NATIONAL CREDIT UNION ADMINISTRATION

1775 Duke Street, Alexandria, VA 22314

DATE: August 24, 1998 **LETTER NO.: 98-CU-17**

DEAR BOARD OF DIRECTORS:

Enclosed is a report highlighting credit union financial trends for the first half of 1998. The analysis is based on data compiled from the midyear 1998 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, 1998 to June 30, 1998

HIGHLIGHTS

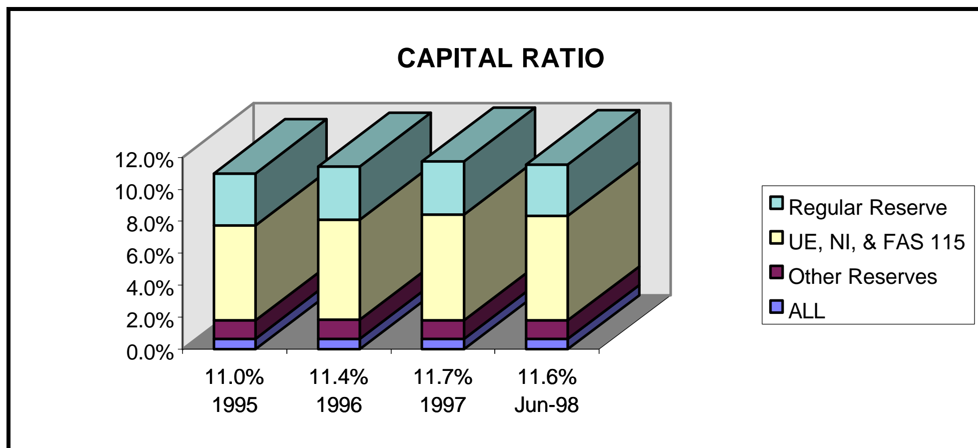
This report summarizes the trends of all federally insured credit unions which reported as of June 30, 1998. As noted below, key financial indicators are strong in all areas.

- **Assets** increased $20.4 billion or 5.8%.
- **Capital also increased, but at a slower rate than assets,** causing the capital to assets ratio to drop slightly from 11.7% to 11.6%.
- **Loans** increased $5.5 billion, or 2.4%, accounting for 27% of the asset growth.
- **Shares** increased $17.6 billion or 5.7%. Because shares grew at a faster rate than loans, the loan to share ratio declined to 73.2%, compared to 75.6% at the end of 1997.
- **Investments** increased $14.1 billion or 13.7%, accounting for 69% of asset growth.
- **Profitability** continued stable with a 1.0% return on average assets ratio.
- **Delinquent** loans as a percentage of total loans declined from the yearend 1997 level of 1.0% to 0.9%, while **net charge offs** remained stable at 0.6% of average loans.

CAPITAL

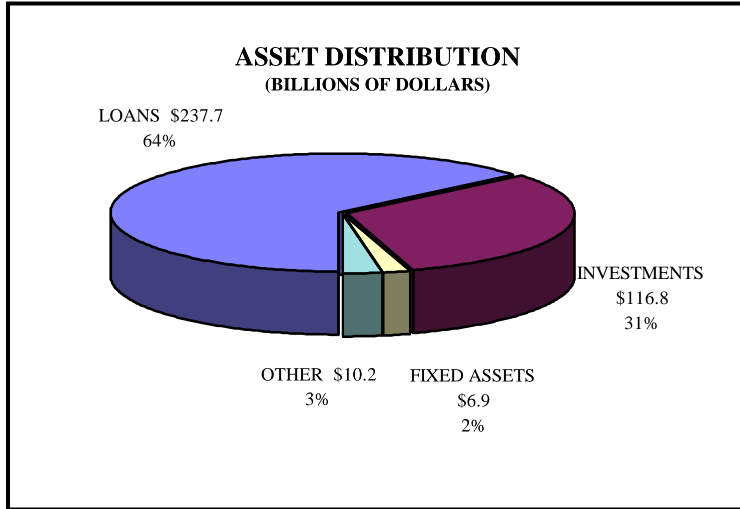
Total capital increased $1.7 billion or 4.3% in the first half of 1998, compared to a 5.1% increase during the same period last year. The capital to total assets ratio decreased slightly from 11.7% at the end of 1997 to 11.6% as of June 30, 1998.

