May 10, 2012

Testimony of

Matthew H. Williams

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Subcommittee on Department Operations, Oversight, and Credit

of the

House Committee on Agriculture

United States House of Representatives

American Bankers Association

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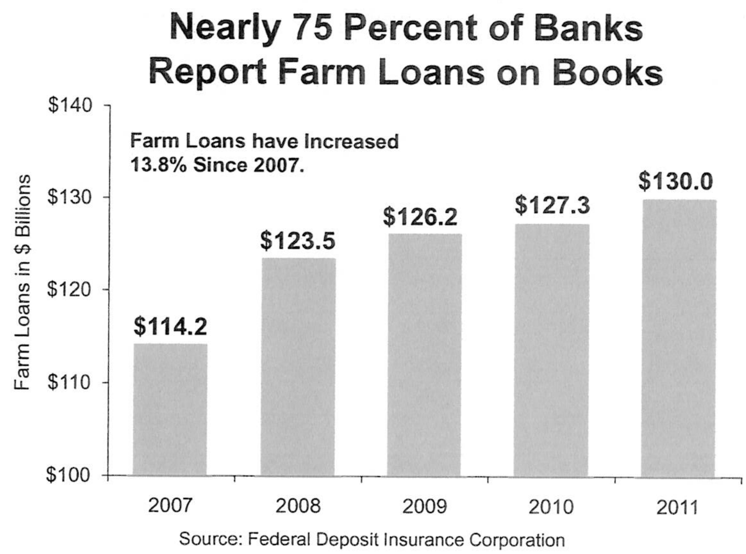
Chairman Fortenberry, Ranking Member Fudge, and members of the Subcommittee, my name is Matthew H. Williams, and I am the Chairman and President of Gothenburg State Bank in Gothenburg, Nebraska. My great grandfather founded the bank in 1902 and our family has operated it since then. My grandfather served as president of the bank and my father followed him in the job. Since it was founded, Gothenburg State Bank and my family have survived many economic catastrophes including the farm crisis of the 1920s, the Great Depression, the farm crisis of the 1980s, and the Great Recession of 2008/2009. We plan to continue to serve the citizens of central Nebraska for the next 100 years or more. Our bank's tag line is "Still Pioneering" and it is a core value of our company. Today, Gothenburg State Bank has two office locations, assets of $125 million, and employs 28 people. Our loans total nearly $87 million with about 75% of our portfolio connected to agriculture in a direct or indirect way.

I also serve as Chairman-Elect of the American Bankers Association (ABA), and I appreciate the opportunity to present the views of the ABA on future farm policy. The ABA represents banks of all sizes and charters and is the voice of the nation's $13 trillion banking industry and its two million employees. ABA is uniquely qualified to comment on agricultural credit issues as banks have provided credit to agriculture since the founding of our country. Over 5,500 banks — nearly 75% of all banks — reported agricultural loans on their books at year end 2011 with a total outstanding portfolio of nearly $130 billion. More farmers and ranchers receive credit from the banking industry than from any other source. Banks are also major providers of credit to small farms and ranches — banks held over 1.1 million small farm loans, with almost 781,000 loans made for $100,000 or less. In addition to our commitments to farmers and ranchers, thousands of farm dependent businesses — food processors, retailers, transportation companies, storage facilities, manufacturers, etc. — receive financing from the banking industry as well.

The outcome of the next Farm Bill is extremely important to my customers in Gothenburg, to my bank, and to bankers throughout the country who provide the credit that American agriculture needs to grow and prosper. We appreciate the opportunity to share our views on future farm policy.

