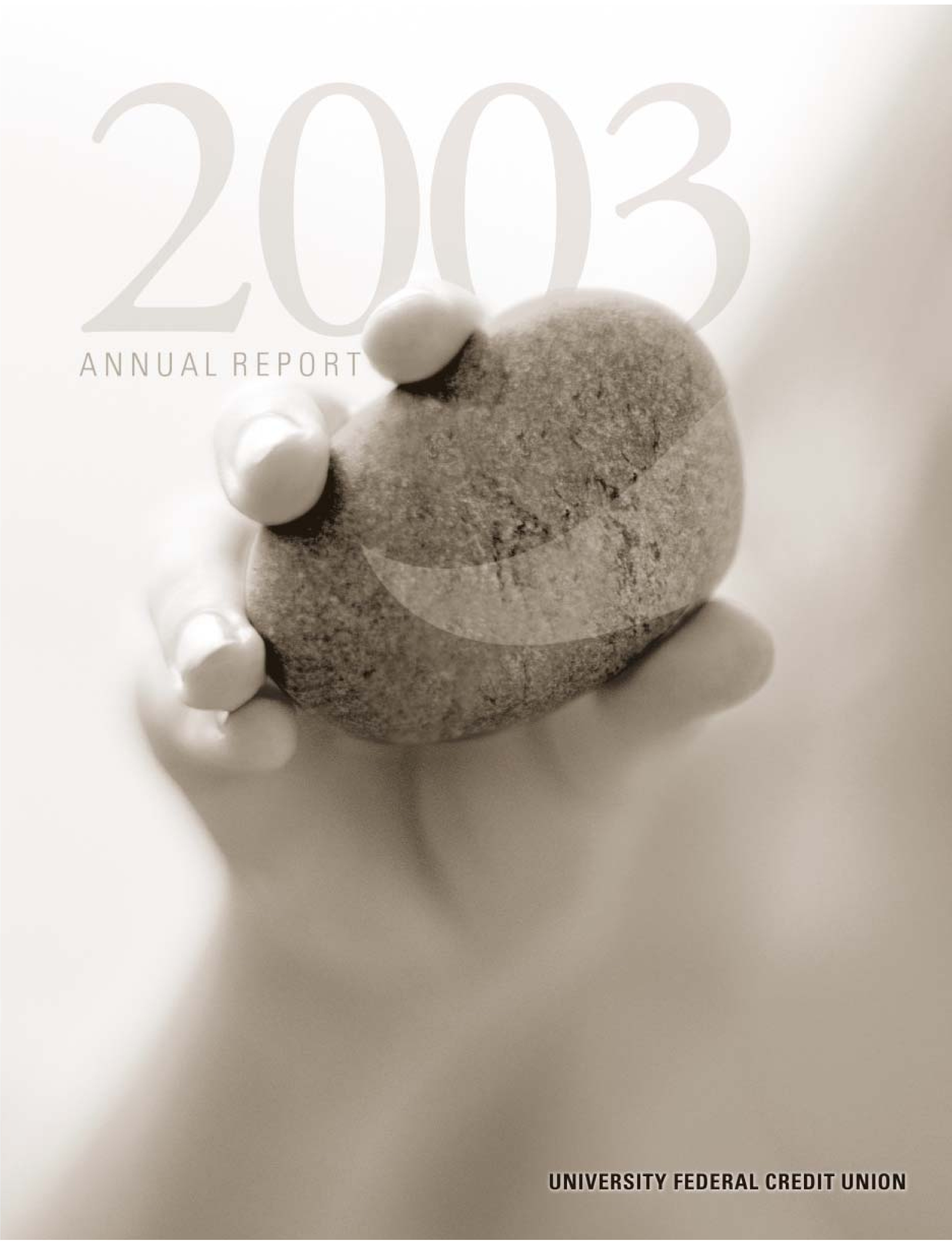
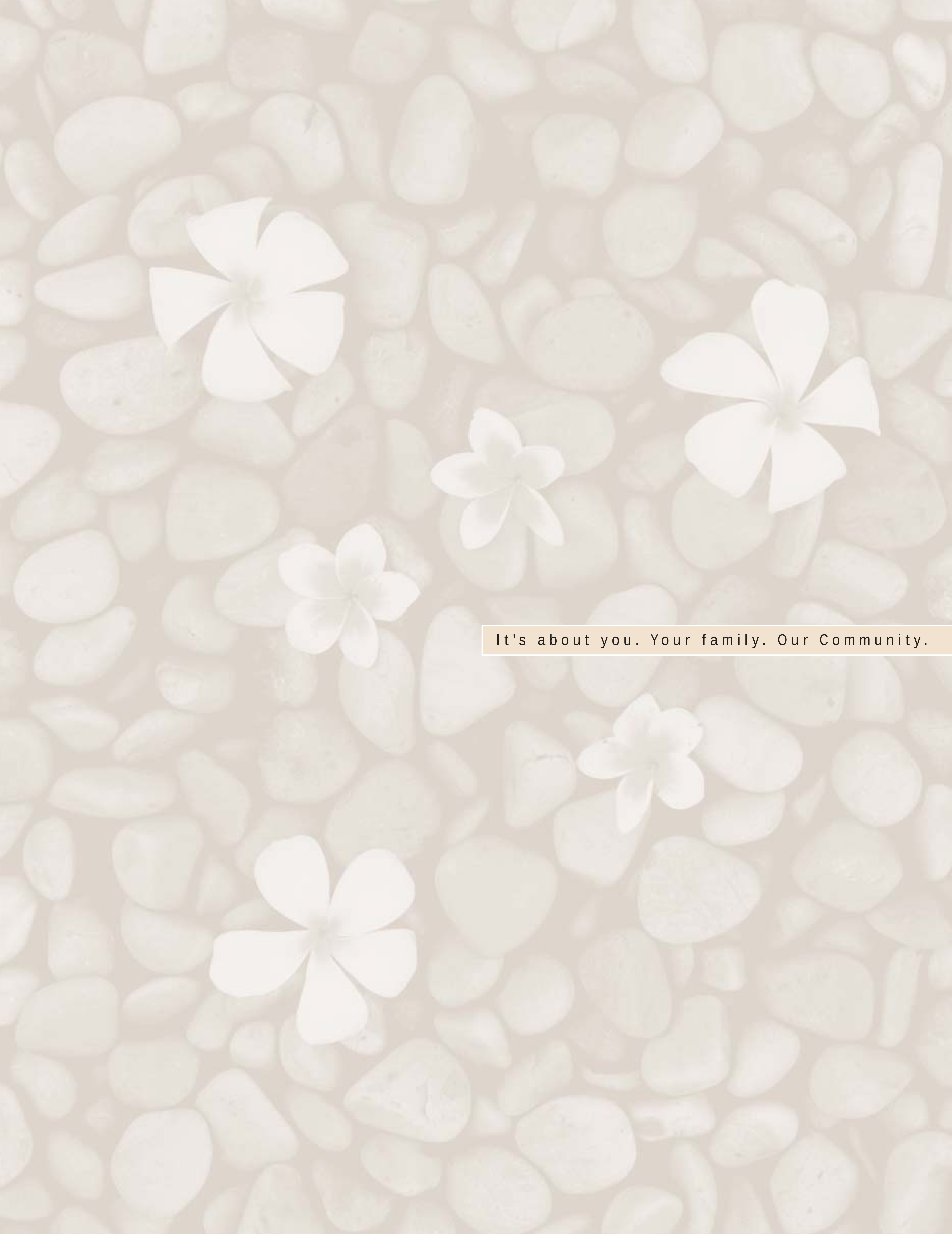
2003

