Industry in Focus

Overlooked and financially under-served

Sizing the financially under-served population in the UK

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TotallyMoney

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Foreword

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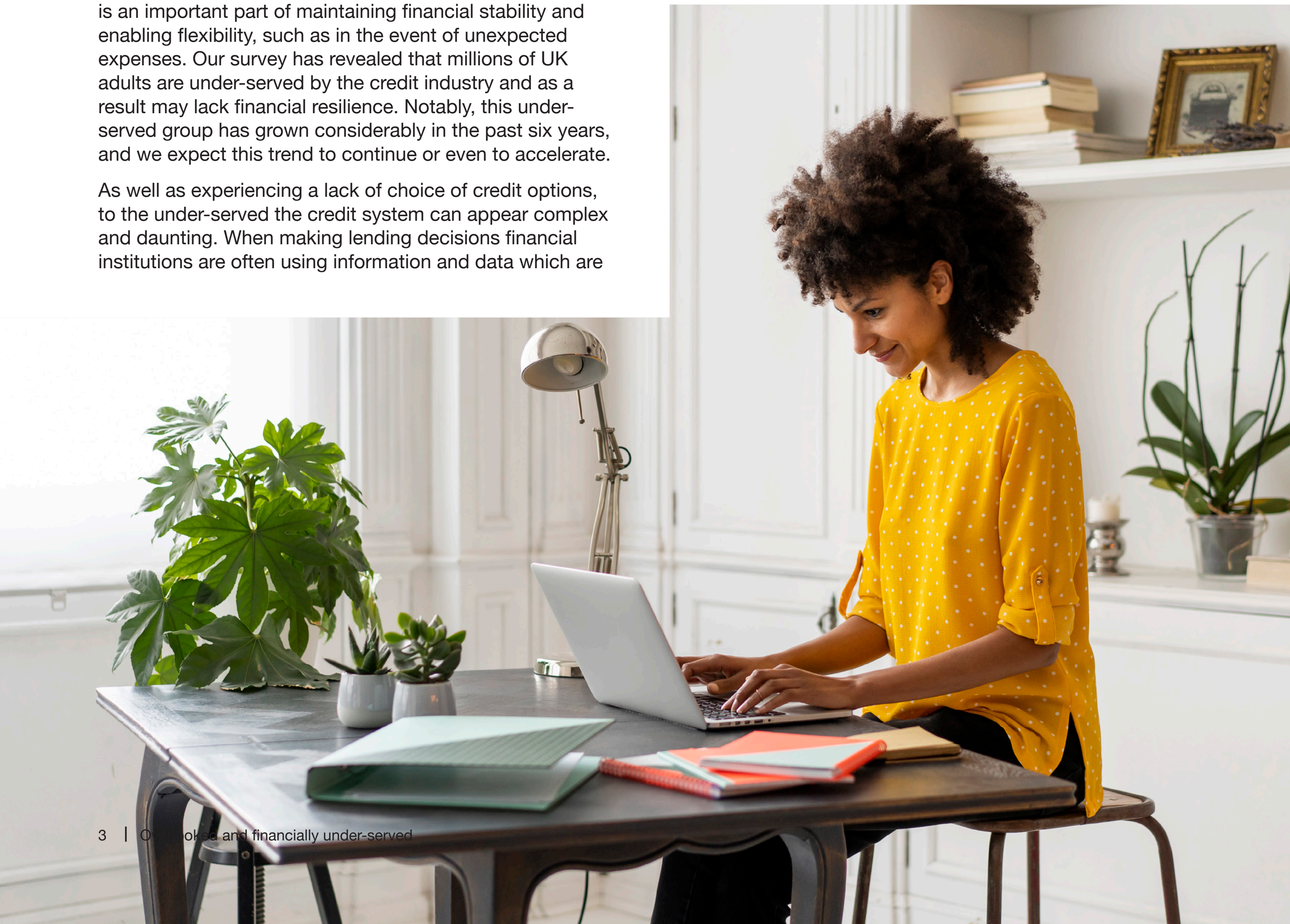
In this report, PwC and TotallyMoney, the credit app, have collaborated to shine a light on the UK's significant financially "under-served" population. This population will likely find it difficult to access credit from mainstream sources, and we believe there is an opportunity for industry players and regulators to collaborate to help provide them with greater choice and more straightforward access to credit. This is particularly important now, given the current economic backdrop and cost of living squeeze.

