easy to apply for further loans from it.

6.39 We explored the frequency with which these reasons were put forward by payday loan customers in our quantitative survey. Of those customers who had taken out more than one loan but used only a single lender (34% of the sample), only 15% had at some point considered going to a different lender, whilst a clear majority (85%) said that they had not considered using alternative providers.

6.40 When asked about the reason why they had not considered switching supplier, the majority (61%) of respondents asked this question[407] said that this was because they were happy with the service provided by the existing lender. Of the remainder, respondents cited the general ease/convenience of sticking with the same lender (11%), avoiding the need to go through a new

[407] Approximately 18% of the survey sample.

application process (6%), concerns about the likelihood of approval with another lender (4%) and that the current lender offered better terms (4%).[408]

6.41 For those customers who had used only one lender but had considered using an alternative provider,[409] again the most common reason given for deciding not to switch (36%) was because the customer was happy with the service provided by the current lender. However, in general these customers were more likely to cite other factors, such as the need to go through a new application process (13%), the general convenience of sticking with the current lender (12%), a preference for the terms offered by their current lender (12%) and concerns about the likelihood of approval with another lender (9%) as reasons for not switching, compared with customers who did not consider using an alternative lender.

6.42 Our qualitative research explored what customers meant when they said that they were 'happy with the service provided by the current lender'. In-depth conversations with customers indicated that customer satisfaction appeared to be related to the perception that the sector was potentially unsafe or that there were 'dodgy' lenders in the market. Therefore, using a lender with which a customer had previously had a good experience could reduce the perceived risk of having a negative experience in the future. A number of factors were cited as contributing to customers having a positive experience with a lender, including: an easy and quick application and approval process; having an account that could be logged into and did not require a customer to provide basic information again; being offered increased loan amounts; not being charged for paying late by a few days; and 'thank you' texts after repayment that make a customer feel valued.[410]

6.43 Where customers reported not having considered switching because they were happy with the service provided, there was some evidence to suggest that these borrowers were often not aware of the alternative products available in the market:

(a) The proportion of customers who had ever shopped around is significantly lower among those who had never considered changing the lender (29%) compared with the equivalent figure for customers who had either used

[408] A smaller proportion of respondents who did not consider changing supplier said that they saw no incentive to switch as they considered lenders to be all the same (3%), they never thought about other lenders (4%) and they were not aware of other lenders (1%).
[409] Approximately 5% of the survey sample.
[410] For high street customers a good experience means: the customer can build up a relationship with the outlet staff; where staff make the customer feel valued by being friendly, helpful, engaging and establishing a report; and by being a 'friend offering a helping hand'.

multiple lenders (53%) or considered changing supplier but did not do so (61%).

(b) Of the customers who did not consider changing supplier as they said that they were happy with the service provided by an existing lender, one in three (32%) had ever shopped around, whereas the equivalent figure is twice as large for customers who considered changing lender but did not do so.

Conclusions on customers' use of multiple lenders

6.44 A substantial proportion of payday loan customers have used multiple lenders, and so will have had some direct experience of the loan terms offered by more than one provider. To summarise the evidence that we reviewed on the factors driving customers' use of multiple lenders:

(a) The borrowing patterns that we observe suggest that where borrowers change lenders, this will often take place where customers are constrained in their ability to borrow further amounts from an existing lender (eg where customers already have a loan outstanding with a lender, or have experienced a repayment problem with the previous loan taken from a lender). However, our customer survey suggested that some switching also takes place where customers change lender because they prefer the product offered by another lender.

(b) For those customers responding to our survey who had taken more than one loan but had only ever used a single lender, the most common reason given for not changing or not considering changing lender is that they are happy with the service provided by their current provider. Our qualitative research suggested that satisfaction with levels of service provided by existing lenders generally stemmed from having had a positive experience in the past: customers were unwilling to switch away from a lender with which they had had a good experience previously, in part because of concerns about unsafe lending practices that may be used by other providers in the market. This is consistent with evidence that lenders have taken actions to improve their customer service in order to retain customers (see paragraph 4.213). Where customers reported not having considered switching because they were happy with the service provided, there was some evidence to suggest that these borrowers were often not aware of the alternative products available in the market. Other reasons given for not switching include the convenience of sticking with the same lender, avoiding the need to go through a new application process, concerns about the likelihood of approval with another lender and a preference for the terms of the existing lender.

6.45 Despite the frequent use of multiple lenders that we have observed, neither the threat of customers switching lender (to the extent that it exists), nor the fact that many customers have direct experience of different lenders' loan terms, appears to have resulted in lenders facing an effective competitive constraint when setting their prices. Evidence on borrowing patterns suggests that in part this is likely to be because the use of multiple lenders is often driven by concerns about credit availability rather than customers seeking out a better deal. In the next section, we consider how this and other characteristics of the payday market may act to impede customers from effectively comparing different loans and responding to variation in prices.

Potential factors limiting customer responsiveness to the price of payday loans

6.46 The discussion above indicates that although some shopping around does take place in the payday lending sector, and many customers have experience of more than one lender's products as a result of having used other lenders in the past, this is not sufficient (or sufficiently effective) to incentivise lenders to compete on price. We considered whether there were aspects of the payday lending market which might lead to this outcome, either by deterring customers from shopping around; impeding their ability to do so effectively; or deterring repeat customers from choosing an alternative lender for their next loan on the basis of its loan offering (rather than simply as a result of them being unable to return to a lender for further credit).

6.47 We began by noting that there are certain aspects of the payday lending market which – other things being equal – we might expect to help make borrowers responsive to the differences in the terms on which products are offered by different lenders:

(a) First, compared with some other financial products (such as, for instance, mortgages), payday loans are relatively simple and the TCC – universally provided by lenders – is a relatively easy way of comparing prices for a given borrowing scenario.

(b) Second, most customers borrow online, where information is generally relatively easy to access.

(c) Third, customers often take out large numbers of payday loans, which are by their nature generally short-term products. This suggests that customers have regular opportunities for learning about payday loan products and to change supplier if they could identify a better alternative (see paragraphs 6.30 to 6.32).

(d) Finally, as many payday loan customers are operating under tight financial constraints, they might be expected to place a relatively high value on any savings on the cost of borrowing that could be achieved by shopping around.

6.48 Notwithstanding the above factors, we identified a number of barriers to shopping around or switching which might explain why customers are unresponsive to variation in payday lenders' prices. These can be categorised as follows:

(a) the context in which the decision to take out a payday loan is generally made;

(b) difficulties that customers face in identifying the best-value offer;

(c) additional factors limiting customers' awareness of and sensitivity to late fees and other extra charges;

(d) the role played by lead generators; and

(e) the risk and loss of convenience perceived to be associated with switching lender.

6.49 With the exception of the issues related to the role of lead generators, which is specific to the online market, these barriers are likely to affect both online and high street customers. In what follows, we discuss each of these potential barriers in turn.

The context in which many customers decide to take out a payday loan

6.50 The first potential barrier that we identified stems from two common aspects of the context in which borrowers' decisions to take out a payday loan are often made. The first aspect is the perceived urgency of taking out a payday loan and the weight that customers place on being able to access credit quickly. The second aspect is the extent to which payday loan customers are uncertain about whether they will be granted credit to meet their borrowing requirements, and from which lenders credit is likely to be forthcoming. These factors, which we discuss in turn below, will tend to frame the way in which customers make decisions about the payday loan that they take out, and their attitude to shopping around and changing lender.

Perceived urgency of the loan

6.51 Payday loans are by their nature a short-term credit option, with most products allowing funds to be accessed quickly (often within a matter of minutes or hours). Payday loans are most commonly used for essential living expenses, often following an unexpected, temporary decrease in income and/or increase in expenditure.[411] Taken together, these factors suggest that the need for payday loans will often be perceived as urgent.

6.52 Related to this, there is evidence to suggest that being able to access funds quickly, once a need for credit has been identified, is important to both new and repeat customers:

(a) As part of our customer survey we asked respondents to indicate the importance of various product characteristics in the choice of payday loan. 'Speed of getting the money' was the factor most commonly emphasised, cited as very or extremely important by 74% of the respondents. When respondents were asked to choose a single factor as being the most important, speed was the most common single factor indicated by both online and high street customers, with (on average) 31% of respondents highlighting speed compared with around one in ten for most of the other factors.[412]

(b) The importance of speed to customers is also supported by consumer research carried out by lenders. For example, a survey commissioned by Wonga found that [✄]% of its customers indicated that the most appealing feature of Wonga's products is 'that it is faster than other lenders'. A survey commissioned by CashEuroNet in 2012 found that [✄] indicated speed of process as the most important driver of the provider choice (although CashEuroNet submitted that more recent evidence suggested that other factors were now more important drivers of product choice than speed because rapid availability of money was provided by all of the main lenders).[413]

(c) Our qualitative research suggested that the importance attributed to speed reflects the psychological state in which customers seek a payday loan[414] and in some cases the speed of application and accessing the

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411 See paragraphs 2.26–2.30.
412 Both new (26%) and repeat customers (35%) cited speed as the single most important factor.
413 Specifically, CashEuroNet referred to a survey from August 2013 which it said suggested that factors such as interest rates [✄] were now more important drivers of product choice than speed within the UK payday loan market. In CashEuroNet's view, this indicated that speed was a less important factor overall because rapid availability of money was provided by all the main payday lenders and therefore 'is not a driver of choice between different online payday loan options' (CashEuroNet's response to the issues statement, p5.)
414 The research identified a number of reasons explaining why customers attribute primary importance to the speed of the process and the speed of accessing the money: *(a)* customers feel they need the money now, in order to deal with their impending financial issue, with some describing themselves as 'panicky' at the time of applying; *(b)* they want to know that they have the money as soon as possible and that the financial issue they have been dealing with is sorted out; and *(c)* they want to get the process of application over as soon as possible so that they can 'return to normal'.

money 'trumps' the value of the deal, with customers in some cases saying that they paid more for a speedy 'peace of mind'.[415] Similarly, qualitative research conducted for BIS by Ipsos MORI found that customers tended to 'need money very quickly, or wished to get the uncomfortable act of taking a payday loan out over with as soon as possible' and this dissuaded them from researching lenders in detail.[416]

(d) Our qualitative research also suggested that the speed of the process may remain important even when the need for the money is more discretionary.[417]

(e) The customer research we undertook as part of our remedies process found that the speed of the application process and the time it took to receive the money were the most important aspects in customers' decision-making. Cost and flexibility were considered by some customers but the importance placed on speed outweighed considerations of cost.[418]

6.53 Lenders appear to be aware of the importance that customers attribute to speed as many of them highlight on their website and/or in the advertising campaigns the speed of the arrangement as a major feature of their offer (see Appendix 6.3 for further details).[419,420] The importance attached by customers to speed has led to the widespread introduction of faster payment services (FPS), which are currently offered by most lenders (see paragraph 4.202).

6.54 Irrespective of the actual time necessary to search for various offers available in the market, one consequence of the perceived urgency that customers attach to getting a payday loan is that borrowers may be unwilling to spend much, if any, time collecting information on different lenders' products and comparing them prior to taking out the loan.[421]

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[415] See TNS BMRB survey report, p93.
[416] See Payday lending advertising research conducted for BIS by Ipsos MORI Social Research Institute (October 2013).
[417] Customers can see payday loans as 'impulse purchases' and they are concerned that if they have time to rationalise their decision they may end up changing their mind about getting a loan ('the longer it takes the longer I doubt things, it was like an impulse thing', 'It's not something you've thought about, it's one of the quick things that you do'). See TNS BMRB survey report, p93.
[418] See TNS BMRB customer research, p11.
[419] Cash Converters submitted that it believed it was at a disadvantage to competitors who relied on credit searches to assess affordability whilst it required customers to complete a detailed income and expenditure form which it then matched with bank statements to verify income and ensure that all expenditures had been declared. It told us that this approach was time-consuming and customers often commented that they went to competitors who could provide them with funds more quickly.
[420] Wonga submitted that it did not consider that it emphasised the easy availability of loans and speed of arrangement but this was not given precedence over the total cost of borrowing (see Wonga's initial submission).
[421] Which? pointed to the results of the survey carried out as part of the Bristol Report which found that payday loan users chose a lender primarily on the basis of convenience and speed of application and payment. It submitted that the behavioural economics suggested that consumers might tend to discount heavily the future

6.55 This is corroborated by the findings of our customer survey, which indicate that the time pressure perceived by payday loan customers can restrict the extent to which they shop around. 'Not enough time to search' was the most common explanation given by respondents (both new and repeat customers) for not shopping around for their most recent loan (cited by 21% of these customers).[422] Among those customers who reported that they had shopped around, the lack of time was cited as the most common barrier to not comparing a larger number of lenders or spending more time comparing offers (cited by 34% of these customers). We also note that customers who regarded speed as being the most important factor when taking out a payday loan were less likely to report having shopped around prior to taking out the loan (see paragraph 6.19*(d)*).

6.56 In response to our provisional findings, Wonga noted the results of our follow-up survey that found that the majority of customers (73%) felt they had spent the right amount of time on shopping around for their most recent loan.[423] However, we note that more than half of these customers reported not having shopped around for the most recent loan at all (and around 40% not having shopped around for any other previous loan). This suggests that the responses to this question are not an especially reliable indicator of whether customers have in fact spent any significant amount of time shopping around, as many of the customers who reported to be satisfied with the time spent on comparing various offers had not apparently made any comparison.

Credit constraints and uncertainty about obtaining credit

6.57 Another key aspect of the context in which the decision to take out a payday loan is often made is that many customers are credit constrained, and as a result will face some uncertainty about whether or not a lender will approve them for a loan.

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cost of credit and as a consequence choose lenders that promise to pay out rapidly at the expense of offers with significantly lower interest rates.

[422] Both online customers (21%) and high street customers (22%) cited 'Not enough time to search' as the most common explanation for not shopping around for their most recent loan. We note that the customers who said that they could easily have gone without the loan (12% of those who did not shop around) cited 'happy with the first loan I looked at' as the most common reason cited (20%), whilst lack of time was cited less frequently (12%). Among those who said that they definitely could not have gone without the loan (62% of those who did not shop around), lack of time was the most common reason cited (21%).This suggests that the more customers consider the loan as indispensable the more they feel under time pressure to obtain a loan. Similar proportions of new customers (24%) and repeat customers (21%) cited 'Not enough time to search' as a reason for not shopping around for their most recent loan, suggesting that this aspect of the context in which customers take out payday loan is common to both customer groups.

[423] See Wonga's response to the provisional findings, paragraph 5.5.

6.58 The evidence we have reviewed suggests that uncertainty regarding credit availability may affect a significant proportion of payday loan customers.

6.59 First, while the average income of online payday loan customers is not dissimilar to the UK population as a whole, many payday loan customers nonetheless display characteristics indicative of relatively high levels of credit risk.[424] According to our survey, over half of payday loan customers were overdrawn in the last year (with around a quarter going over their agreed overdraft limit), and around 30% were turned down for another type of credit. Half of respondents said that they had experienced debt problems such as a bad credit rating or making arrangements to pay off arrears in the last five years.

6.60 Second, the rate of refused loans was often well above 50% for many of the major lenders (see Table 6.1 below) – and likely to be higher for first-time customers – illustrating that a significant number of prospective customers see their application refused. The rate of loan applications that were turned down has risen for some operators in the period January to September 2014 as lenders adjusted their decision criteria to accommodate changes implemented to the FCA's rules.[425]

TABLE 6.1 **Rate of refused loans* for the major lenders†**

Lender	*Brand (if data was provided separately by brand)*	*Rate of refused loans %‡*
CashEuroNet		[✂]
CFO Lending		[✂]
Dollar	PaydayUK	[✂]
	PaydayExpress	[✂]
	TMS	[✂]
Global Analytics		[✂]
H&T		[✂]
SRC	Speedy Cash	[✂]
The Cash Store		[✂]
TxtLoan		[✂]§
Wonga		[✂]

Source: CMA analysis.

*The rate was calculated as the proportion of refused loans over the completed applications.
†Some lenders did not provide this information, namely: Ariste and Wage Day Advance (SRC).
‡The rate of refused loans varies significantly by lender, in particular high street lenders ([✂], Speedy Cash (SRC) and The Cash Store) have on average a significantly lower rate of refusal than online lenders. This may be because high street customers are rejected even before submitting an application as they do not satisfy the minimum requirements. These customers may not be accounted for in the calculation of the rate of refusal.
§[✂]

6.61 Third, our analysis of borrowing patterns (see paragraphs 6.33 to 6.35) suggested that a large proportion of borrowers use multiple lenders, and that a key reason for this is likely to be the credit constraints facing many

[424] See paragraphs 2.23 & 2.24.
[425] See Section 3 for changes to rules regarding the verification of creditworthiness and affordability, rollovers and CPA use.

customers. In particular, we found that a large proportion of those customers changing lenders already have a loan outstanding with a previous lender, or do so following repayment problems with a previous loan.

6.62 Payday loan customers facing uncertainty and expecting that some lenders are likely to refuse to grant them a loan would need to go through an application process in order to establish whether any given lender would be willing to lend to them. When coupled with the perceived urgency surrounding the decision to take out a payday loan (as well as the possibility that customers may be discouraged from applying to multiple lenders by the perceived impact on their credit record),[426] this may result in customers primarily choosing their loan on the basis of which lender they think will approve their application, rather than the merits of a particular lender's product.

6.63 We also noted that some borrowers may be discouraged from applying to multiple lenders by the perceived impact on their credit record. This is often with good reason. Lenders and CRAs told us that the presence of (application) searches on a customer's credit record was a factor commonly used as a risk indicator.[427] Although a similar pattern may also arise when a potential borrower searches the market for the best-value loan product available, a large number of searches may indicate a credit-hungry potential borrower, seeking credit from multiple sources at the same time.[428,429]

6.64 One consequence of the importance of credit availability to payday loan customers is the widespread use of credit brokers – and in particular lead generators – which seek to attract customers on the basis of high acceptance rates and the offer that they will find customers a lender willing to grant them credit. The implications of the role of lead generators for competition to attract customers on price are considered further in paragraphs 6.100 to 6.111.

6.65 Uncertainty may also affect the behaviour of repeat customers, who – having been approved for a loan by a lender in the past – are likely to expect to be approved if they seek to borrow a further amount from that same lender in the future (assuming they had not defaulted on the previous loan). In contrast, a customer is likely to face greater uncertainty about whether or not they will be

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[426] Lenders typically use data from CRAs to assist in making their lending decision, which requires some form of credit check. There are two types of credit check: *(a)* 'enquiry' or 'quotation' searches which do not leave a visible 'footprint' on a customer's credit file (ie that a third party lender can see that a search has been performed by another lender), and *(b)* 'application' or 'credit' search which do.
[427] See Appendix 9.2, paragraphs 126–139.
[428] See Appendix 9.3 for further explanation as to why lenders may perceive increased risk as the number of application searches rises.
[429] For example, one lender ([✂]) submitted data showing a close link between the acceptance rate of customers and the number of credit searches undertaken.

approved for a loan if they apply to an alternative lender, which may take different factors into account in its credit assessments, and will generally not have access to detailed information on that customer's repayment history.[430]

6.66 In this context, looking at those repeat customers in our customer survey who had only used one lender, some respondents attributed their ultimate decision not to change lender (or not to consider doing so) to the higher likelihood of being approved by the current lender (see paragraphs 6.40 and 6.41). Although this was mentioned by a limited number of customers,[431] when considered together with the other evidence described in paragraphs 6.37 to 6.43, it provides a further indication that uncertainty about approval is a material concern for payday loan customers. Cash Converters told us that payday loan customers typically had been turned down for other financial products (eg credit card, store card, etc) and when they eventually found a lender willing to lend, 'they do not want to move out of that comfort zone, for want of a better term, because they have been turned down so many times before'.

Conclusions on the impact of urgency and uncertainty

6.67 To summarise, the evidence we reviewed suggests that:

(a) When taking out a payday loan, customers often perceive their loan to be required urgently, and attach considerable importance to the speed with which they are able to access the credit.

(b) Many payday loan customers are also uncertain, often with good reason, about whether they will be granted credit to meet their borrowing requirements and from which sources credit is likely to be forthcoming, and they may be concerned that applying to multiple lenders would have an impact on their credit record.

6.68 These factors will tend to make customers reluctant to spend time shopping around for the best deal available, and will cause customers to focus on which lender is more likely to lend to them (or, for a repeat borrower, to stay with a lender that they previously used) rather than which lender offers the best

[430] In its response to the provisional findings (paragraph 3.13), CashEuroNet submitted that our analysis of the variables affecting the customers' propensity to shop around suggests that customers who were rejected for a previous loan were more likely to declare that they have shopped around in the past. However, as noted in Appendix 6.1 (paragraph 16), this may reflect some customers having previously had to search for alternative lenders that would approve their application rather than shopping around with the intent of finding the best value loan.

[431] We note, however, that our survey did not directly ask whether uncertainty about approval affects customers' propensity to shop around.

value product. This is likely to reduce the responsiveness of borrowers to variation in lenders' prices.

Difficulties associated with identifying the best value payday loan

6.69 The second barrier that we identified related to impediments to customers' ability to identify the best-value loan for their requirements. As set out in the Guidelines, access to information about the products available in the market and customers' ability to identify which offer provides the best value are key elements in driving effective competition.[432] Where customers perceive their need for a loan to be urgent, are concerned about their willingness to obtain credit and need to take a decision rapidly (see paragraph 6.67), any factor that makes it more difficult to compare loans is likely to magnify the search costs that they face.

6.70 We carried out a review of the websites of online payday lenders as of April 2014, the results of which are set out in detail in Appendix 6.4. We found that in general the key information about different lenders' products is available and presented on their websites (with some exceptions related to information about late payment and default fees, which are discussed in further detail in paragraph 6.97). In addition, our customer survey suggests that of those customers who have ever shopped around for a payday loan, more than eight in ten said that it was easy to find information to compare lenders' offers and that the information they looked at was very or fairly clear.[433]

6.71 Despite information generally being available, we found that customers' ability to identify easily the best-value loan for their needs may be impaired by a number of factors:

(a) While the basic payday lending product is generally relatively straightforward, there are also significant elements of complexity involved in comparing the cost of different payday loans in different scenarios. This can make it difficult for customers to make effective comparisons.

(b) Identifying the different lenders available on the market and their relative prices can be difficult, given that the provision of comparison websites listing different suppliers and cataloguing their prices is at present undeveloped in the payday lending sector, and those sites that do exist often suffer from important limitations.

[432] The Guidelines, paragraph 296.
[433] See TNS BMRB survey report, p108.

Complexities associated with making comparisons of the prices of payday loans

6.72 As set out in paragraphs 4.6 to 4.13, as borrowing criteria such as loan amount, duration and customer repayment behaviour change, the price that a customer pays for a payday loan may also change substantially. This can make it difficult for customers to make effective comparisons between different payday loan products.

6.73 Specifically, despite the relative simplicity of payday lending products (see paragraph 6.47*(a)*), such complexities can arise because different lenders often:

(a) offer products with different rules and levels of flexibility regarding loan duration;

(b) have different approaches to finance charges (eg daily versus monthly interest rates);

(c) use different pricing structures when a borrower does not repay on time (eg different combinations of fixed charges and interest rates); and

(d) are subject to other differentiating factors with implications for the cost of borrowing, such as the ability to repay in instalments, roll over a loan or top up during the term of the loan.[434]

6.74 Comparing the price of payday loans is likely to be particularly difficult if borrowers seek to compare traditional payday loans with 'non-standard' products (eg instalment loans) or if they seek to take into account the risk that they repay late.

6.75 In Section 4 we found that the ranking (according to the TCC paid by the customer) of a sample of the payday loan products offered by the major lenders varied significantly depending on the specific borrowing scenarios considered (see paragraphs 4.33 and 4.34). This indicates that, when comparing different products, the process of identifying the cheapest or best-value payday loan can be complicated for borrowers that have some flexibility around the length of time over which they wish to borrow, or who seek to take into account the risk of repaying late.

6.76 In other credit markets (eg mortgages, credit cards), the APR is often used as a common metric by which the relative price of products may be assessed, thereby reducing the difficulties customers face in making comparisons

[434] See Appendix 2.1.

between products with different pricing structures. The regulatory framework for consumer credit generally seeks to enhance the role of the APR by setting common rules for its calculation and for its use in financial promotions (see Appendix 3.1 for further details). For example, where an advertisement includes an amount relating to the cost of a credit product, the advertisement must also show the representative APR and must give more prominence to the APR than to any of the other financial information presented (including any other rate of charge, comparative indication, the total amount payable, etc). Lenders must also ensure that the advertised APR reflects the price at or below which the lender reasonably expects credit will be provided pursuant to at least 51% of agreements entered into as a result of the advertisement.

6.77 We considered the role of APRs in aiding comparisons in the payday lending market. Evidence from our customer survey suggested that customers were more likely to look at the total cost of the loan than making comparisons on the basis of APRs. For example, nine in ten respondents to our customer survey (89%) looked at the total amount repayable before taking out a loan, compared with around two-thirds (68%) that considered the APR.[435] Qualitative research conducted by Ipsos Mori for BIS found that many borrowers view the APR as irrelevant, 'as they intended the loan to be short-term, and were more interested to know the "fee" – or the amount they would pay if the loan was paid back in a month'.[436]

6.78 One likely reason for customers considering APRs of limited usefulness is that the APR for short-term loans is very sensitive to the duration of the loan. This can make comparisons using APRs based on representative examples difficult, as these interest rates will vary considerably depending on the representative loan duration chosen by each lender. The usefulness of APRs for comparisons will be particularly limited if the customer's borrowing requirements do not closely match the representative example – for example, if the borrower wants to take out a loan for a shorter duration, or wants to compare the cost of different loans in the event that they are repaid late.

6.79 A number of lenders also highlighted problems arising from the application of the APR rules to payday loans. For example:

(a) Wonga noted that the APR may mislead customers and make them 'think that the company with the highest APR is actually the highest priced'

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[435] See TNS BRMB survey report, p109.

[436] TNS BMRB remedies customer research found (see p20) that when looking at PCWs, borrowers compared loans on both the total cost and the APR but they generally did not understand the APR.

while, for example, a shorter loan, even if it had a higher APR, may have a lower cost of credit.[437]

(b) Wonga also told us that because of the nature of payday loans the resulting APRs are significantly higher than 'what people think of as a normal kind of interest rate'. This may have repercussions on the brand image of the lenders.

(c) Elevate told us that it faced difficulties in marketing its risk-based pricing, which offered lower monthly interest rates of 15% to low-risk customers. At that point in time, fewer than [✂]% of its customers received rates of 15% on their first loan while the majority still received an interest rate of 29%, so the 15% interest rate could not be reflected in the advertised APR. Elevate said that while it could have two representative APRs on the main page, this would confuse customers who would not know which interest rate was applicable and this might ultimately lead to disappointment when customers were not granted the lowest rate.

(d) CashEuroNet told us that in relation to risk-based tariffs, it would face difficulties to target low-risk customers with advertisements specifically promoting the cheapest price charged to this group of customers, as it expected that the ASA would require it to specify the exact rates it had (ie. not conditional to the relative risk of a customer).[438]

6.80 In light of the above evidence from customers and lenders, we concluded that the regulatory obligations on lenders to disclose representative APRs were unlikely to be of much, if any, assistance to customers in making comparisons between payday loans. Instead, the most useful basis for customers to make comparisons between payday loans is likely to be on the basis of the monetary cost of a loan in relation to specific scenarios of relevance to the customer (consistent with the analysis set out in Section 4). We also recognised the challenges that could be posed for lenders seeking to advertise risk-based prices, given the regulatory requirement to include a representative APR in the advertisement or promotion, though we also appreciated the need to ensure that advertising about payday loans does not mislead customers as to the price that they are likely to pay.

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[437] It added that:

> in many of the press articles where they will show a table where they have a list for £100 loan what the total cost of credit is but also what the APR is and on many of those tables we actually will be lower on the total cost of credit but we are the highest on annual percentage rate and it is because we are fully abiding by the laws of how to calculate that and so it is more looking at tables like that that are out there in the press and recognising that unfortunately people will see the higher APR and get scared off.

[438] CashEuroNet said that it '[✂]'.

6.81 Nevertheless, we did not consider that the disclosure of the APR was without value for payday loan customers. In particular, given the large number of loans taken out by many customers in a 12-month period (see paragraph 2.48) and the historically high use of rollovers to extend the effective term of a loan, we took the view that the disclosure of an APR can provide an indication of the cumulative cost of taking out multiple payday loans over the course of a year, or of repeatedly extending a short-term loan over a longer period.

Availability and functionality of price comparison websites

6.82 In many markets for financial products, PCWs play a key role in helping customers who are shopping online to compare the offering of different suppliers.[439]

6.83 The evidence we have collected indicates, however, that payday loan customers make only limited use of online price comparison services:[440]

(a) Information submitted by the major lenders suggests that only a very small proportion of customers apply through comparison websites. Based on data submitted by a number of the largest online lenders,[441] only 1.4% of customers[442] taking out their first loan with a lender in 2013 came through PCWs (although there is some variation between lenders, the proportion of customers acquired via PCWs websites is never above 4%).

(b) Our customer survey indicates that 42%[443] of customers who shopped around for their most recent loan or had previously done so reported having visited a PCW.[444] This is significantly less than the proportion of

[439] See, for instance, the customer research commissioned by the FCA (November 2013) in relation to the sale of home, travel and motor insurance through PCWs. The research found that many participants identified significant benefits from using a PCW and 'there was little doubt' that they encouraged consumers habitually to 'shop around' for the lowest-cost general insurance quotes they could find. The PCWs were perceived to allow consumers to achieve in minutes what would otherwise take hours, and make a potentially boring and difficult job relatively painless by presenting complex information in a simple and accessible way (see Appendix 9.2, paragraphs 77–78).
[440] While comparison websites are more likely to be used by online customers, high street customers may also be expected to benefit from a wider availability of online comparison websites. In its report, TNS noted that 'those taking out high street loans still often used online methods to compare' (see TNS BMRB survey report, p101). Of those high street customers who shopped around, visiting the websites of payday lenders was the most common source of information (61%) and visiting comparison websites was mentioned by 22% of those customers.
[441] We asked the 11 major lenders to provide information on the number of new customers coming through various channels. The figures in paragraph 6.83*(a)* are based on the responses provided by Wonga, CashEuroNet, H&T, Ariste, SRC, Lending Stream and MYJAR.
[442] For comparison, in another current investigation, the CMA found that PCWs have become an important sales channel for car insurance and they now account for [55–65]% of all new business sales in 2012. See *Private motor insurance market investigation: Final report* (paragraph 5.32).
[443] 45% of the online customers and 22% of the high street customers.
[444] Approximately 17% of the entire sample.

customers who used lenders' websites (89%) and advertising (57%) as sources of information.[445,446]

6.84 An important reason for this finding is the fact that the availability of PCWs for payday loan products has been limited so far. None of the four largest UK operators of PCWs for financial services[447] – www.moneysupermarket.com, www.gocompare.com, www.comparethemarket.com and www.confused.com – currently covers payday loans (although www.moneysupermaket.com operated a payday loan comparison site until spring 2013[448]).

6.85 www.money.co.uk is currently the largest PCW for payday loans,[449] [✂]. www.money.co.uk told us that most visitors clicked on one or two lenders' products when using the comparison tables, although a small number of visitors will follow the links to a large number of lender websites. It also told us that pay-per-click was the only advertising channel that it used for payday loans [✂].[450]

6.86 Other than www.money.co.uk (which appears prominently in search results for payday-related terms), other comparison websites tend to rank relatively low in payday-related search results, and generate significantly lower volumes of traffic. For instance, www.allthelenders.co.uk told us that the total number of clicks to payday loan products on its page was approximately 500,000 in 2013 and that it made no investment in advertising.[451]

6.87 We considered the reasons why comparison websites are relatively undeveloped in payday lending. These reasons appear to be primarily related – either directly or indirectly – to the reputation of the payday lending market:

(a) Moneysupermarket.com told us that it withdrew its payday loan page partly as a result of the increasing level of media and political scrutiny into payday lender practices, and the perception of non-compliance in the sector (see paragraph 2.156).

(b) Another mainstream PCW ([✂]) told us that [✂].

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[445] Both new and repeat customers use comparison websites as a source of information less often than visiting lenders' websites and seeing advertising, though new customers appear to rely on comparison websites slightly more (50%) than repeat customers (40%).
[446] Our qualitative research suggests that some customers were unaware of PCWs and because of this, they were not able to compare lenders' offer like with like.
[447] See Mintel report *Web Aggregators in Financial Service*', UK, July 2011.
[448] See paragraph 6.87*(a)*.
[449] [✂]
[450] SRC stressed the importance of advertising ('whether it is conventional media or through pay-per-click and SEO strategies') as a key factor to attract visitors to the comparison website. With the exception of money.co.uk, we have seen little evidence of other comparison websites investing to enhance their visibility.
[451] It said that all the traffic was generated from search engines, primarily Google.

(c) Some operators of mainstream PCWs, operating in a number of sectors, had concerns over the impact of offering comparison services for payday loans on their core existing business. These concerns related to restrictions known as 'Consumer Advisories' on paid search imposed by Google AdWords.[452] Under this policy[453], Google restricts advertisements relating to payday lending from appearing in response to a user search unless the search contains the words 'payday loan' or payday-loan-related terms.[454] Google told us that the Consumer Advisory does not prevent PCWs advertising other services on AdWords while also operating a payday loan comparison service under the same brand. Advertisers could segregate their payday loan content on a specific sub-domain of their general site, enabling AdWords advertisements for the rest of the site to show in response to non-payday-lending search terms.[455] Notwithstanding this, we noted that this rule has been widely perceived as being a significant deterrent for mainstream PCWs offering payday loan price comparison tables. Some PCWs' operators told us that they had either had to cease offering payday loan comparison services to ensure their other revenues were not put at risk (as a result of being prevented from using paid search) ([✄]) or had had their paid search account suspended for not appropriately segregating payday comparison tables ([✄]). A number of lenders shared the same concerns.[456,457]

(d) Some lenders reported having considered developing a comparison website, but had eventually abandoned the idea. CashEuroNet said that [✄]. Elevate pointed at the risk that a comparison site built by an individual lender would lack credibility.

6.88 Where online borrowers do use PCWs, these individuals are often offered promotional rates, suggesting that these websites have the potential to increase price competition between lenders to attract those customers that

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452 Google told us that the Consumer Advisory policy was meant to ensure that users searching for other products and services were not targeted by advertisers of payday loan products.
453 Introduced in 2011.
454 See Google response hearing summary, paragraph 3.
455 Google noted that, for instance, money.co.uk was able to operate in this way. In light of Google's comment and money.co.uk's experience we considered that there may be ways in which mainstream PCW operators might be able to reconfigure their websites in order to comply with Google's Consumer Advisory rule. Nonetheless, we noted that this rule is widely perceived as being a significant deterrent for mainstream PCWs offering payday loan price comparison tables.
456 Dollar emphasised the role played by search engines, in particular Google, in regulating and controlling the amount of traffic that a website received. In its view, the risk of experiencing repercussions on the total traffic generated by the website influenced the decision by moneysupermarket.com to drop its payday loan page. Wonga noted the potential difficulty of a generic PCW hosting payday lending comparison tables due to advertising rules imposed by search engines (see response to the Remedies Notice, paragraph 3.20). Uncle Buck also noted that a key challenge for PCWs would be to ensure that the website was not 'blocked' or impeded in its promotion or awareness by the actions of search engines (see response to the provisional findings, p1).
457 See Appendix 9.2.

use them. For example, Wonga used to waive its transmission fee to customers coming through the moneysupermarket.com comparison website. In 2012/13,[458] Dollar's PaydayUK and Payday Express offered a discounted monthly interest rate of 25% to customers referred from moneysupermarket.com.[459] [✂]

6.89 We note that the payday loan PCWs that currently exist suffer from some important limitations:

(a) These websites typically do not allow customers to adapt the search criteria in order to compare loan terms for a given set of borrowing criteria. Instead, products can generally only be ranked on the basis of one or two standardised measures of price (eg APR or TCC for a scenario that may not be consistent across all products), which may not reflect a borrower's requirements, or the range of possible outcomes. Related to this, our qualitative research found that where comparison sites were used, consumers did not find them particularly helpful. This was because comparison sites did not compare 'like-for-like' loans and as a consequence comparison was very difficult. This limitation was also raised by a number of lenders. For example, Wonga told us that comparison websites [✂] tended to compare a standard product but did not allow flexing the search criteria. Elevate said that currently there was no comparison website which enabled customers to evaluate loans on 'easily measurable factors' and compare loans 'based on what happens if things do not progress as the consumer may hope'.[460]

(b) Some comparison websites, such as whichwaytopay.com and money.co.uk, include lead generators among the providers listed in their comparison tables. The prices listed for these lead generators will not necessarily reflect the actual price that customers would pay if they applied through a lead generator (see paragraphs 2.129 to 2.154 for further details on lead generators). [✂] noted that PCWs may be listing the lowest possible price for a lender that the lead generator may source despite sourcing only a small proportion of the leads to this lender.[461]The order in which various products are presented by comparison websites (and even which products are displayed to customers at all) may not solely depend on the relative prices of the products or other factors of importance to customers. For example, [✂]. WizzCash told us that one major concern with comparison websites was that they did not necessarily rank lenders

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[458] Until spring 2013 when www.moneysupermaket.com withdrew the payday loan page from its website (see paragraph 6.84).
[459] See Price over time presentation, slide 24.
[460] See Think Finance response to issues statement, p3.
[461] [✂]

according to the APR but rather according to what they were prepared to pay per click. Along the same line, MYJAR said that some comparison websites worked not too dissimilarly from lead generators as 'the more you pay, the higher you end up in the list'.

(c) The comparison websites that do exist include only a subset of payday lenders. For example, as of 22 April 2014, www.whichwaytopay.com listed 25 providers. www.allthelenders.co.uk offered somewhat better coverage with 38 lenders. www.money.co.uk listed 20 products.

6.90 Comparative advertising may act – to some extent – as a substitute for PCWs in bringing comparisons between payday loans to customers' attention. However, we saw very little evidence of comparative advertising being used by payday lenders.[462]

Conclusions on customers' ability to identify the best-value payday loan

6.91 To summarise, the key information about lenders' products is generally available on their websites, or in the shops of high street lenders. However, customers' ability to use this information to identify the best-value payday loan is likely to be impeded by:

(a) the complexity associated with making effective price comparisons between payday loans, given variation in product specifications and pricing structures, and the limited usefulness of the APR in facilitating such comparisons; and

(b) the limited availability of online comparison services for payday loans and the limitations of those comparisons sites that currently exist.

6.92 The consequence of this is that customers who do seek to carry out comparisons on the basis of price may struggle to identify the best-value loan on offer; moreover that difficulty, in combination with the perceived urgency affecting many customers and the overriding importance of finding a supplier that is willing to lend, may deter some customers from shopping around at all. This

[462] The only two examples that were submitted to us were: *(a)* a leaflet provided by The Money Shop which advertised a cash-back promotion under which customers were offered £5 cash back per £100 borrowed for loans paid back in full and on time, and which included a comparison of the cost of £100 loan for 28 days repaid on time with Cheque Centres, Cash Converters and Wonga; and *(b)* a campaign used by CashEuroNet which presented side-by-side comparison between its own products and Wonga's Little Loan product. One campaign compared QuickQuid's Payday product with Wonga's Little Loans and mainly stressed the differences in relation to: the APR and the total amount repayable for a £250 loan for 30 days, the fee for fast funding, the maximum amount of loan that new (and repeat) customers can borrow and the offering of a loyalty programme. A second campaign compared Pounds to Pocket product with Wonga's Little Loans where mainly non-price factors were emphasised: loan duration, maximum amount of loan, the speed of funding, and the fee for faster funding.

will in turn reduce the responsiveness of customers to the prices offered by different lenders.

Additional factors reducing customers' sensitivity to late fees and other charges incurred if they do not repay a loan in full on time

6.93 The third potential barrier relates to factors which reduce the extent to which payday loan customers take into account, when choosing their loan, potential costs of late fees and other charges incurred if customers do not repay a loan in full on time.

6.94 Late repayment and default are relatively common among payday loan customers. Of the loans issued by the 11 major lenders in 2012, 14% were never repaid in full, and 22% were repaid in full after the originally agreed repayment date (although some loans in this latter category may have been subject to an agreed extension).[463] We estimate that fees specifically related to late payment/default accounted together for approximately 5% of lenders' revenues in 2012. Late payment/default fees, however, represent only part of the revenue generated in cases of late payment as they do not include the interest that continues to accrue beyond the repayment date.[464] Late fees and other charges incurred by customers when they repay a loan after the due date are therefore a common additional cost for customers and a source of revenue for lenders.[465]

6.95 The evidence we collected suggests that customers are in general less well informed about fees and charges incurred if they do not repay a loan in full on time than other aspects of the cost of the loan, and are less likely to factor them into their choice of lender:

(a) Two-thirds of all respondents said that when taking out the loan they looked at the cost they would incur if they did not repay on time. This is significantly less than the proportion of the respondents who reported having looked at information on the total cost of the loan (89%).[466] We also note that only around half of those customers who were not very or not at all confident in their ability to repay the loan (and therefore might

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[463] The FCA found similar figures. Of the loans issued in 2013 by 8 of the 11 major lenders, 17% were repaid late and a similar proportion were never repaid in full (see CP14/10 Technical Annexes supplement, p26).
[464] The data provided by lenders does not allow separating accurately the revenues generated by headline interests and those generated by late payment interests.
[465] Some lenders told us that they did not always charge late payment/default fees. For example, SRC submitted that of the late fees chargeable in the last 12 months, 17% were waived. [✂] Nonetheless, as noted in this paragraph, the amounts actually charged to customers through late fees and interest are clearly substantial.
[466] This holds true for new and repeat customers as well as for online and high street customers (though the proportion of high street customers who reported having looked at information on the total cost of the loan is lower (76%) than the average across the sample).

expect to end up paying late payment fees) looked at the late payment fees prior to taking out their loan; less than the proportion of customers who were more confident in their ability to repay.

(b) Of those customers who reported having shopped around for a payday loan,[467] 63% compared information on the late payment fees. This is significantly less than the proportion of customers who reported having gathered information on the total cost of the loan (92%), the speed of the process (83%) or the amount that they could take out (80%) when shopping around.[468]

(c) Similarly, the Bristol Report[469] found that while 80% of high street payday loan customers considered the total amount they had to repay (including the original amount borrowed) when they took out the loan, fewer than one in two customers (42%) looked at 'other fees or charges, such as early resettlement or penalty charges'.

(d) The results of our qualitative research suggested that some customers became aware of late payment fees only if they ended up paying them.

(e) Of the customers in the contemporaneous sample[470] who failed to repay on time and who are therefore most likely to have incurred late payment fees, 36% considered that they had not spent enough time looking at costs and charges when taking out the loan; significantly higher than the equivalent figure for the customers who repaid on time (10%).

6.96 One characteristic which could prevent payday loan customers from taking the fees charged in case of late payment/default into account when choosing their loan is if they are overconfident about their likelihood of repaying the loan on time. There was some evidence from our customer survey to suggest that customers underestimate their likelihood of repaying late:

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[467] 40% of all respondents (see paragraph 6.15).
[468] These figures are similar for both repeat and new customers. 69% of the new customers and 62% of the repeat customers compared the late payment charges of various lenders. For both types of customers this figure is significantly lower than the proportion of the respondents who reported having gathered information on the total cost of the loan, the speed of the process or the amount that they could take out.
[469] The Bristol Report, Table 5.3.
[470] The contemporaneous sample was made up of customers who had taken out loans on four specific dates in October and November 2013. The objective of the contemporaneous sample was to speak to customers very soon after their loan repayment dates so as to 'get closer to the mindset of customers at the point the loan was taken out' (see TNS BMRB survey report, p8).

(a) Although around 20% of respondents[471] reported having failed to repay in full by the repayment date,[472] almost all customers (95% of respondents) recollected[473] having been very or fairly confident of being able to repay on time[474] at the time they took out the most recent loan.

(b) Among customers who had failed to repay in full by the repayment date, more than 80% reported having been very or fairly confident of being able to repay on time at the point at which they took out the loan.

(c) Given their greater experience, we might expect repeat customers to be better at anticipating the risk of not being able to repay on time. However, our survey shows that, although 14% of repeat customers failed to repay in full by the repayment date, 94% of these borrowers reported that they had been very or fairly confident of being able to repay on time when they took out the most recent loan.

(d) Around half of customers who failed to repay on time said that the total repayment amount was more than they expected when the loan was taken out, whereas only 13% among those who repaid in full by the repayment date said that they paid more than they expected. Commenting on this finding, TNS noted that this might be due to customers either misunderstanding the repayment amount (which might in turn have been a factor in their failure to repay) or not including the late payment charges in their original understanding of what they would need to repay.[475]

6.97 Further, there was evidence to suggest that customers' ability to take late fees into account when choosing their loan may be affected by limitations in the information provided by lenders regarding these charges. In particular, although the key information about loan terms, including default and late charges, is typically available on each lender's website, in our review of lenders' websites as of April 2014 (discussed in Appendix 6.4) we found that:

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[471] This figure is based on those customers whose repayment date had passed at the time of the interview. These customers represent almost 80% of all respondents.
[472] Which? submitted the results of a survey conducted in August 2012 according to which almost half (48%) of the payday loan users had taken out credit in the past that it turned out they were not able to repay. (See Which? Response to issues statement, p2.)
[473] Question QPDSI3 of the CC survey: 'Thinking back to when you first took the loan out, how confident were you that you would be able to repay the loan in full on the date originally agreed with [name of the lender]?'
[474] Of those who said that their need for a loan was due to a change in financial circumstances (80% of the respondents), nine in ten expected this change to be temporary.
[475] TNS BMRB report, p120.

(a) Late payment/default fees are typically not presented on the initial page displaying the TCC.[476] This implies that customers have to make an additional effort in order to find out information on these fees.

(b) There were some examples (Short Term Loan (CFO Lending) and PaydayUK (Dollar)) where late payment fee information on lenders' websites is unclear or not complete.[477]

(c) There are also some instances where these fees are presented in a smaller or less prominent font than other information shown on the website. This is the case for PaydayUK (Dollar) and Cash Genie (Ariste).[478]

6.98 Moreover, we noted in Section 4 (see paragraph 4.13) that the pricing structure of late interest charges varies significantly across lenders. This is likely to make it difficult for any customers who do seek to take late fees into account to compare different offers, particularly given the limited availability of effective online comparison tools.[479]

Conclusions on customers' sensitivity to fees and charges incurred if a customer does not repay a loan in full on time

6.99 To summarise, we found that a combination of the limitations in the information provided by lenders regarding late fees, the difficulty in making comparisons given lenders' different charging structures and a tendency among some customers to be overconfident about their ability to repay means that customers generally do not take these charges into account when choosing their loan. Customer demand is therefore particularly unresponsive to variations in the charges incurred if a customer does not repay a loan in full on time. This is consistent with the evidence on market outcomes (discussed in paragraph 6.10), which indicates that a particularly high degree of variation in prices has been observed in scenarios where a borrower repays their loan late, and that lenders have not been particularly concerned about the impact on demand for their product when setting their late fees.

[476] See Appendix 6.4, paragraph 14.
[477] See Appendix 6.4, paragraph 15.
[478] See Appendix 6.4, paragraph 16.
[479] See paragraphs 6.82–6.89.

The role of lead generators

6.100 The fourth potential barrier that we identified was the impact on online suppliers' incentive to compete on prices of the large proportion of payday loan customers that use lead generators to find their lender.

6.101 Many online payday loan customers take out a loan via a lead generator, rather than going directly to a lender. Based on a sample of customers – those taking out their very first loan from one of the 11 major lenders between June and August 2012[480] – we estimated that around 40% of customers acquired at least one loan via a lead generator, and almost a third of these borrowers (12%) used a lead generator more than once.[481] As shown in Figure 6.1, the proportion of new customers sourced from lead generators varies significantly across the major online lenders – for many lenders, nearly all new customers are acquired via a lead generator.

FIGURE 6.1

Proportion of new customers sourced from brokers/lead generators by lender

[✄]

Source: CMA analysis of transaction data.
Notes:
1. Sample: we used the information on customers from the 11 major lenders, who took out at least one online payday loan and took out their very first payday loan between June and August 2012.
2. The figures for CashEuroNet have been derived using its response to the Market Questionnaire (as transaction-level data on whether customers were sourced via lead generator or broker was not available).

6.102 Lead generators[482] auction customer application details to a panel of lenders, typically selling the lead to the lender which offers them the best commercial terms (eg the lender which is willing to pay the highest amount for that applicant – this process is discussed in greater detail in Section 2). This auction process increases the probability of a customer being able to find a loan compared with a situation in which they applied to a single lender – essentially allowing customers to apply to multiple payday lenders simultaneously.

6.103 In line with this and the importance of credit availability to many payday loan customers (see paragraphs 6.57 to 6.66), our review of lead generators' websites as of May 2014 found that it was common for lead generators to

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[480] For further details see Appendix 6.5.
[481] Among these first-time customers there will be borrowers who have taken out payday loans with another lender previously (see Appendix 6.2, paragraph 29).
[482] In this context we refer to pingtree operators. Lead generators more generally include any party that acts as an intermediary between borrowers and lenders by collecting and passing to providers of payday loans details, including personal contact information, of individuals seeking loans including pingtree operators and affiliates. See Appendix 2.7 for further details.

emphasise high acceptance rates or target individuals with bad credit ratings on their websites or in their advertisements. For example, Google Adword text used by those lead generators that appears most often in the first pages of results generated by Google for payday-loan-related search terms (see Appendix 6.3) contained messages such as 'Very high approval', 'Bad credit loans', 'No credit check', 'High acceptance rate'. Money Gap Group Limited, one of the major lead generators in the UK, told us that 'for many customers price was less important and customers were looking for a lender that would accept their application and lend them the money'. T3, another lead generator, told us that 'given that customers face uncertainty about whether or not they will be approved by a lender they use lead generators as a means to increase the chances of finding a lender willing to accept their application'.

6.104 To the extent that a borrower goes on to take a loan from the lender to whom his or her application is sold, a customer using a lead generator is essentially forgoing any comparison of lenders on the basis of the merits of their loan offering. This is because the relative attributes of different products do not enter the auction process. Given that borrowers have already gone through an application process and their details sold to a lender before they are able to observe any details of the loan that they are being offered, the threat of these customers switching to another lender is unlikely to impose any material competitive constraint on lenders.[483]

6.105 Lenders seeking to win customers with an attractive product offering may even be at a disadvantage if, as a consequence of offering customers a better deal, they are less able to bid higher amounts in lead auctions. For example, H&T told us that other lenders were able to pay for high-quality leads because they charged the customer more. This drove up the cost of leads and/or forced it to acquire riskier customers, with an associated increase in bad debt. Along a similar line, MYJAR told us that because it did not offer rollover loans, leads were less valuable to it than to other lenders that did offer rollovers, and as a consequence it could not bid competitively in the auctions run by lead generators.[484]

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[483] Dollar told us that the drop-out rate of applicants who were offered loans through pingtrees [✂] indicated that customers used lead generators to shop around (see Dollar's response to the provisional findings, paragraph 2.7.1.). We were told by one lead generator, however, that applicants might also drop out of the application process because they had not been offered a loan suitable for their purposes – in most cases because the principal amount offered was lower than they required. One lead generator told us that its customers had used larger branded payday lenders for their initial loans and used its service to increase the amount of borrowing or to repay existing payday loans. We also reviewed evidence from our transaction data set, which suggested that uncertainty about loan approval, and a consequent desire to apply to many lenders simultaneously, does not appear to be the prime factor causing borrowers to use lead generators (see paragraph 6.110*(c)*).
[484] Figure 7.3 sets out evidence about the proportion of customer acquisition expenditure of MYJAR and other large online lenders allocated to lead generators.

6.106 We also saw evidence suggesting that a substantial proportion of customers that use lead generators do not understand the nature of the service that they are being provided, or the difference between lenders and lead generators. In particular:

(a) of those respondents to our customer survey who had applied through lead generators/brokers, two-thirds mistakenly told us that they had applied directly to a lender.

(b) information supplied on the pay-per-click advertising and organic search terms used to generate potential borrower traffic to lead generator websites indicated that (i) the most important search terms related to general payday loan/lending terms rather than directly to the specific services of lead generators (60% of total search terms); and (ii) around 15% of search terms related to attracting applicants looking for a payday loan provider rather than a lead generator.[485,486]

6.107 A review of the information made available to customers by lead generators highlighted the potential for such a misunderstanding to arise (see Appendix 6.4):

(a) Distinguishing between lenders and lead generators is far from straight-forward. A web search for ‘payday lending’ or related terms will often generate a mixture of direct lenders and lead generators among both organic and pay-per-click results (see paragraphs 2.159 to 2.164), and the text accompanying these results, the product or company name, or the website title will very rarely identify the target website as belonging to a credit broker rather than a lender. Although most of those lead generator websites that we looked at informed visitors somewhere on the site that they offer a brokerage service rather than directly lending funds (in differing degrees of prominence and clarity), we found that visually these websites were very similar to those of the lenders themselves.[487]

(b) There is often a lack of transparency in how the service that lead generators provide is described on their websites, particularly in relation to the basis on which customer applications are directed to lenders. Very few lead generators make clear that they are remunerated by lenders who buy the lead, and we are not aware of any examples of lead generators explaining exactly what happens to customer applications after these are submitted (eg that leads are auctioned and sold to the lender that pays

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[485] We also noted that the search volume for the term ‘payday loan broker’ on Google for the last 12 months was very small (around 40 searches per month). See Appendix 2.7.
[486] See Appendix 2.7, paragraph 35.
[487] See Appendix 6.4, paragraphs 29 & 30.

the highest price or the lender which offers the lead generator the highest income stream). Some lead generators describe the service they provide by referring to saving customers the need to search or shop around, which some customers might reasonably interpret as meaning that they were being matched with the 'best-value' loans for them (whereas in practice the customer is usually referred on to whichever lender pays the highest amount for the lead). We also saw some instances where lead generators' websites indicated that the loan found by the lead generator was either the 'best value' or the 'best option'.[488,489]

6.108 This lack of transparency was also noted in the submissions of some lenders. [✂] told us that there was a general lack of transparency in lead generators' websites because disclosure was made at the bottom of the website using small characters or 'buried in secondary text'. It also told us that 'customers may perceive that the lead generator has acted to sort available lenders to provide the cheapest or most suitable alternative. In reality, the lead generator is selling the lead to the highest bidder'. Similarly, allthelenders.co.uk told us that 'it is extremely hard to tell if some of these brokers are lenders or not and many do not display this information clearly enough, some might have it at the foot of their page but many you have to look very hard to find this information, if it's even there at all'.

6.109 [✂] also pointed to what it considered to be misleading price information presented by some lead generators, which it found often presented the cheapest terms among the lenders to which they can sell the lead, although the lead is not necessarily bought by that lender.[490] [✂] added that lead generators typically used APRs of 1,700% and charges of £25 for a £100 loan which in its view understated the actual charges paid by the borrowers.[491] It told us that lead generators' lack of transparency might frustrate online customers' attempts to shop around, as when they applied through lead generators the actual offer they received could be higher than the advertised terms. This might prompt other searches and protract the searching process which ultimately resulted in a poor searching experience and therefore 'low likelihood of switching'.

6.110 The additional evidence about lead generators that we gathered following the variation of our terms of reference[492] is consistent with the finding that a

488 Whilst it was possible that the highest-bidding lender did offer the best value or best option, this description would not be valid in all cases.
489 See Appendix 6.4.
490 For example, [✂].
491 Our review of the pricing information on lead generators' websites indicated that there were a number of instances where the representative APR displayed on lead generators' websites did not reflect the weighted average of the panel of lenders to which leads were sold (see Appendix 6.4, paragraph 45).
492 Notice of a variation of the terms of reference.

significant proportion of customers are likely to confuse lead generators for lenders, and/or misunderstand the basis on which lead generators refer them to lenders. In particular, we considered:

(a) Lead generators' and third parties' views provided in response to our information request, Remedies Notice and at response hearings. While the majority of lead generators told us that applicants use lead generators knowingly to minimise the number of applications required or maximise the chance of getting a loan, a number of other lead generators indicated that customers' use of lead generators is not always the result of an active and conscious search for a broker.[493] money.co.uk submitted that pingtrees and brokers were easily and frequently confused with direct lenders.[494] Together with the CFA, it also raised concerns about the lack of transparency in how lead generators inform borrowers about the service that they provide.[495] One lead generator (D&D Marketing) told us that it did not believe any lead generator described the background process of the sale of leads other than mentioning that the lead would be processed through a panel of lenders.[496]

(b) Review of lead generators' websites.[497] We reviewed 125 websites between 11 and 18 September 2014, and found that 22% of the main websites (27) did not state anywhere that the firm was a broker or lead generator.[498] Additionally our review indicated that only 3% (4) stated clearly prior to the point at which a customer could enter their details that the service provided was that of a lead generator or broker rather than direct lender.

(c) Analysis of our transaction data.[499] By using the transaction data we explored the relationship between factors that could impact on a borrower's uncertainty about loan approval and their use of lead generators. The results indicate (see Appendix 6.5, Annex 1) that the likelihood of borrowers using lead generators does not generally depend on whether a customer had experienced a repayment problem with their previous loan – a factor that is likely to increase uncertainty about approval of any future loan. This suggests that difficulties in finding a

[493] See Appendix 6.4, paragraph 47.
[494] See money.co.uk response to the Remedies Notice, p2.
[495] See money.co.uk response to the Remedies Notice, p2 and CFA response to the Remedies Notice.
[496] This statement was provided by D&D in response to a question regarding whether the operation of its pingtree was made clear to customers who were using affiliate websites for loan applications (see D&D response hearing summary, paragraph 6).
[497] See Appendix 6.4.
[498] See Appendix 6.4, paragraph 36.
[499] See Appendix 6.5, Annex 2.

lender, and a consequent desire to apply to many lenders simultaneously, may not be the prime factor causing borrowers to use lead generators.

(d) Customer research. The customer research we undertook as part of our remedies process found that customers' awareness and understanding of lead generator sites was low.[500] Customers were in general unable to identify lead generator sites and were surprised by how they worked, given their assumption that price comparison sites (or sites resembling them) worked in customers' interests. Customers also felt that lead generators appeared to be deliberately disguising themselves as lenders, and were not being transparent about the practice of sharing personal details.

6.111 Taken as a whole, the evidence suggests that many customers using lead generators either are driven primarily by a desire to obtain credit from any available source and do not make a clear distinction between lenders and lead generators or erroneously believe that by using a lead generator they are being matched with the best-value provider. Such customers are effectively forgoing any price comparison between lenders either because they attach little value to price or because they erroneously expect lead generators to find the best-value loan for them. Such customers are therefore unlikely to be responsive to the terms offered by the particular lender to whom their details are sold. As a result, we would expect any incentive for lenders to compete for these customers by improving their offering to be weak.

