



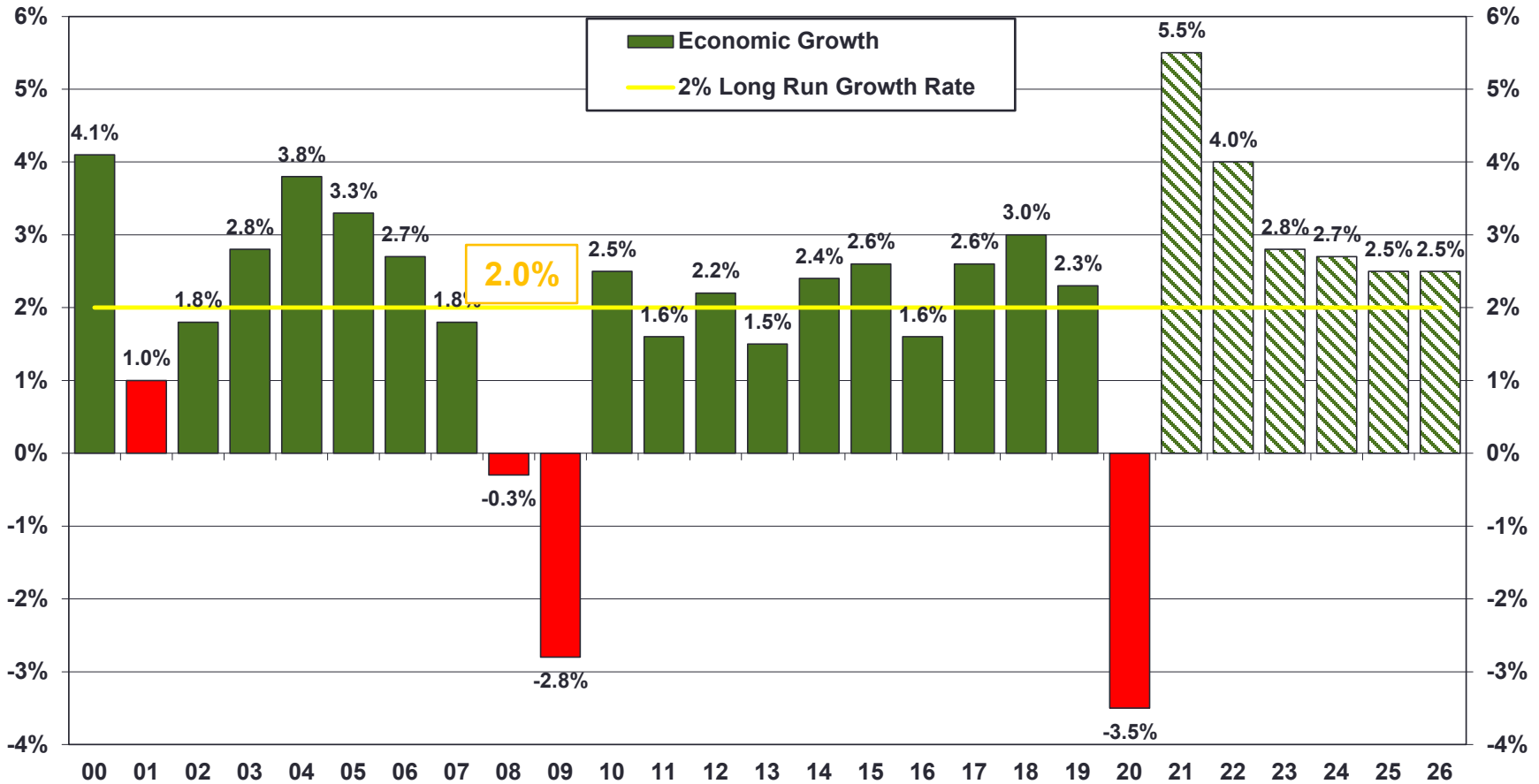
# Economic & Credit Union Update

December 2021

If you have any questions or comments, please contact:  
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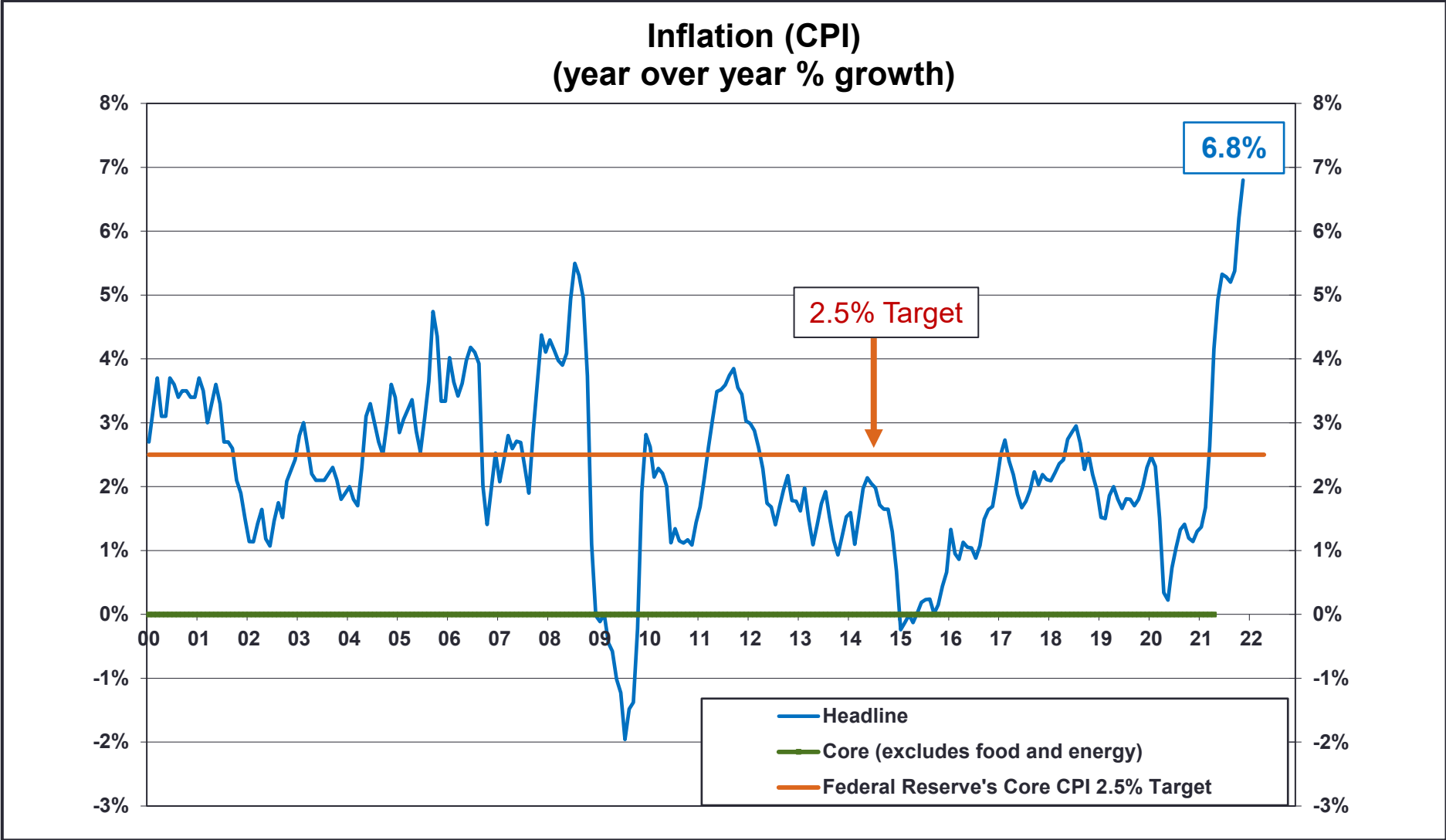
# Above Trend Economic Growth for Next 5 Years

