

State of the System

A briefing for
credit union technologists
and tech providers

3 October 2024

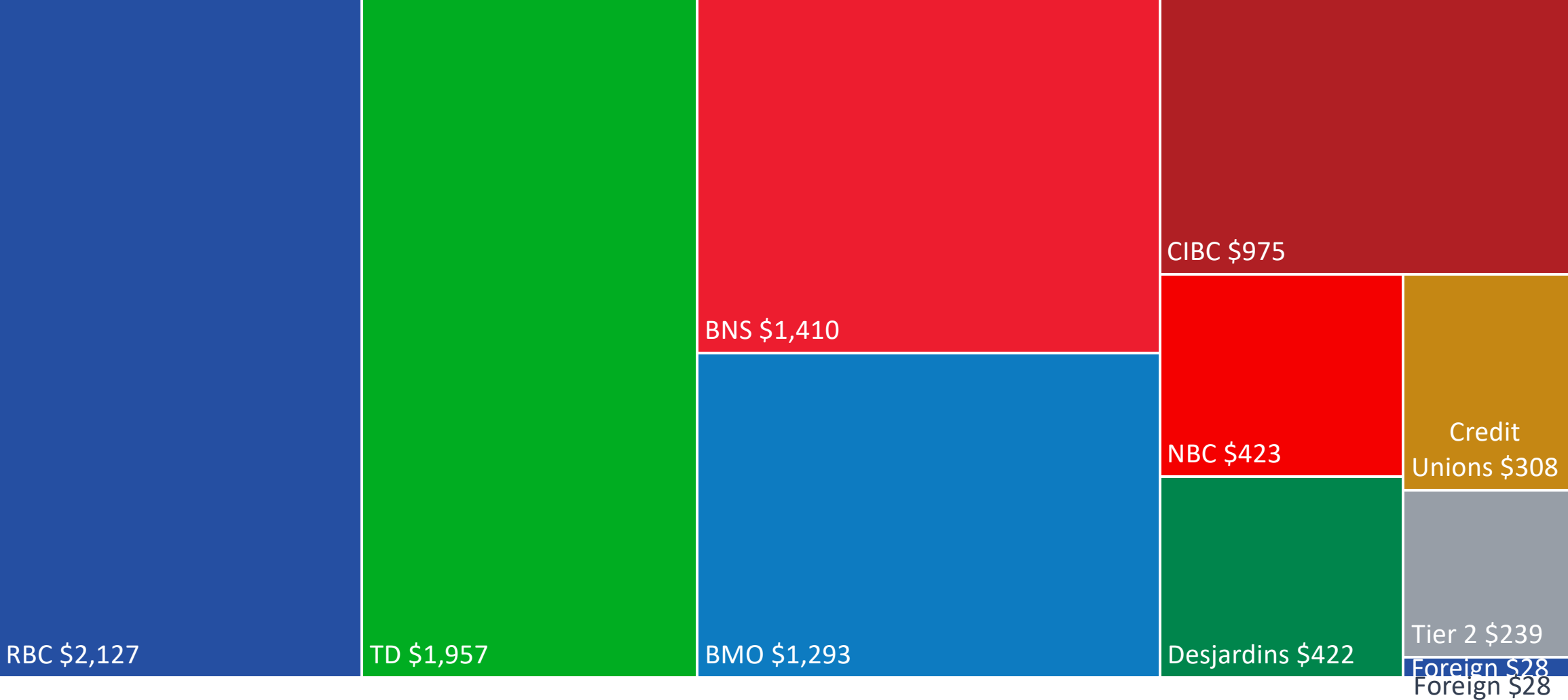


Today's agenda

- 1. Sizing up the competition**
2. Credit union sector current state
3. Implications for technologists
4. Discussion

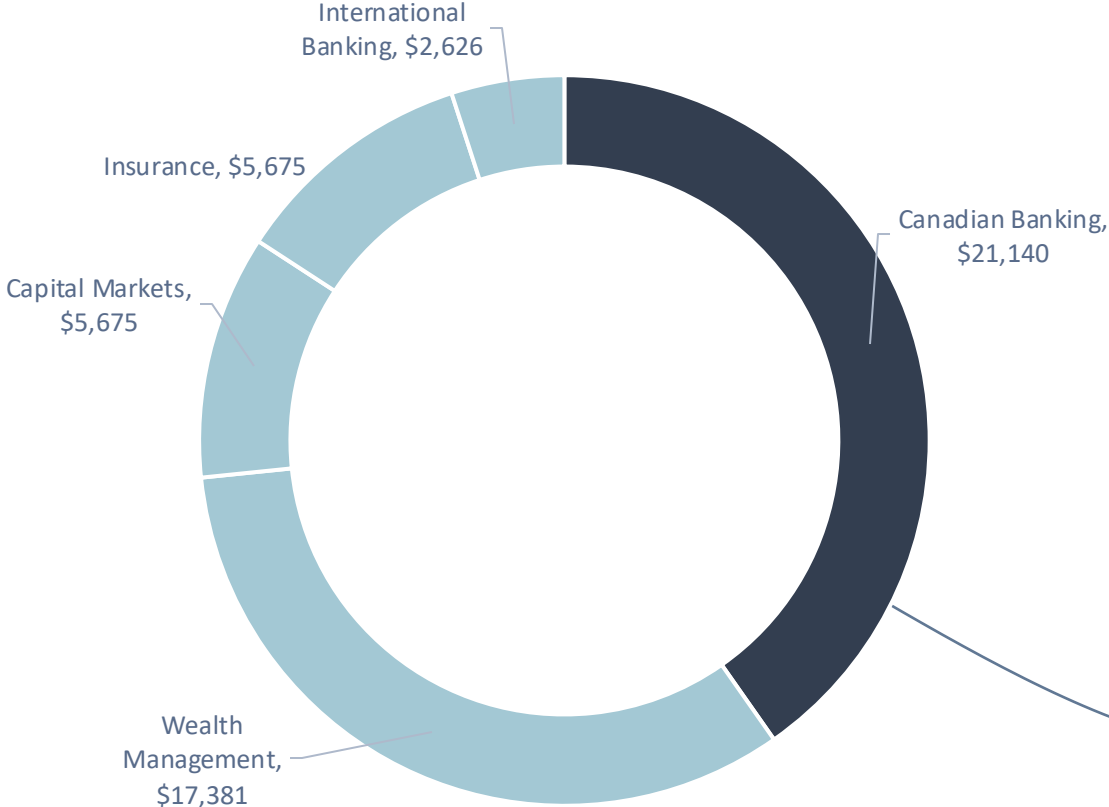
Canadian banking is six companies in a \$9T trenchcoat

Total Assets, FY2023 (\$B)

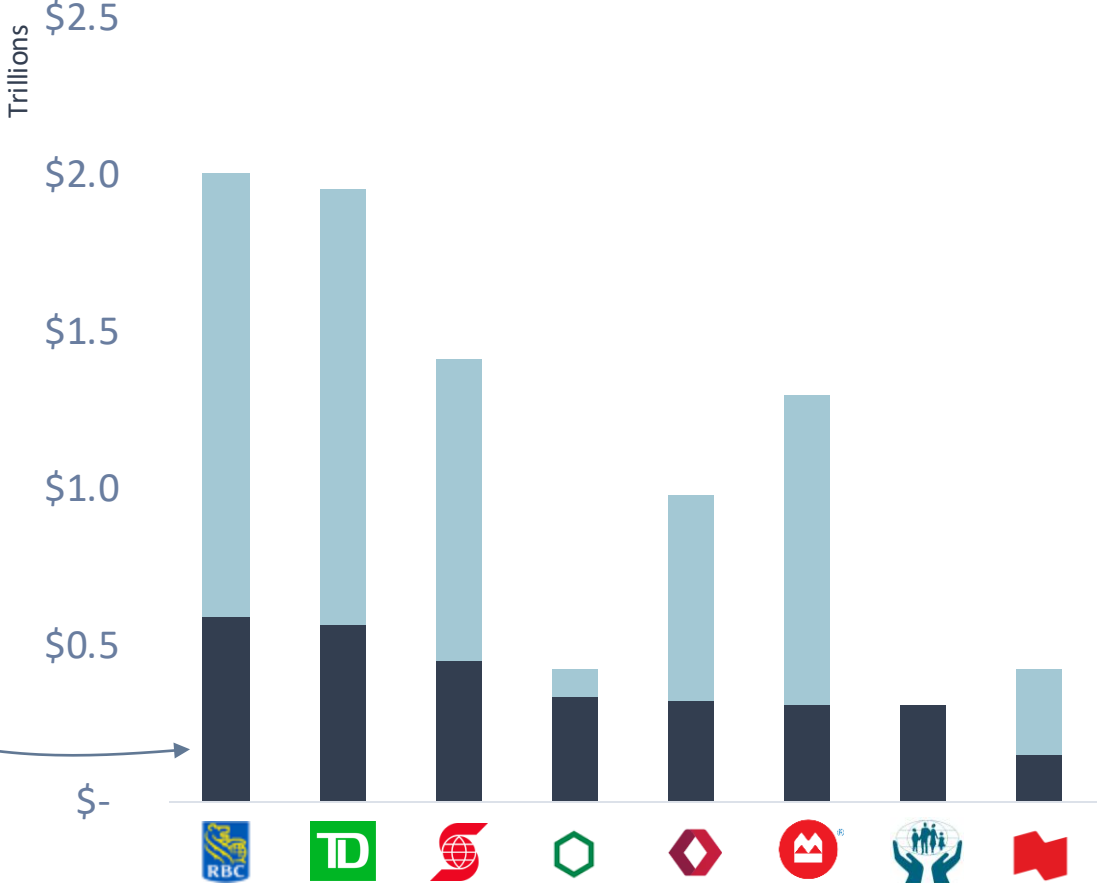


Banks are heavily reliant on Canadian personal and commercial revenue

RBC Revenue by Segment, 2023 (\$B)



