STELLARSTRATEGIC

STELLAR INSIGHTS

SPRING 2018

Direct Versus Indirect Lending

Page 2

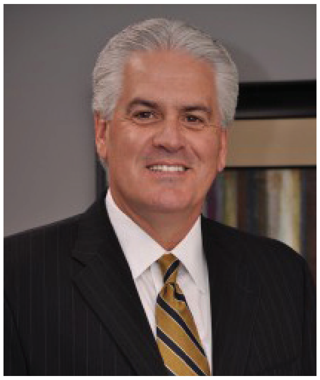
Three Ways to Create Superstars with Your Frontline Staff

Page 4

Fintech Made Easy

Page 6

Welcome to our Spring 2018 Edition of *Stellar Insights*



Let me start by wishing everyone a Happy & Prosperous 2018. This edition of *Stellar Insights* focuses on the trends and opportunities we have seen while servicing our client base.

We touch on a varied list of issues that have become very topical in recent months. Fintech, for example, is a topic you hear referenced on a regular basis…but how much do most people know about it? We have a great Q&A with Alex Jimenez at Zions Bancorporation addressing some key questions directed toward the community banking industry in the article entitled "Fintech Made Easy".

In most of our previous editions we talk extensively about attrition and this edition continues that trend. We like to refer to attrition as a silent killer to growth. For instance, our "Stellar Strategic Spotlight" section discusses how many institutions overlook the key role mortgages can play in reducing household attrition. We also lay out the pros and cons of indirect versus direct auto lending. Again, this is another opportunity to positively affect attrition by adding additional products and services as well as enhance growth via auto refinance.

We sincerely hope this continued sharing of information and best practices is beneficial to you and encourage you to participate by sharing some of your experiences. We also welcome ideas or topic suggestions to feature in future newsletters.

Our sincere thanks to Alex Jimenez for taking the time to contribute to this edition of *Stellar Insights.*

Let's have a great 2018!!!!

Craig Simmers
Founder
410-990-0172
craig.simmers@stellarstrategic.com

Upcoming Events

April 18-20
Cornerstone Credit Union League '18 Annual Meeting & Expo
Marriott Little Rock
Little Rock, AR

April 25-27
VACUL Annual Meeting 2018
Hilton Norfolk The Main
Norfolk, VA

May 17-19
2018 MSCUA Annual Meeting & Convention
Beau Ridge Resort
Biloxi, MS

May 20-22
2018 PCUA Annual Meeting
Nemacolin Woodlands Resort
Farmington, PA

Direct Versus Indirect Lending: Balancing Your Credit Union's Auto Loan Portfolio

By George Monnier, Founding Partner Stellar Auto Loans

Auto lending has increasingly become a profit center for the credit union industry over the years. Most credit unions offer some type of auto loan financing whether directly to their members or through auto dealerships and other relationships. In this article, I will discuss the nuances of both direct and indirect lending strategies to help you determine if there may be other opportunities in your market to better balance your auto loan portfolio. Consider these facts:

- Currently, indirect auto lending surpasses direct-to-consumer lending on average among U.S. credit unions.[1]
- Banks still hold a significantly higher market share compared to credit unions in the indirect sector with almost double the market share.[2]
- On average, indirect lending represents almost 70% of the auto loan volume nationally.[3]

Both banks and credit unions can benefit from increased income and asset growth with indirect lending. In order to be successful, close monitoring (due to tight margins) and *constant* nurturing to build and maintain trusted third-party relationships is needed.

Profitability is continually being squeezed due to steady increases in dealership fees, which have grown considerably in most markets, and in turn reduce margins. In addition, quicker rates of pay-off, increased charge offs and delinquencies add to profitability concerns with indirect lending. Marginal applications (not up to the institutions underwriting standards) and dealership loan documentation discrepancies further create the need to have effective oversight.

