Credit Union National Association

CUNA Economic and Credit Union Forecast

Fourth Quarter 2019

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CUNA Economic and Credit Union Forecast

Fourth Quarter 2019 Overview

Economic growth is likely to slow to its long-term trend of about 1.8% in 2020. Although U.S. consumers remain confident and continue to spend, several factors will contribute to a slowing economy, including contraction in the manufacturing sector, uncertainty regarding the trade war with China and upcoming presidential election, slower international growth—particularly in Asia and Europe—and faded effects of recent tax cuts. However, we see no signs of an imminent recession. Nonetheless, credit unions are likely to feel the effects of slower growth, particularly the drop in auto sales and auto loans, which will reduce membership and loan growth. Portfolio quality is likely to deteriorate slightly but credit union loan portfolios should remain relatively healthy throughout 2020. Credit union liquidity is also expected to improve as savings and asset growth accelerate.

The most significant changes to our previous forecast include:

- Our forecasted economic growth rose from 2.1% in 2019 and 1.5% in 2020 to 2.3% and 1.8%, respectively.
- We now expect unemployment to reach 3.8% in 2020, a decrease from our previous forecast of 4.0%.
- We increased our predicted credit union savings growth from 7.0% in 2019 and 8.0% in 2020 to 8.0% and 9.0%, respectively.
- Our 2019 forecasted membership growth rose from 3.0% to 3.3% for 2019, but remains at 2.5% for 2020.
- We increased our forecasted credit union earnings (ROA) from 0.92% in 2019 and 0.75% in 2020 to 0.95% and 0.80%, respectively.

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CUNA Economic Forecast

Fourth Quarter 2019

	Actual Results		Quarterly Results/Forecasts				Annual Forecasts	
	5 Yr Avg	2018	2019:2	2019:3	2019:4	2020:1	2019	2020
Growth rates:								
Economic Growth (% chg GDP)*	2.42%	2.90%	2.00%	2.10%	2.00%	1.50%	2.30%	1.80%
Inflation (% chg CPI)*	1.52%	2.44%	1.82%	1.65%	3.34%	1.80%	2.29%	1.80%
Unemployment Rate	4.90%	3.90%	3.63%	3.50%	3.50%	3.60%	3.50%	3.80%
Federal Funds Rate (effective)	0.69%	1.83%	2.40%	1.90%	1.55%	1.55%	1.55%	1.55%
10-Year Treasury Rate	2.35%	2.91%	2.34%	1.68%	1.92%	1.95%	1.92%	2.00%
10-Year-Fed Funds Spread	2.22%	1.08%	-0.06%	-0.22%	0.37%	0.40%	0.37%	0.45%

*% change, annual rate. All other numbers are end-of-period values.

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CUNA Economic Forecast

- **Economic growth:** The U.S. economic expansion is now in its 11th year, the longest on record. Despite some recent scares, most recession fears have receded now that the yield curve is back in positive territory, consumers remain confident, and there is a preliminary trade agreement between the U.S. and China. However, the economy is likely to continue to slow due to numerous factors, including slow manufacturing growth and business investment, the effects of the Boeing crisis, slower growth in Europe and China, and continued uncertainty regarding the Trade War and a pending presidential election that could have wide-ranging economic consequences. Moreover, the effects of the Tax Cuts and Jobs Act have now faded, so the economy is likely to return to its long-term estimated growth rate of 1.8%, which is influenced by relatively slow population and productivity growth.
- **Unemployment:** One particularly bright spot in the economy is the strong labor market. As of year-end 2019, the U.S. unemployment rate remains at a near record low of 3.5%. We expect labor markets to remain strong in 2020 but the unemployment rate is likely to rise slightly towards its natural rate of between 4.0% and 4.5% over the next few years. We expect the unemployment rate to grow to 3.8% by the end of 2020, given the slowing economy.
- **Inflation:** Headline CPI inflation experienced a strong fourth-quarter increase of 3.3% and an annual increase of 2.3% for 2019, up from the 1.9% rise in 2018. However, this was largely driven by high energy prices and, overall, inflation remains relatively muted given the strong labor market. The Fed's preferred measure of inflation—core personal expenditure consumption (PCE)—is up just 1.6% over the past 12 months as of November 2019, well below the Fed's target of 2.0%. We expect inflation to remain relatively low in 2020 as well, with CPI headline inflation reaching 1.8% for the year.
- **Fed Funds Rate:** The Federal Open Market Committee (FOMC) has stated its commitment to keeping interest rates stable and letting economic indicators dictate any future rate moves. Barring no major changes to the economy, we expect the FOMC to maintain the effective federal funds rate at a range of 1.50% to 1.75%.

