White Paper

Driving auto sales by verifying consumer employment and income data

March 13, 2020

Contents

This white paper discusses how real-time database supported verifications can help provide auto lenders with detailedinsight into borrower qualifications, while also supporting operational improvements. Recent research illustrates the value of real-time verifications by analyzing the impact of verifying a borrower's employment and income information when applying for an auto loan.

Introduction

Innovation and shifts in transportation ownership models are changing the landscape of the auto financing industry. Today, automotive dealers and lenders have access to useful tools to help identify well-qualified buyers through rich data and insightful analytics. The days when credit scores alone drive lending and business planning decisions are coming to an end. From real-time, individual income and employment verification to overlays of behavioral data, credit and risk business leaders have more information than ever to help make better lending decisions. These and other advances in technology can help lenders lower risk, remove stipulations, expedite decisions and, in some cases, provide borrowers with lower and tailored interest rates.

Subprime and near prime loans currently account for about

40%

of auto originations.*

The resiliency of subprime auto lending

While subprime auto lending has recently experienced new pressure from a rise in delinquencies, the industry as a whole remains relatively stable given historical trends. New insight from Equifax shows how advanced data are helping lenders navigate any possible headwinds. More than ever before, today's auto lenders are armed with consumer insights that give them an unprecedented understanding of how to evaluate the creditworthiness of borrowers. Subprime auto lending delivers a viable second chance for many consumers who may have made credit mistakes in the past, and have since rebuilt their financial and credit risk standing. Equifax research also shows that subprime is a well managed and stable subset of automotive lending — a subset that has been a key driver of our overall economic health.

*Equifax internal study of The Work Number, February 2020.

Today's car buying journey is sometimes fragmented, time-consuming, and burdensome. But waiting for hours at a dealership isn't what shoppers have in mind. In fact, 90% of car buyers expect an extremely efficient purchasing process.

Auto dealers are faced with new challenges due to increasing competition, more buyer options, and a flattening market. Shifting factors such as consumer demands in regards to speed of the process, and the overall perception of the experience, affect all stages of the car-buying journey. Accelerated car-buying journey expectations mean dealers need to get shoppers into their dealership and the right vehicle — fast.

Why? A strong appetite for on-demand services makes time incredibly important to today's average consumer and dealer personnel. Both groups tend to avoid hassle at all costs. More and more consumers opt for a car-buying experience similar to the one they have when shopping online or using same-day delivery services — frictionless, consistent, and user-friendly interactions with businesses when they want it. Knowing these habits, lenders should implement a similar fast-paced and transparent environment into the income and employment verification process.

90%

of car buyers expect an extremely efficient purchasing process.

Time matters: customer satisfaction begins to decline after 90 minutes

Despite the promise of digital retailing, frustrations remain and more work is needed to further enhance the car-buying process and experience. Consumers want more education upfront during their online research phase to help ensure they are looking at a vehicle within their budget. At the same time, they also want a quicker transaction experience at the dealership. They don't want to begin the research process all over again when they step into the showroom.

The 2019 Cox Automotive Car Buyer Journey[2] study illustrates this frustration. The report showed that 61% of car buyers said their latest car-buying experience was not any better — and in some cases, worse — than the last time they bought a car. The culprit? Time. Car buyers said when it comes to the dealership experience, they are most unhappy with the length of the buying process and manual paper procedures are a big part of the problem.

When it comes to the time associated with the buying process, customer satisfaction begins to decline after 90 minutes[3]. Dealers must make every second count: aligning the customer's needs with financing that meets their needs to minimize friction and maximize time. Critical to this is making sure that dealers are verifying information on each customer, particularly when it comes to income and employment.

