NCUA LETTER TO CREDIT UNIONS

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

DATE: October 1999 **LETTER NO.:** 99-CU-15

TO: All Federally Insured Credit Unions

SUBJ: Financial Trends in Federally Insured Credit Unions

DEAR BOARD OF DIRECTORS:

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

For the National Credit Union Administration Board,

/s/

NORMAN E. D'AMOURS
Chairman

Enclosure

FINANCIAL TRENDS IN FEDERALLY INSURED CREDIT UNIONS

January 1, 1999 to June 30, 1999

HIGHLIGHTS

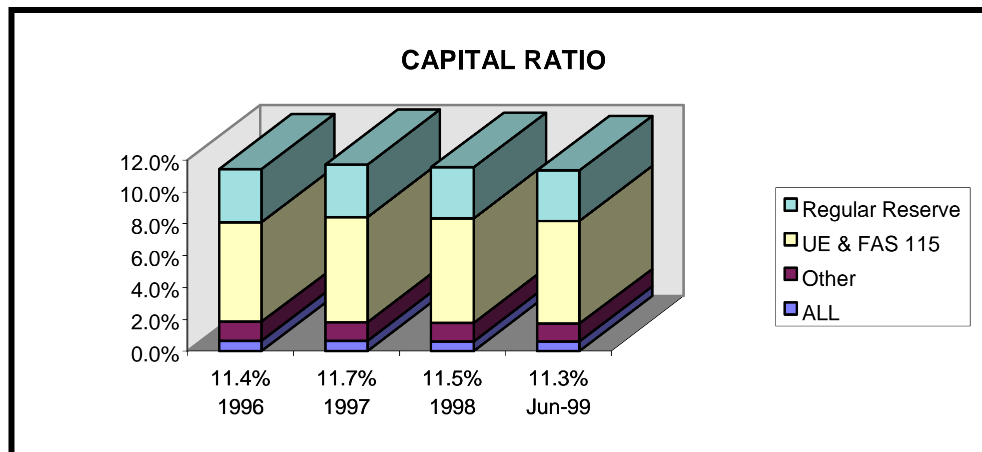
This report summarizes the trends of all federally insured credit unions which reported as of June 30, 1999. As noted below, key financial indicators are strong in all areas.

- **Assets** increased $18.3 billion or 4.7%. Federally insured credit unions now hold over $407 billion in total assets.
- **Capital also increased, but at a slower rate than assets,** causing the capital to assets ratio to drop slightly from 11.5% to 11.3%.
- **Loans** increased $9.2 billion, or 3.8%, accounting for 50% of the asset growth.
- **Shares** increased $16.6 billion or 4.9%. Because shares grew at a slightly faster rate than loans, the loan to share ratio declined to 71.5%, compared to 72.3% at the end of 1998.
- **Investments** increased $8.5 billion or 6.8%.
- **Profitability** is relatively stable with a 0.9% return on average assets ratio.
- **Delinquent** loans as a percentage of total loans declined from the yearend 1998 level of 0.9% to 0.8%, while **net charge offs** declined from 0.6% to 0.5% of average loans.

CAPITAL

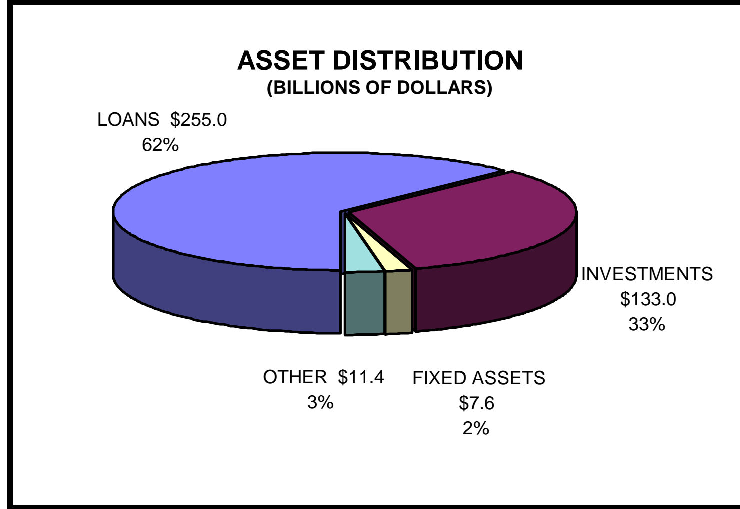
Total capital increased $1.3 billion or 2.9% in the first half of 1999, compared to a 4.3% increase during the same period last year. The capital to total assets ratio decreased from 11.5% at the end of 1998 to 11.3% as of June 30, 1999.

