



C&I Strategy for 2018

Taking the Risk
Out of Small
Business Lending

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C&I in the U.S.

28 Million Business
400 NAICS
3,300 Counties

1.3 Million Possibilities

Thanks!

2018 C&I STRATEGY

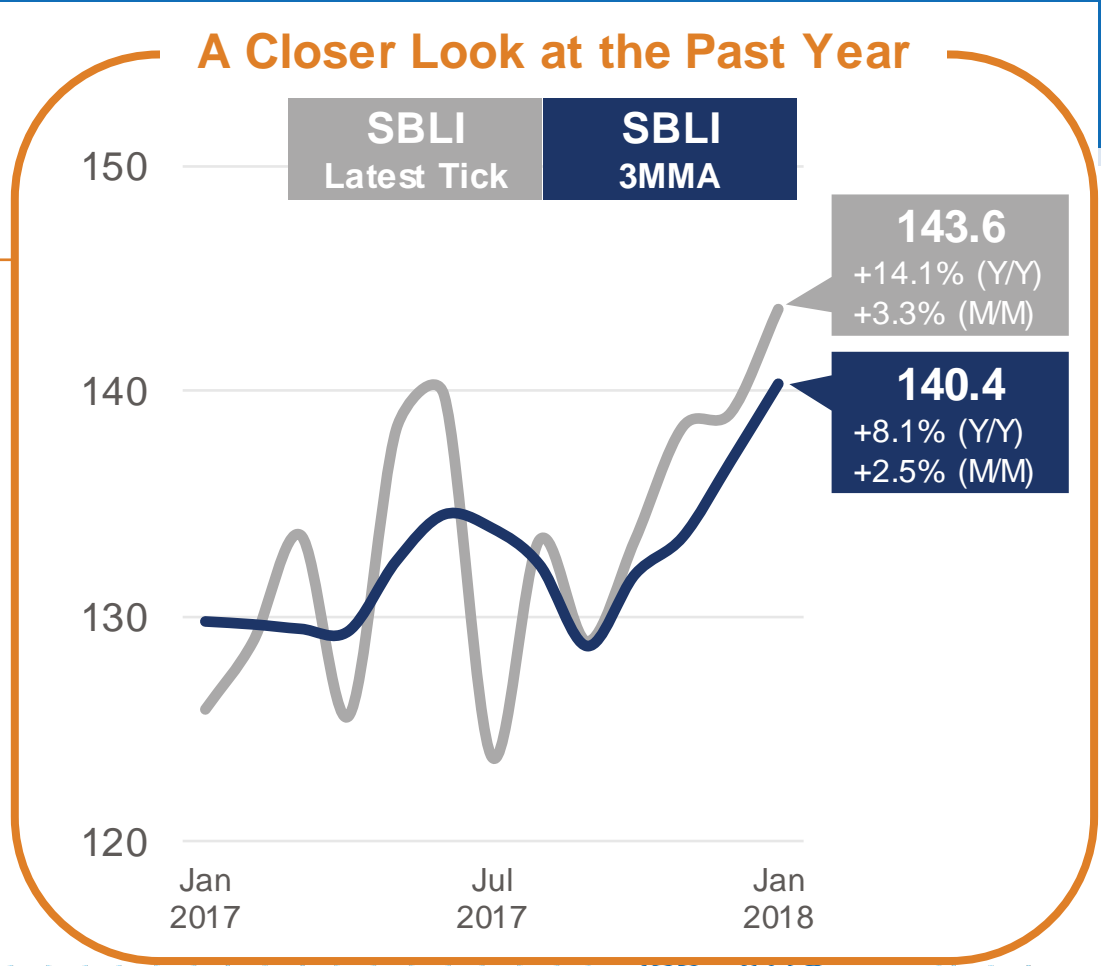
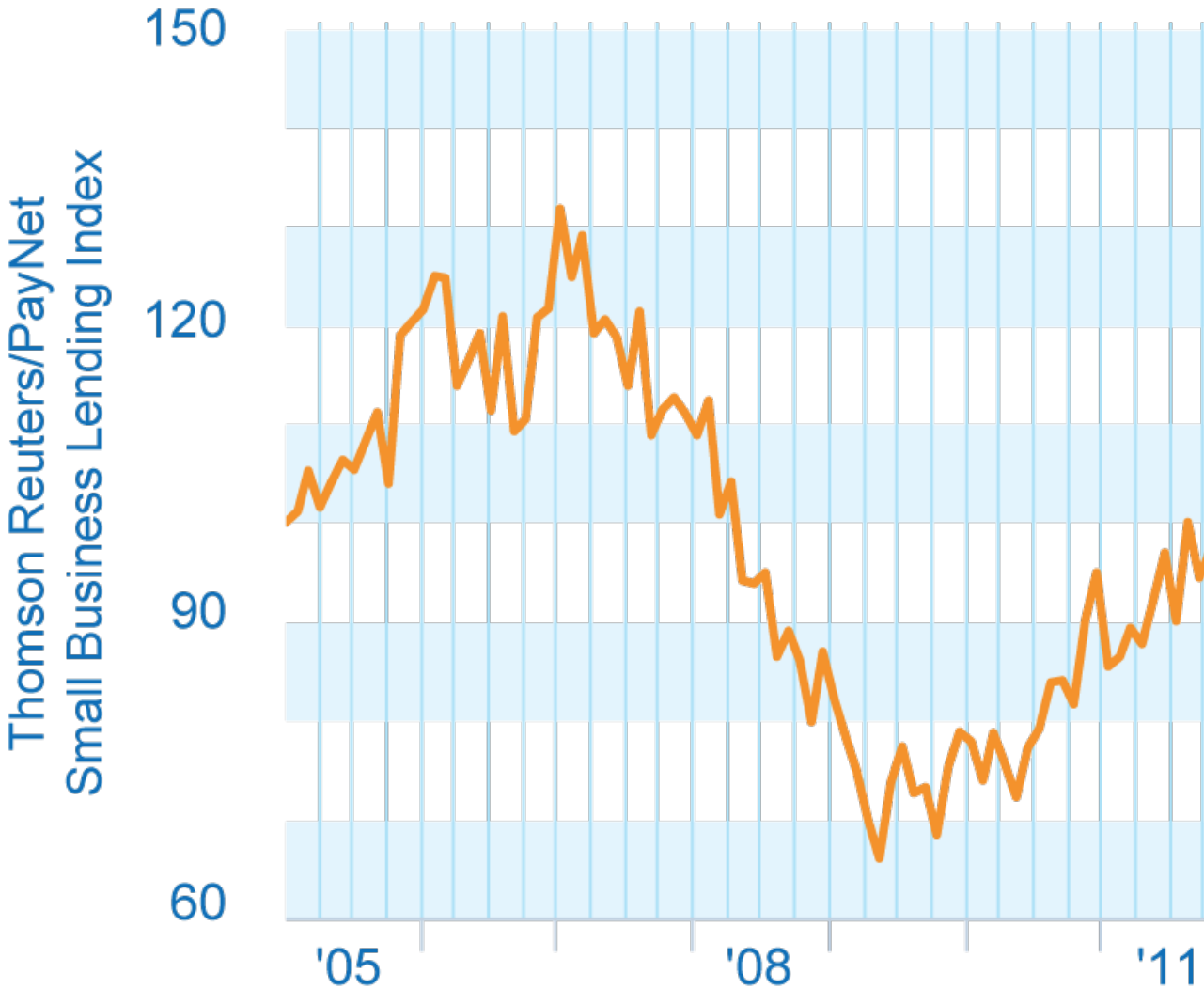
Adopting Financial Technology To Win At C&I

