Mortgage Banking & Technology: Lenders’ Perspective

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Executive Summary

CC Pace recently completed a survey conducted with a broad array of mortgage lenders that highlighted the mix of technology solutions lenders are using in order to meet the challenges in today's marketplace. Although the majority of lenders surveyed consider themselves fast followers, if not early adopters, they feel the technology, particularly with their vendor-maintained loan origination systems, is not up to the task of meeting all of today's challenges.

The survey findings detailed in this white paper include:

- There is a growing optimism among lenders and a transition underway to a more offensive stance regarding the market
- Lenders are facing numerous competing priorities, with creating a better customer experience, cost reduction, the need for product diversification and IT security concerns are at the top of the list
- Lenders believe in the promise of technology providing competitive advantage, but few are actually seeing measurable results in this regard
- Lender satisfaction with their current technology is evenly divided between those that are happy, resigned and decidedly unhappy
- There is a lot of buzz around FinTech, but little shared understanding of what it really is and whether it is here to stay
- There is a much clearer belief that the future lies with the digital mortgage and that everyone needs to get on board
- That said, most are still at the starting gate with little real progress made towards that goal

We hope you find the survey results presented in this white paper to be informative and thought provoking. We encourage you to share your thoughts on these issues with us.

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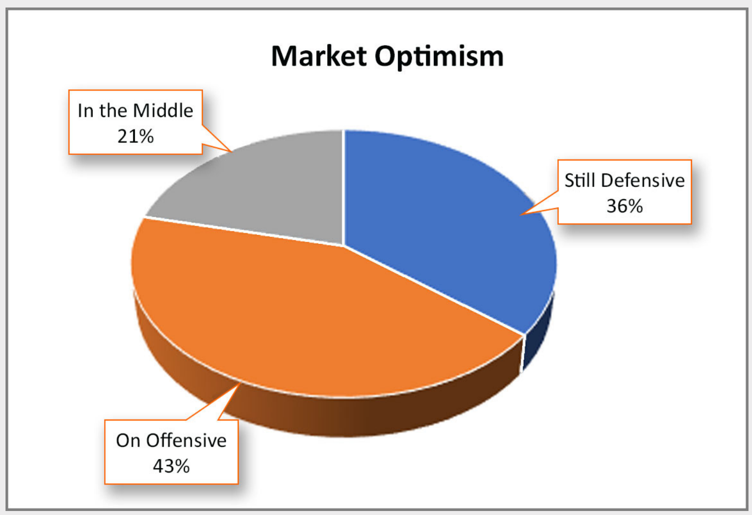
Introduction

CC Pace recently surveyed a broad cross-section of mortgage banking executives across the country. Included in the survey were lenders focusing on one or more of the primary origination channels: retail, correspondent, and wholesale. The size of participating organizations ranged from credit unions and community banks to regional and national mortgage lenders who originate over $10 billion annually. Participation was anonymous to ensure an open conversation regarding some of today's most challenging topics. Lenders shared their perspectives on the current lending environment, their priorities of the day, and their thoughts on moving forward.

Today's Improved Lending Environment

Lending executives largely expressed cautious optimism about the overall mortgage market. When asked if they had officially moved from a defensive posture of combating regulation, to now being on offense, responses were narrowly in favor of optimism, with a number feeling stuck on the fence between the two. Their focus is shifting to organizational development, providing better service, and investing in tools that will enrich the customer experience. As one participant explained, "the credit box is certainly starting to expand a little, which gives us some hope and relief." Another lender remarked, "The need to defend yourself against irrational review is getting much better." Nonetheless, the sense of relief was almost met with a kind reminder by another lender who mentioned, "Product guidelines are shifting back towards pre-crisis levels but we are still years away from having enough performance insight to negatively impact the market." In the meantime, it's safe to say lenders are finding solace in the today's more optimistic environment.



Lenders' Priorities

Lenders participating in the survey shared four key priorities: enhancing the customer experience, reducing cost to produce, product diversification, and IT security. These are not new priorities to the industry, but the rise of IT security

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concerns and a renewed focus on the customer experience serve to shine a new light on these areas.

