

**TRK ADVISORS**

# Credit Card Management Series

## Credit Card Market Overview & Credit Union Performance

*(including thoughts on our current environment)*

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

**CALLAHAN**  
ASSOCIATES  
*the credit union company*

Knowledge. Insight. Strategy.

# Logistics

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- 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](mailto:tkolk@trkadvisors.com))
- Callahan will provide a link to the recording once ready
- Part of a larger set of on-line sessions (details at the end)

# Ok, Enough of That

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## *Today's Topics*

- Why credit card is different
  - A look at market trends and credit union performance
  - Rates, lots happening with rates
  - How to think about where we are today
  - Growth & profitability expectations for 2020
  - What are the things we should start doing *today*
- ...and a free gift! (don't get too excited)

# Why is Card Special (abbreviated!)

## *Credit Card is Unique, and More <sup>usually</sup> Fun*

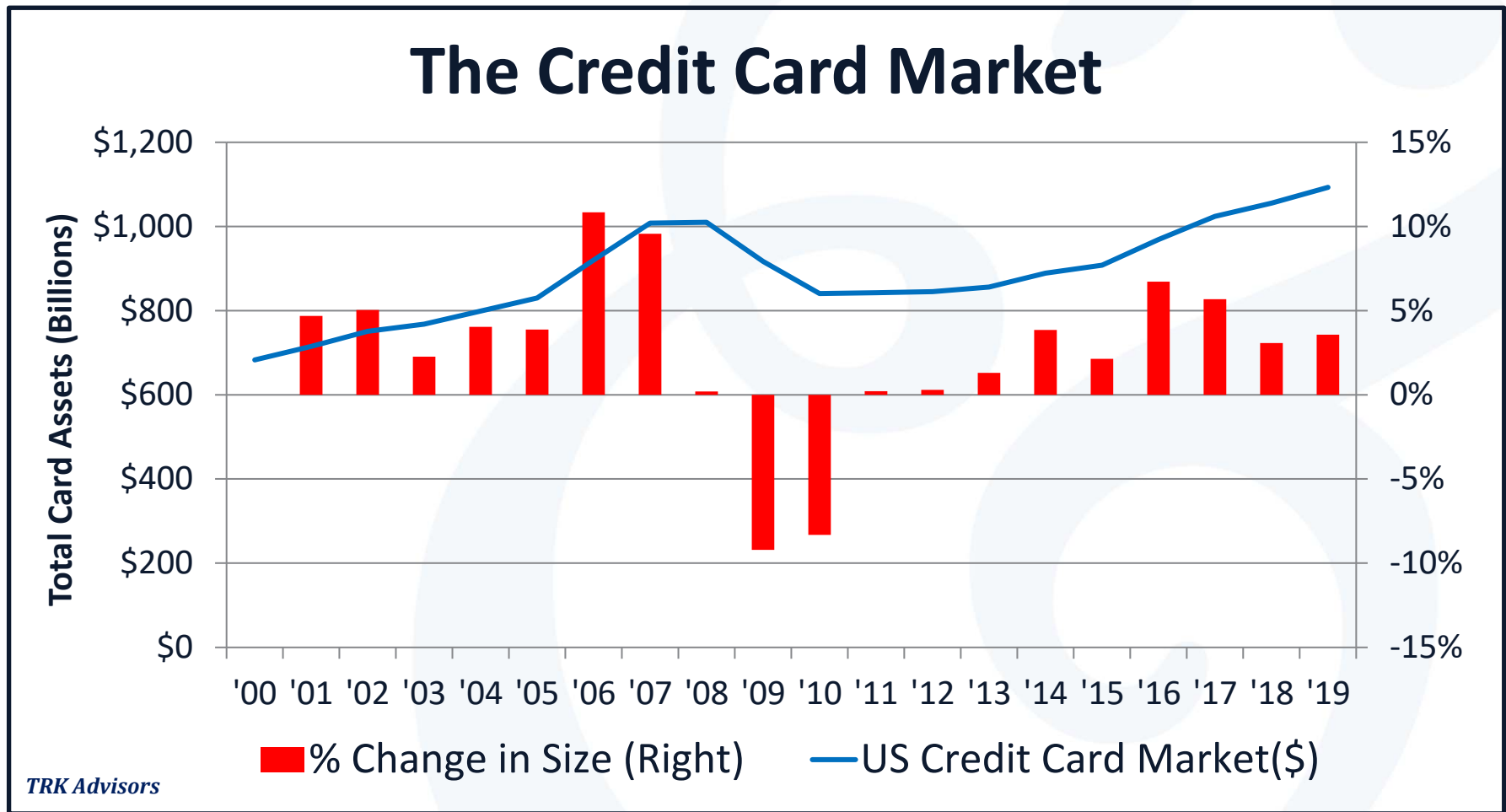
- Originating an account is only the start of the care and feeding it needs
- Performance & risk can change over time, for good or ill
- Can be backbone to a loyalty program
- Often the most used product (if it's a good one)
- Almost always the highest ROA loan product
- Even in bad times some good can be done for CU & members



