HALCYON

POSITIONING YOUR MORTGAGE LENDING FOR SUSTAINABLE GROWTH

HALCYON

INTRODUCTION

Today, as the home finance industry continues to capture as much of the historic loan volume as it can, company growth is all about capacity. There are many mortgage lenders operating in the space today that simply can't handle all of the work they have now[1].

Fannie Mae has predicted that the 30-year Fixed-Rate Mortgage will stay between 2.8% and 2.9% for the rest of the year[2]. But that isn't happening. More recently, Kiplinger reported that "The rise in the 10-year [Treasury] rate will also push up[1] mortgage rates, from 3.1% to 3.5% by the end of the year."

This comes as no surprise. The mortgage business is famously cyclical. Even with over a decade of artificially low interest rates thanks to the Fed's efforts to keep our economy humming along, it's just a matter of time before rates rise, refinance business falls off and housing inventory shortages[3] at the low end of the market shut down the first time homebuyer business.

Eventually, mortgage lenders are going to have to re-learn how to prospect and acquire mortgage leads. That won't mean opening their wallets to purchase leads from the big real estate search engines. Competition for internet leads, which were never considered the highest quality new business opportunities, will be intense as loan volumes fall off.

Where will lenders go to find new business?

In this paper, we will describe a new technology that is making it possible for mortgage lenders to increase revenues now, when times are very good, and secure a viable source of mortgage leads they'll need to grow as we move through the industry's cycle by increasing the value they offer consumers.

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[1] 2021 predictions for mortgage lending . (2020). https://www.nationalmortgagenews.com/list/2021-predictions-for-mortgage-lending

[2] Payne, David. Interest Rates: March 18, 2021. Kipliners. (2021). https://www.kiplinger.com/economic-forecasts/interest-rates

[3] How 2020 broke the housing market: So many homes are selling that we could run out of new houses in months. (2021). https://www.businessinsider.com/how-2020-broke-the-housing-market-inventory-could-run-out-2020-9#:~:text=There%20are%2020%25%20fewer%20houses,dip%20down%20to%202.5%20months.

THE PROBLEM THE INDUSTRY HAS CREATED FOR ITSELF

Sales leads are a means to an end and in the mortgage business, the end goal is company growth. Like every other business in every other industry, the mandate is to grow or die. Companies that don't achieve the former always succumb to the latter.

Mortgage company growth is generally delivered by marketing, sales, strategic business referral partnerships, and M&A. All of these, with the possible exception of the last one, require basic sales skills and a thorough understanding of lead prospecting. Unfortunately, that's not a well developed skill in our industry right now[4], which may be why we have so many sales trainers working here.

Because mortgage interest rates have been so low for so long[5], most of the loan officers working in the field today have had years of easy refinance business. Thus, the people working in the industry today have never been subject to the stress that creates well-trained salespeople. We have become an industry of order takers.

Furthermore, because mortgage customers don't come back for a new mortgage loan very often, building loyalty programs has been a non-starter. Without a system to allow prospective borrowers to alert their lender of their need for a new loan, lenders are forced to guess when consumers are in the buy zone.

Today, that means hoping a real estate agent will call on them to finance a deal or buying leads from someone on the internet who is watching to see when a consumer is searching online for mortgage rates or real estate.

Catching a consumer in the buy zone is very difficult and so most lenders use "spray and pray" marketing methods or just buy as many leads as they can afford.

[4] Selling mortgages is not rocket science - The secret of role-playing. (2014). https://nationalmortgageprofessional.com/news/40105/selling-mortgages-not-rocket-science-secret-role-playing

[5] 30-Year Fixed-Rate Mortgages Since 1971 - Freddie Mac. (2021). http://www.freddiemac.com/pmms/pmms30.html

While business referral partnerships have generally been the least expensive method of getting new business, this has been problematic for lenders because finding, building and maintaining those relationships is difficult and time consuming.

Whereas real estate salesperson relationships were the bedrock of a lender's business 40 years ago, today they are far less effective.

