OLIVER WYMAN

Financial Services

ORGANIZING FOR EFFECTIVENESS AND GROWTH IN COOPERATIVE FINANCIAL SERVICES

A FOCUS ON THE AMERICAS

MARSH & McLENNAN COMPANIES

FOREWORD FROM THE INTERNATIONAL SUMMIT OF COOPERATIVES

We would like to thank Oliver Wyman for their focus on cooperative financial services in the Americas. This pioneering report complements three previous Oliver Wyman studies focused on of the European cooperative banking sector, and its publication is timely as international stakeholders seek to understand better the organizational challenges, dynamics, and opportunities this sector represents. In contrast with Europe, where cooperative banking has a significant market share (and in some countries is the majority of the banking industry), cooperatives in the Americas typically account for a smaller proportion of both deposits and loans, and are systemically less important than their shareholder counterparts. Nevertheless, across the Americas, cooperative banks and credit unions have a significant – and, this report argues, growing – role to play given the natural synergy of cooperative values, member service, and community development. We welcome the fact that the study challenges the conventional wisdom of growth and organizational effectiveness in the sector and seeks to identify practices that will enhance the relevance and sustainability of the cooperative model. Ultimately, we believe these will help to ensure broad access to the financial system by all.

SUZANNE GENDRON

Managing Vice President
Cooperation and Corporate Affairs
Desjardins

STÉPHANE BERTRAND

Executive Director
International Summit of Cooperatives

ACKNOWLEDGEMENTS

Oliver Wyman acknowledges the industry executives and other stakeholders who contributed their perspectives and served as a sounding board in helping formulate our hypotheses throughout this project. Their willingness to share their views is a testament to the collaborative nature of the cooperative movement. Background research provided by Oliver Wyman's Celent business unit helped paint the macro context of the industry. We also thank our academic partner, the International Observatory on Financial Services Cooperatives (IOFSC), for its conceptual input and data contributions, and for having facilitated access to many of the institutions that took part in the project. The IOFSC, part of HEC Montréal, is an initiative of the Desjardins Centre for Studies in Management of Financial Services Cooperatives and aims to contribute to the development of the scientific analysis of financial services cooperatives and their environment by providing academic and institutional researchers access to existing knowledge and relevant data.

EXECUTIVE SUMMARY

Oliver Wyman set out to identify the organizational levers that cooperative banks can and should use to optimize their performance. Our methodology involved primary interviews with credit union and cooperative banking executives and other senior stakeholders from Canada, the United States, and Latin America, and leveraging Oliver Wyman industry analyses and Celent research.

To begin, we establish the strategic case for growth in the cooperative financial services' agenda by examining market penetration, resiliency, and other factors. Our focus next turns to the ways in which these agendas take shape through organizational design and decisions at the individual cooperative and sector level, the extent to which prevailing organizational practices aid or hinder the pursuit of an effective growth agenda, and the key dimensions of an organizational blueprint that will best enable financial cooperatives to achieve their goals.

This report addresses five key questions:

1. Does structure matter?
    - A. Overall, the functional organizational structures across coops tend to be fairly uniform, without a lot of experimentation or variation from one to the other.
    - B. Relatively few cooperative banks deploy senior executives in growth-oriented roles such as strategy/organization, sales, and innovation.
    - C. In situations where such roles do exist, positions tended to be staffed by more junior managers, suggesting less decision-making authority than in shareholder-owned institutions.
    - D. A scarcity of "Chief Operating Officer" roles in the sector suggests that many CEOs become de facto heads of operations and consequently have less time to devote to their organizations' strategic agenda.
    - E. While facing the same intensive cost pressures as the rest of the banking industry, coops' staffing may need to flex in the short-to-medium term in order to pursue strategic growth imperatives aligned with the cooperative mission.

    Many organizational structures can work, but there are steps coops can take with respect to their organization to address opportunities in the banking sector.

2. Is the underlying strength and health of membership a key differentiator?
    - A. Membership criteria have a major influence on financial sustainability and the potential for growth.
    - B. Managing demographics and the needs of specific segments is critical, since coops increasingly must adopt a full lifecycle view of their member base.
    - C. Membership culture influences whether and how the inherent cooperative promise is delivered.

    The underlying fundamentals of membership greatly influence a cooperative's trajectory.

3. Are coops that innovate more around the member experience better able to differentiate their products and services?

   A. While many cooperatives have a concerted innovation agenda, they also tend to adopt a “me too” product and features strategy – truly differentiating initiatives are few and far between.

   B. The level of ambition to innovate depends highly on in-house capabilities.

   C. Coops are focusing innovation on channel mix to contain costs and serve convenience-conscious members, but they ignore the “high touch” and community value of their physical networks at their peril.

   While high-performing coops are able to deliver leading-edge initiatives, most have significant untapped potential for innovation that they could develop through dedicated organization structures, better capabilities, and more focused execution.

4. Does the approach to talent (selection, on-boarding, retention, development, etc.) translate to greater effectiveness and growth?

   A. Smaller cooperatives tend to have CEOs with longer tenures and are less likely to hire those with past shareholder experience.

   B. Higher growth rates tend to be associated with cooperative CEOs who have past shareholder bank experience; lower profitability rates tend to be associated with those with longer tenures.

   C. For hires at the operational level, relationship skills have become the critical ingredient for a successful member experience and for moving cooperatives beyond traditional transaction banking.

   Hiring choices across the organization have a critical effect on performance as coops seek to integrate additional growth and member-service initiatives into the execution of their activities.

5. Does the role of governance affect organizational agility?

   A. Cooperatives employ a variety of governance constructs and interaction models to embody the core value of member ownership.

   B. Board composition and the nature of the interaction with executive management affect the degree to which a strategic agenda can be articulated and executed.

   C. Suboptimal governance can be a threat to both management effectiveness and the growth trajectory, and in some cases significantly hindering the future viability of the institution.

   D. Associations and league structures could be optimized to deliver greater value to the sector.

   Governance choices can hold back a cooperative, or contribute to its agility.

From these core findings, we are able to shine a spotlight on the key organizational levers that cooperatives can use to influence their future success. Regardless of their individual circumstances, we believe all financial services cooperatives stand to gain by progressing on the following five dimensions of organizational effectiveness:

Optimize member management

- Streamline governance and decision-making
- Emphasize member information management and lifetime profitability analysis
- Apply a growth-oriented lens to future membership

Improve employee bench strength

- Rotate talent, e.g. through inter-coop secondments
- Acquire better outside talent from the broader banking, retail, and tech sectors
- Use training as a competitive differentiator

Champion relevancy by rethinking convention

- Rethink long-held precepts regarding channel strategy
- Infuse a ubiquitous culture based on "value with values"
- Plan around next generation banking needs
- Evangelize the commercial benefits of cooperative values

Turbocharge collaboration

- Accelerate the systemic sharing of best practices
- Revisit and revise the role of associations and centrals
- Cooperate more in the market to help the overall coop banking sector win

Build an innovation engine

- Innovate based on a better understanding members' needs...and their current hassles
- Adopt "breakthrough" goals and measure achievement against them
- Create a diversified portfolio of innovation, since no one has a monopoly on the next big thing

These findings have important implications for the ways cooperative banks organize, deal with their members, source talent, and work both individually and in unison to innovate and grow. They also begin to outline the emerging imperatives for cooperatives in re-evaluating their organizational blueprints for the future. First, cooperatives need to be intentional about their purpose. Their field of vision should encompass growth and effectiveness, emphasizing sustainability at all levels. They also need to renew their focus on innovation as a prerequisite for relevancy and incorporate member service and innovation needs into their business and talent strategies.

Second, cooperatives face imperatives concerning their organizational structure. They should help the CEO chart a growth trajectory by hiring growth-focused staff. Simultaneously, cooperatives should aim for levels of employee efficiency seen at shareholder banks by establishing comparison benchmarks based on their best performing profit-oriented peers.

Next, it is important that the right governance processes are in place. Coops should optimize board operations by professionalizing member representation through qualification requirements, setting guidelines for consultation and communication, and adjusting committee structure to focus on current needs rather than past events. The board and management should also measure and track execution against growth-oriented metrics to ensure a focus on future viability as well as current performance.

Resources must be allocated deliberately for growth and effectiveness. Planning and budget cycles should have protected tracks for growth and innovation initiatives, and institutions should have a longer-term growth-focused orientation for managing retained earnings. For new initiatives, a “build versus buy versus partnering” decision should be undertaken deliberately, strategically, and without preconceptions.

The management model should introduce growth objectives and performance incentives throughout the cooperative, increase the role of the center in decision making, and provide coaching for managers to become more entrepreneurial.

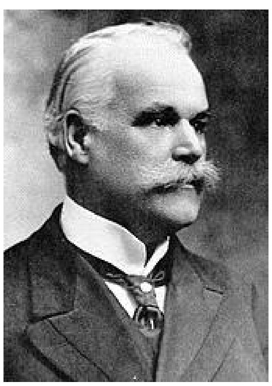
Next, people, talent, and human capital issues are important. Institutions should formalize bi-directional training exchange programs between coop banking entities. To enrich debate and discussion at the senior table, key growth-oriented roles should be tapped from non-traditional sources, and hires and promotions should be based not only on traditional skills but also on growth-culture fit. Coops should also experiment more with role rotation to ensure a diversity of perspectives on key issues.

Beyond these more formalized initiatives, the informal organization also makes a difference. Both strategic and operational decision-making bodies should be encouraged to adopt an entrepreneurial mind-set on behalf of their members. Additionally, the CEO should allocate – and be seen to allocate – bandwidth to growth-oriented responsibilities and initiatives, while rooting out pockets of stagnation or negative culture through regular temperature checks and the clearing of long-standing issues.

We recognize that Canada, the United States, and the 32 countries of Latin America and the Caribbean all comprise substantially different cooperative banking sectors, in distinct types of economies and in particular growth contexts. However, we find that our conclusions set out above – focused on organization – remain broadly relevant regardless of geography, in guiding cooperative banks, large and small, to position for long-term success and effectiveness, while retaining their defining values.

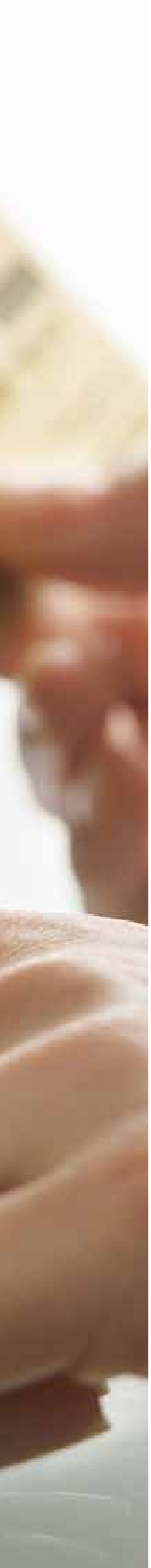
TABLE OF CONTENTS

“Association is the ultimate lever of strength. It’s a truth as old as man himself, but it’s far from being fully understood by all.”



Alphonse Desjardins
L’union des forces sur le terrain économique
La Vérité, September 24, 1910

Progressive coop banks are reshaping their channel mix to cater to their members' needs.



1. INTRODUCTION

1.1. ABOUT THE STUDY

Financial services cooperatives (primarily defined as cooperative banks[1] and credit unions) exist across the Americas. The industry panorama is both varied and dynamic, and the relevance of coops is growing in some countries while waning in others. Throughout the region, these coop entities operate within vastly different macro-economic, regulatory, and competitive environments. The result is a kaleidoscope of challenges, maturity levels, and future outlooks.

Within this context, we set out to identify the organizational levers that cooperative banks can – and should – use to optimize their performance. More precisely, we were interested in understanding the positioning of growth in the strategic agenda and how those agendas took shape through organizational decisions at both the individual coop and sector levels. We were also interested in the extent to which prevailing organizational mantras may hinder coops' ability to effectively pursue a growth agenda and which elements of an organizational blueprint could best equip coops to achieve their goals.

Our objective was to formulate recommendations that would stimulate reflection and debate on the role of organizational levers in maintaining and increasing the relevance of the cooperative banking movement. A disciplined discovery process employed interviews with multiple stakeholders as well as primary and secondary research. We stress that, because of the enormous diversity within the coop movement in the Americas, neither the analyses nor our recommendations are tailored to any individual coop. Rather, they are meant to be directionally accurate for the sector as a whole.

WHY ORGANIZATION?

Many factors contribute to firms' relative success in achieving effectiveness and growth. A recent study performed by the Corporate Executive Board across multiple industries analysed the relative effects of different root causes for stalled growth. Exhibit 1 contains a summary of these results.

As we turn to the financial services industry, one could claim that the effects of regulation carry particular weight and explain much of the sector's growth performance. Indeed, new national and international standards and requirements appear on a regular basis. Moreover, the cooperative-specific regulatory framework in several jurisdictions is also in flux; some Latin American countries have only introduced specific regulations within the last 25 years. Nevertheless, there is a cross-section of performance outcomes for coops within common regulatory environments, as friendly or adverse as these may be.

1 For simplicity, we will use the terms "credit union," "cooperative bank," "coop bank," "coop," "cooperative," and "cooperative financial services" interchangeably throughout the rest of the document

Exhibit 1: Root causes of stalling growth and reduced effectiveness

Focus area for the current study (covers the third and fourth columns)

A partial list of elements

EXTERNAL FACTORS OUTSIDE MANAGEMENT'S CONTROL (13%)	"PURE" STRATEGIC FACTORS (41%)	"HYBRID" ORGANIZATIONAL/ STRATEGIC FACTORS (29%)	"PURE" ORGANIZATIONAL FACTORS (17%)
• Economic downturn • Geopolitical context • Regulatory actions • National labor inflexibility	• Premium position captivity by competitor(s) • Weakness in product offer • Key missing customer dependencies • Premature core abandonment • Voluntary growth slow down	• Failed acquisitions and expansions • Excessive strategic diffusion • Innovation management breakdown • Wrong performance metrics • Inflexible financial goals • Adjacencies failures	• Functional structure design • Capabilities/skills gaps • Flawed decision-making structure • Board inaction • Talent bench shortfall • Narrow experience base

Source The outline of the external perspective Stall Points by Matthew S. Olson of the Corporate Executive Board

The right side of Exhibit 1 shows the causes over which management exerts a direct influence; the study authors noted a fairly even distribution between strategic and organizational/hybrid factors.

An abundance of literature by both consultants and academics explains how the strategic component affects both overall performance and growth. Our assertion is that, in principle and especially over the longer term, strategies can be and are replicated. Yet variations in performance, growth, and survival rates persist across all industries.

We believe that the organizational dimension not only determines the ability of a coop bank to deliver on a specific strategic intent, but also has an important impact on the upstream formulation of the strategic objectives to begin with. Going further, organizational deficiencies – some of which are endemic across the coop industry – have actually resulted in more adverse regulatory environments as authorities have sought to curtail perceived risks to their financial systems. We have observed this effect in Brazil and Mexico, which have introduced regulatory regimes involving stricter scrutiny of coops after a series of failures within the movement. As such, organizational limitations are a major concern because of their "structural nature." They have the compound effect of reshaping the playing field for coops as a whole and preventing individual entities from responding to strategic inputs or adapting adequately in the face of a downturn in the external environment.

