



Mission-Related Investments Update August 12, 2010

Farm Credit Administration



Agenda

- Introduction
- Legal Framework
- Mission-Related Investments/Investments in Rural America
 - Policy Background
 - Types and Volume Trends
 - Investments in Rural America by Type and Location
 - FCS Feedback
 - Looking Ahead



Legal Framework

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Statutory and Regulatory Authorities

- **Section 15(15) and 3.0 (13)(A) of the Farm Credit Act authorizes System banks to invest in U.S. Government and government guaranteed obligations and other investments authorized by FCA**
- **Section 2.2(10) of the Farm Credit Act authorizes associations to invest their funds as approved by their funding bank under FCA regulations**
- **FCA investment regulations authorize System banks and associations to hold investments primarily for liquidity and risk management purposes**
- **FCA regulation section 615.4140(e) authorizes FCS banks and associations to hold other investments that the FCA approves on a case-by-case basis**



Mission Investments

- **Subparts E and F of part 615 of the FCA regulations permit FCS to make the following types of mission oriented investments:**
 - **Farmer Mac Securities**
 - **Farmers' notes**
 - **USDA guaranteed obligations and certain other governmental obligations benefitting rural areas**
 - **Certain municipal securities, agricultural equipment securities and asset-backed securities**
 - **Other investments approved by the FCA on a case-by-case basis under section 615.5140(e)**



Pilot Investment Programs

- **Since 2005, FCA approved “Investments in Rural America” pilot programs for all System institutions on either a district-wide and/or an institution-specific basis**
- **Programs established with an initial 3-year pilot period; continue until FCA Board acts to modify or terminate the programs**
- **Conditions of Approval designed to ensure:**
 - **Mission focus**
 - **Obligations purchased are structured as investment securities**
 - **Safe and sound investment management through investment portfolio, obligor, and maturity limits**
 - **Investments benefit rural communities and residents**



Legal & Policy Issues

- **Size, nature, and method of rural community-based investing requires appropriate and meaningful investment criteria**
- **Conditions of approval enforce the implied statutory distinction between loans and investments by:**
 - Requiring that securities purchased be structured as investment securities commonly recognized in the debt markets as a vehicle for investment
 - Excluding any transaction more similar to a commercial loan transaction than to a traditional investment transaction
 - Specifically prohibiting FCS from directly making or purchasing loans under the program
- **May 1, 2008 written clarification to FCS provided additional guidance and a general framework for investment decisions**
- **Staff continues to study investments made under pilot programs, including mission focus, economic impact (e.g., jobs created/saved), effectiveness and appropriateness, level of risk, and financial impact**



Mission-Related Investments/ Investments in Rural America

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Policy Basis for Mission-Related Investments

- 1. Agriculture and rural communities are interdependent, as the vitality of rural communities is essential for the prosperity of agriculture**
- 2. Congress recognized in the preamble and the Policy and Objectives in section 1.1 of the Act that the System's mission is to provide a flexible flow of money to agriculture and rural areas**
- 3. Rural communities provide the needed infrastructure and supply systems that allow agricultural producers to thrive**
- 4. Farmers and ranchers depend on the off-farm income generated from jobs created and located in rural communities**



Need For Investing in Rural Communities

- **Greater public and private investment in rural communities is needed to abate:**
 - Persistent weak economic conditions in rural areas
 - Lack of sufficient funding and credit availability for critical infrastructure and facilities which are needed to create jobs, sustain economic growth and retain youth and talent
 - Rural funding gaps caused by higher risks and lower returns
 - State and Federal budget constraints
- **Rural communities face a number of obstacles in raising funds:**
 - Inability or inconsistency of lenders to provide reasonable cost funding for costly essential infrastructure and community facilities
 - Limited secondary market for certain segments of rural lending (e.g., business, infrastructure, low-moderate income housing)
 - Cost of credit enhancement and obtaining credit ratings limits use of tax exempt bonds and access to capital markets
 - Limited availability of equity or “start-up” capital



