Technology and the Herd Mentality

We've witnessed the technology stock market bubble and felt the pain of herd mentality when the market crashed in the spring of 2000. The dot-com boom and bust were felt even closer to home with mortgage.com and iOwn. I think we all learned some good lessons from this period, and I'd expect it would be decades before such a debacle would be repeated (let's hope, anyway). What most don't realize, though, is that the herd mentality in mortgage technology remains alive and well.

The mortgage technology industry has its own trends that can be seen over the years in mini-booms and busts. For the last 30 years, we've had numerous examples where a misguided herd mentality drove us down the wrong path. I believe it's important to learn from the past so we don't repeat these mistakes in the future. Still, I have no illusions that mistakes similar to those that will be described here won't continue in the future.

I started in the mortgage technology field in 1982, when I built the first loan origination system (LOS). For the first several years, it was a fledgling area of mortgage technology with only a handful of companies. In the late 1980s it became a full-fledged boom, and I recall one Mortgage Bankers Association (MBA) annual convention where there were no fewer than 50 LOS vendors represented—almost all of which were in startup mode. Those mortgage companies that purchased systems from these startups learned firsthand how easy it was to lose a lot of money on a bad technology investment.

The next big boom was in videoconferencing. At its height, almost every mortgage company was evaluating how its business would be impacted by this new technology, and was either building a defensive strategy or buying into this latest fad. At the very least, more than half a billion dollars was invested into videoconferencing for the mortgage industry. When all was said and done, 100 percent of these investments were lost. The mentality was that videoconferencing would replace the loan officer and would create a whole new way of working with customers. The lesson learned was that technology isn't going to replace the customer relationship (though we know now that it can significantly enhance it).

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The next example where the herd mentality was well-demonstrated was with the old Accredited Standards Committee (ASC) X12 standards. Almost every mortgage technologist bought into this idea as they saw it as the solution to the myriad file formats plaguing the industry. Unlike some of the other fads, this one never made it mainstream. In fact, it was probably the technology firms themselves that were hurt the most as they spent research and development (R&D) money trying to adopt X12 standards that never became a standard. We can see that even the very best technologists can fall prey to herd mentality. The good news was that what we learned with X12 helped tremendously with the newer and successful Mortgage Industry Standards Maintenance Organization (MISMO) standards.

Remember the VANs? I'm not talking about the van conversions you could drive, but the value-added networks heavily promoted by Fannie Mae, Freddie Mac and Computer Power Inc. (CPI; later bought by ALLTEL Information Services and then by Fidelity National Financial Inc.). Hundreds of millions of dollars were spent in this area. The objective was to use a private communications network to carry all the products and services that the industry uses in an electronic format. Each firm sought to control the electronic order and delivery of millions of transactions by the entire industry.

The general thought was that the Internet wasn't secure enough and that the mortgage companies and vendors would pay dearly to use these VANs. Some of the brightest minds in the industry convinced top management at these firms that VANs were the solution every mortgage company and industry vendor needed. Of course, the Internet rolled over VANs like a steamroller over ants. I'm not even sure we learned much other than the fact that even the largest firms can make very expensive mistakes.

Workflow solutions are another area that confused so many mortgage company management teams. This great-sounding solution seemed like just the ticket to eliminate the costly bottlenecks and manual labor processes of mortgage origination. However, in the majority of the installations, the cost of the technology was more than the savings that resulted from its use. Again, even the experts were stymied by this technology, with so many consultants advocating the use of workflow applications to significantly reduce the high cost of loan processing. A lot of mortgage companies wrote off their investments in this area, and this "hot technology" has faded in recent years. Another lesson learned was that there are no

economies of scale in loan production. It's why small mortgage brokers have played a growing role in the origination marketplace in the last few decades. I'll actually argue that a larger regional loan processing center creates a higher cost per loan compared with smaller local offices.

There have been other such fads that received a lot of initial interest and then faded off into history. These include the Internet transaction systems (e.g., nCommand, Xpede, NetOriginate, Bridgespan), hundreds of dot-com E-LOAN imitators, mortgage rate distribution systems, personal digital assistant (PDA) applications, lender application service provider (ASP) solutions (e.g., Ultraprise, eCloser, Loan Trader, etc.) and various imaging solutions.

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Certainly, not all such applications and companies have failed. There are some success stories, but on average there are far more losers than winners. In general, our industry has a difficult time separating the wheat from the chaff. It seems that once a new idea is developed, a ringleader then steps forward. In many cases, a herd then starts to follow the ringleader and pushes for wide adoption of the new technology. There is often a lack of objective analysis of each new technology. In addition, there's a bias that just because it's new technology, it must be better (like workflow applications for loan processing).

I've seen very little testing where true benefits are weighed against all-inclusive costs. I used to use prototypes with any new technology, and would often use a stopwatch with real loan processors. There had to be a sizable cost savings to consider a new solution. For example, when laser printers first came out, they were so expensive ($10,000 or more) that they were more costly per page than the old daisywheel printers with preprinted forms. So for several years, laser printers were a bad investment. It wasn't until Hewlett-Packard developed its low-cost laser printers (then costing about $3,000 each) that it began to make sense for most mortgage offices. Sometimes you have to wait for the technology to mature before you can expect widespread adoption—don't jump on the bandwagon too soon.

I believe there are some new technologies being introduced to our market even today that fall into the category of a bad investment. Yet, companies will be led to make these investments by those that believe strongly they have found a better solution. We've got to avoid the herd mentality and work at making our own analysis before we adopt the next new thing.

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