CUNA Economic and Credit Union Forecast

Third Quarter 2019

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Third Quarter 2019 Overview

The U.S. economy is in its 11th year of expansion - the longest run of GDP growth in modern U.S. history. The economy is growing, but at a slower pace and it's showing signs of fragility – mostly around trade policy uncertainty. Other concerns include declining growth in manufacturing and business investment, slowing global growth, Brexit and geopolitics in the Middle East. Bright spots include the labor market, consumers, and the Federal Reserve's accommodative policies. However, if forces push in the opposite direction and affect consumer confidence, then a recession is much more likely in the next two years. Expect any recession to be shallow and relatively short-lived compared to the recent Great Recession. Whether a textbook recession occurs, credit unions should be prepared for a general slowdown in economic growth, a slowdown in loan growth, membership growth, a decrease in ROA, and other accompanying effects on credit union operations.

The most significant changes to our previous forecast include:

- We decreased our economic growth forecast for 2020 from 1.8% to 1.5%.
- We changed our forecast for the federal funds rate for year-end 2019 from a target range of 2.25% - 2.50% down to 1.50% - 1.75%. We also expect the Fed to continue its accommodative policies into 2020 and reduce the fed funds rate to a range of 1.00% - 1.25% by the end of 2020.
- We reduced our credit union loan growth forecast from 7.5% to 6.5% for 2019 and from 7.0% to 5.5% for 2020.
- We increased our ROA forecast for 2019 from 0.87% to 0.92% and we decreased our 2020 ROA forecast from 0.80% to 0.75%.

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Third Quarter 2019

	Actual Results		Quarterly Results/Forecasts				Annual Forecasts	
	5 Yr Avg	2018	2019:1	2019:2	*2019:3*	*2019:4*	*2019*	*2020*
Growth rates:								
Economic Growth (% chg GDP)*	2.42%	2.90%	3.10%	2.00%	*1.80%*	*1.60%*	*2.10%*	*1.50%*
Inflation (% chg CPI)*	1.52%	2.44%	1.63%	1.82%	*1.76%*	*2.20%*	*1.85%*	*1.75%*
Unemployment Rate	4.90%	3.90%	3.87%	3.63%	3.50%	*3.70%*	*3.70%*	*4.00%*
Federal Funds Rate (effective)	0.69%	1.83%	2.40%	2.40%	*1.90%*	*1.65%*	*1.65%*	*1.15%*
10-Year Treasury Rate	2.35%	2.91%	2.65%	2.34%	1.68%	*1.70%*	*1.70%*	*1.75%*
10-Year-Fed Funds Spread	2.22%	1.08%	0.25%	-0.06%	*-0.22%*	*0.05%*	*0.05%*	*0.60%*

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

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CUNA Economic Forecast

- **Economic growth:** Expect relatively weak GDP growth with the economy expanding at a 2.1% pace in 2019. This represents a slowdown from 2.9% growth in 2018. With more trade policy uncertainty and weaker growth globally than previously expected, our 2020 forecast calls for a sharper slowdown in growth to 1.5% from 1.8% in our previous forecast.
- **Inflation:** Weak overall growth should help to keep inflation in check over the forecast horizon despite the strong labor market and decent wage gains. Uncertainty and increasing volatility are expected to give consumers pause and their spending and borrowing behaviors will reflect those concerns.
- **Unemployment:** Labor markets should remain strong through 2020, though lower consumer confidence, decreased business investment and slower overall growth will combine to nudge the unemployment rate up modestly by the end of 2020.
- **Fed Funds Rate:** The Federal Reserve has been decreasing the fed funds rates in order to sustain economic expansion and to cushion against trade policy uncertainty and slower global growth. Expect this pattern to continue with one additional rate cut this year, resulting in a fed funds target range of between 1.50% to 1.75% and two rate cuts in 2020, resulting in fed funds target range of between 1.00% to 1.25% by the end of 2020.
- **10-Year Treasury:** A lower Treasury rate outlook seems reasonable given heightened investor concerns about future economic growth, low inflation, trade policy uncertainty and negative interest rates in Europe and Japan. Expect Treasury yields to remain relatively low and constant in 2020 as inflation stays muted and economic growth tapers.

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CUNA Credit Union Forecast

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	5 Yr Avg	2018	2019:1	2019:2	*2019:3*	*2019:4*	*2019*	*2020*
Growth rates:								
Savings growth	6.0%	5.2%	4.5%	0.6%	*1.3%*	*0.6%*	*7.0%*	*8.0%*
Loan growth	10.1%	8.9%	0.6%	1.8%	*2.5%*	*1.6%*	*6.5%*	*5.5%*
Asset growth	6.5%	5.4%	3.6%	0.9%	*0.5%*	*1.6%*	*6.7%*	*7.5%*
Membership growth	3.8%	4.4%	1.1%	1.0%	*0.7%*	*0.2%*	*3.0%*	*2.5%*
Liquidity:								
Loan-to-share ratio**	80.2%	85.8%	82.3%	83.3%	*84.8%*	*85.6%*	*85.6%*	*83.8%*
Asset quality:								
Delinquency rate**	0.80%	0.71%	0.63%	0.63%	*0.65%*	*0.70%*	*0.70%*	*0.80%*
Net charge-off rate*	0.54%	0.57%	0.57%	0.54%	*0.60%*	*0.60%*	*0.58%*	*0.65%*
Earnings:								
Return on average assets (ROA)*	0.80%	0.91%	0.95%	0.97%	*0.90%*	*0.85%*	*0.92%*	*0.75%*
Capital adequacy:								
Net worth ratio**	11.0%	11.3%	11.1%	11.3%	*11.5%*	*11.5%*	*11.4%*	*11.4%*

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

CUNA Credit Union Forecast

- **Loan growth:** Slower economic growth, more uncertainty and more consumer caution will slow credit union loan growth. Expect a continued downward trend in auto and first mortgage loans, even if unsecured personal loans pick up as consumers face liquidity challenges (or as a result of continued high consumer confidence).
- **Savings Growth:** A slower-growing economy and modestly weaker labor markets should have consumer confidence softening and spending trending down. Members will be much more likely to be building savings balances in anticipation of rainy days. Credit unions have been pricing longer-term certificate accounts fairly aggressively in an attempt to lock in longer-term funding at low rates.
- **Membership Growth:** Membership growth is heavily influenced by auto loan growth, which has recently slowed. Auto loan growth will continue to decrease over the next year and with more paydowns of indirect loans it seems reasonable to expect more culling of dormant accounts (and lower membership growth overall). Still, memberships should continue to increase at a rate that generally exceeds the pace of U.S. population growth.
- **ROA:** ROA has recently been buoyed by mortgage refinancings, gains on mortgage sales into the secondary market, interchange income and a share insurance equity distribution. However, bottom-line results will come under increasing pressure in 2020 as interest rates decrease credit unions net interest income will decline; gains on sale will slow since most members who can refinance will have already done so; and interchange income will be down as we expect that people spend less.

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