FICO Resilience Index

A new analytic tool to help capture consumer credit risk linked to unexpected economic stress

In the face of severe financial stress such as that brought about by an economic downturn, lenders seeking to reduce their credit risk exposure often resort to tactics executed at the portfolio level, such as raising credit score cut-offs for new loans or dramatically reducing credit limits on existing accounts. While they can be effective in reducing overall exposure, such tactics can hurt profitable relationships with current customers and seriously curtail new account growth. What if lenders were able to factor consumer-level risk adjustments into such decisions rather than using coarser levers? What if lenders could tune their portfolio throughout economic cycles so as not to rely on dramatic measures if/when a downturn materializes?

The FICO® Resilience Index – leveraging traditional consumer credit data from Equifax – is designed to rank order consumers with respect to their resilience or sensitivity to an economic downturn. Even within a narrow FICO® Score band, for example near the common FICO Score cut-off of 680, a range of so-called "stress sensitivity" can be observed. FICO Resilience Index can provide insights into, which "680s" are more likely to go seriously delinquent when economic stress is exerted on a consumer population – giving lenders a new tool to use and potentially avoid taking broad measures that impact insensitive or more "resilient" consumers unnecessarily.

Higher resilience customers tend to have:

- Fewer credit inquiries in the last year
- Fewer active accounts
- Lower total revolving balances
- More experience managing credit

Why use the FICO Resilience Index?

- Better prepare for cyclical downturns
- Assess loan portfolio vulnerability more accurately
- Refine credit marketing and origination strategies
- Improve stress testing outcomes
- Better estimate loss allowances
- Integrate easily with existing FICO Score processes

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Figure 1 shows how FICO® Resilience Index would have differentiated consumer credit risk within narrow FICO® Score bands for bankcard accounts open and active as of October 2007, at the start of the Great Recession. Based on a large randomized national sample, the October 2009 performance results showed that consumers with the highest 20% of FICO Resilience Index values (least resilient quintile) had significantly higher 90+ days past due rates compared to consumers in the lowest 20% FICO Resilience Index value range (most resilient quintile). A lender with FICO Resilience Index in their analytic arsenal might have continued to offer periodic credit line increases to consumers in the lower quintiles while maintaining or proactively reducing credit limits for those in the top quintile, avoiding losses and reducing volatility.

