Navigator

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First Annapolis Consulting Relocates U.S. Headquarters

First Annapolis Consulting is pleased to announce the relocation of its U.S. headquarters to Three Park Place, Suite 200, Annapolis, Maryland. First Annapolis was founded in Annapolis in 1991 and the move marks an exciting homecoming for the company. Yes, First Annapolis is back in Annapolis.

We look forward to hosting you in our new office in a town we are proud to once again call "home." Consider this an open invitation to visit – we will talk payments and sneak in a visit to the Naval Academy, have a drink on the Bay, or enjoy some great Maryland seafood. We hope to see you soon.

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Q4 2013 U.S. Credit Card Issuer Performance Snapshot

By James Watts

Although growth continued to be a challenge for the nation's largest credit card issuers, the outlook for growth in 2014 looks marginally better than the past couple of years (quarter-over-quarter receivables increased by 4.3%, consistent with seasonal trends). Purchase volume increased by 7.5% on a year-over-year basis and 6% quarter-over-quarter; trends that are similar to the growth experienced in the fourth quarter of 2012. There are several trends worth noting:

1. **Receivables Growth Gains Some Traction:** Although single digit receivables growth both quarter-over-quarter and year-over-year is short of impressive, growth is positive and unlike the declines we have seen in previous quarters. Most industry experts are improving unemployment estimates and predicting an increase in consumer spending and modest growth in receivables in 2014 on the heels of a positive uptick in GDP.
2. **Charge-Offs Near 20 Year Lows:** Although the Federal Reserve has not released 4th quarter credit card charge off figures, it is reasonable to expect that the charge off rate in the 4th quarter of 2013, estimated at 3.02% industry-wide, will reach the lowest recorded point since 1995. Similar to 1995, 2013 marks the fourth year of economic expansion following a recession and unemployment rates are approaching 6% (moderately higher than 1995). Looking back to 1995, credit card charge off rates rose by nearly 100 basis points in a year span after a protracted decline and industry experts pointed to both slowing employment and aggressive credit card marketing to lower segments of the credit spectrum, a trend that started as early as the 1980s. While the potential easing of credit standards has been a hot topic as of late, the most recent Federal Reserve Senior Loan Officer Opinion Survey reports that demand for credit card and other non-auto consumer loans did not change significantly and that bank standards on credit cards and other loans remained unchanged for most respondents. Based on the elongated consumer and lender conservatism driven by the fact that the recent Great Recession had a much more significant impact on growth rates than the recession in the early 90's, it is reasonable to expect a much slower return to historical averages.
3. **Issuers Continue to Seek Growth:** Investments in new products and value propositions continued in the fourth quarter of 2013. For example, U.S. Bank and Wells Fargo announced third-party issuance deals with American Express. Additionally, Citi and American Express made several investments in rewards and digital offerings both domestically and abroad and Capital One launched a new General Motors product offering. Many issuers have already signaled that product, technology, and investment trends will likely continue in 2014.

For more information, please contact James Watts, Manager, specializing in Credit Card Issuing, james.watts@firstannapolis.com.

	Receivables			Purchase Volume			Net Loss Rate			After-Tax ROA		
Issuer	($B) 4Q13	Change (vs. 4Q12)	Change (vs. 3Q13)	($B) 4Q13	Change (vs. 4Q12)	Change (vs. 3Q13)	4Q13	Change (vs. 4Q12)	Change (vs. 3Q13)	4Q13	Change (vs. 4Q12)	Change (vs. 3Q13)
Chase[1]	$127.8	-0.2%	3.1%	$112.5	10.7%	5.1%	2.86%	-64 bps	0 bps	2.99%	63 bps	-57 bps
Citigroup[2]	$116.8	4.8%	4.5%	$66.7	7.6%	11.5%	3.79%	-70 bps	-15 bps	3.23%	46 bps	-37 bps
Bank of America[3]	$92.3	-2.6%	2.3%	$54.5	5.6%	3.2%	3.19%	-100 bps	-28 bps	3.67%	59 bps	30 bps
Capital One[4]	$73.3	-11.9%	4.7%	$50.4	3.0%	6.2%	3.89%	-46 bps	22 bps	2.59%	21 bps	-110 bps
American Express[5]	$58.4	4.3%	7.2%	$134.1	8.8%	7.6%	1.50%	-50 bps	-20 bps	4.49%	220 bps	33 bps
Discover[6]	$53.2	3.9%	5.5%	$29.5	2.8%	5.5%	2.09%	-22 bps	4 bps	3.45%	23 bps	-10 bps
Wells Fargo	$26.9	9.2%	5.7%	$14.4	13.8%	4.7%	3.38%	-33 bps	10 bps			
U.S. Bank[7]	$18.0	5.3%	5.6%	$27.9	2.8%	-3.1%	3.72%	-14 bps	-3 bps	4.69%	-73 bps	-65 bps
Sum/Wtd Avg[8]	$566.7	↑ 0.1%	↑ 4.3%	$490.0	↑ 7.5%	↑ 6.0%	3.02%	↓ -64 bps	↓ -8 bps	3.45%	↑ 65 bps	↓ -23 bps

Note:

[1] Includes income from acquiring business and private label receivables and volume.
[2] Purchase volume includes cash advances.
[3] Receivables, purchase volume, and net loss rates are for U.S. consumer cards.
[4] U.S. card business, small business, installment loans only. Purchase volume excludes cash advances.
[5] Receivables and charge-offs are for U.S. Cardmember Lending business only. Purchase volume is for U.S. Card Services segment, consumer and small business. Average earning assets is defined as all cardmember receivables (charge) and loans (revolving credit).
[6] Includes U.S. domestic receivables and purchase volumes only. ROA includes merchant services and implied U.S. Cards tax rate of ~40%.
[7] After Tax ROA reflects Payment Services line of business income and average loans.
[8] After Tax ROA excludes Wells Fargo as credit specific income not reported.

