

CHAPTER 9

THE FUTURE OF CONSUMER LENDING

LEARNER OBJECTIVES

Upon completion of this chapter, you will be able to:

- identify the advantages credit unions enjoy over other consumer lenders in the minds of the American public;
- place current trends in consumer lending into a historical perspective;
- describe the potential offered by electronic lending systems, and their importance to the future of credit unions;
- understand the importance of reaching out to future generations of borrowers with products and services designed for their specific needs.

Too often we underestimate the power of a touch, a smile, a kind word, a listening ear, an honest compliment, or the smallest act of caring, all of which have the potential to turn a life around.

Leo Buscalia

In order to succeed rather than merely survive in managing the credit union lending business, you need to have a passion for lending. You need to love making loans. The quality unique to credit union lending managers is their passion for responsible *lending*. The credit union is concerned not just with the welfare of the organization but also with the welfare of the members who make up that organization.

We tend to forget that on most financial legislative action, credit unions and banks take a similar position. Both kinds of institutions are creditors, and are likely to see issues in a similar light. The place where credit unions differ from banks is that we do not define ourselves solely as creditors. We have the interest of the consumer in mind as well. The typical banker — and his lobbyist — are not so concerned with the rights and interests of their customers as credit unions are with the rights and interests of their members.

Where we've been, where we are

Americans love their credit unions. That's the good news. Chances are your members love your credit union. Year after year credit unions outperform banks in surveys of consumer satisfaction. The people who work for and in credit unions are highly regarded by their fellow citizens. And there's good reason for this.



The quality unique to credit union lending managers is their passion for responsible lending.

► discussion question

As a credit union loan officer, how do you differentiate yourself from a bank loan officer?

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Credit unions are the only financial institution in America that have their members' interest as well as their organizational interest in mind.

In general, credit unions have the best savings rates. We have the lowest fees. We have great loan rates. And we have a friendly and professional staff to serve our members. In short, we're concerned about the financial well-being of our members. That sets credit unions apart from other financial institutions.

Members aren't the only people who love credit unions. Congress loves credit unions, too. Representatives in Congress know that credit unions have more than 86 million of their constituents as members, so they understand the influence those numbers can have in speaking out on financial legislation. Congress also likes the financial strength of credit unions. As a group, America's credit unions have a capital ratio of nearly 11%.

Over the years, credit unions have earned the high regard of the public and legislators by making lots of loans to lots of people and raising the standard of living of millions of families. Aggregate loan totals for American credit unions are approaching \$450 billion. The average loan-to-share ratio is 75%. Credit unions are doing a great deal to help their members manage and improve their financial lives.

Vicki Lovett, vice president of loan operations for Suncoast Schools FCU, and a member of the CUNA Lending Council Executive Committee, puts it this way: "Credit Unions have many advantages over other lenders, including the ability to focus on members and their needs. We should be responsive and sensitive to changes in members' needs, since we typically are locally managed and our focus is exactly their needs."

Lovett also observes that historically, credit unions have relied on auto loans as their bread and butter. But competition for auto loans from multiple channels — dealerships, Internet lenders, community banks, and insurance companies — has become widespread. Credit unions need to develop creative ways of maintaining their share of the market and develop other loan products such as mortgages and member business loans to diversify their portfolios.

As we look forward to possible developments in the future, we can safely assume that some things will remain unchanged. Credit unions' legal and political battles, for example, will not end. Both field of membership and taxation challenges are likely to continue for the foreseeable future. The fight for more regulatory relief will also continue. Despite passage of the the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, we can reasonably expect bankruptcy to continue to be an issue credit unions and their members must deal with.

Regulatory reform will also be on the agenda. Credit unions need to continue to be involved in the regulatory process in order to protect their interests in the marketplace. Each year the Federal Register publishes new and amended rules amounting to 70,000 new pages. The executive branch of government deserves our scrutiny just as the legislative branch does.

Financial privacy is another issue that will continue to occupy credit union lobbying efforts. Privacy will be a concern from both a legislative and a regulatory standpoint.

Competition will continue to increase in the financial services marketplace. Traditional competitors including banks will work harder and smarter to attract business from credit union members. Pension funds are likely to become more aggressive competitors in the marketplace. Life

► hot topic

Next Political Battle for the Credit Union

How will credit unions be affected by issues on the political horizon? What do these issues mean for the loan department?

► discussion question

Who are your credit union's likeliest future competitors for making loans to members?

insurance companies will continue their campaign to remove barriers to their entry into the banking business. Mutual funds will continue to grow. Small loan companies, check-cashing services, and pawn shops will continue to serve their niche of the market. And some of the new competition will even come from other credit unions as more credit unions adopt community fields of membership.

