# Strategic Plan Digest
# 2016

**November 2015**

# Executive Summary

## Plan Development

Alloya has a ten-year vision, a three-year strategic plan and a one-year business plan (budget). 2016 will be the third year of the current three-year strategic plan which reflects a continuing evolution of Alloya's longer-term strategy. Alloya's Vision, Mission, Values and Goals are unchanged (see below). The strategy of Alloya is not fundamentally altered for 2016; however, there are changes in emphasis and tactics based on current events.

## Alloya Advantage

The strengths of the Alloya business model include:

- *Cooperatively owned by the credit union system.*
- *100% dedication to helping members.*
- *A simple business model that delivers great value by aggregating resources and making them available to members.*
- *Efficient and effective distribution, both high tech through Premier View and high touch through fifteen field service and sales staff.*
- *Employees who view themselves as a "department" of the credit union and are committed to their success.*
- *A commitment to education including Connections Calls, Operations Forums, Weekly Relative Value Economic Reports, Economic Forums, CFO Roundtables and League Events.*

Alloya operates from a solid financial foundation and its future is promising. This strategic plan builds on the success of the past two years while investing for the future.

As Alloya pursues its Vision to be a valued partner for its owners in their mission to serve their members, Alloya has established three Goals. As Alloya achieves these Goals, it advances towards its Vision and Mission:

- People/Culture – Alloya's staff are the key driver of the quality products and services it delivers. Alloya will focus on hiring, training and retaining excellent staff. Employees are engaged and proud to work at Alloya. The key theme for this Goal is to connect better internally and to have one, shared culture.
- Member Service – Alloya has distinctive competence in this area and sees this as a key differentiator. Members are engaged and proud to be members. The key theme for this Goal is to serve and connect better with our members by simplifying our operations through cooperative pricing and shared processes.
- Financial/Compliance Performance – Alloya needs to continue to be a safe, sound, well-capitalized, profitable and risk-averse institution. Member value creation will be balanced with the accumulation of retained earnings. The key theme for this Goal is efficiency.

## Environment

The environment in 2016 is likely to be similar to 2015, with moderate GDP and employment growth and continuing stabilization of the housing sector. Interest rates will increase about 25 basis points across the curve, after an increase of 25 bps at the end of 2015. The credit union environment will continue to reflect fewer credit unions, primarily via mergers of smaller institutions, with larger credit unions having stronger earnings and growth rates. Loan growth will continue, but at a slightly slower pace than 2015. Corporates will continue to consolidate as capital constraints of the new regulations continue to challenge many Corporate business models.

## Business Model

Alloya's business model focuses on U.S. credit unions. The following provides a summary of its current business model:

***Market Segments and Targets*** – Alloya segments its markets into four groups including three credit union groups (<$100 million in assets, <$1 billion in assets and >1$ billion in assets) and other credit union entities (CUSOs, league, etc.). For each of the asset segments, Alloya targets credit unions by core[1] and national markets[2], producing six separate target markets. Sales and service approaches vary by segment.

***Value Proposition*** – Alloya believes it has created a powerful value proposition for its members, estimated to be as much as a 35% return on invested capital per year. By the end of 2015, members will have already received a return value of almost *one and half times* their original capital investment just over four years ago. Alloya delivers value to its members through four specific activities by:

- Aggregating volumes to provide efficient lines of credit, settlement and payment processing
- Aggregating back office services by creating systems (Premier View), processes (i.e., cash ordering), and hiring expertise that no individual member can cost justify
- Providing high-touch and high-tech access in-person, on the phone, and electronically
- Providing value-added expertise and free education

***Channels*** – Alloya distributes its products and services via four channels:

- Premier View and other technology
- Phone
- In-person, via a staff of about 15 that work in Alloya's core and national markets
- Partners, including key vendors (see below)

***Member Relationships*** – The way Alloya interacts with its members is critical to its business plan as noted below:

- Trusted, knowledgeable, personalized service
- Efficient, secure, self-service access
- Cooperative ownership

