clearwater
CREDIT UNION

Strategic Plan
2020 – 2024

The Principles of Values-Based Banking

CLEARWATERCREDITUNION.ORG/STRATEGIC-PLAN

Our Mission To be a force for good in banking, in the communities we serve, and in the lives of our members.

Together We Own
We practice responsible banking, grounded in cooperative ownership.

Together We Empower
We solve problems and create opportunities for a better tomorrow.

Together We Include
We choose to be inclusive, not exclusive.

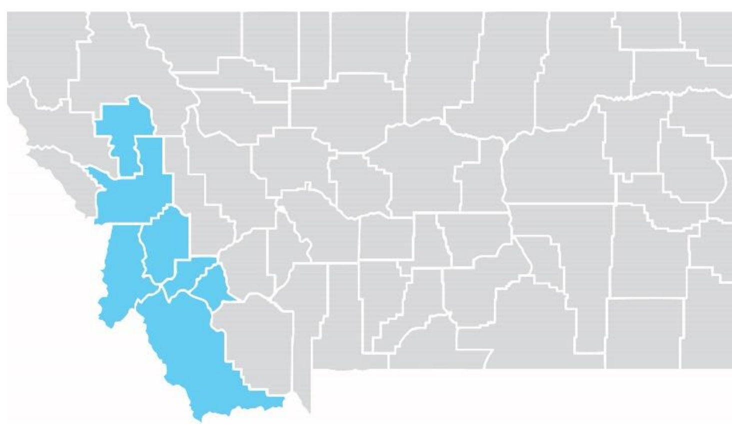
Together We Matter
We are committed to making a difference in the world.

Our Vision By living our values, we will redefine the role financial institutions play in building thriving, sustainable communities.

Part 1 – Diagnosis

Clearwater is a 64-year old credit union, the second-largest credit union in Montana, and the state's largest CDFI. Recent economic performance has been solid: our balance sheet has been growing at approximately 6% per year, loan balances have been growing at more than twice that rate, credit quality is outstanding, profitability is better than peers, and the net worth ratio has been trending upward and is now around 11%.

Three years ago, in 2017, we adopted a Values-Based Banking strategy. We clarified our core organizational values and restated our mission and vision. Since then, we have been working to better align our business operations and balance sheet with those values.



We also recently expanded the credit union's Field of Membership (FOM). We now serve seven southwestern Montana counties, home to 250,000 people. We currently do so from six branches concentrated in and around the Missoula market (one is in Stevensville). In 2020 we will add a branch in Butte.

All of these things—the solid economic performance, the pivot to Values-Based Banking, and the expansion into new markets—are signs of success. However, like any financial institution, we face complex and inter-related challenges. Four of these challenges stand out:

Scale. We are a mid-sized credit union. Yet the industry as a whole is moving rapidly toward larger scale. Benefits to larger size include greater economic efficiency, expanded lending capacity, and increased technological capabilities.

Local competition. Clearwater faces intense local competition. Nationally, there is one financial institution for every ~28,000 people. In our FOM that number is closer to one institution for every 7,100 people. Put another way, our FOM should have nine or 10 financial institutions, but in fact, there are 37.

Fintech competition. In addition to local competition, we also face a growing threat from Fintech. Technology companies moving into financial services threaten to unbundle financial services with product-specific value propositions, first-rate digital interfaces, strategic use of big data, and massive marketing budgets. The proximate threat is not so much deposit-taking or lending – our core business activity – but payments. Google, Apple, Amazon, and PayPal are all fighting to insert themselves between consumers and their traditional financial institutions.

Demographics. Montana's population is aging, making it increasingly important that the brand, products, and services attract and retain the younger populations that all financial service providers are fighting for.

Our strategy needs to confront all of these challenges. It must position us to grow, differentiate us from our competition, keep us technologically competitive, and appeal to a younger demographic.

