COVID-19 : Impact and way forward for Corporate Banking

Overview

COVID-19 is having a profound effect on people's lives and the global economy. Corporate and Commercial banks have a central role to play in supporting the global economy during this crisis, and in facilitating a rapid and sustained recovery afterward. On top of regular commercial lending, these banks will play a key role in implementing many of the government's policies to support SMEs and corporates. Numerous strategies can help the banks speed up their response to the crisis.

The paper outlines some of those strategies along with the key role of AI and analytics in helping orchestrate the response.

Corporate banking: Pre-COVID-19

Rising customer expectations, disruptive competitors, new technologies, and increased regulation were some of the pressures forcing corporate banks to reimagine and evolve their business and operating models. Those with investments in digital and data platforms and the right ambition, tools, and partners are well positioned to be the frontrunners. The key focus area for banks was towards aggressive investments to drive efficiency and enhance the client and employee experience, along with the continued momentum towards a new digital future. Many banks that were building on these investments have truly unlocked the power of their data. Some have moved beyond the investments in operational and CRM platforms, reinventing all analog processes to become truly digital players. Market leaders had increasingly implemented AI and predictive analytics solutions, thus, growing their businesses with real-time decisions at higher returns.

Corporate banking: During COVID-19

Corporate banks are now at the epicenter of the global economic storm fueled by COVID-19. In this storm, banks are up against two-fold headwinds: helping their customers, especially the small and midsized ones, stay afloat while shoring up their businesses and scaling capacity. Below are some of the significant challenges currently faced by the banks:

- **Workforce planning:** Banks around the world are experiencing a surge in customer inquiries, and this trend is likely to continue[1]. For e.g., The National Australia Bank, saw the same volume of customer inquiries in just one week that it would normally see in a year. Banks are acting wisely to deploy people and scale their workforce as effectively and safely as possible. Within days, traditional business banking relationship management models were redesigned to slow down the contagion as some clients still rely heavily on the human touch and paper-based processes while struggling to stay ahead of customer expectations and new regulations.

- **Distressed credit decisions:** COVID-driven travel restrictions and social distancing have had an immediate and dramatic impact on the cashflows of many corporates and SMEs. According to JP Morgan's research, half of all small firms hold a cash buffer of less than one month, and 25% of them hold a buffer of less than 13 days[2]. Banks are already flooded with requests for credit and must make urgent and 'distressed' credit decisions. The flow will just increase in the next few months as cash reserves run down, and clients look to banks for lending, deferral requests, financial insights, and solutions.

- **Adjusting Underwriting criteria:** The traditional approach based on largely manual processes & existing underwriting may not work. It can't cope operationally and can't be relied on to deliver best decisions consistently. Many client requests will be triggered by rapidly declining revenues and weak financial outlook, which would fail standard underwriting criteria at the first hurdle. Underwriting rules will, need to be adjusted to enable lending to clients that should return to health after the effects of COVID-19 have dissipated. However, banks may not relax criteria so far that they lend to clients that were unsustainable before the crisis and will never be able to repay.

Overall, workforce planning, near-term bank credit decisions, and how they respond to clients' financing needs will have a huge long-term impact on the economic consequences of the crisis.

Corporate banking: Response strategy to the crisis

In response to the crisis, corporate banks will need to make difficult decisions that trade-off doing what is right for the clients (and minimize reputation risk) as against protecting the bank's balance sheet and shareholder returns. This would be done by structuring and pricing credit exposures for an increased risk. Getting this trade-off right and making the right decisions will be difficult, and, hence, the next few months will be extremely critical for their recovery.

Below are four key strategies that can help speed up the response/recovery for the banks:

1. Help clients to maintain operations
2. Build a Dynamic Credit Decisioning framework
3. Proactively engage with customers
4. Digitize offerings and automate the process

For each of the above four areas, the response/ recovery can spread across two key phases:

Phase I: What should banks do now- Immediately:
Effectively manage the crisis, ensuring continuity of key operations, and proactively meeting clients' immediate needs.

Phase II: What to do next- Over the next three months:
Monitoring business progress and build more valued relationships with clients that can lead to differentiation and long-term growth.

Data- driven strategies, analytics, and AI will play a significant role across all the four key strategic priorities and help in orchestrating an enterprise-level response.

