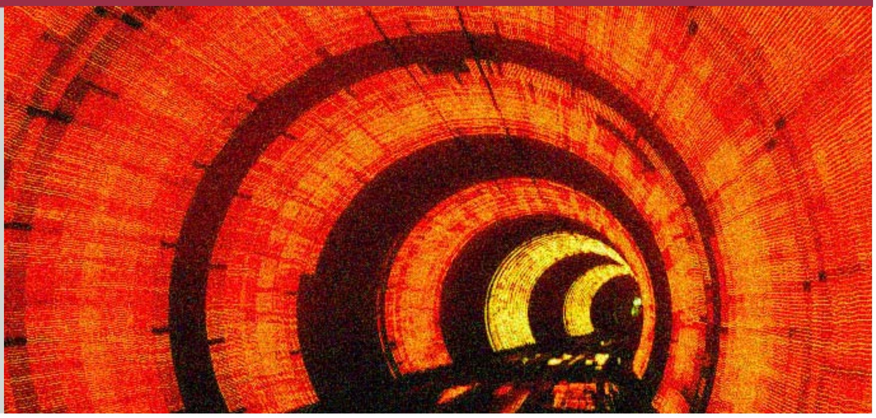
A FAIR ISAAC WHITE PAPER

Dynamic Credit Risk in the Telecommunications Industry

Addressing the Cinderella Syndrome

March 2007



Summary:

Increasing consumer debt levels across Europe have had a considerable effect on the telecommunications industry, especially in the post-pay sector. This, combined with product proliferation, greater product complexity, market consolidation and declining subscriber growth in many key economies, has created several significant challenges for the industry.

Telecom service providers have typically deployed aggressive sales and marketing campaigns to drive customer acquisition and churn reduction. The purpose of this paper is to highlight the significant value the Credit and Risk department can deliver—ensuring the right customers are qualified and targeted and the appropriate solutions and strategies are enabled throughout the customer lifecycle.

Traditionally, credit risk has been seen as a low priority component of the telecom provider's marketing, sales and lifecycle management strategies. Credit risk suffers from the "Cinderella Syndrome"—operating in the background, often unappreciated—while in reality it has the potential to be a star in the organisation.

This paper will highlight the challenges and opportunities that face the credit and risk department, and will propose the first steps that can bring significant improvements to your organization.

In addition, Fair Isaac offers to introduce your organization to the Credit Decision Performance Audit that will establish a road map to move to a truly dynamic credit management approach.

FOR MORE INFORMATION	*telephone*	*Fax*	*email*	*web*
	+44 (0) 870 420 3675	**+44 (0) 870 420 3601**	**emeainfo@fairisaac.com**	**www.fairisaac.com**

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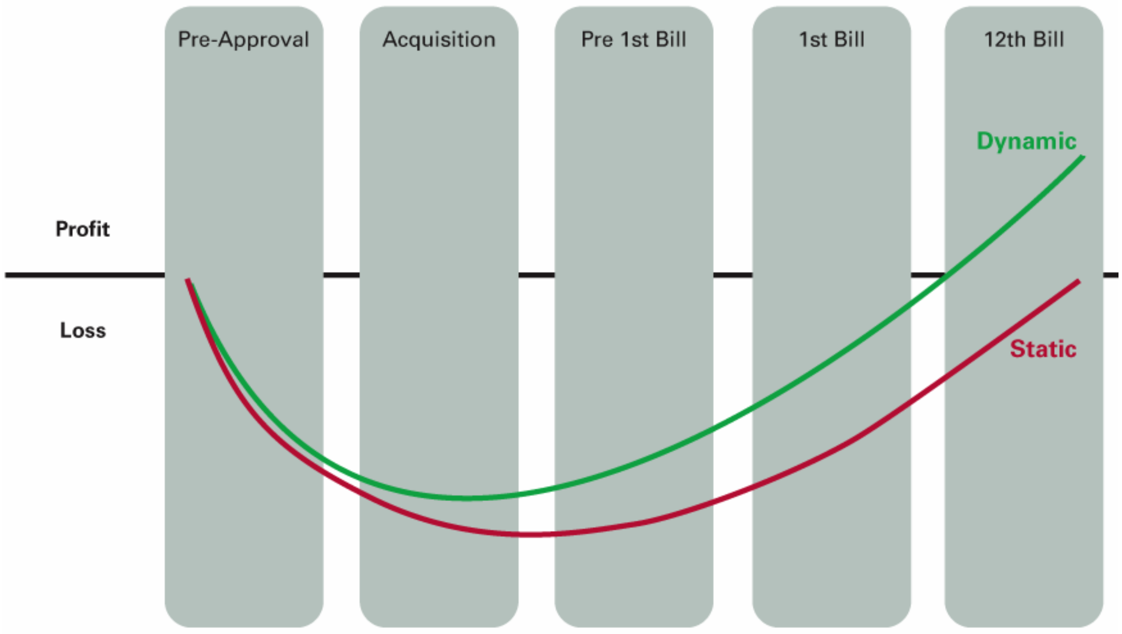
Evolve From Static to Dynamic Credit Risk Management

