



C&I Strategy for 2018

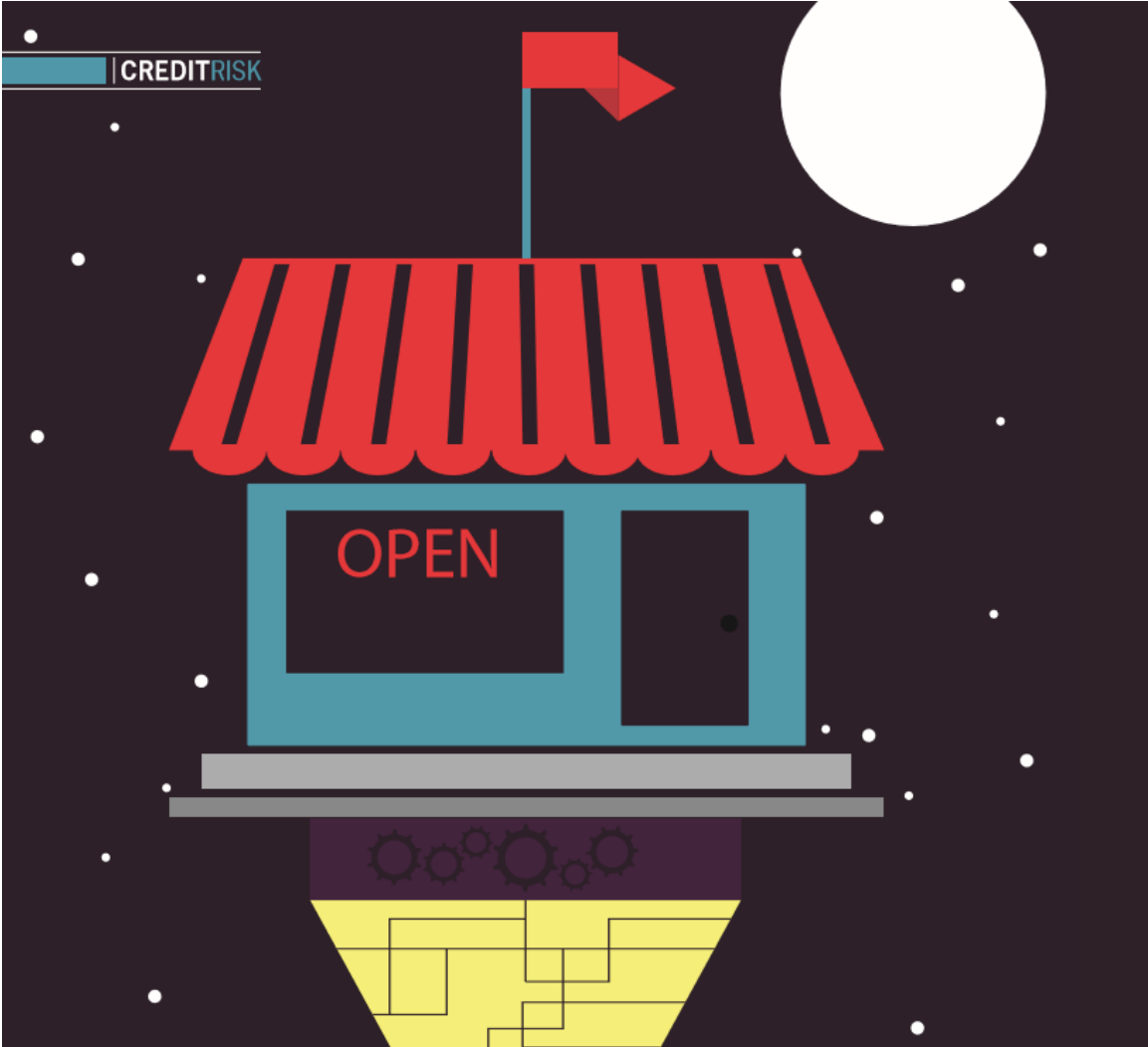
*More Knowledge,
Better Decisions*

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CREDITRISK

PREPARING FOR MAIN STREET LIFTOFF

BY WILLIAM PHELAN

LAST YEAR at this time, big companies were expanding aggressively, as witnessed by the 10.4% jump in the S&P 500 index over the past year. Big technology companies in particular have had a great run: The S&P technology index has averaged increases of 16.3% over each of the last three years.

During that time, Main Street America, which comprises 28 million small businesses and accounts for almost half of private GDP, remained hunkered down. These businesses were not aggressive in borrowing money from banks in any great amounts. Nor were they willing to take the risk to expand property, plant, and equipment, to buy more tools, to add new services, or to hire more employees.

But after remaining patient and holding back on aggressive investment, small businesses are now getting into the game with aggressive increases in borrowing and investment. We are witnessing Main Street liftoff. The real issue

happened. The Bureau of Economic Analysis reported only a 0.1% expansion in U.S. GDP in the fourth quarter of 2012.