Part 2 - Strategy

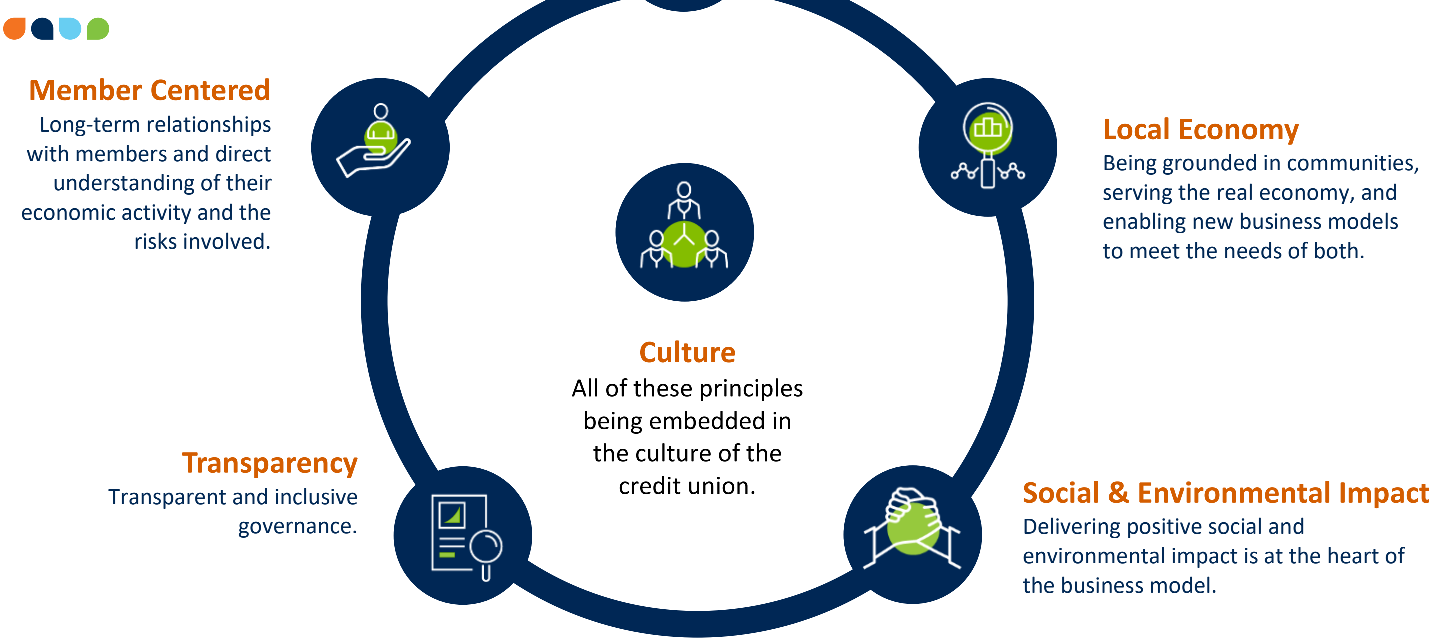
We will continue to adhere to a Values-Based Banking strategy. Within that strategy we will pursue two strategic imperatives.

- First, we must continue to improve on the business fundamentals. Excellent member service, profitable business lines, and careful cost control are the economic foundation of our success.

- Second, we will deepen and improve our ability to measure our commitments to Values-Based Banking.

We see these two strategic imperatives as complementary. We aim to always be competitive on price, competitive on product, and *best* on shared values. We aim to stand out as different in a world where financial institutions are often seen as too complex, too removed from the real world, and too focused on short-term profit to pay attention to the social, economic, and environmental consequences of their actions. Our Values-Based Banking strategy is built around five principles, each of which is firmly embedded in our culture.

Five Principles of Values-Based Banking



Part 3 - Action

In the following pages we describe the set of complementary activities we will pursue to implement the strategy. The activities are organized according to the five principles of Values-Based Banking.

The First Principle: Member Centered

We are a member-owned cooperative. We aim to build long-term relationships with our member-owners, not just transact with them on a one-off basis. To that end, we try to understand their economic activities, problems, and opportunities. We then design products and services to meet those needs.

What will we do to <u>deepen</u> *and* <u>measure</u> our commitment to this principle?

- ***Membership Growth.*** Membership growth is critical to our success. People's decisions to join the credit union, use our products and services, and stay throughout their financial life are the most important indicator of success in our commitment to member-centered banking. Currently, we lack a clear and compelling overall Membership Growth Strategy. That is beginning to show in our membership growth rates, as can be seen in the table below.

