FARM CREDIT ADMINISTRATION

Report on the Financial Condition and Performance of the Farm Credit System

1996

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Message From the Chairman

It is my pleasure to present the 1996 report on the financial condition and performance of the Farm Credit System (System).

During 1996, System banks and associations continued a 9-year trend of improving financial condition and performance. Total loans to agricultural producers, cooperatives, and others increased by 4.4 percent to $61.2 billion, which is the second consecutive year of significant loan growth. Nonperforming loan volume continued to decline steadily, having declined by 67.8 percent from 5 years ago. Net earnings for 1996 were $1.2 billion, up 3.1 percent from 1995. This is the fourth consecutive year that earnings have exceeded $1 billion. System institutions, as cooperatives, return a portion of their income to their borrowers/owners, and in 1996 declared $271 million in patronage distributions. During the past 5 years, System capital has increased nearly 49 percent to $10.7 billion. This figure includes the $1.039 billion in the Insurance Fund managed by the Farm Credit System Insurance Corporation.

For the past 10 years, the System has undergone significant restructuring to achieve operational efficiency. Between January 1, 1993, and January 1, 1997, the number of System banks and associations declined by 31 to 225. One measure of operating efficiency is the operating expense rate—a measure of operating expenses as a percentage of total loan volume. The System's operating expense rate declined slightly in 1996 for the second year in a row to 1.39 percent.

Thanks to its strong financial health, the System continued to issue its debt at highly favorable spreads over Treasury securities. Average spreads over equivalent maturity Treasury securities were 16 basis points during 1996. Because rates in the capital markets declined, System institutions were able to reduce interest rates charged to borrowers during the year. The average interest rate on all System loans declined by 43 basis points over 1995.

Consistent with the trend of improving financial condition, CAMEL ratings—a standard measure used by financial regulators to assess an institution's condition—have improved and enforcement activity has declined. During the 12-month period ending December 31, 1996, the Agency terminated 12 enforcement actions and did not issue any cease and desist orders to System institutions.

The System continues to provide a significant number of loans to young, beginning, and small farmers and ranchers. During 1996, 18.8 percent of the number of System farm loans were made to this group of borrowers, which represented 13 percent of the System's total outstanding loan volume. During the past 3 years as farm income has strengthened, the System has had a significant increase in loans where the primary borrower is a beginning farmer. We believe that additional young, beginning, and small farmers are benefiting from System financing but can not be reflected in the data collected because the primary borrower is a parent or other senior partner.

As the regulator for the Farm Credit System, our intent in all our actions is to strengthen the System and ensure its safety and soundness and its continuing ability to finance the Agricultural Industry.

Marsha Pyle Martin
Chairman
Farm Credit Administration Board
June 30, 1997

Farm Credit Administration Organization

Farm Credit Administration

The Farm Credit Administration (FCA or Agency) is an independent agency in the executive branch of the U.S. Government responsible for regulating and examining the banks, associations, and related entities that constitute the Farm Credit System (FCS or System). Initially created by an Executive order of President Franklin D. Roosevelt in 1933, the Agency now derives its powers and authorities from the Farm Credit Act of 1971, as amended (Act). FCA promulgates regulations to implement the Act and examines FCS institutions for compliance with applicable statutes and regulations, and safe and sound banking practices. If an institution is found to be in violation of these statutes or regulations or is operating in an unsafe or unsound manner, the Agency has several enforcement options at its disposal to bring about corrective action. In addition, FCA annually examines the National Consumer Cooperative Bank and its affiliate, the NCB Development Corporation, and presents the reports of examination to the U.S. Senate Committee on Banking, Housing, and Urban Affairs and the U.S. House of Representatives Committee on Banking and Financial Services.

The Agency has its headquarters in McLean, Virginia. It has field offices at its headquarters and in Marietta, Georgia; Denver, Colorado; Dallas, Texas; Sacramento, California; St. Louis, Missouri; and Bloomington, Minnesota.[1]

Farm Credit Administration Board

Policymaking for FCA is vested in a full-time, three-person board appointed by the President with the advice and consent of the U.S. Senate. FCA Board members serve a 6-year term and may not be reappointed after serving a full term or more than 3 years of a previous member's term. The President designates one of the members as Chairman of the Board. The Chairman also serves as the Agency's chief executive officer.

Marsha Pyle Martin was appointed to the FCA Board and designated Chairman and Chief Executive Officer by President Clinton on October 17, 1994; her term expires October 13, 2000. She brings to her position 35 years of experience in agriculture and agricultural finance. A Texas native, she joined the Federal Intermediate Credit Bank (FICB) of Texas in 1970 and in 1979 earned the distinction of being the first woman appointed to a senior officer position. During her career with the FICB of Texas and the Farm Credit Bank (FCB) of Texas she gained broad management experience, providing leadership and direction for the bank's corporate relations, legal, operations and supervision, management information, human resources, marketing, and public and legislative affairs departments. She has held leadership positions with various agricultural councils and advisory committees in Texas, including the Texas Agricultural Loan Mediation Program Advisory Board, the Texas Department of Commerce Credit Advisory Committee, the Texas Agricultural Lifetime Leadership Board of Directors, and the Texas Agricultural Cooperative Council. In 1990, she received the Cooperative Communicators Association's highest honor, the H.E. Klinefelter Award, in recognition of her distinguished contributions to cooperative communications. In 1995, she was honored by the Board of Directors of the FCB of Texas as the individual who had made the greatest contribution to agriculture and farm credit in Texas and was named to the Academy of Honor in Agriculture. In 1996, she was presented the Distinguished Alumni Award by Texas Woman's University. She holds a B.A. from Texas Woman's University and an M.S. from Texas A&M University.

Doyle L. Cook was appointed to the FCA Board by the President on October 5, 1994, to a term that expires May 21, 1998. Mr. Cook also serves as Chairman of the Farm Credit System Insurance Corporation's (FCSIC) Board of

1. On April 2, 1996, FCA announced plans to close the regional offices in Denver, Colorado, and McLean, Virginia, and the field offices in Marietta, Georgia, and St. Louis, Missouri, during fiscal year 1997.

Directors. He brings to this position 34 years of experience in agricultural lending, 19 of which were with various FCS institutions. Preceding his appointment to the FCA Board, Mr. Cook served as president and chief executive officer of the FCB of Spokane, an active participant on various committees of the banks of the FCS, a director of the Federal Agricultural Mortgage Corporation (Farmer Mac), and a member of the Chicago Mercantile Exchange Lender Advisory Committee. Previously, he served as president and chief executive officer of the Farm Credit Services of Mid-America, Agricultural Credit Association (ACA); senior vice president for credit for the FICB of Texas; and senior vice president of the FICB of Louisville. He began his career with Ralston Purina, where he worked in credit, marketing, finance, and general management for 13 years before joining the FCS. Mr. Cook, a native of Star City, Arkansas, holds a B.S. in agricultural business and an M.S. in agricultural economics from the University of Arkansas.

