



## TRENDWATCH 3Q21



November 9, 2021

# Welcome!



When you join the event, you should automatically be connected to the audio broadcast with your computer. To listen by phone, please dial **+1 312 626 6799**, then input the webinar ID **868 2616 3961** followed by the passcode **424306**.

# Slide Link

Today's slides can be found online at:

<http://bit.ly/3Q-21>



Use the

## Questions Box

located on the bottom of your screen to type your comments or questions.



**Please take our post-event survey. We value your feedback!**



# Ready for 2022?

Expand Your Investment Options Now

Learn more about the TCU Portfolios and discuss implementing policy updates for 2022.

Contact us at [TCUGroup@callahan.com](mailto:TCUGroup@callahan.com) or visit [trustcu.com](http://trustcu.com).

[www.trustcu.com](http://www.trustcu.com)





# Join The Impact Network

Callahan is building a network of leading credit unions that will help us define impact metrics, share perspectives and practices, and work to evolve the credit union story.

**CALLAHAN**  
ASSOCIATES  
*the credit union company*

**CALLAHAN**  
**ACADEMY**

# Leverage Purpose For Greater Impact

*Sustainable Business Strategy  
with Rebecca Henderson*

in collaboration with Harvard Business School Online

---

**Callahan.com/Purpose**





# Callahan's Classic Software, Reimagined.

Coming Early 2022





# Today's Lineup

## Market Update

*Jason Haley, Chief Investment Officer, Investment Management Group, ALM First*

## 3Q 2021 Credit Union Results

*Alix Patterson, Chief Experience Officer, Callahan & Associates*  
*William Hunt, Industry Analyst, Callahan & Associates*

## Measure Your Mission: Quantifying Credit Union Impact

*Jennifer Davis, VP, Information Services and Technology, Callahan & Associates*





# ALM FIRST

for a partnership built on trust.

**TRUST**  
MUTUAL FUNDS  
FOR CREDIT UNIONS BY CREDIT UNIONS

Callahan Quarterly Trendwatch | November 9, 2021

## ALM FIRST MARKET UPDATE

**Speaker**



**Jason Haley**  
Chief Investment Officer

- **Inflation, inflation, inflation**

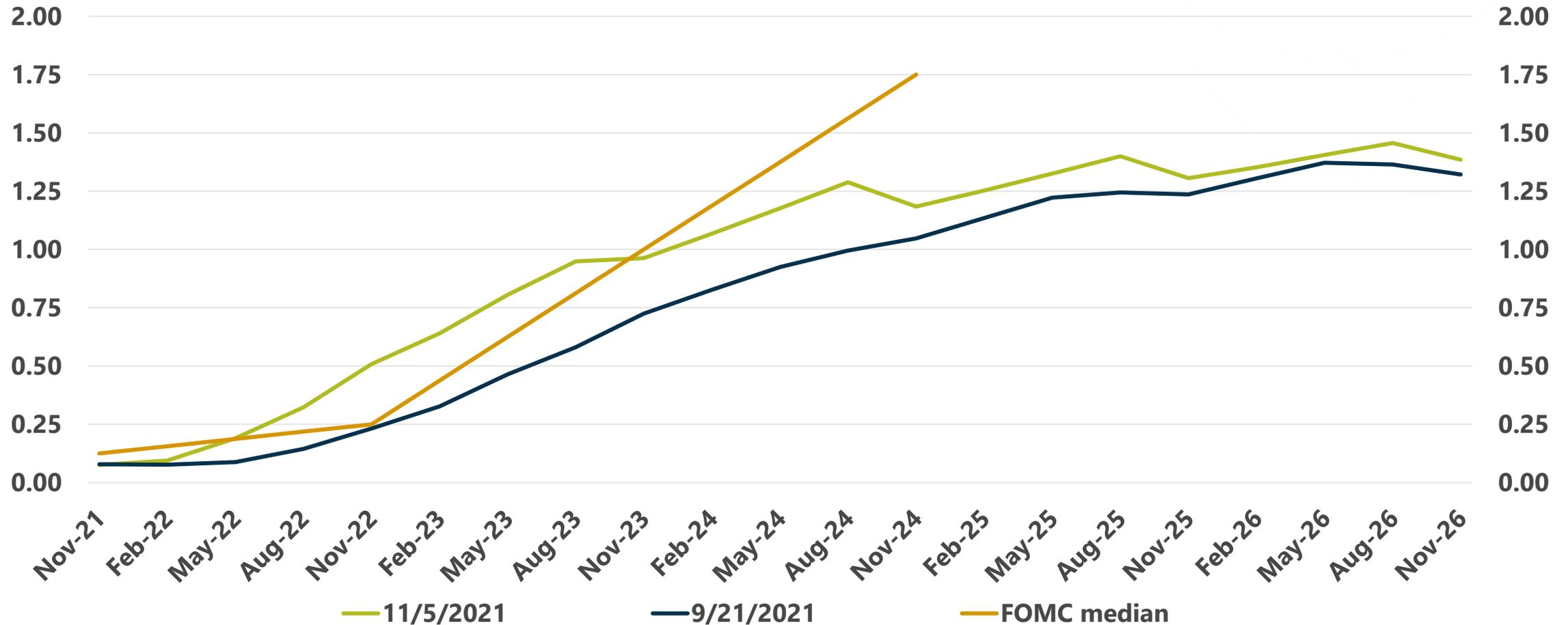
- With COVID-19 trends markedly improved, the predominant economic theme in financial markets over the last two months has been inflation
  - Supply chain have persisted longer than many expected, and tight labor markets are fueling wage inflation
  - More hawkish rhetoric from global central bank leaders starting in September related to inflation concerns
- Market inflation expectations have surged to fresh YTD highs
  - 10yr Treasury Inflation Protected Securities (TIPS) breakeven yields rose to new 16-year high in October
- Market pricing for Fed rate hikes remains aggressive relative to Fed guidance
  - Two 25 bps rate hikes priced in for 2022 and four hikes priced by Q3 2023

- **U.S. & European central banks push back on market pricing for rate hikes**

- FOMC announced initiation of tapering plan at November 3 meeting (as expected), the official statement's description of "transitory" inflation pressures was expanded
  - Powell said there is still progress to be made on unemployment and reiterated official view that current price pressures are related to supply disruptions, not tight labor markets (wages)
- Bank of England (BoE) surprised markets last week by keeping its policy rate unchanged
- European Central Bank (ECB) President Lagarde pushed back on market expectations, saying the ECB was unlikely to raise rates in 2022

# Fixed Income Market Already Priced For Earlier Fed Rate Hikes...

## 1-Month Overnight Index Swap (OIS) Implied Forward Curve (%)



Source: NY Fed, Bloomberg, ALM First

# ...And the Consequential Impact on the Economy

## 2yr/10yr Treasury Spread 2yrs Forward



Source: Bloomberg

# Market Themes

- **Belly of the Treasury curve reprices for Fed hikes**
  - 3-5yr yields up 37-42 bps since the end of July
  - 2yr/5yr spread 43 basis points steeper in 2021(2yr/10yr spread +25 bps YTD)
  - Curve slope volatility at an 11-month high in October on several twists throughout the month
- **Fixed income has struggled in 2021 amid higher rates**
  - YTD total returns negative for broad investment grade bond indices
    - Bloomberg US Aggregate Index -1.75% through October
  - Short duration credit (MBS and corporate debt) has performed well over the last 12 months
  - Even with tapering looming, the Fed’s presence in fixed income markets remains significant
    - Fed balance sheet will continue to expand, and as a result, fixed income spreads should remain at/near historically tight levels heading into 2022

Treasury Curve			
Tenor	11/8/2021 (%)	7/31/2021 (%)	Change (bps)
1-Month	0.04	0.03	0.00
3-Month	0.04	0.04	-0.01
6-Month	0.06	0.05	0.01
1-Year	0.14	0.06	0.08
2-Year	0.44	0.18	0.26
3-Year	0.71	0.34	0.37
5-Year	1.11	0.69	0.42
10-Year	1.49	1.22	0.26
20-Year	1.90	1.80	0.10
30-Year	1.88	1.89	-0.01
Curves			
3mo-10yr	1.45	1.18	0.27
2yr-5yr	0.67	0.51	0.16
2yr-10yr	1.05	1.04	0.01
2yr-30yr	1.45	1.71	-0.26
5yr-10yr	0.38	0.53	-0.15

Source: Bloomberg

# Looking Ahead

- **Near-term economic fundamentals remain strong**
  - Significant growth in household liquid assets over the last 18 months remains a tailwind for consumer spending
  - Corporate balance sheet health has generally improved as well
  - Near-term risks:
    - COVID breakout, Congressional budget negotiations (including debt ceiling), inflation data
- **Depository institutions remain flush with liquidity**
  - Loan activity picking up in recent quarters, but still below pre-COVID levels for the industry
  - Excess reserves in banking system could remain elevated until the Fed begins to normalize its balance sheet
  - Amid ongoing interest margin compression (and volatile markets), profitable risk management as critical as ever
    - Disciplined asset pricing, capital utilization, etc.

3800 Maple Avenue Suite 600  
Dallas, TX 75219  
Phone: 800.752.4628  
Fax: 214.987.1052

[www.almfirst.com](http://www.almfirst.com)



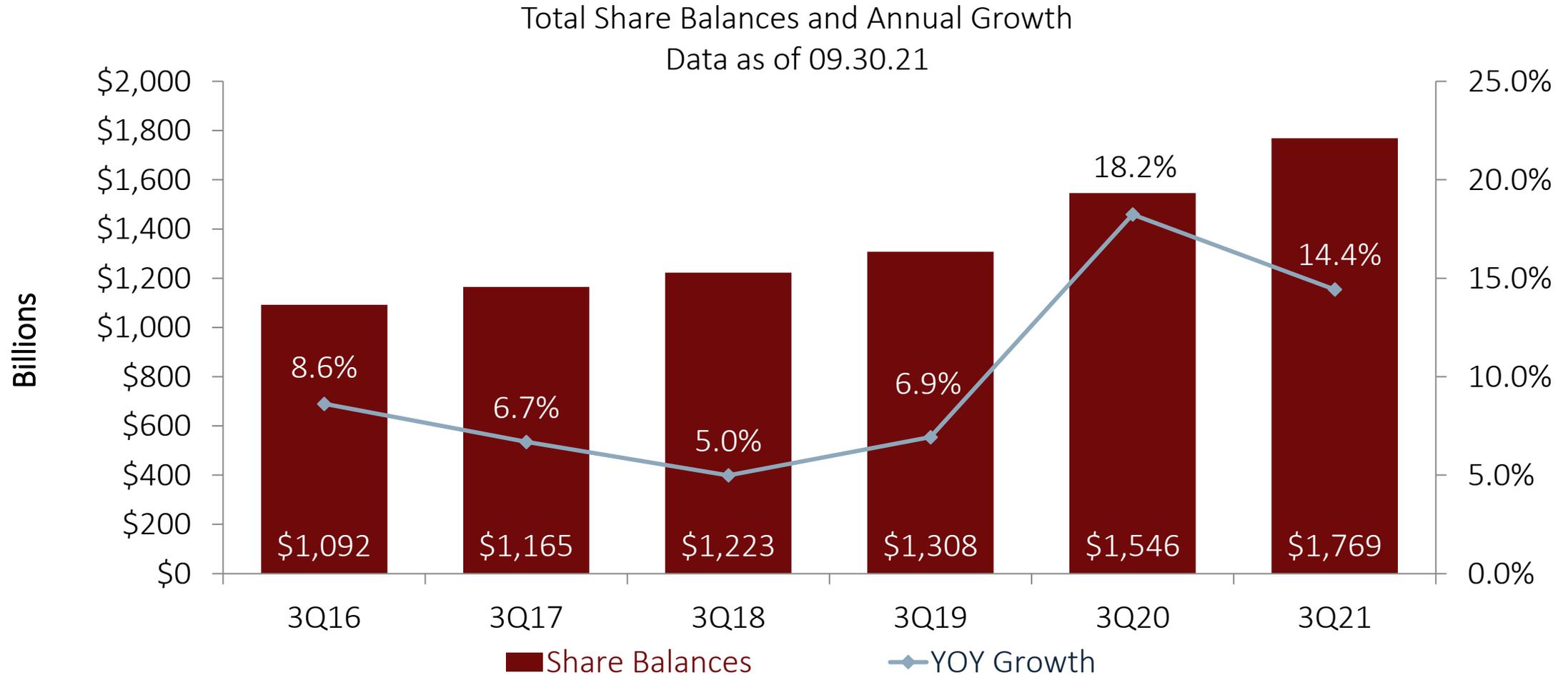
## Industry assets officially surpassed \$2 trillion

	09/30/2021	12-Mo. Growth	09/30/2020	12-Mo. Growth
Assets	\$2,041.7B	12.9%	\$1,807.2B	16.1%
Loans	\$1,236.0B	5.8%	\$1,168.0B	6.3%
Shares	\$1,769.4B	14.4%	\$1,546.3B	18.2%
Investments	\$710.6B	28.6%	\$552.6B	44.8%
Capital	\$217.8B	7.4%	\$202.7B	9.4%
Members	130.2M	4.1%	125.0M	3.4%

