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PHH Mortgage

PHH

Private Label Solutions

www.PHHMortgageSolutions.com

Mortgage Outsourcing: Maintaining Brand Integrity while Reducing Cost & Risk *PHH Mortgage Leads the Way*

Six top financial institutions share valuable insights on the benefits of leveraging PHH Mortgage's industry-leading expertise to grow their mortgage business.



Sumit Sahni-Moderator
Vice President and Director
The Boston Consulting Group

Why did you outsource and how long have you been doing it? Is mortgage still an important part of your business?

Chan Peterson: We started working with PHH Mortgage about six years ago to outsource our mortgage business. During that time we had some gaps in the mortgage business, and it just made a lot of sense for us to outsource it. And because we're doing it from a relationship standpoint, we rely on the branches to source the product. There's increased customer value in offering the product and more often than not, it's an existing customer that we're providing the mortgage for, so when you

talk about the cross sell or the cross buying experience, it's an existing customer coming to us and we're able to take care of the need. We do have a group of about 12-14 outside loan officers spread out through the markets and frankly, more of our production comes from them than the branches. And there's a pretty good level of connection between those outside loan officers and the branches.

Larry Washington: We've been at it for about five years, outsourcing everything to PHH. We believe mortgage is an integral part of our financial business.

Steve Hood: We actually had our own mortgage division up until the late 90's and decided at that point to go to an outsourcing model. It wasn't a core business unit for us. Initially we outsourced with another provider, but since a good number of these mortgages are to existing customers, excellent service and support were critical. In outsourcing, we partnered with PHH Mortgage and that outsourcing piece has worked very well for us. The key component for us in the South Florida area is the relationship piece. There was a time when mortgages were a commodity and now they're becoming more of a relationship staple.

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Steve Hood, BankAtlantic

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Brad Smith, UMB Bank

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Brad Smith: We have been working with PHH as our outsourcing solution for mortgage services for the past two years. The benefits of utilizing PHH are driven not only by the economics of the mortgage loan itself but by additional products generated from this core customer relationship. We view the mortgage loan of a customer as one of the key drivers in the client’s relationship with their financial provider.

Eric Dawes: We’re in the Washington/Baltimore/Virginia corridor and real estate is huge in those areas. We believe we can take a very proactive approach to mortgage and grow this business dramatically.

Richard Musci: Basically our mortgage business was built around the outsource model. We’ve been working with PHH Mortgage for about three years and their ability to deliver quality service under our brand has been key to our continued success.

Talk about how you repositioned the mortgage product in your organization to expand customer relationships.

Eric Dawes: The answer is really twofold. There are certain parts of the mortgage business in which I’m going to buy the assets and actually retain them. We have a division that focuses on community investment and provides mortgages to first-time homebuyers. We also have what I’ll call the private banking group (our professional executive group). The upscale and the traditional mortgage underwriting is not always acceptable to those individuals, and we are going to have PHH write or underwrite them both based on our specifications. But we will actually keep the loans in our portfolio.

Steve Hood: We’ve worked with PHH Mortgage to develop a method by which they transmit an approved origination to us after the application has been approved. And we get all the information we need on the client. The experience is very fluid and service-focused. We began the follow up process with proactive customer contacts in mid-January. And we

re-routed some closings to our local stores and now, we’re getting those customers into the stores for relationship building opportunities. The service and the customer experience are much better when customers go to our local store to close their loan because they can get questions answered. And that’s been a positive experience for the customers. We’re doing actual road shows where we’re going out and talking to every store associate about this program, and the mortgage referral and the potential relationship building opportunity that goes with it.

Larry Washington: We track the success of the mortgage program religiously. We’re not necessarily in the traditional banking business, but we see that the financial advisors are now advising on both sides of the balance sheet. They find that this is an easy way to open the conversation with customers and prospects.

How does having an outsourcing business model help you execute a more offensive strategy versus if you had your own in house mortgage operations?

Chan Peterson: The obvious one for us is it allows us to put capital in places that matter more to the bank, and that is a key benefit to outsourcing the mortgage operation.

Brad Smith: Right, exactly.

Richard Musci: It was particularly important for Schwab because we have existing clients in all 50 states. So, to build a national mortgage lending and servicing capacity from scratch is very resource intensive. Most people talk about entering the mortgage business and they’re talking about six states. We’re trying to provide great products and services to clients in all fifty states.

Steve Hood: Economy-wise, it didn’t make sense for us to get into the mortgage business. The capital investment is too significant for a business line that does not represent a core competency. In outsourcing, service delivery

was a key consideration. And PHH has a passion for quality service. When PHH experiences a service drop, they pick it up, inform you that they dropped it and then do whatever it takes to ensure a positive customer experience. I’ve been very impressed with that. Additionally, our service philosophies are very similar; it’s been a good relationship.

