

Credit Cards: Past, Present, Future

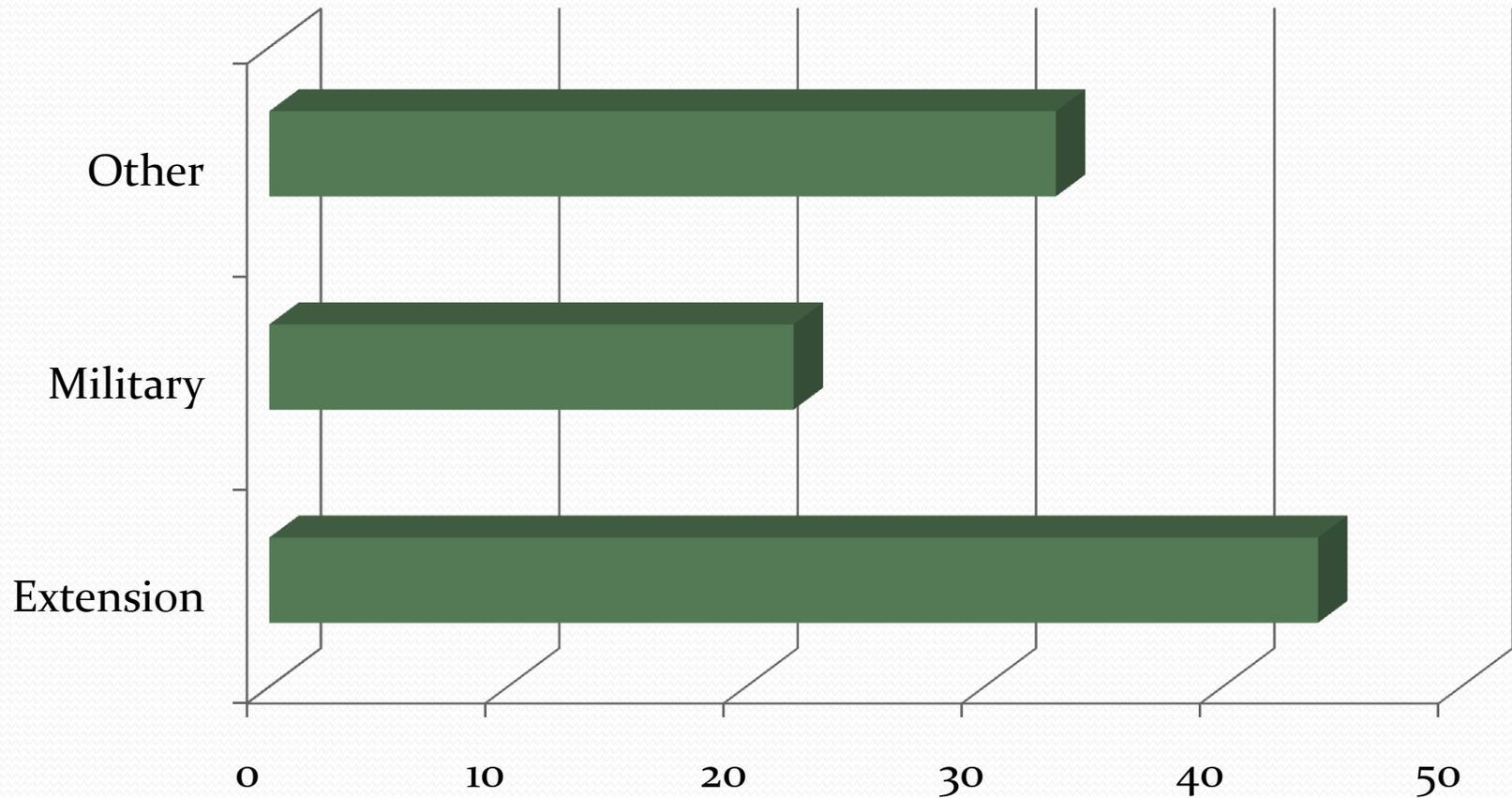
Kathleen Johnson, Research & Statistics
Amy Burke, Ben Olson, Jeanne Hogarth
Consumer & Community Affairs
Federal Reserve Board

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Housekeeping details

- Mute phones
- Use Q & A function to ask questions
- Use the seat indicators if you have issues
- We will use the polling feature

Who is in the audience?



Our cast of characters



Casey Bell



Amy Burke



Jeanne Hogarth

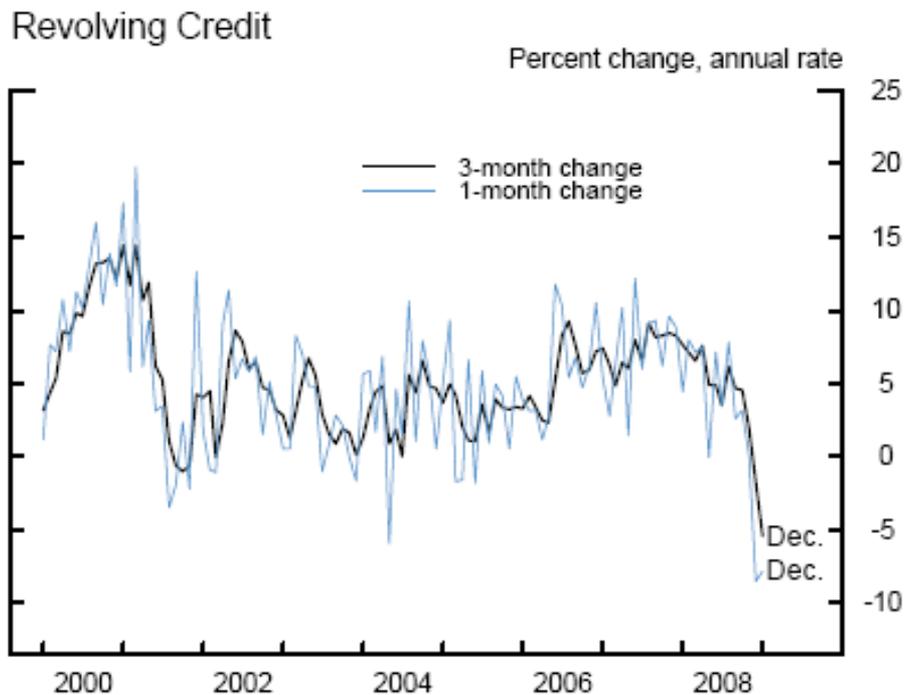


Kathleen Johnson

Ben Olson



Credit growth has slowed



Source: Federal Reserve.

