Lending, levelled up

How to elevate affordability assessments with enriched data, and **why** it's more important than ever

tink

A Visa Solution

Why now is the time to act and enhance your affordability assessments

In the face of the ongoing cost-of-living crisis and changing economic landscapes, the need for robust affordability assessments in the lending industry has arguably never been greater. Traditional methods such as national averages and credit reports can give a limited view when trying to gain a full understanding of creditworthiness since they are backwards-looking with narrow data points. At the same time, consumers are increasingly challenged to make ends meet.

This is why we're setting out the importance of using enriched data for affordability assessments, delving into the key components of how much individuals earn and spend, and highlighting imminent regulatory changes. As the lending industry focuses on key milestones like the new Consumer Credit Directive 2 (CCD2) and Financial Conduct Authority's Consumer Duty, enriched data is essential for responsible lending, operational efficiency and protection against fraud.

As discussed in *McKinsey & Company's* recent global banking annual review, two of the four global trends set to shape the outlook for financial institutions are especially relevant here:

- Technological progress continues to accelerate, and **customers are increasingly comfortable** with and demanding about **technology-driven experiences**

- Governments are broadening and deepening regulatory scrutiny of nontraditional financial institutions and intermediaries as the **macroeconomic system comes under stress** and new technologies, players, and risks emerge

In addition, recent research undertaken by Tink in the UK – where 1,000 borrowers (those who hold either a mortgage or loan) and 200 lenders (from mainstream banks to online lenders) were surveyed – as well as nationally representative consumer research in France and Germany, paints a stark picture on both sides of the lending process.

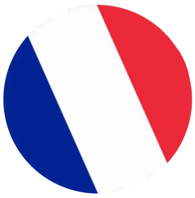
Inflationary economic conditions mean that a significant amount of people are overdrawn at the end of the month – approximately 26% of French citizens and 22% of Germans. In the UK, 15% of borrowers face a similar situation. To mitigate these financial challenges, many citizens are turning to loans, either from those close to them or more formally with financial institutions.

Getting these loans can be a challenge, yet repaying it is also a concern for many. About 11% of Brits surveyed, 15% of French individuals, and 17% of Germans have encountered difficulties in repaying their loans.

Perhaps as a result, an estimated 82% of UK lenders now consider affordability checks more important than ever, and 77% acknowledge the need to improve their risk decisioning models to provide a more accurate view of people's finances.

Continue reading to see how getting a clearer, more up-to-date picture of an applicant's earnings and spendings can turn the tide…

Types of loans taken out in three countries



Friends & family **22%**
Banks **17%**

Friends & family **27%**
Banks **31%**

Friends & family **16%**
Banks **25%**

Key insights:

