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Hello

Welcome to another edition of Euristix Insight, our newsletter which seeks to deliver unique insight and information in the changing world of credit and portfolio management.

This edition's lead article discusses the impact of the current decline in house prices on lenders' capital requirements and suggests actions that can be taken. The thought-provoking 'Questions Corner' invites you to think about generating value from your portfolio in the current turmoil surrounding the credit industry. This edition also offers information on how DCAs can harness the power of credit bureau data (white data) in order to achieve best practice in collections.

Please contact us with any questions. We also welcome any feedback you may have.

Kind regards,

Chris Kemp



In this edition...

Basel II and the Impact of Falling House Prices - Our lead article explores the tools and methodologies which can be used to ensure understanding of future capital costs and profitability, particularly in light of falling house prices.

Questions Corner - In this edition we ask just how well you know your portfolio and where value can be generated.

Using White Data to Enhance Collections - White data can be used to help you understand debtors' circumstances and tailor your actions for each debtor to benefit from this. It can also help to prioritise your collections activities. Our article on 'Achieving Best Practice' explains how.

Basel II and the Impact of Falling House Prices



The transition to Basel II at the start of this year was an important change to the way banks are regulated and more specifically the way in which capital requirements are set. The continuing decline in UK house prices has highlighted the impact of this regulatory change on mortgage lenders who have adopted the advance approach under Basel II. As house prices continue to fall the amount of capital required has increased as a direct result. This is impacting not only the profitability of the banks but also the wider UK economy as mortgage lenders restrict LTVs and increase product rates.

Lenders need to understand both future capital costs within their portfolio and future profitability to inform lending and strategy decisions today. This can be provided by account level forecasting tools that use customer and product characteristics as inputs along with macro economic factors. These tools can provide a unique insight into how capital is allocated in a portfolio and the dynamics with profit. For more detail please read the [full article here...](#)

Questions Corner - Understand Value Generation

It is more vital than ever to understand the value contained in your portfolio and to identify where this value is being generated and destroyed. Consider how your business measures up to the following questions:

- Do you have an accurate and up-to-date view of the true value of your portfolio?

- Do you fully understand how external and internal changes dynamically affect this value and to what extent?
- Do you understand if any parts of your portfolio are destroying value and what actions you can take to correct this?
- Is the entire lifecycle, from marketing to collections and debt sale, managed based on value generation aligned with supporting business targets rather than single performance measures?

A future edition of Euristic Insight will provide more information on ensuring a value generating management paradigm is embedded in your business but in the meantime, please direct any questions to chris.kemp@euristix.com

Achieving Best Practice - Using White Data to Enhance Collections

Opportunity - Recent changes in regulation have granted Debt Collection Agencies access to positive credit bureau information, known as white data. A key application of this data can be to improve the understanding of customers and thereby tailor collections strategies to enhance performance. To understand the potential benefits of white data and the business case for sourcing it, you need to answer the following key questions:

1. How does white data help me better understand my debtors' circumstances, and how can I therefore tailor my actions and conversation to benefit from this increased understanding?
2. How can white data help me prioritise my activities so that I focus on segments that are likely to provide the highest return?

Approach - Whilst the temptation may be to immediately start mining the white data to gain additional insight into customers' circumstances or likely behaviour, this is not necessarily the first step. To begin with, you should question whether you currently make the best use of all the internal data available to you – i.e. have you maximised the use of all the 'free' sources of data, such as information passed with the debt at take-on. Rapid benefits can frequently be obtained through simple segmentation using readily available characteristics such as product type, customer age, balance and past payment behaviour, which can provide the basis for an initial segmentation of debtors, allowing application of enhanced collections treatment strategies.

As there is typically a cost involved in sourcing and integrating white data, it is sensible to ensure that you extract maximum value from your own data first, after which the use of white data can create further benefits.

Whether you decide to source white data or use internal data exclusively, you will need to think carefully about what you want to achieve and how you want to implement the outputs of your analysis into your operations, as this will drive the choice of the analytical approach to be taken.

- If you require actions and messages tailored to customer circumstances, this can be achieved through easy-to-interpret segmentation.
- If the requirement is for higher productivity through better prioritisation, then scoring techniques are best placed to rank accounts by likely probability of repayment. However, this will not provide insight into individual debtor circumstances.
- A combined approach can prove useful to pick out core segments for which targeted actions can be taken, with scoring techniques used to prioritise activity on the remaining segments.

For each of these options, it is important to maintain close collaboration with operational teams at an early stage in order to ensure that the output of the work is well understood, and agreement is reached on how best to apply these results and changes in an operational environment.

Analysis - The initial step of the analysis requires the selection of a sample of previously worked accounts and the assignment of a positive or negative outcome to each account. The outcome definition must provide a robust indication of whether or not the account has performed in accordance with some predefined criteria. This can be something as simple as noting whether a payment was made or as complex as identifying a correlation between recovery costs and payments received.

In addition, it is important to ensure that enough time has been allowed for a mature outcome to be observed.

To fully understand the value of white data, a retrospective bureau sample should be obtained to provide the white data characteristics for each customer at the point the collections process started. This will allow analysis to be undertaken to identify which characteristics are indicative of either a good or bad outcome.

Having identified the most useful internal and/or white data characteristics, a combination of segmentation and scoring techniques can then be applied to build enhanced collections strategies. Finding the best possible method may take a series of iterations and the use of a test and learn approach. This could involve implementing a challenger strategy which can be closely monitored and fine-tuned to provide the final insight required. Typically, useful white data information will include indicators of up-to-date or new performing credit accounts, recent credit searches, signs of emerging defaults and stability at an address.

Implementation - Once the new segmentation strategy has been defined, appropriate sets of actions and tailored messages will be needed to complement this. In addition, if white data is to be part of the newly created segments, development will be required to implement and refresh this data within your existing operating environment. Finally, triggers should be introduced with actions to contact the customer again if certain white data fields change and show something new that has happened to the customer.

Experience suggests that significant uplifts in collection performance can be achieved through an enhanced analytical approach to segmentation and treatment strategy definition, and that the addition of white data to this process can provide further improvements through a more accurate understanding of customer circumstances.

Achieving a best of breed approach for using white data to support collections activities in a DCA or collections environment is a process of constant learning which requires a mixture of capabilities: business acumen, analytics and operational expertise. Other opportunities for white data lay in the improvement of tracing processes and the pricing of debt purchase. For more information on the Euristix approach to this developing area or for any more general queries, please contact johann.grennepois@euristix.com

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