Ann Jorgensen was appointed to the FCA Board by President Clinton on May 28, 1997, for a term that expires in May 2002. She brings to her position extensive experience in production agriculture and accounting. She started farming in partnership with her husband in 1963. Their farming operation now includes a cropping operation, Jorg-Anna Farms, and a hog operation, Timberlane Hogs Ltd. She also worked for 10 years as a tax accountant and as a licensed commodity broker for 7 years. In 1981, she started Farm Home Offices, a mail order catalog company, which markets farm management products that are designed to help farmers improve their financial and production management systems. She has served on a number of governing boards for the State of Iowa, including 6 years as a member of the Board of Regents. The Board of Regents is responsible for the state's three universities, including the University of Iowa Hospital, a world renown teaching hospital, and its affiliated clinics. She is a co-author of a producer's guide entitled *The Farmer's Guide to Total Resource Management* and is the author of a book, *Put Paperwork in its Place.* She was honored as the Outstanding Young Woman for the State of Iowa in 1976 and was inducted into the Iowa Volunteer Hall of Fame in 1989. She and her husband were recognized by *Farm Futures* magazine in 1983 as the owners of one of the Top 10 Best Managed Farms. A native of Iowa, she holds a B.A. from the University of Iowa.

Officials

David C. Lavoie[2]	Chief Operating Officer
Roland E. Smith[3]	Chief Examiner and Director, Office of Examination
Jean Noonan	General Counsel
Michael L. Young[4]	Acting Director, Office of Resources Management
Thomas G. McKenzie[5]	Director, Office of Policy Development and Risk Control[6]
Eileen M. McMahon[7]	Director, Office of Congressional and Public Affairs
Eldon W. Stoehr	Inspector General
Larry W. Edwards[8]	Director, Office of Secondary Market Oversight
Floyd J. Fithian	Secretary to the FCA Board
Gail Hill	Manager, Equal Employment Opportunity

2. David C. Lavoie retired March 31, 1997. The position of Chief Operating Officer had not been filled at publication time.
3. Roland E. Smith became Chief Examiner and Director, Office of Examination, on October 1, 1996. William L. Robertson served as Acting Chief Examiner and Director, Office of Examination, through September 30, 1996.
4. Michael L. Young was appointed Acting Director, Office of Resources Management, on March 5, 1996. He had previously served as Director, Office of Special Supervision and Corporate Affairs. Donald P. Clark was named Director, Office of Resources Management, on April 1, 1997, following the retirement of Michael L. Young.
5. Thomas G. McKenzie was appointed Director, Office of Policy Development and Risk Control, on October 1, 1996.
6. The Office of Policy Development and Risk Control was formed on October 1, 1996, as a result of merging the Office of Special Supervision and Corporate Affairs with the Regulation Development unit, formerly part of the Office of Examination.
7. Eileen M. McMahon was appointed Director, Office of Congressional and Public Affairs, on December 2, 1996. Nancy E. Lynch served as Acting Director from August 19 through December 1, 1996; Deborah A. Dawson served as Acting Director until March 21, 1996.
8. Suzanne McCrory served as Director, Office of Secondary Market Oversight, until March 1, 1996. Larry W. Edwards was appointed to this position on March 5, 1996. He had previously served as Director, Office of Resources Management.

Overview of Organizations

Farm Credit System

The Farm Credit System is a network of borrower-owned cooperative financial institutions and related service organizations that serve all 50 States and the Commonwealth of Puerto Rico. These institutions specialize in providing credit and related services to farmers, ranchers, and producers or harvesters of aquatic products. They may make loans to finance certain processing and marketing activities of these borrowers. They may also make loans to rural homeowners (for housing); certain farm-related businesses; and agricultural, aquatic, and public utility cooperatives.

On January 1, 1997, there were 225 System banks and associations, consisting of the following:

- Six Farm Credit Banks, which make direct long-term real estate loans through 60 Federal Land Bank Associations (FLBAs) and provide loan funds to 65 Production Credit Associations (PCAs), 56 Agricultural Credit Associations (ACAs), and 31 Federal Land Credit Associations (FLCAs). PCAs make short- and intermediate-term loans; ACAs make short-, intermediate-, and long-term loans; and FLCAs make long-term loans.
- One Bank for Cooperatives, which makes loans to agricultural, aquatic, and public utility cooperatives and to other persons or organizations owned by or having transactions with such cooperatives.
- One Agricultural Credit Bank (ACB), which has the combined authorities of an FCB and a BC and provides loan funds to five ACAs. In addition, both the BC and the ACB are authorized to finance U.S. agricultural exports and provide international banking services for farmer-owned cooperatives.

The following FCS entities are also examined and regulated by FCA:

- The Federal Farm Credit Banks Funding Corporation (Funding Corporation) is an entity owned by FCS banks that markets the debt securities the banks sell to raise loan funds.
- The Farm Credit System Financial Assistance Corporation was chartered in 1988 to provide capital to the System through the purchase of preferred stock issued by System institutions that received financial assistance authorized by the FCS Assistance Board.
- The Federal Agricultural Mortgage Corporation guarantees the timely payment of principal and interest on securities representing interests in, or obligations backed by, pools of agricultural real estate loans.

Service corporations organized under Section 4.25 of the Act include the following:

- The Farm Credit Finance Corporation of Puerto Rico uses tax incentives offered to investors to provide low-interest funding (other than that from the Funding Corporation) to the Puerto Rico Farm Credit, ACA.
- The Farm Credit Leasing Services Corporation provides equipment leasing services to eligible borrowers, including agricultural producers, cooperatives, and rural utilities.
- Farm Credit Financial Partners, Inc., provides support services to the associations affiliated with CoBank, ACB.
- AgCo Services Corporation provides management information systems and electronic data processing services to CoBank, ACB, and AgAmerica, FCB, and its affiliated associations.
- The FCS Building Association (FCSBA) acquires, manages, and maintains facilities to house the headquarters and field offices of FCA. The FCSBA is owned by the FCS banks, and oversight of its activities is vested in the FCA Board.

Farm Credit System Insurance Corporation

The Farm Credit System Insurance Corporation was established by the Agricultural Credit Act of 1987 as an independent U.S. Government-controlled corporation. FCSIC's purpose is to ensure the timely payment of principal and interest on insured notes, bonds, and other obligations issued on behalf of FCS banks and to act as conservator or receiver of FCS institutions. By ensuring the repayment of FCS securities to investors, FCSIC helps to maintain a dependable source of funds for farmers, ranchers, and other FCS borrowers. FCA Board members serve ex officio as the Board of Directors for FCSIC; however, the Chairman of the FCA Board may not serve as the Chairman of the FCSIC Board.

Economic and Agricultural Finance Environments[1]

The agricultural economy witnessed a year with more than the usual volatility in commodity prices, but with continued strong export demand, a low inflation rate, and low interest rates. The great uncertainty over the outcome of the farm policy debate was settled with favorable terms for producers of farm program commodities, at least for the next several years. Farmers' financial position generally strengthened as cash income in 1996 advanced significantly over 1995 levels. The financial position of agricultural lenders, including the Farm Credit System, grew stronger. Competition was strong among lenders for loan growth, with the System gradually reversing a long-term decline in market share.

