



NAVY FEDERAL CREDIT UNION
ANNUAL REPORT

OUR MEMBERS ARE
THE MISSION  **N**®



Report of the Chairman and President

Last year saw a number of unexpected challenges, including a worldwide pandemic, a fragile economy with high unemployment numbers and multiple natural disasters. While no one could have predicted these events, through it all, Navy Federal Credit Union helped our members meet the challenges by offering continued stability and support.

Financial Summary

As of December 31	2019	2020
<i>(dollars in millions)</i>		
Assets	\$ 111,986.1	\$ 135,664.1
Loans Outstanding	\$ 83,919.9	\$ 91,679.8
Savings, Checking, MMSAs, IRAs	\$ 56,733.7	\$ 81,902.8
Share Certificates	\$ 29,299.6	\$ 29,302.3
Members' Equity	\$ 13,763.6	\$ 14,932.4
Gross Income	\$ 7,993.2	\$ 8,374.0
Non-Interest Expense	\$ 3,430.8	\$ 3,920.8
Dividends	\$ 1,016.4	\$ 1,123.3
Mortgage Loans Serviced	\$ 77,307.3	\$ 80,585.6
Members	8,959,665	9,927,166



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

Deposit, Loan and Asset Comparisons

Deposits

(dollars in billions)



Loans

(dollars in billions)



Assets

(dollars in billions)



Meeting the Challenge

In the face of so many challenges, we focused first on keeping our employees safe, so we could continue to provide the service members needed. We made sure that members could continue to manage their accounts, apply for credit cards and loans, open or add to their savings accounts and conduct a myriad of other transactions—smoothly and without interruption. We also looked for ways to help members who were financially impacted by the pandemic.

We accomplished these goals by keeping branches open, having ongoing 24/7 live member support, and enhancing our mobile app, website and ATM network. And, we offered refinancing and forbearance assistance, pandemic and emergency relief loans and participated in the Paycheck Protection Program. We're proud to have continued providing members with some of the best loan and savings rates in the industry, as well as low fees and valuable rebates and discounts.

Our employees rose to the challenge by seeking new and innovative ways to serve members' needs. We transitioned 85% of our campus workforce to telework in less than three weeks—with no break in service to members. To keep our teammates and members safe, we quickly deployed strict safety protocols across all our campuses. Members responded positively to all our efforts, with satisfaction remaining high.

Navigating Forward

Throughout our nearly 90 years of serving military members and their families, we've understood that our strength provides them the stability they need to plan for a positive financial future. That strength and stability are due to our solid partnership with our members. Our members' continued trust in us has allowed the credit union to thrive and grow.

In 2020, our assets grew by \$23.7 billion to \$135.7 billion, a 21% increase over 2019. Membership reached 9.9 million members, 11% more than in 2019. The number of branches worldwide increased to 343, with 76 of them on or near military installations. Loans ended the year at \$91.7 billion. And, members' savings increased a record \$25.2 billion to \$111.2 billion.



**Best Overall Experience
in NerdWallet's
Best Mortgage Lenders
for VA Loans
and Bankrate's Best
Mortgage Lender 2020**

Lending Growth

Navy Federal continued to offer low-rate loans and credit cards. We were delighted to be able to help 76,000 families purchase homes, more than 21,000 of whom were first-time homebuyers. And, 38,000 members refinanced their mortgages, almost 19,000 of whom were Active Duty and veterans.

Some of the year's highlights include:

- Mortgage lending set an annual record with originations of \$23.4 billion.



- Auto loans also had a record year, financing 442,455 vehicles for members.
- Our credit cards portfolio closed out the year at \$19.8 billion.

Members also made 11% more debit card transactions, for a year-end total of 1.9 billion transactions, totaling \$69 billion in purchases.

Pandemic Response

Given the problems the pandemic caused some of our members, we responded by offering refinancing options, extensions, payment flexibility, and emergency loans, and participating in the Paycheck Protection Program (PPP).

Refinancing and Forbearance Assistance.

By refinancing mortgages, auto and student loans, our members were able to save money and, in many cases, lower their monthly payments. Members who refinanced auto loans with us saved an average of \$62 per month—more than \$700 per year.¹ Those who refinanced more than \$25,000 in student loans saved an average of more than \$8,000 over the life of their loans.²

We offered extensions on credit card and auto loan payments. And, in accordance with CARES Act guidelines, we processed 41,000 mortgage forbearances for more than \$9 billion in outstanding balances.

Pandemic and Emergency Relief Loans.

Nearly 24,000 members financed a total of \$88 million through this program.

Paycheck Protection Program (PPP) Loan Assistance. We also participated in the Paycheck Protection Program or PPP, which was passed by Congress to help businesses negatively impacted by COVID-19. At an average of \$25,000 per loan, we were able to help 6,700 small businesses keep their workforce employed—for a total of \$166.9 million in loan balances.

Disaster Relief Assistance. We experienced an extraordinary number of natural disasters last year and helped members rise to the challenge with emergency relief options. Members in FEMA-declared disaster areas took advantage of new, low-rate emergency loans and credit cards as well as assistance for existing loans and cardholders.



**Forrester named us #1
for Customer Experience
Among Multi-Channel
Banks/Credit Unions
in their 2020 US Customer
Experience (CX) Index survey
and CX Elite for Customer
Experience Among
All Brands.**

Offering Self-Service Options

Digital Channels. Use of mobile and online banking grew tremendously throughout 2020. In fact, engagement last year was at an all-time high—73% of members used a digital channel, with 1.9 billion sessions completed.

Financial Education. To help members increase their financial acumen, we released more than 65 new educational pages and articles. Members' interest in security topics increased dramatically in 2020, with 629,000 visits to our online Security Center, a whopping 184% increase over 2019.

Member and Community Support

We have a long tradition of strong member and community support. Member Service Representatives answered more than 44.3 million calls (up 15%). And, during the time PPP loans were available, our Contact Center's Business Membership Team fielded over 300,000 calls, a 113% increase over the previous year.

We were also pleased to be able to assist 258 different organizations in support of servicemembers, veterans and their families; COVID-19 relief; domestic violence; diversity and inclusion; and other local causes.

Member and Employee Satisfaction

It's our firm belief that creating a positive work environment for employees is important, as they're one of our highest priorities. We've found that finding satisfaction in their work lives inspires our team to continue to provide the outstanding service for which we're known—and to strive to go above and beyond.

Member Service Recognition. Forrester named us #1 for Customer Experience Among Multi-Channel Banks/Credit Unions in their 2020 US Customer Experience (CX) Index survey and CX Elite for Customer Experience Among All Brands. And, they further recognized us as the Brand Most Recommended by Customers among banks/credit unions (multichannel).³



In their 2020 reports, JD Power rated us:

- Highest overall satisfaction for U.S. Credit Card Satisfaction Study
- Highest overall satisfaction for U.S. Consumer Lending Satisfaction Study among personal loans
- Second highest overall satisfaction in the U.S. Primary Mortgage Servicer Satisfaction Study

Employee Satisfaction Recognition. Employees continue to rate us highly, and we were honored to be recognized in a number of national surveys.

- Fortune named us for the tenth time as one of the 100 Best Companies to Work For, and recognized us in several Best Workplaces areas, including for Parents, Women and Millennials
- Forbes included us in their 2020 Best Employers for Diversity for the second consecutive year, as well as among the Best Employers for Veterans
- Computerworld ranked us in the top ten in their Best Places to Work in IT report