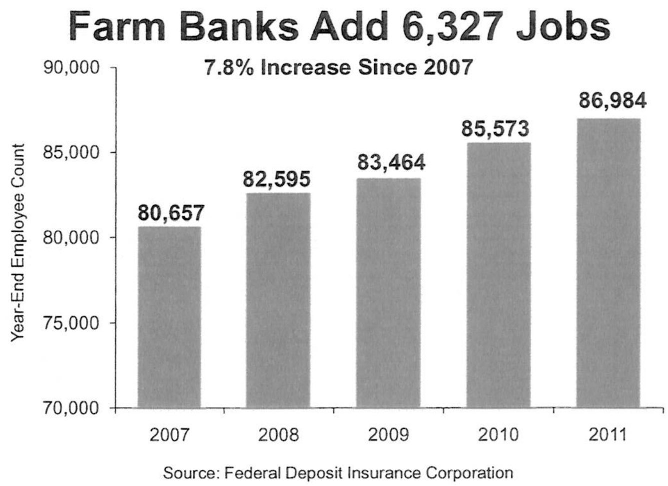


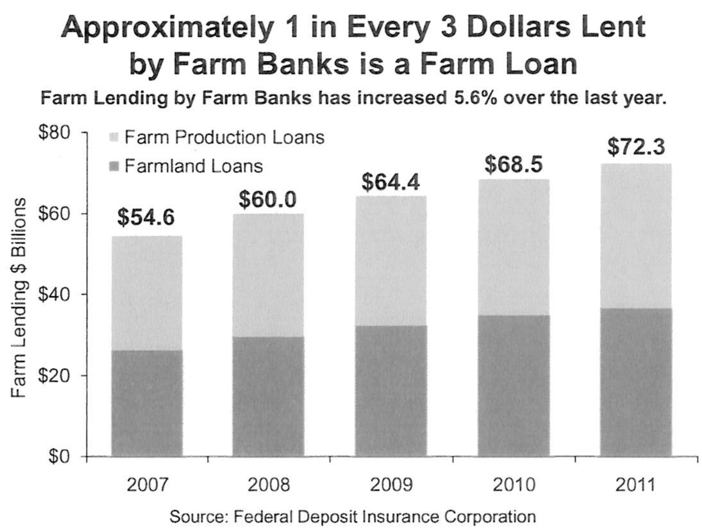
Banks are Healthy and are Providing the Credit Agriculture Needs

I mentioned earlier in my statement that over 5,700 banks have agricultural loans on their books. The ABA produces an annual study of banks that have a concentration in agricultural loans — banks that have over 14% of their total loan portfolio in agricultural loans, which includes Gothenburg State Bank. At year end 2011, there were 2,185 banks in this group. ABA defines these banks as "Farm Banks." I would like to share a few of the findings from the 2011 study:

- Farm Banks are generally small institutions. The median sized farm bank had $90.6 million in assets.
- Farm Banks operate over 7,534 locations throughout rural America.

- Farm Banks employ 86,984 rural Americans and they increased employment by 6,327 employees since 2007.
- Farm Banks increased farm lending in 2011 by 5.6% to $72.3 billion.
- Approximately one in every three dollars lent by a Farm Bank was an agricultural loan. You can see from these numbers that a strong agricultural economy is essential to the success of these institutions.
- Farm Banks reported a strong increase in earnings and improved asset quality in 2011, and over 99% of all Farm Banks met the regulatory requirement of being well capitalized in 2011, the highest capital rating.





The Farm Economy is Strong

2011 was a record breaking year for my customers and for most farmers in the country. USDA reported that net cash income in 2011 was $110 billion, nearly a 20% increase over 2010. While the USDA forecast for 2012 is not quite as good as 2011, net cash income is projected to reach $96.3 billion, well above the average set over the past 10 years. Prosperity has transformed the balance sheets of many of my customers and of many farmers and ranchers throughout the country.

Agricultural Real Estate Values Have Increased Due to Farm Prosperity, Not Leveraged Speculation

There has been a great deal of focus by many on what has been happening with farmland values. The question most asked is, "Are we looking at another asset bubble?" There is no doubt that farmland values have escalated dramatically over the past several years. There are many factors behind this significant increase in land values, and fortunately, excessive lending by banks is not one of them.

Managing agricultural loan risk is what we do at Gothenburg State Bank, and what bankers do all over the country. To give you a sense of our posture towards farm real estate lending, please consider some of the standards at our bank:

- We have very conservative underwriting standards for real estate lending and these have not changed for a decade or more.
- Repayment-ability is the primary driver of our underwriting — if the request does not cash flow, we do not do it —regardless of the collateral position of the customer.
- We only lend a maximum of 60% of the appraised value of the land (loan-to-value).
- In our current farmland loan portfolio, our average loan-to-value is about 40%.
- Even though land values have increased to $6,000 per acre in our service area, we use $3,500 per acre for credit analysis purposes when calculating net worth position, debt to assets, and other key ratios.
- I cannot overstate the value of the technology that my bank and that most banks have invested in that allows us to do credit analysis and run "what if" scenarios almost instantaneously. In a recent exercise at our bank, we projected that a 40% drop in real estate values would reduce the balance sheet net worth of our customers, but it had very little or no effect on the quality of our loan portfolio. Our bank's risk to the FDIC insurance fund would not change.

Our farm and ranch customers, and the farm and ranch customers of many other banks, have enormous skin in the game in their operations. Many are paying cash for real estate. Leverage levels are at or near a historic low. Prosperity is driving the demand for farmland and retained earnings are providing the cash to purchase it.

