



FCA Board Meeting September 2021

Quarterly Report on FCS Condition September 9, 2021

**Steve Koenig
Hal Johnson**





Topics for Open Session

- Economic Conditions Affecting the Farm Credit System
 - Macro economy
 - Commodity markets
 - Farm economy
- FCS Condition and Performance
 - System growth and loan portfolio
 - Earnings and capital
 - Financial Institution Rating System (FIRS)





Economic Conditions Affecting the Farm Credit System

Steve Koenig

**Senior Agricultural Economist
Office of Data Analytics and Economics**



Strong economic growth anticipated

- Historically high 6.4% GDP growth rate in the 1st half of 2021
- U.S. and rural labor markets healing
- Robust business investment and balance sheets
- High levels of government support
- July consumer confidence falls to a 10-year low and consumer spending slows



GDP Growth to Remain High?



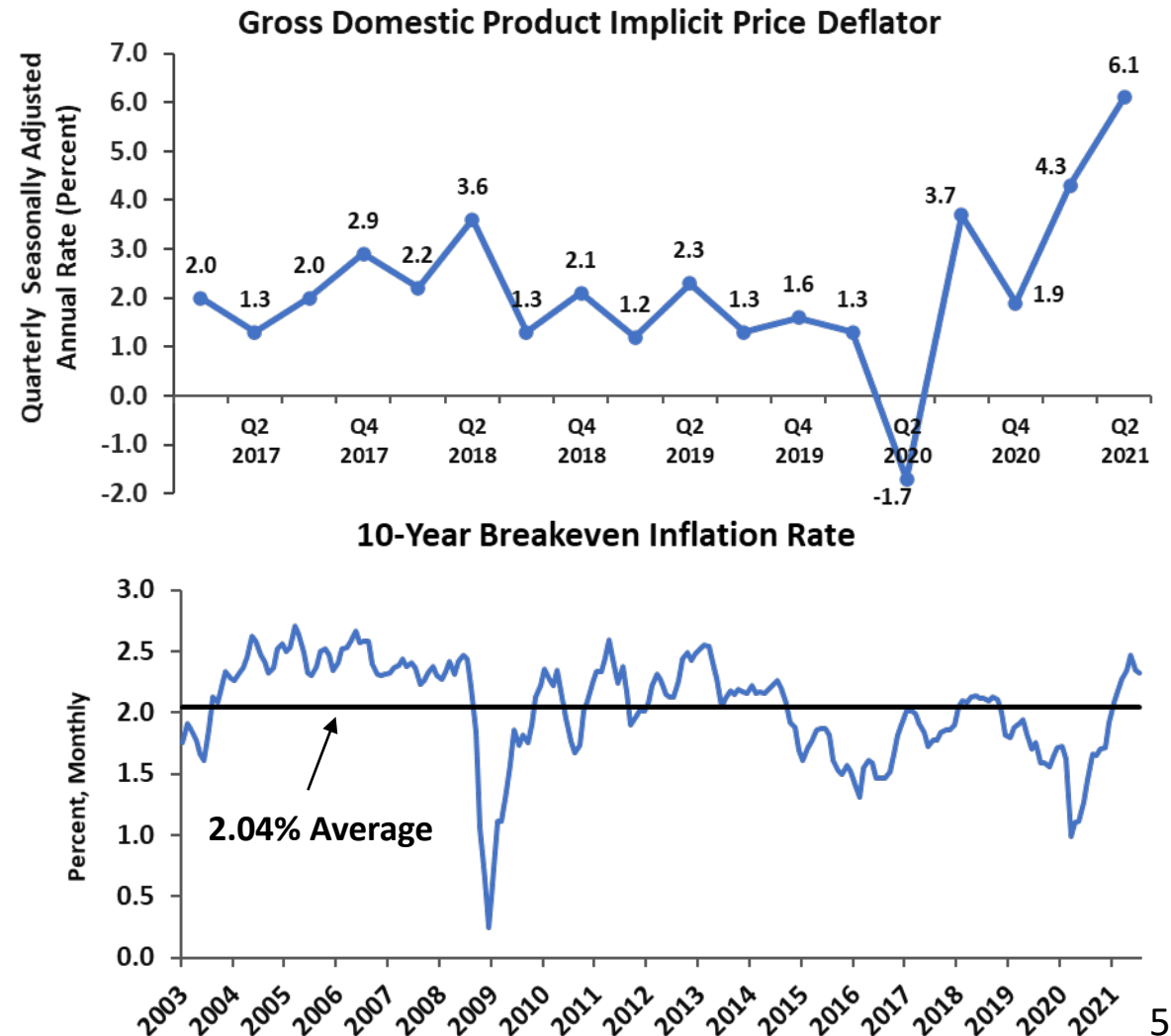
Data source: Federal Reserve Bank of St. Louis.



Inflation worries continue

Inflation accelerates in 1st half

- GDP Implicit Price Deflator exceeds 6% in the 2nd Quarter
- June and July CPI at 5.4%
- Debate on the “transitory” nature of inflation rages on
- 10-Year Treasury breakeven yield suggests the market anticipates more modest inflation ahead



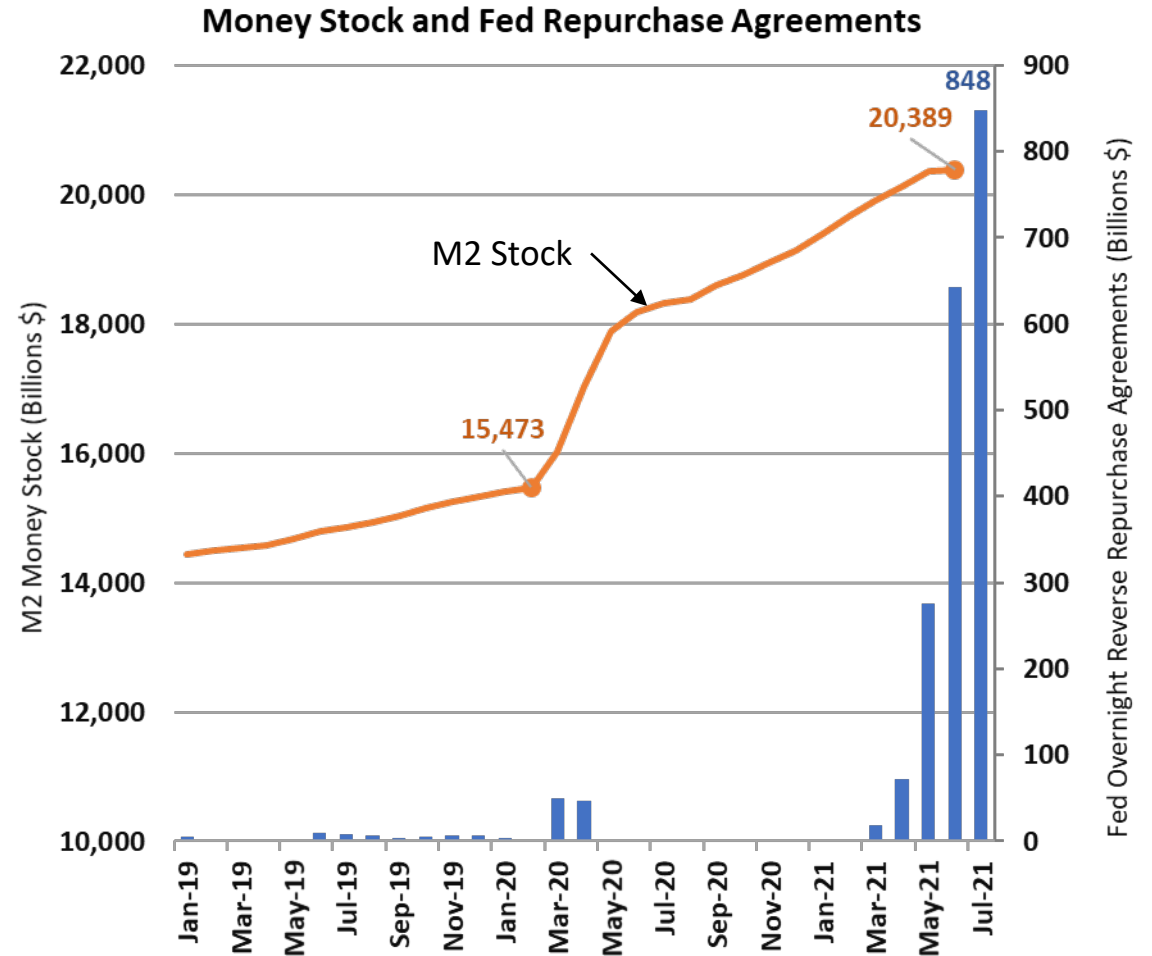
Data source: Federal Reserve Bank of St. Louis.



