A Progressive Digital Media business

COMPANY PROFILE

Discover Financial Services

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COMPANY OVERVIEW

Discover Financial Services (DFS or 'the company') is a direct banking and payments services company. The company provides credit card loans, private student loans, personal loans, home equity loans and deposit products. DFS operates primarily in the US. It is headquartered in Riverwoods, Illinois.

The bank reported interest income of (US Dollars) US$8,616 million for the fiscal year ended December 2016 (FY2016), an increase of 8.4% over FY2015. The net interest income after loan loss provision of the bank was US$5,359 million in FY2016, compared to an operating profit of US$5,170 million in FY2015. In FY2016, the bank recorded a net margin of 27.8%, compared to a net margin of 28.9% in FY2015.

KEY FACTS

Head Office	Discover Financial Services 2500 Lake Cook Rd Riverwoods Illinois Riverwoods Illinois USA
Phone	1 2244050900
Fax	1 302 6555049
Web Address	www.discover.com
Revenue / turnover (USD Mn)	10,497.0
Financial Year End	December
Employees	15,549
New York Stock Exchange Ticker	DFS

SWOT ANALYSIS

Discover Financial Services (DFS or 'the company') is a direct banking and payments services company. The company provides credit card loans, private student loans, personal loans, home equity loans and deposit products. The company's wide array of products and services help retain and attract customers and maintain profitability. However, regulatory changes and intense competition in the cards industry could impact the company's market share and operations.

Strength	**Weakness**
Wide array of banking and payment products Agreements and alliances help expand geographic reach	Lack of geographic diversity increases volatility of the revenues
Opportunity	**Threat**
Growing e-commerce sales Huge opportunity in global small business spending	Intense rivalry within the existing players Regulatory changes could limit profit expansion

Strength

Wide array of banking and payment products

DFS provides its customers with a wide array of banking and payment products and services. The company's direct banking segment includes consumer banking and lending products, specifically Discover-branded credit cards issued to individuals on the Discover Network and other consumer banking products and services, including private student loans, personal loans, home equity loans, and other consumer lending and deposit products. The company's payment services business segment includes the PULSE Network (PULSE), an automated teller machine (ATM), debit and electronic funds transfer network; Diners Club International, a global payments network; and network partners business, which provides payment transaction processing and settlement services on the Discover network. Wide array of products and services help retain and attract customers and maintain profitability.

Agreements and alliances help expand geographic reach

DFS has been signing a number of agreements to expand its card network in the domestic region and foreign locations. For instance, in January 2017, DFS entered into an agreement with PayPal to offer PayPal services to the company's card members, acquirers and merchants. In April 2016, Diners Club International and Computop, an international payment services provider, announced an agreement to increase e-commerce acceptance for DFS, Diners Club and Alliance Partner cards. At the end of 2015, Sumitomo Mitsui Trust Club Co., Ltd., the wholly-owned subsidiary of Sumitomo Mitsui Trust Bank, Limited, became the exclusive issuer and acquirer of Diners Club cards in Japan. During October 2015, the online payments provider Checkout.com announced that all Checkout.com merchants would have the opportunity to accept sales from cards running on the Discover Global Network starting from that month. In May 2015, Diners Club International and Alternatifbank, a subsidiary bank of The Commercial Bank of Qatar Q.S.C., the exclusive provider of Diners Club cards in Qatar, announced an agreement to form a new Diners Club International issuing franchise in Turkey.

In the second quarter of 2014, Diners Club International and Bangkok Bank, a bank in Southeast Asia, started merchant acquiring in Thailand. Diners Club International and Corner Bank, a Swiss banking institution, announced an agreement to form a new Diners Club International franchise in Switzerland in the first quarter of 2014. DFS entered into an alliance with National Payments Corporation of India (NPCI) in 2012. Pursuant to the alliance, the Discover cards and Diners Club International (DCI) cards got accepted at NPCI automatic teller machines (ATM's) and the point-of-sale terminals for purchases in India. Agreements such as the above help the company expand its geographic reach and improve revenues.

