



FARM CREDIT

Testimony of Marc Knisely
on behalf of the Farm Credit System before the
U.S. House Subcommittee on Commodity Exchanges, Energy, and Credit
December 11, 2019

Mr. Chairman, Ranking Member Scott, and other distinguished members of the subcommittee, thank you for calling this hearing today to discuss credit conditions for U.S. agricultural producers and for allowing me to testify on behalf of the Farm Credit System. My name is Marc Knisely. I am the President and Chief Executive Officer of AgCountry Farm Credit Services, based in Fargo, North Dakota.

AgCountry Farm Credit Services is a financial cooperative providing financing, crop insurance and related services to more than 18,000 farmers, ranchers, agribusinesses, and rural homeowners in eastern North Dakota, western Minnesota, and central Wisconsin. We provide \$7.6 billion in loans through our 37 locations throughout our territory and have nearly 600 employees. So far this year, AgCountry made 6,700 loans to farmers and ranchers for over \$2.1 billion.

Most importantly, we are a member-owned, locally-governed cooperative and a proud member of the Farm Credit System. Along with 71 other Farm Credit institutions, AgCountry shares a critical mission to support rural communities and agriculture with reliable, constructive credit and financial services, today and tomorrow.

Farm Credit is a nationwide network of borrower-owned lending institutions that share a critical mission assigned to them by Congress a century ago. These independent institutions include four wholesale banks and 68 retail lending associations, all of which are cooperatively owned by their customers: farmers, ranchers, cooperatives, agribusinesses, rural utilities and others in rural America.

Our mission is to ensure that rural communities and agriculture have a reliable, constructive source of financing irrespective of cycles in the economy or vagaries of the financial markets. Hundreds of thousands of farmers around the country developed a farm operating plan this year knowing that Farm Credit has the financial strength to finance that plan and the strong desire and ability to help them succeed.

Farm Credit's unique cooperative structure means that the customer-owners who sit on our boards of directors are living, working, and raising their families in rural communities. They are deeply invested in the success of those communities and are interested in finding more ways for Farm Credit to contribute to that success.

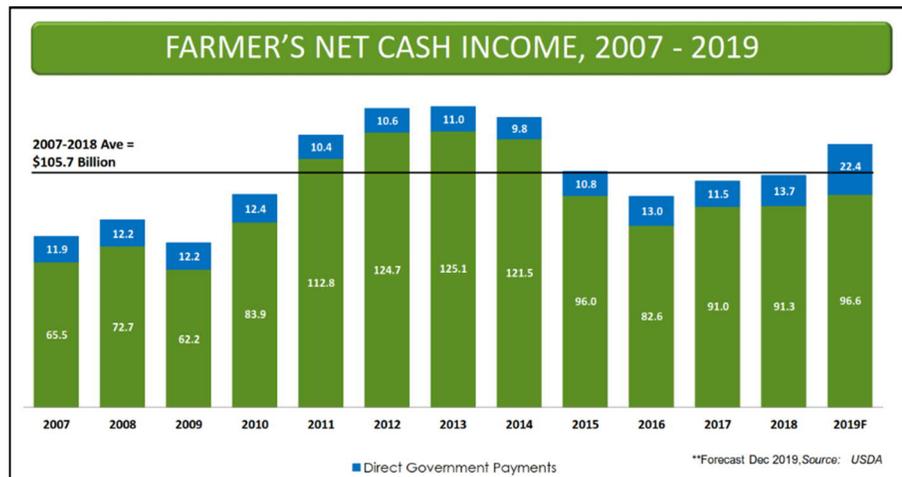
Farm Credit reverses the normal flow of capital, raising money in urban financial centers and bringing it to rural communities.

There is no federal funding provided to Farm Credit. Instead, the four Farm Credit System banks own the Federal Farm Credit Banks Funding Corporation, which markets debt securities to the investing public that fund the lending operations of all Farm Credit institutions. Diversification of lending portfolios is a source of Farm Credit's financial strength. Through diversification of our lending – by geography, industry and loan size – Farm Credit manages risk and insulates itself against the cyclical nature of the industries we serve.