- Includes both credit cards and other types of revolving plans.
- Began to slow in mid-2008.
- Declined about $7\frac{3}{4}$ percent at an annual rate in 2008Q4—it's slowest pace in decades.

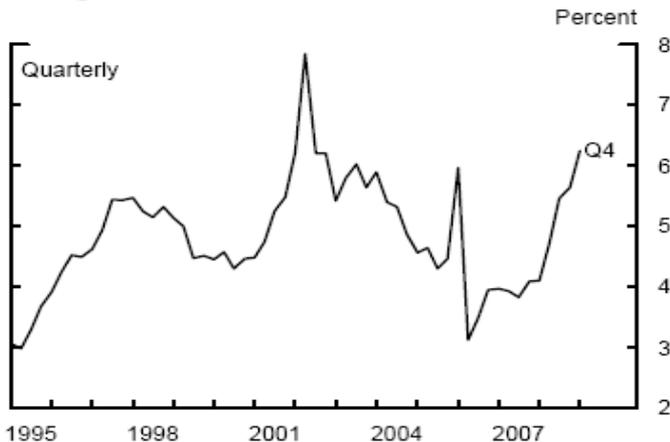
Credit quality has deteriorated

Delinquencies at Commercial Banks



Source. Call Report.

Charge-Offs at Commercial Banks

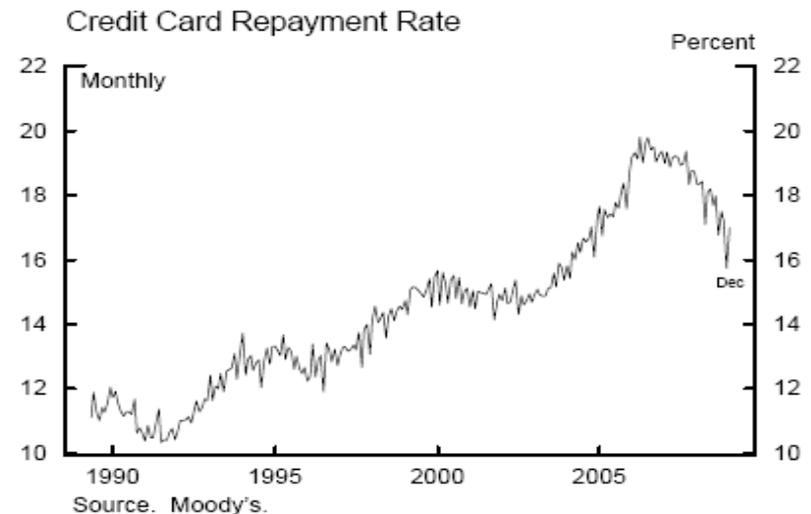
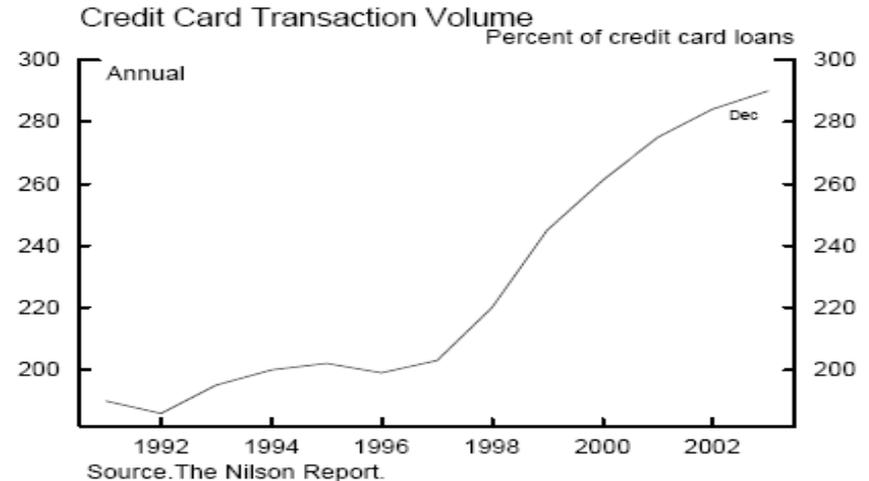


Source. Call Report.

- The fraction of credit card loans that are more than 30 days past due is higher than in recent years.
- The fraction of credit card loans that were charged off has risen to pre-bankruptcy-reform levels.

