

# Northeast Member Business Services

## Small Credit Business Scoring

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# Northeast Member Business Services

## ■ AGENDA

- Background and history
- Validation limit trends
- Industry data from 2004
- Critical scorecard information
- Scorecards and Odds
- Implementation steps
- Questions and answers

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## ■ Background & history

- Collaboration by major banks and Fair Isaac in the 80's
- First release in late 80's validated to \$150,000
- Mid 90's validation raised to \$250,000
- Release 6 (late 2005) will raise validation limit to \$750,000

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50 years modeling experience

Data neutral

15 years small business modeling

Able to leverage  
all of FI capabilities

More than 500 clients  
22 of top 25 small business  
credit grantors

Fair Isaac Models

New Releases

Predicts risk

Regulatory recognition

Extended analytics

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## Business objectives

Increase profitable relationships

Manage overall portfolio risk

Streamline operations for increased cost efficiencies

Maintain regulatory compliance

## How scoring helps

Allows SAFE portfolio growth

Accurate risk prediction – risk is identified at origination

Faster turnaround times by establishing approval criteria

Regulators like consistent, objective decisions

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## Business objectives

Control credit quality

Minimize expense

Maximize revenue

Improve customer relationships

## How scoring helps

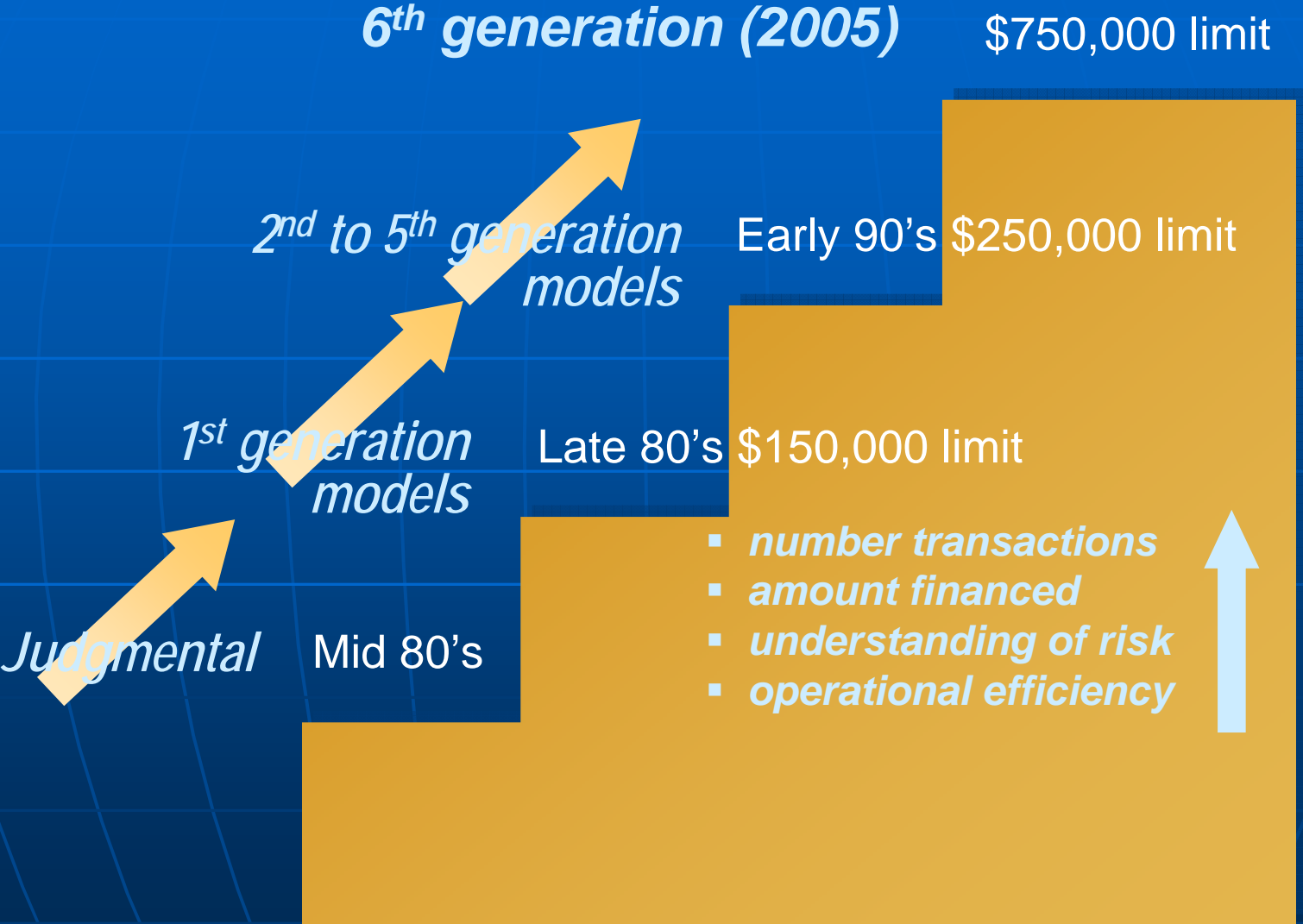
Manage delinquency and loss

Manage workload  
Control operational costs  
Reduce attrition

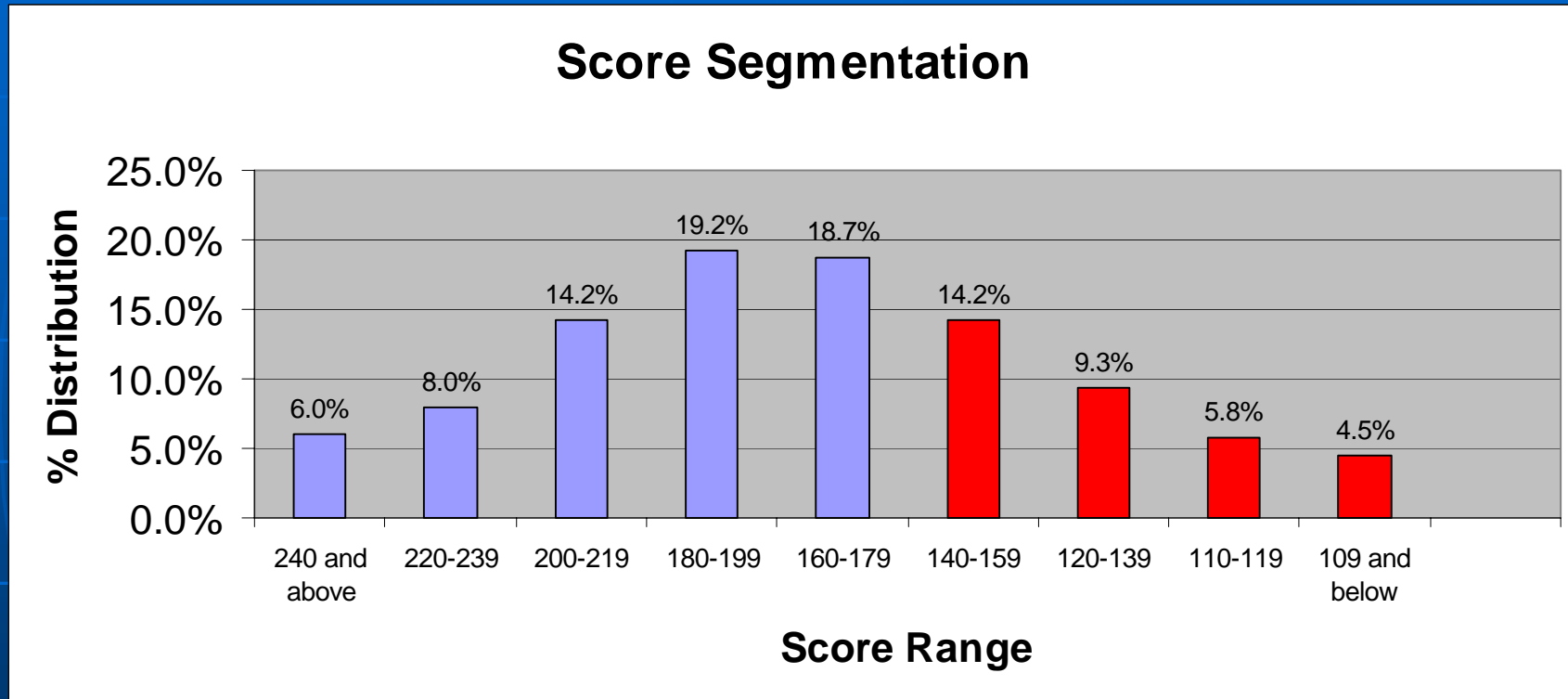
Target promotions

Improve retention

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**Release 5 historic score distributions w/o D&B –  
score is a predictor of future performance**

