Credit Bureaus: A Challenging Partnership

In the UK, the credit bureaus remain a critical component of successful lending. We discuss how to optimise their usage and benefit while avoiding common pitfalls and high costs.

The triumvirate of UK credit bureaus – Experian, Equifax and TransUnion – remain an integral part of the lending landscape. For all the recent focus on new data sources and techniques, it is a rare lender that does not have at least one touchpoint with the bureaus during their lending decision or customer management. But for many this relationship is not a comfortable one; high costs, byzantine terminology, and poor implementations can lead to a view of the credit reference agencies as a necessary evil rather than a beneficial partnership.

Knowledge is Power

In recent years there has been increasing focus on using alternative data sources in consumer lending decisions. The poster child of this new wave of data is Open Banking, formalising and broadening the screen-scraping technologies that preceded it. Other hot topics include psychometric profiling and use of social media data, both falling under the umbrella of 'big data', another previous industry buzzword.

For all this innovation though, many lenders still pivot their lending decision on a consumer's credit bureau file. The reason for this is simple: this information remains exceedingly powerful. A potential customer's credit history can contain a plethora of information and be a hugely valuable tool in making good decisions. For all the insight afforded by Open Banking (and this *is* huge) it will not show the bills a customer is not paying, the utilisation of credit limits, or the unsuccessful applications for other credit products. And a customer chooses which accounts to give a lender access to through Open Banking; there is no guarantee this is the full picture.

So, credit reference data remains a key tool for almost all lenders, a vital source of insight on potential customers, and a crucial weapon in managing risk and avoiding bad debt. So why do so many lenders respond with a grimace when asked about the credit bureaus?

User Unfriendly?

The world of credit reference data is highly complex and can be difficult to successfully navigate without specialised knowledge. Each of the three credit bureaus summarises and presents data differently, with different definitions and acronyms. Similarly-named variables across different bureaus are not always comparable – for example, 'worst current status' on one bureau will include defaults, while on another it will not. Data can be summarised across different addresses and across joint or associated individuals, or this information can be provided separately.

The three main UK credit bureaus are familiar names

To some extent these variances and complexities reflect the fact that all three bureaus are battling with legacy systems that are not easily updated. Some of the core data blocks returned from the bureaus hold fields with a genesis in the '90s, and even TransUnion (previously Callcredit), the newcomer to the group, has now been operating for 20 years and is no longer the nimble tech upstart it once was.

Exacerbating this is the difficulty the bureaus have in 'sunsetting' any of their products. It has

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been mentioned that for many lenders, bureau data and scores are integral to their business processes and have been optimised over many years and signed off at board level. While this is beneficial for the bureaus on one hand – they are very hard to replace – it also means they face significant resistance to retiring any of their products. The result is that a huge suite of versions of each tool, score or product are available, making selecting the right ones a minefield.

In some ways, it actually works in the bureaus' favour that their solutions are seen as complex and there is a level of mystique around what they provide. The truth is that these businesses often make limited profit from the provision of data itself – the margin comes from the sale of consultancy services and added-value tools and scores. With their products already seen as critical, the fact they are also viewed as highly specialised and somewhat opaque will lead more lenders to stump up the extra money for pre-packaged solutions and support. This in turn makes it much harder for lenders to ensure that everything being delivered is entirely necessary or has been optimised to reduce cost.

The unfortunate upshot of this is that while nearly every UK lender will have at least one bureau relationship, only a very small number of these will be getting the most benefit from this at the best price.

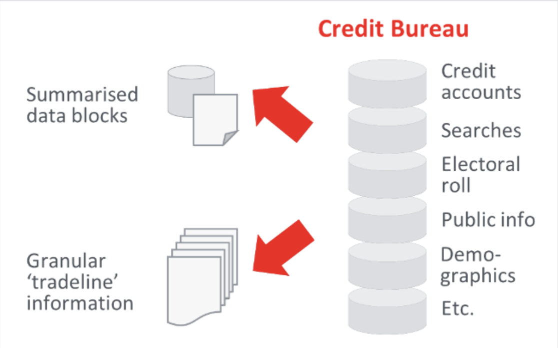
All Present and Correct?

