

NAVY FEDERAL CREDIT UNION

2019 Annual Report

OUR MEMBERS ARE
THE MISSION  [®]

To our members and Board of Directors,

This Navy Federal Annual Report describes how the credit union performed in 2019. We typically present the report at our annual in-person meeting in April. However, due to the unexpected arrival of COVID-19 and the need to adhere to social distancing rules, we had to postpone the event.

During this challenging time, we've been able to keep branches open and ensure members have 24/7 service through our website, mobile app, ATM network and call center. Throughout, members have continued to be able to manage accounts, apply for loans, make transfers, seek personal assistance and conduct other transactions. Plus, with our security, card and account notifications, they have more insight into their finances and more money management tools.

The number of members who can attend the rescheduled annual meeting will be limited according to state and federal guidelines and the need to practice social distancing. Although we can't predict precisely how the future economy will look, we're committed to continuing to focus on meeting member needs as we navigate through it together.



Mary McDuffie
President/CEO
Navy Federal Credit Union



John A. Lockard
Chairman
Board of Directors

Vision Statement:

Be the most preferred and trusted financial institution serving the military and their families.



Our
Members
Are the
Mission®

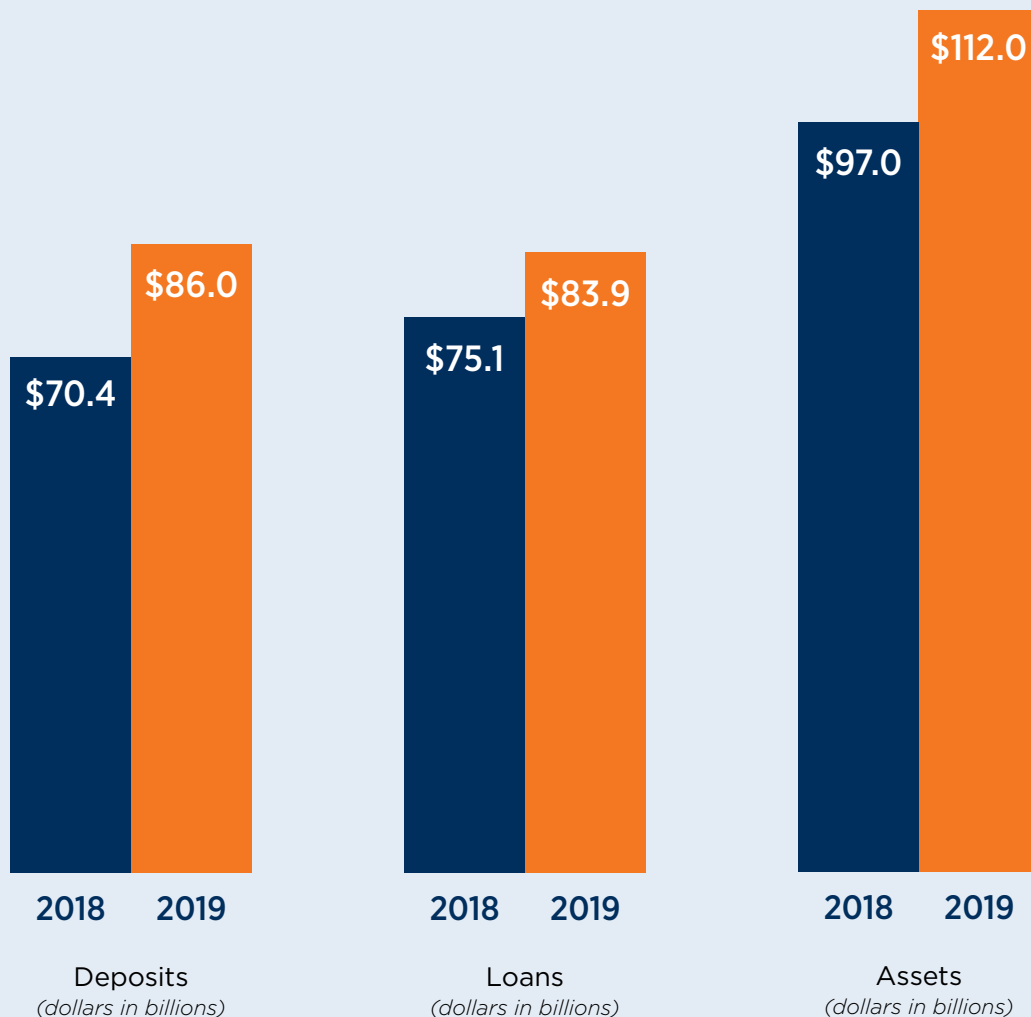
Report of the Chairman and President

Navy Federal Credit Union was founded during a period of tremendous economic crisis, and since 1933, we've weathered all types of financial conditions. Our focus on maintaining strength and stability and providing best-in-class member service has been the hallmark of our success for 86 years. We know that a strong performance during good economic times like we experienced in 2019 and the past few years fuel our ability to invest in our members and our technology in all economic climates. Our members' needs come first, which is why we say, "Our Members Are the Mission."

Financial Summary

As of December 31	2018	2019
<i>(dollars in millions)</i>		
Assets	\$ 96,962.4	\$ 111,986.1
Loans Outstanding	\$ 75,059.2	\$ 83,919.9
Savings, Checking, MMSAs, IRAs	\$ 50,626.6	\$ 56,733.7
Share Certificates	\$ 19,790.9	\$ 29,299.6
Members' Equity	\$ 11,404.7	\$ 13,763.6
Gross Income	\$ 6,818.6	\$ 7,993.2
Non-Interest Expense	\$ 2,844.1	\$ 3,430.8
Dividends	\$ 642.6	\$ 1,016.4
Mortgage Loans Serviced	\$ 68,697.7	\$ 77,307.3
Members	8,232,022	8,959,665

Deposit, Loan and Asset Comparisons



A Solid Foundation

Overall, we saw strong and steady growth last year. Our total assets increased by \$15 billion to \$112.0 billion, and membership increased 9 percent to 9.0 million—249,000 of whom were veterans and their families. We kept our loan and savings rates among the best in the industry, our fees remained low and we offered valuable rebates and discounts. And, both US News & World Report and The Military Wallet recognized us as Best Military Banks and Credit Unions.

Having nearby branches is especially important to those members who want in-person assistance. So, in keeping with our dedication to serving members where they need us, we opened 20 new branches, for a total of 342 worldwide. Many of these new branches were on or near military installations or in areas with a large veteran population. By year's end, branch visits increased 6 percent, reaching 26.5 million.

Partners in Security

Because protecting members' accounts and information continues to be a top priority, in addition to security features already available like 24/7 account monitoring, we offered two more fraud-combatting tools.

2-Step Verification. After entering sign-in credentials, members receive a one-time security code to use as an additional identity verification step. We automatically enrolled all new accounts and rolled out the feature to existing account holders.

Voice ID. Members can now securely access their accounts by phone, through voice identification.

Digital Trends and Support

Our mission is to ensure that members have flexibility in how and when they bank and to make those transactions secure and easy to accomplish. So, in addition to our traditional channels like branches, ATMs and call center, we invested in expanding their digital self-service options, so they can manage their finances remotely. Members responded enthusiastically, with 69 percent of them using a digital channel last year.

Three of our new self-service enhancements are highlighted below.

Electronic signatures. We launched a simple new process to enable members to sign promissory notes for all consumer loans electronically.

Account and security notifications.¹

This popular feature helps members track their spending and account activity and is a significant defense against fraud. They can customize which notifications they want to receive, like security, balance, withdrawal and deposit notifications, and how they want to receive them. We expanded the types of notifications members can set up, and by the end of the year, we sent one billion notifications, a 108 percent increase over 2018.

New online mortgage and home equity application. We were excited to launch HomeSquad, our new online mortgage and equity application. HomeSquad provides step-by-step guidance and enables members to easily apply, upload documents, track their application status, receive notices of key milestones and more.

24/7 support.

We've made sure members can continue to contact us around the clock through 24/7 telephone access to stateside member representatives, eMessages, chat, social media and notifications. Member Service Representatives handled 38.7 million calls assisting 4.9 million unique members, surpassing 2018 by 8.9 percent.

Member support initiatives.

We also introduced an initiative to help members build and improve credit and one that identified career paths that match the values that matter most to servicemembers.

Member and Employee Satisfaction

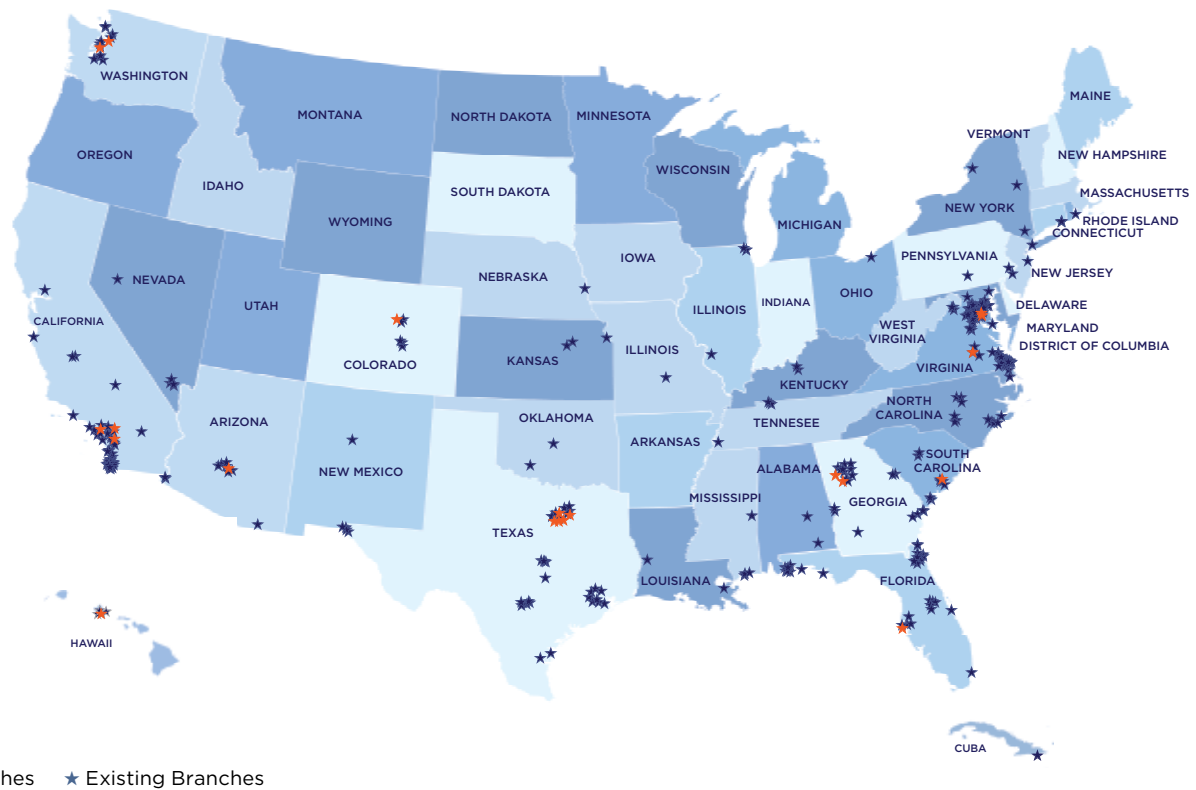
Our corporate road map is rooted in our commitment to always providing an outstanding member experience and creating and maintaining a positive, employee-centric work environment. As a result, our members' and employees' satisfaction remains high, which is reflected in the ratings we receive in national surveys.

Strength and Innovation

The military community is characterized by its strength, and we're proud to serve them throughout all economic conditions. Our members are cut from an amazing cloth—they're a community and a family. It's why we strive to continually improve our service, products, processes, tools and technology—to make their interactions with us easier and to give them a better handle on their finances. Because, above all, our members are the mission.[®]

We're pleased to present this report to you and thank our members for the opportunity to be their trusted financial partner.

2019 United States and Cuba Locations



ALABAMA

Enterprise
Montgomery

ARIZONA

Chandler
Goodyear
Glendale
Mesa
Phoenix (2)
Sierra Vista
Yuma (2)*

CALIFORNIA

Chula Vista (2)
Corona
Coronado
El Cajon
Fountain Valley
Hawthorne
Lake Elsinore
La Mesa
Lemoore*
Long Beach
Monterey*
Murrieta
National City
Oceanside
Ontario
Port Hueneme
Ridgecrest
San Diego (14)*

San Marcos
Santa Ana
Santee
Temecula
Twentynine Palms
Vacaville
West Covina

COLORADO

Aurora
Centennial
Colorado Springs (2)
Fountain

CONNECTICUT

Groton (2)*
New London*

DISTRICT OF COLUMBIA

Pentagon*
Washington
Navy Yard*

FLORIDA

Altamonte Springs
Atlantic Beach
Clearwater
Fleming Island
Gulf Breeze
Jacksonville
Kissimmee
Lutz
Mary Esther

Mayport*
Miami*
Orlando
Pace
Panama City Beach*
Pensacola
Riverview
Satellite Beach
Tampa
Winter Park

GEORGIA

Albany*
Augusta
Buckhead
Buford
Columbus
Conyers
Grovetown
Hinesville
Kennesaw
Kings Bay*
Marietta
McDonough
Milton
Richmond Hill
Sandy Springs
Savannah
Snellville
St Marys
Stockbridge

HAWAII

Honolulu*
Kailua
Kapolei
Mililani

ILLINOIS

Great Lakes (2)*
Gurnee
O'Fallon

KANSAS

Junction City
Leavenworth
Manhattan

KENTUCKY

Elizabethtown
Oak Grove
Radcliff

LOUISIANA

Leesville
New Orleans*

MARYLAND

Accokeek
Annapolis (3)*
Bel Air
Bethesda (2)*
Bowie (2)
Capitol Heights
Fort Meade*
Frederick
Gaithersburg

Gambrills
Germantown
Glen Burnie
Glenarden
Indian Head*
Laurel
Lexington Park
Odenton
Rockville
Suitland*
Upper Marlboro
Waldorf

MISSISSIPPI

D'Iberville
Gulfport (2)*
Meridian*

MISSOURI

St. Robert

NEBRASKA

Bellevue

NEVADA

Fallon*
Henderson
Las Vegas (3)

NEW JERSEY

Cherry Hill
Colts Neck*

NEW MEXICO

Albuquerque

NEW YORK

Evans Mills
Highland Falls
Kings Point*
Saratoga Springs*

NORTH CAROLINA

Cameron
Elizabeth City*
Fayetteville (2)
Garner
Havelock
Jacksonville (2)
Midway Park
Moyock
Raleigh (2)
Richlands
Swansboro

OHIO

Cleveland*

OKLAHOMA

Lawton
Midwest City

PENNSYLVANIA

Carlisle*
Horsham

RHODE ISLAND

Newport*
(continued)

2019 Overseas Locations (All On-Base)



SOUTH CAROLINA

Beaufort
Charleston
Columbia (2)
North Charleston
Parris Island*
Summerville (2)

TENNESSEE

Clarksville (2)
Millington

TEXAS

Allen
Arlington

Copperas Cove
Corpus Christi
Cypress
Dallas
El Paso (4)
Fort Worth (2)*
Garland
Harker Heights
Helotes
Houston
Humble
Katy
Killeen (2)
Kingsville*
Pearland

Round Rock
San Antonio (3)
Spring
Sugar Land
The Colony
Universal City
Webster
Westworth Village

VIRGINIA

Alexandria (3)
Annandale
Arlington (3)
Ashburn
Burke

Centreville
Chesapeake (5)
Colonial Heights
Fairfax
Fredericksburg (3)
Gainesville
Hampton (2)
Lake Ridge
Manassas
Midlothian
Montclair
Newport News (2)
Norfolk (5)*
North Richmond

Portsmouth (3)*
Reston
Springfield
Stafford (2)
Sterling
Suffolk
Vienna
Virginia Beach (11)*
Williamsburg
Winchester (3)
Woodbridge
Yorktown*

WASHINGTON

Bremerton
Everett*
Lacey
Lakewood
Marysville*
Oak Harbor (2)*
Poulsbo
Puyallup
Silverdale
Tacoma

AFRICA

Djibouti*

BAHRAIN

Manama*

CUBA

Guantanamo Bay*

GREECE

Crete*

GUAM

Santa Rita*

ITALY

Caserta*
Sigonella*

JAPAN

Ayase*
Camp Zama*
Iwakuni*
Misawa*
Sasebo*
Yokosuka*
Yokota*

KOREA

Chilgok-Gun*
Daegu*
Pyongtaek*
Osan*

OKINAWA

Camp Courtney
Camp Foster
Camp Hansen
Camp Kinser
Camp Schwab
Futenma

SINGAPORE

SPAIN
Rota*

2019 Board of Directors



John A. Lockard
Chairman of the Board



Bruce B. Engelhardt
First Vice Chairman



Edward R. Cochrane Jr.
Second Vice Chairman



Mary A. McDuffie
Treasurer



Kenneth R. Burns
Secretary



Annie B. Andrews



Kirk A. Foster



Neil W. T. Hogg



William P. Mizerak

Supervisory Committee Input for the 2019 Annual Report

The Supervisory Committee provides the membership with an independent appraisal of the safety and soundness of Navy Federal's operations and activities. It does so in compliance with the Federal Credit Union Act and Navy Federal's bylaws. The Committee reviews all audit reports and meets quarterly to discuss audit results, Internal Audit recommendations for strengthening internal controls, and the status of management's action on all prior Internal Audit recommendations. The Supervisory Committee ensures that Navy Federal's financial statements provide a fair and accurate presentation of its financial condition and that management establishes and maintains sound internal controls to protect the assets of your credit union.

