

## **Portfolio Update**

As of 11/30/2008

The credit and liquidity crisis that began in July 2007 continues to strain global financial markets. Members United is committed to providing our member-owners information about these market events and the quality of our assets. We strive to provide objective, transparent information and data regarding our safety and soundness. While credit and liquidity events continue to foster market instability, we remain confident in the quality and continued strength of Members United's portfolio and in our ability to provide liquidity to members. In addition to this *Portfolio Update*, financial statements are published monthly for your review (available at [www.membersunited.org](http://www.membersunited.org)).

This report focuses on three primary risks within Members United's investment portfolio: interest rate, credit and liquidity risks. Members United has developed the infrastructure, expertise and capability to manage a complex balance sheet, and our intent is to share our position related to these key risk attributes, as well as guidance on how we monitor and report these positions.

### **Economic Overview**

Our three-tiered economic barometer continues to forecast stormy economic weather ahead. Of the three key indicators, mortgage/housing markets, employment conditions and equity values, the first two continue to show marked weakness while the third has demonstrated some recent surprising stability.

As we look at most measures of the housing market we continue to see weakness. On the mortgage side, delinquencies, foreclosures and defaults for sub-prime, Alt-A and even prime loans have been increasing. Many lenders have resorted to loan modifications to ease the payment burden on borrowers. However, in most instances the modifications have not been of material effect, as they have only modestly reduced payment obligations without significant debt forgiveness. The result has been continued weak performance. One survey estimates as many as 59 percent of modified loans end up in default within nine months. However, for modifications with at least a 20-30 percent decrease in payments, this statistic fell almost in half. This makes intuitive sense as relatively small changes in payments provide limited incentive for borrowers to continue to struggle with underwater loans (i.e., when mortgages are greater than the value of the property).

The employment picture also remains challenging. The unemployment rate continues to rise and reached a new high-water mark of 6.7 percent in November. Other employment statistics remain equally bleak, with non-farm payrolls declining for the 11<sup>th</sup> straight month and down 533,000 in November. Initial jobless claims also were very weak, posting an increase of more than 500,000 for five consecutive weeks. With a weak employment market and outlook for jobs, it is likely consumers will re-trench and consumer spending will remain weak. Initial signs show that consumers are spending less this holiday season and looking for deeper discounts on purchases.

Our one positive indicator comes from the equity markets. After penetrating the 8,000 mark on the Dow and trying to test cycle lows near 7,400, the Dow has been holding support at just over the 8,000 mark once again. While consumer sentiment has been negatively affected by the Dow's decline from its 14,000 high, it is important to note the market has held its own, even through the turmoil surrounding the future of the big three automakers. The monumental Fed action reducing the target Fed funds rate to 0% to .25% sparked another stock rally with the Dow approaching the 9,000 mark and further supporting a floor in values, at least for now.

## Members United Outlook

The Federal Reserve Bank has done much to provide liquidity and monetary easing to stimulate the current market. However, moving rates lower is now not an option, and the impact of moving rates from 1% to .25% or 0% is likely to be minimal – except as a strong signal of the Fed's determination. Fiscal and tax policy changes are necessary to move the economy forward. Infrastructure development and plans that support housing values and encourage homeowners to stay in their homes are critical. The new administration is already looking at these and other tools to re-start our economy in advance of taking office in January. However, it will take time for these programs to deliver results. Consumers still need to increase savings and reposition their balance sheets, and consumer spending will remain at subdued levels in contrast to the exuberance of the last few years. However, the seeds of recovery are already, or likely soon to be, planted.

## Portfolio Overview

Members United's portfolio is comprised of highly rated securities and depository obligations issued by U.S. Central Federal Credit Union, all of which we purchase according to tightly defined guidelines. As of November 30, 2008, Members United's investment portfolio, including deposits at U.S. Central, was approximately \$6.9 billion.

