

TRK ADVISORS

Credit Card Management Series

Credit Card Market Overview
& Credit Union Performance

Timothy Kolk
(603) 924-4438
tkolk@trkadvisors.com

CALLAHAN
ASSOCIATES
the credit union company

Knowledge. Insight. Strategy.

Can You Hear Me?

- We are audio broadcasting so please plug in your headphones or computer speakers to listen in.
- If your audio is choppy or slow, you may wish to dial into the teleconference:

Dial: +1 (415) 655-0003

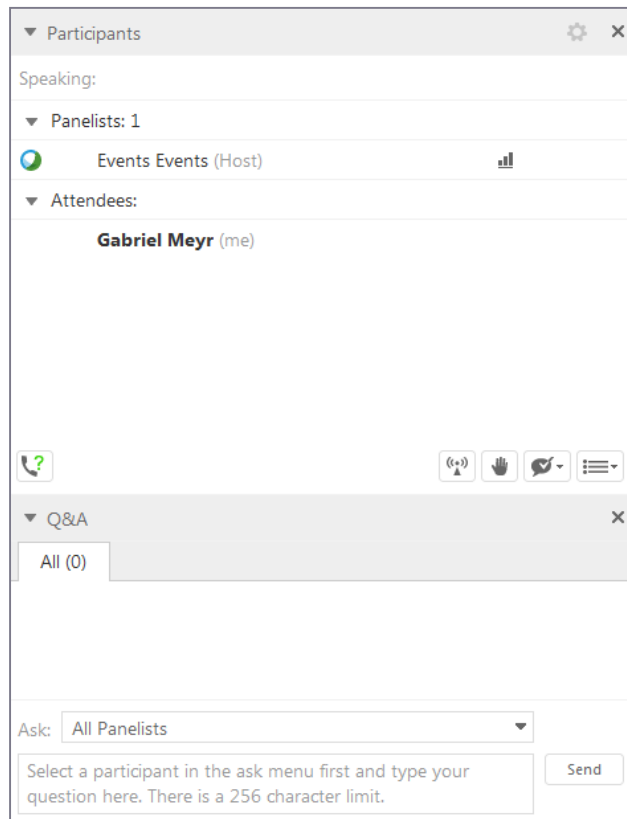
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Slide Link

Today's slides can be found online at:

<http://bit.ly/2019-04-18-ccms-session-1>

We Encourage Questions



Use the

Questions Box

located on the right side of the screen, to type your comments or questions.

Tell Us What You Think!



Please take our post-event survey. We value your feedback!

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The CCMS Purpose

- Provide market intelligence including performance trends, competitive events and market evolution.
- Build staff skills and expertise in managing your credit card program to growth, profitability and member value.
- Share proven tactical approaches and specific action items which you can use immediately.
- Design and provide fair and competitive products that your entire organization can deliver with pride.
- Put you in a position to demonstrate your program's future potential and advocate for the resources it merits.

Logistics

- We target 45-60 minutes, and will stick around for Q&A
- We'll try to handle all questions at the end.
- Downloadable slides available via the link sent by Callahan (but happy to send myself: tkolk@trkadvisors.com)
- Callahan will provide a link to the recording once ready
- We have two more session later in the year:

August: **Calculating Credit Card Profitability**

September: **Mapping Products to Members (Segmentation)**

Ok, Enough of That

Today we look to include the following:

- The four critical priorities of any loan product
- A look at market trends and how credit unions have performed as compared to large bank competitors
- Discuss why credit card is the most important asset-side product you offer
- Quick review of some market developments and research

Why is Credit Card Special?

FI & Loan Product Priorities

Growth Rates

Accounts
Activation Levels
\$ Activity per Account
Revolve Rates
=
Growth Drivers

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Revenues (Yield)

Usually just APR
BUT
Also Interchange & Fees

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Credit Quality

Charge-off Frequency,
\$ Loss per Charge-Off,
Balance per Good Account
Fraud Controls
=
Charge-off Results

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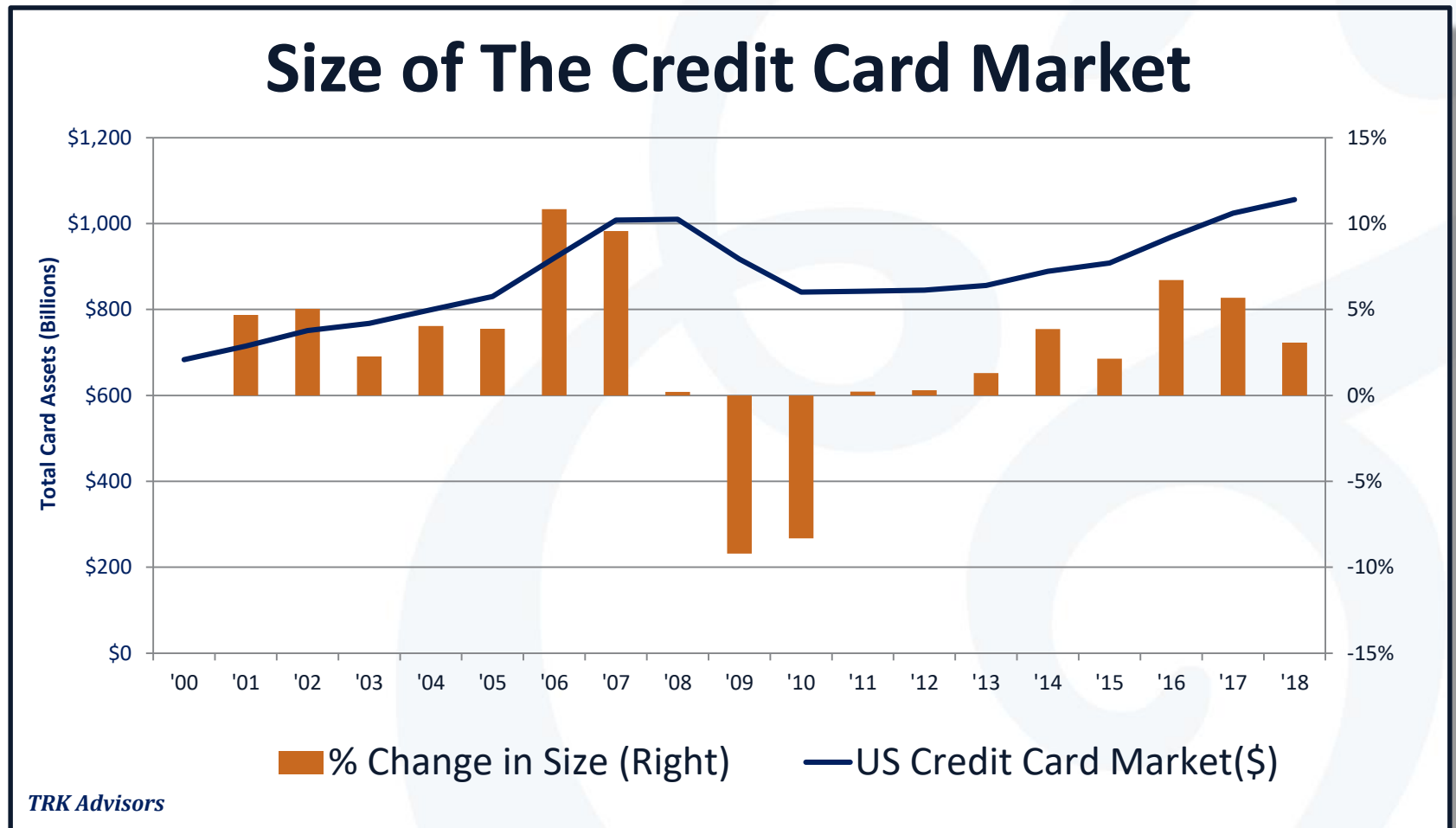
Profitability

All of that PLUS
Operating Expenses, Cost
of funds, Marketing
Campaigns, Rewards...

