Past, present, future

How debt collections in APAC have changed and where they're going next

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Prologue - The foundations for change

Throughout financial history, change has often been documented either as a rapid, disruptive thing or something more insidious and subtle that takes its time to truly settle. For evidence of the former, we only need to look to the disruption of the humble debit card, which was first introduced to the UK in 1987 and transformed the market almost overnight. For the latter, meanwhile, we can look to the rise in mobile banking and fintech that has been slowly moving the ground beneath our feet for the best part of a decade.

Banks in the APAC region find themselves caught somewhere in the middle - with tremendous and nimble economic growth but crippling cultural holdups and an ageing infrastructure unable to support the necessary changes that will accelerate that growth.

Rapid economic growth brings with it several challenges, of course, and APAC banks have experienced many of those challenges in recent years, but most of those challenges have been overcome (or are currently being overcome) through greater utilisation of technology. Nowhere is this more relevant than in the debt collections sector, which has earned its negative reputation in the region thanks to a history of notorious complexity.

This complexity is due to everything from local issues with payment practices, court and insolvency proceedings to cultural and ideological opinions about debt, not to mention local regulations and a significant amount of corruption, often at a very high level.

However, there is a way forward for APAC banks and debt collections. It involves not only looking to neighbouring countries for historical guidance but examining the past fears holding them back. It also means understanding the unique challenges they face today and appreciating the importance of industry-wide digital transformation for the future.

Chapter 01

Japan's millennial debt

> "It might be one of the world's most advanced economies, but, as of 2018, Japan had the highest-rated public debt to GDP ratio at a staggering 253%"

Perhaps even more shockingly, Japan's national debt currently sits at over one quadrillion yen. According to the International Monetary Fund, for Japan to pay down this debt to 80% of GDP by 2030, it would need to reach 5.6% of GDP surplus by next year (2020) and sustain that surplus for a decade. Which is unlikely, to say the least.

Still, whilst one might reasonably assume that such a monumental debt should result in catastrophe, unlike Greece, Japan is a country that is still going strong. There have been over two decades of severe warnings, but the debt crisis that was forecast never arrived, despite the country's debt passing 250% of GDP earlier this year.

Whilst it seems to be perpetually living on the edge, after two decades of strife, Japan now boasts both low unemployment (around 2.5%) and low household debt. Indeed, Japan is continuing to survive and thrive in spite of its public debt problems, but it remains a fascinating case study. So, how did Japan's debt get this way? What has the government been doing to help? And, more pertinently, what could APAC banks learn from those actions?

In the 1990s, the Japanese economy had reached a point of stagnation, which was caused in no small part by a build-up of bad loans that had a cumulatively negative effect on banks in the country. To reset the balance, the government proposed some radical policy changes.

The ambitious Programme for Financial Revival (PFR) was first announced in

October of 2002 as a means of reducing the huge amount of NPLs that had managed to accumulate after the collapse of the economic bubble. Whilst the primary goal of the programme was to solve the loan problem, it also strived to build a stronger and more stable economy by creating new frameworks for the financial system, corporate revitalisation and financial administration.

As a result of the programme, inadequate assessment of assets and disclosure of information were tightened, bank management transparency was improved, NPL disposal was accelerated and the financial institutions' supervisory and regulatory regime was significantly enhanced.

Despite its delayed introduction, it could be argued that the PFR has been successful in stabilising the financial system and reducing NPLs, with the Financial Service Agency (which was created in 2000) reaching its target of halving the amount of bad debt by 2005; just three years after the programme's introduction. Some have suggested, however, that it was a case of "too little too late."

The big banks

The PFR led to a dramatic reduction in bad loans and, as a result, in just two years, many of the leading Japanese banks merged or dissolved, to the extent that the 20 leading banks had become just 4 by 2004. Whilst these larger banks were able to cope (by merging and restructuring), the local banks didn't have the resources to do this and still struggle to compete to this day.

The big banks, however, had been keeping their earnings afloat with high-interest cash advances (or card loans) and those loans started to take a toll a few years ago as the irrecoverable debt started to pile up, with bad debt tied to those advances climbing 13% to 140 billion yen between 2016 and 2017.

These advances were issued at annual interest rates of between 2% and 14% with the money often able to be withdrawn directly - no questions asked. Lenders paid fees to guarantee that companies would repay the loan if the borrower couldn't. Cases of people borrowing more than they can afford in cash advances were growing across Japan throughout 2016 and those cash advances were criticised for leading to the excessive lending that had allowed borrowers to rack up debt from multiple borrowers.

