Experian Risk Radar Report

October 2021

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Executive summary

2021 a year for decisive risk leadership

Pressure is growing for Australian banks and credit providers to improve their credit risk management processes amid a changing and volatile economic landscape.

As Covid-19 thrust financial hardship and default into the spotlight, other underlying social, economic and policy factors have highlighted the importance of managing risk.

Experian, the world's leading global information services company, spoke to six of Australia's senior risk leaders for the inaugural Risk Radar report on risk management and credit decisioning trends. Their in-depth insights were combined with an independent survey conducted by Forrester of 164 APAC banking, fintech and non-banking lender decision-makers – including 54 from Australia – who manage credit risk.

The report found the most critical priorities for Australian lenders was to improve regulatory compliance and update credit policies, while paying close attention to the potential easing of Responsible Lending regulations introduced after the Hayne Royal Commission.

While the Federal Government considers winding back regulations to help more Australians access credit and stimulate the economy, the report found the same result could be achieved by lenders improving their credit decisioning[1].

More than half (54%) of the Australian risk leaders surveyed[1] said their lender was currently declining viable customer applications because they lacked sufficient credit data. With less than half of credit providers making use of the wealth of data available to them[1], it's not surprising applications are being incorrectly rejected.

While risk leaders are well aware of the impact declined customers have on business growth objectives, the research also identified Australian decision makers were highly conscious of the alternative. Two thirds (61%) of Australian lenders acknowledged a poor credit decision could put their customer in financial hardship - the highest of the three countries surveyed[1].

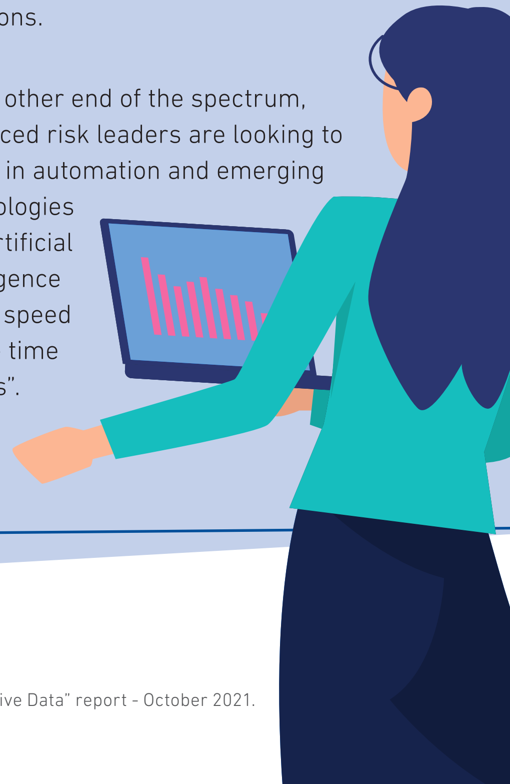
However, as appetite for credit risk has reduced, the battle for Millennial market share is ramping up between traditional lenders and new, nimble fintech entrants. This has posed a new challenge to some lenders with legacy systems, who must find a way to compete with loan approvals in a matter of minutes, rather than hours or days.

Key 2021 Risk Radar findings

1. Lenders are turning away worthy credit customers because of a lack of credit data and difficulty navigating the complex regulatory environment.

2. The maturity of the sector is inconsistent: Many traditional lenders are still improving their access to data sources and analytics capabilities to make better and more efficient decisions.

3. At the other end of the spectrum, advanced risk leaders are looking to invest in automation and emerging technologies like Artificial Intelligence (AI) to speed up the time to "yes".



[1] Forrester and Experian "Drive Speed and Accuracy with Emerging Technology and Alternative Data" report - October 2021.

