



CAPITAL MARKETS *monthly*

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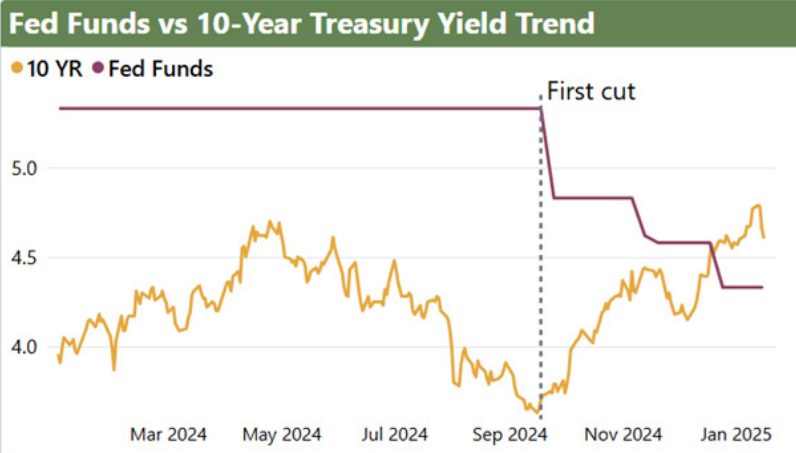


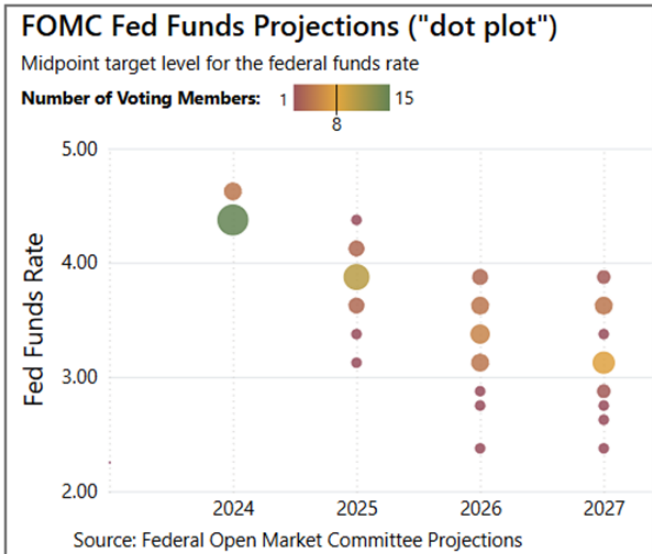
GENERAL MARKET OVERVIEW

New year, same commitment to providing readers with relevant, data-driven, credit union focused insights. We kick off the year with a macro-overview of the NCUA's 2025 exam priorities before diving into a chart-heavy analysis of the most recent call report.

Market trading hours may be put on pause, as they were on January 9 in honor of the late President Jimmy Carter, but the saga of price discovery is an endless and continuous process as current market prices reflect future expectations. Typically, markets price in rate cuts several months before the Fed officially adjusts policy. Historically, yields drop in anticipation of the Fed's transition to a rate cut regime and then move sideways. However, this cycle, the speed and magnitude of yields rising post-cut is one for the record

books. In the four months since the Fed's first cut, the 10-year Treasury yield is up 100 basis points while the overnight rate has been dialed down 100 basis points. *Continued on page 2*

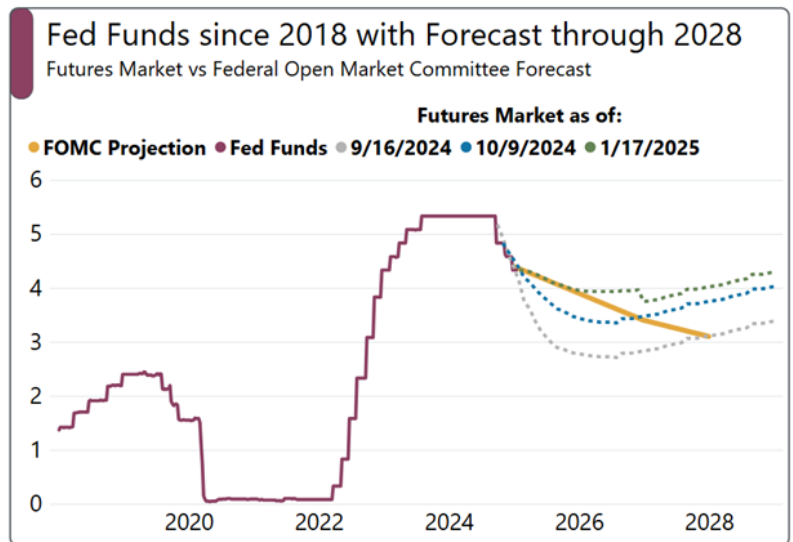




The yield curve has been bear-steepening again with the long end of the curve selling off harder than the short end. With U.S. federal debt-to-GDP at 120%, investors are asking questions about the value of bonds and the path forward with a Fed and Treasury under the most scrutiny since the 1951 Treasury-Federal Reserve Accord separated the two. Ten-year yields are rising as markets price in fewer cuts.