Standing Strong

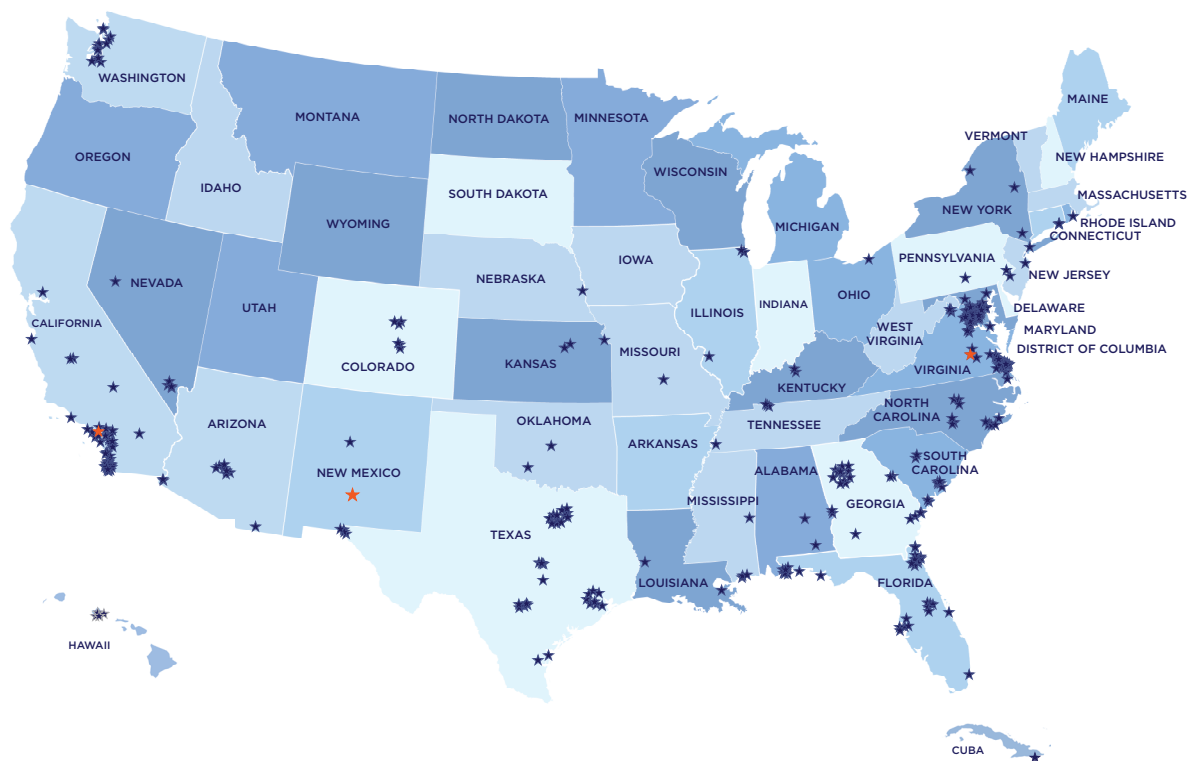
Throughout a year of hurdles and tests, one thing remained the same—our commitment to servicemembers, veterans and their families. They are and always will be our mission. We were able to help them meet their challenges, all while navigating our own. We continue to seek new and effective ways to serve members while keeping our team and communities safe. Together, we are Navy Federal Credit Union.

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

John A. Lockard
*Chairman
Board of Directors*

Mary A. McDuffie
*President/CEO
Navy Federal Credit Union*

2020 United States and Cuba Locations



★ New Branches ★ Existing Branches

ALABAMA

Enterprise
Montgomery

ARIZONA

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

CALIFORNIA

Brea
Chula Vista (3)
Corona
Coronado
El Cajon (2)
Fountain Valley
Hawthorne
La Mesa
Lake Elsinore
Lemoore* (2)
Long Beach
Mission Viejo
Monterey*
Murrieta
National City
Oceanside (3)
Ontario
Port Hueneme
Ridgecrest

Riverside
San Diego (14)*
San Marcos
Santa Ana
Santee

Temecula (2)
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 (8)
Kissimmee
Lutz

Mary Esther
Mayport*
Miami*
San Marcos
Santa Ana
Santee
Pace
Panama City Beach*
Pensacola (5)
Riverview
Satellite Beach
Tampa
Winter Park

GEORGIA

Albany*
Augusta
Buckhead
Buford
Columbus (2)
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
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 (2)

NEW JERSEY

Cherry Hill
Colts Neck*

NEW MEXICO

Albuquerque
White Sands Missile
Range

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

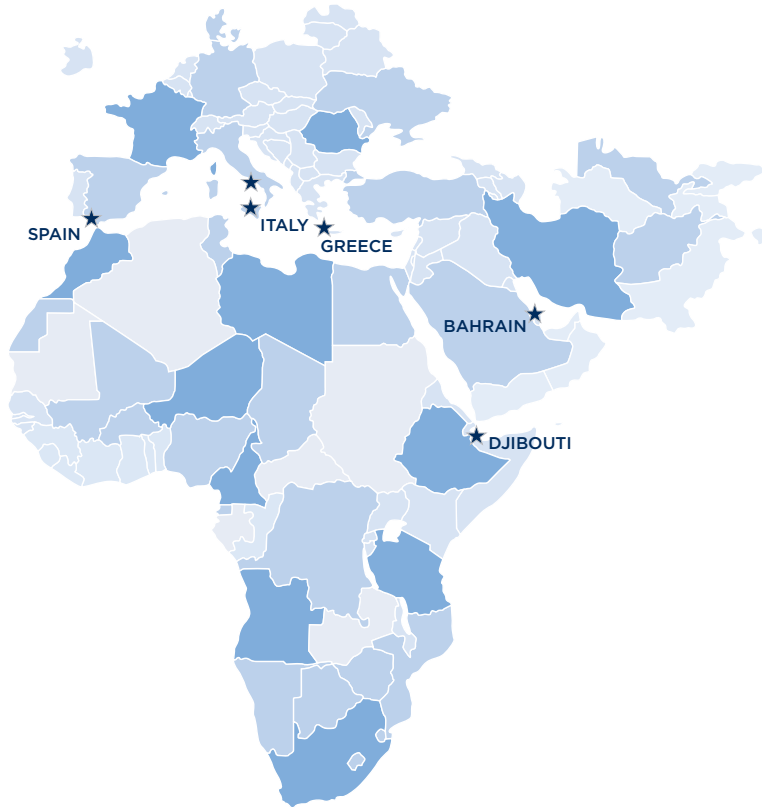
PENNSYLVANIA

Carlisle*
Horsham

RHODE ISLAND

Newport*
(continued)

2020 Overseas Locations (All On-Base)



SOUTH CAROLINA

Beaufort
Charleston
Columbia (2)
Goose Creek
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
Falls Church
Fredericksburg (3)
Gainesville
Hampton (2)
Lake Ridge
Manassas
Midlothian
Montclair
Newport News (2)
Norfolk (5)*

Portsmouth (3)*
Reston
Richmond
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*
Pyeongtaek*
Osan*

OKINAWA

Camp Courtney*
Camp Foster*
Camp Hansen*
Camp Kinser*
Camp Schwab*
Futenma*

SINGAPORE

SPAIN
Rota*

*Denotes on-base branch.

2020 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. Cochrane 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

Supervisory Committee Input for the 2020 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.

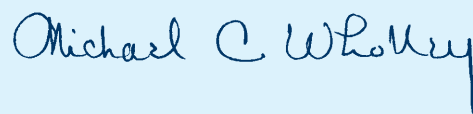
PwC's year-end audit, the *Independent Auditor's Report*, appears in this Annual Report.

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.

Acting as your ombudsman, the Supervisory Committee assures that all members are treated fairly by maintaining an open communication with the membership.



Michael C. Wholley
Chairman

Supervisory Committee



Kirk A. Foster
Rear Admiral, USN (Ret.)
Supervisory Committee
Technology Committee



Patrick J. McClanahan
Captain, SC, USN (Ret.)
Supervisory Committee



Caral E. Spangler
*Financial Strategy and
Investment Committee*
Supervisory Committee



Pasquale M. Tamburrino Jr.
Supervisory Committee
Technology Committee



Michael C. Wholley
Brigadier General, USMC (Ret.)
Chairman, Supervisory Committee

Other Committee Members



John R. Edwards
Brigadier General, USAF
Technology Committee



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



Kelly K. Harrison
CDR, USN
Planning and Strategic
Direction 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



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*



Mark R. Taylor
*Colonel, USA
Technology Committee*



Karin A. Vernazza
*Captain, USN (Ret.)
Technology Committee*



David P. Walt
*Captain, USN
Technology Committee*

OUR MEMBERS ARE THE MISSION ®



¹Monthly payment savings is based on the average monthly payments our members experienced with their new auto loan booked between January and April 2020 compared to their prior loan payments with another lender. Monthly payment reduction may result from a lower interest rate, a longer term, or both. Individual borrower savings may be different. ²The overall average savings claim is based on a review of refinanced loans greater than \$25,000 that were disbursed between February 24, 2020 and August 31, 2020. The calculation is derived by subtracting the average interest after refinancing from the average interest prior to refinancing. The calculation for interest after refinancing includes the 0.25% autopay deduction, if applicable. The overall interest savings may result from a lower interest rate, a shorter term, or both. Individual borrower savings may be different. ³Forrester Research does not endorse any company included in any CX Index™ report and does not advise any person to select the products or services of any particular company based on the ratings included in such reports.

