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CARIBBEAN CREDIT UNION SYSTEM

FINANCIAL VIABILITY

DISCUSSION AND SCENARIO

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FINANCIAL VIABILITY OF THE CARIBBEAN CREDIT UNION SYSTEM

I Key Issues

Four key issues must be addressed by the Caribbean credit union system if financial viability is to be achieved in the coming decade. These are:

- o Institutional development
- o Capitalization
- o Credit union profitability
- o League income structure.

The first issue is directly addressed by the proposed Caribbean Confederation of Credit Unions Regional Development Project, as is the third. Successful implementation of the project will result in technical self-sufficiency of the CCCU's affiliated leagues which in turn will lead to improved management and earnings at the credit union level. Current projections indicate that by the end of the project's first five years, these improvements will result in surplus earnings at the credit union level of approximately $1.1 million.

However, if a true regional system is to develop, these gains must be translated into capitalization at the league and CCCU levels and increased dues and service payments. This will permit the CCCU and its affiliates to mobilize internal share capital for re-lending to credit unions; by the end of f ve years, the CCCU should be able to mobilize internal and external funds for on-lending to leagues. During Phase II of the project, the leadership of the confederation and leagues will address these issues on a territorial and regional basis to design and implement the necessary policies and institutional development programs. These will probably include:

- o Rates and procedures for the capitalization of a given percentage of credit union savings balances in league central finance facilities o Rates and procedures for the payment of a given percentage of league capital into a CCCU capital fund

o Dues assessment and collection systems.

II Financial Self-Sufficiency Strategy

The financial self-sufficiency strategy currently envisioned is a three-stage process:

o First, consolidation, training and increased profitability at the credit union level

o Second, country development grants to enable leagues to provide the services required by their affiliates:

--central finance operations

--management support

--promotional and others

o Third, external support of the CCCU while its service capabilities are developed and a capital base formed.

Income surpluses should begin to appear at the credit union level by project year two; these should be large enough to finance increased dues payments to the leagues by year three. As capital funds are accumulated at the leagues and CCCU, finance margins will become increasingly important elements of their income structure. It is possible that by year ten, the leagues will be in a slight surplus position and the CCCU at break-even.

III Project Funding

Funding of the project should occur in two phases. The first has been outlined in the project proposal. Planning for the second phase and its funding requirements will begin with the major review/assessment scheduled for project year three. At that time, operating results and trends established during the first three years will be analyzed to determine what financial and technical resources will be required after year five. Based on the financial viability scenario discussed below, external funding required to complete the country development grants pending at year five should be about $68,000 and support for the CCCU would total $144,000. In addition, a total of $5 million on loans or grants would be required to fund the CCCU Regional Financial Facility for on-lending to leagues. Thus, total non-credit union movement funding for the Caribbean system would be:

Operating subsidy grants........................	$2,150,397
External capital grants or loans...............	5,000,000
Total....................................	$7,150,397

These amounts are based on the scenario discussed below and represent at best an educated guess of the regional system's development prospects for the next decade.

By way of comparison, investments by USAID in the development of the Latin American Confederation of Credit Unions (COLAC) and its affiliates totaled $15.9 million during the 1962-72 period, including $9.9 million in "soft" loans. USAID operating subsidies to COLAC from 1973 to 1979 have totaled $1.7 million plus a loan of $4 million. Thus total regional funding for the COLAC system has been $21.6 million, not including grants and loans made to COLAC affiliates at the country level since 1972.

IV Possible Financial Viability Scenario

The purpose of this scenario is not to predict how the Caribbean credit union system will develop; rather, it is intended as an illustration of how it might develop if appropriate capitalization and revenue strategies are adopted by the leagues and the CCCU, and the project is successful in improving credit union management and profitability. The following discusses the projections and corresponding assumptions of the accompanying table "Caribbean Credit Union System Possible Financial Viability Scenario."

A. System Base

The levels of savings, loans and assets for 1980-84 are mid-year projections, per the CCCU project proposal, in current dollars at year-end 1978 exchange rates. For the 1985-89 period, the projections are at a lower, linear rate, reflecting uncertainties regarding possible market saturation effects and a potential worsening of the economic environment. Similarly, membership estimates for the 1980-84 period are from the proposal; for 1985-89 the increase per year is decreased by 50% to 21,000.

Capitalization of the league is projected at 5% of total savings balances of affiliated credit unions; purchase of these league capital shares is projected to begin in the fourth quarter of 1980. No external funds are included during the first five years while basic experience in intermediate finance operations is gained. It is, however, probable that external borrowings or grants will be obtained earlier, given the low debt-equity position of the system. Throughout the ten-year period, 80% of available funds are assumed to be lent to affiliates and 20% to be invested in fixed and liquid assets (to meet system stabilization needs). Capitalization of the CCCU Regional Financial Facility is assumed to begin in project year two at a rate of 5% of league capital. All funds are invested during year two, while lending to affiliates is assumed to begin in year three. In the projections, 80% of funds are lent, 20% invested.

External borrowing begins in year six with the net annual increment being $1 million.

B. Credit Unions

Gross income is projected at a rather low level of 7% of assets throughout the period. Increasing efficiency brought about by the project is assumed to be reflected in decreasing expense ratios; accordingly the ratio of gross expenses to assets is projected to decline from 3.6% in year one to 3.1% in year five and then remain constant. As a result of this increased profitability, combined with system growth estimates, net income is projected to increase from six to sixteen million dollars at the credit union level. Dividends are assumed to be constant at 3% of overall savings balances throughout the decade. Surpluses will begin in year two and increase to $1.1 million by 1984. These net earnings are expected to fund the deficits projected at league level as new dues and fee schedules are implemented.

