Credit Union Directors NEWSLETTER

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Build successful fintech partnerships

Embrace the innovative opportunities these collaborations offer.

It is an exciting time to be part of financial services in general and the credit union movement specifically.

The industry is undergoing one of the greatest revolutions in our history. It's a time of monumental change and, along with it, incredible opportunity.

The pace of change continues to increase with new technologies and solutions emerging that shift consumers' demands and make it difficult for credit unions to compete.

Consider the evolution of auto purchasing and financing. Consumers can now go through the entire car-buying process online without ever stepping foot in a dealership.

As we continue to move into these digital ecosystems, the touchpoints where the customer potentially completes a financial transaction or selects a specific lender will be earlier in the buying experience. So it's critical for lenders to be online and visible, and to engage with customers early on in their buying experience.

Between big banks, fintechs, and an ever-changing environment, one thing is clear: Credit unions need to innovate in ways they haven't had to in the past. To keep our system strong, we need to embrace new opportunities rather than fight them.

Credit unions can level the playing field through fintech partnerships. For too long, credit unions shied away from embracing this opportunity and viewed fintechs as the enemy.

CUNA Mutual launched CMFG Ventures in 2016 to bring emerging technologies to credit unions. The new technologies many fintechs offer need to get into the hands of credit unions and the middle-class Americans we serve.

We talk to fintechs every day that are excited about working with credit unions. They recognize the incredible member base credit unions have and our movement's mission.

Just like credit unions can grow by tapping into fintechs, fintechs can further their business by working with credit unions. It's an incredibly complementary relationship.

> "**WE NEED** to embrace **NEW OPPORTUNITIES** rather than fight them."
>
> Brian KAAS

But where do you start? Consider taking these steps to begin the process:

▶**Vet opportunities thoroughly.** Complete a full evaluation of the fintech partnership. Talk to their customers and review the company's financial health and investors.

▶**Define success.** Establish success metrics so you can set expectations from the start.

▶**Collaborate.** Create a dedicated team focused on the partnership's success.

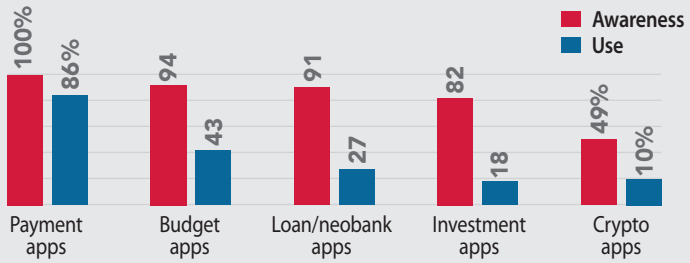
▶**Start small.** Use pilots or targeted rollouts before scaling up with a partner and seek continual feedback from your staff and members.

QUICK TAKE for your next board meeting

Awareness high but use of fintech apps lags

While most people are aware of fintech apps for payments (100%), budgeting (94%), lending/neobank activities (81%), and investments (82%), they're not all using these apps, according to Fiserv's "Expectations and Experiences" consumer trends research.

Awareness and use of fintech apps



Source: Fiserv Expectations and Experiences report

▶**Join the new Fintech Forum.** This new community allows credit unions to connect directly with fintechs, learn about new technologies, and talk with colleagues about their experiences.

Credit unions are a tight-knit community. We take pride in the work we do and keep our mission at the center.

By bringing more fintech partnerships into the credit union system, our industry can remain strong and competitive while better serving members.

BRIAN KAAS *is president and managing director of CMFG Ventures, the venture capital arm of CUNA Mutual Group.*

Cybercrime and digital advancements among top risks

Innovation is key to credit unions' continued prosperity.

Cybercrime, digital advancements, and a reliance on wholesale funding are among the biggest risks facing credit unions, according to two risk professionals.

Fabiana Burkett, vice president, enterprise risk management, at $2.2 billion asset Orange County's Credit Union in Santa Ana, Calif., and Shaundra Warren, senior vice president of risk mitigation at $1.8 billion asset Sharonview Federal Credit Union in Indian Land, S.C., provide insight into the risks credit unions should watch in 2022.

Q: What are the biggest compliance and risk issues credit unions face?