Navy Federal Credit Union
Consolidated Financial Statements and Report of Independent Auditors
December 31, 2020 and 2019

NAVY FEDERAL CREDIT UNION
CONSOLIDATED FINANCIAL STATEMENTS AND REPORT OF INDEPENDENT AUDITORS
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DECEMBER 31, 2020 AND 2019

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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, 2020 and 2019, 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, 2020 and 2019, 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

Arlington, VA
March 19, 2021

PricewaterhouseCoopers LLP, 1000 Wilson Boulevard, Suite 2400, Arlington, Virginia 22209
T: (703) 847-1900, www.pwc.com/us

NAVY FEDERAL CREDIT UNION
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(dollars in thousands)	As of December 31,	
	2020	2019
ASSETS		
Cash and cash equivalents	\$ 16,741,137	\$ 5,035,143
Available-for-sale debt securities	22,272,676	18,772,834
Held-to-maturity securities	401,146	351,708
Mortgage loans held for sale, at fair value	3,501,444	2,477,253
Loans held for investment (\$691,241 and \$77,172 at fair value, respectively), net of allowance for loan losses of \$2,620,569 and \$1,631,851, respectively	85,557,837	79,810,777
Accounts receivable and accrued interest	2,672,974	1,037,763
Property, plant and equipment, net	2,359,122	2,275,394
Investments in FHLB	291,038	451,026
NCUSIF deposit	934,930	741,134
Mortgage servicing rights	418,954	505,298
Goodwill	58,905	58,905
Other assets	453,936	468,843
Total assets	\$ 135,664,099	\$ 111,986,078
LIABILITIES AND MEMBERS' EQUITY		
Deposit accounts		
Checking	\$ 23,244,868	\$ 15,321,607
Savings	27,439,932	18,561,158
Money market savings	22,774,445	15,424,405
Certificates	29,302,302	29,299,556
Individual retirement accounts	8,443,557	7,426,545
Total deposit accounts	111,205,104	86,033,271
Liabilities		
Borrowed funds	6,495,000	10,259,439
Accounts payable and accrued expenses	1,600,374	1,360,429
Other liabilities	1,431,190	569,316
Total deposit accounts and liabilities	120,731,668	98,222,455
Members' equity		
Equity	14,629,545	13,819,544
Accumulated other comprehensive income/(loss)	302,886	(55,921)
Total members' equity	14,932,431	13,763,623
Total liabilities and members' equity	\$ 135,664,099	\$ 111,986,078

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

NAVY FEDERAL CREDIT UNION
CONSOLIDATED STATEMENTS OF INCOME

<i>(dollars in thousands)</i>	For the Years Ended December 31,	
	2020	2019
Interest income		
Loans	\$ 5,764,309	\$ 5,689,296
Investment securities	428,430	487,326
Other investments	47,798	90,748
Total interest income	6,240,537	6,267,370
Dividends and interest expense		
Dividends on deposits	1,123,306	1,016,393
Interest on borrowed funds	318,777	355,212
Total dividends and interest expense	1,442,083	1,371,605
Net interest income	4,798,454	4,895,765
Provision for loan losses	(2,201,114)	(1,520,844)
Net interest income after provision for loan losses	2,597,340	3,374,921
Non-interest income		
Net gain on mortgage loans	477,217	249,517
Net gain on investments	256,275	42,054
Mortgage servicing revenue	158,066	153,794
Interchange income, net	567,395	528,606
Fee and other income	674,550	751,906
Total non-interest income	2,133,503	1,725,877
Non-interest expense		
Salaries and employee benefits	1,886,561	1,721,539
Office operations and equipment	467,925	430,189
Servicing expense	307,028	284,678
Professional and outside services	381,189	277,666
Marketing	153,273	177,894
Depreciation and amortization	271,233	215,304
Other	453,633	323,525
Total non-interest expense	3,920,842	3,430,795
Net income	\$ 810,001	\$ 1,670,003

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

NAVY FEDERAL CREDIT UNION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(dollars in thousands)	For the Years Ended December 31,	
	2020	2019
Net income	\$ 810,001	\$ 1,670,003
Other comprehensive income/(loss)		
Change in unrecognized pension and postretirement amounts	(129,417)	35,890
Change in net unrealized gains on AFS debt securities	584,443	793,555
Change in cash flow hedge derivatives	(96,219)	(140,507)
Total other comprehensive income	358,807	688,938
Total comprehensive income	\$ 1,168,808	\$ 2,358,941

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

NAVY FEDERAL CREDIT UNION
CONSOLIDATED STATEMENTS OF CHANGES IN MEMBERS' EQUITY

<i>(dollars in thousands)</i>	Equity	Accumulated Other Comprehensive (Loss)/Income	Total Members' Equity
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
Other comprehensive income	-	358,807	358,807
Net income	810,001	-	810,001
Balance at December 31, 2020	\$ 14,629,545	\$ 302,886	\$ 14,932,431

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

NAVY FEDERAL CREDIT UNION
CONSOLIDATED STATEMENTS OF CASH FLOWS

(dollars in thousands)	For the Years Ended December 31,	
	2020	2019
Operating activities		
Net income	\$ 810,001	\$ 1,670,003
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for loan losses	2,201,114	1,520,844
Depreciation and amortization	271,233	215,304
Gain on sale of securities	(256,354)	(41,271)
Loss on extinguishment of debt	41,501	26,865
Amortization of loan origination fees and costs	(9,952)	14,951
Loss on valuation of mortgage servicing rights	220,966	114,321
Other adjustments to net income	50,343	5,498
Mortgage loans originated for sale	(10,322,148)	(9,215,730)
Gain on mortgage loans originated for sale	(477,217)	(249,517)
Proceeds from sales of loans held for sale	9,440,805	8,066,483
Accretion and amortization of investment securities	134,664	56,612
Change in accounts receivable and accrued interest	(1,647,892)	(212,052)
Change in mortgage servicing rights	(134,622)	(139,981)
Change in other assets	(127,448)	(63,507)
Change in accounts payable and accrued expenses	235,035	77,320
Change in other liabilities	(60,366)	(139,338)
Net cash provided by operating activities	369,663	1,706,805
Investing activities		
Purchases of AFS debt securities	(9,465,423)	(4,630,494)
Purchases of HTM securities	(149,910)	(201,336)
Proceeds from maturities, paydowns and calls of AFS debt securities	4,677,153	1,769,747
Proceeds from sales of AFS debt securities	2,480,820	1,459,481
Proceeds from maturities, paydowns and calls of HTM securities	100,332	250,544
Proceeds from sales of equity securities	-	225,179
Net redemptions of FHLB stock	159,988	118,949
Proceeds from sale of loans held for investment	124,271	993,591
Net increase in loans held for investment	(7,370,021)	(9,929,144)
Purchases of property, plant and equipment	(360,376)	(592,913)
Increase in NCUSIF deposit	(193,796)	(105,291)
Proceeds from sale of real estate owned and other assets	56,640	77,041
Net cash used in investing activities	(9,940,322)	(10,564,646)
Financing activities		
Net increase in deposit accounts	25,141,426	15,615,737
Net decrease in securities sold under repurchase agreements	-	(250,000)
Proceeds from borrowed funds	10,950,102	7,240,202
Repayments of borrowed funds	(14,756,041)	(10,065,867)
Other, net	(58,734)	(9,516)
Net cash provided by financing activities	21,276,753	12,530,556
Net increase in cash and cash equivalents and restricted cash	11,706,094	3,672,715
Cash and cash equivalents and restricted cash at beginning of year	5,040,129	1,367,414
Cash and cash equivalents and restricted cash at end of year	\$ 16,746,223	\$ 5,040,129
Supplemental cash flow information:		
Interest paid	\$ 1,458,352	\$ 1,383,161
Non-cash activities:		
Transfers of loans held for investment to other assets	\$ 39,093	\$ 77,961
Loans securitization	485,949	48,299
Accrued additions and improvements of property, plant and equipment	(4,910)	22,367
Financed property, plant and equipment	(7,197)	10,689
Transfer of land held for sale to other assets	-	20,486
Transfer of mortgage loans awaiting sale to loans	676,011	81,267
Transfer of loans to mortgage loans awaiting sale	122,625	975,818
Accruals for repurchase of loans	30,407	-

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:

(dollars in thousands)	As of December 31,	
	2020	2019
Cash and cash equivalents on the Consolidated Statements of Financial Condition	\$ 16,741,137	\$ 5,035,143
Restricted cash included in other assets on the Consolidated Statements of Financial Condition ⁽¹⁾	5,086	4,986
Total Cash and cash equivalents and restricted cash in the Consolidated Statements of Cash Flows	\$ 16,746,223	\$ 5,040,129

⁽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, Coast Guard 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, balances due from other financial institutions, cash held at the Federal Reserve Bank (FRB) and short-term investments with stated maturities of three months or less, which include 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 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.