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	Actual Results		Quarterly Results/Forecasts				Annual Forecasts	
	5 Yr Avg	2018	2019:2	2019:3	2019:4	2020:1	2019	2020
Growth rates:								
Savings growth	6.0%	5.2%	0.6%	1.1%	1.8%	5.3%	8.0%	9.0%
Loan growth	10.1%	8.9%	1.8%	2.0%	2.1%	0.3%	6.5%	5.5%
Asset growth	6.5%	5.4%	0.9%	1.2%	1.8%	5.0%	7.5%	8.5%
Membership growth	3.8%	4.4%	1.0%	1.1%	0.4%	0.8%	3.3%	2.5%
Liquidity:								
Loan-to-share ratio**	80.2%	85.8%	83.3%	84.6%	84.9%	80.8%	84.9%	82.1%
Asset quality:								
Delinquency rate**	0.80%	0.71%	0.63%	0.66%	0.70%	0.72%	0.70%	0.75%
Net charge-off rate*	0.54%	0.57%	0.54%	0.55%	0.53%	0.55%	0.55%	0.60%
Earnings:								
Return on average assets (ROA)*	0.80%	0.91%	0.97%	0.97%	0.90%	0.88%	0.95%	0.80%
Capital adequacy:								
Net worth ratio**	11.0%	11.3%	11.3%	11.4%	11.4%	11.0%	11.4%	11.2%

*Quarterly data, annualized. **End of period ratio. Additional information and updates available on our MCUE website.

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- **Loan Growth & Membership Growth:** Auto loans make up roughly one-third of credit union loan portfolios but over 40% of the growth in credit union loan portfolios since the Financial Crisis. However, auto sales fell 3.9% in 2019 and have been on a downward trend over the past few years. Although lower interest rates are helping credit union mortgage lending and HELOCs, the reduction in auto sales will slow credit union loan and membership growth considerably in the fourth quarter of 2019 and into 2020. We expect below-average credit union loan growth of 6.5% in 2019 and 5.5% in 2020, and membership growth of 3.3% and 2.5%. The slower growth will be particularly hard on smaller credit unions, as credit unions with below $100 million in assets are already shrinking in terms of memberships as of September 2019.
- **Savings Growth:** As is common during periods of slower economic growth, credit union savings growth has picked up considerably over the past 12 months. This is due to consumers being more cautious in managing their finances, and to credit unions' attempts to restore liquidity by offering higher deposit rates. We forecast credit union savings growth of 8.0% for year-end 2019 and 9.0% for 2020. This will, in turn, improve credit union liquidity and reduce the credit union loan-share ratio from 84.9% to 82.1%.
- **Portfolio Quality:** The strong labor market will maintain credit union loan portfolios relatively healthy through 2020. However, we expect the delinquency and charge-off rates to rise slightly to 0.75% and 0.60%, respectively, in 2020 as the economy slows, credit union loan growth falls, and borrowers get longer into their loan terms (when payment challenges are more likely to arise).
- **ROA:** The slowing economy is likely to put downward pressure on credit union earnings, and we expect credit union ROA to fall to 0.80% in 2020. This is due to several factors, including more competition for auto loans and mortgages (which reduces interest rate margins), faster asset growth, and reduced fee income from new loans and mortgage sales.

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