NCUA LETTERS TO CREDIT UNIONS

NATIONAL CREDIT UNION ADMINISTATION
1775 Duke Street, Alexandria, VA 22314

DATE: March 9, 1998 | LETTER NO.: 98-CU-6

DEAR BOARD OF DIRECTORS:

Enclosed is a report highlighting credit union financial trends during 1997. The analysis is based on data compiled from the yearend 1997 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.

I thank you for your cooperation in providing this data and look forward to any comments you may have.

For the National Credit Union Administration Board,

/S/

NORMAN E. D'AMOURS
Chairman

Enclosure

FINANCIAL TRENDS IN FEDERALLY INSURED CREDIT UNIONS

January 1, 1997 to December 31, 1997

HIGHLIGHTS

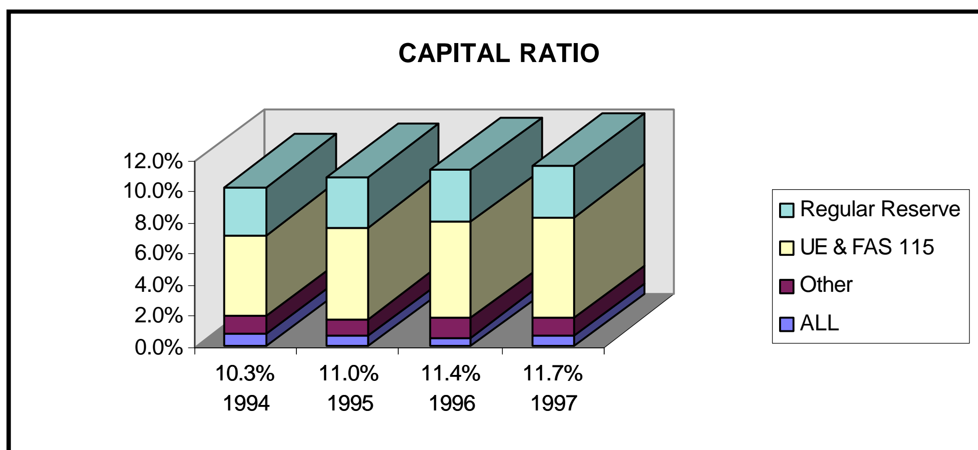
This report summarizes the trends of all federally insured credit unions which reported as of December 31, 1997. As noted below, key financial indicators show strong growth in all areas.

- **Assets** increased $24.3 billion or 7.4%.
- **Capital increased at a faster rate,** 10.3%, a $3.9 billion increase, and the capital to assets ratio now stands at 11.7%.
- **Loans** increased $18.4 billion, or 8.6%, accounting for 76% of the asset growth.
- **Shares** increased $20.5 billion or 7.1%. The loan to share ratio increased to 75.6%, its highest level in this decade.
- **Investments** increased $4.4 billion or 4.4%.
- **Profitability** remained relatively stable with a 1.0% return on average assets ratio.
- **Delinquent** loans as a percentage of total loans remained unchanged from the yearend 1996 level of 1.0%.