# Credit unions add 5.2 million new members over the past year

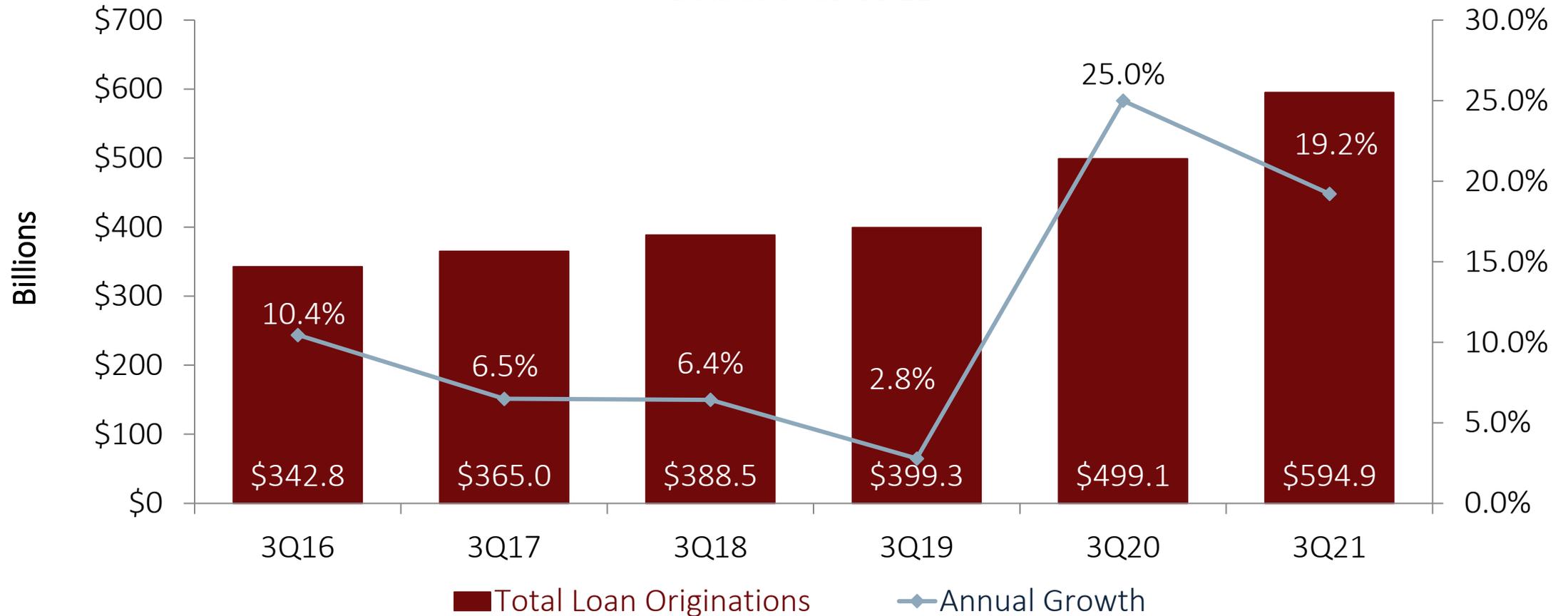


# While share balance growth slows, members continue to save at record pace

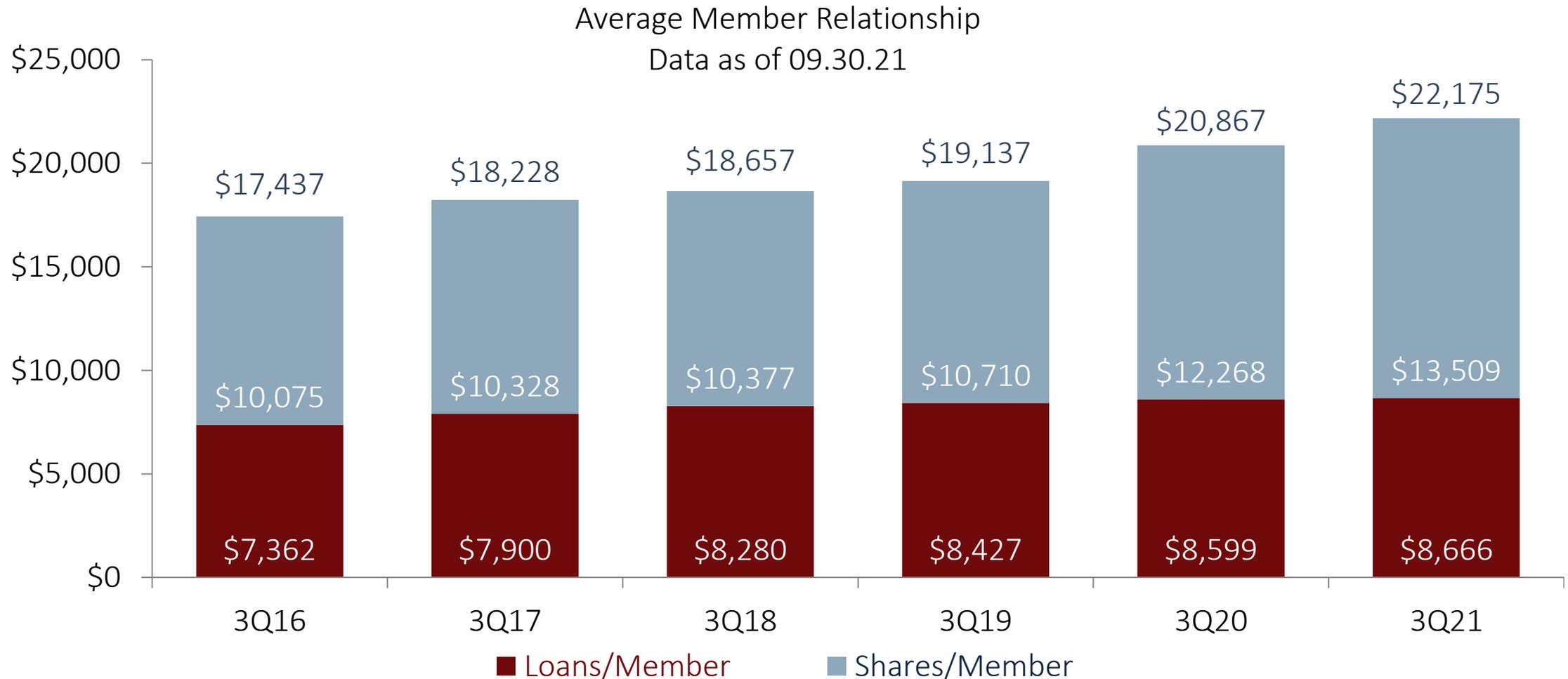


# Loan demand continues its record-breaking pace

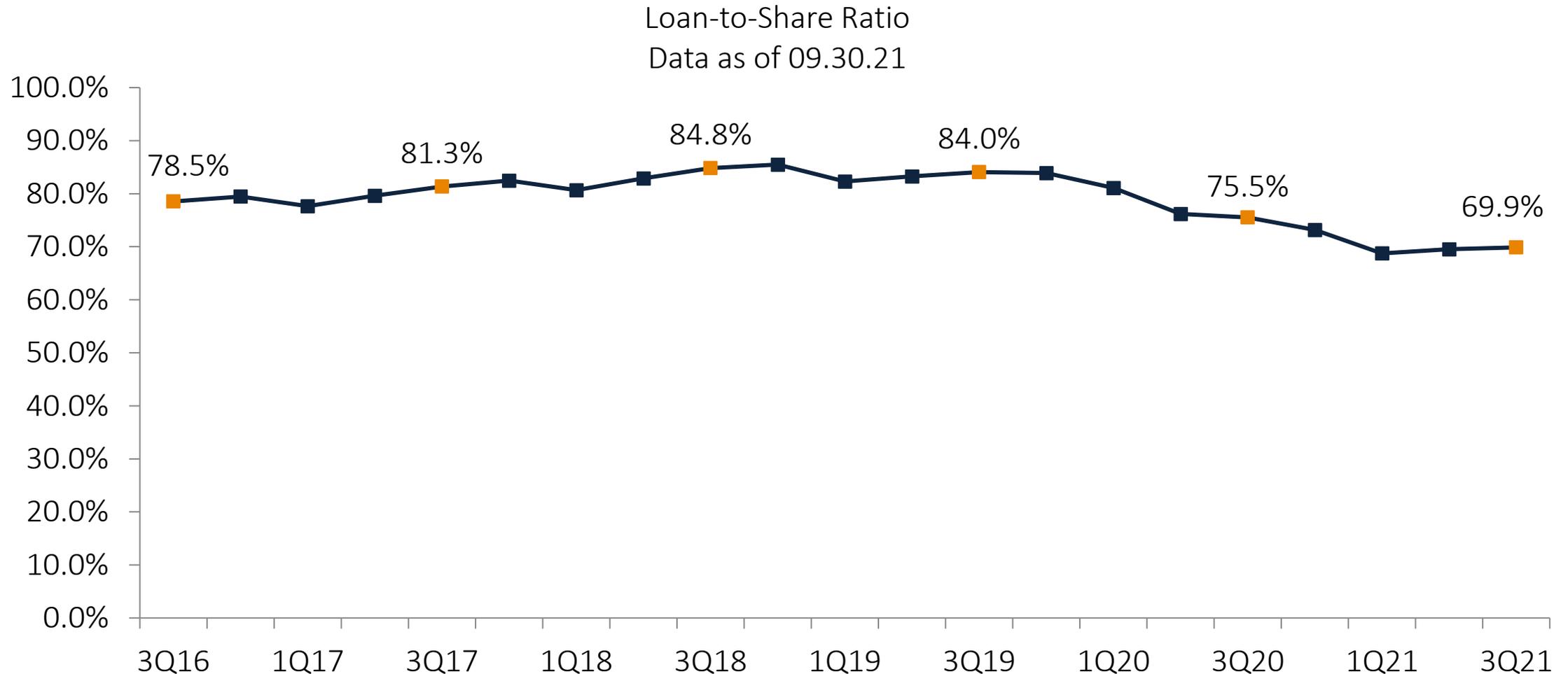
YTD Loan Originations and Annual Growth  
Data as of 09.30.21



# The average member relationship grew \$1,308 year-over-year driven deposit-driven relationships



# The loan-to-share ratio inches up for the second straight quarter as record originations start to stick on balance sheets



# Deposits

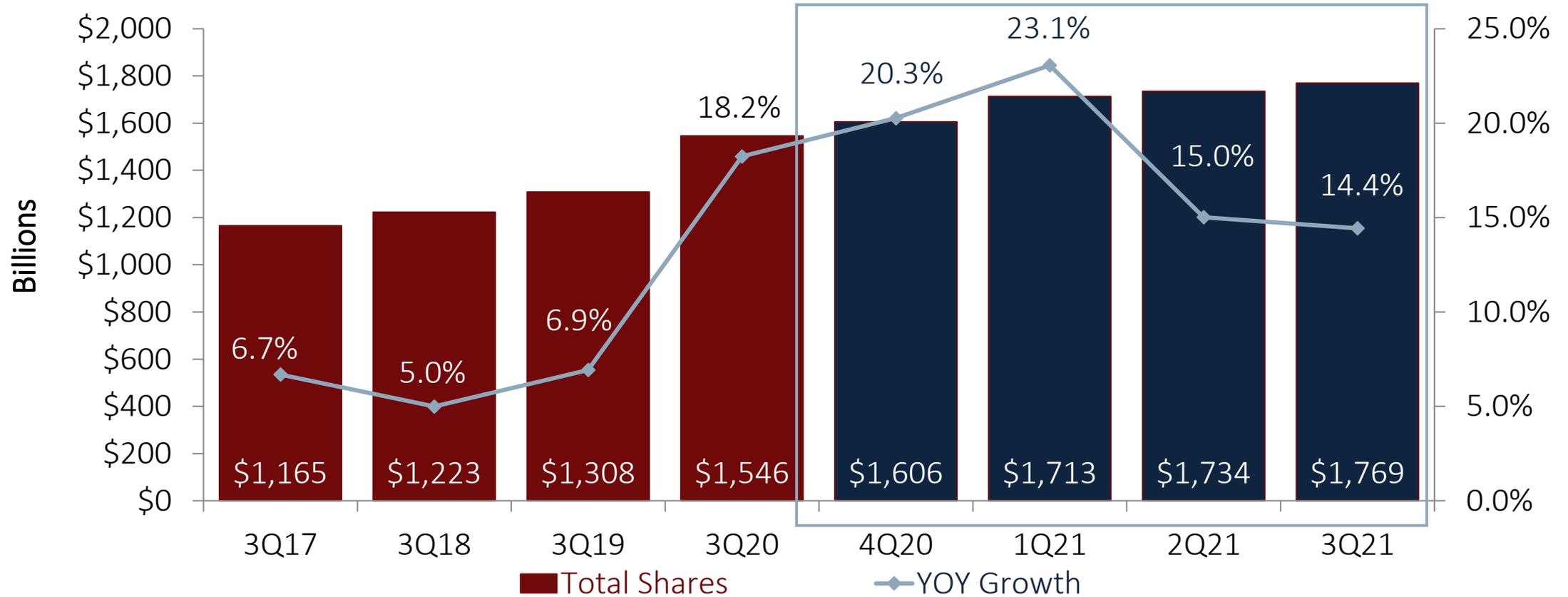
Americans elected to save nearly 40% of cumulative federal relief income

<b>How Households Use Their Stimulus Checks</b>			
Stimulus Round	1	2	3
Reporting Month	June 2020	January 2021	March 2021
Avg % Spent	29.2	25.5	24.7
Avg % Saved	36.4	37.1	41.6
Avg % Toward Debt	34.5	37.4	33.7

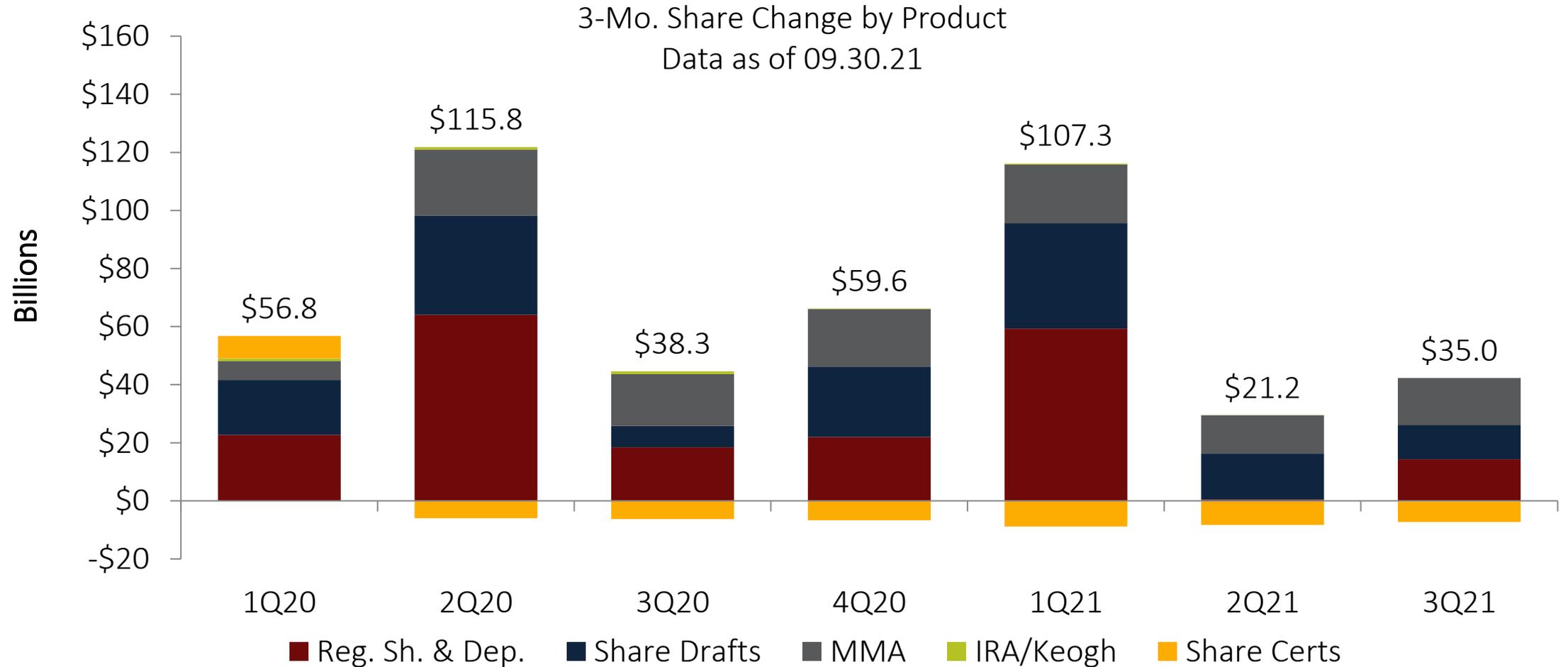
Source: New York Fed Survey of Consumer Expectations (SCE)

# Share growth slows a year removed from the CARES Act

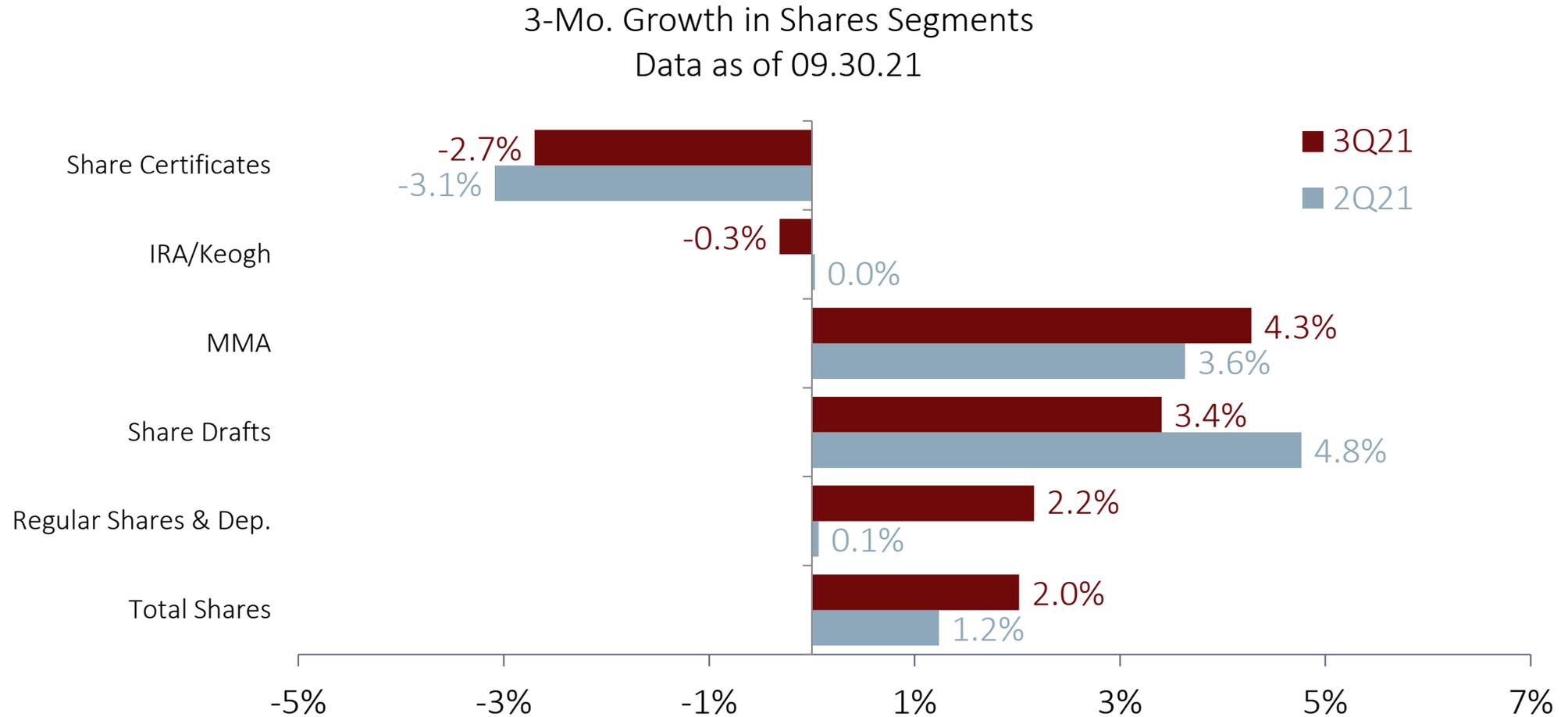
Total Shares and Annual Growth  
Data as of 09.30.21



