NCUA LETTER TO CREDIT UNIONS

NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA

DATE: **May 2003** **LETTER NO.: 03-CU-09**

TO: **Federally Insured Credit Unions**

SUBJ: **Credit Union Financial Trends for the First Quarter of 2003**

ENCL: **Financial Trends in Federally Insured Credit Unions - January 1, 2003 to March 31, 2003**

DEAR BOARD OF DIRECTORS:

Enclosed is a report highlighting credit union financial trends for the first quarter of 2003. We based our analysis on data compiled from the first quarter 2003 call reports submitted by all federally insured credit unions. We are providing this information to keep you informed of current conditions and trends in the credit union industry.

Thank you for your cooperation in providing this data.

Sincerely,

/S/

Dennis Dollar
Chairman

Enclosure

FINANCIAL TRENDS IN FEDERALLY INSURED CREDIT UNIONS

January 1, 2003 to March 31, 2003

HIGHLIGHTS

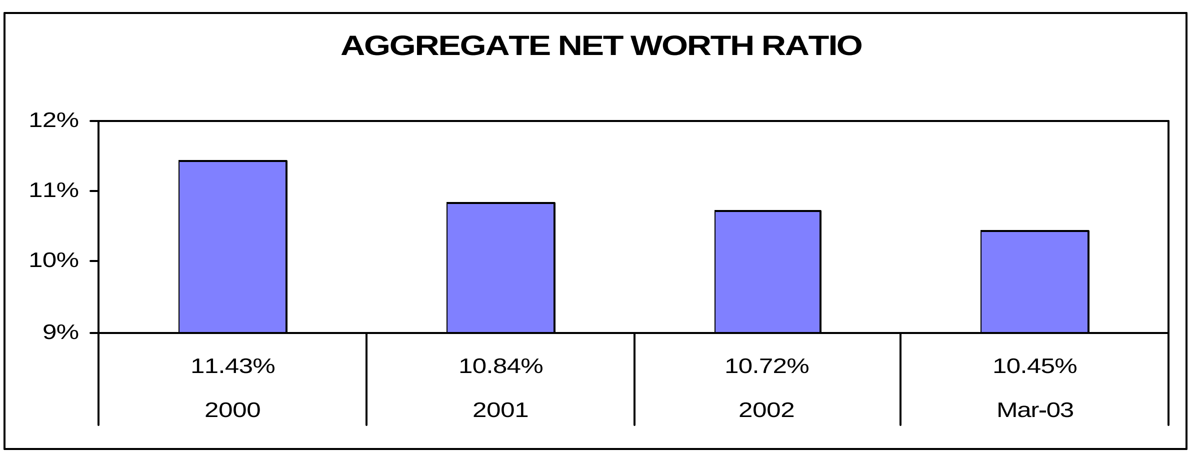
This report summarizes the trends of all federally insured credit unions as of March 31, 2003. This is the first March cycle where all federally insured credit unions were required to file call reports.

Key financial indicators are noted below:[1]

- **Assets** increased $28.4 billion or 5.09%. This equates to an annualized asset growth rate of 20.37%.[2]
- **Capital:** Net worth increased $1.5 billion or 2.47%, while the net worth to assets ratio decreased to 10.45%.
- **Loans** increased $1.9 billion or 0.54%. The loan-to-share ratio decreased to 67.51%.
- **Shares** increased $26.1 billion or 5.39%.
- ***Cash management accounts**, (cash on hand, cash on deposit, cash equivalents*,) **plus short-term investments** (less than 1 year) increased $17.5 billion or 16.88%.
- **Long-term investments (over 1 year)** increased $9.6 billion or 11.33%.
- **Profitability** declined slightly to 1.04% return on average assets.
- **Delinquent** loans as a percentage of total loans declined to 0.74% from the year-end 2002 level of 0.8%. **Net charge-offs** increased from 0.51% to an annualized 0.55% of average loans.

