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# Banking & Finance

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AN EIGHTH DISTRICT PERSPECTIVE

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## Credit Unions: Growing Quickly But Still Little Known

Over the past five years, credit unions in the seven states composing the Eighth Federal Reserve District have grown almost twice as rapidly as commercial banks and thrift institutions.<sup>1</sup> From 1979 to 1984, total assets at credit unions in the District grew at an annual rate of 11.9 percent compared with average annual increases of 6.5 percent for both banks and thrifts. Despite this rapid growth, and the fact that over 50 million individuals are members of credit unions nationwide, the structure and organization of these institutions are not well-known.

The Federal Credit Union Act of 1934 defines a credit union as a "cooperative association organized in accordance with the provisions of [the Act] for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes." Credit union members have a common bond of association, occupation or residence. Ostensibly, credit unions are not-for-profit financial organizations. Earnings from loans and investments either are returned to the members through dividends on deposits and rebates on loans or are used to augment reserves. Credit union members select other members to serve as unpaid volunteer officers who establish credit union policy. Voting is on the basis of one vote per member.

While their growth has been rapid, most credit unions remain quite small compared with other financial institutions. Over half of the almost 3,000 District credit unions had less than \$1 million in total assets while only one out of more than 3,300 banks were this small at the end of 1984. The accompanying table provides a size comparison of credit unions and commercial banks at both the District and national levels. All District credit unions together held assets worth \$13.2 billion at the end of 1984, which represents only 3.9 percent of District commercial bank assets and 11.1 percent of thrifts' assets. At the

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Distribution of Institutions by Size: 1984

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Total Assets (\$ millions)	UNITED STATES		EIGHTH DISTRICT	
	Banks	Credit Unions	Banks	Credit Unions
Less than \$5	2.1%	79.5%	1.5%	83.9%
\$ 5 to \$ 25	36.0	15.3	34.6	12.9
\$ 25 to \$100	45.0	4.2	48.0	2.7
\$100 to \$500	13.5	.9	14.1	.5
Greater than \$500	3.4	.1	1.8	—
	100.0%	100.0%	100.0%	100.0%

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national level, all credit unions' assets amounted to \$113.2 billion at the end of 1984, less than the assets of either of the two largest commercial banks. The \$113.2 billion represented 4.4 percent of all banks' assets and 9.5 percent of thrifts' assets nationally. Most credit union loan portfolios are concentrated in consumer lending areas such as installment credit and automobile loans. At the end of 1984, credit unions held 14.9 percent and 19.1 percent shares of these two loan categories, respectively. Both of these market shares, however, are down slightly from 16.5 percent and 21.2 percent, respectively, at the end of 1979.

The range of financial services offered by credit unions varies widely, and usually according to credit union size. Some provide only basic savings accounts while others offer credit cards and IRA and KEOGH retirement accounts. Since 1982, credit unions have been authorized to form credit union service organizations that offer such services as discount brokerage and financial planning.

## Regulation and Insurance

Credit unions, like commercial banks, have a dual regulatory system of state and federal

<sup>1</sup>The Eighth District officially includes all of Arkansas and portions of Illinois, Indiana, Kentucky, Mississippi, Missouri and Tennessee. Due to data constraints, this article refers to these seven states in their entirety as the Eighth District.



charters. The first credit union in the U.S. was formed in 1909, and until 1934 all credit unions were chartered and regulated at the state level. In 1934, the Federal Credit Union Act was passed allowing credit unions to be chartered and regulated by federal agencies. In 1970 the National Credit Union Administration (NCUA), an agency of the federal government, was established to consolidate the various federal agencies that previously had been responsible for federal credit unions. All federally chartered credit unions (over 10,700 at the end of 1984) are regulated directly by the NCUA and must be insured by the National Credit Union Share Insurance Fund (NCUSIF), which is a federal institution backed by the government and administered by the NCUA. The NCUSIF guarantees members' deposits (or shares, as they are known in credit unions) up to a maximum of \$100,000.