The traditional focus for many credit risk functions is on capturing low risk customers at the acquisition stage and recovering payment in the case of delinquency. However, saturated markets have forced these organisations to look to new, less obvious customer segments, which previously may have been driven to pre-pay offerings, to maintain growth

In order to support these new riskier but ultimately profitable customer segments, a more pro-active, holistic approach needs to be taken to credit risk across the telecommunications enterprise. The credit risk team can help the organisation:

- Identify prospective customers that are likely to default prior to the marketing offer and remove them from marketing activities—improving marketing efficiencies by not acquiring loss making customers.
- Identify in-life customers that become likely to default post activation—reducing collections cost and ultimately impacting bad debt.
- Identify and manage potential customers that may be perceived as high risk but offer significant revenue opportunities—opening new segments without exposing your organization to unnecessary risk.

Early identification enables the telecom provider to reduce churn, increase overall customer ARPU and prevent losses of valuable network resources and effort.



Traditionally credit risk has been seen as a low priority component of the telecom provider's marketing, sales and lifecycle management strategies. This is often due to the conflicting goals of the sales, marketing and operations teams with the Credit Risk department trying to address multiple agendas.

In order to address this challenge, Fair Isaac solutions enable the telecom provider to manage the credit lifecycle dynamically using an end-to-end approach designed to optimise the enterprise's capability to exploit new market segments while effectively managing credit risk at each stage of the lifecycle.

What Are The Challenges When Deploying Dynamic Credit Risk Management?

Many of the telecom providers that Fair Isaac works with agree that a more dynamic approach to credit risk is highly desirable. Then the question is why are telecom providers struggling to implement this approach? Here are a few historical reasons:

- Systems and infrastructure
- Access and visibility of data
- Organisational challenges
- Low priority to invest in credit risk

The systems and infrastructure within today's telecom companies often consist of multiple systems often inherited through mergers and acquisitions, both nationally and internationally. This impedes the Credit Risk department's ability to holistically assess and in a timely manner, individual risks, develop potential solutions and measure the impact of new credit strategies.

Organisational changes often result in the responsibility for credit risk decisions residing in a number of departments throughout the organisation. This leads to fragmented, tactical approaches lacking insight of overall best practice which often confirm the perception that credit risk can be a business inhibiter rather than a contributor to increasing ARPU and reducing churn.

In the past, credit risk has struggled to gain senior management visibility for investment—often losing out to new customer service and marketing initiatives. The challenge is to construct sound business cases which lead to direct financial improvements impacting the bottom line.