Mission-Related Investments

Investment Type	Total Volume 3/31/10*	Total Volume 12/31/09*	Total Volume 12/31/08*	Annual Change	Annual Percent Change
Investments made under prior-approval authorities					
Rural Housing Mortgage-Backed Securities	\$1,162,301	\$1,242,526	\$1,552,005	(\$309,479)	-19.9%
Rural Development Debt Securities**	631,757	635,195	477,445	157,750	33.0%
Credit-Linked Agricultural Notes	11,733	12,261	13,951	(1,690)	-12.1%
Equity Investments	5,274	4,708	2,992	1,716	57.3%
Subtotal	\$1,811,065	\$1,894,690	\$2,046,393	(\$151,703)	-7.4%
Investments made under other regulatory authorities					
Farmer Mac	1,433,330	1,267,409	1,461,320	(193,911)	-13.3%
Tobacco Buyout	548,239	695,503	771,586	(76,083)	-9.9%
USDA Guaranteed Paper***	888,543	799,092	647,436	151,656	23.4%
Farmers' Notes	12,843	12,601	16,392	(3,791)	-23.1%
Subtotal	\$2,882,956	\$2,774,605	\$2,896,734	(\$122,129)	-4.2%
Total all mission investments	\$4,694,021	\$4,454,447	\$4,943,127	(\$273,833)	-5.5%

* Amounts in Thousands

** Includes Agribusiness

*** Estimated Secondary Market Purchases



Investments in Rural America

Objectives by Asset Class

Rural Housing Mortgage Securities

- Improve the liquidity in the rural home financial markets to reduce rural home ownership costs

Agribusiness Investments

- Help agribusinesses obtain access to debt markets through collaboration with commercial banks and secondary market purchases

Credit Linked Agricultural Notes

- Support agricultural lenders through purchase of notes linked to pools of long-term agricultural real estate loans

Equity Investments

- Support starter farmer and cooperative programs and rural entrepreneurs with seed capital