In contrast to the strategic dimension, we found a gap in existing literature on the organization side. That which does exist tends to focus on "supply-side, inside-out" basics such as structure and capabilities where the individual firm serves as the starting point and conversely few perspectives that address the "demand-side, outside-in" aspects of coop organization, which are at the core of a member-centric value proposition. Hence, we set out to address the following questions:

- How imperative is the growth agenda?
- What are the key organizational dimensions that determine an effective and growth-oriented cooperative?
- Are there one or more organizational "formulae" that provide a blueprint for superior cooperative bank or credit union performance?
- Either way, what organizational lessons can be gleaned from a cross-section of the cooperative banking sector in the Americas that may have implications for the future growth and prosperity of the movement as a whole?

WHAT KINDS OF FINANCIAL SERVICES COOPERATIVES WERE INCLUDED?

Our undivided focus has been on cooperative banks and credit unions. Land development banks, building societies, and mutual savings banks are not included.

MUTUAL INSURERS

Another type of cooperative financial institution is the mutual insurer. These enterprises, like cooperative banks, are owned by their members instead of stockholders. Their genesis is similar in that individuals banded together to self-insure where circumstance and opportunity arose. We have excluded mutual insurers from this study for three main reasons:

- They typically have much larger market shares than cooperative banks, making their competitive dynamics fundamentally different.
- In most instances, mutual insurers operate more like stock corporations than do cooperative banks, including a pronounced competitive stance vis-à-vis other participants in their industry segment.
- The insurance supply chain is fundamentally different and many, mutual insurers use broker distribution channels that allow greater separation from owned or leased infrastructure like physical branch networks.

WHY THE AMERICAS?

An analysis of this region complements prior Oliver Wyman studies undertaken in Europe. European banking is characterized by large coop bank entities that exhibit more consistent performance along stable trajectories, given the greater tradition of the cooperative movement and the concomitant maturity of the segment.

In contrast, the Americas are significantly more diverse in terms of individual coop bank size and the industry's overall trajectory, positioning, and market share distribution. This is caused by variations in macro-economic context, competitive forces, culture, and political factors, resulting in a more diverse ecosystem to study. Coop banking penetration rates vary significantly and are at a paradoxically low level in several countries where the need might be perceived as greatest based on traditional definitions of target member segments. In addition to the diversity of the coop sector in the Americas, each banking market is experiencing its own on-going developments, including the entry of new players, industry consolidation, acquisitions, and an ever-evolving regulatory landscape.

In short, the Americas represent a fertile region to study how organizational levers can contribute to the successful deployment and adaptability of the cooperative banking model abroad from its original European roots.

WHAT IS A COOPERATIVE BANK?

Cooperative banks are financial institutions that, while they operate in many ways like a traditional bank, are owned by their members. All people who consume goods or services from the bank register as a member of the cooperative.

The International Cooperative Banking Association describes seven cooperative principles:[1]

1. Voluntary and open membership
2. Democratic member control
3. Member economic participation
4. Autonomy and independence
5. Education, training, and information
6. Cooperation among cooperatives
7. Concern for community

Additionally, cooperatives distribute profits as dividends to members. Cooperative banks have often operated on a more social basis than shareholder banks, aiming to target underserved populations and contribute to their communities.

Some cooperatives have bounded membership, whereas others are more open. Bounded membership is restricted based on some predetermined criteria, such as employment in a given company or industry or residence in a geographic area (such as a U.S. state).

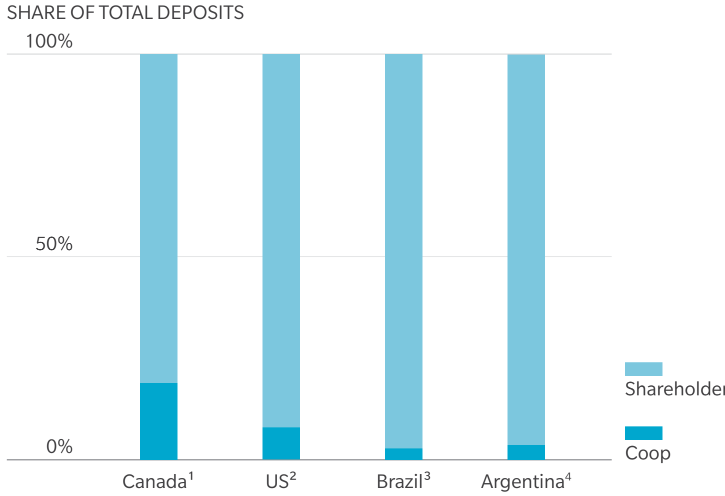
1 International Cooperative Banking Association, 2014

1.2. THE COOPERATIVE FINANCIAL SERVICES LANDSCAPE IN THE AMERICAS TODAY

Banking cooperatives across the region operate in distinct environments with a range of competitive dynamics. These external factors shape their strategic and organizational objectives and profoundly influence their growth. Three major observations apply across the region:

- Cooperatives' current market share leaves ample room for growth.
- Cooperatives are much smaller than shareholder banks but are generally more numerous.
- The market is highly fragmented, although the degree varies by region.

Exhibit 2: Deposit shares in cooperative vs. shareholder banks (Canada, US, Brazil, Argentina)



1 Credit Union Central of Canada and Canadian Bankers Association
2 NCUA and SNL
3 Banco Central do Brasil
4 Banco Central de la Republica Argentina

REGIONAL OVERVIEWS

The credit union industry structure varies dramatically across the Americas. There are many U.S. cooperatives in a fragmented market, yet they retain a small percentage of banking assets at just under 8%[2] (as Exhibit 2 shows). In Canada, employee associations were the genesis of many cooperatives, and deposit share outpaces that in the United States by more than double. Brazil and Argentina, two major Latin American nations, show deposit share levels that trail significantly, at below 3% and 4%, respectively.

Latin America and the Caribbean have very different levels of development and financial sophistication across their countries. With some notable exceptions, coops there tend to be smaller and even more local than in North America. Latin American and Caribbean coops also place a greater emphasis on their social mission, a finding that likely reflects the larger under-banked populations in these countries. In those countries, credit unions have been instrumental in expanding available access to previously unbanked or under-banked populations.[3] While views on the financial inclusion opportunity vary (particularly in Latin America), our estimates of this group's size range from 55–80% of the bankable population for Latin America and the Caribbean, as opposed to 3–5% in Canada and 15–20% in the United States.

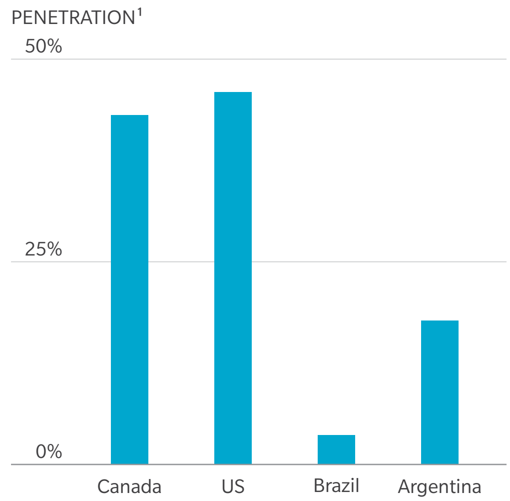
2 The use of assets tends to understate cooperatives' share of the retail financial space, since commercial banks have corporate assets that cooperatives typically lack. Using deposits instead, for example, the United States stands at roughly 10% market share

3 Definitions of "unbanked" and "under-banked" abound. For the purposes of this study, we define the unbanked as those without any access to the formal financial system. The under-banked, by contrast, have access to some financial products, though typically through non-bank channels and for a higher price. We refer to these two groups together as the "underserved."

Banking coops fare better in terms of penetration as defined by the World Council of Credit Unions' metric: "reported credit union members as a share of the economically active population aged 15–64." By this measure, shown in Exhibit 3, coops have the potential to play a much bigger role in society across the Americas than their asset or deposit share would suggest. Given their penetration, they have a long runway for growth, particularly in the developing regions of the Americas.

Despite their relatively smaller share and penetration, credit unions outnumber shareholder banks in every region, as Exhibit 4 shows. They are consequently much smaller on average than their shareholder-owned counterparts, ranging from roughly one-tenth to a fraction of a percent of their size.

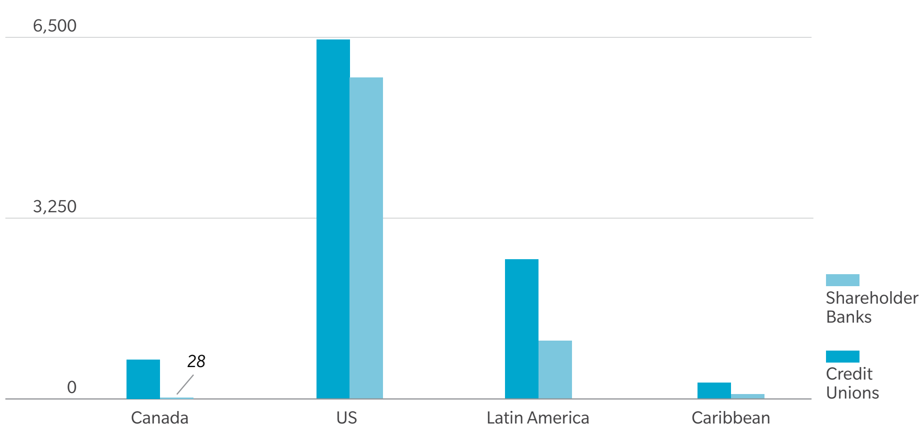
Exhibit 3: Cooperative bank penetration (Canada, US, Brazil, Argentina)



Source WOCCU and World Bank

1 Defined as the number of cooperative bank members as a share of the economically active population aged 15-64 years old

Exhibit 4: Number of cooperative financial services institutions vs. shareholder banks, by region



Source World Council of Credit Unions, FDIC, Canadian Office of the Superintendent of Financial Institutions, Bankscope, IMF, Oliver Wyman/Celent analysis

Exhibit 5: Assets of the top 10 banks (US, Canada, Latin America, Caribbean)

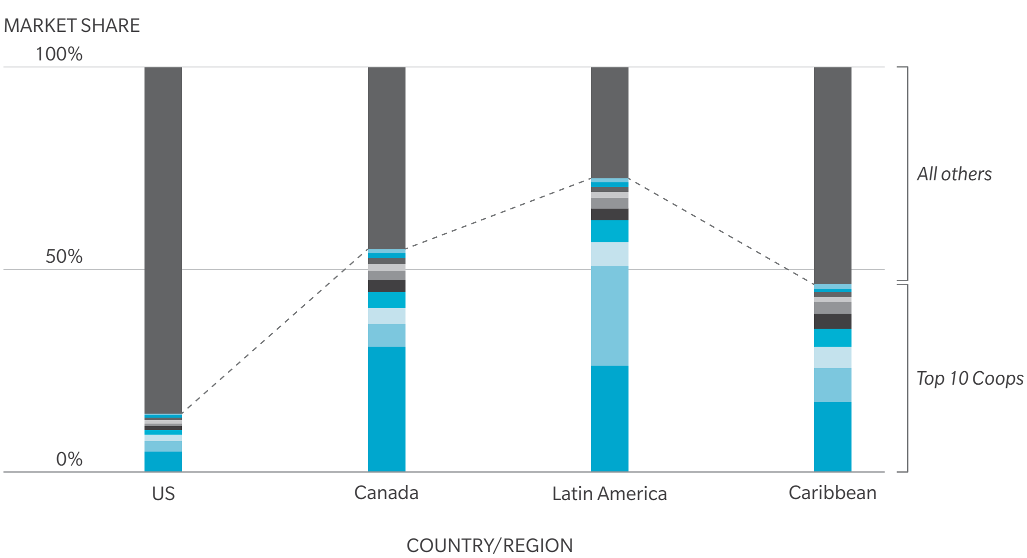
REGIONAL RANK	US	ASSETS, US $BN	CANADA	ASSETS, US $BN	LATIN AMERICA	ASSETS, US $BN	CARIBBEAN	ASSETS, US $BN
1	Navy Federal CU	55.5	Desjardins	173.9	SICOOB	18.2	APAP	1.1
2	State Employees	27.1	Vancity	15.9	SICREDI	16.9	Asociación La Nacional de Ahorros y Prestamos	0.5
3	PenFed	16.8	Coast Capital	11.4	UNICRED	4.1	BPWCCUL	0.3
4	BECU	11.9	Servus	11.1	Banco Credicoop	3.6	ECU	0.3
5	Schoolsfirst	9.9	Meridian	8.4	Caja Popular Mexicana	1.9	Grenada Co-operative Bank	0.2
6	The Golden One	8.2	First West	7.0	COOPEUCH	1.9	Roseau Cooperative Credit Union	0.2
7	Alliant	8.2	Conexus	5.5	COOPENAE	1.0	JTACCU	0.1
8	Security Service	7.7	Steinbach	3.8	MEGO	1.0	First Heritage	0.1
9	Star One	6.6	Affinity	3.6	FACHA	0.7	COKCU	0.1
10	First Technology	6.5	Assiniboine	3.2	COMIXMUL	0.7	Civil Service CCU	0.1

Source: Celent

Exhibit 5 lists the ten largest coops in each geographic region. The largest credit union in the United States, Navy Federal, would rank as the 40th biggest bank in the country, while Canada's Desjardins enjoys such an important market position in its primary provincial market, Quebec, that in 2013 it was designated as a systemically important Canadian bank.[4]

Moving beyond the largest players, credit union market fragmentation is the metric that shows the greatest regional disparity, as Exhibit 6 shows. Market share of the top ten institutions ranges from a low of 15% in the United States to a high of 73% in Latin America.

Exhibit 6: Market share of the top 10 credit unions



Source Individual country and credit union financials; World Council of Credit Unions

4 A designation bestowed by the Basel Committee on Banking Supervision

1.3. KEY INDUSTRY CHALLENGES

Beyond the distinctive landscape of the cooperative sector in the Americas, it is important to address major trends affecting the banking industry as a whole to truly understand the environment in which cooperative banks and credit unions have to operate today, and the options and opportunities available to them. Our view is that the following trends will prove fundamental in shaping the cooperative financial services movement across the Americas.

GATHERING COMPETITIVE HEADWINDS

In some markets, shareholder banks and consumer lending companies, as well as retailers that act as lending institutions, are paying more attention to serving some of the prize coop segments. This can result in either a bleed in membership or, more insidiously, a continuous loss of share-of-wallet among an increasingly savvy and less loyal base that divides its wallet to take advantage of the most economically attractive offer among the slew of options available. In this scenario, the divergence between penetration and market share highlighted above will only grow worse.