While there are numerous forms of risk associated with any type of investment and overall portfolio management, this report will focus on three key risk types: credit risk and interest rate risk in both net interest income (NII) and net economic value (NEV), and liquidity risk.

### Credit Risk

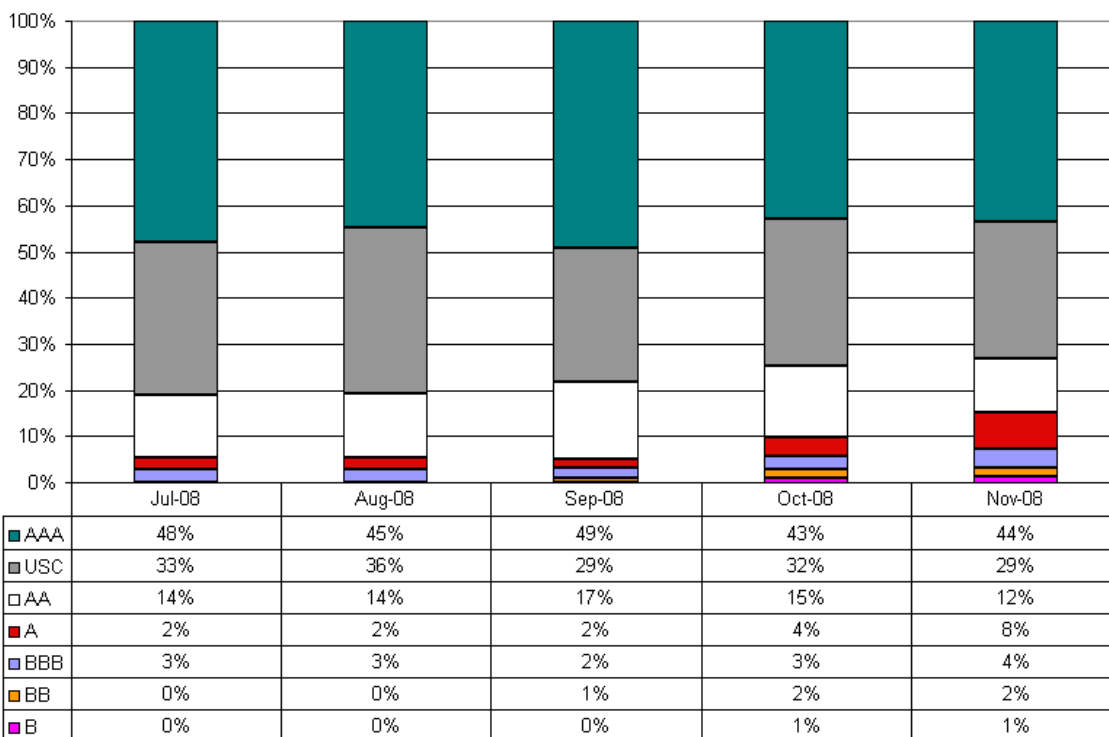
Credit risk is the risk that the par value of an investment will not be returned (fractionally or as a whole). Members United manages credit risk through:

- a diligent pre-purchase review and analysis of all investment securities
- continual monitoring of ongoing credit metrics
- diversification of investments
- reviewing credit grades from primary rating agencies

Members United has the regulatory authority to invest and hold investment securities with a rating of BBB or better. If an investment held by the corporate falls below BBB, an investment action plan must be prepared (and filed with the NCUA) to demonstrate the anticipated performance of the security and any exposure to future cash flows (periodic interest and principal payments).