ANNUAL REPORT



UNIVERSITY FEDERAL CREDIT UNION



It's about you. Your family. Our Community.

Contents:

Chairman's Report

On behalf of UFCU's volunteer Board of Directors, I am proud to report exceptional 2003 financial performance and inception of several critical product and service enhancements which positioned us to better serve our almost 100,000 members. Noteworthy were University Federal Credit Union's continuing emphasis on:

• **Financial education and consumer advocacy**, supported through UFCU's Trusted Advisor program, which offers members unbiased consumer news and advice on how to save money, protect privacy, improve credit, prevent fraud, and confidently manage assets.

• **Strengthened geographic convenience** through an expanded ATM nework, a new full-service branch at Brodie Lane in Southwest Austin, a drive-thru facility at Capitol Credit Union's Ben White/South Congress location, and a remodeled Galveston facility. Members can now access their accounts at 11 proprietay branch facilities and more than 1,300 shared credit union facilities across the country.

• **Expanded investment, brokerage and financial planning** products and services offered through UFCU Financial Services, LLC, which allows UFCU to capably and professionally meet the financial needs of our members, regardless of their stage in life.

• **Enhancement of electronically delivered services** to include eStatements, which replace paper statements, and eChecks, which enable members to electronically view cleared checks, services well received by members. UFCU members regularly access On Demand Internet Banking and Bill Pay services at ufcu.org more than 300,000 times each month!

• **Greatly expanded lending programs** that include a broader menu of mortgage options, flexible small business lending terms, an exceptionally strong education lending program, and home equity lines-of-credit, which are newly available to Texas homeowners.

• **Serving the communities in which we live and work.** We are proud to be from Austin and Galveston, and encourage our employees to be actively involved in the social fabric of the cities we call home.

Our dedicated volunteers and talented staff have built and nurtured a dynamic organizational culture that well positions University Federal Credit Union for continued success in years to come. On behalf of your Board of Directors, I thank you for your membership and the trust you place in UFCU to help manage your financial affairs. After 67 years of service and as Austin's largest, locally-owned financial institution with $600 million in assets, we continue to do business as we always have, one member at a time.

Respectfully,

Mary A. Seng, Chairman

Standing from left to right:

George K. Herbert, Ph.D.
Carl E. Hansen, Ph.D.
Thomas J. Ardis
Arthur B. Martinez
Gilbert O. Gallegos
William T. Guy, Jr., Ph.D.

Seated from left to right:

Cynthia A. Leach
Frank J. Peters
Mary A. Seng
Marilla D. Svinicki, Ph.D.

Board of Directors 2003

Board of Directors:

Mary A. Seng, Chairman
Carl E. Hansen, Ph.D., Vice Chairman
Arthur B. Martinez, Treasurer
Cynthia A. Leach, Secretary
Thomas J. Ardis
Gilbert O. Gallegos
William T. Guy, Jr., Ph.D.
Frank J. Peters
Marilla D. Svinicki, Ph.D.
George K. Herbert, Ph.D., Director Emeritus

Supervisory Committee:

Ned H. Burns, Ph.D., Chairman
Doris F. Constantine, Secretary
George K. Herbert, Ph.D.
Dana M. Malone
Christine A. Plonsky

Treasurer's Report

In spite of a weak economy, UFCU's commitment to responsibly deliver exceptional products and services to its members resulted in strong 2003 performance. Total assets, at year's end, grew 9% to $595 million, while member deposits grew $43 million, or 8.9%, to $536 million. Fueled by extensive mortgage loan refinancing, loans disbursed in 2003 totaled $462 million, boosting total loans outstanding by $101 million, or 28.6%, to $455 million. On total revenues of $45 million, UFCU generated net income of $6 million and elevated reserves 12% to $48 million. This additional capital financially strengthens UFCU and positions us to continue expanding and enhancing our member services.

UFCU Financial Services, LLC, our wholly-owned financial subsidiary, continued to help members build and manage their wealth through attractive, nontraditional financial products and services, including comprehensive financial planning, online brokerage services, a variety of insurance alternatives, and attractive tax preparation services.

As each year brings new challenges, University Federal Credit Union will remain financially strong, retaining our members' trust and confidence.

Best Regards,

Arthur B. Martinez, Treasurer

Supervisory Committee's Report

The Supervisory Committee's primary responsibility is to ensure that UFCU's financial statements accurately and fairly portray the organization's financial condition. To fulfill that obligation, the Committee retained Orth, Chakler, Murnane & Company, an independent accounting firm in Miami, FL, to audit the 2003 financial statements. We are pleased to present their opinion in the Independent Auditor's Report as part of this Annual Report.

In addition to ensuring accurate financial statements, the Supervisory Committee, composed of volunteer members appointed by the Board of Directors, reviews management practices and addresses safety and soundness issues. To that end, the Committee regularly meets with management and directs the activities of the Internal Auditor to monitor internal controls and regulatory compliance. The Committee also reviews related reports from third party consultants and from the National Credit Union Administration, the federal credit union regulator.

Considerable attention is given to both external and internal audit findings and recommendations. The Committee reviews management's responses and commitments to audit issues, and ensures their successful resolution. We praise management for its responsiveness with respect to audit and examination issues, as well as with critical issues of employee safety, network security and privacy.

Throughout the year, Committee members kept abreast of critical issues by attending Board meetings, reviewing Board materials and governance issues, and attending educational events. The Committee is grateful to the Board for its ongoing support.

For their time and efforts, I personally thank the individual members of the Committee: Doris Constantine, Dr. George K. Herbert, Ph.D., Dana Malone and Chris Plonsky.

