KEYNOTE INTERVIEW

Navigating new markets

There are always lessons to be learned when growing a pioneering business investing in European consumer and SME loans, says Selina Burdell, co-founder and chief operating officer at LCM Partners

SPONSOR
LCM PARTNERS

Q What made you decide to enter the European consumer and SME market over two decades ago?

In 1998 we launched this business because we saw that the sale and purchase of what was primarily non-performing consumer credit card debt at that time was producing highly attractive returns in the US, yet nobody seemed to have made the move in Europe. We started out in the UK, approaching banks and consumer credit providers with a new solution for risk management, and our proposition quickly gained traction. Once we had some scale in the UK it wasn't long before we started expanding into new markets.

Q What are some of the key lessons you have learned in the past 23 years?

The biggest lesson that we learned, very early on, was that we would need to have an in-house servicer. It is not possible to buy distressed consumer and SME credit at that level of granularity, then just package it up and sell it. We needed to be able to make it re-perform and produce a cashflow. That meant a shift in mentality from thinking of ourselves simply as investors in debt, to realising the need for a loan servicing and credit management business and to setting up the Link Financial Group. Today, our investment management business, LCM Partners, operates out of London while Link Financial, which I also oversee, employs close to 900 people across eight European markets.

We also had to learn how to price this debt. I think it is fair to say that pricing was somewhat more fluid in the beginning, but today, with over 20 years' track record, we have become pretty good at predicting how portfolios, which often comprise many thousands of loans, will perform; how many non-performing loans will repay and over what time period; or, if it is a performing loan portfolio, how many loans will roll to arrears or even default. I would also add that we have learnt a lot about people along the way – both in respect of our customers and how they behave, but also how to hire, motivate and develop our own team.

Each of these lessons needed to be re-learned every time we expanded into a new country. We needed to build up that pricing data, form relationships with the banks and generate an understanding of the underlying customer base and the local socio-demographic nuances. Do these customers prefer to speak with you or receive written communications? Do they want to be the first to engage or will they respond to your approach? No two European markets are the same.

Q Was it always the intention to build a pan-European platform?

Not at first. The UK represented, and continues to represent, the biggest consumer credit market in Europe, so it made sense to start there. Then, within two to three years, we recognised that similar opportunities existed in other European markets. Indeed, the original consumer finance banks we worked with in the UK are international businesses and they wanted us to be one of the tools they could use for risk management in their other markets. Knowing we had existing partnerships with those active sellers gave us a real advantage when we moved into new countries such as Spain, which was our first market outside of the UK.

Q Are there other challenges you face when expanding into new geographies?

Data or collections experience for pricing is paramount. That access to data is a major barrier to entry. I would say that finding the right management team is also key, particularly as a lot of our early expansion was organic.

In addition, understanding different regulatory environments is critical. The UK is one of the most highly regulated markets in terms of consumer protection, but there are idiosyncrasies in each jurisdiction. Even the EU General Data Protection Regulation is not consistently applied across the continent.

Q Your early expansion was organic. Has that strategy now changed?

Prior to the global financial crisis, we established Link Financial operations

in five new geographies, and we always went down the organic route. That was because it was important for us that each new team shared our values, our approach or processes and made use of our proprietary software. More recently, however, we have pursued a mix of organic and acquisitive growth, each of which comes with its own set of challenges. Typically, we will have tested a market in advance of full launch in any case, working with a local servicer for several years to help scope out the size of the market. The results of those test transactions will inform how we enter the market for the longer term.

Q How did the global financial crisis impact this market?

The best statistics we have on loan sales in 2010 put the market at €12 billion. By 2018, that had grown to €205 billion. Clearly, the global financial crisis greatly magnified the investment opportunity. Our job is to discern what part of that expanding market opportunity we should be targeting to deliver sustainable and consistent returns for our investors.

It's not just the size of the market that has changed but also its composition. A much wider spectrum of performing, re-performing and non-performing receivables are being sold in the market today.

