



Alternative Credit Data Impact Report

A study of the adoption, utilization and impacts of alternative credit data



Adoption of alternative credit data is growing rapidly to help refine account origination strategies and improve lending outcomes with a focus on financial inclusion, portfolio growth and improved competitiveness.

Research background



Methodology

LexisNexis® Risk Solutions has conducted a nationwide survey to assess the adoption and utilization of alternative credit data across different financial institutions for credit portfolio management and growth in consumer and small business lending.

Through Q3 and Q4 of 2022, 225 online and phone-based surveys were completed by senior decision makers for marketing, lending and credit risk in U.S. financial institutions.

Quantitative surveys were followed by in-depth interviews with a small group of consumer credit lending leaders to gather follow up context and insights on the qualitative findings.

Defining alternative credit data

In today's quickly evolving credit landscape, the traditional credit data leveraged in standard credit reports and scores might not provide the most accurate and up-to-date picture of consumer behavior — which can have a significant impact on portfolio growth and profitability. Alternative credit data goes beyond traditional credit data to deliver a broader, more comprehensive picture of consumer creditworthiness, helping financial institutions (FIs) improve risk assessment and identify new opportunities.

Alternative credit data — or simply “alternative data” — is a category of insights which are **not present in traditional credit reporting solutions**, but which adhere to the necessary regulatory and industry standards needed to be leveraged in consumer and/or commercial credit decisions.



Examples of insights which can fall into the alternative credit data category:

1

Life event insights

(professional licenses, asset ownership and public records)

2

Modern credit-seeking behavior insights

(from markets like online lending and short-term lending, which infrequently post hard inquiries to national credit reporting agencies)

3

Rental data and some forms of consented data

Lenders and service providers can leverage alternative credit data to make better, more informed credit decisions — driving growth, efficiency and loss savings across the customer credit lifecycle.

This report will examine the high-level findings from the LexisNexis Risk Solutions nationwide survey on alternative credit data, with a particular emphasis on the adoption and value of these insights across industries and use cases. Subsequent reports will drill down more into specific consumer and commercial lending use cases and qualitative learnings.

KEY FINDING 1

Financial inclusion, increased visibility and improved segmentation driving adoption of alternative credit data

84% of respondents use alternative credit data in marketing and credit risk across the customer lifecycle

When asked which kind of alternative data respondents used in credit risk assessment, risk managers selected an average of 12.6 alternative data types, with **cash flow data, property and asset records and demand deposit account (DDA) info** in the top 3.

Digging a little deeper, at least two-thirds of FIs also used rental bill payment history data for credit risk assessment.

Deeper analysis reveals portfolio management and growth as a top use case for alternative data across FIs

Beyond the headline findings — that over 84% of respondents utilize alternative data assets and in-fact **typically use more than 10 sources** — two of the top three data types are notable because they're often being sourced from within these lenders' own institutions.

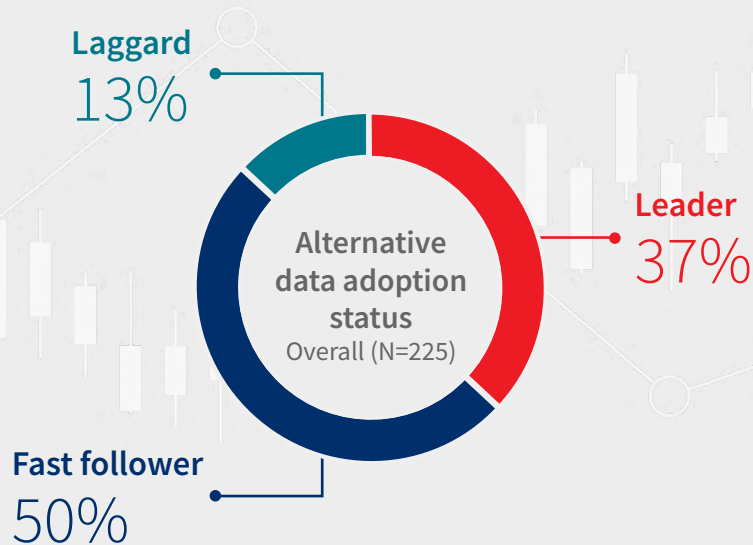
While the coverage of signals like cash flow and DDA insights can be limited when assessing non-existing customers in marketing and account opening use cases, their **value is very significant** particularly in portfolio management — and often represent an easier entry point into alternative data than some external sources.