C. Leagues

Dues and services income to CCCU affiliated leagues is projected on the basis of their pre-existing income structure (largely of Jamaica, Trinidad and Tobago and Surinam), including finance margin earnings; annual increases are projected at 10%. The finance margin income projected in the scenario represents additional earnings derived from the capitalization program described above, with funds lent and invested by the leagues at an average spread of 1.2% External assistance to leagues is projected for years six and seven to complete pending country development grant projects.

Expenses are projected on the basis of the pre-existing cost structure plus increased dues to CCCU and the higher expense levels entailed by the country development grants. League costs are estimated to increase at a yearly rate of 14% during years one through five, decreasing to 7% for the remainder of the period as efficiencies are achieved. The deficits shown would be financed out of increased dues and service fees charged to affiliates; they would of course be charged as expense items at the credit union level, which would decrease the surpluses shown. This was not done in this scenario to show more clearly both the need for and potential magnitude of, such increased charges. The specific needs for increased dues and service charges will be determined on a league-by-league basis during phase II of the project.

D. CCCU

Income from dues and services during years one through three is estimated at the current rate of TT$0.16 per member (US$0.07). This is changed from the project proposal, where dues were estimated at US$.16 per member. Accordingly, there are initial deficits which will need to be addressed through cost-cutting and/or obtaining additional revenues. Although the dues rate is assumed to increase in year four (the CCCU has established a policy of reviewing its dues structure and making necessary changes every three years) to an annual rate of US$0.12 per member, deficits will still be experienced during the last two years of the project. In the last five years of the scenario, deficits are shown implicitly as the value of external assistance. In 1986 dues are assumed to increase again to a level of US$0.16 per member.

Finance margin income is estimated to begin in year two. It is calculated on the basis of a 1% spread on combined loans and investments through 1984. From 1985 to 1989 the spread is projected to increase to 2% due to economies of scale and the possible acquisition of concessional credits.

CCCU expenses are projected on the basis of required service levels as estimated in the project proposal for years one through five. During the 1985 to 1989 period operating costs are projected to increase at an annual rate of 7%.

CARIBBEAN CREDIT UNION SYSTEM POSSIBLE FINANCIAL VIABILITY SCENARIO
1980-1989
(US DOLLARS)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
I System Base										
Credit Unions(1)										
Membership	403	444	485	526	567	588	609	630	651	672
Savings	151,000	193,000	243,000	299,000	362,000	422,000	478,000	533,000	539,000	644,000
Loans	157,000	205,000	261,000	324,000	395,000	467,000	529,000	590,000	652,000	714,000
Assets	174,000	222,000	278,000	341,000	411,000	481,000	545,000	608,000	672,000	736,000
Leagues(2)										
Capital Funds	1.9	9.7	12.2	15.0	18.1	21.1	23.9	26.7	29.5	32.2
External Funds	-0-	-0-	-0-	-0-	-0-	1.7	2.6	3.4	4.4	5.3
Loans Outstanding	-0-	7.7	9.8	12.0	14.5	18.2	21.2	24.1	27.1	30.0
Investments	1.9	2.0	2.4	3.0	3.6	4.6	5.3	6.0	6.8	7.5
CCCU(2)										
Capital Funds	-0-	0.5	0.6	0.8	0.9	1.1	1.2	1.3	1.5	1.6
External Funds	-0-	-0-	-0-	-0-	-0-	1.0	2.0	3.0	4.0	5.0
Loans Outstanding	-0-	-0-	0.5	0.6	0.7	1.7	2.6	3.4	4.4	5.3
Investments	-0-	0.5	0.1	0.2	0.2	0.4	0.6	0.9	1.1	1.3
II Credit Unions (2)										
Gross Income	12.2	15.5	19.5	23.9	28.8	33.7	38.1	42.6	47.0	51.5
Expenses	6.2	7.5	9.2	10.9	12.8	14.9	16.9	18.9	20.8	22.8
Net Income	6.0	8.0	10.3	13.0	16.0	18.8	21.2	23.7	26.2	28.7
Reserves	1.5	2.0	2.6	3.3	4.0	4.7	5.3	5.9	6.5	7.2
Dividends	4.5	5.8	7.3	9.0	10.9	12.7	14.3	16.0	17.7	19.3
Surplus	-0-	0.2	0.4	0.7	1.1	1.1	1.6	1.8	2.0	2.2
III Leagues(1)										
Income										
Dues&Services	526	579	637	701	771	848	933	1,026	1,129	1,242
Finance Margin	19	102	130	159	192	274	318	361	407	450
External Assistance	137	207	170	135	92	46	22	-0-	-0-	-0-
Total Income	682	883	937	995	1,055	1,168	1,273	1,387	1,536	1,692
Total Expenses	686	880	970	1,067	1,174	1,256	1,344	1,438	1,539	1,647
Surplus(Deficit)	(4)	8	(33)	(72)	(119)	(88)	(71)	(51)	(3)	45

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
IV CCCU(1)										
Income										
Dues&Services	28	31	34	63	68	100	129	136	143	150
Finance Margin	-0-	5	6	8	9	42	64	86	110	132
External Assistance	108	106	123	120	110	73	37	24	10	-0-
Total Income	136	142	163	191	187	215	230	240	263	282
Total Expenses	172	177	201	204	201	215	230	246	265	282
Surplus(Deficit)	(36)	(35)	(38)	(13)	(14)					

Notes: (1) Figures in thousands.
(2) Figures in millions.