At the Fed's December meeting, the Federal Open Market Committee updated their suite of economic projections. Of special interest is the Fed's "dot plot" showing voting member forecasts for the midpoint target level for the federal funds rate. The Fed's dot plot represents each of the Fed officials' individual estimates of future interest rate projections. One year out, voting members project rates between 3.125% and 4.375% and a wider 150 basis point forecast dispersion between 2.375% and 3.875% in 2026 and 2027.

Keeping the rate volatility in mind, coupling the Fed's projection with the market forecast gives us a better idea of where rates are likely going. Since September, the market has priced in fewer cuts and is even anticipating higher rates than the Fed's updated December projection. Bond vigilantes and rumors of a Fed policy mistake have only partial explanatory power. Global capital flows have caused the U.S. dollar to surge as tariff potentiality becomes a reality. When the dollar strengthens against other currencies, foreign countries tend to sell U.S. Treasuries to support their own currencies. The most recent move has reached similar levels of selling pressure as prior U.S. dollar tops. *Continued on page 3*



REAL-TIME PAYMENTS (SIMPLIFIED)

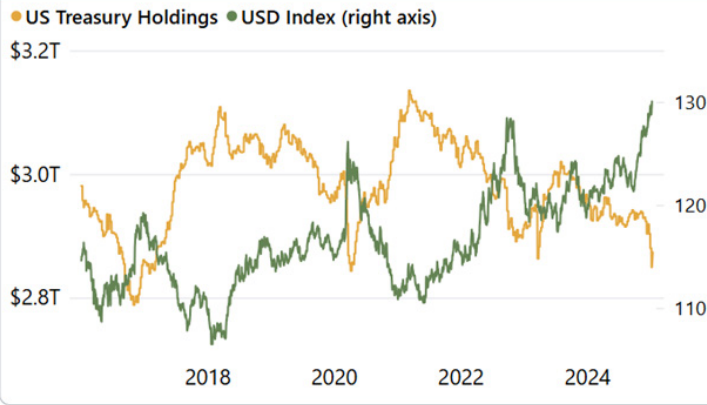
If they have to ask, it's already too late.
Time waits for no one.

alloyacorp.org/real-time-payments-simplified



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Marketable U.S. Treasury Holdings vs U.S. Dollar Index



China is experiencing uncontrolled deflation in their economy, with their currency even likely to de-peg from their desired reference to the dollar. Their solution is to both print renminbi and sell U.S. bonds to stimulate their economy. China's deflation is so bad that their 30-year government bond recently dropped below Japan's (yes, that Japan!) 30-year yield for the first time ever. The dollar rally is getting long in the tooth and nearing a point where the new administration, given the U.S. debt load, will likely intervene.



2025 NCUA'S EXAM PRIORITIES

The NCUA's most recent letter (Letter 25-CU-01) to federally insured credit unions outlined the NCUA's 2025 Supervisory Priorities. These priorities span four main topics: Credit Risk; Balance Sheet Management, Risk to Earnings, and Net Worth; Cybersecurity; and Consumer Financial Protection, summarized below. How can Alloya's Capital Market's Team help? Feel free to contact Brian Myers, AVP, Loan Transaction Services at brian.myers@alloyacorp.org.

Credit Risk

NCUA examiners will focus on a credit union's lending policies, management practices and loan underwriting standards. Other loan practices of the credit union that will be reviewed are loan charge-offs, loan loss reserves and reports to the board of directors. The letter specifically targeted deteriorated credit card portfolios and used vehicle loan performance. See the call report section below for details on recent credit card and used vehicle performance analysis.

Balance Sheet Management, Risk to Earnings & Net Worth

Analysis will again be focusing on credit, liquidity and market risk. NCUA examiners will be looking at the current and future sources of earnings. Your policies and strategic plans will act as a comparison guide threshold. Their primary market risk concern is again interest rate risk—whether it is due to higher or lower interest rates — and the effect those changes have on the investment and loan portfolios. Examiners will continue to consider current and prospective sources of liquidity regarding a credit union's liquidity risk-management framework.

