CUEG

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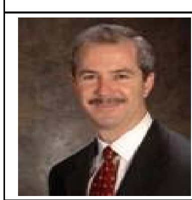	**Eli Vazquez**: Eli Vazquez is Senior Vice President and Chief Financial Officer of American Airlines Federal Credit Union in Fort Worth, Texas, a position he's held since 2006. Mr. Vazquez joined AA Credit Union in 2005 as SVP of Financial Services. Prior to American Airlines CU, Mr. Vazquez worked for American Airlines in several capacities. Mr. Vasquez holds a bachelor's degree in chemical engineering from Tulane University and a master's degree in business administration from the University of California at Berkeley.
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Executive Summary

- As of December 2010, federally insured credit unions' (FICU) asset growth was 3.4 percent. Region II showed the greatest result with 7.2 percent growth in total assets compared with a negative 0.4 percent in Region V.

- Return on average assets (ROA) for all federally insured credit unions' was 0.17 percent. Compared to December 2009, ROA for all FICUs fell by 3 basis points in December 2010. Region II showed the greatest result with an ROA of 0.22 percent in 2010.

- Share drafts saw an increase of 5.6 percent for all FICUs in 2010. Region II experienced the largest growth of 9.2 percent, compared to 1.6 percent in Region V. Overall, share growth was up 4.5 percent. Money market shares were the principal factor driving share growth in 2010, growing 11 percent and accounting for 51.5 percent of total share growth.

- New vehicle lending declined by 16.4 percent in 2010 on the national level, with Region V reporting the strongest decline of 73 percent. In Region II used vehicle loans rose by 6.4 percent, while new vehicle loans decreased by 16.3 percent. Region IV reported the smallest decline (2.2 percent). Used vehicle lending grew 3.4 percent nationwide in 2010.

- First-mortgage real estate loans grew by 2.7 percent during 2010. Other real estate loans experienced a 6.3 percent decline. First mortgages continued to be the lion's share of FICU loan growth, although the weakened housing market has caused a slight decline in overall real estate loan growth.

- In December 2010, the delinquency ratio decreased slightly by 6 basis points from December 2009 to 1.74 percent for all FICUs. Across the country, the delinquency ratio was as low as 1.34 percent in Region II and as high as 2.31 percent in Region V.

- With the likelihood of non-interest income decreasing because of new burdensome regulatory reforms (e.g., limitations on interchange income which will likely reduce fee income), several credit unions would be left with negative net income if they could not apply non-interest income to their bottom lines. This fear coupled with an uncertainty about NCUA premiums in 2011 will leave many credit unions cautious moving forward

- Credit unions will be evaluating their membership in corporate credit unions. Cooperative effort will be required to make sure credit unions continue to benefit from their ownership of corporate credit unions, which includes vital access to payment systems, investments and liquidity. These challenges are expected to lead to a more rapid rate of consolidation of corporate credit unions in 2011.

CUEG Region One

CUEG Region I (Northeast) consists of the states Connecticut, Maine, Massachusetts, Michigan, New Hampshire, New York, Rhode Island and Vermont. As of December 2010, there were 1,255 federally insured credit unions in the region, with total assets of $148.1 billion and total membership of 14.1 million.

Lending

Loans in Region I during 2010 grew by a positive 1.8 percent to $89.4 billion, more than the negative 1.3 percent pace for all federally insured credit unions (FICUs) nationwide. During 2010, loan growth was concentrated in first-mortgage real estate loans and, to a lesser extent, used vehicle loans. The region's credit unions experienced a relatively stronger demand for first-mortgage loan products than found nationwide, while home equity lending contracted less than the negative figure found nationwide. During this year, first-mortgage lending expanded by 5.2 percent, while other real estate loan demand (home equity/second mortgage) declined by 3.3 percent. At year-end, real estate loans comprised 62.1 percent of all loans in the region. Vehicle loan portfolio growth declined during the 2010. New vehicle loans decreased 13.1 percent during 2010 compared to an increase of 6.6 percent during 2009. Used vehicles rose during the year, posting gains of 6.2 percent.

Just like all FICUs, credit unions in Region I experienced an increase in unsecured lending growth. *(Note: Growth in credit card (CC) lending and non-CC unsecured lending slowed in all regions.)* During 2010 credit card lending increased by 3.3 percent, while non-credit card unsecured lending increased by 0.5 percent over the same period. Despite the positive loan growth found among regional credit unions, the loan-to-share ratio fell from 73.5 percent in 2009 to 71.0 percent in 2010 because savings growth outpaced lending. Thus the liquidity among regional credit unions improved on average last year.

Member business loans outstanding grew 16.1 percent to $6.1 billion.

Credit union leaders have indicated that their near-term expectations for loan demand in new vehicles was tied as the most unfavorable (negative) expectation than credit unions in other regions. For used vehicle loan was the highest (positive) expectation than other regional credit unions. Unsecured loans was the third lowest (negative) and real estate loans were the third most unfavorable (negative) expectation than credit unions in other regions. The closest expectation to that of all credit unions was for real estate loans and used vehicle loans; where the region's credit unions were slightly less negative than all credit unions in real estate loans and less positive in used vehicle loans. It is expected that unsecured lending will remain low in 2011.

Member Shares (Savings)

During 2010 total share growth in Region I was 5.8 percent, much higher than the 4.5 percent share growth experienced among all FICUs. Many FICUs in the region saw share growth in regular shares and money market shares outpacing the figures for all credit unions, increasing by 11.1 percent and 13.6 percent, respectively. As many regional credit unions experience a decrease in share certificates, IRA accounts have seen positive growth, negative 3.6 percent growth and positive 4.6 percent growth, respectively, during 2010. “Other” shares also saw an increase of 8.6 percent. The interest rates among the CD have been declining and the largest decline has occurred for the 2 and 3 year jumbo CD rate last year (minus 59 basis points). This has helped to keep the cost of funds low and support the improvements in net income.

Many of the region’s credit unions anticipate share growth to remain near neutral over the near term this year while credit unions in other regions expect share growth to decline slightly. Last year, negative loan demand- coupled with stronger share growth- caused the region’s credit unions’ loan-to-share ratio to decrease from 73.8 percent in December 2009 to 71 percent in December 2010. Among all credit unions, the loan-to-share ratio decreased from 76.3 percent to 72 percent over the same time periods.