However, the Japanese Bankers Association called for tighter screening in March 2017, and many banks have set voluntary financing limits in accordance

with borrowers' annual incomes. This has prevented outstanding lending from growing for the last two years, but bad debt is still piling up from past loans, with the Japanese NPL ratio still standing at 1.1 % as of September 2018.

Hard-learned lessons

Japan is a prime example of what happens when you allow NPLs to mount. If a greater effort had been made back in the 90s to take action on these bad loans, the problem could have been solved and the majority of the damage circumvented.

Greater transparency is also something that other economies should be taking away from the Japanese debt situation. Indeed, Japan themselves have even advocated lenders and borrowers in emerging economies to disclose more debt in order to keep these nations from falling into the same debt trap they currently find themselves in. Because, whilst they might be strong enough to live with this debt, many emerging APAC economies won't be.

As the host of the G-20 meeting for finance ministers and central bankers in 2019, Japan is urging lenders and borrowers in emerging countries [illegible] more information on the size, interest rates and conditions of their debts. It is also advocating responsible lending practices - like ensuring that borrowers have the ability to repay the loans in question.

This proves that Japan has, at least on paper, learned from its own mistakes over the past 20 years. But can APAC governments and retail banks do likewise?

Chapter 02

Fear of bankruptcy

> "...From a cultural perspective, admitting any flaws, weaknesses or imperfections goes against the region's social norms and bankruptcy just might be perceived as the ultimate failure by many."

In many Asian countries, bankruptcy is still seen as one of the great taboos. In APAC, particularly, the idea of owning up to one's debts is severely frowned upon. From a cultural perspective, admitting any flaws, weaknesses or imperfections goes against the region's social norms and bankruptcy just might be perceived as the ultimate failure by many.

This is why there is such a grey cloud around bankruptcy in Asian culture and Asian banks. But what are the implications of this fear? And how could APAC banks be improving their debt collections practices in response to it?

Nobody ever makes a plan to file for bankruptcy, but it can be an unfortunate inevitability. Whilst we have learned to accept the realities of bankruptcy (or insolvency) in the West, there is an inescapable cultural shame that still circles debt throughout Southeast Asia. It's perfectly natural to fear failure and declaring bankruptcy is often seen as a last resort when all other avenues have been explored, and in many APAC countries, there is a pervasive culture of shame surrounding debt, let alone bankruptcy.

Education (or lack thereof) is also partly to blame here and has led to a banking culture that lags quite far behind most Western peers. In Cambodia, for example, according to the World Bank, the percentage of Cambodians aged 15 and over with a bank account stood at just 22%. In a climate where more Cambodians have loans than have bank accounts, debt collectors are bound to struggle, as they are tasked with collecting money from debtors who are essentially 'off the grid'.

Improving financial literacy in both households and businesses should be critical - especially small businesses and those based in rural areas. A decent amount of financial knowledge will not only help debtors to understand their rights and responsibilities, but also to protect themselves from financial fraud or over-indebtedness.

Understanding the fear

Bankruptcy can be a powerful card for debtors to play as long as they don't own many high-value assets and want to avoid paying off a substantial debt. By a similar margin, however, it can also prove devastating for creditors, with courts generally placing an automatic stay on debt collections efforts until the case has been decided. For banks, dealing with bankruptcy means wasting more resources, more time and often not getting paid - or at least getting paid less than they are owed.

The fear of bankruptcy that's so rife in APAC could be perceived as a positive for creditors, as fear is always a powerful motivator for avoidance. However, whilst the fear might be palpable, there are still rising numbers of individuals and companies falling into it, even in the more developed countries like Singapore, where there were 3097 fresh bankruptcy orders made in 2018 (up from 2587 in 2014).

The introduction of the Insolvency Order in Singapore could be seen as a sign of shifting perceptions towards insolvency in the country. The order places greater emphasis on reviewing and rehabilitating companies that are facing shortfall and difficulties, allowing a company to restructure their debts or restructure management as an alternative to liquidation. Whilst this order doesn't help private debtors, it does go some way towards taking the stigma and the shame away from bankruptcy and proving that it is possible to bounce back.