61%

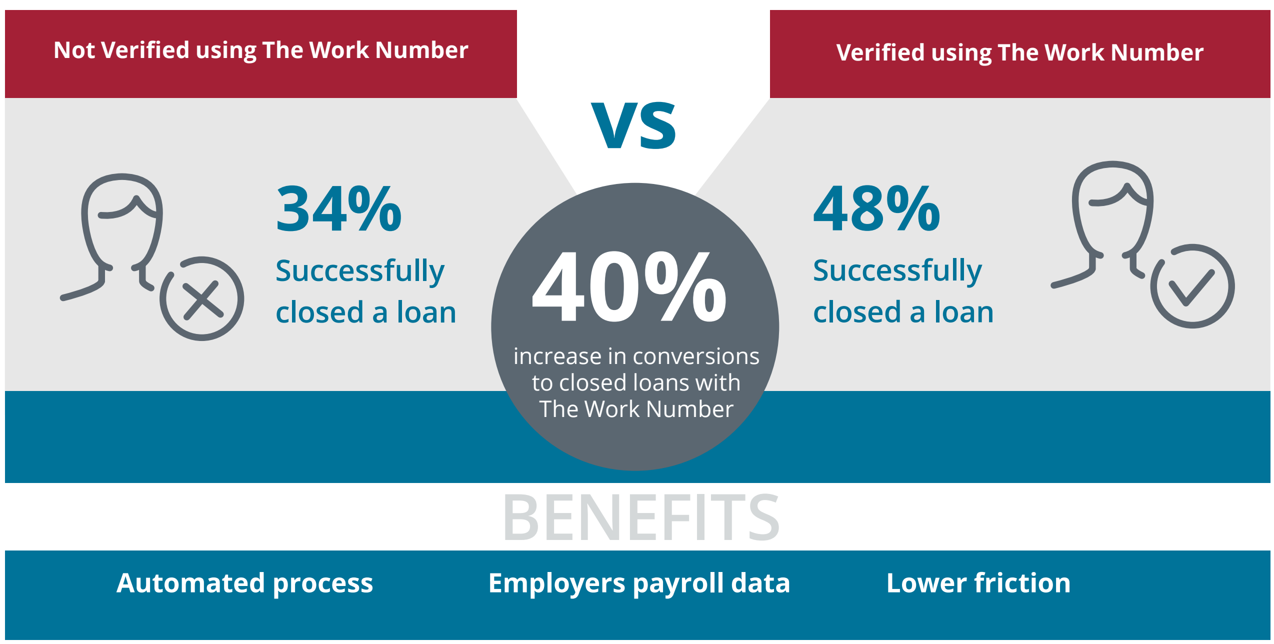
of car buyers said their latest car-buying experience was not any better — and in some cases, worse — than the last time they bought a car.

[2] 2019 Cox Automotive Car Buyer Journey Study. (2019, December 5). Retrieved March 3, 2020, from https://www.coxautoinc.com/learning-center/2019-car-buyer-journey-study/
[3] 2019 Cox Automotive Car Buyer Journey Study. (2019, December 5). Retrieved March 3, 2020, from https://www.coxautoinc.com/learning-center/2019-car-buyer-journey-study/

Verifying buyers' income and employment throughout your sales process can lead to more and faster sales. Real-time verifications can help dealers reduce wasted time and money, verify applicant-provided information, avoid contract buybacks, and clear lender stipulations.

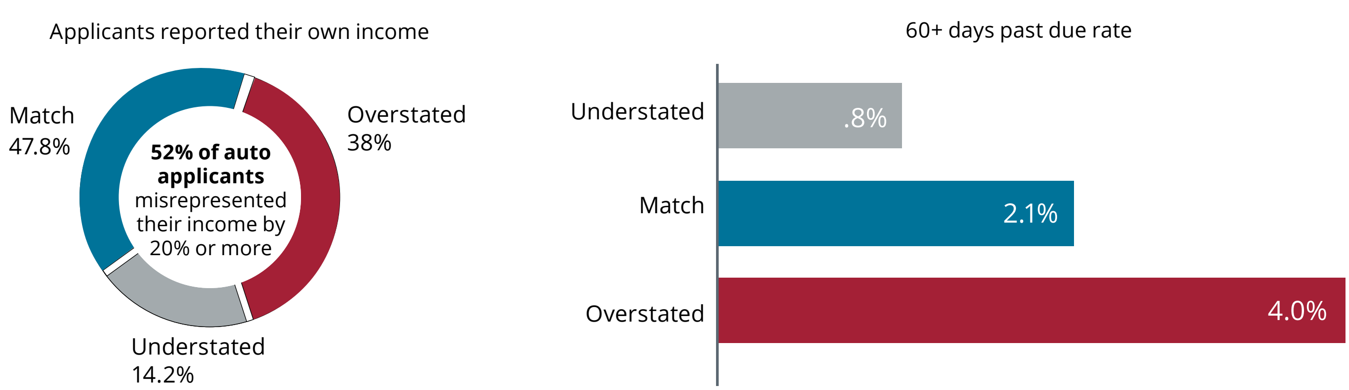
Leveraging instant income and employment verification from databases such as The Work Number® provides numerous benefits to lenders and borrowers, including accelerated closed deals. Information from The Work Number can help verify applicant representations or misrepresentations. Third-party verifications can also help lenders make decisions about extending credit to a consumer.

