



# US CONSUMER CREDIT RISK

## Trends and Expectations, 2nd Quarter 2010

- A Survey by the Professional Risk Managers' International Association

April 2010

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## ACKNOWLEDGEMENTS



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### ZELL CENTER FOR RISK RESEARCH

PRMIA would like to extend special appreciation to The Zell Center for Risk Research at The Kellogg School of Management for their assistance in analyzing the survey responses and writing the report.

The Zell Center for Risk Research promotes the study and understanding of the way people perceive risk, the effects of these perceptions, and the management of risk. The center accomplishes these objectives by encouraging academic research in this area, and through the communication of research findings to a wide audience of academics, students and practitioners. The center is housed within the Kellogg School of Management at Northwestern University, a widely-recognized global leader in management education. The school, located just outside of Chicago, is home to a renowned, research-based faculty and MBA students from around the globe. To learn more, visit [www.kellogg.northwestern.edu](http://www.kellogg.northwestern.edu).



## EXECUTIVE SUMMARY

**T**he Survey of Consumer Credit Risk Trends and Expectations was conducted over 7 weeks between 24 February and 7 April 2010. Respondents to the survey hold a variety of risk-management positions in the U.S. banking sector. They represent various levels of seniority and have experience with one or more credit portfolios. Those who participated in the survey represent firms of all asset sizes, with nearly one-fifth of those surveyed working at firms with a global presence. In total, 127 members of PRMIA located in the USA participated in this survey.

The survey covered three areas regarding the respondent's institution and/or professional opinion concerning: 1) expectations about loan delinquencies during the coming three months, 2) expectations about demand for consumer credit and the lending environment during the coming three months and 3) the effects of the CARD Act. The survey also asked a singular question about the respondent's expectations with respect to risk management at their institution.

From the survey, respondents generally predict that delinquencies will continue to rise, with a particularly negative outlook for mortgages, home equity lines, credit cards and small business loans. The appetite for credit will grow from its current depressed level and those with credit debt will augment their balances. This will occur alongside increases in interest rates for consumer credit and cuts to credit lines from banking institutions. In consideration of the CARD Act, institutions will not be affected equally, but a majority of the respondents foresees a rise in regulatory compliance costs. Additionally, there are mixed opinions on whether the new regulations will work to decrease default rates. Finally, and most importantly, a majority of firms will increase the priority they place on risk management, while no firm looks to de-prioritize risk management.

## KEY FINDINGS

- Approximately half the respondents expect the level of delinquencies in residential mortgages, home equity lines, credit cards and small business loans to increase somewhat, in contrast to auto loans and student loans where they expect delinquency levels to remain about the same. An insignificant number of respondents expect either a significant increase or decrease in delinquencies.
- 45% of respondents expect recovery rates to stay about the same, while 31% expect somewhat of a decrease and 22% somewhat of an increase, reflecting a spread of trends across different sectors.
- Expectations for delinquent accounts are predominantly stable to improving, with 78% of respondents expecting about the same or increased collectability for early stage delinquencies.
- The respondents expect a moderate shift in the balance of consumer credit supply and demand, with 83% expecting demand to increase somewhat or to remain the same, while 88% expect lending standards to hold steady or get somewhat tougher. This expected demand/ supply shift is reflected in the 81% of respondents who expect new credit lines to be about the same or somewhat lower and the 62% who expect consumer credit interest rates to moderately increase.
- Attention paid to consumer credit risk management is clearly on the rise, with 66% of respondents expecting it to receive increased priority and none of the respondents expecting a decrease.
- The 80% of respondents affected by the CARD Act expect it to prompt more stringent credit conditions, with about 50% expecting both somewhat higher interest rates and higher application denials. However, opinions were split on whether the Act would result in lower default rates, with 22% expecting yes, 29% no and 46% no material change.