# MARKET TRENDS

*(I know, I know, but we have to start somewhere)*

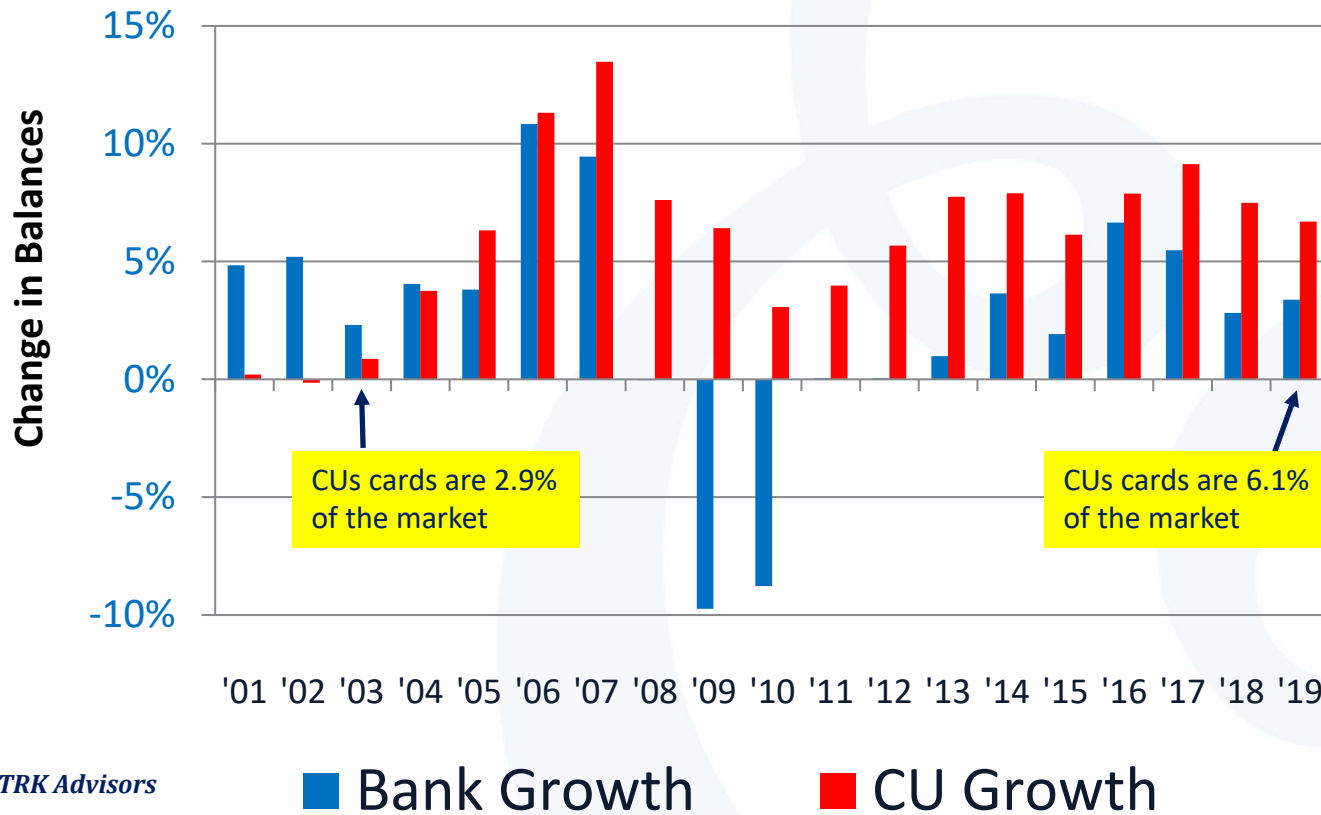
# Every Increase is a New Record



*Today at an all time record. Growth 9 years running.*

# How Have Credit Unions Done?

## Change In Card \$: Banks v. CUs



<b>2011</b>	
Banks	+0.4 Billion
CUs	+1.5 Billion
<b>2012</b>	
Banks	+0.4 Billion
CUs	+2.1 Billion
<b>2013</b>	
Banks	+7.9 Billion
CUs	+3.1 Billion
<b>2014</b>	
Banks	+29.6 Billion
CUs	+3.4 Billion
<b>2015</b>	
Banks	+16.2 Billion
CUs	+2.8 Billion
<b>2016</b>	
Banks	+57.1 Billion
CUs	+3.9 Billion
<b>2017</b>	
Banks	+50.1 Billion
CUs	+4.9 Billion
<b>2018</b>	
Banks	+27.2 Billion
CUs	+4.3 Billion
<b>2019</b>	
Banks	+33.5 Billion
CUs	+4.2 Billion

*Pretty good story for credit unions (overall...)*

# Large Issuer Results (so many #s!)

*Top 10 Visa & MasterCard Issuers in the US, 2019*

Issuer	Volume (\$MM)		Accounts (M)			Per Active		Turn Rate
	Balances	Purchases	Total	Active	% Act	Bal	Purch	
JP Morgan Chase	\$ 168,924	\$ 810,360	76,200	42,224	55%	\$4,001	\$19,192	4.8
CitiBank	115,836	438,343	58,205	39,700	68%	\$2,918	\$11,041	3.8
Bank of America	107,522	377,120	42,605	29,100	68%	\$3,695	\$12,959	3.5
Capital One	107,157	370,246	95,470	50,870	53%	\$2,106	\$7,278	3.5
Wells Fargo	42,956	136,980	17,770	9,990	56%	\$4,300	\$13,712	3.2
US Bank	41,432	153,336	23,111	11,637	50%	\$3,560	\$13,177	3.7
Barclays	26,659	82,263	10,696	7,775	73%	\$3,429	\$10,580	3.1
Synchrony	20,750	57,280	24,200	13,500	56%	\$1,537	\$4,243	2.8
Navy FCU	18,881	24,133	3,487	2,512	72%	\$7,516	\$9,607	1.3
USAA	17,065	44,583	5,499	4,180	76%	\$4,083	\$10,666	2.6
<b>Total, Top 10</b>	<b>\$ 667,182</b>	<b>\$ 2,494,644</b>	<b>357,243</b>	<b>211,488</b>	<b>59%</b>	<b>\$3,155</b>	<b>\$11,796</b>	<b>3.7</b>
<b>2019 Change</b>	<b>5%</b>	<b>8%</b>	<b>2%</b>	<b>3%</b>		<b>1%</b>	<b>4%</b>	
<b>2018 Change</b>	<b>3%</b>	<b>10%</b>	<b>2%</b>	<b>2%</b>	<b>59%</b>	<b>1%</b>	<b>7%</b>	<b>3.6</b>
<b>2017 Change</b>	<b>8%</b>	<b>16%</b>	<b>5%</b>	<b>5%</b>	<b>59%</b>	<b>3%</b>	<b>10%</b>	<b>3.4</b>

Balance growth kind of steady.  
Purchases becoming harder to get.

**(Still a) FUN FACT**  
In 1996 this was 1.5!



# Credit Unions Did Well In Total, But...

**Distribution of Credit Union Card Program Growth**

Size	Size	Balances (2019)		Growth (2019)			% Shrinking
		\$ Bil.	% of \$	\$ Bil.	Rate	% of All	
Top 50	\$161MM-\$17.1B	\$37.5	61%	\$3.6	11%	83%	14%
51-200	\$48-\$159MM	\$12.8	21%	\$0.5	4%	11%	31%
201-500	\$16-\$48MM	\$8.5	14%	\$0.2	2%	5%	40%
501-1000	\$5-\$16MM	\$4.6	7%	\$0.0	1%	1%	50%
<u>1001-2096</u>	<u>\$1-\$5MM</u>	<u>\$2.6</u>	<u>4%</u>	<u>\$0.0</u>	<u>0%</u>	<u>1%</u>	<u>55%</u>
Total		\$66.0	100%	\$4.4	0%	100%	49%