Trends in credit card use

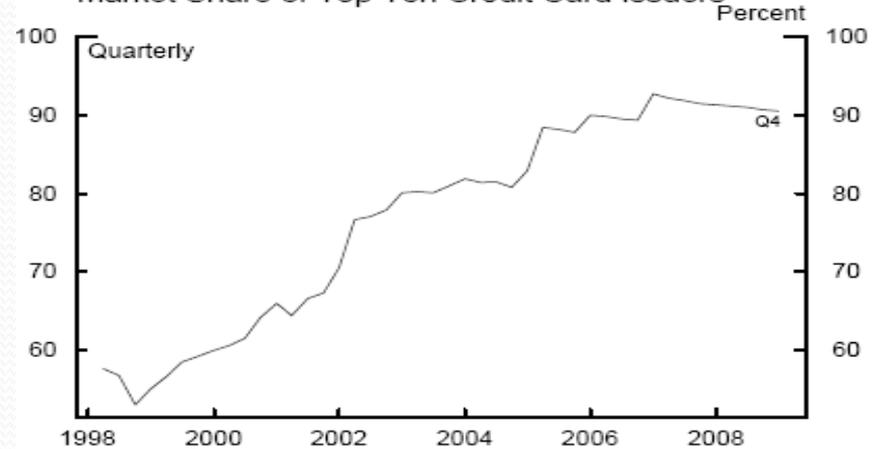
- Transactions volume as a share of total outstanding loans has been rising, suggesting more households are using their cards for convenience.
- In addition, consumers have recently begun paying off a smaller share of their balances, but this share is still high by historical standards.



Trends in the credit card industry

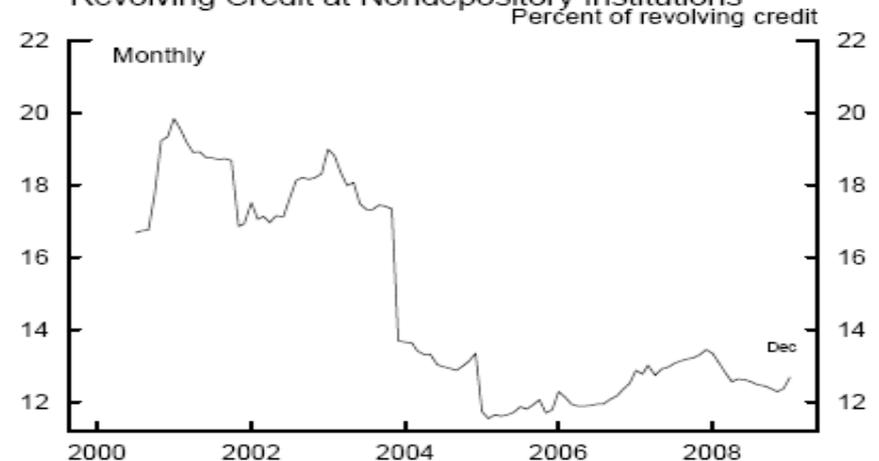
- The credit card industry has become very concentrated, with the top ten bank issuers currently holding about 90 percent of the market.
- Commercial banks account for the majority of the market. Non-depository institutions account for a small share.

Market Share of Top Ten Credit Card Issuers



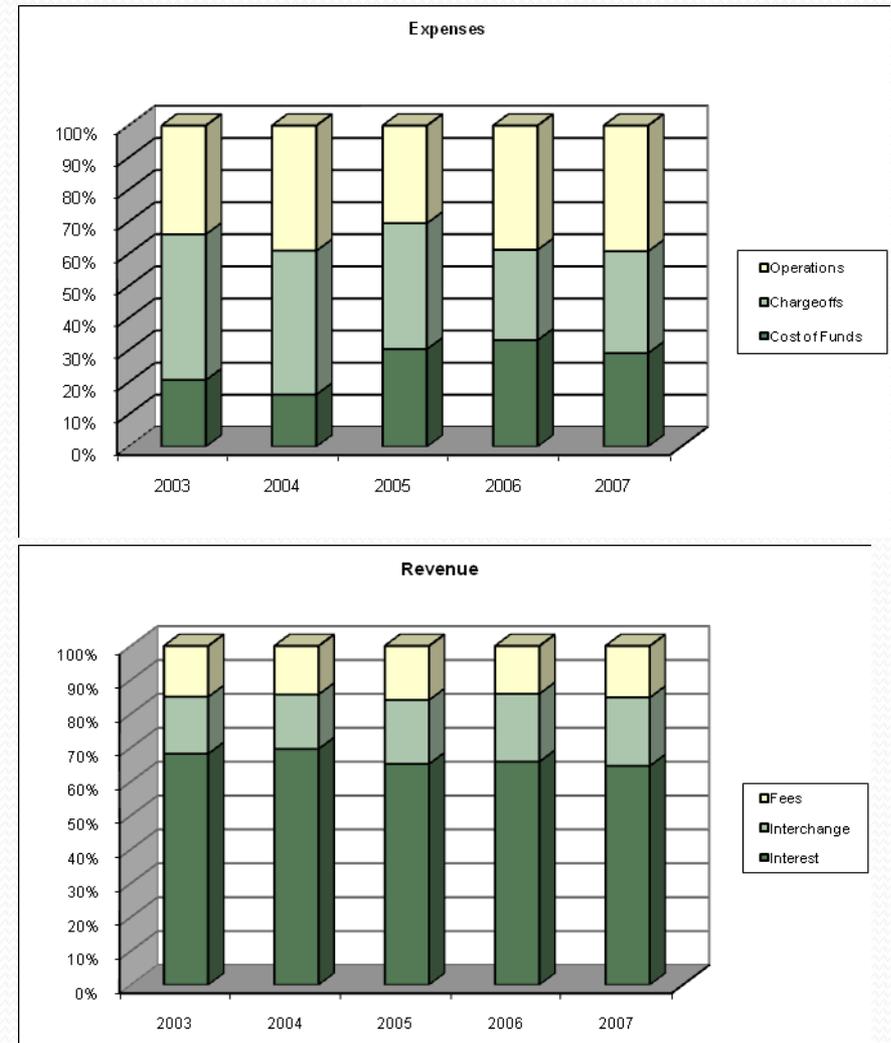
Source: Commercial Bank Consolidated Reports of Condition and Income.