Cybersecurity

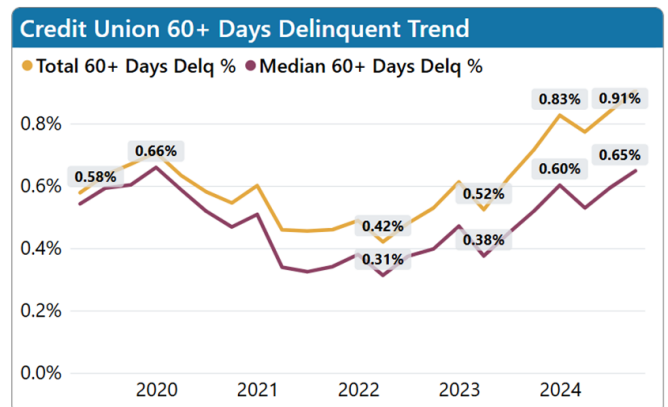
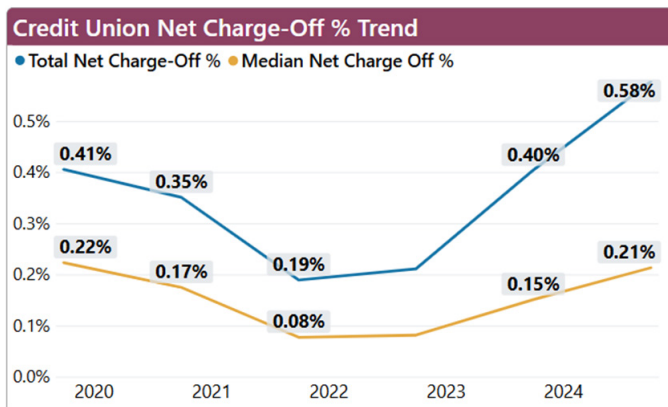
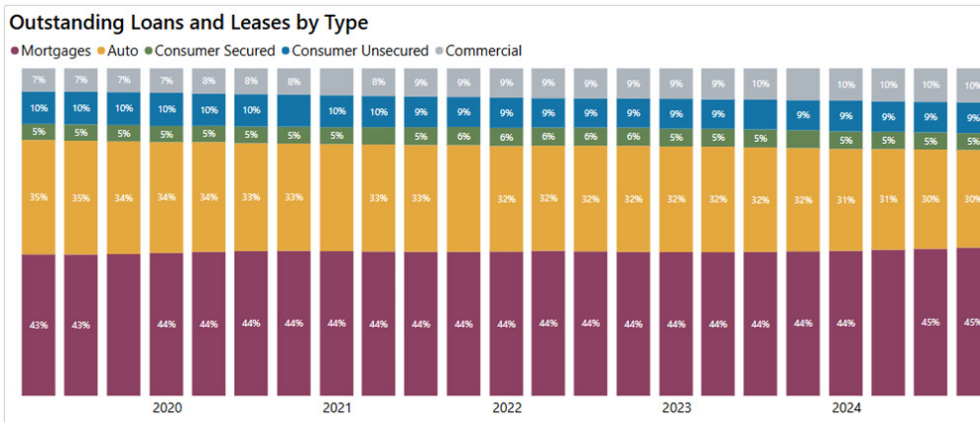
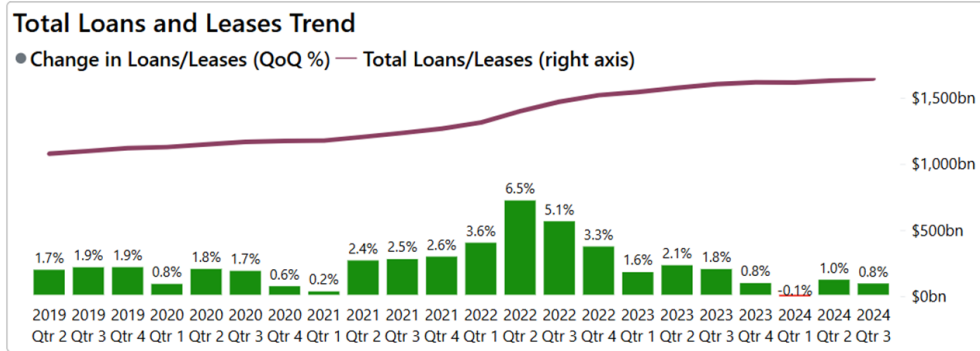
As cyberattacks continue in the financial industry, cybersecurity is a top priority of the NCUA. The NCUA noted that attacks have become more frequent on credit unions and the vendors they use. In light of these increasing attacks, credit unions need to be proactive in their operation plans and conduct ongoing due diligence. Examiners are expected to continue using the information security examination procedures to evaluate information security programs.

Consumer Financial Protection

The NCUA examiners will review your compliance with consumer financial protection laws and regulations. This priority includes a credit union's overdraft programs, fair lending practices, Home Mortgage Disclosure Act and Regulation C, Military Lending Act, and Electronic Fund Transfer Act and Regulation E.



Let us first turn to the NCUA’s number one priority: credit risk. The credit union industry loan book expanded 80 basis points in Q3 2024 to \$1.65 trillion. Loan originations in Q3 decreased slightly to \$136 billion with quarterly originations staying under \$150 billion since 2022.