Accepting the fear

The frugality of the Asian market is a false belief that pervades the global economy. This is largely down to the culture (the self-discipline of Confucianism) and a history of privation amongst developing countries. It's this culture and this history that might also have led to such grave fears surrounding debt. However, relative to income levels, consumer borrowing has risen steadily in

Thailand, Malaysia, Hong Kong and Singapore.

In Thailand, the household debt figure of $372 billion represents 77.6% of GDP. In Malaysia, meanwhile, official estimates placed household debt at 88.4% of GDP in 2016. To release the debt pressure, the Bank of Thailand has already stiffened the rules on credit cards and unsecured loans by reducing credit limits as asset quality pressures mount. To help lighten the load in Malaysia back in 2016, the central bank tightened lending standards and formulated a new consumer credit law to enhance borrower protection and establish fairer and more responsible lending, relief, disclosures and recoveries.

If we can understand the local and regional attitudes towards debt then we will be better equipped to design more effective debt collections responses around them. Of course, the region is vast and eclectic, with various disparate economies and individual cultures to navigate. However, by relying more heavily on customer-centric practices and digital transformation, banks might be able to demystify debt collections a little and cast away some of the shame surrounding it.

What it all means

If banks in the region want to combat the fear of bankruptcy in APAC, they need to start by educating locals and reevaluating their own local debt collections practices. Education can be as simple as making sure customers are aware of the implications and consequences of personal insolvency.

They also need to start approaching bankruptcy not from a moral perspective, but as a purely financial solution. It's all about changing the narrative surrounding debt and bankruptcy and mitigating the fallout both socially and financially.

For collectors, this means not only investing in self-service options but also in AI chatbots, which allow debtors to deal with their accounts without having to speak to another human being. Granted, the infrastructure might not be available in all countries to support all avenues, but there are certainly options to consider.

Chapter 03

Debt collections **challenges**

> " The APAC region is a diverse and culturally rich collection of nations, but it also holds enormous economic potential...."

The APAC region is a diverse and culturally rich collection of nations, but it also holds enormous economic potential as one of the most rapidly developing regions in the world, with projected economic growth rates averaging 5.1% for member states of the Association of Southeast Asian Nations (ASEAN).

For banks operating in these countries (whether they're multinational institutions entering the territory or existing local banks) there remain notable challenges, particularly when it comes to collections operations and debt recovery.

Local regulations

The debt landscape in APAC is incredibly dense and complicated. These nations have many laws and customs that are incompatible with typical western practices, not to mention some incredibly idiosyncratic court systems. This is particularly problematic when it comes to debt collections. Indeed, in a report by Euler Hermes assessing local payment practices, court proceedings and insolvency, the region was found to have amongst the largest number of countries classified as 'severely' complex. However, shifts in policy and initiatives such as the Debt Collection Act and the Debt Clinic set up by the Bank of Thailand are helping to regulate the way creditors collect debt by banning unscrupulous collections tactics and giving individual debtors increased protection and rights.

Lack of technology

While there has been an increase in adoption overall with some countries in the region amongst the hottest spots for fintech growth, there are still some nations lagging on the tech front. Indonesia, for example, poses the issue of cultural acceptance, with online payments still viewed with distrust by many locals. However, this slow adoption means that Indonesia (which currently boasts a young population of over 261 million) is poised as a "large and untapped" market. For banks hoping to invest in digital transformation in the region, the

real challenge is in education and utilising user-friendly software solutions.

Corruption

Corruption remains a major problem for APAC banks to navigate. It's not just emerging economies with this problem either, with over 40% of firms in the region expected to give 'gifts' to secure government contracts. On a local level, meanwhile, Malaysia's 1MDB scandal has shaken the financial world, with a parliamentary committee identifying at least $4.2 billion in irregular transactions related to the company. Cambodia, meanwhile, scored 20 on the Transparency International Corruption Perceptions Index (CPI) and in Laos, the government has lost up to $30 million to corruption. With such shaky foundations underpinning a country's governmental, economic and financial institutions, it makes the collections of delinquent loans that much more difficult. This means that a solid pre-collections strategy is critical and that debtors should be prevented from defaulting on their loans at all costs.

Lack of strategy

Collections strategies in the region still fall well behind their Western counterparts, with banks lending irresponsibly and not taking a long-term view on debt. In Cambodia, for example, only 4% of the population have formal savings, but 28% have taken out formal loans from a financial institution. Those figures simply don't add up. In such an environment, banks need to start being more selective with their loans and using the data available to them to approve or decline loan applications. They also need to understand that collections don't start at default; it's a whole lifecycle. More investment needs to be made not only in pre-collections but in preventing accounts from falling into delinquency.

