TRENDING UP
METRICS THAT MATTER

New opportunities in portfolio management

Portfolio reviews are a valuable tool for financial institutions to monitor, manage, and act upon credit risk and enhance overall returns. Beyond this, there is an opportunity to protect against attrition, build loyalty and stimulate business growth by addressing account shifts. To reach these goals, it is essential to understand consumer behavior fluctuation, economic trends and the dynamics of growth to help create more effective credit risk management strategies. Portfolio reviews have historically provided point-in-time data, but can include even greater predictive insights when performed routinely. Regularly observing changes in individual accounts provides the ability to proactively assess trends in order to manage accordingly. For example, the super prime risk tier has grown 22% since the mortgage bubble.[1] Have you seen this shift impact your portfolio? This paper details changes in consumer trends and data points that may reveal opportunities to better manage risk, make more profitable, competitive lending decisions and strengthen customer or member relationships.

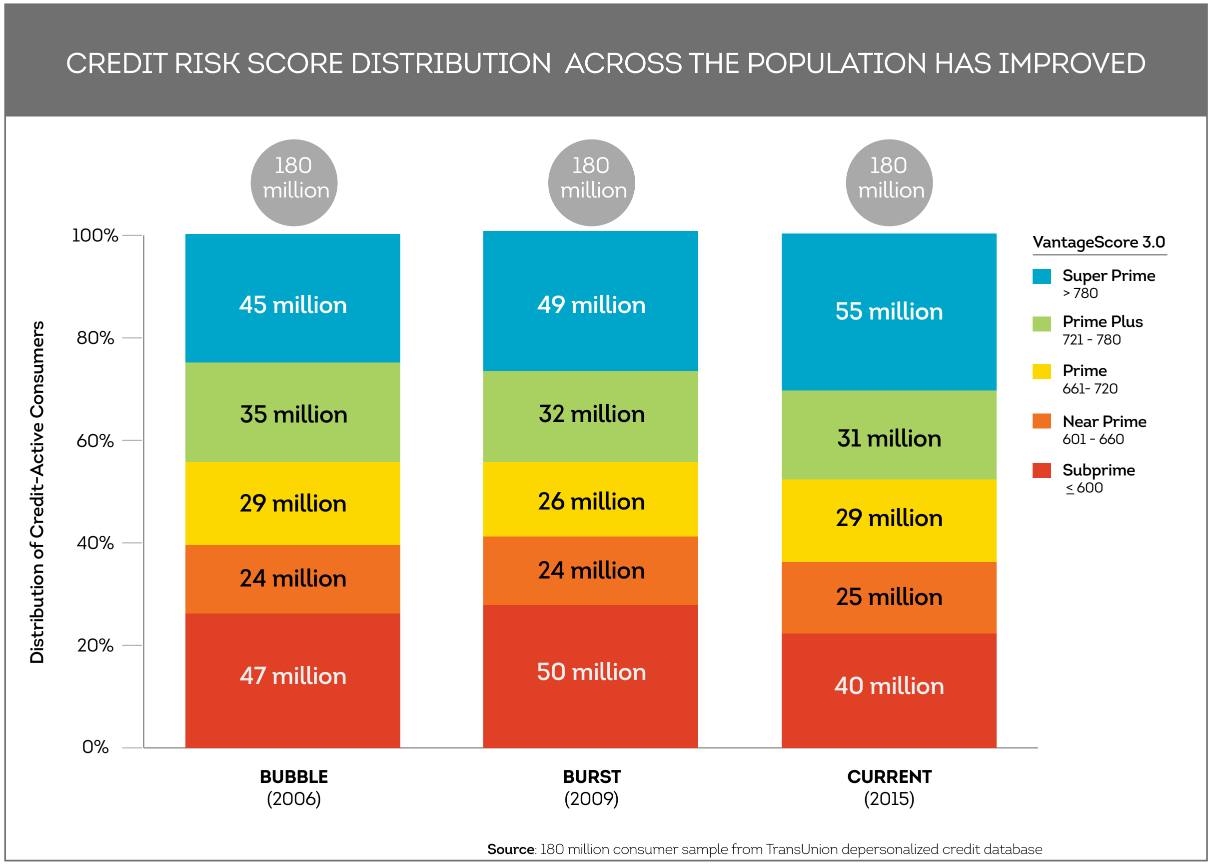
Emerging consumer segments

American consumers have evolved - as shown by their attitudes, behaviors and even changing credit performance. A Forbes article detailing trends that will shape consumer behavior noted a cultural shift toward all aspects of rich and full lives, citing: escape, mindfulness, and super-personalization as major trends, among others.[2] People who have grown up in a digital world are demanding more from every type of experience, with greater value placed on transparency and authenticity. Perhaps you have witnessed this shift in your book of business as well.