Earnings and Asset Quality

During 2010 the credit unions in Region I had a return on average assets (ROA) before stabilization costs of 0.73 percent, up from 0.69 percent in all of 2009. This is equal to what all FICUs experienced as they saw ROA before stabilization increase from a 0.55 percent in 2009 0.73 percent in 2010. While the region’s credit unions’ loan yields were slightly lower than average, the region’s investment yields were higher than those for all FICUs. In addition, the region’s cost of funds was lower than for all credit unions. However, credit unions in Region I generated, on average, substantially less non-interest income than everyone else. *(Note: Fee income as a percent of total assets was second lowest among the regions).*

The asset quality in the region was better in comparison to the asset quality of all FICUs during last year. The delinquent-loans-to-total-loans ratio in the region was 2.72 percent compared to 3.22 percent for all FICUs, while the net charge-offs-to-average-loans rate of 0.78 percent in the region was lower than the overall rate of 1.13 percent. During 2010, member bankruptcies were less of a problem in Region I when compared to other regions. The loan amounts subject to bankruptcy as a percentage of loans outstanding decreased significantly. However, the total number of bankruptcy filings in the region increased by 1.4 percent to 147,082 and the loan amounts subject to bankruptcy decreased from $590.1 million in 2009 to $553.9 million.

Many credit unions are working harder than ever to identify cross sell opportunities. Most members have relationships with multiple financial institutions. Converting these loans that have been made to existing members may be more cost effective than recruiting new members. Many credit unions have found this to be a cost effective method of deepening relationships with existing members and at the same time increasing corporate profitability.

Competition and Credit Union Operational Concerns for 2010

In contrast to other parts of the country, Region I credit unions are seeing their delinquency rates improve slightly as well as net charge-offs (declining ratios from prior year). Also bankruptcies appear to be falling as seen by the lower percentage for loans subject to bankruptcies. In Region I, specifically, there have been concerns about the rising home foreclosures and the rising level of regional unemployment rate (increase from 8.18 percent in 2009 to 8.49 percent in 2010). Credit unions in this region are being forced to adjust their budgets in the hope that the economic expansion will translate to more loans. Despite these growing trends, most credit unions still want to make loans without sacrificing future loan quality.

Although credit unions have not tightened lending standards like other financial institutions, some credit unions have noticed that the quality of lending application have improved slightly. However, the loan volume remains tepid. This implies that further improvement in consumer balance sheets is needed to encourage more borrowings. Credit unions are finding that more operational efficiency is necessary in this economic environment. With limitations on the ability to generate income, expense reduction has become the next reasonable alternative to increase net income. Once recognize, to some degree ignored, credit unions with low operating expense ratios have a significant competitive advantage over less efficient organizations.

The decline in net worth ratios despite improving ROA has caused many credit unions to reevaluate certain expenditures. In particular, many credit unions have reduced their marketing and travel/education expenses. Such reductions may increase pressure on future credit union performance, especially when competing with banks and other financial institutions. In addition to cutting expenses, credit unions are trying to attract low cost sources of funds. However, share certificates are a declining source of funds as members seek higher returns.

Like credit unions nationwide, Region I credit unions are still contemplating how the National Credit Union Share Insurance (NCUSIF) premium and Corporate Credit Union Stabilization assessments will affect their future financials. As the prospects for more premium and assessment costs continue into the future, most credit unions will have to adjust their budgets to account for these events. These expenses have caused many credit unions to think more about their operational efficiency.

Member Concerns and Economic Conditions in 2010

Members of Region I credit unions remain concerned about the economy and its implication for 2010 and beyond. If the Fed keeps the interest rates low, it is likely that credit unions' cost of funds will decline further and compressed margins will thus be alleviated to some degree. However, the experience of low loan demand has forced many credit unions to find alternative revenue sources. Credit unions are hoping that the economy will improve further, especially in the area of employment.

The weak lending last year, especially new vehicle loans coupled with a lower quality of applicants has made weak prospects for strong growth in loans in the near term. The end of government programs, elevated unemployment, consumers hesitating to spend will further curtail loan demand. The economy needs to expand significantly for consumers to spending at robust levels. Rising foreclosures and bankruptcies will also depress real estate loan performance. Members who are unemployed or under employed are unlikely to pay their debts in a timely manner. Additionally, decreased home values have caused members to evaluate the pros and cons of continuing to make payments on mortgages that are under water. Provision for loan losses expenses have grown to a significant level for most credit unions. With the economy improving marginally (uncertainty in financial markets, elevated unemployment and low improvement in consumer spending) it is unlikely that there will be a sharp increase in market interest rates in the foreseeable future.

With the likelihood of non-interest income decreasing because of new burdensome regulatory reforms (e.g., limitations on interchange income which will likely reduce fee income), several credit unions would be left with negative net income if they could not apply non-interest income to their bottom lines. This fear coupled with an uncertainty about NCUA premiums in 2011 will leave many credit unions cautious moving forward.

CUEG Region Two

NCUA Region II (Mid-Atlantic) consists of the states Delaware, Maryland, New Jersey, Pennsylvania, Virginia and West Virginia, plus the District of Columbia. The region's federally insured credit unions (FICUs) have 17.1 percent of the total assets of the nation, up by 0.6 percentage points from December 2009. There are 14.4 million members in this region as of December 2010, up from 14 million (2.9 percent increase) from December 2009. These percentages mirror the regional economy where the gross domestic product by state is about 13.7 percent of the U.S. gross domestic product. Regional production is more concentrated in professional services, government and health/education services than the average concentrations found nationwide.

<u>Lending</u>

Region II FICUs generated positive loan growth of 0.4 percent in 2010, compared to the national rate of negative 1.3 percent. Although it is a small component of total loans outstanding, business lending experienced the sharpest growth, increasing 31.7 percent in 2010. First mortgage loans grew by 4.6 percent during the year. Region II FICUs expects used vehicle lending to be greater than those in other regions over the next 12-month period.

Total vehicle loans in Region II decreased by 4 percent during 2010, compared to a rate of negative 5.2 percent for all FICUs. In Region II used vehicle loans rose by 6.4 percent, while new vehicle loans decreased by 16.3 percent. Looking forward to 2011, Region II FICUs anticipates lower loan growth for new vehicle loans than do FICUs in other regions.

Unsecured loans (excluding credit cards) represent 6.3 percent of all FICU loans in the region. This portfolio segment has increased by 1.5 percent during 2010. Credit card loans increased 5.7 percent during the same period, representing 11 percent of all FICU loans in the region. The credit union leadership in the region believes that unsecured loans will be less of a source for loan growth for the near term, and more pessimistic than that found among all credit unions across the country.

<u>Member Shares</u>

Total savings and deposits reached $127.8 billion in December 2010, up $8.2 billion (6.9 percent growth) from December 2009. During the period, Region II FICU share drafts (11.7 percent of Region II shares) increased 9.2 percent. Regular shares (26.7 percent of Region II shares) increased 11.3 percent during the same time period. Money market share accounts (20 percent of Region II shares) reached $25.6 billion as of December 2010, up by $3.1 billion (14 percent growth) from 2009. FICU share certificates (29.4 percent of shares) experienced a 1.5 percent decrease during 2010. IRA accounts (11.4 percent of FICU shares) were a safe haven for members' precious retirement funds in

2010. This deposit segment advanced 6.5 percent from 2009 compared to a national growth rate of 4.1 percent. For the next twelve months, the share growth anticipated by Region II FICUs is slower than the overall expectations.

