CREDIT & COLLECTIONS

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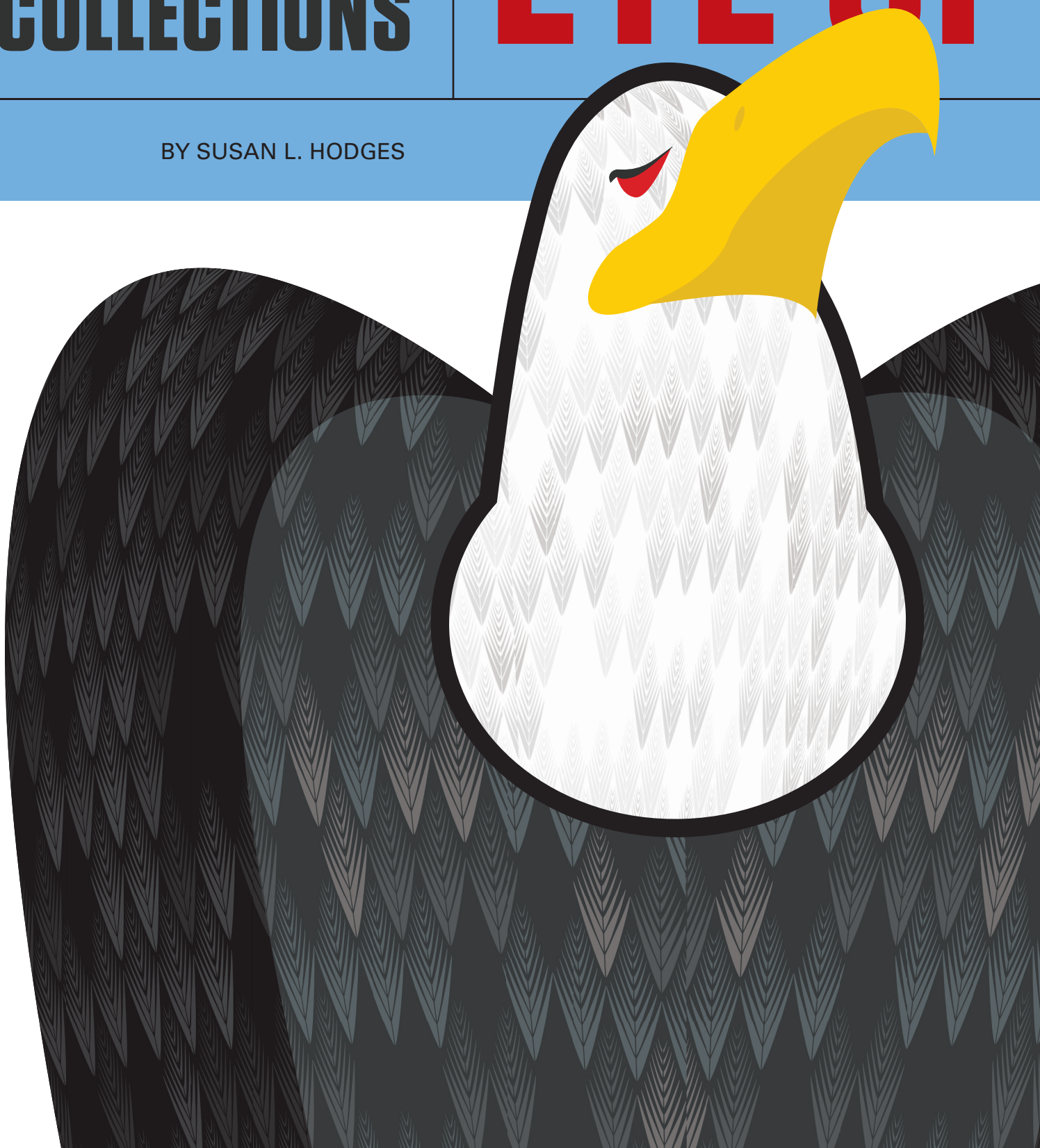

the EAGLE

The attributes of accomplished credit and collections pros might surprise you.

WHAT IF HUMANS HAD EAGLE VISION?

We could spot moving objects more than a mile away. We could focus straight ahead and to the side at the same time. It turns out that astounding visual acuity is not solely the domain of eagles. It's also the stuff of great credit-and-collections executives who use it to read economic currents and groom their equipment portfolios accordingly. Dan Goderis, Director of Portfolio Management for GreatAmerica Financial Services in Cedar Rapids, explains:

"You look at delinquency and see that it's still running at acceptable levels. But it has increased from the historic lows of the last several years. As a result, credit leaders and collections leaders must monitor these trends and the geographic regions where they occur, looking beyond struggling industries and deeper into the feeder businesses around them. In the Dakotas, Oklahoma and Texas, for example, people working in oil and gas spend their money at auto-repair shops, attorneys' offices, restaurants and other businesses where equipment is leased."