Conclusions on the role of lead generators

6.112 To summarise, we found that a substantial proportion of online payday loan customers use lead generators to apply for a payday loan. The auction process used by lead generators to allocate customers to lenders willing to offer them credit is based entirely on which lender offers the best commercial terms to the lead generator (often the lender which bids the highest amount), implying that any incentive for lenders to compete for these customers by lowering their prices was likely to be very weak. The lead generator model may also create an incentive for lenders to increase prices to customers, as lenders offering cheaper loans would find it harder to bid high prices in lead auctions and hence acquire valuable leads. There is often a lack of transparency in how the service that lead generators provide is described in their websites – particularly the basis on which applications are referred on to

[500] We also note that customer interaction data from one large lead generator ([✄]) for its website ([✄]) indicated that only 3% of customers visiting the site in the period 1 August to 31 August 2014 looked at the 'how it works' or 'frequently asked questions' pages. 31% of customers applied directly from the first page they visited on which the firm is described as a 'payday loan website' (71% of customers had applied after their first, second or third interaction with the website). [✄] states that it is a loan broker at the bottom of the home page; however, customers would need to scroll down to see this description.

lenders – and many customers are unaware of the nature of the service that they are being provided by lead generators. This further reduces the likelihood that the risk of customers using another provider will impose a material competitive constraint on lenders.

The perceived risk and loss of convenience associated with changing lender

6.113 We considered whether – additional to those barriers set out above, which would apply equally to new or repeat customers – customers who have taken out a previous loan with a lender would face any further barriers which would inhibit them from changing lender on the basis of price or other aspects of another lender's product offering. The evidence that we reviewed suggested the existence of two additional aspects of the payday market which might dissuade customers from switching to an alternative lender unless required to do so: the perceived risk associated with an unknown lender, and the loss of convenience associated with switching.

6.114 Customers who have the option of staying with their current lender may be discouraged from switching if they perceive there to be risks associated with changing lender. This is likely to be particularly relevant for payday loan customers, given the importance that borrowers attach to aspects of lending relationships that are likely to be difficult to observe prior to taking out a loan with a lender (see the findings of our qualitative research discussed in paragraph 6.42). In particular, these include the quality of a lender's customer service and their approach to loan collections.[501]

6.115 This effect will be heightened by the negative reputation of the payday lending sector and the poor lending practices of certain payday lenders (see paragraphs 3.2 to 3.5 and 6.42). Given the reputation of the sector, some customers are likely to be unwilling to take the risk of using a lender that they have not used before (unless they are forced to do so in order to obtain further credit) – even if the other lender's product is of significantly better value.

6.116 In this context, Elevate told us that when switching occurred, it was driven mainly by negative experiences rather than the promise of a better loan and that it was difficult to disrupt the relationship between customers and lenders, especially with repeat customers, as customers valued the familiarity with the lender and traded this off against the uncertainty related to the conduct of another lender. This is consistent with the focus of many lenders on customer retention (see paragraphs 4.212 to 4.214), and the emphasis placed by

[501] For example, the research conducted by Ipsos MORI for BIS found that payday loan customers are particularly concerned with the actions taken by lenders if borrowers are unable to repay the loan (p35).

respondents to our customer survey on satisfaction with existing suppliers as a reason for using only one lender.

6.117 As well as the perceived risk associated with switching, some borrowers may perceive it to be simply more convenient and straightforward to stay with a lender that they have borrowed from previously, rather than spend time filling in additional application forms or researching alternatives. While this is a factor in many markets, it has an additional relevance in the payday lending market given the short-term nature of the demand for the product, and the perceived urgency of the loan.

6.118 The relative convenience of staying with an existing lender is likely to be particularly high for a borrower who is considering topping up or rolling over an existing loan, as these processes require little effort to arrange with an existing lender. Furthermore, for customers who are considering rolling over a loan, the perceived loss of convenience associated with changing lender may be exacerbated by a concern that funds from any new lender may not be received in sufficient time to pay off the existing loan and make all of the relevant transfers.

6.119 As discussed in paragraphs 6.40 and 6.41, most customers who had remained with the same lender reported having done so because they were happy with the service provided and therefore perceived no reason to give any consideration to changing lender. However, if we look at the remainder – ie those customers who may have had a less positive experience and so would be more likely to be looking to switch lenders – the results of our customer survey suggest that a significant proportion of these individuals identified the ease/convenience of remaining with the current provider and avoiding the need to go through a new application process as a factor contributing to their decision not to switch.[502] We also noted that less than 10% of the customers who had rolled over their most recent loan said that they would consider taking out a loan with a lender in order to pay off a debt to another lender. This indicated a clear difference in customers' perceptions of the attractiveness in refinancing a loan with an existing lender versus taking out a new loan with an alternative supplier.

[502] Of 39% of the customers who did not consider changing lender and who did not report staying with the same lender because they were happy with the service provided, 17% indicated either the ease/convenience of remaining with the current provider or the burden of going through a new application process as reasons contributing to their decision not to change lender.

Conclusions on the risk and loss of convenience associated with changing lender

6.120 In summary, where their choice of lender is not dictated by concerns about credit availability, borrowers may be dissuaded from looking at alternative suppliers by the perceived risks associated with using a new lender (ie a lender not used previously by the customer), particularly in light of the negative reputation of the payday lending sector as a whole. In addition, customers may perceive a loss of convenience associated with applying to a new lender, particularly if the alternatives are rolling over or topping up an existing loan or taking out a new loan shortly after repaying the previous one. These factors, in combination with the other barriers identified in this section, are likely to reduce further the constraint placed on lenders by the threat that existing customers will switch to an alternative lender offering a better-value product.

Impact of the price cap

6.121 As set out in paragraphs 3.29 and 3.30, the FCA implemented a price cap in the payday lending market that took effect on 2 January 2015. The price cap limits the interest and fees that can be charged on a loan to 0.8% per day, caps fixed default fees to £15, and requires that the total amount repaid by way of interest and charges on a loan does not exceed the initial loan principal.

6.122 We considered whether the price cap would affect the features we identified as giving rise to customers' limited sensitivity to variation in prices, or reduced incentive for lenders to keep their prices low in order to prevent customers from choosing alternative suppliers. Considering each of the barriers identified in this section in turn:

(a) The perceived urgency of the need for a payday loan, and the focus on credit availability. The price cap will not reduce the perceived urgency underpinning many borrowers' decisions to take out a payday loan, or remove the uncertainty that many customers face when making the decision of which lender to borrow from.

(b) Difficulties faced in identifying the best-value loan product on offer. Although it is possible that the price cap will lead to an increase in the similarity of the pricing structures used by different lenders (for instance, by encouraging the use of daily interest rates, and simplifying late fees),[503] the underlying complexities associated with comparing loans with

[503] See paragraph 4.73.

different durations and repayment options are likely to remain. Significantly, the current lack of effective PCWs is likely to continue to impede customers from being able to identify effectively the best-value loan for their needs.

(c) The heightened insensitivity to late fees. While the price cap may reduce the detriment to customers from very high charges, it is unlikely to reduce the overconfidence affecting some customers regarding their ability to repay a loan on time. The price cap may, to the extent that it leads some lenders to simplify the structure of their late charges, improve the extent to which customers are able to understand those fees.

(d) The role of lead generators. We would not expect the price cap in and of itself to affect the extent to which borrowers understand the service offered by lead generators, or the success of these intermediaries in attracting loan applicants. The price cap may, however, reduce the profitability of lead generators (given that the price of a lead is likely to be driven by the expected profitability of a customer), leading to the exit of some of these intermediaries from the market.

(e) The perceived risks and loss of convenience associated with switching lender. The price cap is unlikely to affect the loss of convenience associated with switching lender. To the extent that it serves to improve the reputation of the payday lending market, then customers might feel more comfortable trying new lenders in the knowledge that the price cap offers protection from very high charges.

6.123 We concluded that the barriers that we have identified as serving to reduce customers' sensitivity to prices would generally continue to restrict competition between lenders in the presence of the price cap. Although we considered that the price cap could be expected to lead to some standardisation of payday lending products and may reduce the risk perceived by customers considering switching lender, we did not consider that these effects would increase customers' sensitivity to prices such that the threat of losing business would cause lenders to compete effectively on prices. We considered that this loss of competition would be material, as there would remain scope for substantive price (and non-price) competition within the constraints of the price cap (see paragraph 8.12).

Conclusions

6.124 We have identified a combination of market features which give rise to the limited responsiveness of customer demand to prices that we have observed in the UK payday lending market, and which reduce the pressure for lenders to compete to attract customers by lowering their prices. These features act in combination to deter customers from comparing the different loans available, to impede their ability to do so effectively, and to discourage repeat customers from considering and/or selecting a new lender that offers a better-value loan for their needs.

6.125 These market features are:

(a) The context in which customers take out payday loans is often not conducive to customers shopping around to find a good-value loan and may amplify the adverse effects of other barriers to shopping around and switching lender. Customers often perceive the need for their loan to be urgent, and attach considerable importance to the speed with which they are able to access credit. Many payday loan customers are also uncertain, often with good reason, about whether, and from whom, they will be granted credit to meet their borrowing requirements. These aspects of the decision-making environment can tend to make customers reluctant to spend time shopping around for the best deal available, and can cause customers to focus on which lender is willing to lend to them (or, for a repeat borrower, to stay with a lender that they previously used) rather than which lender offers the best-value product.

(b) It can often be difficult for customers to identify the best-value loan product on offer for them. Despite information on headline rates generally being available on lenders' websites or in the shops of high street lenders, customers' ability to use this information to identify the best-value payday loan is impeded by the complexity associated with making effective price comparisons given variation in product specifications and pricing structures, and the limited usefulness of the APR in facilitating comparisons between payday loans. Existing comparison websites, which might help customers compare loans, suffer from a number of limitations and are infrequently used. Consequently, customers who do seek to carry out comparisons on the basis of price may struggle to identify the best-value loan on offer, and – in combination with the perceived urgency affecting many customers and the overriding importance of finding a supplier that is willing to lend – some customers may be put off shopping around for their loan entirely.

(c) Customer demand is particularly insensitive to fees and charges incurred if a borrower does not repay their loan in full on time. Customers tend to be less aware of these potential costs of borrowing than they are of the headline interest rate when choosing a payday loan provider. This is in part because overconfidence about their ability to repay the loan on time can cause some customers to pay only limited attention to these costs

when taking out their loan. Even where customers seek to anticipate the costs associated with late repayment, the information generally provided about such costs is significantly less complete, less easy to understand and/or less prominent than information on headline rates. It can therefore be difficult for customers to estimate, and so make effective comparisons about, the likely cost of borrowing if they do not repay their loan in full on time.

(d) Many online customers take out payday loans via a lead generator's website. Lead generators typically promote their ability to find customers a lender willing to offer them a loan within a short period of time. The value for money represented by different lenders' loan offerings is not taken into account in the auction process operated by lead generators, who instead typically sell customer applications on terms most favourable to them – often to the highest bidder. Furthermore, there is often a lack of transparency in how the service that lead generators provide is described in their websites – particularly the basis on which applications are referred on to lenders – and many customers do not understand the nature of the service offered by lead generators. An implication of the operation of this distribution channel is that lenders acquiring customers through lead generators are unlikely to have a strong incentive to lower their prices. The lead generator model may also create an incentive for lenders to increase prices to customers, as lenders offering cheaper loans would find it harder to bid high prices in lead auctions and hence acquire valuable leads.

(e) Where their choice of lender is not dictated by concerns about credit availability, customers can be dissuaded from looking at alternative suppliers by the perceived risks associated with using a new lender (ie one they had not used previously), particularly in light of the negative reputation of the payday lending sector. Customers may perceive a loss of convenience associated with applying to a new lender, particularly if the alternatives are rolling over or topping up an existing loan. These factors further reduce the constraint placed on lenders by the threat that existing customers will switch to another lender offering a better-value product.

6.126 We considered that in general, the barriers that we have identified as serving to reduce customers' sensitivity to prices would continue to restrict competition between lenders following the introduction of the price cap in January 2015, and other recent regulatory developments in the market.

7. Entry and expansion

Introduction

7.1 The threat of entry by new rivals or expansion by incumbent firms is often an important source of competitive discipline in a market. Entry or expansion can make it difficult for an incumbent firm to exercise market power, promote efficient firms at the expense of inefficient ones, introduce innovation to an industry and lead to more competitive prices as well as greater choice and quality.[504]

7.2 As set out in the previous section, the interaction of a number of barriers to shopping around and switching means that customers are generally unresponsive to the price of payday loans. Consequently, price competition between payday lenders is ineffective. In this section we consider whether – if customers were more responsive to prices – the prospect of new entry or expansion by existing providers would impose a competitive constraint on the prices of payday lenders.

7.3 To do this, we begin by documenting the history of entry and expansion in payday lending. We find that a large number of lenders have entered the payday lending sector in the past five to ten years, that the market as a whole expanded substantially over the period, and that within this broader trend of market expansion a small number of lenders have been able to grow their shares of supply significantly.

7.4 While informative about the historical ease of entry for certain types of supplier, evidence of historical patterns of entry and expansion does not establish how effective the prospect of new entry or expansion is in constraining incumbent lenders, or will be in the future. For this reason, we also considered the market conditions facing a new entrant today, and the ease with which a new entrant or smaller lender could expand sufficiently to become an effective competitor.

7.5 We identified three characteristics of the market which may reduce the strength of the competitive constraint that might otherwise be imposed on payday lenders by new entry or expansion. First, the negative perception of payday lending may deter or prevent some firms from entering payday lending. Second, new entrants and smaller lenders may find it difficult to raise awareness of their product and attract new customers, thus impeding their ability to establish themselves in the market. Third, new entrants and smaller

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[504] See the Guidelines, paragraphs 205 & 206.

lenders may face disadvantages when assessing credit risk, which may also impede their ability to establish themselves as effective competitors.

7.6 After describing each of these potential barriers, we discuss the potential impact of the FCA's price cap and other recent regulatory developments on entry conditions. We then set out our conclusions on the effectiveness of the constraint imposed on payday lenders by the prospect of entry and expansion, and on the factors influencing the effectiveness of this constraint.

History of entry and expansion

7.7 Table 7.1 sets out the date on which the 11 major payday lenders (as defined in Section 2[505]) entered the payday lending sector.[506] It shows that the earliest entrants (The Money Shop, Cheque Centres, Payday Express) first began offering payday loans more than ten years ago. The most recent high street entrant among these 11 larger lenders was Speedy Cash, which entered in November 2010. The most recent entrant among the major online lenders was Ariste, which entered in October 2009 (although H&T and Cheque Centres both launched online products alongside their existing high street operations after this date, in June 2011 and July 2011 respectively).

TABLE 7.1 **Entry dates of the 11 major lenders**

Lender	*Date lending started*	*Date of acquisition by current parent (if applicable)*
Cheque Centres (CNG Financial)	1996 (online Jul 2011)	Jan 2006
The Money Shop (DFC)	1998	Feb 1999
Payday Express (DFC)	Jan 1999	Apr 2009
H&T	Jan 2003 (online Jun 2011)	N/A
PaydayUK (DFC)	Aug 2003	Apr 2011
WageDayAdvance (Speedy Group)	Dec 2006	Feb 2013
Wonga	Jan 2007	N/A
CashEuroNet (Cash America)	Jun 2007	N/A
CFO Lending	Jan 2008	N/A
Global Analytics	Nov 2008	N/A
MYJAR	Mar 2009	N/A
Ariste (EZCORP)	Oct 2009	Apr 2012
The Cash Store	Apr 2010	N/A
Speedy Cash (Speedy Group)	Nov 2010	N/A

Source: Parties' responses to the CMA financial and market questionnaires.

Note: N/A = not applicable.

7.8 We have observed firms entering the payday lending sector using a variety of different strategies, including:

[505] See paragraph 2.9.
[506] Four of the 11 major lenders have recently either exited the market or have temporarily ceased issuing loans (see paragraphs 2.74–2.128 for details of individual lenders).

(a) *Privately funded start-ups.* CFO Lending, Global Analytics, MYJAR and Wonga entered as start-ups and developed online payday lending businesses from scratch funded by private equity investors.

(b) *Acquisition of an existing business.* CNG Financial, DFC, EZCORP and Speedy Group each acquired one or more UK-based payday lending companies that had been founded as start-ups in the UK. Following these acquisitions, the respective parent companies (two of which are listed on North American stock exchanges) have provided the majority of funding for expansion.

(c) *Expansion from payday lending in North America.* Cash America adapted technology systems originally developed in the USA to launch CashEuroNet, which is operated mainly from its existing premises in the USA. The Cash Store Financial Services (based in Canada) and Speedy Group (based in the USA) opened their first UK stores in April 2010 and November 2010 respectively.

(d) *Product diversification strategy.* H&T entered payday lending via a product diversification strategy, adding payday lending products to its existing pawnbroking business.

7.9 In Appendix 7.1 we discuss two examples of relatively recent entry into payday lending by well-resourced lenders, Provident Financial and Elevate. Provident's Satsuma product provides an example of a diversification strategy, representing a move by the largest UK home credit provider to launch an online product that falls within our payday loan definition. Elevate's product, Sunny, provides a recent example of a large US payday lender seeking to enter the UK market, and is also interesting in that the product includes an element of risk-based pricing.

7.10 The period between 2008 and 2012 saw rapid expansion in the payday lending market, both online and on the high street. Payday lending revenue growth for the major lenders ranged from 40% to over 100% a year in the period from 2009 to 2012. Looking across the period as a whole, the total number of payday loans issued by the major lenders increased from fewer than 2 million in 2008, to over 8 million in 2013. The number of stores operated by high street lenders also grew very rapidly in this period (see paragraph 5.75). Despite these historical patterns, and as shown by the evidence set out in Section 4, entry by new firms into the payday market has not resulted in existing lenders being effectively constrained when setting their prices. Following the very strong initial growth, the recent trend has slowed: revenue growth for the major lenders in 2013 was significantly lower, at around 5%. In the first nine months of 2014 revenue contracted by around

27%.[507] The contraction in 2014 is likely to have been driven by a combination of lenders tightening their credit policies, and the exit of some suppliers from the market, as they adjust to and anticipate tighter regulatory conditions (see the discussion of the price cap and other recent regulatory changes beginning at paragraph 6.121).[508]

7.11 Figure 7.1 shows how, within the broader pattern of expansion, the relative size of the 11 major lenders evolved between 2008 and 2013. It shows that since entering in 2007, Wonga's share of loans relative to the other major lenders increased by a significant amount [✂], reaching [✂]% of all loans issued by these lenders in 2013. CashEuroNet and MYJAR had also made gains since entry, although the relative scale of their expansion was smaller, and their shares remained [✂]%. At the same time, the share of loans accounted for by Dollar and H&T had contracted markedly.

FIGURE 7.1

The relative number of loans issued by the major payday lenders, financial years 2008 to 2013*

[✂]

Source: CMA analysis of financial data provided by the major lenders.
*See Appendix 2.5 for a description of how different lenders' financial years have been treated.
Notes: [✂]

7.12 More recently, we have observed some of the 11 major lenders exiting the payday lending market. In particular, Cheque Centres stopped selling single-instalment payday loans in May 2014 as part of an agreement with the FCA, which had raised concerns with the provider regarding its lending practices.[509] In October 2014, EZCORP, the parent company of Ariste, announced that it would be exiting from the UK market in light of changes to the regulatory environment and in the context of the parent company's strategy.[510] The Cash Store went into administration in August 2014. CFO Lending ceased to offer payday loans in May 2014.[511]

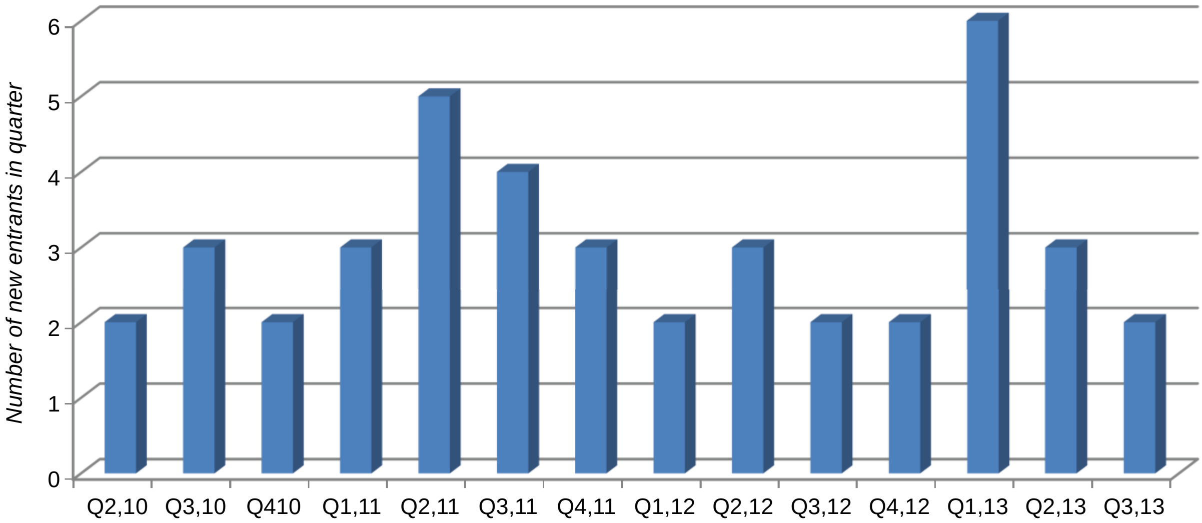
[507] The FCA observed 'a clear reduction in the volume and value of lending (of around 35%) between March and August this year – though this varies between firms' (see paragraph 10, Annex 2 of PS14/16: *Detailed rules for the price cap on high-cost short-term credit*).
[508] Similarly the FCA noted that the contraction does 'not appear to be driven by decreasing demand' but rather by 'a sharp reduction in firms' acceptance rates from April 2014 when the FCA regulation of the consumer credit market transferred from the OFT. This suggests that FCA regulation has affected firms' lending decisions although it is currently unclear whether the magnitude of this change will be sustained as regulatory uncertainty recedes for firms'(see paragraph 10, Annex 2 of PS14/16: *Detailed rules for the price cap on high-cost short-term credit*).
[509] See FCA press release, 5 May 2013.
[510] See paragraph 2.100.
[511] Global Analytics withdrew its Zebit brand but it still trades under the Lending Stream brand.

7.13 Looking beyond the 11 larger lenders, we have also seen large numbers of smaller providers entering the payday lending sector in the period since 2008. As at October 2013, we estimated that there were at least 90 lenders active in the market[512] (see Appendix 2.5).[513] Recently some smaller lenders have exited the market (see paragraph 2.74) and further exit may be expected following the introduction of the price cap (see paragraph 7.113). Nonetheless, as at November 2014, at least as many as 40 lenders appear to be still operating in the market.[514]

7.14 We asked smaller lenders about the date on which they began payday lending. Figure 7.2 illustrates the reported entry dates of these lenders, split by quarter. It shows that companies have continued to enter the sector throughout the period between 2010 and 2013, at a rate of around two to five new entrants per quarter.

FIGURE 7.2

Entry by smaller lenders, first quarter 2010 to third quarter 2013



Source: Response to CMA small company questionnaire.
Notes:
1. The information presented in the chart may underestimate the true number of lenders entering the market in each quarter, to the extent that certain lenders did not respond to our questionnaire (for example, the chart will exclude firms which entered in the period but had exited before 2013).
2. A previous version of this chart showed an apparently large number of smaller lenders entering the market in quarter 1 2010 (see Figure 1 of the working paper on entry and expansion). This anomaly appears likely to have been driven by the design of the questionnaire – many of the lenders recorded as entering in this quarter are likely to have entered the market prior to that date. As a consequence, we restrict our analysis above to the period quarter 2 2010 to quarter 3 2013.

[512] We are aware that a number of lenders have recently ceased issuing loans (see paragraph 2.74). Nonetheless, on the basis of a review of their website, as at November 2014 at least half of these 90 lenders appeared to be still operating in the payday loan market.
[513] See also paragraphs 7.109–7.115 for a consideration of how recent regulatory developments might affect entry conditions.
[514] This estimate is based on a review of the lenders' websites that we carried out in early November 2014.

7.15 To summarise:

(a) The first payday lenders began offering loans over ten years ago. We have observed firms employing a variety of different entry strategies, including start-ups, firms entering by acquisition, entry by North American-based lenders, and diversification by lenders originally offering non-payday credit products.

(b) The payday lending sector as a whole (both high street and online) has expanded rapidly since 2008, with growth particularly strong between 2010 and 2012. More recently, revenue growth has declined, with a significant fall in revenues observed in the first half of 2014, and some major lenders exiting the sector.

(c) Wonga has expanded particularly rapidly since its entry in 2008, becoming the largest payday lender by some distance. CashEuroNet has also increased its share of supply significantly since 2008.

(d) Entry by companies into the payday lending sector has been observed regularly since 2008, at a rate of at least two to five new entrants per quarter, although recently some lenders have exited the market and further exits may be expected following the introduction of the price cap.

7.16 These patterns indicate that large numbers of lenders have managed to enter the payday sector in recent years, and that a small number of lenders have succeeded in significantly increasing their market shares. Wonga told us that this evidence pointed to there being both an incentive to enter and the absence of any significant barriers to entry.[515]

7.17 These patterns showed that barriers to entry had not prevented a number of suppliers from entering the market prior to 2013. However, this observation does not in itself enable us to understand the impact of such entry on the effectiveness of competition and the extent to which smaller suppliers are able to establish themselves as strong competitors to incumbent providers. Nor does it enable us to understand the extent to which further significant new entry should be expected in the future, particularly in the light of recent regulatory developments (see Section 3). For these reasons, we next consider whether any factors exist which restrict the ability of a new entrant or smaller lender to expand sufficiently to become an effective competitor, or to discourage entry by particular types of supplier.

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[515] See Wonga's response to the provisional findings, paragraph 6.2.

Overview of requirements to be an effective payday lender

7.18 We considered the components necessary to operate a successful payday lending business. We identified the following key requirements:

(a) Regulation and compliance – as discussed in Section 3, payday lending is now a regulated activity within section 22A of the FSMA. Consequently no person may carry on that activity by way of business unless that person holds either an interim permission from the FCA (replacing a former OFT consumer credit licence) or has been authorised by the FCA. In addition, the CCA lays down rules requiring information to be given to borrowers before entry into a consumer credit agreement. New Rules and Guidance in the FCA's CONC now cover the verification of creditworthiness and affordability and impose post-contract requirements. Furthermore all firms providing consumer credit loans must now comply with the high-level rules in the FCA's Handbook, for instance with regard to treating customers fairly and cooperating with the regulator.

(b) Customer acquisition – in order to be successful, a lender must be able to promote its product and acquire new customers. Online lenders typically use a variety of different strategies in order to acquire new customers, including television, radio and other types of offline advertising, pay-per-click and other forms of online advertising, and purchasing applications directly from lead generators. High street lenders may also advertise their products, but unlike online lenders will also rely on the visibility of their stores to attract new business.

(c) Credit risk assessments – a core capability for a payday lender is the ability to assess the credit risk of new and returning customers. The importance of this capability has been heightened by lenders anticipating the effect of the price cap by tightening their credit risk thresholds. Further tightening may occur as lenders further respond to the price cap (see paragraph 4.170). As discussed in paragraph 2.70, in order to perform credit risk assessments, lenders typically analyse various different types of information relating to an applicant. Most lenders have developed automated risk models, of varying degrees of sophistication, to carry out these assessments. Some lenders' risk assessments – and in particular high street lenders – also have a manual (ie non-automated) element.

(d) Loan management systems – lenders require certain technology capabilities, including the software and know-how to develop and maintain payday loan management systems. These systems are used to process applications, record loans and repayments, and link to other businesses (eg banks and CRAs).

(e) Payment processing services – payday lenders need a commercial banking relationship in order to make bank transfers of new loans to their customers' bank accounts and recover amounts due. Online products are debit card based and lenders use CPAs to some degree in order to debit borrowers' bank accounts. Payday lenders also need a banking relationship for their day-to-day activities (eg payments for employees, goods and services, and management of working capital).

(f) Customer services and call centres – the extent to which payday lenders use call centres to interact with customers depends on their individual business strategy (eg internet-based lenders generally require a call centre to service customer accounts). The use of call centres to manage inbound customer calls and loan applications can be scaled up or down according to the business requirements. An entrant may also be able to outsource the operation of its call centre to a third party instead of investing in its own operations.

(g) Financing and access to capital – this financing for payday lending includes the capital required to fund start-up costs or business expansion, including the costs of meeting the business requirements set out above. The sources of finance may include private equity investment and retained earnings.

7.19 High street lenders will also have additional requirements. In particular, a high street payday lender would need to rent premises in suitable locations. This will be influenced by the need to operate in areas with high demand for payday lending and the availability of retail units with the appropriate planning use class (A2 Financial and professional services).[516] In addition to this, high street lenders will need to fit out the locations for payday lending and hire staff. High street lenders' ability to expand by opening new stores is discussed in paragraph 5.75, where we conclude that lenders are able to open new stores with relative ease.

7.20 Having reviewed these requirements, we identified three characteristics of the payday lending market which may weaken the competitive constraint that might otherwise be imposed on payday lenders' prices by the prospect of new entry or expansion. These related to the reputation of the payday lending sector, and disadvantages faced by new entrants and smaller lenders in their ability to acquire new customers and assess credit risk accurately. These issues are discussed in turn in the following subsections.

[516] As set out in the Town and Country Planning (Use Classes) Order 1987 (as amended).

The reputation of payday lending

7.21 In recent years payday lending has been an issue which attracts a large amount of political and media attention. There is a widespread perception of the existence of bad lending practices among lenders, and the existence of such practices was highlighted in the findings of the OFT in its review of the sector, which found that non-compliance among payday lenders was 'causing real harm, and the problem has grown' (see paragraph 3.4).

7.22 We identified two main ways in which the reputation of payday lending might affect the extent to which payday lenders' prices and product offerings would be constrained by the threat of new lenders entering the market and competing for their customers. First, some mainstream lenders (or other established businesses) may be discouraged from entering entirely by the negative reputation of the sector. Second, the reputation of the sector may affect payday lenders' access to banking services. We discuss these issues in turn below.

Deterrence of mainstream lenders

7.23 We saw some evidence to suggest that the reputation of the payday lending sector was likely to discourage mainstream lenders (or other businesses with established reputations in other markets) from entering the payday market.

7.24 Lloyds told us that it did not have any mainstream products on sale that had an APR above a given level (orders of magnitude lower than current payday loan APRs) because of the potential reputational and brand damage, as that was the level it judged at which people started to question the legitimacy of the product.[517] The APR was a difficult issue, particularly in relation to how it was communicated and interpreted. In Lloyds' view, the APR was not appropriate for short-term lending products (and this was why it was not used for overdrafts) and presented a false impression of the cost of the product. This could lead to inappropriate comparisons being made using APRs between the cost of very short-term lending products and longer-term products such as a personal loan. However, if there was a way to overcome this issue, then it might make it more likely that Lloyds Banking Group or other mainstream lenders would consider entering payday lending or developing products designed to meet the same need. However, at present the thought of doing so would be difficult reputationally because the very high headline APR

[517] In particular, Lloyds told us that it did not have any mainstream products on the book that had an APR above [✂]% because that was the level it judged at which people started to question the legitimacy of the product.

would be likely to lead to stronger criticism of the banks than that currently experienced by payday lenders.

7.25 Barclays told us that it would be concerned about entering the short-term month-end money-lending business primarily due to questions about the affordability of these products for customers, but it would also have reputational unease.

7.26 Wonga submitted that our evidence on this point was based on two banks and that we had not considered other mainstream credit suppliers.[518] However, we would expect the reputational concerns identified to apply similarly to other mainstream lenders, which is consistent with the reluctance of most banks to provide banking services to payday lenders (see paragraph 7.31), and the fact that no entry into payday lending by a mainstream lender had been observed to date.

7.27 In addition to banks, the reputation of payday lending might serve to dissuade other established businesses that might otherwise consider entering the market. For instance, as discussed in paragraph 6.87 it may also affect the willingness of PCWs to enter the sector (see, for example, the withdrawal of moneysupermarket.com partly as a result of the increasing level of media and political scrutiny into payday lending practices, and the perception of non-compliance in the sector).

7.28 CashEuroNet suggested that reputation may not be the only reason why banks would be unlikely to enter the payday lending sector. In particular, it said that sub-prime customers provided very limited scope for mainstream banks to cross-sell other products and thereby spread acquisition costs, meaning that such customers were unlikely to become a focus for mainstream lenders, even in the absence of negative political and media attention on the sector.

Access to banking services

7.29 As set out in paragraph 7.18, to operate effectively payday lenders need to have access to banking services. There is evidence to suggest that some payday lenders entering the sector today may find it difficult to establish the necessary banking relationship, and that this may be at least partly a result of the negative perception of the sector.

7.30 A number of lenders told us that either they had themselves experienced difficulties accessing banking services, or had observed other lenders having

[518] See Wonga's response to the provisional findings, paragraph 6.7(a).

difficulties, and many reported only being able to find a single bank that was willing to offer them the necessary services. For example:

(a) MYJAR said that the largest barrier to entry was the difficulty of obtaining commercial relationships with the banking sector because the banks considered payday lenders as competitors and were reluctant to progress banking relationships. It said that [✂].

(b) H&T said that it had seen banks withdraw facilities from smaller businesses and that new businesses found it increasingly hard to obtain card-processing accounts.

(c) Loaf told us that its entry into payday lending had been frustrated by the UK banking industry. Numerous banks it approached to open a standard business account had cancelled its application upon learning that it planned to offer payday loans. Loaf said that 'anti-competitive behaviour by the UK mainstream banking oligopoly was a significant barrier to small and independent new entrants providing better value payday solutions to UK consumers'.[519]

(d) Cash Converters said that it had around 130 franchisees, but only one bank which was willing to offer it services.

(e) WageDayAdvance told us that while it was happy with its current bank, it had from time to time looked to see if any alternatives were available, but had found its options were limited.

(f) PDL Finance (Mr Lender) reported [✂].

(g) The Cash Shop reported having difficulties finding a bank when it had entered the sector, and ultimately having had to buy another business because it had a banking facility.

7.31 The submissions of the banks also indicated that they were often unwilling to deal with payday lenders. In particular:

(a) HSBC said that [✂].

(b) Lloyds said that it had limited commercial banking exposure to payday lenders, although there were reputable and well-managed payday companies that it was pleased to support. It said that it looked at each

[519] Loaf submission, p1.

business on its own merits – taking into account a company's credit and regulatory risk.

(c) RBS said that [✂].

(d) Santander said that [✂].

7.32 One exception was Barclays, which told us that it provided corporate banking services to [✂] payday lenders, and merchant acquiring services to [✂] payday lenders. It was not aware of rejecting any applications by payday lenders to bank with Barclays, although it had rejected a number of applications for merchant acquiring services where [✂]. It told us that, with regard to merchant acquiring services, [✂].

7.33 Despite the limited options available to payday lenders, we were not aware of any lenders that had in the past either attempted to enter the market, but had ultimately been unable to because they were unable to access banking services, or lenders which had left the market as a result of their banking services being withdrawn. We were also told by one lender that possible alternatives to dealing directly with the major banks did exist.[520] Nevertheless, we considered there to be a significant risk that a firm entering the payday lending sector today could be impeded from doing so – and even prevented from entering altogether – by the difficulty involved in establishing the necessary banking relationships.

Conclusions on the impact of reputation

7.34 The history of non-compliance and irresponsible lending by some payday lenders and the resulting negative reputation of the sector are likely to reduce the constraint imposed on payday lenders by the prospect of new entry. In particular:

(a) The reputation of payday lending is likely to deter some businesses with established reputations in other sectors – such as mainstream credit suppliers –– from entering the market. This reduces the likelihood of entry by parties with the capability to transform the nature of competition in the market.

(b) Potential entrants may also be dissuaded from entering payday lending by the difficulty – which may itself be linked to the current reputation of the sector – in establishing banking relationships, and the very small number

[520] Specifically, [✂].

of suppliers currently willing to provide banking services to payday lenders.

Difficulties faced by new entrants and smaller online lenders in attracting new customers

7.35 An important determinant of the strength of the rivalry that established lenders will face from new entrants and smaller lenders is how effectively they are able to acquire new customers. The more difficult or expensive it is for a smaller lender to raise awareness about and market its products, the weaker will be the competitive constraint that it will exert on established providers.

7.36 New entrants and smaller lenders' ability to acquire new customers is likely to be significantly impeded by the characteristics of the payday market which restrict the extent to which customers can identify and choose better-value payday loan products which are on offer (see Section 6). In particular, we identified a number of barriers to shopping around or switching that may cause customers to be unresponsive to variation in payday lenders' prices, including aspects of the context in which the decision to take out a payday loan is generally made, difficulties that customers face in identifying the best-value offer (especially if they seek to take late fees into account), the role of lead generators in the online sector, and the perceived risk and loss of convenience associated with changing lender. One implication of these barriers is that it is likely to be difficult for a new lender to raise awareness of its product and win customers on the basis of a low-cost loan offering.

7.37 We considered whether there are additional characteristics of the payday lending market which may make it difficult for new entrants and smaller lenders to acquire new customers and expand.

7.38 We focused in particular on online lenders, as this is by some margin the largest distribution channel and the most likely source of future new entry. In addition, we noted that high street payday lenders generally rely to a large extent on the physical presence of their stores to generate customer traffic. This option is not open to online lenders, who instead use a range of marketing approaches – including online and offline advertising – to raise awareness of their products. Many online lenders also rely to a considerable degree on purchasing customer applications from lead generators in order to generate new business (see paragraph 6.101). On average, customer acquisition expenses (including advertising and promotions costs, and commissions paid to lead generators, brokers and affiliates) accounted for around one fifth of the 2012 total costs of the major payday lenders that offer loans online.

7.39 In our consideration of this issue, we begin by describing the different customer acquisition strategies used by online lenders. We then consider whether smaller online lenders are likely to face disadvantages which mean that they will struggle to establish an effective brand and generate new business organically. Finally, we consider the limitations associated with other marketing channels that are likely to be more accessible to smaller online lenders.

Channels of customer acquisition

7.40 Online payday lenders use a variety of different methods to source new customers. Some lenders rely considerably on traditional 'offline' methods such as television, radio, sports sponsorship and outdoor advertising. Lenders may also seek to generate new business online by buying customer applications directly from lead generators, using pay-per-click advertising (most commonly alongside search engine results, or via affiliates such as PCWs or voucher schemes) or devoting resources to search engine optimisation (ie taking steps to try and ensure that their website appears highly among the results presented by search engines when customers search for terms related to payday loans).

7.41 Table 7.2 summarises how total expenditure is split across the different channels for the largest online payday lenders in 2013.[521] It shows that expenditure on lead generators, offline advertising and online advertising each accounted for around a third of total expenditure on customer acquisition across the sector. Within traditional, 'offline' advertising, television accounted for over 80% of all expenditure. Within online advertising, pay-per-click fees accounted for around two-thirds of all expenditure.

TABLE 7.2 **Total expenditure of the major online payday lenders on different customer acquisition channels, 2013**

Channel	*Proportion of all expenditure on customer acquisition, 2013* %
Lead generators	**34.3**
'Offline' advertising	**33.5**
– TV	27.7
– Other	5.8
Online advertising	**32.1**
– Pay-per-click	20.9
– Comparison websites	3.1
– Affiliates	2.2
– Other	5.8

Source: CMA analysis of customer acquisition expenditure information provided by the major online lenders.

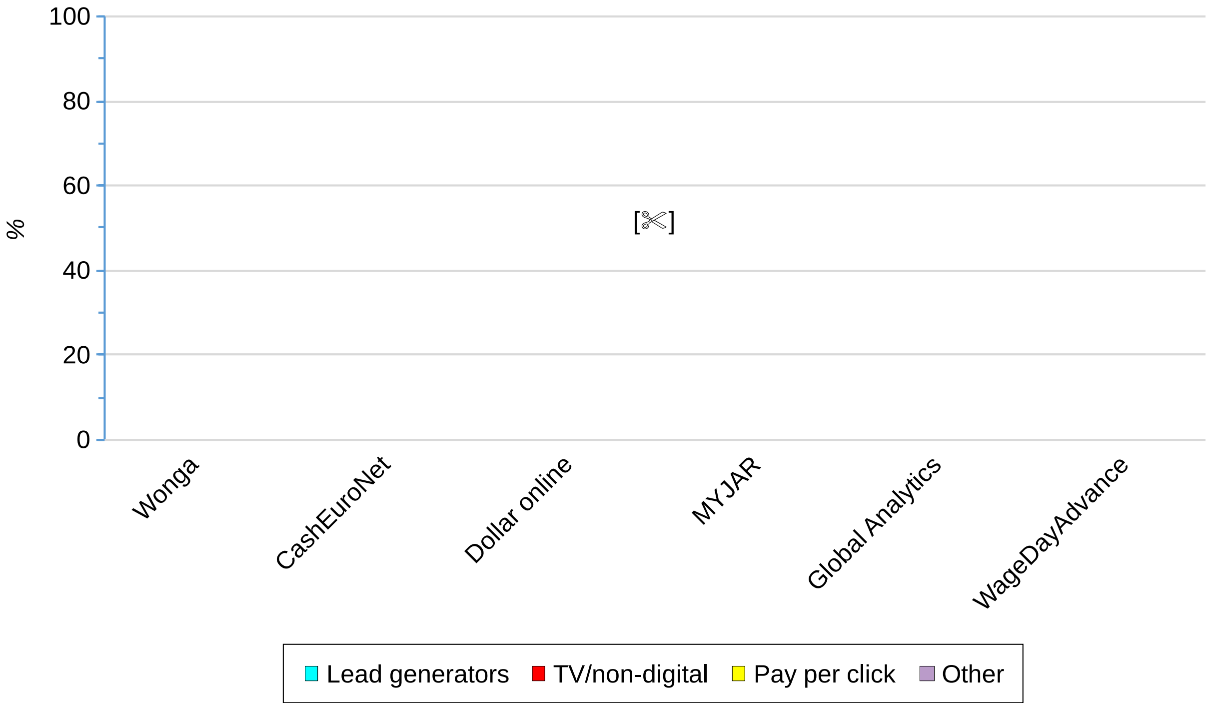
[521] The lenders included in this analysis are Ariste, CashEuroNet, Dollar (Payday Express and PaydayUK), Global Analytics, MYJAR, WageDayAdvance and Wonga.

7.42 The amounts spent by payday lenders on advertising are relatively large compared with those of other credit providers. In its report ‘Consumer Credit & Debt’, Keynote estimates that the top three payday lenders represented approximately 80% of the £33 million spent on main media advertising by providers of *all* forms of unsecured personal loans in 2012.[522] Further, the amount paid to Google for pay-per-click advertisements associated with the most popular payday-specific terms are high compared with terms specific to other credit products (an average of £[✂] paid per click for the term ‘payday loans’ in 2013, compared to £[✂] for credit card specific terms, and £[✂] for personal-loan-specific terms).

7.43 Within this overall allocation of customer acquisition expenditure, we observe significant variation in different lenders’ approaches. Figure 7.3 shows how the proportion of customer acquisition expenditure allocated to each channel varies by lender.

FIGURE 7.3

Customer acquisition expenditure by channel, 2013



Source: CMA analysis of customer acquisition expenditure information provided by the major online lenders.

7.44 The figure shows that the largest online lenders ([✂]) allocate a [✂] greater proportion of their customer acquisition expenditure to television and other forms of traditional advertising than other online lenders.[523] [✂] In contrast,

[522] Neilsen/KeyNote: *KeyNote Market Assessment 2012 – Consumer Credit & Debt report.*
[523] [✂]

the other online lenders tend to rely to a [✂] greater degree on lead generators.

7.45 For some lenders, relative expenditure on different customer acquisition channels has remained quite stable over time. For others, we have observed some significant shifts. For example, CashEuroNet has reduced the proportion of its expenditure allocated to [✂] over the period, while significantly increasing its relative expenditure on [✂]. Dollar told us that since [✂] it had increased its reliance on 'organic' customers, ie new business driven by advertising and branding.

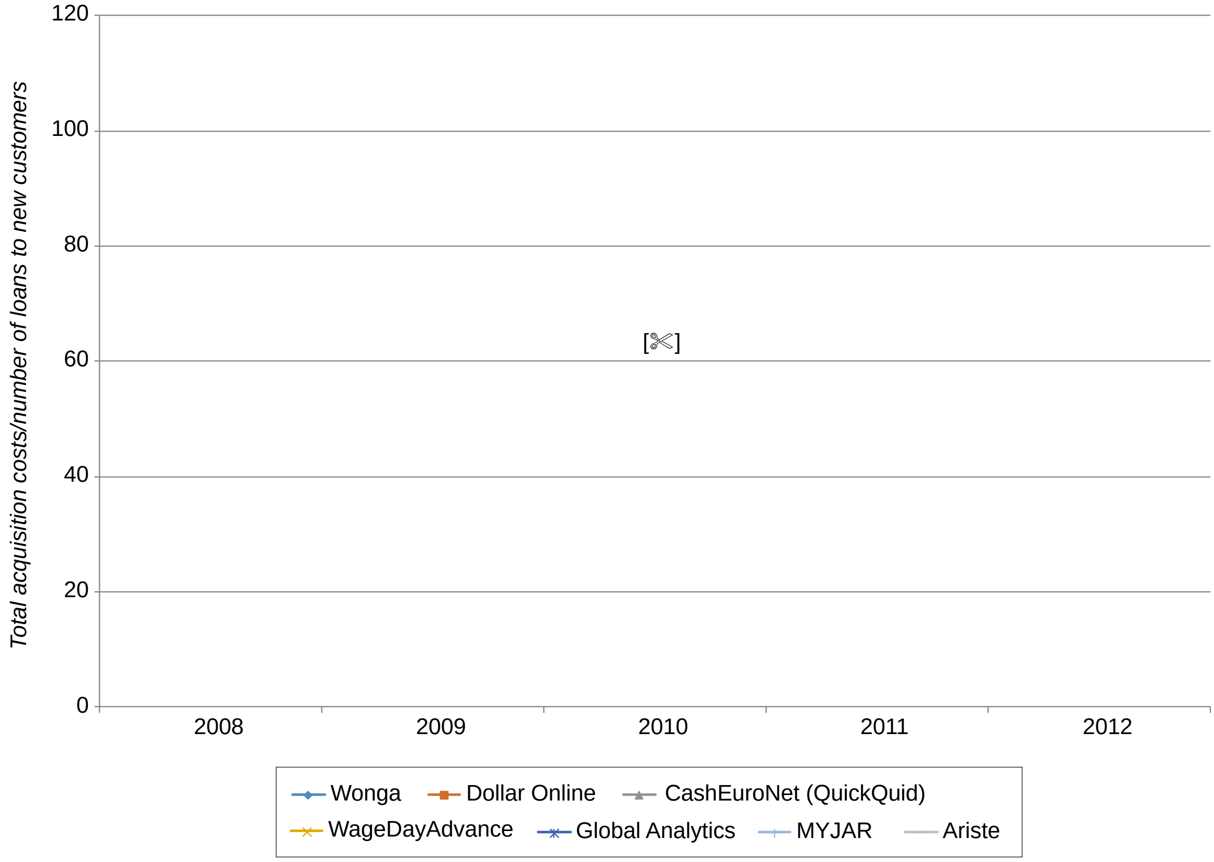
7.46 Different lenders also use a variety of different approaches when sourcing customers from lead generators. For example, Money Gap told us that the largest lenders typically operated 'towards the top of the pingtree', ie bidding for the most sought-after customers. In contrast, [✂].

7.47 We saw some evidence to suggest that the cost of a customer acquired via a lead generator had increased as the payday lending market had grown. Money Gap told us that in 2008, it received around £10 to £20 per accepted customer. For a customer of comparable quality, this [✂]. A number of lenders also referred to this trend. For example, CashEuroNet said that the price of the most expensive leads had risen between 2010 and 2013, from £[✂] to close to £[✂].We noted, however, that the cost of some leads might be expected to fall following the introduction of the FCA's price cap on 2 January 2015 if the cap were to reduce the expected revenue associated with acquiring a customer.

7.48 Looking more generally, the evidence suggested that lenders' total expenditure on customer acquisition (ie across all channels) for each customer acquired had generally increased over the period. Figure 7.4 shows how each lender's expenditure on advertising, promotions and commissions paid to lead generators, brokers and affiliates – per loan issued to a new customer – has increased since the 2008 financial year.

FIGURE 7.4

Expenditure on advertising, promotions and commissions paid to lead generators, brokers and affiliates, financial years 2008 to 2012



Source: CMA analysis of customer acquisition expenditure information provided by the major online lenders.

New entrants and smaller lenders' ability to use advertising to build a brand

7.49 We considered whether a smaller online lender would face disadvantages affecting its ability to use advertising to build a brand and attract customers organically (ie by relying on customers seeking out its website after hearing about its product, rather than customers being redirected to its website by, for example, a lead generator).

7.50 As noted in paragraph 7.44 above, the largest online lenders allocated a [✂] greater proportion of their customer acquisition expenditure to offline advertising than smaller lenders. Offline advertising is likely to be a major driver of customers' awareness of a lender's brand. Table 7.3 sets out the findings of different customer surveys with respect to awareness among customers of different lenders' brands. The table shows that Wonga (and to a lesser extent CashEuroNet) have considerably greater brand awareness than other payday lenders.

TABLE 7.3 **Survey evidence of customer awareness of online payday lenders' brands**

Lender	*CC survey*	*YouGov*	*CashEuroNet*
			%
Wonga	99	77	[✂]
QuickQuid	91	43	[✂]
PaydayUK	56	30	[✂]
Payday Express	28	14	[✂]
WageDayAdvance	-	5	[✂]
Lending Stream	-	-	[✂]
Base	927 'online only' payday customers	2,090 adults aged 18+	[✂]
Date	Oct/Nov 2013	Mar 2013	[✂]

Source: CMA survey.

Note: In all of the surveys reported above, brand awareness was 'prompted', ie customers were asked if they had heard of a particular brand. Where customers were not prompted about a particular lender in a survey, this is denoted with a hyphen.

7.51 One reason that it may be difficult for a new entrant or a smaller lender to build a brand and attract customers organically is if established brands control such a large share of voice that it would be difficult for a new entrant today to raise awareness of its product. The above findings on brand awareness indicate the current strength of the brand of Wonga in particular. A second disadvantage that may be faced by new entrants is the difficulty in recouping the significant cost of the advertising required to build a brand, and in particular television advertising. Wonga's total expenditure on television advertising in 2013 was £[✂] million, CashEuroNet's £[✂] million.

7.52 Commenting on the difficulties faced by lenders in raising awareness of their product, Elevate told us that despite spending a large amount on advertising (its marketing budget for 2014 was £[✂] million, compared with projected revenues of around £[✂] million), it expected that it would take some time for it to establish significant brand awareness, given the established brands of larger lenders. SRC told us that while it had looked at ways that it could be more strategic about its advertising placement, it would be difficult to get through the messaging not only of competitors like Wonga, but television advertisers more generally.

7.53 In relation to the cost of raising brand awareness, SRC told us that unlike in Canada, where it was the second largest player and able to afford a sustained television campaign, it did not have the scale to test whether more advertising would work in the UK. It referred to the high market shares of the largest payday lenders, and said, 'Wonga spends £30 million a year on TV and soccer sponsorships, et cetera. We have tried some TV and it just does not [work] … We cannot get through their kind of onslaught. I would love to try it at some point but we just do not have the pocket book for that right now.' Matching Wonga's media spend would require [✂]. Elevate told us that the cost of advertising on television was much higher today than it had been for previous entrants.

7.54 These difficulties were illustrated by an example of a television campaign run by a smaller lender that had not been particularly successful. Global Analytics, a lender that is primarily reliant on lead generators and pay-per-click advertising, ran a trial of television advertisements in 2011 and 2012, but with very limited success. It spent a total of £240,000 on television advertising in 2011, but estimated that this generated only around 1,000 new loans. It spent a substantially higher amount in 2012 – a total of £600,000 – but estimated that this resulted in only a very small uplift in booked loans (an increase of around 250). CashEuroNet said that there were clear economies of scale with television advertising although it considered this channel not to be necessary for a new entrant.[524]

7.55 However, we also noted that the cost of advertising had not discouraged Elevate from investing heavily in television advertising (although it told us that despite all the investment there was still a significant gap between itself and the two largest lenders in terms of brand awareness). Similarly, MYJAR said that while it would not be possible to match the advertising spend of the largest lender (ie Wonga), it would be feasible for it to match the expenditure of other large lenders. It was testing television advertising, and was confident of its ability to get a share of voice and establish its brand (although this would take a matter of years rather than months).

7.56 Dollar said that it did not think that a minimum investment would be required in order to advertise effectively. Similarly, Wonga told us that much of the costs were scalable and it also referred to the fact that in earlier years its advertising expenditure was much lower than in 2013.[525] We note, however, that when Wonga entered (in 2007), the payday loan market was substantially smaller than today and there were relatively few established lenders. Wonga was therefore likely to have benefited from a 'first-mover' advantage,[526] and since its entry it has built up a strong and well-recognised brand thanks to substantial investment in advertising.[527] New entrants today are likely to find it more difficult to achieve a similar brand strength due to the presence of established lenders.

7.57 Wonga also said that other lenders (Amigo Loans and MyMate) had spent significant amounts on television advertising in the recent years to raise

[524] See CashEuroNet's response to the provisional findings, paragraph 5.3.
[525] See Wonga's response to the provisional findings, paragraph 6.16(c).
[526] See *the Guidelines*, paragraph 222.
[527] See paragraphs 7.50 & 7.51.

awareness of their products.[528] We note, however, that both Amigo Loans and MyMate were supply guarantor loans which, as discussed in paragraph 5.13, are likely to provide only a weak competitive constraint on payday lenders.

7.58 It was also put to us that a lender might not need to build a brand to be successful. In particular, while CashEuroNet said that it was hard to build a brand, it told us that [✂]. We discuss potential limitations associated with the other key channels of customer acquisition open to lenders in the following paragraphs.

The limitations of other customer acquisition channels

7.59 Smaller online lenders typically rely much more heavily than larger lenders on customer acquisition channels other than advertising in order to grow their business.[529] Two channels that are particularly heavily used are lead generators and pay-per-click advertising, and we discuss the extent to which these channels could be relied upon as an alternative to building a brand in turn below. The extent to which we have observed lenders relying only on other channels to acquire customers (such as social media) has been very limited,[530] and so these channels are not discussed further.

- *Lead generators*

7.60 Lead generators have a number of advantages from the perspective of a new entrant or a smaller lender. In particular, they are accessible to all lenders, irrespective of size, and allow lenders to exercise close control over the volume and profile of customers that they want to attract. Lead generators allow a new entrant to build up a loan book quickly, in loan-by-loan increments, and to their own specification. In keeping with this, suppliers entering payday lending more recently have typically relied heavily on lead generators for new business.

7.61 Where a lender expands using lead generators, it is likely to impose little or no competitive constraint on the prices offered by established lenders. In particular, as set out in Section 6, an implication of the operation of this distribution channel – where customer application details are auctioned to the highest bidder – is that lenders acquiring customers through lead generators are unlikely to have a strong incentive to lower their prices and, in some

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[528] See Wonga's response to the provisional findings, paragraph 6.17(d),(e).
[529] Although we also note some variation between large lenders on the extent to which they rely on lead generators.
[530] For example, MYJAR, which attracted the largest number of customers through social media among the lenders that provided this information, sourced approximately [✂] new customers via this channel in 2013 (on average [✂] per month).

cases, the opposite may be true (in so far as lenders offering cheaper loans to customers may not be able to bid as much for leads).

7.62 There are also some limitations associated with relying on the lead generator channel from the perspective of a new entrant looking to compete with established lenders. First, while a large number of payday loan customer applications are available to purchase from lead generators, this is only around 40% of all new online payday customers. Given this, a lender that expands only by taking customers from lead generators will not access over half of the pool of potential new customers. Second, relying on lead generators does not help lenders in raising customers' awareness of their product.

7.63 In addition, a number of lenders told us that the quality of applicants coming via lead generators was lower than those coming from other channels and some lenders referred to what they saw as poor sales practices among some lead generators:

(a) [✄] said that it had sought to reduce its reliance on lead generators because of the 'supply risk' of using them to acquire new customers. It said that lead generators had the highest default rate of customer acquisition channels, and that this might be due to the fact that a lender would not have the opportunity to develop a relationship with a customer finding its website via a lead generator without any knowledge of the identity of the potential lender itself. This is in contrast to where a customer actively seeks out a lender's website and completes an application form on that lender's website, in which case there is an element of relationship creation.

(b) [✄] said that the quality of leads that it got from lead generators was poor, partially because of the practices of those suppliers, which tended to mislead customers. It referred to poor compliance among lead generators as a challenge associated with using this channel.

(c) SRC said that the credit performance of customers who came directly to its website was better than customers who came through its affiliate network.

7.64 We concluded that, given the ease with which they could be used to grow business, lead generators provided a simple and accessible way for a new entrant to establish an initial presence in the payday lending market. However, a lender would not impose an effective competitive constraint on existing lenders if it continued to rely on lead generators alone, and would not be able to access the larger pool of payday loan customers who did not take out their loan via a lead generator. In addition, there was some evidence to suggest that customers acquired via lead generators were generally of a higher credit risk than customers who approached a lender directly, which could put a smaller lender reliant on lead generators at a competitive disadvantage (although the extent of this disadvantage may decrease as a lender's ability to assess credit risk improves – see the discussion beginning in paragraph 7.77).

- *Customer acquisition via search engines*

7.65 An alternative channel of customer acquisition available to new online entrants would be to rely on search engines: either by paying for pay-per-click advertisements to be displayed alongside search results, or by taking steps to increase their website's prominence within organic search results via Search Engine Optimisation (SEO). Most lenders from which we collected information devoted some resources to these forms of customer acquisition, although this typically accounted for a relatively modest proportion of all customer acquisition expenditure ([✂]).