One of the biggest mistakes made by numerous lenders is just accepting that they are getting what they need, what they have paid for, and that what is delivered is actually correct. The good news is that it is a relatively simple process to audit the information being fed in from the bureaus and check it is as expected. There are some simple tests that can be undertaken to avoid common pitfalls:

How is the data delivered?

Without going into the technical details of APIs and agent portals, it is important to know that the bureaus usually provide their data in two forms – consolidated summary blocks or account-by-account 'tradeline' data. The raw form of the tradeline data is useful for detailed manual underwriting, while the summarised blocks are more suited for scoring and automated decisions.

In one case, a lender decided to introduce automated underwriting to support the existing manual process, reasoning that they had now amassed enough bureau history to build a scorecard and associated rules. However, they subsequently discovered that they only had a contract to view data via a portal and did not have access to any of the summarised data blocks on their historic accounts, which derailed their plans.



Bureau information can be consumed in multiple ways

Is the data stored?

The information provided by the bureaus is incredibly useful, but it is also an expensive commodity. Because of this it is critical that this information is stored. While the organisation needs to ensure that this is done sensibly within the constraints of applicable data protection laws, it is important to retain as much of this information as possible, including on rejected accounts. This data is invaluable for developing scores, supporting analysis, auditing decisions, tracking portfolio profiles and providing insight to stakeholders. The credit bureaus will not resupply this information retrospectively free of charge – in fact, we will see below that doing this is actually an important revenue stream.

Is everything populated?

Just because the blocks for the data are there, it does not mean that the fields are populated. As we have discussed, the bureaus offer a menu of different data elements or solutions and empty placeholder blocks for these may be present even when clients do not buy that information. But mistakes do happen, and it is sensible to check that the blocks that *are* being paid for are actually filled. This is as simple as producing frequencies of key variables across the bureau feed, but it is surprising how many issues this can uncover.

Is the data correct?

The final important check is that, when there is data present, it is fit-for-purpose. Unfortunately, this can be a more complex assessment and require more detailed bureau expertise. At its broadest this would cover whether the business is sourcing the right data and products – what are the best tools for decisioning; what data is the most useful; what are others in the sector using? Answering this can require a comprehensive view of the services offered by the bureaus and which are (and are not) likely to add value for lenders.

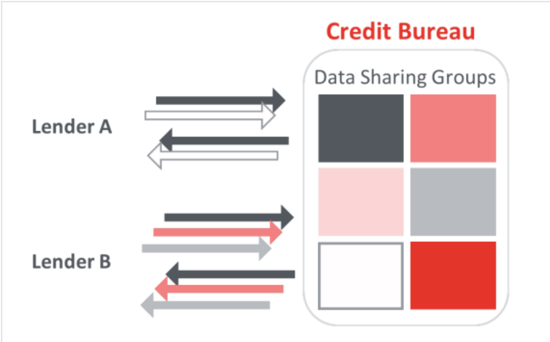
But even when a sensible set of data and products have been selected, there is the more basic question of whether these have been parameterised correctly and the right versions are being sent. We have recently seen more than one case (not limited to just one of the bureaus) of lenders unknowingly receiving obsolete credit scores, several generations out of date, because the bureau feed has not been specified correctly. It is not necessarily obvious that changing a *single digit* in a bureau score label can mean receiving a score built in the 1990s instead of the latest, cutting-edge version!

This is one of the more extreme examples, but there are a number of settings that can have a huge impact on the richness of data returned, such as the number of forwards and backwards 'linked' addresses searched, how joint applicants are treated, and data-sharing membership settings. Each is critical but also serves as one more potential pitfall for an unsuspecting lender.

Return to Sender

The bureaus operate on the principle of reciprocity; to get data out, it is necessary to send data in. Usually, the level of information provided *to* the bureaus by the lender will determine the level of detail they receive in return. True to form, this can get quite labyrinthine, with various reciprocal requirements for each of the bureaus' numerous products and varying levels of data sharing membership.