Assessing earnings correctly 4

Understanding spending habits 7

Getting to grips with new regulations 9

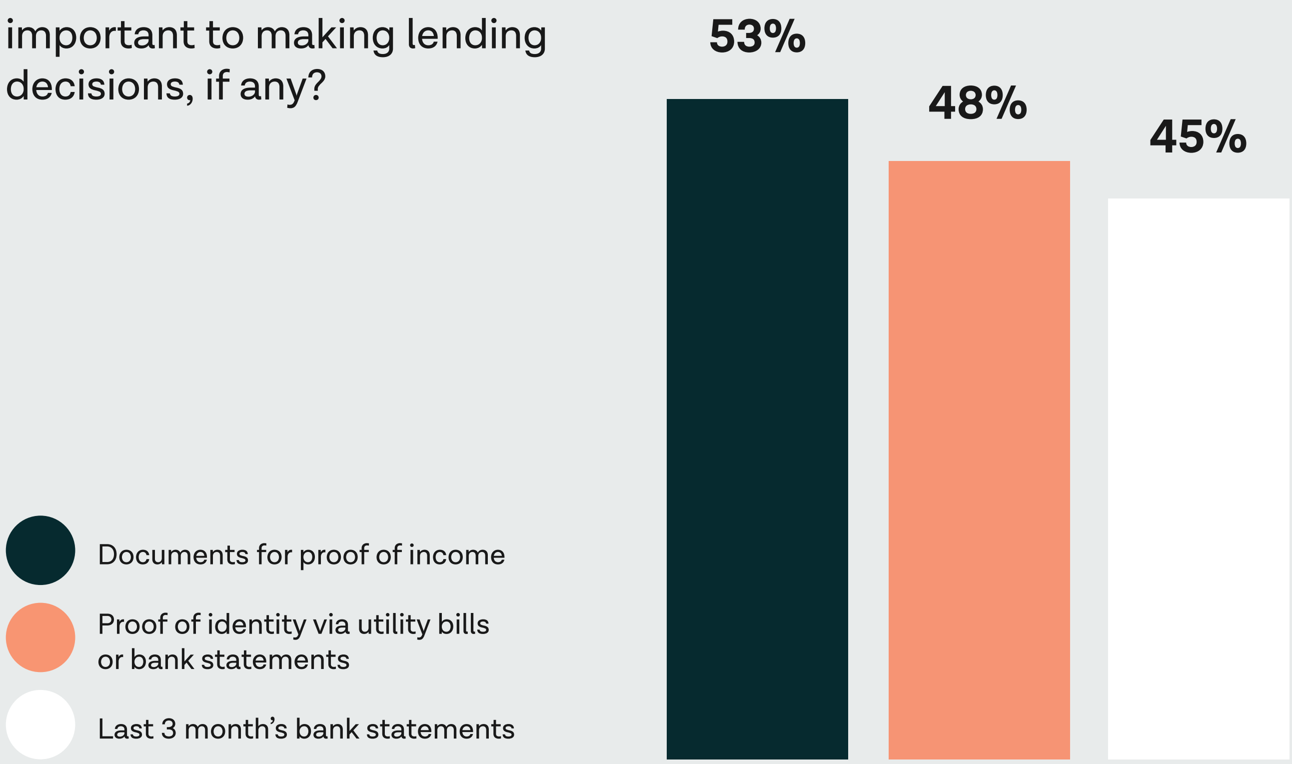
Assessing earnings correctly

It may seem a little obvious to say that when analysing applicant affordability that it's essential to understand their earnings. Over half (53%) of UK lenders we spoke to said that documents showing proof of income were most important when making decisions. However, the way to achieve this effectively has moved on significantly in recent years.

Tink's Income Check product is a key tool for many lenders in Europe – like Bank Norwegian and Sambla Group – and helps them verify an applicant's income in minutes instead of days thanks to open banking technology and access to the user's latest financial data (with their explicit consent). Besides saving time, it also helps the industry be more inclusive through advanced data analysis. For example, self-employed people – whose bank statements can be harder to assess due to more fluctuating income – are less likely to feel unfairly treated in the application process.

Proof of income is the most important aspect of making lending decisions.

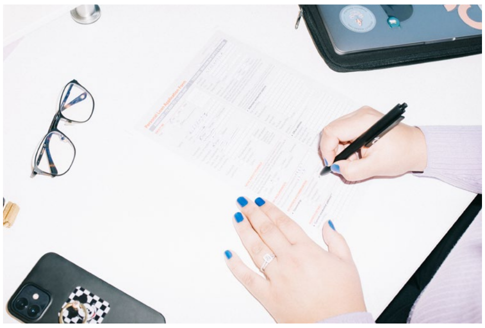
What information is most important to making lending decisions, if any?



Current environment demands comprehensive applicant data

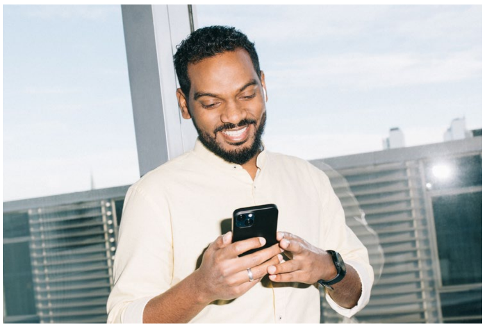
Of the lenders we spoke to, over a quarter said that verifying an applicant's income is one of the most time-consuming elements of the risk decisioning process, whether that's collected manually or digitally.

Thinking about your risk decisioning process, what takes the most time, if anything?



