CORNERSTONE ADVISORS

The Lifetime Value of a Student Loan Refinancing Relationship

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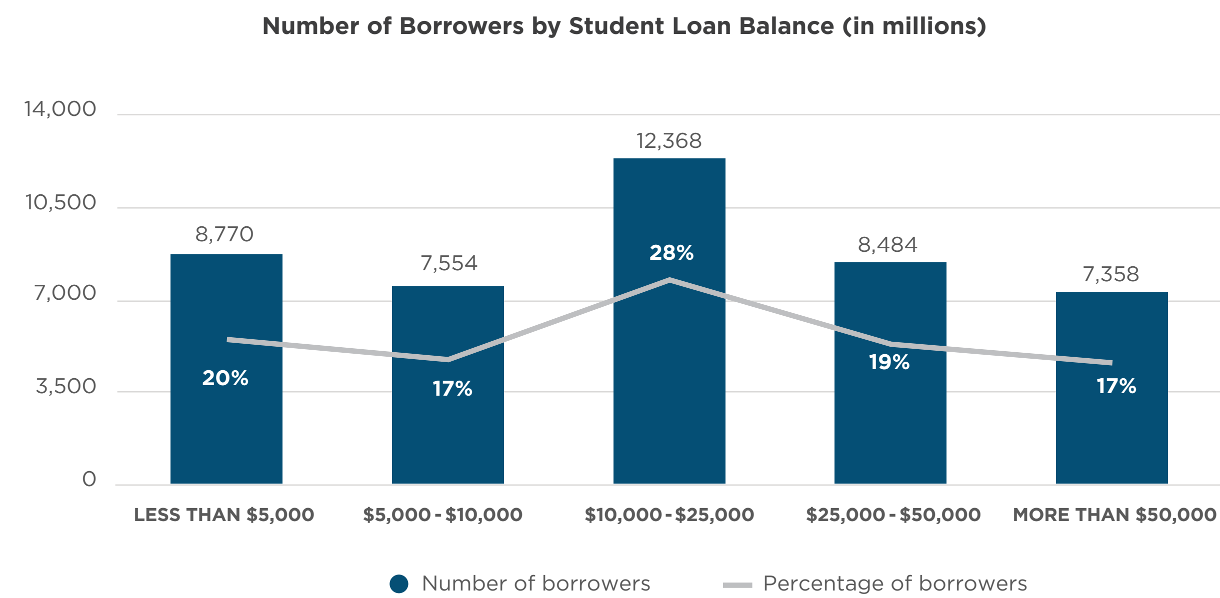
THE STUDENT LOAN REFINANCING MARKET

From a consumer perspective, statistics about student loan debt for U.S. consumers are scary: 1) total student loan debt exceeds $1.5 trillion, 2) one in five American adults — nearly 45 million people — have student loan debt, and 3) the average student loan debt amount is more than $37,000, resulting in an average student loan payment of almost $400 per month.[1] Overall, 17% — almost 7.4 million consumers — owe more than $50,000 (Figure 1).[2]