"The landscape is changing. More complex agreements, growth in bundled services… and changes in the political landscape that could mean more deals and opportunities for more market share."

—Dan Goderis, GreatAmerica Financial Services

Movement on Both Ends

Energy, construction and transportation are three segments credit and collections pros say are wavering slightly in early 2017, producing small upticks in delinquencies and losses. "We're not talking about much," says Steve Gregg, Senior Leader, Data & Analytic Solutions for Dun & Bradstreet in Short Hills, New Jersey—"maybe 25 to 50 basis points to a 2- to 3-cycle delinquency."

Gregg expects the trend to continue for the rest of 2017, with delinquencies and losses rising gradually. But he also thinks application volumes and booked-account volumes will remain strong, perhaps with margins high enough to carry delinquency.

Data from the Thomson Reuters/PayNet Small Credit Report shows that the jury is still out. The February report, containing highlights of last December, showed the share of loans more than 30 days past due up to 1.69%, the highest in four years. But small business lending was also up slightly, with the Small Business Lending Index at 129.7, compared to 129.1 in November.

"It's an improved mood, but the questions are still out there on the policies and how they are going to play out," says Bill Phelan, Chief Executive and Founder of PayNet, referring to policies under President Donald Trump. PayNet forecast a status quo for the first several months of 2017 and for defaults to remain in the range of 1.9% for the rest of the year.

Goderis says GreatAmerica Financial Services has bumped up its headcount to deal with rising delinquencies. "We've seen a slight increase across the board here, and some might say it's a move toward normalization," he says. "But we'll monitor changes in payment behaviors and make the necessary adjustments." Although Goderis expects the situation to remain much the same for the rest of 2017, "due to the company's sound credit discipline and talented and tenured portfolio managers," he leaves room for the unexpected. "It's basically up in the air how business will be affected by the new administration in Washington, D.C.," he says.

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—Bill Phelan, PayNet

No End to Competition

Indeed, credit and collections executives believe the stage could be set for even more aggressive competition. "We need to grow revenue, and that's a huge challenge for all of us in the financial services industries," says Kevin Prykull, Senior Vice President and Underwriting Executive of PNC Equipment Finance, LLC, in Pittsburgh. "We need to balance growth opportunities, new products and ideas, and find new ways of doing things for clients within our risk appetite framework. We must also continue to deliver exceptional customer service and maintain all of the credit-quality metrics that banks are required to maintain. So while we focus on risk within the credit function, we can't ignore the revenue side—we wouldn't be here without it."

Also mindful of both risk and revenue, Scott McCann, Senior Vice President and Lending Manager at Wells Fargo Equipment Finance in Minneapolis, is keeping an eye peeled for legislative changes that could affect the construction and medical-equipment markets. "If an infrastructure bill is passed or if the Affordable Care Act is revised or repealed, we could see changes in demand for equipment within those sectors," says McCann. "We have a healthcare vertical that will be impacted by changes, so we'll be very attuned to potential changes to the ACA."

"Everyone will look for tools to increase automation and decrease expenses this year because interest rates are going to creep up."

—Steve Gregg, Dun & Bradstreet

The company also has a sizeable oil and gas portfolio, which McCann said is being managed through the continuing stress in that space. "We always try to maintain a disciplined approach, regardless of where we are in the cycle," he says. "We don't get aggressive in good times or pull on the reins in bad times."

But as a larger institution, Wells Fargo is seeing spread compression due to increased liquidity. "We're seeing some competitors—and in some cases, ourselves—stretching on structure to land a deal," McCann says. "It's a highly competitive environment, as it has been for several years."

So competitive is it that TBF Financial, a Deerfield, Illinois-based purchaser of nonperforming equipment leases and bank loans, has expanded into other markets. "Competition is so high between established leasing companies and new ones that companies are not requiring guarantees because they'll lose the deal," says Brett Boehm, Principal and Director of Business Development. "And usually, by the time equipment leasing gets charged off by a finance company, the original lessee is out of business, so the only course of action would be to go to the guarantor. Now, there is nothing and no one to go to [for debt repayment]."

Boehm sees tremendous competition on the credit side as well. "Companies are making loans as fast as they can because there's pressure to book the business, especially for publicly traded finance companies," he says.

Dun & Bradstreet's Gregg sees the same trend. "I'm not seeing much evidence that lenders are raising their thresholds, because raising their requirements would lower their

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—Kevin Prykull,
PNC Equipment Finance, LLC,

approval rates," he says. "And if we're raising the bar and others aren't, will we lose market share? That's the question companies are asking, because market share is critical, and if you take too much time to make a qualified decision, someone else could swoop in and say yes."

