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<u>Bob Burrell:</u> Bob Burrell is the Executive Vice President and Chief Investment Officer of Western Corporate Federal Credit Union (WesCorp) in San Dimas, California. Prior to joining WesCorp in 1997, Mr. Burrell was Senior Vice President and group manager of capital markets and portfolio management at Boatmen's Bancshares, Inc., in St. Louis. He also serves on the board of Corporate Exchange, LLC. Mr. Burrell was educated in England where he attended the University of Leeds and earned a Bachelor's degree in Electrical Engineering.

<u>David Colby:</u> Dave Colby is the Assistant Vice President & Corporate Economist for the CUNA Mutual Group in Madison, Wisconsin. Mr. Colby joined CUNA Mutual in 1977 as a Corporate Research Specialist and has progressed through the organization holding various corporate, operational and financial planning positions. Mr. Colby is a graduate of the University of Wisconsin - LaCrosse where he received his Bachelor of Science degree in Economics. He holds the designation of Fellow, Life Office Management Institute.

<u>David Dickens:</u> David Dickens joined U.S. Central Credit Union in Lenexa, Kansas as Senior Vice President, Asset/Liability Management in December 1997. Prior to joining U.S. Central, Mr. Dickens served in the same role at Corporate One Federal Credit Union in Columbus, Ohio. Mr. Dickens also previously served as Senior Vice President of Corporate Network Brokerage Services, Inc. (CNBS). Mr. Dickens earned a Bachelor's degree in Business Administration from the University of Missouri.

<u>Bruce Fox:</u> Bruce M. Fox is the Senior Vice President and Chief Investment Officer of Southwest Corporate Federal Credit Union. Mr. Fox joined Southwest in January 1991 as an investment adviser. Mr. Fox is a member of Southwest's asset-liability committee and chairman of the loan committee. Prior to that, he was an investment portfolio manager at Members Insurance Companies of the Texas Credit Union League. Mr. Fox has Bachelor and Master's degrees in Finance from East Texas State University.

<u>Scott Mainwaring:</u> Scott R. Mainwaring joined VyStar Credit Union in Jacksonville, Florida as the Executive Vice President & Chief Financial Officer in 1991. In addition, Mr. Mainwaring is the President of VyStar Financial Group, LLC, a wholly owned subsidiary of VyStar Credit Union, and is also a CPA. He worked for the public accounting firm of Coopers & Lybrand for five years before joining Vystar. Mr. Mainwaring graduated with a Bachelor's degree in Accounting from Furman University in Greenville, South Carolina.

<u>Brian McVeigh:</u> Brian McVeigh is the Senior Vice President and Chief Financial Officer for State Employees Credit Union (SECU) in Lansing, Michigan and has been there since 1995. Prior to joining SECU, Mr. McVeigh spent eight years with First of America Corporation and three years with Michigan National Corporation. Mr. McVeigh has spent the majority of his nineteen year career specializing in asset and liability management, investments, and accounting after earning a Bachelor's degree in Accounting from Michigan State University.

<u>Jeff Taylor:</u> Jeff Taylor joined NAFCU in 2000 as the Senior Staff Economist in the Research and Analysis Division. Prior to joining NAFCU, Mr. Taylor worked as a financial consultant and Senior Economist and Investment Strategist at Bear Stearns and NatWest Securities, and as a Senior Country Risk Analyst at the U.S. Export Import Bank. Mr. Taylor received a Master's Degree in International Economics from George Washington University and Bachelor's Degrees in Latin American political economy and Spanish from Denison University.

<u>Tun Wai:</u> Dr. Tun A. Wai is in his seventeenth year as NAFCU's Director of Research and Chief Economist in Arlington, Virginia. Prior to joining NAFCU, Dr. Wai held research positions with the World Bank, the Federal Reserve Board of Governors, and the Brookings Institution, an independent research group. Dr. Wai has a Bachelor of Science in Business Administration in Management and a Ph.D. in Economics from Georgetown University, as well as an M.B.A. in Finance from New York University.

Executive Summary

- Loan growth for all federally insured credit unions (FICUs) in 2002 was approximately 6.3 percent, the majority of the growth being in first mortgage loans, followed by used auto lending. Overall lending within Regions 1, 2, and 5 grew at even higher individual rates.
- Most credit unions have expectations of elevated new and used auto lending and unsecured lending for 2003. Several regions revealed substantial growth in new auto lending, albeit at a modest rate, in 2002, due to the erosion of market share resulting from the zero-percent financing incentives offered by automakers throughout last year.
- Continuing geopolitical uncertainty and weak fundamentals lead credit unions as a whole to believe that growth in shares will either be about the same in 2003 or increase even further. Only more of Region 3 credit unions at this time believe that the growth in shares will decline this year.
- Share growth for all FICUs was 10.8 percent in 2002, with growth in every region being concentrated in non-share certificates, particularly regular and money market shares. IRA accounts were also a noticeable safe haven for credit union members' principal last year.
- The average return on average assets (ROA) for all FICUs in 2002 was roughly 1.07 percent. With the exception of Region 3, most credit union management teams seem to believe that the prospects for earnings this year remain positive or about the same.
- Credit unions continue to have low investment returns while remaining very liquid (55 percent of loan portfolio investment has a maturity of less than one year). The average yield on investments last year was about 3.5 percent and is expected to fall further during 2003 as the yield curve remains positive.
- The majority of credit unions nationwide have stated that banks are their primary sources of competition for loans, followed closely by finance companies (Region 3). Banks, as well as other credit unions (Regions 3 and 5) and mutual funds (Region 2), were found to be the primary source of credit unions' competition for savings vehicles.
- Most credit unions in each of the NCUA regions, when asked about their members' general confidence/sentiment, believed that members had about the same outlook currently as they did last year. What appeared to be most on the minds of leadership were financially distressed state and local governments as well as the general economic uncertainty in their region.

NCUA Region One

NCUA Region 1 (Northeast) consists of six states[1]. At year end 2002, there were 1,235 credit unions in the region, with total assets of $64.9 billion and a total membership of 8.5 million.

Lending

Region 1's loan growth last year was 9.1 percent, compared to 6.3 percent for all federally insured credit unions (FICUs). Loan growth in 2002 was concentrated in real estate products, and to a lesser extent, used light vehicle products. The mortgage "refi" wave that swept the nation in 2002 was very evident in Region 1. Home equity loan demand grew at a brisk pace as well. Last year, new light vehicle lending continued to be constrained by the dealer and finance company incentives, while some credit unions experienced an elevated demand for member business loans. Expectations for loan demand in 2003 were very mixed. The weak economic and financial conditions, coupled with severe weather, have many credit unions in a cautionary mode. While 36 percent of the surveyed credit unions believe that loan growth in 2003 will be higher than it was last year, an equal number of credit unions believe that loan growth will be slower than in 2002. Expectations for 2003 real estate loan demand were largely positive, yet 57 percent of the survey respondents believe that new auto loan demand will remain depressed. The majority of the region's credit unions have expectations of elevated used auto and unsecured lending for this year.

