

The Debt Review

QUARTER 1, 2010

Quarterly debt industry newsletter brought to you by TDX Group

Recession over?

Uncertainty lies ahead for the debt industry in 2010

The last year has been a challenging one for the debt industry, confirmed by recent statistics from the Insolvency Service showing an increase of 26% in the number of debtors becoming insolvent during 2009.

Whilst the new year has already seen the official declaration of the end of the recession, it is premature to celebrate. Even if the small improvement in economic conditions is sustained over the coming months, I doubt we will see any positive effect for the debt industry in 2010.

I remain concerned because I expect to see both a further rise in the numbers struggling with their debts and, as competition increases for debt repayment, a risk to recovery levels from many creditors' debt portfolios. We look at these forecasts in more detail on page 2.

The challenges ahead for creditors will be made even more difficult with pressure to reduce costs and even delay investment plans. The delicate balance will be to meet these short-term cost priorities without destroying long-term value.

Inside we also take a look at bankruptcy, an area often overlooked and little understood, but where TDX Group is helping its clients to both reduce costs and unlock value – see pages 2 to 3.

I am also very pleased to announce the launch of TDX Group Capital Markets. This new service will inject substantial amounts of additional liquidity into the debt market during 2010 to help our clients manage and improve the returns on their non-performing assets – see page 6.

Whatever lies ahead in 2010, TDX Group will continue to work tirelessly to help its clients get the very best returns from their debt portfolios.



Mark Sanders,
Chief Executive Officer



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Bankruptcy

We explore the costs

The year ahead...

Over the last three months I have been asked for my views on what lies ahead in 2010. Forecasting is a tough business, but here is a snapshot of what I have been advising:

1. **A further 10% increase in levels of personal insolvency** – Whilst economic conditions may improve a little during 2010, I expect the numbers of debtors unable to avoid slipping into insolvency could rise to 150,000, a staggering 40% rise since the start of the economic crisis in 2007. Expect to see higher levels across the board in numbers of Individual Voluntary Arrangements (IVA), Bankruptcies and Debt Relief Orders (DRO), as well as Trust Deeds and Sequestrations in Scotland.
2. **A 10% fall in levels of debt recovery** – Greater competition amongst creditors for debt repayment at the same time as continued economic pressure on households, creditors and debt collection agencies (DCAs). The likely result will be that debt recovery levels will fall and more DCAs may fail. The winners will be the creditors who can understand where to reduce or increase investment intelligently to maximise recovery levels and who have flexible infrastructure which can react quickly to changes in the DCA industry.
3. **A 5-10% reduction in debtor contributions from IVAs and debt management plans (DMPs)** – We have already seen a reduction of 12% in debtor contributions in IVAs during 2008–9 and I fear a further reduction is likely, compounded by depressed house prices and reduced availability of additional credit to enable refinancing. Whilst insolvency practitioner fee levels may come down in real terms, they remain unchanged as a proportion of the expected final recovery by the creditor.

And finally, in the coming months many creditor organisations will be looking at how to optimise the structure of their balance sheets – perhaps considering whether to sell debt portfolios to realise some value now or whether to invest in driving liquidation over the longer-term. TDX Group is already helping a number of its clients with this complex issue – it is our assessment that this may be one of their most important decisions in the coming months.



Adrian Crean,
Managing Director,
Liquidation Businesses



Volumes and losses continue to rise

The latest data released by the Insolvency Service confirmed the number of individuals made bankrupt during 2009 was 74,670, a rise of 11% on the previous year or 28%, if you include Debt Relief Orders (DRO), a bankruptcy style insolvency for those with debts of less than £15,000, no assets and minimal surplus income (see figure 1).

The challenging economic conditions are clearly continuing to have an effect on some peoples' ability to remain solvent – although higher levels of general unemployment does not appear to be a main factor in bankruptcy as the Insolvency Service data shows the proportion of bankrupts who continue to be in paid employment has remained fairly static at around 60%.

Operational costs dwarf potential returns

Administering bankruptcy accounts can be complex and costly – creating an overhead for creditors which is very real but often unseen. Unfortunately much of the bankruptcy process still involves paper-based interactions between creditor, Official Receiver and Trustees.