Revolving Credit at Nondepository Institutions



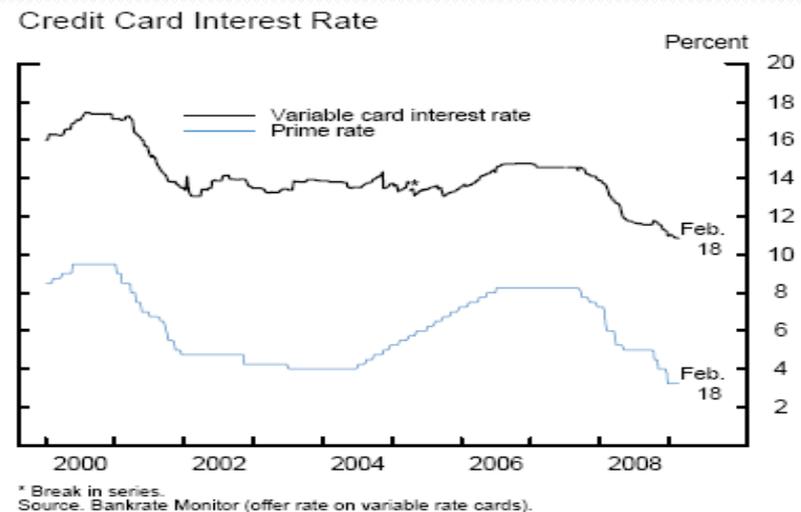
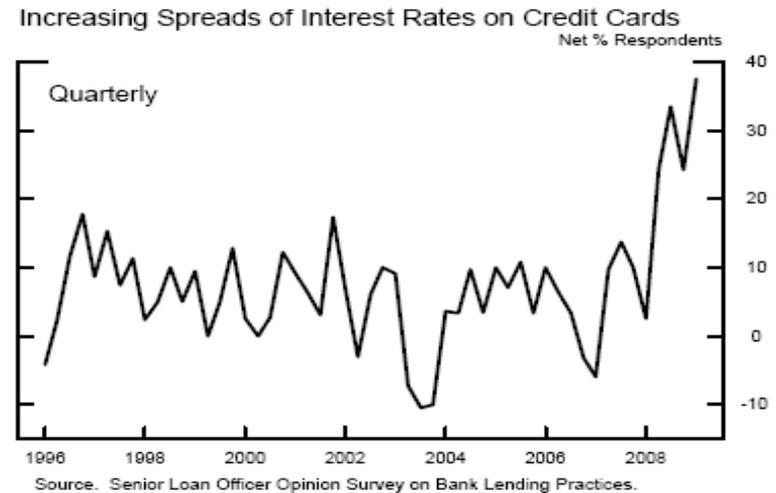
Trends in credit card profitability

- The sources of revenues and expenses have not changed significantly over the past five years.
- Expenses are roughly equally distributed among the cost of funds, charge-offs and operations.
- The bulk of revenues come from interest payments.



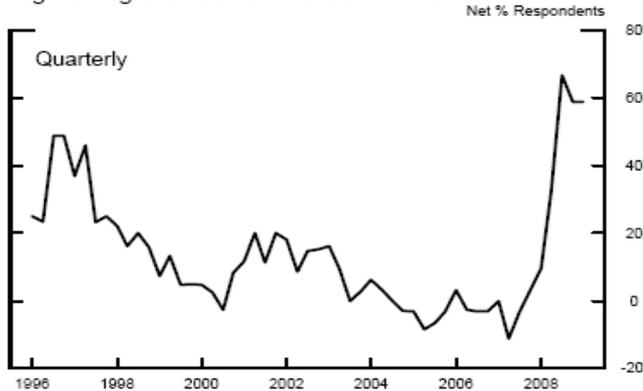
Credit card interest rates

- Nearly 40 percent of banks reported increasing spreads of interest rates on credit cards (the difference between the rate charged consumers and a cost of obtaining funds).
- Although interest rates on credit cards have fallen in 2008, the prime rate has fallen by more.



Credit availability has declined

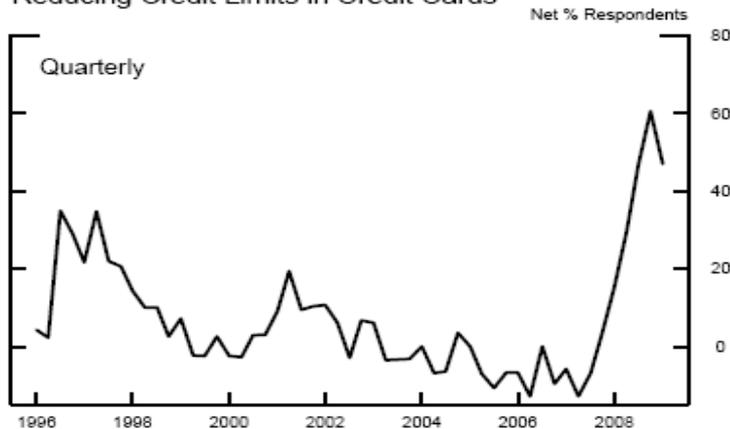
Tightening Standards in Credit Cards



Source. Senior Loan Officer Opinion Survey on Bank Lending Practices.

- A large fraction of banks continue to report tightening credit card standards.

Reducing Credit Limits in Credit Cards



Source. Senior Loan Officer Opinion Survey on Bank Lending Practices.

- Roughly 45 percent reported having lowered credit limits for credit card customers.

