LIETUVOS BANKAS
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Review of the Activities of Credit Unions and the Central Credit Union of Lithuania

4th Quarter of 2014

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Credit unions. As of 1 January 2015, 74 credit unions operated in Lithuania, with a total membership of nearly 150 thousand. As at the end of the previous quarter, 63 credit unions were members of the Lithuanian Central Credit Union (LCCU), 11 were not its members.

In Q4 2014 the assets of credit unions grew by 6.8 per cent (as compared to the data as of 1 January 2014, they contracted by 0.6%) and amounted to LTL 2.1 billion (EUR 617.2 million) as of 1 January 2015. The major contribution to asset growth stemmed from an increase in the deposits of credit union members.

Dynamics of some performance indicators of the system of credit unions

Seq. No	Indicator	Amount				Change Q4 2014, %	Change over a year (%)
		01-01-2014 LTL millions	01-10-2014 LTL millions	01-01-2015 LTL millions	01-01-2015 EUR millions		
1.	**Assets**	**2,144.2**	**1,994.9**	**2,131.1**	**617.2**	**6.8**	**–0.6**
2.	Money	16.9	12.7	17.4	5.1	37.3	3.3
3.	Funds with banks	30.4	19.0	42.5	12.3	2.3 t.	39.8
4.	Funds with the LCCU	292.2	227.1	297.7	86.2	31.1	1.9
5.	Government securities (GS)	646.1	721.9	763.4	221.1	5.8	18.2
6.	**Loans granted**	**1,027.6**	**925.5**	**910.1**	**263.6**	**–1.7**	**–11.4**
7.	Specific provisions for loans	63	40.6	59.5	17.2	46.6	–5.6
8.	Ratio of specific provisions for loans to loans (%)	5.8	4.2	6.1	6.1	–	–
9.	Debt to the LCCU	62.6	80.1	64.2	18.6	–19.9	2.6
10.	**Deposits**	**1,868.1**	**1,698.6**	**1,847.1**	**535.0**	**8.7**	**–1.1**
10.1.	Of members and associated members of credit unions	1,855.8	1,688.6	1,837.4	532.1	8.8	–1.0
11.	**Share capital**	**208.7**	**174.8**	**177.6**	**51.4**	**1.6**	**–14.9**
12.	Profit (loss) for current year	–39.4	10.3	4.3	1.3	–	–

The change in the composition of credit union assets was marginal both in the reporting quarter and over the year. Loans granted to members (LTL 910.1 million, or EUR 263.6 million) represented the largest share of the assets of credit unions (42.7%); they contracted by 1.7 per cent over the reference quarter. The contraction in the loan portfolio resulted from an increase in specific provisions in the reference quarter. While the loan portfolio contracted, according to the data of submitted reports, new loans were issued in Q4 2014 — credit unions granted housing loans and financed business. As a result, the loans granted to legal persons increased to LTL 224 million (EUR 64.9 million) over this quarter, while their share, which was decreasing from 2013, grew by 0.7 p. p. in this quarter and accounted for 24.6 per cent of total loans as of 1 January 2015.

The loans granted in the reference period impaired; therefore, the increased demand for specific provisions determined growth in the loan impairment costs. The specific provisions formed by credit unions boosted by 46.6 per cent over the above-named period, while their ratio to loans — by nearly 2 p. p. (to 6.1%). The share of non-performing loans in the credit unions' loan portfolio expanded. **The growing losses of credit unions due to bad loans and the deteriorating indicators defining the loan portfolio quality of the system of credit unions suggest that they must pay particular attention to the accumulation of capital sufficient to ensure stability of the operations of credit unions.**

Credit unions continued to invest in long-term GS using the funds of attracted deposits, in which deposits with 12 month maturity account for the largest share, for that purpose. Credit unions' investment in GS rose by 5.8 per cent — to LTL 763.4 million (EUR 221.1 million) in the reporting period and accounted for 35.8 per cent of credit union assets as of 1 January 2015. It should be noted that credit unions, after investing in the GS of European Union Member States and European Economic Area countries for two consecutive years, in the reporting period again more actively invested in the GS of the Republic of Lithuania. The Republic of Lithuania GS portfolio, after expanding by more than 7 per cent — to LTL 441.1 million (EUR 127.8 million) in Q4 2014, on 1 January 2015 accounted for 57.8 per cent of credit unions' total investment in GS, or by 0.8 p. p. more than at the beginning of the quarter. It should be noted that credit unions, in investing in GS, ensure high liquidity, as, with an unfavourable turn in the circumstances or a need to hold larger volumes of resources for the discharge of liabilities, they would be able to obtain these funds by selling their GS; however, given their relatively large investment in long-term and low investment grade securities, they assume the counterparty and market risk. Therefore, the Bank of Lithuania is going to apply individual supervisory and prudential measures for credit unions that aggressively invest in GS. Moreover, the Bank of Lithuania, in implementing the provisions of the Law on Credit Unions on investment in government securities, is preparing the Regulations on Credit Union Investment in Non-equity Securities. They are to lay down the requirements for the investment of temporarily spare funds, valuation of the investment portfolio and securities.

