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Lending in the Instant Economy

Hear how leaders from global lenders are tackling the biggest regulatory and technological changes and making payments their unfair advantage.

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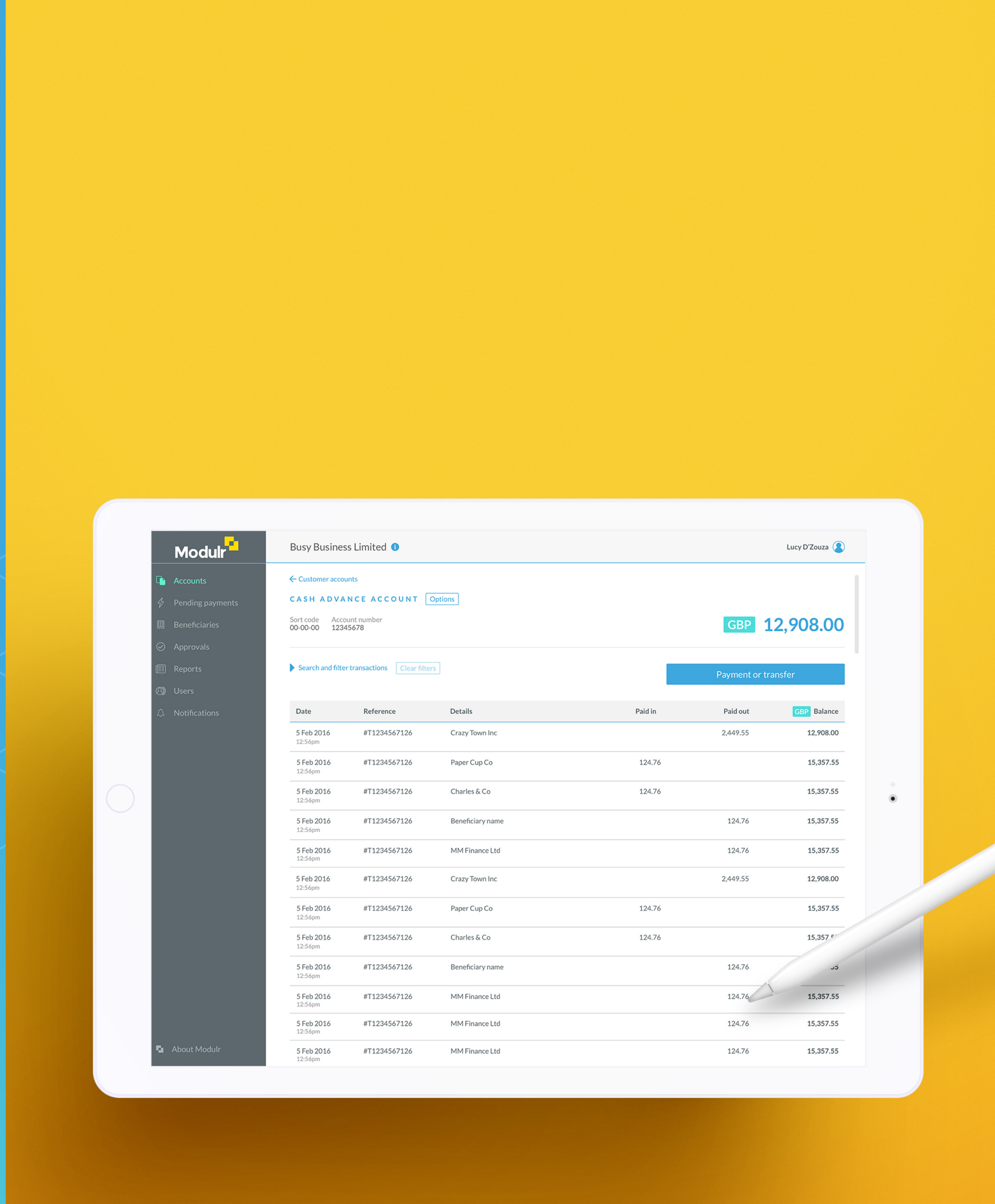
Foreword:
a view from the industry frontline



Businesses and consumers now expect to consume services instantly, and that now applies to financial services and lending.

As a result, the lending landscape is evolving rapidly. Banks and financial institutions now face competition from new market entrants and challenger banks, including peer to peer (P2P) and peer to business (P2B) lenders. To meet changing customer expectations, not just for instant loan approval but also instant loan disbursements, lenders are innovating back office processes.

In the new Instant Economy, real-time, automated services are replacing manual processes surrounding loan disbursements and borrower repayments, while innovative digital payment platforms are eliminating the reliance on legacy banking infrastructure.

The Instant Economy describes a collection of forward-thinking businesses that take advantage of scalable infrastructure to deliver new services at speed and efficiently.

Open access to banking transaction data via APIs is enabling lenders to transform their service offerings. The Instant Economy levels the playing field, enabling lenders to support businesses of all sizes with convenient and reliable lending facilities that help them meet customer demands and give them a competitive advantage.

Modulr works with lenders to make their lending process more efficient and competitive. Our digital payment platform replaces traditional bank accounts allowing lenders to offer instant loans and more convenient, always-on repayment facilities.

We carried out a survey of chief executives, chief information officers and chief product officers from a range of lending businesses to get their views on their current challenges and opportunities. This eBook aims to distil these findings and combine them with our deep insight into the lending sector, offering a practical guide to lending in the age of the Instant Economy.

