4most Credit Risk Market Update

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

December 2021

Consumer credit write-offs

Labour market remains resilient indicating the success of vaccines and furlough scheme.

It is now clear that the peak unemployment rate during the crisis was 5.2% in October-December 2020. This is a much better outcome than anyone was expecting a year ago and is testimony to the success of both vaccines and the government's furlough scheme.

But write-off rates remain flat so far.

Even though the rise in unemployment was muted, it would be expected to have some impact on write-offs of consumer credit given the historic relationship. But the write-off rate, as yet, has been remarkably flat.

At the margin, the rise in Universal Credit at the start of the pandemic provided some extra support for those losing their jobs. There may be some stress to emerge from the removal of this support.

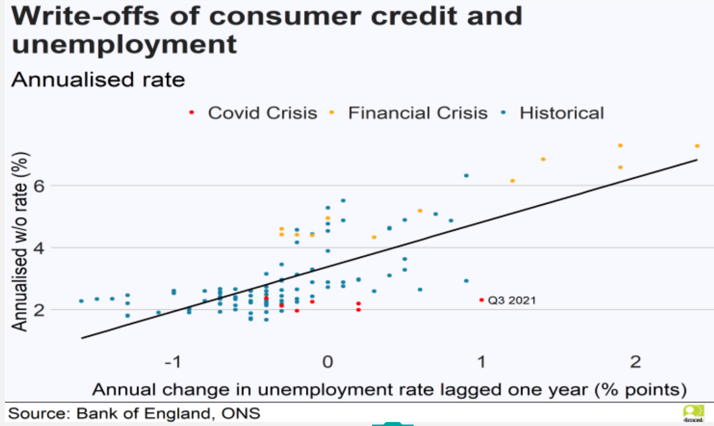
But a more optimistic view would be that this time it really is different. Most of those that lost their jobs are now back in employment. The single-month estimate of the rate was just 4.2% in October.

Recent employment data suggests that finding a job was easier compared to previous recessions.

It has been much easier than in previous recessions for those losing their jobs to find new roles given record levels of vacancies. The combined 331,000 increase in payroll employment in Oct/Nov confirms no nasty surprise at the end of furlough.

But downside risks for credit losses include higher long-term unemployment and SME's debt burdens.

It is not quite time to say that the crisis was a non-event in terms of consumer credit losses. Long-term unemployment is higher. And the big uncertainty of how many SMEs will fail under their higher debt burden remains. These companies provide c60% of private sector employment.



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Regulatory Update

The recently published 4th edition of the regulatory roadmap sets out the planned regulatory changes for the coming year, spanning a variety of key areas. Among the most interesting of these are:

ESG – introduction of disclosure rules and the FCA planning to scrutinise firms' net zero transition plans.

Continuing work on the planned Consumer Duty, with the 2nd consultation published on 7th December. This reflected on the responses to the previous consultation and set out several significant points such as replacing core principles 6 & 7 for retail firms with the new Consumer Duty principle , giving more detail on the planned approach to supervision and enforcement, and for now at least proposing not to include a formal Private Right of Action

Diversity & Inclusion – regulatory work to drive improved D&I continues with a consultation in H1 22 and a policy statement planned for H2.

A New Consumer Duty

The intent is to put in place a ruleset that raises the standard of care, ***delivers good outcomes for customers*** and require firms to demonstrate they are ***acting in the best interest of their customers***

One of the most far-reaching upcoming regulatory changes is the proposed new Consumer Duty. Aiming to create a culture where good consumer outcomes are front and centre of all aspects of a business, from Boards to front-line staff, the potential impact is significant.

The FCA's 2nd consultation was published on the 7th December, firming up on areas where multiple options had been presented, such as proposing that PRINs 6 & 7 be disapplied where the new Consumer Duty principle is applicable, and reflecting concerns flagged by respondents in others – such as clarifying that the entire duty is founded on the concept of reasonableness, and removing the explicit reference in the cross-cutting rules to taking "all reasonable steps" (which many had feared was an unattainably high standard). Many industry stakeholders will be relieved that this consultation proposes not to include the mooted Private Right Of Action (PROA), although it should be noted that the FCA has not completely closed the door on this as yet – referring to not introducing it whilst the duty is being implemented and including an explicit reference to reviewing the PROA in light of industry's compliance with the new duty. This consultation remains open until the 15th Feb '22, and proposes that the new rules would take force from April '23.

Watch this space in the new year for an analysis of the likely impacts.

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Climate change regulation - COP26

November saw the UK host the 26th UN Climate Conference of Parties ("COP26"), hoping to keep the Paris Agreement's +1.5°C temperature increase target within reach. The pivotal role that the Financial Sector plays in achieving this objective was recognised and debated. The COP featured efforts to spread and consolidate the Sector's climate disclosure requirements and improve the transparency of these disclosures.

The formation of the International Sustainability Standards Board (ISSB) – in effect, an offshoot of the IFRS – was a key announcement. This body would construct an authoritative set of climate reporting standards to replace the numerous voluntary frameworks that currently exist. 95% of world securities markets would be obliged to follow these standards, and a sample disclosure has now been made publicly available.

The UK Government announced an intention to support the ISSB's standards through its Green Finance Roadmap, released last month. The Government would further require companies to demonstrate their plans for the transition to a net-zero emissions economy by 2023. UK registered corporates, listed entities, asset managers and owners (pension schemes, insurers etc.) would all fall into scope. These would supplement existing legislative measures for mandatory TCFD-style climate disclosures, which will come into effect by April 2022.

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