Expanding the marketable universe

A changing marketplace
The years 2008 to 2010 presented unique challenges to the lending industry — unprecedented regulation combined with unexpected/unpredictable consumer behavior (new payment priority hierarchy, strategic default, etc.). Marketing budgets were slashed, and marketing engines came to a screeching halt. In mid-2010, some lenders started focusing on growth again — carefully navigating the new terrain by focusing primarily on the least risky consumer segments — ensuring that their known and tested strategies for acquisition would still produce desired results. In 2011, lenders have applied that knowledge and are implementing strategies to grow portfolios by expanding their marketable universe.

Many credit marketers are now moving beyond testing and have started to market to slightly riskier populations (Figure 1). From monitoring and booking lower-scoring segments to identifying strategies for near-prime and underbanked consumers, the breadth of methods that lenders are using to acquire new accounts is expanding.

Figure 1: Average VantageScore® at Origination. The Experian–Oliver Wyman Quality Index dropped from its three-year high to 845 as new lending expanded to riskier VantageScore segments — most notably in mortgage, bankcard and auto loans.

The competitiveness in the prime market — coupled with the new reality of credit underwriting, post–Credit Card Accountability, Responsibility and Disclosure (CARD) Act — are two of the primary influencers driving the way in which lenders are seeking growth opportunities. The current environment has led to key changes among the consumer populations being evaluated for underwriting today — populations that were largely avoided from 2008 to 2011 among the majority of lenders.

Now lenders are re-evaluating their underwriting strategies to meet the needs of their growth objectives in the new credit environment. Figures 2 to 4 below provide additional insight into how the current environment has impacted the manner in which lenders are underwriting consumers, such as slowly moving to lower score ranges by loosening mortgage delinquency requirements and underwriting thin file consumers.

VantageScore is owned by VantageScore Solutions, LLC.
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Figure 2: VantageScore spread between consumers seeking credit and consumers at time of origination. The spread is slowly converging between consumers who are seeking credit and consumers who are being underwritten by lenders. This suggests that some lenders are slowly starting to address the need for credit in the near-prime market.

Figure 3: Mortgage trade 60 days past due at time of origination. The volume of bankcard accounts booked containing a 60-days-past-due mortgage loan has increased since 2009 and 2010. More lenders are adjusting underwriting criteria to accommodate the changes in the mortgage industry.
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**Figure 4: Thin files at time of origination (zero to two previous tradelines).**
Recent analysis indicates that lenders never fully abandoned the thin-file market. The percent of new accounts considered thin files at time of origins has remained stable at approximately 5 percent. Although the total volume is down, the percent of accounts considered thin files has remained constant.

As a result of trends in consumer credit behavior and underwriting practices, lenders are finding it beneficial to take another look at product diversification and universe expansion as key components of their overall marketing strategies. Issuers are finding that becoming more diversified will allow even greater flexibility when marketing to an expanded consumer base.

Of course, any strategy supporting portfolio growth includes the critical use of analytics and data assets that enable desired growth while mitigating risks associated with expanded consumer segments.

**The analysis to support a near-prime strategy**
Experian® can help you redefine the way you evaluate the near-prime market by helping to identify analytically based methods for selecting the most profitable segments of this population to target. Our analysis indicates that you can confidently identify prospects within the near-prime segment who are trending upward and that now is the time to make an offer to these receptive consumers.

To support our advocacy of the value of the near-prime consumer, we conducted a trended analysis of the near-prime bankcard and mortgage markets to illustrate the credit behavior of near-prime segments over a 12-month time period. The analysis evaluated prime and near-prime subpopulations from June 2010 through June 2011 — comparing performance characteristics at quarterly intervals.
Analysis design

Our analysis pulled a sample population requiring each consumer profile to contain at least one new bankcard opened between March 1, 2010, and June 30, 2010. For the 12-month performance window, July 2010 through June 2011, the population was segmented based on VantageScore, VantageScore migration and types of delinquency. The bad definition for this analysis was 60 or more days past due.

The following segments were created to compare performance characteristics:

Figure 5: Analysis design
Within the near-prime segment, two additional segments were developed to place those consumers with only a mortgage delinquency within a separate category. Therefore, near-prime was segmented into (a) near-prime mortgage delinquency only and (b) near-prime any industry delinquency.

To further understand performance dynamics within the consumer population that contained any industry delinquency, this population was segmented into categories that defined their migration path over the performance window: (a) from prime to near-prime, (b) stayed near-prime and (c) from subprime to near-prime.

This strategy allowed us to compare key trended performance data within a segmented near-prime population. Creating a separate view of the credit behavior associated with near-prime mortgage delinquency only allowed further insight into performance associated with consumers who have been categorized as strategic defaulters as compared to any industry delinquency. For this analysis, it is important to note that not all of the consumers within the mortgage only delinquency segment are strategic defaulters. Whether this is due to unemployment or a strategic mortgage default, the near-prime mortgage delinquency only contains consumers who experienced difficulties with first mortgage payments.