**% Growing at Below Average CU Rate**

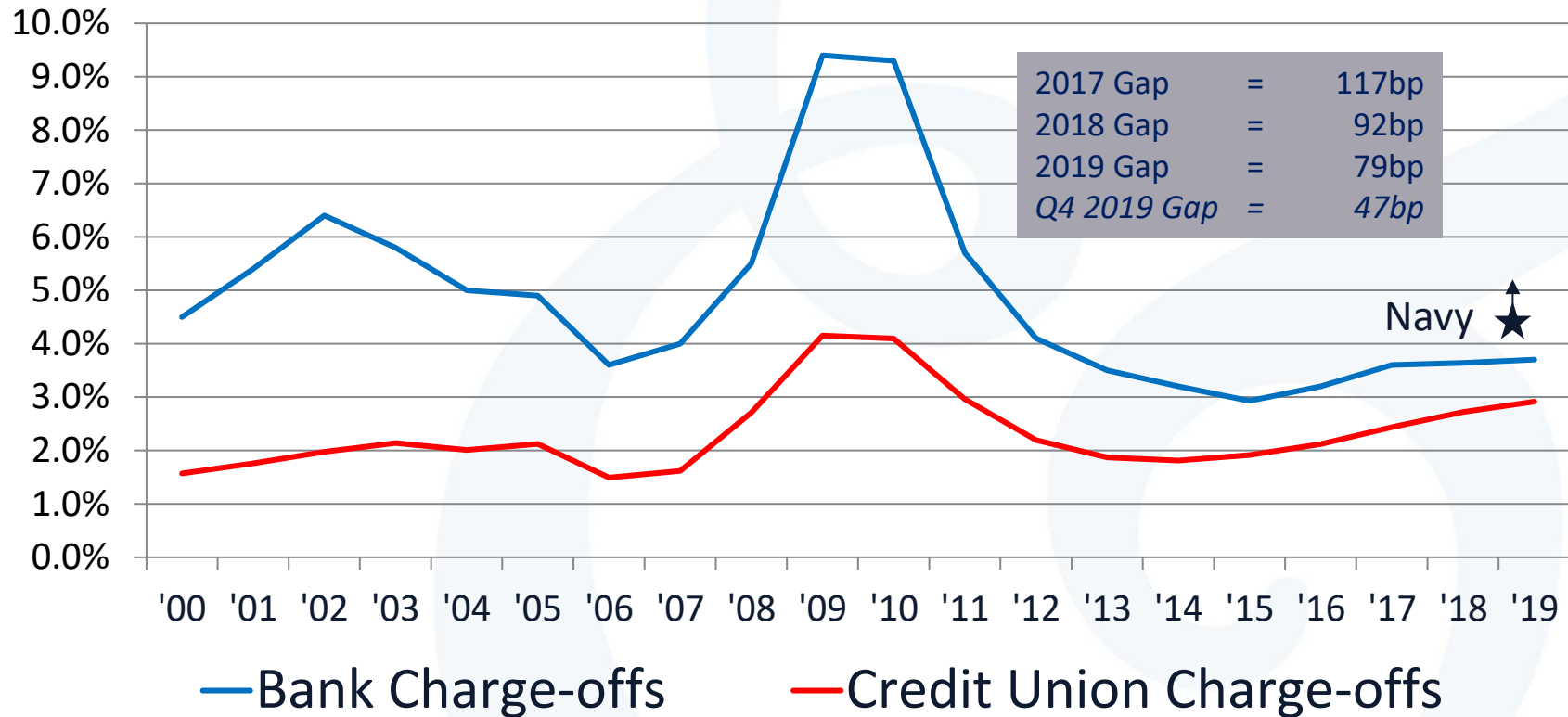
Size (>\$1MM)	2015	2016	2017	2018	2019
Top 50	46%	46%	52%	62%	68%
51-200	67%	67%	65%	77%	77%
201-500	62%	64%	72%	79%	82%
501-1000	73%	77%	75%	77%	82%
<u>1001-2096</u>	<u>78%</u>	<u>80%</u>	<u>83%</u>	<u>83%</u>	<u>85%</u>
<b>Total</b>	73%	75%	77%	80%	83%

## *We Can't Let The Big Picture Distort Our Individual Situations*

- Big get most: Navy has 30% of all CU balances, took 60% of CU growth (+15%)
- Without Navy FCU the credit union market grew at <4%... Same as banks!
- % falling behind is increasing. Even largest are not immune.

