RECEIVABLES FINANCE: THE VOICE OF THE INDUSTRY

The future of receivables finance, as told by providers

LENDSCAPE

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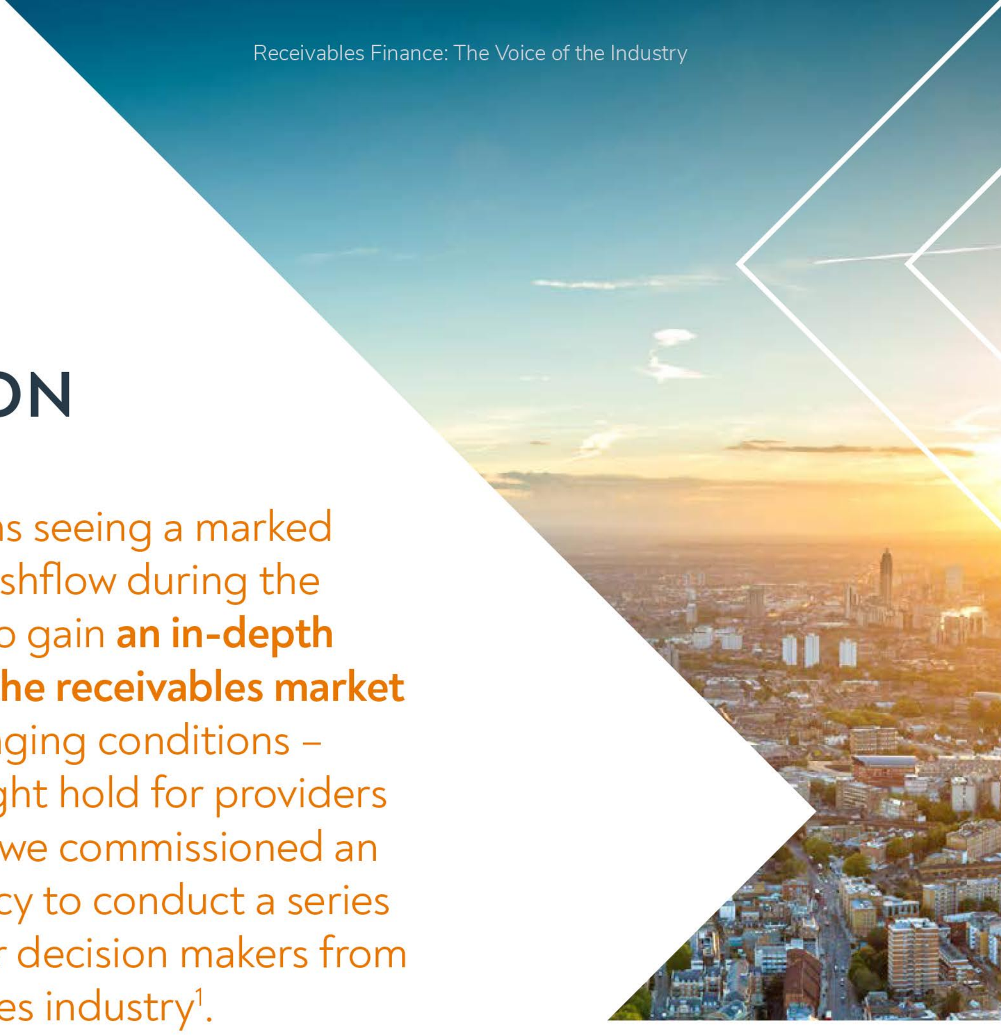


INTRODUCTION

With many organisations seeing a marked deterioration in their cashflow during the pandemic, we wanted to gain **an in-depth understanding of how the receivables market** is faring in these challenging conditions – and what the future might hold for providers everywhere. To do this, we commissioned an independent consultancy to conduct a series of interviews with senior decision makers from across the UK receivables industry[1].

