The Future of Collections in Banking

How adopting latest AI innovations can help banks address ever-changing customer behaviours and solve key challenges of collections

Executive Summary

The financial sector is facing many challenges today, with more extensive competition driving down net interest income and commissions, plus the disruption caused by new banks and lenders such as Google, Apple, Facebook and Amazon (GAFA). threatening the very existence of banks.

These factors, combined with the calling for on-demand services from consumers and the emergence of cloud-based technology and artificial intelligence (AI), are creating an “adapt or die” ultimatum for financial organisations. Now is the time to be more dynamic, cost-effective, diversified and innovative.

One of the most overlooked elements within the financial sector is the importance of efficient debt collection processes and the potential to optimise scoring with that data. While most banks and financial organisations have deployed some sort of proprietary or rented in-house software or have collaborated with a third-party collection agency, very few have started leveraging the technological and analytical potential of the latest artificial intelligence solutions and advanced machine learning (ML).

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Those who embrace the evolution of the global credit environment now and use innovative technology-led collection processes will understand their consumer behaviours on a deeper level, while gaining a competitive edge in the market by operationalising the valuable data gathered before inevitable mass adoption begins.

However, like most technology and innovation in the financial sector, change takes time. A prime example of this is contactless payments, which Mobil gas stations trialled with their Speedpass back in 1997. The financial sector didn’t utilise this technology for another two decades. Similarly, mobile payments came to light in 1997 as well when Coca Cola introduced a limited number of vending machines where customers could make a mobile purchase. Once again, banks and other financial organisations took decades to integrate this technology into their mobile banking services.

Mass adoption of collections technology powered by ML and AI is set to follow the same lengthy process for the diffusion of innovation outlined by Everett Rogers. The concept will require knowledge sharing, persuasion, implementation, confirmation and decision making before key figures take note. It’s just a question of whether a financial organisation wants to be an early adopter or a laggard.

The focus of this paper is to explore why investing in collections processes is important, what the current problems are and the possibilities. In particular, it investigates why simple automation of collection processes isn’t sufficient enough in maintaining customers with the development of financial services offered by GAFA, while revealing new avenues made available to collection processes by AI and ML.

It also uses the latest findings to discuss what the future of collections may look like to help shape an organisation’s long-term strategy. The insights in this paper are particularly useful to retail banks, lenders, collection agencies and financial services consultancies committed to using this process to steer the ship towards top line growth or profit.

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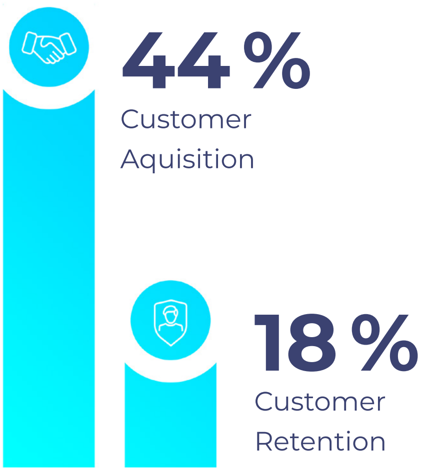
The current state of collections

Why simple automation of collection processes isn't enough and is losing retail banks valuable customers

According to Invesp, it costs five times as much to acquire new customers, than to keep an existing one.

Yet, the current attitude towards collections is to do anything possible to get customers to settle their debts and get them off one's books. In fact, the same report from Invesp shows that 44% of companies place a greater focus on customer acquisition versus 18% who focus on retention.

It costs five times as much to acquire new customers, than to keep an existing one



44 % of companies have a greater focus on customer acquisition vs. 18% that focus on retention

It's a worrying trend that is costing banks and other businesses millions of Euros in marketing and sales costs every year. This approach would not be an issue if every customer with an outstanding debt was deemed as bad or high risk. However, this isn't the case. Every customer has a story and is facing different challenges. To brand every customer as the same is a form of negligence and puts the future of a retail bank in question.

The modern world has the luxury of choice and options. Customers no longer feel obliged or committed to staying loyal to one bank, thanks to low switching costs and the accessibility presented via the emergence of the internet since 1991.

Customers are calling out for a seamless, self-service solution

Younger, computer-savvy Millennials (1981-1996) and Generation Z (1996-2010) customers come with increasing expectations and on-demand solutions. Banks expecting their customers to take calls, or to visit them in branch during work hours, is out of date. Making payments, especially when it involves something as negatively perceived as loans, credit or overdrafts, needs to be quick and simple.