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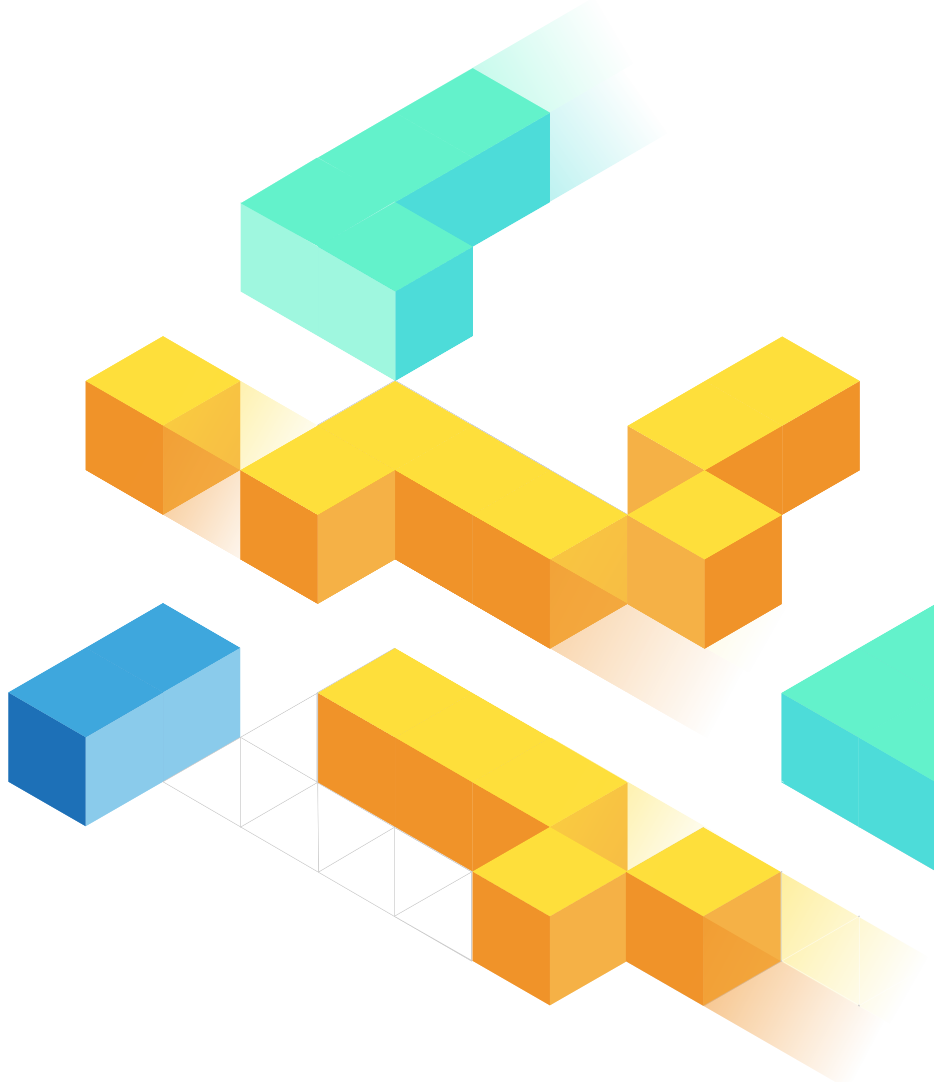
Innovation:
the perfect blend of regulation, technology and customer demand

Innovation: the perfect blend of regulation, technology and customer demand

The push of regulatory disruption, the pull of customer demand and technological developments are driving innovation in lending. Amid these conditions, new entrant FinTechs are able to push through transformation in the lending sector, resulting in ground-breaking business models. And those business models are threatening the status quo as, according to Experian, the lending market has seen a significant shift from traditional financial institutions to fintech companies, which provide alternative finance solutions to borrowers[1].

Recent regulation, including GDPR and PSD2, has driven change in the financial services by freeing up access to banking data within a solid consent framework. These regulatory changes have ushered in the age of Open Banking where banks must now, with consent, share data on customers. This offers lenders increased visibility into potential borrowers' financial history in the credit-scoring and pre-approval process, providing, of course, the lenders have the API capability to receive such data.



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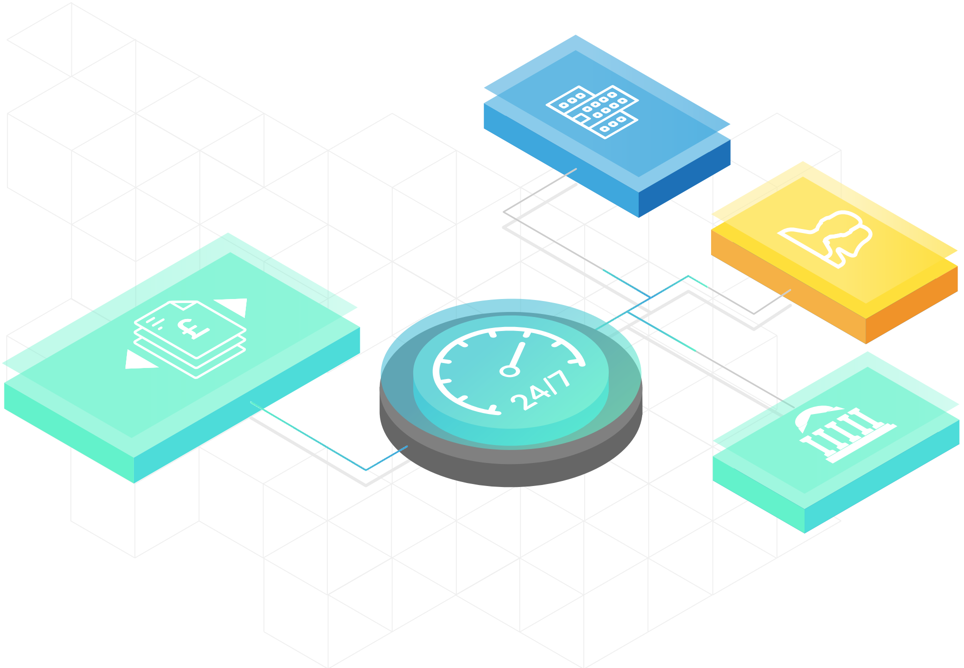

Technology advancements, such as the prevalence of APIs, have combined with regulatory drivers for change to offer improved borrower experiences. FinTechs offering customer-friendly digital lending platforms are emerging as key players in the lending sector. Kyle Macdonald at Financial Cloud, notes, "You'll find lending organisations now go beyond financial services. Really, they're becoming more like technology companies. We found that people welcome user-friendly technology. They don't want to use legacy technology."

