Annexe C

Supplementary analysis from the OFT's consumer survey and other sources of data

June 2010

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1 INTRODUCTION TO CONSUMER RESEARCH

1.1 This annexe presents some detailed analysis of the consumers of a number of high-cost credit products and some mainstream credit products. It examines the general nature of credit users in the UK, as well as users of home credit, payday lending, and some types of credit and store card users.

1.2 The information presented in this annexe is sourced from the OFT survey of consumers carried out in 2009 as part of this review, and data from research entitled 'The new demand landscape for credit provision to those on low incomes and the implications for provision of affordable credit'. This research project was undertaken by Policis with funding from the Friends Provident Foundation and was supported by an advisory board which included a variety of domain experts and national stakeholders, including representatives from various government departments. Both Policis and the Friends Provident Foundation have kindly agreed to allow the OFT to present this information in our report.

1.3 The structure of this annexe is set out as follows:

- Chapter 2 provides some analysis of users of credit generally, and some specific analysis from the OFT's survey in relation to users of home credit.

- Chapter 3 considers users of mainstream credit and store cards who are experiencing a degree of financial stress and some difficulty in repaying their debt. This group of users is selected as a useful comparator group to users of high-cost credit. The data for this analysis was sourced from the OFT's consumer survey.

- Chapter 4 provides some analysis of users of payday loans. The findings draw mainly on the research described above undertaken by Policis and funded by the Friends Provident Foundation.
2 USERS OF HOME CREDIT

Introduction

2.1 In our interim research report we published some initial research from our consumer survey. Since then, we have undertaken further analysis of this survey and we now present the main results from this analysis in relation to credit use generally and specifically home credit.

Summary of analysis

2.2 It is important to be aware that a substantial proportion of adult consumers in the UK do not make significant use of credit. Within this group, many will possess credit cards and have current accounts with overdraft facilities, but report never going overdrawn and always paying off in full any outstanding balance on credit cards. Overall, our survey suggested more than half (56 per cent) of adult consumers made no use of credit beyond that described above.

Summary of users of home credit

2.3 In addition to questions specifically related to the use of credit products, our research asked a variety of standard demographic questions. Calling on these results, it is clear that users of home credit, across a wide spectrum of measures, fall disproportionately into disadvantaged groups. Compared to consumers in general they are substantially over-represented in lower social classes, have markedly lower income, lower levels of final educational achievement, a much higher proportion of single parents, and are substantially more likely to be unemployed or not in paid employment.

2.4 Not surprisingly, this group of consumers reported a lower degree of ability to cope with a need to find the sum of £250. However, given the degree of disadvantage described above, our finding that some 40 per cent thought it would be very, or fairly, easy to do so was a rather higher than expected. At the same time, the extent to which users of home credit were able to access the money from their own savings was very low, suggesting correspondingly low resilience to financial shocks.
To find the sum most of this group reported they would borrow or access new or existing forms of credit.

2.5 The users of home credit reported a substantial level of dependency on the product, with approximately 55 per cent stating that they were very or fairly dependent on the product to support their day-to-day lifestyle. This finding was reinforced by measures of repeated and concurrent use of more than one home collected loan, where more than one in four reported currently holding a number of loans/credit agreements of this same type, and a similar one in four using a number of loans/credit agreements of this same type, which have followed on continuously from each other.

2.6 Overall about half of users were also using other forms of credit, most commonly in the form of catalogue shopping (20 per cent). Estimates here are based on small sample sizes so provide only general indications, but more than one in ten reported using rent-to-buy and overdraft facilities, and around one in ten having an emergency loan from the government’s social fund. Similarly, one in ten also had a personal loan.

2.7 The most frequently reported reasons for using home credit was for the purchase of specific products or to meet the cost of special occasions. These uses generally exhibit the standard feature of credit being used to smooth consumption. However, substantial minorities (approaching 40 per cent) reported using the product for day to day household spending, paying off specific bills or to consolidate or pay off other debts.
Figure 2.1: Home credit - main purpose of loan

Source: OFT survey

Box 2.1 Users of home credit

Our survey of consumers has explored some of the types of consumers that use high-cost credit. We have also sought a number of examples of how high-cost products can be beneficial for consumers and instances where they can be detrimental. The examples below are intended purely to illustrate the effects that these products can have on consumers and are not considered to be representative of users of home credit:

Beneficial use of home credit¹

‘I don’t want to get myself into a hair-raising situation where it is ‘How do I pay this off?’’, so I don’t think I would like it if they can actually have access to your money. They can just take it straight out. So I don’t like the idea of that either. If I don’t want to pay it one week because I have to do something then I won’t pay it. I can’t give what I ain’t got and basically if they can take it out then I would be ‘How am I going to do this now?’ At

least with the bloke that I am with I can miss a week if I have to.

'I am very pleased with it. I would recommend it (home credit loan) to be honest. There are lots of single parents around who are struggling a little bit and it does help you. It is not a huge amount that you are going to get into terrible debt with but it is enough to help you out when Christmas comes along and things like that, or if you want to go on a little weekend away or something. I was a single parent, I brought up my children on my own so I know what it was like.'

'I'd rather go to a home credit company than go to a bank because if you don’t pay the bank, if you miss a few weeks they just tend to send out all the threatening letters and everything all the time.'

'I’m not too keen on going up to [the bank] and filling in all the forms and having to go in there and apply. It feels like you’re going for a job interview. At least with this [home credit] they come to your house, it’s better that way. And that you don’t have to pay it off in any major amount. It’s nothing that’s going to cripple me so I can take my time that way.'