If it is more likely than not that Navy Federal will sell the debt security prior to the recovery of its amortized cost basis and the present value of cash flows expected to be collected is less than the amortized cost basis, the impairment is considered to be other-than-temporary. Such impairment is separated into a credit component and a noncredit component. The credit component represents the difference between the present value of future cash flows and the amortized cost basis of the debt security, and the credit component is recognized immediately as a Net gain/(loss) on investments. The noncredit component represents the difference between the debt security's fair value and the present value of future cash flows, and the noncredit component is recorded in AOCI. If Navy Federal sells the debt security, any noncredit component losses are recognized as a Net gain/(loss) on investments.

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. 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, 2020 and 2019.

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

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. Real estate loans also include loans where Navy Federal has purchased a participation interest in mortgage loans originated by other credit unions. 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 held for investment 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.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (the CARES Act) was signed into law. Pursuant to the CARES Act and in response to the COVID-19 pandemic, Navy Federal has taken action to support members through offering a variety of assistance programs. Members requesting assistance were offered payment forbearance, payment extensions, payment deferrals and other types of loan modifications, collectively COVID-19 Loan Accommodations, to help members deal with the effects of the pandemic. Navy Federal began its pandemic relief program on March 1, 2020 and continues to work prudently with members affected by COVID-19.

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Navy Federal considered the impact of COVID-19 Loan Accommodations and reported delinquency status as follows:

- Loans that were current either at the time Navy Federal's pandemic relief program began or the month end prior to receiving COVID-19 Loan Accommodations (if originated after March 1, 2020) are reported as current throughout the accommodation period;
- Loans that were delinquent either at the time Navy Federal's pandemic relief program began or the month end prior to receiving COVID-19 Loan Accommodations (if originated after March 1, 2020) are reported as delinquent throughout the accommodation period;
- Loans brought current as part of the COVID-19 Loan Accommodations or became current during the accommodation period are reported as current.

All other loans are reported as 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. Generally, Navy Federal does not recognize an allowance for credit losses on accrued interest receivable. Interest received on loans in non-accrual status is accounted for on a cash basis. Loans are returned to accrual status when the principal and interest amounts contractually due are brought current and collection of remaining outstanding contractual payments are reasonably assured.

In accordance with ASC 310-20, *Receivables—Nonrefundable Fees and Other Costs*, loan origination fees and certain direct origination costs related to loans held for investment 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.

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 held for investment 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 those 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 considered the impact of COVID-19 Loan Accommodations on delinquency status and overall credit losses related to the pandemic. Navy Federal applied qualitative adjustments to the modeled allowance for loan losses to major portfolios, which include consumer, credit cards and real estate, to ensure sufficient allowance amounts were booked to capture the impact of COVID-19.

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.

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Mortgage Loans Awaiting Sale

Navy Federal's MLAS portfolio consists of mortgage loans originated with the intent and ability to sell. Interest income on MLAS is recorded as earned and is reported in Interest income—Loans 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, as such these loans are recorded at fair value with subsequent changes to estimated fair value recognized in Net gain on mortgage loans in the Consolidated Statements of Income. Fees and direct costs associated with these loans are recognized as incurred. 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.

In certain circumstances, loans originated with the intent to sell for which fair value option was elected may be transferred to loans held for investment. These loans continue to be measured at fair value with subsequent changes to estimated fair value recognized in Net gain on mortgage loans in the Consolidated Statements of Income.

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.

The CARES Act provides optional, temporary relief from accounting for certain loan modifications as TDRs. Under the CARES Act, TDR relief is available to financial institutions for loan modifications related to the adverse effects of COVID-19 granted to borrowers that are current as of December 31, 2019, and were not previously accounted for as a TDR, as well as federally backed mortgage loans regardless of delinquency status. TDR relief applies to COVID-19 Loan Accommodations made from March 1, 2020, until the earlier of December 31, 2020, or 60 days following the termination of the national emergency declared by the President of the United States. On December 27, 2020, the Consolidated Appropriations Act, 2021 was signed into law, which among other relief provisions, extended the temporary TDR relief provision through the earlier of January 1, 2022 or 60 days following the termination of the national emergency.

On April 7, 2020, federal banking regulators issued the Interagency Statement on Loan Modifications and Reporting for financial institutions Working with Customers Affected by the Coronavirus (Revised) (the Interagency Statement). Loans that do not meet the criteria for TDR relief under the CARES Act may be evaluated in accordance with the Interagency Statement, which allows banks to not designate certain short-term modifications (e.g., six months or less) as TDRs for borrowers with COVID-19 hardships who were current on their payments prior to the modification.

Navy Federal has elected to apply the above provisions of the CARES Act and Interagency Statement for the COVID-19 Loan Accommodations meeting the relevant criteria.

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

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incurred in the planning and post-development project stages are charged to non-interest expense, and costs 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

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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. Hedge accounting was discontinued for certain hedges for the year ended December 31, 2020. See Note 6: Derivative Instruments and Hedging Activities for details. Navy Federal did not discontinue hedge accounting for any hedges for the year ended December 31, 2019.

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 plan and postretirement medical plan 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:

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- 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.
- 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.

Generally, uncertainties in fair value measurements of financial instruments using unobservable inputs may have a significant impact on fair value. Certain of these unobservable inputs will, in isolation, have a directionally consistent impact on the fair value of the instrument for a given change in that input. Alternatively, the fair value of the instrument may move in an opposite direction for a given change in another input. In general, changes in interest rates, constant prepayment rates, servicing costs, best execution forward contract prices or other relevant inputs may result in a significant increase or decrease in the Level 3 fair value measurement of a particular asset or liability as of the reporting date.

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 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" and "Mortgage Loans Awaiting Sale" sections within this Note, respectively.

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 is comprised 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 card fees for standing ready to authorize and provides 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 \$352.0 million and \$339.3 million for the years ended December 31, 2020 and 2019.

The 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.

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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)*
- ASU 2020-05, *Revenues from Contracts with Customers (Topic 606) and Leases (Topic 842)*

These ASUs are effective for the annual reporting periods beginning after December 15, 2021. 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 Dates*
- ASU 2019-11, *Codification Improvements to Topic 326, Financial Instruments—Credit Losses*
- ASU 2020-02, *Financial Instruments—Credit Losses (Topic 326) and Leases (Topic 842): Effective Dates for Certain Entities*

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, 2022. 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

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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.

Note 2: Restrictions on Cash

Navy Federal had \$5.1 million and \$5.0 million in restricted cash as of December 31, 2020 and 2019. 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.

HTM and AFS Debt Securities

The amortized cost of Navy Federal's HTM debt securities as of December 31, 2020 and 2019 was \$401.1 million and \$351.7 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, 2020 and 2019 were as follows:

	December 31, 2020			
	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	\$ 6,506,944	\$ 292,727	\$ (51,910)	\$ 6,747,761
Residential mortgage-backed securities	10,439,590	236,287	(6,606)	10,669,271
Commercial mortgage-backed securities	472,953	36,913	(170)	509,696
Bank notes and corporate bonds	3,319,185	386,493	(199)	3,705,479
Municipal securities	341,562	44,483	-	386,045
Non-U.S. government securities	232,060	22,364	-	254,424
Total available-for-sale debt securities	\$ 21,312,294	\$ 1,019,267	\$ (58,885)	\$ 22,272,676
	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

Navy Federal sold AFS debt securities with a carrying value of \$2,225.2 million and \$1,448.2 million for cash proceeds of \$2,480.8 million and \$1,459.5 million for the years ended December 31, 2020 and 2019, respectively. Gross realized gains of \$255.6 million and gross realized losses of zero were included in earnings for the year ended December 31, 2020. 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.