FIGURE 1: Student Loan Borrowers by Amount of Debt



Source: Make Lemonade

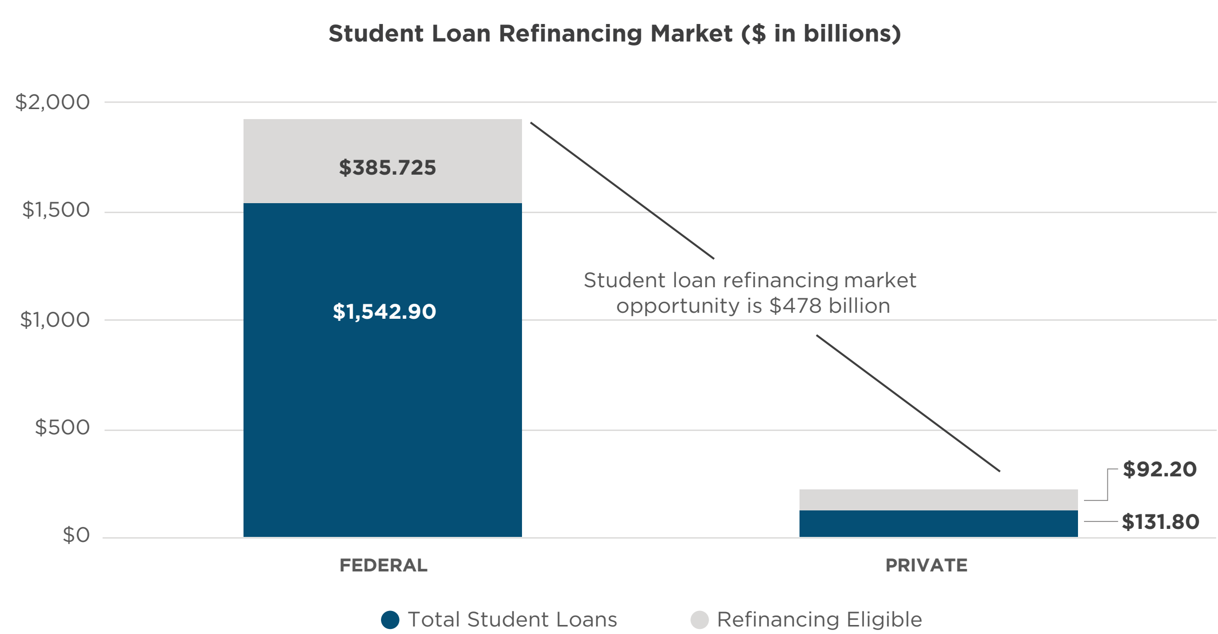
According to Make Lemonade:

> *"On a dollar basis, the highest increase in student loan debt is among 30 to 39-year-olds, who as a group now hold over $461 billion in student loans. On a percentage basis, the amount of student loan debt held by 30 to 39-year-olds has increased 30.2% over the past five years."*[3]

From a financial institution perspective, however, the statistics spell opportunity—not just because of the strong demand for student loans, but because of the need and demand for student loan refinancing. The consumer benefits to refinancing are clear: A study from Nitro found that refinancing student loan debt saves an average of $253 a month or $16,183 over the life of the loan.[4]

A study from Goldman Sachs estimates that 70% of private student loans and 25% of federal loans are "ripe" for refinancing.[5] Based on these estimates, the size of the student loan refinance market in 2020 is roughly $478 billion—$386 billion in federal loans and $92 billion in private loans (Figure 2).

FIGURE 2: Student Loan Refinancing Market



Source: Cornerstone Advisors What's Going On In Banking Study

Despite the numbers and estimates regarding defaults and deferments in the student loan market, the refinancing market paints a different picture as it relates to:

- **Charge-offs** — According to DBRS Morningstar: "Through Q1 2020, charge-offs in the student loan refi sector continued to be extremely low, reflecting high-quality borrower characteristics. While charge-offs will likely increase as a result of the coronavirus, borrowers will likely remain resilient because the majority of refi borrowers entered this national emergency with significant financial strength and are in professions that generally exhibit very low unemployment rates.[6]
- **Delinquencies** — Again, from DBRS Morningstar: "The factors driving low charge-offs in the student loan refi sector are also responsible for very low delinquency rates. While there has been some momentum in the increase of early-stage delinquencies (30+ days past due) over time, this is not a concern as delinquencies remain extremely low.[7]

A growing number of banks and credit unions see this market as an opportunity. According to Cornerstone Advisors' *What's Going On In Banking* study, the percentage of institutions in the student loan market increased from 40% to 55% between 2018 and 2020.[8]

Correspondingly, the percentage of institutions considering student lending a priority increased from 28% to 34% over the same period.