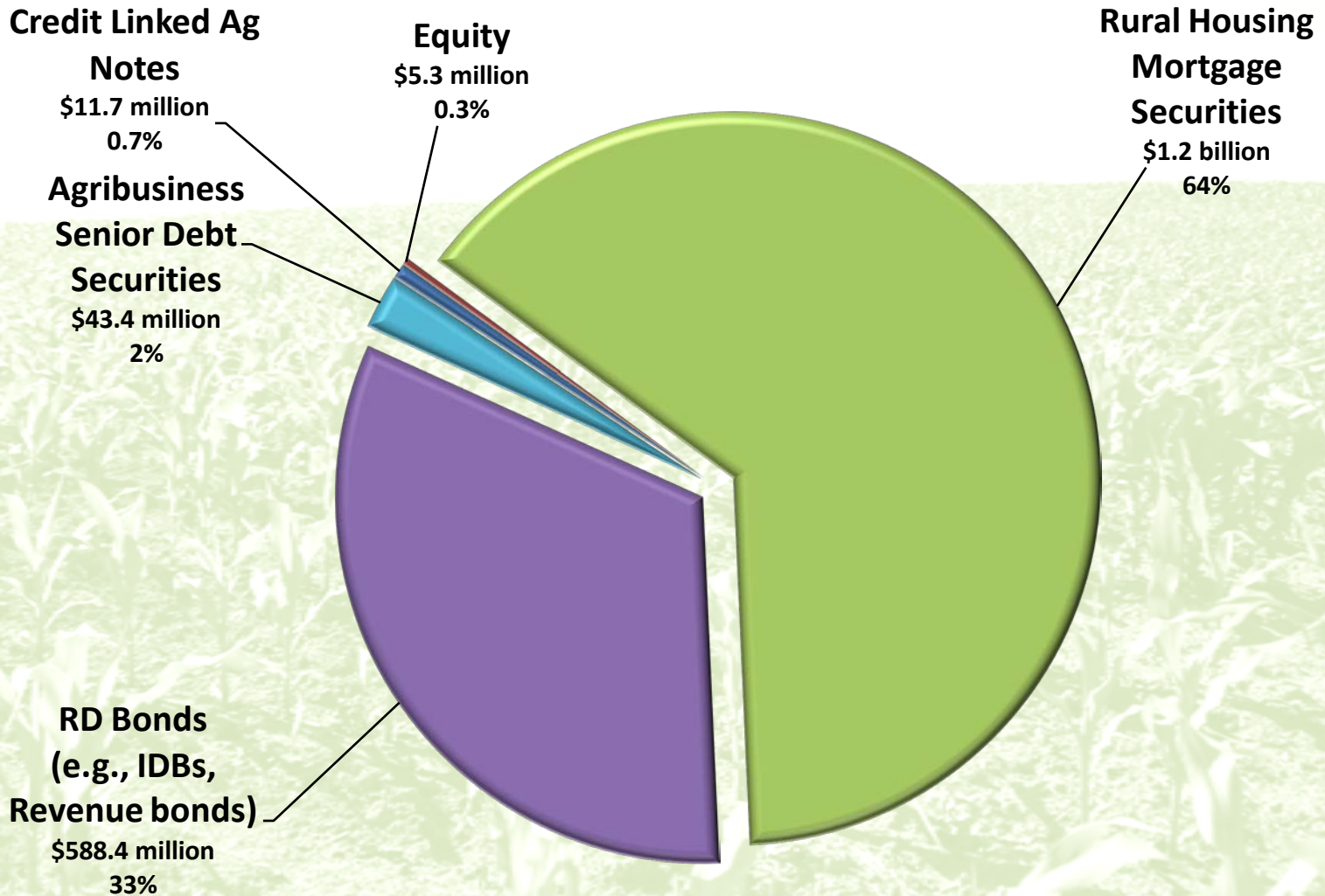
Rural Development Bonds

- Provide flexible flow of funds to rural America for rural development and infrastructure projects



