The State of Alternative Credit Data

How the financial services industry is adopting and benefiting from these new data sources

Experian® has long been a brand associated with data. **Data analytics. Data insights. Data experimentation.** And with 220+ million credit-active consumers on file, there's certainly no shortage of information.

Through the decades, we've created more than **1,800 attributes** to dig deeper into how people spend, pay, earn and generally manage credit.

The traditional credit score has ruled the financial services space for decades, but it is clear the way in which consumers are managing their money and credit has evolved. When we layer on additional sources of data — like rental and utility payment history and short-term loans — suddenly a much more comprehensive picture of the consumer emerges. Enter the buzzworthy topic of alternative data.

What is fair game? How can it benefit lenders and consumers? Is it predictive? Can it coincide with traditional credit data?

Today, individuals are using myriad financial resources to make ends meet and quickly gain access to capital. By understanding and using the data available — both traditional and alternative — it is possible to understand the financial behaviors of more consumers, in greater depth.

So, let's dive into the world of alternative credit data.

Defining

What is it? What types exist?

Defining

What is traditional credit data?

Data assembled and managed in the core credit files of the nationwide consumer reporting agencies, which includes:

- Tradeline information (including certain loan or credit limit information, debt repayment history, and account status)
- Credit inquiries
- Information from public records relating to bankruptcies.

It also refers to data customarily provided by consumers as part of applications for credit, such as income or length of time in residence and employment.

Information used for credit decisioning must be displayable and disputable. This means the data is visible on a credit report and can be disputed by the consumer.

Without credit, it is nearly impossible to buy a home or start a business. People face barriers to accessing credit or pay more for credit for several reasons. Some have negative items on their credit report, such as a record of late payments. Some have trouble documenting their income.

Still others have either no credit history or a credit history that is too scarce, or "thin," to generate a credit score. This issue affects an estimated 62 million Americans and more often affects African-American, Hispanic and low-income consumers, according to the Consumer Financial Protection Bureau (CFPB).[1]

This is where alternative credit data can play a positive role.

[1]https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-study-finds-consumers-lower-income-areas-are-more-likely-become-credit-visible-due-negative-records

What qualifies as alternative credit data?

In the consumer financial marketplace, alternative credit data refers to information used to evaluate creditworthiness that is not usually part of a traditional credit report. To fall under the Fair Credit Reporting Act (FCRA)–compliant umbrella, alternative credit data must be displayable, disputable and correctable.

This data provides more insight into both full-file and thin-file consumers, to drive greater visibility and transparency around inquiry and payment behaviors. Adding the information from alternative credit data sources may allow some consumers to gain more access to credit.

Some examples:

- Rental payments
- Mobile phone payments
- Cable TV payments
- Bank account information, such as deposits, withdrawals or transfers
- Small dollar loans.

Other types of alternative data might relate to things less closely tied to a person's financial conduct, like that person's education or occupation.

Could mobile phone and rental payment data add value to a consumer's credit profile? Consider the stats.

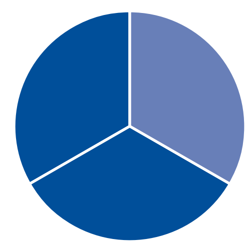
95%

of Americans own a cellphone of some kind[2]

Americans who own smartphones

35% → 77%

2011 2018



About 2/3

of households headed by young adults are rentals[3]

Reporting this data has the potential to thicken an individual's credit file and provide more insights on ongoing payment behavior.

[2]http://www.pewinternet.org/fact-sheet/mobile

[3]http://www.pewresearch.org/fact-tank/2017/07/19/more-u-s-households-are-renting-than-at-any-point-in-50-years

What are the pros of using alternative credit data?

Using alternative data has the potential to help expand responsible access to credit for people who lack a traditional credit score. For example, someone without a loan repayment history on their credit report might pay other bills or recurring charges on a regular basis. These bill payment histories could demonstrate to lenders that the person will repay a debt as agreed. In other instances, alternative credit data can assist lenders with risk, suppressing consumers who may reveal delinquent payment behaviors.

Improved assessments of creditworthiness

Some lenders might not lend to a person with a credit score less than 620. But those lenders might be willing to do so if they could determine which people are less likely to default on the loan by looking at other sources of data.

