

TransUnion®

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Life after Foreclosure and Hidden Opportunities

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Session overview

- While credit risk scores remain the best predictors of risk, certain consumers are more susceptible than others to the impact of external forces
- A clear understanding of how external forces might influence those consumers is therefore critical to lending to them successfully
- An analysis of consumer mortgage behavior during- and after the recent recession reveals segments of consumers who—precisely *because* of the nature of the recession—actually perform better than one would expect
- We quantify the improvement in performance and discuss how this concept might be incorporated into strategy

Credit scores are great predictors of risk, evaluating the net impact of the forces that act upon the consumer



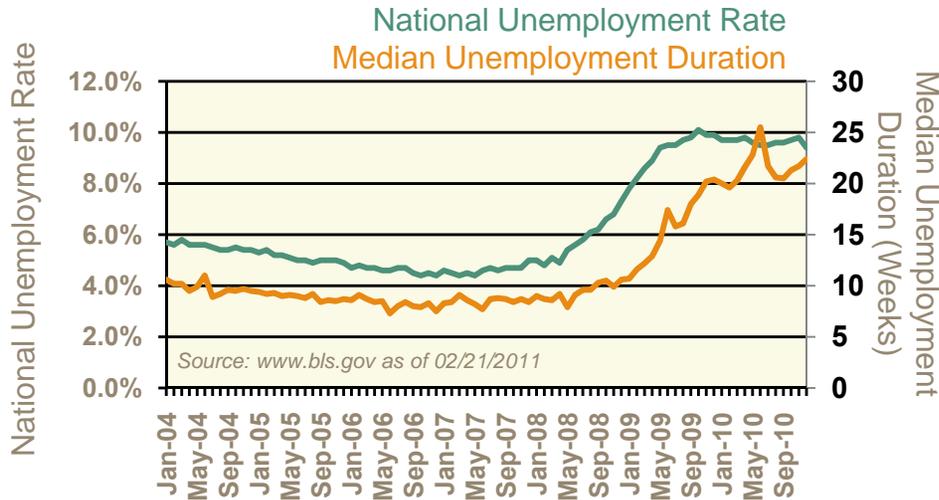
Yet some consumers may be impacted more by external forces than the norm during severe economic turmoil



	2005	2010
Income	Senior Engineer \$6,900 / month	Unemployed \$2,300 / month
Housing	Apartment Renter 	Homeowner 
Family	Wife 	Wife & 2 children 
Debt Burden	\$2,400 / Month	\$3,600 / Month

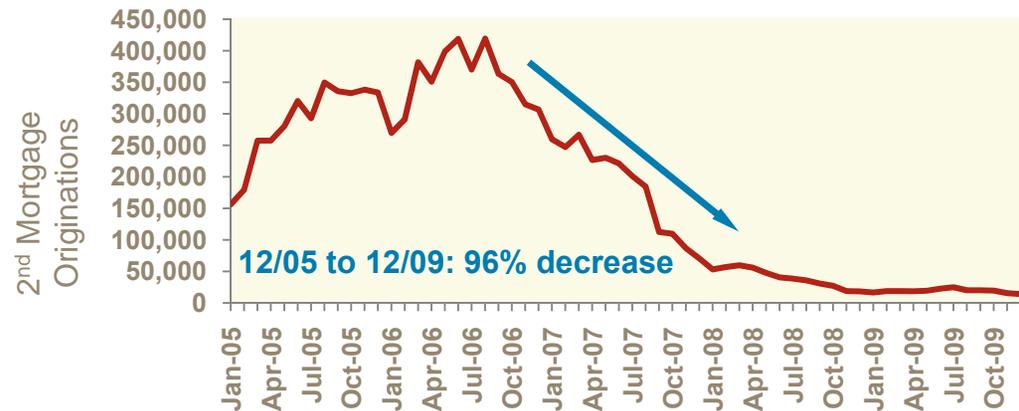
The forces exerted on consumers by the recent recession were quite severe

The unemployment rate doubled...



...and the duration of unemployment nearly tripled

Home value depreciation eviscerated the housing market



Source: TransUnion Credit Reporting Database



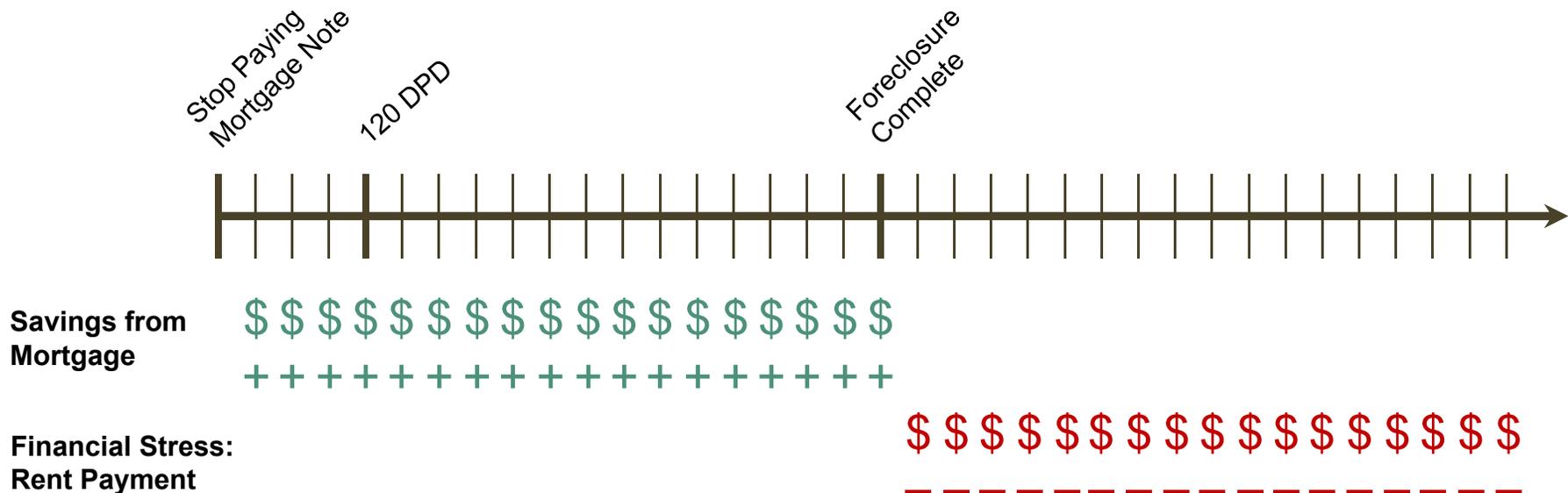
The resulting environment caused unusual behavior. We want to test two related hypotheses accordingly.