A recent study by TDX Group estimates the cost of servicing each bankrupt account is £55 over its lifetime, covering post-handling, record keeping, data and systems infrastructure, account management activities, outbound responses, and facilities and storage (see figure 2). Further costs are incurred for supporting infrastructure, a potential drain on future investment priorities incurring costs for maintenance and changes to processes, systems and staff training.

TDX Group estimates the combined cost to creditor organisations to be in excess of £50 million per annum, dwarfing dividend returns received by creditors.

assets – are they a liability?

and risks for creditors administering bankrupt accounts

Some creditors try to mitigate the impact of these costs by handing-over responsibility of certain aspects of the bankruptcy process to a nominated trustee firm – who in turn will seek to recoup their own costs by being appointed as Trustee on selected cases. But without clear service guarantees these arrangements may not maximise value to creditors.

In an effort to reduce the cost burden, creditors may unwittingly relinquish some or all of their rights in the bankruptcy. TDX Group research suggest two thirds of creditors fail to exercise their right to vote at Meeting of Creditors and creditors who fail to submit valid Proof of Debt documentation, needed to qualify for any prospective dividends, can even be disqualified from receiving any distribution.

Beware the hidden risks

It is common for creditors to assume bankruptcy accounts are of little value and therefore require little attention – an approach TDX Group advises its clients can be fraught with danger.

Many creditor organisations fail to identify bankruptcy accounts in a timely manner and do not regularly screen their customer base. Consequently creditor records can be inadequate – often leading to mistakes or a failure to properly engage in the bankruptcy process.

This may create additional financial and compliance risks:

1. Failing to close or restrict the debtor's accounts potentially allowing the debt balance to expand after bankruptcy declaration;
2. Failing to maintain adequate customer data, electronic and physical records;
3. Failing to halt further collection activity and adhere to Treating Customers Fairly (TCF) principles. TDX Group estimates up to 3% of accounts with debt collection agencies may already be subject to bankruptcy proceedings;

4. Failing to adequately support the Official Receiver or appointed trustee in their statutory duty to investigate the affairs of the bankrupt.

Toxic outlook ahead

Bankruptcy volumes will remain high – the numbers of households struggling with their debts and who go on to become insolvent will lag any improvement in the economic climate. Reforms are also being proposed to make bankruptcy easier, where an individual can apply for bankruptcy without the need to go through the courts. The long-term impact of the DRO remains unknown but volumes have risen every quarter since its introduction earlier in 2009.

Returns will likely remain low and difficult to predict – the last two years have seen a halving in the number of bankruptcy

cases with asset realisations, largely as a consequence of the fall in house prices. As a result returns to creditors have fallen substantially and are likely to remain depressed and uncertain through to 2012.



Carlos Osorio, Head of Bankruptcy at TDX Group (pictured left), said "Creditors appear to have little to gain and much to lose by administering their bankrupt accounts. With no ongoing client relationship to maintain, creditors are increasingly considering disposing of their bankruptcy assets as a means of extracting some immediate value, removing cost and mitigating risk".

This article is an extract from a TDX Group briefing note.

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Figure 1. Number of individuals made bankrupt Q4 2007 to Q4 2009

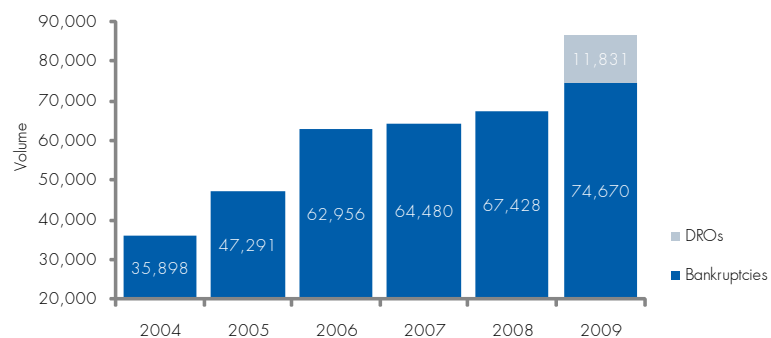
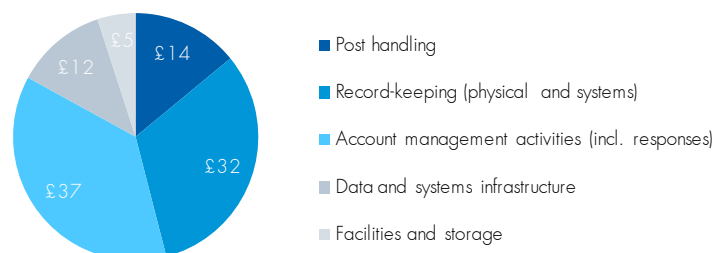