Market Trends

(Feel good, but don't admit it)

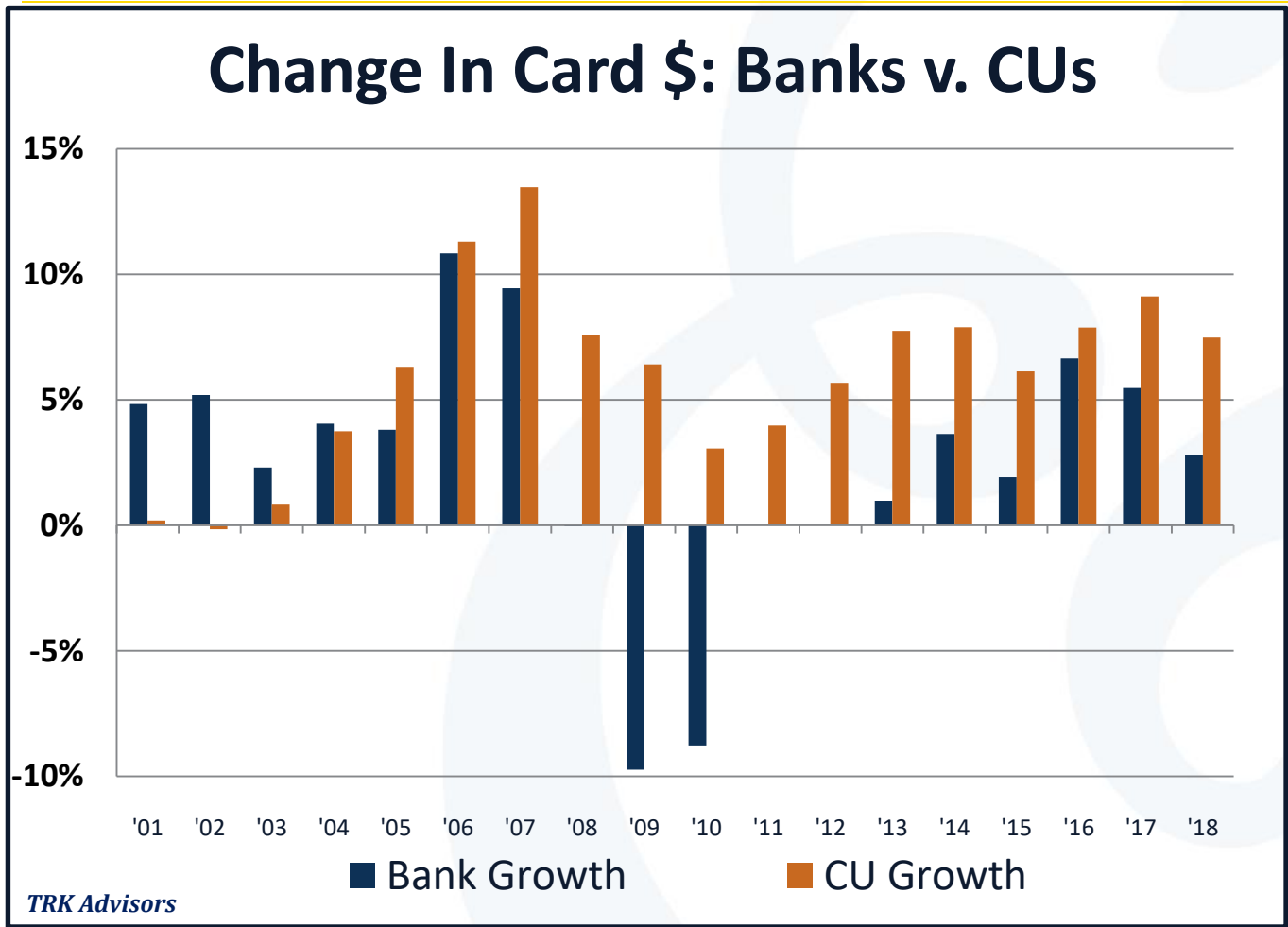
Every Increase is a New Record



Is slowing growth a signal?

Sources: Banks: Federal Reserve G.19, All Unsecured Lending

How Have Credit Unions Done?



2011	Banks	+0.4 Billion
	CUs	+1.5 Billion
2012	Banks	+0.4 Billion
	CUs	+2.1 Billion
2013	Banks	+7.9 Billion
	CUs	+3.1 Billion
2014	Banks	+29.6 Billion
	CUs	+3.4 Billion
2015	Banks	+16.2 Billion
	CUs	+2.8 Billion
2016	Banks	+57.1 Billion
	CUs	+3.9 Billion
2017	Banks	+50.1 Billion
	CUs	+4.9 Billion
2018	Banks	+27.2 Billion
	CUs	+4.3 Billion

Pretty good story for credit unions.

Sources: Banks: Federal Reserve G.19, All Unsecured Lending; Credit Unions: NCUA 5300 Reports

Large Issuer Results (so many #s!)

Top 10 Visa & MasterCard Issuers in the US, 2018

Issuer	Volume (\$MM)		Accounts (M)			Per Active		Turn Rate
	Balances	Purchases	Total	Active	% Act	Bal	Purch	
JP Morgan Chase	\$ 156,632	\$ 739,484	73,751	40,210	55%	\$3,895	\$18,391	4.7
CitiBank	108,570	404,930	56,654	38,500	68%	\$2,820	\$10,518	3.7
Bank of America	107,408	357,646	42,827	28,555	67%	\$3,761	\$12,525	3.3
Capital One	100,210	336,910	90,470	47,700	53%	\$2,101	\$7,063	3.4
Wells Fargo	41,239	131,704	17,510	9,870	56%	\$4,178	\$13,344	3.2
US Bank	39,582	144,731	22,442	11,323	50%	\$3,496	\$12,782	3.7
Barclays	26,391	79,060	10,920	7,680	70%	\$3,436	\$10,294	3.0
Synchrony	23,131	54,369	25,874	14,347	55%	\$1,612	\$3,790	2.4
USAA	17,388	42,901	5,395	4,260	79%	\$4,082	\$10,071	2.5
Navy FCU	16,661	21,714	3,146	2,286	73%	\$7,288	\$9,499	1.3
Total, Top 10	\$ 637,212	\$ 2,313,449	348,989	204,731	59%	\$3,112	\$11,300	3.6
2018 Change	3%	10%	2%	2%	0%	1%	7%	3.4

Source: Nilson Report

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Every growth metric slowed in 2018. Did yours? Do you know?

Source: Nilson Report

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FUN FACT
In 1996 this
was 1.5!

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Credit Unions Did Well In Total, But...

