TRUST: AN ESSENTIAL FOR LENDERS

Does your boss trust you? Do you trust your customers?

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I'm not a regular reader of the annual flock of business books. But, based on friends' high recommendations of it, I recently picked up Stephen M. R. Covey's best-selling The Speed of Trust.

I must say, Speed of Trust lives up to the recommendations. The author's central point is that "trust" is the ultimate core value in all human relationships. In business, without trust, speed goes down and costs go up. It's also true in personal, non-business relationships. Today's divorce statistics and high levels of actual and perceived unethical behavior emphasize how expensive the lack of trust in interpersonal relationships can be.

Covey's book got me thinking about trust and the lender's daily life, and also, the bigger picture.

Does your boss trust you?

I've had a long and varied working career by any of the conventional measures-years, geography, size of banks, types of responsibilities, successes and failures. This includes bosses and colleagues I've both liked and disliked. There are two bosses I particularly enjoyed as friends and mentors and another pair that I cordially loathed.

As they are all still alive as best I know, I'll say less about them than I might otherwise be inclined. One of those I didn't like offended me in the trust dimension and earned my enmity. Here's the quick version of what happened.

He asked me one day whether we had received some promised additional collateral. I confirmed that we had. "Show me!" he demanded abruptly.

So we walked across the bank lobby to the note teller's window and he inspected the documents. We had the collateral, and the documents were in order. But the fact that he insisted on personal verification was insulting to me. Verification is a standard internal control of auditors, loan review, and collateral clerks and the function is important. But in my case, I was the senior lender of that small bank and the account officer on that relationship. My word to the president of the bank was apparently insufficient. Our relationship lasted another few months until I transferred to another job within the company and happily left that situation. I am still offended by the memory of that affront even after nearly 30 years have elapsed.

By contrast, I had a boss a few years later that I liked for all the right reasons. He was experienced, smart, and highly competent lender and a man of his word. He treated all colleagues with respect and showed an abiding trust in what we did and how we did it. He never directly told any of us what to do on an account unless his advice was sought but he was always solicitous about whether we had the resources and support that we needed. I'd have done about anything for that man and he earned my loyalty, and my trust, day in and day out by his consistency, good manners, and unfailing respect.

Thinking about The Speed of Trust and the anecdotes and illustrations of the author has caused me to reflect on how we subtly and perhaps unknowingly impact our work environments. We send signals to peers, subordinates, and superiors by our unconscious actions. How do these impact our effectiveness as lenders? Are we making our workplaces more or less hospitable? The ultimate bottom line of this issue though is how is the risk profile of the institution impacted? Are the impacts always positive?

Trust, due diligence, and character

The Senate Government Affairs committee is about halfway through its series of hearings on aspects of the financial malaise we've been experiencing. As I write, in the next several days it will take up the issue of due diligence activities performed by rating agencies on the securities that were at the heart of a lot of big bank asset quality problems of the last two years-collateral debt obligation quality (the collectability of the mortgage pools securing bonds that were sold to individual and corporate buyers).

It seems to many that the rating agencies failed miserably in their duties of determining the relative level of risk of the underlying collateral of the securities that they examined. Why is this so? Did the agencies manipulate or ignore information? Were they too anxious for income? Were there conflicts of interest?

Maybe some of these issues were present to some degree. But I'm reminded of what President Reagan once said: "Trust but verify."

Due diligence is an important part of a lender's work in that financial information must be evaluated, collateral inspected, and judgments made by the lender on the overall competence and integrity of the borrower. What constitutes adequate due diligence and how might this vary with the individual circumstances?

We can't check everything first hand. Nor should we be in the business of lending to any borrower that requires such scrutiny. Trust is an important component of the interpersonal equation of how we deal with each other.

It's the first C of the Five Cs of credit: Character. Too many lenders who should know better were guilty of having substituted Charm or Charisma at the top of the list at the expense of a reasonable assessment of character.

Can a lender discern character?

How do we evaluate Character? As lenders, we're not trained psychologists nor moral theologians nor normally possessing skill sets or professional qualifications that make us uniquely qualified for specialized, professional judgments.

But we are skilled observers of business. We develop over time a sense of whether a business's financials are conservatively stated, consistent, and reliable. We observe how borrowers conduct their business. Are they, in the words of the TV commercial, "taking care of business?" Is he or she a straight shooter as forthcoming with bad news as well as with good?

Trust is a perishable commodity. We need to know that we're dealing with people who are on the up and up. We also need auditors with their special skills, and solid internal controls that make sure to the satisfaction of our bosses, owners, and regulators that we're doing what we say we are doing. How are we to determine the appropriate balance of trust and due diligence?

There's much to say and think about on this topic in coming weeks, especially as the various committees of the Congress go about their work.

A parting recollection

I recall a cartoon a few years back in The Wall Street Journal that showed two businessmen concluding a deal and shaking hands.

One is saying to the other, "Do you think we should have our lawyers look at this handshake?"

That seemed pretty funny at the time.

But it's not very funny today.

About Ed O'Leary:

Veteran lender and workout expert O'Leary spent more than 40 years in bank commercial credit and related functions, working with both major banks as well as community banking institutions. He earned his workout spurs in the dark days of the 1980s and early 1990s in both oil patch and commercial real estate lending.

O'Leary began his banking career at The Bank of New York in 1964, and worked at banks in Florida, Texas, Oklahoma, and New Mexico. He served as a faculty member and thesis advisor at ABA's Stonier Graduate School of Banking for more than two decades, and served as long as a faculty member for ABA's undergraduate and graduate commercial lending schools.

Today he works as a consultant and expert witness, and serves as instructor for ABA e-learning courses and a frequent speaker in ABA's Bank Director Telephone Briefing series. You can hear free audio interviews with Ed about workouts here. You can e-mail him at etoleary@att.net. O'Leary's website can be found at www.etoleary.com.

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