



# US CONSUMER CREDIT RISK Trends and Expectations

THIRD QUARTER 2011

- A Survey by the  
Professional Risk  
Managers' International  
Association

October 2011

[www.PRMI.org](http://www.PRMI.org)



*PRMIA thanks our survey sponsor*

**FICO**<sup>™</sup>

## ACKNOWLEDGEMENTS



The Professional Risk Managers' International Association (PRMIA) is a higher standard for risk professionals, with 65 chapters around the world and nearly 80,000 members from 198 countries. A non-profit, member-led association, PRMIA is

dedicated to defining and implementing the best practices of risk management through education including the Professional Risk Manager (PRM™) designation and Associate PRM certificate; webinar, online, classroom and in-house training; events; networking; and online resources. More information can be found at [www.PRMIA.org](http://www.PRMIA.org).

# FICO™

FICO (NYSE:FICO) delivers superior predictive analytics that drive smarter decisions. The company's groundbreaking use of mathematics to predict consumer behavior has transformed entire industries and revolutionized the way risk is managed and products are marketed. FICO's innovative solutions include the FICO® Score — the standard measure of consumer credit risk in the United States — along with industry-leading solutions for managing credit accounts, identifying and minimizing the impact of fraud, and customizing consumer offers with pinpoint accuracy. Most of the world's top banks, as well as leading insurers, retailers, pharma businesses and government agencies rely on FICO solutions to accelerate growth, control risk, boost profits, and meet regulatory and competitive demands. FICO also helps millions of individuals manage their personal credit health through [www.myFICO.com](http://www.myFICO.com). FICO: Make every decision count.

## Columbia Business School

PRMIA would like to extend special appreciation to The Center for Decision Sciences at Columbia Business School for their assistance in analyzing the survey responses. The Center for Decision Sciences brings together scholars from a range of fields who share an interest in human decision making. The center facilitates research and understanding on consumer behavior, the implications of decision making on public policy, and the neurological underpinnings of judgment and decision making. The center is housed within Columbia Business School, widely acknowledged as being among the world's top business schools. To learn more, visit <http://decisionsciences.columbia.edu>.

## EXECUTIVE SUMMARY

Since the fourth quarter of 2009, PRMIA and FICO have regularly polled credit risk management professionals regarding their predictions for the next six months and the impact of current events on their field. During the third quarter of 2011, 188 risk management professionals polled expressed much concern regarding their view of the next six months. This suggests that the optimism observed in late 2010 and early 2011 has waned substantially.

The theme running throughout most of the survey results was pessimism. For example, more respondents expect delinquency rates to increase rather than decrease on mortgages, home equity lines, credit cards, student loans, and even auto loans, which had been a bright spot in previous surveys.

Respondents were especially gloomy in their outlook for the housing market. Nearly 60 of respondents expect housing prices to remain below 2007 levels until at least 2020. In addition, over 73% of respondents expect mortgage delinquencies to remain elevated by historical standards for at least five more years.

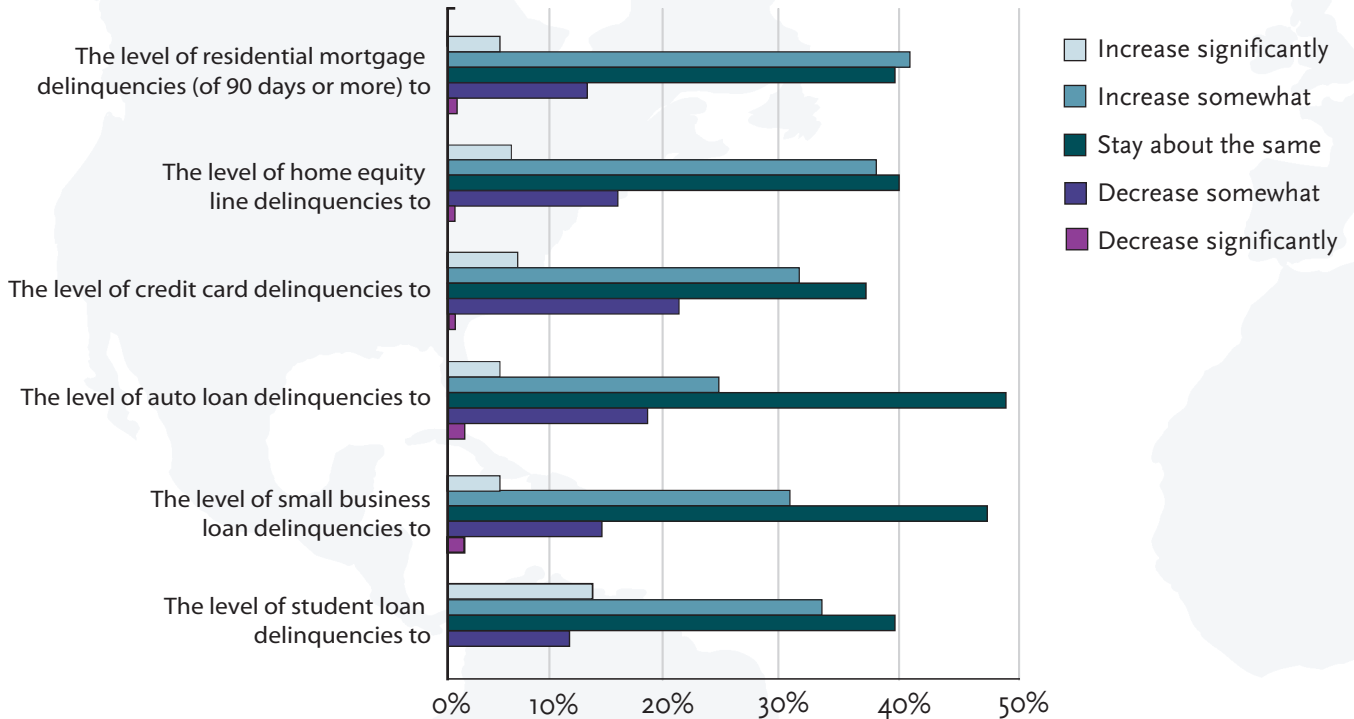
### **Key Findings and predictions about the next six months:**