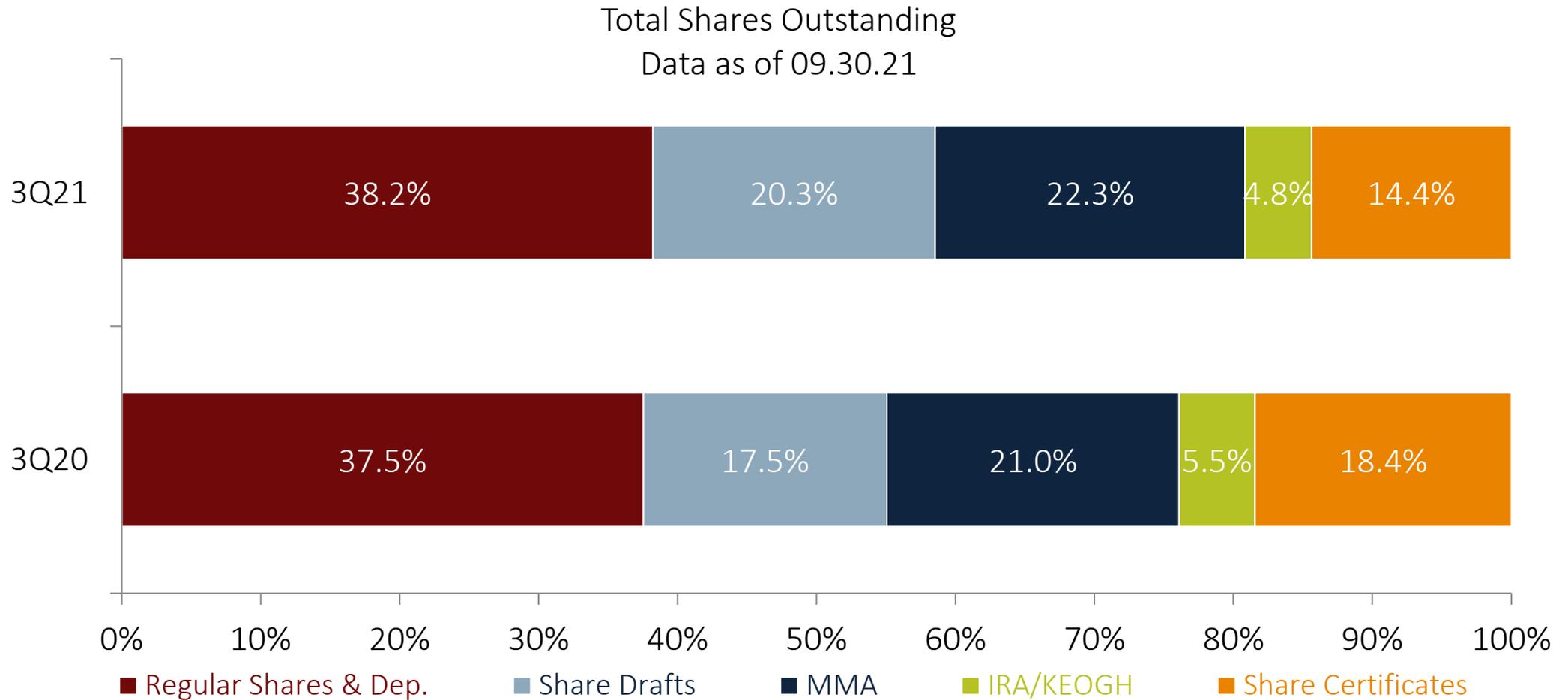
# On a quarterly basis, the impact of federal relief is clear



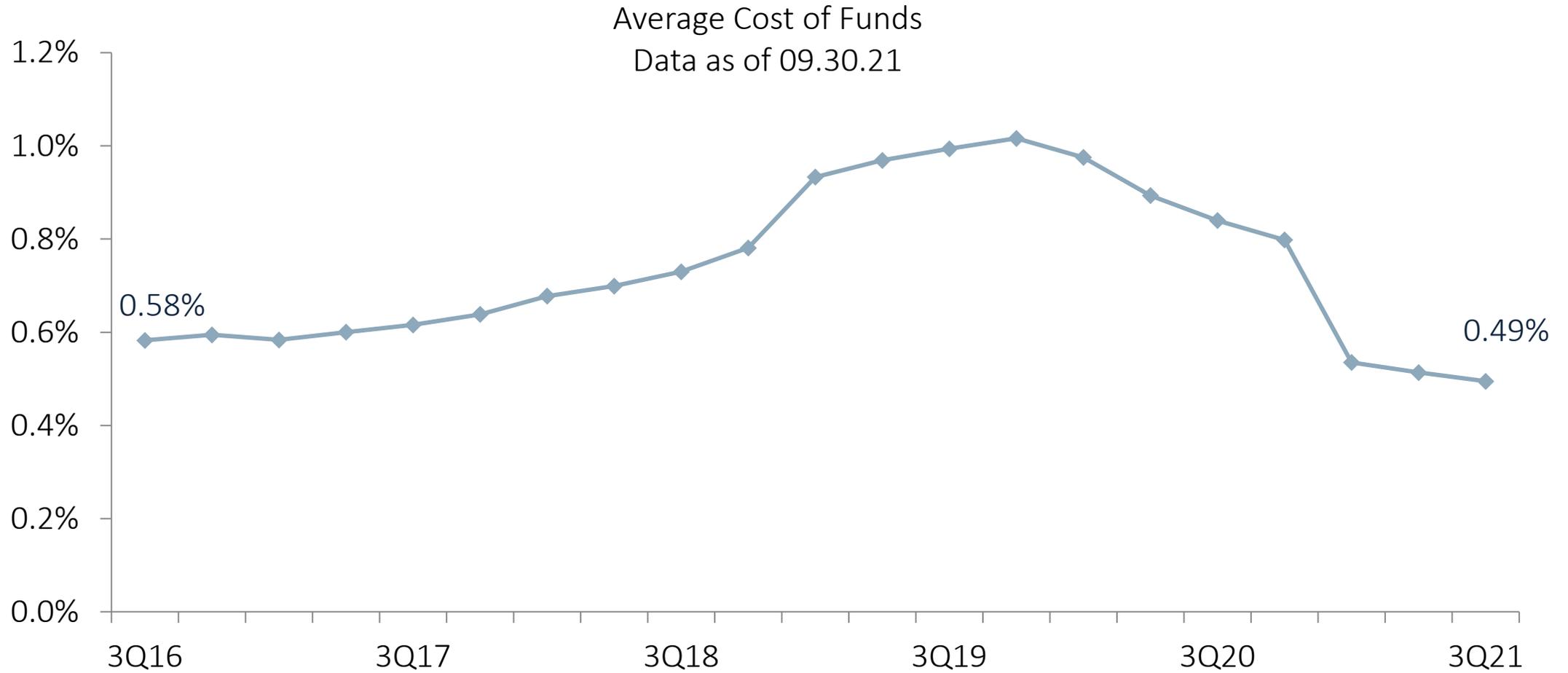
# Liquid core deposits remain the share products of choice for members



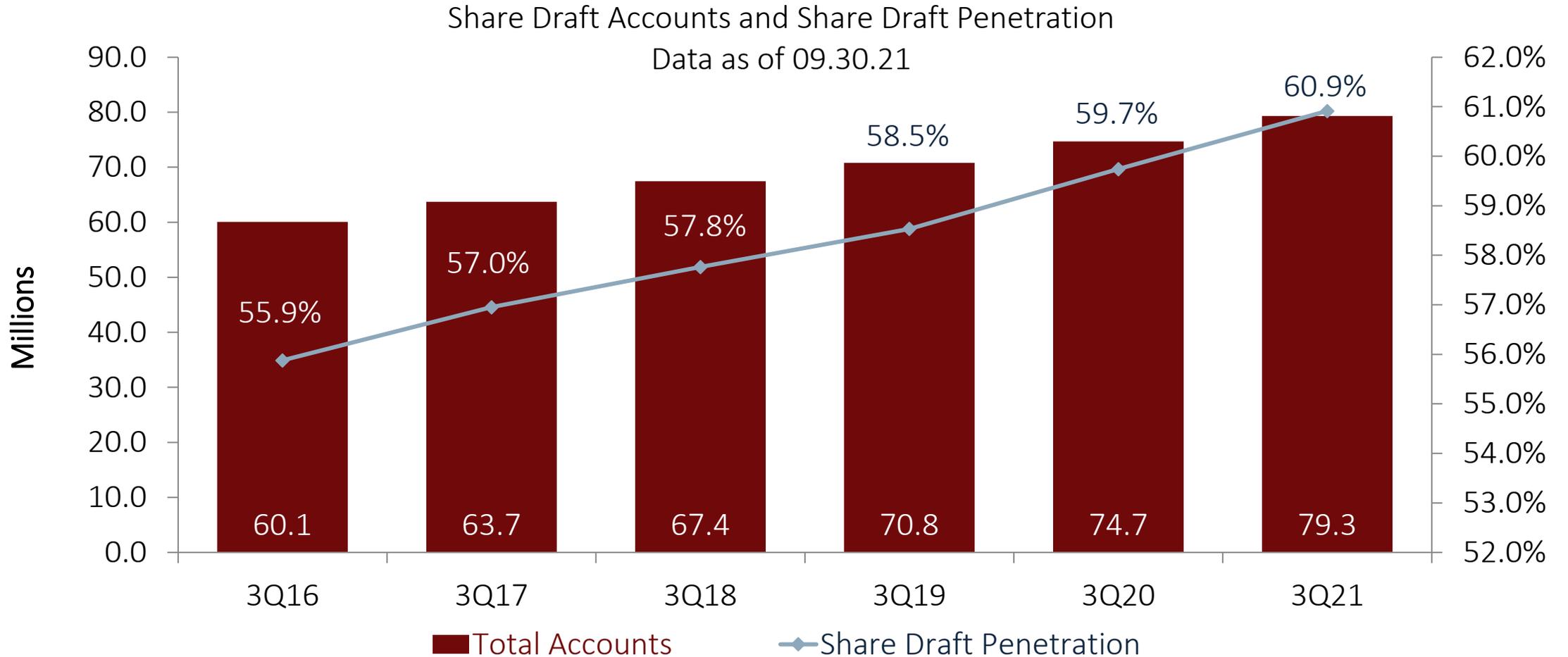
# Core deposits increase portfolio share



# Cost of funds drops then stabilizes



# Total share draft accounts and penetration both hit record highs



# Lending

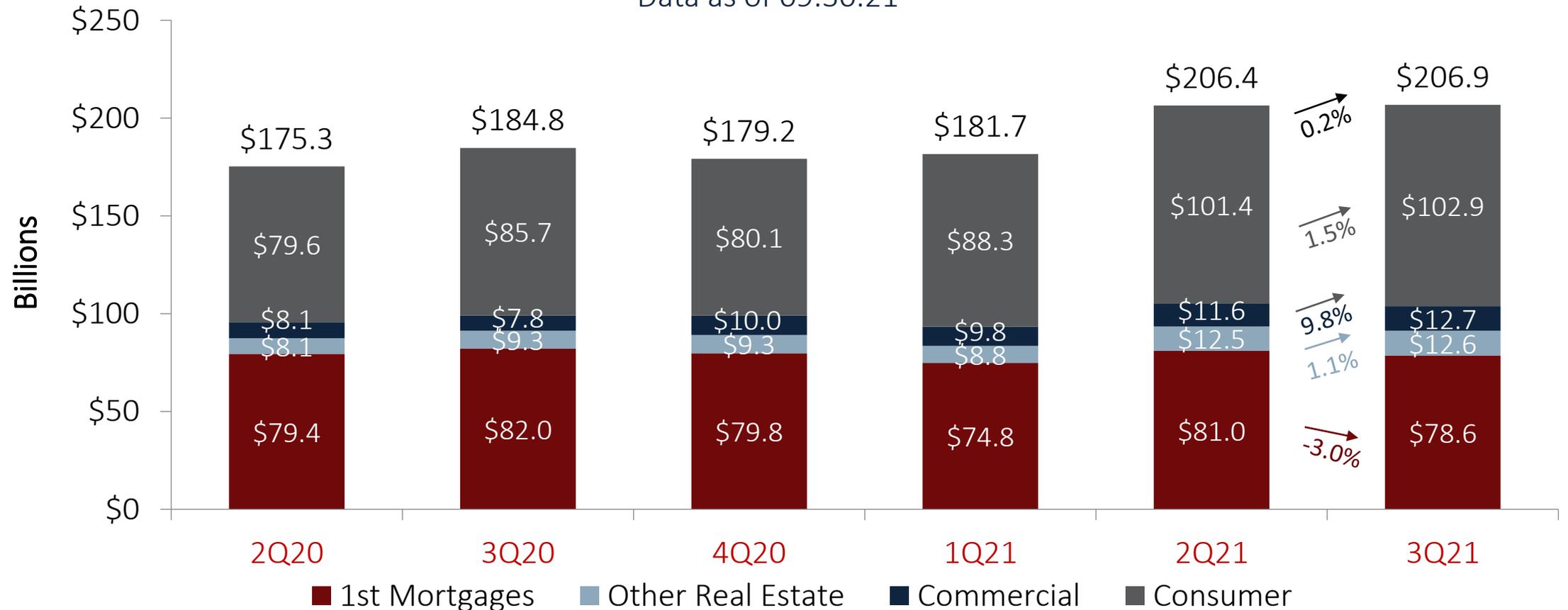
Americans put over 1/3 of stimulus checks towards paying down debt

<b>How Households Use Their Stimulus Checks</b>			
Stimulus Round	1	2	3
Reporting Month	June 2020	January 2021	March 2021
Avg % Spent	29.2	25.5	24.7
Avg % Saved	36.4	37.1	41.6
Avg % Toward Debt	34.5	37.4	33.7

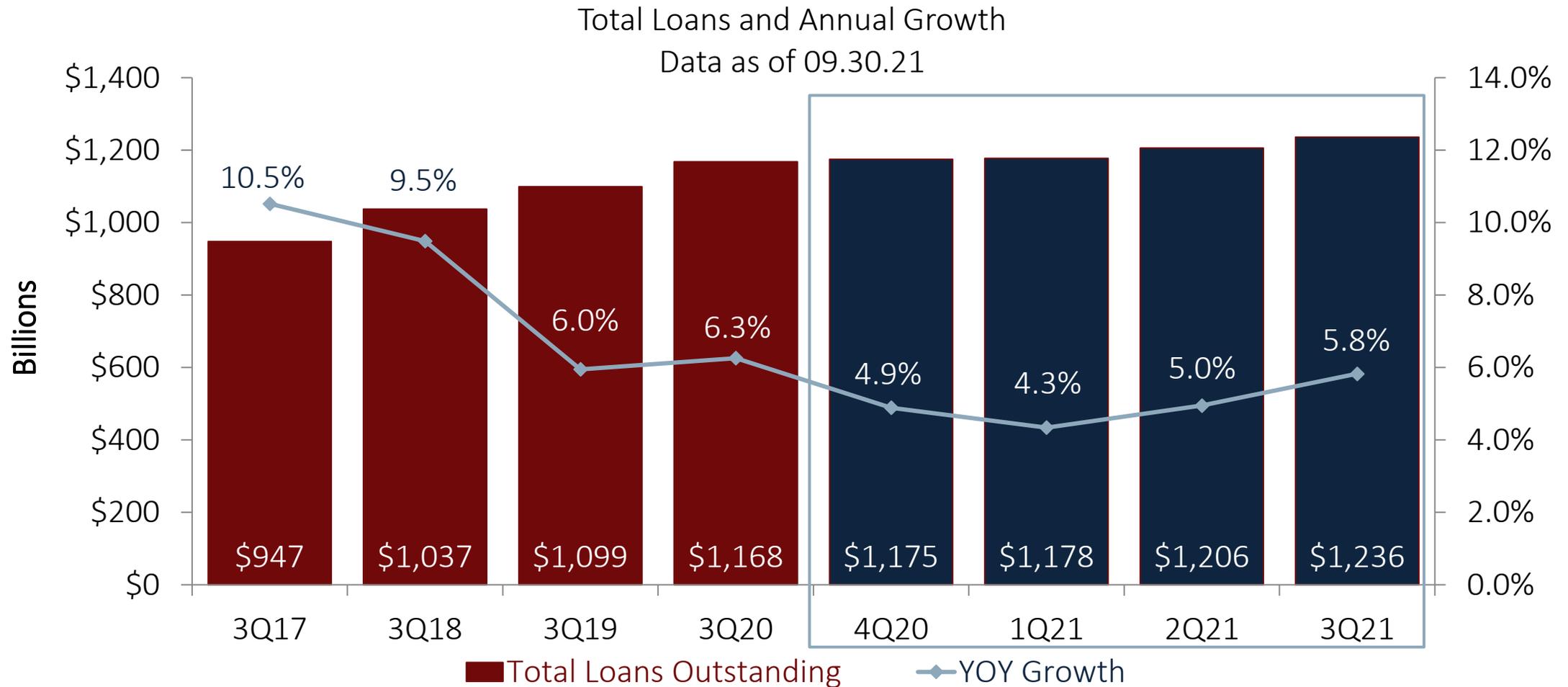
Source: New York Fed Survey of Consumer Expectations (SCE)

