Planning, Analytics, and Expertise: Keys to Implementing a Portfolio Management Strategy

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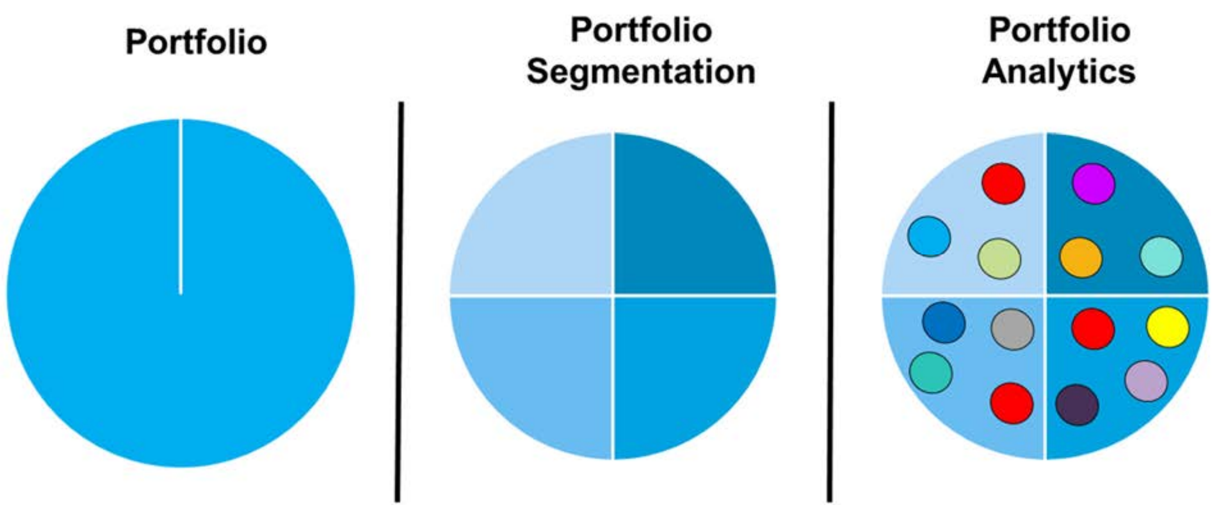
An effective portfolio segmentation strategy will help you engage your cardholders better, respond to their financial needs, and bring profitability to your portfolio. With the right design in place, you will be able to directly affect key business metrics through operational campaigns for both credit and debit card accounts.

Segmentation as a function classifies accounts into groups; applying portfolio analytics adds depth. Rather than dealing with customers as a broadly defined group, the analytic tool might use a set of instructions to discern "all cardholders on the books greater than five days that have not transacted," "debit card users with high demand deposit account balances and with no card transaction activity," or "credit card holders with high credit lines and low usage." Managers can better identify specific account segments with low usage, missed transaction opportunities, and declining activity, and then integrate a targeted marketing strategy.

As Figure 1 illustrates, the portfolio analytic tool creates a granular cluster of accounts. By using a concise definition, portfolio managers can hone in on specific account types and then target actions against each group.

Figure 1: Portfolio Analytics Add Depth to Segmentation



Source: CEB analysis.

The recipe for defining particular groups relies on a review of fields within the account record, or depending upon the complexity of the customer file, multiple records. Once used primarily by large issuers, segmentation tools are now available to financial institutions of all sizes. The real power of segmentation and analytics comes not from the tool itself, but in how it can identify particular account types and facilitate actionable campaigns to achieve a result. Campaigns that follow through with offers to stimulate transaction activity and card usage complement the science of analytics with the art of portfolio management.

An imperative feature of a portfolio growth strategy is the ability to interact with the customer on a one-to-one or one-to-many level based on a series of account actions and conditions. Once a connection occurs, the cardholder can be incented, prompted, or pushed to sustain or increase transaction activity. The result feeds into the portfolio management revenue stream. Campaigns run on demand or tie to events such as account activation, holiday shopping, reduced usage, or cross-selling opportunities. In this manner, portfolio expertise and analytics can boost usage, increase transaction volume, and improve both interest and fee income.

Managers may also use analytic tools to mitigate risk as a complement to existing systems. Portfolio analytics are not intended to replace collection and fraud controls, but they can provide tools to quickly identify certain account segments and create actionable workgroups. As an example, following a data breach at a major retailer, the analytic tools could identify every account with a purchase at an affected retailer and then create workgroups to close and reissue, or simply notify the customer that the financial institution is aware of the condition and future transactions will receive an additional level of scrutiny. Similarly, a manager might use portfolio analytics to keep a watchful eye on new accounts that could receive a more aggressive action should a first payment default occur. It is important to note that while some of the identification features might be available within the collection or fraud system, the portfolio analytic function adds a layer of protection to cross-check and ferret.