Customer Experience

In order to support their customer experience initiatives, lenders are comparing functionality provided by their LOS Vendors to other offerings in the marketplace. Oftentimes they are supplementing their LOS platform with additional functionality from other providers, with an emphasis on mobile computing and better borrower tools. Lenders we spoke with are regularly looking at new solutions to integrate with their LOS platforms as a means to streamline their lending process for both their borrower and themselves. "It's not just opening new offices; we aren't just looking to put more flags down in the dirt. We are constantly analyzing how we can leverage what we already have while constantly looking at new technology in the new climate." Another lender referenced airlines and how they used technology to improve the customer experience: "It's the same as when airlines wanted to leverage technology to help reduce the costs associated with checking people in and then issuing their ticket. Airlines provided consumers a kiosk for self-check in, which ended up being a huge cost savings that also enhanced the customer experience significantly." The mortgage industry and process have unique requirements, but there is a desire to find the mortgage equivalent of the airline online check in, Uber or other solution to provide the customer with the best experience possible.

Reducing Costs and Finding Efficiencies

Always a top priority, but with a growing focus, lenders are working hard to reduce costs. The respondents described wanting to optimize their approach to better leverage technology, as well as address poorly implemented process changes that supported the various compliance and regulatory requirements implemented over the past few years. Yet another driver discussed was interest in enhancing the customer experience to make "self help" more intuitive, thus reducing support costs. Overall, cost reduction was one of the most robust discussion points throughout the survey process.

One lender summed up the criticality of reducing operating costs by saying, "overall cost to produce for lenders needs to go down by as much as 20%, to ensure the survival of many." Yet another lender highlighted their approach by saying, "we are continually looking at digital loan transformation - how can we get more and more data electronically. There is a desperate need for some kind of exchange to conduct e-signs, e-consents and e-delivery so that everyone is using a common platform to execute the final closing." Another lender showed their focus on improving internal operations for an overall

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superior process, "we are focused on process automation, instead of mobile apps or web presence, we want fewer people making better decisions, faster."

Consistently, the responses described the desire to lower cost to produce with the added benefits of higher loan quality, faster turn times and a better customer experience. Process optimization was highlighted as a very critical practice to helping a lender reduce operating expenses and increase efficiencies. While some organizations are using internal resources, others are bringing in external consultants [such as CC Pace]. Engaging consultants who work with multiple lenders each year brings a broader set of best practices and technology insights to the effort, challenging the existing process and more effectively helping lower the cost to produce, thereby resulting in increased efficiencies.

Product Diversification

The reduced focus on regulatory changes and the focus on a purchase market limited by the available credit box has highlighted the need for increased product diversification. The CIO of one emerging markets lender made his point by saying, "The markets are very opportunistic. There are exciting niches for interesting products that are starting to open. It seems other revenue streams are now being considered by the traditional mortgage lender. It's not just a standard mortgage loan anymore." The lenders agreed that the easy answer could be to simply expand further into Non-QM lending, but warned to be prepared for any unintended consequences. Overall, there was a belief that it's prudent to have a healthy balance of QM, Non-QM and niche products to ensure sustainability and for a better balance of risk. However, this may be easier said than done. Lenders footnoted a series of challenges with trying to achieve product diversification. Once a lender has decided on a niche product offering, they then need to fully define their technology limitations and requirements. Next, they will need to define the manual processes, job aids, tools, training, and any other specialization required to execute flawlessly. Lastly, they need to decide if the ROI warrants the expense. Any niche focus will have a direct impact on strategy, processes, technology, people, marketing, and costs, each of which must be taken into consideration. With that said, most lenders mentioned a heavy focus on construction lending.

Each lender we spoke with seemed to hint at some level of diversification among a myriad of different niche products like First Time Homebuyer programs, 203k loans, rural lending, reverse lending, multi-generational

