



Battling for Balances:

Targeting the Lucrative Card-to-Card
Consumer Balance-Transfer Market

An Experian Perspective





The Perfect Storm

After several years of turbulence and uncertainty, the playing field has stabilized for the credit card industry. Lenders have learned an invaluable lesson as it relates to bad credit risk and are now poised to grow their businesses in a more risk-averse, sustainable manner. At the same time, consumers are far better educated about the importance of managing their debt and are interested in deleveraging to improve their credit health in a responsible fashion.

This perfect storm of market conditions presents important challenges as well as opportunities for lenders. Regulatory changes in the lending industry, along with shifting consumer trends, are making it more challenging for banks to maintain market share and profitability. Now, more than ever, lenders need to target and retain the most lucrative consumers to expand their portfolios. Balance transfers represent a critically important revenue lever in the market. Developing effective strategies for targeting and retaining the optimal balance-transfer candidates — those who will deliver returns with minimal risk — are well worth pursuing. Such strategies also will enable lenders to promote the right products to help consumers, thereby strengthening this important relationship.

Federal Regulations Put the Squeeze on Profits

Significant changes in federal regulations are having a profound impact on the banking industry's bottom line, particularly when it comes to the credit card business. In just a few short years, new regulations have challenged the traditional revenue models that rely on earnings on interest income, over-limit and late fees, as well as debit card fees.

The tight squeeze on interest income continues as consumers remain reluctant to carry higher balances. Evidence of this trend can be found in the flat volume numbers for total U.S. credit card debt, which remains virtually unchanged from last year. According to Experian-Oliver Wyman Market Intelligence Reports, total credit card debt in the United States at the end of 2013 was \$592 billion, up less than 1 percent from the previous year.

The Downside of an Upswing in the Economy

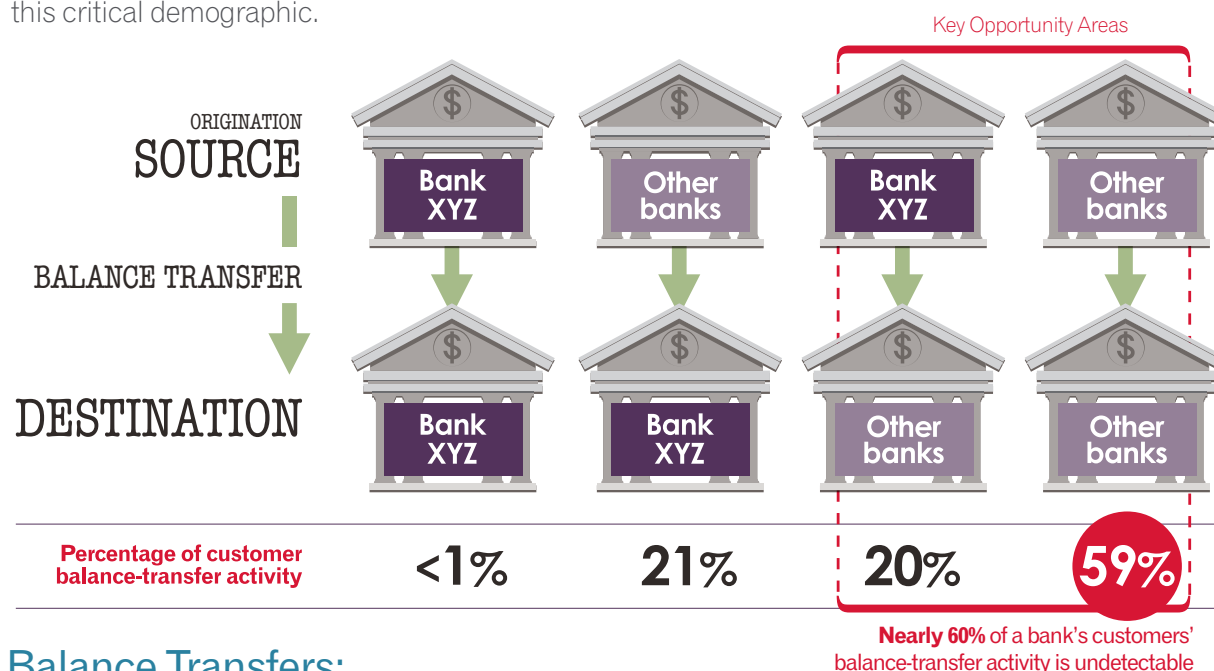
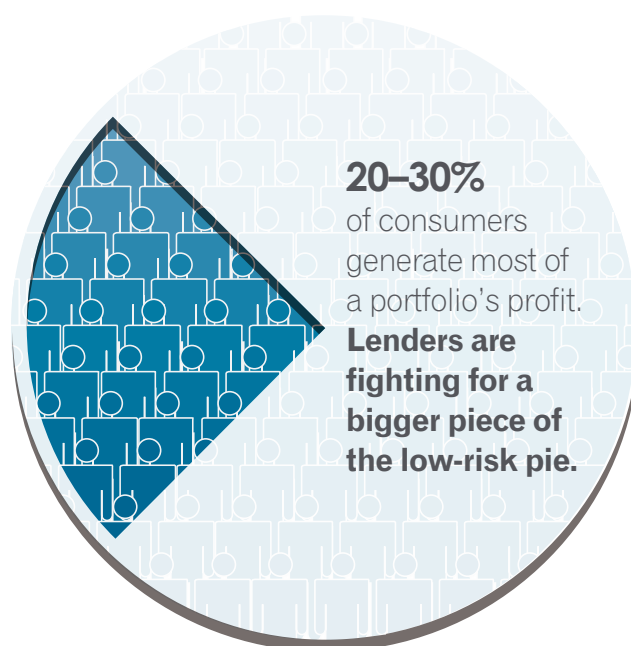
Signs of economic recuperation can be found all around us. Unemployment rates continue to fall. While the nation is not yet at full employment levels, forecasts indicate sustained improvement. The Bureau of Labor Statistics reported that unemployment dipped to 6.1 percent in June 2014, and projections indicate lower rates for the foreseeable future.