Presented across the following pages are the key themes that emerged during the course of these interviews. While every participant in our study shared their own unique – and sometimes differing – insights, the views shared here represent a concise summary of the issues dominating the collective receivables mindset.

Through these responses, we see an industry on the cusp of significant change. The year ahead promises to be one of growth, though some providers may choose to pursue opportunities elsewhere. Those that remain will look to derive greater value, and competitive advantage, from the technology in which they invest. To that end, new approaches and new models may emerge, laying the foundation for stronger and more user-friendly products and propositions.

Naturally, not all of the viewpoints presented here are shared or endorsed by HPD Lendscape. They are presented impartially, and with the clear caveat that they represent the amalgamated thoughts of a select group of individuals rather than the industry as a whole. Nonetheless, they provide a fascinating insight into a potential future for receivables finance.

1 Research for this study was conducted by GrowCap, a multi-disciplinary consulting and services firm, during September 2021.

01

DEMAND GROWS
as recovery continues

The pandemic sparked a crisis in business cashflows. The impact on receivables finance has been tangible, though not in the way that may have been expected.

Covid's crippling effect on business cashflows in 2020 was clear for all to see. Amongst those that accessed finance through either of the government's two Coronavirus-related loan programmes, almost three-quarters did so with cashflow[2] specifically in mind. Even with those schemes in place, many still suffered, with the Bank of England estimating that UK businesses faced an aggregate cashflow deficit of around £140 billion between Q2 2020 and Q1 2021[3].

Naturally, one of the things that we were keen to understand as part of this study was the onward impact of the crisis on the receivables finance market. With invoice financing traditionally providing cash-hungry firms with faster access to cash, the current reality is that demand for receivables finance has weakened – with the robust recovery schemes mentioned above playing their part. Respondents were quick to tell us that utilisation has been "well below historic norms" during the pandemic, with initiatives such as the Coronavirus Job Retention Scheme, Recovery Loan Scheme, and VAT deferral programme having done much to alleviate pressure on short-term finances.

£140 billion

The aggregate cashflow deficit faced by UK businesses between Q2 2020 and Q1 2021

2 *BCC/TSB: Businesses need flexible financial support to recover from pandemic* – British Chambers of Commerce, September 2020

3 *How will the Covid-19 shock affect the cash flows of UK companies?* – Bank of England, June 2020

No-one's rushing to pay back low-rate government lending.

Receivables may have taken a backseat to alternative means of funding, however, there is a suggestion that many of those moving away from it were infrequent users. "Lost customers were marginal users," explained one interviewee, suggesting that any erosion in the perceived value of receivables finance has been primarily at the periphery.

Moreover, we see clear evidence that receivables finance volumes will soon begin to rise again. Even though overall demand may have fallen during the pandemic, respondents cite spring 2021 as a turning point – the moment when volumes once again began to pick up. There is little coincidence that both the Coronavirus Business Interruption Loan and Bounce Back Loan schemes[4] came to an end at the same time, with the furlough programme having ended just a short while earlier.

As we move further away from the closure of those support schemes, 2022 promises to be a growth year for receivables finance. With deferred liability payments coming due, and "event-driven" activities like M&A beginning to surge, respondents foresee a groundswell of demand for receivables related finance.

Small businesses, in particular, may look to receivables finance as a way to deal with other financial commitments; SME debt increased by 25% between 2019 and 2021, compared to just 2% amongst larger enterprises[5]. The full impact of that significant increase in borrowing will likely depend on how eager financial institutions are to pursue the collection of government-guaranteed loans.

4 These schemes were introduced by the UK government to support businesses through the pandemic, and are similar to EIDL programme in the United States, and the Economic Stabilization Fund in Germany.

5 *Financial Stability in Focus: The corporate sector and UK financial stability* – Bank of England, October 2021

02 OPPORTUNITIES ARISE as the market shifts

As demand for receivables finance begins to flourish, willingness to meet it may be dwindling – creating clear opportunities for those who stay the course.

