Virtual Roundtable Series on COVID-19 Mitigation Efforts #16:

Deep Dive: Collections and Risk

July 9, 2020

Q&A Summary

Questions for Standard Chartered:

1. *What are some of the key things you've learned over the past few months as this crisis evolved? If back in April, you knew what you knew now, what would you change? Have you evolved in your approach to supporting clients during the pandemic*

At Standard Chartered, given our footprint, we've been able to take the lessons learned when we began to see the crisis evolve in China and Hong Kong in February, and extend those to the rest of Asia, Middle East and Africa.

One thing that neither banks, nor clients knew at the start, was the scale and intensity of this pandemic.

At the start when lockdowns started to happen, everyone expected this to last for a few weeks and the expectation would be that things would get back to normal soon. But as it started unfolding, people started realising that this will go on for longer. Initially clients thought that they were better off retaining whatever cash they had so that essential expenses could be taken care of. Now that they realise that the virus is here to stay, they are evaluating their businesses and, in some cases, starting to approach the banks for longer term solutions. We recognise that there will be clients who will need a long-term solution because even after normalcy returns, their business may not get back to where it originally was, and this reduction in overall business and profitability will impact their repayment capability.

Even the regulators initially thought that this would be a short-term problem with early guidance focused on short term relief measures. As the pandemic spread, this guidance changed and some regulators asked banks to reevaluate measures such as payment holidays and principal moratoriums and in some cases look to extend the tenor offered.

What has helped is the gradual ease of lockdowns and, for clients, some of the pessimism has given way to a bit of optimism.

We see the impact at two levels but unfortunately no one is yet clear on how this will pan out:

a. Disruption such as lockdowns – for some it's about how long they will last and for others it's about will they return to normalcy
b. Long-term impact after the initial disruption is over – what will change and what will business look like. It is still unclear how (and which) clients will recover and to what extent

Most short-term moratorium address the 'disruption'. Solutions for the 'long-term impact' will be of the nature of long-term forbearance. What some governments have also realised is that in order to help clients restart their businesses, they will need banks to lend more. They are therefore providing guarantees for all or part of the incremental lending that banks offer to clients at this time.

If we had known the full extent and impact of the pandemic sooner, we could have segmented clients based on industries and potential impact earlier and proactively given them longer term solutions that may have been more beneficial than the short-term moratorium.

2. *Can you give us insight into how SMEs are responding to reopening and economic resurgence in East Asia?*

Resurgence depends on the industry that the SME operates in. Those industries with demand destruction face an uncertain future and will need a new business model to survive. This includes physical retail stores, restaurants, and bars, which have reopened but operate under strict regulations with already diminished demand.

Industries with sustained demand will be able to bounce back much quicker, especially those that cater to basic items of consumption, such as grocery stores.

Then there are the industries that have not yet opened up e.g. Tourism/Hotels etc – the impact on these will last even longer.

Also, labour intensive industries, such as manufacturing are suffering more compared to regular traders. Similarly, international traders are affected more due to overall slowdown globally.

3. *What interventions by regulators have seemed to be the most effective?*

It is difficult to truly assess what measures have been effective now, as only time will tell. It seems that when regulators come forward to offer further lending through guarantee schemes as a means of providing liquidity, SMEs genuinely benefit.

Similarly, markets where regulators offer structured industry wide forbearance with reduced interest rates and extended tenors, typically perform better.

4. *Have you made major changes to your collections process?*

We've attempted to simplify our process, as the easier it is for clients to share their challenges with us, the easier it is to provide them solutions.

We are constantly engaging with our clients to ascertain (a) the extent of impact (b) their financial strength to continue paying contractual liabilities. We overlay this information with our knowledge of the industry type of the client to work with the client and provide them bespoke solutions.

With the safety of our collection teams and clients still of paramount importance, we have made several changes to the way we use technology to contact clients to reduce any unnecessary risk.

5. *Can you comment on how you have adjusted your credit and collections strategies and tools? Any broad portfolio line decrease actions or OCL and unused resolving lines? Have you implemented any card authorization parameter adjustments?*

As mentioned above, we are constantly engaging with our clients to understand their financial position and offer them bespoke solutions. We have simplified our processes and included fresh forbearance offerings to our clients

Questions for Lidya:

1. *What is your perspective on collections and risk based on your work in Nigeria, Poland, and the Czech Republic?*

We launched our work in Eastern Europe in the middle of the pandemic, thus it has fully shaped our work. Across most of this market, SMEs that provide essentials goods are operating at almost normal levels and we've been working to finance these businesses to help them maintain liquidity. Currently we have 0% default rates in the Czech Republic in Poland. As things start reopening, we are shifting to begin financing coffee shops and restaurants as well. In Nigeria, Lidya is working to understand shifting risk through data, which depends heavily on the availability and quality of data. This includes a focus on the business's cash flow and demand in the market, yet there is not a lot of data available. When available, bank account data has been a useful way of assessing risk through cash flow. Risk during the pandemic is also sector dependent, and thus we are focusing on industries that are fast growing or essential services. We want to be a catalyst for recovery for SMEs by providing key financing and mitigating SME financing gaps where possible.

2. *As a non-bank lender, are you obligated to stop collections as part of moratoriums?*

As a non-bank lender, we wouldn't fall under moratorium requirements. There also aren't currently moratoria in the countries we operate in. We prefer to focus on short-term cash flow funding that can help SMEs grow, especially for those that may not have access to traditional financial institutions.