1. Defaulting on a mortgage causes temporary excess liquidity. This excess liquidity masks the true risk of the consumer as he goes through the foreclosure process.
2. Certain consumers who defaulted on a mortgage in the recent recession only did so *because* of the recession—they are otherwise good credit risks.

The ability to identify “life event” mortgage defaulters versus chronic defaulters can open up profitable, low-competition target segments

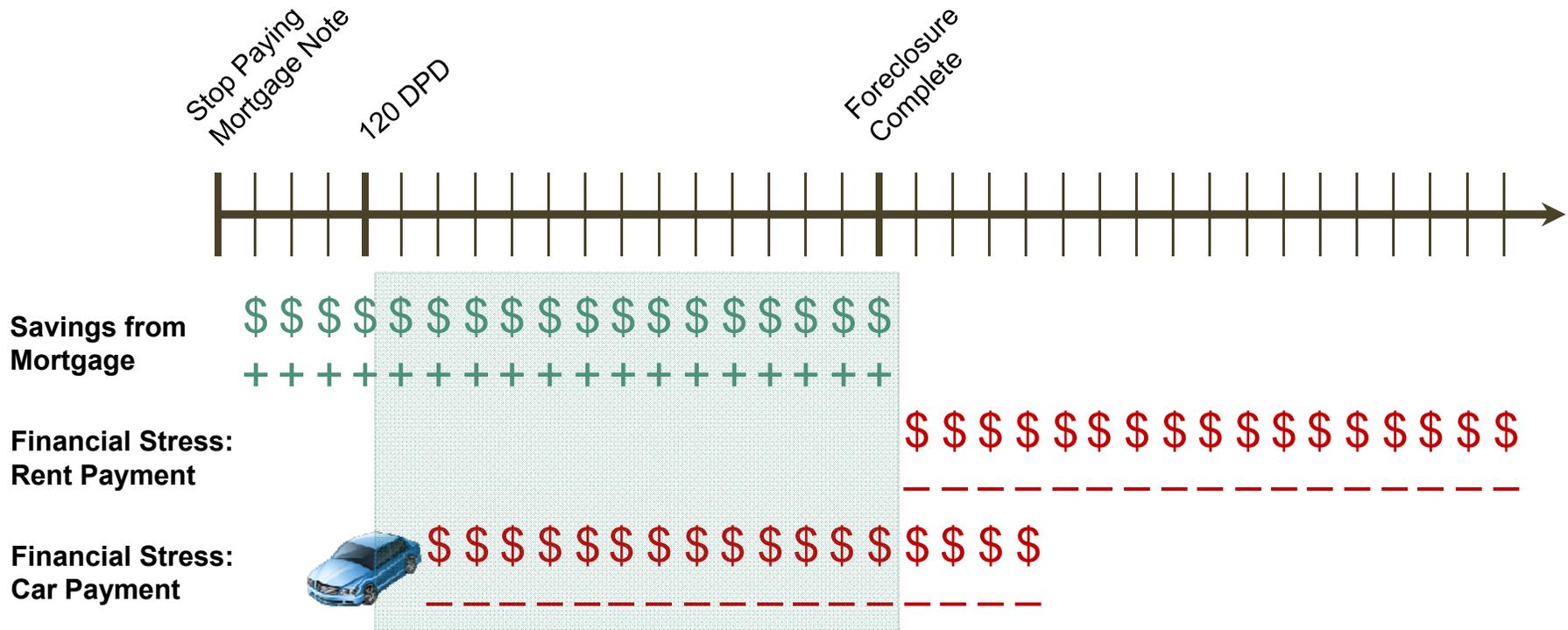
What is the theory behind temporary excess liquidity?

1. A consumer who does not pay his mortgage is saving all or most of the money he would have paid on the note, until he is evicted at the end of the foreclosure process.
2. This consumer only feels credit stress (if at all) once he has to start paying rent (or another mortgage).



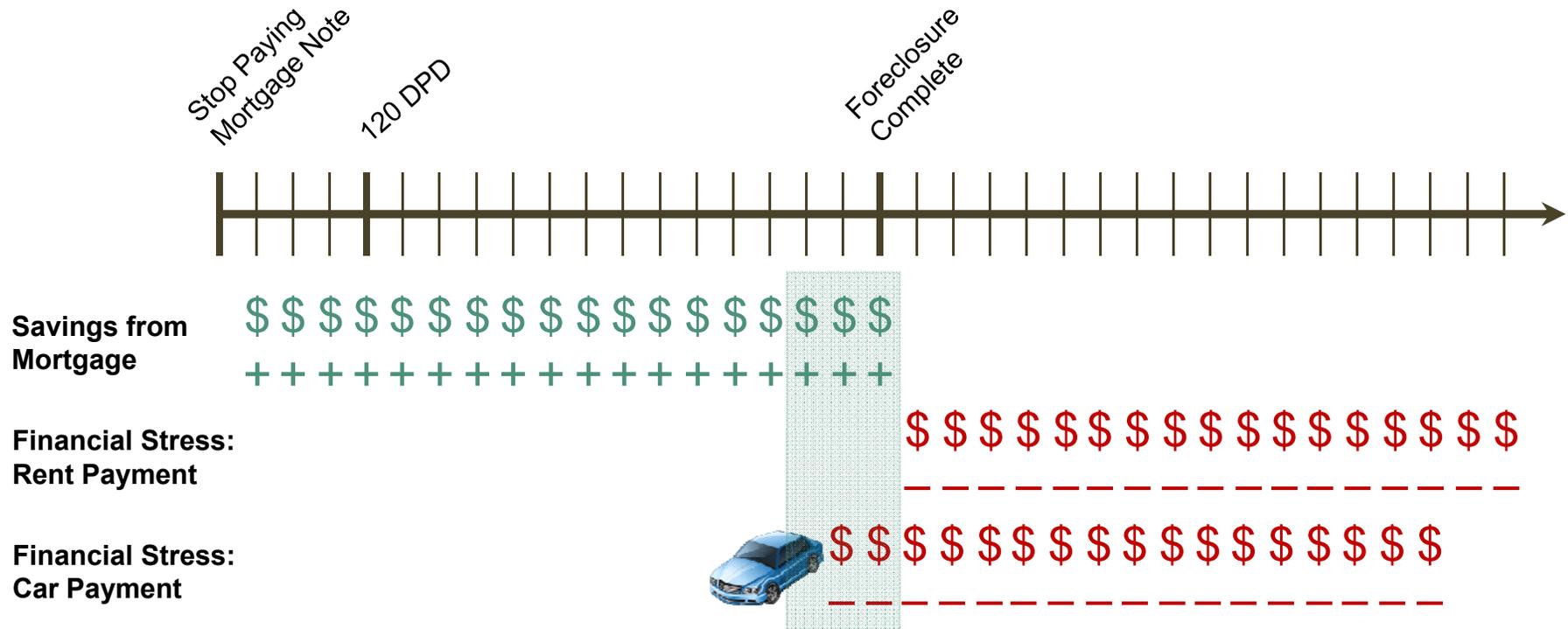
What does this theory mean in terms of other products?

