Optimizing Risk Management for Mortgage Lending

As we all know, consumers place varying priorities on their loan obligations. The BEACON® 09 Mortgage Industry Option — developed by FICO™ using a national sample from Equifax’s database — considers this in helping you to gauge risk.

The BEACON 09 Mortgage Industry Option adjusts the BEACON 09 credit risk assessment score, adding or subtracting points according to predictive information specific to the mortgage industry. What does this mean to you? It means you receive all the proven credit risk assessment benefits of BEACON 09— predicting the relative likelihood that credit applicants, prospects and existing customers will satisfactorily repay their credit obligations over the next 24 months. The BEACON 09 Mortgage Industry Option, however, is designed especially for mortgage lending. As a result, you can make credit decisions with confidence, while further limiting risk.

How the Bankcard Industry Option Was Developed

BEACON 09 was used as the foundation to develop the BEACON 09 Mortgage Industry Option. Hundreds of credit file characteristics were compared with mortgage loan performance records to identify the degree of “bad” behavior (90+ days past due on that industry tradeline) over the span of 24 months relative to “good” behavior, resulting in more than 80 different variables included in the final scoring model. Bankruptcy, from any industry, is also classified as “bad.”

How It Works

To refine consumer assessment for enhanced predictiveness, the BEACON Mortgage Industry Option model was developed to leverage multiple scorecards, or population segments, which distinguish consumers by relevant predictive characteristics, as well as the predictive patterns associated with those characteristics. This methodology empowers the model to not only separate the good from the bad, but also separate the bad from the very bad.

While lenders will receive back only one score, plus reason codes where applicable, the model calculates the score by reviewing the consumer’s credit report and automatically selecting the appropriate scorecard(s) for each consumer credit file. The BEACON Mortgage Industry Option takes twelve population segments from the base BEACON 09 score as a base — eight scorecards for consumer segments where no serious delinquency or derogatory...
The chart above illustrates a 17% increase in the number of “bads” identified below the 10% cutoff threshold. This chart also reveals a 20% improvement in the proportion of “bad” accounts identified above the score cutoff, resulting in improved credit quality of the customers likely to receive favorable treatment.

The Mortgage Industry Option is aligned to reflect similar odds of “good” to “bad” performance as BEACON 09. This means that the Mortgage Industry Option provides the same odds of “good” to “bad” mortgage loan performance at a given score range as a BEACON 09 score range. For example, a Mortgage Industry Option score of 710 would indicate the same degree of risk as a 710 produced from the BEACON 09 score. Scores range from 300 to 850 – the higher the score, the lower the potential for serious delinquency.

Why It’s More Predictive

When you score mortgage loan performance data, as compared to general credit performance data, some unique things happen. At any given percentage of accounts, the Mortgage Industry Option identifies a higher percentage of future delinquencies than BEACON 09.

The Mortgage Industry Option identified 64% (or 36% above cutoff) of all 90+ delinquencies within the lowest 10% of scored files with good performance, compared to 55% (45% above cutoff) with BEACON 09.

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Fine-tuning Interval Score Distributions

The Mortgage Industry Option spreads the distribution outward to both higher and lower score ranges.

Substantial improvements in risk prediction are reflected in the broadening of the score distribution, so a greater percentage of future “bad” accounts are pushed into the lowest score ranges and a higher percentage of future good accounts are pushed into the highest score ranges.

The BEACON 09 Mortgage Industry Option does a better job than the base BEACON 09 score at identifying future “good” and future “bad” mortgage credit performers. As a result, accounts which are likely to remain in good standing tend to have higher scores under the BEACON 09 Mortgage Industry Option, while future “bad” accounts tend to have lower scores.

You will need to evaluate the Mortgage Industry Option’s performance on your own portfolio before deciding where to make necessary score strategy changes to minimize losses.

How You Can Use It

The Mortgage Industry Option gives you the heightened ability to separate future paid-as-agreed loans from potential delinquencies, repossessions and/or bankruptcies. This increased precision helps you:

- Improve risk assessment of expected defaults and reduce early payment default buy-backs.
- Improve portfolio performance and exposure management, as well as enhance refinance/restructuring.
- Refine cash flow and performance evaluation for loan pool pricing/rating.
- Enhance segmentation and messaging for marketing campaigns, and more effectively align resources.

Easy to Implement

A key design objective for the BEACON 09 Mortgage Industry Option was to deliver many of the same easy-to-implement and deliver features as the base BEACON 09 score versions, including a consistent score range, minimum scoring criteria, odds alignment and performance window. The scoring model retains many of the same base BEACON 09 reason codes, although additional implementation requirements will be needed to accommodate the 18 new two-digit numeric reason codes.

Get the Strongest Risk Decisioning for Mortgage Lending

Isn’t it time to elevate your risk assessment capabilities? Get the increased predictive power of the BEACON 09 Mortgage Industry Option — optimized risk assessment designed specifically for mortgage lending. For more information, call your Equifax representative, or 1-800-685-5000, or visit us online at www.equifax.com/Mortgage today.