Member Shares

Region 1's share growth was 13.2 percent in 2002, compared to 10.8 percent for all FICUs. Share growth last year was concentrated in non-share certificates, particularly regular and money market shares. In 2003, share growth in Region 1 is not expected to decline significantly until the geopolitical and economic uncertainties abate. Fifty percent of the surveyed credit unions believe that share growth will slow in 2003, while 29 percent feel that share growth will accelerate this year. The majority of the NAFCU-member credit unions expect that most of the growth in shares in 2003 will come in the form of share drafts, share certificates, and Individual Retirement Accounts (IRAs). For 2003, 36 percent of the credit unions believe that regular share and money market share growth will be lower than in 2002. Regarding liquidity, 57 percent of the region's credit unions expect that their deposit structure liquidity will be similar to their 2002 liquidity, with only 14 percent expecting a more liquid deposit structure this year.

Return on Average Assets (ROA), Spreads, and Asset Quality

Last year, the credit unions in Region 1 had an ROA of 1.06 percent compared to an ROA of 1.07 percent for all FICUs. A lower cost of funds, limiting expenses, and higher fee income allowed for solid earnings. In 2003, the prospects for earnings remain positive for many credit unions, with 46 percent of credit unions expecting an ROA in

[1] The six states are Connecticut, Maine, Massachusetts, New Hampshire, New York, Rhode Island and Vermont.

line with that of 2002. However, due to the economic uncertainty and the likelihood of rising interest rates later this year, 46 percent of the responding credit unions believe that their ROA will contract in 2003. The majority (nearly 70 percent) envision lower gross spreads this year, with the remaining 30 percent expecting similar spreads in 2003. The asset quality of Region 1 credit unions was much better than the asset quality of FICUs overall. The delinquent loans-to-total loans rate in the region was 0.66 percent in 2002 compared to 0.80 percent for all FICUs. Last year's net charge-off rate of 0.34 percent was much lower than the overall FICU charge-off rate of 0.51 percent. While Region 1 experienced a large number of bankruptcies in 2002, the number of cases and their effects on the credit unions was less significant than on many FICUs. Last year, Region 1 had the fewest bankruptcies of any of the six NCUA regions, and its bankrupt loans-to-total loans ratio of 0.22 percent was half of the FICU ratio of 0.44 percent. As a result, only eight percent of the credit unions indicated that bankruptcy is their principal concern for 2003.

Competition and Credit Union Operational Concerns for 2003

The majority (85 percent) of the credit unions feel that banks are their primary source of competition for loans, followed by other credit unions and finance companies (both 23 percent), and retailers (eight percent). For savings, 71 percent of the region's credit unions believe that banks are the primary competition, with 29 percent saying other credit unions, and 14 percent believing that mutual funds and corporate equity are their primary source of competition. In Region 1, 50 percent of the credit unions feel that interest rate spreads/yields are the principal concern for 2003. Eighteen percent believe that expansion costs are the main concern, followed by loan growth, bankruptcy, global economic/political conditions and share growth (8 percent each).

Member Concerns and Economic Conditions in 2003

When asked to assess their member's confidence/sentiment, 71 percent of the credit unions feel that their member's outlook for this year is about the same as in 2002. Twenty-one percent of the credit unions believe that their member confidence/sentiment will be higher this year, while the remaining 7 percent feel that their members will be more pessimistic about 2003 than they were last year. The majority of the region's credit unions characterize their local economic conditions with such phrases as "weak retail sales," poor government fiscal positions," and "high unemployment." Nevertheless, certain parts of the region appear to be recovering, as 25 percent responded that unemployment was low, with 17 percent indicating that their government's fiscal positions were strong and retail sales were robust.

The economic and financial conditions throughout Region 1 are very disparate. During 2002, the economies in Rhode Island and Maine performed relatively well, while non-farm employment declined significantly in Connecticut, Massachusetts and Vermont. In New Hampshire and New York, conditions were mixed, varying greatly in different parts of the state. The region's economy began decelerating in 2001, and as a result, the unemployment rate and much of the region's overcapacity has stabilized. However, the weakness of the information technology, manufacturing, securities, and to a lesser extent, tourism industries continue to constrain the economy's ability to gain significant momentum. Further weighing on the region's economies are the weak fiscal positions of most of the state and local governments. The housing market, while providing significant support to the region's economy, is at risk of suffering some "investment bubble" effects. The Boston, Manchester, N.H. and New York City areas are at greatest risk to experience a moderate depreciation in home values.

NCUA Region Two

NCUA Region 2 (Mid-Atlantic) consists of five states[2] plus the District of Columbia. There are roughly 11.7 million members in this region, up 300,000 (2.8 percent) over the past year. The regional credit unions (CUs)[3] have about 14.5 percent of the total assets, up 14.1 percent for the year. These percentages mirror the regional economy where the regional gross state product is about 14 percent of the U.S. gross domestic product. The regional production is concentrated more in government, services, finances, insurance, and real estate industries than the national average.

Lending

Region 2 CUs generated annual loan growth of 8.9 percent, well above the national average. Over the course of 2002, first mortgages supplied 65 percent of loan portfolio growth, followed by auto loans at 36 percent. Combined real estate secured lending (first mortgages and HELOCs) accounted for 71 percent of the gain.

Going forward into 2003, 20 percent of Region 2 CUs anticipated higher loan growth, with 50 percent expecting results similar to those of 2002. About 60 percent believe they will see their loan-to-share ratios improve, and the remainder are split evenly between the same or lower for this key measure.

Another 90 percent of CUs believe purchase money mortgage lending will be the same or lower in 2003. Survey results also show 80 percent of Region 2 CUs are counting on lower mortgage refinance activity, versus 48 percent expecting the same outlook among all surveyed CUs. Early indications of the first quarter, however, are that mortgage lending is still strong among CUs.

The expectations for "Other Real Estate" (HELOCs and second mortgages) is that 60 percent of the respondents believe they will meet their 2002 results (Region 2 growth of 10.8 percent in 2002), and 40 percent expect higher loan growth.

Total auto loans in Region 2 advanced by 2.9 percent in 2002 versus 4.75 percent for all CUs. Region 2 used auto loans led the way in this category, up 8.6 percent for the year while the new auto portfolio declined 2.1 percent. Only 10 percent of our survey respondents in Region 2 believe 2003 new auto loan growth will be less than 2002. A full 90 percent anticipate better or equal results. The used auto outlook is just as strong, with 70 percent expecting to generate better growth and only 10 percent looking for results to decline.

Unsecured loans (excluding credit cards) represent 10 percent of all CU loans in the region. This portfolio segment declined 2.4 percent in 2002. One factor may be that the average loan rate was almost 13 percent, down just 25 basis points from 2001. About 60 percent of CU leadership in the region do not see this portfolio segment as a source of growth in 2003, but 20 percent do expect to see their results improve.

[2] The five states are Delaware, Maryland, New Jersey, Pennsylvania, and Virginia.
[3] Credit unions (CUs) are federally insured credit unions, except that the surveyed figures are from federally-chartered credit unions.

Member Shares

Member savings deposits reached $69.7 billion in 2002, up $8.5 billion (13.9 percent) during the year. Regular shares contributed 50.8 percent of the increase last year, followed by money market accounts at 30.6 percent. Add in share drafts at 8.8 percent, and you get 90.2 percent of 2002's increase from highly liquid deposit accounts. Bucking the trend were IRA deposits, up 11 percent for the year, reflecting member concern for safety of principal.

For 2003, 50 percent of Region 2 respondents see a similar share growth and another 30 percent see a decline. Only 30 percent believe their deposit liquidity structure will be "more liquid." The other 70 percent are evenly split between "about the same" and "less liquid."