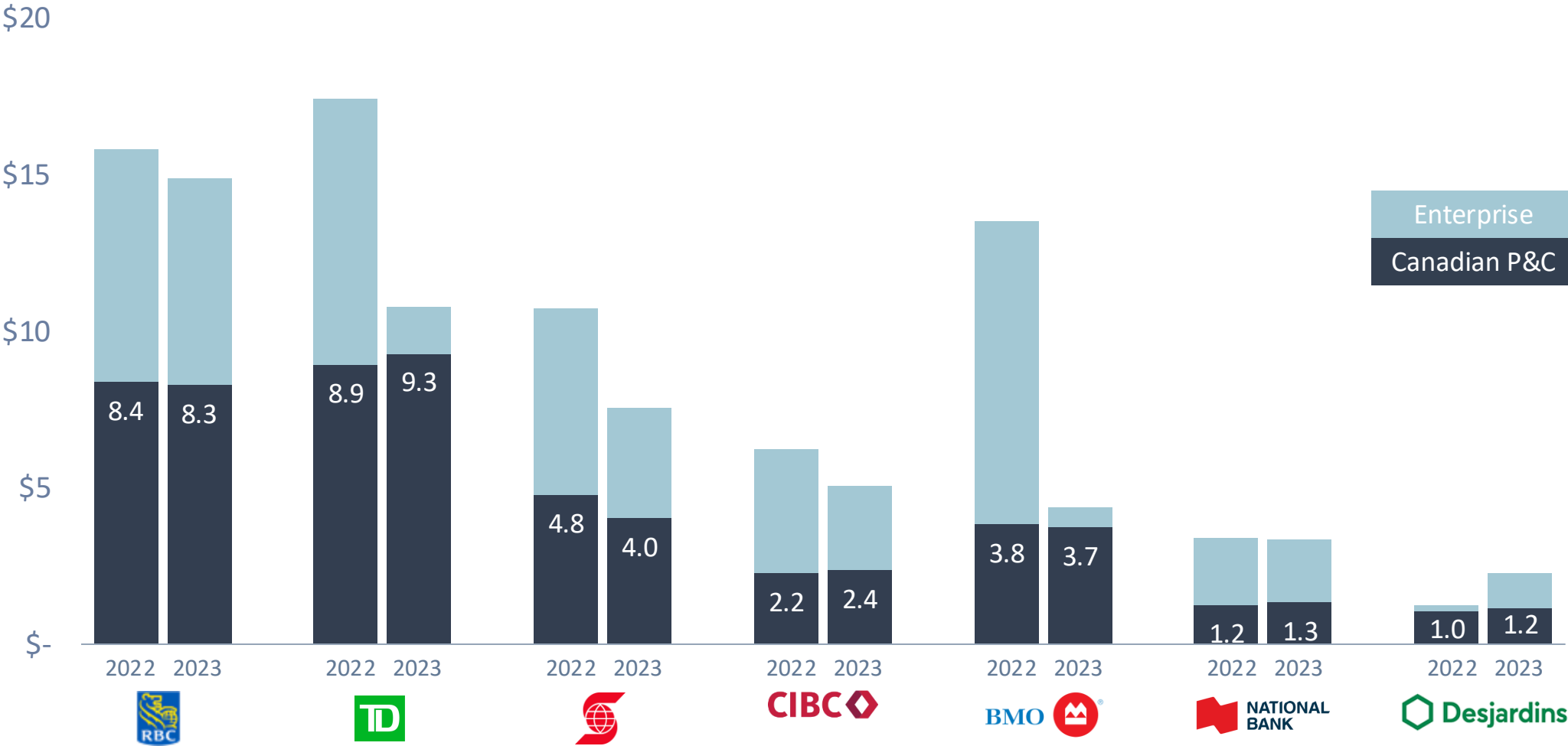
Canadian P&C and Total Assets by FI, 2023 (\$T)



Source: Annual Reports, CCUA, DMSA analysis. Each FI defines Canadian P&C differently – annual report figures are used

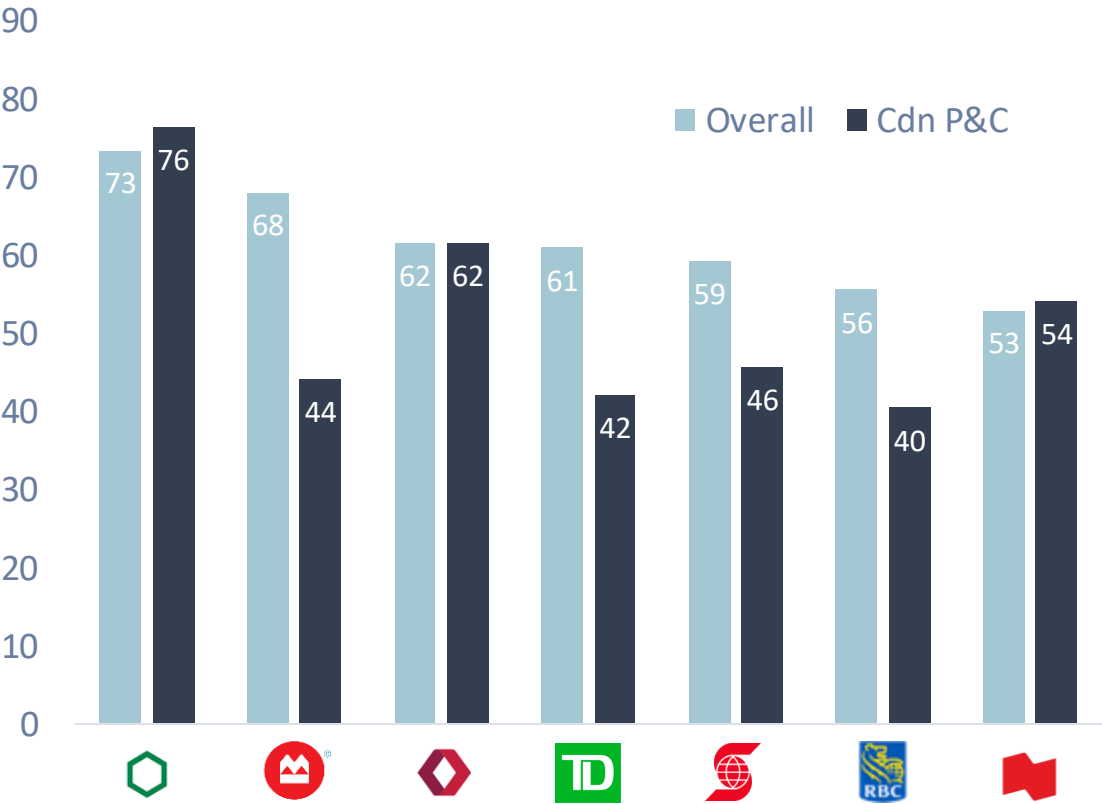
Canadian P&C has been a beacon of stability over the last two years

Canadian P&C and Total Net Income, 2022 vs 2023 (\$B)