# Credit Risk: A Change?

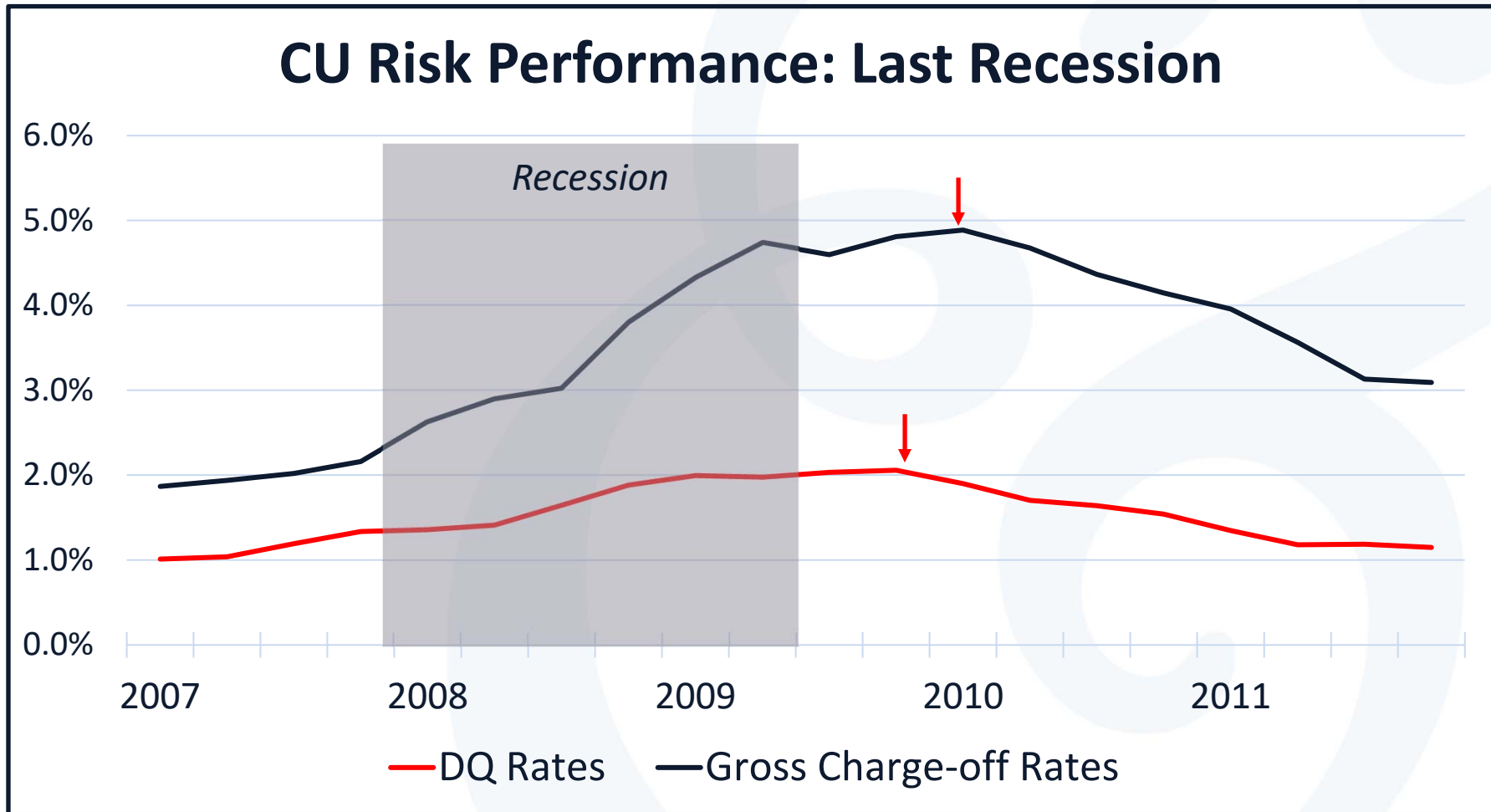
## Net Charge-Off Rates



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*Last Year's Comment: "The next recession will be VERY interesting."*

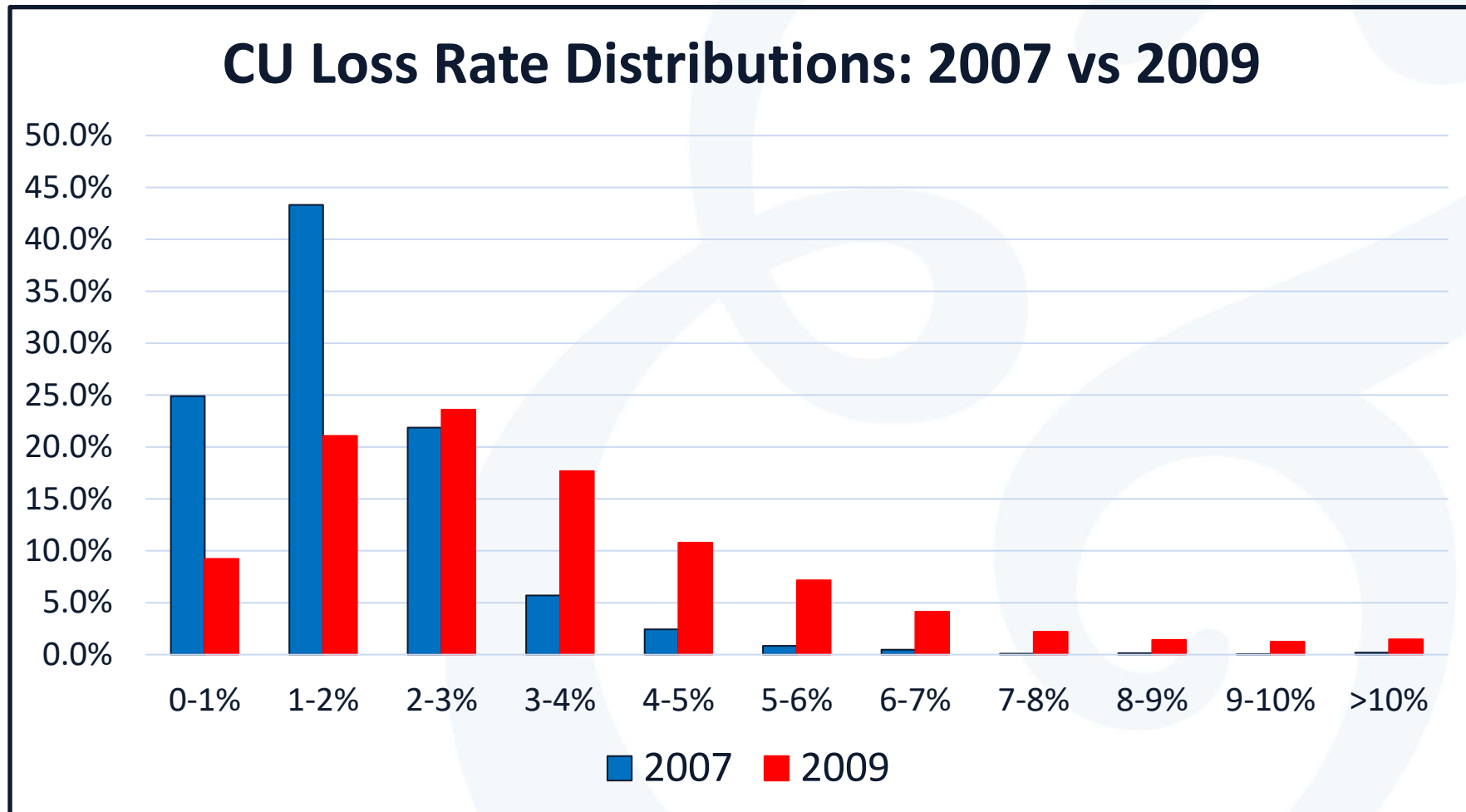
# What Happened in the Last Recession?



