



Thriving in a Higher-Risk Environment

Strategies for Lowering Risk and Lifting Revenue, Even in a Difficult Economy

By Andrea E. Glanz

Energy prices are soaring as house prices collapse. Paychecks are shrinking as profits plummet in financial centers around the world. Consumer spending growth has run out of steam across many sectors, and as spending goes, so goes the economy. It's no wonder that credit card portfolio managers are worried—as they watch credit card charge-off rates trend upward and bankruptcies surge. What should banks and card issuers do?

This issue of *The Advisor* helps you answer that question. We asked MasterCard Advisors' experts in risk and operations management, portfolio optimization, and commercial strategies to provide their perspectives on how to ride out the storm. We offer timely insights into changing consumer

behavior and strategies to better manage risk, stem attrition, and find alternative paths to growth.

If you believe this downturn is different, you're right. Client Business Leader Ramsey El-Assal and Risk Management Global Practice Leader Edmund Tribue argue that each credit crisis has unique characteristics, and that this one is fundamentally different from earlier recessions. In their article, "'Won't Payers' Raise the Risk of Default," El-Assal and Tribue warn that many more consumers are becoming "Won't Payers." Faced with mortgage obligations greater than the value of their homes, they are choosing to pay some debts and forego others. This change in consumer behavior makes it difficult for banks to detect and manage cardholder risk. The authors offer practical advice for identifying worrisome consumer behaviors,

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proactively addressing at-risk cardholders, reevaluating your risk models, and improving forecasting.

How does this growing group of defaulters affect your credit card portfolio? Advisors' risk management experts Rick Openshaw and Tommy Lee believe issuers need to rethink their credit risk strategies. Rather than relying solely on blunt tools like credit scores, they advocate monitoring cardholder behavior and using qualitative and quantitative measures to evaluate each cardholder individually. Only then will you have the insight needed to effectively adjust credit lines, pricing models, risk scores, and collections management tactics. Openshaw and Lee provide numerous examples of issuers who have used these approaches to better manage delinquencies, stem charge-offs, and maintain profitability.

Higher levels of attrition are another side effect of the current environment. MasterCard Advisors' Regional Business Leader Bill Saubert describes an engagement with a top Australian bank that was facing excessive customer defections. Realizing that its CRM strategies, tools, and systems weren't enough to insure customer loyalty, bank executives began asking tougher, bottom-line questions: How much should we invest in a customer who is not likely to leave, or who is not currently profitable? How much should we invest in a customer who is not currently profitable, but could be in the future? Advisors built sophisticated propensity models to determine which customers were most likely to defect, then developed a way to measure expected profitability for each customer, both current and future. The bank was able to more accurately gauge just how much profit it might potentially lose from each customer, readily identify its most valuable customers, and actively work to retain them. Thoughtful analysis led to important insights—and a 22 percent drop in attrition, along with increased profits.

Rounding out this issue on strategies for a higher-risk economy, Advisors' Commercial Segment Global Practice Leader Michael Carbone makes a compelling case for seizing the small business market opportunity. In the U.S. alone, more than 25 million small businesses spend nearly \$5 trillion each year, yet less than 10 percent of those payments are captured on cards. One of the few card markets still growing by double digits, small businesses outspend consumer cardholders, carry larger balances, and are more profitable. Best of all, likely prospects are often already customers of your bank—they just haven't signed up for a small business card yet. Carbone describes how to identify the most attractive segments of this market, match your value proposition to their specific needs, and reach your prospects efficiently, utilizing such channels as retail branches and the Internet.

In these uncertain times, issuers know they need to uncover opportunities to boost revenue, reduce risk exposure, better manage delinquencies, and cross-sell profitable products. *The Advisor* offers payments executives bold thinking and innovative approaches that can help them avoid dangerous pitfalls—and accelerate results. ●



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