



SACRAMENTO

CREDIT UNION

Invest in Sacramento

2004

ANNUAL REPORT

**800 H STREET
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Board of Directors' and President's Report

As Sacramento Credit Union approaches the 70th anniversary of its formation, we look forward to the privilege of serving the membership for many years to come. Adding value to the financial well being of the members is the foundation on which this organization was built. The Board of Directors and management team strive to maintain the credit union's reputation for sound operating standards and integrity. In tandem with its traditions are the ongoing efforts to offer innovative products and services.

In the wake of the nation's corporate scandals and the subsequent demise of internationally respected accounting firms, more stringent audit standards have been imposed throughout corporate America. An independent audit of financial statements and a regulatory examination in 2004 validated the safety and soundness of Sacramento Credit Union. The highest ratings possible were granted, and there were no material exceptions. The credit union maintains its well capitalized status as defined by the National Credit Union Association, while outpacing industry performance in net earnings and achieving 13% loan growth. In an unprecedented interest rate environment, growth has been balanced and risk managed. At the same time, net operating expense was reduced.

The Boards of Directors of both credit unions agreed to the merger of Kai-Perm Sacramento Federal Credit Union into Sacramento Credit Union because of our conviction to the members. The merger has received regulatory approval from federal and state agencies. Sacramento Credit Union is honored to share the benefits of this alliance and the potential it brings.

The credit union introduced first mortgage lending three years ago to enhance its home mortgage program. At its inception a commitment was made to this critical product offering, and in each ensuing year the home mortgage program has evolved. Last year a first time home buyers' program was added. In addition, construction began on *Your Home Loan Center* within our H Street location to better serve your needs in this expanding program.

To *Invest in Sacramento* is the philosophy of Sacramento Credit Union. Two long standing community service projects are the SCU sponsored Skip-A-Loan Payment Program and the Holiday Stocking Program. Proceeds are donated to the Sacramento Children's Home and UC Davis Children's Hospital, respectively. The credit union is a sponsor of the annual Salvation Army Can Tree program and is a participant in the United Way Campaign. On an individual basis, many employees are involved in service organizations and community activities. We believe in the concept of "people helping people", and in doing so, we all benefit.

Submitted by: Les Brown
Chairperson, Board of Directors

Jerrold A. Kinlock
President/CEO



Secretary-Treasurer's Report

Net earnings for fiscal year ended September 30, 2004, were \$3,133,804, equivalent to 112 basis points on average assets of \$280 million. The figures, respectively, for prior fiscal year were \$3,207,084 or 122 basis points on \$260 million. Net worth increased 11.5%, down slightly from the 13.4% realized during prior fiscal year. For 17 of the last 18 fiscal years, Sacramento Credit Union has generated net earnings in excess of 100 basis points, as well as return on equity, in excess of 11%. As a result of nearly two decades of solid financial performance, the net worth ratio stands in excess of 10.6%, far above the 7.0% threshold declared as "well capitalized" by the National Credit Union Association.

During the first three years of this century, the credit union industry experienced vigorous growth in deposits, largely attributed to the demise of the equity markets with potential investors seeking "safe harbor" to preserve net worth. Since late 2003, in contrast, deposit growth has slowed for all credit unions. Sacramento Credit Union's asset growth has slowed to around 3.0%, well under long term norms. A related challenge is the sluggish rate of growth in members, specifically, negative 0.30% for fiscal year 2003 – 2004. Membership at September 30, 2004, totaled 25,410, down 77 from one year earlier.

Also well under long term trends has been the dividend rate paid to depositors for the use of their money. Market rates of interest have defied projections and remained low after three years of precipitous decline. As a result, cost of funds at Sacramento Credit Union dropped 24.0% from the \$4.5 million in dividends paid during fiscal year 2002 – 2003.

Loan growth has proved just as volatile. For fiscal year 2002 – 2003 the portfolio struggled to grow a mere 1.0%. However, thanks to rejuvenated demand for mortgage and auto loans, loan growth surged over 13.0% for fiscal year 2003 – 2004 with the ratio of loans to assets climbing from 69.6% to 73.4%. Concurrently, loan quality has improved with impressive reduction in delinquency, charge-offs and provision for bad debt.

