Trends and Perspectives
The Hispanic Market and the Consumer Finance Industry*

PricewaterhouseCoopers Consumer Finance Group
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A foreword from the authors

Working with our clients over the last year, we have seen that many growth strategies have focused on the long term trends in emerging markets. There have also been many news articles focused on this issue. In the process of understanding this trend and considering alternative strategies for our clients to engage with this growing market, we have thought about many of the issues and opportunities raised. We are pleased to present you with this discussion document intended to highlight what we have seen and provide some perspectives on alternative approaches. Within this document we have drawn upon, are grateful for and have credited research completed by others. By consolidating recent trends, observations and analyses, we hope that you find this helpful as you continue to refine your strategy in this very important part of the market. If you have any questions or comments, please do not hesitate to reach out to us.

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Introduction

The Hispanic market represents one of the biggest growth opportunities for the consumer finance industry. This market not only represents the fastest growing minority but is also expected to have the biggest increase in buying power for the next 20 years. Several financial institutions are hiring more Spanish-speaking tellers and customer service agents, launching websites in Spanish, and partnering with Latin American companies.

Both the companies that have already realized the potential of this market and the companies that have not developed a clear targeting strategy have the opportunity to assess how their business model and competitive advantage can help them to gain a presence in the market some are calling “the next gold rush.”

This document incorporates research that PricewaterhouseCoopers’ Consumer Finance Group has been conducting surrounding the opportunities of the Hispanic market as well as guidance on what companies should take into consideration when developing a Hispanic market strategy.

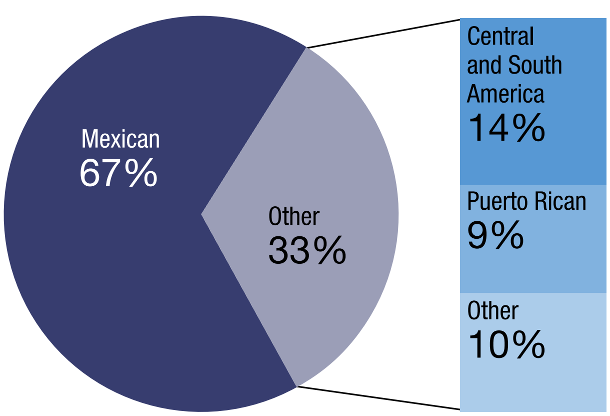
Hispanics in the U.S.

Demographics

Hispanic Americans have become the biggest minority in the nation. According to the latest U.S. Census information, there are 37.4 million Hispanics living in the United States, which accounts for 13.3% of the population. Among the Hispanic population, two-thirds were of Mexican origin, with the remaining third of other Hispanic origins (Figure 1).

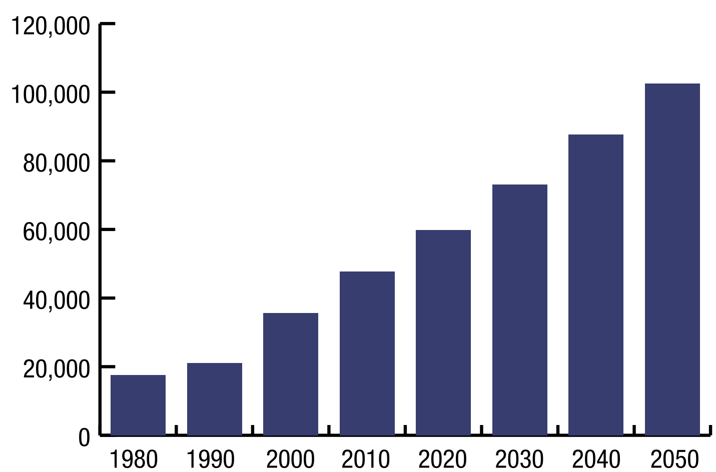
The Hispanic population grew almost 60% in the 1990s. Current growth projections estimate the Hispanic population will grow at four to five times the rate of the general population. The U.S. Census projects that by 2050 one in four Americans will be of Hispanic descent (Figure 2).

