

Debt sale market trends in 2010 and outlook for 2011

February 2011

The volume of debt brought to market peaked at around £9 billion in 2008. Soon after, the market contracted dramatically with volumes reducing by 50% and remaining low for some 18 months. However, in 2010 there were signs the debt sale market was starting to pick-up. With 2011 looking as if it could be the year that the debt sale market recovers to former volumes, creditors are starting to wrestle with the challenge of managing the balance sheet and generating cash while safeguarding customers' interests.

TDX examines the data from 2010 to forecast the key market drivers and predictions for debt sale in 2011.

The key questions creditors and purchasers should be asking:

- 01 Are debt sale volumes increasing?
- 02 Are prices really recovering?
- 03 Are there new purchasers entering the market?
- 04 Is there purchasing capacity for growing debt sale volumes?
- 05 Does the brokerage model still drive value?
- 06 How can the risks associated with selling be mitigated?

For further information, please contact:

Charlie Horner
Head of Debt Sale and Advisory
TDX Group

e: charlie.horner@tdxgroup.com



01 Debt sale volumes showed a modest increase in 2010, with the rate of growth set to accelerate through 2011.

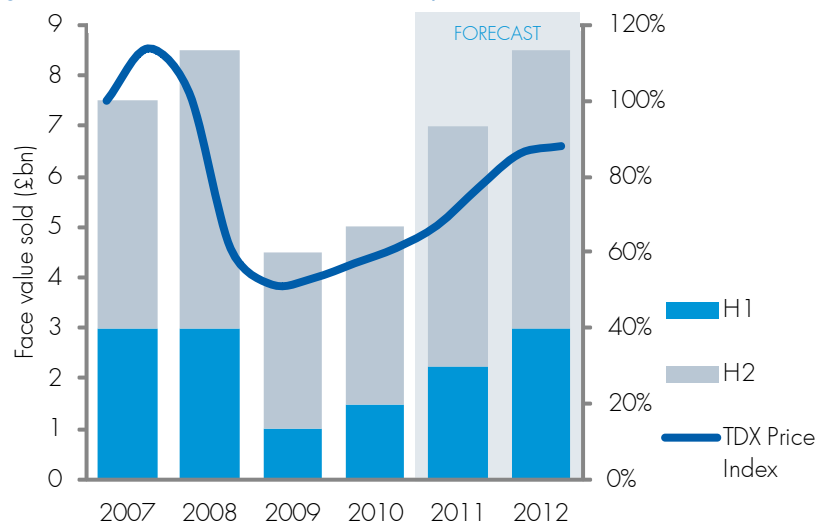
In 2010 there were signs of a market recovery which looks set to continue through 2011 and into 2012. We expect to see sale volumes in 2011 reach £7 billion in face value (40% increase compared to 2010), as creditors re-enter the market and debt purchasers' funding is replenished. Emerging market sectors, such as public sector, are also likely to add to the volume coming to market.

A reinvigoration of the market is to be welcomed, however the risk of oversupply driven by large volumes of debt coming to the market as big banks look to clear their warehouse portfolios should not be underestimated.

Poorly timed sales could be impacted by capacity issues as creditors feel under pressure to address their growing back-book or face increasing numbers of accounts edging closer to becoming statute barred. 'Fire sales' of warehouse portfolios not only result in peaks of supply but will also increase the risk of causing poor quality data causing post-sale issues, poor purchaser participation and ultimately sub-optimal prices.

