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CAPITAL MARKETS *monthly*

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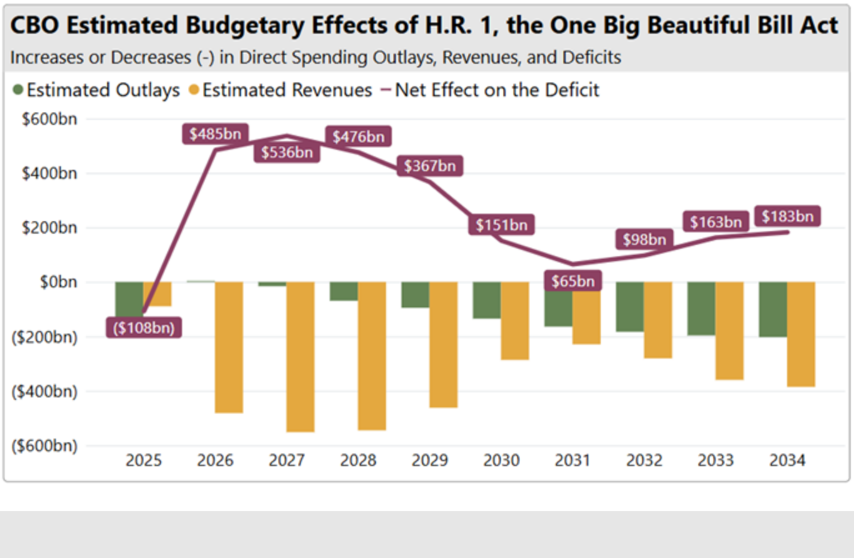
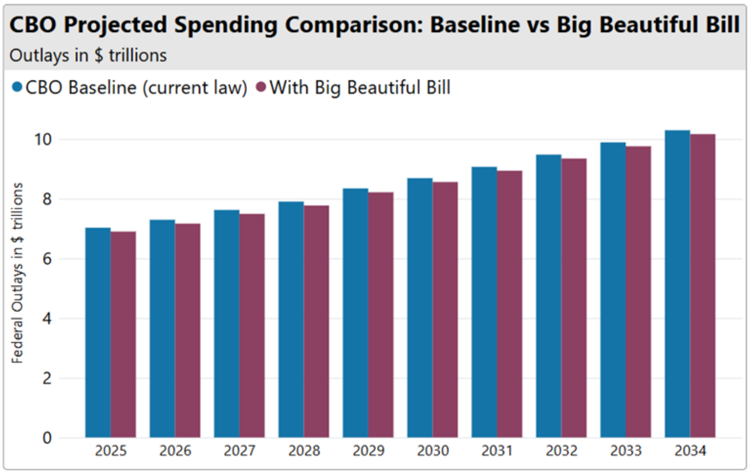
GENERAL MARKET OVERVIEW

The feud over foreign policy with the Israel-Iran conflict coincides with the feud over the domestic fiscal picture with the "One Big Beautiful Bill" (OBBB). According to the Congressional Budget Office (CBO), over the next 10 years, the OBBB will reduce federal outlays by $1.3 trillion. However, the bill would also reduce revenues by $3.7 trillion, leading to a deficit increase of $2.4 trillion. For reference of this analysis, see the CBO Estimated Budgetary Effects chart below, which shows the annual detail by fiscal year.

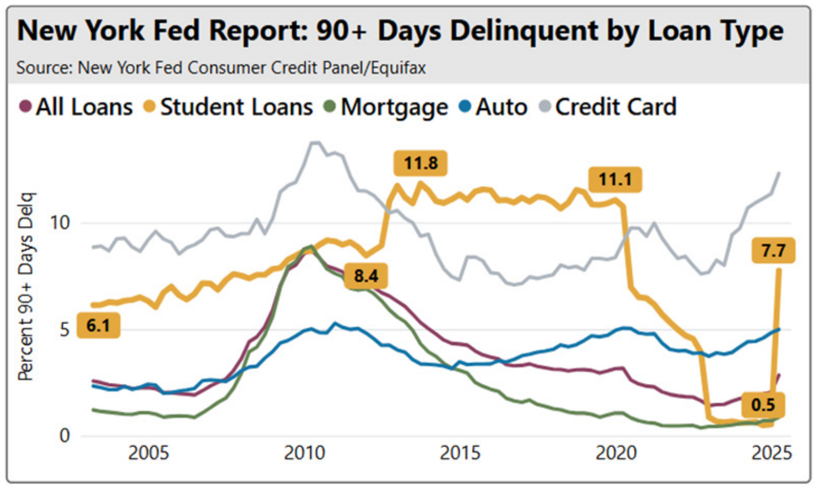
It is worth noting that while the OBBB increases the deficit, it does so by causing taxpayers to keep more of their money by extending the original Trump tax cuts scheduled to expire absent new legislation. Those concerned with the fiscal situation cite a $1.3 trillion reduction over 10 years is ineffective, particularly when the federal budget's baseline growth has outlays rising from $7 trillion in 2025 to $10.3 trillion in 2034 (see **Table B-2** of the CBO's *Budget and Economic Outlook*). The chart on page two shows the minimal impact of the OBBB cuts relative to the CBO's baseline outlays under the current law. *Continued on page 2*