Distribution of Credit Union Card Program Growth

Size	Size	<i>Balances (2018)</i>		<i>Growth (2018)</i>			% Shrinking
		\$ Bil.	% of \$	\$ Bil.	Rate	% of All	
Top 50	\$150MM-\$17.1B	\$33.9	55%	\$3.4	11%	75%	8%
51-200	\$46-\$150MM	\$12.3	20%	\$0.6	5%	13%	25%
201-500	\$16-\$46MM	\$8.4	14%	\$0.3	4%	7%	36%
501-1000	\$5-\$15MM	\$4.5	7%	\$0.2	4%	4%	45%
<u>1001-2169</u>	<u>\$1-\$5MM</u>	<u>\$2.7</u>	<u>4%</u>	<u>\$0.1</u>	<u>2%</u>	<u>1%</u>	<u>52%</u>
Total		\$61.8	100%	\$4.6	7%	100%	45%

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% Growing at Below Average CU Rate

Size (>\$1MM)	2015	2016	2017	2018
Top 50	46%	46%	52%	62%
51-200	67%	67%	65%	77%
201-500	62%	64%	72%	79%
501-1000	73%	77%	75%	77%
<u>1001-rest</u>	<u>78%</u>	<u>80%</u>	<u>83%</u>	<u>83%</u>
Total	73%	75%	77%	80%

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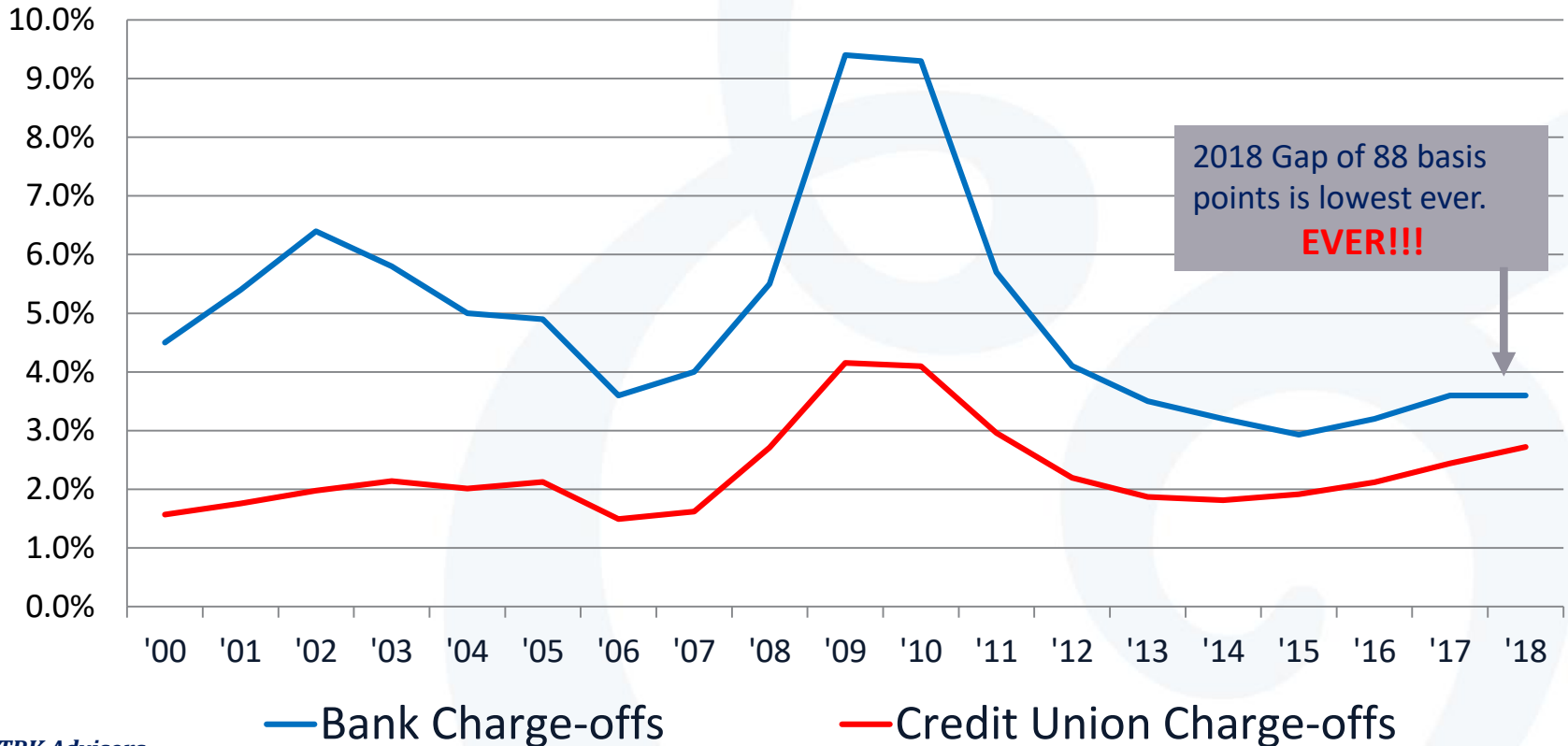
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Work Pays Off, Cruise Control Does Not

- Big get most: Navy has 27% of all CU balances, took 52% of CU growth
- Without Navy FCU credit union market grew at 4.6%... oh my
- % falling behind is increasing. Even largest are not immune

Credit Risk: A Change?

Net Charge-Off Rates



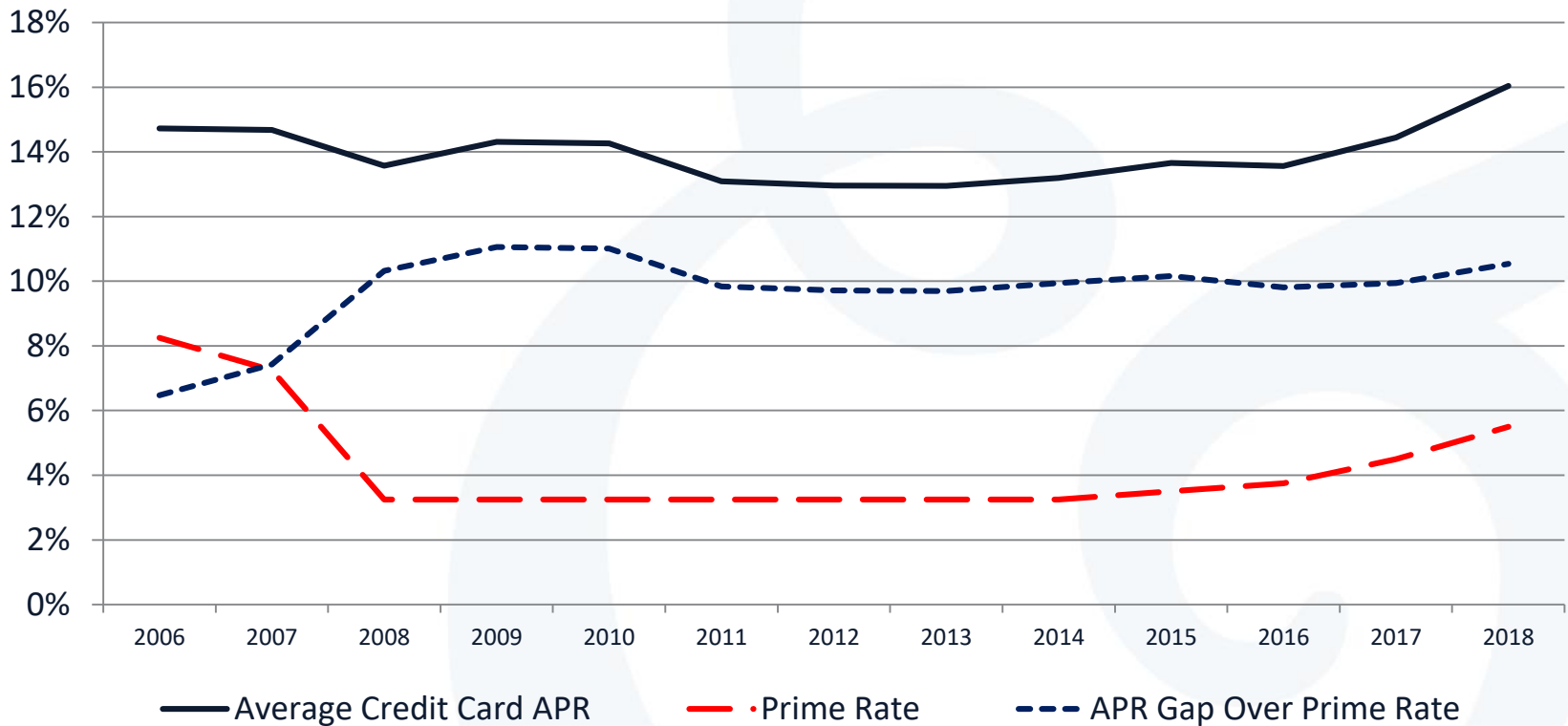
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Compression & Uptick (more to come?)