Q4 2013 Canadian Credit Card Issuer Snapshot

By Cara Weikel

In spite of continued concerns from the Bank of Canada and the Department of Finance regarding Canadian household debt burdens, a review of select Canadian credit card issuers' performance[1] in fiscal year 2013[2] reveals modest gains relative to the prior twelve-month period. Quarterly average credit card receivables were up year over year, and charge-offs improved across the board. Furthermore, Canadian credit card trust delinquencies (percent of balances 30+ days past due) continued to improve from 2.49% in Q4 2012

to 2.24% in the same period of 2013,[3] suggesting that loss rates may continue to decline in the coming months. Please see Figure 1 for portfolio metrics by issuer and Figure 2 for a summary of the aggregated delinquencies for Canadian credit card trusts.

Figure 1: Canadian Credit Card Performance Metrics for Select Issuers[1]

Issuing Bank	Quarterly Average Credit Card Receivables ($B) (Exceptions Noted)			Quarterly Average Credit Card Receivables Growth (%Y/Y) (Exceptions Noted)		Annualized Quarterly Net Charge-offs (% A/R)[4]		
	4Q11	4Q12	4Q13	4Q12	4Q13	4Q12	4Q13	ΔY/Y (vs. 4Q12)
TD	$8.1	$14.2[2]	$15.3[3]	75.9%[2]	7.4%[3]	N/R	N/R	N/R
CIBC	$15.5	$15.1	$14.7	(2.6%)	(2.5%)	4.1%	3.5%	(68 bps)
RBC	$12.8	$13.3	$13.8	3.9%	3.8%	3.0%	2.6%	(42 bps)
BMO	$8.0	$7.8	$7.9	(2.8%)	0.7%	N/R	N/R	N/R
BNS	$8.9	$8.9	$4.0[5]	0.0%	(55.1%)[5]	N/R	N/R	N/R
NBC	$1.9[6]	$1.9[6]	$1.9[6]	N/A[6]	1.6%[6]	N/R	N/R	N/R
CTFS	$4.1	$4.1	$4.4	1.4%	7.6%	6.9%	5.7%	(118 bps)
PCF	$1.9	$2.1	$2.3	5.8%	11.8%	4.4%	4.2%	(20 bps)
Sum/Wtd. Avg.	$61.2	$67.4[2]	$64.3[3,5]	10.1%[2]	(4.6%)[3,5]	4.0%	3.4%	(60 bps)
Adjusted Sum/Wtd. Avg.[7]	$61.2	$58.9	$61.3	(3.8%)	4.1%	4.0%	3.4%	(60 bps)

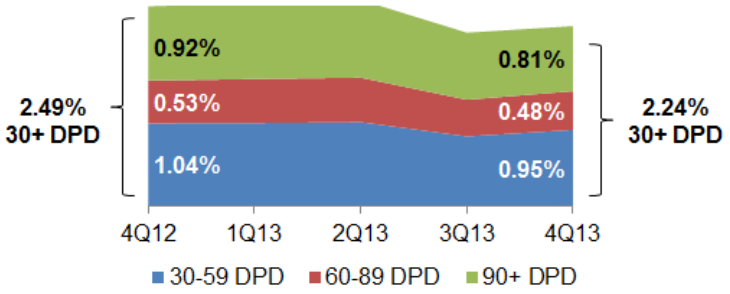
Note: [1] Data is exclusive to Canadian credit card portfolios; international receivables are excluded. Desjardins reported credit card receivables together with other consumer and personal loans, and was therefore excluded from analysis.
[2] Includes TD's December 2011 acquisition of MBNA Canada's credit card business.
[3] Includes TD's August 2013 acquisition of HSBC Retail Services Limited private label credit card portfolio.
[4] TD, BMO, BNS, and NBC net charge-offs for Canadian credit cards not reported.
[5] BNS reported a spot balance for Q4 2013, excluding ScotiaLine Visa receivables ($6B as of Q4 2012 and Q3 2013), rounded to the nearest $1B.
[6] Spot balances for Q4 2011, Q4 2012, and Q4 2013. Year-over-year receivables growth not available for 2012 due to rounding of the Q4 2011 reported balance.
[7] Excludes TD's acquisitions and adds back BNS' restatement to approximate organic receivables growth.

Source: Issuer financial reports and First Annapolis Consulting analysis.

Return to Receivables Growth

For the selected issuers in this index, the average credit card receivables for the fourth fiscal quarter of 2013 decreased by 4.6% relative to the same period in 2012. However, this statistic provides a distorted view of the issuers' organic growth, given TD Canada Trust's ("TD") acquisitions of MBNA Canada's credit card business (December 2011) and HSBC Retail Services Limited (August 2013), and Bank of Nova Scotia's ("BNS") re-categorization of its ScotiaLine Visa portfolio ($6B as of Q3 2013) from its credit card receivables to lines of credit beginning in Q2 2013. After adjusting for TD's acquisitions and BNS' restatement, the selected issuers reported 4.1% growth in quarterly average credit card balances as of the fourth fiscal quarter 2013 versus the previous year, compared to a 3.8% decline the prior fiscal year. President's Choice Financial ("PCF") added 11.8% to its receivables base, the largest gain within the sample set. The company attributed the increase to investment in the active customer base through account acquisition and marketing initiatives. Canadian Tire Financial Services ("CTFS") and TD, now the nation's largest issuer, also reported significant growth in quarterly average outstandings at 7.6% and 7.4%, respectively. CTFS credited its receivables growth to strategic efforts to increase acquisitions and average balances, including the introduction of instant credit in select stores and new offers in retail outlets, such as multiplier points, discounts, and in-store financing. While TD did not comment on its credit card growth, the company's August 2013 acquisition of HSBC Retail Services Limited's private label credit card portfolio accounted for approximately $0.5B, or nearly half, of the increased credit card balances. Among the issuers covered, only Canadian Imperial Bank of Commerce ("CIBC") posted a decline in credit card balances, dropping 2.5% from $15.1B a year ago to $14.7B in the fourth fiscal quarter of 2013. This decrease is aligned however, with the issuer's strategy of focusing on loan quality over balances, and the company indicated that it is satisfied with the resulting improvement in net interest margin. Looking forward to fiscal year 2014, TD will likely widen its leadership position, bolstered by having purchased $3.3 billion of Aeroplan Visa assets from CIBC in December 2013.

Figure 2: Aggregate Delinquencies of Canadian Credit Card Trusts (% of A/R)



Source: DBRS Monthly Canadian ABS Report and First Annapolis Consulting analysis.