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## 2004 Industry Portfolio Facts

- Average portfolio size \$65 million
- Average annual production is \$16 million
- Average loan life 50 months
- Average borrower has 1.29 products
- Average charge off rate is 48 basis points

2004 DQ data	30 Days Past Due	60 Days Past Due	90 Days Past Due
<b>Underwriter</b>	0.02%	0.00%	0.00%
	\$13,157	\$0	\$0
<b>Dedicated Portfolio Manager</b>	0.16%	0.06%	0.10%
	\$105,259	\$39,472	\$65,787
<b>Relationship Manager</b>	0.86%	0.30%	0.43%
	\$565,768	\$197,361	\$282,884

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## Principal 1 Data

- Application
- Consumer credit bureau report



## Principal 2 Data

- Application
- Consumer credit bureau report




## Business Data

- Application Information
- Financials



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Characteristic	Judgment	Credit Scoring
Years in business	+	36
Business DDA balance	+	32
Debt / worth	-	15
Cash / total assets	+	23
Principal income	Neutral	20
CB score	-	2
# of inquiries	-	7
% satisfactory on bus. report	+	25
# of derogs. on bus. report	+	29
<b>Overall decision</b>	<b>+ Accept</b>	<b>189 Accept</b>
<b>Odds of repayment</b>		<b>21:1</b>

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- Scorecard data for release 5.0
  - Two basic groups 'derog' and 'non-derog'
    - 'non derog' – no more than 2X30 on CB
    - 'derog' – more than 2X30 or 1X60 on CB
  - Eleven scorecards
  - Scorecards predict behavior
  - Collateral - not a scored field – regulatory issue
  - By adding FICO score, acceptance rates can change

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- Criteria that is scored
  - Principal's DDA balance
  - Time as owner
  - Time in business
  - Principals' income
  - Credit bureau data (7 factors)
  - Business Financial data
    - Net Profit
    - Current Maturities of Long Term Debt
    - Cash
    - Earnings
    - Total assets
    - Total liabilities
    - Net Worth
    - SIC Code / NAICS Code

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- Odds and Predictability Tables (Proprietary to FI)
  - Cutoff scores of 80-230 (vary per table)
  - Acceptance rate if cutoff score is the sole approval criteria
  - “Bad Rate” – the rate expected to go 1X60 at the cutoff score
  - Odds of Acceptance –how many apps score in that range
  - Odds at Cutoff (odds of going bad, see bad rate)

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- Scorecard characteristics (release 5)
  - Based on 25,000,000 transactions
  - Cutoff scores, combined with FICO score manage predictability
  - 20 Points doubles or halves 'bad' probability
  - Odds at a certain score are the same from card to card
  - Top end score has 40 to 1 odds, low end score has 1 to 1 odds
  - Score (and odds) determine risk based pricing

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- Critical Implementation Items
  - Experienced program supervision
  - Users and user authorities
  - Approval / decline cutoff scores
  - Gray area strategy
  - CU-defined fields / questions
  - Restrictive override criteria
  - Pricing matrix development

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- Base rate – the rate ‘base’ such as WSJ Prime
- Base margin – a fixed margin from the base
- Risk tables – risk-based pricing
- Loan interest rate = base rate + base margin + risk table margin