32% Income verification (manually submit*)

* e.g. PDF upload or via post



28% Income verification (digital)

Meanwhile, defaults and fraud continue to cause problems for lenders.

Some struggling consumers are going to great lengths to try to secure the borrowing they need, with more than one in ten (12%) UK borrowers surveyed saying that when a loan application was denied, they have reapplied with a different lender and altered their credit information so they can access the loan they need.

These consumer behaviours are borne out by insights from UK lenders. An estimated 35% of those surveyed by Tink are seeing a rise in application documents being edited.

With Tink’s income classification models, users are able to prove their income through secure, up-to-date data in their bank account spanning up to 12 months, while Strong Customer Authentication (SCA) adds an additional layer of security in proving the applicant’s identity, reducing risk.

Now is the time to upgrade

Many lenders have already levelled up their risk decisioning tools, and of those that haven’t a significant portion say that they are in the process of upgrading.

Digital income checks based on the applicant’s bank transactions data:

43%

already upgraded

42%

currently upgrading

Understanding spending habits

Traditionally, affordability assessments are based on an applicant's manual input or basic statistical estimates of their spending, combined with data from many different sources – creating friction and misguided conclusions on affordability.

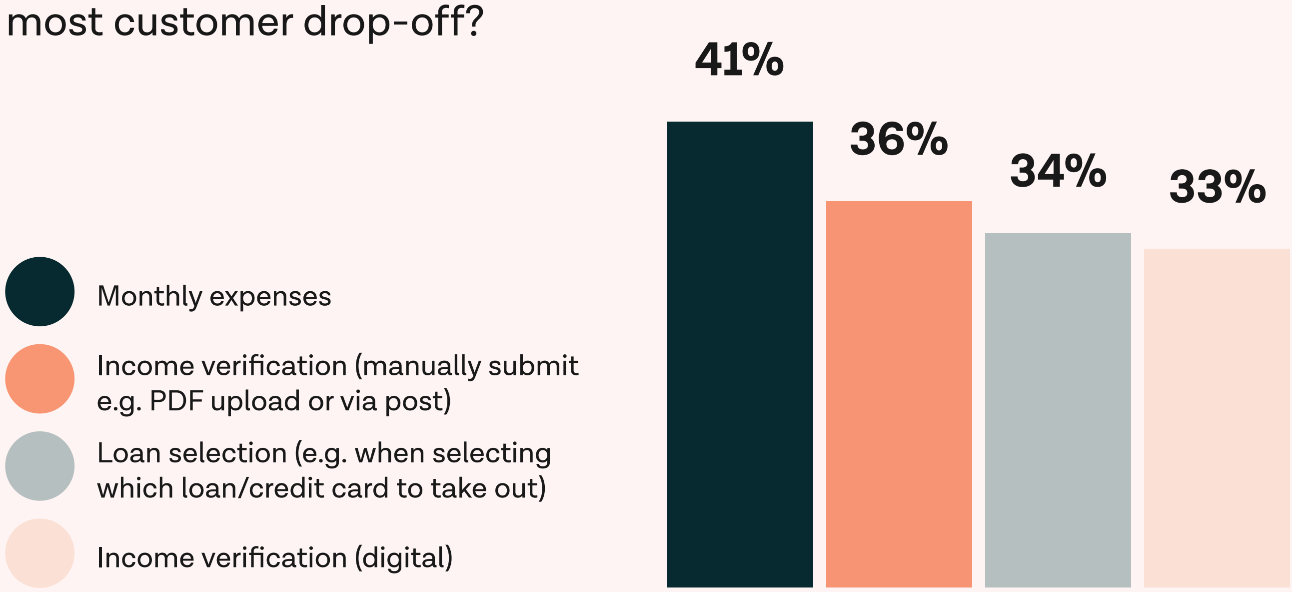
Enter Expense Check

Data-enriched, secure affordability assessments help to solve this potentially messy process by eliminating human error, and another key feature is that they are better at looking at active, or current, spend rather than any legacy expenditure that may have wound down or no longer be relevant when making an assessment (e.g. a subscription that has been cancelled in recent months).

When Expense Check is combined with Income Check, assessing affordability has never been easier.