Some 60 percent of Region 2 surveyed CUs see share drafts (12 percent of Region 2 CU shares) increasing at roughly the same rate as during last year (2002 regional average was 9.9 percent growth), and another 30 percent see higher results. Regular shares (40 percent of Region 2 CU shares) grew an exceptional 18.6 percent in 2002. About 40 percent believe their 2003 results will be lower, while another 40 percent expect a similar year. Money market accounts (15 percent of CU shares) reached almost $11 billion in 2002, up 32.5 percent. Some 30 percent of respondents feel they can match their 2002 results while another 40 percent see lower growth. CU share certificates (22 percent of CU shares) experienced a tough 2002 with a small 0.2 percent increase. Some 60 percent of surveyed Region 2 CUs expect higher share certificate growth, while another 30 percent call for growth to be about the same for this year.

IRA accounts (10 percent of CU shares) were a safe haven for members' precious retirement funds in 2002. This deposit segment advanced 11 percent for the year compared to a national average of 8.2 percent. About 70 percent of our Region 2 respondents see similar growth rates for 2003 and 20 percent expect higher levels.

Return on Average Assets (ROA), Spreads and Asset Quality

With deposits re-pricing faster than loans in 2002, credit unions experienced a healthy improvement in Region 2's consolidated ROA. At 1.07 percent (the same average ROA for all CUs), this profitability measure increased 6 basis points over 2001 for the regional credit unions. Unlike other regions, it appears most CU management teams expect the favorable environment (falling interest rates) may continue in 2003. About 30 percent expect their ROAs to be higher this year. Another 50 percent anticipate no change in the ROA.

Gross spreads declined from 368 basis points in 2001 to 354 last year. About 50 percent of our respondents expect to attain a similar gross spread in 2003, but 30 percent are optimistic they can improve spreads from last year's level. At the same time, 90 percent believe asset quality will stay at current levels, while only 10 percent forecast an improvement.

Competition and Credit Union Operational Concerns for 2003

At a high level, Region 2 CUs view their principal competition for lending to be banks, followed closely by finance companies (including manufacturer sponsored finance companies). Close by on the list are "other CUs." Retailers and Internet lenders are not viewed as major competitive threats at this time.

Region 2 CUs view their principal competition for savings dollars to be banks and mutual funds/corporate equity. Only a small percentage viewed other CUs and finance companies as competitive concerns for 2003.

The primary operational concerns for 2003, cited by our regional respondents, were "loan growth" and "bankruptcies/charge-offs." Among all CUs, "loan growth" typically ranks high. Improving ROAs, rising "share growth," and increasing expansion costs were also mentioned by 11 percent of the regional sample group.

Member Concerns and Economic Conditions in 2003

When asked to access their members' general sentiment/confidence now versus last year at this time, 60 percent of the respondents indicated that it was about the same and 20 percent thought it was better. Another 20 percent felt their memberships' sentiment had eroded from early 2002.

Credit union leadership in Region 2 viewed the potential for negative employment fallout, and financially distressed state governments as a primary economic concern in their states. Low corporate profits and weakness across the retail sector were also cited in their assessments of economic conditions in the region. Continued weak labor markets and layoff concerns will dominate Region 2's economic radar screen.

NCUA Region Three

As of year-end 2002, there were 1,722 credit unions in NCUA Region 3 (Southeast), consisting of ten states and two territories[4]. Total assets equaled $94.4 billion, up 11.8 percent for the year. There are roughly 15.2 million members in this region, up 500,000 (3.2 percent) over the past year. The 25 largest CUs in Region 3 range in assets from $685 million to $9.8 billion. Collectively, they hold 41 percent of the region's assets and 30 percent of the members.

Lending

Region 3 CUs generated annual loan growth of just 5.2 percent, well below the national average. Annualized fourth quarter results shows loan growth slowed to 2.6 percent. Over the course of 2002, first mortgages supplied 54 percent of loan portfolio growth, followed by auto loans at 36 percent. Combined real estate secured lending (first mortgages and HELOCs) accounted for 71 percent of the gain.

Going forward into 2003, 55 percent of Region 3 CUs anticipated higher growth, with 30 percent expecting results similar to those of 2002. Fifty percent believe they will see their loan-to-share ratio improve, and the other half is split evenly between the same or lower for this key measure.

About 75 percent of CUs believe purchase money mortgage lending will be the same or lower in 2003. Survey results also show 55 percent of Region 3 CUs are counting on lower mortgage refinance activity, versus 10 percent expecting to outperform 2002 results. A large supply of first mortgages in the pipeline should ensure CUs will begin the year on a high note.

The expectations for "Other Real Estate" (HELOCs and second mortgages) are that 45 percent of the respondents believe they will exceed their 2002 results (Region 3 growth of 9.9 percent in 2002), and 45 percent expect similar results.

Region 3 total auto loans advanced by 4.6 percent in 2002 versus 5.4 percent for all CUs. Region 3 used auto loans lead the way among all auto loans, up 8.7 percent for the year while the new auto portfolio grew 0.4 percent. Only 5 percent of our survey respondents believe 2003 new auto loan growth will be lower than during 2002. A full 60 percent anticipate better results. The used auto outlook is even stronger, with 68 percent expecting to generate better growth and none of the respondents looking for results to decline.

Unsecured loans (excluding credit cards) represent 4.5 percent of all CU loans in the region. This portfolio segment declined 3.7 percent in 2002. One factor may be that the average loan rate was almost 13 percent, down just 25 basis points from 2001. Eighty percent of CU leadership do not see this portfolio segment as a source of growth in 2003, but 20 percent do expect to see their results improve.

[4] The ten states include Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, Mississippi, North Carolina, South Carolina, and Tennessee, and the territories of Puerto Rico and the U.S. Virgin Islands.

Member Shares

Member savings deposits reached $82 billion in 2002, up $8.4 billion (11.5 percent) during the year. Regular shares contributed 50 percent of the increase last year, followed by money market accounts at 31 percent. Add in share drafts at 9 percent and you get 90 percent of 2002's increase from highly liquid deposit accounts. Bucking the trend were IRA deposits, up 10.9 percent for the year, reflecting member concern for safety of principal.

For 2003, 50 percent of Region 3 respondents see lower share growth and 45 percent see it to be about the same. A full 60 percent believe their deposit liquidity structure will remain the same. The other 40 percent are evenly split between more and less liquid.

Fifty percent see share drafts (12 percent of CU shares) increasing at roughly the same rate as last year (region average was 8.3 percent) and 35 percent see better results. Regular shares (37 percent of CU shares) grew an exceptional 16.3 percent in 2002. Ninety percent believe their 2003 results will be the same or lower. Money market accounts (16 percent of CU shares) reached almost $13 billion in 2002, up 24.4 percent. Forty-seven percent of respondents feel they can match their 2002 results, and 43 percent see lower growth. CU certificates of deposit (25 percent of CU shares) experienced a tough 2002, declining by 0.2 percent. Forty-eight percent of Region 3 CUs experienced declines. Expectations for 2003 are almost evenly split with 35 percent calling for lower growth, 35 percent at about the same and 30 percent expecting better results.

IRA accounts (10 percent of CU shares) were a safe haven for members' precious retirement funds in 2002. This deposit segment advanced 10.9 percent for the year compared to a national average of 8.3 percent. Sixty-three percent of the respondents see similar growth rates for 2003 and 26 percent expect stronger gains.

