UK Debt Collection Industry Report

Key Trends for 2021

4D CONTACT

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Introduction

At midnight on the 31st December 2020, many a glass was raised to the end of the year that brought Coronavirus to the world. However, the discovery of new, more transmissible strains of Covid-19 in both the UK, South Africa and Brazil in fact meant a very different start to 2021 than the one that was hoped with most countries in the world beginning the new year still with lockdown measures in place and with no clear vision of when life could return to normal.

Indeed, it was not until the 22nd February, following a further two months of social distancing, and the unprecedented success in the delivery of the nationwide vaccination program, that the UK government was finally able to announce a roadmap out of lockdown. The plan outlined was cautious, with a slow and steady relaxation of measures over several months with a return to normality not reached until 21st June - and even that date dependant on infection rates remaining stable.

For Europe, that has not managed to replicate the success of the UK vaccination program, the story is very different. As of March, many countries find themselves with rising infection rates and having to implement further lockdown measures – with no end in sight.

> Over 50% of European SME's have significant concerns over whether or not they will survive the next 12 months.

Uncertain economic landscape

For many British businesses this has meant a challenging financial outlook for 2021.
Already under pressure from the economic uncertainty of Brexit, many UK businesses have been battered by the financial implications of the Covid-19 lockdown.
With lockdown measures continuing well into 2021, the financial strain on the retail, hospitality, entertainment and travel industries will be further compounded.

With business rate holidays and the furlough scheme scheduled to end, and with repayments soon to be due on business interruption loans, it is without question that many businesses will have to make some tough decisions in order to survive.

Although the general consensus from economic experts is that the global economy should bounce towards the second half of the year, it may well be too late for many businesses. The McKinsey report "COVID-19 and European small and medium-size enterprises: How they are weathering the storm" published in October found that over 50% of European SME's have significant concerns over whether or not they will survive the next 12 months whilst a Begbies Traynor report suggests that half a million UK businesses at risk of collapse.

Challenging credit management and debt collection landscape

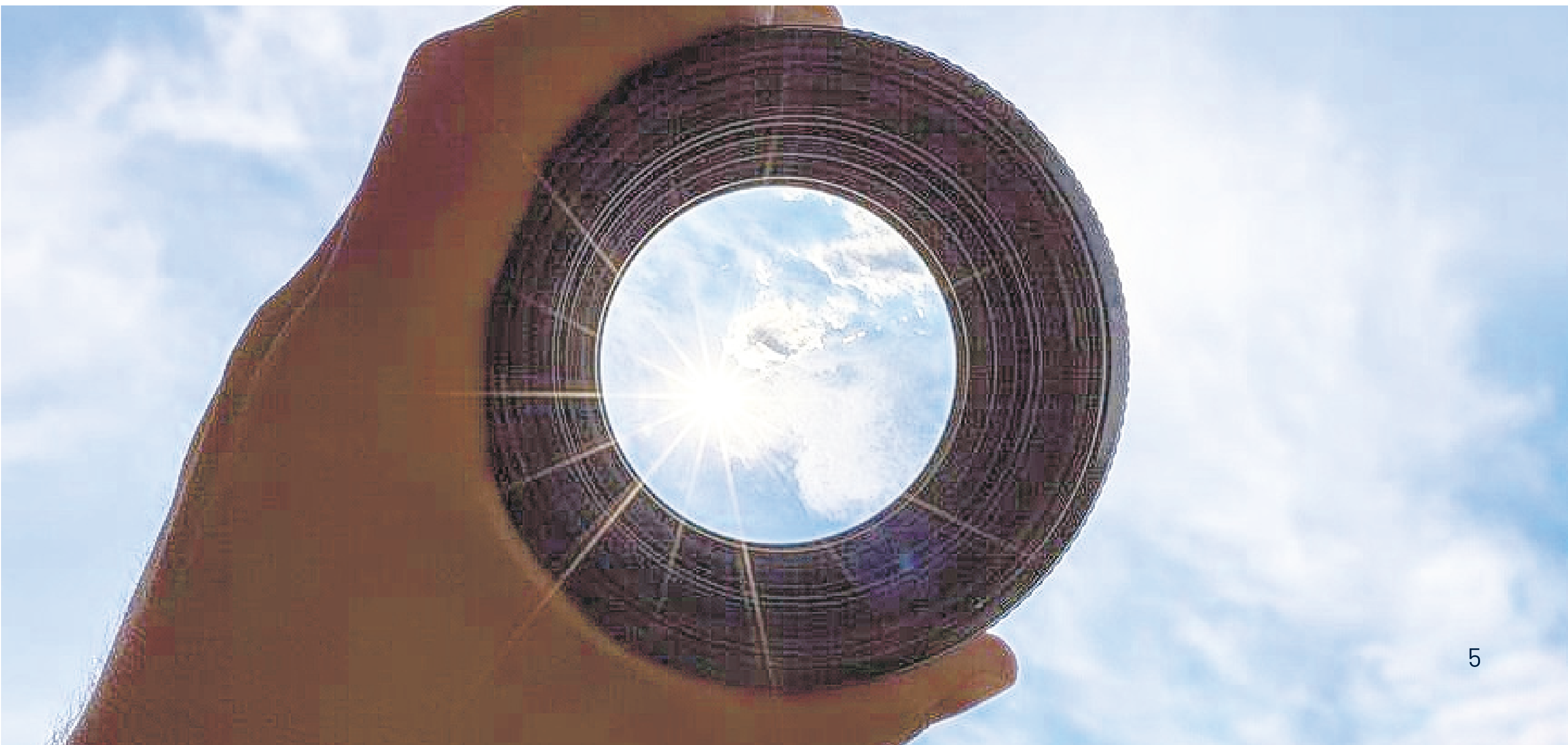
In this world of economic uncertainty one thing is certain – there is going to be an abundance of debt and a wealth of work for those in credit management and debt collection. Many companies and consumers who have never once defaulted on a payment are going to find themselves in a position when they literally cannot find the means to pay. Whilst for many businesses maintaining cash flow by optimizing collections will be critical to survival.