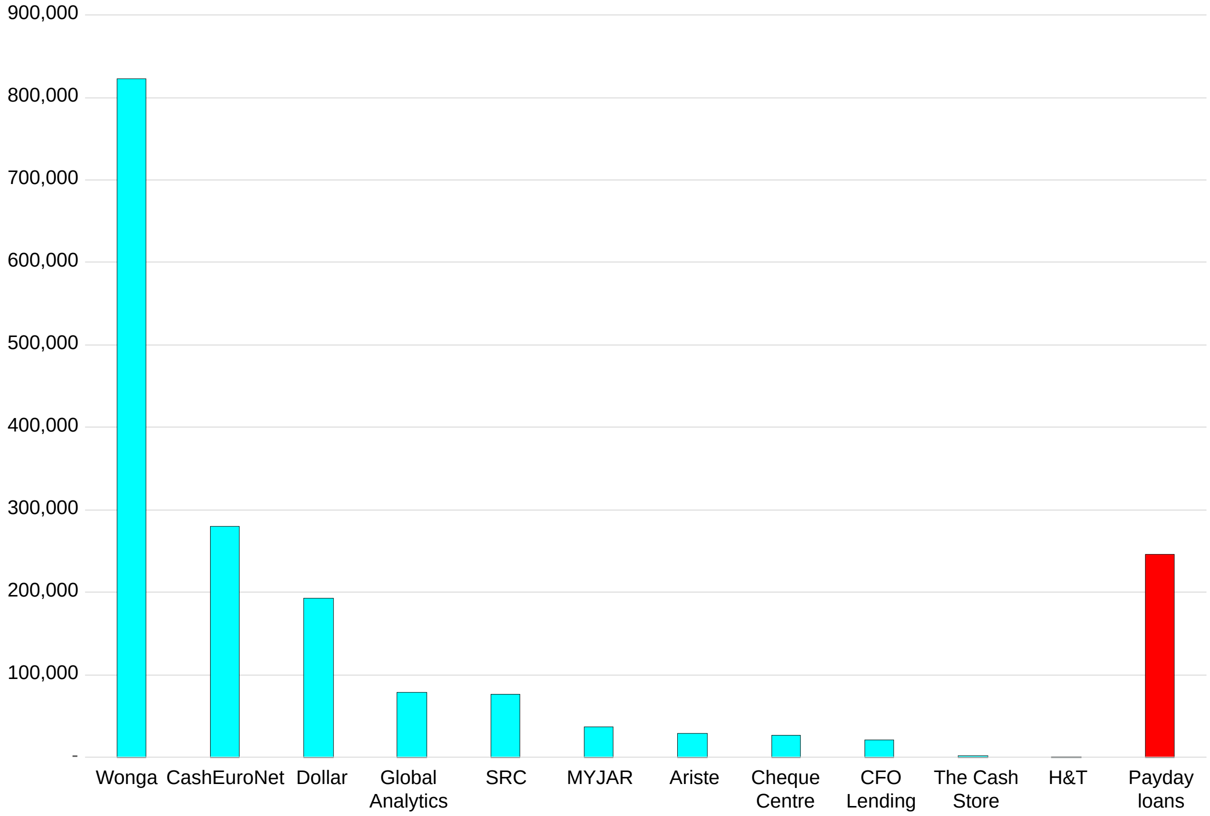
7.66 One limitation of relying on search engines to acquire customers is that, as with lead generators, this is likely to give lenders access to only a limited pool of potential borrowers, because many customers will go directly to a lender's website, and others will have already chosen a payday lender prior to using a search engine.

7.67 We collected information from Google on the average number of monthly searches for different search terms in 2013. In total, the ten most popular payday-related terms which were not specific to a particular lender generated on average around [✂] searches per month.[531] The most popular term, accounting for the majority of these searches ([✂]), was 'payday loans', with between 200,000 and 300,000 searches per month in 2012.[532] Lender-specific terms often received a greater number of hits. Figure 7.5 shows the total number of searches for a number of lender specific payday-related terms, and the term 'payday loans' on Google in 2013.

[531] These terms were [✂].
[532] Google Adwords Keyword planner.

FIGURE 7.5

The average number of monthly searches for different search terms using Google, 2013



Source: CMA analysis of data from Google keywords planner.
Note: The average monthly searches reported relate to the search terms specific to the products of each lender (eg 'wonga' for Wonga, but 'quickquid' for CashEuroNet). For some lenders we included a number of keywords relating to their products/brands.

7.68 These results illustrate the strength of the Wonga brand, as well as suggesting that many customers are likely to have already been influenced in their decision of which provider to use before using a search engine. The customer research we undertook as part of our remedies process found that customers often did not search and went directly to a lender they know. Even when they use a search engine to find a lender, they tend to look for lenders that they know or they are familiar with.[533]

7.69 The evidence on the number of searches for non-lender specific terms related to payday loans also suggests that the volume of new customers available via pay-per-click advertising is unlikely to be sufficient on its own for a lender to expand to become a payday lender of a significant size. In particular, if we combine estimated click-through-rates[534] for the term 'payday loans' (up to 5%

[533] Customer research, p14.
[534] As indicated by Google AdWords Keyword Planner.

for a lender bidding a relatively large amount) with the total number of monthly searches for the ten most popular payday related terms, this suggests that a lender bidding a significant amount on pay-per-click advertising in a search engine might in a 'best-case' scenario be able to direct up to [✂] potential customers to its website a month. We expect that only a small proportion of these customers would then go on to take out loans; assuming that this conversion rate is [✂]% ([✂]), then this scenario would imply fewer than [✂] new loans being generated by pay-per-click advertising per month. By comparison, CashEuroNet, one of the largest payday lenders, made approximately [✂] loans to new customers per month on average in 2013.[535]

7.70 In addition to the limited pool of potential customers, we identified further limitations associated with acquiring customers via search engines.

7.71 First, pay-per-click advertising can be an expensive method of acquiring new customers, because lenders must compete with lead generators in auctions for advertising space. Lead generators will generally be able to pay relatively high amounts for these advertisements, as their business model enables them to maximise the revenue they can earn from any given customer application by selling that lead to the highest bidder.

7.72 Second, it may be difficult for a lender to rely on influencing its position in Google's search results for payday-related terms as a source of new customers, given the difficulty in identifying the precise factors which will determine the ranking of a website (although general 'best practice' guidelines exist), and the fact that a website's position in Google's search results will depend on the content of other websites as well as its own content. In relation to this, Dollar said that acquiring customers via organic search was challenging because it was so dynamic, which meant that nobody had a particular competitive advantage.[536]

7.73 One factor that may serve to heighten this difficulty in the payday lending sector is the prevalence of 'spam' (where individuals try to manipulate search engine results, eg by filling their own pages with irrelevant terms). Where it is successful, spam will push lenders' own websites further down the rankings.

[535] In its response to the provisional findings (paragraph 6.16), Wonga told us that we had overlooked the fact that entrants could use a multitude of advertising channels and that 'it is inappropriate to focus on whether any single channel can be relied upon to deliver wide access to potential customers'. However, we noted that even if we consider the volume of new business available to a smaller lender using *both* lead generators and pay-per-click advertising (and putting to one side the disadvantages of these channels), a significant proportion of applicants will still not be accessible, because many customers visit the websites of the largest lenders directly because of the established brands of these providers.
[536] Google told us that 'there is considerable information available to payday lenders and PCWs (and website designers in general) to help them improve their websites so they are more likely to be relevant and useful in respond to queries on Google Search' (see Google's response to the provisional findings, paragraph 17).

Relating to this, a presentation prepared by Lending Stream referred to the existence of 'bad actors that repeatedly use "black hat" SEO techniques[537] to hijack sites and "steal" many leads out of the market'; and MYJAR said that it was at a disadvantage in terms of SEO because it upheld decent practices.

7.74 In addition, the prevalence of spam relating to payday lending had caused Google to take various steps in order to mitigate spam. We were told that changes to Google's algorithms had had an impact on different lenders' rankings, and we were aware that one outcome of these changes had been to push lenders' websites further down the rankings, in deference to news articles and other non-commercial pages relating to payday lending. One specific example brought to our attention was a penalty imposed by Google on [✂], which [✂] told us took place because a number of poor-quality sites were linking to its website. The penalty reduced the ranking of the [✂] website by 50 positions for all search terms.

7.75 The unpredictable nature of organic search was supported by our consideration of Google search results for a number of payday-related terms. We found that very small lenders appeared relatively prominently among search results, and that the prominence of different lenders varied substantially over time. For example, WizzCash – which issued [✂] loans a month on average in 2013 – regularly appeared as the most prominent payday lender during the period of our review. It told us that it had engaged an SEO marketing agency to manage its website content so as to boost its rankings (for example, by engaging in projects like running a blog). It had been surprised by its success, given its reliance on 'white hat' techniques.[538]

Conclusions on customer acquisition

7.76 We concluded that despite the historic success of some online lenders in establishing themselves in the payday lending market, the ability of a new online entrant to expand and establish itself as an effective competitor is likely to be obstructed by a number of characteristics of the market which make it difficult to raise customers' awareness of their products. In particular, the time and expense required for a lender to establish itself in the market today will be increased by difficulties associated with raising customers' awareness of their product in the face of the barriers to shopping around and switching summarised in paragraph 6.117, the strength of the well-established brands that already exist in the market and the costs associated with advertising on a

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537 'Black hat' techniques essentially refer to deceptive means of driving traffic to a site and are meant to trick search engines into indexing the site different than it really is.
538 'White hat' techniques essentially refer to acceptable and established means of optimising a website to drive traffic to it.

sufficient scale to be effective in overcoming these obstacles. New entrants with established brands in other markets may be able to overcome this disadvantage more easily than other suppliers.

Disadvantages faced by new entrants and smaller lenders in assessing applicants' credit risk

7.77 A core capability for a payday lender is the ability to assess the credit risk of new and returning customers when deciding whether to grant them a loan. One factor that may put smaller lenders at a cost disadvantage – and so potentially impede their expansion – is their more limited ability to assess applicants' credit risks, due to their greater reliance on new customers, and the lack of experience and data available to them to develop and calibrate their risk models.

7.78 While the ability to assess credit risk accurately will be important in all credit markets, it is likely to be particularly significant in the payday lending sector because of the relatively high credit risk profile of payday loan customers (see paragraph 6.59). In addition, certain characteristics of the payday lending sector (and especially the short-term nature of payday loans) means that there are significant limitations to the reliance that lenders can place on information from CRAs when assessing the risk of new applicants (this is discussed further in paragraphs 7.103 to 7.107).

7.79 Our analysis of financial data indicates that a payday lender's ability to assess credit risk accurately will have a significant impact on their performance. Costs associated with doubtful debt represented around 45% of total costs for all lenders in 2012. For online lenders the proportion is around 50%, and for high street lenders this is around 25% (as these lenders must also pay store and staff costs).

7.80 There is significant variation in the approaches taken by different lenders to credit risk assessment. Nevertheless, there are also certain commonalities. As discussed in paragraph 2.70, when performing credit risk assessments lenders will typically rely on some combination of information collected during the loan application process; any information already held about the applicant internally; and relevant third party information sources (eg information purchased from CRAs).

7.81 Most lenders also use automated credit models, which can be used to process the relevant information and generate an internal credit score for a customer in a matter of seconds. These models differ in the information that is relied upon as being predictive of the likelihood that a customer will repay their loan, the weight given to different pieces of information, and the way that information is processed.

7.82 Some lenders' risk assessments also have a manual (ie non-automated) element. All high street lenders have a staff member reviewing the application process. [✂], did not rely on the member of staff to make the ultimate lending decision in all cases. By contrast, only one of the major online lenders, [✂], relies on a human underwriter to make the final lending decision.

7.83 Figure 7.6 shows how default risk – as measured by the principal loss rate[539] – varies across lenders. It shows that the extent of variation is significant, with the loss rate of some lenders as much as [✂] times greater than that of other lenders. This suggests that variation exists in the ability of different lenders to accurately assess different applicants' credit risk (although this pattern could in principle also be driven by other factors, such as variation in lenders' collection policies, lenders' appetite for risk and approach to customer acquisition, or differences in lenders' products in turn driving differences in their customer profiles).

FIGURE 7.6

Variation in principal loss rate across lenders, financial year 2012

[✂]

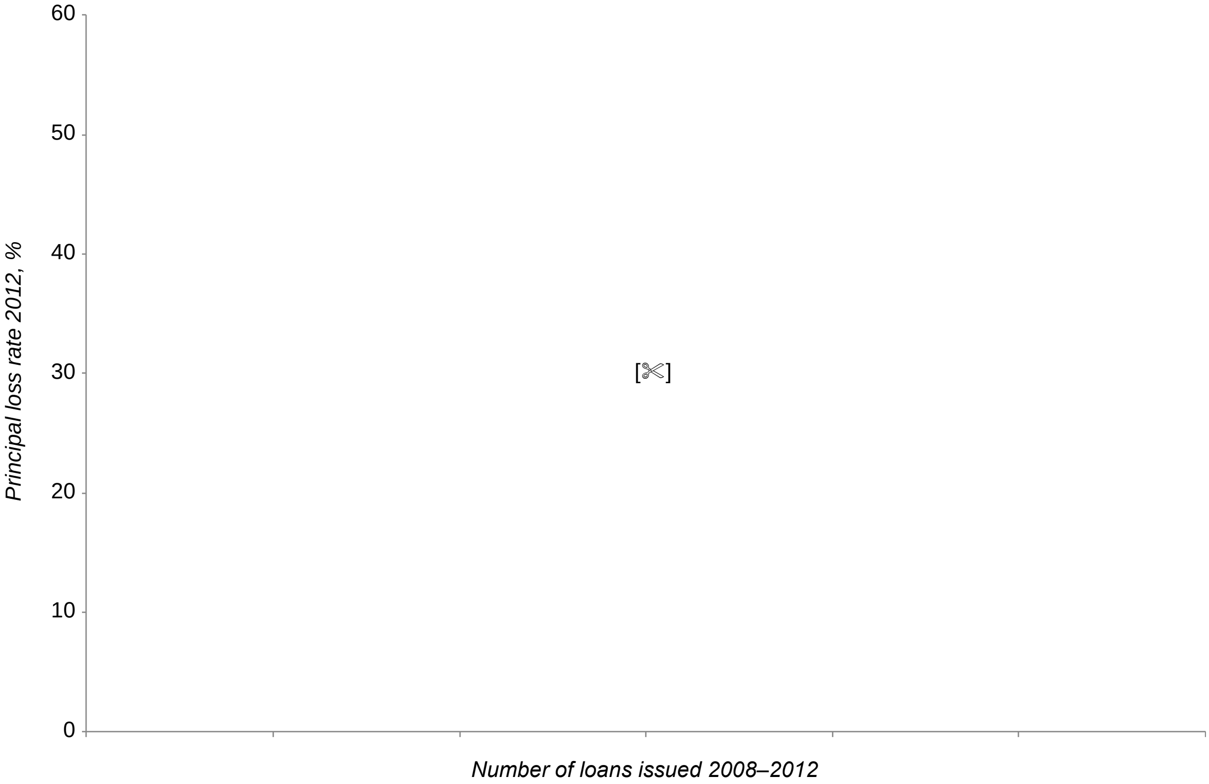
Source: CMA analysis of financial data provided by the major lenders.

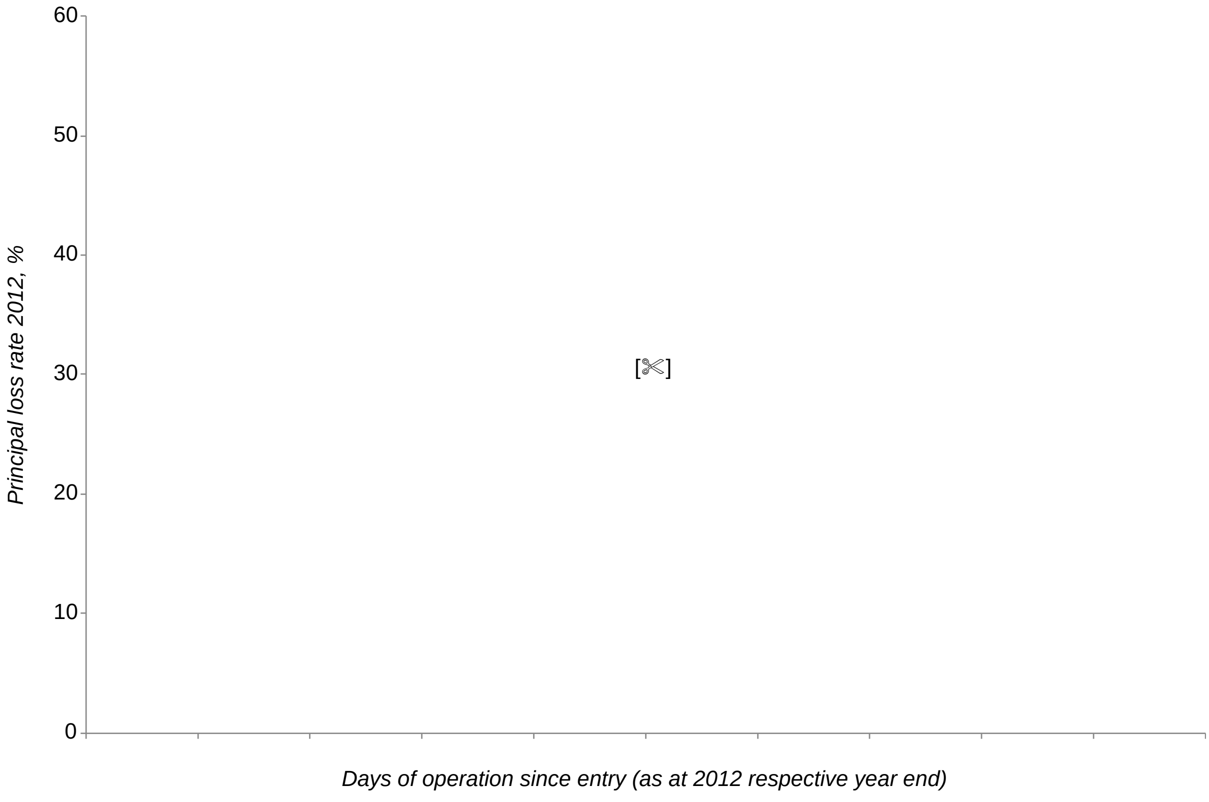
7.84 We considered whether a lender's ability to assess credit risk accurately was influenced by the cumulative number of loans they had issued and/or length of time that they have spent in the market. The top panel of Figure 7.7 shows how principal loss rates vary with the total number of loans issued by a lender since 2008. The lower panel shows how principal loss rates vary with the number of days passed since the lender began issuing payday loans.

[539] This measure of default risk is calculated as *1 – (loan principal collected / loan principal issued) for a given financial year*.

FIGURE 7.7

How principal loss rates vary with the cumulative number of loans issued, and the number of days since the lender entered payday lending





Source: CMA analysis of financial data provided by the major lenders.
Note: 2012 is based on the last reported financial years ended July to December 2012 and January to June 2013.

7.85 The charts suggest that although they are clearly not the only relevant factors at work, a lender's longevity in the market and the cumulative number of loans issued by that lender are positively correlated with its ability to assess credit risk. Interpreting the nature of these relationships is not straightforward, as various confounding factors could in principle exist.[540] To explore these relationships further, we considered in detail two potential reasons why a new entrant might be at a disadvantage in terms of their default costs when compared with a more established lender. First, new entrants are likely to be much more reliant on new customers. Second, new lenders will have had less time and information available to them to develop their risk models. We discuss these possibilities in the subsequent sections, before considering the potential role of information available from CRAs in removing any asymmetries between new and established lenders.

Reliance on new customers

7.86 One way in which new entrants may face a disadvantage in assessing credit risk is because of their heavier reliance on 'new' customers (ie customers to whom the lender has not lent previously).

7.87 As discussed in paragraphs 2.48 and 2.49, demand for payday loans is typically recurring, with a payday loan customer taking out nearly six payday loans in 2012 on average, and around three-quarters of borrowers taking out more than one loan. One impact of this is that lenders rely significantly on repeat business. Around 80% of all loans made by payday lenders in 2012 were to customers to whom a loan had previously been made by that lender.

7.88 A lender's ability to assess the credit risk of a repeat customer is likely to be considerably better than its ability to assess the credit risk of a new customer. In particular, in the case that a customer has repaid the previous loan, that customer has already demonstrated that they are willing and able to repay a loan. Conversely, a lender will know not to lend further amounts to a repeat customer who did not repay a previous loan. Moreover, the information available regarding an existing customer will typically be much richer than that available from a CRA for a customer that has not been lent to before.

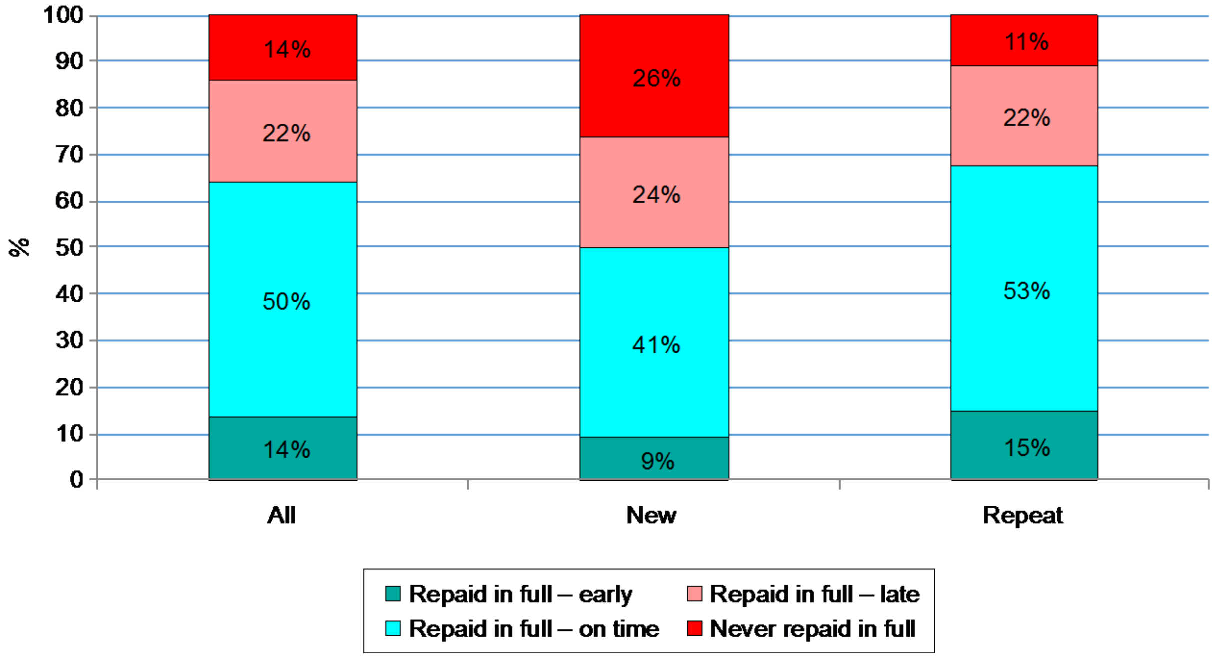
7.89 The existence of differences in lenders' abilities to assess accurately the risk of new and repeat customer groups is supported by evidence on default rates. Figure 7.8 shows the proportion of loans issued to new and repeat customers which were repaid in full early, repaid in full on time, repaid in full late, or

[540] For example, the relationship might be driven, at least in part, by a survival effect, whereby those lenders which start out with superior approaches to judging risk are more successful, and so go on to make more loans.

never repaid in full. It shows that around 26% of all loans to new customers were never repaid in full, compared with 11% of all loans to repeat customers.

FIGURE 7.8

Loans issued in 2012, status as of 1/10/2013



Source: CMA analysis of transaction data of 11 major lenders.

7.90 This pattern was also recognised in discussions held with a number of lenders. For example, Wonga said that repayment data for an existing customer was a very valuable data point, and that it was easier to assess a returning customer than a first-time customer. It also provided data showing that principal loss rates for returning customers were typically around [✂] of those for new customers, or less. SRC told us that the riskiest loan was the first loan made to a customer because no prior credit history was available for that customer. Dollar said that there was a difference in credit quality between new customers, and customers who had been lent to previously. This was particularly the case in payday lending because of the relative lack of historical credit information available from CRAs. There was a natural progression as a business grew for the proportion of repeat customers to increase. Evidence provided by Global Analytics showed that its charge-off rates had been consistently higher for new customers compared with repeat customers.

7.91 Because it will take time to establish a stock of repeat customers, new entrants will typically be reliant on new customers to a much greater extent. This implies that they will be serving a riskier customer group and so will be at a cost disadvantage compared with established lenders.

7.92 The key determinants of how long it takes for a new entrant to develop a stock of good-quality repeat customers and overcome this disadvantage will be the number of times that customers return for additional credit, and the length of the period over which this takes place. All else being equal, the average longevity of the relationships between existing payday lenders and their customers will tend to increase the length of period for which a new lender will be at a disadvantage.[541]

7.93 Dollar told us that it estimated the average customer life to be approximately [✄], while CashEuroNet told us that the average length of time spent by a payday customer with the same lender in the market was around [✄]. Table 7.4 shows that, looking at customers of the 11 major lenders in August 2013, for around 40% of customers their first loan with their lender was taken out a year or more ago. For around 18% of customers their first loan with their lender was more than two years ago, and for 1% of customers, their first loan with their lender was five years ago or more. This suggests that while the largest increases in a lender's stock of repeat customers are likely to be made within a year, the stock of repeat customers is likely to continue to develop over a period of years rather than months.

TABLE 7.4 **Length of payday customers' relationships with their lender (ie time since their first loan from a lender), August 2013**

Length of relationship with lender	*Proportion of all payday customers, August 2013* %
Up to one year	59
1–2 years	23
2–3 years	12
3–4 years	4
4–5 years	1
5 years or more	1

Source: CMA analysis of transaction data provided by the 11 major lenders.

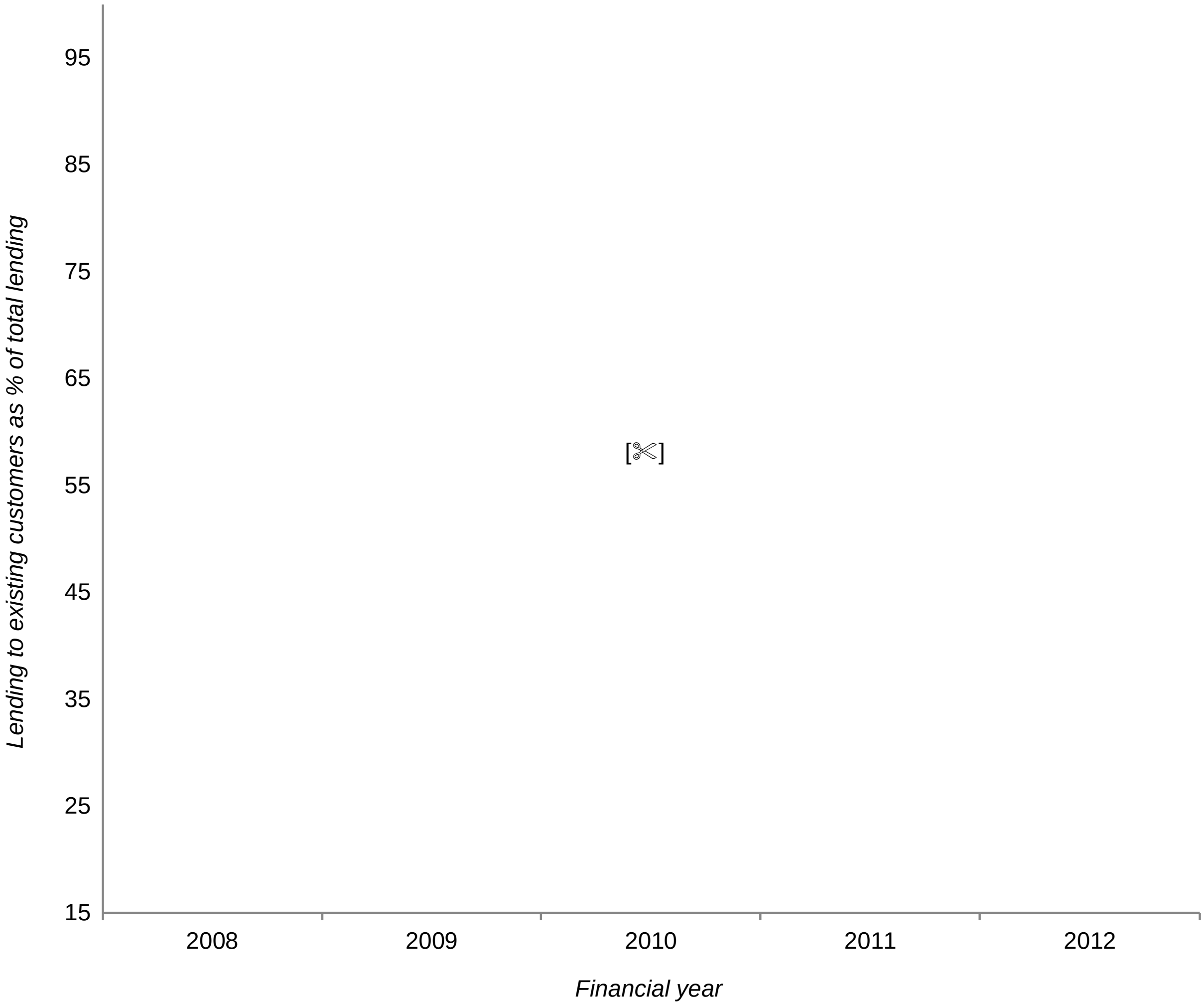
7.94 This observation is also supported by our analysis of the evolution of the proportion of different lenders' businesses accounted for by new customers since entering payday lending. Figure 7.9 shows how the proportion of loans that went to existing customers evolved in the period financial year 2008 to 2012 for a number of the major lenders who began payday lending in 2006 or later (information for 2006 and 2007 for those lenders that were active in these years is not available). It shows that typically these lenders have

[541] To give an example – assume that a lender acquires a constant number of new customers per month, and that following their first loan from a payday lender, each customer goes on to take out a further loan with that same lender every two months for a total of six loans. Then it will take a year for a new entrant to reach the same level of reliance on repeat business as established lenders. If each customer returns for six loans in total, but takes out a loan every four months, then it will take a new entrant two years to have the same stock of repeat customers as an established lender. Similarly, if each customer returns for 12 loans at a frequency of one every two months, it will take a new entrant two years to have the same stock of repeat customers as an established lender.

observed a considerable increase in the proportion of loans made to existing customers since entering payday lending. These gains have generally been sustained across a number of years, suggesting that the process of accumulating a stock of repeat customers can continue for a significant period.

FIGURE 7.9

The evolution in lending to existing customers as a percentage of total lending, financial years 2008 to 2012

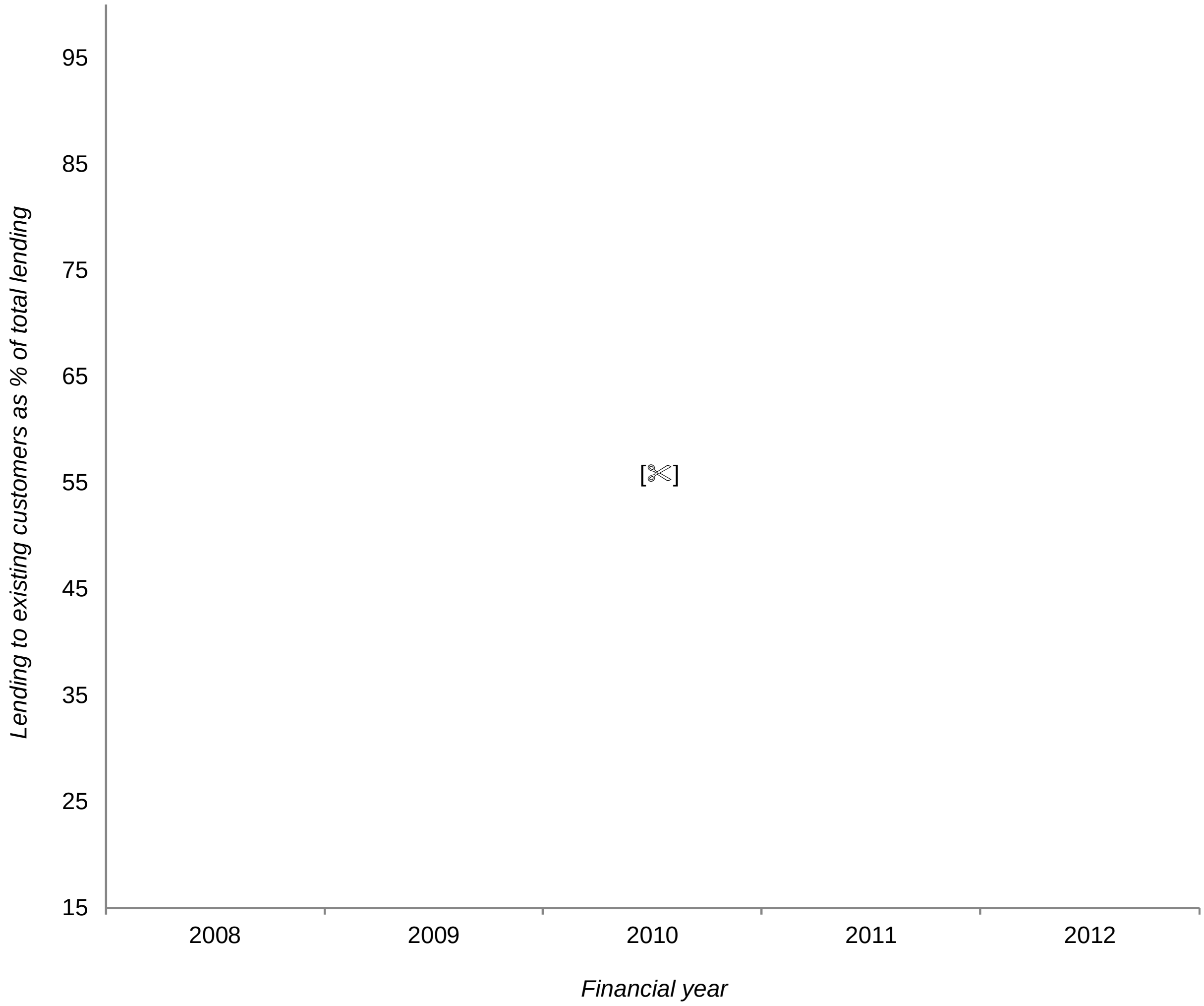


Source: CMA analysis of financial data provided by the major lenders.

7.95 Figure 7.10 shows the same information for [✂], which have both been in the market for longer periods of time. It shows [✂].

FIGURE 7.10

The evolution of lending to existing customers as a percentage of total lending for less recent entrants, financial years 2008 to 2012



Source: CMA analysis of financial data provided by the major lenders.

Information and experience available to develop risk models

7.96 In addition to their greater reliance on new customers, new entrants may face a disadvantage relative to more established lenders because of their relative lack of experience in assessing applicants' credit risk, and lack of information available on historic default behaviour which can be used to test and develop new and improved approaches to credit risk assessments.

7.97 Figure 7.11 illustrates variation across lenders in the proportion of first-time customers that never repay their loan in full. It shows that considerable variation exists in the credit risk of different lenders' new customers, with around [✂]% as many customers of [✂] never repaying their loan in full as is the case for [✂].

FIGURE 7.11

Proportion of loans to new customers never repaid in full

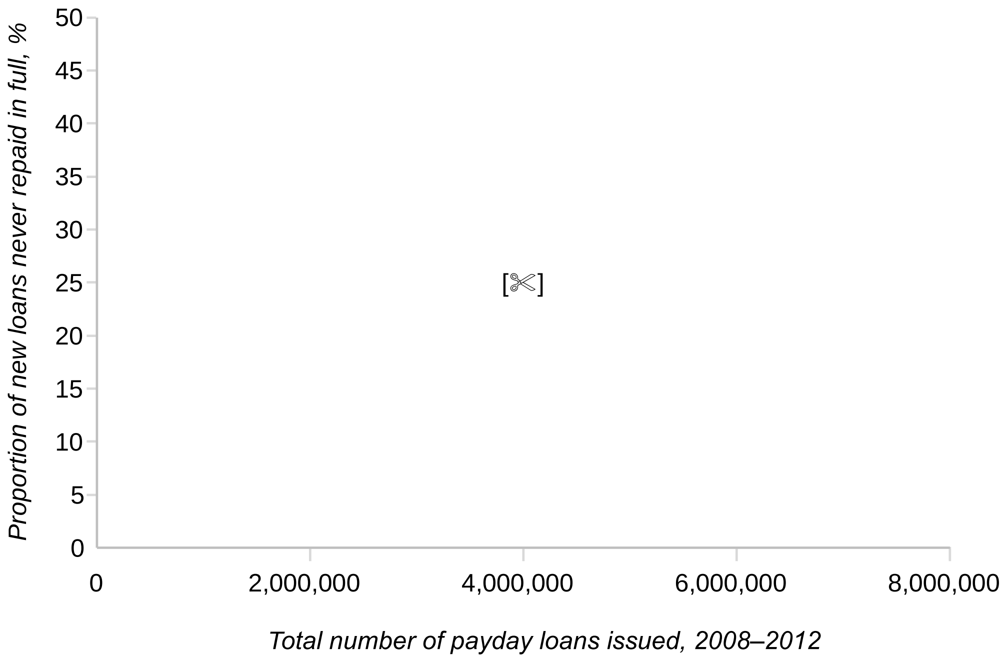
[✂]

Source: CMA analysis of major lenders' transaction data.
Note: Loans issued in 2012 (status as of 1 October 2013).

7.98 To the extent that we interpret variation in default rates as reflecting variation in different lenders' ability to assess credit risk, then this suggests that in addition to differences in the extent of repeat business between lenders, some lenders are better than others at credit risk assessments. Figure 7.12, which plots these new customer default rates against total number of payday loans issued by a lender in the period 2008 to 2012, shows that there is a tendency for lenders that have higher default rates among new customers to also be those lenders that have issued the fewest loans, although we noted some significant exceptions to this pattern, and acknowledge that the cumulative number of loans issued is clearly not the only factor at play in driving the default rates that we observe (other factors such as lenders' customer acquisition strategies may also play a role).

FIGURE 7.12

How the proportion of loans to new customers that are never repaid in full varies with the cumulative number of loans issued by a lender



Source: CMA analysis of major lenders' transaction data.
Note: The proportion of new loans never repaid in full is based on the loans issued in 2012 (status as of 1 October 2013).

7.99 The submissions of a number of lenders supported the idea that lenders' risk models continue to develop with experience. For example, CashEuroNet discussed how it continuously tested new variables in 'dry runs'. It said that the QuickQuid approval model had [✄] variables today, and that it had tested and discarded over [✄] other variables over the last six years. It said that its ability to identify customers able to afford loans was a key competitive advantage, and that it continually developed and improved its methodologies in order to stay ahead of the competition.

7.100 It was clear from lenders' descriptions of their credit risk assessments that historic information often played a key role in model development. For example, Wonga told us that monitoring of arrears was a critical indicator of the success of Wonga's risk management system, and that it used the information regularly to monitor and fine tune its models (although other than in the early stages of a product cycle, model updates were not common). MYJAR described how it had spent time gathering data in recent years in order to help refine its underwriting, and how its business had evolved as a result, such that its ability to write a better loan had improved over the past 18 months. It said that one of the biggest barriers to entry was the amount of data needed in order to make safe underwriting decisions – it cost a lot of money in terms of customer acquisition and bad debt in order to gather data and learn the lessons necessary in order to make credit decisions.

7.101 [✄] also referred to the role of account level historical application data in developing its bespoke scoring system. However, it told us that there were diminishing returns in terms of how much additional customer information allowed a lender to improve its models and decision-making, such that [✄]. It said that it had been able to build a robust high-quality scorecard with a sample of [✄] loans including [✄] 'goods' and [✄] 'bads', and referred to a paper which it said showed that although performance could be improved with a greater number of 'bads', the incremental improvement was very low beyond this point, and models built with this level of 'bads' could still work very well and were robust.

7.102 Further, CashEuroNet said that although internal models for assessing credit risk improved over time, this did not constitute a barrier to expansion because the duration of the loans was so short, which meant that the necessary learning could take place quickly. A good credit model could be built in six months.

Credit reference agency information

7.103 The asymmetry in the amount and quality of information available to new entrants and established lenders about customer repayment behaviour may be offset, to some extent, by the availability of CRA data. CRA records will include some information on previous loans taken by a customer and their repayment behaviour, and is available to lenders irrespective of how long they have been in the market. For example, Wonga said that the information on repayment that it had shared with CRAs meant that a start-up would have very robust information on which to base its underwriting. The breadth and depth of data available would give an entrant today an enormous advantage that was not available when it entered the market.

7.104 However, a number of lenders expressed concerns about the nature of the information available from CRA data:

(a) MYJAR said that lending decisions could not be based on CRA information alone, and referred to an example of a lender that had attempted this, and was struggling as a result.

(b) SRC told us that ‘although we have found a variety of CRA data sources and variables that are predictive of performance in the US, we have struggled to find CRAs or payday-specific CRAs that provide the same level of predictability in the UK’.

(c) CashEuroNet said that QuickQuid imported raw data from [✄] and several other specialised identity verification and prepackaged reports. Its experience in modelling sub-prime customers showed that the standard credit scores produced by CRAs were unsuited for its customer base. Accordingly it had built its own credit-scoring system using individual values for numerous [✄] variables.

7.105 Historically, a key limitation of CRA information has been the frequency with which it is updated. Typically this has been monthly in line with other credit products, which is problematic in this market, given the very short-term nature of most payday loans. We note, however, that the FCA is currently working with lenders and CRAs to increase the frequency of data-sharing with the intention that this data-sharing will be ‘real-time’ and that significant progress has been made over the past 12 months in the development of these systems. At present the frequency of data updates in the existing and proposed real-time solutions offered by CRAs varies from near instantaneous to daily batch updates (see Appendix 9.3).

7.106 Relating to the development of real-time data:

(a) Elevate said that real-time data should help but it did not know yet the extent to which it would. It also said that the most important aspect around credit risk management for Elevate was the time to learn and iterate its lending models.

(b) MYJAR told us that it did not expect the developments in real-time data to lead to a big improvement in its risk assessments. It said that increasingly little reliance was being placed on CRA information. Details included within application forms were particularly important predictive factors, and these would not be available in CRA information.

7.107 Given this evidence, we took the view that even following the development of effective real-time credit record databases, the information disadvantage faced by new lenders would not be eliminated entirely by the availability of CRA information. This is because data from a CRA will only provide key indicators relating to the borrower's loan and its repayment, and will not provide the same level of detail about, for instance, the customer's application and their interaction with the lender. Moreover, information held by CRAs – and especially by any one CRA – will often be incomplete. Nonetheless, we considered the move towards RTDS to be a positive development, in terms of competition. In Section 9, we consider the scope for further improvements in RTDS as a possible component of a remedy package to address the AEC.

Conclusions on credit risk assessments

7.108 While the ability to assess credit risk accurately will be important in all credit markets, it is likely to be a particularly crucial determinant of a provider's success in the payday lending sector, because of the particularly high credit risk profile of payday loan customers. Because of their greater reliance on new customers and the role of learning in the credit risk assessment process, new entrants are likely to face some disadvantages in their ability to assess credit risk for an initial period, which – all else equal – will put them at an initial cost disadvantage relative to more established providers. Given the nature of the disadvantage, new entrants with lending experience from other credit markets, or existing customer bases that they can target, may have some advantages compared with other types of supplier.

Impact of regulatory developments

7.109 As discussed elsewhere in this report, we have recently seen significant regulatory change affecting the payday lending sector, including the new CONC rules introduced by the FCA on 1 April 2014, and the price cap which came into force on 2 January 2015. These developments are described in Section 3 and Appendix 3.1.

7.110 We considered how the FCA's enhanced regulation of the sector was likely to affect any constraint that might otherwise be imposed on incumbent payday lenders by the prospect of further entry and expansion.

7.111 Given the ongoing political and regulatory focus on payday loans, there has been a significant degree of uncertainty affecting the payday sector in the past couple of years, which may have affected suppliers' willingness to enter the market and the willingness of existing lenders to expand in that period. A number of lenders expressed this view. For example, Dollar said that lenders were hesitant to enter the market at the moment because of the instability and the uncertainty created by regulatory changes. Elevate said that the current uncertainty was stifling innovation, with lenders putting plans to launch new products on hold.

7.112 We noted, however, that the level of uncertainty affecting suppliers in the payday lending sector may be expected to have declined during 2014 as the details of the price cap have been finalised, leading up to the publication of final proposals in November 2014, and as the FCA's other new rules have started to bed in.

7.113 Of greater likely future significance is the impact of the FCA's price cap and other regulatory developments on lenders' profitability. In particular, modelling carried out by the FCA suggests that the price cap is likely to significantly reduce lenders' revenues, and lead to substantial declines in profitability. This in turn is likely to reduce the incentive for new suppliers to enter the market, and may lead to the exit of less efficient/well-resourced lenders (though we expect that a variety of suppliers would nonetheless remain in the market following the introduction of the cap).[542] In addition, reduced profitability is likely to increase the time and resources a new entrant requires to overcome its initial disadvantages and establish itself in the market, lessening the ability of smaller lenders to effectively constrain incumbents.[543] While new entrants may benefit if the cap was to result in lower costs for acquiring leads (see paragraph 6.122*(d)*), we did not consider that the disadvantages facing smaller lenders looking to establish themselves in the payday lending market would be mitigated to any significant degree by the FCA's changes.

7.114 We noted that one possible effect of the FCA's price cap – and enhanced regulation of the sector more generally – that might assist entry is that it might improve the sector's reputation, which in turn may reduce the deterrent faced by businesses with established reputations in other sectors which are considering entering payday lending. Nevertheless we considered that even if the reputation of the sector were significantly improved as a result of the price cap and other regulatory developments, the constraint imposed on

[542] See paragraphs 4.171 & 4.172.
[543] One lead generator (SGE Group) also told us that the price cap did not take into account that the base rate will rise in the next year and it will be '4 to 6 times the current rate in the next few years, [✄]'. It told us that this would make it more costly for smaller/new entrants to access capital which, in turn, would further lessen their ability to effectively compete with incumbents. (See SGE Group's response to the PDR.)

incumbents by the threat that mainstream suppliers might enter the market would not be sufficient to effectively constrain their prices, given the barriers to shopping around and switching identified in the previous section.

7.115 We concluded that, on balance, recent regulatory developments in the payday lending market were likely to create market conditions that would be less favourable to entry and expansion than those observed historically, and so would reduce the extent of any competitive constraint which the prospect of new entry or expansion might otherwise impose on incumbent lenders.

Conclusions on the constraint from entry and expansion

7.116 The first payday lenders began offering payday loans to UK customers over ten years ago. Since then, we have observed a large number of new providers enter the market, using a variety of different entry strategies – such that by the end of 2013 there were more than 90 payday lenders active in the market. Before the recent contraction, the size of the payday lending sector as a whole (high street and online) expanded very rapidly since 2008, with the total number of payday loans issued by the major lenders increasing from fewer than 2 million in 2008, to over 8 million in 2013. Within this growing market, a small number of lenders have managed to expand successfully their market shares – Wonga expanded particularly quickly since its entry in 2007, becoming the largest payday lender by some distance.

7.117 Notwithstanding these historical patterns, and as shown by the evidence set out in Section 4, entry by new firms into the payday market has not resulted in existing lenders being effectively constrained when setting their prices. An important cause of this are the barriers identified in Section 6, which reduce payday customers' sensitivity to prices, and weaken price competition between lenders. For example, on many occasions where we have observed new providers entering payday lending, these lenders have relied to a large extent on lead generators for new customers: a lender sourcing new customers via a lead generator is likely to have little or no incentive to compete on prices, given the way in which this channel operates (see paragraph 6.112). To give another example, a new entrant may struggle to capture established lenders' customers on the basis of offering a better-value product, given some customers' preference to stay with a provider they feel comfortable with because of the negative reputation of the payday lending sector.

7.118 Our analysis of the conditions facing new entrants and smaller lenders indicates that the competitive constraint that might otherwise be imposed on payday lenders' prices by the prospect of new entry or expansion is likely to be further weakened by the following combination of market features.

7.119 First, new entrants will face certain disadvantages relative to more established lenders:

(a) The ability of new entrants to expand and establish themselves as an effective competitor is likely to be obstructed by the difficulties associated with raising customers' awareness of their product in the face of the barriers to shopping around and switching summarised in paragraph 6.125, the strength of the well-established brands that already exist in the market and the costs associated with advertising on a sufficient scale to be effective in overcoming these obstacles.

(b) While the ability to assess credit risk accurately is a necessary requirement for any provider of personal credit, it is likely to be a particularly important determinant of a provider's success in the payday lending sector, because of the high credit risk associated with payday loan customers. Because of their greater reliance on new customers and the role of learning in the credit risk assessment process, new entrants are likely to face some disadvantages in their ability to assess credit risk for a period, which would put them at an initial cost disadvantage relative to more established providers.

7.120 Well-resourced lenders, lenders with established positions in other credit markets or lenders with innovative customer acquisition strategies may be able to overcome these disadvantages to some degree. Access to better information from CRAs, in particular real-time data, may also be expected to facilitate entry. Nevertheless, these features are likely materially to increase the time and investment required for small lenders to establish themselves as significant players in the payday market, reducing the constraint that they would otherwise impose on established lenders.

7.121 Second, we found that the history of non-compliance and irresponsible lending by some payday lenders and the resulting negative reputation of the sector are likely to reduce the constraint imposed on payday lenders' pricing by the prospect of new entry. In particular:

(a) The reputation of payday lending is likely to deter some businesses with established reputations in other sectors – such as mainstream credit suppliers – from entering the market. This reduces the likelihood of entry by parties with the capability to transform the nature of competition in the market.

(b) Potential entrants may also be dissuaded from entering payday lending by the difficulty – itself linked to the current reputation of the sector – in

establishing banking relationships, and the very small number of suppliers currently willing to provide banking services to payday lenders.

7.122 We noted that recent regulatory developments in the sector – and in particular the price cap – are likely to reduce substantially the expected profitability of supplying payday loans, and therefore lead to a reduction in levels of new entry relative to those observed historically (indeed, a number of less efficient/ well-resourced lenders are likely to exit the market completely). These developments may also have the effect of increasing the time and resources required by new entrants and smaller lenders to overcome their initial disadvantages and establish themselves in the market, such that they might impose an effective competitive constraint on incumbent suppliers.

8. Findings

8.1 As described in paragraph 1.1, on 27 June 2013, the OFT referred the supply of payday lending in the UK to the CC for investigation, under sections 131 and 133 of the Act. Section 134(1) of the Act requires us to decide whether 'any feature, or combination of features, of each relevant market prevents, restricts or distorts competition in connection with the supply or acquisition of any goods or services in the United Kingdom or a part of the United Kingdom'. If that proves to be the case, under the Act, this constitutes an AEC.[544]

8.2 As we set out in Section 4, there is little evidence of lenders successfully using the price of their loans to attract or retain customers. In general, customers appear unresponsive where lenders have offered lower prices, and many customers take out loans with a particular provider when cheaper options may be available from other lenders to meet their borrowing requirements. This evidence indicates that price competition between payday lenders is not working effectively – an observation which is consistent with our profitability assessment, which shows that the largest lenders have earned profits significantly above the cost of capital over much of the period since 2008, although we have observed significant variation in the level of profitability, both between lenders and over time. By contrast with lenders' pricing behaviour, levels of non-price competition appear more consistent with a well-functioning market.

8.3 In Section 5, we found that competition from other forms of credit only imposed a weak constraint on payday lenders' prices. This was mainly because of the differences that exist between payday loans and other types of credit which serve to limit customers' willingness to substitute between them, and the limited extent to which many payday customers are able to use other credit products when they need to take out a loan, given their prior credit histories. We therefore excluded other forms of credit from our definition of the relevant market.

8.4 For the reasons given in Sections 6 and 7 and summarised below, we have found that there are a number of features in the provision of payday loans in the UK which contribute to, and help to explain, the failure by many payday lenders to compete on price and which either individually or in combination give rise to an AEC.

8.5 First, we have identified the following combination of structural and conduct features, which have limited the extent to which customer demand is

[544] Section 134(2) of the Act.

responsive to the price of payday loans, and so have reduced the pressure for lenders to compete to attract customers by lowering their prices:

(a) The context in which customers take out payday loans is often not conducive to customers shopping around to find a good-value loan and may amplify the adverse effects of other barriers to shopping around and switching lender. Customers often perceive the need for their loan to be urgent, and attach considerable importance to the speed with which they are able to access credit. Many payday loan customers are also uncertain, often with good reason, about whether, and from whom, they will be granted credit to meet their borrowing requirements. These aspects of the decision-making environment can tend to make customers reluctant to spend time shopping around for the best deal available, and can cause customers to focus on which lender is willing to lend to them (or, for a repeat borrower, to stay with a lender that they previously used) rather than which lender offers the best-value product.

(b) It can often be difficult for customers to identify the best-value loan product on offer given their borrowing requirements. Despite information on headline rates generally being available on lenders' websites or in the shops of high street lenders, customers' ability to use this information to identify the best-value payday loan is impeded by the complexity associated with making effective price comparisons given variation in product specifications and pricing structures across lenders, and the limited usefulness of the APR in facilitating comparisons between payday loans. Existing PCWs, which might otherwise help customers to compare loans, suffer from a number of limitations and are infrequently used.

(c) Customer demand is particularly insensitive to fees and charges incurred if a borrower does not repay their loan in full on time. Customers tend to be less aware of these potential costs of borrowing than they are of the headline interest rate when choosing a payday loan provider. This is in part because overconfidence about their ability to repay the loan on time can cause some customers to pay only limited attention to these costs when taking out their loan. Even where customers seek to anticipate the costs associated with late repayment, the information generally provided about such costs is significantly less complete, less easy to understand and/or less prominent than information on headline rates. It can therefore be difficult for customers to estimate, and so make effective comparisons about, the likely cost of borrowing if they do not repay their loan in full on time.

(d) Many online customers take out payday loans via a lead generator's website. Lead generators typically promote their ability to find customers a

lender willing to offer them a loan within a short period of time. The value for money represented by different lenders' loan offerings is not taken into account in the auction process operated by lead generators to sell leads. Lead generators instead generally sell customer applications on the most favourable commercial terms for the lead generator – often to the highest bidder. Furthermore, there is often a lack of transparency in how the service that lead generators provide is described in their websites – particularly the basis on which applications are referred on to lenders – and many customers do not understand the nature of the service offered by lead generators. An implication of the operation of this distribution channel is that lenders acquiring customers through lead generators are unlikely to have a strong incentive to lower their prices. The lead generator model may also create an incentive for lenders to increase prices to customers, as lenders offering cheaper loans would find it harder to bid high prices in lead auctions and hence acquire valuable leads.

(e) Where their choice of lender is not dictated by concerns about credit availability, customers can be dissuaded from looking at alternative suppliers by the perceived risks associated with using a new lender, particularly in light of the negative reputation of the payday lending sector. Customers may perceive a loss of convenience associated with applying to a new lender, particularly if the alternatives are rolling over or topping up an existing loan with an existing lender.

8.6 Secondly, we have found that the competitive constraint that might otherwise be imposed on payday lenders' prices by the prospect of new entry or expansion has been weakened by the following structural features:

(a) New entrants face certain disadvantages relative to more established lenders, in particular:

(i) The ability of new entrants to expand and establish themselves as an effective competitor is likely to be obstructed by the difficulties associated with raising customers' awareness of their product in the face of the barriers to shopping around and switching summarised in paragraph 8.5, the strength of the well-established brands that already exist in the market and the costs associated with advertising on a sufficient scale to be effective in overcoming these obstacles.

(ii) While the ability to assess credit risk accurately is a necessary requirement for any provider of personal credit, it is likely to be a particularly important determinant of a provider's success in the payday lending sector, because of the high credit risk associated with payday loan customers. Because of their greater reliance on new customers and the role of learning in the credit risk assessment process, new entrants are likely to face some disadvantages in their ability to assess credit risk for a period, which would put them at an initial cost disadvantage relative to more established providers.

(b) The history of non-compliance and irresponsible lending by some payday lenders and the resulting negative reputation of the sector are likely to reduce the constraint imposed on payday lenders' pricing by the prospect of new entry. In particular, the reputation of payday lending is likely to deter some businesses with established reputations in other sectors – such as mainstream credit suppliers – from entering the market. This reduces the likelihood of entry by parties with the capability to transform the nature of competition in the market. Potential entrants may also be dissuaded from entering payday lending by the difficulty – itself linked to the current reputation of the sector – in establishing banking relationships, and the very small number of suppliers currently willing to provide banking services to payday lenders.

8.7 Although recent developments in the regulation of the payday lending market are likely to lead to changes in lenders' risk thresholds, market structure and the types of products on offer, we do not expect that these changes would effectively address the underlying market features that we have identified as having impeded competition between lenders for the reasons set out in Sections 6 (paragraphs 6.122 to 6.125) and 7 (see paragraphs 7.109 to 7.115).

8.8 We have therefore found, pursuant to section 134(1) of the Act, that there are features of relevant markets, which alone or in combination prevent, restrict or distort competition in the supply of payday loans to UK customers, and accordingly that there is an AEC within the meaning of section 134(2) of the Act. The features are those that we have identified in Sections 6 and 7 of this report and which are summarised in paragraphs 8.5 and 8.6 above.

Customer detriment

8.9 We considered the nature and potential scale of the harm to payday loan customers arising from the AEC that we have found.

8.10 Looking at the period to the end of 2014, the AEC is likely to have led to customers paying higher prices for payday loans – and to have resulted in reduced innovation in pricing structure among payday lenders – than we would have expected to observe in a well-functioning market. Lower-risk customers, borrowers repaying their loan late, borrowers paying upfront fees and borrowers using 'traditional' 30-day payday lending products to borrow for relatively short periods are likely to have overpaid by a particularly significant amount.

8.11 Our assessment of the scale of the overpayment is set out in Appendix 8.1. This indicated that the scale of the overpayment – and so the customer detriment caused by the AEC – is likely to have been material. On the basis of different plausible assumptions about the level of prices that might be observed in a market in which price competition were more effective, we estimated that, in our base case competitive benchmark, the lack of effective price competition has meant that, on average, borrowers have overpaid for their loans by an amount in the order of magnitude of around £5 to £10 per £100 per month. The extent of overcharging could be up to £14 per loan relative to a 'lower' benchmark scenario that reflected the lowest prices on offer in the market.[545] For context, a typical payday loan has a value of £260 and is taken out for just over three weeks, and with a TCC for a customer who repays in full and on time of around £75. Applying these amounts to the total number of loans issued in 2012 that were repaid in full would imply, in the base scenario, a total potential overpayment of around £48–£85 million in that year. The total potential overpayment could be as high as £74–£127 million if the competitive benchmark were closer to the 'lower' scenario.

8.12 By forcing down the prices of payday loans (these include interest and fees charged during the agreed loan duration, interest and charges in case of default and the total cost of the loan), the price cap will mitigate some of the harm to customers that has arisen from high prices. Nevertheless, we considered that even in the presence of the price cap, significant scope for price competition between payday lenders to further improve customer outcomes would be achievable in the absence of the market features that we have identified. This implies that a material customer detriment would arise from the AEC if it were left unaddressed, and the gains of effective competition were foregone. In particular:

(a) First, even in the short term, some lenders' costs are likely to allow them to price beneath the cap for their products, and as such there is likely to be some scope for these lenders to undercut their rivals in the event that competition became more effective. We note that some lenders have charged headline prices and/or additional charges around or beneath the cap level, and that there is considerable variation in the efficiency of different lenders.[546,547] This suggests that business models exist that

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[545] See Appendix 8.1, paragraph 19.
[546] See paragraph 7.98, and the discussion about how the ability of assessing credit risk varies across lenders in Section 7.
[547] These differences in the efficiency may also increase as a result of the different way suppliers will adapt to the new regulatory regime.

allow lenders to operate viably with prices within the framework provided by the cap. In this context, we also note that the FCA considered that there would still be a viable market for those lenders which decide not to exit.