We believe we can play a more significant role in rural development, revitalizing rural infrastructure, strengthening the rural economy and creating good jobs for rural families. We are prepared to continue working with the committee and our partners in the community banking sector to find ways that all of us can contribute more to the vitality and success of our rural communities.

Credit Conditions Update

Today's subcommittee hearing is timely. Farmers across the country continue to feel the impact of trade disputes, disastrous weather, and low commodity prices. Many producers are struggling to make even a small profit and many others are unprofitable at current price levels.



Net farm income, although projected to be up this year from 2018, remains far too dependent on direct government payments, which might not continue. I will also note that due to harvest delays, there is a lot of crop still remaining in the fields making this projection far from a done deal.

We greatly appreciate this committee's efforts to pass a strong farm bill, including improvements to the federal crop insurance program. Crop insurance clearly is underpinning the farm economy today.

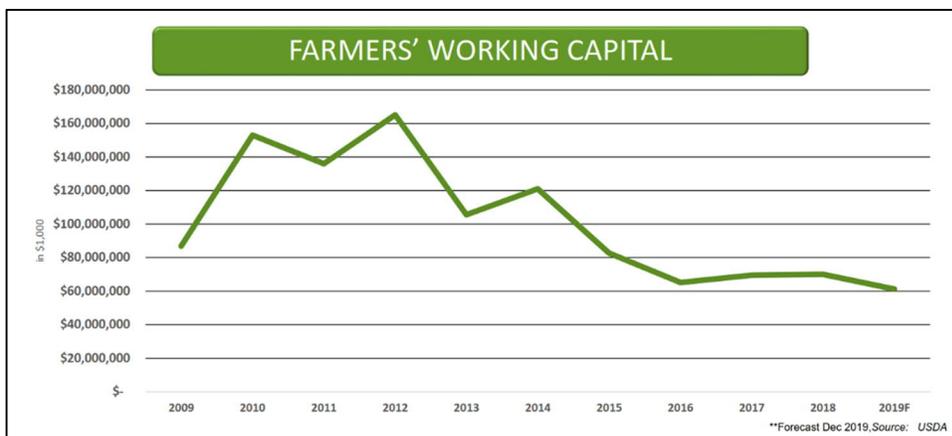
The program is functioning as intended. Farmers pay for coverage they can count on when weather decreases production and cushions the impact of falling commodity prices – to a degree. Thank you for your work to provide this vital tool to U.S. farmers and ranchers.

Last spring we had thousands of acres in Minnesota, North Dakota and Wisconsin that could not be planted due to excess moisture from persistent spring rains. The prevented planting coverage of the crop insurance policy paid claims on those acres to help farmers cover some of their fixed costs and input costs already committed to those acres. This fall we have had unprecedented harvest conditions of snowstorms, fall flooding and more persistent rains. Thousands of acres of good crops in northern Minnesota and northern North Dakota were flooded and destroyed by the rising Red River and its tributaries. Over 100,000 acres of sugar beets were left frozen in the fields because the ground was too wet to get in with harvesting equipment. Crop insurance will help to reduce the losses by covering much of the input expenses and cost of production. However, crop

insurance will not make those acres or the farm profitable. Unfortunately, most of these farmers will experience net operating losses this year.

Similarly, thank you for helping to enact disaster assistance earlier this year. Disaster payments are helping many farmers in areas hit by hurricanes, fires, and other natural disasters survive to plant another year. The recent trade adjustment assistance payments are helping farmers who have no other alternative to cope with trade interruptions brought on by ongoing tariff disputes. We hope that the President, with support from Congress, will continue to make these payments so long as the present trade situation continues.

While disaster assistance and trade adjustment assistance are very welcome, farmers and ranchers need markets they can plan for and on which they can depend. We strongly support swift passage of the U.S./Mexico/Canada trade agreement. USMCA will provide certainty for trade with our two largest agricultural trade partners. We urge your support for passage this year.