Continued Loss Rate Improvement

Average annualized quarterly write-offs continued to improve in fiscal year 2013, falling from 4.0% of average credit card receivables in the fourth fiscal quarter of 2012 to 3.4% of receivables in the same period of 2013. These results are generally consistent with Canadian credit card trust data, which shows a 3.3% average annualized loss rate for the three months ended in October 2013, down from 3.9% a year earlier.[3] While charge-off rates declined for each issuer during the past year, 2013 loss rates for self-issuing retailer portfolios remain higher than the bank industry average by an average of 218 basis points, due to deeper underwriting, primarily store-based (non-targeted) acquisition channels, and mass-market products. CTFS, which had the highest loss rates in the sample set, also reported the largest improvement in write-offs, reducing its annualized charge-off rate by 118 bps from 6.92% in the fiscal quarter ended September 2012 to 5.74% for the same period in 2013.

[1] Except where noted, information and analysis reflects Canada-only credit card performance metrics, sourced from financial statements of Canada's largest credit card issuing banks and Canadian self-issuing retailers President's Choice Financial ("PCF") and Canadian Tire Financial Services ("CTFS").

[2] All performance metrics and commentary for PCF and CTFS reflect the companies' performance for the fiscal periods concurrent with the issuing banks' financial periods, (e.g., data from PCF's third fiscal quarter of 2013, which ended in September of 2013), will be referred to as the fourth fiscal quarter of 2013.

[3] Source: DBRS Monthly Canadian ABS Report and First Annapolis Consulting analysis.

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Large Financial Institutions Choose Mass Card Reissues in Wake of Target Breach

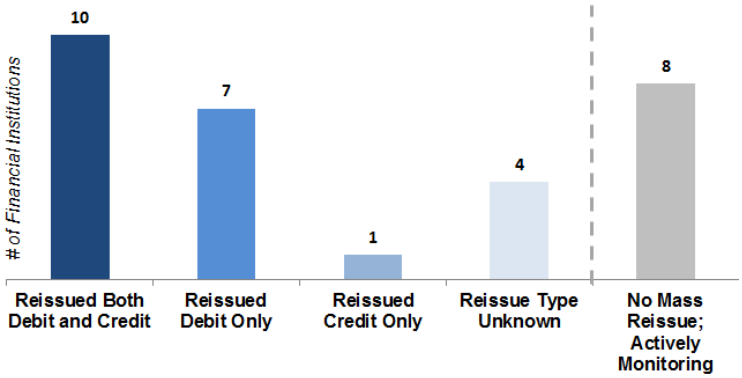
By Casey Merolla

In the wake of the Target data breach late last year that affected as many as 40 million credit and debit accounts and up to 110 million consumers, large U.S. financial institutions have been reissuing debit and credit cards in record numbers. Prior to December, the general trend in fraud prevention had been moving away from mass card reissues and instead emphasized targeted transaction monitoring and tracking. However, the high profile of the Target data breach and, in some cases, the rapid increase in fraud experience, has caused many financial institutions to make the proactive decision to reissue all (or a large portion of) affected cards.

First Annapolis conducted an informal review of top financial institutions and found that 22 of the top 30 issuers by number of debit cards are actively replacing cards. Many of these financial institutions are reissuing affected cards in both debit and credit portfolios, while others have chosen to reissue one product type and monitor others. The remaining eight financial institutions in the top 30 have taken the more traditional route of increasing fraud monitoring and tightening fraud parameters on those accounts and are replacing cards as fraud is identified or at the customer's request. The situation remains fluid however, as issuers continue to make the decision to proactively replace cards. In the last week of January alone, both Wells Fargo and U.S. Bank announced that they will be reissuing cards despite previous public announcements that they would focus instead on transaction monitoring.

Although most financial institutions have declined to release the number of cards being replaced, the Consumer Bankers Association (CBA) reported that its members have replaced over 17.2 million debit and credit cards since the breach was first identified in December. The CBA also estimated that its members' average replacement cost is roughly $10 per card, which includes card plastic costs, communication, shipping, activation, and call center support, for a total estimated replacement cost of nearly $172 million.

Figure 1: Responses to Target Breach Among the Top 30 Debit Issuers



Sources: Financial institution websites, news reports, and First Annapolis primary research.

Similarly, the Credit Union National Association (CUNA) has estimated that credit unions have replaced nearly 5.4 million debit and credit cards at a cost of over $30 million. Combined, these estimates indicate that over 55% of the 40 million cards compromised in the Target breach have been replaced at a cost to the issuing financial institutions of over $200 million. These estimates do not include any fraud losses associated with these accounts, so the actual costs incurred by financial institutions could be much higher.

The effects of this massive data breach and other recently announced breaches will continue to impact the payments industry, putting a laser point on the rising fraud trend in the United States. Undoubtedly, all potential fraud mitigation solutions will be back on the table for consideration during the coming year and beyond.

For more information, please contact Casey Merolla, Senior Manager, specializing in Debit and Prepaid, casey.merolla@firstannapolis.com.

T-Mobile Launches Innovative Prepaid Product

By Jeff Crawford

T-Mobile, one of the country's largest mobile network operators (MNOs), launched a new general purpose reloadable (GPR) prepaid debit card in January through partnerships with Blackhawk Network and Visa. The product is positioned to disrupt the market given its attractive price point and features as outlined in Figure 1. T-Mobile has over 15 million branded prepaid mobile service customers,[1] logical targets for the product, and is part of the mobile payment initiative Isis, thus it is important to examine its further entry into the payments market.