The net capital to total assets ratio, which measures capital after estimated losses, also decreased from 11.1% to 10.9%. The decline in the capital ratios is due to assets increasing at a faster rate than capital increased.

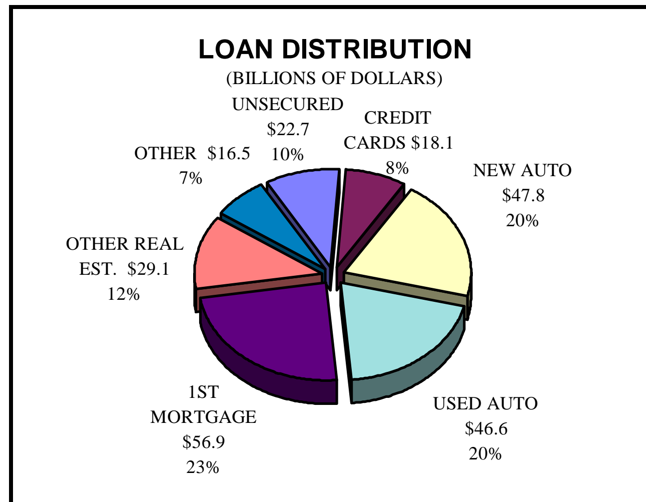


Unless otherwise indicated, all percent changes are year-to-date, and are not annualized.

ASSET QUALITY

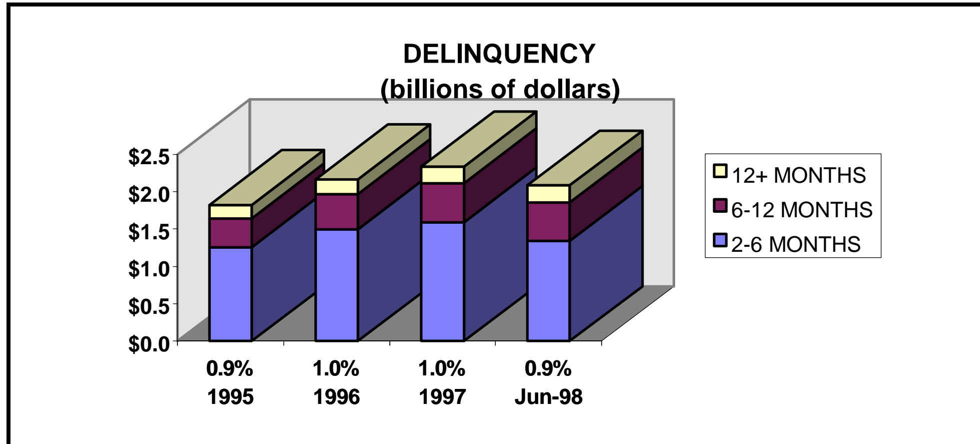


LOAN TRENDS: Total loans increased $5.5 billion (2.4%) during the first half of 1998. First mortgage real estate loans and used auto loans made up most of the growth, with $5.0 billion (9.7% increase) and $3.1 billion (7.0% increase), respectively. Gains in those two categories were somewhat offset by decreases in new auto loans ($1.6 billion or 3.2%), credit card loans ($0.9 billion or 4.7%), and other unsecured loans ($0.8 billion or 3.6%).

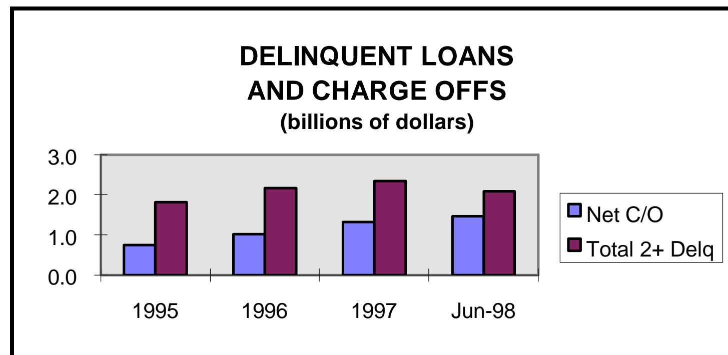


The rate of loan growth during the first half of 1998 was 2.4%, compared to 3.9% for the same period in 1997, and 4.6% in 1996. Historically, loan growth follows a cyclical pattern of low growth in the first half of the year and higher growth in the second half of the year. Because of this, loan growth during the first half of the year tends to be less than share growth, causing the loan to share ratio to decline somewhat in the first six months of the year.

