

Small-Asset Credit Union Financial Performance

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Introduction

Background

- **Federal Credit Union Act (1934)**
- **Time Frame 1994-2012**
 - **Field of Membership Regulation Change (1998)**
 - **Two Recessions (2001, 2008-2009)**
- **Consumer Loan Market Participant**
- **Overall Financial Services Sector Deregulation**
- **Cooperative Structure**

Research Objective

Problem Statement

Determine the characteristics of the US Credit Union sector that are most like the original type – assets between \$0 and \$10 M

Research Objective

Identify the determinants and attributes of internal and external influences on small US Credit Union performance

Literature

Berger , Demsetz and Strahan (1999) - US credit union industry is dynamic with firm level objectives focused upon cost minimization as opposed to profit maximization

Emmons and Schmid (1999) – Fixed costs of obtaining information about repayment capacity were reduced in credit unions by insisting on sharing certain characteristics, such as “occupation or association, or [belonging] to groups within a well-defined neighborhood, community or rural district

Berger et al. (1998) – regulatory changes affect the structure of the credit union sector, dissolve the common bond requirement -Credit Union Membership Access Act

Garden and Ralston - (1999) – X-efficiency concept applied to credit unions, reasoning that credit unions operate in a competitive environment with banks

Sibbald, Ferguson and McKillop (2002) – Electronic transactions have blurred the difference between other retail financial institutions and United States credit unions

Literature

Berger and DeYoung (2005) – Information processing technologies have decreased the time required for a variety of standardized credit decisions. Communication technologies have enabled electronic fund transfers, analyzing credit, and reduced agency costs of overseeing affiliate locations

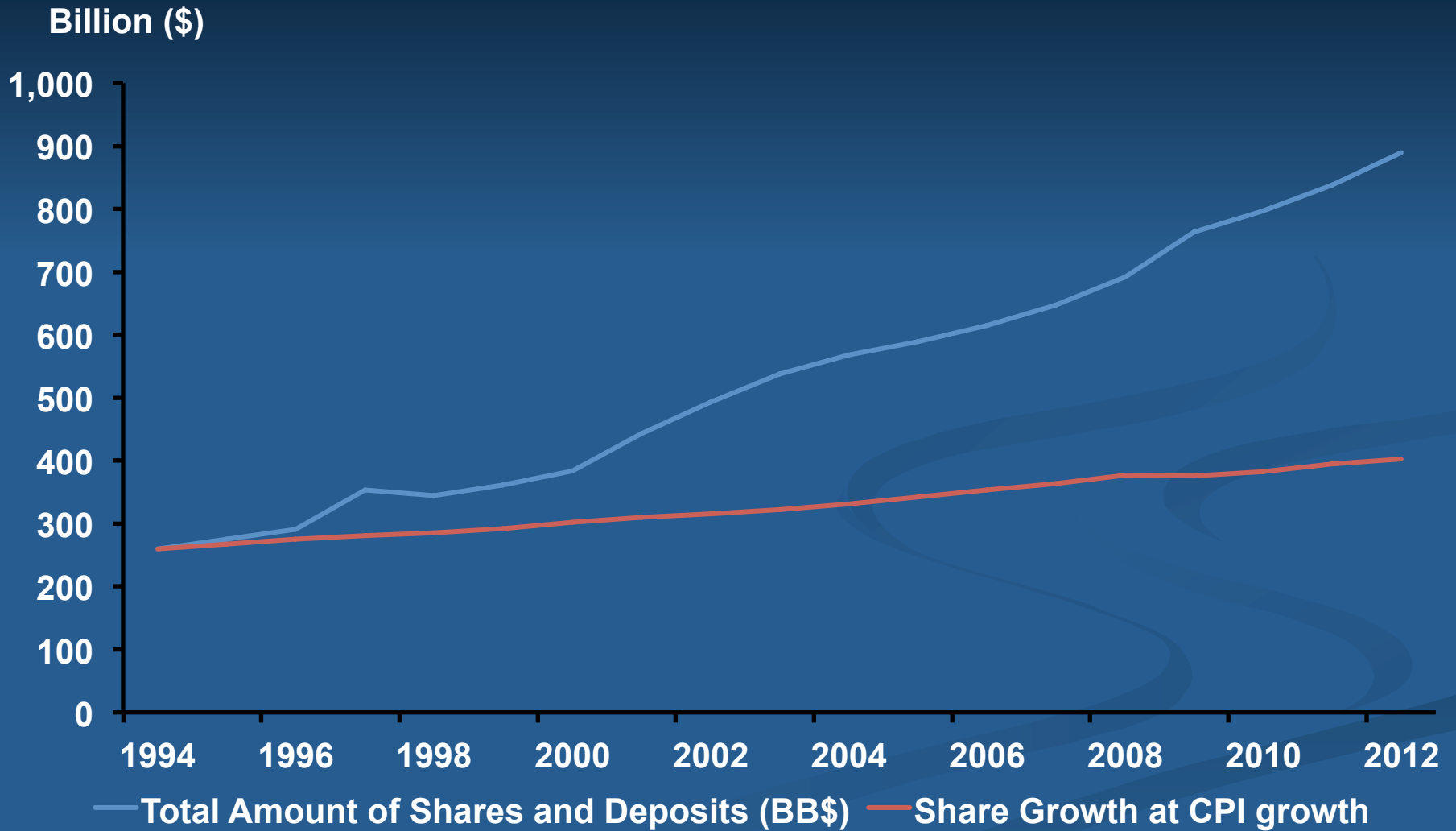
Leggett and Strand (2002) – As credit unions grow (in assets), statistical evidence exists showing management is “able to channel residual earnings away from membership the form of higher net interest margins, towards itself in higher salaries and operating expenses”, a clear case of adverse selection

