WHITE PAPER

Straight Through Processing

Commercial Banking Lending Perspective

– Ashok Mohmud Alexandar

Infosys®

Ensure symmetry in process, people, and technology

Adopt Straight-through Processing (STP) for commercial lending

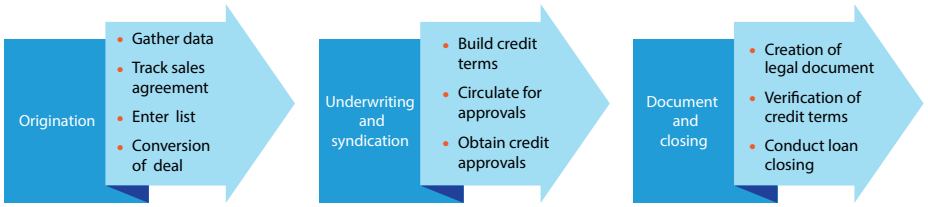
Commercial lending is a complex business activity. Regulations, the global expansion of businesses, the correlation of participants in the lending life cycle, and the disparate operational environment of products and services delivery aggravate the complexity.

Our expert makes a case for STP to manage the lending life cycle and mitigate risks in the loan life cycle. Lending organizations should adopt technology that delivers business results in terms of higher productivity, enhanced risk management, and a superior customer experience.

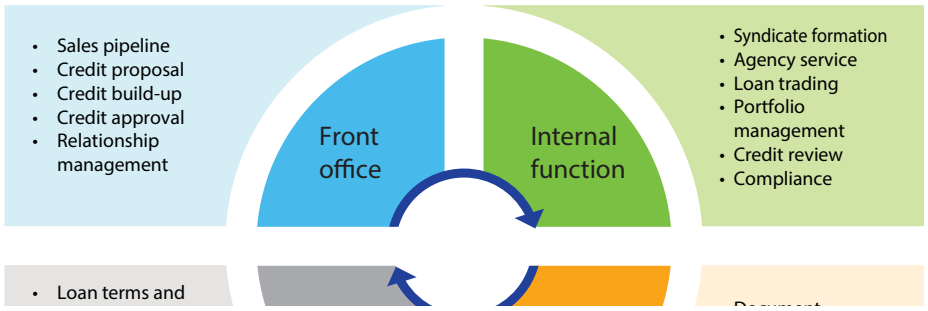
Technology and operations outlook

After decades of functional specialization, commercial lending organizations are constrained by unproductive technology platforms even as they face business challenges of operational expenditure and revenue growth. When mainframe systems executed back-office loan computing and transaction processing, 'lending exercises' were separated from sales and relationship functions.

As operations became more isolated from a jurisdiction standpoint and vendor systems began to proliferate in the 1990s, the conventional business logic of banks was to use best-of-breed applications. During the golden age of commercial lending, semi-sovereign lending divisions (real estate, mid-sized and large organizations, asset-backed, syndicated, etc.) developed or procured systems for their corresponding portfolios, without paying heed to consolidating technology or portfolio data. Invariably, a lending business invested in technology without focusing on its unique specifications and services.

