



Sustaining Client Relationships: Commercial Lender as Trusted Advisor

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WHAT IS THE CONNECTION AMONG TRUST, COMPETITIVE SUCCESS AND PROFITABILITY IN COMMERCIAL BANKING?

Howard was the head of the financial services practice at a consulting firm in the 1990s. One day he received a call from his counterpart at a well-known consulting firm, a major competitor. “One of our banking clients has urgent need of a project; we have tried twice and failed to come up with a team that he and I are comfortable can deliver satisfactorily,” said Howard’s competitor. “This work has to get done. Would you folks do it?” Howard couldn’t believe it—an invitation from a direct competitor to walk in through the front door to a major client. That just doesn’t happen. Howard jumped at the chance.

He took the job and his team did great work. But when he asked the client to consider doing morework with them, the client said, “Thanks very much, you folks did a great job, and we appreciate it. But you know, we would never leave your competitor—because they werededicated enough to bring youin. We know they’ll always do what’s right for us.” “And,” Howard said, “I couldn’t blame them a bit.”The story raises questions about strategy, the role of trust



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and the link between trust and sustaining profitable client relationships. Was this a fluke? How many midmarket commercial bankers do you know that would have done this? Aren't there less risky ways to create trust?

And what does trust have to do with it any-

way? Was Howard's competitor's approach a shrewd, calculating jujitsu approach to converting a weakness into a benefit? Maybe the competitor ran no risk at all, or perhaps the greater risk was to try a third time and fail. In this case, was the competitor's move simply rational, self-interested calculation disguised as chivalry? What's the connection between trust, competitive success and profitability in commercial banking? We'd like to answer that question and to

point out the implications across three market segments—large-, middle- and small-market

customers—and across several product and service lines.

Our answer in a nutshell: Trust can be hugely profitable but paradoxical—it requires risk, and you can't fake it. Trustworthiness can be increased in all market segments and will benefit customer and banker alike. The most dramatic competitive advantages to bankers are available in the middle-market segments.

WHAT'S THE VALUE OF TRUST?

When you think of trust, you probably don't think of hard economics. And when you think of profitability, trust is probably not the first thing that comes to mind. Most bankers think of trust as a good thing—a part of a complex picture of what constitutes a healthy customer or client relationship. They see it as something that comes with time, something cemented by dinners and golf outings. Most bankers would also say something like customers need to trust the strength of their banks' balance sheets. But it is possible to be

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much more precise about trust. When a client trusts a firm like the bank in the opening story trusted Howard's competitor, the economics are incomparable. Envision, for a moment, the most solid trust-based relationship your bank has with a customer.

Start with scale and volume. All else equal,

customers give disproportionate shares of business to banks they trust; that cuts transaction costs for both parties. It gives scale, scope and experience curve economies to the bank.

Now consider loyalty. It's commonly said that "trust takes time." In fact, time is neither necessary nor sufficient for trusting relationships, but—

having been established—trust relationships do tend to last. That means all the powerful economics of loyalty are realized. That includes lowered cost of sales for the bank, higher switching costs for the customer and transactional efficiencies between individuals

who come to know each others' vocabulary and processes, for example.

Perhaps the greatest economic effects of trusted relationships come not from this relatively standard list of profit drivers but from eliminating the plethora of transaction costs that companies erect to minimize risk. Paradoxically, the cost of traditional business risk prevention is enormous: Trust greatly reduces it. Consider James, the CFO for a large client of a Midwestern commercial bank, and William, the bank's relationship manager for that client.

Imagine that James and William have a very high degree of mutual understanding and respect. They also have a reasonable history of working together through a series of transactions in which the bank has added considerable value and earned the client's trust. As a result, James, the client, finds William, the banker, to be completely trustworthy—and James in fact trusts William. They are entering into the serious part of a several-month set of conversations regarding a recapitalization

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plan involving both convertible preferred debt issuance and a potential Eurobond private placement.

William: So, James, as we've discussed, this document lays out the several options facing you. We're prepared to get to work assessing the pricing comparables and scoping out the details of the potential transaction structures.