Best Regards,

Dr. Ned H. Burns, Ph.D., Chairman

Independent Auditors' Report

February 13, 2004

To the Supervisory Committee of University Federal Credit Union

We have audited the accompanying consolidated statements of financial condition of University Federal Credit Union as of December 31, 2003 and 2002, and the related consolidated statements of income, comprehensive income, members' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Credit Union's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

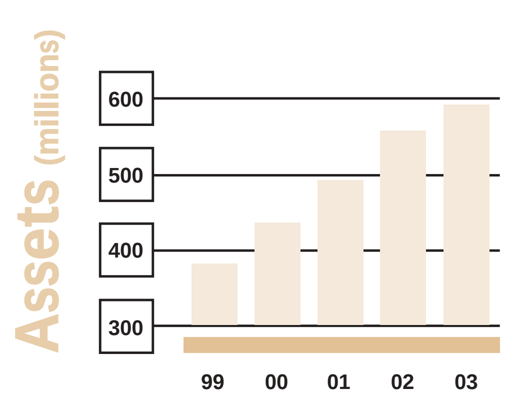
We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

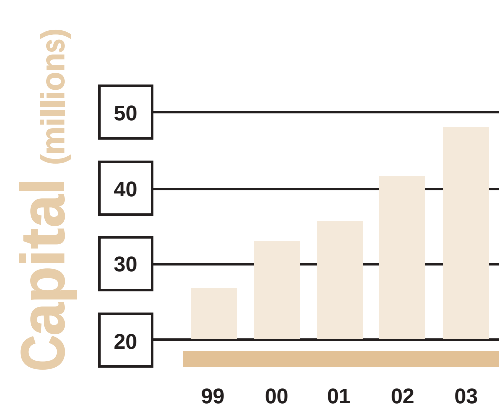
In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of University Federal Credit Union as of December 31, 2003 and 2002, and the results of its consolidated operations and its consolidated cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

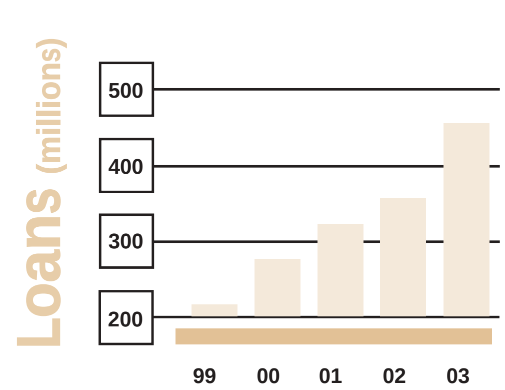
Orth, Chakler, Murnane & Co.

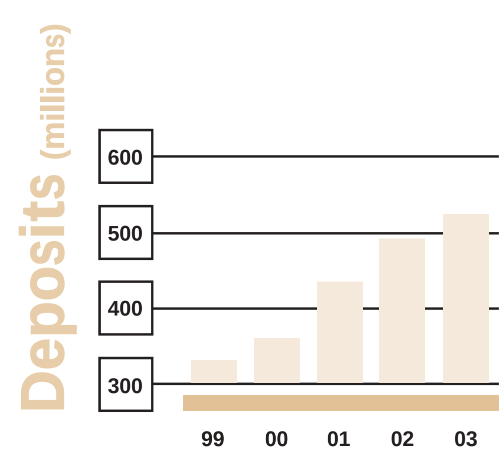
Orth, Chakler, Murnane & Company
Certified Public Accountants

Financial Highlights:









Financials 2002/2003

Consolidated Statements of Financial Condition:

Assets

	As of December 31, 2003	2002
Cash and cash equivalents	$43,752,823	$36,699,979
Investments:		
Available-for-sale	66,819,525	113,087,990
Other	5,659,901	21,655,679
Loans held for sale, student loans	25,082,057	23,625,223
Loans held for sale, real estate	600,000	451,085
Loans to members, net of allowance for loan losses	426,852,473	326,460,355
Accrued interest receivable	2,080,104	2,141,453
Prepaid and other assets	3,110,392	2,776,603
Property and equipment	15,662,762	14,535,059
NCUSIF deposit	5,062,272	4,438,830
Total assets	$594,682,309	$545,872,256

Liabilities & Members' Equity

	As of December 31, 2003	2002
LIABILITIES:		
Members' share and savings accounts	$535,856,106	$492,048,836
Accrued expenses and other liabilities	11,091,507	11,218,373
Total liabilities	546,947,613	503,267,209
Commitments and contingent liabilities	–	–
MEMBERS' EQUITY:		
Regular reserve	8,004,559	8,004,559
Undivided earnings	40,077,117	34,088,657
Accumulated other comprehensive (loss)/income	(346,980)	511,831
Total members' equity	47,734,696	42,605,047
Total liabilities and members' equity	$594,682,309	$545,872,256

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

Consolidated Statements of Income:

	For the years ended December 31, 2003	2002
INTEREST INCOME:		
Loans to members	$27,812,230	$24,818,360
Investments	2,896,711	5,842,825
Total interest income	30,708,941	30,661,185
INTEREST EXPENSE:		
Members' share and savings accounts	6,244,647	9,625,835
Borrowed funds	11,439	7,750
Total interest expense	6,256,086	9,633,585
Net interest income	24,452,855	21,027,600
PROVISION FOR LOAN LOSSES	2,460,094	2,149,311
Net interest income after provision for loan losses	21,992,761	18,878,289
NON-INTEREST INCOME:		
Fees and service charges	13,205,077	11,910,093
Gain on sale of loans	2,145,697	1,837,481
Gain on sale of investments	—	95,794
Total non-interest income	15,350,774	13,843,368
	37,343,535	32,721,657
NON-INTEREST EXPENSE:		
Compensation and employee benefits	13,950,940	12,206,131
Office operating	11,387,596	9,975,061
Other	3,199,915	2,457,162
Marketing and business development	1,966,801	1,578,112
Loss on sale of real estate loans	814,592	—
Loss on sale of investments	35,231	—
Total non-interest expense	31,355,075	26,216,466
Net income	$5,988,460	$6,505,191

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

Consolidated Statements of Comprehensive Income:

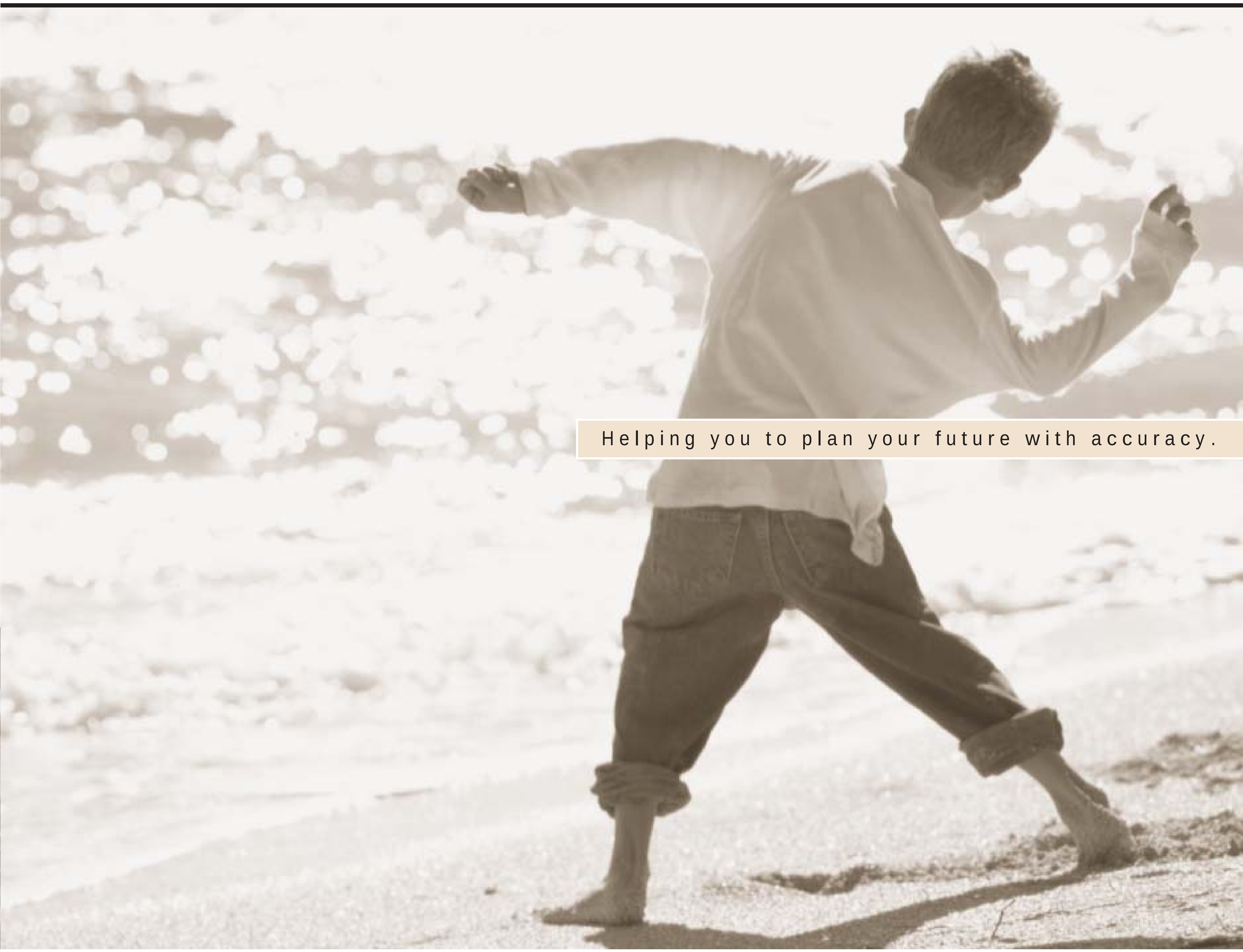
	For the years ended December 31, 2003	2002
NET INCOME	$5,988,460	$6,505,191
OTHER COMPREHENSIVE INCOME:		
Unrealized holding (losses) on available-for-sale investments arising during the period	(894,042)	(63,492)
Reclassification adjustments for losses/(gains) included in net income	35,231	(95,794)
Other comprehensive loss	(858,811)	(159,286)
Comprehensive income	$5,129,649	$6,345,905

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

Consolidated Statements of Members' Equity:

	For the years ended December 31, 2003, and 2002			
	Regular Reserve	Undivided Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2001	$8,004,559	$27,583,466	$671,117	$36,259,142
Net income	—	6,505,191	—	6,505,191
Other comprehensive loss	—	—	(159,286)	(159,286)
Balance, December 31, 2002	8,004,559	34,088,657	511,831	42,605,047
Net income	—	5,988,460	—	5,988,460
Other comprehensive loss	—	—	(858,811)	(858,811)
Balance, December 31, 2003	$8,004,559	$40,077,117	($346,980)	$47,734,696

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



Consolidated Statements of Cash Flow:

	For the years ended December 31, 2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$5,988,460	$6,596,627
Adjustments:		
Provision for loan losses	2,460,094	2,057,875
Depreciation and amortization	2,801,799	2,304,510
Amortization/accretion of investment premiums/discounts, net	488,285	515,818
Amortization of deferred fees and costs	496,669	343,436
Loss/(gain) on sale of investments	35,231	(95,794)
Amortization of servicing rights	48,481	—
Loss on sale of real estate loans	814,592	—
Gain on sale of student loans	(2,145,697)	(1,837,481)
Changes in operating assets and liabilities:		
Loans held for sale, student loans	688,863	(179,593)
Accrued interest receivable	61,349	161,990
Prepaid and other assets	(382,270)	(737,507)
Accrued expenses and other liabilities	(126,866)	(622,234)
Net cash provided by operating activities	11,228,990	8,507,647
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from maturities, sales, and repayments of available-for-sale securities	72,568,300	101,661,273
Purchase of available-for-sale securities	(27,682,162)	(104,944,877)
Net change in other investments	15,995,778	(11,766,263)
Net change in loans to members, net of charge-offs	(149,175,877)	(34,399,563)
Recoveries on loans charged off	216,545	217,605
Expenditures for property and equipment	(3,929,502)	(4,636,659)
Proceeds from sale of mortgage loans	44,646,944	—
Change in NCUSIF deposit	(623,442)	(491,330)
Net cash used in investing activities	(47,983,416)	(54,359,814)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net change in members' share and savings accounts	43,807,270	48,435,097
Net cash provided by financing activities	43,807,270	48,435,097
Net change in cash and cash equivalents	7,052,844	2,582,930
Cash and cash equivalents at beginning of year	36,699,979	34,117,049
Cash and cash equivalents at end of year	$43,752,823	$36,699,979
SUPPLEMENTAL CASH FLOWS DISCLOSURES:		
Interest paid	$6,255,514	$9,633,231
SCHEDULE OF NON-CASH TRANSACTIONS:		
Change in unrealized gain/loss on investments	$858,811	$159,286
Transfer from loans to members to loans held for sale, real estate	$45,610,451	$—
Servicing rights capitalized	$501,450	$—

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

Notes to the Consolidated Financial Statements

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Note One: SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION

University Federal Credit Union (the "Credit Union") is a cooperative association organized in accordance with the provisions of the Federal Credit Union Act for the purpose of promoting thrift among, and creating a source of credit for, its members. Participation in the Credit Union is limited to those individuals that qualify for membership. The field of membership is defined in the Credit Union's Charter and Bylaws.