The detailed rules about data return lead many lenders to view this bureau reporting requirement as an unwelcome overhead and operational chore. It is often not well automated and can become a time-consuming backroom process. And in truth, we have seen a number of cases where lenders have holes or errors in their bureau reporting processes, which at best are not compliant with reciprocity agreements and at worst could lead to customer detriment. Historically the bureaus have not been strong in policing the data returned to them, but this appears to be changing, with a number of the bureaus currently undertaking data sharing reviews.



Bureau data is usually available on a reciprocal basis

However, accurate and timely return of bureau information does have benefit for lenders too (beyond allowing ongoing access to bureau services). The rise in Direct-to-Consumer credit reporting services such as Credit Expert, Credit Karma, ClearScore etc. means that more consumers *see* the impact of missing payments on accounts. It is reasonable to suspect that a borrower in arrears to two creditors would prioritise paying the one that they can visibly see impacting their credit score via such services.

It follows that it is beneficial to report customer performance to all three of the UK's main bureaus. However, it is usual for a lender to report only to the one or two bureaus from whom they actively take data. This links again to the view of bureau reporting as an onerous and time-consuming task. The good news is that if you report to one bureau it is easy to report to all three; the appetite of the bureaus to receive lender data means that they will usually accept report files in any of the UK bureau formats as well as their own.

Caveat Emptor

Bureau data is expensive. Even if the cost per call is relatively low, the volume of cases can quickly lead to hefty monthly bills which contribute significantly to the overall cost of acquisition (or servicing). Obviously, this is highly dependent on the contractual framework in place (tiered pricing by volumes, 'all you can eat' arrangements etc.) which fall outside the scope of this paper. But there are two things we will mention here: optimising the data flow and assessing the cost-benefit of components.

The first of these is relatively straight-forward; lenders can minimise cost by structuring the waterfall of data calls to the bureau efficiently. The key is to ensure data is only pulled when it is definitely going to be used, and with more expensive data elements positioned later in the flow. Intuitively one may think of identity verification happening before the checking of credit risk or affordability for example. But this is a relatively expensive process with a low failure rate, so it is usually more cost effective to do this towards the end of the underwriting process.

While optimising the data flow is an easy win, it has limited value if the data and products being called are simply not cost effective. Some of the bureau solutions are used to meet regulatory requirements (such as AML), but in most cases the data blocks, indices, scores and tools offered by the bureaus are entirely optional and should only be purchased if they are adding genuine value in the underwriting or customer management process.

As has been mentioned, much of the margin for the credit bureaus comes from selling these value-add elements and the sales teams are often strongly incentivised to roll these out to their client base. In addition, the complexity and specialist nature of the data means that the cost-benefit analysis (in the form of proof of concept exercises) is often carried out by the bureaus themselves. Clearly this is not ideal, and we have seen examples of lenders paying for tools and solutions that do not prove to be cost effective.

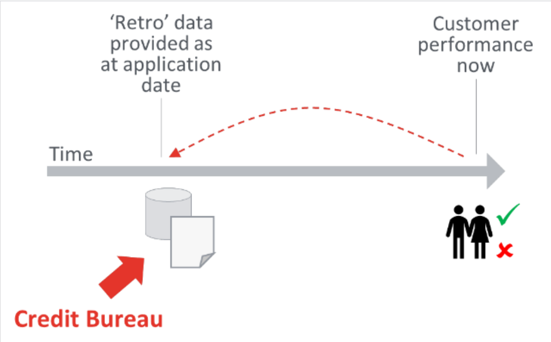
But there is a clear counterpoint to this; in many cases the bureaus' tools and data really are immensely valuable. The credit reference agencies are in a constant 'arms race' with each other to produce new and innovative products and they employ teams of highly capable people to find new data sources or new uses for the data they already have. We see just as many lenders whose processes are sub-optimal or who are operating at a competitive disadvantage because they are not using the right bureau tools (or are not making the correct use of the ones they do have).

Unfortunately, this often does come down to trust. In the relatively insular world of consumer credit risk, everyone has a story of a shaky bureau implementation, underperforming score or difficult sale process, leading many business leaders and management teams to be wary of their bureau partnerships. The upshot is that many lenders are not getting the most out of their bureau solutions, are operating at a disadvantage, and are not serving their customers in the best way.