General Economic Setting

The economy was very favorable during 1996. Economic growth was strong, with real gross domestic product (GDP) rising by 3.4 percent during the year. This growth was one of the larger gains of recent years, with a rate more than double that of 1995. Inflation, as measured by the Consumer Price Index, remained very low during 1996 despite the increased economic growth. The Consumer Price Index "core rate" (minus the more volatile prices for food and energy) rose only 2.6 percent during 1996, down from 3.0 percent in 1995, the lowest rate since 1965. Even with food and energy prices added in, the Consumer Price Index rose only 3.3 percent during 1996, compared with 2.5 percent in 1995. Employment rose briskly, and the unemployment rate edged down to 5.3 percent by yearend, near the lowest level of the current expansion. (Unemployment had been as high as 7.8 percent in June 1992.)

The Federal Reserve reduced the discount rate slightly from 5.25 to 5.0 percent in January 1996, but held rates steady during the remainder of the year, as strong economic growth appeared to create little inflationary pressure. Short-term rates also remained stable with 3-month Treasury rates staying near 5 percent and averaging about 50 basis points lower than during 1995. However, while longer term rates moved higher early in the year, they then declined, and 10-year Treasury securities averaged 6.4 percent for the year, only slightly below the average for 1995. Following the Federal Reserve's cut in January 1996, the prime rate stayed level at 8.25 percent. As a result of the slight decline in average rates, the Farm Credit System's average yield on its loans declined by 43 basis points to an average 1996 rate of 8.4 percent.

Federal Agriculture Improvement and Reform Act of 1996

The Federal Agricultural Improvement and Reform Act of 1996 (1996 Farm Act), signed into law on April 4, 1996, made major reforms to agricultural commodity programs by ending supply controls, delinking Government payments from production decisions and market prices, and enabling farmers to move to a more market-based system. A recent analysis published by the U.S. Department of Agriculture's (USDA's) Economic Research Service suggested some of the impacts of the 1996 Farm Act compared with continuation of previous legislation:[2]

- U.S. agriculture will likely be more price-competitive in world markets in the long run.

- Significant farm-level and regional impacts may occur as production patterns shift to reflect differences in comparative advantage for the production of specific crops.

- Dairy policy changed dramatically, phasing out dairy price supports and consolidating milk marketing orders. Net returns to the dairy sector are expected to decline as the phase-out of price supports lowers prices and production.

- Aggregate net farm income is expected to be higher than projected under previous legislation. Income support payments under the new law are higher than projected deficiency payments would have been under the previous farm law. Declines in net income for dairy and peanut producers will somewhat offset the gain from higher Government payments.

1. The information presented in this section is based on calendar year 1996.
2. Young, C. Edwin and Paul C. Westcott, "The 1996 U.S. Farm Act Increases Market Orientation," Economic Research Service, USDA, AIB-726, August 1996.

- Government payments are now fixed, so farm income could become more variable in response to supply and demand shocks. That is, because farmers' Government payments are not a function of commodity prices, farmers' incomes will be higher in high-price years and lower in low-price years. Loan rates, although capped at 1995 levels for most crops, continue to provide some income protection, but at relatively low levels.

- Farmers will consider marketing alternatives to manage risk and buffer potentially greater income volatility.

Although the new farm legislation provides greater opportunities for farmers, it also requires a higher level of management skill. Marketing and risk management capabilities will be tested in the more volatile business environment. For this reason, FCA has identified implementation of the 1996 Farm Act as having a potential for risk that warrants careful monitoring by both Agency staff and System lenders.

Commodity Developments

The year saw wild swings in grain prices, but earnings for grain producers remained strong for the year as a whole thanks to excellent crops, strong average prices, and the first payments under new farm legislation. Carryover stock levels for wheat and corn were quite low at the beginning of the year, and these conditions, combined with concerns over crop size, sent prices to May-June-July highs, only to plummet as farmers harvested a bigger than expected fall crop. The pattern was similar for soybean producers, with prices moving to 10-year highs in August and remaining at that level until early fall, when larger crop estimates caused prices to drop. Still, for 1996, soybean prices averaged 24 percent above 1995, while corn and wheat prices were 43 and 32 percent, respectively, above 1995 crop year levels. Traditional efforts to reduce financial risks in these volatile markets were often not appropriate, and many producers and their marketing cooperatives lost money as a result of hedge-to-arrive contracts.

Cattle producers were not so fortunate, as the higher prices received by grain producers caused big increases in their input costs. Drought conditions in parts of the Southwest and Southern Plains compounded the problems, and the resulting herd liquidations caused cattle prices to plunge in late spring to their lowest level of many years. However, by yearend, the cattle industry was improving as prices made a solid comeback. Pork and poultry producers (except for turkey producers) did well for the year because of increasing demand and smaller supplies than forecast. Turkey consumption was not sufficient to raise prices. Dairy producers experienced record milk receipts in 1996, although prices fell between September and December, and many producers did not enjoy record returns because of high feed costs and weather-related productivity problems.

U.S. agricultural exports had another banner year, with sales of bulk commodities the highest since 1981 and sales of value-added exports, such as meat and processed food products, at record levels. Overall agricultural export sales gained 10 percent over 1995 to almost $60 billion. Export growth is a crucial underpinning for both the crop and livestock markets and is expected to remain strong, thanks to improving incomes in developing countries, especially in Asia and Latin America, and the movement to freer world trade. The well-publicized rise in the value of the dollar during 1996 could have hurt exports, but the dollar's rise was not nearly as great relative to the currencies of the developing countries so important for U.S. agricultural exports. Another favorable factor for farm exports is farmers' ability to respond to improving world demand now that Government planting restrictions and incentives have been mostly removed.

Farmland, the major source of collateral for System loans, increased strongly in value, especially in the Midwestern States. Optimism was based on the favorable long-term outlook for agricultural exports and the fixed cash flows from "production flexibility contracts" called for in the 1996 Farm Act.

Farm Income in 1996

Farm sector income rebounded sharply in 1996 from the levels recorded the previous year. High crop prices, expanded acreage, and strong export demand resulted in a 12 percent rise in net cash income from the 1995 level to $54.6 billion (Figure 1). From 1990 to 1995, net cash income averaged $52.8 billion. Net cash income measures the cash available to service debt or substitute for additional debt.[3] Net farm income, an accrual measure of farm income, jumped 37 percent in 1996 to $47.7 billion, compared with an average of $43 billion from 1990 to 1995.[4]

