MORTGAGE LENDING BY LIMITED-INCOME CREDIT UNIONS: COMMUNITY DEVELOPMENT OR NOT?

by

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ABSTRACT

Little is known about the "community development" inclinations of credit unions designated "limited income" by the federal government. National Credit Union Administration data show that limited-income credit unions with geographically localized member groups markedly increased their mortgage lending between 1980 and 1986. There is some evidence that this increase occurred as a result of increasing pressure on credit unions, particularly limited-income credit unions, to maintain income as a result of the recession and federal deregulation of financial institutions. Although the motivation of this mortgage lending increase may not have been "community development" -- a desire to provide access to home ownership among lower-income members -- smaller community credit unions and some larger community credit unions appear, based on data for the first six months of 1986, to be making quite small mortgage loans. Thus, the effect, if not the motivation, of this mortgage lending increase may have been to slightly change home ownership patterns in credit union neighborhoods. Larger limited-income community credit unions, however, may need to be drawn into more community development lending.

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Chapter 1 -- Introduction

Credit unions are, essentially, groups of people who pool their savings and lend it among themselves; management of the credit union is vested in a committee elected by the savers -- each person gets one vote, regardless of the amount of savings s/he has invested in the credit union. Since the 1970's, the National Credit Union Administration (NCUA) has had a special designation -- "limited-income credit union" -- for credit unions which serve "predominantly low-income" memberships (1). The "limited-income" designation of these credit unions enables them to accept non-member deposits (2). The notion behind this designation was that credit unions serving low-income people encourage them to become more responsible savers and function as a source of consumer credit for the poor.

Although limited-income credit unions, as a group, have much smaller asset sizes than non-limited-income credit unions, they increased their mortgage lending dramatically between 1980 and 1986. This indicates that they are potentially playing more important, "community development", roles in the neighborhoods in which they are located than was originally thought. It is the purpose of this paper to make some inferences, based on data on mortgage lending (3) by limited-income credit unions with localized fields of membership, about whether this mortgage lending constitutes "community development".

Only a limited number of credit unions are known to have community development goals. In 1980, the NCUA and the Community Services

Administration started the Community Development Credit Union (CDCU) Revolving Loan Fund. This Fund had been announced as part of President Carter's Urban Policy in 1978 and made law in 1979. The law established a fund of $6,000,000 to be loaned to selected "community based credit unions" to "provide improved services to their community members and be a positive force in community development" (NCUA 1980). Thirty-three credit unions -- out of 116 applicants -- were selected in 1980 for the initial phase of the project; a total of $5,000,000 was loaned to these credit unions. Not all of these 33 credit unions were "limited-income" and some applicants had proposed to charter credit unions only upon receipt of the loan money. In addition, twenty credit union examiners were assigned to provide on-site training, technical assistance, and guidance to credit unions receiving these loans (NCUA 1980:26). As of mid-1986, approximately $3.5 million was outstanding under the CDCU Revolving Loan Fund (NFCDCU 1986:60). Thus, at least 33 credit unions have received funds from the federal government to play a community development role in their neighborhoods.

There are indications, however, that more limited-income credit unions than those receiving CDCU Revolving Loan funds consider themselves community development institutions and that among those that do, mortgage lending plays an important role. In a recent survey of limited-income credit unions by the National Federation of Community Development Credit Unions (NFCDCU) (which calls all limited-income credit unions "community development credit unions"), two-thirds of the 85 respondents said they considered "community or economic development" part of their current mission (NFCDCU 1986:44). Of these, 47 mentioned home mortgage lending as an important part of that mission (p. 45); several mentioned home mortgage lending as the area of community development activity in which they had been successful (p. 47). Respondents to the NFCDCU survey, however, numbered only 85 out of a total of 337 limited income credit unions in 1985; and it is likely that these repondents were more interested in community development than non-respondents.

Mortgage lending by credit unions in low-income neighbohoods can have several different effects, depending on the price and recipient of the loan. If the interest rate is no lower than that charged by other other lending institutions and the recipients of the loans would be able to obtain mortgage loans elsewhere if they didn't obtain one from the credit union, then the mortgage lending by the credit union is having no effect on the neighborhood: without the credit union, members receiving mortgage loans would get them elsewhere at equivalent interest rates.

If, however, mortgage loans offered by limited-income credit unions have lower interest rates than those offered at other institutions but are still being offered to members who would be considered "creditworthy" by other financial institutions, mortgage lending by these credit unions may be functioning as an incentive to middle-income residents to remain in the predominantly low-income neighborhood rather than move out. This is, however, unlikely; there are other factors that weigh much more heavily in a middle-income family's decision whether to stay in or leave a lower-income neighborhood. If a middle income family stays in a lower-income neighborhood, it is often either because the family has no other alternative (e.g. because of racial discrimination by house sellers in other neighborhoods) or because it expects property values to increase in the neighborhood where it remains. When property values rise in a neighborhood that is predominantly low-income, at least some displacement occurs; sometimes neighborhoods are "gentrified", resulting in massive displacement.

Neighborhoods in the United States are, in general, very socioeconomically homogeneous; thus, in the United States, neighborhood stability and socioeconomic diversity are often incompatible goals, and lower mortgage interest rates alone are probably not enough to cause middle-income residents of a low-income neighborhood to remain when they otherwise would not. If mortgage loans are being offered by community credit unions in low-income neighborhoods to middle-income people who would be able to get credit elsewhere, the effect of this lending is probably to hasten gentrification rather than increase socioeconomic diversity.

