Adapting to a Consumer-Driven Marketplace

by Larry Walker

There is an entity stronger than all of us in the financial services industry, with far greater power than most of us imagine. That sleeping giant is the consumer. In the marketplace of tomorrow we will have to adopt a perspective that places the consumer at the center of the universe. The big surprise for many of us is that technology placed him there.

As lines of business continue to blur and more information is placed in the hands of the consumer, institutions that don't use all their resources, including technology, to attract consumer interest, serve consumer needs and build consumer loyalty will be marginalized or eliminated altogether.

Conversely, companies that do empower consumers with information will be rewarded with quicker sales and consumer loyalty. This means we must look at our own organizations from a new perspective and adapt to an industry being transformed by the forces of globalization, deregulation, privatization and technology—all with the effect of making the customer king.

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STEPPING OUTSIDE THE BOX

How do we place consumers at the very heart of what we do, and how do we build customer loyalty to foster life-long customer relationships? The answer is by putting more information and, therefore, more power in the hands of the consumer through the creative use of technology.

Technology is raising the bar in terms of service levels and allowing us to focus more intently on relationships with borrowers. Vast amounts of information are becoming available to consumers through on-line sources, and traditional home lenders will increasingly focus their energy on consumer-direct channels. Technology is also allowing home lenders to simplify and standardize processes to make them more accessible to borrowers.

Consider how the introduction of automated underwriting by secondary market agencies in the U.S. changed the business model for mortgage loan applications. In the past, consumers would file loan applications with the lenders, along with authorizations for the lenders to obtain and verify information about the consumers through their employers, depository banking relationships and even credit reporting agencies. Finally, when all of the information had been verified and aggregated in one place by the lender, the information would be presented, in hard-copy format, to a professional mortgage underwriter. This individual was a trained professional, skilled in reviewing information and assessing loan eligibility based on the credit risk criteria of the lender.

This whole process traditionally took anywhere from weeks to even months to complete. Moreover, it involved an excessive amount of processing work on the part of the lender, including amassing an estimated 80 loan documents in every loan file. However, by placing underwriting at the beginning of the process and noting only the requirements for approval, technology has allowed lenders and applicants to respectively satisfy the exceptions and eliminate the expense of overprocessing loans.

More Applications Will Come

The same principle underlying automated underwriting can be applied to other processes that are not yet automated. Consider a scenario in which customers are profiled at the point of application to determine what level of processing their individual loan applications will require. For instance, a lender might implement a policy whereby borrowers who make downpayments of a certain size will not be subject to a property appraisal. This concept could be applied by individual case or by affinity; all borrowers who are employed in certain professions, for example.

The reason we can skip process steps for certain borrowers in the underwriting of mortgage loans is because technology is allowing us to collect and analyze data on home prices, or on credit experiences of groups of consumers, that establishes regular patterns and statistical relationships. These can substitute for the in-depth analysis of the individual borrower or property. There isn't any doubt that technology will allow us to discover and implement other "short cuts" like these, which speed and streamline the process without compromising the integrity of credit or asset quality.

Another technological success story, the automated teller machine (ATM), provides an analog for the path the home mortgage industry is taking. Once viewed as mere dispensers of cash, ATMs have evolved into consumer convenience centers and distribution channels for information. At some banks' ATMs, consumers can buy mutual funds and stocks or hold a video conference with mortgage loan officers. For several years, NBS Bank of South Africa has allowed its home equity bond customers to access their lines of credit through an automated terminal.

Why couldn't mortgage institutions provide more than just mortgage loans? Why couldn't they be consumer convenience centers as well? Mortgage companies could leverage their capabilities and their relationships with other service providers to package solutions based on a comprehensive array of services which they could then sell to consumers. These packages, for example, could include everything from homeowner's insurance to comprehensive relocation services or even home security. Today's mortgage lenders are discovering that, as ATM technology advances, they are able to utilize the ATM as a loan machine, a cross-selling machine, an installment repository, and much more.