They don't want to become experts—they want to find experts they can trust.

James: William, before we pull the trigger on all that work, I do know what the options are in broad scope. Tell me: Do you have a strong feeling about the right option to take here?

William: Yes, I do; I think you're going to be best served by Option B.

James: How much work do you still have to do to satisfy yourself that Option B is the way to go?

William: To satisfy myself? Not much; I pretty much know this situation, and there are only a few things I'd want to be sure to

affirm. Not much. But I want to be sure that we do the homework so you have the ammunition to satisfy the board that we've looked at every angle.

James: First I want you to do those few things you need to satisfy yourself, and if they check out, then we'll go with your recommendation. I trust you. Of course we'll need to show the board we've done the due diligence, but once you assure me what's the best approach, we can get started on planning the execution. Can we do it that way?

Most seasoned bankers know that this is not an unrealistic conversation, even for senior clients in large organizations. Many—not all, but many—buyers of complex intangible services vastly prefer to buy what they need to buy anyway from those they trust. They don't want to become experts—they want to find experts they can trust.

In the James and William example above, we can imagine that the two of them just agreed on steps that will save four weeks of elapsed time, half a person-year of staff



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analysis, \$150,000 in outside legal and accounting fees and 30 person-days of senior executive time between the two organizations. In round numbers, that is perhaps a half million dollars' worth of saved cost. Now add in the value of the banker being slightly more likely

to be correct than the client and the client being willing to follow the banker's advice rather than to fight it. Trust adds up to real money.

Imagine other simple examples. When clients trust bankers, there are enormous opportunities: value-added coming about because of better decisions; decisions taken with less elapsed time; decisions that require far less effort; far fewer prophylactic measures taken to mitigate decision risk; and greater

opportunities for enhanced business effectiveness because of improved solutions by the bank. Those are microexamples. For a

serious peek at the macroconsequences of trust, Philip Evans and Bob Wolf cite one measure by which half the U.S. gross domestic product in 2000 consisted of transaction costs broadly defined¹.

Transaction costs add no economic value but serve to monitor, judge, evaluate, measure or otherwise buffer relationships between entities. Virtually the entire legal and accounting professions are engaged in transaction costs; so is much of the work that goes into measuring bonus plans, compliance procedures and contracts of various sorts.

Much of our economic progress in the last century can be described as lowering the costs of production. A major source of lowered cost of production comes about by specialization of functions or division of labor. Every division of labor requires transaction costs to count, adjudicate and otherwise coordinate the now-separated functions. This decade's phenomenal growth in outsourcing increases not only the opportunities for transaction costs but also the hunger to pursue them.

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And yet, we are approaching the point, say Evans and Wolf, where the savings from reduced production are more than offset by the added costs of transactions. An important part of the solution to rampant transaction costs, Evans and Wolf say, is trust—not blind trust but the kind of trust that comes from demonstrated trustworthiness. Whether you look at it from a micro- or a macroperspective, the power of trust is apparent. But this begs one obvious, huge condition: To obtain these benefits, the truster must trust, and the trustee must be trustworthy.

How is it that one party can come to trust and the other to be worthy of trust? The answers lie partly in personal relationships and partly in four organizational principles of enhancing trust. In this article, we will deal only with the latter.

THE PRINCIPLES OF TRUST-BASED SELLING

The only way to be trusted in banking is to be worthy of trust—to be trustworthy. Intent

matters; there are no shortcuts.

The core of trust-based selling is the belief that if you behave in a trustworthy manner, your customers will more than amply reward you. That sounds simple enough, but in practice, it is very demanding. In practice, it means you must continually measure decisions and actions first by what is good for the client and, second, by what is good for you. It means you must occasionally look past the transaction to the relationship. It means you must be willing to work with your customers as willingly as you would work with your co-workers. And it means you must behave transparently to your clients with respect to data, processes, even internal performance metrics and motivations.

The acid test of trustworthiness is the willingness to respond as the consulting firm partner from the opening story did in a time of stress. The benefits of being trustworthy are enormous—but also paradoxical. They cannot be sought as ends in themselves; they only come to us as side effects.



