

# State of the Industry – Credit Cards

Written by: Tom Koeppen

Published August 26, 2009 on Loyalty360.org

## Loyalty 360

## Loyalty Déjà vu!

## Loyalty Boomerang!

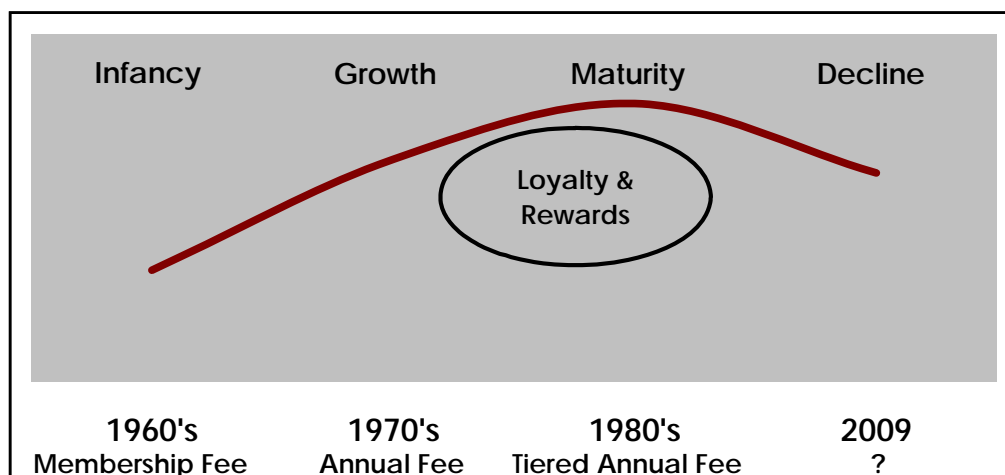
All three depict an image...all encompassing, looking back, coming back around!

These words also portend the key to profitable success in the post “credit crunch” credit card marketplace...LOYAL CUSTOMERS.

The credit crunch has created a world of opportunity to retain existing and create new Loyal Customers.

But, in order to “do it right”, we have to “Boomerang, Déjà vu, 360”...look back and go way back...because as George Santayana proclaimed, “Those who do not learn from history are doomed to repeat it”...so let’s start with some history, hopefully learn from it and then not repeat it!

Below is a depiction of the Life Cycle of the General Purpose Credit Card Market:



### REWARDS PROGRAMS – A Brief History

As the market was growing for credit cards in the 1960's and 1970's, there was no need to add value to the cards, consumers were happy to have the “privilege” to buy now – pay later. But, as the market grew and competition increased from the mid 1970's thru the mid 1980's, adding value became key to differentiating your card from your competitor.

# State of the Industry – Credit Cards

*Written by: Tom Koeppen*

*Published August 26, 2009 on Loyalty360.org*

The value game changed exponentially in 1986 with the launch of DiscoverCard and its “cashback” reward program. Suddenly, the Rewards Wars were on!

From the mid 1980’s through 2008 the war continued, with banks segmenting their customers and offering a staggering list of rewards, incentives and offers...along with fees to support the programs and further segment their cardholders.

This segmentation and specialization of offers and rewards perpetuated the Reward Wars and “upped the ante” in the rewards war, a rewards “arms race” of sorts being waged for the consumer “share of wallet”.

To remain competitive and retain customers the offers developed were re-developed, the rewards enhanced, eligibility requirements changed annually and the rewards redemption thresholds moved up, down and back up depending on the banks profitability.

All of this jostling to capture “share of wallet” (note: “Share of wallet” became the industry’s term for customer payment preference) resulted in a complexity of programs, an escalation of costs and the mainstreaming of “pay to play” marketing strategies across the industry.

## **FEES – A history**

Like rewards, fees (shown at the bottom of the card lifecycle graphic), specifically annual fees, have followed an evolution that tracked and then mirrored the life cycle of rewards programs.

Starting life as membership fees (the “privilege” to belong) in the 60’s, the consumer paid for the privilege to belong or “carry” the card. Perhaps best illustrated in the name itself of one of the first cards in the industry...“Diners CLUB”.

Again, as with rewards, as the market grew in the 1970’s, and cards could be used anywhere, fees became a way to differentiate a cards “exclusivity or brand”.