Our new research with top UK lenders clearly showed that high friction in the application process often arises from monthly expense evaluation, with 41% of respondents saying that this was where they saw the **highest applicant drop-off.**

Thinking about **drop-off** rates in the loan application process, where, if anywhere, in the application flow do you see the most customer drop-off?



Consumers are becoming more open to granting access to their data for improved assessments

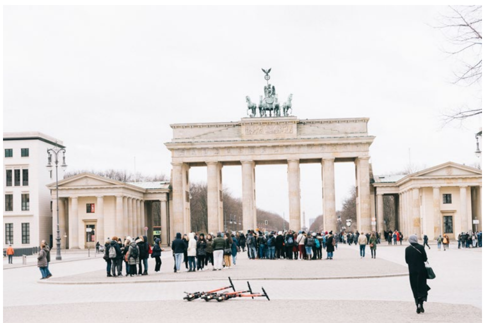
Almost half of the consumers we surveyed in the UK, France, and Germany agreed that they would let financial institutions digitally access their transaction data if it improved the credit decisioning process.

With increasing consumer acceptance and adoption, there is a real opportunity here for further collaboration across the lending process – between applicants, lenders, and third parties. Working together in a more harmonious way will only lead to outcomes that benefit all parties, and enhance overall satisfaction.

“I would enable my lender to digitally view transaction data from my bank account to improve the application process”