Conclusions

- Credit growth is slowing.
- A higher share of card balances are past due, and consumers are paying off smaller shares of their balances.
- Charge-offs are a significant share of the total cost of card issuers and interest income is a significant share of total revenue.
- Issuers report raising the interest rate spread on credit cards, and are reducing credit limits.

Consumer testing

- Why we did it
- How we did it
- What we learned



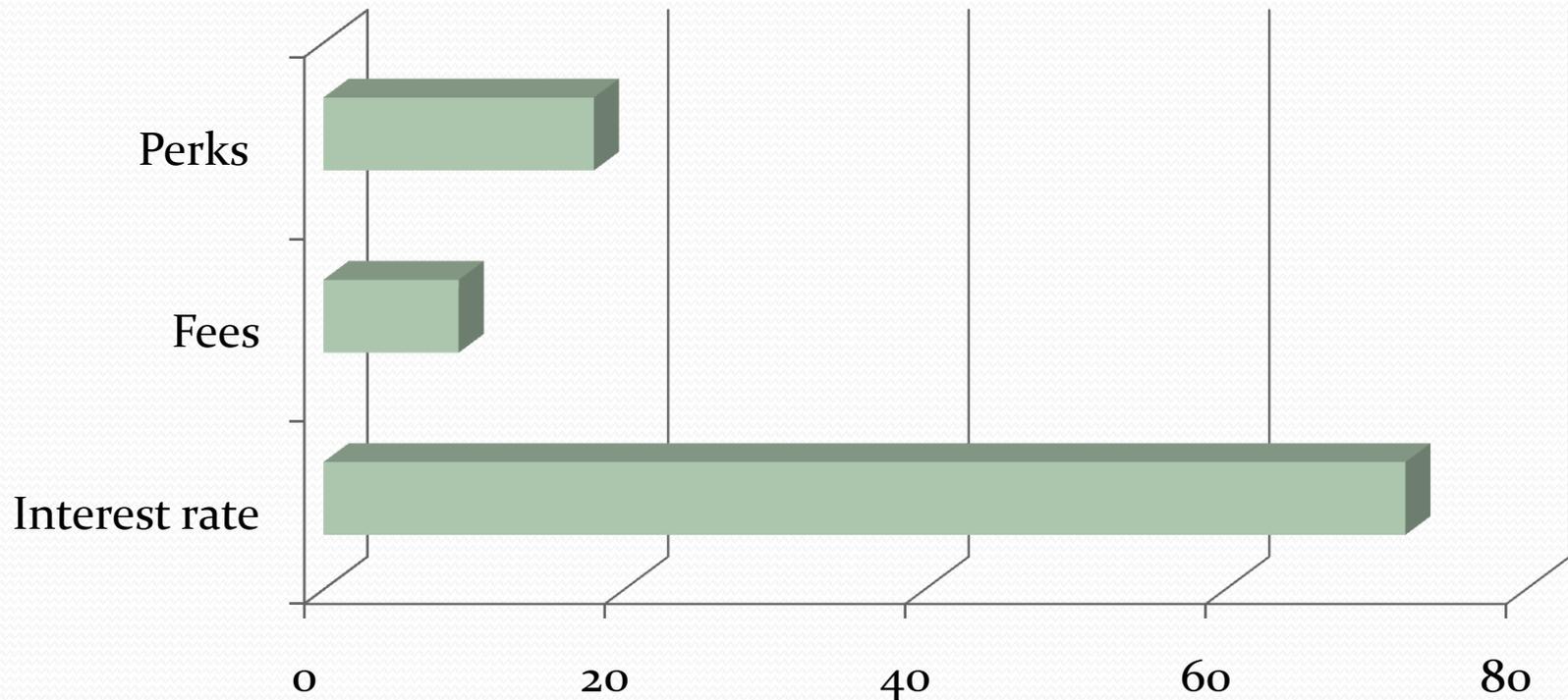
Reports on consumer testing

- Credit cards
 - Design of effective Truth in Lending disclosures (May 23, 2007 press release)
 - Design and testing of effective Truth in Lending disclosures: Findings from qualitative consumer research (December 18, 2008 press release)
 - Design and testing of effective Truth in Lending disclosures: Findings from experimental study (December 18, 2008 press release)
- Mortgages
 - Consumer testing of mortgage broker disclosures: Summary of findings (July 14, 2008 press release)
- www.federalreserve.gov/newsevents/press/bcreg/2009bcreg.htm -- change year to 2007 or 2008

Applications and solicitations

- Credit card issuers must disclose key costs and terms in a table with headings, content, and format substantially similar to the Board's model forms.
- Testing showed that many consumers did not notice additional important disclosures presented outside the table.
- Final rule will require disclosure in table of penalty rate and circumstances that trigger rate, as well as penalty fees.
- Based on testing, final rule requires simplified disclosures regarding variable rates and new terminology to describe grace period.