Since farm income peaked in 2013, profitability for most farmers and ranchers has been on a long decline. Despite some stabilizing over the past two years, most farmers are feeling the compounding effects of multiple

years of low profits or even losses. As a result, the farm balance sheets that were strong in 2013 today are far weaker. Most worrisome, after six difficult years, working capital levels – the difference between current assets and current liabilities – have declined sharply. Working capital is the cushion against tough times. For many producers today, that cushion no longer exists.

Similarly, debt-to-asset ratios for most farmers are climbing. Overall, farm balance sheets remain leveraged at a comparably low rate, with USDA's 2019 forecast predicting an overall debt-to-asset ratio of just less than 13.5%. Farm sector debt-to-asset ratio, however, is climbing rapidly, up from just over 11% in 2013.

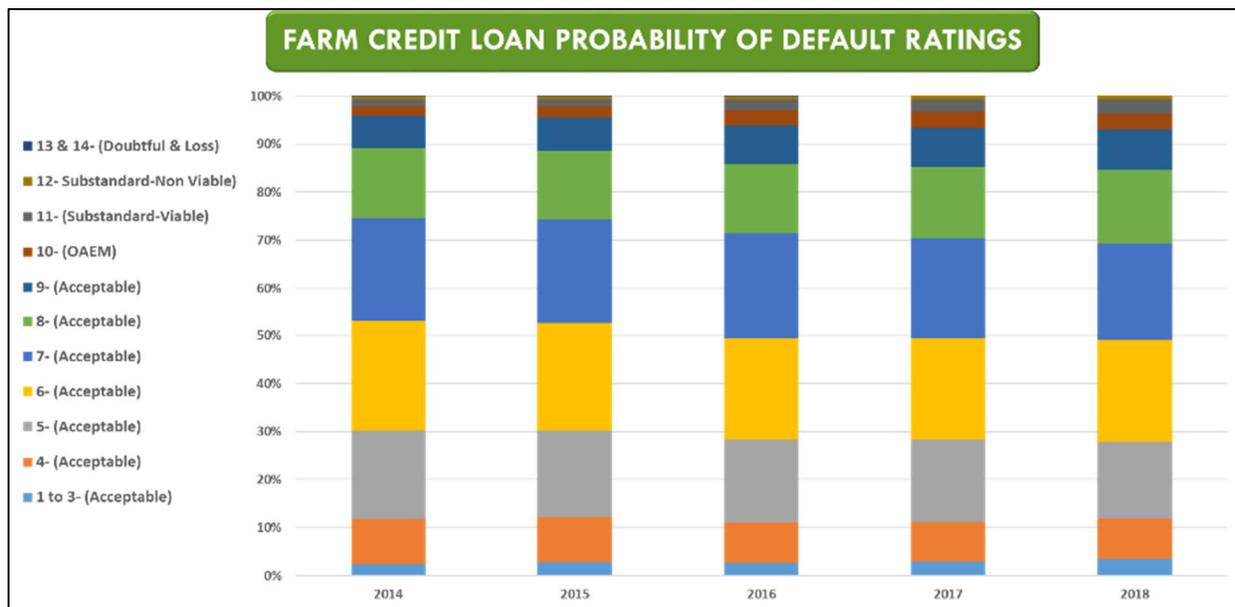
These debt ratio figures are somewhat misleading however, as most farms – and most of the farm real estate – carry no debt. As a result, the industry leverage ratio, which represents the overall average, does not reflect the uneven distribution of debt and its impact on commercial producers. For those producers with debt, who make up most of the farms that produce most of the food and fiber in the U.S., debt ratios are climbing perilously high.

USDA forecasts agree with most private forecasts that commodity prices likely will remain at or near current levels for several years to come. In this price environment, it will be very difficult for farmers to recover the economic losses of the past few years and rebuild their financial strength. That's even more reason that we encourage Congress and the Administration to settle trade disputes, pass USMCA, and pursue other advantageous trade agreements so markets can recover, and farmers can rebuild from the current difficulties.