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If you are a trusted advisor to your clients, you will be very profitable. But if you set out to be profitable through trust—trying to make trust a tactic or a tool—it will blow up in your face. Being trustworthy means being willing to put the client’s interests ahead of our own. If we’re only doing it to make a buck, then by

definition we become selfish and untrustworthy. Hence the paradox: You actually have to care.

Those who do behave in a trustworthy manner tend to apply four basic principles continuously throughout all their business development affairs.

Principle 1: Client orientation for the sake of the client, not the banker. As noted above, “client focus” for the seller’s sake is bogus, no more genuine than

the “client focus” of a vulture. True client orientation means we seek to address the client’s best interests, in the sales process as in all else. If that means another bank is

best for the client for a particular transaction or product, we say so, knowing that in the long run we get credit from present and future clients for being client focused for the client’s sake.

Principle 2: A medium- to long-term perspective. This means a focus on the relationship, not the transaction. We should say, “The relationship is the client.” Acting with the medium- to long-term perspective in mind also solves the usual sellers’ concern about the economics of trust: It means the economics of a particular project or transaction should be discussed in terms of fairness in the long run, rather than in competitive terms. A couple in a marriage quickly compromises on who takes out the garbage, rather than belabor it to get the best deal. There is much more at stake in a serious relationship than getting the best deal in each transaction.

Focusing on relationships fosters transactions, but transactional focus alone—in isolation from others—can choke relationships. That doesn’t mean we can’t focus on

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transactions—just that they can't be viewed in isolation from the stream of transactions over time that define much of the relationship—added value to both the client and the bank.

Principle 3: A habit of collaboration.

Business developers demonstrate trustworthiness by constantly involving the client-

to-be. Don't speculate about what clients are thinking—ask them. View business development processes themselves as things that can be done collaboratively, rather than as a competitive exercise in putting the best face forward. Value meetings over phone calls and phone calls over letters and emails. Practice putting

all issues on the table for joint discussion, rather than negotiating on them from competitive positions.

Principle 4: A willingness to be totally transparent. Nothing destroys client trust faster than the banker who appears to be withholding information or trying to control the

client. When you don't know something, say so. When you haven't got the perfect staff, say so. Be willing to be open about your pricing policies, product offerings, expertise. What you lose in control over perceptions is more than compensated for by the goodwill you get for being transparent.

APPLYING TRUST PRINCIPLES IN COMMERCIAL BANKING

If a bank operates according to those four principles, it will be seen as trustworthy. The four principles pretty much go together; for example, it doesn't make sense to be very collaborative but not transparent. But the relative impact of those four principles and their precise connection to commercial banking profitability will differ by customer types or segments. Exhibit 1 depicts the impact of acting on trust principles across six segments: price/performance buyers and relationship buyers across each of large, middle-market and small commercial segments. Each segment has a particular profit model.

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Exhibit 1 Impact on Segments of Acting from Trust Principles

Segment	Product and Price Opacity	Profit and Trust	Buyer Types	
			Price/Performance	Relationship
Large Corporate /Rated Names	Transparent pricing and product usage. Both are well known to bank and customer alike.	Profit Model	A. Credit RAROC marginal; other services drive profitability.	B. Lead banks get 70% of noncredit revenue if price/performance is good.
		Trust Principles	C. Principles 1, 3: Listen, collaborate to customize. Principles 2, 4: Relationship is transaction driven, credibility key: better to pass than fake it.	D. Principles 1, 3: Spend the time to understand, commit the bank. Principles 2, 4: Your need to know = theirs.
Middle- Market/ Unrated Names	Opaque pricing and product usage.	Profit Model	E. Credit RAROC marginal; need broad product penetration, but best in class, lowest price.	F. Trusted advisor status increases calling success rate and improves pricing.
		Trust Principles	G. Principles 1, 3: Careful listening, plus virtual customization by segment needs, enables affordable responsiveness.	H. Principles 1, 2, 3: Spend time to add value beyond transaction. Principle 4: Don't be greedy or you'll poison the well.
Small Commercial	FICO-based product and pricing bundles.	Profit Model	I. Engineer products and processes for low cost, high value.	J. Winning personal business along with commercial.
		Trust Principles	K. Principles 1, 2, 3, 4: Few actually deliver on their promises to these customers. Say what you'll do, and do what you say, and you'll win.	L. Principles 1, 3: Client must perceive high understanding of his or her situation. Principles 2, 4: Candid answers to "what's in it for me long-term?"