DELINQUENCY TRENDS: Delinquent loan dollars declined 10.9% during the first half of the year, causing the delinquency ratio to decline from 1.0% at the end of 1997 to 0.9% as of June 30. This is the lowest level of delinquent loan dollars since mid 1996.



Net charged off loan dollars again increased during the first half of the year. Compared to the first half of 1997, net charged off loan dollars increased 19.0%. This increase in charge offs explains part of the decline in delinquent loan dollars. Additionally, recoveries on charged off loans increased 8.4% compared to the same period last year. However, the increased level of recoveries was not sufficient to match the increase in charged off loan dollars. Although net charge offs increased, the net charge off ratio remains unchanged because total loans also increased.

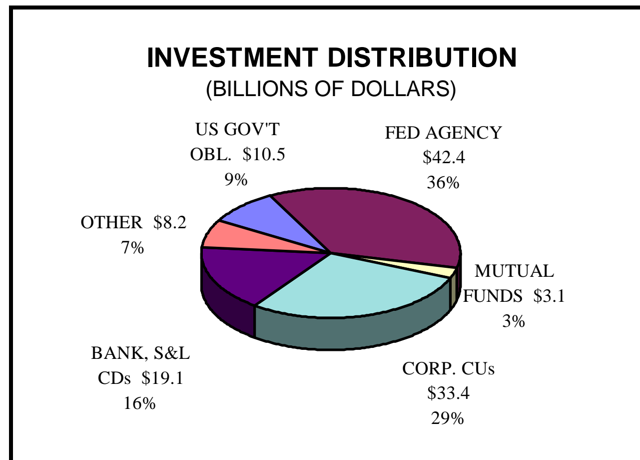


Bankruptcies continue to increase. Credit unions reported nearly $800,000 in loans subject to bankruptcies as of midyear, which represents a slight (1.4%) decrease from the amount reported for the first half of 1997. When annualized, however, this

amount represents an increase of more than 40% over the total for all of 1997.

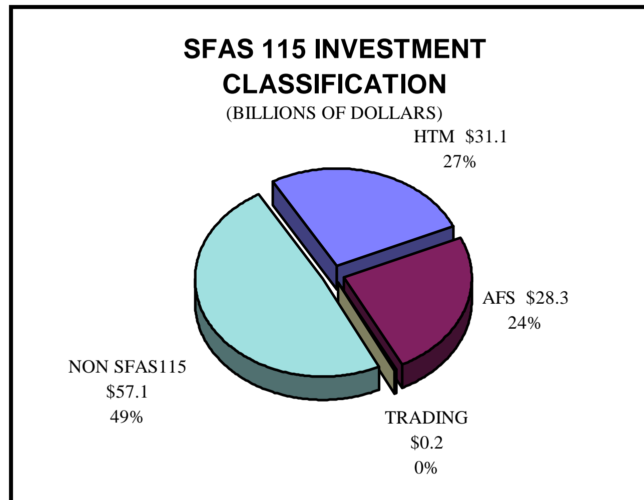
INVESTMENT TRENDS: Investments increased $14.1 billion (13.7%) in the first half of 1998, and represent 31.4% of total assets. The investment increase is consistent with the low loan growth and high share growth discussed earlier, in that excess share growth is placed into investments.

The investment category noting the largest dollar growth is deposits in corporate credit unions, which increased more than $7.3 billion or 28.3%. Significant growth is also noted in federal agency securities ($3.1 billion increase of 7.9%), and deposits in banks ($2.6 billion or 15.8%). Investment in U.S. government obligations was the only investment type which declined ($1.1 billion or 9.7%).



During the first half of 1998, most of the investment growth (65%) was placed in short-term (less than 1 year) instruments. This is reasonable given the pattern of high share growth and low loan growth during the first half of the year which tends to reverse in the second half.

The investment portfolio continues to shift from *held to maturity* and *available for sale* investments into *non-SFAS 115* investments. At the end of 1997, *held to maturity* and *available for sale* investments made up 54.8% of the investment portfolio (30.1% and 24.7%, respectively), while *non-SFAS 115* investments accounted for 44.9% of the portfolio (the remainder was classified as trading). As noted on the graph below, *non-SFAS 115* investments now account for 48.9% of the portfolio. This is due in part to an increase in investments in corporate credit unions.



