Comments of Cecil Gibson
on behalf of National Livestock Credit Corporation
to the
Farm Credit Administration
Public Forum on OFI Lending
Des Moines, Iowa
August 3, 2001

Mr. Chairman and other distinguished members of the FCA Board and staff, my name is Cecil Gibson. I am from Byars, Oklahoma, and am recently retired as the president and chief executive officer of the National Livestock Credit Corporation located in Oklahoma City, Oklahoma.

The organization for which I worked for 40 years had, and still does have, a longstanding OFI borrowing relationship with the Farm Credit Bank of Wichita, Kansas. This lending relationship spans over 68 years (since 1932), and as CEO, I was the OFI's primary contact with the Farm Credit Bank of Wichita for the majority of that time.

I understand from your published information that your primary objective today is to evaluate the Farm Credit Administration's regulations as they pertain to access that organizations like National Livestock have to Farm Credit System funds. I appreciate this opportunity to address you today and have some thoughts about how improvements could be made.

First however, I want to say that as an individual with first-hand knowledge of one such relationship, I must compliment the Farm Credit Bank of Wichita for the way in which they handled our business with them. They were always open and fair in their dealings and treated both myself and the OFI with respect and courtesy. Furthermore, I always felt that our OFI had full access to funding provided for in regulation and that our funds were competitively priced.

The System Bank I dealt with enjoys a good relationship with a handful of other similar OFIs. While the number was much larger a couple of decades ago, difficult times in agriculture, fewer farmers and probably a lack of interest by some lenders in working with a System that some may view as a competitor, has caused the number of OFIs to drop quite a bit over time.

That said, I know there is a lot of interest around the country in how the regulations governing access for OFIs could be improved. I have reviewed the current OFI regulations as cited in your announcement notice for the forum today, and I have a few points I would ask you to consider if you make changes to these regulations.

At one time, there was a significant capital investment required to open a new OFI lending relationship with a Farm Credit Bank. Many years ago, stock requirements may have exceeded 10% of the loan amount in some cases. Through cost containment and solid earnings performance, the Wichita Bank has been able to reduce their stock requirement for OFIs. The Bank's bylaws now set that requirement at only $1,000. This is hardly a "barrier to entry" for a modern lending institution. I can only infer from these facts that the Farm Credit Bank's philosophy is to build any needed capital through earnings, rather than some sort of stock investment. This approach seems fair, and always kept the effective rate charged to our organization at a competitive market rate. In fact, we always felt our borrowing relationship had excellent value.

This takes me to another part of the regulation. Given this minimum investment and the fact that OFIs usually do not require stock from their retail customers, it would also seem logical that Farm Credit borrower rights should not apply to OFIs. This seems to be an unnecessary requirement, and one I feel should be eliminated.

You should be aware that the OFI I led for so many years specializes in short-term loans to livestock producers. Therefore, having access to short-term funds through Farm Credit met our needs then, and continues to do so for the National Livestock OFI today. However, as I review the current OFI regulations, it appears to me that the very detailed, prescriptive approach to lending included in the regulations is seriously outdated. There may have been a time when the FCA had specific reasons to have the regulations address what now appears to be quite procedural. Examples would include the detailed requirements for financing with a certain type of agreement, or prescribing collateral requirements, or even the method for perfection of collateral. But the way business is done today requires more flexibility. To me it would seem that if your objective was to encourage Farm Credit Banks to enter into more OFI relationships, FCA should remove much of the unnecessary language from the current regulations.

As an experienced ag lender, I would have to assume that Farm Credit Banks generally make their lending decisions based on a set of internally developed underwriting standards. I would further assume that these underwriting standards are available for FCA inspection through your normal examination processes. Good underwriting standards would provide protection from safety and soundness concerns, but would be broad enough to allow for some flexibility based on the individual customer's circumstances. In my opinion, if the lending regulations are inflexible and, therefore, burdensome for the Farm Credit Bank, this will eventually restrict access to OFI funding, as there is less incentive to pursue this type of business.

