Sacramento Credit Union

Invest in Sacramento

2012

ANNUAL REPORT

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SACRAMENTO
CREDIT UNION
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Board of Directors' and President's Report

In 2012 Sacramento Credit Union returned to pre-recession levels of strong financial performance as the capital position rose well above industry averages. Despite the headwinds of the Great Recession, timely and appropriate steps were taken to control expenses and manage credit and interest rate risk. The credit union bounced back with record earnings of over $4 million, the majority of which was attributed to the stellar performance of the first mortgage lending program and the reduction in the allowance for loan and lease loss. The credit union continued to provide innovative services to the membership and maintain strong member service satisfaction ratings.

Positive growth was realized in the consumer loan portfolio without sacrificing credit quality, and significant inroads were made in the commercial lending market. SCU partnered with Small Business Administration providers to offer SBA loans to the member base. A business development officer was added to develop and serve the commercial segment. It is anticipated that commercial lending will grow to diversify the lending portfolio. The Permanente Medical Group (TPMG) is a segment of SCU's membership. In the Northern California Region, SCU has consistently earned over 80% of the TPMG financing market. Compared to historical performance, overall loan growth was modest. However, through September 30, 2012, Sacramento Credit Union placed among the top ten Northern California credit unions in terms of overall lending.

Last year's record number of online transactions and the introduction of mobile banking at members' request are testaments to redefining the concept of convenience in a transition from branch to electronic delivery channels. At the same time, branch upgrades were accomplished to keep pace with the times. The Elk Grove office was relocated, and the Madison office was updated to better serve the membership. Sacramento Credit Union strives to provide state of the art technology and personal attention through the current branch network.

Regulations implementing the Dodd-Frank Act challenge financial institutions with administrative burdens going forward. Sacramento Credit Union has never engaged in deceptive business practices such as those that led to the country's financial crisis of 2008. The credit union is an advocate of the membership, serving members and delivering products in a conscientious, responsible manner. Although SCU was not at any time out of compliance, it was necessary to devote resources to product and service disclosures to maintain compliance.

The professional staff of the credit union have always been instrumental in the organization's success and were especially so last year. The diligence of both retail and support staff drove the outstanding results in the mortgage loan and financial equities programs. As evidenced by ongoing satisfaction surveys, members rate highly their service experiences with SCU employees. Throughout the recession, staff have remained committed to providing quality member service and working toward the credit union's goals. The Board of Directors and management thank you, the members, and our staff for your loyalty to Sacramento Credit Union.

Submitted by: Mark Norris, Chairperson, Board of Directors, and Jerrold A. Kinlock, President/CEO

Secretary-Treasurer's Report

Audited net earnings for fiscal year ended September 2012 were $2,839,418, equivalent to 84 basis points on average assets of $340 million. Figures for the prior fiscal year were, respectively, $1,226,760 or 37 basis points on average assets of $330 million. Fiscal year average return on equity (net worth) was 7.17%, more than twice the 3.23% recorded for the prior fiscal year. Growth in net worth again outpaced growth in assets.

Growth in general was moderately positive across 2011 - 2012. Average deposits grew 3.45% and assets 3.76%. After several years of receding, average loans were up 2.77%. Apart from the 7.17% increase in net worth, the next largest source of growth was in surplus funds, which grew 4.23% but were deployed at rates of return under 1.00%.

Disappointingly, the average ratio of loans to assets did not increase, instead ranging between 36.50% and 38.40%. This comes as no surprise given the weak economy plus nationwide consumer focus on saving, shedding debt and rebuilding credit worthiness.

With growth in surplus funds outpacing loans and with the growth in each put on the books at ever lower yields, average yield on assets averaged 248 basis points, down from 272 basis points for 2010 - 2011. As in recent years, this trend was partially offset through cutting cost of funds, which averaged 30 basis points, down from 46 basis points. As a result, net interest margin, or asset yield less of cost of funds, averaged 218 basis points, down from 226 basis points.

The road to the well received 84 basis point net earnings figure was lined with sturdy performance across the other three components of the financial formula: operating expense, provision for bad debt, and fee and other income. The line was held on operating expense, which declined 0.82% from $10,351,374 (313 basis points) to $10,266,026 (302 basis points). Compared to prior year provision for bad debt of $1,731,780 (52 basis points), the 2011 - 2012 provision of $962,608 (28 basis points) reflects improved credit quality. Loans delinquent over 60 days averaged 40 units at 0.63%, down from 54 and 1.00%. Charged-off loans decreased to 106 loans from 131 and to $1,696,295 from $2,326,491. Bankruptcies dropped from 46 loans to 41. The allowance for loan and lease loss was trimmed 10.00% from $4,135,453 to $3,720,621. Fee and other income grew 14.00% from $5,839,504 (176 basis points) to $6,671,980 (196 basis points). Central to this trend was continued success in generating mortgage origination fee income. Sold mortgage loans increased to 345 units from 313 and to $69,473,389 from $60,610.720. Also contributing to ROA were interchange income, financial services income and exception item fee income relating to automated clearing house, share draft and electronic funds transfer transactions.