Turning to consumer debt, the Federal Reserve Bank of New York recently published a **Household Debt and Credit Report** that highlights the stark impact of restarting student loan repayments.

The student loan payment pause acted like a stimulus flowing into the economy and is now coming off. The shift from pandemic deferrals to full repayment has rapidly brought student loan delinquencies back to pre-COVID norms. Delinquencies of 90+ days jumped from 0.5% to nearly 8% of outstanding balances in Q1.

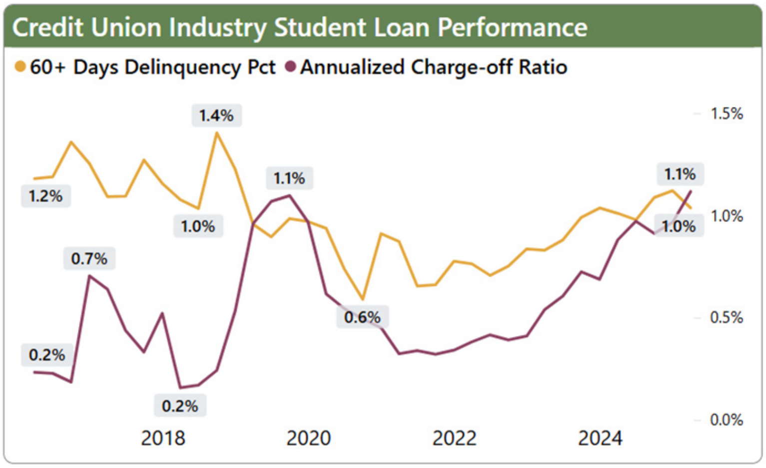


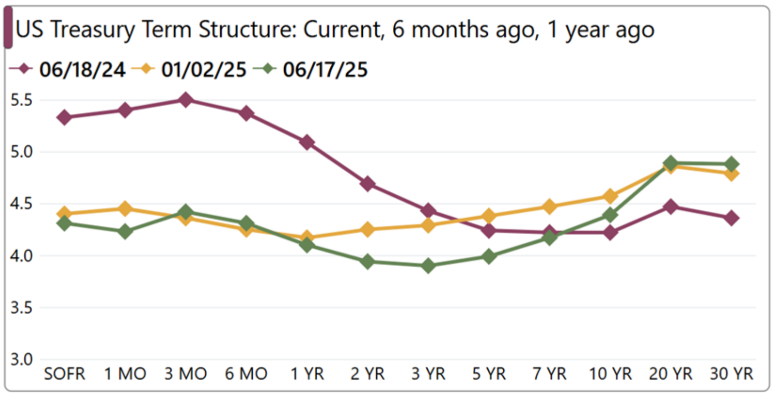
That surge, impacting some six million borrowers, has triggered a wave of credit score declines, with implications for household credit health and the broader economy. Delinquencies are no longer confined to recent graduates. Those aged 40 and above now account for more than 25% of past due accounts. We are discovering the degree of credit score inflation from not counting student loan payments. Roughly 2.2 million borrowers saw credit scores drop by 100+ points after slipping into delinquency in early 2025. Those who originally had top-tier credit are suffering the deepest cuts, jeopardizing mortgage, auto and credit card access.

Borrower Type	Credit Score Impact
Subprime (<620)	- 74 points
Near-prime (620-719)	- 140 points
Prime (>720)	Up to -177 points

According to *Business Insider*, collections resumed in May with federal enforcement (wage garnishment, tax intercepts and even Social Security levies). *The Wall Street Journal* speculates that gross domestic product (GDP) may take a hit of about 0.1% as households trim spending to cover loan obligations.