Infrastructure

A modern debt collections infrastructure means investing in digital transformation, and many countries in the region might not be equipped to cope with the demands such a transformation entails. There are, however, encouraging steps being made, with many businesses relocating their data centres to the region and data centres are increasingly becoming core components of banking operations. From an economic perspective, APAC cities are booming, with Vietnam, Thailand and Cambodia all revealing a potential for significant long-term growth. However, with economies growing rapidly, people are rushing into the cities and many of these cities are unprepared to cope with this massive influx. With rapid, unplanned urbanisation come other challenges too, as rents increase and the cost of living goes up. In this climate, bank customers might struggle to meet their debts and will need the help of their banks to stay ahead.

Tracking debtors

Many APAC countries still rely on physical forms of ID. This reliance is problematic for collections teams, as paperless technology is not only more convenient for both the debtors and the banks, but saves costs and is more environmentally friendly. Without the benefits of digital transformation, tracking debtors down is that much harder and user experience suffers. There are also many APAC countries where it's common for citizens to have no official form of identification. However, there is progress being made. Back in 2001, Malaysia became the first country in the world to use an ID card that incorporates both photo identification and fingerprint biometric data. ID cards have also been standard in Indonesia since 2011 and in Thailand since 2018 thanks to the passing of the Digital ID Bill.

Data

Internet and smartphone penetration in the region is on the rise, with APAC topping the charts in a 2019 report by WeAreSocial when it came to the growth of unique internet, mobile and social media users. With increasing digital penetration and cheaper mobile data, it's also the leading region when it comes to mobile data traffic growth, with data use growing by 29% in 2018. The data centre construction market is looking set to reach $2 billion by 2024, so now would certainly be the right time for banks to invest. However, whilst there is more data than ever before in the region, that amount of data is not without its challenges, particularly in a region that might not be best equipped to handle it. Data centres are slow to build and costly to run. They are also vulnerable to cyber attacks, system failures and power outages. As such, banks looking to invest in the area must prepare their debt collections practices accordingly and invest in stable digital infrastructure.

