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Plotting a SERVICING TAKEOVER

BY STEVEN KROPPER

It's time to put a new face on the mortgage banking business. If servicing was in charge of customer retention (instead of the origination team), the odds of keeping customers in the portfolio would mushroom. New technology, streamlined refi products and data-mining techniques can transform the business.

TODAY YOUR COMPANY IS PROBABLY *STILL* RIDING THE REFINANCING WAVE. Your origination department can barely keep up with the volume. Only in the back of your mind, when you're trying to sleep, do you realize that if you're getting other lenders' customers in droves—someone else is getting yours. But you put yourself at ease by reminding yourself that if your people are busy, business must be good. Right? Fast-forward one year. The refi bubble has burst. Rates are high and going higher. The economy continues its downslide. Consumers are scared, and it seems like no one wants to make a move. Your origination department is covered with cobwebs. You worry: Is your job on the line? What went wrong?

OK, you ignored the ugly little secret of your industry: 93 percent of all borrowers will eventually leave you for another lender. Refis are rate-driven and depend on external factors, while purchase originations are relatively stable; there will always be roughly 5 million single-family home sales a year. And you neglected to notice that where there are refis, there is also massive portfolio runoff. Next time, what will you do differently?

ILLUSTRATION BY SARAH HOLLANDER

THE UNITED STATES
DOLLAR
MONEY
THE UNITED STATES OF AMERICA

Now is the time to hatch a seven-step plan for servicing to take over the mortgage company. It's time for servicing to make a power grab for the good of the organization.

1. Focus on retention, and let your servicing department do the heavy lifting

Sound far-fetched? Not if you want your revenues to grow. Your company is already spending about $2,000 to *acquire* a customer looking for a new loan. This includes sales and marketing costs, processing and the involvement of mortgage brokers. Imagine how much you could save if you spent just a fraction of that amount *retaining* that customer instead of spending so much to acquire his or her neighbor.

Putting servicing in charge of retention efforts costs much less than acquiring loans via the branch office or through mortgage brokers. Let these higher-cost channels keep the first-time buyers while you focus on move-up buyers. Remember—According to *The 2000 National Association of Realtors® Profile of Home Buyers and Sellers,* 58 percent of all purchase loans are for current homeowners buying their next home; that is, your current customers.

Why should servicing (the folks who already have and know the customers) run the company instead of origination (the folks signing new customers) or marketing (the folks trying to bring new customers to origination)? Because servicing knows the customer best. It has the most contact with current borrowers. It sends out the statements every month. It knows the customer's payment history and current rate.

Unlike origination—which, after collecting a commission, has wadded up the customer's paperwork and moved on to the next loan—the servicing group talks to the customer several times a year. When the customer is about to defect, servicing is the first to know.

There is a mistaken perception that loyalty doesn't matter—mortgages are a commodity, and customers will go wherever rates are lowest. However, some studies contradict this theory. According to an April 1998 strategy brief by Frederick F. Reichheld for Boston-based Bain & Company Inc., *The Loyalty Effect Essay #4: The Forces of Loyalty vs. Chaos,* a five percentage point shift in customer retention consistently resulted in 25 percent to 100 percent profit swings. Bain & Company's study looked at retention in a wide array of industries. While the loan itself might be a commodity, the service you provide in getting the loan is your opportunity for differentiation. Just by taking a few proactive steps to keep the customers you have, you can impact profits dramatically.

Now that you've given servicing the priority job of retaining your existing customers . . .

2. Give servicing reps the tools they need

You already know that the best customer data lives in servicing. Now you need to make sure you're gathering the right information and using your database to make the right offers to the right borrowers at the right time.

Lisa Fagan Teifke, vp of e-commerce in the Denver office of Jacksonville, Florida–based ALLTEL Information Technologies, sees the customer database and the tools to access it as critical in servicing-driven retention efforts. "While a department may be set up for retention, it should have access to the servicing record and to the customer history. And because every retained customer is treated as a new customer (because the secondary market requires new documentation and new due diligence, and cannot make use of existing customer information), you need to have [Fannie Mae's] Desktop Underwriter®, [Freddie Mac's] Loan Prospector® and other collateral and credit tools integrated," she says.