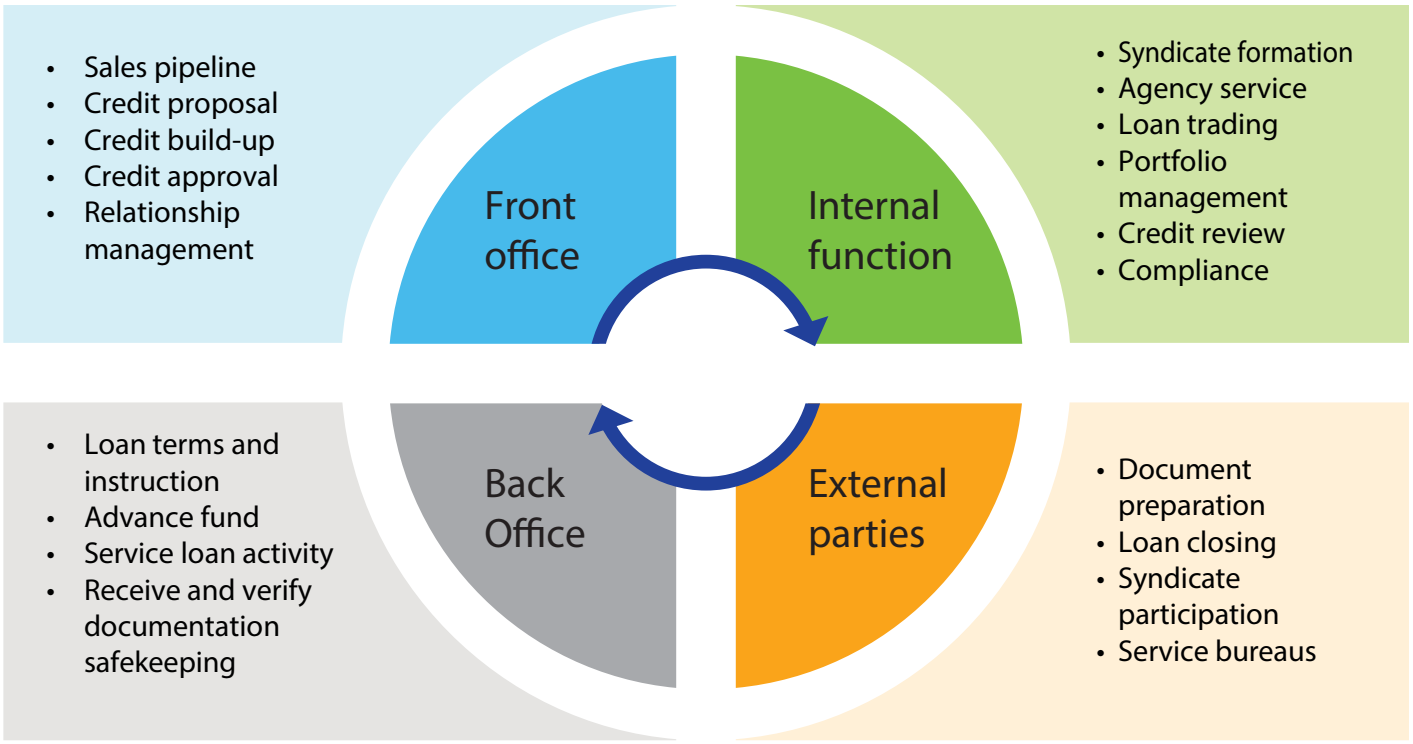


Front office Origination



Back office servicing

The impetus for lenders was to install one-off divisional systems for diverse commercial loan products. However, contrasting systems were silos: technically conflicting, functionally incompatible, and operationally superfluous. A majority of banks detached the loan operations functions from the front office and used technology to automate the manual servicing functions. Consequently, a new business model took shape based on a disintegrated, manual transfer of loan information and instructions from the front office to the back office. For practical reasons, mechanization of the commercial lending cycle commenced at the point of origination into the loan operations servicing system. Opinion on data integrity is divided between the origination and servicing functions in the lifetime of a commercial loan and veers towards incremental development of an unnecessary 'middle-office'. It is designed to complement the workflow, ensure data integrity, and facilitate customer relationship cohesion between the front and back offices.