DISRUPTIVE TECHNOLOGY ON THE RISE

Development complexity is increasing, obsolescence cycles are shrinking, and legacy systems integration is ever more complex. Tools that are available to coops are available to all other industry players as well. Electronic transactions are changing transactional banking and payments, requiring credit unions to continuously upgrade infrastructure in the face of growing technology risk to achieve table-stakes standards of convenience and service for an increasingly sophisticated member clientele. The channel challenge is particularly acute for coops, since they cannot simply opt to migrate from bricks-and-mortar to online and mobile, but must continue to serve the needs of all segments as economically as possible, including traditional clients who value the branch experience.

Data analytics and business intelligence requirements are also becoming more sophisticated each year, creating a key competitive advantage for firms that can harness them. Coops and credit unions are thus precluded from the option of inaction. The capability-building required demands resources and levels of investment that are typically not available to smaller financial coops.

FUNDAMENTAL DEMOGRAPHIC SHIFTS

The aging customer base of many cooperatives presents a multi-pronged challenge. The most obvious is continuity: if new enrolment by younger members does not keep pace with generational turnover, the sector will contract. The second challenge is the value proposition for a younger generation: this must be re-imagined in a world of social media and ubiquitous technology – and be cleverly executed. Thirdly, cooperatives in general will need to move beyond traditional transaction banking to embrace lifecycle relationship banking more fully, such as catering to the needs of seniors for asset and wealth management and retirement planning.

We believe these industry trends will reinforce the need for coop banks to rethink and reinvent their organization and management approaches in order to be well positioned for the opportunities and challenges that lie ahead.

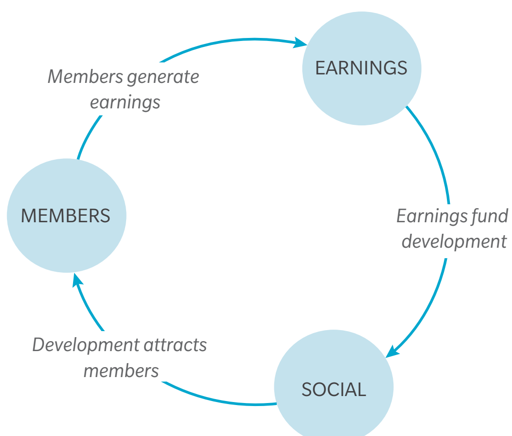
Credit union financing promotes alternative energy sources and sustainable local food systems.

2. MOVING BEYOND "VALUE VS. VALUES": THE NEW IMPERATIVE FOR GROWTH

2.1. WHY SIZE MATTERS

Prior analyses of shareholder banks by Oliver Wyman showed that achieving greater-than-average revenue growth was a fundamental driver for beating the average EBITDA percentage and market capitalization multiple of peers. A different perspective needs to be taken to determine whether the same applies to cooperative banks, taking into account their fundamentally different operating principles. Exhibit 7 captures the essence of the virtuous cycle that is applicable to the functioning of cooperative banks in which members generate earnings that are partially used to fund the long-term development of the community, which in turn serves to attract more members, which in turn drives the continuation of the process.

Exhibit 7: The cooperative banking virtuous cycle



MEMBERS

- Typically share a common bond, e.g.
  - Geography
  - Social or professional affiliation
- Higher degree of community motivation
  - Involvement in self-determination
  - An interest in the improvement of fellow stakeholders

EARNINGS

- Net income generally applied directly to members
  - Lower interest on loans
  - Higher interest on savings
- Serves as capital-raising tool
  - Only option available in several regulatory jurisdictions
- Direct investments in the future
  - Product and services
  - Service and technology investments

SOCIAL MISSION AND LOCAL, LONG-TERM DEVELOPMENT

- Operation not focused on profit generation
- Balancing immediate member needs with holistic-minded investment in communities
- Social inclusiveness perspective in advancing access to financial services

Source Oliver Wyman perspective

THE CASE FOR THE COOPERATIVE BANKING SEGMENT AS A WHOLE

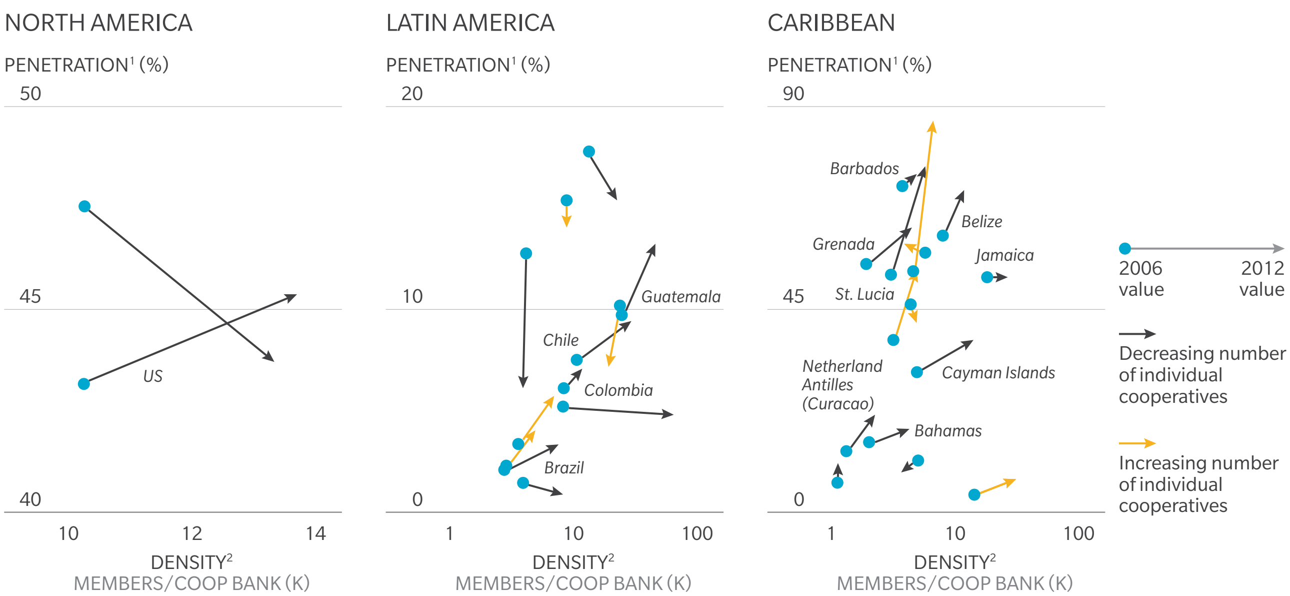
Intuitively, growth serves to advance the agenda of the overall coop banking movement because a positive trajectory both increases and reflects relevance, particularly given low current market share starting points. A growing membership base provides additional earnings, which in turn contribute to initiatives that can be used to further emphasize increased financial access by other segments within the community served by the coop bank, leading to overall development in a virtuous cycle.

Hence, it is important to determine what structural trends at the individual cooperative level in the Americas have led to the greatest growth for the segment. We set out to understand this dynamic by looking at how membership penetration variations over time were related to changes in membership density as well as the degree to which individual cooperatives were created or consolidated.

Exhibit 8 shows a clear correlation between a reduction in the number of individual banking cooperatives and an increase in membership penetration. We believe that most of this reduction is not because of demutualization or market exit (which would reduce the penetration rate), but rather a structural consolidation among existing cooperatives that ultimately makes them more effective in garnering additional presence and support.

We observe in Exhibit 8 that, between 2006 and 2012, almost two-thirds of the countries in the region experienced an increase in the average penetration of cooperative banking members among their economically active populations. It is not surprising, therefore, that in 90% of those cases this increase was accompanied by an increase in the average member density (members per cooperative bank). It is noteworthy, though, that 77% of the cases involving increased member penetration and density actually showed a decrease in the number of individual cooperative banks in operation. (Those countries are listed in the exhibit.) Within this group, the average penetration increase was just under 6%, while the reduction in the number of credit unions averaged 21%.

Exhibit 8: Changes in cooperative bank penetration vs. membership density and consolidation tendency by country (2006 -2012)



Source WOCCU

1 Number of coop bank members as a share of the economically active population

2 Average number of members per coop bank

THE CASE FOR INDIVIDUAL COOPERATIVE BANKS AND CREDIT UNIONS

Turning to the individual enterprise, our study determined several benefits from growth.

- Increased membership via geographic expansion or diversification into additional economic and professional groups within an existing locality is an effective method of diversifying operational risk and building resilience to withstand the ups and downs of the economic cycle
- Adoption of an expanded view of the membership base affords more latitude in setting policies that use the increased profitability of certain segments to invest in the long-term development of other member segments that are either behind economically or else incur excessive costs to participate in the economic system.
- An expanded and heterogeneous member base serves to increase word-of-mouth marketing and advocacy strength.

We also uncovered evidence that growth is possible without compromising underlying membership health, meaning that the average cooperative bank need not go “down market” as it increasingly competes with shareholder banks and other financial services players in order to expand its footprint.

To ensure an appropriate basis for comparison, we reviewed a set of coop banks across a large size range covering

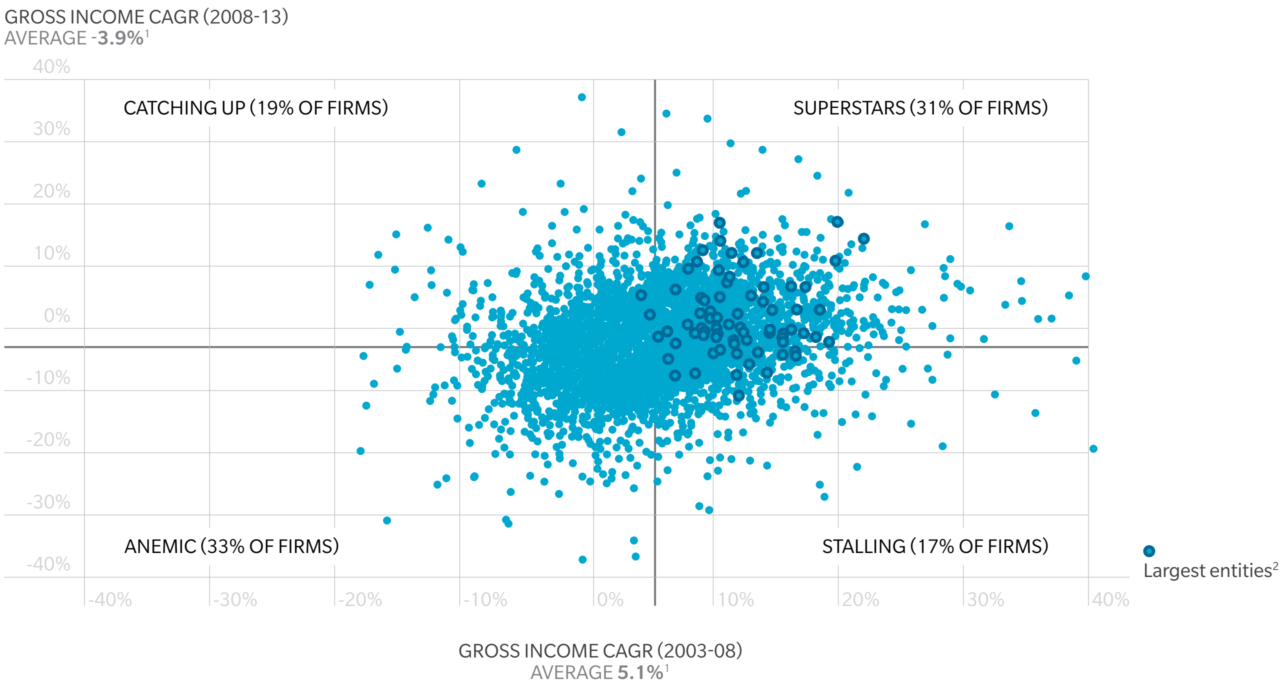
Exhibit 9: Asset base vs. membership base

CREDIT UNION DATA (SIZE OF BUBBLE REPRESENTS TOTAL BRANCHES)

Source SNL, Bankscope, Credit Union Central of Canada, annual reports, company websites three different regions within the Americas. Within each of these, the data shows a linear correlation between the asset and membership bases, as seen in Exhibit 9. No drop-off in average assets per member was observed as coop banks increased in size. Additionally, our analysis of a broad U.S.-only data set containing 6500 entities showed a significant reduction in the variation of average assets per members as asset levels grew. These observations support an assertion that, historically, membership segment "health" has remained constant for those entities that have achieved growth among their membership ranks. History therefore indicates that coops can operate on the premise that growth can be pursued without fear of a reduction in the attractiveness of the overall membership base, as measured by average asset levels.

Importantly, the largest firms were significantly more resilient than the global group in dealing with external shocks. To analyse this, we looked at the distribution of gross income growth before and after the 2008 crisis for a vast set of cooperative banks and credit unions across all geographic regions in the Americas. An examination of Exhibit 10 clearly illustrates the size advantage described above. Overall, only a minority (31%) of coop banks are classified as "superstars," having beaten the average of gross income growth over the five-year periods prior to and following the 2008 crisis. Yet of the largest 100 by asset size, a full 70% fell in this category, representing a 125% increase over the group at large. Moreover, the largest banks came out of the crisis more robustly. While 50% of the overall

Exhibit 10: Coop bank gross income CAGR comparisons before and after the 2008 financial crisis (all Americas' regions)



Source SNL and Bankscope data for cooperative banks. Largest entities are defined as top 100 by assets, results >40% (abs. value) removed

1 Considers all sizes

2 Top 100 by assets

Exhibit 11: Cooperative bank asset growth vs. asset base across the Americas region

SEGMENT	2013 ASSETS RANGE	NUMBER OF FIRMS	SHARE OF ALL FIRMS	AVERAGE ASSETS CAGR (2008-13)
All	All	6616	100.0%	4.3%
Smallest	<$1 MM	401	6.1%	-0.8%
Medium	$1-100 MM	4709	71.2%	+4.1%
Large	$100 MM-$10 BN	1497	22.6%	+6.3%
Largest	>$10 BN	9	0.1%	+5.8%

Source SNL, Bankscope
Note Omitted growth outliers

set grew at below-average rates after 2008, this was true only 19% of the largest group.

In establishing the case for growth, individual cooperative banks may wonder whether there is a "minimum bar" required to successfully pursue it. A review of a broad set of entities over the last 5 years, shown in Exhibit 11, shows that for all but the very smallest of entities, the tendency toward asset expansion has been positive, and that a further upswing kicked in for those entities with more than US$100 million in assets.

2.2. WHAT IS DRIVING THE APPETITE FOR GROWTH?

Cooperative banking growth in a given country provides a positive impact for specific community segments. The preferred route for achieving this impact is through the presence of a concentrated set of cooperatives, each operating with sufficient critical mass. This drives a virtuous cycle of additional membership attraction, asset strength, improved standing vis-à-vis regulators, and overall resilience. Yet while many senior coop stakeholders within a given market espouse the need for growth, the degree to which they explicitly and effectively pursue it in their respective agendas varies considerably. Based on interviews, we determined three broad factors that directly affect the degree to which growth permeates the strategic and operating agenda of individual coops.

