



# Managing Excess Liquidity Investment Trends & Insights For Credit Unions



Jason Haley, Chief Investment Officer, ALM First Financial Advisors

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## Today's Agenda

- ALM First Market Update
- Credit Union Investment Trends
- TCU Portfolios Progress Report



# About Trust for Credit Unions

- Institutional investment options, **created specifically for credit unions**
- **ALM First** serves as *investment advisor*
- **Callahan Financial Services** serves as *distributor*
- Hundreds of credit union investors in our **30+ year history**

## TRUST FOR CREDIT UNIONS

It's our mission to support credit union investment strategies through a professionally managed family of mutual funds that respond to the needs of the credit union industry.

Our mutual fund options keep credit unions always invested, are professionally managed, and are delivered with great client service and the cooperative values of credit unions always in mind.

Since 1987, TCU has helped credit unions invest excess member deposits, focusing on adding maximum value through collaboration.

We value what you value. Our core values, which have been derived from long-standing client relationships, say it all:

- Partnership and Collaboration
- Knowledge and Resource Management
- Access to Information
- Loyal Partners
- Strategic Resource

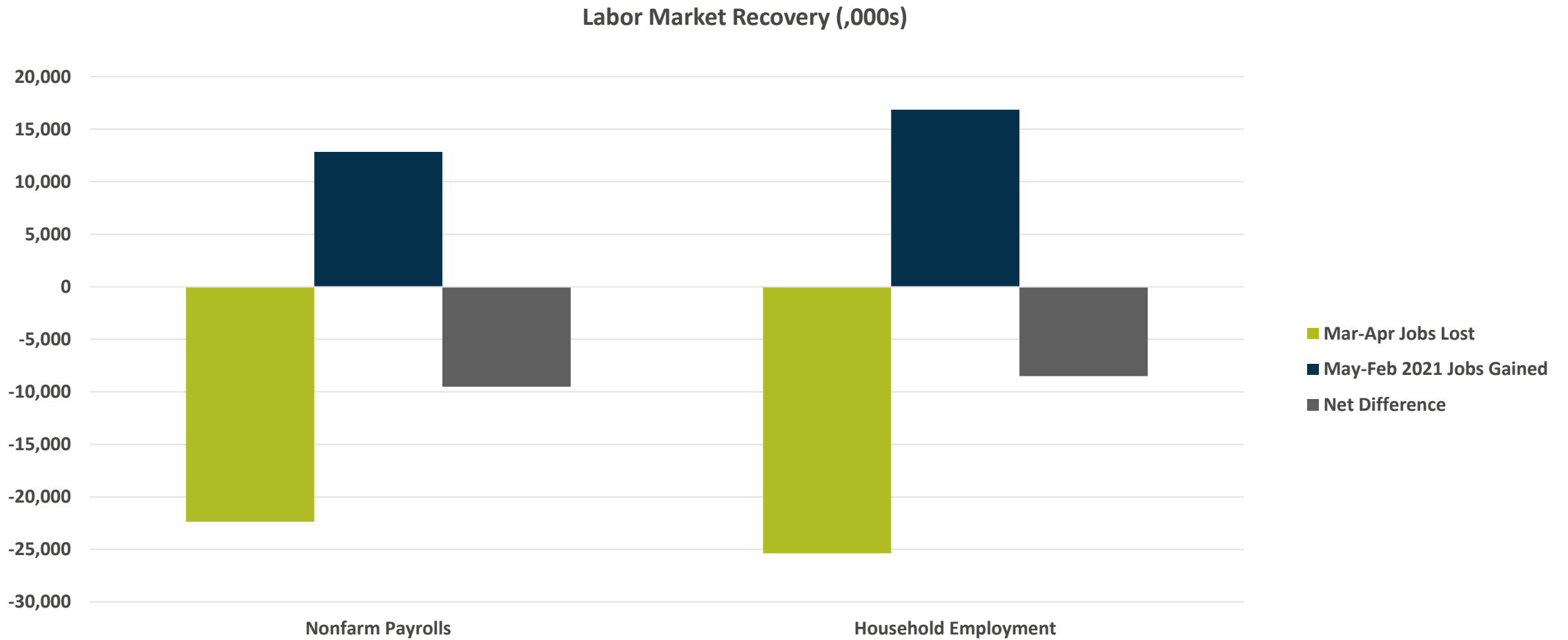


# ALM First Market Update

Jason Haley  
Chief Investment Officer  
ALM First Financial Advisors

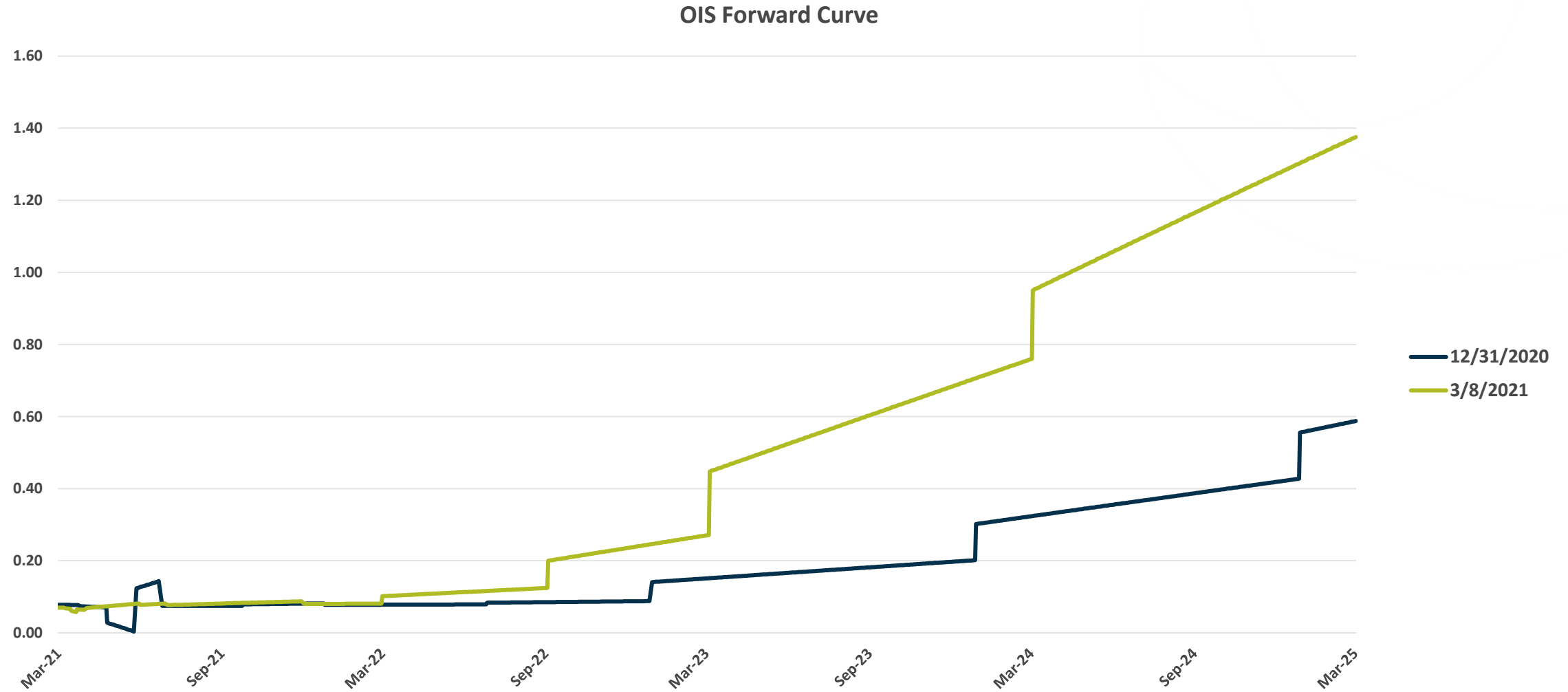
- **The reflation/inflation trade dominated financial markets in February**
  - Treasury curve more than 60 bps steeper YTD on speculation that higher inflation is looming
  - Covid trends have significantly improved in recent weeks
    - New cases and hospitalizations down sharply from late 2020/early 2021 levels
    - In a WSJ Op-ed, Johns Hopkins professor Dr. Marty Makary suggested the U.S. could reach herd immunity by April
  - Recent economic data have beat expectations
    - January retail sales significantly outperformed expectations (Control group +6% m/m vs. +1% expected)
    - February job growth better than expected, but payrolls remain 9mm below pre-Covid levels
  - Congress still pressing forward with ~\$1.9 trillion of fresh Covid relief
    - Larger infrastructure spending package being discussed as well as a potential late-2021 event
- **Fed Chair Powell remains dismissive of inflation risks**
  - Before the Senate two weeks ago, Powell said the economy is still “a long way” from employment and inflation goals
  - He has attributed the recent rise in long-end yields to an improved economic outlook rather than inflation concerns
  - Also reiterated belief that any 2021 inflation will be transitory related to economy reopening