Alternative data type	Overall adoption	Adoption by function	
		Credit risk	Market
Cash flow	83%	87%	78%
Property and asset records	73%	77%	70%
Demand deposit account info	73%	77%	69%



KEY FINDING 1: Driving Adoption of Alternative Data

Lenders who identified themselves as leaders in alternative credit data adoption are more likely to be driven by financial inclusion as their primary objective



Adoption leaders' top objectives:

- Financial inclusion = 55% (banks 62%)
- Improve segmentation = 37%
- Improve swap in/swap out = 24%

Many financial institutions perceive themselves to be fast followers with alternative data adoption



Banks



Non-bank lenders

46%
see themselves as adoption leaders

19%
see themselves as adoption leaders

Looking only at banks, 46% see themselves as adoption leaders — and 92% of Tier One banks (those with loan portfolios exceeding \$1B+) see themselves as adoption leaders. Financial inclusion was a top objective for 55% of respondents, more than half of which were banks.

Non-bank lenders lagged behind other sectors, with only 19% considering themselves adoption leaders.

Financial inclusion — efforts aimed at consumer segments with less credit visibility — is a natural starting point for lenders adopting new alternative credit data signals. These results largely adhere to the industry perception.

Those with a credit-risk role focusing on consumers are also more likely to consider themselves leaders in adopting alternative credit data compared to commercial lenders.

KEY FINDING 1: Driving Adoption of Alternative Data

Frequency of using alternative credit data on new applicants

Fewer than 25%	1%
More than 25% but less than 50%	8%
More than 50% but less than 75%	29%
More than 75% but less than 100%	36%
All applications	26%

Top objective for FIs using on all applications:

- Financial inclusion = 42%
- Improve segmentation = 27%
- Improve swap in/swap out = 12%

62% of FIs leverage alternative credit data on 75% or more applications, but adoption still focuses heavily on deep subprime to near prime applicants

Frequency of alternative credit data use shifts significantly across different types of lenders, with notable fluctuations in use rate at both the high and low ends.

Banks (31%) and credit unions (26%) are the most likely to use alternative data to assess all new accounts, compared to FinTechs (19%) and non-bank lenders (17%). Essentially half of non-bank lenders use alternative data to assess 50%–75% of new applicants, while less than a quarter of FinTechs use alternative data to assess 25%–50% of new applicants.

Thinking about financial inclusion at account opening, while rates can vary, most nationwide financial institutions will see roughly 20–25% of applicants as being “unscorable” with traditional credit data — and typically approve them at a significantly lower rate than “credit scorable” applicants.

These results underscore the fact that while financial inclusion may be an entry point for organizations adopting alternative data, the application of these insights often expands quickly into strategies addressing near prime and increasingly prime prospects and customers.

“

Financial inclusion is definitely the most important factor when we use alternative data. We can leverage alternative data to try to differentiate the bad and good, which will help the bank to approve more good customers.”