Sources: Banks: Federal Reserve for Bank rates; Credit Unions: NCUA 5300 Reports

Tell Me About Rates, Please

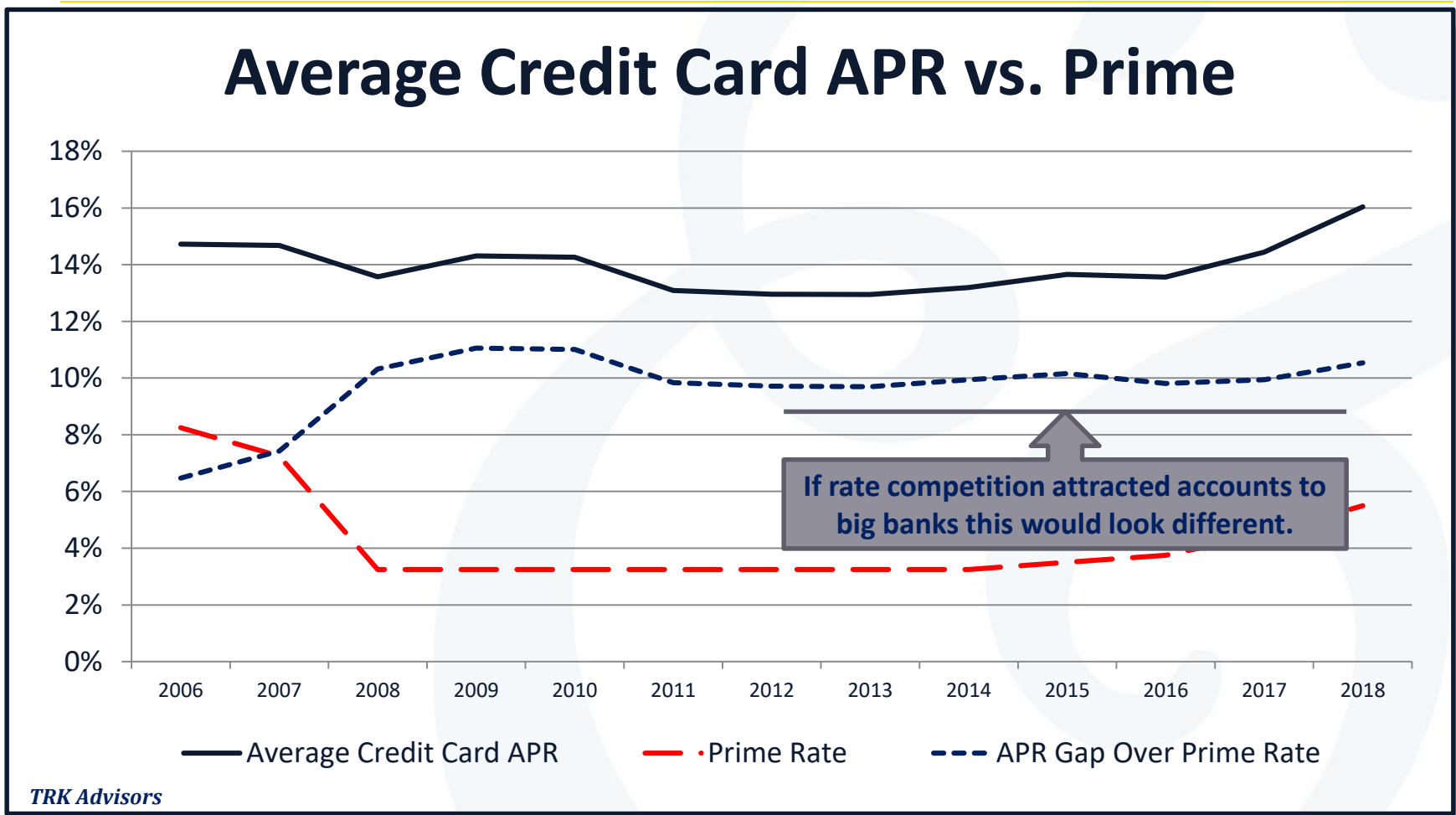
Average Credit Card APR vs. Prime



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Sources: Federal Reserve G.19

