Observations & Insights

from

Jeff Judy & Associates

Business Lending: The Secret Credit Union Advantage

Putting the "Business" Back in "Small Business"

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While some credit unions are involved in business loans of substantial size, the very nature of member business lending is perfectly suited to helping small businesses grow and prosper. Even better, this is one market in business lending where credit unions can enjoy a significant advantage over their banking rivals.

It is no secret that as more credit unions enter the business lending arena, they are playing catch up with banks. Banks have long experience with commercial credit.

But that very experience, especially at the biggest banks, sometimes leads to mistakes that open the door for other providers of small business loans.

Taking the "Business" Out of "Small Business"

One of the strongest trends in commercial credit of the last decade or two has been the increasing automation of credit analysis for small businesses. The biggest banks rely heavily on *credit scoring*, which largely means using sophisticated software to analyze and manage small business loans much as if they were typical consumer loans. And this practice is steadily expanding among community banks.

There's nothing wrong with automated analysis per se. But it often seems to affect how borrowers are viewed and treated. Unfortunately for many small business owners — but fortunately for credit unions — as the analysis process has shifted in this direction, many banks seem to have forgotten how much courage and hard work it takes to run a small business. They have made mistakes that credit unions can turn to their advantage:

- **Understanding vs. Input:** Whether at a bank or a credit union, financial statements and other business data are crucial to sound decisions and well-structured credits. But that business owner sitting across the desk from you quickly gets a feel for whether you are asking questions and collecting information to help you understand how their business works (and is working), or whether you are just "filling input boxes". Frankly, this "data-entry" attitude, when small business owners apply for credit, can get under an owner's skin very quickly. Attitude counts!
- **Member Service vs. Market Fad**: A big bank, especially, will periodically launch a "small business initiative" to "tap this important market". These programs come and go, and when they come, they start with the product (a small business credit) and look for the need. Compare that with how credit unions are expanding their services to members by adding business lending. Starting with the member instead of with the product is a huge advantage.
- **Relationship vs. Process:** Some doctors deal with you as a "case" or a "condition" or "disease", not as a *patient*. They may get the job done, they may cure you, but you won't enjoy the process very much. And there are plenty of

banks who can “get the job done” in making a business loan. But credit unions have the experience to make sure the member not only receives the appropriate credit, but feels respected and valued throughout the process. They can put respect for the “business” back in the expression, “small business”.

Where Credit Unions Could Do Better

The relationship focus that is characteristic of credit unions is not without its hazards. It is easy to get a bit smug about the quality of the relationships credit unions enjoy with their members, to the extent that it hides problems that need to be addressed to protect the combined assets of *all* the members from the higher risks that come with business lending.

In other words, there are still some lessons the banks could teach credit unions. Among the most important are these two:

- **Applying Analyses:** when you get the report from a financial statement or credit analysis, that’s not “the answer”. These reports point to opportunities for some great questions and good advice for your business borrower. *Make sure your staff have sufficient analytical knowledge to take advantage of these opportunities*. Just because a particular employee does not *do* the actual borrower analysis doesn’t mean that there are not huge benefits to being able to *interpret and apply* the analysis.
- **Member Loyalty vs. Business Reality:** while banks often swing too far in the direction of reducing a credit relationship to a set of numbers, sometimes credit unions swing too far in the other direction. Business loans that are not repaid can seriously damage the health of your credit union. Credit staff working in any aspect of member business lending need to be able to objectively assess the business even in the face of a longstanding member relationship.

Credit unions are in a unique position to thrive in lending to small businesses. The secret is to accept the lessons banks, with their long history in commercial lending, can teach, while avoiding the mistakes that many big banks make in their small business relationships.

Jeff Judy's booming voice and unique instructional style have been enjoyed in classrooms and auditoriums across the globe. Jeff is in demand as a trainer for individual financial services institutions as well as regional and national trade associations. His practical, down-to-earth approach consistently wins him high ratings from participants in his seminars and workshops. Jeff also educates audiences through his frequent interviews and articles in trade journals and more general financial media, as well as through his own biweekly electronic newsletter, Jeff's Thoughts. For information about Jeff's work with credit unions, visit www.JeffJudy.com/creditunions.html.

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