The Supervisory Committee employs the independent accounting firm of PricewaterhouseCoopers LLP (PwC) to assist in meeting its responsibilities. The Committee meets regularly with PwC to evaluate audit results and to plan future audit work. PwC conducts quarterly

procedures related to selected operations, and performs a comprehensive audit of the credit union's year-end financial statements. PwC's year-end audit, the *Independent Auditor's Report*, appears in this Annual Report.

Throughout the year, the committee reviews and responds in writing to letters and emails it receives from the membership. Both the membership and the management of Navy Federal benefit from this open communication because your individual concerns are addressed on a personal basis and your comments help to ensure that Navy Federal maintains the highest level of service to its members.

The National Credit Union Administration (NCUA), the regulatory agency for all federally chartered credit unions, also performs periodic supervisory examinations.

Based on the results of the Annual Report of Independent Auditors and the Examination Report of the NCUA, it is the opinion of your Supervisory Committee that Navy Federal continues to be financially strong and well managed, with sound policies and programs.



Michael C. Wholley
Chairman

Supervisory Committee



Kirk A. Foster



Patrick J. McClanahan



Caral E. Spangler



Pasquale M. Tamburrino Jr.



Michael C. Wholley
Chairman, Supervisory Committee

Other Committee Members



John R. Edwards



Trent H. Edwards



Anthony M. Kurta



Brian E. Luther



James L. Moser



Daniel L. Nega



Diane M. Randon



Paul Severs



Jennifer E. Shaar



Mark R. Taylor



Karin A. Vernazza



David P. Walt

Volunteer Officials

Board of Directors

John A. Lockard

Vice Admiral, USN (Ret.)
Chairman of the Board
Executive Committee

Bruce B. Engelhardt

Rear Admiral, USN (Ret.)
First Vice Chairman
Executive Committee
Financial Strategy and Investment Committee
Technology Committee

Edward R. Cochran Jr.

Second Vice Chairman
Executive Committee
Financial Strategy and Investment Committee
Planning and Strategic Direction Committee

Mary A. McDuffie

Treasurer
Executive Committee
Financial Strategy and Investment Committee
Planning and Strategic Direction Committee
Technology Committee

Kenneth R. Burns

Colonel, USMC (Ret.)
Secretary
Executive Committee
Financial Strategy and Investment Committee

Annie B. Andrews

Rear Admiral, USN (Ret.)
Planning and Strategic Direction Committee
Technology Committee

Kirk A. Foster

Rear Admiral, USN (Ret.)
Supervisory Committee
Technology Committee

Neil W. T. Hogg

Captain, USN (Ret.)
Financial Strategy and Investment Committee

William P. Mizerak

Colonel, USMC (Ret.)
Financial Strategy and Investment Committee
Planning and Strategic Direction Committee

Committee Members

John R. Edwards

Colonel, USAF
Technology Committee

Trent H. Edwards

Brigadier General, USAF (Ret.)
Financial Strategy and Investment Committee

Anthony M. Kurta

Rear Admiral, USN (Ret.)
Planning and Strategic Direction Committee

Brian E. Luther

Rear Admiral, USN (Ret.)
Planning and Strategic Direction Committee

Patrick J. McClanahan

Captain, SC, USN (Ret.)
Supervisory Committee

James L. Moser

Technology Committee

Daniel L. Nega

Planning and Strategic Direction Committee

Diane M. Randon

Financial Strategy and Investment Committee

Paul Severs

Captain, USN (Ret.)
Planning and Strategic Direction Committee

Jennifer E. Shaar

Colonel, USMC
Planning and Strategic Direction Committee

Caral E. Spangler

Financial Strategy and Investment Committee
Supervisory Committee

Pasquale M. Tamburrino Jr.

Supervisory Committee
Technology Committee

Mark R. Taylor

Colonel, USA
Technology Committee

Karin A. Vernazza

Captain, USN (Ret.)
Technology Committee

David P. Walt

Captain, USN
Technology Committee

Michael C. Wholley

Brigadier General, USMC (Ret.)
Chairman, Supervisory Committee

Navy Federal Credit Union
Consolidated Financial Statements and Report of Independent Auditors
December 31, 2019 and 2018

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Report of Independent Auditors

To the Board of Directors and Supervisory Committee of Navy Federal Credit Union

We have audited the accompanying consolidated financial statements of Navy Federal Credit Union and its subsidiaries ("the Company"), which comprise the consolidated statements of financial condition as of December 31, 2019 and 2018, and the related consolidated statements of income, comprehensive income, changes in members' equity and of cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Navy Federal Credit Union and its subsidiaries as of December 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

March 20, 2020

*PricewaterhouseCoopers LLP, 1800 Tysons Blvd, McLean, VA 22102
T: (703) 918 3000, F: (703) 918 3100, www.pwc.com/us*

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(dollars in thousands)	As of December 31,	
	2019	2018
ASSETS		
Cash and cash equivalents	\$ 5,035,143	\$ 1,362,428
Available-for-sale debt securities	18,772,834	16,574,816
Held-to-maturity securities	351,708	400,831
Equity securities	-	194,426
Mortgage loans awaiting sale	2,477,253	1,193,288
Loans to members, net of allowance for loan losses of \$1,631,851 and \$1,475,942, respectively	79,810,777	72,389,939
Accounts receivable and accrued interest	1,037,763	824,890
Property, plant and equipment, net	2,275,394	1,930,167
Investments in FHLB	451,026	569,975
NCUSIF deposit	741,134	635,843
Mortgage servicing rights	505,298	479,638
Goodwill	58,905	58,905
Other assets	468,843	347,300
Total assets	\$ 111,986,078	\$ 96,962,446
LIABILITIES AND MEMBERS' EQUITY		
Deposit accounts		
Checking	\$ 15,321,607	\$ 13,531,358
Savings	18,561,158	16,664,659
Money market savings	15,424,405	14,344,397
Certificates	29,299,556	19,790,889
Individual retirement accounts	7,426,545	6,086,231
Total deposit accounts	86,033,271	70,417,534
Liabilities		
Borrowed funds	10,259,439	13,308,239
Accounts payable and accrued expenses	1,360,429	1,304,400
Other liabilities	569,316	527,591
Total deposit accounts and liabilities	98,222,455	85,557,764
Members' equity		
Equity	13,819,544	12,149,541
Accumulated other comprehensive loss	(55,921)	(744,859)
Total members' equity	13,763,623	11,404,682
Total liabilities and members' equity	\$ 111,986,078	\$ 96,962,446

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

(dollars in thousands)	For the Years Ended December 31,	
	2019	2018
Interest income		
Loans to members	\$ 5,689,296	\$ 4,939,073
Investment securities	487,326	420,946
Other investments	90,748	38,314
Total interest income	6,267,370	5,398,333
Dividends and interest expense		
Dividends on deposits	1,016,393	642,614
Interest on borrowed funds	355,212	340,006
Total dividends and interest expense	1,371,605	982,620
Net interest income	4,895,765	4,415,713
Provision for loan losses	(1,520,844)	(1,446,604)
Net interest income after provision for loan losses	3,374,921	2,969,109
Non-interest income		
Net gain on mortgage loans	249,517	167,632
Net gain/(loss) on investments	42,054	(9,519)
Mortgage servicing revenue	153,794	132,594
Interchange income	528,606	461,918
Fee and other income	751,906	667,649
Total non-interest income	1,725,877	1,420,274
Non-interest expense		
Salaries and employee benefits	1,721,539	1,394,426
Office operations and equipment	430,189	382,229
Servicing expense	284,678	290,867
Professional and outside services	277,666	211,667
Marketing	177,894	165,432
Depreciation and amortization	215,304	224,134
Other	323,525	175,357
Total non-interest expense	3,430,795	2,844,112
Net income	\$ 1,670,003	\$ 1,545,271

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(dollars in thousands)	For the Years Ended December 31,	
	2019	2018
Net income	\$ 1,670,003	\$ 1,545,271
Other comprehensive income/(loss)		
Change in unrecognized pension and postretirement amounts	35,890	(81,024)
Change in net unrealized gains/(losses) on AFS debt securities	793,555	(291,831)
Change in unrecognized losses on derivatives	(140,507)	(13,100)
Total other comprehensive income/(loss)	688,938	(385,955)
Total comprehensive income	\$ 2,358,941	\$ 1,159,316

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN MEMBERS' EQUITY

(dollars in thousands)	Equity	Accumulated Other Comprehensive (Loss)/Income	Total Members' Equity
Balance at December 31, 2017	\$ 10,551,156	\$ (320,528)	\$ 10,230,628
Cumulative effects from adoption of new accounting standards	53,114	(38,376)	14,738
Other comprehensive loss	-	(385,955)	(385,955)
Net income	1,545,271	-	1,545,271
Balance at December 31, 2018	\$ 12,149,541	\$ (744,859)	\$ 11,404,682
Other comprehensive income	-	688,938	688,938
Net income	1,670,003	-	1,670,003
Balance at December 31, 2019	\$ 13,819,544	\$ (55,921)	\$ 13,763,623

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Years Ended December 31,	
	2019	2018
<i>(dollars in thousands)</i>		
Operating activities		
Net income	\$ 1,670,003	\$ 1,545,271
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for loan losses	1,520,844	1,446,604
Depreciation and amortization	215,304	224,134
Non-cash adjustments and loss/(gain) on disposal of property, plant and equipment	5,498	(91,924)
Loss on valuation of equity securities	-	8,677
(Gain)/loss on sale of securities	(41,271)	1,013
Loss on extinguishment of debt	26,865	-
Amortization of loan origination fees and costs	14,951	13,728
Loss on valuation of mortgage servicing rights	114,321	46,909
Mortgage loans originated for sale	(9,215,730)	(7,667,792)
Gain on sale of mortgages	(249,517)	(167,632)
Mortgage loan sales proceeds	8,066,483	7,714,985
Accretion and amortization of investment securities	56,612	50,875
Change in accounts receivable and accrued interest	(212,052)	(61,333)
Change in mortgage servicing rights	(139,981)	(134,014)
Change in other assets	(63,507)	(145,523)
Change in accounts payable and accrued expenses	77,320	182,849
Change in other liabilities	(139,338)	67,958
Net cash provided by operating activities	1,706,805	3,034,785
Investing activities		
Purchase of AFS debt securities	(4,630,494)	(3,456,124)
Purchase of HTM securities	(201,336)	-
Proceeds from maturities, paydowns and calls of AFS debt securities	1,769,747	1,129,531
Proceeds from sales of AFS debt securities	1,459,481	844,762
Proceeds from maturities, paydowns and calls of HTM securities	250,544	1,022
Proceeds from sales of equity securities	225,179	-
Issuance of loan receivable	-	(750)
Net redemptions of FHLB stock	118,949	105,235
Proceeds from sale of loans originated for investment	993,591	-
Net increase in loans to members	(9,929,144)	(9,230,193)
Purchases of property, plant and equipment	(592,913)	(422,995)
Increase in NCUSIF deposit	(105,291)	(76,002)
Proceeds from sale of real estate owned and other assets	77,041	42,009
Net cash used in investing activities	(10,564,646)	(11,063,505)
Financing activities		
Net increase in deposit accounts	15,615,737	7,410,791
Net decrease in securities sold under repurchase agreements	(250,000)	-
Proceeds from borrowed funds	7,240,202	28,085,002
Repayments of borrowed funds	(10,065,867)	(30,556,702)
Payments of capital lease and financing obligations	(9,516)	(20,312)
Net cash provided by financing activities	12,530,556	4,918,779
Net increase/(decrease) in cash and cash equivalents and restricted cash	3,672,715	(3,109,941)
Cash and cash equivalents and restricted cash at beginning of year	1,367,414	4,477,355
Cash and cash equivalents and restricted cash at end of year	\$ 5,040,129	\$ 1,367,414
Supplemental cash flow information:		
Interest paid	\$ 1,383,161	\$ 955,685
Non-cash activities:		
Transfers of loans to other assets	\$ 77,961	\$ 28,182
Loans securitization	48,299	356,859
Accrued additions and improvements of property, plant and equipment	22,367	17,367
Financed property, plant and equipment	10,689	6,327
Transfer of land held for sale to other assets	20,486	-
Transfer of mortgage loans awaiting sale to loans to members	81,267	-
Transfer of loans from members to mortgage loans awaiting sale	975,818	-

The following table provides a reconciliation of Cash and cash equivalents and restricted cash from the Consolidated Statements of Financial Condition to the Consolidated Statements of Cash Flows.

	As of December 31,	
	2019	2018
<i>(dollars in thousands)</i>		
Cash and cash equivalents on the Consolidated Statements of Financial Condition	\$ 5,035,143	\$ 1,362,428
Restricted cash included in other assets on the Consolidated Statements of Financial Condition ⁽¹⁾	4,986	4,986
Total Cash and cash equivalents and restricted cash in the Consolidated Statements of Cash Flows	\$ 5,040,129	\$ 1,367,414

⁽¹⁾ Refer to Note 2 for additional details.

The accompanying notes are an integral part of these consolidated financial statements.

Note 1: Summary of Significant Accounting Policies

Organization

Navy Federal Credit Union is a member-owned, not-for-profit financial institution formed in 1933 under the provisions of the Federal Credit Union Act (FCUA) to provide a variety of financial services to those individuals in its field of membership, which includes active duty, veterans and retired military and civilian personnel who are or were employed by the Department of Defense, and their families. Navy Federal is headquartered in Vienna, Virginia with branch locations around the country and abroad.

Navy Federal Financial Group (NFFG), a subsidiary of Navy Federal Credit Union, is a credit union service organization that provides investment, insurance and other financial services. Navy Federal Brokerage Services is a wholly owned subsidiary of NFFG. Navy Federal Credit Union and its consolidated entity are referred to as "Navy Federal" herein.