(b) Second, more effective competition is likely to increase the pressure on lenders to compete for lower-cost customer groups, and such customers might be offered prices significantly beneath the price cap. Such competition currently takes place to only a very limited extent.[548] Examples of customers who might benefit from an increase in this type of targeted price competition include customers with relatively good credit backgrounds or repeat customers with a proven repayment history.

(c) Third, in the longer term we would expect to observe a downwards trend in many categories of lenders' costs. This might happen, for example, as to lenders adapt their products the cap regime; as lenders continue to adjust their business models in response to the FCA changes to CPAs and rollovers;[549] if costs of acquiring customers (eg through lead generators) fall;[550] as external CRA data improves;[551] and as a result of improvements in lenders' ability to assess risk.[552] Without effective price competition, there will be no pressure for lenders to pass any cost reductions of this type on to customers.

8.13 Put another way, in the absence of effective price competition, there will be no incentive for lenders to reflect their costs in the prices charged to customers in the future, irrespective of technological developments, evolution in the products on offer, or changes in market structure. For this reason, we concluded that the scale of the customer detriment caused by the AEC was likely to continue to be material, notwithstanding the reduction in prices brought around by the cap.

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[548] We considered that the current use of risk-based pricing and flexible pricing models was undeveloped relative to the level that we might expect to see in a well-functioning market.

[549] For example, Cash America International, Inc. said that:

> [Turning to the UK] As many of you are aware, our regulator there, the Financial Conduct Authority or FCA, published a rulebook this past winter. As Dan discussed in the call last quarter, many of those rules became effective April 1. One of the main rules that became effective July 1 is a limit on our use of continuous payment authority to debit customers' accounts. Under the new rule, we are only allowed 2 attempts when a debit fails due to lack of funds. We've been testing this change for the last several months and fully implemented it prior to the July 1 deadline. This change will likely result in slightly higher default rates in the UK, but we believe we can offset much of that impact through additional collection efforts. The other significant rules become effective July 1 was a limit on the number of times we can expand a loan to 2. We made this change over a year ago and found very little impact due to a combination of effective underwriting and not being as aggressive with the number of extensions we made prior to the change.

(see Cash America International's CEO David Fisher on Q2 2014 Results - Earnings Call transcript).

[550] See paragraph 7.113.

[551] Paragraph 9.279.

[552] Paragraphs 7.84 & 7.85.

9. Remedies

9.1 In this section we set out the framework for the assessment of the measures needed to remedy, mitigate or prevent the AEC and/or the resulting customer detriment we have found. We also set out our consideration and conclusion of the design, effectiveness and proportionality of our remedies package, taking into consideration recent FCA regulation, relevant customer benefits (RCBs) and the need for remedial action.

9.2 This section sets out:

(a) A summary of the remedies process and package (paragraphs 9.3 to 9.7). In this subsection we briefly outline the stages in the development of our remedies package and how each measure addresses the AEC.

(b) The framework for remedies (paragraphs 9.8 and 9.9). In this subsection we outline the relevant aspects of the statutory framework and our guidance.

(c) We then discuss the design and implementation of each remedy:

(i) Price comparison website (PCW) (paragraphs 9.10 to 9.212).

(ii) Improving the disclosure of late fees and other additional charges (paragraphs 9.213 to 9.234).

(iii) Measures to help borrowers shop around without unduly affecting their access to credit (paragraphs 9.235 to 9.270).

(iv) Measures to encourage development of real-time data sharing (RTDS) (paragraphs 9.271 to 9.291).

(v) A summary of the cost of borrowing (paragraphs 9.292 to 9.355).

(vi) Increased transparency regarding the role of lead generators (paragraphs 9.356 to 9.390).

(d) In paragraphs 9.391 to 9.410 we discuss remedies that we identified in our Remedies Notice and those suggested by third parties but that we have decided not to adopt.

(e) We then set out our assessment of:

(i) Relevant customer benefits (paragraphs 9.411 to 9.414).

(ii) The need for remedial action (paragraphs 9.415 to 9.436). In this subsection we set out our assessment of the need for remedial action with specific reference to FCA regulatory intervention.

(iii) Effectiveness of our package of remedies (paragraphs 9.437 to 9.478). In this subsection we discuss how the package will remedy the AEC, the timescale over which the remedies will be implemented and the coherence of the remedies.

(iv) Proportionality of our package of remedies (paragraphs 9.479 to 9.540). In this subsection we discuss our consideration on the proportionality of remedies and of ensuring they are effective, no more onerous than necessary and do not produce adverse effects.

(f) Decision on remedies (paragraphs 9.541 to 9.542). We formally state our decision on remedies.

Summary of the remedies process and package

9.3 Our remedies package has been designed to remedy the AEC we set out in Section 8. In this section we briefly outline how our package of remedies has evolved in response to our findings and submissions made by parties.

9.4 We published a Remedies Notice with our provisional findings on 11 June 2014 and outlined a number of possible remedies which we considered might remedy the AEC which we had provisionally found. After considering responses to the Remedies Notice we published our provisional decision on remedies (PDR) on 9 October 2014. We received additional comments from the FCA (see Appendix 9.1) and published a further consultation document on 19 December 2014. We considered carefully the responses to each consultation. In this section of the report we set out the remedies we have decided to implement to remedy the AEC and our considerations on the design, implementation, effectiveness and proportionality of the remedies.

9.5 In summary, the remedies package (which, with the exception of the PCW remedy, will apply to both online and high street lenders) will remedy the AEC that we have found (see Section 8 paragraphs 8.1 to 8.8) as shown below:

(a) Measures to promote shopping around through the use of PCWs with greater functionality, in particular a requirement for online lenders to publish details of their loans on an FCA-authorised payday loan PCW combined with a recommendation to the FCA to raise the standards which apply to payday loan PCWs. We have identified a number of aspects of our AEC which this remedy will address:

(i) We consider that encouraging the development of PCWs with greater functionality will allow customers to easily and quickly compare multiple loan products to establish the best-value loan product for their needs. Customers find this difficult to do at present and in any event often do not perceive there to be significant differences between loans. This remedy also helps address the context in which borrowers take out loans, where customers often perceive a sense of urgency.

(ii) Clear presentation of fees and charges on a competitively neutral basis will make it easier for customers to identify loan costs, including those arising from late fees and charges.

(iii) By presenting loan products in ascending order of price, new lenders can seek to enter the market and gain share by competing on price and improving brand awareness through being present on a PCW.

(iv) Our requirement for lenders to provide a hyperlink on their websites and on summaries of the cost of borrowing will increase customers' awareness of the availability of PCWs and reinforce the effectiveness of the remedy.

(b) A recommendation to the FCA to take steps to improve the disclosure of late fees and other additional charges. We found that customer demand is insensitive to fees and charges incurred as a result of late payment. This remedy is necessary because of our finding that information generally provided about such costs is significantly less complete, less easy to understand and/or less prominent than information on headline rates.

(c) A recommendation to the FCA to work with lenders and other market participants to help customers shop around without unduly affecting their ability to access credit and to further consider issues relating to the use of quotation searches and other developments. This measure seeks to address barriers to shopping around and obtaining the best-value loan for a customer for the following reasons:

(i) We have identified that customers do not know if they are likely to be accepted by a given lender for a loan and the only way to establish if they will be offered a loan is by formally applying for the loan.

(ii) We have found that multiple credit searches (which are performed by a lender when assessing an application) are often interpreted by lenders as an indication of credit risk.

(iii) Therefore in developing measures to encourage shopping around we have identified the risk that customers may thereby impact their ability to access credit.

(d) A recommendation to the FCA to take further steps to promote RTDS between lenders:

(i) We consider that further encouraging the adoption of RTDS will benefit both customers and new entrants. By increasing the frequency that Credit Reference Agencies (CRAs) update their databases, lenders will be able to make a decision based on up to date information about the potential credit risk that a given borrower presents and thereby the likelihood that a borrower is prevented from accessing credit as a result of shopping around is reduced.

(e) A requirement for all lenders to provide existing customers with a summary of the cost of borrowing:

(i) By presenting borrowers with a summary of the cost of their borrowing and identifying the impact of late payment, this remedy seeks to encourage customers to actively shop around and to address customers' over-confidence in their ability to repay a loan and their insensitivity to fees and charges for late payment.

(ii) By providing details of one or more PCWs this will encourage shopping around and increase customers' understanding of the costs of their loans.

(f) A recommendation to the FCA to take steps to increase transparency regarding the role of lead generators:

(i) By requiring lead generators to provide clear and prominent information on the nature of their service and details of the commercial basis on which they sell customer details, this remedy seeks to ensure customers are informed about the basis of how they may be offered a loan.

(ii) By remedying the erroneous expectation that lead generators will match them with the best loan for their requirements we would expect some customers to engage in more shopping around, for example, by using an authorised payday loan PCW.

9.6 This package of remedies will operate, in conjunction with FCA initiatives that address irresponsible lending and non-compliance with consumer credit regulation, to address the AEC that we have found and to improve the perception and reputation of the payday loan market so as to encourage further entry into this market and reduce reputational barriers to entry to this market.

9.7 In designing our remedies package we have had regard to any constraints imposed by the Consumer Credit Directive (CCD), the principal source of regulation on consumer credit. The CCD contains provisions specifying the standard information to be included in advertisements[553] and the requirements relating to the provision of pre-contractual information to enable borrowers to compare different offers and take an informed decision before being bound by any credit agreement[554,555] and to provide borrowers with adequate explanations to enable them to assess whether a product is suited to them and their financial situation.[556] We discuss regulation in detail in Section 3. In particular, we consider that our remedy package has been structured in a way that would allow the FCA to take action in a manner consistent with the CCD.

Framework for consideration of remedies

9.8 Where the CMA finds that there is an AEC, it is required under the Act[557] to decide whether action should be taken by it, or whether it should recommend the taking of action by others, for the purpose of remedying, mitigating or preventing the AEC, or any detrimental effect on customers (the customer detriment) so far as it has resulted from, or may be expected to result from the AEC.

9.9 If the CMA decides that action should be taken, it must then decide what action should be taken and what is to be remedied, mitigated or prevented. In deciding these questions, the Act requires the CMA in particular to 'have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the adverse effect on competition and any detrimental effects on customers so far as resulting from the adverse effect on competition'.[558] To satisfy this requirement, the CMA considers how comprehensively potential remedies (or packages of remedies) address the AEC and resulting detrimental effects on customers, as well as whether the potential remedies are effective and proportionate.[559]

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[553] Article 4.
[554] Article 5.
[555] This information must be presented using the Standard European Consumer Credit Information form and include the 'interest rate applicable in the case of late payments and the arrangements for its adjustment, and, where applicable, any charges payable for default' as well as a warning regarding the consequences of missing payments'. See CCD, Article 5(1) (l and m).
[556] Article 5(6).
[557] Section 134(4) of the Act.
[558] Section 134(6) of the Act.
[559] The Guidelines, Part 4.

Price comparison website

Introduction

9.10 In this section we discuss the PCW remedy. We first summarise the remedy and discuss how the remedy addresses the AEC and customer detriment. This section then considers remedy design considerations (paragraphs 9.23 to 9.185) before considering issues around the implementation of the remedy (paragraphs 9.186 to 9.198). We then set out our conclusions in paragraphs 9.199 to 9.212.

Summary of remedy

9.11 Figure 9.1 summarises our remedy to prohibit lenders from providing payday loans unless details of their prices and products are published on at least one authorised payday loan PCW. This remedy has been designed to take account of the FCA's preference to implement the remedy through its existing regulatory framework.

FIGURE 9.1

Price comparison website remedy

The CMA will issue an Order to the effect that:

- Online lenders will be prohibited from supplying payday loans to customers in the UK unless up to date details of their payday loan products are continuously published on at least one payday loan PCW which is operated by an FCA-authorised person following the FCA's implementation of additional standards. Where an online lender can demonstrate that it has been unreasonably excluded from all authorised payday loan PCWs, this prohibition will not apply.

- Online lenders must publish details of their products on an authorised payday loan PCW within 12 months of the FCA publishing its final decision on the standards it will introduce (the 'decision date') or, if later, the date the FCA's new standards become effective. Where at the end of this period, a lender is engaged in negotiations with a payday loan PCW, the lender may apply for a 3 month extension to complete those negotiations.

- Where no authorised payday loan PCW exists at the later of 12 months of the FCA publishing its final decision on the standards it will introduce or the date the FCA's new standards become effective, but online lenders consider that there is a reasonable prospect that a payday loan PCW is about to become operational, online lenders can seek an extension from the CMA of up to 3 months to appear on that PCW.

- If there is no reasonable prospect of an authorised payday loan PCW becoming operational within 3 months online lenders will have to submit an application to the FCA for authorisation of a payday loan PCW within 6 months. Where an online lender has not submitted an application for authorisation, either jointly or individually, but where good progress in preparing an application can be demonstrated and no other authorised payday loan PCW has been created, then an extension of up to 6 months to submit an application for authorisation may be granted by the CMA.
- Online lenders will be required to supply their selected FCA-authorised payday loan PCW(s) with relevant information on each of their payday loan products.
- Online lenders will be required to display a hyperlink prominently on their own websites to at least one FCA-authorised payday loan PCW on which its own loans appear and/or to a web portal containing hyperlinks to all FCA-authorised payday loan PCWs in the event that such a web portal has been created.
- Online lenders will notify the CMA of the authorised payday loan PCWs on which they have published details of their payday loan products and the payday loan PCW or portal to which they have hyperlinked. Where lenders consider themselves to be unreasonably excluded from all authorised payday loan PCWs, lenders will notify the CMA of those PCWs annually and the steps taken each year to publish details of their products on those and any payday loan PCWs which subsequently enter the market.

In support of this Order, the CMA:

- Considers that creation of a web portal containing hyperlinks to all FCA-authorised payday loan PCWs would enhance the effectiveness of this remedy by helping customers to find an authorised payday loan PCW. We therefore recommend that the FCA, working with relevant partners as appropriate, consider how best such a web portal could be implemented and which body would be most appropriate to host the portal.
- Recommends that the FCA consider how to ensure that authorised payday loan PCWs do not unreasonably exclude any FCA-authorised payday loan providers or their payday loan products.

To address identified shortcomings of existing payday loan PCWs, the CMA further recommends that the FCA reviews its requirements for payday loan PCWs and uses its regulatory tools to raise the standards which apply to payday loan PCWs. Given the evidence the CMA has collected, and the AEC it has found, the CMA recommends that, in taking forward this recommendation, the FCA seeks to achieve the following outcomes for consumers (under each outcome we have provided some specific examples). However, it would be for the FCA to determine the standards it requires for payday loan PCWs.

Competitive neutrality

We recommend that the FCA seeks to ensure that authorised payday loan PCWs enable customers to view loans ranked on the basis of objective criteria and that the default ranking should be the price of the loan. To this end, we recommend that the FCA considers how to ensure that authorised payday loan PCWs:

- Present loan product information/results of the customer's searches in ascending order of price unless the borrower requests a different presentation. On the basis of the evidence we have collected, we recommend ranking by the total amount payable.
- Present loan product information to customers on a competitively neutral basis, such that the presentation of product information, or its ranking on price comparison tables, is not affected by any commercial relationship the operator may have with lenders included on the PCW's panel. Similarly, we recommend that, in the event of different products having the same price, any secondary ranking should be on the basis of objective factors that are of benefit to customers and not be linked to the commercial interests of the PCW or of any lender.
- Clearly differentiate any advertising on their website from the ranking of loan products so that customers are not drawn away from the objective ranking of products by banner advertisements.

Customer relevance

We recommend that the FCA seeks to ensure that authorised payday loan PCWs enable customers to identify the loans that best meet their search criteria. To this end, we recommend that authorised payday loan PCWs:

- Provide a search function and return results that reflect the key features of the loan the customer is seeking. We consider that such functionality could include, for example, the ability to specify a desired loan amount, term (or repayment date) and repayment structure (eg the number of instalments).
- Are as transparent as possible about all features of the loan, including the consequences of late or non-payment. We consider that customers would

particularly benefit if they were presented with information about late fees and charges as well as the effect of early repayment on the price of the loan.

Scope

We recommend that the FCA seeks to ensure that authorised payday loan PCWs include only loan products in their loan comparison tables and do not include brokers or other intermediaries in their loan comparison tables.

Compliance

- The effectiveness of this remedy will be enhanced if customers have confidence that they are transacting with a reputable provider and to this end we recommend that the FCA considers how to ensure that authorised payday loan PCWs comply with all relevant laws and regulations.

How the remedy addresses the AEC and/or resulting customer detriment

9.12 This remedy will address a number of aspects of the AEC that we have found by:

(a) reducing the difficulties customers face in identifying the best-value or most suitable offer for them (see paragraphs 9.14 to 9.19);

(b) increasing customer awareness of late fees and other additional charges incurred if a customer does not repay a loan in full and on time and enabling customers to factor this into their choice of lender (see paragraph 9.20);

(c) reducing barriers to entry and expansion associated with difficulties in raising customer awareness of different suppliers' offers (see paragraph 9.21); and

(d) lowering reputational barriers to entry by providing greater credibility to the payday lending price comparison sector and encouraging the participation of mainstream general PCW operators (see paragraph 9.22).

9.13 We discuss each of these mechanisms below.

Reducing the difficulties that customers face in identifying the best-value offer

9.14 By taking steps to facilitate the development of an effective price comparison sector, this remedy will enable payday loan customers to establish the cost of a loan specific to their needs (that is for a given amount and duration) and compare loans and shop around more easily and quickly without having to research numerous lenders. The speed with which comparisons can be made using a PCW is a particularly important consideration in this market, given the perceived urgency for many customers associated with taking out a payday loan (see paragraphs 6.51 to 6.56 and paragraph 8.5*(a)*).

9.15 At present, to achieve a similar outcome, borrowers would need to visit a number of lenders' websites, entering their requirement into each lender's website and make a comparison manually between the products on offer. While there are some PCWs that provide details of payday loans, their functionality is currently limited and the comparison tables presented for an example loan (eg £100 for 28/30/31 days) may not offer an accurate indication of the actual cost of the loan that a customer is looking for. The result is that it is difficult for borrowers to make accurate comparisons between loans (see paragraph 6.89).

9.16 The customer research we undertook as part of our remedies process also indicated that some customers' tendency not to shop around may arise because they do not perceive there to be significant differences between loans.[560] This combines with the sense of urgency and thus the speed at which borrowers choose their loan to deter shopping around.[561] By presenting the cost of a range of loans in ascending order of price – and possibly by other aspects of the loan as determined by the customer – customers will more readily be able to identify quickly and conveniently the difference in price (and non-price attributes) between loans.

9.17 While some customers may still place weight on recognised brands,[562] it will be the underlying characteristics of a loan product that will determine its position on the payday loan PCW.

9.18 As they have done in other sectors, PCW operators are likely to have incentives to develop mechanisms to help borrowers identify lenders who are willing to offer them credit (see paragraphs 9.257 to 9.262). To the extent that this type of capability is built into PCWs in the future, borrowers who have been rejected by some lenders (or are otherwise aware of their own poor

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[560] Our qualitative research found that there was very little evidence of shopping around, and where it did occur it was fairly cursory. This was driven by a desire to access the money quickly, and a perception that all loans cost around the same amount, leading customers to conclude that the benefits of shopping around would be limited, as well as adding extra time to the 'journey'. TNS BMRB research with payday lending customers, p12. Furthermore when customers were presented with a PCW some noted surprise at the number of lenders available and variation in price (p17).
[561] Our quantitative research found that a lack of time was the most common explanation given by respondents for not shopping around for their most recent loan. A lack of time was also cited by customers – who reported to have shopped around – as the most common barrier to not comparing a larger number of lenders or spending more time comparing offers (paragraph 6.55).
[562] TNS BMRB research with payday lending customers, p14.

credit history) will be in a better position to identify and make comparisons between those lenders that would be prepared to lend to them.

9.19 We noted that a PCW would not directly help borrowers without internet access (either at home or on a mobile phone or other portable device) to shop around. Even the minority of customers without internet access[563] would be likely to accrue some indirect benefit from this remedy as a result of a tightening of the constraint that online lenders place on high street lenders' prices (see paragraphs 5.53 to 5.68 and paragraphs 9.93 and 9.105).

Awareness of and sensitivity to late fees and other extra charges

9.20 A PCW helps borrowers to compare the price and other attributes of loans offered by a panel of lenders. In addition to information presented in comparison tables, mainstream PCWs in other markets typically allow a consumer to review additional details for that product. In the case of payday loans, the structure of late fees and other extra charges could be presented in such a way. If payday loan PCWs present late fees in future, borrowers using those websites would be made aware of any differences in fees between lenders even where the 'upfront' price appears similar. The overall impact will be that borrowers will be more aware of the potential cost of late payments and hence more likely to factor it into their decisions. Similarly, payday loan PCWs may choose to allow borrowers to use a representative scenario of late fees and other extra charges as a secondary sort criteria.

Barriers to entry and expansion: raising customers' awareness of new and alternative suppliers' offers

9.21 If a greater proportion of payday loan customers use PCWs, new entrants and smaller lenders would be able to raise awareness of their brands and product characteristics more effectively (and potentially more cheaply) through a payday loan PCW than through alternative channels, such as lead generators, pay-per-click adverts and advertising through traditional media.[564]

Barriers to entry and expansion: reducing reputational barriers to entry

9.22 We considered the reputational barriers to entry that exist in the market. We considered that introducing specific minimum standards for payday loan PCWs would complement the emerging regulatory and enforcement regime of

[563] Only 18% of respondents to our survey who said that they would not consider taking out a loan online gave a lack of internet access as a reason (the most common reason, given by 35% of respondents, was that they preferred speaking to someone face-to-face). TNS BMRB Quantitative research, Survey Tables, Table 315.
[564] See paragraph 7.76.

the FCA in improving the perceived reputation of the market. This would help address some of the concerns that non-payday lenders (such as mainstream credit suppliers) and other established businesses (such as PCW operators) raised as factors that have inhibited entry so far. In addition to the points identified in paragraph 9.21, a payday loan PCW operating under set standards would allow lenders to attract new borrowers without having to rely on advertising, direct marketing or the use of lead generators, which have been a significant source of new loans for existing lenders but which have also been the subject of a number of concerns from consumer groups.[565]

Remedy design

9.23 In this section we consider the design issues around creating one or more payday loan PCWs with the functionality that will facilitate effective shopping around for payday loans. After we have determined the key aspects of remedy design we go on to consider implementation issues with the remedy.

9.24 We were mindful that there are currently a number of PCWs providing payday loan comparison services to customers. However, the functionality of these websites at present is not sufficient to enable customers to compare adequately the price of a given loan[566] from a panel of lenders. We are also aware that there are a number of large, well-resourced PCWs operating successfully in other consumer credit markets (and other financial services markets). A number of parties identified that an established PCW operator would have pre-existing technology for operating a comparison platform that would be able to incorporate payday loans. An established PCW operator would be able to leverage existing customer awareness of its brand and would reduce the initial marketing costs required to promote the site.

9.25 We consider the following aspects of design:

(a) We first consider, in paragraphs 9.26 to 9.37, whether to seek to have a single 'official' payday loan PCW or instead to have a commercial solution with multiple PCWs complying with minimum standards. We conclude that the commercial solution would be preferable.

(b) We then consider how the minimum standards required for the commercial solution to operate should be set and monitored in paragraphs 9.38 to 9.55. In our PDR we proposed that the FCA should operate an accreditation scheme for payday loan PCWs. Following submissions from the

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[565] See FCA response hearing summary, paragraph 33, and the FOS website; 'Ombudsman warns consumers about payday loan middlemen', 19 August 2014.
[566] In the first instance for a loan of a given amount and duration.

FCA and other parties we decided to change the remedy so that the FCA will introduce enhanced standards for authorised payday loan PCWs.

(c) An important aspect of the design of the payday loan PCW is how it will generate funding to cover its costs. We discuss how the PCW should be funded in paragraphs 9.56 to 9.67.

(d) We discuss whether PCWs are likely to wish to be authorised to compare payday loans in paragraphs 9.68 to 9.105. We discuss comments received from parties, including PCWs, about their possible interest. We also consider the impact that Google consumer advisories concerning payday loans may have on the interest of PCWs offering payday loan comparisons. Finally we consider whether payday loan PCWs should be required to list loans from high street providers. We decide that, because of the way the PCW funding model operates, these loans would not have to be listed.

(e) We then discuss the completeness of the panel of lenders on a payday loan PCW, including the obligation to provide a link to a payday loan PCW from their own website (paragraphs 9.106 to 9.128).

(f) Next, in paragraphs 9.129 to 9.162 we consider what the functionality of a payday loan PCW should be, striking a balance between specifying adequate criteria and not creating an over-rigid set of criteria.

(g) Finally, in paragraphs 9.163 to 9.185 we consider a number of issues raised by parties including the treatment of advertising on the payday loan PCW and the situation where a lender has been excluded from being listed on a payday loan PCW.

Single official website or a commercial solution

9.26 We considered remedy options that involved the creation or accreditation of a single ‘official’ PCW. This would have the potential benefit of providing and acting as a single point of reference to which other aspects of our remedy package could link. Over time the ‘official’ website might become an established brand with which borrowers could become familiar.[567] However, this approach would allow limited scope for competition between PCWs in delivering the benefits of this remedy. Depending on its design, this option might risk putting the preferred operator in a very strong negotiating position

[567] However, first-time borrowers may lack awareness of, or familiarity with, the name of the site if it only provided comparisons for payday loans, which may in turn affect the likelihood of them visiting the site prior to visiting a lender.

relative to payday lenders, leading potentially to a need for further regulatory intervention in the future.

9.27 An ‘official’ PCW or accredited site could be established in a number of ways and with different commissioning and governance arrangements. These might include:

(a) creating a new stand-alone site without any involvement from existing PCW operators, developing the site without drawing on any existing PCW infrastructure;

(b) appointing a single existing PCW operator (or other party) to establish a website under new branding; or

(c) appointing a single existing PCW operator or other party to establish a website under their own brand.[568]

9.28 The accreditation (or ‘franchise’) period would last for a given period, with tender processes held periodically.

9.29 We noted that a variant on this approach would be for lenders to be required to provide data to a single third party to aggregate and then supply the data to several PCWs. At present some PCWs operate under a similar model, rebadging a third party supplier’s comparison engine.[569] We noted that there might be scale benefits from a single site collating price and other information. However, if PCWs were dependent on a single party for aggregation services, there may be a lack of incentives for any PCW to innovate. We also considered that requiring lenders to deal with a single aggregator could provide the aggregator with excessive negotiating power. We therefore did not pursue this option further.[570]

9.30 Money Advice Trust (MAT) told us that a single PCW should be operated by an entity independent of payday lenders, such as the Money Advice Service (MAS). MAT considered that such a site would be able to demonstrate it did not receive commission or incentives for recommending certain products.[571] We considered MAT’s points, but we were unable to identify an appropriate

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[568] We also considered the possibility that a site could be hosted by a public sector or third sector organisation but we considered it unlikely that we would identify an appropriate body with both sufficient expertise and inclination to take on this role.
[569] Runpath is an example of a company that provides comparison engines and underlying data to a number of well-known PCWs.
[570] However, if a PCW had arrangements to use a third party’s price comparison services we do not consider that it should be excluded from receiving accreditation because it used a third party partner, as is the case for some other accreditation schemes.
[571] MAT response to the PDR, p2.

body which we thought would be willing and able to operate, promote and fund an effective payday loan PCW.

9.31 An alternative approach would be to establish a set of minimum standards that commercial payday loan PCWs could operate under. This would generate competition between payday loan PCWs which we would expect to bring further benefits to customers, through innovation and promoting choice.

9.32 We considered that having multiple commercial payday loan PCWs adhering to a minimum set of standards would have the lowest risk of distorting the payday loan PCW sector as the remedy would avoid having a single PCW that would have undue bargaining power.[572] However, for a PCW to be effective customers need to be aware of it and/or be able to find it easily. While there would be a lower risk of distortion, the potential benefit of a single ‘official’ PCW having greater prominence (and thus customer awareness) would be lost. Conversely, allowing multiple sites with some form of approved status[573] could increase customers’ awareness of payday loan PCWs in general, particularly if accredited operators were proactive in advertising their websites.

9.33 We were concerned that if a single ‘official’ PCW was created there was a risk that it would have little incentive to invest in innovation.[574] This could be mitigated by frequent, regular retendering or competition to operate the official PCW although this would increase the implementation costs associated with this remedy.

9.34 We then considered the bargaining positions of lenders and payday loan PCWs and how this might be affected by the number of payday loan PCWs with some form of approved status. In a negotiation on fees between payday loan PCWs and lenders a single official payday loan PCW could have a high degree of bargaining power if lenders’ products were required to appear on that PCW and the price paid for referrals could be high. If there were multiple payday loan PCWs, lenders would retain the option of taking business away from any given site. Under this model, even if there was only one site, at a particular point in time that site would be subject to the threat of potential competition from other operators deciding to enter the market to compare payday loans, which would act as a constraint.

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[572] Even if there was only one accredited or authorised payday loan PCW, there would be the potential threat of another payday loan PCW seeking accreditation/authorisation as a new entrant.
[573] Which could be through an accreditation scheme or other mechanism, such as FCA authorisation.
[574] We also note, however, that too-frequent tendering may also reduce the incentives for an operator to invest in new functions in addition to the agreed provision because of the risk that the cost of developing the function might not be recouped over the ‘franchise’ period.

9.35 If there were multiple PCWs that compared payday loans, we considered whether lenders should be obliged to publish details of their products on one of these sites or on all such sites. If lenders were required to agree commercial terms for their products to appear on all the payday loan PCWs, we were concerned that this could undermine lenders' ability to negotiate with PCWs and could have the same effect as if there were a single official site.

9.36 We considered that there would be strong incentives for lenders to be on multiple payday loan PCWs (and potentially low incremental costs of being on more than one payday loan PCW). In particular, given the current propensity of payday loan customers to spend relatively little time searching for a loan, customers may tend to visit only one comparison site ('single-homing').[575] To the extent that a number of comparison websites generate significant volumes of traffic and each has a significant number of single-homing customers who can only be accessed through that specific site, we would expect lenders to have incentives to be on multiple sites. We also expect that as payday loan customers become more aware of the ease and opportunities for using PCWs to compare payday loans and the benefits to them of shopping around they will visit multiple payday loan PCWs. Therefore payday loan PCWs are likely to attempt to develop a substantial panel of lenders, to give them a competitive advantage.

9.37 We concluded that a commercial solution, under which payday loan PCW operators comply with a set of minimum standards, was the most appropriate remedy. We expect that multiple payday loan PCWs would compete against each other and that this would encourage innovation. However, to ensure that the current shortcomings of existing PCWs are not repeated, an appropriate body would need to design suitable minimum standards and evaluate payday loan PCWs against the standards.

How the minimum standards should be set and monitored

9.38 Having decided to adopt a commercial solution, under which PCW operators comply with a set of minimum standards, we now discuss the mechanism for establishing and monitoring the minimum standards. We would expect a scheme run by an expert sectoral regulator, with a focus on enhancing competition, to be particularly likely to have a positive impact on the quality of PCWs operating in that sector. The FCA has responsibility for regulating consumer credit, including payday lending, and also has competition powers and duties. We decided that it would be most appropriate for the FCA to oversee the detailed specification, implementation and monitoring of minimum

[575] Single-homing is discussed further in paragraph 9.178

standards for payday loan PCWs. This will complement and enhance the FCA's existing regulatory framework and oversight of lenders and credit brokers. The FCA has the necessary expertise, focus on consumer outcomes and resources to perform this important role to a high standard. Furthermore, the FCA's ongoing regulation of the sector means that it would be best placed to ensure that the standards are able to adapt and evolve with the industry and potentially to incorporate other types of consumer credit.

9.39 We are aware of PCW accreditation schemes in the energy and telecoms markets being administered by sectoral regulators, and we spoke to Ofcom and Ofgem to understand the operation of their schemes.

9.40 We noted the research conducted by Consumer Futures[576] which included some comparisons of 'accredited' and non-accredited websites. This research suggested that accreditation, by itself, was not necessarily a guarantee of a PCW being better than a non-accredited PCW. However, we noted that the research covered a wide range of accreditation schemes – some were operated by trade or consumer bodies and others by a sectoral regulator; some did not validate data or set standards for the PCW to comply with.

9.41 Given this, we took the view that the details of the minimum set of standards to which payday loan PCWs would have to adhere and the capability of the body operating the scheme were important aspects of the effectiveness of the scheme. We considered that the standards would need to be clearly defined to ensure quality.

9.42 In our PDR, we noted the existence of the Ofgem and Ofcom accreditation schemes, and we proposed that a voluntary accreditation scheme overseen by the FCA should be used to set and monitor the standards that PCWs would have to comply with. This would enable borrowers to identify the PCWs which have achieved the standards. We considered that enabling the accreditation of multiple PCWs would have the benefit of allowing any interested party to develop a PCW and seek accreditation for it, encouraging a market to develop for price comparison services for payday loans.

9.43 In response to the PDR, the FCA told us that operators of PCWs were already likely to require its permission to act as credit brokers.[577] The FCA said that all authorised payday loan PCWs would be held to certain standards, but that

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[576] eDigitalResearch, Comparing comparison sites – Price comparison website mystery shopping report for Consumer Focus.

[577] Many PCWs already have interim authorisation. Many credit brokers have applied for or received authorisation as credit brokers and are bound by the FCA's existing authorisation standards. The FCA has told us that there are some 40,000 credit brokers that would be able to operate a PCW without further authorisation.

under our remedy (as set out in our PDR) those seeking accreditation would have to adhere to different standards. As a result, the FCA was concerned that a two-tiered regulatory system would exist and requested that we consider amending our recommendation so that the FCA used the tools at its disposal to raise the standards of all PCWs.[578]

9.44 In our view the same outcomes could be achieved[579] under both the remedy as drafted in the PDR and as proposed by the FCA. Given that credit broking is a regulated activity,[580] where a PCW effects an introduction between a borrower and a lender, we considered it highly probable that a PCW would need appropriate permissions from the FCA. We were conscious however that by implementing the remedy through the FCA's existing framework the scheme would not be voluntary but would instead be a mandatory set of standards for any PCW providing comparisons of payday loans. This would be different to the proposed accreditation scheme. We therefore consulted interested parties on implementing the remedy by the FCA using its existing framework to authorise PCWs and we received further responses from parties addressing this option.[581]

9.45 Several respondents supported the implementation of the remedy through the existing legal framework.[582] Christians Against Poverty said that use of the FCA framework gave credibility to the remedy and the FCA's actions to date gave confidence that the standards would be enforced. Furthermore, customers would be instilled with confidence to borrow from a lender offering lower prices even if they had not previously heard of the lender, which would lead to a benefit to customers and new entrants.[583]

9.46 Dollar noted that this approach would lead to greater effectiveness and efficiency.[584] Welsh Trading Standards said that it was a more practical and consistent way to implement the remedy.[585] MAT repeated its support for a single independent PCW.[586]

9.47 Quiddi Hub noted that the FCA was currently undertaking the authorisation of consumer credit firms and that consideration should be given in implementing

[578] See Appendix 9.1.
[579] That is that multiple PCWs would be encouraged to adopt a minimum set of standards.
[580] Credit broking is a regulated activity under article 36A of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544) (RAO). Under the OFT there were two separate activities of credit brokerage and credit intermediation which the FCA has combined to make regulation simpler. As a result a greater range of firms are now considered to be credit brokers.
[581] CMA consultation on possible amendments to PCW and the statement of borrowing remedies.
[582] For example, CashEuroNet, CFA, Christians Against Poverty, Dollar, Welsh Trading Standards.
[583] Christians Against Poverty response to the proposed remedies consultation, p4.
[584] Dollar's response to the proposed remedies consultation, paragraph 2.2.
[585] Welsh Trading Standards response to the proposed remedies consultation.
[586] MAT's response to the proposed remedies consultation.

the remedy to avoiding holding up the authorisation process, and allowing firms to incorporate any new standards into their payday loan PCWs.[587]

9.48 Wonga stated that there might be advantages, but without knowing what criteria the FCA would adopt, it could not be certain of the relative cost. Wonga proposed that the FCA should publish information on the criteria it proposed to adopt.[588] As discussed in paragraph 9.77 we would expect there to be a statutory consultation on any criteria, but that based on our discussions the FCA would seek to introduce standards leading to similar outcomes to those we have specified. Wonga stated that the timing of the remedy was unclear.[589]

9.49 Wonga suggested that the FCA should have an 'authorisation window' for PCWs, at the conclusion of which all PCWs would be authorised.[590] There may be merit in having a transitional period that would allow payday loan PCWs to adjust to the new authorisation requirements. We expect, however, that the need for, or practicality of, such a window will be addressed by the FCA's implementation of the standards.

9.50 We considered the views of the FCA and the responses to our consultation. If the FCA ran an accreditation scheme then this could lead to different tiers of 'FCA-approved' PCWs such that customers might have been confused about the relative merits of an FCA-authorised payday loan PCW compared with an FCA-accredited PCW. An accreditation scheme run by the CMA could give rise to the same risk. There would also be a risk that the CMA and FCA could set different standards for the industry, creating uncertainty for the PCW operators and payday loan companies. There could also be additional costs in dealing with two different schemes.

9.51 We considered that a further benefit of including the additional standards proposed by our remedy within the FCA's authorisation of credit brokers is that this would embed the standards within the statutory regime and enable the FCA to use its full range of regulatory and enforcement tools to achieve the outcomes of our remedy proposal.

9.52 As noted in paragraph 9.44 we expect that authorisation as a credit broker would be compulsory for any payday loan PCW. Payday loan PCWs will therefore have less choice and some who might have chosen not to be accredited will, under the revised remedy, be required to incur the additional regulatory cost of the new standards for PCW. However, since it is likely that

[587] Quiddi Hub's response to the proposed remedies consultation.
[588] Wonga's response to the proposed remedies consultation, paragraph 2.18.
[589] ibid, paragraphs 2.19–2.29.
[590] ibid, paragraph 2.25.

all PCWs present in the market would be required to be authorised in any event, the cost of the remedy may be lower than if the accreditation option as specified in our PDR were implemented.

9.53 We also noted that if the required specification of payday loan PCWs was incorporated into the FCA's rules on consumer credit broking, some elements of the remedy as specified in our PDR would need to be amended to work more effectively within this framework or to address concerns expressed about their operation. We also took into account responses to our PDR and additional evidence from PCWs and other parties.

9.54 After considering the views of parties, we have decided to recommend to the FCA to introduce standards for payday loan PCWs through its existing legal framework. In our discussions with the FCA we have noted the need to allow an appropriate amount of time for existing payday loan PCWs to amend their websites and become compliant with the new standards. However, we understand from the FCA that it will consult on the new standards and on when they become effective and will allow a period after it finalises the legal framework for it to be implemented. We expect that this period will be sufficient for existing PCWs to comply with the new standards.

9.55 In the rest of this report we refer to authorisation (and 'authorised payday loan PCW') to refer to any requirement for PCWs to comply with minimum standards when comparing payday loans unless we are distinguishing between authorisation and accreditation, or we are reporting directly comments made by parties about accreditation.

Funding the payday loan PCW

9.56 An important aspect of the design of the payday loan PCW is how it will obtain funding to cover its costs. In this section we discuss the options for a PCW to fund its activities.

9.57 We considered there to be two principal ways in which a payday loan PCW might be funded:[591]

[591] Note that if we had decided to have a single official website we could also have considered a levy on lenders based on the volume or amount of issued loans (or another appropriate financial metric) with the intention of cost recovery shared between lenders in proportion to their share of the market.

(a) commercial arrangements to allow a PCW to receive commission or payment for referral of borrowers to a lender (which could either be based on the volume of leads provided[592] or a fixed listing fee);[593] or

(b) commercial arrangements to allow PCWs to receive payment for more prominent positioning of a lender's products on a PCW.

9.58 We discuss these in paragraphs 9.59 to 9.66 and conclude in paragraph 9.67. Some payday loan PCWs might also wish to carry additional commercial advertising (ie from parties other than payday lenders) but we considered that this was likely to be a secondary source of revenue.

- *Commercial arrangements where a PCW receives commission or payment for referral of borrowers to a lender*

9.59 The typical funding model of a mainstream PCW is to receive commission or a referral fee for any borrower who either clicks through to a lender's website or subsequently takes out a loan.[594] Under this approach, lenders would effectively fund the payday loan PCW, but would do so in return for a commercial benefit (eg the customer 'lead'). The distribution of costs between payday lenders would be determined by commercial negotiations and factors such as the volume of business transacted by different lenders through PCWs. In this way, we would expect lenders who benefit most from this remedy – ie by attracting the largest number of customers – to make the largest contribution to its funding.

9.60 We considered it likely that multiple PCWs would have sought accreditation,[595] such that there would be scope for commissions and fees to be determined by commercial negotiations between lenders and PCW operators.

9.61 However, in the less likely scenario in which only one authorised payday loan PCW was operational we considered that there would be potential for the PCW to exploit this position. Given this, we considered that where a lender had concerns that the PCW was not contracting with it on fair, reasonable and non-discriminatory terms, the parties should seek independent arbitration in

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[592] In turn, this could be measured by 'click-throughs', applications completed or loans issued.
[593] In its response to the further consultation on remedies Wonga suggested that high street lenders could be charged a fee for being listed on a PCW (see paragraph 9.103).
[594] Arrangements vary by PCW and individual lenders. See response hearing summaries of money.co.uk, moneysupermarket.com and Gagemax.
[595] See, for example, response hearing summaries with money.co.uk, moneysupermarket.com and Gagemax. Given *(a)* the FCA's view that all PCWs were likely to need to be authorised; *(b)* that the requirements of a PCW's functionality are no more under the revised amendments; and *(c)* at least two of the parties that have expressed interest in accreditation are already authorised, we consider that the prospect of multiple PCWs remains realistic.

the first instance. Where a lender can demonstrate to the CMA's satisfaction that it has been unreasonably excluded from all PCWs, the lender will not be prohibited from issuing loans. We discuss the steps that would be taken in such circumstances in paragraphs 9.170 to 9.176 below.

- *Payment for more prominent positioning*

9.62 Some existing PCWs have commercial arrangements with lenders which allow their products to be displayed with greater prominence, either in the initial ordering of products on a price comparison table, or how the product is displayed, either on a comparison table or on another page on the PCW.

9.63 Our customer research noted that most customers said they would not scroll very far down a results page, often only looking at the top five results and that brand familiarity and results appearing at the top of search results were the most influential drivers of choice.[596] This was consistent with how customers said they used search engines to find loans.[597] Our research also found that customers generally assumed that loans would be listed either in order of their popularity with customers or in price order and that the site would be working in their interest.[598]

9.64 Given the findings of this research we concluded that any additional prominence given to a product other than on the basis of the price of that product or relevant non-price characteristics chosen by borrowers would significantly reduce the effectiveness of this remedy.[599] Similarly any advantages in reducing barriers to entry would be diminished if established lenders were able to pay higher fees to display their products on a PCW above those of other (lower price) lenders. We also noted that if lenders paid for improved positioning, this might increase customer acquisition costs and these might be passed through to customers.

9.65 Parties expressing a view told us that a PCW should be independent, and nearly all parties told us that the initial order of products should be determined on the basis of price. One PCW operator (money.co.uk) told us that an operator should be able to determine the initial order of products within a

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[596] TNS BMRB research with payday lending customers, p14.
[597] Our research found that having searched for payday loans on a search engine, a prospective borrower's next step was usually to select the lender that was most familiar to the customer – either due to recommendations, advertising, or previous use – or was high in the search results. TNS BMRB research with payday lending customers, p12.
[598] TNS BMRB research with payday lending customers, p20.
[599] Given the significance of the absence of price competition in our AEC finding, we consider it particularly important that this remedy facilitates comparison of the prices of payday loans. However, we acknowledge that non-price factors can also be important to customers, so we would expect accredited PCWs also to enable customers to filter or rank products according to their non-price characteristics.

payday loan comparison on the basis of commercial arrangements as long as the ability to sort or filter results was accessible.[600] Another PCW operator (Gocompare) told us that its secondary sort criteria for some personal lending products (those hosted by lovemoney.com)[601] included acceptance rate, which would make borrowers more likely to choose a product that they would be accepted for, which it considered was beneficial for itself and for borrowers who were uncertain which lender was most likely to accept them.[602]

9.66 We also noted that some PCWs might wish to generate additional income from hosting commercial advertising. This is discussed further in paragraphs 9.164 to 9.169 and we will recommend to the FCA that it ensure that any advertisements on an authorised payday loan PCW are clearly differentiated from the objectively ranked table of payday loan products.

- *Conclusion on method of funding*

9.67 We decided that any authorised payday loan PCW should be funded by lenders making commercial arrangements with that PCW. However, we decided that commercial arrangements should have no impact on the relative prominence or order of lenders in a comparison and there should be no payment for prominent positioning.

Are PCWs likely to seek to be authorised to compare payday loans?

9.68 We next considered whether commercial operators would be interested in seeking authorisation for a PCW. We received a number of responses to our PDR expressing concerns that operators of generalist PCWs may not be interested in becoming authorised to compare payday loans.[603]

9.69 Wonga commented on the accreditation scheme that we proposed in our PDR and said that there were a number of uncertainties facing commercial PCW operators which would discourage entry and/or expansion to the payday segment, namely: *(a)* the accreditation regime, which had not been market-tested and would be finally determined by the FCA rather than the CMA;

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[600] Money.co.uk response hearing summary, paragraph 21.
[601] This does not include payday loans.
[602] If a PCW is paid for loans issued, where two products with identical prices are ranked using the rate of acceptance, and borrowers tend to apply to the lender with the highest acceptance rate, the PCW is therefore more likely to earn a commission. However, this also benefits the borrower by identifying loans they are more likely to be accepted for.
[603] In contrast, the CFA described the lack of a PCW seeking accreditation to be an “unlikely event”. CFA response to the PDR.

(b) [✂];[604] and *(c)* the impact of the price cap, which would create uncertainty about the likely profitability of operating a PCW in the payday loan segment.

9.70 Wonga identified two possible effects of the price cap. The first effect was that as loans would generate less revenue, the price that a PCW could charge for a lead might fall, making offering payday loan comparisons less attractive. The second was that PCW operators might benefit from lower prices for payday search terms as competition from lenders fell. Because the net impact of these effects could not be predicted, Wonga said that the overall uncertainty would discourage entry of PCWs into the market at least in the short term.[605]

9.71 We considered the risk that implementation of our remedy through the FCA authorisation of credit brokers (and thus making this mandatory for all payday loan PCW operators) would discourage PCW operators from offering any comparisons of payday loans regardless of the functionality of their payday loan comparison sites. Specifically we considered the risk that implementation through authorisation would either *(a)* deter new entrants to the market by raising barriers to entry, or *(b)* impose standards which existing authorised firms operating payday loan PCWs considered onerous or that insufficient time would be available to allow for transition.

9.72 Based on the responses received to the accreditation model, and notwithstanding our consideration that payday loan PCWs would need permission from the FCA[606], we considered that the risk with respect to new entrants being deterred was low. We considered that the risks for an authorised credit broker may be greater, if a breach of the standards for payday loan PCWs were to impact on its ability to continue acting as a credit broker in other markets. However, we concluded that the minimum standards we recommend that the FCA introduces will not be onerous and thus considered such a risk to be low.

9.73 We next considered Wonga's response (as outlined in paragraph 9.69) again in the context of implementing the remedy through the FCA authorisation of credit brokers (and noting our considerations in paragraph 9.72). However, we considered that there was little difference in the implementation of the remedy (and defining the relevant standards which PCWs would be required to meet) through the FCA acting as either accrediting or authorising body. We considered that authorisation would be no more onerous than accreditation (see

[604] [✂]
[605] Wonga response to the PDR, paragraph 2.6.
[606] See paragraph 9.44 for our consideration of the need for a payday loan PCW to need FCA permissions.

paragraphs 9.487 to 9.488). Therefore we considered that PCWs would be equally likely to seek to be authorised as to be accredited.

9.74 We further considered how to reduce the risk that no PCW operator would seek authorisation and how to ensure the remedy did not impose an inappropriate burden on lenders.

9.75 Wonga made a number of suggestions in response to the accreditation scheme proposed in the PDR, principally that:

(a) the accreditation scheme should give certainty to potential operators of the likely criteria at an early stage;

(b) the CMA should survey PCWs to understand the likelihood that they would seek accreditation;

(c) the CMA/FCA should request that Google remove its consumer advisory on accredited PCWs;

(d) the accreditation criteria should be revised after six months if no operator has applied; and

(e) lenders should have access to the infrastructure of lenderscompared.org.uk in the event that no PCW operator seeks or receives accreditation.[607]

9.76 We accepted that the market would benefit from transparency and FCA engagement with stakeholders. We note the FCA is able to respond to market developments and amend its rules and guidance, subject to cost benefit analysis and other statutory requirements, including a duty to consult publically.

9.77 We considered Wonga's suggestion of reviewing the FCA's requirements for authorised payday loan PCWs after six months if no PCWs had entered the market. Under implementation through the FCA authorisation of credit brokers we did not think that a review after six months would be practicable, given that it would be subject to FCA statutory consultation processes (and thus would take a number of months to conclude before any decision would be announced). For this reason the implementation of the standards through its authorisation framework would limit the FCA's ability to make amendments at short notice; we also noted that PCW operators would have greater certainty as a result because the scheme would not be subject to frequent changes or 'tinkering'. We concluded that the FCA's consultation on any further

[607] ibid, paragraph 1.7(a).

requirements for authorised payday loan PCWs would be sufficient for PCW operators to identify any significant issues.

9.78 Wonga's concerns with Google consumer advisories were also expressed by a number of other parties. We discuss this issue in paragraphs 9.85 to 9.92.

9.79 With respect to Wonga's suggestion about lenders having access to the infrastructure of lenderscompared.org.uk in the event that no PCW operator seeks or receives authorisation,[608] as the website is owned and operated by home credit providers we do not consider that it would be appropriate for us to require that this access is granted, nor do we have the powers to do so. However, we would not have a concern with payday lenders negotiating access to the infrastructure of lenderscompared.org.uk.

9.80 Prior to publication of the PDR we spoke to a number of PCWs to identify whether they would be interested in seeking accreditation. Some said they did not intend to seek accreditation:

(a) uSwitch told us that it did not currently have any plans to launch a payday loan comparison table. Its concerns were on the appropriateness of these products for its customers. It noted that regulatory actions of the FCA were likely to improve some of the more concerning practices it had seen in the payday loan market. With respect to consumer advisories, uSwitch noted the risks of any future intervention by Google should it offer payday loan comparisons.

(b) MoneySuperMarket was not currently considering seeking accreditation. It continued to have concerns over the consumer advisory and the impact that amending its website would have on its ability to use AdWords, and that for technical reasons (the use of cookies) any customer who accessed MoneySuperMarket's website via Adwords looking for an unrelated product would not be able to access payday loans subsequently, even if directly seeking payday loans.

9.81 However, others suggested they would be interested in seeking accreditation now or in the future:

(a) Runpath told us that it would apply for accreditation for its network of 'B2B2C'[609] services once the scheme was in place. Runpath did not use AdWords but told us that hosting payday loan comparisons on a separate subdomain or folder could affect user experience and the ability of PCWs

[608] This comment was made prior to our consultation on amending the implementation of the remedy to implement new standards under FCA authorisation of payday loan PCWs.
[609] 'Business-to-business-to-consumers', that is, its provision of data to a third party customer facing website.

to engage with customers to understand their specific borrowing needs (where borrowers accessed loan comparisons through an initial filtering tool or complete lending user experience wherein short term lending was a constituent component).

(b) money.co.uk was likely to apply to become an accredited PCW but this was subject to the CMA/FCA discussing criteria with PCWs, and it was concerned about the use of representative APR as the relevant metric of price. A portal linking back to money.co.uk's PCW on the FCA/CMA's website would increase likelihood of applying for accreditation, as would a 'stamp of approval'. money.co.uk told us that the FCA monitoring the activity of non-accredited PCWs would encourage it to seek accreditation. money.co.uk did not consider there to be barriers arising from Google's consumer advisory.

(c) Gocompare told us that given the right regulatory framework and customer protection in place, it would consider launching a payday loans comparison service on its website. It would also consider seeking accreditation if such a mandatory scheme was put in place. It noted the use of third party data suppliers and whether accreditation would pass through if the third party was accredited. Gocompare had concerns that the Google consumer advisory could have an impact on the viability of marketing a payday loan comparison service if payday loans were not visible.

(d) Comparethemarket.com (BGL Group Limited) would consider, at some point in the future, launching a price comparison service that included payday loan products, subject to a number of factors relating to regulatory activity and the outcomes for consumers and its ability to agree sustainable commercial terms with lenders. It did however raise a number of concerns with the need for further regulation of PCWs.[610]

(e) Confused told us that it would not launch a comparison table for payday lending in the short term. However, it may consider payday loans in its medium- to long-term plans subject to stability in the market and when it was confident customers were being treated fairly.

9.82 Moreover, following our consultation and in relation to new standards for payday loan PCWs, the FCA told us that some potential payday loan PCW

[610] It questioned whether further regulation of PCWs displaying payday loans is necessary provided payday lenders are regulated appropriately (but noted that it was difficult to offer further comment until the relevant standards are clear).

operators had expressed interest in operating an authorised payday loan PCW.

9.83 We did not consider it surprising that some of the existing PCW operators had reservations about entry into the market, particularly with respect to the Google consumer advisory and the negative reputation of the market (we identified the reputation of the market as a feature that acted as a barrier to new entry (paragraph 8.6*(b)*). However, we also note that where a PCW has authorisation to act as a credit broker and currently offers comparison services for another type of consumer credit, other than complying with the additional standards required of a payday loan PCW, there would be no additional application or authorisation process. Based on the comments of the PCW operators and expressions of interest made to the FCA[611] we concluded that it was likely that one or more PCWs would seek authorisation to compare payday loans.

9.84 In the event that no PCWs decide to compare payday loans we have decided to implement a fall back where lenders would have to commission a PCW for payday loans. This is discussed in paragraphs 9.187 to 9.196.

- *Google advertising restrictions*

9.85 Some operators of mainstream PCWs expressed concerns over restrictions known as 'consumer advisories' on paid search imposed by Google AdWords and were concerned about the impact of offering comparison services for payday loans on their core business (paragraphs 9.80 and 9.81). One party said it had ceased offering payday loan comparison services to ensure that other revenues were not put at risk (through being prevented from using paid search) ([✂]). Others had had their paid search account suspended for not appropriately segregating payday comparison tables ([✂]). [✂] told us that Google would need to provide an exemption for accredited PCWs.[612]

9.86 We contacted Google about these concerns. Google told us that the consumer advisory was appropriate, reflecting consumer warnings given by the US Federal Trade Commission and other consumer agencies. It ensured that users searching for other products and services were not targeted by advertisers of payday loan products. However, it did not prevent users searching for payday loans from seeing advertisements relevant to them.

9.87 Google said it was not the case that PCWs could not advertise other services on AdWords while also operating a payday loan comparison service under the

[611] As noted in paragraph 9.82.
[612] [✂]

same brand. Advertisers could segregate their payday loan content on a specific subdomain of their general site, enabling AdWords advertisements for the rest of the site to show in response to non-payday lending search terms. Google noted that, for instance, money.co.uk was able to operate in this way. Google further noted that the consumer advisory did not impact on organic search results.

9.88 Our review of money.co.uk's site found that its navigation menu structure was determined by the method that we used to access the site. When visiting the site either by entering the money.co.uk URL directly or searching for 'money.co.uk' and clicking on an organic result, payday loans were accessible under the loan menu. However, when we searched for 'money.co.uk payday' or 'payday comparisons' and clicked on an AdWords result relating for money.co.uk we found that payday loans were not displayed in the menu structure (though for payday search terms we were able to directly access the payday price comparison table). On subsequent visits to money.co.uk by entering the site's URL, payday loans remained hidden on the menu structure.

9.89 We noted Google's comments, and the ways in which mainstream PCW operators might be able to reconfigure their websites with relatively little or no cost in order to comply with Google's consumer advisory rule (such as the use of a subdomain (eg payday.xyz.co.uk), or a separate folder (eg www.xyz.co.uk/loans/payday)).[613]

9.90 We consulted a number of PCWs on these issues. One PCW (Runpath) told us that while it did not currently use AdWords, it considered that customer experience would be impacted if it was required to implement Google's requirements and any associated service redesign. A second PCW (uSwitch) told us that it would need to consider the risk that any future intervention by Google could have if payday loan comparison was offered. A third PCW (ComparetheMarket) told us there was no certainty that these rules would continue to be implemented in the same way. It noted that Google offered price comparison services through 'Google Compare' [✂]. A fourth PCW (Gocompare) told us that if payday loans were not visible when a customer accessed its site from a paid search link this could have an impact on the viability of marketing a payday loan comparison service. A fifth PCW (MoneySuperMarket) considered [✂] and that it would restrict visitors to its site who initially arrived looking to compare other (non-credit) products from subsequently accessing other products.

[613] Google provided evidence that the cost of a subdomain was negligible.

9.91 We considered that the concerns of PCWs were valid. Google provides a significant amount of traffic to PCWs (both organic and paid search) and a failure to comply with Google's interpretation of its consumer advisory could have a significant impact. There was also uncertainty about whether Google might amend its consumer advisory in the future to be more restrictive. We considered this could be a deterrent to PCWs seeking to be active in this market, particularly when combined with uncertainty over the market as a whole. Our terms of reference do not empower us to amend the consumer advisory. While there would be a benefit in interested parties engaging in dialogue with Google we recognise that it is uncertain whether Google would change its position.

9.92 However, we note that money.co.uk had configured its website to be compliant with the consumer advisory without expressing significant concern on its usability. There are other PCWs that operate without using AdWords. Therefore it is viable to operate PCWs in the payday loan market. The design of our remedy (that lenders must link to at least one PCW) means that PCWs will benefit from additional traffic. PCWs are also not constrained for the purposes of organic search from cross-linking between products.

- *High street lenders*

9.93 The principal method for PCWs to generate revenue is through a 'click-through', whereby borrowers click on a hyperlink that links to a URL on a lender's website that is unique to that PCW.[614] Commission is then typically paid either, when a customer clicks on the link and arrives at the lender's page, or if a loan is issued.