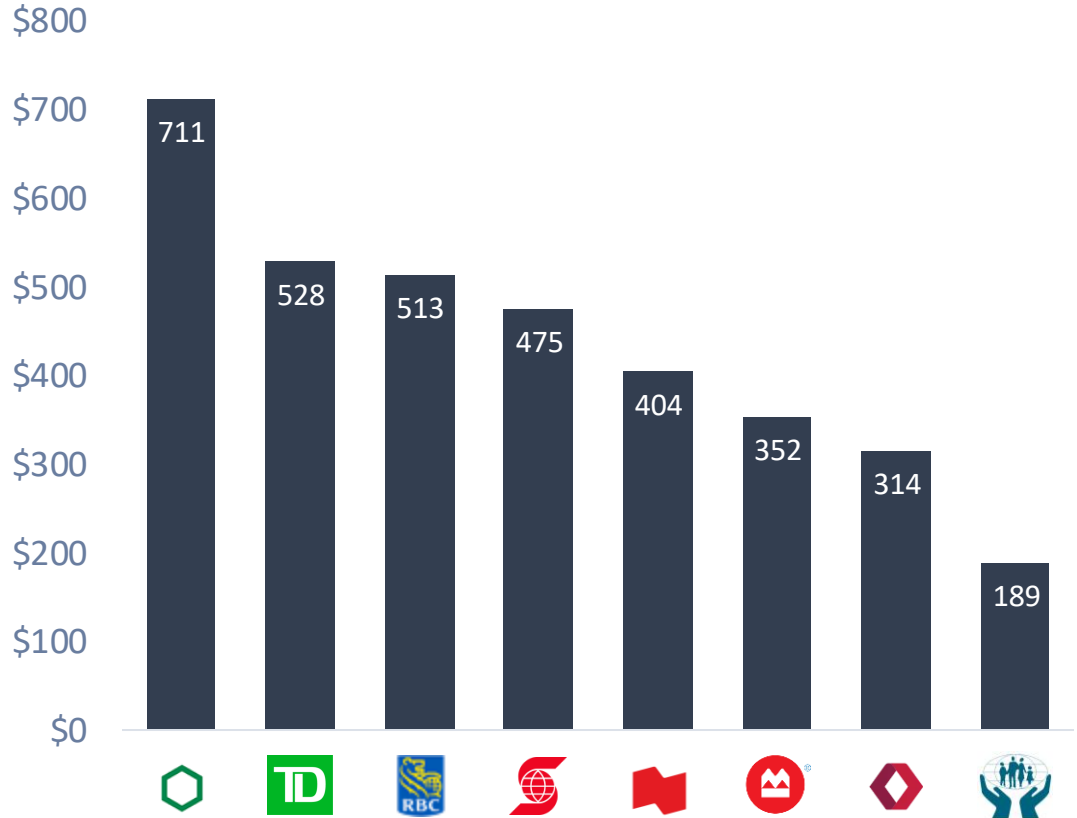


Operating efficiency is a continuing focus for big banks

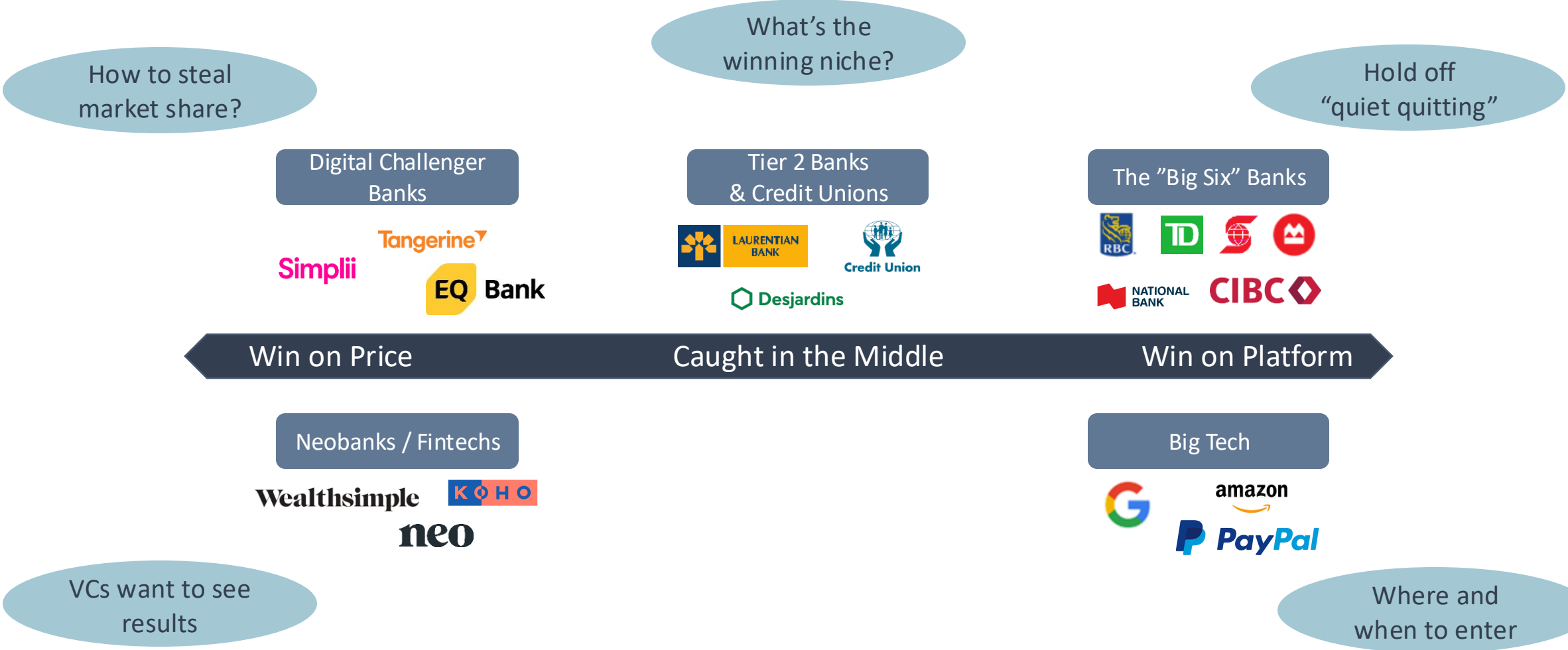
Enterprise and Canadian P&C Efficiency, FY2023



Canadian P&C Assets/Branch, FY2023 (\$M)



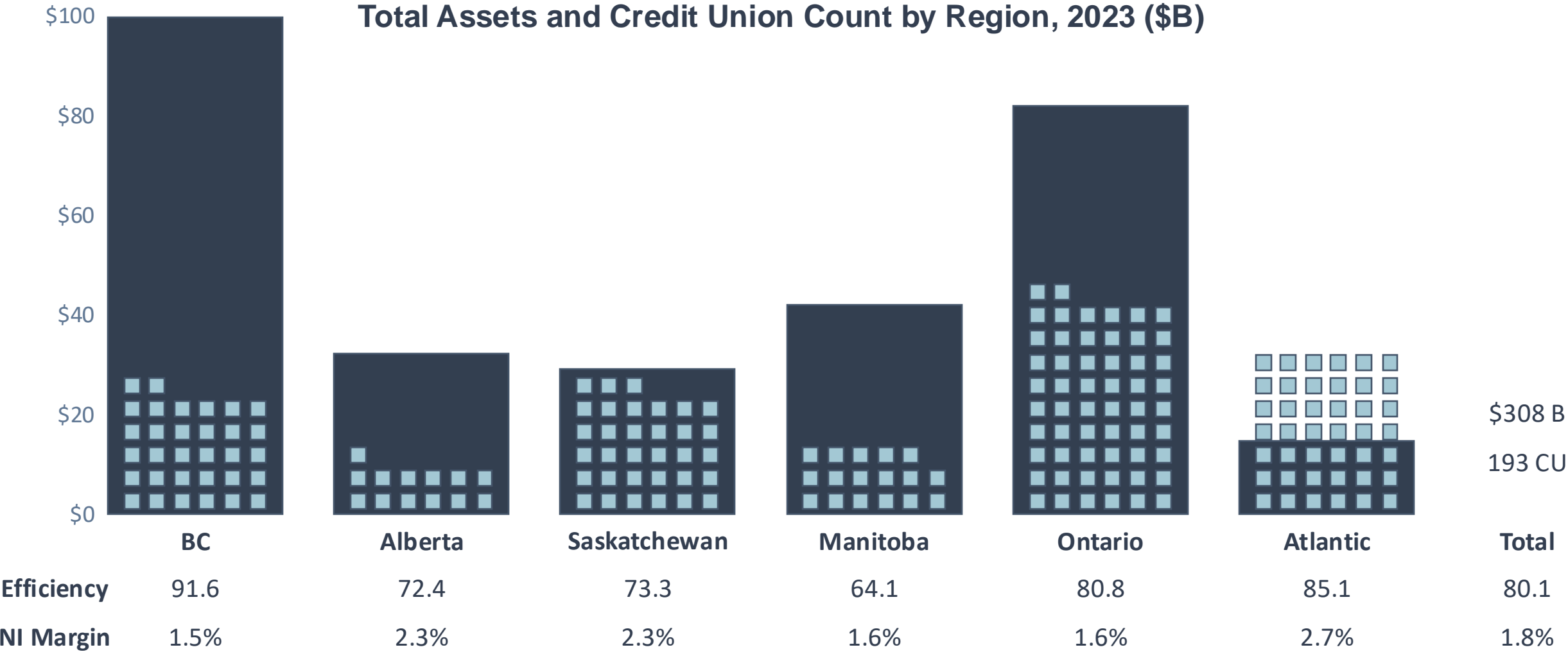
The Big Six are holding off the competition, at least for now