The net capital to total assets ratio, which measures capital after estimated losses, also decreased from 10.9% to 10.7%. 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



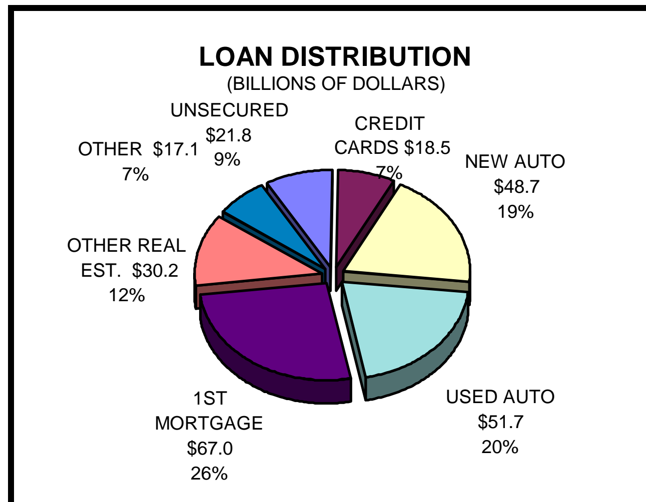
LOAN TRENDS: Total loans increased $9.2 billion (3.8%) during the first half of 1999, which is nearly twice the dollar growth noted for the same period in 1998. Two loan categories again account for most of the increase:

- First mortgage real estate loans increased $5.7 billion (9.3% increase);
- Used auto loans increased $3.2 billion (6.7% increase).

Gains in those two categories were somewhat offset by decreases in credit card loans ($0.9 billion or 4.6%) and other unsecured loans ($0.8 billion or 3.6%). Similar trends were noted for the same period last year.

First mortgage real estate loans ($67.0 billion) account for over 26% of all loans, with $49.3 billion or nearly 74% reported to be fixed rate. Fixed rate first mortgage real estate loans increased 12.3% during the first half of 1999.

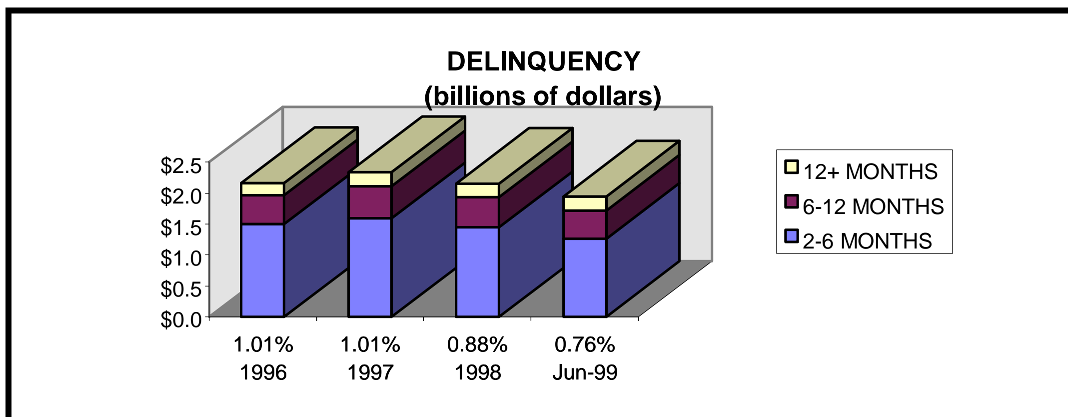
Federally insured credit unions granted $13.1 billion in fixed rate first mortgage real estate loans and $2.9 billion in adjustable rate first mortgage real estate loans during the first half of 1999. Credit unions also reported $4.4 billion (27% of originations) in first mortgages sold onto the secondary market during the first half of 1999 (includes both fixed and adjustable rate). This is slightly less than the $4.8 billion (32% of originations) reported for the same period last year.

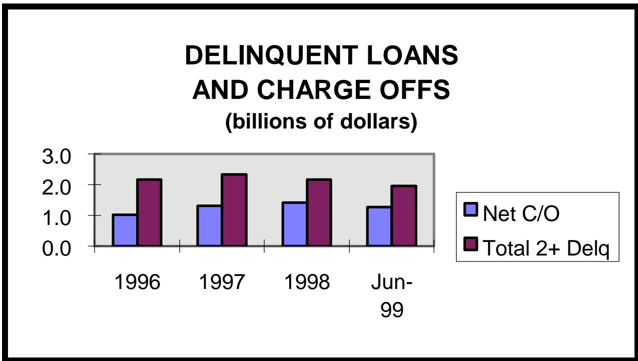


DELINQUENCY TRENDS: Delinquent loan dollars declined 9.9% during the first half of the year, causing the delinquency ratio to decline from 0.9% at the end of 1998 to 0.8% as of June 30. This is the lowest level of delinquent loan dollars since mid 1996.