Demand for receivables finance may have dipped, but few expect it to stay that way for long. However, as the market continues to recover, it may also come to look very different – with respondents suggesting that one of 2022's major trends could be a fundamental shift in terms of provision.

Several factors are at play here, but chief amongst them is the belief that some larger banks and lenders are now looking to minimise their exposure to risk. Respondents note that – with banks already carrying the lending burden of the two main Coronavirus support schemes – simplification is likely to be their new imperative.

As a result, and as they seek to standardise their portfolios, many may start to scale back their receivables finance offerings.

Further weight is added to this sentiment with the suggestion that bad debt and fraud could rise in the coming months. Some banks have already stressed that between 40-50% of those who utilised the Covid support schemes may default on repayments[6], a thought that will undoubtedly be front of mind as they evaluate their lending strategies going forwards. However, respondents do note that there is yet to be evidence of that deterioration.

40-50%

Between 40-50% of those who utilised the Covid support schemes may default on repayments

6 *UK banks warn 40%-50% of 'bounce back' borrowers will default* – Financial Times, May 2020

> **[Banks] don't see much growth potential for invoice finance.**

While risk may be a major concern, it isn't the only issue driving change. The continued cost to serve, in tandem with a sensation that larger banks and lenders may be re-focusing their lending propositions on organisations that present greater long-term value, lead some study participants to speculate that receivables finance is simply less attractive to banks than it once was.

In their eyes, respondents believed this will create a potentially substantial opportunity for independents. Some even go so far as to state that they believe independents will gradually take the lead around receivables, as larger banks or lending organisations exit the market altogether in favour of more "standardised" finance offerings.

Independent or not, capitalising on the growing opportunity around receivables may in part depend on being able to navigate the expanding divide between invoice financing and factoring. Interviewees highlighted a significant shift away from factoring, with invoice discounting and even short-term loans taking precedence in many instances.

If this trend of reduced bank-factoring continues, it will create a growing need around this SME segment and present a clear opportunity for those wishing to pursue it. While not every end customer will make a clear distinction between the unique benefits offered by factoring and discounting, those that do could prove to be a rich source of business as supply of the former continues to contract.

03 VALUE GOES UNREALISED as profitabilty challenges persist

The high cost to serve is one of the numerous issues undermining the receivables market today, with finance organisations running into frequent challenges caused by overly complex technology.

As with any financial product, the viability of a receivables offering isn't just about the raw value that it delivers. For it to be truly sustainable, a receivables finance solution must also be efficient, scalable, and easy for customers to use. All too often, these are qualities that many struggle to recognise in the systems that they currently employ.

The technology that underpins today's receivables finance market is an area of major contention. Respondents cite several problems, all of which cause significant friction for their internal teams and the end customer. Crucially, these concerns run right across the underlying infrastructure, from onboarding to in-life execution.

One of the primary factors here is the need for greater simplicity. Several interviewees mentioned a growing need for streamlined systems – ones that can improve operational efficiency for their own businesses while simultaneously reducing friction for end users.

> **"By comparison, [customers] can get other financial products with a few clicks.**

1,000 clients, each with 1,000 customers is... a meaningful scale for analysis.

Using technology to improve the customer experience is seen as a priority, with many borrowers seemingly struggling to realise the true value of receivables technology platforms. Onboarding is called out as a particular pressure point, one that can feel slow and intrusive to customers. Some solutions also seem to hamper crucial tasks such as audit and reconciliation and prevent potentially additive ones like accounting data extraction from taking place.

The latter of these in particular is seen as something that could prove to be a "goldmine" in the near future – empowering smarter risk management, and providing the insights required for organisations to drive meaningful service enhancements and new offerings aligned with customer needs.

Generally, there is little doubt amongst respondents that technology holds the key to a better and more mature future for receivables finance. Several participants point towards wider trends such as cloud, API-based systems, and microservices, stating that vendors must fully embrace those technologies if they're to play a role in the next generation of receivables finance platforms.