Year	2015	2016	2017	2018	2019
Membership Growth Rate	4.32%	4.05%	3.80%	2.03%	1.97%

In early 2020, we will develop and implement a Membership Growth Strategy. We will reverse the declining membership growth rate. We will track and report metrics covering new member acquisition, reasons for member exit, and overall net membership growth. We will target the following growth rates:

Year	2020	2021	2022	2023	2024
Membership Growth Rate	3.00%	3.25%	3.50%	3.75%	4.00%

<u>Measurement</u>

  - New members (and reasons for joining)
  - Lost members (and reasons for exit and tenure)
  - Net membership growth (by geography)
  - Existing Member Demographics (by geography, tenure, and demographics)
  - Conversion and product utilization rates as young members transition into later stages of life

- ***Member Voice.*** As a member-owned cooperative, we should have clear and easily accessible opportunities for our members to exercise their voice. Today we do not. During the year 2020, we will develop channels for members to provide both solicited and unsolicited feedback. These opportunities will be available in branches, within the website and mobile banking, via email, and via telephone. In addition, beginning in 2021, we will conduct an annual Member Product and Service Needs Assessment. We also recognize that the depth of members' relationship with the credit union is an important indicator of their satisfaction with the quality of our products, service, and pricing. We will continue to measure and monitor that depth of relationship.

<u>Measurement</u>

  - Member satisfaction levels findings from the on-going feedback channels
  - Utilization rates of these feedback channels

- Product and service adequacy findings from the annual Member Product and Service Needs Assessment
- Trends in members' depth of relationship with the credit union

- ***New Branch Model.*** In early 2020 we will launch a new retail branch model at our Brooks Street campus. This change to our retail banking model has the goal of enabling front line co-workers to do more for members (without handing them off to a "specialist") and freeing branch managers to become more engaged in brand-building and outreach (versus staff management). After a trial period where we collect member and co-worker feedback, the new model will be rolled out to other branches. Success will mean that our branches function as brand builders by demonstrating our core organizational values, serve as membership acquisition centers, and become recognized as places to access product, service, and financial education.

  Measurement

  - Account opening, product and service additions, and loan generation
  - Member satisfaction with the new branch model
  - Change in the depth of relationship of members using the new branch model vs. traditional branches
  - Universal Associate feedback and retention

The Second Principle: Long-Term Resiliency

Financial stability is the foundation for our success. We are focused on long-term sustainability, not short-term gain. We cannot entirely insulate ourselves from the larger economy, but we can manage risk and build protection for long-term resiliency.

What will we do to deepen *and* measure our commitment to this principle?

- ***Fundamental Economics.*** We begin the plan period from a position of relative economic strength. Growth rates are solid, credit quality is outstanding, profitability is above peer, and the net worth ratio is close to 11%. With the one exception of total loan deployment (we still run a loan to asset ratio that is low relative to peer), our fundamental economics are strong. We will manage the balance sheet, income and expenses to achieve continuing solid growth and financial performance. A key objective for the loan portfolio is to maintain appropriate levels of profitability with acceptable credit and interest rate risk. A continued growth in non-rate sensitive relationship shares is assumed which needs to be kept under close review. Financial resilience also includes the ability to withstand shock, so tracking will include metrics to assess the credit union's ability to endure an economic downturn.

  Measurement

  - 7% average annual asset growth rates, with balance sheet exceeding $750 million in 2024
  - 15% average annual loan balance growth rates, with total loans exceeding $530 million in 2024
  - Loan to asset ratio climbing to at least 70% in 2024, with
  - Loan portfolio composition, inclusive of participation or whole loan purchases, with a goal of participations and purchases not exceeding 10% of the balance sheet by YE 2024
  - Funding composition, inclusive of any wholesale or brokered borrowing
  - Efficiency ratio averaging not more than 77% during the 5-year plan period
  - Operating ROA averaging 70 bps during the 5-year plan period
  - Net worth ratio averaging 11% during the plan period, staying within a 10% - 12% range
  - Credit risk: net charge offs to average loans (24-month annualized) not greater than 0.50%
  - Annual assessment of the financial performance, profitability, and risk profile of the major components of the loan and investment portfolios
  - Annual assessment of the financial performance of the major components of funding
  - Annual assessment of the credit union's mortgage retention practices, taking into account profitability and risk profile