I would recommend that FCA allow OFIs to be financed with all of the modern lending tools available, including syndications, specialized loan facilities, portfolio purchases, purchases of farmer notes, participations and so forth. This is simply the way modern financial transactions take place, allowing both lender and borrower to tailor the financial package to their needs.

Mr. Chairman, one other area of the regulations also seems troublesome to me. It is the requirement for OFIs to do business only with a certain Farm Credit Bank based on the OFI's geographic location. Granted, under the current regulations, if a Farm Credit Bank denies an OFI loan, the OFI can then contact other Farm Credit Banks. However, this requirement prevents the OFI from shopping around to find the best deal available on the front end. In addition, many modern OFIs are spread across several states, and others may have a national or even international presence. This “territorial requirement” appears to be an outdated and unnecessary access issue. In my view, it could be eliminated without incurring any safety and soundness risks. I realize there may be similar territorial issues that are a problem for Farm Credit associations, and I understand your agency has been working to address these issues. I personally believe you should work to eliminate territorial restrictions for all borrowers of the Farm Credit System, including OFIs. Other GSEs don’t have these kinds of access requirements based on geography, so why should access to Farm Credit be unique?

One of the questions posed in your announcement was, “How can we amend our regulations to encourage greater cooperation and partnering between system and non-system lenders?” My response to that would be to let market forces operate with the fewest number of restrictions possible. I don’t believe lenders need special incentives to make loans whenever a profitable market exists for those loans. I also believe that Farm Credit Banks will actively seek to both buy and sell all types of eligible agricultural loans if the free market is allowed to operate without unnecessary restrictions. To correct this may be as simple as the regulation stating that pricing to OFIs should be based on market considerations. It appears to me that the regulations for the financial services industry have advanced much faster than the current Farm Credit regulations. If FCA could remove the unnecessary and outdated regulations, I believe relationships with other financial institutions would work well within the Farm Credit System.

Your announcement also posed an interesting question about how alternative funding arrangements might be developed to better finance rural businesses. In my experience, the problems here have been a somewhat restricted definition of what constitutes an eligible borrower. So many of our small rural businesses support the economic fabric of our rural communities. Yet, in many cases, loans to these businesses are ineligible for financing through Farm Credit. Today, production agriculture may be only one small part of an enterprise that is designed to produce, process and market products. Yet, it seems OFIs can only access Farm Credit funds to finance production activities because of eligibility restrictions, and are limited in their ability to finance the value-added side of the enterprise. Clearly, credit risk is mitigated when you can finance the entire value chain instead of just the production side. It seems a broader definition of eligibility here could help all concerned.

Another area to explore is whether an OFI could also have the option to borrow directly from or have other financial alliances with a Farm Credit association. This may serve a retail customer well under certain circumstances. I question that the only lending relationship described in regulations is with Farm Credit Banks. I believe that groups of associations have formed alliances to fund pools of loans in some cases, and Farm Credit Banks may even be participating in those arrangements. Why shouldn't an OFI be able to work directly with associations as possible funding sources if that works to <u>their</u> customer's advantage?

I want to also mention the important role that I believe organizations like National Livestock play in today's agricultural lending market. We understand that the market for agricultural loans is competitive. That's especially true today with the past 10 years or so being pretty good in terms of net farm income. But, this will not always be so. National Livestock Credit Corporation has a specific mission to serve the livestock industry with specialized products, innovative services and competitive rates. We are extremely proud of our long service to the livestock industry and believe we have every right to be at the bargaining table with the other lenders here today. Our industry offers a unique type of service that is valued by our customers, as evidenced by our strong record of service and growth. We are not in ag lending because it is fashionable or because it offers unusually high returns on invested capital. We are in it to insure that our unique understanding of the market and our generations of lending experience are always there to assist livestock producers everywhere. We intend to continue this commitment going forward and appreciate your agency's attention to OFIs as you evaluate your regulations.

Mr. Chairman, thank you again for this opportunity to address you in this important forum. My experiences in working with the Farm Credit System have always been positive and productive. Even so, there is always room to make improvements, and I appreciate this chance to make my thoughts known.

I would be happy to address any questions you or other members of the FCA Board or staff might have.

Thank you.

Cecil Gibson-Retired President and CEO
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