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Evaluating your credit card business

By Wally Hess

The payment industry continues to evolve rapidly. Successful credit unions understand this change and continue to assess and adjust their offerings to meet their members' needs. In this issue, we will focus on the role credit cards play in a credit union's strategy. Since most credit unions offer credit cards, either directly or through an issuing partner, we will focus on the key strategic issues involved in deciding on what route to take when offering credit cards.

At first glance, the credit card business looks daunting for credit unions. There are approximately $650 billion in credit card receivables, and 92 percent of these are owned by the top 10 banks. The remaining 8 percent is split about evenly between credit unions and non-top 10 banks. This concentration has occurred over the past 15 years because the large issuers can afford larger credit limits, custom-tailored reward programs, 24/7 customer service anywhere in the world and lower rates as well as aggressive marketing and promotion programs. They have either purchased portfolios or lured cardholders away from the smaller issuers.

This does not mean that credit unions should abandon the credit card business. However, it is important that your offering be well-planned, both in terms of marketing and implementation. For example, not only should there be a full-time management team assigned to the business, senior management must make an ongoing commitment of marketing and financial resources as well as time. A successful card program requires the involvement of the entire organization.

In addition, it is important for credit union card issuers to regularly evaluate their credit card businesses. This should be performed by an outside industry expert about once per year. To enable an impartial evaluation of all options, it's important that the firm not be exclusively aligned with a single bank issuer. This evaluation should clearly show the trends in the credit union's card business and the financial effect on the credit union. It should also suggest alternative ways to improve.

A complete analysis will also assess the costs and opportunities associated with all strategic options, including a portfolio sale and partnering with a larger issuer. Several of the key components of this evaluation are:

- account growth and account utilization,
- trends of balances per account,
- finance charge yield,
- card usage,
- fee structure, and
- credit losses and delinquency trends.

It will be important to understand the underlying factors in each of these trends and relationships. The cost of reversing negative and accelerating positive trends, and the resulting benefits, should also be assessed.

The evaluation should provide the credit union with a range of future performance forecasts for the portfolio based on:

- past performance,
- credit card industry trends,
- demographics, growth and membership size, and
- discussion with management on planned programs and changes.

The financial summary should include the value of the credit card business to the credit union. It should also measure the resources necessary to maintain and grow the business in house.

When considering whether to outsource the credit card business, two major factors to consider are:

1. The financial effect on the credit union. The transaction can be structured to both purchase the portfolio at a premium and to provide on-going revenue to the credit union. The cash, capital and management time freed up by this type of transaction can be used by the credit union to invest in additional products, services or branches for its members.

2. The effects on the members. This is at least as important as the financial effects. A good partner will provide a card product that is very competitive on rate, fees, customer service and special features. A good partner will be most interested in making the member happy, because it does not want to lose the cardholder. It will be in everyone's interest to make the transition to the new issuer as seamless as possible to the member.

Once this evaluation has been performed and thoroughly discussed with management along with the measurement of alternatives, it should be clear which alternative actions should be pursued.

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