CONVERGENCE

Deregulation, privatization and globalization are opening a market space where diverse industries, technologies and services are converging at the point of sale, and where more nontraditional players are entering the financial services industry. While these forces make room for convergence, technology is the vehicle by which we can achieve this convergence.

Fiber optics is just one example of a technology that encourages convergence by providing virtually unlimited capacity and smashing barriers between communication and industries. Today, optical fiber is used at less than one ten-thousandth of capacity; about 25 trillion bits per second in just one strand. That's enough capacity to handle every call in the U.S. during the country's peak moment of Mother's Day, that country's busiest calling day. Because American companies alone are laying 4,000 miles of fiber optic cable a day, the potential represented by just this one technology is staggering. The greater speed, capacity, and flexibility provided by this and other technologies will make it possible to share vast amounts of information on line. Can the promise of the much-vaunted electronic marketplace be far off?

In a deregulated environment, cooperative information-sharing ventures, such as the U.S. mortgage industry's Mortgage Electronic Registration Systems (MERS), will not only simplify processes, they will also change the thinking behind those processes. The mortgage industry's first large-scale collaborative technology initiative, MERS stands to save the industry as much as $200 million annually by re-engineering today's error-prone, paper-based registration processes with a registry that tracks mortgage ownership and servicing rights electronically. MERS operates as a national clearinghouse for mortgage information which is accessible to industry-related organizations such as land title registries and land title insurance companies, as well as to consumers.

By crossing borders to team with mortgage industry players globally, and teaming with players from other industries altogether, mortgage lenders will extend their own reach into nontraditional areas to offer more value-based services and chart new territory for revenue and growth. The most successful companies will give consumers more choices and build relationships with customers throughout their lifetimes. Success will come from giving customers more control of their products and services throughout the life of the relationship.

MAKING THE SHIFT

In the Information Age there are three principles for successfully giving customers more choices: (1) Presence, (2) Pathways and (3) Promise.

First, you must establish a formal, recognizable information presence with customers so that the information they need to make decisions or purchases is immediately available to them. Second, you must create two-way information pathways by which you and your customers can communicate, interact and gain a better understanding of each other. Finally, you must deliver on the promise of mass customization: harnessing information about your customers to mass produce products and services which still cater to their specific needs or individual circumstances. The effective use of technology is the key to implementing all three principles.

Information Presence

Information has become a valuable global currency. But, unlike other currencies, information is most valuable in the hands of employees who can enhance the experience of the customer, or else in the hands of customers themselves to help them make their own decisions.

Let's look at a couple of examples in real estate finance. Perhaps the most obvious is the opportunity for cross-selling. A housing finance institution may have a relationship with consumers who have purchased homes. It also wants to sell these customers a credit card (among its other financial services products) as well. From a practical standpoint, only a certain percentage of the borrowers will buy the credit card when it is pitched to them. Of course, the institution can make the pitch to every single one of the borrowers to uncover those who will ultimately buy. Or, using its information systems more effectively, it can segment characteristics which are exhibited by buyers of credit cards.

A new technology, neural network modeling, is a form of artificial intelligence which learns from its experiences. In this instance, neural network modeling could be used to identify what all of the current credit card customers have in common, and then course through the mortgage portfolio to find customers who exhibit similar characteristics. These "discovered" customers are those who would be most likely to buy a credit card if the institution targeted them for a solicitation. You can see that, using this one technology, the institution would get to those new credit card accounts faster and cheaper, thus making the entire process more efficient and more profitable.

Similar scenarios are being played out to determine how collection efforts will be implemented on delinquent home loans, and this is an area where the power of information is really just being discovered. By using technology to identify trends and factors which are predictive of defaults, we can use the same identifiers for use in prioritizing collection efforts or even lending efforts. Of course, the information (i.e., trends and predictive factors) was always there; we were just never able to access it or use it in these ways before technology made it possible.

The way we view information can make all the difference in how we revolutionize our business. FedEx (formerly known as Federal Express) became an example of this concept when it developed its Powership™ package-tracking software after it began to see itself not as a deliverer of packages but as a custodian of information. FedEx's software puts information (about the location of a package being shipped) in its customers' hands worldwide, delivering speed, convenience and control, while cutting the company's costs. Technology, of course, is the key to FedEx's success, and the customer's newfound power in this example.

