

Due Diligence in Collections and Recoveries Operations

By Paul Matthews

The capabilities, infrastructure and interconnections of a collections and recoveries operation are the fundamental foundations of performance. Good results depend on having strength across a number of key components, and these need to be aligned and working in concert with each other. From the people and operational structure, through the technological systems to the monitoring and governance, it is vital that all these components fit together well to deliver the business's aims. Whilst a good operational infrastructure alone does not guarantee success, a poor one will certainly ensure failure. And the collections and recoveries chain is only as strong as its weakest link.

More Focus, Less Stability

Rising arrears, uncertain economic conditions and limited origination activity are all causing organisations to switch their focus to their collections and recovery (C&R) functions. These back end processes, which sat far down the pecking order during the growth cycle, are coming under increasing scrutiny as businesses realise the value opportunity they represent.

Sadly, this increased focus comes at exactly the time when the collections environment is at its most uncertain. From mainstream lenders, through to debt purchasers and DCAs, there have been seismic shifts in the way collections and recoveries processes are performing. Shifting consumer circumstances, market changes and the economic downturn have all conspired to make collections much more difficult. Overlay regulatory and cultural changes and the picture that emerges is one of a vital business function needing to adapt and improve in an unfamiliar landscape.

The profile of customers flowing through to collections and recoveries has changed. The attitudes and options for people in debt are changing too. The systems and processes that are used to treat these customers may have become obsolete or sub-optimal. And at the same time, new technology, data and tools are available to slot into the process. Change is crucial, but so is maintaining the correct governance and compliance; the change must be correct, timely and well thought out.

The Role of Due Diligence

Against this backdrop many businesses are undertaking due diligence exercises on their collections and recoveries operations. While there is a realisation that change may be necessary, the most prudent approach is to understand what can be extracted from the current processes, where change is most needed, and what are the true value and implications of those changes. Failure to do this comprehensively can result in taking the wrong steps, spending money in the wrong areas, or introducing initiatives with unanticipated and unwanted effects elsewhere in the chain.

The purpose of due diligence here is to complete an end-to-end review of the current operation, giving a clear understanding of the strengths and weaknesses. By including the entire operational process, and unpicking the whole value generation chain, a true picture can be gained as to where the business is excelling and where it is most at risk.

A common pitfall for businesses when reviewing their C&R operation is to seize upon the known or anticipated weaknesses in the system and to curtail the scope of their due diligence based on pre-supposed findings. It can be difficult to step back from the day to day running of the function to evaluate it with a fresh and unbiased eye. The result of this can be cursory reviews focussing on the areas where problems are already known.

The scope of an operational due diligence should be wide but well-specified. At Euristix we conduct our due diligence of C&R operations across the five categories outlined below:



People and Structure

This covers the organisation of the function, and the capabilities and management of the people within it. From training and incentivisation through to capacity planning and contribution measurement, this area deals with getting the most value from the human element of the process.

Technology and Data

In the ever more sophisticated area of C&R, it is vital to use the right data and tools. The technological platform (dialler, queuing, diary etc.) needs to be bolstered with the most appropriate 3rd party and internal data used in the right way. From storing data and capturing costs to automating processes and providing collector scripts, technology is a potentially powerful ally in the collections world.

MI and Tracking

Champion-challenger performance, board reports, collector performance, system efficiency, compliance... reporting is a key aspect for any well run C&R operation. Ensuring the correct



KPIs are calculated, triggers are set for performance shifts, and feedback loops are in place is a vital aspect of efficient C&R management.

Collections Processes

The collections processes themselves are the building block of performance. Analytical tools such as segmentation, scoring, profiling and optimisation underpin trace and operational activities from settlement guidelines to contact strategies. All of these need to be fully fit for purpose and aligned to deliver the best results.

Policy and Strategy

The final component is having the correct governance, ownership and communication to drive through the policy and strategy changes required in an ever-changing C&R environment. This ensures the correct people having the remit and information they need to deliver well-defined collections goals within transparent cost and ethos guidelines.

