

# SERVICING MANAGEMENT

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## Is An Oligopoly Good Or Bad?

*Interdependence and the collaborative development of more standardized system platforms are on the horizon.*

BY DAN SCHEUBLE

The pace of consolidation in the mortgage industry is still breathtaking. Five years ago, the top 10 loan originators controlled 39% of the market. Today, they control 56%. The banking industry is heading toward what economists would call a classic oligopoly, with a few mega-players in the industry controlling 30 million to 40 million loans each.

There are several characteristics of an oligopoly that the mortgage industry, specifically, will see played out in greater degrees as time goes on. These include interdependence, non-price competition and, of course, more mergers. All of these characteristics will have technology implications, affecting not just the way companies operate, but the way they relate to each other.

In an oligopolistic environment, there can be a great deal of diversity in the ways companies differentiate themselves. In the mortgage industry, differentiation will be mostly about speed, since open architectures and iterative development will make technology-based advantages easy to duplicate.

A "first to market" strategy will not mean rolling out new capabilities every few years, but rather the ongoing, rapid-fire release of innovations that, at best, will keep companies 90 days ahead of their competitors.

Technology will help level the playing field for smaller companies, but these companies must be strong players in highly specialized niches to survive. In the mortgage industry, this has already taken several forms - from

product specialization (such as subprime) and brand specialization (like online origination) to distribution specialization (such as subservicing).

As functionality in the servicing arena continues to be disaggregated, niche players will proliferate in areas like customer service, tax administration, payments processing and default solutions.



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Regardless of where an organization finds itself within an oligopolistic industry, it is critically important for an IT organization to understand its company's business strategy. Business survival will be heavily dependent on the ability to link on-target technology solutions to the areas of business specialization or differentiation. Additionally, the marketplace will demand that technologies work together across diverse operations in more sophisticated ways.

Will the industry be ready?

In an oligopoly, interdependence usually means that companies keep a close eye on the moves of others in their industry and react to those moves to protect market position. However, in the servicing segment, interdependence may also end up meaning the collaborative development of more standardized system platforms.

A good case in point was recently articulated by Kevin Shannon of Bank of America at a technology conference. He cited an example

from the automotive industry to make his case.

Toyota, one of the largest automobile manufacturers in the world, had a huge lead over rival Nissan in hybrid-car technology. However, the company came to a startling conclusion. Even with all their resources, Toyota recognized it would fail if it attempted to commercialize this vital new technology on its own. So it gave the technology to Nissan and started a collaborative hybrid program with one of its most bitter rivals.

Players in our industry will be looking for new ways to partner with vendors, competitors and the GSEs, while still retaining their own unique specialization. Even though system architectures may become standardized, three basic technologies will still facilitate the "secret sauce" of differentiation that companies will use to vie for market share: workflow automation, business rules and Web services.

The easiest way to describe workflow is to think of it as the automated navigation through a series of tasks that are required to complete a business process. As an example, think of the origination of a government loan. More than 2,500 tasks may be required to close the loan and satisfy the customer. In addition, because the overall path through those tasks may be dramatically different

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based on the particular characteristics of the loan, 10,000 or more paths may be possible. Workflow technology is the dynamic routing and re-routing through this kind of maze to perform a process in the most efficient manner.

Workflow is not new - most legacy servicing systems have an imbedded, rigid workflow. What is new is the concept of a dynamic, configurable capability which is designed into the architecture of the application.

### ***Rules processing***

Business rules processing, like workflow, is also not new. Business rules are algorithms, logic statements and calculations that define or constrain some aspect of the business - in other words, the same things human beings have been doing since the inception of the business.

The part that is new is the availability of rules engines that automate and codify institutional knowledge - and are powerful and easy to use.

The power of rules-based processing is the consistent manner in which the same process gets performed anywhere in the organization. In combination with workflow, rules processing allows organizations to focus valuable human experts on the toughest exceptions. Customer service is dramatically improved, and overall costs go down.

Web services technology is a combination of tools - extensible mark-up language (XML) and a series of standards (Web Services Description Language and SOAP) - that together facilitate and simplify the interaction between two or more programs running across disparate platforms or channels.

### ***Scratching the surface***

Most organizations have just begun to scratch the surface of the possibilities. The objective is to facilitate a whole new generation of services that can extend re-engineering efforts to a large group of mortgage industry players.

But our challenges as an industry are very large. Data is difficult to ac-

cess and comes from multiple, disparate sources. Inconsistent formats make the data difficult to use or map to other applications. There is also a heightened concern about both security and privacy, which will make the journey to fully leveraging Web services technology even more interesting.

Widespread deployment of these three powerful technologies can help all servicing organizations maximize cost efficiencies, so price advantages will eventually be slim to none. Instead, the ability to quickly innovate from a base of automated institutional knowledge will dominate a non-price-competitive strategy.

In most companies today, it is nearly impossible to harness the experience and knowledge of each staff member or leverage that knowledge for competitive advantage. To implement new operating processes, organizations must invest in time-consuming training and system re-tooling. After all that effort, inconsistent adherence to those processes is still inevitable.

### ***Leverage knowledge***

The solution to this dilemma is rules technology which can be configured (within limits) by individuals who specialize in codifying an organization's business intelligence. By implementing operating processes through rules engines, institutional knowledge can be consistently leveraged and quickly adapted to seize emerging business opportunities. Servicing organizations will be able to respond immediately to the moves of competitors and maintain or improve their market position.

Workflow technology is another powerful enabler of competitive strategy. Consider the example of an institution providing outsourced servicing to multiple external clients. After loans are funded and ready for boarding, the fundamental elements of servicing are very similar regardless of where the loan comes from.

But the servicing model each client wants to use (i.e., private label) will affect the ownership, order and mix of tasks that must be com-

pleted. With a workflow layer built into the servicing application, these variables can be customized and automated for each client. Workflow technology can expand the range of new business opportunities a servicer can effectively manage, and help free up resources to take advantage of them.

There is no reason to expect that consolidation in the mortgage industry will end or even slow down in the near future. As a result, the need to quickly shift from one platform to another - or even run multiple platforms efficiently - will continue to be an IT challenge.

Web services has the power to enable a deeper, more meaningful interaction between mortgage industry players. In the case of a merger, it also allows for a rapid transition from one platform to another - within days or hours, instead of weeks or months. This helps improve the overall economics of mergers, since consolidation efficiencies can be realized much faster when technology barriers are removed.

### ***Time will tell***

Is an oligopoly good or bad for the mortgage industry? Time will tell, but there is every reason to believe that the industry will continue to become more efficient and dynamic in this environment. In fact, with the evolving technology landscape, the face of the entire mortgage industry will be re-shaped in the coming months and years.

Ultimately, these technologies have the staying power needed to transform the mortgage industry, whether operating in an oligopoly or not. The market structure is not as important as how well we use the tools now available to us to drive changes that need to be made.

Internal politics aside, the most challenging shift will be the one in our thinking. We must look at our world from a more macro perspective and be willing to cooperate - and collaborate - with nontraditional partners. Only then can any of us expect to survive. **SM**