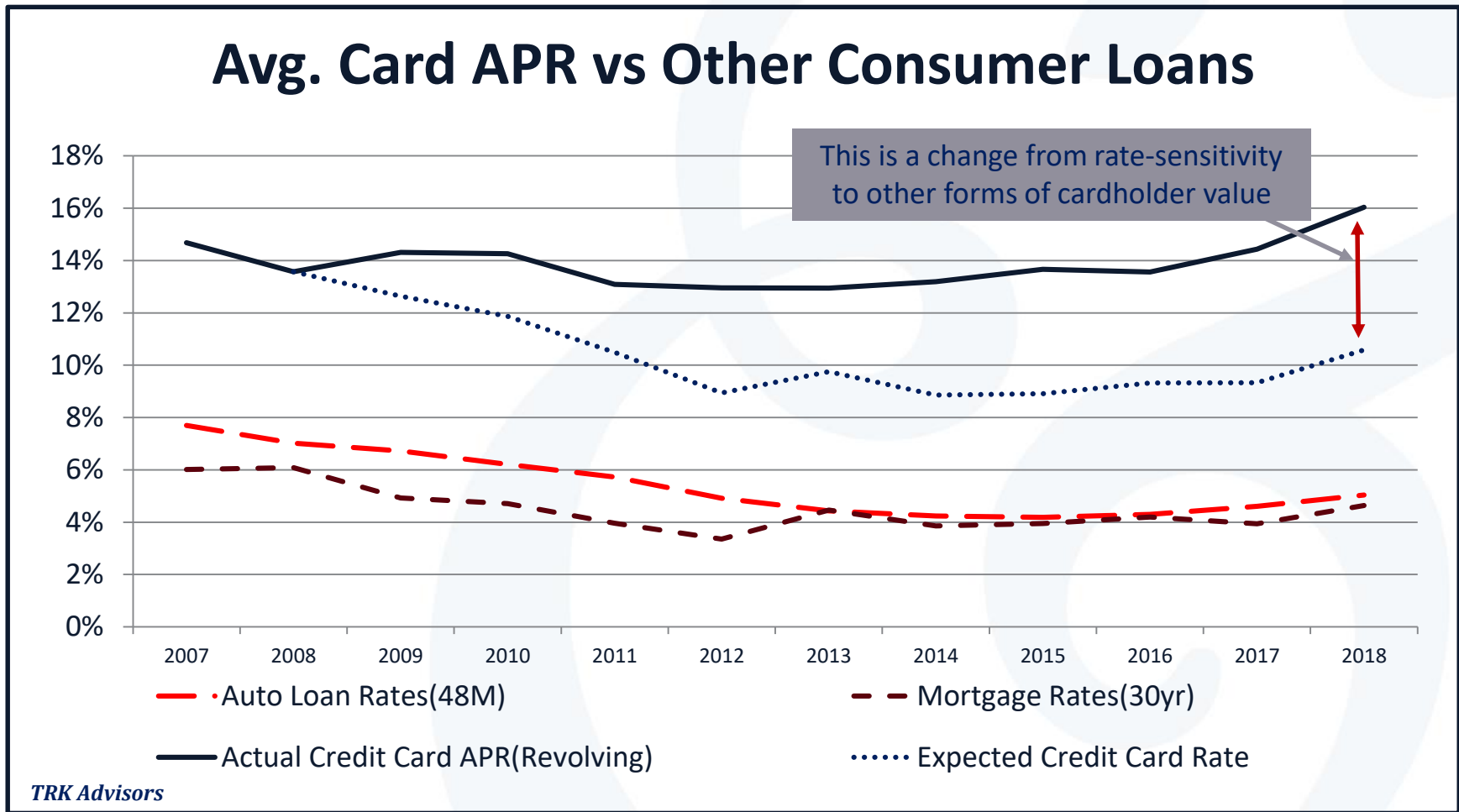
Tell Me About Rates, Please



How much do you talk about rate? About rewards (& how)?

Sources: Federal Reserve G.19

Card: Permanently Higher Rates

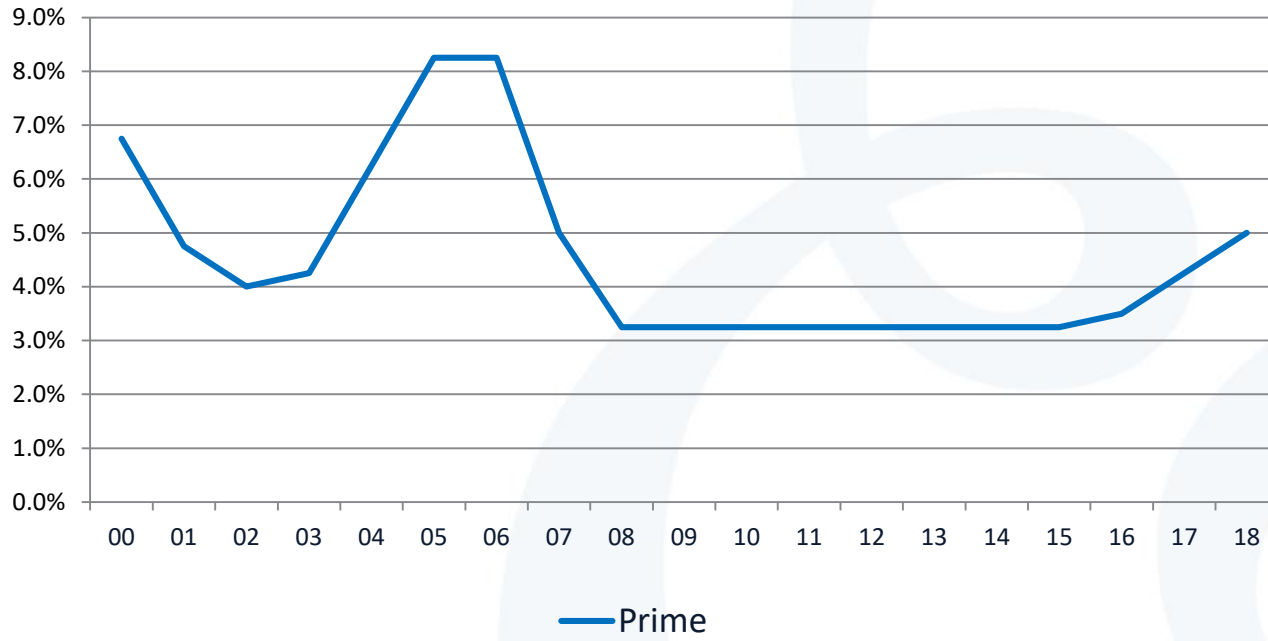


See card value from consumers eyes, not old-timey CU eyes.

Sources: Federal Reserve G.19 for auto and credit card rates; Mortgage News Daily for mortgage rates.