Past Masters

One of the most useful services offered by the bureaus, and often the start point for any new engagement, is the retrospective bureau pass, or 'retro'. This allows a lender to retrieve bureau data, including any new products or scores, on a set of their own historical accounts, which can then be analysed against how the accounts actually behaved. This is commonly done when a lender switches to a new bureau or is looking to test the usefulness of data blocks and scores that they did not receive historically. Or if they did not store the data they did receive and need to recreate it!

This window to the past can provide an invaluable analytical tool, enabling lenders to derive policy rules, models, pricing etc. without having to wait for outcome to be available on today's accounts. It also allows new bureau services and data to be assessed comprehensively on the lender's own book, supporting the cost-benefit requirement discussed earlier. As such, retros are one of the most common ad-hoc exercises carried out by the bureau providers.



Retrospective data attachments can be hugely useful

In some cases, lenders may not have a set of historical accounts suitable for a retro process. This would be the case for a new lender, or an established lender looking to enter a new market, target a new customer segment, or launch a different product. In this situation it is possible to rely on the generic tools produced by the bureaus – the Delphi, Gauge or Risk Navigator credit scores for example. But a better solution might be a generic sample, a set of anonymised representative data from other lenders in the required market segment. The process, output and uses are very similar to a retro, it is just that the accounts used are not those belonging to the lender themselves but to other (anonymised) lenders who have operated in the required market space.

As ever, there are key things to be aware of when working with retros and generic samples, primarily to ensure that these are specified correctly. In both cases, it is important that the settings used retrospectively mirror those that will be available in the live system. It is not useful to bring back and analyse data points on the historic data if these are simply not going to be available in the live environment. Similarly, searching multiple forward and backwards address links in the retro or generic sample will be misleading (and significantly overstate benefit) if a single backward link has been agreed in the contract for the live process.

We have seen several successful new lending businesses grow quickly and effectively by leveraging the benefits of generic samples, bridging the gap between weaker generic solutions and true bespoke developments. But we have also seen businesses waste significant time and money because of badly specified or inappropriate retros, which have either not been representative of their target market, have included data that doesn't match the live system, or have simply been run over an inappropriate time window.

Beyond the Basics

The topics touched on in the paper are some of the basic considerations when implementing an effective bureau solution. And in truth many lenders will not take things much beyond this, content to run a minimal bureau solution, ticking some regulatory and operational boxes while keeping the credit reference agencies at arm's length. But for those lenders looking to integrate bureau data and solutions more comprehensively within their businesses, this is just the start.

More advanced topics include running effective multi-bureau solutions, using bureau information beyond the underwriting stage (such as in collections and customer management) and deriving bespoke variables from the raw data to capture behaviours not available on summarised blocks. These and many other areas are interesting and potentially very valuable but lie outside the scope of this brief paper. With the three bureaus introducing new innovations all the time, such as the recent focus on trended data, there is always something new to assess and potentially leverage.

In a nutshell, the bureaus deliver information. While the adage that knowledge is power holds true, it is also the case that knowledge doesn't always come cheap. While still viewed a little distrustfully by some, especially those burned by previous interactions, the bureaus are simply a tool. This tool can be used effectively or poorly, but that is entirely down to lenders themselves.

The key is that lenders need to take control of this process, proactively testing cost-benefit, ensuring accuracy and optimising settings. It is these hands-on lenders that will reap the rewards of a successful relationship with the credit bureaus and leverage the most value in their businesses. Sadly, those that fail to get involved and assume the benefits of credit reference data will 'just happen' are the ones who will continue to get caught out or fail to extract the value they could from these assets.

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About Vestigo

Vestigo is a team of experienced and dynamic analytics and credit risk professionals established in 2017. With a strong pedigree in financial services and credit risk, and experience across numerous other industries, we deliver comprehensive analytical support and risk services. Our London-based team of consultants, specialists and practitioners provide services to clients worldwide on a consultancy, contracting or outsourced basis.

The Vestigo team have engaged with several clients recently to assist them in optimising their use of bureau data. Recent projects include improving a lender's underwriting flow to ensure the most efficient use of all available data sources, building a bespoke scorecard for a new lender using generic sample data, and undertaking cost-benefit analysis of a new bureau product.

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