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In each segment, the interaction of the trust principles and the profit models is unique.

SEGMENTATION BY MARKET SIZE

The market-size segmentation drives important differences in needs, cost to serve and revenue potential by segment;

products used; support services required; sales process; skills needed; pricing; etc .But one characteristic stands out as relevant to trust: the degree of transparency or opacity of pricing and product usage in the market segment.

In the large corporate/rated names segment, there is a great deal of transparency regarding both price and product usage. The clients know the banks' products and pricing. The bankers know the

clients' usage and what they're likely to pay. Each knows that the other knows. In fact, most deals done in this market are well publicized.

In such a market, Trust Principle 4—transparency—is virtually built into the market. This has powerful effects in successful sales behavior: Since those who do not conform to the fourth principle shoot themselves in the foot, everyone is likely to conform; hence, the relative importance of other principles is increased.

By contrast, in the middle-market/unrated names segment, pricing and product usage are quite opaque; relevant comparative benchmarks for each factor are difficult to obtain for both parties. In such a market, acting according to Trust Principle 4 has a highly differentiating impact. So does Principle 2, the medium- to long-term perspective.

SEGMENTATION BY BUYER BEHAVIOR

The buying behavior segmentation has helped many banks hone their offerings and sales approaches to better fit how clients want to do business. Some—price/performance buyers—see themselves as the experts or want to

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They tend either to believe they don't have the level of expertise their bank does or to prefer to focus their energy on other areas of the business and find an expert they can trust in the banking business.

function as their own general contractors. They are disproportionately represented in the large

market segment but by no means only there. While they tend to focus on transactions, that does not mean they are immune to trust relationships. They are as much influenced by trust dynamics as relationship buyers, but their locus of trust assessment is around the transaction itself.

They will trust a bank if the bank shows excellent client focus in designing custom solutions built on a deep understanding of the client's situation.

Others—relationship buyers—prefer to buy from a very few key banks with whom they have deep, long-lasting relationships.

They tend either to believe they don't have the level of expertise their bank does or to prefer to focus their energy on other areas of the business and find an expert they

can trust in the banking business. Rather than take the risk themselves, they prefer to pay an “insurance premium” in the form of higher pricing to assure themselves that they can trust that they have a call on their relationship bank's balance sheet if and when needed.

PROFIT MODELS BY SEGMENT

The six-box grouping in Exhibit 1 also leads to differential profit models for the bank. For example, a bank may make money by customized products (large corporate, price/performance) or by share of services (middle-market, relationship).

TRUST PRINCIPLES BY SEGMENT

The relative impact and importance on bank profitability of the trust principles varies by segment. Let's look at each of the six cases in turn (Exhibit 1).

LARGE CORPORATE/RATED NAMES

Price/performance buyers. With the more transaction-focused price/performance buyer



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(A, C in Exhibit 1), the buyer wants to act as a general contractor. Credit RAROC (risk-adjusted return on capital) is marginal due to competitive, Libor-based pricing. Profits are made through other services—investment banking and operational.

Trust Principle 1 helps bankers in this segment by careful listening. That

The market for banking services for mid-market, unrated names is relatively opaque.

allows them to customize solutions priced at or below the market and to deliver on the promised performance. Once won, trust provides competitive advantages in cross-selling the products on which account prof-

itability rests, as long as trust is maintained, transaction by transaction.