More timely information

Data traditionally used by lenders often does not reflect a person's most recent activities. Alternative data could provide more up-to-date, real-time information.

Better service and convenience

Some kinds of alternative data, such as online bank account information, may allow lenders to automate tasks that are done manually during the loan approval process. This automation could speed up application processes or avoid subjective interpretations that could lead to differences in treatment or wrongful discrimination.

Lower costs

Using alternative data could lower costs for lenders and, in turn, benefit consumers through lower prices.

81%

of Americans have a social media profile

Representing a 5% growth compared with the previous year as it was reported in 2017. Facebook, Instagram, Twitter, Snapchat – the platforms are endless.

Can social media data be used for credit decisions? It depends.

On the business front, almost 9 of 10 companies in the United States are using social media for marketing purposes. It's no secret that small businesses especially can soar or sink on social reviews and shares.

The question is: Can banks, credit unions and online lenders look at social media profiles when making a loan decision and garner intel to help them make a credit decision?

In the case of business credit, YES.

Think of the business world and how we operate today. Ready to buy a product? Selecting a place to dine? Deciding on an airline or a hotel? Consumers often turn to reviews. As such, social media data can be used as a decisioning factor for credit review. The FCRA does not apply to business lending. Thus, there are different standards when using various alternative data sets. Alternative data can provide a deep profile of businesses — especially small businesses — that would otherwise be unknown and hard to evaluate. Yelp reviews, Foursquare check-ins and online rankings and ratings can all shed light on a business's health, growth and stability.

On the consumer side, NO.

There are two key concerns when considering social media data as it pertains to financial decisions for consumers.

1. Recall the Equal Credit Opportunity Act, which states that credit must be extended to all creditworthy applicants regardless of race, religion, gender, marital status, age and other personal characteristics. A quick scan of any Facebook profile can reveal these things and more. Credit applications do not ask for these specific details for this very reason. Lenders want to ensure there is absolutely no judgement or bias when evaluating a consumer's creditworthiness.

2. Social media data can be manipulated. One can "like" financial articles, participate in educational quizzes and represent themselves as if they are financially responsible. Social media can be gamed. On the flip side, a consumer can't manipulate their payment history.

There is no question that data is essential for all aspects of the financial services industry, but when it comes to making credit decisions on a consumer, FCRA data trumps all. In short, credit data must be displayable and disputable. Lenders' primary goal is to assess a consumer's stability, ability and willingness to pay. Today, social media can't address those needs. This is not to say that social media data can't be used in the future, but financial institutions are still grappling with how it can be predictive of credit behavior over time.

Regulation

How lawmakers are assessing alternative data

Regulation

Regulatory barriers — especially at the state and local level — deter utility and telecommunications companies from furnishing on-time payment data to credit bureaus.

To help address this issue, Congress is considering bipartisan legislation that would amend the FCRA to clarify that utility and telecommunication companies may report positive credit data such as on-time payments. The legislation unanimously passed the House of Representatives on Feb. 27, 2018 and is now being debated by the Senate. It also requires the Government Accountability Office to undergo a study after two years to assess the effectiveness of the inclusion of on-time payments.

Experian submitted comments in May 2017 that encouraged policymakers to clearly differentiate between different types of alternative data.

What exactly is alternative data?

Policymakers are grappling with the need to more clearly define the term. "Alternative data" often lumps together data sources that meet regulatory standards for accuracy and fairness with data sources that do not.

As part of its analysis, the CFPB launched a request for information in Feb. 2017 that sought comments from stakeholders on the use of alternative data and modeling techniques in the credit process. Experian submitted comments in May 2017 that encouraged policymakers to clearly differentiate between different types of alternative data. It also encouraged focus on the consumer and commercial credit industry on public policy recommendations. The goal is to increase the use of data sources that can be shown to meet legal and societal standards for accuracy, validity, predictability and fairness.[4]

