
WHAT SHOULD 'OUTSIDE THE BOX' MEAN TO A LENDER?

Sometimes, the issue is, where is the box and who's standing in it?

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Over a long career, I've heard lots of talk about "thinking outside the box."

I'm not sure what that means, other than being a cliché intended to goad bankers into thinking in unconventional ways. These are the kinds of times when people haul out such clichés (ironically), in hopes of finding new avenues for success.

Be careful. But don't reject the cliché out of hand, either.

A macro lesson from micro-lending

Thinking outside the box can result in running roughshod over an otherwise conservative lending policy.

There are basic principles in our business, and they are time-tested and roadworthy, by and large.

There's not much new either, other than more creative ways to package or sell services.

There are new products or variants of financial products introduced most every day. Providers and sellers of life insurance products are the best examples of product innovation that come most easily to mind. Banking typically moves more slowly-as it should, as our currency is in the form of other people's money.

As I was concluding my merger-related duties with the absorption of First Security Bank of New Mexico into Wells Fargo, I had an opportunity to devote quite a bit of time over a period of a few months to the activities of a micro lender, Accion of New Mexico. Accion is part of a network of commercial micro lenders that are affiliated with, but independent of, an international organization of a similar name. I was also a board member for several years preceding my functioning as a loaned executive from Wells.

I firmly believed that Accion needed a revised lending policy. What it had was decent. But the policy didn't adequately describe what Accion had evolved into over the previous several years. It was now a lender with a top lending amount per client of medium five figures. It had come to have a variety to its loan portfolio that was hardly considered possible just a few years before.

I set about to rewrite the policy with the encouragement of its president. Having written many loan policies in my banking life, it was not hard to do. When it was ready for comment, I took it to a small committee of client borrowers and internal lenders.

One woman, an early and successful borrower at Accion, listened patiently and politely to my presentation.

Suddenly she said, "I know what you're doing. You're selling money."

Keeping your lending eye on the ball, carefully

Everyone around the table—except me—seemed to think this was a "Eureka" moment.

Frankly, I was confused by what the customer meant. It fell to others to explain to me that the group had never read nor seen a loan policy that honestly attempted to find ways to do a deal rather than pick a deal apart.

Here's a point to consider by way of illustration.

If your loan policy says that your bank will advance 65% of NYSE listed collateral, then would your management encourage its lenders to be more conservative than that? Would an attitude acknowledging that 65% is allowed but 50% is more conservative and therefore better, be encouraged? I hope not!

You don't expand loan outstandings by encouraging ways to lend less to each customer.

One lesson learned early in my lending career was that you should lend a customer enough to accomplish his or her purpose. If you can't prudently do that, then you shouldn't lend into that situation at all.

These are small examples of thinking outside the box when writing a loan policy. You're selling money. Are you really telling a lender how this can be done or are you finding ways to show how conservative you and your bank are? I used to tell my lenders, "Don't say no, say how."

Taking your job home, in a good way

Another rich source of experience in learning to think outside the box comes from hands-on workout experience. Here's an off-the-wall example of what my years in the workout trenches taught me about structuring a deal.

My house in Albuquerque is for sale. In fact, it has been for months, in a lousy market. No offers have been received yet, even after a reasonably steady flow of lookers.

As I write this I'm expecting a written offer from a doctor who is moving to town from California. The problem is that the contract will be contingent on the sale of her condo in Berkeley.

One way to think of this is to imagine that I'll now be captive to the sale of two homes, one of which I have no control over whatever.

The other is to say that the prospective purchaser is about the best prospect I'll likely ever get in this market and I'd better get the deal done if it's humanly possible.

My wife and I don't want a contingency contract. That's the easy part of the analysis but the challenge is to find a way.

How about a lease purchase? How about carrying a purchase-money mortgage back for a large amount but with a balloon maturity that's four or six months out with acceleration clause upon sale of the Berkeley condo? How do I transfer the fundamentals of ownership to the doctor while preserving her capacity and willingness to enter into the deal on a sensible basis for both sides?

The outcome is not yet clear. I may write about it in a future columns. But with all of the restructuring I've done and the money I've "sold" there must be a way-short of making the price so low that I'd not want to do the deal at all.

That's what thinking outside the box means to me.

On the job, such challenges some might call "the hard part."

But, frankly, for me, it's the fun part.

- 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.