With permission, lenders can use Open Banking to access more customer banking data than ever before and more quickly than ever before. This is enabling fast loan decisions and efficient and customer-friendly loan disbursement, repayment and payment resolution processes. Now lenders do not just use credit scores to assess borrower suitability for loans – they can see actual banking data and the real-world spending patterns of the applicant before deciding whether or not to grant a loan.

Legacy payment processes, where borrowers would wait days for manually processed loan disbursements, are being replaced by real-time payments. Previously, although consumers and businesses could apply for loans online, traditional lenders often had to resort to manually keying in account numbers to disburse loans. The latest digital platforms integrate with the lender's platform and, as soon as the loan is approved, the funds are disbursed immediately. As funds arrive in the borrower's account, the borrower receives an automatic notification. This all happens in real-time and 24/7.

The emergence of the Instant Economy comprising forward-thinking lenders – taking advantage of scalable infrastructure to provide new services in real time – is having a visible impact on small business borrowers. Damian Brychcy, Chief Operating Officer at Capital On Tap, explains:

"A business which runs a corner store and needs £5,000 to stock up before Christmas doesn't want to go through a four-week process with a traditional lending institution. And so, they turn to alternative lenders who can provide that loan much quicker, with simplicity and ease. Many alternative lenders are doing it in less than 48 hours and some alternative lenders like Capital on Tap are even doing it in minutes. This transformation in speed and convenience has been the biggest change in the market over the past five years."

This is just a glimpse of the wider picture. While the consumer lending market is seeing rapid change, the full impact on the business lending market has yet to be felt. Alex Kousiopoulos, Global Product Director at Bibby Financial Services, says: "I don't think that the industry has settled on a certain direction. There are definitely a lot of opportunities due to new regulations as well as the deployment of technological standards. There's the potential for new business models, which we haven't truly seen so far. We've only seen 1% of the innovation that could come out of Open Banking. Until now, most efforts have been focused on the consumer side of things. There is a lot of potential in B2B."

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The four pillars of success in the Instant Economy

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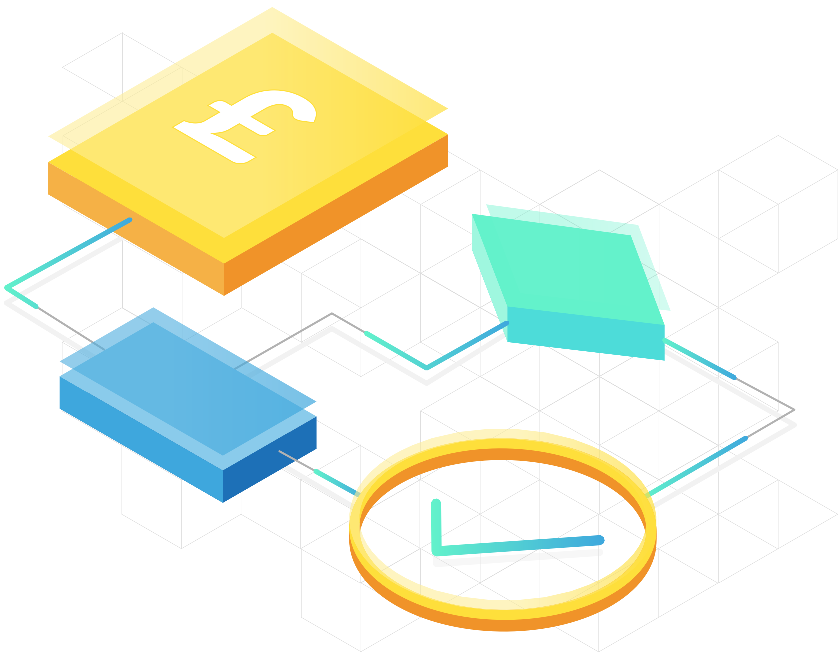


“The worst thing when you walk into a car showroom is when you’re told you can’t have your car for a couple of months. You want to walk out there with the car there and then. People just expect that now from financial institutions. It’s just that whole instant gratification piece, it’s just snowballed. So, lenders now have to keep up with it.”

Kyle Macdonald,
Chief Executive Officer at Financial Cloud.

To compete in the fast-changing lending marketplace, lenders must focus on four critical success factors.

1. Real-time Payments

Consumers and businesses are used to receiving service at the point of transaction. They don’t want to wait for banks to open and loan payments to be made. Lenders who are able to offer real-time payments will be able to profit from this consumer and business expectation. Kyle Macdonald, Chief Executive Officer at Financial Cloud, notes, “People will go for convenience over cost. Lenders who are able to do instant pay-outs will be able to charge higher interest rates as a result. We’ve already seen a very slick user experience and a slick customer journey. People are willing to pay a premium for that.”

Lenders are progressing from manual disbursement processes to real time API-driven loan disbursement. At Capital On Tap, Damian Brychcy says: “If you’re a small business in the UK, our credit decision engine can give you a credit limit within ten seconds and you can have access to that funding within ten minutes into your bank account, as fast as the Faster Payments network will let it go. We’ve had customers that Googled ‘business funding’ and had £15,000 in their bank account within ten minutes. It’s something we’ve been doing for years and I think other people are catching up to that.”