Basis of Presentation and Use of Estimates

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. These estimates are based on information available at the time the consolidated financial statements are prepared. Actual amounts or results could differ from these estimates.

Principles of Consolidation

The consolidated financial statements include the accounts of Navy Federal Credit Union and its wholly owned subsidiary. All significant intercompany accounts and transactions have been eliminated in consolidation.

Business Combinations

The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 805, *Business Combinations*, requires all business combinations be accounted for by applying the acquisition method. Accordingly, Navy Federal allocates the acquisition price of assets obtained and liabilities assumed in a business combination at fair value on the acquisition date. Any excess of the acquisition price over the fair value of net assets acquired is recognized as goodwill, and transaction costs are expensed as incurred.

Reclassifications

Certain amounts in the prior year consolidated financial statements have been reclassified to conform to current year presentation.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and balances due from other financial institutions, including minimum cash reserves required and cash in excess of minimum reserves held at the Federal Reserve Bank (FRB), federal funds sold and securities purchased under agreements to resell. Cash and cash equivalents exclude restricted cash, which is included in Other assets on the Consolidated Statements of Financial Condition. See Note 2: Restrictions on Cash for details.

Investments

Navy Federal's investments in debt securities are classified as available-for-sale (AFS) or held-to-maturity (HTM) in accordance with ASC 320, *Investments—Debt Securities*. Debt securities classified as AFS are carried at fair value, with any unrealized gains and losses recorded in accumulated other comprehensive income (AOCI). Debt securities classified as HTM are carried at cost, adjusted for the amortization of premiums and accretion of discounts. Management has the ability and intent to hold these securities until maturity. Gains and losses on dispositions are computed using the specific identification method and are included in Net gain/(loss) on investments in the Consolidated Statements of Income. For both AFS and HTM debt securities, interest income is recognized on an accrual basis, and premiums and discounts are amortized or accreted as an adjustment to interest income using the effective interest method. See Note 3: Investments for details.

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Navy Federal evaluates its debt securities in an unrealized loss position for other-than-temporary impairment in accordance with ASC 320. Navy Federal assesses whether it (a) has the intent to sell the debt security, (b) is more likely than not that it will be required to sell the debt security before recovering its amortized cost basis or (c) does not expect to recover the entire amortized cost basis of the debt security even if it does not intend to sell the debt security. In order to determine whether the entire amortized cost basis of the debt security can be recovered, Navy Federal compares the present value of cash flows expected to be collected from the debt security with its amortized cost basis and considers (1) the amount, and length of time, fair value has been less than amortized cost, (2) adverse conditions specifically related to the debt security or specific industry, (3) the volatility of the debt security and its expected cash flows, and (4) changes in ratings of the issuer. Declines in fair value that are other-than-temporary are recognized in earnings.

Navy Federal's investments in equity securities are classified as Equity securities on the Consolidated Statements of Financial Condition in accordance with ASC 321, *Investments—Equity Securities*. Equity securities are carried at fair value, with any unrealized gains and losses recorded in earnings and included in Net gain/(loss) on investments in the Consolidated Statements of Income. See Note 3: Investments for details.

Navy Federal has stock in the Federal Home Loan Bank (FHLB) of Atlanta with maturities of three months or less. Accordingly, the carrying amounts are considered a reasonable estimate of fair value. FHLB stock is a restricted investment that is included in Investments in FHLB on the Consolidated Statements of Financial Condition and is evaluated for impairment annually. There was no impairment for the years ended December 31, 2019 and 2018.

In accordance with ASC 860, *Transfers and Servicing*, repurchase agreements and reverse repurchase agreements are recorded at historical cost and accounted for as secured financings or investments. Navy Federal transfers title to the collateral sold or purchased under repurchase and reverse repurchase agreements, respectively, and monitors the fair value of the underlying financial assets, which are primarily U.S. government and federal agency securities.

Loans to Members

Navy Federal's loan portfolio consists of consumer, credit card and real estate loans. Consumer loans consist of auto loans, signature loans, checking lines of credit and education loans. Real estate loans consist of mortgage and equity loans. At origination, all consumer, credit card and equity loans are classified as held for investment. Mortgage loans are classified as either mortgage loans held for investment or mortgage loans awaiting sale (MLAS) based on management's intent and ability to hold the loans for the foreseeable future or until maturity/payoff, or to sell the loans.

In accordance with ASC 310, *Receivables*, loans to members are carried at the amount of unpaid principal balance (UPB) adjusted for net loan origination fees and certain direct origination costs, less an allowance for loan losses. Interest is accrued on loans using the effective interest method on a daily basis except for credit card loans, for which interest is calculated by applying the periodic rate to the average daily balance outstanding.

Loans are determined to be delinquent based on the contractual terms and are considered delinquent when they are 30 days past due. When a loan becomes 90 days past due, accrued interest is reversed and the loan is placed into non-accrual status. Interest received on non-accrual status loans is accounted for on a cash basis. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

In accordance with ASC 310-20, *Receivables—Nonrefundable Fees and Other Costs*, loan origination fees and certain direct origination costs are deferred and amortized over the life of the loans using the effective interest method (effective yield) for all products except for credit card loans, where fees and costs are netted and deferred and amortized on a straight-line basis over 12 months.

A loan is considered impaired when, based on current information and events, it is probable that Navy Federal will be unable to collect all amounts due from the borrower in accordance with the original contractual term. Navy Federal measures and recognizes impairment in accordance with ASC 310. All loans subject to a troubled debt restructuring (TDR) are individually evaluated for impairment. Interest income on restructured loans that return to accrual status is recognized on an accrual basis.

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Allowance for Loan Losses

Navy Federal accrues estimated losses in accordance with ASC 450, *Contingencies*. The allowance for loan losses is a reserve against loans to members established through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the collectability of the loan amount is unlikely. Recoveries on previously charged-off loans are credited to the allowance.

Navy Federal's loan portfolio consists mainly of large groups of smaller-balance homogeneous loans that are collectively evaluated for impairment. The allowance for loan losses is maintained at a level that, in management's judgment, is sufficient to absorb losses inherent in the portfolio based on monthly evaluations of the portfolio's collectability. Collectability is determined by historical experience, overall delinquency and delinquencies by loan product, and current economic conditions and trends that may adversely affect a borrower's ability to pay. The allowance for loan losses is subject to estimates and uncertainties associated with factors and processes used in determining the amount. Actual loan losses may differ from the estimates. Loans that are not in foreclosure, undergoing a modification or subject to a repayment plan are generally charged off to the allowance at 180 days past due.

Navy Federal also maintains an allowance for unfunded commitments at a level that is appropriate to absorb estimated probable credit losses. The allowance for unfunded commitments is derived in a manner similar to the methodology used for determining the allowance for loan losses. The allowance for unfunded commitments is recorded in Other liabilities on the Consolidated Statements of Financial Condition and the related provision expense is included in Provision for loan losses in the Consolidated Statements of Income.

Mortgage Loans Awaiting Sale

The initial loan level basis for MLAS is equal to UPB adjusted for net loan origination fees and certain direct origination costs. Interest income on MLAS is recorded as earned and is reported in Interest income—Loans to members in the Consolidated Statements of Income. ASC 825, *Financial Instruments*, permits entities to irrevocably elect to measure many financial instruments at fair value. Navy Federal has elected the fair value option for MLAS, and subsequent changes to estimated fair value are recognized in Net gain on mortgage loans in the Consolidated Statements of Income. Loans are removed from the Consolidated Statements of Financial Condition when sold and sales treatment is applied when, in accordance with ASC 860, *Transfers and Servicing*, the conditions for sale of financial assets are met. See Note 5: Loan Sales and Continuing Involvement in Assets Transferred for details.

Mortgage Servicing Rights

Navy Federal recognizes mortgage servicing rights (MSR) when mortgage loans are sold and Navy Federal retains the right to service those loans. Navy Federal recognizes MSR at fair value with changes in fair value recognized in Other in the Consolidated Statements of Income. Navy Federal recognizes revenue from servicing mortgage loans as such fees are earned based on specific contractual terms. See Note 5: Loan Sales and Continuing Involvement in Assets Transferred for details.

Troubled Debt Restructurings

A TDR is a loan for which Navy Federal has granted a concession it would not have otherwise considered because a member is experiencing financial difficulty. The types of concessions Navy Federal grants in a TDR primarily include term extensions and/or interest rate reductions. TDR loans are accounted for in accordance with ASC 310-40, *Receivables—Troubled Debt Restructurings by Creditors*. See Note 4: Loans and Allowance for Loan Losses for details.

Property, Plant and Equipment

Land held for use is carried at cost. Buildings, furniture, fixtures, equipment, computer software and capitalized information technology (IT) assets are carried at cost less accumulated depreciation and amortization, which are computed on a straight-line basis over the assets' estimated useful lives. The cost and related accumulated depreciation and amortization are eliminated from accounts when assets are disposed. Gains or losses upon disposition are included in Other in the Consolidated Statements of Income. Expenditures for repairs and maintenance are charged to earnings as incurred. Improvements that extend the useful life of an asset are capitalized and depreciated over the extended useful life. Navy Federal purchases, as well as internally develops and customizes, certain software to enhance or perform internal business functions. Software development costs incurred in the planning and post-development project stages are charged to non-interest expense, and costs

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incurred in the application development stage are capitalized and amortized using the straight-line method over a five-year period. Leasehold improvements are carried at cost less accumulated amortization and are amortized over the lesser of the useful life or the remaining fixed non-cancelable lease term. Useful lives for each asset category are estimated as follows:

	Useful Life
Buildings	40 years
Equipment, furniture and fixtures	5 to 7.5 years
Computer equipment	2 to 3 years
Computer software and capitalized IT assets	5 years

Navy Federal uses the straight-line method to account for its operating leases. Under this method, Navy Federal divides the total contractual rent by the total term of the lease. The average monthly rent is recorded as rent expense, and the remaining rent amount is deferred. Navy Federal reviews its operating leases at inception, and subsequently on an ongoing basis, for the existence of asset retirement obligations that are accrued, when material, pursuant to ASC 410-20, *Asset Retirement Obligations*.

NCUSIF Deposit

The deposit in the National Credit Union Share Insurance Fund (NCUSIF) is in accordance with the FCUA and the National Credit Union Administration (NCUA) regulations, which require the maintenance of a deposit by each credit union in an amount equal to 1% of its insurable shares. The deposit would be refunded to Navy Federal if its insurance coverage is terminated, the operations of the fund are transferred from the NCUA Board or if NCUA decides to make a distribution to credit unions based on the equity ratio's excess over the net operating level.

Goodwill

Goodwill represents the excess of purchase price over the fair value of assets acquired and liabilities assumed in business combinations. In accordance with ASC 350-20, *Intangibles—Goodwill and Other*, intangible assets with finite useful lives are amortized and goodwill and intangible assets with indefinite lives are evaluated at least annually for impairment. Navy Federal evaluates goodwill for impairment annually as of September 30, or more frequently should events or changes in circumstances occur, that would more likely than not reduce the fair value of Navy Federal below its carrying value. Impairment exists when the carrying amount of goodwill exceeds its implied fair value. Navy Federal assesses qualitative factors including, but not limited to, the general economic environment, industry and market considerations and overall financial performance of Navy Federal. See Note 9: Goodwill for details.

Derivative Financial Instruments

Derivative financial instruments are financial contracts that derive their value from underlying changes in assets, rates or indices. Derivatives are used to protect or hedge against changes in prices or interest rate movements that could adversely affect the value of certain assets or liabilities and future cash flows.

Navy Federal accounts for its derivative financial instruments in accordance with ASC 815, *Derivatives and Hedging*, which requires all derivative instruments to be carried at fair value on the Consolidated Statements of Financial Condition. Navy Federal executes certain derivative contracts over-the-counter and clears these transactions through a derivative clearing organization. Some of Navy Federal's derivatives are subject to legally enforceable master netting agreements, which allow Navy Federal to settle positive and negative positions held with the same counterparty on a net basis. As such, Navy Federal reports these positions on a net basis on the Consolidated Statements of Financial Condition. All derivative financial instruments are recognized at fair value and classified as Other assets or Other liabilities on the Consolidated Statements of Financial Condition. See Note 6: Derivative Instruments and Hedging Activities for details.

Economic Hedges

Navy Federal enters into mortgage loan commitments, also called interest rate lock commitments (IRLCs), in connection with its mortgage banking activities to fund residential mortgage loans at specified times in the future. The IRLCs are considered derivative instruments under applicable accounting guidance and expose Navy Federal to the risk that the price of the loans underlying the commitments may decline between the inception of the rate lock and the funding date of the loan. Navy Federal is exposed to further price risk after the funding date until the mortgage loan is sold. To protect against price risk, Navy Federal enters into forward sales contracts with

counterparties. Changes in the fair value of economic hedges are included in Net gain on mortgage loans in the Consolidated Statements of Income.

Accounting Hedges

Under the provisions of ASC 815, *Derivatives and Hedging*, derivative instruments can be designated as fair value hedges or cash flow hedges. Fair value hedges are used to protect against changes in the value of assets and liabilities as a result of interest rate volatility. Navy Federal uses interest rate swaps as fair value hedges to offset the change in value of its fixed-rate AFS debt securities. Changes in the fair value of fair value hedges are recorded in the same Consolidated Statements of Income line item as the related hedged item. Cash flow hedges are used to minimize the variability in cash flows resulting from interest rate fluctuations. Navy Federal uses interest rate swaps to hedge against the variability in cash flows of its floating-rate debt payments. Changes in fair value of cash flow hedges are reported as a component of AOCI and reclassified into earnings in the same period when the hedged transaction affects earnings, and in the same Consolidated Statements of Income line as the hedged item.

At the inception of a hedge relationship, Navy Federal formally documents the hedged item, the particular risk management objective, the nature of the risk being hedged, the derivative being used, how effectiveness of the hedge will be assessed and how ineffectiveness of the hedge will be measured. Navy Federal utilizes a regression analysis at the inception of a hedge and a qualitative analysis for each reporting period thereafter to assess whether the derivative is expected to be, and has been, highly effective in offsetting changes in the fair value or cash flows of a hedged item.

Navy Federal discontinues hedge accounting when it is determined the derivative is not expected to be or has ceased to be a highly effective hedge; the derivative expires or is sold, terminated or exercised; the derivative is de-designated; or in the case of a cash flow hedge, it is no longer probable that the forecasted transaction will occur by the end of the originally specified time frame. Subsequent to discontinuing a fair value or cash flow hedge, the derivative will continue to be recorded on the Consolidated Statements of Financial Condition at fair value, with changes in fair value included in earnings. For a discontinued fair value hedge, the previously hedged item is no longer adjusted for changes in fair value. If the forecasted transaction is no longer probable to occur, Navy Federal discontinues hedge accounting designation and immediately recognizes the previously unrealized gain or loss in AOCI into earnings. For other discontinuing type events, the unrealized gain or loss continues to be deferred in AOCI until the forecasted transaction affects earnings. Navy Federal did not discontinue hedge accounting for any hedges for the years ended December 31, 2019 and 2018.

Pension Accounting and Retirement Benefit Plans

Navy Federal has a defined benefit pension plan, 401(k) defined contribution and 457(b) savings plans, and a non-qualified supplemental retirement plan. Navy Federal also provides a postretirement medical plan for certain retired employees. Navy Federal accounts for its defined benefit pension plans in accordance with ASC 715, *Compensation—Retirement Benefits*. See Note 12: Retirement Benefit Plans for details.