In the pages that follow, we discuss why the timing is right to implement a clear portfolio strategy, what features you should incorporate into a robust plan, and how you can implement an effective management process.

Take Action Now

The payment card industry moves at a fast pace. Industry estimates by the Nilson Report indicate US retail card payments will surge between 2009 and 2019, from 107.5 billion transactions to 362.1 billion. During that same period, credit volumes will more than triple as debit quadruples. Between 2004 and 2017, the Federal Reserve's most recent triannual payment study projects card-based transactions will continue to displace cash; cash transaction volume will fall nearly in half, from 40.2% of total to only 22.0%. At the same time, all cards will generate 61.5% of transaction volume, up from 31.9%. Within this growth, best practice research and technology firm CEB projects mobile payments will spike from the US Department of Commerce's 2009 estimate of 3.6% of total retail sales to 12.1% in 2019.

These metrics all point to growth for issuers, though it is important to note the uneven distribution of both debit and credit cards to top-tier financial institutions. National banks dominate the US industry; the general rule of thumb is that the top 12 issuers account for 85% of portfolio value, leaving the remainder for regionals, community banks, and credit unions.

Amid this growth is the entrance of modestly regulated participants looking to seize revenue from financial institutions. Payment initiatives range from companies firmly established in payments, such as PayPal, to technology companies including Apple and Samsung who aggressively encroach the space. In short, volume growth will continue, competition will intensify, and now is the time to make the most of your card portfolio.

Protecting and growing your portfolio begins by understanding account behavior and ensuring your offerings fill cardholder needs. An enhanced portfolio management strategy will help you maximize cardholder potential and will deepen your card relationships, driving engagment and loyalty. Setting the foundation with powerful tools and proactive strategies will better position your financial institution for the highly competitive payment world now and in years to come.

Create an Action Plan

Implementing an enhanced portfolio segmentation strategy requires seven major steps as shown in Figure 2. Defining the objectives of the strategy is at the top of the order because there must be a clear vision of the end result.

Figure 2: Segmentation: Seven Steps to Rapid Implementation

Source: CEB analysis.

Depending upon the departmental configuration, a user may decide to attack credit card receivables or debit card accounts; both card products share the same objective of increasing overall transaction value and volume to increase non-interest revenue lines. Credit accounts also offer potential to increase revolving debt and interest revenue.

Selecting the right analytic tools will typically be based on whether the issuer uses a full-service card platform provider or runs their platform in house. If the former is the case, the likely option would be selecting an offering from the platform services provider; if the provider is well-established in the industry, they will have the tool readily available and implementation may be as simple as turning on access through the account representative.

Once objectives are defined and analytic tools are selected, issuers should consider using expert skills to get the process started quickly. The use of consulting resources is a favored way to accelerate the impact of an enhanced segmentation strategy for three reasons: 1) consultant resources typically have experience in working these tools through the entire credit cycle and can implement rapidly; 2) if the resources are attached to the platform services provider, there will be no learning curve that could slow down integration; and 3) the service provider will often have multiple routinized campaigns available which can be adjusted to the individual needs of the issuer. An additional benefit of using external resources is that the issuer will not have to be dependent upon a particular employee to manage integration and execution of the program.

Setting goals and targets fall into the strategy as the fourth step. With broad objectives defined, such as increasing non-interest revenue and tools selected, the issuer should work with their expert to set specific and measurable goals, and compare their results to their peers. These goals might be to ensure all newly booked debit card accounts are activated within ten days of card receipt; if not, reach out with a reminder message that the card is ready to use. Another example, in an effort to create lift on credit card interest revenue, might be to run a campaign around a birthday or the holiday season reminding the cardholder of a transaction bonus, open-to-buy, or the availability of new loan product.

Creating a plan and executing, steps 5 and 6, amplify the importance of expert skills. The issuer should expect the consulting resources to drive them toward attainable and realistic goals that link to the overall strategy of enhanced portfolio segmentation.

The final step, review and adjust, is essential because it requires you to measure your results against the original objectives, goals, and targets, and then assess the results achieved by your campaigns. The constant learning that gets recast into action is essential. A segmentation strategy is not a one-and-done exercise; it should be part of your customer strategy to maximize customer satisfaction, portfolio health, and profitability.