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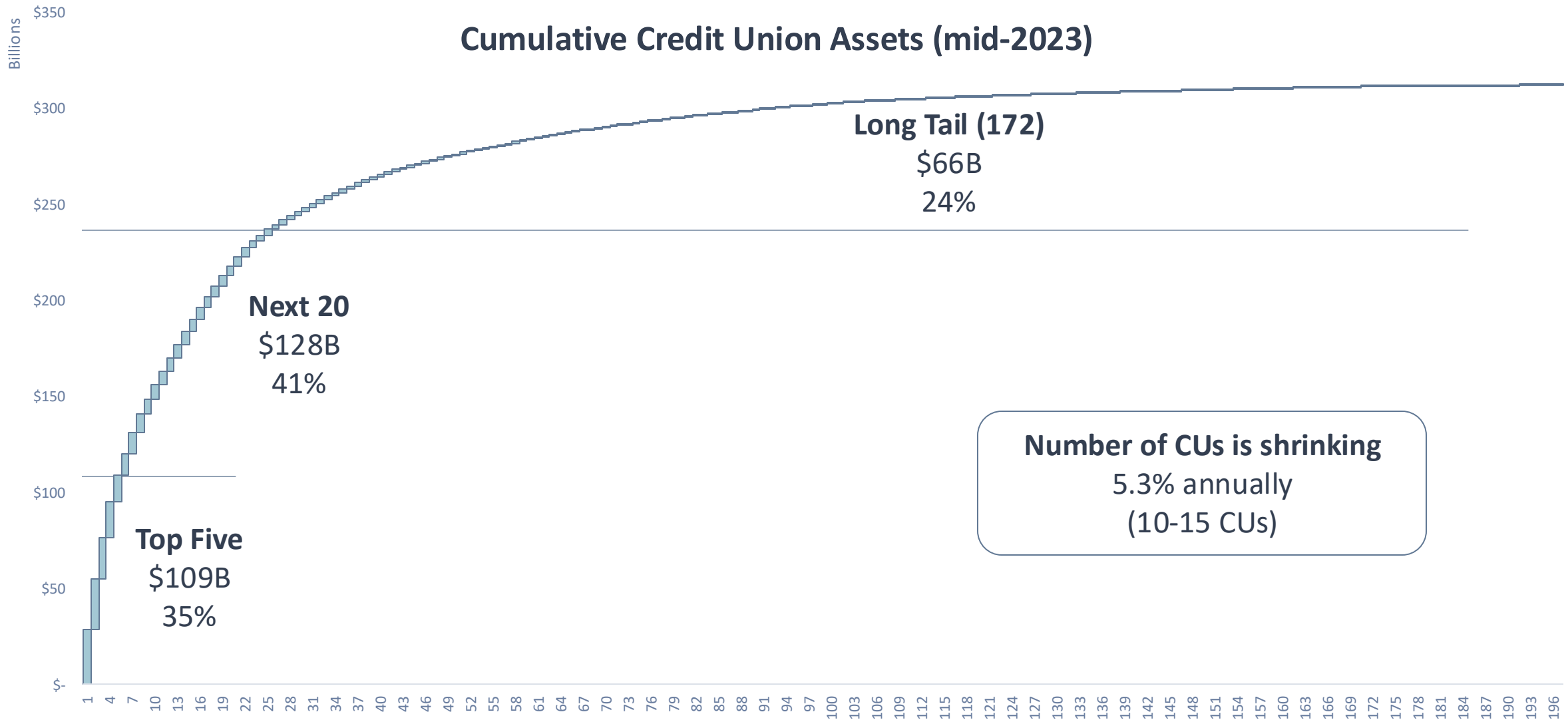
The credit union system exhibits significant regional variation



Source: CCUA, includes CCUA affiliated and unaffiliated credit unions. All data FY2023



Credit union bifurcation continues, with the top 25 credit unions holding three quarters of total assets



Mergers are starting to get larger

\$19B + 7B provincial juggernaut



\$6B + \$2B + \$2B Manitoba aggregator



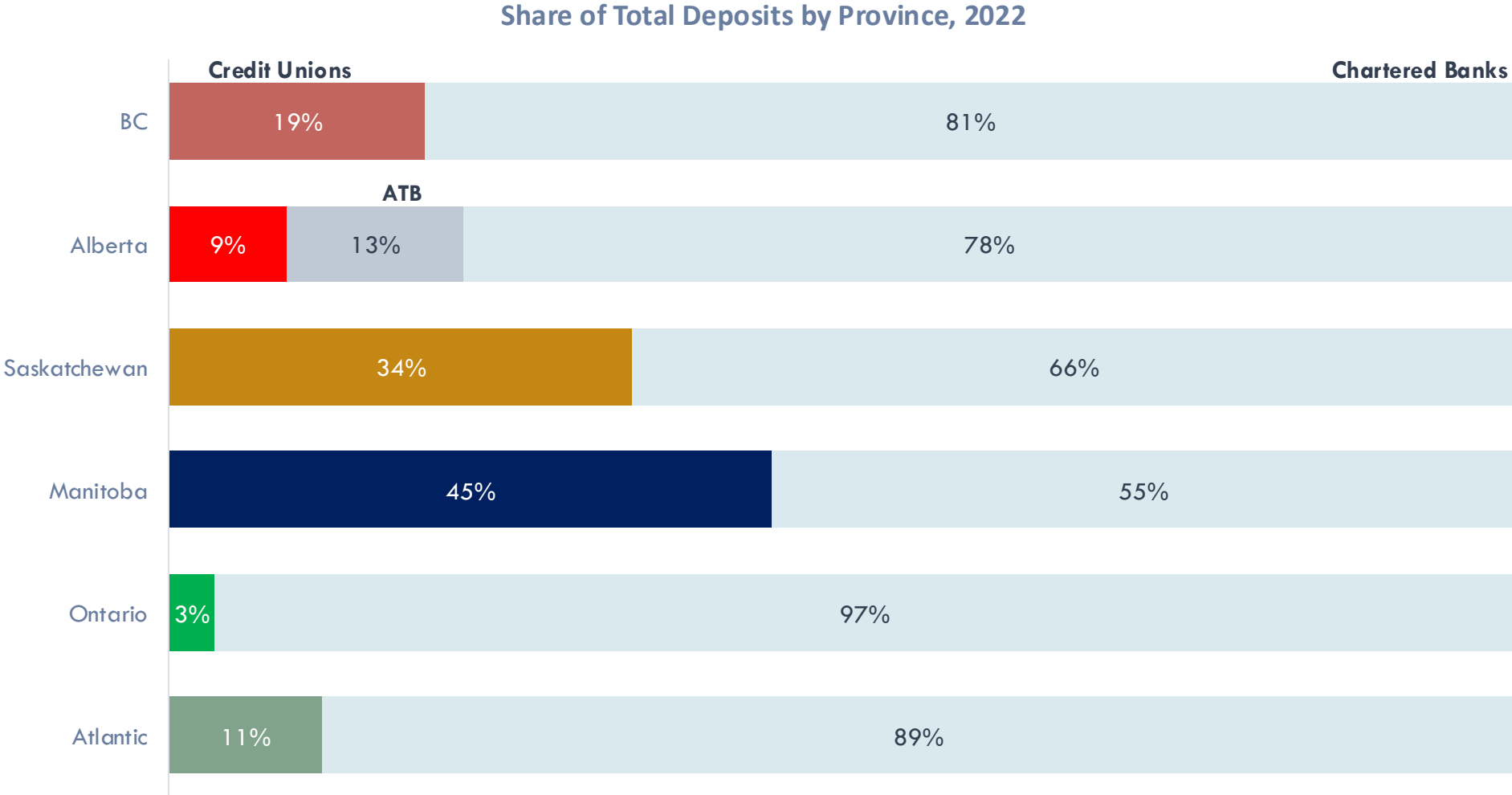
\$5B + \$3B + \$0.4B Vancouver + Interior