Customers are calling out for a seamless, self-service solution accompanied by positive touch points along the way. Digitalisation is already commonplace in banks with online banking and on-demand apps. Yet, the adoption of it within collection processes is leaving a lot to be desired. Banks haven't prioritised overhauling their collections processes and are still heavily relying on letters and calls instead of modern forms of communication like emails, text messages and push notifications. Despite customers preferring the latter.

Exhibit 2

Credit-card customers mostly prefer to be contacted by email & text

Preferred channels of contact, ranked by % of respondents[1]

[1] N = 434 survey respondents. Analysis excludes respondents under 30 days delinquent
[2] Balance criteria: low <= $1,000, high >$1,000
[3] Risk criteria: low, FICO > 620; high, FICO < 620

https://www.mckinsey.com/business-functions/risk/our-insights/the-customer-mandate-to-digitize-collections-strategies

McKinsey & Company

Innovative Treatments

In terms of tone, collections should be treated as a form of communication and not the imposition of terms. It's a matter of developing a dialogue and providing solutions that are personalised to suit a customer's unique story.

Customers have a psychological need for agency and control. While the concept can be found in slight variations in many different domains, the general concept revolves around a human's need to feel in control. In McKinsey's guide on behavioural insights and innovative treatment in collections, it discusses how many overdue customers refuse to speak to collectors by making use of caller ID. While at the same time, they intend to make a payment as soon as they have the money. However, being contacted multiple times makes the customer feel like the situation is out of their hands and they're being forced to make a payment.

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This leads to something psychologists call "reactance", which is where a customer takes measures to assert control, such as withholding payments or ignoring collectors.

Studies highlighted in the same McKinsey report revealed that 20% of respondents said they withheld a planned payment at least once after receiving an upsetting call from a collector, while 80% didn't make a payment until they received a firm prodding.

Customers are more likely to respond if they have access to a self-service solution led by a series of 'nudges'. Nudges is a term used to describe the action of guiding human behaviours by the use of user-interface and design elements in digital environments. Scientific studies prove that on a cost-adjusted basis, the effectiveness of nudges is often greater than that of traditional approaches.

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Nudges come in all shapes and sizes, playing an integral role in optimising the messaging of digital forms of communication, such as emails and SMS. Prime examples in the world of banking collections include the carrot and the stick method. This is where banks offer incentives like early payment discounts, waive fees or agree to payment plans before resorting to warnings, administrative penalties and taking legal action.

Another area which is often overlooked by banks is an unwillingness to send messages out prior to a customer entering the late payment cycle. Banks have all the reactive measures in place but are failing to consider the effectiveness of being proactive. Sending warm and friendly payment reminders out weeks before can guarantee sufficient banking account coverage in advance, while reducing the stress on the collections team.

It seems the world has continued to move at lightning speed, but the approach from banks is continually playing catch up.

The possibilities presented to banks

How improved collections can help banks save money and achieve further growth

As discussed in the Executive summary, various collection solutions are being presented to banks. However, most of them focus on workflow automation instead of self-optimising for time and conversion using AI and driving a resolutive dialogue with the customer.

There's an opportunity to leverage advanced technology to analyse and utilise existing data. AI can attain vital demographic and behavioural data and use it to craft the right message, send the message at the right time and know what channel to use.

Recovery rates can be drastically improved with a significant cost decrease when banks go digital with collections

Customers can be approached in a personalised way via their preferred channel, at a time they want and using a nudge that resonates.

Advanced analytics allow for a very nuanced breakdown of content performance and can give banks an insight into which content piece performs best for a particular demographic. Pairing this knowledge with modern digital marketing KPIs can significantly help enhance operations too. As Deloitte highlights in its white paper on 'Collections strategies for the digital age', using the right analytics, and doing it well, can enable banks to understand which customers are most likely to be positively influenced by certain collections benchmarks.

While common collections metrics and KPIs, such as Right Party Contacts (RPC) and Profit per Account (PPA) are still useful for assessing volume and results, they don't give banks a better understanding of customer behaviours and responses. Total email delivery rates/bounce rates, email open rates, click-through rates, traffic by source or channel, landing page views and reaction times are just a few of the digital marketing KPIs that will help banks address the route of the problem with their collection processes.

Having access to this kind of detailed information will enable banks to deliver more specific optimisation, address any content issues and effectively automate some stages of the collection process.

On a more general basis, recovery rates can be drastically improved with a significant cost decrease when banks go digital with collections. Emails and text message payment reminders are more intertwined with the busy demands of everyday life and can be accessed on the go. Customers no longer have time to take calls during work hours or want to be bothered during their downtime, and letters asking them to go out of their way to make a payment, i.e. call them or visit a website, will be greeted with frustration.

