WHITE PAPER

The Five Dimensions of Digital Commercial Lending

The rise demand for Commercial Lending has caught banks off-guard. In order to fully leverage the opportunity presented by the positive growth environment, lenders need a model to address various counter-balancing elements of growth, profitability, customer-centricity, operational efficiency, risk management and regulatory compliance. In a nutshell, 'The Digital Imperative' is upon them.

What does it mean to be digital in commercial lending? What are the five dimensions of digital commercial lending? What model would really work? How do leaders make progress today?

Commercial Lenders in a Perfect Storm

Commercial lending is gaining momentum which has caught banks off-guard. The increasing demand for commercial loans has spurred banks to take proactive and preventive actions – such as, bringing in tighter underwriting rules and policies for managing risks better, given the fact that the overall creditworthiness of potential borrowers is on a decline. **The demand for commercial loans in various forms has not been as strong in almost a decade.** This development spells a perfect storm for commercial lenders. To add to this build-up, many other competitive forces makes it imperative for lenders to take strong actions now.

The business lending opportunity is up for grabs

Banking and financial services industry has been on a slow recovery path since the 2008 financial crisis. However, in the last few years, a steady and noticeable rise has been observed in commercial lending sector. This upward trend has fuelled banks of all sizes – across various commercial loan offerings, into action to tap this opportunity. Lenders are realizing that majority of their current portfolio today comprises commercial lending products. This sharp rise has led to a situation where business loans are overtaking residential mortgage loans for the first time since the 1980s; and, commercial lending accounts for a whopping 21% of all outstanding loans from banks - the highest level in 13 years.

However, at the same time, the percentage of overdue loans is also increasing, even as total rate of non-current loans has been going down. Despite the risk aversion sentiment that gripped the market since the financial crisis, there is business on offer and banks cannot afford to overlook it. Make hay while the sun shines, if you will!

However, lenders face a perfect storm of challenges

While lenders want to tap the business opportunities presented to them, they face a set of challenges that force them to trade off business with risks. Their progress is hindered by lack of their own capability to counter these risks effectively.

Every client is unique. Banks need to profile prospects and customers in a detailed manner and also as precisely as possible. This uniqueness of customers and their requirements make it difficult for banks to assess risks and service them duly without adequate information support.

Commercial lending processes are complex. Unique client needs poses a complexity of its own, however, what makes commercial lending further complex is the cross-functional nature of these processes. Additionally, for proper risk and portfolio assessment, these processes involve participation of subject matter experts and risk officers at various stages, making these workflows even more complex.

Products and offerings tend to vary. Unique customer needs also mean that lenders need to offer variations in their products to satisfy those needs. These variations pose further difficulties for banks in applying their policies and rules without the requisite support from systems and processes.

Regulatory regime continues to get stricter. Post the financial crisis, while banks became risk averse, the regulatory requirements have become even more stringent. Banks need to be able to perform Portfolio Management, Credit and Risk Management while ensuring compliance.

Broken context in loan servicing. One of the biggest challenges for lenders that prevents faster loan disbursal is that the customer context is not carried through the whole lending lifecycle seamlessly. Broken processes, siloed systems, under-leveraged experts, and complex rules do not allow lenders to service their customers adequately and fast enough.

Inefficient middle office and back office operations. For lenders, one thirds of operational costs are due to reworks, waiting times and delays. The slow and cumbersome processes often lead to disenchanted customers, while good quality customers are already on a decline in the overall commercial lending space. Customer servicing and retention are key focus areas, and lenders struggle with outdated processes and systems even with the best intent.

Increasingly competitive environment. The middle market firms, the firms with loan requirements of up to $1 million or more, or on the lower end of $250K and less, are the biggest demand drivers in the market for many banks today. However, competitive forces vying for the same growing segment is increasing as well. While there's enough competition from banks of various sizes and scale, lenders face additional competition from alternate lending and P2P lending players, albeit marginal but with potential to grow further.