FIGURE 1. HISPANICS BY ORIGIN



Source: The Hispanic Population in the Unites States: March 2002, U.S. Census Bureau, June 2003

FIGURE 2. US HISPANIC POPULATION GROWTH



Source: The Hispanic Population in the Unites States: March 2002, U.S. Census Bureau, June 2003

As a group, Hispanics are younger than the general population. The median age for Hispanics is 27 versus 36 for the general population. Almost 40% of Hispanics are under the age of 18. This will translate to millions of new families being formed who will demand a multitude of financial products and services.

More than 35% of the Hispanic population is concentrated in the following ten cities:

CITY	HISPANIC POPULATION
1. Los Angeles	4,559,255
2. New York	2,769,550
3. Miami	1,326,700
4. Chicago	1,046,950
5. Houston	1.017,640
6. San Francisco	920,980
7. Dallas	855,265
8. San Antonio	734,220
9. Phoenix	653,550
10. San Diego	526,025

Source: Source: Scarborough USA+, DMA – Release 1, 12-month 2004

California, Texas, Illinois, Arizona, Florida and New York are the states that have historically shown the highest increases in Hispanic population. However, over the past few years, this trend has started to change. As the Hispanic population is growing, it is also spreading into areas with previous low Hispanic concentration such as the Carolinas, Georgia, Tennessee and Virginia.

Buying power

Hispanic buying power has been consistently growing as well. As of 2004, Hispanics had an estimated buying power of $686 billion that is primarily concentrated in five states:

STATE	HISPANIC BUYING POWER ($ BILLIONS)
1. California	$198.5
2. Texas	$119.3
3. Florida	$63.7
4. New York	$56.6
5. Illinois	$31.3
Buying Power of Top 5 States	68%

Source: The Multicultural Economy 2004, Selig Center for Economic Growth, Q3 2004

The 2002 U.S. Census estimated median Hispanic household income at $34,634, which was 20% less than the general population. But with the fastest increasing income growth of any other group, this gap is closing. From 1995 to 2001, median income growth for Hispanics was 27% while the growth rate for the general population was only 7.4%.

The immense buying power of Hispanic consumers is reshaping the retail and commercial landscape of the United States. The Selig Center for Economic Growth estimates that Hispanic purchasing power will reach $992 billion in 2009. According to the Center, the nation's Hispanic buying power will grow at a dynamic compound annual rate of 8.2%. The 2009 value will exceed the 1998 value by 347.1% – a percent that is substantially greater than either the 148.5%increase in non-Hispanic buying power or the 158.8% increase in the buying power of all consumers.[1]

[1] The Multicultural Economy 2004, Selig Center for Economic Growth, Q3 2004.

The Hispanic market and the consumer finance industry

The Hispanic market will be one of the most significant growth drivers for retail banking for the next decade and beyond. Hispanics are under-indexed for all banking products, including mortgages, deposits, credit cards, loans, investments and retirement services. There are several reasons that might explain this lower product acceptance:

- Some Hispanics may have the misconception that the U.S. banking system works the same way that banks in their countries worked before they emigrated to the U.S. (perfect credit score to have access to a loan or mortgage, bank employees that give preference to high-income customers, very limited product offering, etc.).
- Hispanics usually do not have long credit histories and this translates into lower or non-existent credit scores.
- The information available in Spanish is not available or incomplete.
- Some banks believe that a successful Hispanic strategy only involves translating information into a different language.

Below is a comparison of the percentage of people within each minority who have certain financial products.

PRODUCT	WHITE	ASIAN	AFRICAN-AMERICAN	HISPANIC
Deposit Accounts	93%	86%	71%	58%
Savings Accounts	87%	94%	78%	63%
Credit Cards	86%	90%	67%	64%

Source: 2002 U.S. Census

The Hispanic market is as diverse as it is large with numerous products and market segments. The U.S. consumer finance industry has been developing new products targeted at Hispanics, hiring Hispanic financial services professionals, creating Spanish language educational programs, opening Hispanic language service centers and customer support lines, and launching new Spanish and English language advertising campaigns – all of these efforts designed to acquire a share of this market.

