

WHY BANKS SHOULD STOP IGNORING THE UNDERBANKED

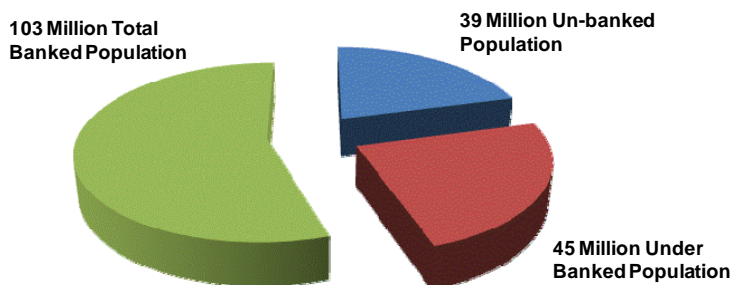
SUMMARY

The underbanked segment is a significant percentage of the entire U.S. population and while banks do acknowledge the underbanked live in their service area ⁽¹⁾, the vast majority of banks are not actively pursuing or offering services to these individuals. Therefore the underbanked are paying fees for prepaid debit card transactions, check cashing services, remittance payments and other financial transactions to non-bank institutions. Check cashing storefronts, debit card providers and non-banks such as Wal-Mart are benefiting from providing these services for this market. Banks tend to view the underbanked segment as too risky by assuming that all have both low income and low credit scores. While a portion of the underbanked does have those qualities, there is a segment of the underbanked that needs traditional bank products and is able to afford them. There are also products and services that can be designed to address the riskier segment as well. By designing an underbanked program that brings the underbanked into the banking sector, banks can position themselves to move the qualified underbanked into profitable traditional products and generate non-overdraft related income from nontraditional products.

DEBUNKING THE UNDERBANKED

The unbanked are consumers that do not have a checking or savings account with a bank. The underbanked are consumers that may have a current checking or savings account but have made at least one financial transaction at a non-bank in the last 30 days. For the purposes of this document, the underbanked term will include both the unbanked and the underbanked. Estimates for the number of underbanked individuals vary but all agree it is an extremely large segment. The chart below shows a conservative estimate of 84 million underbanked which includes the 39 million unbanked and 45 million underbanked populations.⁽²⁾ Other industry reports indicate the number could be as high as 106 million individuals.

SIZE OF THE UNDERBANKED MARKET



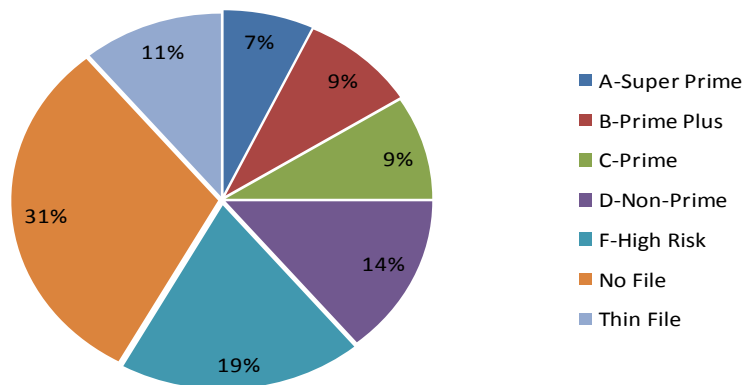
DEMOGRAPHICS OF THE UNDERBANKED ⁽³⁾

- Household Income: \$26, 390 (median), \$47,500 (mean)
Note: 18% of survey did not provide household income
- Ethnicity: White 60%, Hispanic 19%, Black 16% and Other 5%
- Homeownership: 63% own, 28% rent, 8% live rent free
- Marital Status: 29% never married, 27% married, 16% divorced/separated, 8% widowed
- Employment Status: 47% full-time, 11% part-time, 41% not-employed
- Reason for unemployment: Retired and homemakers make-up 52% of those not currently employed

UNDERBANKED FINANCIAL SERVICES ⁽³⁾

- Currently have neither checking nor savings accounts: 51%
- Have never had a bank account: 48%
- Have borrowed money in the last 12 months: 28%