\$8B + \$6B Consolidator



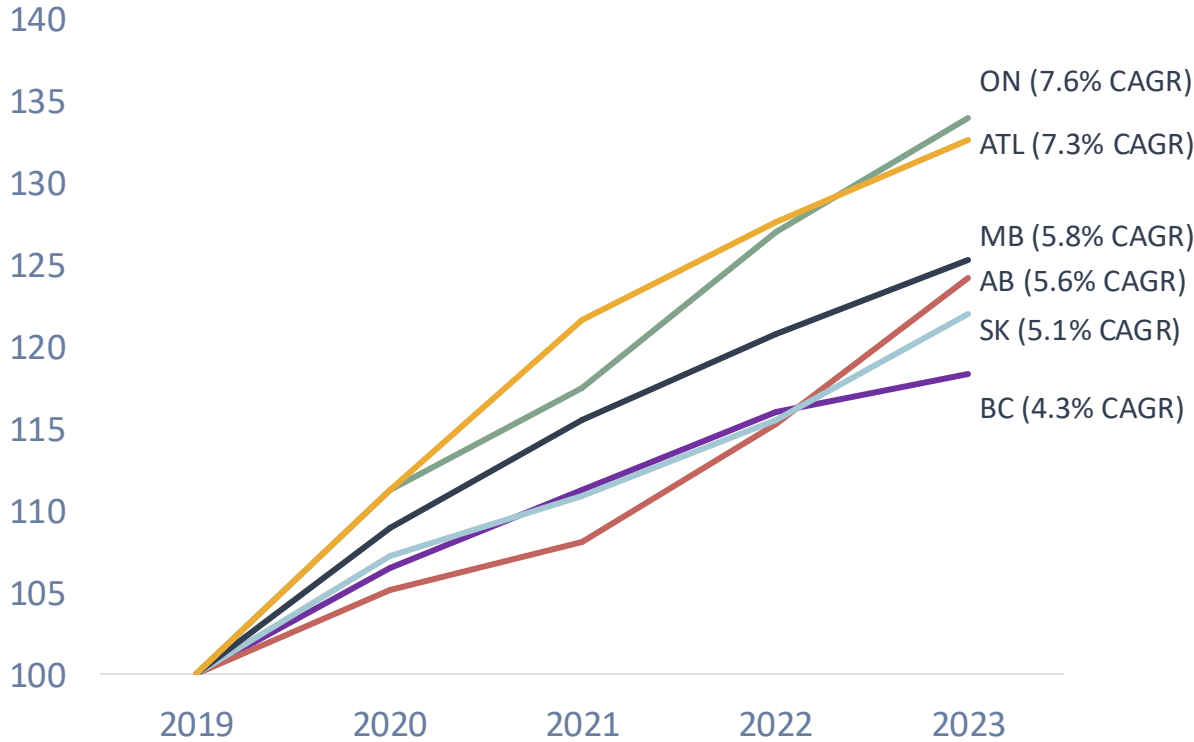
Credit union market share varies significantly by region



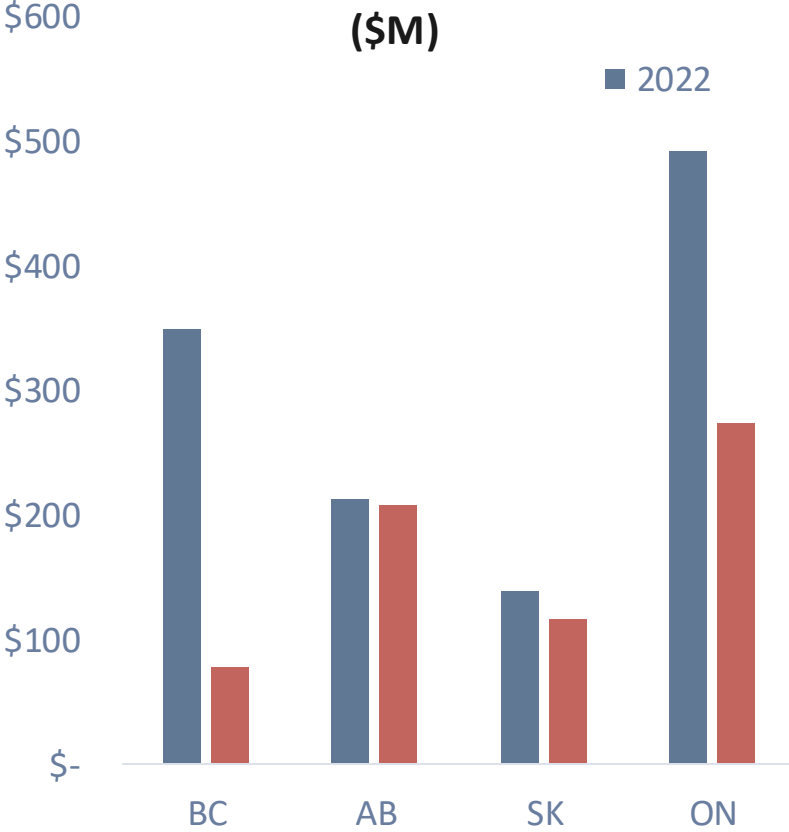
Source: OSFI, CCUA, DMSA Analysis. Bank deposits exclude FI deposits.

Ontario leads growth, but profitability has taken a significant hit

**CU System Assets by Region, 2019-2023
(2019=100)**



**System net income, 2022 vs 2023
(\$M)**

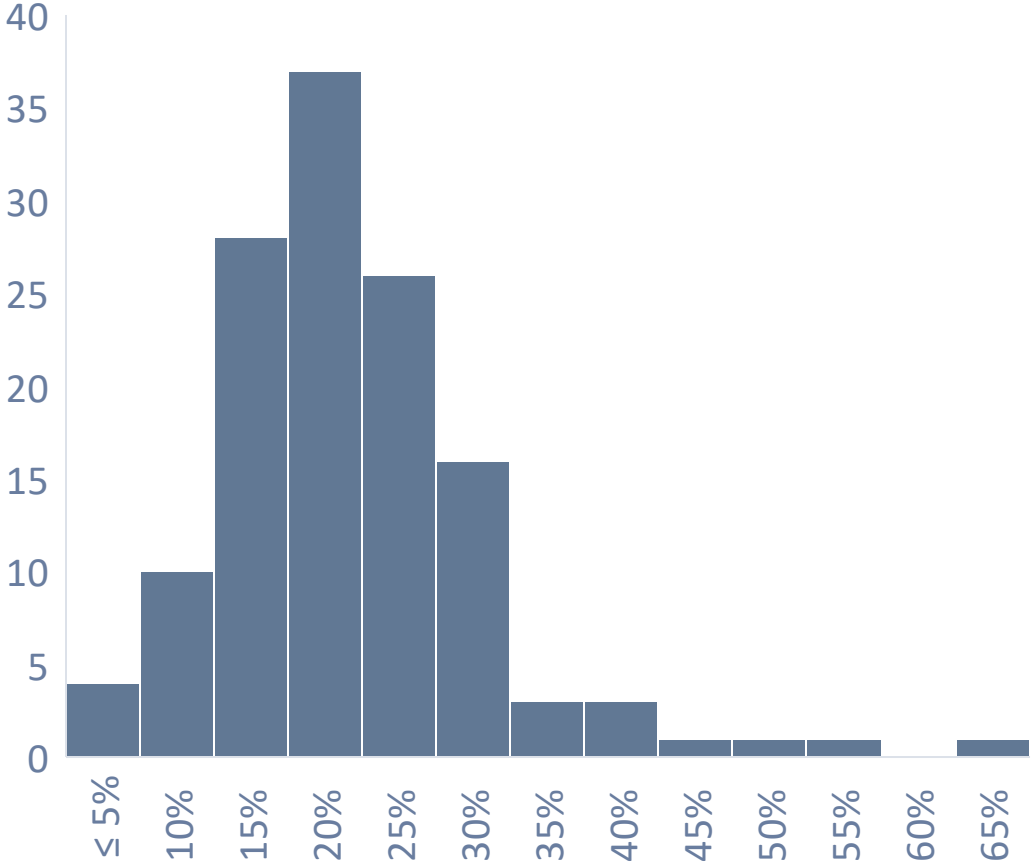


BC's slump may generate merger opportunities, while ON and Prairie fundamentals are stronger