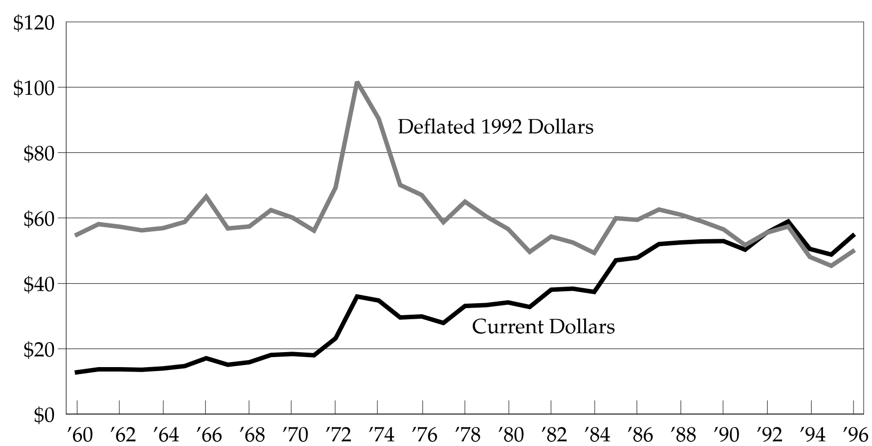
The resurgence of farm income was driven by increases in both crop and livestock receipts. Crop receipts grew more than 9 percent to $107.9 billion in 1996; livestock receipts grew 4 percent to $90.5 billion. Offsetting the growth in cash receipts was a 4.4 percent increase in production expenses. Costs of manufactured inputs such as fertilizer, fuel, and pesticides increased more than 7 percent, while costs of purchased feed jumped about 10 percent. Total interest expenses rose just 2 percent in 1996, as farm sector debt grew and interest rates on farm loans declined relative to 1995. Total interest expenses declined slightly as a percentage of total production expenses, to 7.1 percent.

Direct Government payments were $7.3 billion in 1996, about the same as the previous year. Government payments to farmers in 1996 were largely a "bonus" that resulted from the 1996 Farm Act. Because of the high prices received by crop producers in 1996, Government payments would have been just a fraction of the $7.3 billion paid had the previous legislation been in force. Hence, the fixed transition payments mandated by the 1996 Farm Act resulted in billions of dollars of additional income for farmers, leading to a booming farmland market in the Midwest, soaring farm machinery sales, and continued growth in farm debt.

Farm Sector Financial Ratios in 1996

Since the mid-1980s, the financial condition of farmers as a group has improved markedly. The level of farm debt outstanding fell precipitously from its peak of $194 billion in 1984 to $138 billion in 1989. (Farm debt has recovered to more than $155 billion as of December 31, 1996.) The value of farm assets has stabilized since 1986 after falling more than 20 percent during the first half of the 1980s. Farm sector asset values have risen at more or less the rate of inflation since the late 1980s. However, in the past few years, debt use has picked up and

Figure 1
Net Cash Income from Farming, 1960–1996
(Dollars in Billions)



Note: Data for 1996 are forecasts.
Source: USDA, Economic Research Service: National Financial Summary-1993, ECIFS 13-1, December 1994, and Agricultural Outlook AO-239, April 1997.

3. Net cash income is a cash accounting of commodity sales, Government payments, farm-related income, and operating expenses associated with producing that revenue. Neither depreciation nor capital expenditures are deducted.
4. Net farm income is an accounting of farm income and expenses on an accrual basis. Thus, net farm income has adjustments for inventory changes (to reflect only the current year's output), depreciation as an expense, and recognition of other noncash income and expense items. Overall, income tends to be more stable when expressed on a cash basis, because it partly measures how farmers manage to average their sales and expenses from more than one production year.

growth in farmland prices has accelerated, rising faster than debt. The result has been declining debt-to-asset ratios and, recently, rising measures of the debt burden when expressed in terms of income and interest expense.

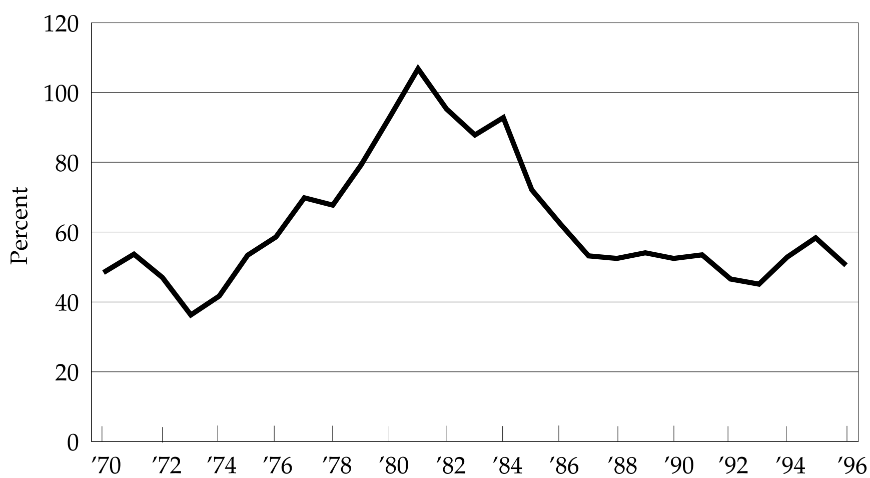
Financial leverage can have a positive effect on farm earnings when commodity prices are high and revenues are strong. However, leverage is a double-edged sword. When revenues decline, farmers with higher financial leverage generally experience a greater decline in earnings than those who employ a more conservative financial management strategy. Consequently, with the resurgence of farm debt growth, we can expect more volatile farm earnings for a given change in gross farm income. Despite the positive financial performance of the farming sector in 1996, prudence dictates that trends in the various measures of farmers' debt burden be monitored carefully.

The strong income generated by farmers in 1996 pushed various financial ratios to healthier levels. This generally healthier financial environment is evidenced by improvements in farmers' use of their credit capacity, the interest coverage ratio, and the debt-to-asset ratio.

Farmers' use of credit capacity is based on current outstanding debt compared with the debt level that could be serviced with current net cash income before interest. In 1981, credit capacity utilization peaked at about 106 percent, meaning that farmers, as a group, exceeded their ability to service debt out of net cash income. The high debt burden that this measure illustrates led to the financial shakeout in agriculture that continued throughout much of the 1980s. Clearly, any upward trend in farmers' use of credit capacity should be viewed as an early signal of potential financial difficulties in the farm sector. In 1996, farmers' use of credit capacity dipped to 51 percent from 58.4 percent in 1995 (Figure 2). This improvement followed 2 years of increases in this debt burden indicator. According to USDA's Economic Research Service, larger commercial farms, as measured by farm sales, have used about a fourth of their total debt repayment capacity. Small and moderate-size commercial farms, however, have tended to use one-half to two-thirds of their debt capacity.[5]

The interest coverage ratio (net cash income before interest divided by interest) is a measure of the earnings available to service interest expenses. The higher the value, the greater the coverage and the lower the debt servicing burden, all else being equal. After declining for several years, farm sector interest expenses have risen from \$10.8 billion in 1993 to about \$13 billion in 1996. This recent trend has helped to push down the interest coverage ratio from 6.4 in 1993 to 4.8 in 1995. The strong farm income recorded in 1996 led to an improved interest coverage ratio of 5.2 in spite of continued growth in interest charges.

Figure 2
Use of Farmers' Credit Capacity



Notes: Use of credit capacity is computed as the ratio of actual debt to debt repayment capacity. Capacity is based on the debt level that could be serviced with current net cash income before interest. Data for 1996 is a forecast.
Source: USDA, Economic Research Service, unpublished data.