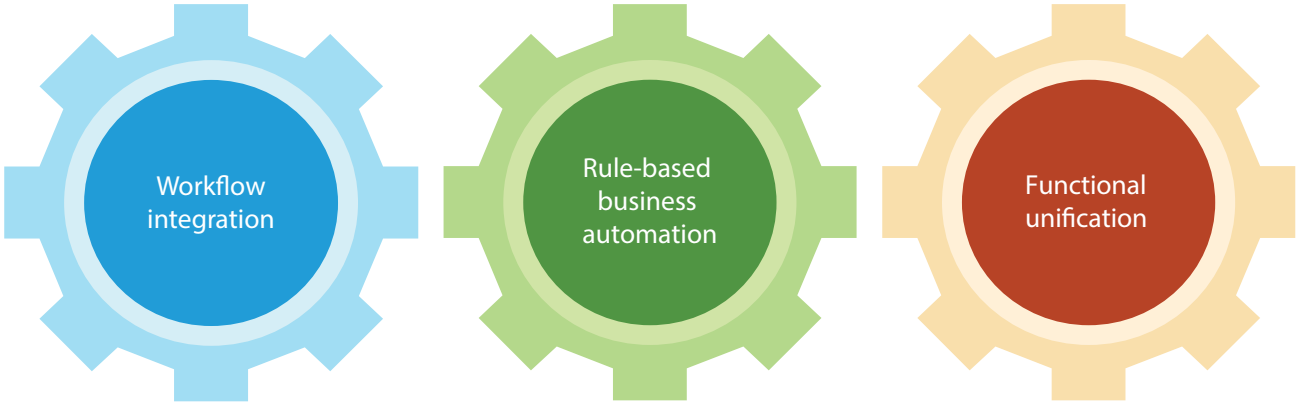
Middle Office

The manual framework was not ably supported since technology could not serve the entire lending life cycle. In addition, limited front-end interfaces appeared (initially, as deal management tools, and later as credit databases) and the advent of the Internet made it possible to provide access to loan information for all parties, including borrowing customers. Despite enhancements, the internal organizational arrangement at several banks adopted the 'dumbbell shaped' business model, where origination and servicing are connected by a weak link. Diverse software interfaces were connected to network systems and databases in a provisional manner as banks recognized the potential of integrating processes and information. However, such solutions are makeshift at best. As the application landscape becomes increasingly complex, the rationale of adoption becomes tenuous and expensive.

Commercial Lending and STP

Lending organizations are now prepared to reassess their business operations and are figuring out means to make it more productive and efficient. Financial institutions realize that they must look beyond Microsoft Excel spreadsheets and invest in unified and automated systems while fixing obsolete technology.

Straight-through Processing swaps automated tasks and processes for manual ones. STP ensures that a business process or service (e.g., the inception, servicing, and arrangement of a commercial loan) can be automated from beginning to end. In STP, relevant information (about new customers and loan specifications) is registered only once. Any operation calling for such information fetches it from a central database. All sub-processes, tasks, assignments, exchanges, computation, reporting, communiques, sub-tasks, and other events are performed without a monotonous entry or manual conversion. The functions do not occur concurrently, but happen seamlessly. Actually, they cannot occur simultaneously, since complex business operations take days, weeks, or months. A term that best describes STP is 'unified processing'. While the approach of 'straight-through' automation from front to back processes is well rooted, 'straight-through processing' does not evoke the potential of process automation. Multiple points of view on STP encapsulate the original front-to-back process and how it can be achieved singly or through consolidation over time. In addition to front-to-back automation, STP should be explored in the context of functional unification, workflow amalgamation, and non-transitional and rules-based business automation. Any type of system amalgamation or unification that reduces or eliminates manual processing is a logical corollary to STP.



Catalyst of STP

A comprehensive approach can become extremely complex, which explains why the full potential of STP in lending applications is yet to be realized. Currently, applications are confined to sub-pattern, usually within a single business line and involving human intervention at one or more points to advance the process. Inconsistencies persist at points where small sub-systems can be invoked to ensure cohesion and unlimited automation. The ultimate objective is automated processing across functional areas and business lines, and eventually across the enterprise perimeter. However, interfaces are in the realm of middleware (point-to-point and hard-coded) and restricted within the perimeter of a company. Such a situation arises since technology cannot link key points of integration. The challenges include specifications, intricacies, distinctions, divergences, and inconsistencies in commercial lending. The task becomes more demanding in the light of changes in the industry landscape such as syndication and trading, regulatory compliance, consumerization of technology, and sophisticated Customer Relationship Management (CRM) applications that are highly analytical compared to the erstwhile contact list management. In many respects, STP shares the same perception as CRM in banking. A nuanced concept that characterizes a strategic approach to administer operational processes has often been termed as 'simplistic'.

Commercial lending from an STP context

STP links the entire process of commercial lending in a unified Web-based network of information about loan assets. It is available to lenders, credit officers, relationship managers, internal systems, associated staff, external rating agencies, legal counsel, syndicate members, investors, regulators, as well as customers.

