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# Countering the opportunity loss of trillions of cash lying unused with banks

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It has been a year since the Federal Government imposed the Supervisory Capital Assessment Program (SCAP), also known as the bank stress test. "By setting reasonably ambitious capital targets, we hoped to hasten the return to a better lending environment," said Ben S. Bernanke, Chairman of the United States Federal Reserve, speaking at an event in Chicago in early May, this year (2010). However, Mr. Bernanke admitted that the objective had still not been met. "Bank lending continues to contract, and terms and conditions remain tight," added Bernanke.

This document is an attempt to understand the depth of the problem and the measures that can be taken to curtail the opportunity loss.

## Cause And Effect

Bloomberg's recent analysis shows that U.S. banks have USD 1.29 trillion sitting in idle cash, equal to a record 98 percents for every dollar of existing business loans. The ratio of cash-to-corporate loans has more than quadrupled from 21 percents in June 2008. This implies for every dollar of business loan given out, slightly less than a dollar remains parked in the bank's cash book.

The gradual build-up of cash and decelerated rate of lending has been the outcome of an unstable economic environment; an overtly zealous posture by banking regulators toward banking operations and bank executives; and the overall dislocation in credit markets. Banks have taken a well-deserved cautious approach toward maintaining adequate capital and reserves for absorbing losses without running short on liquidity.

Looking at it from the business borrowers' perspective, the recessionary economy has reduced the loan appetite across the board from small business to large corporations. In effect, banks are today sitting on trillions in idle cash, resulting in gradual opportunity loss and impact on revenue.

The loss of revenue to banks on account of holding cash and not making advances can be stemmed in different ways. This would require a re-evaluation of the lending processes, the lending policy and credit risk management function.

## Selectively Opening The Coffers

The need-of-the-hour is to increase the loan book, identify creditworthy customers, and understand their credit needs and negotiate most opportune terms and conditions.

In the present state of the economy, with recovery being gradual, achieving this goal is challenging. Banks will need to locate a sizable number of creditworthy borrowers; assess their creditworthiness; and if approved, ensure a more rigorous monitoring of their portfolio. There are multiple

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initiatives that banks can take to achieve this seemingly impossible task as outlined below. Each set of initiatives, however, has its own set of challenges to grapple with.

a. **Finding the right borrowers:** The identified borrowers might be smaller than the minimum accepted ticket size or might seek a product, which is not the focus forte of the bank (for example, a borrower might require project finance for a real estate project, while the bank's concentration on that segment might have already been maxed out). Banks could, in turn, consider loan proposals from other sectors and other products (for instance, Letter of Credit for an equipment manufacturer). This would involve amending the credit policy to include these customers as target. Searching for credible borrowers who need such products and fit the bank's credit risk norms would be a key challenge.

b. **Fillip to sales and CRM functions:** If a bank's sales and client relationship teams are deployed in locating such eligible borrowers, it would take higher than the normal volume of application / prospecting to yield the requisite change in the loan book, given the extra-cautious posture of banks and the general lack of creditworthy borrowers. All these would translate into higher number of sales / CRM resources / foot soldiers to be deployed by the banks. Given the reduced business volumes and an unprecedented pressure on banks' P&L, investing in prospecting staff for locating these borrowers could be an arduous task.

c. **Reducing the resource crunch:** Typically bank's resources are divided across multiple products, functions and have some element of shared operations. If a bank's loan book is to be bolstered, the existing structures will have to be challenged. For example, the underwriters and credit risk manager's throughput capacity will have to be increased by isolating non-core processes assigned. These non-core processes will be best undertaken by a third-party with exposure to banking and proven competence in managing processing.

d. **Overhaul the service delivery infrastructure:** Banks should re-visit their service delivery infrastructure from the standpoint of increasing the proposal management capability, time-to-market, resources to sell / service and hours of availability. Partnering with a competent provider could give the required impetus.

   1. Banks need to re-assess their relationship management / sales management operating model and determine the activities, which do not require the involvement of their staff / officers. Examples of such activities could be from collating and spreading the financials of a prospect to creating a prospect profile on the core banking system. An analysis of the process flow of the bank, identification of such non-core processes and subsequent disengagement of respective resources will ensure that specialist resources are more judiciously deployed to manage a higher throughput of prospects.
   2. Banks should re-engineer their processes and re-baseline their speed-to-market / time-to-delivery in a bid to overcome the reduced loan volumes. This can be done in partnership with an external provider that is equipped with the tools of process design and has the required domain expertise and sensitivity toward banking operations. An external party can leverage strengths, which are derived from analogical operations and developed over multiple engagements. For example, we at WNS consulted for a bank and deployed techniques of managing air tickets to loan applications (ensuring every loan proposal was accounted for every single minute, this meant quicker disbursing). Few successful deployments of such projects would ensure the cash lying unused is for a minimal period of time and is not constrained by processing hours / turn-around time of loan proposals.
   3. Banks should re-evaluate their collateral risk monitoring and analytics procedures. Conventionally, these functions have been close to core risk management operations, however, the non-core processes can be identified, and passed on to a provider, which will remotely manage them. Thus, the current risk management staff can be channelized toward more strategic / development activities. Activities such as running the models, preparing reports (ad hoc / periodic) can be delegated to a competent external vendor.
   4. Ideally, generation and dissemination of such reports should be available on-demand and across time zones. This can be easily achieved by deploying a work-sharing mechanism with a process-centric partner. Part de-centralization of report production process will enhance the rigor of monitoring.

The disturbance in equilibrium caused by the downturn will soon settle. Businesses will soon return to where it all began... but banks must learn from the lessons that the downturn taught to re-assess and re-establish themselves.

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