William Phelan, President, PayNet, Inc.



2018 C&I Credit
Conditions
NATIONAL VIEW

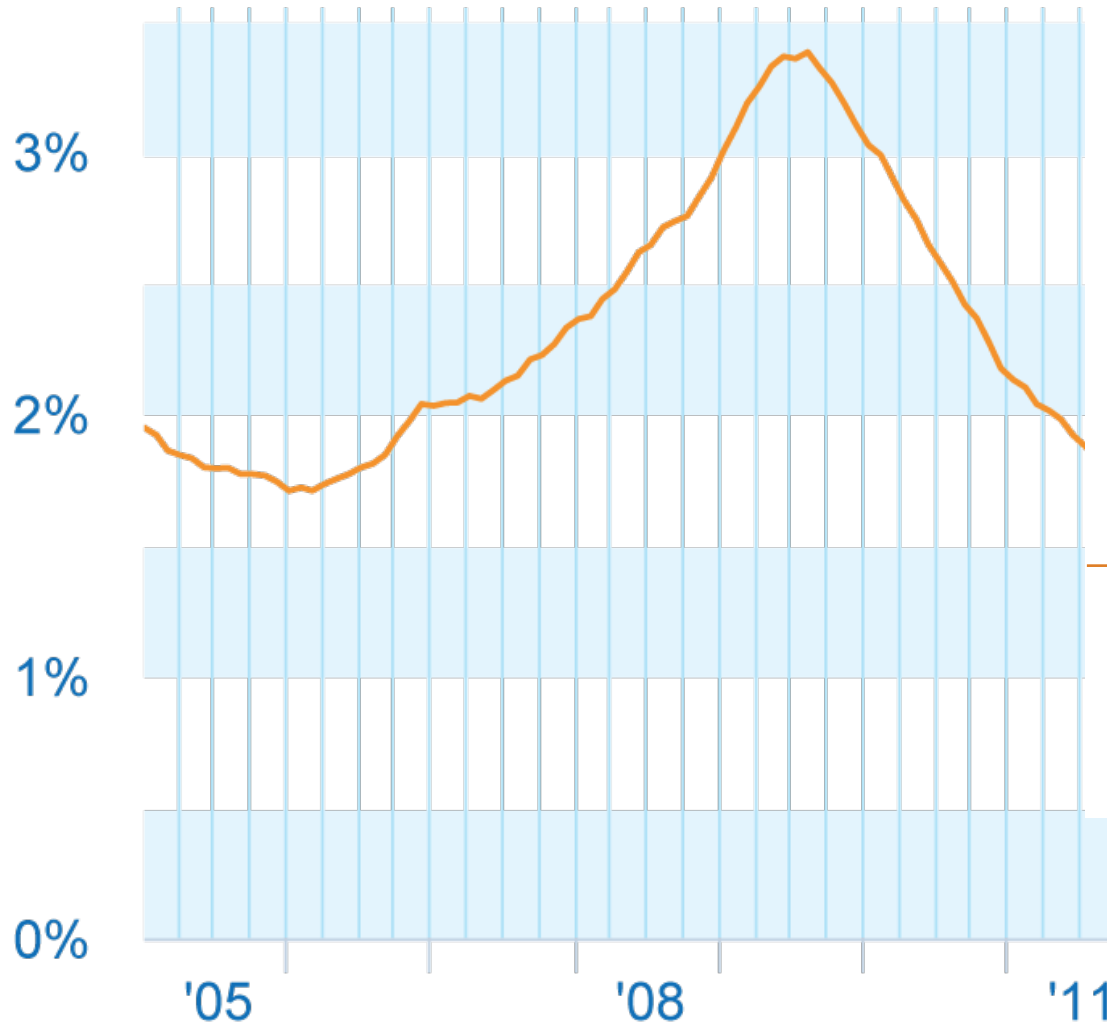
Lending Activity – National



Jan. 2018
 ● US: 143.6

Loans Past Due – National

Thomson Reuters/PayNet
Small Business Delinquency Index
(31-90 Days Past Due)