In this latest report, the business cycle remains in the low-risk expansion phase. Risk is at all-time lows as delinquency rates for loan 90 days past due are less than 0.35%. Expansion is occurring, although at a slow rate, as measured on a quarterly basis. Fiscal challenges loom still for the U.S., but the risk of contraction and an end to the current business cycle seems to have lessened. (See Figure 1.)

Recent Investment Activity

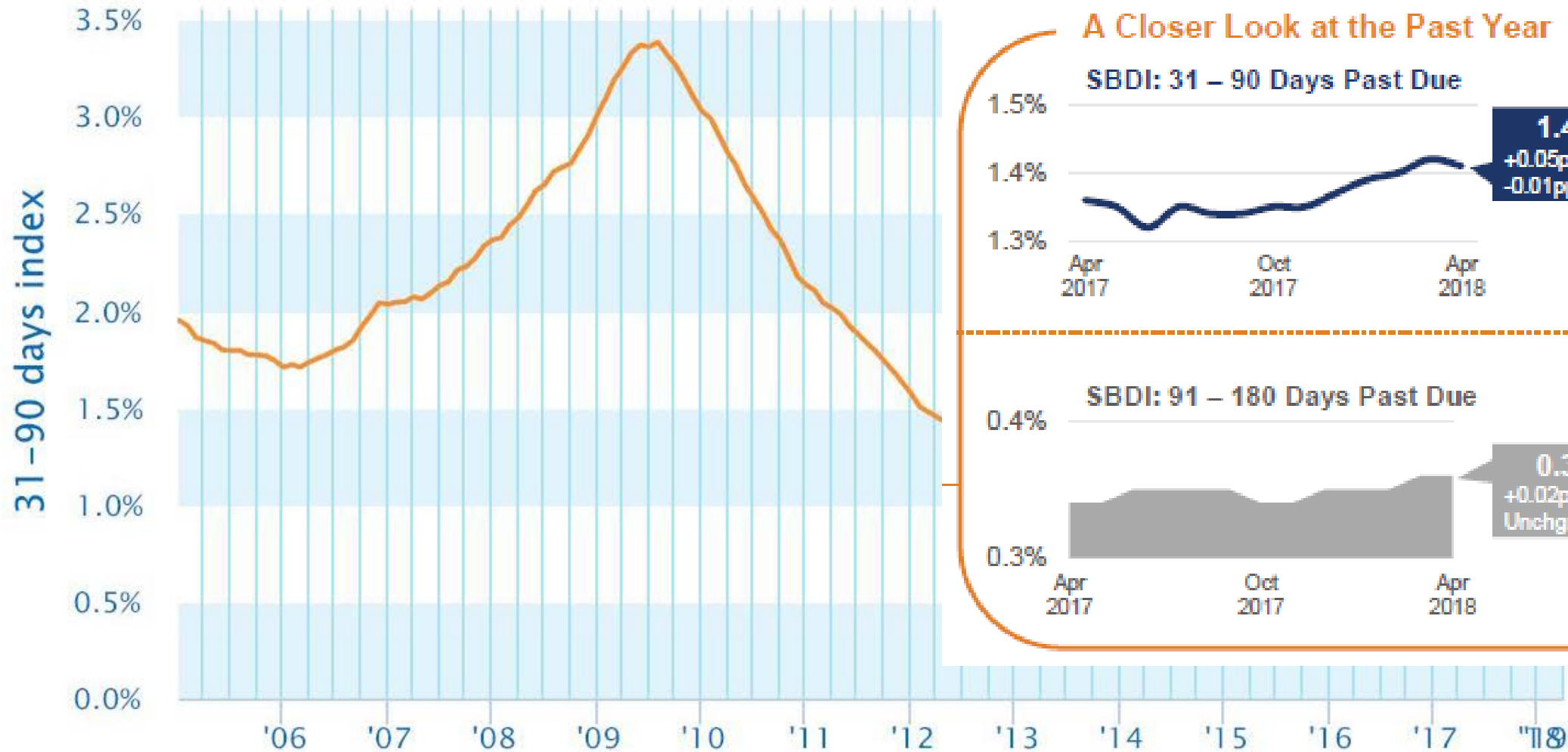
Main Street liftoff is clear from the recent acceleration in borrowing by small businesses. Investment by small businesses took off beginning in October 2017 and has continued unbroken for the past five months. The February 2018 annualized increase of 12% was preceded by a 14% rise in January after healthy advances of 4% and 7% in December

Lending Activity – National



Thomson Reuters / PayNet SBLI

Loans Past Due – National



Thomson Reuters / PayNet SBDI



2018 DEFAULT FORECAST:

NATIONAL



WHERE ARE DEFAULTS HEADED?