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The contractual maturities of Navy Federal's HTM debt securities as of December 31, 2020 were as follows:

		December 31, 2020
		Amortized Cost
<i>(dollars in thousands)</i>		
Held-to-maturity debt securities		
Due in one year or less	\$	149,983
Due after one year through five years		201,163
Due after ten years		50,000
Total held-to-maturity debt securities	\$	401,146

The contractual maturities of Navy Federal's AFS debt securities as of December 31, 2020 were as follows:

		December 31, 2020	
		Amortized Cost	Fair Value
<i>(dollars in thousands)</i>			
Available-for-sale debt securities			
Due in one year or less	\$	806,877	\$ 815,855
Due after one year through five years		3,978,407	4,254,855
Due after five years through ten years		2,697,501	2,955,121
Due after ten years		13,829,509	14,246,845
Total available-for-sale debt securities	\$	21,312,294	\$ 22,272,676

Navy Federal held 2 HTM and 34 AFS debt securities in an unrealized loss position at December 31, 2020. 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. For a majority of these investments, 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. For one investment, other-than-temporary impairment credit losses of \$2.4 million were recognized during the year ended December 31, 2020 resulting from adverse changes in the present value of the associated future cash flows. For the remaining investments, 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, 2020 and 2019.

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, 2020					
		Less than 12 Months		12 Months or Longer		Total	
		Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
<i>(dollars in thousands)</i>							
Held-to-maturity debt securities		\$ 190	\$ -	\$ 51	\$ -	\$ 241	\$ -
Available-for-sale debt securities							
U.S. government and federal agency securities		1,183,366	(51,910)	-	-	1,183,366	(51,910)
Residential mortgage-backed securities		805,372	(6,606)	-	-	805,372	(6,606)
Commercial mortgage-backed securities		27,091	(170)	-	-	27,091	(170)
Bank notes and corporate bonds		24,787	(199)	-	-	24,787	(199)
Total available-for-sale debt securities		2,040,616	(58,885)	-	-	2,040,616	(58,885)
Total debt securities		\$ 2,040,806	\$ (58,885)	\$ 51	\$ -	\$ 2,040,857	\$ (58,885)

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	December 31, 2019					
	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
<i>(dollars in thousands)</i>						
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)
Non-U.S. government securities	-	-	-	-	-	-
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)

As of December 31, 2020 and 2019, Navy Federal had pledged \$186.7 million and \$152.0 million, respectively, of investment securities as collateral with counterparties for derivative transactions under master netting agreements. As of December 31, 2020 and 2019, Navy Federal pledged zero 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 past due status of loans that received COVID-19 Loan Accommodations under the CARES Act is generally frozen during the accommodation period, and as a result, loans may be reported as current in the tables below even if payments are past due based upon the loan's original contractual terms. See Note 1: Summary of Significant Accounting Policies for additional details.

The composition of Navy Federal's loans by portfolio and delinquency status as of December 31, 2020 and 2019 was as follows:

	December 31, 2020					
	Current	30-89 Days Delinquent	90 Days or More Delinquent	Total Delinquent Loans	Unamortized Cost/ (Deferred Fee)	Total Loans
<i>(dollars in thousands)</i>						
Consumer loans	\$ 24,279,782	\$ 203,633	\$ 87,804	\$ 291,437	\$ 45,499	\$ 24,616,718
Credit card loans	19,466,912	235,017	179,296	414,313	6,869	19,888,094
Mortgage loans	40,910,782	290,706	290,740	581,446	(213,666)	41,278,562
Equity loans	2,340,410	13,482	21,158	34,640	19,982	2,395,032
Total loans held for investment	\$ 86,997,886	\$ 742,838	\$ 578,998	\$ 1,321,836	\$ (141,316)	\$ 88,178,406

	December 31, 2019					
	Current	30-89 Days Delinquent	90 Days or More Delinquent ⁽¹⁾	Total Delinquent Loans	Unamortized Cost/ (Deferred Fee)	Total Loans
<i>(dollars in thousands)</i>						
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 held for investment	\$ 79,813,138	\$ 1,119,461	\$ 654,374	\$ 1,773,835	\$ (144,345)	\$ 81,442,628

⁽¹⁾ Loans 90 days or more delinquent represent loans on non-accrual.

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Non-accrual Loans

When a loan becomes 90 days past due, accrued interest is reversed and the loan is placed into non-accrual status. Loans that received COVID-19 Loan Accommodations under the CARES Act are placed on non-accrual under the same policy. As a result, the table below includes loans that are not reported as delinquent due to receiving certain COVID-19 Loan Accommodations but are classified as non-accrual due to missing three consecutive payments according to the terms of their original contractual agreement.

The composition of Navy Federal's loans by portfolio on non-accrual status as of December 31, 2020 is as follows:

<i>(dollars in thousands)</i>	2020
Consumer loans	\$ 87,804
Credit card loans	179,296
Mortgage loans	3,449,199
Equity loans	137,882
Total	\$ 3,854,181

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.

Pursuant to the Interagency Statement and in connection with the credit reporting provisions per the CARES Act, the December 31, 2020 delinquency status of accounts that received COVID-19 Loan Accommodations aligns with the rules set forth for financial institutions to report delinquency status to the credit agencies. As a result, certain COVID-19 Loan Accommodations are not reported as past due as of December 31, 2020 based on the contractual terms of the loan, even where borrowers may not be making payments on their loans during the accommodation period.

Consumer Loans

Navy Federal uses FICO score as an indicator of credit quality for secured consumer loans, which consisted of the following as of December 31, 2020:

<i>(dollars in thousands)</i>	December 31, 2020
FICO	Total
Greater than or Equal to 610	\$ 15,874,508
Less than 610	2,676,171
Total	\$ 18,550,679

Navy Federal uses delinquency status as an indicator of credit quality for unsecured consumer loans, which consisted of the following as of December 31, 2020:

<i>(dollars in thousands)</i>	December 31, 2020
Delinquency Status	Total
Performing	\$ 5,936,451
60+ days and foreclosure	72,615
Total	\$ 6,009,066

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

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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, 2020 and 2019.

Mortgage Loans

Navy Federal uses delinquency status as an indicator of credit quality for mortgage loans held for investment as of December 31, 2020. Refer to the loan composition and delinquency status table above for information as of December 31, 2020.

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

(dollars in thousands)		December 31, 2019	
FICO		Total ⁽¹⁾	
Greater than or Equal to 610	\$		35,035,074
Less than 610			2,576,927
Total	\$		37,612,001

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

Equity Loans

Navy Federal uses FICO score as indicators of credit quality for equity loans, which consisted of the following as of December 31, 2020:

(dollars in thousands)		December 31, 2020	
FICO		Total ⁽¹⁾	
Greater than or Equal to 610	\$		2,287,699
Less than 610			97,541
Total	\$		2,385,240

⁽¹⁾ Excludes unamortized cost of \$20.0 million and other adjustments of \$(10.2) million.

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

		December 31, 2019		
		FICO Score		Total ⁽¹⁾
		Less than 610	Greater than or Equal to 610	
Delinquency Status				
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.