Investments in Rural America by Asset Class

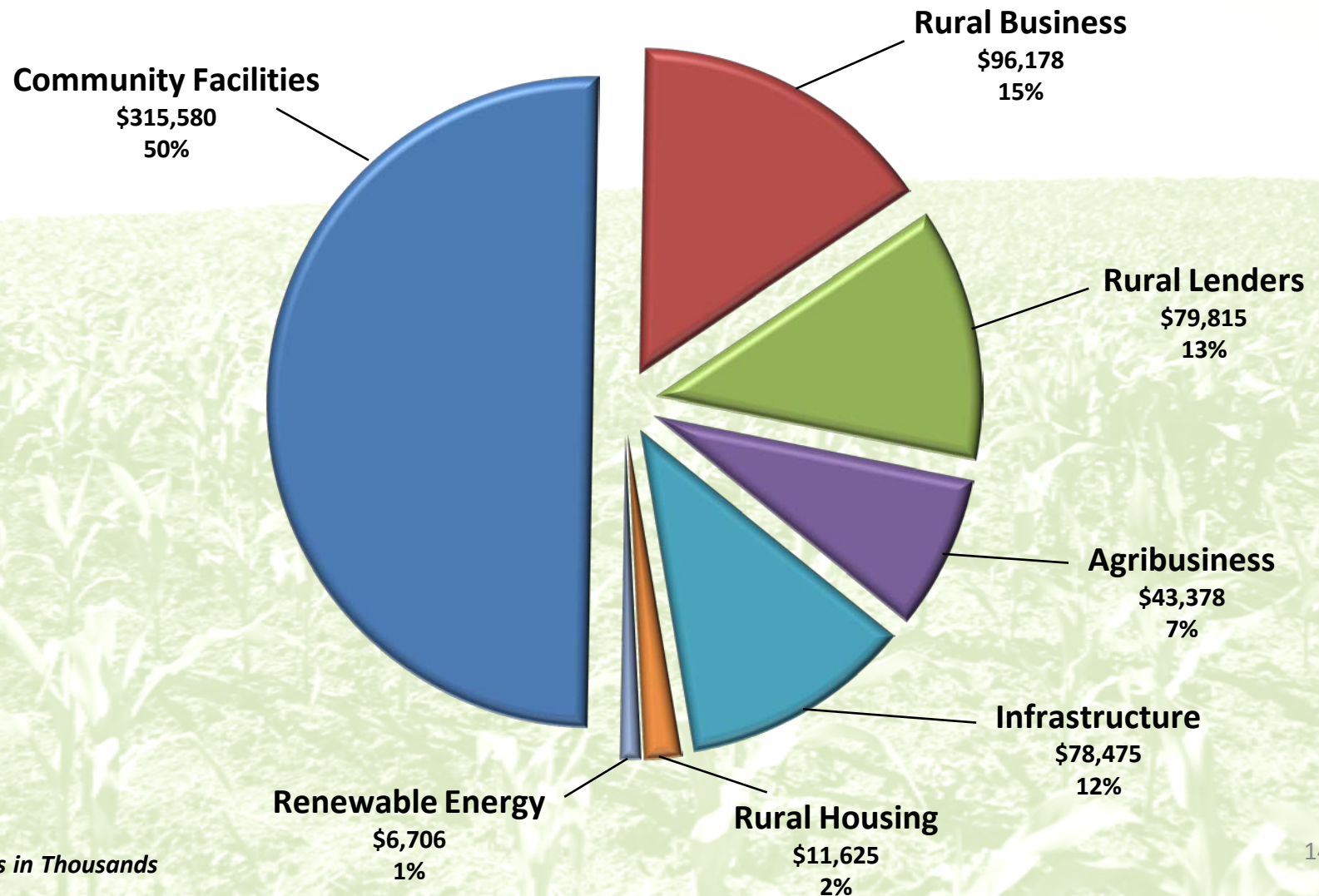
Total \$1.8 billion





Rural Development Investments by Purpose