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

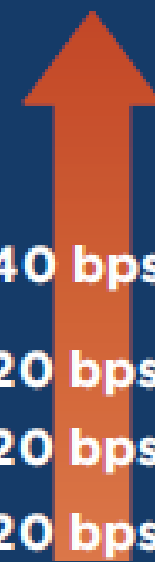
BORROWERS



SHOW MORE
RECENT & FREQUENT
LOAN DELINQUENCIES

INDUSTRIES WHERE

RISK IS ON THE **RISE**



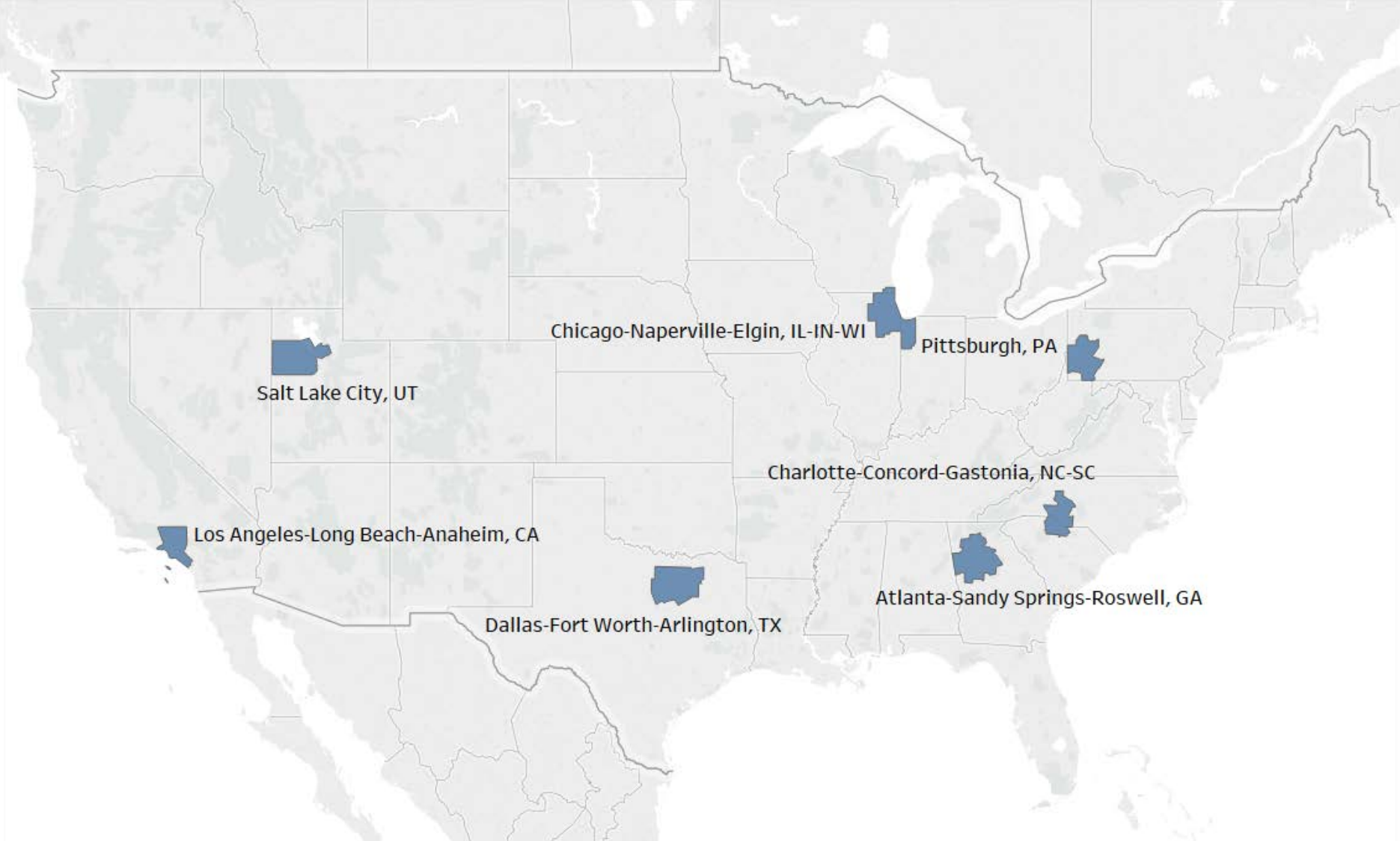
ACCOMMODATIONS & FOOD		+40 bps
CONSTRUCTION		+20 bps
HEALTHCARE		+20 bps
RETAIL		+20 bps