# Consumer lending remains healthy, although first mortgages slow a bit

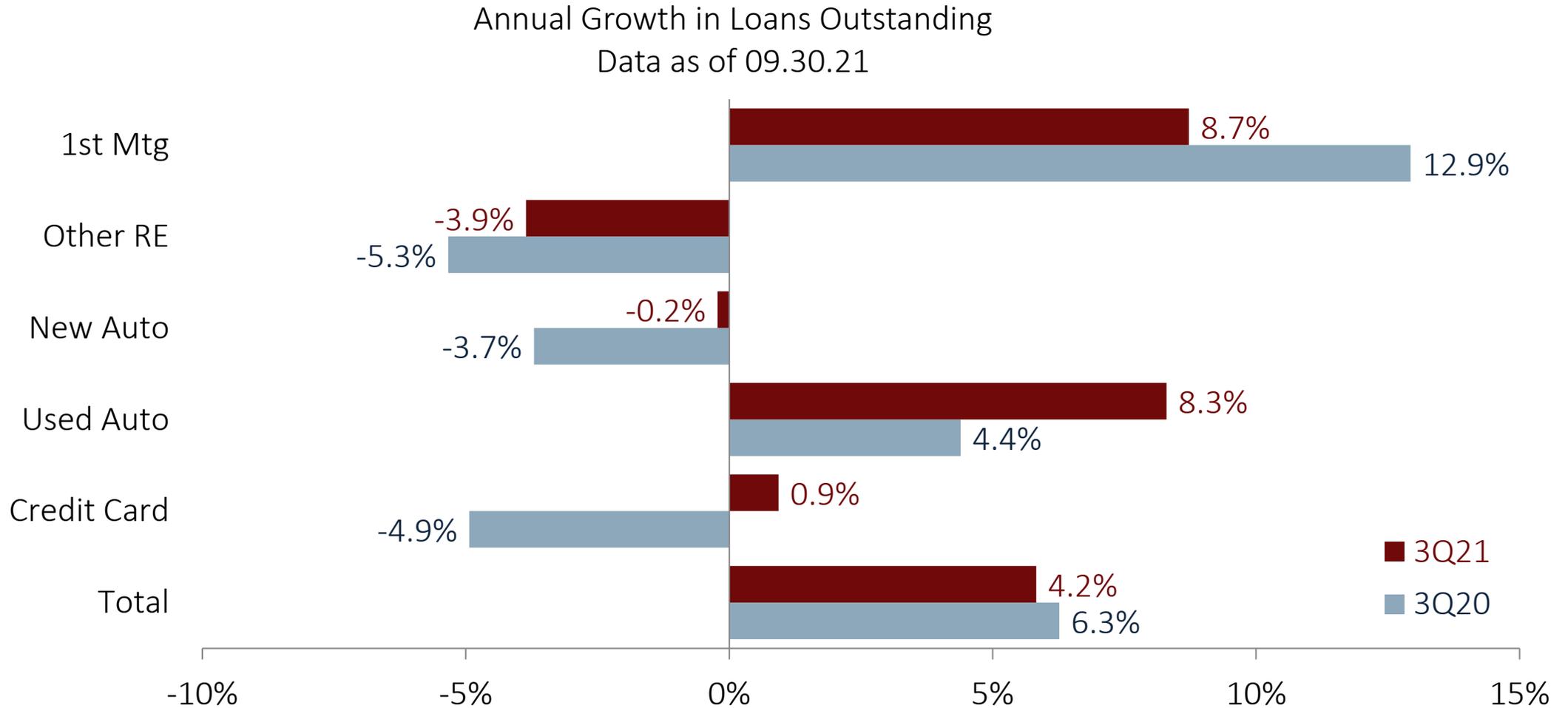
Quarterly Loan Originations Booked  
Data as of 09.30.21



# But record originations aren't translating to record balance sheet growth

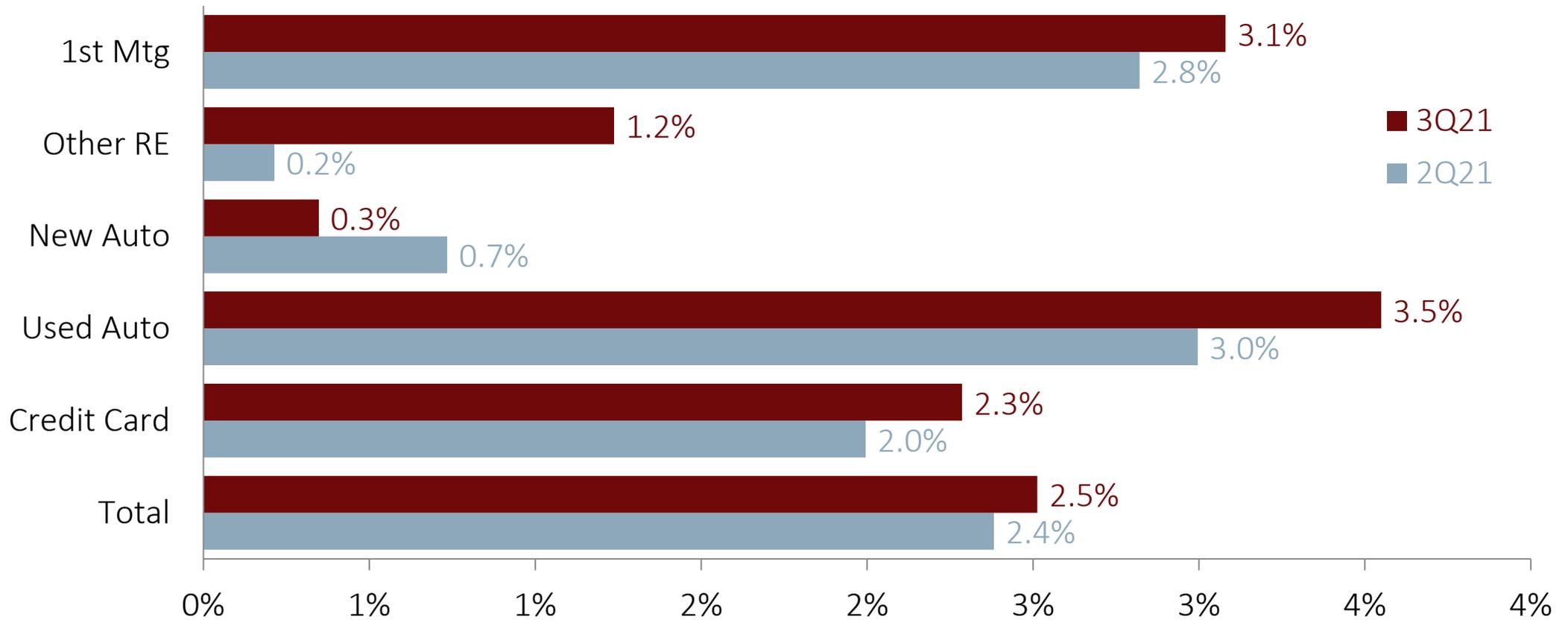


# Annual first mortgage growth decelerated after a record year

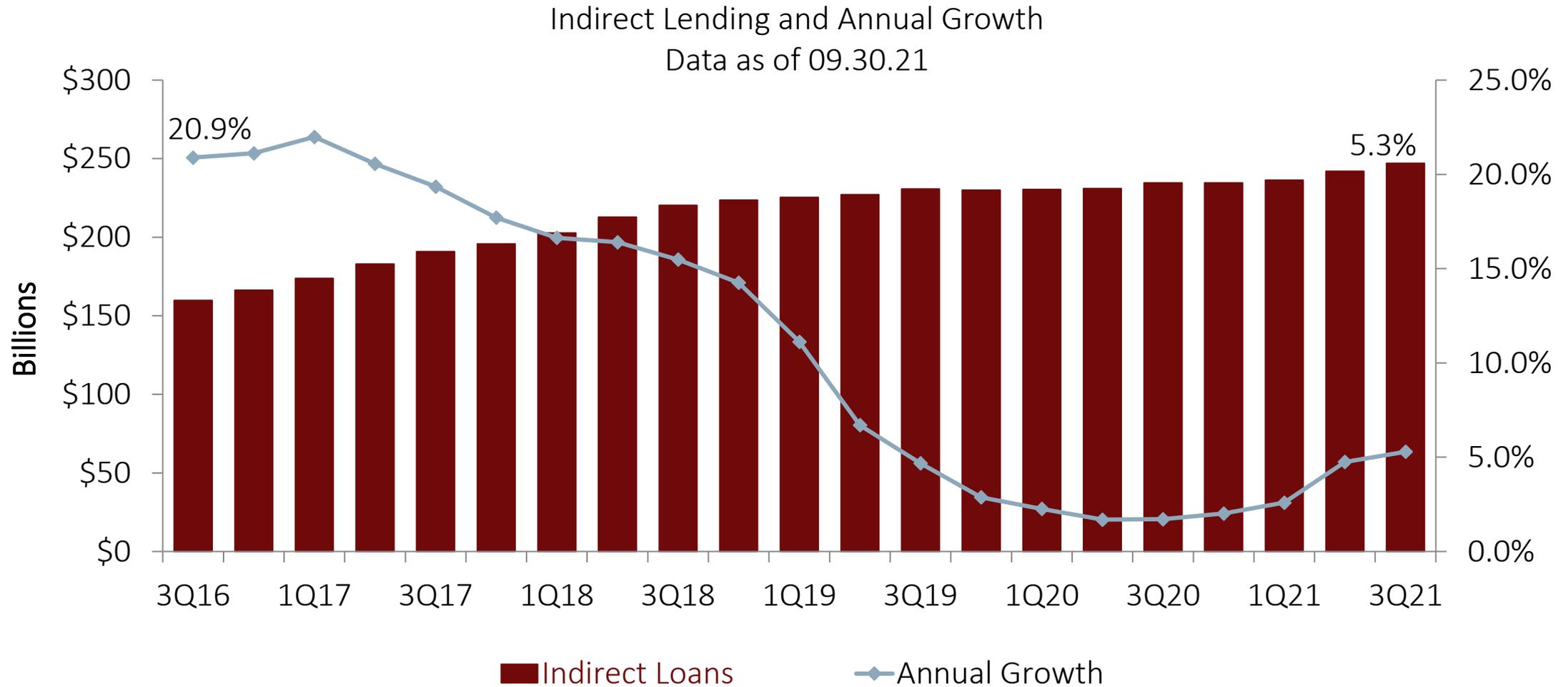


# But balances expanded across all major loan products between the June and September

Quarterly Growth in Loans Outstanding  
Data as of 09.30.21



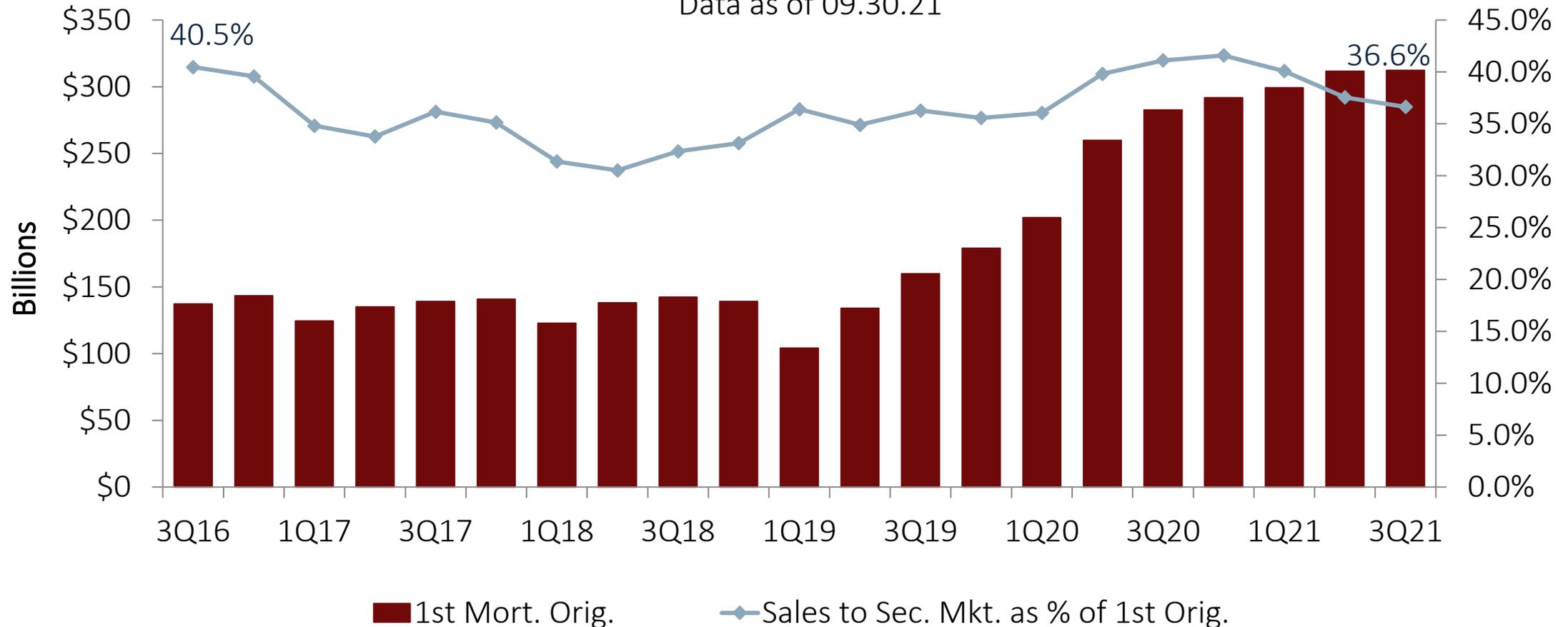
# There is a rebound in indirect programs to generate loan growth



# Secondary market mortgage sales slow as credit unions focus on managing the balance sheet

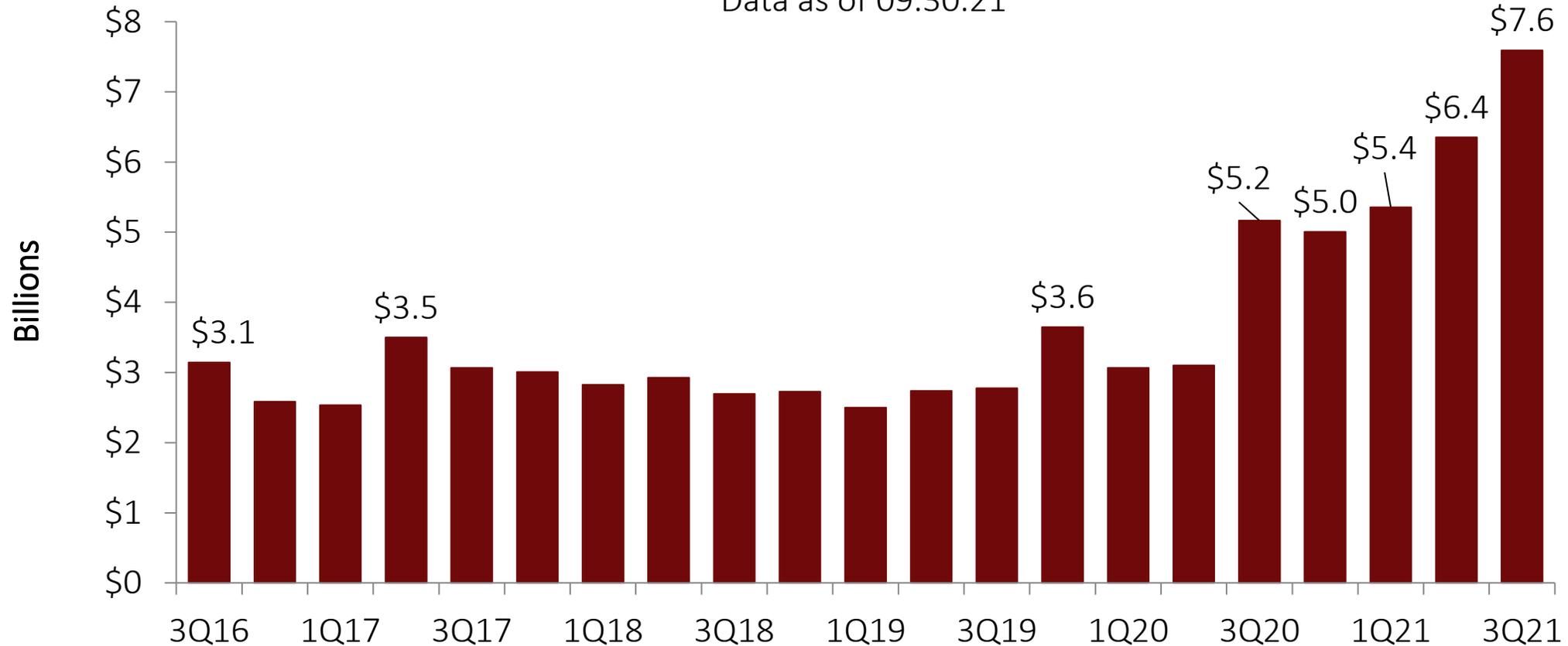
Annualized 1<sup>st</sup> Mortgage Originations & Secondary Market Sales as % of 1<sup>st</sup> Orig.