The changing demands of consumers are partially due to Millennials, one of the largest and most influential generations in history. Approximately 80 million Millennials holding $200 billion in buying power are entering their peak spending years.[3] This is happening alongside well-managed balance growth and low levels of delinquency - further support that the U.S. economy has recovered.

Together, evolving consumer behaviors and the improved economy have created new opportunities. Backed by strong economic fundamentals, consumer credit performance has been steadily improving within certain lending products such as Mortgage and HELOCs. Concurrently, subprime auto lending has caught up to its pent-up demand and account volumes have doubled in the last six years. There have also been 13 consecutive quarters of double-digit, year over year declines in mortgage delinquencies[1]; do you know how that impacts your portfolio?

It is important to consider whether your current non-prime customers are behaving better than they were five years ago. A sampling of the TransUnion depersonalized credit database studied over 10 years revealed that more consumers are moving upward to better risk profiles. Credit risk score distribution, as shown here, details the growth of near prime, prime and super prime risk tiers to levels equivalent or higher than those in 2006. The subprime tier has decreased to levels lower than 10 years ago, showing that more consumers are managing credit better than they have in the past.



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[1] TransUnion's Q3 2015 Industry Insights Report

[2] Barkworth, Hazel. "Six Trends That Will Shape Consumer Behavior This Year" Forbes. February 4, 2014.

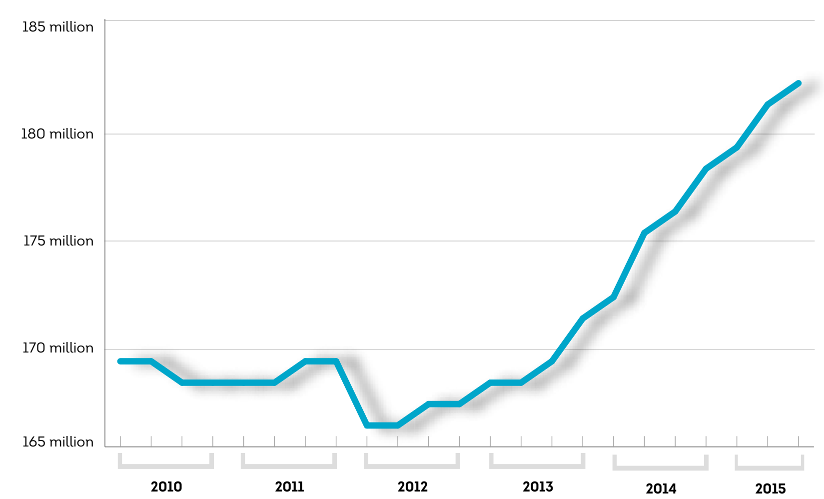
[3] Fromm, Jeff. Garton, Christie. "Marketing to Millennials" 2013.

More consumers are gaining access to credit

As the economy improves and the credit landscape changes, we must also consider the number of consumers with access to an open revolving line of credit. From Q3 2014 to Q3 2015, the number of consumers in the market with access to a revolving line of credit has increased by approximately six million, as indicated in the chart below. This is an incredible surge in a short time that could mean growth in your portfolio when proactively addressed.

With an increasing volume of consumers gaining access to credit, lenders should regularly review portfolios to better understand the trajectory of all accounts, in order to create optimal risk strategies. Identifying portfolio trends grants the ability to cater to those who might be eligible for a credit line increase or other applicable offers.

NUMBER OF CONSUMERS WITH ACCESS TO AN OPEN REVOLVING LINE OF CREDIT

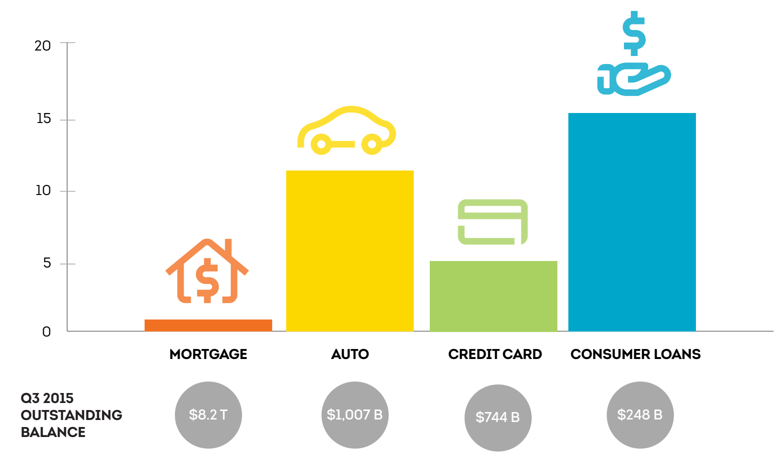


Source: TransUnion Consumer Credit Database

Dynamics of growth

TransUnion's Q3 2015 Industry Insights Report detailed a steady decline in average revolving balances since 2010, with total average balances falling over $4,000 in five years. There has also been a stable debt level on non-revolving balances, with the average balance per consumer decreasing from over $125,000 to below $115,000 in that same time frame.[1] However, as average personal income and consumer confidence have increased,

