NCUA LETTER TO CREDIT UNIONS

NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA

DATE: **May 2000** **LETTER NO.: 00-CU-03**

TO: **Federally Insured Credit Unions**

SUBJ: **1999 Credit Union Financial Trends Report**

DEAR BOARD OF DIRECTORS:

Enclosed is a report highlighting credit union financial trends for 1999. The analysis is based on data compiled from the yearend 1999 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.

Sincerely,

_________/s/___________________________________
Norman E. D'Amours
Chairman
National Credit Union Administration Board

Enclosure

FINANCIAL TRENDS IN FEDERALLY INSURED CREDIT UNIONS

January 1, 1999 to December 31, 1999

HIGHLIGHTS

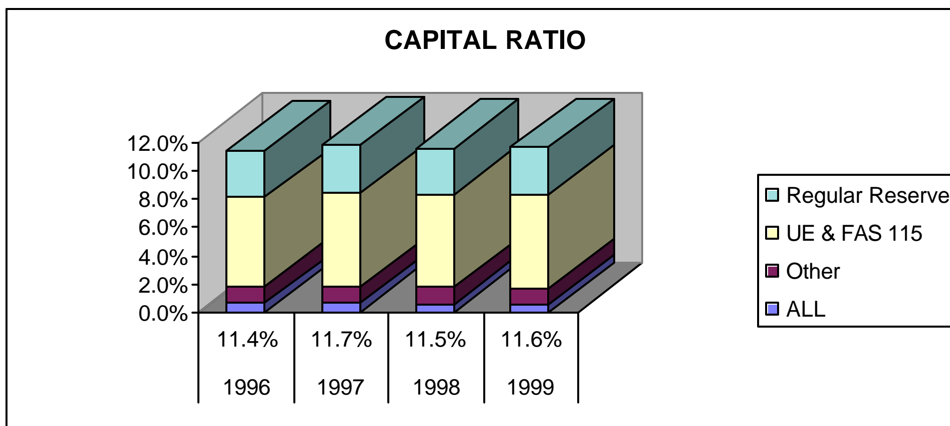
This report summarizes the trends of all federally insured credit unions that reported as of December 31, 1999. The trends discussed for all federally insured credit unions do not necessarily reflect the trends in smaller credit unions.

- **Assets** increased $22.7 billion or 5.8%.
- **Capital increased, at a faster rate,** 6.5% ($2.9 billion increase), and the capital to assets ratio increased to 11.6%.
- **Loans** increased $25.8 billion, or 10.5%.
- **Shares** increased $16.9 billion or 5.0%. The loan to share ratio increased to 76.1%.
- **Cash, cash equivalents, plus short-term investments (less than 1 year)** decreased $12.9 billion or 14.9%.
- **Long-term investments (over 1 year)** increased $8.8 billion or 20.0%.
- **Profitability** remained stable with a 0.93% return on average assets ratio.
- **Delinquent** loans as a percentage of total loans decreased from the yearend 1998 level of 0.88% to 0.75%.

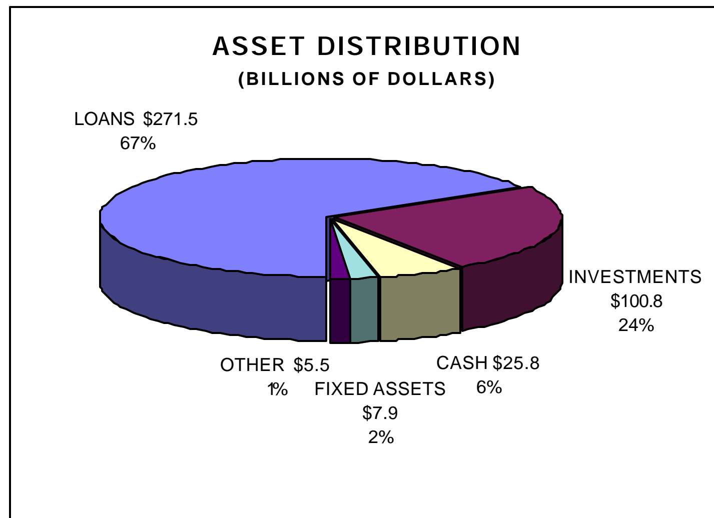
CAPITAL

Total capital increased $2.9 billion or 6.5% during 1999, compared to an 8.8% increase in 1998. The capital to total assets ratio increased from 11.5% at the end of 1998 to 11.6% at the end of 1999, as capital growth outpaced asset growth.