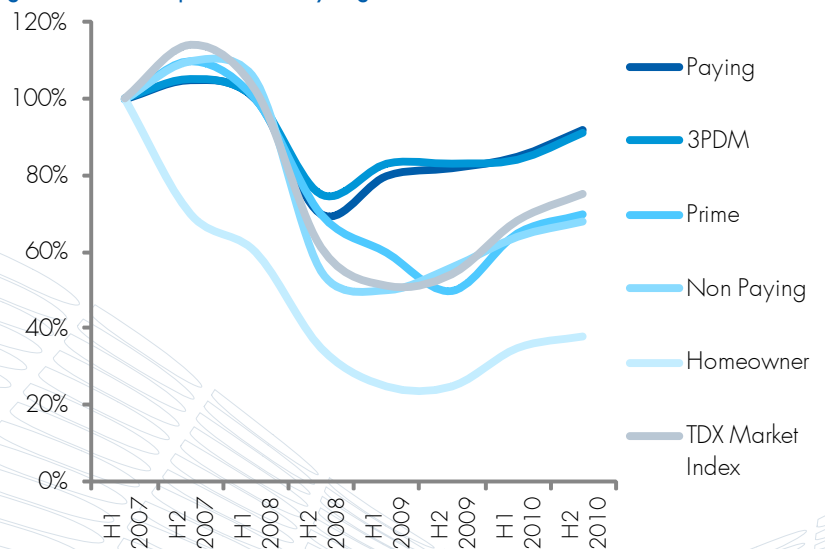
“ Having visibility of supply/demand levels to ensure the correct timing for bringing a sale to market will be key to avoid peak periods and maximise value.”

Figure 1a. Face value of debt sold and TDX price index



Source: TDX Group

Figure 1b. Market price trends by segment



Source: TDX Group

02 Pricing is set to increase by 20%, with variations at a segment level.

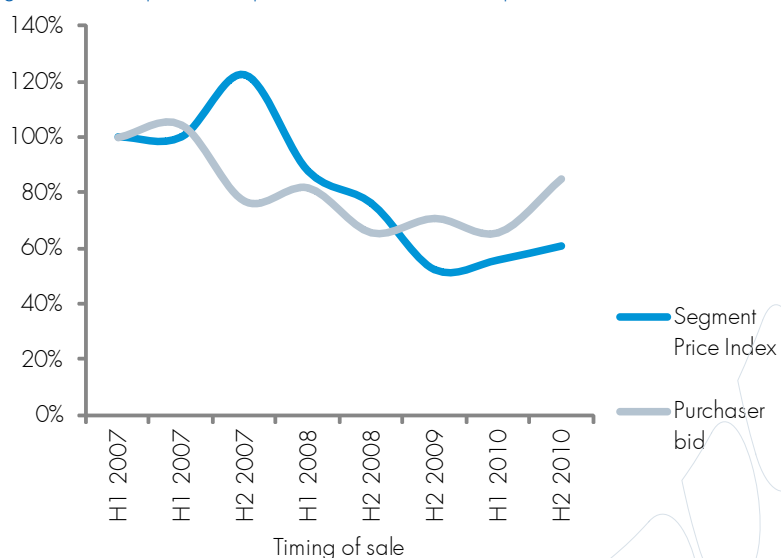
Sale prices improved in 2010 (see fig. 1b) and we expect this trend to continue through 2011 as purchasers' funding returns, their view of the economic outlook improves and opportunistic bidding reduces as supply and demand becomes more stable.

However, do not expect to see prices reach the levels seen in 2007 as purchaser confidence is yet to be fully restored. Through 2010 we have seen a wide range of bids across segments, with purchasers continuing to test the market by varying their bids to ensure they are not over-paying (see fig. 2a). We also saw significant uplifts between bidding rounds, with low first round bids reflecting purchaser uncertainty (see fig. 2b).

Now more than ever, a strong understanding of purchaser appetite at the segment level will be key to achieve prices that represent best value for the seller and are sustainable for the purchaser. Sellers with limited purchaser panels and a lack of historic pricing run the risk of failing to get the best price in a rising market.