- The consumer will not feel credit stress from any product already held or opened early in the foreclosure process because of the money saved from the missed mortgage payments. Only after the foreclosure is complete will he begin to feel credit stress.



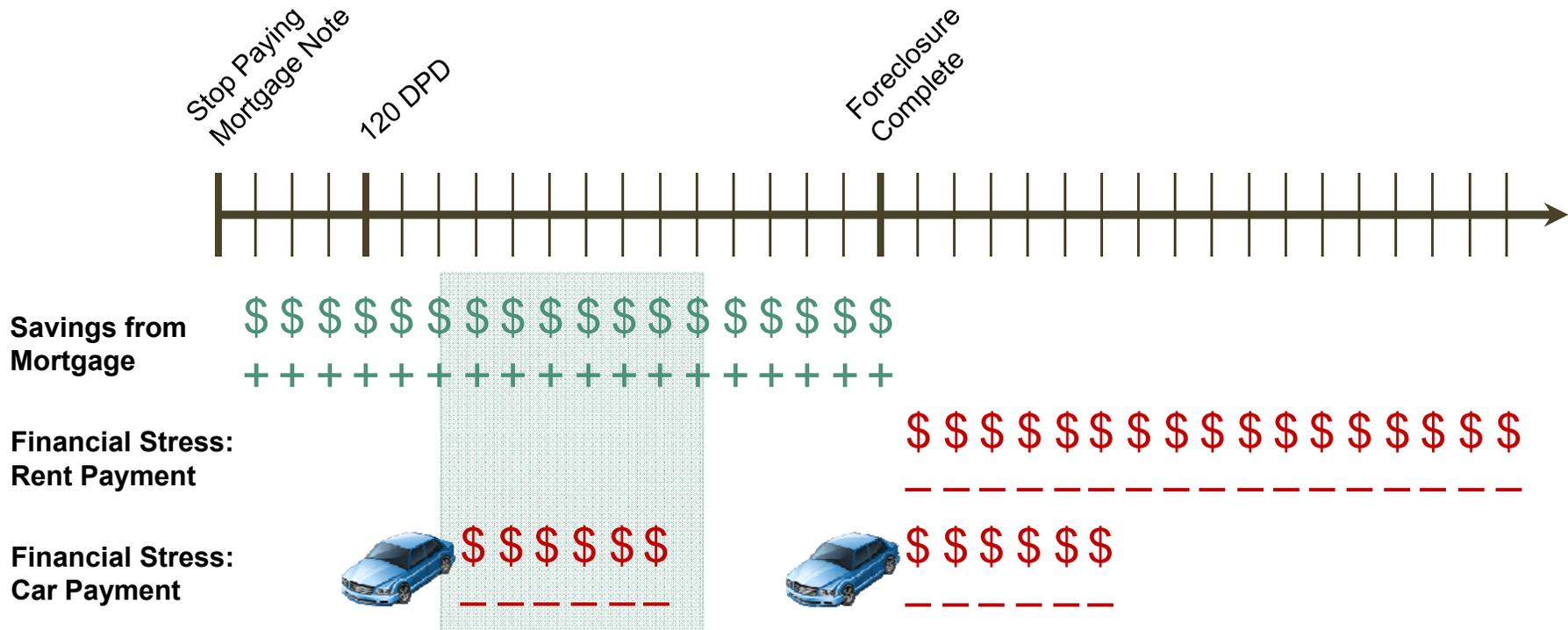
What does this theory mean in terms of new account timing?

- 4. The closer to eviction the consumer opens a new account, the less “protection” he has from saved mortgage payments and the more credit stress he will feel.



If the theory holds true, the effect would be quite clear over a short performance window

- The account opened earlier would have no additional credit stress, while the account opened later would have a lot of additional credit stress.