Glass and McKillop (2006) - Economies of scale in credit unions are present

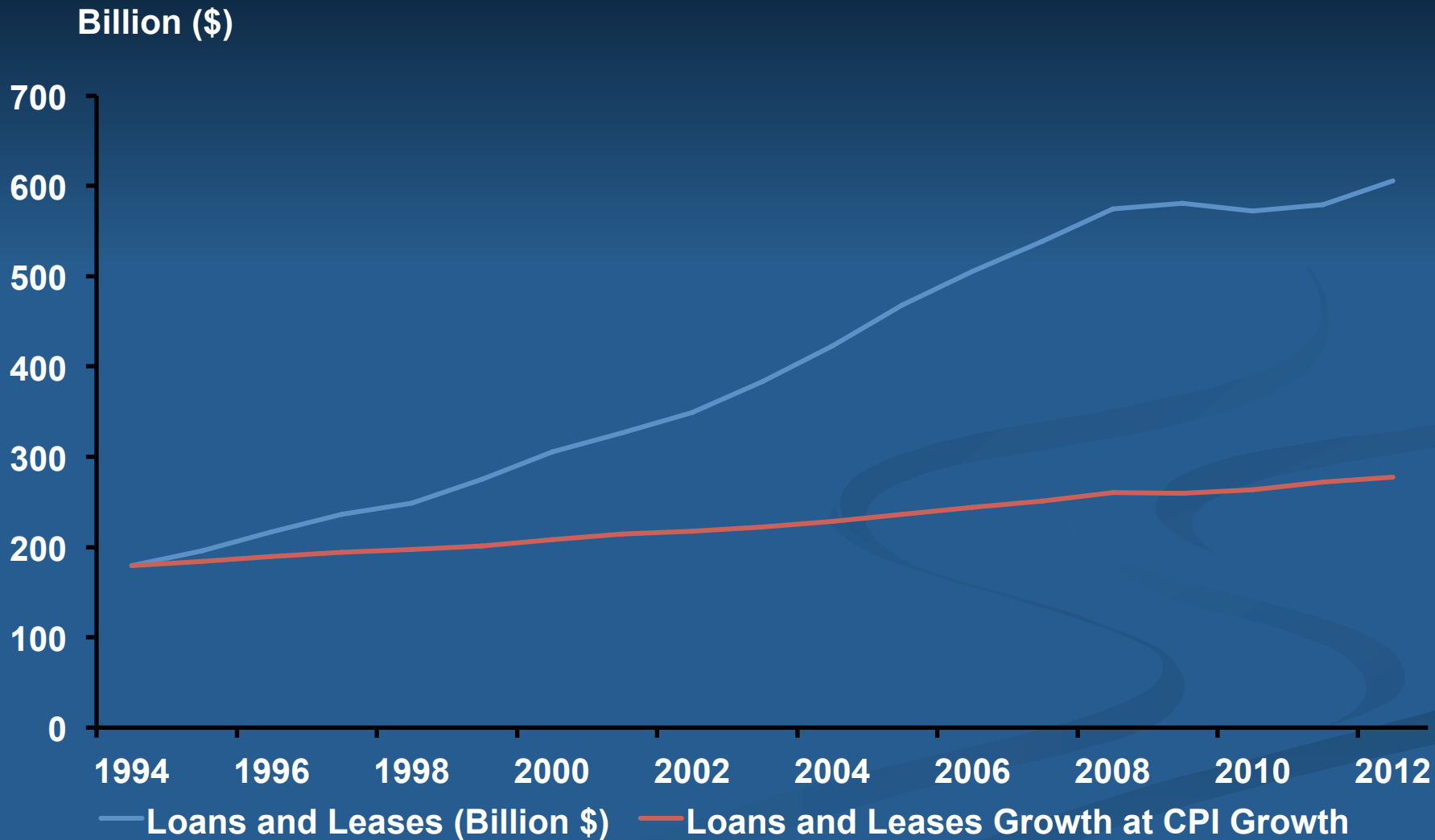
Goddard, McKillop and Wilson (2008) – Common bond and charter effects all make relatively small (although statistically significant) contributions to the explanation of the variation in growth performance