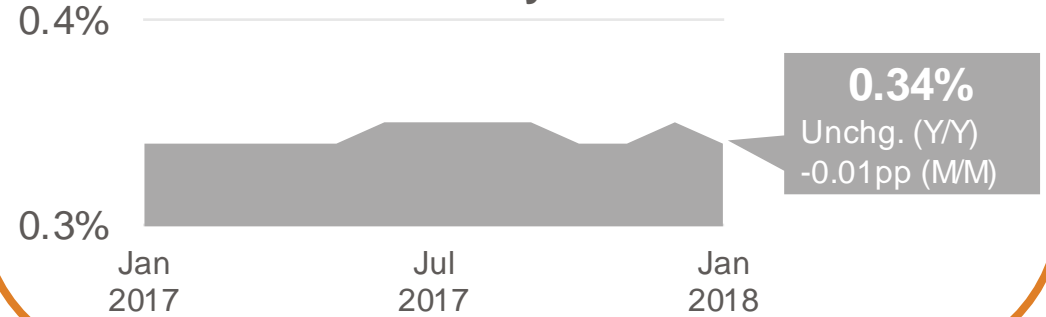


A Closer Look at the Past Year

SBDI: 31 – 90 Days Past Due



SBDI: 91 – 180 Days Past Due





2018 DEFAULT FORECAST:

NATIONAL



WHERE ARE DEFAULTS HEADED?



The main challenge for lenders in the U.S.:

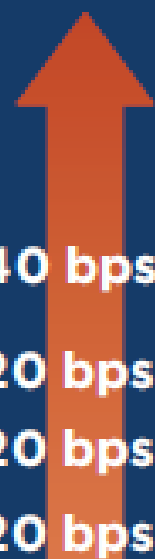
BORROWERS



SHOW MORE
RECENT & FREQUENT
LOAN DELINQUENCIES

INDUSTRIES WHERE

RISK IS ON THE **RISE**



ACCOMMODATIONS & FOOD		+40 bps
CONSTRUCTION		+20 bps
HEALTHCARE		+20 bps
RETAIL		+20 bps



2018 C&I Strategy

NATIONAL VIEW

Commercial & Industrial (C&I) Lending

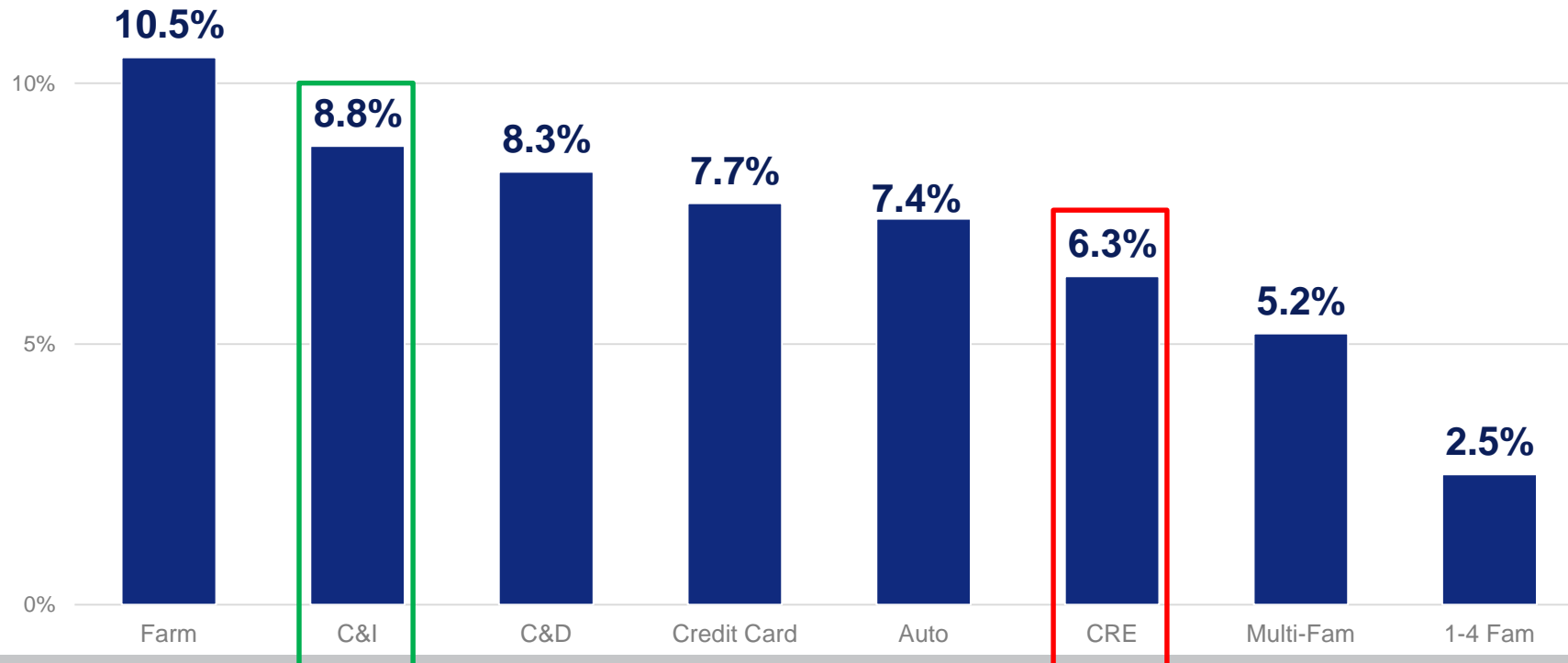
One Of The Highest Return Businesses For Banks