Burkett: Cybercrime is one of the major risks credit unions are facing today. Cyberattacks, which are becoming more sophisticated and frequent, can be costly and seriously damaging to a credit union's reputation.

Implementing and maintaining robust cybersecurity programs will help prevent breaches and allow for quick response when incidents occur, mitigating the impact.

> "We can be too risk averse rather than mitigating risk and taking on new opportunities."
>
> Shaundra Warren

Other concerns are the fast advancement of digital technology, automation, artificial intelligence, and the evolving competitive landscape. Tech giants and other entities are starting to blur the definition of a financial institution.

To continue to prosper, credit unions must innovate while staying true to our core values as member-owned cooperative financial institutions. Partnering with fintechs can be a solution. But vetting these companies well and evaluating the risks involved with such alliances—especially compliance risk—is key.

Additionally, our political environment has created a new regulatory climate which may lead to increased regulatory burden on credit unions, especially around consumer protection laws. That will create higher compliance costs which, especially for smaller credit unions, threaten our ability to lend and operate.

Warren: Reliance on wholesale funding is another risk. We continue to look for ways to reduce our reliance on wholesale funding.

The risk relating to wholesale funding is in the pricing. Brokered deposits are often more expensive than organic deposits, leading to a rising cost of funds and squeezing of the credit union's net interest margin.

We're forward-thinking and looking at new opportunities, new channels, and opportunities to bring in new revenue.

The economic markets continue to change, and that will affect rates and borrowing.

Q: What are future risks that should be on credit unions' radar?

Burkett: Credit unions need to pay close attention to the developments around digital currency and decentralized finance. They have the potential to displace traditional financial solutions by becoming easier to use, and they have bigger players adopting them.

Q: What advice would you offer other risk leaders?

Warren: Understand the business and the organization. We can be too risk averse rather than mitigating risk and taking on new opportunities.

Be a part of building the infrastructure that supports mitigating risk. Be in the know, have a seat at the table, and have great relationships.

That's paramount in any leadership role, but it's more important in risk mitigation.

Have relationships so people understand what you're trying to do and why it's important to have policies, procedures, and mitigating factors to prevent any real detrimental impact.

Credit Union National Association
CUNA

AVAILABLE THROUGH SEPTEMBER 11, 2022

Adapt strategic plans with insights from current industry trends

CUNA

Trends into Action

eSchool (RECORDED)

At CUNA Trends into Action eSchool (recorded), credit union leaders and board members will learn about four key industry trends important for consideration as they engage in strategic planning.

The content and trends covered, compiled from the 2021-2022 CUNA Environmental Scan, address the current industry environment. Board members will receive expert analysis of how current trends may evolve and ways to plan for those possibilities.

cuna.org/trendseschool

Credit Union National Association
CUNA

AVAILABLE THROUGH
JUNE 6, 2024

Build a solid knowledge of credit union financials

CUNA

Credit Union Finance for Boards & Committees

eSCHOOL (RECORDED)

Board and committee members who are looking to gain a better understanding of their financial responsibilities at the credit union and want to satisfy their NCUA requirement for financial literacy should attend this 6 session eSchool.

By attending, board members will also leave with the CUNA Credit Union Board Financial Literacy Certificate.

cuna.org/cufeschool

2022 economic forecast: 3 factors to consider

Public health challenges will ease, but uncertainty persists.

Three key factors will shape the 2022 economy, according to Mike Schenk, CUNA chief economist and deputy chief advocacy officer: the pandemic, labor markets, and inflation.

First, the coronavirus isn't going away, he says. "Public health professionals tell us we'll be talking about variants for a long time into the future."

Significant increases in cases slow economic activity, intensify labor market dislocations, and disrupt supply chains, leading to inflationary pressures.

"It's no surprise that fewer economists are talking about 'transitory' inflation," Schenk says.

Initial indications are that the omicron variant may be more contagious but less dangerous and with fewer hospitalizations and deaths. That has implications for CUNA's forecast.

> "Significant increases in coronavirus cases slow economic activity, intensify labor market dislocations, and disrupt supply chains, leading to inflationary pressures."

CUNA economists dialed back their expectations on overall economic growth with the onset of the delta variant, dropping the outlook for U.S. gross domestic product (GDP) growth by roughly one percentage point to 5.3% in 2021 and 4.5% in 2022.