9.94 We contacted generalist PCW operators to establish if they had experience of providing comparison services for products not available online. These PCWs told us that they had no or little experience of providing such comparison services. Many of these lenders also raised concerns about the difficulties associated with listing high street lenders in their website.[615,616]

[614] The actual page may be the same but by amending the URL the web server is able to readily identify how the borrower was referred to the site.
[615] One PCW (Confused.com) was unconcerned. It said that listing high street lenders provided an additional challenge but it did not anticipate that this would, in itself, decrease its likelihood of seeking accreditation, should the accreditation accommodate these lenders market position.
[616] We note the CFA was also concerned about how high street lenders could operate alongside a PCW. It said that additional thought was needed about how high street lenders could operate alongside a PCW. Potential customers searching for a loan via an online PCW were unlikely subsequently to go to a high street lender in order to get a loan. A high street lender might be required to pay a specific price for a click through from a PCW when the net result was likely to be that a customer visited the lender's website but was unable to transact with the lender. The CFA said this was quite different from an online lender that was more likely to write some

9.95 One PCW (Gocompare) told us that it would be difficult for the PCW to maintain an audit trail for those customers who selected a high street provider and consequently to realise income in respect of those customers. It added that with high street lenders a PCW would lose sight of any quality control or insight into the customer experience once the customer had left the PCW's website. It said that these concerns would ultimately reduce the likelihood of a PCW seeking accreditation. Another PCW (money.co.uk) told us that in order to provide a helpful comparison of loans offered by high street lenders against those available online it would need to know the customer's location so that relevant and accessible results could be displayed. However, it was concerned that customers were generally unwilling to provide personal information. It also said that it would require an accurate and consistently updated postcode database which would be expensive to purchase and maintain. A third PCW (uSwitch) said that the PCW model in personal finance usually worked best when based on commission payment where a customer took out a product, rather than payment for click-through leads. This required customers to be tracked throughout their sale journey, which would be difficult with high street lenders who had no online presence.

9.96 In view of these concerns, we considered whether high street lenders might encounter difficulties in agreeing commercial terms with PCWs. This, in turn, may discourage PCWs from seeking approval if they perceive an obligation to find agreement with high street lenders even if they do not consider this to be viable and this could prejudice the effectiveness of our key remedy which is to create an effective pay day loan PCW sector in order to facilitate shopping around by customers, the vast majority of whom use online lenders. We therefore decided that lenders who only offer loans on the high street should not be obliged to have the details of their loans published on an authorised payday loan PCW. We did not conclude however that high street lenders should be necessarily excluded from authorised payday loan PCWs.

9.97 In this respect, we noted our finding that 83% of payday loan customers had taken out a loan online. To the extent that they provide competitive offers, high street lenders may therefore have incentives to be listed on an authorised payday loan PCW. We also noted that customers using high street lenders may be able to use a PCW to research alternatives online. Our customer survey indicates that among those customers who used only high

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business as a result of the click-through and as a result an online lender might be happy to negotiate a specific click-through rate with a PCW as there was an increased chance that the customer may apply for a loan. The CFA said that for a high street lender the costs would be excessive as the customer was unable to transact online and that the PCW may have little incentive to be flexible and lower their price for high street lenders, resulting in the PCW becoming inaccessible for high street lenders, at a reasonable price. (See CFA response to the PDR, pp1-2.)

street lenders and who have shopped around in the past, the majority relied on online sources to compare lenders.[617] This suggests that, even if they are not listed on a PCW, high street lenders would face competitive constraint as a result of customers using good quality PCWs to shop around and to compare prices offered by other lenders, including online providers. However, even if included on a PCW, we do not think that high street lenders would put a significant constraint on online lenders.

9.98 Not all respondents referred to our proposal to remove the requirement for high street lenders to publish details on a payday loan PCW.[618] Those responses which expressed a view were mixed with a number expressing concerns over protection for high street borrowers.[619]

9.99 Christians Against Poverty noted that while most loans were issued online, the high street market was not insignificant, and it was not convinced of the constraint that online lenders would place on high street lenders. It was concerned that high street borrowers on average had lower incomes and shopped around less than online borrowers.[620] As such they were more vulnerable and needed greater encouragement to shop around. Similarly, while noting the dominance of online lending, Welsh Trading Standards said that there was scope for some customer vulnerability.[621]

9.100 Wonga noted that 29% of borrowers had taken out a loan on the high street. It said that a number of indicators from the CMA's analysis pointed to greater harm in the high street segment of the market and it disagreed that high street operators would face competitive pressure in any event. It noted that our survey results had found that high street borrowers were less likely to compare products than online borrowers and said that high street lenders should not be excluded.[622]

9.101 We considered Wonga's point that high street borrowers should be encouraged to shop around, but considered that the factors that deter those borrowers shopping around online were unlikely to be remedied

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[617] 61% of these customers reported to have visited lenders' website and 22% used PCWs. TNS BRMB survey report, p101.
[618] Six parties did not explicitly refer to this matter in their responses. Six parties made reference to this and a seventh party (Torfaen CBC and Torfaen Local Services Board) supported the views of Welsh Trading Standards.
[619] Those supporting the removal of the requirement included Dollar and CFA. Christians Against Poverty, Islington Debt Coalition and Welsh Trading Standards either supported the inclusion of high street lenders or supported additional protections for high street customers. Wonga stated that exclusion of high street lenders was not proportionate.
[620] Christians Against Poverty response to the proposed remedies consultation, pp 4–5.
[621] Welsh Trading Standards response to the proposed remedies consultation.
[622] Wonga's response to the proposed remedies consultation, paragraphs 2.3–2.15.

proportionately. By requiring the inclusion of high street lenders, the number of PCWs seeking to offer payday comparisons would be adversely impacted.

9.102 We considered that there was a realistic expectation that the proportion of lending occurring online would continue to grow (as the proportion of the population with internet access and experience of undertaking online transactions increases). We acknowledge that a significant proportion of borrowers have used high street lenders, but note that a far greater proportion have used online lenders. While around half of high street borrowers use high street loans exclusively, the other half use both channels and any increase in competition online will become apparent to those borrowers. We considered that if high street lenders did not respond to the increased price competition online borrowing volumes would shift to online lenders, and this would increase the incentive for high street lenders to engage in price competition.

9.103 Wonga stated that there were potential ways to address the difficulties identified of including high street lenders on PCWs, such as lenders paying a listing fee to appear on a PCW.[623] Evidence submitted to us by PCWs indicates that there is a preference to generate revenue from completed purchases (paragraphs 9.93 to 9.95). With the listing fee the PCW would have no visibility of the volumes of business that were directed to a high street lender. Conversely the lender may pay a levy without receiving any referrals.

9.104 Wonga also suggested a click-through to a high street lender's website.[624] However, while larger high street lenders may have websites, our research indicates that small lenders very often do not and may not have the ability to implement appropriate tracking of referrals. We noted Wonga's further suggestion that identifying a local high street shop could be done by regions/ localities.[625] We agree that this is a potential solution but the issue could remain problematic for certain geographic areas (for example, how 'localities' within a large metropolitan area would be identified without providing a borrower with either an overly restrictive list or an overly exhaustive list of lenders of uncertain distance away).

9.105 We acknowledge that high street lending is a significant part of the market. However, we are conscious that a significant proportion of high street lenders have low volumes of payday loans and are likely to have weak bargaining power (as PCWs would need to devise ways of generating revenue from an 'offline' business, or would need to charge a flat fee). PCWs would find verifying product and price data much harder for high street lenders than for

[623] ibid, paragraph 2.14.
[624] ibid, paragraph 2.14.
[625] ibid, paragraph 2.15.

online lenders and they would be more expensive to include in the PCW's panel. We therefore concluded that high street lenders will not be required to appear on a PCW. However, we note that high street lenders would still be required to include a web link to an authorised payday loan PCW or a portal listing all authorised payday loan PCWs on the summary of borrowing.[626]

Completeness of a panel of lenders

9.106 The purpose of a PCW is to facilitate shopping around. To make this process effective, customers should be readily able to compare loans from a panel of lenders both on price and other characteristics that they consider relevant.

9.107 The effectiveness of borrowers' shopping around will be determined by the extent to which their search identifies the products potentially on offer to them. A good quality PCW enables customers to review a large number of products quickly and effectively, as it performs much of the search process for the customer and helps identify the products that are most likely to represent good value, given the customer's requirements. All else equal, a PCW is likely to be more effective in assisting a customer to find the most appropriate product for its needs the more products are on it.

9.108 We also identified that there may be circumstances where a restricted panel of products is more relevant to a customer, for example where specialist or niche products exist in a market. A PCW that specialises in those products could be more relevant to its target customers than if it listed a wider range of products.[627]

9.109 We discussed in paragraphs 9.35 and 9.36 whether lenders should be required to be present on all authorised payday loan PCWs and the implications for the bargaining power between lenders and payday loan PCWs.

9.110 Following on from our assessment of the effectiveness of shopping around in paragraph 9.107, we consider that using a PCW with as full a panel of lenders as possible would maximise the likelihood that customers take out the best-

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[626] See paragraphs 9.296, and 9.349 to 9.352 for discussion of this point in the context of a summary of the cost of borrowing.
[627] A specific example might be where certain customers are excluded from accessing all products in a market, such as mortgages which must be repaid by a certain age. By specialising in mortgages for older people, the initial panel of results, or set of default filters, could be focused on the needs of older customers. While such filtering could be done by requesting details of customers' age, a whole-of-market PCW requiring such information may be less user-friendly to customers in general, either in respect of design or time taken to complete a comparison.

value loan for them.[628] We also considered that it is generally in the interests of lenders for their products to appear on as many PCWs as possible in order to maximise exposure,[629] and it will usually also be in the interest of PCWs to offer borrowers a full panel of lenders as a source of a competitive advantage to attract borrowers to their sites[630] and generate revenue.[631] We took the view therefore that there are sufficient incentives on all parties for PCW lender panels to allow comparison of a large number of lenders.

9.111 We considered that some lenders might prefer their products not to be listed on sites where they would offer poor value compared with other products, and they might therefore seek to circumvent this remedy by only appearing on sites which offered customers a limited range of products.[632] A lender might seek to be listed on a spurious 'comparison site' that excluded new entrants or better-value products, possibly one created by the lender.[633]

9.112 In our view the incentives on both lenders and PCWs discussed in paragraph 9.110 limit the risk of this occurring in practice. We also noted that the FCA's Principles for Business[634] emphasise fairness and integrity and it seemed to us unlikely that creating a spurious PCW would be compliant behaviour.[635] Finally, where an expensive product was nevertheless the cheapest product listed on a payday loan PCW, other cheaper lenders may seek to list on that PCW.[636] In view of these points we concluded that it was unlikely that a lender would seek to avoid the remedy by listing on an expensive payday loan PCW or creating a spurious payday loan PCW.

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[628] Acknowledging that a restricted panel of products can be comprehensive where the nature of the restriction reflects the needs of a customer.
[629] This would be especially the case for new, or less well-known lenders. Simply appearing on the table is likely to increase brand awareness to some extent, particularly for those appearing at the top of a comparison. Where a PCW charges lenders for click-throughs, there will be little or no financial cost to a lender of appearing on the PCW.
[630] However, we note that PCWs could choose to compete on other aspects of their offering, such as offering credit eligibility tools or tailored panels of lenders.
[631] We considered that without revenue from pay-per-click arrangements from other lenders, there would be no incentive to advertise the PCW (such as through paid search). As a result, any borrower aware of PCWs and searching for general payday comparison terms would be less likely to access that PCW and thus borrowers would visit other PCWs and seek loans from other lenders.
[632] This was a point that Which? and Islington Debt Coalition made in response to our consultation on our amended remedy and further suggested that a lender might choose to create its own PCW to avoid appearing in any comparison table.
[633] However, we identified that even where a lender is not the cheapest, there were incentives to appear on a PCW: (i) the potential for a customer to compare loans on a price and non-price basis; (ii) circumstances where a customer is not eligible or cannot access the cheapest loan products; and (iii) the opportunity to enhance brand awareness. These are particularly true where a lender incurs costs in relation to the volume of leads it receives.
[634] For example, Principle 6: 'A firm must pay due regard to the interests of its customers and treat them fairly', and Principle 1: 'A firm must conduct its business with integrity'. Furthermore CONC 2.5.3 states that brokers must disclose links to any lender which it refers customers to.
[635] We considered the costs of creating a PCW and seeking FCA authorisation also to be a sufficient deterrent.
[636] Which would be reinforced by our recommendation to the FCA, set out in paragraph 9.175, to consider how to encourage PCWs to not exclude lenders unreasonably.

9.113 We identified a secondary risk that a lender with expensive products would choose to link to a PCW where its products did not appear (see also paragraph 9.352).[637] We therefore decided that a lender should provide hyperlinks from its own website only to authorised payday loan PCWs that the lender's products are listed on.

9.114 Parties generally supported the requirement for all lenders to be included on a payday loan PCW (though in a number of cases this was in specific reference to a single official or accredited site). One PCW operator told us that only FCA-authorised lenders should be included and that those lenders included would be the right type of organisations to be associated with its brand.[638] It would therefore wish to have the right to exclude certain lenders for reputational reasons or if it considered that a lender was not compliant with FCA rules.

9.115 Parties did not support the inclusion of credit brokers on a PCW, although one PCW thought that there should be appropriate consideration of the possible unintended consequences of excluding brokers.[639] Reasons given for excluding credit brokers from accredited PCWs were broadly related to the issues we have identified with lead generators (paragraph 8.5). Parties also told us that if brokers were included on a PCW, it would not be able to display an accurate price for a specific loan. We agreed with these submissions and considered that brokers should not be included within a price comparison table.[640] In response to our consultation on our amended remedy, both parties that commented on this point supported the exclusion of lead generators and brokers from a PCW and we received no submissions favouring their inclusion.[641]

9.116 Before reaching a decision on whether all PCWs must feature all lenders we considered the requirements of two accreditation schemes operated by sectoral regulators. Ofcom requires PCWs to be 'reasonably comprehensive'

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[637] If a lender considered that its product would be unlikely to be selected by a borrower using a PCW, it might consider that preventing a borrower comparing other loans with the loan initially selected by the borrower might increase the likelihood that the borrower would return to the originating lender (by pressing the back button on the browser).
[638] moneysupermarket.com response hearing summary, paragraph 19. It considered, however, that any PCW would need a critical mass of lenders to be successful (ibid, paragraph 29).
[639] Money.co.uk response hearing summary, paragraph 20.
[640] Some parties specifically stated that lead generators should be excluded; other parties stated that only authorised lenders should be included (which we took to mean no unauthorised lenders or any other credit intermediary). Views expressed by parties on the specification of the PCW to include the ability for a borrower to enter the amount and duration of a loan and see products ordered by price seemed incompatible with the inclusion of lead generators. For example, CashEuroNet said that the inclusion of lead generators could confuse customers unless their status was clearly identified (response to provisional findings and Remedies Notice, paragraph 8.3). See also Appendix 9.2, paragraphs 51–66.
[641] [✂], MAT response to the proposed remedies consultation.

(which is achieved by including products which combined have over 90%[642] market share within a customer's chosen market) while Ofgem requires PCWs to list all suppliers regardless of whether commercial arrangements have been agreed.

9.117 We considered the requirements of Ofgem's Confidence Code to better understand these issues. We understand that the Confidence Code requires PCW operators to include all tariffs except where an energy supplier requests a PCW not to show its tariff information.[643] However, some PCWs give greater prominence to the suppliers that customers can switch to online (and thus ones that the PCW receives commission from).[644]

9.118 In the scheme that we proposed in our PDR we would not expect the same problem to occur as there was no requirement to list all lenders.[645] Given the speed and perceived urgency with which borrowers sought to take out loans and the ability to access a loan, presenting lenders which were not directly available[646] would offer little benefit.

9.119 A significant change from the scheme proposed in our PDR is that PCWs would have been able to provide comparison services without having to be accredited but now would be required to be authorised. Given this, we were keen to ensure that the standards were not unnecessarily onerous. We considered that if all products had to be displayed this may reduce the incentive for PCWs to offer payday loan price comparison services and may force existing PCW operators to cease providing payday loan comparisons.[647]

9.120 While acknowledging there may be benefits to borrowers from ensuring PCWs cover a large proportion of lenders' products, we were concerned not to distort the market by affecting the bargaining power of different parties.

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[642] Report for Ofcom, *Accreditation scheme for price comparison services: audit guidance document*, 5 November 2013.
[643] 'Requirement two – Tariffs and Price Comparisons', Ofgem Confidence Code. Certain types of tariff are also excluded.
[644] For example, see BBC news story, 20 October 2014 and The Big Deal on Energy website. This is an area of the Confidence Code that has been consulted upon and has been changed to require a whole of market comparison by default. See Ofgem Confidence Code review – January 2015 policy decision.
[645] As there would be little benefit to a PCW of listing lenders from which they did not receive commission, unless they intended to market themselves as a whole-of-market comparison.
[646] We considered that borrowers that tended to use high street lenders would be an exception.
[647] We acknowledge that there are a number of PCWs in the energy market that are accredited, however, given the *(a)* different sizes in the number of customers in the two markets and *(b)* the number of suppliers, there may be very different economic considerations. Furthermore, the nature of information collected for energy comparisons make the ability to 'click through' or switch as part of the comparison to be a far more significant aspect in deciding which provider to choose.

However, we also recognise that a comprehensive panel of lenders may assist customers to shop around more effectively.[648]

9.121 We decided that for the reasons set out in paragraph 9.115, in order to ensure that borrowers were comparing information about actual loan products, an authorised payday loan PCW should not include entries from credit brokers or other intermediaries.

- *Link from lenders' websites to the authorised payday loan PCW*

9.122 To enhance the effectiveness of the remedy, we considered it important for borrowers to be made aware of the existence of authorised payday loan PCWs adhering to enhanced standards. For borrowers searching for loans using search engines, both organic and paid search may help promote the sites.

9.123 Some borrowers may repeatedly use the same lender and may return to the lender's site directly without shopping around. These customers may not become aware of payday loan PCWs. We consider that the effectiveness of the remedy would be enhanced by requiring lenders to include a prominent link to one or more authorised payday loan PCWs on both their publicly accessible website and any summary of borrowing costs.[649]

9.124 We consider that the link should be prominent and positioned so that it would be clearly visible to a borrower prior to beginning an application (even if that borrower was directed to the lender from a lead generator's website). The link might be immediately adjacent to a set of sliders to specify a loan, or any link to an application page (or on the landing page if a customer was directed to the site from a lead generator). It should be in text of appropriate size, font and colour so that a borrower is aware of it.

9.125 Given our decision to recommend to the FCA the introduction of standards for PCWs which would allow multiple authorised payday loan PCWs, we considered that there were two main options for this aspect of the remedy:

(a) The lender could link to a list of all authorised payday loan PCWs.[650]

(b) The lender could link to one or more authorised payday loan PCWs of their choosing on which that lender's products appear).

[648] As noted in paragraph 9.175 we are recommending to the FCA that it consider how to ensure that payday loan PCWs do not unreasonably exclude FCA-authorised payday loan providers or their payday loan products.
[649] As discussed below in paragraph 9.349.
[650] Which might be hosted on the accrediting body's website.

9.126 There are pros and cons of either approach. A requirement to link to a list of all authorised payday loan PCWs would increase customers' awareness of all the available PCWs and reduce the risk of lenders directing customers to a PCW where they ranked favourably. Islington Debt Coalition thought that allowing the lender to choose a website might indicate bias, given the reputation of some PCWs.[651] Christians Against Poverty told us that a portal containing hyperlinks to all authorised payday loan PCWs should be maintained by an independent body.[652] We considered that this was a task that either the FCA or MAS would be able to undertake and we recommend that the FCA as authorising body considers how to develop such a portal.

9.127 We considered this further and identified that linking to a list of all authorised payday loan PCWs might reduce the risk of a lender linking to a poor website. Conversely, our customer research indicated that respondents thought it would be desirable to minimise the time and number of steps required to navigate to a PCW, which would support the option of linking directly to one website.[653] Given these considerations, we decided that lenders could choose which of these two options to take.

9.128 Views of parties were mixed on the requirement to hyperlink to a PCW.[654] MAT told us that the link would not be sufficient on its own without debt advice.[655] Global Analytics was concerned that placing the hyperlink on its site would reduce its customer conversion rate. It was concerned that its marketing expenditure on clearly and transparently informing consumers about its products would be channelled to directing borrowers to other lenders.[656] We agree that there may be a diversion of visitors from a lender's website to an authorised payday loan PCW, but a PCW may also cause other visitors to go to the lender's website, depending on the strength of the lender's products. We considered that this did not preclude lenders from developing strong brands and competing both on price and on non-price features of their products. While an authorised payday loan PCW would facilitate comparison of price and other attributes, borrowers might consider the reputation of the lender and their own experience with those lenders as factors in choosing between similarly priced loan products.

[651] Islington Debt Coalition response to the PDR, p2.
[652] Christians Against Poverty response to the proposed remedies consultation, p3.
[653] TNS BMRB research with payday lending customers, p37.
[654] See Appendix 9.2.
[655] MAT response to the proposed remedies consultation.
[656] Global Analytics response to the proposed remedies consultation.

The functionality required of an authorised payday loan PCW

9.129 We considered what should be the minimum functionality of a payday loan PCW. In so doing, we sought to strike an appropriate balance between helping borrowers to find, compare and contrast products and creating a set of overly rigid criteria which could deter the emergence of a thriving price comparison sector for payday loans.

9.130 We noted the shortcomings of existing PCWs in paragraph 6.89, which in our judgement necessitated setting some minimum standards as part of the approval of PCWs. We noted, however, that over-specifying such criteria also carried some risks, namely:

(a) discouraging participation by making compliance onerous and burdensome;

(b) an overly prescriptive specification may not be appropriate for future product offerings;

(c) the user experience could be impaired if providers had to focus on compliance over usability;

(d) increasing monitoring costs; and

(e) discouraging innovation and competition between payday loan PCWs.

9.131 Our research with users of payday loans found that borrowers wanted to be able to enter a specific loan amount and duration and compare the total cost of repayment. While headline price remained the most important aspect that customers wanted to compare, customers also wanted to sort by other variables, including: the time it took to receive the money and the documentation required; late fees; and the flexibility of repayment.[657]

9.132 We therefore took the view that a customer should be invited to specify the amount and duration of a loan before a comparison table is presented, to ensure that borrowers understand the relative cost of the loan they wish to take out.

9.133 In developing our package of remedies we commissioned customer research to understand how customers engaged with PCWs and the information presented. With respect to ways of measuring the price of a loan, our customer research indicated that borrowers compared loans on both the TCC and the APR. APR, while generally not well understood, was perceived as

[657] TNS BMRB research with payday lending customers, p8.

being easy to compare, and acted as a proxy for price when the total repayment amount was not listed. Respondents tended to look briefly at the representative example, but were unable to use it to compare loans as the loan periods were often different.[658]

9.134 We considered that where lenders offer variable pricing for a given product or substantially similar products[659] the price published should be that achieved by at least 51% of customers.

9.135 Parties universally supported the ability for borrowers to specify the amount and duration of a loan (including instalment loans for durations greater than 28 days). Views on specific search and filtering criteria differed but referred to a broad variety of criteria which included:

(a) amount of loan;

(b) duration of loan;

(c) repayment structure (eg whether repayments are made in single or multiple instalments);

(d) speed of processing the application;

(e) whether applications and payment are processed 24/7;

(f) the ability to enter a postcode to find high street lenders;

(g) flexible payment options (whereby early repayment would reduce interest); and

(h) late fees and other additional charges.

9.136 Islington Debt Coalition told us that the ability to identify faster payment options should not be over-emphasised, as this tended to encourage customers to make a choice based on this factor rather than considering whether a payday loan was right for them.[660]

9.137 We considered that the ability to search and filter by these criteria would assist borrowers in shopping around. However, in the first instance we consider it is most important that a customer understands the price of a given loan, which requires a borrower to specify the amount they wish to borrow and the duration. To the extent that a payday loan PCW facilitates searching on

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[658] ibid, p20.
[659] Such that a lender whose products were not different in material aspects other than the rate of interest and/or other charges.
[660] Islington Debt Coalition response to Remedies Notice.

additional variables we consider this would be beneficial as long as it does not make the site more difficult to use (or provide scope to influence the way the loans are ranked for commercial reasons). We would not envisage the authorisation criteria preventing this.

9.138 We considered the accessibility of a site with respect to the significant number of users accessing loans (and PCWs) using mobile devices (whether this is smartphone or tablet).[661] In our view requiring a detailed set of standard search features to be available would run the risk of impairing an operator's ability to design an attractive, accessible website. We considered that commercial PCW operators and professional web designers would be best placed to incorporate the findings of our customer research and the other evidence we have published.

9.139 We considered Islington Debt Coalition's suggestion that an accredited payday loan PCW should offer a telephone service[662] and that this would be valuable for customers who did not have internet access. Such customers were necessarily unlikely to use online lenders, so we thought the value of such a service would be limited. We noted that for many borrowers there may only be one high street lender in their local area and this service would thus offer little utility to many customers. We further considered that the cost of establishing a call centre might deter PCW operators from seeking authorisation. However, we saw no reason that a PCW operator could not offer such a service if it chose to do so.

9.140 We discuss some aspects of assisting borrowers to identify the loans for which they would be accepted in our discussion of measures to facilitate shopping around without unduly affecting a borrower's ability to access credit (paragraphs 9.257 to 9.262).

- *Total amount payable*

9.141 The purpose of our remedy is to remedy the AEC we have identified by encouraging the creation of a marketplace for payday loan PCWs that offer customers a comparison service enabling customers to determine which loan best meets their search criteria. To this end we initially proposed that the best method of comparing the price of a loan was the TCC.

9.142 Following further discussions, the FCA told us that the total amount payable (being the TCC and the loan amount) might be a more appropriate measure

[661] For example, Gagemax told us that over half of its traffic came from mobile devices (Gagemax response hearing summary, paragraph 19).
[662] Islington Debt Coalition response to the PDR, p2.

for us to recommend as the primary basis for comparison. We consider that the total amount payable by the customer would be an equally appropriate figure to present to the customer and by which to rank products. The ranking of lenders would be the same as if the products were ranked by TCC, but the amount shown to the customer would be the full amount that the customer would need to repay.

9.143 A number of parties supported our proposal for products to be ranked by objective criteria using price as the default (using total amount payable as the relevant metric)[663] and to allow additional searching and filtering based on product criteria.[664] Christians Against Poverty strongly supported the use of total amount payable rather than APR as it increased transparency and encouraged borrowers to be forward thinking about the implications of their choices.[665] Global Analytics noted that ranking by total amount payable was appropriate as long as the length of loans compared was equal. It was concerned that very short-term products might be developed to appear higher up on a PCW.[666] Wonga stated that it had no concerns over this presentation and noted it already provided this information to customers.[667]

9.144 We are satisfied that the total amount payable would be an appropriate measure of price for the purposes of the primary sort criteria and therefore recommend to the FCA that this should be the default measure by which products should be ranked.

9.145 Comparethemarket.com told us that if our intention was that payday loan products should be ranked on the basis of objective criteria selected by the customer then we should confine the text of this remedy to this specific point.[668] We disagree on this point. Having regard to certain practices that we have identified in the market, we consider that, in addition to the requirement that loan products are ordered using objective criteria, it is important that products are presented in a consistent manner and with equal prominence.[669] It is for this reason we consider that a PCW should be 'competitively neutral'.

[663] For example: CashEuroNet response to the proposed remedies consultation, paragraph 2.3.6; Christians Against Poverty response to the proposed remedies consultation, pp5&6; Dollar response to the proposed remedies consultation, paragraph 2.2(i); Global Analytics response to the proposed remedies consultation; Welsh Trading Standards response to the proposed remedies consultation.
[664] CashEuroNet response to the proposed remedies consultation, paragraph 2.3.6.
[665] Christians Against Poverty response to the proposed remedies consultation, p5.
[666] Global Analytics response to the proposed remedies consultation.
[667] Wonga response to the proposed remedies consultation, paragraph 2.30.
[668] BGL Group Limited response to the proposed remedies consultation, paragraph 4.1.5.
[669] That is that certain products should not be shown in larger text, or different colours, or with any wording that might draw a customer's attention away from the product ranked the highest based on the criteria that the customer has used to search and order products by.

9.146 Comparethemarket.com also said that our use of the term 'competitively neutral' and our requirement that listings should be 'independent of any commercial relationship' would result in confusion for payday loan PCW operators. It further told us that these requirements may also discourage product innovation.[670,671]

9.147 We disagree that our requirements would cause confusion. For the reasons set out in paragraphs 9.62 to 9.67 we consider that it is an important aspect of our remedy that commercial arrangements have no impact on the relative prominence or order of lenders in a comparison. We consider this to be a clear requirement that is unlikely to cause confusion. Linked to this is the issue raised by Comparethemarket.com about innovation. Our requirement that products are presented objectively does not prevent lenders and PCWs negotiating on the commission payable (which may result in lower prices to the borrower).

9.148 We also note that detailed implementation of this recommendation will be subject to FCA consultation.

- *Secondary sort criteria*

9.149 In our PDR we stated that any ranking on price comparison tables should not be affected by any commercial relationship the operator may have with lenders included on the PCW's panel. We had previously identified that should the total amount payable for two identically specified loans[672] be the same, a PCW would need to utilise some form of additional sort criteria (which we refer to as secondary sort criteria). In revising this remedy we consider it appropriate to clarify our expectation that the secondary sort criteria should also be independent of any commercial relationship the PCW operator may have with lenders included on its panel.

9.150 A number of parties responded to our proposal for competitive neutrality.[673] CashEuroNet suggested that sorting by post-default charges would generate consumer benefit by incentivising lenders to lower late fees.[674] Christians Against Poverty told us that guidance should be issued on what should be

[670] Comparethemarket.com gave the specific example of where a PCW might otherwise agree to share some of its commission with a lender to subsidise the cost of the loan to the consumer, which might affect rankings, but the PCW does not do so for fear of such an arrangement conflicting with the obligation to ensure a 'competitively neutral' proposition. (BGL Group Limited response to the proposed remedies consultation, paragraph 4.1.5.)
[671] We also consider that our proposed standards are sufficiently high-level that they do not prevent innovation in the design and presentation of PCWs.
[672] That is, with respect to the borrower's search criteria.
[673] Note also our discussion on the use of total amount payable as the primary sort criteria.
[674] CashEuroNet response to the proposed remedies consultation, paragraph 2.3.6.

used as secondary sort criteria and suggested customer ratings or the impact of late fees would be appropriate.[675] Dollar, however, said that secondary sort criteria should be on the basis of normal commercial arrangements between the PCW and lender.[676] However, we conclude that it would be inappropriate for an authorised payday loan PCW to determine the order of products in any comparison on the basis of the commercial arrangements it has in place with individual lenders.

- *Scope of comparisons made using authorised payday loan PCWs*

9.151 We considered the range of products that should be included on a payday loan PCW.

9.152 During the course of the investigation we identified a number of different credit products available to customers for periods of one year or less which, subject to their use by customers, were within the scope of our investigation.

9.153 Parties broadly supported the ability of a PCW to provide a comparison of a wider variety of credit products than payday loans, such that a PCW could present a continuum of credit products for borrowers to compare.

9.154 In response to our PDR MoneySavingExpert.com told us that if borrowers were concerned about price they would not use a payday loan and that the PCW remedy would not have a huge impact. MoneySavingExpert.com told us we should encourage alternative types of sustainable borrowing, such as credit union borrowing and social fund borrowing.[677] MYJAR told us that other forms of credit should not be prevented from appearing on a PCW.[678] Similarly, CFA told us that we should encourage the FCA to look at requiring all consumer credit providers to participate on accredited PCWs.[679]

9.155 We considered the benefits of requiring a PCW to incorporate all types of consumer credit. We see clear advantages in customers being able to compare a range of types of personal credit, some of which may better meet the customer's needs than payday loans. However, we would be unable to compel providers to list these products on a PCW as our terms of reference are limited to payday loans.

[675] Christians Against Poverty response to the proposed remedies consultation, p6.
[676] Dollar response to the proposed remedies consultation, paragraph 2.2(i).
[677] MoneySavingExpert.com response to the PDR.
[678] MYJAR response to the PDR.
[679] CFA response to the PDR.

9.156 Comparethemarket.com told us that it was possible that brokers or other intermediaries might seek to offer payday loans under their own broker/intermediary brands, with the underlying finance provided by a traditional lender. It told us that should such 'white label' loans be excluded from a PCW, this would reduce competition.[680] We considered that where a broker offered a specific product (as outlined by Comparemethemarket.com) there was unlikely to be any issue with it being listed by a PCW.[681] We considered that the FCA would be best placed to consider how to ensure standards appropriately reflect this distinction in a broker's role.

9.157 We have therefore decided that while payday loan PCWs should not be precluded from offering a wider selection of products for comparison, we will not require an authorised payday loan PCW to include non-payday loan products. However, as noted in paragraph 9.121, we do not consider it appropriate to include credit brokers or other credit intermediaries in a price comparison and we are recommending to the FCA that only loan products should be listed. We also do not require PCWs to include high street products, for the reasons discussed in paragraphs 9.93 to 9.105, but we will not prohibit them from doing so.

- *Stating the number of lenders compared*

9.158 In our discussions with the FCA, it suggested that a PCW should be clear, fair and not misleading in its description of its coverage of the market and that we might consider recommending that a PCW should state how many lenders were included in the PCW's panel. This was not originally an aspect of our remedy as set out in our PDR, but in our view it would assist borrowers if they were to understand the number of lenders (and products) being compared and provides some context to the nature of the comparison undertaken. Furthermore the ability to assess the size of a panel of lenders would allow borrowers to compare how comprehensive a PCW's panel is.[682] To the extent that payday loan PCWs might wish to develop as broad a panel of lenders as possible, we considered that this could reduce the likelihood that lenders would be unable to find a payday loan PCW that is willing to include that lender's products (subject to agreeing commercial terms).

9.159 Christians Against Poverty supported the need for a PCW to state how many lenders were in its panel, but considered that borrowers would benefit to a

[680] BGL Group Limited response to the proposed remedies consultation, paragraph 4.1.6.
[681] However, we did not consider that it would be appropriate for brokers promoting a specific loan product to then promote its brokerage services if a customer was not eligible for that loan.
[682] We considered that this would aid a customer in understanding the breadth of comparison, particularly where a PCW had only a limited number of lenders on its panel, but which might not otherwise be apparent.

greater extent if the total number of authorised payday lenders was stated to give a better indication of coverage.[683] Comparethemarket.com told us that the requirement on PCWs to state how many lenders they had on their panel was unlikely to cause problems for PCWs but noted that if consumers associated the largest selection of lenders with the most comprehensive or desirable PCW offering, this might disadvantage those PCWs that were more selective and demanded higher-quality standards of the lenders they listed.[684] We considered that payday loan PCWs could choose to compete in a number of ways in respect of the panel of lenders that they presented to borrowers.[685]

9.160 We considered whether the requirement to state the size of the panel would disadvantage subsequent PCW entrants whose panel of lenders might not be as extensive. However, as discussed, we see significant advantages for lenders to be present on as many payday loan PCWs as possible,[686] which would assist a new payday loan PCW in developing its panel.

9.161 We conclude that it would be beneficial to borrowers to be able to identify whether payday loan PCWs had broad coverage of the market and that this in turn would encourage PCWs to develop a broad panel of lenders. We consider that the FCA may choose to require PCWs to provide this information, but we are not including this as a specific recommendation.

- *Conclusion on minimum functionality for authorised payday loan PCWs*

9.162 We decided that the basic functionality of an authorised payday loan PCW should be:

(a) The ability for a customer to specify for the loan they wish to take out:

(i) the amount of the loan;

(ii) the duration of the loan; and

(iii) the repayment structure (eg single repayment, instalments).

(b) The products listed on the PCW results list should be displayed by the total amount payable, in ascending order. Where two products are equally ranked on price, a payday loan PCW should choose criteria that reflect an

683 Christians Against Poverty response to the proposed remedies consultation, p6.
684 BGL Group Limited response to the proposed remedies consultation, paragraph 4.1.7.
685 For example by emphasising the rigorous process for lenders to be listed, or in offering a broad panel of lenders.
686 As payment for appearing on a PCW is typically determined by click-throughs, cost is only incurred as the result of receiving a lead.

objective product characteristic but not a commercial relationship with lenders.

(c) By using the website, the customer should be able to:

(i) identify the structure of late fees charged by lenders; and

(ii) identify if a loan can be repaid early and whether this will reduce the loan cost.

(d) Payday loan PCWs should not be precluded from offering a wider selection of products for comparison but we will not require an authorised payday loan PCW to include non-payday-loan products. However, we do not consider it appropriate to include credit brokers or other credit intermediaries in a price comparison and we are recommending to the FCA that only loan products should be listed. We do not require payday loan PCWs to include high street products but we will not prohibit them from doing so.

(e) The FCA may choose to require payday loan PCWs to provide information on the total number of lenders compared but we are not including this as a specific recommendation.

Other issues

9.163 Finally we consider some other issues relevant to remedy design.

- *Advertising*

9.164 In paragraph 3.63 of our PDR we noted that our customer research showed that most customers would not scroll very far down a results page, often only looking at the top five results and that brand familiarity and results appearing at the top of search results were the most influential drivers of choice. Our research also found that customers assumed that loans would be listed in order of their popularity with customers or their price and that the site would be working in the consumer interest.

9.165 In our PDR (paragraph 3.67) we proposed that there should be no advertising of payday loans on the PCW's payday loan page. The purpose of this exclusion was to ensure that customers should not confuse a loan ranked at the top of the table on objective criteria with a paid-for advertisement for a payday loan that may not best meet the customer's search criteria.

9.166 The FCA has told us that it would find it difficult to prohibit payday loan banner advertisements from a PCW. The FCA told us that its existing rules required that advertisements and other financial promotions be fair, clear and not misleading. It considered that the objectives of our remedy would be addressed through its supervision of authorised firms.

9.167 The FCA's Consumer Credit Sourcebook (CONC) requires that financial promotions should be clear, fair and not misleading.[687] The FCA said that this might be sufficient to ensure that any advertising is separate from and additional to the ranking of loan products so that it did not cause confusion to borrowers. Guidance within CONC states that a firm should ensure that a communication or a financial promotion is clearly identifiable as such,[688] and if it compares a product or service with one or more other products, that the comparison is meaningful and presented in a fair and balanced way.[689] Credit brokers must also indicate the extent of their powers and should make it clear to borrowers the nature of the service they provide.[690] We noted, however, that the FCA told us that it would review its existing rules and guidance in light of our recommendations, and consult on any additions or amendments.

9.168 We consider that there is a benefit to including our proposed remedy within the FCA's authorisation of credit brokers, and that the FCA shares our objective of not allowing advertising to undermine the value of the objective ranking of loan products on a PCW. We are therefore recommending to the FCA that the FCA ensures that any advertisements on an authorised payday loan PCW are clearly differentiated from the ranking table of payday loan products.

9.169 Christians Against Poverty told us that our proposals to ensure advertising was clearly differentiated from the comparison table was welcome, but offered weaker protection to customers than an outright ban on advertising. It supported a ban on all direct advertising by lenders (including 'featured products').[691] However, we did not consider that this would be proportionate.

- *Unreasonable exclusion of lenders*

9.170 In our discussion on the completeness of a panel of lenders we considered that using a PCW with as full a panel as possible would maximise the likelihood that customers take out the best-value loan for them (paragraph 9.110). We noted that there were incentives for customers, lenders and individual PCWs for a payday loan PCW's panel of lenders to be as comprehensive as possible. However, we also identified that there were

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687 CONC 3.3.1.
688 CONC 3.3.5(4).
689 CONC 3.3.8.
690 CONC 3.7.3 and guidance in 3.7.4.
691 Christians Against Poverty response to the proposed remedies consultation, p5.

circumstances where customers may benefit from a restricted panel of lenders such as where a payday loans PCW specialises in particular products (paragraph 9.108).

9.171 MYJAR identified the risk that a PCW might not allow a given lender to appear on its listing.[692] Comparethemarket.com told us that there were all manner of reasons why a PCW might not wish to contract with a payday lender and provided 9 reasons why a PCW may not wish to contract with a lender and vice-versa.[693] It further argued that there was no compelling legal basis to require a PCW to justify its decision.[694]

9.172 In our PDR we proposed recommending to the FCA that the accreditation scheme should require PCWs not to unreasonably exclude any lenders from their site. The purpose was to ensure that lenders should not be excluded from the market as a result of our Order through being unable to achieve a PCW listing. In our revised remedy we have included a carve-out from our Order to allow lenders who are unreasonably excluded by all authorised payday loan PCWs to continue to provide payday loans if they are able to demonstrate to the satisfaction of the CMA that they have been unreasonably excluded. However, such lenders will be required to continue to seek to identify an FCA-authorised payday loan PCW on which their products would be listed and to provide the CMA with evidence of the steps taken. Where a lender is found to have been reasonably excluded, the obligation on the lender to publish its prices on an authorised payday loan PCW will remain. If the lender wishes to stay in the market as an online payday lender it will have to be prepared to negotiate terms or set up an authorised payday loan PCW.

9.173 In response to our consultation a number of parties have asked what criteria might be used in an assessment of unreasonable exclusion. For a lender to be listed on a payday loan PCW, the PCW and lender will need to agree commercial terms. If the PCW and lender fail to do so it would be necessary to assess whether the payday loan PCW has offered terms that were discriminatory without justification. Having reviewed a number of other factors, including those provided by Comparethemarket.com,[695] we considered that

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[692] MYJAR response to the PDR, p2.
[693] The factors were: (i) the PCW's own lack of knowledge of the payday sector; (ii) the lender's reputation; (iii) the lender's willingness/ability to provide information and meet the PCW's service levels; (iv) the lender's record of regulatory compliance; (v) how the lender advertises its products and whether this reflects badly on the PCW's brand; (vi) the lender's financial standing; (vii) customer complaints regarding the lender; (viii) the commercial terms that can be agreed by the parties (including commission); and (ix) a basic decision on the part of the PCW to limit its panel.
[694] BGL Group Limited response to the proposed remedies consultation, paragraph 4.1.8.
[695] Unless a PCW operator was only offering specialist or niche products we did not consider that the PCW's own lack of knowledge of the payday loan sector would be a valid reason for us to conclude that a lender had not been unreasonably excluded since we would expect a PCW to research the market so that it could decide whether to offer a payday loan comparison service.

relevant objective factors in an assessment of unreasonable exclusion might include:

(a) the lender's reputation and how it advertises its products;

(b) the lender's willingness/ability to provide information and meet the PCW's service levels;

(c) the lender's record of regulatory compliance;

(d) the lender's financial standing; and

(e) customer complaints regarding the lender.

9.174 We would expect a PCW's concerns about a lender's reputation to be based on factors such as FCA regulatory action[696] or customer complaints to the PCW which were significantly greater in volume or severity than for other lenders.[697]

9.175 We are continuing to recommend to the FCA, for the reasons outlined in paragraph 9.172, that it considers how to ensure that PCWs do not unreasonably exclude a lender.

9.176 In our view the combined effect of these two provisions (that lenders are required to publish details of their payday loans unless unreasonably excluded and our recommendation that PCWs do not unreasonably exclude lenders) should continue to achieve our aim of allowing new entrants to enter the market without concerns of being unreasonably excluded from all authorised payday loan PCWs[698] and discourage authorised payday loan PCWs from excluding any lender.

[696] Where the FCA took regulatory action, we would consider that this would be reason for removal from a panel, but where a lender commits to changing its borrowing practices to the satisfaction of the FCA, ongoing exclusion would not be appropriate.
[697] In part the nature of negative reputation might need to be considered in light of the scale of the lender, such that a larger, better-known lender could develop a negative reputation, while smaller lenders could provide the same level of service but remain outside of the public consciousness.
[698] In paragraph 3.14 of the PDR we noted that if a greater proportion of payday loan customers used PCWs, new entrants and smaller lenders would be able to raise awareness of their brands and product characteristics more effectively and potentially more cheaply through a PCW than through alternative channels, such as lead generators, pay-per-click adverts and advertising through traditional media.

- *PCW market power*

9.177 Two parties[699] raised concerns that PCWs would have excessive market power which could increase costs to lenders and thus borrowers.

9.178 CashEuroNet referred to the CMA's findings in the private motor insurance (PMI) market investigation[700] that PCW operators 'appeared to enjoy a significant degree of market power'. It told us that while there might be competition between products on PCWs, competition between PCWs would be less fierce, borrowers would 'single-home' on one PCW, and we should restrict the use of MFNs.[701,702]

9.179 CashEuroNet also raised concerns that if only one PCW was accredited it would have even greater market power and that the commercial relationships between lenders and PCWs should be monitored.[703] For this reason, we considered that in the unlikely event that only one authorised payday loan PCW was operational and where a lender had concerns that the PCW was not contracting with it on fair, reasonable and non-discriminatory terms, the parties should seek independent arbitration in the first instance. Where a lender could demonstrate to the CMA's satisfaction that it had been unreasonably excluded from all authorised payday loan PCWs, the lender would not be prohibited from issuing loans.[704]

9.180 We considered the issues found in the PMI market. We did not consider that it is necessarily the case that those issues will arise in this market. In the design of this remedy, we envisage multiple authorised payday loan PCWs and lenders able to choose the PCWs they wish to link to. This will provide lenders with bargaining power in their negotiations with PCW operators. For the reasons set out in paragraph 9.534*(a)*, we do not consider that payday loan PCWs will acquire excessive market power. However, we considered it appropriate for the FCA to reach its own conclusion on this point in specifying the authorisation standards. We also note that the FCA would be able to assess whether a PCW was abusing its position under its concurrent competition powers.

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[699] These included [✄] and Wonga (Response to proposed remedies consultation, paragraph 2.22; Response to the PDR, paragraph 1.6(a).)
[700] www.gov.uk/cma-cases/private-motor-insurance-market-investigation.
[701] Most favoured nations – restrictions imposed by (for example) a PCW that a supplier's product will not be available at a lower price from another source.
[702] CashEuroNet response to the PDR, paragraphs 3.3–3.8.
[703] ibid, paragraphs 3.9 & 3.10.
[704] However, as noted in paragraph 9.172, such lenders will be required to continue to seek to identify an FCA-authorised payday loan PCW on which its products will be listed and to provide the CMA with evidence of the steps taken.

- *Other*

9.181 MoneySuperMarket.com supported the need for PCWs to adopt high standards but was concerned that accreditation could limit innovation.[705] We considered that our approach should mitigate this risk by focusing on a small number of product features that customers need to compare to find the loan that best meets their needs. We also note that the minimum standards will be subject to FCA consultation.

9.182 In response to the accreditation scheme outlined in the PDR money.co.uk made a submission on a number of points on the scheme (relating to the information lenders should provide, the metric of comparison and the default ordering of products).[706] We did not think that money.co.uk's suggestions were inconsistent with our approach, but it will be for the FCA to determine the appropriate standards and to consult stakeholders as part of any change to the Consumer Credit Sourcebook.

9.183 CashEuroNet said that use of the existing FCA framework could be a strong basis for achieving our aims if it was supported by a specialist advisory board.[707] As regards CashEuroNet's suggestion of an advisory board, we considered that seeking views of stakeholders will be an important aspect of ensuring that suitable standards are introduced and that periodic reassessment may be necessary as the market develops. However, we consider that it is appropriate for the FCA to decide how to engage with the market.

9.184 MAT[708] told us that PCWs should include a disclosure, similar to the 'health warning' required on lenders' websites. It is our understanding that this is already a requirement for all authorised firms offering promotions for HCSTC (which would include credit brokers and thus PCWs).[709] Christians Against Poverty told us that borrowers would benefit from signposting to free debt advice and that borrowers should be assured that using a PCW would not affect their ability to access credit, and should be further informed prior to having a credit search undertaken at the point of application.[710]

9.185 MoneySavingExpert.com told us that we had misunderstood the payday loan market: the issues in the market were regulatory issues not competition

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[705] MoneySuperMarket noted that PCWs were likely to come under the scope of FCA regulation of consumer credit broking (see response to the PDR). We considered that the FCA would therefore be best placed to develop a scheme which complemented its own existing consumer credit rules.
[706] money.co.uk response to the PDR.
[707] CashEuroNet response to the proposed remedies consultation, paragraphs 2.1.1–2.1.4.
[708] MAT response to the proposed remedies consultation, p1.
[709] CONC 3.4.1 requires the disclosure for all promotions of HCSTC.
[710] Christians Against Poverty response to the proposed remedies consultation, pp6&7.

issues, and a PCW would therefore not be effective.[711] We disagree, for the reasons summarised in paragraphs 9.12 to 9.22.

Implementation of remedy

9.186 Having specified the design of the remedy we now consider implementation issues. We first discuss a fall-back remedy, to cater for the event (which we consider unlikely) that no potential PCW operator seeks to be authorised to provide a payday loan PCW (paragraphs 9.187 to 9.196). We then discuss timing of implementation of the remedy (paragraphs 9.197 to 9.198).

Fall-back position

9.187 In our PDR we discussed the risk, with the accreditation option, that no payday loan PCWs applied to be accredited. We considered this risk to be low. However in our PDR (paragraph 3.45) we decided that in the event that no payday loan PCWs applied for accreditation we would implement a 'fall-back position'. In such circumstances online lenders' products would still be required to be listed on a payday loan PCW and online lenders would therefore need to create or commission an accredited payday loan PCW. We set out a time period to allow lenders to comply.[712]

9.188 As we are now proposing that the standards should be part of the FCA's authorisation of credit brokers and in order to give a market-based solution sufficient time to develop, we have amended the fall-back position. Online lenders would be required to create or commission an authorised payday loan PCW (fall-back PCW) in the event that no authorised payday loan PCW exists by the Obligation to Publish Date (the later of 12 months after the FCA publishes its decision[713] (the Decision Date) or the date the FCA's new standards become effective). In our additional consultation on remedies we stated that online lenders would be given a period of 6 months to create or commission a fall-back PCW and apply for authorisation. The requirement for online lenders' products to be listed on an authorised payday loan PCW would apply once this PCW was authorised.

9.189 The CFA were concerned that, should lenders need to establish their own payday loan PCW, it would take more than 6 months for them to be ready to

[711] MoneySavingExpert.com response to the PDR.
[712] In footnote 72 of our PDR we noted that 'The CMA remedy order would provide that in the event that no PCW applies for accreditation within a specified period – for example, six months of making the Order – lenders would be required to create or commission a PCW that satisfied the accreditation criteria within a further period (for example, 12 months).'
[713] Which will be through the publication of a Policy Statement.

make an application for authorisation.[714] Wonga told us 12 months would be an appropriate period for lenders to establish a website and that lenders should only be required to publish details of their products after a further 6 months.[715]

9.190 We recognise the potential challenges for lenders to establish their own payday loan PCW. We noted Wonga's point that it could not be expected to begin commissioning a website before the end of the initial 12 month period. It should be apparent some time before the end of the 12 month period whether or not a payday loan PCW is likely to be authorised because negotiations with lenders would need to occur before launch of the payday loan PCW to allow products to appear on it when it was launched. We are keen to encourage the development of a PCW as soon as possible. We are therefore amending the remedy so that the application for authorisation of the fall-back PCW must be submitted within 6 months of the Obligation to Publish Date. Where that cannot be done but demonstrable progress to that end has been made the CMA may allow an extension of up to 6 months.[716]

9.191 We considered the timeframe after authorisation of a fall-back PCW within which online lenders would be required to publish details of their products. We considered that Wonga's request for a further period of 6 months was too long. However, we recognise that after a PCW operator has been authorised there may be some residual issues before the site can launch. Where lenders are cooperating on establishing a fall-back PCW arrangements for those lenders to be listed on the fall-back PCW can be made at the same time as the site is being authorised. However other online lenders may seek to be listed on the fall-back PCW that have not been directly involved in its design or specification. We decided that a period of 3 months following authorisation of a fall-back PCW should be allowed for lenders to appear on it. This is consistent with the provisions for appearing on third party PCWs.

9.192 Where an application for authorisation of a fall-back PCW is declined or granted on a conditional basis, online lenders can apply to the CMA for a short extension (of up to 3 months) if this extension would then allow authorisation to be obtained or any conditions to be satisfied.

9.193 To ensure the remedy is not overly costly to lenders, we are keen to facilitate an industry led solution and do not expect individual lenders to have to

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[714] CFA response to the proposed remedies consultation.
[715] Wonga response to the proposed remedies consultation, paragraphs 2.19–2.29.
[716] We would expect lenders to keep the CMA informed of their progress in obtaining authorisation of a fall-back PCW throughout the process and signal well in advance of the deadline whether an extension might be required. We would not usually expect an extension for the full 6 months to be required.

establish their own PCW. We would expect a PCW to be commissioned on behalf of a wider group of lenders and we see value in the fall-back PCW being made open to all online lenders.[717] Where a single lender, or consortium of lenders undertakes to directly commission a fall-back PCW on behalf of a wider group of lenders, the lenders involved in any such arrangement should notify the CMA of this arrangement, to demonstrate compliance with our Order.

9.194 Based on evidence from PCWs and our discussions with the FCA, we consider that a greater number of authorised payday loan PCWs will be active in the PCW market than at present and the fall-back position is unlikely to be required. We also understand that, if the fall-back PCW were required, there would be a large number of firms that could provide a PCW commissioned by lenders.[718] An option for lenders would be for them to commission a credit broker to develop a fall-back PCW.[719] Were this option to be followed by lenders, the same timescales would apply as in paragraph 9.190 – the PCW should be operational within 6 months of the Obligation to Publish Date. Where the fall-back PCW is not operational within 6 months of the Obligation to Publish Date but demonstrable progress has been made the CMA may allow an extension of up to 6 months.

9.195 In the event that online lenders publish their details on one or more independent third party authorised payday loan PCWs in compliance with our Order and all such PCWs then exit the market we consider that it would be appropriate for lenders to enter discussions with the CMA and the FCA to explore the opportunity to create an industry-led PCW.

9.196 Wonga told us that if lenders were required to develop a PCW it might not be subject to the same competitive pressure from other PCWs and would lack incentives to compete actively for lenders and visitors.[720] We recognise that there would not be the same competitive dynamic in this situation. We identified that the fall-back PCW would have an incentive to become efficient as the costs of the site would be passed directly to lenders but similarly recognised that individual lenders would have different appetites for expenditure on the development, enhancement and promotion of the site other than through hyperlinks from lenders' own websites. We concluded, however, that if the fall-back PCW met appropriate standards and if lenders

[717] We would necessarily assess other online lenders' (which were not directly participating in the commissioning of the payday loan PCW) ability to publish prices on an industry led payday loan PCW.
[718] As a result of a large number of firms having appropriate permissions to act as a credit broker.
[719] We would consider a credit broker with interim permissions to be 'authorised' for the purposes of our remedy. However, as the broker would be obliged to go through the authorisation process in a window determined by the FCA's timetable, we considered it would be inappropriate to impose the same requirement on existing brokers.
[720] Wonga response to the PDR, paragraph 2.11.

included hyperlinks as appropriate, the remedy would remain an effective way for customers to shop around to find the best-value loan for them.

Timing issues and facilitating compliance

9.197 We have decided that we will require online payday lenders to publish details of their loans on a PCW operated by an FCA authorised firm or approved person according to the following timings:

- *The requirement to publish*

(a) Online lenders will be prohibited from issuing loans unless details of their products are published on an authorised payday loan PCW[721] by the Obligation to Publish Date.

(b) Where one or more such PCWs exist at the Obligation to Publish Date but an online lender does not have details of its loans published on an authorised payday loan PCW, the CMA may grant an extension of up to 3 months provided that the lender can demonstrate that negotiations are underway with one or more PCWs that are reasonably likely to result in agreement.

(c) Where no authorised payday loan PCW exists at the Obligation to Publish Date but online lenders consider that there is a reasonable prospect that a payday loan PCW is about to become operational and that lenders and PCWs will be able to agree terms, lenders can seek an extension from the CMA of up to 3 months to appear on that PCW.[722]

- *Obligation to establish an authorised payday loan PCW*

(d) Where there is no reasonable prospect of an authorised payday loan PCW becoming operational quickly (ie within 3 months of the Obligation to Publish Date) online lenders will have a period of 6 months after the Obligation to Publish Date to submit an application to the FCA for authorisation of a payday loan PCW.

(e) Where an online lender has not submitted an application for authorisation, either jointly or individually, but where good progress in preparing an

[721] That is a PCW operated by a FCA authorised firm or approved individual. We expect that all payday loan PCWs operating in the UK will necessarily be subject to the amended standards that we expect the FCA to introduce.
[722] We expect that lenders would be aware of a new PCW before its launch, as the PCW would likely wish to engage in negotiations to develop a panel of lenders. Furthermore, to the extent allowable by the FCA, the CMA will share intelligence on likely new entrants.

application can be demonstrated and no other authorised payday loan PCW has been created, then an extension of up to 6 months to submit an application for authorisation may be granted by the CMA.

(f) Where an authorised credit broker is commissioned to create a fall-back PCW FCA authorisation is not required. Online lenders will be allowed 6 months from the Obligation to Publish Date for the fall-back PCW to be operational. Where the fall-back PCW is not operational after 6 months but demonstrable progress has been made, the CMA may allow an extension of up to 6 months for the site to become operational. When the fall-back PCW is operational 3 months will be allowed for online lenders to appear on it.

(g) Where an online lender (or group of lenders) establishes or commissions a payday loan PCW on behalf of other lenders, each lender must notify the CMA that it is associated with the application for authorisation.

(h) Where an application is made by an online lender (or lenders) for authorisation of a payday loan PCW, details of their payday loan products must appear on the PCW within 3 months of authorisation. Where an application for authorisation is declined by the FCA or granted on a conditional basis the CMA will consider whether an extension of 3 months would allow FCA authorisation to be obtained or any conditions to be satisfied.

- *Unreasonable exclusion*

(i) Where an online lender is able to prove to the satisfaction of the CMA that it has been unreasonably excluded from all authorised payday loan PCWs, the prohibition on lending will not apply.

(j) Where an online lender that has been unreasonably excluded from one or more PCWs becomes aware of additional payday loan PCWs or where the CMA notifies the lender of the operation of additional payday loan PCWs, the lender must demonstrate it has attempted promptly to negotiate reasonable commercial terms with those PCWs.

- *Demonstrating Compliance*

(k) Online lenders must notify the CMA at the point at which:

(i) they have complied with the requirement to publish details of their loans on an authorised payday loan PCW;

(ii) they wish to apply for an extension;

(iii) they intend to apply for authorisation for a fall-back PCW; or

(iv) they believe themselves to have been unreasonably excluded from all authorised payday loan PCWs.

(l) Online lenders will report quarterly from 6 months after the Decision Date to 6 months after the date they are listed on a payday loan PCW and annually thereafter (on a date to be determined):

(i) Whether they are in discussion with PCWs about publishing their loans on a payday loan PCW (until their loans are published on at least one payday loan PCW);

(ii) Whether details of their loans are published on an authorised payday loan PCW;

(iii) Details of the payday loan PCWs on which their products are published; and

(iv) Details of any authorised payday loan PCW from which the lender considers itself to have been unreasonably excluded.

(m) Where details of an online lender's loans are not published on any authorised payday loan PCW and it considers itself unreasonably excluded, it should state the attempts taken to gain access to the PCWs from which it considers itself excluded. Furthermore such lenders should state the attempts they have made to gain access to any authorised payday loan PCWs which subsequently enter the market.

9.198 It is our expectation from our discussions with the FCA is that it will consult on its proposals on how to introduce enhanced standards in summer 2015 and will publish these standards in late 2015 or early 2016. As part of that consultation, we understand from the FCA that it will consult on the new standards and on when those standards will become effective.