State-chartered credit unions in Arkansas, Kentucky and Mississippi are required to have federal insurance through the NCUSIF. State laws in Illinois, Indiana, Missouri and Tennessee allow insurance from either the NCUSIF or from private or "cooperative" insurance funds.

Before 1984, the NCUSIF functioned like the FDIC and FSLIC; credit unions were assessed an annual premium of one-twelfth of one percent of insurable deposits. Due to a large number of involuntary liquidations and assisted mergers early in the 1980s, the NCUSIF required insured credit unions to pay double assessments in 1982 and 1983 to rebuild the weakened fund. In 1984 a one-time capital investment of one percent of insurable deposits was made by all insured credit unions. Under the new procedure, the NCUSIF can authorize annual assessments, but none were made in 1985 and none are planned for 1986. The NCUSIF is required to make dividend distributions back to insured credit unions when the value of the fund exceeds 1.3 percent of insurable deposits. In 1985 the NCUSIF made one such distribution.

Credit unions have been required to hold reserves at Federal Reserve Banks against deposit liabilities since the Depository Institutions Deregulation and Monetary Control Act was passed in 1980. Credit unions also have the privilege of using the Federal Reserve as a "lender of last resort." Before coming to the discount window, however, credit unions have a number of alternative sources of funds. The primary source of borrowed funds is a network of corporate credit unions that have regular credit unions as their members and function in a manner similar to that of a correspondent bank. In addition to lending to member credit unions, central credit unions provide services such

as pooled investment programs.

The credit union industry's own "lender of last resort" is the Central Liquidity Facility (CLF), established by Congress in 1979 and administered by the NCUA. To become a member of the CLF, credit unions must subscribe to the capital stock of the CLF to the amount of one-half percent of the credit union's paid-in and unimpaired capital and surplus. The CLF provides members with a source of funds to meet liquidity needs in the same manner that the Federal Reserve's discount window provides this service to commercial banks.

Unlike commercial banks, federally chartered credit unions are not restricted with respect to interstate branching. They are free to expand operations to serve their membership. State-chartered credit unions, however, are not permitted to branch across state lines unless the states involved have reciprocal branching agreements.

## Taxation

Due to their status as cooperative non-profit associations, credit unions are exempt from paying federal taxes on their earnings. With their strong growth and diversification into financial products formerly offered only by banks and thrifts, some analysts suggest credit unions should be taxed to eliminate the competitive advantage offered by tax-exempt status. The industry, however, has argued that taxation would jeopardize the service orientation of credit unions and reduce their safety. A proposal to repeal the tax-exempt status originally was included in the Administration's tax reform package as well as in a number of the other tax programs. The tax reforms passed by the House last fall and currently pending in the Senate, however, made no mention of credit unions. The Senate could alter the bill to include taxation of credit unions.

## Credit Union Performance

Despite the rapid asset growth of credit unions over the past five years, the ratio of total capital (consisting of reserves and retained earnings) to assets has declined only slightly in both the nation and the District. Capital in federally insured institutions fell from 6.03 percent in 1980 to 5.85 percent of assets in 1984 for the nation and from 6.46 percent to 6.15 percent in the District. Loan performance over the same period, however, has improved as loans delinquent more than 60 days have fallen from 3.32 percent to 2.02 percent of total loans in the U.S. and from 3.93 percent to 2.41 percent in the District.

