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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 slips away. Mergers can assist many credit unions in remaining viable while maintaining market share in an otherwise completely unfavorable operating environment.

Today there are approximately 8,000 credit unions, down from 10,000 plus six to seven years ago. Looking ahead to the year 2015, most estimates place the number of credit unions at near the 5,000 number - a 38% decrease in the number of active institutions.

In addition, member growth over the past three years has averaged less than 1% for all credit unions with the smaller credit unions (under $24 million in assets) actually recording a decrease of 0.71%. During the same three year period, $1 billion plus organizations grew at a rate of 4.89%.

<u>Survival and Growth Strategies</u>

There are many reasons why credit unions are selecting mergers 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.

There are some observers of the credit union industry who have the misperception that only small credit unions need to merge. Although credit unions with under $100 million in assets should certainly give the merger strategy serious consideration, it is the mid-sized credit unions with 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 with over $500 million in assets can leverage economies of scale to be significant market players.

Mid-sized credit unions, especially those with community charters, often underperform due to the lack of niche positioning plus the lack of scale and capital. Since shrinking a credit union to become a niche player makes no sense, the mid-sized credit union should seek to join other mid-sized or larger credit union partners in order to establish a sustainable market presence.

In-Market Expansion

The following is a typical example of a mid sized West Coast credit union that used mergers as a strategic expansion tool. The credit union, 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 created through mergers with two other smaller area credit unions that brought multiple branches, healthy core deposits, and community-wide membership eligibility to the new organization. The merging credit unions gained economies of scale and expanded service offerings. Not more than a year following the merger, the new conglomerate was close to recording the $1 billion mark in assets.

Multiple State Efforts

Another successful merger example was that of a mid-sized credit union located in the Midwest that realized it could remain relevant to its members and stay competitive in the marketplace but needed to at least triple its size to $500 million in assets. Mergers were the only way the credit union could accomplish this growth objective within the desired three to five year time frame. The credit union now operates branches in three states and intends to expand regionally within those markets. In addition, it is seeking mergers with credit unions with $50 million in assets and larger in a dozen specifically targeted markets 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 achieve healthy growth and profitability through mergers.

Proactive Strategy a Must

Regardless of size, most credit unions will benefit from a customized, proactive capital and asset growth merger strategy. The strategy should include a specific definition of what constitutes a good merger candidate along with a laundry list of what the merger-seeking credit union brings to the table. The strategy should also identify what the credit union is willing to do in terms of governance, management, employee retention, and financial incentives that will be needed to achieve its objective. The strategy should also contemplate the myriad of factors inherent in any merger such as technology issues, regulatory compliance, media relations, corporate culture assimilation, and operational integration.

GRFI has a question and answer merger checklist that is available with no obligation for credit unions wanting to explore various options prior to formally identifying mergers as a strategic consideration for the future of their organization. Please contact Christine Gibney at cgibney@grfiltd.com or 312-856-1444 to reserve a copy of the checklist.