UNDERBANKED CREDIT SCORES ⁽³⁾



- 25% had a prime credit score
- 42% had thin or no credit
- 33% were considered subprime

WHY THE UNDERBANKED ARE NOT USING BANKS

The underbanked are transacting with non-banks due to a variety of reasons and circumstances. A portion of the underbanked has negative credit histories or very thin credit files which prevent them from opening traditional checking accounts. Others use non-bank services such as check cashing or remittance payments for the convenience or because banks do not offer the services. Underbanked consumers can also be living paycheck to paycheck with little need for banks or live in low income areas that do not have banks or the bank hours are not convenient. Significant portions of the underbanked are

immigrants who are faced with language or cultural barriers which prevent them from being traditional bank customers.

More than one-third of the underbanked individuals in the United States would rather use a prepaid card than a checking account for basic financial transactions if costs were equal according to one study ⁽³⁾. These consumers indicated it was the convenience, transparency, and privacy of prepaid cards that swayed them. These days, prepaid cards offer most of the convenience of a checking account, as well as savings products and credit building potential.

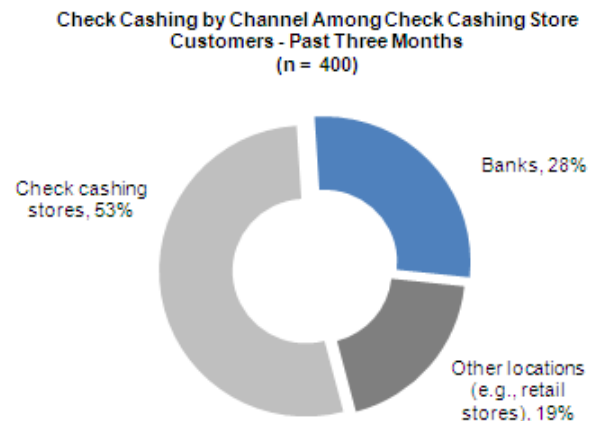
WHAT THE FEW BANKS IN THE MARKET ARE OFFERING

A regional bank is offering a check-cashing service in almost a quarter of its branches and is tracking those customers in the bank's customer relationship management (CRM) system which would allow the bank to offer other products as those customers move up in credit worthiness. Another large national bank is using its remittance services program to establish relationships with new customers. This bank is encouraging checking account opening by offering the same remittance service at a lower price point with an account as well as even lower prices for transfers from domestic checking accounts to bank accounts across borders. An international bank is focusing on a comprehensive strategy to serve Latin American immigrants which include remittances, check-cashing, home mortgages and even retirement accounts. ⁽⁴⁾ A few banks in the regional and national categories currently offer second chance accounts to individuals who do not qualify for a regular checking account. One of the regional banks adds on remittance payments through a money transfer partner (Western Union) in addition to offering second chance accounts. It's important to note that only one of the banks mentioned above has a comprehensive strategy to bring underbanked into the banking sector.

THE REAL PLAYERS IN THE UNDERBANKED MARKET

Check Cashing storefronts conduct a lot more than just check cashing these days. ACE Cash Express offers the following array of services: payday loans, tax refund checks, home loans, check cashing, bill payments, money transfers, prepaid debit cards, credit cards, purchase plans for televisions and computers (through America's Purchase Plan), auto loans (through a auto financing partner), direct deposit/payroll cards, prepaid phones and money orders. As shown below, more than twice as many customers are cashing checks at check cashing stores than at banks. ⁽⁵⁾

Large retailers have gotten into the banking arena as well. Wal-Mart, arguably the most aggressive in the financial services area, offers check cashing, money transfers, money orders and bill payment in its money centers as well as prepaid debit cards with a partner Green Dot who provides prepaid program management. Other retailers are



providing at least a prepaid debit card product.

Online banks are currently the biggest provider of second chance accounts for individuals with either bad or no credit history. Also in the market to provide second chance accounts are third party service providers that negotiate with banks to open checking accounts for those who are listed in Chex Systems or Telecheck for a fee up to \$75.

