

A presentation on

Economic Update & State of the Industry

William G. Berg, MBA, CCUE, CUCE, BSACS, & CUERME

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*League of Southeastern
Credit Unions & Affiliates*

National & Local Issues

- **Risk Based Capital Rule & Business Loans**
- **CECL**
- **ADA/Website Compliance**
- **The Economy**
- **The State of the Industry**

Risk-based Capital Rule

- The NCUA delayed the current effective date of the risk-based capital rule approved in October 2015 to Jan. 1, 2020. Previously, the effective date was Jan. 1, 2019.
 - **“This proposed rule is a substantive solution, not just another delay,” Board Member Rick Metsger said. “It will give the agency time to finalize its systems and give the handful of complex credit unions who do not have adequate risk-based capital time to raise capital or adjust their balance sheets to achieve compliance and protect their members. ...”**

Regulatory Relief

- Importantly, this legislation also carried a major charter enhancement provision, **exempting one- to four-family non-owner occupied loans from the member business lending cap**. Taken together with our success on the NCUA's MBL rule, **which exempts from the cap loan participations purchased from other credit unions**, we can officially declare final victory on the system's 20-year battle to restore credit union business authority.

Regulatory Relief

- Congress to enact the first major piece of regulatory relief legislation since 2006 – S2155.
- Legislation includes several important credit union priorities, including:
 - Amendments to the Dodd-Frank Act to reduce regulatory burden, a provision that holds the **NCUA** accountable by requiring it to hold an **annual hearing on the budget**, and a provision that **protects credit union officials that report suspicion of elder abuse**.

FASB's CECL MODEL

- After the financial crisis in 2007-2008, FASB (Financial Accounting Standards Board) decided to revisit how financial institutions estimate losses in the ALLL (Allowance for Loan and Lease Losses) calculation.
- The current existing impairment model is based on incurred losses when it is likely that we will not collect payments in full under the originally contracted terms. That model will be replaced by CECL.

FASB's CECL MODEL

- **Under CECL, financial institutions will be required to use historical information, current conditions, and reasonable forecasts to estimate the expected loss over the life of the loan.**
- **This transition will bring significantly greater data requirements and changes to methodologies to accurately account for expected losses.**

FASB's CECL MODEL

- Credit unions will be required to comply with CECL guidance beginning January 1, 2022.
- You should have already begun obtaining granular data on your loan portfolio including delinquencies, charge offs, and recoveries.

FASB's CECL MODEL

- **Because of the change from the incurred loss model to the expected credit loss model, credit unions will be permitted to make a one-time transfer from retained earnings into the ALLL without going through the income statement.**
- **This is both good news and bad news.**

FASB's CECL MODEL

- **We don't have to adjust the ALLL account with initial, large impacts to net income.**
- **We can transfer money from our retained earnings to the ALLL account.**
- **Thomas Curry, Comptroller of the Currency has stated that banks should expect a 30% to 50% increase in their allowance level.**

FASB's CECL MODEL

- **During FASB meeting in December 2018, Board Chairman Russ Golden announced that FASB will host a public roundtable discussion on implementation issues related to the credit losses standard. FASB expects the roundtable to take place in January and include several discussion topics:**
 - **FASB staff's research on credit losses agenda requests**
 - **A proposal to consider an alternative to the income statement impact of CECL.**



FASB's CECL MODEL

- **FASB staff announced its work on a CECL implementation Q&A document that will be published in January. The document will include discussion of the use of WARM (weighted average remaining maturity) as part of a CECL calculation.**

ADA/Website Compliance

- **The Fourth Circuit of Appeals has ruled in favor of Department of Labor Federal Credit Union (DOL FCU) related to a frivolous lawsuit alleging website noncompliance with the Americans with Disabilities Act (ADA). A panel of federal appeals court judges determined the plaintiff lacked standing.**
- **Credit Union National Association (CUNA) stood alongside DOL FCU and filed an amicus brief in support of the credit union last year. This landmark decision would provide binding legal precedent in states under the Fourth Circuit's jurisdiction.**
- **Griffin v. DOL FCU is especially significant because it is the first CU-specific ADA case to be decided at the appellate level.**

ADA/Website Compliance

CUNA and the state CU leagues of Wisconsin and Illinois filed an amicus on Thursday, December 20, in the U.S. Court of Appeals for the 7TH Circuit. The brief was submitted in support of a credit union facing a lawsuit related to ADA website accessibility.

