4most Credit Risk Market Update

Keeping you up-to-date with our latest expert insights

April 2022

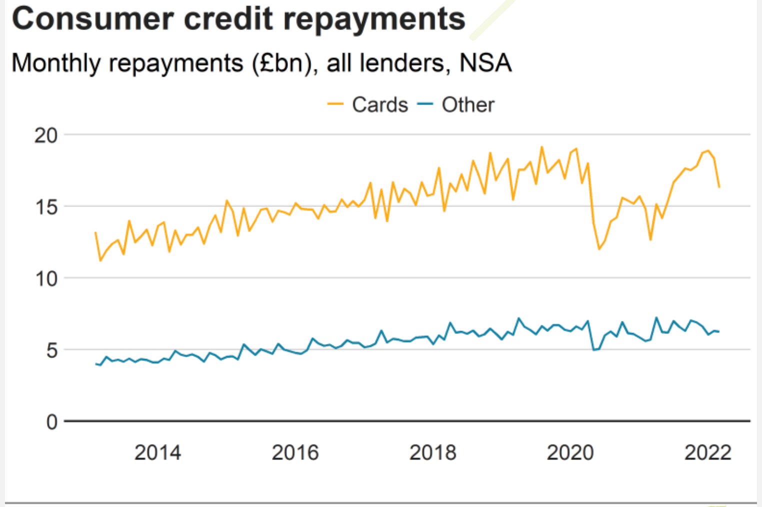
Are measures announced in the Spring Statement enough?

Measures outlined by the Chancellor may help at the margin, but do not change the reality – an unprecedented shock to the cost-of-living is underway and support measures don't mitigate the shock, leaving poorer households vulnerable.

Increasing the National Insurance threshold and cutting fuel duties means the median household now faces around a 4% cut in effective real income. But the hit will be around 6% for those at the bottom end of the income spectrum, who are reliant on benefits.

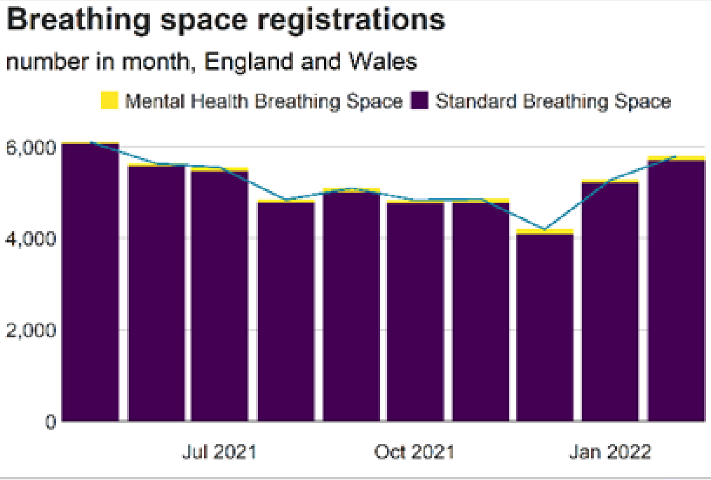
Repayments in unsecured debt, and in particular credit cards fell in February - an initial sign of financial stress

While the focus is understandably on recent rises in petrol prices and the 50%+ increase in domestic fuel bills, many have been feeling the squeeze since last summer. There were already signs of stress in February as the amount paid off credit card balances plummeted. While, in credit risk terms, it is unsecured lending where credit losses are likely to be focussed, rent arrears are also set to rise.



Source: Bank of England

The number of people registering for "breathing space" from creditors have been rising since December.



Source: Insolvency Service

The numbers seeking protection from creditors rose again month-on-month.

There are difficult months ahead for many families, particularly if the current level of wholesale gas price remains high, as it would mean another jump in fuel bills in October.

The Chancellor may well have to look again at the level of support he has given; poor local election results in May might trigger this rethink.

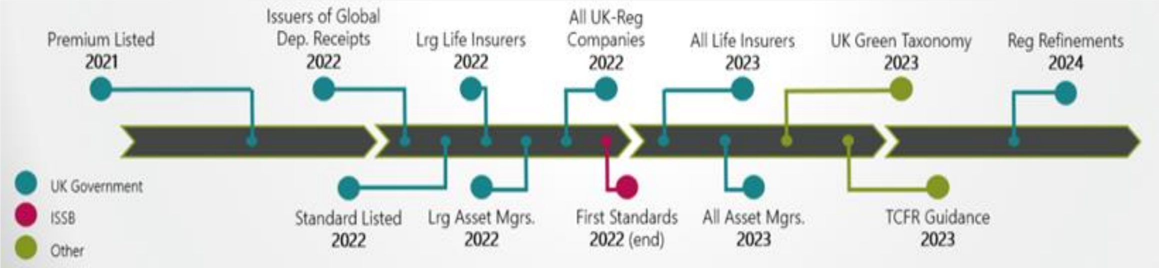
4-most.co.uk
info@4-most.co.uk

4most Credit Risk Market Update: April 2022

Keeping you up-to-date with our latest expert insights

Introduction of Mandatory Climate Risk Reporting Requirements: It is almost here…

This month, subject to parliamentary approval, mandatory Climate Risk reporting will become law across the UK.