In general, then, it is likely that mortgage lending by credit unions in low-income neighborhoods is only having a positive effect if it is being offered, regardless of the interest rate, to members who would not otherwise become homeowners. If this is the case, such mortgage lending promotes neighborhood stability by increasing resident equity in a neighborhood; more importantly, it increases that equity among people who would otherwise not have equity in any neighborhood. This is an especially important goal in neighborhoods where property values (and rents) are rising, whether or not they are undergoing "gentrification". Low-income people move frequently -- in response to even slight rent increases. For the purposes of this paper, this type of mortgage lending will be called a form of "community development".

Moreover, displacement in Northern cities which are centers of corporate control is the logical result of the centralization of such control which has occured in the last several years. This is because, in Northern cities, people of color often live at the core; thus, the result of the expansion of corporate control/service activity in such cities is, increasingly, displacement of these residents by office building development and the resulting migration of middle- and upper-income workers to central cities. The fact that more than one-third of limited-income-designated credit unions are located in Northern states is additional reason why limited-income credit unions should be providing their mortgage loans to lower-income people considered "risky" borrowers by banks and thrifts (savings and loans and mutual savings associations).

In this paper, I will show the magnitude and nature of the increase in mortgage lending among limited-income credit unions between 1980 and 1986. I will then point to some compelling reasons why limited-income credit unions may not <u>necessarily</u> have expanded their mortgage lending during these years solely out of a commitment to promote neighborhood access to mortgage credit or neighborhood stability by providing this credit to its lower-income members. Specifically, I will show that a "crisis" in the credit union industry caused by the most recent recession and federal deregulation of financial institutions may have impelled credit unions (particularly limited-income credit unions) into mortgage lending, after liberalization of NCUA mortgage lending rules, to maintain their income. Thus, mortgage lending was probably primarily a matter of survival for middle-sized and larger limited-income credit unions rather than only a result of a desire among these credit unions to increase opportunities for home ownership among low-income people. Nevertheless, smaller and middle-sized credit unions are constrained by their size to make smaller mortgage loans and are, as a result, probably increasing access to mortgage credit among their lower-income members. Some larger limited-incomce credit unions appear to make small mortgage loans but many make large mortgage loans; the data do not indicate whether large limited-income credit unions making large mortgage loans are promoting access to home ownership for lower-income people by, for instance, lending to housing cooperatives or to community development corporations for development projects.

In analyzing the "community development impact" of mortgage lending by limited-income credit unions, I will consider only a specific group of limited-income credit unions: those with geographically localized memberships -- memberships consisting of residents of urban neighborhoods, church members, or community organization members (4). For the purposes of this paper, I will call these credit unions with geographically-concentrated types of memberships "community credit unions". In 1986, there were 1,563 community credit unions. 214 of these were "limited-income"; this was 60.8% of all limited-income credit unions. Among community credit unions, limited-income credit unions were smaller than non-limited-income designated credit unions in 1986: 64.5% of limited-income community credit unions had assets under $500,000; 42.5% of non-limited-income community credit unions had assets of this size; and 26.8% of all federally-chartered and federally-insured credit unions had assets of this size.

It is not known how accurately the group of "limited-income" designated credit unions reflects the actual number of credit unions serving low-income memberships. Because hardly any states grant any special priveleges to state-chartered credit unions serving low-income memberships, they have no reason to distinguish between limited-income and non-limited-income credit unions under their aegis. Table I indicates that there are more credit unions that have predominantly low-income memberships than are designated "limited-income" by the NCUA. It shows the distribution of credit unions with localized fields of membership (urban residential, church-based, and community-organization-based) among zip code areas of different median family incomes in four states -- Michigan, New York, Ohio, and Pennsylvania -- in 1980. Among community credit unions in these four states, fully 49.3% in zip code areas with median family income below $10,518 (125% of the 1980 poverty level) were not designated "limited-income" and 64.4% of the credit unions in zip codes with median family incomes below $14,044 (the 1980 BLS lower standard of living) were not designated "limited income".

Although zip code areas are large (and may not reflect the median family income in the immediate location of a credit union) and a credit union may be located at the edge of a zip code area (so that much of its membership may be located outside of the zip code area), this table is at least an indication that there are probably a significant number of credit unions serving a predominantly low-income membership that have not been designated "limited-income". Because this "matching" of credit unions with demographic data is a less reliable way of identifying credit unions serving low-income memberships than the federal "limited-income"

TABLE I

MEDIAN FAMILY INCOME OF ZIP CODE AREA, COMMUNITY CREDIT UNIONS IN MICHIGAN, NEW YORK, OHIO, AND PENNSYLVANIA, 1980

MEDIAN FAMILY INCOME IN ZIP CODE AREA	LIMITED-INCOME Number	LIMITED-INCOME Percent	LIMITED-INCOME Cum. Pct.	NON-LIMITED-INCOME Number	NON-LIMITED-INCOME Percent	NON-LIMITED-INCOME Cum. Pct.	TOTAL Number	TOTAL Percent/ Cum. Pct.
Below $10,517	36	50.7	50.7	35	49.3	49.3	71	100.0
$10,518 (1) - $14,043	16	21.3	35.6	59	78.7	64.4	75	100.0
$14,044 (2) - $19,927	10	5.4	18.7	175	94.6	81.3	185	100.0
$19,928 (3) - $29,999	2	1.5	13.7	134	98.5	86.3	136	100.0
$30,000 or Over	1	4.5	13.3	21	95.5	86.7	22	100.0

Source: National Credit Union Adminstration 1980 Midyear Financial and Statistical Report and 1980 Census
1. 125% of Poverty Level
2. Bureau of Labor Statistics Lower Standard of Living (the National Credit Union Administration considers individuals with incomes below this amount to be "low-income".
3. Median Family Income for the United States, 1980

designation, I will use the latter in the analyses that follow. Because the number of non-limited-income credit unions that appear to be in low-income neighborhoods is not inordinately large, conclusions about differences between credit unions with and without low-income memberships based on comparisons between limited-income-designated and non-limited-income designated credit unions will still be considered valid.

