

Survey Finds Room for Automation

By Brian Shaw

More than half replied that their commercial lending process is less than 50 percent automated.

Custom Credit Systems touched base with 25 commercial lenders for its 2009 annual survey to learn how they are approaching commercial lending technology as they prepare for economic recovery. Responding institutions ranged in assets from the low billions to trillions, representing a total of nearly \$4 trillion in assets. Of the participating financial institutions, two were top-five bank holding companies and three were top-10 commercial banks. Community banks active in the commercial market were also included.

By the Numbers: Is There Growth in Our Future?

Ninety percent of respondents have seen an increase in small business loans, mostly between one percent and 50 percent.

We have all seen some upward ticks in home prices, the Dow, international markets and now in commercial lending. The big question remains: Is this an upward trend or just a blip on a flat line? Overall, loan approval ratings have fallen, but loan application volumes are still up 15 percent to 20 percent for some financial institutions. To put this in perspective, in the United States, average long-term loan growth is six percent, while some periods, such as the 1980s, experienced an average growth of 16 percent. Recently, loan growth has been completely flat, so this spike of up to 20 percent will help the average remain consistent.

To properly predict future loan volumes, we must consider what can cause a true surge in volume. Changes in political power and technological advancements—such as the personal computer (PC) and Internet—have been known to restart the economy. Many were looking forward to emerging industries, such as the green sector, but recent events have cast doubt on whether this is the next new economic recovery driver. There does not appear to be anything

of the scale of the PC or the Internet visible in our near future.

The current uptick that we see may be surfacing because there is now very, very tight correlation between supply and demand. Corporations have trimmed their fat and work more efficiently and effectively than they have in the past. This is demonstrated in the retail environment. Stores were overstocked and had an abundance of inventory during the holiday season in 2008 when the stock market fell dramatically, which led to drastically reduced demand and, in turn, drastic reductions in price. By 2009, the lesson had been learned and retailers carefully monitored their volumes, leaving little (or an appropriate amount) for the clearance rack.

“Lenders have begun accepting more borrowers in comparison to what they were practicing in mid-2009, but we still have a long road to reach the healthy lending practices that we had years ago,” explained Mark Hill, managing partner of Collina Ventures. “Right now, the caution in the marketplace is palpable. Origination is low and a lot of the new loans being processed are for existing borrowers with strong credit. This market will eventually dry up and banks will need to make some changes.”¹ Some financial institutions are optimistic, however, that real loan growth opportunity is just around the corner. Stephen Steinour, president and CEO of Columbus, Ohio-based Huntington Bank, is gearing up by adding 150 new small business bankers. He was quoted in the WALL STREET JOURNAL on February 11, 2010, saying, “We are all in on this. We are not dabbling.”²

By the Numbers: Technology's Reach

Respondents unanimously agreed that technology is a major component for helping financial

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institutions maneuver through current economic challenges.

It is clear that commercial lenders need technology to revive the industry, but the reason is for much more than just efficiency. Technology started bringing banks efficiency with the introduction of the PC and the Internet. Now, handheld devices, mobile phones and an array of other gadgets help us save time and increase productivity. While society “could not live without” all of these conveniences, commercial lenders also should not live without a proper portfolio management system.

Loan portfolio management systems provide lenders with the ability to quickly and reliably analyze both the scale and dynamics of portfolio changes and adjust their actions accordingly. If financial institutions had a better view of what their lending departments were facing five years ago, we might never have been in the recession that we are all experiencing today. Likewise, if proper measures are not taken, we might fall into the same trap all over again.

A true portfolio management system will work across all silos of lending, providing one cohesive report. Commercial, commercial and industrial (C&I), real estate, indirect and all other loans should be consolidated, common-sized and analyzed as an entity. Once this is done, credit officers, branch managers and anyone involved in lending can easily identify daily, weekly or monthly trends such as rise in delinquencies, charge-offs, risk rates, workout loans and utilization. Then systematic, knowledgeable actions can be made to adjust the bank’s course of action and address the growing trend before it becomes detrimental.

The necessity of a portfolio management system was never as obvious as it has been during the recession, with some lenders freezing accounts and halting lending when they should be continuing to make wise decisions and benefiting from the appropriate credit/interest rate equivalency. Risk departments do not have all the information they need to assess their risk properly right now. Most excuses for poor reporting involve a lack of data or skill set, but this does not have to be the case. Poor information leads to faulty decisions and poor economies. An active portfolio management system will protect banks as they climb out of the recession and far into the future.

More than half of the respondents cited that their commercial lending process is less than 50 percent automated.