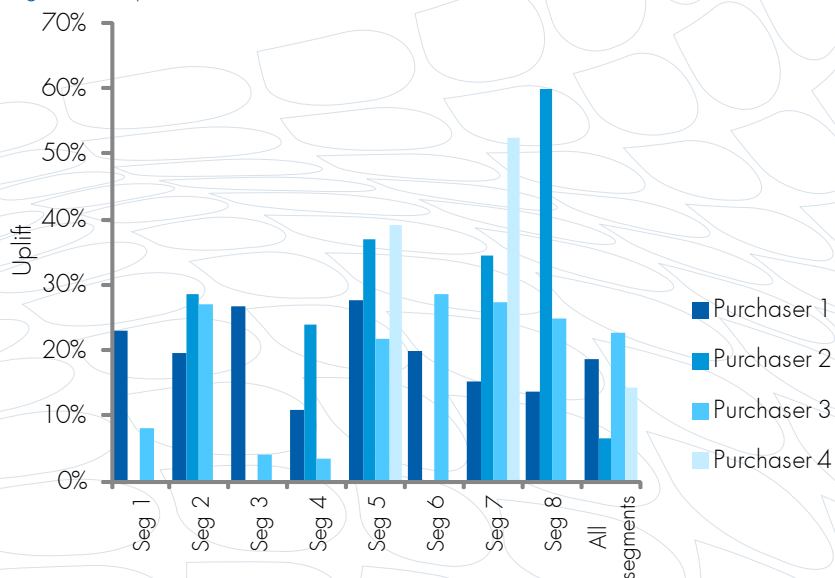
“A sustainable and efficient debt sale market can only be a reality by transacting at a fair price – this will be driven by open dialogue between creditor and purchaser, as ever, supported by healthy competition between purchasers.”

Figure 2a. Comparison of purchaser bids to market price trend



Source: TDX Group

Figure 2b. Uplift in bids between rounds (recent financial services sale)



Source: TDX Group

03 The purchaser landscape has changed.

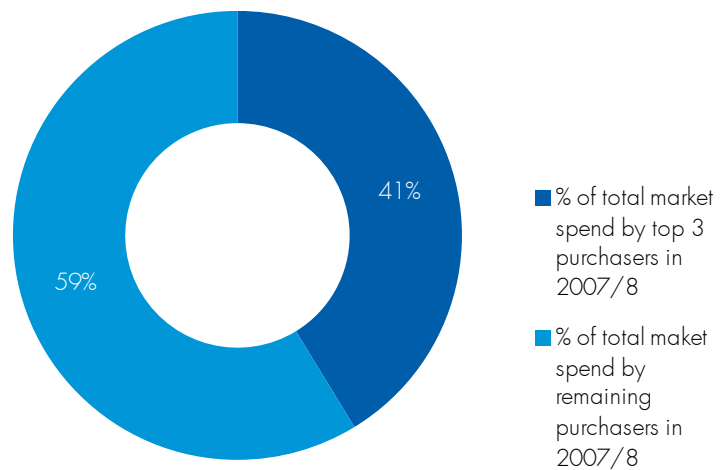
Of the purchasers active in 2008, many now have reduced funding or are not participating in the market. Turbulent market conditions through 2009 and 2010 saw some purchasers fail while others suffered significant reductions in funding lines. Several purchasers have had to prioritise internal investments above purchase as a result of greater regulatory and press scrutiny.

However, a small number of purchasers with renewed funding have established a strong position and will continue to dominate the market through 2011. There are also some new players in the market which will further stimulate recovery in 2011. We expect private equity funding to find its way to market through purchasers with servicing capabilities rather than directly or via new entrants.

Given the extent of changes, sellers who have been absent from the market, or have used direct relationships with small numbers of purchasers, may find themselves at a disadvantage when returning to the market.