2018 C&I Strategy

NATIONAL VIEW

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

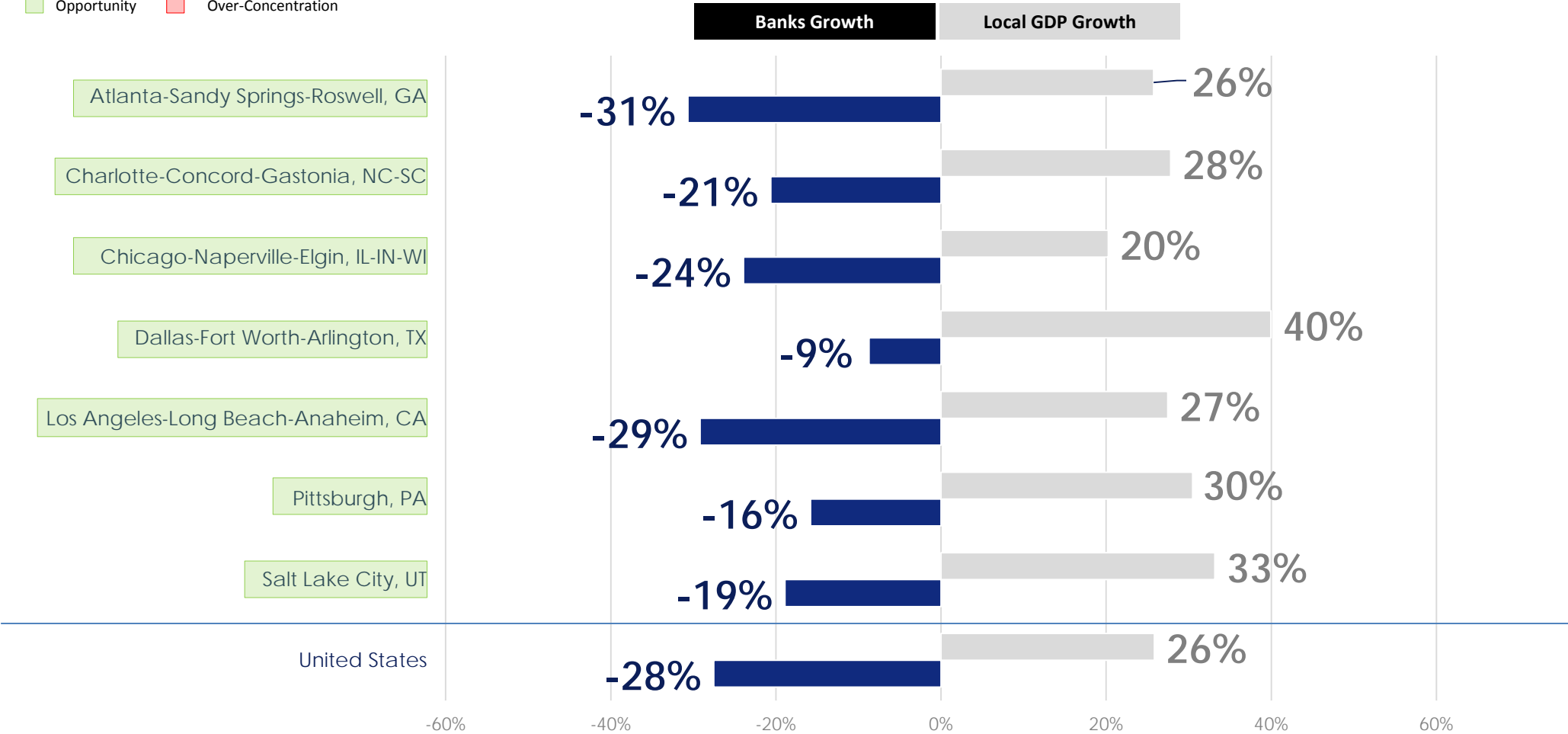


In several MSAs, Bank's C&I loan growth has not reflected local economic conditions, suggesting that geographic targeting could be improved.