That's because the Realtor isn't just connected to the loan officers who live in their neighborhood, but also all of their social media contacts as well. Sharing business among all of those connections means fewer leads for any individual lender.

> "Business referral partnerships have generally been the least expensive method of getting new business"

The problem the mortgage industry has created for itself today is that it has existed for so long on easy refinance business that it has all but lost the critical skills required to source, cultivate and convert mortgage leads.

This has happened because company growth has not depended on increasing sales, but rather on increasing capacity.

We saw this very recently in the volume runup coinciding with the global pandemic, when explosive loan growth effectively doubled the cost to hire experienced loan underwriters and processors and sent many lenders offshore in search of business process outsourcing.

The only existing strategy that provides both growth and additional capacity is M&A.

M&A, YESTERDAY'S GROWTH ENGINE

2020 was the second-busiest year since the financial crisis for deals involving banks, financial technology companies, insurers and asset managers. The $507 billion in financial services transactions announced last year was topped only by 2019, according to Bloomberg.[6]

Unfortunately, growth through acquisition is not organic and while it ensures that the size of the company increases, the critical metric, closed loan per full-time employee, doesn't increase. This renders growth by merger or acquisition unsustainable because after the boom part of the cycle ends, the company could collapse under its own weight.

When one lender acquires another, the staff count in every department increases. A lender now has more operations staff than before but because the two companies are almost never working on the same tech stack or operating by the same playbook, the new company does not achieve 100% efficiency. The new company rarely performs as well as part of the new organization as it did when it was on its own.

This is particularly troublesome in the sales department, where the lender now has twice as many order takers as it did before. Both teams are subject to the pareto principle, so 20% of the resulting sales force will generate the lion's share of the company's revenue.

[6] Bloomberg - Are you a robot?. (2021). https://www.bloomberg.com/news/articles/2020-12-03/boom-year-for-financial-services-m-a-still-has-more-to-come

Additionally, from a mortgage lead perspective, growth by acquisition is the most expensive way to generate new business. It costs a great deal of money to find the prospective company, perform due diligence, negotiate a deal and then complete the acquisition. Even then, many of these transactions don't work out and don't ultimately serve to grow the business.

Some would argue that you're not actually even acquiring new business when you buy another lender, but instead just acquiring another operation that also needs to source leads. The acquirer gets bigger, it's capacity to process business increases, but the transaction does little if anything for the operation's ability to source new business.

IT'S TIME FOR A BETTER SOLUTION FOR SOURCING NEW MORTGAGE BUSINESS

We're caught in a loop, working in an industry that hasn't unlocked customer loyalty, is no longer expert at sourcing new business, and is therefore dependent upon low interest rates to bring in new business.

Unfortunately, interest rates have nowhere to go but up. Lenders must find a better solution to growth or when refinances fall away, so will their businesses. Some experts predict this will happen by year's end.[7]

But there is a solution and diversified financial services companies are already adept at using it. Traditional banks (depositories) have long known that the key to a successful banking relationship hinges on share of wallet.[8] The more bank products and services the consumer buys, the more tightly bound that consumer is to the institution.

That's why cross-selling is an important competitive strategy for these institutions. Mortgage lenders also need to find a way to diversify their offerings and gain more share of wallet.

To achieve this, some lenders are forming alliances with professionals who serve prospective borrowers every year, like tax preparation professionals. In fact, this could be the very best move a lender could make in order to source a continuous supply of affordable mortgage leads.