# Still More Jobs To Recover..



Source: BLS, Bloomberg

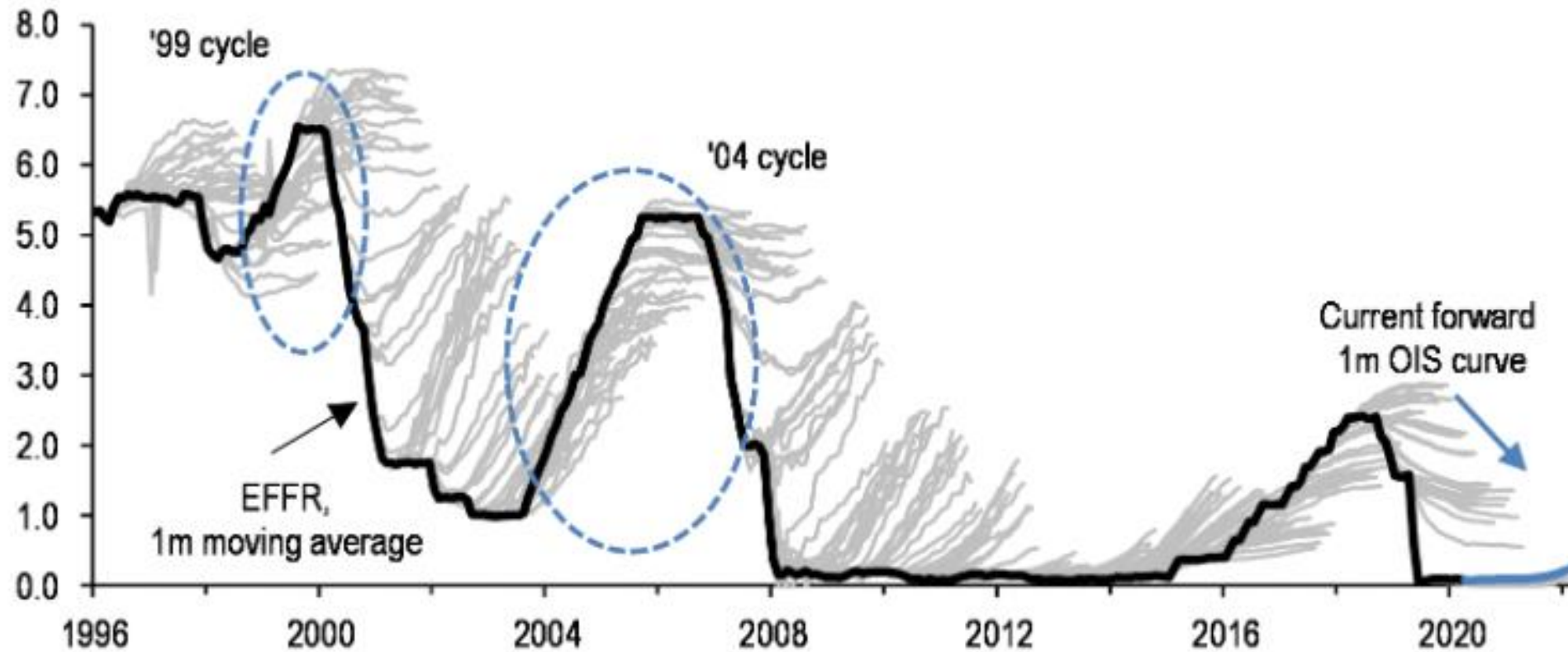
# Market Pricing for Forward Fed Funds



Source: Bloomberg

# Market Tends To Prematurely Price Fed Action

EFFR vs forward 1m OIS (%)





# Market Themes

- **Treasury curve is sharply steeper in 2021**
  - Long-end yields at highest levels in over a year (before 150 bps of Fed rate cuts)
  - Market pricing for first fed hike moved up to early 2023 (historically premature in pricing Fed action)
- **Fixed income performance has been mixed in 2021**
  - Total returns are negative for most sectors given the increase in rates
  - Corporates have outperformed Treasuries, but February MBS performance was expectedly poor amid the curve steepening (cashflow extension)
    - 15yr MBS outperformed 30yr MBS
  - Reinvestment rates are higher looking forward
- **Despite recent steepening, the Fed still casts a major shadow over the bond market**
  - A flood of liquidity chasing fewer assets
  - New round of fiscal stimulus coming soon
  - As such, spreads remain at historically tight levels
  - Steeper yield curve is a positive for credit union NIM and deposit franchise values

Treasury Curve			
Tenor	3/8/2021 (%)	12/31/2020 (%)	Change (bps)
1-Month	0.03	0.03	0.00
3-Month	0.03	0.06	-0.03
6-Month	0.05	0.08	-0.03
1-Year	0.08	0.10	-0.03
2-Year	0.16	0.12	0.04
5-Year	0.85	0.36	0.49
10-Year	1.59	0.91	0.68
20-Year	2.20	1.44	0.76
30-Year	2.32	1.65	0.67
Curves			
3mo-10yr	1.56	0.86	0.70
2yr-5yr	0.69	0.24	0.45
2yr-10yr	1.43	0.79	0.64
2yr-30yr	2.15	1.52	0.63
5yr-10yr	0.74	0.55	0.19