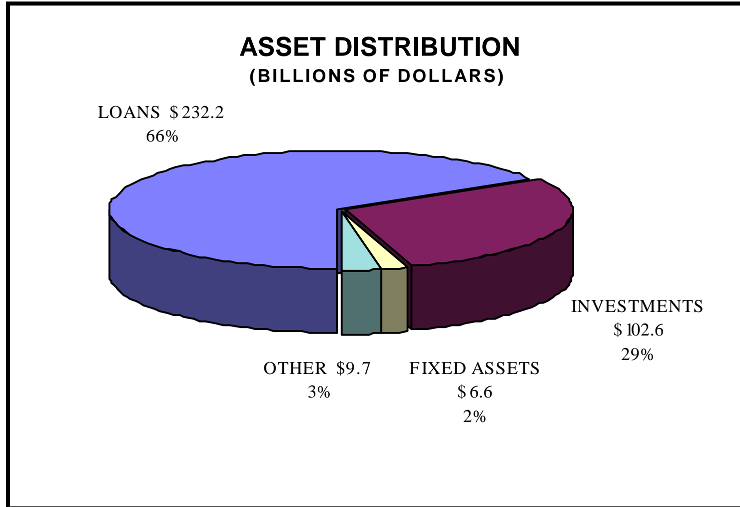
CAPITAL

Total capital increased $3.9 billion or 10.3% during 1997, compared to a 10.8% increase during 1996. The capital to total assets ratio increased from 11.4% at the end of 1996 to 11.7% at the end of 1997.

The net capital to total assets ratio, which measures capital after estimated losses, increase from 10.8% to 11.1%.



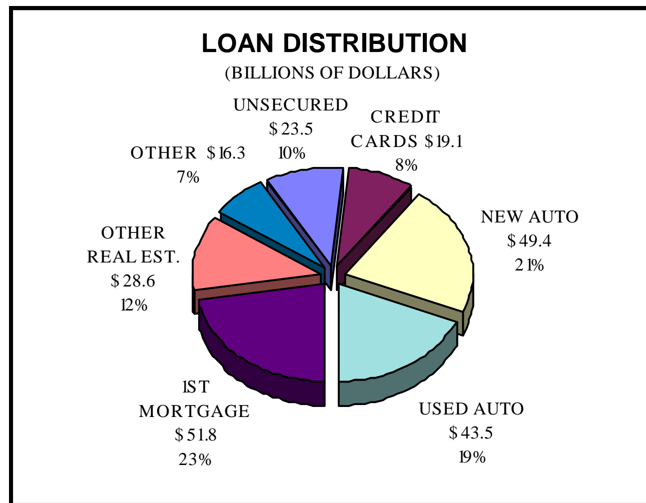
ASSET QUALITY



LOAN TRENDS: Total loans increased $18.4 billion or 8.6% during 1997. Four loan categories accounted for nearly all of the increase:

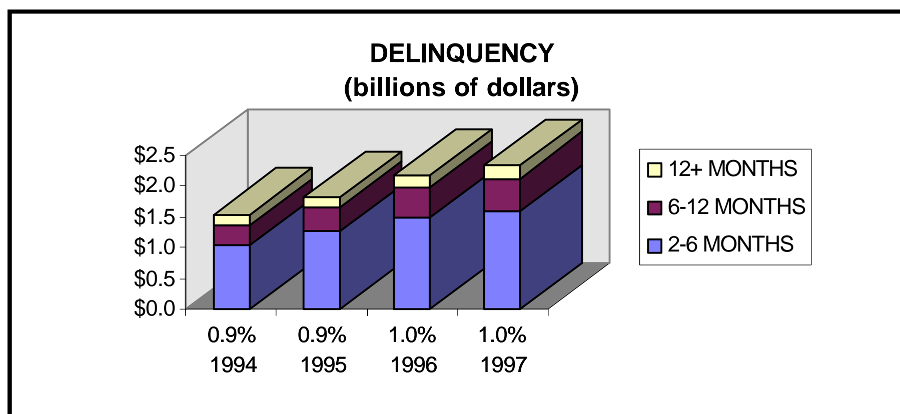
- Used auto loans increased $6.5 billion (17.5% increase);
- First mortgage real estate loans increased $6.2 billion (13.7% increase);
- Other real estate loans increased $3.6 billion (14.2% increase); and
- Unsecured credit card loans increased $1.7 billion (9.7% increase).

Other unsecured loans (excluding credit cards and other lines of credit) was the only loan category which declined ($0.8 billion or 3.4%).