## U.S. Economic Growth Rate



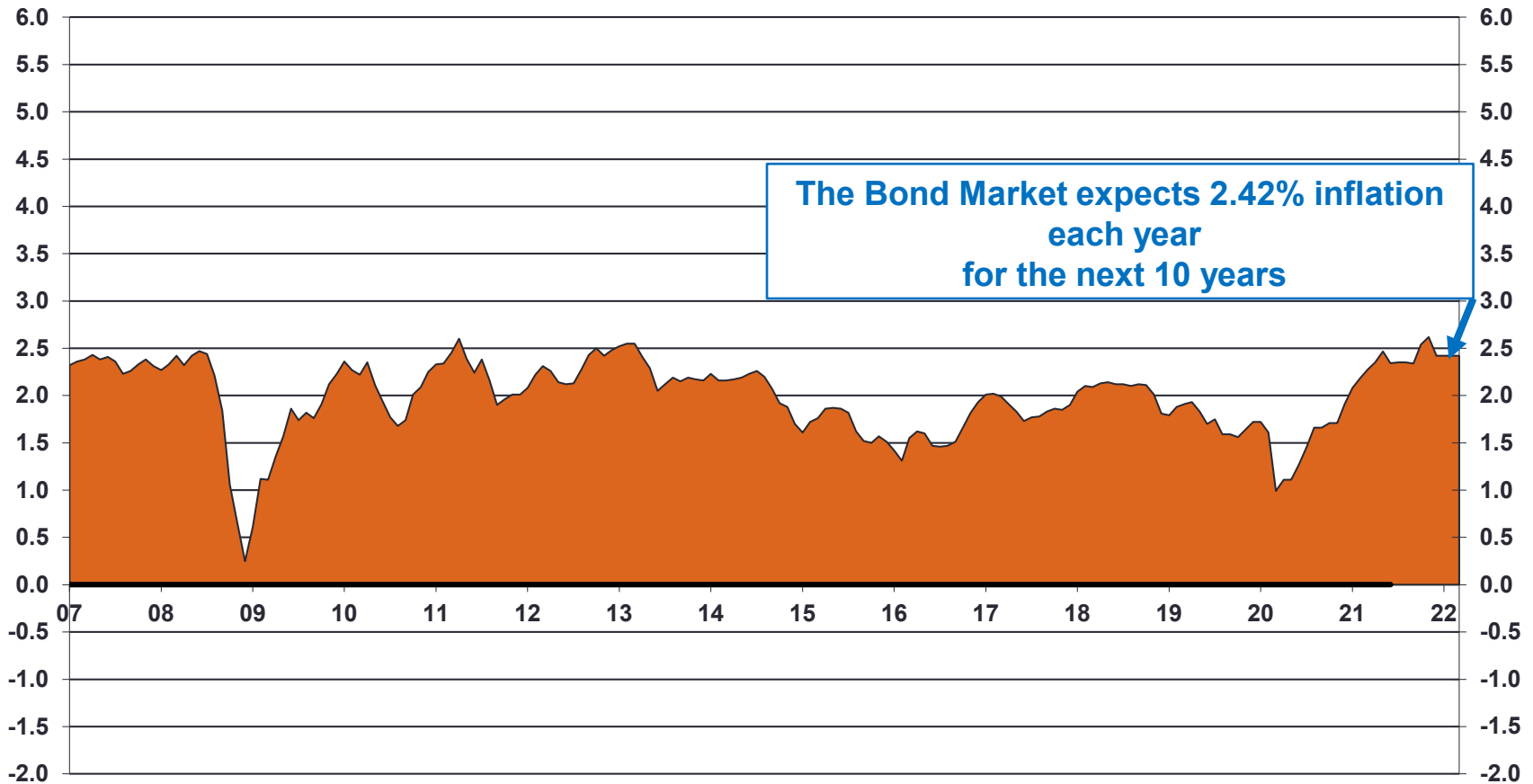
Source: Department of Commerce

# High Inflation for the Next Year



# Inflation Expectations are Anchored Below 2.5%

## Inflation Expectations



# The Inflation Debate:

## Higher Inflation Factors:

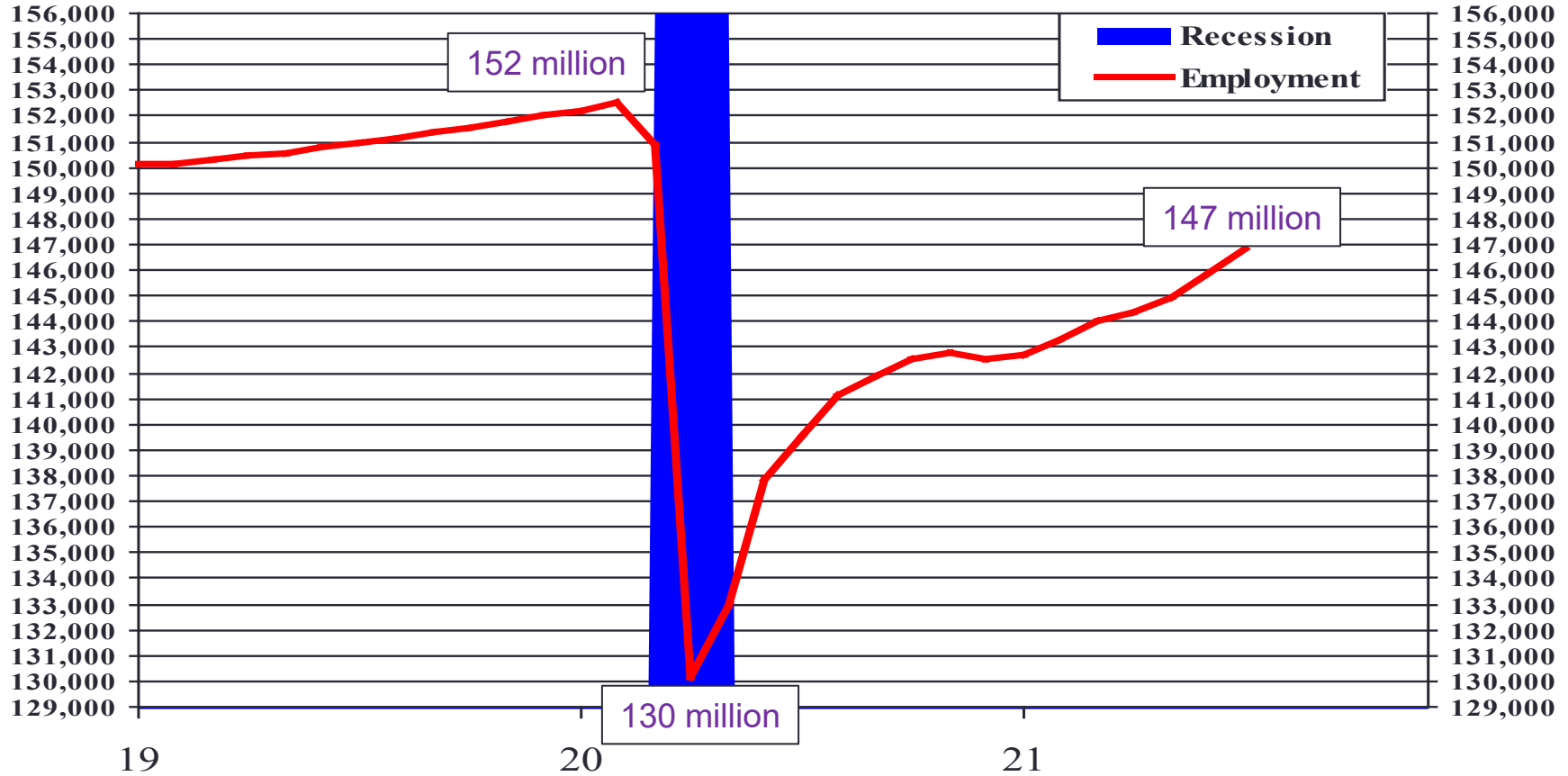
1. Pent up demand for goods and services
2. Rising energy & commodity prices
3. Massive monetary and fiscal stimulus
4. Lower dollar exchange rate => import prices
5. Rising housing and medical care costs
6. Rising Inflation Expectations

## Lower Inflation Factors:

1. eCommerce is a powerful deflationary force