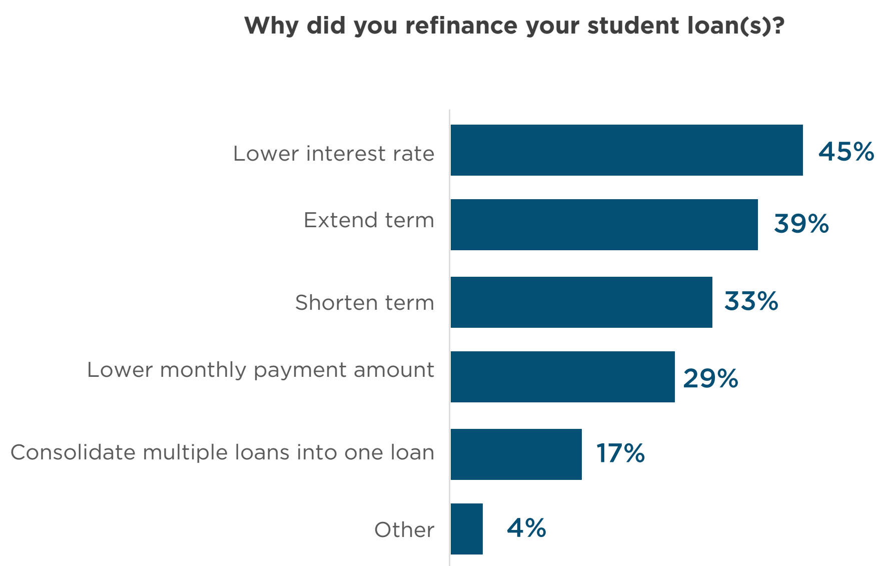
Banks and credit unions are waking up to the idea that student loan refinancing is the gateway product to access educated young adult borrowers entering their prime borrowing years. Strong demand isn't sufficient to get more financial institutions into the market, however. They need to see a path—and a relatively *quick* path—to profitability in order to enter the market or ramp up their efforts.

Based on the results of a July 2020 survey of 3,004 U.S. consumers and other consumer and industry data, this report looks at the market for student loan refinancing and develops a lifetime value model based on consumers' relationship activities following a refinancing of their student loan(s).

CONSUMER REFINANCING ACTIVITY

Over the past five years, roughly 13% of all consumers have refinanced at least one student loan, with 5% refinancing two or more loans. Nearly half were looking for a lower interest rate, but roughly four in 10 did so to extend the term of a loan, and a third did so to shorten the term (Figure 3).

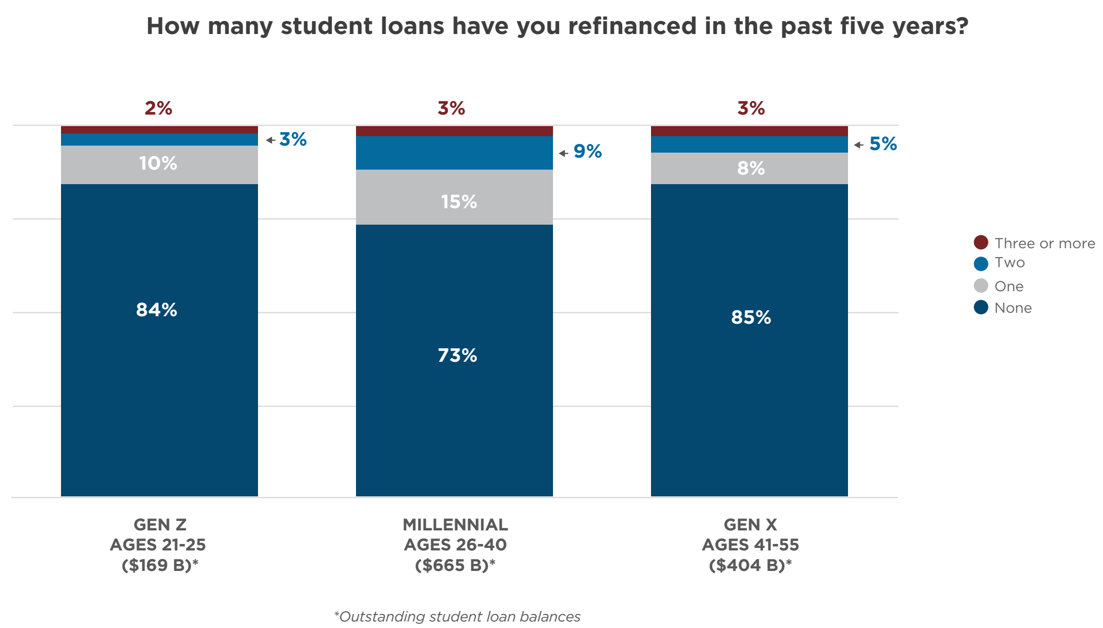
FIGURE 3: Reasons for Student Loan Refinancing