Source: Bloomberg



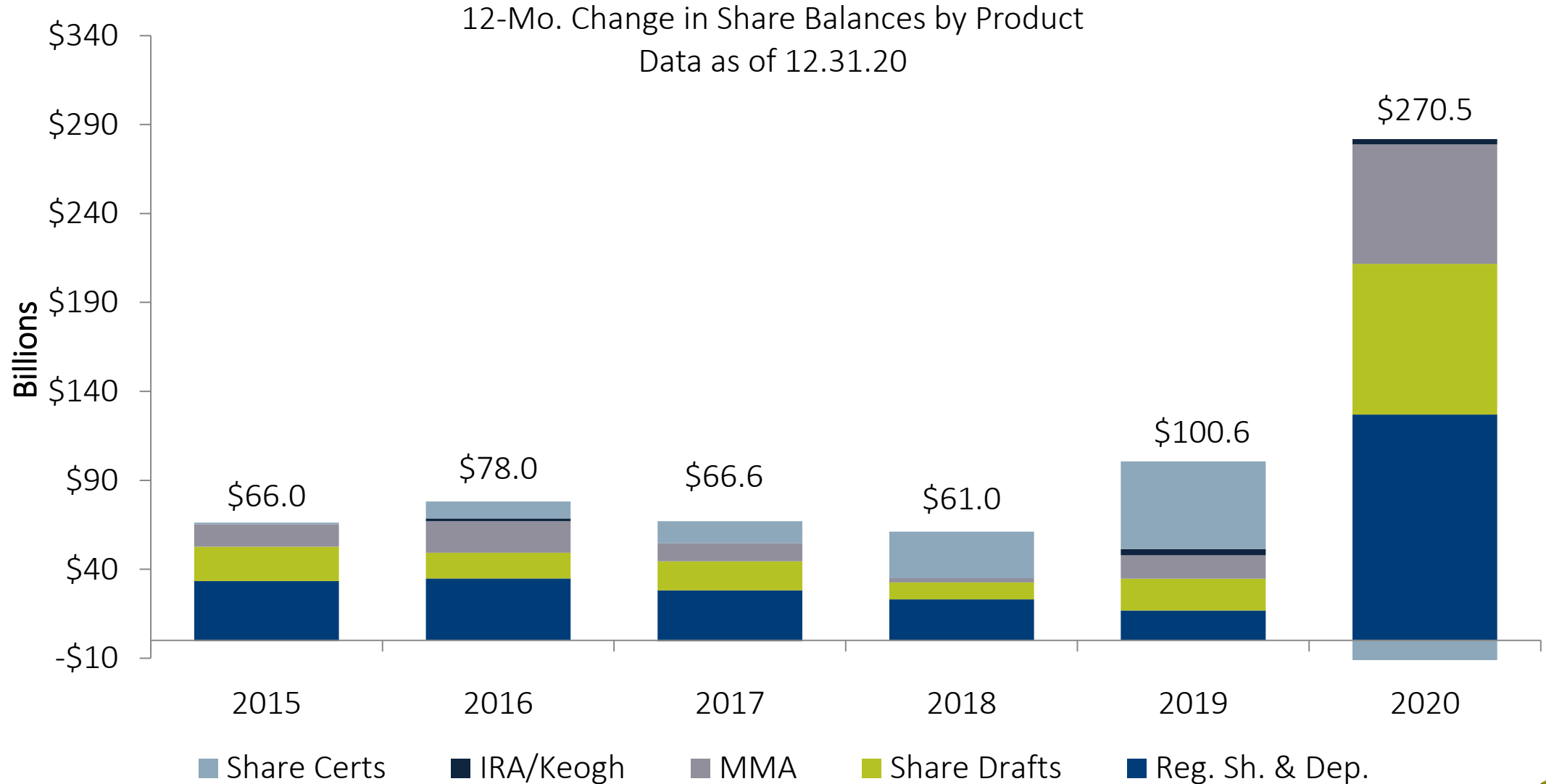
# Credit Union Investment Trends

Sam Taft  
AVP, Business Development  
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## Headline Numbers at year-end 2020

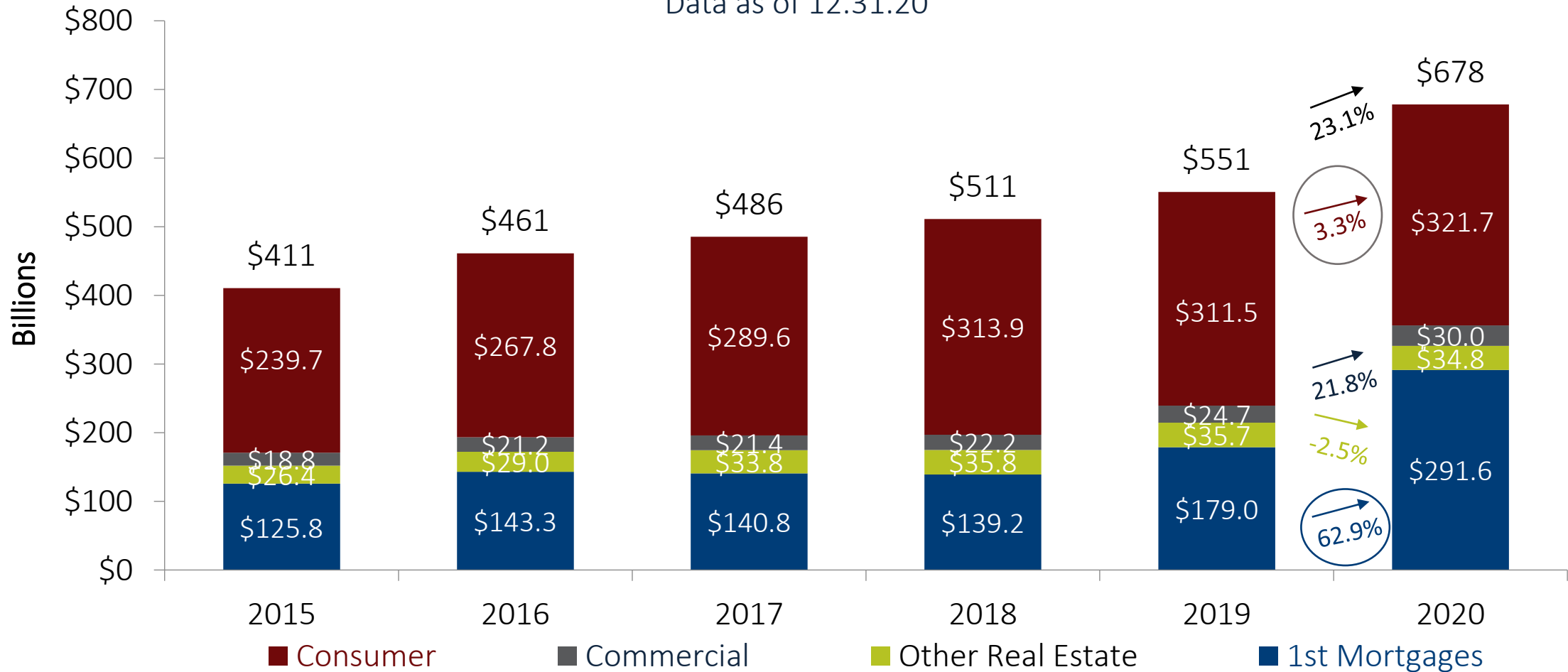
	12/31/2020	12-mo. Growth 2020	12-mo. Growth 2019
Assets	\$1,865.4B	17.7%	7.7%
Loans	\$1,175.0B	4.9%	6.1%
Shares	\$1,605.9B	20.3%	8.1%
Investments	\$601.8B	54.6%	11.1%
Capital	\$206.5B	9.8%	10.5%
Members	125.7M	3.3%	3.6%