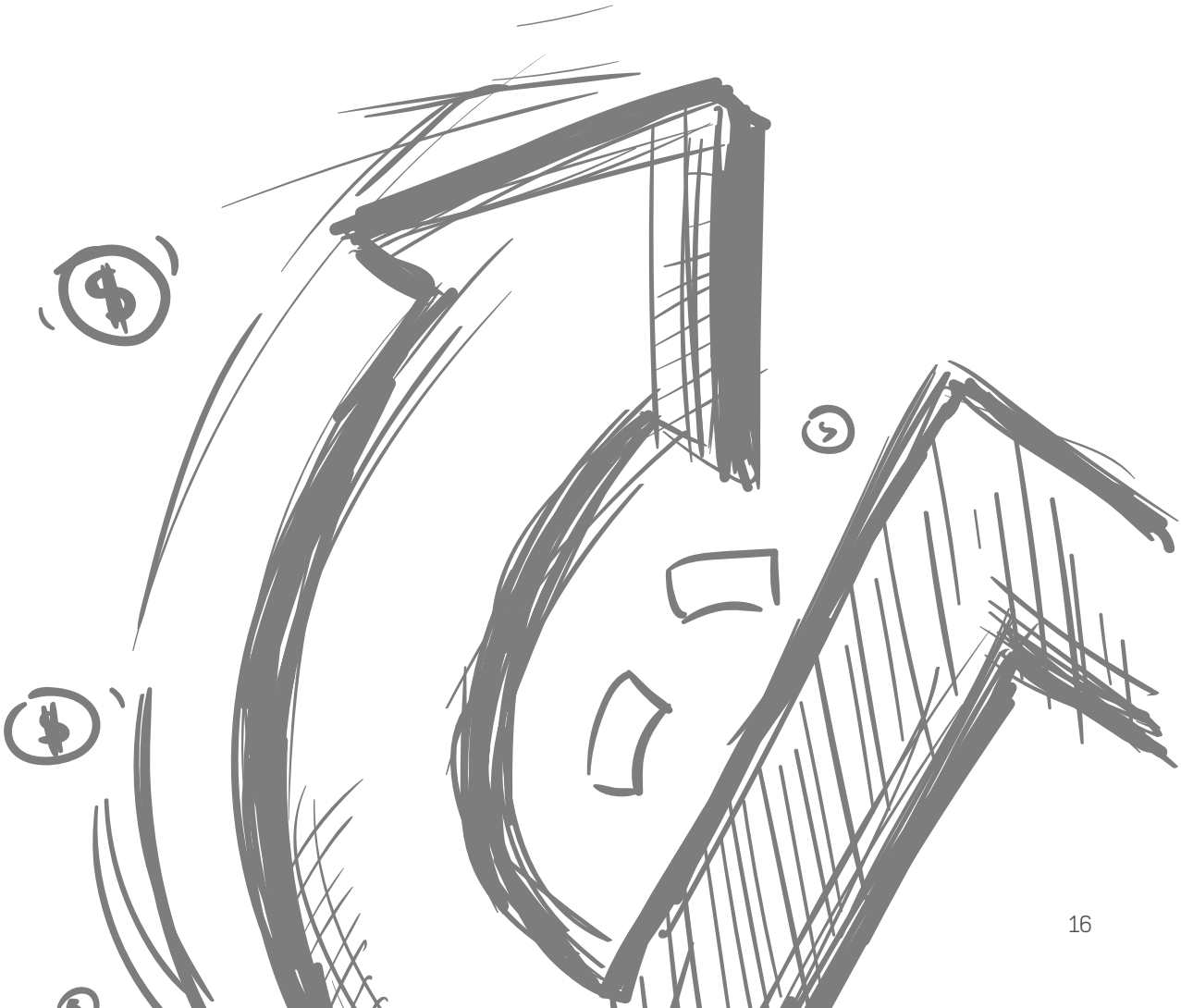
Culture

There are numerous specific cultural sensitivities to take into account - from the religious to the negative connotations surrounding debt collections due to a history of agencies in the region using third-party force. Banks must be able to customise their tech to cater to the cultural needs of their local customers. There is also the opinion that cultural differences could be a barrier to digital transformation in the region. Particularly for debt collections practices, customers need to understand that identities are no longer tied to pieces of paper and that there are plenty of robust and regulated digital identity services emerging that have the flexibility to attend to their cultural needs and work with local collections strategies.

Accepting the challenges

There are undoubtedly challenges facing those banks looking to make an impression in Southeast Asia, but with such enormous economic potential, it's certainly worth the effort. Whilst it might appear as though the challenges above offer a few significant hurdles to overcome, the majority of them can be comfortably navigated given the right tools and the right approach.

Ultimately, debt collections will always impact different countries in different ways relating to their economic and cultural climates. Underneath it all, though, they are all looking to make the process as painless and as friendly as possible and that's something all banks, regardless of their size or their country of origin, should be taking to heart.



Chapter 04

The future of APAC **debt collections**

> "PwC predicts that, by 2020, consumer intelligence will be the most important predictor....."

PwC predicts that, by 2020, consumer intelligence will be the most important predictor of revenue growth, the public cloud will be the most dominant infrastructure model, and - crucially - that Asia will emerge as a key centre of technology-driven innovation.

Microsoft and IDC predict that AI will be a major driver of economic growth, increased productivity, cost reduction and customer advocacy between now and 2021, supporting 40% of digital transformation initiatives. However, the same report suggests that only 7% of companies in the APAC region are positioned to lead these transformations. These businesses are concerned about how AI and other technologies will disrupt their competitiveness, they are creating cultures of innovation within their organisations, and they are aware of the challenges that lie between them and a return on investment in AI.

But how many of those leaders will you find within the APAC region's banking sector? Are APAC banks ready for AI? Can it help with the particular challenges the region is facing? And are banks, debt collectors and other financial institutions ready to embrace AI?

AI in APAC

The APAC region is already a hotbed for financial technology innovation, often targeted directly at areas where daily operations slow down around human interaction. For instance: opening a bank account in Hong Kong is now automatic, thanks to a direct interface between digital ID systems and virtual banks, streamlining a process that was previously slow, paper-based and burdened with a need for hard copy documentation.

In China, Xiaoi - a major league chatbot with 500 million users and 100 billion conversations to date - has seen widespread adoption across the financial, e-commerce and telecoms industries. Xiaoi handles all manner of routine interactions that don't necessarily need a person to make decisions; straightforward transactions like money transfers and repayments, along with data collection and user analysis by the banks. Xiaoi also provides China Merchant Bank's knowledge base system, distributing expertise and knowledge across departments on demand.