46% UK

42% France



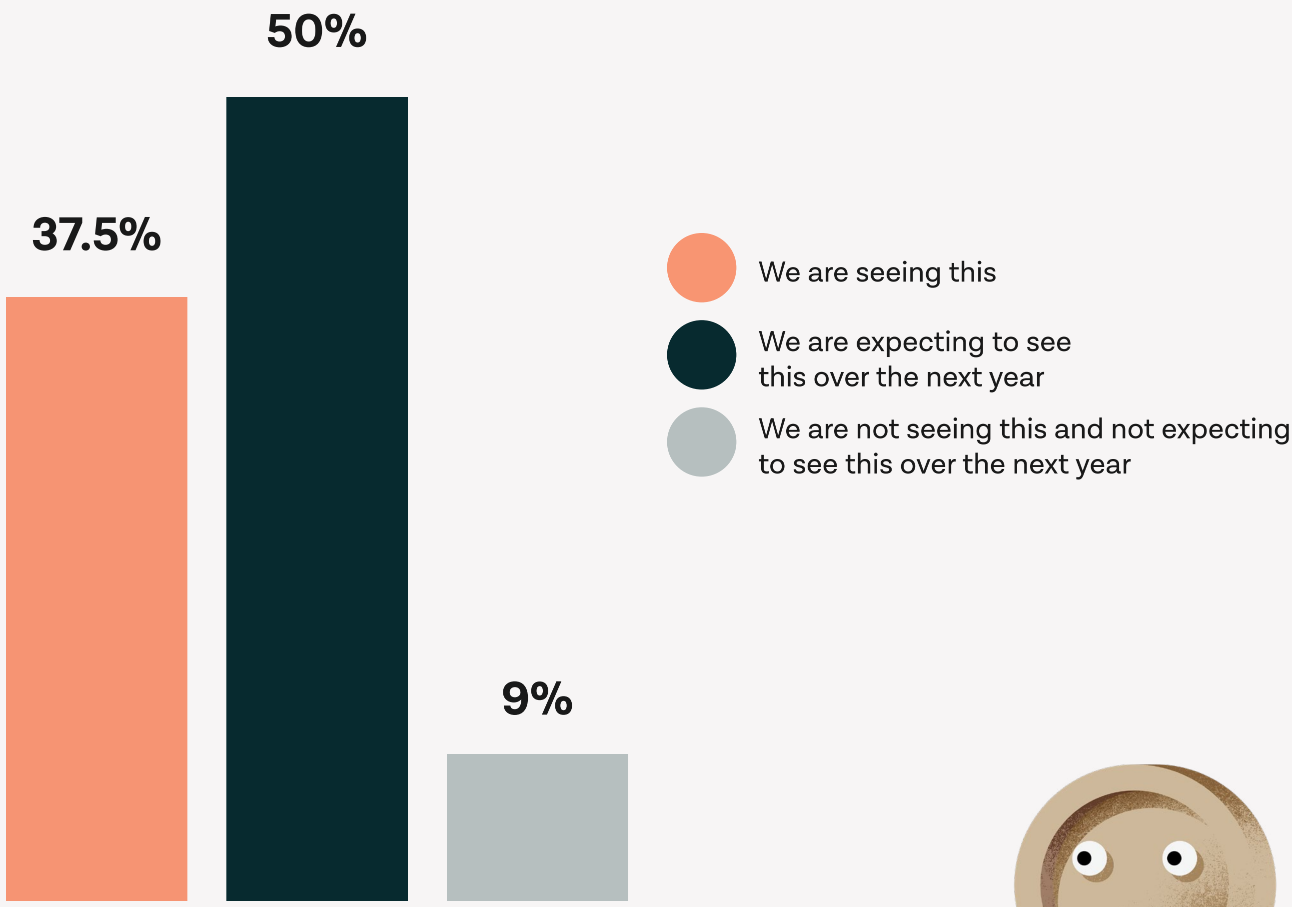
43% Germany

Getting to grips with new regulations

As ever in the world of finance, lenders cannot stand still with an ever-changing technological and regulatory landscape. With tightening regulations afoot, there is increasing pressure on lenders to ensure thorough risk assessments are adopted, that help support people in the current challenging economic times.

When we asked UK lenders if they are experiencing stricter regulations on affordability assessments, **seven out of eight** (88%) respondents said that they are either seeing this now or expect it in the next year.