"Take advantage of information in your hands. . . . With the risk of runoff so high and portfolio sizes growing, the lender focus needs to be on retaining what they have. The current lender is armed with information that a competitor would kill for, but it's only useful if they're mining the data," says Teifke.

Sam Rizzuti, director of servicing business technology at Principal Residential Mortgage, Des Moines, Iowa, sees retention as "a partnership between origination and servicing." Principal's data warehouses contain a lot of information, including loan and customer data. Rizzuti says, "Success comes from consolidating the history of customer contact, loan parameters and contact behaviors.

"There is the potential to profile customers behind the scenes, based on Web and phone behavior, then to present them with proactive and relevant offers based on your mining of the data," he adds. One of Principal's goals is to have a customer profile available in customer service, at the customer service rep's desktop. That way, the rep can present a relevant offer—as if the customer were doing self-service over the Web—and make a data-rich handoff to production if needed.

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"For many customers, self-service is the best service, and is easily delivered with Internet tools," says Teifke.

Currently, transferring a call from servicing to origination is anything but seamless. Loan production typically has no access to servicing's knowledge database on the

borrower and won't know the borrower's payment history. This will frustrate the borrower, who expects each bank department to have access to the same information. But this problem is not unsolvable, as Bank of America, Charlotte, North Carolina, has discovered.

According to a November–December 2001 article in *Financial Services Marketing* by Matthew DePaula, "Go Ahead, Call Me," Bank of America is making call-center improvements for its mortgage loan customers to avoid such frustrations, by broadening roles and responsibilities so that credit-risk and approval decisions are made more quickly. No longer does one department specialize in only one step in the process. As a result, Bank of America has reduced mortgage customer handoffs for approval from five to two, according to the DePaula article. Bank of America began treating its existing mortgage customers differently, with practices such as eliminating stringent income-verification requirements.

Bank of America's main goal was to boost its overall marketing strategy and deepen customer relationships—not only to retain borrowers, but to cross-sell other financial products. Increased efficiency was another fortunate by-product of these changes. Bank of America decreased its decision time for home loans by 87 percent and reduced the period from loan application to closing to 19 days.

3. Give your servicing reps the incentives they need

Today, servicing is being offered incentives to minimize the time spent with borrowers and to intervene only in the event of default or delinquency. Minimizing agent call time is the measure of success; even better is not having the phone ring at all. In the servicing department, silent phones are a sign of success, while in loan origination the opposite is true.

You'll have to challenge the status quo to make this turnaround in management attitudes toward servicing occur. "Many lenders view servicing as an operational function rather than a strategic, relationship-building one," says Norwood, Massachusetts–based independent industry analyst Richard Beidl. "This is partly why there is such a high rate of defection in the mortgage industry," he says. "Instead of reducing obstacles for existing customers, the lender does nothing. Given that existing customers have to jump through the same hoops as new ones, most would rather get a root canal than refinance."

Start the sea change in servicing's role by mining value from the payoff request. When customers call to find out their payoff balance, it's too late to keep them—but not too late to realize some revenue through a referral to a move-related vendor. Property and casualty insurance carriers, moving companies, utilities and home-maintenance services all want to know ahead of time when someone is moving, so they can offer their services. A payoff request comes at the right time for these companies to make an offer.

Based on my experience and research, I estimate that revenue from all move-related vendors per customer ranges from $20 to $150. Once you've developed a revenue stream, you can install a compensation plan to motivate the servicing representatives to make these referrals. This will require tracking and compensation for anything from simple name capture to a more extensive performance-based system where reps are paid for signing up the customer to particular services. Third parties make Web-based sign-up for services available, and these can be installed on the reps' desktop in a day, customized to track their ID and generate reporting.

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The next step toward implementing compensation requires moving upstream to an earlier point in the home-buying and borrowing processes, and taking action to retain your customers before they're ready to move. Obviously, you will want to know if your customer is considering moving at a point at which you can do something to retain him or her. If the borrower is making a casual query to confirm his or her equity, you've got a valuable opportunity for an origination referral. You can train your reps to follow up each payoff request by asking the reason for the query, to remind the borrower that he or she has preferred status (or some other fancy name for the premium you will offer your existing customer for sticking with you) and ask if the borrower would like to be transferred to origination for a quote.

