

NCUA LETTER TO CREDIT UNIONS

NATIONAL CREDIT UNION ADMINISTRATION 1775 Duke Street, Alexandria, VA 22314

DATE: August 2011 **LETTER NO:** 11-CU-11 (*Revised*)

TO: Federally Insured Credit Unions

SUBJ: Impact of U.S. Debt Downgrade

ENCL: Federal Agencies Issue Guidance on Federal Debt

Dear Board of Directors:

On August 5, one of three main Wall Street rating agencies (Standard & Poor's) lowered the long-term debt rating of the U.S. government and federal agencies from AAA to AA+. That same day, NCUA and the other federal financial regulators jointly issued the attached risk-based capital guidance to reassure their regulated institutions that risk weights remain unchanged.

Meanwhile, two of the three main Wall Street rating agencies (Fitch and Moody's) reaffirmed their highest ratings for all debt backed by the U.S. government.

This letter more specifically describes how these various actions may affect NCUA, credit unions and members.

Credit Union Investments – No Change to Government Risk Weights

NCUA examiners continue to assign *zero risk weights to credit union investments in NCUA Guaranteed Notes (NGNs), as well as corporate credit union investments in Treasury securities and other securities issued or guaranteed by the U.S. government.*¹

NCUA Guaranteed Notes – No Impact on Sale Proceeds

Standard & Poor's downgraded NGNs from AAA to AA+ as a direct result of S&P's downgrade of U.S. long-term sovereign debt.

The downgrade of NGNs will have no impact on NCUA, since all NGNs have already been collateralized and sold. The proceeds from NGN sales provided liquidity to the corporate credit union system and reduced overall costs of the corporate stabilization program.

¹ This sentence was revised from the previously posted version of this document to clarify the risk-weighting treatment.

If your credit union bought NGNs and plans to hold them to maturity, the downgrade in NGNs from AAA to AA+ might nominally affect the securities' value depending on your accounting treatment.

If your credit union bought NGNs and plans to re-sell them rather than hold to maturity, the price of NGNs may fall or rise based on changing market conditions.

Corporate Credit Union Liquidity Guarantee Program – No Increase in Costs

As another direct consequence of Standard & Poor's downgrade of U.S. long-term debt, S&P has downgraded other types of debt issued or guaranteed by federal agencies. As it applies to NCUA, this S&P downgrade only covers four unsecured debt issues from two corporate credit unions that NCUA guaranteed under the Temporary Corporate Credit Union Liquidity Guarantee Program.

This S&P downgrade does not affect the costs of these corporate debt obligations to NCUA or credit unions.

Money Market Funds – Limited Impact

S&P reaffirmed its highest rating (A-1+) on short-term debt of the U.S. government.

This clarification should limit any impact on money market funds and other short-term lending markets.

Consumer Confidence – Potential Impact on Share and Loan Demand

News reports about the U.S. credit downgrade and market volatility may raise concerns among consumers. As a result:

- *Credit unions may experience temporary balance sheet fluctuations. Market conditions may lead to unusually large deposit inflows or draws on existing lines of credit. Credit unions should contact NCUA and/or their State Supervisory Authority to address such developments, especially if significant balance sheet growth leads to a temporary decline in regulatory capital levels.*
- *NCUA encourages credit unions to consider all reasonable and prudent actions that could help meet the critical financial needs of their members. The credit union system has nearly \$89 billion in cash on hand. Credit unions have ample capacity to meet members' financial needs.*
- *Credit unions should maintain a dialogue with their examiners as they assess risk management challenges.*

Communications with Members – Reassurance Needed

In your communications, NCUA encourages you to reassure credit union members that:

- *The U.S. credit union system is strong and well capitalized.* Credit unions maintain an aggregate capital buffer of nearly 10% – substantially higher than the 7% threshold to be defined as “well capitalized” by law.
- *Most importantly, federally insured credit union deposits remain safe and protected as always.* NCUA continues to insure deposits up to \$250,000 per account at all federally insured credit unions.

And of course, NCUA will continue to work diligently with credit unions to mitigate risks and maintain stability in order to uphold the safety and soundness of the credit union industry.

Sincerely,

/s/

Debbie Matz
Chairman

Enclosure