

Business Banking – Loan Portfolio Growth Case

A large regional bank faced a major challenge to grow organically in the face of unexpected losses. As a result of the losses, significant expense reduction measures had been put in place. The head of business banking identified this bank's small business loan portfolio, with over 10,000 borrowers, as a primary segment for growth and outlined a plan to explore additional credit and cross-sell opportunities for the bank's customer facing teams. Regular monitoring of changes in borrower credit worthiness and insights into small business market lending and credit conditions were included in the plan. The bank approached PayNet to support the execution of the plan. PayNet, after assessing the situation, recommended a four point solution to spur growth:

Outreach: Identify a pool of existing borrowers using specific criteria to define the opportunity population. Employ the PayNet AbsolutePD Portfolio Manager "Borrower Profile" report to provide key information to the customer facing teams as the basis to explore additional credit and cross-sell opportunities. PayNet conducts training for those teams on how to read and interpret the Borrower Profile report to support client outreach, and facilitates the delivery of quarterly reports.

Increase Share of Wallet: Calculate the delta between PayNet "High Credit" and loan balance with the bank to formulate capacity for additional credit offerings.

Monitor Changes: Assess movement in AbsolutePD (APD), the probability of default, each quarter to continue refining the target list over time – remove deteriorated Borrowers and add improved Borrowers to credit offering program.

Benchmark Market Conditions: Employ PayNet indices and AbsolutePD Outlook forecast to analyze and understand lending and credit conditions in targeted segments of the Bank's footprint.

PayNet examined the Bank's AbsolutePD data on the Small Business portfolio to explore the potential for growth. The first step was to identify the borrowers that fit the current risk profile of the bank. Next, the pool was narrowed to borrowers which might be able to take advantage of increased borrowing capacity. Assumptions were made for the utilization of increased credit limits on revolvers and acceptance of new term loans to arrive at portfolio growth of 9-10%, representing incremental annual revenue of approximately \$1,912,000.

Defining the Opportunity

- ***Starting Point:*** The bank had over 8,125 active small business borrowers that were present in 3 consecutive quarters (Q1 2015, Q2 2015, and Q3 2015). Recently-observed product mix was 64% Term Loan/36% Revolver.

- **Credit Worthiness:**
 - APD must show quarter over quarter consecutive improvement in the 2 most recent periods.
 - The initial borrower APD must be <2%.
- **Demonstrated Borrowing Capacity:**
 - The Bank's aggregate exposure to the individual borrower must not exceed 50% of "high credit" (where high credit is defined as the most the borrower has owed at any given point in time across all lenders in the PayNet Database).

Portfolio Opportunity Population

- 1,998 borrowers (24.6% of the active borrowers) qualified for the loan growth initiative using the above criteria. These borrowers carried a current balance (using the most recent period's data) of \$336 Million.

Opportunity Borrowers										
Borrower Name Borrower Number	State	Business Unit Portfolio	Exposure (\$000)			AbsolutePD	APD Chg	Number of Lenders	Status	Last Serious Delinquency
			Current	Change	Wtd PD					
			\$ 512,000	\$-75,440	\$32,325	1.08%	-0.05%			
Angel Dealer 5005	CT	Business Banking Current	958	-13	14	1.43%	-0.13%	14	Current	10/12 Warn 30
Horned Frogs Grains 31403	TX	Business Banking Current	953	-762	14	1.45%	-0.13%	3	Current	8/96 Warn 30
Emeralds Transport 27752	OR	Business Banking Current	947	9	14	1.43%	-0.23%	3	Current	7/12 Warn 30
Geoducks Marine Shipping 35110	WA	Business Banking Current	946	-209	14	1.53%	-0.20%	5	Current	1/04 Warn 60
Beer Dairy 1259	AR	Business Banking Current	940	-41	14	1.51%	-0.01%	6	Current	8/10 Warn 30
Pioneers DDS 22905	NJ	Business Banking Current	939	430	14	1.52%	-0.13%	7	Current	Never
Monarchs Dealer 33585	VA	Business Banking Current	935	65	14	1.52%	-0.23%	12	Current	1/13 Warn 30
Golden Rams Engineering 28040	PA	Corporate Current	908	-559	14	1.54%	-0.10%	1	Current	Never
Lutes Bookstore 34926	WA	Branch Current	868	82	14	1.61%	-0.23%	50	Current	4/13 Warn 30
Lumberjack & Son Farm 1886	AZ	Branch Current	866	230	14	1.53%	-0.20%	27	Current	Never
Red Storm Marine 32833	UT	Business Banking Current	839	45	14	1.62%	-0.05%	5	Current	12/09 Warn 30
Meads Toy Store 2419	AZ	Branch Current	835	-68	14	1.73%	-0.04%	24	Current	11/11 Warn 30
Mustang Auto Shippers 21136	ND	Business Banking Current	779	-221	14	1.85%	-0.05%	11	Current	2/14 Warn 60