4. Meet your customers where they are

Cheryl DeRoche-Johnson, first vice president of e-commerce in Ann Arbor, Michigan–based ABN AMRO Mortgage Group Inc.'s Norridge, Illinois, office, advocates being able to communicate with borrowers in their preferred communication channel. "ABN communicates with the customer in as many ways as possible, so that they can proceed with a new loan in whatever method they're comfortable with," DeRoche-Johnson says.

"The technology and systems that enable this should be available to all channels, so that anyone who touches the customer—whether they're in the call center, the branch office or online—has access to the same customer information. The lender will provide real value if [it] can address the

consumer with a smart analysis of their current portfolio information in conjunction with market conditions, and tell them automatically how much they can save with a new loan," she adds.

When you communicate with your customers, your message should be that you are available for them and eager to help them obtain their next loan. You should also clearly convey that, as an existing customer, they have a leg up either in pricing, processing or some other product benefit. Give them a discount on closing costs, a slightly better rate or a reduction in paperwork as a dividend for sticking with you.

You also can implement e-mail rate watches, specific messages about refi savings, cash-out options or a link to multiple listing service (MLS) listings or historical home-sales prices (comps) such as those available at Domania (www.domania.com).

The right kind of regular customer contact should help detect when the borrower is at risk of leaving your portfolio. You can start when the customer tips you off during a servicing call. Begin implementing proactive practices that determine when the borrower moves into the buy zone, becomes at risk for runoff and warrants an outbound solicitation.

5. Once met, move them online

To detect customers' plans, you need to do more than just mail a statement each month. You need to migrate your customers to e-mail and the Web. Direct mail is too slow and too expensive. It also has a low success rate. Online systems, on the other hand, enable you to gather customer information while providing your borrowers with the information and service they need to make smart home-financing decisions.

Moving the customer online has additional benefits. With online statements and electronic bill payment, you're reducing costs dramatically and accelerating payment receipts. You can offer incentives to your customers to move them out of the call center to online with benefits such as online balance checking, real-time escrow and payment reporting. Tasks that currently require your time and money can be outsourced to the customer by moving to online self-service. Meanwhile, you can use technology on top of traditional methods to detect when your customer is looking at rates or considering moving, and tailor your offers accordingly.

6. Streamline, streamline, streamline

A streamlined loan application process means the servicing rep simply notifies existing borrowers that they enjoy a discount for a new loan, and are required to fill out much less paperwork than new customers. Taking the pain out of a very arduous process through streamlining can result in improved customer retention rates as well as dramatically reduced costs for the lender. "We believe the lender can save 171 basis points per streamlined application and bring direct costs down to $300 per loan," says Matt Lind, a Hingham, Massachusetts–based partner in the STRATMOR Group. Streamlining the application process for existing borrowers will give you an advantage over competitors vying for your customer's next loan.

Currently, the agencies and government-sponsored enterprises (GSEs) offer what are called "streamline loans" for rate and term refinances. Under the terms of these loans, borrowers with superior payment histories can be approved for a new loan with virtually no documentation and new paperwork. Moreover, processing of such loans involves little more than a title update, after which the loan can be closed—in other words, no hassle for the borrowers and low fulfillment costs for the lenders. Few lenders, however, have harnessed the automation potential of streamline loans from marketing through closing.

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One lender that has accomplished this during the current refinance boom is Irwin Mortgage Corporation, Indianapolis. "Originating loans under a streamline format can save lenders around $1,000 to $2,000 per loan in marketing and back-office costs, relative to standard loan origination processes," says STRATMOR Group's Lind, who led Irwin's streamline initiative. By taking out all the unnecessary steps, he says, "you can originate a streamline loan for around $300." Extending streamline concepts to cash-out refinances and purchase loans would, according to Lind, "revolutionize the industry" and give the existing lender a tremendous advantage over other lenders vying for their customers' next loan.