COMPETITIVE INTENSITY

The competitive environment within which coop banks operate is highly varied. In the markets studied, coops typically compete with shareholder banks, primarily at the community-level, but also at a regional and national level as well. Our observation is that coops with lower real growth appetites assume a "default strategic position" focused on market segments that their competitors have essentially ceded to them; these tend to be underserved, more remote, and less economically attractive. While individual coops cannot exert control over the surrounding industry context, this should not be a factor in setting individual coops' growth appetite. We assert that – as part of their mission to ensure that their constituent communities have widespread and affordable access to financial products – coop stakeholders should champion their relevancy through an explicit growth agenda independent of the competitive intensity of their market. In addition, profit-driven players (whether stock banks or private financing companies), are increasingly targeting core coop segments with effective marketing campaigns (and are typically doing so at higher costs to the end consumer). We expect that coops will need to increasingly respond and "take the fight" to these competitors. Growth can no longer be viewed as a discretionary option for the coop segment but rather as a means to ensure the survival of the overall sector.

We noted that competitive pressures from non-cooperative entities – while keeping managers up at night – are very healthy for the movement. Across all markets, they actually drive growth-focused behavior, including greater efforts to implement operational efficiency, expansion of the product and service portfolio, additional emphasis on rolling out alternative channels, and the implementation of alliances and partnerships. In contrast, we found that decision makers in lower competition areas were more likely to focus on a more limited, more localized, physical branch-based offering that relied almost exclusively on a "high touch" service orientation. We observe that, in certain markets, cooperative banks often compete with each other. While their service offerings and value propositions may differ and cater to different membership groups, the low current penetration level of the segment as a whole should encourage coops to focus their long-term growth efforts on competing with shareholder banks rather than against each other.

REGULATORY FRAMEWORK

Coop banks in many countries throughout the Americas face rapid and constant change in their regulatory environments. This evolution is typically accompanied by ever-increasing compliance requirements and costs that benefit larger institutions that can amortize those costs over a larger member and asset base.

We note that several countries have only established cooperative regulatory frameworks within the last 30 years, and to this day the repercussions of their implementation continue to be felt as entities strive to adhere to compliance norms. The effects of regulation are conflicting. In some cases, they promote consolidation and individual bank growth, while in others they limit the type of operations that a bank can participate in, thus choking off potential avenues of growth. An example of this is the requirement in many markets to raise capital exclusively through retained earnings. This increases the appetite for member and asset growth as an avenue for achieving those earnings while simultaneously limiting institutions' ability to raise capital and liquidity through other means in order to invest to achieve a positive trajectory.

As we alluded to earlier, markets with well-run cooperatives – those that have demonstrated in the aggregate sustainable practices through appropriate governance, priority setting, and disciplined execution – are more likely to enjoy an overall favorable regulatory environment.

ORGANIZATIONAL EFFECTIVENESS

These elements are completely within the control of the cooperative banking segment itself – a combination of factors at the industry and individual bank level, where levers can be used with a large degree of independence from macro-economic, competitive, and regulatory factors. The next section highlights our main findings in this regard, and the final section of the report covers specific recommendations for improving industry performance.

Across Latin America, cooperative financial services play a vital role helping small businesses reach their financial goals.

3. MAIN STUDY FINDINGS: TESTING KEY ORGANIZATIONAL HYPOTHESES

While the opportunities and risks confronting coops across the Americas warrant a separate extensive strategic review, we believe that, in all geographies, "business as usual" will no longer be sufficient to compete and grow. Our analyses and interviews were guided by a desire to test the organizational hypotheses formed at the outset of the study.

3.1. DOES STRUCTURE MATTER?

Structure consists of a variety of aspects of a business's organization, including: the presence of functional capabilities, linkages and groupings among these, roles and responsibilities, and the activities/deliverables of individual functional entities. A corporation's operating model includes its organizational structure acting in concert with its governance. As part of our study, we investigated whether specific organizational choices affected coop banks' effectiveness and their ability to grow. We found that although a variety of organizational structures can be effective, the presence of certain key elements specifically affected the growth trajectory.

Oliver Wyman views organizational structure through the prism of both its strategic and its operational design. Exhibit 12 highlights the differences between those two dimensions.

Exhibit 12: Strategic and operational organization structure design

STRATEGIC		OPERATIONAL
Global direction and shape of the organization, focus and policies	WHAT TYPE OF DECISIONS?	*Functional structures, checks and balances, operational processes, work flows, job descriptions, headcount*
Top levels	WHAT PART OF THE ORGANIZATION?	*All levels, as necessary*
Top-down	DESIGN LOGIC	*Bottom-up*
Strategic intent	DESIGN DRIVEN BY	*Execution focus*

Source Oliver Wyman perspective

Credit union executives are conscious of the importance of structure and in a few cases have adopted novel approaches to the subject. From a strategic design perspective, one senior manager pointed out that his coop was organized around members rather than individual product lines. He ventured that this provided an advantage in contrast to the more silo business line mind-set that is prevalent in many shareholder banks. Overall, though, we detected significant convergence in the overall shape of coop banking structures and observed that many structures can work as long as core capabilities were brought to bear in managing member relationships. Our research identified opportunities for improvement in certain key areas.

STRATEGIC ORGANIZATIONAL STRUCTURE DESIGN TYPICALLY LACKS KEY GROWTH-ORIENTED ROLES

Coops looking to promote change would benefit from the presence of executives in "growth-focused" roles who can help ensure that the organization has the right capabilities and initiatives in place to grow.

The functions in question are those that can have a particularly noticeable effect on an organization's growth prospects, including strategy/organization, marketing/development, innovation, information technology, and sales. The analysis of U.S. coop banking senior manager ranks in

Exhibit 13: Occurrence of growth-focused senior roles at US cooperative banks[1]

Source Capital IQ

1 Excluding Federal Home Loan Banks

Note Pie charts are share of companies, where as column charts are the distribution of executives

Exhibit 13 shows the percentage that have at least one senior manager across these functions. The presence of key growth-oriented executives within the strategic organizational design of the bank indicates how coop banks view their direction and can have a tangible effect on their performance.

The data reflects a low prevalence among coops of "growth-focused" roles. In all cases, these were lower than the corresponding situation at U.S. shareholder banks. Our particular concerns are as follow:

- The relative absence of a dedicated senior focus on growth can result in a diluted and atomized growth agenda.
- For those banks where there are these growth oriented roles, the observed skew to more junior management titles may reduce the level of effective authority in internal discussions. It may also indicate a lower level of investment commitment, thus limiting the coop's ability to attract the most qualified candidates to these roles.
- The dearth of formally assigned senior innovation executives within the cooperative space can significantly dilute efforts to develop and implement new solutions.

While the need to reduce costs and drive efficiency gains often superseded other considerations within smaller banks, progressive management teams still included growth-focused roles. One credit union CEO indicated that his executive team was deliberately lean, consisting of just a CFO, a risk officer, HR and IT VPs, and importantly an EVP for retail, as well as senior leaders of corporate development and marketing.

We also consider the presence of a Chief Operating Officer (COO) to be a catalyst role, highlighting it in Exhibit 13. While broadly speaking the operations function is not usually tasked with driving a growth agenda, a dedicated professional in this area does serve to target improvements in transactional capabilities, facilitating the transition to relationship banking. This structure also helps liberate the CEO from daily firefighting, allowing the top executive to focus on the future roadmap. In this sense, coop banks (20% of whom have a COO) are half as likely to have a COO as their stock counterparts, of whom 41% do.

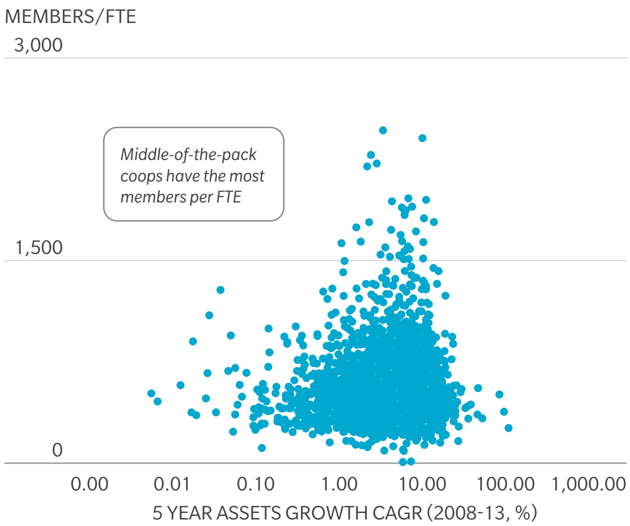
MID-SIZED COOPS AND THOSE SHOWING AVERAGE GROWTH TRAJECTORIES HAD THE MOST EFFICIENT HEADCOUNT PERFORMANCE INDICATORS

At the operational design level, coop banks need to remain highly conscious of their staff efficiency ratios, which are an important contributor to both the cost-to-income ratio and the member experience. Interestingly, a review of a large sample of U.S. cooperative banks highlighted that both members per FTE (in Exhibit 14a) and assets per FTE (in Exhibit 14b) don't exhibit simple scale economies. The results for the full spectrum of size and growth rates are shown.

We are not suggesting that coops eschew the pursuit of efficiency over the long term while they strive to pursue growth. However, the data suggests that in certain situations additional headcount may be required to generate growth and that this "investment" may result in lower efficiency ratios over the short- and medium-term. It also implies that the largest members of the coop group are not immune to inefficiency and must remain vigilant on this point.

Exhibit 14a: Members per FTE vs asset growth 2008 - 13 and coop size (US cooperative banks)

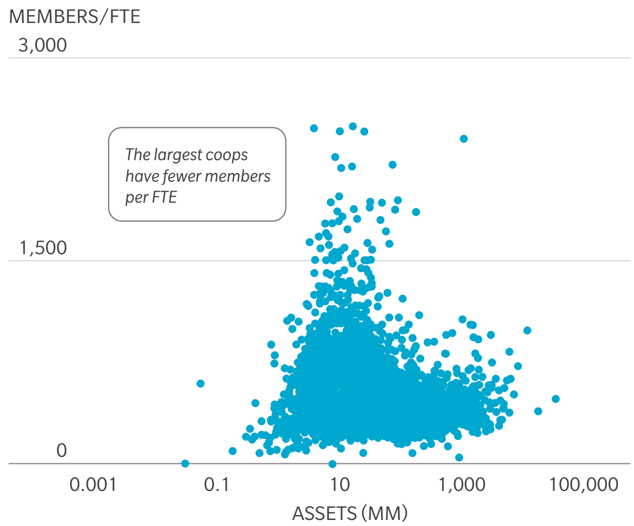
GROWTH



For coops above average growth: 473/FTE
For coops below average growth: 496/FTE

Faster growing coops have fewer members/FTE

SIZE

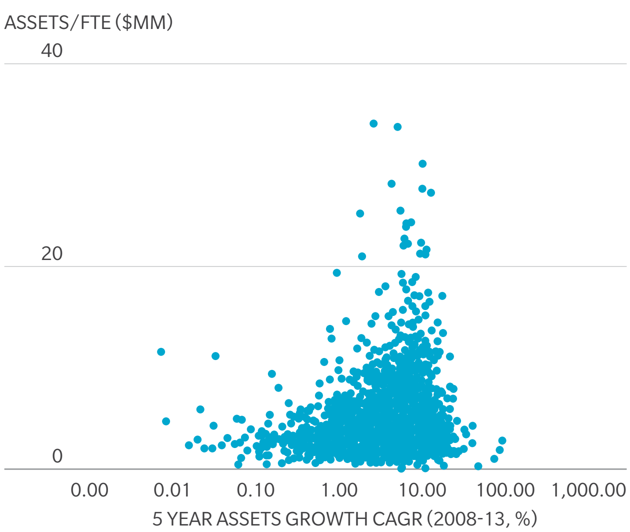


For coops above average growth: 404/FTE
For coops below average growth: 503/FTE

Larger coops also have fewer members/FTE

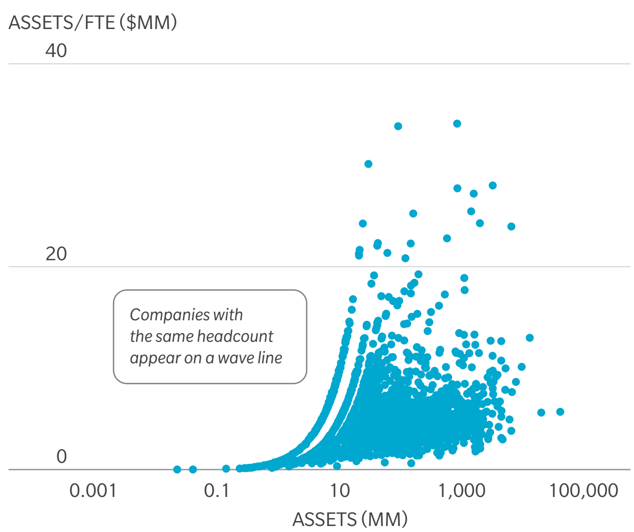
Source SNL
Note Coops with >3000 members/FTE have been omitted

Exhibit 14b: Assets per FTE vs asset growth 2008 - 13 and coop size (U.S. cooperative banks)



For coops above average growth: $4.1 MM/FTE
For coops below average growth: $3.5 MM/FTE

Faster growing coops have more assets/FTE



For coops above average growth: $4.7 MM/FTE
For coops below average growth: $3.6 MM/FTE

Larger coops also have more assets/FTE

Source SNL
Note Coops with >$40MM /FTE have been omitted

There is a need to move beyond a mathematical analysis of headcount efficiency and to dig deeper into an analysis of the actual areas where staff are concentrated to determine how they support the growth agenda. On a positive note, we found that coop banks are well prepared to integrate additional relationship banking components into their value proposition given the focus on advisory services and the desire to relate to individual members on a regular basis through branch-based interactions. This is an area that should be further emphasized as coops look to the future. On the other hand, the drive to remain "connected" to members results in a greater tendency to perform less value-adding activities (such as collections) in-house. Shareholder banks will typically outsource these activities to a much greater extent, creating greater economic efficiency. The overall effect is that staffing levels within branch structures are typically over-weighted in relation to profit-driven peers. We found that there was an opportunity to rethink this model, combining a leaner approach to branch staffing while retaining staff in key high-touch relationship banking roles and diverting expense savings towards investment in the digital and online proposition.

Following our examination of a set of organization charts, we found that although there was a tendency for homogeneity in organizational structures, specific levers assisted in improving performance: senior executives in growth-focused functions and proper prioritization of internal headcount on the key member relationship capabilities.

3.2. IS THE UNDERLYING STRENGTH AND HEALTH OF MEMBERSHIP A KEY DIFFERENTIATOR?

The cooperative movement is defined by member ownership and direct member participation in governance. This fact leads coops to approach business with a social mission orientation, targeting population segments that have been historically underserved by shareholder banks.

Does the underlying strength and health of membership affect the growth and effectiveness of cooperatives? And if so, should cooperatives deliberately target this dimension as they think about their future membership base?