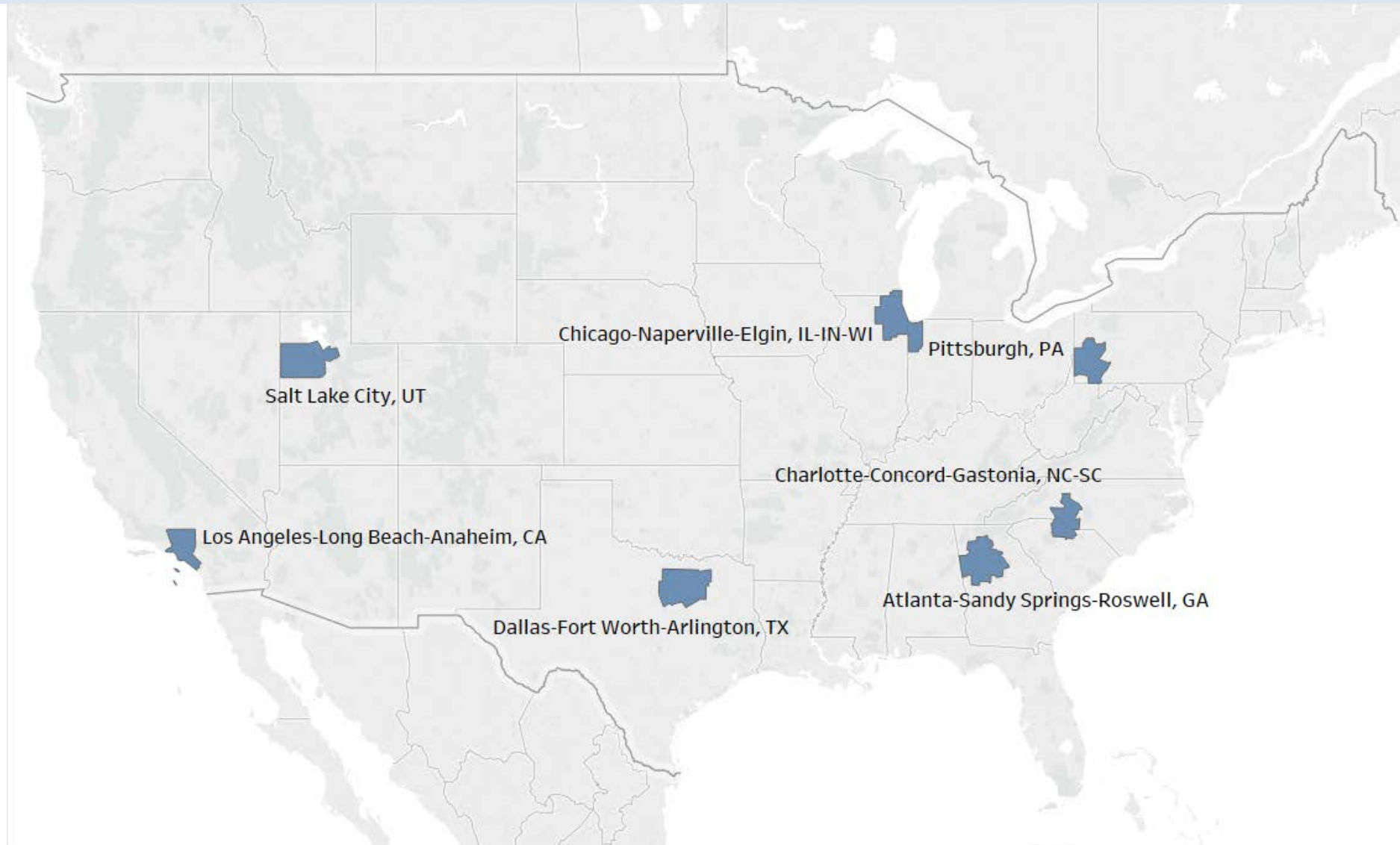
- CRE's 6.3% ROE is below the industry's cost of capital
 - Many banks are not compensated for risk of heavy CRE exposure
 - Banks with high CRE concentrations rarely deliver steady dividends or decent ROE
- RICK PARSONS, Author of "Investing in Banks" (2016)

Average 2014 Return on Equity (ROE)

Average for Top 200 Banks with Greatest Exposure to Loan Type



Bank originations of less than \$1M in selected metropolitan statistical areas (MSAs) across the U.S.