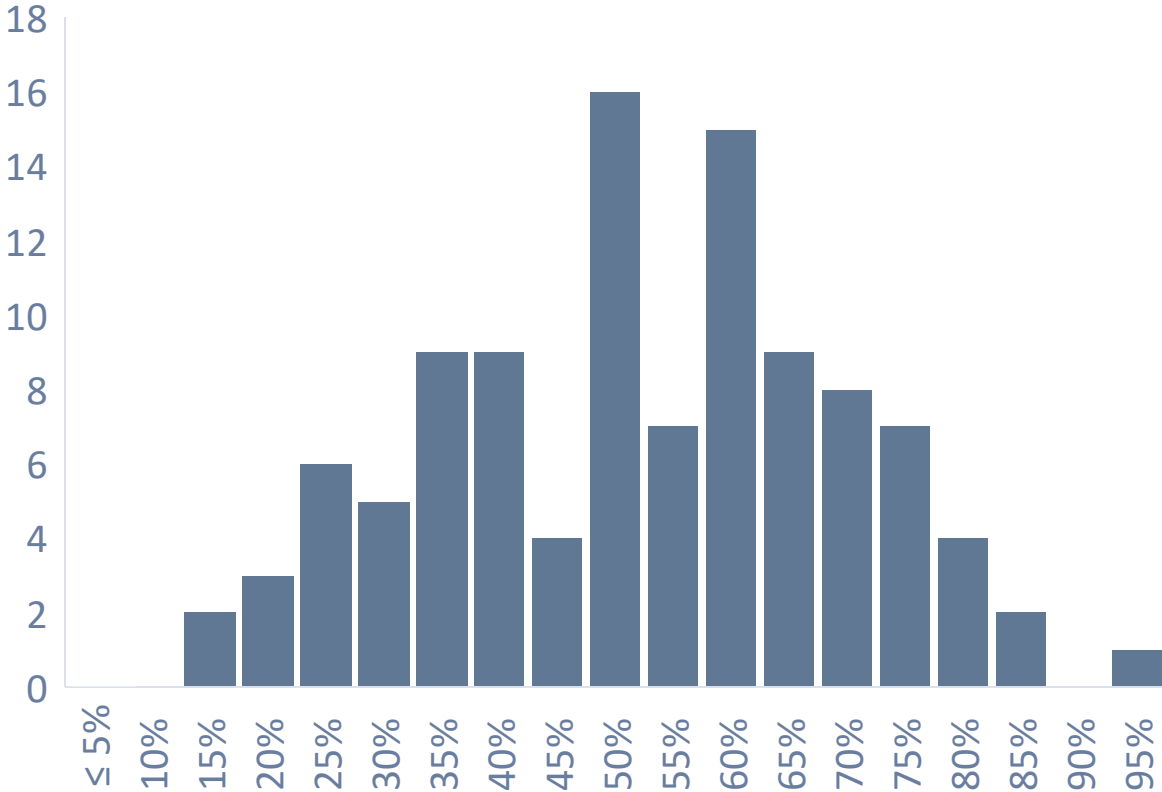
Many credit unions have a revenue diversification challenge

Share of Non-Interest Revenue, 2023 (N=132)



Typical Big 6 Bank Cdn P&C is ~30% Non-Interest

Retail Mortgage as a Share of Total Inv. Assets, 2023 (N=102)

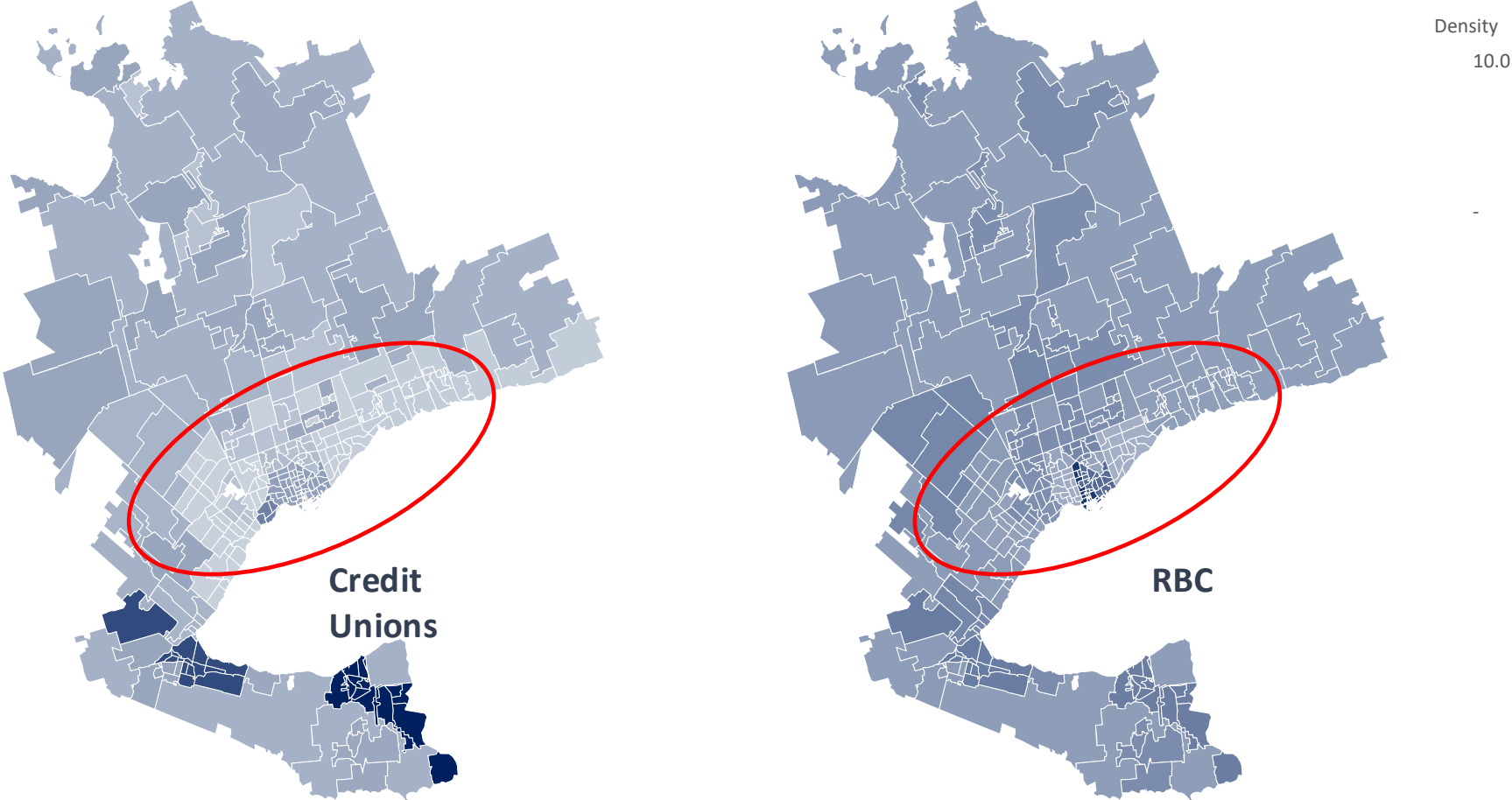


Typical Big 6 Bank Cdn P&C is 50-60% Retail Mortgage Share



Credit unions are under-represented in areas of high population growth

Credit Union vs RBC locations per 100k residents, L&M postal codes



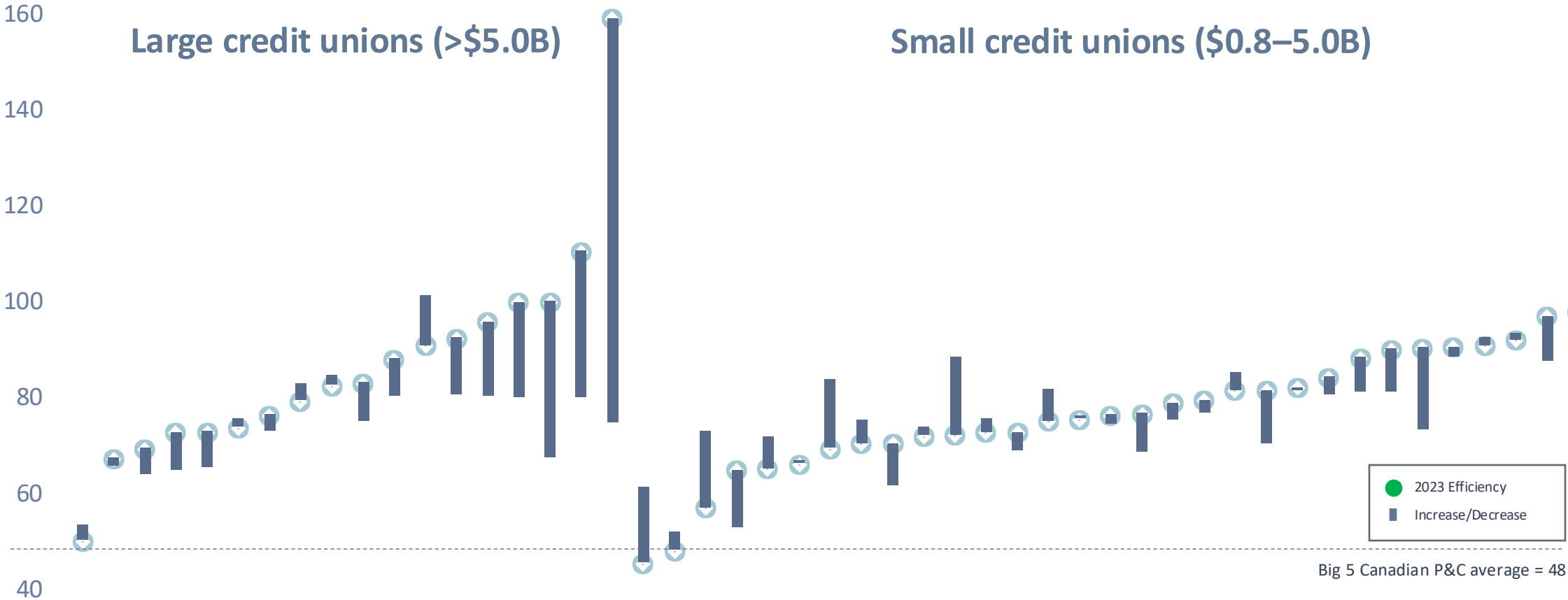
Source: Statistics Canada, Payments Canada FIF. Location and population data grouped by first two digits of postal code