Indeed, our experience acquiring performing loan portfolios led us to launch our Strategic Origination and Lending Opportunities direct lending strategy in 2018. It's a niche, asset-backed strategy focusing on pockets of the market that have been largely vacated by the banks and other financial institutions post-GFC but still at the granular end of the loan market.

Q What impact do you think the covid crisis will have?

There is no doubt that covid has been a big challenge for our industry. Taking everything that you do, in a highly regulated environment, and moving to a remote working scenario almost overnight was difficult. It forced us to look at new ways of doing things. We went from having 900 people working in Link Financial's offices, printing and mailing documents, to operating far more in digital ways, such as through helping our customers become more self-servicing online. The pandemic has accelerated the use of technology in this market.

Covid will also have an impact on customers' ability to repay loans,

Q How gender diverse is this corner of the financial services industry?

I am not sure private debt or credit is any different from the rest of our industry, which tends to be fairly male dominated. LCM has a good level of gender diversity, although there is room for improvement in some areas. For example, our legal team is majority women while the investment team is currently a little less well represented in that respect. However, I am pleased to say that at least a third of our July new intake is female, so we are slowly improving the balance. As we are investing on a pan-European basis, we also have a multi-national team in the London office with at least 10 European languages being spoken and a variety of cultural backgrounds.

Across the wider Group, including Link Financial, we have excellent gender diversity and a growing proportion of women in senior leadership roles, with over 40 percent of management roles being taken up by women.

"Each lesson needed to be re-learned every time we expanded into a new country… No two European markets are the same"

particularly when government support schemes are eased. I expect there will be an increase in defaults, but I don't think it will be as high as many would have predicted last year. There is still a whole section of society that has benefited economically. They have more money in their pockets, having saved on commuting costs, lunches out and even drinks after work, and they have used that money wisely, including reducing personal borrowing.

At the same time, customers who work in the retail and hospitality sectors may struggle when the wage support mechanisms that have been in place across the UK and Europe are withdrawn. If interest rates rise as the economy takes off that could also hit our customers in the pocket.

Q How have you adapted as a firm to keep pace with this changing market?

From our investment teams to our servicing operations, the Group has become a great deal more sophisticated over the years. We actively encourage our people to learn new skills and to gain knowledge of new types of assets they can manage, for example. That could mean us working for third party originators to gain experience in an emerging product or sector. We have enough scale in both our asset management and servicing business to be able to invest for the long term in that way.

The Group also launched its own software business in 2019. When we first started out, the software we needed to manage all these customer accounts did not exist, so we had to build it ourselves. Having those capabilities in-house has been a huge advantage during covid. It has allowed us to be flexible and helped us achieve what we needed both in terms of executing complex data migrations and increasing operating capability.

Q What do you believe the future holds and what are your priorities?

At the moment, the future remains uncertain. We have some markets coming out of lockdown, while others are facing a fresh set of restrictions. I would love all our operations to return to business as normal. We can do our jobs remotely, but I think we can do them better when we're together.

Good quality deployment, meanwhile, is a perennial priority. We operate two strategies – a non-performing loan focused Credit Opportunities strategy and the Strategic Origination and Lending Opportunities direct lending strategy I mentioned earlier. Both have strong pipelines and I believe the covid crisis will benefit both businesses but, as with all asset classes that generate attractive risk-adjusted returns, there is healthy competition in the market.

We have an advantage in the length and depth of experience we have built up in this space but there is always more that can be done in both the short and long term. We continue to look for new ways to make our loan servicing and management operations more efficient. We have recently opened an office in Romania to enable us to take advantage of near-shoring and to centralise some of our servicing capabilities.

At the same time, we are pursuing some exciting projects in the realm of robotics and robotic process automation, with the aim of driving even greater efficiency. As we emerge from the pandemic, we will continue to balance the needs of our investors with those of our team, ensuring everyone is safe and motivated to deliver continued success. ■

LCM Partners is part of the LC Financial Holdings Group which includes the Link Financial loan servicing and credit management business