When applicants' income and employment are verified by The Work Number, auto applicants are 40% more likely to be funded.*



In one Equifax study, borrowers who overstated their income on an auto financing application by more than 20% had a serious delinquency rate (60 or more days past due) more than triple the rate of borrowers who did not inflate their income. Borrowers benefit as well: they are relieved of the burden of providing documentation and can complete the transaction faster. Ultimately, by providing more verified information into underwriting, lenders can confidently consider extending loans to those with less than perfect credit.

Overstated income predicts delinquency



*Equifax Internal Study of The Work Number Inquiry Data, December 2017. United States auto loans. Individual results may vary.
Understated income is when stated income is 20% less than The Work Number and overstated income is when ststed incoms is 20% more

Lenders should look beyond damaged credit

Many auto lenders still rely on traditional credit scores and applicant-reported details to determine creditworthiness or to predict the stability of loans. However, relying solely on credit scores may not give a comprehensive view of credit risk. Not all consumers behave as their credit scores might indicate, especially when economic conditions may cause setbacks that impair credit. Recent Equifax research revealed that a significant segment of the population has average to damaged credit (i.e., near-prime or subprime) combined with positive financial capacity measures, such as low debt to income ratios.[4] This combination attests to their ability to afford additional financial obligations — despite a low credit score.

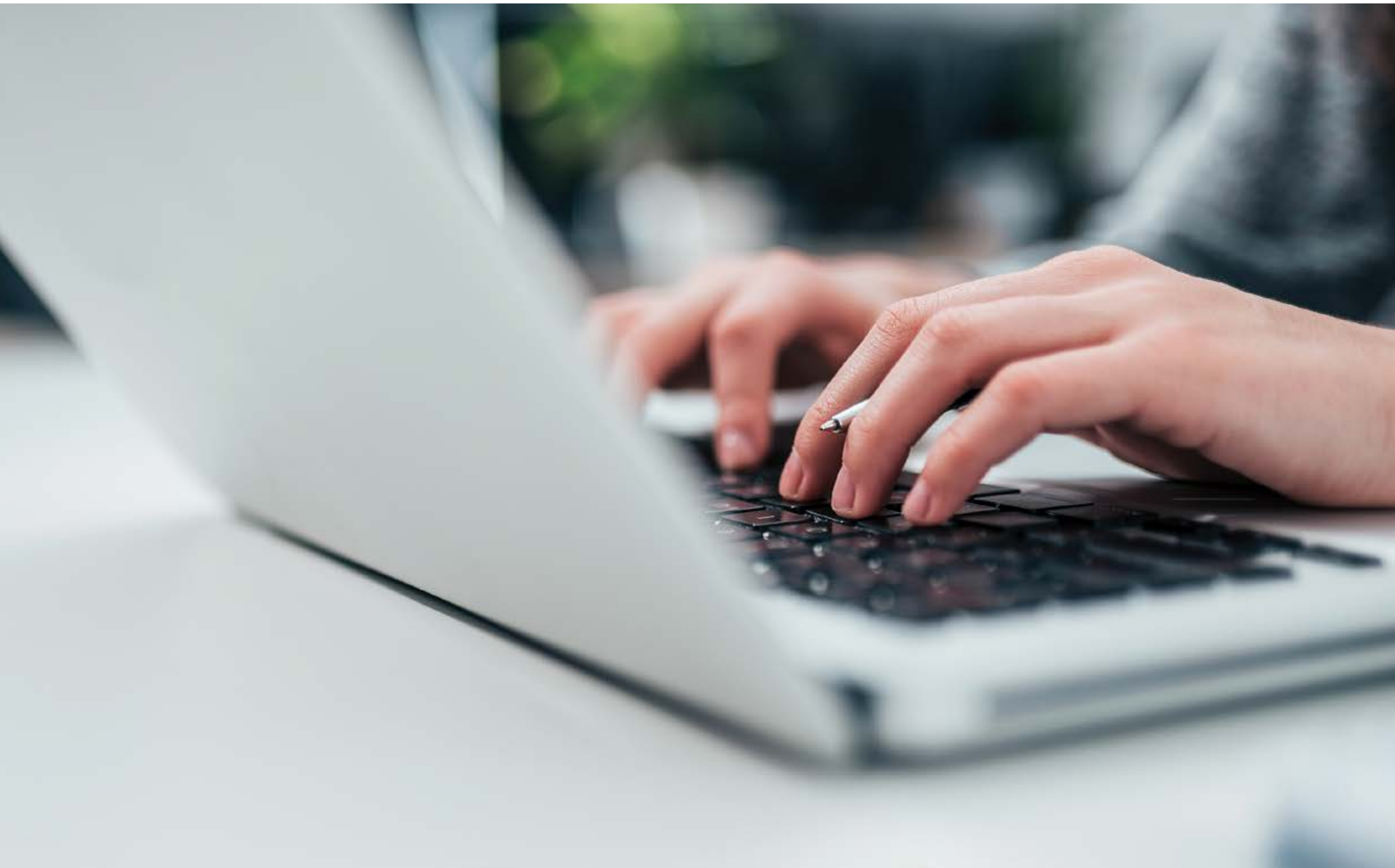
Credit scores shine light on only a fraction of the full view of risk or worthiness of a borrower, and may not be the most accurate or comprehensive way to assess borrower qualifications.