Information about volume of mortgage lending and size of mortgage loans is available for all credit unions semiannually from the NCUA Financial and Statistical Report. The Financial and Statistical Report contains detailed financial and operating data on on all federally-chartered credit unions and those state-chartered credit unions which are federally-insured. In this database, lending is broken down into several categories, but the categories represent, in general, the security, not the purpose, of the loans. Aside from automobile lending, the only category of loan for which the security and the purpose is the same is first mortgage lending. All loans in the "first mortgage" category go to the purchaser and resident of a 1-to-4 family home for the purchase of that home, are of twelve or more years' duration, and are secured by a first lien.

For this study, data from the NCUA Financial and Statistical Report were obtained for midyear 1980 and midyear 1986 (end-of-year 1986 was not available at the time the data were requested; midyear rather than end-of-year 1980 was selected to control for seasonal fluctuations in loans and shares in comparisons with 1986). This database does not include credit unions that are state-chartered and not federally-insured;

the Credit Union National Association (CUNA) estimates that, in 1986, there were 2,270 state-chartered, privately-insured or non-insured credit unions; thus, in this year, 86.7% of all credit unions were included in the NCUA Midyear Financial and Statistical Report.

In Chapter 2, I will describe patterns of mortgage lending among limited-income and non-limited-income community credit unions and all credit unions between 1980 and 1986. In Chapter 3, I will describe changes in the credit union industry since the recession beginning in 1978-79 and deregulation beginning in the early 1980's. In Chapter 4, I will make some inferences, in light of the findings presented in Chapters 2 and 3, about the community development effect of mortgage lending among limited income credit unions and their memberships.

Chapter 2 -- Recent Changes in Mortgage Lending by Limited Income Community Credit Unions

Data from the NCUA Midyear Financial and Statistical Report indicate that there was a substantial increase in mortgage lending among limited-income community credit unions between 1980 and 1986, a much more substantial increase than that among non-limited-income credit unions. This increase was permitted by a significant liberalization of mortgage lending regulations for federally-chartered credit unions. Although state-chartered credit unions in many states had long been able to make mortgage loans of standard maturity and size, mortgage lending by federally-chartered credit unions (which constitute the bulk of the NCUA database) is a fairly recent phenomenon. Along with the granting of permission for federally-chartered credit unions to offer share draft accounts (interest-bearing "checking accounts") in 1980, liberalization of mortgage lending rules was one of the most important new powers granted to credit unions as a result of deregulation. In 1977, the maximum allowed maturity for residential real estate loans made to finance the acquisition of a one-to-four family dwelling for the principal residence of a credit union member secured by a first lien was increased from ten to thirty years. This more liberal mortgage loan regulation applied only to credit unions with assets of $2 million or more; credit unions with assets less than $2 million had to get permission from the NCUA to make such loans. Larger credit unions didn't need permission but could only devote 25% of their assets to such loans without NCUA permission.

In 1981, the NCUA permitted federally-chartered credit unions with assets of less than $2 million to make mortgage loans, permitted all federally-chartered credit unions to make variable rate mortgage loans, and made the 25% limitation on the amount of real estate loans applicable to fixed-rate mortgage loans only. In 1982, the maturity limit on mortgage loans was increased to forty years and refinancing of first mortgages was allowed. The maximum loan interest rates allowed by the NCUA was raised in March 1980 from the long-standing 12% rate (1% per month) to 15%; the NCUA was also given permission to raise loan interest rates even further for periods of 18 months at a time if economic conditions warranted. Finally, in September 1984, the limitation on the amount of fixed-rate mortgages was removed, though mortgage lending by federally-chartered credit unions remained subject to the restriction on the amount of any lending made by a credit union to any individual member to ten percent of total share capital.

These more permissive mortgage regulations also took effect in the nineteen states which have "wildcard" laws that grant new powers to credit unions chartered in those states as soon as they are granted to federally-chartered credit unions (Heaton 1985). Some state credit unions, however, had enjoyed more liberal mortgage lending regulations before 1976. In 1975, state-chartered credit unions in thirty states had the authority to make long-term real-estate loans; at year-end 1975, 16% of the total loan portfolio of state-chartered credit unions in these states was secured by real estate. During this year, only 8.7% of loans to members by federally-chartered credit unions were real estate loans (Melvin 1977:29-30).

Tables II (A) and (B) show that the increases in aggregate and per-credit-union mortgage loans out were much greater among limited-income community credit unions than other community credit unions, but that the increases among community credit unions were much greater than those for the credit union industry as a whole. In addition, aggregate and per-credit-union real estate loans out among community credit unions rose to become a significant portion of total loans out during this period -- much more so than for all credit unions.

