WHITEPAPER

Future of Commercial lending

Taking Banks to the
future, faster. Together.

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Introduction

Regulatory hindrances and the time needed to secure the funds in commercial lending are still quite high and not feasible for corporates and businesses to fulfill their need in today's competitive business world. A business can fulfil its operational purpose i.e., purchasing supplies, paying payrolls, acquiring assets, etc., and borrow funds from a financial institution for business expenses, covering costs or equipment purchases required for operations or expansion. The major requirement which commercial lending fulfils is capital expenditure of a business or the cost bore for expansion of business.

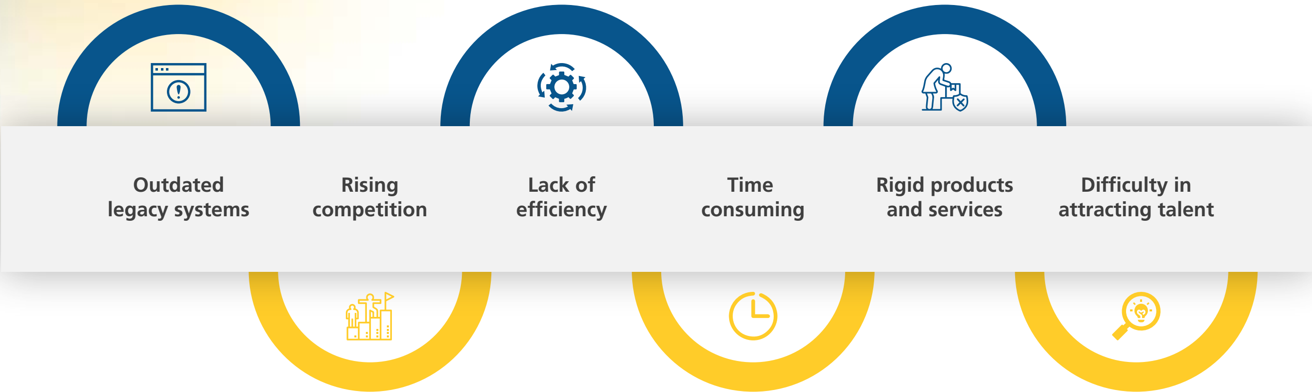
As per a survey by Allied Market Research, the global market size of commercial lending was $8,823.53 billion in 2020, which is going to be $29,379.83 billion in 2030. It is expected to grow further with a CAGR of 13.1% from 2022 to 2030, with the US holding more than 36% of it. This continuous growth shows how necessary commercial loans have become when it comes to any investments like investments in technology, equipment, businesses, etc.

Why does the current process of commercial lending require a change?

Outdated legacy systems

Legacy systems make the process of commercial lending more complex. These outdated systems increase costs and time consumed, leading to hindrances in terms of scale of growth, while the organization is not able to harness latest innovations in the market.

The pandemic ensured that all banks switched to digital. This led to fintechs using their tech expertise to educate bankers on the use of latest technology and digitized ways of lending.



Rising competition

Due to the rise in current market competition, commercial banks need to uplift their product quality and personalize the consumer experience while promoting data analytics. To cope up with the changing technology, banks need to digitize and switch to the latest technologies to increase their customer base and create brand loyalty. Fintechs are challenging the banking industry through digitization. Data and technology are the two main aspects where fintechs are a big challenge for the legacy banking model of commercial lending.

A rise in the number of new small businesses and startups can be seen, as people are selling an existing business and moving to another venture. This has led to a drastic increase in the demand for commercial loans.

Lack of efficiency

The problem related to optimum use of resources always exists in an organization. A bank always wants to streamline its operations to reduce the cost of maintenance of legacy systems. To tackle the rapid change in technology, banks need to shift to newer technologies.

Heavy investments are being made by banks in data cleaning. Tech experts are providing new databases, which will make the lending process faster and more efficient.

Time-consuming

The current commercial lending process is so time-consuming that the customer must wait for a long period of time before the bank completes its formalities. It takes around five to six days to find a lead, go through underwriters and close the deal for small or mid cap businesses. It is a cumbersome process and sometimes decreases the working efficiency. Due to the time-consuming process of legacy paper-intensive underwriting, banks are suffering losses in terms of customer generation, leading to them losing their positions in a competitive market.