Each of these competitors sees the financial services industry as a potentially lucrative market and will fight hard to gain a larger share of that market. Each of them poses unique challenges.

On the user side of the equation, we can expect continued change in consumer attitudes toward the use of credit. The national epidemic of personal bankruptcies is one example of the kind of change we've seen in attitudes about debt and personal responsibility. The stigma of bankruptcy is gone and it will take more than a new law on the books to change our cultural perceptions with respect to financial responsibility. In the long term, it's education, not legislation that will effect a permanent change in attitudes.

Credit unions can contribute in a significant way to the achievement of the educational goal. Credit unions are the only financial institution in America that have their members' interest as well as their own interest in mind. People love credit unions because they know that credit unions exist to serve them, not just to make a profit. So when a credit union speaks out on issues that affect the financial well-being of consumers, the message carries a great credibility.

The object is to deliver technology to members without losing the personal touch.

► definition

Technology Plan

Method for defining, prioritizing, managing, and measuring the use of technology and its costs.

The Internet

Technology, and more specifically the Internet, is changing the way credit unions do business in substantial ways. For many credit unions, it already has. The Internet has brought the whole world to our fingertips as consumers, and we're ready to take advantage of that world. Financial service providers now have a number of delivery channels available to them: person-to-person, the mail, the telephone, and now the Internet.

Today, more than half of all U.S. households have computers. (The percentage varies by state, from a high of 65% in Alaska to a low of 38% in Mississippi.) In a relatively short time many of those households have come to expect, even demand, doing their financial business on the Internet. And credit unions need to be prepared to compete in this new marketplace. Members need to be able to access their credit union at any time, day or night, weekday or weekend and use any of the credit union's services immediately. Quick answers are essential for success on the Internet. Service requests must be fulfilled within seconds, loan decisions within a minute or two of application submission, and answers by e-mail, mail, and phone as rapidly as members expect them.

The technology is there to be used, and if credit unions do not use it somebody else will. Concerns such as privacy and security are valid but with a well-developed technology plan the credit union can address these issues and overcome any obstacles they may present.

Consumers want their loans delivered better and faster. Our society may be moving a bit too fast but there's no time to stop and reflect on the implications of technology. The world of consumer finance is moving

Lending Products and Services Segmented by Member Age

<p>Youth Members (under age 18)</p> <ul style="list-style-type: none"> • Education loans • Automobile loans • Credit cards • Consumer loans for bicycles, other hard goods 	<p>Midlife (ages 25 to 40)</p> <ul style="list-style-type: none"> • Home improvement loans • Home equity loans • Second mortgages • Automobile loans
<p>Young Adults (ages 18 to 25)</p> <ul style="list-style-type: none"> • First-time home loans • Student loans • Computer loans • Vehicle loans • Lines of credit • Recreational equipment loans 	<p>Mature Adults (ages 41 to 65)</p> <ul style="list-style-type: none"> • Recreational vehicle loans • Travel loans • Second home loans • Luxury automobile loans • Home equity lines of credit • Electronic services loans • Reverse mortgages

Figure 9.1 Lending Products and Services Segmented by Member Age

► your notes

at lightning speed, and credit unions need to keep pace in order to remain viable. The object is to deliver technology to members without losing the personal touch.

Here’s how Vicki Lovett at Suncoast Schools FCU puts it: “Internet availability of financial services has gone from rare to commonplace very quickly. Credit unions need to enable a broad array of services online to meet their members ever more sophisticated technological needs. And credit unions must also be aware of the pitfalls of electronic commerce, most notably the risk of fraud and identity theft and ensure that software and origination practices are in place to avoid losses in this area.”

As credit unions embark upon the age of electronic commerce, we need to retain as much of the personal touch as possible. Lending, because it is at the heart of the credit union mission, is the place where this personal service is most likely to be delivered.

Connecting with Future Borrowers

The next generation of members comprises the borrowers of our future. Research shows these members are more technically savvy, more demanding of quick service but extremely loyal to those who meet their needs. Credit unions that find a way to meet their needs will have great success with this demographic.

Credit unions need to examine its members to determine what sorts of services they are likely to need in the future, and to develop services

aimed specifically at them. For example, if a credit union's field of membership were segmented in terms of age, the list of lending products and services for its primary age groups might look like this:

Of special interest to lending managers are the young adults just entering the market for loans, generally referred to as generation Y. Analysts at CUNA suggest that the average credit union stands to lose \$14 million in loans over the next decade if it does not increase loan penetration among 18- to 24-year-olds. These are our future borrowers and attracting them is critical to the long-term success of the enterprise.