- Most (85.2%) feel that the level of mortgage delinquencies will rise or stay the same.
- Nearly half (48.9%) feel that auto loan delinquencies will stay the same.
- Over half (54.1%) predict that interest rates for consumer credit will decrease or stay the same.
- Nearly half (49.8%) predict that the average credit card balance will increase.
- Over half (52.3%) predict that the approval rate for credit and loan applications will stay the same.
- Many respondents (48.3%) feel that the U.S. is heading for a double-dip recession.
- A majority (63.9%) feel the U.S. consumer credit card usage is unlikely to reach pre-recession levels for at least five years.

## KEY FINDINGS AND ANALYSIS

### Delinquency Predictions Show Little Change

Looking at the industry as a whole, over the next six months, do you expect: (check all that apply)

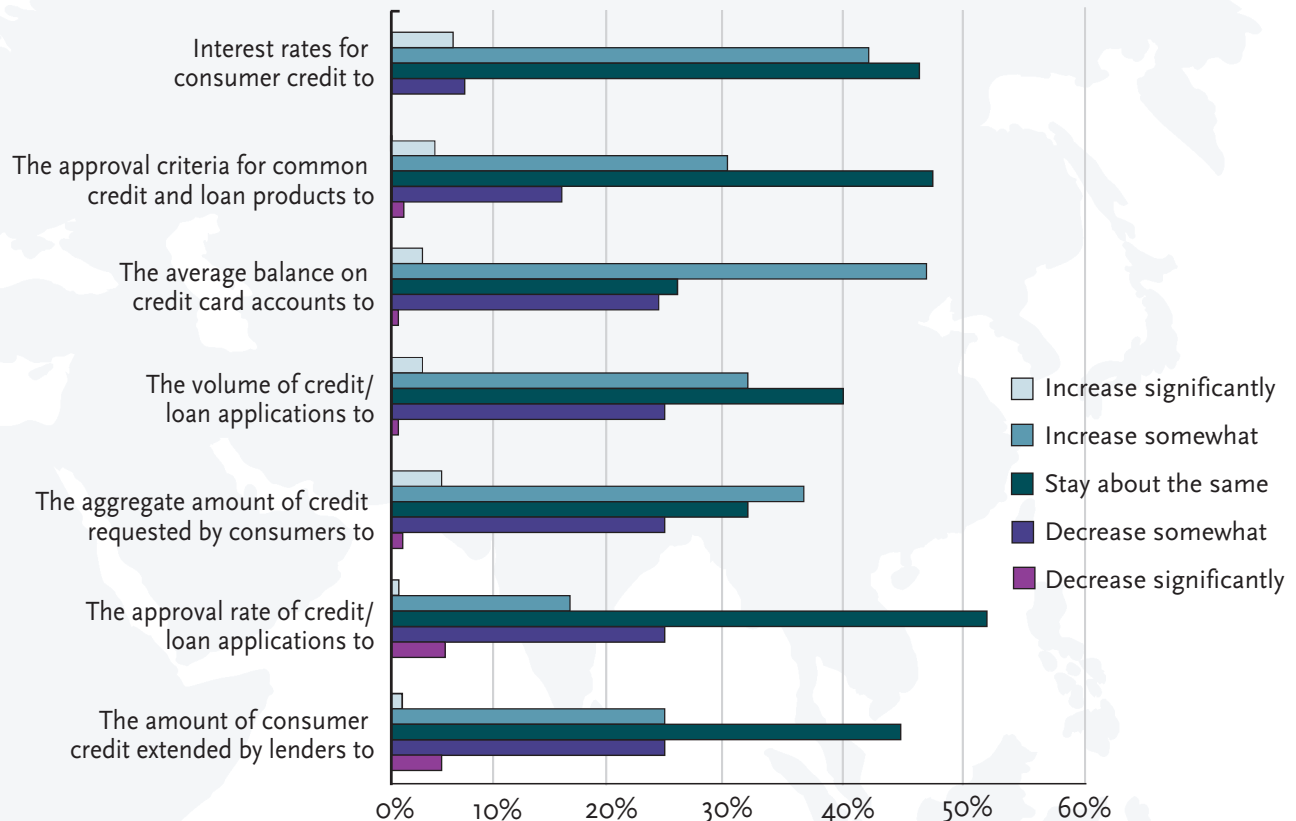


The overall delinquency picture remains pessimistic and similar to that seen in Q2 2011 with the only positive exception being the level of home equity line delinquencies (which Q3 respondents felt were more likely to stay the same, whereas a plurality of Q2 respondents predicted increase).

Beginning with mortgage delinquencies, 45.6% expect an increase, compared to only 14.8% who predict any sort of decrease. Home equity line decreases, as noted above, find 40% predicting levels would remain the same. Credit card delinquency predictions show 39.7% of respondents predicting an increase, slightly more than the 30.6% predicted this in Q2. Slightly less than half (48.9%) predict no change to the level of auto loan delinquencies, and similarly, 47.5% predict no change to the level of small business loan delinquencies. Finally, just less than 40% (39.8%) of respondents predict the levels of student loan delinquencies to stay the same, and nearly half of respondents expect an increase in delinquencies.