With individuals and businesses forced to make difficult decisions, prioritizing who to pay and when, collecting what is due is going to be increasingly difficult. It will be critical to ensure your business is either top of the payment queue or has the flexibility to work with customers, be they business or consumer, to develop longer-term payment strategies.

In this challenging debt collection environment, ensuring you have a robust credit-control process in place will mean that potential issues can be identified early and action taken to avoid defaults and minimize risk.

Indeed, the importance of a proactive and flexible approach to credit management is reinforced by the reported backlog in the British courts. The government ban on statuary demands and winding up petitions is currently due to end on the 31st March. However, current estimates suggest that even if you do choose to pursue your debtors through the courts, your case is unlikely to heard until 2022.

But what does this mean for the credit management and debt collection industry? Outlined below are some of the key credit and collections industry trends we believe will be seen in 2021.



1. Increased corporate focus on the cash collection cycle

It is reasonable to say that under normal circumstances companies primarily focus on growing the top line while managing the bottom line. Routine back-office functions such as accounts payables and cash collection are often taken for granted until there is a crisis. The Covid-19 pandemic presented just such a crisis - with widespread business interruption and a worldwide economic downturn - businesses were forced to start focusing on the balance sheet as well as the income statement in order to manage their working capital levels and remain liquid. This has meant a rise in the profile of credit management teams across the globe as optimising the efficiency and effectiveness of cash collection became a business priority.

In 2021, with the global economic outlook remaining uncertain, and companies now aware of the importance of strong liquidity to survive the unexpected, this increased focus on working capital looks set to remain on the corporate agenda. Without a doubt this will see increased focus and investment in credit and collections that could potentially drive seismic leaps forward in systems and process improvements.

2. Greater digital transformation

The credit and collections industry had already embraced the digital revolution prior to 2019. The data insight, analysis and automation enabled by modern software solutions delivered significant quantifiable improvements in efficiency and effectiveness versus the historic manual spreadsheet-based systems. However, high implementation costs and the challenges of competing for IT time versus other digital initiatives had meant that adoption had perhaps been slower than the gains warranted.