- Insufficient income and employment data can result in the wrong risk level being placed on deals, denying qualified applicants or inadvertently approving excessively high-risk borrowers.
- Applications may contain inflated or misrepresented information.
- Verifiable insights into historical job tenure and disruptions can be highly predictive of ability to pay.
- Because underwriters and lenders try to close deals quickly, manually verifying income and employment may not be the most efficient method for dealerships.

Alternative data sources, such as income and employment information, in addition to credit scores, provide timely insights into borrowers' qualifications. Verified income and employment information tell a more complete picture of the borrower, potentially identifying or mitigating risk.

Relying solely on credit scores may not give a comprehensive view of credit risk

[4] 10 years post the Great Recession, Equifax suggests communication providers review alternative data for emerging qualified customers. (n.d.). Retrieved March 6, 2020, from https://investor.equifax. com/news-and-events/news/2019/06-05-2019-121400730



Income and employment tenure: specific levels predict specific loan performance

Equifax compared real-time database-supported verifications to traditional internal verifications to demonstrate just how practical — and ultimately, profitable — database verifications are. The studies looked at the impact of four specific attributes on borrower credit-worthiness:

Income verification

Employment tenure

Pay frequency

Employment disruption

Each of these attributes helps create a more complete context in which to interpret credit ratings. They also enable lenders to develop a dynamic understanding of each applicant's circumstances. The studies compared a random ten-percent sampling from The Work Number database to traditional credit bureau reporting and verification processes.

Income verification

Equifax research revealed that the risk of delinquency is reduced approximately 50 basis points for every $10,000 salary increase for individuals earning $10,000-$80,000 annually. What is most important in this finding is not that better qualified applicants earn more, but that income verification (versus only relying on credit scores) can help identify prospects who are less likely to be delinquent on loans. Being able to quantify the likelihood of default so specifically enables lenders to develop more accurate strategies to improve portfolio performance.

Income verification is also important in determining appropriate rates, terms and deal structures. A significant portion of applicants qualify for more refined terms over the life of their loans. This improves customer satisfaction and increases the likelihood of nurturing a long-term customer.

And then there's the need for lenders to verify income through a trusted database like Equifax's The Work Number based on the reality of the auto industry. Fake pay stub creation tools and applicants who overstate and understate their income, further point to the importance of verifying information. Whether consumers intentionally or unintentionally overstate or understate their income should not be a concern for auto finance companies, as they are not forensic experts and shouldn't have to be.