2. Rising competition from globalization
3. Rising productivity => falling costs per unit
4. Low population growth
5. Negative output gap and excess production capacity
6. Excess supply of labor

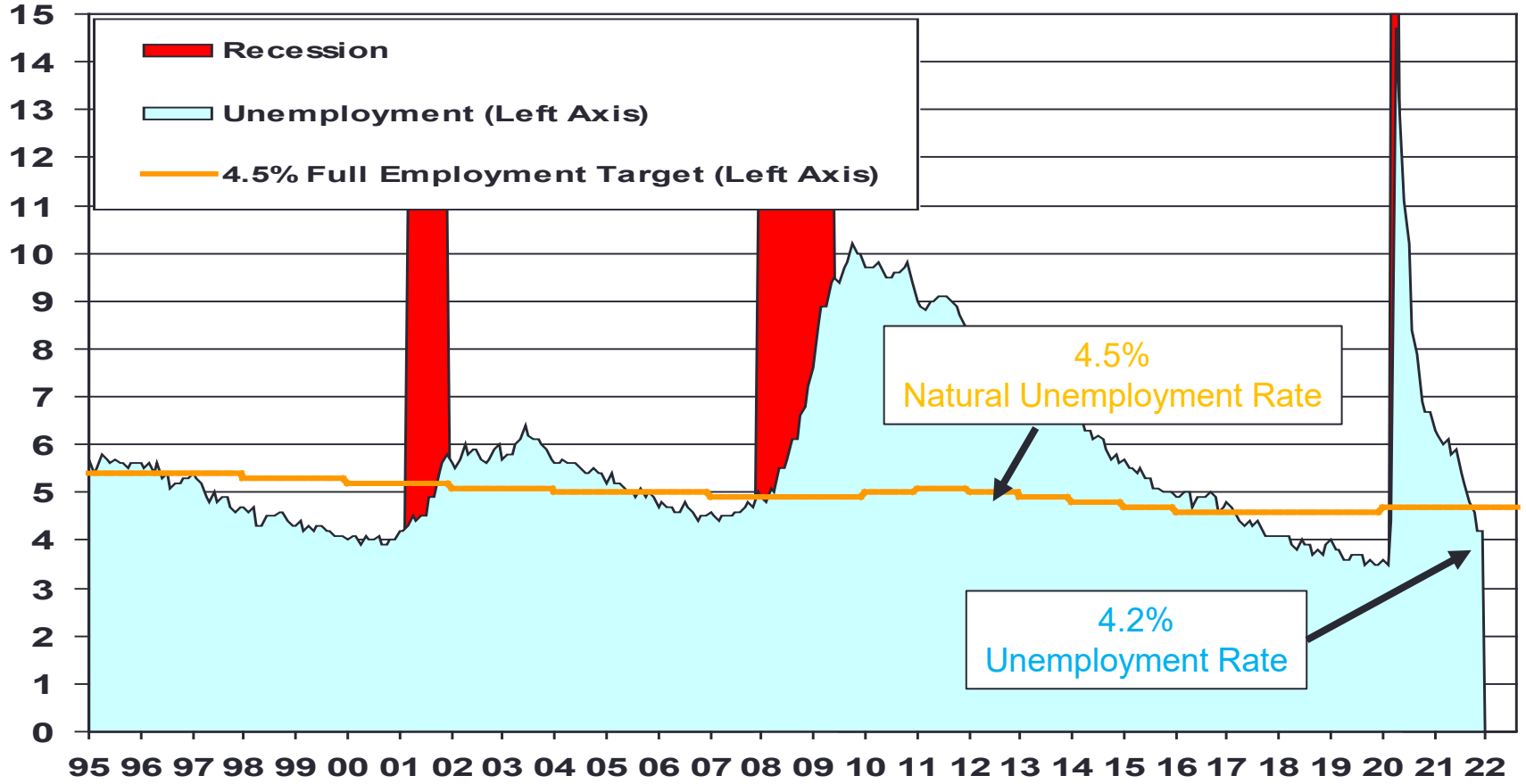
# 5 million Few Americans Working Today Compared to February 2020's 152.5 million

## Total Nonfarm Employment (Thousands, SA)



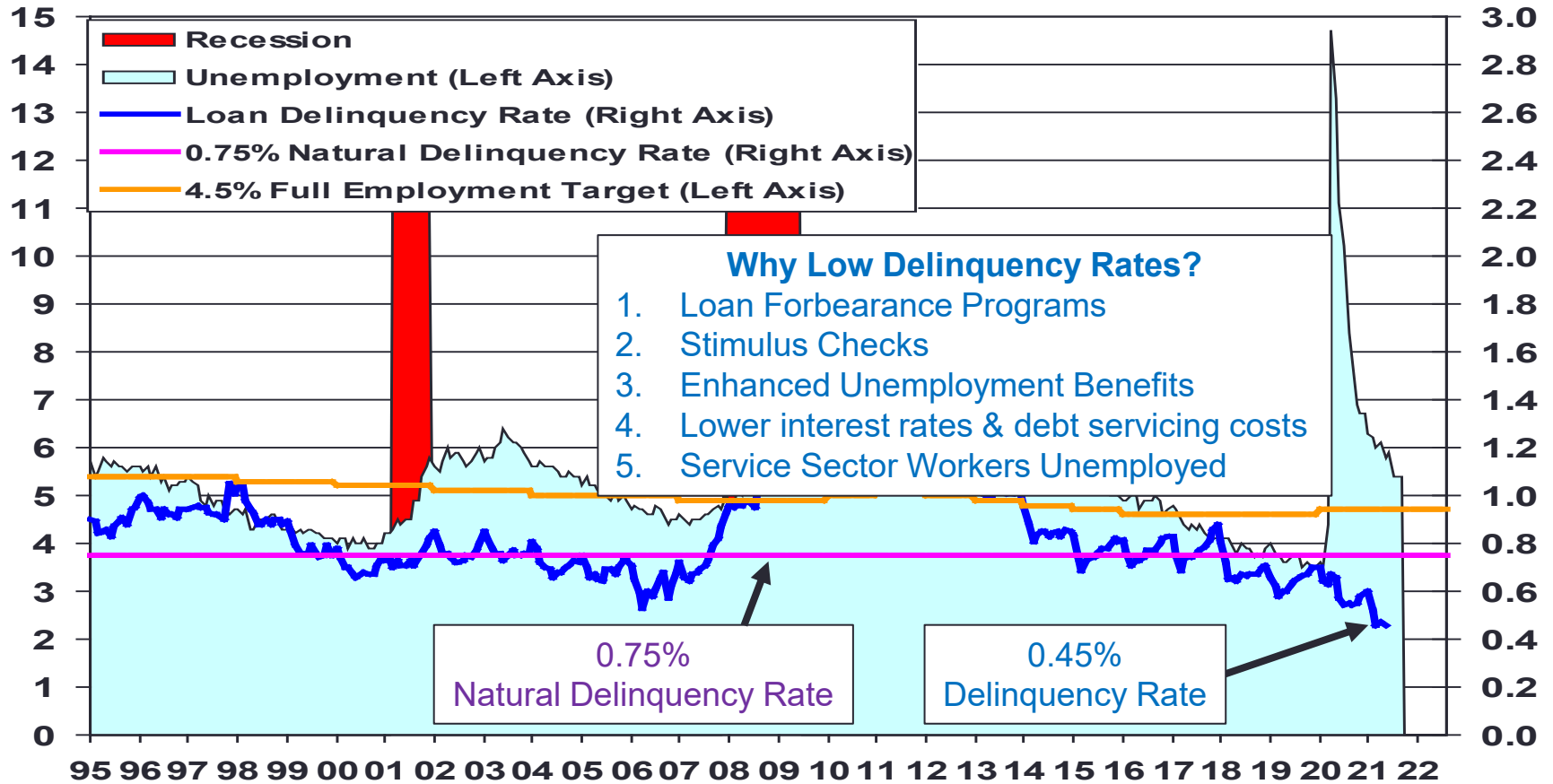
# Unemployment Rate Below Natural Unemployment Rate

## CU Delinquency Rate Versus Unemployment Rate



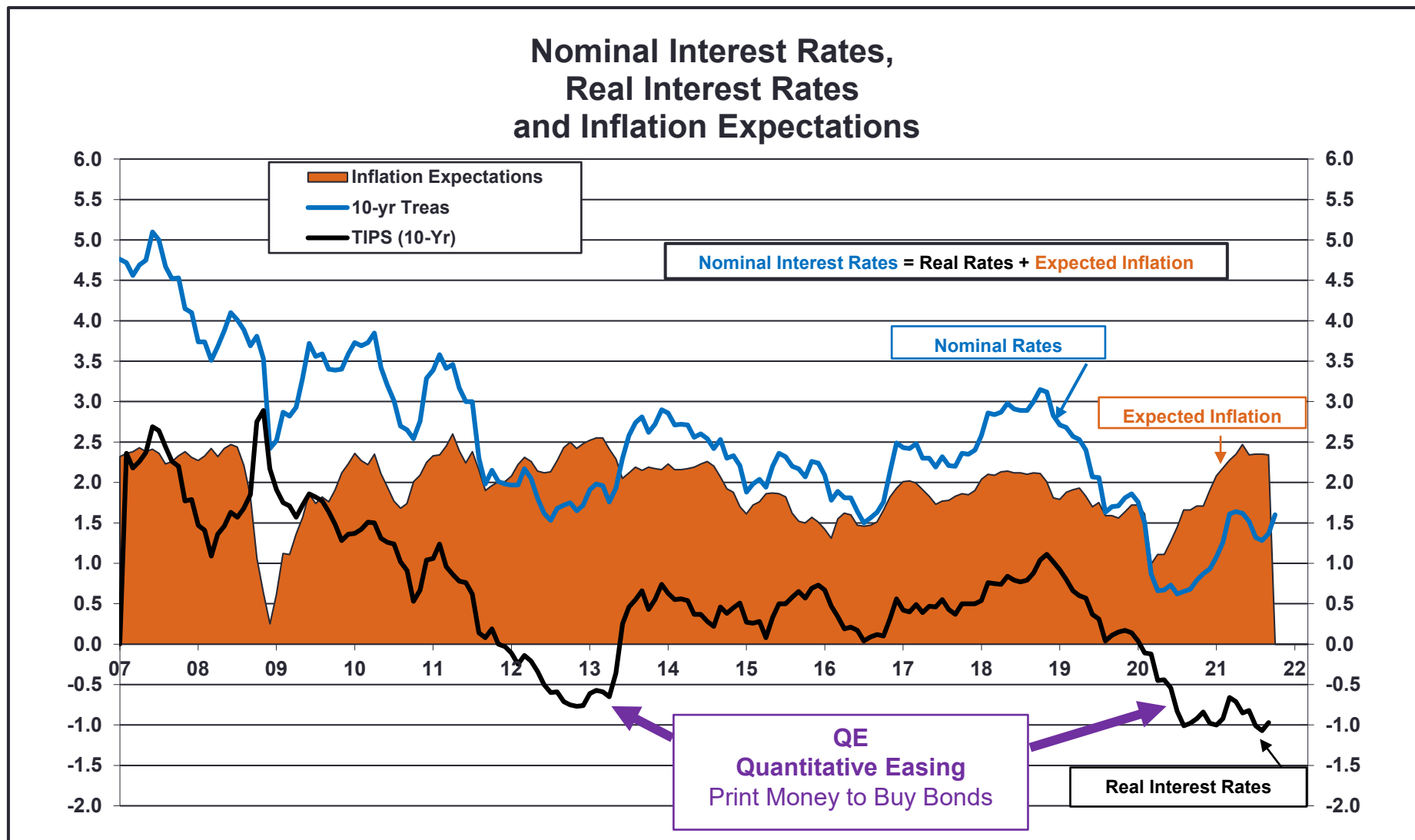
# CU Loan Delinquency Rates at Record Lows