The Mindset Conundrum - A Key bottleneck

While it is true that Banks are facing real challenges at business and operational front, our experience with customers globally also tells us that mindset is one of the key deterrents in making real progress with lending transformation. With a long legacy of IT systems, and increasingly complex operational and risk management demands, most IT leaders are stuck with the basic problem of how to proceed, and fast. Their experiences from past transformational initiatives with large systems and point solutions have alienated them from taking on ambitious process transformation programs. It's a task that seems either too ***expensive*** *or too* ***complex*** *to undertake – mostly both!*

What Drives Commercial Lenders today?

Commercial Lenders, today, are driven by a multitude of factors. While on one hand, they want to drive revenue and focus on customers, on the other they have to manage risk and profitability.

Drivers for Commercial Lenders

Customer & Revenue

- Ability to Sell More
- Improved Customer Touch-points
- Better Customer Experience
- Stronger Customer Relationship
- Unified Face of Customer

Operational Efficiency

- Straight-through Process Automation (STP)
- Automation of Risk Assessment
- Optimum Workforce Participation
- Streamlined Processes
- Document Integration

Cost Effectiveness

- Cost of Sales
- Operational Costs
- Total Cost of Ownership (TCO) for Technology
- Minimized Regulatory Penalties
- Minimized Opportunity Cost

Risk & compliance

- Better Compliance & Reduced Fines
- Better & Holistic Portfolio Management
- Comprehensive Covenant Monitoring
- Effective & Efficient Collateral Management

Figure 1: Drivers for Commercial Lenders

Many of these drivers are the market levers for better overall business profile. And some, such as Operational Efficiency, are organizational levers to achieve those larger goals of business revenue and profitability.

It is obvious that a customer focused approach would lead to more business revenue from lending, however, it is also true that lending remains one of the greatest sources of risk to a Bank's financial stability. Banks have been looking for automation and straight through processing as an answer to these challenges for some time now, however, outdated and fragmented systems, along with dozens of siloed third party applications and point solutions make it difficult to achieve the desired results.

The digital imperative is upon commercial lenders today.

The Digital Imperative for Commercial Lending

Let's take a step back and see what this means for Banks. While they continue to tighten their policies and risk management, they need to gear up operationally and technologically to meet the demands of the new business dynamics. In essence, it boils down to –

- Delighting customers. Achieving customer-centric mindset and operations.
- Being fast and agile. Ability to respond to requirements of operational efficiency as well as flexibility to change, as and when dictated by external factors.
- Acting as an 'Anytime Anywhere Business'. Ensuring that organization act as infinite business where partners and customers can participate seamlessly, from anywhere.

Figure 2: The Three Digital Imperatives for Organizations

Lenders need to be digital. Period. This knowledge, however, is only half a step. Lenders today face real deterrents that do not allow them to take the next steps in their digital journey in commercial lending. Part of it is mindset, but, still dictated by real challenges on ground.

Why does it seem daunting to undertake Digital?

Banks are aware of the requirements of their business. Business leaders, and IT leaders alike, understand at broad level the leverage that digital offers them to address the challenges they face. Customer Servicing, Business Agility, and Responsiveness are key ingredients for success in commercial lending. However, the ongoing legacy and state of their processes do not allow them to take a very aggressive and risky transformation program. There are multiple factors leading to this mindset in undertaking digital in commercial lending.

Legacy, Point Solutions and Siloed Systems. From IT perspective, trend in the past has been to rely on core legacy systems for backend and specific point solutions for front and middle office. However, these siloed and disparate systems continue to be a source of inflexibility and disadvantage in the digital economy.

Customer Centricity v/s Operational Efficiency. The Straight Through Process (STP) automation continues to remain elusive without an adequately capable platform. Finding the right balance between efficiency-centric automation versus customer relationships and knowledge worker leverage requires a thorough customer centric and process driven mindset, supported by the right platform.