In lending, Chinese financier Ping An uses AI 'computer vision' to screen loan customers for reliability. Prospective borrowers answer questions about their income and plans for repayment over a video call: the AI views those calls live, monitoring 50 tiny facial tics to determine whether they are telling the truth. By pinpointing likely defaulters, Ping An hopes to head off debt collections issues before they arise - but what can AI do when an account is already failing to perform?

AI and debt collection

The kind of screening that Ping An uses AI to carry out would be ideal for addressing the loose credit control situation in China, India and Thailand. Personal insolvency is implicated in 24% of complex debt collections cases across the APAC region: AI can help identify would-be borrowers who are insecure or less than truthful about their financial circumstances.

Such insights can also be used to shape and guide approaches to dealing with debtors. Machine learning allows banks to preserve their relationships with customers in debt: AI can quickly identify and recommend the time of day, the tone of voice, and the specific way to pay that a given customer profile is most likely to respond well to. Personalising the debt collections service like this ensures that the actual labour hours of collectors are put to the best possible use.

There's also a question of operational efficiency to consider. As more and more banking systems become integrated with AI, the bank's operations as a whole can become more joined up. The easier and more responsive a system is to use, the more people will use it; and with complexity being such a serious cause of loan delinquency in APC, that simplicity is sure to pay off.

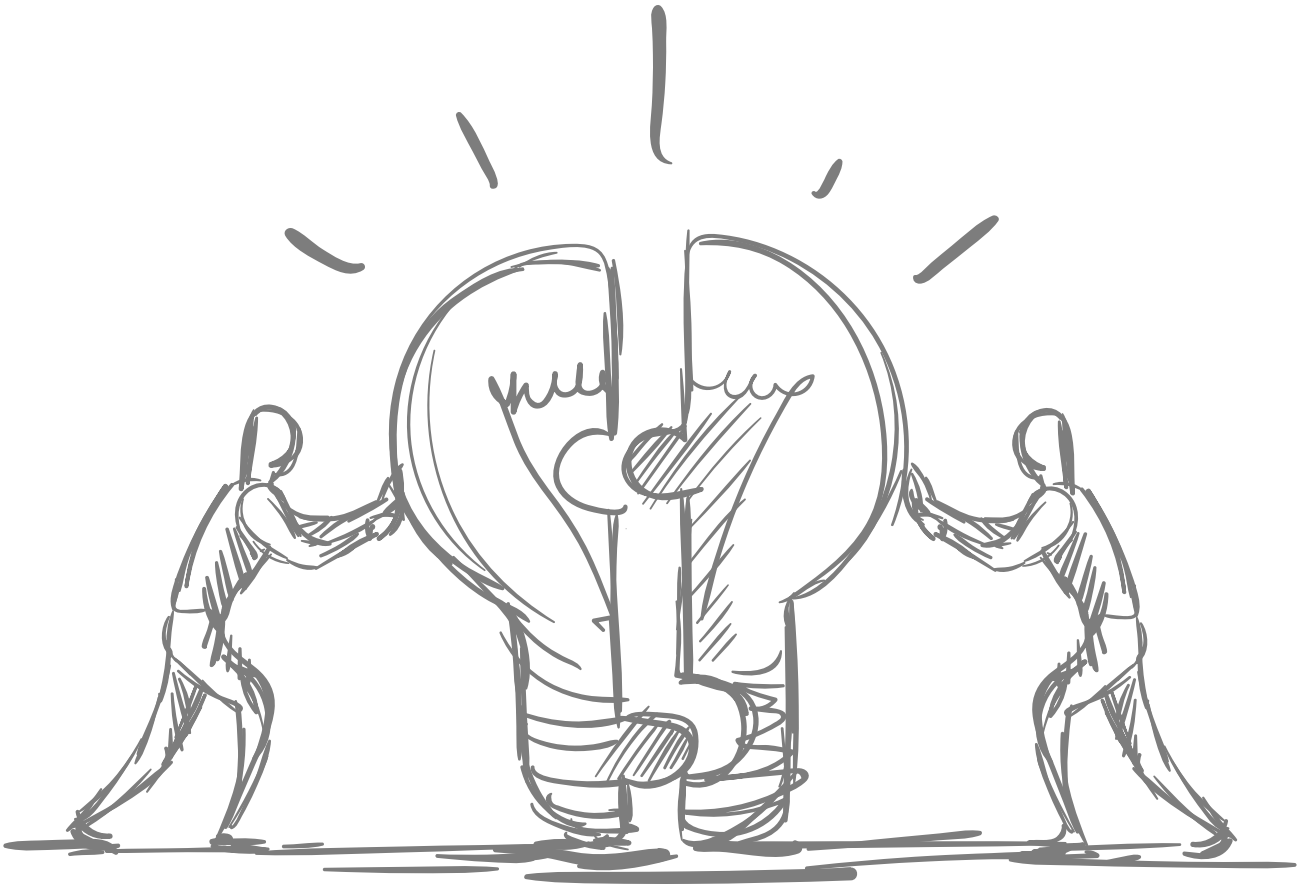
The reality: what can AI do for banking as a whole?