***Revenue Streams*** – Alloya generates its revenues from three major sources:

- Net Interest Income (50%)
- Finance-related fees primarily from Balance Sheet Solutions (25%)
- Payment processing fees (25%)

***Key Resources*** – The following are Alloya's key resources:

- People
- Premier View and other technology
- Partners

[1] Core Markets = WY, CO, UT, NE, SD, MN, IL, IN, MI, NY, NJ, CT, MA, RI, PR

[2] National Markets = All non-core U.S. states and territories

***Key Activities*** – In providing its value proposition, the following are Alloya key activities:

- Investing and lending
- Efficient payment processing
- Hiring, training and retaining talented people
- Effective member sales, service and training interactions
- Providing secure, efficient, self-service transaction access

***Key Partners*** – Alloya partners with the following organizations to provide a full array of products and services:

- Financial institutions
- Regulators
- Payment system and cash providers
- Human resource service providers
- Trade associations
- Technology providers
- CUSOs

***Cost Structure*** – Alloya's cost structure:

- Is value-driven as it is willing to spend on service quality and people
- Maximizes economies of scale and scope
- Minimizes fixed costs

## 2016 Plan

Alloya's 2016 Strategic Plan has the following key tenets:

***Mission*** – To deliver products and services that add value to owners.

***Vision*** – To be a valued partner for its owners in their mission to serve their members.

***Guiding Principles*** – Alloya affirms that it:

- Exists to add value to owners in their mission to serve their members
- Is committed to transparent, participative governance
- Is open and transparent in communications with owners at all times
- Is ethical, reflecting professional behavior, as defined in Alloya's policies and procedures
- Ensures that the safety and soundness of owners' transactions and their investment in Alloya are always held paramount
- Goes above and beyond owners' expectations in product and service quality

***Risk Management Philosophy*** – Alloya is committed to:

- Focusing on the return of principal versus the return on principal
- Utilizing off-balance sheet products to protect the capital owners entrust to Alloya
- Having the proper infrastructure and resources to measure and report risk levels to owners
- Sharing Alloya's risk profile and mitigation strategies with owners
- Providing a mechanism for owner input into the risk profile

***Values*** – Alloya's values determine how its employees will behave toward our members, partners and each other. Alloya's values drive which employees it hires and promotes. Alloya's values are:

- Respect – Act in ways that show you care

- Integrity – Have a commitment to safety and soundness
- Service – Do more than simply what is expected
- Engagement – Believe in what you are doing and have passion for what you do

***Goals*** – Alloya will pursue the following Goals in pursuit of its Mission and Vision:

- People/Culture – Alloya's staff are the key driver of the quality products and services it delivers. Alloya will focus on hiring, training and retaining excellent staff. Employees are engaged and proud to work at Alloya. The key theme for this Goal is to connect better internally.
- Member Service – Alloya has distinctive competence in this area and sees this as a key differentiator. Members are engaged and proud to be members. The key theme for this Goal is to serve and connect better with our members by simplifying our operations.
- Financial/Compliance Performance – Alloya needs to continue to be a safe, sound, well-capitalized, profitable and risk-averse institution. Member value creation will be balanced with the accumulation of retained earnings. The key theme for this Goal is efficiency.

To achieve the strategic plan Goals, Alloya will undertake several Objectives including Business Plan Initiatives (BPIs) and Key Success Measures (KSMs) as shown in the following chart.