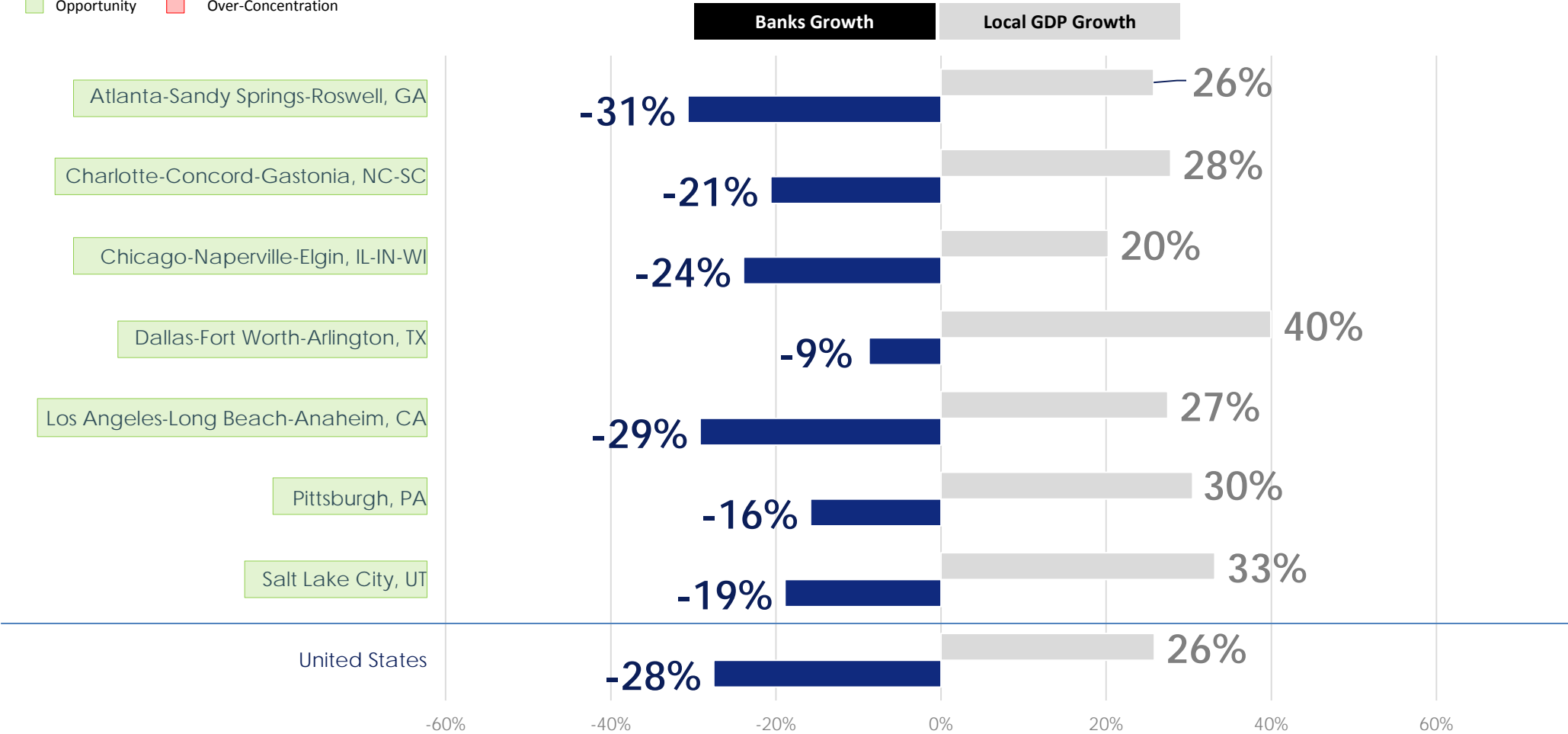


In several MSAs, Bank's C&I loan growth has not reflected local economic conditions, suggesting that geographic targeting could be improved.

Local GDP Growth vs. Bank's C&I Loan Origination Growth

By MSA, 2008 - 2016

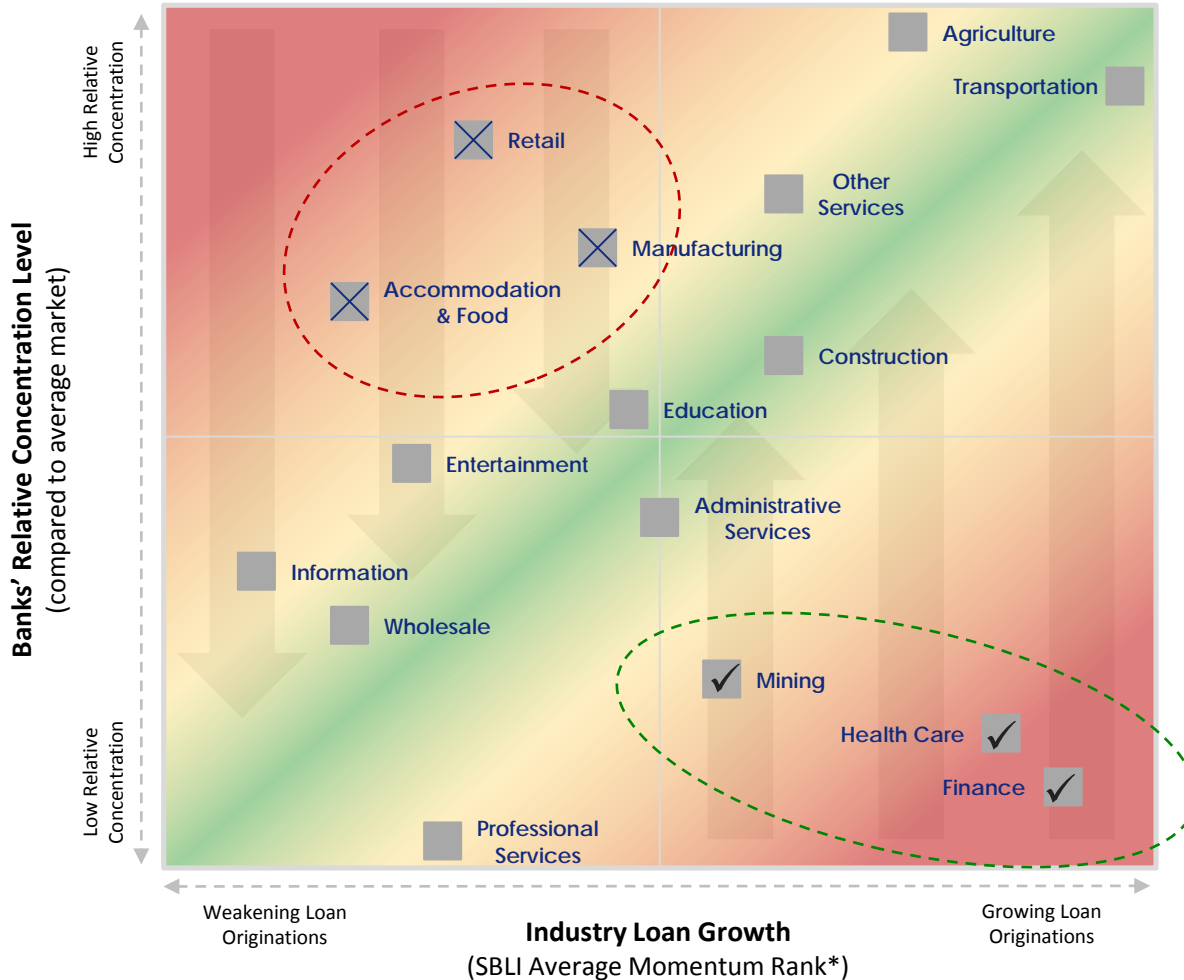
Opportunity Over-Concentration



Banks could also improve their lending portfolio by targeting industries with uncaptured loan originations growth . . .