Fair Value Measurement

Navy Federal measures certain financial assets and liabilities at fair value in accordance with ASC 820, *Fair Value Measurement*, which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between willing market participants at the measurement date. Navy Federal employs various valuation approaches to measure fair value including market and income approaches. The market approach uses prices or relevant information generated by market transactions involving identical or comparable assets or liabilities. The income approach involves discounting future amounts to a single present amount and is based on current market expectations about those future amounts. Valuation techniques and parameters used for measuring assets and liabilities are reviewed and validated by Navy Federal on an annual basis. In measuring fair value, Navy Federal maximizes the use of quoted prices and observable inputs. A description of the fair value hierarchy is as follows:

- Level 1 – Valuation is based on unadjusted quoted prices in an active market for identical instruments.
- Level 2 – Valuation is based on observable inputs such as quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions (rates, volatilities, credit spreads) for financial instruments are observable.

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- Level 3 – Valuation is generated from techniques that use significant assumptions that are not observable in the market. Valuation techniques include pricing models, discounted cash flow methodologies or similar techniques.

See Note 16: Fair Value Measurement for additional information.

Revenue Recognition

In the ordinary course of business, Navy Federal recognizes two types of revenue in its Consolidated Statements of Income: Interest income and Non-interest income.

Navy Federal's principal source of revenue is interest income from Loans to members and Investment securities, which is recognized on an accrual basis using the effective interest method. For information on Navy Federal's policies for recognizing Interest income on investments and loans, refer to "Investments", "Loans to Members" and "Mortgage Loans Awaiting Sale" sections within this Note.

Non-interest income includes revenue from various types of transactions and services provided to members and customers. For information on Navy Federal's policies for recognizing Net gain on mortgage loans, Net gain/(loss) on investments, and Mortgage servicing revenue, refer to "Mortgage Loans Awaiting Sale", "Investments" and "Mortgage Servicing Rights" sections within this Note.

Non-interest income also includes Interchange income and Fee and other income which are accounted for in accordance with ASC 606, *Revenue from Contracts with Customers (ASC 606)*. Navy Federal adopted ASC 606 beginning January 1, 2019 using the retrospective method. Revenue and interest income earned on financial instruments, such as loans, investments and derivatives are not in the scope of the amended revenue recognition accounting guidance and are accounted for under other GAAP. Thus, the adoption of this amended guidance did not have a material impact on Navy Federal's consolidated financial statements.

Revenue from contracts with customers comprises of non-interest income earned by Navy Federal in exchange for services provided to customers and recognized when services are completed or as they are rendered and based on agreed-upon rates. Majority of the contracts with customers are short-term by nature and can be terminated by our members or customers at any time.

Interchange income consists of credit and debit cards fees for standing ready to authorize and provide settlement on card transactions processed through the payment networks. Interchange fees are recognized upon settlement with the payment networks. Interchange rates are set by the payment network and are based on transaction volumes and other factors.

Interchange income is reported net of the cost of rewards programs based on card usage. The rewards cost totaled \$339.3 million and \$293.7 million for the years ended December 31, 2019 and 2018.

Majority of Fee and other income relates to service charges on deposit accounts for account maintenance and various transaction-based services such as overdrafts, ATM usage, returned items fees and other deposit related fees. The revenue from these fees is recognized when services or transactions are completed and are based on the type of services provided and agreed-upon rates. Payments for services provided are either withdrawn from the member's account as services are rendered or in the billing period following the completion of the service.

The adoption of ASC 606 resulted in an immaterial impact on the consolidated financial statements.

Advertising Costs

Advertising costs are expensed as incurred and are included in Marketing in the Consolidated Statements of Income.

Income Taxes

Pursuant to the FCUA, Navy Federal is exempt from federal and state income taxes.

Dividends

Dividend rates on deposit accounts are set by Navy Federal's Board of Directors. Dividends are charged to Dividends on deposits in the Consolidated Statements of Income and paid to members monthly.

New Accounting Pronouncements

The following accounting pronouncements have been issued by the FASB, but are not yet effective:

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*, which requires a lessee to recognize assets and liabilities on financing and operating leases with terms exceeding 12 months. This is a change from current GAAP, which requires only capital leases to be recognized on the balance sheet. The ASU will also require additional disclosures to help financial statement readers better understand the amount, timing and uncertainty of cash flows arising from leases. The following ASUs comprise Topic 842, which collectively allow entities to elect a simplified transition approach:

- ASU 2018-01, *Practical Expedient for Transition to Topic 842*
- ASU 2018-10, *Codification Improvements to Topic 842, Leases*
- ASU 2018-11, *Leases (Topic 842): Targeted Improvements*
- ASU 2019-01, *Leases (Topic 842): Codification Improvements*
- ASU 2019-10, *Financial Instruments: Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*

These ASUs are effective for the annual reporting periods beginning after December 15, 2020. Navy Federal is currently evaluating these ASUs to determine the impact on its consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which replaces the incurred loss impairment methodology in current GAAP with a methodology that reflects lifetime expected credit losses of assets carried at amortized cost. The following ASUs comprise Topic 326, which collectively allow entities to elect a simplified transition approach:

- ASU 2018-19, *Codification Improvements to Topic 326, Financial Instruments—Credit Losses*
- ASU 2019-04, *Topic 1, Topic 2 and Topic 5, Codification Improvements to Topic 326, Financial Instruments—Credit Losses*
- ASU 2019-05, *Financial Instruments: Credit Losses (Topic 326): Targeted Transition Relief*
- ASU 2019-10, *Financial Instruments: Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Date*
- ASU 2019-11, *Codification Improvements to Topic 326, Financial Instruments: Credit Losses*

These ASUs are effective for the annual reporting periods beginning after December 15, 2022. While it is expected that the adoption of these ASUs will increase the provision for credit losses, Navy Federal is currently assessing the impact of these ASUs on its consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, *Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*, effective for annual reporting periods beginning after December 15, 2021. This ASU simplifies the subsequent measurement of goodwill by eliminating Step 2 from the goodwill impairment test. The amendments require an entity to perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which a reporting unit's carrying amount exceeds its fair value, but the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. The ASU must be applied on a prospective basis. Navy Federal believes this guidance will not have a material impact on its consolidated financial statements.

In March 2017, the FASB issued ASU 2017-08, *Receivables—Refundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities*, effective for annual reporting periods beginning after December 15, 2019, which shortens the amortization period for certain callable debt securities held at a premium. The amendment does not require a change for securities held at a discount. Navy Federal believes this guidance will not have a material impact on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*, effective for annual reporting periods beginning after December 15, 2019. The amendments in this ASU either removed or modified disclosure requirements related to fair value measurements in accordance with Topic 820. Navy Federal believes this guidance will not have a material impact on its consolidated financial statements.

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In August 2018, the FASB issued ASU 2018-14, *Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans*, effective for annual reporting periods ending after December 15, 2021. The amendments in this ASU remove disclosures that no longer are considered cost beneficial, clarify the specific requirements of disclosures, and add disclosure requirements identified as relevant for employers that sponsor defined benefit pension or other postretirement plans. Navy Federal is currently evaluating this guidance to determine the impact on its consolidated financial statements.

In October 2018, the FASB issued ASU 2018-16, *Derivatives and Hedging (Topic 815): Inclusion of the Secured Overnight Financing Rate (SOFR) Overnight Index Swap (OIS) Rate as a Benchmark Interest Rate for Hedge Accounting Purposes*, effective for annual reporting periods beginning after December 15, 2019. This ASU permits the use of the OIS rate based on SOFR as a U.S. benchmark interest rate for hedge accounting purposes under Topic 815. This will provide entities more lead time to prepare for changes to interest rate risk hedging strategies for both risk management and hedge accounting purposes. Navy Federal believes this guidance will not have a material impact on its consolidated financial statements.

Note 2: Restrictions on Cash

Navy Federal had \$5.0 million in restricted cash as of December 31, 2019 and 2018. Restricted cash amounts are included in Other assets on the Consolidated Statements of Financial Condition.

Note 3: Investments

Equity Securities

Navy Federal sold its equity securities portfolio in 2019, which consisted of investments in a mutual fund and redeemable common stock. Navy Federal recognized \$30.8 million of realized gains from the sale of equity securities for the year ended December 31, 2019. Navy Federal recognized \$8.7 million of unrealized losses on equity securities during the year ended December 31, 2018.

HTM and AFS Debt Securities

The amortized cost of Navy Federal's HTM debt securities as of December 31, 2019 and 2018 was \$351.7 million and \$400.8 million, respectively. Substantially all of the HTM debt securities are U.S. government and federal agency securities.

Navy Federal's AFS debt securities as of December 31, 2019 and 2018 were as follows:

	December 31, 2019			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
<i>(dollars in thousands)</i>				
Available-for-sale debt securities				
U.S. government and federal agency securities	\$ 7,151,567	\$ 142,848	\$ (25,973)	\$ 7,268,442
Residential mortgage-backed securities	6,890,999	67,605	(16,577)	6,942,027
Commercial mortgage-backed securities	473,741	12,433	(90)	486,084
Bank notes and corporate bonds	3,326,532	173,161	(611)	3,499,082
Municipal securities	321,882	17,936	(2,239)	337,579
Non-U.S. government securities	232,422	7,198	-	239,620
Total available-for-sale debt securities	\$ 18,397,143	\$ 421,181	\$ (45,490)	\$ 18,772,834

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	December 31, 2018			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
<i>(dollars in thousands)</i>				
Available-for-sale debt securities				
U.S. government and federal agency securities	\$ 6,204,036	\$ 10,599	\$ (169,764)	\$ 6,044,871
Residential mortgage-backed securities	6,658,838	16,654	(136,417)	6,539,075
Commercial mortgage-backed securities	475,075	76	(13,404)	461,747
Bank notes and corporate bonds	3,202,482	6,441	(123,117)	3,085,806
Municipal securities	244,755	2,103	(2,264)	244,594
Non-U.S. government securities	207,808	-	(9,085)	198,723
Total available-for-sale debt securities	\$ 16,992,994	\$ 35,873	\$ (454,051)	\$ 16,574,816

Navy Federal sold AFS debt securities with a carrying value of \$1,448.2 million and \$846.5 million for cash proceeds of \$1,459.5 million and \$844.8 million for the years ended December 31, 2019 and 2018, respectively. Gross realized gains of \$11.5 million and gross realized losses of \$0.2 million were included in earnings for the year ended December 31, 2019. Gross realized gains of \$5.0 million and gross realized losses of \$6.7 million were included in earnings for the year ended December 31, 2018.

The contractual maturities of Navy Federal's HTM debt securities as of December 31, 2019 were as follows:

	December 31, 2019
<i>(dollars in thousands)</i>	Amortized Cost
Held-to-maturity debt securities	
Due in one year or less	\$ 99,849
Due after one year through five years	251,859
Total held-to-maturity debt securities	\$ 351,708

The contractual maturities of Navy Federal's AFS debt securities as of December 31, 2019 were as follows:

	December 31, 2019	
	Amortized Cost	Fair Value
<i>(dollars in thousands)</i>		
Available-for-sale debt securities		
Due in one year or less	\$ 938,617	\$ 943,781
Due after one year through five years	3,704,995	3,777,804
Due after five years through ten years	4,995,058	5,147,520
Due after ten years	8,758,473	8,903,729
Total available-for-sale debt securities	\$ 18,397,143	\$ 18,772,834

Navy Federal held 3 HTM and 114 AFS debt securities in an unrealized loss position at December 31, 2019. All securities in an unrealized loss position were reviewed individually to determine whether those losses were caused by an other-than-temporary decline in fair value. Navy Federal makes a determination of whether unrealized losses are other-than-temporary based on the following factors: whether Navy Federal intends to sell or hold the security until its costs can be recovered, the nature of the security, the portion of unrealized losses that are attributable to credit losses and the financial condition of the issuer of the security. Navy Federal does not intend to sell nor would Navy Federal be, more likely than not, required to sell these securities before recovering their amortized cost basis. The unrealized losses associated with these investments are not a result of changes in the credit quality of the issuers; rather, the losses are reflective of changing market interest rates. Navy Federal expects to recover the entire cost basis of these securities as there were no declines in the fair value that were considered other-than-temporary during the years ended December 31, 2019 and 2018.

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The following tables present HTM and AFS debt securities at fair value and their associated gross unrealized losses broken down by the amount of time the investments have been in a loss position:

December 31, 2019						
	Less than 12 Months		12 Months or Longer		Total	
<i>(dollars in thousands)</i>	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Held-to-maturity debt securities	\$ 200,255	\$ (778)	\$ -	\$ -	\$ 200,255	\$ (778)
Available-for-sale debt securities						
U.S. government and federal agency securities	1,007,291	(24,175)	148,689	(1,798)	1,155,980	(25,973)
Residential mortgage-backed securities	1,109,796	(6,246)	885,431	(10,331)	1,995,227	(16,577)
Commercial mortgage-backed securities	26,944	(90)	-	-	26,944	(90)
Bank notes and corporate bonds	105,499	(611)	-	-	105,499	(611)
Municipal securities	55,025	(2,216)	8,698	(23)	63,723	(2,239)
Total available-for-sale debt securities	2,304,555	(33,338)	1,042,818	(12,152)	3,347,373	(45,490)
Total debt securities	\$ 2,504,810	\$ (34,116)	\$ 1,042,818	\$ (12,152)	\$ 3,547,628	\$ (46,268)

December 31, 2018						
	Less than 12 Months		12 Months or Longer		Total	
<i>(dollars in thousands)</i>	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Held-to-maturity debt securities	\$ 220	\$ -	\$ 396,309	\$ (3,232)	\$ 396,529	\$ (3,232)
Available-for-sale debt securities						
U.S. government and federal agency securities	199,496	(340)	4,535,410	(169,424)	4,734,906	(169,764)
Residential mortgage-backed securities	83,450	(1,009)	4,710,523	(135,408)	4,793,973	(136,417)
Commercial mortgage-backed securities	125,057	(960)	311,600	(12,444)	436,657	(13,404)
Bank notes and corporate bonds	1,282,662	(32,857)	1,525,358	(90,260)	2,808,020	(123,117)
Municipal securities	16,924	(284)	114,254	(1,980)	131,178	(2,264)
Non-U.S. government securities	54,173	(592)	144,549	(8,493)	198,722	(9,085)
Total available-for-sale debt securities	1,761,762	(36,042)	11,341,694	(418,009)	13,103,456	(454,051)
Total debt securities	\$ 1,761,982	\$ (36,042)	\$ 11,738,003	\$ (421,241)	\$ 13,499,985	\$ (457,283)

As of December 31, 2019 and 2018, Navy Federal had pledged \$152.0 million and \$62.8 million, respectively, of investment securities as collateral with counterparties for derivative transactions under master netting agreements. As of December 31, 2019 and 2018, Navy Federal pledged zero and \$258.1 million, respectively, of U.S. Treasury and federal agency securities as collateral for borrowed funds under repurchase agreements. For securities sold under agreements to repurchase, Navy Federal would be obligated to provide additional collateral in the event of a significant decline in fair value of the collateral pledged. The risk is managed by monitoring the liquidity and credit quality of the collateral, as well as the maturity profile of the transactions. See Note 11: Borrowed Funds for maturity information of the associated liabilities.

Note 4: Loans and Allowance for Loan Losses

Navy Federal's loan portfolio consists of consumer, credit card and real estate loans.

The composition of Navy Federal's loans by portfolio and delinquency status as of December 31, 2019 and 2018 was as follows:

(dollars in thousands)	December 31, 2019					
	Current	30-89 Days Delinquent	Non-Performing ⁽¹⁾	Total Delinquent Loans	Unamortized Cost/ (Deferred Fee)	Total Loans
Consumer loans	\$ 20,710,824	\$ 336,242	\$ 163,381	\$ 499,623	\$ 39,615	\$ 21,250,062
Credit card loans	19,144,736	338,631	268,216	606,847	5,433	19,757,016
Mortgage loans	36,988,681	416,135	211,069	627,204	(212,976)	37,402,909
Equity loans	2,968,897	28,453	11,708	40,161	23,583	3,032,641
Total loans to members	\$ 79,813,138	\$ 1,119,461	\$ 654,374	\$ 1,773,835	\$ (144,345)	\$ 81,442,628

⁽¹⁾ Non-performing loans represent non-accrual status loans that are 90 days or more past due.