## CU Delinquency Rate Versus Unemployment Rate



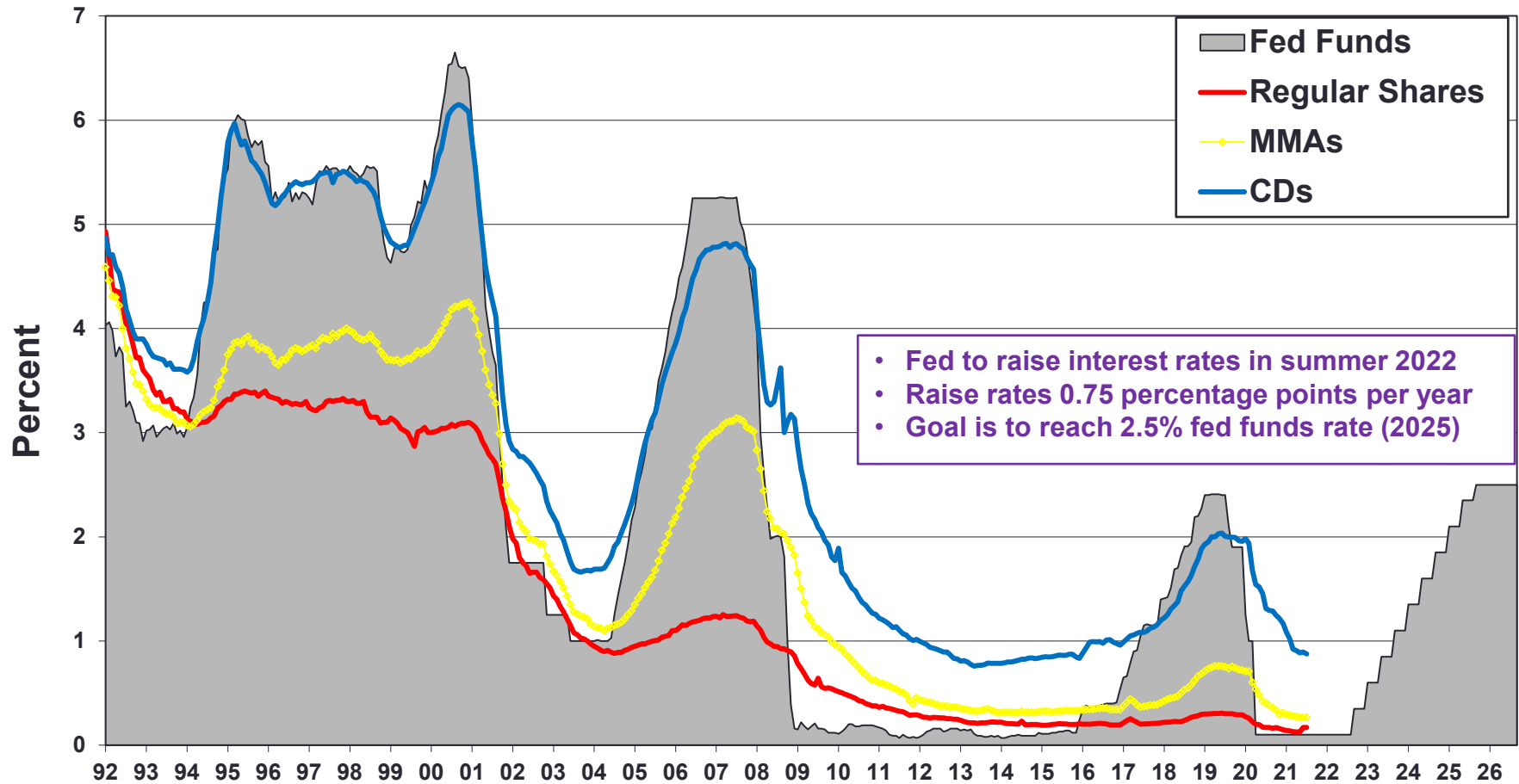


# Rising Real Interest Rates, and Rising Inflation Expectations are Pushing Up Nominal Interest Rates

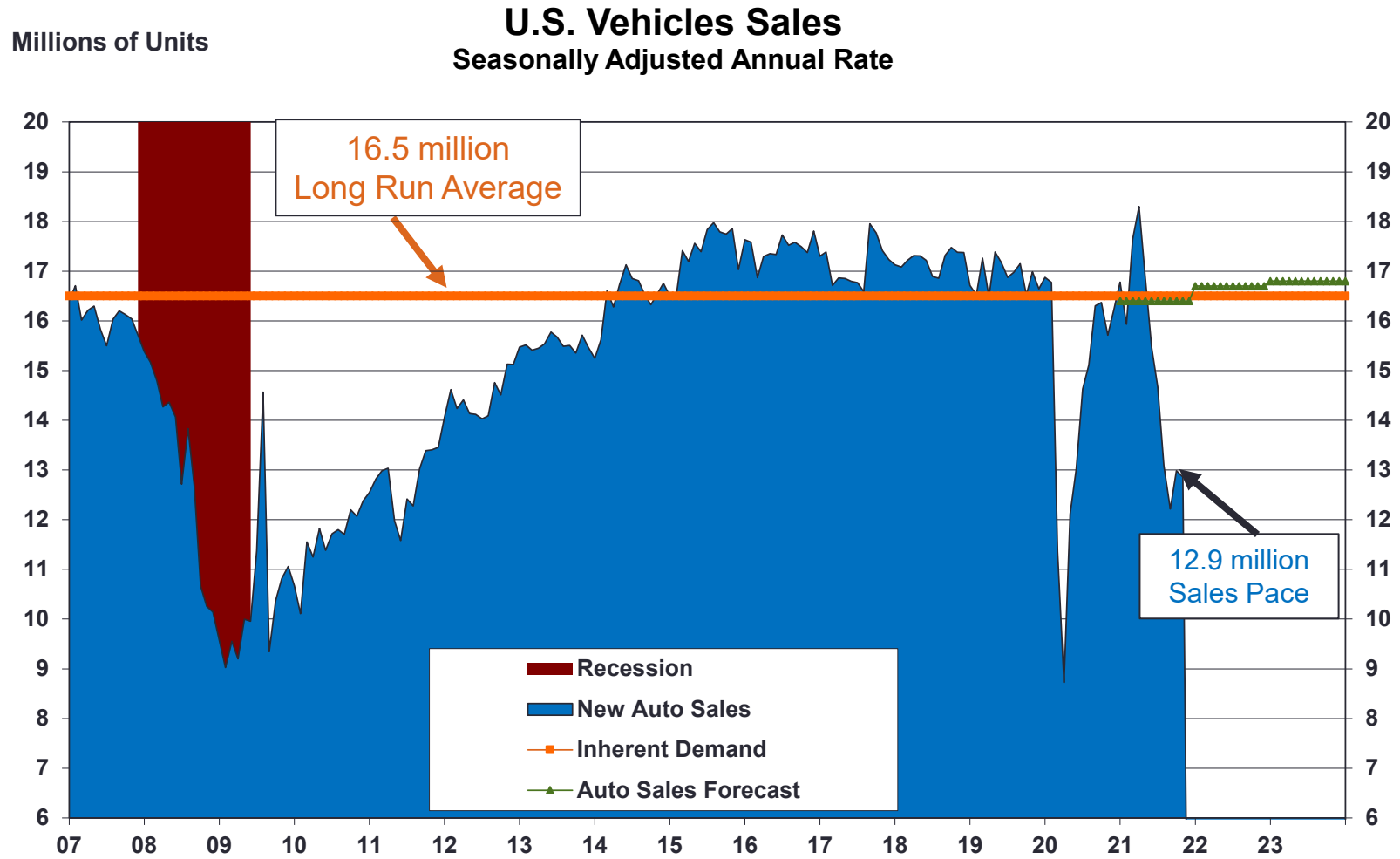


# Falling Deposit Pricing and Low Fed Funds Interest Rate

## Deposit Interest Rates versus Fed Funds

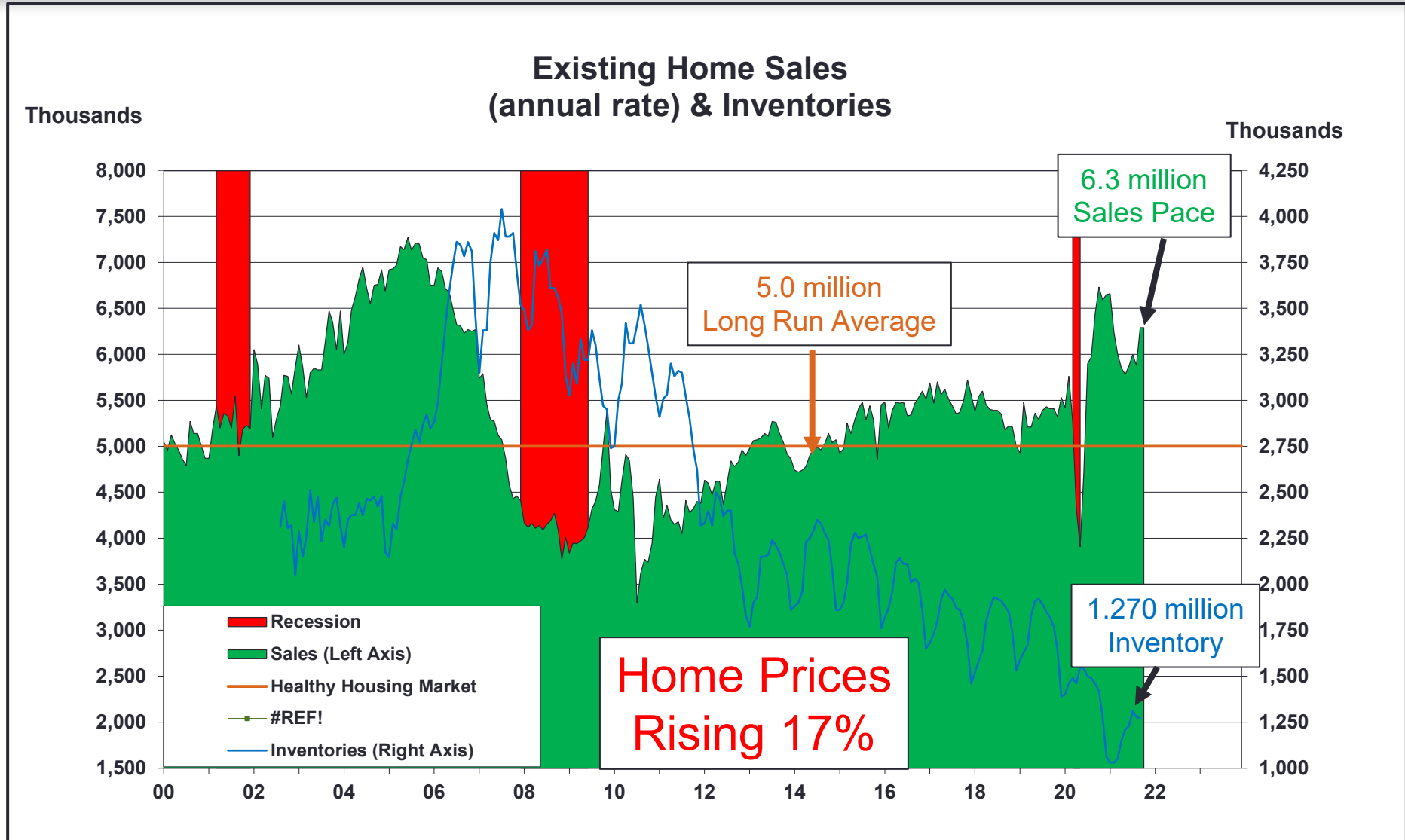