Figure 2. Costs per account



Debt industry news:

Our round-up of some of the headlines from the past three months

CONSUMER NEWS

Credit Card spending continues to rise

Figures published by The Payment Council¹ in December 2009 reveal an increase in credit card spending in the UK. The number of debit and credit card transactions rose by 6.9% in the third quarter of 2009. According to these figures, gross credit card lending was 7.5% lower than the same period in 2008. Repayments fell by 4.7% reflecting the lower spending levels. According to financial claims management company Cartel Client Review, more than £21 billion of the UK's credit card debt is covered by unenforceable credit agreements and could be written off.

Note:

1. The Payments Council is an independent body which ensures that UK payment systems and services meet the need of users, payment service providers and the wider economy

Sources:

- Plastic card spending on the rise, 01.12.2009, CreditToday
- £21bn of credit card debt "unenforceable", 25.09.2009, CreditToday

Britons to prioritise financial planning in the New Year

Research conducted by Equifax and published in December 2009 has found that consumers from London and the South East were more optimistic about their finances in 2010 than anywhere else in the country. However consumers in the same region were amongst the most worried about job security, which has led to Britons focussing on financial planning in the new year.

The trigger for this financial prudence is the expectation of increasing monthly outgoings not supported by an increase in income, with 58% of respondents keeping managing finances as a priority in 2010.

Source:

- Londoners The Most Hopeful For A Pay Rise In 2010 But Also Amongst The Most Worried About Job Security, 08.12.2009, Creditman

DEBT INDUSTRY NEWS

Over a third of debt collectors face financial difficulty into 2010

According to analysis conducted by Plimsoll, the global financial crisis has adversely affected UK Debt Collection Agencies (DCAs), with over 115 DCAs ending 2009 in financial difficulty. This delicate financial situation means that takeover activity in the industry is expected to gain momentum in 2010.

The financial ill-health of DCAs and consumers alike is cause for concern as collectors are more likely to take aggressive steps to settle debts, or negotiate unfeasible repayment plans. The impetus for improving the situation is now on the regulators and trade associations, who are in the process of increasing their visibility in and control over the sector.

Sources:

- Nearly 38% of debt collectors facing financial difficulty, 11.11.2009, Debt Management Today
- Collections performance stabilises in 2009, 18.09.2009, CreditToday

LEGISLATION NEWS

Government seeks opinion on personal debt management schemes

The UK Government, in its efforts to aid vulnerable consumers through the current economic downturn, has published a consultation paper, 'Debt Management Schemes', to help deliver effective and balanced solutions for both debtors and creditors.

The report is due to be published in 2010 and will identify practices harming customers and reasons for non-compliance as well as suggesting appropriate enforcement actions.

Source:

- Government seeks views on personal debt management schemes, 20.09.2009, Creditman

TDX Group commentary:

“Through our experience with our Debt Management Exchange (DMX) in 2009, we continue to believe there is an urgent need for better supervision within the sector.

Current practices don't always drive the appropriate treatment of debt for customers. Furthermore operational challenges due to a lack of standardisation often mean a high cost burden for creditors and a poor experience for their customers.”

UK Government proposes reforms to bankruptcy procedures

The Insolvency Service has published a consultation document proposing a number of reforms to existing bankruptcy procedures to make the process quicker and easier. The proposals include allowing individuals to submit bankruptcy applications online or through the post, rather than in court.