After the pandemic, banks have changed and customized their products according to customers' needs. Due to new tech partnerships, quickly approved loan applications and diversified digital products can be seen.

Rigid products and services

When banks have limited access to customer's data, it leads to a decline in performance. In most cases, customers want banks to understand their preferences and requirement, which isn't the case. Automation of lending processes have led to banks achieving new heights in generating revenues out of a self-service portal.

Difficulty in attracting talent

Technology changes and a growing demand for latest software, coupled with employees who understand only legacy codes, have led to roadblocks in attracting new and talented individuals with expertise in new technologies.

A new department with expertise in specific services should be introduced. As products are being personalized according to the customer, services provided through portals and applications need to be upgraded.

Which commercial loans are generating more revenue for banks?

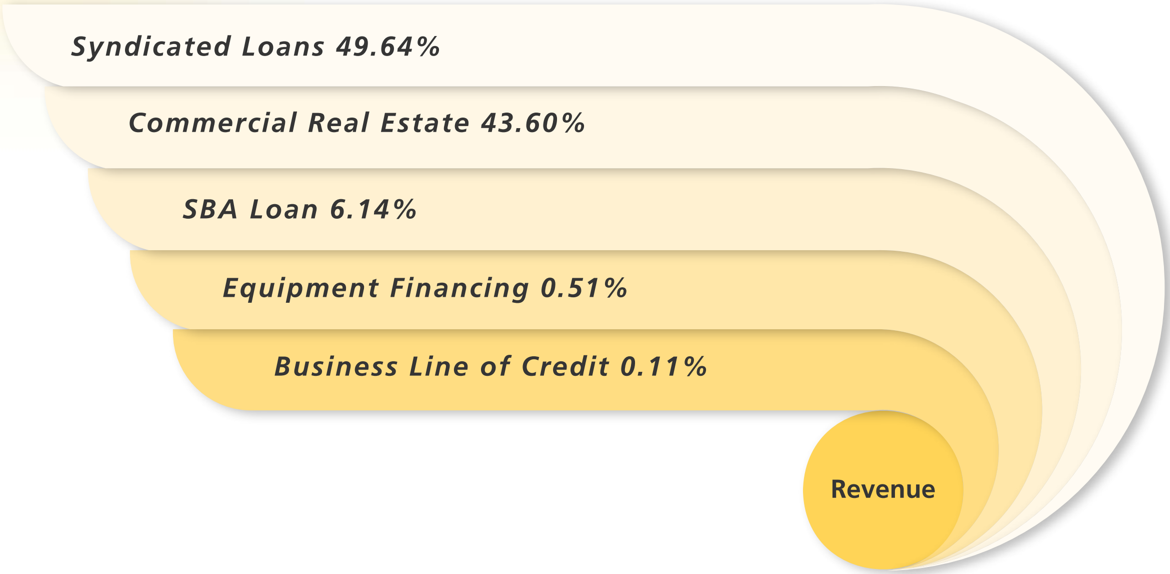
Banks usually deal in commercial mortgages, equipment loans, loans secured by AR (account receivables) and loans planned for expansion. The main question that arises here is that are these loans able to increase the profitability of banks? For banks, to be able to make more profits out of commercial loans, they need to focus on those that provide assistance to business operations and fund startups. Some loans that can generate more profits to banks in the upcoming years are:

Loan Type	Global Market Size (USD)	US Market Size (USD)	CAGR (%)	Revenue (USD)
Commercial Real Estate Loan	$7968 Billion	$430.7 Billion	11.3	$900.38 Billion
Business Line of Credit	$34.8 Billion	$14.1 Billion	7	$2.36 Billion
Equipment Financing	—	$36.92 Billion	4.7	$10.6 Billion
SBA Loan	$435.71 Billion	$270 Billion	9.2	$126.69 Billion
Syndicated Loans	$3800 Billion	$2500 Billion	14.4	$1025 Billion

Commercial real estate loan

This type of loan provides finance to businesses looking to buy new property. These are loans that generate more profits to banks as there is an uptrend on new businesses setting up. A sub-category of this is Commercial Construction Loans, which will be profitable for banks in the long run, given the pace of the construction industry’s growth. Construction companies have started to recover from losses owing to lack of operation due to the pandemic. The requirement of commercial construction loans has increased given that companies are expanding their region to support the growth of recovery.