Source: Cornerstone Advisors survey of 3,004 U.S. consumers, Q3 2020

From a generational perspective, Millennials were the most active refinancers, with more than a quarter of them refinancing at least one student loan (Figure 4). Among Gen Zers, just 15% refinanced a student loan, but we expect that percentage to grow significantly over the next five years.

FIGURE 4: Student Loan Refinancing by Generation



Source: Cornerstone Advisors survey of 3,004 U.S. consumers, Q3 2020

Getting a lower interest rate was the most frequently cited reason across all generations. Nearly a fifth of Millennials, and one in five Gen Xers, however, said they refinanced in order to consolidate loans (Table A).

TABLE A: Reasons for Student Loan Refinancing by Generation

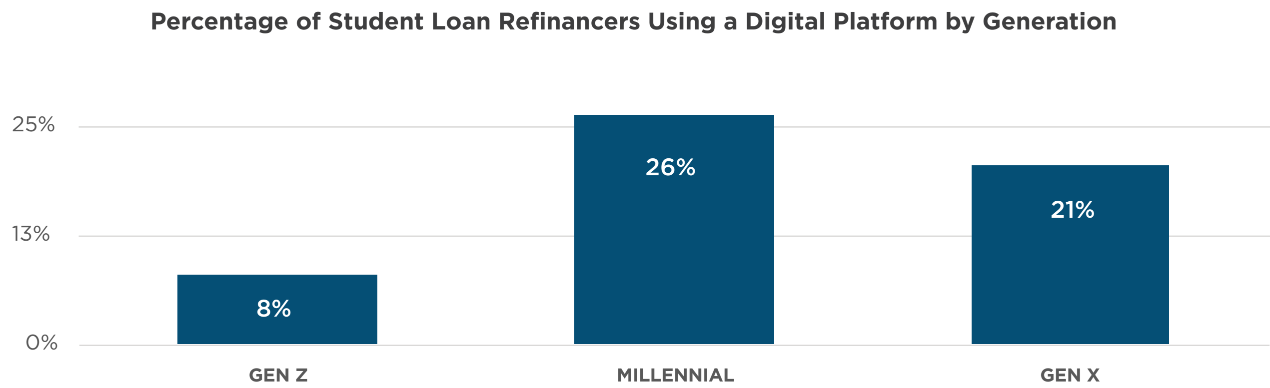
Why did you refinance your student loan(s)?

	Gen Z	Millennial	Gen X
Lower interest rate	41%	45%	49%
Reduce monthly payment amount	30%	32%	20%
Extend term	25%	42%	41%
Shorten term	18%	38%	34%
Other	14%	2%	2%
Consolidate multiple loans into one loan	5%	18%	20%

Source: Cornerstone Advisors survey of 3,004 U.S. consumers, Q3 2020

Overall, 53% of consumers refinancing a student loan did so directly through a bank or credit union. Digital student loan platforms, or marketplaces, were used by one in five Gen Xers and one in four Millennials to refinance a student loan (Figure 5).[9]

