Remarks by
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Farm Credit Administration
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Introduction

Good morning and thank you for the opportunity to be here.

I'd like to thank Tony Wilkie and the Farm Credit Council staff for their work to ensure the Farm Credit System has a strong advocate for its interests in Washington.

The Council has been a leader of the Rebuild Rural Infrastructure Coalition. This coalition of more than 200 organizations is making sure that the voice for rural America's infrastructure needs is heard. So I especially want to thank you for your leadership on this important topic.

I'd like to take a moment to recognize the FCA and FCSIC staff who are with us today. They are committed to the mission of the Farm Credit System and some of the HARDEST-working people in all of government.

I would also like to recognize my FCA board colleagues, Jeff Hall and Glen Smith.

Jeff is the current chairman of the Farm Credit System Insurance Corporation. In case you missed it earlier this month, FCSIC announced it will lower the premium rate on adjusted insured debt in 2018. With the new rate of NINE basis points for 2018, I'm sure Jeff is the most popular person in the room!

In all seriousness, it's a great privilege to work with Jeff. His experience, candor, and steady approach are valuable assets for the board. Thank you for your partnership and for being a strong champion for rural America.

Glen was recently sworn in to serve on the board. We're lucky to have him. His many years of experience in farm management and land appraisal will serve us well during his tenure on the FCA board. If you haven't already, I hope you will have the chance to meet Glen here in San Antonio.

Year in review

Last year, I was sworn in as the Chairman and CEO of the Farm Credit Administration. At that time, I outlined five areas I planned to focus on during my tenure:

- Strengthening confidence
- Finding the best possible outcomes for all borrowers
- Delivering all services to all borrowers
- Building partnerships
- And strategic thinking about System structure

As a farmer, former System borrower, former Undersecretary at USDA, and now member of the FCA board, I believe these areas are central to the success of the System. That's why I spent most of last year traveling to meetings to talk about these areas with many of you. I've appreciated your willingness to engage with me on these topics.

When I addressed this session last year, I talked about the 1980s and the similarities – and differences – between now and then. It's clear to me that the System learned a great deal from the 1980s. As a result, the System remains safe and sound and is in a strong position to manage the economic conditions facing U.S. agriculture.

Institutions have strengthened their balance sheets by retaining capital, and the FCS banks are maintaining high quality investments for liquidity. As of September 30, 2017, liquidity at the banks covered almost 6 months of maturing debt.

Institutions have adjusted underwriting standards to keep new debt at sustainable levels. This will keep loans from becoming vulnerable if income and asset values decline.

As of September 30, 2017, the System had $55 billion in total capital and the System's total capital-to-assets was a little more than 17 percent. Nonperforming assets remained less than one percent of gross loans. And the System reported net income of $3.7 billion.

That's not to say there aren't challenges. Large global supplies of grains and soybeans are keeping prices low. Stress in the grain sector has added to the general weakness in farmland values in parts of the country. This has caused some of your members to struggle despite slight improvements in farm income last year.

That's why I'm focused on encouraging the System to find the best possible outcome for all borrowers within the bounds of safety and soundness. I know this is important to you, as well.

Over the past year, I've learned a lot about the System's efforts to support producers in stressed sectors of the farm economy. Both large and small associations are using innovative ways to support their members.

For example, at a meeting in Colorado last year, I learned that some associations are giving some of their borrowers the option to defer the principal portion of their 2018 payments. This gives these producers the chance to re-amortize the outstanding balance over the remaining life of the loan. It also gives them additional working capital, which in turn gives them flexibility and time to make needed adjustments to their operations.

Other associations are developing memorandums of understanding with borrowers in stressed sectors. These agreements provide associations and their borrowers a clear understanding of each party's expectations for continued financing.

This is exactly the type of service that will build confidence in your cooperative and ensure the best possible outcome for your members. Plus, Congress is clearly interested in learning about the services you're providing.

Last year, FCA testified at two congressional hearings. In both hearings, members of Congress wanted to know what the System was doing to help farmers and ranchers facing financial difficulty. So you can strengthen congressional confidence in the Farm Credit System by seeking the best possible outcome for each borrower.

Congress also wanted to learn about your services to support the young, beginning and small farmers. With the average age of a farmer now over 58, Members of Congress continue to express their interest in supporting the next generation of producers.