(dollars in thousands)	December 31, 2018					
	Current	30-89 Days Delinquent	Non-Performing ⁽¹⁾	Total Delinquent Loans	Unamortized Cost/ (Deferred Fee)	Total Loans
Consumer loans	\$ 19,505,537	\$ 298,983	\$ 139,213	\$ 438,196	\$ 33,934	\$ 19,977,667
Credit card loans	16,602,471	281,540	226,665	508,205	5,286	17,115,962
Mortgage loans	33,621,618	372,160	157,024	529,184	(199,297)	33,951,505
Equity loans	2,762,680	26,603	12,340	38,943	19,124	2,820,747
Total loans to members	\$ 72,492,306	\$ 979,286	\$ 535,242	\$ 1,514,528	\$ (140,953)	\$ 73,865,881

⁽¹⁾ Non-performing loans represent non-accrual status loans that are 90 days or more past due.

Credit Quality

Navy Federal closely monitors the credit quality of its loan portfolio based on economic conditions, loan performance trends and certain risk attributes. The risks in Navy Federal's consumer and credit card loans portfolio correlate to broad economic trends, which are monitored in conjunction with borrowers' risk attributes. The risks that may affect the default experience on Navy Federal's mortgage and equity loans portfolio include changes in home prices in various geographic locations, which are monitored in conjunction with various loan attributes such as vintage, product type and property type. This information is utilized to evaluate the appropriateness of the allowance for loan losses. Credit quality indicators, as described below, are obtained and updated every month.

Consumer Loans

Navy Federal uses delinquency status as an indicator of credit quality for consumer loans. Refer to the loan composition and delinquency status table above for information as of December 31, 2019 and 2018.

Credit Card Loans

Navy Federal uses delinquency status as an indicator of credit quality for credit card loans. Refer to the loan composition and delinquency status table above for information as of December 31, 2019 and 2018.

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Mortgage Loans

Navy Federal uses FICO score as an indicator of credit quality for mortgage loans held for investment, which consisted of the following as of December 31, 2019 and 2018:

(dollars in thousands)	December 31,			
FICO	2019 ⁽¹⁾		2018 ⁽²⁾	
Greater than or Equal to 610	\$	35,035,074	\$	32,569,252
Less than 610		2,576,927		1,594,278
Total	\$	37,612,001	\$	34,163,530

⁽¹⁾ Excludes deferred fee, net of \$(213.0) million, other adjustments of \$(36.9) million and loans in process of \$40.8 million.

⁽²⁾ Excludes deferred fee, net of \$(199.3) million, other adjustments of \$(37.6) million and loans in process of \$24.9 million.

Equity Loans

Navy Federal uses delinquency status and FICO score as indicators of credit quality for equity loans, which consisted of the following as of December 31, 2019 and 2018:

December 31, 2019				
(dollars in thousands)	FICO Score			
Delinquency Status	Less than 610	Greater than or Equal to 610	Total ⁽¹⁾	
Performing	\$ 109,874	\$ 2,889,531	\$ 2,999,405	
60+ days and foreclosure	12,451	6,049	18,500	
Total	\$ 122,325	\$ 2,895,580	\$ 3,017,905	

⁽¹⁾ Excludes unamortized cost of \$23.6 million, loans in process of \$2.7 million and other adjustments of \$(11.5) million.

December 31, 2018				
(dollars in thousands)	FICO Score			
Delinquency Status	Less than 610	Greater than or Equal to 610	Total ⁽¹⁾	
Performing	\$ 98,576	\$ 2,690,861	\$ 2,789,437	
60+ days and foreclosure	14,662	4,283	18,945	
Total	\$ 113,238	\$ 2,695,144	\$ 2,808,382	

⁽¹⁾ Excludes unamortized cost of \$19.1 million, loans in process of \$3.8 million and other adjustments of \$(10.6) million.

Allowance for Loan Losses

Changes in the allowance for loan and lease losses during the years ended December 31, 2019 and 2018 were as follows:

December 31, 2019					
(dollars in thousands)	Consumer	Credit Cards	Real Estate	Total	
Allowance for credit losses:					
Balance, beginning of year	\$ 499,784	\$ 896,635	\$ 79,523	\$ 1,475,942	
Provision expense	500,272	1,005,188	15,384	1,520,844	
Loans charged off	(602,365)	(928,285)	(17,745)	(1,548,395)	
Recoveries	111,131	71,020	8,481	190,632	
Net change in allowance for unfunded commitments	119	(7,291)	-	(7,172)	
Balance, end of year	\$ 508,941	\$ 1,037,267	\$ 85,643	\$ 1,631,851	
Ending balance: loans individually evaluated for impairment	\$ 165,305	\$ 221,711	\$ 64,192	\$ 451,208	
Ending balance: loans collectively evaluated for impairment	\$ 342,800	\$ 815,556	\$ 19,300	\$ 1,177,656	
Ending balance: loans acquired with deteriorated credit quality	\$ 836	\$ -	\$ 2,151	\$ 2,987	
Loan amount (excluding allowance):					
Ending balance: loans individually evaluated for impairment	\$ 851,820	\$ 614,503	\$ 1,137,299	\$ 2,603,622	
Ending balance: loans collectively evaluated for impairment	\$ 20,396,349	\$ 19,142,513	\$ 39,285,371	\$ 78,824,233	
Ending balance: loans acquired with deteriorated credit quality	\$ 1,893	\$ -	\$ 12,880	\$ 14,773	

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(dollars in thousands)	December 31, 2018			
	Consumer	Credit Cards	Real Estate	Total
Allowance for credit losses:				
Balance, beginning of year	\$ 485,152	\$ 693,150	\$ 107,397	\$ 1,285,699
Provision expense	503,510	956,438	(13,344)	1,446,604
Loans charged off	(579,473)	(794,758)	(24,311)	(1,398,542)
Recoveries	90,726	50,358	9,781	150,865
Net change in allowance for unfunded commitments	(131)	(8,553)	-	(8,684)
Balance, end of year	\$ 499,784	\$ 896,635	\$ 79,523	\$ 1,475,942
Ending balance: loans individually evaluated for impairment	\$ 178,113	\$ 181,968	\$ 63,628	\$ 423,709
Ending balance: loans collectively evaluated for impairment	\$ 319,274	\$ 714,667	\$ 13,328	\$ 1,047,269
Ending balance: loans acquired with deteriorated credit quality	\$ 2,397	\$ -	\$ 2,567	\$ 4,964
Loan amount (excluding allowance):				
Ending balance: loans individually evaluated for impairment	\$ 899,728	\$ 514,202	\$ 1,248,089	\$ 2,662,019
Ending balance: loans collectively evaluated for impairment	\$ 19,074,164	\$ 16,601,760	\$ 35,508,196	\$ 71,184,120
Ending balance: loans acquired with deteriorated credit quality	\$ 3,775	\$ -	\$ 15,967	\$ 19,742

Changes in the allowance for unfunded commitments during the years ended December 31, 2019 and 2018 were as follows:

(dollars in thousands)	2019	2018
Balance, beginning of year	\$ 47,453	\$ 38,769
Net change in allowance for unfunded commitments	7,172	8,684
Balance, end of year	\$ 54,625	\$ 47,453

Troubled Debt Restructurings

TDRs are individually evaluated for impairment beginning in the month of restructuring. For loans that have not been approved for foreclosure or discharged under Chapter 7 bankruptcy, impairment is measured as the difference between the net carrying amount of the loan, less any fees received to affect the restructuring, and the modified future expected cash flows discounted at the loan's original effective interest rate. For real estate loans approved for foreclosure, impairment is measured by the difference between the recorded investment and the collateral value, net of costs to sell. Chapter 7 bankruptcy TDRs are considered to be dependent solely on the collateral for repayment. The loans are measured based on the estimated fair value of the collateral less estimated cost to sell and a charge-off is recorded if the carrying value exceeds the fair value of the collateral.

The following tables summarize the financial impact, by concession type, of loans that became TDRs during the years ended December 31, 2019 and 2018:

(dollars in thousands)	2019 ⁽¹⁾				
	Interest Rate Reduction and Term Extension	Interest Rate Reduction	Term Extension	Other ⁽²⁾	Total
Consumer	\$ 27,183	\$ 24,174	\$ 34,589	\$ 8,848	\$ 94,794
Credit card	-	143,477	-	4,225	147,702
Real estate	7,130	110	8,767	790	16,797
Total	\$ 34,313	\$ 167,761	\$ 43,356	\$ 13,863	\$ 259,293

⁽¹⁾ Excludes loans that were classified as TDRs in prior years and re-modified during the year.

⁽²⁾ Includes TDR loans resulting from actions taken by a bankruptcy court, such as the reduction of the loan's contractual principal or interest, or where the borrower has been released from personal liability.

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(dollars in thousands)	2018 ⁽¹⁾				
	Interest Rate Reduction and Term Extension	Interest Rate Reduction	Term Extension	Other ⁽²⁾	Total
Consumer	\$ 28,022	\$ 33,622	\$ 51,249	\$ 7,740	\$ 120,633
Credit card	-	131,999	-	3,722	135,721
Real estate	6,747	116	10,228	1,322	18,413
Total	\$ 34,769	\$ 165,737	\$ 61,477	\$ 12,784	\$ 274,767

⁽¹⁾ Excludes loans that were classified as TDRs in prior years and re-modified during the year.

⁽²⁾ Includes TDR loans resulting from actions taken by a bankruptcy court, such as the reduction of the loan's contractual principal or interest, or where the borrower has been released from personal liability.

Subsequent to designation as a TDR, interest income is recognized based on a loan's modified expected cash flows and revised effective interest rate. Additional impairment is recognized for TDRs that exhibit further credit deterioration after modification.

For the year ended December 31, 2019, TDRs that were more than 90 days delinquent within the first 12 months after modification totaled \$310.6 million, which included \$130.3 million of consumer loans, \$114.2 million of credit card loans and \$66.1 million of real estate loans.

For the year ended December 31, 2018, TDRs that were more than 90 days delinquent within the first 12 months after modification totaled \$270.7 million, which included \$141.4 million of consumer loans, \$78.7 million of credit card loans and \$50.6 million of real estate loans.

Impaired Loans

Interest income was not recognized on loans that remained impaired and did not return to performing status during the years ended December 31, 2019 and 2018. Interest income on impaired loans in non-accrual status is recognized on a cash basis. The following table represents information regarding loans individually evaluated for impairment as of and for the years ended December 31, 2019 and 2018:

(dollars in thousands)	December 31, 2019				
	Loan Amount	Associated Allowance	Average Balance	Interest Income (Accrual Basis)	Interest Income (Cash Basis)
Impaired loans with an associated allowance					
Consumer	\$ 845,569	\$ 165,305	\$ 870,135	\$ 69,070	\$ 74,073
Credit card	605,936	221,711	554,579	57,045	52,641
Real estate	950,260	64,192	844,297	37,864	38,371
Total impaired loans with an associated allowance	\$ 2,401,765	\$ 451,208	\$ 2,269,011	\$ 163,979	\$ 165,085
Impaired loans without an associated allowance					
Consumer	\$ 6,251	\$ -	\$ 5,640	\$ 679	\$ 688
Credit card	8,567	-	9,774	1,461	1,444
Real estate	187,039	-	348,398	6,258	6,290
Total impaired loans without an associated allowance	\$ 201,857	\$ -	\$ 363,812	\$ 8,398	\$ 8,422
Total impaired loans	\$ 2,603,622	\$ 451,208	\$ 2,632,823	\$ 172,377	\$ 173,507

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	December 31, 2018				
	Loan Amount	Associated Allowance	Average Balance	Interest Income (Accrual Basis)	Interest Income (Cash Basis)
<i>(dollars in thousands)</i>					
Impaired loans with an associated allowance					
Consumer	\$ 894,700	\$ 178,113	\$ 847,413	\$ 69,659	\$ 76,384
Credit card	503,222	181,968	442,731	43,403	40,002
Real estate	738,333	63,628	706,013	30,135	29,805
Total impaired loans with an associated allowance	\$ 2,136,255	\$ 423,709	\$ 1,996,157	\$ 143,197	\$ 146,191
Impaired loans without an associated allowance					
Consumer	\$ 5,028	\$ -	\$ 4,406	\$ 1,110	\$ 923
Credit card	10,980	-	8,301	2,088	1,968
Real estate	509,756	-	474,764	17,650	17,193
Total impaired loans without an associated allowance	\$ 525,764	\$ -	\$ 487,471	\$ 20,848	\$ 20,084
Total impaired loans	\$ 2,662,019	\$ 423,709	\$ 2,483,628	\$ 164,045	\$ 166,275

Note 5: Loan Sales and Continuing Involvement in Assets Transferred

In the normal course of business, Navy Federal originates and transfers qualifying residential mortgage loans in securitization or sales transactions in which it has continuing involvement. Loans are sold to Federal National Mortgage Association and Federal Home Loan Mortgage Corporation, collectively Government Sponsored Enterprises (GSEs), and Government National Mortgage Association (GNMA). The GSEs and the GNMA generally securitize loans into mortgage-backed securities that are sold to third-party investors in the secondary market or retained by Navy Federal for investment purposes. Navy Federal may also sell loans that were previously retained for investment purposes to private third-party investors.

Navy Federal originated \$18.5 billion and \$15.3 billion, and sold/securitized \$8.9 billion and \$8.1 billion, of first mortgage loans during the years ended December 31, 2019 and 2018, respectively. The following table provides a summary of the cash flows exchanged between Navy Federal and transferees on all loans transferred during the years ended December 31:

<i>(dollars in thousands)</i>	2019	2018
Cash from sale of mortgage loans and mortgage-backed securities	\$ 9,060,074	\$ 7,714,985
Repurchase of previously transferred loans	25,828	37,800
Contractual servicing fees received	153,794	132,594

During the year ended December 31, 2019, Navy Federal reclassified \$975.8 million of mortgage loans from held for investment to MLAS. Navy Federal transferred these loans to MLAS at fair value and subsequently sold them for cash proceeds of \$993.6 million and recognized MSR assets of \$13.1 million for the year ended December 31, 2019. During the year ended December 31, 2018, Navy Federal did not reclassify any loans from held for investment to MLAS.

Gains on the sale of MLAS are included in Net gain on mortgage loans in the Consolidated Statements of Income and totaled \$185.7 million and \$180.5 million for the years ended December 31, 2019 and 2018, respectively. Navy Federal recorded \$63.5 million of fair value gains and \$12.9 million of fair value losses for the years ended December 31, 2019 and 2018, respectively, in Net gain on mortgage loans in the Consolidated Statements of Income.

Navy Federal's continuing involvement in loans transferred includes ongoing servicing, repurchasing previously transferred loans under certain conditions, loss-sharing agreements, holding of mortgage-backed securities issued by securitization and obligations related to standard representations and warranties. Navy Federal may also incur incremental obligations related to various forms of credit enhancements afforded to third-party investors for securities partially backed by the transferred loans.