Jacewitz and Kupiec (2012) - The number of credit union members and value of assets has increased (1996-2002)

Deposits

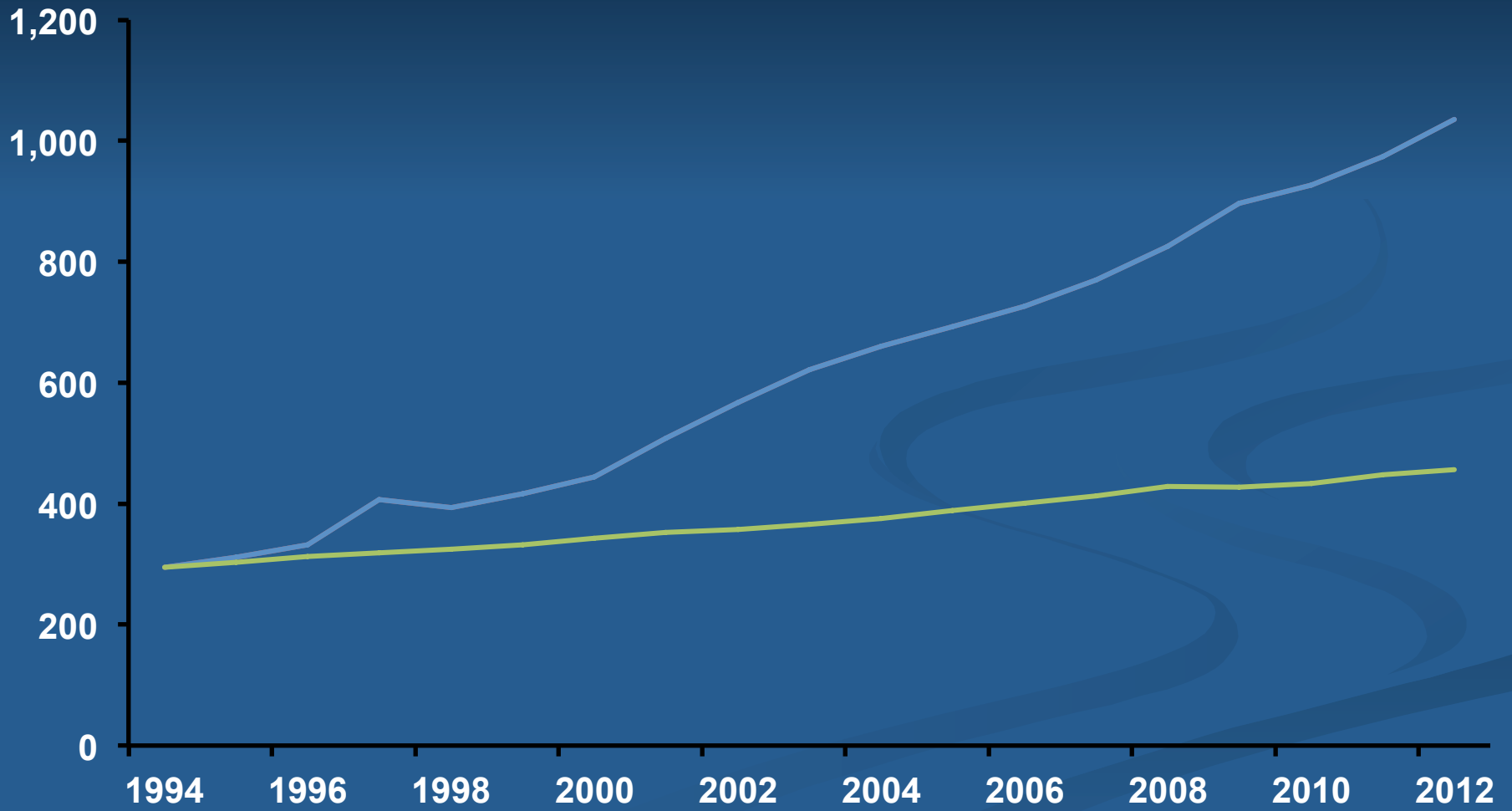


Loans



Assets

Billion (\$)



Value of Deposits 1994, 2012

Asset Type	1994		2012	
Transaction accounts	153,746,506,322	(63%)	392,206,527,485	(58%)
Certificates of deposit	58,653,377,240	(24%)	200,360,115,221	(30%)
Retirement accounts	32,968,621,534	(13%)	79,856,159,663	(12%)

Small shift toward medium term deposits, away from transaction accounts

All Credit Union Loan Portfolio Distribution 1994-2012

Loan Type	1994	1999	2004	2009	2012
Consumer	70.0%	69.9%	65.4%	60.1%	57.8%
Home	8.1%	9.6%	13.2%	17.1%	20.1%
Real Estate	6.1%	7.0%	9.5%	11.1%	9.6%
Credit card	3.1%	3.6%	3.2%	3.5%	4.0%
Business	0.7%	0.7%	1.0%	2.0%	2.7%

Year	Charter		Number of Credit Unions	Assets	Net Income	Loans	Deposits
	Type						