A majority of credit unions have experienced declining efficiency

Credit Union Efficiency Ratios 2019 vs 2023

(sorted by 2023 efficiency, lower is better)



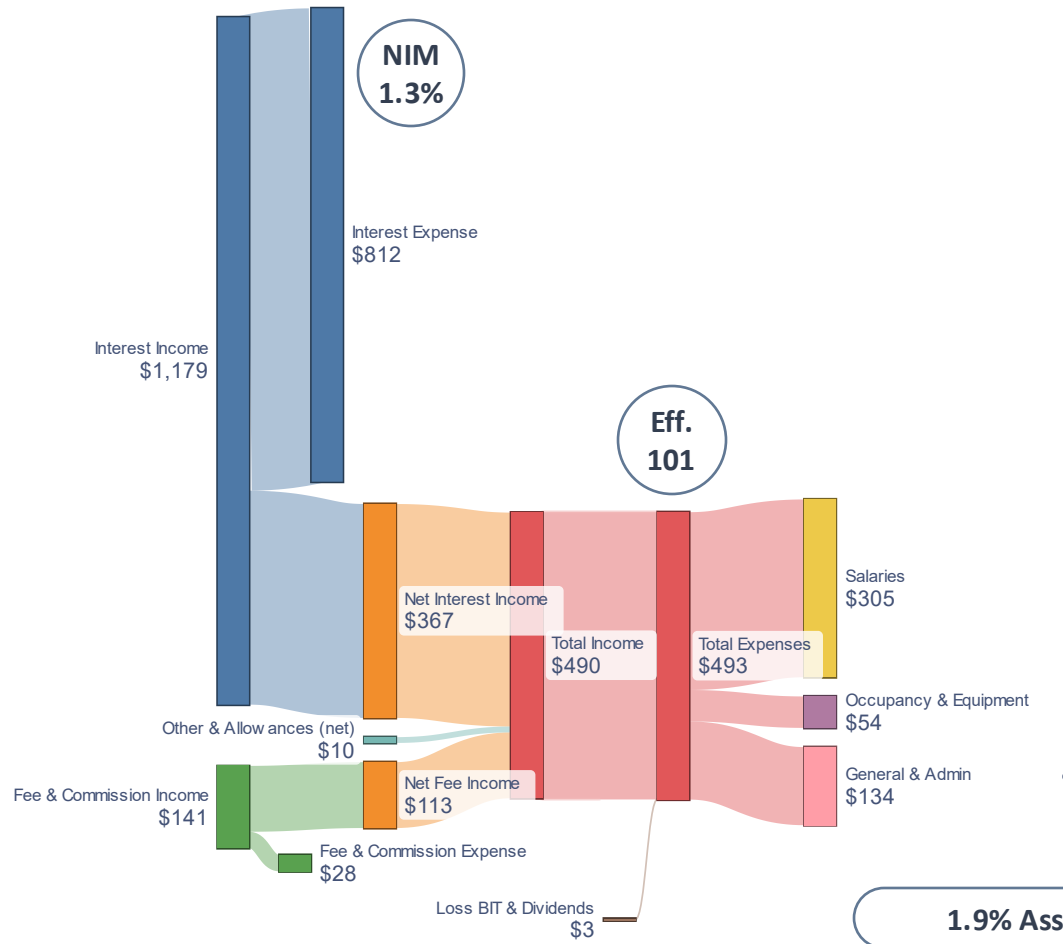
Big 5 Canadian P&C average = 48

Source: Annual Reports, DMSA Analysis. All data FY2023 unless otherwise noted. Provision for loan losses not included.

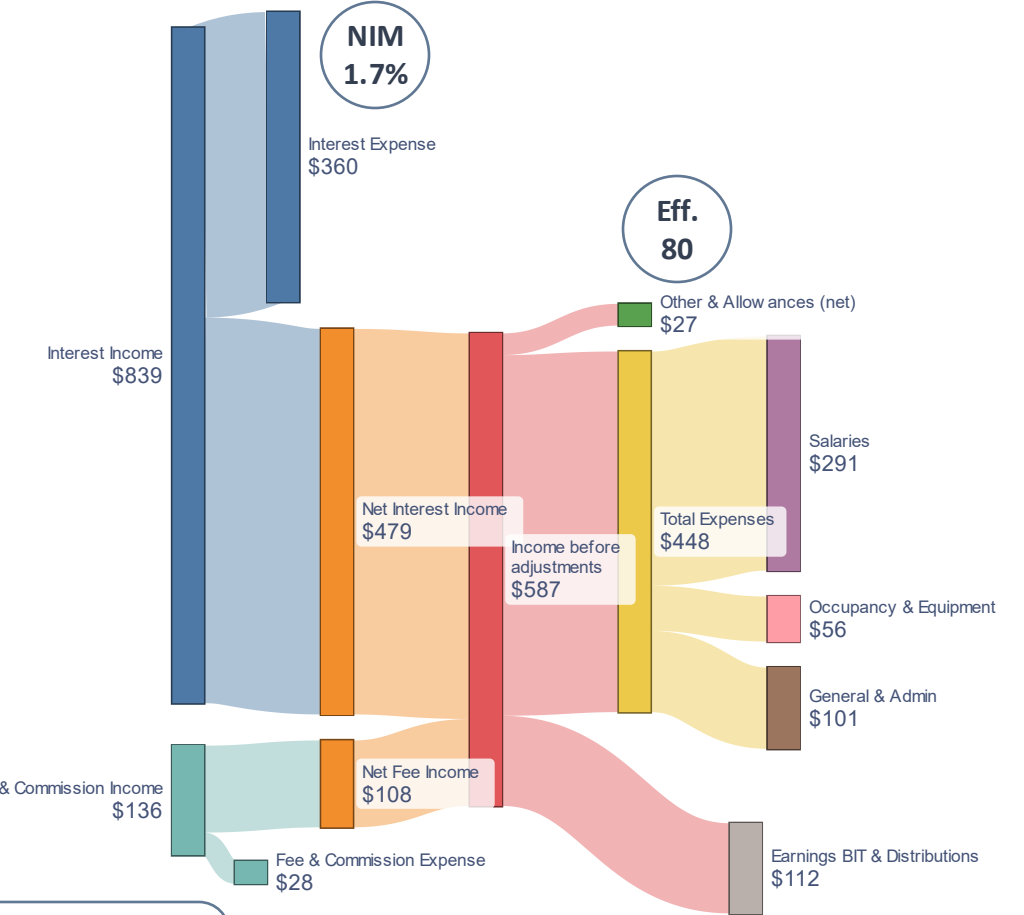


High interest rates and inflation created a challenging 2023 for many credit unions

Vancity Income Statement (2023)



Vancity Income Statement (2022)



1.9% Asset Growth



Reduced performance is impacting credit ratings



- Trends on First West Credit Union's Credit Ratings changes to Negative from Stable, Confirms Long-Term Issuer Rating at BBB (high) and Short-Term Issuer Rating at R-1 (low)
- Reflects weakened profitability amid the challenging economic environment, which could affect the Credit Union's ability to absorb potential credit losses and generate internal capital
- The Credit Union will likely incur net operating losses in 2024
- Despite a potential earnings rebound in 2025, elevated funding costs could challenge earnings recovery in the near to medium term and 2025 could likely continue to exhibit margin pressure
- The Credit Union has a higher contribution from noninterest income relative to its credit union peers, as well as stable operating expenses. The Credit Union maintains sound asset quality and balance sheet fundamentals, including stable funding sources, and solid liquidity and capital positions.