Wherever you sit on the credit spectrum, access to credit is an important part of maintaining financial stability and enabling flexibility, such as in the event of unexpected expenses. Our survey has revealed that millions of UK adults are under-served by the credit industry and as a result may lack financial resilience. Notably, this under-served group has grown considerably in the past six years, and we expect this trend to continue or even to accelerate.

As well as experiencing a lack of choice of credit options, to the under-served the credit system can appear complex and daunting. When making lending decisions financial institutions are often using information and data which are not well-understood by individuals. Individuals in the under-served population in particular do not always have a good understanding of their credit rating and how it impacts their financial lives.

Cross-industry collaboration is vital, with credit reference agencies, lenders and FinTechs all having an important role to play. We believe the industry can increase both transparency towards and trust among the under-served population, through designing products to serve the needs of this population and supporting financial education. It is equally important that regulation adapts. The Woolard Review[1] highlights the need for greater involvement of mainstream lenders in the non-prime credit markets, however mainstream providers continue to find it challenging to serve the "under-served".

PwC and TotallyMoney have conducted this research to size the under-served population, how it has grown since 2016, and the drivers for this change. With the insights from this report, the industry and regulators can start to develop a way forward and explore the steps that need to be taken to change credit for the better, for everyone.



1. Who are the under-served and why are we focusing on them?

Ahead of conducting this research, we had a hypothesis that the size of the "financially under-served" population may be bigger than expected. The last time a concerted effort was made to size the population was in 2016 and since then we have seen a confluence of factors, such as the pandemic and rising cost of living, put a strain on people's financial health.

Indeed, we found that there are 20.2m people who are under-served today. This means that 1 in 3 adults in the UK may have difficulty accessing credit from mainstream lenders, perhaps due to a thin credit file, minor adverse credit history and/or low or volatile incomes that may impact affordability.

This segment does not include the unbanked or sub-prime populations, who are typically better served by alternative credit providers.

It is important for the financial services industry, alongside regulators, to understand a current and accurate picture of the size of this segment, so that appropriate solutions and support can be provided. The Woolard Review[1] summarises that access to credit depends on the following factors: "the cost of credit and what's affordable; the availability and quality of credit information to allow lenders to assess consumers' creditworthiness; and consumer awareness of available credit options."

Having access to sustainable credit is an important part of being able to maintain financial resilience, for example, when unexpected events occur that might otherwise lead to financial difficulty. In this report, we also consider the 8.9m people that are not under-served today, but are "financially fragile". With a significant squeeze on the cost of living underway, and due to intensify, there is a real risk that this segment becomes under-served in the next couple of years.

The financially under-served may have difficulty accessing credit from mainstream lenders, and could, therefore, lack financial resilience

2. How have we sized the population?

PwC was commissioned by the credit app TotallyMoney to characterise and size the financially under-served population in the UK. Given the characteristics of this segment, there is no definitive, publicly available data to size it.

As a result, we ran a bespoke customer survey of >2,000 UK adults with YouGov in February 2022. The survey provides a statistically significant representation of the UK population, at greater than a 95% confidence level.

To be defined as "financially under-served", respondents needed to meet some basic eligibility criteria (to screen out those who are unable to borrow e.g. deep subprime or unbanked) and at least one of three definitions.

To calculate the overall size of the population, a set of mutually exclusive groups was developed based on survey responses. The results were then extrapolated to the total UK population. The questions posed are a continuation from a PwC survey conducted in 2016, enabling us to estimate how this population has changed in size.

Once we had isolated the under-served population from the remaining respondents, we then sought to identify those who are "financially fragile". We defined this segment as the respondents who did not meet the financially under-served criteria, but did exhibit at least one indicator of fragility, e.g. they would need to borrow to make an unexpected bill payment of £300 in next 12 months.