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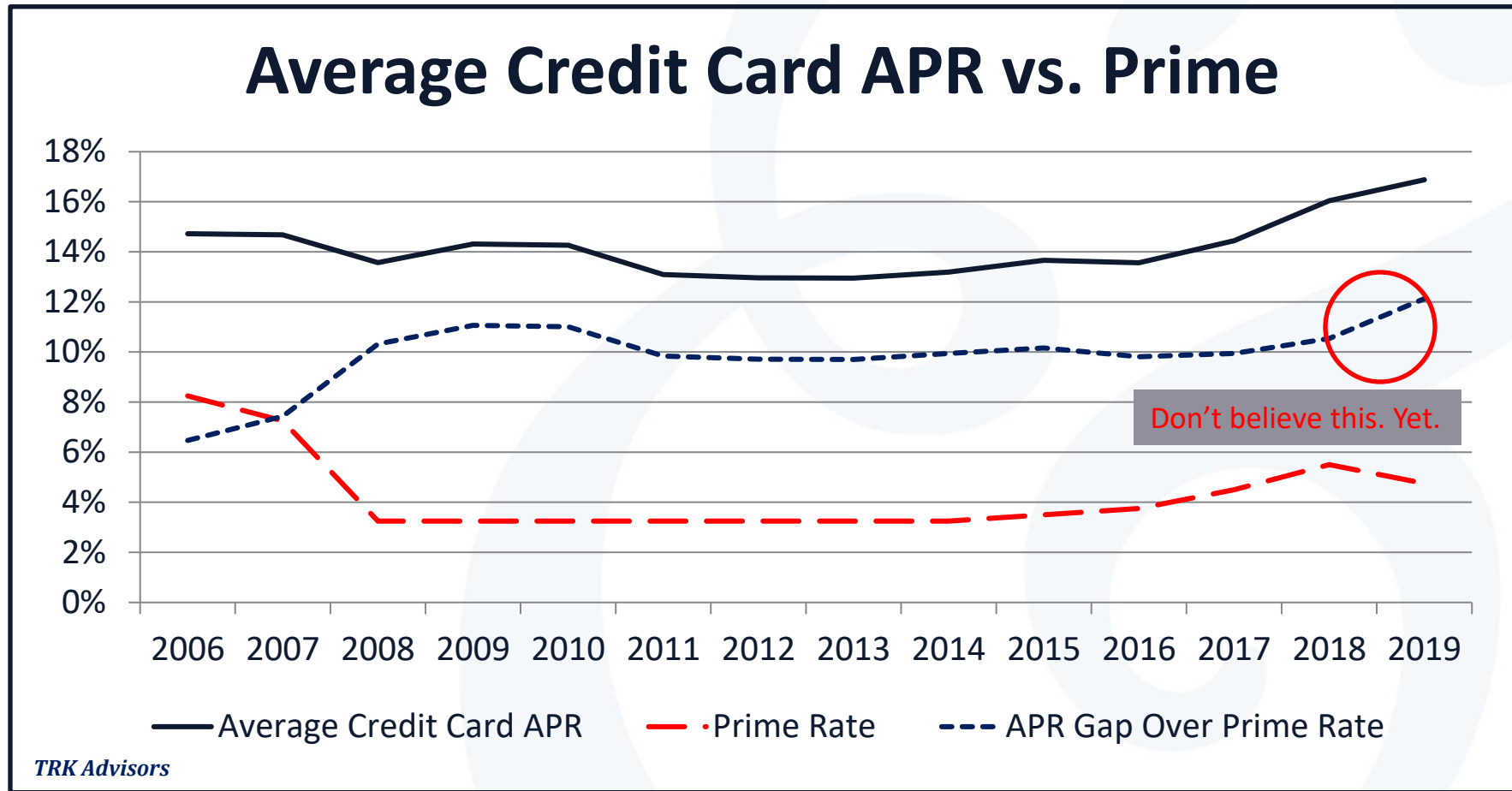
*Rapid escalation across quarters once it started.*

# What Happen Last Recession?



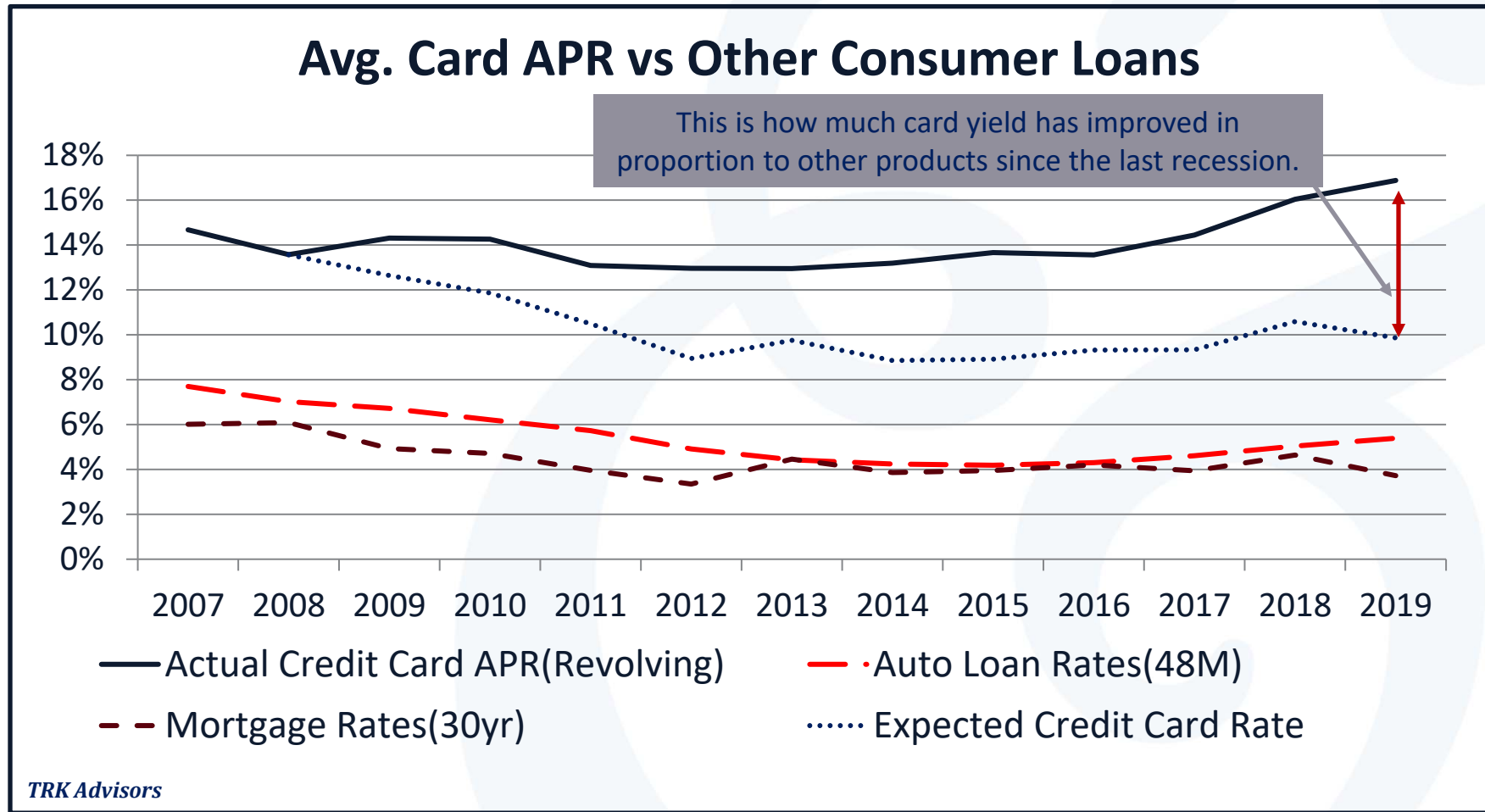
*Recessions = Greater Performance Variations (you have some influence)*

# Oh Yeah: What About Rates?



*Consumers have been disinterested in rate competition for years.  
How are you communicating your value?*

# WAKE UP: This One Is Important!



*Just because it's a smaller asset category, don't lose sight of it.*

# 2019 Profitability

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## *(Another) Very Strong Year*

- Largest issuer card profitability was up from 2018, fueled by a rising Prime Rate and a very attractive loss rate (for the banks)
- A survey of seven of the largest issuers reported Net Income up 9.6% over 2018 (*source: Nilson Report*)
- Pretax ROAs are estimated to range from 3-5%
- Most of our credit union clients also saw very strong years
- Average Prime was up about 50 basis points, while overall credit union funding costs were up 20 basis points.
- Typically, the biggest challenge has been funding market-level rewards without premium products (Signature/World) and also with below market interest rates.