EuroDebt supported the initiative and stated that these reforms would be an important development for individuals facing serious financial difficulties, reducing the time between bankruptcy petitions being submitted and bankruptcy orders being issued, as well as reducing costs.

However simplification of the bankruptcy procedure has also attracted criticism from those who argue that, with a reduced stigma attached to bankruptcy, it may be seen as the easy option compared with first attempting to pay their debts.

Individual Voluntary Arrangements (IVA) Data bank

TDX Group commentary:

“DCAs are under significant pressure as creditors seek to pay lower commissions. Creditors need to be prepared for more industry change and ensure flexibility exists to redirect placement if a chosen DCA fails.

At a time of intense focus on the rights of consumers, creditors need to ensure their agencies are delivering on agreed Treating Customers Fairly (TCF) objectives.”

Sources:

- EuroDebt comments on the Insolvency Service proposals for bankruptcy reform, 18.11.2009, Creditman
- Proposed reforms to bankruptcy procedures will help people in debt and reduce court costs, 13.11.2009, Creditman
- Bankruptcy is Too Easy, 19.12.2009, Creditman

TDX Group commentary:

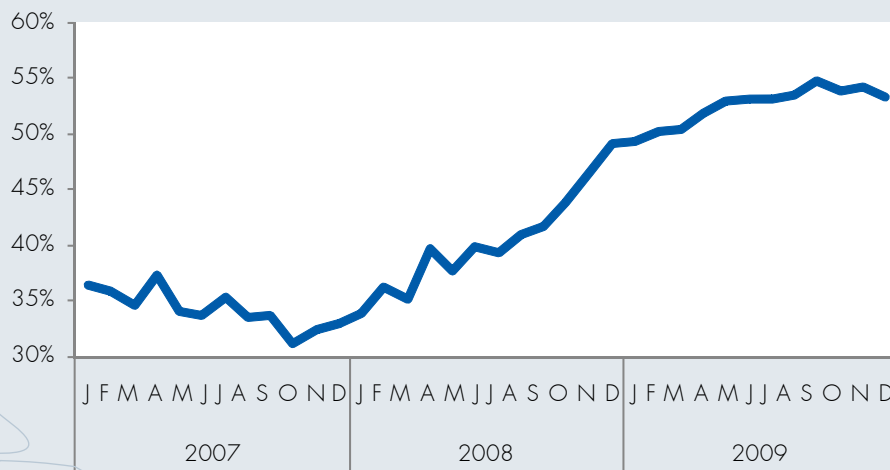
“Creditors will need to watch out for continued high levels of bankruptcy – see our article on pages 2 to 3.”

IVA statistics	Dec 2007	Dec 2008	Dec 2009
IVA cases (last 12 months)	42,165	39,116	47,641
Total unsecured debt in an IVA	£43,399	£39,964	£41,859
Debtor salary	£22,507	£25,241	£25,137
Debtor income vs. expenditure	1.23	1.19	1.16
Debtor monthly payment (proposed*)	£358	£324	£309
Debtor monthly payment (activated*)	£368	£333	£323
% cases with homeowner	32.2%	46.6%	54.4%
% cases with higher rate tax payer	9.8%	15.1%	14.3%
% cases with equity release option	18.8%	20.7%	18.4%
IP fees (proposed*)	£6,708	£6,936	£6,858
IP fees as % of dividend (proposed*)	41%	49%	49%
IP fees (activated*)	£6,088	£5,583	£5,553
IP fees as % of dividend (activated*)	33%	33%	33%
Dividend (proposed*)	37.6p	35.6p	33.4p
Dividend (activated*)	43.1p	42.3p	40.0p

*Proposed: Initial terms proposed

*Activated: Final terms agreed

Levels of home ownership on proposed IVAs



2009 saw the number of IVAs activated increase by 22%, with an ever-increasing number of homeowners seeking protection from creditors within the IVA. As a result, it will be important for creditors to monitor equity release to protect dividend returns.

Matt Trueman
Head of The Insolvency Exchange (TIX)

How are you prepared for 2010?