[4]https://www.regulations.gov/document?D=CFPB-2017-0005-0059

Personas

Seeing individuals through the alternative data lens

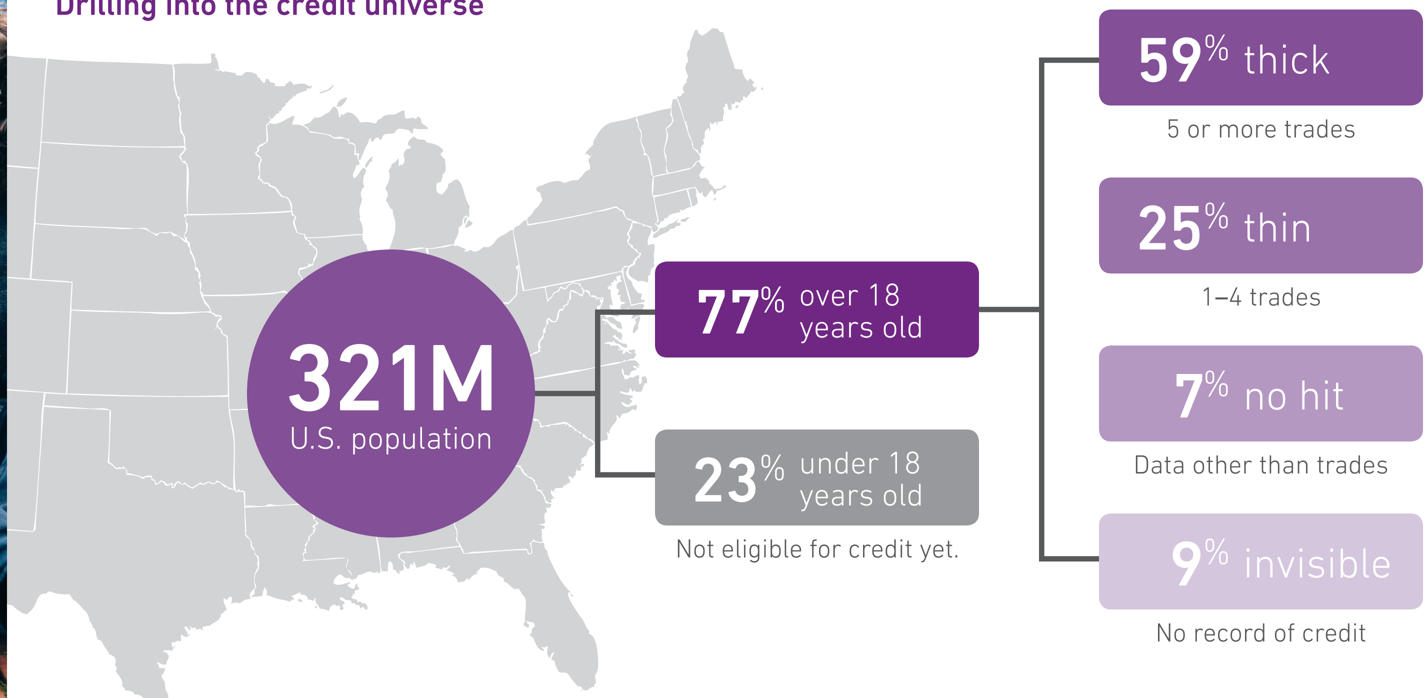
Personas

Alternative finance consumers, who leverage products like rent-to-own, payday and short-term loans, are a key group who could ultimately benefit from alternative credit data. So, who are these individuals?

The average consumer is 42, typically married (61 percent), with some college education (51 percent) and a nearly even chance of being a man or woman (51 percent versus 49 precent). Alternative finance consumers also tend to be much younger on average compared to the U.S. population on the traditional credit bureau's file. In fact, 35 percent are either Millennial or Gen Z, compared to the average consumer who is a baby boomer.

Consumers who use alternative finance have a lower average VantageScore® (579) versus consumers with no history of alternative finance (694) or those on the traditional credit bureau file (677). They also have lower debt and fewer trades, spend less on credit cards and hold higher bad rates.

Drilling into the credit universe

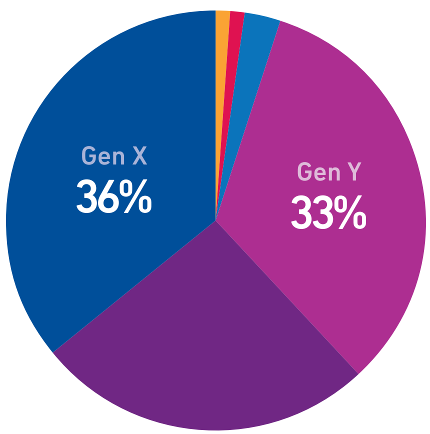


Demographically, alternative finance consumers are younger. Financially, they differ from the U.S. average.