Detrimental use of home credit

'A CAB in Derbyshire saw a 44-year old man who was unable to work because of a permanent disability, in receipt of benefits and living in social housing. He had been given a succession of 14 loans by two different home credit suppliers totalling £4,300. The man was unable to pay these debts and the stress was worsening his medical condition.'

'A Merseyside CAB saw a 60-year old married woman who lived in social rented housing. She was disabled and in receipt of disability living allowance high rate mobility & low rate care. Her husband was in receipt of pension credit and they received full housing and council tax benefit. The woman said she had been a customer of a home credit supplier for about 20 years. She had a number of outstanding loans with repayments totalling £170 per week. Because she could not afford the repayments she had been taking out new loans with the home credit supplier to meet weekly repayments. She came for advice when she realised she could not carry on in this way.'

'A CAB in the West Midlands saw a 29-year old woman who was a single parent with 3 dependant children, one of whom was disabled. The woman was in receipt of means tested benefits and disability living allowances in respect of her son. She had four loans with a home credit supplier totalling over £3000. The home credit firm continuously encouraged her to take out additional loans and she felt pressured to use her son’s disability living allowance to make repayments. She was in effect borrowing from the

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2 Comments from Citizens Advice Bureaus in the UK.
credit supplier to pay them back.'

Sample analysed

2.8 For most practical purposes the consumer group of concern in this study is limited initially to adults of 18 years and over. In the UK in the middle of 2008 that was some 48.26 million persons. If you are under 18, it is still theoretically possible to enter into a credit agreement, but such events are likely to be very uncommon, and would only be possible if an adult was able to act as a guarantor. Below the age of 18 you cannot usually be legally held to a contract and as a result a lender will not usually be able to take a young person to court if they break the terms of a loan.

How many consumers are affected by the cost of credit and interest rates?

2.9 Drawing on results from our consumer research, the study estimated that 64.6 per cent of consumers were not accessing any form of credit product from our list of identified products. While not using the listed credit products, some 46 per cent of consumers within that group reported having one or more credit cards, but of these 71 per cent reported that they always paid off any outstanding balance on their card or cards in full.

2.10 On this basis, we estimate that roughly 56 per cent of the UK adult population are for all practical purposes, unaffected by the cost of credit

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3 Source: Population Estimates Unit, ONS Centre for Demography, Office for National Statistics

4 This is a revised estimate based on the full set of interviews, albeit exclusive of those aged 16 to 18 as discussed in paragraphs 1.1 and 1.2. The original estimate was based on our extended questionnaire directed at approaching 2,000 consumers conducted in the first wave of data gathering.

Note that the product list at this stage is inclusive of mainstream products. In contrast, some later analysis is limited to specific sub groups of users. This distinction is important and will be emphasised wherever possible to avoid potential confusion.
either in the form of charges or interest rates. This is not a simple homogeneous group, but made up of some consumers who make no use of credit products at all and some who are users of credit but who do so in ways that avoid charges and interest.

2.11 Note that there exists a distinct difference in the proportion of card holders always paying off their credit cards in full, in relation to their use of other credit products. As reported above, of those who do not make use of other credit products but hold credit cards, 69 per cent report always paying off in full. Of those who make use of credit products and also hold credit cards, just 44 per cent report always paying off in full.

2.12 Consumers who have an overdraft facility but no current overdraft or a credit card are free to make use of those credit facilities with considerable ease should they choose, but equally some people who are overdrawn or with an outstanding balance on a card may clear that debt. The groups are not static and over time there is likely to be migration between the two.

2.13 However, applying these results to the UK population would, at a given point in time, suggest there are roughly 21 million consumers of credit products that will be subject to the cost of credit in the form of charges and interest (as defined above) and 27 million consumers that will not. Summary results are shown in the table below. For these results, the credit products involved include: mainstream products, such as personal loans; use of overdrafts; car loans and finance deals amongst others.

2.14 In some later analyses, results are presented that focus on specific sub groups of these categories. For example, personal loans obtained from lenders specialising in securing such loans for those with impaired credit ratings.
Table 2.1: Use of credit products and related credit card use: UK adults

<table>
<thead>
<tr>
<th></th>
<th>Yes (%)</th>
<th>No (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Use of specified credit products</td>
<td>35. 4</td>
<td>64. 6</td>
</tr>
<tr>
<td>of which:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Also have credit cards</td>
<td>67. 8</td>
<td>46. 2</td>
</tr>
<tr>
<td>No credit cards</td>
<td>32. 2</td>
<td>53. 8</td>
</tr>
<tr>
<td>Of those with credit cards:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Always paying off in full</td>
<td>47. 6</td>
<td>71. 4</td>
</tr>
<tr>
<td>All other payment patterns</td>
<td>52. 4</td>
<td>28. 6</td>
</tr>
</tbody>
</table>

Source: OFT survey

2.15 Credit product use in a broad sense (that is inclusive of overdrafts and use of credit cards where the balance is not being paid off in full as well as loans and other products) is observably associated with middle age. Those who do not make use of credit at all or use it in ways that does not expose them to charges and interest are in the majority among the young, among those in late middle age and to a substantial degree among the retired.
2.16 Making similar comparisons between consumers subject to the cost of credit versus other consumers across different social classes, it can be seen from the following diagram that people in higher social classes are more likely to be credit users subject to charges and interest and those in lower classes less likely.