Media stories over the past year noted a rise in farm bankruptcies and those reports are true – although perhaps a bit misleading. While the bankruptcies are rising, the actual number of farm bankruptcies remains very low. Continuing strong land values, low interest rates, and aggressive cost cutting by farmers all help avoid more bankruptcies. For now, farmers have options, lenders like Farm Credit and community banks, are proactively working with farmers to rebalance loans. Farmers are selling some assets voluntarily and taking other steps to position their operations to withstand the low-price environment.

Despite these efforts, however, financial stress is rising for many producers. An analysis of Farm Credit’s loan portfolio demonstrates the current financial stress under which many farm families operate today.

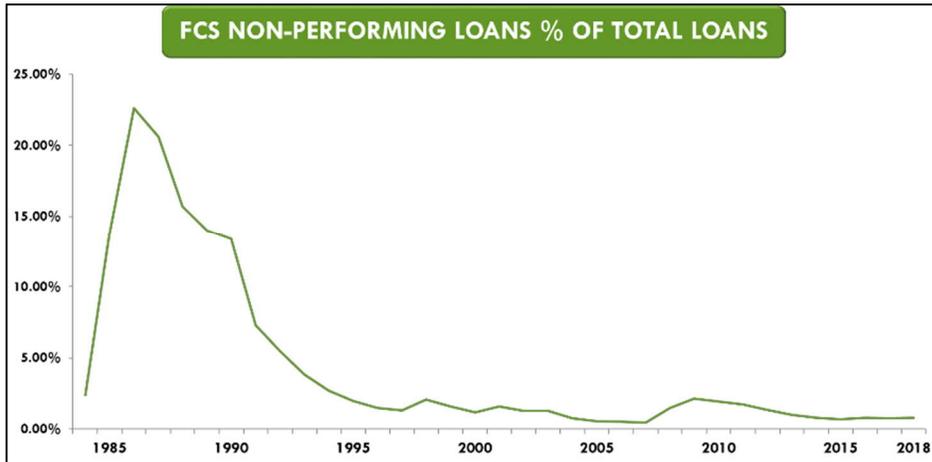
There is little question that commodities across that board have seen their share of challenges, but perhaps no other commodity has suffered as much as the dairy industry in the past few years. Since the beginning of 2017, the state of Wisconsin – which is commonly referred to as America’s Dairyland - has lost nearly 1,700 dairy operations. In neighboring Minnesota, one in 10 dairies went out of business in 2018 alone.



Farm Credit, like most lenders, assigns a credit risk rating for each of its loans. The ratings, on a 1-14 scale, are an accumulation of the many factors impacting the financial standing of a farm operation. The higher the numerical rating, the more stressed the operation. The chart adjacent shows how these risk ratings – which measure the probability that a loan will default – are migrating upward across the past five years. Loans that were rated as 6 – a very strong rating – are now rated as 8 – still good but weaker. Loans that were an 8 are now pushing toward 10 – the beginning of the troubled loan category. Loans rated 10 and above increased from 4.2% in 2014 to 7% at the end of 2018.

As difficult economic conditions continue, farmers are becoming more financially stressed and Farm Credit loan portfolios are beginning to show that stress. Fortunately, three important factors are combining to give farmers and ranchers a chance to survive this downturn – low interest rates,

continuing strong land values, and a non-farm economy that continues to provide job opportunities outside the farm gate.



Probably most importantly, farmers themselves are proving to be highly skilled at cutting costs and taking advantage of narrow marketing windows to keep their operations going. Extending the life of equipment, precisely targeting input supplies, and cutting