Allowance for Loan Losses

The allowance for credit losses at December 31, 2020 was \$2.6 billion, an increase of \$988.7 million compared to December 31, 2019. The increase in the allowance for credit losses was primarily driven by the deterioration in the economic conditions resulting from the impact of COVID-19. Changes in the allowance for loan and lease losses during the years ended December 31, 2020 and 2019 were as follows:

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(dollars in thousands)	December 31, 2020			
	Consumer	Credit Cards	Real Estate	Total
Allowance for credit losses:				
Balance, beginning of year	\$ 508,941	\$ 1,037,267	\$ 85,643	\$ 1,631,851
Provision expense	636,705	1,448,820	115,589	2,201,114
Loans charged off	(554,462)	(884,018)	(10,970)	(1,449,450)
Recoveries	118,742	95,647	10,561	224,950
Net change in allowance for unfunded commitments	1,622	10,482	-	12,104
Balance, end of year	\$ 711,548	\$ 1,708,198	\$ 200,823	\$ 2,620,569
Ending balance: loans held for investment, individually evaluated for impairment	\$ 128,233	\$ 208,754	\$ 65,173	\$ 402,160
Ending balance: loans held for investment, collectively evaluated for impairment	\$ 582,489	\$ 1,499,444	\$ 133,102	\$ 2,215,035
Ending balance: loans held for investment, acquired with deteriorated credit quality	\$ 826	\$ -	\$ 2,548	\$ 3,374
Loan amount (excluding allowance):				
Ending balance: loans held for investment, individually evaluated for impairment	\$ 588,172	\$ 456,353	\$ 1,531,227	\$ 2,575,752
Ending balance: loans held for investment, collectively evaluated for impairment	\$ 24,026,954	\$ 19,431,741	\$ 42,131,635	\$ 85,590,330
Ending balance: loans held for investment, acquired with deteriorated credit quality	\$ 1,592	\$ -	\$ 10,732	\$ 12,324

(dollars in thousands)	December 31, 2019			
	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 held for investment, individually evaluated for impairment	\$ 165,305	\$ 221,711	\$ 64,192	\$ 451,208
Ending balance: loans held for investment, collectively evaluated for impairment	\$ 342,800	\$ 815,556	\$ 19,300	\$ 1,177,656
Ending balance: loans held for investment, acquired with deteriorated credit quality	\$ 836	\$ -	\$ 2,151	\$ 2,987
Loan amount (excluding allowance):				
Ending balance: loans held for investment, individually evaluated for impairment	\$ 851,820	\$ 614,503	\$ 1,137,299	\$ 2,603,622
Ending balance: loans held for investment, collectively evaluated for impairment	\$ 20,396,349	\$ 19,142,513	\$ 39,285,371	\$ 78,824,233
Ending balance: loans held for investment, acquired with deteriorated credit quality	\$ 1,893	\$ -	\$ 12,880	\$ 14,773

Changes in the allowance for unfunded commitments during the years ended December 31, 2020 and 2019 were as follows:

(dollars in thousands)	2020	2019
Balance, beginning of year	\$ 54,625	\$ 47,453
Net change in allowance for unfunded commitments	(12,104)	7,172
Balance, end of year	\$ 42,521	\$ 54,625

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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. In addition, COVID-19 Loan Accommodations granted to members resulting from the effects of the COVID-19 pandemic, who were otherwise in current payment status, are not considered to be TDRs in accordance with the CARES Act and guidance set forth within the Interagency Statement. For additional information regarding the TDR relief provided by the CARES Act and the clarifying TDR accounting guidance from the Interagency Statement, see Note 1: Summary of Significant Accounting Policies.

The following tables summarize the financial impact, by concession type, of loans that became TDRs during the years ended December 31, 2020 and 2019:

	2020 ⁽¹⁾				
(dollars in thousands)	Interest Rate Reduction and Term Extension	Interest Rate Reduction	Term Extension	Other ⁽²⁾	Total
Consumer	\$ 6,284	\$ 8,717	\$ 14,013	\$ 2,796	\$ 31,810
Credit card	-	41,006	-	920	41,926
Real estate	4,535	81	9,619	726	14,961
Total	\$ 10,819	\$ 49,804	\$ 23,632	\$ 4,442	\$ 88,697

⁽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.

	2019 ⁽¹⁾				
(dollars in thousands)	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.

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, 2020, TDRs that were more than 90 days delinquent within the first 12 months after modification totaled \$154.1 million, which included \$59.8 million of consumer loans, \$66.9 million of credit card loans and \$27.4 million of real estate loans.

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.

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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, 2020 and 2019. 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, 2020 and 2019:

	December 31, 2020				
	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	\$ 583,762	\$ 128,233	\$ 714,666	\$ 55,800	\$ 53,575
Credit card	451,271	208,753	528,604	51,172	49,522
Real estate	1,250,924	65,173	1,100,592	30,182	30,851
Total impaired loans with an associated allowance	\$ 2,285,957	\$ 402,159	\$ 2,343,862	\$ 137,154	\$ 133,948
Impaired loans without an associated allowance					
Consumer	\$ 4,411	\$ -	\$ 5,331	\$ 999	\$ 1,002
Credit card	5,081	-	6,824	865	853
Real estate	280,303	-	233,671	5,502	5,790
Total impaired loans without an associated allowance	\$ 289,795	\$ -	\$ 245,826	\$ 7,366	\$ 7,645
Total impaired loans	\$ 2,575,752	\$ 402,159	\$ 2,589,688	\$ 144,520	\$ 141,593

	December 31, 2019				
	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	\$ 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

Loan Transfers

Navy Federal reclassified \$676.0 million and \$81.3 million of MLAS to mortgage loans held for investment during the years ended December 31, 2020 and 2019, respectively. Navy Federal transferred these loans to mortgage loans held for investment at fair value and continues to account for them at fair value.

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 the Government Sponsored Enterprises (GSEs), and Government National Mortgage Association (GNMA). The GSEs and 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.

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Navy Federal originated \$23.4 billion and \$18.5 billion, and sold/secured \$9.6 billion and \$8.9 billion, of first mortgage loans during the years ended December 31, 2020 and 2019, 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>	2020	2019
Cash from sale of mortgage loans and mortgage-backed securities	\$ 9,565,076	\$ 9,060,074
Repurchase of previously transferred loans	1,549,758	25,828
Contractual servicing fees received	158,032	153,794

During the year ended December 31, 2020, Navy Federal reclassified \$122.6 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 \$124.3 million and recognized MSR assets of \$2.5 million for the year ended December 31, 2020. 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.

Gains on the sale of MLAS are included in Net gain on mortgage loans in the Consolidated Statements of Income and totaled \$372.5 million and \$185.7 million for the years ended December 31, 2020 and 2019, respectively. Navy Federal recorded fair value gains of \$104.8 million and \$63.5 million for the years ended December 31, 2020 and 2019, 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.

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>	2020	2019
Weighted-average life (years)	5.93	6.64
Weighted-average CPR	11.55%	9.59%
Decline in fair value from 10% adverse change	\$ 20,098	\$ 17,289
Decline in fair value from 20% adverse change	38,674	33,392
Option adjusted spread	8.84%	9.41%
Decline in fair value from 10% adverse change	\$ 13,286	\$ 16,120
Decline in fair value from 20% adverse change	25,735	31,202

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, 2020 and 2019, Navy Federal received \$3.4 million and \$3.1 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

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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, 2020 and 2019 totaled \$98.9 million and \$33.0 million, respectively.

Due to continued borrower requests for COVID-19 Loan Accommodations as a result of the COVID-19 pandemic, the amount of servicing advances of principal and interest remained elevated in 2020. The amount of advances may continue to increase if additional COVID-19 Loan Accommodations are provided.

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

(dollars in thousands)	2020	2019
Principal balances of loans serviced ⁽¹⁾	\$ 35,812,939	\$ 37,426,413
Delinquent loans ^{(1), (2)}	235,188	243,872

⁽¹⁾ Includes loans that are in the GNMA early pool buyback program of \$970.6 million and \$141.3 million at December 31, 2020 and 2019, 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 860-20, *Sales of Financial Assets*, 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.

(dollars in thousands)	2020	2019
Weighted-average CPR	32.63%	13.97%
Anticipated credit losses ⁽¹⁾	\$ -	-
Weighted-average life (years)	2.29	4.49

⁽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)	2020	2019
Weighted-average CPR		
Decline in fair value from 10% adverse change	\$ 4,679	1,150
Decline in fair value from 20% adverse change	8,768	2,438

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 \$840.4 million and \$778.5 million as of December 31, 2020 and 2019, 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. COVID-related payment deferrals have resulted in an increase in members failing to make payments for three consecutive months and a corresponding increase in loans eligible

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for repurchase from GNMA securitization pools. 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. Of the loans that became eligible for repurchase under the Early Pool Buyback Program, \$1.5 billion were repurchased out of GNMA securities during the year ended December 31, 2020. The loans bought out of GNMA securities are recorded as mortgage loans held for investment. At December 31, 2020 and 2019, amounts associated with the Early Pool Buyback Program recognized in MLAS and Other liabilities totaled \$970.6 million and \$141.3 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, 2020 and 2019 was \$13.3 million and \$24.1 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, 2020 and 2019. 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, 2020 and 2019, Navy Federal estimates it is reasonably possible it could incur additional losses in excess of its accrued liability of up to approximately \$32.0 million and \$47.6 million, respectively.

The total UPB subject to representations and warranties was \$34.7 billion and \$36.4 billion as of December 31, 2020 and 2019, respectively.