Top credit risk priorities for Australian risk leaders 2021

Improving regulatory compliance

78%

46% | 31%

Critical | High priority

Modernising legacy systems

70%

35% | 35%

Critical | High priority

Updating credit policies

65%

41% | 24%

Critical | High priority

Leveraging new data sources

60%

30% | 30%

Critical | High priority

Leveraging emerging technologies like AI

57%

31% | 26%

Critical | High priority

Top business priorities for Australian lenders 2021

Grow revenue

76%

Critical	High priority
30%	46%

Improving customer experience

72%

Critical	High priority
46%	26%

Improve employee experience

69%

Critical	High priority
39%	30%

Accelerate the shift to a digital business

67%

Critical	High priority
37%	30%

Improve ability to innovate

64%

Critical	High priority
33%	31%

Improve the use of data and insights in business decision making

65%

Critical	High priority
43%	22%

Tools, techniques and technology used to conduct credit risk and fraud management today

Risk management software and technology (e.g. Experian, other provider)	54%
Digital and electronic signatures	50%
Open Banking technologies (e.g. APIs)	41%
AI	39%
Advanced data analytics	35%

Less than half of Australian credit risk leaders surveyed said their organisation was accessing the wealth of data sources available to them, including:

- Digital transaction data
- Banking data
- Credit Bureau data
- Alternative lending and Buy Now Pay Later (BNPL) data
- Employment and tax data
- Subscriptions data
- Payroll (income) data

Perceptions of industry performance

Risk Radar leaders have mixed views on Australia's risk management strategies and credit decisioning. While companies are doing an adequate job, many leaders identified room for improvement across the risk management lifecycle:

33%

At the customer acquisition phase[2]

60%

During customer management[2]

25%

During the hardship and collections process[2]

Australia's views on the industry are worse than perceptions across APAC, where 90% of risk leaders believe their organisations are doing an adequate or excellent job at credit risk decisioning[2].

Australian risk leaders rated their credit risk decisioning on average 9% lower than their international colleagues, across customer acquisition, customer management, hardship and collections management, and reducing fraud loses. Reducing credit losses (+7%) was the only stage Australian lenders said they were exceeding[2].

One risk leader from a large Australian bank said: *"The regulatory environment can be quite complex, resulting in aspects of applications requiring thorough oversight in place of procedural automation."*

Overall, half of risk leaders said proactive financial stress management was very or extremely important to the industry[3]. Two-thirds of leaders (66%) said the first sign of financial stress was when a customer missed a payment, while only one in six were able to identity red flags using a customer's transaction data[3].

