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Midtiers Need a Holistic Risk Management Strategy



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The midtier banking market is feeling the impact of a volatile U.S. economy.

Despite the fact that many have historically used conservative underwriting standards and prepared their balance sheets for a difficult period, they are not immune to the effects of the deteriorating economy. Delinquency and chargeoff rates are increasing across the board, and the cost of acquiring and managing profitable customers is escalating in tandem with rising losses, resulting in thinner profit margins.

Faced with such a challenging lending environment, many midtier institutions are recognizing the need to get back to the fundamentals of risk management.

Siloed and inconsistent risk practices across business units is often a contributing

factor to the increase in delinquency and charge-off rates. This lack of consistency hinders cross-selling and hides the true extent of risk exposure. For example, a lender might pursue collection efforts on an auto loan while raising a credit card limit for the same customer, simply because data and strategies are not being shared.

Institutions should consider a holistic approach to risk management both in terms of customer life cycle and product type. Here are some best practices.

- Revalidate risk-based lending strategies on a regular basis. By conducting a simple retrospective analysis, a bank can determine the score and/or score combinations that are most effective at separating accounts that perform well from those that do not. Banks can gain even more insight by incorporating a segmentation analysis. This granularity can allow an institution to further isolate pockets of strong accounts by identifying specific credit characteristics that are performance drivers.

Together, these analyses provide a solid basis for acquisition or portfolio management strategies tailored to meet risk tolerance levels.

- Identify high-risk populations from a geographic perspective. The previously mentioned analyses will isolate credit characteristics needed to identify these populations. However, today's economy

presents a geographic risk component that is difficult to dismiss. Banks should evaluate delinquency trends and forecasts within certain areas as they consider adjustments to their account management strategies and optimize resource allocation.

It should be noted that geographic analysis should be approached with caution and in partnership with your compliance department, to avoid redlining and other disparate impacts.

- Develop proactive account management and collection strategies. Portfolio reviews and event-based portfolio management strategies can become the backbone of effective account management.

As more delinquencies move to the chargeoff stage, banks may want to consider models and strategies designed to increase recoveries and reduce third-party expense.

With a sound risk management strategy in place, banks can turn to re-evaluating their growth strategies. Just as risk managers are adjusting their focus from account acquisition to portfolio management, so should marketing managers increase the emphasis on cross-selling and retention as conservative avenues for growth.

Inevitably, the economy will turn for the better, and when it does, your institution should be positioned to take advantage.

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