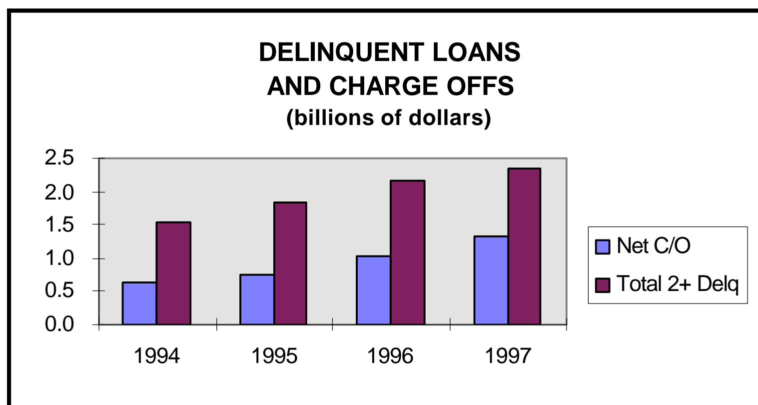


The rate of loan growth (8.6%) continues a 5-year trend of exceeding the rate of share growth (7.1%). As a result, the loan to share ratio increased to 75.6%, its highest level in this decade.

DELINQUENCY TRENDS: After a slight decline during the first half of 1997, delinquent loan dollars increased substantially in the second half of the year. At year end, loans delinquent two or more months increased $172 billion or 7.9% over the 1996 level. Despite this increase, the delinquent loans to total loans ratio remained stable at 1.0% because total loans also increased.



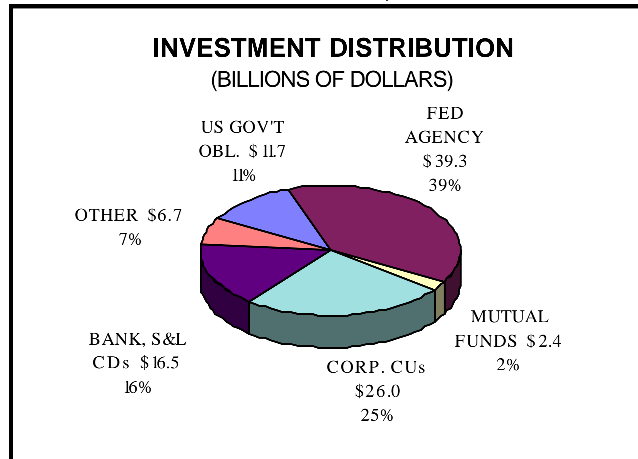
While the delinquency ratio was unchanged, the net charged off loans to average loans ratio increased from 0.5% for 1996 to 0.6% for 1997. This small ratio increase equates to a $319 million increase in loan dollars charged off – a 26% increase over 1996's charge offs. Recoveries on charged off loans increased only 4.7%. Because loan loss dollars increased at a faster rate that total loans, the net charge off ratio increased.



Bankruptcies continue to increase. Credit unions reported more than $1.1 billion in loans subject to bankruptcies in 1997, an increase of 15% over 1996's level. More than 250,000 credit union members filed for bankruptcy, a 25% increase over the 1996 level. Despite the increases, bankruptcies represent only 0.5% of total loans and 0.4% of all members.

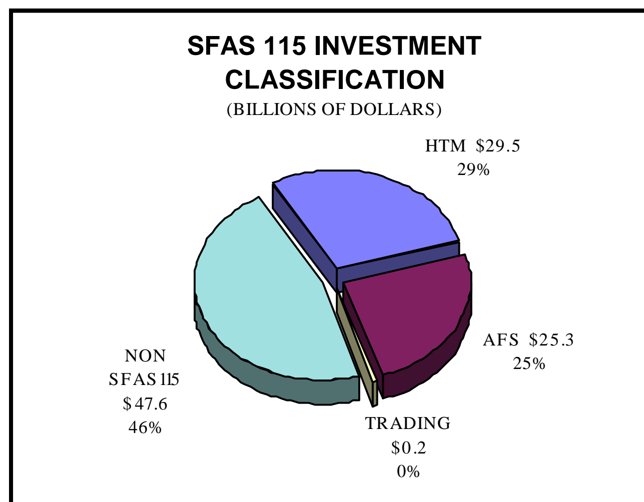
INVESTMENT TRENDS: Investments increased just $4.4 billion (4.4%) during 1997, and represent 29.2% of total assets. This is a decrease from the 1996 level of 30.1% of assets, indicating a shift of asset dollars from investments to loans.