Data as of 09.30.21

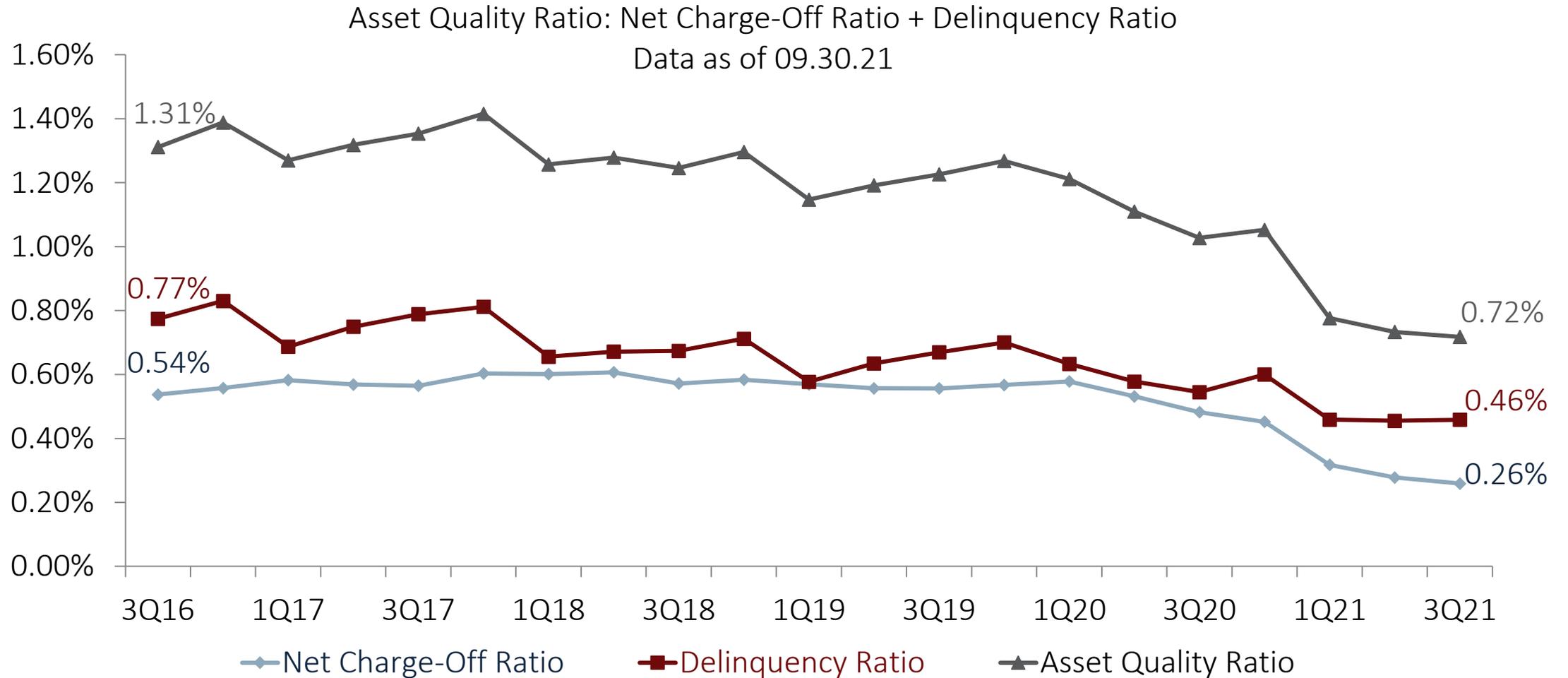


# Credit unions have also turned to secondary market participations to help manage balance sheets

Participations Purchased by Quarter  
Data as of 09.30.21



# The asset quality ratio improves, reaching a historic low



# YOY Delinquency improved across all major loan products

Annual Change in Delinquency  
Data as of 09.30.21



Total  
0.46%  
↓ 0.08%



1<sup>st</sup> Mortgage  
0.41%  
↓ 0.09%



Auto  
0.35%  
↓ 0.09%



Other RE  
0.53%  
↓ 0.06%



Indirect  
0.38%  
↓ 0.09%



Credit Card  
0.85%  
↓ 0.02%

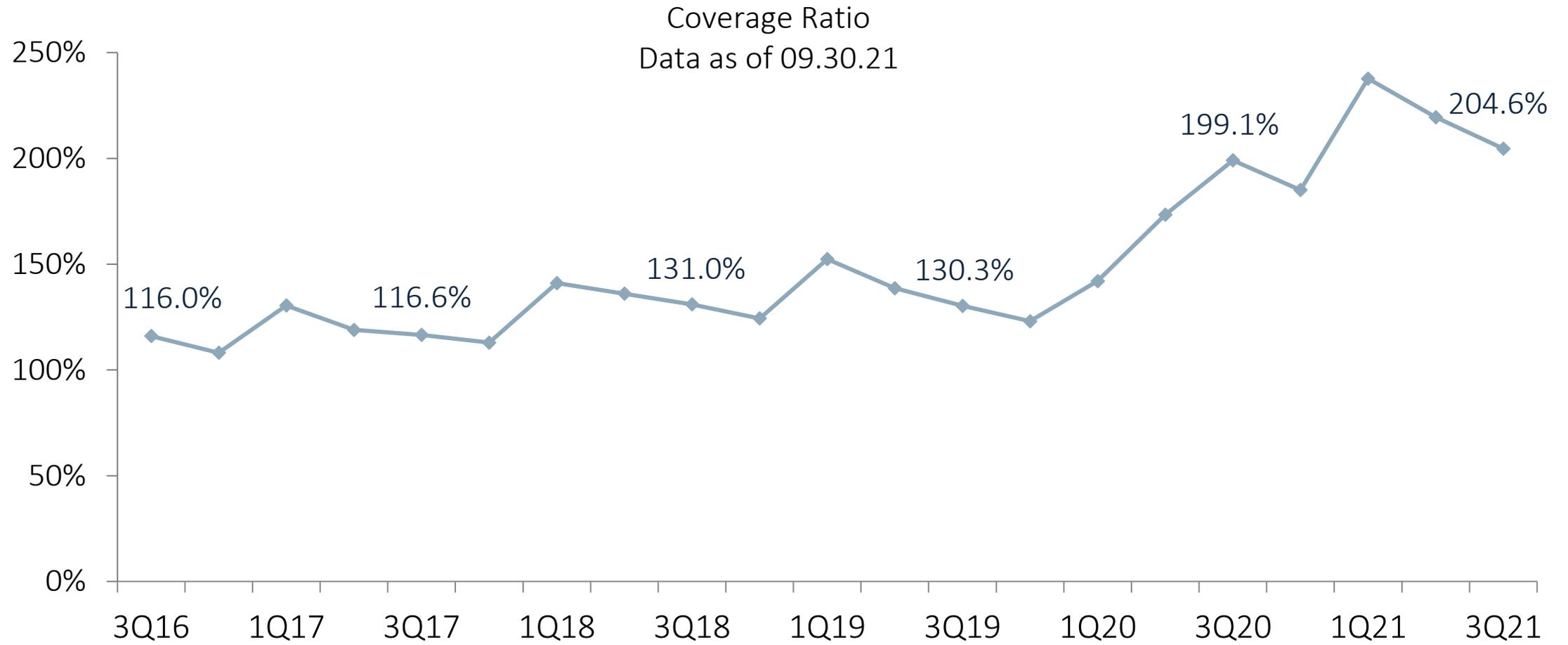


Member Commercial  
0.48%  
↓ 0.20%

# Given asset quality, credit unions are pulling back on their PLL



# Although coverage ratio still almost double the historical average

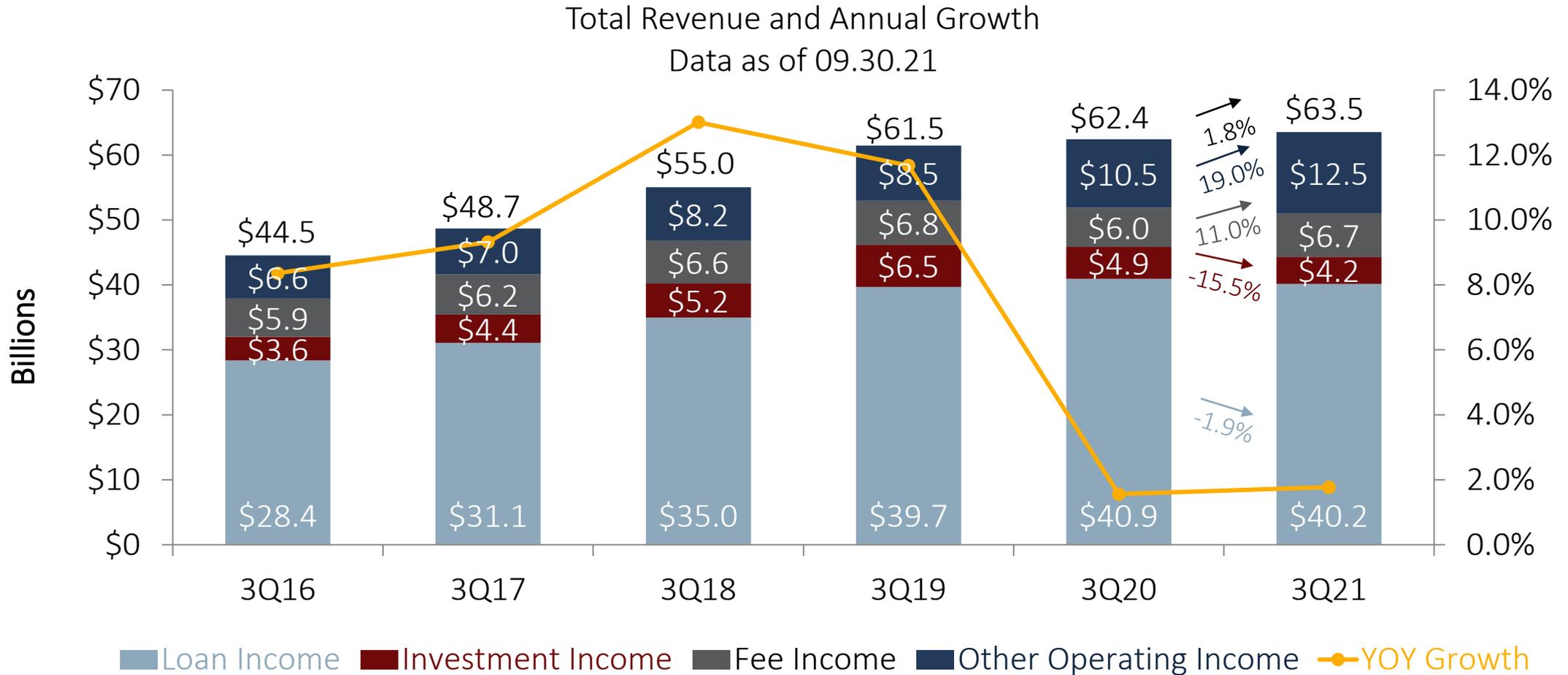




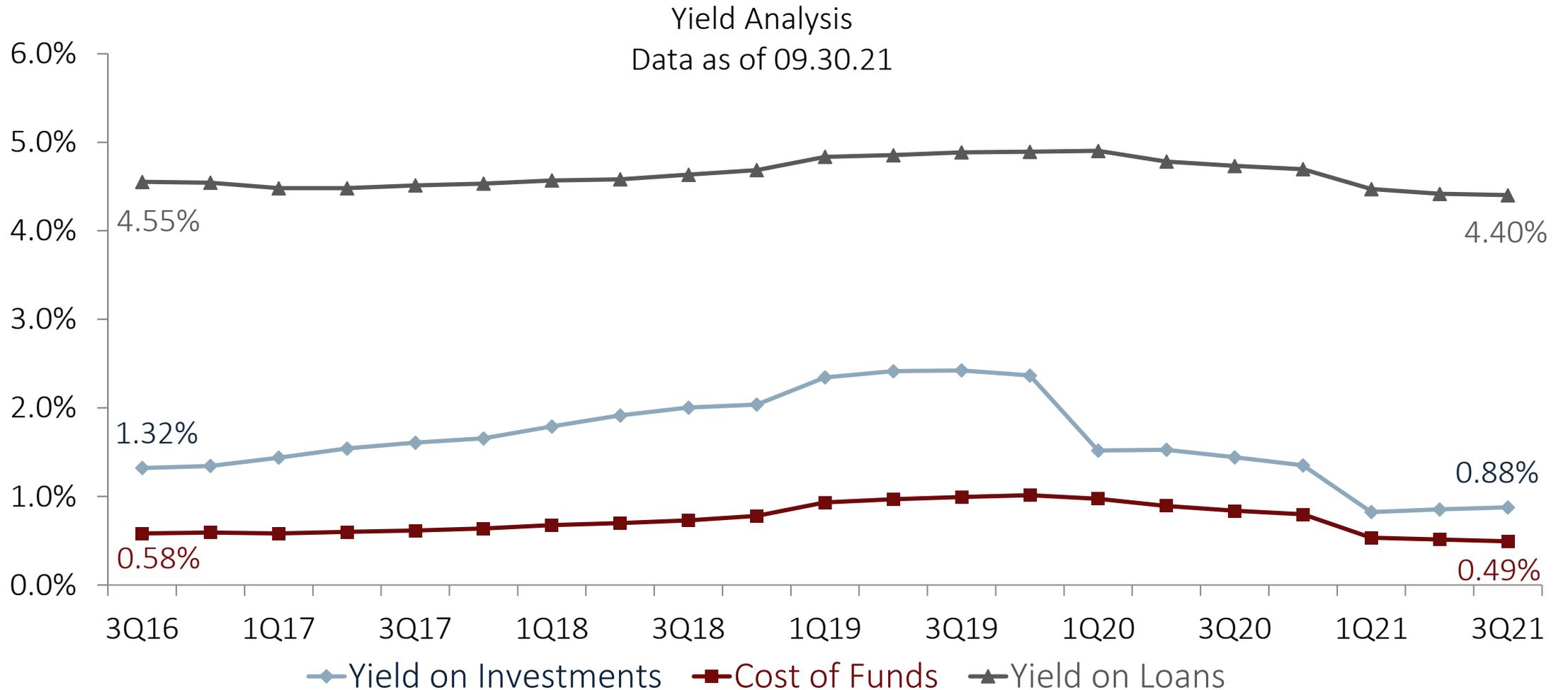
# Earnings & Capital



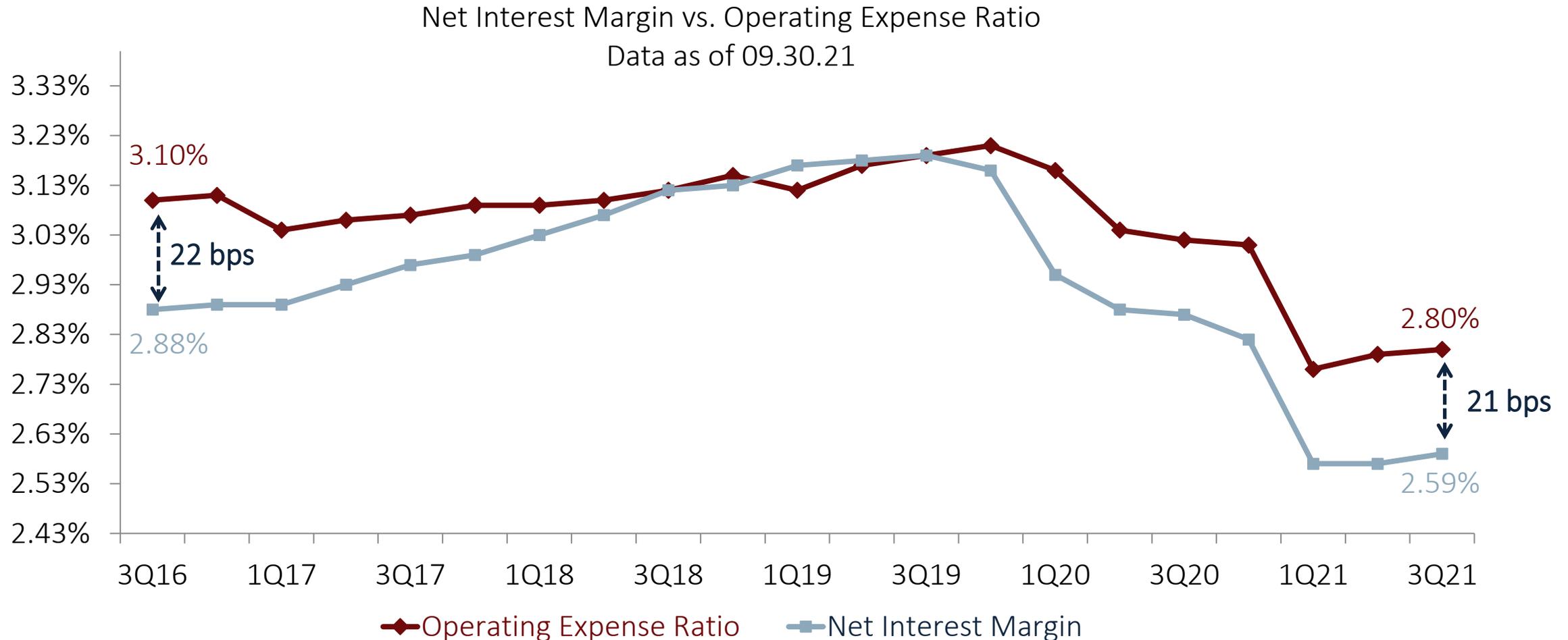
# Top-line earnings up, propped by non-interest income



