Deposits and Data
By Charles B. Wendel

In the past few days, CNBC reported on the huge increase in deposits sitting in banks and Reuters printed a UK-focused story on the need for banks to rethink their approach to data analytics. Different topics, but each raises issues and challenges for banks recovering from Covid-19.

Regarding deposits, CNBC reported: "A record $2 trillion surge in cash has hit the deposit accounts of U.S. banks since the coronavirus first struck the U.S. in January, according to FDIC data." The article went on to clarify: "Deposit gains were concentrated at the very top of the industry: JPMorgan Chase, Bank of America and Citigroup grew much faster than smaller firms in the first quarter, according to company data…"More than two-thirds of the gains went to the 25 biggest institutions, according to the FDIC." Their takeaway was that deposits rates would drop. Of course.

That may be great for the biggest banks, but it means the other 5,000 banks have to fight over scraps. It provides yet another illustration of the increasing, not decreasing, market power of the biggest banks, however, much of those dollars may have come from companies drawing down their lines in anticipation of tougher times ahead. Some banks are in the mode of circling their wagons to reduce loan losses. Most banks lack and still need a deposit strategy, in particular for the long term.

The article goes to quote an industry observer, "But banks, which will be cautious lending money in the midst of a recession, are running out of uses for their growing mountain of cash." If that is the case, these banks need to put their dollars where their PR mouths are and take on an active role in helping lower income consumers and communities. Many banks seem happy to spread some $ here or there to quiet complaints but fail to do more to serve minorities or small businesses. Will they take meaningful action, that is provide "risk assets" to those who need them? PPP and SBA guaranteed loans only go so far.

No matter the results of the next election, banks should expect increased demands on them to demonstrate how they are helping the neediest rather than sucking dollars from the poorest with overdraft fees and high credit card interest rates. Providing advice and counsel whether in person (too expensive), using the phone or apps (best option) should become a priority. Banks should audit themselves for their effectiveness at being positive forces in the community before unfriendly outsiders do.

The second article, this one from Reuters is titled, "Model Misbehaviour: Coronavirus Confounds Bank Risk Systems." It begins, "The novel coronavirus has upended how banks manage lending risk, with decades of data rendered moot by a once-in-a-lifetime mix of global economic shutdowns, unprecedented government support and an uncertain path to recovery." It goes on to quote an HSBC exec: "The one thing that I have learned in 34 years in banking is that credit risk models and scorecards will work really, really well except when there is a significant abnormal shock." Well, guess what?

The data has not been rendered moot, but the ability to rely on modeling for decision making has. The article, being British, uses a pub as an example of modeling inadequacies: "[Consider] a British pub with a beer garden. It will likely be able to serve many more customers than one with only indoor space under social distancing rules - a brighter prospect unlikely to be captured by existing models." No current modeling would likely pick this us, but a person would. A banker who knew the client and how the company operated could provide immediate insights and help the bank to "pivot" to the new world.

The article correctly states, "The uncertainty created by the new environment may also offer good lending opportunities which banks could miss if traditional models flag such clients as too risky." Of course, but what about leveraging a team of expert lenders who know the regional issues and individual clients. The need reminds me of a phrase used during a period of demonstrations decades ago, "People Power." Your people.

"The back history here is not going to be a predictor of the future - trying to model coming out of a virus is not easy," said a StanChart executive. He's right. Maybe banks should deemphasize their models for a while and rely on human experts.

We have been working virtually with clients on these and related issues. Given continued uncertainty and the need for flexibility, all FIs need to focus on the future as they manage current portfolios and changing customer expectations.