February 2021

NCUA's supervisory stress test (SST) consists of baseline and severely adverse scenarios, which regulation requires NCUA to provide by 28 February each year. As in past SST exercises, the NCUA's 2021 SST scenarios follow the domestic scenarios published by the Federal Reserve Board of Governors (FRB) for the CCAR and DFAST exercises.

The near-term portion of the baseline scenario is similar to the January 2021 consensus projections from *Blue Chip Economic Indicators* and *Blue Chip Financial Forecasts*. The scenario's long-range forecast is comparable to the October 2020 *Blue Chip* releases. The severely adverse scenario describes a hypothetical set of conditions designed to assess credit unions' resilience under adverse conditions. These scenarios follow the FRB's Policy Statement on the Scenario Design Framework for Stress Testing and do not represent forecasts of the NCUA or the FRB.[1]

A summary of each scenario follows:

<u>Baseline Scenario</u> - The baseline scenario is an economic expansion over the 13-quarter scenario:

- Real GDP increases to 4.8 percent in 2021 3Q and slowly tapers to 2.2 percent by 2024 Q1;
- Unemployment begins the testing horizon at 6.6 percent and gradually decreases to 4.6 percent at the end of the scenario;
- CPI inflation stays in a narrow range throughout the horizon. Inflation begins at 2.1 percent and remains between 1.8 percent and 2.2 percent throughout the scenario;
- Short-term Treasury rates start at 0.1 percent and increase to 0.8 percent in 2024 Q1;
- 10-year Treasury securities rise from 1.0 percent to 1.9 percent over the 13-quarter horizon;
- Prime rates move in line with short-term Treasury rates. Mortgage rates and corporate bond yields rise in line with long-term Treasury rates;
- Equity prices rise between 3.0% and 3.5% each year, and equity volatility slowly decreases over the testing horizon;
- Nominal housing prices rise about 3.5 percent in 2021, incrementally increasing each year to 4.0 percent at the beginning of 2024. Commercial real estate prices initially fall through 2021, and then rise for the test of the scenario.

[1] 12 CFR 252 Appendix A

Severely Adverse Scenario – The severely adverse scenario represents a severe global recession with considerable stress on commercial real estate and corporate debt.

- Real GDP begins falling in 2021 Q1 and bottoms out in the third quarter of 2022;
- Unemployment immediately increases to 7.8 percent at the start of the scenario and climbs to 10.8 percent in 2022 Q3. Unemployment gradually decreases through the recession to 7.4 percent at the end of the test horizon;
- Inflation follows a recessionary track and falls to 1.0 percent in 2021 Q3 then slowly increases to 2.2 percent in 2024 Q1;
- Short-term Treasury remain at 0.01 percent for the entire scenario;
- The 10-year Treasury rate immediately falls to 0.3 percent and increases to 1.5 percent in 2024 Q1;
- Investment-grade spreads and residential mortgage spreads widen during the first five quarters and then narrow through the rest of the testing period;
- The House Price and Commercial Real Estate Price indices fall sharply through most of the scenario and modestly increase from the low by the end of the horizon;
- Equity prices fall by 55 percent through the first three quarters and then increase through the rest of the scenario.