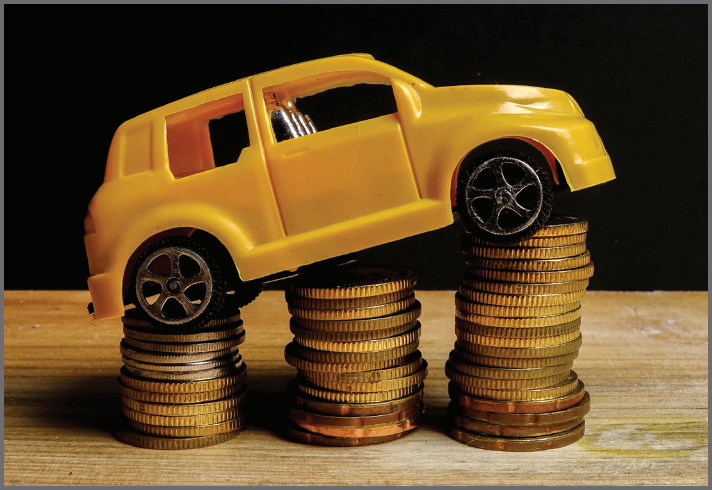
With a well-managed indirect program, financial institutions will generate incremental interest income. Unfortunately, little (if any) non-interest income is realized by credit unions as the dealership keeps the MBI, GAP, AD&D, documentation fees and other fees.

This all points to the need to balance an indirect program with other loan strategies.

Credit unions are making advances with student loans, credit cards, and first mortgages. But on the auto loan side, we suggest that they redouble their efforts to generate *direct* auto loans with both new and existing members. In other words, don't rely on indirect auto lending alone.

As a side note, one non-dealership corporation has started to leverage this opportunity nationwide. The corporation pays the marketing costs for potential members, completes the loan approval process, and presents the packaged loan to the institution for their acceptance. Part of that corporation's strategy is to keep the majority of the non-interest income from insurance add-ons for themselves, leaving the credit union with another "indirect" loan member. Institutions that benefit the most from this program are typically the ones that have the lowest rates in the market.

On the direct-to-consumer side, many auto loan marketing strategies use a "shotgun" approach featuring a low rate offer. This approach can generate good initial response rates. However, the majority of those responders do not meet the credit union's loan approval parameters. Internal resources are wasted due to high application volumes and low approval rates - which frustrate both the loan department as well as the individual households responding.



A concerted effort to reach new potential members (residing in your community charter or association footprint) can significantly increase loan growth and profitability per loan. Targeting households missed by your indirect program can be done effectively and economically with the right marketing strategies. A successful direct lending program will utilize credit bureau analytics to create a customized offer to profitable audience segments, with easy-to-understand messaging and multiple response options.

This type of direct approach allows loan officers a *direct line of communication* with qualified prospects that have been vetted through some form of credit approval process. After all, a key source of lost income from indirect loans is the inability to establish that direct relationship with the new member. According to CUNA News, "69% of credit union auto loans originate through the indirect channel, only 5% of those indirect members use additional credit union products." As it has been documented numerous times, single service relationships tend to end when the loan is paid off and are difficult to cultivate into overall real membership growth.

(Continued on Page 3)

(Continued from Page 2 - Direct vs Indirect Lending)

Below are average calculations from our current clients comparing income generated on a direct loan versus an indirect loan. Please note, the income number on direct loans is being underreported in this chart since many of these relationships continue after the average loan life of 24 months. Consumers are much more likely to continue using the credit union for future loans (and other banking services) with a direct-to-consumer loan approach.

	Direct	Indirect
Loan Amount:	$17,000	$17,000
Interest Income:	$1,185 (based on 4.5% blended rate, 24 months average life)	$889 (based on 4.5% blended rate, 18 months average life)
Non-Interest Income: (GAP, MBI, AD&D, etc.)	$288	$0 (Dealer keeps this income)
Checking Accounts: (Interest income, incentives to open, debit card interchange, overdraft fees, etc.)	$240	$12 (Little to no additional income)
Other products: (Credit Cards, Unsecured loans, HELOCs, etc.)	$247	$12 (Little to no additional income)
Total Income:	**$1,960**	**$913**

As you can see, total income more than doubles when the credit union can keep non-interest income and add additional accounts and services with the member directly. Having membership friendly "built-in" incentives for cross-sales helps generate faster on-boarding for additional services. Ultimately, the goal with direct lending is to gain a lifelong relationship with a new member, not just a loan. Building relationships one member at a time has proven very successful in the past, and should continue to be successful in future years.