Financially under-served definitions

1 **Meet at least one under-served characteristic** (e.g. have a thin credit file / minor adverse credit history) and / or

2 **Hold a near prime credit card** (e.g. cards with a higher APR / focus on building credit score) and / or

3 **Perceive themselves to be under-served** (e.g. think they would struggle to access credit)

3. How many people are under-served and has this number grown?

We estimate there to be 20.2m financially under-served adults in the UK in 2022 (see figure 1). This means that at least 1 in every 3 adults may have difficulty accessing credit from mainstream lenders.

Applying the same definitions, this figure is around 50% larger than it was in 2016 when there were 13.6m financially under-served adults. Overall, more adults now meet each definition of being under-served – either exhibiting an under-served characteristic, holding a near prime credit card or perceiving themselves to be under-served.

On average, the under-served population tends to be younger than those who are not under-served (45 vs. 51 years old) and typically has a lower gross personal income (£27k vs. £34k per annum).

The under-served population has lower savings that they can call upon and are more likely to feel out of financial control or to have seen a deterioration in what they can afford (see figure 2).

20.2m

adults in the UK are now defined as financially under-served

Figure 1: Size of the financially under-served population in the UK (Adults: millions, 2022)

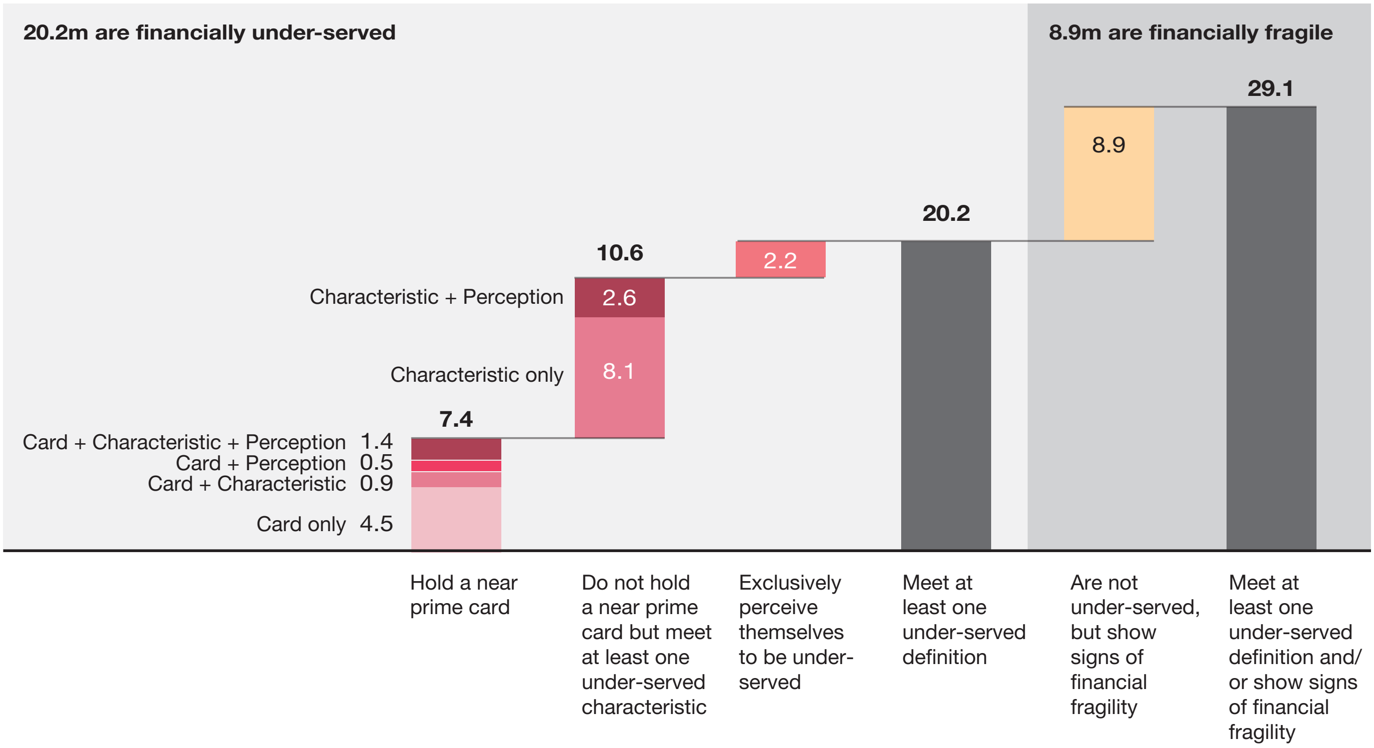
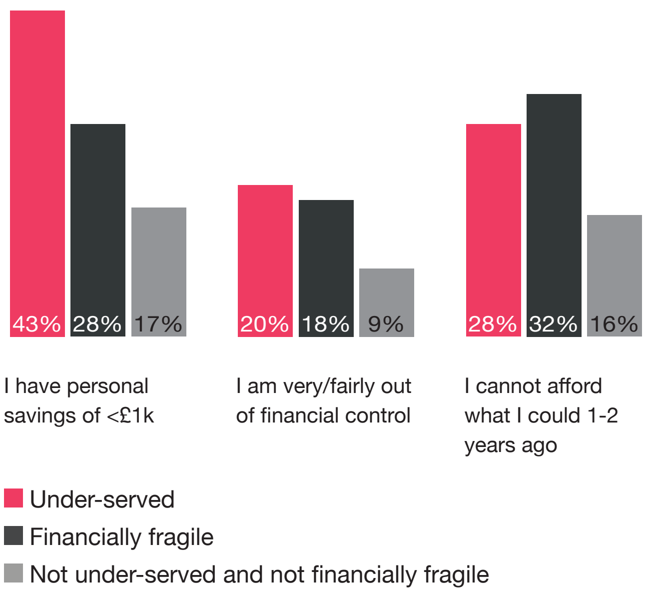