Q3 2015 YEAR-OVER-YEAR BALANCE GROWTH



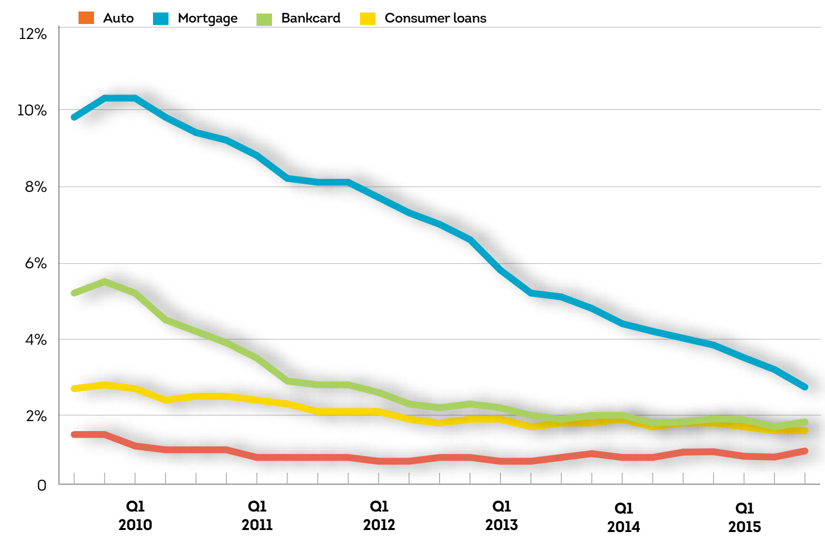
Source: TransUnion Consumer Credit Database

personal consumption has benefited. With the confluence of higher consumer optimism on borrowing and improved credit performance, the volume of consumer credit balances grew for mortgage, auto, credit card and consumer loans, as indicated in the chart above.

[1] TransUnion's Q3 2015 Industry Insights Report

To date, as illustrated in the chart below, delinquencies are stable for credit cards and personal loans, but still decreasing for mortgage, and have been at consistently low levels for the last five years in auto. Some sectors have

60+ DAYS BALANCE-LEVEL DELINQUENCY RATES



Source: TransUnion Consumer Credit Database

recovered faster than others, and auto is one of them. The most recent figures available reveal nearly 7.5 million new auto loan accounts in Q2 of 2015, an increase of approximately 500,000 new auto loans from Q2 of 2014.[1] Even taking into account seasonality with auto finance lending, we see there has been steady growth year over year. From the consumer level perspective, the Q3 2015 Industry Insights Report detailed that the number of consumers with an auto loan balance has increased steadily year over year since Q3 of 2013. Between Q3 2014 and Q3 2015 alone, the total number of consumers with an auto loan balance increased by approximately 8%.[1]

With low default rates—supported by a robust job market, low interest rates and consumer confidence—auto lenders are feeling confident about extending credit to more borrowers. Research also shows that auto loans are the most prioritized payments and reflect the lowest delinquencies compared to other lending products. These data points provide further insight into how many people are taking on debt and the kind of debt. How well-positioned are you to accommodate the credit needs of your customers?

Addressing account shifts in either direction

Most portfolios have a specific range of credit risk where accounts are commonly the most profitable. As a general rule, this sweet spot for the majority of banks and credit unions is the near prime risk segment. The near prime group carries balances, makes reliable payments and generates occasional fees for minor delinquencies. What is the sweet spot in your portfolio and what changes are trending in your book of business?

For instance, an increase in the proportion of highest-risk customers can indicate red flags for your policies. Overall, the economy continues to grow and consumers are gaining access to credit, but according to TransUnion data, there were over 11 million new collections accounts reported in Q3 of 2015. However, collections are down from previous years.[1] Nevertheless, some individuals can have a bad year and it is important to determine opportunities for tighter management of risk. Portfolio reviews can help identify customers exhibiting riskier behavior, in order to more actively manage and adjust loss forecasts.

Conversely, disproportionate growth in the number of lowest-risk customers could signify overly conservative business rules and lending practices, which may be diminishing returns on your portfolio.

[1] TransUnion's Q3 2015 Industry Insights Report

Likewise, the biggest opportunity to increase profitability could be in looking at the numbers of accounts with an upward trend in credit score. Customers who have shown responsible use of credit could warrant an increase in credit line or a change in the product pricing structure to better accommodate their needs.

We've been able to identify changes in the risk levels to see who has improved and moved into a higher tier, as well as which members have had challenges. Utilizing the right tool has helped us improve efficiencies and determine where there are opportunities to create more long-lasting relationships with our most profitable members by providing the right offers at the right time.