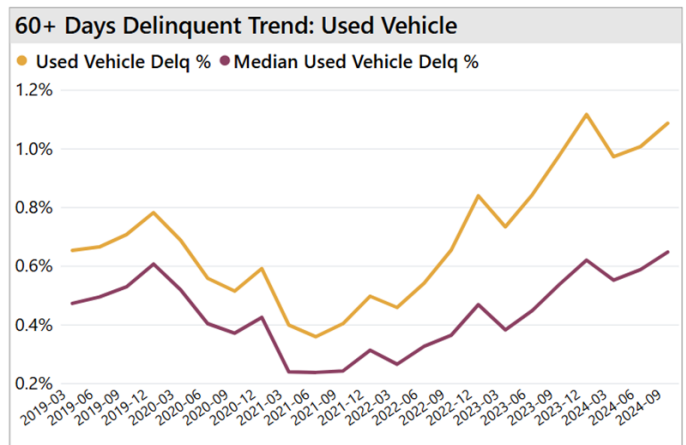
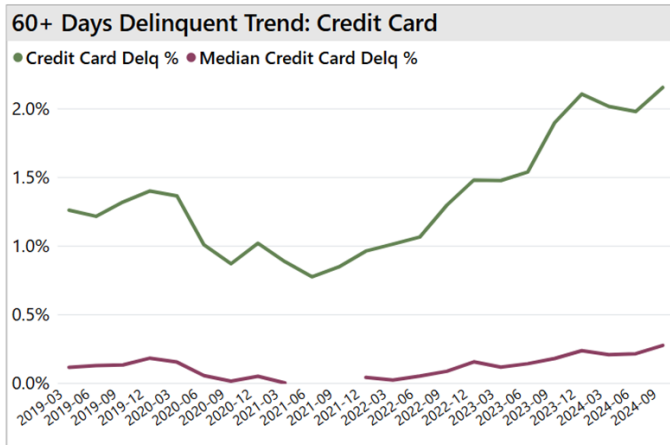
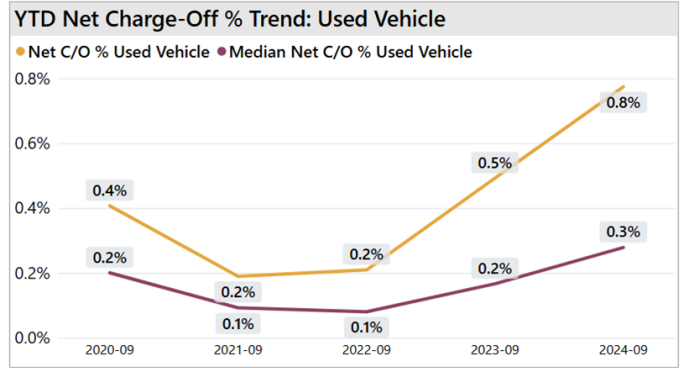
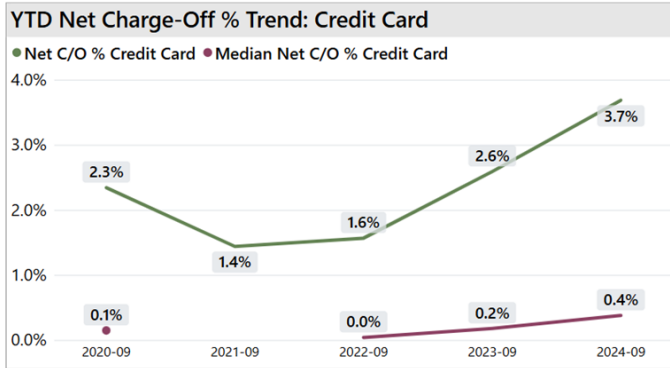


Loan type composition has been stable over the last five years. Auto loans as a percentage of total loans have decreased 5% since 2019 while the allocation to commercial loans has increased from 7% to 10%. Less than half of credit unions have any exposure to commercial loans at all. Of those with commercial exposure, the median allocation is 6.5% of loans.

Both charge-offs and delinquencies have ticked up. The net charge-off ratio bottomed out in 2021 and has risen to 58 basis points as of Q3 2024. However, the median credit union’s charge-off ratio is 21 basis points, the same loss ratio as in 2019.

The total industry 60+ days delinquent percentage increased to 91 basis points, while the median credit union has only 65 basis points of the outstanding loan amounts 60+ days delinquent. *Continued on page 5*

Recall the NCUA's concern over credit card and used vehicle loan performance. See the accompanying charts for both the net charge-off ratios and 60+ day delinquencies for credit cards and used automobiles. The industry net charge-off ratios on credit cards and used vehicles increased to 3.7% and 0.8%, respectively. Median charge-off ratios are lower, particularly in credit cards where fewer credit unions participate. Delinquency trends with credit cards and used vehicles mirror the broader loan portfolio. Delinquent used vehicles are just over 1.0% with the median credit union at 65 basis points of outstanding used vehicles. And delinquent credit card balances climbed to 2.15% of outstanding credit card loans with the median credit union at 27 basis points.