The second tier of shared services providers is in a period of transition

Liquidity Centrals



Products

Aviso Wealth

Collabria
(Credit Cards)

CUMIS
Insurance

Co-operators
Group

Treasury

Central 1
(Treasury & Trust)

League Savings
& Mortgage

Concentra
(EQ Bank)
(Bank and Trust)

Stabilization
Central (BC)

Technology

CGI
(ex Celero)

League Data

Central 1
(Digital Banking)

Payments

Central 1
(Payments)

Prairie Payments
Joint Venture

Everlink

Group Clearing
Joint Venture

The Exchange
Network

ACCULINK
Network

Trade Groups

Canadian Credit
Union Association
(CCUA)

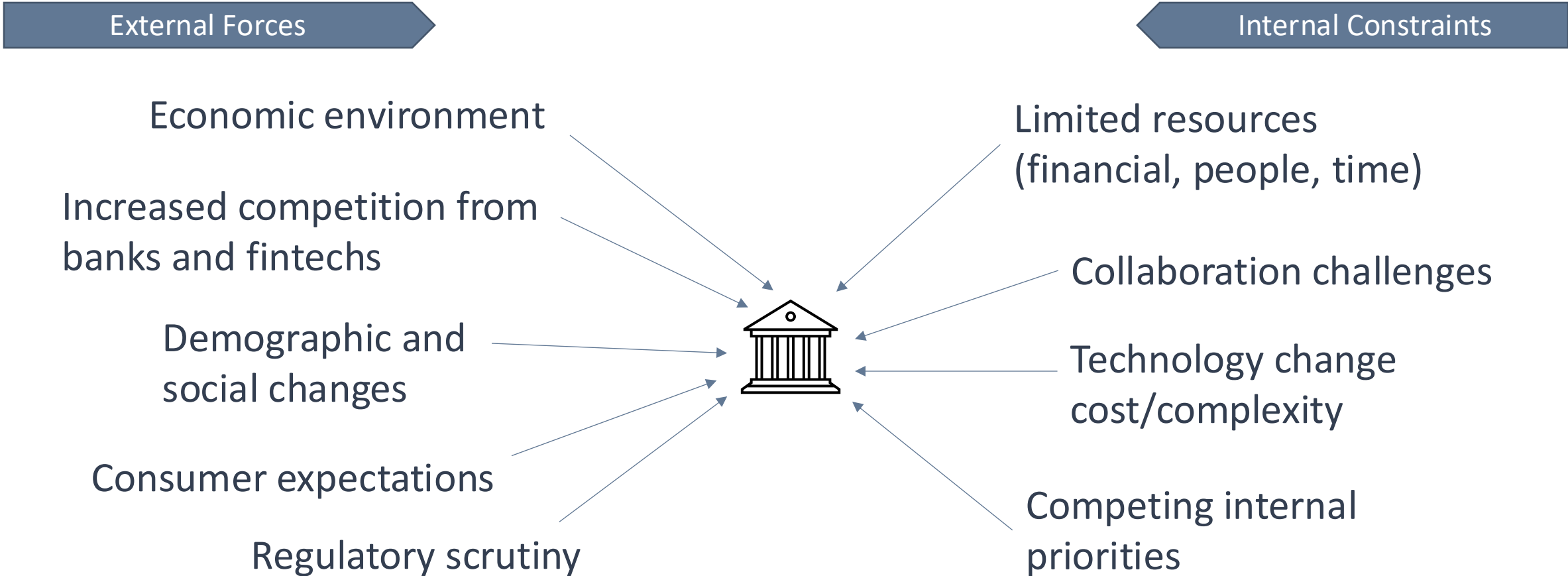
Large Credit Union
Coalition (LCUC)

Blue Group
& Others

Illustrative | Non-Exhaustive



Successful credit unions will build resilient organizations in the face of change



How can technology providers help?



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Credit unions have an opportunity to tackle IT challenges together



Digital Banking Transformation

- Future of Member Direct / Forge digital banking platform
- ebankIT deployed with large credit unions and CGI (Celero)
- VeriPark, Intellect Design and other new entrants



Payments Modernization

- PPJV lost \$38M in 2023, with no clear path to stability
- Central 1 is meeting targets, but transformation is complex
- Direct-to-Interac and custom payments solutions are gaining popularity



Core Banking and Hosting

- League Data has gone live with first Mambu clients
- CGI (Celero) has completed cloud conversion
- Some small CUs are going direct to vendor



Open Banking

- Caspian One has secured LCUC endorsement, Central 1 and a number of clients
- Flinx has partnered with Everlink and FirstOntario
- Most CUs lack a defined Open Banking strategy



AI and Data

- Member-facing and back-office transformation
- Lots of uncertainty for capabilities, cybersecurity, business case
- Foundational capabilities missing for many (e.g., cloud hosting)

Credit unions are up against deep-pocketed rivals



\$1.1B, 10.8% of revenue



\$1.1B, 9.0% of revenue ↑22% YoY



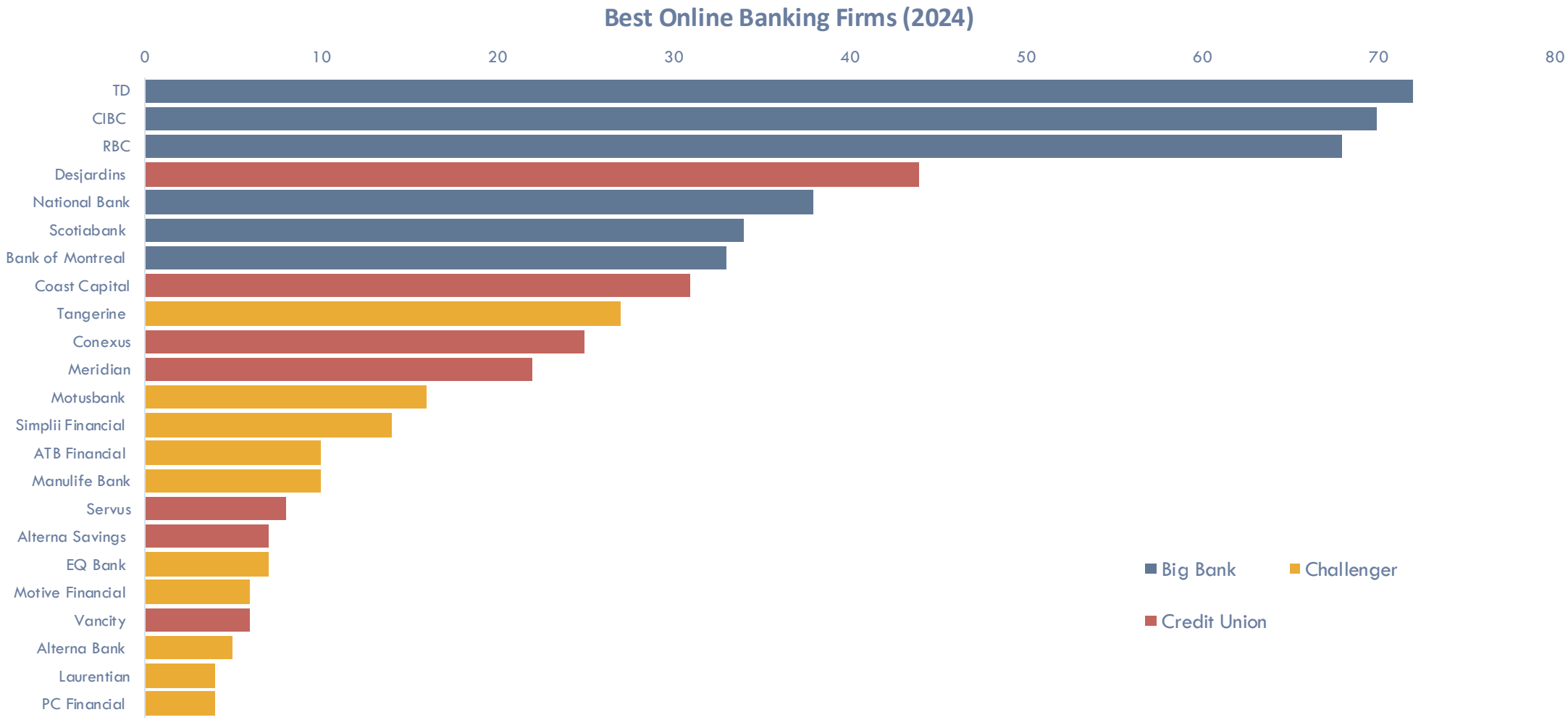
\$2.3B, 4.6% of revenue



\$1.0B *per month*, 15.6% of revenue ↑9% YoY
50% build 50% operate

Equivalent credit union spend of \$300-700M

Example: The gap between big bank and credit union digital capabilities remains large



Source: Survivor, *Best online banks and credit unions in Canada for 2024*



What must credit unions do?



Grow and diversify revenue streams

- Offer pipeline of competitive products
- Increase share of non-interest income
- Diversify loans beyond residential mortgages
- Attract low-cost deposits



Build membership

- Execute a differentiated market position
- Attract members, including new Canadians
- Build business member base
- Retain existing members throughout lifecycle



Sell and service

- Become experts at “distribution as a service”
- Increase share of wallet



Reduce operating costs

- Drive down efficiency ratio via cost reduction
- Seek out and support collaboration opportunities
- Outsource non-core, scale and high-expertise activities
- Consider mergers for scale



Manage risk

- Diversify revenue stream
- Generate retained earnings to support growth
- Manage cyber and other risks
- Stay in front of regulation

How can technology support?

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Group discussion





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