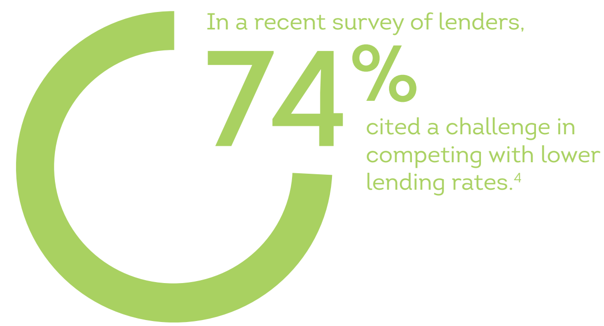
– South Bay Credit Union

Staying competitive

The new financial and credit environment requires adapting to changes in the market with a more competitive portfolio management strategy. Keep in mind the data presented thus far – delinquencies and collections are down from previous years, while credit access has increased.[1] Proof of lower delinquencies means people are paying on time – an indication of better management of financial commitments.

On the flip side, low delinquency levels do not mean you can sit back and relax. Low delinquencies could mean that some of your customers or members could be appealing to other lenders. You can stay competitive by identifying the right customers with more consistent portfolio reviews. Are you currently taking a strategic approach that creates lasting relationships?

Executing risk and growth strategies by looking at your portfolio regularly and making adjustments not only helps you stay on top of regulatory requirements, but also helps build customer loyalty for life. Consider the credit risk score migration chart from page 2 – understanding credit shifts and customer credit usage makes way for quick but appropriate reactions in adjusting offers. Lenders can benefit from using regular portfolio reviews to establish stronger customer relationships.



TransUnion research found that once consumers identify their preferred credit card–known as their 'top of wallet' card–they remain quite devoted throughout the year. In order to be top of wallet or to stay in wallet, lenders must consider a more competitive approach by providing the right offer or product based on current information.

Building loyalty and protecting against attrition

When an individual changes his or her credit behavior – whether positively or negatively – this change in behavior is not always distributed equally across all accounts. For example, an individual with affinity to a credit union or

[1] TransUnion's Q3 2015 Industry Insights Report

[4] Versta Research & TransUnion, "The State of Alternative Data" Survey Report, 2015.

preference for one account may continue to perform well on that account while others deteriorate. By the time the situation is recognized, it may be too late to take corrective action. This can lead to unanticipated losses particularly for credit unions and community banks. With regular portfolio reviews, the possibility of such scenarios may be reduced. This gives you the opportunity to review the consumer's account more thoroughly, and if warranted, make preemptive changes to limit exposure.

In a time of evolving consumer behaviors, it is critical to know how your portfolio is trending in order to best evaluate customer credit needs. By conducting portfolio reviews regularly, you can get more insight into the potential for attrition or the drivers of attrition if it has already happened. A portfolio review can quickly and objectively quantify the level of attrition risk contained in your portfolio at any given time.

The customer journey is a series of questions that must be answered.

Lenders want to retain long-term relationships and loyalty with their customers, but doing this requires quantitative portfolio knowledge. Simply measuring the raw numbers of accounts that are 30, 60 or 90 days past due has limited predictive ability. It doesn't tell you the likelihood that any sub-segment of accounts will further improve or degrade. It offers no insight into what proportion of accounts might warrant different credit offerings or loan pricing.

Take action

Portfolio performance, including both profitability and loss rates, directly correlates with how well you identify, anticipate and manage fluctuations. With regular account insights, you can make better-informed decisions about any further action you might need to initiate in your portfolio. A portfolio review shows your current balance of high-risk accounts against those that are low-risk, opening the door for more insights to change, whether positive or negative. These changes can occur swiftly and on a monthly basis, which a yearly review would miss. Perhaps a large portion of your customer base spends more during the back-to-school season than during the holidays. Which is it? You won't really know until you look. But that look will reveal critical information that may help you make more informed decisions.

TransUnion's 2016 Forecast noted that prime consumer demand and increased supply from new entrants in the consumer loan market are expected to increase average consumer balance while delinquencies remain low. In the mortgage market, delinquencies are expected to scale back to pre-recession levels and average consumer balance is expected to follow with the confluence of rising home values.

Consistent portfolio reviews are a reiterative analysis that will better serve the dynamic credit cycle. They can also help track and identify changes in your risk composition that could impact profitability– either positively or negatively. With regular portfolio reviews, you can watch trends over time in order to make more profitable decisions, staying competitive and building loyalty along the way.

Questions?

For more information on TransUnion's portfolio review solutions, please call **844-245-4071** and choose option 3.

MONITOR RISK TRENDS EACH MONTH

Quick, effective and consistent process

Easily identify accounts where action should be taken

Measure risks unique to each customer and portfolio