FINANCIAL STATEMENTS

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the dates of the consolidated financial statements and the reported amounts of revenues and expenses for the periods then ended. Actual results could differ from those estimates. Estimates that are particularly susceptible to change relate to the determination of the allowance for loan losses and the fair value of financial instruments. The significant accounting principles and policies used in the preparation of these consolidated financial statements, together with certain related information, are summarized below.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Credit Union and the significant accounts of its wholly owned Credit Union Service Organization (CUSO), UFCU Financial Services, LLC. All significant intercompany accounts and transactions have been eliminated.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash on hand, demand deposits and non-term share deposits in Southwest Corporate Federal Credit Union. Amounts due from banks and the corporate credit union may, at times, exceed federally insured limits.

INVESTMENTS

Investments are classified into the following categories: available-for-sale and other. Investment securities classified as available-for-sale are measured at market value as of the consolidated statement of financial condition date. Unrealized gains and losses for available-for-sale investments are reported as a separate component of members' equity. The Credit Union has elected to classify certain cash equivalents as other investments. This election is available to the Credit Union according to the terms of SFAS No. 95, "Statement of Cash Flows." Realized gains and losses on disposition, if any, are computed using the specific identification method. Investments are adjusted for amortization of premiums and accretion of discounts over the term of the investment by a method which approximates the interest method. Adjustments are recognized to interest income on investments.

LOANS HELD FOR SALE

Loans intended for sale in the secondary market are carried at the lower of cost or estimated market value in the aggregate. All sales are made without recourse.

LOANS TO MEMBERS AND ALLOWANCE FOR LOAN LOSSES

Loans to members are stated at the amount of unpaid principal net of certain deferred fees and costs and reduced by an allowance for loan losses. The allowance for loan losses is increased by a provision for loan losses charged to expense and decreased by charge-offs (net of recoveries). Loans are charged against the allowance for loan losses when management believes that collection of the principal is unlikely. Recoveries on loans previously charged off are credited to the allowance for loan losses.

As of December 31, 2002, the allowance for loan losses was maintained at a level considered adequate to provide for expected loan losses in the portfolio based on the specific evaluation of impaired consumer loans and the Credit Union's prior loan loss experience applied to the remainder of the performing loans. As of December 31, 2003, the allowance for loan losses was maintained at a level considered adequate to provide for incurred loan losses in the portfolio by applying a historical loan loss rate to consumer loan pools that have similar risk characteristics. There is no longer a specific evaluation of impaired consumer loans. Individually significant, non-homogeneous loans are measured for impairment in accordance with SFAS No. 114. These loans are evaluated individually based on an examination of the current financial information of the borrower and an estimate of the value of the collateral, if any. If the carrying value of any of these loans is greater than the estimated net realizable value of the property or of the collateral securing these loans, a reserve is established for the difference.

Interest on loans to members is recognized over the terms of the loans and is calculated on principal amounts outstanding. The accrual of interest is discontinued when a loan exceeds 90 days delinquent or when management believes that collection of interest is doubtful. Generally, loan fees which are charged to members are recognized in income when received and direct loan origination costs on loans to members are recognized in expenses when incurred; however, certain costs paid on indirect automobile loans, mortgage loans and home equity loans are deferred over the life of the loan as an adjustment to yield on loans using a method that approximates the interest method. This is not materially different from fees and expenses that would have been recognized under the provisions of SFAS No. 91, "Accounting for Non-refundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases."

Note One: SIGNIFICANT ACCOUNTING POLICIES—CONTINUED.

MORTGAGE SERVICING RIGHTS

The Credit Union recognizes originated mortgage servicing rights (MSRs) as assets at the date of transfer by allocating the previous carrying amount between the loan and the servicing rights based on their relative fair values. The fair values of MSRs is based on the current market price for similar products. Significant assumptions used to estimate fair value include future prepayment rates based on current interest-rate levels, other economic conditions and market forecasts, as well as relevant characteristics of the servicing portfolio, such as loan types, interest-rate stratification, delinquencies and recent prepayments experience. Mortgage servicing rights are amortized based on a method which approximates the ratio of net servicing income received in the current period to total net servicing income projected to be realized from the MSRs over their fair value. For purposes of measuring impairment, MSRs are stratified on the basis of loan type and term.

PROPERTY AND EQUIPMENT

Property and equipment are carried at cost less accumulated depreciation. Buildings, and furniture and equipment are depreciated using the straight-line method over the estimated useful lives of the assets. The cost of leasehold improvements is amortized using the straight-line method over the term of the lease, or the estimated life of the asset, whichever is less. The Credit Union reviews property and equipment (long-lived assets) for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

PROPERTY AND EQUIPMENT

Property and equipment are carried at cost less accumulated depreciation. Buildings, and furniture and equipment are depreciated using the straight-line method over the estimated useful lives of the assets. The cost of leasehold improvements is amortized using the straight-line method over the term of the lease, or the estimated life of the asset, whichever is less. The Credit Union reviews property and equipment (long-lived assets) for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

NATIONAL CREDIT UNION SHARE INSURANCE FUND (NCUSIF) DEPOSIT

The deposit in the National Credit Union Share Insurance Fund (NCUSIF) is in accordance with National Credit Union Administration (NCUA) regulations, which require the maintenance of a deposit by each insured credit union. The deposit would be refunded to the Credit Union if its insurance coverage is terminated, it converts to insurance coverage from another source, or the operations of the fund are transferred from the NCUA Board.

MEMBERS' SHARE AND SAVINGS ACCOUNTS

Members' shares are subordinated to all other liabilities of the Credit Union upon liquidation. Interest on members' share and savings accounts is based on available earnings at the end of an interest period and is not guaranteed by the Credit Union. Interest rates on members' share accounts are set by the Board of Directors, based on an evaluation of current and future market conditions.

MEMBERS' EQUITY

The Credit Union is required to maintain a statutory reserve (regular reserve) in accordance with the Federal Credit Union Act. This statutory reserve is not available for the payment of interest.

REGULAR RESERVE

The Credit Union is required to maintain a statutory reserve (regular reserve) in accordance with the Federal Credit Union Act. This statutory reserve represents a regulatory restriction and is not available for the payment of interest.

FEDERAL AND STATE TAX EXEMPTION

The Credit Union is exempt from most federal, state, and local taxes.

RECLASSIFICATION'S

Certain 2002 consolidated financial statement amounts have been reclassified to conform with classifications adopted in 2003.