This statistic points to one of the major flaws of banking: lack of innovation. As a former banker, I

can attest to the fact that the first reaction to solving many problems is adding people rather than making the investment into technology. Of course, one does not need to be overly creative to automate lending processes any more. Automation of the lending process and the tools to analyze portfolio composition and trends have emerged in the last decade. Today, systems are proven and readily available to truncate the entire practice, from applications to fulfillment to monitoring. Full automation is growing; as time goes on and progressive institutions continue to tout their success, this trend will increase exponentially.

“Banks are under intense pressure to make sound, safe decisions on approving loans. As a result, bankers can benefit from end-to-end loan automation now more than ever to help drive down the time-consuming and costly processes that are associated with heightened underwriting standards,” Hill explained.

Respondents all use at least four different systems to process and manage one commercial loan from beginning to end, with 45 percent of them using upward of seven systems.

The journey toward a fully automated lending solution has already started for most financial institutions with the purchase of point solutions. In some cases, one department grasped an idea or a technology faster than another, some were trying to keep up with competitors on a microlevel and others had the full picture in mind with no idea how to execute. Now, most commercial lending processes are a blend of several disparate systems. Compound that with mergers and acquisitions (adding another four-plus solutions to the deal), and the process can become overly complicated. Part of this multifaceted business can be blamed on the regulatory environment. The structured and siloed rules by which banks are tested and governed demand expert personnel and specific solutions for each part of the lending process.

Bankers should start trying for full automation now because it is the future of lending. A proper suite will be able to manage any loan from the simplest small business loan to the largest commercial loan.

“The end-to-end solution is understood conceptually, but it will take a lot of hand-holding to truly fulfill this goal,” noted Jim Daley, principal of New Coin Financial. “The biggest impediments are a lack of expertise and authority in the lines of business to select the right solutions and stitch them together seamlessly. As a result, lenders need to find vendors that they can

rely on as trusted partners and empower them with C-level access to work around organizational impediments. Growth by acquisition has borne ill-defined job responsibilities and long approval processes which an outside consultant's perspective can help with."³

By the Numbers: Technology's Value

A single point of entry was considered the most beneficial feature in the respondents' current commercial loan processing solutions.

This should be no surprise, since a single point of entry would dramatically increase efficiency and effectiveness. It reduces the chance of human error, tremendously speeds the process and even provides a hassle-free environment for the borrower. The next question should be: Why haven't banks done this yet?

Banks' speed of adoption holds them back from simple solutions that other industries are already using. Take the airline industry, for example: Based on data from the Bureau of Transportation Statistics, American Airlines flew roughly around 80 million passengers in U.S. flights alone in 2009.⁴ The company handled each of those passengers through one single point of data entry when the ticket was purchased. Imagine how a passenger would respond if they were required to provide full, detailed personal information at the time of booking ... and then again at the time of check-in ... and then again when boarding ... and baggage claim. You get the idea. This industry goes even further with its affinity programs that allow an extremely expedited process for frequent travelers and eases transactions with airline partners or for add-on products such as car rentals or vacation packages. Stop and consider how fluid this industry is compared with your lending operation.

Focus on Profitability

Commercial lenders play a very strong role in the U.S. economy; they fuel the growth of our nation's busi-

nesses and livelihoods and are a major component of ending the recession. One chief credit officer recently told me he was "trying every way possible to deny a \$20 million commercial real estate deal." That should never be the case; there is no need to throw away a loan if it has merit.

"Commercial lending should be the most profitable area of a bank, particularly for the regional and sub-regional institutions," noted Daley. "And bankers need to realize that automation will help them to further improve profits and the quality of their performance. Now that merger activity and consumer business is slowing, more attention can (and should) be placed on commercial lending. The attention from the government and regulators is an extra incentive—the wind at your back—for a plan that should already be in progress."

It is of the utmost importance that lenders continue to lend, and an automated, straight-through commercial loan process will ensure that wise lending decisions are made and the loan is monitored throughout its life. This survey confirms that the industry still has more work to do, and technology, combined with a sound strategy, will help lenders better manage their portfolios and get back to the three Cs of lending: character, capacity and collateral. Let's ensure we have the knowledge, processes and technology to make solid loans.

Endnotes

- ¹ Comments from a conversation on Feb. 15, 2010, with Mark E. Hill, a Managing Partner of Collina Ventures. Hill cofounded Baker Hill® in 1983.
- ² Marshall Eckblad, "Huntington to Double Small-Business Loans" *Wall St. J.*, Feb. 11, 2010, accessed at <http://online.wsj.com/article/SB10001424052748704140104575057580541457488.html?KEYWORDS=Huntington+Bank#articleTabs%3Darticle>.
- ³ Comments from a conversation on Feb. 10, 2010, with Jim Daley, Principal of New Coin Financial. Prior to New Coin, Daley cofounded PCi Corp. (now a division of Wolters Kluwer, NV).
- ⁴ This data is based on enplaned passengers. Each time a person flies is counted as an additional passenger.

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