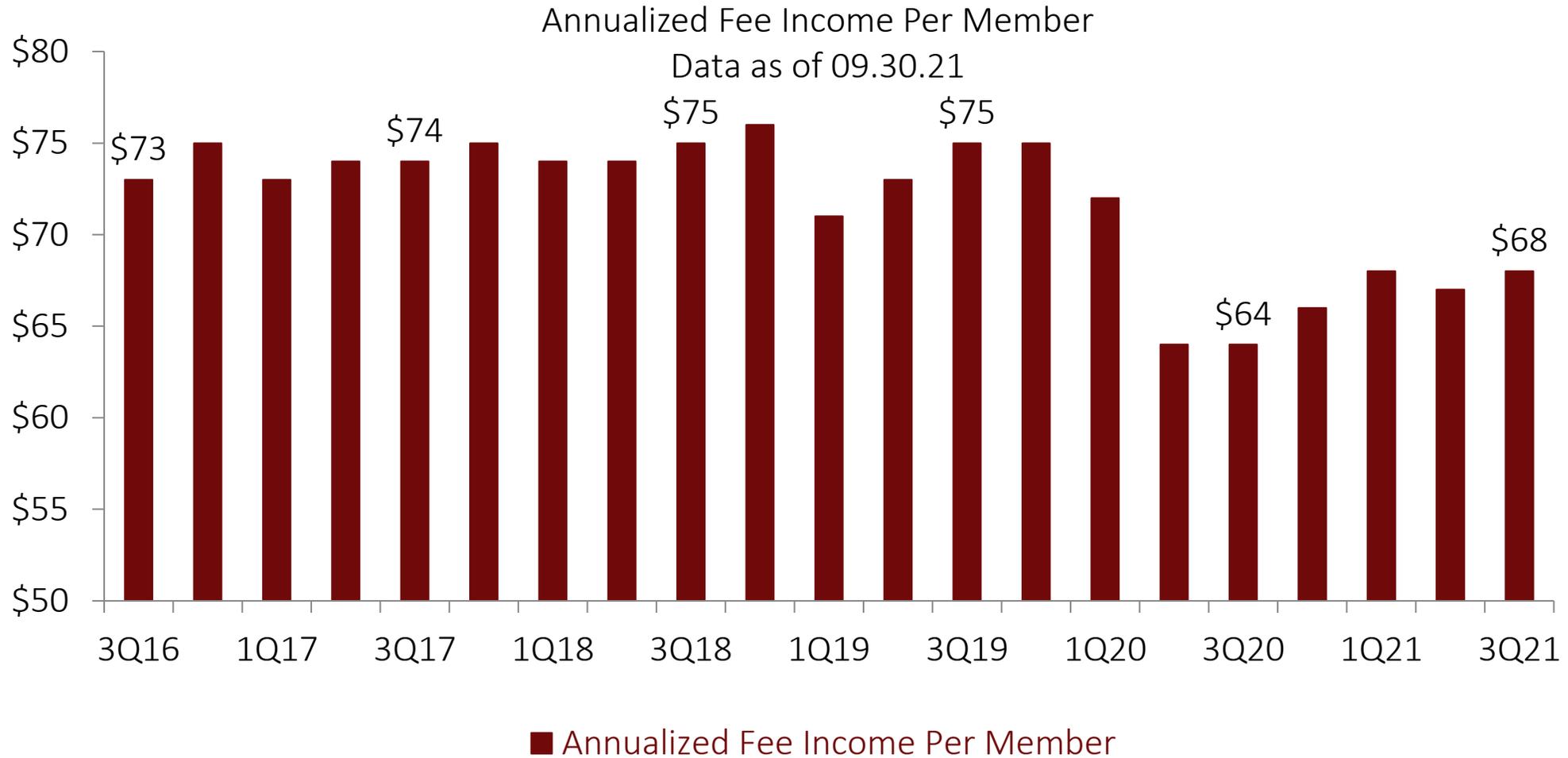
# Yields remain unchanged



# The gap between the net interest margin and operating expense ratio stays steady



# Credit unions cut fees in pandemic, and they remain below average





## **Affinity Becomes Iowa's First CU to Reduce, Eliminate Fees**

By Michael Ogden

The decision comes as credit union officials attempt to help members break the cycle of

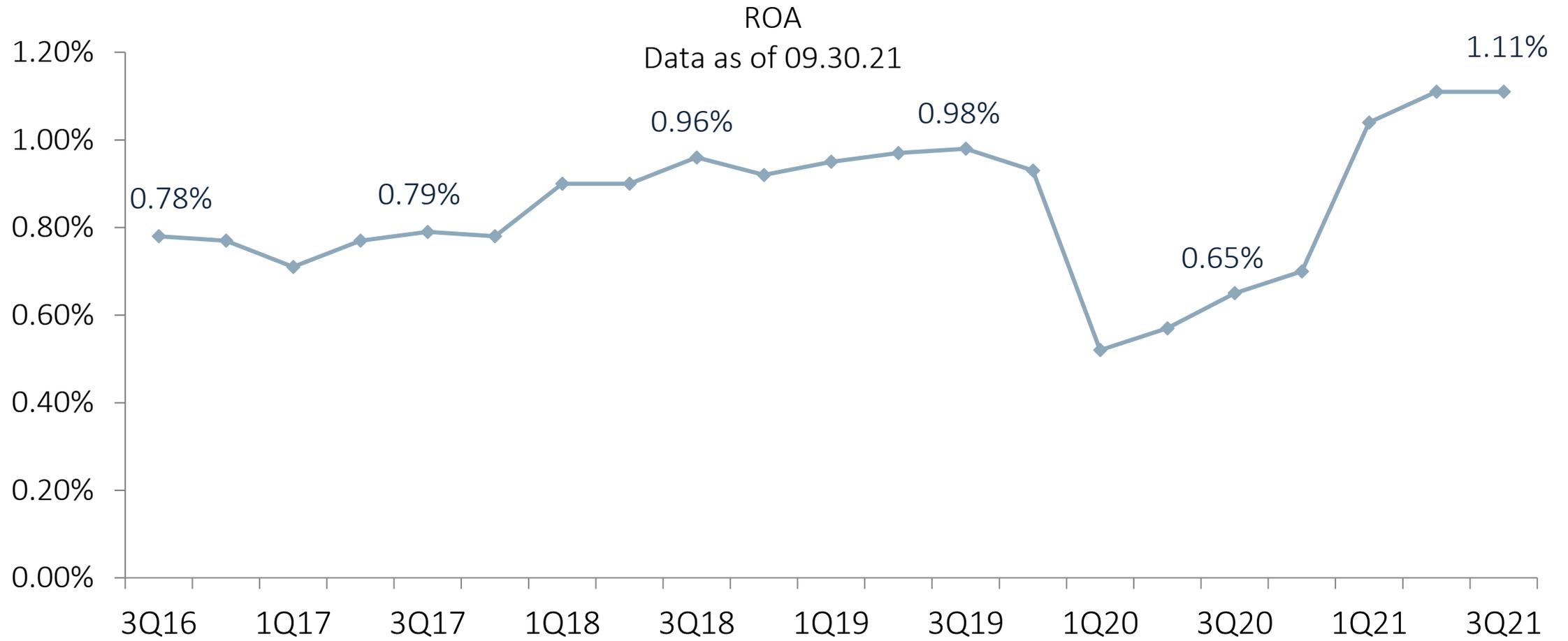


## **Westerra CU Rebrands, Drops Fees, Launches Modern 'Transformation'**



## **Fee Elimination, Reductions Go Into Effect Nov. 1 at Two Large CUs**

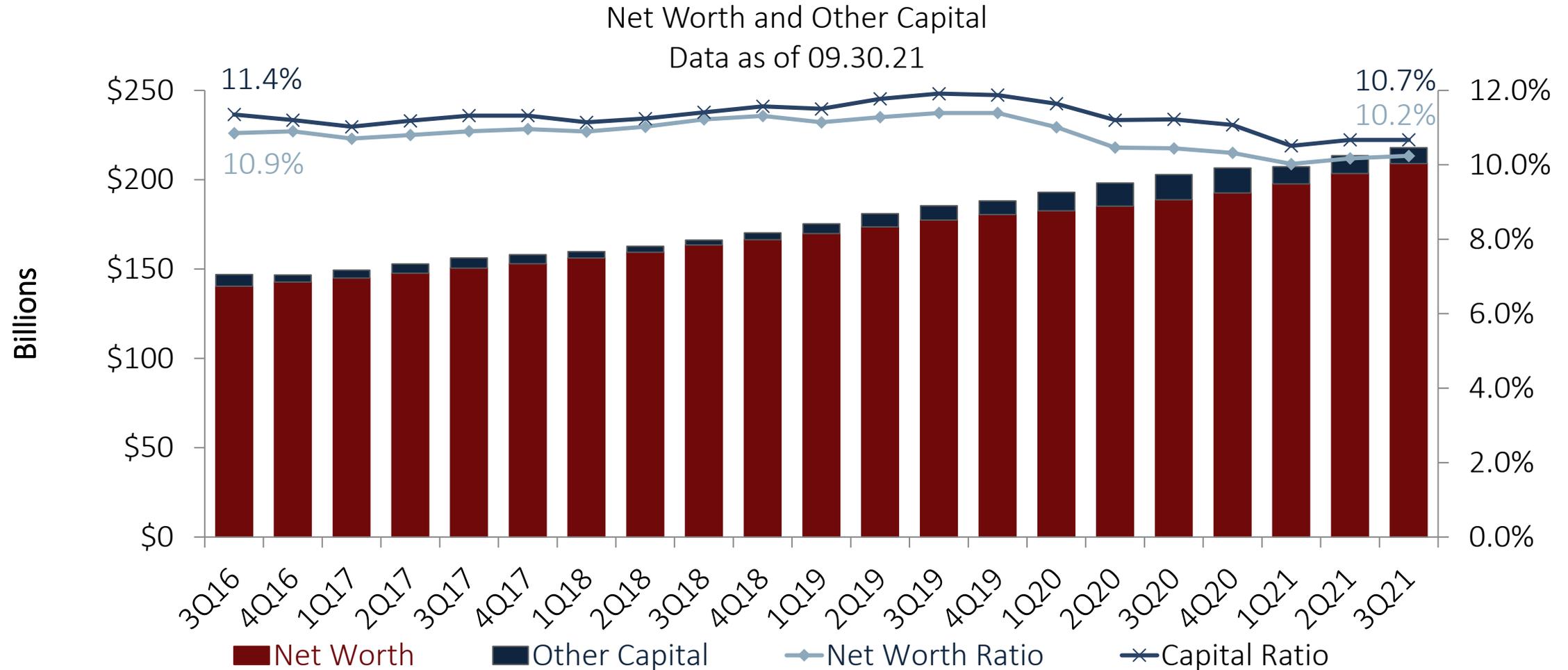
# ROA at highest levels this century



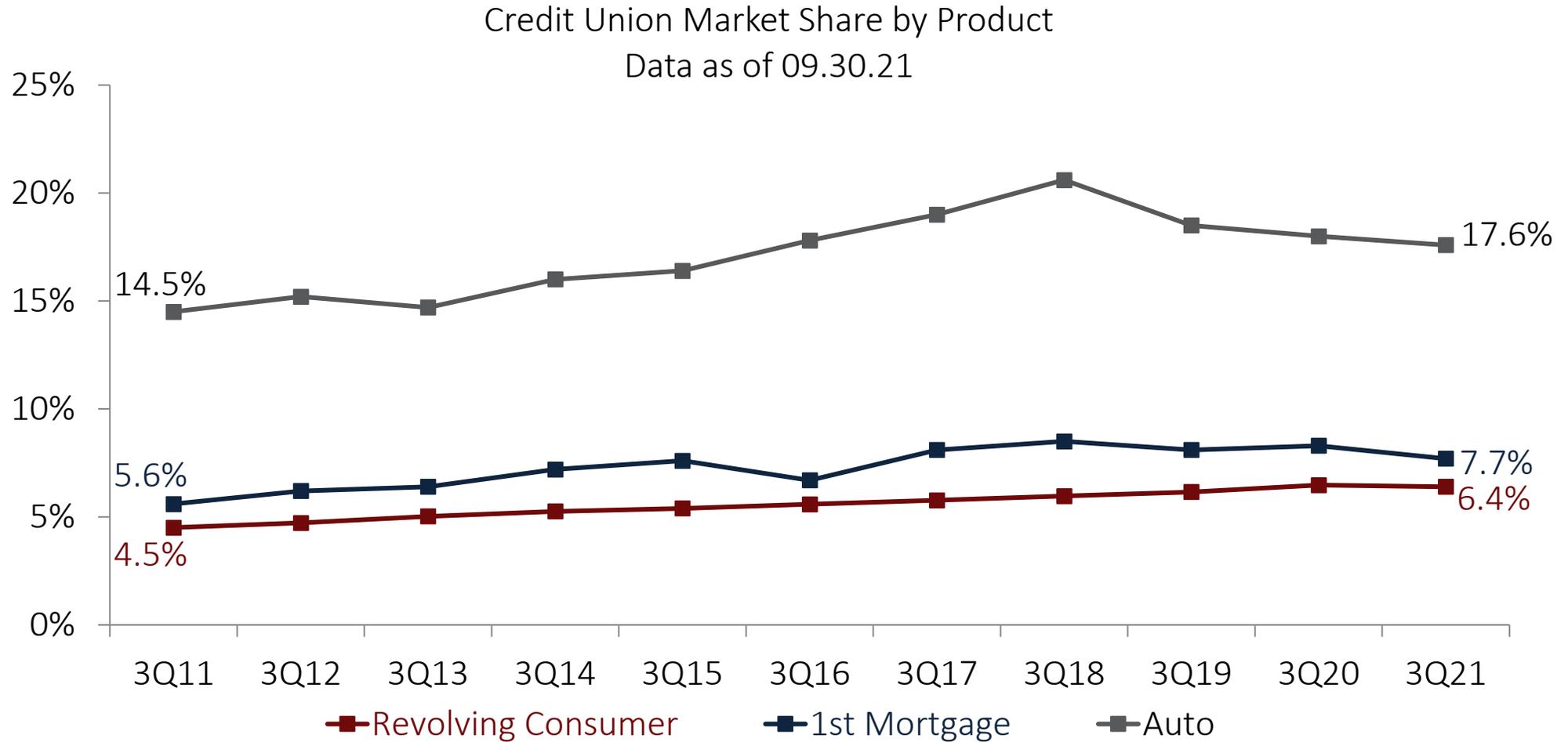
## Most ROA growth came from expense controls

	As of 09.30.2021	As of 09.30.2020	12-mo. Change (bps) 09.30.2021
Interest Income/Avg. Assets	3.03%	3.61%	-58
Interest Expense/Avg. Assets	0.44%	0.74%	-30
Net Interest Margin	2.59%	2.87%	-28
Non-Interest Income/Avg. Assets	1.39%	1.37%	+2
Non-Interest Expense/Avg. Assets	2.80%	3.02%	-22
Provision for Loan Losses	0.06%	0.56%	-50
ROA	1.11%	0.65%	+46