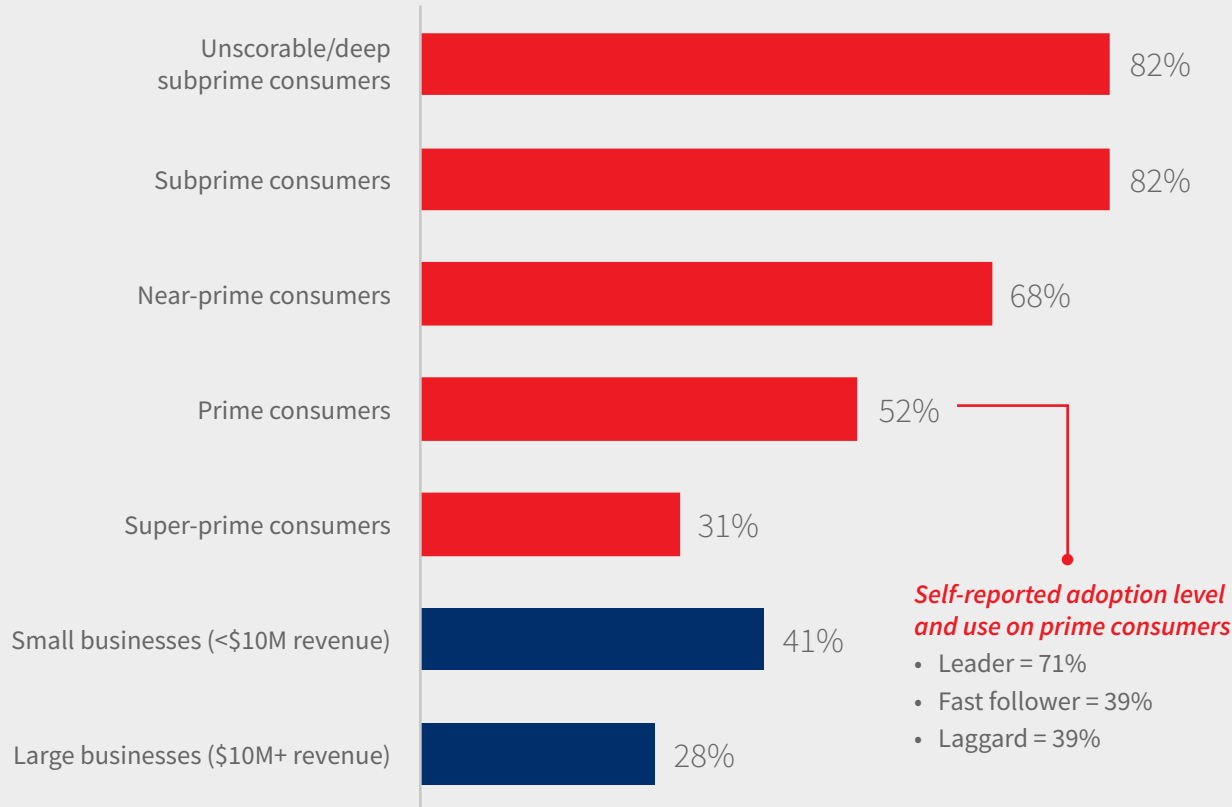
– Director, Tier 1 Bank



KEY FINDING 1: Driving Adoption of Alternative Data

Use of alternative credit data by customer credit segment

Overall (N = 168)



FIs are most likely to use alternative data in their credit risk assessment of deep subprime, subprime and near-prime consumers. Lenders who defined their organization as leaders in alternative data adoption, however, are also particularly likely (71%) to use it when assessing the credit risk of prime consumers.

Following the theme of this set of questions, the largest areas of adoption are in the assessment of unscorable, deep subprime and subprime consumers. These populations are the **most closely associated with financial inclusion**, the use case typically driving most lenders' initial adoption of third-party alternative data sources.

KEY FINDING 2

Alternative credit data drives meaningful business impacts

Improving pricing strategies and increasing financial inclusion are top business drivers for alternative data adoption

Risk managers are increasingly aware of the competitive advantages enabled by using alternative data to help improve consumer targeting.