# Falling Auto Sales Below Long-term Trend

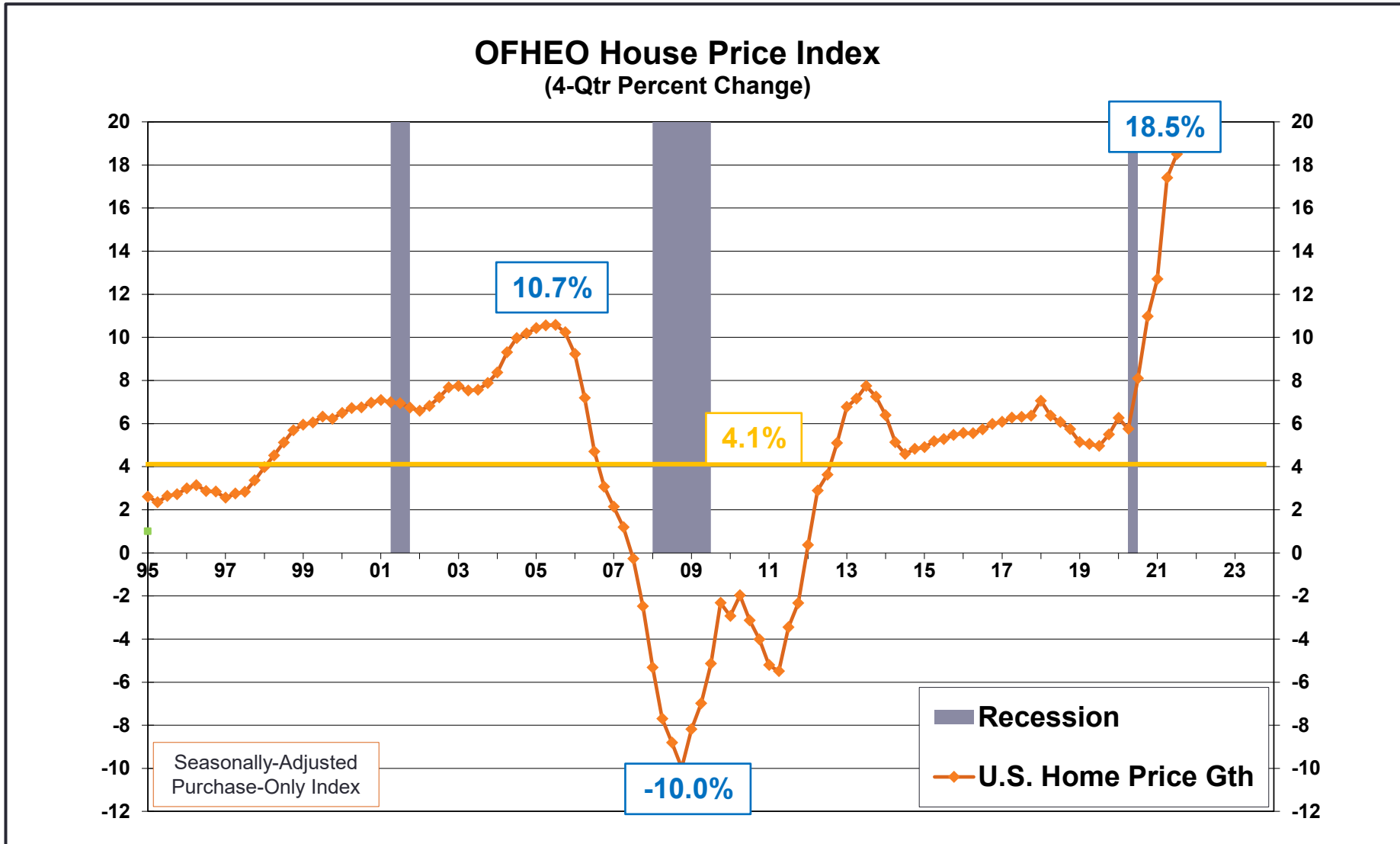


Source: Autodata Corp.

# Home Sales are Strong, but Inventories are Low

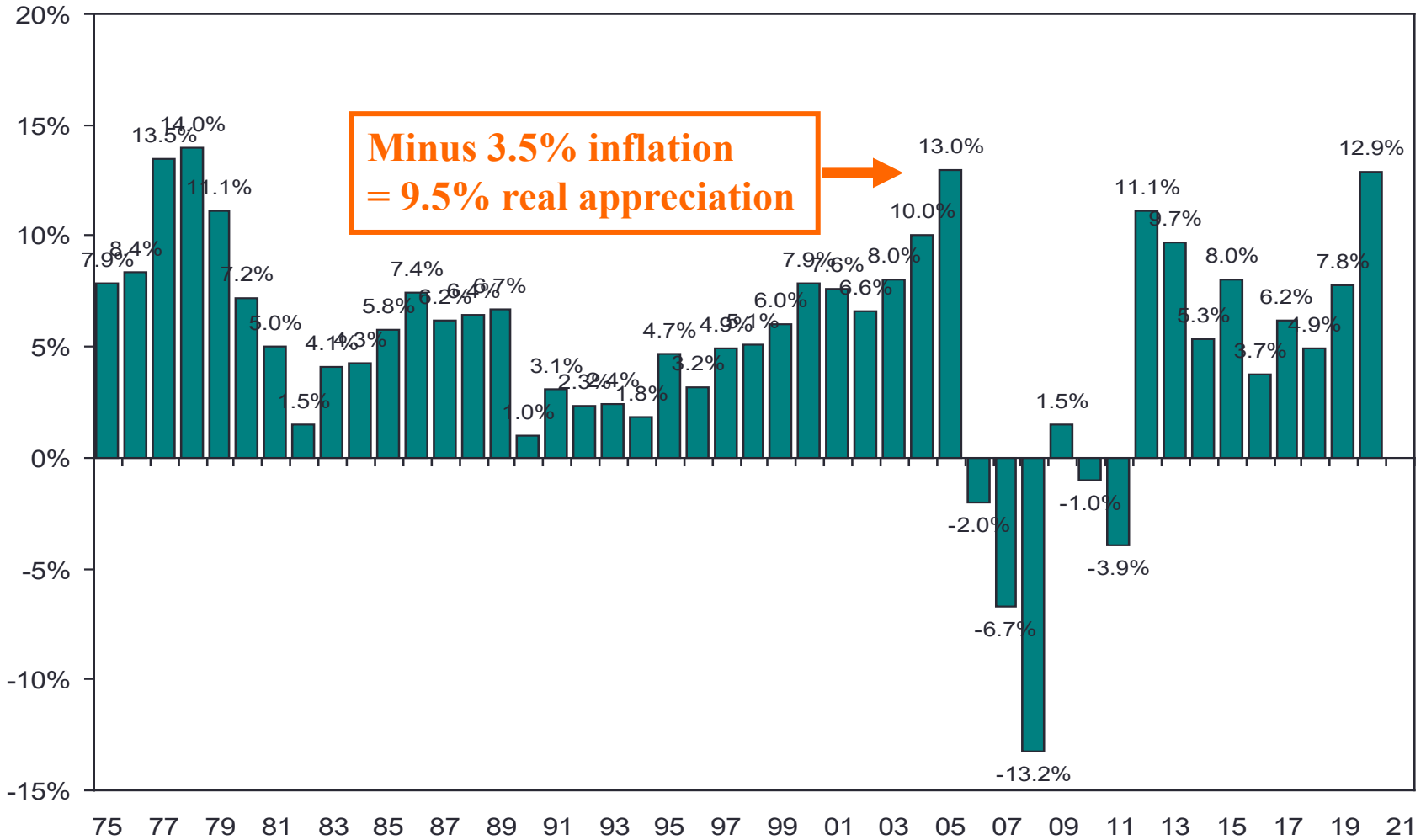


# Faster Home Price Growth Rates will Boost Household Wealth and Consumer Spending



# Median Existing Home Prices

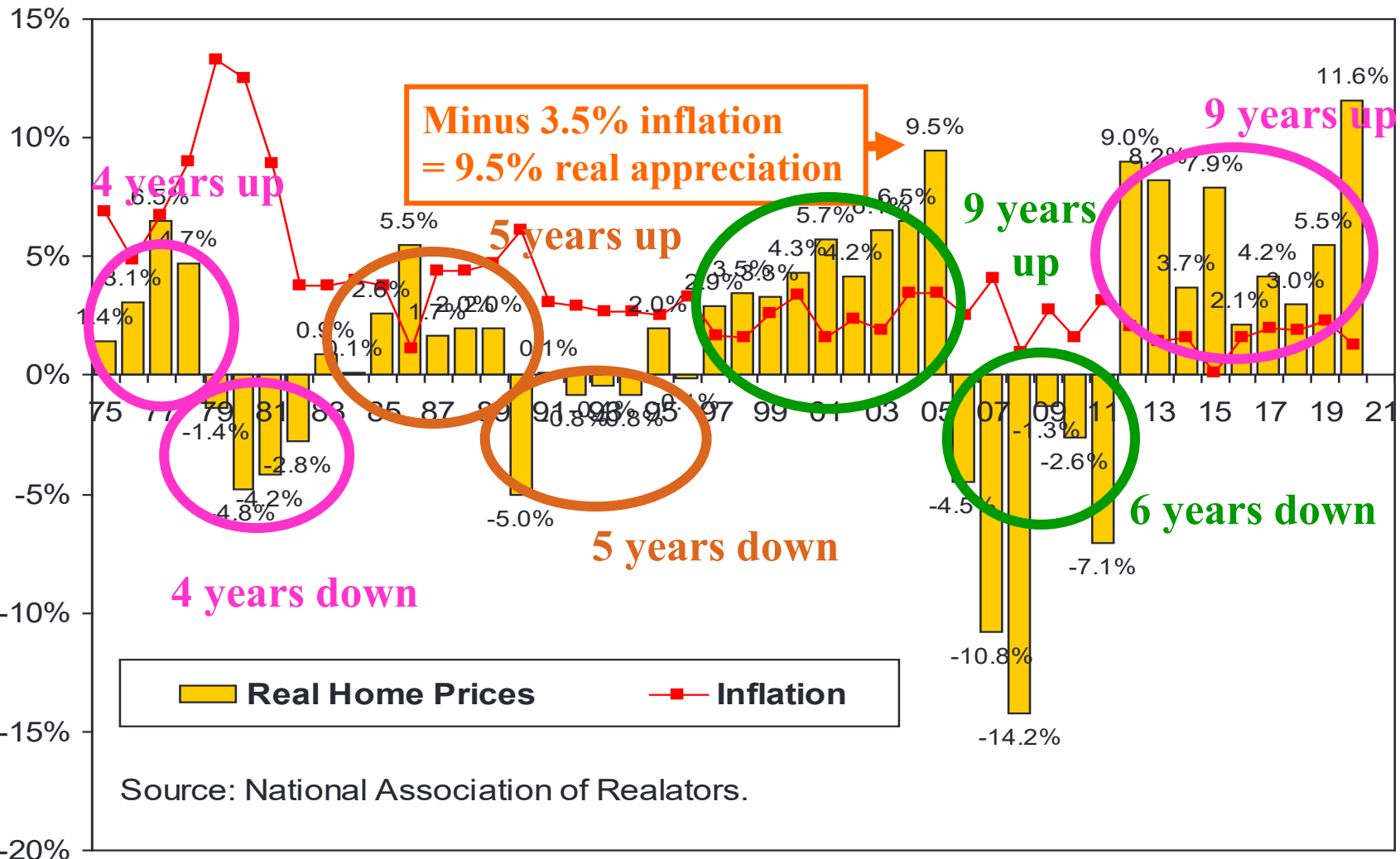
## (Nominal Annual Home Price Increases)



Source: National Association of Realtors.