The basic processing operation contains details about commercial loan variation, information applicable to a particular customer and loan facility, which is stored in a consolidated central database. All workflow arrangements, transmission protocols, guidelines, confirmation tables, approval pyramids, and sequence management are guided by predefined business logic rules that can be reorganized actively.

The commercial loan is not established and evaluated as an arrangement between lender and borrower. It is a commoditized asset in the bank's portfolio of assets, with a market value and subject to custody, sale, securitization, or hedging, whatever best suits the asset management strategy. For this reason, STP delivers a critical adequacy. By exploring the factors of data about the loan (providing more detailed customer, credit, pricing, collateral, and covenant and valuation data), it administers a real-time valuation. The parties and systems that are integral to the process need to be allied to the conventional commercial loan value chain.

The STP value proposition for commercial lending

- Functional efficiency: Banks can standardize credit and operational guidelines by automating and regulating a significant portion of the loan origination process. It ensures consistency in credit decisions and promptly detects deviation from guidelines for better governance.
- Risk management: In the wake of the Dodd-Frank Act, Basel III, Foreign Account Tax Compliance Act (FATCA), and other regulations, banks have to aggregate, analyze, estimate, and share data about customer transactions. STP facilitates data coherence and integrity due to a single entry and depository in a shared database. In several scenarios, it can also 'author' and collect data due to automated processes, which ensures a nuanced and 'source-given' feed of information for regulatory compliance, risk management, and customer service.
- Lifetime customer value: A common grievance among commercial lending customers is the sub-standard quality of service offered by banks. Corporate banking customers are demanding, especially when competition among banks makes lending a buyer's market. In such a situation, any business process improvement that expedites the fulfillment of business deals or diminishes the frequency of operating errors vastly enhances customer satisfaction and loyalty. STP realizes these objectives. The elimination of human intervention and unnecessary inputs in sourcing or servicing functions accelerates operations. STP features such as an automated e-mail or phone alert notification with details of lending limits improve customer satisfaction. One instance of successful STP is the facility of providing access and servicing capability in corporate banking customer loan accounts. Some banks provide customers with the ability to send Web-based requests for funding from their loans, but they require the bank manager to complete the transaction.
- New business opportunity: Banks can administer a huge volume of transactions and loan facilities with existing resources supported by the enhanced output and efficiency of STP. New products can be developed based on detailed data, refined analytical capabilities, or more responsive and real-time reporting. It will result in additional business since lenders will less likely forfeit fees for customers when they know the system captures and reports the event. The superior level of customer service can indirectly result in additional revenue due to targeted cross-selling and a higher retention rate.

Functional efficiency

- Elimination of redundant systems
- Reduction of manual labor
- Streamlined process
- Lower costs

Risk management

- Workflow
- Data integrity
- Exception management
- Accountabiliy

Lifetime customer value

- Responsiveness
- Accuracy
- Timeliness
- Customer retention

New business opportunity

- New product development
- Customer retention
- Increased productivity
- Segmentation

STP Value Proposition

Best practices for integrated STP

Several commercial lenders recognize the potential of technology to achieve strategic business objectives. However, a commercial lending organization cannot improve profitability solely by leveraging technology. An Intelligent solution would include implementation of STP with technology consolidation. It can be achieved by use of adaptable suits to realize the profit of a unified system.