ABA's Recommendations to Congress for the next Farm Bill

Repeal Term Limits on the USDA Farm Service Agency Guaranteed Loan Program

I have spoken about the prosperity that many farmers and ranchers have enjoyed over the past decade. However, for many reasons, that prosperity has not benefited all farmers or ranchers. For over forty years the banking industry and the USDA have worked cooperatively to provide access to credit to those farmers and ranchers who have some deficiency in their operation that makes them ineligible for bank credit. Many of these farmers and ranchers who borrow are young and are still acquiring the asset base they need to be able to qualify for bank loans. Most of these farmers operate small farms because the average loan is under $200,000 which is not a large farm loan today given the capital that modern agriculture demands. Despite the challenges these young and small farmers and ranchers face, they are conscientious customers who handle their credit obligations very well.

I am referring to the farmers and ranchers who borrow money from banks through the guaranteed farm loan programs offered by the USDA's Farm Service Agency (FSA). Since it is a credit guaranty, banks like mine underwrite and fund the loan and the USDA provides the bank with a guaranty against loss on the loan. Over 35,000 farmers and ranchers access credit through this program. Banks are not the only participants as Farm Credit System lenders, credit unions, state agricultural credit programs, and others work with USDA to provide credit to these farmers and ranchers.

The program has been a resounding success. Each year a limited appropriation is leveraged into a significant program that, in many cases, is the only way these farmers and ranchers can access credit. At the end of FY2011, the portfolio of guaranteed farm and ranch loans exceeded $10 billion. Even though these customers have some financial statement or operating deficiency, they are very conscientious borrowers. FY2011 year-end loan delinquencies were 1.43% and losses in the program were .50% of outstanding loans. From a delinquency and loan loss perspective, this is a very sound portfolio of loans.

In the early 1990s, Congress inserted "term limits" into the program that only allowed farmers and ranchers a limited period of eligibility for the program. While the goal of term limits was understandable, it has created uncertainty for many farmers and ranchers. I should also note that I do not know of any comparable eligibility limitation in other federal loan guaranty programs. Given the volatile nature of the agricultural economy, the practical application of FSA term limits has caused hardship to those farmers and ranchers who can least weather a financial setback. As a result of term limits, an increasing number of farmers and ranchers are no longer eligible for additional credit under the program, which could make access to credit in the future very difficult, if not impossible, for these producers.

For this reason, the American Bankers Association (and many other lender and farm organizations) recommends the repeal of term limits on the USDA, Farm Service Agency Guaranteed Loan Program.

Preserve the Federal Crop Insurance Program

As this committee seeks ways to craft a new Farm Bill that is responsible to the budgetary needs of our country, as well as to continue to provide farmers and ranchers with some measure of protection against catastrophic losses, I want to remind you that Federal Crop Insurance provides my customers with the certainty they need to make responsible planting decisions and provides my bank with the confidence we need to extend credit to our customers. Our job at the bank is to manage risk and Federal Crop Insurance is an important tool that we use to manage the enormous risk in today's agriculture. Input costs to plant crops today are staggering. My customers use credit from the bank to help them get a crop planted and harvested. If Federal Crop Insurance was in some way diminished, our ability to lend — in some cases —would be curtailed.

In preparation for this hearing I spoke to many of my farm customers about what they would seek in the next Farm Bill. Overwhelmingly they said the current crop insurance program should be preserved and strengthened. My customers, and all farmers and ranchers, are extremely confident and self-sufficient people. It takes a great optimist to plant a crop, work on it all year, harvest it, and then sell it. But, no matter how optimistic farmers are, they can not control the risks presented to them by weather. In addition to protecting against acts of nature, farmers have the confidence in Crop Insurance to utilize price risk hedging techniques because they know that a percentage of their crop is guaranteed. Without this key risk management element, fewer farmers would hedge their crop prices and more of them would be restricted to selling at harvest, when prices are typically at their lowest.

For these reasons, the ABA urges this committee to preserve the Federal Crop Insurance program. The program is widely accepted by farmers as a key element of a solid risk management program that they can take to the bank.

The Banking Industry is Concerned about the Risk a Government Sponsored Enterprise Poses to the Rural Economy

The market for agricultural credit is very competitive. I compete with several other banks in my service area, finance companies from all of the major farm equipment manufacturers, several international banks, credit unions, life insurance companies, and finance companies owned by seed and other supply companies to name a few. However, the most troublesome competitor I face is the taxpayer-backed and tax-advantaged federal Farm Credit System (FCS). The FCS was chartered by Congress in 1916 as a borrower-owned cooperative farm lender at a time when banks did not have the legal authority to make farm real estate loans.