# Core deposits drive the saving surge, growing nearly 6 times 2019's results

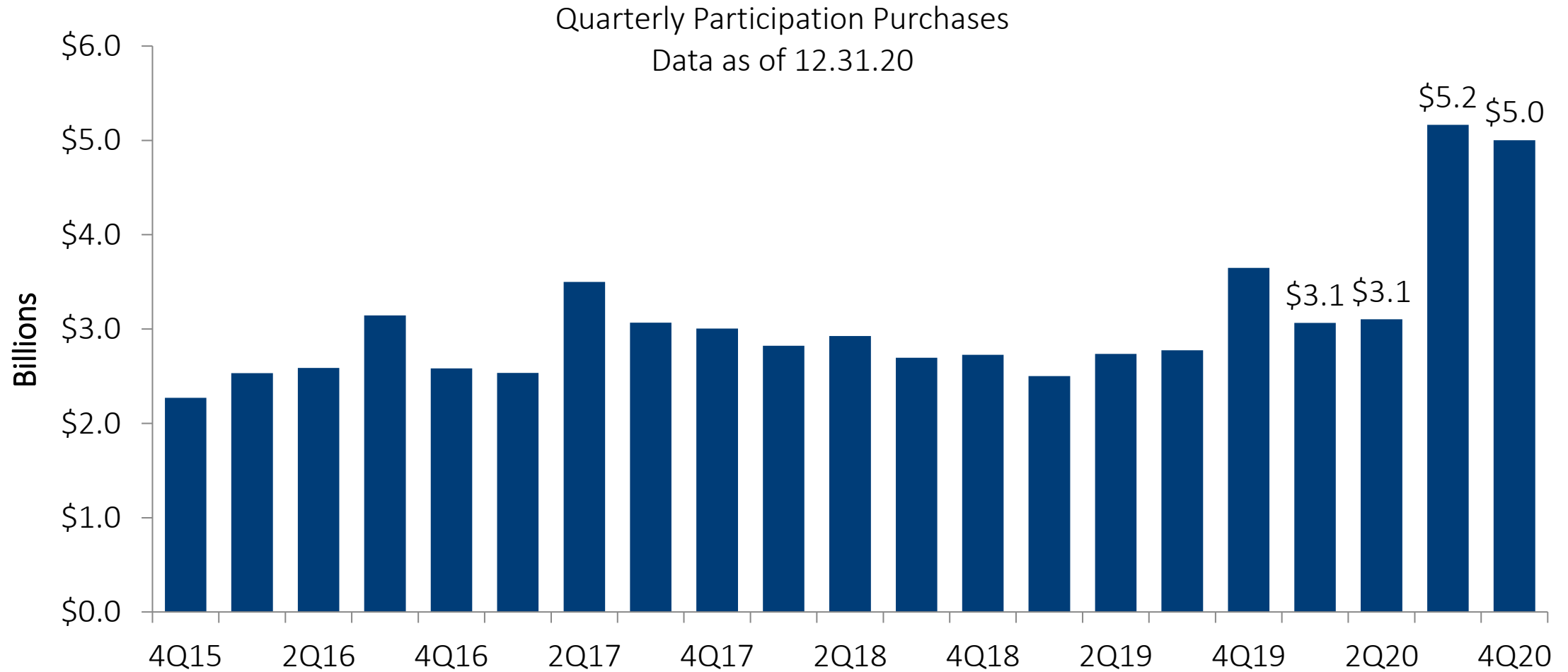


# Mortgage lending drives origination growth, though consumer lending remains credit unions' primary business

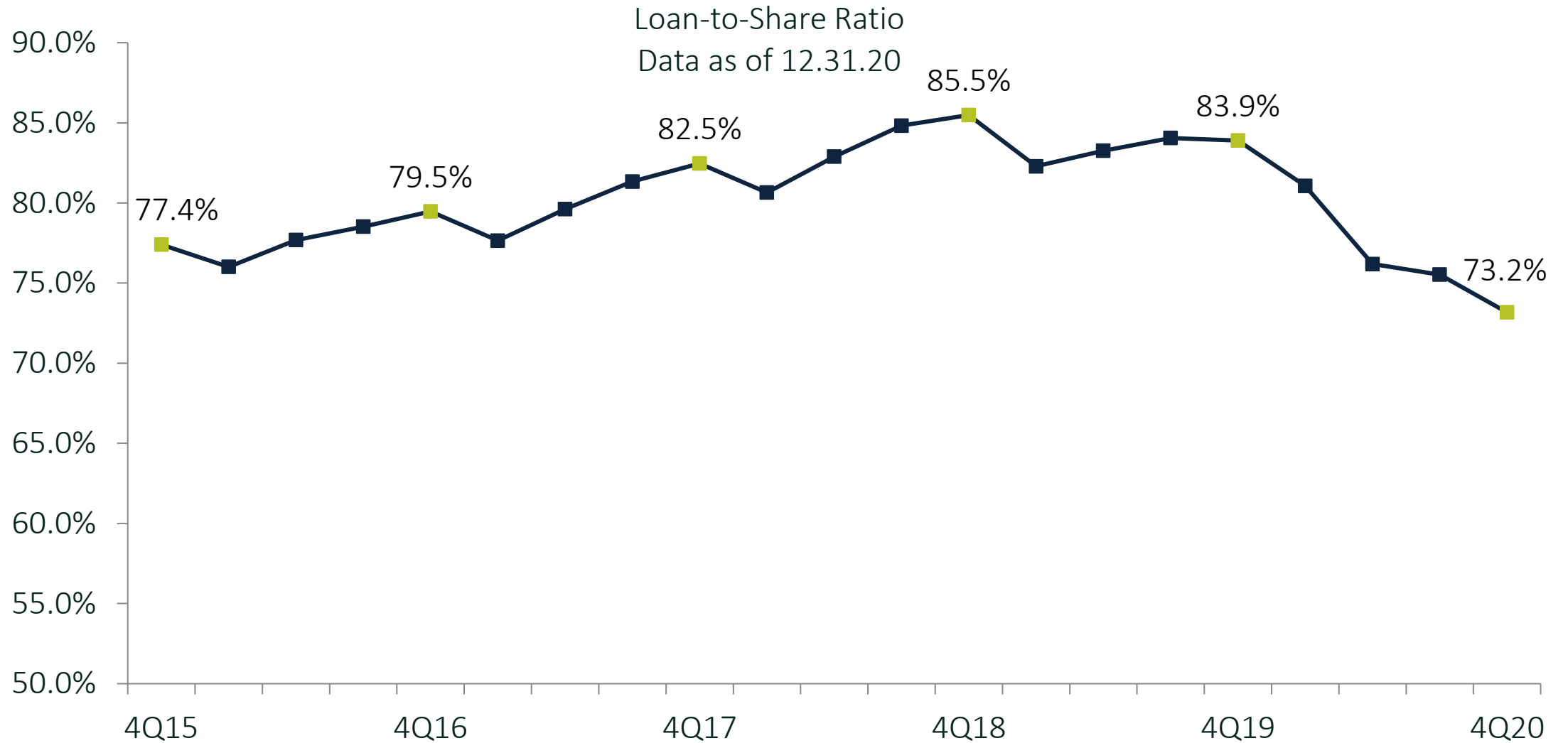
YTD Loan Originations  
Data as of 12.31.20