Because streamlined application processing reduces sales and marketing costs as well as much of the origination function, some cash is freed up to offer your customers very compelling pricing. You can offer a lower price or up to $1,000 off of the front-end costs. Or you can offer a higher price with conveniences such as instant closing with a rate that's one-quarter of a point higher. Think of the advantage you would have over competitors in the thick of a refi boom by being able to offer your existing customers a menu of quick options from which to pick. Many borrowers would gladly pay 7½ percent with no extra effort, instead of 7 percent with massive paperwork, credit checks and everything else that accompanies a new loan—especially if they could take that loan with them to their next house.

According to DeRoche-Johnson, ABN AMRO Mortgage is

using technology to streamline the process, with one of the goals being making relevant data available to anyone who touches the customer in any channel. But there's still room for improvement, she says. "We're using Loan Prospector and Desktop Underwriter, but there are no industry-standard delivery mechanisms and there are technology integration issues. Some parts of the process are automated, such as ordering credit reports, pulling a title and ordering the appraisal," says DeRoche-Johnson. "There are a lot of options out there, but the question is: Whose technology will get there faster?"

The best indicator that a borrower will be timely and consistent in making payments is past performance, and the servicing department has perfect information on payment history. Automated underwriting engines are effective to a degree, attempting to predict the future based on the past, using proxies such as credit reports to forecast future payment behavior. However, using the servicing department's definitive payment data can result in more seamless automation and higher loan production.

After all, says Beidl, "The current lender has perfect information on [its] customers' payment practices. While income and collateral do matter, it is the propensity to pay, and to pay the mortgage specifically, that are important."

Robert Habert, senior vice president of Toronto-based BCE Emergis, a provider of business-to-business (B2B) e-commerce infrastructure solutions to the mortgage industry, says, "Recent experience during the refinance boom has shown that 18 percent of rate-locked, streamline refinance offers made to eligible borrowers have been accepted. This already high acceptance rate would have been even higher were streamline cash-out refinances available. We believe that lenders can save over $1,000 per loan using streamlined processes for marketing and fulfillment—as well as dramatically increase production volume. Clearly, going forward, streamline loans and streamline processes will be increasingly important factors in retaining borrowers."

7. Challenge the secondary market

Dealing with the secondary market issues of streamlined products is one of the most difficult steps, as it involves some factors not under your control. But the market is beginning to recognize that current systems must evolve and allow for streamlined products. You want to make it easier—not harder—for your customers to stick with you for their next home loan. One way to make it easier is to treat your existing customers differently. Selling a new loan to a new investor will require full documentation, but keeping the loan with the current investor, with different terms, should require less.

"The industry structure ensures that there is currently no customer loyalty to one lender over another," says Beidl. "But Countrywide, for one, is making it easy for customers to stay by offering a product for the customer to do a one-time rate reduction refinance. The rate and the amortization schedule change, but nothing else. The note and the lien remain unchanged; the loan has simply been restructured within its current portfolio." The challenge is to convince investors it's a better alternative to keep a renegotiated loan in the portfolio than to lose the loan altogether.

One solution Beidl foresees is, because the GSEs hold 45 percent of all loans they could negotiate with top lenders to craft a new transferable product—a new kind of mortgage-backed security that allows for a change in conditions without creating a new loan. Clearly, there is a future for portable mortgages that go with the borrower, not the house. It works in Europe today.

As an alternative, the lender could change the property address on the note and then put a second mortgage on top to fill the gap between the last loan amount and the new amount to be financed. Today, some lenders deal with GSE loan limits that prevent jumbo lending by topping off the loan with a second tranche.

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You now have a seven-step plan to allow servicing to take over the mortgage company by seizing control of retention efforts. If you empower the servicing group with the right tools, technology and compensation, and enable it to use the valuable customer information it has, you can prevent your borrowers from leaving.

Your customers can't help but stay, because it will cost them less to stay than to go with a competitor. You'll identify your at-risk borrowers and make relevant proactive offers. You'll streamline the application process to make it easy for them to stick around.

Do you really want to leave your company's future to the whims of the market and the ebb and flow of refinance and home-buying activity? Or do you want to build a firm foundation for success before the refi bottom drops out once again? **MB**

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