DO YOU HAVE A DR. NO IN LENDING Â– PART II

by Steve Brown

Yesterday we explained why pinning the "Dr. No" label on your CCO may not be entirely fair, considering many banks have understaffed their credit function or operate inefficiently. Taking a cue from Honey Rider in the classic James Bond film when she said, "James, you are going to have to move a little faster," many loan departments could also stand some streamlining. As our past research has uncovered in focus groups with commercial lending clients, banks that can deliver an underwriting answer in 3 days or less have a distinct advantage when it comes to price and/or garnering the loan business. Banks that have adopted credit scoring for loans under $500k have made huge strides in processing and (with similar or better accuracy) at a fraction of the cost and time, compared to traditional credit underwriting. However, a recent review of several bank's loan departments unveiled even more areas of possible efficiency improvements. One the largest bottlenecks uncovered is a problem we alluded to yesterday. Due to client pressure, lenders often present incomplete credit packages, causing analysts and credit management to either wait while they collect the information or potentially make sub-optimal decisions. The credit department can gain efficiencies by defining "high priority" elements required to process credit. Though additional information may come in during underwriting, making a clear distinction about the minimum data required ensures that the queue is not clogged with incomplete requests. Since different credits require different "mandatory" information, some banks assign a set of "gatekeepers" to do an initial review of the credit. They prioritize approvals, note policy exceptions and detail missing information or analysis. This is done during the period of time between submission of a lender's summary and completion of an in-depth review by a credit analyst. The gatekeeper helps keep the process flowing, provides another credit opinion and prioritizes the depth of review (since all credits do not require a full underwriting). In this manner, resources can be better allocated and thus assigned different resources. A company with stable and growing earnings in a protected market (due to technology, patents, etc.) should require about half the analysis of a cyclical company with strong competition. In the future, we will be focusing more on what is working for community banks and how they can process credit more efficiently and accurately. If you have any ideas, we would love to hear about them.

BANK NEWS

M&A

Fifth Third Bancorp ($101B, OH) said it will buy First Charter ($4.9B, NC) for about $1.1B or roughly 2.25x book. The purchase gives Fifth Third 57 branches in NC and 2 in Atlanta, boosting the bank's presence in the Southeast.

M&A

The HC for Pinnacle National ($2.2B, TN) will acquire the HC of Bank of the South ($495mm, TN) and PrimeTrust Bank ($549mm, TN) for $196.2mm, or roughly 1.8x book.

Countrywide

Countrywide Financial, the country's #1 mortgage loan originator, has been forced to draw down on $11.5B in credit lines (from 40 large banks) in an effort to avert a liquidity crunch. The company said it also plans to push its mortgage business under its banking operations, which currently amounts to $94B in assets. The Company's shares plunged 13% in active trading yesterday (down 21% for the year) and its 30-day commercial paper was being quoted at 6.50%. Banks that sell mortgages to them should have contingency plans in place to mitigate the risk if the liquidity goes away.

DEPOSIT TACTICS

Given market turmoil, banks should be reminding their customers of the safety of FDIC insured deposits. We have had great success helping client banks reduce their deposit rates (note the 1.16% change in short-term rates in the chart below) and increase marketing in order to capture outflows from equities and mutual funds. The results are starting to appear, as banks build deposits at lower rates. Now is the time to take a leadership position with your customers and transition them away from rate and into safety and service.