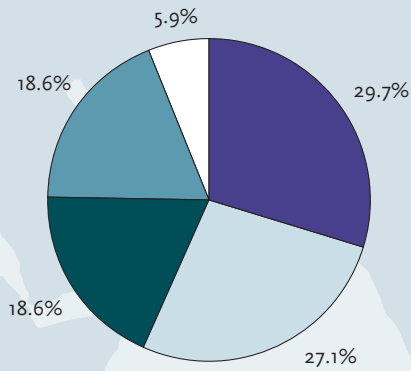
## BACKGROUND

This survey arrives at an opportune time, just as the US financial sector is beginning to recover from the consumer credit repercussions of the most severe economic downturn in the past 50 years. While consumer credit risk management methods and metrics have progressed tremendously during the intervening years, up until now there has been no reliable barometer of national consumer credit risk trends and expectations. This is what prompted PRMIA and FICO to undertake this groundbreaking survey.

# RESPONDENT PROFILE

The survey participants work in a wide variety of risk management positions and represent various levels of seniority (Figure 1), with experience in one or more of the portfolios in Figure 2.

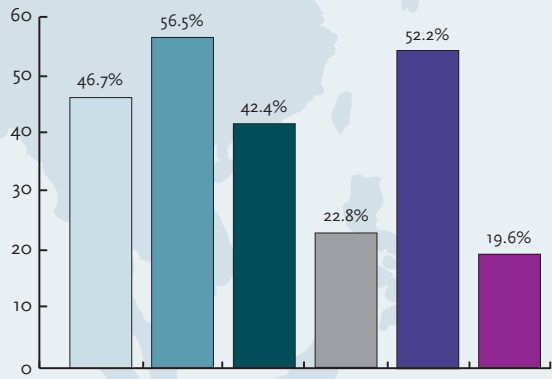
## Your job (select most appropriate)



- Business/risk analyst
- Chief Risk Officer
- Portfolio/product management
- Functional leader
- Other

FIGURE 1

## What is your area of responsibility (check all that apply)?

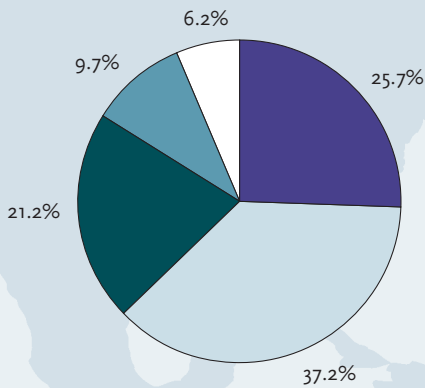


- Card portfolio
- Mortgage portfolio
- Auto loan portfolio
- Direct deposit accounts
- Lines of credit
- Student loans

FIGURE 2

Institutions (by assets) varied across the spectrum, with nearly 40 % representing institutions with smaller than \$5 billion (Figure 3). The next largest group of respondents came from institutions of \$40 billion or more (25.7%). Nearly two-thirds of respondents work in a full service bank (Figure 4).

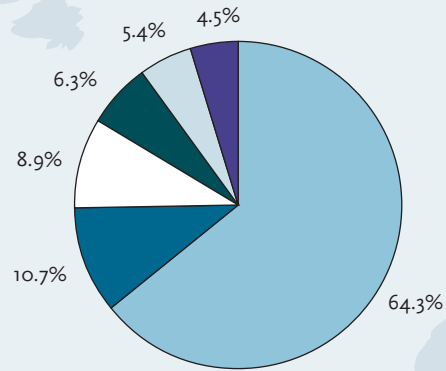
### What is the size of your institution (by total assets)?



- \$40 + billion
- \$20 - \$40 billion
- \$10 - \$20 billion
- \$5 - \$10 billion
- Up to \$5 billion

FIGURE 3

### What is the business orientation of your institution (select the most appropriate)?



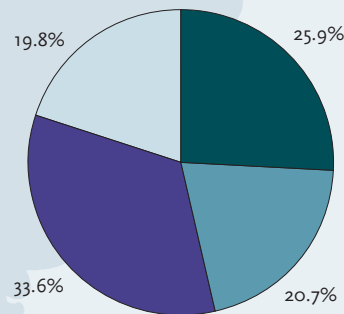
- Full Service Bank
- Credit Union
- Mortgage lender
- Wealth management, investments, retirement services
- Discount and/or self-serve financial services
- Credit Card Monoline

FIGURE 4

### What is the geographic reach of your institution?

A majority (79.3%) of respondents represent institutions that operate within the United States while approximately one-fifth of respondents had a global presence.