2. Back Office Automation

Innovation has also come in the back office. Back office payments processing has until recently been largely manual. Automation has brought efficiency savings and improvements in customer service. Many traditional lenders disburse funds through a process of batch files. In a single day, they might have 100 customers who sign up for a loan. They will capture information about all the loan agreements and send them in one spreadsheet to the bank at the end of the day. Automating this process is key to enabling real-time disbursement and repayment reconciliation.

Collection and reconciliation of loan account holder repayments has been ripe for automation. Legacy systems make it difficult to allow borrowers to make one-off repayments. This often involves the borrower logging into their own bank account, inputting account details for the lender and manually sending repayments that way. As well as the scope for error in inputting these account details, the lender also faces the issue of potentially many hundreds of borrowers depositing money into one account, making it difficult to identify which borrower is which, based on the repayment information.

All this puts pressure on the lender's customer service department, with borrowers phoning in to complain that their repayment hasn't been credited. This is an expensive and unnecessary overhead for the inbound call centre. It is also difficult for the lender to calculate any repayment amount or term adjustments, if information about the repayment date is unclear.

The latest digital lending platforms enhance inbound payment reconciliation by allowing the lender to open an account for each borrower, enabling borrowers to repay money directly into their own individual account. Repayments are automatically reconciled with the right account for the loan, cutting out any manual processing.

John Battersby, Head of Communications and Policy at RateSetter, points out, "Of course, the thing that matters overall is the efficiency of the whole lending process, the whole network. The efficiency of the funding, efficiency of processing, the efficiency of delivering payments, all those things are really important. And that efficiency can be reflected in a more competitive price to the end user. So, the borrower gets a better deal. And getting all those things right will result in a much better delivery and much better alignment between the industry and the customer's needs."

Automating routine processes delivers a win-win outcome. The resulting savings may be passed to the customer in the form of competitive interest rates and other perks, while making the business more competitive.

"I see significant innovation. I know cases where back office costs have been eliminated by 78 to 80% by deploying new technologies or allocating income payments and automating outbound ones. Absolutely, there's lots of disruption and there's lots of potential. And it's already happening. It's not a thing for the future."

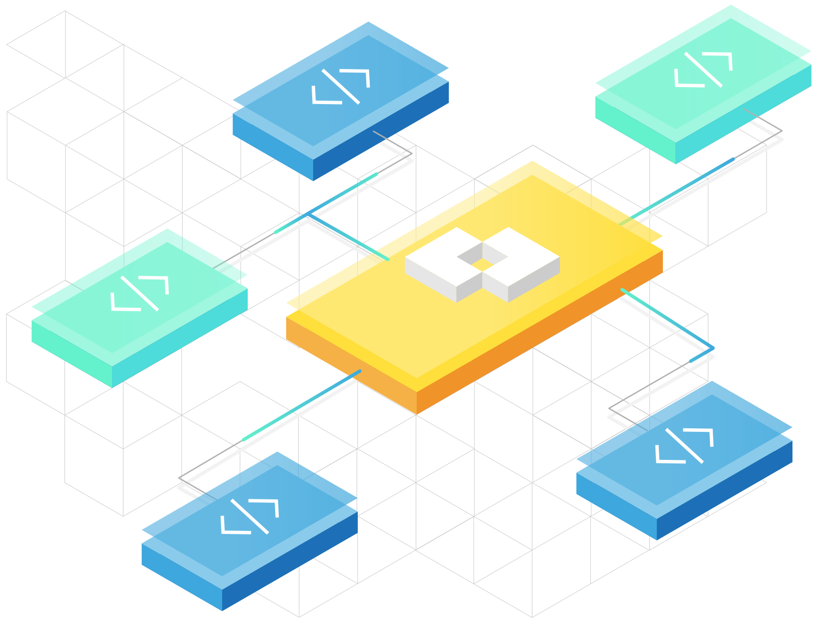
Alex Kousiopoulos,
Global Product Director, Bibby Financial Services

3. Customer Experience

As the payments landscape continues to evolve at an accelerating pace, Gareth Wilson, MD Global Payments at Accenture, predicts that the consumer experience for payments will become a battleground for lenders[2]. With the advent of Open Banking, lenders can use customer data to get a better picture of the customer's finance than that offered by the traditional credit score.

Borrowers want loans 24/7 all year round. They want a choice of repayment options. Lenders need to offer a range of loan disbursement and collection choices for borrowers, and many are doing this by accessing various payment options through a single API. At the same time, automating routine processes frees up employees to deliver more responsive customer service, adding the human touch that wins and retains customers.

Steve Robson, Founding Shareholder and Managing Director at **CapitalStackers**, says, "I was brought up in an industry where a banking manager knew his clients, as opposed to some faceless person that was dealing with credit scoring. We've seen changes in that regard, with some movement back in that direction with the likes of Handelsbanken, who now have local managers dealing with their local profit centre and dealing with clients personally. A lot of how the market will unfold in the future will depend on more than just the technology involved."