These results speak to what is arguably the fastest growing application of alternative data — enriching evaluations to fine-tune offer strategies at account opening or during account life. While this is reflected in the “improved pricing strategies” response line, it’s worth noting that the

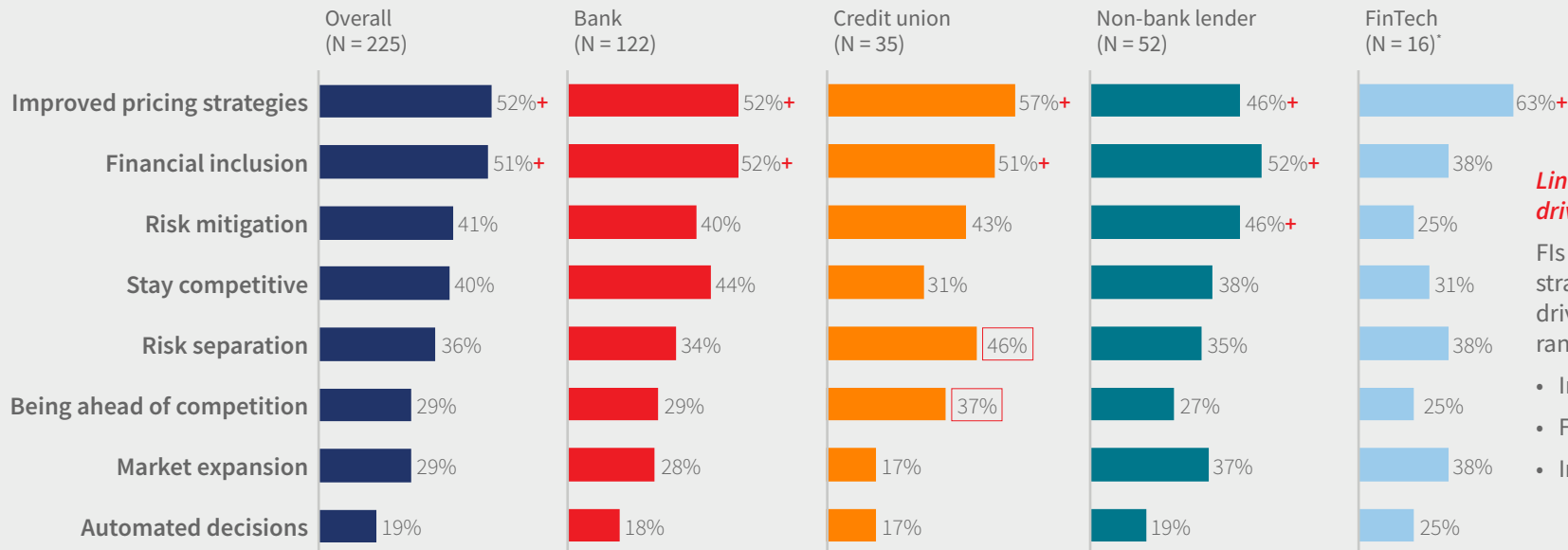
pressure to improve those strategies typically comes from the imperative to stay competitive in markets with increased consumer choice — reflected in the “stay competitive in the market” and “being ahead of the competition” responses.

Business drivers for adoption of alternative data (% ranked as top 3)

**Small sample size (directional comparisons only)*

+ = significantly or directionally higher than most or all other responses within segment

□ = significantly or directionally higher than same response in other segments



Linking alternative data adoption drivers to top business objectives

FIs that ranked “improved pricing strategies” as their top business driver were also likely to highly rank these objectives:

- Improved segmentation = 58%
- Financial inclusion = 51%
- Improve swap in/swap out = 45%