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

By MSA, 2008 - 2016

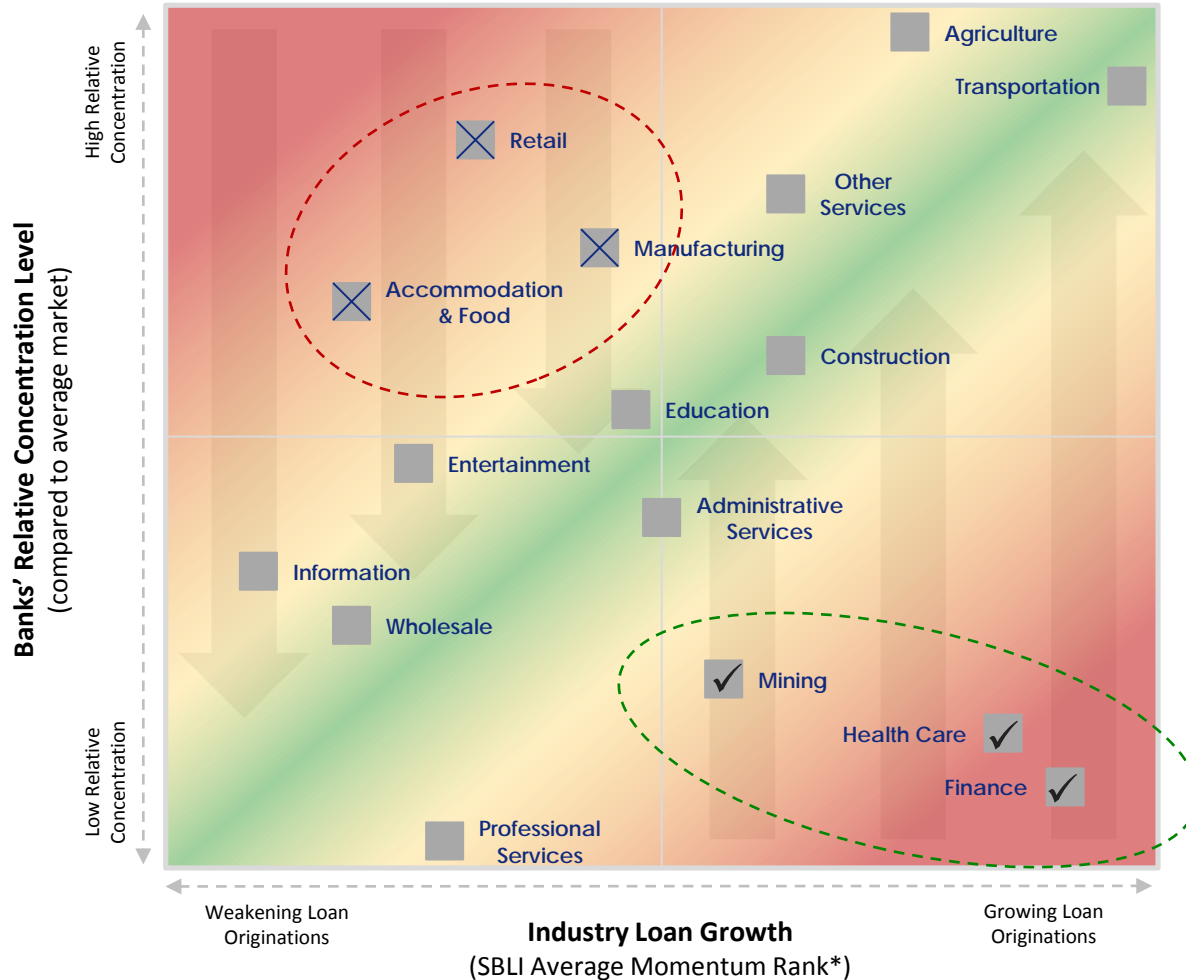
Opportunity Over-Concentration



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

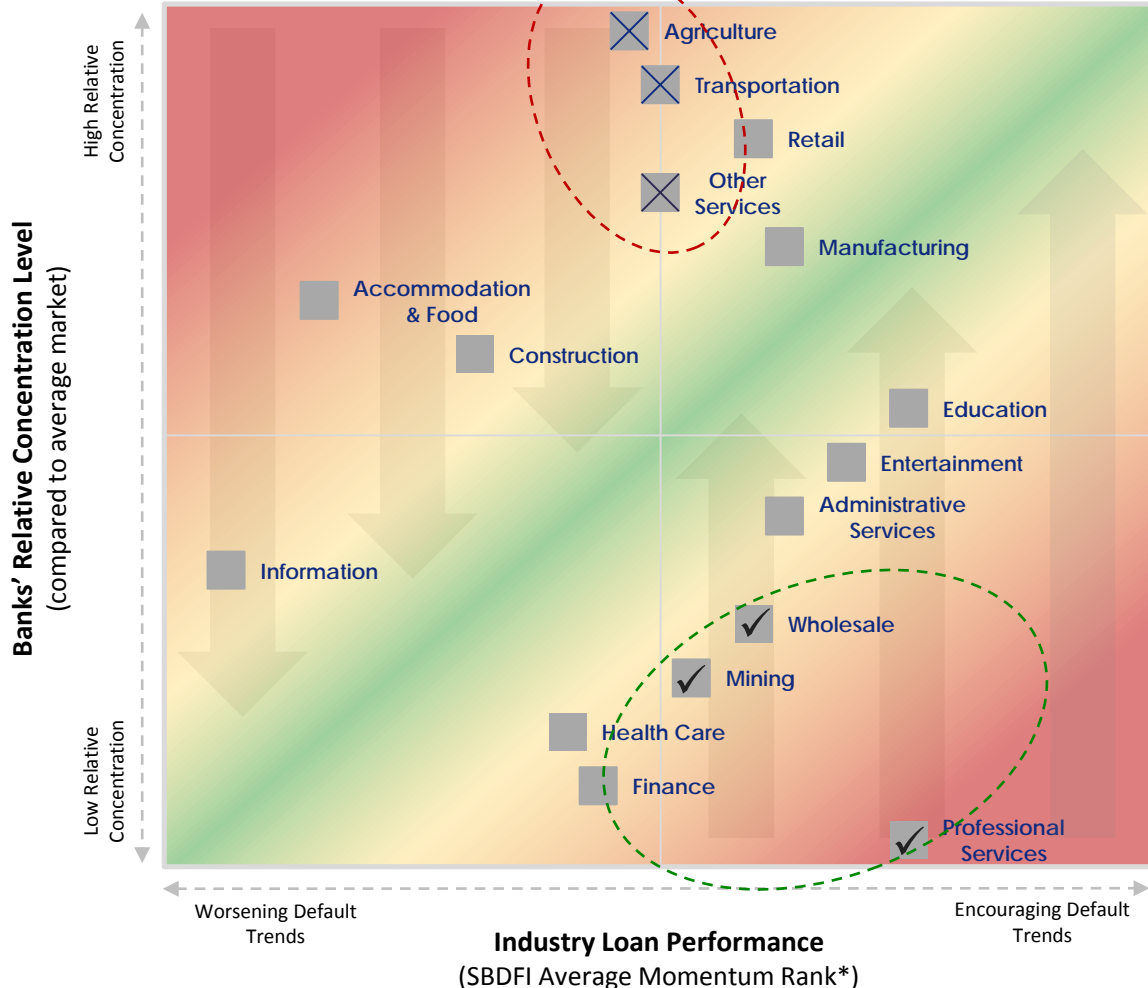
Industry	Industry Loan Growth	Bank Share	Market Share
Accom. & Food	-5.0	5.33%	5.29%
Retail	-3.0	9.28%	6.92%
Manufacturing	-1.0	10.10%	9.85%