I. Help clients to maintain operations

Corporate banks around the world are seeing unprecedented demand from concerned and troubled small and mid-sized businesses looking to manage their insecure cashflow, as best they can, with extended credit[3]. They are seeking new loans, both organic and through government programs, modifying existing loan payment terms or interest schedules, creating facility or line extensions, and helping address impending credit risk deterioration. In many countries, banks are finding it hard to scale their operations to handle the influx of new credit requests.

To manage such operational impacts, banks need to move quickly to: Creating a command center and building scalable capability.

Creating a command center

Phase I: What to do now:

- Establish a fully integrated command center to coordinate all aspects of crisis response.
- Focus the command center on the areas where the bank is most likely to see volume spikes.
- Setting and operationalizing the credit strategy in response to the crisis.
- Create clear accountability on who is running the command center and empower the leader.
- Define the broader response strategy and clearly articulate it across the organization.

Key considerations for analytics:

- Redeploying resources to aid business in crisis management – build a war room environment to surface relevant, dynamic, and daily insights.
- Short term focused projects (e.g. crisis management metrics) require rapid deployment (1-2 weeks) to be relevant for the current need.

Phase II: What to do next:

- Continuously monitor crisis-related task forces and plan for the long-term sustainable future.

Key considerations for analytics:

- Deploy analytics & AI for workforce and capacity planning to accurately map real-time forecasting of call volumes, Average Handle Time (AHT), staff prioritization, etc.

Building a scalable capability

Phase I: What to do now:

- Stand up scalable processes that enable clients to draw funds from the financial system quickly.
- Address pressure on new credit requests by either designing a new loan origination process or expedite the existing one to enable the processing of high volumes of applications.
- Redirect as much volume as possible towards digital or automated facilities.
- Plan for possible loan modifications, communicate first, and then work through the operational implications, including changes to loan servicing systems.

Key considerations for analytics:

- Improve senior management visibility by helping define & report the underlying data strategies.
- Create insights around the number, value, and segmentation of new loans and modifications, how many new requests are coming in daily, understand bottlenecks and breakdowns.

Phase II: What to do next:

- Understand roll-rate projections beyond the payment deferrals and to better understand the credit risk position of the bank and devise strategies accordingly.
- Partner with ecosystem players to improve the speed and the scalability of loan processing.

Key considerations for analytics:

- Dedicate specialists to model roll-rate projections and accurately predict credit risk position- ideally in real-time, using all internal and external data to guide targeted interventions.
- Existing analytics resources should be redirected to credit management as some banks' success will largely depend on their ability to understand and predict changes in credit risk.

II. Build a dynamic credit decisioning framework

With many banks relaxing credit policy substantially to issue credit faster, tomorrow's problem may become that of higher defaulters and the need for a more intensive collection process. The credit decisioning framework provides a decision logic that recommends treatment strategies based on the client's situation. An important task in the near-term will be to build client eligibility criteria for government-backed schemes and combine it with the bank's existing underwriting criteria. For e.g., under the UK Coronavirus Business Interruption Loan Scheme (CBILS), the bank must determine that the customer is "considered viable in the longer-term" and will be required to underwrite 20% of the loan[4].

> Banks will look to protect themselves and their customers from the likely credit deterioration and, ultimately, defaults in what will be a long-term recovery to pre-crisis levels of demand.

Phase I: What to do now:

- Proactively monitor portfolios to make quick and right credit decisions.
- Quickly adjust to underwriting criteria while minimizing future default rate.

Key considerations for analytics:

- Micro-segment customers based on criteria (industry, exposure, collection priority etc.) to promptly identify clients that have a greater chance of future credit deterioration and cluster them for different advice.
- Build a framework using scenario-planning that includes epidemiological factors (how will the pandemic play out), macro-economic factors (effects on GDP, inflation, sector performance), credit risk factors (default probabilities), while complying with regulatory/compliance requirements.

Phase II: What to do next:

- Continuously track which types of businesses will likely be hardest hit and which are likely to recover faster.
- Create a system to detect early warning signs for default to make better credit decisions or take corrective actions quicker.
- Create an advice portal for stressed businesses in need of immediate answers and solutions such as finding cheaper rent, restructuring employee contracts, and accessing government funds.