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

Region II's credit unions experienced growth in consolidated ROA during the first half of 2010. At 0.70 percent (ROA for all FICUs was 0.51 percent) this profitability measure increased by 20 basis points since 2009 for the region's credit unions. This figure includes the National Credit Union Share Insurance Fund (NCUSIF) premium of 12.4 basis points and the Stabilization Fund assessment of 13.4 basis points. Comparing income before these costs, Region II ROA was 0.90 percent in 2010, up from 0.84 percent in 2009. This increase in ROA is mainly due to the decrease in cost of funds, which has declined from 1.99 percent in 2009 to 1.49 percent in 2010. We expect to see asset yields stabilize as most of the older loans and investments have re-priced to current market rates, and the overall cost of funds remain low throughout 2011. We continue to see non-interest income and expenses remain steady. These factors, when taken together, point to a fairly steady or slightly increasing ROA.

Gross income increased by 0.7 percent from $8.08 billion in 2009 to $8.14 billion in 2010. Fee income/average assets declined by 1.4 basis points from 2009 and operating expenses/average assets increased by 10.5 basis points.

Loan Loss Trends

In the area of loan quality, Region II FICUs had lower delinquency and charge-off ratios than credit unions nationwide during 2010. Reportable delinquencies (those which are 60 days late or more), fell from 1.41 percent in 2009 to 1.34 percent. The decline in unsecured credit card delinquencies contributed 45.6 percent of the overall decline. Net chargeoffs declined slightly, from 1.13 percent in 2009 to 1.09 percent through December 2010. During this period, mortgage chargeoffs increased from 0.07 percent to 0.10 percent. Region II FICUs experienced a lower loan exposure to bankruptcies compared to the pattern found among credit unions nationwide. During 2010 the portion of total loans subject to bankruptcy was 0.75 percent among Region II FICUs, while nationwide the ratio was 0.88 percent.

Member Concerns and Region II Economic Conditions in 2010

Credit union leadership in Region II stated they have gotten strong savings growth, despite having reduced the interest rate and this is making managing asset growth more difficult. Some credit unions believe that this savings growth may be due to the more stable economy found in the region when compared to other parts of the country.

Bankruptcies and real estate foreclosures will continue to be a focus over the coming year. The region has not reached a point of price stability in the housing markets, so there will be continued pressure from 1st mortgage loans that are "upside down" and 2nd mortgage loans that are essentially unsecured. There is similar concern that credit card loan portfolios will continue to underperform because of large losses. Some credit unions have indicated that the trend of members resolving such problems may continue throughout the year.

The anticipation of NCUSIF and Corporate Credit Union Stabilization costs this year has created some anxiety and uneasiness among regional FICUs. There is still too much uncertainty around the amount of the premium for this year. The amount budgeted by some credit unions have been 25 basis points. Some credit unions in this region have put business plans on hold or modifying them as a response to the Nation Credit Union Administration recommended premium range (20 to 35 basis points). This is a major source of concern among FICUs, and the NCUA needs to continue working with FICUs in order to provide more transparency to the situation.

CUEG Region Three

CUEG Region III (Southeast) consists of the states Alabama, Florida, Georgia, Indiana, Kentucky, Mississippi, North Carolina, Ohio, South Carolina, and Tennessee, and of the territories Puerto Rico and U.S. Virgin Islands. It finished 2010 with 1,502 federally insured credit unions (FICUs). This represents a net decline of 53 or 3.41 percent of Region III FICUs over the past year. Region III holds 20.47 percent of all FICUs, 19.5 percent of all assets and 22.4 percent of all FICU members. Total assets in the region rose to $178.4 billion. This translates into an annual growth rate of 2.5 percent, which is 0.9 percentage points below the reading for the nation as a whole. Membership in the region climbed to 20.3 million, up 176,000 over the past year. Membership growth in Region III was at 0.9 percent in 2010 and was above the 0.7 percent national average rate of increase. Total employment (full- and part-time FICU employees) was 55,347, which was a 0.3 percent year-over-year reduction. The 50 largest FICUs in the region hold 53.9 percent of all assets and 43.7 percent of the total membership in the region. Included in this group are 35 FICUs with assets in excess of $1 billion.

Region III covers a wide expanse of geography. The impact of the recession continues to affect this region, especially credit unions in Florida, which is known as one of the sand states impacted greatly by declining home values. Mergers continue to be a major factor impacting credit unions in the region as today there are 53 fewer credit unions in the region when compared to one year ago. Loan growth is more negative and savings growth was slightly higher than found among other credit unions nationwide. Managing the margin squeeze along with improving loan quality are priorities for credit unions in the region as credit unions remain concerned over elevated levels of unemployment.

Credit unions in the region are working to get the message out to consumers and businesses that, as an industry, credit unions remain fiscally safe and sound and have money to lend. As of December 2010, Region III FICUs collectively remained in good health and their net worth ratio rose to 10.4 percent from 10.2 percent at year-end 2009. Region III annualized Return on Average Assets (ROA) increased by 22 basis points to 0.48 percent over the past year. Loan delinquencies climbed to 1.98 percent of total loans, up from 1.9 percent at the end of 2009. Net loan charge-offs declined 8 basis points while provision for loan losses decreased 27 basis points.

Extraordinary events during 2010 have had a materially negative impact on financial performance. The costs of resolving the conservatorship of corporate credit unions are a concern of many of the region's credit unions. The NCUA estimated that losses, in excess of capital among the five conserved corporate credit unions, would total $6.4 billion.

The NCUA estimates that the combined Corporate Stabilization assessment and National Share Insurance Fund (NCUSIF) would cost credit unions between 20 basis points and 35 basis points during 2011. In 2010 the total cost was 25.8 basis points.

Lending

At negative 1.3 percent, annual loan growth in Region III was the same as the national average. The 153 FICUs in Georgia posted the strongest annual loan growth at 3.6 percent. FICUs in Florida and South Carolina posted the lowest performance in loan growth with decreases of a negative 6.4 and a negative 2.3 percent respectively.

At 69.4 percent, the loan-to-share ratio was down 3.8 percent over the past year. Region III FICUs are under-performing the total U.S. which had a loan-to-share ratio of 71.8 percent. The U.S. loan-to-share ratio has declined 4.3 percent year-over-year.