Return on Average Assets, Spreads and Asset Quality

With deposits re-pricing faster than loans in 2002, Region 3 experienced a healthy improvement in consolidated ROA. At 1.11 percent, (total Movement ROA in 2002 estimated at 1.07 percent) this profitability measure increased 17 basis points over 2001. The top 25 CUs had an average ROA of 1.27 percent, versus 1.17 last year. In total, 920 of the region's 1,722 CUs generated a better ROA in 2002. It appears most CU management teams recognize the favorable environment (falling interest rates) will not be repeated in 2003. Forty-five percent expect their ROAs to be lower this year. Only 20 percent anticipate improvements.

Gross spreads improved from 375 basis points in 2001 to 388 last year. Only 10 percent of our respondents expect to attain a higher gross spread in 2003, but 55 percent are optimistic they can maintain spreads at last year's level. At the same time, 70 percent believe asset quality will stay at current levels. Just 10 percent forecast deterioration.

Competition and Credit Union Operational Concerns for 2003

At a high level, Region 3 CUs view their principal competition for lending as finance companies (includes manufacturer-sponsored finance companies), followed closely by banks. Further down the list are other CUs. Retailers and Internet lenders are not viewed as major competitive threats at this time.

Region 3 CUs view their principal competition for savings as banks and other CUs. Only a small percentage viewed mutual funds and the equity markets as competitive concerns for 2003.

The primary operational concerns for 2003 cited by our respondents were loan growth and bankruptcies/charge-offs. These two items typically rank high. Improving ROAs and shrinking spreads were also mentioned by 13 percent of the sample group. Global economic conditions were cited by just 6 percent of the respondents.

Members Concerns and Region 3 Economic Conditions in 2003

When asked to access their members' general sentiment/confidence now versus last year at this time, 65 percent of the respondents indicated that it was about the same and 30 percent thought it was better. Only 5 percent felt their memberships' sentiment had eroded from early 2002.

Credit union leadership in Region 3 viewed financially distressed state governments and the potential for negative employment fallout as a primary economic concern in their states. Low corporate profits and weaknesses across the retail sector were also cited in their assessments of economic conditions in the region. Continued weak labor markets and layoff concerns will dominate Region 3's economic radar screen.

NCUA Region Four

NCUA Region 4 (North Central) consists of seven states.[5] The regional credit unions have about 16.3 percent of total credit union assets, up 9.3 percent for the year. There are roughly 14.7 million members in this region, up 130,000 (0.9 percent) over the past year. These percentages mirror the regional economy where the regional gross state product is concentrated more in manufacturing than the national average.

Lending

Region 4 CUs generated annual loan growth of just 4.7 percent for 2002, well below the national average. Over the same time period, first mortgages supplied 61 percent of loan portfolio growth, followed by auto loans at 14 percent.

Mortgage activity is still strong but down from the peaks of the fourth quarter of 2002. Home prices appear to be rising less rapidly now than they were three months ago. Existing homes seem to be taking slightly longer to sell, but that may be seasonal. At a minimum, this slower market has put a damper on price increases.

Most credit unions adhere very strongly to the 80% LTV, so slight declines would be a concern but not terribly threatening. Larger price declines could be a significant concern as most credit unions in the North Central Region have experienced very little, if any, losses on residential real estate loans. Accordingly, very little loan loss reserve is allocated to the mortgage portfolio.

Further, a decline in home pricing could lead to a noticeable decline in loan demand. If consumers were to become concerned about the equity in their homes, the expected reaction might be to rein in other borrowing and cut discretionary spending. While there is a slight concern about price support, the key here seems to be the general strength of the economy and the indications of unemployment. The concern for home prices will likely follow the unemployment picture. Fifty percent of Region 4 CUs, when surveyed, expected first mortgage loan growth (new originations) to remain the same throughout 2003.

It appears that refinancings are declining (most have already occurred) but continue to be a large portion of total mortgage activity. During 2002, many of the refinancings were 30-year loans converting to 15-year loans. In recent months, the 30-year loans are growing in the proportion of new loans made that they represent. This recent decline in refinancing is supported by approximately 83 percent of surveyed CUs in Region 4 believing that growth in refinancing will either be "about the same" or "lower" in 2003.

Homeowners continue to extract equity from their homes and it appears that the aforementioned shift to more 30-year loans is to make more room for other borrowings, either currently or in the near future. In fact, more than 80 percent of CUs within the region think that non-first mortgage loan growth will either be "higher" or "about the same" this year. It appears though that the amount of equity extraction when compared to

[5] The seven states are Illinois, Indiana, Michigan, Missouri, Ohio, West Virginia, and Wisconsin.

that of the fall of 2002 is lower. We suspect that the consumer is more concerned about future borrowing power than current consumption.

Home equity lending has also slowed from the peaks of 2002. Credit unions appear to be lowering interest rates to counter the decline in demand.

It appears auto lending is decreasing during the first quarter of 2003. Sales volumes at local dealerships have declined. Credit unions seem to be receiving typical percentage shares of the volume that is occurring.

The zero-percent financing (in place since mid-2002) has definitely reduced the credit union share of new auto financing. Despite the fact that not all borrowers qualify for the zero percent financing, the consumer seems to be steering in the direction of the auto financing companies. Roughly 83 percent of CUs in the region expect new auto loan growth to be "higher" or "about the same."

Credit unions appear to be getting more used car financing as new car financing declines. Credit standards have not been compromised, but many credit unions are offering the same rate or a slightly lower rate for new and used auto loans than they did last year. The underwriting standards have not changed, but pricing (low rates) seems to be the general response to the lower volumes of sales and new auto financing (taken by the auto financing companies).

Loan quality

In general, underwriting standards are not changing. However, it appears some credit unions may be getting into lending areas, such as indirect auto lending, that are new to their operations. In this sense, there may be a slight upswing in credit risk. Currently, such risk appears to be the exception rather than the rule.

Member Concerns for 2003

Credit union members appear to be 'shoring up' their financial positions. The current uncertainties in the economy are causing a pause in borrowing commitments. However, the low interest rate environment has the consumer jockeying for future borrowing capacity.

Credit union members appear to be cautious in their use of consumer lending. The only real growth is being seen in the mortgage and home equity area. General trends show all other loans declining. As a result, credit unions in Region 4, according to our survey, have a significant amount of confidence in overall loan growth in 2003, as 50 percent claim that growth will be "higher" and 33 percent believe that loan growth will be "about the same" this year.

Credit union concerns for 2003

It appears that loan delinquencies and charge offs are up slightly. Expectations are to see this continue until the economy becomes more robust. Massive delinquencies and charge-offs do not appear to be looming.

It appears credit unions are currently challenged by the fact that deposits are growing more rapidly than loans (again, the consumer appears to be positioning for the future). The investment options beyond loans will not produce the same spreads we are accustomed to seeing. Fifty percent of Region 4 CUs actually expect 2003 gross spreads to be "lower" than in 2002, as the other 50 percent are split between higher and relatively similar spreads. This leads to several critical questions about the operation of the credit union and pricing of deposits.

NCUA Region Five

NCUA Region 5 (Central) consists of eleven states[6] and 1,745 credit unions as of year-end 2002. The regional credit unions have about 16.9 percent of the total assets, up 10.9 percent for the year. There are roughly 14.8 million members in this region, up 276,000 (1.9 percent) over the past year. These percentages mirror the regional economy where the regional gross state product is about 16.8 percent of the US gross domestic product. The regional production is concentrated more in transportation, public utilities, farms, forestry, fisheries and retail trade than the national average.