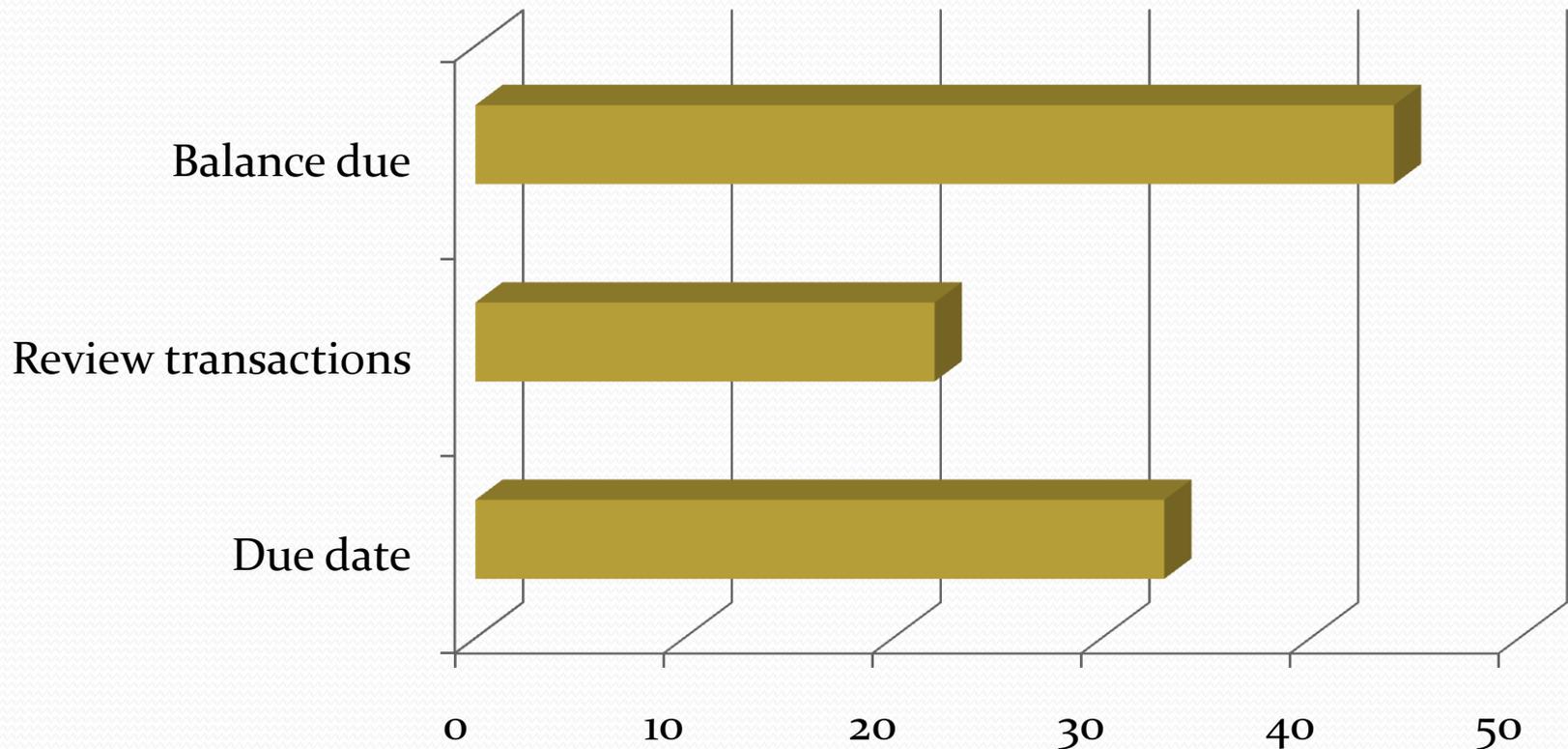
What do you look for when shopping for a credit card?



Account-opening disclosures

- Key terms disclosed at account-opening often are interspersed with long, complex credit agreements.
- Testing shows that consumers may not typically read these account agreements in small print and dense prose.
- Final rule will require key terms disclosed at account opening to be presented in a summary table substantially similar to table provided with applications and solicitations.

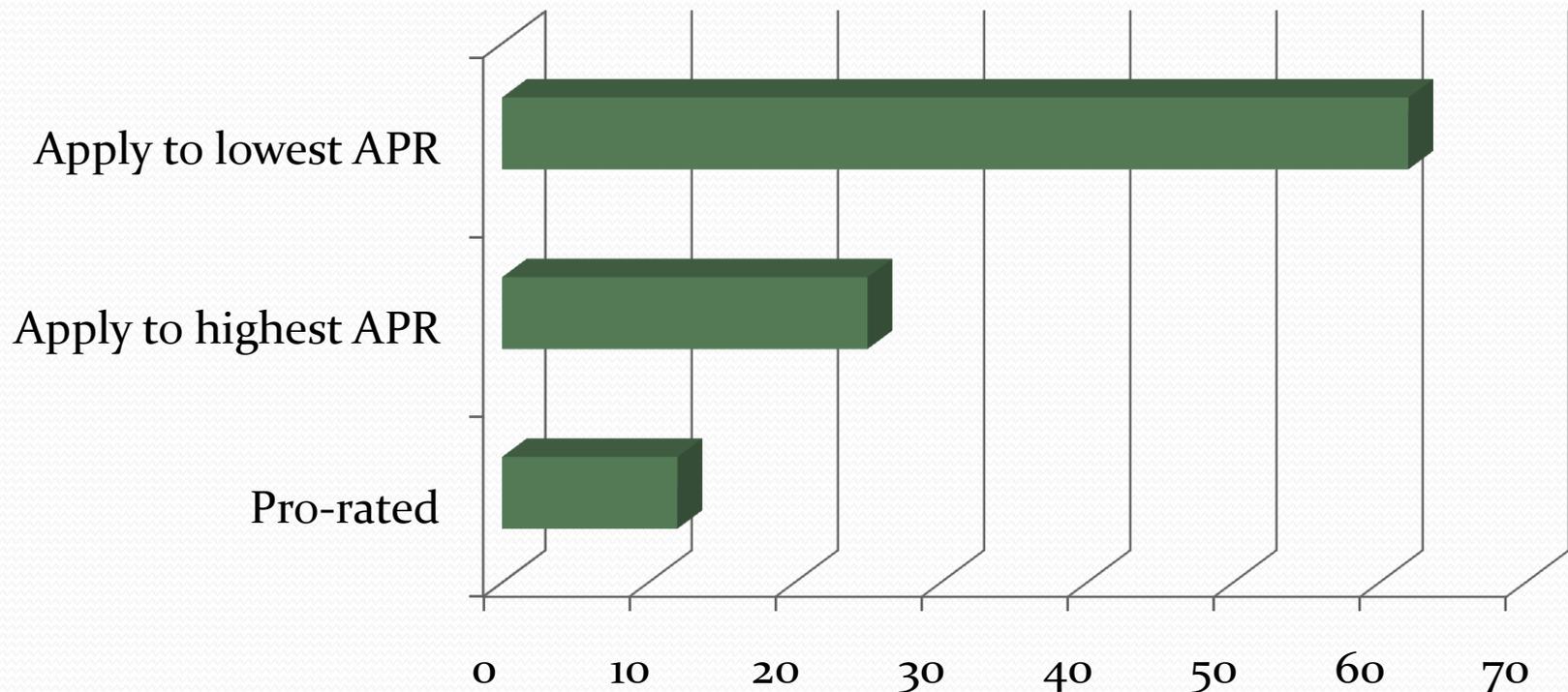
What do you look at first when you get your credit card bill?