The investment mix also changed, with increases noted in corporate credit union deposits and federal agency securities ($3.3 billion and $2.1 billion, respectively). The largest decline was in U.S. Government obligations, which decreased $2.2 billion.



During 1997, investments with maturities or repricing periods less than 1 year increased 11.7%, while investments with maturities between 1 and 3 years decreased 8.8%. This indicates that credit unions are reducing the maturities of the overall investment portfolio.

During the past twelve months, the investment portfolio has shifted somewhat from *held to maturity* and *available for sale* investments into *non-SFAS 115* investments. At the end of 1996, *held to maturity* and *available for sale* investments made up 60.3% of the investment portfolio (35.6% and 24.7%, respectively), while *non-SFAS 115* investments accounted for 39.4% of the portfolio (the remainder was classified as trading). As noted on the graph below, *non-SFAS 115* investments now account for 46.3% of the portfolio. This is due in part to an increase in investments in corporate credit unions.



Investments in the 3 to 10 years maturity category and greater than 10 year maturity category increased only nominally (3.5% and 0.6%, respectively). The following table compares the changes in the maturity structure of the investment portfolio during 1997.

Investment Maturity or Repricing Interval	% of Total Investments Dec. 1996	% of Total Investments Dec. 1997
Less than 1 year	56.3%	60.2%
1 to 3 years	28.9%	25.2%
3 to 10 years	10.2%	10.1%
Greater than 10 yrs	4.6%	4.5%

EARNINGS

The earnings ratios remain substantially unchanged from yearend 1996, with differences noted in mere basis points. A minor increase in the gross income to average assets ratio was offset by increase in the cost of funds and operating expense ratios. Provision for Loan Loss expense shows the most significant increase; which although minor, resulted in a decreased Return on Average Assets ratio, as noted in the following table. This is consistent with the increase in net charge offs discussed earlier.

Ratio	As of 12/96	As of 12/97
Gross Income	8.33%	8.41%
Cost of Funds	3.61%	3.64%
Operating Expenses	3.27%	3.32%
PLL	0.35%	0.44%
ROA	1.11%	1.03%

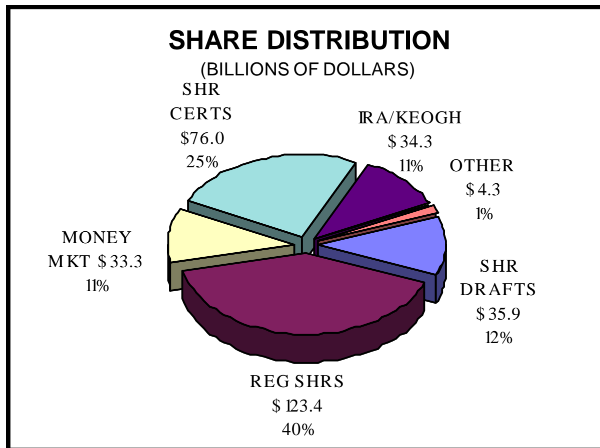
ASSET/LIABILITY MANAGEMENT

LONG TERM ASSET TRENDS: Long term assets continue to increase as a percentage of total assets. These assets, which have maturities or repricing intervals greater than 3 years, equaled 20.2% of total assets, compared to 19.0% at the end of 1996. This increase is the result of growth in first mortgage and other real estate loans discussed earlier.

SHARE TRENDS: Total shares increased $20.5 billion or 7.1% in 1997, compared to 6.1% in 1996. Growth rates among the various share categories were consistent with 1996 growth rates, with the exception of share drafts. During 1997, share drafts increased 12% or $3.8 billion, compared to share draft growth of $1.7 billion or 5.6% during 1996. While it is unclear exactly why this level of growth occurred, it may be due to the high fees for checking accounts charged by other financial institutions.

