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Readiness Strategies for a Downward Spiral of Delinquencies

By: Anthony Lamm
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All of us in the finance industry know that delinquencies are at an all time low. As a matter of fact, they are at a historic low. This doesn't mean however there are not steps in your asset recovery, managed assets or collections departments to take. I recently talked to one bank official who stated that their company is adding an individual to their workout department whose sole responsibility will be to identify and monitor weaker accounts, even if the payments are current or just a little slow.

If your organization has an individual with capacity right now (because delinquencies are low), I would recommend this approach as one method of preparation for a turndown in the economy and an increase in delinquencies. Another approach is to identify industries or areas of business that historically are first to experience difficulty in managing cash flow and paying their loans or leases because they lost a major customer causing a decline in sales, experiencing technology changes, or were not proactive in anticipating the effects of external forces such as weak consumer purchasing power or increases in commodities and fuel.

Trucking and businesses that support transportation companies are usually some of the first businesses to show cracks when the economy weakens. This typically occurs because consumer-spending power has weakened or insurance and gas prices have increased. High-end restaurants, considered a luxury for most people, also become an area of business that experiences weaker demand.

Therefore, working capital loans or leases for restaurants and their equipment could be vulnerable in a weakened economy. Identifying the concentrations of businesses subject to a slower economy and securing recent financial statements and site visits are two ways to develop a picture of whether these accounts are weakening.

Signs of Trouble

In my experience, accounts that pay over 20-30 days usually have a problem, which may be covered up by owner investment or high credit card usage. Examining accounts receivables and accounts payables to determine if there are any noticeable trends is a way to detect an underlying susceptibility for short-term and longer-term problems. Meeting with these borrowers and discussing the cash flow of their businesses and considering a forbearance or restructuring of the loan or lease could be a good way to make the customer's payment more manageable. At the same time, recommending that these particular clients seek out their other vendors in an effort to restructure payments can relieve the overall burdens on cash flow that a business with weakened receivables needs. Partnering with your borrower at a very early stage with a view in mind to assist them by recommending changes is advantageous to both parties because the cost and return of liquidating most companies results in a substantial loss.

Shadowing Accounts

Since change can only happen in an enterprise from top to down, management must embrace a philosophy that effective portfolio management includes all functional areas within any lending organization. For example, if there is no procedure to cross examine accounts by the line officers and then sharing information with the managed assets departments, taking action to restructure or work out emerging problem accounts will be delayed. Time is the enemy of all collections and therefore introducing a "shadowing" procedure alleviates any time gaps in responding to an account that is going or may become delinquent. Shadowing accounts that line officers share with workout personnel maximizes the skill set of the individuals hired to manage an account that has difficulties, which in turn will bring the financial institution the best result in preventing losses.

It is clear that there are tremendous opportunities to get prepared for the next downward cycle in the economy if your organization highlights the portfolio in its entirety and brings the right individuals to respond to a given situation. It requires a determination for early evaluation of your accounts in segments and concentrations and near 30-day accounts. The philosophy that is "forewarned is forearmed" adopted by any financing company will increase alertness which results in detection, identification and ultimately evaluation and counseling to reach the best solution. This makes everyone a winner!