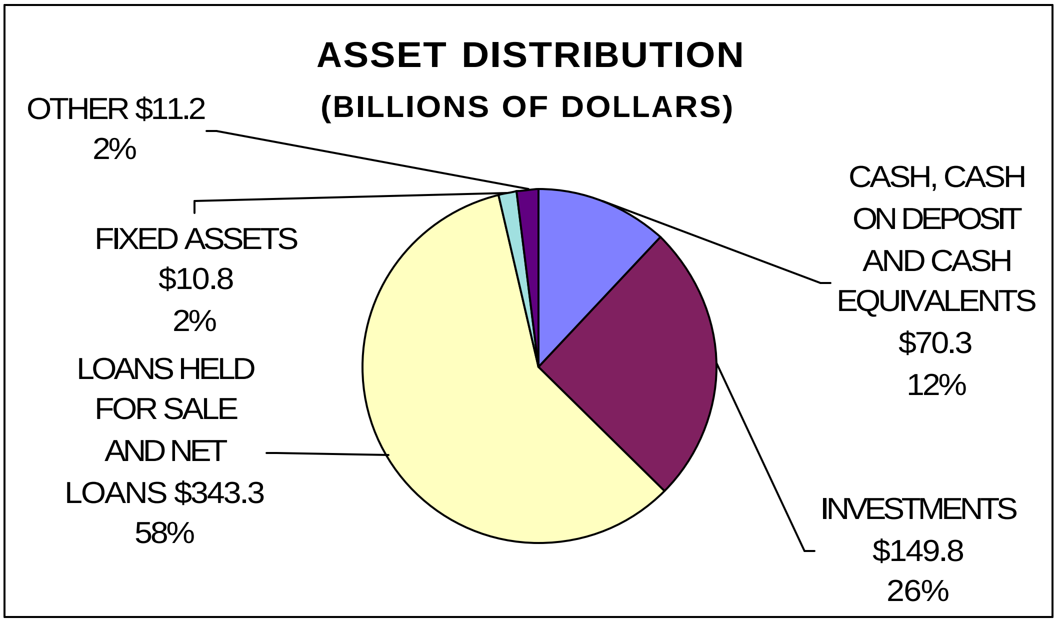
CAPITAL

Total net worth increased $1.5 billion or 2.47% during the first quarter of 2003. The aggregate net worth to total assets ratio decreased from 10.72% at the end of 2002 to 10.45% as of March 31, 2003, as annualized asset growth of 20.37% outpaced annualized net worth growth of 9.89%. The average net worth ratio among individual credit unions decreased from 13.50% at the end of 2002 to 13.11% as of March 31, 2003.



1. *Unless otherwise indicated, all percent changes are year-to-date, and are not annualized.*
2. *Historically the first half of the year exhibits a high rate of growth which moderates during the second half of the year.*

ASSET QUALITY

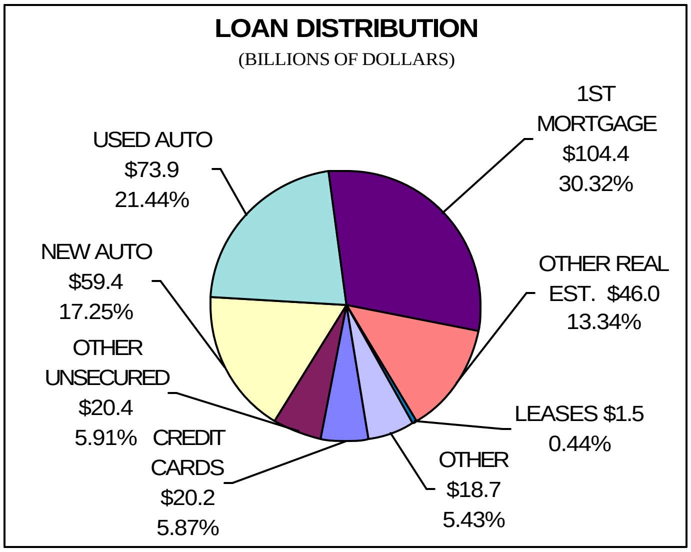


LOAN TRENDS: Total loans increased $1.9 billion or 0.54% through the first quarter of 2003. All loan categories except *Used Auto Loans, First Mortgage Real Estate,* and *Other Loans* decreased. Growth in the various categories was as follows:

- Unsecured credit card loans decreased $1.3 billion or 6.24%;
- All other unsecured loans decreased $0.8 billion or 3.65%;
- New auto loans decreased $1.0 billion or 1.73%;
- Used auto loans increased $1.7 billion or 2.36%;
- First mortgage real estate loans increased $3.7 billion or 3.70%;
- Other real estate loans decreased $0.5 billion or 0.97%;
- Leases receivable decreased $27.7 million or 1.78%; and
- All other loans increased $63.9 million or 0.34%.