Weakness

Lack of geographic diversity increases volatility of the revenues

DFS has most of its presence in its domestic region, the US. The company derives significant portion of its revenues from the US. Though the company has been extending its card network outside the US through agreements and alliances, revenues from foreign countries has been very insignificant. Concentration in one geographic unit makes the company’s performance vulnerable to regional economic, political, social and demographic conditions. Hence, the lack of geographic diversification increases volatility of the revenues leading to uncertain future.

Opportunity

Growing e-commerce sales

With an increase in interactive methods and limitless content, retail e-commerce is growing at a faster rate globally. According to the US Census Bureau, the estimate of US retail e-commerce sales for the fourth quarter of 2016, adjusted for seasonal variation, but not for price changes, was $102.7 billion, an increase of 1.9% from the third quarter of 2016. Total retail sales for the fourth quarter of 2016 were estimated at $1,235.5 billion, an increase of 1.9% from the third quarter of 2016. The fourth quarter 2016 e-commerce estimate increased 14.3% from the fourth quarter of 2015 while total retail sales increased 4.1 % in the same period. The e-commerce sales in the fourth quarter of 2016 accounted for 8.3% of total sales.

According to industry experts, e-commerce is the fastest growing retail market in Europe. Sales in the UK, Germany, France, Sweden, The Netherlands, Italy, Poland and Spain are expected to grow from £132.05 billion in 2014 to £156.67 billion in 2016 (an increase of 18.4%), reaching £185.44 billion in 2017. In FY2017, overall online sales are expected to grow by 18.4%, but 13.8% in the US on a much larger total. Thus, the growing e-commerce sales would act as a catalyst in increasing the company's revenue growth.

Huge opportunity in global small business spending

As per industry estimates, for the vast majority of global small-business spending only cash and checks are used instead of credit cards. In fact, the US small businesses use credit/charge cards for only about 15% of their spending and that amount is likely to be even lower internationally. Moreover, the midsize companies worldwide use cards for less than 10% of their major purchases such as travel and entertainment and office supplies. As a matter of fact, out of the total global consumer spending of $28 trillion each year, only 14% is carried out on charge, credit and debit cards. The overall spending pattern, however, has been witnessing a continuous shift from cash to cards, which presents a significant opportunity for the company. Considering the fact that the company has more than a billion credit and other payment cards in circulation worldwide, it is well poised to exploit this opportunity.

Threat

Intense rivalry within the existing players

DFS competes with other consumer financial services providers, including non-traditional providers such as financial technology firms and payment networks on the basis of a number of factors, including brand, reputation, customer service, product offerings, incentives, pricing and other terms. The credit card business is highly competitive. Some of the company’s competitors offer a wider variety of financial products, including automobile loans, which may currently position them better among customers who prefer to use a single financial institution to meet all of their financial needs. Some of the competitors enjoy greater financial resources, diversification and scale than DFS, and are therefore able to invest more in initiatives to attract and retain customers, such as advertising, targeted marketing, account acquisitions and pricing offerings in interest rates, annual fees, reward programs and low-priced balance transfer programs. In addition, some of the competitors have assets such as branch locations and co-brand relationships that may help them compete more effectively. Intense competition in the industry may impact the company's market share and operations.

Regulatory changes could limit profit expansion

As the volume of card-based payments has increased in the recent years, interchange reimbursement fee has become subject to increased regulatory scrutiny worldwide. It is widely believed that regulators are increasingly adopting a similar approach to interchange reimbursement fees, and, as a result, developments in any one jurisdiction may influence regulatory approaches in other jurisdictions. During FY2012, in accordance with the Reform Act, the Federal Reserve capped the maximum US debit interchange fee assessed for cards issued by large financial institutions at 21 cents plus five basis points, before applying an interim fraud adjustment up to an additional one cent. This amounted to a significant reduction from the average system-wide fees charged previously. The Federal Reserve has also promulgated regulations requiring issuers to make at least two unaffiliated networks available for processing debit transactions on each debit card. The rules also prohibited the company and issuers from restricting a merchant's ability to direct the routing of electronic debit transactions over any of the networks that an issuer has enabled to process those transactions. These regulations have negatively impacted the company's debit business in the US and associated revenues by creating negative pressure on its pricing, reduced the volume and number of the US debit payments processed, and diminished associated revenues. Such contemplated and likely legislative changes regarding interchange fees and related practices could have significant impact on the company's profitability.