Legacy Community Federal Credit Union retains revenues and enhances branch profitability with ProfitStars®

What started out as a project to satisfy regulators has turned into a powerful planning and financial management model for Legacy Community Federal Credit Union – helping it make portfolio decisions valued at $100,000 in annual revenue, and allocating resources to enhance profitability at its branches.

Legacy Community FCU is a nearly $200 million credit union that has grown from its university roots in Birmingham, AL, to serve residents, students and workers in the seven-county Greater Birmingham/Hoover Metropolitan Statistical Area. In 1999, regulators required the credit union to establish a system to monitor its exposure to interest rate risk. Legacy Community FCU chose the PROFITstar ALM/Budgeting software and PROFITability® model delivered by ProfitStars®, a division of Jack Henry & Associates.

“The main reason we installed PROFITstar ALM/Budgeting at that time was to satisfy a regulatory requirement,” recalls Paula Miller, senior vice president of finance. But since then, Legacy Community FCU has discovered that it delivers a powerful strategic and decision-support tool as well – and therein lies the unique value proposition of this application.

“Bankers have to realize that examiners and managers view asset/liability management (ALM) differently,” notes Martin Webster, a sales director with ProfitStars. “Both views are correct, but they naturally have different intents. Contrary to popular belief, ALM should be used to control risk, but never to minimize risk. If you sought to minimize risk, you would have no loans and no investments other than Treasuries. Controlling risks means finding an acceptable and manageable level of the different risks while meeting the goals of the financial institution.”

Why nots and what-ifs
Prior to installing PROFITstar ALM/Budgeting, Legacy Community FCU used spreadsheets for financial analysis; of course these tools did not have the capability to perform rate shocks or net economic value (NEV) analysis. With the PROFITstar ALM model, Miller can easily analyze the impact on net interest margin, net income, ROA and other key metrics under different interest rate scenarios by running the Interest Rate Risk Sensitivity Analysis (IRSA) and by looking at the fair value matrix. This contributes to a better management of not only short-term interest rate risk on earnings but also the long-term risk on capital through the NEV analysis. Miller uses these tools to evaluate and recommend strategic product and pricing decisions to the management team.

At one time, Legacy Community FCU was considering whether it should sell its credit card loan portfolio. By running the what-if simulation, Miller showed that Legacy Community FCU could make much more money by keeping it rather than selling it. Legacy Community FCU decided not to sell the portfolio, which now returns revenues of more than $100,000 per year. “One of the biggest benefits of the model is its ability to do what-ifs,” says Miller. “We made our decision to keep our credit card portfolio using the what-if scenario analysis. It helps us to keep a huge amount of revenue in our credit union.”
Most of Legacy Community FCU’s loans are home equity and automobile loans. Before deciding to promote any particular product, Miller runs a what-if model to see what the financial impacts would be. The model can predict the break-even on promotional expenses, generate multiyear revenue forecasts and support insights into balancing competitive and profitability factors when pricing the loans.

Another useful application is that each year, before launching a “swap and drop” loan promotion program, Miller runs a what-if model. A “swap and drop” loan is a special loan extended to members when they swap their loans from another institution to Legacy Community FCU; the interest rate offered is below the general market rate. “We generally know the volume of new loans we can expect, so we pick a rate we’re going to offer and run the analysis to evaluate our interest margins and rate shock,” Miller says. Legacy’s promotion typically lifts monthly loan production by about 50 percent — to $3.5 to $4 million per month versus an average of $2.5 to $3 million per month.

**Better, faster budgeting and reporting**
In the past, the preparation of the monthly board package was very time consuming and creating the annual budget was extremely cumbersome. The Projection and Budgeting functions in the PROFITstar ALM/Budgeting model have helped Legacy Community FCU streamline these processes.

“Without the model, it took two days just to prepare the reports for board presentation. Now it takes only half a day!” Miller exclaims. “I can produce graphs and reports much faster. The model makes budgeting so much easier too.” In fact, the PROFITstar ALM/Budgeting model has reduced the time required to develop the annual budget by about 60 percent. Moreover, any required changes from senior management to the proposed budget can be quickly input into the model and the recalculated figures are available faster.

**Making branches more profitable**
While ALM/Budgeting provides a powerful financial modeling tool, ProfitStar’s companion PROFITability solution provides P&L visibility down to the branch and product category. Miller uses the PROFITability model every month to produce branch financial reports for both branch managers and senior management.

One of the most helpful management disciplines enabled by PROFITability is that the true contribution of each branch to Profit & Loss can be accurately measured. By applying “matched Funds Transfer Pricing (FTP),” management sees a level playing field among its branches and can develop an “apples-to-apples” comparison among them.

Miller applied this model to the 11 branches of Legacy Community FCU, where some branches made loans and acted mainly as funds users, but some branches took members’ shares and acted as funds suppliers. With FTP and by allocating the indirect costs, Miller realized there were a couple of branches that were not as profitable as she initially thought. In one instance, she noted a branch in a declining area could no longer produce the loan volume it once had. She then worked to make the branch more efficient by changing the controllable items to better match its income and expenses. For example, she transferred the higher paid employees from that branch to another branch to lower costs. As a result, the staff resources were better allocated to improve the overall bottom line of the credit union. In addition, it helped management better understand which expenses were controllable and which were not and to reward the branch employees accordingly.

At Legacy Community Federal Credit Union, Paula Miller and her team continue to prove that when it comes to PROFITability, what’s good for the regulators can be good for management as well.