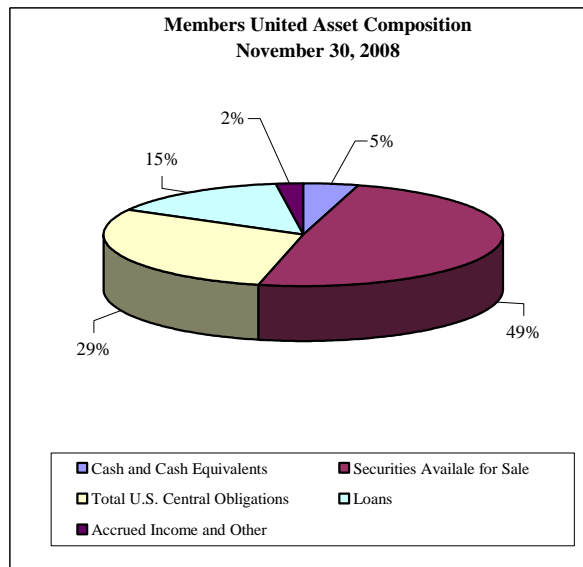
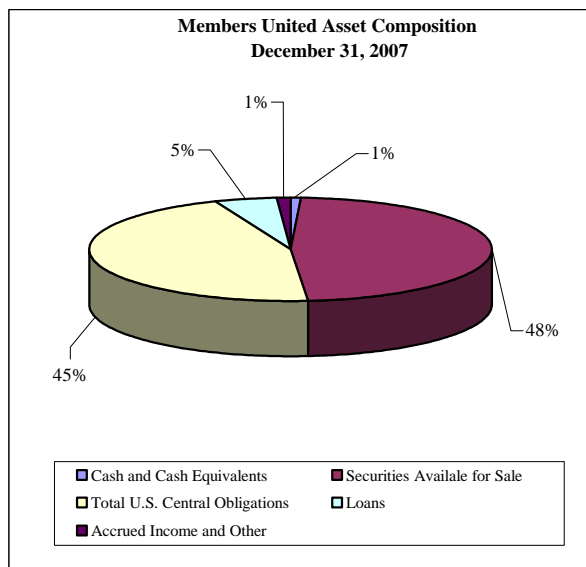
Since the beginning of this credit and liquidity crisis and after tens of thousands of ratings downgrades from the rating agencies, the rating of 343 of the 513 investment securities in Members United's diversified portfolio remain unchanged. During November 2008, 27 bonds were downgraded for the first time. Currently, we have nine bonds wrapped by FGIC, totaling \$150.3 million, which have ratings below BBB (the minimum acceptable level to be held in our investment portfolio). In addition, three bonds wrapped by Syncora Guarantee Inc. (formerly XL Capital Assurance Inc.) totaling \$37.8 million have ratings from two agencies that are below BBB. Management is finalizing its investment action plan and continues to monitor these bonds closely. The following chart provides the ratings trends on Members United's investment holdings since July 2008.

### Portfolio Ratings Trends



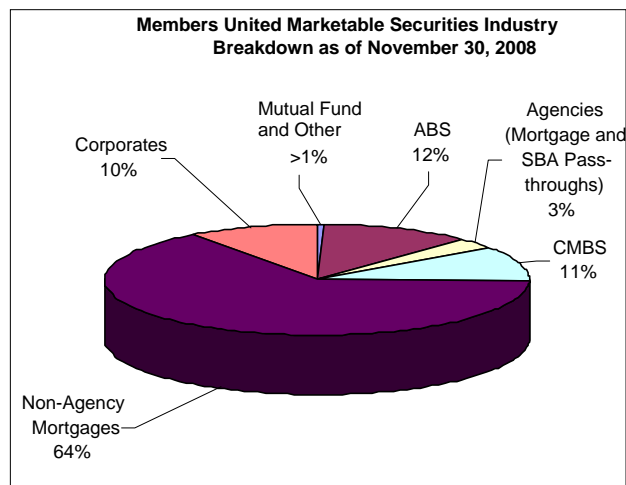
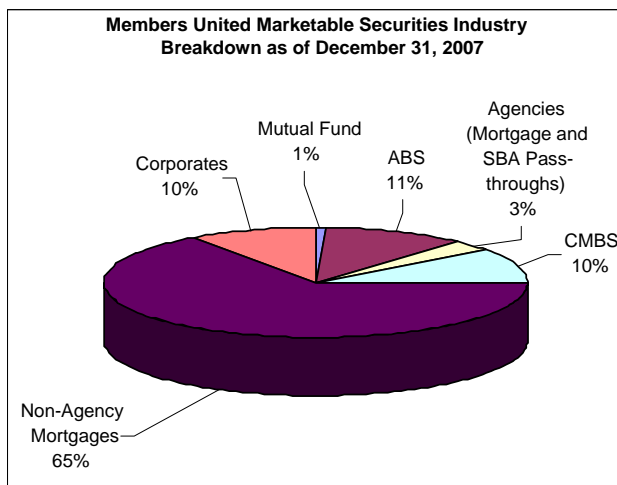
### Asset Composition