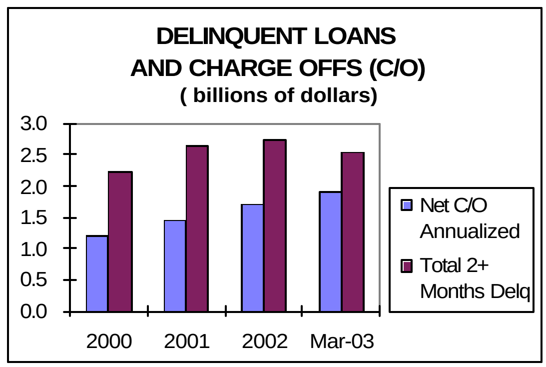
First mortgage real estate loans in the amount of $104.4 billion account for 30.32% of total loans. Used automobile loans comprise the second largest loan category with $73.9 billion or 21.44% of total loans. New automobile loans make up the third largest loan category with $59.4 billion or 17.25% of total loans. Other real estate loans are the fourth largest loan category with $46.0 billion or 13.34% of total loans. These four loan categories account for 82.35% of the total loan portfolio.

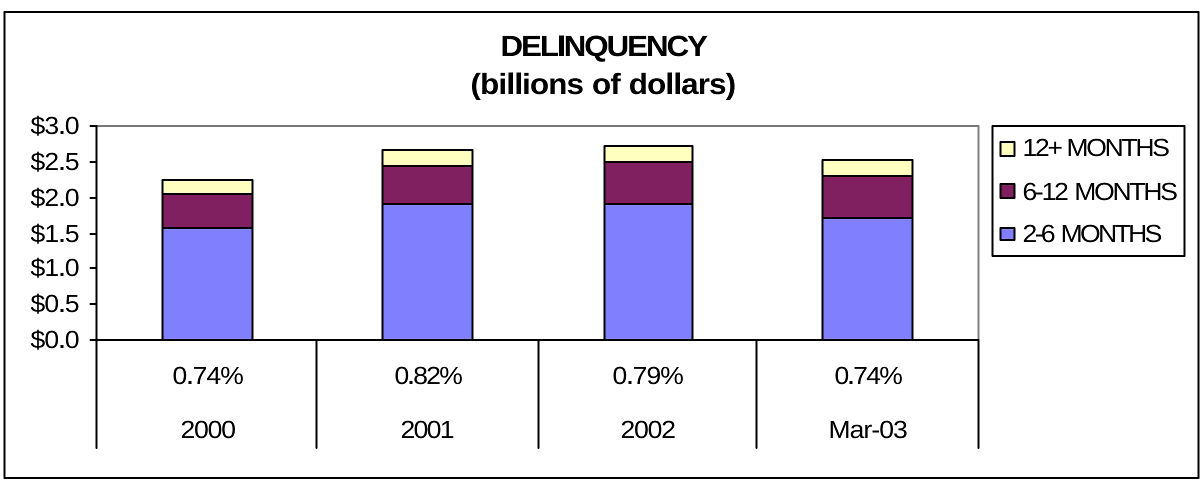
Annualized loan growth was 2.16% while shares grew at an annualized rate of 21.57%, resulting in a decline in the loan-to-share ratio to 67.51%.



DELINQUENCY TRENDS: Delinquent loans decreased $185.4 million or 6.80% through March 31, 2003, and the delinquent loans to total loans ratio declined from 0.80% at the end of 2002 to 0.74%.

Total loans charged off in the first quarter of $552.8 million exceeded the decrease in delinquent loans. The net charge-off loans to average loans ratio increased from the year-end rate of 0.51% to an annualized rate of 0.55%. Annualized Charge-off loan dollars increased 11.07% since year-end 2002, and recoveries increased 6.77%.