Conclusion on PCW remedy

9.199 Given our assessment of the evidence and views submitted by both the FCA and other interested parties we have amended the remedy we set out in the PDR. We have decided to introduce standards for payday loan PCWs through the FCA's authorisation of credit brokers. We therefore recommend to the FCA that it reviews its requirements for payday loan PCWs and uses its regulatory tools to raise the standards which apply to them.

9.200 We have set out above the core principles that we believe should underpin a new set of standards for payday loan PCWs and we will make a recommendation to the FCA that it should incorporate them into its existing regulatory framework for credit broking.

9.201 The revised remedy retains the main feature of the original proposal. There remains an obligation on online lenders to show their products on at least one payday loan PCW that satisfies the necessary criteria. These criteria will now be embedded within the FCA's authorisation standards.

9.202 The loan product details that online lenders will be required to publish on at least one authorised payday loan PCW should allow the payday loan PCW, as a minimum, to rank each loan product according to the total amount payable. The details should include the total price of the product, the duration, repayment structure, late fees and early repayment rules for each product.[723]

9.203 The remedy outlined above in Figure 9.1 has greater emphasis on and sets out clearly the consumer outcomes that we wish to achieve. The FCA has confirmed its desire to achieve these outcomes. However, the FCA will retain its discretion as to how best to realise these outcomes and it has a statutory duty to consult on the new standards. We consider that substantial benefits would arise from our payday loan PCW remedy.

9.204 Having decided that the use of the FCA's existing regulatory framework is the most appropriate method of raising standards of payday loan PCWs, we are keen to ensure that all payday loan products are available for comparison. To ensure that customers are able to shop around more readily we intend to issue an Order to require payday lenders to supply details of their prices and products for publication on at least one PCW operated by an authorised person or firm and to provide prominent links on their website to the authorised payday loan PCW.

9.205 We will continue to engage with the FCA following the publication of this report in order that the FCA may consult on how to introduce new standards in parallel to our work in making the Order. We expect to issue a draft Order for informal consultation shortly after publication of this report followed by a formal consultation. In line with statutory time frames we expect to issue the final Order within six months of this report.[724]

9.206 We do not anticipate that the Order will require immediate publication of prices on an authorised payday loan PCW when the new standards

[723] We note that the PCW is also required to show the APR for each product, but this should not form the basis of the ranking.
[724] See paragraph 9.458 for further details.

introduced by the FCA become effective; rather, lenders will be required to have published details of their products within 12 months of the Obligation to Publish Date.

9.207 For the purpose of compliance a person or firm that has interim permission from the FCA will be considered to be authorised.[725]

9.208 Our current expectation is that if within 12 months of the Obligation to Publish Date there are no authorised payday loan PCWs, lenders will have a further period of six months to develop an authorised payday loan PCW. Where lenders can demonstrate to the satisfaction of the CMA good progress a further period of six months will be permitted.

9.209 We note that there may be payday loan PCWs which currently have interim permission or authorisation but whose current website is unlikely to comply with the enhanced standards to be introduced by the FCA. In demonstrating compliance with our Order we consider that lenders should confirm with the authorised payday loan PCW that the PCW considers itself to be compliant with FCA requirements.[726]

9.210 We have sought to avoid over-specifying the authorisation criteria in order to facilitate innovation and increase the likelihood of multiple operators seeking authorisation. Both the FCA and potential payday loan PCW operators will have access to our customer research[727] and findings in conjunction with their own product testing to introduce appropriate standards and design payday loan PCWs with appropriate functionality respectively.

9.211 To aid the monitoring of this remedy we will require all online lenders issuing payday loans to periodically notify the CMA of the authorised payday loan PCWs on which their products are published and the PCW or portal to which the lenders hyperlink. Lenders will be required to report quarterly from 6 months after the Decision Date to 6 months after the date they are listed on a payday loan PCW and annually thereafter (on a date to be determined).[728]

9.212 We discuss the potential costs of the remedy in paragraph 9.508 to 9.520.

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[725] Consumer credit firms that held a Consumer Credit Licence from the OFT and wish to continue regulated activities have had to seek interim permission which will be effective until the firm applies for authorisation according to a series of windows for different firms, which will last until March 2016. Because the window that different firms must apply during varies by circumstance we are keen not to inadvertently give a competitive advantage to certain PCWs because of the authorisation process.
[726] Such confirmation could be sought during commercial negotiations.
[727] TNS BMRB research with payday lending customers.
[728] As per paragraph 9.197(l)–(m).

Improving the disclosure of late fees and other additional charges

Summary of remedy

9.213 Figure 9.2 summarises our remedy to improve the disclosure of late fees and other charges.

FIGURE 9.2

Measures to improve the disclosure of late fees and other additional charges

In order to increase customers' awareness of late fees and other additional charges, the CMA has decided to recommend to the FCA to:

- Take the steps necessary to ensure that payday lenders and relevant intermediaries are fully aware of their obligations to disclose to customers prominently and on a timely basis details of late fees and other charges payable if a loan is not repaid in full and on time.
- Review proposals by payday loan PCWs for complying with these obligations as part of the authorisation process.
- Monitor actively the presentation by payday lenders and relevant intermediaries of information about late fees and other charges payable if a loan is not repaid in full on time and the accessibility of this information to customers, and to take enforcement action where necessary.

How the remedy addresses the AEC and/or resulting customer detriment

9.214 We found that customer demand is particularly insensitive to the fees and charges incurred if customers do not repay their loans in full and on time. We found this to be the result of a combination of:

(a) the limitations in the information provided by lenders regarding late fees;[729]

(b) the difficulty in making comparisons given lenders' different charging structures;[730] and

(c) a tendency among some customers to be overconfident about their ability to repay.[731]

[729] See paragraph 6.97.
[730] See paragraph 6.98.
[731] See paragraph 6.96.

9.215 By improving lenders' disclosure of late fees and charges we expect to address and remove the limitations identified.

9.216 We also expect that if information on late fees is disclosed prominently and on a timely basis, customers would be more aware of the existence of these charges and they would be more likely to take these fees into account when choosing a payday loan. To the extent that payday loan PCWs also disclose this information prominently and on a timely basis this would improve customers' ability to make informed comparisons and to factor this pricing element – when relevant – into their decisions.

9.217 Our remedy requiring a lender to provide existing borrowers with a summary of borrowing costs (paragraphs 9.292 to 9.355) complements this measure. It enhances customers' ability to assess the likelihood that they will incur late repayment charges by providing them with timely information on the outcome of their most recent loan and the charges they incurred on that loan (and of the charges incurred on all loans with the lender during the past 12 months).

Remedy design

9.218 We set out below our consideration of issues relating to the design of this remedy:

(a) In paragraphs 9.219 to 9.225 we consider ways in which disclosure of late fees and charges may be improved.

(b) In paragraphs 9.226 to 9.227 we consider potential unintended consequences that might result from an excessive focus by customers on late fees and other charges incurred if a customer does not repay a loan in full and on time.

(c) In paragraphs 9.228 to 9.31 we discuss the impact of the FCA's price cap.

Options to improve the disclosure of late payment fees and charge

9.219 During our investigation, we reviewed a number of lenders' websites. While the headline rate or price is typically obvious on the front page, charges arising from late payment are not always prominently displayed or clearly presented.[732] We received broad support for this remedy option in responses to our Remedies Notice[733]and PDR.[734]

9.220 We identified two ways of presenting information on late fees:

(a) Setting out the structure of late fees and the events that will cause those charges to be levied.

(b) Requiring the inclusion of a common scenario of late payment such as the cost of payment two weeks late based on the loan applied for.

9.221 We considered whether such information could be presented alongside the initial quote for the price of a loan when a customer enters their desired loan amount and duration. Such information would also be useful to borrowers if made available on a payday loan PCW.

9.222 We received broad support from parties that the presentation of fees and charges should be transparent.[735] A number of parties told us that existing regulation was sufficient but that enforcement action by the FCA might be necessary.

9.223 Some parties told us that scenarios were a useful way of presenting the potential additional costs that borrowers could incur and were likely to have a greater impact than other methods of presentation. However, other parties told us that there was a danger that a scenario could be misleading as it focused attention on one specific example and necessarily could not present the potential costs of borrowing accurately. To maximise the impact of any disclosure of additional costs, some parties suggested that this disclosure should occur early in the application process.[736]

9.224 We discuss the potential impact of the FCA's price cap in paragraphs 9.228 to 9.231 and in greater detail in Section 6.

9.225 We noted that lenders currently presented their fees and charges with varying levels of transparency and this variation was reflected in the responses by parties to our consultation. MAT said that we should recommend that the FCA ensures lenders present the information in a uniform way using prescribed

[732] See paragraph 6.93.
[733] See Appendix 9.2, paragraphs 93–119.
[734] For example, see the responses to the PDR from CashEuroNet, CFA, Dollar, Islington Debt Coalition and MAT.
[735] A number of lenders told us that they had appropriate disclosures but supported transparency in the market as a whole. See Appendix 9.2, paragraphs 92–106.
[736] See Appendix 9.2, paragraphs 92–106.

terms and a similar format.[737] We considered that the widespread adoption of the best practices present in the market would go some way towards remedying the problems we have identified but that the FCA was best placed to consider whether uniform presentation was appropriate. We noted that within CONC there is guidance stating that 'a firm should consider highlighting the principal consequences for the customer, including the consequences of missing payments or underpaying'.[738]

Potential risks of excessive focus on late fees

9.226 In our view borrowers enter a credit agreement on the basis that they expect to be able to repay the credit facility as agreed. However, borrowers should be made aware of the potential additional costs of the loan in the event that they are unable to repay the loan or an instalment on time.

9.227 We considered whether increasing the prominence of late fees would mean that customers may choose a loan primarily on the basis of the charges if they were unable to repay on time or in full. Based on the limited consideration of late fees by potential borrowers at present and the consistent views received from parties, we judged that this risk was unlikely to materialise in practice.[739]

Price cap and FCA regulation

9.228 The FCA price cap came into force on 2 January 2015.[740] It limits the total cost of a loan including interest for late payments and default fees.

9.229 Prior to the introduction of the cap, a number of lenders[741] told us that they would not envisage using low late fees as an advertising tool and that borrowers did not typically apply for credit expecting to default.[742] However lenders may have different late fee structures – for example, some lenders may not levy additional charges whereas others might not charge ongoing interest – albeit that they must now operate within the overall constraints of the price cap. Consequently there remains potential for customers to take additional fees and charges into account in shopping around even if some

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[737] MAT response to the PDR, p2.
[738] CONC 4.2.2.
[739] Provident told us that it thought this was a low risk based on its experience in the home credit market (Provident response hearing summary, paragraph 24). CashEuroNet also told us that it did not see any significant risk of increasing prominence (CashEuroNet response hearing summary, paragraph 19).
[740] See also Section 3.
[741] For example, CashEuroNet did not think default fees were a factor in a borrower's decision on whether to take out a loan (CashEuroNet response hearing summary, paragraph 19).
[742] To the contrary, we have found the opposite: that customers are over-optimistic about their ability to repay.

lenders do not actively use the structure of their late fees in promoting loans to customers.

9.230 We discuss the price cap at greater length in paragraphs 9.420 to 9.427 below.

9.231 MYJAR told us that our remedy as proposed in the PDR was superfluous given the FCA's powers and statements on their use.[743] We recognised that the FCA has the appropriate powers and therefore we concluded that making a recommendation to the FCA was appropriate and would ensure that any regulatory response was fully consistent with existing regulation but gave greater impetus to the FCA to consider the issue. The FCA is likely to consider the issues we have identified as part of its authorisation process and ongoing monitoring, but we still find it important to indicate formally to the FCA that we consider there is inconsistent practice within the market.

Implementation of remedy

9.232 We considered whether our overall objective of increasing customer awareness of late fees and other additional charges would be best implemented by means of an Order (for example, requiring lenders to disclose these fees in a particular way), or by making a recommendation to the FCA.

9.233 We considered that making a recommendation to the FCA was more appropriate as this would ensure that action taken as a result of this remedy complements the existing regulatory activity of the FCA, uses the full range of its regulatory tools and is consistent with the requirements of the CCD.

9.234 We have therefore decided to recommend to the FCA to:

(a) take the steps necessary to ensure that payday lenders and relevant intermediaries are fully aware of their obligations to disclose to customers prominently and on a timely basis details of late fees and other charges payable if a loan is not repaid in full and on time;

(b) review proposals by payday loan PCWs for complying with these obligations as part of the authorisation process; and

(c) monitor actively both the presentation by payday lenders and relevant intermediaries of information about late fees and other charges payable if a loan is not repaid in full and on time and how this information is made available to customers, and to take enforcement action where necessary.

[743] MYJAR response to the PDR, p2.

Measures to help borrowers shop around without unduly affecting their access to credit

Summary of remedy

9.235 Figure 9.3 summarises our recommendation to the FCA to help customers shop around without unduly affecting their ability to access credit.

FIGURE 9.3

Measures to help borrowers shop around without unduly affecting their access to credit

The CMA has decided to recommend to the FCA that it work closely with lenders, CRAs and operators of authorised payday loan PCWs to encourage initiatives, including greater use of quotation searches, to enable customers to search the market without adversely affecting their access to credit.

Based on our analysis, the following specific issues appear likely to merit further exploration as part of any further work in this area:

(a) Whether the disclosures made to borrowers by lenders and intermediaries are sufficient in respect of (i) the point at which a credit check will be undertaken and its nature; and (ii) whether at the end of an application process a credit search has been performed and whether it has left a 'footprint' on the customer's credit file.

(b) Whether customers should be informed immediately prior to the point that a credit check is undertaken that one will be performed.

(c) Whether FCA guidance on the use of quotation searches should be revised to the status of a rule in situations where lenders introduce variable or risk-based pricing structures.

(d) Whether there is consistency in the availability, format and visibility of quotation searches and whether guidance to CRAs and lenders could be developed.

How the remedy addresses the AEC and/or resulting customer detriment

9.236 This remedy is intended to complement our payday loan PCW remedy in reducing the difficulties that borrowers face in shopping around and identifying the best offer. The development of an effective price comparison sector will help borrowers to shop around and find out about the price and non-price characteristics on offer. However, as the market currently operates, borrowers will typically not be able to establish their likely eligibility for any given loan without applying for that loan.

9.237 Payday loan borrowers facing uncertainty about whether they will be approved for a loan currently need to go through a full credit application process in order to establish whether any given lender would be willing to lend to them. When coupled with the perceived urgency surrounding the decision to take out a payday loan (see paragraphs 6.51 to 6.56 and paragraph 8.5*(a)*), this may result in borrowers either choosing their loan primarily on the basis of which lender they think will approve their application, or that gave them a loan before (rather than the merits of the lender's product), or cause them to use lead generators).

9.238 We also note that borrowers may be discouraged from applying to multiple lenders by the perceived impact on their credit record.[744] If borrowers make multiple credit applications as a result of being declined by their first choice of lender, or if lenders offer variable pricing determined by a borrower's profile, the 'footprints' of these credit searches on a borrower's credit record may affect a borrower's ability to obtain a loan.[745] While this is not currently a significant impediment to customer search, it is likely to become a more pressing consideration for customers if our remedies succeed in removing or reducing other barriers.

9.239 We would expect that any measure that encourages lenders to help borrowers assess their creditworthiness and eligibility for loan products without leaving a footprint would thus support other measures aimed at addressing the barriers to search that we have found.

Remedy design

9.240 We set out below our consideration of issues relating to the design of this remedy:

- *(a)* In paragraphs 9.242 to 9.247 we consider the different ways in which customers may shop around and establish their eligibility for credit.
- *(b)* In paragraphs 9.248 to 9.254 we consider the scope for increasing the use of quotation searches, if they do not leave a 'footprint' on a customer's credit record, to facilitate shopping around.

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[744] See paragraph 6.62. See also TNS BMRB research with payday lending customers, p26.
[745] Wonga submitted (see Wonga response to Remedies Notice, paragraph 5.15) that the privacy policy on its website explicitly stated that 'large numbers of applications by a customer in a short period of time may affect their ability to obtain credit (whether their application has been accepted or declined)'.

(c) In paragraphs 9.255 to 9.256 we consider the scope for using standard credit scores as a means for communicating to customers their likelihood of obtaining credit from different lenders.

(d) In paragraphs 9.257 to 9.262 we consider other solutions which third parties (eg operators of PCWs) might develop to help customers shop around without adversely affecting their access to credit.

9.241 We discuss these matters in greater detail in Appendix 9.3.

Ways of shopping around and establishing eligibility for credit

9.242 We explored a variety of ways to ensure that borrowers could shop around easily and establish which lenders would offer them a loan and at what price without unduly affecting their ability to obtain credit.

9.243 We noted that each lender determines its own prices and pricing structure and designs a loan approval process that determines the types of borrowers to whom it will lend.[746] Lenders offering products at variable prices will, as part of this process, determine the different prices at which they will offer credit to different categories of borrower.

9.244 Each lender's decision on whether to offer credit will include a variety of considerations, such as the eligibility (eg by reference to a borrower's age, employment status, income), creditworthiness (eg by reference to a borrower's history of repayment of previous credit accounts) and affordability (ie whether a borrower is able to afford to repay the loan given existing debt or other commitments). For the purposes of this discussion we do not consider these individual aspects separately as they may be interlinked in a lending decision.

9.245 In addition to reviewing data they have collected themselves, lenders purchase information from CRAs. This may include data to verify a borrower's address, identity and income and also a customer's credit history. A request for credit information is referred to as a credit search. There are two main types of search conducted with CRAs which we refer to as an 'application' search and a 'quotation' search.[747]

9.246 We initially understood that the principal defining feature of a quotation search was that, other than *(a)* the lender requesting the search and *(b)* the CRA from which the lender requested the information, no third party was able to

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[746] See Appendix 2.4.
[747] Terminology used by different CRAs may vary and not all CRAs offer quotation searches.

see that the search had occurred. In contrast, we understood that an application search would be visible to any third parties that subsequently undertook a credit search.[748] This is sometimes described as leaving a 'footprint' on a customer's credit file.[749] In response to our PDR, Callcredit told us that quotation searches are excluded from the aggregated counts of searches used to build credit scorecards. They are visible to lenders conducting a relevant search, but clearly differentiated from credit application searches.[750]

9.247 Additionally, CRAs may also offer lenders a credit score for a customer that uses data collected by the CRA to indicate a customer's likely creditworthiness (though many lenders may use the underlying data provided by the CRA rather than its standard credit score).

Greater use of quotation searches

9.248 Both quotation and application searches report a borrower's outstanding debts and their repayment history. As noted, one significant difference between these two types of search (albeit not for all CRAs) can be that a third party[751] performing a subsequent credit search would be able to identify the number of recent application searches undertaken on an individual.[752]

9.249 We understand that most payday lenders use application searches (and other CRA products) but do not use quotation searches. However, quotation searches are used by some lenders that offer variably priced products (eg CashEuroNet[753]) to present the price at which they would lend to a borrower.

9.250 Currently, borrowers can shop around for a payday loan – subject to the limitations identified in Section 6 – by researching lenders online and/or on the high street. Such research can establish the prices of different loan products. However, without applying for a specific loan a borrower will not currently be able to establish if a particular lender will lend to them, or, if that lender has variable prices, the price (if any) at which the lender will offer a loan to them.

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[748] Credit searches will typically provide credit information relating to a defined period of time, and thus after a number of months or years these searches will cease to be included in the content of a credit search.
[749] We have found that this perception appears to be held by a number of consumer groups and websites offering advice on accessing credit (for example, see Which?: 'Your credit score explained').
[750] Callcredit response to the PDR.
[751] This could be a second lender or financial service provider (for example, lenders or insurers) that the borrower requests a quotation from or makes an application to.
[752] Some CRAs have told us that there is no difference in content between a quotation and an application search but others have said that an application search contains more information. Some CRAs have also told us that quotation searches are visible to third parties.
[753] CashEuroNet response to provisional findings and Remedies Notice, paragraph 8.10; CashEuroNet response hearing summary, paragraph 21.

Where a lender does not use quotation searches, any such application will leave a footprint.

9.251 Lenders and CRAs have told us that the presence of application searches on a customer's credit record is a factor in determining whether a lender will issue a loan.[754] One lender ([✂]) provided us with data on the relationship between the number of application searches and their acceptance rate[755] and the standard credit risk score provided by their CRA. Customers who had been subject to [✂] application searches in the preceding three months were significantly (around [✂]%) less likely to be accepted than those who had no previous application searches.[756]

FIGURE 9.4

[✂]

Source: CMA analysis [✂]
[✂]

9.252 In order to remedy the AEC that we have found, we are seeking to encourage customers to shop around. Consequently, we are concerned to ensure that borrowers who have shopped around to identify the cheapest loan available do not impair their subsequent ability to obtain credit.

9.253 We noted that if lenders replaced some or all application searches currently conducted with quotation searches, this would reduce or remove the risk of borrowers being penalised for shopping around. As some lenders already use quotation searches in this way to provide prices to potential borrowers at present we do not perceive there to be significant technical challenges to implementing this as part of the lending process. However, we were conscious of the fact that there is not consistency across CRAs in the relative visibility and content of quotation searches compared with application searches.[757]

9.254 We also noted that any lending decision based on the use of a quotation search would need to be provisional. We acknowledge that the presence of

[754] See Appendix 9.3 for details on the use of application searches.
[755] We use the indexed acceptance rate here to show the relative likelihood. The proportion of applications where there have been no previous credit searches that are accepted by [✂] is lower than 100%.
[756] This evidence is consistent with the view that, if shopping around increases the number of credit searches on customers' records, then this could create a barrier to access to credit in the short term. In the longer term we would expect lenders to adjust their assessment of the credit risk associated with the number of application searches a borrower has performed in the recent past to reflect the greater possibility that customers are shopping around, rather than seeking to access multiple sources of credit at once. This would mitigate the risk that customers would have their access to credit reduced, but, in the absence of the measures discussed in this section, would not remove it entirely.
[757] See paragraph 9.246.

an 'application search' on a customer's file can assist responsible lending by other lenders – particularly in circumstances where a customer has actually obtained credit from one lender – as it would provide a possible second lender with some reassurance at the point of application by a borrower that a loan may have recently been issued to the customer.[758] In addition, we were told that if having performed a quotation search on a potential borrower there was a delay before the customer decided to formally apply for a loan, a lender would need to conduct a subsequent application search in order to ensure that it was fully informed about the customer when issuing the loan.[759] Consequently a requirement on lenders always to conduct a quotation search would involve lenders incurring an additional cost for each loan issued.

Use of standard credit scores

9.255 While encouraging the use of quotation searches would reduce any impact of multiple credit searches, it would still require customers to apply sequentially to lenders until they found one which would offer them a loan. We considered whether lenders could indicate to customers a 'typical' CRA credit score above which they would be likely to lend to a customer. If customers knew their standard CRA score, they could then identify which lenders were most likely to lend to them.

9.256 We identified three main issues that would reduce the effectiveness of this approach.

- *(a)* First, lenders told us that they did not rely on standard credit scores and instead developed bespoke algorithms that analysed credit information to reach a lending decision.
- *(b)* Second, we identified that customers would need to obtain credit scores from the CRA(s) that the lender used, that there would be costs to the customer of doing this, and that in comparing two or more lenders, scores from other CRAs would potentially be necessary. Given the urgency involved when loans are taken out, we thought this would be impractical.
- *(c)* Third, we considered that even if there was a direct link between a standard credit score and the likelihood of acceptance on the grounds of creditworthiness, this might not be a reliable indicator of the likelihood of receiving a loan. This was because a lending decision would potentially depend on a variety of other eligibility and affordability criteria that were

[758] As the lender would see an application search on a borrower's credit file, even if the file did not show the new loan facility.
[759] That is that no loans or other credit activity had occurred between the quotation search and the point at which the application was made.

not factored into a credit score (for example, a borrower might have an excellent credit history but might not earn enough for a loan of a given amount to be affordable).

Other third party solutions

9.257 We considered the potential use of third party aggregators, such as those present in the personal loans market (and accessed through PCWs) which allow a customer to submit their details once and receive an indication of the likelihood of being offered credit.

9.258 One way that such facilities establish a customer's likely eligibility is the use of a quotation search combined with information provided by lenders on their lending criteria to the third party provider.[760] An alternative technical solution is one that is integrated into lenders' systems and operates using similar systems interfaces to 'pingtrees'[761] operated by lead generators.[762] A borrower's details are effectively shared with multiple lenders at once (although multiple lenders willing to lend rather than the highest bidder for that customer would be identified).

9.259 Our customer research indicated that there were varying levels of interest among customers about whether there should be an indication on a PCW of their likely eligibility[763] for a payday loan. Customers with good credit scores felt eligibility was irrelevant to them. Those with lower credit scores or experience of being turned down for loans in the past spontaneously raised eligibility as a useful feature.[764]

9.260 During our research we found that among inexperienced users in particular there was relatively low awareness of why understanding eligibility might be useful, and of the impact of credit searches. Once made aware of these issues there was a desire for them to be more widely publicised and customers were mostly willing to trade off the 'hassle' of entering personal information against securing an indication of the likelihood of approval.[765]

9.261 We considered that such services could assist both borrowers and lenders. However, we considered that requiring lenders to integrate with a specific third party provider might be disproportionate, either as a result of development costs or the requirement to share information on credit decision-making

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[760] For example HD Decisions or Pancredit Equiniti.
[761] Pingtrees are the auction mechanisms by which many lead generators sell leads to payday lenders and other third parties.
[762] See Appendix 2.7 for a description of pingtrees and their role in the lead generation sector.
[763] That is, likelihood of acceptance on any ground.
[764] TNS BMRB research with payday lending customers, p22.
[765] ibid, p26.

with a third party. In addition, it would be difficult to specify such a requirement given the fact that the underlying technology is still evolving.

9.262 We considered instead that operators of authorised payday loan PCWs in particular would have a strong incentive to develop and implement such solutions and that this could be a differentiating factor between PCWs and a driver of non-price competition between them.

Other issues

9.263 In response to the PDR, CFA noted that uncertainty about access to credit existed in all credit markets regardless of product.[766] We do not disagree with this point, but considered the evidence on the use of payday loans, namely the context of the perceived urgency with which they are taken out and (in some cases) repeat borrowing from the same lender meant that this was a particular issue in this market.[767] CFA also noted the relative bargaining position of lenders and CRAs and the potential for any remedy to affect competition between CRAs.[768] We considered these points. Our adopted approach reflects the potential implications of encouraging developments in CRA products. We also note that the products offered by CRAs to payday lenders are used by other credit providers, which is another reason why we have chosen to make a recommendation to the FCA in this regard.

9.264 Wonga told us that there was no compelling evidence that customers were choosing lenders based on whether they believed a lender would offer a loan.[769] We consider that as a result of our remedies package as a whole there will be greater and more effective shopping around by borrowers, both with respect to the ability to identify actual lenders and the ability to make informed and reliable price comparisons. We consider that a number of features in the market at present prevent this and we agree that customers do not shop around only on the basis of eligibility (though they may return to a lender on the basis of the greater likelihood of being offered a loan). However, not all borrowers will be accepted for all loans and borrowers should not be penalised solely for shopping around when trying to identify the cheapest loan.

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[766] CFA response to the PDR, p2.
[767] Perhaps because of the perceived increased likelihood of accessing credit from a lender that had previously issued a loan to that borrower.
[768] CFA response to the PDR, p2.
[769] Wonga response to the PDR, paragraph 4.9.

9.265 Wonga told us that there were risks from mandating quotation searches as application searches were a useful risk indicator.[770] However, as discussed below, application searches are used because of the uncertainty of a borrower's liabilities and loan performance (a point made by 118 118 Money[771]). Our recommendation to the FCA that further improvements to RTDS are needed means that the presence of credit searches on a borrower's credit file will become less significant. However, we recognise the risks identified by Wonga, and consider that the FCA is best placed to consider these issues.

Implementation

9.266 Given the AEC that we have found, and the focus of our remedy package, we consider it important that, by encouraging borrowers to shop around, our measures do not unintentionally prevent or reduce their access to credit.

9.267 The measures set out in this section can play an important role in supporting other elements of our remedy package, particularly in relation to PCWs, in developing a market in which payday loan customers are confident in shopping around for the best deal. A number of lenders and CRAs have indicated that there are potentially significant additional costs in requiring lenders to conduct a quotation search rather than an application search in the first instance. We are also conscious that the technology in this area is still evolving and that FCA guidance on the use of credit searches relates to all consumer credit, and we would not wish to add complexity to the regulation of consumer credit as a whole.

9.268 In light of the assessment above we have decided that the most appropriate way to address this particular aspect of the difficulty faced by borrowers when shopping around is to recommend to the FCA, having regard to our own findings, to work closely with relevant stakeholders to encourage initiatives, including greater use of quotation searches, to enable customers to search the market without adversely affecting their access to credit.

9.269 The evidence we have gathered indicates that there is little consistency in the availability, format and visibility of quotation searches for different CRAs. Therefore imposing a requirement to use quotation searches in their current format may not be a fully effective remedy to facilitate borrowers shopping around. However, because of their use in multiple credit markets we are not in a position to make recommendations on their content and use and consider it

[770] ibid, paragraph 4.12.
[771] 118 118 Money response to the PDR, p7.

appropriate for the FCA to lead in developing their use in this and other credit markets.[772]

9.270 Based on our analysis the following specific issues appear likely to merit further exploration by the FCA as part of any further work in this area:

(a) Whether the disclosures made to borrowers by lenders and intermediaries are sufficient in respect of (i) the point at which a credit check will be undertaken and its nature; and (ii) whether at the end of an application process a credit search has been performed and whether it has left a 'footprint' on the customer's credit file.

(b) Whether customers should be informed immediately prior to the point that a credit check is undertaken that one will be performed.

(c) Whether FCA guidance on the use of quotation searches should be revised to the status of a rule in situations where lenders introduce variable or risk-based pricing structures.

(d) Whether there is consistency in the availability, format and visibility of quotation searches and whether guidance to CRAs and lenders could be developed.

Measures to encourage development of real-time data sharing

Summary of remedy

9.271 Figure 9.5 summarises our recommendation to the FCA to continue to encourage the development and use of open, RTDS systems.

[772] We considered MAT's concern that if no progress was made by the FCA it was unclear what steps, if any, the CMA would take, however for the reasons stated we did not feel that we could prescribe specific action in this area given the potential impact on other credit markets. See MAT response to the PDR, p3.

FIGURE 9.5

Measures to encourage development of real-time data sharing

The CMA has decided to recommend to the FCA to continue to work closely with lenders and CRAs to encourage the development and use of real-time data sharing systems that are open to all payday lenders and other credit providers. This will address barriers to entry and expansion and support other measures to facilitate shopping around. Based on our analysis, the following specific issues are likely to merit further exploration as part of any further work in this area: *(a)* Developments in the supply and use of real-time credit information to ensure that customers are not penalised for shopping around, including the frequency that data is refreshed. *(b)* The sharing of credit information by payday lenders with more than one CRA. *(c)* The terms of access to real-time data-sharing schemes, to ensure that these do not act as a barrier to entry or expansion.

How the remedy addresses the AEC and/or resulting customer detriment

9.272 This remedy addresses a number of aspects of the AEC that we have found.

9.273 First, greater use of RTDS systems, and the further development of those systems, are likely to reduce the barriers to entry and expansion faced by new entrants (including those that operate in neighbouring markets) and smaller lenders in assessing applicants' credit risk. Because of their greater reliance on new customers and the value of previous experience in the credit risk assessment process, new entrants are likely to face some disadvantages in their ability to assess credit risk, which would put them at an initial cost disadvantage relative to more established providers.[773] Improvements in the quality of data shared through CRAs – including a reduction in the delay before such data is shared – is likely to reduce the extent of such disadvantages, and hence facilitate new entry and expansion.

9.274 Second, and building on the recommendations in Figure 9.3, further steps towards RTDS will reduce the risk that shopping around is misinterpreted by lenders as a sign of a customer seeking to access simultaneously multiple sources of credit, and so customers will not be penalised for shopping around.

[773] See paragraphs 7.77–7.107 and 8.6(a)(ii).

This will support other measures, in particular in relation to PCWs, aimed at making it easier for customers to search for the best-value loan for them.

Remedy design issues

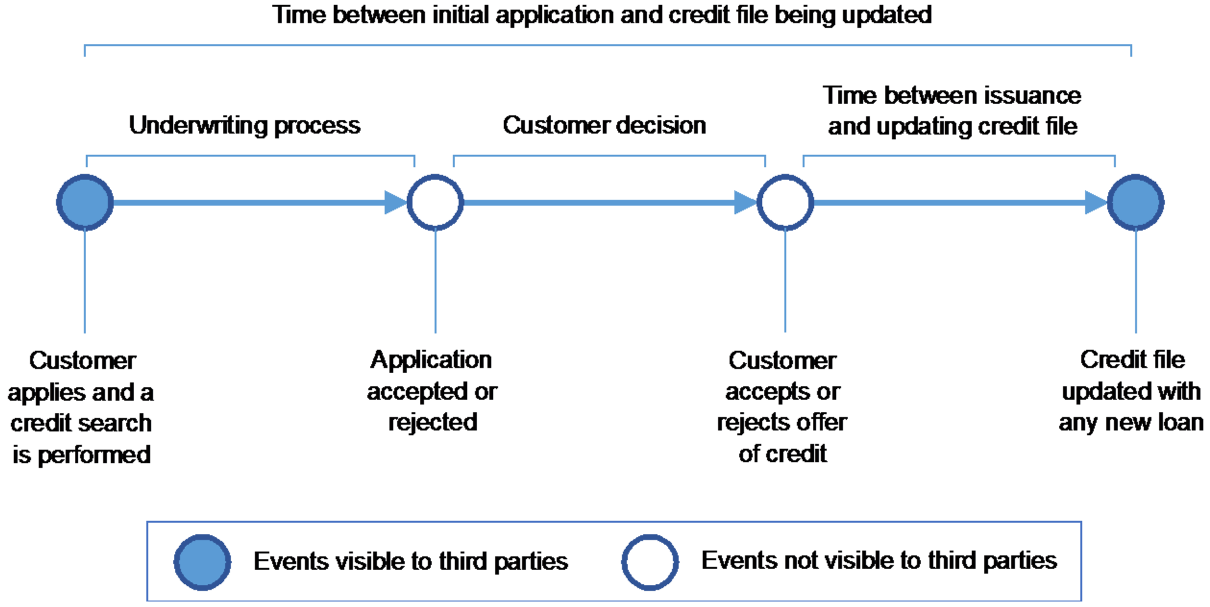
9.275 Until recently, CRA data has been updated on a monthly cycle, which in part has reflected many borrowers' traditional monthly cycle of salaries, credit cards and loan instalments.[774]

9.276 We have been told that the existence of a large number of application searches on a borrower's credit file is a risk factor in credit risk assessment. Having a large number of application searches can be seen to be an indicator of 'credit hungriness'.[775] This behaviour might in itself suggest that a borrower is experiencing financial problems and looking aggressively for credit. More fundamentally it provides evidence to a lender that a borrower has recently applied for (and has potentially been issued) credit. However, whether credit has actually been granted will only be known after the CRA update cycle and the credit search will therefore remain on the customer's record as a risk factor until a lender is satisfied a loan has not been issued.[776] The main stages of this process are shown in Figure 9.6.

[774] Individual lenders may have updated the CRA on a more frequent basis, but this information might have only been visible to third parties once the monthly update cycle had been completed.
[775] See Appendix 9.3, for discussion of this and Appendix 9.2 (paragraphs 126–139), for parties' submissions.
[776] If no loan has been issued the lender will also be unaware of why the loan has not been issued, either as a result of a rejected application or a customer's decision not to proceed with the offer of credit.

FIGURE 9.6

Visibility of credit decision-making



Source: CMA analysis.

9.277 Increasing the frequency with which lenders provide updates to CRAs and the frequency that CRAs in turn make that information available to third parties reduces the risk that a lender will issue a loan to a borrower without being aware that another lender has also recently issued a loan to the same borrower. 118 118 Money told us that the importance of application searches in credit risk scoring is because of the lack of RTDS on credit facilities and borrower repayment history and that credit searches are a poor proxy of a customer's liabilities and gave an indication of unknown but potential liabilities.[777] We agree with this point and we consider that further developments in the frequency of data updates and wider adoption of RTDS across credit markets would be beneficial.

9.278 The FCA has worked with lenders and CRAs to increase the frequency of data sharing with the intention that it will be 'real-time' and we noted in our PDR[778] that significant progress has been made over the past 12 months. At present the frequency of data updates in the existing and proposed real-time solutions offered by CRAs varies from near instantaneous to daily batch updates. We consider that the implementation of RTDS would assist lenders by reducing credit risk and assist borrowers by ensuring that lenders are not

[777] 118 118 Money response to the PDR, p7.
[778] PDR, paragraph 121.

deterred in offering them a loan as a result of the customer having shopped around for credit.

9.279 Because the availability of RTDS is likely to assist in the credit risk assessment of individual borrowers it is likely to assist lenders, particularly newer lenders who are more reliant on attracting new business, in reducing their overall costs relating to default. We also considered that any reduction in the costs of lenders, particularly new and/or expanding lenders, was likely to enhance competition.

9.280 We also saw benefits to competition in encouraging the greater sharing of data (in real time) with multiple CRAs.[779] Some CRAs told us that the proportion of payday lending credit agreements where information was shared with multiple CRAs was significantly lower than in more established credit markets. We considered that even where RTDS existed there would be some residual uncertainty whether or not a borrower had been issued with a loan, because a lender could not be certain that their CRA's dataset was complete. As a result lenders would incur greater costs in either obtaining credit searches from multiple CRAs for no certain benefit, or would reflect the increased credit risk in the price of credit. While we acknowledge the benefits to lenders and borrowers of sharing data more widely, we were concerned that a regulatory requirement to do so (and specifically requiring the sharing of data with all CRAs) could reduce the competitive dynamic of CRAs which may currently compete on the extent of their coverage of the market.

9.281 We identified a further risk that where CRAs seek to recover the costs of developing RTDS from lenders, the conditions for accessing the schemes, including the structure of fees, may act as a barrier to entry or expansion for new or smaller lenders. This is a particular risk when not all CRAs have a RTDS system in place, and lenders' choice of which CRA to use may therefore be driven by the extent of their coverage of the market. To protect their commercial position, established payday lenders may have incentives to share data as part of a 'closed' system, with a finite number of members, rather than one that is open to a wider variety of lenders.

9.282 We considered that competition would be enhanced to the benefit of borrowers through the sharing of credit information among CRAs and the development of RTDS systems accessible to all lenders in the market. Real-time data is an issue that the FCA is actively considering and we consider that

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[779] We note, for example, that the Government is promoting the sharing of business customer account information by banks through CRAs to enable small and medium-sized enterprises better access to finance. We also note that in the Home Credit market investigation the CC identified the competition benefits of requiring lenders to share credit information with at least two CRAs.

it is the appropriate body to ensure its continued development and availability to lenders.

9.283 Responses to this measure were broadly supportive. MoneySavingExpert.com saw improvements in data sharing as complementing the FCA's restrictions on rollovers[780] and MAT told us that a real-time database was a vital tool in helping to address the failures of payday loan lenders to conduct proper credit assessments of potential customers.[781]

9.284 CFA[782] told us that RTDS should be adopted by lenders in other markets. We can see benefits in improving the sharing of credit information, but we do not consider that our terms of reference or evidence base warrants a recommendation in this regard.

9.285 We discuss additional issues relating to the cost of accessing real-time data and the sharing of data with more than one CRA in Appendix 3.1.

Implementation

9.286 We noted the progress that the FCA has made in encouraging greater sharing of credit information with greater frequency. In its recent policy statement the FCA has stated that it did not propose to consult on introducing RTDS requirements at this time.[783] The FCA further stated that as part of its authorisation process it would be challenging lenders that were not using real-time data about the way they were conducting up-to date affordability assessments and would be seeking to maintain momentum in the market.[784] We also noted that RTDS systems are still evolving, such that there might be additional risks – eg of distorting competition between CRAs – if we were to seek to achieve the change in this area by imposing a prescriptive requirement on lenders by making an Order ourselves. We consider that further development of RTDS, specifically the frequency of updates, would benefit borrowers and lenders and that our recommendation is not redundant and is a proportionate response.

9.287 MYJAR (prior to the FCA's policy statement announcement) told us that the FCA's actions to date made this measure superfluous.[785] However, as

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780 MoneySavingExpert.com response to the PDR.
781 MAT response to the PDR, p3.
782 CFA response to the PDR, p3.
783 FCA, PS 14-16, p49.
784 FCA, PS 14-16, p52.
785 MYJAR response to the PDR, p2.

outlined below, we consider that there will be benefits arising from continued development in the availability and implementation of RTDS.

9.288 118 118 Money told us that there should be a regulatory requirement on CRAs to provide real-time data and for lenders to provide this data.[786] We agree that widespread adoption of RTDS would benefit the market, but do not consider that we have power to require CRAs to offer such a product, and thus we cannot compel lenders to use such a product. We also identified issues in requiring all CRAs to provide real-time data, as in addition to the largest three we are aware of a number of smaller CRAs which provide a more disparate range of products.

9.289 Some respondents to the FCA's consultation on the price cap and RTDS identified the need to improve the frequency with which lenders update CRAs to prevent multiple borrowing. In response to this criticism, the FCA undertook analysis and found that only 1% of loans are taken out with different lenders on the same day and that increased frequency of data updates was not necessary to prevent multiple borrowing. However, we consider that for the purposes of shopping around, as outlined in Appendix 9.3 improved frequency of data updates would benefit borrowers.

9.290 Given the above, we decided that a recommendation to the FCA to continue to pursue its work in this area, having regard to our own findings, particularly the benefits to borrowers of increased frequency of data updates, would be the most appropriate way to address the problems we identified.

9.291 We have therefore decided to recommend to the FCA to continue to work closely with lenders and CRAs to encourage the development and use of RTDS systems that are open to all payday lenders and other credit providers.

A summary of the cost of borrowing

Summary of remedy

9.292 Figure 9.7 summarises our remedy to require payday lenders to provide their existing customers with a summary[787] of the cost of borrowing on the settlement of a loan.

[786] 118 118 Money response to the PDR, p8.
[787] In our Remedies Notice we referred to a 'statement' of borrowing costs; we have chosen to use the term 'summary' to refer to proposed additional retrospective information provided to borrowers to avoid any confusion with any other statements which lenders currently issue to borrowers.

FIGURE 9.7

Obligation to provide customers with a summary of the cost of borrowing

The CMA intends to issue an Order to the effect that:

1. Lenders will be prohibited from providing payday loans to UK customers unless they make available to borrowers a summary of their borrowing history with that lender and inform borrowers of how to obtain this summary.

2. The summary will state:

    - for the borrower’s most recent loan with a lender: the initial amount borrowed, details of all payments made in relation to that loan and the total amount of all fees and charges made in relation to that loan;

    - the total amount of fees and charges paid by the borrower to the lender and the additional cost incurred as a result of late or partial payment in relation to all loans taken out during the 12-month period preceding the date of the borrower accessing the summary;

    - how borrowers can access more detailed information on their loans; and

    - the web address of one or more authorised payday loan PCWs or a portal listing all authorised payday loan PCWs.

3. A lender is required to make the summary available when:

    - a borrower settles the balance of a credit account; or

    - where a borrower’s account is closed as a result of default or forbearance.

4. A lender is required to notify the borrower of the availability of the summary as soon as practicable and at the latest within one bank working day of either event described in point 3, with the exception of high street premises which are closed on the given day.

5. The summary shall be made available to borrowers according to the method that the loan was issued:

    - Where the settled loan was issued online: the summary shall be available on the lender’s website (through a personal account management function), or by email if requested by a borrower at the time at which an application is submitted or loan issued.

- Where the settled loan was issued from high street premises: the method of distribution should be chosen by the borrower at the time at which the loan is issued. A high street lender must offer borrowers the opportunity to receive the summary in a durable medium in-store (such as paper) but may choose additionally to offer access via post, its website (through a personal account management function) or by email.

6. Where the summary is not distributed directly by a lender to the borrower, notification of the availability of the summary should be according to the preference of the borrower at the time of application.

7. Lenders should take all reasonable steps to bring the summary to borrowers' attention. To demonstrate this, before an existing borrower commences a further loan application process with a lender, the lender should request that a borrower confirms that they are aware that they have had the opportunity to access the summary issued following the conclusion of the borrower's most recent loan with that lender. At the point of this confirmation, a link should be available for the borrower to access the summary, or, for high street lenders, borrowers should be reminded of the availability of the summary.

8. The obligations placed upon lenders under requirements 1 and 7 above will exist for a period of 12 months after the date the loan is settled.

9. We also propose to recommend to the FCA that it supports the CMA in monitoring compliance as part of its routine supervision of authorised lenders, to the extent that its powers allow.

How the remedy addresses the AEC and/or resulting customer detriment

9.293 This remedy, which is particularly targeted at repeat borrowers, contributes to addressing a number of aspects of the AEC, by:

(a) making customers aware of, and encouraging them to consider, the full costs of their last loan (and other recent loans) including late fees and other additional charges before they are able to apply for a further loan from the same provider;[788] and

[788] We found that 11% of respondents to our survey reported not having looked at information on the total cost of their most recent loan, and that around a third of customers had not looked at the costs they would incur if they did not repay a loan in full on time (see paragraph 6.95).

(b) increasing the likelihood that repeat borrowers will shop around by providing links to authorised payday loan PCWs.

9.294 We have observed that many of the occurrences of borrowers changing lender are likely to have taken place as a result of borrowers being constrained in their ability to return to their previous lender for additional credit (rather than as a result of shopping around).[789] We further found that repeat borrowers may be dissuaded from looking at alternative suppliers by the perceived risk and loss of convenience associated with changing lender.[790]

9.295 A retrospective summary of borrowing costs would have the effect of drawing borrowers' attention to the costs that they have incurred in relation to their most recent loan and the cumulative costs of borrowing from a lender over a period of time. As a result we would expect borrowers to give greater consideration to the price they pay for payday loans and that this would encourage some customers to consider alternative offers, rather than simply returning to the same lender for additional credit.

9.296 The inclusion of a reference in such a summary to one or more authorised payday loan PCWs would further promote shopping around by repeat borrowers. As explained in paragraph 9.14, PCWs provide an environment where borrowers are able to compare numerous lenders easily and quickly, and identify the best-value offer for them. By reminding customers in a timely manner of the cost of borrowing from their current lender and providing them with easy access to tools with which to make effective comparisons with other lenders, this remedy will help customers identify the potential benefits of switching and make it more convenient to move to another supplier.[791]

9.297 We also found that some borrowers had a tendency to be overconfident when assessing their ability to repay loans on time.[792] Because of this, borrowers may not factor additional fees and interest charged for late payment into their assessment of the cost of a loan when choosing a lender. We considered that a retrospective summary of borrowing costs could assist borrowers in understanding the actual cost that they had incurred and, when compared with the amount they expected to repay, would improve customers' awareness of the possible costs associated with late repayment. In conjunction with the use of a

[789] See paragraph 6.44.
[790] See paragraph 6.120.
[791] We are aware of the MiData initiative led by the Department for Business, Innovation & Skills and HM Treasury that will allow consumers to download data on their personal current account usage in a standard format to use on a PCW. This is a voluntary scheme for banks. Those banks participating will make data available to consumers from April 2015.
[792] See paragraph 6.96.

PCW, we considered that customers would be more likely to review the relative late fees of loans with a similar headline rate.

Remedy design

9.298 The principal design issues relating to a requirement to provide existing payday loan customers with a summary of the cost of borrowing that we identified were:

(a) the content of the summary including the period of historical borrowing;

(b) the trigger point for the availability of the summary;

(c) the method of distribution of the summary;

(d) ensuring borrowers receive and have the opportunity to review the summary; and

(e) using the summary to encourage borrowers to shop around.

9.299 We reached our decision by considering all of these aspects of remedy design together, but for clarity discuss each aspect in turn. We discuss the issues relating to the content of the summary in greater depth in Appendix 9.4 and we present an example of how this might be presented in that appendix.

Content of summary

9.300 We considered that there was a balance to be found in making any summary both accessible and informative. The content of the summary should be sufficient to make borrowers aware of the total cost of their borrowing and the costs arising from late payment or default, but should it not contain unnecessary or confusing information that might reduce customer engagement.

9.301 To achieve this balance, we considered that a summary of borrowing should consist of information relating to *(a)* the loan that had just been repaid, and *(b)* details of borrowing over a preceding period. The remedy would thus need to specify the level of information provided on both aspects and the appropriate time period to be covered by the summary. To encourage shopping around, the summary should also include a link to one or more authorised payday loan PCWs (see Figure 9.1).

9.302 The CFA told us that while it thought requiring lenders to provide a summary of the cost of the most recent loan was sensible, the proposal that every summary should also include information from the last 12 months was more difficult to justify.[793] The CFA and MYJAR characterised this as a rolling 12-month summary.[794] MYJAR considered that providing this information could be confusing and patronising.[795] We considered the characterisation of the summary as a rolling summary was true for the very heaviest of payday borrowers who return to the same lender repeatedly.[796] However, given the features in the market that we have found, we do not perceive the points raised to be an issue. The ability to understand the cost of borrowing resulting from a borrower's actions (and particularly over the medium term) is important in assisting borrowers to make appropriate choices and understand their own credit needs. Conversely for infrequent borrowers (with a particular lender) the summary may contain only their most recent loan.

9.303 The CFA and MYJAR also compared our requirement to requiring a credit card customer to receive a rolling annual statement and be required to confirm they had read it before they could use the credit card for their next purchase.[797] We did not consider this to be a valid comparison given the difference in the nature of the products and we did not consider the burden on payday lenders to be onerous.[798] However, we have amended the wording of the remedy to clarify that a borrower needs only to confirm that they are aware that they have had an opportunity to review the summary.

9.304 We noted the points raised by Dollar with respect to the consolidation of borrowing costs from different products and channels. We were concerned that requiring only the cost of borrowing from a single product to be included could result in gaming by lenders who might introduce 'new' products, which differed in non-material ways.[799] Dollar noted the difficulty of integrating different systems for different products, particularly those which had been withdrawn. We thought the impact of this would be mitigated through two factors: first, the summary requires only a summary of costs incurred in the preceding 12 months, which will limit the number of legacy systems that would require integration or one-off data extraction;[800] and second, this remedy

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[793] CFA response to the PDR, p3.
[794] ibid, p3; MYJAR response to the PDR, paragraph 5(b).
[795] ibid, paragraph 5(b).
[796] Other borrowers would only receive a summary of the cost of their borrowing as frequently as they took out loans.
[797] CFA response to the PDR, p3; MYJAR response to the PDR, paragraph 5(a).
[798] We did not consider this to be a valid comparison for the following reasons: firstly, a credit card is an open-ended credit facility, whereas a payday loan is for a specific amount of interest-bearing debt and each loan is subject to a separate credit agreement. Secondly, the nature of a credit card is such that if the balance of the debt is paid off in full, there will be no charge to the borrower and that other than where a credit card is paid in full by direct debit the balance of the account and any interest incurred will be sent to a borrower on a monthly basis and payment of the balance will implicitly require an appreciation of the cost of the loan.
[799] The specific risk we identified was that one small aspect of the terms and conditions for a given product could be amended and/or the product renamed to justify the exclusion of other products.
[800] Any products phased out more than 12 months ago would thus not need incorporating into a summary. Given the nature of products on offer it is unlikely that any customer would continue to be repaying such a product,

would only come into effect after the CMA issued an Order which we would expect would include transitional provisions on which we would consult. Therefore any future system could be designed to incorporate our requirements.

9.305 We considered which products should be included when a single group included a number of distinct brands, lending entities (which held their own credit licences) and lending channels. We considered that lenders should take account of the following in deciding whether borrowing costs of different loans should be included in aggregate:

(a) Whether the loan was issued under the same FCA authorisation/ consumer credit licence.

(b) Whether the loan was issued under the same brand or by the same legal entity.

(c) Whether loan performance data from a previous loan was used in the decision to issue the current loan, other than where this was taken from a CRA.[801]

(d) Whether the loan was issued through the same channel or portal (such as a website and the underlying customer account management system).

9.306 Dollar raised two principal issues with respect to the 12-month period of the summary:

(a) First, relating to the cost of implementing the remedy. Dollar told us that, to ensure that the summary was accurate, a static version of the summary would need to be created at the point at which the final repayment was made. This static summary would then need to be stored for 12 months. As a result Dollar told us that it would potentially incur significant additional costs in establishing a data warehouse facility and ongoing storage and thus the remedy was disproportionate.[802]

(b) Second, commenting on the relative utility of the summary under different specifications of the 12-month period. Dollar told us that providing

unless they had agreed a debt management plan and less likely that any customer with a debt management plan would be issued an additional loan by a lender.

[801] We considered that if lenders were sharing customer data between operating units in their lending decisions (and which a third party lender would not have access to in the same level of detail) it was an indication that the operating structures overseeing products were related.

[802] Dollar told us that the information held on its personal account management sites was constantly updated in order to reflect the most recent position for that customer. To generate the summary as described in our PDR it would be necessary to create and electronically store the summary, which would incur significant data warehousing costs. A more practical solution for Dollar would be to generate a summary of the preceding 12 months at the point of access. (See Dollar response to the PDR, paragraph 7.5(ii).)

information to a borrower relating to the 12 months immediately preceding the point at which the summary was reviewed would ensure that an up-to-date snapshot of a borrower's position at the time the summary was reviewed.

9.307 We were concerned to ensure that our remedies should be no more onerous than needed to achieve their aim. For this reason we consulted on amending the specification of the 12-month period in our additional consultation and sought views on whether this would affect the costs of implementing the remedy and its effectiveness in remedying the AEC.

9.308 CashEuroNet did not agree with linking the period of the summary to the date of settlement as it did not allow cost comparison. It proposed that an annual summary should be issued by all lenders on the same date, to facilitate comparison and said that this would be simple for lenders to implement with lower compliance costs and greater quality assurance.[803]

9.309 The CFA told us that under the price cap, loans would be at uniform cost, reducing the utility of the summary. Amending the 12-month period would reduce data storage costs.

9.310 In responding to our consultation Dollar reiterated the points made in its response to the PDR about ease of comparison, timeliness of information and cost and further added the need to allow a suitable period (a minimum of 12 months) to allow lenders to implement the remedy.[804]

9.311 MAT did not think that borrowers would either read or understand the summary so would not be affected. MAT considered that information on alternative forms of credit and debt advice should be provided instead.[805]

9.312 Which? told us that the remedy as originally drafted would better achieve our aims, but that consumer testing might be needed.[806]

9.313 Wonga agreed that amending the period of the summary might assist customers in understanding the cost of their borrowing over time by making it easier to aggregate information from different lenders. It told us [✂].[807]

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[803] CashEuroNet response to the proposed remedies consultation, paragraphs 3.1–3.5.
[804] Dollar response to the proposed remedies consultation, paragraphs 2.3–3.1.
[805] MAT response to the proposed remedies consultation.
[806] Which? response to the proposed remedies consultation, p4.
[807] Wonga response to the proposed remedies consultation, paragraphs 3.5 & 3.6.

9.314 CFA said that the benefit of the remedy would be diminished under the price cap.[808] We disagree. It will continue to inform borrowers of both the cost of individual loans but also their borrowing in aggregate and the costs of late payment. We considered that if borrowers are able to consider their borrowing over the medium term they would be better placed to anticipate their future need for credit[809] and be aware of the tools available to assist in shopping around and finding the most appropriate credit product.

- *Decision on the content of the summary*

9.315 We concluded, with respect to the borrower's most recent loan, that a summary should include:

(a) The initial amount borrowed.

(b) The original duration of the loan or the facility.

(c) Details of any subsequent increase in the amount borrowed or the duration of the loan.

(d) An account of whether payment was received in full and on time or whether partial or late payment was received. Where the loan was repaid in multiple instalments, the summary must contain details of the number of instalments where the borrower either did not make the agreed repayment or payment was late.

(e) The amount of:

(i) fees and interest charges relating to the original loan or credit agreement;

(ii) any fees or interest charges arising from rollover or extension of the loan;

(iii) any fees or interest arising from late payment or default; and

(iv) the total of (i) to (iii).

(f) A summary of any costs accrued but not paid as a result of default or forbearance.

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[808] CFA response to the proposed remedies consultation.
[809] Where the individual is able to access other forms of credit which may require a longer period for an application to be processed and credit to be available, understanding the ongoing nature of credit usage may act as a prompt to consider using those other forms of credit.

9.316 We have considered the responses to the PDR and to our consultation. Only one party, Dollar, raised concerns that the definition of the 12-month period in the PDR would prove difficult to implement. Two other large lenders were neutral on the cost of implementation. We recognise there could be benefits with respect to the ability to aggregate the cost of loans and in providing timely information.

9.317 We considered the evidence submitted and concluded that borrowers could obtain significant benefits from having access to timely and relevant information which would be more readily aggregated with information from other lenders. For this reason we have chosen to amend our remedy such that the summary should include the relevant 12-month period preceding the point that the summary is accessed by the borrower. Given the importance of repeat borrowing in this market, we considered that information about cumulative borrowing costs over a 12-month period could represent a significant amount of money and that awareness of this would help emphasise the potential benefits of shopping around.

9.318 As a borrower may have taken out a number of loans from the same lender over this period we were conscious of the need to ensure that borrowers were readily able to absorb and reflect on their past borrowing. We therefore concluded that a summary of this 12-month period should include:

(a) the number of loan or credit agreements in place over the course of the 12-month period preceding the date that the summary was accessed;[810]

(b) the total amount of fees and charges paid during this period; and

(c) the total amount of fees and charges incurred as the result of late or partial repayment during this period.

9.319 Where no other loans had been outstanding at any point in the preceding 12-month period we considered that a simple statement to this effect would be sufficient.

9.320 Lenders should not be constrained by this remedy from providing more detailed historical information on loans to borrowers in addition to the summary.

[810] We consider that the specific definition of the relevant 12-month period should be determined by the lenders, and depending on their systems could be 12 calendar months, 52 weeks or 365 days.

Trigger point for making the summary available to borrowers

9.321 We considered what would be the most effective timing for providing any summary. We identified two principal options:[811]

(a) time-based or periodic: the availability[812] of a summary determined on a standard cycle for all lenders with which a borrower has had a credit facility in a defined period; and

(b) event-based: the availability determined by a borrower's activity with a given lender.

9.322 We identified a periodic summary (that is, one sent out at regular intervals) as a possible remedy in our Remedies Notice. We noted that requiring all lenders to distribute summaries at the same time of year had the potential benefit of ensuring that borrowers who used multiple lenders would be able to establish an overview of the cost of their borrowing activities with all lenders. This could reinforce the message to such customers that it was worth shopping around, given the cumulative cost of borrowing. CashEuroNet proposed that an annual summary should be issued by all lenders on the same date (paragraph 9.308).