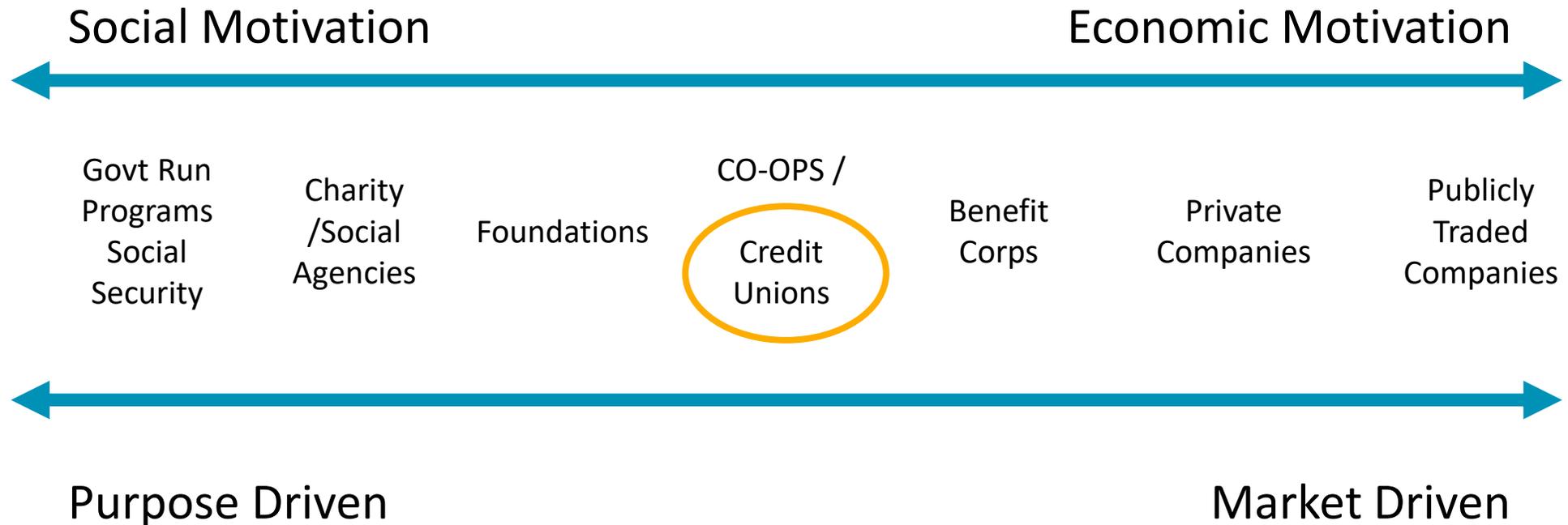
# Strong earnings bolster industrywide capitalization



# Despite industry-wide growth, credit unions are ceding market share to banks and other lenders



# Spectrum of Economic Organizations

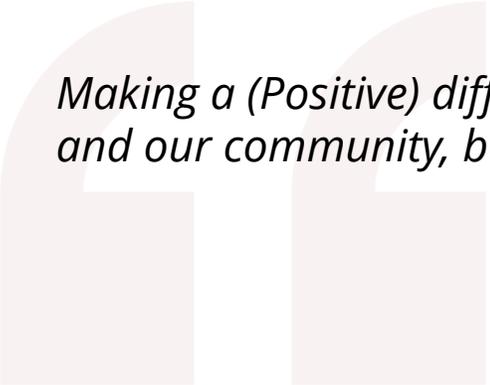


# Measure Your Mission

How to Quantify Credit Union Impact



# How Credit Unions Define Impact



*Making a (Positive) difference in the lives of our members, our employees, and our community, both now and in the future."*

*How we improve members' lives. How many jobs we create in our communities. How much we spend on third parties.*

*Our impact is defined by the strategic goals we pursue in serving five specific constituents. **Members, Employees, Our Community, the CU Industry, Our CU***

*Value that extends well beyond product or price, leaving members feeling like we are the best choice of all available options.*

*Measurable change as a result of a deliberate action.*





# Finding Common Ways to Define/Measure

## Employees

---

Living Wage, 401K, Career Advancement, Employee Giving, Volunteer Support, DEI

## Community

---

Products & Services, Institutional Footprint

## Members

---

Emergency Savings, Home Ownership, Financial Management, Environment, Citizenship, Other

## Environment

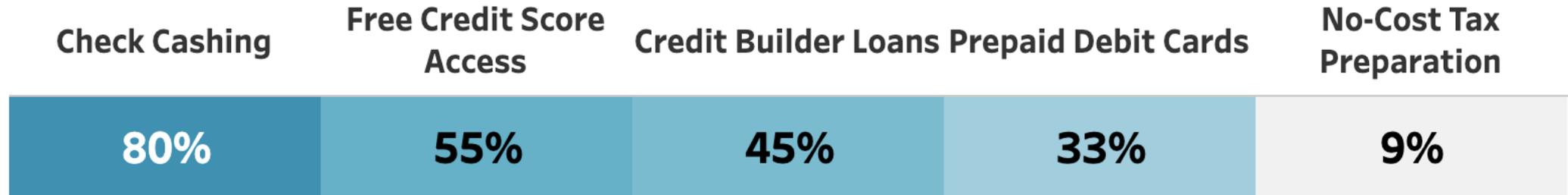
---

Economic Development, Foundations, Credit Union Contributions

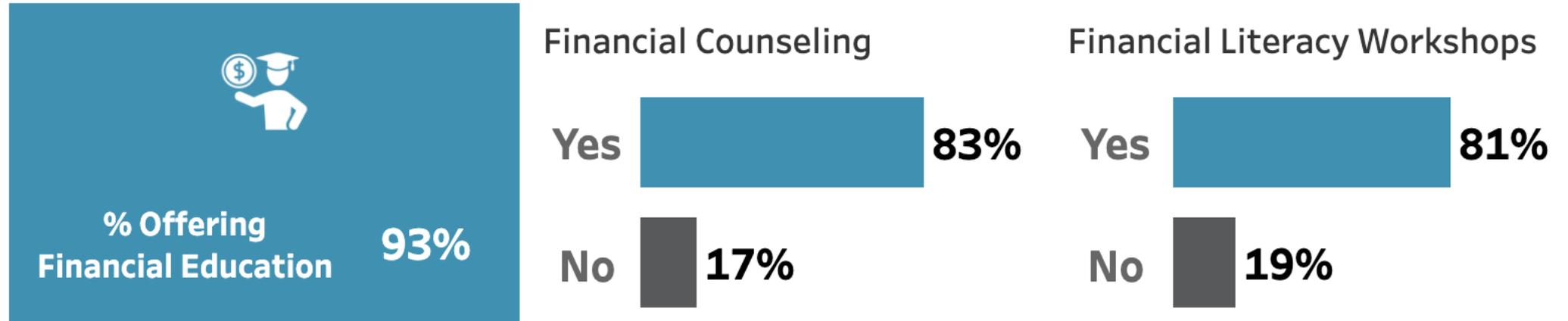


## Member Impact: Financial Management

What percent of participating credit unions offer these member services?



### Financial Wellness



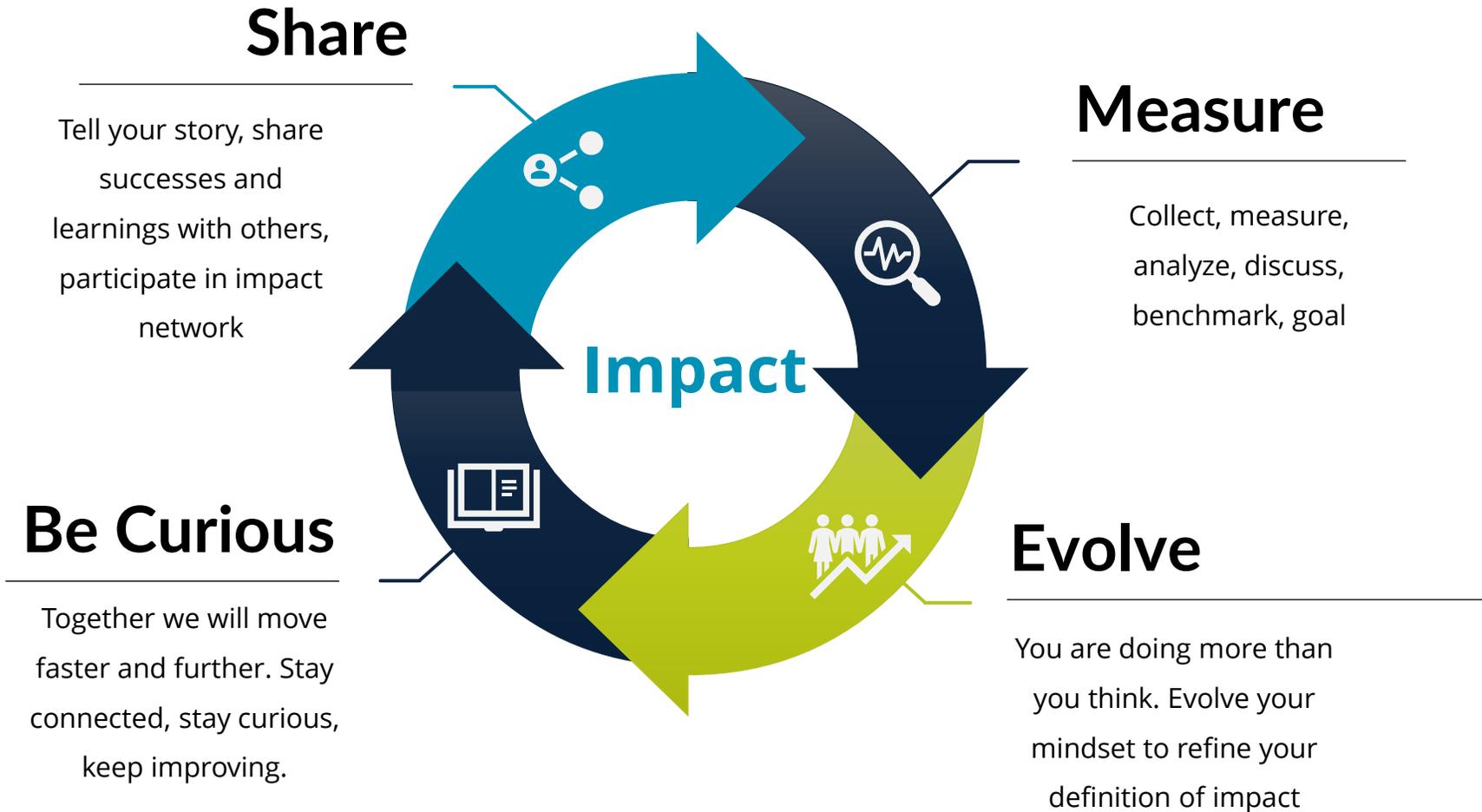
### Unique Member Services Offered



## What We've Learned So Far

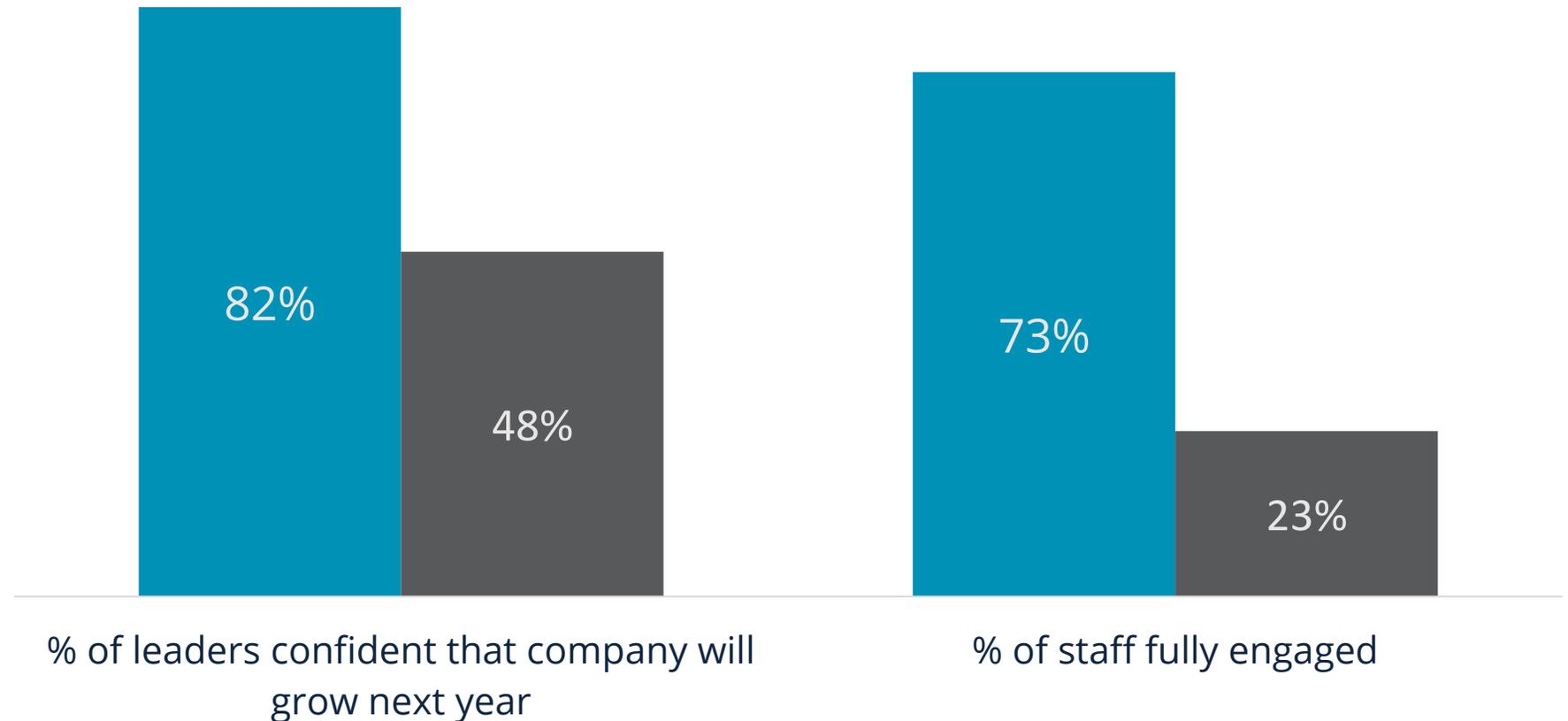
- This dataset will evolve
- Logistics is the key barrier
- Credit unions are humble!
- This is a collaborative project within the credit union
- Already inspiring conversations and new ideas

# Socialize a Broader Definition of Success



# The Impact on Your Employees

- Companies with a strong sense of purpose
- Companies without a strong sense of purpose