MEMBERSHIP CRITERIA HAVE FUNDAMENTAL IMPLICATIONS FOR A COOP'S FUTURE

Recall our finding in Exhibit 9 (Chapter 2) that cooperatives have historically been able to expand their memberships without reducing average assets per member. Nevertheless, membership criteria have a fundamental effect on a coop's future growth prospects. While "bounded" membership (defined as very specific affiliation criteria that must be met to join a cooperative) was the norm when many entities were formed at the outset of the movement, most major growth stories have been accompanied by a migration to an open membership concept, typically centred around a specific geography.

In theory, bounded cooperatives can claim to be closer to the specific needs of a more homogeneous member base. For the largest bounded affiliations, typically a department of the public sector or a major multinational employer, this can be an advantaged position to occupy. As captive parts of large organizations they enjoy significant runway and have the potential to achieve critical mass and economies of scale. Most bounded institutions, however, suffer from limited growth opportunities and hence struggle to reach the critical mass necessary to optimize their value proposition. As such, the perceived advantage of being more attuned to their membership's needs in theory is curtailed by the difficulty in executing on that advantage. Many fall into the insidious trap of maintaining existing membership levels while suffering an erosion of wallet share as increasingly opportunistic members split their business and mix and match their financial services providers.

EXPANDING HORIZONS FOR THE GREATER GOOD

A majority of the coops surveyed were concerned about the rising average age of their members and a dearth of younger new members. The specifics of this problem differed by geography:

- In Canada and the United States, an aging member base tended to be associated with the risk of excessive capitalization of the coop, as credit needs are concentrated in a younger demographic.
- For developing countries with less stable economies and more youth-oriented work forces, credit needs continued later into life, and a lack of younger workers affected the deposit base, risking the possibility of insufficient funds to satisfy seniors' borrowing requirements.

A particularly unexploited opportunity for unbounded coops is to consider additional up-market transitions, targeting higher-end membership segments to generate additional deposits that can be used to finance the overall social mission. Independent of market, many are wary to go head-to-head with shareholder banks in serving segments that they are not traditionally familiar with.

MEMBERS FUNDAMENTALLY SHAPE THE COOP CULTURE

A long-term, affiliation-centric view of the value of members clearly represents a departure from the way shareholder banks typically consider customers. However, even within the coop movement, the relative focus on long-term investment in communities, as opposed to maximizing the "return" to members, results in different strategic choices. We find that the more individual members are driven by the desire to maximize their financial position over the short term (without reference to the cooperative mission) the less the strategic agenda reflects a holistic and long-term concern for membership growth and community impact.

One American executive shared the way members' priorities affect his credit union's culture. While the members had chosen the credit union for its service quality and low costs, their desire to keep decision making very local limited the extent to which he could deploy shared services and a lean branch structure. Coop banks that we spoke with actively encouraged their employees to take on roles in their communities in order to emphasize the "local" nature of the coop and to promote its social mission. One Canadian credit union actively seeks membership input into its culture using annual surveys and hosts an on-boarding session for new members.

The cooperative model of "serving members" results in a simplicity of focus that stands in contrast to the typical situation of shareholder banks, which have to balance the competing needs of separate constituencies: client satisfaction and shareholder returns. This is one of the most powerful tools at the coop banks' disposal – regardless of whether it shows up as flexibility in extending credit to its members, the matching of local deposit gathering with local credit needs, deep involvement in the community by its representatives, or a focus on local employment in the communities it serves. When this model applies to a robust and diverse membership base, it creates significant value; where the base is not as healthy (e.g., solvent, sustainable, committed, and engaged), the risks to the model become apparent, to the point of putting the coop's financial livelihood in jeopardy.

The health and strength of members play a fundamental role in the long-term prospects of a cooperative. Coop banks can shape their destiny by managing their membership base proactively in order to magnify the positive effect of the cooperative model in their communities.

3.3. ARE COOPERATIVES THAT INNOVATE MORE AROUND THE MEMBER EXPERIENCE BETTER ABLE TO DIFFERENTIATE THEIR PRODUCTS AND SERVICES?

The fact that post the financial crisis innovation has become important again in financial services was not lost on the coop executives we spoke with. The pace of investment in innovation has clearly picked up in recent years across the sector, with several cooperatives in Canada and the United States reporting an explicit goal of initiating new "releases" on a set timetable.

EVIDENCE OF CREATIVE SPARK IN A SECTOR LONG CHARACTERIZED BY A "ME TOO" PRODUCT AND CHANNEL MENTALITY

We found widespread focus on the leverage of technology to foster the development and use of direct channels and to increase connectivity with members. However, in most cases these initiatives could be described as attempts to either catch up with or match capabilities that already exist among shareholder-owned competitors. Additionally, many cooperatives are seeking to develop the youth segment by deploying social media and expanding their multi-channel strategy (telephone, mobile, and online) to better cater for convenience-driven members and lower the cost-to-serve in branches.

Coops are also mining their special relationship with members to listen for and reveal members' needs and using this feedback to develop solutions that will fulfil them. Examples include the launch of no-fee accounts in response to member feedback, as well as differentiating service levels to adjust the value-to-cost ratio for serving the needs of different segments. Digital channels are being developed to facilitate new member on-boarding without the need for an in-branch visit. One Canadian credit union is staking out a leadership position in the industry with respect to remote deposit capture. To strengthen the cooperative relationship and encourage participation, progressive coops are also enabling online member participation in their Annual General Meetings.

In the main, however, most of the innovation in the sector we noted is incremental in nature and "bold bets" including major changes to the business model are relatively rare. One of the reasons for this, according to management, is the complexity of dealing with a multi-level governance structure. Prohibitive costs and risk associated with "breakthrough"-type innovation were also mentioned, underscored by coops' reliance on retained earnings for capital.

INNOVATION AMBITION DEPENDENT ON CAPABILITIES

While innovation ranks high on their strategic agenda, coops across the Americas are not uniformly creating the roles or organization structures to achieve it. Typically, innovation efforts are a diffuse affair, relying on spare or part-time capacity. Although advantageous from a short-term financial perspective, executives told us that the lack of dedicated teams had a tendency to dilute efforts, stretching them out sometimes indefinitely, as the day-to-day business needs crowd out bandwidth for new initiatives. Innovation efforts are often viewed as "side projects" that contribute to a preference for incremental change as opposed to bold new initiatives and breakthroughs.

The appetite for innovation is also correlated to in-house competencies. Some coops feel they have strong software development and other technical skills, but they believe they lack the talent or skills to pursue a vigorous innovation agenda. On the other hand, the less self-sufficient coops are increasingly willing to partner with peers to secure innovative products and services. We also noted that a willingness to embrace change and drive innovation was associated with tenure – executives and member representatives who grew up with their cooperatives over many years and in many cases created their legacy systems seemed the least motivated to innovate.

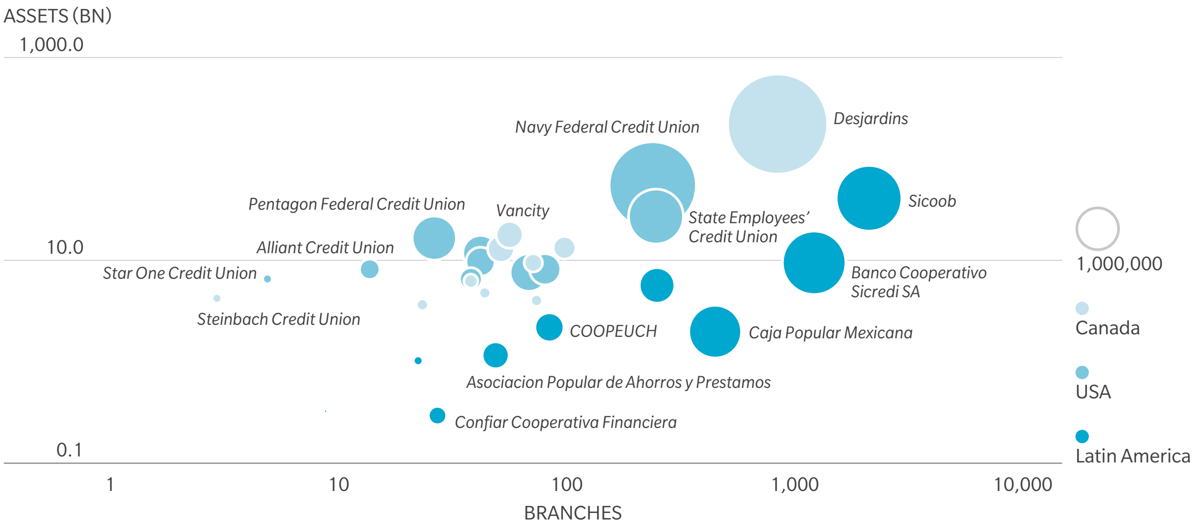
DRIVING EFFICIENCY THROUGH ALTERNATIVE CHANNELS AND THE "NETWORK EFFECT" OF CRITICAL BRANCH DENSITY

Alternative distribution channels represent a key area of focus for innovation efforts that affect the member experience, driven by a desire to reduce the high fixed costs associated with branches. Exhibit 15 below shows the relationship between assets and branches for a set of leading cooperatives across the Americas.

Although the data above does not display all the coops we studied, it indicates that within each region, the member and asset levels of the dominant market players by branch presence are somewhat higher than the linear relationship across the rest of the branch quantity spectrum. This suggests a "network effect" associated with branch density in which market leaders receive a disproportionate share of assets from their physical footprint. Coops with the largest number of branches generally have more assets per branch than smaller and mid-size ones, resulting in a disproportionate compensation for efficiently achieving a physical footprint advantage.

Exhibit 15: Asset base vs number of branches

CREDIT UNION DATA (SIZE OF BUBBLE REPRESENTS MEMBERSHIP)



Source SNL, Bankscope, Credit Union Central of Canada, annual reports, company websites

While worthy of consideration, this finding does not imply a prescription for credit union management or even a realistic goal for smaller coops. A majority of managers don't actively consider this in their planning criteria; one executive at a smaller credit union said that maintaining a small number of branches was central to organizational efficiency; reducing regional management overhead took priority over causing any additional member inconvenience. A mid-size Canadian credit union countered the "branch critical density" effect by locating its branches in business center "hubs," thereby reducing the overall number of branches while still maintaining accessibility for members.

While many coops are innovating, only a relative few have been able to move beyond a "catch-up" posture in terms of member experience and deliver a differentiated proposition through leading edge or 'big bet' initiatives centered on the cooperative promise. Their primary focus has been on channels and convenience, responding to competitive pressures and members' transactional banking needs.

3.4. DOES THE APPROACH TO TALENT TRANSLATE TO GREATER EFFECTIVENESS AND GROWTH?

Beyond the pro-growth executive roles we discussed in section 3.1, the type of talent that coops look for and groom plays a role in driving organizational effectiveness and a growth orientation.

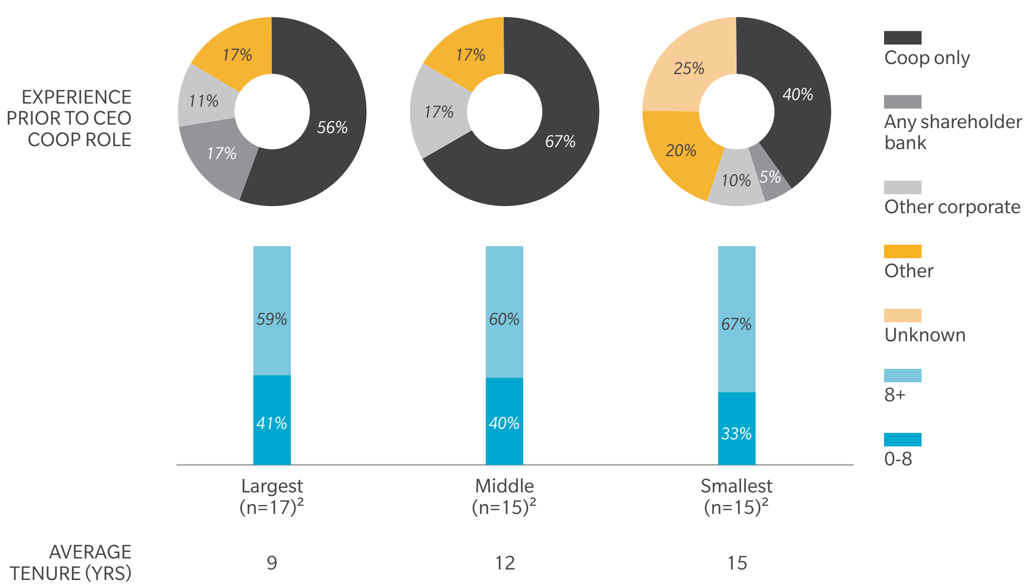
COOPERATIVE CEOS TEND TO LAST A LONG TIME

A sample of U.S. credit unions in Exhibit 16a shows that cooperative CEOs tend to stay in their positions for a long time. Among small coops in particular, the average tenure was about 15 years and two thirds of the CEOs had been in their roles for more than eight years. Exhibit 16b shows that longer tenures (8+ years) are associated with higher asset growth but lower profitability. Note that in the coop context, lower "profitability" may not be negative, as we observe two alternative strategies for long-term sustainability in the sector:

1. Use of lower profitability targets and ROE, albeit accompanied by an efficient operating ratio, as the conduit to offer more desirable conditions to members, e.g., better credit terms and/or deposit rates ("relevance strategy").
2. Generation of higher ROEs with the view to building a war chest of retained earnings for future investments, e.g., optimizing the digital/mobile offering to attract a next generation of members.

Long-tenured CEOs appear to choose the former path, which seems to put the priority on maintaining the existing base of membership. The opportunity cost of this strategy (and leadership perspective) may be in foregoing the kinds of alternative value

Exhibit 16a: CEO tenure and experience prior to coop CEO role by company size (selected U.S. cooperative banks[1])



Source Company websites, press announcements

1 Selected from top 100 by assets, with largest being at the top (1-20), middle (40-60), and the smallest (80-100)

2 Bracketed number represents number of CEOs (out of 20) for which tenure information was available

propositions associated with rejuvenating member demographics.

FOR THE MOST PART, COOPERATIVE CEOS HAVE ONLY WORKED IN THE COOPERATIVE SECTOR

Exhibit 16b also reveals that CEOs across credit unions of all sizes are most likely to have only ever had cooperative banking experience.