9.323 Having reviewed the responses to our Remedies Notice and the results of our customer research[813] we considered that the information contained in periodic summaries would not necessarily be perceived by customers as timely (that is, they would not be aligned to customers' borrowing behaviour) unless summaries were sent out with great frequency. This would reduce the impact of this remedy on borrowing behaviour and hence reduce its effectiveness. We therefore considered that the benefits arising from the alignment of the dates of summaries from multiple lenders were unlikely to exceed the diminished timeliness of the summaries. For the reasons outlined above and based on submissions received in response to the Remedies Notice[814] and our customer research[815] we therefore considered that a periodic summary would not be timely or as relevant to a borrower's behaviour, and that the average borrower may have taken out a number of loans before having access to a summary of the cost of borrowing.

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[811] We also considered the development of a regulatory database of loan information to allow a single summary to be produced. However, we discounted this as requiring significant development costs and was thus likely to be disproportionate.
[812] In our PDR we referred to the point at which the summary would be distributed. We now refer to the point at which the summary is available, as lenders providing a web based summary would not be distributing the summary itself but notification of its availability.
[813] TNS BMRB research with payday lending customers, p42; Appendix 9.2, paragraphs 177–217.
[814] For details of submissions see Appendix 9.2 (paragraphs 177–217).
[815] TNS BRMB Survey Report.

9.324 In our view making the availability of the summary event-driven would ensure that availability (and notification of the availability) of the summary was driven by the behaviour of a borrower and would thereby maximise the likelihood that the summary would be available in a timely manner and be perceived as relevant. By having a summary available at the point of settlement of a loan, a borrower would be better able to associate the impact of their behaviour (for example, with respect to timeliness of payment) for that specific loan with the cost of that loan. In addition, making a summary of previous borrowing costs available at the conclusion of a loan would help counteract any tendency for over-confidence by a borrower.

9.325 In response to our PDR, CFA[816] and Dollar[817] reiterated a concern that the automatic notification of the availability of a summary would be considered as unwanted contact from a lender. This was also a view expressed by some participants in our customer research.[818] However, we consider that informing borrowers of the cost of their most recent loan and cumulative borrowing is an important aspect of understanding which credit products would be most appropriate and in comparing the available products. To reduce the likelihood of the notification of the availability of the summary being perceived as unwanted, it should not include any promotion of the lender other than its name, contact details and information on accessing the summary (if not distributed by email). Any page linked to, from a notifying email, and the summary itself should not include reference to taking out a further loan.

9.326 We further considered that making the notification at the point at which a loan is settled closely links this notification to a borrower's actions and is consequently a reasonable and understandable contact from a lender.

9.327 We considered whether there should be a time limit by which point a summary should be made available. We identified that the method of payment would determine the lender's ability to confirm receipt of funds.[819] We expect that in the majority of cases a summary could be made available when payment is made.[820] However, we acknowledged certain manual processes and the need to allow funds to clear overnight might cause a delay between payment being taken and this being recognised by a lender's systems. We concluded that the summary should therefore be available as soon as possible and at the latest

[816] CFA response to the PDR, p3.
[817] Dollar response to the PDR, paragraph 7.5.
[818] TNS BRMB Survey Report, p40. The research found that 'initial reaction to the idea of receiving a statement of borrowing were negative or neutral, as customers recognised it could be uncomfortable or distressing to confront their spending'.
[819] Where payment is made online or in store we did not consider there to be any reason that a summary could not be made available at the point of settlement, even if funds had not cleared.
[820] Particularly where a customer has actively made a payment such as by making a payment in cash or chip and pin transaction in store, or debit card online.

within one bank working day of settlement of a loan or credit facility. Where high street premises are closed on the day a loan is settled, we concluded that the summary should be available on the next working day.

- *Decision on trigger point for summary*

9.328 For the reasons outlined above we concluded that the summary should be made available when a loan is settled or an account closed as the result of forbearance. It should be available within one working day of the repayment of a loan or closure of an account (other than where a store is closed on a given day). For the reasons set out in paragraphs 9.300 to 9.320, it should cover the loan that has been repaid and the costs of borrowing with that lender over the 12 months period preceding the customer accessing the summary.

Method of distribution

9.329 We considered how best to distribute the summary to borrowers. We identified three main potential channels:

(a) post,

(b) email; and

(c) lenders' online personal account management system (ie a web interface from the lenders' website that is linked to a borrower's account).

9.330 We set out our detailed consideration of each method of distribution in Appendix 9.4. We identified issues with respect to the constraints of SMS message length, the cost of distribution by post and the possibility of messages being mistaken for 'junk mail' or 'spam' email by recipients and thus dismissed. We considered that using online lenders' existing personal account management facilities would be a cost-effective and secure channel that built on the way in which customers currently engage with their lenders.

9.331 We considered the possibility that lenders operating from high street premises (and potentially some smaller online lenders[821]) may not have any online personal account management functionality. Mandating the use of an online portal to deliver the summary may require significant development costs for these lenders, and would thus be potentially disproportionate. Furthermore, customers borrowing from high street premises may be less likely to be comfortable using an online account management function, should one be

[821] However, we are not aware of any online lenders that do not create an online account into which returning customers may log in.

available, and hence may be less likely to view a summary on a lender's website.

9.332 We were conscious that while online borrowers would have internet access, or access to email, the same assumption should not be made for high street borrowers. Therefore we considered that high street borrowers should always be offered the ability to receive the summary in hard copy, but where the lender's lending platform allowed the generation of automated emails, or a web portal, this could be offered as an alternative.

9.333 We further considered that where a summary is not distributed directly to a borrower at the relevant trigger point (for example, because the borrower needs to come in-store, or visit a website) that the offered means of communicating the availability of the summary should be appropriate for the way in which the loan was issued.

9.334 We considered that it would generally make sense for online borrowers to be informed by email of the availability of a summary, though other channels such as SMS might also be used. We considered that the most appropriate means of contacting high street borrowers was likely to vary according to how lenders normally kept in touch with existing customers. As such, we considered that high street lenders should be able to choose their preferred method of communicating that a summary was available (eg by post or email), provided that this was through a medium appropriate to the customer in question (consistent with the way in which other important messages were communicated to the customer). We further considered that where a high street borrower settled a loan in-store, that notification in-store could be used.

- *Data protection and security*

9.335 We identified a number of potential data protection and security issues with respect to distributing summaries of payday loans usage. Principally these related to the potential for fraud or identity theft and the social sensitivity associated with using payday loans.

9.336 We were told that these issues could arise, in part, because of the transience of borrowers which meant that lenders could not be certain that a borrower's contact details would remain correct for any extended period of time.[822] Because of this we considered that there were particular benefits of the

[822] Dollar noted that its customers were often transient (Dollar response hearing summary, paragraph 38).

summary being presented through an online personal account management system, where this is available.

9.337 We noted the CFA's concern for high street borrowers who may not have internet or email access.[823] We agree with this point and have clarified the wording of the summary of this remedy to make it clear that for high street borrowers it should be their choice how to receive the summary; lenders could offer online access, but are not compelled to do so.

- *Decision on method of distribution*

9.338 We decided not to require the distribution of a summary by post because of the potential cost of administration and because it would provide little or no additional benefit in terms of effectiveness relative to other channels. However, we considered that high street borrowers should be able to choose to be provided with a hard copy of the summary.

9.339 Because of data protection and security concerns we considered that requiring a summary to be sent by email may not always be appropriate (individual lenders would be best placed to decide), and we considered that SMS was not a practical or reliable way of communicating this information, though it could be an appropriate means of communicating that a summary was available.

9.340 We therefore decided that for online borrowers the summary should be presented using a lender's online account portal (where such a portal exists).[824] The availability of the summary should be communicated to online borrowers by a method that is consistent with the way in which other important messages are communicated to the customer (eg email, SMS).

9.341 We concluded that borrowers whose loan has been issued from high street premises should also have the opportunity to review the cost of their borrowing. As it was less likely that high street borrowers would be regular users of lenders' online account management functions, we concluded that greater flexibility should be allowed to high street lenders to find appropriate and cost-effective ways of delivering the summary and informing the customer of its availability. For example, some high street lenders might choose to inform customers (eg by email or SMS) that a hard copy summary was available in-store on request or, alternatively, automatically distribute a summary by post or email, once a loan has been repaid. High street lenders

[823] CFA response to the PDR, p3.
[824] As noted above, we are not aware of any online lenders that do not create an online account into which returning customers may log in.

may also choose to make the summary available through the same methods as online lenders, where this is consistent with the way in which they normally communicate important information to the borrower.

9.342 We have revised the wording of the remedy with respect to the distribution of a summary by high street lenders to make clear our expectation that any distribution by email to high street borrowers would be by automated email and not in response to an ad hoc request.

Ensuring borrowers have had the opportunity to receive and review the summary

9.343 We considered ways to ensure that borrowers had had the opportunity to review the summary before taking out a subsequent loan.

9.344 We considered that requiring the summary to be displayed in an online lender's account management system would allow a remedy to be designed that required the summary to be presented to a borrower when they logged on, regardless of the method by which, or point at which, a borrower chose to access the lender's website. We initially considered that a simple confirmation button or tick box could then be clicked to allow the borrower to acknowledge that they had reviewed the summary. This might occur at any point after the customer had been informed that a summary was available.[825] However on further consideration we decided that it was not appropriate to require borrowers to declare that they had read the summary. We decided that it would be more appropriate for borrowers to declare that they were aware of the opportunity to review the summary.[826]

9.345 In relation to high street borrowers, we initially considered that it would be similarly practicable to ask returning customers, when taking out a subsequent loan, whether they had received and reviewed the summary relating to their most recent loan with that lender. Where this had not occurred (and where a customer had not previously requested a summary from the lender), a copy of the summary should be presented to borrowers for review before any further loan is be taken out. To demonstrate that the summary has

[825] We noted that returning online borrowers applying for a new loan may for a number of reasons not use the same account as previously (perhaps as the result of forgotten login details). In such circumstances we identified that a borrower on creating an account might not be associated with previous loans and would not be requested to review a summary. Given the extensive use of CRA data for confirming identity we judge it unlikely that a lender could issue a loan to a previous borrower without identifying their previous loan relationship, unless there was a significant period of time (perhaps two to five years) since a previous loan had been issued. We consider that lenders will be best positioned to consider how to ensure their systems identify such an eventuality and how to ensure that borrowers are shown a summary of their borrowing history prior to an additional loan being taken out.
[826] We note responses to our consultation in this regard in paragraph 9.347.

been received, a signed[827] declaration should be recorded by the lender, either when a customer requests the summary or before a subsequent application starts. As discussed above in paragraph 9.344, we reconsidered this requirement, and considered a question asking if borrowers were aware of the opportunity to review the summary would be more appropriate.

9.346 In paragraph 9.336 we noted that certain borrowers may change their contact details on a regular basis. By using a web portal, or presenting borrowers with a hard copy of the summary (eg in-store), borrowers were more likely to have received or had the opportunity to review the summary before taking out their next loan. Provided the summary is appropriately concise, this would enable borrowers to review the content of the summary before deciding whether or not to take out a loan with their existing lender. However, while we consider that there should be an opportunity to see the summary when making a subsequent application, it would not be necessary for the lender to provide it unless the borrower was unable to make the declaration outlined in paragraphs 9.344 and 9.345. Should the borrower state they were unaware of the opportunity to review the summary, the lender would be required to provide access to the summary. We provide an example of how a summary might be displayed online in Appendix 9.4.

9.347 In response to our PDR the CFA told us that it would be entirely disproportionate for lenders to be required to prove that customers had actually read the summary.[828] We do not consider that lenders should be required to prove this, rather our intention was that lenders would be required to document that borrowers confirm that they have had the opportunity (in that a summary was available) to review the summary. As explained in paragraphs 9.344 and 9.345 we have therefore amended the wording in the summary of this remedy to make this clearer. MYJAR told us that it did not consider this requirement to be proportionate, particularly given that it did not apply to other credit markets and was unfair and patronising to payday customers to make this confirmation.[829] We disagree with MYJAR in this respect. As discussed in paragraphs 9.293 and 9.297 this requirement has been included specifically because of the features in this market that we have identified and we further note that under other forms of consumer credit any additional period of borrowing is part of the use of an open-ended line of credit, and not a separate credit agreement as is the case with a payday loan.

[827] An electronic signature or affirmation incorporated into the loan application would be acceptable subject to the lending process adopted in-store.
[828] CFA response to the PDR, p3.
[829] MYJAR response to the PDR, paragraph 5(a).

- *Decision on ensuring customers have had opportunity to consider the summary*

9.348 To ensure that this remedy is effective, it is important to maximise the likelihood that customers read and engage with the summary. We expect lenders to take all reasonable steps to ensure that borrowers have the opportunity to review the summary, by ensuring that borrowers are made aware of its availability in a timely manner. We have decided that lenders should obtain confirmation that the borrower is aware of having the opportunity to review the summary issued following the conclusion of the borrower's most recent loan before that lender allows the borrower to start an application for another loan. We have indicated above how online and high street lenders might go about obtaining such confirmation.

Using the summary to encourage shopping around

9.349 We considered that providing a summary of borrowing costs would in itself stimulate interest in the cost of borrowing and potential alternatives. However, we also noted that those borrowers who were stimulated to consider the cost of borrowing would not necessarily know how to find a more appropriate loan and that this could limit the remedy's impact in encouraging shopping around. We therefore considered that including a hyperlink to one or more authorised payday loan PCWs on the summary of borrowing costs would enhance the remedy package as a whole by helping borrowers to compare lenders' offers and potentially find a more suitable loan. This would reinforce the impact of the obligation on lenders to include hyperlinks to authorised payday loan PCWs on their own websites (see paragraphs 9.122 to 9.128), by increasing the number of occasions where customers are invited to shop around and the variety of points at which this information is presented to them.[830]

9.350 Wonga told us that requiring the inclusion of a hyperlink was disproportionate given that a hyperlink would be displayed on the lender's main website prior to the commencement of any application.[831] As lenders have the potential to distribute the summary by email and noting that a borrower might not return to a lender's website subsequent to reviewing the summary, we considered that making borrowers aware of the existence of an authorised payday loan PCW was appropriate, as it would further encourage borrowers to consider

[830] For example, some existing customers might be prompted to visit a PCW having looked at a summary on conclusion of a previous loan, while others might be prompted by the disclosure on a lender's website when taking out a subsequent loan. Repetition of this information in different stages of the customer's borrowing experience may also reinforce its impact on customers.
[831] Wonga response to the PDR, paragraph 3.12.

shopping around. Furthermore, linking the availability of PCWs to the act of reviewing the costs of borrowing was a useful aspect of the remedy.

- *Decision on using the summary to encourage shopping around*

9.351 We have concluded that the summary should include a short reference to the existence of authorised payday loan PCWs and that online lenders will also be required to include a hyperlink to one or more authorised payday loan PCWs on which the lender publishes details of its products and/or a list of all authorised payday loan PCWs.

9.352 Given our decision not to require high street lenders to publish details of their loans on a PCW, we considered the requirement for a high street lender to make reference to the availability of PCWs. It was also important to ensure that high street lenders did not 'game' the system by choosing a PCW on which they did not appear, but which consisted of expensive products offered by other lenders that made its own products appear to be relatively cheap. Therefore we conclude that for high street lenders, the summary should include either the URL of a portal listing all authorised payday PCWs or an authorised payday loan PCW that publishes details of its products. Where a portal containing a list of authorised payday loan PCWs does not exist and that lender's product details are not available on a PCW, a high street lender should include the URL of an authorised payday loan PCW. We consider that high street lenders should make their choice of this PCW with regard to the FCA's Principles for Business.[832]

Implementation of remedy

9.353 We have decided to implement this remedy by using our statutory Order-making powers. We therefore intend to issue an Order prohibiting lenders from providing payday loans to UK customers, unless borrowers are provided with a summary of their recent borrowing history with that lender and unless the lender has taken all reasonable steps to bring the summary to borrowers' attention. To achieve this, before an existing customer commences a further loan application process with a lender, the lender should obtain confirmation that the borrower has had an opportunity to review the summary issued following the conclusion of the borrower's most recent loan with that lender.

9.354 To allow lenders sufficient time to design and amend their lending platforms, the requirement to make available a summary of the cost of borrowing will become effective 12 months after our Order is made. The requirement to

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[832] See paragraph 9.112 for further discussion on this point.

include a hyperlink or reference to a PCW will not apply until an authorised payday loan PCW exists.

9.355 We also propose to recommend to the FCA, as part of its regular oversight of authorised lenders, that it assist the CMA's monitoring of compliance with respect to both the availability of summaries and how borrowers are notified of the availability of the summaries, to the extent that its powers allow.

Increased transparency regarding the role of lead generators

Summary of remedy

9.356 Figure 9.8 summarises our remedy to increase the transparency of the role of lead generators[833] in the payday lending market.

FIGURE 9.8

Measures to increase transparency regarding the role of lead generators

In order to address competition problems arising from the operation of the lead generator distribution channel, the CMA has decided to recommend to the FCA that it should take the steps necessary to ensure that:

All lead generators passing customer details to payday lenders and/or other lead generators in return for a payment:[834]

(a) disclose clearly, prominently and concisely – using a means that ensures customer interaction – that they are 'not a lender'; and

(b) state explicitly – using a means that ensures customer interaction – that the sale of customer details collected is on the best commercial terms for the lead generator rather than the customer and may not result in an offer of the cheapest loan that is available to meet the customer's needs.

Given the wider concerns raised about the operation of intermediaries in the payday lending market, we consider that there is also a case for the FCA to continue to focus on the operation of lead generators and their compliance with CONC and continue to prioritise its consideration of the activities of lead generators in future credit consultations.

[833] Any party that acts as an intermediary between borrowers and lenders by collecting and passing to providers of payday loans details, including personal contact information, of individuals seeking loans.
[834] In this context payment relates to payment from a lender to a lead generator, or a payment from one lead generator to another, and not a payment from a borrower to a lead generator (including fee-charging credit brokers which are specifically covered by the new rules introduced in PS14/18).

How the remedy addresses the AEC and/or resulting customer detriment

9.357 We found that there is often a lack of transparency in how lead generators describe the service they provide – particularly the basis on which applications are referred to lenders – and that many customers do not understand the nature of the service offered by lead generators. See paragraph 8.5*(d)* and paragraphs 6.106 to 6.111 for further details.

9.358 By requiring lead generators to provide clear and prominent information on the nature of their service and details of the commercial basis on which they sell customer details in a way which ensures customer interaction, we would expect a reduction in the number of instances where customers confuse lead generators with lenders, or use lead generators in the erroneous expectation that these intermediaries will match them with the best loan for their requirements. This is likely to induce some customers to engage in more customer search, for example, by using a PCW.[835]

9.359 We also expect this remedy to increase the likelihood that customers will make an informed decision to use a lead generator as an active choice, rather than as a result of a misunderstanding or by chance, and it will thereby play a part in improving the reputation of the market. Hence we considered that this remedy would contribute to alleviating the reputational concerns that have been a factor in inhibiting entry by lenders with an established reputation in other markets (see paragraph 8.6*(b)*).

9.360 On 1 December 2014 the FCA published Policy Statement PS14/18 'Credit broking and fees'[836] which set out its concerns about the practices of some credit brokers – particularly in the HCSTC and other sub-prime credit markets – which charge upfront fees to consumers. PS14/18 introduced new rules targeted at ensuring that key features of brokers' relationships with consumers are transparent. The new rules came into effect on 2 January 2015 and fee-charging brokers cannot now take fees without having first issued an information notice to a customer (new CONC 4.4.3R) and received a customer acknowledgement (new CONC 4.4.4R). In PS14/18 the FCA stated that it would consult on whether to retain or modify these rules, and whether to introduce additional rules. We considered that if these new rules are retained post consultation, they would be likely to address the concerns we had identified in the PDR about lead generators that were operating as fee-charging brokers.

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[835] See our discussion of our PCW remedy in paragraphs 9.11–9.212.
[836] PS14/18: Credit broking and fees.

9.361 PS14/18 also introduced a new rule, CONC 3.7.7 R (1), requiring all credit brokers to ensure that any financial promotion states prominently that the firm is a credit broker and that it is not a lender. We judged that if CONC 3.7.7 remains in force post consultation that this new rule would be likely to reduce the number of instances where customers confuse lead generators with lenders, and was therefore likely to address aspects of the concerns that we had identified regarding the transparency of the role of lead generators.

9.362 Notwithstanding CONC 3.7.7 R (1), we considered that lead generators should be required to state that they were not a lender in a way that ensured customer interaction, thereby maximising the chance that customers were able to distinguish between lenders and lead generators. We also noted that aspects of the competition problem we had identified arising from the operation of the lead generator distribution channel were outside the scope of PS14/18. We therefore judged that it remained an important part of our remedy that lead generators should be required to state explicitly that application details are sold on the best terms for the lead generator rather than the customer, and that this may not result in an offer to the customer of the cheapest loan that is available to meet the customer's needs. We would expect a declaration of this nature to reduce the number of instances where customers use lead generators in the erroneous expectation that these intermediaries will direct them to the best loan for their requirements.

9.363 In its response to our PDR Quiddi told us that greater consideration should be given to the role that lead generators play in fostering competition. Quiddi said that to date the lead generation route to market had been the most 'cost effective' route for new lenders to enter the market in the absence of a substantial brand or marketing budget. Quiddi also told us that lead generators allowed new lenders to effectively understand the risk associated with this sector in developing their lending policies.[837]

9.364 We considered Quiddi's views. We noted in paragraphs 7.60 and 7.61 that lead generators have a number of advantages from the perspective of a new entrant or a smaller lender, being accessible to all lenders and allowing lenders to exercise close control over the volume and profile of customers that they want to attract. The use of lead generators by new entrants may also reflect the strength of the well-established brands that already exist in the market and the costs associated with advertising on a sufficient scale to acquire sufficient new customers. Lead generators also allow a new entrant to build up a loan book quickly. However, we also note that where a lender expands using lead generators, it is likely to impose little or no competitive

[837] Quiddi response to the PDR, paragraph 1.

constraint on the prices offered by established lenders. We therefore do not consider that lead generators are effective in fostering price competition between lenders.

9.365 We considered that while encouraging new entrants into the payday lending market was likely to improve competition between lenders, we were not seeking new entry for entry's sake. Rather we wish to encourage new entrants that would compete effectively on the price of products, thereby altering the market dynamic for the benefit of consumers. We judged that if a new entrant's point of difference relative to established competitors was to offer a lower price, such companies would be more likely to target the use of payday loan PCWs to acquire customers than rely on the lead generation channel. This was because, as we have described, a PCW would enable the clear communication of a product's price (and price relative to competitors) and could therefore be a more cost-effective means of acquiring leads than lead generators (see paragraphs 7.60 and 7.61).[838]

Remedy design

9.366 We set out below our consideration of the main issues regarding the design of this remedy.

Issue 1: Promoting customer engagement – placement and wording of disclosure

9.367 In designing this remedy we have been mindful that the context in which customers take out a payday loan may increase the likelihood that information presented to applicants may be disregarded in favour of making a speedy application. Two lead generators, Quiddi and Ratio Network Limited, said that customers rarely read, much less acted on, existing disclosures such as the representative APR text and cookie warnings, and our customer research indicated that customers were likely to be reluctant to scroll down through multiple screens to the bottom of a webpage.[839]

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[838] We noted that several lead generators had started to develop models giving customers more input into the choice of lender or broker, such as Quiddicompare.co.uk (Quiddi), kwikcash.co.uk (Money Gap) and controlpayday.co.uk (Nouveau Finance). Money Gap told us that kwikcash.co.uk indicated to applicants details of any lenders that had pre-approved their application, thereby enabling the customer to choose a lender if there was more than one option available. We noted, however, that Money Gap told us that very few applicants were using the new functionality on kwikcash.co.uk. Nouveau Finance told us that controlpayday.co.uk would allow customers to indicate preferred lenders and that the resulting lead would then be offered to preferred lenders first, before being shown to the general pingtree panel.
[839] TNS BMRB research with payday lending customers.

9.368 In light of the challenge to engage customers we first considered where and how a disclosure should be placed to maximise customer engagement.

9.369 Responses to our Remedies Notice indicated that respondents were generally in favour of a disclosure which appeared both on an intermediary's home page and during the application process.

9.370 Based on these responses and the customer research, we took the view that lead generators[840] should place the disclosure prior to the point at which an applicant can input their details into an application form or fields that capture customer contact details, such as phone numbers or email addresses.[841,842] Our review of the main websites used by lead generators[843] indicated that implementing a remedy in this way would significantly increase the transparency of existing websites – only 3% of websites reviewed disclosed the lead generators' broker status above the first 'Apply' button on the home page, and 22% of websites reviewed made no mention that the firm was a broker anywhere on the website.[844]

9.371 We noted that it was also important that the disclosure was prominently placed on any landing pages to which a borrower is directed by means of marketing materials (emails, SMS, advertisements etc). We would expect the disclosure to be made in a similar font size to other mandatory disclosures, such as the representative APR text, and to be visible on the first screen a borrower sees, irrespective of the means by which the borrower is accessing a lead generator's website (smartphone, tablet, laptop, desktop etc).

9.372 Our customer research suggested that applicants were more likely to read and engage with a disclosure which forced an interaction, such as a modal dialogue box with yes/no buttons. Quiddi said that it thought that consumers did not engage with pop-ups,[845] believing that at the point at which a pop-up appeared a customer was likely to have made up their mind on a course of action. It also told us that one of the ways in which there was human interaction with a message was via a modal window.[846] We also noted the

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840 Including when lenders, having declined an applicant, offer to pass the applicant's details on to a lead generator.

841 Also including telephone and SMS application systems used by lead generators.

842 This was supported by our analysis of how customers interacted with the website of a large lead generator ([✂]), which showed that only 3% of customers visited the 'how it works' or 'frequently asked questions' pages of the website.

843 We asked the lead generators in our sample to provide details of their top ten payday loan websites. These websites were reviewed between 11 and 18 September 2014. See Appendix 6.4.

844 Also known as 'above the fold', that is prior to any scrolling down by the user.

845 Quiddi gave the example of the EU requirement for websites to provide disclosure on the use of cookies on websites that almost all internet users ignored without engaging with the message.

846 A modal window requires a user to confirm they have read a message before they can interact with the main website.

Australian Government requirement for an interactive consumer warning in the Australian payday lending market (see Appendix 9.5). We therefore took the view that requiring customers to interact with the disclosure in such a way was an important part of seeking to ensure its effectiveness.

9.373 We then considered how the choice of words might be expected to affect levels of customer engagement and understanding. During our customer research, respondents told us that they were likely only to skim the text of any disclosure and would be put off reading wording which looked too dense or complicated.[847] Accordingly we considered several aspects of the potential wording of a disclosure in paragraphs 9.374 to 9.377 below.

9.374 In relation to the description of the service offered by a lead generator:

(a) We considered that applicants were more likely to understand that they were entering details in a lead generator's website if the disclosure included the words 'is not a lender' in addition to the statement 'is a broker'. We noted that for a firm which is a credit broker and not a lender CONC 3.7.7R is set out on this basis and requires the firm to state prominently that the firm is a credit broker and that it is not a lender.[848]

(b) We considered that terms such as 'passing customer details' or 'introducing customers' were not sufficiently clear descriptions of the process where applications from potential borrowers are auctioned by lead generators operating a pingtree.[849] A more blunt, concise statement such as 'sells your details' would be likely to increase customer engagement and set out clearly the nature of the commercial relationship. Our customer research indicated that blunt, unambiguous messages would be more likely to communicate the nature of the sites quickly and clearly.[850]

(c) We considered two possible approaches to describing the way that customer details are sold by lead generators:

(i) Our analysis indicated that lead generators generally sold customer details on the most favourable commercial terms for the lead generator concerned. Buyers of leads in pingtrees were usually those that submitted the highest bid at the time of the auction. We considered

[847] TNS BMRB research with payday lending customers, p36.
[848] CONC 3.7.7 R (2) requires a firm which is both a credit broker and a lender to ensure that any financial promotion that solely promotes its services as a credit broker states prominently that the financial promotion is promoting the firm's services as a credit broker and not its services as a lender.
[849] The auction mechanism by which many lead generators sell leads to payday lenders and other third parties.
[850] TNS BMRB research with payday lending customers, p37.

that including the wording 'sells your details to the highest bidder' in the disclosure would be likely to maximise customer engagement.

(ii) We also considered that broader wording such as 'sells your details on the best terms for us rather than you' was an alternative option, and had the advantage that it did not pre-suppose an applicant's knowledge of the pingtree auction process.

Three parties submitted that there were circumstances in which leads were not sold to the highest bidder including Credit Benefit Services, Stop Go Networks and SGE Loans.[851] We noted that further consideration would need to be given on a case-by-case basis as to how, for example, lead generators who were effectively advising customers which loan to select from a number of possible options might best be described.

(d) We considered that variations on the word 'matched' should be avoided in a disclosure given the possible connotation that a loan offer resulting from an applicant's use of a lead generator had been subject to some sort of review relating to suitability or value for money.

9.375 We considered two options for text regarding the potential offer of a loan:

(a) 'cheaper loans may be available elsewhere/direct from lenders'; or

(b) 'may not result in an offer of the cheapest loan available to meet your needs'.

9.376 Although we considered that *(a)* was potentially more easily understood in isolation by applicants, we decided that *(b)* was preferable.[852] This was because we considered the wording a better fit in the context of the message. We also noted that *(a)* risked the unintended consequence of raising the ranking of lead generator sites in borrower searches for 'direct lenders' if applicants were using this search term as a way of avoiding brokers.[853]

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[851] Credit Benefit Services indicated that a lender bidding for a higher volume of leads at a set price might be offered a lead in preference to a lender seeking a lower volume at a higher price. Stop Go Networks told us that it might choose to sell leads to a lender rather than a broker bidding a higher price, in order to maintain good relationships with lenders. SGE Loans told us that in cases where its call centre employees discussed a number of loan offers with borrowers, the product chosen by the customer might be the 'best match' for the borrower, as discussed with the call centre employee who was aware of the best match options for the customer as determined by the SGE Loans CRM system which matched the loan options available with the customer requirements to find a 'best match'. The system lists available loans in four groups: best matches, same-day credit, alternative loans and alternative credit.
[852] This approach was supported by Islington Debt Coalition. See Islington Debt Coalition response to the PDR.
[853] Additionally we noted that *(a)* might not just be applicable to lead generators, for example in a response to our Remedies Notice, My Home Finance stated that 'it was probably true for most lenders that cheaper loans may be available elsewhere so requiring this wording in a disclosure seems prejudicial'.

9.377 Figure 9.9 shows an example of a dialogue box illustrating the considerations discussed above.

FIGURE 9.9

Illustrative example of lead generator dialogue box

Lead Generator A example

- We are a broker, not a lender
- We sell your application details on the best terms for us rather than you
- This may not result in an offer of the cheapest loan available to meet your needs

Do you wish to proceed? Yes No

Source: CMA.

9.378 The submissions we received in response to our PDR were broadly supportive of the above remedy.

9.379 Wonga suggested that lead generators should also be required to make the same risk warning that lenders are required to make.[854] It is our understanding that a fully compliant credit broker would make this disclosure.[855] Wonga also suggested that lead generators should publish prominently that they receive a fee or commission.[856] We considered that this did not need to be a specific recommendation to the FCA, rather, that it formed part of the recommendation of improving transparency and that specific wording was for the FCA to decide. Wonga also told us that we should recommend that lead generators should disclose how details might subsequently be sold.[857] We did not identify this as a specific feature in our AEC and considered that this would be subject to appropriate data protection disclosures.

[854] Wonga response to the PDR, paragraph 4.23(a).
[855] CONC 3.4.1.
[856] Wonga response to the PDR, paragraph 4.23(b).
[857] ibid, paragraph 4.23(c).

Issue 2: Technological considerations

9.380 SGE and Stop Go Networks suggested that it might be difficult to fit an extra disclosure on to the smaller screens of smartphones, and this could be a problem given the increasing use of mobile devices by customers to access online payday lenders. We noted this potential issue but considered that it was capable of being overcome through the website design or smartphone application. For example, it would be possible for home screens to display a combination of disclosures pinned to the bottom of the first screen and dialogue boxes which would take into account other required information including the representative APR and the CONC 'risk warning' (see paragraph 3.14*(f)*). We also noted that it might be possible for information to be provided to potential borrowers using the page description or 'snippet' displayed by lead generators when advertising using paid search (see Figure 9.10).

FIGURE 9.10

Google AdWords advertisement showing page description

Source: Google, accessed 19/09/14.

9.381 Google told us that the content of the 'snippet' was generated by its algorithms so it was not possible for a lead generator to ensure that appropriate disclosure was made. Google also told us that the text included in paid search was provided by the advertiser, so any such remedy would need to be imposed on lead generators and not advertising platforms. Furthermore, the amount of text that was available for Adwords adverts was limited (as it was for other paid search advertising platforms) which would constrain the nature of the disclosure and the text promoting the site. Regardless of the route of accessing a lead generator Google considered that an alternative would be that a customer would be presented with a disclosure of the nature of the service provided on a landing page.[858]

9.382 We noted the need for any disclosure requirement placed on lead generators to avoid being too prescriptive regarding technological considerations, so as to ensure that it would remain applicable if future technological developments led to borrowers accessing information in new ways and/or on new devices.

[858] Google response to the PDR paragraphs 17–20.

This led us to the view that the obligation should be phrased in terms of principles and/or higher-level objectives (for example, that disclosure should be clear, prominent and concise), with guidance being issued as necessary on how to implement these principles through different media.[859]

Issue 3: Link to price comparison websites

9.383 We considered whether the disclosure placed on lead generators' websites should include a link to payday loan PCWs. Our customer research indicated a mixed response to prompts which used 'test disclosures' including a link to a PCW.[860] We considered that the most important function of this proposed disclosure was to ensure that applicants understood that the value for money of different lenders' loan offerings was not taken into account in the lead generator auction process. Considering both our customer research, and our objective of providing customers with the greatest opportunity to understand the disclosure, we decided not to recommend a link to a PCW in our PDR.

9.384 We received two responses to the PDR that lead generators should be required to provide a hyperlink to an authorised payday loan PCW.[861] We considered the submissions and while recognising the potential benefit to borrowers we concluded, for the reasons outlined in paragraph 9.385 below, that our proposed disclosure was sufficient, and that therefore the further requirement would not be proportionate.[862] We also considered the risk identified by CashEuroNet that a lender would establish and promote a broker that channelled customers to that lender's website exclusively.[863] Such behaviour would not be consistent with the FCA's Principles for Businesses and a hyperlink was therefore not required.[864] We also considered that a borrower would ultimately be presented with a prominent hyperlink on arrival on a lender's website.

9.385 Notwithstanding the absence of a link to a PCW in the text, we considered that some customers would be prompted by this disclosure to search the market for cheaper loans. This process would be expected to increase customer exposure to different lenders and encourage shopping around. We noted that any borrowers visiting the websites of lenders (including following

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[859] We noted that lead generators also communicate with customers using SMS messages and telephone calls and that a disclosure should relate to these media in addition to existing web-based communications.
[860] TNS BMRB research with payday lending customers, p36.
[861] These responses were received prior to our consultation to amend the implementation of our PCW remedy. (See CashEuroNet response to the PDR, paragraph 3.11; Islington Debt Coalition response to the PDR, p2.)
[862] For example, we identified that a PCW which had chosen not to be authorised could be classed as a credit intermediary and would need to hyperlink to a direct competitor.
[863] CashEuroNet response to the PDR, paragraph 3.11.
[864] http://fshandbook.info/FS/html/handbook/PRIN/2/1 see also paragraph 9.112.

referral by a lead generator) would encounter a link to a PCW as a result of our PCW remedy.

Other issues

9.386 During our investigation a number of parties raised concerns about the operation of this section of the UK payday lending market and the substantial volume of customer complaints generated.[865] Many of these concerns – for example, regarding fee-charging brokers and the lack of control or transparency for customers as to who might receive their data – are wider than the contribution of the lead generator channel to the AEC. The FCA's recent prioritisation of action against a number of credit brokers[866] and new rules for credit brokers who charge a fee to the customer address concerns regarding the activities of fee-charging brokers. In view of data integrity issues and our evidence on the extent of data sales by lead generators, it seems to us that there is also a case for the FCA to continue to prioritise its supervision of the operation and practices of lead generators.

9.387 In our Remedies Notice we asked for views on whether lenders should be prohibited from selling or providing customer details to third parties including, for example, selling declined leads to lead generators. One lender (Global Analytics) submitted that selling leads helped customers find a loan at their time of need.[867] Wonga submitted that a general prohibition on lenders providing customer details to third parties would have the unintended consequence of precluding lenders from sharing data with CRAs.[868] SGE told us that prohibiting lenders from selling or providing customer details to third parties would not be in the customer interest, especially if the lender was not able to provide the customer with a loan.[869] Having considered this issue further, our view is that this issue would be better treated as part of any wider consumer-focused review of the sector, rather than as a remedy to the AEC that we have found.

Implementation of remedy

9.388 We considered that the implementation of the disclosure remedy would sit well within the FCA's payday loan reporting requirements taking effect from October 2014, and could build on the relevant 'status disclosure' obligations in

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[865] FOS, 'Ombudsman warns consumers about payday loan middlemen', 19 August 2014, pp69&70. This point was again repeated in response to the PDR by MAT.
[866] The FCA has closed seven firms to new business, referred three firms for enforcement action and are investigating a further 23 firms, see PS14/18: Credit broking and fees, paragraph 2.9.
[867] Global Analytics response to Remedies Notice.
[868] Wonga response to Remedies Notice, paragraph 7.15.
[869] SGE response to Remedies Notice.

CONC and the new financial promotions and communications rules for credit brokers which came into force on 2 January 2015. The FCA's authorisation process would be a natural time frame to conduct a wider review of consumer and compliance issues, and undertake any enforcement action that the FCA determined was necessary. We therefore decided to address the problems we identified by making a recommendation to the FCA.

9.389 We have therefore decided to recommend to the FCA that it should take the steps necessary to ensure that all lead generators passing customer details to payday lenders and/or other lead generators in return for a payment:[870]

(a) disclose clearly, prominently and concisely using a means that ensures customer interaction that they are 'not a lender'; and

(b) state explicitly using a means that ensures customer interaction that the sale of customer details collected may not result in an offer of the cheapest loan that is available to meet the customer's needs.

9.390 Given the wider concerns raised about the operation of intermediaries in the payday lending market, we consider that there is also a case for the FCA to continue to focus on the operation of lead generators and their compliance with CONC and to continue to prioritise its consideration of the activities of lead generators in future credit consultations.

Other remedies considered but not adopted

Remedies identified by the CMA in the Remedies Notice

9.391 In our Remedies Notice, we invited views on two remedies that we were not minded to take forward, including on whether either or both of them should be given further consideration. These potential remedies were:

(a) prohibition of additional fees; and

(b) FCA 'badging' of authorised lenders' websites.

9.392 We consider each of these options in turn below. We then consider a number of options put forward in response to the Remedies Notice.

[870] In this context payment relates to payment from a lender to a lead generator, or a payment from one lead generator to another, and not a payment from a borrower to a lead generator (including fee-charging credit brokers which are specifically covered by the new rules introduced in PS14/18.

Prohibition of additional fees

9.393 We considered a remedy which would prohibit the charging of any fees in addition to interest charges on the principal lent to customers.

9.394 We have found that it can often be difficult for customers effectively to compare prices of loans in different scenarios.[871] By prohibiting additional fees, any comparison of the price of loans would potentially be simpler.

9.395 We noted in our Remedies Notice that the FCA was considering the most appropriate way of implementing its obligation to deliver a price cap. Given this, we saw little merit in considering additional direct restrictions on fees and charges ourselves. Our focus has instead been on measures that will empower customers to find the best-value product for them and therefore impose greater competitive pressure on lenders to offer better terms than those specified by current or future regulations.

9.396 No party submitted to us that we should take a different approach, and we consequently have not considered this option further.

FCA 'badging' of lenders' websites

9.397 In the Remedies Notice, we considered a remedy that would allow the websites of payday lenders to promote the fact that they were accredited and regulated by the FCA (with the ability for a visitor to confirm on the FCA's website that the lender was accredited). A similar system is used for the registration of online pharmacies. We considered that these responses applied equally to authorisation. Regulatory 'badging' of authorised lenders' websites might give customers confidence that the lender was being supervised, which might help address reputational barriers to entry and/or expansion.

9.398 However, we judged that the remedy would be unlikely to be effective because consumers' expectations of authorisation might differ from the scope and nature of the FCA's regulatory activities and an unintended 'expectation gap' might arise. Further, we were concerned that any badge may have an impact on the FCA's ability to change its authorisation and/or supervisory arrangements. While we would expect the strengthening of the regulatory framework to reduce reputational barriers to entry, we did not wish to detract from the obligations on lenders to improve their business practices or to give customers a misleading impression about particular lenders.

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[871] See paragraph 8.5.

9.399 No party submitted to us that we should take a different approach, and we have not considered this option further.

Additional remedies proposed by third parties

9.400 We received a number of suggestions of additional remedies from third parties in response to our Remedies Notice.[872]

- *(a)* Wonga told us that the CMA should consider making a recommendation to the FCA (and the Government, as appropriate) that the price cap should be subject to a periodic review.[873]
- *(b)* The Association of British Credit Unions Limited (ABCUL) told us that the Pew Institute had found the prohibition of single-instalment loans in Colorado to be particularly effective.[874]
- *(c)* The Debt Advice Foundation recommended that all non-online advertising of single instalment-loans should be prohibited.[875]
- *(d)* Money Advice Scotland (and others) recommended greater public education on personal finance.[876]

9.401 We considered each of these in turn.

Periodic review of the price cap

9.402 Wonga suggested that if sufficient competition was found to exist as a result of the package of remedies introduced then the price cap should be lifted.

9.403 We understand that the FCA will be undertaking periodic reviews of the price cap. It was therefore not clear to us what additional benefit would arise from us making a recommendation in this area, nor how this would address the AEC and/or resulting customer detriment which we had identified.

Prohibition of single-instalment loans and restricting advertising of single-instalment loans

9.404 We were told by ABCUL that prohibiting single-instalment loans would ensure that repayment schedules better reflected a borrower's capacity to repay (by

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[872] We received no substantive suggestions of additional remedies in response to the PDR.
[873] Wonga response to Remedies Notice, paragraph 1.11.
[874] ABCUL response to Remedies Notice, pp2&3; The Pew Institute has undertaken various pieces of research into short-term credit.
[875] Debt Advice Foundation response to Remedies Notice, p4.
[876] Money Advice Scotland response to provisional findings, Remedies Notice and Notice of a request for a variation of the terms of reference, p2.

repaying the capital over a longer period of time, the amount of capital repaid in each instalment would be lower). Similarly, as noted above, the Debt Advice Foundation suggested that all non-online advertising of single-instalment loans should be prohibited.

9.405 It was not clear to us how this proposal would address the AEC we have found. Moreover, without imposing further regulation of prices we did not consider that the TCC would be reduced as a result of restricting single-instalment loans (although instances of default might be reduced). We considered that this would potentially be disproportionate if different types of credit were subject to unequal restrictions; for example, credit cards, over-drafts and other lines of credit could all be paid in single instalments.

9.406 We understand that the FCA is reviewing lenders' assessment of affordability as part of its authorisation process. If the result of this review leads to tighter criteria, lenders may choose to offer multiple-instalment products to those less able to afford to repay a loan in a single instalment.

9.407 In proposing a ban on advertising of single-instalment loans other than online, the Debt Advice Foundation noted that 83% of loans were taken out online. However, we considered that it might be disproportionate to prevent lenders who may service borrowers that do not have access to the internet from advertising in channels that their customer base would access.

9.408 As we were not able to establish how such a restriction on either the ability to offer or advertise single-payment loans would remedy the AEC that we have found, we decided not to pursue these proposals.

Improved education on personal finance

9.409 We considered whether borrowers needed to have a greater level of financial literacy and whether this would address the AEC we have found. We thought that there could be clear benefits from this – not limited to payday lending – but we considered that directly addressing the specific features of this market that we have found would be a more cost-effective, focused and timely means of tackling the AEC and resulting customer detriment that we have found.

Conclusion

9.410 In our PDR we provisionally decided not to include any of these remedies in our remedies package. We did not receive any substantive additional responses to the PDR suggesting that any of the remedies outlined in paragraph 9.400 should be adopted or that any other additional remedies should be considered. We have therefore decided not to include any further remedies in addition to the package outlined in the PDR.

Relevant customer benefits

9.411 In deciding the question of remedies, the CMA may 'have regard to the effect of any action on any relevant customer benefits of the feature or features of the market concerned'.[877] RCBs are defined in the Act and are limited to benefits to relevant customers in the form of:[878]

(a) lower prices, higher quality or greater choice of goods or services in any market in the UK (whether or not the market to which the feature or features concerned relate); or

(b) greater innovation in relation to such goods or services.

9.412 The Act provides that a benefit is only an RCB if the CMA believes that:[879]

(a) the benefit has accrued as a result (whether wholly or partly) of the feature or features concerned or may be expected to accrue within a reasonable period of time as a result (whether wholly or partly) of that feature or those features; and

(b) the benefit was, or is, unlikely to accrue without the feature or features concerned.

9.413 In the Remedies Notice, we invited parties to inform us of any RCBs to which we should have regard. No party submitted any evidence about any possible RCB. Nor did we identify any RCBs ourselves.

9.414 We concluded that there were no RCBs that might be lost as a result of introducing our proposed package of remedies. Therefore we see no need to modify our remedy package to take account of RCBs.

The need for remedial action

9.415 In Section 8 we set out a number of features of the payday lending market which meant that price competition between payday lenders was not effective, and which resulted in customers paying more for their loans than we would expect in a well-functioning market.

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[877] Section 134(7) of the Act.
[878] Section 134(8)(a) of the Act.
[879] Section 134(8)(b) of the Act.

9.416 The FCA has recently implemented new rules in relation to CPAs and rollovers, taken enforcement action against a number of lenders, introduced new rules for credit brokers and introduced its price cap, which came into force on 2 January 2015.[880] In this section we consider the impact of these developments on the effectiveness of competition between payday lenders, and on the ongoing need for remedial action to address the AEC that we have identified.

9.417 We have already discussed in the previous sections the potential implications of the price cap for the payday lending market (see Section 4), the potential consequences of the cap for the effectiveness of competition between payday lenders (see Section 6 and 7), and for customer detriment (Section 8). In the following paragraphs we summarise these potential effects and discuss possible impacts of the cap.

Implications for the payday lending market of the FCA's price cap

9.418 Given the scale of the reduction in charges implied by the level of the cap, the FCA's price cap is likely to have significant implications for the payday lending market. Drawing on the FCA's analysis of the price cap, we identified three main effects that might be expected to result.

(a) Those lenders that were pricing above the cap are now required to reduce prices to continue lending legally and thus revenues will fall (unless there is a sufficient compensating increase in lending volumes). This may mean that some less efficient and/or less well-resourced lenders exit the market (see paragraph 4.169).

(b) By reducing the expected revenue associated with a given customer, the cap is likely to cause lenders who currently charge above the cap to tighten their risk thresholds, granting fewer loans to high-risk customers (see paragraph 4.170).

(c) The structure of the cap is also likely to influence the characteristics of the loan products that lenders offer, by affecting the relative profitability of different types of product or by making it more difficult to structure certain types of product in ways that comply with the cap (see paragraph 4.73).

[880] See Section 3 for a detailed overview of recent developments in regulation.

9.419 We considered that these effects may become more apparent over different time frames for different lenders as they amend their strategy and business models.[881]

Implications of recent developments for the effectiveness of competition

9.420 We considered the impact of the FCA's price cap on the features of the market that we had identified as giving rise to an AEC.

9.421 Those features which limit customers' responsiveness to prices generally reflect underlying characteristics of the short-term unsecured lending market, and so would be expected to continue to restrict competition between lenders in the presence of the price cap. Therefore the need for remedial action remains. For example, the cap is highly unlikely to reduce the perceived urgency underpinning many borrowers' decisions to take out a payday loan, or remove the uncertainty that many customers face when deciding which lender to borrow from (see paragraphs 6.121 to 6.126).

9.422 The cap is also unlikely to mitigate any of the characteristics of the payday lending market which limit the constraint that lenders face from the threat of entry and expansion, putting smaller lenders at a disadvantage when establishing themselves in the market. The cap may even weaken the constraint further, if by reducing expected post-entry profitability the cap reduces the incentive for new lenders to enter, and increases the resources and time required by a new entrant to overcome its initial disadvantages and establish itself in the market (see paragraph 7.115).

9.423 A further potential effect of the price cap on competition is that it may further dampen price competition between lenders by providing a 'focal point' or 'going rate' for payday loan pricing. One lender raised the possibility that the combination of this effect, together with higher market concentration and increased price transparency provided by PCWs, will facilitate mutual recognition of interdependencies between lenders. This lender suggested that this could in turn facilitate the emergence of tacit coordination. We also considered that the possibility of lenders pricing up to the level of the cap might be facilitated by the barriers to entry and expansion giving rise to an AEC that we had identified in our provisional findings (and possibly by those barriers being raised by the cap itself – see paragraph 9.422 above).

[881] Lenders might, for example, tighten lending criteria immediately after the introduction of the cap before subsequently relaxing their lending decisions as lending models are developed. Similarly any exits from the market might be as a result of a strategic decision prior to the cap being introduced, or might be made in response to a lender's financial performance.

9.424 We took the view that any possibility that the price cap might facilitate tacit coordination further increases the need for remedies that expose lenders to greater competition and incentivise entry and expansion. Our package of remedies is designed to achieve this. However, while we acknowledged the possibility that the price cap might become a 'focal point' for coordination, we also noted that the significant variation in market shares, efficiency, costs and products offered by different lenders would likely frustrate coordination efforts, particularly if the obstacles to competition we have identified were addressed effectively.

9.425 We did not agree that the development and promotion of more effective payday loan PCWs was likely to increase the likelihood of coordination. Although we note that better PCWs would increase the transparency of pricing information available to payday lenders – thereby making it marginally easier for lenders to monitor deviations from any coordinated outcome – the main impact of this element of our remedy package would be to reward lenders who offer customers low prices and to make entry and expansion by smaller lenders possible. These effects are likely to significantly increase the incentives on lenders to compete rather than coordinate.

9.426 We identified two areas where the cap might moderate to a limited extent the adverse impact of some of the features of the market that give rise to an AEC. First, if it leads to some simplification of the products on offer in the market (eg in relation to late fees and charges), the price cap may increase the comparability of different payday products, making it easier for customers to identify the best-value loan for their requirements (see paragraph 6.121*(b)*). Second, to the extent that the cap – together with the FCA's enhanced regulation of the payday lending sector more generally – improves the reputation of the sector and offers borrowers additional protection, it may reduce the risk perceived by customers of switching lender. It may also make the payday loan sector more attractive to businesses in other sectors and encourage them to enter (see paragraph 7.114). However, we did not expect these indirect effects of the cap to be sufficient to prevent the AEC that we have found, such that the need for competition-enhancing measures targeted on its underlying causes was removed.

9.427 We considered that the recent deterioration in payday lenders' financial performance was likely to reflect lenders anticipating and adjusting to a tougher regulatory regime (see paragraphs 4.165 to 4.166), rather than any increase in competition resulting from a weakening in the barriers to price competition that we had identified. Consequentially, we rejected the view that these recent developments indicated that there was no longer a need for remedial action to address the AEC.

Implications of recent developments for future customer detriment

9.428 Given the above assessment, we concluded that the price cap will not address the key underlying features of the market that we have identified as giving rise to an AEC. The price cap might also give rise to the risk that price competition between payday lenders is further dampened (albeit around a lower interest rate than is currently observed in the market) – for example if the cap were to become a focal point for the price of payday loans. However, by enforcing a significant reduction in customer price the cap may generate some of the beneficial effects that we might otherwise expect more effective price competition to bring about.

9.429 Notwithstanding the beneficial effects of the price cap, as discussed in Section 8 (see paragraphs 8.12 to 8.13), our view is that scope for substantive price (and non-price) competition within the constraints of the price cap would remain. In relation to the possible risk that the price cap reduces the scope for competition by incentivising lenders to price at the level of the cap, we discussed above (see paragraph 9.423 to 9.425) how the cap might facilitate tacit coordination. We considered that the risk of coordination would only increase the importance of our package of remedies, including the introduction of effective PCWs. By stimulating customers' responsiveness to prices and by facilitating entry and expansion our remedies would increase incentives on lenders to compete with each other, undermining the sustainability of coordination.

9.430 We concluded that the potential detriment to customers as a result of the AEC would still be significant with the cap in place, especially given that the longer-term dynamic benefits of competition are very difficult to replicate through measures to control outcomes such as a price cap. Therefore, we concluded that significant further benefits could be realised by the introduction of effective remedies to the AEC that we have identified in the UK payday lending market. We did, however, take the impact of the FCA's price cap into consideration as part of our assessment of the effectiveness and proportionality of our remedies.

The need for ongoing remedial action

9.431 As noted above, we are conscious of the regulatory actions of the FCA and we expect that the market will continue to evolve. We considered the possibility of including a 'sunset' clause for our remedies (that is to specify a date at which lenders would cease to be obligated to adhere to them), or a specific review date at which point the CMA would commit to considering the ongoing need for remedial actions.

9.432 Where our remedies take the form of a recommendation to the FCA, we consider that the FCA is in a suitable position to adapt or lift any regulatory intervention which it introduces in response to our recommendation, at an appropriate point. For our remedies where we will be making an Order (ie the obligations to publish on an authorised payday loan PCW and make available a summary of the cost of borrowing), we considered that the FCA would be in a suitable position to monitor developments in the market and that basing the timing of any review of our remedies package on submissions from the FCA would facilitate greater responsiveness and flexibility.

9.433 Given the ongoing regulatory role of the FCA we therefore do not intend to introduce a fixed lifespan to any remedy in our package. Rather it is our expectation that the FCA will keep the operation of the market under review and that the CMA will review any request made by the FCA to lift or amend our Order as appropriate.

Conclusion on the need for ongoing remedial action

9.434 We concluded that the price cap is likely to lead to significant changes in the payday lending market, including a significant reduction in the number of loans issued, some market exit, and a change in the nature and range of products on offer. In general, the cap is unlikely to address the underlying features of the market that we identified as giving rise to an AEC, and – absent remedies to promote effective price competition – may further dampen price competition (eg if the cap became a focal point for payday loan pricing). While the cap may also have some limited beneficial consequences to the extent that it leads to greater simplification of the products on offer in the market, facilitating their comparability[882] and/or improves the reputation of the sector, we did not expect these indirect effects to be sufficient to prevent the AEC that we found.

9.435 While the cap will significantly reduce the price paid by many payday loan customers, and in this way generate some of the potential benefits that we might expect from more effective price competition between lenders, we concluded that a significant customer detriment would remain as a result of the AEC, even with the price cap in place. Fundamentally, in the absence of effective price competition, there will be no incentive for lenders to compete below the cap, keeping their prices low and reflecting their costs in the prices they charge in the future. Absent effective competition, prices are unlikely to

[882] The comparability of loans will be subject to the nature of the products and pricing structures that individual lenders choose to supply. One such change might be lenders choosing to move away from single instalment loans.

respond to changes in market conditions, such as technological developments, evolution in the products on offer, or changes in market structure. We conclude that that there remains a need for effective and proportionate remedies to address the AEC that we have identified in the payday lending market.

9.436 As discussed in paragraph 9.431, we have not specified a fixed sunset clause or review date for these elements of the remedy package that we are introducing. It is our expectation that the CMA will review any submission made by the FCA with respect to our remedies package.

Effectiveness of our package of remedies

9.437 Based on the assessment above, we have decided the following measures should be included within a package of remedies that will work together to address the AEC that we have identified:

(a) Measures to promote the use of effective authorised payday loan PCWs, in particular a requirement for lenders to publish details of their loans on at least one PCW operated by an FCA-authorised firm combined with a recommendation to the FCA to introduce new guidelines for payday loan PCWs (see Figure 9.1 in paragraph 9.11).

(b) A recommendation to the FCA to take steps to improve the disclosure of late fees and other additional charges (see Figure 9.2 in paragraph 9.213).

(c) A recommendation to the FCA to take steps to help customers shop around without unduly affecting their ability to access credit (see Figure 9.3 in paragraph 9.235).

(d) A recommendation to the FCA to take further steps to promote RTDS between lenders (see Figure 9.5 in paragraph 9.271).

(e) A requirement for lenders to provide existing customers with a summary of the cost of borrowing (see Figure 9.7 in paragraph 9.286).

(f) A recommendation to the FCA to take steps to increase transparency regarding the role of lead generators (see Figure 9.8 in paragraph 9.356).

9.438 In our assessment of the effectiveness of this package of remedies, we consider below:

(a) how the package of remedies addresses the AEC and/or the resulting customer detriment (paragraphs 9.439 to 9.451); and

(b) other aspects of the effectiveness of our package of remedies (paragraphs 9.452 to 9.477).

How the package of remedies addresses the AEC and/or resulting customer detriment

9.439 We discuss the rationale for each element of the package of remedies in the consideration of the design of each remedy above. In this subsection, we summarise how the elements in the remedy package work together to remedy the AEC that we have found, and/or the resulting customer detriment.

9.440 We consider first how the package of remedies addresses those features of the market that restrict competition between payday lenders by limiting the extent to which customer demand is responsive to prices. We then consider how the package of remedies addresses those features of the market which restrict the constraint on payday lenders' prices that might otherwise be imposed by the prospect of new entry or expansion. We consider the synergies between the various measures and the coherence of the package of remedies later in this section (see paragraphs 9.472 to 9.477).

Impact on the extent to which customer demand is responsive to price

9.441 We have found that the limited extent to which customers respond to differences in payday lenders' prices is the result of a combination of features which tend to reinforce one another. These features are:

(a) the context in which the decision to take out a payday loan is often made;

(b) difficulties that customers face in identifying the best-value offer;

(c) additional factors limiting customers' awareness of and sensitivity to late fees and other extra charges;

(d) the risk and loss of convenience that customers perceive to be associated with switching lender; and

(e) the role played by lead generators.

9.442 The package of remedies will address this aspect of the AEC by lessening the extent to which these features reduce customer responsiveness to price and restrict competition between payday lenders. We consider below the contribution made by each element of the package of remedies to addressing these features.

9.443 First, good-quality PCWs provide an environment where customers can consider multiple offers simultaneously and compare prices on a like-for-like basis, enabling them to identify easily and quickly the best loan for their needs. Our package of measures will encourage the use of PCWs among borrowers (including through a hyperlink on lenders' websites and from the summary of borrowing costs) and – through minimum standards introduced through the FCA's regulatory framework – improve the quality of the PCWs available to payday loan customers. We expect this to increase the proportion of new and returning customers that shop around and to improve the frequency and effectiveness of the comparisons that customers make before taking out a loan. This will in turn increase pressure on lenders to ensure that their rates are competitive relative to others. We would expect this effect to be significant, even with the FCA's price cap in place.

9.444 Second, to the extent that actions taken by the FCA in response to our recommendations lead to an improvement in the clarity and prominence of how information about late fees and charges is presented, customers will be more likely to take this information into account in their choice of lender. This effect will be reinforced to the extent that authorised payday loan PCWs also display prominently information on late fees and other charges alongside the headline cost of the credit and by the requirement on lenders to show such additional costs for a customer's most recent loan as part of a summary of borrowing costs. We noted that some customers pay limited attention to these additional costs, because they are confident that they will not have to pay them.[883] However, we would expect increased prominence of these charges to increase competition among lenders in relation to the extent to which such fees are levied and the level at which they are set (having regard to the FCA's cap) as part of their overall customer proposition and for fear of losing some customers if they do not offer good value overall.