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Servicing

Navy Federal retains MSR on loans transferred in sale transactions and loans securitized by the GSEs and GNMA. MSR assets are recognized at fair value on the date of sale or securitization. Actual and expected loan constant prepayment rates (CPR), discount rates, servicing costs and other economic factors are considered in determining the MSR fair value. The MSR valuation is sensitive to interest rate and prepayment risk. The sensitivity analysis of the hypothetical effect on fair value of MSR as a result of a 10% and 20% adverse change in the CPR and option adjusted spread at December 31 is presented below:

<i>(dollars in thousands)</i>	2019	2018
Weighted-average life (years)	6.64	7.10
Weighted-average CPR	9.59%	8.52%
Decline in fair value from 10% adverse change	\$ 17,289	\$ 14,164
Decline in fair value from 20% adverse change	33,392	27,436
Option adjusted spread	9.41%	9.00%
Decline in fair value from 10% adverse change	\$ 16,120	\$ 14,882
Decline in fair value from 20% adverse change	31,202	28,834

See Note 16: Fair Value Measurement for further details.

Navy Federal earns servicing and other ancillary fees for its role as servicer. Navy Federal's servicing fees are priced based on parameters set by the GSEs and GNMA. Navy Federal's servicing revenue is included in Mortgage servicing revenue in the Consolidated Statements of Income. During the years ended December 31, 2019 and 2018, Navy Federal received \$3.1 million and \$2.5 million, respectively, of late charges and miscellaneous fees, which is included in Fee and other income in the Consolidated Statements of Income.

Navy Federal's responsibilities as servicer typically include collecting and remitting monthly principal and interest payments, maintaining escrow deposits, performing loss mitigation and foreclosure activities, and in certain instances, funding servicing advances that have not yet been collected from the borrower. Navy Federal recognizes servicing advances in Accounts receivable and accrued interest on the Consolidated Statements of Financial Condition. Servicing advances as of December 31, 2019 and 2018 totaled \$33.0 million and \$32.0 million, respectively.

The following table provides the outstanding and delinquent loan balances of transferred loans for which Navy Federal retains servicing rights at December 31:

<i>(dollars in thousands)</i>	2019	2018
Principal balances of loans serviced ⁽¹⁾	\$ 37,426,413	\$ 33,458,117
Delinquent loans ^{(1), (2)}	243,872	212,215

⁽¹⁾ Includes loans that are in the GNMA early pool buyback program of \$141.3 million and \$108.8 million at December 31, 2019 and 2018, respectively.

⁽²⁾ Serviced delinquent loans are 60 days or more past due.

Retained Investment in GNMA Securities

GNMA securities backed by Navy Federal loans may be retained as investments by Navy Federal and classified as AFS debt securities. See Note 3: Investments for details.

In accordance with ASC 860-30, *Secured Borrowing and Collateral*, the effect of two negative changes in each of the key assumptions used to determine the fair value of Navy Federal's investment in GNMA securities must be disclosed. The negative effect of each key assumption change must be calculated independently, holding all other assumptions constant. The table below details the key assumptions used in Navy Federal's analysis, specifically, CPR, anticipated credit losses and weighted-average life.

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(dollars in thousands)	2019	2018
Weighted-average CPR	13.97%	12.49%
Anticipated credit losses ⁽¹⁾	\$ -	\$ -
Weighted-average life (years)	4.49	5.02

⁽¹⁾ GNMA securities are fully collateralized by government-insured loans and as such, there are no anticipated significant credit losses.

The sensitivity analysis of the hypothetical effect on fair value of GNMA securities as a result of a 10% and 20% adverse change in the CPR at December 31 is presented below:

(dollars in thousands)	2019	2018
Weighted-average CPR		
Decline in fair value from 10% adverse change	\$ 1,150	\$ 344
Decline in fair value from 20% adverse change	2,438	728

The sensitivities in the table above are hypothetical and may not be indicative of actual results. The effect of a variation in a particular assumption on the fair value is calculated independently of changes in other assumptions. Further, changes in fair value based on variations in assumptions generally cannot be extrapolated because the relationship of the change in assumption on the fair value may not be linear.

The fair value of GNMA securities held by Navy Federal was \$778.5 million and \$927.1 million as of December 31, 2019 and 2018, respectively.

GNMA Early Pool Buyback Program

Navy Federal has the option to repurchase pooled loans out of GNMA securities when members fail to make payments for three consecutive months. As Navy Federal has the unilateral ability to repurchase these loans, effective control over the loans has been regained. Navy Federal recognizes an asset in MLAS and a corresponding liability in Other liabilities on the Consolidated Statements of Financial Condition regardless of whether it has the intent to repurchase the loan. At December 31, 2019 and 2018, UPB associated with the Early Pool Buyback Program recognized in MLAS and Other liabilities totaled \$141.3 million and \$108.8 million, respectively.

Financial Guarantees Related to Recourse Provided in Assets Transferred

Representations and Warranties

For mortgage loans transferred in sale transactions or securitizations to the GSEs, GNMA and other investors, Navy Federal has made representations and warranties that the loans meet specified requirements. These requirements typically relate to collateral, underwriting standards, validation of certain borrower representations in connection with the loan and the use of standard legal documentation. In connection with the sale of loans to the GSEs, GNMA and other investors, Navy Federal may be required to repurchase the loan or indemnify the respective entity for losses due to breaches of these representations and warranties.

Navy Federal recognizes a liability for estimated losses related to representations and warranties from the inception of the obligation when the loans are sold. This liability is included in Other liabilities on the Consolidated Statements of Financial Condition. In the Consolidated Statements of Income, the related expense is included as an offset to Net gain on mortgage loans for loans sold during the current period, or in Servicing expense for re-measurement of the liability related to loans sold in prior periods. Navy Federal's estimated representations and warranties liability at December 31, 2019 and 2018 was \$24.1 million and \$33.6 million, respectively.

Management believes the liability for representations and warranties appropriately reflects the estimated probable losses on indemnification and repurchase claims for all loans sold and outstanding as of December 31, 2019 and 2018. In making these estimates, Navy Federal considers the losses expected to be incurred over the weighted average life of the sold loans. While management seeks to obtain all relevant information in estimating this liability, the estimation process is inherently uncertain and imprecise and, accordingly, it is reasonably possible future losses could be more or less than Navy Federal's established liability. At December 31, 2019 and 2018, Navy Federal estimates it is reasonably possible it could incur additional losses in excess of its accrued liability of up to approximately \$47.6 million and \$82.0 million, respectively.

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The total UPB subject to representations and warranties was \$36.4 billion and \$32.5 billion as of December 31, 2019 and 2018, respectively.

Loss-Sharing Agreements

Navy Federal sold mortgage loans to the GSEs under loss-sharing agreements dated from 2006 to 2019. Navy Federal must indemnify the GSEs for losses related to loans with higher loan-to-value (LTV) ratios through the life of the loans or loans with higher LTV and no private mortgage insurance that occur during a period of three to four years from the applicable settlement date. The following table summarizes the outstanding balance of loans sold and payments made for losses under these agreements during the years ended December 31, 2019 and 2018:

<i>(dollars in thousands)</i>	UPB of Loans Sold as of 12/31	Maximum Future Exposure	Losses Paid During the Year Ended 12/31	Carrying Value of Liability as of 12/31
2019	\$ 809,131	\$ 94,209	\$ 1,486	\$ 9,114
2018	1,048,310	115,163	4,000	17,292

The liability recognized for estimated losses related to these loss-sharing agreements is included in Other liabilities on the Consolidated Statements of Financial Condition. In the Consolidated Statements of Income, the related expense is included as an offset to Net gain on mortgage loans for loans sold during the current period, or in Servicing expense for any re-measurement of the liability related to loans sold in prior years.

Note 6: Derivative Instruments and Hedging Activities

Navy Federal's risk management strategies include the use of derivatives as economic hedges and derivatives designated as qualifying accounting hedges. The goal of these strategies is to mitigate market risk so that movements in interest rates do not adversely affect the value of Navy Federal's assets or liabilities, earnings or future cash flows. The fair value of derivative instruments in a gain or loss position, net of legally enforceable master netting agreements, are reported in Other assets and Other liabilities, respectively, on the Consolidated Statements of Financial Condition as of December 31, 2019 and 2018.

The following table presents the notional amount and fair value of derivative instruments on a gross basis:

(dollars in thousands)	December 31, 2019			December 31, 2018		
	Notional Amount	Derivatives at Fair Value		Notional Amount	Derivatives at Fair Value	
		Asset	Liability		Asset	Liability
Derivatives not designated as accounting hedges:						
Interest rate lock commitments	\$ 981,751	\$ 22,178	\$ 162	\$ 750,621	\$ 19,937	\$ 2
Forward sales contracts ⁽¹⁾	2,890,000	1,958	5,297	1,496,500	160	21,788
Total derivatives not designated as accounting hedges	\$ 3,871,751	\$ 24,136	\$ 5,459	\$ 2,247,121	\$ 20,097	\$ 21,790
Derivatives designated as accounting hedges:						
Interest rate contracts:						
Fair value interest rate contracts	\$ 10,000	\$ 2	\$ -	\$ 10,000	\$ -	\$ 13
Cash flow interest rate contracts	2,950,000	2,335	-	2,950,000	-	11,227
Total derivatives designated as accounting hedges	\$ 2,960,000	\$ 2,337	\$ -	\$ 2,960,000	\$ -	\$ 11,240
Total derivative instruments, gross	\$ 6,831,751	\$ 26,473	\$ 5,459	\$ 5,207,121	\$ 20,097	\$ 33,030
Less: Legally enforceable master netting agreements		(1,958)	(1,958)		(160)	(160)
Total derivative instruments, net		\$ 24,515	\$ 3,501		\$ 19,937	\$ 32,870

⁽¹⁾ As of December 31, 2019, the notional amount related to forward contracts in assets and liabilities was \$90.0 million and \$3.0 billion, respectively. As of December 31, 2018, the notional amount related to forward contracts in assets and liabilities was \$15.0 million and \$1.5 billion, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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Offsetting Derivative Financial Instruments

As discussed in Note 1: Summary of Significant Accounting Policies, some of Navy Federal's derivative instruments are subject to legally enforceable master netting agreements, which allow Navy Federal to settle positive and negative positions held with the same counterparty on a net basis. As such, Navy Federal reports these positions on the Consolidated Statements of Financial Condition on a net basis.

The following tables present total gross derivative assets and liabilities at December 31, 2019 and 2018, which are adjusted to reflect the effects of legally enforceable master netting agreements. The following tables also include financial instruments or cash collateral related to legally enforceable master netting agreements that represent securities or cash collateral received or pledged with the same counterparty. These amounts are not offset on the Consolidated Statements of Financial Condition, but are shown as a reduction to total derivative assets and liabilities to derive net derivative assets and liabilities.

	December 31, 2019					
	Gross Amounts Recognized	Gross Amounts Offset in Statement of Financial Condition ⁽¹⁾	Net Amounts Presented in Statement of Financial Condition	Gross Amounts Not Offset in Statement of Financial Condition		
				Financial Instruments Collateral ⁽²⁾	Cash Collateral ⁽²⁾	Net Amount
<i>(dollars in thousands)</i>						
Financial Assets						
Derivative instruments not subject to master netting agreements	\$ 22,178	\$ -	\$ 22,178	\$ -	\$ -	\$ 22,178
Derivative instruments subject to master netting agreements	4,295	(1,958)	2,337	-	-	2,337
Total derivative assets	\$ 26,473	\$ (1,958)	\$ 24,515	\$ -	\$ -	\$ 24,515
Financial Liabilities						
Derivative instruments not subject to master netting agreements	\$ (162)	\$ -	\$ (162)	\$ -	\$ -	\$ (162)
Derivative instruments subject to master netting agreements	(5,297)	1,958	(3,339)	3,116	223	-
Total derivative liabilities	(5,459)	1,958	(3,501)	3,116	223	(162)
Total	\$ 21,014	\$ -	\$ 21,014	\$ 3,116	\$ 223	\$ 24,353

⁽¹⁾ Includes offset by same counterparty where legally enforceable under master netting agreements.

⁽²⁾ Amounts are limited to the derivative asset/liability balance and, accordingly, do not include excess collateral received/pledged.

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	December 31, 2018					
	Gross Amounts Recognized	Gross Amounts Offset in Statement of Financial Condition ⁽¹⁾	Net Amounts Presented in Statement of Financial Condition	Gross Amounts Not Offset in Statement of Financial Condition		
				Financial Instruments Collateral ⁽²⁾	Cash Collateral ⁽²⁾	Net Amount
<i>(dollars in thousands)</i>						
Financial Assets						
Derivative instruments not subject to master netting agreements	\$ 19,937	\$ -	\$ 19,937	\$ -	\$ -	\$ 19,937
Derivative instruments subject to master netting agreements	160	(160)	-	-	-	-
Total derivative assets	\$ 20,097	\$ (160)	\$ 19,937	\$ -	\$ -	\$ 19,937
Financial Liabilities						
Derivative instruments not subject to master netting agreements	\$ (2)	\$ -	\$ (2)	\$ -	\$ -	\$ (2)
Derivative instruments subject to master netting agreements	(33,028)	160	(32,868)	11,240	19,216	(2,412)
Total derivative liabilities	(33,030)	160	(32,870)	11,240	19,216	(2,414)
Total	\$ (12,933)	\$ -	\$ (12,933)	\$ 11,240	\$ 19,216	\$ 17,523

⁽¹⁾ Includes offset by same counterparty where legally enforceable under master netting agreements.

⁽²⁾ Amounts are limited to the derivative asset/liability balance and, accordingly, do not include excess collateral received/pledged.

Derivatives Accounted For as Economic Hedges

Navy Federal is an active participant in the production of mortgage loans that are sold to investors in the secondary market. At origination, these loans are classified as MLAS on the Consolidated Statements of Financial Condition. Prior to origination, the corresponding IRLCs related to MLAS mortgage loans exposes Navy Federal to the risk of adverse changes in interest rates between the time of the loan commitment and the time Navy Federal funds the loan at origination. Navy Federal is also exposed to the risk of adverse changes in value after funding the loan up until the time when the loan is delivered to the investor. To offset this exposure, Navy Federal enters into forward sales contracts to deliver mortgage loans to investors at specified prices in the "To Be Announced" market (TBA securities). These forward sales contracts act as an economic hedge against the risk of changes in the value of both the IRLCs and the funded loans. Navy Federal accounts for these derivatives as economic hedges in accordance with ASC 815, *Derivatives and Hedging*.

The table below presents gains and losses resulting from derivatives accounted for as economic hedges for the years ended December 31:

<i>(dollars in thousands)</i>		2019	2018
Derivative Instruments	Location of Gain/(Loss) Recognized in Earnings		
Interest rate lock commitments	Net gain on mortgage loans	\$ (2,080)	\$ 2,596
Forward sales contracts	Net gain on mortgage loans	\$ (18,289)	\$ (18,764)
Total		\$ (20,369)	\$ (16,168)

Derivatives Accounted For as Qualifying Accounting Hedges

Under the provisions of ASC 815, *Derivatives and Hedging*, derivative instruments may be designated as a qualifying fair value or cash flow hedge.

Fair Value Accounting Hedges

Navy Federal uses qualifying fair value hedges to protect certain fixed-rate investments against adverse changes in fair value attributable to changes in interest rates. For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative instrument and the gain or loss on the hedged item attributable to the hedged risk are recognized in current earnings. When interest rate fluctuations result in changes in the fair value of fixed-rate investments, the gains or losses on the derivative instruments are highly effective in offsetting the change in fair value.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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The table below summarizes recognized gains and losses related to derivatives designated as fair value hedges during the years ended December 31:

<i>(dollars in thousands)</i>		2019	2018
Changes in Fair Value	Location of Changes in Fair Value Recognized in Earnings		
Interest rate swaps hedging fixed-rate investments	Fee and other income	\$ (231)	\$ 116
Hedged fixed-rate investments attributable to risk being hedged	Fee and other income	473	130

As of December 31, 2019, the following amounts were recorded on the Consolidated Statements of Financial Condition related to cumulative basis adjustments for fair value hedges:

<i>(dollars in thousands)</i>			
Line Item on Statements of Financial Condition Which Hedged Item is Included	Carrying Amount of Hedged Asset	Cumulative Fair Value Hedging Adjustments Included in Carrying Amount of Hedged Asset	
Available-for-sale debt securities	\$ 9,926	\$	(19)

Cash Flow Accounting Hedges

Navy Federal funds a portion of its operations with variable rate debt obligations. Navy Federal uses pay-fixed interest rate swaps to hedge the variability in cash flows related to existing and anticipated replacement funding that reprices based on the London Inter-bank Offered Rate. For derivative instruments that are designated and qualify as cash flow hedges, the gain or loss on the derivative instrument is reported in AOCI and reclassified into earnings in the same period during which the hedged transaction affects earnings and is presented in the same Consolidated Statements of Income line item as the earnings effect of the hedged item.

