Our Credit Lives on Main Street—*Not Wall Street*

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The banking industry, like most of us, is focused on signs of light at the end of the COVID-19 tunnel. With promising vaccines and therapeutics on the horizon, the quick return of the Dow to record territory, the massive federal stimulus, and the regulatory reliefs afforded bankers, it's easy to miss the fact that our credit world is dominated by the economics of Main Street — not Wall Street. And the economic health of Main Street is far more precarious. How will this reality affect our loan portfolios in the coming months? And what steps can we take to stay on top of managing credit risk and ensuring any degree of reasonable loan growth?

Why we must be vigilant

Despite the economic shock of COVID-19, our loan quality indicators are relatively unaltered from prepandemic days. When we consider the interjection of PPP loans and regulatory relief in the form of liberalized provisions regarding extensions, modifications, TDR suspensions and the like, it can be argued that the underlying credit stress in our loans has simply been temporarily masked. Also adding to a false sense of reality is the COVID-high of this year's nonorganic loan growth and deposit liquidity.

We cannot afford to ignore that we are in the midst of a recession and its historic adverse effect on credit quality. Statistically, no more than 50 percent of Americans have a 401(k) plan or are directly invested in the stock market. The other half makes up a good percentage of consumer banking borrowers and, at this point, it's unclear when or if Congressional consensus will extend economic relief to the sector. Additionally, no Wall Street bonds fund small business survival. In short, many of today's bank borrowers are likely just trying to survive — not investing for future growth. That reality alone is a major risk factor in credit 101.

What we must do in the months ahead

First off, bankers need to accept the current challenges, embrace vigilance, and begin taking steps to reduce the uncertainties that lurk within each of our portfolios.

Self-analysis of our portfolios begins with:

- Recognizing the diverse COVID-19 impacts on industries and segmenting our portfolios accordingly
- Realizing that individual hotspots within our portfolios will have markedly different profiles — and require different risk mitigation strategies — than might appear appropriate for the portfolio as a whole
- Tediously identifying stressed borrowers who are being wholly masked by extensions and modifications

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- Aggressively enhancing loan review coverages and effectiveness
- Strategizing on how we replace the temporary loan growth afforded by the likes of the PPP program
- Creating a comprehensive credit risk profile unique to your bank — and describing and defending it before a regulator, sensing a vacuum, does it for you!

Embrace government-guaranteed lending as never before

Recognizing that, for the foreseeable future, the qualified borrower pool for traditional organic loan growth will likely diminish, and as a hedge against the heightened credit-risk environment, there could never be a greater impetus for bankers to take advantage of government-guaranteed lending programs. No matter the fate of any one-off federal relief initiative, one would be safe to predict nothing but an expanding commitment to SBA and USDA loan programs.

The benefits of such a strategy can be:

- Greater organic loan growth under the patronage of an additional underwriter of the risk
- Continued goodwill garnered by the community banking industry during the exemplary delivery of PPP funds
- Profitability from the fees and secondary-market sales afforded by SBA/USDA lending programs

While some banks choose to strategically sell the guaranteed portion of these loans, we have to remember, *these borrowers, by definition, are not prime credit quality.* Detaching the guaranties may add to your credit risk.

All of this is to say, regardless of a (hopefully) near-term conquest of COVID-19 and the deceptively benign appearance of current loan portfolios, most risk experts know that the so-called credit tails of economic shocks are ALWAYS longer than the events — and are often problematic. This can be especially true for community bankers who need to understand the true nature of their borrowers and who need to alter lending strategies going forward in order to both serve the borrowers and quantify their embedded risks.

IntelliCredit can help your bank manage these 2021 credit risk challenges with the most practical, efficient and affordable tools available. Please contact us to learn more.

For more information on IntelliCredit, visit **www.intellicredit.com** or email **info@intellicredit.com**.