Figure 2: Financial traits of the under-served and financially fragile populations in the UK (Percent, 2022)



An additional 8.9m adults exhibit signs of financial fragility. These people are among the most at risk of becoming under-served in the near future as a result of a further squeeze on their finances as the cost of living crisis continues.

This population is more likely to use their overdraft to cover spend on everyday essentials (e.g. groceries, bills), to have had their income negatively impacted by the pandemic or to struggle to make repayments on their borrowing in the next year.

Considering this population as well, 1 in 2 adults are either under-served and/or show signs of financial fragility.

8.9m
adults in the UK are defined as financially fragile

4. What is driving change in the market?

(i) Lasting impact of the pandemic

Our survey indicates that the pandemic has had a lasting impact on income for a significant group of people. 11 million adults – or 1 in 5 adults – have had their personal income impacted by the pandemic and do not expect it to recover in the next two years. This group is more at risk of entering financial difficulty, particularly those with lower gross personal income (31% earn less than £15k per annum).

As an immediate result of the pandemic, household savings rose and outstanding balances of unsecured debt fell. However, this picture at the aggregate level masks the fact that some households have had to run down savings and have increased their debt levels since the start of the pandemic.

The ONS[2] found that by December 2020, approximately 9m people had to borrow more money than usual as a result of the pandemic. The groups most likely to have taken on more debt are: "renters, people from minority ethnic groups, parents and carers, disabled people and those who are shielding, and young people."[3]

The pandemic has driven more people into the under-served population as those with more variable income are less likely to be served by mainstream lenders.

> "Once Covid-related Universal Credit was stopped, I noticed that I was having more trouble paying for transportation and my family had to pay for a few extra journeys for me."
>
> Male, 25-34, London

1 in 5

adults had their income impacted by Covid and don't expect it to recover in the next two years

(ii) Increasing cost of living

Our survey has also shown that around three-quarters of adults in the UK are worried about the rising cost of living and 43% have already had to adjust their budget as a result. Concerningly, Citizens Advice has found that 1 in 12 people turned to Buy Now Pay Later (BNPL) to cover basic costs in the last six months[4].

The rising cost of living is a growing threat to people's financial situations. It is likely to further increase the size of the under-served market – particularly among those we define as showing signs of financial fragility – as everyday spending becomes less affordable, and the likelihood of missed payments increases.

PwC expects that rising prices could mean that the average UK household would have to pay an extra £2,500 in 2022/23 to buy the same goods and services as in 2021/22[5]. Nominal pay is also expected to rise, but not by enough to fully compensate workers for the increased prices of goods and services.