Industry Opportunity Matrix

Concentration and Growth of Bank Lending Portfolios by Industry



Opportunities

Industry	Industry Loan Growth	Bank Share	Market Share
Finance	6.5	7.94%	10.91%
Healthcare	5.5	11.07%	12.23%
Mining	1.0	0.39%	1.38%

Over-Concentrations

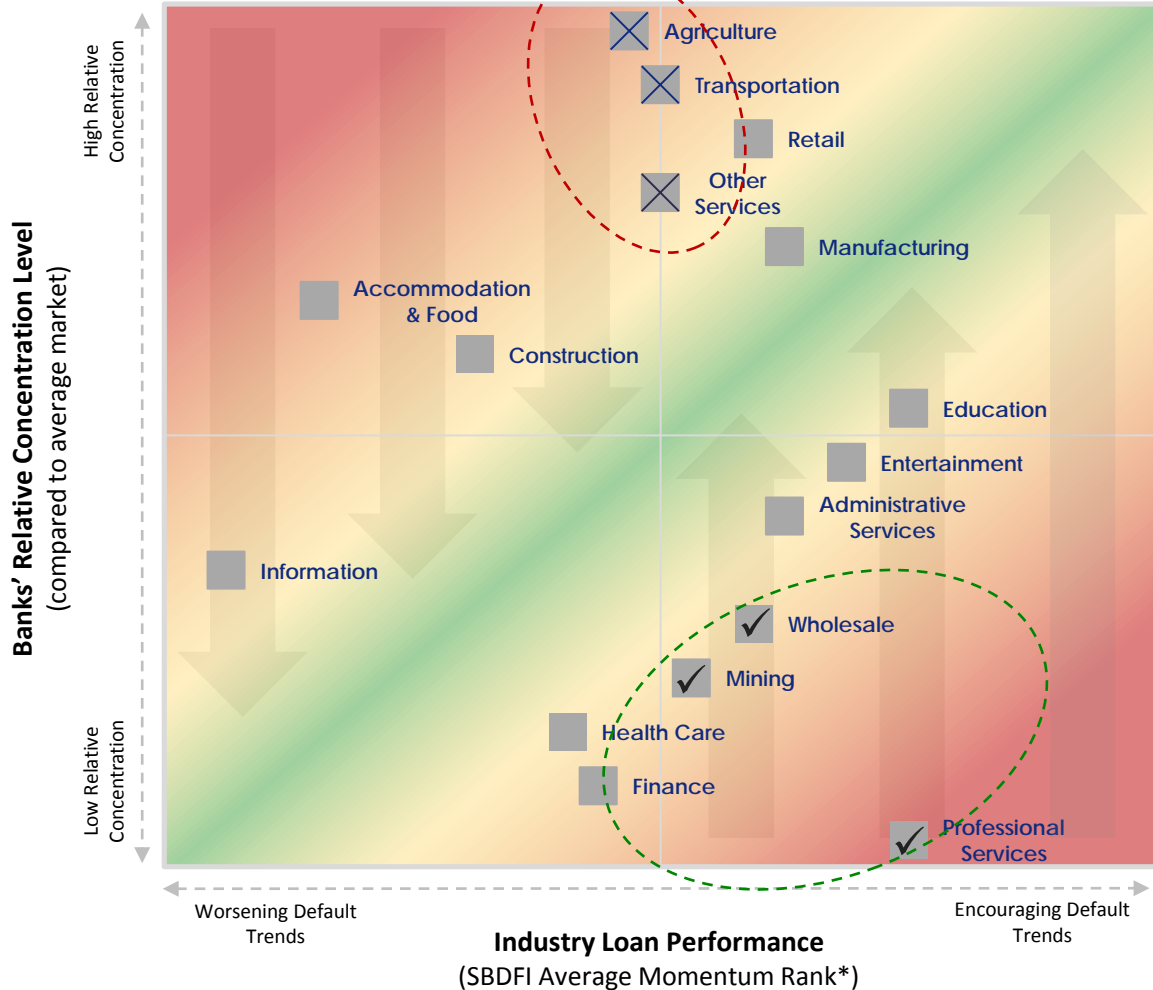
Industry	Industry Loan Growth	Bank Share	Market Share
Accom. & Food	-5.0	5.33%	5.29%
Retail	-3.0	9.28%	6.92%
Manufacturing	-1.0	10.10%	9.85%

*Note: SBLI Average Momentum Rank = Average of Difference Between 6 Mo (annualized) and year-over-year growth rank and Difference Between 3 Mo (annualized) and year-over-year growth rank in the local market (Centered)

... and by pursuing industries with strong loan performance.

Industry Opportunity Matrix

Concentration and Performance of Bank Lending Portfolios by Industry



Opportunities

Industry	Industry Loan Performance	Bank Share	Market Share
Prof. Services	4.0	11.10%	14.85%
Wholesale	1.5	6.99%	7.95%
Mining	0.5	0.39%	1.38%

Over-Concentrations

Industry	Industry Loan Performance	Bank Share	Market Share
Agriculture	-0.5	7.89%	1.55%
Transportation	0.0	6.12%	3.08%
Other Services	0.0	7.04%	6.65%