They may revise their 2022 outlook to 4% GDP growth due to the rise of the omicron variant. Still, that's well above the 2.8% long-run average growth rate, Schenk notes.

Labor markets

The unemployment rate, despite some concern about people's willingness to work, remains an overall economic strength, Schenk says.

"But omicron may slow the improvements we've seen recently, with front-line workers especially hesitant to return to their jobs," he says, both in the U.S. and globally.

The resulting slower income gains and rising uncertainty likely will translate to less spending and more saving, creating an expectation of softer demand relative to previous outlooks, Schenk says.

By extension, softening labor markets would put more strain on supply chains.

That would result in continued higher prices for goods and services, crimping consumers' spending power.

Supply-chain difficulties, however, won't likely be as prevalent or as impactful by mid-year 2022, Schenk says.

He bases that prediction on an October 2021 survey conducted by *The Wall Street Journal* of 67 economists. Nearly 60% of respondents predicted supply-chain disruption will largely recede by the third quarter.

Inflation

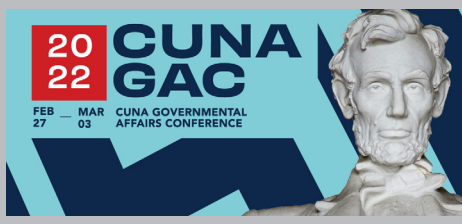
CUNA economists believe headline inflation will ease to about 3.5% in 2022 after increasing to 7.0% in 2021.

However, the Federal Open Market Committee (FOMC) announced it will end its quantitative easing program by the end of March 2022 in response to high inflation. Through this program, FOMC purchased billions of dollars in Treasury securities and mortgage-backed securities to stimulate the economy.

"As demand for those securities goes down, upward pressure will be put on long-term interest rates," Schenk says. "That will almost certainly affect demand for first mortgages."

The Mortgage Bankers Association's baseline forecast reflects a nearly 40% decline in total mortgage originations in 2022, he adds. "If that happens it will hit many credit unions hard."

Resources



CUNA Governmental Affairs Conference, Washington, D.C., Feb. 27-March 3: *cuna.org/gac*

CUNA board and committee solutions: *cuna.org/board*

CUNA Board of Directors Community: *community.cuna.org*

CUNA Mutual Group: *cunamutual.com*

Replacing noninterest income

Use long-term planning to find ways to create new revenue streams.

Many credit unions want to adjust their revenue sources and ease the pressure on potentially lost income streams such as overdraft fees, nonsufficient fund fees, interchange income, and mortgages.

Threats to noninterest income are nothing new, says Tony Hildesheim, chief operating officer of $6.7 billion asset Redwood Credit Union in Santa Rosa, Calif. He says credit unions should use long-term planning meetings to examine how to drive efficiency or create new avenues of revenue.

"Anyone who hasn't been under a rock knows that the big pressure coming right now is overdraft protection and nonsufficient fund fees," Hildesheim says. "Look at your main sources of revenue and ask, 'What happens if that goes away or gets threatened? What else do we have? And how else can we serve our membership?'"

Hildesheim addressed a CUNA Councils virtual roundtable "Potential Solutions for Pressure on Noninterest Income."

Rob Johnson, president of c. myers, advises credit union leaders to examine their exposure to legislative changes, rising inflation, and the prospect of the federal government offering digital currency. He also urges credit unions to take steps to prepare for those scenarios.

"For the last decade, we've run long-term simulations of what could happen if noninterest income got materially reduced," Johnson says. "How do we diversify our reliance away from this?"

Thirty-two percent of credit union revenue is from noninterest income, says Johnson, which makes it essential for credit unions to adapt, diversify, and find sustainable earning solutions.

Financial institutions must think from a member perspective and appeal to consumers to create lasting solutions. Johnson advises credit unions to evaluate their products and services and determine how a digital version would compare to the in-person experience.

If members value a service, such as unlimited overdrafts, they'll be much more willing to pay a fee and view it as beneficial rather than a penalty.

A credit union's messaging goes a long way in shaping how members view services. However, Johnson stresses it's important to follow through on that message.

"What is the purpose of the fee?" Johnson asks. "Decision-makers often look at fees solely from a financial perspective versus whether members benefit."

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Rob Johnson

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