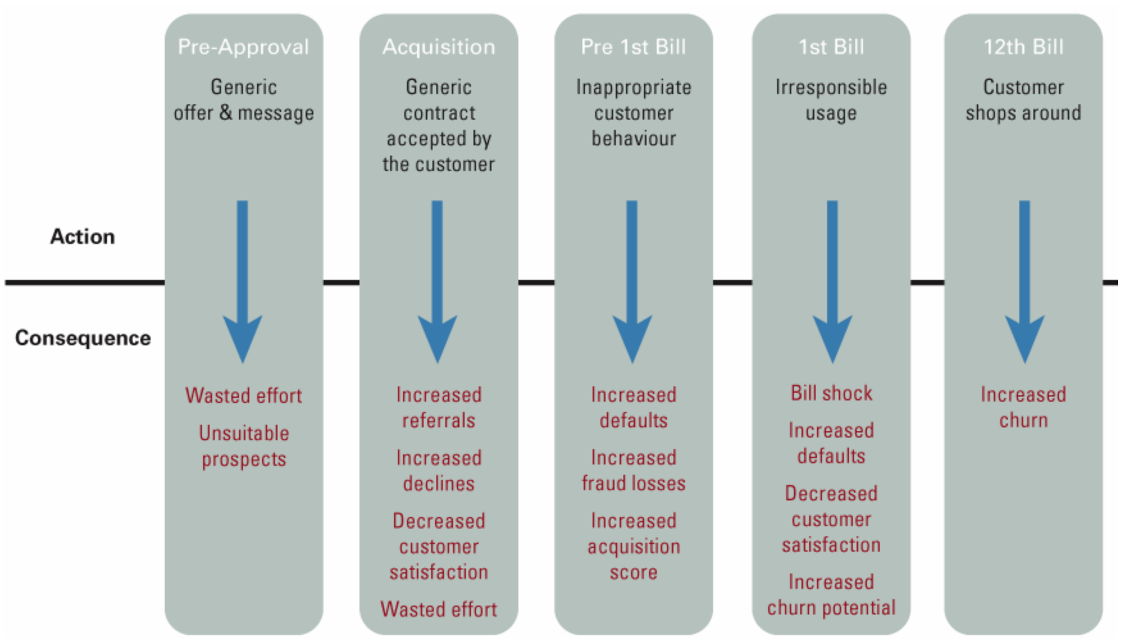
In summary, Credit Risk can be thought to suffer from the 'Cinderella Syndrome'—operating in the background, often unappreciated—while in reality it has the potential to be the star in the organization contributing significantly to the success of the organization, increasing overall profitability reducing bad debt.

The Impact of Poor Credit Risk Management: The Ugly Step Sister

Poor credit risk management impacts the telecom provider throughout the customer lifecycle. Prior to acquisition, at the pre-approval stage, unsuitable prospects can receive inappropriate marketing offers and messages. The impact to the telecom company is that unsuitable prospects move into the acquisition process—wasting valuable resources that could be better applied to more suitable and profitable prospects.

Once prospects become customers, poor credit management can lead to increased delinquency and customer churn. It also potentially masks fraudulent behaviour that is often eventually written off as bad debt.

The following diagram represents actions or events that occur at key stages throughout the customer post-pay lifecycle within a telecom environment and the consequence if the associated risk is not mitigated.



The Impact of Dynamic Credit Risk Management: Cinderella Goes to the Ball

Dynamic Credit Risk Management can significantly enhance the customers experience throughout the lifecycle, and boost their profitability to the telco.

Prior to acquisition, the Credit department should be working with Marketing to rate prospects, pre-approving the best targets. This ensures prospects receive relevant offers, reducing waste and improving take up rates amongst potentially profitable customers. The impact of acquiring more profitable customers will improve the telcos financial performance throughout the lifecycle, reducing defaults, bad debt and the internal resources required to manage delinquent customers that could be better applied to more suitable customers.

As the telco reduces the number of delinquent customers acquired through improved credit management, clearer understanding of the real numbers of fraudulent accounts is possible—enabling targeted programs to be introduced.

An additional benefit of the dynamic credit organisation is to enable the telco to improve understanding of riskier customers, who although may not fit the traditional view of a ‘good’ customer, may prove to offer significant profit opportunities, if managed appropriately.

