

AFFORDABILITY XMetric

In response to a marketplace that is growing increasingly concerned about the issues of over-indebtedness, DecisionMetrics has introduced its unique AffordabilityMetric solution.

For many forms of credit it is becoming politically unacceptable to merely assess the propensity of an applicant to repay the debt without gaining an understanding of the applicant's ability to repay.

Appreciating that this is not as straightforward as it sounds, DecisionMetrics has developed AffordabilityMetric to provide lenders with a scalable product that ranges from an "out of the box" solution using a generic set of parameters, to a comprehensive tailored solution designed to fit exactly the profile and circumstances of a lender's applicant base and product portfolio.

The product will ensure that lenders do not fall foul of any adverse publicity caused through the inability to identify that a new loan will push an already heavily indebted applicant into an over-indebted situation.

Description of Product

The concept was to build a solution that could cope with limitations in data. If every lender had a full breakdown of income and expenditure, life would be easy but most do not and there needs to be a way to model external information to derive substitutes for the missing values. It is in this area where much of the sophistication lies as it is relatively straightforward to calculate affordability once you have suitable data.

Given there is no reliable substitute for Income, this must be available for the AffordabilityMetric to be calculated. For expenditure it uses a combination of bureau data and other external data sources to derive the level of indebtedness. It then puts that indebtedness into context by comparing it with the income to generate five key affordability ratios.

These statistics are similar to those calculated by many lenders and given that they are likely to be more robust, they can simply be used as substitutes. However, whilst knowing an applicant's affordability position today is quite useful, it is much more powerful when combined with a prediction of their future affordability position. Therefore, in addition to key affordability ratios, AffordabilityMetric contains a statistical model that delivers this future affordability prediction.

This enables AffordabilityMetric to add real value to the affordability assessment. Not only is it possible to identify those applicants that are clearly over-indebted and thus prevent a lender from making the tabloid headlines, it is also possible to identify applicants that are likely to suffer some future financial stress, therefore allowing the lender to refer the case for further investigation.

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AffordabilityMetric

The AffordabilityMetric provides an estimate of an individual's committed income, debt burden and an index. It is this index that is most commonly accessed as a ranking model that ranges from 0 – 100 providing a strategic tool that can be used alongside traditional credit scoring models.

Model inputs are a combination of lender supplied, credit bureau and publicly available data sources. Minimum inputs are:

- Income details covering annual or monthly gross or net income. Where available bonus and overtime details can be included.
- Credit commitments sourced from one of the three credit bureaux. The AffordabilityMetric delivers the same outputs regardless of the credit bureau used, however the calculation method varies according to the data supplied by each credit bureau.
- A set of application details that assist in the estimation and calculation of expenditure items. These criteria (covering age, marital status, residential status and number of dependants) can be provided in the most convenient format for the lender.

From these inputs the model calculates the AffordabilityMetric outputs using a range of direct calculations and estimation models dependant upon each individual's demographic profile. Where 'missing' or incomplete data is found, estimation models are used, which have been developed using techniques similar to credit scoring.

Whilst primarily aimed at those instances where income is available the AffordabilityMetric also provides a ranking tool based solely upon expenditure to enable those lenders to review and control exposure to over-indebted individuals.

IndebtednessMetric

There are many circumstances where it is not possible or desirable to capture income details; this is most applicable in the point-of-sale industry where capturing any sensitive personal information is difficult.

For these circumstances DecisionMetrics has adjusted the solution to provide an indication of an individuals indebtedness levels and it is then possible to derive the likely gross annual salary required to support this.

The Indebtedness model provides an index, ranging from 0 – 100 which indicates the comparative level of indebtedness that an individual has.

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Strategy

DecisionMetrics recommends that the use of an affordability measure within a credit strategy is best served by producing a matrix of credit score and affordability. It is often the case that over-indebted customers have a clean credit record and are therefore assessed as good credit risks. Overlaying an affordability measure on top of the risk assessment will identify these conflicts and allow an integrated strategy to be developed.

Prior to implementation, DecisionMetrics will help to devise this strategy by undertaking an analytical exercise to produce a matrix of credit score by AffordabilityMetric.

Implementation

The model has been implemented within DecisionMetrics' own decision software to allow a quick and convenient implementation method. The AffordabilityMetric for each Client is delivered as a web service that calculates the outputs according to a lender's specific set of parameters. Where the 'standard' sets are used the solution can be taken immediately.

DecisionMetrics can also provide the solution as a web service hosted externally to the lender's systems. This method still delivers all of the functionality associated with a software implementation approach.

For more information on *AffordabilityMetric* visit www.decisionmetrics.co.uk or call Gary Scott on 01707 282640.

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