Revenue Comparison of commercial loans



Business Line of Credit

A type of loan which allows a customer to borrow a pre-determined amount of funds whenever needed and pay it back later. This type of loan highly in demand as businesses need funds to manage their operating expenses and short-term needs. More businesses being setup translates to managing additional short-term finances and operational costs.

Equipment Financing

Banks fund businesses by providing these loans that are specifically used to purchase equipment needed to run the operational activities. This will lead banks generating more revenue as demand for these loans is consistent.whenever needed and pay it back later.

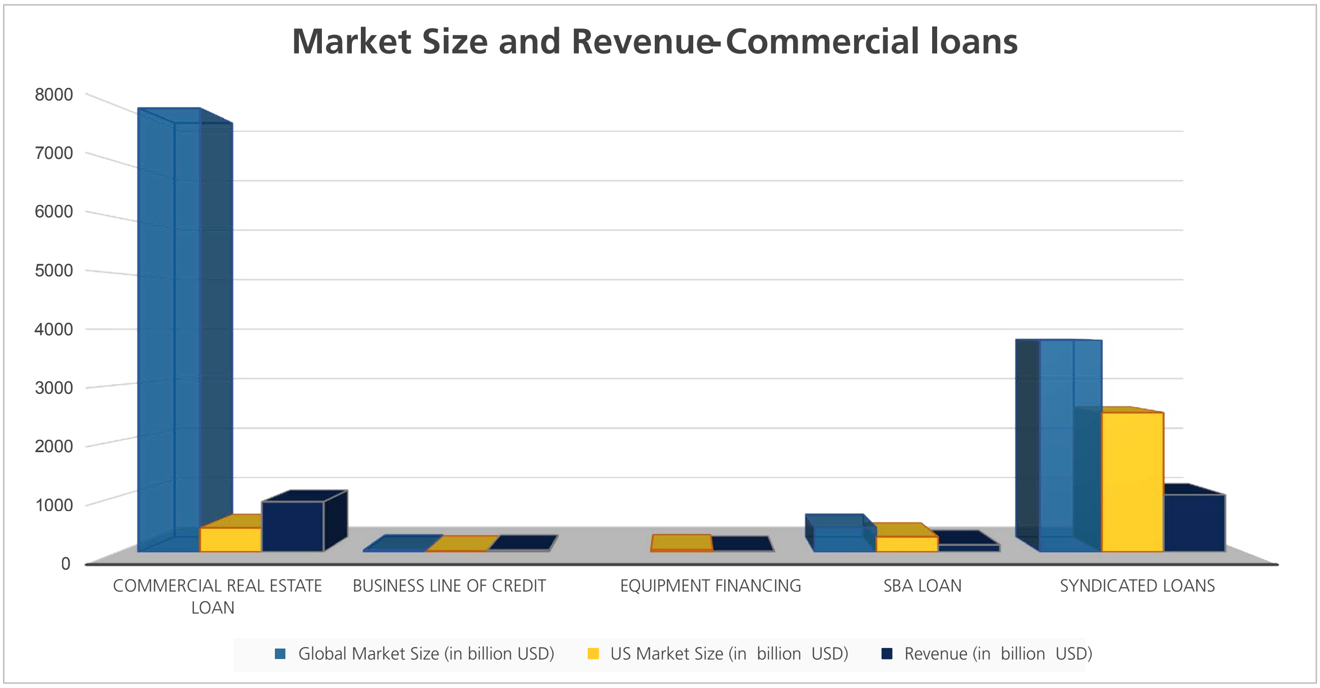
SBA (Small Business Administration) Loan