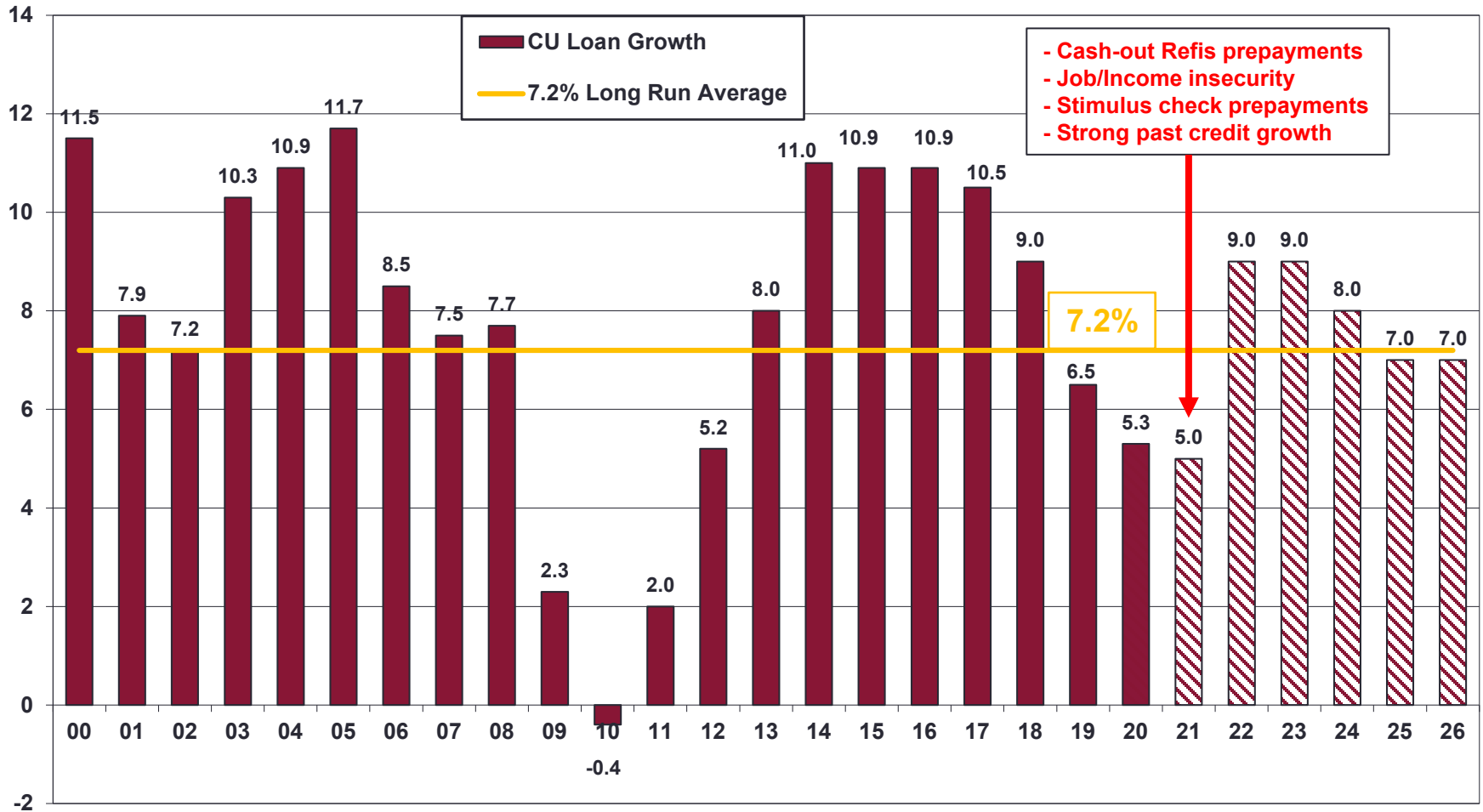
# The Housing Cycle

## (Inflation-Adjusted Annual Home Price Increases)



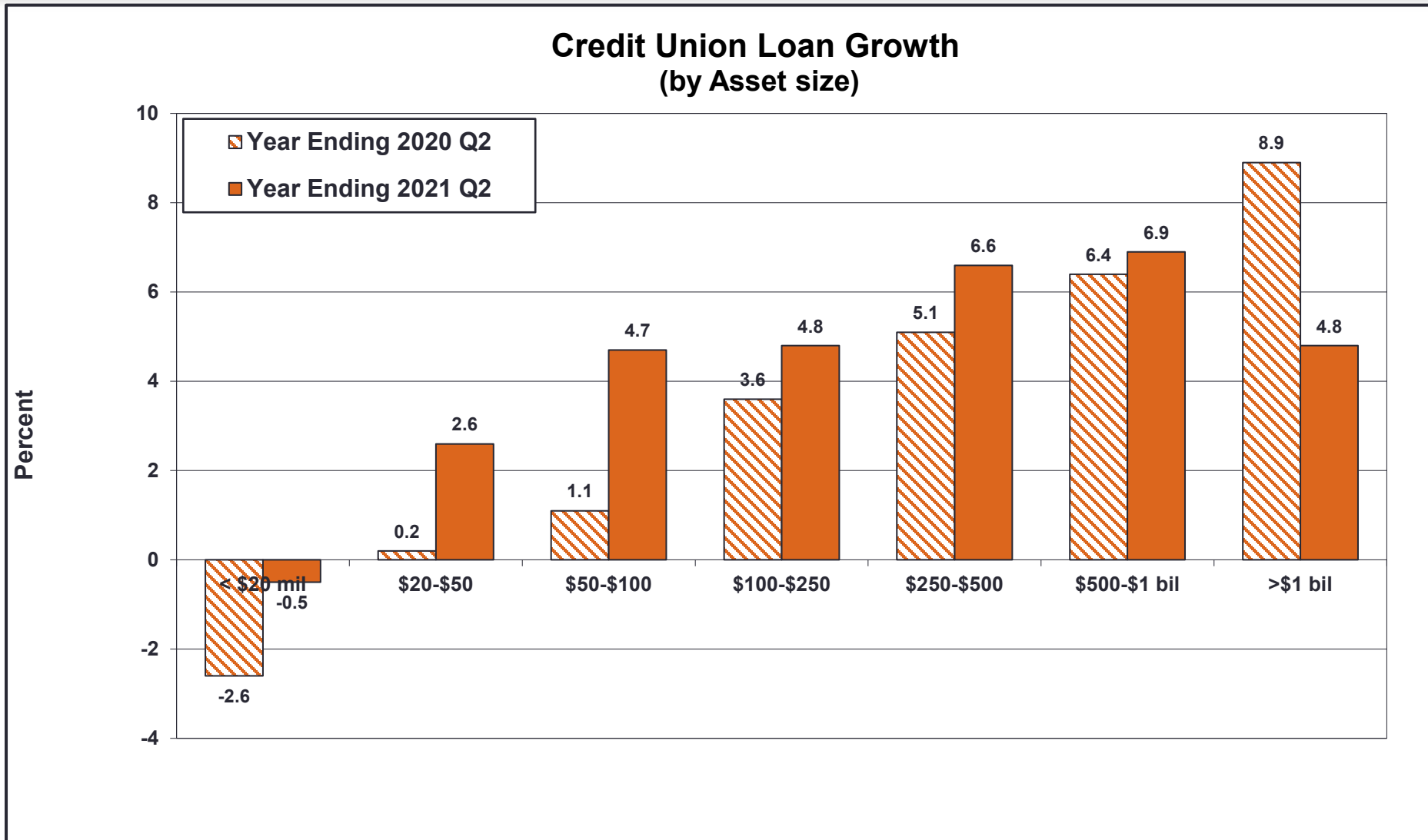
# Above Trend Credit Union Loan Growth

**Credit Union Loan Growth**  
(Annual Percent Growth)



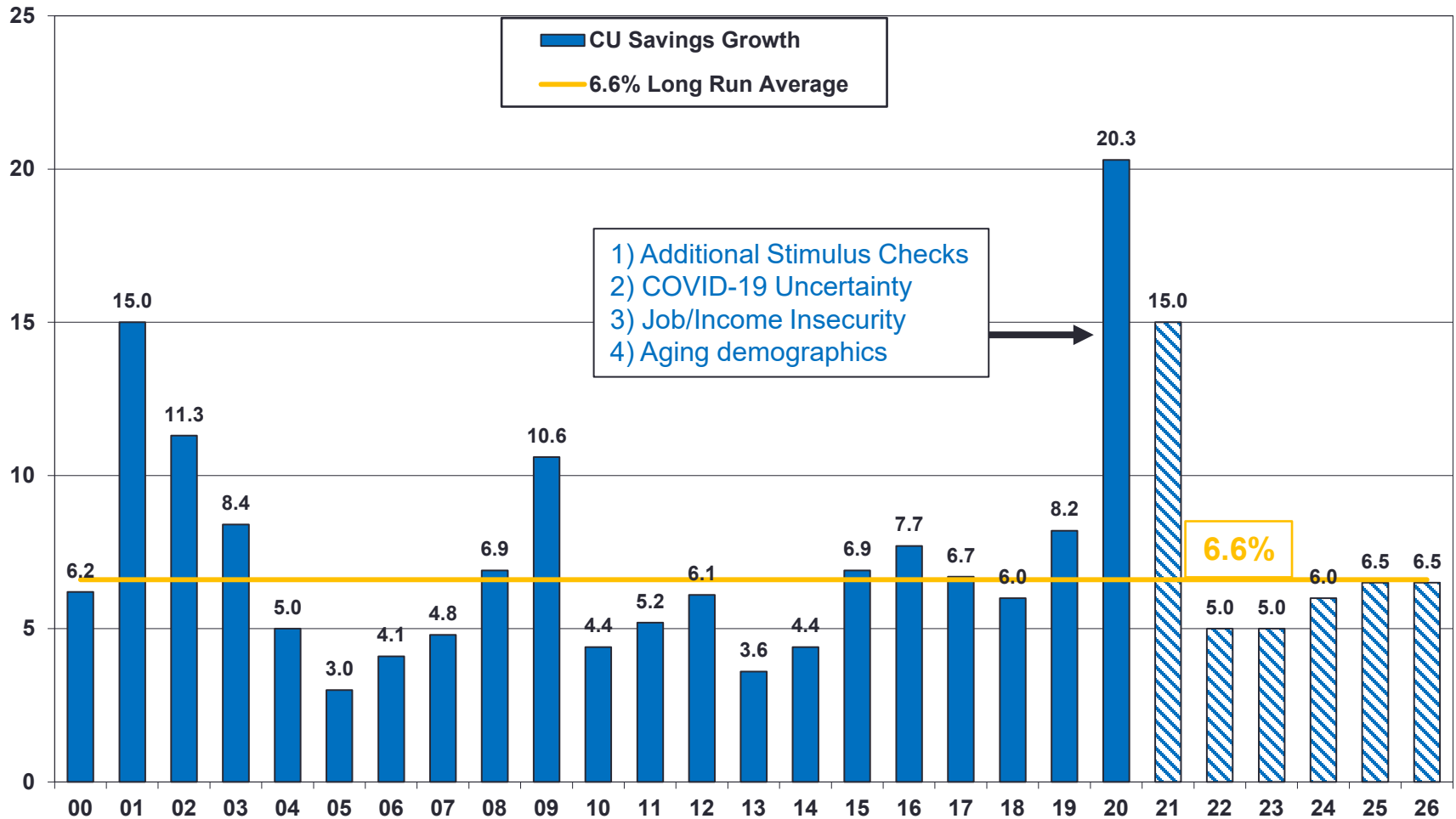


# 9% Credit Union Loan Growth in 2022

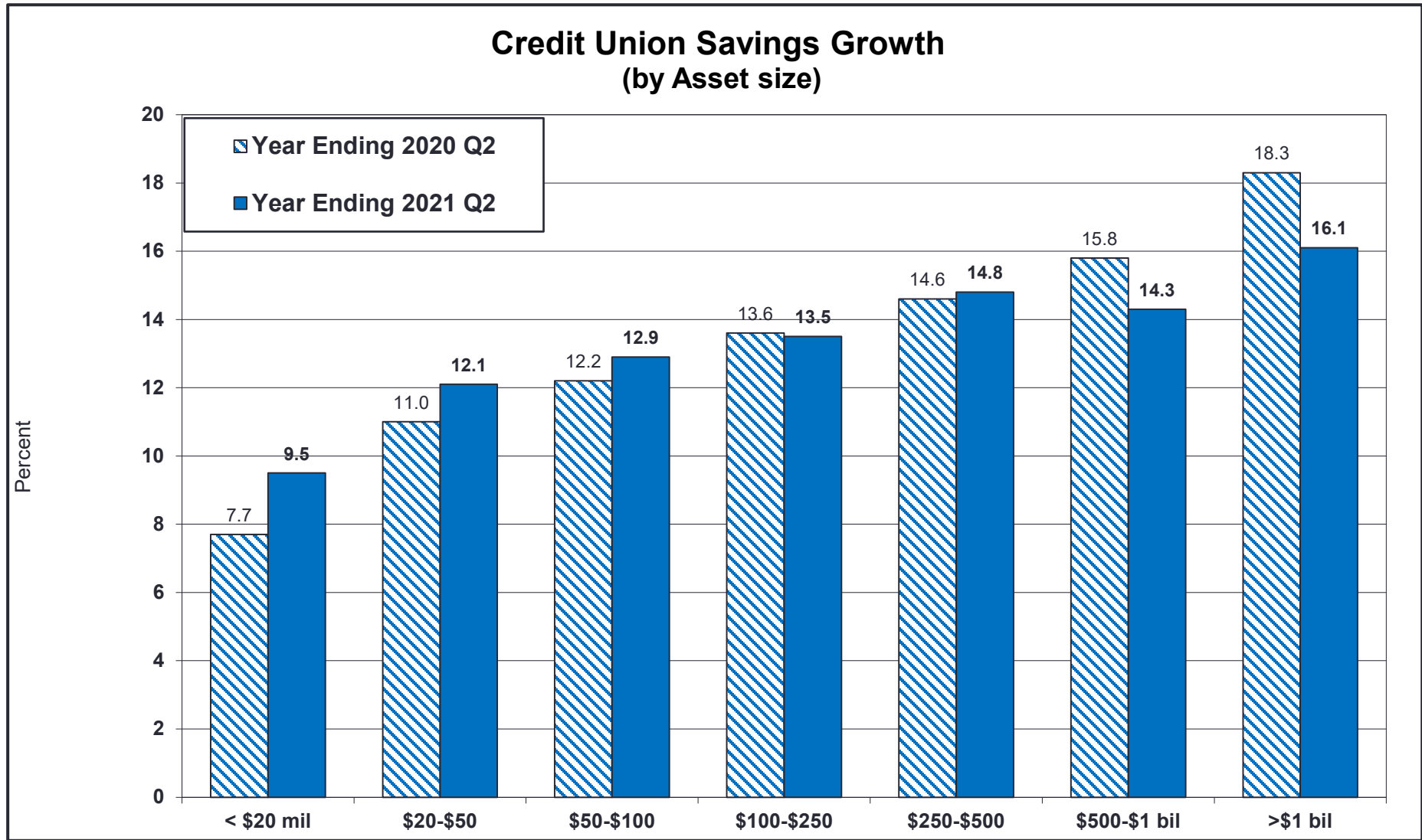


# Below Trend Credit Union Saving Growth

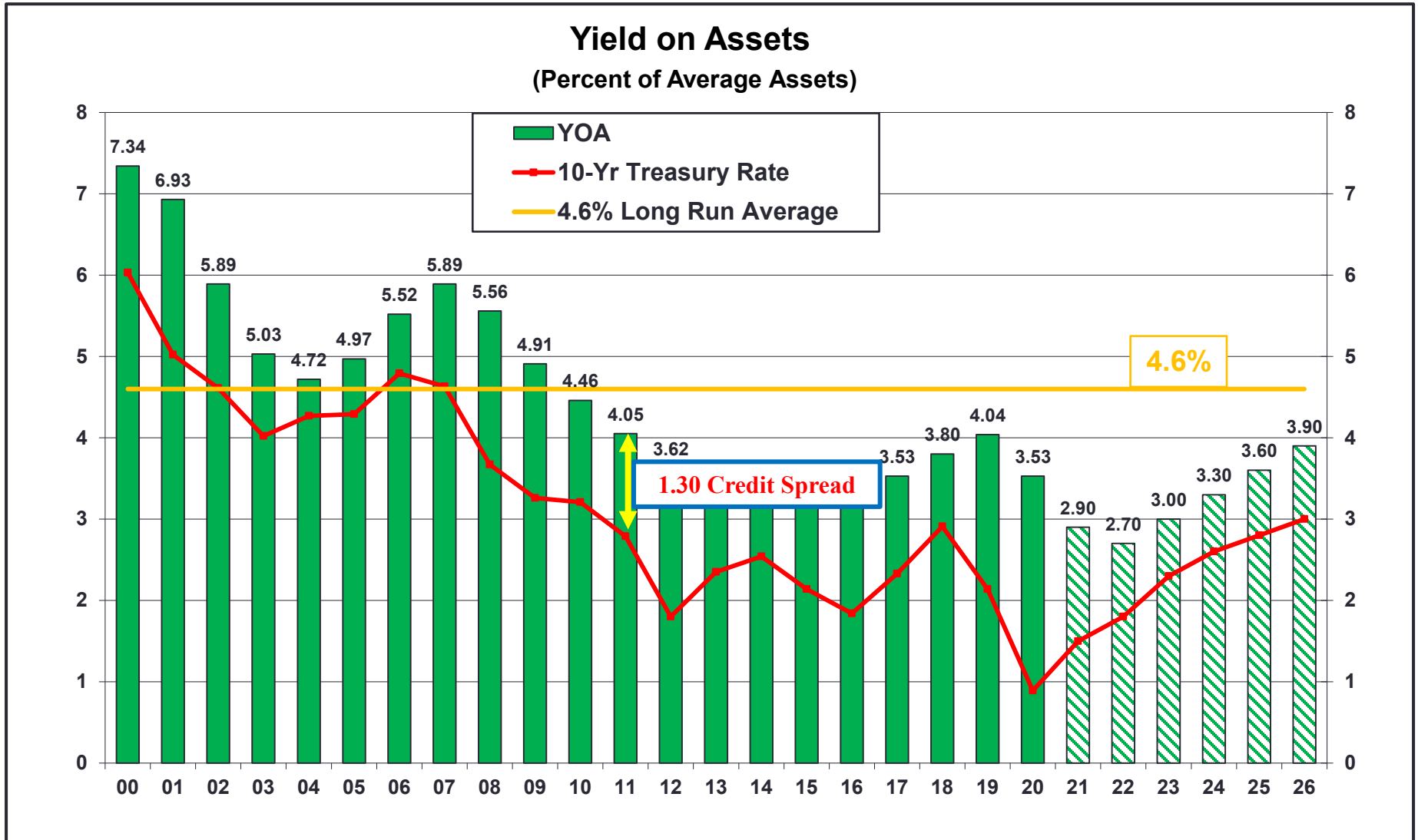
**Credit Union Savings Growth**  
(Annual Percent Growth)