As mentioned before, using the analytics and behaviours presented by AI and ML and using digital forms of communication will allow banks to break down the barrier currently blocking them from improving the effectiveness and speed of collections.

Implementing the solution into the strategy

How to make collection processes a critical part of a bank's overarching strategy

In previous sections, we've discussed the positive impact an innovative approach can have on the customer experience, churn rate and day-to-day operations, but what about a bank's central strategy?

Take the possibility of GAFA entering the banking industry as an example. Since the rise of digital banking and the decline of the branch, the relationships between banks and customers have dwindled. Financial institutions, in general, are all under pressure to keep up with digital transformation, while maintaining an excellent customer experience.

Banks must do everything they can to remain central in the lives of customers

Google, Apple, Facebook and Amazon already have access to the data of billions of users around the world and are experts in communicating. For instance, when a customer orders something on Amazon, they'll receive several personalised emails and texts keeping them informed about the status of their delivery.

Plus, GAFA is already utilising the best in cloud computing, customer-facing artificial intelligence and big data customer analytics. With this in mind, it would be a relatively seamless process to extend their current offering to cover lending and payment services.

Banks must recognise this threat and do everything they can to remain central in the lives of customers by creating an experience across the digital and physical environments.

Banks who solely rely on letters and calls aren't taking the opportunity to address every touchpoint in the customer journey. One day a customer takes out a loan and is regarded as a valuable customer, and the next, they're in arrears and are being harassed to settle their account. They are also not leveraging that critical data pool in order to improve the origination of new loans and drive growth or a higher customer lifetime value.

For banks, addressing this issue and implementing it into its wider strategy is about taking note of GAFA's ability to effectively communicate and then integrate that data into every decision it's making.

As briefly mentioned earlier, collections must be treated as a form of communication and not the imposition of terms. It's a matter of using all the digital touchpoints on offer and handling the situation well. Customers who enter a bank's collections cycle should remain valued and loyal customers.

Many forward-thinking telecom and utility companies today will send emails to their customers a week before a monthly direct debit leaves their account. This way, customers have the opportunity to check whether they have sufficient funds and take action if required. Adopting this approach prevents future payment issues and is a welcome reminder put in place to improve the customer experience.

There's no reason why banks can't use a similar approach when it comes to reminding customers about loan payments, credit card payments and unarranged overdraft charges. Creating additional touchpoints to include customers who aren't in collections will show them that their bank cares about them and serve as a reminder that they're on hand to help whenever they need it.

Applying further touchpoints into a collection strategy would have been particularly useful in dealing with the coronavirus pandemic

Applying further touchpoints into a collection strategy would have been particularly useful in dealing with the coronavirus pandemic too. With millions of redundancies and working hour cutbacks, a personalised, supportive approach would have gone a long way.

Having access to the latest AI, ML and digital automation technology is one thing, but adopting the right attitude is as equally as important. Banks must look beyond the primitive approach of just maximising cash flow and build a real financial relationship with customers in order to drive loyalty, recoveries and overall returns.

If a bank can embed this philosophy into the overarching strategy and harness the knowledge provided by the latest innovations in collections, they'll prosper in the long-term.

Where the journey is taking us

Looking into the future of collections and how technology can bear fruit for early adopters

The future of collections is limitless and is already providing savvy banks with opportunities to enhance the customer journey. Digital channels, such as email, SMS and apps are enabling banks to contact their customers on the go, while leveraging AI and ML is providing key information to make smarter, data-driven decisions. Having access to this allows the strategic thinkers to work towards the overall goals of the bank, while the teams in operations can understand their customers on a deeper level, contact them at the perfect time of day and adapt the approach according to their specific needs.

Banks also have the potential to enhance the existing scoring system and make smarter risk assessments on customers

In the same light, banks can use these digital channels to create personalised communication, add extra touchpoints and send preventive payment reminders.

However, this is just the beginning of the evolution in how banks can drive results by focusing on a truly changed process that drives resolution.

Amazon is already using behavioural targeting, predictive modelling and personalisation by getting Alexa to pick up on keywords said by customers to determine what adverts they'll be most interested in. Leveraging both dynamic content and behavioural economics means banks can send reminders, contact requests and predictive payment plans to prevent collections from happening in the first place.

By operationalising all the data, banks also have the potential to enhance the existing scoring system and make smarter risk assessments on customers. Therefore, allowing banks to send predictive communications to a customer before they start experiencing payment issues. Furthermore, improved scoring can also help achieve better segmentation using value-at-risk and other metrics, and using this as the fundament for different treatments. Combining existing methodologies with the actual operational data is a powerful way to make a clear decision when determining how you want the loan book to look.