5. USDA, Economic Research Service, Web site, Debt Repayment Quick Tour Reading Room.

The farm sector debt-to-asset ratio, a measure of financial solvency, also improved in 1996, dropping from 15.4 percent in 1995 to a more favorable 15 percent. The value of total farm sector assets grew 5.8 percent compared with a growth rate of just 3.1 percent for farm debt.

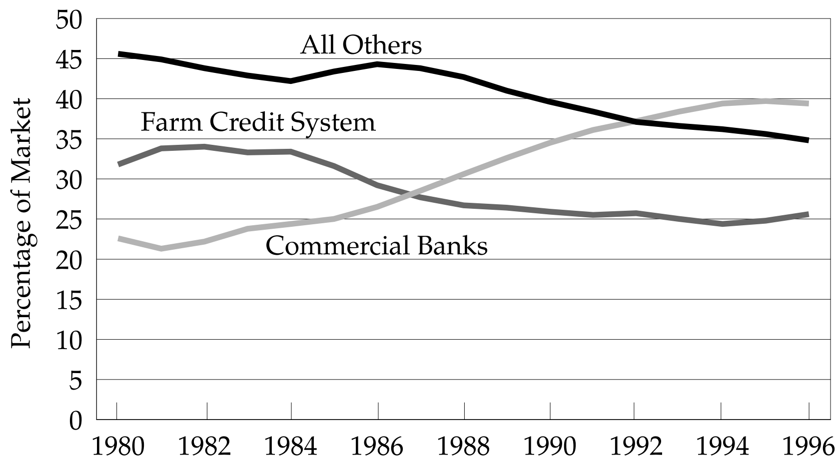
Farm Debt Markets and Lender Shares[6]

By the end of 1996, the Farm Credit Banks and their affiliated associations, as well as those affiliated with CoBank, ACB, had completed 2 years of significant growth, their first since 1982. More notably, this growth was sufficient to reverse the long-term decline in the System's share of farm business debt that lasted 12 years (1983–1994). During 1996, the FCS accounted for 54 percent of the estimated $4.7 billion increase in farm lending, compared with 25 percent by commercial banks, the other major lender to agriculture. By the end of 1996, USDA estimates that the System's market share of total farm business debt outstanding had increased slightly to 25.6 percent, compared with a low of 24.4 percent in 1994 and a high of 34 percent at the end of 1982 (Figure 3). It is interesting to note that the 1994 low was higher than the debt share held by the System during the 1960s. Commercial banks, with a 39.4 percent market share by the end of 1996, continued to hold the largest share of total farm business debt. However, their share during 1996 trended downward after having increased for 14 years, from 21.3 percent at the end of 1981 to a peak of 39.8 percent at the end of 1995.

Figure 3

Total Farm Business Debt, Market Shares 1980–1996

(As of December 31)



Notes: "All Others" includes trade credit, seller financing of real estate, life insurance companies, USDA's Farm Service Agency, and Farmer Mac. Data for 1996 are preliminary estimates.
Source: USDA, Economic Research Service: Agricultural Income and Finance Situation and Outlook Report, AIS-64, February 1997.

Among all agricultural lenders, farm business debt grew 3.1 percent during 1996, to $155.5 billion. Total farm business debt reached a high of $193.8 billion in 1984, fell to $137.9 billion in 1989, and has been gradually increasing only during the past 4 years. During 1996, growth rates of about 3.1 percent in both the real estate-secured portion and the non-real estate portion brought outstanding real estate debt to $81.8 billion and non-real estate debt to $73.7 billion. The similar growth rates in real estate debt and non-real estate debt reversed a trend of recent years in which real estate debt had lagged behind.

6. Market share data provided here does not include loans to farmers made through credit affiliates of agricultural cooperatives that are funded by System institutions.

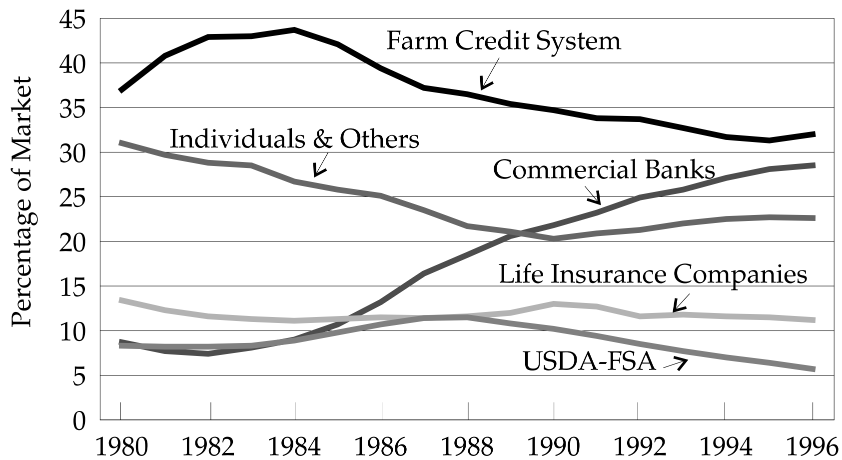
The FCS has been, and continues to be, the dominant lender for farm real estate loans, while commercial banks continue to be the dominant lender in the non-real estate area. However, in recent years, commercial banks have gained market share in both areas, reaching all-time highs in 1996 for real estate debt and in 1994 for non-real estate debt.

For the System, 1996 growth in real estate debt outstanding was 5.2 percent, higher than in any of the past 12 years. This growth brought the System's share up slightly, to 32.0 percent, and reversed the decline that had been continuous since the peak of 43.7 percent in 1984 (Figure 4). System non-real estate debt grew by 10.1 percent in 1996. The System's non-real estate market share has been gradually increasing, from a low of 14.2 percent at the end of 1988 to 18.6 percent in 1996 (Figure 5).

Commercial bank market share of real estate-secured loans increased almost fourfold during 1982 to 1996, rising continuously from 7.4 percent to 28.5 percent. Bank share of non-real estate debt has been increasing since the end of 1987, reaching a high of 53.1 percent at the end of 1994. By 1996 yearend, the share had declined to 51.4 percent.

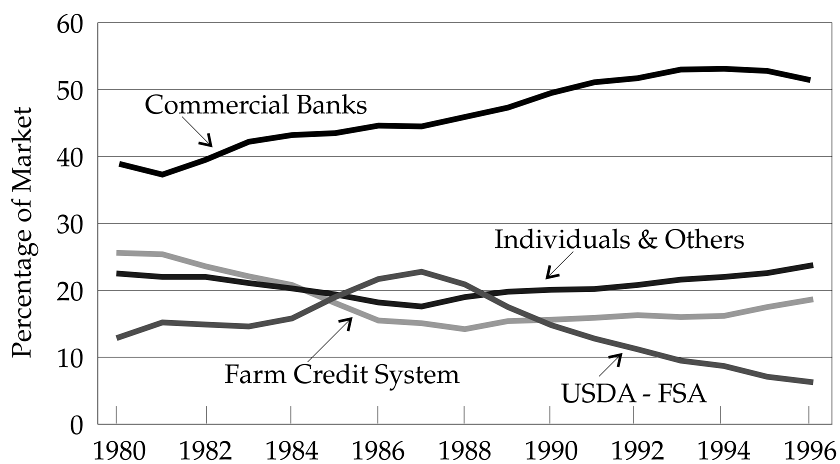
Both System and commercial bank share in the farm non-real estate area is probably slightly higher than USDA data show because of "point-of-sale" credit provided by farm input or equipment

Figure 4
Real Estate Farm Business Debt, Market Shares 1980–1996
(As of December 31)



Notes: "Individuals and Others" is mainly credit and seller financing of real estate, but also includes Farmer Mac loans. USDA-FSA is the USDA's Farm Service Agency. Data for 1996 are preliminary estimates.
Source: USDA, Economic Research Service: Agricultural Income and Finance Situation and Outlook Report, AIS-64, February 1997.