A $1.1 billion gain in first mortgages and lines of credit accounted for 18.1 percent of all loan growth year-over-year while new vehicle lending fell $2.7 billion during the year. Despite the crisis in the overall housing market, first mortgage originations totaled $7.5 billion. First mortgage originations decreased to a similar level found in 2007 ($10.9 billion) and were largely driven by refinancing activity. First mortgage loan sales to the secondary market were $4.8 billion for the regional credit unions and produced a 2.4 percent year-over-year first mortgage portfolio gain. When the 4.5 percent drop in home equity and second mortgages is added to first mortgages, the combined real-estate portfolio segment accounted for 54.1 percent of total loans for FICUs in Region III. Credit card and used vehicle lending were also growth segments in 2010 with 2.5 and 2.9 percent growth rates respectively.

An 18.1 percent contraction in new vehicle loans outstanding for Region III FICUs was partially offset by the 2.9 percent increase in used vehicle portfolio. However, total vehicle loans outstanding in the region declined 5.7 percent in 2010.

The economic recovery has shown early signs of sustainability during 2010; however, consumers' utilization of credit displays the trends typical of the recent economic recession. New vehicle and home equity lending declined while credit card balances, used vehicle and first mortgages posted positive gains. The similar trend in distressed member's repayment patterns continues as keeping access to credit card lines of credit is a priority for individuals whose home values have declined.

The foreclosure process was slowed nationally in 2010 as the large national banks legal review processes for foreclosures was challenged. This appears to be behind us but we continue to see long delays for getting foreclosures cleared by courts in many areas and off the balance sheets of the large financial institutions. The real estate market is reporting increased activity in many markets but a deeper look at the data reveals this to be largely driven by short sales. Unemployment concerns and low home values continue to impact the willingness of consumers to take on new debt. However, low mortgage loan rates, especially for terms of 15 years or less, kept the mortgage refinance market alive for last year.

A total of 370 FICUs in Region III reported having an indirect lending channel, compared to 360 FICUs at year-end 2009. Indirect loans outstanding are down 7.5 percent over the past year and now account for 11.25 percent of total loans.

Total Member Shares

During 2010, total shares in Region III rose 4.1 percent to $155.5 billion. This gain was close to the national average of 4.5 percent. Share drafts, regular shares, money market shares and IRA/KEOGH accounts all posted annual growth while share certificate balances fell 6.7 percent across Region III. Sharp increases in regular shares and money market accounts combined with falling certificate concentrations indicate an increasing balance of “hot” money on the balance sheet. The 153 FICUs in Georgia and 99 FICUs in North Carolina generated the strongest rates of share growth during 2010 recording gains of more than 6 percent.

The low interest rate environment and a multi-year shift in the savings structure away from higher cost CDs have moved Region III FICUs’ cost-of-funds down 53 basis points to 1.2 percent of average assets over the past 12 months. Given the economic uncertainty, slowing loan demand and a growing savings rate, we expect the cost-of-funds to continue drifting downward, although at a slowing rate by the middle of 2011. Managing the cost-of-funds will continue to be important as one of the tools that credit unions in the region exercise in working to absorb higher loan losses and the anticipated additional charges from the NCUA. It will be imperative that credit unions manage growth in deposits in relation to loan demand and capital growth.

Asset Quality and Operational Results

At year-end 2010, the annualized ROA for Region III FICUs was 0.48 percent, reflecting a 22 basis point increase from the December 2009 level. A total of 943 FICUs (62.7 percent of the region’s FICUs) reported a positive ROA, while 559 reported losses or no gain for 2010. The FICUs with a negative ROA represented 13.8 percent of the region’s assets. This is an improvement from the prior year, which showed 24 percent of the region’s assets were at a negative ROA institution.

A pervasive combination of slow economic recovery and continued high unemployment has adversely impacted asset quality. The loan delinquency rate was up 8 basis points in 2010 to 1.98 percent of total loans. The national FICU delinquency rate at year-end 2010 was 1.74 percent of total loans, down 10 basis points year-over-year. Over the same period, net charge-offs decreased from 1.21 percent of average loans to 1.13 percent nationwide and from 1.18 to 1.10 percent among FICUs in Region III.

One measure of operating efficiency (the ratio of operating expenses to average assets) was down 18 basis points year-over-year to 3.46 percent. Expenses related to share insurance costs, office occupancy and loan servicing were growing the fastest. This growth is reflective of costs associated with the corporate credit union stabilization, recession level loan performance and loan growth plus credit unions growing to fill the void created by traditional competitors pulling back.

Loan demand and credit quality continue to be a concern. New vehicle loan volume has been anemic and while there have been pockets of demand for mortgage refinances; the purchase mortgage market has been slow to return. Home values have not stabilized and are not expected to until a back-log of foreclosures are liquidated and unemployment improves. Rising gas prices may have some impact on the value of used vehicles but the pipeline of repos remains constant. As far as improved efficiencies relating to operating expenses are concerned, credit unions have taken steps to reduce staffing as a result of lower production volumes and, in some areas, branch closures (regional credit unions have reduced part-time staff, but have increased full time staff). The challenge will be to leverage technology and to assure that service does not suffer as the result of these reductions.

Looking forward, we see significant challenges and opportunities for Region III and all FICUs. We are seeing some stabilization of the U.S. and global economies and the national unemployment rate has fallen from its highs. Credit unions will be evaluating their membership in corporate credit unions and the need for many to make new capital contributions under revised business plans. Cooperative effort will be required to make sure credit unions continue to benefit from their ownership of corporate credit unions, which includes vital access to payment systems, investments and liquidity. These challenges are expected to lead to a more rapid rate of consolidation of corporate credit unions in 2011.

In aggregate, the capital cushion appears to be adequate, but individual FICUs will struggle to increase their provision for loan losses and to maintain capital levels. As the economy recovers and employment improves, the current challenges of slow loan demand may improve while the uncertain impact of governmental regulations, like Durbin on debit interchange income, remain troublesome. The opportunity will be to leverage the disruption that consumers faced during the crisis and gain the ability to attract new profitable members. Emerging successfully from the recession will require FICUs to sustain strong lending initiatives and a culture that can acquire and maintain relevance with active members.

CUEG Region Four

NCUA Region IV (Austin) consists of 2,191 federally insured credit unions (FICUs) in the states of Arkansas, Illinois, Iowa, Kansas, Louisiana, Minnesota, Missouri, Nebraska, North Dakota, Oklahoma, South Dakota, Texas, and Wisconsin as of year-end 2010. The credit unions in this region represent 29.9 percent of all FICUs and with total assets of $189 billion, hold 20.6 percent of all FICU assets. Total membership in Region IV reached 20.1 million and now accounts for 22.2 percent of all FICU members. A high level summary shows a net loss of 59 Region IV FICUs during 2010, but asset growth in excess of 5 percent. Region IV FICUs added 262,000 members in 2010 and loan growth of 2.2 percent was in sharp contrast to the 1.3 percent decline for the total market. The net worth ratio improved slightly, but remained just fractionally below 10.1 percent. At the end of 2010, total employment (full and part-time FICU employees) was 58,380 and there were 5,414 branches within the region. The 50 largest FICUs in the region held almost 46 percent of all assets and over 35 percent of the total membership. Included in this group are 30 FICUs with assets in excess of $1 billion.