Interactive Pathways

Interactive pathways allow service providers and consumers to connect directly with each other via electronic channels. Let me illustrate with yet another example. DOCUNET, a document delivery company in Washington, D.C., used ATM technology to virtually eliminate its fleet of trucks. At hundreds of ATMs throughout the city, customers use credit or debit cards to purchase documents—traveler's checks, airline and concert tickets, hotel reservations and rental car confirmations—which are dispensed through the ATM machines, in their new role as interactive pathways.

It used to be that the consumers would order airline tickets or concert tickets, and then have to wait for DOCUNET to deliver them. Today, those same consumers can simply stop by the designated machine and pick up whatever they need. This interactive pathway saves customers time and money, and avoids inconvenience. It also saves time and money for the companies DOCUNET works with. It eliminates the cost of maintaining a trucking fleet and supporting branches all over the city.

Promise of Mass Customization

Many companies misunderstand the term "mass customization" and its significance in competing for customers. It does not mean producing as many different kinds of products, such as home loans, as possible to meet the tastes of every consumer. It means doing whatever it takes to understand and interest your customer, and then giving the customer the ability to easily locate and securely purchase your products and services to match their needs. This can be difficult, but the power of technology is putting power into the hands of the consumers, and winning new business for the companies that seek mass customization with technology.

Companies like The Custom Foot, on the east coast of the U.S., are experimenting with kiosks that scan foot measurements of customers in order to create custom-made shoes. At the kiosks, consumers use point-and-click video technology to choose the color, leather grade, style and type of shoe they want. This example illustrates the concept of true mass customization. There is no middle-man and no inventory; a pair of shoes is created only after it has been ordered, eliminating 50% of the cost. Technology is making it possible for The Custom Foot to give customers exactly what they want, when they want it. At the same time, the benefits of mass production in its manufacturing plants are retained, so the shoes can be offered at a price that customers will pay.

These are some examples from which the mortgage industry can learn. Mortgage lenders could establish presence, pathways and promise through on-line channels like the Internet, where consumers could view MLS listings, shop for rates and prequalify for mortgages. What if an employee being transferred from New York City could take a virtual reality tour of a home in Rome, Italy? Or, instead of shopping lenders for the best home loan deal, what if consumers could put their requirements for a home loan into an electronic "auction ring," where multiple lenders bid for the individual consumer's business by means of attractive rates and loan features which meet the customer's individual criteria?

Why couldn't a mortgage lender combine its resources with those of a large corporation to purchase entire housing developments for use by frequently relocated employees? Relocating employees could simply turn in the keys of their current house after selecting another home from the network of homes in their new city. Instead of owning a home that might not sell on the open market, the employees could own points which continue to accrue in place of equity. When the employee moves to the next home, money never changes hands; this would be true digital currency. Might technology be a key to offering home finance customers a custom housing finance solution, while at the same time affording the lender the opportunity to leverage its funding sources (i.e., securitization)?

Roles, Relationships Are Changing

Traditional roles and relationships within and between industries are changing. Market forces are forging a closer relationship between the consumer and the producer and between the technology and the service it provides access to. In many cases, in fact, the service is becoming indistinguishable from the technology, and the pathway is becoming as appealing as the product. This is especially true in the case of home lending. One of the world's largest mortgage origination companies proudly bills itself as "a technology company that just happens to make home loans." Clearly the focus on technology that mortgage lenders have today makes it easy to see how they lose sight of the fact that technology is the means to the end, rather than an end in and of itself.

As we move further into what has been described as the Information Age, the customer is being placed in control by technology, made available by the providers of the world. If we leverage technology to give customers presence, pathways and promise, they will become more engaged by our products and services, and they will return to our business again and again, perhaps becoming customers for life. As we meet customer expectations today, we must also anticipate how they will define their expectations tomorrow—and be ready to meet and exceed those expectations. Institutions that lead with this framework in mind will have a tremendous competitive advantage in the future.