Lending

Region 5 CUs generated annual loan growth of just 7.4 percent, slightly above the national average. Over the course of 2002, auto loans supplied 52 percent of loan portfolio growth, followed by first mortgages at 31 percent. Combined real estate secured lending (first mortgages and HELOCs) accounted for 48 percent of the gain.

Going forward into 2003, a similar number of Region 5 CUs (36 percent) anticipated higher or equal loan growth from the 2002 results. About 50 percent believe they will see their loan-to-share ratio improve, and 40 percent expect a lower result for this key measure.

Another 75 percent of CUs believe purchase money mortgage lending will be the same or lower in 2003. Survey results also show 46 percent of Region 5 CUs are counting on lower mortgage refinancing activity, similar to the 48 percent expected among all surveyed CUs. Early indications of the first quarter, however, are that mortgage lending is still strong among Region 5 CUs.

The expectations for “Other Real Estate” (HELOCs and second mortgages) is evenly split (91 percent of the respondents) between meeting their 2002 results and expecting higher loan growth (Region 5 growth of 9.9 percent in 2002 for this loan category).

Total auto loans in Region 5 advanced by 7.5 percent in 2002 versus 4.8 percent for CUs overall. Region 5 used auto loans lead the way, up 10.8 percent for the year while the new auto portfolio increased 4.2 percent. Credit unions are generally optimistic regarding new automobile lending activity in 2003. Only 27 percent of our survey respondents believe 2003 new auto loan growth will be lower than during 2002. A full 73 percent anticipate better or equal results. The used auto outlook is just as strong, with 46 percent expecting to generate better growth and only 9 percent looking for results to decline.

Unsecured loans (excluding credit cards) represent 5 percent of all CU loans in the Region. This portfolio segment declined 1.7 percent in 2002. One factor may be that the average loan rate was almost 13 percent, down just 25 basis points from that of 2001. Almost none of the CU leadership in the region sees this portfolio segment as a source of

[6] The eleven states are Arizona, Colorado, Iowa, Kansas, Minnesota, Nebraska, New Mexico, North Dakota, Oklahoma, South Dakota, and Texas.

growth in 2003. In fact, about 91 percent of credit union managers expect unsecured loan growth to be about the same this year as in 2002.

Member Shares

Member savings deposits reached $81.9 billion in 2002, up $7.7 billion (10.4 percent) during the year. Regular shares contributed 40.8 percent of the increase last year, followed by money market accounts at 34.2 percent. Add in share drafts at 6.6 percent, and you get 81.6 percent of 2002's increase from highly liquid deposit accounts. IRA deposits were also up 10.1 percent for the year, reflecting member concerns for safety of principal.

Geopolitical concerns and uncertainty related to the economy are the primary reason credit unions expect share growth to remain relatively strong in 2003. For 2003, 46 percent of Region 5 respondents see a higher share growth and another 36 percent see a decline. About 60 percent believe their deposit liquidity structure will be "about the same." The other 40 percent are evenly split between "more liquid" and "less liquid."

Some 55 percent of Region 5's surveyed CUs see share drafts (13 percent of Region 5 CU shares) increasing at a higher rate than during last year (the 2002 regional average was 4.9 percent growth), and another 36 percent see similar results. Regular shares (33 percent of Region 5 CU shares) grew an exceptional 13.2 percent in 2002. About 55 percent believe their 2003 results will be about the same, while another 36 percent expect another banner year. Money market accounts (18 percent of CU shares) reached $15 billion in 2002, up 21.3 percent. Some 25 percent of respondents feel they can match their 2002 results and another 50 percent see lower growth. CU share certificates (25 percent of CU shares) experienced a tough 2002 with a small 2.2 percent increase. Only 18 percent of surveyed Region 2 CUs expect higher share certificate growth, while another 46 percent call for growth to be about the same for this year.

IRA accounts (8 percent of CU shares) were a safe haven for members' precious retirement funds in 2002. This deposit segment advanced 10.1 percent for the year compared to a national average of 8.2 percent. About 73 percent of our Region 5 respondents see similar growth rates for 2003 and 18 percent expect higher levels.

Return on Average Assets (ROA), Spreads, and Asset Quality

With deposits repricing faster than loans in 2002, credit unions experienced a healthy improvement in Region 5's consolidated ROA. At 1.06 percent (slightly lower average ROA than for all CUs), this profitability measure increased 9 basis points over 2001 for the regional credit unions. Like other regions, it appears most CU management teams expect the favorable environment (low interest rates) to continue in 2003. About 55 percent expect their ROAs to be about the same this year. Another 27 percent anticipate a lower ROA than last year.

Gross spreads declined from 416 basis points in 2001 to 406 last year. About 73 percent of our respondents expect to attain similar or lower gross spreads in 2003, but 27 percent are optimistic they can improve spreads from last year's level. At the same time, 90 percent believe asset quality will stay at current levels. Just 10 percent forecast an improvement.

Investments

Deposit growth outpaced loan growth resulting in a 25.5 percent growth in investments in 2003. Total investments ended the year at $21.8 billion. Credit unions continue to maintain the majority of their investments short-term. Approximately 91 percent of all credit union investments will mature or reprice within 3 years and over 59 percent will mature or reprice within 12 months.

Competition and CU Operational Concerns for 2003

At a high level, Region 5 CUs view their principal competition for lending as banks, followed closely by “other CUs.” Close by on the list are finance companies (including manufacturer-sponsored finance companies). Retailers and Internet lenders are not viewed as major competitive threats at this time.

Region 5 CUs view their principal competition for savings dollars as “other CUs,” mutual funds, and banks. Only a small percentage viewed finance companies as competitive concerns for 2003.

The primary operational concerns for 2003, cited by our regional respondents, were “loan growth,” “interest rate spreads,” and “membership growth.” Among all CUs, “loan growth” typically ranks high.

Member Concerns and Region 5 Economic Conditions in 2003

When asked to assess their members' general sentiment/confidence now versus last year at this time, 50 percent of the respondents indicated that it was about the same and 50 percent thought it was better. No respondent felt their memberships' sentiment had eroded from early 2002.

Credit union leadership in Region 5 viewed the potential for low company profits and financially distressed state governments as a primary economic concern in their states. High unemployment and weakness across the retail sector were also cited in their assessments of economic conditions in the region. Continued weak labor markets and layoff concerns will dominate Region 5's economic radar screen.

NCUA Region Six

Region 6 (Western) comprises ten states and two territories[7]. As of December 31, 2002, the region's 1,272 credit unions made up 13 percent of all federally insured credit unions and held some $133 billion in total assets, nearly 24 percent of the nation's total credit union assets. During 2002, assets grew some 9.8 percent while net worth increased 9.5 percent to $13.5 billion. Share growth (9 percent) significantly outpaced loan growth (5 percent) and consequently investments grew nearly 19 percent. A large part of these excess funds remain in short-term investments and cash equivalents.

Loan Growth

In 2002, loan growth slowed to an annual rate of 4.9 percent with total loans for Region 6 ending the year at $82.4 billion – making up just fewer than 62 percent of assets.

Real estate loan growth did show an increase for the region but at a slower pace. Looking forward, credit unions generally view the prospects for real estate lending as remaining fairly positive, although there is some expectation that refinancing activity will eventually slow. Following two years of double-digit growth, real estate loans at year-end made up 44 percent of total loans. Of that total, 22.5 percent comprised fixed-rate first mortgage loans, 8.5 percent consisted of adjustable rate mortgages and 13 percent were in home equity and other real estate secured loans.