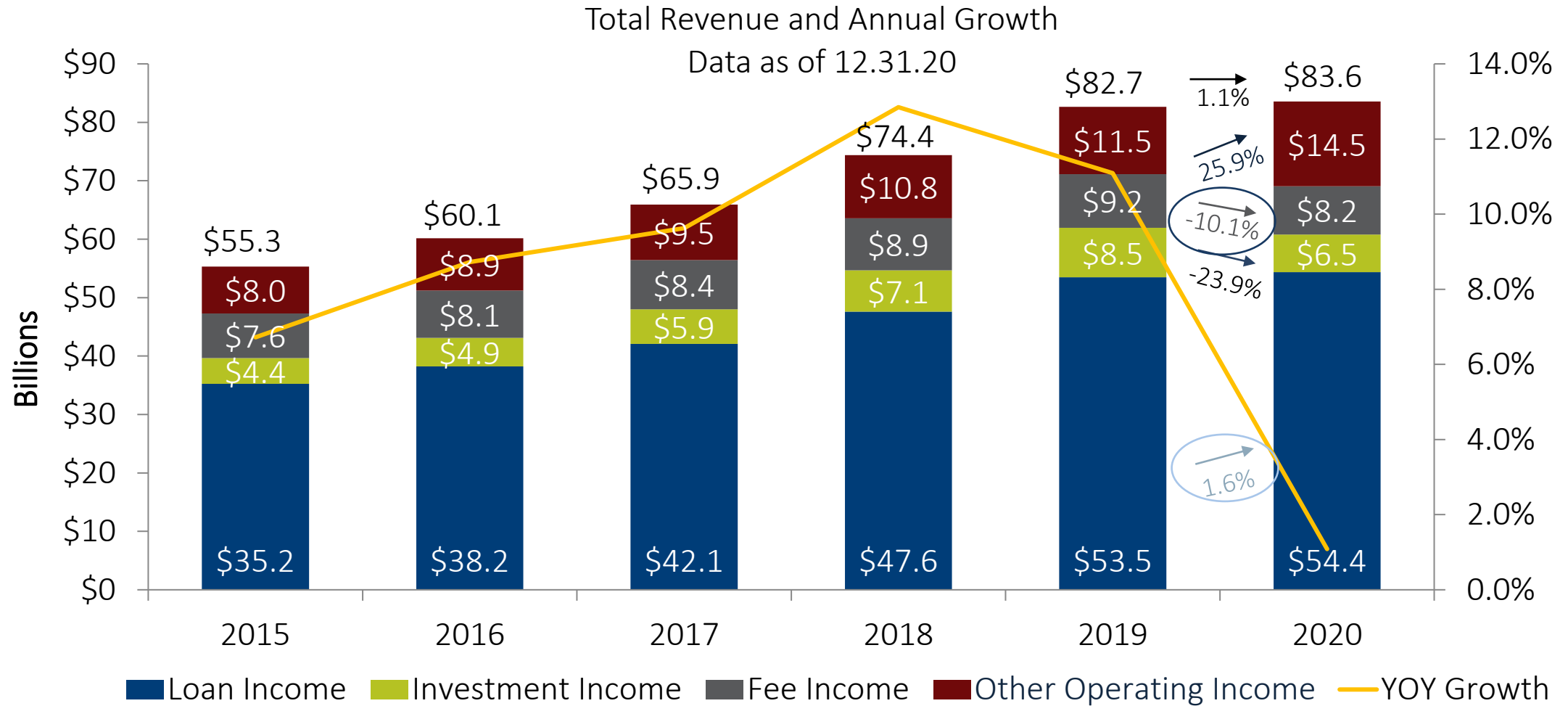
# Credit unions purchase nearly \$16.4B in participation loans in 2020 to combat margin compression



