

DG speech to APPG Credit Unions – 30th November

Thanks

I only have a short time so I'm going to start by making a simple statement.

“Low income borrowers are being ripped off, and despite assurances that this is a policy priority, nothing effective has been done about it.”

There is a lack of effective price competition in the high cost credit markets and firms are able to extract excessive levels of profit from our poorest borrowers and communities. Far in excess of what would be expected from a properly functioning market economy.

We know that is a fact in the Home Credit market, because following a lengthy inquiry the Competition Commission told us in 2006 that there was a 'striking' lack of price competition which was costing consumers at least £75 million per year and that this had been taking place since at least the year 2000. So the value of that alone is £750 million, drained from our poorest communities in the last ten years by profiteering door to door lenders.

But we know that this profiteering is also likely to be happening in other forms of high cost credit markets as well. That's because the same features which prevent competition in the home credit market apply equally well elsewhere.

Firstly, low income borrowers are not sensitive to prices. Because the poorest are constantly juggling bills and struggling to meet everyday expenditures they often have an urgent need for cash when emergencies arise. The price isn't the main consideration, but the speed at which they can obtain cash is. So lenders are able to take advantage of that.

Secondly, they don't have a whole heap of options and the market is particularly poor for people without bank accounts who need cash. Pawnbroking is only possible if people can provide some form of security. Other types of borrowing, such as mail order or hire purchase only deliver up goods, not cash.

Credit Unions, for all of the great work that they are trying to do, simply don't exist at sufficient scale to provide a real alternative for many people. A report from the Financial Inclusion Taskforce indicates that it will take a decade at their current rate of growth before they are in a position to provide any sort of real alternative to the high cost lenders.

So we have a problem. We know that low income borrowers are being ripped off. We know that there is inadequate competition from Credit Unions and it is not likely in the current climate that Government will be able to pump in the resources required to make a significant difference to that. So what do we do?

In Debt on our Doorstep we have been clear about this for the past 10 years. We should cap prices. We made that argument not because we don't see the dangers of price caps in competitive markets. We do. In competitive markets, price caps ration supply and cause market distortions (for example changes in pricing behaviour). So we agree with the opponents of price caps in competitive markets. Let me be clear - we do not support the use of price caps in competitive markets.

But these are not competitive markets, and all of those objections to price caps do not apply.

I have to say here, some brief words about the quality of UK research on this subject, which has been very poor. A report released last week by the New Economics Foundation ('Doorstep Robbery') shows that the Policis research on the use of rate caps in France, Germany, and the US failed to meet even a basic standard of social research.

Let's take the two most common arguments against caps and look at those. Firstly, it's argued that caps will cause lenders to withdraw from the market and open the way for an increase in illegal lending. As Doorstep Robbery points out, the Policis findings concerning levels of exclusion and illegal lending in France and Germany are inaccurate. But think about it logically. Why would caps cause lenders to withdraw from the market? They are making an enormous level of profit at the moment – in excess of what they would make if the market was properly competitive. If we introduce a cap and that causes some loss of profit – not all of it, but some – then why would they withdraw? Last year Provident made nearly £130 million in profit. It isn't going to stop trading if next year it only makes £80 million. Of course, if the cap eliminated all profit then that clearly would make lenders leave the market. So it is the level of the cap and its impact on profitability which is important not simply whether one exists or not.

And let's just spell it out. Since the Competition Commission report in 2006, Provident are charging more not less and profits are increasing not reducing. They are now charging £82 in costs and interest for every £100 they lend. That's obscene because three years ago, at the time of the Competition Commission report, they were charging £65 for every £100 lent.

So their prices have actually gone up by 26% in three years. This is despite a range of measures that the Commission introduced which were designed to increase competition and bring prices down. Those measures, however well intentioned, have clearly failed.

Which brings me to the second major argument against caps. That caps don't address the underlying reasons for a lack of competition. We agree. They don't. Other things need to be done to achieve that. The Commission needs to look again at what they are. It considered breaking Provident up last time and it needs to think about that again because we estimate that Provident now has 70% of the market and no new entrants are going to be able to compete with their economies of scale and marketing presence.

More money also needs to go to Credit Unions. But it isn't likely to be coming from Government in anywhere like the amount needed. We therefore think that banks, in which we have invested so much money of late, should be placed under an obligation to show how they are meeting the needs of lower income groups for affordable credit. They should be able to discharge that obligation either directly or by partnering with Credit Unions. We believe that obligation – monitored by the FSA and under the scrutiny of Parliament and other agencies – would make a significant difference to levels of Credit Union funding

What is clear is that all of that will take time. We cannot just say that people can continue to be ripped off whilst we spend another five, six, ten years, trying to address the underlying causes. It is time to act against rip off companies now, and if there is to be no price cap then my question to you is this – what will you now do to deliver a fair price to consumers in this market – not in three years time, but within three months. They should not have to wait any longer.