As of November 30, 2008, our assets were \$8.8 billion. Marketable securities represented \$4.3 billion, and outstanding loans totaled \$1.3 billion. Deposits at U.S. Central totaled approximately \$2.6 billion.



## Industry Composition

Members United's industry composition has remained relatively stable since fiscal year-end 2007, with no category changing by more than 1 percent, as noted in the graphs below.



## Total Investment Portfolio

The table below summarizes Members United's total available-for-sale securities, by category, as of November 30, 2008:

(All dollars are reflected in thousands)

	Par Value	Unrealized Loss*	Fair Value
Non-agency mortgages	\$ 3,991,946	\$ (1,463,313)	\$ 2,528,633
Asset-backed securities (secured by non-mortgage assets)	729,679	(93,919)	635,760
Commercial mortgage-backed securities	661,880	(257,328)	404,552
Corporates	606,699	(86,176)	520,523
Agencies (mortgage and SBA pass-throughs)	185,556	(3,094)	182,462
Mutual fund and other	27,590	-	27,590
Total investment securities	\$ 6,203,350	\$ (1,903,830)	\$ 4,299,520

\*Excludes net unrealized loss on derivative instruments of \$32,219.

## Mortgage-Related Securities

Credit events driven by housing price declines and the resulting impact on mortgages and mortgage-related securities continue to be the most observable risk that investors face. As such, news regarding rising default rates in certain geographic areas, rising rates on adjustable mortgage loans, large bank and broker write-downs, and instances of fraudulent practices by certain originators (and some borrowers) continue to generate headlines. As of November 30, 2008, Members United's investments in non-agency, mortgage-related securities were approximately \$4 billion. The following represents the aggregate mortgage-related holdings:

(All dollar amounts are reflected in thousands.)

Mortgage Portfolio Category	Dollar Amount Outstanding
Total Non-Agency Mortgage Exposure	\$3,991,946
Prime	1,194,906
Sub-prime (FICOs < 680)	1,046,268
Alt-A	1,750,772

Many of the risks associated with mortgage-related securities have been highlighted in the sub-prime market. However, Members United monitors other sectors within the mortgage arena that have similar performance characteristics. The following provides a high-level summary of Members United's mortgage-related holdings as of November 30, 2008:

<b>Mortgage Portfolio Statistics</b>	<b>Prime</b>	<b>Alt –A</b>	<b>Sub-prime</b>
Percent of non-agency, mortgage-related securities	30%	44%	26%
Percent of total investments	17.4%	25.5%	15.4%
Weighted average FICO score	725	708	632
Weighted average loan to value	78%	79.3%	83%

### Monolines

A component of the credit quality of structured finance investment vehicles is the credit enhancement available to protect the investor from loss of principal or interest. A common method of providing credit enhancement for these investments is to use an insurance "wrap" from a monoline insurer, which writes a single line of insurance contracts. A monoline insurer is a financial risk insurance company that specializes in insuring bond issues, including municipal bonds, residential mortgage-backed securities (RMBS) and asset-backed securities (ABS). A "monoline wrap" is a guarantee covering the timely payment of interest and the ultimate payment of principal.