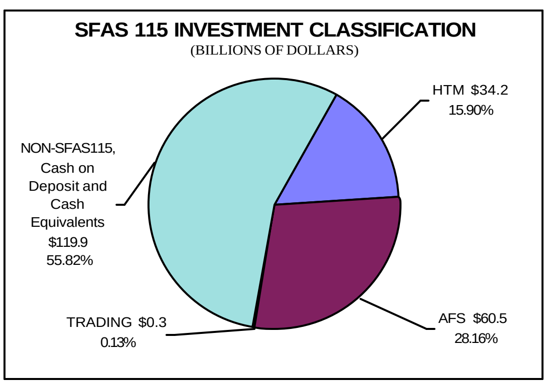
INVESTMENT TRENDS: Total investments increased $27.0 billion or 14.39% through the first quarter of 2003.

Cash management accounts increased $17.4 billion or 36.60%. The combined categories of *cash management accounts*, plus investments with maturities of less than one year increased $17.5 billion or 16.88% through the first quarter of 2003.

Investments with maturities greater than a year increased $9.6 billion or 11.33% with the majority of growth in the three-to-ten year maturity range.

Investment Maturity or Repricing Interval	% of Total Investments 12/2002	% of Total Investments 03/2003
Less than 1 year	55.09%	56.29%
1 to 3 years	32.03%	30.11%
3 to 10 years	11.73%	12.52%
Greater than 10 yrs	1.15%	1.09%

The increase in investments with maturities less than one-year is consistent with the higher increase in the cash management accounts compared to total investments.



Non-SFAS 115 Investments increased from $100.1 billion to $119.9 billion ($19.8 billion or 19.75%). *Held to Maturity* investments increased from $32.2 billion to $34.2 billion ($1.9 billion or 5.93%). *Available for Sale* investments increased from $55.2 billion to $60.5 billion ($5.3 billion or 9.63%). *Trading Securities* increased from $253.5 million to $277.2 million ($23.7 million or 9.36%).

As of March 31, 2003, *Held to Maturity* and *Available for Sale* investments made up 44% of the investment portfolio (16% and 28%, respectively), while *non-SFAS 115 Investments, Cash on Deposit,* and *Cash Equivalents* accounted for 56% of the portfolio (a small amount was classified as *Trading*).

EARNINGS

The large growth in deposits and modest loan growth experienced since 2001, coupled with a low interest rate environment, has significantly reduced the gross income to total assets ratio. Adjustments to the cost of funds, along with a reduction in operating expenses in relation to average assets, limited the decline in the return on average assets ratio to 3 basis points, as noted in the following table.

Ratio	As of 12/2002	As of 03/2003	Effect on ROA
Gross Income	6.94%	6.31%	- 63 bp
- Cost of Funds	2.29%	1.84%	+ 45 bp
- Operating Expenses	3.27%	3.17%	+ 10 bp
- Provision for Loan & Lease Losses	0.35%	0.30%	+ 5 bp
+ Non-Operating Income	0.04%	0.04%	- 0 bp
= Return On Assets	1.07%	1.04%	- 3 bp

ASSET/LIABILITY MANAGEMENT

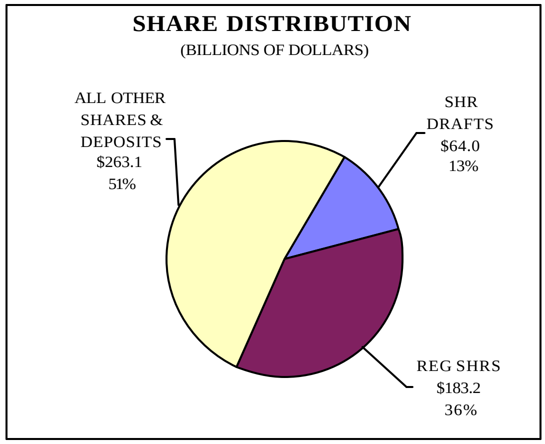
LONG-TERM ASSET TRENDS:
Long-term assets are primarily investments having maturities or repricing intervals greater than 3 years and real estate loans having maturities or repricing intervals greater than 5 years.