*But now....other immediate concerns*

# 2020 Rate Environment

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## *Yield & Cost of Funds Impacts*

### **Yield**

- Prime is down from 5.50% entering 2019 to 3.25% today.
- Average Prime in 2019 was 5.3%.
- If it stays at 3.25%, Prime will average 3.6% this year
- Variable APRs will be down about 170 basis points from 2019
- Yield impact depends on revolve rate...more coming in a sec.

### **Cost of Funds**

- Should also come down. Was 0.9% in 2019.
- All time low was 0.5% in 2015. 4 years after the recession.
- Moves more slowly than Prime Rate changes.

*We rode a wave up, now we ride it down.*



# 2020 Consumer Economy

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## *Balances and Purchases*

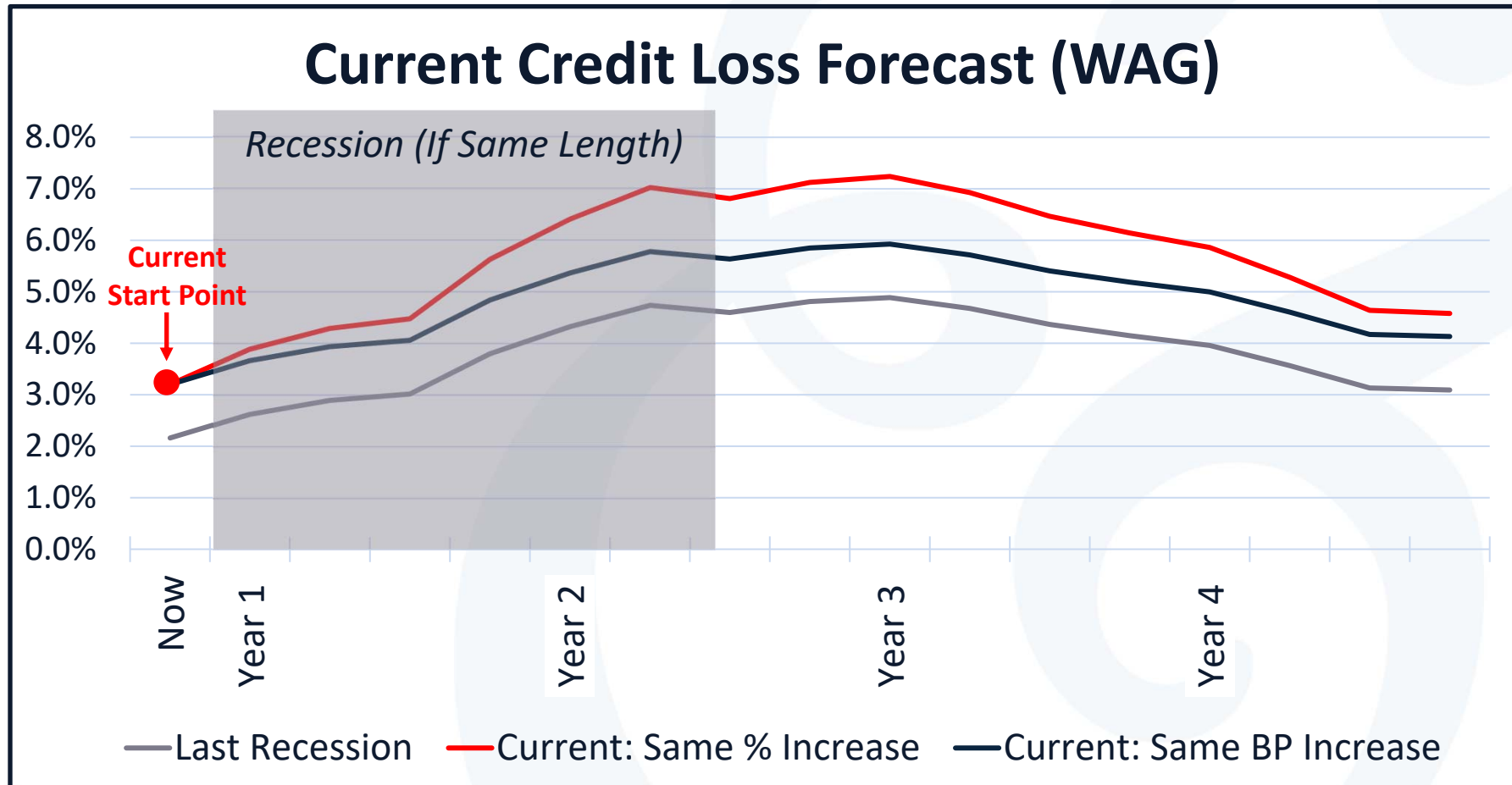
### **Balances**

- Balances tend to pretty sticky, even in a recession.
- 2009-2010 total balances came down \$169 billion.
- But there were almost exactly that many dollars charged-off.
- Consumer appetite and capacity stayed pretty level.
- But it took until 2014 to get to 3+% growth again.
- Took until 2017 to get to 2008 balance levels overall
- Credit unions grew throughout

### **Purchase Volumes**

- More immediate changes: 2008-2009 down about 10% in total
- Back to record volumes by 2011