Showing 1 to 13 of 1,998 borrowers

Portfolio Growth Analysis:

- Using the difference between the borrowers' aggregate loan balances with the Bank and the PayNet high credit, total opportunity was calculated at \$1.5 Billion.
- A product mix ratio of 64% Term Loan/36% Revolver was applied to refine the opportunity for extending additional credit in the form of Term Loans and Revolvers: \$960M and \$540M, respectively.
- A 25% acceptance rate in Term Loans, and 50% utilization for the increased lines in Revolver was applied to project new Small Business Banking Portfolio Loan Growth of \$510 Million, to 1,998 borrowers representing loan portfolio growth of 9.5%.

- Using a 75 basis point spread, and assumptions of 25% acceptance rate for Term Loans and 50% utilization for Revolvers, incremental annual revenue would total \$1,912,000 (\$900,000 for Term Loans and \$1,012,000 for Revolvers).

Ongoing Strategy for Client Retention/Sales Coordination

Target Sales Efforts on Areas of Greatest Opportunity:

Client Retention/Sales: Geographical analysis of the potential borrower pool showed the largest opportunity. The \$1.5B in incremental loans broken down by state showed concentrations in 5 states.

Client Retention/Sales: Similarly, analysis of the potential pool on a broad industry basis identified concentrations in 3 major NAICS segments:

1. Transportation
2. Agriculture
3. Retail

Client Retention/Sales: The focus of the sales initiative is narrowed by finding the intersection between industry/state potential. Transportation, previously identified as having the largest “potential” of any single industry segment, presents the greatest opportunity in states One and Two – 233 borrowers in these states show \$106 Million in potential new loans.

Review Market Conditions:

Lending Activity: The Bank benchmarks Transportation lending activity within states One and Two to identify warning of possible investment problems in these markets utilizing PayNet Small Business Lending Index at www.sbinsights.net.

Loan Delinquency: The Bank benchmarks loan performance for state One by assessing 31-90 day delinquencies for signs of financial stress in the context of state One and overall US utilizing PayNet Small Business Delinquency Index at www.sbinsights.net.

Default Rates: The Bank benchmarks state One’s Transportation default rates for the past 12 months in the context of state One and US with PayNet Small Business Default Index at www.sbinsights.net.

Refine Sales Target List of Individual Borrowers

Client Retention/Sales: The Bank compiles the list of target clients from the overall pool for further examination and runs APD Portfolio Manager “Borrower Profile” reports (shown below) for detailed analysis of each individual borrower.

Summary

The Bank refined its sales program and employed PayNet’s AbsolutePD and indices to achieve 9.5% targeted growth in its loan portfolio with \$1,912,000 increased revenue. PayNet AbsolutePD enabled management to quickly filter the small business loan portfolio to identify credit-worthy

borrowers which were evaluated further to identify increased credit capacity. PayNet's Small Business Indices are utilized to benchmark this pool of high potential borrowers against market performance by state and industry. In addition, the APD Borrower Profile Report is employed by relationship managers and centralized risk personnel to synthesize borrower credit-worthiness and benchmark vis-à-vis geographic and industry peers. With quarterly APD updates, the Bank monitors borrowers for deteriorating or improving credit risk.

Borrower Profile Report

As reported 10/1/2015

Borrower Name

Mustang Auto Shippers

Borrower No.