Total \$631.8 million

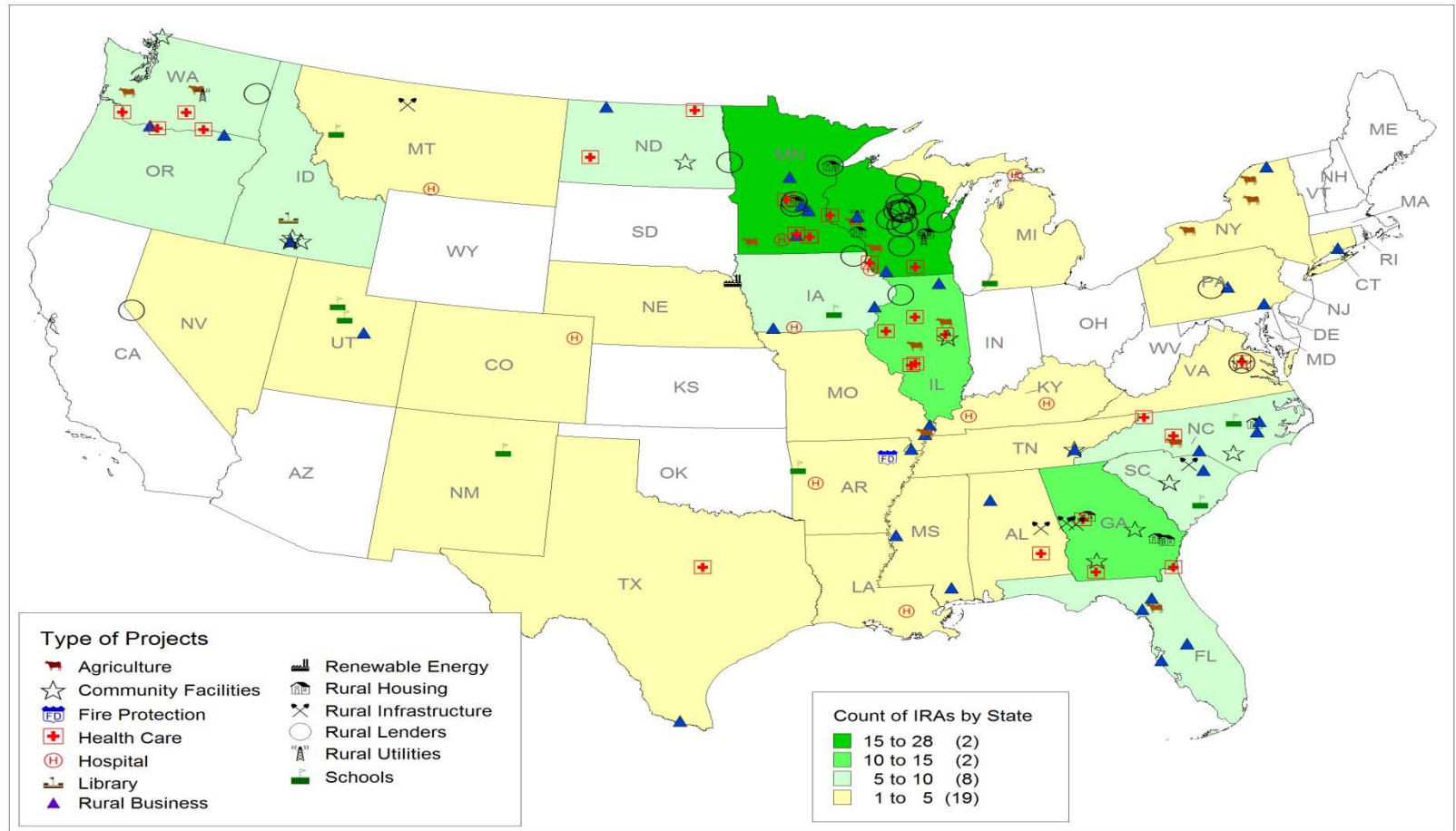


* Amounts in Thousands



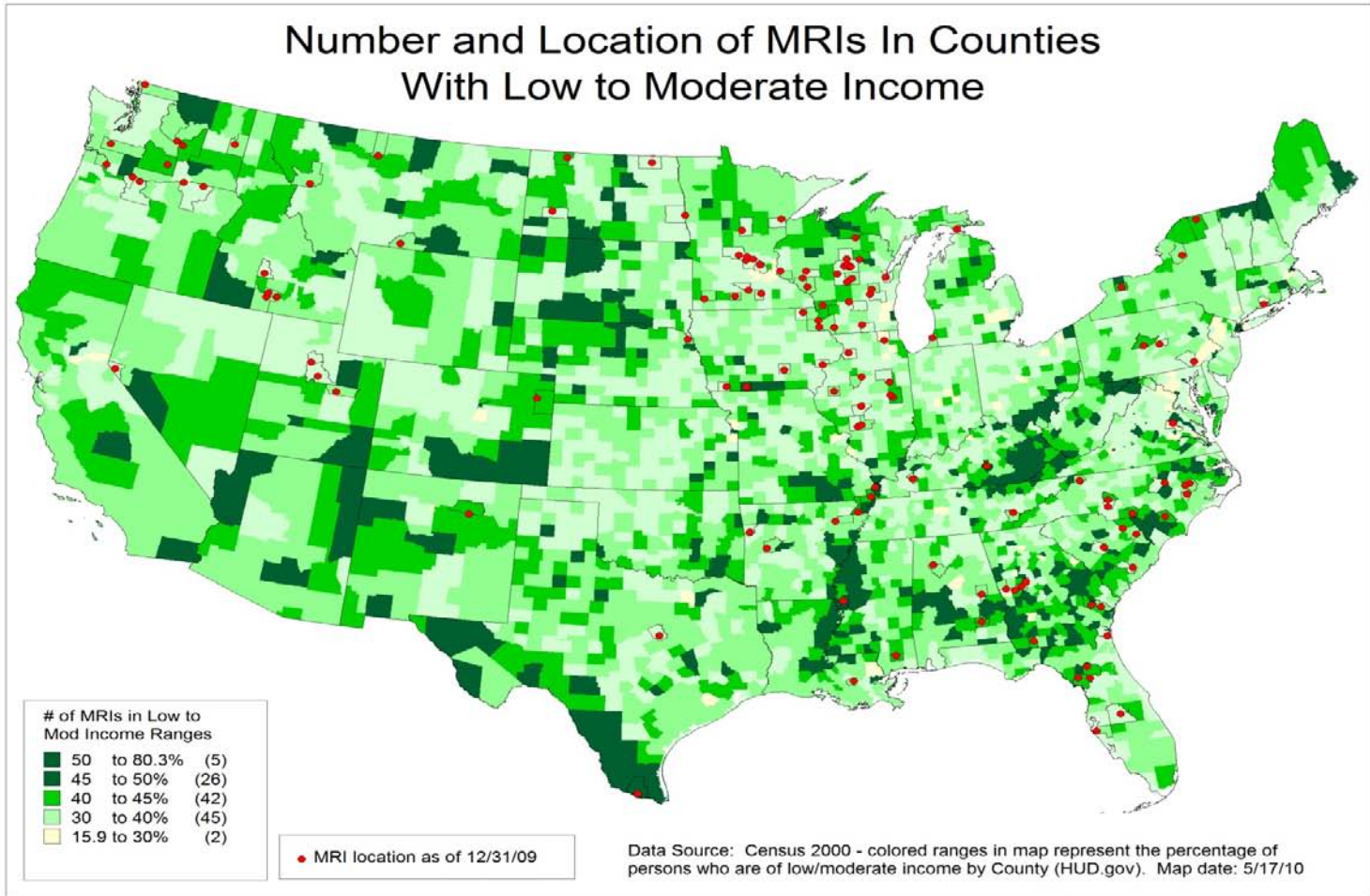
Location of Rural Development Investments