The credit union industry has minimal exposure to student loan debt, but we will likely feel some of the knock-on effects. The national situation is drastically different from credit unions' student loan exposure. Credit unions have de minimis exposure to student loans at only 40 basis points of total outstanding loans. As of Q1 2025, the delinquency rate on student loans is just over 1%, with a Q1 annualized estimated charge-off ratio of 1.1%. While direct exposure to student loans is negligible, the general trends with falling credit scores will likely impact loan pricing and risk metrics. *Continued on page 3*



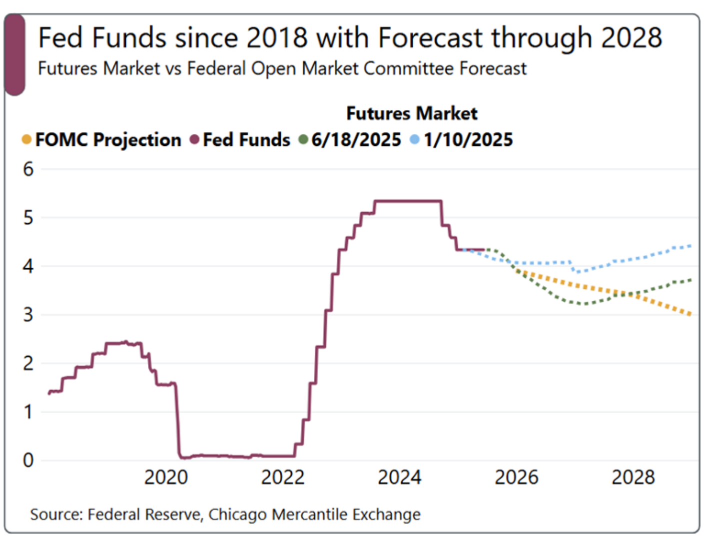


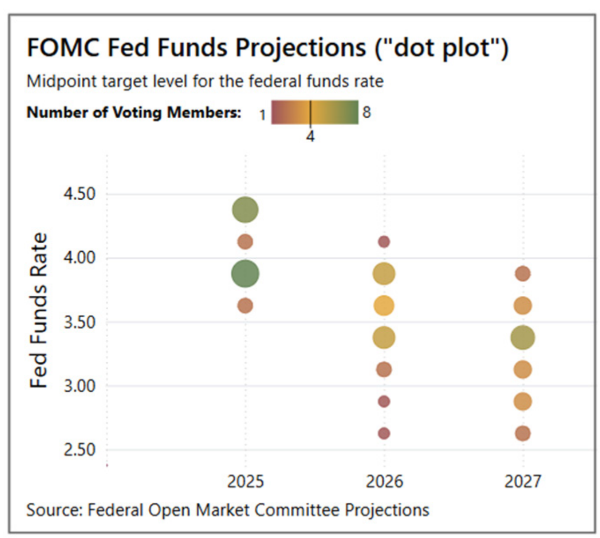
Over the past six months, Treasury market yields have significantly fallen, particularly in the belly of the curve between the two-year and the five-year maturity horizon, which is the investment target area for most credit unions. This comes despite ongoing global uncertainties, including tariff tensions, the war in Ukraine and the Israel-Iran conflict.

The Federal Reserve again left interest rates unchanged at their last Federal Open Market Committee (FOMC) Meeting on June 18. We also have updated FOMC projections that show policymakers are uncertain as a group, as seven have expressed no change in interest rates this year. This is contrary to other Fed members that project two rate cuts by year's end. Estimates on 2025 GDP have fallen to between 1.2% to 1.5%. Typically, any calendar year GDP print that drops below 1.3% all but guarantees a recession in that calendar year, and the Fed is predicting economic growth to be down in this danger zone through 2026. Coupled with slowing growth, the Fed's unemployment forecast ticked up, but not enough to react to the anticipated economic weakness. The Fed models are stuck in the same holding pattern as in 2024. They see downside weakness to the economy while citing Consumer Price Index risk to the upside from tariffs and are waiting for something to break on either side before reacting.