Source: OFT survey
Figure 2.3: Consumers subject to the cost of credit versus other consumers: Distribution across social classes

Source: OFT survey

Figure 2.4: Consumers subject to the cost of credit versus other consumers: Comparisons within social classes

Source: OFT survey
2.17 Further findings are illustrated above in two charts, each showing comparisons between consumers subject to the cost of credit compared with consumers not using credit products or using credit in ways that does not expose them to costs and interest. The first chart shows the distribution across social classes, and the second the proportion falling into each class. As reported above this is around 44 per cent of the adult population in all. Those in the lower social classes are distinctly less likely to be subject to the costs of credit through charges and interest, a result probably driven by their reduced ability to access mainstream products.

Users of home credit

2.18 Our research used considerable resources and effort to interview large numbers of ordinary consumers, eventually completing a total of around 7,600 interviews – with UK consumers aged 18 years and over. Despite this very large initial sample, the number of respondents reporting that they had made use of certain credit products within a reasonable recall period was often small.

2.19 For example, we found 82 participants who reported making use of home credit services, and just 53 who reported using rent-to-buy credit to obtain household goods. Only handfuls reported borrowing money by means of log book loans or using mobile phone text messaging services. Estimating the characteristics of credit product users therefore relies on rather small sample sizes and results need to be treated with caution.

2.20 The rate at which respondents reported using home credit equates to 443,000 people or just less than one per cent of all adults, and just over two per cent of the 21 million users of credit products identified in section 1 above.

2.21 To put this figure in context, it was based on reported product use within a recall period of six months, and does not take into account

\[5\] Survey results in general are weighted. This estimate is very similar but not exactly equal to 82 divided by 7600, the equivalent estimate without weighting.
some reported level of concurrent use of products from one or more supplier, or products following on continuously from one another. The figure may also include some level of under reporting due to participant reluctance to disclose their use of the product. It is not a direct estimate of total loans issued in a period such as a year.

2.22 In order to deduce very rough orders of magnitude, we allow for this figure (self reported users with current product or product obtained within the previous six months) to be representative of a rather higher number of loans per year. We assume that the number of loans issued is at least double, allow for some degree of concurrent use of products and allow an expansion of another 50 per cent. This would suggest around 1,500,000 such loans being made each year. If loans were on average £500 each, this would imply a total value of loans issued of £750 million. If loans were £700 or £1000 each, it would imply a total value of £1.05 billion or £1.50 billion respectively. To an order of magnitude the survey results suggest a total value of loans issued around £1 billion each year, though potentially somewhat higher if under reporting is present to any serious degree.

2.23 Keeping the previously stated caveats about sample size in mind, the charts below address a variety of key topic areas relating to users of home credit.
2.24 Home credit users are over represented in the younger and early middle age groups, and under represented in the late middle age and retired group. This is a result reasonably consistent with the use of credit products; that is, that older generations tend to have accumulated greater assets – both physical and financial and tend to have a decreasing need for credit.
Figure 2.6: Social class

Source: OFT survey

2.25 Users of home credit are heavily skewed towards the lowest social classes.
Figure 2.7: Home credit users: Income

Source: OFT survey

2.26 Compared to the profile for all consumers interviewed, to a considerable degree, users of home credit are more commonly found in the lowest two income groups and are under represented in the highest.
Figure 2.8: Home credit users: Educational attainment

Source: OFT survey

2.27 Users of home credit show substantial degree of under representation in the highest levels of educational attainment and a similar degree of over representation at the lower levels.

Figure 2.9: Home credit users: Gender

Source: OFT survey
Figure 2.10: Home credit users: Employment status

Source: OFT survey
2.28 The three charts above are included to provide further illustration of the characteristics of users of home collected credit. It can be observed that they more likely to be female than male and the charts show further evidence of falling disproportionately into disadvantaged groups, in the cases shown demonstrating a degree of over representation among the unemployed or not in paid employment, and substantially increased likelihood of being a single parent.

2.29 We do not argue that the results presented here are based on a sufficiently large sample size for great reliance to be placed on individual estimates, but argue that collectively, the evidence points to strong association between users of home credit and being disadvantaged. A consistent pattern emerges across a variety of demographic characteristics including but not limited to final educational achievement, income, social class, employment status and the likelihood of being a single parent.

Credit dependency and co-use of home credit

2.30 The users of home credit admitted to a substantial level of dependency on the product. When asked 'How dependent or otherwise would you
say you are upon this type of loan or credit in your day-to-day lifestyle at the moment?' roughly 55 per cent reported being very or fairly dependent.

Table 2.2: How dependent or otherwise would you say you are upon this type of loan or credit in your day-to-day lifestyle at the moment?

<table>
<thead>
<tr>
<th>Level of dependency</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Very dependent</td>
<td>13.2%</td>
</tr>
<tr>
<td>Fairly dependent</td>
<td>39.0%</td>
</tr>
<tr>
<td>Not very dependent</td>
<td>33.4%</td>
</tr>
<tr>
<td>Not at all dependent</td>
<td>14.4%</td>
</tr>
</tbody>
</table>

Source: OFT survey

2.31 This finding was reinforced by measures of repeated and concurrent use of more than one home collected loan, which was reported at high levels in the original report. For ease of reference these are repeated here.