CUNA's primary arguments in the case, Carello v. Aurora Policemen CU are:

ADA/Website Compliance

- **That the appellant lacks standing, and had not suffered concrete and particularized harm because he does not meet the eligibility requirements to become a member Aurora Policemen FCU;**
- **A website is not a place of public accommodation, and therefore the ADA does not apply; and**
- **Applying Title III of the ADA to websites renders the statute impermissibly vague in the absence of any implementing regulations by the Department of Justice.**
- **CUNA consulted with all state leagues in the 7TH Circuit Court's jurisdiction when preparing its brief.**

The Economy

- **The Federal Reserve (Fed) hiked interest rates four times last year (a total of 9 hikes since it began raising rates) and those increases were supportable. However, as the short-term rates get closer and closer to neutral it becomes much more difficult for the Fed to gage the amount and direction that is should take with interest rates. Inflation will need to pick up to support future increases.**
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- **The neutral rate assumes very stable inflation, full employment, and economy operating normally.**

The Economy

- **Last year, the economy had some very strong tailwinds:**
 - **The large tax reduction**
 - **Continuation of the now longest recovery on record**
 - **Continuation of the reduction in unemployment rates**
- **With few headwinds and strong tailwinds the GDP was very good in 2018. 2019 is quite likely to be different!**



The Economy

2019 has some very strong headwinds:

- **Two hikes in short term interest rates down from three**
- **Globally there are concerns with what will happen with Brexit and Italy**
- **The trade war with China (if no agreement is made tariffs will go up from 10% to 25%)**
- **The overall world economy is slowing down**

The Economy

- **The Yield Curve is flatter. The 2 years to 10-year yield curve being flat or inverted is the most accurate predictor of a recession. However, the economy can bounce around for some time with a flat or inverted yield curve before a recession hits. Economic data always looks good when the yield curve inverts.**
- **The stock market suffered its worst December since 1931. (The stock market could be giving us pre-quake tremors). Stocks set new all-time highs in September before imploding at year-end.**



The Economy

2019 has some very strong headwinds continued:

- **Each 1 basis point (BP) increase in interest rates because of the huge amount of government debt costs \$2 billion when those increases are fully factored into the costs of government borrowing.**
- **Shut down of parts of the Federal Government (SBA and FHA Lending has been shut down)**
- **Business investment across all categories has slowed**
- **Home sales have slowed**

The Economy

2019 has tailwinds

- **GDP growth has accelerated year over year**
- **Continuation of the now longest recovery on record**
- **Continuation of the reduction in unemployment rates**
- **We now have 99 months of consecutive job growth (a record of 8 years and 3 months) The tax reduction push to the economy has now been factored in and is no longer a push**
- **Wage growth has picked up**

The Economy

- **Jorge Augustín Nicolás Ruiz De Santayana, (born December 16, 1863, Madrid, Spain—died September 26, 1952, Rome, Italy), Spanish-American philosopher, poet, and humanist who made important contributions to aesthetics, speculative philosophy, and literary criticism. From 1912 he resided in Europe, chiefly in France and Italy.**
- **“Those who do not remember the past are condemned to repeat it.” George Santayana**