**Key findings**

*Figure 6: Bankcard bad rate.* As expected, near-prime performed better than subprime at all points in time throughout the performance window. At 12 months, June 2011, there is a huge spread between the prime bad rate of 0.9 percent and subprime at 36.4 percent. Near-prime is at 9.8 percent.
Figure 7: Bankcard bad rate – migration to near-prime. Using the 9.8 percent bad rate in Figure 6 as the benchmark, the formerly subprime segment contained significantly higher bad rates. The formerly prime segment that migrated to near-prime performed at a bad rate well below the all near-prime rate of 9.8 percent, further supporting consumers who were formerly prime seeking to return to a prime status.

Figure 8: First mortgage bad rate – near-prime bad rate on first mortgage. Focusing on June 2011, prime had a bad rate of 0.9 percent, and subprime, 5.3 percent. Just as illustrated with bankcard, near-prime is between the two at 2.8 percent.
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**Figure 9: First mortgage bad rate – migration to near-prime.** With a 2.8 percent bad rate for all near-prime as a benchmark, the lowest-risk segment is stayed near-prime. Static or stable is better but only negligibly so. With a consumer who has improved his or her score for a mortgage, this is possibly just a temporary improvement. The stable score is the least risky for this group.

![Bar chart showing first mortgage bad rate – migration to near-prime](chart.png)

**Figure 10: 12-month VantageScore shift of migration to near-prime segments.** The formerly prime segment illustrates a 50 percent increase for the 6+ change in VantageScore over the performance window. We can infer that the formerly prime segment is only temporarily near-prime and most are tracking back to prime.

![Bar chart showing 12-month VantageScore shift of migration to near-prime segments](chart2.png)
Figure 11: Bankcard bad rate for near-prime delinquency segments. The bankcard bad rate for the near-prime mortgage only group indicates stability over the nine- and 12-month time periods. However, for the near-prime segment with delinquencies from any industry (the distressed group), the bad rate continues to increase. We can infer that consumers who are only going delinquent on a mortgage might be a better risk for bankcards.

![Bar chart showing bankcard bad rates for near-prime delinquency segments.]

Figure 12: 12-month VantageScore shift for near-prime delinquency segments. Ninety percent of the total population within mortgage only and any delinquency shift at least 6 points during a year, most likely going up rather than down in score, whether they are late on their mortgages only or other debts. The percent change upward is higher within the mortgage only segment, possibly due to a higher volume of consumers who were prime and who are now trying to move back into the prime space.

![Bar chart showing VantageScore shifts.]

Shifts from June 2010 through June 2011
Analysis conclusions
The data indicates that 1) formerly prime consumers continue to recover from the economic downturn; 2) formerly near-prime consumers, although remaining in the near-prime category, exhibit stable fluctuations with respect to decreases in VantageScore; and 3) formerly subprime consumers, although now near-prime, have a higher propensity to decrease in score.

Additionally, based on the illustrated credit behavior characteristics, the near-prime segment that was formerly prime is a key segment to identify and expand your marketable universe — now — while the volume of offers to these consumers is not as competitive (or repetitive) as prime consumers are experiencing. Within the mortgage only segment, there appears to be subpopulations, pulled into near-prime due to life events, that would respond positively to new product offerings and perform similar to prime.

There is significant opportunity in the near-prime space to generate and accelerate portfolio growth. The use of trended attributes and propensity models to segment and target subsegments within the near-prime universe will aid in identifying the risk that is appropriate and likely to open consumers within the population.

Building the strategy behind universe expansion
The analysis above, coupled with current industry growth activities, indicates that lenders can find viable consumer populations within the near-prime consumer population — and many credit marketers are actively evaluating this market today. Current strategies to initiate growth begin with understanding the spectrum of data required to target and underwrite prospects confidently.

Figure 13 below provides an overview of key questions that should be addressed to prospect for new customers as well as deepen existing relationships. There exists a variety of credit behaviors and asset questions that, when answered, will provide credit marketers with the ability to provide the right products to the right set of consumers.

The behaviors listed below are credit-specific: How do consumers manage credit? Are they seeking credit? How risky are they based on their credit behavior? How are they using credit products? What do they think about the use of credit? How are they using credit at a transactional level?

Understanding a consumer’s ability and capacity to repay a loan are critical components to understand to augment your understanding of their proven risk behavior. Questions that address a prospect’s income, net worth and deposits are all relevant to ascertain a complete financial and risk assessment.

Evaluating all of these consumer behaviors at the point of marketable universe selection will drive the most efficient use of marketing budgets.
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**Figure 13: Behavioral and asset questions to construct a consumer profile for portfolio growth and expansion.**

Continuum of growth initiatives

After determining data requirements, development of a continuum of growth initiatives will allow lenders to create a strategy that is specific to their portfolio growth objectives and budget constraints. Additionally, the continuum should include strategies that allow lenders to explore both internal and external growth mechanisms.

Universe expansion opportunities can be categorized by those initiatives that are internal to an organization versus external. Traditionally, growth strategies have a more internal focus, encompassing how the organization can make key product and policy changes to impact growth. Today’s most efficient universe expansion opportunities are those that utilize external data sources to target more effectively. Figure 14 illustrates initiatives that are currently most prevalent in the industry.

