After the “go-go days” What next?

This is part one of a series of four articles by Phil Cotter, BIIA Staff Writer

As we move into the post-recession, post-credit crunch era, it is pertinent to take a look at what shape the global credit information players are in and how they intend to grow their businesses in the future. Over the course of four articles we will look at the strategies of the largest players Experian, Equifax, FICO, D&B, two emerging players Cortera and Creditsafe as well as some regional players such as Creditreform & Coface who intended to be game changers by launching the EASY Number. In a time of continuing uncertainty, how does each of these organisations plan to extend their services to customers and increase their returns to shareholders?

“The Go-Go Days”

In May 2010, Don Robert, CEO of Experian, made a reference to the period prior to the credit crunch as the “go-go days”. The twenty years from the late 80’s until 2008 where definitely the “go-go days” for the credit information industry and its customers in the developed western economies

So before looking forward to the future, it is worth looking back as a reminder of the factors that played a part in driving growth in the demand for credit information and analytics prior to the credit crunch. In the writer’s opinion there were three main factors contributing to an unprecedented period of growth in the credit information market from the late 1980’s until 2008:

- Increasing demand for consumer and business credit in the USA and Europe
- The deregulation of consumer and business lending leading to the industrialisation of credit granting by banks and other lenders, supported by advances in analytics and credit scoring techniques
- The advent of the Internet as a low cost means of distribution, combined with advances in computing technology that allowed large datasets to be managed cost effectively, enabled credit information and scores to be retrieved in “real time” and embedded into lenders credit granting workflow.

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Between March 1997 and July 2008 the total amount of consumer credit in the USA grew from $1.2 trillion to $2.5 trillion a growth rate of 104%. During the same period total consumer credit in the UK grew 180% from £500 billion to £1400 billion. For eleven years total consumer credit grew month on month in the USA until the credit crunch in 2008. This phenomenal growth in credit provided the foundation on which the credit information industry was built.

By contrast since reaching a peak of $2.6 trillion in July 2008, total consumer credit in the USA had declined to $2.4 trillion at the end of May 2011. Not surprising that the industry itself has found growth difficult to come by recently.

For those of us old enough to remember, getting a loan from the bank prior to the late 1980's involved a personal interview with your bank manager who made a decision based on his experience and assessment of you as an individual. From the late 1980's onwards there was a convergence of technology and market demand that led to a period of rapid innovation and development in the credit information industry. In a relatively short period of time credit information players went from providing their data by telephone or fax, via dial-up view data terminals and 3270 emulation "green screens" to embracing the Internet and the graphical user interfaces we are familiar with today.

At the same time as they embraced these developments in communication and distribution technologies, they also began to innovate in analytics and workflow solutions, developing credit scoring and software solutions that enabled their customers to automate their risk management processes. In a period of less than 10 years consumer credit granting in the USA and other markets went from a 100% manual process to 70%+ automated, straight through processing by the early 1990's.

Similar developments took place in the extension of trade credit and credit insurance. Credit management decisions, which used to be the domain of the credit manager and underwriter, are today highly automated with approximately only 20% of credit decisions being made by credit managers and underwriters.

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This industrialisation of credit granting reduced the costs of processing new credit applications significantly and allowed the lenders to satisfy the growing demand for credit in their markets.

The advent of the internet added further impetus to this innovation as it provided a means of lowering the cost of distributing information and credit scores. Where prior to the internet the cost of the technology to deliver sophisticated risk management solutions was expensive and could only be afforded by the major lending institutions, the advent of the internet allowed smaller lenders and businesses extending trade credit to their customers to have access to this technology. This provided a further stimulus for growth to the credit information market at the start of the millennium.

In this conjuncture it should be noted that consumers and businesses (borrowers) benefited from this development reflected by objective (as opposed to subjective) extension of credit, easier access and lower cost of borrowing.

"Will the near future be like the recent past?"

Credit scoring works on a fundamental principle that past behaviour is likely to predict future performance. However it is extremely difficult to apply this principle to forecasting the future for the credit information industry against a background of Eurozone Crisis, USA debt worries and the current uncertain macro-economic environment.

A BIIA survey of credit managers in 2009 revealed that balance sheets were rendered useless during the recent credit crunch because of the rapid collapse of liquidity within the supply chains.