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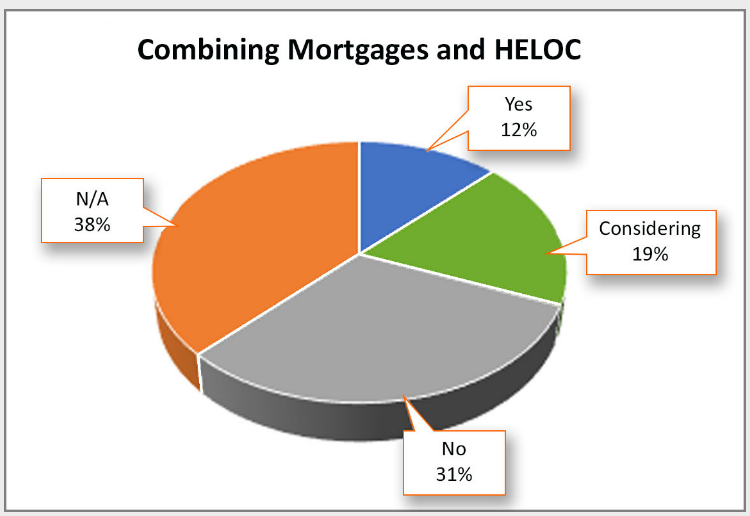
home lending, manufactured housing, and even consumer lending. Even as lenders believe product diversification is key to their long-term success, there are some concerns that their off the shelf ("OTS") LOS platforms lack the needed agility to address the changing product mix. [CC Pace has played an active role in helping our clients achieve this diversification with an individual project focus. Advice we offer our clients is to not assume, but rather to dig deep into offered technology to fully understand the actual capabilities of what is available.]

IT Security

With Equifax being just the latest in a string of breaches and security failures, it is no surprise that IT security ranks high among areas of concern for lenders. Generally, lenders feel that the question wasn't "if" a breach will happen, but a matter of when and of what severity. Lenders are focused on mitigating the risks that do exist by minimizing the number of incidents, with quick resolution should an issue arise. Larger institutions remain a bigger target, but smaller lenders are equally vulnerable, as they balance more constraints related to time, resources, and budgets. There is an increased reliance on third parties to manage some security aspects, as lenders utilize more cloud-based products with the system and data managed directly by a third party. This does not alleviate the responsibility or accountability of the lender, but does help to mitigate the stress associated with managing this focus area.

Integrating Mortgage and HELOC

We asked participants specifically whether they were contemplating combining equity production, typically aligned with consumer lending, with first mortgages in light of regulatory changes and the demands placed on lending platforms to conform to the integrated TILA and RESPA requirements. Contrary to our recent experience with client initiatives, creation of a consolidated real estate lending operation was not high on the list for many lenders. Based on our participant sample, lenders were evenly split



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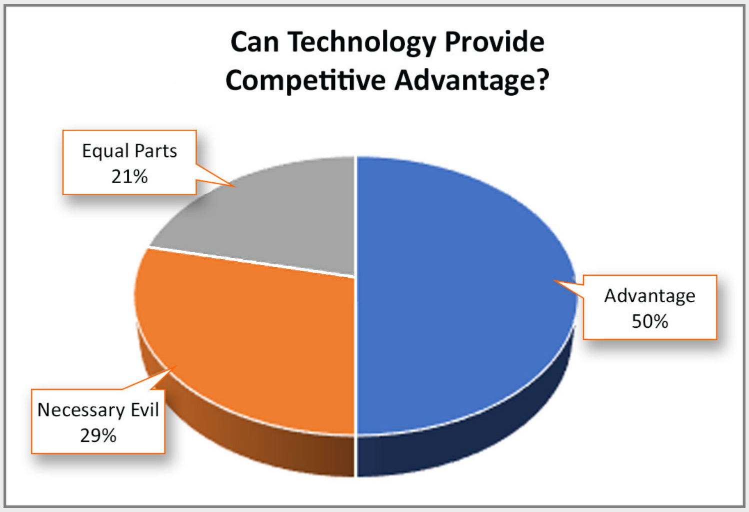
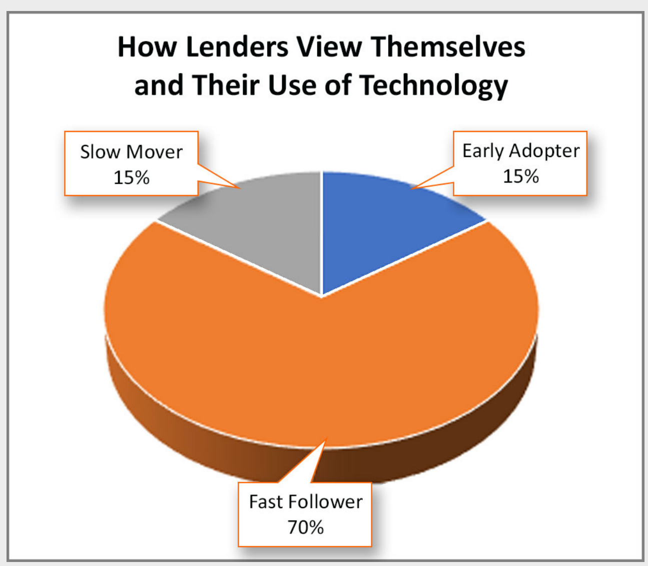
between those that have already combined their organizations or are considering doing so, those that are not actively considering it, and those that do not originate equity products or do so through affiliations.