Several factors are driving this fall in real income. PwC[5] forecasts UK inflation to hit a 40-year high of around 11% in Q4 2022, with people facing significantly higher energy and fuel bills, as well as increased costs of essential items, including food. At the same time, National Insurance payments will go up, and those with new or variable rate mortgages will face higher repayments due to interest rate hikes.

16m

adults in the UK would need to borrow money in order to afford an unexpected payment of £300 in the next 12 months

We estimate that 16m adults in the UK would need to borrow money in order to afford an unexpected payment of £300 in the next 12 months. In the context of the cost of living squeeze, it is easy to see how this could push more people into the under-served segment, particularly as it becomes more challenging to pass affordability checks by mainstream lenders.

In line with the FCA's New Consumer Duty act[6], lenders will need to evidence the right levels of care, understanding and support for these people – many of whom will fall into the financially under-served segment.

> "I'm already starting to see a difference in my weekly shop. I'm trying not to use my car as much because petrol is so expensive."
>
> Male, 25-34, Yorkshire and the Humber

(iii) Growing segment with thin credit files or no credit history

There is a growing group of people that either does not use credit at all or has a thin credit file. As a result, this group is less likely to pass creditworthiness assessments based on traditional risk assessments.

There is also emerging evidence of some people being less attracted to traditional forms of credit. Our survey indicates that there are approximately 11m adults in the UK who do not hold a credit card and would not consider using one in the future. This is more prevalent among young adults, with 32% of this population aged between 18-34 years old, compared to 22% for those that hold a credit card or would consider using one in future.

60% of those that have said they would not consider using a credit card do not currently hold any other unsecured lending product. This, again, leads to a lack of credit history on which the reliability of repayments can be assessed, meaning that this group is more likely to need to turn to near prime lenders for their borrowing needs.

One factor that is likely to be contributing to this growing population is the rise of "Generation Rent". While there are now services that report rental payments in a similar way to mortgage repayments, these are not widely known about or used. As a result, most of this population misses out on the potential to improve their credit rating by evidencing a regular repayment history.

> "I don't have any assets; I'm not a homeowner. I know my credit score is pretty much in the bin. I probably don't have that many [financial products] on offer to me."
>
> Female, 18-24, Wales

29%

increase in the number of people with no credit history in the last six years

(iv) Alternative forms of employment

We estimate that there are around 4m adults who are in an alternative form of employment, such as those that are self-employed or part of the gig economy. This segment has an average gross personal income of £25k per annum compared to £37k per annum for those in full-time employment.

Compared to those in full-time work, self-employed workers have a lower level of job security, are at greater risk of stress when on leave without sick pay and are more exposed to external shocks in the economy.

Lower and less predictable income profiles mean that this segment is looked upon less favourably than more conventional forms of employment. As a result, 58% of this group is defined as under-served, relative to 37% of the overall population.

58% vs 37%

58% of those in alternative forms of employment are defined as financially under-served, relative to 37% of the overall population

5. What conclusions can we reach?

Having grown by around 50% in the last six years, and with further growth likely due to the cost of living crisis, the financially under-served population is becoming too large to ignore.

With at least 1 in 3 adults in the UK now defined as under-served, the consumer credit market must focus on designing credit products that meet the needs of this segment and provide them with a range of credit options.

According to the Woolard Review[1], “greater involvement of mainstream lenders directly in non-prime credit markets, with their expertise and economies of scale, is essential to driving competition and innovation. Consumer choice and outcomes will likely remain limited without this.”

There is also an opportunity for existing near prime lenders to enhance their propositions and deliver new solutions that truly meet the needs of this large and diverse segment of society. At the same time, there is an opportunity for other financial services organisations to step in and better help consumers to navigate this landscape.

Given the size and growth of this segment, actions to support the population will need to be taken quickly to avoid more people facing challenging financial circumstances.

1in2

adults in the UK are either financially under-served and/or financially fragile

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3 – House of Commons (July 2021), "Coronavirus: impact on household debt and savings"

4 – Citizens Advice (March 2022), "One in 12 now using Buy Now Pay Later to cover essentials"

5 – PwC Economics forecast (March 2022)

6 – FCA (December 2021), "CP21/13: A new Consumer Duty"

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