9.445 Third, to the extent that our recommendations regarding credit searches and the development and use of real-time CRA databases improve customers' ability to find out if they are eligible for a loan without affecting their subsequent ability to access credit, then this will support the other measures in our remedy package in encouraging customers to shop around for their loan.

9.446 Fourth, a retrospective summary of borrowing costs[884] will draw customers' attention to the costs associated with borrowing from their lender, and will encourage some customers to consider alternative offers. This will increase

[883] See paragraph 6.95.
[884] By which lenders must make a summary available to returning customers once a loan has been repaid and which customers are required to indicate that they have had opportunity to review before applying for a further loan from that lender.

the pressure on lenders to keep their terms competitive so as to retain existing customers.

9.447 Fifth, to the extent that actions taken by the FCA in response to our recommendations ensure that lead generators and other credit intermediaries provide clear, concise and prominent information on the nature of the service that they offer[885] this will improve customers' understanding of lead generators. As a result, the likelihood that customers use a lead generator in the mistaken expectation that they are dealing with a lender or that these intermediaries will match them with the best loan for their requirements will be reduced. We would expect this to prompt some customers to increase the extent of their search activity. This in turn will increase pressure on lenders to ensure that they offer loans that are competitive in terms of the value for money for customers, rather than in terms of the fees paid to intermediaries.

9.448 As a result of these effects, we expect that the package of remedies will increase the extent to which customers are responsive to prices and choose the best loan for their requirements. This will in turn increase pressure on lenders to keep their prices low, rather than simply pricing at the level of the FCA's price cap, in order to attract new customers and/or retain existing ones, and in this way address the AEC and the resultant customer detriment that we have identified.

Impact on the constraint imposed by the prospect of entry or expansion

9.449 We have found that the competitive constraint that might be imposed on payday lenders' prices by the prospect of new entry or expansion is weakened by a number of features:[886]

(a) new entrants will face disadvantages relative to more established lenders, in particular in relation to the cost of customer acquisition and the assessment of credit risk; and

(b) the negative reputation of the sector reduces the constraint imposed on payday loan pricing by the prospect of new entry, especially by businesses with established reputations in other sectors.

9.450 We considered that our remedy package will help to address the AEC by increasing the constraint imposed on established lenders by the prospect of new entry or expansion. In particular:

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[885] Including the fact that they are not a lender and a simple explanation of the basis on which customers are referred on to lenders (see Figure 9.8).
[886] See paragraph 8.6.

(a) If more payday loan customers consult a PCW before taking out their loan, this would better enable new entrants and smaller lenders to raise awareness of their products, and so establish themselves in the market to rival incumbent providers. A smaller lender with an attractive product, will be able to bring their product to customers' attention, irrespective of the lender's size or the time they have been in the market, by virtue of the product appearing prominently in comparison tables.[887] By providing for the authorisation of multiple PCWs, our remedy is intended to facilitate competition between PCWs which we would expect to constrain the commissions charged to lenders by PCW operators.

(b) We also see significant benefits to competition associated with any measures which improve the utility of CRA data, by improving its coverage, accessibility or the frequency with which it is updated.[888] We would expect further developments in this area to reduce the disadvantage that new entrants and smaller lenders currently have in assessing customers' credit risk, relative to more established players.[889]

(c) The emergence of authorised payday lending PCWs would complement the regulatory actions of the FCA and contribute to improving the reputation of the sector. This would address the reputational concerns that some non-payday lenders have raised as factors that have inhibited entry to date. We would similarly expect the overall reputation of the market to benefit from the increased transparency in relation to late fees and additional charges and from lead generators displaying information about their role more prominently and explicitly.

9.451 We considered that, taken together, these measures would contribute to create a competitive environment where entry and expansion will be easier than would be the case otherwise. As a result, we expect the package of remedies to result in established lenders facing a stronger competitive constraint from the prospect of smaller lenders expanding in the market and/or the threat of entry from providers established in other markets. This will put downward pressure on prices, reducing the customer detriment arising from the AEC.

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[887] There is evidence of this happening in other markets. For example, the CMA found that 'New private motor insurance providers have been able to enter the market and have attracted customers by posting competitive prices on PCWs rather than spending money on advertising.' (See *Private motor insurance market investigation: final report*, paragraph 8.4). See also paragraphs 7.35–7.75 for a discussion of the difficulties new entrants currently face in generating awareness of their products.
[888] See paragraph 7.104 for a discussion about the concerns relating to the information available from CRA data. Appendix 9.2 (paragraphs 164–172) reports the view of some lenders about at the importance of introducing RTDS to encourage entry and promote competition in the market.
[889] See paragraph 7.119.

Other aspects of the effectiveness of our package of remedies

9.452 For the reasons set out above, we have concluded that our package of remedies will be effective in targeting a number of the main causes of the AEC that we have identified. In evaluating the effectiveness of our package of remedies, we have also considered the following further factors:

(a) the extent to which the remedy measures are capable of effective implementation, monitoring and enforcement;

(b) the timescale over which the remedy measures will take effect;

(c) the consistency of the package of remedies with existing and likely future laws and regulations; and

(d) its coherence as a package of remedies.

Implementation, monitoring and enforcement

9.453 In developing each of the remedy measures, we have considered how each remedy measure could best be implemented, monitored and enforced.

9.454 Our consideration of how each measure could be implemented, monitored and enforced is set out in our assessment of each remedy in paragraphs 9.10 to 9.390. In summary, we have concluded that:

(a) We introduce by CMA Order the prohibition on lenders from supplying payday loans unless details of their prices and products are published on at least one authorised payday loan PCW. We recommend to the FCA that it considers how to raise standards for payday loan PCWs.

(b) We address the problems that we have identified in relation to late fees and other additional charges by making a recommendation to the FCA, which is well placed to monitor and enforce compliance, using its existing regulatory mechanisms.

(c) We recommend to the FCA to take measures to help customers assess their own creditworthiness and to facilitate the development of RTDS.

(d) We introduce an obligation on lenders to provide a summary of a customer's borrowing history by CMA Order. We recommend to the FCA that it supports the CMA in monitoring lenders' compliance with this obligation, to the extent that its powers allow. It would fall to the CMA to enforce compliance with the Order and to take any enforcement action necessary.

(e) We address our concerns in relation to the operation of the lead generator channel by means of a recommendation to the FCA, which is well placed to monitor and enforce compliance, using its existing regulatory rules and mechanisms.

9.455 We therefore concluded that each of the measures was capable of effective implementation, monitoring and enforcement.[890]

The timescale over which the remedy measures will take effect

9.456 In evaluating the timescale over which the remedy measures within our package of remedies are likely take effect, we considered:

(a) the time that it is likely to take to implement the remedy measures following publication of our final report; and

(b) the time that it is likely to take for the remedy measures, once implemented, to remedy the AEC and the resulting customer detriment.

- *Time taken to implement remedies*

9.457 The time taken to implement remedies following a CMA investigation will depend, in part, on whether the CMA is taking action itself or recommending that action be taken by others.

9.458 Where the CMA is taking action itself, the implementation of remedies following a CMA investigation typically involves two stages. In the first stage, the CMA makes an Order.[891] This includes a period of informal consultation with relevant parties followed by a formal public consultation, as specified in Schedule 10 to the Act.[892] The CMA must make a final Order within six months of the date of publication of the market investigation report. The CMA may extend this six-month period by up to a further four months if it considers that there are special reasons why a final Order cannot be made within the statutory deadline.[893] In the second stage of implementation, the parties

[890] In reaching this view, we noted that our package of remedies contains a large number of recommendations compared with some other market investigations. We consider that this is appropriate to the particular facts and circumstances of this investigation, as the ongoing regulatory role of the FCA means that it is best placed to integrate many of the further actions necessary to address the AEC with its other interventions in the payday lending market (see the Guidelines, paragraph 390).
[891] It is also possible for the CMA to accept undertakings (see the Guidelines, paragraphs 92 & 93). This is unlikely to be practicable in this case given the potentially large number of parties from whom undertakings would need to be sought.
[892] The action required by the CMA may be a one-off action (eg to implement a divestiture) or a continuing commitment (eg to comply with a behavioural remedy). A timescale is normally specified within the relevant order/undertakings within which parties must take the necessary action.
[893] Section 138A of the Act. These time limits do not apply to any further implementation required after final undertakings have been accepted or a final order made.

subject to any Order take the action required by the CMA within the period specified in the Order.

9.459 We would expect to be able to put in place an Order in relation to those measures to be implemented by the CMA (ie the prohibition on lenders from supplying payday loans unless details of their prices and products are published on at least one authorised payday loan PCW and the obligation on payday lenders to provide customers with a summary of their borrowing history) within six months of publishing our final report. An additional transitional period may be given to enable lenders to make the necessary changes to comply with the Order.

(a) In relation to the obligation to publish on an authorised payday loan PCW, this timescale will itself be determined by the time frame in which the FCA develops the minimum standards for payday loan PCWs and the point at which firms are authorised (see paragraph 9.197). However, once one or more authorised payday loan PCWs have been created, we would expect lenders to be able to comply with the Order quickly (paragraph 9.197*(c)*).

(b) The requirement for lenders to provide customers with a summary of the cost of borrowing will become effective 12 months after our Order is made. Once a lender is listed on an authorised payday loan PCW, a link to this PCW will need to be included unless a link to a list of all authorised payday loan PCWs is provided. Given lenders' general comments on the relative ease with which existing communications with customers could be adapted, we do not expect any additional transitional period for the inclusion of a link to a PCW once a lender is published on a PCW.

9.460 The timescale for implementing the measures that we recommend the FCA to implement will depend upon the time required for the FCA to consult on the measures and the time allowed for their implementation. Our current expectation in relation to these measures is as follows:

(a) The FCA has said it plans to consult on the changes to the PCW regulatory framework for payday loans in summer 2015. Depending on the responses to the consultation we anticipate that the FCA would put in place the regulatory framework for payday loan PCWs by the end of 2015 or early 2016, with the changes becoming effective by the end of 2016. We therefore expect that lenders would be in a position to comply with their obligations under the Order within around two years of publication of our final report.

(b) We would expect the FCA to be able to make significant progress in taking forward our recommendation in relation to late fees and other charges within 12 months of our final report.

(c) We would expect the FCA to be able to make significant further progress in establishing how to take forward our recommendations in relation to enabling customers to assess their own creditworthiness and RTDS within 12 months of publication of our final report.

(d) We consider that the FCA's full authorisation process for credit intermediaries would represent a natural time frame during which to take forward our recommendations regarding lead generators. We would expect the FCA to be in a position to take these measures forward within 12 months of publication of our final report. We also note that the FCA has already introduced new rules to tackle poor practice in the credit broking market which came into force on 2 January 2015. The rules are intended to ensure that customers are given clear information about who they are dealing with, what fee will be payable, and when and how the fee will be payable. These rules implement part of our recommendations concerning lead generators.

- *Time taken for remedy package to take effect*

9.461 We considered the likely time required for the package of remedies – once implemented – to take effect and to lead to greater competition between payday lenders.

9.462 One key factor on which this will depend is the time taken for PCW operators to decide to set up payday lending comparison tables and develop their sites to meet the requirements of any new FCA standards. We considered that this process would take place in the time specified by the FCA for the new regulatory framework to take effect. We would not expect it to be an excessively complex exercise for an established PCW to develop a payday lending comparison table,[894] or to adapt existing payday lending tables to meet the new standards for payday loan PCWs, but we note that the FCA's proposed timeframe would be subject to consultation. Consequently, we expect lenders could be listed on payday loan PCWs by summer 2016 if a

[894] [✂] told us that there existed off-the-shelf aggregation technology and content management systems that would enable operators to implement a PCW relatively easily and quickly. Gocompare.com told us that it had used a third party provider (Runpath/LoveMoney) as its supplier of price comparison services for financial products since 2011, and this provider had a panel of payday lenders. Gocompare had not incorporated this panel into its site so far but it said that adding this functionality to its website would be relatively simple.

third party PCW enters the market within six months of the FCA publishing its standards.[895]

9.463 While it would inevitably take some time for awareness of effective payday loan PCWs to improve among the payday lending population, we considered that this process would be assisted by the measures required of lenders regarding publicising the existence of PCWs, as well as PCW operators' own efforts to promote their services.[896]

9.464 On this basis, we took the view that our remedies relating to PCWs were likely to have a material impact on the proportion of payday loan customers using PCWs within around two years after publication of our final report and that this effect would continue to grow as awareness (and usage) of the sites developed.

9.465 We would expect that, following implementation, measures requiring lenders to make available a summary of borrowing would have an immediate effect on the behaviour of some customers with loans subject to the requirement. We would expect that the likely impact of this measure would increase over time as a greater proportion of customers received summaries. They would be prompted to consider whether their previous lender was the best provider to meet their requirements. Further, once authorised payday loan PCWs start to operate, the requirement for the statement to include the web address of one or more authorised payday loan PCWs or a portal listing all authorised payday loan PCWs will raise awareness of the existence of authorised payday loan PCWs.

9.466 Measures requiring lead generators to disclose to potential applicants the service that they offer, would have an immediate effect on the understanding among new and repeat applicants taking out a loan via a lead generator. As with the other measures, we would expect the impact on the extent of competition in the payday lending market to increase over time, as a greater proportion of customers were exposed to the message.

9.467 Finally, the time taken for the recommendations to enable customers to assess their own creditworthiness, to encourage RTDS and to improve the

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[895] As set out in paragraph 9.36, we considered that the risk that no commercial operator would be interested in seeking authorisation and/or capable of meeting the necessary standards was low. In the unlikely event that this eventuality arose, and lenders worked together to develop an authorised site, then this might take longer to implement.
[896] For example, [✂] told us that its total marketing budget was £[✂]. It spent around £[✂] a year on television and the majority of its remaining expenditure was Google-paid search. [✂] provided figures of payday-specific pay-per-click spend in 2012 and 2013 (first six months to June) when it was active in the market 2012: £[✂]; 2013: £[✂]. [✂]

provision of information regarding late fees to have an effect will depend on the actions taken by the FCA. We note that the FCA has given significant attention to ensuring compliance among payday lenders and intermediaries,[897] and so would be likely to take an active and timely role in ensuring that lenders display information on late fees clearly and prominently. We also noted the considerable progress that had been made in respect of the provision of real-time CRA data in a relatively short period of time as a result of the FCA's efforts in this area.[898]

- *Conclusion on timescale for remedies to address AEC*

9.468 We concluded that the remedies would have a significant beneficial impact on competition around two years after publication of our final report and that this effect would continue to grow, as customers became more aware of the benefits of shopping around and of the tools available to help them do so.

Consistency with existing laws and regulations

9.469 As part of our consideration of the design of each of the measures in our package of remedies, we considered whether any elements of this package would be inconsistent with other relevant laws and regulations applicable to the UK payday lending sector.

9.470 A particular focus of our assessment of this aspect of remedy design has been the interaction of our remedies with regulation governing the provision of consumer credit – in particular CONC and the CCD (see paragraph 9.7). This has shaped our design of the various elements of the remedy package.

9.471 We concluded that our package of remedies, and the elements within it, are consistent with current laws and regulations applicable to the UK payday lending sector.

Coherence as a package of remedies

9.472 We considered the extent to which the remedy measures contained within our package of remedies were likely to be mutually reinforcing and identified a number of important synergies between the different elements of the remedies package.

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[897] See FCA response hearing summary, paragraphs 32–35.
[898] ibid, paragraphs 31 & 32.

9.473 First, our measures work together to support the development and use of effective PCWs by payday loan customers.[899] The introduction of new standards for payday loan PCWs and the requirement for lenders to inform customers of the availability of such comparison tools both on their own websites and in the summary of borrowing costs would all be expected to increase the use of PCWs among payday loan customers. This would encourage them to consider different lenders and compare prices before taking out a loan.

9.474 Second, our remedies may be expected to work together to increase customer awareness of the price of payday loan products.[900] The price of a loan will be the default ranking of products on authorised payday loan PCWs (see Figure 9.1) and this is likely to play an important role in driving customer decisions of which lender to borrow from, when using such sites. The summary of borrowing costs will help increase customers' awareness of the cumulative cost of borrowing, the impact of late fees and other additional charges and the potential existence of cheaper lenders in the market. Similarly, the recommendation to the FCA aimed at increasing the clarity and prominence of information on late fees and charges complements the other measures by improving the visibility of these fees, making it more likely that customers will factor them into their borrowing decision.[901] We would therefore expect this combination of measures to result in an increase in borrowers' sensitivity to differences in price between lenders.

9.475 Third, the remedies have the synergy of simultaneously addressing both the demand-side features (relating to customers' lack of responsiveness to prices)[902] and the supply-side features (relating to barriers to entry and expansion)[903] of the market which give rise to the AEC that we have found. For example, the development of effective PCWs both encourages shopping around, and facilitates entry and expansion by providing an additional channel through which new entrants and smaller lenders willing to compete on price can raise awareness of their offer and attract new customers. Similarly, we would expect developments in the provision of real-time CRA data to mitigate the competitive disadvantage that new entrants and smaller lenders face relative to more established providers, and to reduce the potentially negative

[899] See paragraphs 9.14–9.16 for further discussion on the reasons why we consider the development of an effective payday loan PCW sector to be important in order to enable payday loan customers to shop around.
[900] See paragraph 9.16.
[901] Our remedy regarding PCWs complements and reinforces the benefits of this measures by providing a convenient tool that enables customers to compare offers along this dimension to help increase their responsiveness to late fees and charges.
[902] See paragraph 8.5.
[903] See paragraph 8.6.

impact on a customer's credit record of applying for multiple loans when shopping around.[904]

9.476 We also noted the synergies between our remedies and the regulatory action that the FCA is undertaking. We consider that in the presence of the price cap, which might otherwise risk reducing price competition between lenders (eg by making entry more difficult and/or facilitating coordination), there will be increased importance attached to measures that enhance price competition between lenders. This is recognised by the FCA.[905] In addition, the introduction of new standards for PCWs and requirements for lead generators to provide improved disclosure about their services will work alongside the cap and other measures being introduced by the FCA, to help improve the reputation and perception of the payday lending sector and the market for short-term loans more broadly. We consider that a better regulated, more compliant payday lending sector with a better reputation will provide an environment more conducive to new entry – including by companies with the capability to transform the nature of competition.[906] Price competition between lenders will be made more effective. We did not identify any ways in which the objectives of the various elements of the package of remedies could come into conflict either with each other or with actions by the FCA.

9.477 We therefore concluded that this represents a coherent package of remedies, whose elements are mutually reinforcing and which support the policy aims and objectives pursued by the FCA.

Conclusion on effectiveness of remedy package

9.478 We have concluded that the package of remedies represents an effective solution to the AEC that we have found.

Proportionality of our package of remedies

9.479 Many of the matters that we have discussed above relate directly to the issue of proportionality. These include considerations relating to the detailed design of individual remedy options; the possibility that other less onerous remedy options could be effective; whether any measures in our package of remedies would result in a loss of RCBs; whether there remains a need for remedial

[904] See paragraphs 9.272–9.274.
[905] See, for example, paragraph 1.84 of the FCA's consultation paper and pp20&21 of the subsequent Policy Statement.
[906] See paragraph 7.121(a).

action in light of market developments; and the effectiveness of our remedy measures.

9.480 In the rest of this section, we summarise our assessment of whether our package of remedies would be a proportionate response to the problems we have found. We do this by considering the following questions:[907]

(a) Is the package of remedies effective in achieving its aim?

(b) Is the package of remedies no more onerous than necessary to achieve its aim?

(c) Is the package of remedies the least onerous if there is a choice?

(d) Does the package of remedies produce adverse effects which are disproportionate to the aim?

Effective in achieving its aim

9.481 For the reasons set out above, we concluded that our package of remedies would be effective in its legitimate aim of remedying the AEC and the customer detriment that is likely to continue to result from the AEC if its underlying causes are not addressed.

No more onerous than necessary to achieve its aim

9.482 In assessing whether the package of remedies is no more onerous than necessary, we considered:

(a) whether each measure within the package of remedies is required to remedy the AECs that we have found; and

(b) whether the design of each remedy measure within the package of remedies is no more onerous than it needs to be.

Is each element of the package of remedies necessary?

9.483 We considered whether it would be possible to achieve a sufficiently comprehensive solution to the AECs without implementing all of the measures in our package of remedies.

9.484 Based on our assessment in paragraphs 9.439 to 9.451 of how the elements of the remedy package contribute to remedying the AEC, we took the view

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[907] The Guidelines, paragraph 344.

that each measure made a material contribution to the effectiveness of the remedy package, such that its overall impact would be weakened if any single measure were removed from the package. The contribution to the overall impact of the package varies between remedies but each has an important role to play in addressing the AEC that justifies its inclusion in the package. They are also mutually reinforcing (see paragraphs 9.472 to 9.477). While the measures work together to address the AEC, we nonetheless considered some elements – in particular the measures to promote the development and use of effective PCWs – to be particularly important in generating greater price competition, so that they would make a significant contribution to remedying the AEC even in the absence of the other remedies. However, in order to achieve as comprehensive a solution as is reasonable and practicable to the AEC and the resulting customer detriment that we have found, we consider that the complementary effect of the various elements of the remedies package is an important aspect of the effectiveness of the package as a whole.

9.485 We concluded that it was necessary to include each of the measures in our package of remedies in order to achieve a sufficiently comprehensive solution to the AEC we have identified.

Is the design of each remedy measure within the package of remedies no more onerous than it needs to be?

9.486 Our consideration of the design and implementation of each of the measures is set out in the respective section for each measure above. In reaching our decisions on remedy design, we have sought to avoid imposing costs and restrictions on parties that go beyond what is needed to achieve an effective remedy.

9.487 For example, our approach to improving the standard of PCWs through our recommendation to the FCA to introduce guidelines on payday loan PCWs means that multiple PCWs can exist in the market (via authorisation of the respective firm operating the PCW) rather than creating a single authorised operator.[908] We also considered whether requiring lenders to publish prices on an FCA-authorised payday loan PCW was any more onerous than for an 'accredited' PCW (as we had proposed in our PDR). We identified no additional burdens to lenders. We then considered the cost to existing PCW operators. Our understanding from discussions with the FCA is that the

[908] We consider, in paragraphs 9.26–9.37, whether to have a single 'official' payday loan PCW or instead to have a commercial solution with multiple PCWs complying with minimum standards.

activities of any (consumer credit) PCW would mean that its operator requires FCA authorisation and thus there is no incremental cost in this respect.[909]

9.488 To the extent that payday loan PCW operators will be required to adhere to specific FCA guidelines rather than choose to follow those guidelines by seeking accreditation we considered that there could be a cost to existing PCWs where those PCWs fail to reach the expected standard. However, we consider that this marginal cost is justified in ensuring consumers are able to compare loans on functional and regulated PCWs which will directly address aspects of the AEC that we have found.

9.489 With respect to the summary of borrowing costs we have developed our requirement for customers to be provided with a summary of borrowing costs in such a way that lenders can use distribution channels that are most likely to be cost-effective for them (eg online lenders might distribute such a summary by means of email and/or access to an online portal) while achieving the aim of this remedy. In response to comments from Dollar we have consulted on whether amending the design of this remedy as set out in the PDR would reduce costs to payday lenders without reducing its utility to borrowers and consequently we have amended the period that the summary relates to.

9.490 We have sought to strike a similar balance in terms of remedy implementation, for example our decision to implement our remedies around credit searches and RTDS by means of a recommendation to the FCA will allow greater flexibility to market participants to implement the necessary changes compared with prescribing a specific approach via an Order. In these ways, we have sought to ensure that no measure within the package of remedies is more onerous than it needs to be, in order to address the AEC.

9.491 We therefore concluded that our package of remedies was no more onerous than necessary in order to remedy the AEC and resulting customer detriment.

Least onerous if there is a choice

9.492 If the CMA is choosing between two remedy measures which appear to be equally effective, it should choose the remedy measure that imposes the least cost or is least restrictive.

9.493 In addition to the measures included in our package of remedies, we also considered some other possible ways of addressing the AEC and/or customer detriment. These included measures that we had put forward ourselves for

[909] We are aware that some PCWs have not previously sought authorisation from the OFT or FCA.

consideration and some other measures that were put to us by parties in response to the Remedies Notice.

9.494 Our consideration of these alternative measures is set out in paragraphs 9.391 to 9.410. We found that each of these alternative measures was of limited effectiveness and/or was not needed to remedy the AEC, if the measures in our package of remedies were pursued. We were not able to identify an alternative package of measures that would be both less onerous and effective in remedying the AEC. However, we took care to avoid including measures in our package of remedies that did not make a material contribution to remedying the AEC (see paragraphs 9.483 to 9.485).

9.495 We concluded that, to the limited extent that we have a choice between effective remedies, we have identified the package of remedies that imposes the least cost and is least restrictive.

Does not produce adverse effects which are disproportionate to the aim

9.496 We considered whether the package of remedies – or any specific measure within it – was likely to produce adverse effects which were disproportionate to the aim of remedying the AEC and/or the resulting customer detriment.

9.497 In reaching a judgement about whether to proceed with a particular remedy, the CMA will consider its potential effects – both positive and negative – on those persons most likely to be affected by it. The CMA will pay particular regard to the impact of remedies on customers. The CMA will also have regard to the impact of remedies on those businesses subject to them and on other affected parties (also in light of the possible implications of the FCA's price cap), such as other businesses (eg potential entrants, or firms active in upstream or downstream markets), government and regulatory bodies, and other monitoring agencies.[910]

9.498 In paragraphs 9.499 to 9.506 we set out the benefits of the remedy package, before considering the costs in paragraphs 9.507 to 9.535 and concluding on the balance of benefits and costs and proportionality in paragraphs 9.536 to 9.540.

Benefits of remedy package

9.499 We considered the likely benefits of the remedy package.

[910] The Guidelines, paragraph 348.

9.500 As described in paragraphs 9.439 to 9.451 above, the key benefit of the package of remedies is to encourage price competition between payday lenders, in this way reducing the amount that customers pay for their loans and increasing the extent to which charges reflect the costs of supplying a given borrower. By facilitating customer access to information about the different loans available, the terms of those loans and the role of intermediaries, we would expect our remedies to increase the proportion of customers that choose the most suitable loan for their requirements.

9.501 We concluded that the scale of the detriment caused by the AEC was likely to be material (see paragraph 8.11 for an indication of the expected detriment). This suggests that the potential savings to customers as a result of heightened competition between lenders that we would expect to result from our remedies proposals, as a proportion of the detriment, are likely to be significant. As discussed in paragraph 9.435, while the price cap will reduce the extent to which customers are overpaying for their loans, and so reduce the scope for further price reductions, we nevertheless consider that there remains an important role for price competition between payday lenders under the new regulatory regime. Moreover, our competition-enhancing remedies are likely to complement and enhance the beneficial impact of the FCA's price cap and its other regulatory actions (see paragraph 9.476).

9.502 We considered the potential order of magnitude of any such further benefits that might accrue from increased competition. In our estimates of the customer detriment arising from the AEC that we found (see Appendix 8.1 paragraphs 6 to 9) we considered three possible competitive benchmarks with monthly interest rates that ranged from 22.5% to 27.5%, where the 'low-price' case competitive benchmark (22.5%) would be more relevant if the lowest prices then available in the market were more representative of the prices that we might expect to see in a market where competition was working more effectively. We note that the FCA has stated that it was confident that the implementation of the price cap (which corresponds to a monthly interest rate of around 24%, already beneath the 'mid-price' case we used in Appendix 8.1) would not prevent a viable market.

9.503 In its response to the PDR Wonga noted that our analysis had previously used a benchmark price of £25 per £100 (25%) for a one-month loan and that the benchmark had changed to £22.50 per £100 (22.5%) to reflect the introduction of the price cap. Wonga noted that the £22.50 per £100 reflected the lowest prices on offer in the market – for example those offered by Speedy Cash or CashEuroNet.[911]

9.504 We note that the expected downward trend in many categories of lenders' costs (see paragraphs 8.12 and 9.506*(c)*) will provide additional scope for lenders to reduce their prices below the level of the cap. In light of this, we consider that the 'low-price' case of 22.5% is likely to be more relevant to assess the annual detriment. Using this case, the analysis in Appendix 8.1 shows a detriment to customers from the AEC of around £74–£127 million (note that, unlike the FCA, we did not consider the savings to customers who did not pay back or paid back late, see Appendix 8.1). By applying the methodology described in Appendix 8.1, a 30-day interest rate reduction from 30% to 24% would result in an annual detriment to customers from the AEC of around £58–£102 million. Comparing these two scenarios indicates that if increased competition prompted by our proposed remedies were to reduce prices to the 'low-price' case, the additional annual customer savings to be captured by customers, over and above the benefits generated by the FCA's price cap, would be in the order of £16–£25 million.

9.505 We consider that there is substantial scope to reduce prices towards the 22.5% benchmark, and potentially further and therefore would expect the large majority of the calculated detriment to become a benefit to customers. The cost-benefit analysis (see paragraphs 9.536 to 9.539) shows that the remedies would still be proportionate even if only a small proportion (less than 20%) of the detriment calculated using the 22.5% benchmark was captured by customers (this is based on the one-off costs of £2.5 million in year 1 and the low calculated detriment (see above) of £16 million. In future years less than 10% of this detriment would need to be captured by customers).

9.506 We considered that the scope for customers to benefit from increased price competition as a result of our remedy package would continue to be material, notwithstanding the FCA's price cap. We reached this view in light of the following considerations:

(a) The likely future size of the market. Total revenue in the payday lending sector was around £1.09 billion in financial year 2012, or approximately £107 per loan. While this figure is likely to have fallen in 2013 (see Appendix 4.5 which describes the recent financial performance of the major lenders) and may fall further in the presence of the cap[912] we have seen no indication that the underlying demand for short-term loans will

[911] Wonga response to the PDR, paragraphs 5.12 & 5.13.
[912] Partly because many customers will be paying less for their loans and also as lenders tighten their lending criteria.

reduce dramatically. We also note that the FCA has set the cap at a level at which lenders will continue to be able to meet the majority of this demand. The FCA estimates that most payday loan customers will still be eligible for loans after the introduction of the cap and that only 7% of individuals who would otherwise get HCSTC would no longer get loans. We would therefore expect a significant market for payday lending – as defined in our terms of reference – to remain following the cap.

(b) The weakness of price competition in the absence of the remedy package, as evidenced by the extent of historical customer detriment that we had identified as arising from the AEC (see paragraphs 8.9 to 8.13). As set out in paragraphs 9.420 to 9.427, the price cap is unlikely to address the underlying causes of the AEC.

(c) The intrinsic limitations of a price cap in fully addressing the customer detriment arising from the AEC, as set out in paragraphs 9.428 to 9.430, particularly once dynamic considerations are taken into account, and the continued scope for price competition under the cap, given:

(i) the differences in the efficiency of different lenders (and so the significant potential for differences in costs to be reflected in lenders' prices);

(ii) the differences in the expected costs of supplying different customer groups (and so the significant potential for the costs associated with different types of customer to be reflected in the prices that they pay); and

(iii) the expected downwards trend in many categories of lenders' costs which account for a considerable proportion of the total costs incurred by lenders (and so the significant potential for any cost reductions to be passed on to customers). For example, we would expect the cap to drive down the costs of acquiring customers through lead generators.[913] Similarly, any improvement in CRA data is likely to have a beneficial effect on lenders' ability to assess risk and therefore on their costs associated with doubtful debt.[914]

(d) Our conclusions on the effectiveness of our package of remedies as set out in paragraph 9.478.

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[913] Customer acquisition expenses accounted, on average, for around one-fifth of the 2012 total costs of the major online payday lenders (see paragraph 7.38) and a third of these expenses were to lead generators (see Table 7.2).

[914] The costs associated with doubtful debt represented around 45% of total costs for all lenders in 2012 (see paragraph 7.79).

Costs of remedy package

9.507 We considered the potential scale of the costs generated by the remedy package.

- *Price comparison website remedy*

9.508 One aspect of the package that may generate material costs is our proposal to require lenders to provide data to one or more authorised payday loan PCWs. We considered below the extent to which lenders, the FCA and the firms operating PCWs seeking authorisation might incur additional costs as a consequence of this remedy.

9.509 As part of our consultation on the remedy package we collected views from lenders on the costs associated with providing data to one or more accredited[915] PCW operators. More specifically, we asked lenders[916] to provide estimates of any set-up cost and any recurrent/ongoing costs related: *(a)* to publishing details of their loans on an accredited PCW, and *(b)* to displaying a hyperlink prominently on their website to at least one accredited PCW.

9.510 Overall the total costs of the remedy to lenders appear to be limited. Estimates of the set-up costs vary between £3,000 and £12,000 with an average of £8,000. The recurrent costs are estimated to be on average around £5,000 per year.[917] We also noted that lenders would incur referral (or click-through) fees for any customers they acquired through accredited PCWs.[918] However, lenders would be able to negotiate commercial terms and would receive a commercial benefit in return for these fees (ie additional customers). In addition, any additional costs to lenders associated with the use of PCWs are likely to displace other costs in the distribution of payday loans (eg the costs to lenders of acquiring customers through lead generators, or direct advertising). Consequently, we do not consider any additional referral fees that lenders might pay to authorised payday loan PCW operators to be a relevant cost of this remedy. Based on the cost estimates provided, we consider that one-off costs of implementing the remedy and the ongoing

[915] In our proposed design and implementation in the PDR we consulted on the costs associated with an accredited PCW. As noted, we subsequently undertook an additional consultation on the amendment to the implementation of the remedy through new standards introduced as part of FCA authorisation of payday loan PCWs. With respect to the cost to lenders we have not identified significant differences between our original proposal and our amended implementation through FCA authorisation.
[916] Six of the 11 major lenders responded to our request for information, namely Wonga, CashEuroNet, Dollar, Global Analytics, SRC and MYJAR.
[917] Some lenders (SRC and MYJAR) submitted that these costs would be minimal and/or part of their ‘business as usual’ activity.
[918] See paragraphs 9.56–9.67.

compliance cost would be unlikely to exceed, respectively, £400,000 and £250,000 per year.[919]

9.511 We considered the cost of the remedy to the FCA and to the operators of PCWs.[920]

9.512 To estimate the potential costs incurred by the FCA, we sought to understand what the costs of operating a stand-alone (ie unrelated to other relevant regulatory activity) set of standards would be.[921] We considered the nature of the activities undertaken by the relevant body. Ofgem[922] told us that, for its accreditation scheme, it used a third party 'auditor' whose contract envisaged [✂] of external review per website per year. This review consisted of checking the comparability of a PCW's results to other accredited PCWs.[923] In addition, Ofgem staff conduct quarterly audits of each site. Currently, Ofgem did not charge any fee to PCWs for the audit, although this position is currently being reviewed.[924] The accreditation scheme also included a self-assessment of compliance by the PCW operator which was then reviewed by Ofgem staff and the auditor. The 'one-off' accreditation of a site is contracted at [✂] hours per website. Ofgem typically deployed two to three full-time equivalent (FTE) staff who oversaw the accreditation and audit scheme, and management of the Ofgem Confidence Code.

9.513 Ofcom[925] told us that to be accredited by it sites were required to undergo an initial audit and to undertake 18-month review audits[926] to ensure information was accurate and correctly presented. The direct cost to PCWs of accreditation related to the cost of a technical audit from an independent analyst

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[919] This is based on the following assumptions:

- Set-up costs of £8,000 per lender;
- Annual ongoing compliance costs of £5,000 per lender; and
- 50 payday lenders operating in the market: of 100 responses we received to our market questionnaire (see Appendix 2.5) from companies who operated in the payday sector at some point between January 2010 and October 2013, more than 20 had left the market as at October 2013. Considering that the price cap is likely to significantly reduce lenders' revenues, and consequently lead to the exit of a number of less efficient/well-resourced lenders (see paragraph 7.113), we think that this assumption is unlikely to underestimate the number of lenders that will be operating in the market following the introduction of the cap.

[920] In our PDR we identified that that there would be some relevant costs associated with an accreditation scheme, principally *(a)* an accrediting body operating the scheme; and *(b)* PCWs complying with the scheme criteria. Subject to the terms of any accreditation or supervisory regime, the costs incurred by the body responsible for supervising the scheme or regulating the operators may pass those costs through to the operators of PCWs.

[921] This information was gathered in reaching our PDR from Ofgem and Ofcom which currently run accreditation schemes in the energy and telecommunications sectors.

[922] There are presently 11 accredited website operators.

[923] Practically, this involves inputting six standard customer profiles into each PCW and comparing the top 10 to 20 ranked energy suppliers.

[924] Domestic third party intermediaries (TPIs): Confidence Code and wider issues.

[925] There are presently five accredited website operators.

[926] The first review will take place 12 months after initial accreditation and every 18 months thereafter.

commissioned directly by Ofcom through a periodic competitive tender process. For PCWs with a relevant turnover greater than £200,000, Ofcom recovered most of the costs of the audit fee from PCWs by charging £13,775 (initial audit) and £8,550 (review audit). In order to ensure that the costs of accreditation did not become a barrier to entry, Ofcom charged discounted fees to smaller PCWs (with a relevant turnover of less than £200,000)[927] and subsidised the costs of the technical audit. Ofcom had two staff who managed and oversaw the accreditation scheme in addition to other duties, and estimated that the scheme required approximately 0.6 FTE employees.

9.514 On the basis of Ofgem's and Ofcom's experience, we considered that the total costs to the regulator and PCWs[928] of operating and complying with an accreditation scheme would be unlikely to exceed £300,000 a year on average.[929] We would expect costs to be somewhat higher than this in the first year, as additional resources would be required to set up the accreditation scheme and to accredit the initial providers. Conversely, we would expect costs to be somewhat lower than this once the scheme had been established. Although this is only an indicative estimate of the magnitude of the overall costs, it strongly suggests that operation of the accreditation scheme is likely to result in only modest costs relative to the size of the payday lending market (see paragraph 9.506*(a)*) and the calculated detriment.

9.515 We next considered whether the costs that the FCA would have to incur under an accreditation scheme would be likely to differ materially from the cost of the FCA authorising payday loan PCWs.

9.516 We considered the specific types of cost that would need to be incurred by the FCA.

(a) The cost of establishing the scheme. We considered that under either an accreditation scheme or new standards for payday loan PCWs (introduced as part of its authorisation of credit brokers) the FCA would need to undertake a statutory consultation of the scheme criteria.[930] We

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[927] £1,000 for initial audit, and £500 for review audit.
[928] We consider the cost to the accrediting body and the PCWs of compliance together, as the nature of the pass-through of costs incurred by the accrediting body may vary.
[929] This estimate is based on the following assumptions: *(a)* the cost of any technical audit to grant accreditation to a PCW would be in the region of £10,000–£12,000 per year. If we assumed for indicative purposes that ten PCWs were granted the accreditation – which may overestimate the number of accredited websites, given the difference in the size of the payday lending market compared with energy or telecommunications – the total cost of audit would not exceed £100,000–£120,000 per year; and *(b)* based on the experience of Ofgem and Ofcom, the operation of the accreditation scheme might require one or two FTE employees of the regulator. If we take an indicative cost per FTE employee of £100,000 a year, the total cost for the FCA of supporting the scheme might be in the region of £100,000–£200,000 per year.
[930] The FCA has a statutory requirement to make and maintain effective arrangements for consulting practitioners and consumers on the extent to which its general policies and practices are consistent with its general duties.

considered that an accreditation scheme would require an overarching framework, but that introducing new standards as part of the authorisation of payday loan PCWs would similarly require the FCA to develop a number of high-level rules or guidelines to amend or accompany the Consumer Credit Sourcebook.

(b) The cost of authorising PCWs and their operators. We understand that any operator of a payday loan PCW would be expected to seek authorisation by the FCA regardless of the introduction of a PCW remedy. As such, we considered that having separate authorisation and accreditation processes could increase costs relative to introducing enhanced standards for authorised credit brokers in the Consumer Credit Sourcebook.

(c) The cost of ongoing supervision. To the extent that the PCW and its operator would be subject to the same level of scrutiny under either scheme, we did not identify any difference in costs. However, where supervision is able to be incorporated into ongoing supervisory activities across authorised credit brokers, there may be some efficiency benefits.

9.517 As with the accreditation scheme, the direct cost of supervising compliance with new standards for authorised payday loan PCWs would be borne by the FCA. We have identified that implementation through either route would be unlikely to result in the FCA incurring a materially different level of direct costs.[931]

9.518 Introducing additional specific standards for payday loan PCWs might generate additional costs for payday loan PCWs, regardless of whether the remedy was implemented via an accreditation scheme or the FCA's existing regulatory framework. For example, PCWs may have to bear the costs of managing the payday loan comparison table and monitoring/complying with the required standards. However, we expect that such additional costs – over and above the costs that would need to be incurred in any case – are likely to be very small, given the approach we have proposed to the authorisation criteria.[932] We did not identify any reason why the cost of compliance would differ significantly between the two methods of implementation.

Section 1M of the Financial Services and Markets Act 2000 (ss 1A-3S substituted by the Financial Services Act 2012 s.6(1)).
[931] The FCA finances itself by charging fees to authorised firms in financial markets.
[932] [✂] told us that the costs of managing payday loan data and ensuring compliance would be approximately around £40,000 per year, though if an infrastructure/system is in place already to promote other products, 'the additional cost of managing payday loans is virtually zero'.

9.519 Clearly, new PCW operators seeking to provide payday loan comparisons (and subsequently seeking authorisation) would have to incur additional costs to develop a website on which to present payday loan information. Under the remedy set out in our PDR, we envisaged that PCWs would voluntarily seek accreditation. However, under FCA authorisation, any existing PCW offering comparisons of payday loans would need to adhere to the enhanced standards and thus will have to incur any costs associated with upgrading the functionality of its existing PCW. There is no imposition on generalist PCWs to include a payday loan comparison table on their site or to adhere to the specific standards required for payday loans. However, all things remaining equal we acknowledge that the cost of establishing a legally compliant payday loan PCW will increase.

9.520 We consider that the increase in costs is likely to be modest and to be justified by the enhanced consumer outcomes anticipated from PCWs offering meaningful and transparent comparisons. Ultimately we expect that PCW operators are likely to choose to be present in the market on the basis of commercial considerations as to whether they can profitably design and operate a payday loan comparison site. For this reason, and given that no party has responded to our consultation with concerns that we have deterred entry to the market, we do not consider that any additional costs related to the development of new PCWs are significant considerations in the assessment of this remedy. We note further that any additional costs incurred by new entrants would be directly linked to providing a consumer-focused service with greater functionality.[933]

9.521 We considered whether the other parts of our package were likely to generate significant costs for payday lenders or other parties. The remedy relating to disclosure of late fees (see Figure 9.2) could be implemented with relatively

[933] Although we considered it unlikely, we identified the need for a fall-back should no third party choose to operate a payday loan PCW (see paragraphs 9.187–9.196). We would expect this to be implemented by means of a competitive tender process, the outcome of which would determine the cost to lenders of the remedy, in this scenario. In this context, we noted that [✂] told us that the cost of developing a price-table solution from scratch depended on the degree of sophistication, but an indicative estimate to have an 'up-and-running service' would be in the region of £[✂]. Similarly, [✂] said that implementing a complete system from scratch (which would entail 'an admin system to manage data, an admin system and processes to manage commercial agreements and proprietary tracking and reporting') would cost more than £1 million. However, we noted there exist alternative solutions that may limit the set-up costs. For example, [✂] told us that its comparison tables (except for that covering six core insurance products) were powered by third party providers, which hosted the tables and provided the relevant data. This enabled [✂] to add products to its range quickly, without needing particular expertise specific to the sector. In the case of financial products, its comparison tables were provided by [✂] whose service was remunerated on the basis of the volume of products sold through [✂] comparison table that it hosted (ie the revenues generated by the comparison table are shared between [✂] and [✂]). We also noted that the total set-up costs for establishing lenderscompared.org.uk had been substantially less than £0.5 million (see paragraph 3.56 of our PDR for more detail on its establishment). We therefore considered that if lenders were required to create or commission an authorised website the total costs of establishing such a site would be very unlikely to exceed £1 million and could be substantially less than this.

simple changes to lenders' websites and documentation, and we do not expect these changes to generate significant costs.[934] The summary of borrowing costs (see Figure 9.7) and transparency of lead generators' role (see Figure 9.8) would each require lenders and lead generators to change the way some information is presented to customers. We collected views from lenders and lead generators on the costs they would incur to implement these remedies.

9.522 The costs of implementing our requirement to provide a summary of borrowing costs will vary between lenders. Many lenders already allow customers to view aspects of their borrowing record on their website (through 'my account' type functions) and could build upon these functions to meet the requirements of this remedy. [935] Some lenders that do not currently provide this type of service to customers through their website might need to undertake additional development work.

9.523 Estimates provided by lenders suggest that the development costs associated with this remedy may vary by lender from £6,000 to £53,000[936] with an average of £22,000. Any recurrent costs associated with distributing the summary and informing customers of how to obtain the summary are considered to be small by online lenders (on average £2,500 per year).

9.524 One high street lender (Dollar) submitted that the costs of processing the summary requests may be around £[✂] per year. This estimate is based on the assumption that each request would require 5 minutes of staff time in a store (in addition to the cost of printing) and given that its stores were currently operating at full capacity, implementing the remedy would require Dollar to incur additional staff costs[937] to process the requests.

9.525 We consider Dollar's figure to be an overestimation of the potential cost. First, once the system is in place, we expect that the generation of a summary would be largely automated and thus this would not materially increase the time taken to complete an application. Second, while some customers may raise queries as a result of receiving a summary we consider that any query requiring 5 minutes of staff time would be at the upper end and that the average marginal amount of staff time required would be much lower.

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[934] Our expectation is based on what we have been told by a number of interested parties, see Appendix 9.2, paragraphs 115–118.
[935] See Appendix 9.2, paragraphs 177–183.
[936] The highest estimate, submitted by one lender ([✂]), is twice as large as the second highest estimate provided by lenders. The figure is largely driven by the expected technical/software costs to implement the remedy.
[937] Either as a result of employing additional staff or introducing longer working hours for existing employees.

9.526 We further noted that the amount of time taken to complete an application in-store for a number of lenders varied from 5 to 30 minutes[938] and for returning customers we assume that the time taken would be reduced given that the lender would already hold a significant proportion of the relevant details necessary to complete an application. In this context we further considered that the 5-minute estimate would overestimate the time spent by borrowers in reviewing the summary. Furthermore lenders would have the option to send the summary by post or, subject to customer preference, by email.

9.527 We considered Dollar's estimate of the resource cost of producing summaries of 48,000 man hours per year in greater detail. Assuming that its network of 500 stores are open 300 days per year[939] this would equate to a marginal increase in processing time of just under 20 minutes per store per day[940] which we would anticipate being shared over a number of members of staff and we expect could be carried out, to a large extent, by existing staff within their regular working hours. Lenders would also have the opportunity of either offering to provide online summaries or sending summaries by post, should either option be less costly.

9.528 We noted that SRC, which also operates high street branches (under the Speedy Cash brand), did not indicate any material costs associated with generating and processing summaries.[941]

9.529 Overall we considered that the one-off cost of implementing the remedy and the ongoing compliance cost would be unlikely to exceed, respectively, £1 million and £250,000 per year.[942]

9.530 Regarding the remedy on the transparency of lead generators' role, most lead generators submitted estimates of the set-up costs ranging from zero to £8,000. One lead generator (Quiddi Hub Limited) estimated substantially higher costs (£48,000) based on 'previous experience in new software development where the scope is very broad as the terms of reference for this

[938] See Appendix 2.1, Table 4.
[939] Assuming stores are closed on Sundays, Bank Holidays and some allowance for staff training.
[940] This assumes that customers requesting a summary are distributed equally over stores. Using Dollar's assumption of 5 minutes per application, this would suggest that each store processes only four loans per day, or that the estimate of 5 minutes overestimates the average time spent.
[941] SRC submitted that the total costs, including both set-up and recurrent costs, would amount approximately to £17,500, with the majority of them incurred to set up the remedy.
[942] This is based on the following assumptions:

- Set-up costs of £20,000 per lender.
- Annual ongoing compliance costs of £5,000 per lender: while this may overestimate the costs for online lenders, it may underestimate the costs for high street lenders. However, considering that online lenders account for the majority (70–80% in 2012) of the volume of payday loans, our assumption is likely to be overall an overestimate of the total costs incurred by lenders.
- Fifty payday lenders operating in the market: see footnote 919 for further details on the rationale behind this assumption.

remedy are not sufficiently defined to give exact estimations'. We consider, however, that the measures we recommend to the FCA to implement would essentially require fairly limited changes to the code and the design of the website and they are unlikely to require the development of a completely new software. In light of this, we consider that a more realistic estimate of the set-up costs would be on average around £3,000 per lead generator.[943]

9.531 Eight out of 17 lead generators who provided estimates of the remedy's costs indicated that the remedy would not entail any additional cost for compliance and monitoring. While one lead generator submitted an estimate as high as £36,000, few estimates were in excess of £10,000. We note, however, that the costs indicated by these lead generators include activities such as compliance with existing regulations, server maintenance and monitoring website performance. To a very large extent these would be incurred by lead generators in any case as part of their routine business activities and are not caused by our remedy. For this reason, we consider a more realistic estimate of the annual ongoing costs of the remedy to be on average around £2,000 per lead generator.[944] Overall, we consider that one-off costs of implementing the remedy and the ongoing compliance cost would be unlikely to exceed, respectively, £240,000 and £160,000 per year.[945]

9.532 In addition to the development costs discussed in paragraph 9.521, the remedies relating to disclosure of late fees, summary of borrowing costs and transparency of lead generators' role could potentially involve a more indirect cost for customers if they make the navigation of websites more cumbersome. Customers may dislike having to click through more screens to take out a loan. Moreover, if customers can only process a limited number of messages, then the provision of additional information has an 'opportunity cost' in that customers are likely to pay less attention to other messages. We have sought to keep the disclosures in our remedy package simple and would expect

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[943] This is based on the average of the cost estimates submitted by lead generators if we exclude Quiddi Hub Limited's estimate.
[944] This is based on the average of the cost estimates submitted by lead generators if we exclude estimates above £10,000 per year.
[945] This is based on the following assumptions:

- Set-up costs of £3,000 per lead generator.
- Annual ongoing compliance costs of £2,000 per lead generator.
- Eighty lead generators operating in the market: we note that 130 lead generators were operating in 2012 (see paragraph 2.134). As part of our assessment of the costs of remedies, we sent a request for information to 27 lead generators, of which three did not reply and one said that it was not a lead generator. Of the remaining 23 lead generators, 5 (approximately 20%) indicated that either they had left the market recently or they were developing a new product. Applying this rate of exit to the 130 lead generators identified in 2012 would result in approximately 100 lead generators remaining in the market. In addition, we noted that the cap may lead to the exit of some of these intermediaries from the market (see paragraph 6.122). For the purposes of estimating the costs of our remedy we assumed that the cap will trigger a similar rate of exit as the one observed on the sample of lead generators responding to our request for information, which would further drive the number of lead generators operating in the market down to 80.

lenders and lead generators to have strong incentives to manage the implementation of these remedies to ensure that their websites continue to be easy to use, while providing customers with the relevant information prescribed in these remedies. As such, we did not expect this type of indirect cost to be material.

9.533 We noted that our remedies to assist customers to assess their own creditworthiness and to encourage the development of RTDS have been framed as broad recommendations to the FCA. We would consequently expect the FCA to take into account any material costs associated with these measures prior to imposing more specific obligations, should it decide to do so.

9.534 Finally, we considered the risks of our package of remedies leading to more indirect costs or unintended consequences. We considered the following risks:

(a) **PCW operator market power**. If our remedies result in PCW operators acquiring market power in the distribution of payday loans, then this might lead to increased commissions for lenders and higher prices to customers. In our view, the risk of PCWs acquiring significant market power in the payday lending market as a result of our intervention is small, as we expect there will be a number of authorised payday loan PCWs and that barriers to entry for PCWs seeking authorisation in this sector are likely to be low. Nevertheless, we expect PCW operators to be aware of their obligations under Chapters I and II of the 1998 Act and Articles 101 and 102 TFEU and of the concurrent competition powers of the FCA and CMA, and to ensure compliance as appropriate.

(b) **Distortions due to the requirements of authorisation**. If the requirements for FCA authorisation are too prescriptive then this could raise barriers to entry or stifle innovation in the payday loan PCW sector. However, we do not believe that this is a serious risk given the criteria that we have recommended to the FCA to establish. They leave considerable discretion to PCWs with respect to how they present information to customers and the commercial terms they agree with lenders. There is no indication that similar schemes have stifled competition in other sectors.

(c) **Reduced role of lead generators**. One potential consequence of the remedies is that they could result in a significant reduction in the extent to which customers use lead generators (as understanding of the service offered by these suppliers improves). A smaller proportion of applicants available via lead generators could potentially create difficulties for new entrants and small lenders who are currently heavily reliant on this channel to acquire new customers. However, we believe that a stronger

payday loan PCW sector could provide these lenders with an alternative way of acquiring new customers, in a way that is likely to be more beneficial to customers and competition.

(d) **Encouraging inappropriate use of payday loans**. One argument put to us was that a more effective payday loan PCW sector might encourage the use of payday loans, with detrimental consequences for those customers for whom a payday loan is not the most suitable credit product.[946] Related to this, we were conscious of the FCA's findings that many of the highest-risk payday loan customers may have been made worse off as a result of taking out their payday loan. Nevertheless, we considered that this risk would be best managed by the FCA – for example, by regulating how lenders apply the affordability criteria, as well as the protections offered by the price cap – rather than allowing the AEC to continue.

9.535 In light of this assessment, we considered that the costs associated with putting in place our package of remedies were likely to be limited. We reached this view in light of the following considerations:

(a) There would be some ongoing costs to the FCA associated with supervising authorised payday loan PCWs. Based on our assessment in paragraph 9.514, these costs are unlikely to exceed around £300,000 a year. Lenders may also incur some costs in publishing details of their loans on a PCW and displaying a hyperlink on their website to at least one authorised payday loan PCW. These costs overall are unlikely to exceed £650,000[947] in the first year of the remedy implementation and £250,000 in any subsequent year (see paragraph 9.510).

(b) There would be some costs to lenders associated with our remedy relating to the summary of borrowing costs. We estimated that these costs are unlikely to exceed £1,250,000[948] in the first year of the remedy implementation and £250,000 in any subsequent year (see paragraph 9.529). We do not expect the remedy relating to disclosure of late fees to generate any significant costs.

(c) There would be some costs to lead generators associated with our remedy relating to improving the transparency about the role of these intermediaries. These costs are unlikely to exceed £400,000[949] in the first

[946] Dominic Lindley response to Remedies Notice.
[947] This includes the set-up costs as well as the ongoing compliance costs in the first year of the remedy implementation.
[948] See footnote 947.
[949] See footnote 947.

year of the remedy implementation and £160,000 in any subsequent year (see paragraph 9.531).

(d) Our remedies to assist customers to assess their own creditworthiness and to encourage the development of RTDS have been framed as broad recommendations to the FCA on how it should seek to shape market developments to benefit customers and enhance the competitive process. They do not contain specific obligations on firms. We are not therefore in a position to estimate specific costs that may ultimately arise from these recommendations, but we would expect the FCA to take into account the main costs associated with any subsequent actions, if it decided to impose more specific obligations.

(e) Our remedies have been designed in such a way to minimise the risk of unintended consequences. In particular:

(i) we do not expect our remedies to result in PCW operators acquiring market power in the distribution of payday loans, or the authorisation criteria to raise barriers to entry or stifle innovation in the payday loan PCW sector;

(ii) a stronger payday loan PCW sector would provide lenders, which currently rely heavily on lead generators and might therefore suffer from a reduced role of these intermediaries, with an alternative way of acquiring new customers; and

(iii) we expect the FCA to monitor and intervene to prevent any inappropriate use of payday loans which could be encouraged by the wider availability of price comparison tools.

Balance of benefits and costs

9.536 We considered whether the benefits of the remedy package exceeded its likely costs.

9.537 We concluded in paragraph 9.506 that the benefits from increased price competition as a result of our remedy package would continue to be material, notwithstanding the FCA’s price cap. Set against these benefits, we considered, for the reasons set out in paragraph 9.535, that the costs of implementing our remedy package were likely to be modest. While we have not quantified every aspect of our remedies, we consider that the total costs associated with the remedy package are unlikely to exceed around £2.5 million in the first year of the package implementation and £1 million for any subsequent year. By comparison we consider there is substantial scope to reduce prices and the remedies would still be proportionate even if only a small proportion of the detriment calculated was captured by customers (see paragraphs 9.504 and 9.505). We expect that a substantial proportion of the detriment would be captured by customers.

9.538 Put another way, the package of remedies would need to result in only a very small further reduction in lenders' prices for the benefits to customers to exceed the costs of the package that is being decided. To place such a price reduction into context, the price cap would limit the upfront interest and fees chargeable on a £100, 30-day single repayment loan to £24. Considering a cautious estimate of the future size of the payday lending market,[950] a reduction of around 10 pence in the first year and of around 4 pence[951] in any subsequent year would be sufficient to outweigh the costs of the remedy package. For the reasons set out in paragraphs 8.12 to 8.13 and paragraphs 9.499 to 9.506 such reductions may be supported by efficiency savings made by lenders and we consider that the remedy package is likely to lead to an overall reduction in prices of substantially more than this.

9.539 We have therefore concluded that the benefits of the remedy package are likely to exceed its costs and that, consequently, the remedy package was unlikely to give rise to adverse effects that were disproportionate to its legitimate aim.

Conclusion on proportionality

9.540 We concluded that our package of remedies represented a proportionate solution to the AEC and resulting customer detriment.

Decision on remedies

9.541 We have decided that we should introduce the package of remedies summarised in paragraph 9.437.

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[950] We assumed the future size of the market to be £600 million. The market size by revenue was around £1 billion in financial year 2012 (see paragraph 9.506(a)). The FCA estimated that the price cap would reduce lenders' revenue by 39% (which would imply a market size by revenue of approximately £600 million). The FCA, however, noted that its estimate was based on a cautious assumption that the reduced levels of lending at August 2014 would continue, but it considered it likely that 'lending volumes will recover to some extent, as firms see reduced regulatory uncertainty following the imposition of the cap and having completed authorisation.' (FCA, PS 14/16, p33).

[951] A reduction in lenders' prices of 0.42% would generate savings to customers equal to the costs of the remedy package in the first year. A 0.42% reduction in the cost of this loan (£24) would be around 10 pence. Similarly, a reduction in lenders' prices of 0.17% would generate savings to customers equal to the costs of the remedy package in any subsequent year which in turn would imply a reduction in the cost of this loan of around 4 pence.

9.542 In our judgement, this represents as comprehensive a solution as is reasonable and practicable to the AEC and resulting customer detriment that we have found.