Table 2.3: Repeated and concurrent use of more than one home credit product

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>I am currently holding a number of loans/credit agreements of this same type, either with the same company or with different companies</td>
<td>27.6%</td>
</tr>
<tr>
<td>I have been using a number of loans/credit agreements of this same type, which have followed on continuously from each other</td>
<td>26.4%</td>
</tr>
<tr>
<td>Neither of these</td>
<td>45.4%</td>
</tr>
</tbody>
</table>

Source: OFT survey

2.32 Additional to these effects, some concurrent use with competing products was also found. These estimates are based on small sample sizes and are subject to substantial sampling errors so should be interpreted as only broadly indicative.
Table 2.4: Home credit users: Use of other credit products

<table>
<thead>
<tr>
<th>Other credit product</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal loan</td>
<td>9.3%</td>
</tr>
<tr>
<td>Authorised overdraft</td>
<td>13.3%</td>
</tr>
<tr>
<td>Car manufacturer finance/credit agreement</td>
<td>6.8%</td>
</tr>
<tr>
<td>Credit agreement/finance on retail purchase</td>
<td>6.6%</td>
</tr>
<tr>
<td>Retail store card (excluding loyalty cards)</td>
<td>7.3%</td>
</tr>
<tr>
<td>Payday loan</td>
<td>0.0%</td>
</tr>
<tr>
<td>An item of value pledged to a pawn broker in return for a loan</td>
<td>0.8%</td>
</tr>
<tr>
<td>Rent to buy or hire purchase agreement</td>
<td>13.3%</td>
</tr>
<tr>
<td>Catalogue shopping purchase/mail order loan</td>
<td>19.6%</td>
</tr>
<tr>
<td>Loan from credit union</td>
<td>3.3%</td>
</tr>
<tr>
<td>Emergency loan from the government’s social fund</td>
<td>10.6%</td>
</tr>
<tr>
<td>Mobile phone loan by text</td>
<td>0.0%</td>
</tr>
<tr>
<td>Log book loan</td>
<td>0.0%</td>
</tr>
</tbody>
</table>

Note: The list of credit products in this table is not constrained and does not refer to any selected subgroup

Source: OFT survey

Table 2.5: Home credit users: Level of use of other credit products

<table>
<thead>
<tr>
<th>Level of use of other credit products</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>No other product used</td>
<td>48.1</td>
</tr>
<tr>
<td>One other</td>
<td>25.2</td>
</tr>
<tr>
<td>Two others</td>
<td>18.5</td>
</tr>
<tr>
<td>Three others</td>
<td>5.3</td>
</tr>
<tr>
<td>Four or more others</td>
<td>3.0</td>
</tr>
</tbody>
</table>

Source: OFT survey

Reasons for using home credit

2.33 Our survey asked participants to indicate the main purpose of using home credit. Broadly speaking this was an attempt to distinguish between using the product to support discretionary spending, versus using it for purposes that may be considered basic living essentials.

2.34 In the event, the distinction is not fully clear, as a need to purchase a particular item may encompass basic living essentials such as a washing machine for a family with a young baby, versus something less essential
such as an MP3 player docking station. Despite this, almost 40 per cent of users indicated that the loan was for day-to-day household spending or to pay an outstanding bill such as gas or electricity or to provide a way of consolidating or paying off other debts, which appear far removed from discretionary or luxury items.

Table 2.6: Home credit: Main purpose of loan

<table>
<thead>
<tr>
<th>Purpose of loan</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>To purchase a particular item</td>
<td>30.9%</td>
</tr>
<tr>
<td>Needed money for a special occasion (Christmas, Birthday, Wedding, etc)</td>
<td>29.4%</td>
</tr>
<tr>
<td>To help with day-to-day household spending</td>
<td>10.3%</td>
</tr>
<tr>
<td>To cover an outstanding bill such as gas or electricity</td>
<td>19.1%</td>
</tr>
<tr>
<td>To provide a way to consolidate/pay off other debts</td>
<td>8.8%</td>
</tr>
<tr>
<td>Other</td>
<td>1.5%</td>
</tr>
<tr>
<td>None of these</td>
<td>2.9%</td>
</tr>
</tbody>
</table>

Source: OFT survey

Availability of alternative financial products and financial resilience for home credit users

2.35 The main findings of our consumer research were published in December 2009, as Annexe A to the interim research report. As explained in chapter 2 of this report, the methodology involved directing one set of questions at an initial sample of 2000 consumers, then subsequently putting a modified set of questions to an additional 6,000 participants. Full details can be found at the reference given.

2.36 As part of this research, certain questions were asked about how the respondent would cope with a need to find a sum of £250 or £750 for an unseen event, or to pay for something. However, these were only asked of the initial 2,000 sample. As users of home collected credit were encountered only rarely across all our samples, examining how people responded to these questions in relation to their use of home collected credit produced very small sample sizes. These results should be viewed with caution.
2.37 Noting the above caveats, users of home credit were less optimistic about their ability to access the sum of £250 than consumers generally. However, given the degree of disadvantage associated with these users, the fact that some 40 per cent collectively thought it would be very or fairly easy to do so was a better than expected result.

**Figure 2.12: Home credit users: Ability to find £250**

Source: OFT survey

2.38 On the other hand, the extent to which users of home credit were able to access the money from their own savings was very low, suggesting correspondingly low resilience to financial shocks. The ability to use existing financial assets was found only at very low levels and most users sought to borrow or access new or existing forms of credit.
Figure 2.13: Home credit users: Most likely method of finding £250

Source: OFT survey
3 FINANCIALLY STRESSED CREDIT AND STORE CARD HOLDERS

Summary

3.1 Among the substantial proportion of consumers that held either a credit card or store card, we made use of further questioning to identify a small subset that reported the reason they had taken out the card was to cover an outstanding bill such as gas or electricity, to help with day-to-day household spending, and to provide a way to consolidate/pay off other debts. For the credit card we additionally checked that the user was not paying off the outstanding balance in full.