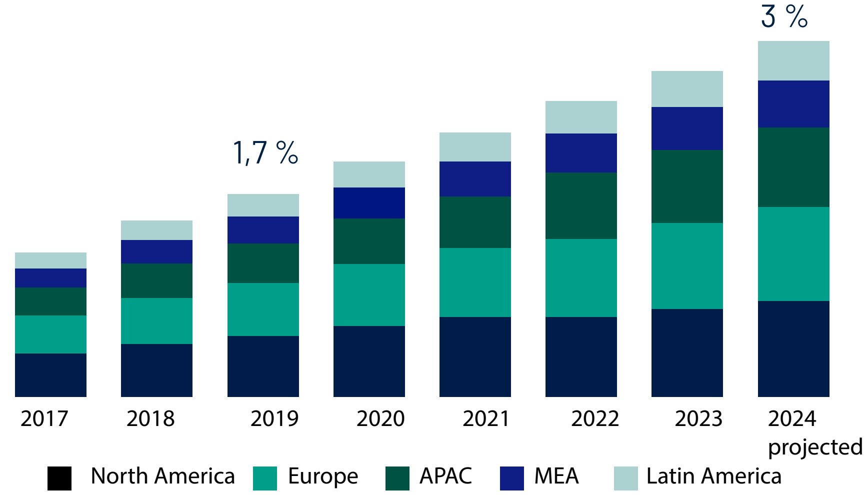
But there is nothing like a pandemic, with the need for everyone to access one system from home, combined with an economic downturn, and the need to maintain cashflow, to push an initiative up the corporate priority list.

"As the COVID-19 crisis forces your customers, employees, and supply chains into digital channels and new ways of working, now is the time to ask yourself: What are the bold digital actions we've hesitated to pursue in the past, even as we've known they would eventually be required? Strange as it may seem, right now, in a moment of crisis, is precisely the time to boldly advance your digital agenda." McKinsey Digital, Digital Strategy In A Time of Crisis

As per McKinsey's predictions, COVID-19 did indeed force businesses to make bold moves forward with their digital agenda and as we look ahead to 2021, one of the few positives from 2020 is the modernization of the credit and collections process.

The accounts receivable automation market size is expected to grow from USD 1.7 billion in 2019 to USD 3.0 billion by 2024.

Accounts receivable market , by region (USD Billion)



Accounts Receivable Automation Market Report – Markets & Markets

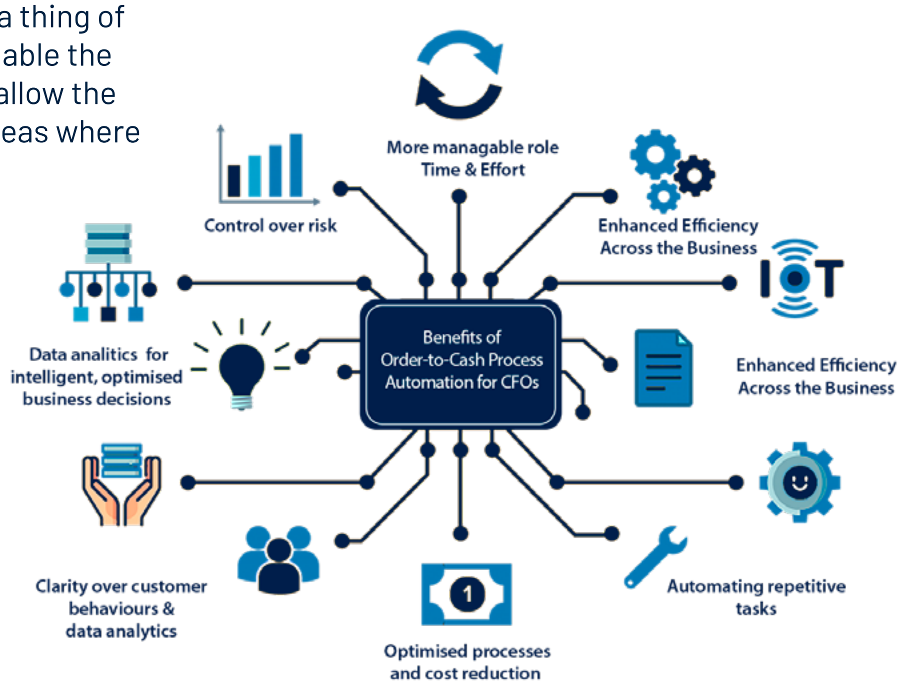
This marks a Compound Annual Growth Rate (CAGR) of 12.1% during the forecast period. A growth rate that must in part be attributed to the increase in focus on the improvement of cash flow and reduction in days sales outstanding driven by the pandemic.