Tables III (A) and (B) show the same phenomenon from the perspective of individual credit unions. They show that the percentage of individual community credit unions devoting a significant percentage of their total lending to mortgage lending also increased sharply between 1980 and 1986. This increase was particularly pronounced among limited-income community credit unions with assets over $2 million: the percentage of these credit unions with real estate lending amounting to at least 25% of the total loan portfolio jumped from 10.8% to 51.2% between 1980 and 1986. The increase for non-limited-income community credit unions was slightly less: "25% mortgage lenders" in this category increased from 4.6% to 25.6% between 1980 and 1986. The percentage of community credit unions in the mid-sized asset category ($500,000 to $1,999,999) devoting 10% to 24% of their total lending to mortgage lending also increased greatly. For limited-income credit unions in this category, the percentage increased from 1.3% to 17.1%; for non-limited-income credit unions in this category, the increase was less: 3.1% to 8.1%. The proportion of moderate- and large-asset-sized community credit unions making no mortgage loans at all decreased dramatically between 1980 and 1986.

TABLE II (A)

CHANGE IN TOTAL LENDING AND REAL ESTATE LENDING BY CREDIT UNIONS, 1980-1986

LOAN CATEGORY	LIMITED-INCOME COMMUNITY CUs	NON-LIM.-INC. COMMUNITY CUs	ALL CREDIT UNIONS
Total lending			
1980 (1)	61,101	2,192,172	53,914,419
1986	789,886	4,447,467	78,865,000
Percent change	1192.8	102.9	46.3
Real estate lending			
1980 (1)	8,599	312,206	4,037,858
1986	318,014	2,536,047	7,710,566
Percent change	3598.3	712.3	91.0

Source: National Credit Union Administration Midyear Financial and Statistical Report, 1980 and 1986

1. In 1986 dollars

TABLE II (B)

CHANGE IN MEAN PER-CREDIT-UNION TOTAL LENDING AND REAL ESTATE LENDING, 1980-1986

LOAN CATEGORY	LIMITED-INCOME COMMUNITY CUs	NON-LIM.-INC. COMMUNITY CUs	ALL CREDIT UNIONS
Total Lending			
1980 (1)	351,153	1,712,634	3,089,120
1986	3,691,057	3,296,862	5,317,937
Percent change	951.1	92.5	72.2
Real Estate Lending			
1980 (1)	49,421	243,911	231,356
1986	1,486,046	1,879,946	519,930
Percent change	2906.9	670.8	124.7

Source: National Credit Union Administration Midyear Financial and Statistical Report, 1980 and 1986

1. In 1986 dollars

TABLE III (A)

MORTGAGE LENDING AS A PROPORTION OF TOTAL LENDING AMONG COMMUNITY CREDIT UNIONS, 1980

ASSETS	PERCENTAGE OF TOTAL LOAN DOLLARS OUT REPRESENTED BY REAL ESTATE LENDING (NO./PCT. OF CREDIT UNIONS) 0% No.	0% Pct.	1-9% No.	1-9% Pct.	10-24% No.	10-24% Pct.	25% or Over No.	25% or Over Pct.	Total No.	Total Pct.
Under $500,000										
Limited-Income	60	100.0	0	0.0	0	0.0	0	0.0	60	100.0
Non-Limited-Income	199	100.0	0	0.0	1	0.0	0	0.0	200	100.0
$500,000 - $1,999,999										
Limited-Income	71	92.2	4	5.2	1	1.3	1	1.3	77	100.0
Non-Limited-Income	356	92.2	15	3.9	12	3.1	3	0.8	386	100.0
$2,000,000 and Over										
Limited-Income	19	51.4	8	21.6	6	16.2	4	10.8	37	100.0
Non-Limited-Income	438	60.7	143	19.8	80	11.1	33	4.6	694	100.0

Source: National Credit Union Administration Midyear Financial and Statistical Report, 1980

TABLE III (B)

MORTGAGE LENDING AS A PROPORTION OF TOTAL LENDING AMONG COMMUNITY CREDIT UNIONS, 1986

ASSETS	PERCENTAGE OF TOTAL LOAN DOLLARS OUT REPRESENTED BY REAL ESTATE LENDING (NO./PCT. OF CREDIT UNIONS) 0% No.	0% Pct.	1-9% No.	1-9% Pct.	10-24% No.	10-24% Pct.	25% or Over No.	25% or Over Pct.	Total No.	Total Pct.
Under $500,000										
Limited-Income	128	93.5	1	0.7	5	3.6	3	2.2	138	100.0
Non-Limited-Income	544	94.9	10	1.7	13	2.3	6	1.0	573	100.0
$500,000 - $1,999,999										
Limited-Income	20	57.1	6	17.1	6	17.1	3	8.6	35	100.0
Non-Limited-Income	240	77.9	32	10.4	25	8.1	11	3.6	308	100.0
$2,000,000 and Over										
Limited-Income	7	17.1	4	9.8	9	22.0	21	51.2	41	100.0
Non-Limited-Income	173	37.0	91	19.4	84	17.9	120	25.6	468	100.0

Source: National Credit Union Administration Midyear Financial and Statistical Report, 1986

Moreover, it appears that the increase in mortgage lending among community credit unions between 1980 and 1986 represented a large increase in the proportion of shares and deposits loaned out as real estate loans; and it appears that this enabled limited-income credit unions to bring their overall loaned-out ratio -- the proportion of shares and deposits loaned out -- closer to that of non-limited-income unions (see Table IV). A higher loaned-out ratio yields more income for a credit union, and limited-income credit unions have historically had lower loaned-out ratios than other credit unions.