Central Bank response



- \$5 trillion in money supply growth
- Signals it will “soon” be “tapering” its \$120 billion in monthly purchases
- Has been extensively using Overnight Reverse Repurchase Agreements since March



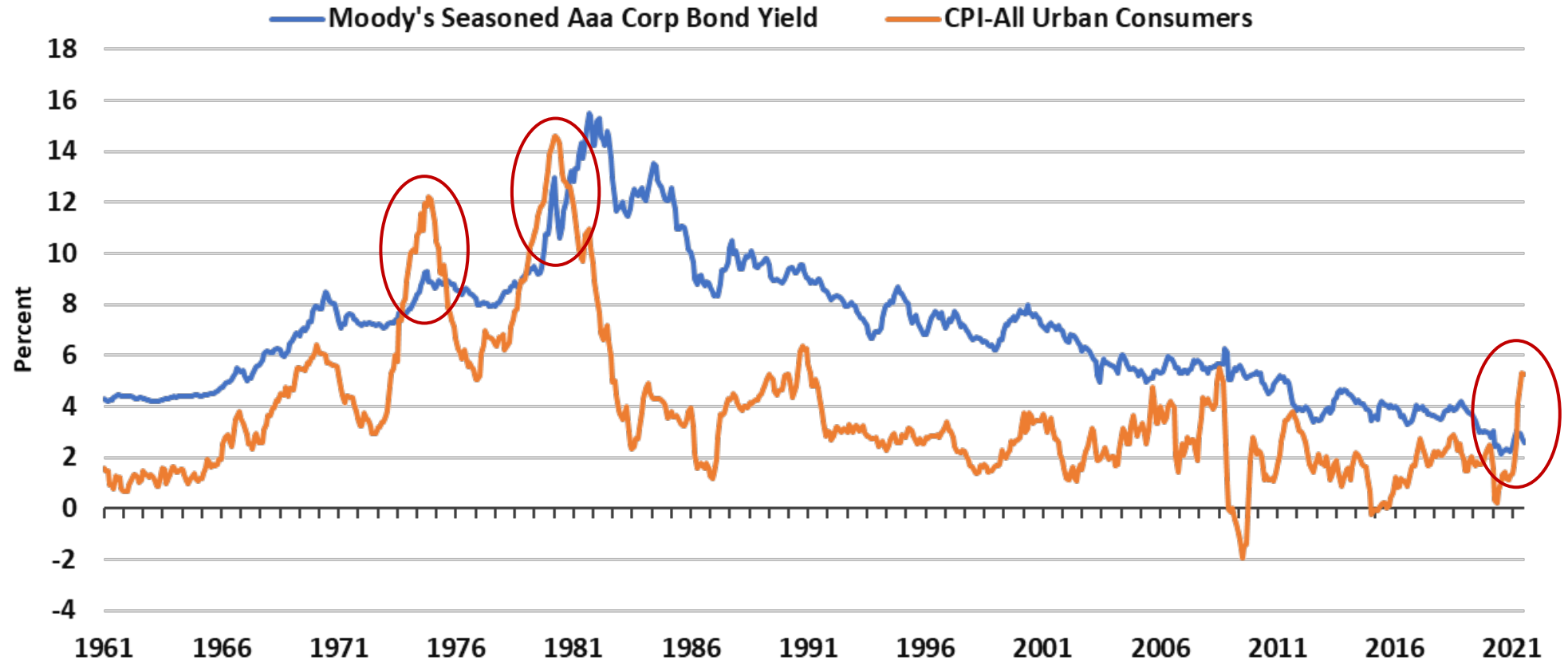
Data source: Federal Reserve Bank of St. Louis.



Negative real returns after 40-year absence



Corporate Yields and the Inflation Rate



Data source: Federal Reserve Bank of St. Louis.

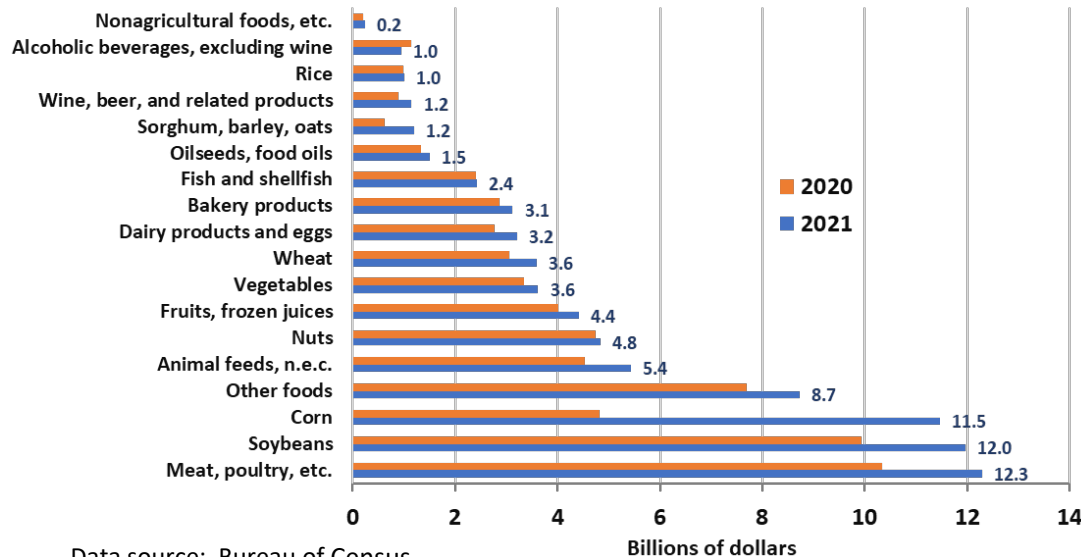


Value of agricultural exports rise in first half

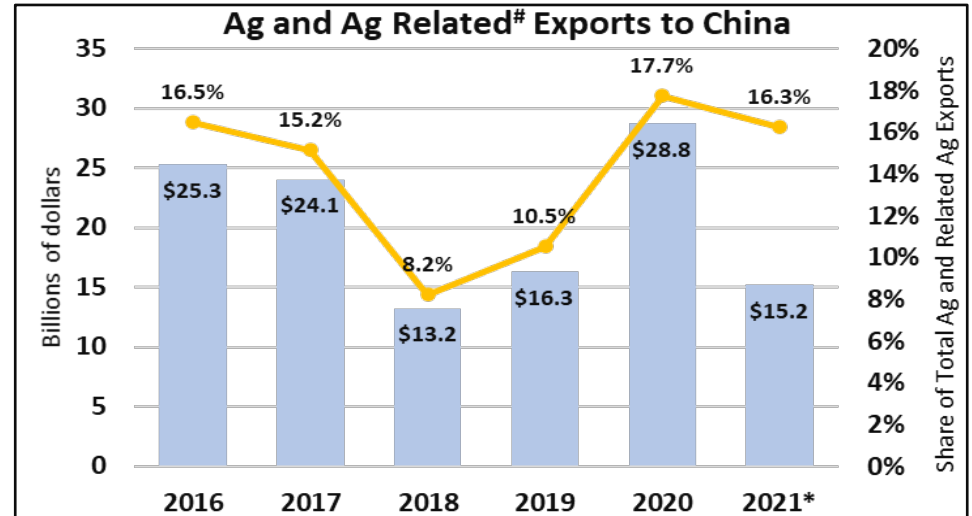
- \$ volume up 24% in the first half of 2021
- Relatively stable dollar
- Exports to China are key



US Ag/Food Exports 1st Half of the Year



Data source: Bureau of Census.



Includes, seafood, forestry, and biofuels. * First 6 months.

U.S. Export Values to China (millions)

Top 10	Jan - Jun 2021	Jan - Jun 2020
Soybeans	\$3,566	\$1,339
Corn	\$3,320	\$61
Course Grains	\$1,160	\$471
Pork & Pork Products	\$1,086	\$1,362
Forest Products	1,012	815
Cotton	\$854	\$643
Beef & Beef Products	\$623	\$54
Wheat	\$458	\$136
Poultry Meat & Prods (exclude eggs)	\$396	\$306
Dairy Products	\$353	\$242



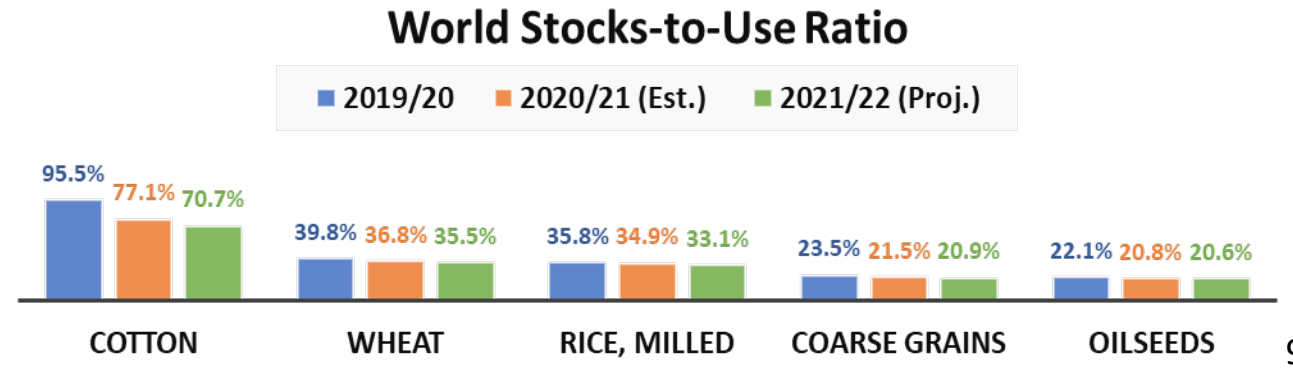
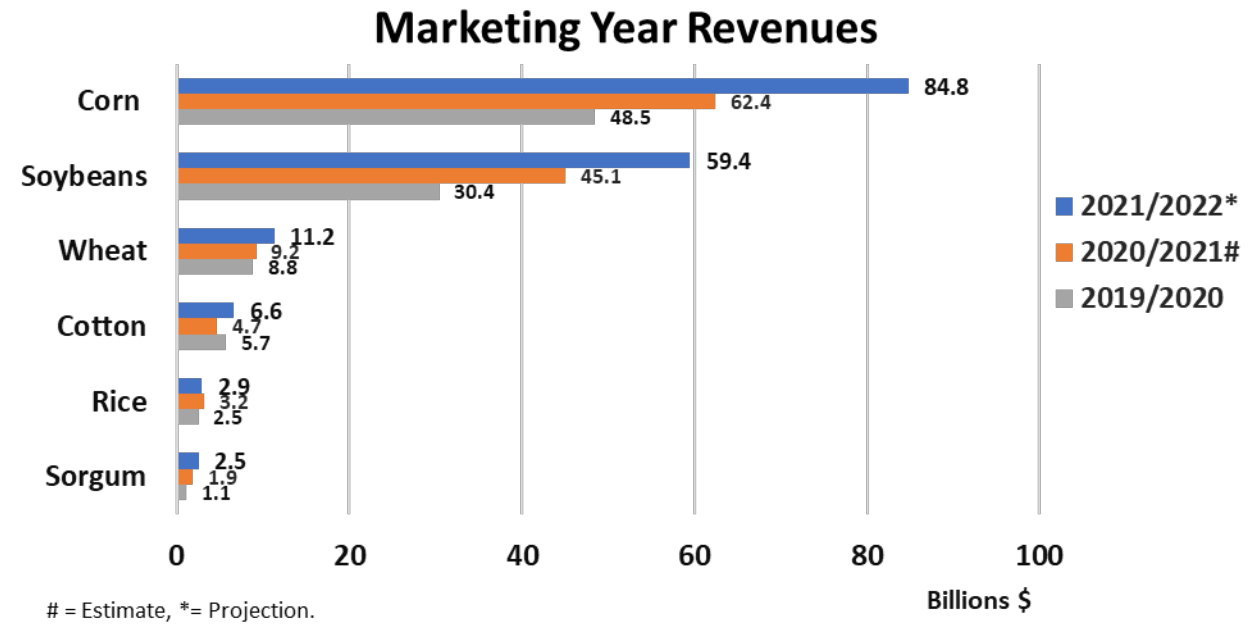
Key grain and oilseed revenues soar