The table below summarizes gains and losses on cash flow hedges for the years ended December 31:

	2019		2018		2019		2018		
<i>(dollars in thousands)</i>	(Loss) Recognized in AOCI		Location of (Loss) Reclassified from AOCI into Earnings		Amount of (Loss) Reclassified from AOCI into Earnings				
Interest rate contracts	\$	(149,942)	\$	(21,654)	Interest on borrowed funds	\$	(9,435)	\$	(8,554)

During the next 12 months, net losses in AOCI of approximately \$29.8 million on derivative instruments that qualify as cash flow hedges are expected to be reclassified into earnings.

For open or future cash flow hedges, the maximum length of time over which forecasted transactions are or will be hedged is approximately 13 years.

Note 7: Commitments and Contingencies

Commitments

In the normal course of business, Navy Federal enters into conditional commitments to extend credit and makes financial guarantees to help meet the financing needs of its members. Unfunded loan commitments are amounts Navy Federal has agreed to lend to a member generally as long as the member remains in good standing on existing loans. Commitments generally have fixed expiration dates or other termination clauses. Navy Federal uses the same credit policies in making commitments as it does for all loans to members, and accordingly, at December 31, 2019 and 2018, the potential credit risk related to these commitments could be similar to existing loans, if these commitments became funded loans.

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Commitment balances as of December 31, 2019 and 2018 were as follows:

<i>(dollars in thousands)</i>	2019	2018
Credit cards	\$ 27,239,340	\$ 22,703,476
Home equity lines of credit	1,560,282	1,407,564
Checking lines of credit	1,165,123	1,170,453
Pre-approved auto loans	578,220	569,186
Other	85,060	106,193
Total	\$ 30,628,025	\$ 25,956,872

Contingencies

Navy Federal is party to various legal and regulatory actions normally associated with financial institutions, the aggregate effect of which, in the opinions of management and legal counsel, would not be material to Navy Federal's consolidated financial statements.

Note 8: Property, Plant and Equipment

The following is a summary of Navy Federal's property, plant and equipment as of December 31:

<i>(dollars in thousands)</i>	2019	2018
Land and buildings	\$ 1,881,083	\$ 1,677,281
Equipment, furniture and fixtures	647,286	477,989
Computer software and capitalized IT assets	796,088	679,527
Leasehold improvements	184,026	169,618
Subtotal	3,508,483	3,004,415
Less: Accumulated depreciation/amortization	(1,233,089)	(1,074,248)
Total	\$ 2,275,394	\$ 1,930,167

Navy Federal has obligations under a number of non-cancelable operating leases. The future minimum payments under the terms of the leases as of December 31, 2019 were as follows:

<i>(dollars in thousands)</i>	Amount
2020	\$ 29,035
2021	26,336
2022	21,225
2023	17,053
2024	13,164
Thereafter	34,334
Total	\$ 141,147

Rent expense was \$33.9 million and \$30.5 million for the years ended December 31, 2019 and 2018, respectively, and is included in Office operations and equipment in the Consolidated Statements of Income.

Note 9: Goodwill

Navy Federal completed its annual impairment assessment as of September 30, 2019 and 2018 using a qualitative assessment and concluded there was no impairment. Navy Federal did not have any goodwill adjustment activities during the years ended December 31, 2019 and 2018.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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Note 10: Deposit Accounts

Navy Federal's deposit accounts consist of demand and time deposits. The aggregate amount of time deposits that meet or exceed the \$250,000 NCUA insurance limit, which is reported at the members' applicable account ownership category, was \$8.8 billion and \$6.3 billion at December 31, 2019 and 2018, respectively.

As of December 31, 2019, scheduled maturities of time deposits for each of the next five years were as follows:

<i>(dollars in thousands)</i>	Amount
2020	\$ 18,575,618
2021	8,147,308
2022	2,478,092
2023	2,037,499
2024	3,495,344

Overdrafts on demand deposits of \$83.7 million and \$72.6 million at December 31, 2019 and 2018, respectively, have been reclassified to Loans to members on the Consolidated Statements of Financial Condition.

Interest rates on deposit accounts are set by the Board of Directors and are based on an evaluation of current and future market conditions. Interest on deposit accounts is based on available earnings for each interest period and is not guaranteed by Navy Federal. In claims against the assets of Navy Federal, such as in the event of its liquidation, amounts in deposit accounts that exceed the \$250,000 NCUA insurance limit are subordinate to other liabilities of Navy Federal.

Note 11: Borrowed Funds

Navy Federal's borrowings as of December 31, 2019 and 2018 were as follows:

<i>(dollars in thousands)</i>	December 31, 2019				
	Amount Outstanding	Coupon	Fixed/Float	Payment	Maturities
FHLB borrowing	\$ 1,890,000	2.76% - 4.72%	Fixed	Monthly	2020 - 2037
FHLB borrowing	3,869,439	1.83% - 4.62%	Fixed	Quarterly	2020 - 2033
FHLB borrowing	4,500,000	1.74% - 2.08%	Float	Quarterly	2020 - 2022
Total FHLB borrowings	\$ 10,259,439				

<i>(dollars in thousands)</i>	December 31, 2018				
	Amount Outstanding	Coupon	Fixed/Float	Payment	Maturities
FHLB borrowing	\$ 500,000	2.31%	Fixed	At Maturity	2019
FHLB borrowing	2,688,800	2.41% - 4.72%	Fixed	Monthly	2019 - 2037
FHLB borrowing	4,419,439	1.01% - 4.62%	Fixed	Quarterly	2019 - 2036
FHLB borrowing	5,450,000	2.44% - 2.98%	Float	Quarterly	2019 - 2022
Total FHLB borrowings	\$ 13,058,239				
Securities sold under repurchase agreements	\$ 50,000	1.88%	Fixed	Quarterly	2019
Securities sold under repurchase agreements	200,000	3.25%	Float	Quarterly	2019
Total securities sold under repurchase agreements	\$ 250,000				
Total borrowed funds	\$ 13,308,239				

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The following table displays the amount of borrowed funds by maturity for each of the next five years and thereafter as of December 31, 2019:

<i>(dollars in thousands)</i>	Amount
2020	\$ 4,414,439
2021	500,000
2022	565,000
2023	50,000
2024	500,000
Thereafter	4,230,000
Total	\$ 10,259,439

During 2019, Navy Federal prepaid \$1.2 billion of its borrowings with the FHLB. In connection with this prepayment, Navy Federal incurred \$26.9 million of debt extinguishment costs which is included in Other non-interest expense in the Consolidated Statements of Income. Navy Federal did not make any prepayment of its borrowings during the year ended December 31, 2018.

As of December 31, 2019, Navy Federal pledged \$27.2 billion of consumer and credit card loans to the FRB as collateral for the ability to borrow up to \$20.9 billion. As of December 31, 2019, Navy Federal pledged \$30.6 billion in mortgage loans held for investment and \$0.8 billion in investment securities to the FHLB as collateral for the ability to borrow up to \$27.0 billion. As of December 31, 2018, Navy Federal pledged \$26.9 billion of consumer and credit card loans to the FRB as collateral for the ability to borrow up to \$20.7 billion. As of December 31, 2018, Navy Federal pledged \$27.7 billion in mortgage loans and \$0.9 billion in investment securities to the FHLB as collateral for the ability to borrow up to \$23.7 billion.

Navy Federal had the following unused lines of credit as of December 31:

<i>(dollars in thousands)</i>	2019	2018
Federal Reserve Bank	\$ 20,997,758	\$ 20,726,595
FHLB	16,539,321	10,528,967
Fed Funds	250,000	272,500
Total	\$ 37,787,079	\$ 31,528,062

Note 12: Retirement Benefit Plans

Navy Federal Credit Union Employees' Retirement Plan

Navy Federal Credit Union Employees' Retirement Plan (the Plan) is a defined benefit retirement plan with benefits based on set formulas. Navy Federal transitioned to a Cash Balance design as of January 1, 2001, but retained the Traditional design for those employees who opted to remain under the Traditional formula. The following describes how the benefits are calculated:

- **Cash Balance** – This design provides either a single sum payment upon retirement or a monthly annuity. The annuity option is available for each Cash Balance Plan participant who has a benefit value of more than \$5,000.
- **Traditional** – This design provides a lifetime of monthly retirement benefits, determined by a set formula. The formula is based on the final average earnings (an average of the three highest consecutive years of income) multiplied by 2%, times the length of employee service.

Retiree Medical Plan

Navy Federal provides to employees hired prior to January 1, 2009, postretirement benefits to offset the cost of medical insurance premiums or out-of-pocket medical expenses. The plan provides a lump sum, notionally credited, to a health reimbursement account equal to \$75 or \$100 (depending on the retiree's age on September 1, 2008), multiplied by the number of years of continuous service the retiree provided to Navy Federal, multiplied by a lump sum factor.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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The pension assets are recognized in Other assets and the retiree medical plan liabilities are recognized in Other liabilities on the Consolidated Statements of Financial Condition. The following table provides key balances and transaction amounts of the pension and retiree medical plans as of and for the year ended December 31:

	Pension		Retiree Medical	
	2019	2018	2019	2018
<i>(dollars in thousands)</i>				
Accumulated benefit obligation at year end	\$ 1,313,775	\$ 1,114,899	N/A	N/A
Projected benefit obligation at year end	1,467,650	1,238,325	66,246	57,097
Fair value of plan assets at year end	1,682,982	1,406,909	-	-
Over/(under) funded	215,332	168,584	(66,246)	(57,097)
Employer contributions	25,000	25,000	2,985	2,684
Plan participants' contributions	-	-	184	141
Benefits paid	(53,725)	(47,123)	(3,169)	(2,824)
Net periodic benefit cost	21,653	2,547	4,625	4,989

Navy Federal reports service cost and other components of net periodic benefit cost in Salaries and employee benefits in the Consolidated Statements of Income. The weighted-average assumptions used to determine the projected benefit obligation and net periodic benefit costs for the pension and retiree medical benefit plans for the years ended December 31 were as follows:

	Pension		Retiree Medical	
	2019	2018	2019	2018
Discount rate				
Projected benefit obligation	3.35%	4.35%	3.35%	4.35%
Net periodic benefit cost	4.35%	3.70%	4.35%	3.70%
Rate of compensation increase	4.43%	4.42%	N/A	N/A
Expected long-term rate of return	7.00%	6.50%	N/A	N/A

The long-term rate of return assumption represents the expected average rate to be earned on plan assets and future plan contributions to meet benefit obligations. The assumption is based on several factors, including the anticipated long-term asset allocation of plan assets, historical market index and plan returns and a forecast of future expected asset returns.

The amounts in AOCI that have not yet been recognized as components of net periodic benefit cost as of December 31 are:

	Pension		Retiree Medical	
	2019	2018	2019	2018
<i>(dollars in thousands)</i>				
Accumulated other comprehensive loss				
Net prior service cost	\$ 21,805	\$ 27,090	\$ 831	\$ 1,070
Net loss	221,658	259,774	16,468	8,718
Accumulated other comprehensive loss	\$ 243,463	\$ 286,864	\$ 17,299	\$ 9,788

The amounts recognized in AOCI for the years ended December 31, 2019 and 2018 consist of:

	Pension		Retiree Medical	
	2019	2018	2019	2018
<i>(dollars in thousands)</i>				
Amounts amortized during the year				
Net prior service cost	\$ (5,284)	\$ (5,284)	\$ (239)	\$ (239)
Net loss	(14,331)	(3,324)	(253)	(617)
Amounts arising during the year				
Net prior service cost	-	-	-	-
Net (gain)/loss	(23,786)	93,816	8,003	(3,328)
Total recognized in other comprehensive (income)/loss	\$ (43,401)	\$ 85,208	\$ 7,511	\$ (4,184)

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The amounts in AOCI expected to be recognized as components of net periodic benefit cost in 2020 are as follows:

<i>(dollars in thousands)</i>	Pension		Retiree Medical	
Net loss	\$	5,079	\$	853
Prior service cost		4,171		239
Total expected amortization	\$	9,250	\$	1,092

The following table discloses the benefits expected to be paid in the next 10 years:

<i>(dollars in thousands)</i>	Pension		Retiree Medical	
2020	\$	66,484	\$	3,128
2021		70,459		3,176
2022		74,697		3,226
2023		79,119		3,289
2024		82,752		3,342
2025-2029		465,976		17,597

The anticipated employer contribution for 2020 is \$25.0 million for the pension plan and \$3.1 million for the retiree medical benefit plan. The measurement date for the pension and retiree medical benefit plan for 2019 and 2018 was December 31.

The investment strategy of the Plan is to employ an investment approach, whereby a mix of equity and fixed-income investments are used to maximize the long-term return of plan assets at a prudent level of risk that includes consideration of benefit obligation volatility. The intent of this strategy is to keep the Plan well-funded over the long run. Risk tolerance is established through careful consideration of plan liabilities and plan-funded status. Investment risk is measured and monitored on an ongoing basis through annual liability measurements, periodic asset/liability studies and regular investment portfolio reviews.

As of December 31, 2019, the target allocation of plan assets was 25% U.S. equity securities, 40% global equity securities and 35% fixed-income securities. Most of the U.S. equity assets are invested in a large company index fund and in defensive equity funds with the balance in small- and mid-sized company equity securities. Most of the global equity allocation is in developed markets around the world, with the balance in emerging markets. The fixed-income allocation is comprised of a small allocation to cash to provide liquidity for benefit and expense payments, with the balance invested in intermediate and long-term bonds, the majority of which are investment-grade.

The tables below present the Plan's assets within the fair value hierarchy as described in Note 1: Summary of Significant Accounting Policies as of December 31:

<i>(dollars in thousands)</i>	December 31, 2019				
Asset Category	Level 1	Level 2	Level 3	Total	
U.S. equity securities	\$ 85,398	\$ -	\$ -	\$	85,398
Global equity securities	679,208	-	-		679,208
Fixed-income securities	319,839	186,213	-		506,052
Cash and cash equivalents	25,419	-	-		25,419
Total assets in the fair value hierarchy	\$ 1,109,864	\$ 186,213	\$ -	\$	1,296,077
Investments measured at net asset value:					386,906
Total investments				\$	1,682,983

<i>(dollars in thousands)</i>	December 31, 2018				
Asset Category	Level 1	Level 2	Level 3	Total	
U.S. equity securities	\$ 62,850	\$ -	\$ -	\$	62,850
Global equity securities	547,675	-	-		547,675
Fixed-income securities	275,224	136,181	-		411,405
Cash and cash equivalents	23,673	-	-		23,673
Total assets in the fair value hierarchy	\$ 909,422	\$ 136,181	\$ -	\$	1,045,603
Investments measured at net asset value:					361,306
Total investments				\$	1,406,909

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The following is a description of the valuation methodologies used to value fixed income securities that are classified within Level 2 of the fair value hierarchy. Municipal bonds, corporate bonds and corporate notes are valued based on yields currently available on comparable securities of issuers with similar credit ratings. Asset-backed securities are priced based on specific characteristics of the security, prepayment speeds, underlying collateral, and cash flows. Non-agency collateralized mortgage obligation securities are based on specific characteristics of the security, prepayment speeds, underlying collateral and cash flows.