3.2 In general this group showed evidence that at the time they obtained the cards they were able to access mainstream credit but were also financially stressed – as evidenced by the reasons given for taking out the cards. In the first report of these results these groups were treated separately but in view of the broad similarity in their status have been combined for this further analysis.

3.3 As judged by a variety of demographic measures this group showed some differences to the set of consumers as a whole but not to a substantial degree. One observable characteristic was for the card group to be slightly more concentrated in the middle age groups than the others, and similar related effects also seem to spill over into related variables such as working status where there are fewer retired and students.

3.4 But notably the differences were far less prominent than the differences observed when comparing all consumers with users of home credit reported in section two above. In many respects they look fairly typical of consumers that access credit, and show no strong or consistent evidence of being over-represented in disadvantaged groups.
Figure 3.1: Age profile of users

Source: OFT survey

Figure 3.2: Social class

Source: OFT survey
Figure 3.3: Income

Source: OFT survey

Figure 3.4: Educational attainment

Source: OFT survey
Figure 3.5: Gender

Source: OFT survey

Figure 3.6: Employment status

Source: OFT survey
Figure 3.7: Partners and children

Source: OFT survey
4 USERS OF PAYDAY LOANS

OFT research

4.1 As reported in the OFT’s interim research report, the consumer research that was undertaken used considerable resources and effort to interview large numbers of ordinary consumers, eventually completing a total of around 7,600 interviews with UK consumers aged 18 years and over.

4.2 Despite this very large initial sample, the number of respondents reporting that they had made use of certain credit products either ‘making use of the product currently or having used them within the previous six months’ was often small. Among the groups with the lowest representation, completed interviews were made with just 17 participants who reported use of payday lending.

4.3 This sample sizes falls short of a level that would permit even very crude ball park estimates and is not considered appropriate for any further analysis, beyond providing support for the view that this product is routinely used by only a very small proportion of the general public, and, indeed, a small proportion of all credit users.

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Box 4.1 Users of payday lending

Surveys of consumers explore some of the types of consumers that use high-cost credit. We have also sought a number of examples of how high-cost products can be beneficial for individual consumers, and instances where they can be damaging. The examples below are intended purely to illustrate the effects that these products can have on consumers:

**Beneficial use of payday lending**

Would just like to say how excellent [company name] is. The customer service is outstanding and they always keep you updated and inform you of deferral options. I’m so pleased I found this company and I remain a valued happy customer. Well done [company name]. You’re a top service and I appreciate the helpful and kind service, as well as everything you have provided for me. Thanks again.

Your service is great and your staff are always professional. I get updates on my loan on a regular basis and when ever I have taken out a new loan the money is in my account on that same day. I have recommended your service to friends and family. Thank you [company name].
Not being from the UK I have found this the nicest and easiest way to borrow money, I might not have the best credit history, but even when my job paid me 2 days 2 late,[company name] was cool about it. If only the banks where like this.

[Company name] have not only helped me through some difficult times, but also helped build my credit rating thank you guys for everything.

**Detrimental use of payday lending**

A CAB in the West Midlands saw a 22-year old man who was single and living alone in local authority flat. He was working but in receipt of a low wage. When he got into financial difficulties he turned to the internet and a payday lender. They loaned him money until his next pay day when the money was taken from his bank account. He was then short of money for the following month and so took out another loan and his situation just got worse.

A Merseyside CAB saw a 24-year old man who had taken out a payday loan for £375 at cost of £75. He could not pay back full amount before the next month. When the CAB contacted the lender it became apparent that the terms of the advance were such that if the capital amount was not repaid each month the man was considered to have taken a fresh advance each month at cost of £75. It appeared that the loan had been revolved three times in this way.

A CAB in Yorkshire saw a 35-year old man on a low income who was desperate for money to pay bills. He took out a payday loan by signing seven £100 cheques and one £50 cheque, receiving £85 cash for each £100 cheque. He had to make a payment of £14.99 each month to stop his cheques being cashed.

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**Policis and the Friends Provident Foundation research**

4.4 The information presented in this chapter is drawn mainly from research entitled 'The new demand landscape for credit provision to those on low incomes and the implications for provision of affordable credit'.

4.5 The project was undertaken by Policis with funding from the Friends Provident Foundation and was supported by an advisory board which included a variety of domain experts and national stakeholders, including representatives from various government departments. It had two broad strands. The first set out to capture the nature and scale of change in

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6 Comments from Citizens Advice Bureaus across the UK.
the demand landscape for credit provision to those on low incomes and
to explore how far access to credit and credit supply is meeting credit
needs of different segments in the post-crisis world. The second strand
set out to examine the challenges for third sector lenders in changed
market conditions, how the target market for credit unions as social
businesses might most appropriately be defined and to explore new
opportunities for social lenders. The help and support of Policis and the
Friends Provident Foundation are kindly acknowledged.

4.6 The research methodology was based on a quantitative survey with a
nationally representative sample of 1500 low income consumers,
together with boosted samples of newly banked and unbanked
consumers, undertaken face to face and in home over December 2009
and January 2010. This was complemented by two telephone surveys
with high cost credit users, being a representative random sample of
500 home credit users and a representative random sample of payday
lending customers, in both cases drawn from the customer databases of
leading commercial providers and having borrowed within the last twelve
months. The payday lending sample was split between customers of on-
line providers and retail providers. The research was conducted by
telephone in November and early December 2010.

