The Loan Market and the Digitisation Imperative

Do you remember that time you transferred an old mixtape from a cassette to an MP3? That was digitisation. Digitisation, simply put, is the process of changing data into a digital form that can be easily read and processed by a computer.

Digitisation is not a radical change in what we do, it's a change in how we do it. A change that has the potential to transform and grow the loan market – from the automation of documentation to the improvement of straight-through processing – resulting in shorter settlement times and faster access to cash.

It all starts with the digitisation of loan data.

This article, the first in the series of three, looks at some of the key drivers to embracing digitisation.

The journey ahead

In a recent IDC report[1], 40% of global financial institutions said that responding to the pandemic forced them to quickly shift to a digital-first strategy that they will continue to pursue. And whilst many in the industry are already shifting towards continuous digital evolution, the loan market has yet to gather pace on the pathway to digitisation; a pathway the bond market has already successfully navigated.

In 2021, global loan volumes exceeded US$5trn, with EMEA loan volumes reaching US$1.1trn. These figures are far from insubstantial, and as deals become bigger and more complex, technology has the potential to bring significant benefits to the loan market.

Currently, many agent banks continue to rely on manual processes such as fax and emails to share updates with lenders, who then need to sort and store these communications and upload the data in their systems. These tasks are labour-intensive and time-consuming, requiring a vast number of resources to handle the flow of data. In contrast, digitisation facilitates the automation of manual processes such as document management, improving operational efficiency, saving time, and reducing costs. Reducing manual processes enables banks to free up capacity, enabling their teams to focus on value-added projects, which can contribute to improved job satisfaction, and lead to higher retention rates and greater expertise in the market.

A tech native future

By 2025, millennials will account for over 75% of the global workforce. They grew up with the internet and social media platforms, they are used to accessing any service from the tip of a finger, living in a world of seamless, embedded experiences. These tech natives expect work applications to function as effortlessly and effectively as the applications they use in their personal lives, an expectation which does not marry with the reality of today's loan market.

If the loan market wishes to attract and retain talent, it must adapt to the expectations of the new entrants. A large part of this will be down to embracing the opportunities digitisation affords, freeing up capacity to focus on creating value for customers, with the technology taking care of the repetitive and mundane.

It is only by embracing the opportunities new technologies afford that the loan market will have a truly successful future, and this is something we as a market should be working towards.

1 https://www.finastra.com/sites/default/files/file/2022-05/resource-idc-infobrief-new-service-models-accelerate-innovation-banking.pdf

The need for a common language

The first step on the pathway to digitisation is the adoption of common standards across the industry, such as a unique identifier. This is not a step that can be avoided and preconceptions that a unique identifier is only required to achieve greater efficiencies in secondary trading must be dispelled.

A unique identifier is essential to achieving greater efficiencies in the loan market, opening the gateway to digitisation and more. It provides a standardised method for identifying loans, making it easier for market participants to monitor and track deals. This identifier must have two key attributes. First, it must be unique. Second, it must form part of a commonly-recognised global standard. For syndicated loans, the market requires these unique, commonly-recognised identification numbers to be applied to facility agreements, at both deal and facility level.

In the US, the leveraged loan market has come together and already adopted CUSIPs as the identifier of choice, with over 95% of deals having a CUSIP in place. The European market, however, has yet to agree on a common standard. It might seem logical for the European market to adopt ISINs; both ISIN and CUSIP follow a similar structure so they can "talk" to each other. Essentially, as long as one global common standard is agreed, it does not matter what that standard is.

Whilst the allocation of an identifier is very much one small step for man – in fact one small step for the agent, given it is the agent who would likely apply for an identifier – it really equates to one giant leap for the loan market in terms of future potential.

Think outside your box

Global events such as the COVID-19 pandemic, climate change, and the move to risk-free rates have pushed all market participants to work outside of their "boxes" and to collaborate in ways not seen before. Appreciation of the whole is exactly the mindset required to best effect the transition to digitisation.

> Lenders, vendors, and advisors need to draw together to put in place the foundations needed for digitisation to be most effective. Adoption of an identifier is not all that is required. We need to go further and implement the standardisation of operational terms – something that is largely achieved via the LMA documentation templates – as well as the standardisation of communication among market participants. Vitally, widespread digitisation of data in the loan market will pave the way to a golden source of truth, making data readily available and searchable via a single platform interface, in real time, facilitating loan reconciliation and transactions.
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> Whilst expertise of the part will always be required, appreciation of the whole will be essential.

About us

Gemma Lawrence-Pardew
Director - Legal, LMA

gemma.lawrencepardew@lma.eu.com
+44 (0)20 7006 2034

Helen Orton
Senior Director, Product Management, LenderComm, Finastra

helen.orton@finastra.com