Though it is clear from the statistics presented above that even small and mid-sized limited-income credit unions developed the administrative capacity to provide mortgage loans to their members between 1980 and 1986, it is not clear whether these mortgage loans increased access to mortgage credit among lower-income residents of the neighborhoods in which these credit unions are located --- in other words, whether the increase in mortgage lending was impelled by a commitment to changing home ownership patterns in their neighborhoods. In the following chapter, I will describe changes in the credit union industry since 1980 that may have led limited-income credit unions to significantly increase their mortgage lending for their own survival rather than primarily for "community development" reasons.

TABLE IV

LOANED-OUT RATIO AND REAL ESTATE LOANED OUT RATIO FOR COMMUNITY CREDIT UNIONS, 1980 AND 1986

ASSET SIZE	TOTAL LOANS ($)/ SHARES ($) 1980	1986	REAL ESTATE LOANS ($)/ SHARES ($) 1980	1986
$-499,999				
Limited-Income	0.543	0.609	0.000	0.018
Non-Limited-Income	0.630	0.678	.000	0.011
Differential	-0.087	-0.069	.000	0.007
$00,000-1,999,999				
Limited-Income	0.711	0.715	0.008	0.070
Non-Limited-Income	0.814	0.738	0.009	0.036
Differential	-0.102	-0.023	-0.002	0.035
$,000,000 or Over				
Limited-Income	0.734	0.662	0.064	0.186
Non-Limited-Income	0.848	0.670	0.052	0.103
Differential	-0.113	-0.008	0.013	0.083

Source: National Credit Union Administration Midyear Financial and Statistical Report, 1980 and 1986

Note: For the 1980 data, there were 188 missing values for the variable "total shares and deposits" (the denominator of the ratios above) out of 1483 cases. In addition, four cases were eliminated for 1980 and one for 1986 because the loaned-out ratios were over 4.

Chapter 3 -- Recent Changes in the Credit Union Industry

The disproportionate increase in mortgage lending among limited-income community credit unions between 1980 and 1986 occurred in the context of major changes in financial markets: particularly relevant is the crisis in the credit union industry resulting from the recession and deregulation and the competition, particularly between limited income credit unions and other financial institutions, for the deposits of a few higher-income members.

Credit unions experienced significant economic stress between 1980 and 1986. Since the most recent recession and federal deregulation of all financial institutions, they have experienced unusually high charter cancellation rates and, for the first time in the industry's history, significant annual declines in numbers (most federal credit union cancellations are due to liquidations of insolvent credit unions and mergers; a much smaller number are due to conversions to state charters and charter revocations (NCUA 1980:29-30)). Table V shows the magnitude of the decline in the industry; it shows charters issued and canceled, net change, and active federally-chartered credit unions for the years 1980 to 1986. Since 1934, when federal chartering of credit unions was first allowed, net change in the number of credit unions had been negative in only six years; between 1980 and 1986, however, net change in number of credit unions was negative. Since 1934, charters canceled had only exceeded 500 in two years; between 1981 and 1985, they exceeded 500 in every year. Finally, the number of active credit unions had not fallen below 12,000 since 1965, whereas they were below this number between 1981 and 1986 and fell to 9,658 in 1986.

TABLE V

CHANGE IN NUMBER OF FEDERALLY-CHARTERED CREDIT UNIONS
1980 - 1986

YEAR	CHARTERS ISSUED	CHARTERS CANCELED	NET CHANGE	ACTIVE CREDIT UNIONS
1980	170	368	-198	12,440
1981	119	554	-435	11,969
1982	114	556	-442	11,631
1983	107	736	-629	10,976
1984	135	664	-529	10,548
1985	55	575	-520	10,125
1986	59	441	-382	9,658

Source: National Credit Union Administration 1986 Annual Report

The recession caused economic stress for credit unions in several ways. An increase in interest rates beginning in 1978-79 and the advent of money market accounts (which had no interest rate limitation) caused savings outflows among financial intermediaries during the early 1980's as consumers, spurred by inflation, sought to obtain maximum returns on their savings. Growth in credit union lending began to slow markedly during 1979, when interest rates had increased to the point where the 12% cap on credit union loan interest rates made lending insufficient to yield the revenues to pay the high share dividend rates needed to attract deposits. In addition, there was a large decline in demand for consumer lending among all financial institutions (except finance companies) as people's earnings failed to keep pace with inflation. In March 1980, the Depository Institutions Deregulation and Monetary Control Act raised the credit union loan interest rate cap to 15% and authorized the NCUA to raise it further for periods of 18 months if economic conditions warranted; demand, however, remained low. Thus, during the second half of 1980, there was a big decline in loan/share ratios among credit unions.

Federal deregulation of financial institutions also created shifts in the credit union industry. Although deregulation gave credit unions new powers vis-a-vis banks and thrifts, it also reduced the "sheltered" status of credit unions by giving banks and saving and loans powers which had traditionally been the domain of credit unions. In 1980, federally-chartered thrifts (savings and loans and mutual savings associations) were given the power to offer automobile loans and personal loans (the traditional specializations of credit unions) for the first time. In 1982, thrifts' aggregate lending limit in consumer and other loans was increased. Although, in 1982, legislation was passed which immediately removed the 7% ceiling on credit union share, share draft, and share certificate accounts (so credit unions got a head start on deposit rate deregulation), the Depository Institutions and Deregulation and Monetary Control Act of 1980 provided for gradual removal of ceilings on most types of bank and thrift deposits between 1982 and 1986; the ceiling on passbook accounts for these institutions (which was 5.5% at the time) was lifted on April 30, 1986 (passbook accounts at banks and thrifts are equivalent to credit union share accounts (the most common type of credit union deposit account)).

