



# enhance

In association with Priority Collection

for people involved in payment card marketing and product development

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Issue Five, March 2007

## In The News

### There's no substitute for quality

Troubling but not completely unexpected news from the UK: following an investigation by the Financial Services Authority, some leading institutions have been hit with substantial fines. The highest, which was paid by GE Capital Bank, was a whopping £610,000 (nearly \$1.2 million), while Capital One was fined £175,000 (\$400,000).

The reason? Mis-selling of Payment Protection Insurance (PPI). Valued at as much as £5.5 billion (\$10.6 billion) a year, PPI is designed to cover policy-holders for the repayment of loans if they fall ill or lose their jobs. According to the Office of Fair Trading, which has referred the PPI market to the Competition Commission, only around 15-20% of premiums were paid out as claims.

For many financial services institutions in the UK, PPI has been a very important source of income:

Source: CSFB

Institution	Estimated share of group pre-tax income
Lloyds TSB	15%
A & L	15%
Northern Rock	10%
HBOS	
RBS	7-8%
Barclays	

It's important to stress that the vast majority of PPI sellers have adequate systems and controls in place, and that GE Capital Bank and Capital One have hurried to put things right, internally and with their policy-holders.

But there's an important lesson here for all card issuers: sustained, quality profits depend on offering sustainable, quality products to customers.



## Channel optimisation:

### 6 rules for getting the most value out of your card acquisition budget

Here are a couple of statistics to think over:

**Fact 1:** According to Forrester Research, nearly three out of four new credit card hopefuls in the US now choose to apply via the Internet.

**Fact 2:** U.S. issuers mailed nearly 8.0 billion credit card solicitations last year, a 30% increase over the prior year. The increase came even though response rates are hovering at 0.3%, down from 1.2% ten years ago. (www.cardwatch.com).

So what conclusion should we draw from this? Should card marketers drop other channels and focus on the Web to generate new applications?

Or put the question another way: How should issuers choose the best combination of distribution and communication channels?

Not an easy question to answer: for example, a good deal will depend on what is meant by “best”. For most issuers, it’s likely to mean a combination of reach and cost per account – all in the context of what actually is available in the market in question.

Direct mail, for example, the classic tool of the marketer, depends entirely on lists that are up-to-date, open for mailing, and have known, or at least reasonably predictable, characteristics. Also, which is sometimes forgotten, it depends on a reliable mail service, not something we can assume exists in every market.

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And, of course, response rates are only the start of the process: the Internet may generate applications by the lorry-load, but Internet approval rates are another thing entirely.

Capital One, for instance, has mentioned approval rates as low as 22%, and many issuers struggle to do better than 45%. This suggests that credit-stressed consumers make up a high proportion of Internet-generated applications. This is further reinforced by the finding that renewal rates are lower for Internet-generated cards, especially from campaigns featuring low or zero rate balance transfers (BTs): it’s a commonplace these days that accounts acquired from BT offers attrite or move their balances immediately after “re-price” – the reversion to standard (sometimes called “Go To”) rates of interest.

So it’s no surprise that an advisory firm serving the US card industry has come up with the following metrics for card acquisition:

### US Acquisition Metrics

Source	Activity (%)	Renewal (%)	Cost per approved account (\$)	Approval (%)	Response (%)
DM	80-90	85-90	95-112	55-65	0.3-0.7
Telemarketing	60-70	65-70	60-70	55-65	3.0-6.0
Internet	55-60	60-65	10-45	35-55	0.6-2.1

Costs include marketing, bureau expense, credit processing, and card issuance

Source: RK Hammer

And this review, of course, ignores the richest channel of all: the bank’s own customers. Going back to Forrester again, the firm suggest that full service banks – they cite Bank of America as an example – generate as many as 77% of their card applications from among their own customers.