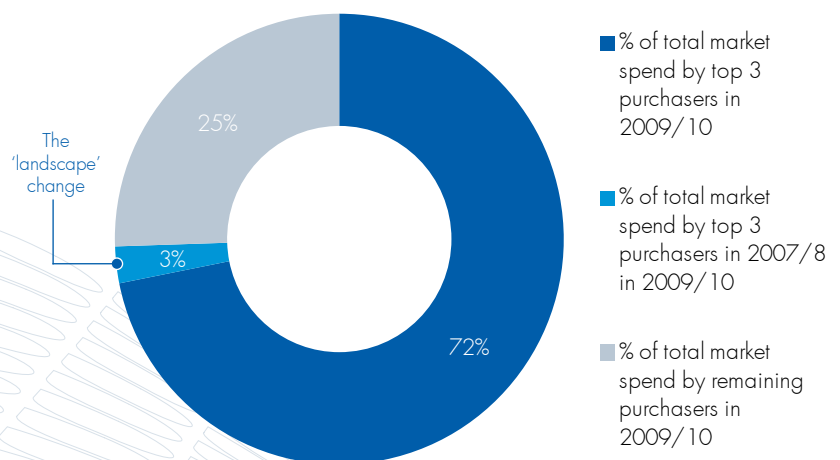
“ Consolidation has occurred in the market and we predict that 80% of spend in 2011 will be from six purchasers. However, the dominant players are as likely to change over the next 24 months as they have done in the previous 24 months.”

Figure 3a. Market shares of purchasers in 2007-8



Source: TDX Group

Figure 3b. Market shares of purchasers in 2009-10



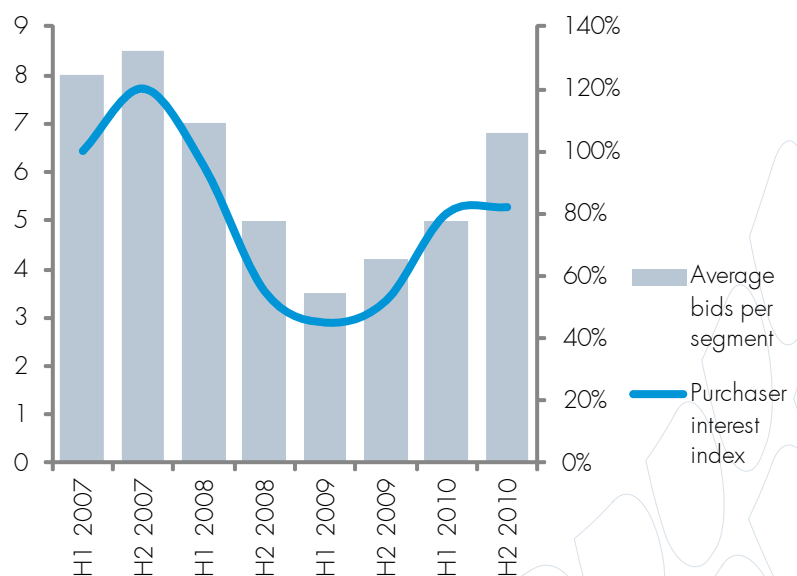
Source: TDX Group

04 Purchaser appetite has increased as the market has recovered.

There are now signs of an uplift in the number of purchasers participating in sales, the number of segments they will bid for and the number of overall bids per segment. However, levels of interest remain below historic levels as purchasers continue to focus on specific segments which are suited to their business model. As a result supply, demand and spend cycles will continue to impact the market. Successful sellers will need to consider timing, segmentation and purchasers' specific sweetspots in all sale strategies.

“ Bubbles of demand will exist and will drive price inflation in 2011 as the market continues to normalise.”

Figure 4a. Purchaser participation over time



Note: Average bids per segment = number of bids in half year/number of segments
Purchaser interest index = movement since 2007 in the average % segments available that a purchaser bids on