Loss-Sharing Agreements

Navy Federal sold mortgage loans to the GSEs under loss-sharing agreements dated from 2006 to 2020. 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, 2020 and 2019:

<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
2020	\$ 912,983	\$ 121,809	\$ 648	\$ 4,959
2019	809,131	94,209	1,486	9,114

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.

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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, 2020 and 2019.

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

(dollars in thousands)	December 31, 2020				December 31, 2019	
	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	\$ 2,214,761	\$ 88,329	\$ 6	\$ 981,751	\$ 22,178	\$ 162
Forward sales contracts ⁽¹⁾	3,633,500	2,493	29,669	2,890,000	1,958	5,297
Total derivatives not designated as accounting hedges	\$ 5,848,261	\$ 90,822	\$ 29,675	\$ 3,871,751	\$ 24,136	\$ 5,459
Derivatives designated as accounting hedges:						
Interest rate contracts:						
Fair value interest rate contracts	\$ 10,000	\$ -	\$ 1	\$ 10,000	\$ 2	\$ -
Cash flow interest rate contracts	2,200,000	1	2,564	2,950,000	2,335	-
Total derivatives designated as accounting hedges	\$ 2,210,000	\$ 1	\$ 2,565	\$ 2,960,000	\$ 2,337	\$ -
Total derivative instruments, gross	\$ 8,058,261	\$ 90,823	\$ 32,240	\$ 6,831,751	\$ 26,473	\$ 5,459
Less: Legally enforceable master netting agreements		(2,493)	(2,493)		\$ (1,958)	(1,958)
Total derivative instruments, net		\$ 88,330	\$ 29,747		\$ 24,515	\$ 3,501

⁽¹⁾ As of December 31, 2020, the notional amount related to forward contracts in assets and liabilities was \$375.0 million and \$4.0 billion, respectively. 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.

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, 2020 and 2019, 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.

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	December 31, 2020					
	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	\$ 88,329	\$ -	\$ 88,329	\$ -	\$ -	\$ 88,329
Derivative instruments subject to master netting agreements	2,494	(2,493)	1	-	-	1
Total derivative assets	\$ 90,823	\$ (2,493)	\$ 88,330	\$ -	\$ -	\$ 88,330
Financial Liabilities						
Derivative instruments not subject to master netting agreements	\$ (6)	\$ -	\$ (6)	\$ -	\$ -	\$ (6)
Derivative instruments subject to master netting agreements	(32,234)	2,493	(29,741)	28,638	1,103	-
Total derivative liabilities	(32,240)	2,493	(29,747)	28,638	1,103	(6)
Total	\$ 58,583	\$ -	\$ 58,583	\$ 28,638	\$ 1,103	\$ 88,324

⁽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.

	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
(dollars in thousands)						
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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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:

(dollars in thousands)		2020		2019	
Derivative Instruments	Location of Gain/(Loss) Recognized in Earnings				
Interest rate lock commitments	Net gain on mortgage loans	\$	66,308	\$	2,080
Forward sales contracts	Net gain on mortgage loans		(23,838)		18,289
Total		\$	42,470	\$	20,369

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.

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

(dollars in thousands)		2020		2019	
Changes in Fair Value	Location of Changes in Fair Value Recognized in Earnings				
Interest rate swaps hedging fixed-rate investments	Fee and other income	\$	(323)	\$	(231)
Hedged fixed-rate investments attributable to risk being hedged	Fee and other income		409		473

As of December 31, 2020, the following amounts were recorded on the Consolidated Statements of Financial Condition related to cumulative basis adjustments for fair value hedges:

(dollars in thousands)					
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	\$	9,954	\$	229	

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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. During the year ended December 31, 2020, prepayment was made on certain FHLB borrowings which resulted in the de-designation of a cash flow hedge relationship and the termination of the associated swap. As the hedged forecasted transaction is no longer expected to occur, approximately \$57.9 million of losses were reclassified from AOCI into earnings.

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

	2020		2019			2020		2019	
(dollars in thousands)	(Loss) Recognized in AOCI		Location of (Loss) Reclassified from AOCI into Earnings			Amount of (Loss) Reclassified from AOCI into Earnings			
Interest rate contracts	\$	(210,554)	\$	(149,942)	Interest on borrowed funds	\$	(114,335)	\$	(9,435)

During the next 12 months, net losses in AOCI of approximately \$56.7 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 12 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, and accordingly, at December 31, 2020 and 2019, the potential credit risk related to these commitments could be similar to existing loans, if these commitments became funded loans.

Commitment balances as of December 31, 2020 and 2019 were as follows:

(dollars in thousands)	2020		2019	
Credit cards	\$	31,803,023	\$	27,239,340
Home equity lines of credit		1,411,228		1,560,282
Checking lines of credit		1,264,592		1,165,123
Pre-approved auto loans		896,314		578,220
Other		75,567		85,060
Total	\$	35,450,724	\$	30,628,025

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.

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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>	2020	2019
Land and buildings	\$ 1,957,621	\$ 1,881,083
Equipment, furniture and fixtures	705,498	647,286
Computer software and capitalized IT assets	970,152	796,088
Leasehold improvements	188,635	184,026
Subtotal	3,821,906	3,508,483
Less: Accumulated depreciation/amortization	(1,462,784)	(1,233,089)
Total	\$ 2,359,122	\$ 2,275,394

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, 2020 were as follows:

<i>(dollars in thousands)</i>	Amount
2021	\$ 28,261
2022	25,386
2023	21,265
2024	16,959
2025	12,944
Thereafter	31,369
Total	\$ 136,184

Rent expense was \$35.9 million and \$33.9 million for the years ended December 31, 2020 and 2019, 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, 2020 and 2019 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, 2020 and 2019. Navy Federal will continue to monitor developments regarding the COVID-19 pandemic and measures implemented in response to the COVID-19 pandemic, overall economic and industry conditions and any other triggering events or circumstances that may cause an impairment of goodwill in the future.

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 \$11.3 billion and \$8.8 billion at December 31, 2020 and 2019, respectively.

As of December 31, 2020, scheduled maturities of time deposits for each of the next five years were as follows:

<i>(dollars in thousands)</i>	Amount
2021	\$ 22,124,304
2022	5,727,875
2023	3,399,360
2024	3,633,856
2025	923,231

Overdrafts on demand deposits of \$53.2 million and \$83.7 million at December 31, 2020 and 2019, respectively,

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have been reclassified to Loans 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, 2020 and 2019 were as follows:

	December 31, 2020				
<i>(dollars in thousands)</i>	Amount Outstanding	Coupon	Fixed/Float	Payment	Maturities
FHLB borrowing	\$ 1,880,000	2.76% - 4.72%	Fixed	Monthly	2022 - 2037
FHLB borrowing	2,415,000	2.90% - 4.62%	Fixed	Quarterly	2023 - 2033
FHLB borrowing	2,200,000	0.22% - 0.32%	Float	Quarterly	2021 - 2021
Total FHLB borrowings	\$ 6,495,000				

	December 31, 2019				
<i>(dollars in thousands)</i>	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				

The following table displays the amount of borrowed funds by maturity for each of the next five years and thereafter as of December 31, 2020:

<i>(dollars in thousands)</i>	Amount
2021	2,200,000
2022	15,000
2023	50,000
2024	-
2025	115,000
Thereafter	4,115,000
Total	\$ 6,495,000

During 2020 and 2019, Navy Federal prepaid \$5.3 billion and \$1.2 billion of its borrowings with the FHLB, respectively. In connection with these prepayments, Navy Federal incurred \$41.5 million and \$26.9 million of debt extinguishment costs, respectively, which is included in Other non-interest expense in the Consolidated Statements of Income.

As of December 31, 2020, Navy Federal pledged \$25.5 billion of consumer and credit card loans to the FRB as collateral for the ability to borrow up to \$19.6 billion. As of December 31, 2020, Navy Federal pledged \$29.1 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 \$25.2 billion. 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 and \$0.8 billion in investment securities to the FHLB as collateral for the ability to borrow up to \$27.0 billion.

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

<i>(dollars in thousands)</i>	2020	2019
Federal Reserve Bank	\$ 19,649,854	\$ 20,997,758
FHLB	18,730,633	16,539,321
Fed Funds	250,000	250,000
Total	\$ 38,630,487	\$ 37,787,079

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.