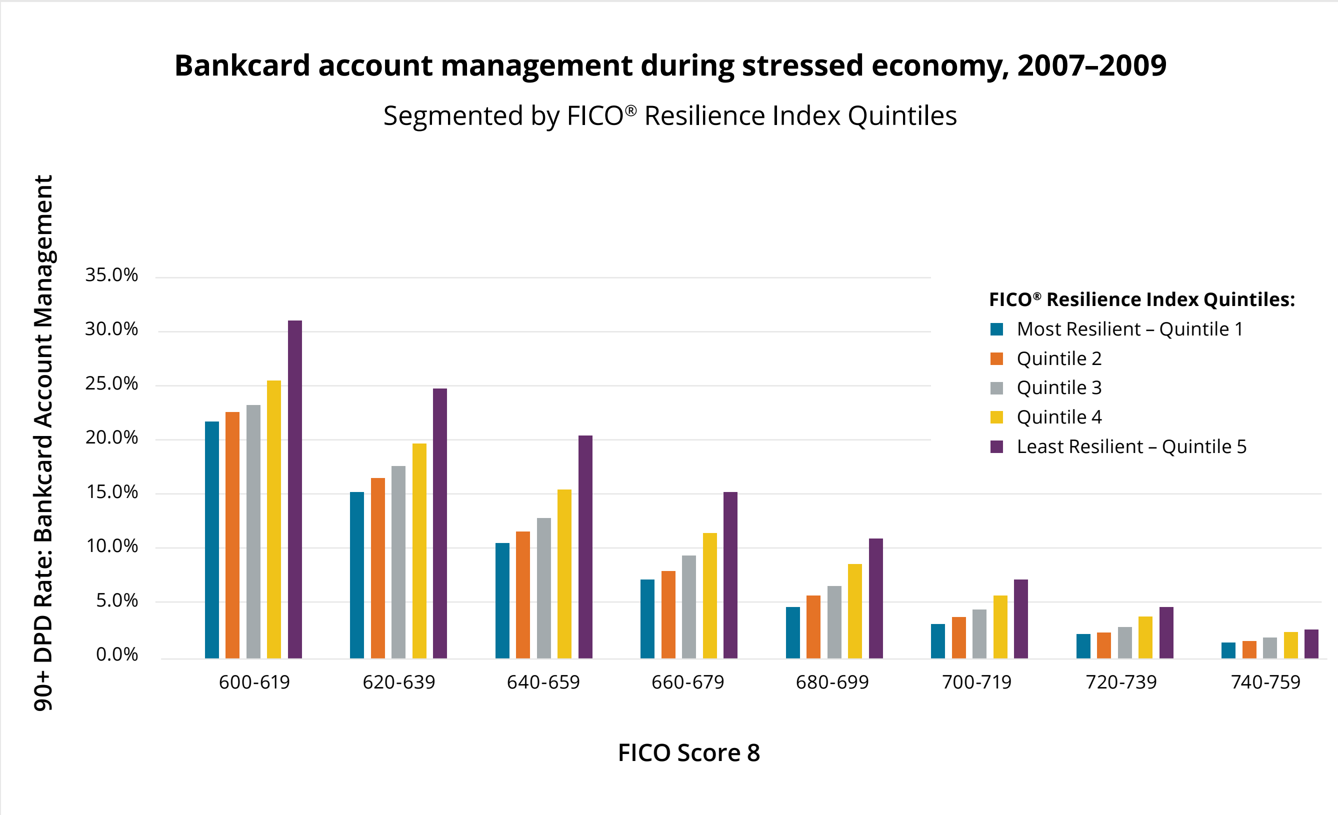

Figure 1: FICO® Resilience Index provides strong additional credit risk rank-ordering in recessionary environments. During unstressed periods, serious delinquency rates within FICO® Score bands are expected to be relatively homogeneous.

FICO Resilience Index can be used by lenders as another input into credit decisions and account strategies across the credit lifecycle.

Paired with the FICO Score for better decisions, better portfolio management

FICO® Resilience Index can be used by lenders as another input into credit decisions and account strategies across the credit lifecycle. It can be delivered with a credit file, along with the FICO® Score. It's scaled from 1 to 99, with higher values representing higher sensitivity to economic stress. FICO Resilience Index is delivered with up to five reason codes that help lenders better understand the output as well as support adverse action communication, if necessary. Some lenders may use FICO Resilience Index in conjunction with the FICO Score, for example as a dual score matrix or as an additional decision key. Other lenders may choose to use FICO Resilience Index to generate an adjusted FICO Score with adjustment factors tuned to the lender's view of macroeconomic forecasts.

FICO® Resilience Index Version 1.0 is most effective for account management and may be used selectively for account origination, particularly personal installment loans and mortgage lending.

FICO® Resilience Index is also conducive to portfolio stress testing and can be used as an element to better understand and estimate the impact of increased economic stress on portfolio performance. As lenders better understand FICO Resilience Index relevance to their own portfolio, this metric can be used to tune portfolio structure over time to be more resilient in the face of impending economic stress. And, by actively managing FICO Resilience Index distributions within their portfolios, lenders may improve capital coverage in severe stress test scenarios required for regulatory stress tests such as Comprehensive Capital Analysis and Review (CCAR) and Dodd-Frank Act Stress Test (DFAST).