Loan Growth

Region IV FICUs generated 2.2 percent loan growth in 2010, down from 6.2 percent in 2009. FICUs in Region IV added $2.5 billion to loans versus a $7.7 billion decline for the nation as a whole. Total loans outstanding in Region IV now equal $118.6 billion, representing 62.9 percent of total assets down from 67.7 percent just two years ago. Roughly 68 percent of all loan growth in 2010 was attributable the 50 largest FICUs.

Over the course of 2010, first mortgages and used vehicle loans were the largest components of loan growth. First mortgages increased 6 percent during the year and accounted for over 87 percent of all loan growth. Used vehicle loans rose 8.5 percent in 2010 and accounted for over 85 percent of Region IV loan growth. Large declines were reported in new vehicle and other real estate loans.

While down from 2009's record pace, 2010 was another solid year for originating member real estate secured loans. A total of $17.4 billion in first mortgages were originated in 2010, the third highest year ever. Roughly 75 percent of 2010 originations were in fixed-rate product, 16 percent in balloon/hybrid and just 9 percent in adjustable-rate loans. Other real estate loans granted were down 8.2 percent in 2010 with 5.9 percent growth in HELOCs granted being more than offset by significant declines in second mortgage originations.

FICUs nationwide continue to struggle to maintain their vehicle loan portfolio. While Region IV FICUs saw new vehicle loans decline 9.5 percent, used vehicle loan growth was solid, increasing 8.5 percent during the year. In total, the vehicle loan portfolio in Region IV rose just 0.6 percent. This is in sharp contrast to the entire FICU market, which posted a 5.2 percent decline. In 2010, just 40 percent of Region IV FICUs reported vehicle loan portfolio gains and only 16 percent reported gains in new vehicle loans outstanding. In total, Region IV vehicle loans increased just $253 million in 2010, but point-of-sale indirect loans were up $615 million.

Region IV credit card balances grew 5.4 percent in 2010 and their share of loans increased fractionally to 4.6 percent. Member business loan (MBL) growth of 6.9 percent was solid, but well below 2009's rate of increase. MBLs now equal 7.1 percent of total loans, up 32 basis points over the past year. FICUs in Region IV granted $3.7 billion in MBLs in 2010, up 24.8 percent over 2009 origination volumes.

Shares and Deposits

Total shares and deposits finished the year up $9.8 billion or 6.4 percent. Growth results in 2010 were 6.5 percentage points below a very strong 2009, but 1.9 percentage points more than the national average. Historically low deposit yields were part of an overall strategy to discourage large deposit inflows. Total shares and deposits finished the year at $164 billion, with almost 95 percent of the gain coming from highly liquid accounts (share drafts, regular shares, and money market accounts).

After advancing 7.3 percent in 2009, the CD (or share certificate) component of the deposit portfolio growth 1.3 percent in 2010. The Region IV decline was much less than the 5.4 percent contraction reported by all FICUs. This portfolio segment now equals 28 percent of all deposits, down from 30 percent in 2009. After advancing 16.5 percent in 2009, IRA/KEOGH balances were up 5.8 percent in 2010. At $14.6 billion, this portfolio segment now represents 8.9 percent of all deposits.

Regular shares grew 9.1 percent during the year, but fourth quarter growth slipped to just 1.3 percent. Regular shares were the largest component of deposit growth despite yields below 0.5 percent at 54 percent of all Region IV FICUs. The $4.2 billion increase in this portfolio segment accounted for 43 percent of all deposit growth in 2010 and regular shares now equal 31 percent of all deposits.

2010 was a year where credit unions intentionally kept deposit rates low. Given low loan and investment yields, plus net worth ratio management, this was necessary. This action benefited cost-of-funds and helped improve spreads. Again, we expect members to remain liquid in anticipation of higher CD yields likely over the next couple of years. Due to the lack of demand for short-term consumer loans and/or FICUs not wanting to hold low-yielding fixed-rate loans, deposit pricing will remain low. Additionally, we see some credit unions intentionally managing deposit and asset growth down (to improve the net worth and other key ratios); this implies slow share and deposit growth again in 2011.

Loan Quality

Over the course of 2010, loans two or more months delinquent as a percent of total loans outstanding (delinquency ratio) fell to 1.4 percent or 15 basis points below the year-end 2009 level. Delinquent loans now equal 0.88 percent of assets. In addition to lower delinquencies, charge offs moved down from 0.86 percent of average loans in 2009 to 0.79 percent at year-end 2010. Both key measures of loan quality in Region IV improved in 2010 and they remained much better than the results for the nation as a whole. Looking at high level detail, we see that real estate secured loans (first mortgages, second mortgages and home equity loans/lines of credit) two or more months delinquent rose just 1.5 percent in 2010, but the real estate delinquency ratio fell to 1.48 percent. Credit card delinquencies fell almost 19 percent to 1.5 percent of outstanding balances. With net charge offs down 4.6 percent in 2010 and the provision for loan losses falling 17.5 percent, many in credit union leadership positions believe we have passed the peak of credit quality challenges for this cycle. This conclusion should hold, barring further market shocks and a continuation of the trend of improving employment conditions within the region.

Investments

With deposit inflows outpacing loan growth by almost seven percentage points, Region IV credit union investments rose by almost 13 percent to $48 billion. Investments now equal 25 percent of Region IV assets, up from 19 percent at the end of 2006. When combined with cash and cash equivalents, the year-end 2010 ratio climbs to 33 percent. Given that the yield on average loans is 424 basis points above the yield on average investments, this higher share of cash and investments is dampening growth in the bottom line. Credit unions are challenged to manage growth in deposits with extremely low investment rates. Yield on average investments declined by 68 basis points even as the region's credit unions grew balances in the 3-5 year and 5-10 year maturities by 28.5 percent and 73 percent respectively. This growth in long-term investments could present ALM challenges if we enter a rising interest rate environment.

Earnings and Capital Adequacy

Region IV full-year return on average assets (ROA) was 53 basis points, an increase of 14 basis points from full-year 2009. Estimates show that without stabilization expense and NCUSIF premiums, the Region IV ROA would have been 75 basis points. Region IV results were just fractionally better than the nation as a whole. At the end of 2010, 40 percent of the FICUs in the region reported a negative ROA and these FICUs held 12 percent of the region's assets. Just one credit union with assets over $1 billion reported a negative ROA. The net interest margin improved slightly in 2010 to 3.25 percent as the cost-of-funds declined 50 basis points.