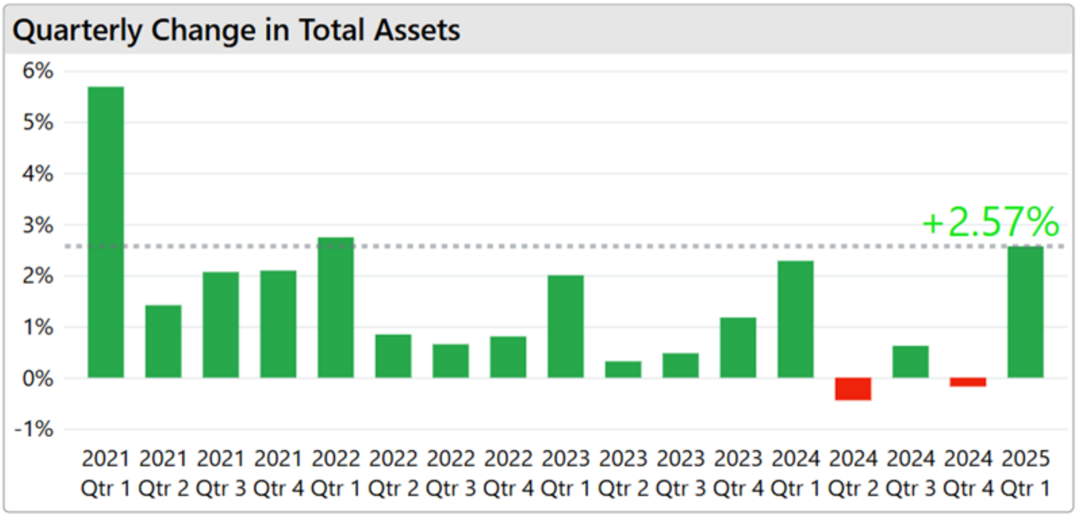
The median "dots," representing each of the Fed officials' estimates of future interest rate projections, stayed roughly the same with a slight upward tilt. Seven members now see zero rate cuts in 2025 versus only four members projecting zero cuts back in March. By year-end, voting members project rates between 3.625% and 4.375%, and a wider 150 basis point forecast dispersion between 2.625% and 4.125% in 2026.

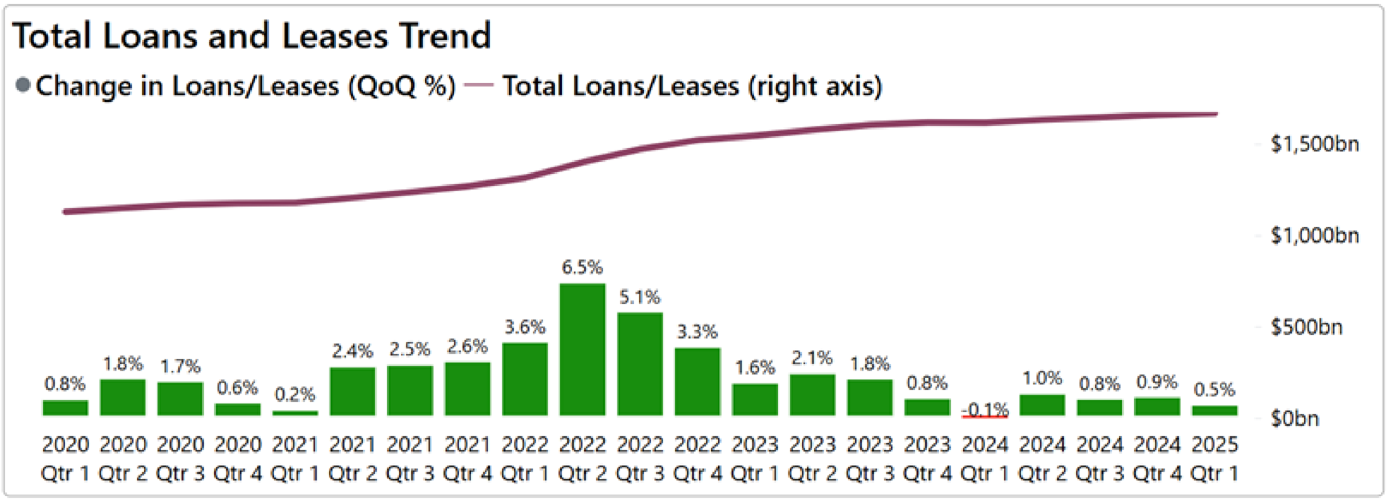
The market forecast, as derived from fed funds futures contracts, sees lower rates through 2027 compared to Fed FOMC projections and then higher rates in 2028. The futures market forecast is volatile. In Q1 2025, futures pointed to higher rates than the Fed forecast.