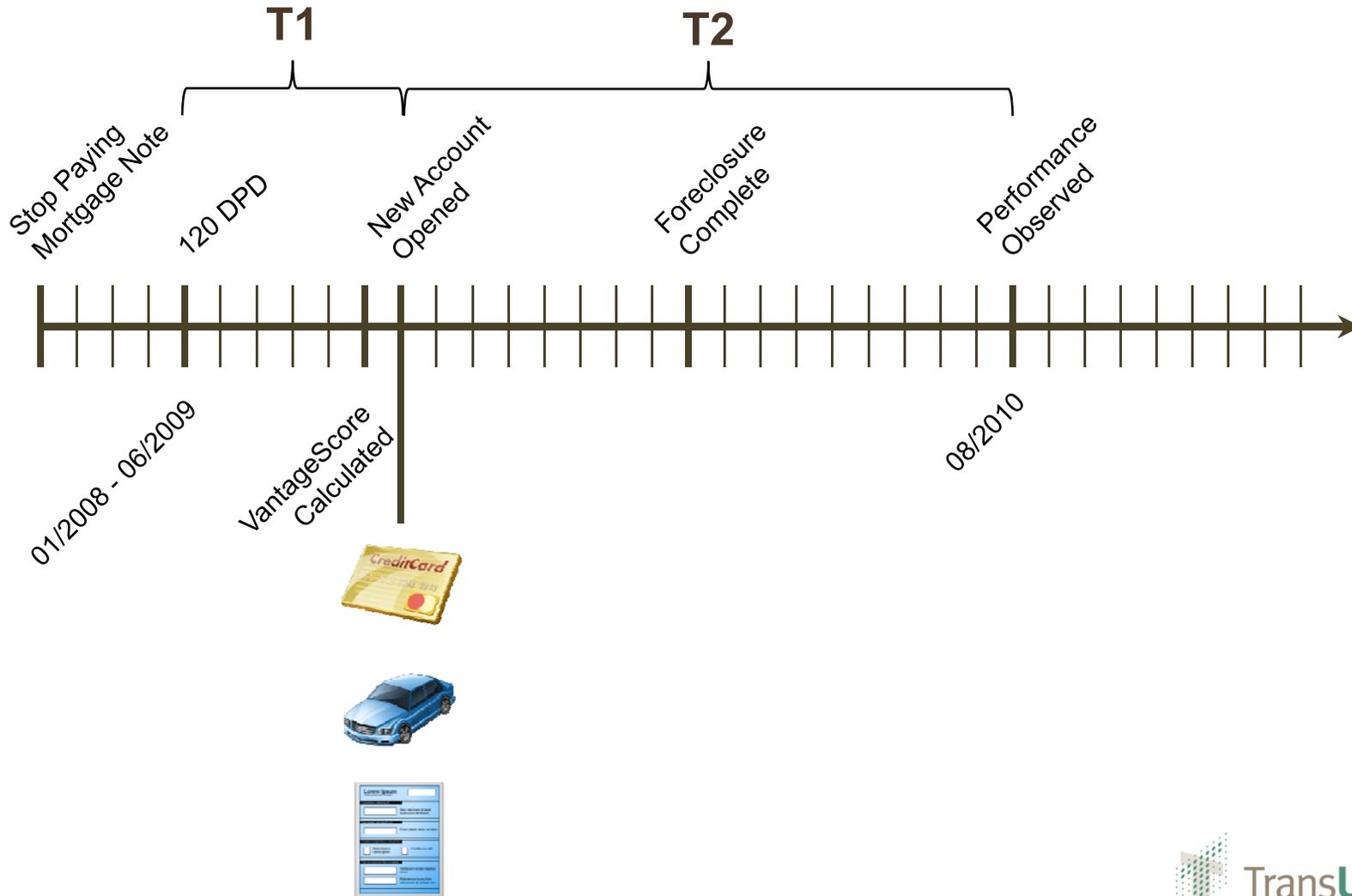
What does this theory mean in terms of delinquency?

- Accounts opened later in the foreclosure process are more likely to go delinquent than those opened early in the foreclosure process, and hence should exhibit higher delinquency rates over a fixed performance window
- This is why lenders are often hesitant to lend too soon to consumers with good behavior other than a mortgage default—it is believed the excess liquidity allows for temporary good performance

To test both hypotheses, we performed a “Life after Foreclosure” analysis

- Started with a random sample of 5 million consumers with an open MT trade in 01/2008
- Selected the subset who:
 - Had at least 1 non-MT trade open as of 12/2007
 - Went 120+ DPD on the MT trade between 01/2008 and 06/2009
 - Opened at least one additional trade after the MT went bad
 - This left us with ~129,000 consumers
- Evaluated the product mix for these consumers post-foreclosure
- Calculated each consumer’s VantageScore® in the month prior to the new tradeline opening
- Evaluated the delinquency rates of those new trades with 7-11 and 12-17 months of performance through 08/2010 (~65,000 new trades opened)

The study may be illustrated like this



We devised a nomenclature for the study

T1: The time between the mortgage 120+ DPD default and the opening of the new tradeline

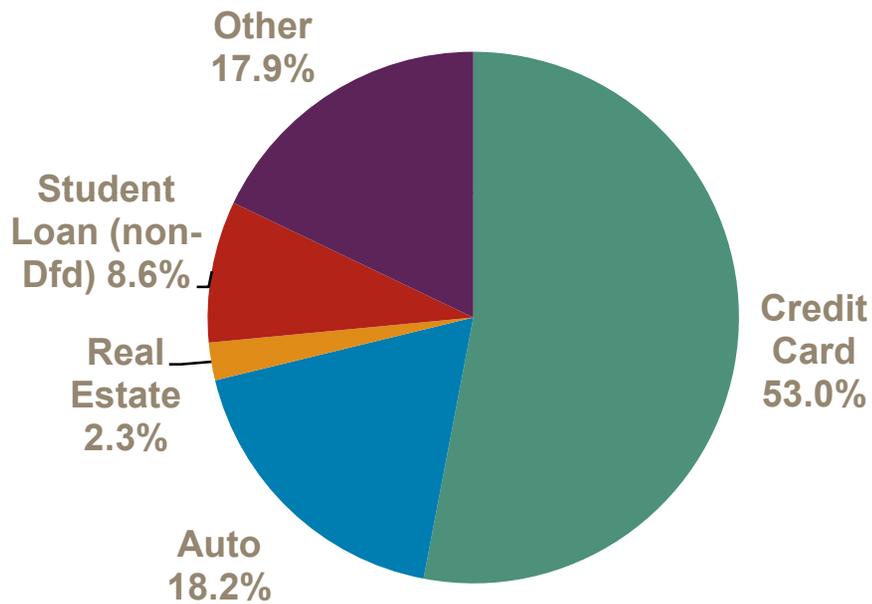
T2: The performance period of the new tradeline (generally, T2 = 12 - 17 months in this study)