4.7 Some information used for comparison with other groups is drawn from
the OFT’s own research. Any associated commentary and conclusions,
however, are attributable to the OFT and should not be seen as
indicating any views or opinions held by Policis, the Friends Provident
Foundation or any advisory organisation to Policis or the Friends
Provident Foundation.

General demographic information

4.8 The following section presents some information on the demographic
profile of payday lending customers. Some differences in approach can
be observed between the OFT research and that undertaken by Policis.
While these make comparisons slightly more complicated, we note that
they do not prevent reasonable comparisons and conclusions from being
drawn.
4.9 One essential feature of payday lending customers is that they are in paid employment at the time of taking the loan, and by implication are of working age. In table 4.1 below, the research conducted by Policis was restricted to people of working age.\(^7\)

**Table 4.1: Age profile of payday lending customers, compared with all consumers**

<table>
<thead>
<tr>
<th>Age band</th>
<th>Percent</th>
<th>Age band</th>
<th>Percent</th>
<th>Percent excluding 65+ group</th>
</tr>
</thead>
<tbody>
<tr>
<td>18 to 25</td>
<td>22.9%</td>
<td>18 - 24</td>
<td>12.1%</td>
<td>15.2%</td>
</tr>
<tr>
<td>26 to 45</td>
<td>53.4%</td>
<td>25 - 44</td>
<td>35.4%</td>
<td>44.5%</td>
</tr>
<tr>
<td>46 to 65</td>
<td>23.7%</td>
<td>45 - 64</td>
<td>32.0%</td>
<td>40.3%</td>
</tr>
<tr>
<td>All ages</td>
<td>100%</td>
<td>All ages</td>
<td>100.0%</td>
<td></td>
</tr>
</tbody>
</table>

NB: Survey sample base for Policis research was restricted to 18 - 65 years olds

4.10 It should be noted that the age bands from the Policis research are not an exact match to those used in the OFT study, though they are sufficiently close for reasonable comparisons to be made, and it is clear that payday lending customers are more concentrated in the younger and middle year groups, and under represented in the older pre-retirement groups.

4.11 Taking as a comparator the income profile for all consumers established in the OFT consumer research, it is apparent that payday lending customers are under represented in the extreme parts of the income distribution. See table 4.2 below. The median income for all consumers,

\(^7\) The assumption that payday lending customers will not include those over retirement age is a reasonable one. While it cannot be claimed that it will never occur, the instances are likely to be very few.
the median being the amount for which 50 per cent have greater income and 50 per cent have lower income, is slightly below £25,000. Payday lending customers are heavily concentrated in the range below median income but generally above the lowest income bands.

**Table 4.2: Distribution of income for payday lending customers**

<table>
<thead>
<tr>
<th>Income band</th>
<th>Percent</th>
<th>Income band</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to £6,600 pa</td>
<td>4.0%</td>
<td>UP TO £6,499</td>
<td>8.0%</td>
</tr>
<tr>
<td>£6,600 up to £11,100 pa</td>
<td>6.4%</td>
<td>£6500 - £11,499</td>
<td>16.9%</td>
</tr>
<tr>
<td>£11,100 up to £15,000 pa</td>
<td>13.3%</td>
<td>£11,500 - £17,499</td>
<td>17.0%</td>
</tr>
<tr>
<td>£15,000 up to £19,200 pa</td>
<td>25.4%</td>
<td>£17,500 - £24,999</td>
<td>9.5%</td>
</tr>
<tr>
<td>£19,200 up to £24,300 pa</td>
<td>22.0%</td>
<td>£25,000 PLUS</td>
<td>48.7%</td>
</tr>
<tr>
<td>£24,300 pa and upwards</td>
<td>28.9%</td>
<td>Total</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

Total 100.0% Total 100.0%

NB Policis results for annual income are based on 12 times monthly income

4.12 Further information on the incomes of payday lending customers is shown below in figure 4.4 which shows income profiles of payday and home credit users by decile of household income. The comparator for figure 4.4 is implicit, given that across all households 10 per cent would fall into each decile band, and provides further illustration that while payday lending customers have income below the median there are only low proportions in the lowest two deciles, whereas home credit users are heavily concentrated in the lowest two income deciles.

4.13 Payday lending customers also show a tendency to be men rather than women. This is in contrast to consumers in general where there is a very slight imbalance in favour of women, and contrasts strongly with the situation for users of home collected credit reported elsewhere, where women are the major user group.
One final characteristic for which payday lending customers differ from consumers in general is in the family structure, where payday lending customers are notably fewer in the group where the family is a married couple or other partnered couple but without children. In part this is likely to reflect the absence of those over retirement age, as this group typically contains a good proportion of couples where children, if any, have left home. However, it may also partly reflect that couples without children may generally have less pressure on their finances than families that have the added financial burden of looking after children.
**Figure 4.2: Payday lending customers: Family structure**

![Bar chart showing family structure of payday lending customers compared to all consumers.](image)

**Source:** Policis and the Friends Provident Foundation

**Differences between payday lending customers and users of home collected credit**

4.15 Users of payday lending show some degree of separation to other users of high costs credit. In particular, there are a number of characteristics for which they are distinctly dissimilar to users of home credit. It is a basic requirement of users of payday lending that they have a bank account and are in employment at the time the loan is arranged.