Table 1 – Goals and Objectives

| Initiatives (BPIs) | Measures (KSMs) |
|---|---|
| People/Culture – Employees are engaged and proud to work at Alloya. | |
| 1. Invest in Staff<br>a) Invest in Shared Culture (Facilities)<br>b) Connect Better (Unified Communications)<br>c) Staff Professional Development | 1. Staff engagement survey = **66%** |
| Member Service – Members are engaged and proud to be members. | |
| 1. Shared Capabilities<br>a) Check Processing<br>b) ACH Processing<br>c) Contracts<br>2. Cooperative Pricing<br>3. Product Innovation<br>a) Liquidity Options<br>4. Connect with Members<br>a) Co-sponsor Regional Events | 1. Member engagement survey = **4.50**<br>2. Selected new contracts = **100** |
| Financial/Compliance – Member value creation will be balanced with the creation of retained earnings. | |
| 1. BSS as Industry Leader<br>2. Implement Shared ALM Modeling<br>a) Consolidate BSS Modeling to ZMFS<br>b) Convert Alloya Modeling to ZMFS<br>3. Advance Technology Consolidation Plan | 1. Net income = **$7.3 million** |

## 2016 Budget

As part of the strategic plan development, Alloya creates an annual budget and a longer-term financial projection based on the BPIs and KSMs in the Plan. For 2016, Alloya is targeting a balance sheet of about $3.2 billion, with about the same amount off-balance in EBA accounts. Alloya plans to earn about $7.3 million in net income for 2016. This is based on an increase from 2015 in Net Interest Income (NII) of $200,000 (rates), a moderate increase in fees of $400,000 (Balance Sheet Solutions sales increases) and a significant decline in operating expenses of $1.2 million (one-time merger expenses end). Retained earnings increase to 2.3%, while the leverage ratio drops to 6.6% due to the regulatory lock-out of a portion of Perpetually Contributed Capital (PCC), though both the Retained Earnings and Leverage ratios are at the well-capitalized levels.

On a longer-term basis, Net Income will increase to about $12.6 million per year by 2020 as assumed rate increases (about 175 bps over five years) improve NII. Fee income increases from about $20.1 million in 2015 to $25.0 million by 2020. The key drivers are increased Balance Sheet Solutions sales and the new cooperative correspondent pricing, which includes inflation increases of about 4% from 2018-2020. While operating expenses decrease in 2016 as one-time merger-related expenses complete in 2015, expense rises to $38.4 million in 2020 as a little more than 2% inflation is assumed.

Alloya's Retained Earnings ratio increases steadily to about 3.6% by 2020 due to annual contribution of net income, net of PCC dividends. Starting in 2017, PCC dividends are targeted on an "ability to pay basis" of 20% of net income. The leverage ratio is projected to increase through 2019 to 8.5%, but will decline in 2020 to 7.2%, which is a result of the final lock-out of PCC reflected in regulation. This ratio is still well above the well capitalized level in regulation of 5%. Please see the following summary for details:

Table 2 – Summary Pro Forma

| | Projected - Expected | | | | | | |
|---|---|---|---|---|---|---|---|
| | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
| Average Assets (MDANA) | $3,181 | $3,087 | $3,245 | $3,140 | $3,012 | $3,008 | $3,007 |
| Leverage Ratio | 8.9% | 9.3% | 6.6% | 7.2% | 7.9% | 8.5% | 7.2% |
| Retained Earnings/Total Assets | 2.0% | 2.2% | 2.3% | 2.6% | 2.9% | 3.2% | 3.6% |
| | | | | | | | |
| Net Interest Income | $20.4 | $21.3 | $21.5 | $21.8 | $21.9 | $24.3 | $26.0 |
| Fee Income | 22.5 | 20.1 | 20.5 | 22.3 | 23.2 | 24.1 | 25.0 |
| Operating Expenses | (34.7) | (35.9) | (34.7) | (35.5) | (36.4) | (37.4) | (38.4) |
| Net Operating Expenses | (12.2) | (15.8) | (14.2) | (13.2) | (13.2) | (13.3) | (13.4) |
| Net Income | 8.2 | 5.5 | 7.3 | 8.6 | 8.7 | 11.0 | 12.6 |
| PCC Dividends | 1.2 | 1.5 | 1.5 | 1.7 | 1.7 | 2.2 | 2.5 |
| Change to Retained Earnings | $7.0 | $4.0 | $5.8 | $6.9 | $7.0 | $8.8 | $10.1 |