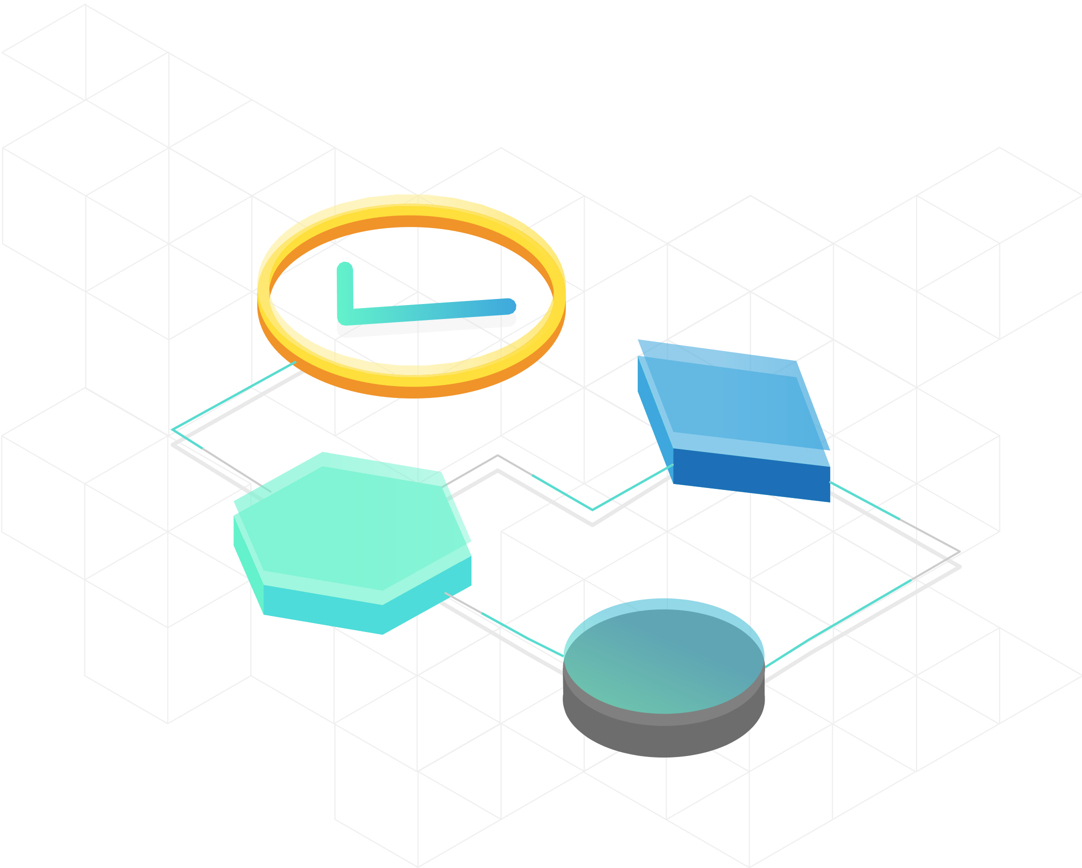
"I think for us, whether it's consumer or SME, any technology that improves the experience will be the one we invest in. Whether it's integrating into a customer's bank account with all their payments or integrating into their accounting software, anything that makes it easier for our customers who run their small business, that's what we're going to invest in. Companies are going to invest in making the customer experience better and better over the next few years."

Damian Brychcy,
Chief Operating Officer at Capital On Tap.

Good customer service is about more than just rectifying poor payment experiences caused by clunky legacy reconciliation systems. Delighting customers by offering them the right product at the right time and flexible management of their loan is key. Gone are the days of charging people for early repayment.

John Battersby at **RateSetter**, notes: "I think there are a number of elements that matter to somebody who's looking for a loan, rather than just the payment process itself. There are things such as eligibility, first and foremost. Does a lender adequately understand my needs as a borrower to design a product which caters to those needs? And flexibility is another important point. It wasn't so long ago that people were actually penalised for making early payments on loans as a standard. That's now changing."

He adds, "Now, sub sectors like P2P lending have transformed methods. It is now a good thing that people can repay loans early. That's the flexibility which is an integral part of our system."



4. Reducing Risk

Having a single loan disbursement banking partner has traditionally posed a significant risk to lending businesses. Lenders face the real risk of a banking partner having scheduled downtime – or an unscheduled IT outage. When lenders are tied to a single banking partner, platform availability is the difference between success and failure.

However, digital payment API platforms built to equip lenders in the Instant Economy benefit from a newer tech stack resulting in superior SLAs around platform uptime. It's the reason why we, Modulr, gained direct access to the Faster Payments and Bacs schemes, to remove our reliance on traditional infrastructure.

As such, we can provide industry-leading SLAs around platform availability and payment processing speed. As of Q4 2019, access to make payments on our platform was 99.9%.

"We are a client of Modulr because that back-end flexibility – and the features that they have such as multiple accounts per person and the ability to transfer money – is almost the backbone of what we do."