This Is Fundamentally Important

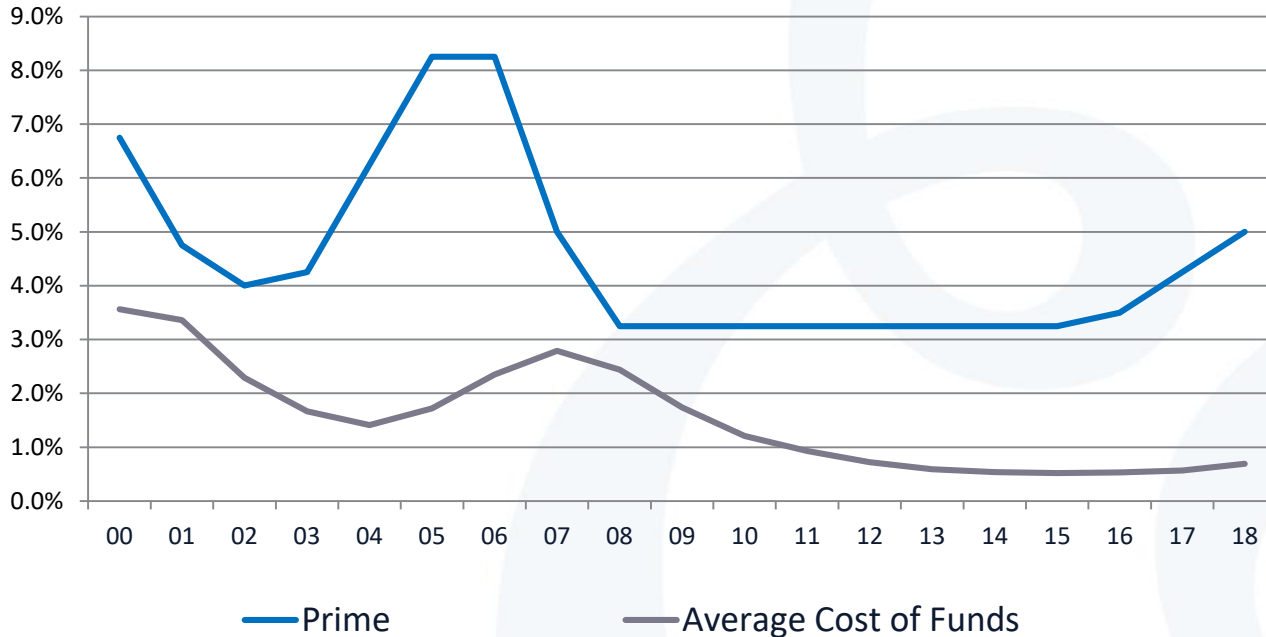
Prime, Funding Cost & Margin



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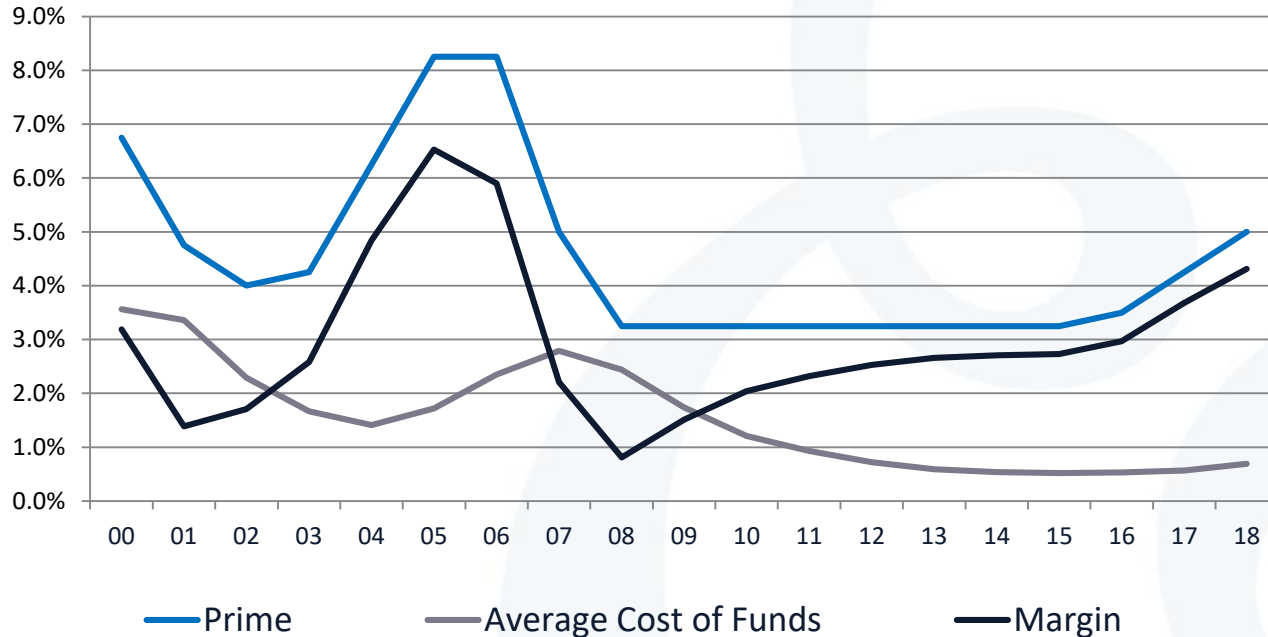
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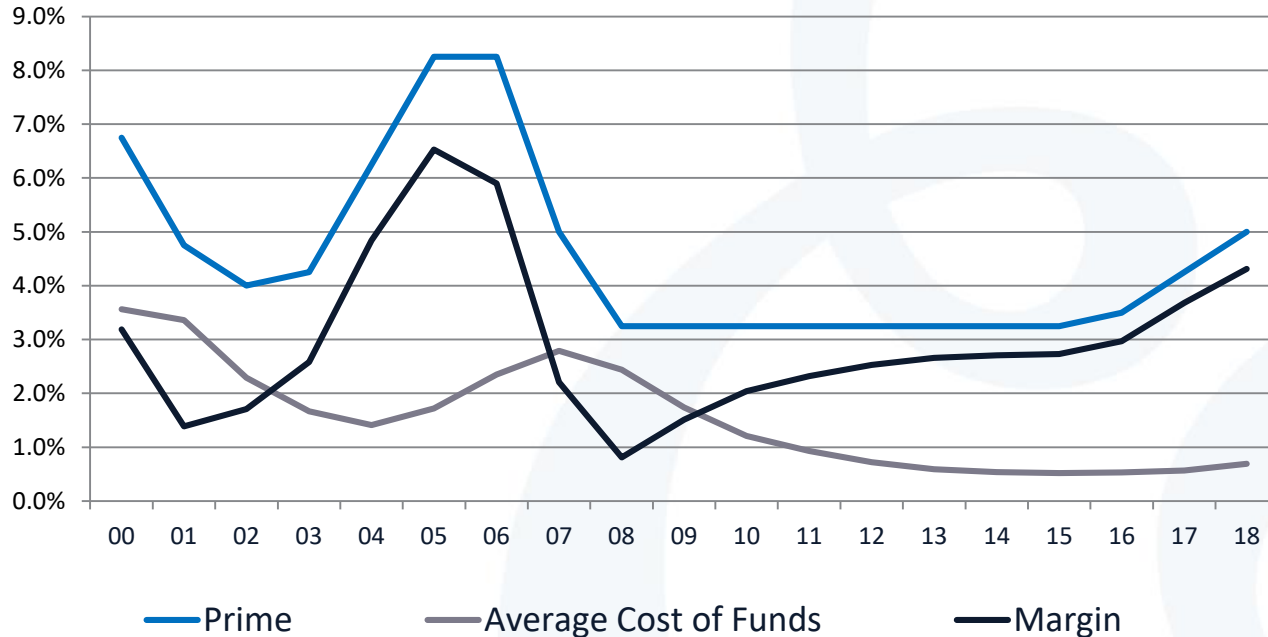
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PRIME less FUNDING COST (MARGIN)

	00	01	02	03	04	05	06	07	08	09	10	11	12	13	14	15	16	17	18
Prime (Mid-Yr)	6.75%	4.75%	4.00%	4.25%	6.25%	8.25%	8.25%	5.00%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.50%	4.25%	5.00%
Cost of Funds	3.56%	3.36%	2.29%	1.67%	1.41%	1.72%	2.35%	2.79%	2.44%	1.74%	1.21%	0.93%	0.72%	0.59%	0.54%	0.52%	0.53%	0.57%	0.69%
Margin	3.19%	1.39%	1.71%	2.58%	4.84%	6.53%	5.90%	2.21%	0.81%	1.51%	2.04%	2.32%	2.53%	2.66%	2.71%	2.73%	2.97%	3.68%	4.31%

This Is Fundamentally Important

Prime, Funding Cost & Margin



For Variable Rate Cards

- When Prime rises, margins rise.
- When margins rise, profits rise.
- Like all profits: keep them, or use them to grow. A nice option.

For Non-Variable Cards

- You missed the increase
- You do not have the same \$ to invest for member value.
- Great for some members, but a failure for most.

PRIME less FUNDING COST (MARGIN)

	00	01	02	03	04	05	06	07	08	09	10	11	12	13	14	15	16	17	18
Prime (Mid-Yr)	6.75%	4.75%	4.00%	4.25%	6.25%	8.25%	8.25%	5.00%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.50%	4.25%	5.00%
Cost of Funds	3.56%	3.36%	2.29%	1.67%	1.41%	1.72%	2.35%	2.79%	2.44%	1.74%	1.21%	0.93%	0.72%	0.59%	0.54%	0.52%	0.53%	0.57%	0.69%
Margin	3.19%	1.39%	1.71%	2.58%	4.84%	6.53%	5.90%	2.21%	0.81%	1.51%	2.04%	2.32%	2.53%	2.66%	2.71%	2.73%	2.97%	3.68%	4.31%

Four Realities from All of This

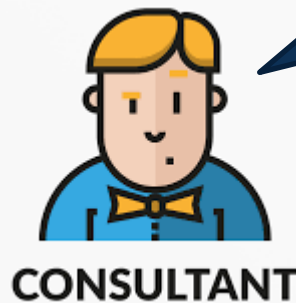
1. Take advantage of improving margins to either:
 - a) Make extra money and spend on other things, or
 - b) Make extra money and invest in the card program
2. Promotional offers matter (rate & rewards)
3. 1% reward value is weak
4. Signature/World are now mass market

Card program failure is a slow motion wreck.