Auto lending has historically been a strong area for credit unions. Auto loan growth did slow to a 5.2 percent pace, ending the year at $33.6 billion outstanding. The zero percent financing offered by automakers has eroded credit unions' share of the new car financing market. Increasing activity in indirect lending has helped maintain portfolio balances. Credit unions are generally optimistic about future prospects, particularly in the used car market.

Elsewhere, loan prospects are not so bright and there is little expectation for any major growth in unsecured lending. Unsecured lending fell throughout the region in 2002, ending the year at $8.3 billion in outstanding balances – a decline of 5.2 percent. Only Hawaii and Utah managed positive growth.

Loan Quality

Credit unions continue to do a good job in managing credit risk and generally remain very positive about the outlook for 2003. Delinquency rates remained unchanged at 0.7 percent in 2002 compared to the national average of 0.8 percent. However, the ratios of individual states did vary widely. For example, Alaska's ratio of delinquent loans increased to 1.4 percent from 0.5 percent last year, while Utah declined to 0.89 percent from 1.13 percent. Other Real Estate Owned (OREO) in the region dropped by 6.0 percent to some $30 million compared to a 9.4 percent increase nationally.

[7] The ten states include Alaska, California, Hawaii, Idaho, Montana, Nevada, Oregon, Utah, Washington, Wyoming, and the territories are Guam and American Samoa.

Helping loan quality, bankruptcy filings by members declined by 1.4 percent to 53,770. The Region again reversed the national trend, where national bankruptcies increased by 6.3 percent to 240,482. Bankruptcies accounted for 37 percent of total loan losses in the region and 39 percent nationwide.

Investments

With share growth outpacing loan growth, investments grew by 18.7 percent and ended the year at $44.5 billion or 33.5 percent of total assets and an increase from last year's ending balances of $37.5 billion. Credit unions continue to keep the majority of their investments short term. Some 85 percent of investments will mature or reprice within 3-years and over 53 percent will mature or reprice within 12 months. Credit unions continue to hold ample liquidity.

Share Growth

Continuing geopolitical uncertainties and weak fundamentals lead credit unions to believe that prospects for share growth will remain the same or even improve in 2003. Most of this growth is likely to come in regular share and money market share accounts. Credit unions also remain fairly optimistic about the prospects for continuing growth in certificates of deposits while IRA/Keogh accounts are expected to continue to grow fairly modestly. In 2002, shares and deposits grew 9.4 percent to $116.6 billion, however, certificates fell nearly 3 percent due to the low rate environment. While savings with less than a 1-year maturity increased some 8 percent to $105 billion, longer term maturity accounts did see some strong gains. Savings accounts with 1-year to 3-year maturities increased almost 20 percent to $8.8 billion while savings accounts with greater than 3-year maturities increased 45 percent to $2.8 billion.

The current low rate environment makes it very difficult for credit unions to issue long-term certificates. We are hearing some concern from credit unions about the need to match funding sources for some of their residential loan portfolios.

Earnings

2002 was a good year for most credit unions in the region with the average ROA increasing 20 basis points over the prior year to 1.15 percent. Gross income fell 107 basis points to 6.91 percent. Despite this drop, the net margin improved slightly to 4.69 percent. The average cost of funds declined by 120 basis points - much faster than the yields on loan portfolios which more than offset sharp declines in investment returns. However, liability rates cannot decline much further and many credit unions are paying rates significantly higher than the wholesale market to assist members living on fixed income and investment dividends. A large number of credit unions are worried about declining margins in 2003, as both loan yields and investment returns continue to decline. Fee income remained unchanged at 67 basis points, while operating expenses and provision for loan losses declined modestly.

The improved returns did translate into a 9.6 percent increase in net worth but was outpaced by the 9.8 percent asset growth. Consequently, the net worth ratio remained at 10.2 percent for the second year. Within the region, six states (Alaska, Idaho, Nevada, Oregon, Washington and Wyoming) showed stronger net worth ratios while three states (Hawaii, Montana and Utah) declined modestly. The net worth ratio for California credit unions remained unchanged.

Credit Union Operational Concerns for 2003

When asked to name the principal concern for 2003, nearly 27 percent cited loan growth and asset growth. For the year 2001, credit unions in Region 6 experienced growth rates in assets and loans significantly above the national average. For the year 2002, the growth rate in both categories declined and fell below the national average growth rates. The second most often cited concern was margin pressures. Twenty-three percent of responding credit unions felt this was the primary concern. Many credit unions are concerned about margins coming under pressure if the low rate environment persists throughout 2003. The struggle to continue to pay members top market rates could become even more difficult if returns on investments and assets continue to decline.

A distant third concern expressed by 10 percent of credit unions was credit quality. While loan losses have been manageable, there is concern that an extended period of economic decline would cause deterioration in the credit quality of the loan portfolio.

Other concerns included expense control, capital adequacy, regulatory issues, and member services, but these concerns were expressed as a top concern by relatively few credit unions.

Member Concerns for 2003

Credit union members are definitely feeling the effect of declining equity values on their retirement savings. Also, members living on fixed incomes and investment dividends are suffering great hardship due to the low rates currently available on their savings. Members cited this concern 47 percent of the time when asked for their primary concern for 2003. The overall state of the economy and geopolitical risk were cited frequently but far less often than concerns about low rates.

General Economic Conditions

Most Western states, including Alaska, California, Montana, Nevada, Oregon, Utah, and Washington, are dealing with significant budget shortfalls and this is curtailing public spending plans. This is a particularly difficult time for state employees who are a significant sector of credit union membership. There is an expectation that some states will be forced to lay off state workers and/or teachers, cut back hours, and reduce planned staff additions in 2003 to cope with the shortfalls.

Away from the state budget problems, the economic outlook for 2003 remains neutral to positive. Clearly, any positive economic assumption starts with a quick and definitive conclusion to war with Iraq. Should the conflict drag on for a lengthy period, the economic outlook could darken quickly.

The Federal Reserve Bank of San Francisco reported that sluggishness in the West during the latter months of 2002 was the result of a falloff in consumer spending as consumer sentiment deteriorated. Layoffs also accelerated in 2002, especially in the fields of information technology and manufacturing. The State of California Labor Department recently reported that job losses for 2002 are likely to be revised higher. They added that another concern is that, among those laid-off workers who have found employment, the compensation levels of those new jobs are considerably lower than of the jobs lost. For 2003, the employment outlook remains a concern, but a majority of economists believe that long-dormant business spending will revive in the second half of 2003 and lead to increased hiring.