Figure 5
Non-real Estate Farm Business Debt, Market Shares 1980–1996
(As of December 31)



Notes: "Individuals and Others" is mainly trade credit. USDA-FSA is the USDA's Farm Service Agency. Data for 1996 are preliminary estimates.
Source: USDA, Economic Research Service: Agricultural Income and Finance Situation and Outlook Report, AIS-64, February 1997.

suppliers. Often this credit is funded through line-of-credit arrangements with System institutions or commercial banks.

Other institutional lenders to farmers include insurance companies and USDA's Farm Service Agency (FSA). While only six insurance companies are now active in farm lending, these companies were very active in the farm real estate market in 1996. Insurance companies emphasize larger loans (more than $500,000) and have held about 11 to 12 percent of the farm real estate-secured debt since the early 1980s, or about 6 to 7 percent of overall farm debt. FSA, the "Government lender of last resort," reached a high in both real estate and non-real estate lending during 1986 to 1988. This lending continued to decline through 1996 to an overall farm debt share of only 6.0 percent. The decline reflects the intentional shift in the FSA's direct lending programs to guarantees of loans made by other lenders, with guaranteed loans showing up on the books of both commercial bank and FCS lenders. The category "individuals and others" constitutes the remaining group of farm debt holders and mostly represents seller financing for real estate and trade credit. The percentage held by this category was 23.1 at the end of 1996.

The strong growth rates for the System during the past 2 years have come at a time when the System has rebuilt its financial strength following the agricultural financial crisis of the mid- to late 1980s. System lenders can now serve their chartered markets with more competitive interest rates and more aggressive marketing efforts. In addition, many System lenders are changing their credit delivery systems, with greater emphasis on expanding customer relationships for large, complex loans and more efficient means of credit delivery for smaller loans (generally under $100,000). However, these changes also come at a time when commercial banks, in spite of rising loan-to-deposit ratios, continue to have the liquidity to be strong competitors in the farm lending arena. Insurance companies are also competing actively for the larger credits. In addition, trade (or "point-of-sale") credit, while not as accurately measured as other farm debt, appears to be experiencing strong growth. The result has been continued strong competition in farm lending markets for creditworthy borrowers. The same is expected for 1997.

Potential Risks in the Farm Finance Outlook

As a safety and soundness regulator, the Farm Credit Administration acts to protect the customers/shareholders of FCS lending institutions and investors in FCS debt securities. Through its regulatory, enforcement, and examination functions, FCA monitors and helps control the risks to these stakeholders. In carrying out these functions, the Agency has identified several risks that bear watching over the next few years. Five of these risks are discussed briefly below.

Land Price Surge—High crop prices combined with generous Government payments have fueled the farmland market in the Midwest. The Chicago Federal Reserve Bank reported that, in 1996, the value of good farmland rose 10 percent in its district (Illinois, Indiana, Iowa, Michigan, and Wisconsin). In Indiana, however, farmland prices jumped 15 percent during that period. Some forecasters expect land values to drop after the 1996 Farm Act expires in 2002. Indeed, because farmland is generally illiquid and suitable for only a single purpose, the uncertainty that currently characterizes the income stream of farmers is reflected in the value of agriculture's most important asset, farmland. Sound underwriting standards call for real estate loans to be supported by reasonable expectations for the income stream that will be used to service the loans. The risk is that underwriting standards may not adequately focus on repayment capacity from current or future income.

Highly Competitive Markets and System Loan Growth—System loan volume has grown in the past 2 years. Fifty-eight associations experienced loan growth in excess of 10 percent during 1996. Overall, System loans to the farming sector grew 6.8 percent in 1996, a healthy increase. Now, market share trends that for a decade favored commercial banks have begun to reverse. At the same time, nontraditional lenders such as input suppliers (e.g., John Deere and Pioneer Hi-Bred) have been developing a more competitive presence in the farm credit marketplace. Although farm lending conditions have been quite good because of relatively strong income and rising farmland prices, rapid growth in a competitive environment can raise concerns regarding the underlying credit quality of loans. Even though FCA has found no systemic evidence of credit quality problems, vigilance is called for on the part of the Agency.

Implementation of New Farm Legislation—The 1996 Farm Act ushered in a new era in farm policy. The Government has reduced its involvement in the agricultural sector, making farming and farm lending riskier businesses. The 1996 Farm Act has removed supply controls for program commodities and allows nearly complete planting flexibility. These changes will result in greater year-to-year commodity price volatility and greater variability in farm income, making debt repayment capacity more uncertain over time. Underwriting standards need to take these factors into consideration. There will be strong competition to gain and retain lending relations with well-managed producers who are financially able to withstand the increased risks. Over time, the credit quality of less well managed producers is likely to deteriorate. Transition payments mandated by the 1996 Farm Act have contributed to a boom in the farm economy and may lead to greater economic activity throughout the course of the 1996 Farm Act. Lending decisions based on this policy-induced environment may result in serious credit problems if farm policy were to change abruptly when the 1996 Farm Act expires in 2002.

New Risk Control Devices for Farmers—A riskier environment resulting from the reduced Government role in agriculture will lead farmers to seek new ways to control risks to their farm income, and lenders need to understand how these techniques can reduce loan portfolio risk. Such risk-control devices include commodity price hedging contracts, yield futures, and revenue or crop yield insurance that could lead to unexpected risks if not properly understood and implemented. For example, forward contracting a specified number of bushels of corn at a specific price can be a way to manage price risk. However, if a harvest falls short of expectations and prices rise relative to the contract price, a producer might have to enter the market to purchase corn at the prevailing market price and deliver it to cover an obligation at the lower price. Fortunately, USDA's Risk Management Agency has insurance programs designed to protect farmers from this kind of risk. Hedge-to-arrive contracts that led to significant credit problems in 1996 offer a perfect example of how a risk management or marketing tool might expose both the borrower and the lender to unexpected risks. In a riskier environment, we can expect both public and private sources to develop new risk management tools. It is critical that both farmers and lenders fully understand these tools and use them effectively to protect themselves from unforeseen financial risks.