Source: TDX Group

05 Segmentation and the brokerage model still drives best value.

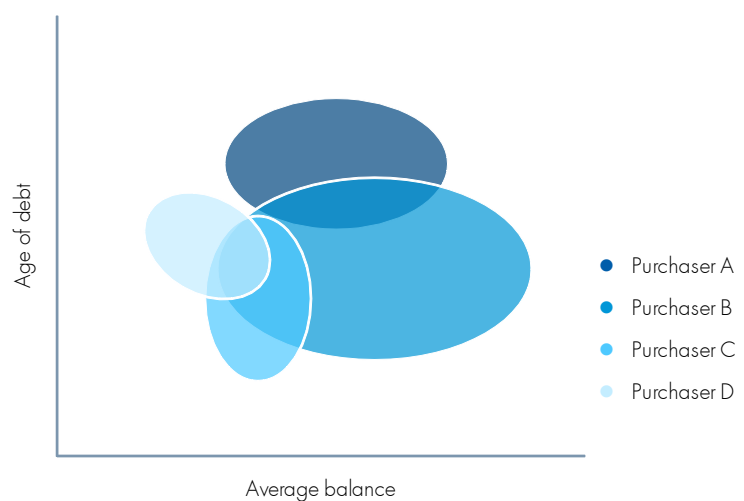
Given the reduction in the number of purchasers, some creditors have considered consolidating purchaser panels and selling at the portfolio level, questioning whether segmentation and a competitive brokerage model still has a role to play.

At TDX we saw clear evidence through our brokered sales in 2010 that segmentation and competitive bidding to a strategically selected panel of purchasers is still the most effective way to sell. It not only delivers the best price, but also ensures sellers have relationships with multiple purchasers to ensure sustainability for the longer-term.

Sellers should continue to segment to meet the market demand and involve the right purchasers to avoid portfolios being sold below best value.

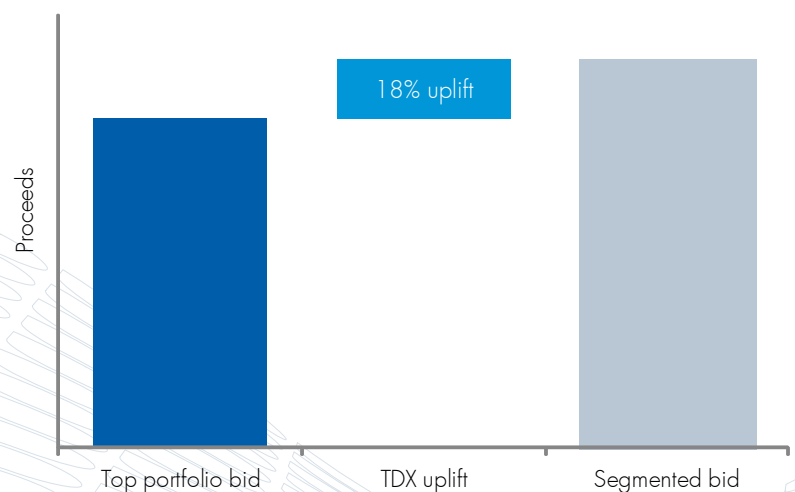
“ There are fewer purchasers and healthy purchasers are now more selective. However, segmentation is still relevant as no two purchaser valuation models are the same.”

Figure 5a. There are still gaps and overlaps between purchasers' ideal segments



Source: TDX Group

Figure 5b. Price uplift achieved through segmentation (from recent financial services sale of over £100 million in face value)



Source: TDX Group

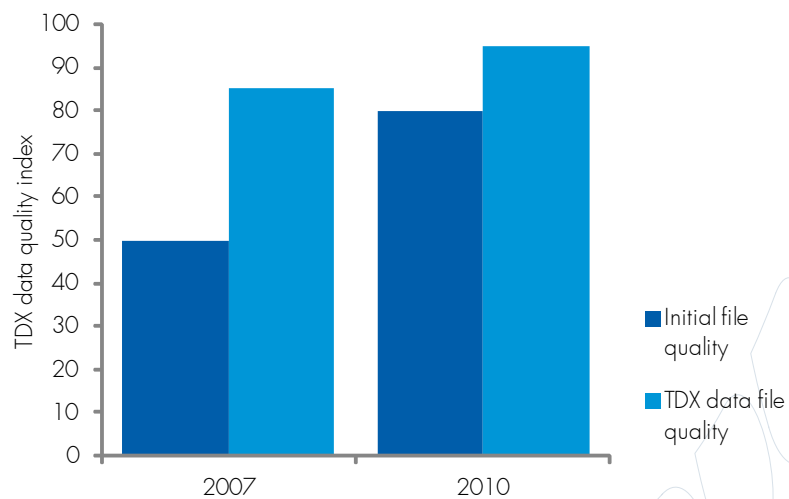
06 Risks associated with debt sale can be mitigated.