- ***Growth Through Mergers.*** Consolidation in the credit union industry continues. The number of credit unions in the U.S. has declined from around 24,000 in 1970 to about 5,750 today. Most consolidation happens through mergers, not credit union failure, and generally consists of smaller credit unions merging into larger ones. Mergers may be driven by regulator pressure, the voluntary pursuit of economies of scale, or by leadership retirement and difficulty recruiting talent into small credit unions. Having recently expanded our FOM, upgraded our core banking system, and changed our name, we are well-positioned to be a partner for credit unions seeking a merger. Sharing our story, building trust, and cooperating with other credit unions is a strategic priority. Any prospective merger must be rigorously analyzed and pursued only if determined to be in the best interest of our members.

  Measurement

  - For any merger that takes place within our FOM, were we considered as a potential partner?

- ***FOM Expansion.*** We recently expanded our FOM from three counties to seven, but we remain a mid-sized credit union in a relatively small market. We currently serve 51,000 members out of a total population of less than 250,000 within our FOM. While our recent expansion has provided the opportunity to win new market share, this will not be easy. We are working on our entry to the Butte market, and we will continue to pursue expansion within our current FOM. We will also continue to seek opportunities to expand our geographic FOM under a federal charter, and to explore the potential costs and benefits of a conversion to a state charter.

  Measurement

  - Has our FOM expanded beyond the current seven counties and 250,000 population by year end 2022?

- ***Technology.*** Traditionally, data security and core banking system stability have been at the heart of credit union technology strategy. Those two concerns remain as important as ever. However, two new concerns have arisen. The first is Fintech, which has transformed the competitive landscape. The proximate threat is not so much deposit taking or lending – our core business activity – but payments. Google, Apple, Amazon, and PayPal are all fighting to insert themselves between consumers and their financial institutions, and they are using payments services to get there. Second, data analytics have increased the value of consumer data. (This is one of the main reasons Fintech is entering the banking space). . To address these concerns, we have developed and will continue to update a comprehensive technology strategy that is designed to provide security, relevance, efficiency, and knowledge. Guiding success principles for technology going forward are:

  - ***Core-centric.*** The value of our new core will increase as we integrate more of our data and processes with the system. As we evaluate ancillary systems, we will find partners that understand the value of core-centric data and processes.
  - ***Information Security.*** We will stay committed to excellence in protecting our member data through the systems we choose, the vendors we partner with, and the co-workers we hire.
  - ***Data Transparency and Analytics.*** Given our commitment to transparency, we need to report impact, results, and the use of resources to our members. This will demand a clear understanding of our data, as well as responsible and effective use of that data.
  - ***Leading Edge, not Bleeding Edge.*** To stay relevant, we need to place resources into new technology. We cannot afford to be technology deficient. But we do not need expose ourselves to high-risk ventures.

- ***Staffing.*** Arguably the most import aspect of technology success. We must continue to attract and retain technology co-workers that live our company's values and exemplify our technology principles.

Measurement
- Use of on-line and mobile banking tools
- Number and impact of data security incidents
- Number and impact of business continuity incidents

- ***Branch Metrics.*** We lack accurate and actionable information about the productivity, profitability, and member use of individual branches. This hinders strategic analysis, resource allocation and learning across the branches. With a new core banking system and our expansion into new markets, correcting this deficiency has become an important priority. In the year 2020 we will develop a branch metric tracking system.

Measurement

- Number of members joining and exiting at each branch (including demographics)
- Number of new member *accounts* opened at each branch (including demographics)
- Number of members connected to each branch through active use (including demographics)
- Number, dollar value, and types of loans originated at each branch

- Branch balance sheets, income, and expenses

The Third Principle: Local Economy

Our first priority is to meet the financial needs of the individuals, households, and small businesses that make up our membership. This includes a commitment to investing in the local economy. We will track this commitment in the four core financial segments: assets, liabilities, income, and expenses.

What will we do to deepen *and* measure our commitment to this principle?

- ***Assets.*** Local lending is perhaps the most important function we perform. Loans to members meet local economy credit needs, stimulate local economic activity and represent the highest return assets on our balance sheet. Loan products must be competitively designed, competitively priced, and supported by our operations such that local economy lending dominates our balance sheet. We also have a strategic advantage in our in-house mortgage servicing capacity that should be further developed and leveraged.