As the market continued to grow throughout the 1980’s and more cards were in more consumer’s hands, differentiation again became a necessity. Remember that “share of wallet” objective? This period ushered in and cemented the connection and inter-relationship of fees and rewards.

As the marketplace raced from growth to maturity in the 1980’s and 1990’s, fees increasingly became tied to the level or amount of a card’s rewards. If a consumer wanted one airline mile for every dollar they spent on their card, they would gladly pay \$60 annually for that privilege. If a consumer wanted Cashback on every purchase, they could pay \$25 for that benefit. On and on it went, more rewards, more fees, tiered

# State of the Industry – Credit Cards

Written by: Tom Koeppen

Published August 26, 2009 on [Loyalty360.org](http://Loyalty360.org)

rewards, tiered fees etc. Throughout all of this, fees became more and more linked to rewards.

Now tied directly to cardholder rewards, and no longer about the privilege of being in the club, cardholders no longer had an intrinsic affinity to a brand or level of service...share of wallet was the goal and the strategy was "pay to play".

## 2009 – The game changes

As the lifecycle chart illustrates, in 2009 the market decline begins. The decline, driven by the banks themselves, as they attempt to "clean up" their portfolios, to reduce risk and reduce expenses, includes some of the following tactics:

- Closing accounts
- Lowering credit lines
- Raising redemption thresholds on rewards programs
- Increasing fees

## LOOKING AHEAD – It's Déjà vu all over again!

Not just a play on words...let's exam the current marketplace trends...

1. Customers actually possessing a credit card account – down
2. Average credit line available – down
3. Rewards programs – declining
4. Fees – going up

Sound like something from our history lesson? That's right...welcome back to the 1970's!

So do we learn from our past or are we doomed to repeat it? We, as marketers, can re-write history the second time around! Let's take a look at how....

Below is the "most likely" next steps being taken by banks to gain sales and share of wallet. It's a short-term focused, a "What do I need to survive today?" strategy.

### Most Likely Industry "Next Steps"

More Risky	Risky	Less Risky
\$50-75 Annual Fee	\$30-50 Annual Fee	No Fee
Limited Rewards	Standard Rewards	Standard Rewards

The connection of fees and rewards is still cemented in the minds of the banks marketers - most likely a result of the struggle to market in an environment where management is looking to reduce risk at all costs. It's a narrow view - for the near term, look for more of the past.

# State of the Industry – Credit Cards

Written by: Tom Koeppen

Published August 26, 2009 on [Loyalty360.org](http://Loyalty360.org)

Below is a look at the next “next steps” that will evolve when the above, most likely next steps scenario, proves to not gain sales.

## Potential “Enhanced” Programs

More Risky	Risky	Less Risky
\$50-75 Annual Fee	\$30-50 Annual Fee	No Fee – Standard Rewards
Limited Rewards	Standard Rewards	\$20-25 - Enhanced Rewards

Once again, witness the connection of fees and rewards, but as banks recover from the likely fall-out from the “reduce risk at all costs” strategies, banks will determine that they must find a way to “hold on” to their best (ie: less risky) customers. For these fortunate folks...they can pay for more rewards. “Pay to Play” strategies will continue.

Finally, below is the scenario that we believe makes the most economic sense for building sales and adding value.

## Makes the Most Sense Programs

More Risky	Risky	Less Risky
\$20 Annual Fee	\$20 Annual Fee	\$20 Annual Fee
No Rewards	Standard Rewards	Enhanced Rewards

Research shows, a fee program gets preferential treatment and usage over those cards that don't have an associated cost. Therefore, keeping annual fees static and using rewards and enhancement programs as strategies allows the card's “value” to be adjustable for each type of customer's risk profile. To that end, experience tells us:

- Risk profiles correlate with a customer's loyalty and value - the riskier a cardholder, the fewer alternatives are at their disposal. Customer's share of wallet can be maintained at much lower levels of value.
- Using rewards and enhancements to add “value” allows marketers maximum flexibility to provide a payment vehicle to riskier customers and influence higher usage for all others.
- The outcome is cards that are coveted by a broader range of customers, by providing the right reward structure to encourage usage and loyalty, with high perceived value.

So yes, as marketers we can re-write history the second time around, using the tools we have today (modeling, analytics, offer optimization and opportunity segmentation) we can CREATE loyal customers without engaging in Rewards and Fee wars.