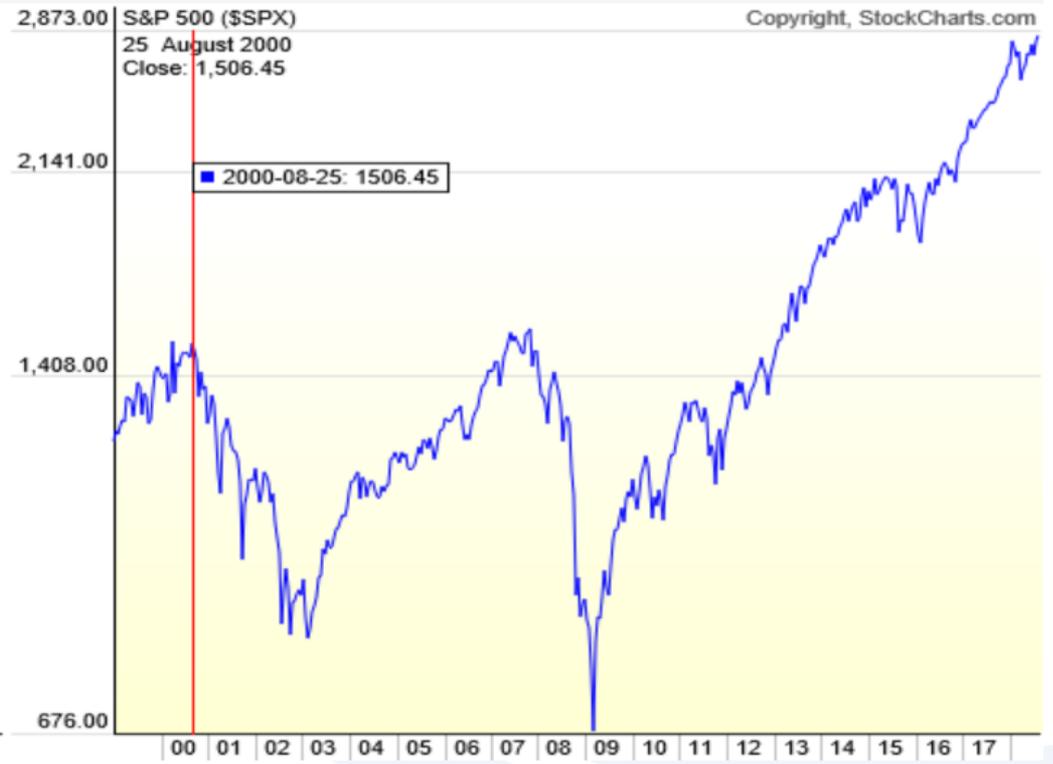
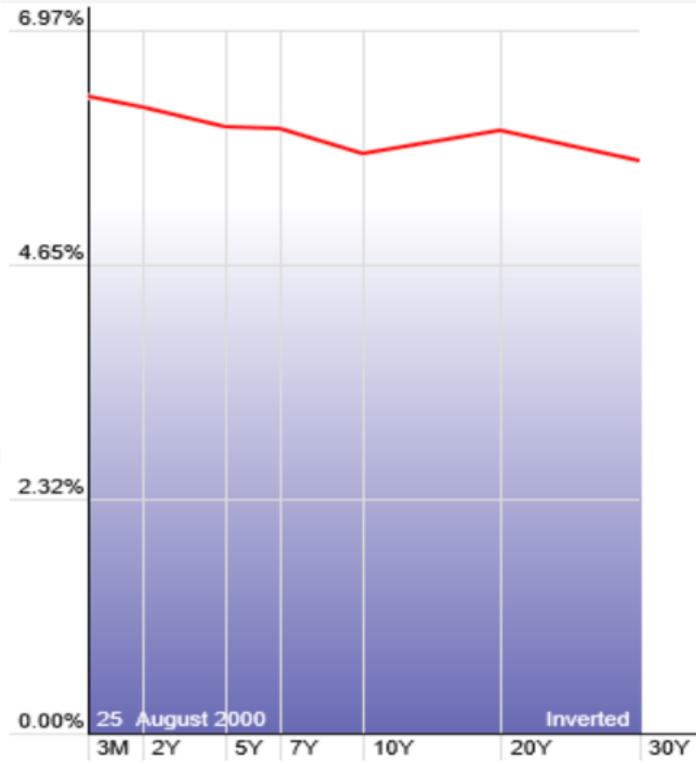
The Economy