Relationship buyers. Relationship buyers (B, D in Exhibit 1) among large, rated names trust those who make the effort to learn enough to be willing to credibly commit to providing the balance-sheet support they think they will need over time. They will pay a premium price for such assurances and reward

their relationship bank(s) with privileged dialogue and access that leads to superior cross-sell and account profitability. In return, the bank must be transparent in its commitment, the conditions that underlie it and how it expects to be compensated for the risks it is underwriting.

MIDDLE-MARKET

The market for banking services for mid-market, unrated names is relatively opaque. There is little if any publicly available data on transactions, pricing or product usage in this segment. Competitive advantage can be gained by developing better analytical tools that enable more accurate prediction of product needs and revenue potential and by using targeting approaches that direct selling expense where it will be most productive. Perhaps because of the difficulty of accomplishing this systematically better than the competition, banks that know how to engender trust among their targeted clients enjoy particular advantages in this market. But, as



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in the large corporate market, differences in buying behavior mean that trust is earned in different ways.

Small companies can be very profitable for trusted providers who have the cost structure, highly defined products and distribution systems to be competitive in this market.

Price/performance buyers. Price/performance buyers (E, G in Exhibit 1) want virtual customization based on deep understanding of industry segment needs. This is the key to being able to afford the perceived responsiveness that forms the basis of trust in this market segment. But even these clients know that their bankers must make an adequate return on their capital and expense to want their business. And they appreciate and reward trust engendered

by candor, which avoids wasting their time, with a willingness to continue the dialogue on the next transaction when you may have lower costs or better product performance.

Relationship buyers. Relationship buyers (F, H in Exhibit 1), on the other hand, want a trusted bank-ing partner who has a deep understanding of their particular business and often their personal financial situation as well. Winning their trust and keeping it by spending the time and adding value well beyond a specific transaction offers the opportunity to be an insider in ways that no competitor can duplicate. These can be highly profitable relationships, particularly with growing companies, as few if any sales are lost at reasonable pricing. Transparency in the relationship assures no unpleasant surprises, which is one of the few ways competitors may have an opportunity to displace the trusted provider.

SMALL COMMERCIAL

Small companies can be very profitable for trusted providers who have the cost structure, highly defined products and distribution systems to be competitive in this market.

Price/performance buyers. Bankers must be careful to avoid over servicing price/



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performance buyers (I, K in Exhibit 1) in this size segment, as they will not likely reward them with enough revenue to justify the cost. At the low end of this market, credit is little more than unsecured personal loans based on FICO scores. Trust is earned more by the care with which product, pricing and distribution

The power of trust—in concrete, solid economic terms—is enormous.

is engineered to fit the needs of specific segments and by delivering on the promise than by time spent advising.

Relationship buyers. Relationship buyers (J, L in Exhibit 1) in the small commercial market are open to consolidating their business with one provider they trust if the incentives for doing so are clear and compelling. Since the personal and business finances are often intertwined, there is ample opportunity to win client trust through careful selection among structured, low-cost but value-added advisory services that meet their business and personal needs. Properly done for clients with the right revenue potential, the cost is a good investment in winning and keeping a profitable relationship.

TRUST AND COMMERCIAL BANKING

The power of trust—in concrete, solid economic terms—is enormous. A bank that succeeds in establishing trust with its customers can dramatically outperform its competitors.

Further, a bank that succeeds in understanding the various permutations of trust—and further applies them specifically to the distinct needs of varying buyer segments—will succeed in competitively differentiating itself.

But the paradox of trust cannot be overstated. If you set out to achieve those results by trying to use trust as a tactic, a tool, a technique, you will fail conspicuously. The core of trust is a genuine focus on the Other—in this case, the customer. If used only as a tool for the bank's profitability, customers will smell insincerity a mile away and run from it. Trust and selfishness cannot coexist.

If you want to be trusted, be worthy of trust. Be trustworthy. If you do so, the economic benefits come as a by-product. They are subverted only if we think customer focus is a means to an end, rather than the end itself.



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ENDNOTES

- ¹ Philip Evans and Bob Wolf, Collaboration Rules, *HARVARD BUS. REV.*, July–Aug. 2005.

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