4.16 This creates a degree of separation with home credit users, who as a group tend to fall into the lowest social classes where an increased proportion of consumers have no bank account, and as a group also having elevated levels of people unemployed or not in paid work.
4.17 This is illustrated in the above chart. The proportion of benefit dependent person using payday borrowing is very small when compared with the other situations described, and especially compared with users of home credit.

4.18 Reinforcing this finding that there is separation between users of home credit and payday lending, our own research found that among home credit users roughly half were using other forms of credit at the same time, but in our sample not a single home credit user reported being also a user of payday loans. The table below illustrates this.
Table 4.3: Home credit users: Level of use of other credit products

<table>
<thead>
<tr>
<th>Level of use of other credit products</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>No other product used</td>
<td>48.1</td>
</tr>
<tr>
<td>One other</td>
<td>25.2</td>
</tr>
<tr>
<td>Two others</td>
<td>18.5</td>
</tr>
<tr>
<td>Three others</td>
<td>5.3</td>
</tr>
<tr>
<td>Four or more others</td>
<td>3.0</td>
</tr>
</tbody>
</table>

**Among other credit products: Commonly used**

<table>
<thead>
<tr>
<th>Credit product</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Catalogue shopping purchase/mail order loan</td>
<td>19.6%</td>
</tr>
<tr>
<td>Rent to buy or hire purchase agreement</td>
<td>13.3%</td>
</tr>
</tbody>
</table>

**Among other credit products: Not commonly used**

<table>
<thead>
<tr>
<th>Credit product</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>An item of value pledged to a pawn broker in return for a loan</td>
<td>0.8%</td>
</tr>
<tr>
<td>Payday loans</td>
<td>0.0%</td>
</tr>
</tbody>
</table>

Note: Base: 82 interviews with users of home credit

Source: OFT survey

4.19 In terms of income, the chart below demonstrates that while a large majority of payday borrowers have income below the median there are only low proportions in the lowest two deciles. Home credit users are heavily concentrated in the lowest two income deciles, and this is consistent with the picture that emerged for home credit users from our own consumer research.
Payday lending customers: with and without other credit options

4.20 At the request of the OFT, Policis defined two separate types of payday users: those for whom payday is their only credit option at the time they took out their most recent loan, and those using payday but having other credit options. This division into these two groups was on the basis of declarations made by research participants themselves, who in answer to questions stated that their only option was payday when they took out their most recent payday loan.

4.21 On this basis, Policis found that just 20 per cent of payday borrowers had this as their only credit option, with the remaining 80 per cent having self reported 'other options'.

4.22 The differences that are apparent between the two groups reflect the slightly lower average incomes and slightly higher levels of average credit repayments per month for the group without other credit options, as depicted in the chart below.
Figure 4.5: Credit options, household income and value of repayments

Source: Policis and the Friends Provident Foundation

4.23 Similarly those without options appear on average to be slightly more indebted and with lower cash savings. They also appear to be using payday borrowing a little more frequently and borrowing slightly more than those with other options. The differences, while not large, seem to suggest that those without options are, across a range of measures, somewhat less well placed financially than their counterparts with other options.
Figure 4.6: Value of savings and debt for payday loan users

![Bar chart showing value of mainstream and revolving debt for payday loan users.]

Source: Policis and the Friends Provident Foundation

Figure 4.7: Number and value of payday loans

![Bar chart showing number and value of payday loans per annum.]

Source: Policis and the Friends Provident Foundation
The uses that are made of payday loans

4.24 One key feature of payday loans is that, to a greater degree than most other types of credit, they are not used for longer term smoothing of consumption, and are used simply to meet immediate needs.

Figure 4.8: Uses of credit by credit type

Source: Policis and the Friends Provident Foundation

4.25 Payday loans are most likely of those products above, to be used for mortgage, rent or utility payments. They are however, less likely to be used simply for cash when money ran out, particularly compared to cash advances on credit cards. The evidence suggests that payday borrowers are not using these loans to simply bring forward by a few weeks purchases such as a holiday or expensive item of consumer goods.

4.26 Expanding the analysis to examine differences between payday borrowers with and without options, reveals slightly greater proportions of those without options are likely to be using the funds as distress borrowing, but the overall pattern of use is broadly similar for the two groups.
Figure 4.9: Uses of payday loans

Source: Policis and the Friends Provident Foundation

Other potential sources of short term cash

4.27 It is of interest to explore the range of options available to consumers in need of cash to meet short term commitments. Among potential candidates, bank account holders with overdraft facilities, credit card holders, or consumers in possession of valuable items could consider using their credit facilities or pawning their valuables as a source of short term cash.

4.28 It cannot be assumed that these will be available to all consumers of high-cost credit. First, the consumer may not have these facilities. Second, even if they are available to the consumer in theory, if he or she is already overdrawn, close to the maximum limit on his or her credit card, or has no suitable valuables, they may not be available in practice.

4.29 The chart below depicts the credit repertoires of products used by families on low incomes and indicates that an overdraft is used as a reported source of credit by nearly 40 per cent and a credit card as a source of cash by around six per cent, though use of a pawnbroker is reported in only three to four per cent of cases.
4.30 These products appear to have the potential to provide alternatives to payday borrowing and therefore provide competition as sources of short term cash. The evidence presented below has been selected because of its relevance to the range of options that are available to the consumer at the time he or she needs the loan.