Mortgages

While less than half of the country's Hispanics own their homes, Hispanic homeownership is expected to represent 40% of new homeowners by 2020, according to the Joint Center for Housing Studies. As a result, mortgage banking and home equity lenders are beginning to focus on this growing market now that the refinance boom is over and long-term production strategies are being re-assessed. The growth in Hispanic homeownership will primarily come from three sources:

1. Gains in income and education on an increasing number of young adult Hispanics who are entering the home buying market;
2. First- and second-generation Hispanics who will have access to mortgages due to expanded FICO scores and the acceptance of alternative forms of identification (such as the Individual Tax Identification Number or ITIN); and
3. Financial institutions' willingness to increase their focus on emerging markets.

Several of the companies are starting to target the Hispanic market by:

- Offering Spanish websites that provide information to consumers about the home buying process, how to improve credit scores, and about the different types of products that are available.
- Hiring Spanish-speaking loan officers and customer service representatives.
- Partnering with local organizations that support the Hispanic community and educating them on the benefits of owning a home.

Despite these efforts, mortgage information and services available for Hispanics are still limited and do not offer the same level of sophistication as other products, such as savings accounts or wire transfers. This presents a big opportunity for companies that are currently targeting Hispanics or for those that are interested in capturing a share of this promising market. The market potential can become even greater as companies start accepting additional forms of identification other than Social Security numbers. Just among the nation's roughly 6 million undocumented Hispanics is a potential $44 billion market for homes, according to a study released by the the National Association of Hispanic Real Estate Professionals.

In addition to the volume that Hispanic customers can bring to mortgage banks, companies are also starting to talk about the additional benefits of lending to Hispanics. Although not enough evidence is available yet, it seems that Hispanics' desire to maintain a good credit history and greater brand loyalty are resulting in lower prepayment and delinquency rates.

The following two tables show which of the top ten prime and subprime originators offer a Spanish website as well as Spanish toll-free numbers.

SPANISH INFORMATION OFFERED BY TOP 10 PRIME ORIGINATORS[2]

RANK	NAME	SPANISH WEBSITE[3]	EDUCATION SECTION?	SPANISH PHONE NUMBER?
1	Countrywide Financial Corp.	Yes	Yes	Yes
2	Wells Fargo Home Mortgage	Yes	Yes	Yes
3	Washington Mutual	No	No	Yes
4	Chase Home Finance	Yes	Yes	Yes
5	Bank of America	Yes	Yes	Yes
6	CitiMortgage, Inc.	No	No	No
7	GMAC Residential Holdings	No	Yes	No
8	National City Mortgage	No	No	No
9	Golden West Financial Corp.	No	No	No
10	Aurora Loan Services, Inc. (AA)	No	No	No

SPANISH INFORMATION OFFERED BY TOP 10 SUBPRIME ORIGINATORS[2]

RANK	NAME	SPANISH WEBSITE[3]	EDUCATION SECTION?	SPANISH PHONE NUMBER?
1	Ameriquest Mortgage Corp.	Yes	Yes	Yes
2	New Century Financial Corp.	No	No	No
3	Countrywide Financial Corp.	Yes	Yes	Yes
4	Washington Mutual	No	No	Yes
5	Option One Mortgage Corp.	No	No	No
6	First Franklin Financial	No	No	No
7	CitiFinancial	No	No	No
8	WMC Mortgage Corp.	No	No	No
9	Well Fargo Home Mortgage	Yes	Yes	Yes
10	HSBC Mortgage	No	No	No

[2] Source: PwC Research as of Q1 2005
[3] With equivalent content to website in English.