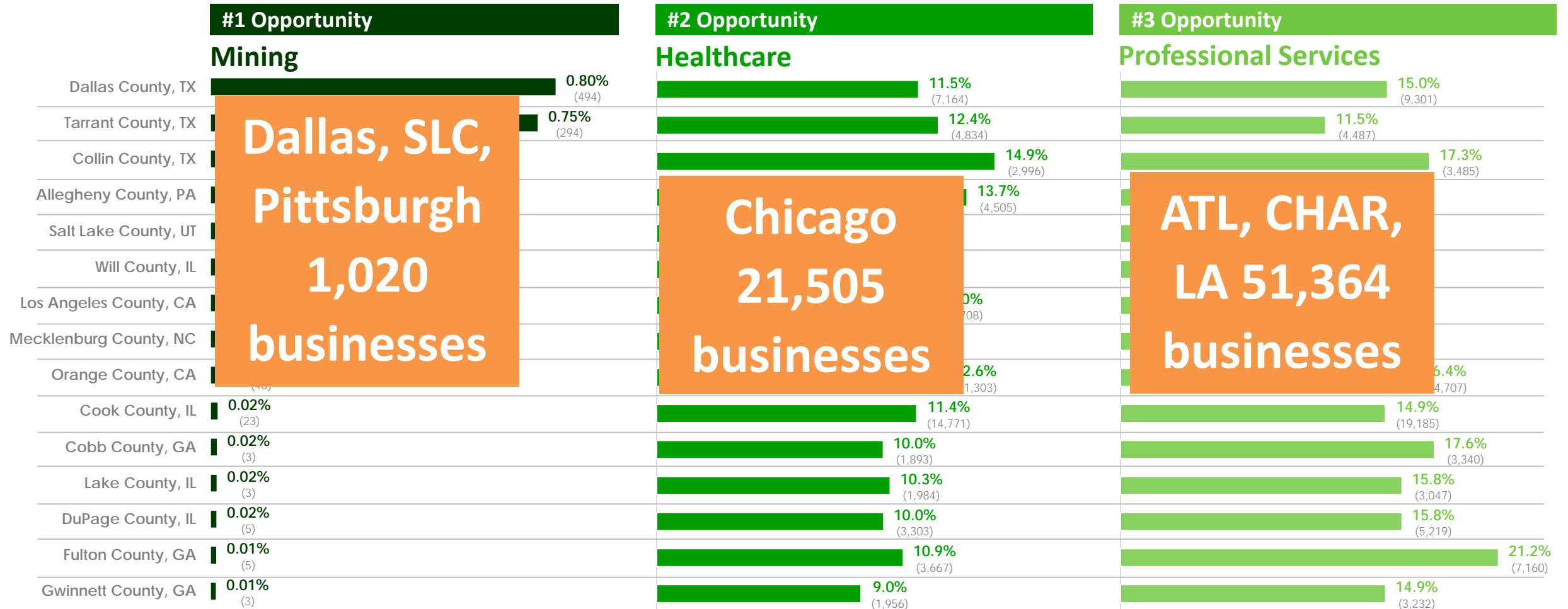
*Note: SBDFI Average Momentum Rank = Average of Change in Default Rate Over Last Three Months rank and Current SBDFI Level rank in the local market (Centered)

Source: PayNet; Census Bureau; BEA; SBA

To take advantage of industry opportunities, banks should target counties in the U.S. where underutilized industries have a strong presence . . .

Geographic Distribution of Opportunities

Share and Number of Establishments in Top Opportunity Industries*, by County



*Note: The top opportunity industries are determined via a composite score that accounts for the industry's loan growth, loan performance, and banks' relative concentration level in the industry.

CURRENT Underwriting and Review Process

Commercial Underwriting Process

30 Days
10 loans/Month
\$5,000/application

Credit Review Metrics:
2 days to complete 1 loan
 Analyst can produce 120 loans/mo.

Challenger Bank

Business Borrower

Manager

- Collect F/S
- Build Relationship via "Centers of Influence"

Spreading Dept.

- Conduct F/S spreads

Credit Dept.

- Underwrite
- Credit Write-Up

Approval

- President \$2m - \$5m
- Credit Cmte \$5m - \$10m

Data/Tools:

- Moodys spreads
- FICO personal score
- Lexis Nexis Public Records

Underwriting:

- Uses spreads to do Cash Flow Analysis
- Add PN and DNB to analysis
- Get Behind the Numbers to Tell the Story
- \$4m deal used 52 pg. write-up
- \$500k deal used 5 pg. write-up

Credit Review

- Same Underwriting Process
- All credits Quarterly
- All Credits Annually

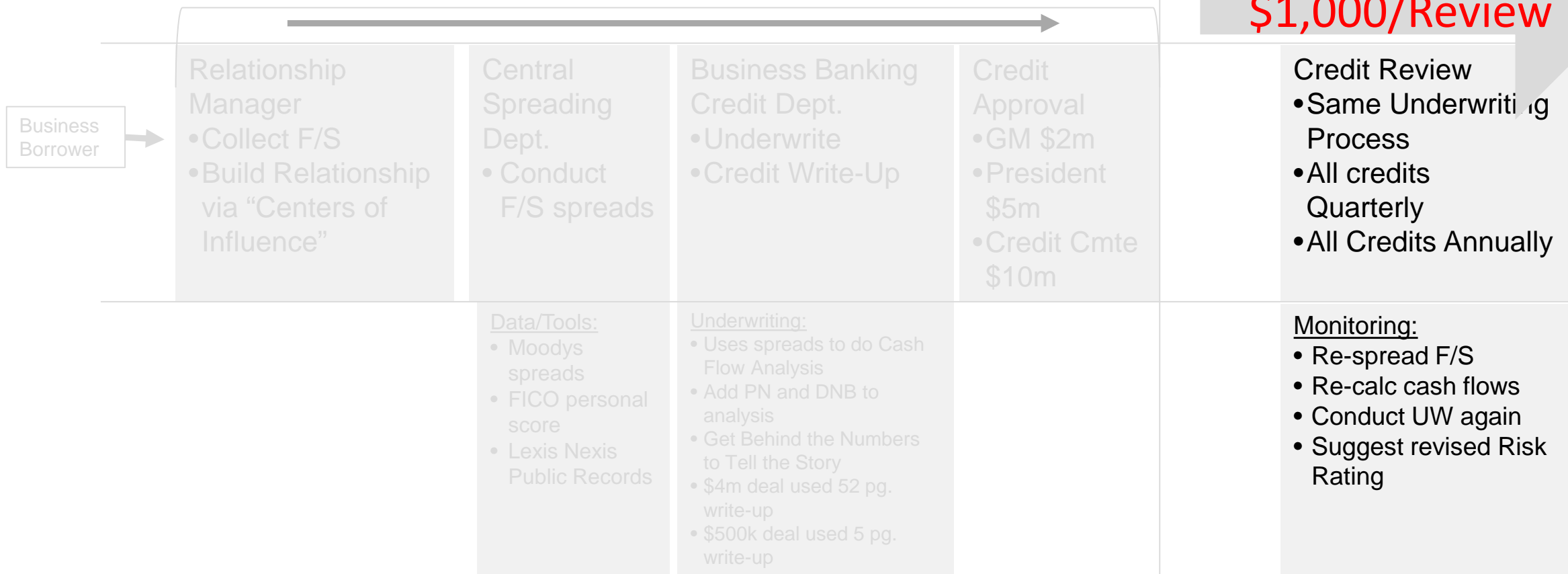
Monitoring:

- Re-spread F/S
- Re-calc cash flows
- Conduct UW again
- Suggest revised Risk Rating

CURRENT Underwriting and Review Process

Challenger Bank

Underwriting Metrics:
7-30 days to complete 1 loan
 Analyst can produce 10 loans per month



Credit Review:

2 Days
120 loans/Analyst
\$1,000/Review

NEW UNDERWRITING PROCESS

Portal

Application

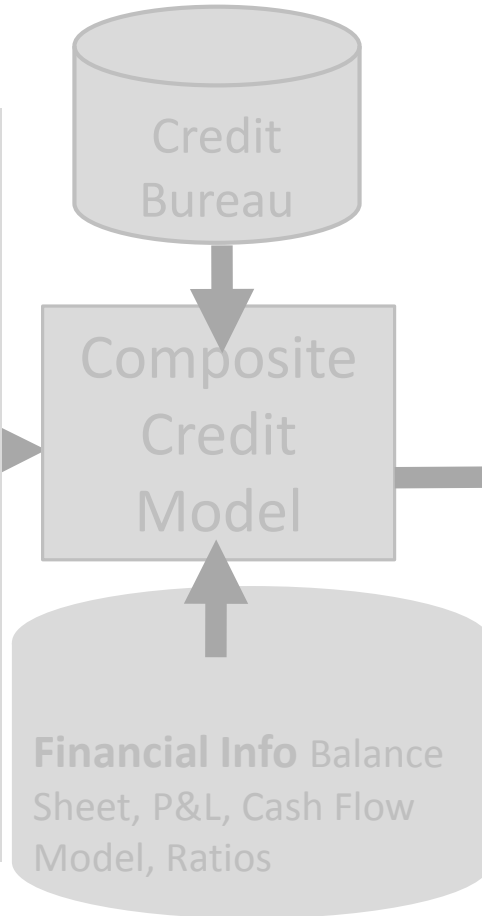
Credit Application

- Borrower/Guarantor:
- Name, Address,
 - Years In Biz,
 - Legal Structure
 - TIN
 - History,
 - Business Description,
 - Management Team

- Terms and Conditions
- Credit Structure, Purpose of Credit Facility
- Pricing, Relationship Models, Cross Sell Strategies

Decision Engine

Data Gathering & Automatic Adjudication



Credit Policy/Process

Automated Review

Credit Analyst Review (<\$100k)

- Commercial Credit Scores
- Consumer Credit Score

Manual Review

Credit Analysis (\$100k-\$1M)

- DSC, D/E Ratios
- Appraisal / Analysis
- EL = LGD x PD
- Competitors
- Collateral
- Industry Analysis
- Significant Events

Compliance Checks

Terms and Conditions
Credit Structure

Approve/
Decline

Approve/
Decline

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Application

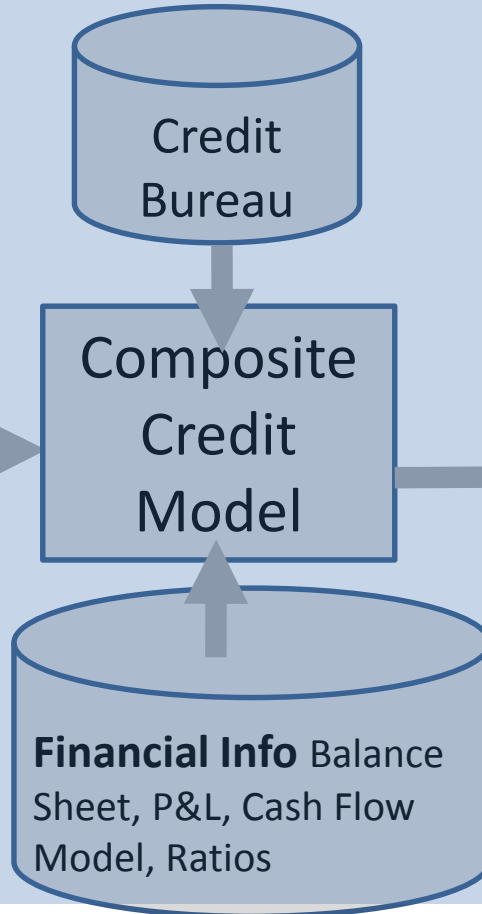
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- Credit Score
 - Industries

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Composite Credit Model

Credit Bureau

Financial Info Balance Sheet, P&L, Cash Flow Model, Ratios

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Underwriting - Shorten Response Times To Commercial Customers

	Small Balance	Middle Balance	Large Balance
Credit Size	≤ \$100,000	\$100,000 - \$1 million	> \$1 million
Objective			
Risk			
Capacity			
	10 applications/analyst/month		30 days/application
RESULTS			
	60 – 120 applications/ analyst/month		~5 days / application

NEW CREDIT REVIEW PROCESS

4X Per Year By Allocating Resources To Highest Risk Loans

	Low Risk	Middle Risk	High Risk
Portfolio Mix	95%	2.5%	2.5%
Re	 <p>100 – 200 reviews/analysts/year</p>		
Re			
Pro			
Eff			
RESULTS			
	2,000 reviews/analysts/year		

PAYNET CAN HELP IDENTIFY GROWTH OPPORTUNITIES AND AUTOMATION

Increased profits via opportunity analyses

- Through geographic and industry targeting, **C&I earning assets by \$110 Million** from 2007 – 2015 while also managing risk effectively.
- **\$3.4 million** extra interest each year.

Credit process efficiencies through automation

- Incorporating industry-leading risk analysis tools (e.g., PayNet's Credit Review Express, PayNet's C&I Express) into banks' credit processes adds scale:
 - Increase application handling from 10 applications/month to 60;
 - Increase annual reviews from 100 – 200 reviews per year to 2,000.
- Typical **\$2B bank saves \$680,000 in underwriting costs and \$570,000 in review costs each year** while also managing risk effectively.

Note: Assumes 230 loan applications and 920 borrower reviews per year

Source: FDIC; PayNet



THANK YOU
SBInsights.paynetonline.com

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