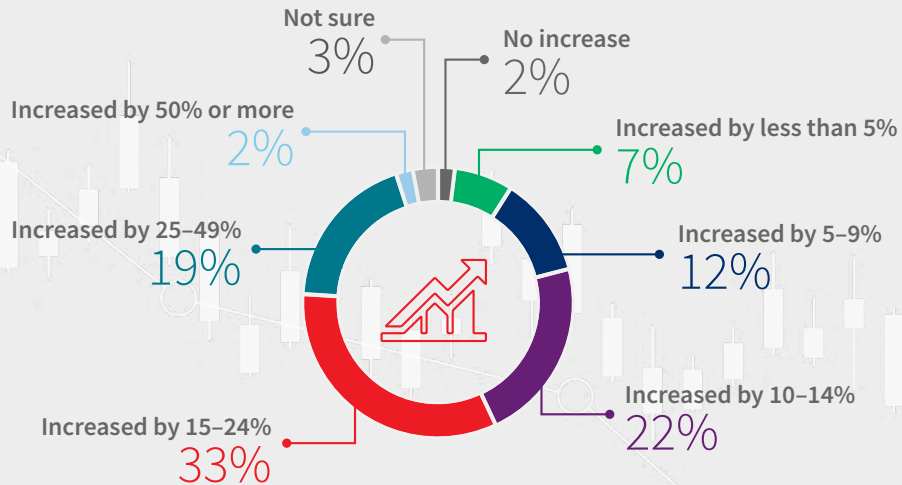
KEY FINDING 2: Business Impacts of Alternative Data

Alternative credit data increases revenue and improves customer experience

Use of alternative data has **positively impacted revenue growth for nearly all FIs surveyed**, with the majority saying revenue has increased by at least 15%. Firms focused on financial inclusion report even greater revenue increases, with over nearly one-third indicating a 25% or higher increase. Firms focused on consumer credit have also seen significant revenue growth, with 33% of respondents indicating a 25% or higher increase.

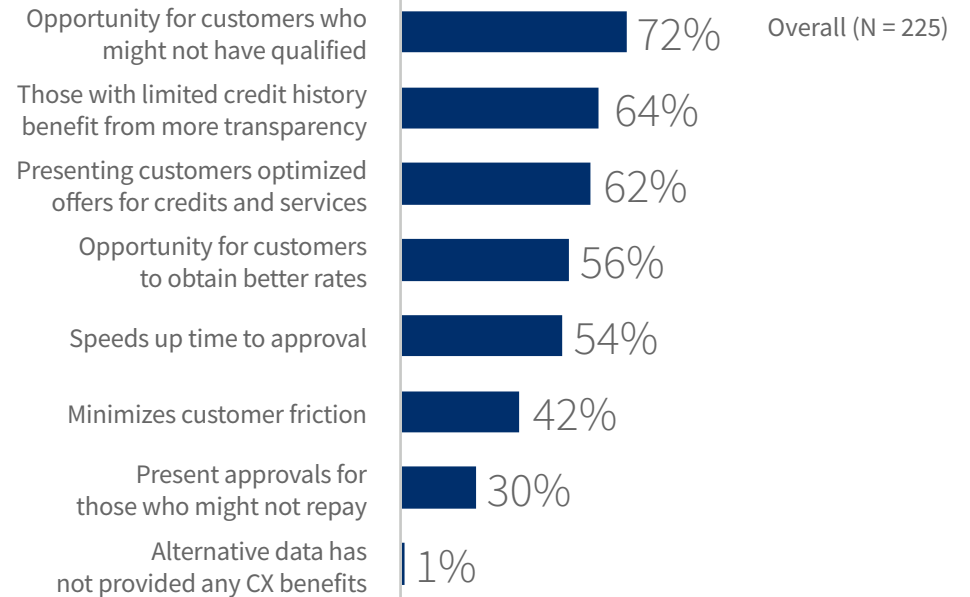
Impact of alternative data on revenue growth

Overall (N = 225)



Alternative credit data has also **helped improve customer experiences**. Previously unscorable consumers can qualify for more credit offers than before, and many consumers can obtain better rates and receive credit and services that are better targeted to their needs. Consumers with limited or no credit history also benefit from the increased transparency of knowing what goes into their credit risk assessment.