Net charged off loan dollars decreased during the first half of the year. Compared to the first half of 1998, net charged off loan dollars decreased 9.3%. Additionally, recoveries on charged off loans increased 10.0% compared to the same period last year. A decrease in charged off loan dollars, increase in recoveries, and increase in total loans produced a decline in the net charge off to average loans ratio to 0.5%.

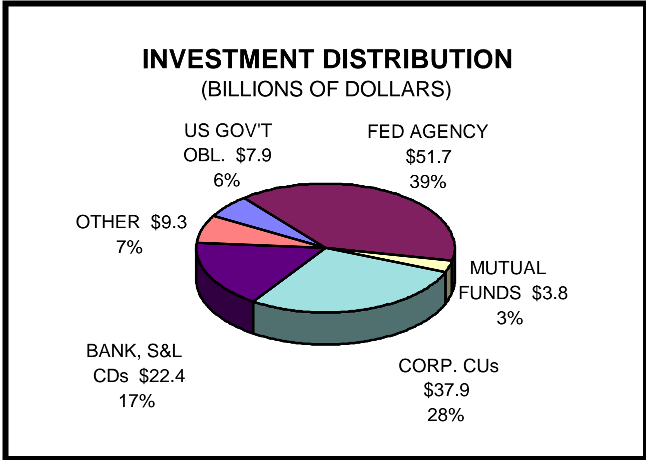
Bankruptcies declined somewhat during the first half of 1999. Credit unions reported just over $600 million in loans subject to bankruptcies as of midyear, which represents a 23% decrease from the amount reported for the first half of 1998. Loans charged off due to bankruptcy also declined 9.2% compared to the same period last year. Nearly 116,000 members (0.2% of all members) were reported to have filed bankruptcy during the first half of 1999, the lowest amount reported since 1996.



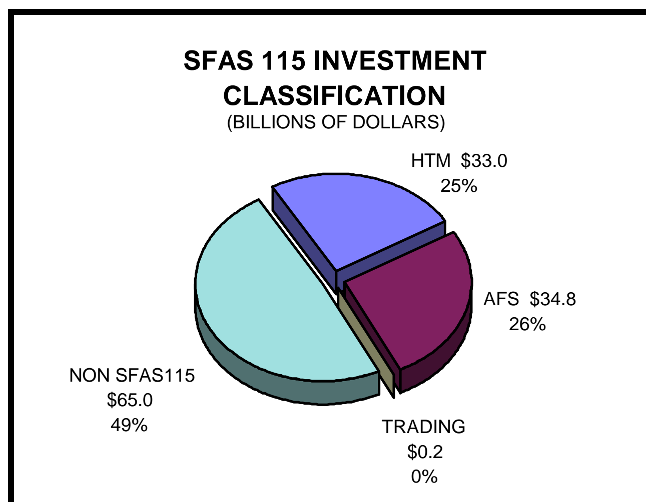


INVESTMENT TRENDS: Investments increased $8.5 billion (6.8%) in the first half of 1999, and represent 32.7% of total assets. The investment increase is consistent with the low loan growth and high share growth discussed earlier, in that excess share growth is placed into investments.

The investment category noting the largest dollar growth is federal agency securities, which increased more than $7.7 billion or 17.6%. Nominal growth was reported for mutual fund investments ($245 million or 6.8%) and deposits in banks ($1.1 billion or 5.3%). Investments in U.S. government obligations was the only investment type which declined ($1.3 billion or 14.1%).



During the first half of 1999, most investment growth occurred in *available for sale* investments ($14 billion or 13%). Short-term (less than 1 year) investments declined 2.6%. Conversely, during the same period last year, most investment growth (65% of all investment growth) was noted in the less than 1 year maturity category. At mid-year 1998, *held to maturity* and *available for sale* investments made up 50.9% of the investment portfolio (26.6% and 24.3%, respectively), while *non-SFAS 115* investments accounted for 48.9% of the portfolio (the remainder was classified as trading). As noted on the graph below, *non-SFAS 115* investments now account for 48.8% of the portfolio, virtually unchanged from the same period in 1998.



The table to the right compares the changes in the maturity structure of the investment portfolio in the first half of 1999. The table illustrates a shift from the less than 1 year category to the 3 to 10 year maturity category. Such a shift is consistent with the large increase in investments in federal agency securities previously discussed.