A combination of improving employment and a write-off of bad debt has led to a decline in late-stage bankcard delinquency rates. Personal bankruptcy filings, which peaked in 2010, dropped by as much as 12 percent in 2013, and fluctuations in home equity and mortgage debt have contributed to a fundamental shift in credit behavior as more consumers focus on paying off their outstanding debt. The steadily narrowing debt-to-income ratio is indicative of this overall trend. While this bodes well for the economy, lenders continue to face profitability hurdles.

Fighting for a Bigger Piece of the Low-Risk Pie

As the industry emerges from the effects of recession, having expunged bad paper, lenders are finally looking to grow their portfolios again. Evidence of these efforts can be found in new card originations, which were up 20 percent year-over-year in 2013. Most significantly, new debt is far lower-risk with more than 90 percent of originations in the super-prime to near prime segments.

For most lenders, 20 percent to 30 percent of consumers generate most of a portfolio's profit, which means as prospecting picks up, more and more companies are narrowly focused on the same low-risk customer segment. Lenders are fighting for a bigger piece of the low-risk pie, making it increasingly important to understand better where the greatest opportunities lie and how to attract this critical demographic.

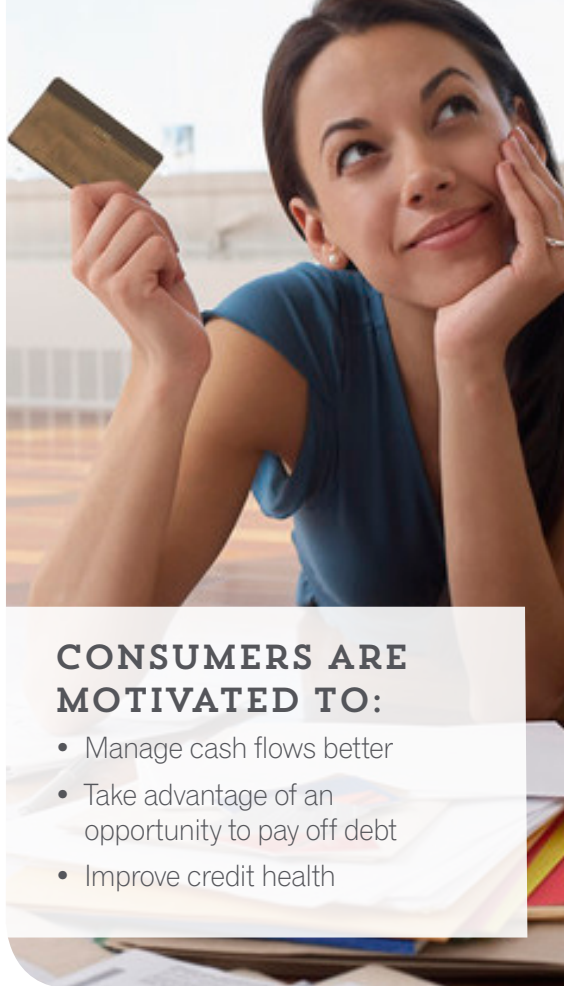


Balance Transfers: A Profitable Opportunity

Card-to-card balance transfers represent a substantial profit opportunity for lenders. According to Experian estimates, balance-transfer activity is currently in the range of \$35 billion to \$40 billion annually. Much of this debt is concentrated in the prime segment. This lower risk portfolio makeup is proving to be a highly attractive market for banks.