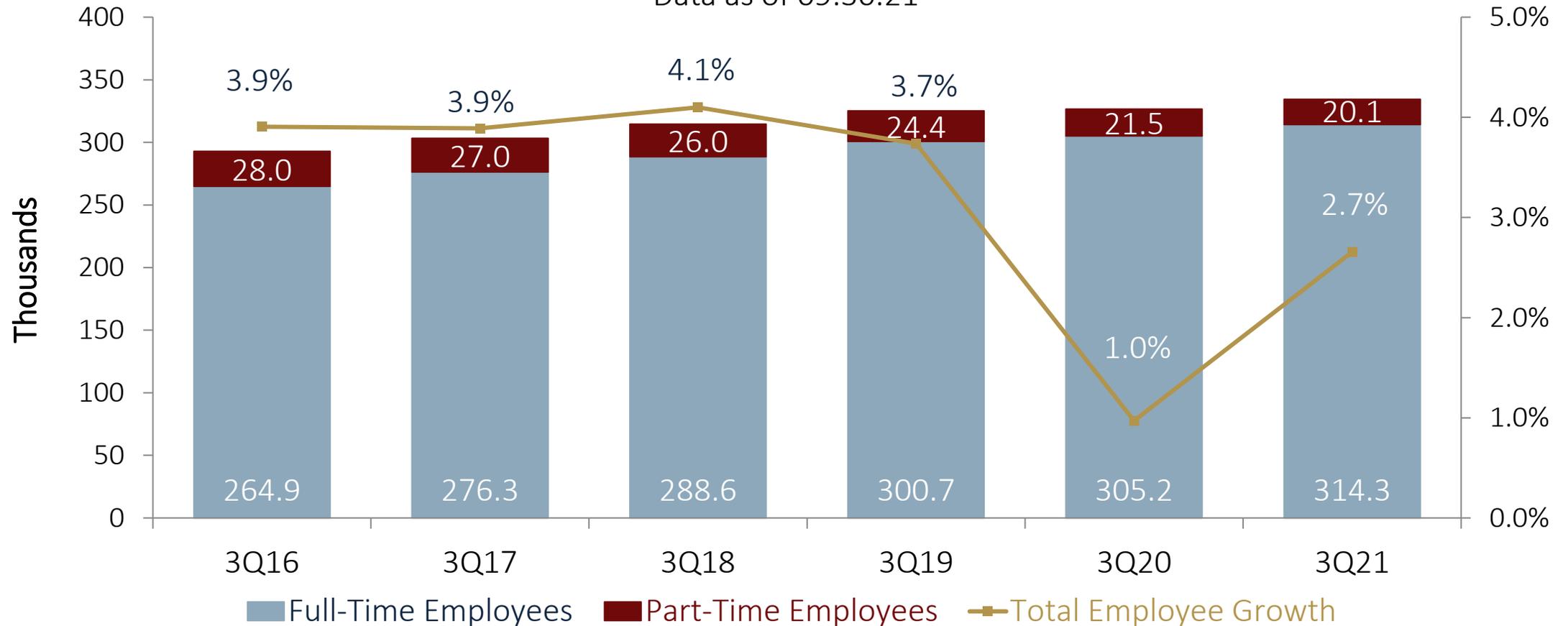




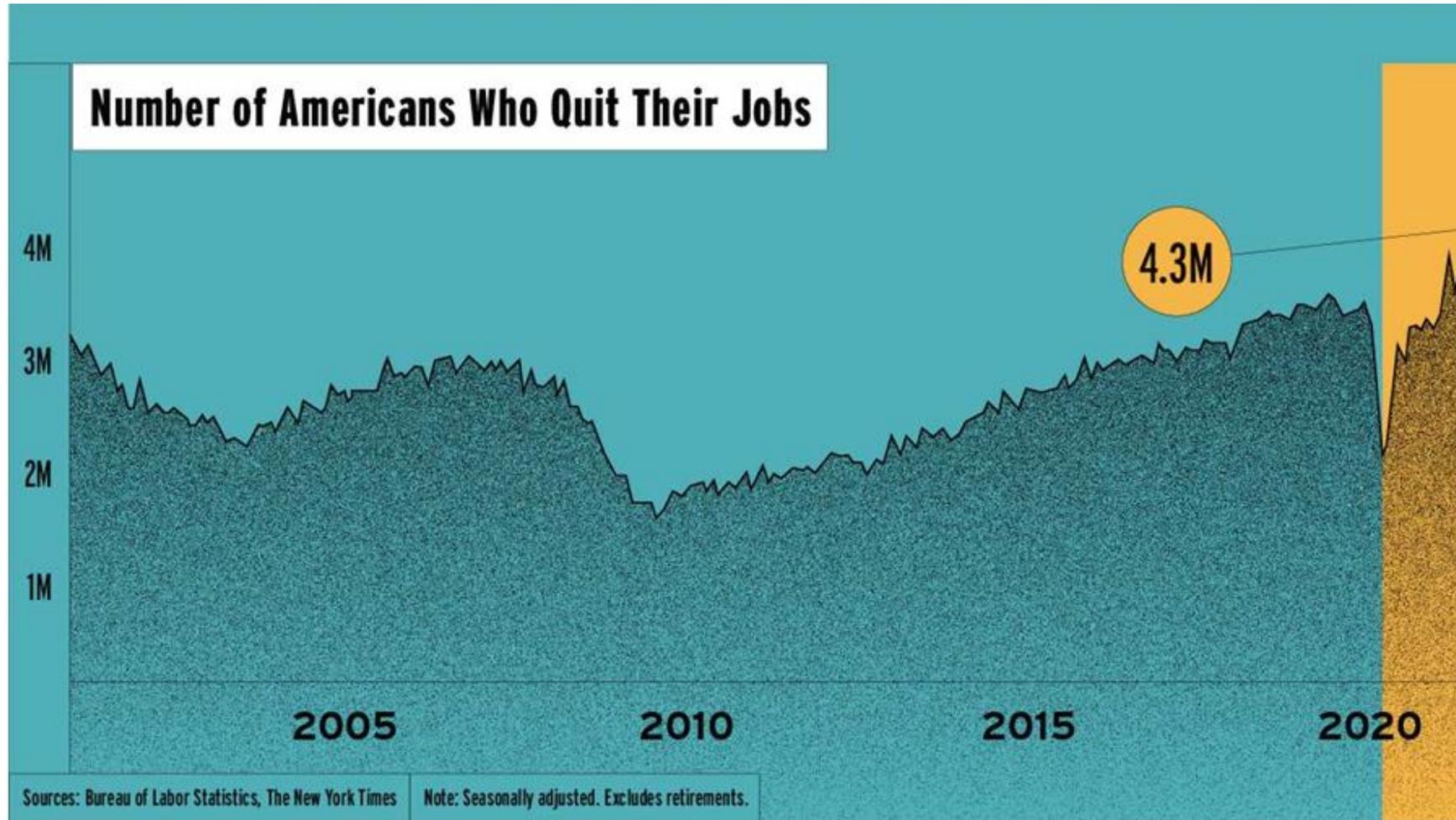
~~Human Capital~~  
The Most Important  
Asset of All: Your People

# The ability to hire and retain employees is on the top of every CEOs' agenda in 2021

FT & PT Employees and Annual Total Employee Growth  
Data as of 09.30.21



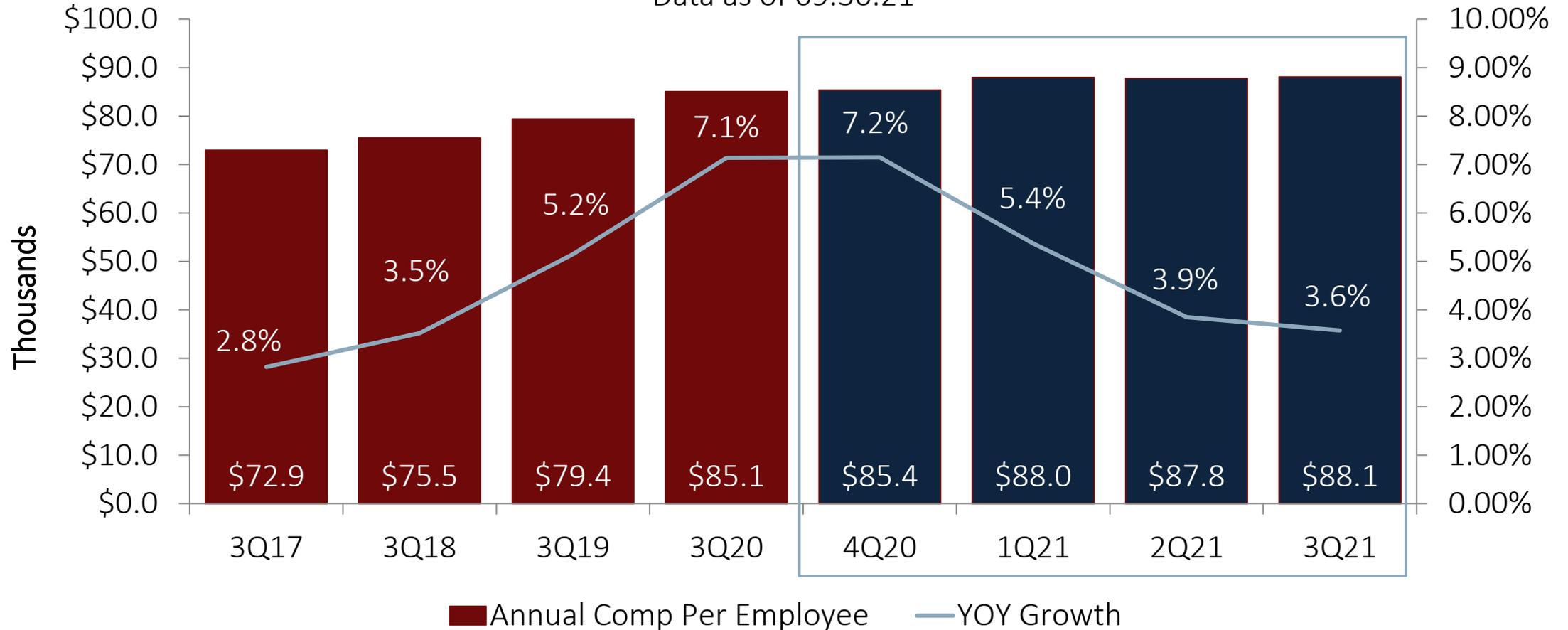
Tight labor markets pose issues to credit union staffers, especially on the front lines



# Compensation increased over the year as credit unions fight to compete for a front-line workforce in high demand

Annual Salary & Benefit Expense per Employee and Annual Growth

Data as of 09.30.21



Avg. Minimum Starting Wage (Hrly)

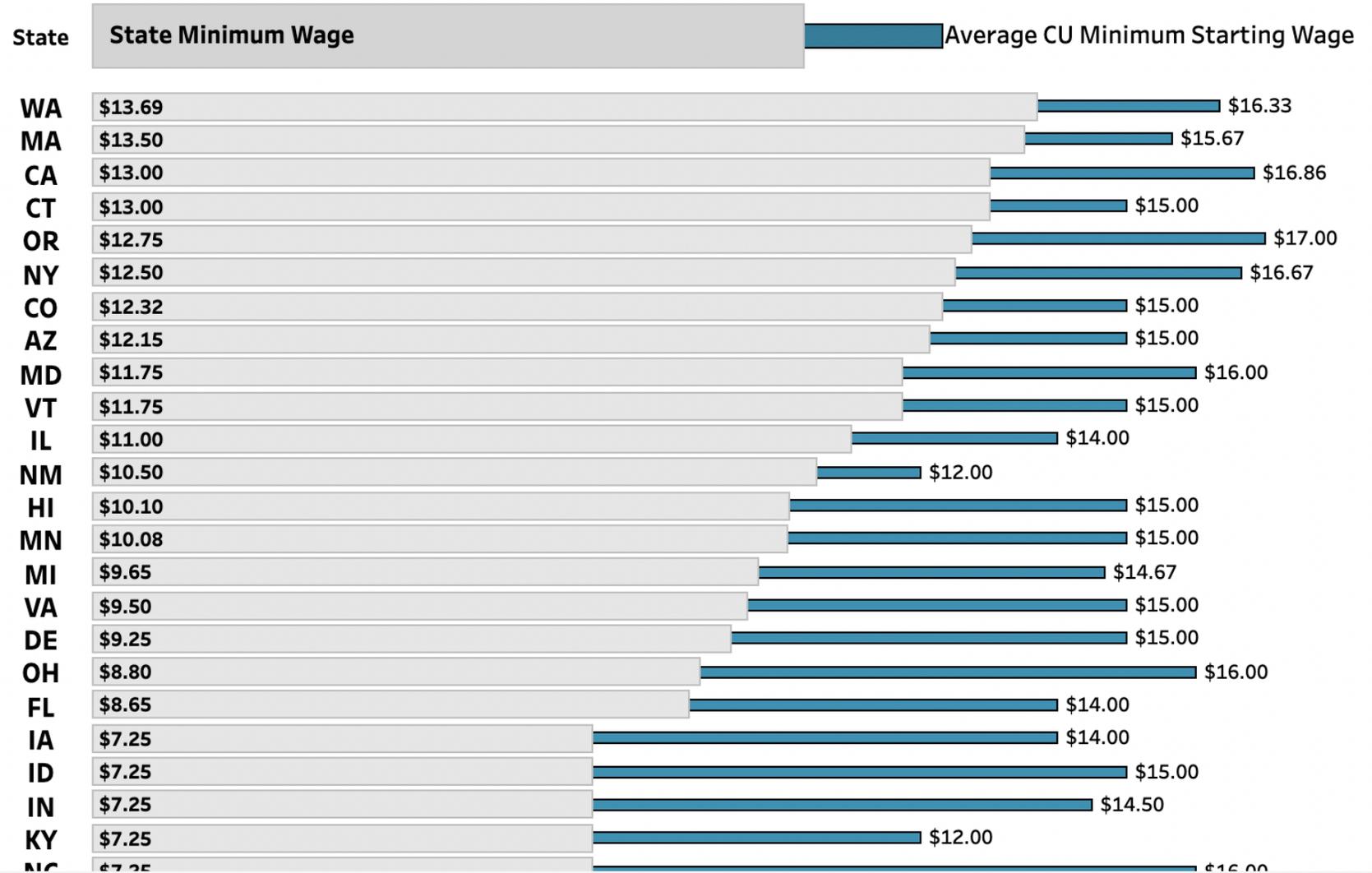
Avg. % Difference From State Min. Wage

\$14.91

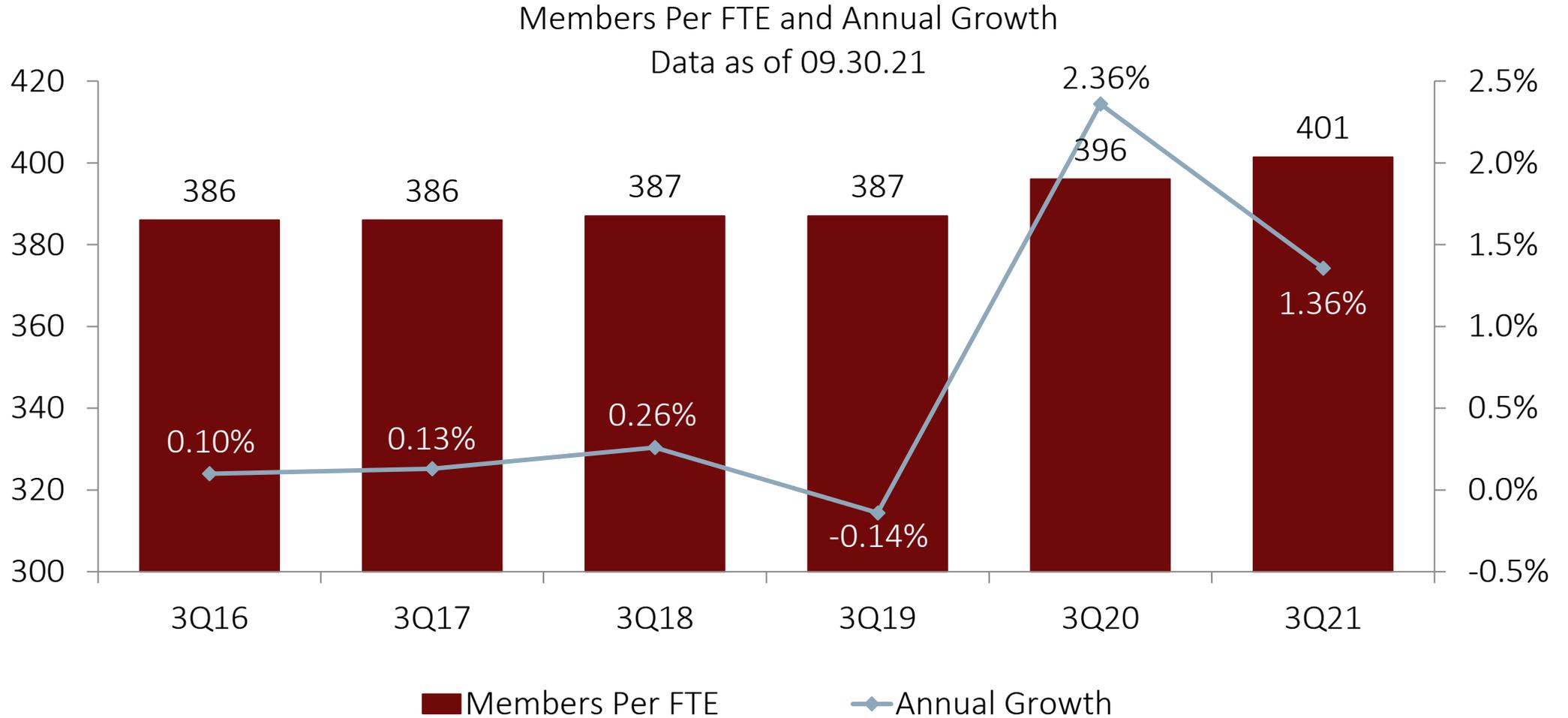
154%

### The CU min. starting wage was consistently above the state minimum wage.

LA, TN, and AL do not have state minimum wage or adhere to the federal minimum wage.



# We are asking employees to do more for a growing membership



# Lessons & Looking Forward

- With strong earnings, the industry at large has room to take calculated risks. How can we invest in our staff, members, and communities to maximize our impact?
- COVID accelerated the adoption of technology-driven member relationships. How will these changes affect financial delivery channels in the long run?
- We need to go beyond table-stakes to differentiate in a commodity market. How do we rediscover our purpose?

# THANK YOU FOR WATCHING



1001 Connecticut Ave NW  
Ste. 1001  
Washington, DC 20036



[callahan@callahan.com](mailto:callahan@callahan.com)  
[www.callahan.com](http://www.callahan.com)



800-446-7453