Measurement

- Local economy assets as a proportion of total assets. (Numerator includes loans to people and small businesses within our FOM, unfunded commitments to people and small businesses within our FOM, mortgage balances managed within our mortgage servicing portfolio, municipal bonds purchased within Montana, and fixed assets. Denominator includes total assets plus mortgage balances sold-and-serviced)
- Local economy assets ratio of at least 80% by year-end 2022

- ***Liabilities.*** Deposit products must be competitively designed, competitively priced, and supported by our operations such that local economy funding drives the majority of our economic activity.

Measurement

- Local economy funding as a proportion of total assets. (Numerator includes member deposits and member-owned net worth. Denominator includes total assets).
- Local economy funding remains above 90%

- ***Income.*** As with assets, income from local economy loans and fees should make up the bulk of our income.

  Measurement

  - Income derived from local economy assets as a proportion of total income. (Numerator includes all income derived from local economy assets. Denominator includes total operating income).
  - Local economy income greater than 80% by year-end 2022

- ***Expenses.*** As part of our commitment to the local economy, we will strive to spend locally wherever we can.

  Measurement

  - Local operating expenses over total operating expenses, with a target of growth year over year.

- ***Geographic Reach.*** Historically, our branch network and membership has been concentrated in the Missoula market. However, our FOM now includes seven counties in southwestern Montana. By early 2020 we will have a new branch in Butte, our second facility outside of Missoula (joining Stevensville). We also have a reasonably robust set of remote delivery options, from account opening through account funding and lending. Brand building, marketing, and outreach must begin to reach all corners of our FOM.

  Measurement

  - Number of members in each of the counties in our FOM
  - Number of businesses in each of the counties in our FOM
  - Deposit balances mobilized from members in each of the counties in our FOM
  - Loan balances managed in each of the counties of our FOM
  - All the above normalized by the population of each county

The Fourth Principle: Social and Environmental Impact

Generating reasonable profit is essential to our long-term success. But is not a stand-alone objective. We also want our resources and balance sheet to work toward delivering positive social and environmental impact by: 1) building inclusive economies; 2) empowering people; and, 3) protecting the environment. We recognize that not every product or service we offer will meet these objectives, but we are committed to increasing the share of our resources and balance sheet that do. We are focused on both measuring and reducing the adverse climate impact of both our business operations and our balance sheet.

What will we do to deepen *and* measure our commitment to this principle?

- ***Business Operations.*** Here we focus on measuring and reducing the environmental impact of our business operations. We empower a team of co-workers (the Green Team) to measure our environmental impact and pursue management and reduction goals. This work is documented and published on our website.

  Measurement

  - Greenhouse gas emissions
  - Water consumption
  - Paper consumption

- Solid waste production
- Tracking and reporting progress towards the goals of our Environmental Management Plan

- ***Balance Sheet Evolution.*** Our lending teams (Consumer Banking, Mortgage Banking, and Business Banking) support a wide variety of member needs, both *traditional* and *impact*. We consider impact loans to be those loans that make an active contribution to 1) building inclusive economies; 2) empowering people; and/or, 3) protecting the environment. Each team has identified the impact loans within its portfolio (attachment 2). Each team is committed to business development in those areas with the goal of increasing the proportion of impact assets on the balance sheet. We will work to measure and track the results of those efforts. In addition, we have a significant securities portfolio (~$200M), which we need to assess for impact alignment. We understand that defining impact characteristics, operationalizing impact categorization, and monitoring results can be difficult and sometimes controversial. We are just beginning this practice. We are committed to refining and improving our approach as we go.

  Measurement

  - Total loans directed to building inclusive economies (in each business line)
  - Total loans directed to empowering people (in each business line)
  - Total loans directed to protecting the environment (in each business line)
  - Total impact assets as a proportion of total assets, with a goal of 2.5 percentage points of annual growth

- ***Balance Sheet Carbon Impact.*** In 2019, along with a number of our partners in the Global Alliance for Banking on Values (GABV), we committed to a concerted, global effort among financial institutions to track and monitor the carbon impact of our portfolio of loans and investments. Following the framework established in the Platform for Carbon Accounting (PCAF) we expect to begin annual measurement and publication in 2021.