In recent years, the monoline insurers expanded into insuring credit default swaps (CDS) and collateralized debt obligations (CDO) backed by residential mortgage securities, including those with sub-prime collateral. Members United does not own any CDOs or hold any CDS contracts.

As the credit markets deteriorated and the sub-prime crisis worsened, these insured portfolios recognized large unrealized losses. Most of these wrapped obligations are synthetic structures, resulting in inconsistent valuations through the use of multiple valuation models by the insurance entities, the rating agencies and brokerage houses. These unrealized losses affected the monoline insurers' capital ratios, making it more difficult to support 'AAA' ratings.

Members United has exposure to these insurers, through securities that have monoline insurance, in addition to the underlying collateral supporting the respective securities. The following table provides a brief overview of this exposure:

(All dollar amounts are reflected in thousands.)

<b>Monoline</b>	<b>November 30, 2008 Total Holdings Wrapped</b>	<b>November 30, 2008 Total Holdings Wrapped (% of Investments)</b>
<b>Ambac</b>	\$454,006	6.6%
<b>MBIA</b>	432,715	6.3%
<b>FGIC</b>	196,247	2.9%
<b>FSA</b>	101,561	1.5%
<b>SGI (f.n.a. XLCA)</b>	58,393	0.8%
<b>CIFG</b>	15,586	0.2%
<b>Total</b>	\$1,258,508	18.3%

Most of Members United's holdings are in the two largest monoline insurers – Ambac and MBIA. Both firms' claims-paying ability and liquidity remain strong. Many of the underlying securities also have additional layers of protection in the form of over-collateralization, subordination and excess interest. The following table illustrates a sector breakdown in which holdings are wrapped.

The structure of an individual trust is important in determining the amount and timing of the monoline payment (if applicable). The insurance policy normally provides an unconditional and irrevocable guarantor of timely payment of interest and ultimate repayment of principal on the final maturity date. The monoline covers funding shortfalls and is not assumed to cover the entire principal balance unless significant economic events warrant this.

## Interest-Rate Risk

Interest-rate risk measures the impact of changing interest rate scenarios on the value of our balance sheet and net interest income. One common measure is NEV, which measures the net change in the value of our assets and our liabilities given changes in interest rates. Members United adheres to NCUA's Rules and Regulations Part 704 and analyzes NEV monthly. We assess the impact of interest rate shocks, from a 300-basis-point decline to a 300-basis-point increase in rates, in 100-basis-point increments. However, we do not model for rates less than zero (currently, the Down 300 and Down 200 scenarios meet this criterion and are suspended). These changes assume an instantaneous and parallel shift of the yield curve – a very aggressive assumption designed to produce a “stress test” of the balance sheet.

Additionally, Members United evaluates the impact on NEV of changes in the shape of the yield curve, prepayment rates, credit spreads and basis risk. Management and ALCO review this information monthly. The chart below demonstrates the NEV impact for November 2008. Given the calculation impact of the unrealized losses (which we continue to believe are largely temporary) creating a base net economic value close to zero, the worst-case scenario (an instantaneous rise in interest rates of 300 basis points) reflects a decline in the NEV by approximately \$1.3 billion. The percentage change calculations are exaggerated due to the base case being so small and are shown as N/A on the chart.

(All dollar amounts are reflected in thousands.)

<b>Net Economic Value</b>			
<b>November 30, 2008</b>			
	<u>Net Economic Value</u>	<u>Dollar Change</u>	<u>Percentage Change</u>
-100 basis point decline in rates	N/A	N/A	N/A
Base net economic value	(1,109,871)	-	-
+300 basis point rise in rates	(1,298,689)	(188,818)	N/A

The valuations reflected in the base NEV calculation continue to be constrained due to the market illiquidity as well as the wider credit spreads that have affected all investors. With the dislocation occurring within the markets, economic vs. market prices are significantly different, and we believe this is a condition that will eventually correct itself. As a footnote, the change in NEV has not resulted from any investment purchase and sale activity, but rather the dislocation in market price valuations. For now, this condition continues to be exacerbated by the high levels of price volatility in the markets. The impact to Members United's NEV computation is compounded by utilizing market pricing (which we believe in this environment fails to capture the true economic value) and the increases in volatility.