Key considerations for analytics:

- Build a credit portfolio management tool powered by AI that processes internal and external data to predict credit deterioration; this can be embedded into different portfolio management functions.
- Automated model management and monitoring frameworks will be needed to enable efficient use of constrained resources.
- An AI based Early Warning System (EWS) both at the sector level and individual company level to identify high-risk default customers. This can include various possible signals such as borrowers' cash flows, distress on revenues, industry type, exposure, etc.
- Cash flow forecasting to provide early warning of upcoming cash flow issues for businesses and increase cross-sell opportunities around short-term loans, deposit products, where excess cashflow is experienced.

III. Proactively engage with customers

Many small and medium enterprises are feeling the heat of supply chains that are sluggish and, at worst, have been disrupted. Most of them are shifting their focus to key survival-critical priorities such as managing cash and debt obligations, ensuring continuity of working capital financing, and keeping their supply chains as stable as possible.

> Corporate banks are in the critical stage now and next to provide support for their customers and proactively engage with them.

Phase I: What to do now:

- Support clients in providing perspectives on how best to manage business and funds.
- Extend assistance to the most-impacted client segments with provisions on reducing their costs or easing their payment obligations through actions such as moratoriums.
- Support customers in restructuring their businesses for e.g., advisory, debt structure, divestments.
- Develop client-specific product offerings factoring in possible discounts and waivers and considering any government-driven financial assistance schemes.

Key considerations for analytics:

- Create data-driven economic scenarios as the COVID-19 pandemic evolves and provide perspectives on how clients can best manage a business in those situations.
- Create client clusters more severely impacted, profile them to create customized strategies.

Phase II: What to do next:

- Offer 'digital' loans to provide quick access to financing.
- Advice on strategies to capitalize on new business possibilities, better manage fixed and variable costs, and optimize tax opportunities.

Key considerations for analytics:

- Create a singular dynamic view on client-specific account receivables and payables to support real-time cash forecasts and enable faster decision making.
- Use insights from various markets, products, and government sources to help structure appropriate product propositions for specific clients.

IV. Digitize offerings and automate processes

Amidst crisis, banks had to move rapidly to digital platforms, with traditional relationship management methods that had to be re-thought, along with the types of branch-based services that many businesses valued. Similarly, to prevent the pandemic from blocking their ability to acquire new customers and sell new products, some banks chose to move quickly towards electronic customer onboarding, online document submission, and e-signature tools. The necessity that today drives small businesses and other corporate customers to use digital services will improve their propensity to engage with banks in this way long after the virus is under control.

Corporate banks that choose to be integrated into a digital ecosystem of platforms and service providers and have invested in digitizing their services will be able to roll out new or complementary offerings rapidly and will engage with their customers more safely.

> In many ways, COVID-19 is forcing corporate banks to accelerate digital transformation initiatives and move customers quickly to digital offerings.

Phase I: What to do now:

- Understand exactly where the impacts will show up more in customer journeys.
- A quick assessment of internal capabilities at-hand to support impacted journeys (including the urgent demand for credit (such as government-backed loans) and understand gaps.
- Use automation to deploy large-scale change in a standardized, low-risk, and efficient way.
- Create and enable a technology steering group to make key decisions and technical resources with access to multiple automation tools and techniques.

Key considerations for analytics:

- Leverage data to define & analyze these impacted areas prioritized based on volume, impact, and customer necessity, urgency for credit and map them to existing digital offerings.
- Marry data and analytics with the digital agenda and help automate current processes.

Phase II: What to do next:

- Partner with organizations that can help deliver rapid digital credit origination at scale.
- Extend the existing retail banking digital offering infrastructure to corporate customers for very basic, self-servicing functions, reducing menial tasks for relationship managers.

Key considerations for analytics:

- Digital transformation through the Analytics Response Centre covering use-cases such as digital relationship management, adoption of digital platforms, and digital identity verification, among others.
- AI/ ML algorithms to flag possible digital fraud cases.

Conclusion

While the full economic impact of the crisis remains to be seen, corporate banks have an opportunity to support both new and existing clients through this difficult time and to emerge as trusted partners in market-leading positions. AI and analytics will be a must in enabling banks to thrive and seize the competitive advantage while navigating through the crisis. It will help them emerge stronger--providing the skills, capacity, support, and advice needed to shorten and reduce the impact of the COVID-19 crisis.

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