Remittances

Growth in the remittances market has recently been exponential. Just looking at the U.S.–Mexico remittances volume provides evidence of this. In 2004, Mexican immigrants in the United States sent a record $16.6 billion to their relatives in Mexico, an increase of 25% from 2003 and of 180% from 2001.[4]

What was a simple service almost exclusively provided by Western Union and Moneygram is now a multibillion dollar business that includes companies like Wal-Mart and Citibank. The dynamics of this business have changed dramatically in terms of the options available to send money to Latin America and the range of fees that institutions charge for providing this service. In the late 1990's dispatching a $200 remittance to Mexico could cost as much as $30 or 15% of the amount sent. By early 2004 the cost had been cut in half to 7.32% and it is now even 0% in one example we found.

Despite substantial marketing campaigns and very large investments over the past three years, U.S. banks have captured only a small fraction of the remittance transfer market. The four largest banks in this field – Citibank, Wells Fargo, Harris Banks and Bank of America – conduct less than 100,000 transactions a month. The vast majority go to Mexico. In 2003 an estimated 40 million remittance transactions carried money from the United States to Mexico, which suggests the banks have captured about 3% of the market.[5]

We can expect that the future of the remittances market will be dictated by two types of institutions:

1. Financial institutions that see the remittances market as a way to establish a long-term relationship with the senders. We can expect that these institutions will be more and more likely to offer free remittances or low-fee remittances to those customers who open savings or checking accounts. The trend is similar to free checking in the late 1990's or free online banking a couple of years ago.
2. Companies like Wal-Mart that want to increase the flow of Hispanic customers to its stores in the U.S. and companies that want to increase the flow of customers who are receiving remittances in Mexico.

Remittances can be sent and received at widely different types of establishments. For example, money dispatched by an agent for a wire transfer service out of a grocery store in Chicago might be picked up at a bank in Mexico. And likewise, money sent from a bank branch in the United States might be retrieved from an electronics store in Latin America.[6]

U.S. banks with a direct presence or alliance in Latin America are in a better position to increase their marketshare. As the banking systems in Latin America keep evolving, customers will be more likely to accept receiving their money via a debit card or in a checking account at a local bank instead of having to go to a bank branch or store to collect the money. This trend is very clear in the Mexican market, where Citbank is offering the "Tarjeta Tricolor" through its Mexican subsidiary Banamex and where Bank of America offers the SafeSend store value cards that can be used at any of the Plus and Visa Electron ATMs.

While consumer usage of wire transfers does correlate to income level, wire transfers are not exclusively a low-end product. Many banks have been surprised by the profile of their wire transfer customers. In fact, a 2003 study by the Multilateral Investment Fund and the Pew Hispanic Center revealed that over half of foreign-born Hispanics who sent wire transfers had incomes of over $30,000 and almost 20% had incomes over $50,000.[7]

[4] Vivek Taparia, "Banking Across Borders: The Future of U.S. Mexico Remittance Corridor," *Texas Business Review*, February 2005.
[5] Manuel Orozco, "The Remittance Marketplace: Prices, Policy and Financial Institutions," Pew Hispanic Center Report, June 2004.
[6] Ibid.
[7] "U.S. Retail Banking and the Hispanic Market Growth Engine," CMGP Hispano, March 1, 2004.

Two countries, one Hispanic market

Recent developments

Over the past few months, we have started to see that many companies are realizing that the competitive advantages and strategies they have been using to target the Hispanic market either in the United States or in Mexico can be combined to develop a single effort that targets a similar group of customers in two different geographic locations. What started solely as remittance-related ventures are becoming more and more integrated financial services businesses with operations in both the U.S. and Mexico. Companies from both sides of the border can benefit from this:

- U.S.-based institutions can learn from their Mexican counterparts as they have been working with Hispanic customers for decades and have direct access to government and financial market authorities south of the border. As the Mexican economy keeps growing, these learning experiences can translate into business opportunities through a direct presence (just as Citigroup did with the acquisition of Banamex), capital investment in a Mexican banking institution (as with Bank of America's investment in Santander-Serfin), or joint ventures (as with MBNA's recently announced joint venture with Ixe Banco).
- Mexican-based institutions can benefit from partnering with U.S. counterparts as this gives them access to additional sources of funding as well as access to knowledge of U.S. practices in product expertise, risk management, technology, controls and corporate governance.