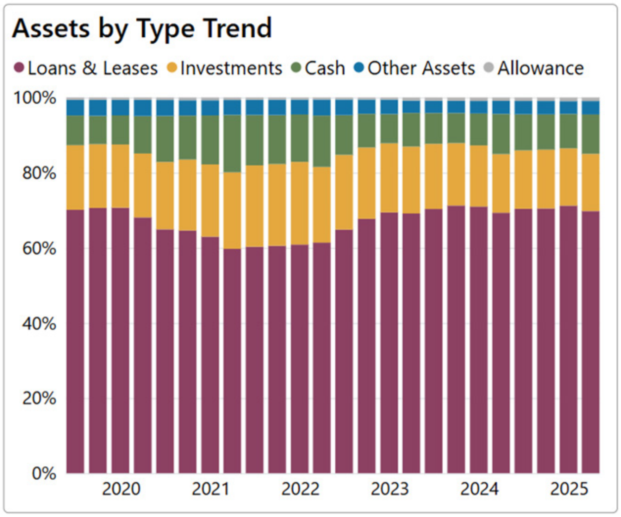


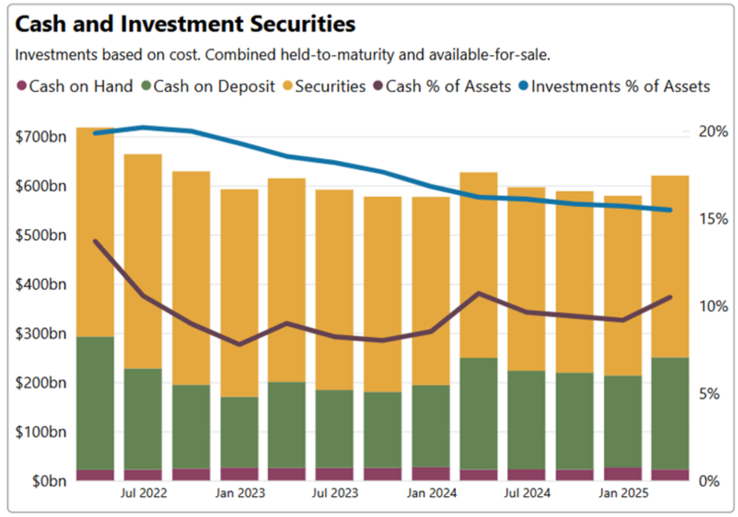
Total assets increased by 2.57% in Q1 2025, the largest quarterly increase in assets since Q1 2022. The credit union industry loan book expanded 50 basis points in Q1 to $1.67 trillion. Loan type composition remained stable with a slight decrease in autos offset with a marginal increase in mortgage loans.



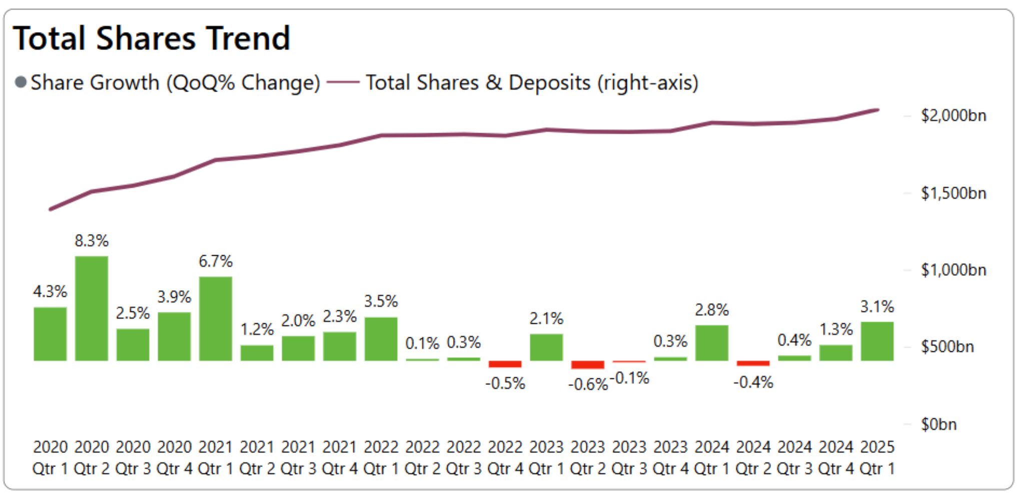


Even with $137 billion in loan originations during Q2, the largest change by asset type composition was the increase in credit unions' cash holdings. Cash increased from $213.6 billion to over $250 billion, or 10.5% of assets, the largest cash position since Q1 2022. While cash increased, cash as a percentage of assets is still below 2022 levels. Investments as a percentage of assets continue a steady decline to 15% from 20% in 2022.

