Apex Insight

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Online Payday Lending

UK Market Insight Report 2014

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About this report

What does the report contain?

- This market involves the provision of high-cost, short-term loans via a website. As well as 30-day loans designed to tide the borrower over until the next payday, we include other loans with interest rates of over 100% and terms of less than one year.
- We quantify the market size, historical growth rates, segmentation patterns and levels of industry profitability while reviewing key factors behind these figures.
- We also carry out an in-depth analysis of the relevant drivers of industry growth – in particular the macroeconomic environment and regulatory framework – setting out historical trends and available forecasts.
- Our forecast for industry growth is based on this analysis of historical trends and growth drivers.

What are the objectives of this report?

- Payday lending has emerged and grown into a major industry with customers measured in millions in just a few years.
- The industry is frequently in the news.
    - Lenders are often criticised for charging high rates of interest which exploit low-income consumers
    - However, many lenders inspire high levels of customer loyalty and enjoy satisfaction rates that would be the envy of the mainstream banks
    - Recently, regulators have taken a great interest in the industry and many lenders have pulled out of the market
- This report aims to explore the industry behind these statements, probe the factors which have driven its historical growth and recent more mixed performance and provide a view on how the market is most likely to perform in the future.
- Other questions the report considers include:
    - Why did payday lending grow so rapidly in the UK and what factors have made it develop more rapidly here than elsewhere.
    - Who takes out payday loans and why?
    - Who are the main companies in the market, who owns them and how have they performed?
    - What impact is the FCA's price cap likely to have on the market in future?
    - How are lenders adjusting their business models in response to it?
- It is intended for:
    - Operators of payday lending businesses themselves
    - Investors in these businesses
    - Potential new entrants to the market
    - Market regulators and policymakers
    - Banks, analysts, consultants and other parties with interests in the sector

What are the sources and methodology?

- This report is based on
    - Interviews with senior-level contacts in the consumer credit industry
    - Extensive research into published industry sources
    - In-depth analysis of the macroeconomic environment and relevant market drivers
    - Financial analysis of the accounts of companies in the industry
- Information from these sources has been synthesised and presented clearly and concisely with extensive use of charts and tables to illuminate points and support conclusions
- Market forecasts have been constructed using simple assumptions which are clearly stated. Supporting evidence is provided for our assumptions but readers can easily flex them to model alternative scenarios.

Summary

Market background

- Online payday loans are intended to offer customers an immediate advance on their wages until payday.
- Most borrowers report that they need the money to cope with an unexpected cost such as a car repair or vet bill.
- Service levels are high with well-designed websites, quick and simple application processes followed by an instant decision and transfer of funds shortly afterwards.
- Being designed for short lending periods measured in days, payday loans have particularly high APRs with levels typically being over 4,000%. Lenders and customers focus more on the £ cost to repay the loan than the APR.
- There is concern that some borrowers roll over payday loans to meet living expenses or support repayments on other forms of credit. Given the costs involved, this is unlikely to be sustainable.

Market growth and drivers

- The market grew rapidly from start-up to approach a value of £900m in 2012.
- This growth resulted from the convergence of three key drivers:
    - A significant increase in the number of customers in the sub-prime segments as a result of the economic downturn
    - Significant reduction in the appetite of the mainstream banks for serving such customers
    - The ‘light touch’ regulatory environment in the UK which created an environment more favourable to high-cost credit providers than elsewhere in Western Europe and North America
- In the last couple of years the market has reversed as regulation has become much firmer. This is likely to continue with the introduction of a price cap by the FCA expected in January 2015. This will limit the total level of interest and fees that lenders can charge.

Competitive landscape

- The top three online payday lenders are:
    - Wonga, which has driven the growth of the market through high-profile marketing campaigns including TV advertising and football club sponsorship
    - Cash America, which operates the number two payday lender, QuickQuid as well as the instalment loan brand, Pounds to Pocket. It also has a large network of pawnbroker stores in the US, and is listed in New York
    - DFG Global, the leading US operator of pawnbroking shops which now has almost half its revenue in the UK from the Payday UK and Payday Express loan brands as well as its high street chain, The Money Shop. Until recently it was listed on Nasdaq but was acquired by private equity firm, Lone Star Capital, in 2014.
- High street lenders such as pawnbrokers and money stores also offer payday loans but evidence suggests that online lenders account for more than 80% of all such loans. High-street loans:
    - Have a different customer base (older, more likely to be female, less tech-savvy)
    - Are of lower average value

Outlook

- The nature and impact of regulation is the main uncertainty in the market with the FCA’s loan cap proposals now out for consultation, with implementation scheduled for January 2015.
- The nature of the UK economy, policies outlined by the main parties and other factors such as the UK housing market and student loan system suggest that there will continue to be demand for payday loans.
- There appears to be no prospect of either mainstream banks or new financial service models such as peer-to-peer lenders competing to serve payday lending customers.

About Apex Insight

Company background

- Apex Insight is an independent provider of research, analysis and advice
    - Founded in 2012 by a team with experience of working in strategy consulting and the transaction advisory team of a Big 4 firm
    - Focus on a range of services markets including consumer credit
    - Publish market reports and carry out consulting work to address more specific requirements

Consulting services

Custom market analysis

- Research and evaluation of your required market to your desired scope.
- Market quantification, competitor insight and intelligence, analysis of drivers and forecasts

Commercial / operational due diligence

- Experience of leading c.100 transactions.
- Work includes assessment of market attractiveness, competitive position, customer relationships, information systems and operational performance.

Primary research

- We have deep experience in conducting face-to-face interviews with senior-level decision-makers and managing large-scale surveys, plus even more experience in analysing findings to provide insights and actionable results

Growth strategy

- Outward looking and fact-based: market entry strategies, search and screening programmes for new partners, customers or acquisition targets, benchmarking.

Related research

Pawnbrokers & Payday Loan Stores (April 2014)

- Consumer Credit Forecasts (October 2013)
- Rent-to-Buy Retail (April 2014)
- Peer-to-Peer Lending (October 2013)
- Consumer Debt Purchase & Debt Collection (July 2013)
- Home Credit (April 2014)
- High-Cost Consumer Credit (October 2012)
- Consumer Debt Solutions, Market Insight (September 2012)

Research subscriptions

- For clients who require access to multiple reports plus report updates and analyst time for further research, presentations, etc.
- Can be tailored to meet individual requirements cost-effectively