		U.S. average	Traditional finance only	Traditional and alternative finance
DEMOGRAPHICS	Age	52	53	**42**
	% < age 35	22%	20%	**35%**
	Gender M/F	50%/50%	50%/50%	**51%/49%**
	Some college	54%	55%	**51%**
	Married	75%	77%	**61%**
FINANCIAL	VantageScore	677	694	**579**
	Currently 90–180 DPD	3.9%	2.5%	**11%**
	Total debt	$87K	$92K	**$57K**
	Total annual plastic spend	$18.5K	$19.6K	**$9.5K**

Alternative finance consumers tend to be much younger, on average, than the U.S. population on File One.[SM] Additionally, they have lower average scores, lower debt, higher bad rates and much lower spend.

Alternative finance consumers by risk tier and generation



	%	Average VantageScore	Median monthly income	Average total loans amount
Gen Z	1%	505	$1,500	$1,644
Gen Y	33%	566	$2,083	$3,203
Gen X	36%	566	$2,654	$4,776
Boomer	26%	588	$2,500	$6,031
Silent	3%	610	$2,069	$6,700

*Plus 1% of alternative finance consumers are from the **missing** generation.*

Perceptions

Market research on how lenders and consumers view alternative data

Perceptions

Survey methodology

276 financial institutions

540 consumer participants

Experian conducted two national online surveys with both credit providers and consumers regarding attitudes, awareness and use of alternative data.

For the lender survey, 276 partial and completed responses were collected across industries including banks, credit unions, auto finance, mortgage, bankcard issuers and utility providers. The lender survey was fielded Jan. 23 – Feb. 1, 2018. Sixty-two percent of participants were financial institutions. Nearly half (46 percent) of survey respondents are executive leaders. One-third work for organizations that reported asset sizes exceeding $1 billion.

For the consumer survey, Experian conducted a nationwide online survey of 540 respondents balanced to the U.S. Census. An additional oversample of 146 consumers was also gathered to provide insights at the generational level. The survey was fielded March 13 – 19, 2018.

Consumers are open to sharing their credit data.

70% are willing to provide additional financial information to a lender if it increases their chance for approval or improves their interest rate for a mortgage or car loan.

More and more lenders are using alternative credit data to determine if a consumer is a good or bad credit risk.

Recent research by Experian unearthed this and other insights into the growing use of alternative data.

A survey of lender and consumer perceptions about using alternative data for credit decisions found:

80% of lenders rely on a credit report plus additional information.

>50% verify income, employment, and assets and check public records before making a credit decision.