*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 credit profiles.

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%

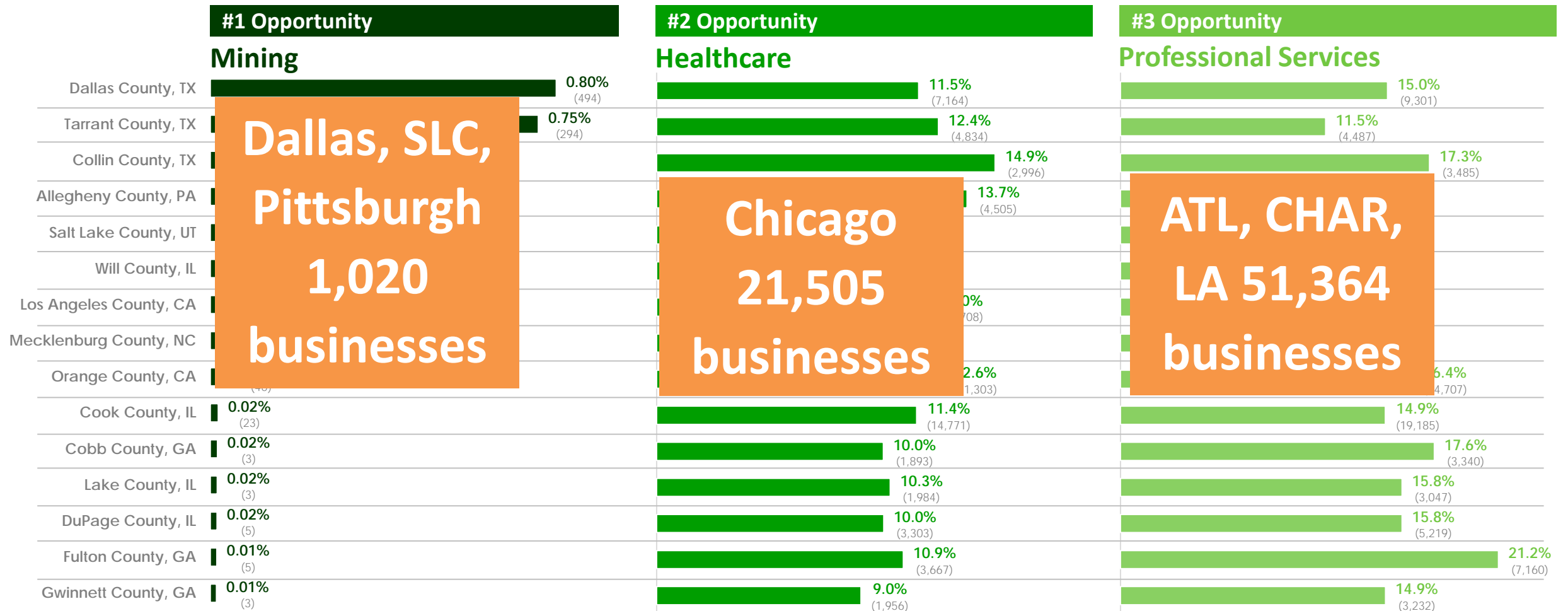
*Note: SBDFI Average Momentum Rank = Average of Change in Default Rate Over Last Three Months rank and Current SBDFI Level rank in the local market (Centered)

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.

A tale of two credits



Recent College Grad
Graphic Designer
Approved in 4 hours

----- Forwarded message -----
From: <[Carolina Macias@carmax.com](mailto:Carolina_Macias@carmax.com)>
Date: Tue, Oct 4, 2016 at 12:22 PM
Subject: Finance Approval
To: ecp@hotmail.com

Dear Emily,

Congratulations! You been approved for a 2015 Chevy Equinox through CarMax Auto Finance. I recommend you take advantage of this great offer. I will call you to discuss the terms of your approval. I look forward to working with you. Thank you for shopping with CarMax!!