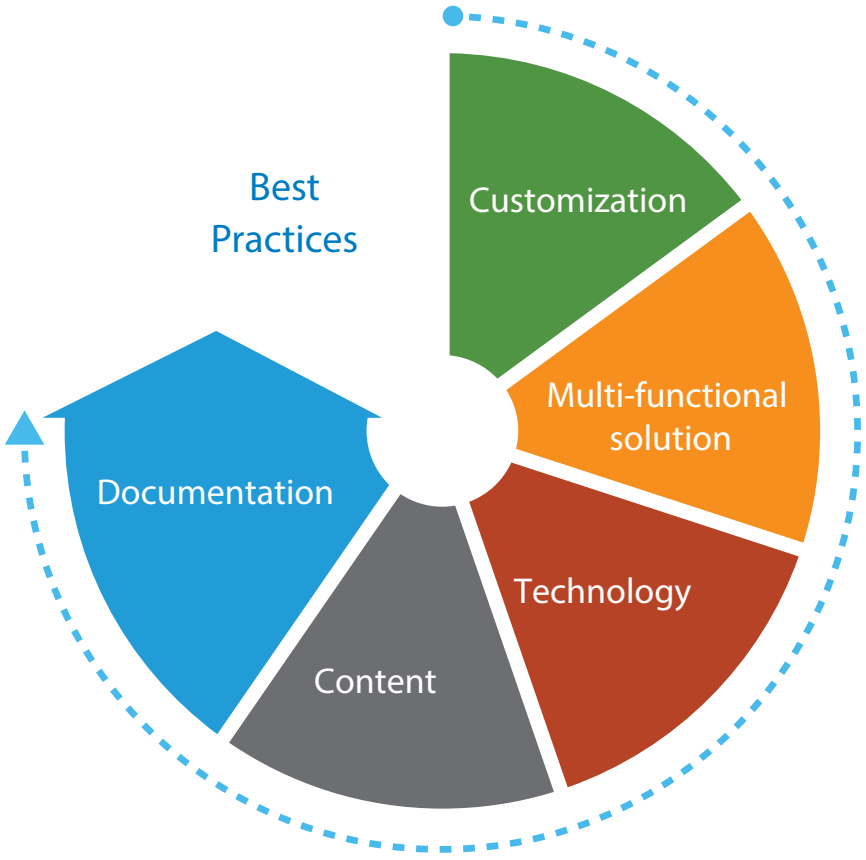
Multi-functional solution: As part of STP unification, Commercial Banks must determine one unique system that provides the latest compliance measures and technology. A consolidated approach that combines technology with required content which helps to run the business efficiently, would weaken risk and be more responsive to customer and market requirements.

Technology: The STP solution should blend with the lender's current systems, enhance workflow by coupling divergent systems, and eliminate ineffective business processes by transferring information across systems.

Content: Content management system should be unique across business horizontals with a flexibility to adjust business divergence. Lenders operating with legacy platform and technology must be well accustomed to all the regulatory requirements of the state and the country in which they operate.

Documentation: The business imperative is a solution that determines and produces all documents required for every loan irrespective of the degree of complexity. Managing documents designed for execution in commercial lending is inadequate when law firms produce high quality professional commercial documents and regulators are focusing on credit and document quality.

Customization and updates: A content management system should assimilate content creation tools that prompt lenders to modify content as lending opportunities arise. In addition, the solution should have the ability to update documents that reflect changes in regulation and business practices.



Best Practices

Coupling strategy with best practices

An STP-based lending platform must be able to audit document flow between departments and track resource activities. Banks should define requirements, inputs, and stakeholders. Systems with capability to handle various key processes and sub-processes in lending application like recognition of customer, transaction details, and delivery of products with capability of multi-regional coverage should execute supervise, recognize, and manage possible costly delays in processing.

Review of information gathering and sharing: Banks can ensure that information flows seamlessly by routinely examining their STP processes. For example, Process reviews may assist in acknowledging that different regions do not have different built-in information gathering standards in front, middle, or back office operations. STP review end result should be the establishment of uniform business rules across offices even though some offices are less engaged in commercial loan processing activities. This process must collect and retain data in spreadsheets, monitoring software, etc., as a part of daily activities. It should predict gap in information, lack of which may cause delays in delivery of service or product, and generate unpredictable risk to lenders.

Troubleshooting: A single front office error related to loan processing such as incorrectly captured customer or financial data or security details can cause cascading problems that affect multiple departments. Poor information gathering and sharing between STP connections can create delay in key document delivery and execution. The initial error buried within a multi-layered delivery web can be expensive without the right tools. For example, capturing wrong asset and guarantor details by front office may create customer dissatisfaction. When data gets captured accurately at every step of the process, it ensures that resulting output is relevant for business purposes. Significantly, it helps increase client satisfaction and ensures repeat business.