Despite these volatile financial markets and substantial deregulation in the financial services industry, Table VI shows that, in comparison with non-community development credit unions, the number of limited-income community credit unions has remained relatively stable. The data in this table indicate that, as a group, limited-income credit unions fared better in terms of numbers between 1980 and 1986 than non-limited income credit unions: the number of limited-income credit unions increased by 18%, whereas the total number of credit unions increased by only 1%. In addition, the number of large limited-income community credit unions increased (by 11%), while the number of large non-limited-income community credit unions declined (by 33%). The fact that there were equivalent numbers of large limited-income credit unions in 1980 and 1986 indicates that cancellation rates among these credit unions were low (5). Limited income community credit unions, however, fared less well than non-limited-income community credit unions at smaller asset sizes: for community credit unions with assets under $500,000, the increase in number of limited-income credit unions was 130%, whereas the increase in number of non-limited-income credit unions was 187%; among mid-sized credit unions (assets of $500,000 - $2,000,000), the decline in the number of limited-income credit unions was much greater (-55%) than the decline in the number of non-limited-income credit unions (-20%).

The apparent increase in number of (and absence of cancellations among) large limited-income credit unions between 1980 and 1986 is surprising. In the 1970s, much was made of the very high failure rate of the 500-odd credit unions that were started by the Office of Economic Opportunity between 1964 and 1970 as part of the War on Poverty. Of these credit unions, only half of them were still in operation by 1978 (Caftel 1978:40). A 1971 General Accounting Office report blamed this

TABLE VI

CHANGE IN NUMBER OF COMMUNITY CREDIT UNIONS
1980 - 1986

ASSET SIZE	1980	1986	PERCENT CHANGE
Under $500,000			
Limited Income	60	138	130.0
Non-Limited Income	200	573	186.5
$500,000 - $1,999,999			
Limited Income	77	35	-54.5
Non-Limited Income	386	308	-20.2
$2,000,000 or over			
Limited Income	37	41	10.8
Non-Limited Income	694	468	-32.6

Source: National Credit Union Administration Midyear Financial and Statistical Report, 1980 and 1986

high failure rate on the limited savings of low-income families and poor management (Feldman 1974:451). Cargill (1975) also called attention to the poor financial health of these limited-income credit unions.

Moreover, limited-income credit unions pay higher share dividend rates than non-limited-income credit unions to become and remain large (member savings constitute the bulk of credit union assets); this fact makes it even more surprising that the number of large limited-income credit unions remained so stable between 1980 and 1986. Table VII shows that, among community credit unions with asset sizes of $2 million or over which offer share accounts, a slightly higher percentage of limited income credit unions (31.6%) than non-limited-income credit unions

(23.8%) pay share dividend rates above 7.0%, the maximum rate allowed for credit unions before rates were deregulated in 1982. Only one limited-income community credit union at this asset size paid dividend rates below 5.5%, the ceiling for bank and thrift passbook accounts until rates on those accounts were deregulated on April 30, 1986. Thus, many large community credit unions have raised their dividend rates above the previous ceiling since 1982.

TABLE VII

SHARE DIVIDEND RATES OFFERED BY COMMUNITY CREDIT UNIONS WITH ASSETS OF $2,000,000 OR OVER 1986

RATE	LIMITED-INCOME	NON-LIMITED-INCOME
Under 5.5%		
Number	1	29
Percent	2.6	6.7
5.5%-6.9%		
Number	25	300
Percent	65.8	69.4
7.0% or over		
Number	12	103
Percent	31.6	23.8
Total		
Number	38	432
Percent	100	100

Source: National Credit Union Administration Midyear Financial and Statistical Report, 1986

The results of the NFCDCU survey also indicate that large limited income credit unions must compensate for the fact that many of their members are low-balance depositors by paying higher share dividend rates than large non-limited-income credit unions. 24% of the member share balances of the limited-income credit unions responding to the NFCDCU survey were $50 or under; 36% were under $100; 49% were under $200; and 64% were under $500 (NFCDCU 1986:27). Those limited-income credit union respondents that felt that they had been successful in attracting member deposits said their ability to pay a high or competitive dividend was the factor most responsible for their success (p. 30). Conversely, low dividends were cited most often as an obstacle in promoting savings (p. 33) and cited by some as an obstacle in attracting non-member deposits (p. 64). One limited-income credit union official wrote that the costliness of his credit union's numerous "low-balance, service intensive" accounts prevented the credit union from offering competitive rates on higher balances (p. 33). NFCDCU survey respondents "often cited competition from other financial institutions [including other credit unions] as an obstacle to attracting savings to CDCUs.... It is that segment of CDCU membership with larger savings or more substantial income -- a small but important minority of CDCU members -- which is the object of competitive appeals." (p. 34). Some respondents thought that they would lose deposits if they lowered their dividend rates (p. 80). Most limited income community credit unions over $2 million are residential, and credit unions with residential fields of membership are, in general, more "depositor-oriented" than "borrower-oriented" (Pugh 1984) -- (i.e. they charge higher interest rates on loans and pay higher dividend rates on shares than other credit unions). The need for limited-income credit unions to pay high share dividend rates has important implications. It means that maintaining adequate income has been an important consideration for these credit unions, particularly since deregulation.