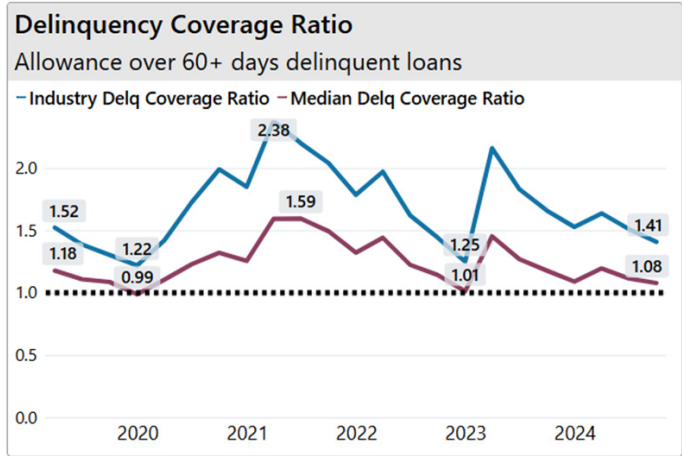
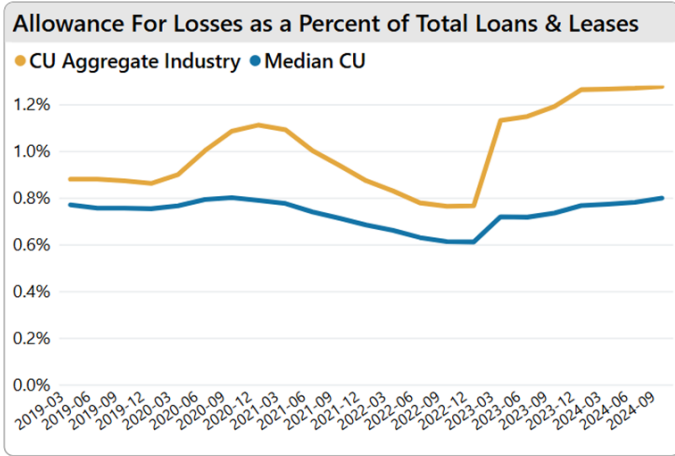
Comparing these numbers to your own loan books will help you anticipate whether your portfolios will draw additional scrutiny during your next NCUA exam. In particular, the NCUA will assess if your allowance is adequate to cover potential losses. The allowance set aside for loan losses climbed to over \$21 billion, or 1.28% of outstanding loans, while the median credit union has an allowance of 80 basis points. Another way to assess allowance adequacy is to look at the delinquency coverage ratio (DCR) or the loan allowance over 60+ days delinquent loans. A ratio of 1 means the credit union has a dollar of loan allowance for every dollar 60+ days delinquent. The total industry delinquency coverage ratio has declined from Q1 2023 to 1.41 as of Q3 2024, while the median credit union DCR declined to 1.08. *Continued on page 6*