- Projected 2021/22 corn and soybean revenues to rise \$55 billion over 2019/20
- Strong export and domestic demand and limited supplies should keep prices elevated
- Tight supplies forecasted



U.S. 2021/2022 Ending Stocks-to-Total Use	
Commodity	Ratio
Soybeans	3.5%
Feed grains	8.6%
Rice	15.4%
Cotton	17.1%
Wheat	30.5%

Data source: USDA/WASDE, August 12, 2021.



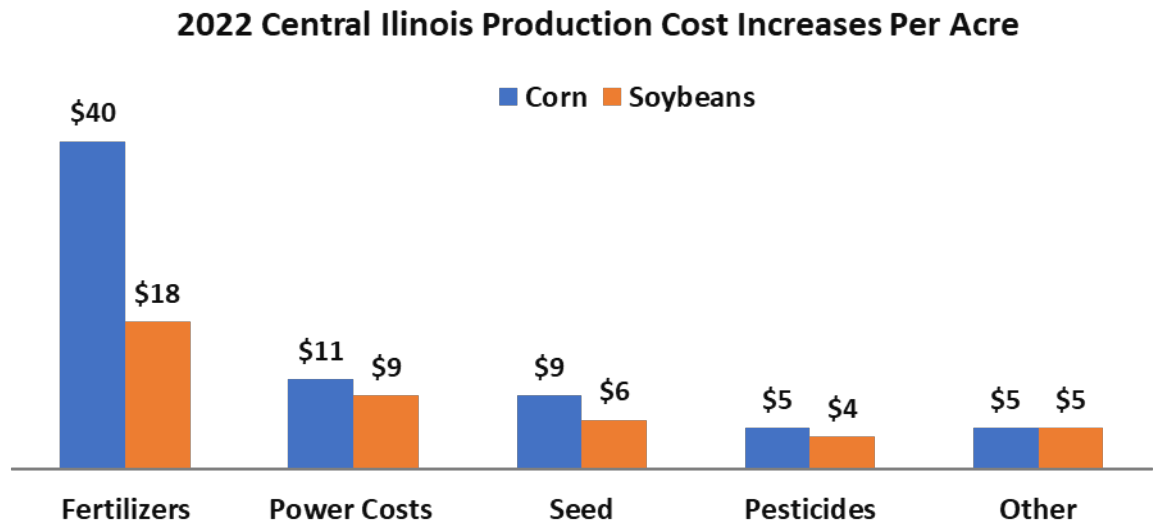
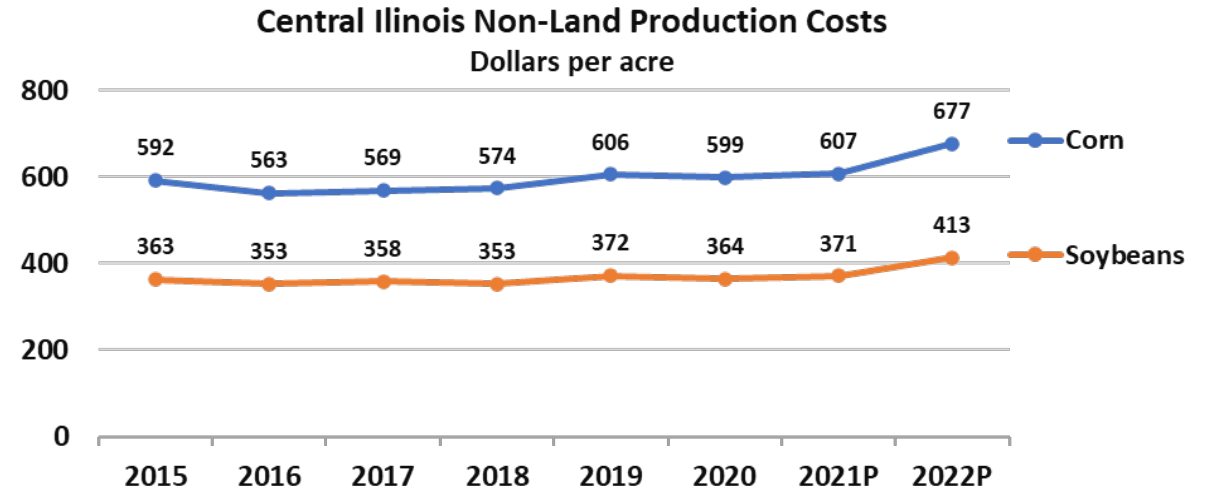


Higher costs to erode crop revenue gains



- Illinois input costs forecasted to rise sharply in 2022
- Higher fertilizer expenses to be the biggest cost driver
- Land costs (rental costs) should also rise significantly
- Any lowering of revenues would translate into thinner margins for next year's crop

Source: University of Illinois.





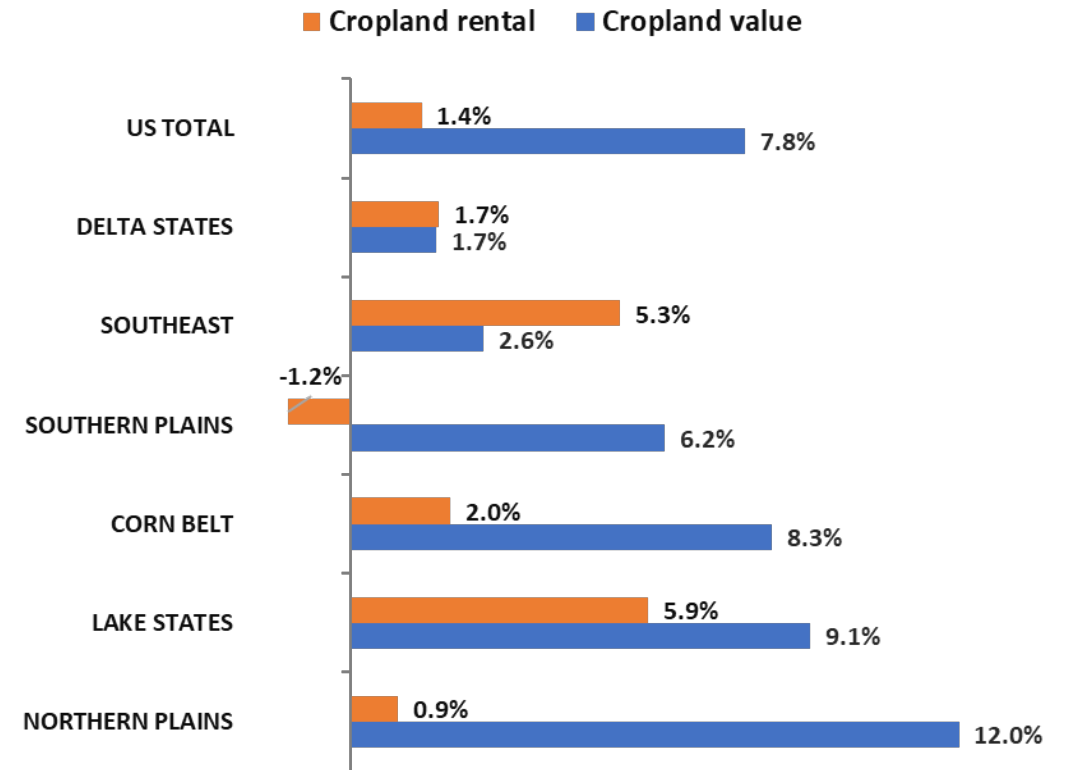
Stronger crop revenues fires up land markets

- Cropland: \$4,420 per acre up 7.8%
- Pastureland: \$1,480 per acre up 5.7%
- Rental rate increases lag land value increases
- Midwest banker surveys and others suggest stronger price increases

Year-over-year changes in the second quarter of 2021				
Federal Reserve District Survey	Cropland Value*	Cropland Rental Rates*	Ranch Pastureland Value	Pasture Rental Rates
Annual Percent				
Chicago	14	-	-	-
Kansas City	11	7	11	1
Minneapolis	16	9	13	6
*Nonirrigated				

Data sources: District Federal Reserve Banks and USDA.

