THE CREDIT UNION
JOURNAL

www.cujournal.com THE NATION'S LEADING INDEPENDENT CREDIT UNION NEWSWEEKLY August 1, 2005

The Great Credit Card Debate: Should My CU Buy In Or Sell Out?

By Timothy Kolk

Quite a lot has been written lately about credit unions selling their credit card portfolios. Reactions range from "never in a million years" to "makes perfect sense to me."

The intensity of the different viewpoints about this became apparent to me recently when I participated in a debate hosted by Metropolitan Area Credit Union Management Association (MACUMA).

The topic was: "Should Credit Unions Sell Their Credit Card Portfolios?" While cordial, the debate demonstrated that there were clear differences in opinion rooted in a wide variety of strategic, philosophical and financial considerations.

The most surprising thing I learned, however, had little to do with credit unions selling their credit card portfolios.

The critical thing I learned is that most credit unions do not fully understand how best to proceed with an evaluation of this option. There are many potholes that can prevent a thorough and objective evaluation.

Unfortunately, an inaccurate or biased analysis can be worse that no analysis at all. To help remedy that I have summarized the things a credit union should consider when evaluating a credit card portfolio sale.

The Tough Questions

So, what do credit unions need to understand when beginning this evaluation? The following questions are ones we believe every credit union should consider.

1) What do we compare when trying to evaluate our options?

Most credit unions start from the position of gathering information but having no bias in favor of a card portfolio sale.

Credit unions in this position need to initiate a process that is both comprehensive and objective. They certainly need to look at the purchase and agent offers available to them.

They then need to look at the impact of selling the portfolio compared to both current profitability and what the credit card business could become if internal improvements were initiated.

Most credit card processing organizations as well as various consulting firms can help you assess your card program's potential benchmarking sale options against current performance is not sufficient; benchmarking against what is possible internally should be required.

2) How do we get live offers on our portfolio for this comparison?

There are a couple different ways to do this. The first is to call various credit card issuers directly and forward the portfolio and credit union information each requires.

The second is to engage an advisor to manage the process for you and create a comparative analysis of your offers. Each has its advantages and disadvantages.

Keep in mind, understanding available offers is much more complicated than putting offer letters on a table and circling the premium rates.

A Thorough Assessment

A thorough assessment must include comparisons of products, marketing plans, rates and fees, service levels, various critical contract terms, noncompete commitments, and a myriad of other post-sale considerations. Most credit unions have been highly satisfied with the results of their portfolio sale, but in our experience those that are least satisfied are the ones that took the largest number on a piece of paper and assumed all the rest would work out just fine. This decision requires a higher level of due diligence.

Doing it all yourself requires a substantial commitment of time and energy but can be a better fit for some credit unions. If you have enough expertise in the card industry and the time and resources available from internal staff you should consider this approach.

On the flip side, a qualified advisor can pay dividends well in excess of the cost.

An advisor can not only do most of the work but should also create a truly objective situation where all offers are compared fairly.

One of the more difficult tasks in this process is comparing not only the financial offers (and they often differ in hard-to-see but critical ways) but also all the other elements of an agent program initiated after sale.

Recognize that there is an asymmetry of knowledge in this negotiation: a credit union will only sell a credit card portfolio once but the buyers have done it many times.

In the words of Donald Rumsfeld, sometimes "we don't know what we don't know." The reasons we find it necessary to engage professionals such as attorneys, accountants or doctors are much the same.

3) If we use an advisor, what do we need to know?

This is perhaps the most critical question. If you choose to engage an advisor, you need to ensure that they are able to be objective.

They also should have a long track record with many potential buyers to ensure all available offers are found (and ask for examples). This requires each potential advisor to answer two questions:

First: is selling your portfolio the only service they can offer? If an advisor cannot help you grow your portfolio internally then it will be difficult for that advisor to do anything other than advocate a portfolio sale.

We see many credit unions that would be better served by putting together an internal improvement plan than by selling their portfolio, if only they knew how. Ask any advisor for specific examples of credit unions that they have helped to do this. Then check references.

Second: is the advisor aligned with any particular issuer or are they a neutral party? Some firms in this industry are actually sales forces for specific portfolio buyers.

By design that makes them advocates of only one outcome: "sell now and sell to my partner." A CU needs to understand the motivations of the advisor it is working with, and must then decide if it is comfortable with those motivations.

Advisors tied to a specific buyer benefit if they can prevent an objective and neutral expert from sitting next to the credit union during the analysis and negotiation process.

That, after all, may only increase the level of competition they face. Any credit union in this situation needs to retain control of the process and follow an approach that ensures the most open, comprehensive and unbiased environment possible is maintained from start to finish.

Hopefully this overview has provided a deeper understanding of what needs to be considered in a credit card portfolio sale analysis. No credible advisor can enter a dialogue with the assumption that you should sell your credit card portfolio. To reach that conclusion requires an in-depth comparison of purchase offers to a realistic analysis of portfolio growth potential if retained.

If a sale of the portfolio appears to make sense after this step, each credit union has to make sure that it puts itself into a position to control that process and create the most competitive possible negotiating position.

To do that, engaging an advisor unaffiliated with any particular credit card issuer may or may not make sense. Either way, you must carefully design a process that ensures the analysis is comprehensive, objective and exhaustive.

This is the only way to reach a decision that you can be confident serves the needs of your board of directors, your members and the credit union as a whole.

Timothy Kolk is Managing Partner of Brookwood Capital. He can be reached at 603-924-7215 or tkolk@brookwoodcapital.net.