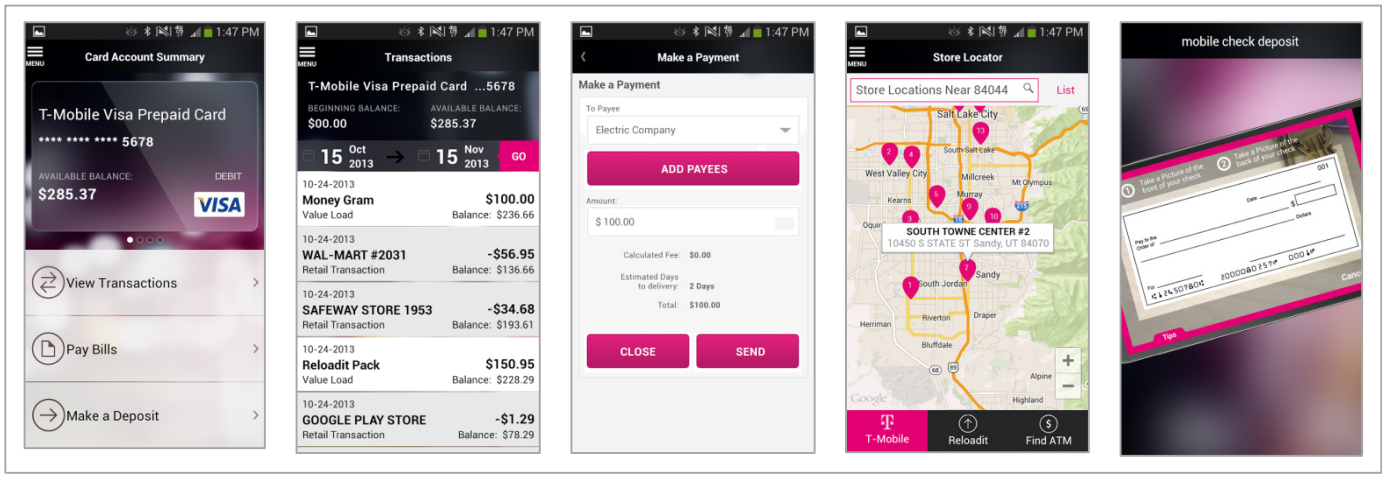
T-Mobile has gained significant attention since the launch of its "Uncarrier" campaign aimed at dramatically changing how it offers services and devices to its customers. In the course of the past ten months, T-Mobile has eliminated contracts, offered unlimited voice, talk, text, and data plans, extended

Figure 1: T-Mobile® Visa® Prepaid Card: Selected Fees

Fee Type	Standard	T-Mobile Customers who provide their T-Mobile wireless number at registration
Purchase / Maintenance Fees		
Retail Purchase Fee	• $4.00	• $0 • No charge at participating T-Mobile stores; if purchased elsewhere, the fee will be refunded to card account within 30 days
Monthly Maintenance Fee	• $5.00 per month • Waived for cardholders who load $500 or more on the Card during the preceding monthly billing cycle	• $0
Reload Fees		
Retail	• $3.00 - $3.95 (varies by retailer) • Fee is refunded for reloads of $300 or more	• $0 in T-Mobile stores • $3.00 - $3.95 elsewhere (varies by retailer). Fee is refunded for reloads of $300 or more
ATM Fees		
Domestic ATM Withdrawal Fee	• $0 at in-network ATMs nationwide • $2.00 at out of network ATMs	

Source: https://t-mobilemoneyservices.com/Need-Help/Fees.

Figure 2: Mobile Money App by T-Mobile



Source: Google Play, Mobile Money By T-Mobile.

international data plans, and made upgrading phones and switching carriers easier for customers by offering direct subsidies. These moves have been very successful to date, creating a net gain of 4.4 million subscribers in 2013.[1]

Coming on the heels of these announcements, the launch of its prepaid card and accompanying money management app, Mobile Money, T-Mobile is continuing to shake up the market while creating significant benefits for its customers. More specifically, T-Mobile has structured its pricing and product features in a very customer-friendly manner. T-Mobile wireless customers have the ability to purchase and use the card at no cost (see Figure 1). Pricing for non-T-Mobile customers is comparable to other leading GPR card products.

In addition to the physical card, T-Mobile is offering a feature-rich mobile app, Mobile Money. The company is positioning the app as a way for customers to manage their money with features including balance view, transaction history, check deposit, bill pay, and account to account transfers, while also enabling phone service payments, creating a potentially sticky feature for T-Mobile wireless customers.

The implications for the prepaid card market are two-fold. One, this announcement, along with the release of competing offerings from Sprint and the Boost Mobile (Boost Mobile Wallet is a plastic prepaid card and money management app), provides further evidence that the GPR market is becoming even more competitive as new entrants offer innovative products. Two, it may signal a shift in GPR pricing models for some large players. Instead of relying on customer fees, competitors such as T-Mobile may use GPR as a means to deepen existing customer relationships for their core businesses (i.e., wireless phone service). Such a development could place further pricing pressure on more traditional GPR products.

[1] *T-Mobile Press Release "T-Mobile U.S. Reports Preliminary Fourth Quarter 2013 Customer Results" January 8, 2014.*

For more information, please contact Jeff Crawford, Manager, specializing in Debit and Prepaid, jeff.crawford@firstannapolis.com.

Acquiring Time Machine: Revisiting Price Elasticity in Merchant Acquiring

By Chris Sanson

Ten years ago, we published a short piece in our newsletter describing the price sensitivity of small merchants (April 2003, "Price Elasticity in Acquiring" by David Woynerowski). Much has changed in the acquiring industry in the past ten years, and we were interested to see whether the price sensitivity of small merchants appears to have shifted in a material way. Using our merchant-level database, we ran a regression analysis in 2003 relating ranges of merchant pricing to attrition for merchants with < $30,000 in annual V/MC volume. Our analysis at that time suggested that the price-independent attrition rate for merchants of this size was 23%, and that attrition increased at a rate of 1.6 basis points (0.016%) for every 1 basis point increase in pricing. We reproduced the 2003 analysis in late 2013 using our current merchant-level database, increasing the merchant size threshold to $37,000 to adjust for inflation.

There are several key observations about the relationship between 2003 and today. First, the price-independent attrition rate (e.g. the y-intercept in Figure 1 or the constant in the equations in Figure 1) has not changed very much over this time span, remaining just above 20%. The price-independent attrition rate is essentially the attrition rate even if the merchant was priced at interchange – in essence, it is the minimum attrition from all sources other than pricing-level. Of course, business failure will be a significant source of attrition, though both 2003 and 2013 fall in similar stages of the business cycle, the couple of years following a recession.