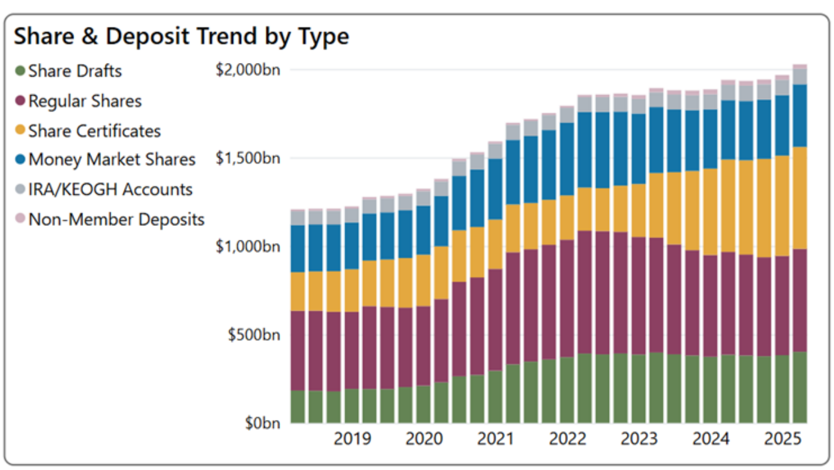


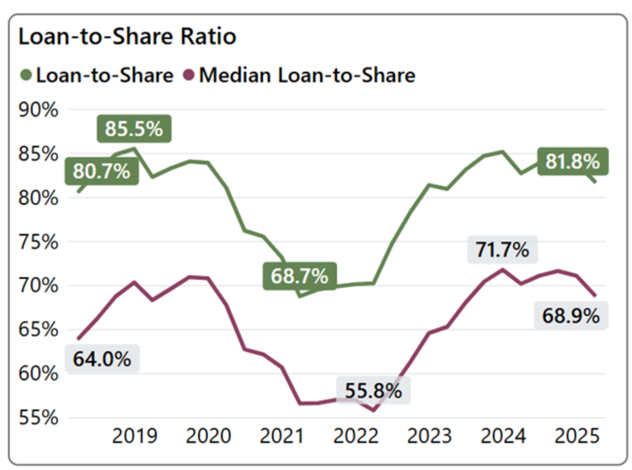


Shares increased 3.1% in Q1 2025, surpassing the impressive milestone of $2 trillion. Although the composition of share type continues to shift from regular shares to share certificates, the trend chart below shows the broad-based growth in all share types.

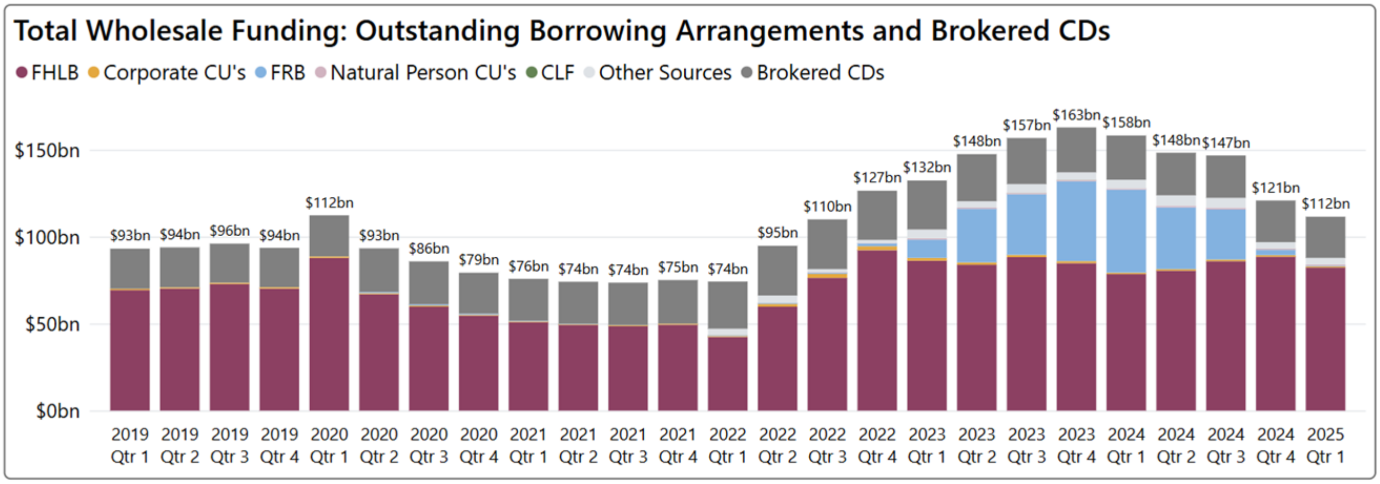


The higher share versus loan growth led to a 2% drop in the loan-to-share (LTS) ratio. The industry LTS fell to 81.8% while the median credit union LTS is 68.9%.