1994	State		2,967	\$ 2,791,132	\$122,319	\$1,748,089	\$ 2,451,834
	Federal		4,881	\$ 2,783,524	\$115,800	\$1,675,103	\$ 2,440,828
1999	State		2,391	\$ 3,725,303	\$163,900	\$2,400,836	\$ 3,193,626
	Federal		4,112	\$ 3,521,870	\$136,118	\$2,197,833	\$ 3,005,571
2007	State		1,309	\$ 4,000,542	\$168,801	\$2,442,941	\$ 3,304,377
	Federal		2,398	\$ 3,756,735	\$150,751	\$2,250,413	\$ 3,105,204
2011	State		900	\$ 4,033,989	\$134,905	\$1,991,769	\$ 3,401,533
	Federal		1,778	\$ 4,027,739	\$127,867	\$1,896,586	\$ 3,432,396

Trends

	Total # of all CUs	# of CUs w/\$1+ billion in assets	% of all CUs with \$1+ billion assets	# of CUs w/less than \$100 million in assets	% of all CUs w/less than \$100 million in assets
2007	8,332	123	1.5%	7,080	85.0%
2008	8,215	132	1.6%	6,920	84.2%
2009	8,066	137	1.7%	6,760	83.8%
2010	7,710	159	2.1%	6,311	81.9%
2011	7,442	173	2.3%	6,023	80.9%
2012	7,165	194	2.7%	5,700	79.6%