# 5% Credit Union Saving Growth in 2022

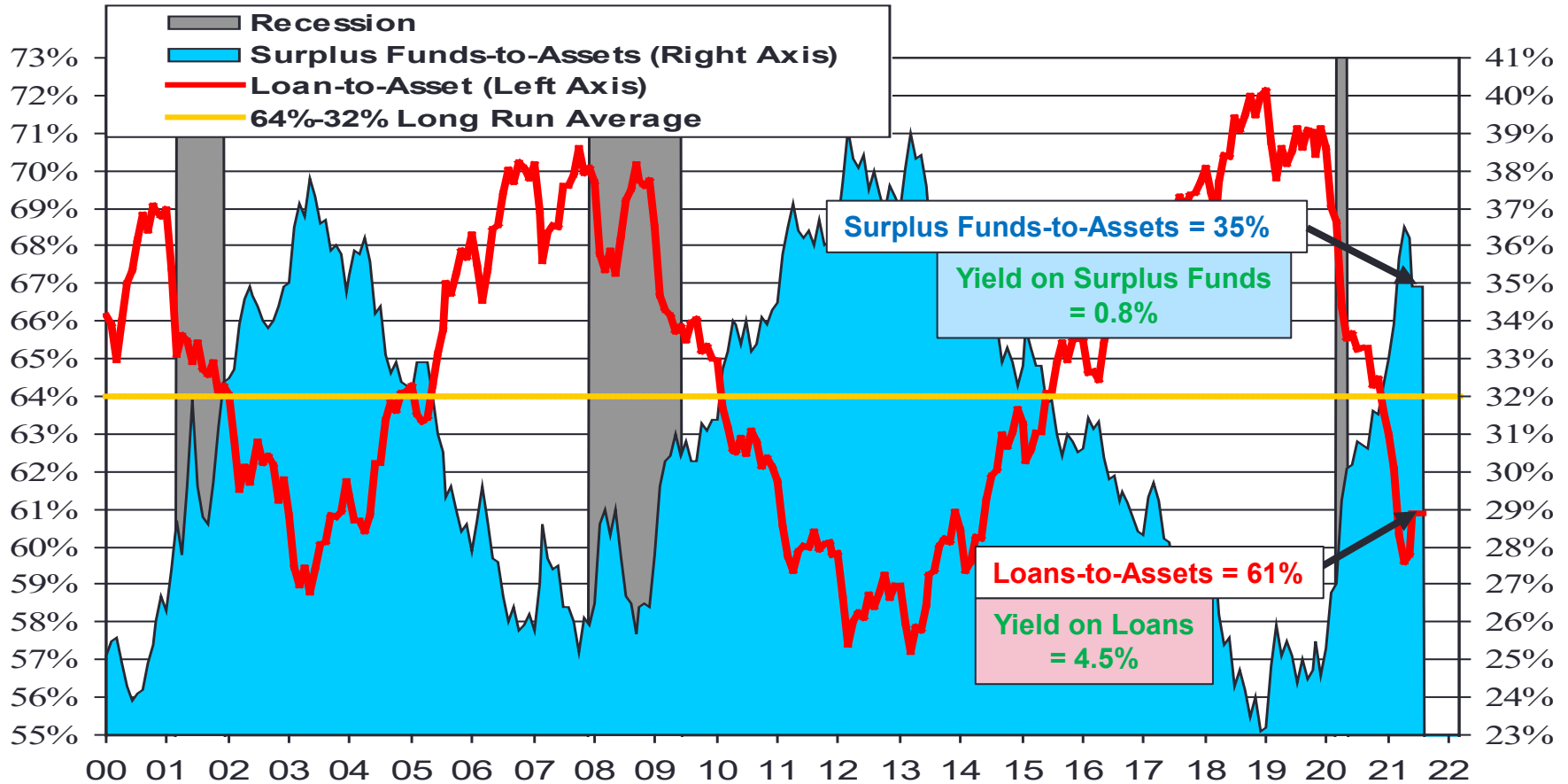


# Yield-on-Assets Falling to Record Lows in 2022

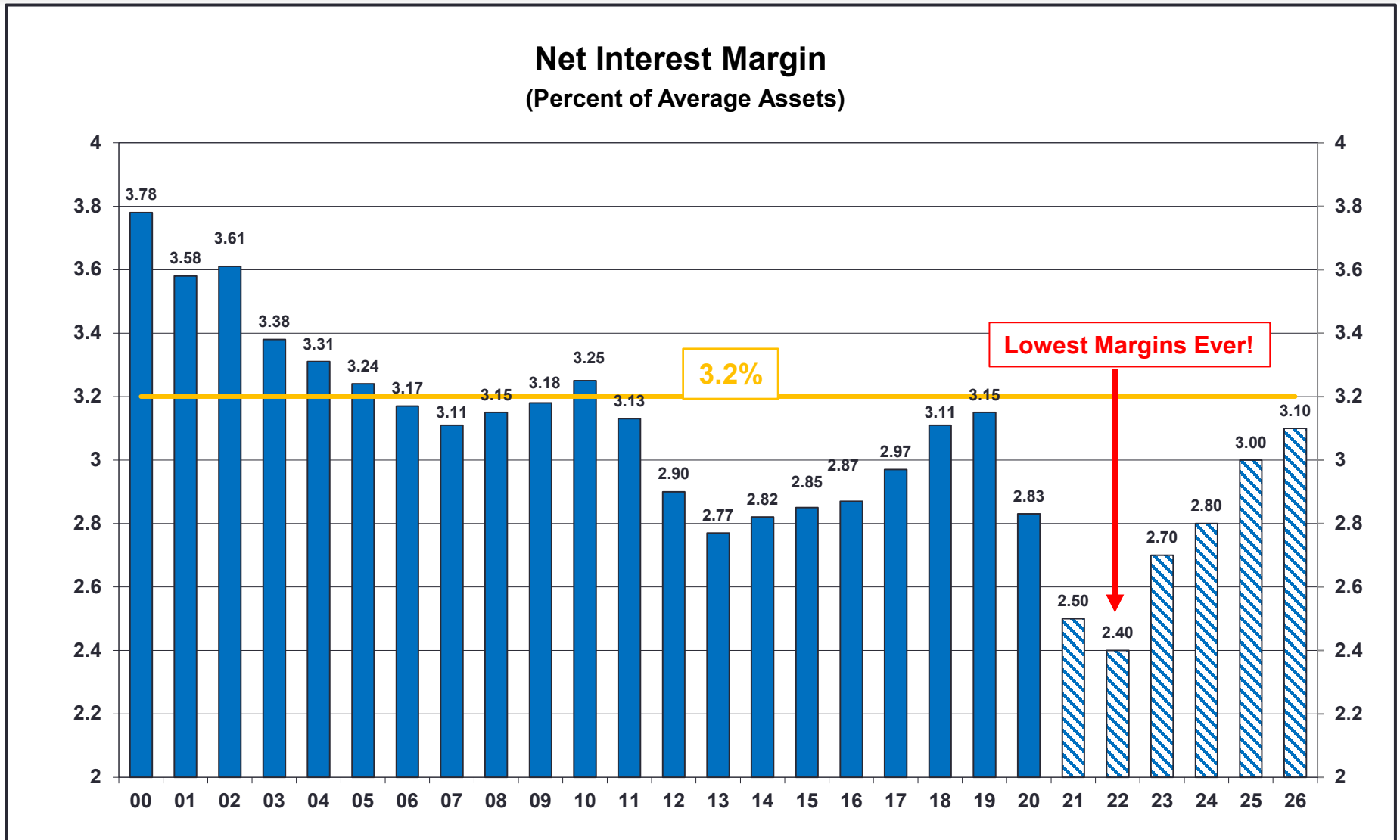


# Investments Are Rising and Yields Are Falling

## CU Surplus Funds (Cash + Investments)

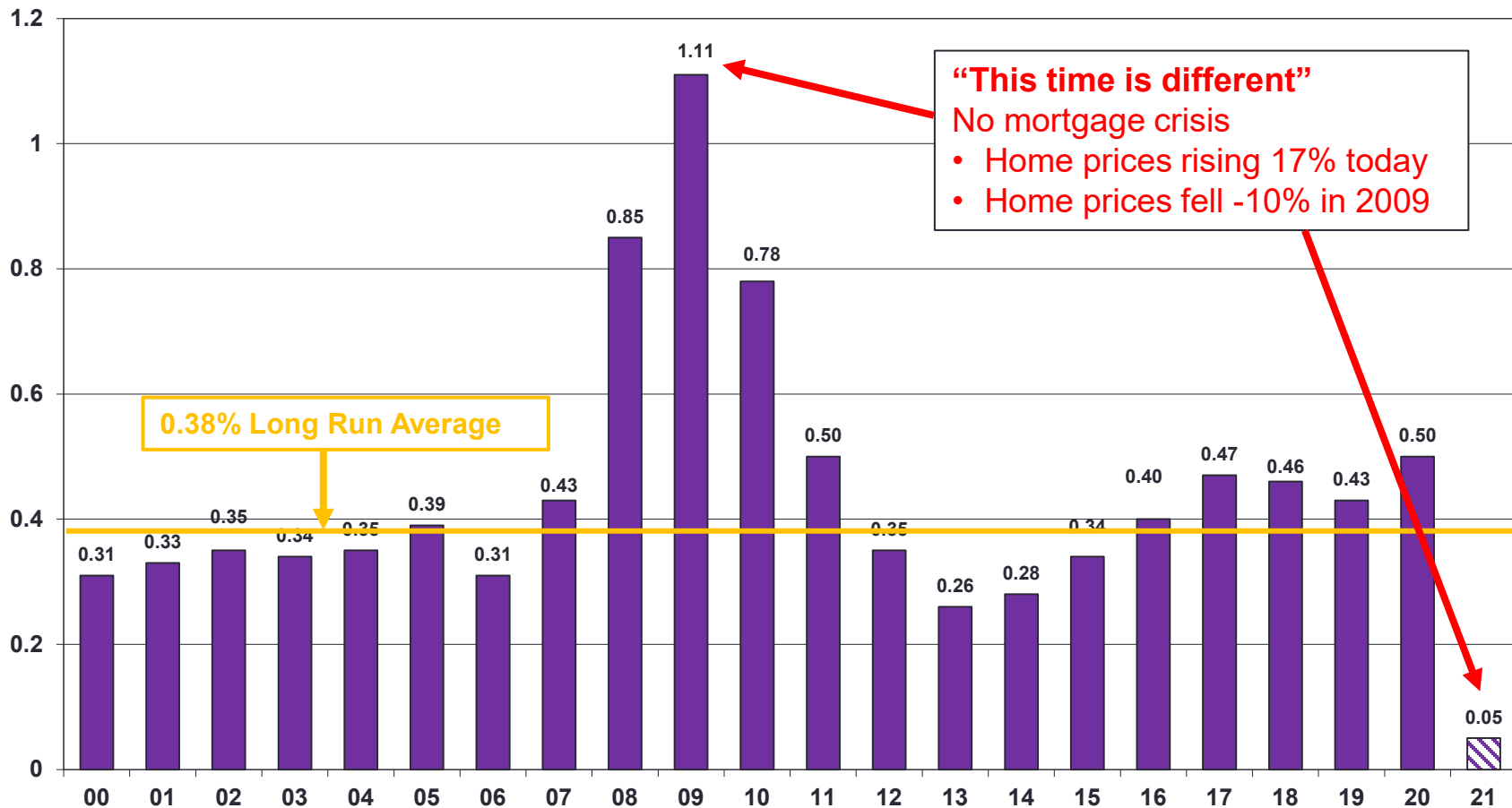


# Net Interest Margins will Fall to Record Lows in 2022

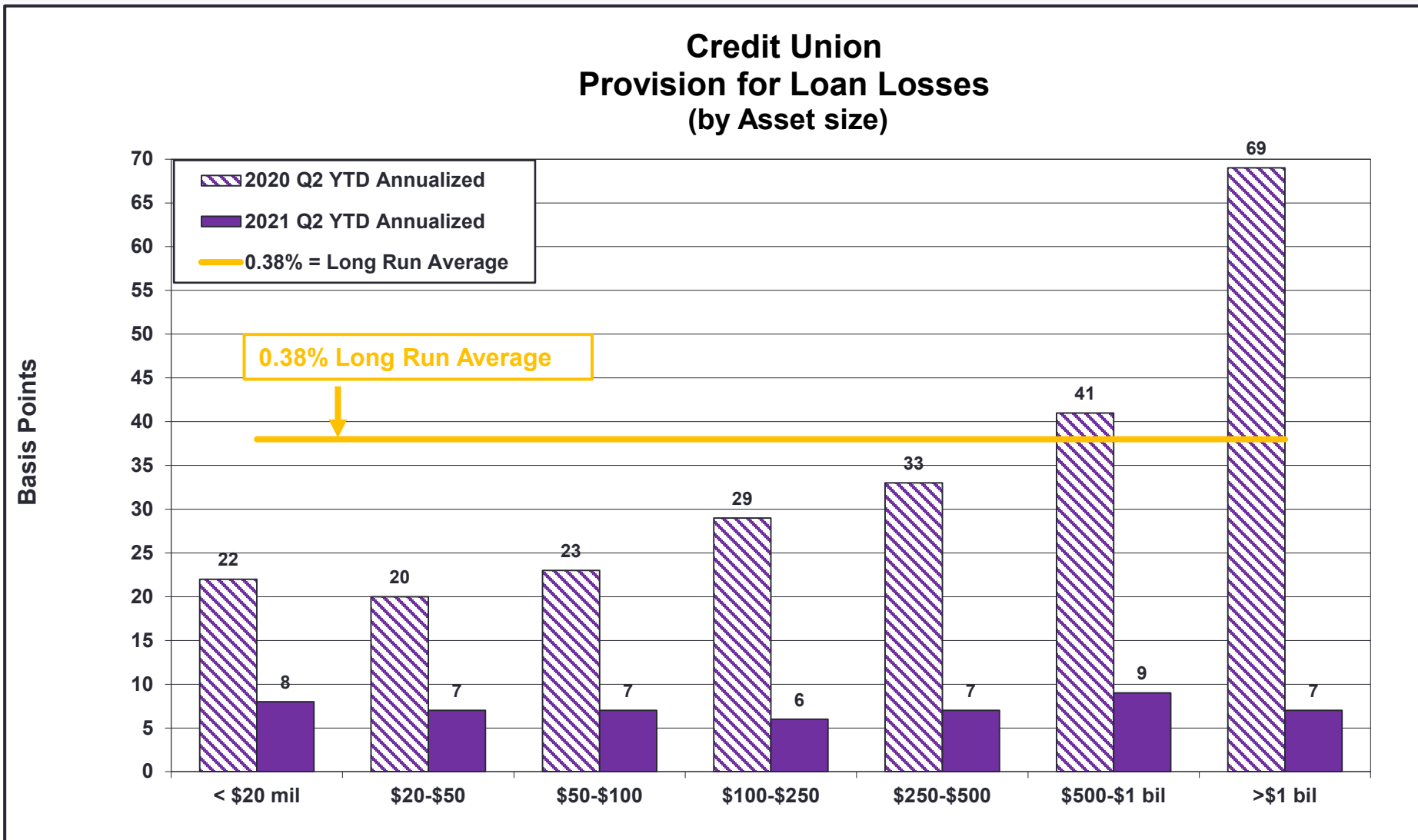


# Falling Provisions for Loan Loss Ratios

Provision for Loan Losses  
(Percent of Average Assets)