  Measurement

  - Carbon impact of total loans and investments on the credit union's balance sheet

- ***Philanthropy and Volunteerism.*** Our philanthropic and volunteer activities are an important part of our mission to use our resources to catalyze positive social, economic, and environmental change. We target annual philanthropy of 5% of net income. We empower our employees to contribute volunteer time to non-profit organizations and initiatives in our FOM. We coordinate volunteer activities, we recognize outstanding volunteer contributions by our co-workers, and we compensate co-workers for a total of 24 hours of time committed to non-profits within our FOM.

  Measurement

  Philanthropy

  - Number of gifts and total dollars directed to building inclusive economies
  - Number of gifts and total dollars directed to empowering people
  - Number of gifts and total dollars directed to protecting the environment
  - County by county geographic distribution of gifts within our FOM

  Volunteerism

  - Number of hours directed to building inclusive economies
  - Number of hours directed to empowering people
  - Number of hours directed to protecting the environment

- County by county geographic distribution of volunteer hours contributed within our FOM

The Fifth Principle: Transparency

Our cooperative structure demands that we practice transparent and inclusive governance. We aim to build open, honest relationships with members, co-workers, and the communities we serve. To that end, we aim for higher levels of transparency in reporting than are required by external rules and regulations.

What will we do to <u>deepen</u> *and* <u>measure</u> our commitment to this principle?

- ***Strategic Plan Metrics.*** Values-Based Banking is what differentiates us from our competition. Deepening and measuring our commitment to these principles helps us track challenges and success. We will track and publish all metrics described in this Strategic Plan.

<u>Measurement</u>

- Completeness, frequency, and accessibility of the reporting

- ***Compensation Philosophy.*** Compensation is our largest single expense category and an important way we reward and empower our co-workers. Our compensation programs are designed to align with our mission, values, and vision. Transparency about compensation is realized through the publication of a Compensation Philosophy document and annual Compensation Metrics.

<u>Measurement</u>

- Average compa-ratio for each job class
- Number of salaries below the range minimum
- Number of salaries above the range maximum
- Base entry level wage versus living wage in our FOM
- Multiple of the highest paid co-worker to the lowest paid co-worker
- Average compa-ratio by gender for each job class
- Challenges in attraction, retention, and turn-over related to compensation

Part 4 - Culture

The five principles of Values-Based Banking are embedded in our organizational culture. Our culture is shaped by our organizational values. Above all, we accept the responsibility to serve our co-workers and members at the highest ethical standards. And in doing so, we work hard to provide co-workers with: 1) the tools to succeed; 2) a voice in decision-making; and, 3) the power to solve problems.

What will we do to <u>deepen</u> *and* <u>measure</u> our commitment to strengthening the culture?

- ***Internal Product and Service Training.*** Excellence in internal training is an important part of our culture. We provide co-workers with an outstanding suite of compliance, operational, behavioral and leadership training opportunities. However, to serve our members effectively, our co-workers also need to have a clear and reasonably complete understanding of the products and services we offer. We have heard from our co-workers that we have room to improve. We are agreed on the need for better, more on-going, and consistent internal product and service training. We will retool our product and service training in 2020 to ensure first-rate, easy-to-access training content.

<u>Measurement</u>

- Completeness of the suite of training opportunities

- Attendance/participation in training opportunities
- Co-worker rating of training quality
- Regular internal testing and recognition

- ***Diversity, Equity, and Inclusion.*** As a community development-oriented financial cooperative, we are well placed to help address the racial, gender, and wealth gaps that exist in the communities we serve. We also recognize that this work needs to start from within and that we ourselves can and must do a better job at ensuring that we have a healthy diversity of perspectives and voices in our organizational management, leadership, and governance.

  Measurement
  - In 2020 we will develop a formal Diversity, Equity, and Inclusion Plan

- ***Open Management.*** In addition to working hard to provide clarity about mission, values, vision, and strategy, we recognize a need to increase the transparency and openness of our management and governance. This includes generating input and feedback from our workforce to inform management and governance.