This sentiment, as we'll explore next, can almost certainly be traced back to the disruptive influence of fintechs.

04 CONTEXT BECOMES KEY
as new solutions emerge

Just as they have elsewhere, fintech companies have the potential to fragment the receivables finance market – presenting buyers with a raft of new considerations.

While the majority of the problems posed by existing receivables finance products are caused by complexity at the core, the actual symptoms tend to manifest most prominently where clients interact with them. As a result, where financial institutions might be looking to meet modern expectations around the digital customer journey, they're often left with one that can feel decidedly vague to end users. While products may demand a certain level of depth under the surface, after all, that doesn't mean that the customer experience should be disordered or complicated as a result.

Not only does this have a negative impact on the customer experience, respondents note that it also presents a distinct commercial risk. Drop-off rates in receivables finance are high, they point out, meaning that the time and effort required to onboard a customer can ultimately translate into just a few months of actual business. When combined with the previously mentioned cost to serve, many opportunities prove to be less profitable than initially envisaged.

With that in mind, it's little wonder that the development of simpler, more streamlined products and propositions has become an overriding priority.

> **[Customers] want cash, not an invoice finance product.**

> **10 years ago, talking to a fintech was thought of as a risk. Now it's not.**

In pursuit of those new models, many organisations demonstrate clear admiration for the focus and "design thinking" demonstrated by fintechs – centred as they tend to be on solving specific problems within a single process. The implication is that, by virtue of their ability to resolve individual customer pain points, fintechs could be instrumental in helping providers achieve the kind of simplification they're seeking.

There are arguments both for and against this line of thinking. On the one hand, the specificity offered by fintechs may allow organisations to address some of the more deep-seated issues within their receivables offering.

On the other, those businesses may end up trading technical simplicity for architectural complexity, needing to integrate a disparate selection of vendors in order to create a cohesive end-to-end experience. And while this may be a tolerable exchange for some, others will undoubtedly prefer to maintain the stability that comes with a more traditional approach.

Despite the caveat, a modular and collaborative approach to receivables finance holds clear potential for those willing to pursue it. Providing the ability to mix and match technical solutions to specific tasks, a model of this kind could bring a new level of flexibility and agility to the receivables landscape – if, of course, it is implemented in the right way.

> **The number of SMEs using fintechs is growing hugely, because their focus is on (customer) experience.**