High-Concentration Portfolios—Stress in association lending portfolios with high concentrations in single or related commodities could lead to deterioration of certain System institutions. Many FCS institutions have high concentrations of borrowers producing commodities under Government support programs. Some FCS institutions also have high concentrations in cattle, dairy, or other single commodities, such as corn, citrus, or grapes. For example, at the end of 1996, 12 FCS institutions had portfolio concentrations in corn in excess of 30 percent, representing more than $3 billion in loans. Twenty-five institutions had at least a 30 percent concentration in dairy lending, representing more than $2 billion in loans. There are FCS institutions with concentrations in single commodities as high as 86 percent. The Agency is concerned about commodity concentration risk because borrower repayment capacity could deteriorate as a result of the phasing out of Government support programs or adverse market developments, such as declines in export markets, that could affect several institutions simultaneously.

Farm Credit System Performance Report [1,2]

During 1996, Farm Credit System banks and associations continued a 9-year trend of improving financial condition and performance. Earnings were more than $1 billion for the fourth straight year. In the past 5 years, System capital has increased nearly 49 percent. Nonperforming loan volume continues to decline steadily and is 32 percent of what it was 5 years ago. The System's ability to absorb risk continues to increase as capital grows, primarily through retained earnings.

Earnings

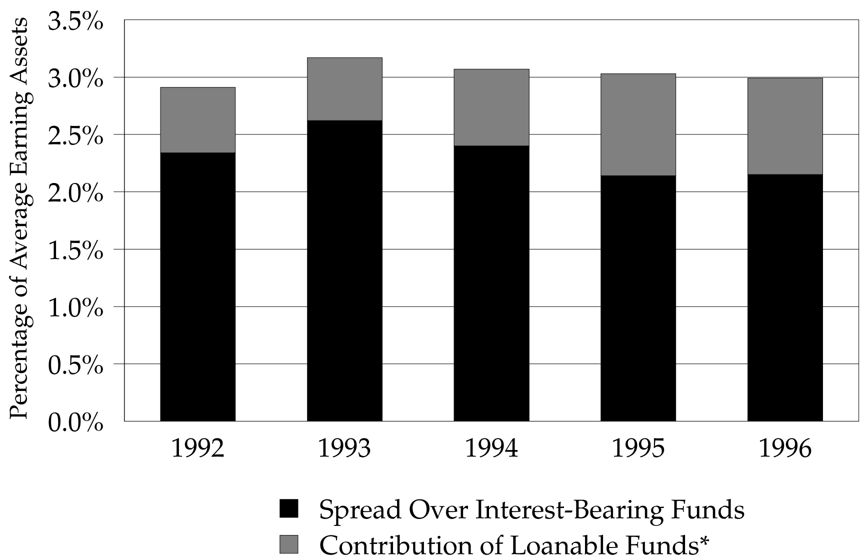
Net earnings for 1996 were $1.2 billion, up 3.1 percent from 1995 earnings. Reasons for the increase included greater loan volume, gains on other property owned, and no reported costs associated with mergers and restructuring in 1996. These positive influences were offset by an increase in the provision for income taxes.

Net interest income was up 6.9 percent over 1995, to nearly $2.2 billion. Net interest income increased because of higher loan volumes, partially funded by an increase in loanable funds.[3] The net interest margins fell slightly from 3.03 percent of average earning assets in 1995 to 2.99 percent in 1996 (Figure 6), because of a lower yield on earning assets. The net interest spread[4] increased 1 basis point[5] to 2.15 percent.

Results for individual banks and their affiliated associations were mixed. The AgFirst, AgriBank, Texas, and Wichita districts increased their net income from 1995. The largest increase in net income was in the Texas District (184 percent), and the largest decrease was at the St. Paul Bank for Cooperatives (50 percent). The AgFirst, Texas, and Western districts and the St. Paul BC increased their net interest margins,[6] while the AgAmerica, AgriBank, Wichita, and CoBank districts all saw a decline in their net interest margins. Systemwide, the return on assets for the 12 months ended December 31, 1996, was 1.63 percent, compared with 1.74 percent for the 12 months ended December 31, 1995.

Operating expenses for 1996 totaled $846 million, a 3.2 percent increase from 1995. Salaries and employee benefits, the largest

Figure 6
Net Interest Margins, 1992–1996

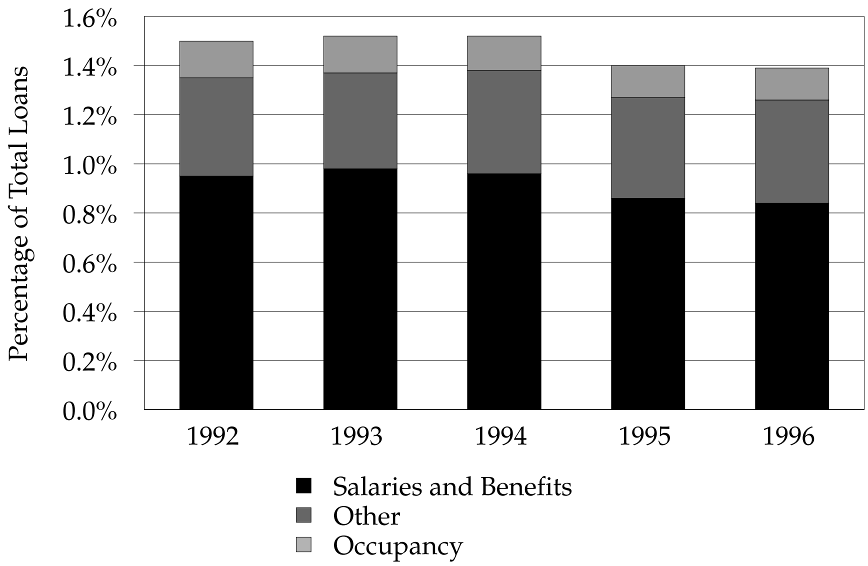


*Loanable funds are owned (interest-free) funds that support interest-earned assets.
Source: Federal Farm Credit Banks Funding Corporation Annual Information Statements.

1. The material on the Farm Credit System, Farmer Mac, and the Farm Credit Insurance Fund section is based on calendar year 1996.
2. The information presented in this section includes all Farm Credit Banks and the Agricultural Credit Bank and their affiliated associations and the Bank for Cooperatives. References to individual districts include financial data for the district bank and its affiliated associations, adjusted to eliminate transactions between institutions in the district. Separate analysis of Farmer Mac, the Farm Credit Leasing Services Corporation, and the Farm Credit Insurance Fund follow. The data used in the overall FCS analysis were provided by the FCS institutions to the Federal Farm Credit Banks Funding Corporation, are based on publicly available information, and have been adjusted to eliminate transactions between FCS institutions.
3. Loanable funds are the excess of interest-earning assets after subtracting interest-bearing liabilities.
4. Net interest spread is the difference between the interest rate charged to borrowers and the interest rate paid by the institution.
5. A basis point is one-hundredth of 1 percent.
6. Net interest margin is the ratio of net interest income to average earning assets.

portion of expenses, increased only 1.8 percent. Occupancy and equipment expenses were virtually unchanged. AgFirst, Texas, and CoBank districts experienced declines in operating expenses (1.0, 0.3, and 2.6 percent, respectively). For the third year, the System has reduced its operating expense rate (operating expense as a percentage of total loans), thanks in part to the larger loan portfolio. The operating expense rate improved from 1.4 percent in 1995 to 1.38 percent in 1996 (Figure 7). All Farm Credit Banks showed decreases in their operating expense rate (all less than 10 basis points), while both CoBank and the St. Paul BC showed an increase of 1 basis point each.