Annual Changes in USDA's June Land Survey for Major Crop Regions





Land markets reflect financial conditions

➤ Land market drivers

- Higher crop revenues
- Large government payments
- Negative real borrowing rates
- Inflation fears and nonfarmer interest
- Limited supply of land on the market
- Stronger farm financial footing

➤ Farm Financial Indicators

- Land prices push farm assets higher
- Strong farm income
- Improving credit quality
- Rising farm debt





Drought damage piles up

Estimated Production cuts vs. 2020

➤ Northern Plains

- Spring wheat – 41%
- Durum wheat – 50%
- Montana barley – 54%
- North Dakota dry edible beans – 46%
- South Dakota alfalfa hay – 50%

➤ Western States

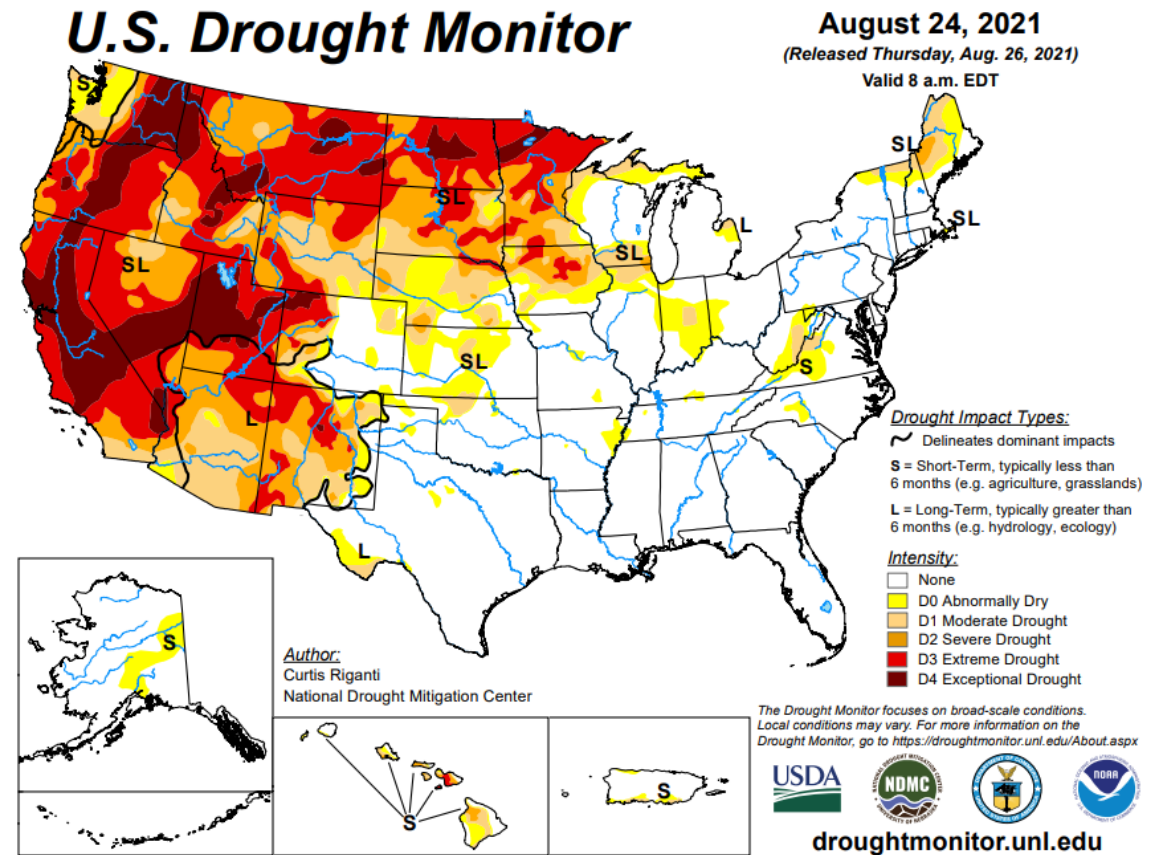
- Washington winter wheat – 44%
- Washington pears – 20%
- California almonds – 10%

➤ Pasture rated “Poor to Very Poor”

- 10 states > than 60% on 8/23/21

WY, UT, SD, ND, NV, MN, MT, WA, OR, ID

Source: USDA.



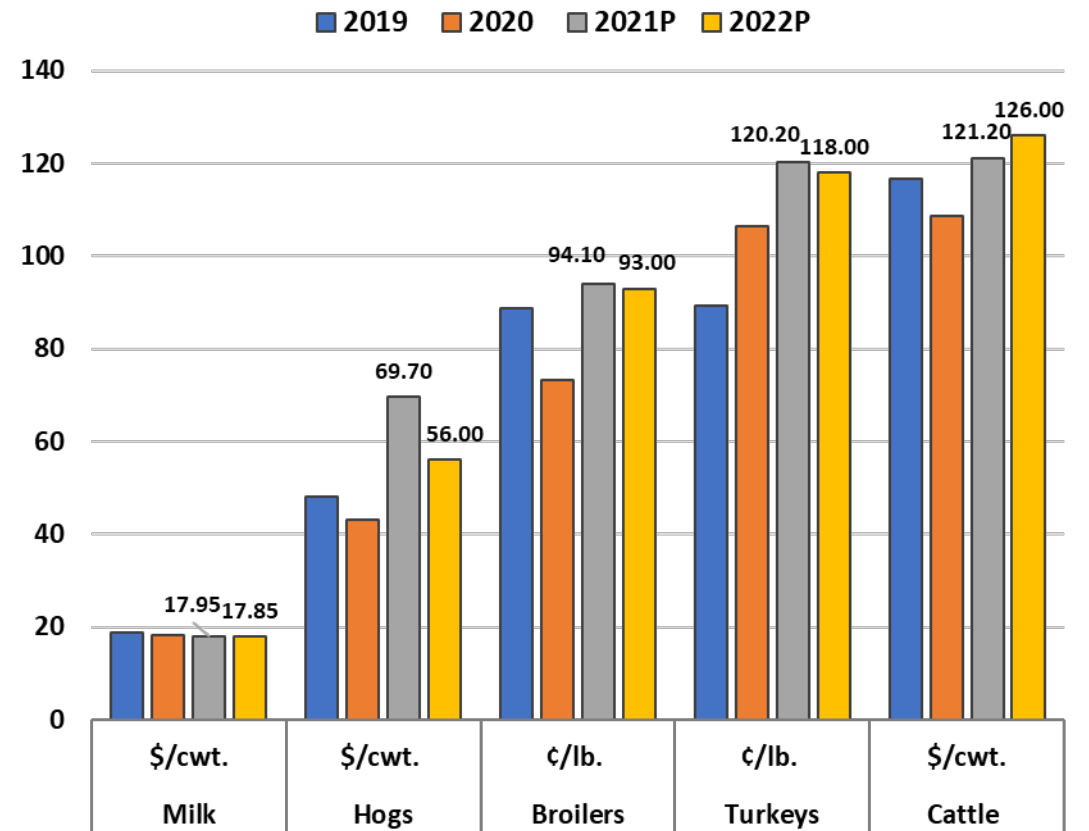


Outlook for proteins



- USDA's 2022 forecast calls for modest increases in cattle prices but lower hog prices
- With exception of milk, prices are forecast to be above 2019 or 2020 levels
- Except for dairy, near-term producer margins are generally favorable
- Higher production costs are likely to erode 2022 gains

USDA Price Outlook



Data source: USDA/WASDE August 2021.



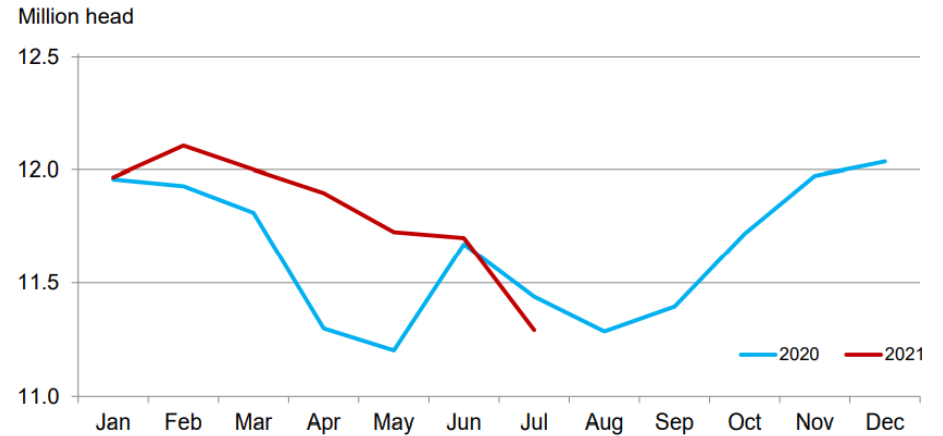
Improving cattle outlook

- Cattle numbers are declining, aided by herd liquidations from drought
- Tighter cattle supplies and robust consumer demand lift packer bids
- Retail beef prices are approaching new highs, making pork and chicken more attractively priced
- Feedlot profitability is being hampered by higher feeder cattle costs and higher feed costs



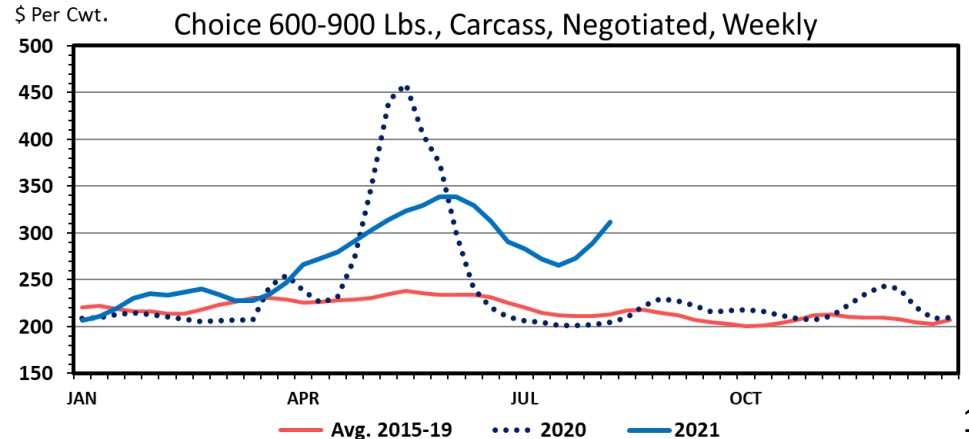
Source: USDA & Livestock Marketing Information Center.