The net capital to total assets ratio, which measures capital after estimated losses, also increased from 10.9% at the end of 1998 to 11.0% at the end of 1999.



ASSET QUALITY



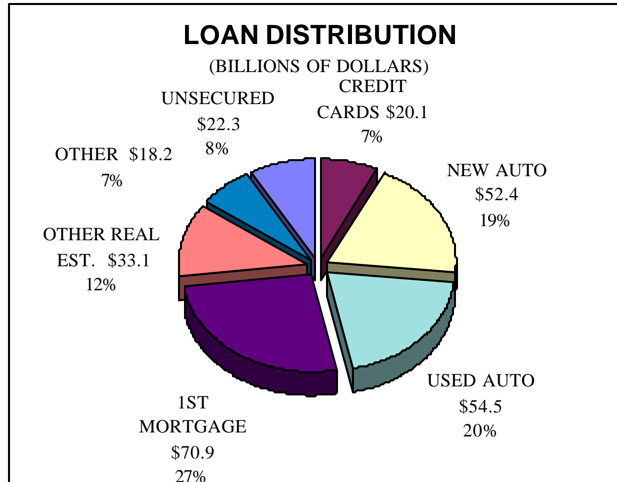
LOAN TRENDS: Total loans increased $25.8 billion or 10.5% during 1999. All loan categories increased, except for unsecured loans (excluding credit cards and lines of credit). Growth in the various categories was as follows:

- First mortgage real estate loans increased $9.5 billion (15.5% increase);
- Other real estate loans increased $3.6 billion (12.4% increase);
- Used auto loans increased $6.1 billion (12.5% increase);
- New auto loans increased $4.6 billion (9.6% increase);
- Other loans (including leases) increased $1.5 billion (9.3% increase); and
- Credit card loans increase $0.8 billion (3.9% increase).

Unsecured loans (excluding credit cards and other lines of credit) declined $0.3 billion (1.6%).

First mortgage real estate loans ($70.9 billion) account for 26.1% of all loans, with $51.8 billion or 73% reported to be fixed rate. Federally insured credit unions granted $21.4 billion in fixed rate and $6.1 billion in adjustable rate first mortgage real estate loans in 1999. Credit unions also report $7.1 billion of first mortgages sold in 1999 (includes both fixed and adjustable rates).

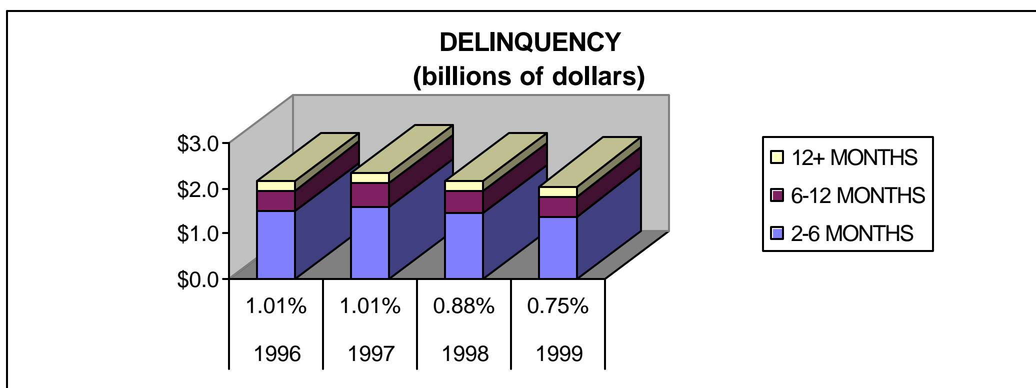
Loan growth of 10.5% was the strongest since 1996. Shares grew at a much slower rate, causing the loan to share ratio to increase to 76.1%.

