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*Lenders Can
Reduce Credit
Card Write-Offs By
Knowing Who
They Are Dealing
With*

GIVING CREDIT WHERE CREDIT IS DUE ... AND NOT

Panicked by the prospect that credit cards defaults could rival those of the mortgage meltdown, banks are taking adverse actions and initiating aggressive recovery programs against borrowers at an unprecedented rate. Our analysis says this is the wrong path to take.

All delinquent borrowers are not created equal; they differ in both their ability to pay and their willingness to do so. Once lenders know where a debtor stands, they can determine when, how, and what to do to maximize not only collections, but the probability that delinquent borrowers can be returned to performing, paying, and loyal customers with the minimum amount of adverse action.

So where do borrowers fit? In general, there are four types:

- **On the Edge, but Not Over.** These are good customers whose behavior sends up a sudden red flag. An adverse action against a good customer, particularly one not in delinquency, is a breach of trust that's difficult to repair. It drives customers to competitors, ruins brands, and kills performance, so it's critical to be able to identify good customers who are going to pull back from the brink without draconian measures.
- **Recoverable.** Some responsible borrowers would repay if they could. Spurred by the economic recession, this group is larger than ever before, right now representing 20-25% of defaulted loans. Applying standard dunning techniques to these people will garner only pennies on the dollar and potentially lose you far more important things: their goodwill now, and their business when they recover (as they are almost 100% certain to do). A smarter approach uses thoughtful, customized programs that nurture good-customers-gone-bad back to financial health. We have found that handling recoverables with sensitivity and care delivers more than 2½ times the money as heavy-handed approaches. Lenders also earn the loyalty of customers, who appreciate the bank standing by them in difficult times. Plus, returning good customers to the economy is a significant beneficial by-product to everyone.
- **Non-Starter.** Among customers who wind up defaulting, 34% will never ever pay anything. The key here is to ensure these customers don't take up scarce internal collection resources. Their cases need to be closed quickly and their files moved to external agencies. Doing so can free up 10% or more of a bank's collection capacity, allowing resources to be focused against accounts with higher payback potential.
- **Just Need a Nudge.** 20% of defaults will cure with minimal intervention. Don't use expensive channels like a personal collection call when a letter or text message will be just as effective.

The key is to identify where each individual fits – but in a sea of defaulting credit card customers and a fast-changing, complex economic environment, that's not such a simple task. What can help: using more sensitive and flexible segmentation models that incorporate very recent behavioral data along with the pattern of customers' relationships over the long term, and employing good old-fashioned business judgment. Knowing what type of debtor a lender is dealing with can point the way to detailed contact and collections strategies that improve recoveries, foster loyalty, and support higher profits in the long term.