  Measurement
  - A CEO message to all co-workers will follow Executive Team meetings (at least monthly)
  - A Board Chair message to all co-workers will follow Board meetings (monthly)
  - Co-workers will have an opportunity to respond to these communications with their own questions, comments, and input

OUR CULTURE IS SHAPED BY OUR ORGANIZATIONAL VALUES.

Above all, we accept the responsibility to serve our co-workers and members at the highest ethical standards. And in doing so, we work hard to provide co-workers with:

1) **The tools to succeed;**
2) **A voice in decision-making; and,**
3) **The power to solve problems.**

- ***Effective Meetings.*** Many people within the organization spend a good deal of time in meetings. If our meetings are engaging, efficiently run, productive and inclusive of the right people, they strengthen the culture. If they are not, they erode the culture. In 2020 we will establish an Effective Meetings Task Force to do the following
  - Take stock of all standing meetings and internal committee structures
  - Evaluate purpose, necessity, and co-worker composition of all standing meetings and internal committee structures
  - Suggest changes
  - Establish mechanisms for on-going rating and improvement of the quality of all standing meetings and internal committee structures
  - Develop recommendations for implementing remote meetings
  - Propose a training/mentorship/empowerment program to help co-workers lead more effective meetings and provide opportunities for them to use their skills.

  Measurement

  - Recommendations to Executive Team by June 30, 2020
  - Ratings and improvement system in place by December 31, 2020

- ***Annual Strategy Sessions.*** Reinforcing clarity around mission, values, vision and strategy requires frequent assessment, fine-tuning, and re-commitment. Beginning in 2020 we are committing to annual strategy sessions to include all co-workers, working in small groups of 20-25 people each, led by Clearwater's CEO and/or other members of the Executive Team and Board. These will be opportunities to reflect on our progress executing on this strategic plan, they will result in reporting back to Executive Team, and they will be organized around five central questions:
    - Why do we exist? (Mission)
    - How do we behave? (Values)
    - What do we do? (Core Business Activities)
    - How will we succeed? (Strategy)
    - What is most important, right now? (The single strategic priority)

  Measurement
    - Frequency of execution
    - Attendance and participation in the sessions
    - Attendee ratings of the sessions

Part 5 - Conclusion

Over the last several years, Clearwater has delivered a strong financial performance while making significant strategic progress in clarifying and living our commitment to values-based banking. Going forward, we must continue to deliver on both fronts. Fundamental economic performance is the foundation of our success, and strong performance in our core operations must always be a priority. We also need to continue to advance our values-based banking strategy. The goals presented in this plan do both. There is a lot of work here, but this is a 5-year plan. Some activities will be implemented quickly, others will take more time. By working towards the goals in this plan, we will strengthen both our financial position and our commitment to values-based banking.

Appendix

Social and/or Environmental Impact Loans

Line of Business	Loan Purpose Description
Consumer	Loans to Credit Challenged People (<670 score and no score)
Consumer	Loans to Low to Moderate Income Borrowers (Household income <49K outside Missoula or <56K in Missoula)
Consumer	High MPG (>40 MPG city) or Clean Fuel
Consumer	Responsible Debt Consolidation (Lowering fees, rates, DTI)
Consumer	Credit Builder Loans
Consumer	Education Loans
Consumer	Emergency Funding (PAL, medical, primary vehicle repair)
Consumer	Energy Efficiency Loans (Renewables, high efficiency HVAC, bikes)
Mortgage	Loans to Credit Challenged People (<670 score and no score)
Mortgage	Loans to Low to Moderate Income Borrowers (Household income <49K outside Missoula or <56K in Missoula)
Mortgage	First Time Home Buyer Loans
Mortgage	Manufactured Housing Loans
Mortgage	Responsible Debt Consolidation (Lowering fees, rates, DTI)
Mortgage	Affordable Housing (Housing payment < 30% of income, primary residence, to 120% AMI)
Mortgage	VA, MBOH, Rural Development
Mortgage	Home Equity Finance to Improve Building’s Environmental Performance
Mortgage	Construction and Permanent for High Environmental Performance Buildings
Business	Social and/or Environmental Impact Business Model
Business	Social and/or Environmental Loan Purpose for Traditional Business Model
Business	Underserved, Minority, Female Ownership
Business	Construction and Permanent Loans for High Environmental Performance Buildings
Business	Microfinance (Small business loans less than $50,000)