No Cookie-Cutter Solution. Commercial Lending cannot be handled with cookie-cutter and one-size-fits-all approach. C&I and CRE (incl. Multifamily) products need deeper, rigorous and expertise driven processes while being efficient at processing. Small Business loans and SBA loans on the other hand provide for much lesser margins with much higher expectations on speed and volume. Additionally, commercial lending processes are prone to emergent and exceptional scenarios.

What's the way out?

Doing Digital 'right' in Commercial Lending

Banks cannot afford to be stuck between revenue making and risk management. The opportunity presented by changing dynamics always comes with a timeline to act. Speed is key. **However, organizations cannot just paste a digital face to the same-old transactionally disparate mechanism of doing things. They need to have a unified approach that addresses the end-to-end lending lifecycle – from prospecting to lead generation to closure and then servicing – with the right balance of customer-centricity, process automation, and knowledge worker leverage.**

What has traditionally made it difficult for lenders to arrive at a cohesive approach is that lead generation and loan origination business owners have objectives that are different and sometimes orthogonal to the underwriting and risk management objectives. However, a contextually consistent process should ensure what's best for the lender organization – both in terms of revenue and in terms of financial risks. This requires an approach that considers the various drivers holistically and provides a way to bridge those gaps through a unified process solution.

What 'Digital' means for Commercial Lending

Digital is not just about Automation, but it is also about connecting people, processes, systems and things in your ecosystem to deliver customer-centric, agile and responsive organization. That's what Commercial Lending needs. As Commercial Lending process cuts through multiple functions and systems, it cannot be looked upon as a transactional point solution. There needs to be a holistic process approach in consideration of multiple dimensions that lenders have to address.

Digital Commercial Lending Model - The Five Dimensions

Organizations need a model for Digital Commercial Lending – a blueprint that provides for leverage points supported by an architectural approach.

Based on our experience of working with many successful lending organizations and banks globally, we've developed an approach that enables organizations transition from constrained legacy systems and point solutions driven environment to a modern digital commercial lending platform.

This model comprises five key dimensions that make a commercial lending platform 'truly digital'.