MO: “**Mortgage Only**” A consumer who goes 120+ DPD on a mortgage but has **no other delinquent** existing tradelines at the time the new tradeline is opened

MD: “**Multiple Delinquencies**” A consumer who goes 120+ DPD on a mortgage but has **at least one delinquent** existing tradeline at the time the new tradeline is opened

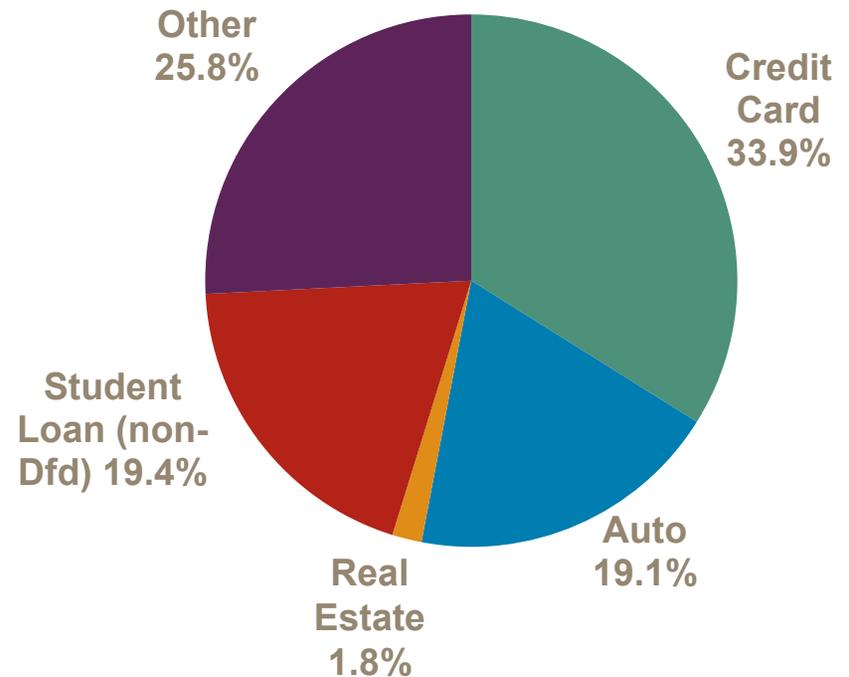
As expected, new tradeline openings were not uniform between MOs and MDs