## Rates Increase Seen As Unlikely Compared to Previous Quarter

Looking at the industry as a whole, over the next six months, do you expect: (check all that apply)



Focusing now on consumer underwriting, slightly less than half (46.6%) of the respondents polled felt that interest rates for consumer credit would stay the same, compared to 34.5% who felt this way in Q2. The Q2 dominant prediction of increase (62.3%) has shrunk substantially to 45.9% in Q3. While rate predictions differ between quarters, predictions regarding approval criteria remain consistent, with 47.4% expecting criteria to remain the same. Almost half (49.8%) predict that the average balance on credit cards will increase (consistent with the Q2 prediction), and 74.6% predict the volume of credit or loan applications to increase or stay the same.

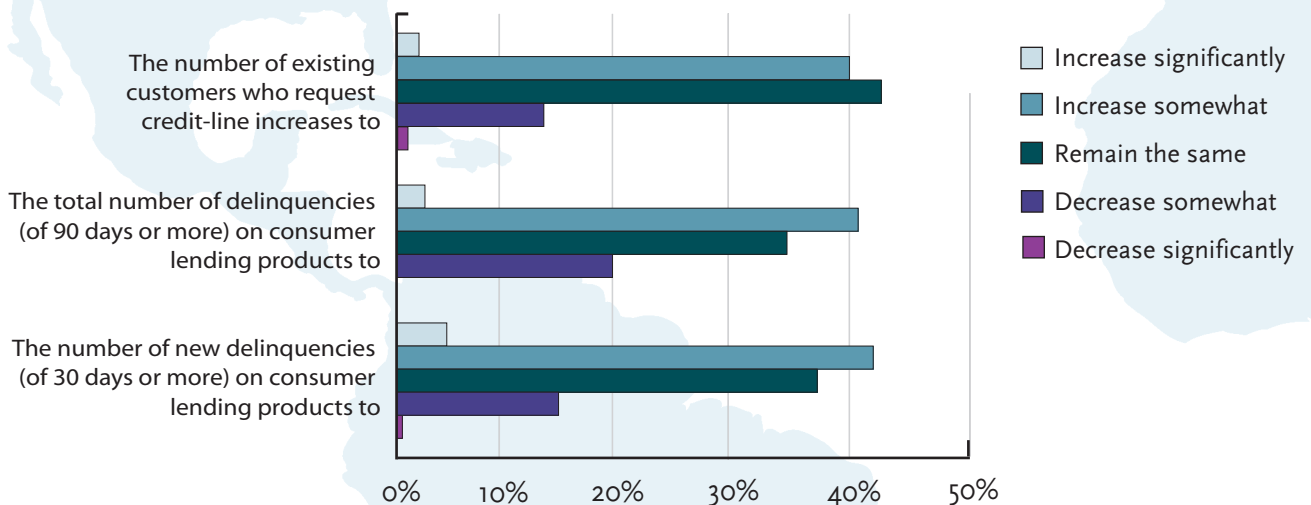
Interestingly, a subtle shift from Q2 to Q3 predictions was observed in belief regarding approval rates. Whereas Q2 saw rather mixed beliefs, a majority of Q3 respondents (52.3%) felt that approval rates would stay the same. Similarly, Q3 respondents predicted the amount of credit extended by lenders differently than those in Q2. In Q3, while 44.3% believe the amount will stay the same, an equal number (25.3%) felt a small increase or decrease would be observed. This is a change from Q2 where 40% predicted a small increase, and only 19.6% predicted a small decrease. This suggests that predictions of growth or change are being replaced with predictions of consistency or small change.

## SURVEY DETAILS

Overall, the underwriting predictions of this quarter speak to a state of consistency, with a prediction of change only clear in one category (credit card balances, predicted to increase). As with delinquency predictions, this suggests that volatility in the economy over the past quarter has done little to sway underwriting predictions as a whole.

### The Industry as a Whole

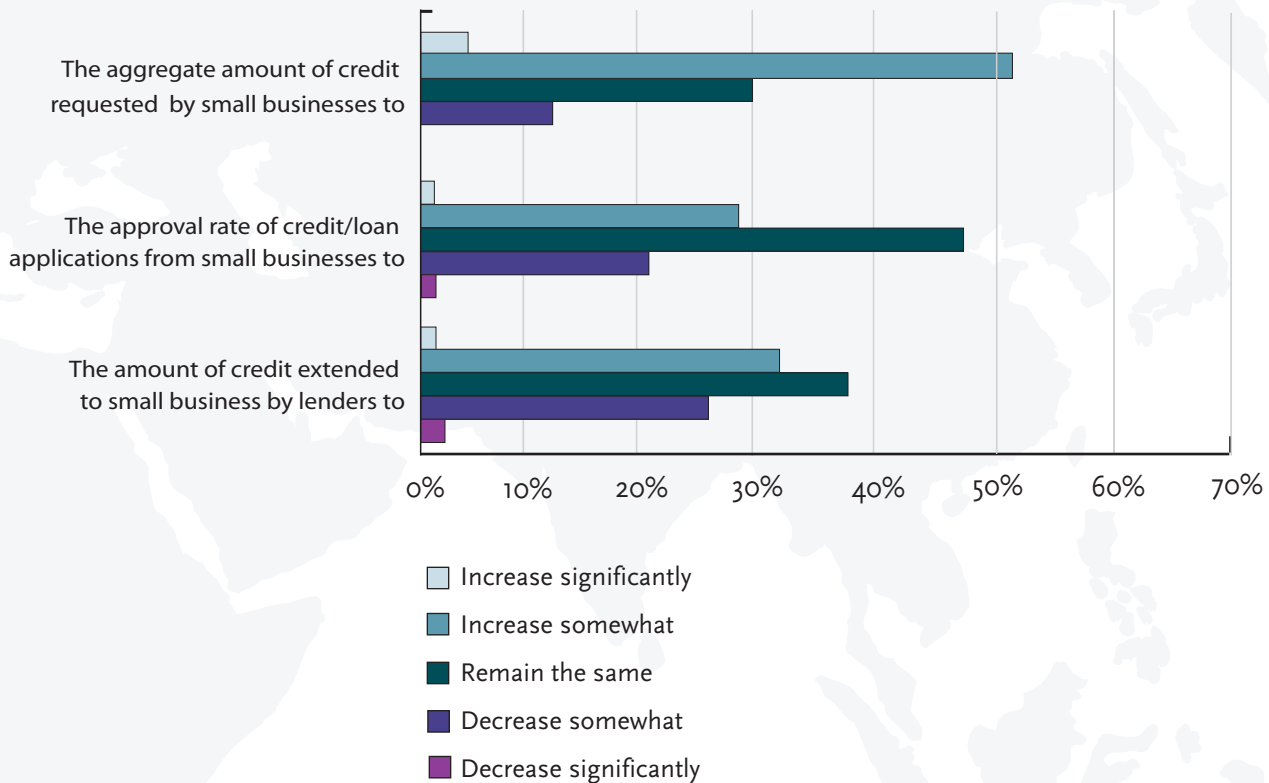
Looking at the industry as a whole, over the next six months, do you expect:



Predictions of the industry in general show a nearly equal number of respondents predicting an increase in credit-line increase requests and those predicting the level will stay the same (41.4% and 43.1% respectively). This is slightly different than Q2 levels, which had more respondents predicting an increase. In Q3, 45.4% predict an increase in the total number of delinquencies over the next six months, compared to 36.2% predictions in Q2. Similarly, respondents were mixed regarding new delinquencies, with 46.6% predicting an increase and 37.4% predicting levels would stay the same. Observing trends from Q2, respondents in Q3 appear to lean much more strongly toward change in total and new delinquencies versus consistency. By greater than a 2-to-1 margin, more respondents are expecting total delinquencies to rise rather than fall. This reflects the increasingly pessimistic outlook among survey participants.

## The Outlook on Small Businesses Remains Guarded

Looking at the industry as a whole, over the next six months, do you expect:



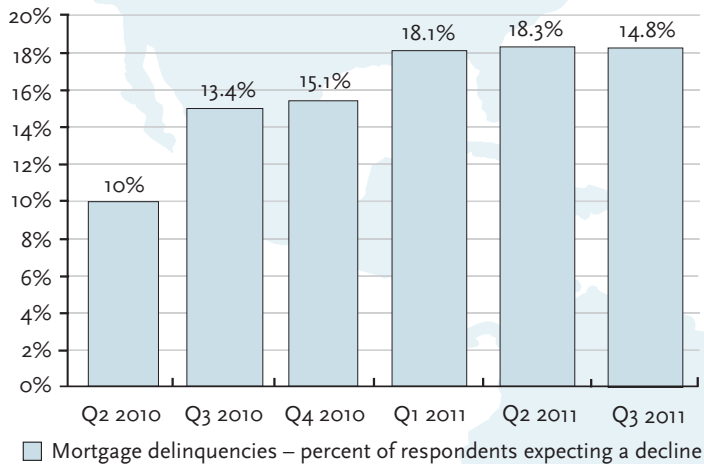
The Q2 PRMIA survey found that respondents' attitudes toward small business growth had cooled substantially since Q1, and Q3's results tend to continue this trend. More respondents this quarter (30.0%) felt that the amount of credit requested by small businesses would remain about the same, compared to 22.6% who felt this way last quarter. This is further illustrated by the 17.3% decrease in those who felt that the amount of credit requested would increase (Q2: 73.8%, Q3: 56.5%). In terms of the approval rates for these loans, beliefs remained quite similar between Q2 and Q3, with slightly less than half of respondents (47.1%) believing that the approval rate would remain the same. Finally, in regards to the amount of credit extended to small-businesses, the trend observed in Q2 of predictions of increase (46% versus 35.9% who felt it would stay the same) has reversed, with only 33.6% now predicting an increase. These results reflect a continued "credit gap" for small businesses between the credit being requested and the credit being extended. This headwind is making it challenging for small businesses to secure financing for both operations and expansion..

## Historical Analysis

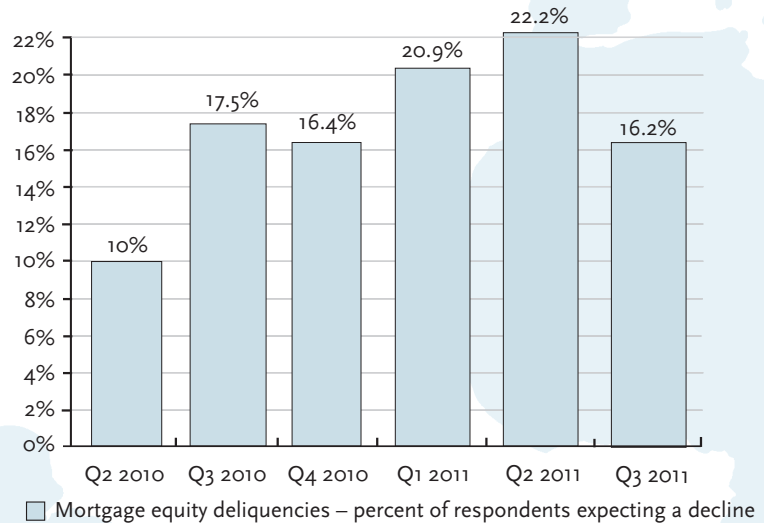
As noted in the previous quarter's report, responses from 2010 were generally more positive than Q2 and Q3 of 2011, with Q1 showing the most optimism in terms of small business growth and delinquency declines. However, it is interesting to note the following in terms of historical trends:

- Q2 2010 saw only 10% of respondents predicting that mortgage delinquencies would drop, and Q1 and Q2 2011 saw this number increase to approximately 18%. However Q3 has seen this optimism decrease slightly, with 14.8% predicting a decrease. This is still higher though than Q2 2010.
- The highest percentage of those expecting the volume of credit and loan applications to decrease was observed in this quarter, 25.5%, surpassing Q1 2010's volume prediction.