Garry Evans,
Chief Product Officer at Tully

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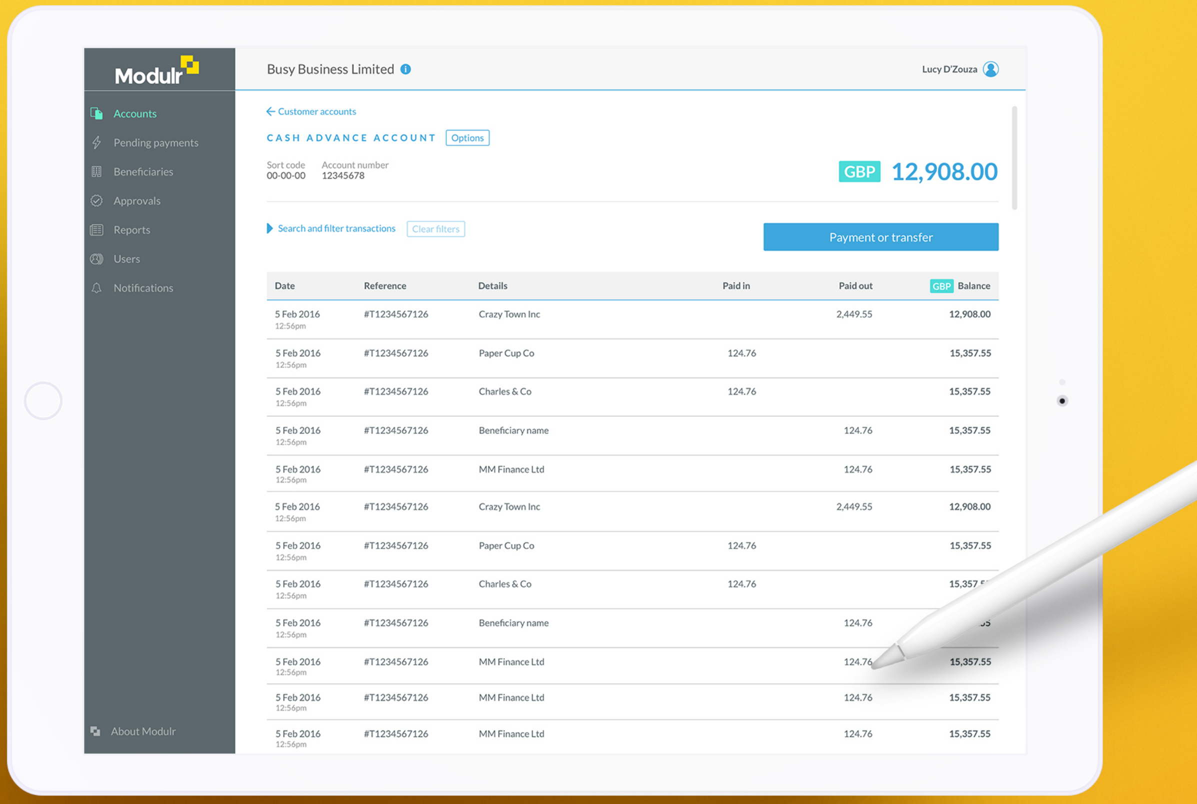
Winning in the Instant Economy



In the past, consumers and businesses went to banks and financial institutions for loans. In the new Instant Economy era, banks and traditional lending institutions are disintermediated and borrowers can access loans instantly from multiple sources.

Smaller lenders can now compete with bigger banks, in terms of access to funds and cost of funds, while transforming and disrupting the customer experience. Lenders of all sizes will be able to build up a picture of who the customers are and how they are using their money. This data will allow lenders to be more competitive.

The lending sector will change beyond recognition in the next few years. Lenders who emerge as leaders in the field will be those who have embraced the change, transforming their business to meet and anticipate consumer and business demand for digital platforms offering real-time loans and ease of payment.

"I think the banks still own 95% of the market. And so, they're still going to be the key for the next five to 10 years. But I think, if they don't get better at what they're doing, that the FinTechs are going to start to take more and more market share away."

Damian Brychcy,
Chief Operating Officer at Capital On Tap

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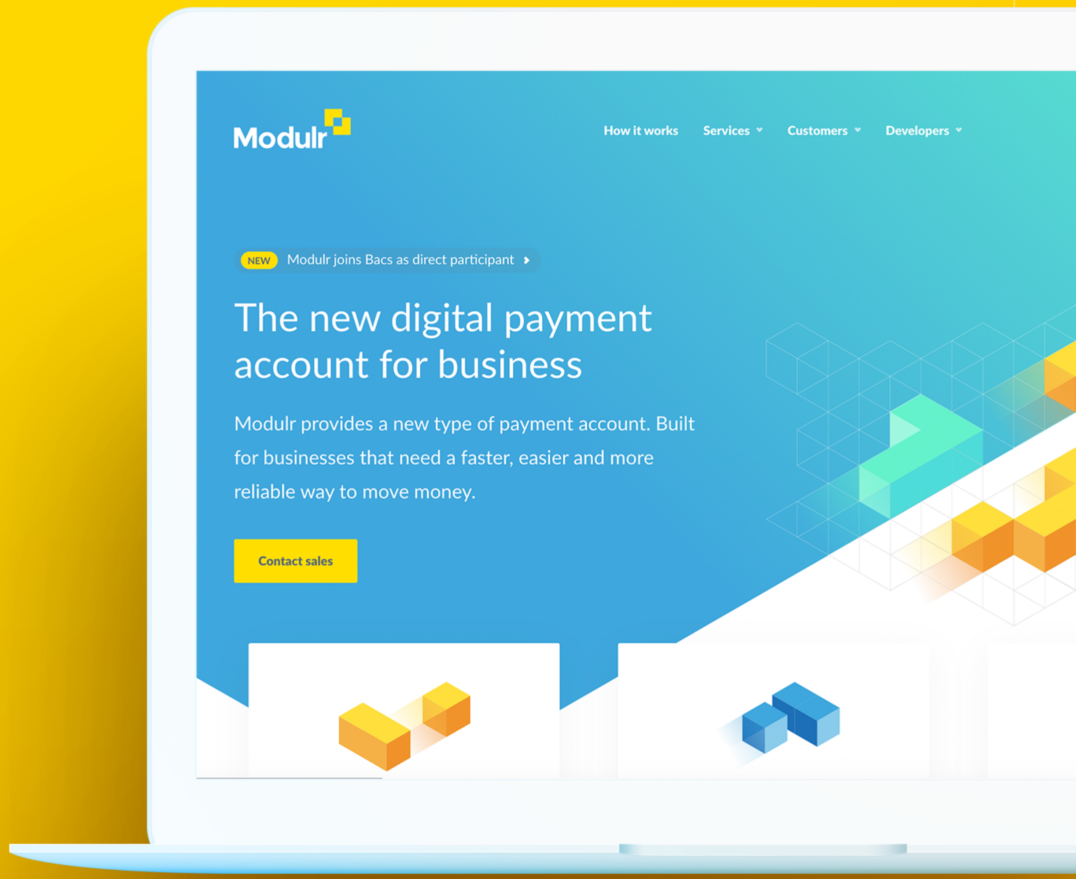
About Modulr & Acknowledgements



About Modulr

Modulr is the Payments as a Service API platform for digital businesses. It integrates into any product or system. Modulr's new type of payment accounts are built for businesses that need a faster, easier and more reliable way to move money.