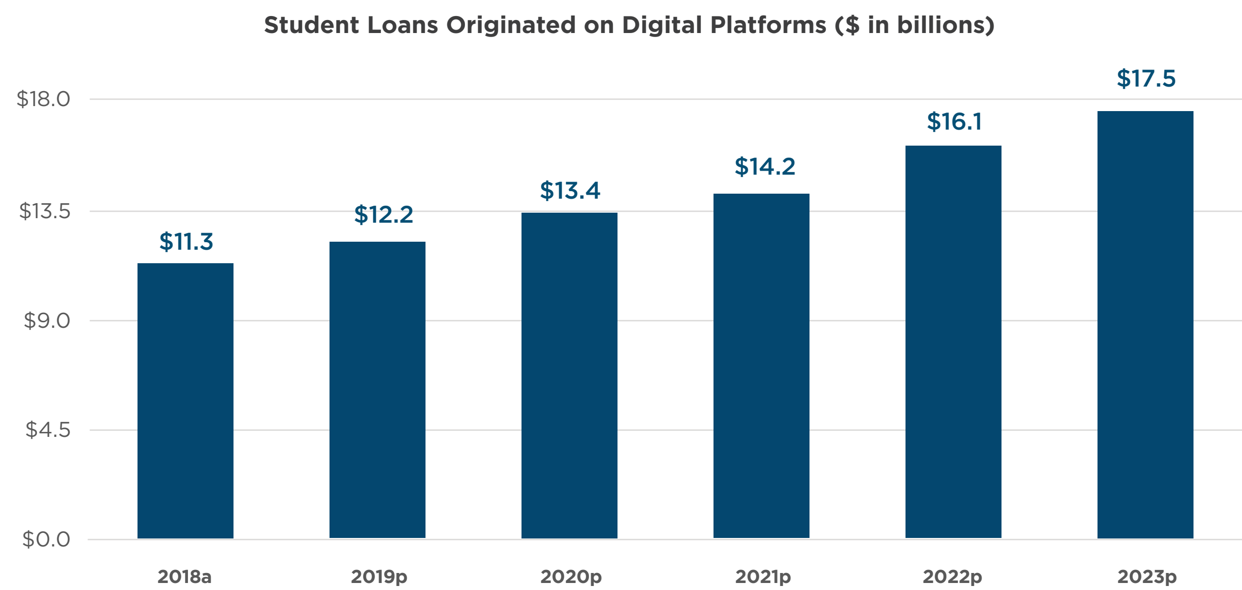
FIGURE 5: Use of Digital Platforms for Student Loan Refinancing



Source: Cornerstone Advisors survey of 3,004 U.S. consumers, Q3 2020

The use of digital platforms will increase as banks and credit unions continue to enter the online student loan refinancing lending space. S&P Global forecasts a 55% increase in student loans originated on digital platforms between 2018 and 2023 (Figure 6).

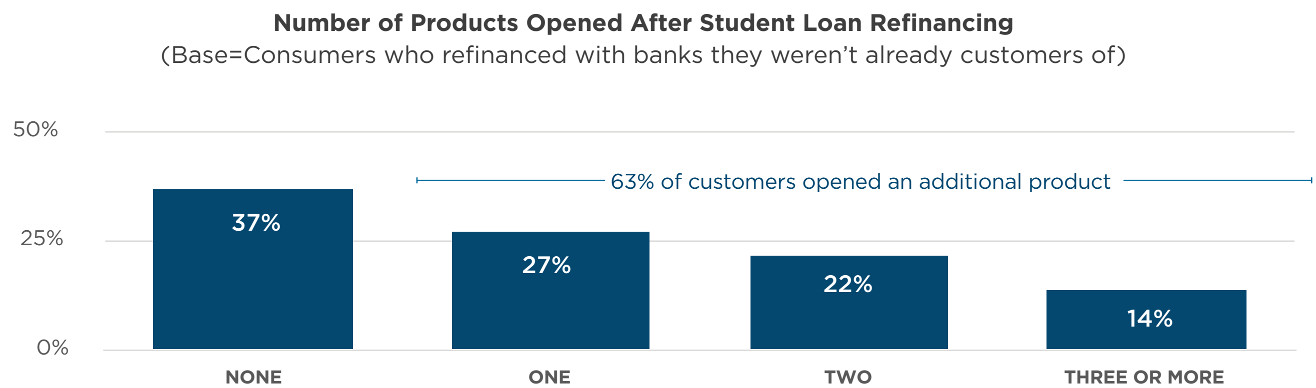
FIGURE 6: Student Loan Originations on Digital Platforms