In summary, finding the right balance between direct and indirect lending approaches will be critical to the bottom line. Whereas indirect auto lending may not always be part of the mix, we do recommend nurturing and growing your direct-to-consumer strategy because of the likelihood for longer term relationships and increased income.

George Monnier has spent over 16 years helping financial institutions generate new deposits and loans. He is a founding partner of Stellar Auto Loans, a division of Stellar Strategic Group, which offers pay-for-performance auto refinance programs to the banking industry. To learn more about Stellar Auto Loans[sm], please contact george.monnier@ stellarstrategic.com or 402-708-2425.

[1]*Creditunions.com: Breaking the Indirect Addiction: Marc Rapport: November 2017*
[2]*Autocount.com: Driving Future Auto Loans: Bill Meyer: December 2014*
[3]*CUNA.org: 2017 Lending Outlook, This Month in Credit Union Magazine: November 2016*

Stellar Strategic Spotlight: Mortgage Analytics

In previous editions of *Stellar Insights*, we chronicled the pitfalls and opportunities of customer attrition. One area that most institutions tend to ignore (that is both a contributor to attrition and a selling opportunity) is targeting current clients for mortgage refinancing. Very likely, your customers or members are frequently targeted by other financial institutions with refinancing offers. If and when they succeed, you are at high risk of losing the entire relationship.

We are excited to announce a proven solution to minimize exposure to your existing non-mortgage households. Mortgage Analytics identifies current accounts that are prime refinance targets for your institution. We analyze existing mortgages based on interest rate and credit-worthiness, then calculate the amount they could save by refinancing with your bank or credit union.

Mortgage holders with higher-than-market interest rates and good credit are being poached from community banking institutions daily. There's no reason to let this happen in your market any longer. A proactive approach not only retains existing relationships but also deepens that connection with your account holder. Monitoring your account base to find these existing mortgage opportunities

should be standard practice and a key component of any strategic marketing plan.

As part of the Mortgage Analytics launch, we are offering a FREE ANALYSIS of your current database to gauge the level of opportunity that may exist in your market. **BONUS: If you sign up for our program before July 1st, we will discount the set-up fee to $250… a savings of $749.**

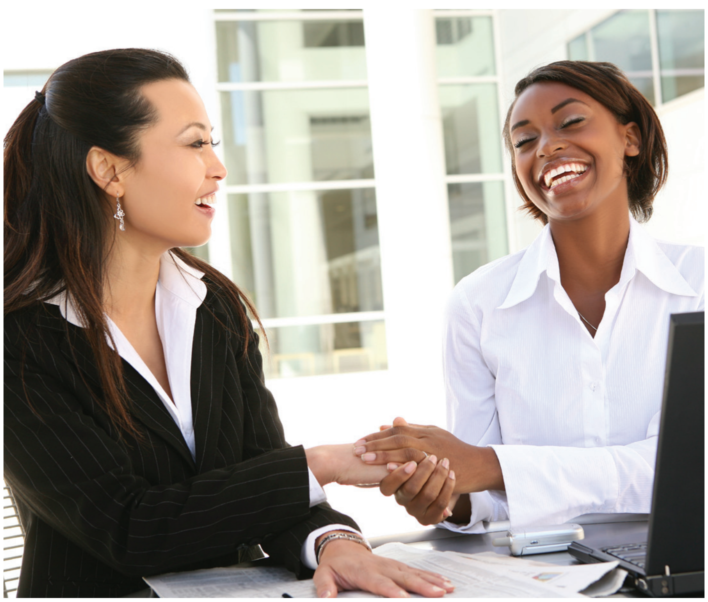
Three Ways to Create Superstars with Your Frontline Staff: Lessons Learned While Mystery Shopping

By Jennifer Brooks, Chief Marketing Officer

I consider myself lucky. Over the years, I have accrued wonderful memories and great experiences while mystery shopping at bank and credit union branch locations across the United States.