Investment Maturity or Repricing Interval	% of Total Investments June 1998	% of Total Investments June 1999
Less than 1 year	60.9%	56.7%
1 to 3 years	23.9%	23.3%
3 to 10 years	11.3%	15.9%
Greater than 10 yrs	3.9%	4.1%

EARNINGS

All the earnings ratios note declines compared to the first half of 1998. The gross income to average assets ratio declined from 8.22% to 7.81%. This decline is likely due primarily to lower market interest rates on both loans and investments. Reduced cost of funds, operating expense, and Provision for Loan Losses ratios compensated for most of the decline in the gross income ratio.

The following table compares the earnings ratios for the first half of 1998 to those for the first half of 1999:

Ratio	As of 06/98	As of 06/99
Gross Income	8.22%	7.81%
Cost of Funds	3.57%	3.33%
Operating Expenses	3.29%	3.25%
PLL	0.42%	0.35%
ROA	0.95%	0.90%

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 24.3% of total assets, compared to 21.2% as of June 30, 1998. This increase is primarily the result of growth in first mortgage real estate loans and investments with maturities greater than 3 years.

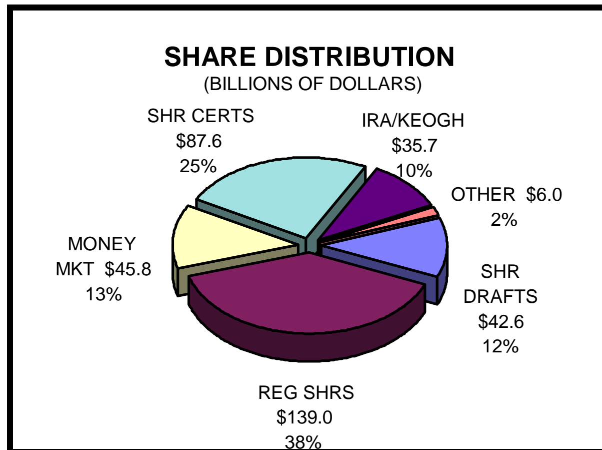
SHARE TRENDS: Total shares increased $16.6 billion or 4.9% during the first half of 1999, compared to $17.6 billion or 5.7% during the same period in 1998.

Growth rates among the various share categories vary greatly from those noted during the first half of 1998. The categories noting the largest dollar increases are regular shares ($8.3 billion, 6.4%) and money market shares ($5.0 billion, 12.4%). Half of all share growth ($16.6 billion) was in regular shares ($8.3 billion).

Growth rates for the first half of 1999 in the various share categories are as follows:

- Share drafts -- ↑ $8 million, less than 1%;
- Regular shares -- ↑ $8.3 billion, 6.4% (this represents the largest dollar increase);
- Money market shares -- ↑ $5.0 billion, 12.4% (this represents the largest percentage increase in a major share category);
- Share certificates -- ↑ $1.7 billion, 1.9%;
- IRA/Keogh accounts -- ↑ $696 million, 2%;
- Other shares -- ↑ $898 million, 21.3%; and
- Nonmember deposits -- ↓ $27 million, 3.1%.

Growth in regular shares was stronger during the first half of 1999 ($8.3 billion) than for all of 1998 ($7.2 billion). Continued growth in liquid accounts may indicate members' uncertainty about the market, or it may indicate that market rates generally favor shorter terms.



All share growth during the first half of 1999 occurred in the "less than 1 year" maturity category.

Share Maturity or Repricing Interval	% of Total Shares June 1998	% of Total Shares June 1999
Less than 1 year	90.0%	91.0%
1 to 3 years	8.1%	7.2%
3 or more years	1.9%	1.8%

OVERALL LIQUIDITY TRENDS: Because share growth exceeded loan growth in the first half of 1999, credit unions had excess liquidity for investing. As discussed earlier, the excess liquidity was invested primarily in federal agency securities. With respect to asset liability management, depending on the characteristics of the security, some agency securities may possess greater market risk (interest rate and liquidity risk) than other investments (such as U.S. Treasury securities or fixed rate bullet certificates of deposit) with similar maturities.

Total unused commitments equaled $73.0 billion, up $9.9 billion or 15.7% in the last year. Unused credit card lines equaled $45.4 billion (62% of the total), noting an increase of $6.7 billion (17.3%).

Increasing contingencies, coupled with growth in longer term investments and real estate loans, require prudent funds management strategies. Credit union management is encouraged to consider all these areas in the overall funds management plan.