Use of appropriate metrics and guidelines with accurate milestones in processes mitigates inaccuracies, business errors, neglect, and payment issues. It protects banks from contagious processing mistakes. Banks should consider developing solutions to administer metrics such as advanced data analytics, key matrices, and dashboards to show and provide information from all key areas along with industry benchmark and key reviews for benchmarked credit processes.

Deployment and availability of resources: Acceptance by all levels in an organization is key to a successful STP process in commercial lending. Acknowledgement and backing of senior management with addition to regular testing and enforcement checks and balances are very essential in the success of STP. To accurately address security and technology roadblocks, committed project management teams are required with skilled IT teams. Project governance, data integrity, data allocation, and corrections require inputs from other support like risk, legal, HR functions that are beyond the scope of the bank's finance and IT departments. Process representatives from these functions may need to review project results and provide inputs to ensure consistency.

Coupling Strategy with Best Practices

A commercial lending organization should ensure that its process has the prerequisites to manage an STP system. Firstly, the scope of an STP process should incorporate all tools for a successful implementation. It should encompass all departments that involve a loan transaction, not just the credit management team. Secondly, the STP environment should include essential controls that aid in establishing where challenges originate. In addition, it should support implementation of processes required to address challenges at the source promptly. Finally, all levels of the organization should support and enforce the STP process.

Process automation tool: A catalyst for STP implementation

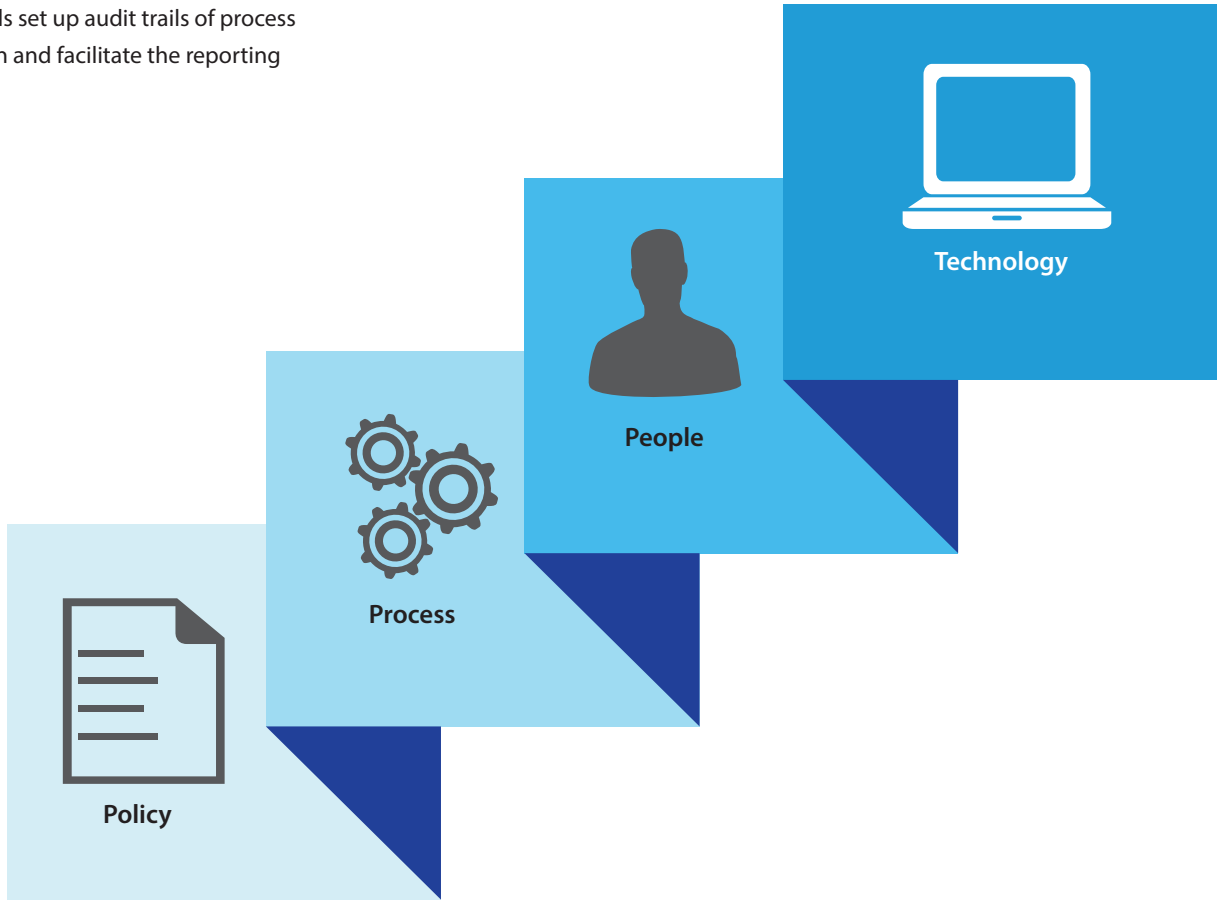
Process automation tools enable organizations to create new processes or micro-applications that run on top of current applications. Typically, the menu of such products includes:

- IBM WebSphere Business Modeler and IBM BPM 8.x suite
- Oracle BPM suite
- Pegasystems SmartBPM suite
- SAP Process Integrator (PI)
- Software AG Business Process Management suite

These tools make it easier to integrate STP with existing applications. A business process that blends diverse applications can be implemented using the same tool. Such tools set up audit trails of process execution and facilitate the reporting techniques based on the data flowing through processes. The tools enable the formulation of compounded applications consisting of functions and services from existing applications. It ensures that neither the data nor the process is duplicated. The tools are useful for STP for transactions such as loan origination. Rather than re-entering data for the loan application, financials, key ratio, scoring, credit decision, and legal documents, business process tools automate a major portion of the process by exhibiting and reworking functions in the existing systems and bridging the functions in new ways. In addition, process tools implement complex rule definition as well.

STP roadmap: Policy and process before technology

A huge and often costly miscalculation made by organizations is to implement technology as a solution to a business problem. A common misconception is that technology can salvage the business. A holistic approach involves an enterprise-wide, unified path to process management - focus on policy, process, and people before investing in technology.



Benchmark Pathway

Benchmark pathway

Organizations often run the risk of focusing on technology for a business solution. An organization should select a technology only after thorough analysis. The bank's policy should drive the processes for operations, lending, and other activities. It is a complex task for technology to undertake a gray process riddled with inconsistencies. Technology should be implemented based on rational, well mapped out, and regenerative processes to effect a transformation. It is imperative to articulate and crystallize processes as much as possible. Consequently, it may require re-engineering to phase out irrelevant portions of the process. Organizations that seek to effect a business transformation in the proper order – policy, process, and people, followed by technology – complete technology design and implementation faster and in a more cost-effective manner.

STP – The ideal foil for commercial lending

Straight-through processing determines the success of commercial bank lending operations. A firm commitment from the management, and process and planning stakeholders is required to realize the potential of STP. The potential of STP lends structure to the process of the lending value chain.

About the author

Ashok Mohmud Alexandar

Consultant with the Commercial Banking Practice team of Infosys Ltd.

Ashok Mohmud Alexandar is a Consultant with the Commercial Banking Practice team of Infosys Ltd. He has more than five years of experience in commercial banking - lending, credit rating, treasury, and risk management. He was associated with various leading banks in their corporate banking - credit management group. He has deep insight on corporate lending cycle, rating models, and capital requirement. Currently he is working on BASEL-III implementation with a large European bank. He has been providing consulting services and has been managing large and critical IT engagements for numerous clients. He has extensive techno-functional skills and an in-depth understanding of process models. Ashok holds an MBA (Finance) degree from Bharathidasan Institute of Management Tiruchirappalli (BIM-Trichy) and a bachelor's degree in Electrical Engineering from Orissa Engineering College.

He can be contacted at ashok_alexandar@infosys.com and LinkedIn-Ashok Alexandar.

For more information, contact askus@infosys.com

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