# CREDIT WHERE IT'S DUE

## OVERCOMING THE BARRIERS TO MAINSTREAM CREDIT WITH DATA

The Financial Inclusion Commission in its 2015 report found that too many people are still excluded from mainstream credit. One of the key challenges to financial inclusion is the credit gap faced by people on low incomes who are not served by the mainstream market.

Policy in Practice has been commissioned by the Financial Inclusion Commission to investigate how public sector data can be used to widen access to mainstream credit, and improve the credit files of those who may be at risk of financial exclusion.

There are clear opportunities from the wider use of data to boost financial inclusion. Data is increasingly being seen as an asset, inside and outside of government. The introduction of Universal Credit puts an emphasis on financial inclusion, and will hold information that can be used to widen access to financial services.

The literature shows the extent of financial exclusion, with mainstream credit inaccessible to 6 million people in the UK. Young people and migrant workers are most likely to have no credit file at all, whereas poorer households, older people and social tenants often have 'thin' credit files, with limited evidence to apply for credit. This leads people to borrow from alternative lenders, such as doorstep and payday lenders, at high interest rates. No, or limited, evidence in credit files is a key driver of this form of financial exclusion.

We built on our past research and looked at recent initiatives into financial inclusion, particularly to access mainstream credit, and on data sharing. We have outlined the key barriers to sharing data and highlighted learning from where these have been overcome. We have also spoken to credit reference agencies, lenders and owners of non-traditional sources of data to assess the impact of using and opening up this data.

The credit reference agencies and lenders we spoke to would value extra evidence in credit files. This would be valuable for three parts of the credit process: for **identification and verification**; to **assess risk and creditworthiness**; and in **assessing affordability**.

Unless applicants can verify their identity and address, they won't be able to access mainstream credit. The three credit reference agencies referred to the identification and verification stage of the credit process as the "gateway", or the first stop towards affordable credit.

Lenders take different views on creditworthiness. A mainstream bank lending a mortgage over 25 years will accept a different score to a high street lender for white goods lending over three years. But whereas the credit score protects the lender, the affordability check ensures the borrower can repay comfortably, without stretching themselves. Regulatory pressure has put more emphasis on these affordability checks as part of the credit process.



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We then focused on understanding the barriers to the wider use of data, and where these had been overcome. There are privacy issues, technical barriers and market hurdles. We also looked into the approach to sharing data across institutions. This reinforced our view of the power of data and the general movement towards more and better use of data.

The recent Digital Economy Act, which seeks to break down costly barriers to data sharing within the public sector, is complemented by regulatory initiatives such as Open Banking as directed by the Competition and Markets Authority, and private sector programmes including the Rental Exchange. We found that public sector and other non-traditional data sources offer the opportunity to develop a more complete credit profile. Universal Credit places an emphasis on promoting financial inclusion, and alongside other government initiatives including GOV.UK Verify and Real Time Information on earnings, builds a rich pool of data that could be used by government to improve a range of outcomes, including financial inclusion.

Technical barriers include the ability to match non-traditional data with evidence already on credit files, as well as issues around data quality, privacy legislation and the ability to obtain the proper consent to allow for the sharing of data from public sector agencies and the lending market. Experian's Rental Exchange programme shows that these technical and privacy hurdles can be overcome. Although credit reference agencies need to understand, clean and turn any new source of data into evidence in credit files, they already have the experience to do this with data from a large number of varied sources. Standardised datasets, of the sort that already exist within the public sector, make it even simpler for analysis to be carried out at scale. Overcoming privacy issues by obtaining informed consent is possible, as shown by a range of initiatives including the Rental Exchange where opt-out rates were less than 1%.

Market acceptance of new sources of data may be a bigger challenge than the technical barriers. Lenders need to be convinced that new sources of data on credit files will improve their lending decisions. The lenders we spoke to were keen on having more data in credit files. One stakeholder told us that newer lenders, in contrast with the traditional banks and building societies, are most likely to accept new sources of data where they can see a statistical improvement in scores. We also have examples of telephone and utility data now being incorporated, and accepted, in credit files.

This report looks at the positive impact of a small number of datasets on the ability of people with thin or no credit files to gain access to mainstream credit. Lenders, credit reference agencies, local authorities and housing associations see the benefit in boosting credit files for people with no or limited evidence in their files. Evidence from Rental Exchange and administrative datasets including Housing Benefit data shows how these new data sources boost credit files:

- A big jump from 39% to 84% in digital identity authentication for social tenants when rent data is included in credit files;
- In 76% of cases, tenants with no significant arrears see their credit score improve, whereas only 8% of tenants have rent arrears, suggesting it helps ten times as many households as it harms.
- Additional information on household income and earnings could encourage lower income thresholds for loans, making an additional 4.8m consumers attractive to lower cost lenders.

A broader analysis of the available datasets, including transactional data on payments to government and on rents, could help many more households. A wider view of the benefits to financial inclusion and, more broadly, to the government and its partners in tackling exclusion and vulnerability, would also indicate that the potential gains are underestimated. Using benefit data to assess financial resilience, the report finds 47% more households in work are financially vulnerable, compared with traditional measures.

Government legislation to open up public sector data is crucial for this to succeed. The collection of data can be done at a local or a national level and electronic 'data wallets' with informed consent offer different ways to collect and share this data. The barriers to sharing data can be overcome, but require legislation that recognises the benefits as well as the risks. Universal Credit is a great opportunity for doing this, because of the scale of information it will collect, but it must be backed up by education to show the public the real value in sharing data with their active and informed consent. Lenders also need to have a more sophisticated understanding of lower income consumers, and how the information on them can help them to open up markets and lend responsibly.

## ABOUT POLICY IN PRACTICE

Policy in Practice believes the welfare system can work more effectively. It can improve living standards and help people towards greater independence if we make it simple for people and organisations to understand.

We show local authorities how individual households are affected by all policy changes, now and in the future.

0330 088 9242
hello@policyinpractice.co.uk
www.policyinpractice.co.uk

## ABOUT FINANCIAL INCUSION COMMISSION

The Financial Inclusion Commission is an independent body of experts drawn from frontbench UK politics, senior management roles in financial services, businesses and the charity sector, national regulators and academia.

commission@UKFinclusion.org.uk
www.financialinclusioncommission.org.uk