In aggregate, Net Long-term Assets increased $7.7 billion or 6.04% in the first quarter resulting in the ratio of long-term assets to total assets increasing from 22.93% to 23.13% as of March 31, 2003. Investments over 3 years showed the largest increase in both dollars and rate of growth increasing $5 billion or 20.75%, followed by real estate loans greater than 5 years which increased $2.3 billion, or 2.64% in the first quarter. In addition, member business loans increased $354 million or 5.32%.

Long-term Assets	In $ Billions		
	12/02	03/03	+/-
Investments >3 yrs	$24.2	$29.2	$5.0
RE Loans >5 yrs	$86.4	$88.7	$2.3
Member Business Loans	$6.6	$7.0	$0.4
Other Net LT	$10.5	$10.5	-
Total Net LT Assets	$127.7	$135.4	$7.7

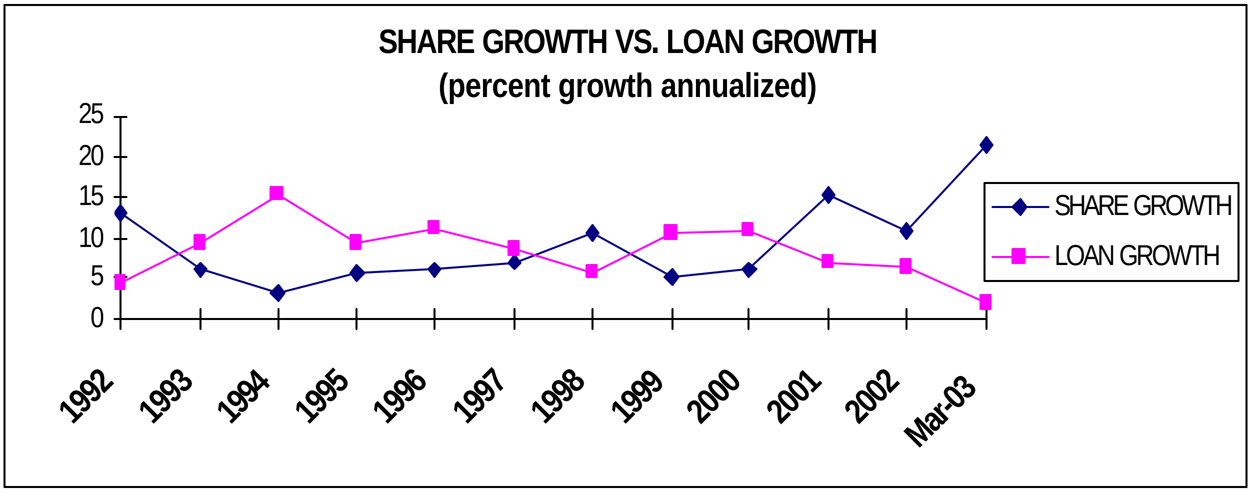
SHARE TRENDS: Total shares increased $26.1 billion or 5.39% in the first quarter of 2003. Most of the growth was in regular shares and share draft accounts. Growth rates for the various share categories are as follows:

- Share drafts increased $6.0 billion or 10.41%;
- Regular shares increased $11.1 billion or 6.45%; and
- All other shares and deposits increased $9 billion or 3.53%.



OVERALL LIQUIDITY TRENDS: As of the first quarter of 2003, credit unions held 21.55% of total assets in cash and short-term investments. This is slightly higher than the historic average aggregate level of approximately 20% of assets. Increased liquidity is also evident based upon the decline in the loan-to-share ratio from 70.77% at year-end to 67.51%.

Annualized Share growth of 21.57% far exceeded annualized loan growth of 2.16%. This continues the recent trend that began in 2001 when the rate of share growth surpassed the rate of loan growth. While some of the first quarter share growth may be a result of seasonal fluctuations, the difference between share and loan growth rates has widened considerably.



If rapid share growth combined with marginal loan growth continues, balance sheet management could become more challenging for credit unions. The credit union industry has adjusted over the past several years to address the inflow of shares and declining yield on assets. Since share growth is concentrated in short term liquid accounts and loan portfolios are shifting toward longer-term fixed rate loans, credit unions must remain vigilant and continue to manage net interest margins during these dynamic economic times.