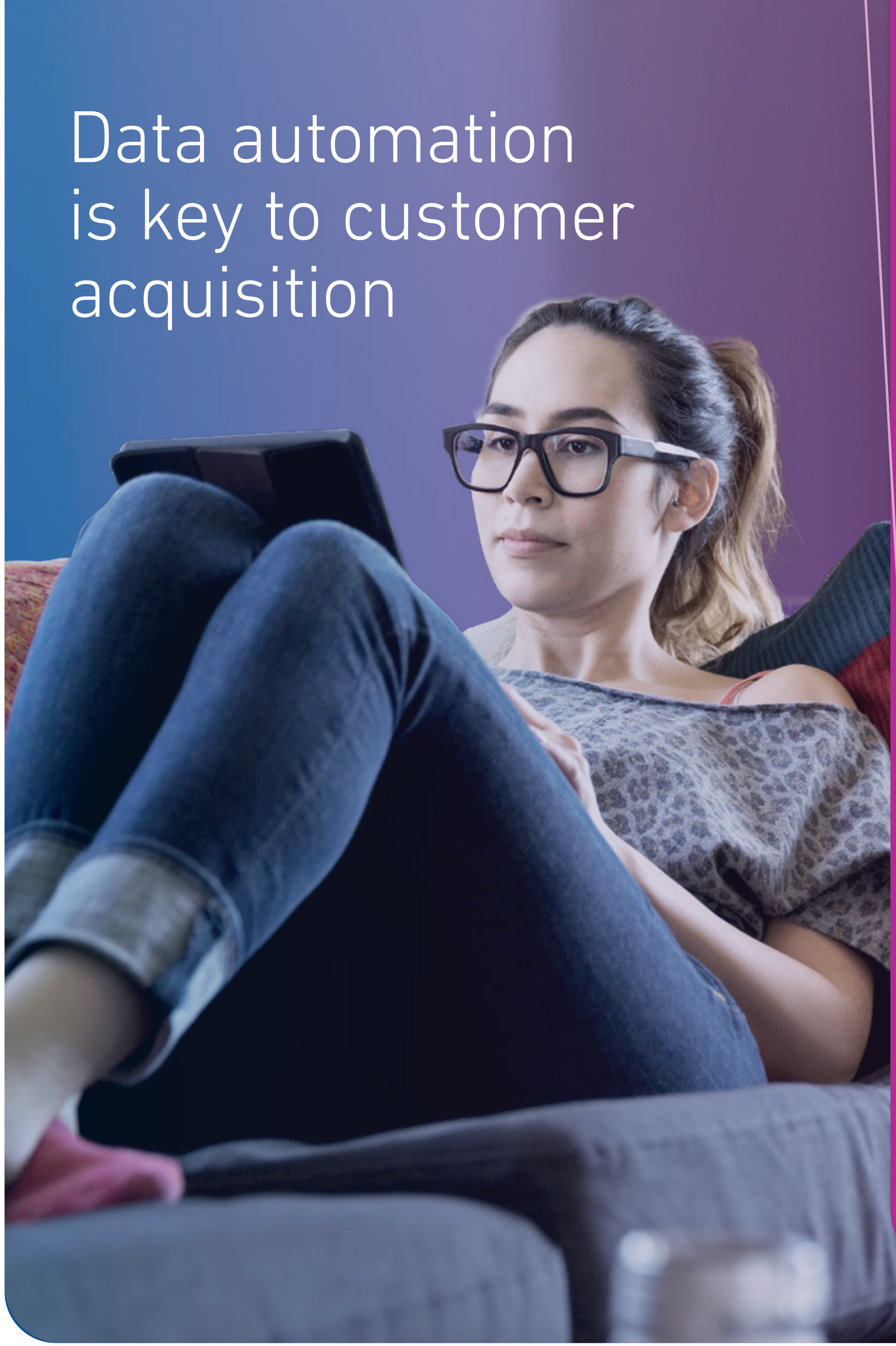
Decisioning technology innovation

Risk leaders need to strike the balance between ensuring a smooth and efficient interaction and making a thorough and robust decision based on a person's ability to afford a line of credit. It's crucial to get to the right decision quickly while protecting both the consumer and the lender from the point of application and throughout the customer relationship. The key lies in having easy access to a wealth of reliable data.

Open Banking data can be used in association with current account turnover data, transaction data and credit information, to reach the fastest path to a decision. Emerging technology and tools could provide additional insight to income shock, employment status, use of overdraft, liquidity and spend characteristics for example. This could help lenders meet every individual's unique needs and goals along the way.

[2] Experian Risk Radar research - August 2021

[3] Forrester and Experian "Drive Speed and Accuracy with Emerging Technology and Alternative Data" report - October 2021



Data automation is key to customer acquisition

Recent Experian research conducted in June 2021 shows three-quarters of Australian consumers believe home loans should happen in three days – and most of these (50%) expect approval within just 24 hours.

However, lenders have reported turning away credit customers entirely because of a lack of data.

Traditional lender challenges

33%

Face automation challenges because their technology is not mature enough[4]

26%

Face automation challenges due to existing legacy technology and systems[4]

52%

Say automation improvements would increase the speed of credit decisions[4]

50%

Say it would reduce manual errors in risk decisioning and management process[4]

[4] Forrester and Experian "Drive Speed and Accuracy with Emerging Technology and Alternative Data" report - October 2021

While some lenders are in the process of significantly transforming their legacy systems, other nimble lenders and fintechs, as well as BNPL platforms are already meeting demands for frictionless onboarding and approving customer loans in just mere minutes. So how can traditional banks compete with new fintech entrants and enhance the customer experience?

Investment in automation that improves data and analytics capabilities is the answer, according to 73% of Risk Radar leaders surveyed.

Adopting emerging technologies like AI can solve ongoing issues with customer acquisition by creating better data insight that allows for faster credit decisioning. By creating more sophisticated risk models using new technology, lenders can ultimately improve customer management, reduce credit losses and minimise fraud.

Large bank risk leader...