A few stand-out memories pop into my mind:

- During one of those notorious Seattle downpours, a teller insisted she walk me to my car holding an umbrella over my head to keep me dry.
- Down in southern Louisiana, a new account representative went out of her way to help me make dinner reservations at a delicious creole restaurant when she realized I was not familiar with the area.
- In Ohio, a new accounts representative called to follow-up with me a few days after I had visited his branch. That was the only time someone asked for my name, number and called me after my initial shop. It was a nice touch.



Had I been truly moving, I would have opened a checking account with any of these superstars at their branch. Experiences like these didn't happen every day, but they sure left a memorable impression on me. I also had a handful of not-so-great experiences too.

One extreme case happened while discussing checking options with an assistant branch manager. Everything was going great until I heard the familiar sound of a vibrating cell phone. Immediately his attention went to that phone, and after a few seconds of struggling to ignore the call, he impulsively reached for it and answered. I was a bit surprised (and disappointed) he would take a personal call while I was in his office. However, I was more startled with what he said to the unknown caller. To paraphrase it was along the line of "Leave me alone, I am working". But, there was one word he included in his response that really made me cringe...yup, he used the f-word.

He quickly hung up his phone and gave me a short apology for the interruption. An overwhelming sense of dread grew at that moment realizing I would have to recount this conversation to the CEO of the bank the very next day. The CEO did not take it very well – that assistant branch manager was immediately fired.

Thankfully, that was the only time I witnessed inappropriate behavior to that level. More often poorly-rated experiences centered on less offensive behavior (being aloof, a bit condescending, slightly unfriendly, extremely shy) or just having a poor grasp of product and service offerings. However, a majority of frontline staff were welcoming, warm, and generally knowledgeable about the financial institution's products and services.

During most shops my focus revolved around needing a new checking account, primarily interacting with tellers and new account representatives. If I were to average branch scores from all shopping experiences, I would say frontline staff earned about a 79%. Not bad. There were, however, a handful of superstars that earned a score of 90% or above. Those high scores all had something in common – they successfully incorporated the following three skills:

1. Asking Relevant Questions

Knowing facts and being able to communicate the most relevant facts are two different skills. Memorizing features and benefits of each checking account offered is certainly the first step, but simply regurgitating every line item about each account will leave the consumer feeling overwhelmed and totally confused.

Superstars ask relevant questions to understand a consumer's needs and adapt how they approach a conversation about account options. Questions like, "Why are you looking for a new account?" or "What do you like/dislike about your current account?" are great ways to encourage an open dialogue with the consumer. Further questions about specific checking behaviors such as, "What kind of balance do you keep in your checking account?" or "Do you prefer paper statements or electronic?" will help frontline staff determine the best account for the consumer.

Besides finding the best checking account, asking the right questions should also lead to the discovery of other financial products and services that are relevant to that consumer.

(Continued on Page 5)

(Continued from Page 4 - Three Ways to Create Superstars with Your Frontline Staff)

2. Positive Positioning

Sometimes a consumer will ask a question in which "no" is the simple answer, but not the answer we know the consumer wants to hear. Superstars know how to answer a NO question with a positive spin. Take the following example assuming a traditional free checking account is not offered:

Consumer: *"Hi, I was wondering if you offer a Free Checking account?"*
Teller: *"No, sorry, we do not…"*
Consumer: *"Ok, thank you…"*

The teller did nothing wrong per se, but learning how to spin a negative NO answer into a selling opportunity is something that can be learned. Let's try the same question again:

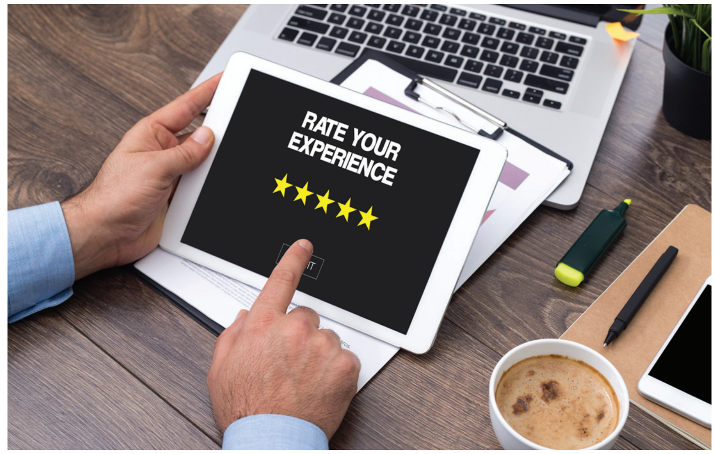
Consumer: *"Hi, I was wondering if you offer a Free Checking account?"*
Teller: *"Actually, we have two checking options that make it easy to avoid monthly fees, and you can qualify to earn interest as well…may I ask you a couple of questions to see which account would work best for you?"*
Consumer: *"Sure, go ahead…"*

Not only does the second option avoid using NO as the answer, it also keeps the consumer engaged in dialogue. Of course "no" can be used in a positive way – as in, "There are NO monthly fees on this account." Spend time crafting best-practice answers on common questions or objections your frontline staff frequently encounter. Be honest but position your accounts in the most positive light.

3. Going Above and Beyond

There are many ways to go above and beyond what is expected when a consumer visits your branch for the first time. Obviously, the teller that walked me to my car with an umbrella is a great example of this, but that approach is not always practical nor realistic in most situations. Some branches would be too busy at times, others wouldn't be safely staffed to allow that to happen. Going above and beyond is getting into the habit of looking for extra opportunities to stand out from your competition. In other words, a little extra effort can go a long way. Here are a couple of ideas that DO make a difference:

- Show, don't just tell! If a brochure is not available, print out the information that the consumer is requesting. Staple a business card with name, direct line and email address for easy follow-up. If there are visual tools that will help the consumer understand your products or services better, make sure those are available to the frontline. A comparison chart



that has all the information about each account makes it much easier for the consumer to follow during the discussion. Make more of an impact by showing your fees in comparison to competitor's big bank fees for the same services if applicable.

- Ask for the business. This doesn't mean asking the consumer every minute, "Are you ready to open the account?" That becomes annoying and feels just too-over-the-top salesy and insincere. Instead, try approaches that make the consumer feel at ease, not just a notch on the sales belt. For example, "If you have your driver's license with you today, I can start the process now, it should only take 10 – 15 minutes." And if they are not able to commit at that moment, make it clear that you do want them as a customer or member by reminding them why your financial institution is a good option, "We would really love to have you bank with us - our Prime Time Checking account looks like a perfect fit for your checking needs…".

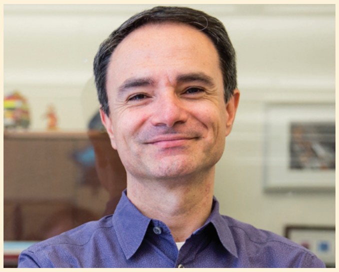
Each of the skills listed above can be learned and implemented if your frontline staff is provided with the tools to recognize these opportunities. Putting the right people in the right position will make everyone's job easier in the long run. For example, it would be an uphill battle to take the quiet accountant/analyst and expect to achieve a "superstar" new account representative. Behaviors can be tweaked, facts can be learned, but starting with someone who truly likes to interact and help people is critical to creating more superstars with your frontline staff.

Jennifer Brooks has over 20 years in the financial marketing industry. She is Chief Marketing Officer at Stellar Strategic Group. To learn more, please contact jennifer.brooks@stellarstrategic.com or 402-281-0692.