# Rapid deposit growth quickly pushed the loan-to-share ratio lower in 2020

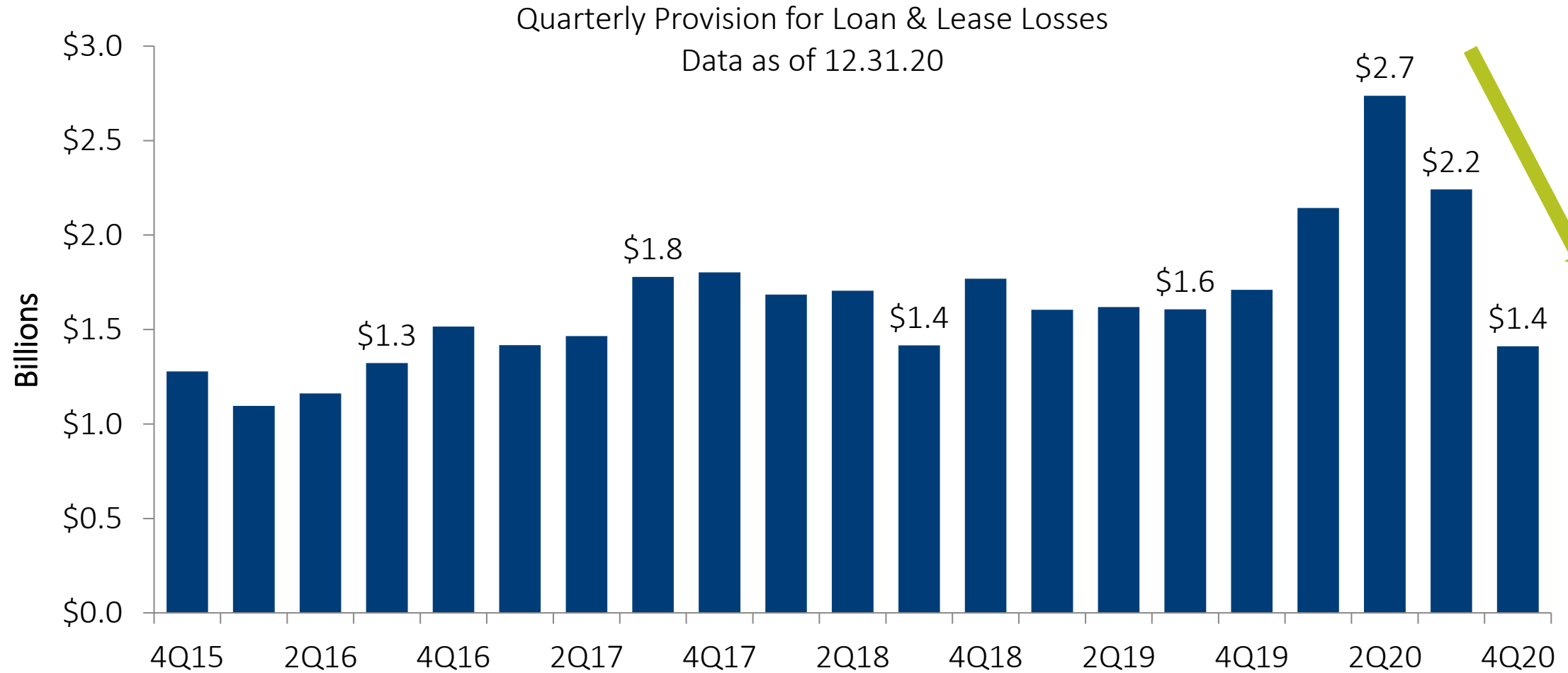


# Other operating income, including gains from mortgage sales and interchange income, generates marginal revenue growth

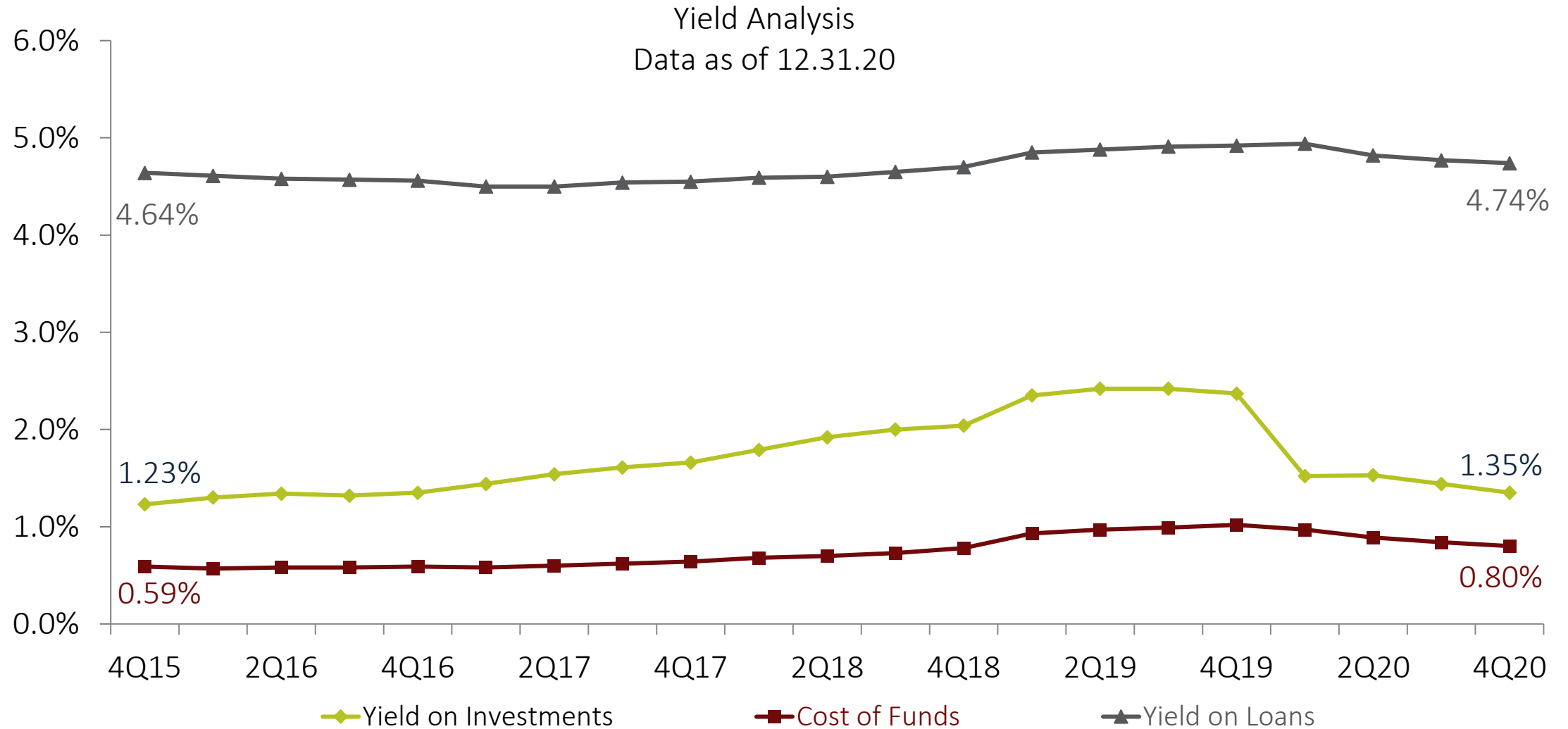




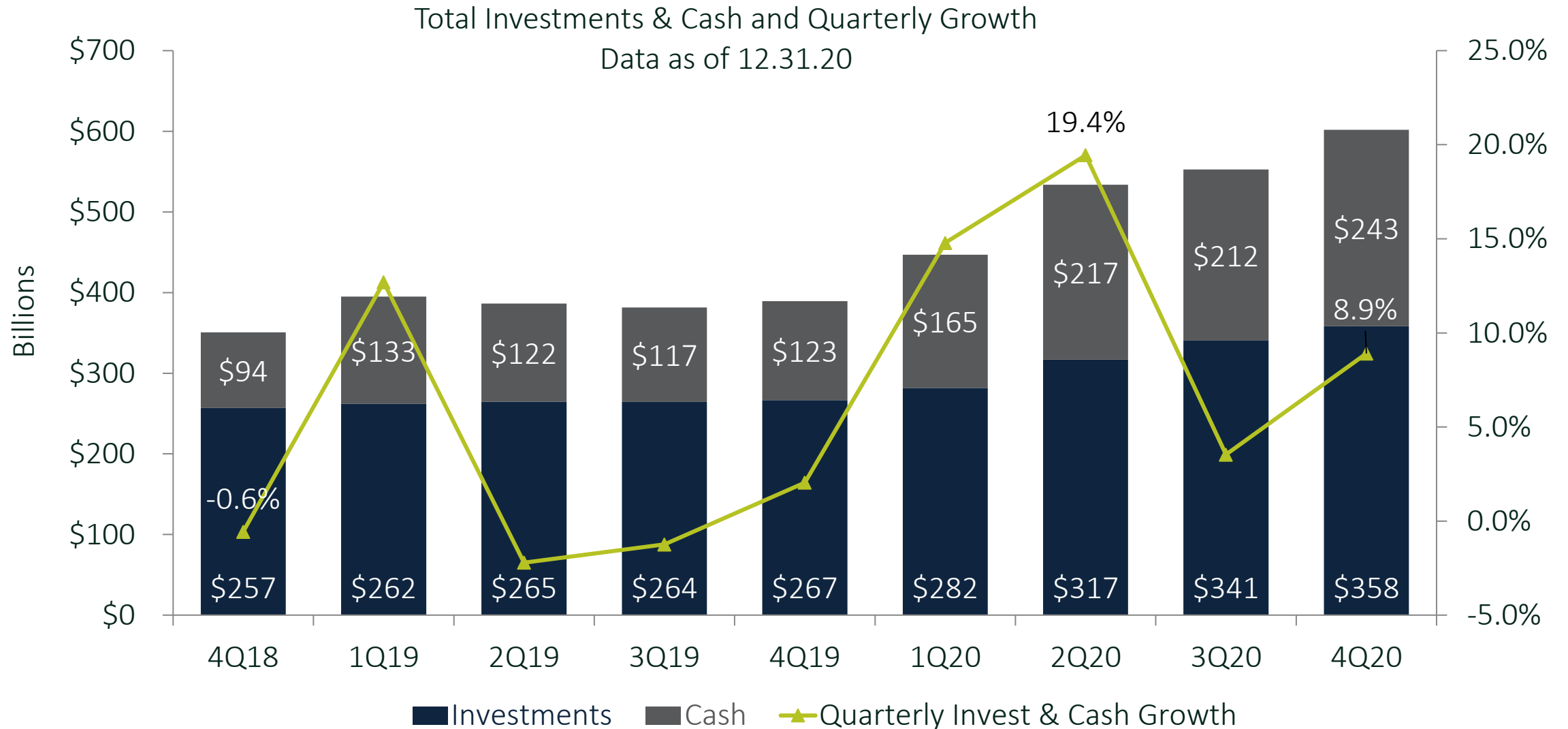
# Credit unions post \$8.5 billion in provision for loan losses in 2020, the highest ever