Source: S&P Global

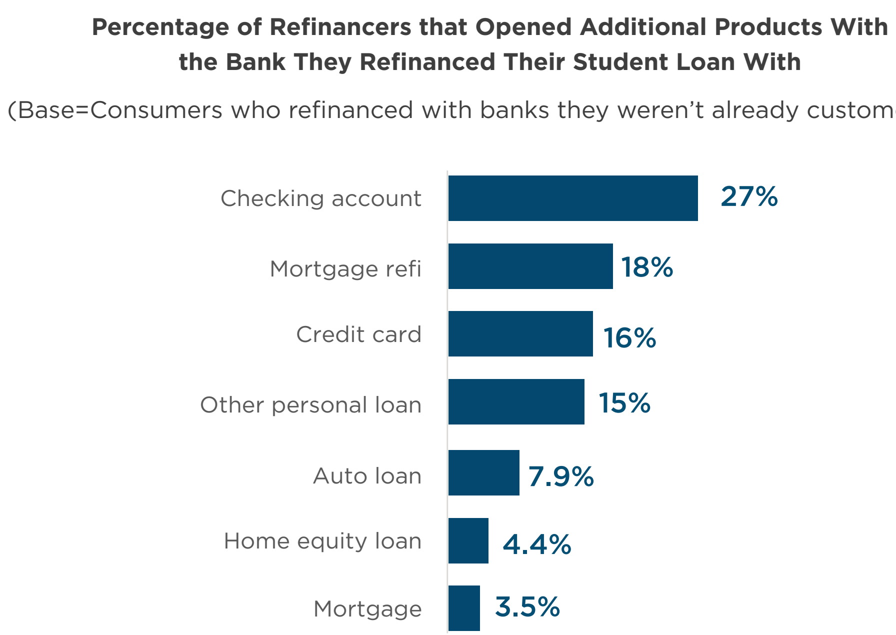
Among consumers who refinanced directly through a bank or credit union, 75% did so with institutions with which they were already customers. Among the other quarter, 63% went on to open at least one more product with that institution (Figure 7). Specifically, 27% opened a checking account, 18% refinanced a mortgage and 16% took out a credit card (Figure 8).

FIGURE 7: Number of Products Opened Following Student Loan Refinancing



Source: Cornerstone Advisors survey of 3,004 U.S. consumers, Q3 2020

FIGURE 8: Product Adoption Following Student Loan Refinancing



Source: Cornerstone Advisors survey of 3,004 U.S. consumers, Q3 2020

STUDENT LOAN REFINANCE LIFETIME VALUE

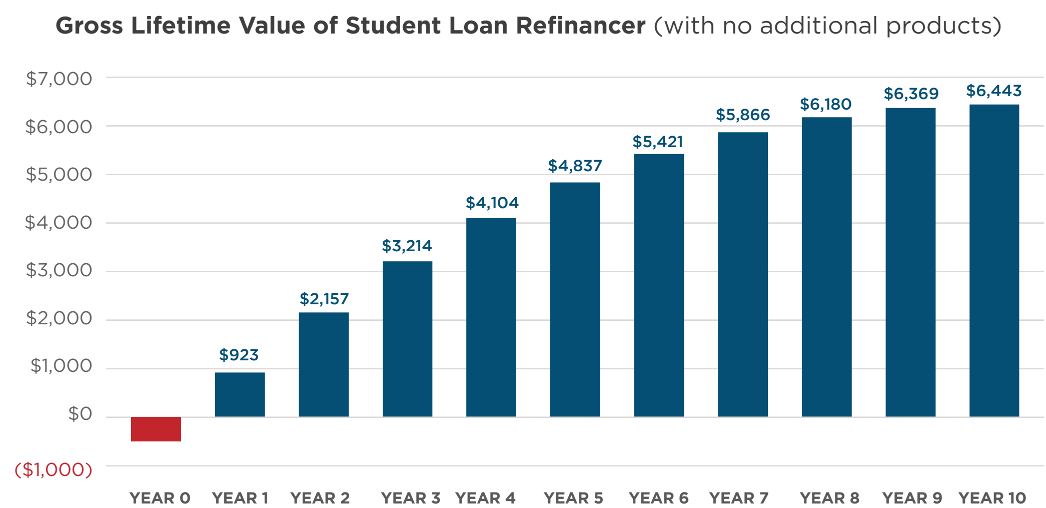
Based on the consumer survey and Cornerstone Advisors' industry benchmark data, we developed a customer lifetime value model to estimate the expected value of a student loan refinancing relationship over a 10-year period. For a list of the assumptions made in the model, see the Appendix in this report.