Periodic statements

- Creditors are required to provide statements reflecting account activity for the billing cycle. Statements must include an “effective APR” which reflects both interest and fees.
- Testing showed that few consumers understood the effective APR disclosure, but that consumers notice and understand credit costs expressed in dollars.
- Final rule requires disclosure of total fees and interest for the cycle and year to date, and eliminates the requirement to disclose an effective APR.

Suppose you owe \$500; \$200 at 0% for balance transfer, \$200 at 12% for purchases, \$100 at 15% for cash advances. You make a \$100 payment – how is it applied?



Payment allocation

- Credit cards often have different rates for different balances (for example, purchases, cash advances, balance transfers).
- Issuers maximize interest by applying payments first to the balance with the lowest rate.
- Testing shows that disclosure does not enable consumers to understand how payment allocation affects interest charges.
- Final rule will require issuers to apply payments to the highest rate balance first or pro rata among all balances.

Increasing interest rates

- Consumers rely on the stated rate when using their credit cards for transactions, only to have that rate increase.
- Disclosure not adequate because reason for increase may not be avoidable by consumer (for example, payment received after due date because of delays in mail delivery).
- Final rule generally prohibits rate increases on past transactions unless specifically disclosed in advance (for example, “5% for six months, then 15%”).

Two-cycle billing

- Some issuers reach back to prior billing cycles to calculate interest when the consumer loses the grace period (two-cycle billing).
- Testing shows that disclosure does not enable consumers to understand the effect of different calculation methods on interest charges.
- Final rule prohibits the two-cycle method.

Reasonable time to pay

- Some issuers do not mail statements sufficiently in advance of the due date for consumers to review and make payment.
- Disclosure cannot remedy this issue.
- Final rule prohibits issuers from treating payments as late unless consumers have a reasonable amount of time to pay.
- Safe harbor for mailing or delivering statements 21 days before the due date.

High-fee credit cards

- Some credit cards marketed to subprime consumers charge fees that consume most of the available credit (for example, \$250 in fees on a card with a \$300 limit).
- Disclosure can improve understanding but cannot protect consumers who have no other options.
- Final rule limits fees to 25% of the credit limit at account opening and 50% of the limit during the first six months.

Coming soon

- Credit card repayment calculator
- Credit card website

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Credit Card Repayment Calculator

[Print](#)

Welcome to the Federal Reserve's Credit Card Repayment Calculator. Based on the information you provide, the calculator will give you an estimate of how long it will take you to pay off your credit card balance. The calculator assumes:

- you make no more charges; and
- you make only the minimum payment each month.

A second calculation can help you develop a plan for paying off your balance sooner.

Please use your most recent credit card bill. You may get a more accurate estimate from your credit card issuer's web site.

How long will it take me to pay off my credit card balance if I make only the minimum payment?

My total balance: \$ 

My highest annual percentage rate (APR) with a balance: % 

CALCULATE NOW

Last Update: February 26, 2009

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How long will it take me to pay off my credit card balance if I make only the minimum payment?

My total balance:

\$



My highest annual percentage rate (APR) with a balance: %



(Please scroll down to see your results)

You have entered a balance of \$7,900 at 15.00%. We estimate that:

\$158

Estimated initial minimum payment 

31 years

Amount of time to pay off your balance, if you make no more charges and make only the minimum payment on time each month

\$12,080

Interest charges you will pay in that amount of time

You have entered a balance of \$7,900 at 15.00%. We estimate that:

- \$158 Estimated initial minimum payment 
- 31 years Amount of time to pay off your balance, if you make no more charges and make only the minimum payment on time each month
- \$12,080 Interest charges you will pay in that amount of time

This is an estimate based on the information you provided and assumptions made about your account. The actual time and cost to pay off your balance by only making the minimum payment will depend on the terms of your account and future account activity. 

How do I pay off my credit card balance sooner?

The following estimates are based on your balance of \$7,900 at 15.00%.