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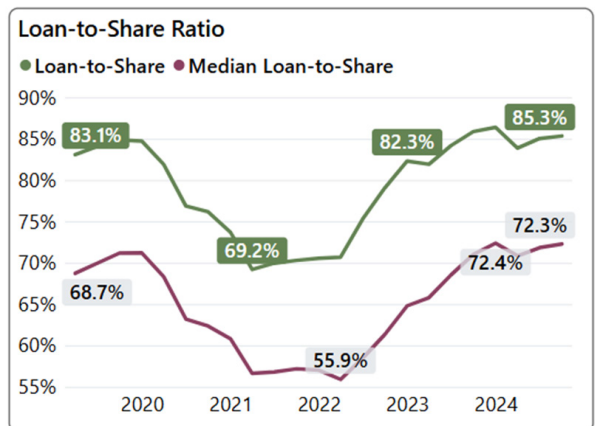
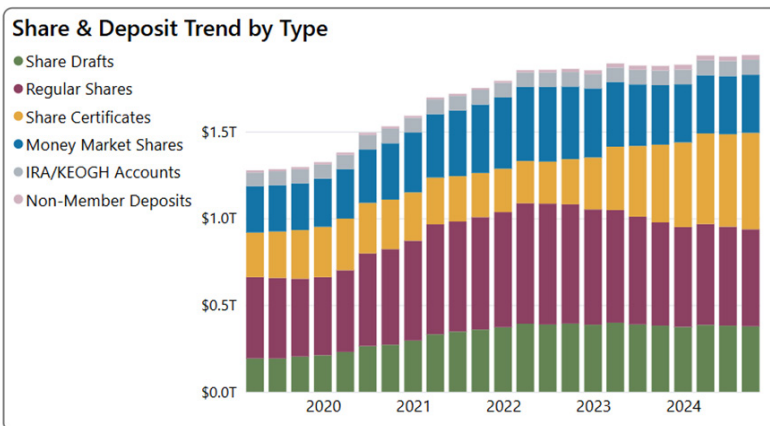
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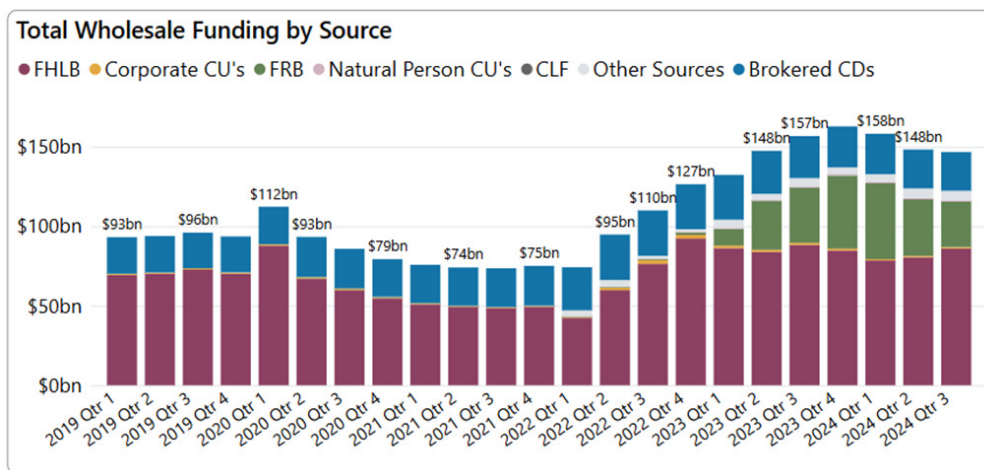


The next NCUA priority is balance sheet management and its impact on earnings and capital. Total shares and deposits increased 40 basis points from the previous quarter and are in striking distance of crossing the \$2 trillion milestone. As you can see from the chart below, the composition of share type has shifted from regular shares to share certificates as credit unions compete for deposits.

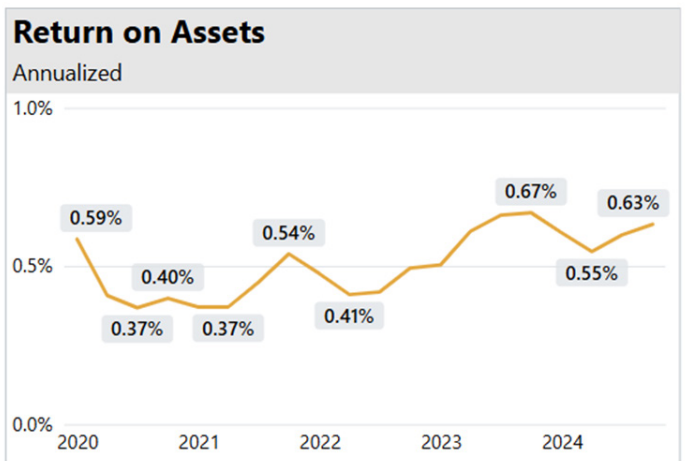
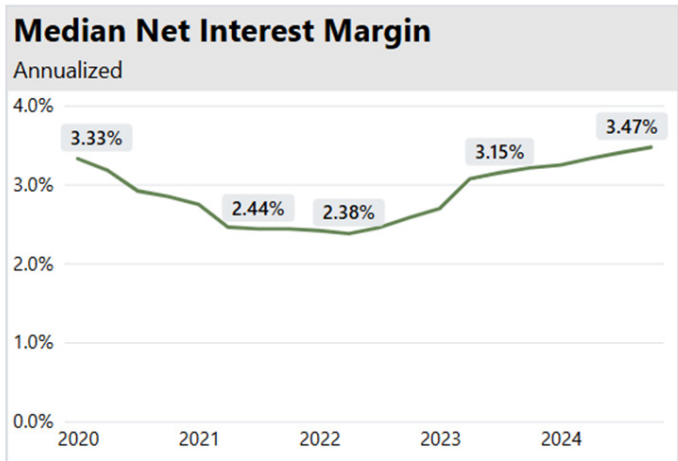
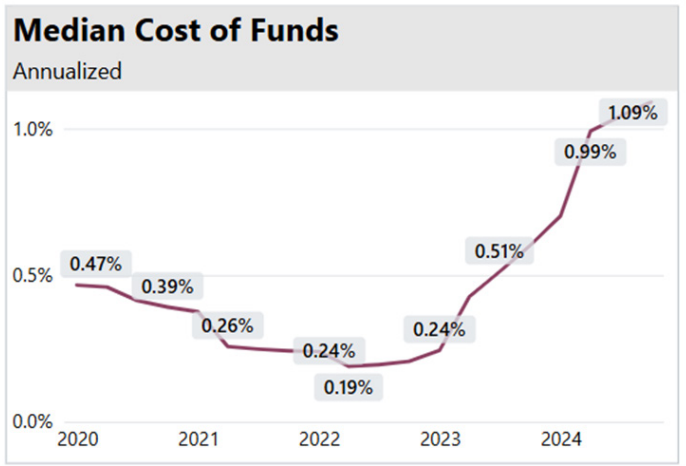
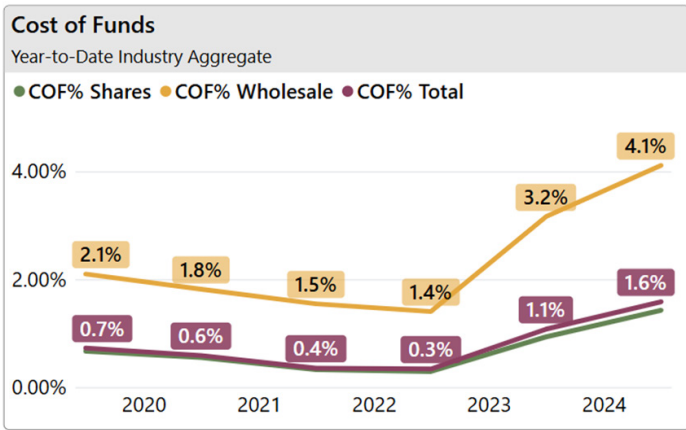
The small net change in both loans and shares led to a narrow increase in loan-to-share (LTS) ratios. The industry LTS ratio is 85% while the median credit union LTS ratio is 72%.