Since 2007 –14% decline in CUs—one per day

	Total # of all CU branches	CUs w/5+ branches	CUs w/10+ branches	CUs w/only 1 branch	% of CUs w/1 branch
2007	20,694	1,006	341	5,393	26.1%
2008	21,122	1,032	350	5,176	24.5%
2009	21,290	1,058	364	5,005	23.5%
2010	21,341	1,075	367	4,520	21.2%
2011	21,433	1,100	402	4,311	20.1%
2012	21,406	1,116	415	4,093	19.1%

Branch growth flat—except top 100 712 new branches, 552 (78%)

Trends

	Total # of all CU members	Net new members for all CUs	# of members belonging to Top 100	% of all CU members belonging to Top 100	# of net new members for Top 100	% of net new CU members joining the Top 100
2010	91,175,370	1,313,996	26,054,728	28.6%	1,600,415	121.8%
2011	92,236,368	1,060,998	27,234,013	29.5%	1,179,285	111.1%
2012	93,735,068	1,498,700	28,498,526	30.4%	1,264,513	84.4%

Membership gains in top 100 CUs offset by losses across system

	Total members for all CUs w/less than \$100 million	Total assets for all CUs w/less than \$100 million
2007	23,611,594	\$130,955,476,177
2008	22,893,541	\$130,436,860,982
2009	22,175,487	\$128,981,918,784
2010	19,936,802	\$126,602,264,544
2011	18,825,575	\$127,632,660,886
2012	17,646,314	\$125,867,933,673
NET LOSS	-5,965,280	-\$5,087,542,504

2007-2012 under \$100 M CUs lost \$5 Bil and 6 million members

Small Credit Union Loan Portfolio Distribution 1994-2012

Year	New Vehicles	Used Vehicles	1st Mortgage/Lines of Credit	Other Real Estate Loans/Lines of Credit	Unsecured Credit Card	Busine ss	Other Unsecured	Leases
1994	31.8%	22.0%	5.7%	5.3%	2.3%	0.6%	21.2%	0.0%
1999	26.1%	27.7%	9.2%	9.3%	4.5%	0.7%	13.9%	0.2%
2007	24.0%	27.1%	13.1%	12.8%	3.7%	1.0%	11.7%	0.0%
2011	13.4%	28.2%	22.0%	13.2%	4.9%	1.8%	10.4%	0.1%

Asset Size	1994	2012	Percentage
(\$ Million)	Population	Population	Change
Below \$5 million	6000	1607	-73%
\$5.1 to \$10	1848	882	-52%
\$10.1 to 20	1478	1036	-30%
\$20.1 to \$50	1484	1277	-14%
\$50.1 to \$100	662	775	17%
\$100.1 to \$250	473	686	45%
\$250.1 to \$500	166	315	90%
\$500.1 to \$1,000	66	210	218%
More than \$1,000	24	172	617%

Variable	Average change (2008 to 2011)		
	All Credit Unions	Small Asset Credit Unions	
		0 to \$4.99 M	\$5 to \$9.99 M
Net interest income	\$717,645	(\$19,865)	(\$11,756)
Interest expense	(\$1,391,794)	(\$22,892)	(\$74,167)
All loans	\$2,525,652	(\$188,348)	(\$234,290)
Consumer loans	(\$603,011)	(\$269,671)	\$652,661
All deposits	\$21,606,165	(\$382,891)	(\$301,469)
Core deposits	\$13,735,845	(\$20,444)	\$744,765

- Two thirds of all small asset credit unions shifted their operational focus
 - significant asset and deposit growth occurred
 - growth in assets and deposits was accompanied by lower growth rates for net income and total loan activity
 - increasing fraction of small asset credit union assets are not being converted to loans

- Current loans channeled to real estate purchases as opposed to prior short term vehicle loans.
 - Increased deposits must increasingly as a source of income, either through investments or deposits elsewhere.
 - Inability to diversify into a variety of savings products may constrain their ability to enhance income
 - The shift in the loan portfolio may also be a response to products needed by the membership of these credit unions

Study Design

- Call Reports 1994-2012; 2008-2011
- **Credit Unions by Asset Size**
- Macro Trends