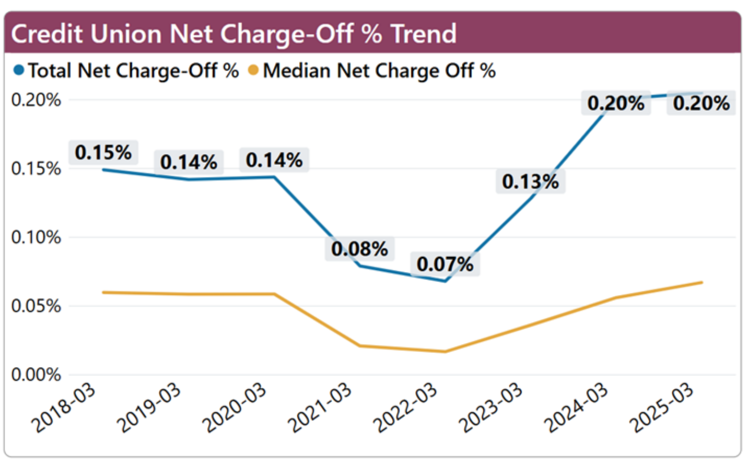


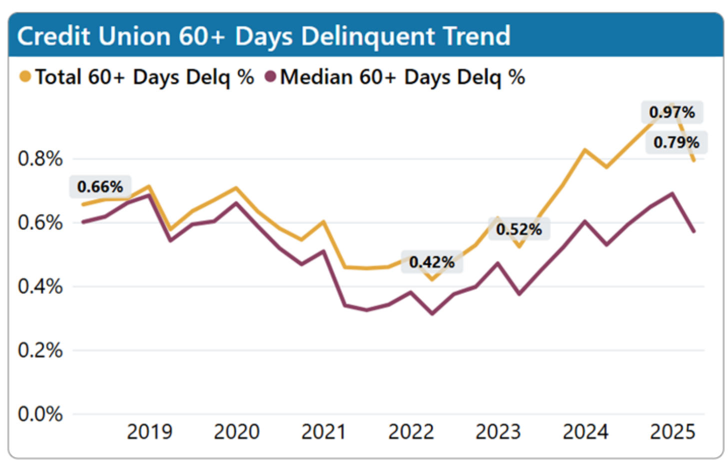


Wholesale funding fell for the fifth consecutive quarter to $112 billion. The industry's total wholesale funding ratio decreased to 5.2% from 5.8% of liabilities. Even Federal Home Loan Bank (FHLB) advances decreased, which had been recently increasing as advances replaced maturing Federal Reserve borrowings from the legacy Bank Term Funding Program (BTFP). Note the expanding then contracting light blue Fed borrowings in the Total Wholesale Funding chart below.