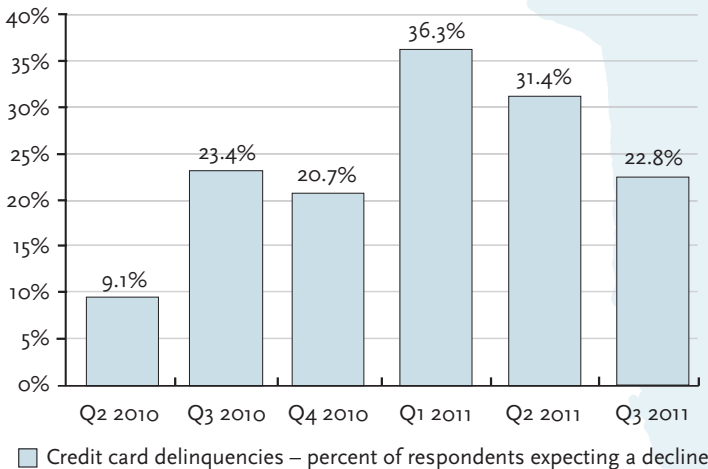
**Mortgage delinquencies expect a drop.**



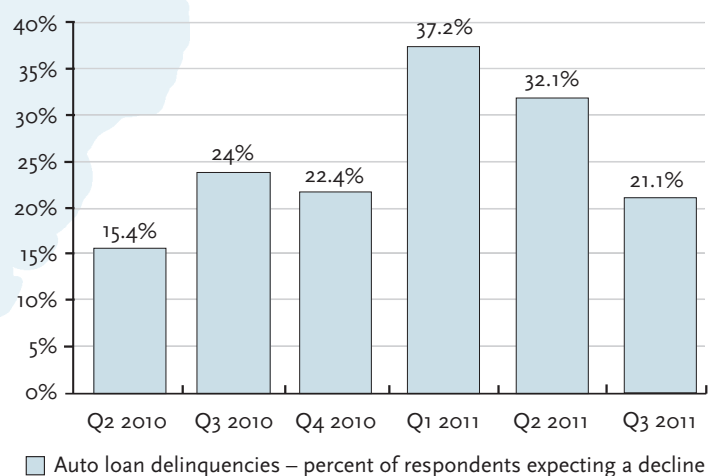
**Home equity delinquencies expect a drop.**



**Credit Card delinquencies expect a drop.**

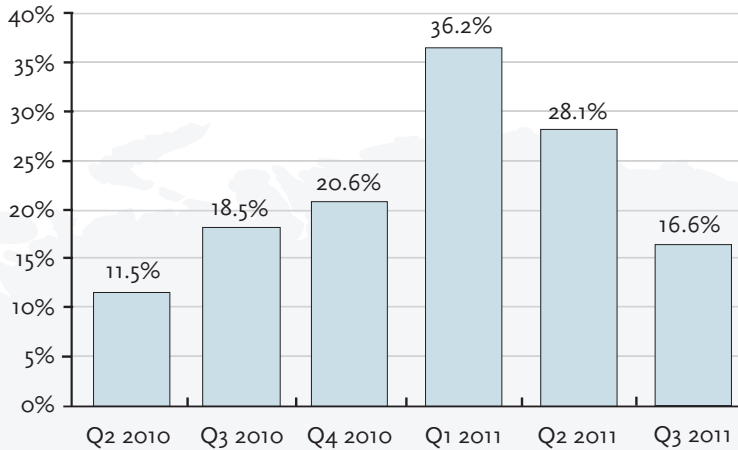


**Auto loan delinquencies expect a drop.**





### Small business loan delinquencies expect a drop.

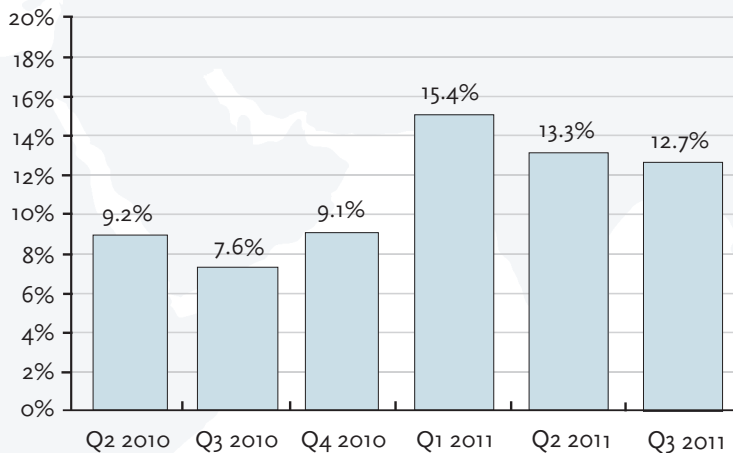


Small business loan delinquencies – percent of respondents expecting a decline

- Similarly, the highest percentage of those expecting credit line increase requests to decrease was observed this quarter, 15.5%.