On the prepaid debit card front, large program managers Net Spend and Green Dot dominate the market with their retail partners providing distribution to a large section of the underbanked. The prepaid debit sector also has a lot of smaller players who provide a range of services from program management to distribution. The overall prepaid market is substantial and growing rapidly. Below are some prepaid industry estimates demonstrating the size of the market:

Prepaid Industry Estimates⁽⁶⁾

Aite		Federal Reserve	Mercator	Pelorus
Estimate	\$113 billion in transactions in 2007	312.8 million prepaid transactions in 2006, with a total value of \$13.3 billion	\$38.7 billion loaded onto prepaid cards in 2007	\$106 billion in transactions in 2007

POTENTIAL UNDERBANKED PRODUCTS AND SERVICES

The size of the underbanked market and the diversity of the credit-worthiness coupled with the significant revenue that non-bank institutions are generating from these individuals on financial transactions and products should be incentive enough for banks to get into this market. Banks have the capability to offer products that fit the needs of the underbanked segment now but also in the future as a portion of the underbanked climb up the credit score ladder. Below are products that meet the needs of the underbanked and are being offered by non-banks.

BILL PAYMENT

Bill payment options can include standard bill payment, next-day bill payments and same day payments through an express partner (i.e. Money Gram or Western Union). Separate price points can be set for all the different bill payment types and additional discounts can be offered for those who open a second chance or regular checking account with direct deposit.

CHECK CASHING SERVICE

Allowing non-customers to cash checks will allow banks to bring in new potential customers while also charging a fee to offset the risk. Utilizing a bank's CRM system to track these customers and obtain the required information for Know Your Customer regulations will allow banks to better market additional products and services to the underbanked.

PREPAID DEBIT CARDS

Offering General Purpose Reloadable (GPR) debit cards to bank customers who do not qualify for a credit card and utilizing the credit building functionality allows banks to move customers who establish sound credit into traditional credit products. Interchange revenue as well as fee revenue from the reloading fees can make this a profitable bank offering.

REMITTANCE PAYMENTS

Partnering with a money transfer service (i.e. Money Gram, Western Union, etc.) or offering money transfers as a stand-alone product will encourage non-customers to frequent branches and potentially buy other products or services from the bank.

SECOND CHANCE ACCOUNTS

For individuals that do not meet the regular checking account opening requirements either due to bad credit history or thin credit files, offer a second chance account. Banks should offer an account with features that appeal to this segment (debit cards, online bill pay, etc.), and restrictions that minimize risk (limiting overdraft capabilities, etc.

Second chance accounts will generate interchange revenue from the debit card transactions and a monthly maintenance fee. Banks can reduce the risk by prohibiting the customers to overdraw the account and not allowing checks to be written on the account. Electronic statements will reduce the paper expense associated with regular transaction accounts and requiring direct deposits will encourage “stickiness” and allow the bank to form a credit history on the account.

RESOURCE INFORMATION

⁽¹⁾An estimated 73 percent of banks in the United States recognize that unbanked or underbanked individuals live in their service area. Specifically, all Tier 1 banks, 90 percent of Tier 2 banks, and 71 percent of Tier 3 banks are aware of these populations. Source: FDIC study titled Banks’ Efforts to Serve the Unbanked and Underbanked for The Federal Deposit Insurance Corporation

⁽²⁾Source: Bearing Point, VISA

⁽³⁾Source: Center for Financial Services Innovation, “Underbanked Consumer Study”, June 2008, and “Underbanked Consumer Overview & Market Segments Fact Sheet”, Released: June 8, 2008

⁽⁴⁾Source: Center for Financial Services Innovation, “Highlights from the 3rd Annual Underbanked Financial Services Forum”, 2008

⁽⁵⁾Source: Aite Group, “Survey of 400 Check Cashing Store Customers”, November-December 2008

⁽⁶⁾Source: Federal Reserve System, “Electronic Payments Study”, 2007