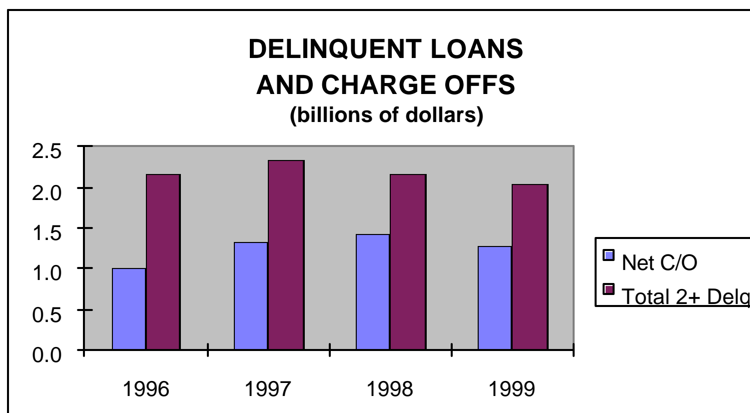


DELINQUENCY TRENDS: Delinquent loans decreased $115 million or 5.3%, and the delinquent loans to total loans ratio decreased from 0.88% at the end of 1998 to 0.75% at the end of 1999. This is the lowest delinquency ratio ever noted in federally insured credit unions.

The net charged off loans to average loans ratio also declined from 0.59% to 0.49% during 1999. Loan dollars charged off decreased $132 million or 8% compared to 1998, and recoveries on charged off loans increased 5.3%. The net charge off ratio declined because loans increased and net charge offs decreased.

Federally insured credit unions reported fewer members filing bankruptcy in 1999. The number of members filing bankruptcy decreased 12% to 214,700 (0.3% of all members), with nearly $1 billion in outstanding loans subject to bankruptcy and another $684 million charged off in 1999 as a result of bankruptcies.





INVESTMENT TRENDS: The December 1999 call report included major changes to the classification of investments. To the extent possible, the changes have been considered in the comparisons and conclusions in this trend report. Where specific data is not available for comparison, similar areas are reviewed for trending purposes. The changes included moving the NCUSIF deposit from investments to other assets, and moving certain investments to *cash equivalents*.[1]

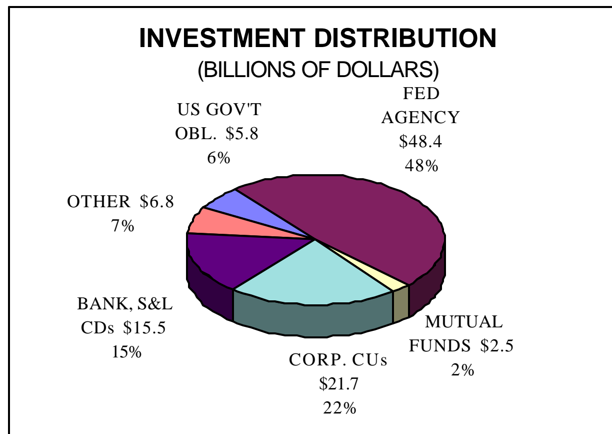
Total investments decreased $20.9 billion (17.2%). The decrease is likely the result of multiple factors. First, investments likely decreased at the end of 1999 as credit unions planned additional liquidity for the century date change. Second, the substantial loan growth in 1999 well outpaced share growth, necessitating liquidation of investments to fund new loans.

Finally, certain short-term investments were reclassified to the *cash equivalents* category on the call report. Cash and cash equivalents increased $16.9 billion (190.6%), which represents 81% of the corresponding decrease in total investments. Although cash and cash equivalents increased, the combined categories of cash plus investments with maturities of less than one year decreased $12.9 billion or 14.9% from December 1998 to December 1999.

Conversely, investments with maturities greater than a year increased $8.9 billion (20.0%).

The investment mix also changed, primarily because of the cash equivalent reclassification. The largest decline ($16.5 billion or 45.6%) appears in deposits in corporate credit unions (other than membership capital and paid in capital), all of which is likely now reported as cash equivalents. Other declines are noted in U.S. Government Obligations ($3.3 billion or 36.3%) and certificates of deposit in banks ($5.7 billion or 27.0%). The only investment category reporting a significant increase is federal agency securities, which increased $4.4 billion or 10% in 1999.