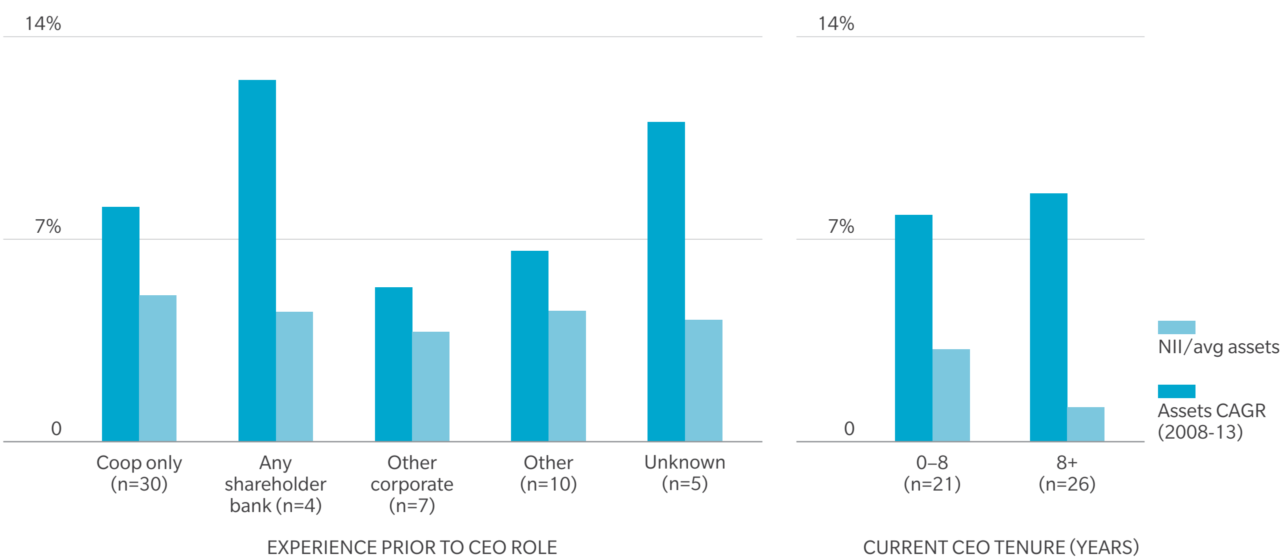
From Exhibit 16a, we see that the largest coops have been the most open to bringing in talent from shareholder organizations. They have also been the most successful in attracting this talent, by virtue of the compensation packages and career challenges they are able to offer, along with greater resources to manage and an ability to generate broader impact. Since this group of CEOs has historically generated more growth, this becomes a virtuous cycle for those largest credit unions.

Credit unions that are successful in blending cooperative values with an eye toward value generation have had the most success in positioning themselves to attract and hire talent with shareholder experience at all management levels.

MEMBER RELATIONSHIP AND RELATED SKILL SETS TRUMP BANKING EXPERIENCE AT THE OPERATING LEVEL

Although we found that CEOs with shareholder company experience delivered greater growth without compromising profitability, executives from all three zones in the Americas prioritized "people empathy" over "functional knowledge"

Exhibit 16b: Select company performance measures by type of CEO experience and tenure in selected US credit unions[1]



Source Company websites, press announcements

1 Selected from top 100 by assets: the firms among the top 20 for which data were available, among the middle 20 for which data were available, and among the smallest twenty for which data were available

as both the prized operational skill in staff hiring decisions and the best predictor of success once hired. Those who expressed this view stressed that relationship skills were key to delivering on the member-centric promise experienced through daily personal interactions between members and coop staff. Important skills arising out of member empathy include: addressing members' needs without overtly selling, a strong community orientation, and an ability to adhere to the cooperative's particular niche, instead of trying to be "all things to all people."

OPPORTUNITIES FOR STRENGTHENING TODAY'S TRAINING EMPHASIS ON ATTENTIVENESS TO MEMBERS

Cooperative executives take pride in the investments they make in their people, emphasizing that the continuous development and honing of skills is vital to their organizational proposition and relevance. Those we spoke with invariably cited training as one of their most important talent differentiators. The insularity of the movement from the larger profit-driven banking sector also necessitates this approach. Although the focus of formal and informal training has been on employees' member management skills and know-how, several coop executives pointed out that the development of leadership and technical skills was stagnant. They perceive that skills such as "proactive management," creative marketing, and cooperative value proposition messaging were weaker within their organizations. Latin American executives were more optimistic that specialized skills could be developed through in-house training while those from Canada and the United States showed a greater affinity for sourcing specific skills via outside hiring or the use of third parties, e.g., as a way of accelerating time-to-market for key initiatives.

We find that the approach to talent plays a significant role in the cooperative bank organizational agenda. Prior CEO experience and length of service can be linked to performance, but a confluence of other factors (e.g., competitive market dynamics) preclude a definitive view on whether any particular background, set of experiences, or tenure are predictors of success. Coops use training as an important development and retention tool, but this should not come at the expense of opportunities to enhance and infuse new skills.

3.5. DOES THE ROLE OF GOVERNANCE AFFECT ORGANIZATIONAL AGILITY?

Governance – in particular the policies and practices of member representation – is one of the most important factors that distinguishes cooperatives from their shareholder counterparts. It is at the same time a powerful lever that coops can use to further their agenda, while also posing potential hazards to organizational agility. Overall, we found that the broad framework surrounding the governance of cooperative financial institutions does play an important role. To support management's ability to innovate and grow the organization's services and reach, boards need to serve as "strategic partners" with the executive teams, not "shadow managers." The duty of a progressive, well-functioning coop board should not be to drill deep into the day-to-day management or second-guess operational decisions. Rather, boards should act like boards; and because they serve cooperatives, they should also act like owners.

COOPERATIVE GOVERNANCE IS FUNDAMENTALLY DIFFERENT

Democratic member representation on boards is a hallmark of the cooperative movement. This was illustrated for us vividly by one Canadian cooperative that had elected a 19-year-old university student as one of its directors. Fundamental differences versus shareholder banks revolve around:

- The "one member, one vote" principle. Unlike shareholder banks, where one's stake equates to voting power and can translate to a Board seat, "one member, one vote" likely has a homogenizing effect on coop boards and even membership, as potential members might be disinclined to serve or even join without proportionate representation
- "Bottom-up governance". Shareholder banks tend to have a single, centralized board that operates top-down through an appointed CEO with wide latitude to define the company's operating strategy, policies and structures from the center. This "command and control"-style decision making greatly facilitates the implementation of enterprise-wide initiatives. By contrast, credit unions' boards – especially those with unbounded membership criteria operating over a large coverage area – tend to work "bottom-up," with board members selected through local elections, regional councils, second-level boards, etc.

RISK OF STAGNATION?

The governing bodies of individual cooperatives across the Americas are in need of review and in many cases renewal, given the potential for loss of market share and the need to chart new directions for the organization that will enhance the relevance of cooperative banking. Executives we spoke with cited a number of risk factors with their current governance model:

- Longer decision-making cycles created as a result of multiple governance layers, leading to lost opportunities and slow reaction to developing threats or challenges
- A diminishing ability to "pivot" strategically, leading to a long-term decline in the relevance of the cooperative bank
- Lower membership participation rates that erode the defining value of membership. Several CEOs of credit unions across all three major geographies told us that their members were not very concerned with participation, but were more motivated by convenience and pricing. We heard anecdotal references to less than 1 percent AGM participation in several instances
- Weak financial services knowledge, lack of forward thinking, and/or an inability to challenge or effectively communicate with management as a source of tension with elected Board representatives
- Suboptimal routines – e.g. frequency of board meetings, revisiting of decisions that have already been taken, lack of clarity on authority levels between parties, duplication of efforts – stalled execution.

BOARD COMPOSITION AND PREPAREDNESS AS LEVERS FOR CHANGE

Buoyed by increasing pressure from regulators to professionalize their boards, coop banks and credit unions are taking steps to make their boards more efficient. Across Latin America, the separation of duties between execution and oversight bodies continues to materialize. Increasingly, coops are requiring formalized training for their directors. In Canada, there is a particularly strong push to implement director certification requirements.

One Latin American cooperative explained that its board members are required to have basic industry knowledge and demonstrate alignment with cooperative values. A Canadian credit union has implemented continuous learning initiatives for its board, providing its directors with a comprehensive orientation and several additional information sessions. Another has a curriculum to educate the board and a policy which blocks directors from being renewed if they do not meet certain standards after one term. Others have recently been trying to attract more directors from executive and senior professional positions, who in turn can provide significant strategic input to management while maintaining their fiduciary role.

Many coop CEOs are crediting these changes with making a positive difference in the relationship between management and the Board.

BOARDS MUST BE ABLE TO CONTRIBUTE TO THE STRATEGIC AGENDA

It behooves the cooperative board to act as a strategic advisor in partnership with the CEO and the rest of the executive team, rather than as surrogate management for day-to-day operations. We heard a lot of evidence, particularly among smaller, more localized credit unions, of boards that were excessively "in the weeds." These examples emphasized the stifling effect an intrusive, tactical board can have on a credit union's effectiveness. On the other hand, where cooperatives and their boards had managed to align their priorities strategically and in partnership, the CEOs we spoke with sounded very enthusiastic about their coops' future growth trajectory.

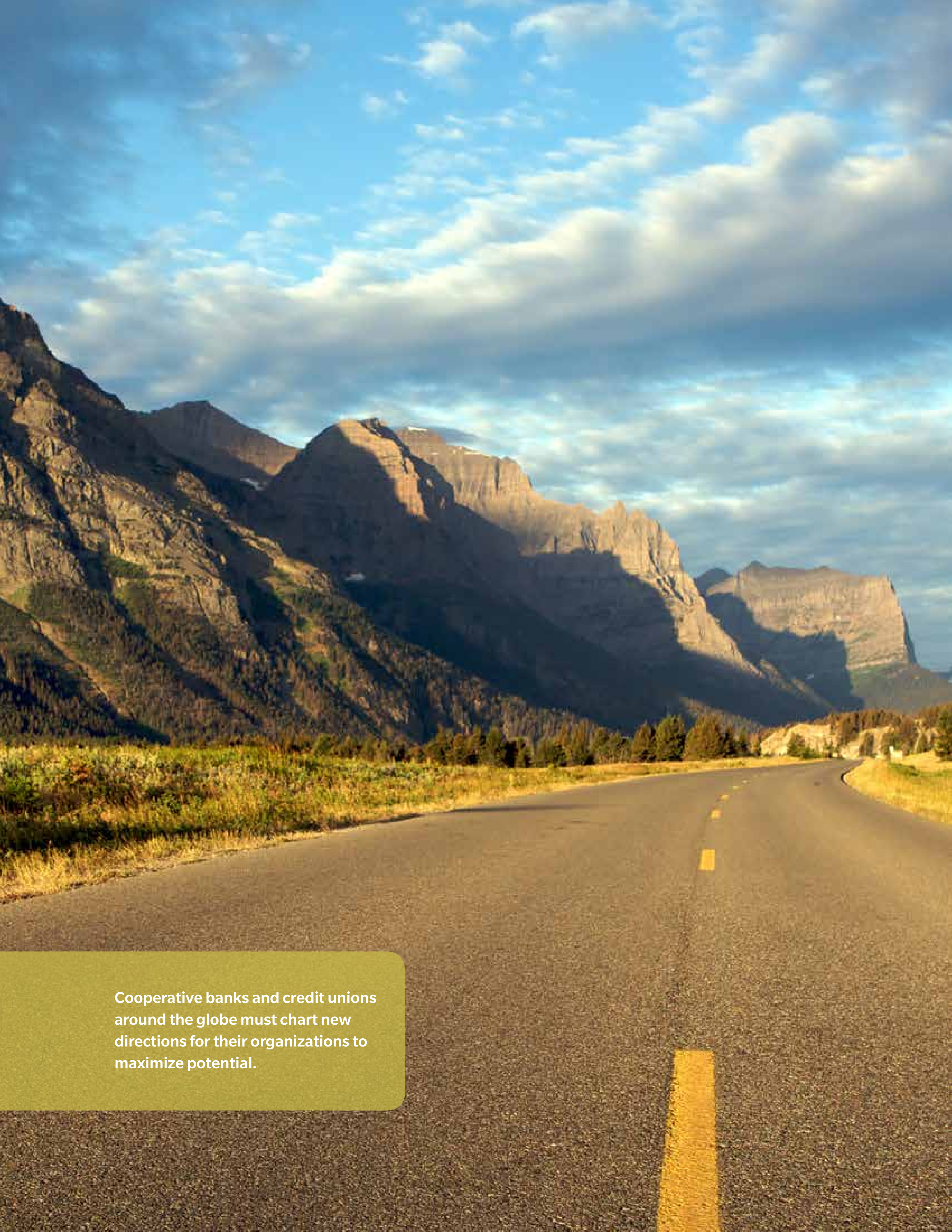
ADDITIONAL SCOPE FOR COOPS TO LEVERAGE THEIR INDUSTRY ASSOCIATIONS?

Beyond individual constituent banks or credit unions, the cooperative financial services sector features a wide array of associations and leagues at regional, national, continental, and global levels. While there are many instances of collaboration among these stakeholders (e.g., best practices sharing, training, lobbying efforts, etc), a degree of inefficiency pervades this aspect of the movement given the parallel and overlapping nature of the entities.

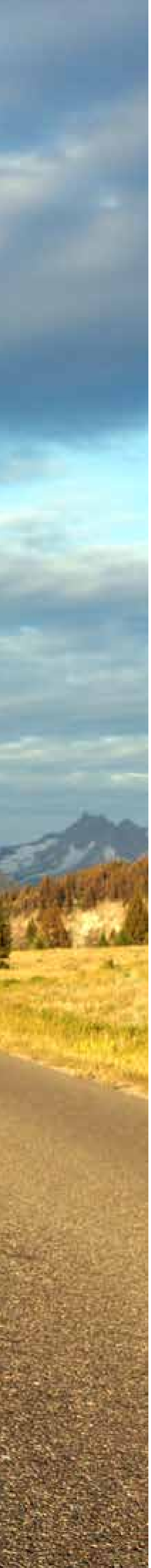
The specific roles, functioning, and sources of added-value from these entities with respect to defining the future directions for the sector were not clear to several interviewees. At the same time, association representatives and leaders we spoke to expressed a desire to be more directly involved in the macro-development of the sector.

In particular, a few North American cooperative bank executives shared the view with us that industry associations were of greater use to smaller credit unions, suggesting to us an opportunity for reimagining the role of associations and their portfolio of services to cater for cooperatives of different scale and needs.

Governance will likely remain an active area for debate within cooperative financial services given the membership ownership and participation in the sector. However, by progressively adjusting board composition and their role as strategic partners as well as advisors, cooperatives can become more effective in their marketplace. Adding industry associations into the mix as a source of advice, strategic services and strategic direction for all tiers of cooperative banks, will optimize what is now often an overlapping and diffuse set of relationships.



Cooperative banks and credit unions around the globe must chart new directions for their organizations to maximize potential.