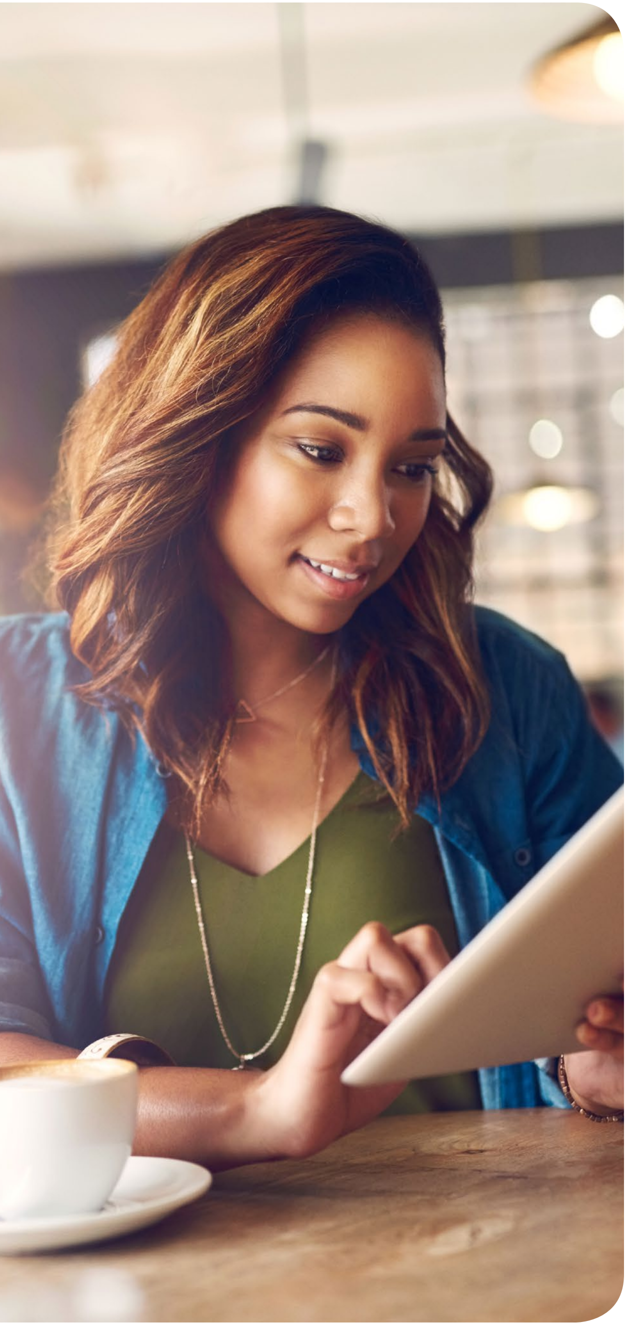
78% believe factoring in alternative data allows lenders to extend credit to consumers who otherwise would be declined.

If given a choice, many consumers would prefer alternative credit data sources be evaluated in their credit history.

These include:

- Utility bill payment history (48%)
- Savings/Checking account transactions (39%)
- Mobile phone payment history (38%)

More than half (53 percent) believe the addtional data would have a positive effect on their credit score.



The survey indicates traditional financial institutions that enhance the client's experience will win. Consumers describe the mortgage application process as "stressful," "time-consuming" and "frustrating."

The ongoing trending topic of digital access to financial data is appealing to **55%** of those consumers surveyed, who believe it would be more convenient. But just **29%** believe that digital access is more secure than providing hard-copy documents to lenders.

Financial institutions may also expand their portfolios, whether it is with clients outside of their current risk tiers or by focusing on Millennials, who will be the recipients of the next generational wealth transfer. More than any demographic surveyed, millennials are projecting they will apply for a mortgage loan, personal loan, payday loan and/or auto loan over the next three years.

Lender insights

Lenders believe the Top 3 benefits of alternative data are:

1. Assessing a consumer's ability to pay
2. Underwriting insight
3. Expanding their lending universe.

71%

of lenders believe consumers will increasingly allow access to their data for lending decisions if they are empowered to turn it on and off.

1 in 6 lenders surveyed by Experian plan to use rental payment or utility data in the future to assist in making lending decisions.

Consumer insights

60%

of consumers believe their credit score accurately represents their creditworthiness.

Meanwhile, 47% of consumers believe they are a better borrower than their credit score represents.

56%

of consumers agree/strongly agree that allowing lenders to access their financial data digitally would be more convenient than collecting hard-copy documents.

Data insights

The stories and trends we see with the new data assets

Data insights

The alternative financial services industry, a $140B market, continues to grow annually at a 7%–10%, offering consumers additional products like payday loans, cash advances, short-term installment loans, rent-to-own and title loans. These alternative finance products are not visible on a traditional credit file, but Experian can append alternative credit data to provide a more holistic view of a consumer.

Traditional credit data, capturing payment insights on things like credit cards, mortgage payments, home equity lines and personal loans, provide intelligence on a consumer's likelihood and ability to pay. But these products are not always inclusive of all the credit products consumers are utilizing today.

Suddenly, we can see if a consumer on the traditional file is using alternative finance products at the same time, revealing how they are treating payments in both spaces. Additionally, alternative credit data can shed a light on an entirely different consumer population not on the traditional credit file. Some of these individuals may have struggled to obtain traditional credit due to immigrant status or simply being young and new to the credit space. Others use alternative finance due to a destabilizing financial event like a job loss or medical setback. And some have been irresponsible with credit altogether, so payday and short-term loans are their only options.