"Automated decisioning is key with an improved application of the quantitative risk lens. Risk based scoring would particularly further benefit products like mortgages. However, the structure of the market would need to change for this."

Online lender risk leader...

"To a large extent, credit risk has been traded away for managing regulatory risk and fear of lending. I think there is great opportunity to treat consumers as true individuals by leveraging the data that's available to help make the best risk and price point decisions."

Risk strategy under review

Risk strategies are under the microscope as lenders aim to balance their commercial goals with their appetite for risk. The vast majority of risk leaders (83%) believed risk strategy has been very or extremely important to business performance in recent months amid the Covid-19 pandemic[5].

Right now, leaders report the major economic, social, technological and industrial factors influencing risk strategy are:

1. Covid-19 impacts on loan deferrals, house prices and interest rates[5]
2. Proposed changes to Responsible Lending regulations[5]
3. Impacts of BNPL on customers, including collections and arrears[5]
4. Hardship Flags and Consumer Credit Reporting (CCR) changes[5]
5. New Design and Distribution Obligations (DDO)[5]

Australia's Open Banking regulations were a critical or high priority for two in three (61%) Risk Radar leaders, however many were still taking a 'wait and see' approach, monitoring the implications of the UK's more advanced Open Banking regime[5].

MoneyPlace: *"There are ongoing macroeconomic factors and implications of vast areas of the country undergoing lockdowns - while 2020 was much more resilient and upbeat than most people expected, some of those tailwinds remain, but headwinds are gathering strength."*

Risk Radar leaders were split 50/50 on whether risk strategy should be reviewed continuously, or on an annual or biannual bases[5].

One risk leader from a large Australian bank said: *"It should be continual depending on the changing environment. A risk strategy needs to answer the desire of managing risk and growth, taking into account the economics and competitor activity."*

A risk leader from an online personal loan provider said: *"Proactive [reviews] should be considered regularly, with changes as required ...but given the past 18 months, there has likely been more reactive updates! In terms of the frequency, to some extent this will depend on each provider's underlying technology - some might only be able to make changes monthly or quarterly in line with enterprise releases, while others might have the ability to make changes weekly or even daily if they wanted to."*