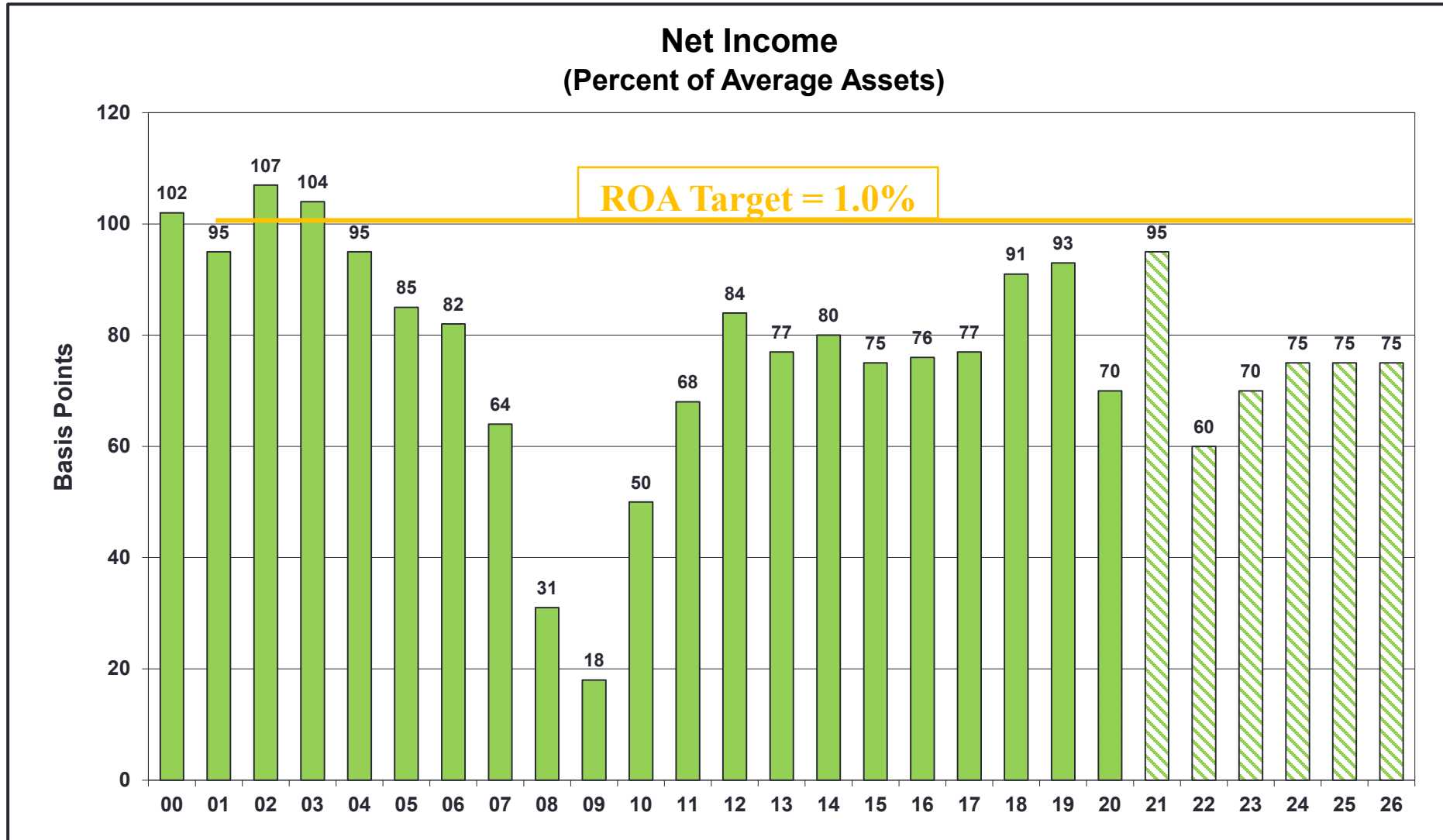


# Falling Provisions for Loan Loss Ratios



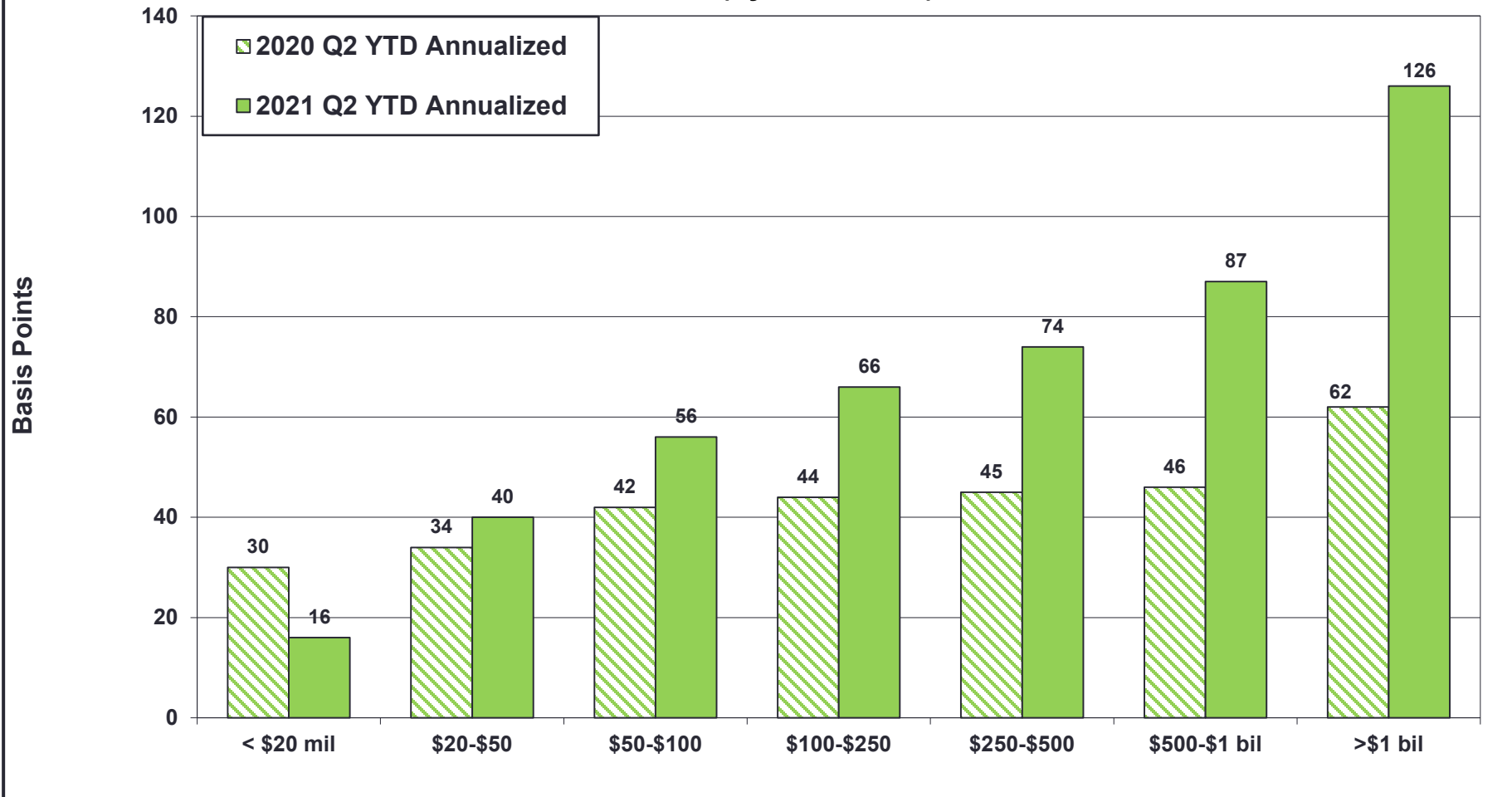


# Credit Union Earnings Below Trend



# Rising Return-on-Asset Ratios

Credit Union Return on Assets  
(by Asset size)



# Economic Update Summary

## 2021-2022

1. Very strong economic growth for the next 2 years
2. Long-term interest rates rising 1 percentage point over the next 2 years
3. Unemployment rate falling below normal by end of 2022
4. Low credit union loan growth in 2021, rebounding in 2022
5. Record low net interest margins in 2021 & 2022

# Top 10 CU Issues For 2021

1. Record low net interest margins will lead to expense containment
2. Monitor employee stress and morale during pandemic
3. Update business activity expectations and reallocate staff
4. The new economic environment will create new path for profitability
5. Opportunities for prime real estate purchases and future branching
6. Adopt COVID-19 related design changes for old and new buildings
7. Excess liquidity will intensify search for higher yielding assets
8. Monitor closely the drop in capital-to-asset ratios
9. Focus on serving financially stressed members will build brand loyalty
10. Plan for post recession opportunities

# 5-Year Strategic Plan Focus Areas

## (How the Pandemic May Change Financial Institutions)

FOCUS AREAS	Temporary vs Permanent (1-3)	Impact to Credit Union (1-3)	Management Focus (1-3)	Freak-out Score (Multiply previous 3 numbers together)
Low Market Interest Rates				
Low Net Interest Margins				
Weaker Consumer Finances (higher loan chargeoffs & weaker loan demand)				
Digital Acceleration				
Less Face-to-Face Product Delivery and Less Branching				
Lower Capital Ratios				
Consumers Saving More of their Income				
Rising Health Insurance Costs and Premiums				
COVID-19 Building Design Changes				
More Remote & Less Onsite Staffing				
Loss of Tax-Exempt Status				
Market Expansion/Membership Growth				

# Economic Forecast

- **Economic Growth:** The Real gross domestic product has increased by [6.3% and 6.6%](#) in the first and second quarter of the year, respectively according to data from the Bureau of Economic Analysis (BEA). This growth not only recovered what was lost in economic output because of shutdowns but also exceeded the peak level of output prior to the pandemic. [Increases](#) in consumer spending, nonresidential fixed investment, exports, and local government spending drove this impressive growth. Nonetheless, the rise in delta Covid variant since July has cooled off the momentum. Consumer sentiment index registered a monthly steep decline of 13% in August to 70.3 – the lowest level in a decade. CUNA Economists forecast the economy will grow at 6% in 2021 – strong growth rate in several decades – and 4.5% in 2022.
- **Unemployment:** [The Bureau of Labor statistics](#) reported a job growth of 235,000 for the month of August which is much smaller than the [anticipated](#) 700K+. After a strong job's report of about a million per month in June and July, August was also expected to perform well considering the resumption of in-person school instruction for the fall and the expiration of additional federal unemployment benefit in September. Decline in employment in retail and no additions in leisure and hospitality in August shows that delta is weighing heavily on the labor market. The expiration of Federal supplemental unemployment benefit may lead to increased labor force participation that remain unchanged through most of the pandemic. This coupled with fear of the virus may keep the unemployment rate from declining as needed despite modest job growth in the coming months. CUNA Economists expect unemployment will fall to 4.8% by the end of 2021 and to 4% by 2022.
- **Inflation:** consumer prices have increased since March following a strong consumer demand and economic growth. The August [consumer price index](#) report shows that prices are 5.3% higher compared to last year. However, the monthly price increase has slowed to 0.3% after five consecutive months of large increases above 0.5%. Federal Reserve chairman Jerome Powell argues that factors that push the inflation rate higher are [temporary](#) caused by rapid reopening of the economy and imbalances in supply and demand. On the other hand, survey of consumer expectations published in August by the [Federal reserve Bank of New York](#) shows that the short –and –medium term inflation expectations rose to series highs of 5.2% and 4.0%. CUNA Economists expect the inflationary pressures to start slowing down in the third and fourth quarter of 2021. They forecast the headline consumer Price index to increase to 5.5% in 2021 and fall to 2.5% in 2022.
- **Interest Rates:** Federal reserve chair Jerome Powell has announced recently that it is important to monitor incoming data on inflation and employment before making changes to [monetary policy](#) that impacts interest rates. Long term inflation expectation is consistent with the 2% Fed's target; hence policy should look through temporary changes in inflation according to Powell. As a result, CUNA economists see no change in the forecast for effective federal funds rate in 2021 and 2022 compared to previous forecast. The consensus is that it will start to go up in early 2023 but if the economic condition is stronger than what we have put together in this forecast, it may go up in late 2022. Credit Unions should continue to monitor this closely. The 10-year treasury is expected to reach 1.5% by the end of 2021 and go up to 2% in 2022.

# Economic Forecast – September 2021

	Actual Results		Quarterly Results/Forecasts				Annual Forecasts	
	5 Year Average	2020	2021:1	2021:2	2021:3	2021:4	2021	2022
<b>Growth Rates:</b>								
Economic Growth (% Change GDP)*	1.1%	-3.5%	6.4%	6.6%	4.5%	6.0%	6.5%	4.5%
Inflation (% Change CPI)*	1.9%	1.3%	4.9%	9.3%	5.0%	2.5%	5.0%	2.5%
Unemployment Rate	4.6%	6.7%	6.0%	5.9%	5.2%	4.8%	4.8%	4.0%
Federal Funds Rate (effective)	1.18%	0.09%	0.07%	0.08%	0.10%	0.10%	0.09%	0.10%
10-Year Treasury Rate	2.08%	0.93%	1.74%	1.45%	1.40%	1.50%	1.50%	2.50%
10-Year-Fed Funds Spread	0.90%	0.84%	1.66%	1.37%	1.30%	1.40%	1.41%	1.90%

\*Percent change, annual rate.  
All other numbers are end of period values.

# Credit Union Forecast

- **Loan & Membership Growth:** Quarterly NCUA report shows that Credit union loan portfolio grew 2.5% in the second quarter. This growth rate is consistent with the long run trend we observe for a second quarter. Memberships grew 1.3% following another robust performance of 1.2% in the first quarter. Strong economic growth of the previous two quarters and consumer spending contributed to these increase. CUNA economists expect loan and memberships to grow at 6% and 3.4%, respectively by the end of the year. In 2022, loan growth is expected to converge to its long run average of 9% as the economy fully recovers from the effects the pandemic. Memberships will increase by 4% by 2022 slightly inching above the long run average of 3.7%. Experience shows us that credit union memberships growth are a little bit higher after economic crisis wanes.
- **Saving & Asset Growth:** Savings and asset growth tapered in the second quarter following a big first quarter performance boosted by federal government's stimulus direct payment to households. Second quarter savings and assets increased by 1.4% and 1.5% after first quarter growth of 6.8% and 5.7%, respectively. CUNA economists forecast savings and assets to grow by 12% and 11.5%, respectively by the end of 2021. Next year, savings will grow at 6% since the demand for savings will decline considering the high saving rate in 2021. However, If there is another Covid surge which induces fear of face-to-face interaction, people may limit spending which could drive saving above forecast for 2022. Asset growth will be 5.5% in 2022.
- **Asset Quality:** Asset quality of credit unions is at its healthiest. Delinquency rate in the second quarter was 0.46%. Net-charge off rates dropped to historic low of 0.24% which is lower than the long run average by 50 percent. However, most of the factors that contributed to improved asset quality have ended and their effect will be felt more likely at the end of this year and next year. There is no additional pandemic assistance from the federal government, additional unemployment benefits have expired, and the moratorium on evictions has ended. Therefore, CUNA economists forecast that delinquency rate will be 0.65% by 2021 and 0.6% by 2022. Net Charge-off rate will be 0.31% by 2021 and 0.5% by 2022. These values are still lower than the long run average despite slight increases.
- **ROA:** Credit unions have registered record earnings for the second time this year. Second quarter ROA grew 1.16% following another strong first quarter performance of 1.04%. However, this growth is not evenly distributed among all credit unions. Large Credit unions with asset size over \$1B have ROA of 1.26% compared to 0.87% for the next large asset group (\$500Mil - \$1B) or 0.16% for small credit unions (<20Mil). Going forward, earnings will be hindered by tight interest margins, supply chain challenges in the auto sector, and a slowing housing market; nonetheless, credit unions should expect relatively robust ROA of 0.95% in 2021. CUNA economists also forecast ROA to decline to 0.7% 2022. Further falling interest rate margins, provisions going back to normal, and probability of lower mortgage origination rate or refinance are downside risks to the 2022 forecast.



# Credit Union Forecast – September 2021

	Actual Results		Quarterly Results/Forecasts				Annual Forecasts	
	5 Year Average	2020	2021:1	2021:2	2021:3	2021:4	2021	2022
<b>Growth Rates:</b>								
Savings Growth	9.6%	20.6%	6.8%	1.4%	1.7%	1.7%	12.0%	6.0%
Loan Growth	8.4%	5.0%	0.3%	2.5%	1.6%	1.5%	6.0%	9.0%
Asset Growth	9.1%	18.1%	5.7%	1.5%	2.0%	2.0%	11.5%	5.5%
Membership Growth	3.7%	3.1%	1.2%	1.3%	0.6%	0.3%	3.4%	4.0%
<b>Liquidity:</b>								
Loan-to-Share Ratio**	80.4%	73.6%	68.7%	69.5%	70.0%	69.9%	69.9%	71.9%
<b>Asset Quality:</b>								
Delinquency Rate**	0.74%	0.61%	0.45%	0.46%	0.60%	0.65%	0.65%	0.60%
Net Charge-off Rate*	0.53%	0.47%	0.31%	0.24%	0.30%	0.40%	0.31%	0.50%
<b>Earnings:</b>								
Return on Average Assets (ROA)*	0.79%	0.65%	1.04%	1.16%	0.80%	0.80%	0.95%	0.70%
<b>Capital Adequacy:</b>								
Net Worth Ratio**	10.9%	10.3%	10.0%	10.2%	10.0%	10.0%	10.0%	10.2%



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