Research by the Filene Research Institute reveals some startling facts about the market opportunities in reaching out to young adults:

- Teenagers alone spent \$172 billion in 2001. And today's youth market is larger than even the baby boom generation.
- Age, marital status, and the presence of children in the household are key factors in segmenting the young adult market.
- Today's young adults have access to a tremendous library of information on products and services and they use that information to become better shoppers. They understand their market power and have raised their expectations.
- Young Americans are active consumers of financial products — savings and loan instruments as well as investment vehicles.
- An investment today in serving young members will pay significant dividends in marketing core credit union products in the future.

In short, research from a variety of sources indicates that credit unions cannot ignore the importance and the market power of their young adult members and potential members.

These trends have serious implications for the future of credit union lending. It will take planning to work our way through these trends. Planning is more important than ever. It becomes more important than ever to attract members — and borrowers — while they are still young. An individual's choice of financial institutions is made at a relatively early age and like other purchase decisions, becomes habit-forming. Individuals who choose the credit union for an education loan or a bike loan in their teen years are likely to continue to borrow at the credit union when they are ready for an automobile loan and then a first mortgage loan. Loyalty is established early in life and is likely to stay with us for decades to come.

How can the credit union reach out to young people today? Earlier we discussed the increasing importance of making credit union services available on the Internet. Young people are the most aggressive users of Internet technology and should be a target segment for loan products using electronic commerce. They are computer literate, they are in the process of forming lifelong shopping habits, and they will be a prime group for loans for years to come.

Across the nation credit unions have begun raising their awareness of the opportunities inherent in attracting and serving the millennial generation. Credit union executives are putting programs in place to catch the eye of their young adult members and creating products to serve them. Products and services developed to attract members at an early age (savings accounts for preteens, auto savings and loan programs for teens,

► important concept

Choosing Financial Institutions at an Early Age

To continue to be viable financial institutions, credit unions must reach out to the youth market. Check out Web sites for credit unions that are online to see what they are doing to attract the youth market.

Ensuring the future of credit unions

In order to assure the future success of the credit union, we need to focus on what makes it special and get better at those services and attitudes that have served us well in the past. According to data compiled by the Filene Research Institute, the typical credit union has:

- 35% of its members' credit card business
- 45% of its members' auto-loan business
- 51% of its members' personal loan business
- 20% of its members' IRAs

In addition:

- 55% of members have checking accounts at the credit union
- 64% of members have bank checking accounts
- 43% of members say the credit union is their primary financial institution

Success in the future will depend upon an enormous effort to improve these numbers, especially the number of members who regard the credit union as their primary financial institution. And the place where success begins is in the loan department. In order to provide the greatest good to the greatest number of people the credit union will have to constantly improve its lending services offering new and better products to serve all potential members.

For example, call centers have provided benefits of both speed and personal service to members applying for loans at their credit union. The call center environment offers a quick response time to members' loan requests, and it also gives them "live" response to loan inquiries.

Through automated lending software the credit union can simplify the lending process and free its employees to do the most important job in the credit union — talking to members about their loan requests and helping them to improve their financial well-being.

Part of the answer to maintaining the credit union's relevance in its members' lives is to maintain our market awareness. The credit union needs to understand who its competition is and what its competitors are doing. It also needs to remain cognizant of who its members are and what they want in terms of loan products.

Credit unions also need to maintain their political awareness and strength. The credit union movement has been extraordinarily successful in its lobbying efforts over the years due primarily to its ability to organize grassroots support for legislative programs that affect the organization and its members. These efforts will become even more important in the future as term limits make education of new legislators a priority issue. Keeping in touch with the people who make laws will be essential to the success of the credit union mission.

Along with maintaining contact with legislators — and the judiciary — credit unions will also have to continue to monitor regulatory changes on both the state and national levels. For example, new rules are being considered regarding electronic disclosure and financial privacy which will affect all credit unions in the future. It's not enough to skim these

new regulations. They must be examined in detail, for it's the details that could have major impact on the operation of the credit union.

Loans are the lifeblood of the credit union system. The manner in which the credit union provides loans is what sets it apart from the competition and makes it special. If the credit union doesn't make a massive effort to remain special, it stands to lose market share. It may also lose its privileged position in the estimation of Congress and attitudes on taxation could change. In a worst-case scenario, the credit union could ultimately become irrelevant in the financial lives of its members, the greatest tragedy of all.

Credit unions and their people can take pride in what they are and what they do for consumers. For one hundred years credit unions have stood apart as America's consumer-owned financial cooperatives. The heart and soul of credit unions is their mission to provide affordable credit to people of modest means in order to help them to richer, more fulfilling lives. It's up to all of us to maintain that tradition and to assure future generations that the credit union stands by them for their individual and collective financial success.

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