By folding in alternative finance data, lenders can explore both universe expansion and risk mitigation. *(See table below.)*

Universe expansion and risk mitigation is possible with alternative data layered in

Layering on alternative finance data allows lenders to identify the consumers they would like to target and suppress those that are higher risk.

	Old way	New way with short-term lending data
Super prime	Keep	Keep
Prime	Keep	Keep
Near prime	Exclude	DECISION
Subprime	Exclude	Exclude
Deep subprime	Exclude	Exclude

Changing your cut-off score from 660 to 631 but keep the 4.5% bad rate.

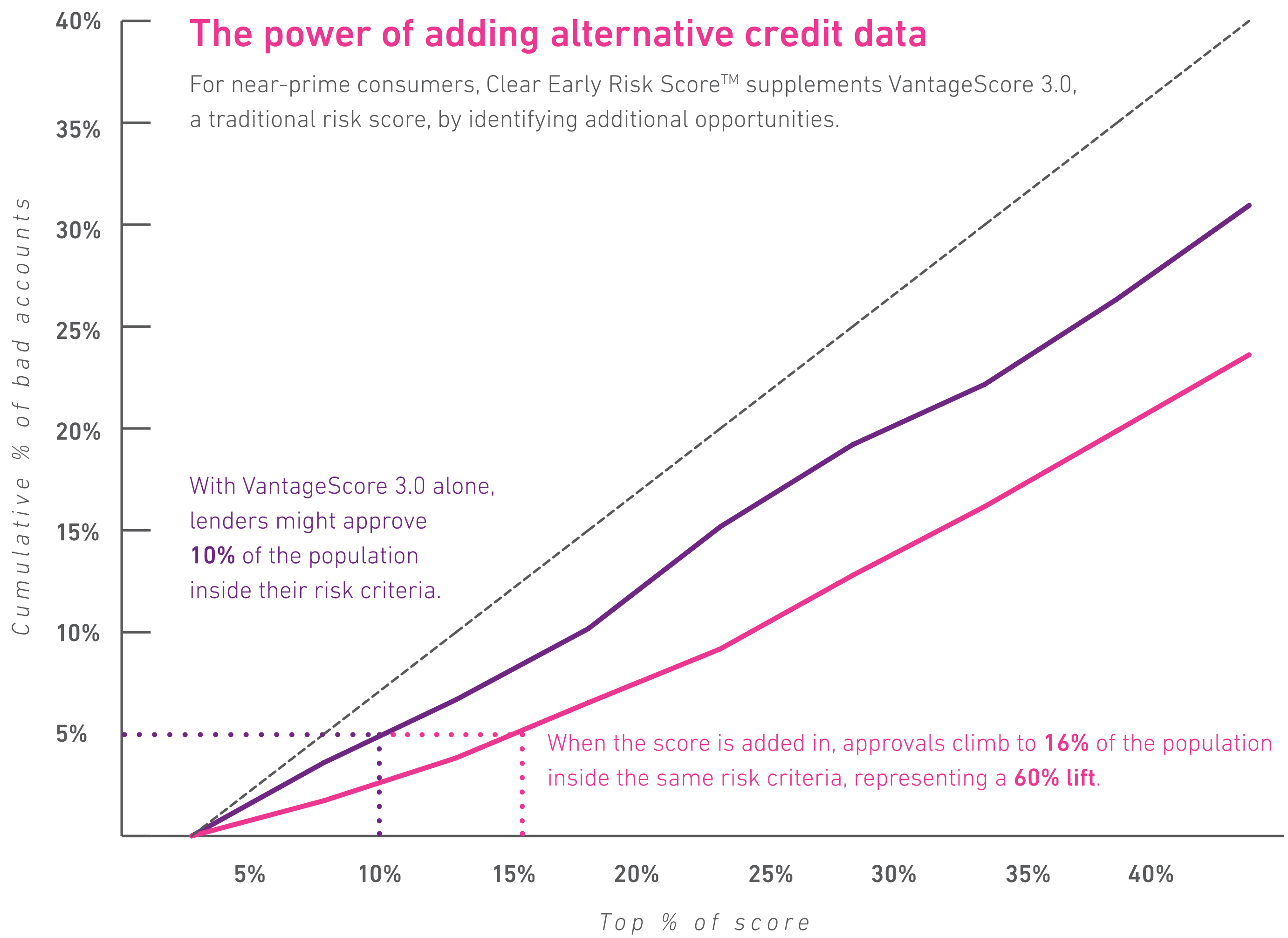
Near prime	No alt data	Bad rate	Has alt data	Bad rate
651–660	Keep	2.9%	Keep	4.5%
641–650	New	3.6%	Exclude	5.4%
631–640	New	4.3%	Exclude	6.5%
621–630	Exclude	5.3%	Exclude	7.7%

Alternative finance users tend to be more subprime, but almost 20% are prime or better.