Mortgage Only



N = 64,500

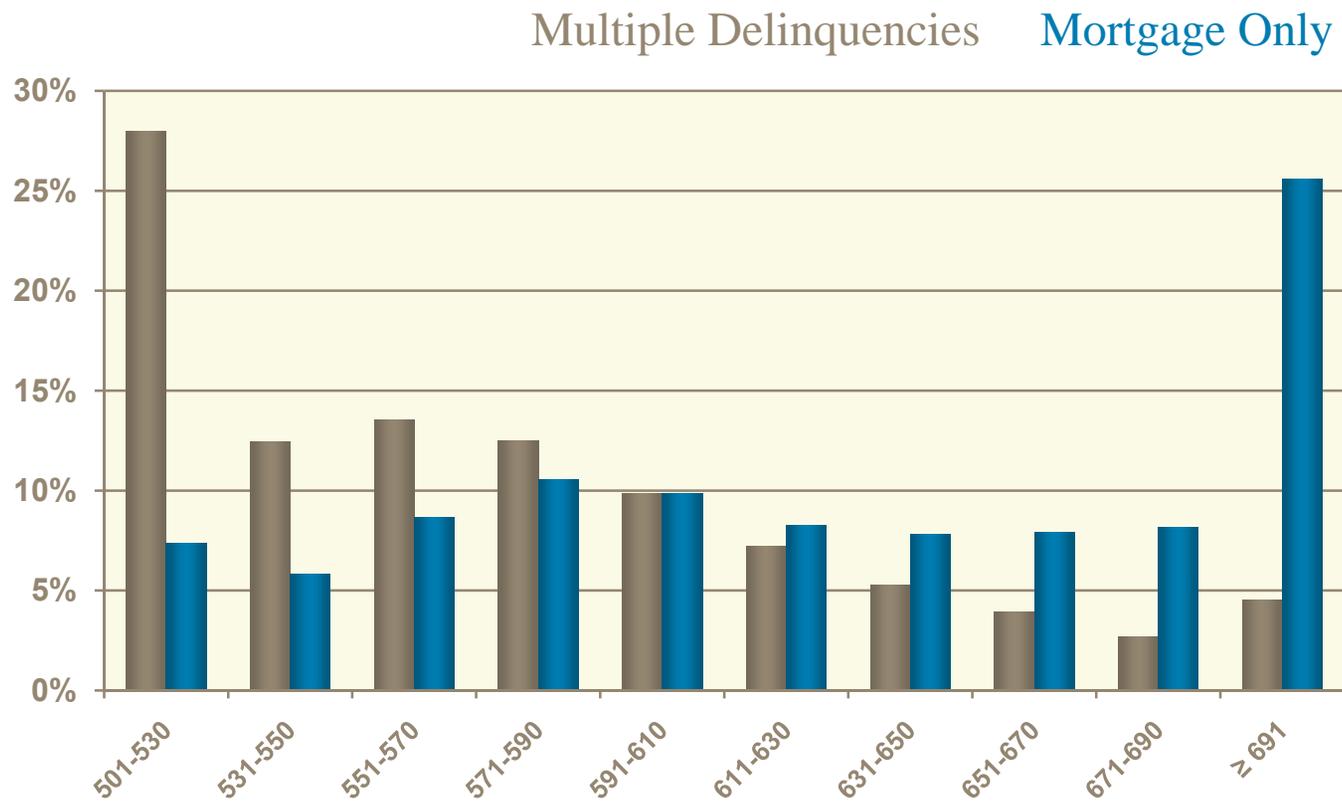
Multiple Delinquencies



N = 65,000

Nor was the distribution by score the same; the study controlled for this

VantageScore Distribution at New Account Opening



Result #1: The data do not generally support the “excess liquidity” theory

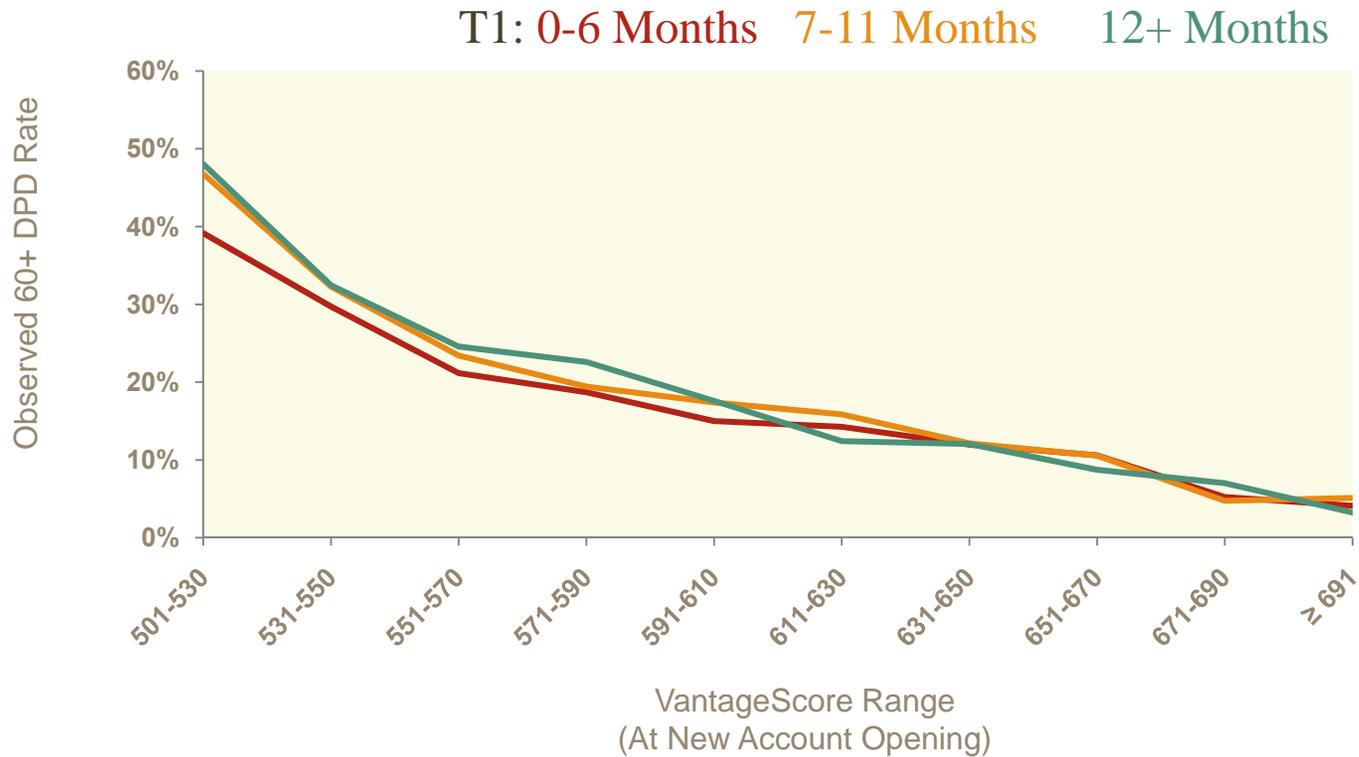
P(60+ DPD), Performance (T2) = 12-17 Months

Product	T1—Time to Opening of New Tradeline		
	0 - 6 Months	7 - 11 Months	12+ Months
Auto	10.4%	9.7%	9.3%
Other	18.9%	17.0%	16.4%
Credit Card	15.5%	18.5%	18.7%
Overall	18.8%	21.3%	20.5%

- Delinquency rates do not generally get worse over time
- Auto and Other loan types actually refute the theory
- While cards do show an increase in delinquency over T1, the increase from 7-11 to 12+ is *de minimis*. We do not discount these results, but we do not consider them conclusive.

This result holds true generally across score bands

60+ DPD Rates, All Products, Performance (T2) = 12-17 Months



Even for a short performance window, we do not see material evidence of an excess liquidity effect

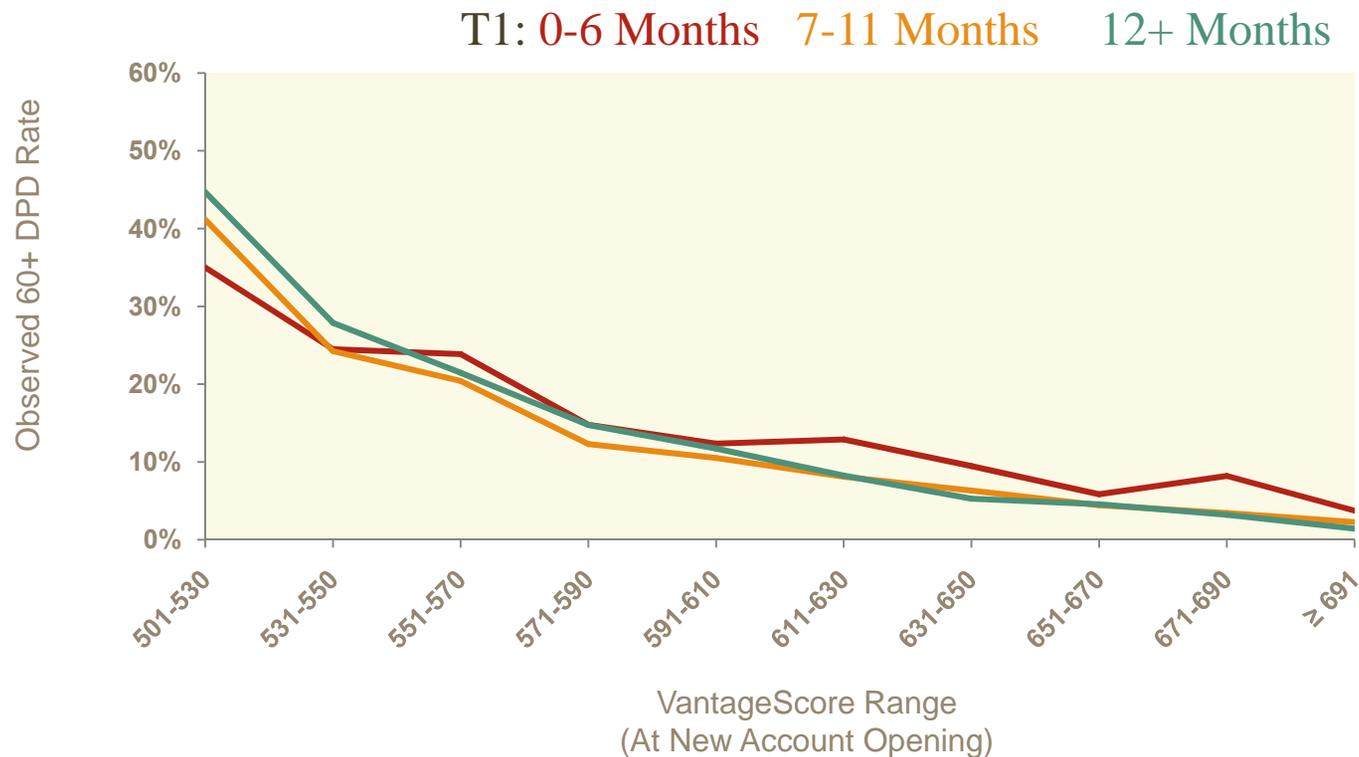
P(60+ DPD), Performance (T2) = 7-11 Months