Fintech Made Easy: Where to Begin for Community Banking Professionals

A Q&A with Alex Jimenez, Vice President and Senior Strategist at Zions Bancorporation

By Jennifer Brooks, Chief Marketing Officer



Fintech, Blockchain, Neo-Bank, Digital Disruption. These topics have increasingly become commonplace in the banking industry. You want to better understand these concepts, so you Google and find numerous articles on the subject matter. After researching, you can't help but think to yourself, "Interesting, but how does this affect me and my financial institution?"

Fintech: computer programs and other technology used to support or enable banking and financial services.

Blockchain: a digital ledger in which transactions made in bitcoin or another cryptocurrency are recorded chronologically and publicly.

Neo-Bank: a new type of app-only, online bank with no brick and mortar branches or ties to legacy banking systems.

Digital Disruption: any level of change to normal business models and practices caused by new digital technology or processes.

Sound familiar? Don't worry; you are not alone!

I was happy to have the opportunity to ask several fintech-related questions to Alex Jimenez. Currently, Alex leads the technology investment planning process for Zions Bancorporation. He was named one of the top 100 global influencers in Financial Technology (Fintech) by Onalytica, Hot Topics and Jay Palter. Mr. Jimenez has been quoted in the Wall Street Journal, the Boston Globe, The Financial Brand, the American Banker and the Boston Business Journal on this subject.

The following are Alex's insights specific to community-based financial institutions…and, some of his answers might surprise you!

Q: What should community banks and credit unions worry about when it comes to blockchain technologies?

A: While there is significant industry attention and investment in blockchain technology, community banks and credit unions don't need to lose sleep yet. The promise of blockchain technology to revolutionize banking, and many other industries, might prove to be true. However, use-cases for the average banking customer are still in the development and testing phase. Scalability and adoption are areas that need to be addressed.

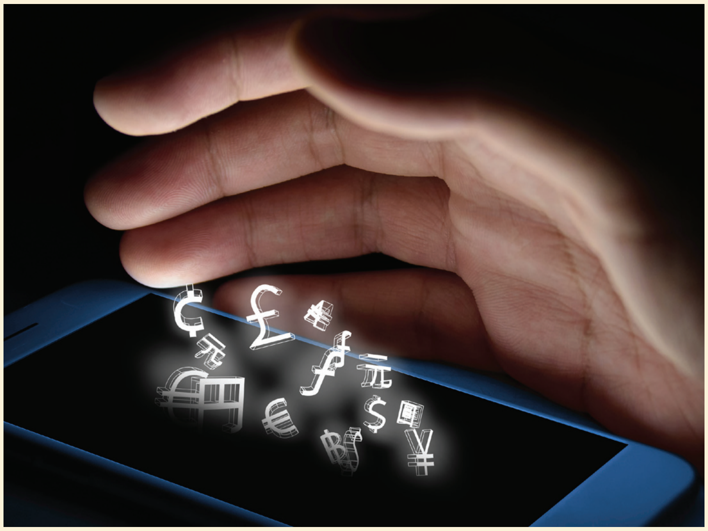
Community banks and credit unions should become aware and educate themselves about the space. They should take opportunities to remain knowledgeable, and if interested participate in tests from their technology partners. They should be ready to jump in when commercially available solutions are available that address a customer or member need.

Q: Are mergers and acquisitions between small and mid-sized financial institutions going to be the only way for them to succeed (from a Fintech perspective)?

A: Absolutely not! Community banks and credit unions can play in the fintech space just as much as any other kind of financial institution. The focus needs to be on meeting customer or member needs and not on what shiny technology is available. Fintech brings a focus on customer experiences that are not saddled with legacy thinking and systems. Community banks and credit unions are better tooled to understand the customer experiences that their customers or members expect compared to the larger institutions. For smaller institutions, the knowledge of their customer base is an asset that can be leveraged to partner with fintech companies - and beat their larger competitors.

Q: Concerning the future of Fintech, if you were the CEO of a $500 million asset financial institution where would you focus in 2018?