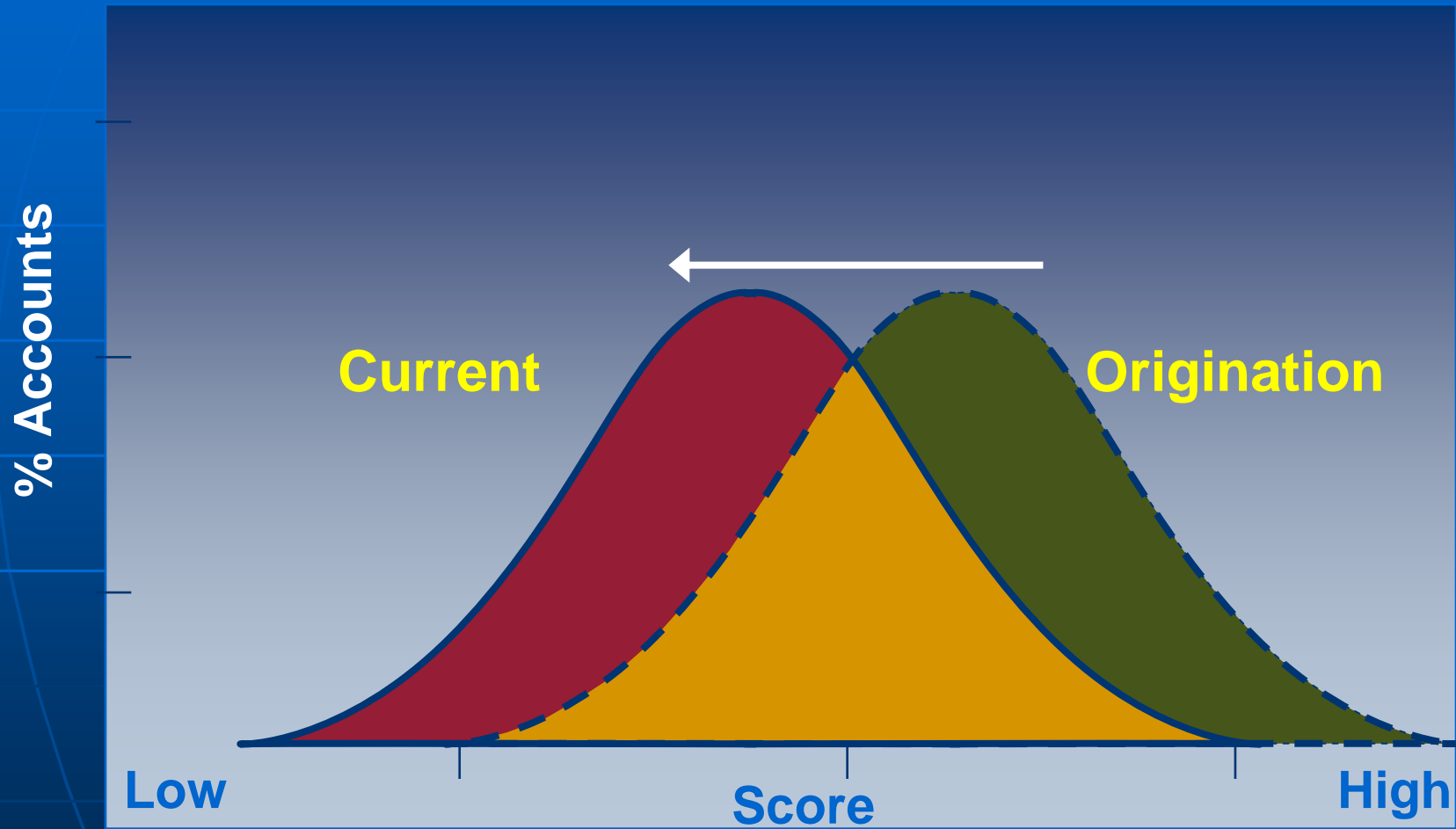
<b>RISK TABLE</b>	<b>Credit Score</b>			
<b>CB score</b>	<b>0-159</b>	<b>160-175</b>	<b>176-190</b>	<b>&gt;191</b>
<650	Decline	Decline	Decline	Decline
651-680	Decline	3.00	2.00	1.50
681-720	Decline	2.00	1.50	1.00
>721	Decline	1.50	1.00	0.00

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- Underwriting:
  - Meets the market expectation
  - Meets the MBL policy standard
  - Meets regulatory standards
- Servicing
  - Meets the competition (banks)
  - Delinquency and problem loan management

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Scoring allows for automated portfolio analysis



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- Questions and answers
- Contact information:

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**THANK YOU!**