Growth rates for 1997 in the various share categories are as follows:

- Share drafts -- ↑ $3.8 billion, 12.0%;
- Regular shares -- ↑ $1.5 billion, 1.2%;
- Money market shares -- ↑ $4.5 billion, 15.8%;
- Share certificates -- ↑ $9.6 billion, 14.5%;
- IRA/Keogh accounts -- ↑ $0.6 billion, 1.8%;
- Other shares -- ↑ $136 million, 4.0%; and
- Nonmember deposits -- ↑ $250 million, 50%.

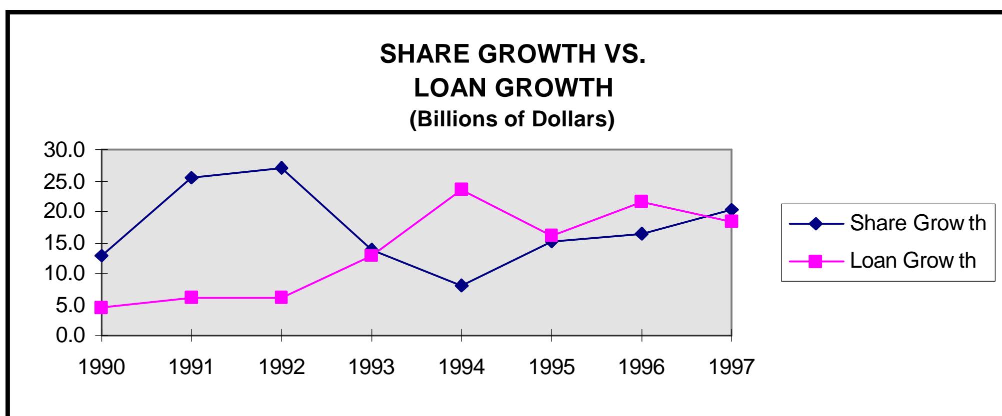


Consistent with the large increase in share certificates, share growth during 1997 was concentrated in shares with maturities or repricing intervals between 1 and 3 years. These shares increased 23.0% ($4.8 billion). Although the dollar increase in the less than one year category was higher ($15.8 billion), it represented an increase of just 6.1%. Shares with maturities greater than 3 years declined $73 million (1.3%).

Share Maturity or Repricing Interval	% of Total Shares Dec. 1996	% of Total Shares Dec. 1997
Less than 1 year	90.9%	89.9%
1 to 3 years	7.3%	8.3%
3 or more years	1.9%	1.8%

OVERALL LIQUIDITY TRENDS: As previously noted, 1997 was the fifth consecutive year that that rate of loan growth (8.6%) exceeded the rate of share growth (7.1%). However, 1997 was the first of these 5 years where share dollars increased more than loan dollars ($20.5 billion and 18.4 billion, respectively). The remaining share dollars ($2.1 billion) appear to have been placed in short term investments.

The trends of loan growth versus share growth are well defined over the past eight years, as illustrated in the following graph.



Since the beginning of 1990, share growth exceeded loan growth by $30.3 billion in total. During the periods when share growth exceeded loan growth, excess funds were placed in investments. Now that loan growth has consistently exceeded share growth, credit unions are liquidating the investments to make loans. For all

years, liquid assets (cash and investments with maturities less than 1 year) remained relatively constant at about 23% of assets.

At the end of 1997, cash and short-term investments made up about 20% of total assets, allowing credit unions ample liquidity to meet daily cash needs.

One area of asset/liability management which calls for notice is “off balance sheet” or “unused” commitments, including unused credit card limits and home equity lines of credit. During 1997, total unused commitments increased $4.8 billion (8.7%) and now total nearly $60 billion. Increased credit card lines of credit accounted for $3 billion or 62% of the increase. Credit union management should ensure that unused commitments are addressed in funds management plans.