# What if Risk is Like Last Recession?



*By all accounts this one is coming faster and harder. Duration?*

# Alright, Let's Bring It Together

	<i>Non-Rewards Product</i>		<i>Rewards Product</i>	
<i>Portfolio Drivers</i>	2019	2020	2019	2020
<b>PER ACCOUNT \$</b>				
Average Balance	\$3,000	\$3,000	\$2,500	\$2,250
Average Spend	\$4,500	\$4,050	\$7,500	\$6,000
<b>APR &amp; YIELD</b>				
Average Prime Rate	5.3%	3.6%	5.3%	3.6%
+ Margin: Prime +	6.9%	6.9%	8.9%	8.9%
= Resulting APR	12.2%	10.5%	14.2%	12.5%
x Revolve Rate	90.0%	90.0%	70.0%	75.0%
= Yield	11.0%	9.5%	9.9%	9.4%
<b>OTHER</b>				
Interchange Rate	1.70%	1.70%	1.85%	1.85%
Reward Cost/\$	0.00%	0.00%	\$0.011	\$0.011
Operating Expense	\$125	\$125	\$125	\$125
<b>P&amp;L Items</b>	<b>2019</b>	<b>2020</b>	<b>2019</b>	<b>2020</b>
Yield	11.0%	9.5%	9.9%	9.4%
Cost of Funds	-0.9%	-0.7%	-0.9%	-0.7%
Net Interest Income	10.1%	8.8%	9.0%	8.7%
Net Charge-offs	-3.5%	-5.3%	-2.5%	-3.8%
Interchange	2.6%	2.3%	5.6%	4.9%
Reward Expense	0.0%	0.0%	-3.4%	-3.0%
Net Interchange	2.6%	2.3%	2.2%	1.9%
Fees	0.4%	0.4%	0.2%	0.2%
Operating Expense	-4.2%	-4.2%	-5.0%	-5.6%
Net Income	5.4%	2.0%	3.9%	1.5%
Net Income/Acct	\$161	\$61	\$98	\$34

## *Profitability: 2020 vs 2019*

- Based on what we think are reasonable numbers, but do your own!
- Assumes 10% purchase reduction on low-rate cards, 20% on reward cards.
- Funding cost down 20bp
- Charge-offs + 50%.
- \$125 per year operating costs per active account.
- Rewards: 1.5 points per \$1, 1 cent per point value, 75% redemption.
- If you don't have a reliable P&L that is something to get done immediately.

*Expect a meaningful decline*

# Alright, Let's Bring It Together

## Profitability: 2020 vs 2019

Portfolio Drivers	Non-Rewards Product		Rewards Product	
	2019	2020	2019	2020
<b>PER ACCOUNT \$</b>				
Average Balance	\$3,000	\$3,000	\$2,500	\$2,250
Average Spend				
<b>APR &amp; YIELD</b>				
Average Prime Rate				
+ Margin: Prime +				
= Resulting APR				
x Revolve Rate				
= Yield				
<b>OTHER</b>				
Interchange Rate				
Reward Cost/\$				
Operating Expense				
<b>P&amp;L Items</b>				
	2019	2020	2019	2020
Yield				
Cost of Funds				
Net Interest Income				
Net Charge-offs				
Interchange	2.6%	2.3%	5.6%	4.9%
Reward Expense	0.0%	0.0%	-3.4%	-3.0%
Net Interchange	2.6%	2.3%	2.2%	1.9%
Fees	0.4%	0.4%	0.2%	0.2%
Operating Expense	-4.2%	-4.2%	-5.0%	-5.6%
Net Income	5.4%	2.0%	3.9%	1.5%
Net Income/Acct	\$161	\$61	\$98	\$34

**For every \$10 million in balances, expect about \$300,000 in bottom line reduction**

**We think this is more likely optimistic than pessimistic**

**Actions you take now can have an influence**

- If you don't have a reliable P&L that is something to get done immediately.

*Expect a meaningful decline*

# So, What Can We Do?

## Member Supporting

- Provide payment flexibility (e.g. automated skip-a-pay, payment deferrals, be liberal with servicing requests)
- Suspend interest and fee assessments
- Consider rate promotions to those you feel good about
- Consider incentives to those that worry you (e.g. rewrite card balances as closed end loans at lower rates & reduce line)
- Encourage rewards redemption (for paydown of balances!)
- Change reward promotions to more relevant categories

## Credit Union Protecting

- Monitor credit scores quarterly, watch for erosion
- Watch for behavior and relationship changes (e.g. paid-in-full stops, direct deposit stops)
- Prepare Collections for more volume (& make sure card is not ignored)
- Monitor cards that are newly used after being dormant
- Review for single service or trivial relationship and consider closing
- Consider tightening approval requirements (particularly new members)
- Line decrease programs? Maybe.

*Card programs don't turn on a dime. But smart tactics can make a difference.*

# Other Potential Implications

## *What Other Impacts? Let's guess:*

- Accelerates focus on remote servicing and delivery, esp. mobile. Once acclimated they are unlikely to revert.
- Capturing eCommerce sales ~~important~~ CRITICAL
- Branches as a new account source? Nope.
- Proactive marketing to existing members: more important than ever.
- Cash rewards more appealing, redemption rate up?
- Contactless sounds pretty nice right now
- Overall credit risk shift. When to consider repricing?  
(*Partial answer: 3 years before you need it*)

*A level head, a clear understanding, and internal trust are critical.*

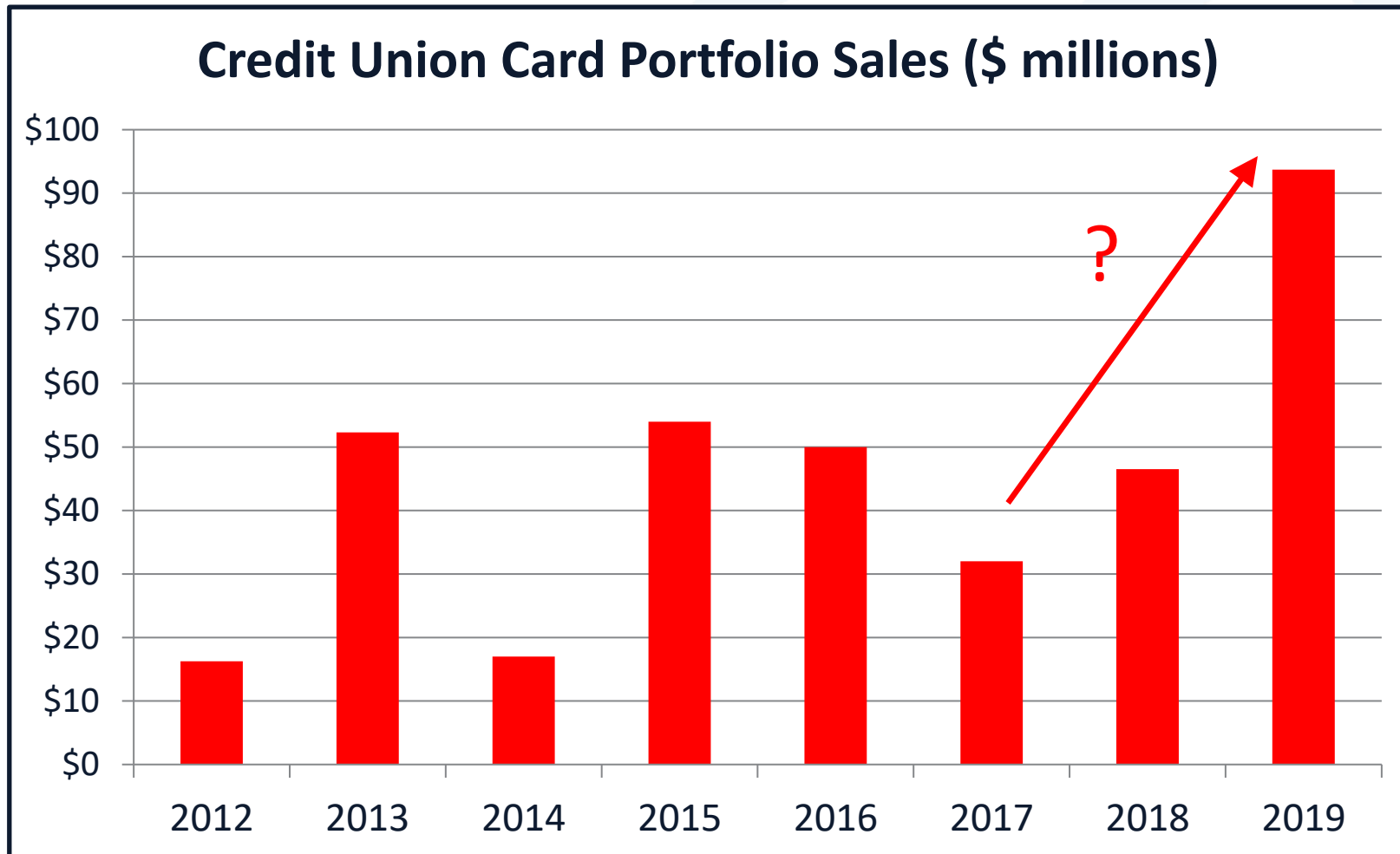
# WHAT TO DO RIGHT NOW!