Despite credit quality issues, stabilization assessments, NCUSIF premiums and minimal loan portfolio growth, Region IV FICUs improved the collective net worth ratio to 10.09 percent. This key measure of safety and soundness is fractionally better the national average. A closer look at the data indicates 104 Region IV FICUs had a net worth ratio below 7 percent. These credit unions held just 3.6 percent of the region's assets.

CUEG Region Five

CUEG Region V is comprised of 13 states: Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, New Mexico, Nevada, Oregon, Utah, Washington, Wyoming, and the territory Guam. Looking back on 2010, difficult economic conditions have continued to plague the region, despite the overall rebound being felt in many other parts of the country. The modest gains in both assets and membership experienced in Regions 1-4 remain elusive in the west. Membership declined 1.9 percent (more than 400,000) in 2010 and assets declined 0.36 percent. While still at the lowest levels for all regions, net worth did rebound from 9.11 percent in 2009 to 9.49 percent at the end of 2010. It seems that many credit unions' efforts to lower deposit rates as a means to drive out deposits and protect interest margin and capital position have been largely successful; but with the consequence of driving many consumer deposits away as account holders seek better rates. Nationally, total shares grew 4.49 percent in 2010, but Region V share growth lagged well behind at 1.33 percent. Total shares at year-end were $23.6 billion.

Loan Growth and Trends

Consumer demand for loans continues to be of paramount concern in the industry, and nowhere more urgently than in Region V, where total loan balances fell 6.66 percent in 2010.

New vehicle loans are down across the board for all CUEG regions, but used vehicles have rebounded back to positive figures everywhere except in the West, where those loan balances declined 3.24 percent in 2010.

Reflecting the continuing struggles of the western housing market, real estate loan balances fell 1.69 percent for first mortgages and 9.92 percent for other real estate loans. These declines come at a time when home loan rates are at record lows and the market is flooded with more affordable homes. This suggests several factors are working against home lending efforts. Among these factors are: "cash" purchases steadily rising as investors have stepped-up their presence in many Region V markets; refinance activity continuing at a relatively stagnant pace as home equity remains sparse; consumers continuing to find alternate lending sources for home loan refinancing; and consumer confidence remaining so weak that, despite the many market incentives for the home buyer, consumers are unwilling or unable to take on additional debt at this time.

Nationally, member business loan growth was strong in 2010 with an increase of 7.77 percent. Continuing the trend, Region V did not share in that growth, dropping 1.73 percent. Quarterly trends showed progress in the first half of 2010, only to lose steam in the third and fourth quarters. This will likely remain an area of concern well into 2011, until consumer confidence begins to strengthen.

Loan Quality

Delinquency and Write-Offs are an ongoing concern. During 2010, the delinquency ratio fell from 4.1 percent to 3.85 percent, which is good news, though the majority of that dip came between quarters one and two. That ratio actually climbed 3 basis points in quarter four. Net charge-offs are down slightly for 2010, falling to $2.52 billion (from $2.87 billion). Charge-offs due to bankruptcy climbed in all regions, signaling continued stress on consumers struggling to meet their debt burdens. Region V saw the largest increase in bankruptcy charge-offs, ending the year at $642 million, an increase of $64 million over the previous year. Of particular note are 1st Mortgages, where charge-offs grew almost $78 million in 2010, erasing gains in other areas. The 1st Mortgage Delinquency Ratio's trend has flattened, however, bringing some hope that loan losses in this area should begin to abate. In general, delinquency and charge-offs remain at traditionally unacceptable levels, and overall performance and profitability in the industry will continue to be challenged as long as this is the case.

Shares

Region V's Total Share growth was relatively flat in 2010 coming in at 1.33 percent. As credit unions have struggled to protect their capital ratios, a strategy of lower deposit rates has prevailed, driving many consumers out into the market to seek better rates. Certificate deposits in particular illustrate this trend, losing nearly $7 billion in balances over the course of the year (-11 percent) as consumers chose not to commit to long-term deposits in an extreme low-rate environment and preferring more liquid share and money market accounts. As a result, Regular Shares increased by a substantial 10.3 percent to $5.5 billion. Likewise, Money Market Shares increased 7.3 percent to $3.8 billion. This growth in lower yielding liquid savings accounts benefits credit union net interest margins, but there is a risk that those funds could flee to other institutions' higher long term rates, jeopardizing the industry's ability to fund loan growth when the economy begins to expand.

Investments

Total Investments surged nearly 14 percent in 2010, reaching $64.2 billion by year-end. This was fueled largely by sluggish loan growth and the resulting surplus in cash. Total Cash balances grew $1.5 billion (8 percent), ending the year at $20.5 billion in Region V. Rising long-term interest rates have spurred increased investments in the 5-10 year (up 87 percent to $5.2 billion) and 3-5 year (up 47 percent to $11.3 billion) ranges. With overnight and short term interest rates lingering at near record lows, credit union managers are beginning to invest some of that excess liquidity in longer term investments as a means to shore up meager yields on investment. Region V borrowings decreased 45 percent in 2010, which given heightened liquidity levels, is hardly a surprise. As long as consumer loan demand remains depressed, large liquid cash balances will likely remain the norm.

Earnings and Equity

2010 marked a return to profitability as Region V return on average assets rebounded from a dismal -0.29 percent in 2009 to a positive 0.4 percent in 2010. While still trailing all other CUEG regions, this is welcome news given the struggles of the past two years. The region's $985 million in net income comes as a result of a $1.6 billion improvement in Net Income over 2009 (-$656 million). Region 5 leads the nation in Net Interest Margin, posting a $254 million gain over 2009 levels. As a percentage of average assets, Region V's net interest margin of 3.37 percent is 0.12 percent better than the national average (3.25 percent). Fee Income did decline in 2010. As a percentage of Average Assets, Region V matched the national average at 0.78 percent.

Operating expense did grow in 2010 by 6.7 percent to $7.9 billion. As a percent of average assets, however, Region V's 3.26 percent was actually below the national average (3.29 percent). As discussed earlier, decreased deposit rates served not only to slow deposit growth, but also to reduce interest expense. Given the already low-rate environment, 2010's reduction in interest expense of $1.36 billion is significant.

Region V continues to trail the nation in capitalization, but 2010's results indicate significant progress in this area. Net worth climbed $854 million in 2010. The net worth Ratio (as a percentage of average assets) climbed from 9.11 percent at the end of 2009 to 9.49 percent in 2010. Given the hits that equity has taken in the wake of NCUA stabilization assessments and heavy loan losses, the small gains being made to capital are a solid step in a positive direction.

Economic Commentary and Credit Union Concerns

It goes without saying that the last two years have been among the most challenging in the industry's history. Having weathered much of the storm, the national economy in general and the financial industry in particular is beset by two closely linked forces that impede both credit union growth and economic expansion: unemployment and consumer confidence.