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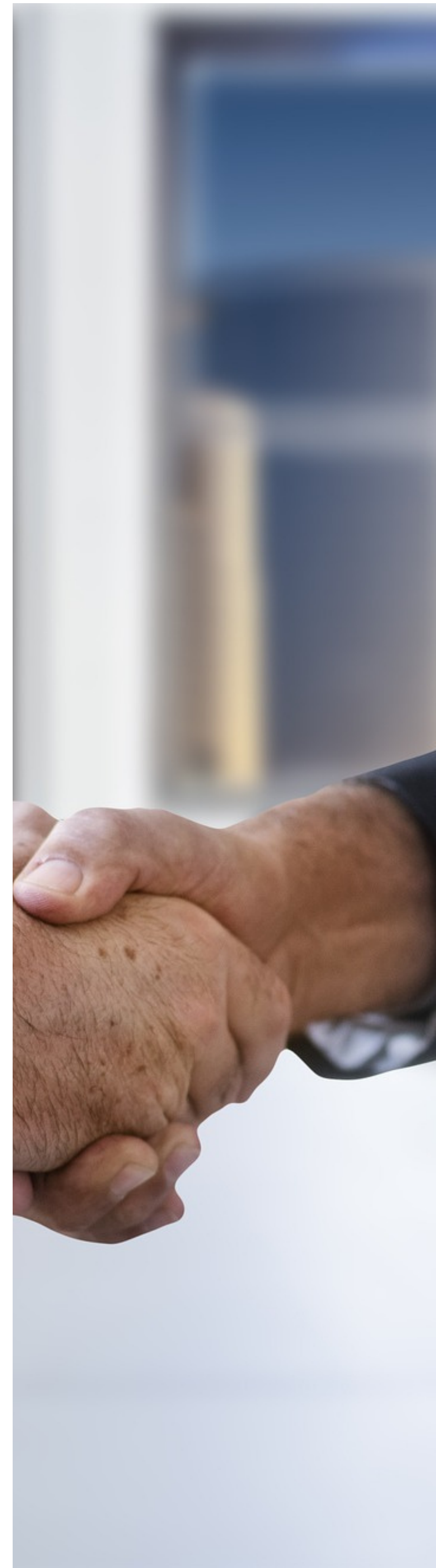
[7] Royal, J. (2021). Bankrate's Interest Rate Forecast For 2021 | Bankrate. https://www.bankrate.com/finance/interest-rates-forecast/

[8] What Share of Wallet (SOW) Tells Us. (2021). https://www.investopedia.com/terms/s/share-of-wallet.asp#:~:text=Benefits%20from%20increasing%20a%20client's,customer%20satisfaction%2C%20and%20brand%20loyalty.



Each year consumers complete their annual tax returns, providing a plethora of information about their financial position. While this information is an essential work input for the CPA completing the consumer's tax return, it is much more to a lender. This data unlocks the prospective borrowers' financial situation and opens the door to the lender adding value by suggesting new home financing options that would be of benefit.

Benefits to the consumer….

By seeing this information when the consumer's taxes are filed, the lender will know if the borrower could benefit from a new loan even before the consumer knows. This puts the lender in a position to be a true advisor, helping to educate and offer options that would improve the borrowers' financial position. Such advice builds loyalty, as borrowers realize that the lender is there to offer assistance, not just try to sell something. This type of borrower loyalty is an elusive goal that the mortgage industry has been trying to crack for years.

Of course, the reason more lenders don't do this today is that forming relationships with tax preparers and CPAs was very difficult in the past, to say nothing of maintaining them. The seasonal work means CPAs are often out of the office and unreachable except for tax season, when they are too busy to be bothered.