This five-minute checklist could help you improve your debt recovery results for the next 12 months

Please tick



- 1 Do you **segment** your debt portfolio?
Make sure your segmentation approach is robust, updated regularly and ideally also uses external data sources.
- 2 Do you **append external data sources** to improve the quality of your customer information?
Best practice is to add information from three to four different data sources.
- 3 Is the **amount of debt** you place with each debt collection agency meaningful?
Being a significant client for a DCA (10–15% of their revenue) will help ensure your debt gets the attention it deserves.
- 4 Do you get good quality weekly **performance statistics**?
Ensure it does not simply report on what has happened but also gives insight into why and what to do next.
- 5 Have you conducted any **call-listening** on your collectors?
Regular checks are imperative not only to confirm TCF compliance but also to improve future collections activity.
- 6 Are you confident you know what **good performance** looks like?
Do not be guided by your own historic performance – ensure you get to see latest industry benchmarking, ideally at segment level.
- 7 Do you proactively **“recycle”** your debt?
Do not wait six months to recall debts - ensure your systems actively monitor and re-allocate, all the while keeping reconciled.
- 8 Have you **cut costs** by squeezing debt collection agency commissions?
Simply cutting cost is risky if you are not absolutely sure about impact it may have on returns for each segment.
- 9 Do you ever **pay more to get more**?
Regular testing will help ensure commission levels are set for each segment to get you the very best returns.
- 10 Have you set aside enough to **invest in your recoveries infrastructure** in 2010?
You will struggle to keep up with the competition if you do not have a strong, flexible and data-rich platform.



If you want to know more about improving the amount of debt you collect or how to best manage debt collection agencies, then contact **Jason Incles**, TDx Group's Head of Recoveries Management. By the end of 2010 TDx Group will manage three million accounts, representing £1.5 billion of debt placed with over 40 debt collection agencies. This year TDx Group will recover £70 million on behalf of its growing number of clients.

Company news

A new Capital Markets division

TDX Group research has shown that many investors (investment banks, hedge funds, private equity firms) would like to access the non-performing loan (NPL) market, but have insufficient experience and data. In addition, many investors would like to access the market without having to invest in a purchaser and the corresponding infrastructure.

With a view to addressing these needs, TDX Group has created a new Capital Markets division to provide new funders with access to the NPL market and a platform on which to service their accounts.

The major benefits of this new function to our clients are:

- Access to a diverse set of funders with a wide range of investment requirements;
- Seamless and speedy transfer of ownership for assets on Recoveries Management (RM) and The Insolvency Exchange (TIX) servicing platforms to meet short-term call requirements (service-to-sale proposition);
- Dedicated post-sale support team;
- Established, fully licensed purchasing vehicle.

For further information, please contact **Stuart Bungay**, Head of Capital Markets
e: stuart.bungay@tdxgroup.com

TDX GROUP IN THE NEWS

Standard & Poor's announces 'above average' ranking on TDX Group as a master servicer of consumer finance

Standard & Poor's (S&P) has improved its master servicer ranking of TDX Group's Recovery Management division from average to above average. This reflects S&P's recognition of TDX Group's management team, its thorough auditing processes of its debt collection agency (DCA) servicers and its award-winning recoveries management information system (RMIS). This comes in a year which has seen a fourfold increase in debt portfolios under management, offering above average returns through a network of over 40 DCAs.

The full press release can be found at: www.tdxgroup.com/standardandpoors.html

Management re-organisation

With the launch of TDX Capital Markets (see left), Mark Onyett (founder and CEO) will be focussing on this new initiative and a number of other new services which are in development.

As a result, we are pleased to announce that Mark Sanders has assumed the role of Chief Executive Officer for our core business operations, including Recoveries Management, The Insolvency Exchange (TIX) and Asset Sale brokerage.

British Gas Residential: new business win

British Gas (BG) has embarked on a four-year relationship with TDX Group, which will see TDX Group manage BG's late final debts using BG's own internal customer recovery treatments for its residential customers.

A major part of TDX Group's role will be to rigorously select, manage and oversee the activities of all DCAs and ensure that BG's residential customers in recoveries continue to be treated in line with best industry practices and with the utmost dignity, respect and fairness.