The Five Dimensions of Digital Commercial Lending

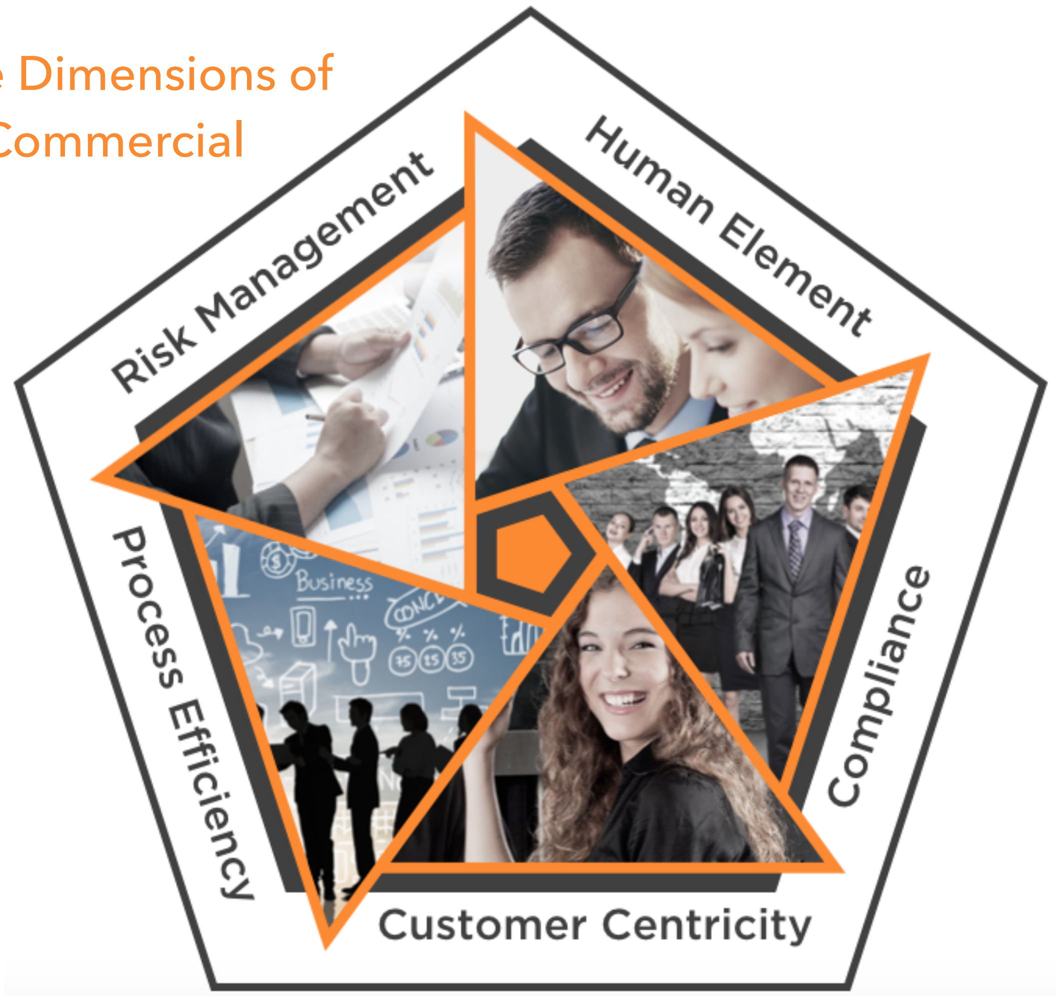

Figure 3: The Five Dimensions of Digital Commercial Lending

These five dimensions make Digital Lending truly and comprehensively digital.

1. Customer-Centricity. Customers need to be addressed in their context, and with speed. This is especially important because lending needs for every customer is unique. A set formula doesn't work so well, which unfortunately is what rigid point solutions and legacy systems dictate in terms of lending products design and servicing. The lender organization's relationship managers and loan officers need to be equipped with customer information along with process intelligence in order to "talk" to customers in their context. A flexible process-driven approach supported by a system that provides for customer context throughout lending lifecycle is key. This requires a "Unified" commercial lending approach.

2. Process Efficiency and Straight Through Processing. Customers expect a fast response, and contextually correct action. It is easier said that done, though. This requires a process mindset, supported by a flexible workflow driven platform, with the ability to delink business rules from the transactional aspects of the process. Customer data, customer documents and collaterals, lending policies and rules, risk management policies and regulatory compliance aspects need to work in mutual conjunction without forcing rigidity and tight-coupling in the process.

3. Risk Management. Lending business is all about managing risks against revenue and profitability. Risk is as much prevention of a bad quality loans as it is about making sure that a creditworthy customer is assessed and treated well. It has two key aspects: One, automation of credit checks and isolation of policies into a better manageable and flexible rule management system. And two, empowering loan officers and risk officers with the right level of participation and authority, along with flexibility to act in the customer context. This needs process visibility, content integration, flexible workflows, robust and flexible business rule management system, and great exception handling capability at process as well as transactional level.

4. Regulatory Compliance. A thorough process monitoring, a tight control over application of credit policies, a comprehensive portfolio management and covenant & collateral management are the basic requirements for regulatory compliance. However, it is also critical to be able to respond to regulatory changes and indeterminate regulatory aspects. A modeling driven approach with a faster time to market becomes critical; not only in terms of competitive advantage, but also for a timely regulatory adherence. Most importantly, for a thorough 360 degree adherence, a unified platform across lending products provides a handy overview and visibility.

5. Human Element. Lending is a people-driven business supported by automation and technology. Digital is not 'truly digital' without consideration of the human element. Most long term lending business relationships are driven by people supported by systems that empower and facilitate them to their best intent. Customers need a human connect when they interact with lending organizations, and even though automation of the communication channels helps streamline the resources better, a customer still needs a timely and contextual engagement. Similarly, risk officers, loan officers, and relationship managers have their own needs in order to serve the organization as well as customers better. A unified platform that provides them all the right information and allows them to make timely decisions in the best of their capacity is critical for an effective commercial lending process that is customer-centric and efficient, i.e. digital.