Brad Smith: One of our key motivations for outsourcing is the opportunity to capitalize on the technology and the back room efficiencies of a “best in class” provider like PHH while at the same time staying involved in the customer’s transaction. Our business is all about customer service and relationship management. PHH’s loan process allows us to have an active and visible role in the loan application. Ultimately we want to make sure the customer’s experience is one that exemplifies the standards of UMB Bank. Our customers value this participation.

What kind of insights or lessons learned can you share around going through the mortgage outsourcing process, and what are the key rationale and benefits of making the decision to outsource? What insights can you share around the process?

Steve Hood: Several key benefits of outsourcing are the opportunity for efficient capital allocation into core competencies. Additionally, we talked about our desire for core relationship growth. Leveraging partners to help facilitate that growth and allowing our customer service representatives to remain focused on growing the deposit aspect of the business create value. Meanwhile, we leverage PHH to grow the mortgage aspect and utilize that partnership to deepen relationships. And, we must remain active in the relationship process to make sure we get the relationship base. Those are the key drivers. That’s what’s going to help us drive this success.

Larry Washington: You want something simple, seamless, and comprehensive, and that’s the solution that PHH Mortgage offers. They do the

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front end, the secondary marketing piece, and the servicing piece. And they’re not going to compete with you so they’re not going to take your customer. They’re going to do everything from beginning to end for you.

Chan Peterson: Nobody’s willing to give up the brand.

Larry Washington: That was a big consideration for us — finding someone who can provide a total solution, as opposed to putting the responsibility on us to cobble together some series of vendors that can make it all work.

Richard Musci: If you’re going to be in the mortgage business, and want to provide clients with great service under your brand, you have to go with somebody like PHH. Alternatively, if you just want to have mortgage production, an 800 number will work just fine and you’ll generate some revenue, but the client experience may not be optimal.

Chan Peterson: With our customers, that’s a critical issue. So when we went through the process, PHH was the only firm we found that really understands that. That was a great move.

Steve Hood: I go by this simple philosophy: inspect what you expect. I feel like we’ve got a very focused management team that is out to make sure that we get all the attention we need. Anything we need to have accomplished, PHH is there to respond. They make sure that we’re treated as one of those big players, and they expect us to grow to that level.

Now that you’ve outsourced your mortgage operation for a few years, if we were to go and talk to the CEO or CFO of your institutions, what would be their perspective as to the relative success and the key business impacts of the program to date?

Steve Hood: I think he’d ask, “What is the value derived from the mortgage business?”, “What are you going to do next year in terms of

growth?” and “How you’re going to grow the relationships and what kind of measures are you going to use?” From a relationship perspective, how are you going to grow the deposits? How are you going to deepen the relationship? We’re at the front end of that with the mortgage offering. We haven’t gone after the customer relationship expansion piece; we’ve just started that in the last 60-90 days. In the past, we’ve really just used it as a commodity tool and now we are taking the next step.

Richard Musci: Well, we went from zero to six billion dollars in client assets within 2½ years — a great success from everybody’s perspective. The mortgage business has played a key role. We originate \$1.3 billion in mortgages per year.

Larry Washington: In terms of the operating leverage, and expense control, mortgage outsourcing is a positive. The downside is, you really only have one outlet. I have one provider for processing and secondary marketing, and so on. I’m selling all the loans to one person as opposed to different lenders.

Brad Smith: We’re not finding ourselves having to cut back on the mortgage program. Quite the contrary, similar to what Eric said, we’re getting more aggressive into the business. If we were in an in-house mode, we’d probably be getting less aggressive. The other thing — it is a little bit of chicken-and-egg. There is a philosophical difference that we’ve adopted as far as how we want to position ourselves with the client, and to be the advocate of the client. Previously, following industry trends, we moved into being a fulfillment organization. And we’ve recently moved from fulfillment to being an advocate. In order to do that, you need to be consistent with that message; you need to have product, process, and people. And, to Chan’s point, how can you do that without a mortgage? Economically, as we are becoming more committed to mortgage, we’re seeing that commitment to enhance our products for the customer. And we’re seeing the energy and the proactive nature of the interaction really explode.

Chan Peterson: If you’re a community bank like we are, it (mortgage) makes a ton of sense. The returns in small business banking are much more significant to us than they ever could be in the mortgage business. But, you know the mortgage is important to the small business customer and the retail consumer. As far as the CEO/CFO question, I think we would say six years later we know what to expect in terms of service. So, I think it’s working pretty well. We see a lot of lower-end customers; we see a lot of first-time customers, mortgage customers, and so forth. Being able to be more effective in those markets is important.

Brad Smith: The mortgage tool for our organization is a way to acquire customers. It is also a tool to expand relationships with our existing customers. So, that product and that gateway are not differentiated whether it’s a new customer or an existing relationship.

How does the PHH relationship help right the volatility in the interest rate cycle?

Larry Washington: Remarkable. I mean, can you imagine the impact to your financials in this down market, if you had to eat all the overhead, if you didn’t have a per unit, cost structure? This is when it really makes sense.

