

LOAN FOR HIRE AND CROSS-DURATIONS

by [Steve Brown](#)

While innovation of cash management products can be easy to come by, creativity in lending is difficult. Because of this, bankers should take note of a new loan program that Chase is rolling out. It not only is worthy of consideration as an offer, but it also highlights a key product design concept called "cross-durations." The "Loan For Hire" program is marketed to small businesses and gives them up to a 2% discount off their loan rate when a qualifying business takes out a loan, hires new employees (up to 3) and maintains a business checking account. For example, businesses that get approved for a term loan or line of credit can get 50bp deducted from the borrowing rate for every employee they hire in 2010 to a total of a 1.5% discount. Businesses that open a checking account get another 50bp. Chase is targeting businesses with annual sales revenues of \$10mm or less and this program applies to new credit lines or new increases of existing lines between \$10k and \$250k. An I-9 Form is required to verify employee hiring and interest rates are then reduced on the loan 14 to 30 days after receipt of this proof. This offer runs until the end of the year, while discounts provided for new employee hiring are good for the life of the loan.

Now that the details of this new program are out of the way, let's do some analysis. Our first comment is that Chase is stepping up their marketing and product innovation game. This is the 2nd product this year that has the public talking (the first was retail RDC). The Loan For Hire program is innovative and has a couple of items going for it. First, it plays into the current concern regarding unemployment. Second, it positions the bank as a helpful partner, supportive of small business.

The combination is powerful and Chase also gets high marks for how they promote the product. The product is smartly supported by banner advertisements, press releases, a website landing page and the latest effective advertising in banking - video. The well done video library not only explains the details and gives testimonials in an engaging format, but positions the bank as a thought leader and a trusted advisor to small businesses by offering hiring and business strategy tips.

Another reason we like this product is that it is a perfect illustration of cross-duration extension in product design. Basically, Chase has originated a small balance business loan that is normally unprofitable and made it profitable. While cross-marketing checking accounts to a loan is common (and should be the rule, not the exception in your marketing efforts), what is missed is the intricacies of this new tactic. While most bankers will assume new deposits are always good, the reduction of rate and the cross-marketing of the loan and deposit specifically, accomplish something much more than that.

By giving up 50bp, the bank gets a non-interest deposit. Thus, on the surface, if you assume an average \$150,000 loan, the bank gave up \$750 in revenue per year, but gained a deposit. If you assume an average balance of \$35k, then the bank would be on the losing end of this deal, given the current rate environment. However, while any cross-sell helps the bank, having a loan and a checking account together does what few other bank product combinations do - it increases the duration of both the deposit AND the loan. A deposit makes the customer more likely to keep the loan outstanding or refinance with the same bank. On average, this equates to about 2Ys of extra cash flow from the loan, which is important considering the average risk-adjusted small business margin is approximately 3%. On the other side of the equation, having the loan outstanding dramatically

increases the positive convexity of the deposit, thereby extending duration of that item as well. As the economy improves, businesses are much more likely to increase their profit and operating account balances, usually at a time when rates are going up. This cross- duration is an aspect of bank profitability that largely goes unnoticed. In this case, a small business loan (assuming a \$150k balance) and the deposit, equates to approximately \$9,400 of additional value.

Marketing a loan and core deposit together and using a loan rate reduction mechanism is a smart move. Marketing that packages both small businesses and hiring is brilliant. Community bankers may want to come up with a similar product to capture your community's attention and boost profitability.

BANK NEWS

On Hold

On Saturday, Bank of America became the first bank to halt foreclosure proceedings and sales in all 50 states.

Lawsuits

American Banker is reporting that the FDIC will file lawsuits against over 50 executives and officers from failed banks in an attempt to recover \$1B in losses.

Interest Rates

The chief economist of Goldman Sachs predicts the Fed will do \$500B of quantitative easing and hold interest rates at current levels until 2015 or later, to spark economic growth and avoid a dip back into recession.

Very Slow

A story in the WSJ found home foreclosures take 100 days longer on average in FL (where judges are involved) than in CA (where judges are not involved).

Mortgage Walk

A Pew Research survey shows 59% of people say it's wrong to walk away from a mortgage, 19% said it's acceptable, and 17% said it depends on the circumstances. Not surprisingly, the group that said it was OK to walk away were more likely to have negative equity in their homes.

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