—Kenneth C. Carraro

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## EIGHTH DISTRICT BANKING DATA

LARGE WEEKLY REPORTING BANKS<sup>1</sup>

	Level IV/1985 (\$ millions)	Rates of Change			
		Current Quarter	Current Year	Same Periods Previous Year	
		III/1985- IV/1985	IV/1984- IV/1985	III/1984- IV/1984	IV/1983- IV/1984
<b>Selected Assets &amp; Liabilities</b>					
Total Loans & Leases	\$14,839	10.3%	10.7%	12.1%	19.7%
Commercial Loans	5,157	3.6	0.8	16.7	10.5
Consumer Loans	3,412	25.5	26.8	18.0	14.2
Real Estate Loans	3,076	6.0	8.1	5.9	15.5
Loans to Financial Institutions	900	-27.4	-16.9	-19.5	22.2
All Other Loans	2,294	33.0	37.7	25.5	94.9
Total Securities	3,420	-1.4	5.3	-10.6	NA
U.S. Treasury & Agency Securities	1,897	-20.4	-0.8	-22.9	NA
Other Securities	1,522	30.9	13.9	12.1	NA
Total Deposits	17,683	10.8	4.2	12.1	10.5
Non-Transaction Balances	10,835	4.2	2.3	15.2	NA
MMDAs	2,324	19.0	16.0	24.1	7.9
\$100,000 CDs	3,604	11.7	-3.2	8.8	23.9
Demand Deposits	5,328	29.5	4.7	4.6	0.8
Other Transaction Balances <sup>2</sup>	1,522	26.8	18.0	17.5	NA

SMALL WEEKLY REPORTING BANKS<sup>3</sup>

	Level IV/1985 (\$ millions)	Rates of Change		
		Current Quarter	Current Year	Previous Year
		III/1985- IV/1985	IV/1984- IV/1985	III/1984- IV/1984
<b>Selected Assets &amp; Liabilities</b>				
Total Loans & Leases	\$4,589	6.2%	7.0%	11.9%
Commercial Loans	1,420	0.8	0.5	1.6
Consumer Loans	930	13.0	6.5	25.4
Real Estate Loans	1,834	6.7	9.5	15.4
All Other Loans	405	8.3	23.5	8.6
U.S. Treasury & Agency Securities	1,684	-0.9	4.0	-8.9
Other Securities	687	10.1	3.9	4.6
Total Deposits	7,325	10.9	10.5	5.8

<sup>1</sup> A sample of commercial banks with total assets greater than \$750 million. Historical data have been revised to incorporate adjustment factors that offset the cumulative effects of mergers and other changes involving weekly reporting banks during 1984. All data are not seasonally adjusted. Rates of change are compounded annual rates.

<sup>2</sup> Includes NOW, Super NOW, ATS and accounts permitting telephone or pre-authorized transfers.

<sup>3</sup> A sample of commercial banks with total assets less than \$300 million as of January 1984.

## EIGHTH DISTRICT BANKING DATA

### Bank Performance Ratios

<u>RATIOS</u>	<u>III/1985</u>	<u>III/1984</u>	<u>III/1983</u>
<b>Loans to Deposits</b>			
Large Banks <sup>4</sup>	77.37%	77.82%	69.64%
Small Banks <sup>5</sup>	60.42	61.43	58.06
<b>Loan Loss Reserves to Total Loans</b>			
Large Banks	1.44	1.36	1.61
Small Banks	1.19	1.08	1.03
<b>Delinquent Loans to Total Loans</b>			
Large Banks	3.90	4.45	6.76
Small Banks	4.93	4.61	4.56
<b>Net Loan Losses to Total Loans</b>			
Large Banks	0.49	0.30	0.29
Small Banks	0.54	0.36	0.40

### EIGHTH DISTRICT INTEREST RATES<sup>6</sup>

	<u>December 1985</u>	<u>November 1985</u>	<u>October 1985</u>	<u>Year Ago December 1984</u>
Super NOW	6.02%	6.07%	6.08%	6.86%
MMDAs	6.86	6.91	6.93	7.75
Time CDS				
92 — 182 days	7.31	7.44	7.53	8.49
1 — 2½ years	8.15	8.36	8.39	9.27
2½ years and over	8.52	8.75	8.87	9.50

<sup>4</sup> All Eighth District banks with total assets greater than \$750 million. Ratios are derived from Call Reports.

<sup>5</sup> All Eighth District banks with total assets less than \$300 million.

<sup>6</sup> Average interest rates paid on new deposits by a sample of District commercial banks.