Measuring consumer stability

One of the most predictive factors to determine intent to repay is a consumer's stability — both in relation to their financial affairs and personal information. In the subprime market, consumer stability is linked directly to future loan performance. The more changes a consumer has in cell phone number, bank account or home address, the higher the likelihood of a default or delinquency.

Additionally, by adding in the visibility of alternative credit data to a near-prime population, lenders could see an increase in the approval rate within a population that was historically being left behind. *(See graph below).*



Spotting the consumer who has no plans to pay you back

When assessing "riskier" consumers, lenders want to know who is likely to pay them back and who is not. What are the red flags to determine the difference between the two?

- Number of payday loans acquired within a year
- Number of first-payment defaults
- Number of inquiries within the past 30–90 days
- Income discrepancies reported by consumer.

The consumers who don't intend to pay happily accept as many loan offers as possible, with no intention of repaying their debt, constituting a form of fraud. Alternative credit data can reveal these behaviors, helping lenders spot risk at the start of the underwriting journey.

Beyond the alternative finance data, other alternative data can be folded in and combined with traditional credit data to aid lenders in underwriting, prospecting and overall account management. Rental data and comprehensive public record attributes can help predict and power risk assessment of historically difficult-to-evaluate consumers. In the case of younger credit-eligible consumers especially, it's not as easy to establish and build a credit history today due to the Credit Card Accountability Responsibility and Disclosure (CARD) Act signed into law in 2009. Insights into rental payment history, therefore, help to provide a much more complete picture of a consumer.

An "unscoreable" individual is not necessarily a high credit risk — rather they are an unknown credit risk. Many of these individuals pay rent on time and in full each month and could be great candidates for traditional credit. They just don't have a credit history yet.

Bottom line: Alternative credit data is one of the most effective tools to cut through the noise and give lenders the predictive attributes they need when it matters most.

Alternative credit data can take the shape of alternative finance data, rental data or deeper attribute insights to shine a light on a consumer's overall stability. Overall, it's clear these additional fields deliver a more complete view of today's credit consumer.

The future

What's to come?

Consumer-permissioned data and beyond

The Future

What is consumer-permissioned data?

This data is typically obtained with the consumer's permission by either screen scraping or application program interfaces (APIs). It can enable lenders to access various accounts, including checking, savings and 401(k) accounts, in a more streamlined, digital fashion.

The volume, velocity and variety of data is growing exponentially every year. More than 90 percent of the data in the world has been generated in just the past five years.

What does this mean for alternative credit data?

It's a safe bet to believe new data sources will continue to emerge in the years to come — and some of these data sources will benefit both lenders and consumers as credit decisions are considered.

Already, lenders are finding ways to leverage consumer-permissioned data. For example, in the mortgage approval and underwriting journey, income and asset verification are generally required. Retrieving data directly from a consumer's financial accounts provides a fuller financial picture, resulting in better risk assessment. No need to scan documents or rely on consumers to provide paper copies. Consumers can simply digitally permission data to the lender, leading to faster decisioning.

Additionally, new scores and models are in development, combining traditional and alternative credit data sources.

By pulling in new data sources that include alternative financing, account aggregation, and on-time utility and rental payments, we can provide a more holistic view of all consumers. These insights can help lenders identify and prevent fraud, determine an applicant's ability to pay and verify an identity.

Ultimately, it can improve credit access and decisioning for millions of consumers who may otherwise be overlooked. The data exists. Now the opportunities are unfolding to leverage it in all-new ways to reveal today's diverse consumer base.

To learn more about Experian's alternative data solutions, visit www.experian.com/alternativedata.

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