Wholesale funding decreased slightly to \$147 billion, or 7% of liabilities. This was the third consecutive quarterly decrease in wholesale borrowings. Interestingly, Federal Home Loan Bank advances have increased over the same time frame, likely from credit unions replacing maturing Federal Reserve borrowings (Bank Term Funding Program runoff). *Continued on page 7*



Wholesale borrowing cost of funds is up markedly from 2022, but credit unions have managed their balance sheet sufficiently to maintain both net interest margins and return on assets. While industry wholesale funding costs are over 4.0%, the median credit union total cost of funds is just over 1.0%. The (annualized) median net interest margin is shy of 3.5%, with the median return on assets at 63 basis points.



SMALL-DOLLAR LENDING (SIMPLIFIED)

Lend your members a hand without lifting a finger.

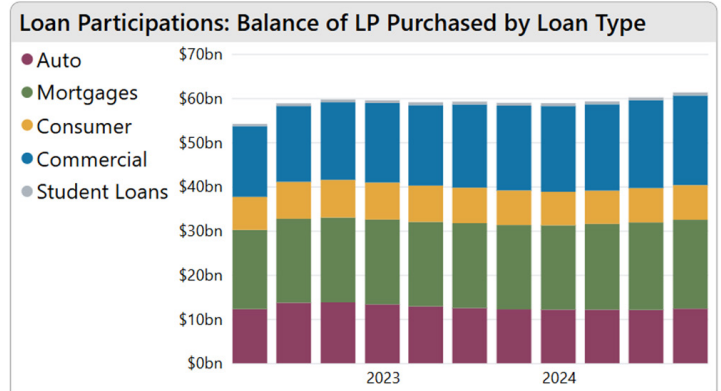
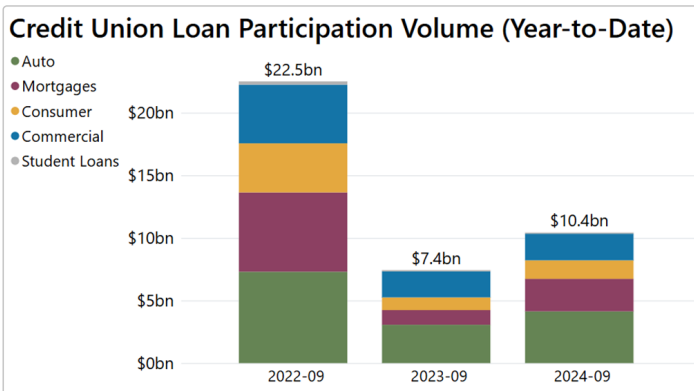
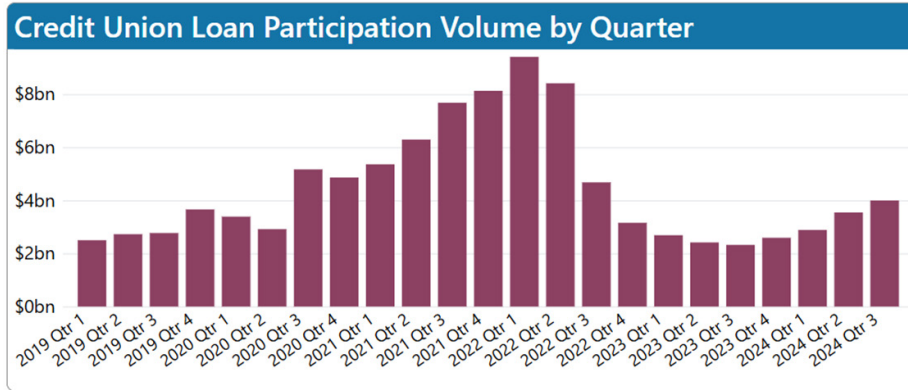
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Effective balance sheet management, the kind the NCUA will be looking for in their examinations, utilizes loan participation (LP) as a reliable and effect liquidity tool. Q3 2024 loan participation volume increased by \$4 billion, or 1.9%, the largest quarterly increase since Q2 2022. Year-to-date volume is over \$10 billion, materially more than the annual volume through Q3 last year. The loan type composition of LP volume remains consistent with prior years, with some additional activity in 1-4 family real estate. New volume exceeded runoff over the last several quarters, lifting Q3 2024 LP outstanding over \$60 billion.