Did I mention that 80% of CU programs grew at below CU average rates?

Profitability Expectations?

- Coming out of the recession, profitability moved toward record highs: historically low charge-offs, historically low cost of funds, APR's permanently increased.
- Last few years has remained high: increasing marketing competition and reward costs, offset by increasing Prime Rate (unless you were fixed rate...oops)
- But what happens now?



It depends...

Possible Paths

1) Prime does not change

- ✓ Yield level, Cost of Funds up
- ✓ Profitability takes a modest hit



CONSULTANT

2) Prime increases

- ✓ Yield up, Cost of Funds up
- ✓ Profitability probably keeps improving
- ✓ But for many the 18% cap is becoming a problem

3) Prime decreases

- ✓ Yield down, Cost of Funds probably still up
- ✓ Profitability takes an immediate hit

Regulators Making Business Decisions

The NCUA is disadvantaging credit union credit card programs for no good reason.

18% Rate Cap

- NCUA voted to maintain the cap as rates were rising
- Most credit unions now have variable rates and risk-based pricing. This is new(ish).
- If you have a tier at P+12.5% you are now at the cap. All future rate increases will only hurt profitability.
- Figure out what % of balances are capped. And what % are close enough to worry about (e.g. P+ 11.9%).

And don't get me started on risk-based capital against unused card lines...

The Point: Prepare Your Credit Union

- Start with current P&L (You have this right? And you proved the card program's value, right?)
- Start to think through each path with Senior Management (including the Finance folks... they're actually decent people)
- Already some downward pressure on profitability: charge-offs creeping up, rewards are definitely not getting cheaper, operating expenses never come down...
- If a recession peeks around the corner entire organizations will be under stress: be the cool, knowledgeable expert in the room. In tough times credit cards becomes even MORE important to the CU

A Quick Look at Market Offers

**Mass-market cards are kind
of boring (and that's ok)**

APRs level (to Prime)

Rewards at 1.5% value (mostly)

Teasers: 12-18 months

Rewards: 15,000+ pts

No annual fee

Market Offers: Chase

Chase Freedom Unlimited® credit card



(9,963 cardmember reviews)

NEW OFFER!

NEW CARDMEMBER OFFER

Earn 3% cash back on all purchases in your first year up to \$20,000 spent.

AT A GLANCE

Cash back on every purchase. Earn up to \$600 cash back. That's **3% cash back** on all purchases in your first year up to \$20,000 spent. After that, earn **1.5% cash back** on all purchases.

APR

0% intro APR for 15 months from account opening on purchases and balance transfers.† After that, 17.24%–25.99% variable APR.†

ANNUAL FEE

\$0†

Chase Freedom® credit card



(14,811 cardmember reviews)

NEW CARDMEMBER OFFER

\$150 bonus after you spend \$500 on purchases in the first 3 months from account opening.

AT A GLANCE

Earn cash back for every purchase Earn 5% cash back on up to \$1,500 in combined purchases in bonus categories each quarter you activate and unlimited 1% cash back on all other purchases.

APR

0% intro APR for 15 months from account opening on purchases and balance transfers.† After that, 17.24%–25.99% variable APR.†

ANNUAL FEE

\$0†

Market Offers: Citi

Cash Back Credit Cards (1)

Citi® Double Cash Card

Citi® Double Cash Card is one of the most popular cash back cards, earning you 2% cash back for those purchases.



Earn 2% cash back on purchases; 1% when you buy and 1% as you pay.

Balance Transfer Rate: 0% Intro APR on balance transfers for 18 months; after that the variable APR will be 15.74% - 25.74% based on your creditworthiness.

Purchase Rate: 15.74% - 25.74% variable APR based on your creditworthiness.

PRICING & INFORMATION



11579 Reviews v

ThankYou® Credit Cards (4)

NEW: Citi Rewards+SM Card

Earn points for great rewards while having fun with the Citi Rewards+SM Card. Earn ThankYou anything through the ThankYou® Rewards program.



New Card Offer: Earn **15,000 bonus points** after spending \$1,000 within the first 3 months of account opening.

Purchase and Balance Transfer Rate: 0% Intro APR on purchases and balance transfers for 12 months; after that the variable APR will be 15.74% - 25.74%, based on your creditworthiness.¹

PRICING & INFORMATION

Simplicity Credit Card (1)

Citi Simplicity® Card

Keep it simple with no late fees, no annual fee and our lowest introductory APR. Save time.



Peace of mind with no late fees or a penalty rate.

Purchase and Balance Transfer Rate: 0% Intro APR on balance transfers and purchases for 18 months, after that the variable APR will be 16.24% - 26.24% based on your creditworthiness. Balance transfer fee of 3% or \$5 of the amount of each transfer, whichever is greater.

PRICING & INFORMATION



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You don't have to match every proposition from the big banks \$-for-\$, but you can't be too far off.

Market Offers: Capital One

Quicksilver® Rewards



Earn a one-time \$150 cash bonus once you spend \$500 on purchases within 3 months from account opening*

Earn unlimited 1.5% cash back on every purchase, every day

0% intro APR for 15 months; 16.24% - 26.24% variable APR after that

VentureOne® Rewards



Earn 20,000 bonus miles once you spend \$1,000 on purchases within the first 3 months from account opening*

Earn unlimited 1.25 miles per dollar on every purchase, every day — plus 10X miles on thousands of hotels, through January 2020

0% intro APR for 12 months; 14.24% - 24.24% variable APR after that

Market Offers: Discover



Discover it® card

Get cash rewards on every purchase, everyday.

5% cash back in categories that change each quarter, up to the quarterly maximum when you sign up.

[5% Cashback Calendar](#)

1% cash back on all other purchases.

We'll match all the cash back you've earned at the end of your first year- for new cardmembers only.¹

0% Intro APR[†] for 14 months on purchases and balance transfers.

Then 14.24% to 25.24% Standard Variable Purchase APR applies.



Discover it® Miles card

Earn Miles on every purchase, and then redeem Miles to pay for airline, hotel and other travel purchases.

1.5x Unlimited Miles on every purchase and your Miles never expire¹

We'll Match All the Miles You've Earned at the end of your first year – for new cardmembers only.²

No blackout dates. Redeem your Miles for any amount to credit travel purchases such as airlines, hotels and more.³

0% Intro APR[†] for 14 months on purchases and balance transfers.

Then 14.24% to 25.24% Standard Variable Purchase APR applies.