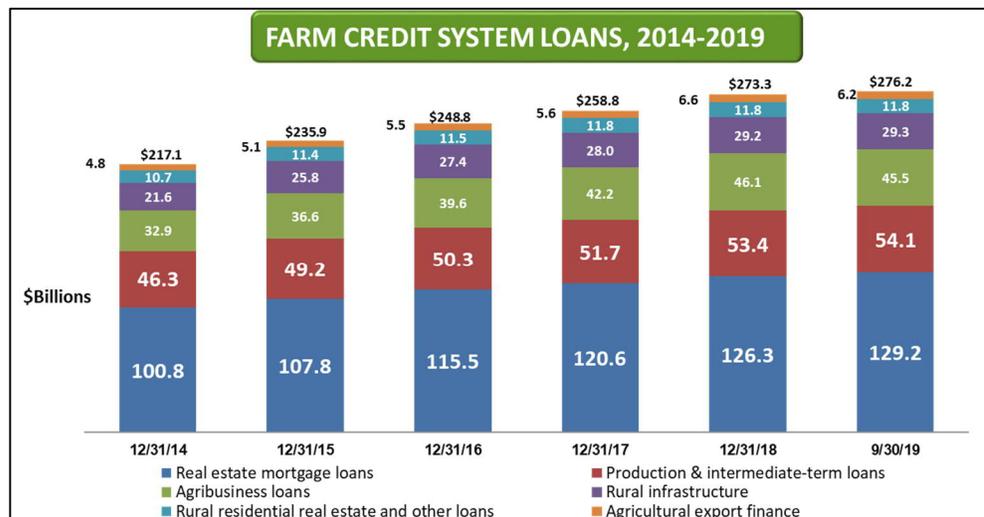
family living expenses all are helping farmers continue despite low prices. This expert management by farmers only goes so far, however, and soon many farmers will need to see better price levels to survive.

We are also seeing a rise in voluntary exits from farming, particularly among older farm operators. As the outlook for prices remains low, many older farmers are selling or renting land and pulling out of direct operation. Continuing strong land prices are providing much flexibility, both to exiting farmers and to farmers rebalancing their operations.

Fulfilling Farm Credit's Mission During a Downturn

We have a simple philosophy as we approach difficult economic circumstances farmers are experiencing now – we know our customers well, understand and respond to their needs and work cooperatively with them to analyze and structure our transactions to provide them with the best possible outcome.

Farm Credit is a responsible lender. We understand that credit cannot be a substitute for income. We work proactively with customers to explore a wide range of options to give them the best possible chance to succeed.



Farm Credit is leaning-in to support farmers and ranchers. While overall loan growth slowed somewhat this year, we continue to increase our lending to farmers. Since the beginning of the downturn in 2014, Farm Credit increased its farm real estate and farm production lending by more than \$36 billion.

Today, Farm Credit provides about 40% of the financing for production agriculture and serves nearly 500,000 customers across all our lines of business, including agribusiness, rural infrastructure, rural housing, and agricultural export finance.

We are working with our farm and rancher customers to provide the time and space they need to stabilize their operations and adapt to the reality of a long-term downturn in commodity prices. Our loan officers proactively reach out to customers – on their farms – to work through options that might provide an opportunity to succeed.

As we speak, AgCountry is working with a third generation family farm in Minnesota. This particular dairy farm has been extremely successful in the past, but the tough economic environment of the last four years has led to yearly losses reaching as high as \$500,000. We are doing everything in our power to help out, including working with the Farm Service Agency, allowing interest-only payments and extending the repayment terms. The reality of this situation, and many situations like it, is that our options are starting to run low. If markets continue to struggle, two families on this farm will lose their livelihood, an older generation will see their retirement nest egg disappear, and 20 part-time workers will have to look for other employment.

I want to expand a little more on Farm Service Agency guarantees, which help us work with troubled customers and provide an opportunity for young and beginning farmers. A guarantee on an existing loan strengthens the loan, making FCA examiners less wary of us continuing with the loan, and providing additional time for a customer to find a way to operate profitably. We rarely collect on these guarantees. The value of the guarantee for these customers is the regulatory relief it provides us so we can continue to seek that best possible outcome for our customer. We are grateful that this committee changed the FSA loan limits in the last farm bill. We are using that new authority to farmers' benefit as intended. We also strongly support The BALE Act, HR. 2797, introduced by Representative Mike Bost. The bill would further raise the caps on FSA loan guarantees providing greater flexibility to serve farmers.