Technology Strategy and Satisfaction

All survey participants believe their vendors have room to improve, with an even split between those who see the technology offerings available to the mortgage industry as being "behind the times" versus others that believe their vendors are "adequately" supporting today's requirements. No participants viewed the technology currently used by the industry as being truly innovative, or at least not to the extent that they would like it to be.



When asked if they viewed technology as being capable of providing a competitive advantage or whether it is simply a necessary evil and a requirement of being in business, our lenders were more optimistic. Regardless of whether the participations believed their own systems were providing sufficient advantages today, they clearly espoused the potential for technology to make a difference in how they compete in today's market. Meanwhile, our participating lenders categorized themselves and their approach to technology as being predominately "fast follower," rather than being early adopters or slow movers.



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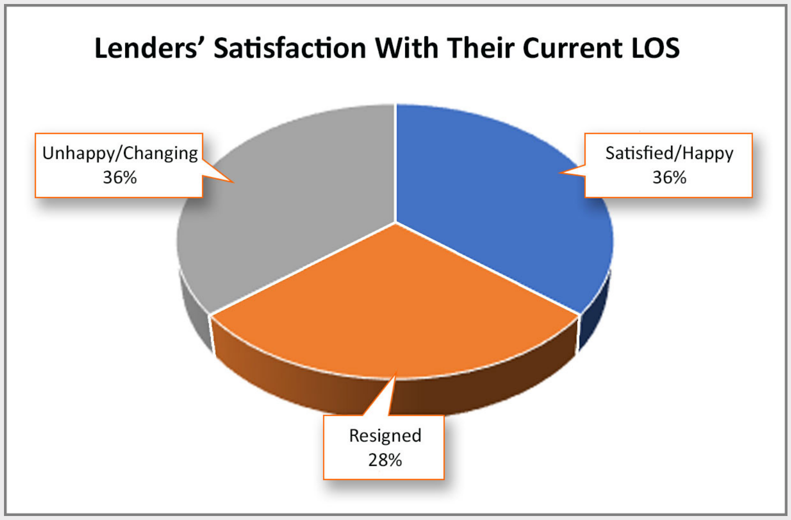
Technology in the Mortgage Industry

It was interesting to learn that despite technological advancements and changes within the industry, general sentiments regarding the OTS LOS platform are consistent with historical conclusions. Given the lender's general view of technology in the industry, it was no surprise to learn that lenders are not ecstatic about their own LOS platforms.



One frequently mentioned theme was that regardless of the marketing hype, technology vendors aren't doing anything revolutionary. At the same time lenders concur that technology is the key to a lender's ultimate success in this business. One executive pointed out, "if you look around at the larger originators who are growing – they are the technology based firms." Despite the successes of the current lending environment, lenders aren't necessarily confident or sure their existing technology will be able to support their changing needs, whether from product mix to customer experience to whatever disruptor may be around the corner.

FinTech

While FinTech is regularly mentioned in industry news and updates, our responses showed that lenders do not have shared understanding of what the term represents. The survey results highlighted that definitions of FinTech are like snowflakes, in that no single definition was the same. While one executive simply admitted they had no idea what it means, others defined it as a payment processing system, process automation, or something as simple as that of a new app for the phone. Several found it difficult to distinguish FinTech from the larger digital mortgage movement. So, despite the glamour and excitement surrounding the word "FinTech," at present there seems to be no specific path for defining the general concept.