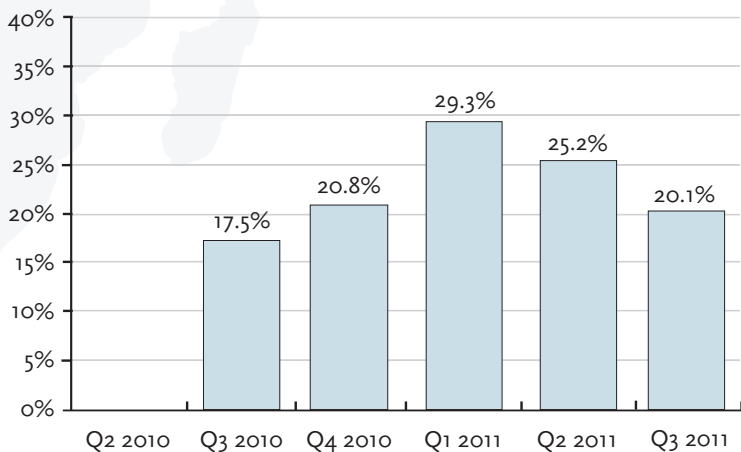
In looking at the numbers, despite the specific prediction differences noted above, it is clear that the optimism observed in late 2010 has waned quite a bit, with Q3 showing a return to early 2010 numbers.

### Student loans delinquencies expect a drop.



Student loan delinquencies – percent of respondents expecting a decline

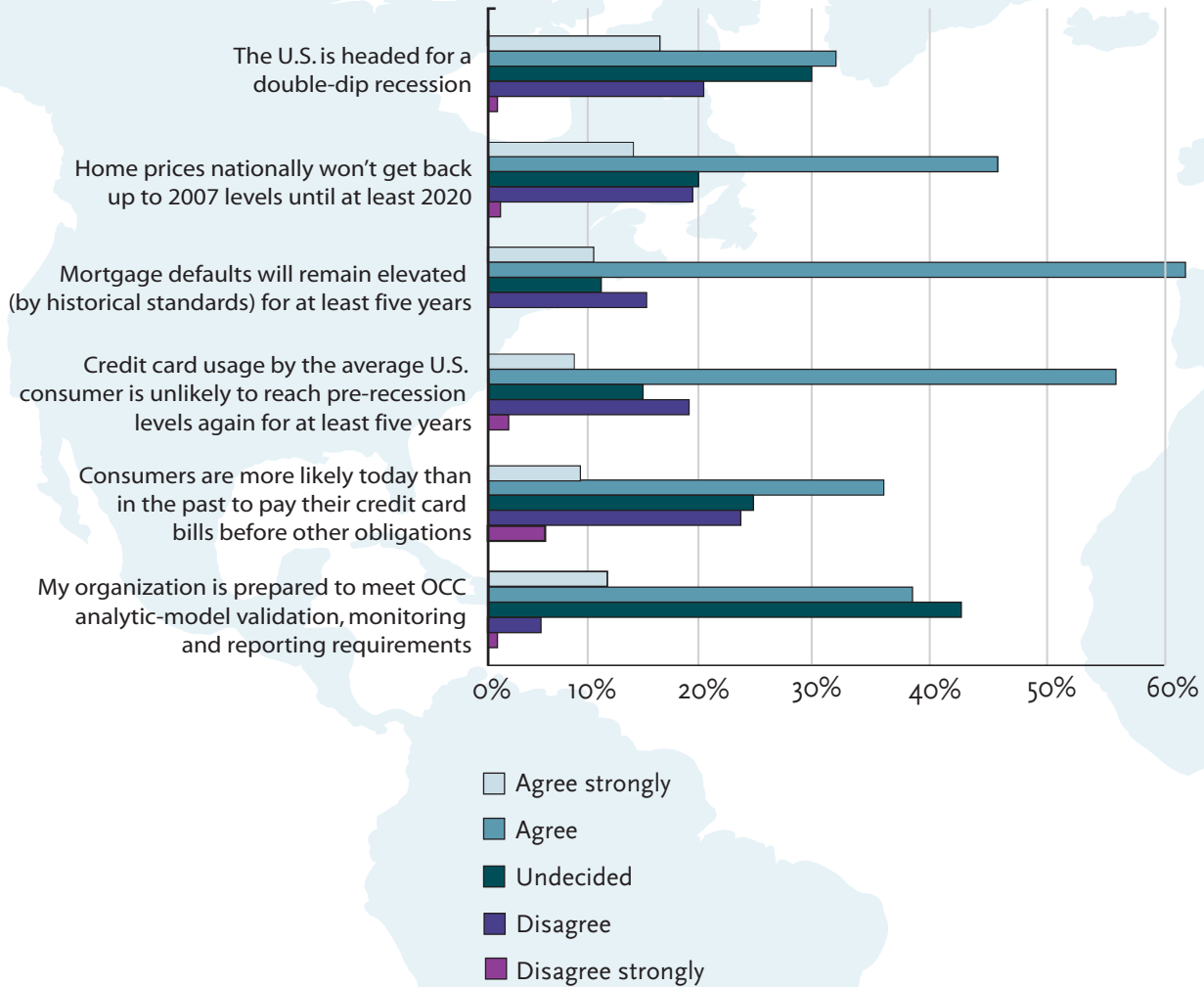
### Total loan delinquencies expect a drop.



