

Remarks by Glen R. Smith
Board Member
Farm Credit Administration
Farm Credit Bank of Texas
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It's great to be here in New Orleans, Louisiana, for the Texas Bank annual meeting, and thank you to CEO Larry Doyle and Chairman Jimmy Dodson for our invitations. It's been quite an adventure for my wife and me this past 16 months since we moved to Washington, D.C., from our rural farm home of 36 years in western Iowa. You directors can appreciate the difficulty and complexity of this change. It isn't just a change of vocation, it's leaving our lifetime investments and way of life. Fortunately, our 29-year-old son has proved to be very capable in assuming active management and operation of our Iowa farms and businesses.

A big part of the past 16 months is learning the complexities of this wonderful Farm Credit cooperative system and what makes it work so well. Another part is understanding its history and some mistakes made in the past so that we're not — as the saying goes — destined to repeat them.

I believe an important part of this job is understanding the challenges of different agricultural enterprises and operations throughout the entire country, and to fully understand them, you have to visit. I know a fair amount about raising corn, soybeans, hogs, and cattle in Iowa and Nebraska. In my travels this past year, I've learned about challenges facing citrus in Florida; hurricane damage in South Carolina; a maple syrup sap operation in Vermont; dairies in upstate New York and West Virginia; a free-range chicken operation in Minnesota; a cattle seed-stock operation in North Dakota; almond, pistachio, and vegetable operations in California and Arizona; and crawfish, rice, and sugarcane operations in Louisiana. I've traveled a lot, learned a lot, but I've got a ways to go. Notice I haven't been to Texas yet, but give me a little time and I'll get there.

As I talk to groups outside of Farm Credit, I emphasize this huge enterprise and locational diversity as a strength of the System. Investors in System securities like it too. As I talk to these same groups, I like to detail the critical role the System plays in funneling global investor funds to the farm gate in the most efficient, low-cost manner possible. The System's cost of funds is truly the envy of the financial world — 7 to 9 basis points above Treasury notes. Along with the System's GSE [government-sponsored enterprise] status and tax exemption on real estate financing, I call it the Farm Credit System's "golden goose," which the System and its regulator absolutely must protect.

It is amazing that we have kept that world-class rating after five years of decreasing farm income and deteriorating balance sheets. With the trade wars still raging and major weather

events like floods and hurricanes, I don't see 2019 exactly shaping up as a turnaround year. At FCA we can't help with the price of milk or corn or cattle or control the weather; we are only the regulator of the financier. But what the System can do is provide the lowest possible effective interest rates to farmers and ranchers across the country and lead the market for these lowest rates with the competition. It is imperative that we maintain high credit ratings on System debt instruments in order to preserve those low-cost funds.

Two weeks ago, FCSIC [the Farm Credit System Insurance Corporation], in coordination with FCA, invited two of the rating agencies, Moody's and Fitch, to come to McLean to discuss the priorities they placed on rating our Farm Credit securities so high. Several items made an impression on me personally as the board faces current and future decisions placed before us at FCA. These are my personal notes from the rating agencies' discussion, which closely parallel the thoughts and opinions I have developed throughout the past year. Again, I'll emphasize, these are my personal opinions and observations and not those of the board:

- **A strong capital position** — This was the most frequently mentioned positive consideration. "Heavy weighting was placed on the two-tier structure of capital," said one of the rating agency representatives. "Capital resides with risk with this structure, and it makes it easy to call if there is a need. This creates a second loss position (layer), and losing it could result in a downgrading."

Another representative from a rating agency indicated that "having strong capital at the bank level is comforting, particularly during times of economic duress in agriculture."

- **FCSIC** — The rating agencies like the fact that the System's insurance for its security investors (timely payment of principal and interest) is a separate government corporation, not part of FCA, and provides an independent view of economic and financial analysis and outlook.
- **Structure** — The rating agencies like the structure of the district bank for its strong supervisor role and good visibility and are concerned as critical services like A&L [assets and liabilities] management and IT are removed.
- **A strong regulator** — This is a major determinant in rating analysis:
 - Regulator not afraid to say *no* where appropriate.
 - Regulator not afraid to push back and take regulatory action where appropriate.

A recent business news article on GSE status and privatizing Fannie Mae and Freddie Mac cited the administration as saying two main criteria would need to be met before bringing them out of conservatorship:

- The two companies would need to hold more capital.
- There would need to be a strong regulatory presence that would restrict their activities to their core statutory mission.

That's a pretty good endorsement from our administration, which is generally known for its nonregulatory views.

The last item I would like to talk about is FCA's stepped up emphasis on YBS [young, beginning, and small farmers and ranchers] as part of our mission. Before initiation, we thoroughly researched FCA's authority under 4.19 of the Farm Credit Act of 1971, as amended. We are clearly within our authority. FCA provided more specific guidance in 2000, but that now has been almost two decades ago. First, the data collection needs to be modernized. The second step will be for FCA to encourage the expansion and growth of every one of the System's 69 associations' YBS programs. The last step will be to evaluate the effectiveness of each program and monitor its growth. Encouraging aggressive growth in the System's YBS programs is being true to our mission, but also makes good business sense for the future of Farm Credit.

I understand that 2018 was a good year for the Farm Credit Bank of Texas: over \$190.5 million in net income, modest loan growth, \$1.8 billion in capital, and — probably most impressive — 90.3% of net income paid out in patronage and dividends to your borrower-stockholders. I admire your cooperative model, treating all associations, large and small, equally for loan pricing and services. How do you grow up in agriculture, making hay and working cattle with your neighbors without possessing a strong cooperative spirit?

Again, thank you for your kind invitation. It's been a great year being the junior member of our three-member board, and I've learned a lot from my fellow board members Jeff Hall and Chairman Dallas Tonsager, as well as the FCA staff and, most importantly, the System borrowers. As the junior member, I have the distinction of having the longest length of term ahead of me, and I fully intend to make the best of it.