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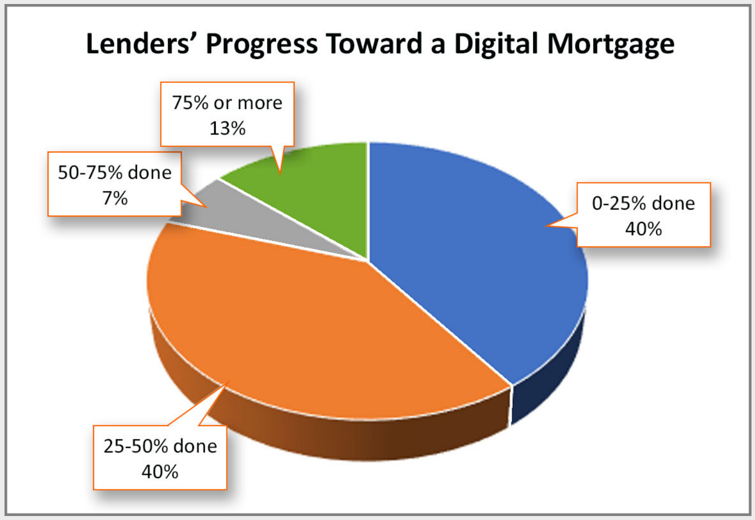
Digital Mortgages

Whereas FinTech proved elusive, lenders shared a relatively consistent definition of a digital mortgage: that of an end-to-end paperless loan transaction. Lenders were asked how far along they were in being able to deliver the fully digital mortgage. Not surprisingly, the results were a direct reflection of the overall view of today's technology, as indicated in this chart.



Relatively few of our respondents claimed to be close to having the capability to offer their customers a digital mortgage experience, with a significant majority, fully 80%, believing they are not yet half-way to achieving their goals. Everyone recognized that this is where the future lies, but many owned up to the fact that they have barely begun the process. Aside from the biggest hurdles of appraisal, title and investor delivery – most agreed that the primary challenges to achieving their goals are related to process gaps, data gaps, and disparate systems. One lender in our survey highlighted Fannie Mae's Day 1 Certainty, and the role it may play to achieve a truly digital mortgage. Others pointed to artificial intelligence and robotics. Virtually everyone agreed that a greater emphasis on data sharing and validation, with a significant increase the interconnectedness between systems is required to get there.

While just a limited number of lenders appear to be close to delivering a digital mortgage experience at this time, the majority are clamoring for a solution that will get them there faster.

Conclusion

The culmination of our responses made it clear that increasing pressure on vendors and their off the shelf LOS platforms is expected, as the desire for technological improvements and seamless integration across providers continues to rise. In order to meet their own specific needs, lenders are

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looking to extend their existing systems, either with internally developed functionality or (more frequently) with one of the many products being offered via the Cloud. At the same time, and to manage costs, lenders are continually looking at what their LOS vendors are doing with the platform, and what functionality is being added that may negate the need for one or more of those additional products.

Vendors are aware of the changing landscape and many are providing enhanced functionality by offering integration tools to streamline the exchange of data with other products or purchasing add-on technology or vendors to integrate into their own offering (with varying degrees of success). Others, unfortunately, are simply maintaining status quo without a clear strategy for their future. Those in the latter position can be expected to see a loss of market share as lenders migrate to solutions with better connectivity and functionality.

While it is unlikely that an Uber-type solution could work in the mortgage industry, there is competition looming from the FinTech arena. What form that competition will take or how revolutionary the change it brings to the industry is still unknown. Lenders need to stay aware of offerings from those that aim to disrupt the standard technology offerings to remain competitive, despite what changes may be coming.

While there is still a lot of work ahead of them, lenders have clearly recognized digital mortgages as their future. However, there are still too many lenders who view this transition as a technology-based change rather than the business-driven transformation that it needs to be. There are many aspects that need to be considered throughout the evolution, including business process, vendor and investor acceptance and business model assessments of service providers to ensure a cohesive, legal and efficient process. While technology clearly has a role, it should not be the driver for this change.

There is a lot happening within the mortgage industry. While the LOS vendors are making attempts to keep up, lenders are looking beyond the core system to ensure they have the needed functionality to remain competitive and provide a positive customer experience for their borrowers.

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About Us

CC Pace is a business and technology consulting firm headquartered in Fairfax, Virginia. For over 35 years, CC Pace has built its reputation on an unwavering commitment to customer satisfaction and is nationally recognized for solving business problems and delivering high-impact results. CC Pace specializes in the mortgage banking and financial services industry and our clients appreciate that we understand their business. Our deep domain experience allows us to design solutions to not only meet their needs, but achieve both measurable bottom-line results and significantly improved business execution.

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