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- Calculate profitability impact on the card program (and overall credit union)  
*Don't have a trusted P&L for card? There's a webinar for that!*
- Create a plan to address service requests & develop a proactive strategy for member relief.
- Help cardholders leverage all available mobile servicing tools.
- Get ahead of collections bubbles: staffing, prioritizing, logistics.
- Average revolving card APR is now about 15% (Prime +12%). If yours is significantly below that you may be being nicer than can be sustained. Consider careful changes.
- Consider reducing approved accounts for newer or less well known members. All scores are going to be dramatically behind.

*These are not things to do tomorrow. Today is tomorrow.*

# Agent Programs Already on the Rise?



*Can be a strategic way to deliver the product at less risk. But be careful!*



# How On Earth Will I Stay Current?

## TRK Advisors Online Card School

- June 4*    **DESIGNING CARD PROGRAM REPORTING FOR SUCCESS**
- Aug 27*    **BUILDING YOU ANNUAL CARD ACTION PLAN**
- Oct 29*    **LET'S SEE WHERE WE ARE...**

To register for 2020 live sessions:  
[onlinecardschool.com](https://onlinecardschool.com)

Click on green registration buttons

# But Wait, There's More!

## For Callahan Clients

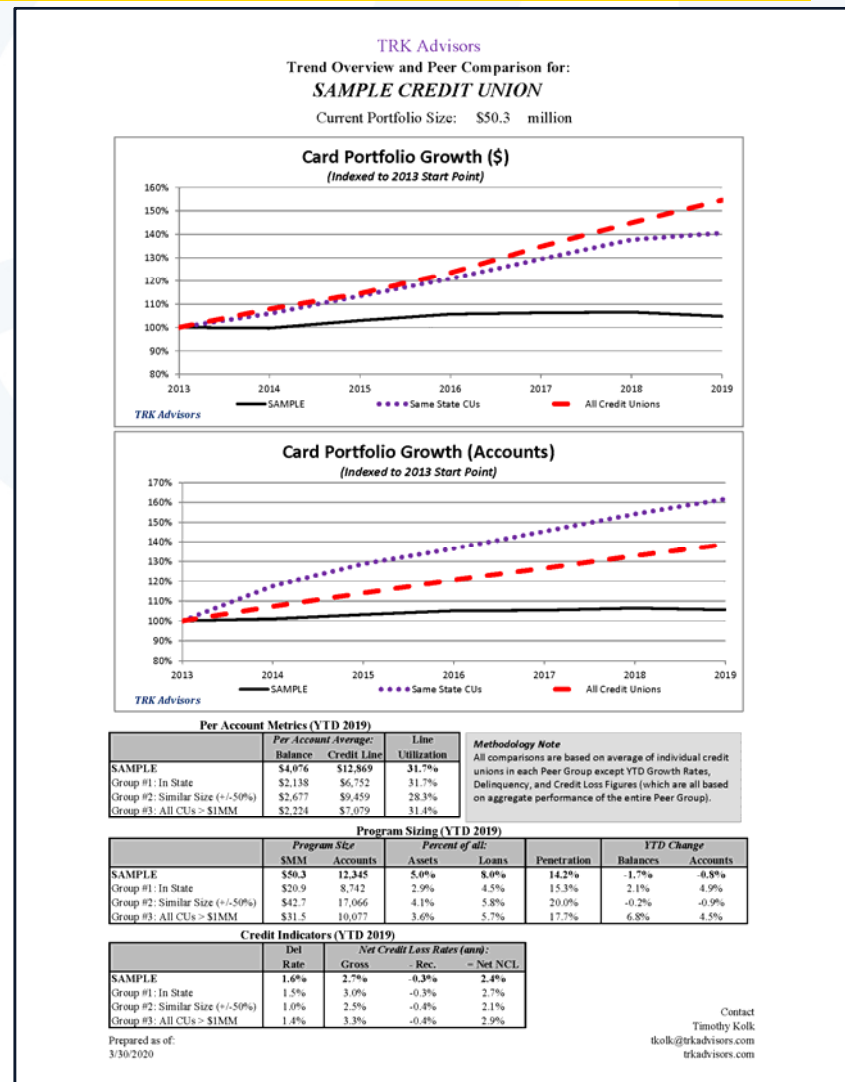
### Peer Benchmark Report

Benchmark your card program's performance to a variety of peer benchmarks for growth trends, size and penetration, average balance metrics, and risk levels.

email: [tkolk@trkadvisors.com](mailto:tkolk@trkadvisors.com)

phone: 603-924-4438

site: [trkadvisors.com](http://trkadvisors.com)



Thank You!

Tim Kolk, TRK Advisors

[tkolk@trkadvisors.com](mailto:tkolk@trkadvisors.com)

(603) 924-4438

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ASSOCIATES  
*the credit union company*

Knowledge. Insight. Strategy.