The next two sections discuss ways to approach credit and debit card accounts which have different customer value propositions. Credit card accounts have the potential to generate both interest and non-interest revenue. As cardholders transact against open credit lines and carry balances from month to month, issuers assess interest for servicing the account risk; fees generate from merchant interchange, the cost of acceptance at the point of sale, plus any other transactional or punitive charges associated with the cardholder terms. Debit cards rely on merchant interchange because they access available funds in the cardholder's daily demand deposit account (DDA) and are part of broader retail relationship with the consumer.

Find Value in Your Credit Card Accounts

By selecting a series of conditions or account characteristics, the portfolio manager can readily segment their accounts into broad groups. Figure 3 illustrates a simple segmentation model regularly used by financial institutions to classify credit card accounts; a variant model for debit cards follows in Figure 5.

Figure 3: Credit Card Segmentation: Mutually Exclusive Groups

Transactors Regularly Purchases and Settles Balance

- Monthly Pay Off, Does Not Carry Forward a Balance
- Only Card Fee and Interchange Revenue

Revolver Carries Balance from Month to Month

- Generates Interest Revenue in Addition to Fees and Interchange
- Most Profitable Segment of Credit Card Business

Inactive No Balance, Not in Use

- Limited Revenue Opportunity
- Contingent Credit Liability

Paydown Not Actively Purchasing, Eliminating Balance

- No Recent Charging
- Reducing Debt

Source: CEB analysis.

By selecting a set of mutually exclusive account-level features, the portfolio manager would simply group four important credit card segments: Transactors, who regularly use their cards to settle their balances within the billing cycle; Revolvers, accounts that carry balances from month to month; Inactive, dormant cards with no activity in N days; and Paydowns, accounts in the process of liquidating their balances.

These groups break down accounts based on their payment behavior, but adding a deeper level with portfolio analytic tools will permit you to deal with finer customer groups where you can target your message more strategically. As an example, consider the Revolver group and how risk varies on those who use more than 75% of their credit line, versus those who only use 25%, or add in another attribute that considers the length of the cardholder relationship as new or established.

Rather than requesting a special processing run to categorize these broad sub-groups, a portfolio manager or the industry expert could perform this simple analysis or could define more granular workgroups, as shown in Figure 4. Instead of generating a systems request to classify Transactor, Revolver, Inactive, and Paydown groups using current and previous balance, the manager can add attributes to the mix and isolate accounts of interest.

WHAT THE BEST COMPANIES DO

Figure 4: Credit Card Segments: Eight Workflow Examples

Segment	Date Became Member	Line Value	Utilization Rate	Balance Versus 3 Months Ago	Action
TRANSACTOR	New (<1 Year)	Any	Moderate (20-40%)	N/A	Assess Line
	Established (1-3 Years)	Moderate ($3-5,000)	Low (10-20%)	Stable (90-110%)	Encourage Usage
	Long Term (> 3 Years)	High (>$5,000)	Low	Stable or Decreasing	Reward
REVOLVER	Established	Moderate	High (>40%)	Increasing	Increase Line
	Long Term	High	Low	Stable	Reward
INACTIVE	<30 Days	Any	None	N/A	Trigger Account
	>30 Days	Any	None	No Balance	Encourage Usage
PAYDOWN	Any	Any	Any	Decreasing	Reward

Source: CEB analysis.

Instead of dealing with a small issuer portfolio of 100,000 accounts, the model might cull out 5,000 inactive accounts, but the portfolio analytic tool would drill down the work group to be 23 accounts that were booked, but did not trigger.

For the Transactor pool, the manager could also pull out new accounts on the books less than a year with moderate use of the credit line. A simple series of tests could be run to see if the customer might use their account more if they have a higher credit line. The credit line value could be tweaked, and the test could be done on credit lines less than $1,000, or perhaps only those accounts with credit lines greater than $4,000.

This deeper view of the customer can continue through other segments, such as identifying Revolvers who maintain moderate lines and use a significant portion, suggesting the possibility of a credit line increase to generate more interest income. The opposite tact could occur, reducing a high credit line on a customer that rarely uses the credit, to shield against the contingent credit risk.

In creating these analytic cells, portfolio managers can build broad or granular groups of accounts. Each one of the groups in the above table could be reduced into finer segments if additional attributes such as cash advance usage, EMV card activation, active Daily Demand Account (DDA) indicator, or multiple cardholder flags were layered into the tool.

A well-designed portfolio analytic system enables a manager to cluster broad or highly defined account groups. Broad definitions such as “all credit accounts” might be used to balance the receivable, in contrast to defining a dataset that might only call for credit card reward accounts booked between September and December 2015 and have no purchase activity. This would result in compilation of new credit cardholders that did not use their account, creating an action group that should be called or contacted to understand why the account has not been used. A friendly call or perhaps a reward incentive might activate the account and ignite a revenue flow.