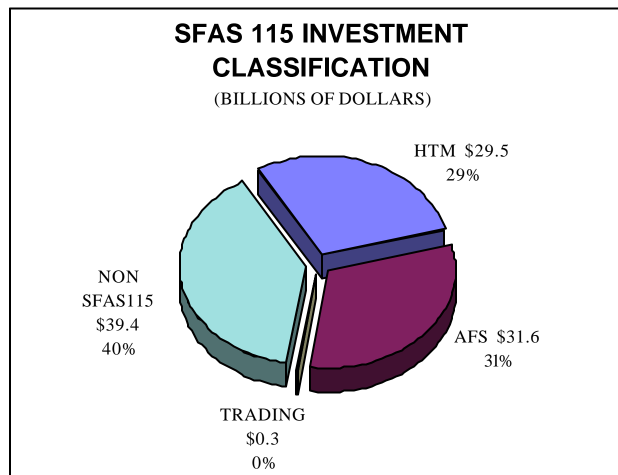
[1] *Cash equivalents* are defined as short-term, highly liquid investments with original maturities of three months or less. Examples include overnight accounts at a bank or corporate credit union, Fed Funds sold, and checking accounts.



The call report category changes resulted in an apparent maturity restructuring within the investment portfolio, because most of the shift from investments to cash equivalents came from the non-SFAS 115 category. Non-SFAS 115 investments declined from $61.1 billion to $39.4 billion ($21.7 billion or 35.5% decline).

Held to maturity investments decreased $150 million in total, with a $3.3 billion decrease in maturities less than a year and offsetting increases in maturities greater than one year. *Available for sale* investments increased nearly $800 million in total, with a $2.7 billion decrease in those investments with maturities less than one year, and offsetting increases in investments with maturities greater than a year. Trading securities increased $126 million, or 66.1% for the year.

At the end of 1998, *held to maturity* and *available for sale* investments made up 49% of the investment portfolio (24% and 25%, respectively), while *non-SFAS 115* investments accounted for 51% of the portfolio (a small amount was classified as trading). As noted on the graph below, *non-SFAS 115* investments now account for 40% of the portfolio, with the remainder nearly equally split between *held to maturity* and *available for sale* investments.



Investments in the less than one year maturity category decreased consistent with the reclassification of shorter-term investments to cash equivalents on the call report. Relatively small dollar increases in investments with maturities greater than one year, coupled with decreased total investments, cause the apparent shift in the portfolio maturity structure.

Investment Maturity or Repricing Interval	% of Total Investments Dec. 1998	% of Total Investments Dec. 1999
Less than 1 year	63.7%	47.3%
1 to 3 years	21.8%	30.9%
3 to 10 years	12.8%	19.4%
Greater than 10 yrs	1.7%	2.4%

EARNINGS

Although most earnings ratios declined in 1999, the return on average assets ratio remained steady at 0.93% of average assets. Gross income to average assets (yield) continues to decline, despite strong loan growth. The decline can be attributed to lower yields on investments and lower rates on mortgage loans (which account for most of the loan growth in 1999).

The decline in yield was offset by declines in the cost of funds and provision for loan loss expense (see table).

Ratio	As of 12/98	As of 12/99
Gross Income	8.23%	7.98%
Cost of Funds	3.57%	3.37%
Operating Expenses	3.31%	3.34%
PLL	0.42%	0.34%
ROA	0.93%	0.93%

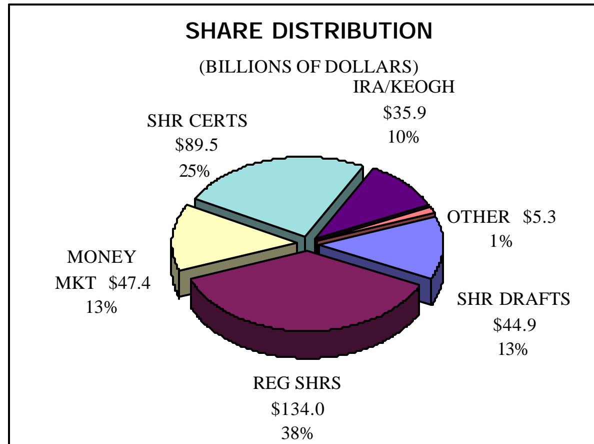
ASSET/LIABILITY MANAGEMENT

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 24.9% of total assets at the end of 1999, compared to 22.4% at the end of 1998. This increase is primarily the result of growth in real estate loans discussed earlier.