Here and now, AI is what 'big data' was three years ago. Industries are excited about it, innovators are obsessed with it, but very few institutions are clear about what exactly they mean by it or what they can use it for. In many cases, banks are ahead of the game: they have worked with business intelligence tools for quite some time, and there's less room for innovation here than outsiders generally realise.

What banks haven't done is to automate - outside of innovation hotbeds like

Hong Kong, banking operations often rely on Excel, paper, and considerable labour hours. This is the application of AI that makes sense for banks - automating the processing of information, assembling it and comparing it to the criteria that determine who is a low or high-risk borrower. This is not a massive change to operations, but it is a significant improvement in their efficiency, with computers taking over the donkey work of routine credit checks, transaction handling and frequently asked questions.

AI can't solve all of a bank's problems, but it can improve the efficiency with which they identify and understand the problems and deploy their solution. So, as long as APAC banks are ready and willing to embrace AI, there is no reason why they won't be able to compete with some of the biggest banks in the world.



Epilogue - Learn from the past and build for the future

The APAC region is one of intense, focused growth that continues to defy expectations and promote progressive economic ideas. This spirit of invention and adaptation needs to find its way to the retail banks and, more specifically, their debt collections teams.

The way forward lies in APAC banks examining what has come before and where the market is heading, and using those insights to plot a course for the future. That means understanding the way Japan used transparency to solve their millennial debt crisis without losing face and taking stock of the fears that are holding banks in the region back.

There are specific considerations to be made for APAC banks, of course, with so many disparate cultures and situations at play in the region and governmental corruption that, in some cases, doesn't appear to be going anywhere soon. The banks need to be flexible with their debt management solutions in order to negotiate these tumultuous waters with poise and clarity and there are many alternative avenues to explore that don't adhere to the antiquated methods of old.

The region is certainly ready for change. Indeed, a study has even revealed that APAC businesses are more open to alternative debt collections solutions than even their European counterparts. Does this also mean the region is open to accepting digital transformation? It would appear the population are more than ready and it's now up to the banks to make those changes happen.

If they can do so by making debt collections more simple, customer-centric and approachable via digital transformation, then all the historic cultural shame, local governmental noise and deep-rooted fear in the world won't be able to stop them from competing on the global stage.

About EXUS

EXUS is an international enterprise software company specializing in credit life cycle management. EXUS was founded in 1989 with the vision to transform the complex software industry, making it simple, accessible and exciting. Our products have been designed through a deep understanding of our customers' needs and in line with our purpose to simplify complexity and enable intelligent action.
Through our corporate headquarters in London, our offices in Athens and our partners, we support financial institutions, telecom operators and utilities companies around the world to improve their credit risk management efficiency, increase confidence in their strategic decision-making, and achieve success in demanding and competitive markets.

EXUS Financial Suite

"EXUS Financial Suite" (EFS) is our comprehensive suite of software applications that manages credit risk along the whole lifecycle of accounts, from the moment of disbursement until write-off or debt sale. EFS helps organisations in 30 countries around the world to identify and treat credit risk early, perform efficient collections, manage legal proceedings and recoveries and gain detailed insight into portfolio evolution, collections strategies and resource efficiency.

EFS was rated "**best-in-class**" solution for collections in the first ever global technology analysis of loan collections systems by leading industry analyst issued by CEB – GARTNER.

EXUS also received the **XCelent Depth of Customer Service Award** from **Celent** in 2019. Based on customer feedback, EXUS was ranked highest amongst all global vendors participating in the study and in the top right quadrant for breadth of functionality and advanced technology

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