Total number of delinquencies – percent of respondents expecting a decline

## Looking Ahead

Choose the answer that best describes your sentiment:

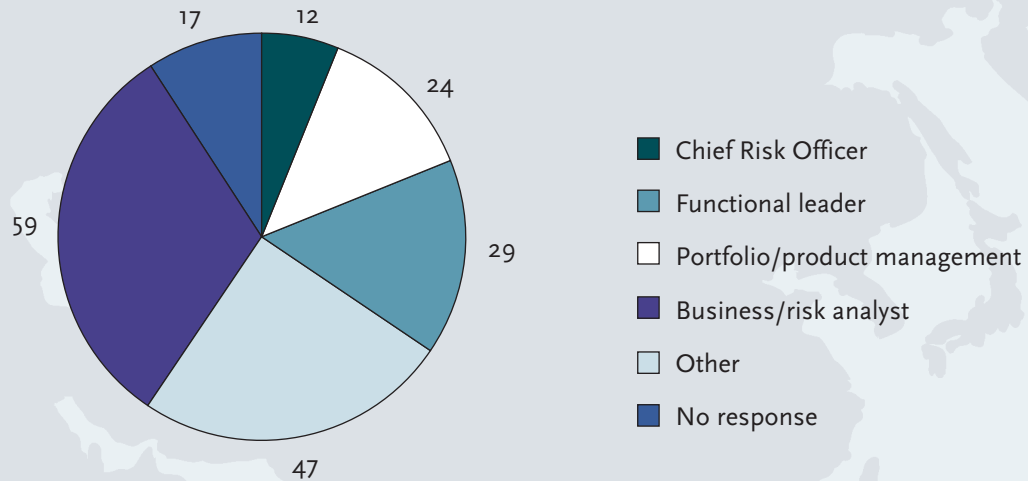


The PRMIA survey asks a number of topical questions each quarter, gauging risk managers' beliefs regarding the impact of financial news and developments. In this quarter, a belief held by almost half (48.9%) of respondents was that the United States is headed for a double-dip recession.

Additionally, 59.3% of respondents don't predict home prices to get back to 2007 levels until at least 2020. Continuing the trend of negative beliefs, 73.1% believe that mortgage default rates will remain elevated for at least five more years, and 63.9% do not believe that credit card usage will reach pre-recession levels in less than five years. In regards to consumer debt payment strategy, attitude was mixed, with 45.1% believing that consumers were more likely today than in the past to pay off their credit card bills before other obligations, with 29.8% disagreeing with that assessment. Finally, slightly less than half (43.2%) of the respondents polled were unsure if their organization was prepared to meet OCC validation, monitoring, and reporting requirements.

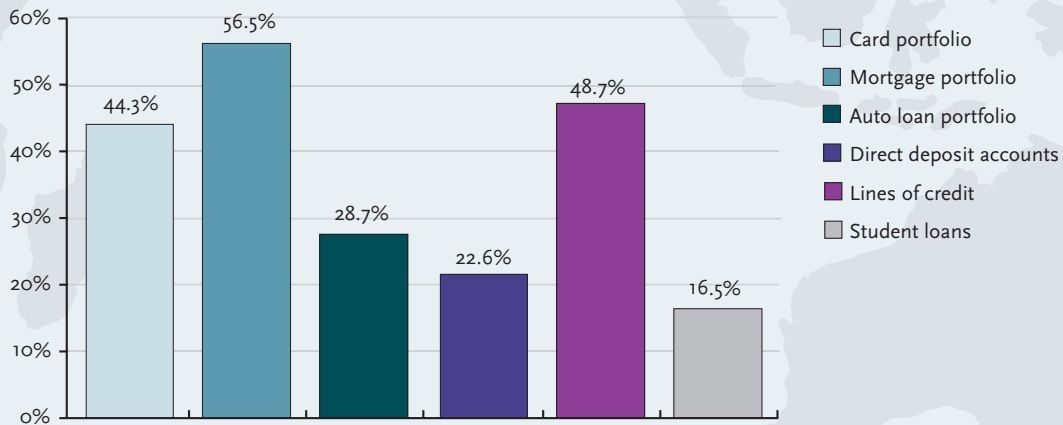
## RESPONDENT PROFILE

### Your job (select most appropriate)



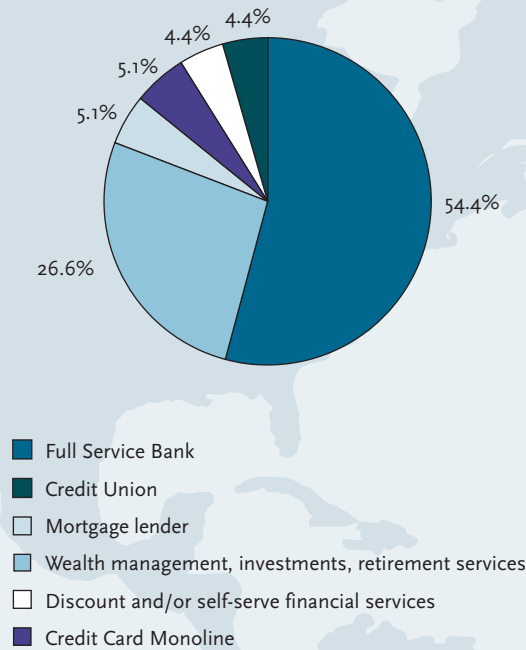
188 respondents completed the survey, with 34.5% of respondents identified as a Business or Risk analyst, and 7% identified as the Chief Risk Officer of their company (a decrease in Chief Risk Officers over the previous quarter). 14% work in portfolio or product management.

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

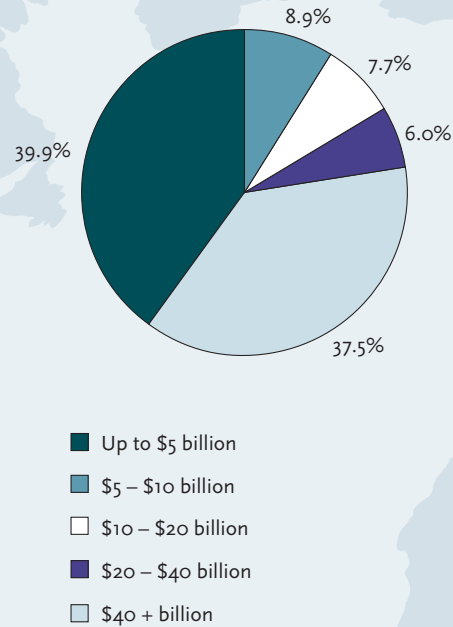


The majority of respondents (56.5%) were trusted with managing a mortgage portfolio. Around half were responsible for a card portfolio or lines of credit (44.3% and 48.7% respectively).