How alternative data use has benefited the customer experience



KEY FINDING 2: Business Impacts of Alternative Data

Ability to reach previously underserved markets is the top ranked advantage of using alternative data

Expanding reach to previously underserved markets is the top ranked advantage of using alternative data. Groups like young adults, new immigrants, the unemployed, students and foreign investors disproportionately contain consumers with thin or no credit files, challenging organizations' ability to evaluate the risk and opportunity of engaging with these segments. Alternative credit data can **help fill in the gaps and, in some instances, be the sole indicator of consumer or business risk.**

Overall, 44% of FIs surveyed use alternative credit data to help reach previously underserved markets. Of that 44%, 57% consider themselves adoption leaders. **Improved pricing strategies is a key driver in using alternative credit data** for marketers focused on consumer prescreen offers.

Advantages of using alternative data

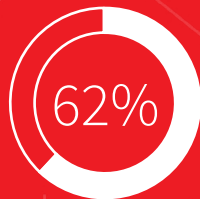
Overall (N = 225)

44% Reach previously underserved market

23% Better mitigate risk with a more holistic credit risk assessment

19% Balance speed of approval against customer friction

15% Deliver optimized offers for credit and services for customers



It's worth noting that the use of alternative data to optimize offers to prospective and existing customers — an innovative concept only a few years ago — is now part of the lending strategies for **62% of risk managers** in the survey.

KEY FINDING 2: Business Impacts of Alternative Data



Delaying adoption of alternative credit data can come with disadvantages

Lack of alternative data could increase approval times and customer friction leading to abandonment and lost opportunities for growth/market expansion. Traditional credit data is increasingly viewed as too narrow and limited on its own to support effective risk mitigation strategies. Credit unions and those making credit risk decisions for SMBs are particularly concerned about speed and abandonment.

Potential disadvantages of not using alternative data

Overall (N = 225)



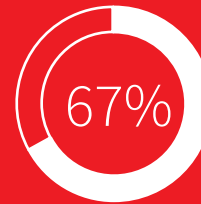
KEY FINDING 3

There is overall satisfaction with alternative data, though there are challenges and barriers to utilizing the data for credit and marketing

Across data types, challenges remain with leveraging data for credit risk

The narrow scope of available data can also limit expansion (a concern that is most pressing for banks and credit unions) and even impact the effectiveness of risk mitigation efforts. FinTechs are more likely to express concern over reduced approval speeds leading to customer abandonment. Because this survey looked across the customer lifecycle, it's important to note that **some of the frustration here stems from not being able to access very powerful data signals driving value in one stage of the consumer lifecycle in other areas.** For example — customer cash flow data would be available to a bank on nearly every existing customer during portfolio management but rarely available at underwriting when evaluating applicants with no previous history at the bank.

Alternative data can help widen that scope to deliver a more comprehensive view. However, **FIs still face challenges even with alternative data.** Data drawn from social media, travel history and relatives and associates are the most challenging alternative data signals for FIs to implement — in part due to the murky compliance situation facing these signals, depending on the consumer/commercial and lifecycle use case.



of FIs have reported insufficient data to target the right customers as one of the **top challenges they face**, along with inaccurate and outdated data.