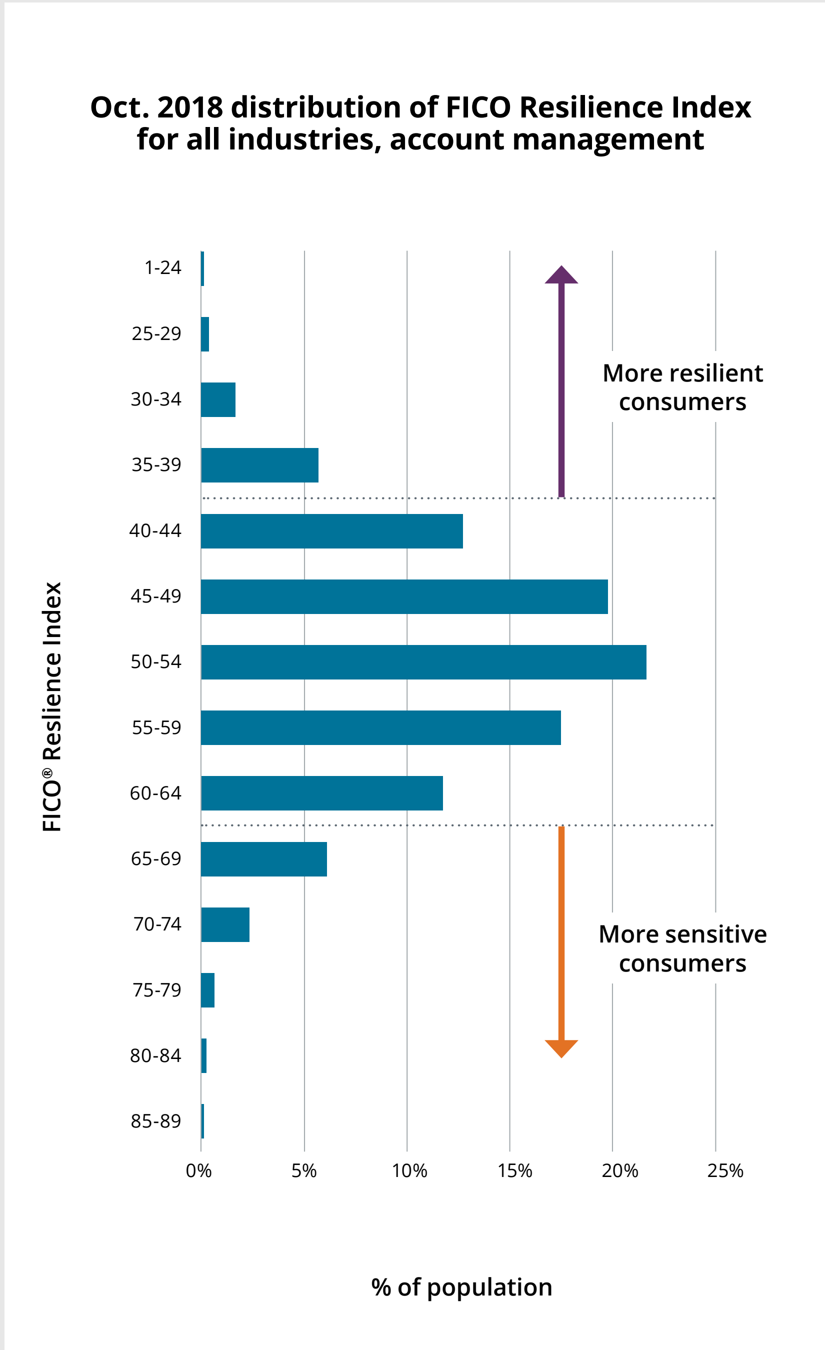

Figure 2: FICO® Resilience Index rank-orders consumers by their sensitivity to severe economic stress, with lower values representing greater resilience (or lower sensitivity).

A new view of loan asset health for lenders, investors, and regulators

As investors in asset-backed securities begin to appreciate the additional risk insights FICO® Resilience Index can provide, lenders may find that more resilient portfolios are considered to be of more value. The performance differentials captured by Figure 3 sharply illustrate how identifying latent pools of risk in a portfolio can matter, particularly if a lender or investor seeks to model or prepare for adverse or severely adverse economic scenarios.

	20% Most resilient at FICO® Score* 680	20% Most sensitive at FICO® Score* 680
Normal economy 90+ DPD rate	4.3%	4.4%
Great recession 90+ DPD rate	6.3%	13.3%

*FICO Score 9, All industries, account management

Figure 3: FICO compared the average serious delinquency rate for consumers with a FICO® Score near 680 in a stable economy (2013–2015) compared to the steep downturn of 2007–2009. While the 20% most sensitive consumers had over double the serious delinquency rate compared to the stable economy, the 20% most resilient had only a slightly elevated serious delinquency rate.

Start building resilience today for tomorrow's economic uncertainty

FICO® Resilience Index is available today from Equifax and can be added to lenders' current FICO® Score processes as a simple extension to existing online and batch processes. Lenders can get started by validating the performance of FICO Resilience Index for a portfolio that was active or originated during the Great Recession or another period of observed economic stress in a target portfolio. With meaningful evidence in-hand showing that FICO Resilience Index will predict differentiation in future economic downturns, financial institutions can begin to better prepare for and reduce the financial volatility associated with economic disruptions by making FICO Resilience Index a key part of their resilience-building strategies.

To learn more about how FICO Resilience Index can support your portfolio, please contact us today.

The FICO Resilience Index – leveraging traditional consumer credit data from Equifax – is designed to rank order consumers by their sensitivity to a future economic downturn.

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