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No more credit, is debt the new oil?

As Britain's personal debt at the end of December 2010 gains momentum and Europe's debt crisis sends seismic ripples throughout the EU, CEOs and business leaders across all sectors are faced with the question: How can growth be sustained in the current economic climate?

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Many companies are now turning to innovative ways to maximise the value of receivable assets and sustain profit. So is debt the new oil? The European receivables management market generated approximately €11.2bn in revenues and €2.2bn in profits in 2009, and is expected to continue its growth of around 10-15 percent per annum, going forward. Many business leaders today face tough decisions as they struggle to deliver profit expectations against a weakening Euro, high manufacturing and service cost and increased price competition within the market place.


So how can debt collection provide a solution to help European companies in the current harsh economic terrain? Are CEOs missing out on strategic advantages in not considering the use of recovery agents? The debt collection industry particularly in the UK is a maturing market, which is managing to shake-off the "tough guy" strong-arm tactics image, which plagued the industry in the late 1970s and 80s.

Today the industry boasts a well-oiled sophisticated machine, corporately packaged to deliver a range of flexible products consisting of:

- Credit information: ranging from identifying attractive potential customers to early warning of identification of credit risks;
- Propensity to pay scoring: which evaluates statistically the likelihood of payment being achieved;
- Invoicing services: corporately branded invoicing service to meet the clients' exact specification;
- Receivables management outsourcing: a fully branded professional target driven outsourced collections team, delivering cash direct into the clients account daily. This high growth sector often represents cost savings of 30 percent working deliver board approved day sales outstanding (DSO), targets;
- Third party debt collection: real-time debt collection by letter telephone, or visits. Remuneration is usually by commission, no success no fee;
- Pre-legal collections: detailed robust collections pre-legal action, testing the debtors' ability to pay, against court costs outlay;
- Surveillance and recovery: tracing absconders who disappear without paying. Credit file activity monitoring.

Despite the impressive suite of products





on offer by debt recovery agents, (DCA), debt purchase portfolio acquisition, has proved to be the protagonist on the debt management stage. Portfolio acquisition represents approximately 65 percent of the total €11.2bn staggering revenue pool in the industry, with a marked 77 percent of debt being derived from financial institutions. Interestingly there are no signs at present that this is likely to slow in growth. The UK and Germany remain the largest consumer lenders in the European market, followed by France and Spain. Market growth over the last years appears to be driven by two key elements: An increase in outsourcing and growth in debt sales.

Many commercial and consumer related businesses have gained strategic cost advantages through outsourcing. Variable costs are often lower than in-house expenses. Outsourcing often provides a benchmark against internal teams, resulting in the delivery of higher thresholds of performance from in-house teams. Staff often perceive the introduction of a “champion challenger” as motivation to “raise their game” which invariably leads to an increase in productivity establishing new thresholds in performance.

Outsource can also be used strategically, to manage high service dependency areas of the business, which require strict controls often with a multitude of measurable variables, such as call response times, fluidity in inbound and out bound calls, and more increasing 24/7 call centre manning. Many receivables management companies have advanced IT and telephony technologies and highly skilled staff, which are used to dealing with high volumes of calls, to tailored call scripts. The industry in the UK is heavily regulated by OFCOM. This has culminated in increasingly high standards. Depending on what is required, costs savings have been reported to be as high as 40 percent, by one company working in the utility sector.

Increasingly, many companies in the financial sector are turning to the advantages of debt sales. Debt sale was first recognised in the early 1980s although it may well have taken place as early as the late 1970s. It provides a clear strategic advantage for a company to manage its profit and loss, in a timely, controlled way. Naturally the asking price has to meet the market conditions (demand and supply). There is also an accounting arbitrage benefit to be gained from debt selling. Many leading sellers have gained advantage in price differences between two or more potential purchasers keen to acquire a “debt portfolio” as it is dubbed within the industry.

Another advantage which should not be ignored is International Financial Reporting Standards in particular (IAS39), which creates an incentive to sell debts due, at high discount rates, on non-performing debt books. Interestingly in 2009 the debt market across Europe was markedly quiet, with 2010 remaining almost the same, with some activity towards the end of the year. Interest from buyers remains strong with possibly only six or seven players within the European market with the level of funding to be involved in significant deals. 2011 promises to be an interesting year with many new entrant sellers seeking to gain advantage in their P & L.

So what are some of the barriers to entry that the debt recovery industry face in persuading companies to use their services? Some of these could possibly be:

- Brand protection – Many companies prefer to distance themselves from recovery agents because of the stigmatisation, which the function brings. However many DCAs already operate as an integral part of many well known brands in the forms of call centres, lettering services, sales ledger manage and collections. This branded solution achieved through training and client induction, gives the client full control enabling the DCA to become part of the company's ethos.

- Reputation – Clients often worry about their company's reputation and the reputation of the agents being used. How can this be overcome? The debt recovery industry, particularly in the UK is heavily regulated by the Office of Fair Trading, Information Commissioner and other legislative bodies. In fact some are now saying, the industry's regulation regime is almost akin to the banking sector. Reputable agencies avoid problems and adverse publicity. They set in place uncompromising compliance teams and audit processes. It is estimated that the industry could spend at least five percent of its operating budget in the area of compliance. In summary, if ever a period could be defined as “safe” to use debt recovery agents its now.

In 2011, it is predicted, the only CEOs who will remain standing in the coliseum of business, are the gladiators who are prepared to take risks in introducing innovative costs saving concepts, which add value and maximise profit. This article will hopefully challenge you to question whether you are prepared to embrace some of these concepts to add value to your business. ■

Experto Credite is a receivables management company with Offices in UK: Reading, Norway and Sweden.