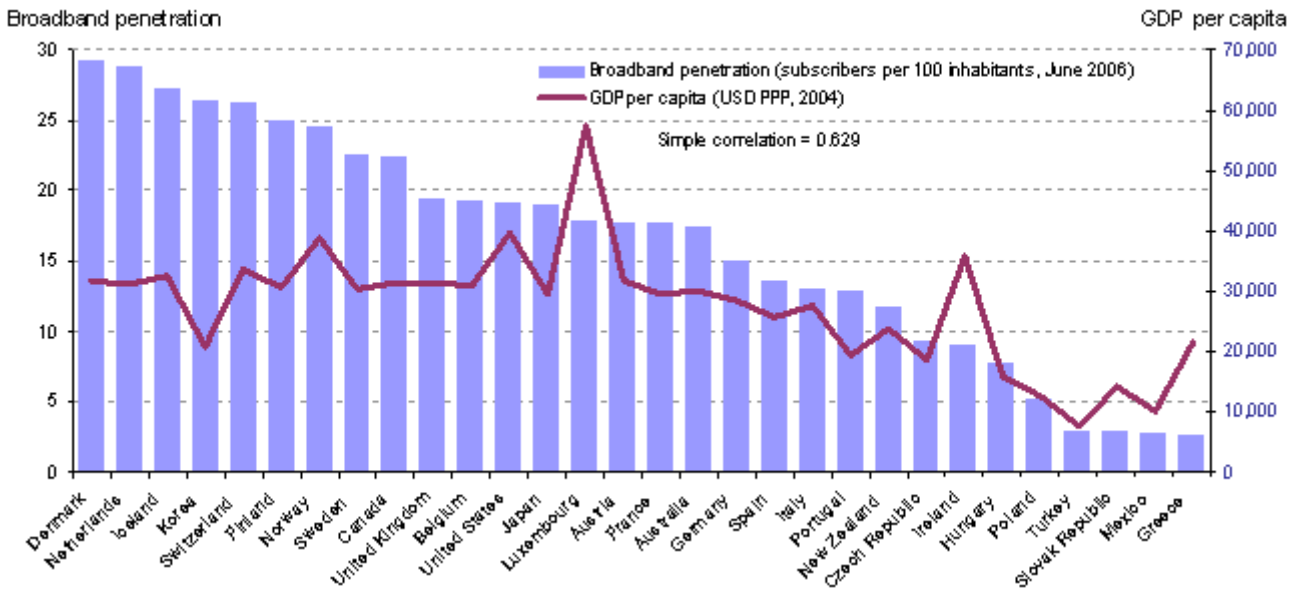
So what are the rules around channel mix?

**Rule 1: Run the numbers.** Many a new-to-the-business marketer has been shocked to find how many impressions or opportunities to view or click-throughs need to be generated to create only a modest number of approved applications. It’s a sobering fact that with a response rate of 1% and an approval rate of 60%, you’d need to mail 1 million pieces to generate 6,000 approved applications.

**Rule 2: Start with your own customers.** They know you – hopefully they trust you. And in your branch network, you have a potentially highly effective and relatively low-cost sales tool. But it’s only realistic to recognise that in many banks there’s a challenge to persuade Retail Banking bosses to give much “airtime” to your product: one UK bank expects its staff to sell, and presumably be knowledgeable about, over 140 consumer services of one sort or another. You’ll need to be very persuasive!

**Rule 3: Understand the limitations of the medium.** The needs of direct mail we've already talked about – but the Internet stands or falls on how many homes are connected. The numbers tell the story: about 70% of the population now has Internet access in North America, but the figure falls to 11% in Asia and less than 4% in Africa (The Economist, 10 March 2007). Broadband access doesn't go hand in hand with national income, either: penetration in Greece and Ireland, for example, is lower than would be expected in the light of their GDP per head:

**OECD broadband penetration and GDP per capita**



Source: [OECD](#)

**Rule 4: Whatever channels you are working with, adopt an integrated approach.** That way, your different communication programmes will work together, enhancing each other's impact, rather than operating in isolation.

**Rule 5: Test and learn.** Enough said: this simple motto should be written above every marketer's desk

**Rule 6: Have something to say.** Whatever the medium you're using, recognise that you're fighting to get your prospect's attention. This isn't the place to go into the details of how successful issuers maximise communication impact, but one common feature stands out. No matter how clever your creative, it stands or falls on the strength of the value proposition: if your offer isn't relevant, unique and attractive, the best channel mix in the world won't save your programme.