We are also seeing that non-U.S. financial institutions are making strategic investments on both sides of the border with the specific objective of serving the Hispanic market. The most evident examples are BBVA's ownership of Bancomer in Mexico as well as their recent acquisition of the Laredo National Bank in Texas and Valley Bank in California.

Cross-border mortgage banking

The most recent evidence of the integration between the Mexican and U.S. mortgage banking markets has been the launch of a mortgage product for the Mexican immigrants who reside in the United States and who are interested in purchasing a home for themselves or for their relatives in Mexico. Although the loans will be originated in the U.S., the program is being funded by SHF (Sociedad Hipotecaria Federal) for loans up to $1.7 million pesos (roughly $150,000 USD).

SHF estimates that between 9% and 16% of the $16 billion of money transfers to Mexico are used for housing. Therefore, this program has the potential of generating between $1.4 and $2.6 billion USD in new origination volume every year.

Companies with a strong retail presence in those areas with a high Mexican immigrant concentration could especially benefit from this as Mexican mortgage banks will be looking to partner with them to get to the customers they are trying to serve.

Developing a Hispanic market strategy

Top five strategic considerations

1. End to End Hispanic Customer Service

Today, most financial institutions offer brochures in Spanish as well as offering Spanish-only websites and toll-free numbers. However, just limiting a company's effort to translating 100% of the information about products and services is not enough. According to David C. Schmittlein, professor of marketing at Wharton, "Reaching the U.S. Hispanic population is seldom as easy as translating print ads and information into Spanish. It is about influencing an entirely different culture, while remaining mindful of the mainstream."[8]

Hispanic customers are increasingly demanding "Hispanic-style" customer service at every stage of the customer relationship, from origination to loan closing and servicing. Some banks are already addressing this demand in very creative ways including creating playrooms for children, introducing the customer to the branch's entire staff, and offering free local phone service in the branches located in neighborhoods with a large concentration of Hispanic customers.

It is important for companies to understand the Hispanic culture and implement an integrated execution of their strategy at all levels of the organization. To be successful, Hispanic customers should see company employees as trusted advisors with whom they can talk about their mortgage, their personal finances and even their families. Lilia Alvarado Escobedo, vice president of Hispanic banking at Harris Bank, said that, "For many Hispanics, loans are family affairs, with two or more family members taking part in the transaction."[9]

Companies should also be very careful when offering printed information and Spanish websites. The same type of information and services should be offered to English- and Spanish-speaking customers. There are many examples of companies stating that they have a Spanish website to serve the Hispanic market while only providing a very brief description in Spanish of the services they offer.

2. Hispanic Market

Hispanics have very different product and service preferences based on their income level, education and number of years that their families have been in the U.S. While many may perceive the Hispanic population to be mainly lower income (it is estimated that approximately one in five Hispanics live in poverty), 14.5% can be considered affluent with incomes over $75,000.[10]

Following a single strategy that tries to address the needs of the Hispanic market as a whole may not be the right approach. Before implementing a strategy, the company first should identify those segments of the Hispanic market that can be more profitable and that fit the bank's overall strategy. These segments can range from low-income Hispanics who can only access subprime mortgages to high-income Hispanics interested in more sophisticated mortgages and home equity loans.

In addition to identifying the demographic and economic differences inside the Hispanic market, companies should also take into consideration potential clients' preferences about their preferred language to conduct business transactions. An important number of Hispanics are fluent in both English and Spanish but prefer to speak in English. Some companies make the mistake of sending information translated into Spanish to customers just based on whether or not their last name sounds "Hispanic-like."

[8] "Habla Español? Your Company Will Soon Have to Do That," Knowledge@Wharton, August 13, 2003.
[9] "Banks Look to Hispanics," *Chicago Sun-Times*, May 2, 2005.
[10] "U.S. Retail Banking and the Hispanic Market Growth Engine," CMGP Hispano, March 1, 2004.