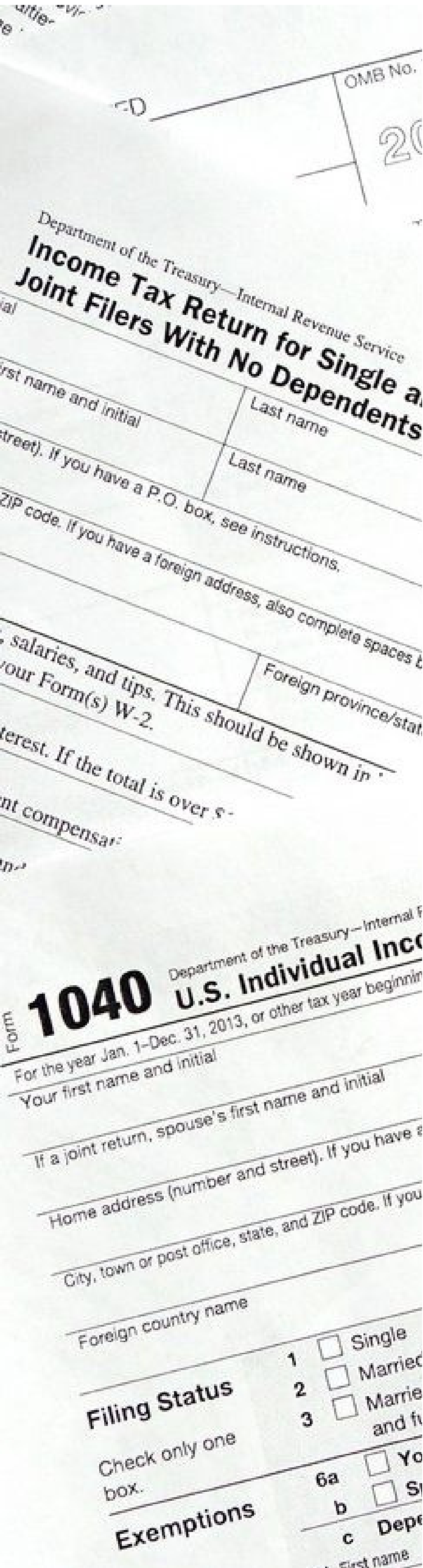
Still, having these relationships will pay huge dividends to lenders. The question is, how can this best be accomplished?

A NEW PARTNERSHIP THAT SOLVES THE LENDER'S LEAD SOURCING DILEMMA

Given the situation, it might appear that lenders are hopelessly dependent upon low interest rates to maintain their businesses and since they lack the skills required to source their own mortgage leads, and that many will fail when rates begin to rise.

That's not necessarily true.

Lenders need an effortless way to build new business referral contacts, but instead of tossing their client relationships over the fence to a partner or begging for a piece of the action, the lender needs to actually own the relationship by offering the service.



Tax accounting is a perfect solution for this as every borrower needs it every year, the tax return data provides accurate mortgage lead information and there is now powerful software available to make tax reporting easier.

The right solution would use technology to handle most of the work and then a national network of CPAs to sign off on the paperwork once completed, so the lender would never have to give up the client relationship but add no new risk or effort to the lending operation.

While this may sound like a dream, Halcyon has launched a crowdsourced platform built on software used by tax professionals on millions of individual consumer returns that now allows mortgage lenders to easily offer tax preparation services to their borrowers and profit from it by easily partnering with professional tax preparers.

The service is easy and convenient for consumers, instantly connects lenders to thousands of credentialed tax preparers and provides the perfect reason for lenders to stay in touch with borrowers, year after year.

Here's how it works.

Mortgage Lenders make the Halcyon platform available to their mortgage customers on their existing websites. This borrower-facing site makes it easy for consumers to come to the lender's website and find the expert tax preparation support they need. The lender needs to do nothing during this process.

The platform itself offers industry-leading Optical Character Recognition (OCR) technology that is already in use by some of the mortgage industry's largest investors and by thousands of tax preparers across the country. Allowing the consumer to start the process easily, uploading their documentation into the platform.

On the back end, thousands of licensed CPAs from around the country connect to the Halcyon platform to find new clients. Consumers enjoy the convenience of an instant connection to a qualified tax-preparation professional via chat or video call to answer questions and get advice that allows them to minimize tax liabilities without having to book appointments and then wait months to get time with a CPA still working in the brick-and-mortar world.

Because the Halcyon platform does much of the heavy lifting, CPAs are able to review all the documents and sign off on them in a fraction of the time it took previously. This allows CPAs to focus on providing valuable advice to consumers. In a world where the tax code seems to get more complex each year, this is a fantastic benefit to offer the lender's past customers.

QUANTIFYING THE BENEFITS

If lenders suddenly had a way to build lasting relationships with their borrowers that would:

- Give them a reason to stay in touch with the borrower every year;
- Give them access to all of the borrower's financial information;
- Give them fee income for every tax transaction that occurs;
- Give them immediate access to most of the information required to underwrite a loan;

it would change the game and make customer loyalty finally an achievable goal for the home finance industry. Suddenly, the mortgage lender/borrower relationship wouldn't just be transactional. It would become an ongoing partnership.