There were no Internet-based firms represented amongst those surveyed (Figure 5).



- Local
- Regional
- National
- Global
- Internet-based

FIGURE 5

## DELINQUENCIES

Majorities believe delinquencies on mortgages (90+ days) and home equity lines will grow, with only 10% expecting fewer of either.

Expectations are also negative for credit card delinquencies and limit reductions/cancellations, which will both increase ~ 60%.

Delinquencies on small business loans will be problematic, increasing either “significantly (56%)” or “somewhat (9%)”.

Recovery rates for delinquent accounts will slightly decrease (30%) more than slightly increase (23%). Roughly the opposite is true of early stage collectability. (Figure 6)

Over the next three months, do you expect: (check all that apply to your business)

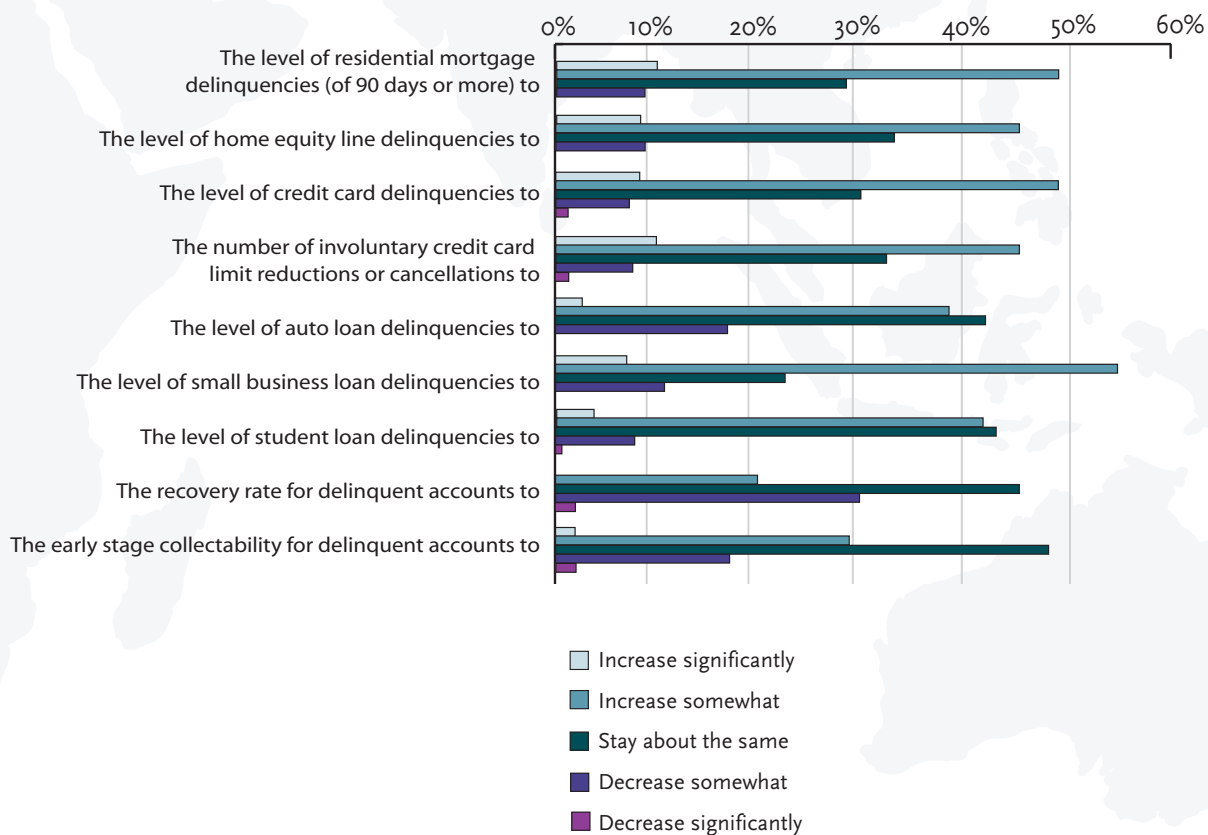


FIGURE 6

## SUPPLY AND DEMAND

Demand for consumer credit will increase (~55%) alongside of hikes in interest rates on consumer credit (~60%) and cuts to the average credit line (~50%).