Carolina Macias
Sales Consultant
[773-945-8366](tel:773-945-8366)
[708-237-3685 ext. 2501](tel:708-237-3685)
Carolina_Macias@carmax.com

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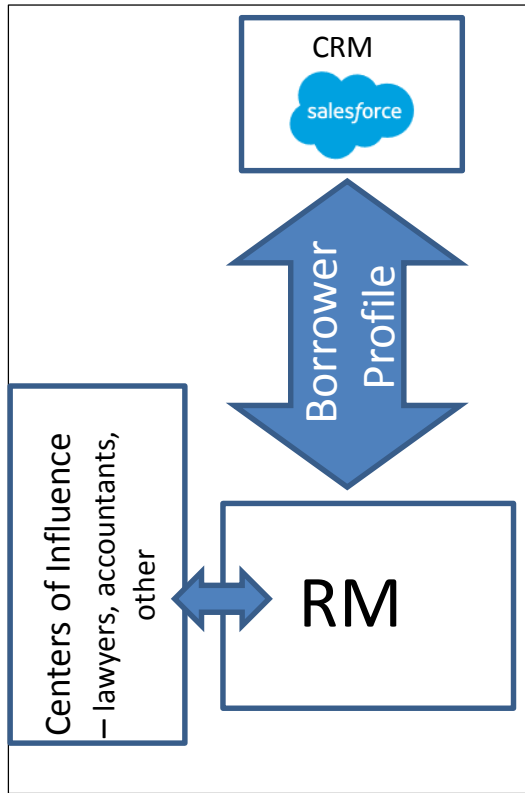
- Fast Growing Company
- Data & Analytics Business
- 45 - 60 Days