In the context of the changes in the credit union industry described in this chapter, it appears that this increase in volume of mortgage lending among limited-income community credit unions may have been, at least partly, a business decision. Credit unions, including limited-income credit unions, need to cover their costs, and larger limited income credit unions (more than large non-limited-income credit unions) pay high share dividend rates to attract deposits. It appears that the dramatic increase in mortgage lending by limited-income credit unions between 1980 and 1986 was, in part, a strategy to maintain income in the wake of the most recent recession and financial deregulation.

Mortgage lending has operational advantages that may have been particularly appealing to limited income credit unions. It is a less costly way of increasing lending (and thereby increasing income) than providing more consumer loans because small consumer loans (the traditional domain of credit unions, particularly limited-income credit unions) have high per-dollar administrative costs. An increase in lending among credit unions was particularly needed during the recession. In addition, mortgage lending, because it can be offered at variable rates as well as fixed rates, probably increased the consistency as well as volume of credit unions' earnings. A wider range of lending services, too, is an advantage in the competition for high-deposit members. In addition, the more consistent earnings afforded by mortgage lending may account, in part, for the low failure rate among large limited-income community credit unions (the most prolific group of mortgage lenders) between 1980 and 1986.

That the causes of the increase in mortgage lending among limited-income community credit unions between 1980 and 1986 was not impelled by a community development agenda but by a need to maintain income doesn't, however, necessarily mean that it didn't have "community development" effects. In the next chapter, I will draw some conclusions about who has benefitted from this mortgage lending.

Chapter 4 -- Conclusion: Mortgage Lending by Limited-Income Community Credit Unions as a Community Development Activity

Though limited-income credit unions are required to make all of their loans to their members and the memberships of limited-income credit unions are predominantly "limited-income", it does not neccessarily follow that mortgage loans by limited-income credit unions go to limited-income individuals. Data on total amount and number (and thus mean size) of first-mortgage loans for the first six months of 1986 (obtained from the NCUA Financial and Statistical Report) provides some limited information about the size, and thus the income of the recipients of, mortgage loans issued by community credit unions during the first six months of 1986; these data are presented in Table VIII. Although it is not clear how accurate these data are (see footnote 1 for Table VIII), they indicate that there is not a large difference between the incomes of recipients of first-mortgage loans from limited-income and non-limited-income credit unions: 58.3% of the limited-income community credit unions and 74.9% of the non-limited-income community credit unions providing mortgage loans during this period had a mean first-mortgage loan size less than the price of a house affordable by a lower-income family. The data also indicate that small and mid-sized credit unions provide fairly small first mortgage loans (88.9% and 91.4% in the lower size category, respectively). Large community credit unions appear to make both small and large first mortgage loans. It is not clear from the data whether or not the larger first-mortgage loans made by these larger limited-income credit unions went to housing cooperatives

TABLE VIII

MEAN LOAN SIZE OF FIRST-MORTGAGE LOANS, COMMUNITY CREDIT UNIONS FIRST SIX MONTHS, 1986 (1)

ASSETS	CREDIT UNIONS WITH MEAN FIRST MORTGAGE LOAN $46,718 (2) OR BELOW	CREDIT UNIONS WITH MEAN FIRST MORTGAGE LOAN ABOVE $46,718 (2)	TOTAL
Under $500,000			
Limited Income	1	1	2
Non-Limited Income	7	0	7
$500,000 - $2,000,000			
Limited Income	7	0	7
Non-Limited Income	25	3	28
$2,000,000 or over			
Limited Income	13	14	27
Non-Limited Income	144	56	200

Source: National Credit Union Administration (NCUA) Midyear Financial and Statistical Report, 1986

1. Of the 305 credit unions which entered first mortgage loan figures for the first half of 1986 in their reports, 34 had mean first mortgage loans below $10,000; the NCUA Office of Examination and Insurance says that this is probably a reporting error -- some credit unions may be reporting home improvement loans in this category. Thus, cases with mean mortgage loan size below $10,000 were not included in this table. Nevertheless, even the remaining credit unions may have reported home improvement loans as first mortgage loans for 1986; thus, the loan sizes in this table may be artificially low.
2. This is 250% of the 1980 BLS Lower Standard in 1986 dollars (1980 was the last year in which the BLS standard-of-living classification was used); as a rule of thumb, home purchasers are considered to be able to afford a home with a price equivalent to 250% of their income.

(this is possible, since membership in federally-chartered credit unions may include incorporated and unincorporated organizations if permitted by the Board of the credit union (CUNA 1986:26). The NFCDCU has written that "collaboration with, as well as financing of, housing cooperatives has begun to increase" among limited-income credit unions (NFCDCU 1986:49).

Based on the data presented in Table VII, it appears that small community credit unions (those with assets under $2 million), because they are more "close to the ground" -- member-run and proxy to positive "informal" information about the ability of members to repay loans -- are in a unique position to provide loans to lower-income members who are perhaps considered "high-risk" by other financial institutions (through credit unions with assets under $500,000 provide very little mortgage lending). Larger credit unions, the ones that have most dramatically increased their mortgage lending, are less "close to the ground". The lending decision process among larger limited-income credit unions is probably more similar to other financial institutions because positive, informal information about loan applicants is probably less available to these credit unions than to smaller credit unions, larger credit unions often hire staff members to make their lending decisions, and, as we saw in the previous chapter, they may be more concerned with maintaining income than smaller credit unions and less interested in service-intensive lending (such as that which might be necessary for new and smaller-loan mortgage borrowers).