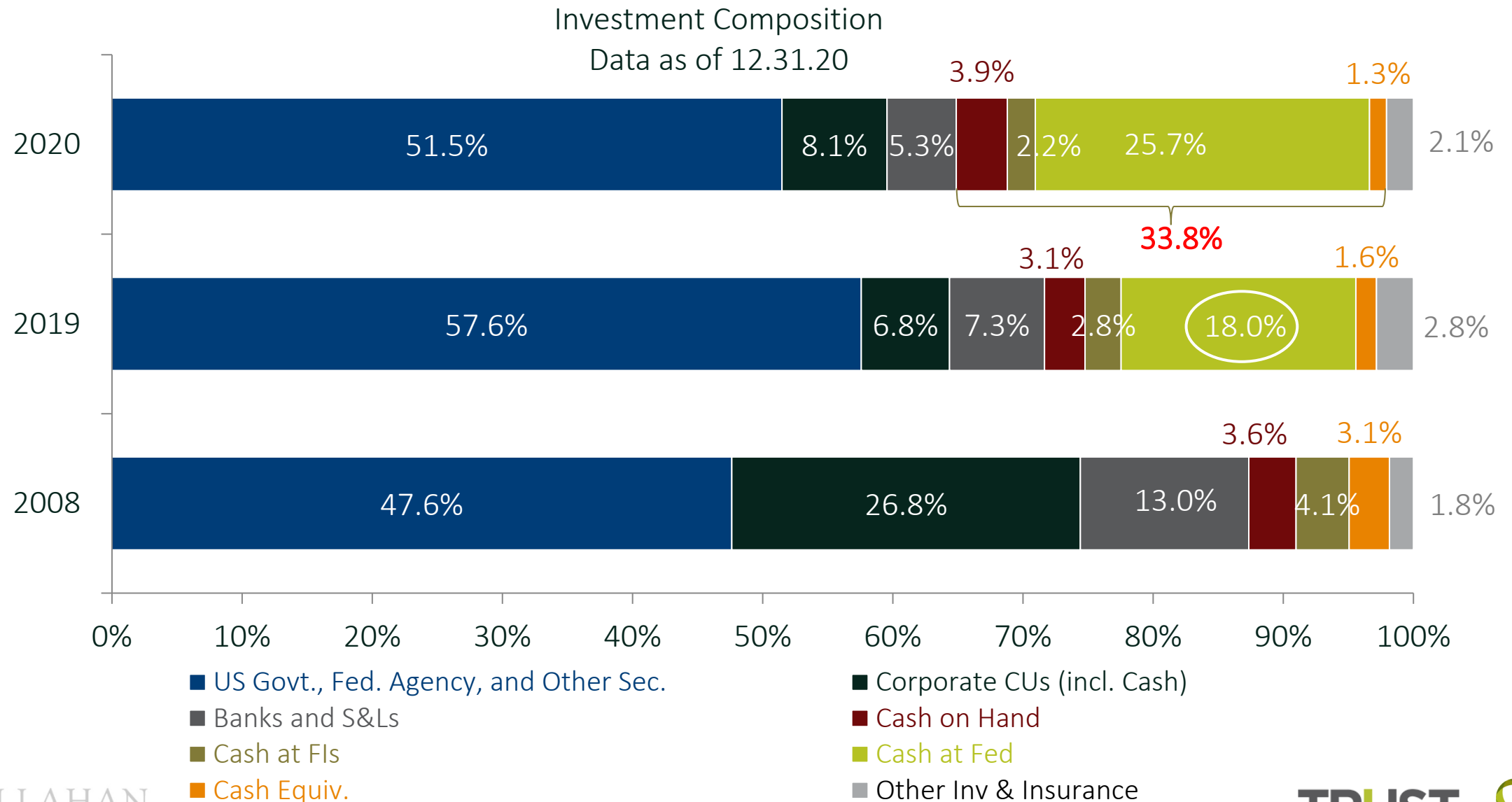
# Returns decline across the balance sheet following spring rate cuts