An alternative security pricing methodology involves obtaining option-adjusted spread (OAS) quotes on our securities holdings and sectors. In the current marketplace, prices calculated from these OAS quotes do not reflect the same degree of liquidity bias seen in direct price quotes from our regular pricing sources (which reflect market makers not truly interested in bidding for securities except at deep discounts). Members United regularly reviews security pricing service indications to OAS-derived prices. The disparity between such results is currently quite wide.

As can be seen from the table below, the NEV calculations from OAS-derived prices are better compared to the NEV results using security pricing services. By using the OAS spreads, the base case NEV is higher.

This rise in the base case value decreases the percentage changes in the rate shock scenarios. The large disparity in results reflects the difference between the OAS-based model (which is closer to estimated economic value) and current liquidation value in an illiquid and fragmented market.

(All dollar amounts are reflected in thousands.)

<b>Net Economic Value</b>			
<b>OAS – Derived Security Prices</b>			
<b>November 30, 2008</b>			
	<b><u>Net Economic Value</u></b>	<b><u>Dollar Change</u></b>	<b><u>Percentage Change</u></b>
-100 basis point decline in rates	(\$480,947)	\$1,973	- .41%
Base net economic value	(478,974)	-	-
+300 basis point rise in rates	(698,231)	(219,257)	-45.78%

In addition to the NEV risk computations, Members United prepares monthly net interest income (NII) forecasts utilizing the same data to calibrate the modeling of NEV. The following table illustrates Members United's projected NII over the next 12 months. As appropriate with modeling NII and/or NEV, Members United captures the embedded optionality associated with all assets and liabilities.

(All dollar amounts are reflected in thousands.)

<b>Net Interest Income Projection</b>			
<b>November 30, 2008 (12-month projection)</b>			
	<b><u>Net Interest Income</u></b>	<b><u>Dollar Change</u></b>	<b><u>Percentage Change</u></b>
100 basis point decline in rates	\$36,858	\$(4,282)	(10.48%)
Base case NII	40,867	0	0.0%
300 basis point rise in rates	48,466	7,599	18.59%

### Liquidity Risk

Liquidity risk addresses the ability to create liquidity to fund cash flow requirements, both expected and unexpected, which usually result from share withdrawals and member loan requests. Members United maintains a \$310 million committed line of credit and advised lines of credit that total more than \$2 billion. The following table outlines our sources of liquidity:

<b>(All dollars are reflected in thousands)</b>	
<b>Current Liquidity</b>	
Cash and short term deposits at U.S. Central	<b>\$ 1,223,173</b>

Source of Liquidity	Gross	Used	Net
US Central - committed line	\$ 310,000	\$ 310,000	-
FHLB Chicago line of credit	240,000	230,000	\$ 10,000
US Central - advised line	1,439,045	271,700	1,167,345
State of Illinois deposit	100,000	100,000	-
Commercial paper	270,000	268,000	2,000
Available-for-sale securities - sales	1,238,352	-	1,238,352
Available-for-sale securities - borrowings	337,867	254,691	83,176
Fed funds	500,000	15,000	485,000
Term investment option (TIO)	-	-	-
Fed discount window	1,018,254	-	1,018,254
<b>Subtotal</b>	<b>5,453,518</b>	<b>1,449,391</b>	<b>4,004,127</b>
<b>Total</b>	<b>\$ 6,676,691</b>	<b>\$ 1,449,391</b>	<b>\$ 5,227,300</b>
<b>Total member loans</b>	<b>\$ -</b>	<b>\$ 903,029</b>	<b>\$ -</b>