The pension assets, net of the accumulated benefit obligation 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:

<i>(dollars in thousands)</i>	Pension		Retiree Medical	
	2020	2019	2020	2019
Accumulated benefit obligation at year end	\$ 1,516,827	\$ 1,313,775	N/A	N/A
Projected benefit obligation at year end	1,748,016	1,467,650	72,331	66,246
Fair value of plan assets at year end	1,894,772	1,682,982	-	-
Over/(under) funded	146,756	215,332	(72,331)	(66,246)
Employer contributions	65,000	25,000	3,258	2,985
Plan participants' contributions	-	-	127	184
Benefits paid	(56,063)	(53,725)	(3,385)	(3,169)
Net periodic benefit cost	8,247	21,653	5,255	4,625

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:

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	Pension		Retiree Medical	
	2020	2019	2020	2019
Discount rate				
Projected benefit obligation	2.65%	3.35%	2.80%	3.35%
Net periodic benefit cost	3.35%	4.35%	3.35%	4.35%
Rate of compensation increase				
Projected benefit obligation	5.16%	4.43%	N/A	N/A
Net periodic benefit cost	4.44%	4.43%	N/A	N/A
Expected long-term rate of return	6.50%	7.00%	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	
(dollars in thousands)	2020	2019	2020	2019
Accumulated other comprehensive loss				
Net prior service cost	\$ 17,635	\$ 21,805	\$ 591	\$ 831
Net loss	351,156	221,658	20,797	16,468
Accumulated other comprehensive loss	\$ 368,791	\$ 243,463	\$ 21,388	\$ 17,299

The amounts recognized in AOCI for the years ended December 31, 2020 and 2019 consist of:

	Pension		Retiree Medical	
(dollars in thousands)	2020	2019	2020	2019
Amounts amortized during the year				
Net prior service cost	\$ (4,171)	\$ (5,284)	\$ (239)	\$ (239)
Net loss	(8,411)	(14,331)	(844)	(253)
Amounts arising during the year				
Net prior service cost	-	-	-	-
Net (gain)/loss	137,910	(23,786)	5,172	8,003
Total recognized in other comprehensive (income)/loss	\$ 125,328	\$ (43,401)	\$ 4,089	\$ 7,511

The amounts in AOCI expected to be recognized as components of net periodic benefit cost in 2021 are as follows:

	Pension		Retiree Medical	
(dollars in thousands)				
Net loss	\$	13,325	\$	1,073
Prior service cost		3,666		239
Total expected amortization	\$	16,991	\$	1,312

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

	Pension		Retiree Medical	
(dollars in thousands)				
2021		71,255		3,252
2022		75,609		3,257
2023		80,008		3,316
2024		84,381		3,348
2025		88,857		3,356
2026-2030		504,713		17,173

The anticipated employer contribution for 2021 is \$25 million for the pension plan and \$3.3 million for the retiree medical benefit plan. The measurement date for the pension and retiree medical benefit plan for 2020 and 2019 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

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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, 2020, 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 a defensive equity fund 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:

(dollars in thousands)				
December 31, 2020				
Asset Category	Level 1	Level 2	Level 3	Total
U.S. equity securities	\$ 98,083	\$ -	\$ -	\$ 98,083
Global equity securities	767,267	-	-	767,267
Fixed-income securities	356,174	203,729	-	559,903
Cash and cash equivalents	30,556	-	-	30,556
Total assets in the fair value hierarchy	\$ 1,252,080	\$ 203,729	\$ -	\$ 1,455,809
Investments measured at net asset value:				438,963
Total investments				\$ 1,894,772

(dollars in thousands)				
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

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 and non-agency collateralized mortgage obligation securities are valued using observable inputs based on similar assets in the market place.

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

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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 \$77.6 million and \$68.1 million for the years ended December 31, 2020 and 2019, 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, 2020 and 2019, total liability related to these plans was \$8.7 million and \$8.1 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, 2020 and 2019 were \$58.0 million and \$52.0 million, respectively. Total deposit balances of credit union officials as of December 31, 2020 and 2019 were \$33.3 million and \$27.5 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, 2020			
	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	\$ (260,762)	\$ 375,713	\$ (170,872)	\$ (55,921)
OCI before reclassifications	(143,082)	840,718	(210,554)	487,082
Amounts reclassified from AOCI to:				
Salaries and employee benefits	13,665	-	-	13,665
Net (gain)/loss on investments	-	(256,275)	-	(256,275)
Interest on borrowed funds	-	-	114,335	114,335
Net change in AOCI	(129,417)	584,443	(96,219)	358,807
Balance, end of year	\$ (390,179)	\$ 960,156	\$ (267,091)	\$ 302,886

	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)

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.

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, 2020 and 2019 was 5.67% and 6.08%, respectively. As of December 31, 2020, the RBNW criterion has not been met. Therefore, Navy Federal is not considered complex.

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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 10.78% and 12.34% as of December 31, 2020 and 2019, 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, 2020 that management believes would have changed Navy Federal's categorization.

As of December 31, 2019, Navy Federal met the minimum average reserve balance during a 14-day maintenance period as required by the FRB. Effective March 2020, the FRB eliminated this requirement.

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, 2020 and 2019.

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, 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.

Loans Held for Investment

Loans held for investment at fair value are transferred from MLAS for which the fair value option was elected at the time of origination. These loans do not trade in an active, open market with readily observable prices. Therefore, Navy Federal uses internal valuation models and a combination of both observable market inputs based on loans with similar characteristics as well as Navy Federal specific risk factors and adjustments to value these loans. As significant unobservable inputs are utilized in their valuation, these loans are classified as Level 3 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, 2020				
(dollars in thousands)	Level 1	Level 2	Level 3	Netting Adjustments ⁽¹⁾	Total
Available-for-sale debt securities					
U.S. government and federal agency securities	\$ -	\$ 6,747,761	\$ -	\$ -	\$ 6,747,761
Residential mortgage-backed securities	-	10,669,271	-	-	10,669,271
Commercial mortgage-backed securities	-	509,696	-	-	509,696
Bank notes and corporate bonds	-	3,705,479	-	-	3,705,479
Municipal securities	-	386,045	-	-	386,045
Non-U.S. government securities	-	254,424	-	-	254,424
Total available-for-sale debt securities	-	22,272,676	-	-	22,272,676
Mortgage loans awaiting sale	-	3,501,444	-	-	3,501,444
Loans held for investment	-	-	691,241	-	691,241
Mortgage servicing rights	-	-	418,954	-	418,954
Derivatives ⁽²⁾	-	2,494	88,329	(2,493)	88,330
Total assets at fair value on a recurring basis	\$ -	\$ 25,776,614	\$ 1,198,524	\$ (2,493)	\$ 26,972,645
Derivatives ⁽²⁾	\$ -	\$ 32,234	\$ 6	\$ (2,493)	\$ 29,747
Total liabilities at fair value on a recurring basis	\$ -	\$ 32,234	\$ 6	\$ (2,493)	\$ 29,747

⁽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, 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
Equity securities	-	-	-	-	-
Mortgage loans awaiting sale	-	2,477,253	-	-	2,477,253
Loans held for investment	-	-	77,172	-	77,172
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	\$ 604,648	\$ (1,958)	\$ 21,857,072
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.

Items measured as Level 3 in the fair value hierarchy as of December 31, 2020 and 2019 consist of MSRs, loans held for investment for which the fair value option was selected and interest rate lock derivatives. Issuances of MSRs for the years ending December 31, 2020 and 2019 were \$134.6 million and \$140.0 million, respectively. There were no issuances of loans held for investment that are accounted for at fair value for the years ending December 31, 2020 and 2019. Additions during the year only consisted of transfers as noted below. Issuances of interest rate lock derivatives for the years ending December 31, 2020 and 2019 were \$563.7 million and \$282.5 million, respectively.

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 date of the event or change in circumstances that caused the transfer. Loans originated as MLAS that are subsequently reclassified to held for investment are transferred from Level 2 into Level 3 of the fair value hierarchy. During the years ended December 31, 2020 and 2019, \$676.0 million and \$81.3 million of MLAS were reclassified to loans held for investment, respectively. There were no transfers out of Level 3 for the years ended December 31, 2020 and 2019.

Note 17: Subsequent Events

Navy Federal evaluated subsequent events through March 19, 2021, the date these financial statements were issued, and concluded that no subsequent events existed that are material to the consolidated financial statements.





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