Several challenges face lenders in securing a greater share of balance transfers. On average,

nearly 60 percent of a bank's customers' balance-transfer activity is undetectable, or "off bank." As banks look to lure balance-transfer customers away from competitors, those very same competitors are trying to attract their customers. Further complicating this hunt for highly coveted balance-transfer customers is the need to identify the right prospects. Segmenting the profitable from those less-profitable consumers, who are habitual rate surfers, is instrumental to capturing long-term profitability.



CONSUMERS ARE MOTIVATED TO:

- Manage cash flows better
- Take advantage of an opportunity to pay off debt
- Improve credit health

Understanding the Drivers Behind Transfers

In targeting card-to-card balance transfers, lenders must gain a clear understanding of the drivers motivating this activity. Consumers generally are propelled by a strong desire to manage cash flows better, take advantage of an opportunity to pay off debt and improve credit health. In order to attract these consumers, lenders typically offer incentives, including zero or near-zero percent APR, for an introductory period. To lure prospects, lenders may extend introductory periods with a small transfer fee or offer a shorter introductory period with no fee.

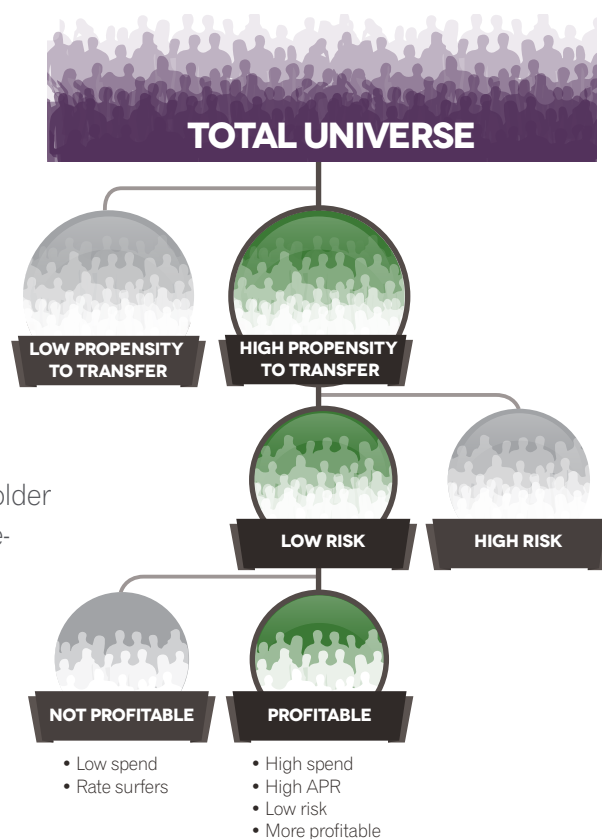
Research shows even with highly attractive low rate introductory periods, high “go-to” rates can prove to be a disincentive. Despite the attractiveness of an offer, it’s only effective if it reaches the right audience. In order to solicit the desired response to a balance-transfer campaign, lenders can use behavioral models that will predict the likelihood of a consumer responding to a balance-transfer offer. With such insights in hand, highly effective offers can be tailored to meet the needs of these targeted customers.

Improving Response Rates: The Power Of Propensity Modeling

Propensity modeling is an invaluable tool in predicting a consumer’s future credit usage behavior and maximizing response rates of consumer campaigns. Balance-transfer models are among the tools that use a consumer’s past balance-transfer activity in combination with deep credit usage attributes to predict future appetite for a balance transfer and a high propensity to take action.

By using aggregate wallet information on consumers, a balance-transfer model can offer critical insights into future cardholder behavior. Key predictors typically used in such a model are balance-transfer history, historical balance-transfer amounts, cards carried and used, as well as payments and spend.

Additional attributes and models — such as an advanced estimate of spend, payment rates and wallet share insight — combined with income information can further segment the high-value balance-transfer population. Understanding the credit health and financial position of the customer, as well as his or her propensity to take action on a new offer of credit, identified by a balance-transfer model, would highlight those segments of consumers more likely to respond to your offer and that are more profitable to your business.





Segmenting Surfers and Deleveragers

An Experian analysis shows that as much as 20 percent of high-propensity balance-transfer candidates are perpetual surfers and will transfer out within an 18-month period. Lenders need to identify this segment in order to avoid targeting consumers who hold little to no profitability promise. Models that predict the likelihood of a consumer being a surfer can be leveraged in combination with a balance-transfer model to filter out this unprofitable segment.