KEY FINDING 3: Challenges of Using Alternative Data

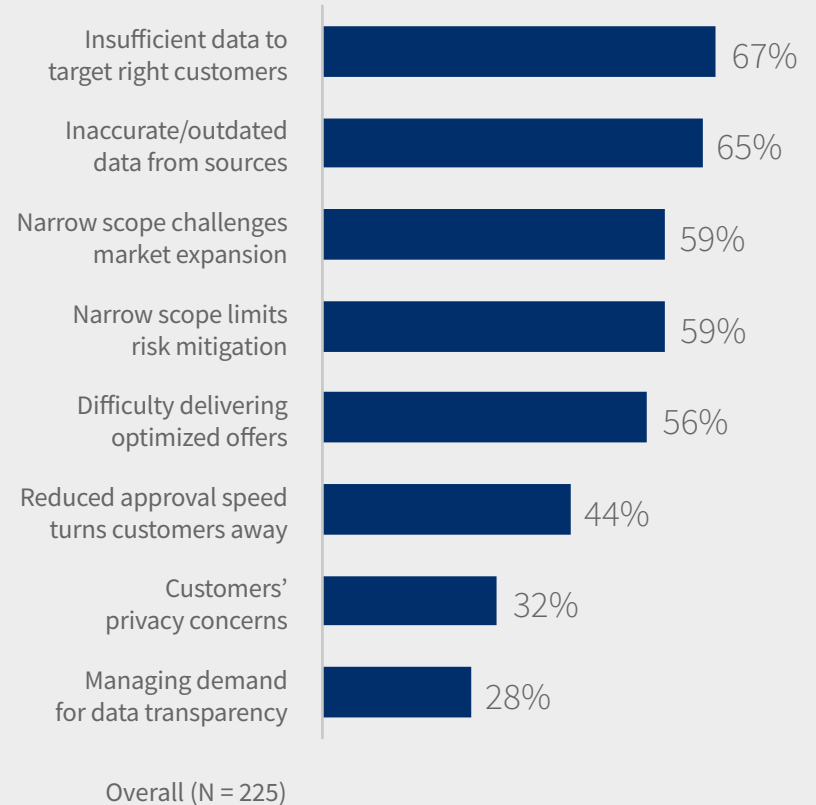
Challenges with data used in credit risk assessment

Many firms still lack access to near-real time updating of customer data. A majority of FIs use third-party sources to update customer data weekly, but **few are leveraging near-real time updating.**

None of the non-bank lenders in the survey used third-party sources for near-real time updating. A significant number elected to update monthly, if at all. **Banks are leaders in this aspect** as 23% reported using third-party sources to update in near-real time, with credit unions close behind at 17%. Organizations with loan portfolios exceeding \$1B are significantly more likely to use third-party sources to update customer data in near-real time.



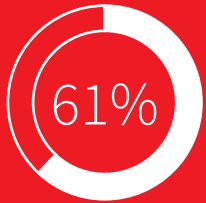
These responses also reflect the distinguishing traits of leading third-party providers — as real-time updates, sufficient/accurate coverage and privacy/data transparency concerns are all essential qualities among the top U.S. credit reporting agencies offering alternative data solutions.



KEY FINDING 3: Challenges of Using Alternative Data

Outdated data management systems and poor data quality across systems present barriers to using customer data in prescreen marketing and credit decisions

Respondents identified data management systems and data-sharing protocols as the primary barriers to utilizing data for credit decisions. Credit unions and those focusing on small business accounts are particularly likely to struggle with maintaining data quality across various systems.



61% of credit unions indicate that compliance and government regulations are a significant deterrent to customer data adoption.

Credit unions

61%



Non-bank lenders

62%

cite concerns over the cost of third-party sources as another considerable barrier



As using alternative credit data becomes standard practice in financial inclusion, lenders will likely seek to leverage it across other use cases

Taken as a whole, the key findings from this initial readout of the LexisNexis Risk Solutions 2022 alternative credit data impact survey capture the current state of increasingly critical set of solutions and signals. Adoption seems to have reached a point where use of alternative credit data in risk management strategies is moving from an innovative approach to an established best practice for financial inclusion. While commercial and consumer lenders agree on that front, consumer lenders seem to be leading the way in the next phase of alternative credit data use — leveraging these insights on near-prime and prime consumers to refine pricing strategies.

While some pain points still exist for adopting alternative credit data — particularly for smaller lenders — most of these issues have been well addressed by the leading providers in the space. Practices like on-demand compliance documentation and data availability across marketing, account opening and portfolio management use cases should become the standard expectation for any lender considering expanding their use of these solutions. Over 75% of respondents directly attribute a revenue increase of 10% of more to their use of alternative data — a figure which would be difficult to imagine only a few years prior.

With the high-level picture of alternative credit data use now in focus, we will continue our drill down into survey findings specific to consumer and commercial lending — looking at quantitative and qualitative insights on how risk managers in these categories are using alternative credit data. As the state of alternative credit data continues to evolve, these deeper dives should provide critical and current insight into the data types and strategies moving the needle in each market.

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