For example, using digital marketing metrics like email open rates, landing page views, email click-through rates, landing page conversions and response times allows banks to identify and react dynamically to the situation. This rapid reaction time is then critical when deciding on how to grow or adapt the strategy.

Valuable digital marketing KPIs to use in collections

Total email delivery rates

This total shows the percentage of E-Mails that have been delivered.

Email bounce rate

This total shows the percentage of emails that haven't been delivered.

Email open rates

This shows the percentage of emails that have been opened by a customer.

Email click-through rates

This shows the percentage or number of customers who have clicked a link or a call to action button on an email.

Traffic by source or channel

This metric shows where customers have come from – i.e. they've arrived on a payment landing page via email, SMS or a link included on a letter (direct visitors).

Landing page views

This figure shows how many customers visited the payment landing page.

Landing page conversions

This figure shows how many customers made a payment on the payment landing page.

Response time

This indicates how quickly it takes a customer to view an email or to make a payment.

Accurate scoring via these metrics can help banks price NPLs much more accurately and become efficient in identifying the accounts which can't be recovered and need selling.

The rise in smartphone users is set to continue influencing the way banks communicate with their customers as well. As it stands, 67% of internet users worldwide already visit the web on a mobile device and there will be 3.8 billion smartphone users around the world by 2021. This will undoubtedly lead to legacy software making way for mobile optimised payment landing pages, automated communications and rapid payment solutions.

CONCLUSION

The world we live in today is full of options thanks to technology. While GAFA threatens to challenge the very existence of retail banks with its use of cloud-based technology and advanced automation, nothing concrete has come to fruition yet.

In the meantime, the banking industry needs to think smarter when it comes to collections. This is critical operational data, that once truly integrated, can create powerful results. Time and time again, retail banks have been laggards, allowing other businesses to lead from the front.

Much like the slow adoption of blockchain technology, banks are sceptical of implementing new collection processes due to regulation. However, innovative debt collection solutions don't come with the same uncertainty as volatile cryptocurrencies like Bitcoin. Digital channels such as email and SMS are already established and can be used as a more convenient way of reaching customers.
Artificial intelligence and machine learning have been developed to a high standard to enable banks to attain critical behavioural traits and potential trends. With collections, this means banks can master the tone of the messages and send it at the right time, using the perfect channel.

> Banks that adopt future processes by harnessing AI, ML and digital automation now, have the potential to drive the overall business strategy

Modern digital marketing KPIs can provide banks with further analytics on customer behaviour and recognise potential risks before they even occur. For example, if a customer doesn't open up multiple emails, this could suggest that they're choosing to ignore and/or are experiencing financial hardship. As a result, banks can develop more personalised solutions to include nudges via further touchpoints.

Over the years, collections have developed a bad reputation for its cut-throat approach to retrieving money. In particular, banks have been guilty of jeopardising the customer relationship by repeatedly calling during inconvenient hours, prolonging the experience via call queues and sending easily misplaced, last-minute letters. In the space of a couple of weeks, customers can go from feeling valued to criminalised. The truth of the matter is customers don't suddenly become bad customers overnight. It's the fault of the bank who has abandoned their needs and failed to create a journey which involves multiple touchpoints before reaching the collections cycle.

Customers have a psychological need to agency and control, which banks need to understand and appreciate. Collections must be treated as a form of communication and not the imposition of terms. It's a case of using the behavioural insights and analytics presented by AI and leveraging the effectiveness of digital channels to handle the situation effectively. Customers who are a part of the collections cycle should be converted into loyal customers for a lifetime depending on how they are treated, driving up customer lifetime value.

Looking ahead, technology in collections will evolve. Artificial intelligence will inevitably create a more well-rounded experience, facilitating the ability to set boundaries and legal requirements, as well as the optimisation goal. Behavioural targeting is destined to continue developing, making predictive modelling and automated personalised communications a reality. It's just a case of when, not if.

The banks that adopt future processes by harnessing AI, ML and digital automation now, have the potential to drive the overall business strategy. It starts with the ability to understand their customers on a deeper level and build a complete journey that creates long-standing connections for many years to come, while directly benefiting from a better Return on Experience in their core business.

Learn more about the future of collections

If you're interested in rethinking debt collections using the latest technology and behavioural insights, get in touch with our team at Receeve today.

We've created a platform that provides the power of data-driven decision-making while handling the shifting preferences of modern customers by offering a self-service model of repayment. Not only does it improve visibility into the process for driving results, it will enable the ease of repayment to maximise cash flow and liquidity in banks, while adding more humanity in the process of collections.

Our AI-driven platform adjusts and learns best practices from your recovery implementations and continuously improves over time to incorporate the latest technological advancements.

To find out more, visit receeve.com