Certain investments are measured at net asset value (NAV) per share, or its equivalent, as a practical expedient and therefore are not classified within the fair value hierarchy. These investments are valued at NAV, which is calculated based on the underlying investments and is provided by the respective investment managers as a practical expedient to estimate fair values. Most of the underlying investments are traded in markets that are considered to be active. For those underlying investments that are not considered to be actively traded, the fair values are based on quoted market prices of similar assets, dealer quotations, or valuations from pricing sources supported by observable inputs.

The preceding methods may produce a fair value calculation that may not be indicative of net realized value or reflective of future fair values. Although Navy Federal believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Interest in the investments measured at NAV can be purchased or redeemed at specified times during the month with advance notice of two to five days. For one investment, settlement of redemptions of more than \$1.0 million will occur 10 business days following the trade date. There were no other significant redemption terms or conditions for the other investments measured at NAV.

Navy Federal 401(k) Savings Plan

The Navy Federal 401(k) savings plan is a defined contribution plan where employees can contribute up to the statutory limits to a 401(k) retirement account and receive employer matching contributions. The matching contribution percentage is based on the formula the employee receives in the defined benefit retirement plan. Employees eligible for the Cash Balance benefit receive a 100% employer match on the first 7% of pay they contribute to their 401(k) account up to IRS limits and are vested after completing two years of service. The employees eligible for the Traditional benefit receive an employer match of 50% on the first 7% of pay they contribute to their 401(k) account up to IRS limits.

The expense recognized for the 401(k) Plan, including matching contributions and administrative costs, was \$68.1 million and \$58.7 million for the years ended December 31, 2019 and 2018, respectively.

Deferred Compensation Plan

The Navy Federal 457(b) deferred compensation plan is a non-qualified plan that offers a before-tax savings opportunity to highly compensated employees. The annual deferral amount allowed mirrors the 401(k) Plan limits, and contributions held by Navy Federal earn monthly interest based on Navy Federal's monthly gross income divided by average earning assets (loans and investments).

Non-Qualified Supplemental Retirement Plans

The non-qualified supplemental retirement plans are primarily designed to "make up" for benefits not paid through the qualified retirement plans as a result of IRS limitations. Internal Revenue Code Section 401(a)(17) limits the amount of compensation that can be used in a qualified retirement plan calculation, and Internal Revenue Code Section 415 limits the amount of monthly annuity that can be paid from a defined benefit plan.

All benefits are paid from Navy Federal's assets and are in compliance with all federal laws and regulations. As of December 31, 2019 and 2018, total liability related to these plans was \$8.1 million and \$9.4 million, respectively.

Note 13: Related Party Transactions

In the normal course of business, Navy Federal extends loans to and receives deposits from credit union officials. Credit union officials are defined as volunteer members of the Board of Directors and board committees, and employees with the title of Vice President and above. The total outstanding loan balances extended to credit union officials as of December 31, 2019 and 2018 were \$52.0 million and \$43.7 million, respectively. Total deposit balances of credit union officials as of December 31, 2019 and 2018 were \$27.5 million and \$26.0 million, respectively. Loans to credit union officials are made under similar terms as loans entered into by all members. Deposit accounts held by credit union officials earn interest at the same rates provided to all other members.

Note 14: Accumulated Other Comprehensive Income/(Loss)

Details of AOCI as of and for the years ending December 31 were as follows:

	December 31, 2019			
	Unrecognized Net Pension and Postretirement Amounts	Unrealized Net Gain/(Losses) on Available-for- Sale Debt Securities	Unrealized Net Gains/(Losses) on Cash Flow Derivatives	Total
<i>(dollars in thousands)</i>				
Balance, beginning of year	\$ (296,652)	\$ (417,842)	\$ (30,365)	\$ (744,859)
OCI before reclassifications	15,782	804,831	(149,942)	670,671
Amounts reclassified from AOCI to:				
Salaries and employee benefits	20,108	-	-	20,108
Net (gain)/loss on investments	-	(11,276)	-	(11,276)
Interest on borrowed funds	-	-	9,435	9,435
Net change in AOCI	35,890	793,555	(140,507)	688,938
Balance, end of year	\$ (260,762)	\$ 375,713	\$ (170,872)	\$ (55,921)

	December 31, 2018			
	Unrecognized Net Pension and Postretirement Amounts	Unrealized Net Losses on Available-for-Sale Debt Securities	Net Gains/(Losses) on Cash Flow Derivatives	Total
<i>(dollars in thousands)</i>				
Balance, beginning of year	\$ (215,628)	\$ (87,639)	\$ (17,261)	\$ (320,528)
Cumulative effects from adoption of new accounting standards	-	(38,372)	(4)	(38,376)
OCI before reclassifications	(90,489)	(286,484)	(21,654)	(398,627)
Amounts reclassified from AOCI to:				
Salaries and employee benefits	9,465	-	-	9,465
Net (gain)/loss on investments	-	(5,347)	-	(5,347)
Interest on borrowed funds	-	-	8,554	8,554
Net change in AOCI	(81,024)	(330,203)	(13,104)	(424,331)
Balance, end of year	\$ (296,652)	\$ (417,842)	\$ (30,365)	\$ (744,859)

Note 15: Regulatory Matters

Navy Federal is subject to regulatory capital requirements administered by the NCUA. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on Navy Federal's consolidated financial statements. Under capital adequacy regulations and the regulatory framework for prompt corrective action, Navy Federal must meet specific capital requirements that involve quantitative measures of Navy Federal's assets, liabilities and certain commitments as calculated under GAAP. Navy Federal's capital amounts and net worth classification are also subject to qualitative judgments by its regulators about components, risk weightings and other factors.

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Quantitative capital adequacy regulations require Navy Federal to maintain minimum capital balances and ratios of net worth to total assets. Credit unions are also required to calculate a risk-based net worth (RBNW) that establishes whether the credit union will be considered "complex" under the regulatory framework. A credit union is defined as "complex" if the credit union's quarter-end total assets exceed \$50.0 million and its RBNW requirement exceeds 6%. Navy Federal's RBNW requirement as of December 31, 2019 and 2018 was 6.08% and 6.37%, respectively. Based on the RBNW requirement, Navy Federal is considered "complex" as of December 31, 2019. There is no impact to Navy Federal based on the complex designation because its statutory net worth ratio qualifies Navy Federal as "well capitalized" by NCUA standards.

Navy Federal is categorized as "well capitalized" under the NCUA regulatory framework for prompt corrective action as a result of a net worth-to-assets ratio of 12.34% and 12.53% as of December 31, 2019 and 2018, respectively. To be categorized as "well capitalized," Navy Federal must maintain a minimum net worth ratio of 7%. The components of Navy Federal's capital are stable, and the occurrence of factors that could significantly affect capital adequacy is considered to be remote as they are limited to extraordinary regulatory or economic events. There are no conditions or events that have occurred since December 31, 2019 that management believes would have changed Navy Federal's categorization.

The FRB requires Navy Federal to maintain a minimum average reserve balance during a 14-day maintenance period. As of December 31, 2019 and 2018, Navy Federal met the reserve requirement set by the FRB.

Note 16: Fair Value Measurement

Navy Federal measures certain financial assets and liabilities at fair value in accordance with ASC 820, *Fair Value Measurement*, through various valuation approaches as described in Note 1: Summary of Significant Accounting Policies. Management has not made significant changes in the valuation techniques and parameters used for the fair value measurement of its financial assets and liabilities during the years ended December 31, 2019 and 2018.

Financial Assets and Liabilities Accounted For at Fair Value on a Recurring Basis

The following are the valuation methodologies and inputs used by Navy Federal in estimating the fair value of assets and liabilities measured on a recurring basis and classified as Level 2 and Level 3 in the fair value hierarchy.

Available-for-Sale Debt Securities

Navy Federal receives pricing for AFS debt securities from a third-party pricing service provider. Below includes the valuation methodologies used for AFS debt securities classified as Level 2 in the fair value hierarchy.

- **U.S. Government and Federal Agency Securities, Bank Notes and Corporate Bonds, Municipal Securities and Non-U.S. Government Securities** – These financial instruments are valued based on similar assets in the marketplace or derived from model-based valuation techniques for which all significant assumptions are observable.
- **Residential and Commercial Mortgage-Backed Securities** – These financial instruments include agency and non-agency securities, and are valued based on similar assets in the marketplace and the vintage of the underlying collateral.

Mortgage Loans Awaiting Sale

Navy Federal elects the fair value option for MLAS at origination or when a firm sale commitment is executed for loans that had been previously classified as held for investment. The fair value of MLAS is determined based on an evaluation of best execution forward sales contract prices sourced from the TBA market by agency. As such, MLAS are classified as Level 2 in the fair value hierarchy.

Mortgage Servicing Rights

MSR assets do not trade in an active, open market with readily observable prices. The fair value of MSR is determined by discounting projected net servicing cash flows. Actual and expected loan prepayment rate, discount rate, servicing costs and other economic factors are all considered in measuring the MSR fair value. The valuation model and underlying assumptions are corroborated by values received from independent third parties and through comparisons to market transactions. The fair value of Navy Federal's MSR portfolio is primarily affected by changes in mortgage interest rates resulting in loan prepayment acceleration factors to increase or

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decrease. As the MSR valuation is based on unobservable inputs, MSR assets are classified as Level 3 in the fair value hierarchy.

Derivative Assets and Liabilities

Fair values of interest rate swaps designated as cash flow and fair value hedges are determined based on third-party models that calculate the net present value of future cash flows discounted using the OIS rate. Counterparty non-performance risk is considered by discounting future cash flows using the OIS rates adjusted for credit quality. As the inputs utilized in the valuation are observable in the market, interest rate swaps are classified as Level 2 in the fair value hierarchy.

Fair values of forward sales contracts on TBA securities are determined based on an evaluation of best execution forward contract prices sourced from the TBA market, by agency. As such, forward sales contracts are classified as Level 2 in the fair value hierarchy.

Fair values of IRLCs are determined based on an evaluation of best execution forward contract prices sourced from the TBA market, adjusted by a factor that represents the probability it will settle and become a MLAS. As there are significant unobservable inputs in the fair value measurement, IRLCs are classified as Level 3 in the fair value hierarchy.

The tables below present certain information regarding assets and liabilities measured at fair value on a recurring basis on the Consolidated Statements of Financial Condition as of December 31:

	December 31, 2019				
	Level 1	Level 2	Level 3	Netting Adjustments ⁽¹⁾	Total
<i>(dollars in thousands)</i>					
Available-for-sale debt securities					
U.S. government and federal agency securities	\$ -	\$ 7,268,442	\$ -	\$ -	\$ 7,268,442
Residential mortgage-backed securities	-	6,942,027	-	-	6,942,027
Commercial mortgage-backed securities	-	486,084	-	-	486,084
Bank notes and corporate bonds	-	3,499,082	-	-	3,499,082
Municipal securities	-	337,579	-	-	337,579
Non-U.S. government securities	-	239,620	-	-	239,620
Total available-for-sale debt securities	-	18,772,834	-	-	18,772,834
Mortgage loans awaiting sale	-	2,477,253	-	-	2,477,253
Mortgage servicing rights	-	-	505,298	-	505,298
Derivatives ⁽²⁾	-	4,295	22,178	(1,958)	24,515
Total assets at fair value on a recurring basis	\$ -	\$ 21,254,382	\$ 527,476	\$ (1,958)	\$ 21,779,900
Derivatives ⁽²⁾	\$ -	\$ 5,297	\$ 162	\$ (1,958)	\$ 3,501
Total liabilities at fair value on a recurring basis	\$ -	\$ 5,297	\$ 162	\$ (1,958)	\$ 3,501

⁽¹⁾ Amounts represent the impact of legally enforceable master netting agreements with the same counterparties.

⁽²⁾ Derivative assets are included in Other assets and derivative liabilities are included in Other liabilities on the Consolidated Statements of Financial Condition.

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	December 31, 2018				
	Level 1	Level 2	Level 3	Netting Adjustments ⁽¹⁾	Total
<i>(dollars in thousands)</i>					
Available-for-sale debt securities					
U.S. government and federal agency securities	\$ -	\$ 6,044,871	\$ -	\$ -	\$ 6,044,871
Residential mortgage-backed securities	-	6,539,075	-	-	6,539,075
Commercial mortgage-backed securities	-	461,747	-	-	461,747
Bank notes and corporate bonds	-	3,085,806	-	-	3,085,806
Municipal securities	-	244,594	-	-	244,594
Non-U.S. government securities	-	198,723	-	-	198,723
Total available-for-sale debt securities	-	16,574,816	-	-	16,574,816
Equity securities	194,426	-	-	-	194,426
Mortgage loans awaiting sale	-	1,193,288	-	-	1,193,288
Mortgage servicing rights	-	-	479,638	-	479,638
Derivatives ⁽²⁾	-	160	19,937	(160)	19,937
Total assets at fair value on a recurring basis	\$ 194,426	\$ 17,768,264	\$ 499,575	\$ (160)	\$ 18,462,105
Derivatives ⁽²⁾	\$ -	\$ 33,028	\$ 2	\$ (160)	\$ 32,870
Total liabilities at fair value on a recurring basis	\$ -	\$ 33,028	\$ 2	\$ (160)	\$ 32,870

⁽¹⁾ Amounts represent the impact of legally enforceable master netting agreements with the same counterparties.

⁽²⁾ Derivative assets are included in Other assets and derivative liabilities are included in Other liabilities on the Consolidated Statements of Financial Condition.

The following tables summarize the changes in fair value for items measured as Level 3 in the fair value hierarchy on a recurring basis during 2019 and 2018:

<i>(dollars in thousands)</i>	2019	
	Mortgage Servicing Rights	Derivatives, Net
Balance, beginning of year	\$ 479,638	\$ 19,935
Realized/unrealized (losses)/gains included in earnings	(52,395)	43,672
Issuances/purchases	139,981	282,463
Settlements/sales	(61,926)	(324,055)
Balance, end of year	\$ 505,298	\$ 22,015

<i>(dollars in thousands)</i>	2018	
	Mortgage Servicing Rights	Derivatives, Net
Balance, beginning of year	\$ 392,533	\$ 17,339
Realized/unrealized gains included in earnings	2,026	10,196
Issuances/purchases	134,014	174,258
Settlements/sales	(48,935)	(181,858)
Balance, end of year	\$ 479,638	\$ 19,935

Net unrealized losses related to MSR assets still held at December 31, 2019 and 2018 were \$61.9 million and \$13.8 million, respectively which were recognized in Other non-interest expense in the Consolidated Statements of Income. Net unrealized gains on IRLC derivative instruments still held at December 31, 2019 and 2018 were \$22.0 million and \$19.9 million, respectively, which were recognized in Net gain on mortgage loans in the Consolidated Statements of Income.

Transfers into or out of Level 3 are made if the significant inputs used in the pricing models measuring the fair values of the assets and liabilities become unobservable or observable, respectively. Transfers are considered to be effective as of the end of the reporting period. There were no transfers into or out of Level 3 for the years ended December 31, 2019 and 2018.

Note 17: Subsequent Events

Navy Federal evaluated subsequent events through March 20, 2020, the date these financial statements were issued, and concluded that no subsequent events existed that are material to the consolidated financial statements.

The recent outbreak of the coronavirus has spread across the world, causing disruption to financial markets and overall economic conditions. The effects of the virus are rapidly evolving and, while Navy Federal is taking active risk mitigation efforts, the full impact and duration of the emergency is uncertain and the financial condition and results of operations could be adversely affected.

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