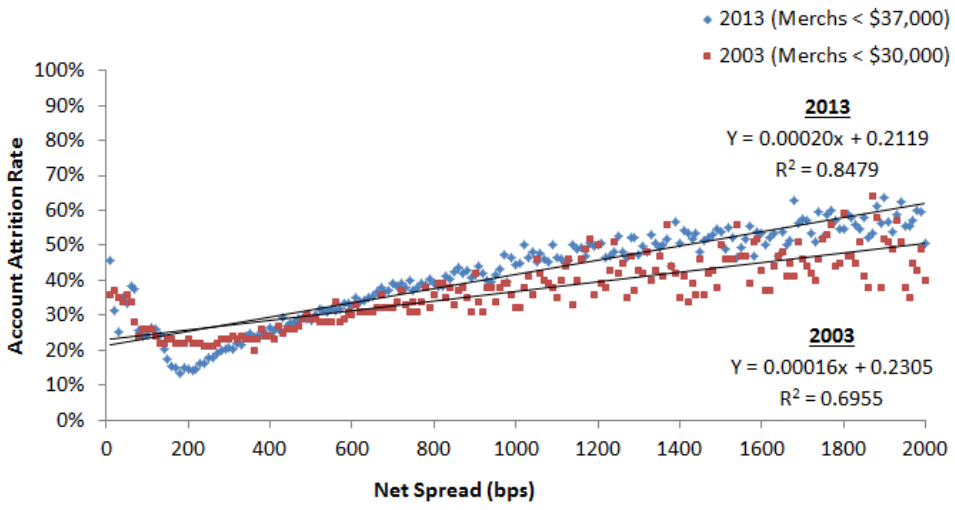
Second, merchants appear to have become more price sensitive over this time period. Whereas in 2003 a 1bp increase in pricing suggested a 1.6bp increase in attrition, that rate has grown to 2bps today. Furthermore, we are seeing a tighter spread in the data points (e.g. a higher R^2, which is a measure of the strength of the relationships in the regression analysis).

What do these relationships reflect? One hypothesis is that Square and similar mobile players have triggered greater price sensitivity for such small

merchants. We have also observed an increase in the prevalence of interchange-plus pricing, even in the small merchant space, which is also associated with a higher level of price sensitivity among merchants. Or probably most likely, the increasing price sensitivity reflects the general intensification in competition across the industry.

For more information, please contact Chris Sanson, Associate, specializing in Merchant Acquiring, chris.sanson@firstannapolis.com.

Figure 1: Price Elasticity in Merchant Acquring



Source: First Annapolis Consulting merchant-level database.

Update on Card Product Development Trends in Europe

By Maria Popova

While European countries vary substantially in terms of the level of market development, structure, and consumer demand, we have observed three key themes in recent card product development trends across Europe. Issuers are expanding their product offerings to the affluent segment, striving to enhance customer value propositions (although this will be complicated by forthcoming interchange regulation), and giving customers greater control over their finances. We examined each of these themes by reviewing the product offerings of representative European card issuers (see Figure 1).

Theme 1: Expansion in the affluent segment

Following the financial turmoil across Europe, resulting in increased capital requirements and more stringent underwriting regulations, issuers have launched new products targeted at affluent customers in order to reduce the credit risk in their portfolios. Typical attributes include 1% - 2% cash back on purchases (points programs are less prevalent, with the exception of co-brands), and annual fee waivers based on spend. For super-premium cardholders, concierge services, merchant discounts, and extra travel insurance are fairly standard.

Theme 2: Enhanced customer value propositions

As European credit cardholders have become more sophisticated and demanding of card products, issuers have responded with new products that promote simplicity, immediacy, personalization, and extra soft benefits. Many issuers have shifted rewards programs from points to cash back in order to simplify and better convey the value of the card to customers, however forthcoming decreases in interchange will likely cause many issuers to revisit their rewards strategies. Issuers are also examining card-linked merchant offers to reduce rewards costs while providing higher "headline" rewards, and simplifying their overall product sets to allow for straight-forward sales messaging. We have also observed examples of efforts to increase personalization (e.g., choose your own card image) and efforts to target merchant offers to specific segments.

Theme 3: Enabling more control over finances

In the face of economic uncertainty, customers are displaying more careful borrowing behavior, and issuers are responding with products that offer greater flexibility and control over personal finances via mechanisms such as installment payments, increased marketing of automatic repayment options (although this negatively impacts revolving rates) and combining debit and credit features in one product. We have not observed more complex budgeting and repayment features such as those exhibited by Chase's Blueprint platform in the U.S., likely due to systems limitations.

Considerations for Issuers

As we noted in the September 2013 edition of the Navigator, interchange reductions will necessitate significant changes to European issuers' product and marketing strategies via product set rationalization, reducing rewards costs, introducing merchant-funded rewards, commercializing data, and migrating small business users to commercial cards. Within this context, we have identified two general considerations for issuers based on our market scan:

1. **Fit the product set to the strategy.** Aligning the product set with the sales strategy is critical to driving sales and a positive initial customer experience. For example, issuers focused on selling through branches typically benefit from promoting fewer, clearly differentiated products. On the other hand, issuers that leverage direct channels can use a broader product set with more nuanced variations to target different segments.

2. **Fit the product set to the target customer base.** Segmenting the customer base by needs, preferences, and lifestyles can enable targeting the right customer with the right product. Additionally, incorporating meaningful product features (e.g., unique rewards, budgeting tools, customization, etc.) differentiates the offering from the competition and helps sales uptake. However, the level of product segmentation and breadth of product features can vary widely depending on the issuer's scale and strategy – for many issuers, a product set consisting of an entry-level/basic product, a mass market product, and a premium/affluent product is sufficient.