Brad Smith: Absolutely.

Larry Washington: It made a lot of sense in the up market too, because you had a machine. You had a system that could take an incredible amount of capacity in a short period of time. We would have never done anywhere close.

Steve Hood: In a low interest rate environment, we could not hire the infrastructure quick enough. Yet today, with rates rising and the mortgage production slowing, we would be faced with curbing costs. PHH has the volume across multiple markets to ride the highs and lows and maintain a stable workforce. And they continue to consistently deliver with an experienced team.

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Over the last few years, what kind of ramp up in mortgage volume have your organizations seen and have you seen a downturn? And how has mortgage outsourcing impacted your ability to manage through it?

Richard Musci: We opened the doors and turned on the lights on April 28, 2003. The next month the ten-year interest rate hit a low and the refinance boom started. Without the capacity provided by PHH Mortgage we couldn’t have handled the volume. In those six months, we did more volume than in all of 2004.

Larry Washington: Our volume has done pretty much what the industry has done, and that is, it tripled. And now it’s down, those shocks are very difficult to take. There’s a great appreciation on the financial side for the power of the relationship that we have with PHH. And the thing that’s remarkable is that they seem to be managing through the fluctuations in volume and still provide great service to our customers.

Steve Hood: If you’re changing your program, hiring out, cutting back, it usually impacts your credibility and ultimately, your profitability. Consistency is key, so the more consistency we can generate, the more successful we’re going to get.

Eric Dawes: One of the reasons that you don’t find some of the banks becoming more aggressive is because they’ve grown to like and count on the income at the peak times and now as they go into a downturn market, they are left with large overhead expenses. I think that obviously PHH helps you to leverage mortgage like a large player and be able to continue to try to grow it in the fashion that it doesn’t cost you as much to do it as if you had an in-house operation.

What were the challenges you faced in outsourcing your mortgage program and in retrospect, are there any things that should have been or can be done differently?

Brad Smith: We were concerned about having our customers’ experience be subject to the employee

quality of PHH. I can empathize with the brokers, you know; establishing a relationship within a corporate organization takes some time before referrals and hand-offs naturally take place. Why did we select PHH? It was the visibility and involvement of the leadership in the executive team. Also, it was the belief that the philosophies of our organizations were aligned. In the past year, as we’ve grown as an organization and adopted and refined our strategy, we’ve found PHH to be doing that right along with us. So it’s felt very comfortable, almost like the same organization.

Steve Hood: The only challenge we face is we weren’t asking enough of PHH to help us build the business. So we worked with them to determine how we could get more customer information to develop that relationship piece — by providing the information so we can do simultaneous home equity loan closings, build that business, and make that seamless to the customer. All of that adds to the customer’s positive perspective of the bank.

Eric Dawes: One concern was underwriting loans for very elite customers and also some of the challenging loans from the emerging market. We now have the ability to say look, we don’t care what your rules are, we’re going to keep that loan and just streamline the process and put it through. So, we’ll see how successful PHH is in dealing with this concept.

What were the concerns you had when you made the decision to outsource mortgage and what was the reality?

Chan Peterson: Fifty percent of the bank’s customers are Hispanic. So, when you talk about outsourcing and servicing, we need to have bilingual capability in our own call center; 75 percent of the incoming calls are in English and about 23 percent are in Spanish; the other 2 percent are in Polish, Chinese, and Korean. That bilingual capability was an influence in our decision to re-up our arrangement with PHH.

Richard Musci: We have a very clear way in which we communicate to our client base, based on

the values that Schwab lives by. So, we spent a lot of time with the PHH staff pre-launch discussing our culture and how we communicate to our clients.

Steve Hood: We have a significant investment in building our brand across our network and the last thing we wanted was to see brand erosion by going to a partner. We did some of the same things Schwab did — we sent our training group to the call center at the PHH headquarters. Ultimately, we worked to develop a relationship with each PHH associate to establish similarity in our service cultures.

Brad Smith: Initially when I was introduced to the PHH relationship I was concerned that we had a New Jersey firm that was basically focused on being a low-cost delivery provider. I was concerned that the customer’s experience was going to be one that was impersonal and it wouldn’t be consistent with the value proposition we were trying to offer at UMB Bank. That all changed when PHH’s senior management team came in and shared their commitment to maintaining our brand integrity and customer value proposition. Like any organization, it starts at the top. They have been active partners that have been engaged, and once we felt we had corporate alignment, frankly, the rest of it was easy. I think what’s unique in this conversation is whether you’re Merrill Lynch doing billions of dollars or you’re an organization that’s doing millions, or tens of millions, or hundreds millions of dollars, the service in the relationship seems to be common and that makes it reassuring to look to the future because I think that’s the greatest risk we have.

Larry Washington: With the cutting edge standard that PHH upholds, we stand to benefit by offering a competitive product in the marketplace. ■

Find out how PHH Mortgage Private Label Solutions can help grow your business.

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