Snagging New Customers

If market share is the ultimate prize, it's no wonder that equipment finance firms are spending big money on technology they hope will increase it. "Last year our bank went to a new credit adjudication system that in the long run can provide us with detailed data we need to better run our business," says Prykull. "We're also in the throes of implementing a new leasing system that can take us to the next generation. Technology is key," he adds, "and we know it's going to be all about technology and its application in the future. You've got to spend the money on technology today for the future."

Boehm thinks this year's technology spend will be focused on making it easier for customers to apply for and obtain credit. "Millennials are already getting older; they just want to click a few buttons to get things done, so it will be interesting to see how companies work to satisfy customers and eliminate processes," he says. He's unsure whether equipment financing will attain the transaction speed already achieved by alternative lenders, in which a customer applies online, receives instant approval, borrows money and begins paying it back the next day through automated withdrawals from his checking account. "But companies are definitely putting money toward that kind of technology," he says.

Gregg sees technology focused on efficiency and profits. "Everyone will look for tools to increase automation and decrease expenses this year, because interest rates are going to creep up," he says. Although larger players have been tied to score-based solutions and automation for years, "They'll always try to build the next best one with more attributes that will help them squeeze out that last half percent," he says. "Now smaller companies are turning to tools like that."

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—Scott McCann,
Wells Fargo Equipment Finance

Small and mid-size finance companies are also joining "give-to-get" repositories that provide access to anonymized data on how businesses pay their financial-services debt. "The big guys have been members of these repositories for a long time, because through them they can find out whether

or not their applicants are going to repay them," says Gregg. "Now smaller companies are joining and taking advantage of the data to help them remain competitive and help them further automate their credit-decisioning."

At D&B, a growing tech focus is on macro-analytic and other proprietary data sources. "Anyone in the data-and-insight-provider space has to look for ways to create demand for their services by using new data sources that will help you make a more informed decision," Gregg says. "We're in the data-and-analytic space, so that's where we are looking to come out with new capabilities."

Waxing Rates, Waning Regulation?

If interest rates do inch up this year as expected, alarms won't sound at the companies whose credit and collections executives spoke for this story. "Increases will probably have some impact on higher leveraged companies, but they're not likely to have much impact on our portfolios," says McCann. Wells Fargo Equipment Finance customers are mostly middle-market companies that are not highly leveraged. "We do have a fair number of accounts that are owned by private equity groups," McCann says, "but we pick our spots to make sure we're working with companies that have staying power, and whose sponsors are financially sound and responsible from a lender's perspective."

Prykull puts expected interest-rate increases into perspective: "When I was beginning my career in the late '70s and early '80s, I had an adjustable mortgage that started at 12% and went up to something like 16%, so I'm not as concerned today. Companies know there will be an added cost if they have a lot of variable-interest debt, but I don't see interest-rate increase and its impact on debt service as a material factor—yet!"

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—Brett Boehm, TBF Financial

Goderis thinks it's too early to tell how rising rates will affect portfolio quality. He's more concerned about hiring and retaining portfolio managers and leasing managers in general. "People aren't knocking down the door to come into our industry," he observes. "And the landscape is changing. More complex agreements, growth in bundled services, including managed print, and changes in the political landscape that could mean more deals and opportunities for more market share. You look at areas where you might be able to expand your footprint, and you know you must attract talented individuals to join your organization. How we attract and retain them is key to our mutual success."

McCann notes the same issue, saying his company is very focused on staff management, particularly early talent development. "I read a piece lamenting the possibility of easing bank regulation because it would result in lower employment within banks' compliance groups," he says. "But compliance has been a rapidly growing area the last few years, and slowing that rate of growth would lower costs and give us an opportunity to add different types of jobs. If we're not hiring compliance people, we can hire more sales people and others who support new loan origination."

Thinking along similar lines, Boehm says credit and collections pros could become even more sought-after if the regulatory environment relaxes, particularly as it concerns Dodd-Frank. "That would appear to mean a possible increase in the flow of business, allowing finance companies to push more deals through," he says. For the short-term, he believes such a development would be good for the economy, and thus for equipment finance companies. He says, "Those that aren't selling debt could start selling again, and with more business being loaded on the front end, there should be more collections on the back end." Maybe 2017 will put feathers in everyone's cap. ■

Susan Hodges writes about equipment finance and other business topics from her office in Wilmette, Ill.

Don't miss the 2017 Credit & Collections Management Conference, June 4–6 at the Hyatt Regency Baltimore on the Inner Harbor. For details visit *www.elfaonline.org/events/calendar*.