Figure 1: Example European Card Products

Theme	Country	Issuer	Product	Type	Description
Expansion in the Affluent Segment	UK	Capital One	Aspire Elite	Credit	• Aimed at high earners, • Cash back, concierge, insurance
	Czech Republic	ČESKÁ SPOŘITELNA	Visa Infinite	Credit	• Part of private banking offering • Concierge, discounts, insurance
	Russia	Russian Standard Bank	Imperia Platinum	Credit	• Part of private banking offering • Annual fee waivers, cash back
Enhanced Value Propositions	UK	Santander	123 Card	Credit	• Tiered cash back
	Czech Republic	Raiffeisen BANK	De Luxe / Style / Easy	Credit	• Simplified product set with three offerings
	Turkey	Garanti	Flexi Card	Credit	• Optional personalized design and merchant offers
	Poland	Millennium	Visa Impresja	Credit	• Cards targeted at women • Gifts and discounts • Purse insurance
	Czech Republic	KB	Lady Karta	Credit	
	Portugal	barclaycard	CEPSA	Credit	• Fuel co-brand card • Discounts on petrol
	UK	Lloyds Bank	Everyday Offers	Credit / Debit	• Targeted cash back for debit and credit cardholders
More Control	France	Crédit Mutuel	Carte 3 F	Credit	• Payment in installments for purchases above threshold
	Poland	citi handlowy	"Comfort"	Credit	• Post-purchase installment loan
	France	BNP PARIBAS	Esprit Libre	Credit / Debit	• Product package • Checking account, debit, credit card, insurance
	France	Societe Generale	Visa Simply One	Combo	• Debit / credit combination cards • Selection debit or credit function at POS • Debit by default
	France	Crédit Agricole	Double Action	Combo	
	France	Crédit du Nord	Carte Debit - Credit	Combo	

Source: Card product websites.

Although the ultimate success of a product set and individual products will vary depending on the market, customer characteristics, and execution, we encourage European issuers to consider the product trends described above along with the importance of fit when considering responses to interchange reductions.

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P-Card Acceptance Update (Part 2)

By Frank Martien

In the November / December 2013 Navigator, we explored p-card acceptance rates for several global geographic regions and, specific to the U.S., by organization spend vertical based on a 2013 First Annapolis Consulting / NAPCP (www.napcp.org) purchasing card acceptance survey (n=103). In this article, we explore key reasons for supplier card acceptance as well as supplier resistance.

Suppliers have many reasons to take cards. In the 2013 survey, 62% of respondents reported that their suppliers took their P-Card / One Card to achieve quick payment (i.e., improve working capital); while, for 48% of respondents, guaranteed payment was the second most cited benefit. One can see in Figure 1 that process ease for the supplier was cited by less than 40% - in part because many suppliers still handle card acceptance in a somewhat manual, "exception process" manner.

Specific to ePayables (i.e., non-plastic virtual accounts riding p-card rails), the top three reasons cited were quick payment, guaranteed payment, and to be "preferred." Counter intuitively, process ease ranked fourth. While ePayables solutions are often specifically designed to automate AP and AR payments, the AR component, like P-Cards / One Cards, is regrettably often handled as an exception process by the supplier. A key opportunity for the industry is to better educate suppliers on how ePayables can improve so-called auto cash. Potential also exists as an industry to harmonize ePayables and electronic invoicing solutions in areas such as interfaces and file formats to ease supplier adoption.

This survey also explored reasons suppliers resist or won't take cards for payment. "Fees too high," at 67%, was by far the most common impediment depicted in Figure 2 with only a slight decrease from 71% in 2009 despite substantial provider / industry progress made regarding lower large ticket

interchange rates during the past four years. "Too hard to set up" was still the second most frequently observed reason by one-fourth of respondents followed by "don't understand the benefits."

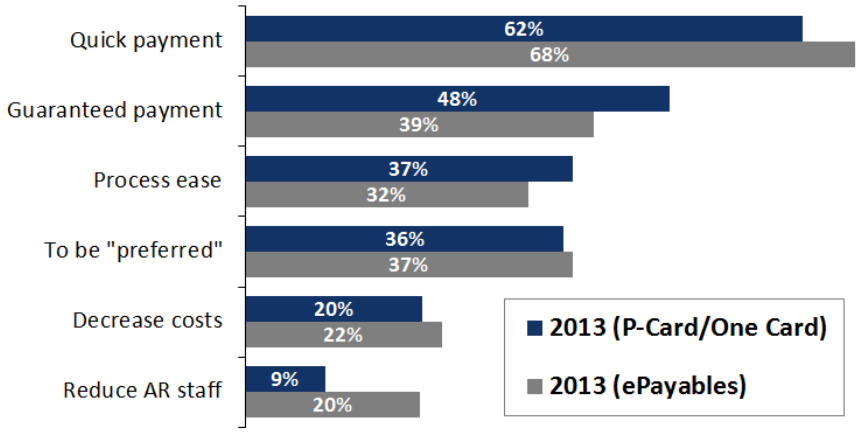
The 2009 and 2013 surveys also measured the transaction size at which supplier resistance / refusal is most commonly encountered. Back in 2009, the vast majority of respondents stated they did not encounter supplier resistance / refusal based on transaction size, likely due to the fact that nearly half prohibited use of a P-Card / One Card for transactions larger than $2,500. In 2013, 83% of respondents allowed P-Card / One Card usage for transactions larger than $2,500, which likely resulted in the higher frequency of supplier resistance / refusal responses for larger ticket amounts shown below. While 58% of respondents are still NOT encountering supplier resistance / refusal based on transaction size, for those that do encounter this, this threshold often starts at $10,000 or $15,000.

Results from this survey suggest substantial opportunities still exist to:

- Educate suppliers on actual (versus perceived or legacy) transaction fees, including large-ticket interchange rates offered by card networks;
- Assist or provide support as practical for set up; and,
- Explain or re-explain the benefits of accepting cards.

For more information, please contact Frank Martien, Partner, specializing in Commercial Payments, frank.martien@firstannapolis.com.

Figure 1: Reasons Suppliers Take Cards, According to End-Users



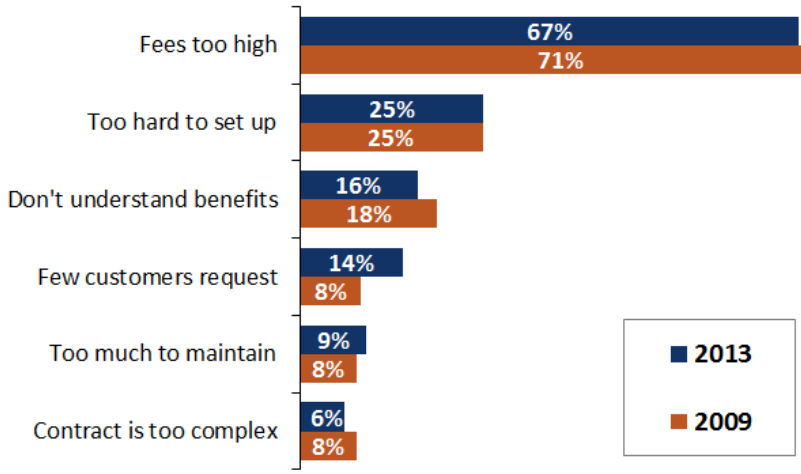
Note: results between 2009 (P-Card/One Card) and 2013 (P-Card/One Card) were relatively comparable.