Product	T1—Time to Opening of New Tradeline		
	0 - 6 Months	7 - 11 Months	12+ Months
Auto	5.7%	4.4%	4.6%
Other	12.4%	11.1%	10.5%
Credit Card	13.1%	9.3%	10.6%
Overall	14.8%	12.8%	14.5%

This is an important baseline finding, as any further results in the study should not then be attributed to an excess liquidity effect.

Again, the excess liquidity theory does not appear to hold up when evaluated across score bands

60+ DPD Rates, All Products, Performance (T2) = 7-11 Months



Result #2: An MO default during the recession indicates a better risk, regardless of when the new account opens

60+ DPD Rates, Performance (T2) = 12-17 Months

Auto	T1—Time to Opening of New Tradeline			
	0 - 6 Months	7 - 11 Months	12+ Months	Overall
Mortgage Only	6.6%	4.3%	6.0%	5.8%
Multiple Delinquencies	14.1%	14.0%	12.1%	13.1%

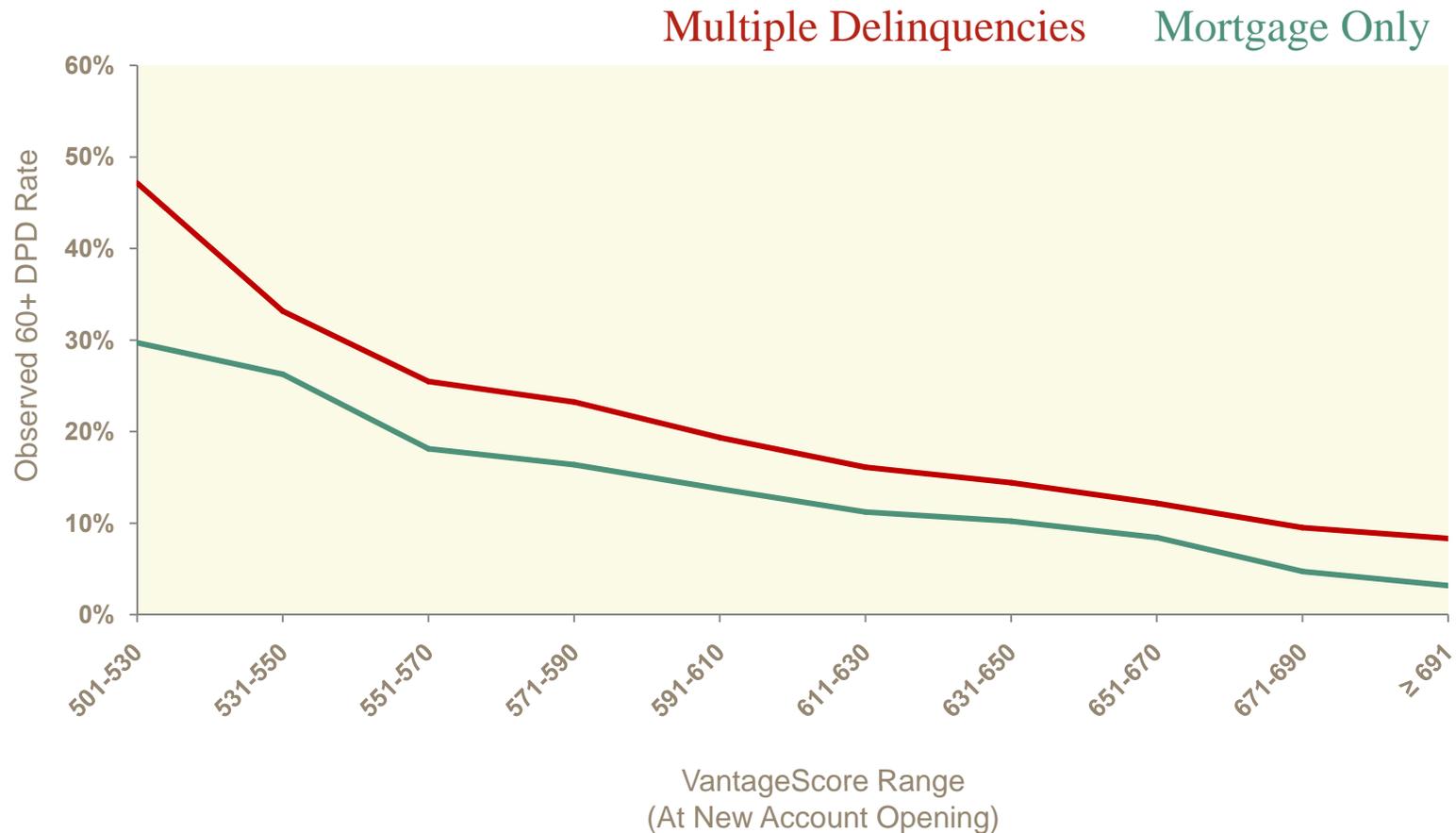
Other	T1—Time to Opening of New Tradeline			
	0 - 6 Months	7 - 11 Months	12+ Months	Overall
Mortgage Only	15.2%	13.2%	11.4%	13.1%
Multiple Delinquencies	21.2%	19.3%	19.8%	20.1%