The table to the right compares the changes in the maturity structure of the investment portfolio in the first half of 1998:

Investment Maturity or Repricing Interval	% of Total Investments Dec. 1997	% of Total Investments June 1998
Less than 1 year	60.2%	60.9%
1 to 3 years	25.2%	23.9%
3 to 10 years	10.1%	11.3%
Greater than 10 yrs	4.5%	3.9%

EARNINGS

The earnings ratios are substantially unchanged from yearend 1997. Cost of funds, operating expenses, and Provision for Loan Loss expense ratios all remained the same as those noted for 1997. The only ratio that changed is the gross income to average assets ratio, which declined from 8.4% to 8.2%. This decline is explained by the fact that a larger portion of assets are comprised of investments which produce a lower yield than do loans. The gross income ratio is expected to increase in the second half of the year as loans increase.

Ratio	As of 12/97	As of 06/98
Gross Income	8.4%	8.2%
Cost of Funds	3.6%	3.6%
Operating Expenses	3.3%	3.3%
PLL	0.4%	0.4%
ROA	1.0%	1.0%

ASSET/LIABILITY MANAGEMENT

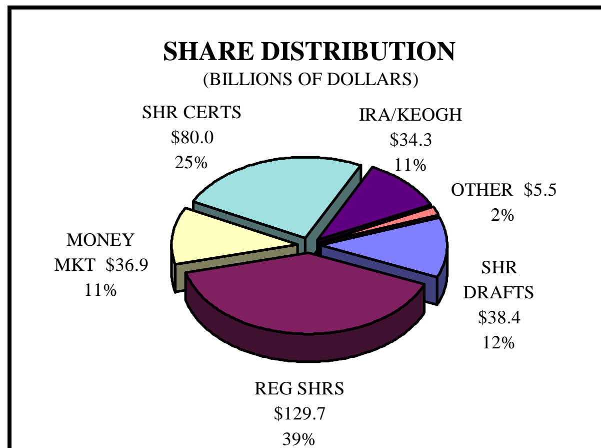
LONG TERM ASSET TRENDS: Long term assets as a percentage of total assets increased slightly since yearend. These assets, which have maturities or repricing intervals greater than 3 years, equaled 21.2% of total assets, compared to 20.2% at the end of 1997. This increase is primarily the result of growth in first mortgage real estate loans discussed earlier.

SHARE TRENDS: Total shares increased $17.6 billion or 5.7% during the first half of

1998, compared to $16.1 billion or 5.6% during the same period in 1997.
Growth rates among the various share categories are comparable with those noted during the first half of 1997. The categories noting the largest dollar increases are regular shares ($6.3 billion, 5.1%), share certificates ($3.9 billion, 5.1%), and money market shares ($3.7 billion, 11.1%). The "other shares" category shows the highest relative increase with 33.5% growth or $1.2 billion.

Growth rates for the first half of 1998 in the various share categories are as follows:

- Share drafts -- ↑ $2.5 billion, 7.0%;
- Regular shares -- ↑ $6.3 billion, 5.1%;
- Money market shares -- ↑ $3.7 billion, 11.1%;
- Share certificates -- ↑ $3.9 billion, 5.1%;
- IRA/Keogh accounts -- ↑ $7.8 million, less than 1%
- Other shares -- ↑ $1.2 billion, 33.5%; and
- Nonmember deposits -- ↑ $23.5 million, 3.1%.



Share growth during the first half of 1998 is concentrated in the "less than 1 year" maturity category, with $16.1 billion or 91% of total share growth noted in this category.

Share Maturity or Repricing Interval	% of Total Shares Dec. 1997	% of Total Shares June 1998
Less than 1 year	89.9%	90.0%
1 to 3 years	8.3%	8.1%
3 or more years	1.8%	1.9%

OVERALL LIQUIDITY TRENDS: Because share growth exceeded loan growth in the first half of 1998, credit unions had excess liquidity for investing. As discussed earlier, the excess liquidity was invested primarily for the short-term (less than 1 year) in corporate credit unions and other liquid instruments. This strategy should place credit unions in a good position to fund the loan growth historically seen during the last half of the year.