40% expect creditworthiness of new applicants to decrease “somewhat” or “significantly”. A similar percent will “stay about the same”.

40% will augment their lending standards while 55% will “stay about the same”

A majority of respondents think clients will grow their balances, with only one-quarter of customers staying “about the same”. (Figure 7)

Over the next three months, do you expect: (check all that apply to your business)

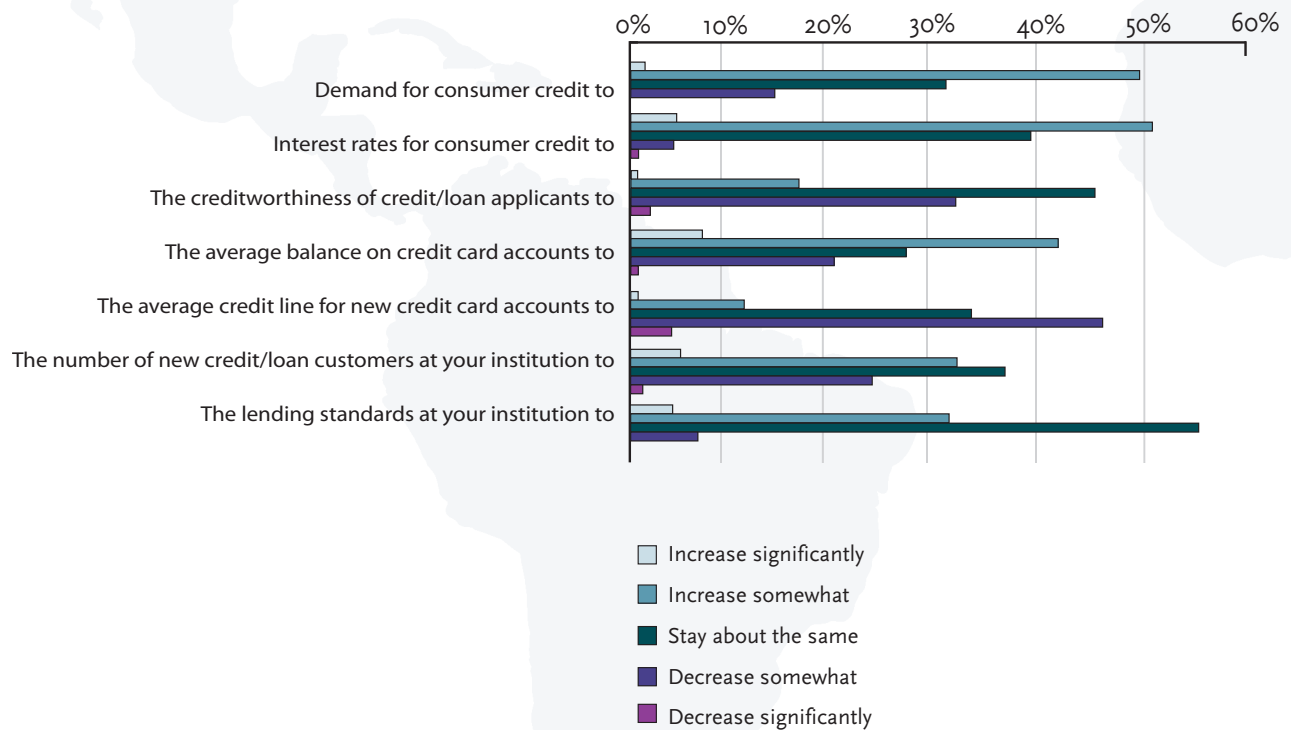


FIGURE 7

## THE CARD ACT

Two-thirds expect a rise in regulatory compliance costs from CARD while 50 percent predict a rise in interest rates.

The Act will slightly contract lines of credit, with one-third predicting “about the same” and one-third predicting “somewhat lower”.

Participants split on how the Act will influence defaults, with 25 percent expecting some sort of increase and 25 percent expecting some sort of decrease.