Embrace the Full Value of Debit Cards

The portfolio analytic strategy works similarly with debit cards; revenue opportunities are typically lower than credit products since debit accesses current cash in DDA accounts and credit offers revenue from risk-based interest. Consider the logic used in the credit card example in the context of debit cards. Since debit cards are cash access products, they do not revolve; every customer transacts so in this example we discard the revolver and transactor segments. Here we are more concerned about usage and create four groups centered around activity, as shown in Figure 5. The first cluster looks at whether the customer has ever used the card, and if not, or they have been inactive, they slot into the first group. Then by using the portfolio analytic tool, simply parse the groups into high-, medium-, and low-usage categories. This might require adjusting as groups are defined, but the categories provide a similar level of visibility as we saw in the credit card segmentation model.

Figure 5: Debit Card Segmentation: Mutually Exclusive Groups

Non-User/Inactive Card Not Issued or Not in Use

- Card Never Issued or Never Activated
- Issued Card but No Recent Use

Low Usage Limited or Erratic Transactions

- Occasional Transactions
- Small, "No-Cash-in-Pocket" Purchasing

Moderate Usage Regular Usage but Not Fully Committed

- Routine Low Ticket Buying
- Consumptive Spending

Heavy Usage Prefers Card over Cash for Routine Purchases

- Most Profitable Segment
- Committed to Debit Card Usage

Source: CEB analysis.

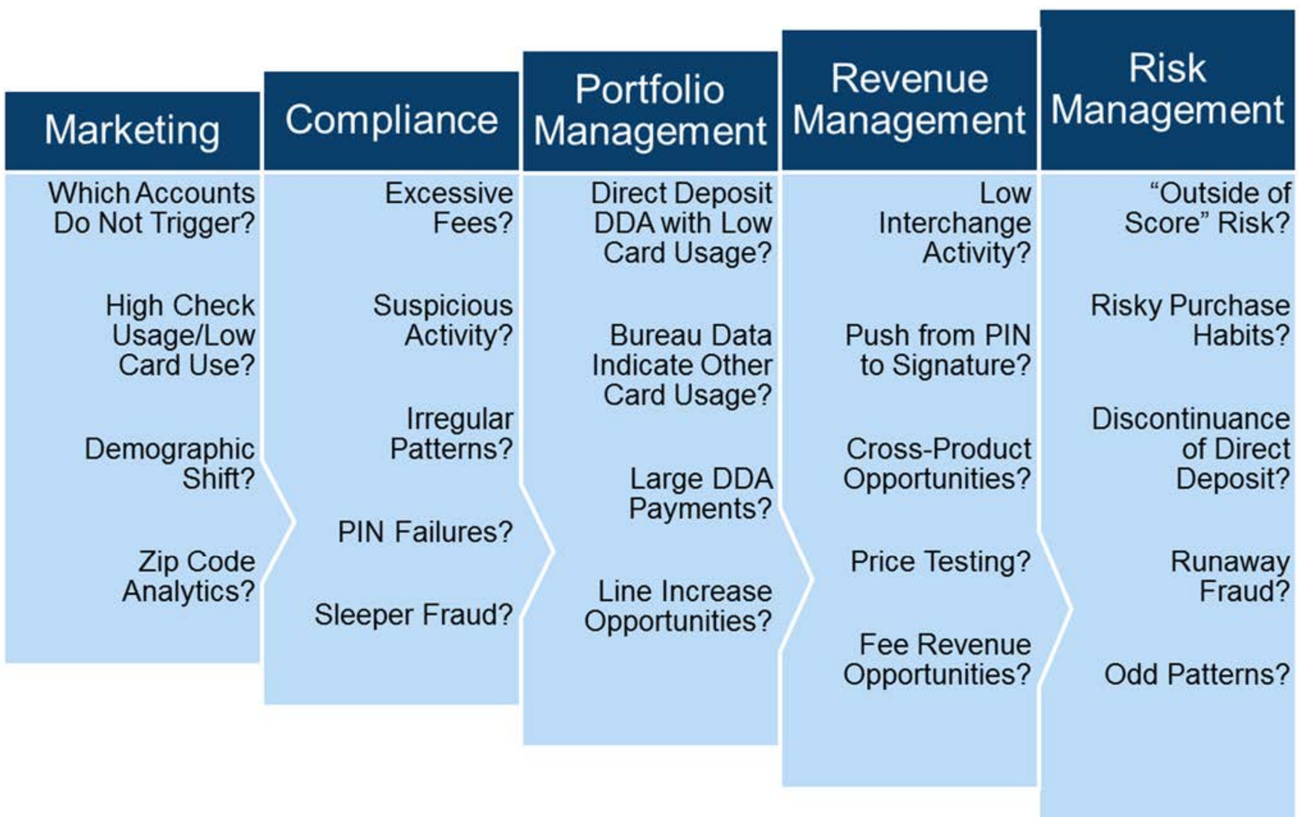
The use of the analytic tool should not be limited to the portfolio management function. Other functional areas, responsible for tasks ranging from acquisitions to risk management, can use the tool to audit, ferret, or simply explore the behavior of the customer base, and create incentives to move behavior in a desired direction.