20 PERCENT OF HIGH PROPENSITY BALANCE-TRANSFER CANDIDATES WILL TRANSFER OUT WITHIN AN 18-MONTH PERIOD

Another consumer segment that lenders could look to identify are deleveragers. These consumers may have a high balance-transfer propensity, and because their goal is to pay down their balances as quickly as possible, they require a combination of a low APR and a favorable reward program to retain loyalty beyond their balance payoff.

Insights gained using a combination of the balance-transfer index and attributes and models that identify rate surfers and those looking to deleverage, can highlight consumer segments that are more loyal and potentially profitable in the long term

Solving the Retention Dilemma: Focus on Your Own Portfolio

As lenders increasingly focus on attracting consumers with balance-transfer offers, they may be overlooking a lucrative market right under their noses. Being able to identify customers in your own portfolio, who may potentially transfer their balances to another bank, is critical. A balance-transfer index can provide lenders with an invaluable ability to segment card holders who represent an attrition risk within their own portfolio.

Lenders can apply the same propensity and segmentation criteria to their own customers as they would to a target population in order to identify the risk of balance transfer out. Armed with this vital customer information, lenders can tailor incentives to their own cardholders

based on specific needs. Lenders can use lower APRs, increase credit lines or sweeten rewards to prevent these profitable customers from transferring their balances to a competitor. A balance-transfer index is a key strategy in solving the card portfolio retention dilemma.

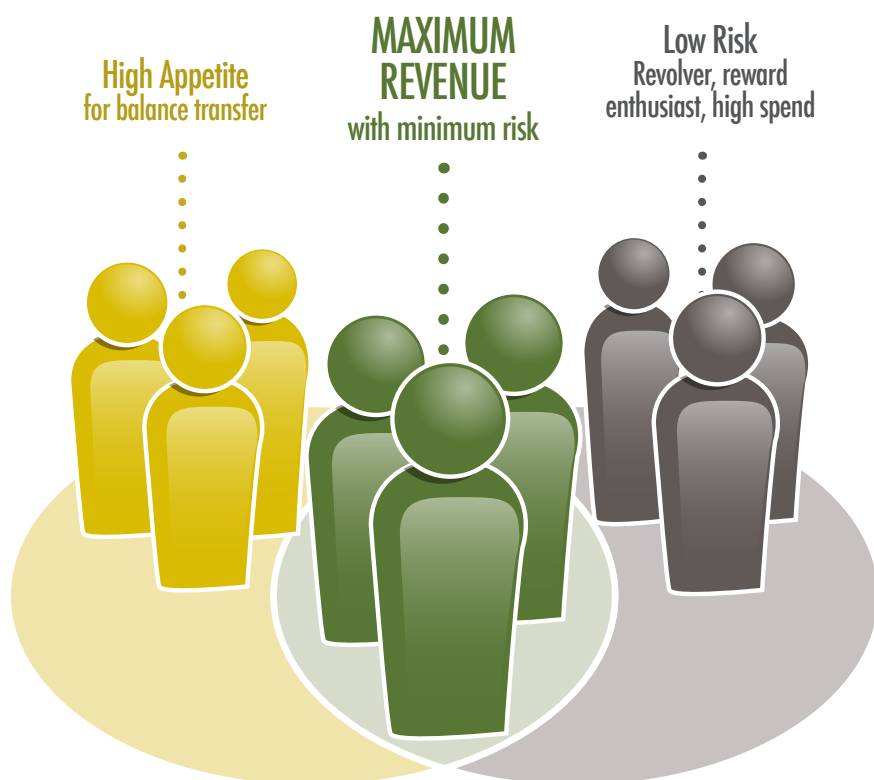
The impact to brand loyalty is obvious, but it should be noted that by improving the offering to consumers, lenders are also better serving their customers, further reinforcing their status as valued-clients. The more customers view their card lender as being focused on delivering benefits they truly care about, the more loyal they will be in the future.

Segmentation: The Key To Identifying Balance-Transfer Appetite

As lenders look to overcome regulatory challenges and the changes these restrictions have imposed on doing business, they must increase efforts to target lucrative balance-transfer prospects in order to grow their portfolios. Banks need to capitalize on this important segment, developing effective strategies for identifying optimal balance-transfer candidates who can deliver maximum revenue with minimal risk.

Extracting profitable segments for a balance-transfer strategy is not a one-dimensional approach. Within the segments live rate surfers and deleveragers, necessitating micro targeting in order to achieve the most impactful campaigns.

The identification and segmentation of highly desirable balance-transfer consumers requires a deep understanding of the balance-transfer universe. This understanding can be achieved using a set of predictive tools that effectively aide in targeting the most profitable current and future consumer relationships. The battle for balances is underway, and the savviest lenders will be poised to win.



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