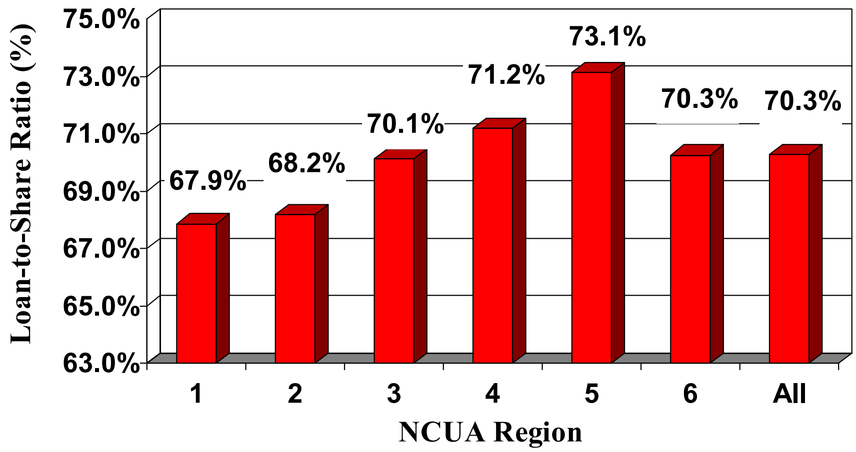
As 2003 has progressed, the rise in energy prices, as well as heightened concerns about the war with Iraq, has been a further drag on consumer spending. Cash from refinancing, as well as a generally strong housing market, has helped to offset some of the impact. While these energy price increases have been a drag on the economy early in 2003, a reversal of the price increases could be equally stimulative in the later months of 2003.

Travel and tourism is a significant industry in many Western states, and revenues have been declining since 2000 for most states with the exception of Alaska. With geopolitical concerns and rising energy prices, 2003 is off to a slow start as well. As with consumer spending in general, tourism is expected to return to more normal levels once the Iraqi conflict is resolved.

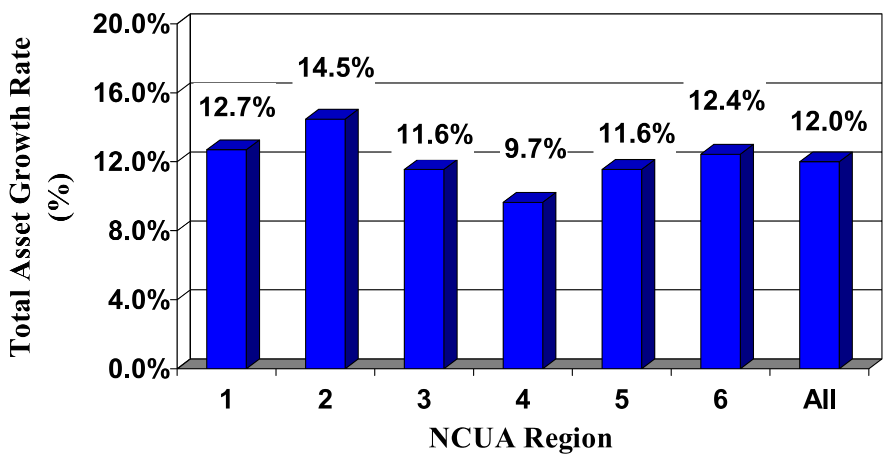
During 2002, two Utah state-chartered credit unions converted to federal charters – a reversal of previous trends and the first such conversions in Region VI since 1999. Both cited state field of membership restrictions and a perceived anti-credit union environment as reasons for converting. Since the passage of a state taxation law on credit unions, several others are considering or are in the process of converting to federal charters.

In general, economic conditions weakened during the second half on 2002 in most Western states, but optimism for 2003 remains high. The more positive outlook is primarily based on the assumption that geopolitical concerns are largely responsible for the current sluggish conditions. Once the Middle East war is resolved, the true test of the economy will begin. Growth in jobs and increase in production capacity usage will be critical in assessing the long-term prospects for the economy. The general belief is that consumer spending will continue to provide the foundation for the economy and, for the first time in roughly three years, businesses will once again regain the confidence necessary to expand for the future.

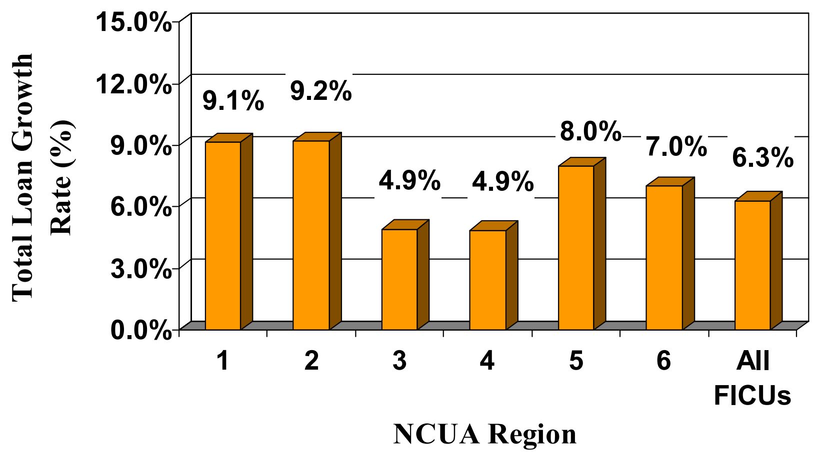
Loan-to-Share Ratio
Federally Insured Credit Unions
by NCUA Region
December 2002



Total Asset Growth
Federally Insured Credit Unions
by NCUA Region
December 2002



Total Loan Growth
Federally Insured Credit Unions
by NCUA Region
December 2002



Total Share Growth
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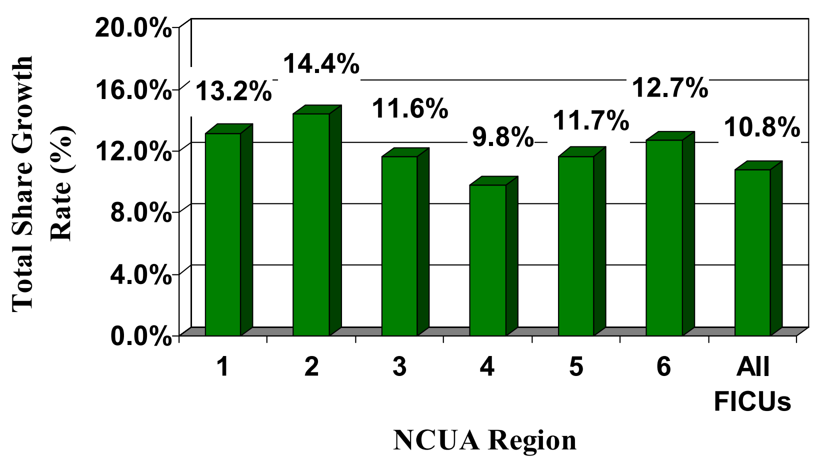
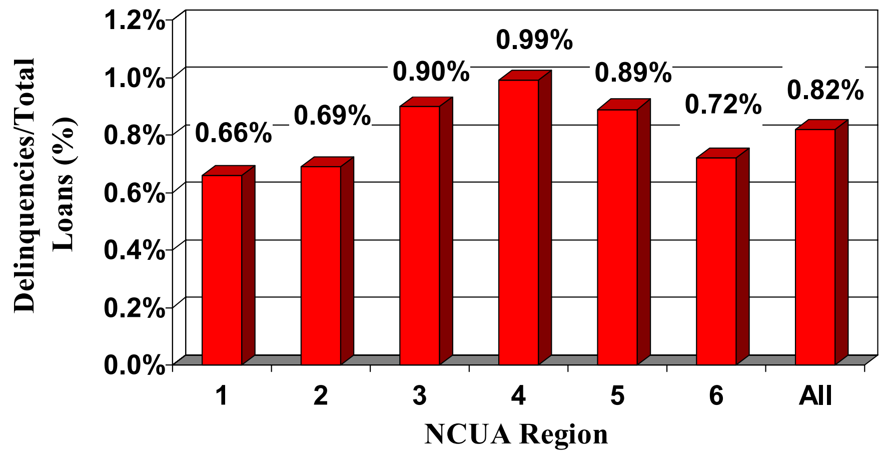
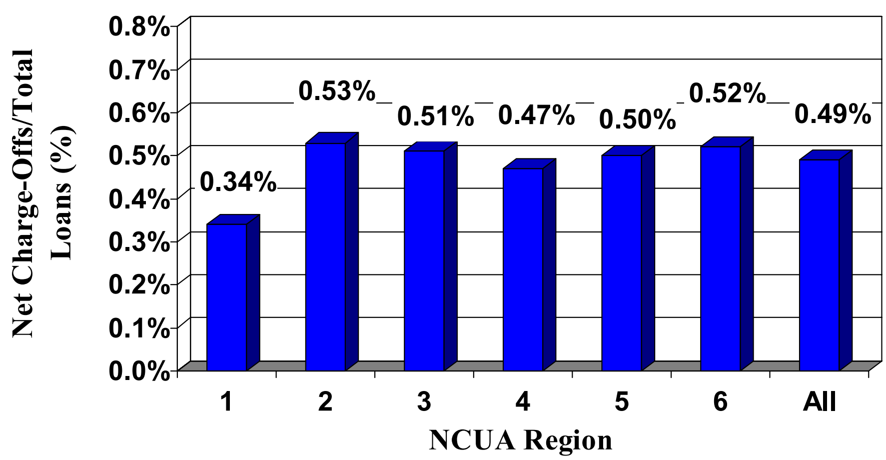
by NCUA Region
December 2002