Credit Card	T1—Time to Opening of New Tradeline			
	0 - 6 Months	7 - 11 Months	12+ Months	Overall
Mortgage Only	9.7%	11.9%	12.5%	11.4%
Multiple Delinquencies	26.5%	28.0%	27.0%	27.1%



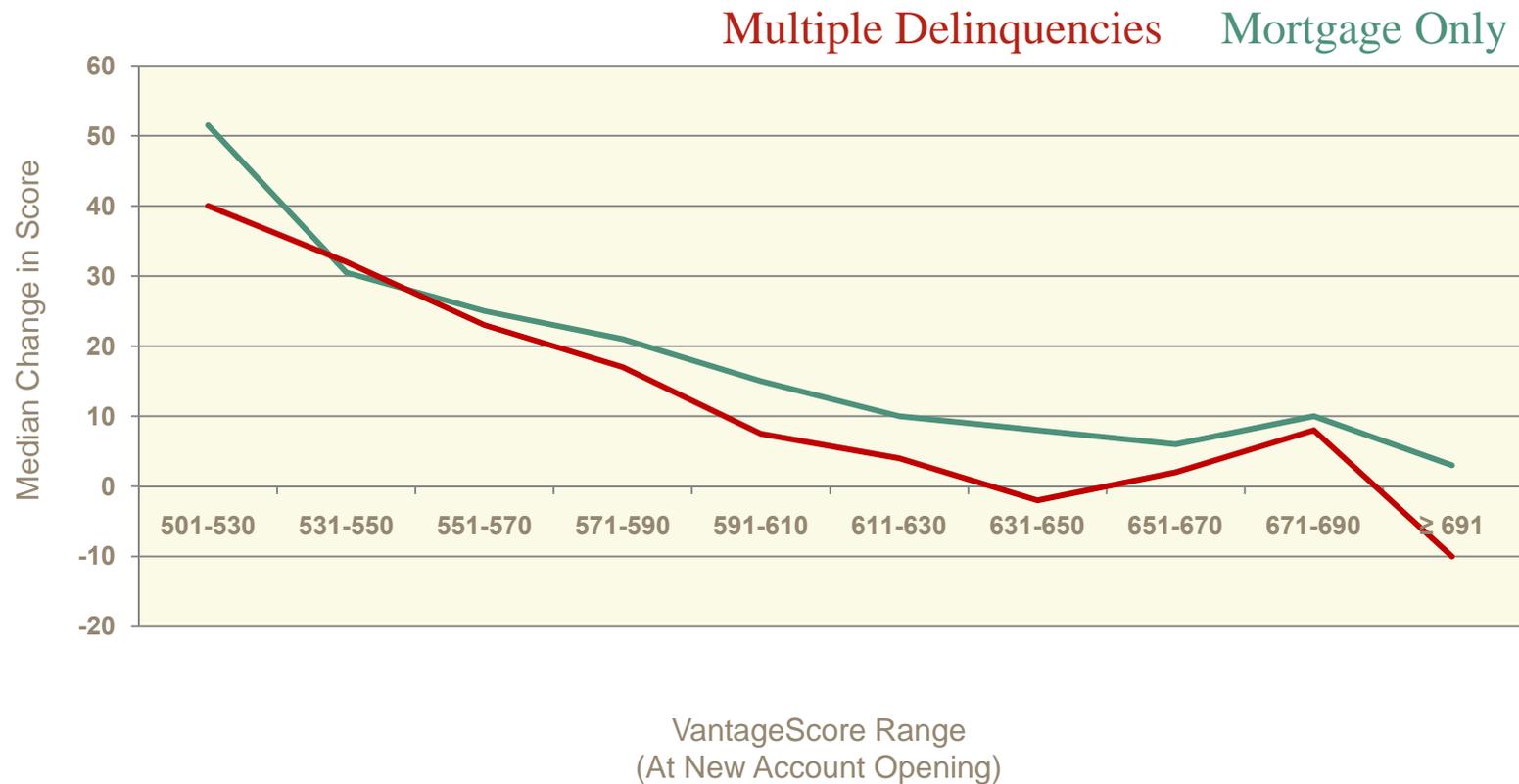
Once again, this result holds true uniformly when controlling for credit score

60+ DPD Rates, All Products, Performance (T2) = 12-17 Months



Result #3: Scores for mortgage-only defaulters tend to “rebound” faster than for those w/multiple delinquencies

Median Improvement in Credit Score over 12-17 Month Performance Window



Incorporating these results into strategy is not difficult

- Identify MOs—a relatively simple task at the credit file level
- Adjust score cut-offs for MOs in prescreen
- Adjust pricing for MOs in offer

The benefits can be material

- “Buy deeper” without the accompanying loss rates
- Avoid the tough competition currently vying for the cleanest segments
- Target a segment that will not otherwise get attractive pricing
- Achieve higher risk-adjusted margin than is currently available in other segments
- Build loyalty at a time when consumer dissatisfaction is relatively high



Beware: you may encounter challenges with execution

- Data and decisioning capabilities
- Formulation of specific strategy—analytical bench strength
- Monitoring performance as environment changes
- Originating loans for sale or securitization
- Executive buy-in

Session summary

- There is a temporal element to looking across your enterprise; behavior that was once considered high-risk may no longer be so
- An understanding of how external factors impact consumers can reveal acquisition opportunities your competitors might miss
- The recent recession is a great example of exceptional behavior; mortgage-only defaulters may not be as bad as you think
- Radical changes to the environment can limit the effectiveness of intuition based on prior experience