Stricter regulations on affordability assessments

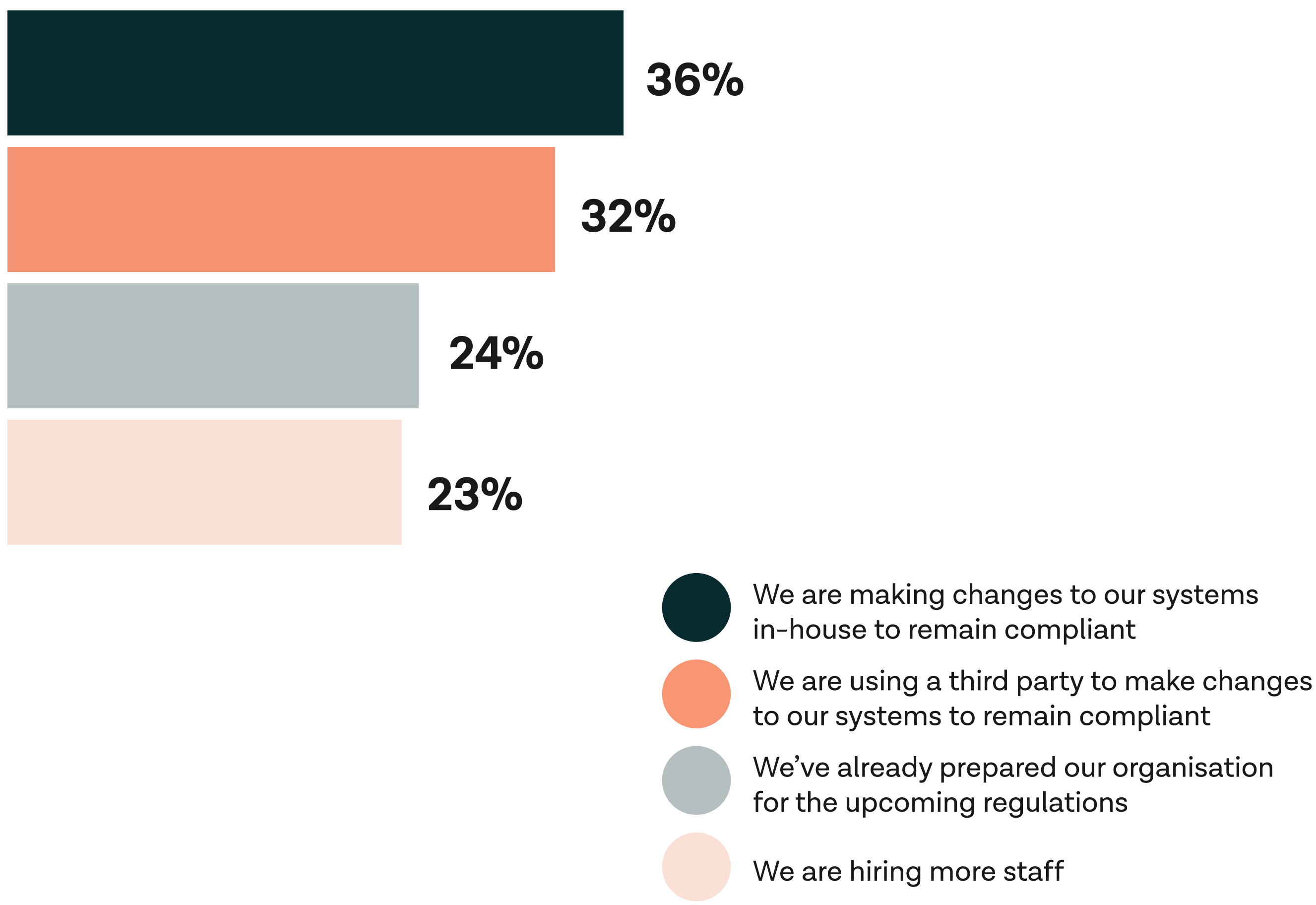


Meanwhile, around a third (34%) of UK lenders said that lending compliance checks, such as ensuring the product offered meets the Financial Conduct Authority's new Consumer Duty, is the element that **takes the most time** in their risk decisioning process.

The new Consumer Duty has also helped focus many lender's minds on strengthening affordability assessments, with **78%** agreeing that this was the case.

Around a third of lenders (32%) are turning to third parties for assistance in making their systems compliant, with just under a quarter of those we spoke to saying that they feel confident that their organisation is ready for upcoming regulatory change.

Thinking about upcoming regulations impacting your loan process, how are you preparing your business to ensure compliance, if in any way?



In the EU, the new Consumer Credit Directive (CCD2) emphasises the importance of a thorough creditworthiness evaluation. It means looking at not just how much money people earn and spend but also considering their existing financial responsibilities, living costs for them and their family, and their overall financial obligations. **To meet this objective, utilising enriched data and improved affordability assessments is the path forward, and many in the industry are well aware of this need for change.**

“Through the FCA’s Consumer Duty and CCD2 in the EU, the responsible lending wave has been made more tangible. They, along with other pieces of regulation and policy, represent an effort to ensure increased benefits across the board in the financial ecosystem. By making lending decisions more comprehensive, it helps to reduce the chance of consumers taking up unaffordable loans and therefore falling into financial difficulty. To do this, the data used during credit assessments needs to improve and deepen.

“Without analysing an applicant’s real banking behaviour, understanding their true affordability can be a bit of a guessing game. By looking at transactional data with open banking solutions like those offered by Tink, in combination with traditional credit checks, banks and lenders can understand better if an applicant has the ability to repay a loan by utilising categorised, monthly income and expense information. With responsible lending at the forefront of regulatory agendas, it’s essential to prove an applicant’s affordability no matter the loan or line of credit.”

Jonathan Wildish,
Tink Product Solutions Lead (Lending)

In a world where the cost-of-living crisis continues to affect consumers, and the lending industry faces new regulations, it's key to elevate your affordability assessments with enriched data.

Let's navigate these challenges together and adapt to the changing landscape. Contact Tink today.

tink.com/contact-us

Disclaimer

Consumer research in the UK was conducted by Censuswide on behalf of Tink in September 2023, amongst 1,000 borrowers aged over 18 (i.e. those who currently have either a mortgage or a loan).

Consumer research in France and Germany was conducted by OpinionWay on behalf of Tink in October 2023, amongst 1,000 consumers aged 18 and over. The sample was constituted using the quota method, based on gender, age, socio-professional category, urban area and region of residence. The sample was interviewed using a CAWI (Computer Assisted Web Interview) self-administered online questionnaire.

Lender research in the UK was conducted by Censuswide on behalf of Tink in September 2023 amongst 200 executives at a High street bank, Building society, Challenger bank, Payday lender or BNPL lender who have a decision-making role in the lending process.

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