[5] Experian Risk Radar research – August 2021

Keeping it simple for customers

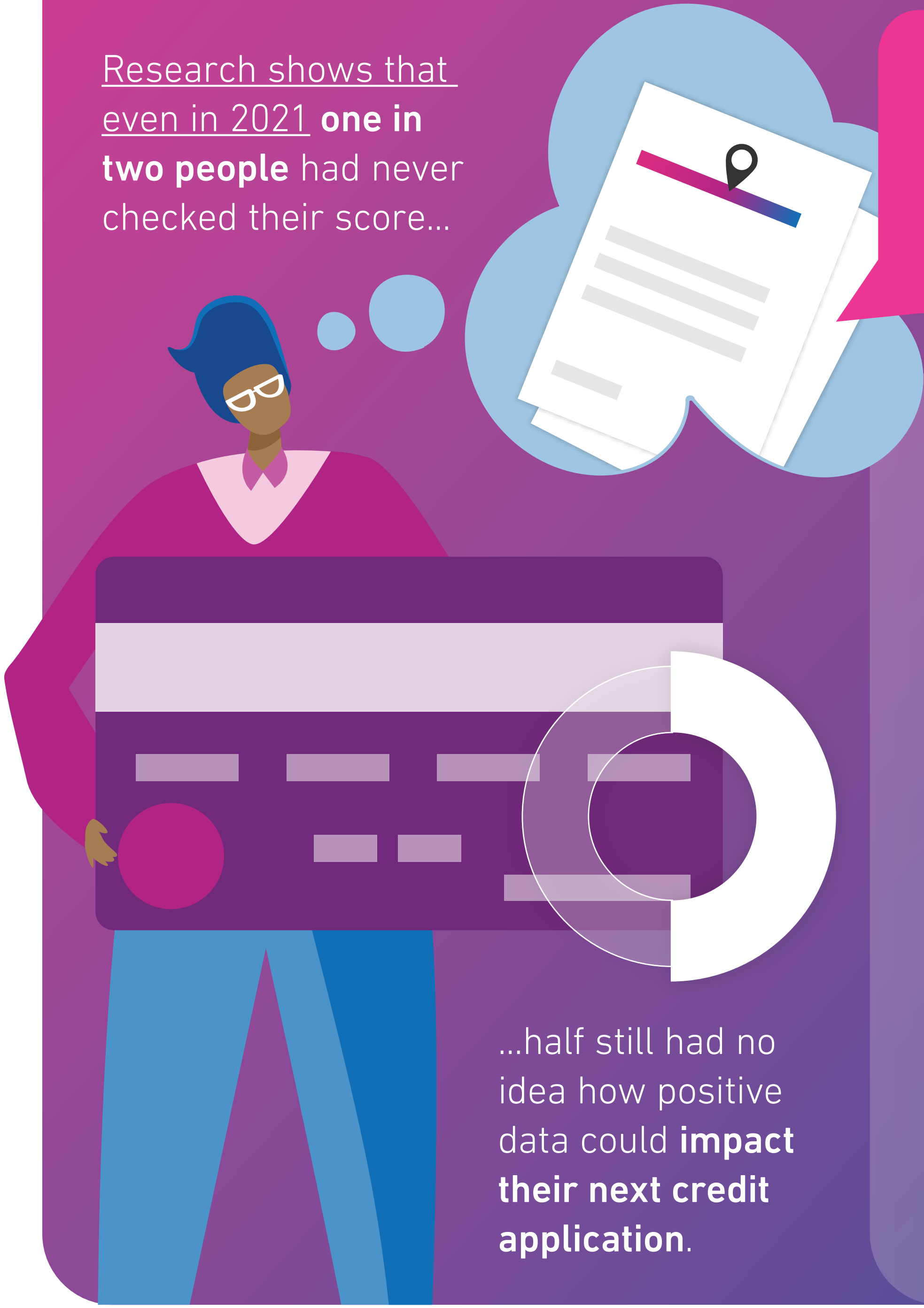
Risk leaders believe customers do not demand or need complicated or unnecessary information about how credit providers assess risk. Not only could an information overload confuse customers, but it could also open the door to fraud by giving away too much detail about exactly how applications are assessed, according to some risk leaders.

Risk leaders believe customers need detail on:

- Length of processing time
- How credit scoring works
- Whether they have been approved or not for a line of credit

At Experian we've been helping to educate consumers about their credit scores and how they're calculated. Unlike markets such as the US, where knowing your credit score is common, many Australians have still never checked their score.

Research shows that even in 2021 **one in two people** had never checked their score...



...half still had no idea how positive data could **impact their next credit application**.

"More effort should go into financial awareness and the impact credit products may have on a customer's situation."

–Great Southern Bank

MoneyPlace

"There should be some easy-to-understand collateral about why risk assessment is important, how it impacts what people can borrow, and at what price, and the long-term implications of different types of credit. It should be available on company sites, together with general approaches available on CRBs [Credit Reporting Bureaus], industry / peak bodies and government pages."

People's Choice Credit Union

"Customers should have fast and easy access to their credit score and what they can do to improve it."

Methodology

Forrester and Experian "Drive Speed and Accuracy with Emerging Technology and Alternative Data" report

In this study, Forrester conducted an online survey of 164 Financial Services decision-makers at organisations in Australia, India and Indonesia to evaluate the state of credit risk and fraud management in APAC. Survey participants included decision-makers in credit and fraud risk, IT and business/product roles. The study began in June 2021 and was completed in October 2021.

Experian Risk Radar research

In this research conducted in August 2021, Experian spoke to six of Australia's senior credit risk leaders from banks and fintechs on risk management and credit decisioning trends. Their in-depth insights were combined with the Forrester "Drive Speed and Accuracy with Emerging Technology and Alternative Data" report.

About Experian

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We have 17,800 people operating across 44 countries and every day we're investing in new technologies, talented people and innovation to help all our clients maximise every opportunity. We are listed on the London Stock Exchange (EXPN) and are a constituent of the FTSE 100 Index.

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