As the world emerges from the recession of 2008/2009, for the global credit information companies, it is a very different environment from that which existed prior to the crash. As we have seen growth prior to 2008 was driven by the exponential growth in credit in western economies, despite their attempts to diversify into other vertical markets and services, credit information players remain heavily reliant on the demand for credit in their markets and particularly the extension of new credit to consumers and businesses.

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Economic recovery in developed economies is slow, particularly in Europe and the USA. In these markets Consumer and Business credit activity, through a combination of lower demand and credit policy tightening, are at significantly lower levels than pre-credit crunch. The credit boom of the early 2000s is well and truly over and this has implications for the future growth of businesses operating in these markets.

Economic growth has been far stronger in emerging markets such as Brazil, India and China and represents opportunities for future growth for credit information companies, as demand for consumer and business credit in these markets grows. However even in these markets there is a degree of uncertainty. Concerns are beginning to emerge regarding increasing consumer indebtedness and defaults in Brazil and overheating in China's economy all of which may have a negative impact on future growth prospects.

There are increasing concerns over the potential for sovereign debt default in the Eurozone. As Greece, Ireland and Portugal struggle with their debt burdens, presents a potential threat to economic recovery generally and to the future health of the banking industry in particular as they face the potential of further losses from sovereign debt default.

Increased regulation designed to prevent a further banking crisis, may create opportunities for the credit information companies as banks are required to carry out greater due diligence before extending credit to consumers and businesses. However many opportunities created by these regulatory changes could require significant investment by the credit information companies in new information assets. Information such as annual income, rental payment records and details of deposits and other assets are all required to create a more complete picture of a consumer's ability to pay. In business credit one of the biggest challenges is to improve the quality and increase the quantity of information held on SMEs, particularly the payment of trade credit.

Have the "go-go days" gone for ever or just moved next door to the emerging markets in Brazil, India and other parts of Asia Pacific and Latin America? Only time will tell.

In spite of the macro-economic environment, technology continues to advance apace, posing questions about the strategic direction of the credit information market.

Will the increasing amount of data available on the web, the development of cloud computing and the rise of mobile devices represent a threat or opportunity to the big players?

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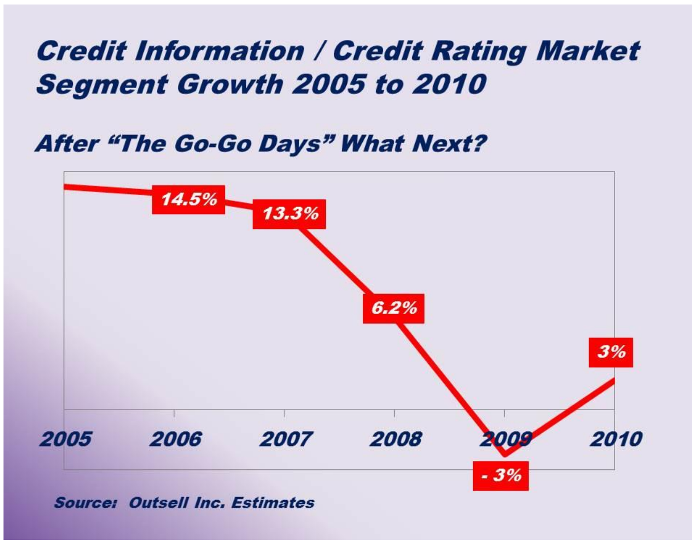

Will other players such as eBay or Alibaba, who are building extensive datasets about SMEs and their behaviours, create disruptive business models in business information? Will the trend towards business information for free continue?

Is the "big data" model where the credit information provider aggregates and stores vast quantities of information one that will stand the test of time or does the future lie in "confederated data models" and partnerships between data owners to provide solutions to the market?

These are strategic questions that the major players in the global credit information market need to be able to answer.

In the next article the focus will be on Experian, Equifax and TransUnion. It will look at how they are adapting to the current environment, the progress they are making in executing their plans and where they are focusing their attention in pursuit of growth in the future.

Until then I leave you with one final thought on the future from William Gibson an American writer***: "The future is here. It's just not widely distributed yet".***

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