Liquidity has stabilized and looks positive for the remainder of the year. The November ending balances show cash equivalents at about \$1.25 billion. In looking at alternative sources of funding, our USC line and discount window access could supply up to another \$2.1 billion. These combined provide about \$3.3 billion in liquidity sources (ignoring all other sources) in relation to an overnight account of about \$3.25 billion at month end. Our fed funds lines are improving as corporates are one of the few participants with the ability to trade fed funds with the NCUSIF guarantee program. We have seen increased interest in opening new lines based on the guarantee.

The introduction of the Credit Union System Improvement Program (SIP) and Homeowners Affordability Relief Program (HARP) will also provide additional liquidity to the corporate credit union system. The HARP program even goes a step further by providing credit unions an alternative to defray some of the costs of helping homeowners stay in their homes. For qualifying loans, the HARP can defray up to half the costs of loan modifications. These loan modifications can be effective in managing mortgage payments and keep borrowers in their homes and avoid expensive foreclosures.

#### Derivative Positions

Members United is exposed to credit risk on derivative instruments if the counterparty should fail to perform under the terms of the contract. Members United manages credit risk through the use of comprehensive credit-approval processes, the selection of only creditworthy counterparties and effective collateral administration. In addition, Members United requires legally enforceable netting arrangements, which permit netting of transactions with the same counterparty. The amount of credit exposure is limited to the interest receivable and the fair market value of the derivative contracts in gain positions, reduced by the value of any collateral pledged by the counterparty. As of November 30, 2008, there was no credit exposure with our derivative counterparties.

#### **Financial Overview** [rj]11

Members United's net income of \$3.4 million for the month ended November 30, 2008, compares favorably to the \$0.5 million earned for the same period in 2007. On a year to date basis, a net loss of \$20.1 million is primarily due to losses recorded on financial instruments.

Members United recently announced proactive business model changes to better position the corporate to navigate through this uncertain market and to position the company for continued success in the future. These changes will realize operating efficiencies, focus our member service teams on our core markets and preserve member capital. Every day, Members United provides value-added payment and investment products and services to its members, and this will continue. From a financial perspective, operating expenses were higher in

November as costs associated with implementing this plan were accrued; however, savings will begin to be realized as early as December 2008.

The financial crisis continues to pressure the market value of our investments. Unrealized losses totaled \$1.9 billion as of November 30, 2008 – and increase of \$0.3 billion over the prior month. We continue to believe that the unrealized losses represent temporary declines in value, and we intend to hold the securities until they recover in value, which in some cases may mean maturity. All investments, except our Lehman holdings, continue to pay principal and interest.

Liquidity is a primary factor in our ability to hold the investments until they recover in value. Cash and overnight share accounts as of November 30, 2008, totaled \$1.2 billion, unused advised lines of credit totaled \$1.2 billion, and access to the Federal Reserve discount window has been established as a backstop and totaled \$1.0 billion. The NCUA recently announced the SIP and HARP programs, which should only further strengthen the liquidity position.

Capital totaled \$866 million as of November 30, 2008, including \$300 million of reserves and undivided earnings. Members United did not record any permanent impairment charges (OTTI) during the month of November.

We greatly appreciate the continued support from our credit union members who continue to provide us with the liquidity and capital to come through these challenging economic times together.

## **Summary**

Members United has made a commitment to developing a leading investment and risk infrastructure for our members. The combination of expertise, practices, tools and controls should provide assurance to our member-owners that we are well-positioned to navigate through these unprecedented markets. We will continue to provide monthly updates with full transparency in an effort to communicate our portfolio and risk exposure, and to affirm the strong financial position of Members United.

## **Contact Information**

For questions related to any information contained in this update, please contact any of the following individuals:

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