Sacramento Credit Union remains financially safe and sound with management vigilant in the detection and management of risks inherent in an economic environment replete with ballooning deficits and twin threats of rising rates of interest and inflation.

Submitted by: Terry Tice
Secretary-Treasurer, Board of Directors



Lending Report

Sacramento Credit Union experienced strong loan growth in all areas of its operation during fiscal year 2004. During this period, the credit union funded \$93 million of consumer loans and \$58 million in residential first mortgage loans. This production represents a 43% increase in consumer loan funding and a 21% increase in first mortgage funding over the prior year. Total loans outstanding as of September 30, 2004, were \$214,592,164, an increase of 13% over the prior year.

The credit union's Residential Lending Department and Consumer Loan Department continued to take advantage of the strong Sacramento area real estate market by increasing marketing efforts to attract new first and second mortgage borrowers. To manage the interest rate risk associated with holding fixed rate first mortgage loans, the credit union routinely sells these mortgages to a number of investors, including CUNA Mutual Mortgage Company, Country Wide Mortgage Company and the Federal National Mortgage Association.

While loan volumes increased during the period, the overall quality of the loan portfolio continues to remain strong. Loan charge-offs net of recovery were 0.78%, a reduction from the previous year.

<u>Loan Type</u>	<u>Percent of Portfolio Mix</u>	<u>September, 2003</u>	<u>September, 2004</u>	<u>Percent Change</u>
Secured	52.95%	\$103,635,136	\$113,633,603	9.65%
VISA	2.49%	\$ 4,988,848	\$ 5,333,963	6.92%
Signature	0.51%	\$ 1,996,797	\$ 1,087,145	(4.56%)
Mortgage*	44.05%	\$ 78,519,557	\$ 94,537,453	20.40%
Total	100.0%	\$189,140,338	\$214,592,164	13.45%

*Does not include loans sold to investors.

Submitted by: Jim Kelly
 Vice President, Lending



Supervisory Committee Report

McGladrey & Pullen, LLP, Certified Public Accountants, were retained to perform the 2004 annual audit of the credit union's financial statements. Their examination included a study and evaluation of Sacramento Credit Union's accounting systems, procedures, internal controls and other auditing procedures sufficient to provide assurance that the financial statements are accurate.

The comparative highlights from the credit union's audited financial statements for the 12 month period ending September 30, 2004, are as follow:

Key Financial Performance Comparison Fiscal Year Ending September 30, 2004

<u>Performance Category</u>	<u>September 2004</u>	<u>September 2003</u>	<u>\$ Change</u>	<u>% Change</u>
Assets	\$285,925,484	\$277,054,160	\$ 8,871,324	3.2%
Net Loans	\$205,924,548	\$186,035,633	\$19,888,915	10.7%
Member Deposits	\$253,868,943	\$248,564,590	\$ 5,304,353	2.1%
Net Capital	\$ 30,284,685	\$ 27,150,881	\$ 3,133,804	11.5%
Asset Yield	\$ 13,318,483	\$ 14,975,027	(\$ 1,656,544)	(11.1%)
Less Cost of Funds	\$ 3,451,525	\$ 4,512,117	(\$ 1,060,592)	(23.5%)
Gross Spread	\$ 9,866,958	\$ 10,462,910	(\$ 595,952)	(5.7%)
Less Net Operating Expense	\$ 5,233,311	\$ 5,694,632	(\$ 461,321)	(8.1%)
Less Provision Bad Debt	\$ 1,499,843	\$ 1,561,194	(\$ 61,351)	(3.9%)
Net Income per NCUA	\$ 3,133,804	\$ 3,207,084	(\$ 73,280)	(2.3%)

The Supervisory Committee meets periodically with management and independent accountants to review the work of each and to satisfy itself that each person properly discharges his or her responsibilities.

Additionally, the Committee has reviewed and examined various internal credit union policies and procedures throughout the year. It is the opinion of the Committee that Sacramento Credit Union properly discharges its financial responsibilities and that it has continued its growth and development as a solid financial institution.

Submitted by: Edward Lambert
Chairperson, Supervisory Committee



LOCATIONS

Elk Grove **9160 East Stockton Boulevard, #120**

Fair Oaks **8100 Madison Avenue**

Sacramento **800 H Street**

3660 Bradshaw Road

2255 Watt Avenue, #10