To: Senior Management

From: Kieran Patel

Re: New Model Memo

**Background**

The new balance teaser model is a model using current data to predict trends of our product against our competitors, it is designed to help find an optimal position for the firm to be at regarding credit card loans, but requires certain input variables. Using the same model, competitors have also been included to be able to compare profit margins. The model provides the data of profit for up to 61 months beyond which, it is assumed a new model will be in place. It should be known the model uses core and secondary assumptions and while the main program of the model is highly sensitive and not entirely reasonable, in terms of results returned during the investigation of a suitable approach to our problem, initiative and critical thinking has been used to make the new model and predictions of the competitors’ responses.

**Proposal**

The proposal suggested is to increase the teaser length to 11 months to appeal to a broad range of users, while this is also appealing to gamers, our prime target is customers. The new model also suggests decreasing the balance transfer fee to 1.1% and our post-teaser APR to 21%. This is because a competitive edge is needed in the market to engage customers who are seeking long-term loans. In addition to this suggested route, is the suggestion to evaluate the market and the firm’s stance in it after 8 months and then change the model once more to a higher risk, higher reward option at 12 months, 1.2%, and 21% for new users from that date, or a more balanced approach at 9 months, 1.2%, and 23%. This is so that the first 8 months are to test are testing the waters and gives flexibility with any arising problems that the firm may encounter.

From modifying our loans plan, it is expected that our competitors will adapt their schemes also, for which the model has also been used. It is expected that A retain their 1st rank by keeping 12 months as any less will see them to 2nd position. They also keep their fee and APR the same at 1.5% and 20.90% respectively, giving them 2.5M customers and a profit of £241.3M, well beyond any single competitor in the market. We expect competitor B to keep at 11 months but increase their fee to 1.5% and decrease their APR to 20%. Competitor C is expected to go for a low risk, low reward scheme, targeting loyal customers with a teaser length of 1 month but 0.8% fee and 16% APR, resulting in a profit of £38.8M, leaving them in 6th position but with 0.25M customers just as competitor E. Competitor D is expected to just decrease their APR to 20.5% and leave with teaser at 10 months and fee at 1.3%, in a bid to compete with C and E. Finally, we expect E to also reduce the fee to 0.8% but keep at 8 months and 19.9%. This now leaves the ranks as following: A, our product, B, D, E, and then C. This model shows our product and A dominating the market, as intended.

Adhering to this proposal will advance the firm to 2nd rank, meaning a share of one million customers as opposed to 250,000 at the current model rate. This advancement has made it possible to increase the number of teaser months, but at the same time income is needed which is why the proposed solution includes an increase to the percentage of the fee and APR. This method also leaves the firm with a profit of £105.9M which would make our product the second most profitable in the market in the forecast at a c20% share of the total industry profit, second to competitor A’s c45%.

**Key Risks**

Certain risks have been identified to potentially cause some confliction with the model with one of them being economic instability. During high inflation, the likelihood of loans will increase and while there will tend to be fewer defaults due to the depreciation of the pound, it is this very fact that the income retained will have less value and gamers will tend to make more use of this. Being in second rank means that competitor A will have the most gamers but we could reduce the teaser to 9 months, and then increase fees and APR to 1.2% and 23%. For a recession period, we would expect to see hesitation with loans taken out so we could propose to increase the teaser to 12 months for an increase in fees and APR to 1.2% and 21%, mitigating these risks.

Another risk identified is strategic change where we could be faced with unforeseen circumstances and be incurred with large expenses such as technicality issues or regulatory issues which affect may affect our position in the market and so, we may be faced with a significant loss. These issues could be dealt with a more appealing plan by the 12-month suggestion plan just mentioned and the increased fees are to cover the costs.

A final risk worth noting is the credibility of the model as there are core and secondary assumptions which the model is highly sensitive to. We assume this data is correct and reliable to extrapolate data from but there is an issue of not being able to forecast rise in defaults due to some economical change but this is where our re-evaluation after the first 8 months to direct the model in a more suitable direction. This means the model reflects the current climate, customer satisfaction and takes into consideration their feedback. Furthermore, the percentage of defaults per open jumps to 0.3% from 0% in month 7 which attempts to take into consideration defaults to some extent but given the model is a prediction, it will always have limiting factors.

**Justification of approval:**

The proposal is justifiable to approve as it not only presents one long-term solution but a solution which is responsive as it reflects on its productivity and suitability during the current period. The risks have been considered and should these pivotal risks arise there is a built-in response to follow. The fact we have aimed to remain at 2nd rank is so that in the event of a problem in the market, all the competitors’ and our product will feel the setback but none more so than competitor A, who hold the most gamers whom firms make the least profit from, according to this model, as they leave once the teaser period ends.