- **A few moments ago, when I was talking about headwinds, I promised you more information. Well here it is.**
- **Expansions are followed by contractions. It has always been so and it always will be so – Economics 101**

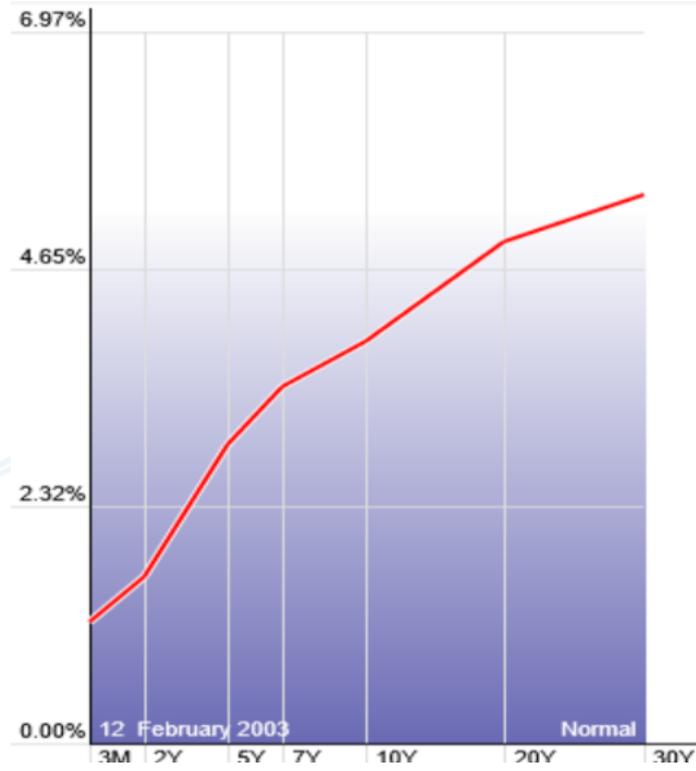
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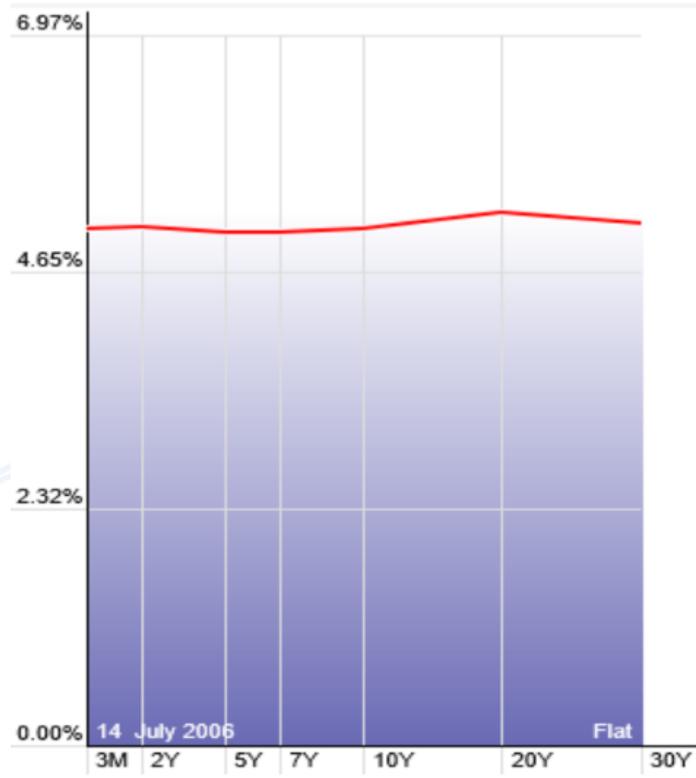
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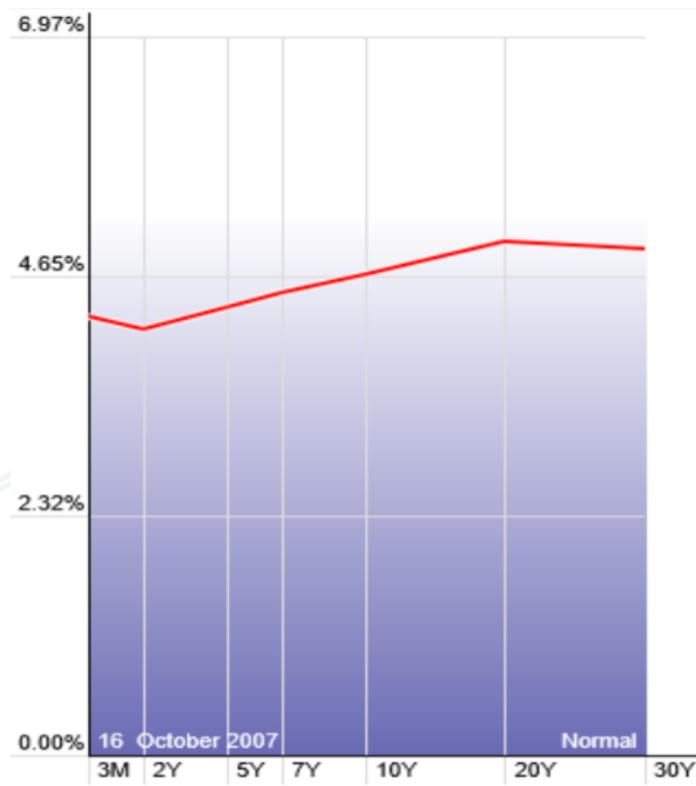
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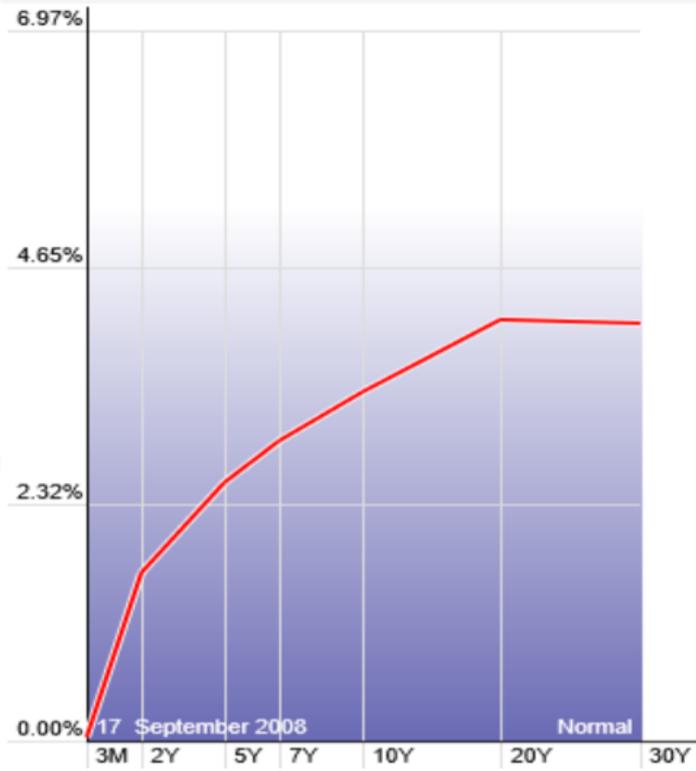