The new format newsletter

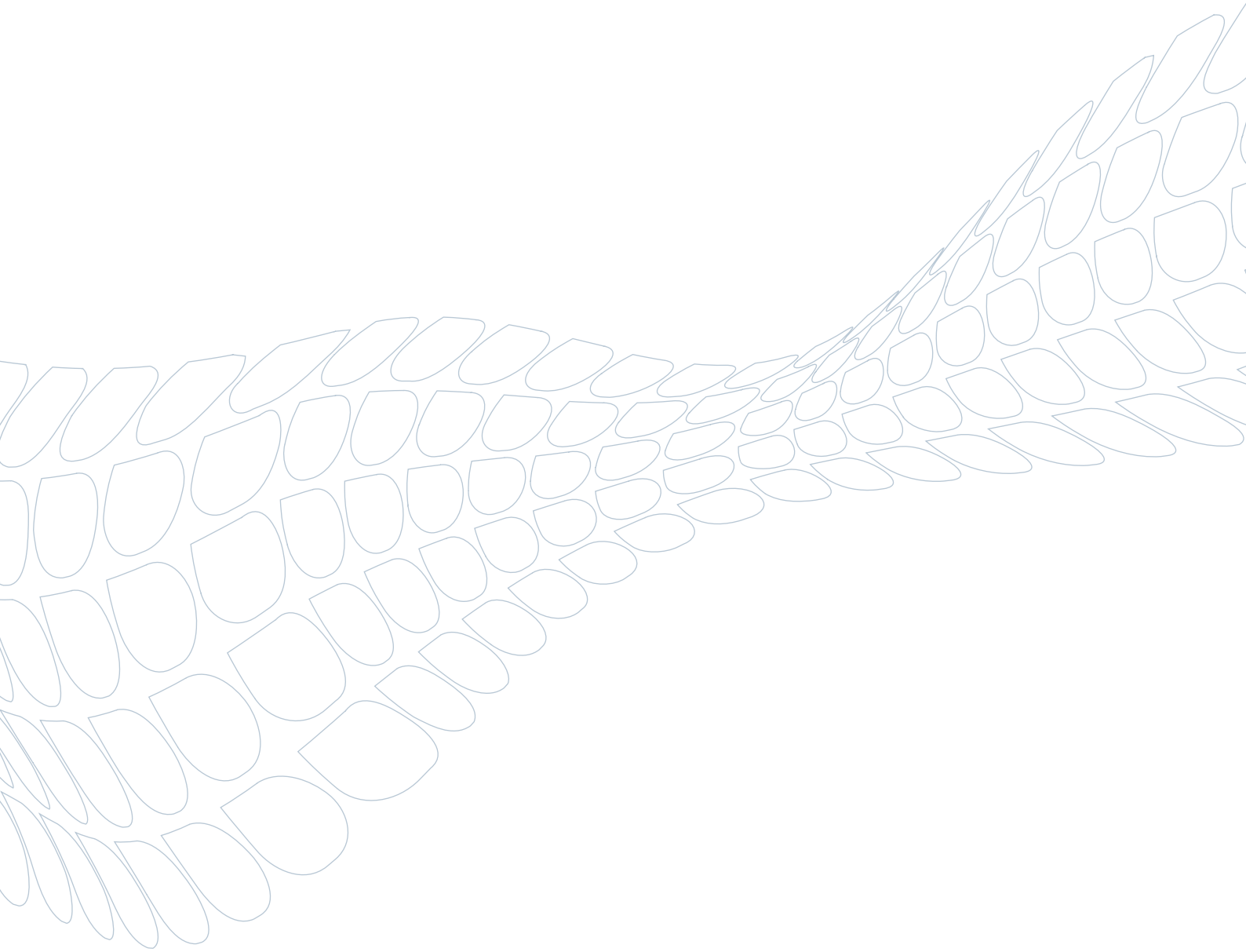
This is the first edition of the new format "Debt Review"; replacing the previous "Debt Tracker".

If you have any questions or comments on The Debt Review, or have suggestions on how it could be improved to be more useful to you,

please do not hesitate to contact us.

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