For creditors there are three main areas of risk when it comes to debt sale: financial, reputational and regulatory. Financial risks arise from uncertainty that sales will complete at the right price, that there will be significant put backs or that valuation at segment level is challenging. Regulatory and reputational risks arise from the greater industry scrutiny from regulators and press.

The most important action sellers can take to mitigate these risks is to provide high quality data. Sellers who provide good quality, clean, consistent data not only maximise price through high purchaser confidence, but also minimise post-sale risks. Data quality across the market has improved over time but there is still work to be done, especially as potential lending standards revisions may increase this focus. Increasingly we are seeing that purchasers are prepared to walk away in cases where data does not meet their requirements. For this reason, taking a data-driven approach to debt sale remains at the core of our proposition.

“All sellers and purchasers are finding themselves under greater scrutiny. The balance of best price and minimal post-sale risk will be achieved only where the data file is of highest quality.”

Figure 6a. Data quality scores



Note: Data quality index calculated from data coverage, address quality and availability of customer identifiers, payment history and default data

Source: TDX Group

Creditor checklist:
Planning for success

To ensure the best results, creditors need to include several important elements in their sale strategy:

1. Clear understanding of portfolio value at the segment level.
2. Strong analytical capability to produce high quality, clean data.
3. Relevant data enrichment and segmentation.
4. Access to a wide panel of purchasers.
5. Robust and transparent process.



Oliver Betts
Head of Client
and Product
Development

Key predictions for 2011:
A summary

1. Volumes will increase, largely driven by financial services seeking to reduce levels of warehoused debt but also by the emergence of some new markets such as public sector.
2. There will be bubbles of demand where well-funded purchasers will be competing; this will drive price recovery.
3. There will be periods of over-supply where purchaser spend and capacity will be at their limit. Sellers should be careful to avoid these periods in order to get the best level of purchaser attention.
4. Purchasers will continue to focus on their strengths and will place increasing importance on good quality data. Purchasers will be more willing to walk away from bidding where there are data concerns.
5. The winners in 2011 will be the those on both sides of the transaction who create a transparent dialogue and share relevant data to achieve best value.

New for 2011

TDX is now offering you direct access to its debt sale platform, tools and services in a series of new engagement models to enable you to build direct sustainable relationships with purchasers whilst benefiting from TDX capabilities. This offers the flexibility to incorporate specific elements of TDX expertise to enhance your existing capabilities.

Where our data comes from

The high level analysis outlined in this report is drawn from a series of data points including:

- Data from 5,000 historic bids across all debt types
- The sale of 3.7 million accounts over the past five years
- Pricing on over 200 portfolios

Launched in 2005, TDX is the UK's largest broker of non-performing debt. Through the brokerage of over £7 billion of debt spanning all market sectors, TDX has unparalleled insight into the debt sale and purchase market.

With a network of over 30 CSA member debt purchasers, experience of over 200 debt sales and a market-leading suite of tools and services, TDX has maximised value for clients, delivering over 20% of uplift in sale proceeds using its Segmented Sale™ process.

If you would like further information, detailed analysis and insight is available on request. Please contact, Charlie Horner, Head of Debt Sale and Advisory,

e: charlie.horner@tdxgroup.com
t: 0115953 1200



TDXGROUP

City Gate East
Tollhouse Hill
Nottingham
NG1 5FS

p. + 44 (0)115 953 1200
f. + 44 (0)870 460 2694
e. info@tdxgroup.com
w. www.tdxgroup.com