Q: What reasons do suppliers give for accepting your P-Cards/One Cards? Indicate the frequency for which suppliers cite each of the following.

Q: What reasons do suppliers give for accepting your ePayables payments? Indicate the frequency for which suppliers cite each of the following.

Source: NAPCP supplier acceptance survey of 2013 (n=103).

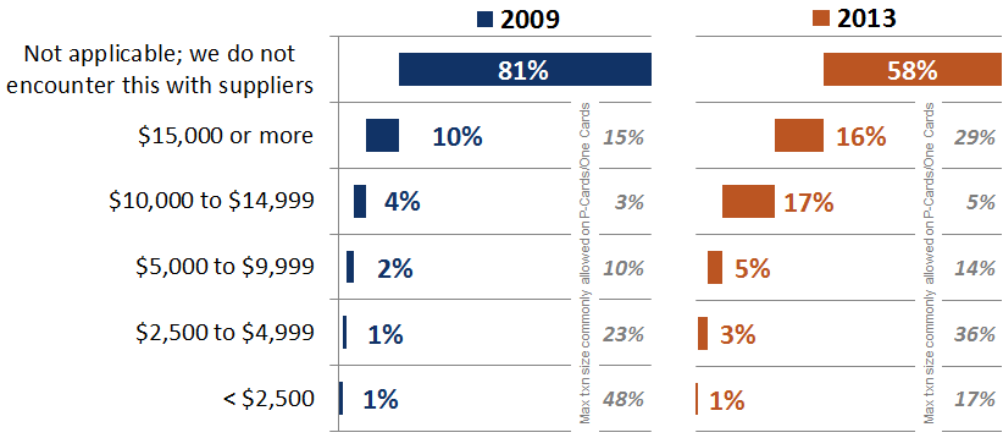
Figure 2: Reasons Suppliers Resist / Won't Take Cards



Q: What reasons do suppliers give for resisting or not accepting your P-Cards/One Cards?

Source: NAPCP supplier acceptance surveys of 2013 (n=103) and 2009 (n=146).

Figure 3: Transaction Size at Which Suppliers Most Commonly Resist / Refuse Cards



Q: Which of the following dollar ranges best reflects the point at which your card accepting suppliers most commonly resist or refuse to accept a card payment (due to cost or other factor)?

Q: Which of the following dollar ranges best reflects the highest transaction amount your org commonly allows on a P-Card/One Card? "Commonly allowed" could be demonstrated through a cardholder's usual single transaction limit or your org's willingness to grant a temporary limit increase.

Source: NAPCP supplier acceptance surveys of 2013 (n=103) and 2009 (n=146).

Blackhawk Network On the Move

By Aaron Mercurio

In the prepaid business, distribution has long been king. Blackhawk Network, the prepaid distribution provider and technology platform best known for its strong presence in retailer-based gift card malls, has created a lot of buzz in recent months. Since its IPO in April 2013, Blackhawk has executed a series of strategic moves designed to expand both its product suite and distribution channels with a strong focus on the digital arena:

- A strategic alliance with e-commerce and m-commerce giant PayPal
- The acquisition of prepaid B2B and incentives solution provider InteliSpend
- Piloting a prepaid program for open-loop GPR cards with partner T-Mobile
- A partnership with Coinstar for digital gift card fulfillment

Strategically, it appears that the company will look to drive gift card partners into the digital and mobile spaces in both the direct-to consumer and business-to-business channels. While First Annapolis believes plastic cards will continue to retain a strong appeal in gifting, the prepaid industry is evolving as the legacy product makes headway into several familiar payments arenas:

- Banking Alternatives such as open-loop GPR and Payroll
- Loyalty platforms such as the Starbucks Card (or should we say, Starbucks app)
- Incentive and B2B solutions
- New closed-loop card use cases (group-gifting, event registry, budgeting, RAN cards)
- And, mobile payments

We offer a quick perspective on Blackhawk's recent moves:

PayPal

Through an alliance with PayPal, Blackhawk provides its card partners with an entry point into the PayPal mobile wallet app. It is expected that consumers will be able to purchase and give gift cards via the mobile device or e-commerce engine, and also input and store gift cards within the wallet for use. For PayPal, the solution is yet another step in the direction of full mobile wallet, as the firm's recent partnership with Alliance Data suggests a similar application for retailer-branded private-label credit cards.

The partnership is a clear bet on gift cards in the mobile environment, both as a digital acquisition point as well as the form factor for transacting. With 137 million total accounts worldwide and a digitally-inclined customer base, PayPal is a logical partner. Blackhawk will also work with PayPal to enable its distribution partners to be able to sell PayPal open-loop prepaid products and enable PayPal loads using Blackhawk's ReloadIt prepaid reload network.

InteliSpend

Through InteliSpend, Blackhawk enhances its B2B offering in a meaningful way. The B2B business is complex, where incentive houses, scrip companies, loyalty providers, financial institutions and a variety of specialists compete for corporate sales. Gift cards have become an important redemption option for the incentives business, with an emphasis on open-loop gift cards which have wide consumer appeal. Serving the B2B market requires significant sales coverage and unique fulfillment capabilities, both of which InteliSpend bring to the table. The combination of the two entities could potentially bring Blackhawk's 100+ card partner relationships, for both plastic and digital or e-gift cards, and the firm's proprietary open-loop prepaid products to InteliSpend's 1,000+ corporate relationships.

T-Mobile Prepaid GPR

Wireless carriers such as T-Mobile are sought-after channels for financial services providers because of their massive reach (T-Mobile has 45 million wireless subscribers and 70,000 direct and indirect distribution points), sticky customer relationships (churn in the cell-phone industry varies by provider but is typically <5-10% annually), and obvious fit with mobile technology. By winning the program management business for T-Mobile, Blackhawk throws its hat into the ring with the likes of Green Dot, Netspend (TSYS), Xerox, and several financial institutions and others for end-to-end third-party prepaid providers.