Cattle on Feed Inventory on 1,000+ Capacity Feedlots – United States



Source: USDA.

BOXED BEEF CUTOUT VALUE



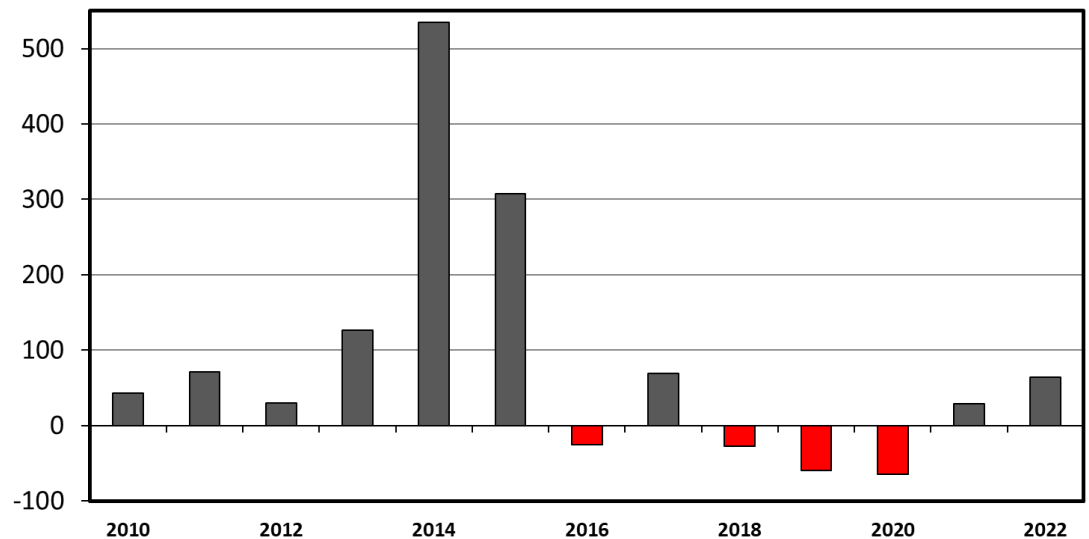


Higher returns predicated for cow-calf producers

- 1/3 of total cattle inventory is in drought areas – West and Northern Plains
- Poor pastures and high hay costs in those regions to accelerate cow slaughter rates
- Higher cow-calf returns are predicated on higher calf prices due to the constraints on supply resulting from herd liquidations
- This cattle cycle could generate calf prices that outpace those in 2015 if the liquidation continues at the current pace



ESTIMATED AVERAGE COW CALF RETURNS
Returns Over Cash Cost (Includes Pasture Rent), Annual



Source: USDA & Livestock Marketing Information Center.

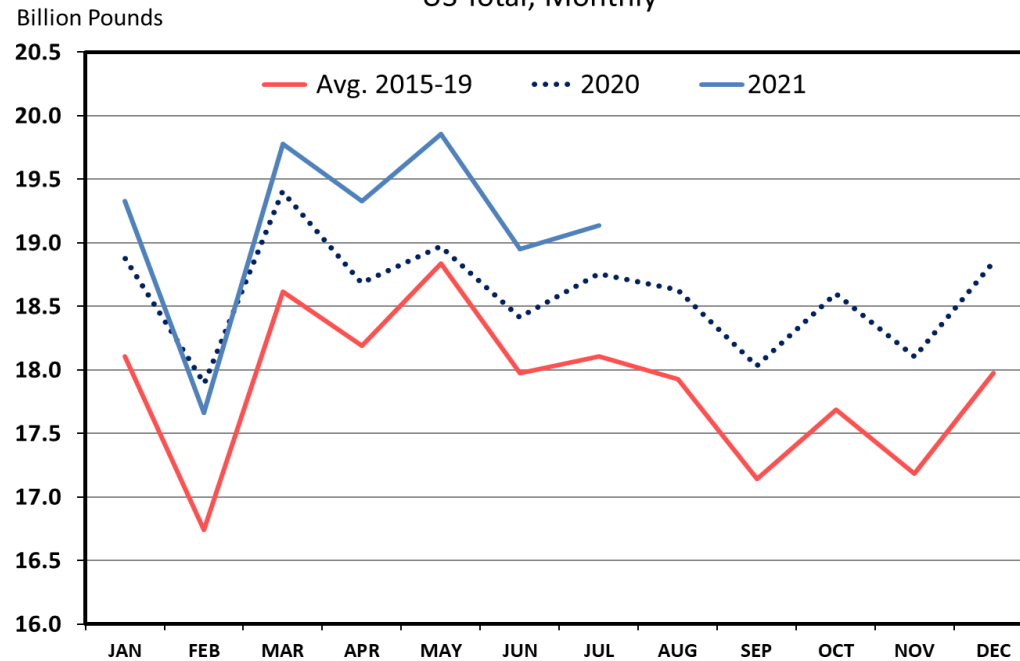


Dairy production pressures margins

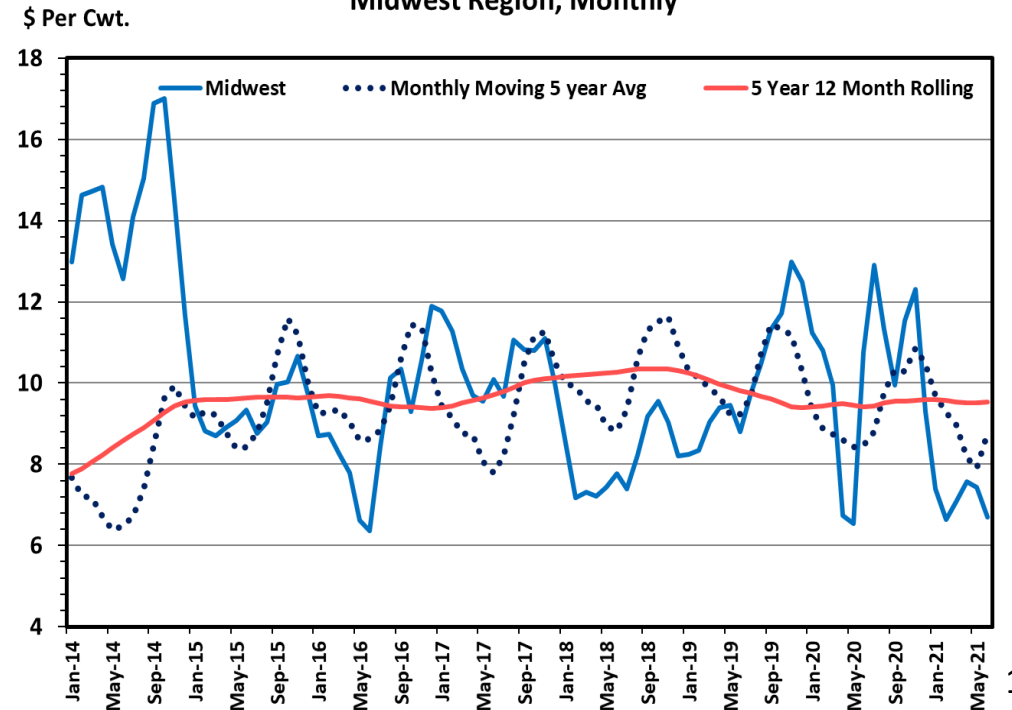
- Production increased 2% in July relative to last year with a 1.3% herd expansion
- Dairies face limited margins due to flat pricing and higher feed costs
- While exports have been healthy, domestic demand remains unsettled
- USDA announced \$350M in new pandemic assistance payments to dairy farmers



