New Opportunities in the Small Business Credit Card Market

During the depths of the recent recession, many small businesses saw their access to credit diminish significantly and sometimes disappear completely. According to the U.S. Small Business Administration, the number of micro-loans (i.e., financing less than $100,000, including credit cards and credit lines) fell 16 percent from 2008 to 2009, and the total value of this financing declined over 5 percent. The SBA attributes the decrease, in part, to banks retreating from the small business credit market in the wake of the recession and credit crisis.
Belying their diminutive label, small businesses have an enormous impact on the U.S. economy. There are approximately 27 million of them, and they account for about half of both GDP and the private workforce.\(^1\) They spend approximately $5 trillion per year and, according to the Federal Reserve, a whopping 83 percent used credit cards in 2009.

The retreat from this market by many lenders during and immediately after the recession creates an enormous opportunity now that economic conditions are finally improving. Not only does the small business credit card market represent a huge and lucrative business, it’s up for grabs like never before. What’s more, many of these small businesses are getting healthier as the economic recovery takes hold and will soon need access to additional credit to finance their growth. In fact, one-fifth of all small businesses in the U.S. applied for a new credit card in 2009 (75 percent of these applications were successful), and this number is expected to have increased in 2010.\(^2\)

Until 2000, small financial institutions were active issuers of small business credit cards. However, last decade’s technology changes and evolving economies of scale ultimately resulted in a highly consolidated competitive landscape for credit cards. Many small issuers eventually sold their portfolios to larger institutions. By 2008, only 36 percent of U.S. financial institutions were still issuing credit cards.\(^3\) And according to the SBA, by 2009, institutions with assets of $10 billion or more controlled 82 percent of micro-business loans (including credit cards).\(^4\)

Given that the U.S. economic recovery is gaining momentum—2010 GDP figures exceeded estimates and prompted upwardly revised predictions for 2011\(^5\) —it’s not a stretch to presume that small businesses will be growing, too and increasingly requiring access to credit. In light of all this, community financial institutions should rethink their decisions to cede control of the small business credit card market to the largest banks.

The technology constraints that helped to force small financial institutions out of the business a decade ago no longer exist. Back then, a card issuer’s choices were few: it could decide to implement and administer its own in-house solution, or it could cobble together a patchwork of external services to handle the multitude of card administration chores. Both of these approaches were costly and inefficient, and many institutions reluctantly sold their portfolios and exited the credit card business. Today, however, full-service credit issuing solutions are robust, flexible, comprehensive and cost-effective. Services are available that can handle everything from origination to remittance and collections.

For example, it is unnecessary for banks to deploy expensive call centers for inbound customer service calls; the leading solution providers offer cost-effective 24/7/365 customer call center support for credit cardholders. Nor do banks have to worry about creating or maintaining Internet banking Web sites to accommodate their online credit card customers. Solution providers offer sophisticated Internet banking applications customized with a financial institution’s desired look and feel. Partners can also support dynamic statement printing, e-delivery and mail services incorporating the messaging and branding of the financial institution.

Additionally, these solution providers allow a bank or credit union to define and adjust its own credit administration procedures—including underwriting guidelines, credit limits, balance-transfer policies and other parameters related to individual accounts or the entire portfolio. Even concerns about fraud are better addressed today than in the recent past. Providers of the more sophisticated credit card management services use neural networks for fraud scoring and decisioning systems to check every transaction for potential fraud, and to verify suspicious activity with cardholders.
These technology advances make it feasible for smaller institutions to develop a whole new line of business to serve small business credit needs, one that can boost revenue and build customer loyalty and brand equity. Of course, banks must listen closely to customers so they can understand how small businesses are using credit and design card programs with features that appeal to small businesses. For instance, small businesses often use credit to help maintain payroll, cover short-term inventory costs, manage expenses, free up capital, and compensate for cash flow volatility. With these needs in mind, banks might design cards that include features such as cash back or rewards to pay for business travel costs.

By paying attention to customers, and by partnering with an experienced solutions provider that offers scalable credit card services customized to each institution’s needs, a smaller financial institution can:

- **Drive incremental income.** Small business credit cards can be a consistent, recurring source of interest, fees and interchange income.

- **Foster loyalty.** Credit cards, along with demand deposits, savings accounts and traditional loans, are the four pillars of a financial relationship. By offering all four a financial institution can deepen its customer relationships. But the opposite is also true. The relationship is vulnerable if a customer requires a product or service—such as a credit card—and it’s not available.

- **Build the brand.** When a full menu of credit and deposit products is combined with excellent customer service, a financial institution burnishes its brand, enhances its ability to cross-sell, and strengthens its ties with individual customers and the community.

- **Improve convenience and efficiency.** Credit cards give consumers quick access to the funding they need—for short- or long-term requirements—without filling out time-consuming forms or opening and closing loans repeatedly. Financial institutions also benefit from this efficiency. Less paperwork and fewer delays for financing approvals translate into steady, high-margin interest and fee income.

**Conclusion**

The technology advancements in credit card management, combined with the increased income, loyalty, and brand equity that a commercial credit card program can generate make this line of business appealing—even compelling.

To reach out to small businesses, institutions must supplement their conventional direct mail, print and web marketing by joining small business associations, taking advantage of local sponsorship opportunities, and participating in Chamber of Commerce training and events. Many institutions have also found success in this market by stepping up their direct sales efforts—literally going door-to-door visiting local businesses to pitch their credit offerings. It is critical for local and regional financial institutions to be creative in order to rise above the promotional clamor: in the first quarter of 2010 alone, small business were bombarded with 46 million direct mail credit card offers, an increase of 256 percent over the previous year. This massive increase implies that institutions appreciate the opportunity that exists in the small business market right now—but it also means that in order to compete successfully, smaller institutions may need to emphasize their community ties and commitment to local markets.

With the economy set to expand and the need to access credit likely to grow, the small business credit card market is more attractive than ever. It presents an enormous opportunity for small and regional financial institutions, if they move quickly and adeptly enough to take advantage.
Sources:

1. U.S. Small Business Administration
2. U.S. Small Business Administration
4. U.S. Small Business Administration