Consumer adoption will ultimately be a function of the product's value proposition, pricing, load capabilities, T-Mobile's channel integration, and Blackhawk's ability to execute, but if the program reaches national roll-out, even capturing a fraction of 1% of T-Mobile's 45 million subscriber base will drive meaningful scale and card volume to the partnership. We should note that the initial pilot program will likely occur in a small subset of T-Mobile channels with the opportunity for expansion if successful.

Coinstar

In Coinstar, Blackhawk finds a strong and unique distribution partner, allowing consumers to exchange coins for retail gift cards at Coinstar machines. Coinstar, which processes over $3B worth of coins annually, estimates that 90% of American households live within 5 miles of a Coinstar machine. While exchanging coins for gift cards at a Coinstar machine isn't new, First Annapolis expects that the Blackhawk-Coinstar partnership will drive digital gift card sales for Blackhawk for reasons including: (1) customers will prefer a digital gift card for self-use because of the immediacy of retail gift cards that can be delivered electronically and (2) the underlying economics and operational benefits surrounding the digital gift card transaction can expand the number of card options available and offset real costs to consumers (for consumers to get cash from Coinstar, they pay a % transaction fee).

Sources: Blackhawk Investor Relations, Quarterly Earnings Presentations, Company Websites, Company Press Releases, Google Finance, First Annapolis Consulting Analysis.

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Federal Reserve Releases Tri-Annual Payments Study

By Collin Bauer

The Federal Reserve released its tri-annual study of noncash payments in December 2013. The study reinforces the steady growth of electronic-based transactions and the increasing popularity of non-credit products in the U.S. market as cash and checks are displaced. The product that experienced the largest percentage growth in transactions over the last three years was general-purpose prepaid, averaging ~33% growth from 2009-2012. Over the same period the number of credit transactions rebounded after experiencing a decline from 2006-2009. Debit payments remained strong, experiencing an increase over the last three years of almost 10 billion transactions, accounting for nearly two-thirds of all non-cash payment growth over the same period. While the credit card market is relatively mature, we expect electronic payments to experience elevated growth as cash and check usage continues to erode.

For more information, please contact Collin Bauer, Senior Analyst, specializing in Credit Card Issuing, collin.bauer@firstannapolis.com.

Figure 1: Number and Growth of Noncash Transactions

	2003	2006	2009	2012	CAGR 2003 – 2012	CAGR 2009 – 2012
Total Transactions (B)	81.4	95.2	108.1	122.8	4.7%	4.4%
Credit	19.0	21.7	21.0	26.2	3.6%	7.7%
General Purpose	15.2	19.0	19.5	23.8	5.1%	6.8%
Private Label	3.8	2.7	1.5	2.4	-4.8%	17.1%
Debit	15.6	25.0	37.5	47.0	13.0%	7.7%
Prepaid	0.8	3.3	5.9	9.2	31.2%	16.0%
General Purpose[1]	0.0	0.3	1.3	3.1	N/A	33.5%
Private Label	0.8	3.0	4.6	6.1	24.9%	9.7%
ACH	8.8	14.6	19.1	22.1	10.9%	5.1%
Checks (paid)	37.3	30.5	24.5	18.3	-7.6%	-9.2%

[1] The number of general purpose prepaid card transactions in 2003 was negligible.

Note: Chart reorganized and recreated by First Annapolis Consulting.

Source: 2013 Federal Reserve Payments Study.

Payments Industry Stock Price Tracker

By Collin Bauer

Figure 1 is the Payments Industry Stock Price Tracker for January 2014. The table measures stock prices and market capitalization, as well as movement over the last month, and year-to-date (from January 2013). Along with the broader market, the sectors that First Annapolis monitors across the payments value chain experienced declines in January, but each sector is exceeding the broader market's 26% increase since the start of 2013.

In summary:

In January, the issuing sector posted a decline of 3% in aggregate and matched the overall market. Downward pressure on the issuing sector in January was largely driven by quarterly earnings releases. All of the issuers tracked posted a decline in January except for Bank of America, which beat analyst earnings estimates and gained 8% last month. Issuers, as a whole, have experienced gains of 33% since the beginning of 2013.

The processor / acquirer sector posted declines in January, with an overall decrease of 6%. Global Payments was the lone processor / acquirer to experience a gain last month (2%) and did so after exceeding earnings expectations for the quarter and announcing plans to acquire Payments Processing Inc. All companies tracked within this sector have experienced gains of between 40% and 50% since the start of 2013.

In aggregate, MasterCard and Visa declined 6% in January, but have overall gains of 48% over the last 13 months.

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Figure 1: Monthly Stock Price Tracker

Companies	Jan. 31, 2014	Month Δ	YTD Δ	Current Market Cap ($Billions)
Issuers				
American Express	$85.02	-6%	49%	$88.70
Bank of America	$16.75	8%	44%	$177.10
Capital One	$70.61	-8%	23%	$39.48
JPMorgan Chase	$55.36	-5%	28%	$205.15
Citi	$47.43	-9%	20%	$140.67
Discover	$53.65	-4%	40%	$24.89
FleetCor	$106.32	-9%	98%	$8.58
U.S. Bank	$39.73	-2%	25%	$71.08
WEX	$82.36	-17%	9%	$3.10
Weighted Average	-	-3%	33%	-
Acquirers / Processors				
FIS	$50.70	-6%	46%	$14.31
Fiserv	$56.05	-5%	42%	$14.09
Global Payments	$66.09	2%	46%	$4.56
Heartland	$43.11	-14%	47%	$1.57
TSYS	$29.88	-10%	40%	$5.41
Vantiv	$30.34	-7%	49%	$4.21
Weighted Average	-	-6%	44%	-
Networks				
MasterCard	$75.68	-9%	55%	$90.74
Visa	$215.43	-3%	43%	$135.97
Weighted Average	-	-6%	48%	-
Market Index				
S&P 500	$1,792.59	-3%	26%	-

Note: Weighted Averages are based on current market caps.
Source: Yahoo Finance, First Annapolis Consulting research and analysis.