NATIONAL CREDIT
UNION ADMINISTRATION
ALEXANDRIA, VA 22314-3428
OFFICIAL BUSINESS

Call Report Form and Instructions

MUST BE RECEIVED BY: October 22, 2013

TO THE BOARD OF DIRECTORS OF THE CREDIT UNION ADDRESSED:

This booklet contains the third quarter 2013 NCUA 5300 Call Report. All credit unions must complete pages 1 – 10 of this form. Page 11 is the PCA Net Worth Calculation Worksheet and requires no input unless you have completed a merger or acquisition that qualifies for Business Combination Accounting or intend to use an optional Total Assets Election and/or Alternative Risk Based Net Worth calculation to compute your net worth ratio. Page 12 is the Standard Components of Risk Based Net Worth Requirement worksheet which is automated and requires no input. Pages 13 – 18 contain supplementary schedules and should be completed as applicable.

Please complete the Call Report using accounting and statistical information from your credit union's records as of September 30, 2013. You may complete a paper copy of the form; however, we urge you to consider filing your Call Report using the online, web-based system. This system is more efficient to use, more cost effective and helps to ensure more accurate data.

Please return your completed Call Report information as soon as possible, but no later than **October 22, 2013**. If you have any non-technical questions, please contact your National Credit Union Administration Regional Office or your state credit union supervisor, as appropriate. Please call NCUA Customer Service at 1-800-827-3255 with any technical questions.

NATIONAL
CREDIT UNION
ADMINISTRATION



THIRD QUARTER
CALL REPORT

2013

- Unemployment rate
- Annual payroll (by industry; total)
- HPI (MSA, statewide)
- Transfer payments (all types)
- Per capita income
- Car sales

- Over 90 percent of all credit unions have 6 or fewer branches
 - 50.2 percent operate one branch;
 - 64.4 percent of credit unions conduct business operations with one or two branches.
- In the case of credit unions with assets below \$10 million, 91 percent have one branch while 6 percent have two branches

Dependent Variables

- Range of financial ratios
 - Profitability
 - Interest income
 - Interest expense
 - Loan volume
 - Any type
 - Consumer only
 - New and used cars, unsecured

Dependent Variables

- Deposit terms
 - Any type (regardless of length)
 - Core (savings and checking)

Model Formation

Absolute change in CU performance (2008 to year t) =

α + performance in lag year + year intercept + size + equity + volume of delinquency + HPI + payroll + transfer payments + per capita income + unemployment rate + car sales + urban dummy + use of transactional website + ε

Cross term for all credit unions; cross terms for 0-4.99, 5-10

Based on DeYoung, Lang and Nolle (2007) specification of community banks with respect to Internet banking—Asset view and bank structure, economic conditions, bank performance, market conditions

Key idea – **trend** in growth, not **level** of growth

Key results

- The lag always matters
 - Reduce income, expense change
 - Increase loan volume change
 - Decrease total deposits change; increase core deposits change
- Sensitive to changes in **transfer payments**
 - Increased magnitude of change in loan volume and interest expense
 - Transfer payments increase loans, interest paid
 - Change in small asset credit union income is reduced by increased transfer payments
 - Transfer payments associated with stable/flat income

- Per capita income
 - No effect on income
 - Reduction in change in core deposits for 0-5 million
 - Increase in change in core deposits for 5.1-10 million
 - Magnitude of per capita income growth on change in interest expense and core deposits is greater than for all credit unions
- The effect of asset growth and HI
 - Change in income, loans and deposits is smaller in magnitude than for all other credit unions sizes

- Changes in volume of income, loans, and deposits are not significantly affected by adopting transactional website technologies
 - Economic stimulus in recession helps by income, not payroll volume
 - Implication: create loyalty
 - Real estate value change was largest driver

- All results suggest asset growth leads to accelerated performance
 - If they don't, must maintain low costs within their fixed FOM
- Relatively small membership and assets limits the capacity of these credit unions to
 - expand their ability to service deposits
 - adopt product marketing tools
 - process new loan applications efficiently
 - distribute the fixed costs of regulatory compliance
- 1998 Access Act facilitates accelerated growth
- Prospects for smallest CUs?

Thank you

Questions