Figure 4.10: Credit repertoires for consumers on low incomes

![Credit repertoires for consumers on low incomes](image)

Source: Policis and the Friends Provident Foundation

4.31 As discussed earlier, only 20 per cent of payday borrowers report that they have no other option. This appears to be an encouraging finding as it raises the prospect of these consumers examining alternative options and sets up potential for competition between payday and these other credit options.

4.32 However, the OFT’s survey of consumers found that 62 per cent of high-cost credit users surveyed did not consider any other options when taking out their credit agreement. Only 15 per cent said they actually considered and investigated alternatives.

4.33 The OFT is aware that measuring the levels of substitutability are inherently difficult in many markets including high-cost credit, although our market definition analysis does indicate that payday lending is a separate economic market to other high-cost credit products. We note that analysis of this using many survey techniques may not always
demonstrate the true elasticity of demand characteristics of consumers of high-cost credit.

**Figure 4.11: Consumers’ motivation for using payday loans**

![Bar chart showing consumers' motivation for using payday loans](chart.png)

Source: Policis and the Friends Provident Foundation

4.34 Most consumers appear to be motivated to use payday lending for ease and its speed. The OFT’s survey of consumers also found this to be a consistent trend among consumers of a number of different high-cost credit products.

4.35 The following three charts give an indication of the financial stresses present for users of payday lending. There are some examples where results differ dependent on whether the consumer had access to alternative products, while other results may be more indicative of the behaviour generally of the demographic groups that use payday loans among other products.
Figure 4.12: Repayment patterns with credit cards for payday users

Source: Policis and the Friends Provident Foundation

Figure 4.13: Credit card usage patterns among payday customers

Source: Policis and the Friends Provident Foundation
Figure 4.14: Refused applications among payday customers

Source: Policis and the Friends Provident Foundation

4.36 This evidence is consistent with that indicating that one aspect of consumer preference for payday borrowing is to reduce the risk of getting into major financial difficulty with mainstream products.

Reasons for choosing payday loans

4.37 There is clear evidence that that some consumer behaviour is focussing not on the deal itself but on the possible consequences of payment delinquency, including both the cost and risk. This can be seen in the chart below. Payday borrowers report that missing payments can make credit cards more expensive, overdrafts can be more expensive and that credit cards can trap you into a debt spiral at higher levels than similar observations about payday borrowing. While not all the evidence is fully consistent, the wider financial implications of payment delinquency appear to be of concern to many payday borrowers.
Figure 4.15: Reasons for customers using payday loans

Source: Policiis and the Friends Provident Foundation

4.38 In our own consumer research, the priority that was afforded by consumers to different aspects of credit the deal on offer was also investigated. It emerged that for various credit products, consumers attached greater importance to a wide variety of issues such as speed with which the deal could be arranged, absence of credit record checks and affordability of payments rather than interest rates or the overall amount repayable. However, there was very little evidence in our own consumer research about choosing the product that in any way related to the consequences of getting into difficulties with repayments.

4.39 The Policiis and Friends Provident Foundation research notes that issues of avoiding getting into difficulties are a notable concern for users of payday loans. We note that this applies more widely to similar consumers in their use of other credit products, such as credit cards and overdrafts.
4.40 The charts above appear to the OFT to be, collectively, an indication that payday borrowers may be showing a number of significant financial stresses. For borrowers in such circumstances, adding to their burden of conventional financial products poses very real risks and it is a rational evaluation of their financial circumstances to avoid that risk.
Figure 4.17: Share of debt accounted for by home credit and payday loans

<table>
<thead>
<tr>
<th></th>
<th>Home credit users’ indebtedness</th>
<th>Payday lending users’ indebtedness</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit card debt</td>
<td>£1,820</td>
<td></td>
</tr>
<tr>
<td>Home credit debt</td>
<td>£500</td>
<td></td>
</tr>
<tr>
<td>Mainstream credit agreements</td>
<td>£4,450</td>
<td></td>
</tr>
<tr>
<td>Payday borrowing</td>
<td>£275</td>
<td></td>
</tr>
<tr>
<td>Mainstream credit agreements</td>
<td>£3,770</td>
<td></td>
</tr>
</tbody>
</table>

Source: Policis and the Friends Provident Foundation
Note: The data above refers purely to home credit and payday loan users that also have mainstream debt, excluding those with no such debt.

**Credit dependency and default**

4.41 Despite the views of some payday borrowers noted above that using payday borrowing they were less likely to get into trouble, some payday borrowers also show evidence of struggling to meet repayments and defaulting on their loan agreements. In nearly 30 per cent of loans, the borrower fails to meet the initially agreed repayment of within 30 days/next payday and the loan is extended. Also nearly 10 per cent of payday loans go beyond 90 days.
Figure 4.18: Extensions and rollovers of payday loans

Source: Policis and the Friends Provident Foundation

4.42 The immediate consequences of failing to meet the agreed repayment period may not result in any wider repercussions provided that the borrower contacts the lender in time and both consumer and lender are willing to agree an extension to the repayment period. It is known that some lenders make such a contact routinely to ensure the necessary funds will be present in the borrower’s bank account. However, there are often significant additional costs faced by consumers in the event that loans are rolled over, in addition to the interest costs which may continue to accrue.

4.43 Direct evidence of default levels is not included in the above chart. However, in addition to the information provided above about deferred payments Policis provided estimates of payday borrowers who report having payment problems. Overall this is more than 10 per cent of all users of payday loans.