In order to compete in today's growth environment, organizations need to address the five dimensions of Digital Commercial Lending.

Digital Commercial Lending Model - Getting the Technology 'Right'

Let's recap on what makes it difficult for organizations to implement what they already know that needs to be done.

- Legacy, point solutions and silo'ed systems, that are the source of inflexibility and disadvantage in digital economy.
- Finding the right platform that provides leverage for customer centricity as well as operational efficiency.
- Unique customer requirements and emergent scenarios that make cookie-cutter solutions ineffective.

Build?

Traditional enterprise technology solutions built internally do not provide process level flexibility to deal with the demands of today. In fact, they are hard to build and maintain in the fast paced digital world. Also, the multi-layered, disparate and siloed systems, even though supported through data integration technologies are too limited and rigid. Now, in order to really make something happen today, a 'build' approach is unthinkable because of the vast amount of work needed to be done while sense of urgency is high.

Buy?

On the other hand, **buying an off-the-shelf point solution provides a "false" sense of speed.** Customizing a point solution to the organization's needs – beyond configuration – is equivalent to attempting a facade of modern elevation on a cottage house. You can only modify or polish the surface, but cannot touch the nuts and bolts and hardened bricks and mortars. It gets an organization no where, because a point solution is typically built for the 'majority' requirements of lenders based on past and present needs. Packaged applications – as organizations have come to know by experience – lack platform agility, have inflexible workflows, come with hard coded rules and provide weak integration capabilities. Hence, they fail to provide the organizations with the capability to differentiate their lending offering. Not just that, they fail to fulfill the fast changing demands of commercial lending business today.

The right mix

A commercial lending solution built over a BPM framework provides the right mix for 'truly digital' commercial lending.

The BPM framework provides the underlying workflow automation, process flexibility, loosely coupled business rules management, knowledge worker participation, and integrated transactional content management. These form the basis for the agile and architectural flexible platform for technology needs across lending products.

A solution accelerator, built atop this framework lends organizations faster time to market for implementation of their lending products across commercial lending segments. This 'Unified' and "BPM platform" based approach provides lending organizations the required coverage across all the five dimensions of digital commercial lending.

What is a Solution Accelerator?

An accelerator is a ready domain solution built with the intent of fast time to market with the advantage of custom commercial lending solution supporting differentiated and flexible product offerings. It allows lenders to avail the benefits of both 'build' and 'buy' worlds, i.e. they get readymade domain rich solution that can be deployed quickly while also enhancing its capabilities through a configurable and flexible fully loaded BPM framework underneath.

Why does it work?

This model for Digital Commercial Lending driven by a unified platform for all lending products works because it helps organizations 'pragmatically' address the five dimensions, and by providing the much needed bridge between the business & customer objectives with risk management & compliance.