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Note Two: INVESTMENTS

The amortized cost and estimated market value of investments are as follows:

Available-for-sale:	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Market Value
	As of December 31, 2003			
Mortgage-backed securities	$19,466,312	$76,370	($93,712)	$19,448,970
Mutual funds	34,207,629	—	(395,400)	33,812,229
Federal agency securities	13,492,564	75,248	(9,486)	13,558,326
	$67,166,505	$151,618	($498,598)	$66,819,525

Available-for-sale:	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Market Value
	As of December 31, 2002			
Mortgage-backed securities	$42,009,142	$375,516	($51,505)	$42,333,153
Mutual funds	36,364,757	13,990	(22,163)	36,356,584
Federal agency securities	34,202,260	222,846	(26,853)	34,398,253
	$112,576,159	$612,352	($100,521)	$113,087,990

The following table shows the gross unrealized losses and fair value of investments, aggregated by length of time that individual securities have been in a continuous unrealized loss position.

	As of December 31, 2003					
	Less than 12 months		12 months or Longer		Total	
Available-for-sale:	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Mortgage-backed securities	$10,839,014	$70,231	$1,167,692	$23,481	$12,006,706	$93,712
Mutual funds	14,984,653	89,339	18,827,575	306,061	33,812,228	395,400
Federal agency securities	3,490,250	9,486	—	—	3,490,250	9,486
	$29,313,917	$169,056	$19,995,267	$329,542	$49,309,184	$498,598

Unrealized losses on securities issued by the U.S. Government and its Agencies have not been recognized into income because the principal balances of these securities are guaranteed by the U.S. Government. Additionally, the decline in these fair values is largely due to increases in market interest rates, and the fair values of the securities are expected to be recovered as these securities approach their maturity date and/or market rates decline. Management has the ability to hold these securities for the foreseeable future.

Other Investments:	As of December 31, 2003	2002
Certificates of deposit	$3,100,000	$10,100,000
Federal Home Loan Bank Stock	1,432,400	1,400,900
Capital shares in Southwest Corporate Federal Credit Union	1,000,000	1,000,000
Stock in credit union service organization	127,501	127,501
Money market account	—	9,027,278
	$5,659,901	$21,655,679

The Credit Union maintains deposits at Southwest Corporate Federal Credit Union which normally exceed federally insured limits. Included in the deposits with Southwest Corporate Federal Credit Union is a restricted capital share base which is required for membership. This amount was $1,000,000 as of December 31, 2003 and 2002.

The amortized cost and estimated market value of investments by contractual maturity are shown below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay certain obligations without call or prepayment penalties.

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Note Two: INVESTMENTS—CONTINUED

The amortized cost and estimated market value of investments are as follows:

	As of December 31, 2003 *Available-for-sale*	
	Amortized Cost	Market Value
No contractual maturity	$34,207,629	$33,812,229
1-5 years	13,492,564	13,558,326
	47,700,193	47,370,555
Mortgage-backed securities	19,466,312	19,448,970
	$67,166,505	$66,819,525

As of December 31, 2003 and 2002, securities having a market value of approximately $30,172,000 and $76,700,000, respectively, were pledged as collateral to secure borrowed funds.

Proceeds from the sale of investments classified as available-for-sale approximated $10,000,000 and $12,064,000 for the years ended December 31, 2003 and 2002, respectively. Gross gains approximated $400 and $95,800 for the years ended December 31, 2003 and 2002, respectively. Gross losses of approximately $35,600 were realized on the sale of investments classified as available-for-sale during the years ended December 31, 2003. There were no realized losses on the sale of investments classified as available-for-sale for the year ended December 31, 2002.

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Note Three: LOANS TO MEMBERS

The composition of loans to members is as follows:

	As of December 31, 2003	2002
Loans outstanding:		
Real estate	$177,314,047	$87,793,642
Vehicle	175,019,984	176,533,397
Unsecured	58,902,590	55,612,625
Shares and other collateral	8,460,584	7,642,155
Member business loans	8,088,478	1,499,844
	427,785,683	329,081,663
Deferred fees and costs	2,132,381	809,982
	429,918,064	329,891,645
Less allowance for loan losses	(3,065,591)	(3,431,290)
	$426,852,473	$326,460,355

Loans on which the accrual of interest has been discontinued or reduced approximated $936,000 and $657,000 as of December 31, 2003 and 2002, respectively. If interest on these loans had been accrued, such income would have approximated $40,000 and $28,000 for the years ended December 31, 2003 and 2002, respectively.

A summary of the activity in the allowance for loan losses is as follows:

	For the years ended December 31, 2003	2002
Balance, beginning of the year	$3,431,290	$3,196,566
Provision for loan losses	2,460,094	2,149,311
Recoveries	216,545	217,605
Loans charged off	(3,042,338)	(2,132,192)
Balance, end of year	$3,065,591	$3,431,290

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Note Four: PROPERTY AND EQUIPMENT

A summary of the Credit Union's property and equipment is as follows:

	As of December 31, 2003	2002
Land	$1,436,427	$1,436,427
Buildings	6,279,336	6,072,840
Furniture and equipment	14,402,008	13,816,983
Leasehold improvements	5,879,011	4,185,354
	27,996,782	25,511,604
Less accumulated depreciation and amortization	(12,334,020)	(10,976,545)
	$15,662,762	$14,535,059

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Note Five: MEMBERS' SHARE AND SAVINGS ACCOUNTS

Members' share and savings accounts are summarized as follows:

	As of December 31, 2003	2002
Share drafts	$130,446,627	$112,866,099
Shares and equivalents	162,087,032	139,734,356
Money market accounts	126,983,496	114,882,816
IRA shares	21,167,995	18,453,641
Share and IRA certificates	95,170,956	106,111,924
	$535,856,106	$492,048,836

The aggregate amount of members' time deposit accounts in denominations of $100,000 or more was approximately $16,671,000 as of December 31, 2003.

Scheduled maturities of certificates are as follows:

	As of December 31, 2003
Within 1 year	$68,058,778
1 to 2 years	15,009,625
2 to 3 years	5,875,800
3 to 4 years	3,827,235
4 to 5 years	2,351,298
Thereafter	48,220
	$95,170,956

SHARE INSURANCE

Members' shares are insured by the NCUSIF to a maximum of $100,000 for each member. Individual Retirement Accounts carry an additional $100,000 coverage.

6

Note Six: EMPLOYEE BENEFITS

401(K) PROFIT SHARING PLAN

Participation in the 401(k) profit sharing plan is limited to all employees who meet specific age and service year limitations. Employees may contribute up to the maximum limits authorized by the Internal Revenue Service. During the year ended December 31, 2003 and 2002, the Credit Union made a discretionary contribution of 4% of employees' compensation, which is subject to a five-year vesting schedule at the rate of 20% per year. The 401(k) profit sharing plan is structured to match 100% of employees' elective contributions up to 3% of compensation, and 50% of contributions to the extent that such contributions exceed 3% but do not exceed 5% of compensation. Employee contributions and the employer matching contributions vest immediately. The expense for the plan approximated $746,000 and $713,000 for the years ended December 31, 2003 and 2002, respectively.