Mature Market: Working the Niches

Petal

Prime + (9.74 – 20.74%), No Fees, No Credit Score Needed

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4% CB on Dining & Entertainment, 2% Grocery, 1% Other

Prime + (11.24 – 20.24%),

\$500 Bonus if spending \$3,000 in 3 months

\$95 Fee (waived first year)

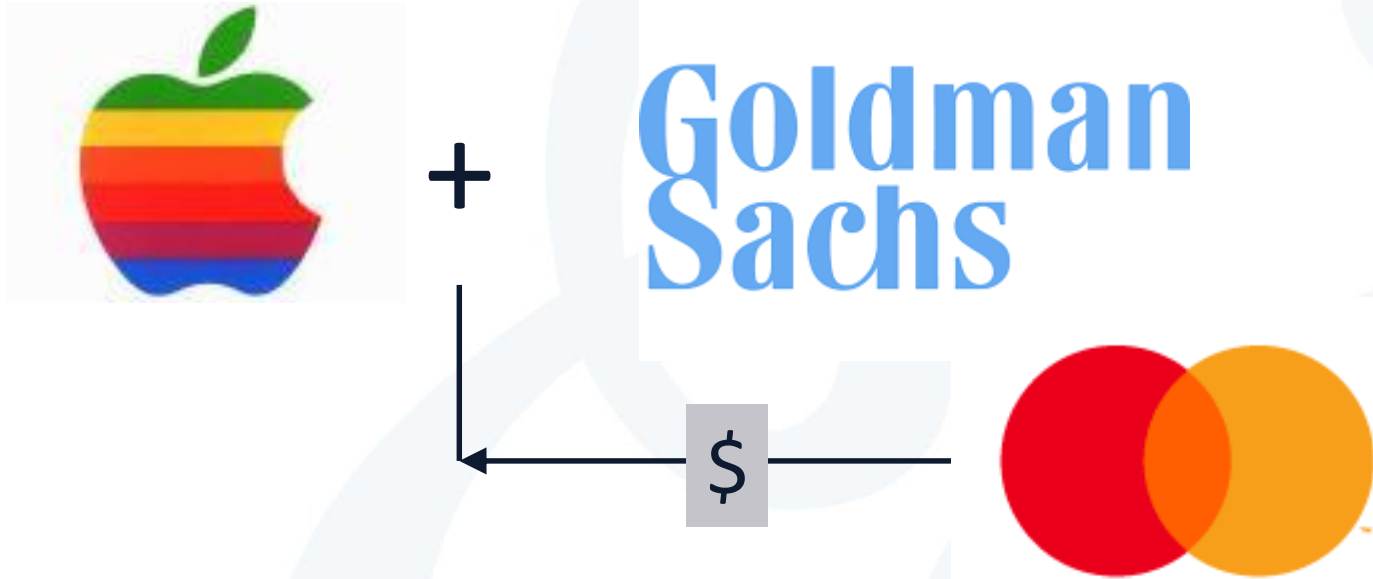
Ohoho! Someone Made a Move...



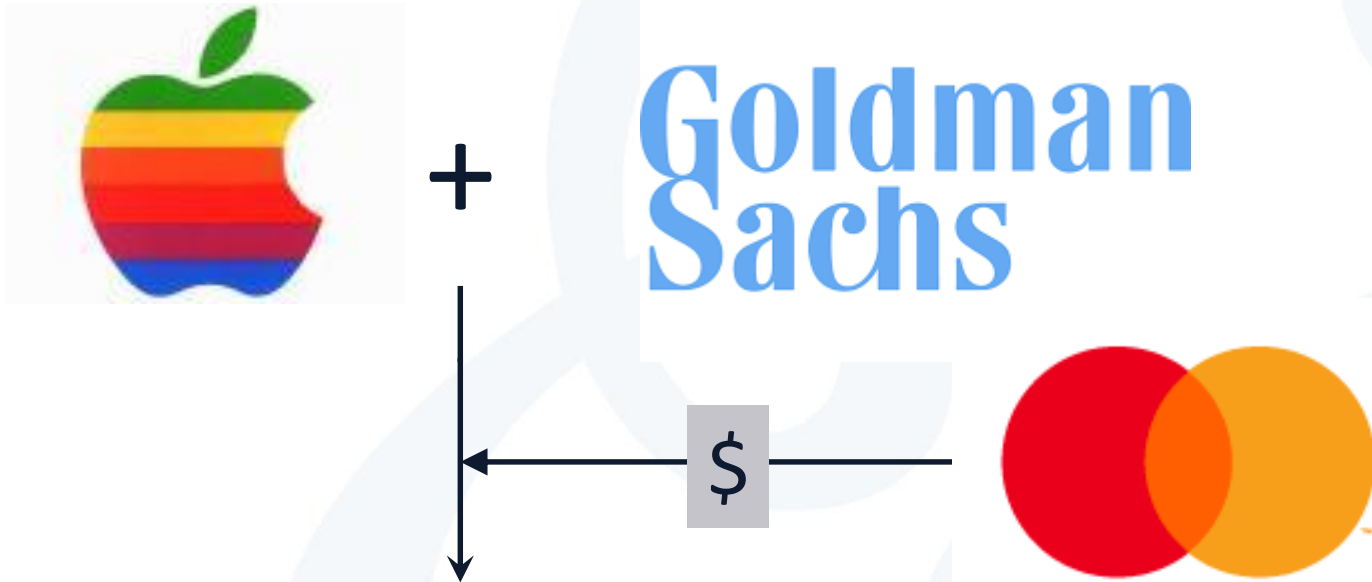
+

Goldman
Sachs

Ohoho! Someone Made a Move...



Ohoho! Someone Made a Move...



This is  Card.

**A new kind of credit card.
Created by Apple, not a bank.**

Ohoho! Someone Made a Move...



Ohoho! Someone Made a Move...



Why Is This Relevant

- **The proposition is decent:**
 - ✓ Rates P+ (7.74% - 18.74%)
 - ✓ 1% cash back physical card, 2% ApplePay, 3% Apple
 - ✓ Daily credit to account
 - ✓ No fees. At all.
 - ✓ High-end titanium physical card
- **The technology is cool:**
 - ✓ Instant approval and card on iPhone immediately!
 - ✓ Cutting edge account security
 - ✓ Very cool spending and calculation tools
- **But have we ever seen a cobrand card that doesn't provide redemption for brand merchandise?**

So What Are They Up To?

- **Move the dial on ApplePay transactions**
 - ✓ Who uses ApplePay?
 - ✓ Those with 50+ years left to live.
- **Why?**
 - ✓ Revenue source for Apple
 - ✓ If people use more ApplePay, then there will be growing lists of people who use ApplePay

So What Are They Up To?

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 - ✓ If people use more ApplePay, then there will be growing lists of people who use ApplePay
- **If you were Goldman Sachs who would you target for the card? I'd target the people who use ApplePay. Maybe the people to whom you provided ApplePay? Huge bummer.**

CU Advantages: Now More Than Ever

Having them ≠ using them

Financial

- Strong Revolver loyalty
- Better credit loss rates
- Lower funding costs
- Lower ROA Hurdles
- Lower new account costs
- Longer-term horizons

Other

- Better member access
- Internal member data
- Can be more nimble
- More trust, better reputation
- Better servicing support
- Relationship rewards!

Biggest CU Weakness

Having no data-anchored information to focus strategy conversations

It's Worth The Effort

Credit Card is Central to Strategy

- For almost all of your members who can get one, credit card is a critical product (but maybe not yours?)
- It gets used more than any other (and in public)
- It is used for specific reasons and with specific intent
- A strong card relationship is supportive of a strong total relationship; others in use are an active threat
- Can be the keystone to an overall loyalty program
- You have advantages the competition cannot match

So, What Are You Going to Do?

- Credit Card is too important to your bottom line to avoid working on it.
- Credit Card is too important to your member's interests to let your products stagnate.
- Competition is too intense to assume past successes will continue because your members love you.
- Plus, it's super interesting, a lot of fun, and really can advance individual careers.

*But Tim, you ask,
"How can I stay focused on these things?"*

How On Earth Will I Stay Current?

Callahan & Associates Credit Card Management Series

Today

CARD MARKET OVERVIEW

Aug 8

CALCULATING PROFITABILITY

Sept 19

**MAPPING PRODUCTS TO
MEMBERS (SEGMENTING)**

Thank You!

Tim Kolk, TRK Advisors

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CALLAHAN
ASSOCIATES
the credit union company