While perhaps 10% of a borrower's past customers will traditionally be ready for a new mortgage in any given year, 100% will be ready to file an annual tax return. Self-employed borrowers will require quarterly assistance.

In truth, many more borrowers could benefit from a new loan, but they don't know it and the CPAs who traditionally file their paperwork don't know it. But with Halcyon, the lender will know it and be in the perfect position to grow their business by adding this valuable service for the existing customers.

Unlike the mortgage business, tax preparation is a non-cyclical business that is largely the same from year to year. CPAs have access to the consumer financial information that makes it possible for the lender to determine when the borrower is in need of a new loan.

Instead of sitting down to find out who a borrower is and what they need after they have already selected a new home to buy, the lender now really knows their customers and can go to them when they see a new opportunity for the borrower to benefit from a new loan.

"Move From A Transactional Relationship to an Ongoing Partnership"

THE NEW ECONOMICS OF MORTGAGE LEAD GENERATION

Lenders who are exploring this alternative lead generation strategy are finding it much more affordable than any other method of acquiring mortgage leads.

Talk to any Chief Marketing Officer with experience in this business and they'll tell you that the price of a mortgage lead varies wildly, from about $15 for an internet lead up to as much as $500 for a lead cultivated by a marketing company.

Generally, leads for low margin, agency loan products tend to be less expensive, but often those same leads are sold to many lenders. It's a race to get to the borrower first and the return isn't very high.

Higher margin loan products allow lenders to spend more to acquire leads. Once acquired, it's all about conversion. And that's another problem. Because borrowers are completing loan applications with more than one lender,[9] the conversation rate on these leads is lower.

This is a risk lenders face even after the application is in the pipeline, with about 50% of the loans being processed failing to close because the borrower ultimately didn't qualify, the borrower chose to go with another lender who was either further along in the process or offered the borrower a lower rate or better terms.

Ultimately, the industry expects to convert between 18%-20% of the leads lenders buy, depending upon the source of the lead and the expertise of the lender's sales team.

So, what does this do to the ultimate marketing cost per loan closed? It varies by lender, but a good rule of thumb is to expect lenders to spend upwards of $2,500 on marketing for every loan they close. This is reported differently by some lenders because they add in the cost of their loan officers in this calculation, which pushes this price up.

In MBA surveys, the sales and marketing expense generally accounts for 58% of the total cost to close a mortgage loan.[10] What does it cost to close a loan? Some credit unions can do it for less than $5,000 per loan. Respondents to the MBA's surveys have reported costs almost twice as much.

But what if the lender didn't have to spend any of this money to acquire a lead? What if the lender was already doing business with the prospect?

Now, the cost to acquire is reduced to the cost of an email or phone call to an existing customer to cross sell them on an additional product.

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[9] Berry, C. (2019). Can you apply for a mortgage with two lenders at once? | Mortgage Rates, Mortgage News and Strategy : The Mortgage Reports. https://themortgagereports.com/26611/can-you-apply-for-a-mortgage-with-two-lenders-at-once

[10] MBA Chart of the Week: Components of Cost to Originate in Retail Production Channel | Mortgage Bankers Association . (2021). https://www.mba.org/publications/insights/archive/mba-insights-archive/2019/mba-chart-of-the-week-components-of-cost-to-originate-in-retail-production-channel

This effectively saves the lender between $500 (the cost of a good lead in today's market) and 58% of the total cost of originating the loan, which could be thousands of dollars per loan. If you are a mid-size lender who is originating 1000 loans per year, saving $2,000 per loan would mean $2,000,000 in savings.

READY TO FIND OUT MORE?

Are you ready to add a new dimension to your bank, credit union or mortgage bank? Find out how easy it is to own your customer relationships like never before and to finally say good-bye to buying mortgage leads that don't convert.

Find out more by visiting us online at https://www.halcyonsw.com/about-halcyon.