To model the student loan refinancing lifetime value, we created six scenarios based on the likelihood of a student loan refinancer opening additional products over the life of the loan:

1. No additional products beyond student loan 1 refinancing
2. Student loan refinancing plus checking account in year 1
3. Student loan refinancing plus checking account in year 1 and credit card in year 2
4. Student loan refinancing plus checking account in year 1, credit card in year 2 and personal loan in year 3
5. Student loan refinancing plus checking account in year 1, credit card in year 2, personal loan in year 3 and auto loan in year 4
6. Student loan refinancing plus checking account in year 1, credit card in year 2, personal loan in year 3, auto loan in year 4 and mortgage refi in year 5

The results of the model show that the discounted lifetime value of a student loan borrower who refinances $45,000 in student loans at 4% over 10 years and doesn't add any additional products is nearly $4,500, and $6,443 on a gross basis (Figure 9).

FIGURE 9: Lifetime Value of a Student Loan Refinancer



Source: Cornerstone Advisors survey of 3,004 U.S. consumers, Q3 2020

However, among student loan refinancers who refinanced with a financial institution that they didn't already have a relationship with, 63% went on to add more products with that institution.

For consumers that go on to add five additional products, the discounted lifetime value of that customer is almost $22,000 and nearly $38,500 on a gross basis. For a portfolio of 100 borrowers, the gross lifetime value is more than $820,000 based on a conservative estimate of the percentage of borrowers in each scenario (Table B).[10]

TABLE B: Student Loan Refinance Lifetime Value Model

Scenario	Lifetime value per customer (discounted)	Lifetime value per customer (gross)	Scenario distribution	Lifetime value per 100 refinancers (discounted)	Lifetime value per 100 refinancers (gross)
No additional products	$4,484	$6,443	37%	$165,899	$238,383
Add checking account in year 1	$5,118	$7,541	27%	$138,185	$203,607
Add credit card in year 2	$6,193	$9,388	22%	$136,245	$206,533
Add personal loan in year 3	$6,471	$9,779	11%	$71,177	$107,570
Add auto loan in year 4	$8,069	$13,080	2%	$16,139	$26,160
Add mortgage refi in year 5	$21,279	$38,497	1%	$21,279	$38,497
TOTAL	**$51,613**	**$84,727**	**100%**	**$548,923**	**$820,749**

Source: Cornerstone Advisors survey of 3,004 U.S. consumers, Q3 2020

Note that the model only considers the 10-year life of the student loan refi. Since many of the products are assumed to be purchased at staggered intervals later during the life of the loan, the actual lifetime value could be higher if: 1) the order of products added is different, or 2) additional products are added earlier in the relationship.

CONCLUSIONS

The alarm over the seemingly high level of student debt obscures two facts: 1) most student loan holders are able to make their monthly payments, and 2) the high level of debt translates into refinancing opportunities for financial institutions.

While fintech startups like SoFi make headlines for their student loan refinancing activity, roughly half of student loan refinancers refinanced through banks or credit unions—and many of them with institutions where they didn't have previous relationships.

Of consumers that refinanced with institutions where they had previous relationships, many added products after refinancing their student loans. But we can't necessarily attribute that cross-sell success to the refinancing event. Among those that refinanced with institutions where they didn't have previous relationships, however, additional relationship growth can be attributed to the student loan refinancing.

While the resulting overall lifetime value of a student loan refinancer is dependent on how well an institution cross-sells, over a 10-year period a pool of 100 refinancers could put more than $800,000 on an institution's bottom line.