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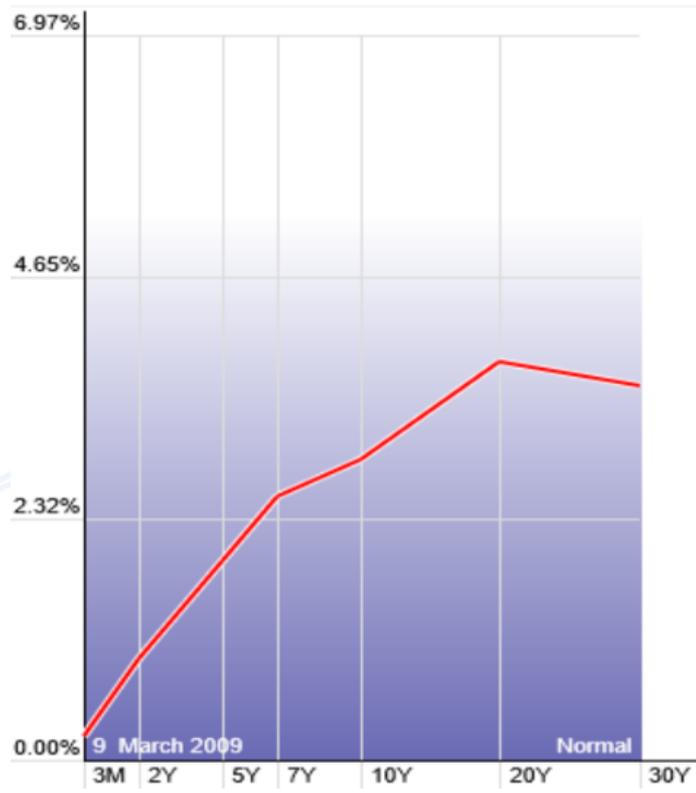
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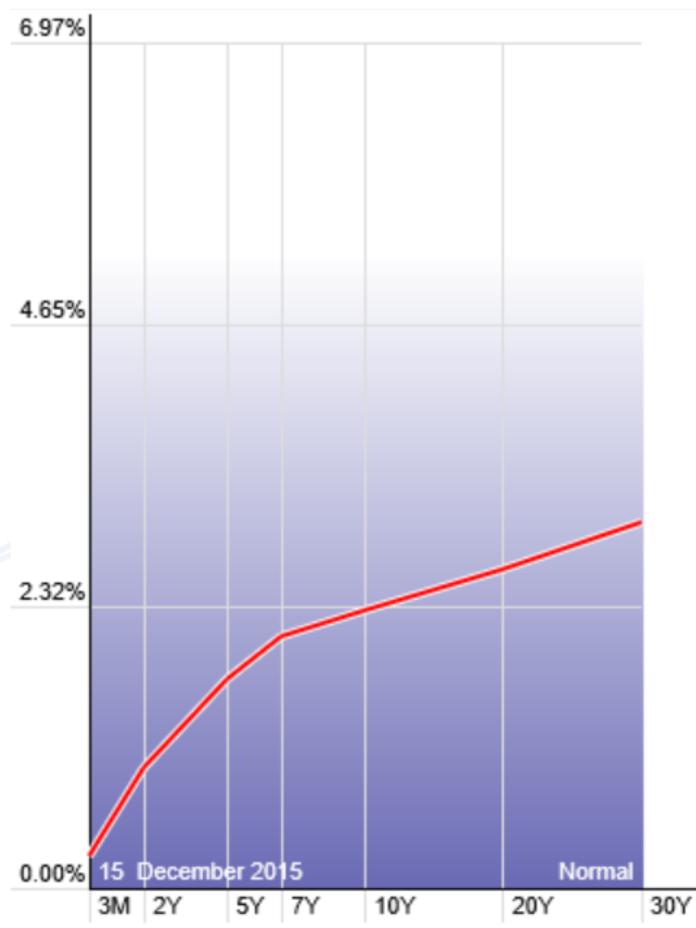
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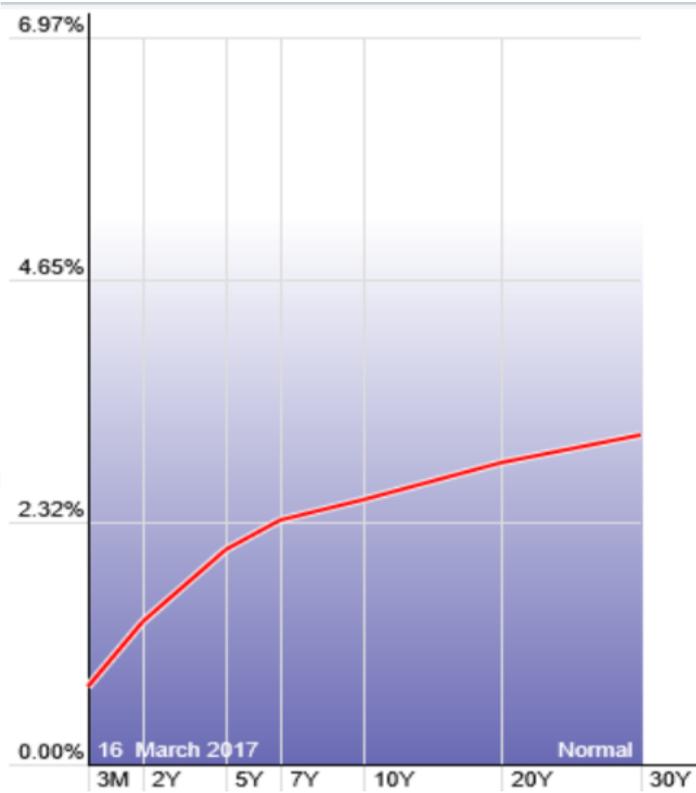
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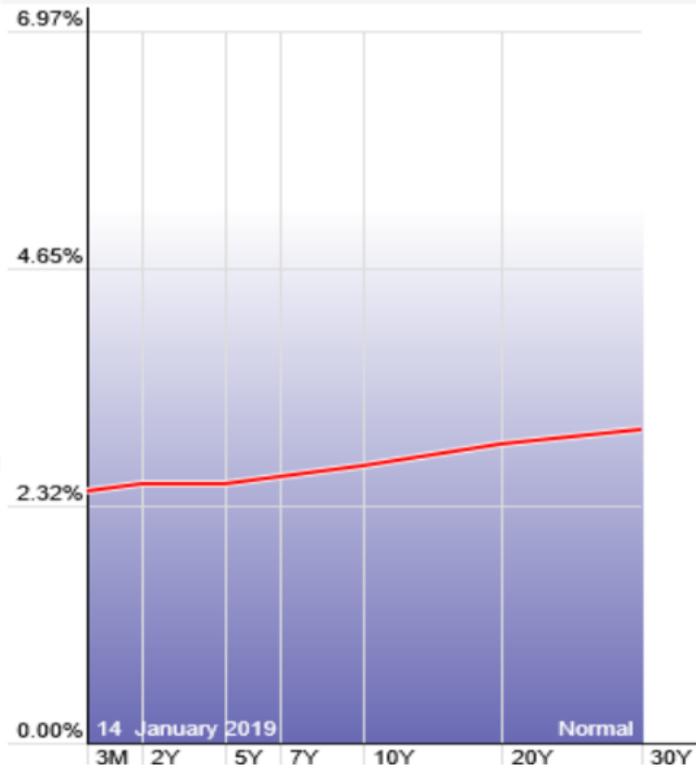
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The Economy



The Economy



The Economy



The shrinking numbers of credit unions

- In 2000, there were 10,439 credit unions.
- As of September of 2018, that number had dropped to 5,551 or a 46.8% drop!

- In 2000, there were 249 Florida credit unions.
- As of March of 2018, that number had dropped to 133 or a 46.6% drop!

The shrinking numbers of credit unions

- **NCUA Region III merged into the Austin Region on 12.31.18.**
- **Size matters and obtaining Economies of Scale should be a critical component of your strategic plan**
- **Florida Profile**
- **Excel Handouts**

The shrinking numbers of credit unions

- Is truly a tale of two cities or sizes of credit unions!
- As of Q4 2018 (the most current call report data available). Credit unions over \$500 million in assets are performing very well as a group while credit unions under \$10 million in assets are struggling in Florida. Of course, these are averages with some credit unions exceeding the average and others not. The next slide demonstrate the positive correlation of size with performance and some of the operating economies of scale.

Thank You!

Please feel free to contact me with questions using the below information:

William G. Berg, MBA, CCUE, CUCE, BSACS,
CUERME

Vice President, Compliance Training and
Information

866.231.0545 x1028

bill.berg@lscu.coop