While there are no fixed rules on the categories and considerations that form the scope of the due diligence review, and this will of course change from business to business, the key is to build a comprehensive picture of what is driving performance across the function.

Operating in the Real World

In an ideal world of limitless funds, an abundance of time and endless resources, we would all enjoy building the ultimate collections operation. Sadly, real life does not allow for such platonic ideals and we are all operating within time and budget constraints, with a remit to squeeze maximum performance from what is available. A due diligence exercise can only add value if it is aligned to these aims, and helps optimise the real world achievable performance of the C&R process.

It is in this area that a full operational review can either fail most spectacularly or really prove to be an invaluable exercise. At one end of the spectrum there is a tendency to compare the real world process to an unobtainable, 'perfect' system, giving little insight other than illustrating how difficult real world collections can be. At the other end however, the bigger picture provides a realistic grading of the various components of the process and allows the management team to prioritise actions where they will generate material value.

By focussing on the full C&R framework and benchmarking performance in each area against what has been actually achieved within other businesses, the resulting gap analysis provides opportunities for real improvement. Benchmarking against the real performance achieved by other participants in the industry is vital here. Resources and budgets can be focussed on those areas where the business is genuinely behind the curve rather than on chasing an ideal that is not being achieved anywhere in the industry. To do this of course requires a good view of



practices and performance across the sector and this is one area where organisations can benefit from an external view.

If it isn't Broken...

Interestingly, our experience has led us to believe that often those who gain the most benefit from a full C&R review are those whose processes are already relatively sophisticated. A business whose processes are very poor and totally unfit for purpose is usually already aware that their operation requires a full overhaul – here the key is to implement simple, efficient processes quickly and effectively. However, for the businesses where the C&R function is established and has received some investment there can be real benefit in reassessing the incumbent processes. It is here that optimising and aligning the components to the latest environment can bring the most value.

In many cases, substantial improvement can come in the form of 'quick wins' – simple, easily implemented tweaks to the existing processes that help to align the end-to-end operational goals and provide consistency of action and purpose. Simply having an external or independent view of the entire process, removed from politics or day to day running of the business, can identify inconsistencies, black holes or inefficiencies that are easily rectified with minimal capital expenditure.

Similarly, there is huge benefit in understanding what initiatives other, similar businesses have tried and which have added value. Often successful strategies and ideas can be incorporated into the C&R process within the existing framework – it is simply a case that they have not occurred to or been prioritised by the current business. This knowledge can also avoid the pursuit of initiatives that have proven to have limited value elsewhere, despite appearing promising on paper. Again, this is where a due diligence review needs to be grounded in real-world, achievable practices rather than being an overly-idealistic, academic exercise.

Of course there is always a chance that the review could highlight some aspects of the C&R process as being significantly behind other players in the sector, value-destroying, or even a potential business risk. In this case the review should provide not only the detail of the problem, but also a sensible mitigation plan and guidance on the cost-benefit impact associated with rectifying the problem. This will allow the management team to prioritise their actions and focus their efforts on ensuring good capability across the C&R chain.

Stepping Back and Striding Forward

Collections and recoveries operations are under huge pressure, whether it be within a wider lending operation or as specialist debt collection and debt purchase departments. In these conditions it can be incredibly difficult to make the time to step back and review the full, end-to-



end process. The individuals within the organisation often have remits for particular aspects of the function, simultaneously chasing monthly targets, fighting fires and running the shop. All of which makes it very difficult for them to step back and take a wider, objective view.

But the potential benefits of this type of endeavour are huge. By delivering real insight into the capability of the end-to-end process, benchmarking against the market, and identifying any activities not aligned to the overall goals, the management is empowered to make valuable, targeted change. From implementing quick wins through to driving longer term, strategic improvements the information gathered in this way provides a vital roadmap to squeeze optimum value from the existing platform and maximise the benefit of any investment. In today's environment, with the huge focus and demands on collections and recoveries activities, it cannot be overstated how important this may prove to be.

If you would like to discuss any of the points above, or if you would like any further information on the research carried out by Euristix, then please contact Paul Matthews at paul.matthews@euristix.com