Looking forward, digitalization of the credit and collections process will now become the norm for credit management and debt collection agencies and larger inhouse teams leading to greater understanding of the effectiveness of credit-control and debt collection activities and further improvements to credit-control and debt collection processes.

However, in 2021, the cost to implement credit and collections software solutions is likely to remain a barrier to smaller businesses – which are often those most in need of support to get their money through the door promptly.

3. Greater automation

Tied to the forecast growth in digital transformation is greater automation within the order-to-cash process. Manual Dunnings letters and emails, and time spent churning through excel spreadsheets will be a thing of the past as machine learning will enable the automation of repetitive tasks and allow the human workforce to focus on the areas where they can really add value.



4. Improved customer segmentation

One of the major developments we shall see from the growing digital transformation of the credit and collections process is the improved segmentation of customers. The ability of **modern collections software systems** to capture data on customer payment behaviours and patterns enables customers to be easily segmented based on their risk of default. **Targeted collections activity** can therefore be delivered where the data analytics suggest it will deliver the strongest results, whilst avoiding unnecessary contact with good payers.

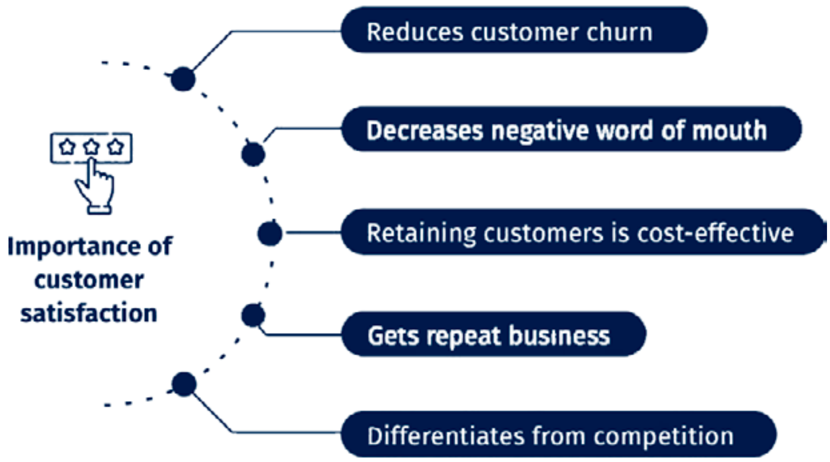
This ability to segment customers and deliver targeted collections activity **based on their propensity to pay** has the potential to drive massive improvements in the efficiency and effectiveness of a collections team.
The process automation enabled by digital transformation will potentially allow infinite personalisation of process, depending on and/or scenarios which will equate to a reformation from the one-size fits all historic process which many businesses still use to manage their collections process.

This ability to **utilize payment data to better** understand customers will be critical in 2021 as the challenging economic environment sees an increasing number of jobs at risk. Due to circumstances beyond their control, customers who have never defaulted on a payment in their life, may be in a position when they are simply unable to pay. The availability of different metrics to segment customers will ensure the swift identification of potentially vulnerable customers. This will allow strategies to be put in place promptly to avoid longer-term issues arising for either the customer or the business. Thus enabling data-informed decisions to be made about how to deliver the positive outcomes both for business and customer.

5. Rising importance of the customer

In 2021 delivering positive customer outcomes will become an increasingly important metric for credit and collections teams. This is a reflection of the overall global change in the customer relationship landscape – driven for most part by the meteoric growth of social media.

Social media has provided customers with a voice which they are prepared to use. This fast, impactful, un-editable public forum has meant businesses can no longer control the conversation regarding their products and services. This shift in power, combined with the increasing understanding across all industries that future market share will be as much won on customer experience as on product and price, has led to it becoming ever more critical that all customer interactions are positive – even for collections teams when dealing with customers who have defaulted on payments



6. Greater adoption of omnichannel collection strategies

With greater understanding of customers comes the ability to better understand the effectiveness of collections strategies and how they can be individually targeted to drive results. In 2021, it is without question that we shall see the credit and collections industry follow where the marketing industry has led and see the widespread adoption of omnichannel collections strategies.