3. Education Is Key!

Every Hispanic market strategy needs to include an educational component as many Hispanic borrowers apply lending criteria from their former experiences within their family or in the country from which they or their ancestors have come. For example, it is possible that a borrower could qualify for a prime mortgage but may believe that there is a 15-20% downpayment requirement or that the borrower needs to be in the same job for at least five years. Some Hispanic borrowers also believe that they can't sell the property they acquired until the original loan term expires. As a result, there are often many misconceptions among Hispanics regarding mortgages or credit approval processes in general.

In addition to this, there are some consumer finance concepts that might be entirely new to groups of customers who were not born in the U.S. An example of this is an escrow account linked to a mortgage (a concept that does not exist in countries like Mexico).

Hispanic immigrants tend to be more risk averse and conservative with investments than the average American, which explains in part why they avoid debt and are less likely to have a credit history. There is consensus that financial education is useful and necessary to the extent that individuals have financial decisions to make and are presented with choices.[11]

Some companies have developed alliances with Hispanic organizations to create websites that educate Hispanic consumers on how to buy a home step-by-step or how to improve their prospect for homeownership. The GSEs have also developed educational programs specifically targeted to Hispanics. One example is CreditSmart, a bilingual consumer education curriculum that introduces participants to the importance of credit in U.S. society and teaches them about money management skills.

4. Thinking Beyond Traditional Credit Evaluation

Entering the Hispanic market requires loan approval flexibility. For many companies, the mortgage loan approval process has become very rigid and is strictly dependant on the applicant's credit score and job history. Many times, companies are required to follow these types of standard guidelines in order to sell or securitize loans. However, many times Hispanics do not have a good credit score either due to their preference for cash transactions or their relatively short credit history. As a result, there are many strategies by which companies can proactively help Hispanic customers to enhance their loan eligibility:

- Ask customers for letters that demonstrate they have been paying their bills and rent on time for months and send this information to the credit reporting agencies. Information about the money they have been remitting to their home countries might also be useful to assess payment capacity.
- Encourage customers to apply for a secure credit card and start paying for some expenses (such as utility bills) using the card. This will add more information to the credit history and translate into a higher credit score.
- Help customers obtain their Individual Tax Identification Number (ITIN) if they are not eligible for Social Security and make sure that they have all their tax returns in order.
- Permit the pooling of money for downpayment and closing costs.

5. Today's Investments Are Tomorrow's Profits

Any executive in the process of implementing a Hispanic market strategy should be aware that big profits might not arrive in the short term. Entering or increasing participation in the Hispanic market represents an investment and a change of behavior across the organization to effectively target this important and growing segment of the consumer market. Those companies with a broad range of products and services can start serving segments of the Hispanic market with simple products such as credit cards and savings accounts and be the first company of choice once their customers' income increases and they start demanding mortgages and home equity loans. The growth of the Hispanic market's income and buying power is evident and the potential is enormous.

[11] "Financial Education in Latino Communities: An Analysis of Programs, Products and Results/Effects," National Council of La Raza, December 9, 2004.

In a time when mortgage banks and other players in the consumer finance industry are reassessing their strategies and plans for the future, the Hispanic market can be considered as one of the most important opportunities for growth.

Some financial institutions have already launched comprehensive initiatives and educational programs, such as proposals to fund home loans to minorities and lower-income borrowers, business to business Spanish websites, financial literacy programs, and more. Other institutions have only translated some of their services into Spanish. While their commitment and approach may not be effective, these companies have also acknowledged the growth potential of the Hispanic market.

Furthermore, while this report focused more on mortgages and remittances, similar trends are expected for credit cards and auto loans.

"Emerging markets" used to be a term that was the purvue of international banks. Today, that term applies to global institutions as well as regional and even local banks that are looking to expand their marketshare and capitalize on the opportunities of the emerging Hispanic market.

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