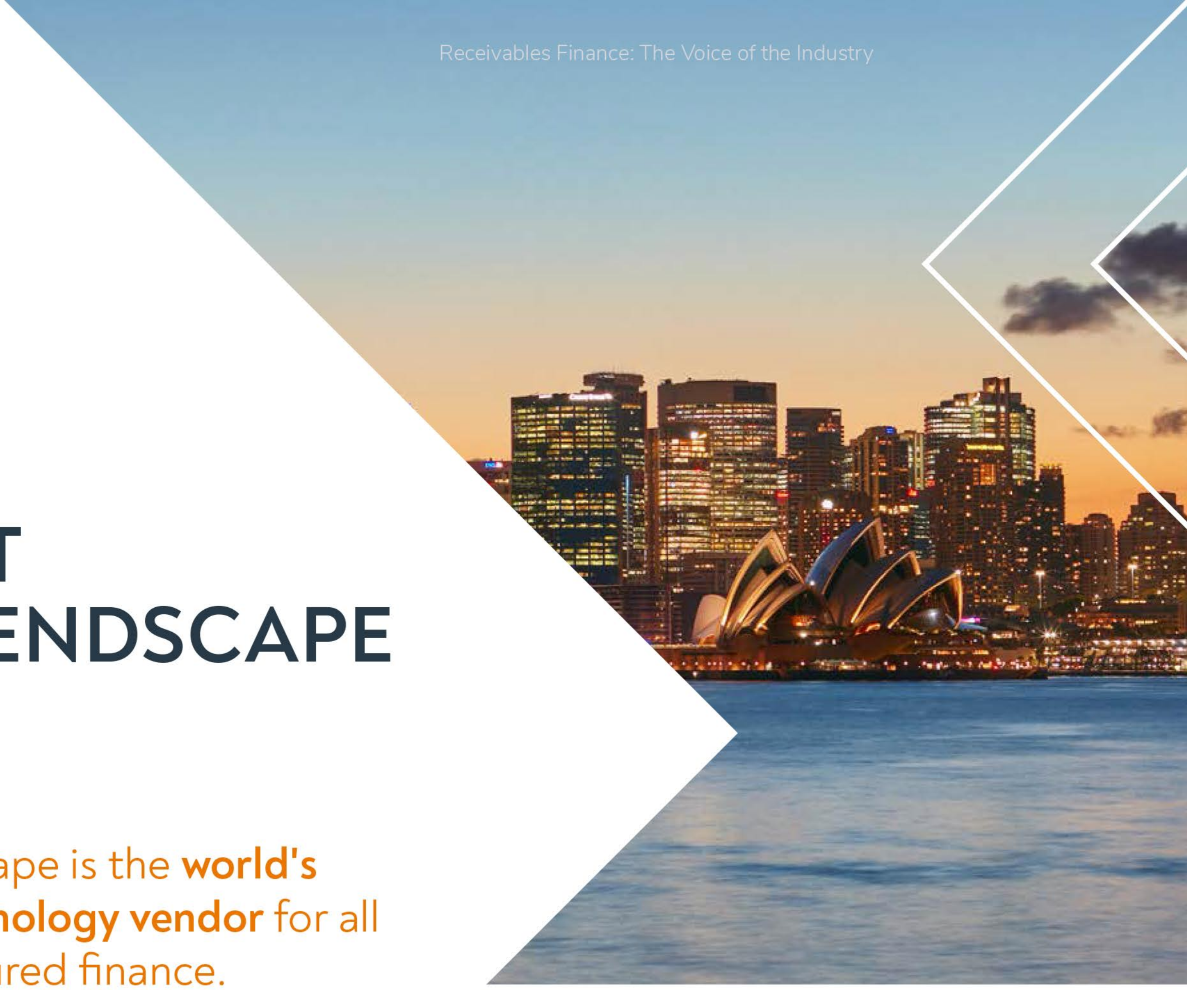
05 Conclusion: CHARTING A COURSE for a better future

In the many hours of interviews conducted for this study, three messages about the future of receivables finance came through time and time again: the short-term outlook is strong, and there are clear opportunities ahead, but the technological infrastructure underpinning the industry requires significant modernisation.

At HPD Lendscape, our vision is of a market in which technology empowers a smarter working capital finance experience. For the industry to thrive as it should, technology must deliver value across the entire spectrum – creating engaging experiences for customers, reducing cost and effort for providers, and allowing them to develop new and profitable solutions and services where appropriate.

In pursuit of that future, providers will need to be certain that the technology in which they invest provides them with a true platform for growth. Solving the challenges of today is one thing, selecting a system that's ready for tomorrow is another, and providers must ensure that the technologies they put in place can match the scale of their ambitions across the long term.

Whether through traditional, linear architectures or modular approaches that combine best-of-breed applications, the technology driving the future of receivables finance must offer stability, security, flexibility, and agility in equal measure.



ABOUT HPD LENDSCAPE

HPD Lendscape is the **world's leading technology vendor** for all forms of secured finance.

With over 45 years of experience and in-depth industry understanding, our dynamic team has designed, developed, and delivered secured lending technology to over 50 markets and some of the worlds' most prestigious banking and financial services providers.

Our secured lending platform, Lendscape, supports a range of working capital financial solutions such as factoring, invoice discounting, supply chain finance, asset-based lending as well as many other forms of specialist finance.

To learn more about HPD Lendscape and the solutions we offer, contact us on the information above or please visit **www.hpdlendscape.com**.

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