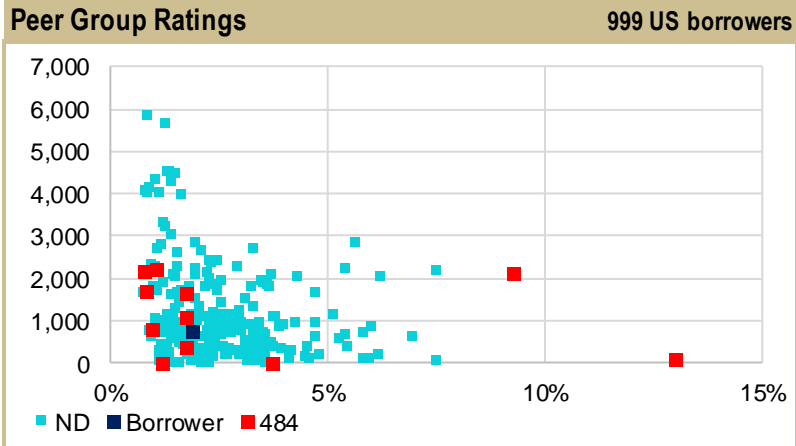
21136

State Borrower Exposure Business Unit Branch Portfolio
ND \$ 779,089 Business Banking Mustang Current

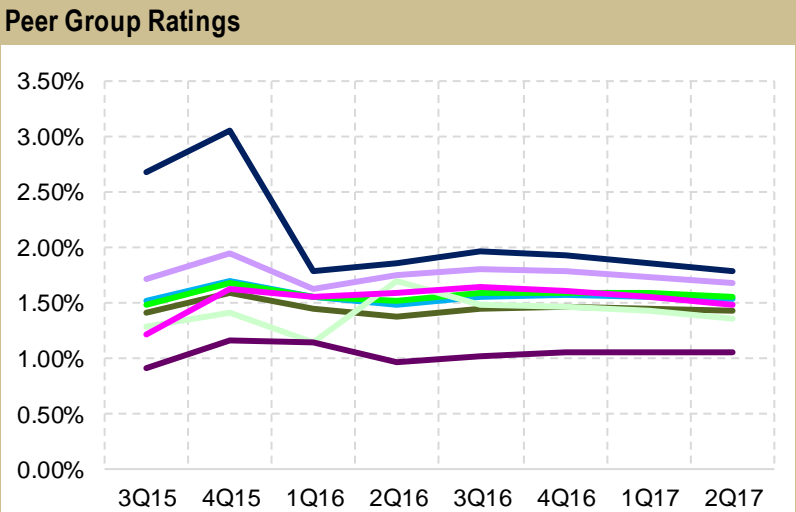
NAICS
Specialized Freight - Long (484230)

\$ 779,089 total for borrower and 1 affiliate

Rating Characteristics			
System	4	AbsolutePD	1.85%
AbsolutePD Ratings			
		Prior Quarter	Prior Year
Scale	Current		
Lender	3	3	2
PayNet (1-20)	8	7	7
Industry Segment	Transportation		
Rating Factors (for latest APD)			
+ Large Business Size/Extensive Borr...			
+ Recent / Overall Prompt Payments			
+ Long Time Borrower			



Rating Characteristics			
Oldest Contract Date	2/10		
Newest Contract Date	7/14		
High Credit Ever	\$1,553		
Total Ever Borrowed	\$2,732		
Total Annualized Pmts	\$187		
No. of Lenders	4		
Delinquency	31-60 days	61-90 days	>90 days
Exposure	0	0	0
Payments()	0	0	0
Last Occur.	8/12	2/14	never
No. Occur.	76	3	0



Affiliated Entities (\$000)			
Borrower Name	Ratings		
Borr. Number	Exposure	Lender	
Portfolio	Last Rpt	Related by	APD

	Borr 21136	All Borr	Rating 4	SBU Comm	Branch Mustang	State ND	NAICS 484	Segment Transp
3Q15	2.67%	1.51%	1.41%	1.48%	1.29%	0.91%	1.22%	1.71%
4Q15	3.06%	1.69%	1.58%	1.68%	1.41%	1.16%	1.62%	1.94%
1Q16	1.79%	1.55%	1.44%	1.55%	1.14%	1.15%	1.56%	1.63%
2Q16	1.85%	1.49%	1.38%	1.52%	1.69%	0.97%	1.59%	1.75%
3Q16	1.96%	1.56%	1.45%	1.59%	1.49%	1.02%	1.64%	1.81%
4Q16	1.93%	1.57%	1.46%	1.59%	1.46%	1.05%	1.61%	1.79%
1Q17	1.86%	1.56%	1.45%	1.58%	1.42%	1.06%	1.55%	1.74%
2Q17	1.78%	1.53%	1.43%	1.55%	1.36%	1.05%	1.48%	1.67%