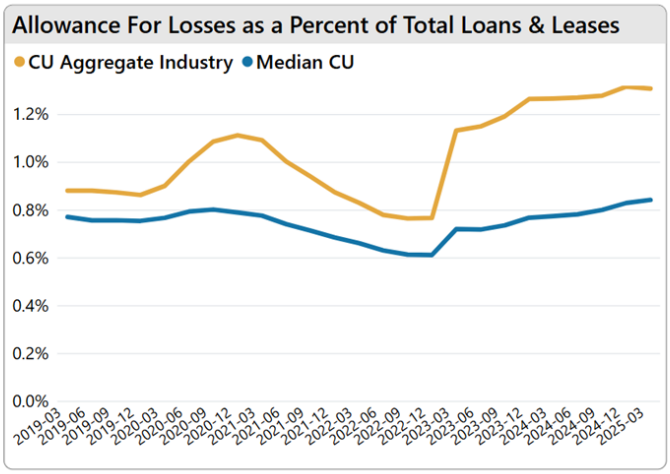


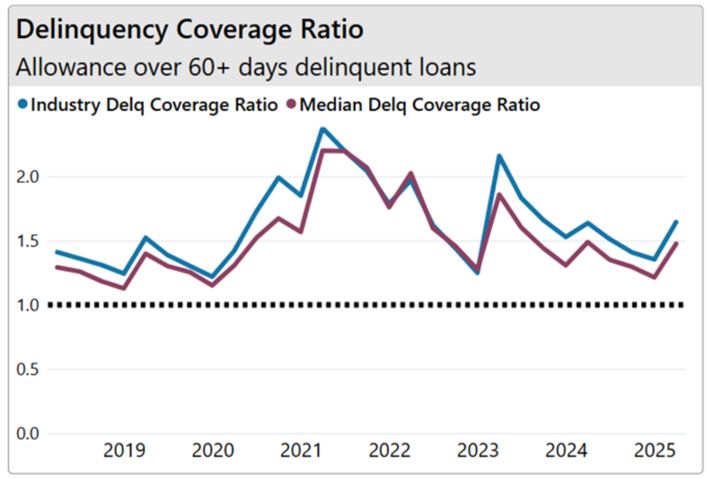
The National Credit Union Administration's (NCUA) **2025 Supervisory Priorities (Letter NO: 25-CU-01)** returned credit risk to the headline priority. Individual credit union performance varies; however, industry performance shows signs of improvement. Net charge-offs were flat quarter over quarter, a welcoming respite after many quarters of rising losses. The first quarter net charge-off ratio was 20 basis points, in line with 2024 and still elevated from pre-COVID era norms. The median credit union's year-to-date charge-off ratio increased slightly from six to seven basis points from Q1 2024 to Q1 2025. The total industry 60+ days delinquent percentage decreased 18 basis points to 0.79%, while the median credit union decreased to 0.57% of outstanding loan amounts 60+ days delinquent.





All else equal, these improved delinquency numbers strengthen credit unions' loan loss allowance. The allowance set aside for loan losses remains just under $22 billion or 1.31% of outstanding loans, while the median credit union allowance increased to 84 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 one means the credit union has a dollar of loan allowance for every dollar 60+ days delinquent. The total industry delinquency coverage ratio increased to 1.64 as of Q1 2025, while the median credit union DCR increased to 1.48.

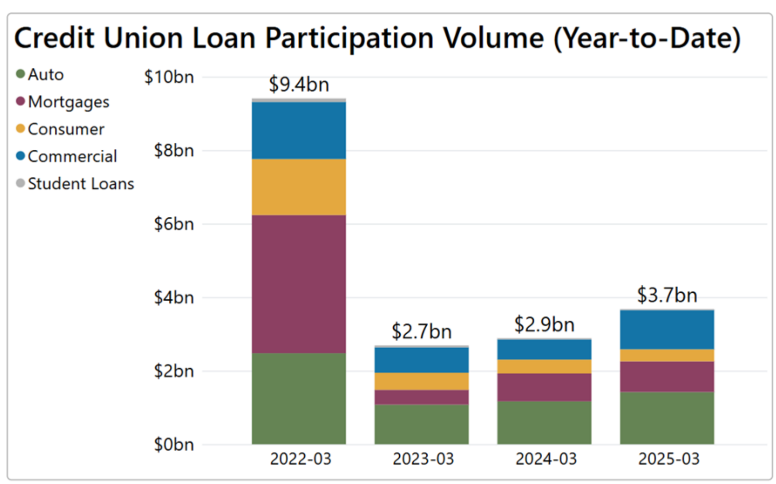




LP MARKET OVERVIEW

Loan participations are currently being used by 45% of credit unions to better manage their balance sheet and risk profiles. NCUA examiners look for current and prospective sources of liquidity regarding a credit union's liquidity risk management framework, and nearly half of credit unions utilize loan participations to meet their liquidity management needs. In Q1 2025, credit unions participated out over $3.7 billion, compared to $2.9 billion through Q1 2024. The loan type composition of loan participation volume remains consistent with prior years, with additional participation activity in commercial loans. New volume exceeded runoff for the fifth consecutive quarter with loan participations outstanding over $63.5 billion as of Q1 2025.

	3/31/2025
CU's with LP Outstanding	2012
% of CU's with LP Outstanding	45%
CU's with LP Purchased	1921
CU's with LP Sold	865
5 Yr Change in # of CU's with LP	56
5 Yr Change in % of CU's with LP	3%
LP Purchased Outstanding	$64bn
5 Yr $ Change in LP Purchased Outstanding	$30bn
5 Yr % Change in LP Purchased Outstanding	87%



FINAL THOUGHTS

Crude oil initially climbed over 10% following Israel's strikes on Iranian targets and the escalation of regional tensions — particularly after the U.S. joined with airstrikes. However, prices have since retreated, falling back below $65 per barrel at the time of this writing.

In today's fluid capital markets environment, oil remains a key barometer. Unlike headlines crafted for attention, oil prices often distill complex geopolitical and economic developments into a more objective probability signal. The recent pullback suggests market expectations of de-escalation and improving sentiment.

Given the backdrop of rising interest rates, geopolitical uncertainty and a significant shift in the Treasury yield curve, what should credit unions consider when identifying relative value opportunities?

Alloya's Capital Markets Group designs solutions to manage liquidity and investments across all our members' unique situations. Have questions? Feel free to contact Brian Myers, Assistant Vice President, Loan Transaction Services at **brian.myers@alloyacorp.org.**