**Figure 14: Universe expansion opportunities.** Growth through universe expansion can be categorized into four key areas: near-prime marketing, channel expansion, identification of new entrants and radical processing changes.
Some of the key strategies lenders are evaluating on a large scale and more limitedly implementing to meet portfolio growth objectives are reflected within each of these areas.

1. Near-prime marketing: strategically targeting up and down the risk scale
2. Channel expansion: prequalifying consumers online to manage risk of prospects being evaluated for underwriting; utilizing email campaigns to communicate offers to consumers
3. New entrants: capturing new entrants to the lender’s criteria; identifying new consumers to the bureau’s marketing file, evaluating thin-file/no-hit consumers for credit marketing
4. Radical processing: acquiring prospects based on event changes; implementing strategies using propensity models; marketing smaller, more targeted campaigns on a more frequent basis to coincide with consumer need

**Near-prime**

In order to expand into the near-prime segment, lenders are requesting Experian’s assistance with regard to identifying the segments of this population with the most manageable risk.

- Best practices begin with conducting a vintage campaign analysis to understand performance dynamics of near-prime within your existing portfolio
- The next step is to conduct a near-prime analysis using archived data to understand how the consumer has trended over time using a risk score and/or attributes
- In addition to the analytics, we are recommending using tools to understand consumer credit spend data and income assessment models to address a consumer’s ability and willingness to pay

These strategies lay the analytic and data groundwork by providing in-depth targeting and segmentation strategies that will allow you to strategically expand your marketable universe within the near-prime consumer population.

If you are interested in forgoing the vintage analysis described above and moving immediately to market testing, it is important to develop strategies that provide you with data that addresses specific solutions. The first piece of data that defines the consumer as near-prime is a risk score. In addition to the score, data attributes (credit usage/behavior) have long been a source of additional information to segment and target prospects. Of recent interest is the evaluation of trended data to identify a prospect’s behavior patterns over both the recent short term (previous three, six and nine months) and longer term (previous 24 months). The combination of scores and data attributes (both point-in-time and trended) allow for microtargeting within subsegments of the near-prime population.
Channel expansion
Questions surrounding channel expansion typically involve the development of an online acquisitions strategy. Forward-thinking credit marketers who choose to expand into the online channel have integrated tools that assess a prospect’s risk prior to the application process. This reduces the volume of prospects who go through the full application process, resulting in better approval rates and ROIs for this channel. This is part of the full point-of-contact strategy that most lenders have developed to address how to best acquire new customers and cross-sell existing customers at each point of contact with their institutions — from Websites to call centers. A point-of-contact strategy expands the acquisition efforts outside of direct mail while managing risk and using tools that provide insight during interactions.

New entrants and radical processing
Lenders are positioning themselves to take advantage of new entrants to their marketable universe and the bureau file as well as radical processing solutions to supplement direct-mail campaigns.

In today’s marketplace, lenders seek to quickly respond to consumers who are in the market for credit products or who now qualify for these products based on the credit marketers’ lending criteria.

The strategy to achieve successful results and capture “new entrants” and “credit seekers” consists of the following:

• Implementation of a “continuous” prospect monitoring process, using propensity scores, triggers and attributes that identify consumer credit migration behavior

• Integration of a propensity model into prescreen programs by conducting a vintage campaign overlay to determine score cut strategy; implementation of a mail/monitor strategy to analyze the impact of the propensity model

• Augmentation of current processes with “hot lists” that identify new-to-bureau consumers

• Evaluation of thin-file/no-hit consumers for marketing

• Inclusion of an email campaign to communicate offers to consumers; test-driving consumers to mobile devices to maximize response

The benefits of the initiatives outlined above include higher approval rates, as these consumers either have not been heavily marketed to (new entrants/hot lists) or are shopping for credit (credit seekers). In addition, strategic targeting strategies, whether propensity models or trigger/attribute overlays, allow lenders to zero in on the most responsive segments of prospects. The bottom line is that all of these strategies allow for acquisitions growth outside of direct mail and typically augment acquisitions strategy at a lower CPA.
In conclusion
Experian is helping you to redefine credit marketing by delivering unique predictive insight to redefine how you target prospects and manage your portfolio growth. Our unmatched expertise in data, analysis and innovative technology will guide you decisively; mitigate risk; and secure valuable, profitable relationships.

Credit marketers who evaluate the right data assets to supplement targeting efforts have the capability set to target viable niches within the subprime population and to expand their channels for communicating prequalified offers to consumers. These marketers will emerge quickly over the next 18 months as leaders in portfolio growth. The key is getting the right product to the right consumer at the most appropriate time. Whether that is a new product or a version of an existing product, with new line assignment and/or new pricing, selecting the right prospects within the near-prime market and/or identifying the tools to match these consumers to the right products is now a reality that most top lenders are pursuing. The tools and data are available to begin expanding your marketable universe now.