## What happened to all the good ideas? Maximising profit the right way

In a surprise move, Lloyds TSB in the UK will now charge £35 for little-used accounts where the balance is paid off in full each month.

Sandra Quinn, spokesman for national payments industry body APACS is very clear about what's happening: 'This - the introduction of annual fees - is a natural outcome to the work the Office of Fair Trading did last year on default charges,' she said.

'If you have lost one area of income, all credit card issuers will be looking at other ways to get income. They are not charitable organisations. The message is either use your card or cut it up.'  
(Daily Mail 21 February 2007).



There's no doubt about the message, Ms Quinn. But is it really the best the industry can do?

Because, make no mistake about it, if financial regulators in your market haven't decided to investigate payment card fees and charges, they soon will. And under those circumstances, it's entirely understandable that issuers will follow Ms. Quinn's advice, and start looking for other sources of income.

With this in mind, a recent review of the 2007 marketing project list in a leading European bank was a real eye-opener: without exception, every campaign was designed to extract more profit from card-holders. From straightforward decreases in days' grace, to more subtle changes in when transactions are credited or debited, each project aimed at building the bottom line.

But it's hardly an approach calculated to build customer confidence and trust. Surely there must be a better way?

Let's start with the basics: Yes, the industry will have to find new revenue streams to replace the ones that it's losing (and, by the way, that's not necessarily a bad thing: a little more transparency in charges is perhaps overdue). That could well mean charging a fee.

But older hands in the business will remember that we've been here before. Back in the 80s, in a bid to re-build profits, UK banks began to charge an annual fee for credit cards. It didn't last too long: first one issuer, then another, broke ranks by launching free cards, and pretty soon annual fees were a memory. Unless competition in your market is particularly weak, this is a likely outcome for any issuer who dares to charge fees without giving something valuable in return.

And that's the key: rather than simply looking at more-or-less nuanced ways of squeezing profits out of existing accounts, wiser issuers are considering how they can add value to their products – value which will make customers happy to pay a fee.

**“Wiser issuers are considering how they can add value to their products – value which will make customers happy to pay a fee.”**

Right now, super premium cards carry annual charges starting at around £250: many go much higher. Why? It's not just because the high net worth people who have them can afford them or enjoy the prestige they confer: it's because they value the top-end concierge services and other goodies that these cards offer. Why not apply the same principle further down the line?

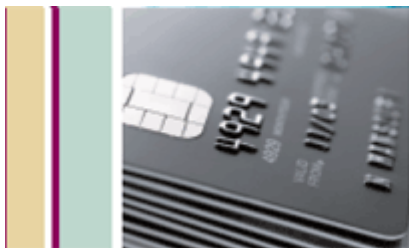
For every group of customers, there's a product or service they value which you can bolt on to your card and charge a fee for.

In essence, what all this is about is helping cards to break out of the commodity trap: so long as your card performs in exactly the same way as your competitor's, and delivers nothing more in the way of valued services than the competitors, so long will it be very difficult, and maybe even impossible, to charge a fee and make it stick.

But find a way to distinguish your card that excites your customers and makes sense to them, do it in a way that makes it tough to copy, and you have a real chance of driving sustainable new income to your bottom line.

So here's a prediction: sometime in the next twelve months, a major issuer will launch a mid-market acquisition programme offering added value for an annual fee.

Who's going to be first off the mark where you do business?



**And finally...**

**It's the way that you tell them**

Some US airlines have been busily cutting the length of time for which miles on their frequent flyer programmes are valid. Far from conceding that the change is a reduction in customer value, carrier spokespeople have been boldly asserting that in fact frequent flyers will benefit, as fewer of them will be trying to use their miles for seats...

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**Coping with the commoditised credit card:** Using relationships to build profitability

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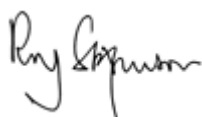
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**In the next issue of Enhance:**

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**How telecoms companies manage churn:** The lessons for card issuers

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