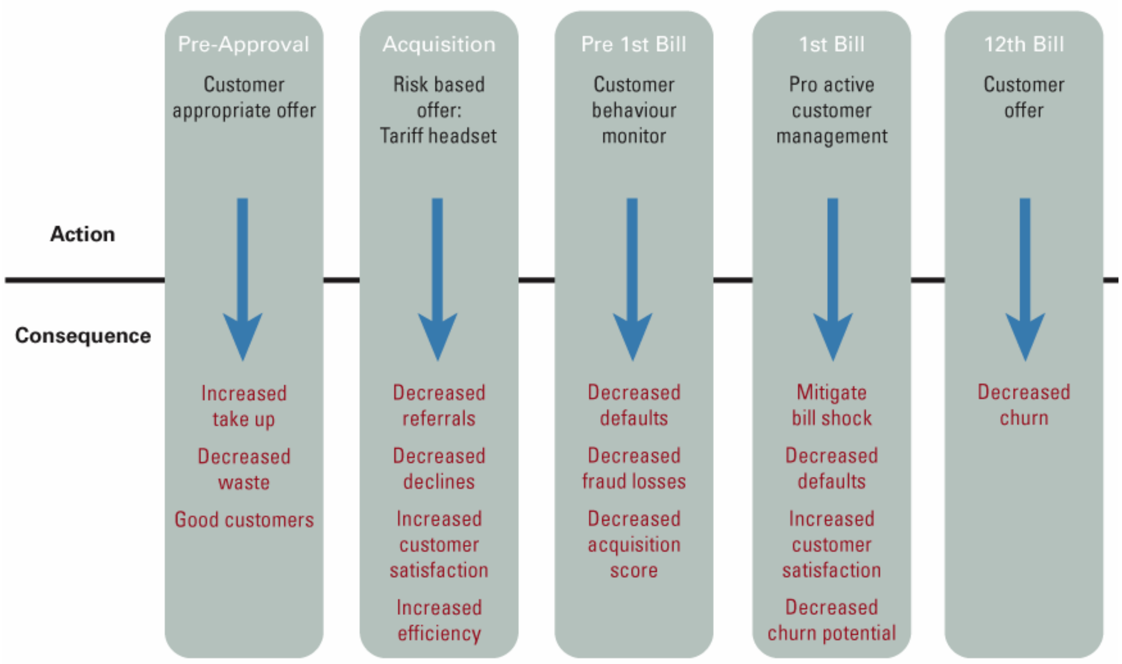
For example, foreign students wanting a contract (rather than pre-pay) present a challenge for many telcos. While a contract offers greater potential profits for the operator, it brings higher risk. Fair Isaac enables the operator to deploy the dynamic credit strategies to penetrate this growing customer segment with three key elements:

- Understand the behaviour and profiles of existing ‘good’ foreign student customers (possibly from pre-paid accounts), apply this profile during the customer acquisition process
- Develop appropriate handset and tariff packages that minimise initial exposure for the telco, with the opportunity for the customer to upgrade as a credit history is developed
- Analyse in near real time the customers behaviour to confirm post activation behaviour fits the profile of a ‘good’ customer—if not alert and take remedial action

> “In today’s highly competitive telecom environment the credit function needs to act as an enabler for the core business providing an end to end risk management capability whilst ensuring the required degree of flexibility to support innovation.”
>
> —Veran Pathan, Vodacom SA

By deploying Fair Isaac solutions that enable dynamic credit management, the operator can profitably exploit new segments with confidence.

The following diagram represent actions or events that occur at key stages through out the customer post pay lifecycle within a telecommunications environment and the consequence if the associated risk is not mitigated.



In summary, dynamic Credit Management will increase revenues and profits while reducing risk , churn and cost within the telco.

Evolving the Credit Organisation

The first step to introducing dynamism to the credit management function is to measure the current performance level, identify opportunities and prioritise potential improvements.

Fair Isaac has developed a process to measure and improve a credit risk department's decision-making efficiency and effectiveness. This is called a Credit Decision Performance Audit.