SHARE TRENDS: Total shares increased $16.9 billion or 5.0% in 1999, compared to 10.7% in 1998. Share dollars in all categories increased in 1999, as follows:

- Share drafts -- ↑ $2.3 billion, 5.4%;
- Regular shares -- ↑ $3.4 billion, 2.6%;
- Money market shares -- ↑ $6.6 billion, 16.3%;
- Share certificates -- ↑ $3.6 billion, 4.1%;
- IRA/Keogh accounts -- ↑ $0.8 billion, 2.4%;
- Other shares -- ↑ $0.2 billion, 5.1%; and

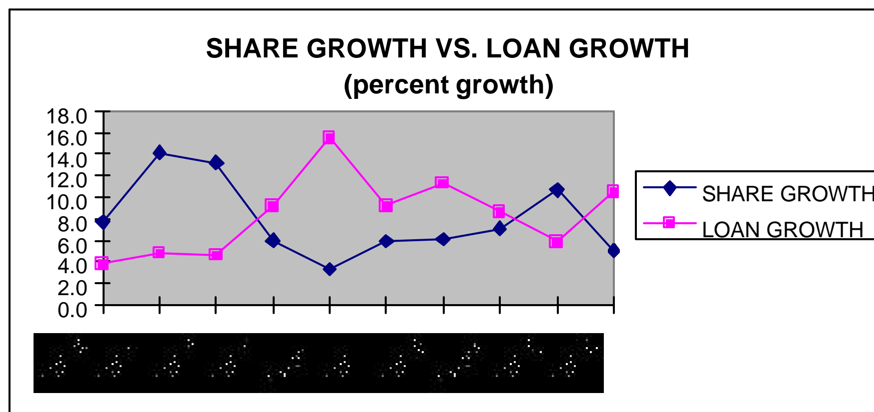
• Nonmember deposits -- ↑ $19 million, 2.1%.



Share growth during 1999 was approximately half the level noted in 1998. Growth was fairly evenly distributed across the maturity categories, resulting in a stable maturity structure over the past two years, as noted in the table to the right:

Share Maturity or Repricing Interval	% of Total Shares Dec. 1998	% of Total Shares Dec. 1999
Less than 1 year	90.2%	90.7%
1 to 3 years	7.9%	7.6%
3 or more years	1.9%	1.7%

OVERALL LIQUIDITY TRENDS: A five-year trend of the rate of loan growth exceeding the rate of share growth reversed in 1998 and then recovered in 1999. The trends of loan growth versus share growth over the past ten years are illustrated in the following graph.

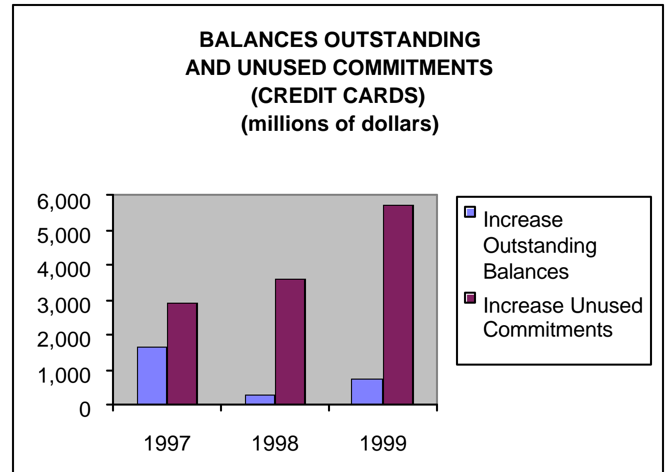


Since the beginning of 1990, share growth has exceeded loan growth by $40.7 billion in total. During the periods when share growth exceeds loan growth, excess funds are placed in investments. For all years before 1999, liquid assets (cash and investments with maturities less than 1 year) remained relatively constant at about 23% of assets. However, liquid investments declined in 1999 to 17.9%, apparently because of the strong loan growth.

Total unused commitments equaled $75.2 billion, up $7.3 billion (10.8%) in 1999. The increase in unused commitments was primarily in home equity lines of credit (HELOCs) and unused credit card lines. Unused HELOCs increased 5.9% ($763 million) in 1999, compared to 1998's growth of 23.7% ($2.5 billion) in HELOCs.

Unused credit card lines equaled $46.2 billion, increasing $5.8 billion or 14.2%. Unused credit card lines account for 61.4% of all unused commitments, and the increase in this type of commitment accounted for nearly 80% of the growth in commitments.

Growth in unused credit card commitments is well outpacing growth in credit card loans outstanding. Note the following comparison of growth from 1997 through 1999:



In light of the need for prudent management of liquidity and contingency funding arrangements, credit union managers are encouraged to consider the funding implications posed by unused commitments when evaluating their overall funds management strategies.