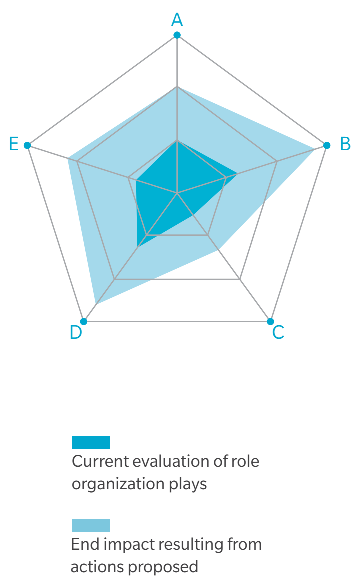


4. RECOMMENDATIONS FOR THE ORGANIZATIONAL AGENDA IN COOPERATIVE FINANCIAL SERVICES' STRATEGY

Our findings serve to highlight the organizational imperatives facing cooperative financial services across the Americas and some of the key factors that enable or inhibit their effectiveness and growth. The natural next question becomes what are the priorities for organizational design and implementation that cooperative banks should embrace to improve their long-term prospects? For example, is there a "silver bullet" that can address or solve a range of issues as once?

We did not find this to be the case. Rather, we conclude that the main opportunities for advancing the strategic agenda of coops across the Americas lie along five organizational dimensions. Exhibit 17 presents these dimensions and provides a summary of the main aspects of each.

Exhibit 17: Major opportunity areas for enhancing the role organization can play in advancing the effectiveness and growth agenda in cooperative financial services



A. OPTIMIZE MEMBER MANAGEMENT
- Governance and decision-making streamlining
- Member information management, profitability and lifecycle analysis emphasis
- Applying a growth-oriented lens on future membership

B. ENRICH EMPLOYEE BENCH STRENGTH
- Rotational talent secondments
- Targeted acquisition of outside talent – banking, retail, tech sector
- Training as a competitive differentiator

C. HONE THE INNOVATION EDGE
- Innovation focus based on members' needs and decoded hassle maps
- Dedicated measurement framework and adoption of stretch "breakthrough" goals
- Appropriate innovation portfolio diversification

D. TURBOCHARGE COLLABORATION
- Accelerated systemic sharing of best practices
- Revisiting and revising the role of associations and centrals
- Greater integration in the planning of coop banking markets

E. CHAMPION RELEVANCY BY RETHINKING CONVENTION
- Rethinking long-held precepts regarding channel strategy
- Infusion of a ubiquitous "value with values" based culture
- Long-term planning around next gen banking needs
- Commercially-inspired evangelism of cooperative values

Source Oliver Wyman perspective

The "spider-gram" shown above is a classic consulting tool for showing a graduated set of capabilities across different dimensions that reinforce and complement each other. The cooperative banks and credit unions we surveyed exhibited a range of maturity and sophistication levels across each of these dimensions. The levels attained (darker blue) indicate our assessment of the current general positioning of organizational capabilities across the sector in the Americas today. Several coops of course gave evidence of higher levels of maturity or sophistication on certain dimensions, but on the whole we did not observe systemic evidence of outperformance across all dimensions in any geography or individual coop. This leads us to conjecture that significant scope remains in each respective market to reach the next levels of organizational performance and success (as indicated illustratively by the lighter blue "webbing.") Note that the difference between this level and the theoretical maximum reflects the degree to which other performance drivers beyond organization (e.g., strategy, financial and credit policy, operations) exert a bearing on a coop's ability to exercise that dimension.

The rest of Section 4 discusses each of the organization dimensions identified above and what an 'ideal' positioning might look like. Section 5 then outlines how cooperative financial enterprises might frame their organizational blueprints to best execute along the set of dimensions.

4.1. OPTIMIZING MEMBER MANAGEMENT

PARTICIPATION IN GOVERNANCE

Because member representation is the hallmark of a cooperative bank, our initial set of recommendations begins there. We believe that a "performance-based" view of membership, in which credit unions and coop banks manage their members as assets that contribute to the overall mission of the organization benefits both the overall member base as well as the coop's agenda. Central to this proposition is the potential for improving coop governance by streamlining layers of member representative committees at the local, regional, and centralized council levels. Efforts to socialize new ideas or proposals and shorten decision cycles would be further enhanced by more compact governance bodies and a greater premium on seats, thereby helping to ensure that the broad membership is represented by the best qualified candidates. By setting qualification criteria and raising the bar for board service, two aims are reinforced: 1) that members are truly invested in the fulfillment of their board responsibilities, and 2) that they discharge their fiduciary and oversight duties with a strategic mind set and from an informed base of understanding.

A clearer division of responsibilities between member representatives serving on boards and executive management would also help maintain a focus on strategic oversight, while allowing management flexibility and authority over the operational direction of the coop and the tools and resources needed to execute it – without getting bogged down in the details of the day-to-day operations.

UNDERSTANDING TODAY'S AND TOMORROW'S "RANK AND FILE"

Beneath the layer of member representation in governance, better information is a fundamental requirement to enhance member service and better address their needs. Deepening the coop's understanding of historical behavior, in combination with direct member polling and research, are the most effective ways to ensure that future products and services will be designed to maximize relevance for its members and anticipate collective needs throughout evolving life stages.

Whether a coop's membership is large or small, urban or rural, relatively affluent or more modest, cooperative bank market intelligence should focus beyond today's membership profile. A focus on the "rank and file of the future" is necessary both as a blueprint for migrating from today's membership base to tomorrow's and as a thought exercise for imagining what the coop's target membership could or should be. Such an objective re-assessment and challenge to legacy thinking can stimulate a more open dialogue on how the future membership might evolve, and lead to structural decisions (e.g. strategies for moving beyond bounded membership).

4.2. ENRICHING EMPLOYEE BENCH STRENGTH

The dynamics of the cooperative banking marketplace, characterized by ubiquitous competition, including for talent, requires urgent and creative methods for building the skills base in the sector through internal and external means.

NURTURING TALENT FROM WITHIN THE SECTOR

Cooperatives can learn from each other – especially those that have gone through existential or strategic challenges. Rotating in experienced staff from high performing entities provides a way for successful coops to "give back" while offering development opportunities for their prized staff, whether at home or further afield. Equally, having managers from fledgling credit unions work in more established coops – gaining experience and techniques that can be applied when they return home – represents a real opportunity. These exchanges would allow the entire sector to benefit, transferring know-how from larger, more sophisticated coops and credit unions to less established or mature cooperatives across geographic lines. In addition, the relationship value resulting from these exchanges can be tapped to facilitate collaboration in other dimensions, such as innovation.

TARGETING RECRUITMENT OF OUTSIDE TALENT

Bringing in talent with diverse experiences enriches overall bench strength and fuels healthy internal discussion. The increased diversity of perspectives obtained by considering targeted hires from shareholder banks can create additional debate in the boardroom, but undoubtedly provides a broader view on potential future direction.

Talent acquisition from shareholder institutions should emphasize functional roles that drive the growth agenda – including strategy, product management, marketing, sales, innovation, and operational excellence. Shareholder banks in particular can serve as high-performance training grounds due to the demands of their marketplace, from which coops may benefit from. The ability to "acquire" professional expertise, versus growing it internally via training and development, represents an essential potential complement to typical talent strategies. Assuming compatibility of these new resources with the cooperative mission, their presence can represent a positive signal to the workforce that the coop is invested in talent development and has high performance expectations.

We do not see external recruiting from shareholder financial institutions as the sole panacea to cooperatives' talent needs. Acquiring talent from other information-based industries, such as the retail sector or the internet economy, can complement financial services know-how by sourcing fresh perspectives in marketing, segmentation, and branding – in addition to securing disruptive technologies aimed at transaction banking and alternative distribution channels. Growing technical bench strength from industry in general would engender more "big picture" technology and operational excellence thinking, increase the effectiveness of the interaction between IT departments and the business lines, and also help catalyze innovation.

FOCUSING TRAINING ON THE COOPERATIVE PROMISE

Given that serving members - as opposed to selling to clients - is a hallmark of the cooperative banking experience, in-house training efforts should continuously (and pervasively) focus on empowering cooperative principles in all aspects of the staff's work: how they structure, prioritize and carry out their activities; how they interact with members; how they follow through; etc. The "cooperative promise" itself can evolve as the coop's value proposition changes, but requires that the training program be adapted accordingly.

Particular attention should be paid to the onboarding of new staff from adjacent career paths to the cooperative. This could take the form of a "two-track" integration program: one for the new executive or skilled professional joining the coop, and one for the coop management team responsible for her acculturation. The purpose of this program would be to ensure rapid assimilation of the cooperative values on the part of new hires, but equally important, the ability of existing management and operating teams to benefit from the outside perspectives and experience of these new employees. New talent and skills sets are only as valuable as the coop's ability to absorb them – they can be incorporated more formally in coop training programs, e.g., through industry lessons learned, topical discussions, brown-bag luncheons, etc. designed to leverage this outside experience.

4.3. CHAMPIONING RELEVANCY BY RETHINKING CONVENTION

Coop banks cannot afford to become complacent about their role and value in the financial services landscape. By continuously challenging prevailing wisdom, individual cooperatives may be able to ensure an effective path toward a successful future.

INCULCATING A "VALUE WITH VALUES" CULTURE

The cooperative sector needs to counteract the notion that generating value and adhering to cooperative values are somehow in opposition. This begins with the recognition that the surrounding environment has changed, perhaps inexorably. New regulatory scrutiny and capital adequacy rules, ever-increasing competition from traditional and non-traditional players, product proliferation and remote channel reach, and greater discernment and wallet-sharing by members can all be expected to continue and likely increase. At the same time, in some markets demographics are shifting in the coops' favor – a new generation of members awaits, one which is far more civic-minded, socially-conscious and motivated by causes such as 'green growth,' 'local food' and 'gender opportunity.' The obligation remains with coops to put the greatest emphasis on nurturing values, as well as generating value, for their members.

To assist in this, coops should actively pursue – within the context of their value proposition and membership promise – operational effectiveness measures to the same extent as their shareholder counterparts. Comparing cooperative banks' cost-income ratios and other key performance indicators to shareholder banks' provides the impetus and basis for action in operational and channel efficiency, including staff right-sizing.

As the resulting benefits to the membership are realized, coops could gain further from more commercially-inspired "evangelism" of their value proposition. Reinvigorating messaging through more targeted and nuanced marketing – a departure from tradition – could enable cooperatives to capture share of mind in today's world of overly-hyped and -saturated brands. They could appeal to a new generation of engaged members, while reinforcing their cooperative cultures internally. External marketing and branding can work hand-in-hand with product development and service departments to create a differentiated value proposition both to existing members and prospective ones. Messages that appeal to cooperative values – stewardship, community, equity – could breathe new life into cooperative banking, facilitate marketplace outreach, and create affinity by catering to members' sense of belonging. Financial cooperatives should view this kind of marketing spend as revenue generation, not sunk cost, and prioritize activity and budgets accordingly.

LONG-TERM PLANNING OF NEXT GENERATION BANKING NEEDS

Coop banks need to redouble their efforts across the board on the needs of future members. In the main, these represent a younger demographic than today's typical coop membership. In more developed markets, this segment carries a higher credit load which helps to finance coop operations. In developing countries, where personal credit requirements tend to extend into senior years and the labor market is skewed towards the young, attracting a younger, productive membership helps to improve the deposit base.

Coop banks must become more adept with, perhaps even leaders in the use of alternative channels such as social media that resonate with this demographic, while developing a complete member lifecycle approach in their strategic thinking. We found evidence of this way of thinking among even the smallest credit unions, e.g., early use of hand-held phones to make payments. This strategy could have significant implications for the management of retained earnings, since coops may need to put greater emphasis on investing in their future members' value proposition than returning value to current members.

REVISITING LONG-HELD PRECEPTS ABOUT CHANNEL STRATEGY

An area where coops urgently need to rethink their organizational footprint is in origination and distribution, which have historically relied on a physical branch network. Some coops/credit unions we spoke with have taken this leap of faith (usually driven by the economic realities of their geographic scope) – and have realized that their social mission can not only be achieved via an in-house branch model. Nevertheless while some markets already feature partnership agreements that allow coop members to obtain services via alternative networks, there is still ample leeway for:

- Promoting the benefits to members of alternative digital channels by the front office
- Forming alliances with telecoms providers to further promote the uptake of digital services in communities with previously limited access.
- Incorporating mobile vehicle banking especially in rural or remote communities

As coop banks rethink their target channel mix, they need to become disciplined about measuring and managing the use and profitability of the various means of interacting with members. This includes assigning the appropriate resources and budget to effect the desired migration of member traffic to more cost-efficient channels.

TECHNOLOGY AND OPERATIONS INVESTMENT REQUIRED

New, robust technology and operations infrastructure is required to support the array and complexity of today's banking requirements and this necessitates a critical mass of investment. Since capital-raising in cooperatives is limited to retained earnings, cooperative banks and credit unions need to be purposeful and highly organized in their IT infrastructure investment planning.

4.4. TURBO-CHARGING COLLABORATION

Proactive collaboration among the diverse groups of cooperative stakeholders that exist today in financial services can be raised several notches. A concerted effort toward this goal would both benefit individual bank cooperatives and align well with the movement's founding principles.

ACCELERATING SHARED BEST PRACTICES AND AVOIDING PITFALLS TO GROWTH

A sectoral agenda that emphasizes the levers that drive long-term growth and financial sustainability, e.g., membership portfolio management, new segment-based marketing, R&D best practices, product/solutions development, and technology optimization, would help focus the entire sector.. Through systematic sharing of "what to do" and "what not to do," cooperative financial services can build a more competitive market proposition together. Appointing leadership within each organization with explicit responsibility for incorporating and generating "learnings" and encouraging regular dissemination of intellectual capital would allow more substantial progress. This also suggests a more active role for the sector in applied knowledge management.

REVISITING THE ROLE OF ASSOCIATIONS AND LEAGUES

Beyond best practice sharing, there are other measures that the cooperative financial services sector can take to optimize the performance of its constituent banks and credit unions. We believe there is opportunity to rationalize and refocus coop banking association and league structures across the Americas. This would include a perspective on the number and configuration of associations and leagues that would best serve the interests of the sector going forward. Rationalizing the missions and spheres of influence at all levels – state/provincial, regional, national and international – would drive inefficiency and overhead out of the system and streamline channels of communication, and could promote more substantive collaboration among constituencies. Adopting the right transformational agenda and augmenting the effectiveness of the leagues and associations would reinvigorate their importance and send a clearer signal that they can play a powerful role in charting the future development of cooperative financial services. Strong associations provide thought leadership and direction that rise above the interests of individual cooperatives to encompass the collective benefit of the entire sector.

GREATER COORDINATION OF MARKETPLACE ACTIVITY

Emulating their shareholder counterparts – but on a collective basis – independent cooperatives should pursue operational synergies more purposefully. Increasing the deployment of middle- and back-office hubs and shared service centers, which would be co-funded by groups of cooperatives coming together, is a proven path to the benefits of operational scale and pooled expertise, when critical mass of one's own is lacking. Also, where relative efficiencies warrant it, a greater openness to using specialized third party services would allow redirecting scarce resources toward strategic or core activities. These pursuits of marketplace efficiency are very consistent with cooperative values; they demonstrate to members that their interests are being held top of mind.

Shared development costs for technology among coops however requires a high degree of coordination – but the overhead may be worth it to significantly increase access for smaller or more remote coops that would not be able to take advantage of such initiatives on their own.