Portfolio Analytics: From Marketing Strategy to Risk Management

When banks consider justifying the cost of a portfolio analytics function, they should understand that the tool can be used by many functional groups. Portfolio analytic tools are not limited to the portfolio manager who wants to search for account-level revenue opportunities. Entitled users can span the enterprise and service a wide variety of requirements, whether the interest be to create a dashboard summary of events, an exception report, or a worklist. More sophisticated users can spool off accounts into a workgroup that could interact with an autodialing machine or integrate with a direct mail campaign, another point for expert support.

Figure 6 illustrates potential use cases across the credit cycle with Marketing, Compliance, Portfolio Management, Revenue, and Risk areas in mind. A compliance manager, for example, might want to audit how Fraud managers handle particular transactions, such as any purchase greater than $7,000, though they might want to exclude those transactions involving a payment to an educational institution, which can be done by simply excluding Merchant Category Code (MCC) 8220 for MasterCard or the Visa equivalent.

Figure 6: Cross-Functional Uses for Portfolio Analytics



Source: CEB analysis.

From the cross-selling lens, one could easily identify candidates for a potential automobile loan by looking for regular transactions coded to MCC 5511, automotive repairs, or watch for transactions coded for casual dining (5812), fast food (5814), and nightclubs (5813), and then build assumptions on how cardholders might fit into additional retail lending products.

The transaction might flow through the normal approval process in the production system, but the compliance manager could independently identify the transaction and audit every action along the way. Risk managers might also look at newly issued EMV cards to understand if cardholders are increasing or decreasing usage after chip issuance, and perhaps add reward incentives or educate the customer on the importance of EMV implementation.

To be sure, large banks do similar analysis when they move into your local bank footprint. They can mine their data for activity at certain merchants that could be outside of their traditional markets, and push local incentives to cardholders. With a little effort, analytics can identify small business owners and target them with special products, or even identify customers who might be in need of a term loan based on transaction activity.

Consider the case of the compliance manager who wants to prepare for a Safety and Soundness audit; combing the file, validating that fees are properly assessed, and that multiple collection calls do not occur is an another example.

Despite what you hear on the power of "big data," the morsels developed with "small data" at the account or transaction level are valuable. And with tools currently available, you do not need to be a mega-issuer to get to the data.

Building Strategic Campaigns

Simple querying will provide a wealth of raw data and knowledge, but it is important to put the data into action with routine campaigns. Effective campaigns can wrap around holidays or cardholder anniversary dates, with offers to increase available credit. Reward incentives can also be applied. Whether the card issuer chooses to align with a consultant, or brave it on their own, an end result of the portfolio analytic strategy should be to create customer campaigns that build customer satisfaction and revenue. Depending upon available tools and skills, the marketing manager might want to test groups for credit line increases or perhaps reward cardholders around a holiday.

Putting the data into action, which begins with extracted files, and then linking to direct mail campaigns and branch office solicitations, will generate additional volume, and although a deep discussion is beyond the scope of this white paper, users will find a robust strategy rewarding.

Conclusions

Large issuers have been using portfolio analytic tools for years, and they are now available to a wider audience. The software can be acquired as individual packages or through full-service providers that simply activate the capabilities through the card management system. Portfolio analytics are essential, particularly as payments continue to grow. The tools service portfolio managers, but they are useful throughout the enterprise for additional analytics such as the ability to create dashboards and find particular account conditions. Users can whittle down volumes into actionable groups for customer outreach, or they can use the models to create real-time dashboards that assess performance or augment other systems.

Most programs are intuitive, but consulting support will help define a clear and actionable strategy that increases revenue and deepens cardholder engagement. Issuers of all sizes have the ability to know their cardholders better, find ways to serve, and create actionable insights that help grow the business and generate profitability. Finally, remember that effective strategies require persistence, follow-through, and planning, but the results will reward your organization with better revenue and happier cardholders.