MILK PRODUCTION US Total, Monthly



DAIRY INCOME OVER FEED COSTS Midwest Region, Monthly

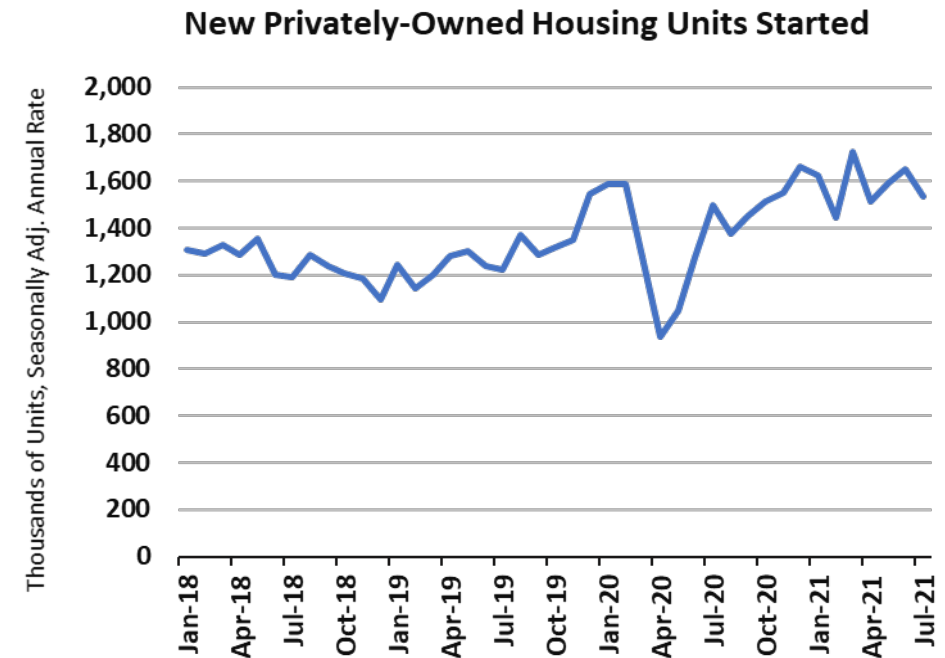
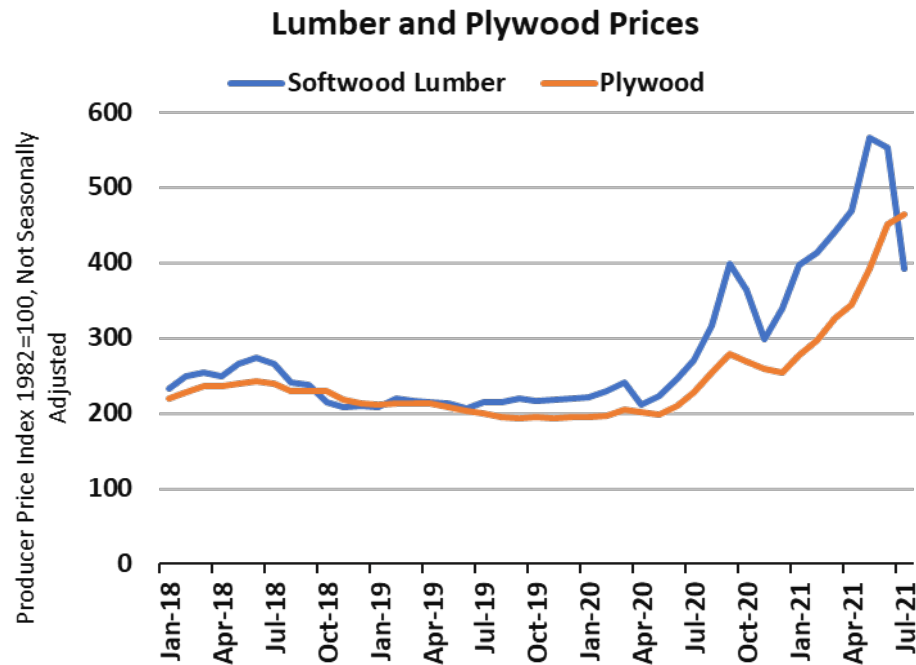


Source: USDA-AMS & USDA-NASS. Livestock Marketing Information Center.



Historic lumber price run-up ends

- Lumber and wood product prices set records this spring, but have since fallen back
- Softwood timber did not experience the large price rise
- Housing starts stall on affordability problems and building material shortages
- Supply catching up as exceptional demand wanes



Source: Federal Reserve Bank of St. Louis.



Concluding comments

- Robust near-term U.S. economy
- Future inflation rates and central bank responses remain critical
- Strong U.S. farm economy with certain commodities and regions (drought) facing challenges
- Exports, particularly to China are key
- Fall harvests are underway





Questions





Farm Credit System Condition and Performance

as of
June 30, 2021

Hal Johnson
Sr. Financial Analyst
Office of Examination



Topics

- ▶ System growth
- ▶ Portfolio credit quality
- ▶ Earnings
- ▶ Capital | Liquidity
- ▶ FIRS

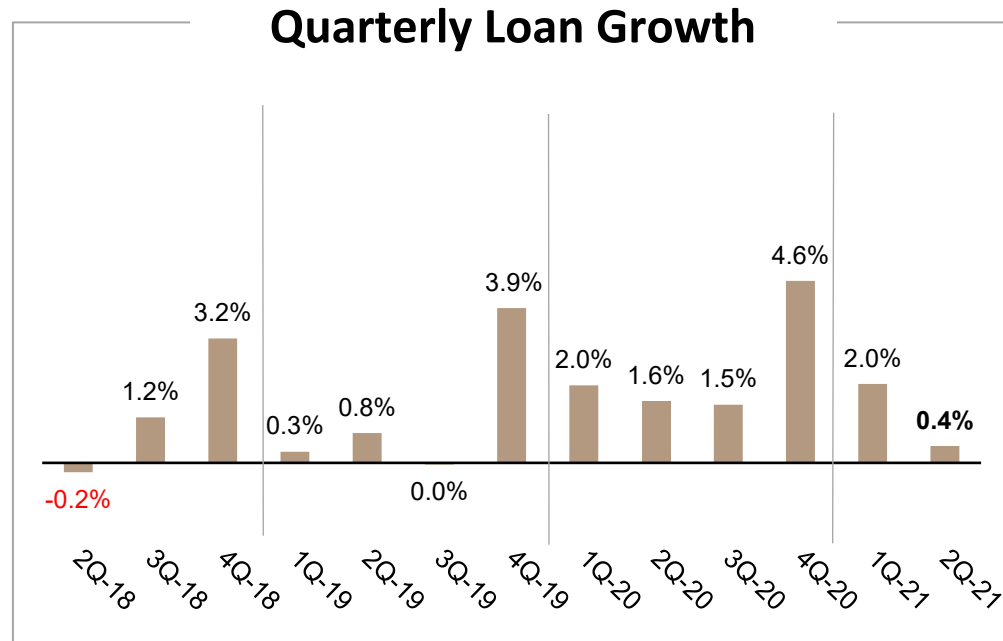




Real estate mortgage lending drives System growth in the first half of the year



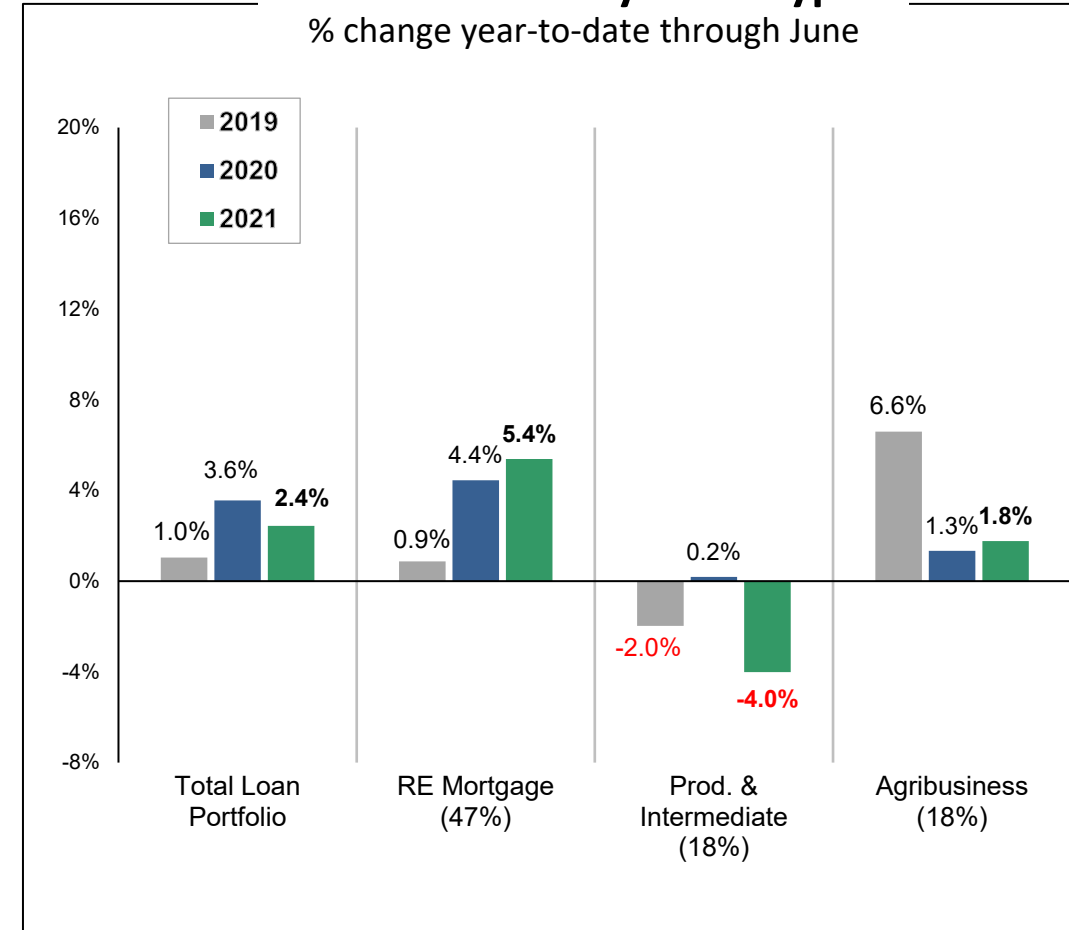
Total Assets 6/30/21	\$407.8	+0.9% Qtr	Gross Loans 6/30/21	\$323.2	+0.4% Qtr
	billion	+1.8% YTD		billion	+2.4% YTD
		+6.0% 12M			+8.8% 12M