Finally, a more concerted effort to develop cooperative financial services' marketplace footprint should be prioritized. One of the key advantages coops have is the ability to act as a movement and within this context strategy-setting and decision-making can lead to market share gains for the sector as a whole. Consolidation and critical mass are central to achieving this goal, and the prospect of smaller, less viable coops partnering and combining or consolidating to a greater degree in order to compete should become commonplace.

We note that adopting a more "holistic" approach toward market development for the benefit of the cooperative collective will continuously challenge coops and their members to place individual agendas to the side as a roadmap for the entire sector is created.

4.5. HONING THE INNOVATION EDGE

Innovation must be viewed as an essential ingredient for growth as cooperative banks and credit unions look to renew their propositions for serving members and focusing on the solutions of the future. Sporadic, lengthy, diffuse, or unfocused initiatives will be too little, too late to ensure that coops can thrive. Because of their typically limited resources and small, part-time teams, coops must set an innovation agenda comprising:

- A deep understanding of members' hassles and preferences
- Appropriate diversification of the portfolio being pursued
- Tracking, measuring outcomes, and integrating initiatives in a program that maximizes impact.

A focus on addressing members' hassles and resolving future needs helps direct resources to the areas where they can have the most benefit, the soonest.

BASING INNOVATION ON MEMBERS' HASSLES AND FUTURE NEEDS

A focus on addressing members' hassles and resolving future needs helps direct resources to the areas where they can have the most benefit, the soonest.

Front-line staff in coops should be empowered to poll members on their immediate and long-term needs during the course of regular interactions, enhancing their own engagement and participation in the coop's future growth. This approach should be complemented with targeted customer research best organized, we have found, through focus groups led by trained staff. A broad cross-section of members should be included, ranging from satisfied members to those who are at risk of quitting.

Additional lenses of how products are used and how members behave are important for coops to become more proactive in charting the services and mix of products that will increase value to members. However, the most proactive cooperative banks will not limit themselves to analyzing the needs of current members. Rather, they will seek to identify and engage with future prospective members to create an innovation agenda that is geared growth – both of members and assets.

Prior to launch, innovation efforts should be evaluated through additional filters as well, for example alignment with overall business objectives, and competitive market positioning. The financial equation is vital too; the expected net present value of approved projects has to be positive at the appropriate hurdle rate. A track record of failed or unprofitable innovation attempts can dampen the creative spirit and openness to change of even the most progressive coop.

DIVERSIFYING THE INNOVATION PORTFOLIO

The innovation portfolio should be balanced between internally- and externally-facing initiatives. Though new products and services usually have the most cachet and management attention, “behind the scenes” innovation in the form of process innovation or technology renewal can have a profound effect on the coop’s overall performance and the member experience.

While most innovation tends to be incremental, we believe that cooperative portfolios should include at least a 20 percent allocation for “stretch R&D” with the potential for adapting the business model and developing whole new markets.

A DEDICATED FRAMEWORK FOR MONITORING AND MEASURING INNOVATION

Systematic approaches must be implemented to govern innovation effectively. Programs should be formalized, starting with the identification of “change agents” charged with harnessing ideas from across the organization. Giving a member of the top management team visible responsibility for driving the innovation agenda can motivate all employees and demonstrate seriousness of intent.

A dedicated innovation pipeline with specific financial, market, and risk criteria is often necessary to distinguish from “business-as-usual” projects, and to ensure that these initiatives do not get de-prioritized in favor of the day-to-day business. The separate pipeline also helps remind management of its commitment to innovation and to approach these projects with an open-minded view of risk and reward.

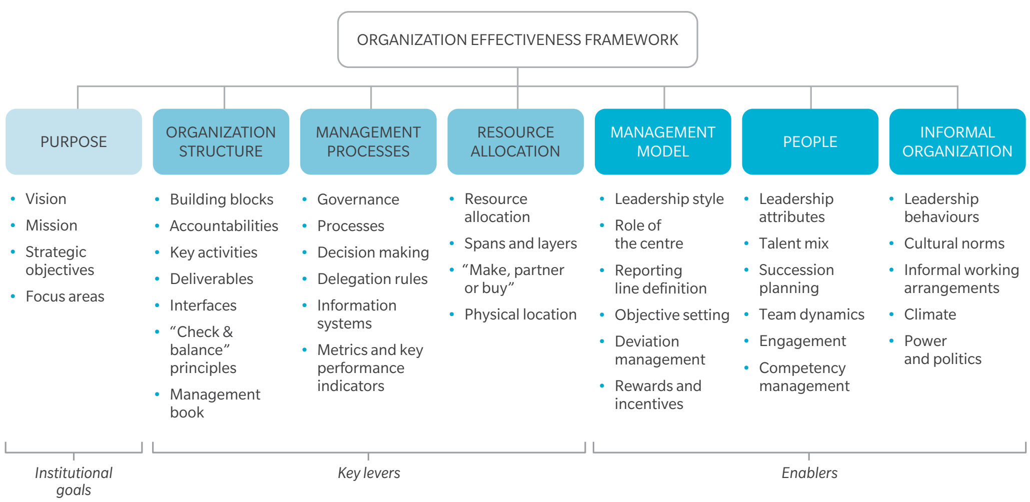
By focusing on organizational effectiveness and growth, cooperative financial services can play an evergreen role in ensuring financial inclusiveness and opportunity in the communities they serve.

5. PRACTICAL APPLICATIONS: IMPLICATIONS FOR THE ORGANIZATIONAL BLUEPRINT

The previous section established the priority areas for cooperative banks to reinforce their organizations in the pursuit of sustainable growth and long-term effectiveness – the 'why' and 'what' if you will. In Section 5, we make actual recommendations in the form of actions coops' management and boards can undertake to effect real changes in their organizational DNA – the 'how'.

Exhibit 18 describes the building blocks of Oliver Wyman's organizational effectiveness framework. It frames the components of institutional goals, supported by definitions of key organizational levers and enablers. Below each building block are descriptors of the key elements making up that organizational capability.

Exhibit 18: The organizational effectiveness framework serves to identify the key focal areas for improving impact



Source Oliver Wyman perspective

Using this framework, in this section we offer specific prescriptions for an organizational blueprint that will help improve the ability of coops and credit unions to deliver on their growth and effectiveness agendas. In thinking about the applicability of these to their particular circumstances, individual cooperatives will first want to evaluate where they fall on the maturity diagram (see Exhibit 17), evaluate their current situation and then select their individual priority areas.

PURPOSE

- Develop and manifest a vision for growth at all levels, internally from the Board and CEO down and externally via "enthusiastic evangelism" of coop value and values, employing proactive member marketing and branding.
- Incorporate innovation goals into strategic objectives, framing initiatives as critical to the future of the organization and linking these directly to the individual coop's specific mission and context.

ORGANIZATION STRUCTURE

- Help the CEO chart a growth trajectory by boosting growth-focused staffing (e.g., strategy, innovation, marketing, relationship banking) and hiring strong operational seconds-in-command.
- Drive for shareholder-bank level FTE efficiency by benchmarking to the best performing peer coops and shareholder organizations.

MANAGEMENT PROCESSES

- Optimize board operations and membership by professionalizing qualification requirements for member representation, defining appropriate consultation and communication cadences, and creating a strategically-oriented committee structure focused on growth, innovation, and membership management.
- Measure and aggressively manage growth-oriented performance metrics by leveraging appropriate business intelligence and CRM tools in order to implement data-driven member-centric value proposition design processes.

RESOURCE ALLOCATION

- Include ring fences and budgetary earmarks for growth and innovation agenda initiatives, actively ensuring that resources are assigned to those initiatives and not squeezed out by business as usual concerns.
- Take a long-term view of managing retained earnings focused on supporting the growth agenda, including subsidizing switching incentives to drive the acquisition of attractive new members and financing critical capital projects and consolidation plays.
- Build when internal expertise is available and opportunity cost is not excessive, buy when cost-effective solutions are available, and partner appropriately when stakeholders share goals and bring appropriate resources to the table for the implementation of growth-oriented initiatives (particularly if the partnering is for the greater good of the coop movement).

MANAGEMENT MODEL

- Introduce growth-oriented objectives and incentives for all staff from senior-most managers down to the front lines.
- Increase the role of the center in multi-level coop banks in decision making on growth-oriented initiatives, recognizing that structural changes typically need to be driven top-down, having been

informed via increased coordination with association and league management on overall industry direction.

- Coach senior leaders and middle management in adopting a more entrepreneurial perspective.

PEOPLE

- Formalize bi-directional training exchange programs between coop banking entities, prioritizing functional areas including strategy, marketing, innovation, and socializing lessons learned.
- Acquire outside talent for key growth-oriented roles from a range of sources, including shareholder banks, retailers, new internet economy companies, and technology-focused development companies, and train the incumbent peer team to best take advantage of the new external perspectives.
- Hire and promote based not only on traditional skills but also on a growth-culture fit, including risk tolerance, long-term orientation, and demonstrated growth track record.

INFORMAL ORGANIZATION

- Nurture an entrepreneurial mindset by increasing risk tolerance in macro business decisions, providing "permission to fail" and actively encouraging the questioning of long-held precepts regarding membership and the value proposition.
- Proactively allocate CEO bandwidth and visibility to growth-oriented functions, and celebrate growth-oriented successes through internal communication.
- Root out negative climate issues by periodically polling the organization's to identify areas for improvement, raising issues to the board level and focusing on addressing entrenched obstacles to change.

CONCLUSION

Throughout our study, as we spoke to cooperative bank and credit unions leaders across the Americas from the Canadian Prairies to the far reaches of the Southern Cone, we were impressed by their profound shared belief in the cooperative model and their determination to put members first. In some cases, cooperative leaders face significant challenges to their model and are working hard to improve their businesses and better serve their constituents. While some of the long-held precepts within the cooperative world may have inadvertently hindered the growth prospects of coops, exciting times lie ahead. We are confident that by addressing the organizational levers we have outlined in this report, cooperatives can improve their performance and increase their impact. A conscious effort to rethink and recast precepts will invigorate the industry as it evolves over the next generation. We express great optimism for the future of the movement and its ability to successfully chart a positive growth agenda.

APPENDICES

METHODOLOGY

This study was compiled through a combination of the following major sources by the Oliver Wyman project team:

- Analysis based on financial and organizational data from cooperative banks and credit unions
- A series of senior management interviews with cooperative banking executives throughout the Americas
- Interviews with members of the movement's political bodies, focused on global trends perceived within the sector
- Discussions with academics and members of relevant think tanks
- Review of internal Oliver Wyman case studies
- Research and analysis of third party literature
- Internal work sessions, framework analysis, and determination of recommendations

BIBLIOGRAPHY

1. Groeneveld, J. & Llewellyn, D.T. (2012), Corporate governance in cooperative banks
2. Oliver Wyman (2008), Cooperative Bank: Customer Champion
3. Oliver Wyman (2012), Banking on values, building on agility
4. Oliver Wyman (2014), Leveraging the cooperative difference to adapt to a new environment

DATA SOURCES

Data was obtained from the following sources

- SNL
- Bankscope
- International Observatory of Financial Services Cooperatives (HEC Montreal)
- International Summit of the Cooperatives
- Annual & CSR Reports
- Company websites, investor and other presentations

INDUSTRY ASSOCIATIONS, STATE BANKS, REGULATORY BODIES, AND THINK TANKS

Executives at the following institutions were polled, providing important perspective on industry direction.

COUNTRY	INSTITUTION
Canada	Credit Union Central of Canada
Chile	Federación Chilena de Cooperativas de Ahorro y Crédito
Colombia	Confederación de Cooperativas de Colombia
Mexico	Banco del Ahorro Nacional y Servicios Financieros
Mexico	Confederación de Cooperativas de Ahorro y Préstamo de México
Panama	Confederación Latinoamericana de Cooperativas de Ahorro y Crédito
Peru	Federación Nacional de Cooperativas de Ahorro y Crédito del Perú
USA	Cornerstone Credit Union League
USA	Filene Institute
USA	National Association of Mutual Insurance Companies
USA	World Council of Credit Unions

COOPERATIVE BANK PANEL

Oliver Wyman interviewed executives at a representative sample of cooperative banks and credit unions in Canada, the United States, and Latin America. Interviews were held with very senior-suite members at each of the entities below.

COUNTRY	COOPERATIVE BANK
Argentina	Banco Credicoop
Brazil	Banco Cooperativo do Brasil
Brazil	Banco Cooperativo Sicredi
Brazil	Banco do Brasil SA
Brazil	Sicoob Central Northeast
Canada	Affinity Credit Union
Canada	Citizens' Bank
Canada	Coast Capital Savings
Canada	Conexus Credit Union
Canada	Desjardins
Canada	Meridian Credit Union
Canada	Prospera Credit Union
Canada	Servus Credit Union
Canada	Steinbach Credit Union
Canada	Vancity
Colombia	Grupo Coomeva
Mexico	Caja Popular Mejicana
United States	Alliant Credit Union
United States	CUNA Mutual Group
United States	Element Federal Credit Union
United States	Forum Credit Union
United States	United Federal Credit Union

For additional information regarding this report and cooperative banking in the Americas, please contact the authors of the report:

Andrew Hanff, P. Eng.
Principal

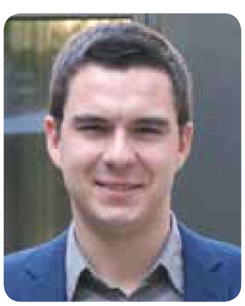
Andrew is based out of our Montreal office and brings over 20 years of international experience across financial services, B2B, and other sectors. With a value-based management focus, he assists clients principally in the areas of strategic and business design, growth initiatives, operations and cost improvement, and organizational transformation and design.

andrew.hanff@oliverwyman.com +1 514 841 7954

John Boochever
Partner

John is a senior partner based in Washington, DC, and New York, who has 25 years of experience advising senior executives across their range of organizational, management, operational, and systems effectiveness issues at the C-suite level. His consulting work has focused on helping senior clients think through the implications of their strategies in terms of organizational and operational capabilities with a focus on top-tier financial institutions and their subsidiaries in universal banking.

john.boochever@oliverwyman.com +1 646 364 8433



Julian Dean
Consultant

Julian is a consultant based in Oliver Wyman's New York office. He has worked on engagements for banks, insurance companies, and financial market infrastructure providers, advising on strategy, operations, finance, and risk. He holds an AB in Political Economy from Princeton University, where he researched the implementation of United States financial regulation post-crisis.

With offices in 50+ cities across 25 countries, Oliver Wyman is a global leader in management consulting that combines deep industry knowledge with specialized expertise in strategy, operations, risk management, and organization transformation. Oliver Wyman is a wholly owned subsidiary of Marsh & McLennan Companies [NYSE: MMC]. Follow Oliver Wyman on Twitter @OliverWyman.

For more information please contact the marketing department by email at info-FS@oliverwyman.com or by phone at one of the following locations:

AMERICAS
+1 212 541 8100

EMEA
+44 20 7333 8333

ASIA PACIFIC
+65 6510 9700

www.oliverwyman.com

OLIVER WYMAN