Farm Credit is fortunate that our independent federal regulator, FCA, has deep knowledge of agriculture and considerable experience in the inevitable business cycles our members face. Their ability to look holistically at a customer's operation and understand an individual customer's risk-bearing capacity and equity position will, in many cases, determine whether we can continue with that customer. If the FCA is overly restrictive in its approach, it might tie our hands as we work to help members through this cycle. We are optimistic about the FCA's continued good judgment.

While the focus of our testimony today is the financial stress many producers face, we cannot ignore the emotional and mental stress building in among farm families and rural communities resulting from six long, difficult economic years in agriculture. Farm Credit is working to provide resources to help farm families cope with these kinds of stress as well.

Unfortunately, mental health resources in rural communities are lacking and, in many areas, there remains some level of stigma associated with seeking help with mental health issues. Farm Credit is partnering with Michigan State University (MSU) to create an online training course focused on mental and emotional health. It will help provide support and advice for loan officers having difficult or stressful conversations, while also offering tips for strengthening their own mental well-being. The training will also help Farm Credit System employees identify signs of stress in customers and provide techniques to get customers the help they might need to manage that stress.

The Farm Credit training curriculum is modeled on a successful program funded by Congress and created by MSU for USDA's Farm Service Agency personnel. It will be made available to all Farm Credit institutions beginning next February. The training is made possible by a grant to MSU from Farm Credit.

Farm Credit will provide a version of this program to regional and state leaders at the American Farm Bureau Federation and National Farmers Union at their respective annual conventions. These trainings offer additional resources to rural communities across the country to help reach additional individual farmers and ranchers. We hope to make the program available to more farm and rural organizations in 2020.

The training builds on other Farm Credit System efforts to support rural mental health. We are partnering with AgriSafe Network to educate rural health professionals on the mental health risks faced by farmers and ranchers and trains them to integrate basic mental health screenings into their primary care practices. The "Total Farmer Health" campaign helps address the limited mental health services in many rural areas and trains primary care practitioners to better understand and recognize the challenges agricultural producers face and how they might manifest. Farm Credit also is partnering with the Progressive Agriculture Foundation to develop a new curriculum focused on the mental well-being of rural youth ages 4-13, as part of "Ag Safety Days" it hosts across rural America. This curriculum launches in January 2020.

In addition, we and several other Farm Credit institutions are offering our customers access to a free, confidential resource service that had previously been available to Farm Credit employees. We felt it right that given the struggles our customers are facing, they, too, could benefit from the support and guidance of trained professionals when facing increased challenges and the emotional difficulties that follow.

The stress that our customers are facing right now can be further reflected in the faces of our employees. There have been times over the course of the past few years where you can walk into one of our offices and see the emotional weight our staff is carrying with them. As the CEO, this greatly pains me.

We are also concerned that the continuing low commodity price environment is impacting young, beginning, and small farmers. Young and beginning operators especially are likely to have lower equity and be more vulnerable to profitability swings. Smaller operations oftentimes have fewer options for cost-cutting and other managerial changes to help the bottom line. Offsetting this somewhat is the continuing strong non-farm economy that is providing off-farm employment.

Farm Credit's service to young, beginning, and small farmers is increasing. FCA's 2018 annual report reveals that overall volume of Farm Credit lending to YBS farmers increased from 2017 to 2018. In addition, the number of Farm Credit loans made to young, beginning, or small farmers as a percentage of total Farm Credit loans made increased from 2017 to 2018.

Farm Credit makes extraordinary efforts to support young, beginning and small (YBS) farmers and ranchers. Each year, the FCA, our independent federal regulator, compiles data on Farm Credit YBS lending and reports it to Congress. Based on FCA's report:

- Farm Credit made 46,680 loans to young producers (under age 36) in 2018 for a total of \$9.7 billion, up from \$9.07 billion of loans made in 2017.

- Farm Credit made 62,323 loans to beginning producers (10 years or less experience) for \$13.3 billion in 2018, up from \$12.45 billion of loans made in 2017.
- Farm Credit institutions made 114,817 loans to small producers (less than \$250,000 in annual sales) for \$12.5 billion in 2018, up from \$11.69 billion of loans made in 2017.