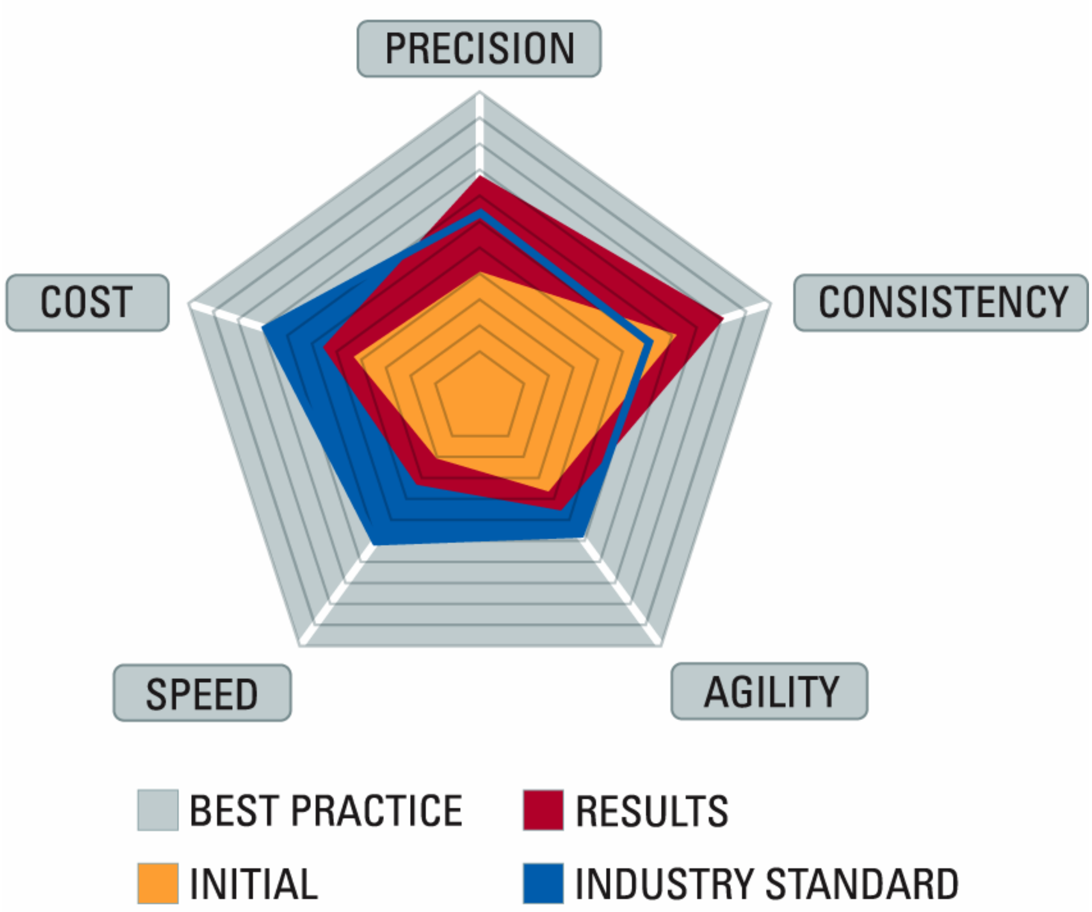
The process focuses on of five key areas, these being:

Precision	How effective are your customer-facing credit decisions in realising short and long term financial goals?
Consistency	Is the same credit decision made the same way across the enterprise?
Agility	How long does it take for a credit manager to change the rules or strategy—from design through testing and implementation?
Speed	What tradeoffs are made between the speed of execution of credit policies and the accuracy of a credit decision?
Cost	Are your credit decisions made through manual intervention or human review? Or are they executed through scalable, low-cost automated systems?

These five areas can be audited to understand improvement opportunities within the organisation. Fair Isaac audits these areas using a variety metrics, performance indicators and qualitative assessments:

- Delinquency and liquidation rates
- ARPU vs. average delinquency balance per segment
- Number of customer referrals and rejections per acquisition strategy
- Channel and segment approach

Below is a graphical representation of a sample Credit Decision Performance Audit—highlighting initial performance, results of decision improvements and finally industry best practice.



The Credit Decision Performance Audit will lead in later phases to the design of an integrated business architecture for managing decisions; build client decision capabilities in terms of technology, business process, and organisational alignment; improve decision-precision through analytic improvements; and run a client's decision environment.

Typically the Credit Decision Performance Audit will uncover improvements in the Credit Risk department that both increase revenues from improved customer spending and reduce the operational costs of the organisation.

Fair Isaac offers to introduce your organization to the Credit Decision Performance Audit that will outline a road map to move to a truly dynamic credit management approach.

About Fair Isaac

Fair Isaac Corporation (NYSE:FIC) makes decisions smarter. The company's solutions and technologies for Enterprise Decision Management give businesses the power to automate more processes, and apply more intelligence to every customer interaction. Through increasing the precision, consistency and agility of their decisions, Fair Isaac clients worldwide increase sales, build customer value, cut fraud losses, manage credit risk, reduce operational costs, meet changing compliance demands and enter new markets more profitably. Founded in 1956, Fair Isaac powers hundreds of billions of decisions a year in financial services, insurance, telecommunications, retail, consumer branded goods, healthcare and the public sector. Fair Isaac also helps millions of individuals manage their credit health through the *www.myfico.com* website. Visit Fair Isaac online at *www.fairisaac.com*.

Fair Isaac Corporation (NYSE:FIC) provides the leading solutions and technologies for Enterprise Decision Management, giving businesses worldwide the power to make smarter decisions.

European Headquarters:
Fair Isaac International Ltd.
5th Floor
Cottons Centre, Hays Lane
London SE1 2QP
United Kingdom
+44 (0) 207 403 1333 *tel*
emeainfo@fairisaac.com

Offices Worldwide:
Australia, Brazil, Canada, India,
Japan, Malaysia, Singapore, Spain,
United Kingdom, United States

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