Today, the System's outstanding loans to young farmers are about one out of every six System loans; to beginning farmers are about one out of every four; and to small farmers are about one out of every two. This is something you should be proud of.

But remember, the potential future members of your cooperative need confidence that the System will do its best to meet their credit needs, without regard to their race, gender, or type of operation.

So continue to focus on your YBS mission. Make sure that your marketing strategies are reaching young, beginning and small producers who may not be aware of the services that the System can provide.

I'm also encouraging the System to provide a full suite of services in your service territories. In California and Illinois last year, I was excited to learn about associations partnering to provide rural home loans. As some associations scaled back or discontinued their home lending programs, they partnered with other institutions to provide these services in their territory.

These partnerships are EXACTLY what I mean when I say, "ALL services for ALL borrowers."

And speaking of partnerships, it's been great to see the work the System is doing to improve the vitality of our rural communities. Your partnerships with one another, with private investors, with Farmer Mac, and with commercial banks are strengthening rural communities.

We've all seen the daunting statistics regarding the state of our rural infrastructure. Farms, agribusinesses, and others in rural communities need quality infrastructure to be competitive in the future.

For decades, the System has used its statutory authority to finance rural development projects – especially energy and water projects. In doing so, it has improved countless rural communities.

I applaud this work and encourage all associations to use your statutory authority to improve the vitality of rural communities. One way to do this is through Rural Business Investment Companies (RBIC). These companies can inject investment capital to reenergize the rural economy, helping small businesses grow and strengthening local communities.

RBICs require only a modest amount capital, but can do an enormous amount of good — not only for rural America but for agriculture, too.

Speaking of capital, the System provided over $1BILLION in patronage payments in 2016. Think about that for a minute.

That amounts to a billion-dollar stimulus to agriculture and rural America – courtesy of the System's cooperative structure. Think about that for a minute. That's truly a remarkable contribution to the rural economy.

Structure and capital

I've spent a good deal of time this morning talking about issues important to me. But I also know the importance of listening. Let me spend a few minutes now on a couple topics that I know are important to many of you.

System Structure. Some folks think I kicked a hornet's nest last year by suggesting we have a year of dialogue around the topic. This is not a new issue, but it is an important one.

The System has been in a constant state of renewal since its inception in 1916. As it continues to evolve, we must evaluate how any proposed change could impact the integrity and cooperative structure of the System.

We must look at the operational, managerial, and reputational risks that might result from the change. And we must consider how the change might affect the relationship between the funding bank and its associations.

Bottom-line, your members and stakeholders must have confidence that structural changes are in the best long-term interest of the System and those it is serves.

Now let's talk about capital. Empirical data show that the System has thrived over many years. It has continued to grow and has posted favorable returns on assets.

The new capital rules went into effect at the beginning of 2017. They were the product of many years of work by FCA staff, with significant input by System representatives. The goal was to adopt capital rules appropriate to the System, yet comparable to those established for commercial banks.

Over the past year, there has been a lot of discussion within the System about the new capital rules, capital efficiency and the location of capital. We've also heard concern that the new criteria used to assign a capital rating under the Financial Institutions Rating System or FIRS may constrain growth in the future.

To implement the capital rules, our Office of Examination developed criteria to assess capital adequacy under the new rules. This included certain numeric benchmarks that our examiners could use when evaluating what capital rating an institution should be assigned.

Now that the new capital regime has been in place for a year, FCA staff is reviewing whether any changes are warranted in how we examine and evaluate capital adequacy at System institutions.

As you know, capital is only one of SIX components we use to evaluate the safety and soundness of System institutions under FIRS. Today, we want to make this clear: achieving a FIRS 1 capital rating is not -- in itself – the only measure of strength for a System institution.

What IS of vital importance is ensuring that FCS institutions are well managed and are meeting their mission to provide competitive credit to agriculture and rural America. High levels of capital alone cannot guarantee this.

Over the past year some System institutions have expressed the need to maintain a FIRS 1 capital rating regardless of what else is going on. The FIRS 1 benchmark has become a sort of self-imposed minimum for some institutions.

Keep in mind that various FIRS benchmark ratios are intended to measure different aspects of capital. Some ratios measure total capitalization, while some measure quality and composition of capital. When evaluating capital adequacy and setting FIRS ratings, our examiners look at both qualitative and quantitative elements.