To put Farm Credit's lending to small farmers and ranchers into perspective, at year-end 2018 Farm Credit had 910,113 loans of all kinds outstanding, and just over half (456,305) were to small farmers and ranchers.

Note: The numbers above cannot be combined. A single loan to a 25-year-old rancher in her third year of ranching with annual sales of \$100,000 could be counted in the young, beginning, and small categories. We report this way for two reasons: our regulator requires it and, more importantly, it is the most accurate portrayal of who we serve. Our regulator, the Farm Credit Administration, is engaged now to better define data requirements surrounding YBS lending.

Note: The number of loans made to YBS farmers during 2018 cannot be directly compared to the number of loans made to YBS farmers in prior years due to a change in the technical counting procedures used in multilender loan participations. The change in counting procedure does not impact the counting of \$ volume of loans made and, as a result, \$ volume figures are comparable year-over-year. The Farm Credit Administration's [2018 annual report](#) explains this in more detail.

Farm Credit institutions have a deep commitment to YBS farmers beyond providing loans. At AgCountry, we provide scholarships to young farmers and their spouses for farm-related education programs, marketing classes and conferences. We provide succession and retirement planning to help young farmers develop transition plans with their parents. We greatly reduce or waive fees for farm accounting and tax planning services. In addition, we host a young and beginning farmer advisory committee to help provide feedback to our association and identify areas to better meet the needs of those within this demographic.

We engage across the spectrum with those entering agriculture, whether they are focused on conventional, organic, sustainable, indoor, farm-to-market operations, or other emerging business models.

As I mentioned earlier, Farm Credit is a customer-owned cooperative. Significant amounts of our operating expenses go toward better serving our customers through new technology, helping them grow their businesses through educational programs and supporting our communities through charitable giving. The net income we generate can be used in only two ways: retained within a Farm Credit institution as capital to build financial strength that ensures continued lending OR paid to customer-owners by way of cooperative dividends, which effectively lowers the cost of borrowing for our customers. In 2018, Farm Credit returned \$2.3 billion in patronage dividends to our customers and over the past five years, Farm Credit returned nearly \$9 billion to our customers. At AgCountry, we returned \$42.5 million last year, lowering our customers' average interest expense by just more than half of a percentage point (54 basis points).

Farm Credit's mission extends well beyond the farm gate. Our mission includes financing for farmer-owned cooperatives and other agribusinesses that farmers depend on to succeed. Farm Credit has financed more than \$6 billion in exports of U.S. agricultural products. We also make nearly \$12 billion in loans for families to buy homes in very rural areas. Because a steady flow of credit means more jobs and economic growth, Farm Credit helps ensure the vibrancy of communities throughout rural America.

Strong, reliable and resilient rural infrastructure is critical to the success of rural communities and a key component of Farm Credit's mission. Farm Credit finances more than \$29 billion in rural infrastructure, including rural electric cooperatives, water systems, telecommunications and broadband providers. These loans improve the quality of life in our rural communities, providing clean drinking water, broadband for our schools and reliable energy for rural families and businesses. Farm Credit's mission is as vital today as it has ever been. We support rural communities and agriculture with reliable, constructive credit and financial services. We provide farmers, ranchers and agribusinesses with the capital needed to make their businesses grow and succeed.

Like the producers we serve, Farm Credit built financial strength in anticipation of this challenging economic cycle. We have been fulfilling our mission for more than 100 years and have deep experience in the inevitable cycles of agriculture. Like most, we could not predict with accuracy when this cycle would begin, nor can we predict when it will end. But experience told us it was coming, and our institutions proactively prepared for it.

When it comes to the present conditions facing agriculture, the bottom line is this: farmers and ranchers across our three states and the country are struggling. This holds true regardless of the commodity, experience level of the farmer or size of the operation. To their credit, and the credit of financial lenders, all parties are working hard to do the things necessary to survive this economic cycle and ensure the vibrancy of communities throughout rural America.

Thank you again for calling this important hearing. I would be pleased to respond to your questions.