The move formalises a 2020 announcement to progressively require reporting consistent with the FSB's TCFD (Task Force on Climate-Related Financial Disclosures) framework . One significant and additional inclusion is a requirement for qualitative scenario analysis, as announced during last year's COP26 summit by the UK Chancellor of the Exchequer, Rishi Sunak.

This is in addition to the four standard TCFD disclosure pillars: Risk Management Assessment, Strategy, Governance, Metrics and Targets, which each have their own detailed disclosure guidance.

For example to account for, and disclose, financed GHG (Green House Gas) emissions businesses will need to be familiar with the PCAF (Partnership for Carbon Accounting in Financials) standards and their additional requirements such as detailed knowledge of customer emissions.

There will be opportunities presented by these developments. Those companies with a methodical, embedded approach to recognising the impacts of climate change on their activities – as facilitated by these regulations - will similarly be first to recognise the opportunities, as they arise.

UK based regulations however, are only part of a much wider swathe of Climate Risk Disclosure regulations, unveiled by various governmental and industry bodies.

Where the UK Government focuses on climate Metrics, Governance, Risk Management and Strategy; wider focus from other bodies have started to address measures such as capital adequacy, and reporting standards and these include

- EU Green Capital Ratio assessments,
- Sustainability Reporting standards by the IFRS' International Sustainability Standards Board,
- UK and EU Green Taxonomies, and;
- recommendations from the Basel Committee.

US companies are likely to face similar requirements to those of the UK and EU, with the SEC releasing a first draft of planned mandatory Climate Risk reporting requirements this week.

FCA Strategy Letters' Summary: Focus 2022

The FCA has published letters sent out to mortgage lenders detailing their areas of focus for the upcoming year. Three of these focus areas are supporting customers in difficulty, treating vulnerable customers fairly, and helping mortgage prisoners.

Although the CONSUMER DUTY is yet to be finalised the FCA continues to expect firms to treat customers fairly. This includes an expectation that firms support customers through the current difficult financial environment and that the Tailored Support Guidance, set out in response to COVID, continues to provide an appropriate forbearance framework

Firms are expected to evidence ongoing monitoring of outcomes for VULNERABLE CUSTOMERS. Firms must also evidence changes, as a result of this monitoring, that enhance outcomes for these customers.

The FCA wants to further support MORTGAGE PRISONERS, and those at risk due to approaching the end of their interest only mortgages. The FCA has asked firms to consider adjusting their lending criteria to allow lending to mortgage prisoners who are close to their risk appetite, whilst ensuring that they have a clear communication strategy in place to give interest only mortgage customers time to act before the end of their term.

4most Credit Risk Market Update: April 2022

Keeping you up-to-date with our latest expert insights

Consumer Duty: Role of Quantitative Analysis

We see that one of the key takeaways from the consumer duty is the role that quantitative analysis can play in providing firms with the evidence and assurance they need that their products are appropriately designed and are meeting expectations over time.

With the broad scope of changes, and a slated implementation date of April '23, firms need to be taking action now to ensure they're compliant. And that's where we'd recommend all firms start – a detailed gap analysis against the requirements to highlight focus areas, followed by a clear programme to address those gaps.

> That means you don't need to wait for us to give detailed rules – you can get a head-start now by making sure you have the right mindset, culture and data in place, and looking for gaps between where you are now and where you'll need to be - Brian Corr, Interim Director of Retail Lending said in a speech to the 2022 Credit Summit

By taking a quantitative approach to forecasting and monitoring, firms can be confident that they have designed products that are appropriate and customers are receiving the expected outcomes

Outcome Prediction

Use of quantitative analysis to forecast outcomes where multi-state survival analysis can be used to estimate outcomes across key customer groups and ensure products are designed to mitigate potential poor customer outcomes

Pricing and Fair Value

Techniques such as unit economic analysis can be used to evidence that pricing remains fair across product and customer groups. Such quantitative analysis can provide baseline expectations for a product, and clearly evidences that the design stage properly considered customer outcomes,

Early Warning

This is key for providing early warning if customer outcomes are deviating from expectations, allowing corrective actions to be taken swiftly to mitigate against poor customer outcomes.

Robust Monitoring

Quantitative analysis can provide a solid baseline of expectations to monitor actual performance against throughout the product lifetime.