7

Note Seven: COMMITMENTS AND CONTINGENT LIABILITIES

As of December 31, 2003, the Credit Union maintained a $20,000,000 unsecured and unused line-of-credit agreement with Southwest Corporate Federal Credit Union.

As of December 31, 2003, the Credit Union maintained a $6,000,000 unsecured and unused line-of-credit agreement with Bank of America.

The Credit Union has entered into a secured line-of-credit agreement to borrow funds from Southwest Corporate Federal Credit Union. Amounts borrowed under this line-of-credit agreement are secured by investments safe kept at Southwest Corporate Federal Credit Union. The available line-of-credit under this agreement fluctuates based on the amount of investments safe kept at Southwest Corporate Federal Credit Union. As of December 31, 2003, the unused line of credit was $2,790,000.

The Credit Union has entered into a secured line-of-credit agreement with the Federal Home Loan Bank of Dallas. Amounts borrowed under this line-of-credit agreement are secured by investments safe kept with the Federal Home Loan Bank of Dallas. The available line-of-credit under this agreement fluctuates based on the amount of investments safe kept at the Federal Home Loan Bank of Dallas. As of December 31, 2003, the unused line of credit was approximately $29,517,000.

The Credit Union leases certain office space and equipment. The minimum noncancelable lease obligations approximate the following as of December 31, 2003:

Year ending December 31,	Amount
2004	$1,480,000
2005	1,247,000
2006	1,138,000
2007	982,000
2008	590,000
Thereafter	2,459,000
	$7,896,000

Rental expense under operating leases was approximately $1,476,000 and $1,122,000 for the years ended December 31, 2003, and 2002, respectively.

The Credit Union has entered into an agreement to purchase a new branch located in Austin, Texas. The unfunded commitment as of December 31, 2003 approximated $1,349,000.

The Credit Union is a party to various miscellaneous legal actions normally associated with financial institutions, the aggregate effect of which, in management's opinion, would not be material to the Credit Union's consolidated financial statements.

8

Note Eight: OFF-BALANCE-SHEET RISK AND CONCENTRATIONS OF CREDIT RISK

The Credit Union is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its members and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amounts recognized in the consolidated statements of financial condition. Commitments to extend credit are agreements to lend to a member as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses. Since many of the commitments may expire without being fully drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

As of December 31, 2003, the members' total lines of credit approximated $154,680,000, of which approximately $108,470,000 had not been funded. The Credit Union evaluates each member's creditworthiness on a case-by-case basis. The amount of collateral obtained, if any, is based on management's credit evaluation of the member. The Credit Union may be exposed to credit risk from a regional economic standpoint, since a significant concentration of its borrowers work or reside in the Austin, Texas area. However, the loan portfolio is well diversified and the Credit Union does not have any significant concentrations of credit risk.

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Note Nine: REGULATORY CAPITAL

The Credit Union is subject to various regulatory capital requirements administered by the NCUA. Failure to meet minimum capital requirements can initiate certain mandatory-and possibly additional discretionary-actions by regulators that, if undertaken, could have a direct material effect on the Credit Union's consolidated financial statements. Under capital adequacy regulations and the regulatory framework for prompt corrective action, the Credit Union must meet specific capital regulations that involve quantitative measures of the Credit Union's assets, liabilities, and certain off-balance-sheet items as calculated under generally accepted accounting practices. The Credit Union's capital amounts and net worth classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Credit Union to maintain minimum amounts and ratios (set forth in the table below) of net worth (as defined in NCUA's Rules and Regulations) to total assets (as defined in NCUA's Rules and Regulations). Credit unions are also required to calculate a Risk-Based Net Worth Requirement (RBNWR) which establishes whether or not the Credit Union will be considered "complex" under the regulatory framework. The Credit Union's RBNW ratio as of December 31, 2003 was 5.39%. The minimum ratio to be considered complex under the regulatory framework is 6.0%. Management believes, as of December 31, 2003, that the Credit Union meets all capital adequacy requirements to which it is subject.

As of December 31, 2003, the most recent call reporting period, the NCUA categorized the Credit Union as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized" the Credit Union must maintain a minimum net worth ratio of 7.0% of assets. In performing its calculation of total assets, the Credit Union used the quarter-end option, as permitted by regulation. There are no conditions or events since that notification that management believes have changed the Credit Union's category.

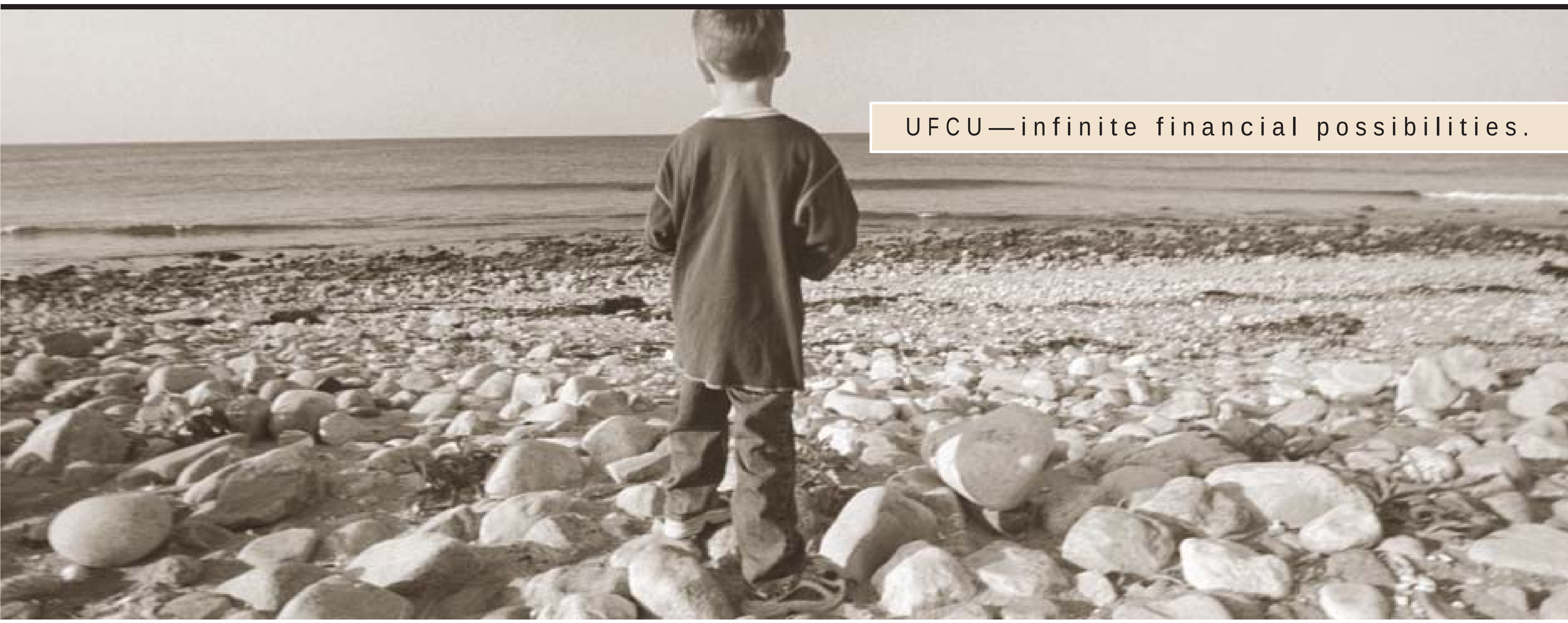
The Credit Union's actual and required net worth amounts and ratios as of December 31, 2003 and 2002 are as follows:

As of December 31, 2003

	Actual		Minimum required to be Well Capitalized	
	Amount	Ratio	Amount	Ratio
Net worth	$48,081,677	8.09%	$41,627,762	7.00%

As of December 31, 2002

	Actual		Minimum required to be Well Capitalized	
	Amount	Ratio	Amount	Ratio
Net worth	$42,093,216	7.71%	$38,211,058	7.00%



10 Note Ten: LOAN SERVICING

Mortgage loans serviced for others are not included in the accompanying consolidated statements of financial condition. The unpaid principal balances of these loans are summarized as follows:

	As of December 31, 2003	2002
Mortgage loan portfolio serviced for:		
Federal National Mortgage Association	$44,832,000	$—
Custodial escrow balances	$168,000	$—

11 Note Eleven: MORTGAGE SERVICING RIGHTS

The components of capitalized mortgage servicing rights, included in other assets, as of December 31, 2003 and 2002, were as follows:

	As of December 31, 2003	2002
Mortgage servicing rights:		
Balance, beginning of year	$—	$—
Additions	501,450	—
Amortization	(18,325)	—
	483,125	—
Less allowance for market value impairment	(30,156)	—
Balance, end of year	$452,969	$—

As of December 31, 2003, the fair value of servicing rights was determined by using a discount rate of 9.0% and an average prepayment speed of 10.77%.

12 Note Twelve: SUBSEQUENT EVENTS

As of December 31, 2003, the Credit Union had entered into an agreement to purchase an office building; however, the agreement was funded and finalized subsequent to December 31, 2003. The amount funded subsequent to December 31, 2003 approximated $1,349,000.

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Note Thirteen: FAIR VALUES OF FINANCIAL INSTRUMENTS

The estimated fair value amounts have been determined using available market information and appropriate valuation methodologies. However, considerable judgement is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented are not necessarily indicative of amounts that could be realized in a market exchange. The use of different assumptions and estimation methodologies may have a material effect on the estimated fair value amounts.

The following methods and assumptions were used to estimate fair value of each of the financial instruments for which it was practicable to estimate.

CASH AND CASH EQUIVALENTS

The carrying amount is a reasonable estimation of fair value.

INVESTMENTS

Estimated fair values for investments are obtained from quoted market prices where available.

MORTGAGE SERVICING ASSETS

Fair values of mortgage servicing assets are obtained from an independent third party evaluation.

LOANS TO MEMBERS

The estimated fair value of variable-rate loans is the current carrying amount. For estimation of fair value purposes, credit card loans are considered variable-rate loans since interest rates may be changed by the Credit Union. The fair value of fixed-rate loans should be estimated by discounting the estimated cash flows using the current rate at which similar loans would be issued; however, management has determined that the fair value of these loans would not be materially different from the carrying amount. Therefore, the fair value of fixed-rate loans is the carrying amount.

LOANS HELD FOR SALE

The carrying amount of mortgage loans held for sale is a reasonable estimation of fair value. The fair value of student loans held for sale was estimated based on the terms of the contract with North Texas Higher Education Authority, Inc., and the history of past sales.

MEMBERS' SHARE AND SAVINGS ACCOUNTS

The estimated fair value of demand deposit accounts is the carrying amount. The fair value of fixed-rate share certificates should be estimated by discounting the estimated cash flows using the current rate at which similar certificates would be issued; however, management has determined that the fair value of fixed-rate share certificates would not be materially different from the carrying amount. Therefore, the fair value of fixed-rate share certificates is the carrying amount.

The carrying value and estimated fair value of the Credit Union's financial instruments are as follows:

	As of December 31, 2003		As of December 31, 2002	
Financial Assets:	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents	$43,752,823	$43,752,823	$36,699,979	$36,699,979
Investments:				
Available-for-sale	$66,819,525	$66,819,525	$113,087,990	$113,087,990
Other	$5,659,901	$5,659,901	$21,655,679	$21,655,679
Loans held for sale	$25,682,057	$26,748,044	$24,076,308	$25,134,154
Loans to members, net	$426,852,473	$427,493,076	$326,460,355	$326,460,355
Mortgage servicing asset	$452,969	$452,969	$—	$—
Financial liabilities:				
Members' share and savings accounts	$535,856,106	$535,856,106	$492,048,836	$492,048,836
Unrecognized financial instruments:				
Commitments to extend credit	$—	$108,470,000	$—	$98,058,000

Standing from left to right:
Tony C. Budet
Steve E. Kubala
Yung V. Tran

Seated from left to right:
James A. Nastars
Sheila Jo Wojcik, Ph.D.
Michael T. Hintz

Officers 2003

Principal Officers:

President/CEO:
Tony C. Budet

Senior Vice Presidents:
Steve E. Kubala, Operations/COO
Yung V. Tran, CPA, Finance/CFO

Vice Presidents:
Michael T. Hintz, Information Technology
James A. Nastars, Lending and Collections
Sheila Jo Wojcik, Ph.D., Membership

Administration:

Senior Managers:
William R. Berglund, Real Estate and Business Lending
Yvonne V. Brooks, Human Resources
James M. Brown, Consumer Lending
Scott E. Derber, Business Development
Marla M. Heger, Performance Development
L. Vincent McConnell, Direct Delivery
Robert Miller, Information Technology
Bradley J. Shoff, Remote Delivery
Ellen S. Simpson, Internal Audit
Rhonda M. Summerbell, University Relations
Corina L. Watts, Marketing
Phillip B. Weinstein, Investment Services

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Dobie Mall
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Downtown
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Galveston
428 Postoffice Street, Galveston, Texas

Highway 79
201 West Palm Valley Boulevard, Round Rock, Texas

Lakeline
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North Guadalupe
4611 Guadalupe Street, Austin, Texas

South MoPac
5033 US Highway 290 West at MoPac, Austin, Texas

Steck
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