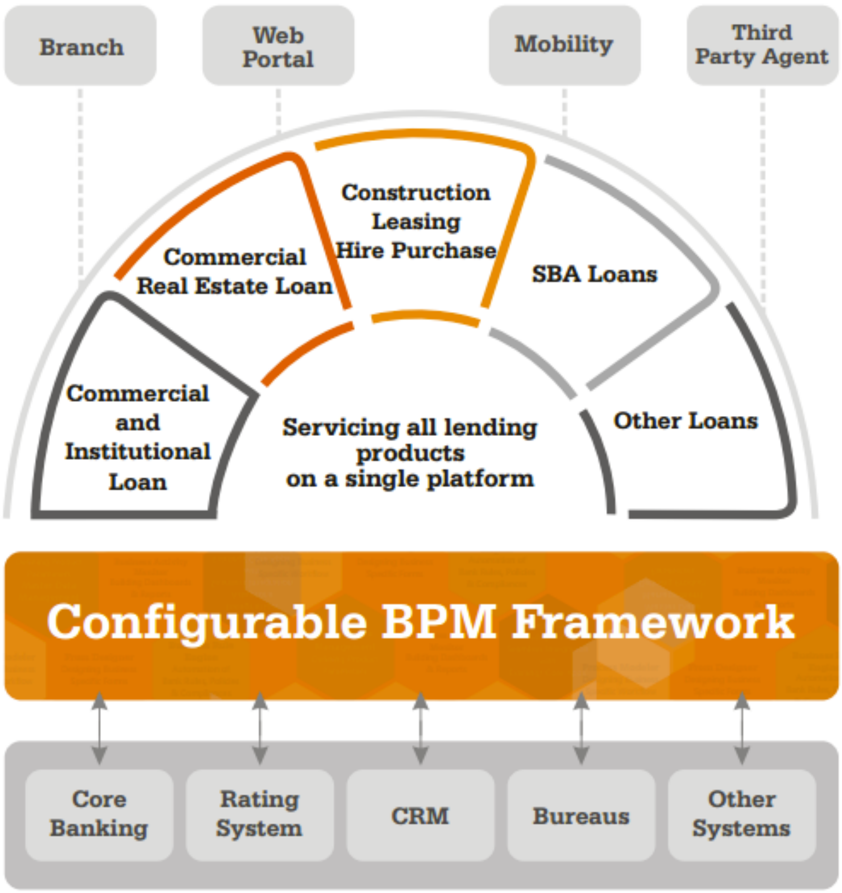

Figure 4: Unified Digital Commercial Lending Solution

This is achievable more specifically by -

- Unifying all lending products (C&I, CRE, Construction, SBA, Agriculture, Leasing etc.) for end-to-end lending cycle management from prospecting, document capture, digitization, origination, approval, closing & disbursement, to servicing.
- Automating the lending approval process and implementing an optimized workflow, that enables

improved TAT, predictability, transparency and better decision-making.

- Managing lending rules and policies as organizational assets - centralizing these rules and making them explicit as well as accessible.
- Segregating high value tasks from non-value tasks to enable the RMs to focus on relationship.
- Mobility embedded in process solution to enable a truly digital experience, with flexibility to capture documents any-time anywhere and carrying them through process.
- Building a process wrapper over all existing loan systems to enable 360 degree view and portfolio management.
- Ability for Risk Managers and Analysts to use discretion for better decisions with the access to right information, enabling effective exception handling.
- Build organization's own differentiated lending products and manage their lifecycle with flexibility in lending process and business rules. Faster time to market.

With the right approach, organizations can achieve a truly digital commercial lending platform. Leaders can start with building up the mindset for this goal, map their current processes against the five dimensions, identify the immediate actionable, and leverage the right platform.

What can you do, today?

- *Assess your current lending processes and where current bottlenecks lie.*
- *Identify how you are addressing the five dimensions in your commercial lending processes today.*
- *Identify key differentiators and how a flexible process platform underneath would help in longer term.*
- *If you think we can be of any help, contact us!*

About Newgen

Newgen Software is a leading global provider of Business Process Management (BPM), Enterprise Content Management (ECM), Customer Communication Management (CCM) and Case Management, with a global footprint of 1300+ installations in more than 61 countries with large, mission-critical solutions deployed at the world's leading Banks, Insurance firms, BPO's, Healthcare Organizations, Government, Telecom Companies & Shared Service Centers.

Newgen's Quality Systems are certified against ISO 9001:2008 and Information Security Standard, ISO 27001:2013. Newgen has been assessed at CMMi Level3.

Write to us:

USA & CANADA: info@newgensoft.com

INDIA: corpmktg@newgensoft.com

APAC: asiapac@newgensoft.com

EMEA: emea@newgensoft.com

For sales enquiry, dial:

USA & CANADA: +1 (202) 800 7783

INDIA: +91 11 40773769

APAC: +65 3157 6189

EMEA: +44 (0) 2036 514805, +973-1-619-8002

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www.newgensoft.com