In order to optimize collections, it is critical engage with your customers and an omnichannel approach enables you to contact the right customer through the right channel at the right time.

7. Increased volume of commercial debt

It is arguable that we are still to see the full economic impact of the pandemic, as it has been hidden by the government support measures such as loans, furlough, VAT and rent deferrals, and restrictions on statutory demands and winding up petitions.

However, as government support starts to unwind in 2021, it is widely predicted that there could be financial disaster about to unfold for many businesses. As well needing to start repayments on bounce back loans, SMEs could potentially have built up additional liabilities, such as delayed tax payments, deferred rent arrears and a build-up in trade debts – all of which will need to be dealt with in 2021.

The National Audit Office is estimating up to £26bn in expected defaults and fraud losses on the Bounce Back Loan and Business Interruption loan schemes. With banks currently split over the best recovery strategy and several finance experts forwarding the argument that it will be more costly to attempt to collect these bounce back loans than write them off, 2021 looks set to present a unpredictable commercial debt collection landscape in which the only two certainties are that many businesses are going to face significant financial challenges and that payment defaults will rise.

8. Increase in outsourcing

If there is one positive to come out of the COVID-19 pandemic, it is the change it has driven in working practices. Although in recent years there has been a steady shift towards more flexible working, misplaced concerns over whether remote workers would be as efficient and effective as inhouse teams, a lack of confidence in building and managing remote teams and worries over data security had slowed adoption. However, when the only way to maintain business continuity is to have a remote workforce, it is not surprising how quickly these perceived barriers could be addressed, and organisations embrace a new way of working.

This short-term global acceptance of a remote workforce is going to have long-term implications on the future organizational structure of businesses. As companies now have proof that people and processes do not have to be located in one place to be efficient and effective, the expense of having large, centralised offices will be difficult to justify going forward. Without doubt, a more deconstructed approach to workforces will be commonplace in future business.

It is highly likely that this shift towards remote working will also mark a trend towards increased outsourcing of non-core business functions. Outsourcing has historically faced similar barriers to adoption to remote working – fears over control, data security, and effective management processes – all which have been overcome with the necessity of moving to remote working during the pandemic. This has made the decision to outsource far less of a leap of faith and, as businesses start to consider what their business should look like post-COVID, it would be surprising if looking to increase outsourcing did not make it on to the corporate agenda.

"A remote work culture is being ingrained gradually within companies, and this will help them access global talent from the most cost-effective locations. It would also allow companies to hedge their risks by diversifying their delivery locations.

Also, with the global economy expected to contract, firms are "looking at ways to preserve cash." All these developments suggest that the needle will be tilting more towards outsourcing."

Deloitte Global Outsourcing Survey 2020

For debt collection, the growth in outsourcing will be also driven by the volume of debt forecast to arise from the Bounce Back Loan and Business Interruption loan schemes. With some effort certainly required to recover public funds, and the banks unlikely to be able to recruit enough people to service this debt internally, they will have to look to collection agencies for support. This all suggests significant expansion of the outsourced debt collection market in 2021

Conclusion

In conclusion, 2021 looks set to provide both challenges and opportunities for the debt collection industry. As government support initiatives draw to a close, there will be an inevitable tidal wave of delinquencies and defaults in both the consumer and commercial world. Whilst this will equate to a wealth of work for those in the business of cash collection, in a challenging economic environment it could be monies that are hard to collect.

Those businesses with deep pockets and the data analytics available to them to identify customers who have a good payment history but who are suddenly defaulting, might be wise to look to play the long game. No measure of threats will collect a debt where there are no funds available. However, if these customers can be identified, patience and fair treatment when they are struggling now, could turn them from a customer into a loyal advocate when they get back on their feet.

But post Covid-19, when the one lesson learnt as we enter 2021 is that cashflow is king, how willing will any business be to risk reducing their working capital?

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