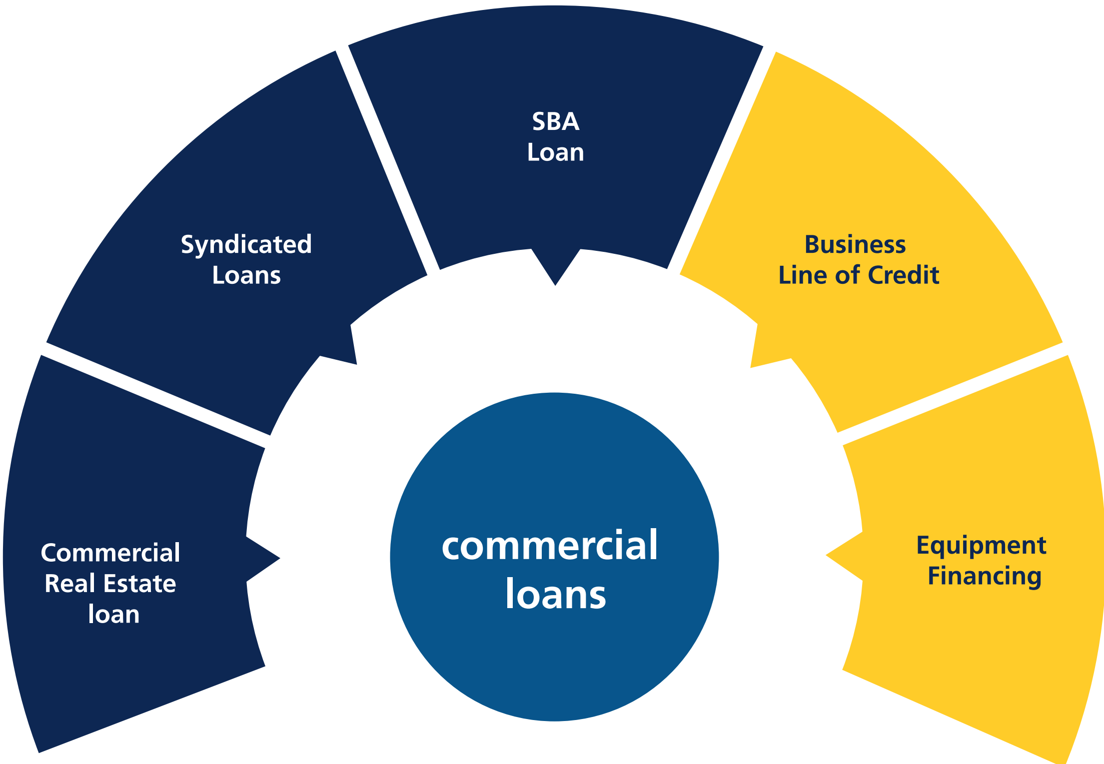
These are loans provided by other parties' intermediary lenders as partners with SBA under certain conditions and eligibility. For instance:

- SBA 7(a): Loans financed for long-term working capital arrangement, real estate, and business debts
- SBA 504 loans: Loans provided to purchase major assets or expand a business
- Micro-loans: Loans provided to startup a business or minor expansion

Syndicated loans

It is a loan provided to a large borrower extended by a group of several lenders and financial institutions as a syndicate. Both parties, bank or non-bank, provide the part of the total amount assigned to them and bear a part of the lending risks





There are other loans as well, but the ones highlighted in green are those that banks and FIs should focus on to increase their profitability, as they generate more revenue.

Gaps in the process of commercial lending

Inefficient gathering of documents

A clear credit policy is needed, as currently, the lack of a consistent credit policy is making it difficult to gather documents efficiently and consistently. Technology should be leveraged to collect and track down documents and fix this problem.

Manual data entry

Manual data entry leads to additional time-consumption, which increases the risk of costly errors. Digitizing the document -gathering and data entry process can solve these issues and provide an easy flow of information through applications.

Underwriting process efficiency

The current underwriting process lacks operational efficiency. This paper-intensive process not only consumes a lot of time but is also bound by the limitations of legacy systems' policies. Automation and AI should be introduced in the process to streamline their operations and introduce an algorithmic underwriting process.

Servicing and collection paperwork

The problem of servicing in commercial lending is mainly extensive paperwork and the time gaps that get created after the loan application, till the collection of funds. There is a lot of paperwork in every process, leading to service delays. Additionally, a business is required outline its business plans and goals to apply for and collect the funds.