Although credit unions increased their investment in GS, with the growth of deposits, their funds with banks and the LCCU increased in the reporting quarter and accounted for 16 per cent of the credit unions' total assets at the end of the quarter.

Credit unions, although marginally, but continued to cut their deposit rates in the reporting quarter. According to the data of submitted reports, most credit unions, at the end of the quarter, offered depositors annual interest rates not above 1.6 per cent for the most popular deposits, i.e. those with a 12 month maturity in national currency (at the beginning of the year, most credit unions paid 1.5–2.5% on these deposits). Despite the cutting of deposit rates, as was mentioned before, deposits with credit unions rose. According to the data of submitted reports, in Q4 2014 the deposit portfolio expanded by 8.7 per cent and stood at LTL 1.8 billion (EUR 535 million) on the reporting date, a decrease of 1.1 per cent from a year ago. The growth in deposits is likely to have been triggered by the approaching adoption of the euro, since demand deposits grew more than time deposits, while their share expanded by more than 3 p. p. — to 22.6 per cent of deposits. The deposits of natural persons continued to account for the largest share of deposits (97%).

The share capital of credit unions grew marginally in the reporting quarter and, as of 1 January 2015, amounted to LTL 177.6 million (EUR 51.4 million). Amendments to the Law on Credit Unions provide a possibility to increase the capital of a credit union when its members acquire preferred shares.

According to the data of unaudited financial statements, due to the increased loan impairment costs, in the reporting quarter credit unions incurred losses amounting to LTL 6 million (EUR1.7 million); however, their operating result for 2014 is a profit of LTL 4.3 million (EUR 1.3 million) (in 2013 they incurred LTL 39.4 million (EUR 11.4 million) of losses). Those 54 credit unions whose operations were profitable earned a profit of LTL 21.6 million (EUR 6.3 million), while those 20 that operated at a loss incurred losses in the amount of LTL 17.3 million (EUR 5 million). In 2014 credit unions earned 12 per cent more income and had 16.5 per cent less expenses than in 2013. Interest income, which accounted for 60 per cent of total income, was the main source of revenue for credit unions. Income of one-off character, received from securities operations, accounted for a significant share of income (32.7%) — the profit from the securities sold amounted to LTL 37.2 million (EUR 10.8 million), the profit due the change of the value of securities — LTL 10.2 million (EUR 3 million). In some credit unions, income from securities operations accounts for the largest share of their income. Attention should be paid to the fact that some credit unions incur significant expenses through acquisition of disproportionally expensive and doubtful investment consultancy or other services and paying rather high fees to these service providers (periodical, success, for extra consultancy, etc.). These expenses have a negative effect on the capital of credit unions. **Given that, as was also mentioned in the previous reviews, strengthening of capital is one of the central tasks for the sector of credit unions; for the formation of sustainable capital, they must take every measure, including the use of their profit earned.**

According to the data of reports submitted on 1 January 2015, the capital adequacy ratio of credit unions was 22.82 per cent, the liquidity ratio — 69.87 per cent. High quality liquid assets of credit unions stood at LTL 477.6 million (EUR 138.3 million), while their net outflow of cash — LTL 16.1 million (EUR 4.7 million). All credit unions complied with the liquidity ratio on the reporting date, while the capital of one credit union was insufficient to ensure compliance with the capital adequacy ratio; one more credit union was short of high quality liquid assets to cover its net outflow of cash. In addition, seventeen credit unions, which mainly held funds in bank accounts as a reserve necessary for the exchange of litas into euro, did not comply with the maximum exposure to a single borrower ratio. Most credit unions submitted information that they already complied with the prudential ratios in January. To credit unions that have not ensured compliance with prudential ratios, the enforcement measures established in the Law on Credit Unions will be applied.

The working group set up by the Seimas of the Republic of Lithuania continues to develop the concept of Sustainable Operation of Credit Unions. It is aimed to restructure the system of credit unions of Lithuania and create the conditions for effective and sustainable activities of the credit union sector.

The Review of the **Lithuanian Central Credit Union**, due to the changed time limits for the submission of financial statements, will be published together with the updated information on the activities of credit unions based on the data of audited financial statements for 2014.