3. *How granularly do you need to analyze cash flow for SMEs in order to best assess risk? Does that include looking at real time account data?*

It depends on our ability to access data, as in Nigeria there is limited API integration but in the Czech Republic and Poland we have much easier access to client data. We have clients share their account data with us and we rely on machine learning to assess the integrity and validity of the data, including data from bank statements. As many SMEs operate in high volatility markets, we rely on technology to help us consistently underwrite customers for short-term loans and evaluate ongoing risk.

4. *Can you provide more information on your operations in Nigeria?*

We operate in every state in Nigeria, however our work tends to follow GDP spread and thus we have the highest number of clients in Lagos. As our business model is based in technology and we only have one local office, we have a lower fixed cost for expanding operations, which in turn allows us to offer cheap financing. It also allows us to minimize biases in lending that may come from face-to-face interactions. Our standard product is basically a large value credit card, providing short-term cash flow financing for growing SMEs, with an average loan size of $1500. We have about 95% of customers returning for additional financing and a 0.6% default rate as of now.

5. *How do you scale your business model in communities that lack access to telecommunications structure?*

Clients can utilize our platform via phone, email, or our website. We've realized building trust is critical for clients that are used to brick and mortar banking, especially among older populations, and thus we have established multiple channels for clients to interact with staff and build trust, including phone lines. 3G is available in most of Nigeria, even in rural areas, and the introduction of cheap smartphones means many underbanked clients can easily access our services. The younger generation is well-versed in digital interfaces and they often support older clients when they begin working with us.

6. *As a completely digital group, how do you deal with collections in general?*

All of our collections are digital, and payments are run through the client's bank. We never collect in cash or disburse loans in cash. Clients are able to voluntarily connect us to their bank and clients have to agree to automatic payments or make them directly. If there is no money in the account, we understand there might be short term liquidity issues and we work with the SMEs to address it. Our clients are aware they have limited access to capital, so they do not want to ruin their opportunity to receiving funding from us.

Questions for IFC:

1. *Are you seeing similarities in regulation and collection across the IFC portfolio in Sub Saharan Africa?*

Right now we're seeing COVID-19 cases rise in Sub Saharan Africa and thus its having a greater impact on the markets. Regulators began implementing measures in March and moratoriums have broadly been a central part of the response. Three months into the pandemic, we're starting to see a second round of moratoriums as clients indicate they are unable to begin repayments right now. We likely will see this continue for some time, especially as COVID-19 spreads in Sub Saharan Africa.

In a number of countries, the government or central banks formed guarantee funds as part of their response, however SMEs are rarely receiving the benefits. While we may need more time to see the true impact, liquidity is not currently being passed on to the SMEs, making these funds less impactful. When banks do credit risk assessment, they often determine these SMEs to carry higher risk and we're seeing higher pricing of loans to SMEs, which is worrying to us at IFC. The informal sector is also not being supported by these government responses which will likely impact many markets. We want regulators to use this opportunity to reset their methods for regulating these markets in a way that decreases SME financing gaps.

2. *What are you finding about African preparation for COVID-19 and the financial impacts? How well are countries prepared? What can IFC do to help?*

It varies from country to country, as some have institutions that prepared well in advance and had strong risk management measures in place. IFC is working with clients to help them stress test their portfolios and explore and the impact COVID-19 might have on their capital and liquidity. We are also working to help financial institutions develop contingency plans. Our clients and partners are at different stages of maturity, and some lack the capabilities to handle this process and fully monitor risk on their own.

Questions for all:

1. *To what extent is cloud-based accounting software becoming central in risk assessment?*

Standard Chartered: We have our traditional underwriting models for credit underwriting. This extensively uses credit bureau data. We are also using alternative data as a means of evaluating and monitoring client risk. Cash flow data from bank statements and information obtained from tax filings serves as a good source of information for client onboarding and also for account monitoring. We are mindful that in the current environment, because of the prevalence of relief programs across the industry, the bureau status might not always give the complete picture.

Lidya: Alternative data and credit bureau data are both important, but it depends on the customers we serve. We work with some underbanked clients and thus credit bureaus do not have a lot of information to offer on them. In Nigeria, we have been focusing on credit education for SMEs so that they are aware of the importance of credit.

2. *What is the 30+ DPD & 90+ DPD Delinquency ratio SME financing is witnessing around the world?*

Standard Chartered: Delinquencies have increased across most markets but in those markets where the pandemic has been controlled and normalcy has returned, we are seeing delinquent inventories coming down to Pre COVID levels

3. *With different government directives facilitating delayed repayments for customers, how can we address rising PAR and save our portfolios from being affected by moral hazard?*

Standard Chartered: Delinquencies have increased across most markets but in those markets where the pandemic has been controlled and normalcy has returned, we are seeing delinquent inventories coming down to Pre COVID levels

However – there will be clients who will find it challenging to regain their past business volumes and profitability for the next couple of years and these clients will require longer term support as they may not be able to fulfil their contractual liabilities.

What is unclear at an individual client level is, how this will pan out. We are also mindful that because of the prevalence of relief programs across the industry, the bureau status may not give the complete picture. It is for that reason that we are constantly engaging with our clients to assess their financial position and provide them with workable solutions.

As mentioned above, we see two impacts. One is Disruption – which is short-term in nature and is addressed through the moratoriums. The other – which is slightly long-term in nature will require bespoke forbearance solutions.