Current Commercial Lending - Too Long and Costly

120-180 days
>\$10,000 per lead

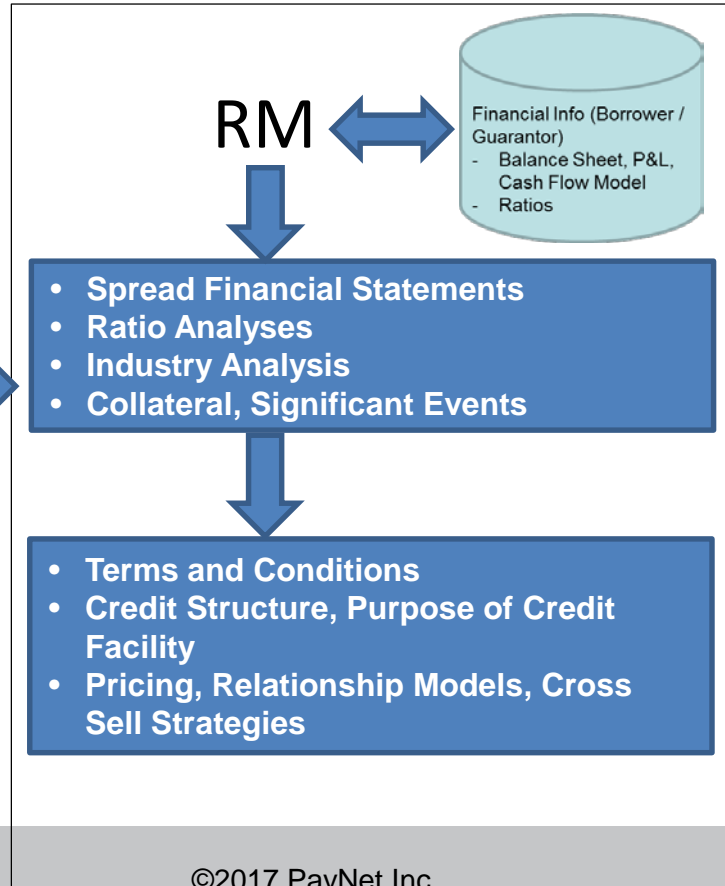
30 - 45 days
>\$5,000 per application

Business Development

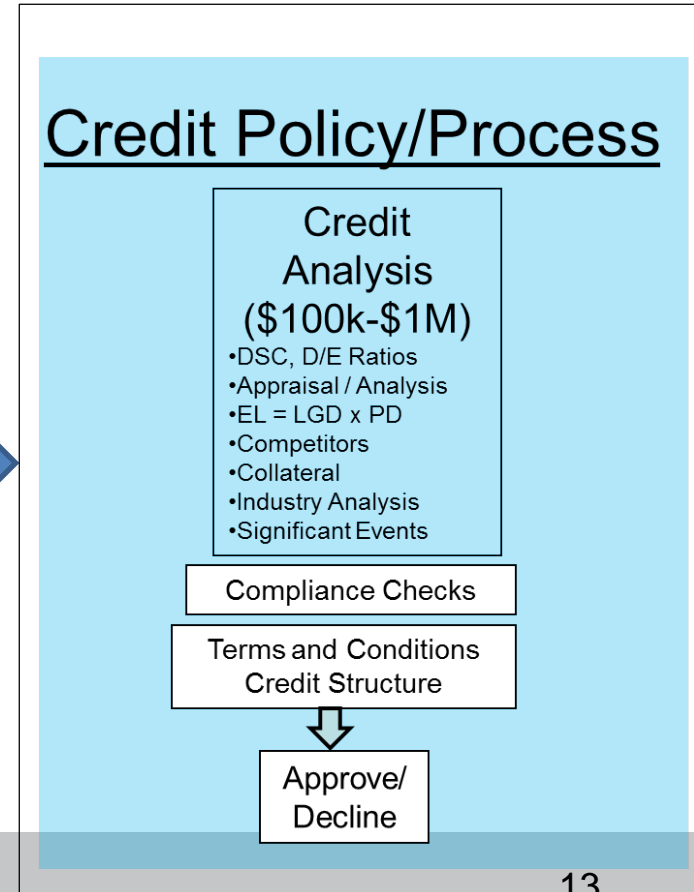


Evaluation

Meet with the Business Owner
Exploratory, Qualify, Collect Financial Data



Underwriting/Decision



New Underwriting Process – Application Only (\$0-\$100k)

Business Development

Evaluation

Underwriting/Decision

Portal

Borrower/Guarantor:

- Name, Address
- Years In Business
- Legal Structure
- TIN
- Request
- Annual Revenue Estimates
- Business Description
- Management Team
- E-Signatures

Decision Engine
PASS
Credit Model

Automated Program Links
Commercial and Consumer Scores, Public Filings, Internal

Risk Rating

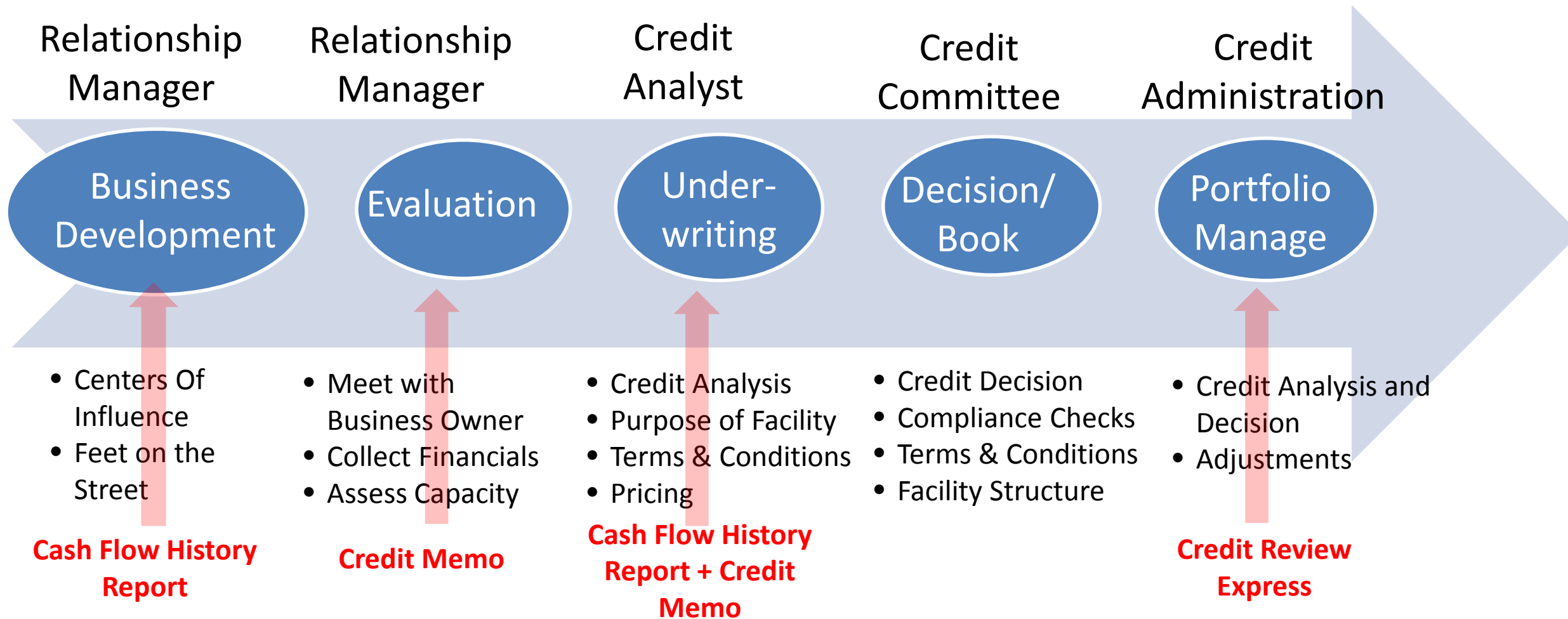
Credit Policy

- ≤ \$100K Exposure
- Established Business
- Low Risk Industry

Approval Letter

Decline Notification

New Underwriting Process – (\$100k - \$2M)




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			
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



“You can’t buy a championship, you have to build it” – Tom Ricketts, Owner Chicago Cubs



THANK YOU
SBInsights.paynetonline.com

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