The challenge for many mid-size institutions is how to profitably get into the market. The rise of digital student loan platforms is helping to address that. Beyond the obvious (but needed) support for lead generation, these platforms help financial institutions with:

- **Demand generation** — Hanging a sign that says "we offer student loan refinancing" isn't going to cut it for most institutions. Student loan platforms like LendKey attract student loan borrowers looking to refinance and help financial institutions enter the market faster and at a far lower cost than they could do themselves.
- **Loan origination** — Platforms' digital origination processes enable financial institutions to review electronic loan jackets and include electronic signatures, account verifications and automatic funds disbursements.
- **Credit decisioning** — Platforms can provide best practices for credit criteria and program guidelines that fit an institution's risk level and goals while allowing them to remain competitive.
- **Loan servicing** — Platforms typically service institutions' loan portfolios, including invoicing, payment processing and real-time reporting.

APPENDIX

Assumptions regarding product acquisitions costs; retention, interest and discount rates; and other additional product variables are listed in Table C.

TABLE C: Student Loan Refinancing Lifetime Value Model Assumptions

	Assumption	Value
Expenses	Acquisition cost (initial student loan refinancing)	$500
	Acquisition cost (per additional product)	$250
	Average cost of funds	0.75%
Products	Average student loan refi funded amount	$45,000
	Average student loan refi interest rate (fixed)	4.00%
	Student loan refi term (in years)	10
	Annual income per checking account	$168
	Annual interchange income per credit card account	$295
	Average personal loan funded amount	$10,000
	Average personal loan interest rate (fixed)	10.0%
	Personal loan term (in years)	3
	Average auto loan funded amount	$30,000
	Average auto loan interest rate (fixed)	4.50%
	Auto loan term (in years)	4
	Average mortgage refi funded amount	$150,000
	Average mortgage refi interest rate (fixed)	4.50%
	Mortgage refi term (in years)	15

Source: Cornerstone Advisors survey of 3,004 U.S. consumers, Q3 2020

About the Author

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Ron Shevlin is the director of research at Cornerstone Advisors where he leads the firm's fintech and consumer research efforts. Author of the book *Smarter Bank* and the Fintech Snark Tank on Forbes, Shevlin is ranked among the top fintech influencers globally.

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ABOUT

CORNERSTONE ADVISORS

Cornerstone Advisors delivers consulting services, industry insights and executive forums aimed at helping financial institutions improve their profitability and performance—quickly and efficiently. Armed with nearly two decades of experience, the philosophy that financial institutions can't improve what they don't measure, and an authoritative database of performance metrics and vendor contract data, Cornerstone can show banks and credit unions how laser-focus measurement can lead to more competitive business strategies, better vendor contracts, educated technology decisions and purposefully re-engineered processes.

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ABOUT

LENDKEY

LendKey delivers seamless technology, servicing and support that financial institutions need to establish a strong digital lending presence and build lifetime relationships with prime borrowers. Lenders optimize their offerings by drawing upon LendKey's demand generation, online decisioning and loan origination engines, loan servicing, compliance expertise and proprietary balance sheet options. Founded in 2009, LendKey works with hundreds of credit unions and banks that have collectively deployed over $4 billion in private student loans, student loan refinancing and home improvement loans. Visit lendkey.com/lend or email info@lendkey.com for more information.

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ENDNOTES

[1] https://www.nitrocollege.com/research/average-student-loan-debt

[2] https://www.makelemonade.co/student-loan-debt-statistics

[3] Ibid.

[4] https://www.nitrocollege.com/research/average-student-loan-debt

[5] https://www.nitrocollege.com/refinance-student-loans

[6] https://www.dbrsmorningstar.com/research/361920/dbrs-morningstar-student-loan-abs-update-q1-2020-performance

[7] Ibid.

[8] https://hs.crnrstone.com/banking-2020

[9] A digital lending platform is a mortgage point-of-sale tool that encompasses all components of the lending process from lead generation through rate lock.

[10] Our consumer survey found a higher percentage of borrowers adding products. For the purpose of the model, we changed the distribution to produce a more conservative estimate.

Have questions
about this report?

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