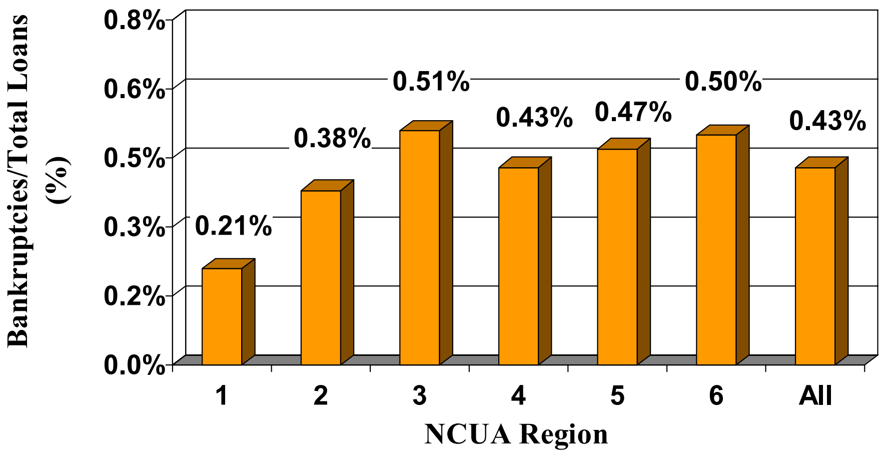
Delinquency Ratio
Federally Insured Credit Unions
by NCUA Region
December 2002



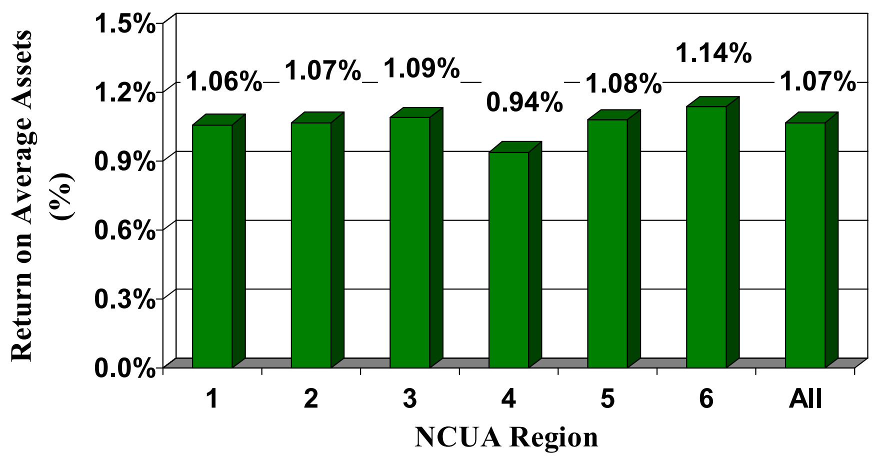
Net Charge-Offs/Total Loans
Federally Insured Credit Unions
by NCUA Region
December 2002



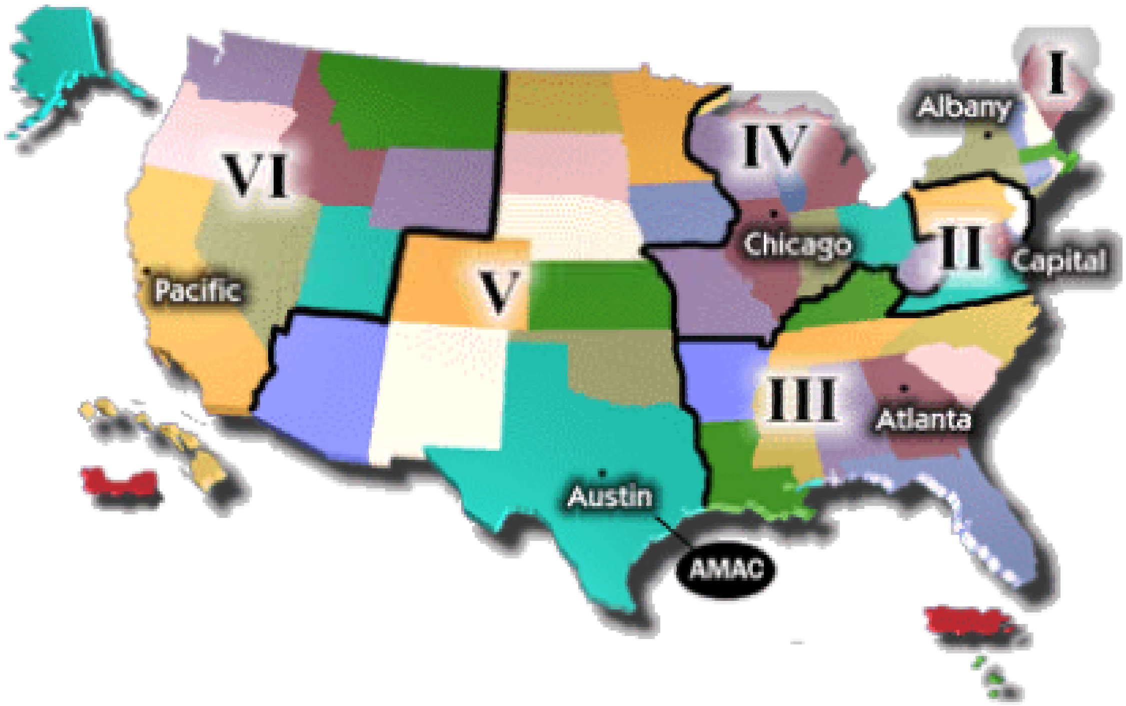
Bankruptcies/Total Loans
Federally Insured Credit Unions
by NCUA Region
December 2002



Return on Average Assets (ROA)
Federally Insured Credit Unions
by NCUA Region
December 2002



NCUA REGIONAL BREAKDOWN



Source: NCUA Web site - http://www.ncua.gov/org/regionalmap.html