Employment tenure

The length of time an applicant has held his or her job is highly predictive of loan delinquency. While it seems obvious that longer tenure indicates greater stability and more positive loan performance, internal Equifax studies found that:

- In the subprime population, borrowers with less than one year of tenure and loans of less than $15,000 are nearly twice as likely to become delinquent than those with ten+ years.
- Borrowers in the general population with less than one year of tenure are three times more likely to go 90+ DPD than borrowers with ten or more years.

Credit scores do not include job tenure data, but The Work Number can add such insight across all income levels. This level of analysis provides valuable tools for identifying increased risk and opportunities that might otherwise be missed.

Pay frequency

Hourly workers may be riskier regardless of income.
Even high paid hourly employees are less likely to stay current with loan payments than those who are salaried. Because The Work Number data is updated with each pay period for contributing employers and does not rely on information provided by borrowers, it offers the most timely and reliable information on pay frequency. This means deals can be structured to reflect the most realistic circumstances. In other words, terms can be tailored to the most probable estimates to ensure a borrower's likelihood of keeping payments up to date.

Job disruption

It is no surprise that loan applicants and current customers who have recently lost their jobs present greater risk than if they were still employed. The Work Number database presents a unique opportunity to notify customers of employment changes within their consumer portfolio.

Because The Work Number data is updated each time contributing employers process payroll, job disruption can be detected almost immediately. Relying on credit reporting alone only indicates the consequences of lost income well after employment has ended. Early detection can create opportunities for lenders and dealers to respond quickly, proactively, and productively:

- Work with borrowers before payments become delinquent.
- Avoid unnecessary expenses by finding the right alternatives to keep the customer in the vehicle.
- Work in partnership with customers to avoid default and improve the customer relationship instead of creating an adversarial environment.

Prime lenders can also find value from Income and Employment Verification

There is an obvious imbalance in the verification process that auto lenders can and should work to stabilize. Prime lenders do not verify income and employment data as often as subprime lenders. On the surface, it makes sense, and prime customers (those with 620 and higher credit scores) are often a safer bet with prime lenders making the argument that a prime borrower's credit score offers enough information. Hence, the risks of approving a loan for them is relatively low. But even prime lenders have battle scars from fraudulent or unaffordable loan activities. All it should take is one $30,000 mistake for a prime lender to realize that verifying income and employment is the right thing to do for their business, the industry and their customers. Instead of viewing verifications as a tool only for the subprime market, it should be considered standard practice for all lenders to tell a more complete picture of the borrower.

What makes The Work Number better?

The Work Number, regulated by the Fair Credit Reporting Act (FCRA), provides unique employment data directly from employers. It also helps lenders and dealers efficiently approve more profitable and comprehensively verified vehicle loans than ever before.

This is made possible through:

- Over 100 million active records that come directly from employers, and are updated each pay period
- Strong credibility with partners made possible through the timeliness of the database and automated verification
- Comprehensive data that includes generation Z employees, the demographic group directly following the millennials, who may not have established desirable credit histories but are an essential segment of future customer bases.

The Work Number's automation and transparency adds to the arsenal of tools necessary for dealers and lenders, and enables them to confidently close more deals. The database allows 24/7 access to employment and income verifications, allowing a salesperson to verify customers instantly, even after hours.

THE WORK NUMBER® from Equifax

About The Work Number

The Work Number database is the largest central source of consolidated employment and income information. The database houses more than 100 million active employment records. These records are contributed by more than half a million employers nationwide — from Fortune 500 companies to small regional and local employers representing every major industry. Accessible 24/7, The Work Number database enables a streamlined verification process for both automotive dealers and lenders alike.

Key Takeaways

Make better, faster loan decisions fueled by better data!

Equifax can help with it all — delighting your customers with an improved buying experience and unlocking automotive commerce along the way.

1

Relying on applicant-provided information is risky — either honest mistakes are made or intentional misrepresentation can occur.

2

Waiting for applicants to provide information and documentation can cause delays in the process and potentially negatively impact the customer experience and delay dealer funding.

3

Real-time income and employment verifications improve the entirety of the car-shopping process for the finance company, the customer, and the dealer. With the most current information accessed early on, lenders can offer tailored packages to consumers.

4

Today's auto consumers aren't just interested in a faster and more personalized buying experience — they're demanding it.

5

Leveraging information from The Work Number can help provide greater transparency and detailed insight into applicants' qualifications. This insight provides a competitive edge when evaluating applicant risk and opportunity.