ITM & ATM CAPTURE (SIMPLIFIED)

Too many cooks in the kitchen?
ITM/ATM Capture should be a simple recipe.

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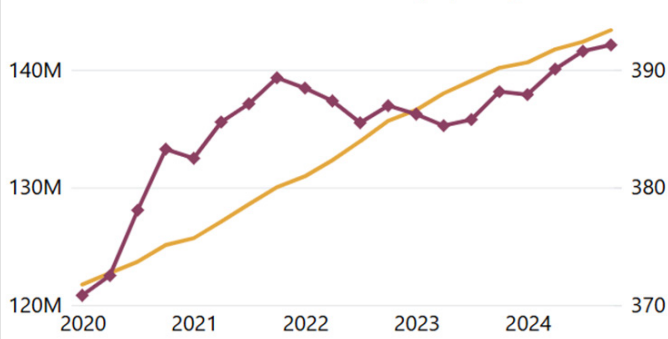
FINAL THOUGHTS

The new Trump Administration begins with great tension, much like pulling back a bow — the greater the tension, the farther the target. Legendary investor Stan Druckenmiller said that in his 50-year career, this is the largest shift to a pro-business administration he has seen and that the CEOs he speaks with are “somewhere between relieved and giddy.” Cautiously optimistic credit unions are poised for success with this palpable rise in sentiment. While December is a natural time for reflection, January is for putting our best selves forward, both personally and professionally, in pursuit of our mission to meet the ongoing needs of our respective members.

In total, 366,000 employees support more than 143 million credit union members. Industry membership is growing, though year-over-year growth has slowed to 2.3% from over 4% in 2023. Not all credit unions are experiencing membership growth. Over the last five years, the median credit union has been shrinking on a rolling year-over-year basis except for a brief increase in membership in the first half of 2023.

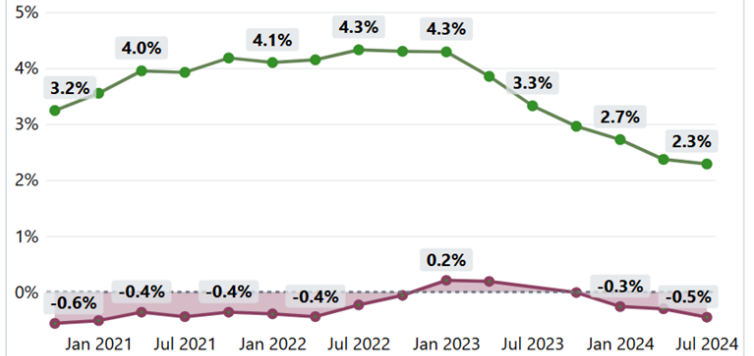
Number of Members and Supporting CU Employees

● Number of Members ◆ Members Per Employee (right axis)



Year-over-Year Membership Growth

● Change in Membership ◆ Median Change in Membership



Alloya, a credit union for credit unions, can simplify your back office to help your employees do more for your members and to address the NCUA’s heightened scrutiny of balance sheet management. Join Alloya in seizing the momentum, the optimistic business outlook, and the improved liquidity landscape to meet the ever-growing needs and opportunities the new year presents.

Attending the GAC?

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Please join us for networking, cocktails and light hors d'oeuvres at Alloya’s Member Appreciation Reception at the Governmental Affairs Conference! RSVP is requested but not required.

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