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



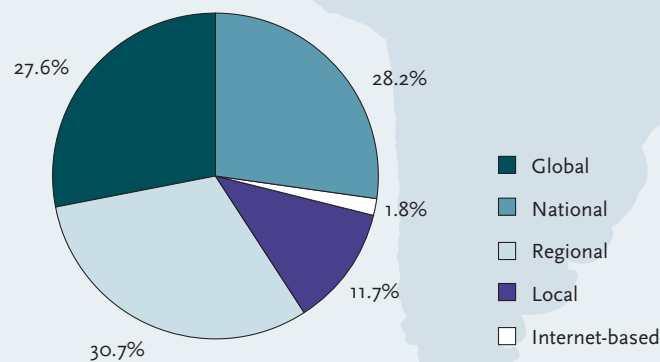
### What is the size of your institution (by total assets)?

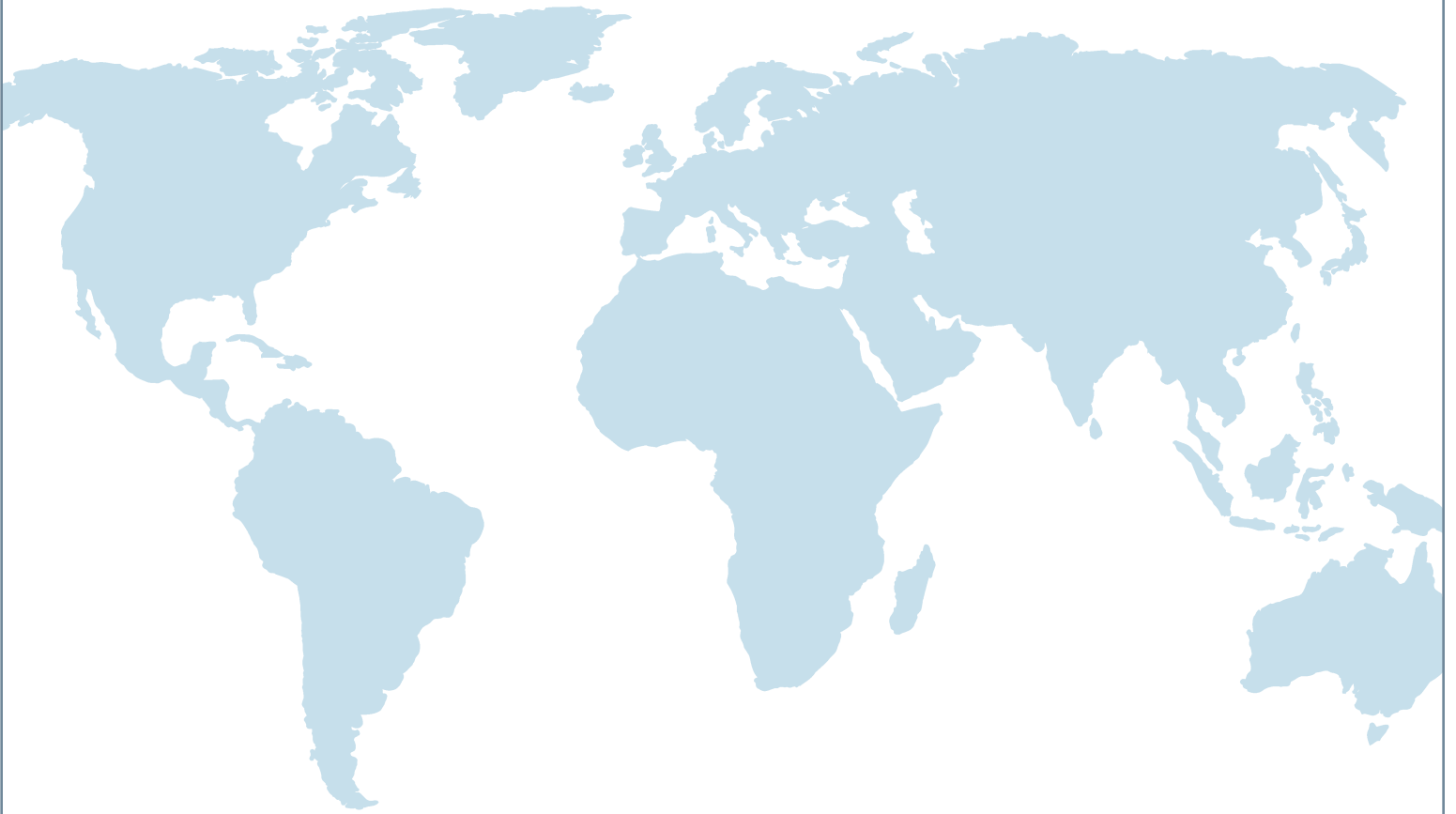


Finally, 37.5% work at companies with more than \$40 billion dollars in assets, with a bit more than a third (39.9%) working at a smaller firm (up to \$5 billion in assets). Most (54.4%) work at full service banks, and slightly over a quarter (26.6%) work at a firm specializing in wealth management, investments, and/or retirement services.

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

Many respondents (58.9%) worked at an institution with regional or national reach.





**FICO**<sup>TM</sup>

[www.PRMIA.org](http://www.PRMIA.org)