A: Understanding your customers' or members' needs is key. That doesn't mean doing surveys and cataloging what they perceive about you. Instead, organizations should endeavor to understand customer needs and behaviors. Merely asking them what they



(Continued on Page 7)

(Continued from Page 6 - Fintech Made Easy)

want won't bring you any insights. Financial institutions should work on anticipating customer experiences that will address customer needs and wants.

As Henry Ford once said, "If I had asked people what they wanted, they would have said faster horses." Financial institutions that stick to looking for faster horses will eventually lose all their customers. In this age of digital transformation, a company's strategy should be built on customers' needs, and not just in digital spaces - but in all interactions.

Q: When talking about "Digital Disruption," what might that look like in the next 12 months in the community banking space?

A: I expect to see more partnerships between fintech companies and community banks or credit unions. I'm not sure if this will start within the next 12 months. The larger and most-forward looking organizations (not always the same) are already moving away from the pack. In the next 12 months, the difference between "digital strategic" organizations and those that are waiting to follow will be very evident. At that point, some will have a very difficult time catching up. In the age of digital disruption, there is no such thing as a fast follower, particularly in an industry where the least complicated technology project takes a year at best.

Q: What is a "Neo-Bank" and what effects will that have in the banking industry over the next five years?

A: A Neo-Bank is a fintech bank that is 100% digital. Unlike an established bank, they are built on brand new platforms for both the underlying systems and the customers' experience. There are very few banks in the U.S. in that space mostly because of regulatory hurdles in starting a new bank. There are many newer digital-only banking providers from established organizations like TIAA-CREF and Discovery. However, most of them are built on legacy systems and suffer from the same limitations as traditional banks' digital efforts.

Other brand-new, digital-only banks, like Moven and Simple (now part of Spain's BBVA), get closer to the ideal of Neo-Banks, but they still must contend with a certain level of non-digital legacy systems from their partner banks. Goldman Sachs' Marcus is said to be a true Neo-Bank built from the ground up using digital technology. There are many Neo-Banks in Europe like Germany's N26 and Fidor or the UK's Monzo and Sterling. The bottom line is that we will see a lot of innovation coming from other markets, but the average U.S. community bank and credit union won't have to worry about them anytime soon. These first models are an opportunity to learn from and, in some cases, partner with in the future.

For more information about Alex Jimenez, visit his website at alexjimenez.info or email alex@alexjimenez.info. You can also follow Alex on Twitter and LinkedIn.

Jennifer Brooks has over 20 years in the financial marketing industry. She is Chief Marketing Officer at Stellar Strategic Group. To learn more about digital marketing, please contact jennifer.brooks@stellarstrategic.com or 402-281-0692.

STELLARSTRATEGIC

ABOUT US

Our Beginning

In 2000, our founder had a vision of applying what he had developed in the newspaper industry to acquire new customers and duplicate it in the banking industry. Never did he envision we would have been fortunate enough to have worked with over 1,700 institutions since that time.

Relationships

Achieving strong, long-lasting relationships with our clients is a top priority for Stellar Strategic Group. Simply stated, we continually evolve our product line to meet the ever changing market demands our clients face. Plus, we work to deliver the projected ROI promised, and treat your budget as if it's our own. The bottom line is that we care about each of our clients and it shows in how we partner with you to achieve your goals every step of the way.

Market Growth

Today we offer a suite of products that do one thing extremely well. That one thing is helping our clients grow retail market share at a pace that exceeds that of their competitors. If you have an interest in working with a company that successfully combines traditional marketing approaches with the ever-changing digital marketing revolution, Stellar Strategic Group can help.

Partnership

If you appreciate working with a partner as opposed to a vendor, Stellar Strategic Group is definitely that company. We are committed to building strong, mutually beneficial relationships and recognize not all client projects can be handled the same way. That's why we work closely with you to meet your individual needs.

Put the power of Stellar Strategic Group to work for your institution. Contact us today.

Contact Us: Email info@stellarstrategic.com or call (toll free) 866.347.5632

www.stellarstrategic.com

Corporate Office: 60 West Street, Suite 215, Annapolis, MD 21401