

# White paper summary

A profit driven approach to risk-based pricing



## The issues of risk-based pricing

The concept of pricing according to risk isn't new; it is common practice in the insurance industry and has been used in the credit industry for over a decade. Risk based pricing is the practice of considering the 'risk' of an applicant and applying different lending interest rates and terms based on their profile.

Those customers who are considered lower risk receive better terms, while those who are considered higher risk are offered higher interest rates, reflecting the potentially increased costs and losses associated with lending to those 'riskier' customers.

The adoption of risk based pricing can bring many benefits to the financial institution implementing the strategy, the customers and financial market as a whole.

Lenders can increase volumes, take-up and bookings whilst reducing attrition and mitigating the effects of adverse selection.

For customers, those who are lower risk are rewarded for their good financial performance, with higher risk customers gaining more access to credit.

The financial market and economy benefits by more of the population being brought into the mainstream lending process.

However risk based pricing has its critics, especially from some consumer protection organisations.

This paper reflects the many years of experience Experian has gained from working with financial lenders implementing risk management decision support and scoring systems.

### Want to read more?

This executive summary is taken from the Decision Analytics white paper [A profit driven approach to risk-based pricing](#).

Access a copy of this, and other Decision Analytics white papers, at: [www.experian-da.com](http://www.experian-da.com)

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