Credit Insight Partners, LLC

Case Study: Lifting Portfolio IRR through Marginal Profitability Optimization

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Background:

A mid-sized fintech lender focused on unsecured consumer loans had scaled rapidly by leveraging a proprietary risk model and aggressive growth targets. The company historically approved accounts by ensuring that the **average IRR per vintage** exceeded a fixed hurdle rate—**16%**.

Problem Statement

Despite hitting vintage-level IRR targets, a granular performance audit revealed that **high-risk accounts were generating negative IRRs**, eroding the gains from more creditworthy borrowers.

- **Low- and medium-risk tiers** were cross-subsidizing high-risk losses.
- The company lacked a **loan-level or tier-specific profitability framework**.
- Portfolio volatility and loss forecast deviations had grown, straining liquidity and investor confidence.

Engagement Objectives

- Identify credit policy inefficiencies dragging down profitability.
- Create a dynamic credit policy that **assesses risk at the margin**, not in aggregate.
- Ensure **every approved account is independently profitable**.

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Approach and Analysis

1. Segmented IRR Analysis

Using historical loan performance, I stratified all approved accounts by risk decile and calculated their realized IRRs. The findings:

Risk Tier	IRR (Before)
Low Risk	23%
Medium Risk	15%
High Risk	-5%

Insight: The bottom 20% of the portfolio by risk was not only underperforming—it was destroying value.

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2. Policy Redesign

I implemented a **marginal IRR floor policy**:

- Set **minimum IRR thresholds** per risk tier:
  - Low risk: ≥ 20%
  - Medium risk: ≥ 15%
  - High risk: ≥ 5%
- Integrated a **loan-level profitability engine** within the automated underwriting platform.
- Recalibrated scorecard cutoffs, loan pricing, and term structures based on IRR forecasts, not just PD or loss rates.

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3. Risk-Based Approval Strategy

Risk Tier	Approval Rate (Before)	Approval Rate (After)
Low Risk	95%	95%
Medium Risk	75%	70%
High Risk	50%	30%

Result: Reduction in high-risk exposure by prioritizing **marginal profit** over volume.

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4. Outcome and Impact

Metric	Before Optimization	After Optimization
Portfolio IRR	16%	22%
Revenue	–	-7%
Loss	–	-23%
Profit	–	**+13%**

- **Every risk tier became profitable**, with high-risk now at +5% IRR.
- The portfolio became **less volatile**, with better capital allocation.
- Merchant confidence increased, enabling more favorable funding terms.

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Conclusion

This case exemplifies how fintech lenders can unlock meaningful gains by **moving from average-based to marginal decisioning**. By setting **IRR floors per risk tier**, rather than relying on vintage-level averages, the company improved profitability by **13%** and reduced exposure to unprofitable accounts.

Takeaway: Sustainable growth in fintech lending doesn't come from more approvals—it comes from smarter ones.