The total effect of the CARD Act is not uniform with 20 percent of respondents in each category foreseeing no effect from the CARD Act. (Figure 8)

### What effects do you anticipate the CARD Act will have on your institution?

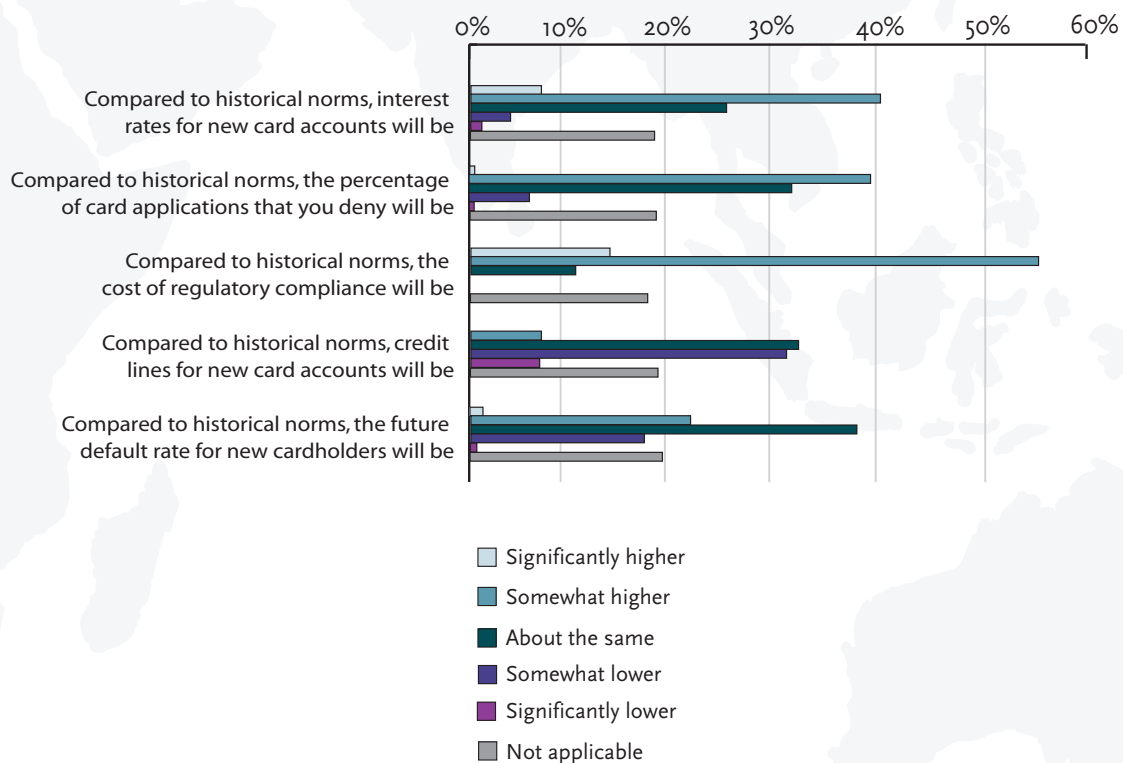


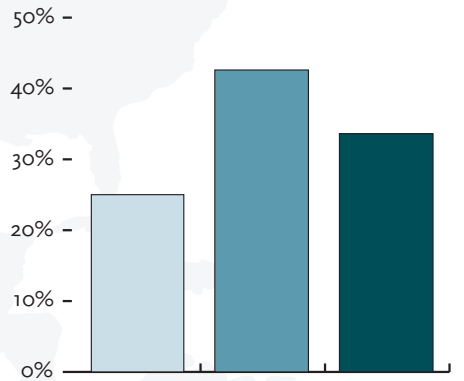
FIGURE 8

## RISK MANAGEMENT

All respondents will either increase or maintain their priority on risk management.

During the next budget cycle, a super-majority will increase either “significantly” or “somewhat” their priority on risk management. (Figure 9)

During the next budgeting cycle, do you expect:



The priority placed on risk management at your institution to

- Increase significantly
- Increase somewhat
- Stay about the same
- Decrease somewhat
- Decrease significantly

FIGURE 9

Raw data is available on request – contact PRMIA at [surveys@prmia.org](mailto:surveys@prmia.org)



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