Once integrated, businesses can instantly set up as many accounts as they need. Getting paid, reconciling and making payments is fully automated and can be managed in real-time, 24/7 through their existing software applications.

Modulr's API makes it easy for businesses to streamline existing services, launch new products and scale more efficiently. Modulr Finance Limited (FRN: 900699) is registered with the Financial Conduct Authority as an EMD Agent of Modulr FS Limited (FRN 900573). Modulr FS Limited is an Authorised Electronic Money Institution, regulated by the Financial Conduct Authority.

"I don't think we could run our business without someone like Modulr."

Garry Evans,
Chief Product Officer at Tully.

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Acknowledgements

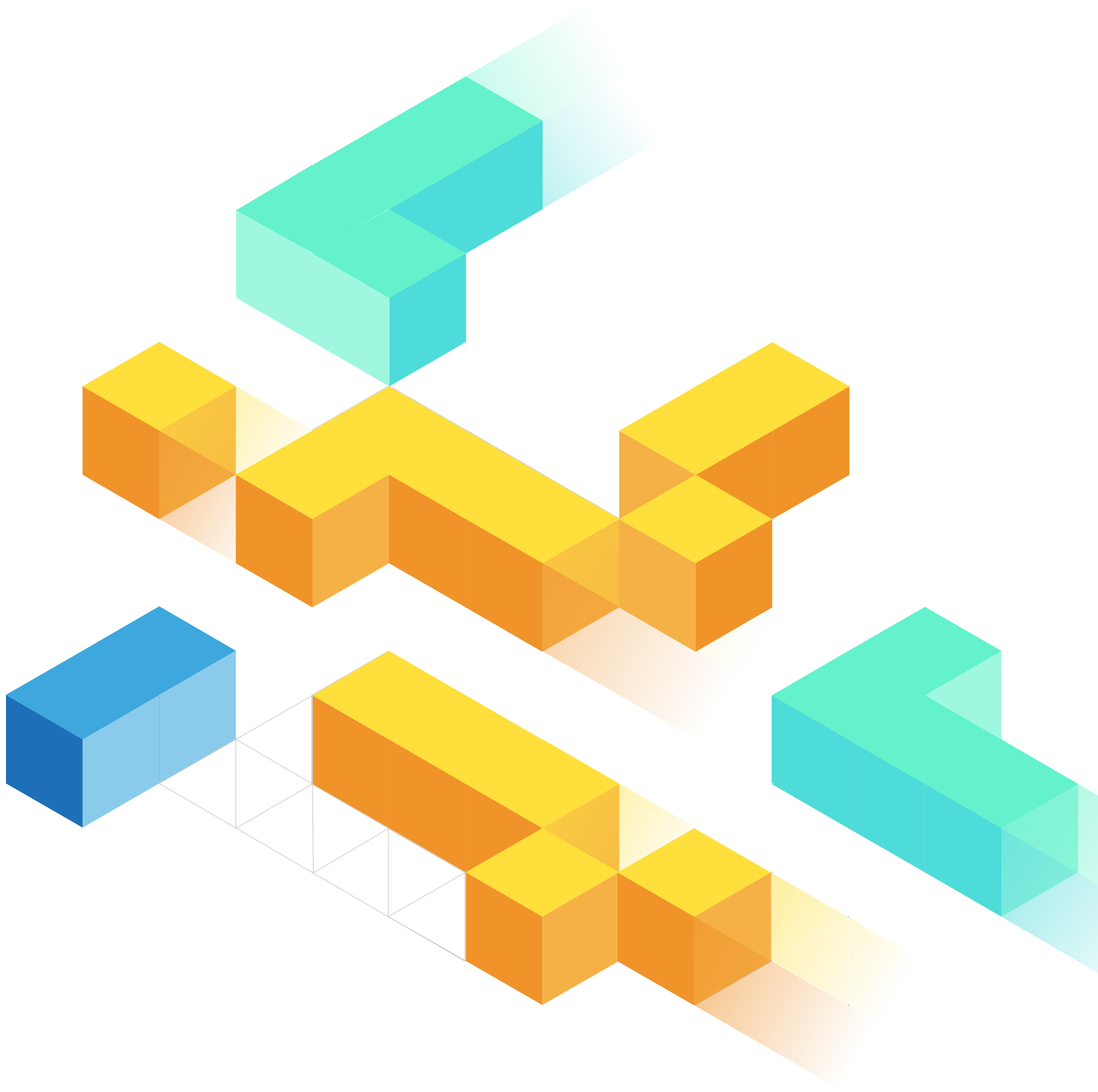
This report benefits from the input of CxOs at some of the most prominent global enterprises, who kindly shared their insights into the lending market in the fast-developing Instant Economy.

We would like to extend particular thanks to those we have cited directly in this eBook, along with the numerous others who contributed more general insights towards the bigger picture.