Thus, the resources of larger limited-income community credit unions should be tapped -- for mutual benefit -- by community development corporations and state and local public agencies, and these larger limited-income credit unions should be encouraged to promote access to mortgage credit and home ownership in the neighborhoods in which they are located if they are not already. Smaller limited income community credit unions, which are more numerous, appear, in general, to be already providing their mortgage credit to low-income members with their limited funds. Both large and small community credit unions located in low-income neighborhoods, whether or not they have been designated "limited-income", should be considered community development organizations.

Moreover, the fact that credit unions have a "self-generated" source of income may be a potential community developement advantage with the recent liberalization of federal credit union commercial lending powers that will enable limited-income credit unions to engage in commerical development if they wish. Community development corporations largely rely on grants for operational support; and it is, in many cases, much harder -- and time-consuming -- to maintain a continuous flow of grants than it is to maintain a deposit base through sufficiently high dividend rates. In addition, community development corporations, because they are dependent on outside financing for development projects, must constantly react to changes in national policy that dictate what kinds of community development are feasible: currently, they are almost exclusively developing real estate (primarily through taking advantage of the tax code to leverage private investment) and not focusing, as they used to, on industrial development and job creation. As of this year, this focus, too, must change as a result of tax reform. Credit unions, although they are small and thus limited in their development activities, are not as susceptible to such national policy changes; although they are directly affected by federal regulatory changes, they are protected against such changes, to an extent, by being members of an industry that has a strong trade association and a federal regulatory agency that protects the industry's interests.

The Paul Cuffee Credit Union, in the South End of Boston, with assets of about $500,000, is a good example of how even small limited-income credit unions can effect a shift in the economic position of some of their members. In the early 1980's, the credit union foresaw that many neighborhood residents would be displaced as property values rose. With their limited assets, they targeted abandoned and foreclosed properties in the neighborhood, making 33 members home owners through this strategy. Today, with neighborhood property values significantly higher and the neighborhood significantly "gentrified", these 33 homeowners are still in the neighborhood and have realized an increase in "wealth" through the houses they bought just a few years ago.

Most limited-income credit unions, like the Paul Cuffee Credit Union, are too small to reverse or halt neighborhood investment and disinvestment trends. Patterns of urban development are, in large measure, the aggregate result of regional, national, and international capital flows which are largely influenced by people outside of low-income neighborhoods. Nevertheless, the Paul Cuffee Credit Union demonstrates that even small credit unions can promote development within this context if they use their assets in a carefuly-planned way. Limited-income credit unions, because they are experienced mortgage lenders, clearly have the potential to target their assets in a way that can provide access to mortgage credit to those who would not ordinarily have such access and thus perform a "community development" role in their neighborhoods. Whether or not they do depends, it appears, on the proclivities of those who operate the credit union and government policies encouraging such lending, not (as I have shown) solely on the amount of capital available to that credit union.

FOOTNOTES

1. "Low-income members" are defined by the NCUA as

"(1) those members whose annual income falls at or below the lower standard of living classification as established by the Buréau of Labor Statistics, U.S. Department of Labor, (2) those members who are residents of a public housing project who qualify for such residency because of low income, (3) those members who qualify as recipients in a community action program, and (4) those members who are enrolled as full-time or part-time students in a college, university, high school, or vocational school." (Fed. Regs. 1986:731)).

The BLS lower standard of living was part of a tripartite classification -- lower, medium, and high -- of standards of living for an urban family of four; it was derived from the BLS urban family budget survey.

2. The extent to which limited-income credit unions have taken advantage of their ability to accept and insure non-member deposits appears to be uneven and total non-member deposits in limited-income credit unions is believed to be small (NFCDCU 1986:57). The NFCDCU writes that survey respondents reported about $15.3 million in non-member deposits. Individuals were the largest sources of non-member deposits ($4.7 million) among survey respondents. The second-largest sources was churches and religious organizations ($4 million); corporations (including insurance compnnies and banks) ranked third ($2.82 million); and foundations were the fourth-largest source ($1.23 million). Non-member deposits by state and local governments were found to be small: $200,000 and $521,665, respectively. Finally, NFCDCU survey respondents said they held $741,283 in federal deposits (the NCUA considers loans from the CDCU Revolving Loan fund non-member deposits). The NFCDCU writes that their experience suggests that their survey respondents include the majority of those CDCUs which are the most active in seeking non-member deposits and they estimated the total non-member deposits for all CDCUs to be probably no more than $20-$25 million, or 5.7% of the estimated $400 million in aggregate CDCU assets. (NFCDCU 1986:57)

Moreover, these non-member deposits are only held by a small number of the NFCDCU respondents. Almost two-thirds (52 out of 80) of the respondents to the NFCDCU survey said that they did not actively seek non-member deposits, and 28 out of 85 said that they did not know that they were classified "limited- income" and are thus eligible to receive non-member deposits (NFCDCU 1986:60). Some indicated that they did not have the staff time or expertise to solicit non-member deposits (NFCDCU 1986:61).

3. In this paper, the terms "mortgage loans" and "real estate loans" will be used to mean loans provided for the purchase of a home.

4. The other common types of credit union memberships tend to be more geographically dispersed: workplace-based credit unions, labor union based, and fraternal association based. I did not include rural residential credit unions because I am particularly interested in urban community development.

5. It is probable that, in large part, the limited-income credit unions that were in the large asset size category in 1980 are the same as the ones in 1986 because 1) assets of limited-income credit unions probably do not grow at a rapid rate and 2) a credit union usually acquires limited-income status at chartering rather than upon a decline in membership income. For both of these reasons, the increase in number of large limited-income credit unions probably does not represent the <u>net</u> of a large cancellation rate plus a large growth rate.

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