Normal Operating Level (NOL)

NOL is the *desired equity level* of the SIF.

- **Under FCU Act, NOL:**
  - Can be set from 1.20 to 1.50 percent (12 U.S.C. 1782(h)(4))
  - Distribution to credit unions required if SIF equity exceeds normal operating level and other statutory conditions are met (12 U.S.C. 1782(c)(3) & 1790(e))

- **Board last set NOL at 1.38% (Dec. 2019) based on methodology approved by Board in Sept. 2017**
• **Board policy objectives:**
  
  – Retain public confidence in federal share insurance
  
  – Prevent impairment of the 1 percent contributed capital deposit
  
  – Ensure Insurance Fund can withstand moderate recession without equity ratio declining below 1.20 percent over a five-year period
Setting the NOL

• Calculation based on projections related to:
  – Modeled SIF performance over five-year period assuming moderate recession
    • Stress scenario entails estimating three primary drivers of outcomes: insurance losses, insured share growth, and yield on investments
  – Potential decline in value of SIF’s claims on corporate asset management estates in a moderate recession as modeled by BlackRock
  – Projected equity ratio decline through end of 2021 without economic downturn
Approximating Moderate Recession

• The Federal Reserve did not publish the economic scenario NCUA typically uses for approximating a moderate recession (Adverse Scenario)
  – To approximate an Adverse Scenario/Moderate Recession, NCUA (OCE) used mid-point of the Base and Severely Adverse Scenarios published by Federal Reserve in September
  – Federal Reserve published two Severely Adverse scenarios in September; OCE used average of the two to make a combined Severely Adverse scenario
  • OCE used midpoint between Combined Severely Adverse Scenario and Base scenario as the Moderate Recession Scenario
Factors Warranting Consideration

• Potential decline in value of SIF’s claims on corporate asset management estates in a moderate recession as modeled by BlackRock
  – NGN notes are expected to mature in 2021 and corporate asset management estates are expected to be liquidated
  – Factor will no longer be relevant after NGN matures but there will be risk related to corporate asset management estates

• Projected equity ratio decline through end of 2021
  – Factor was originally formulated as backstop to provide extra protection for equity ratio to address the time it might take to liquidate corporate asset management estates
  – With corporate asset management estates so close to liquidation, the original intent of this factor may no longer be necessary
# NOL Options

<table>
<thead>
<tr>
<th>Option A</th>
<th>Option B</th>
<th>Option C</th>
</tr>
</thead>
</table>
| Set NOL using all three risk factors noted in policy | Set NOL using only following factors:  
- Modeled performance of SIF over a five-year period assuming moderate recession  
- Potential decline in value of SIF claims on corporate asset management estates in a moderate recession as modeled by BlackRock | Leave NOL unchanged (1.38%) |
## NOL Options (Continued)

<table>
<thead>
<tr>
<th>Component</th>
<th>2020</th>
<th>2021 (option A)</th>
<th>2021 (option B)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Statutory Minimum</td>
<td>1.20%</td>
<td>1.20%</td>
<td>1.20%</td>
</tr>
<tr>
<td>Potential Decline in SIF Performance</td>
<td>0.15%</td>
<td>0.16%</td>
<td>0.16%</td>
</tr>
<tr>
<td>Potential Decline of Value in Claims on Corporate Estates</td>
<td>0.02%</td>
<td>0.01%</td>
<td>0.01%</td>
</tr>
<tr>
<td>Projected Equity Ratio Decline through Dec. 2021</td>
<td>0.01%</td>
<td>0.02%</td>
<td>NA</td>
</tr>
<tr>
<td><strong>Equals: NOL</strong></td>
<td><strong>1.38%</strong></td>
<td><strong>1.39%</strong></td>
<td><strong>1.37%</strong></td>
</tr>
</tbody>
</table>
### Adverse & Severely Adverse Results

<table>
<thead>
<tr>
<th>2020 Scenario for 2021</th>
<th>Adverse* (option A)</th>
<th>Adverse* (option B)</th>
<th>Severely Adverse*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity for SIF Stress</td>
<td>1.36%</td>
<td>1.36%</td>
<td>1.42%</td>
</tr>
<tr>
<td>Equity for Potential Declines of Value in Claims on Estates</td>
<td>0.01%</td>
<td>0.01%</td>
<td>0.01%</td>
</tr>
<tr>
<td>Projected Equity Ratio Decline in 2020 and 2021</td>
<td>0.02%</td>
<td></td>
<td>0.02%</td>
</tr>
<tr>
<td><strong>Equals: NOL</strong></td>
<td><strong>1.39%</strong></td>
<td><strong>1.37%</strong></td>
<td><strong>1.44%</strong></td>
</tr>
</tbody>
</table>

*Numbers may not add up due to rounding

- **Recommend maintaining NOL at 1.38%**
- **In moderate recession, equity ratio would not fall below 1.20%**
- **Prevents impairment of 1% contributed capital deposit**
Factors May Impact Results

- Projected declines in equity ratio, even under no economic stress
- Unanticipated losses and/or failures in credit unions that are not market-related (such as those from fraud or other asset “bubbles”)
- Unusual or abnormally high insured share growth materially different from historical correlation
- Volatile economic conditions involving one or more market indicators compared to stress scenarios modeled
Next Steps

• Establish working group in the first quarter of 2021
  – Consider factors that impact methodology
    • Absence of the Federal Reserve’s adverse economic scenario
    • NGN program maturity
  – Request public comment
  – Recommend changes to methodology if necessary
Contact our office with questions or comments.

Email@ncua.gov

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