The Western United States, and most particularly California and Nevada, continues to be plagued by high unemployment. Unemployment has essentially become a two-headed monster, eating away at credit union profitability.

First and most directly, as members become unable to pay their debts after a job loss, cash flows disappear as loans become delinquent and earning assets are lost as those loans are written down or off. As discussed earlier, write-offs, while slowing, are still at extremely high levels.

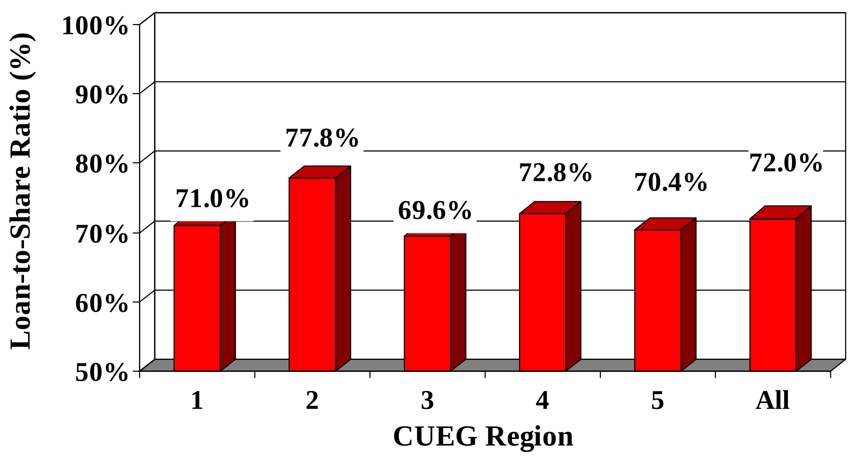
Second, high unemployment is perhaps the biggest factor influencing consumer confidence. Because so many consumers fear for their job security, consumers have developed a bunker mentality, saving as much as they can and eliminating extraneous expenses. According to the Bureau of Economic Analysis, from 2005 to 2008, personal savings (as a percent of disposable income) hovered around 2 percent. Since 2008, that rate has jumped to a level consistently over 5 percent, reaching a high of more than 7 percent in the second quarter of 2009. The immediate effect on credit unions has been significantly decreased demand for consumer loans. A quick look at the decline in total loan balances (down 6.6 percent in Region V) demonstrates how consumers have dramatically scaled back their spending.

This decrease in spending isn’t just a problem for financial institutions’ bottom lines. It has a snowball effect on the economy as a whole. High cash balances at financial institutions show that these funds are not being spent or invested, effectively removing those dollars from circulation in the economy. This slows GDP growth, which causes corporate belt-tightening and further loss of jobs, as the whole cycle starts over. In the end, it all comes back to employment. Once consumers feel more secure about their livelihoods, they will begin spending again. Until that time, Credit Union loan growth will likely remain challenged.

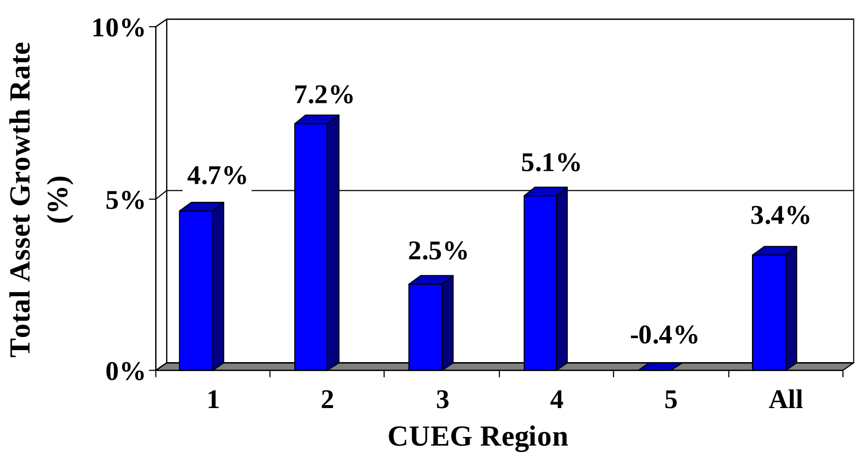
Despite the feeling that this economic downturn will persist indefinitely, there are many signs pointing to a real recovery. Job creation is gaining some momentum, and corporate profits have been very strong. As the nation breaks free from its economic malaise, the Credit Union Industry’s high cash levels have helped position it to quickly rebuild loan portfolios and capital levels as consumer demand returns. As Credit Unions are able to entice their membership back into the lending marketplace, they stand to gain a great deal in the coming months as they make the most of opportunities to build market share, grow membership, and add quality assets.

Appendix A:
CUEG Regional Financial Ratio Analysis

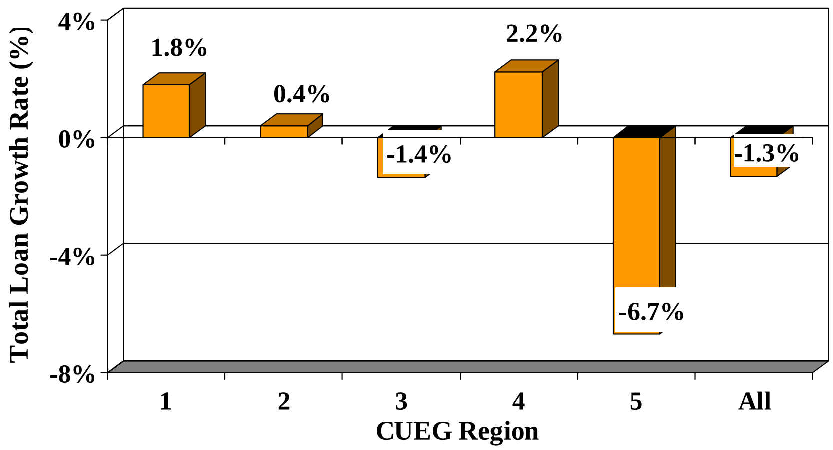
Loan-to-Share Ratio
Federally Insured Credit Unions by CUEG Region
December 2010



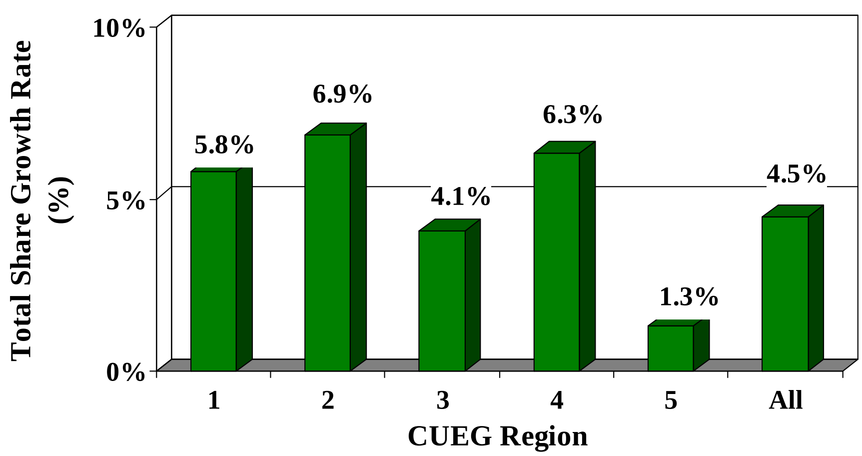
Total Asset Growth
Federally Insured Credit Unions by CUEG Region
December 2010