Source: FCS Information Statements

Loan Growth by Loan Type

% change year-to-date through June

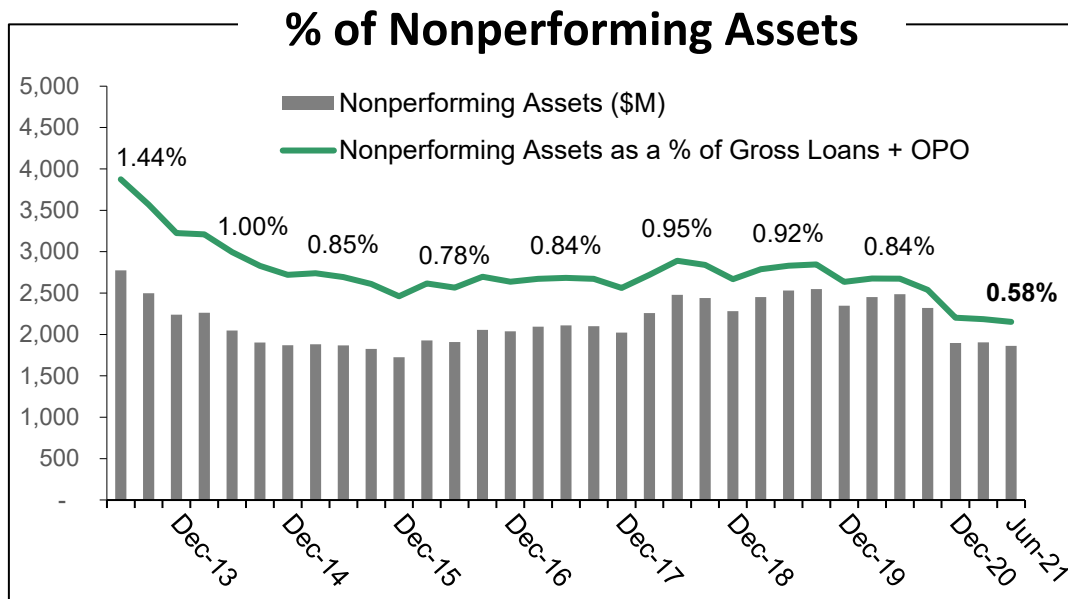
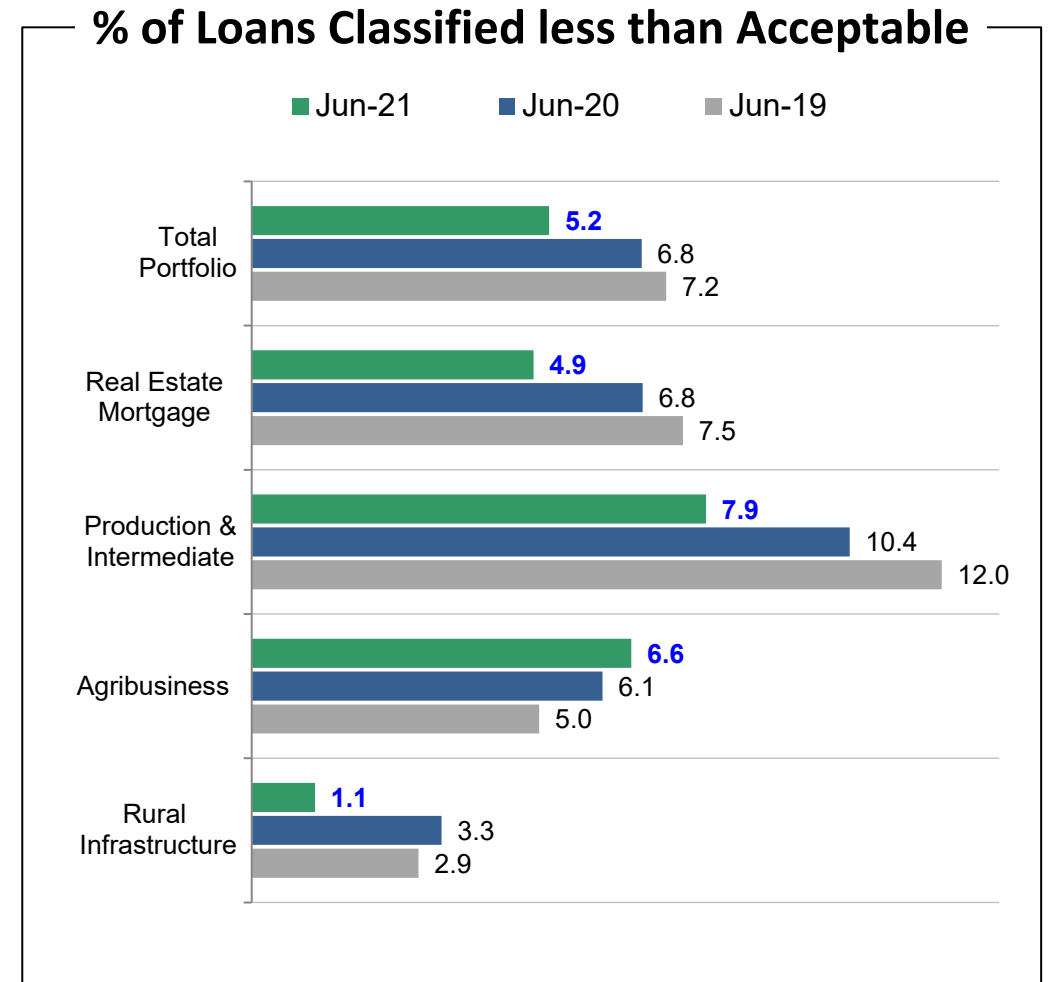




Portfolio loan quality is very good; credit risk elevated for certain agricultural sectors

Nonperforming Assets (6/30/21)	\$1.861 billion	Qtr chg. -\$44M or -2.3%
		12 month chg. -\$626M or -33.6%
Delinquencies ⁽¹⁾ (6/30/21)	0.24%	Q4 '20 0.28%
		Q2 '20 0.37%

(1) accruing loans 30 days or more past due as a % of accruing loans



Source: FCS Information Statements

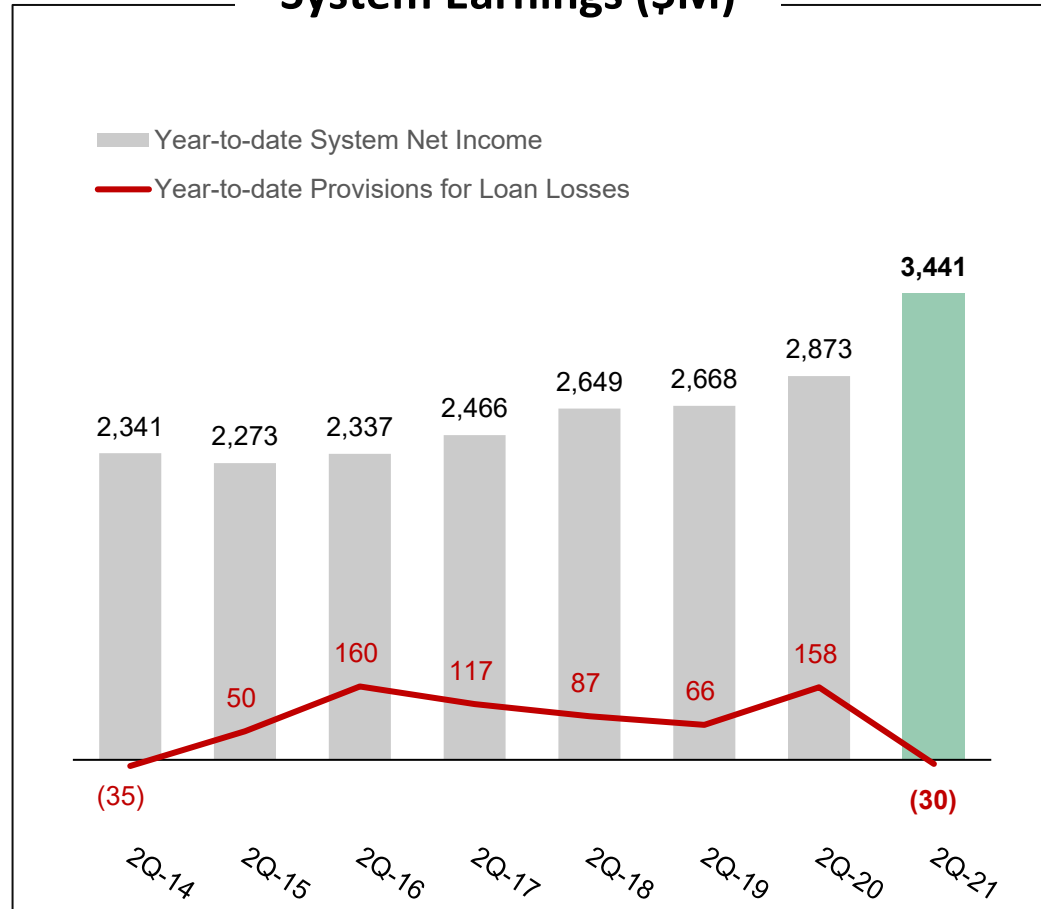




System is financially sound; reports strong year-over-year earnings growth



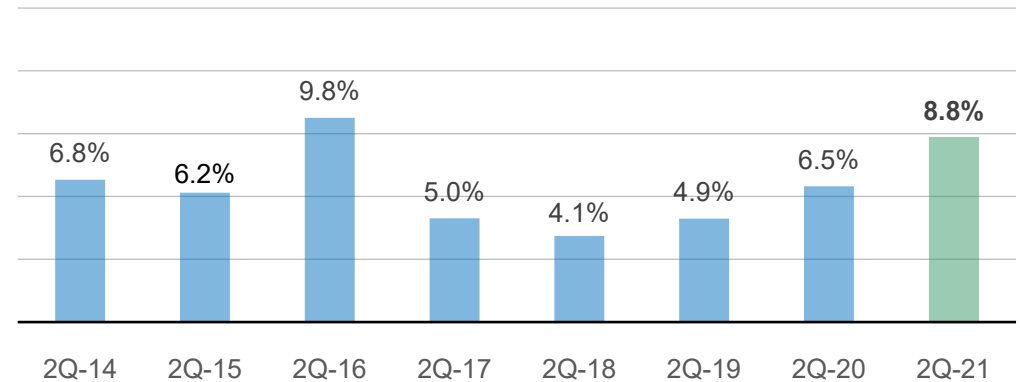
System Earnings (\$M)