Sources

1 http://www.experian.com/blogs/insights/2019/03/4-ways-fintech-changed-lending/ Four Ways Fintech Has Changed the Lending Process and How Other Financial Institutions Can Keep Up

2 https://bankingblog.accenture.com/payments-predictions-2019



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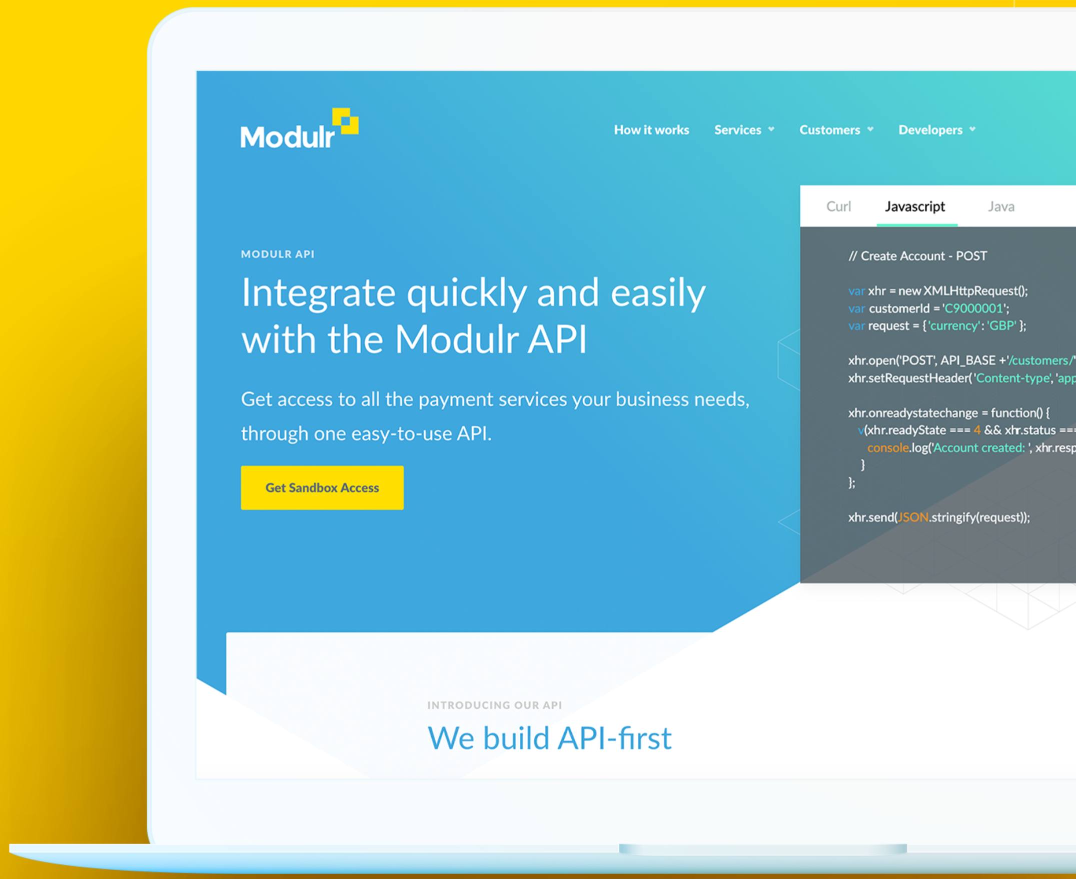
Biographies



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Damian Brychcy

Chief Operating Officer at Capital on Tap

Damian is the COO of Capital on Tap, a FinTech credit card provider. Prior to moving to London, Damian worked as a corporate attorney in the United States. Damian lives in North London and is passionate about his puppy (Rosie), college football, reading, and going to the pub.

Garry Evans

Chief Product Officer at Tully

Garry is the Chief Product Offi cer of Tully, the world's first digital debt adviser. Tully helps people easily understand and make the most of their money with simple, accurate online budgets. Tully budgets power personalised financial education, debt advice as well as preventative money coaching designed to help people make long term and lasting positive behavioural changes.

Garry has almost twenty years of leadership experience in the debt industry with companies including Capital One, TDX and Equifax. He has led teams delivering consultancy, debt brokerage, insolvency and recoveries management, sales and product management. He successfully launched TDX's global expansion into Australia and was responsible for Equifax's global collections and recoveries product portfolios.

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Steve Robson

Founding Shareholder and Managing Director at CapitalStackers

Steve Robson is the founder and Managing Director of FCA authorised and regulated CapitalStackers, a platform specialising in real estate development finance. Prior to setting up this business, Steve had spent his career in banking, the last 20 years of which were involved in structured real estate finance for a number of banks. He established and led successful lending teams for Hypo Bank, RBS, Singer & Friedlander and Macquarie. At RBS he structured and funded Bolton Wanderers football stadium and adjacent retail park and at Singers he pioneered the funding of direct let student accommodation well before the asset class became institutional.

He is the founder and director of pi-FRAME Ltd, a boutique software house which sells property finance risk analysis applications and a non executive director of developer contractor Williams Tarr Holdings Ltd.

John Battersby

Head of Communications and Policy at RateSetter

John oversees communications and policy at RateSetter, the UK's most popular peer-to-peer lending platform. Johnjoined RateSetter in 2015 from Lloyd's of London, where he led the communications and marketing team. Prior to this he held several positions in communications and in policy at HM Treasury, including Head of Communications Strategy and Head of News.

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Alex Kousiopoulos

Global Product Director, Bibby Financial Services

Alex's self-motivated, results-driven approach has seen success with multiple blue chip corporations across verticals n P&L management, product management, services marketing, portfolio management and performance improvement.

As Global Product Director at Bibby Financial Services, Alex has successfully balanced strategic thinking while also building high performance teams with a clear sense of purpose.

Kyle MacDonald

Chief Executive Officer, Financial Cloud

Kyle's extensive career has cut across finance, banking and technology.

After graduating with a civil engineering degree from the University of Glasgow, he transitioned into the banking and financial sector. Following successful spells as an analyst for some of the UK's top banks, he headed acquisitions for the Nasdaq-listed PRA Group before joining Financial Cloud as CEO in 2013.

Based in Glasgow, Financial Cloud provides an innovative software platform that enables lenders, legal firms and enterprise clients to get the most from their investment in technology.

Featured contributors

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Founding Shareholder and Managing Director, CapitalStackers

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