NOW IS THE TIME
The Compelling Case for Credit Union Mergers

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When it comes to credit union mergers, there has never been a better time than now to consider this possible activity as a strategic option for future growth and profitability. Pressure on margins, regulatory growth limits, eroding capital, upcoming changes in merger accounting rules, and the anticipated flood of retiring CEOs are all factors driving the increased need to merge now before the opportunity evaporates. Mergers can assist many credit unions in remaining viable while maintaining market share in an otherwise completely unfavorable operating environment.

The strategic case for merging currently healthy credit unions has never been more compelling. For many still well capitalized credit unions facing multiple reporting quarters of eroding earnings and limited prospects for growth, now is the time to negotiate the best merger deal. Once that capital erodes and the deposit base dwindles, so do the prospects for a Best of Breed Merger. In other words, for many credit unions if they do not merge now it won't be long before they are weakened to the point where they become a Regulatory Basket Case rather than an attractive strategic partner.

<u>Survival and Growth Strategies</u>

There are many reasons why credit unions are selecting merger as a survival and growth strategy, rather than relying on the often-too-slow growth capabilities fueled only by

retained earnings. Merging credit unions can often grow exponentially. The best strategic reasons to merge are well known:

- Asset and Member Acquisition
- Stronger Branch and Infrastructure Systems
- Product and Services Portfolio Growth
- Creation of Proactive Market Share Strategies

All of the above elements are needed due to the relentless competition from larger well-capitalized financial institutions.

Mid-Sized Credit Unions Have Unique Merger Opportunities

There are some observers of the credit union industry who have the misperception that only small credit unions need to merge. Although credit unions under $100 million in assets should certainly give the merger strategy serious consideration, it is the mid-sized credit unions between $100-500 million in assets that have the most to gain from consolidation. Smaller credit unions can often compete as niche players and large credit unions over $500 million can leverage economies of scale to be a significant market player. Mid-sized credit unions, especially community credit unions and those serving multiple employee groups, often under perform due to the double-whammy of the lack of niche and the lack of scale. Since shrinking the credit union to be a niche player makes no sense, the mid-sized credit union should seek other mid-sized credit union merger partners in order to establish a sustainable market presence.

In-Market Expansion

DPS Credit Union in Denver, CO is a good illustration of a credit union using mergers as a strategic tool. The mid-sized credit union, which was primarily serving a single sponsor employee group with one location, decided that it needed to diversify to ensure survival and growth. It analyzed its strengths…excellent service, value pricing, and a full range of product offerings, as well as its weaknesses…the lack of convenient locations and the lack of diversity in its membership base. The strategic solution was found through two mutually beneficial mergers with two other mid-sized Denver area credit unions that brought multiple branches, healthy core deposits, competent additional staff, and metro community-wide membership eligibility to the new organization. The two merging credit unions gained economy of scale and expanded service offerings. When the currently pending merger is completed, the new conglomerate credit union will jump from the sixth largest credit union in Colorado, prior to the mergers, to the third largest and will soon surpass $1 billion in assets.

Multiple State Efforts

Another mid-sized credit union located in the mid-west that prefers to remain anonymous, realized that to remain relevant to its members and stay competitive in the marketplace it needed to at least triple its size to become a half-billion-dollar credit union within three-to-five years. Mergers were the only way the credit union could accomplish this growth objective within the designated time frame. The credit union currently operates branches in three states and intends to expand those markets. In addition, it is assertively seeking mergers with credit unions $50 million in assets and larger in over a

dozen specifically targeted markets within major metro areas that have high growth potential. This is certainly not a timid strategy and is illustrative of a new breed of credit union managers and board members who are not afraid to have a giant growth and profitability vision for their institutions.

Proactive Strategy a Must

Regardless of size, every credit union will benefit from a customized, proactive Capital and Asset Growth Merger Strategy. These strategies should include a specific definition of what makes a good merger candidate and a detailed laundry list of what the merger-seeking credit union brings to the table. The strategy should identify specific targeted merger partners that have desirable membership growth potential and infrastructure characteristics located in highly promising markets. The strategy should identify what the credit union is willing to do within a merger in terms of governance, management, employee retention, infrastructure, and financial incentives that will be needed to get the deal done. The strategy should also contemplate the myriad factors inherent in a merger such as technology issues, regulatory compliance, media relations, corporate culture assimilation, and operational integration.

For many credit unions, growth through merger is a strategy that promises a thriving future, not just a surviving future. The current marketplace factors driving credit union mergers are compelling and the window of opportunity is wide open. Smart credit unions will act now before that window closes.

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