There are issues over the collection of funds too. Business must send a closing agent to close the deal and submit any remaining documents. If these documents have anomalies, they are resubmitted by agents, which again go through underwriting and inspection.

Why is it important for banks to prioritize commercial lending?

Higher income on interest

Loans given to businesses are much higher than those given individually. The fundamental income of banks is the interest charged on loans provided to businesses. They charge different interest rates according to a customer's financial history, business, and risk profile. Additionally, the extra benefit of fees and late penalties can boost the income.

Customer loyalty

Banks provide loans to businesses to encourage them to use more of their services. , thus leading to increased brand loyalty. The banking industry depends on creating customer loyalty by providing as many services as they can. For instance, providing additional services over a loan like tax consultancy, financial advisory service and business checking and savings account.

Cumulative inc ome bene fits

When businesses and companies take loans, it directly affects the stability and income of banks. More businesses can grow and develop if they have access to commercial loans. The local economy gets affected too; in case businesses start making profit and generate employment, it will increase the saving account deposits, thus providing resources to banks to lend more.

Inter-bank lending

According to the central bank's guidelines, a bank must maintain a cash reserve ration with the central bank, which is based on the volume deposited. Through inter-bank lending, one bank can give a loan to another on a regular basis to maintain that ratio with the central bank. This ensures the availability of cash reserves for withdrawal, leading to increased customer trust.

How can cloud-based lending be used to tackle challenges?

Cloud-based solutions help in data migration and security, providing an encrypted centralized server system to store data in a better manner, and secure the personal information of clients and businesses.

- Helps in building better customer relationships by eliminating unwanted delays in the loan origination process, while human errors can be corrected by an automated cloud-based software. It also provides positive response times to respond to queries related to data and information.
- Cloud-based computing provides data backup and recovery in case of changing business plans and goals If data is lost, it can be recovered from the cloud.
- Cloud-based technology is scalable and productive. It gives banks the ability to upgrade their products or services, helps in maintenance, and provides IT support, which can help them focus on innovation and efficiency.
- It helps remove the time-consuming, unsustainable legacy framework with thousands of files. Instead, it makes it easier by pre-filing the customer information automatically, and creating the client summary, loan analysis and credit memo.
- Cloud-based computing provides better regulatory compliance with its real-time data classification storage and maintenance capabilities.

Mobile-optimized UI

- Removes accessibility challenges
- Makes customers and bankers work with each other anywhere and anytime on a mobile deviceDigtial

Digtial engagement

- A single platform comprising onboarding, fulfillment, and sales. It automates these services for a seamless end-to-end experience

nCINO

Use of AI and machine learning

- Enhanced credit underwriting
- Aided decision-making
- Analysis by generating insightful reports

Data analysis

- Individual and global risk assessment
- Spreading, auto-decisioning and risk rating features

Q2

End-to-end lending experiences

Robust and sophisticated business banking solutions by offering features and workflows totally oriented to small and micro business users

Providea monitoring and access controls to consumers

- Checks who accesses their data and how often they do so

Real-time solutions

- Reduces the time consumed for the loans and documentation
- Modular solution that manages the whole loan lifecycle efficiently

Provides precision and agility while dealing with repeat buyers

- Stores the consumer data
- Data informed experiences and cross sales

The way forward

Given that the pandemic changed the legacy system of commercial lending to digitization, 2022 will lead to rapid advancements in the commercial lending process and system. Fintechs are partnering with banks and credit unions to provide AI and cloud-based solutions. Clients don't have to go back to manually filling loan applications at different branches. The commercial lending industry is on its way to incorporating automation and machine learning technology. A positive impact can be seen in product and service development by banks. Fintechs are playing a huge part in bridging banks and digital solutions. There is an increase in mobile and online banking, translating to easier end-to-end commercial lending.

This era of commercial lending comes with greater accessibility, better user experience and regulatory compliances, and more profitability. Technological advancements are about to create new growth opportunities for commercial lending in the future. According to report published by Research Dive, the global market size of commercial lending is about to reach an estimated $9,712.8 billion in revenue between 2021 to 2028, with a CAGR of 14.4%. Mergers, partnerships and collaborations, and product development are some widely-used business strategies the current global market players of commercial lending are working on.

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