Source: FCS Information Statements

	Jun '19	Jun '20	Jun '21
Net Interest Spread (YTD annualized)	2.00%	2.21%	2.33%
Net Interest Margin (YTD annualized)	2.40%	2.44%	2.46%

% increase in Average Earning Assets⁽¹⁾ (compared to the same period a year ago)



(1) year-to-date annualized



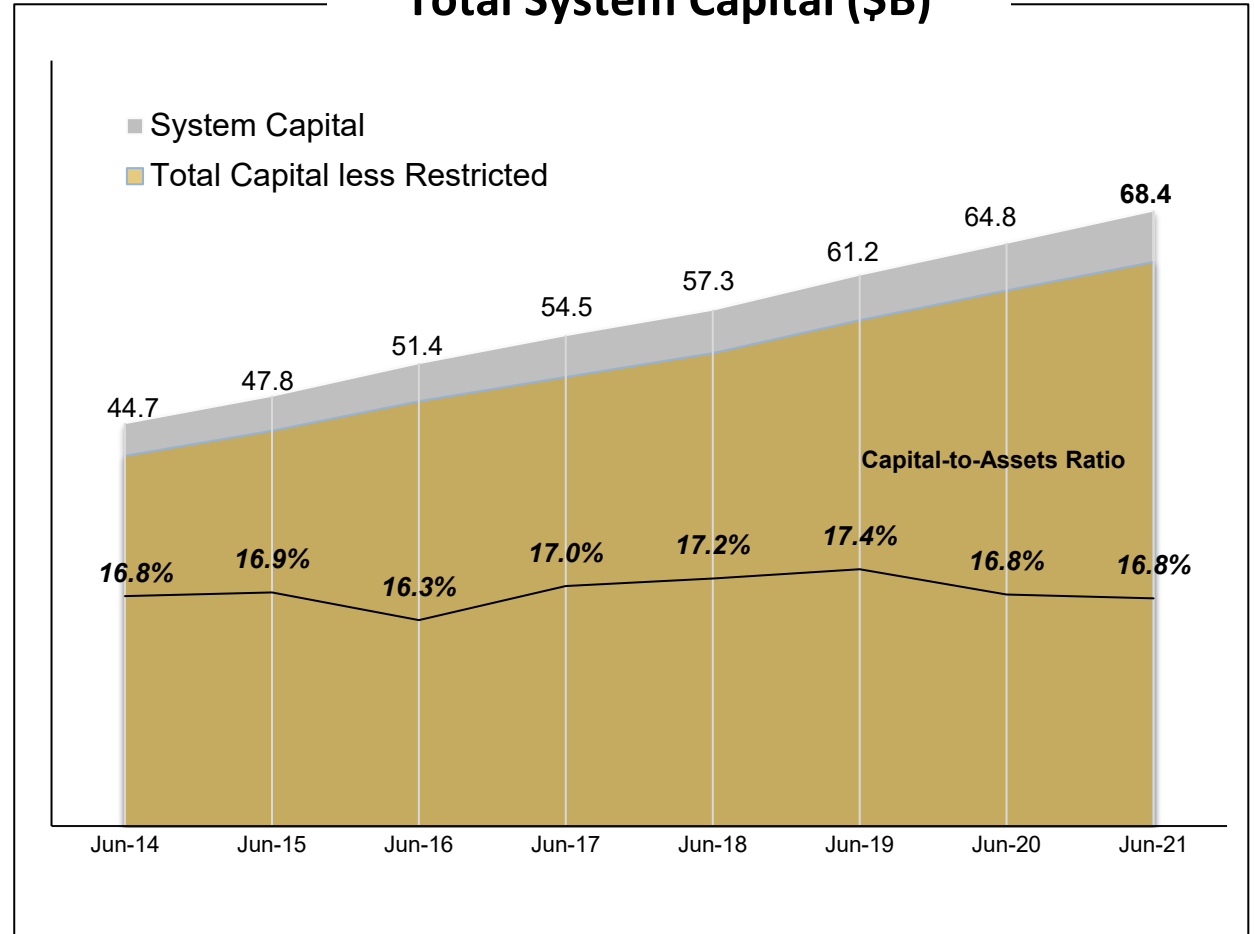
System is strongly capitalized; well-positioned for the current risk environment

Capital and Liquidity (as of June 30, 2021)

- ▶ Total Regulatory Capital:
Banks | 14.7% to 18.5%
Associations | 11.5% to 35.2%
- ▶ Days of liquidity for the four funding banks ranged from 165 to 223 days
- ▶ Capital and the allowance for loan losses as a % of loans outstanding ranged from 18.2% to 23.2% at a combined district level

Source: FCS Information Statements

Total System Capital (\$B)



Note: Restricted capital represents capital associated with the Insurance Fund.



System FIRS ratings

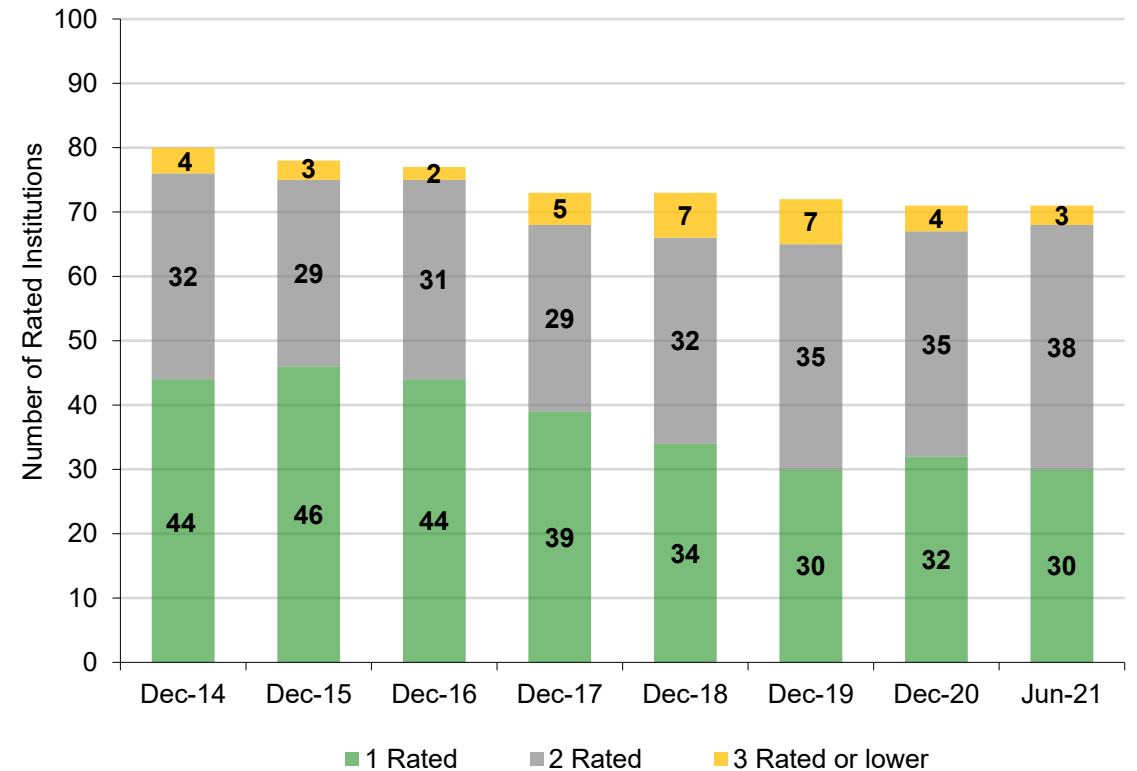
FIRS Ratings

(based on 6/30/21 financial reporting)

- ▶ Composite FIRS ratings were largely unchanged in the 2nd quarter
- ▶ Over 95% of System banks and associations have a Composite FIRS rating of 1 or 2
- ▶ Institutions rated 3 or lower hold less than 1.0% of System assets



Composite FIRS Ratings Farm Credit System Banks and Associations



Source: FCA's FIRS ratings database



Summary and final points



- ▶ U.S. economic activity ramps-up, inflation worries remain
- ▶ Soaring grain and oilseed revenues push farmland prices higher
- ▶ Revenues for much of the livestock sector are expected to improve next year, but higher production costs could erode gains
- ▶ All eyes focused on continuing drought and weather in the West
- ▶ The Farm Credit System continues to be safe and financially sound. Portfolio loan quality is strong, but credit risk is elevated for certain sectors and geographic regions
- ▶ System institutions are strongly capitalized and well-positioned to meet borrower funding and liquidity needs



Questions



THANK YOU