Today the FCS is a large and complex financial services business with over $230 billion in assets. It is profitable — it earned $3.9 billion in 2011. It is tax-advantaged and enjoyed a combined local, state, and federal tax rate in 2011 of 6.4%. In spite of their size, current profitability and tax advantages, the Farm Credit System presents the same kind of liability to the American taxpayer as Fannie Mae and Freddie Mac. As a Government Sponsored Enterprise (GSE) like Fannie Mae and Freddie Mac, the American taxpayer is the ultimate backstop should the Farm Credit System develop financial problems. The potential liability that GSEs pose to taxpayers became very real in 2008 when the federal government seized Fannie Mae and Freddie Mac. An earlier near collapse of the federal Farm Credit System in the late 1980s, as a result of their irresponsible farm lending, foreshadowed what taxpayers would confront more than twenty years later with the housing GSEs. Congress will take up the question about what to do with the housing GSEs in an effort to restructure home mortgage finance in the United States. I urge this committee to include the federal Farm Credit System in those discussions as there is no difference between the risk the housing GSEs pose to our economy and the risk the Farm Credit System poses to our rural economy.

The Banking Industry is Well Positioned to Meet Agriculture's Needs

For the past decade, U.S. agriculture has enjoyed one of the longest periods of financial prosperity in history. It has been an exciting time in farm country. Financially, American agriculture has never been stronger. In 2011, many American farmers and ranchers enjoyed their most profitable year ever. The balance sheet for U.S. agriculture is the strongest it has ever been with a debt-to-asset ratio of less than ten percent. Farm and ranch net worth is in excess of $2 trillion. This unprecedented high net worth is due in part to a robust increase in farm asset values (mainly farm real estate), but is equally due to solid *earned* net worth as farmers have used their excess cash profits to retire debt and to acquire additional equipment and additional land. As a result, farmers and ranchers today have the capacity to tap their equity should there be a significant decline in farm profitability resulting in diminished cash flows. While no farmer or rancher wants to take on additional debt, the strength of the U.S. farm and ranch balance sheet gives producers options to do so if the need arises.

When the agricultural economy collapsed in the middle 1980s, the banking industry worked with farmers and ranchers to restructure their businesses and to rebuild the agricultural economy. Since that time banks have provided the majority of agricultural credit to farmers and ranchers. While other lenders shrank their portfolios or exited the business altogether, banks gained market share by expanding lending, just as we did following the economic crisis of 2008/2009. We saw opportunity where others did not.

The American Bankers Association has worked with Congress on <u>every</u> Farm Bill ever passed. We are proud of what we have contributed to the debate in the past and we look forward to working with Congress in the future as you craft the next farm legislation.

Thank you for the opportunity to express the views of the American Bankers Association. I would be happy to answer any questions that you may have.

United State House of Representatives
Committee on Financial Services

"TRUTH IN TESTIMONY" DISCLOSURE FORM

Clause 2(g) of rule XI of the Rules of the House of Representatives and the Rules of the Committee on Financial Services require the disclosure of the following information. A copy of this form should be attached to your written testimony.

1. Name:	2. Organization or organizations you are representing:
Matthew H. Williams	American Bankers Association

3. Business Address and telephone number:
1120 Connecticut Avenue, N.W. Washington, D.C. (202) 663-5359

4. Have you received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?	5. Have any of the organizations you are representing received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?
☐ Yes ☑ No	☐ Yes ☑ No

6. If you answered "yes" to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets.

7. Signature:

Please attach a copy of this form to your written testimony.

American
Bankers
Association

Building Success. Together.

MATTHEW H. WILLIAMS

ABA Chairman-Elect

Matt is Chairman and President of Gothenburg State Bank, a $125 million community bank located in Gothenburg, Nebraska. He is a fourth-generation banker and has been with the family owned bank since 1973.

Matt currently serves as Chairman-Elect of the American Bankers Association and also serves on the ABA Board. Matt has been a member of the ABA Government Relations Council and has served as the ABA State Grassroots Coordinator for the State of Nebraska. He is currently serving as one of 14 bankers from across our country on the FDIC Advisory Committee on Community Banking. Matt was chairman of the Nebraska Bankers Association in 2003-2004 and has served on many NBA committees.

Matt also serves as a Trustee of the University of Nebraska Foundation, UNL Ag Builders, the University of Nebraska President's Advisory Council, the University of Nebraska Finance Department Advisory Board, and is a past Director of the State Chamber of Commerce. He was recently appointed by the University of Nebraska's Board of Regents to the Board of Directors of Innovation Campus. Matt has been very involved with economic development in Gothenburg and Dawson County formerly serving as Chairman of the Gothenburg Improvement Company and President of the Gothenburg Area Chamber of Commerce. Matt recently served as a State Director for the Tom and Nancy Osborne TeamMates mentoring program.

Matt received his undergraduate and Law degrees from the University of Nebraska-Lincoln. Matt and his wife Sue have two children and three grandchildren.

December 2011