How much capital any institution really "needs" requires careful evaluation of current and emerging business risks by board members and management. This process is often more a matter of reasoned judgment than scientific precision. It also means not relying too much on only one model or one measure.

Also, how much capital an institution needs -- or its board believes it needs -- can vary based on local situations. Many System associations currently operate at capital levels well over the FIRS 1 benchmark.

We want you to know that if you are following prudent risk management practices you can safely operate with a FIRS 2 capital component rating. A FIRS 2 rating indicates that you have adequate capital.

The Farm Credit System is a government-sponsored enterprise and represents a public policy success by fulfilling its statutory mission. We recognize that determining how much capital is needed is a complex question, so we're open to a healthy discussion with and among System representatives on the issue.

Cooperative principles

Now I would like to speak directly to those of you who serve on a bank or association board of directors. Early in my career, I had the chance to serve on the board of directors of the local grain elevator in Oldham, South Dakota. It was a big responsibility for a young farmer – especially since I was selected to fill the seat my father had held before me.

It was fun to be a part of this board. Every year, I had the chance to go to the Grain Terminal Association's annual meeting in Minneapolis. But for me, the big event was our local annual meeting. The local TV guy provided the entertainment by playing the guitar and telling some colorful stories. We handed out the checks and served supper.

Leonard, the local feed representative, would bring a big grill that he pulled behind his truck. He'd dump several bags of charcoal in the grill to make a couple hundred hamburgers for the crowd. One year he was anxious to get home and he didn't close the grill tightly or wait for the coals to die.

About five miles down the road, the grill was glowing red from the rushing air, and red-hot ash was flying out and landing in the August-dry ditches. Needless to say, our annual meeting was cut short. Some of the board members and attendees had to fulfill other responsibilities as volunteer firefighters.

All this is to say, as a board member you have an enormous responsibility. That means putting out fires quickly and preventing them whenever possible. It means having healthy checks and balances with management. It means adhering to the cooperative principles that have been the foundation of the System's success. I was reminded of the importance of these principles throughout my travels this past year.

Healthy cooperatives work to innovate and grow. They provide their members the education and training they need for democratic participation in the cooperative. Education and training are especially critical for boards of directors so that they can help set effective policy and make good decisions on behalf of the cooperative and its members.

A principle that may often get overlooked is cooperation among cooperatives. This may be the most important principle for the Farm Credit System. Each institution has the autonomy and independence to grow and create opportunities to serve its own members. But board members must remember that many stakeholders, including investors and members of Congress view the System on a consolidated basis. Put another way, they view the System as ONE.

So the actions of one institution can and will affect the reputation of the System as a whole. This means that each of you must think about how your actions affect the confidence of the public, Congress, and investors.

It's no secret that some people don't see the continued need for the System. The best way to combat that idea is to maintain public and congressional confidence in the Farm Credit System by fulfilling your mission to serve agriculture and rural America in good times and bad.

Being a member of the board is a tremendous responsibility. Every time you step into the boardroom, keep in mind the cooperative principles on which the System is based, as well as the future of the Farm Credit System as a government sponsored enterprise!

Conclusion

I will close by saying that many if not most of you in the audience today are farmers or ranchers. You know what most nonfarmers don't: That farming is stressful.

You know the toll it can take on your body and mind. You know what it feels like to lie awake at night wondering when it's ever going to rain and then — a couple weeks later — when it's ever going to stop.

You know how it feels to work 16-hour days to get a crop planted or harvested. You know how it feels when the prices are so low you can barely cover your costs.

What makes the System unique is that The LEADERS of the cooperative are also the CUSTOMERS of the cooperative. Your borrowers trust you because they know that YOU know what it's like to be in their shoes. You've borrowed money to buy tractors and combines, and you've borrowed money to expand your operations. No other lender can understand the needs of farmers and ranchers the way you can. That's the beauty AND the strength of the cooperative model.

So hold fast to those cooperative principles. ESPECIALLY the one about cooperation among cooperatives. No problem is too big if you work together.

Find ways within your authority to help support rural communities and the modernization rural infrastructure. And ALWAYS keep your mission to farmers, ranchers, and rural America as your top priority.

In the end, THAT is what matters. THAT is what will win you the confidence of all your stakeholders. THAT is what will ensure your success for the next 100 years.

Thank you.