I want to pay off my credit card balance in a specific number of years:

Enter number of years: [GET MONTHLY PAYMENT](#)

- \$153 Amount you need to pay each month to pay off your balance in the time above, if you make no more charges and pay on time each month 
- \$4,906 Interest charges you will pay in that amount of time

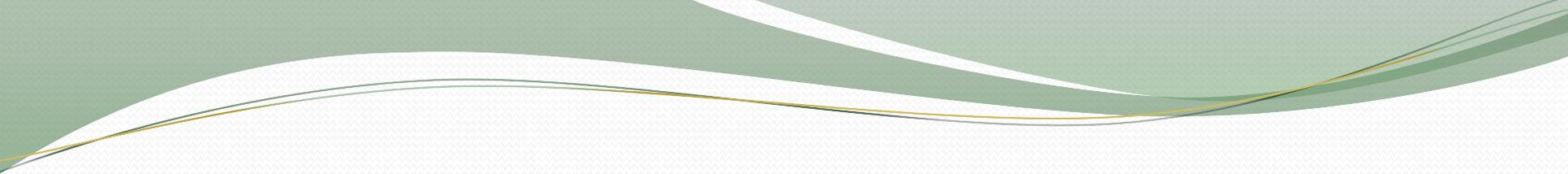
or

I want to pay a specific amount each month:

Enter monthly payment: \$ [GET TIMEFRAME](#)

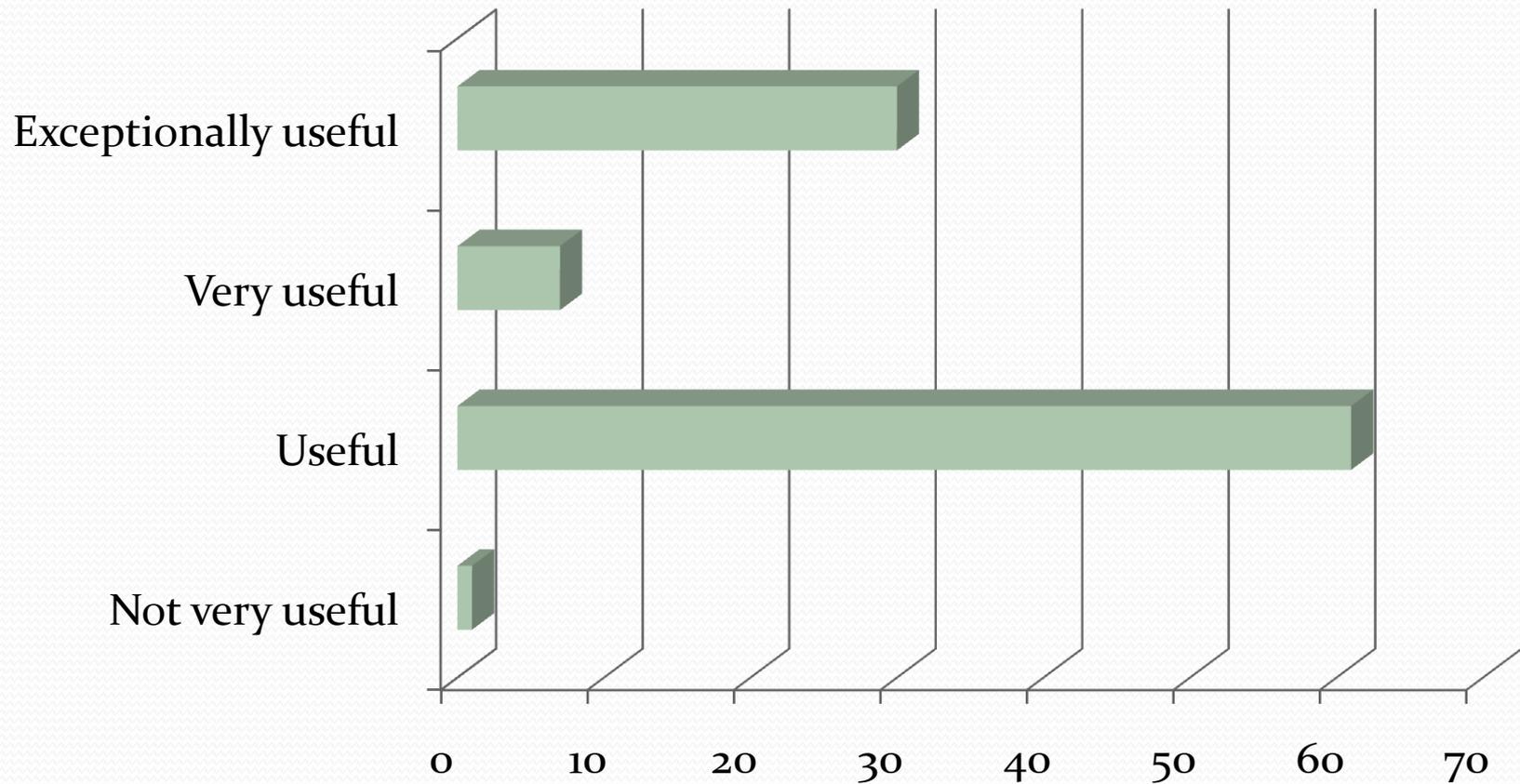
- 7 years Amount of time to pay off your balance if you make no more charges and make the above payment on time each month 
- \$4,576 Interest charges you will pay in that amount of time

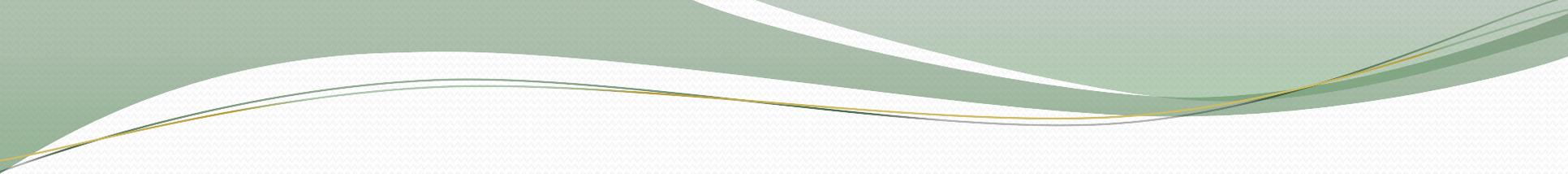
[START OVER](#)



Questions?

How useful was this for you?





Thank you!