FCS Investments in Rural America as of 3/31/2010





Investments by County Income Level





Rural Development Debt Securities

Community Facilities

- 59 projects totaling \$315.6 million
- Investments support essential community facilities development (e.g., construction/expansion and modernization) and permanent financing including:
 - Critical access hospitals, assisted living centers, disabled/disadvantaged citizens facilities and medical/health facilities
 - Schools, libraries, childcare facilities, youth shelters/camps and public fairground facilities
 - Fire and rescue stations, police stations, community centers, and public buildings
- Often sponsored by local governments and non-profits to provide cost effective essential human services
- Targeted investments in essential community facilities that advance the quality of life in rural communities



Rural Development Debt Securities

Rural Lenders

- 26 investment relationships with commercial banks totaling \$79.8 million
- Investments in obligations issued by rural lenders that are secured by the issuer's qualifying collateral (e.g., interests in one or more rural business or rural development loans)
- Commercial bank involvement in projects
 - construction financing, credit enhancement for portion of public issuance, operating financing, trustee services, and other bank services
- Benefits of rural lender partnerships—Rural communities obtain greater access to longer term funds and increase capacity to finance larger rural development projects



Rural Development Debt Securities

Rural Business

- 34 investments totaling \$96.2 million
- Key objective is to support businesses that create and retain jobs in rural areas
- Focus on manufacturing products in rural areas or providing services to rural residents rather than service to broad market of both urban and rural areas
- Often sponsored by economic development authorities, which help coordinate community priorities and rural interests
- Recently, we have seen investments coupled with SBA guarantees provided under the American Reinvestment and Recovery Act (ARRA)



Rural Development Debt Securities

Rural Infrastructure

- Investments in 8 projects totaling \$78.5 million
- This segment supports projects that fund water, waste, utilities, transportation, and rural infrastructure projects in rural areas
- Examples include hydroelectric, water and sewer, and securities issued by economic development authorities on behalf of a government entity in support of rural economies
- Community impact – Investments helped preserve and create jobs and supported local inputs and provided communities with a key source of scarce financing during current economic downturn



FCS Feedback

- **Pilot Program Attributes**

- Positive impact on rural communities and quality of life of rural residents (e.g., healthcare, schools, housing and high-speed internet)
- Earnings and portfolio diversification
- Provides an opportunity to build image as positive corporate citizens in rural areas
- Provides rural areas with a “patient” and “affordable” source of capital
- Improves infrastructure necessary for agricultural businesses to thrive
- Opportunities to seek out new partners and manage risk
- Rewarding and interesting



FCS Feedback (cont.)

- **Pilot Program Challenges**

- Too complex and timely to develop necessary partners with other (local governments, USDA, EDAs, etc..) to make it successful
- Other financial and credit related issues soften interest
- For some FCS institutions, hard to find viable investments that meet program mission objectives
- For others, investment opportunities exceed available capital
- Uncertainty surrounding the pilot program and how long it will continue



Investing in Rural America

- Capital and time intensive
- Requires multiple financial and government partners
- Rural communities often contract for essential services—thus contractors need financing
- Significant government support often needed to make projects viable
- Term financing is scarce and highly sought
- Rural communities and lenders seek credit enhancement providers for projects



Key Observations

- FCS is building new and stronger relationships with USDA state and local offices, which have rekindled mutual mission objectives
- System philosophy remains conservative with focus on projects with ample equity, government support, and credit enhancements
- Collaboration with commercial banks continues to increase and is having a positive affect on program and attitudes toward FCS
- Private placements, such as Rural America Bonds, are becoming increasingly important for rural communities as financial markets remain soft and issuers face obstacles to access public capital markets



Looking Ahead

Over the next 6-12 months we plan to:

- Enhance our on-going reporting and oversight processes
- Further evaluate the economic impact of Investments in Rural America
- Consider changes to pilot program criteria to ensure effectiveness
- Monitor general economic conditions that are adding stress to some projects, which may necessitate adjustments to original projects and our oversight
- Continue to identify success stories and challenges
- Participate in an open dialogue with USDA on non-leveraged RBICs, NMTCs, and secondary market sales of USDA guaranteed paper



Thank You

Questions?

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