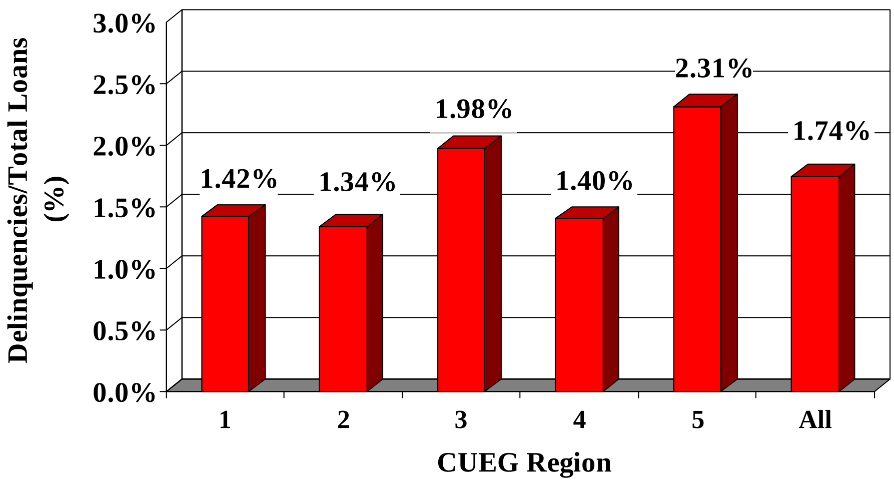
Total Loan Growth
Federally Insured Credit Unions by CUEG Region
December 2010



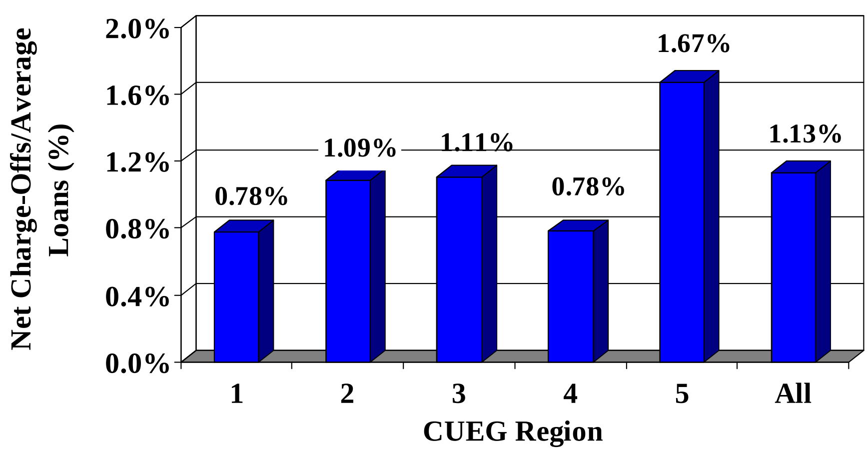
Total Share Growth
Federally Insured Credit Unions by CUEG Region
December 2010



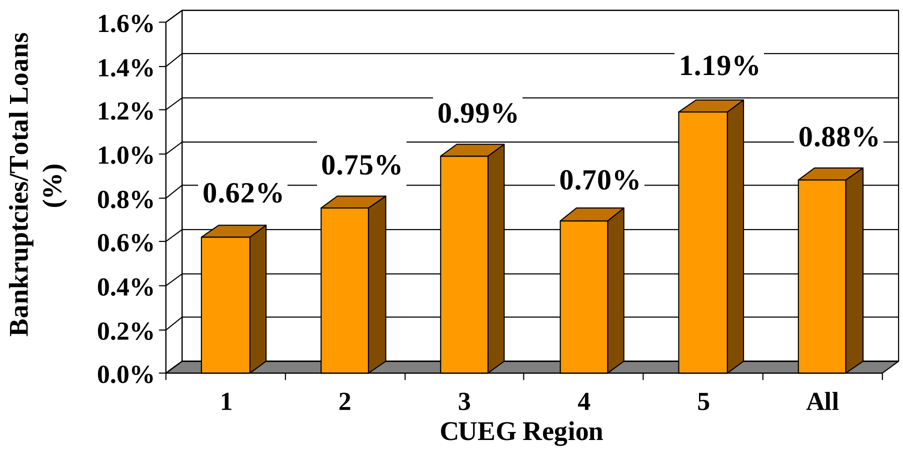
Delinquency Ratio
Federally Insured Credit Unions by CUEG Region
December 2010



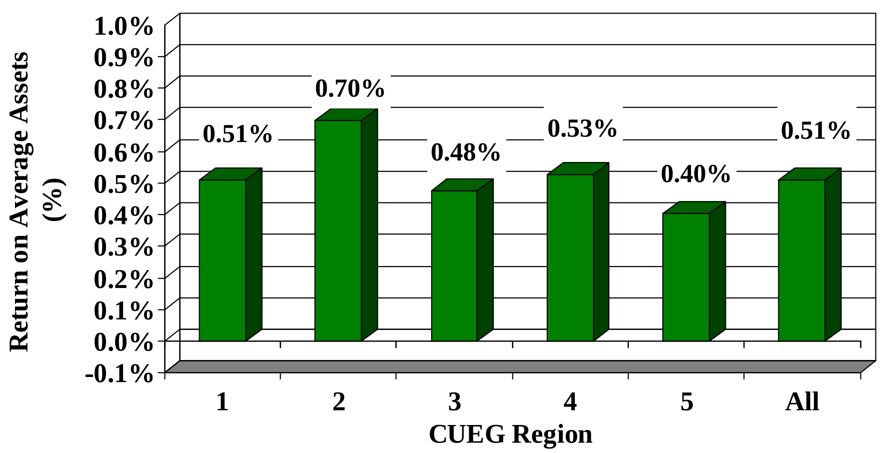
Net Charge-Offs/Average Loans
Federally Insured Credit Unions by CUEG Region
December 2010



Bankruptcies/Total Loans
Federally Insured Credit Unions by CUEG Region
December 2010



Return on Average Assets (ROA)
Federally Insured Credit Unions by CUEG Region
December 2010



Appendix B: CUEG Regions

CUEG REGIONAL BREAKDOWN