Submitted by: Jan Reeves, Secretary-Treasurer, Board of Directors

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Lending Report

In fiscal year 2012 the loan portfolio increased, growing by 3.04%. This continued a trend of growth in the portfolio for the second year in a row. Two major loan portfolios, fixed second mortgages and second mortgage home equity lines of credit (HELOCs) continued to recede by 20% and 4%, respectively. These decreases were attributed primarily to early pay offs and a reduction in new production for second mortgages. The secured portfolio (Other Secured) continued to perform remarkably well with growth of 24%. The loan portfolio experienced significant growth in the unsecured, commercial and loan participation segments, collectively adding $5,590,357 to the portfolio.

Loan Type	Portfolio Mix	September 30, 2012	September 30, 2011	Variance
Unsecured	11.1%	$ 14,399,280	$ 11,376,260	26.57%
Vehicle	22.9%	$ 29,649,420	$ 29,407,167	0.82%
Other Secured	17.8%	$ 23,160,440	$ 18,604,771	24.49%
Commercial	1.9%	$ 2,419,797	$ 1,475,758	63.97%
Second Mortgage HELOC	13.0%	$ 16,945,862	$ 17,581,308	(3.61%)
Second Mortgage Fixed	18.1%	$ 23,567,253	$ 29,367,641	(19.75%)
First Mortgage	11.0%	$ 14,258,605	$ 14,374,065	(0.80%)
Participation	4.2%	$ 5,474,851	$ 3,851,552	42.15%
Total	100.0%	$129,875,507	$126,038,522	3.04%

New loan production experienced strong growth which was due primarily to increased loan originations in the sold first mortgage and the indirect vehicle segments. Production in these segments increased 33% and 150%, respectively. Increased first mortgage production can be attributed to stable rates, high demand for home loans and a continued focus on first mortgage originations. The increase in indirect vehicle production was due in large part to a stronger focus on dealer relationships, as well as an improved delivery channel. SCU experienced significant declines in production in the credit card and second mortgage segments. Weak demand for both credit cards and second mortgages contributed to the decline in production from the previous year. As in prior years, first mortgages were primarily committed to secondary market investors to limit interest rate risk exposure, as well as generate non-interest income.

Loan Type	Production Mix	September 30, 2012	September 30, 2011	Variance
Credit Card	1.8%	$ 2,041,233	$ 3,526,016	(42%)
Other Unsecured	2.2%	$ 2,444,072	$ 2,154,560	13%
Vehicle Indirect	6.7%	$ 7,449,788	$ 2,977,711	150%
Vehicle Retail	8.9%	$ 10,031,167	$ 9,117,086	10%
Other Secured	8.3%	$ 9,316,092	$ 8,997,909	4%
Second Mortgage HELOC	1.9%	$ 2,066,906	$ 2,389,178	(13%)
Second Mortgage Fixed	1.0%	$ 1,105,300	$ 1,403,535	(21%)
1st Mort-Orig & Sold	63.5%	$ 71,192,737	$ 53,554,009	33%
1st Mort–Orig & Portfolioed	2.6%	$ 2,963,800	$ 5,799,416	(49%)
Commercial	0.9%	$ 990,250	$ 0	0%
Participation	2.2%	$ 2,496,222	$ 3,500,000	(29%)
New Loan Production	100.0%	$112,097,567	$ 93,419,420	20%

Submitted by: Blake B. Cairney, Vice President, Lending Operations

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Supervisory Committee Report

McGladrey LLP, a licensed CPA firm, was retained to perform the 2012 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, 2012, are as follows:

Key Financial Performance Comparison Fiscal Year Ending September 30, 2012

Performance Category	September 2012	September 2011	Variance	
Assets	$354,452,556	$341,572,068	$ 12,880,488	3.77%
Net Loans	126,382,517	122,087,392	4,295,125	3.52%
Member Deposits	309,223,368	300,207,424	9,015.944	3.00%
Net Capital	41,243,064	38,403,646	2,839,418	7.39%
Interest Income	8,417,596	8,995,792	(578,196)	(6.43%)
Less Cost of Funds	1,021,524	1,525,382	(503,858)	(33.03%)
Net Interest Margin	7,396,072	7,470,410	(74,338)	(1.00%)
Less Provision for Bad Debt	962,608	1,731,780	(769,172)	(44.42%)
Add Non-Interest Income	6,671,980	5,839,504	832,476	14.26%
Less Operating Expenses	10,266,026	10,351,374	(85,348)	(0.82%)
Net Income	$ 2,839,418	$ 1,226,760	$ 1,612,658	131.46%

The Supervisory Committee meets periodically with management and independent accountants to review the work of each and to satisfy themselves that each person properly discharges his or her responsibilities. Additionally, the Committee reviews and examines various credit union internal policies, internal controls and procedures throughout the course of the year to ensure that members' assets are protected.

Submitted by: Remie Diva, Chairperson, Supervisory Committee

SACRAMENTO
CREDIT UNION

LOCATIONS

Elk Grove	**8351 Elk Grove Boulevard, Suite 600**
Fair Oaks	**8100 Madison Avenue**
Sacramento	**3660 Bradshaw Road**
	800 H Street
	3045 Arden Way, Suite 200
	Kaiser Hospital, 6600 Bruceville Road