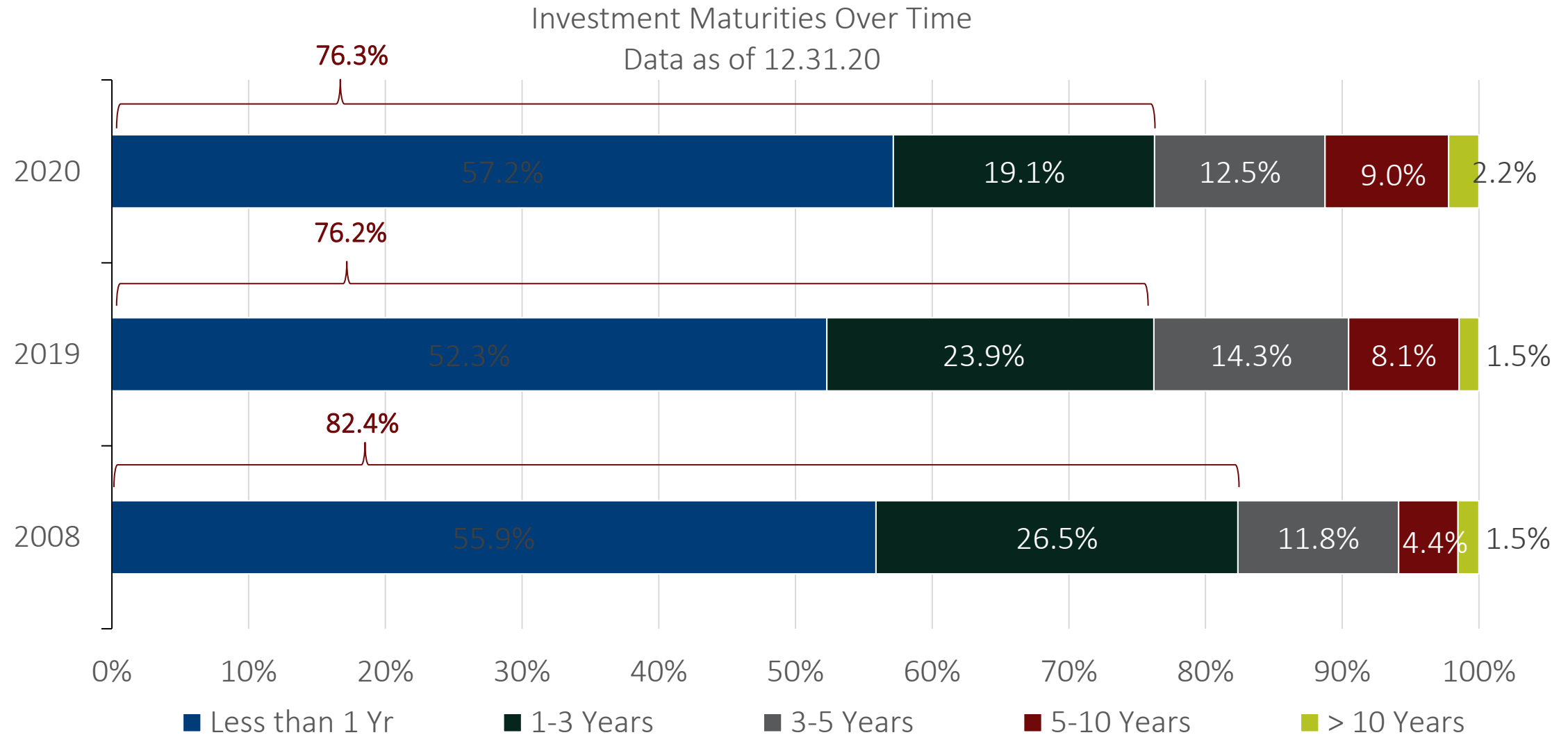
# Cash rises 15.0% in final three months +98% in 2020



# Overnight cash balances rise 103% annually, Agency investments up 38.2%



# Portfolios lengthen from 3Q20 – weighted average life increases to 1.86 years





# TCU Portfolios Progress Report

Jason Haley  
Chief Investment Officer  
ALM First Financial Advisors

- **TCU Ultra Short Duration Portfolio**

- \$2.61 billion total assets (as of 3/8/21)
- 3mo Treasury Index benchmark
- Strategy aims to minimize interest-rate risk while maintaining a reasonable yield spread over IOER
- ***Not a money market fund (and not intended to be)***
- As of 3/8/21, 0.31% 30-day yield for Investor shares and 0.34% for TCU shares

- **TCU Short Duration Portfolio**

- \$1.23 billion total assets (as of 3/8/20)
- 2yr Treasury Index benchmark
- Portfolio generally represents ALM First's best ideas for a core bond portfolio of 703-permissible securities
- Portfolio is in 15<sup>th</sup> percentile of all funds in its Morningstar category for a 3yr timeframe

# TCU Ultra Short Duration Portfolio

TCU Ultra Short Duration Portfolio				
	Current Allocation	Ex- Ante Analytics		
		Eff. Dur	Sprd. Dur	OAS
ARM	0%	0.89%	3.95%	92
Agency Floater	0%	0.38%	1.66%	80
Bank Note Float	4%	0.11%	1.00%	66
CMO Fixed	0%	2.23%	3.27%	42
CMO/ACMBS Floaters	66%	0.30%	4.07%	19
MBS Fixed	0%	2.44%	3.32%	87
Repo	30%	0.03%	0.04%	38
	100%	0.22%	2.75%	27

Yield Summary			
	TCUUX <sup>2</sup>	Benchmark <sup>3</sup>	Excess
1-Day Yield	0.42%	0.04%	0.38%
30-Day Yield	0.33%	N/A	N/A

Total Return Summary <sup>1</sup>			
	TCUUX <sup>2</sup>	Benchmark <sup>3</sup>	Excess
3 month	0.09%	0.03%	0.06%
YTD	0.06%	0.02%	0.04%
12 month	1.14%	0.40%	0.74%
Avg Annual <sup>4</sup>	1.55%	1.48%	0.07%

<sup>1</sup> As of 2/28/2021

<sup>2</sup> Yields for TCUUX are after expenses (SEC yield)

<sup>3</sup> Prior to 1/1/2019, benchmark was effectively a 9-month Treasury bill index; current benchmark is 3-month Treasury bill index

<sup>4</sup> Since 4/30/2017 (when ALM First became portfolio manager)



# TCU Short Duration Portfolio

TCU Short Duration Portfolio Summary <sup>1</sup>				
	Current	Ex-Ante Analytics		
	Allocation	Eff. Dur	Sprd. Dur	OAS
ARM	1%	0.99%	3.82%	86
Bank Note Fixed	4%	1.35%	1.45%	26
Bank Note Float	3%	0.10%	1.06%	119
CMBS Fixed	21%	4.54%	4.46%	46
CMO Fixed	3%	0.35%	4.87%	109
CMO/ACMBS Floaters	28%	0.64%	3.35%	21
MBS Fixed	30%	2.79%	3.89%	38
Repo	9%	0.00%	0.00%	3
Muni	1%	4.83%	4.88%	43
	100%	2.07%	3.36%	36

Yield Summary			
	TCUDX <sup>2</sup>	Benchmark <sup>3</sup>	Excess
1-day	0.69%	0.15%	0.54%
30-day	0.70%	N/A	N/A

Total Return Summary <sup>1</sup>			
	TCUDX <sup>2</sup>	Benchmark <sup>3</sup>	Excess
3 month	-0.62%	0.04%	-0.66%
YTD	-0.70%	-0.03%	-0.67%
12 month	1.50%	1.51%	-0.01%
Avg Annual <sup>4</sup>	2.42%	2.03%	0.39%

<sup>1</sup> As of 2/28/2021

<sup>2</sup> Yields for TCUDX are after expenses (SEC yield)

<sup>3</sup> Benchmark is 2-year Treasury index

<sup>4</sup> Since 4/30/2017 (when ALM First became portfolio manager)

# Closing Thoughts

- **February curve steepening was sharp and sudden**
  - Ultra-short portfolio has minimal sensitivity to rate changes
  - In order to generate reasonable long-run returns, the short duration portfolio will maintain a diversified mix of 703-permissible assets and actively manage non-rate related risks
- **Fund balances, liquidity, etc.**
  - TCU balances continue to grow amid flood of liquidity from monetary and fiscal stimulus
    - 14 new investors and +\$800M since Jan. 1
  - Portfolios are well positioned from a liquidity management perspective to manage volatile inflows/outflows

# Questions & Discussion

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