Figure 7
Operating Expenses as a Percentage of Loans, 1992–1996



Source: Federal Farm Credit Banks Funding Corporation Annual Information Statements.

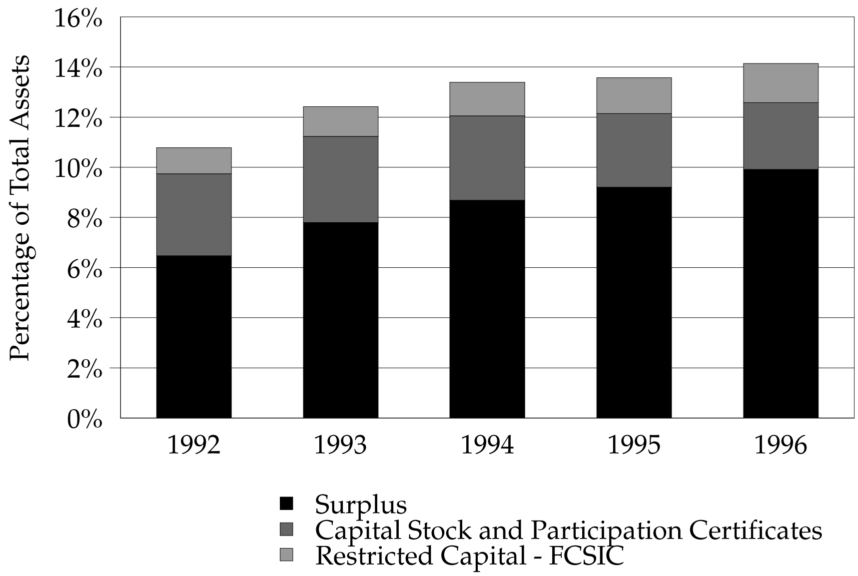
In 1996, the System added $141 million to the allowance for loan losses, $105 million more than in 1995. All districts and the St. Paul BC added provisions to the allowance account. While the banks were responding to an increase in loan volume and the inherent risk associated with the increase, several recognized the potential risk in certain commodities prevalent in their territories. These risks resulted from the effect of higher grain prices on cooperatives' grain marketing and related hedging contracts, higher input costs relative to returns anticipated in some livestock enterprises, higher grain costs to food processors, the effects of adverse weather, and other economic stresses.

Offsetting increases to net income included a $37 million increase in the provision for income taxes, to $174 million. Since System institutions are cooperatives, they can offset some of their tax liability by declaring patronage distributions, thus returning a portion of their income to the borrowers/owners. In 1996, the System declared $271 million in patronage distributions, of which $83 million is to be paid in cash. Of the remaining $188 million in declared patronage, $118 million was transferred to allocated surplus, and the remaining $70 million was declared as capital stock.

Capital

As the System generates and retains earnings, total capital continues to grow.[7] During 1996, total capital grew 8.8 percent, to $10.7 billion. Capital rose from 13.8 percent of total assets at yearend 1995 to 14.3 percent at yearend 1996 (Figure 8). Surplus increased 13 percent and comprises 69 percent of total capital compared with 67 percent at the end of 1995. Also contributing to capital was a $6 million net unrealized gain on investments available for sale versus a $7 million net unrealized gain at yearend 1995. Nonperforming loans were 8.6 percent of total capital, compared with 11.7 percent at yearend 1995.

Figure 8
Farm Credit System Capital as a Percentage of Total Assets, 1992–1996
(As of December 31)



Note: Protected stock is not included since it represents a small (1.2 percent) percentage of total capital at yearend 1996.
Source: Federal Farm Credit Banks Funding Corporation Annual Information Statements.

As of yearend 1996, all System institutions were in compliance with FCA's minimum capital requirements. The Agency requires each institution to maintain a minimum 7 percent permanent capital to risk-adjusted assets ratio. Permanent capital to risk-adjusted assets in FCS institutions range from 9.3 percent to 50.0 percent.

Assets

Total assets increased 4.9 percent over yearend 1995 to $74.9 billion. The System's investment portfolio, up 7.5 percent from a year ago to $11.8 billion, contributed to the increase. Systemwide, 45 percent of the investment portfolio consists of mortgage-backed securities, 14 percent of prime commercial paper, 12 percent of Federal Funds, and 29 percent of various other types of investments. Total investment portfolios of System banks averaged just under 20 percent of average loans, well under the 30 percent regulatory maximum. Total loans of $61.2 billion, which constitute 82 percent of assets, increased 4.4 percent (Table 1). The largest increase came in production and intermediate-term loans, up $1.4 billion, a 10.6 percent increase over 1995. This gain was due to increased production borrowings by farmers, competitive loan pricing, and improved marketing

7. Total capital includes protected capital and restricted capital. Protected capital ($131 million at yearend 1996) consists of borrower stock, participation certificates, and allocated equities that were outstanding as of January 6, 1988, or were issued or allocated before October 8, 1988. Protection of certain borrower capital is provided under the Farm Credit Act of 1971, as amended, which requires FCS institutions, when retiring protected borrower capital, to retire such capital at par or stated value regardless of its book value. Restricted capital ($1.17 billion at yearend 1996) represents the total assets under the control of the Farm Credit System Insurance Corporation including those which have been identified for estimated insurance obligations ($0.13 billion) and the Insurance Fund equity ($1.04 billion). See following section on the Insurance Fund.

Table 1
Farm Credit System Loan Volume, 1992-1996
(Dollars in Millions)

Loan Category	1992	1993	1994	1995	1996	Percentage Change from 1992
Long-Term Real Estate	$26,907	$26,461	$26,440	$26,635	$27,556	2.4
Production and Intermediate-Term	10,398	10,979	11,648	13,255	14,659	41.0
Domestic Cooperatives	6,474	7,604	7,700	10,390	9,954	53.8
International Loans	3,892	3,739	3,202	2,759	2,623	(32.6)
Rural Utilities	2,265	2,468	2,927	3,208	3,890	71.7
Rural Home	1,772	1,737	1,680	1,628	1,584	(10.6)
Other	699	921	1,079	714	912	30.5
Total	**$52,407**	**$53,909**	**$54,676**	**$58,589**	**$61,178**	**16.7**

Source: Federal Farm Credit Banks Funding Corporation Annual Information Statements.

efforts. The System also saw an increase of $682 million (21.3 percent) in loans to rural utilities and a $921 million (3.5 percent) increase in long-term real estate lending. Although the long-term loan portfolio has increased 2.4 percent over the past 4 years, the proportion of long-term farm mortgages to total volume fell from 51.3 percent at yearend 1992 to 45.0 percent at yearend 1996.

All Farm Credit Banks contributed to the rise in 1996 loan volume. The largest increases were in the Wichita District (13.1 percent), in part because of reaffiliation of an association from the Texas District, and in the AgriBank District (11.9 percent). Both CoBank and the St. Paul BC saw decreased loan volumes in 1996.

Asset Quality

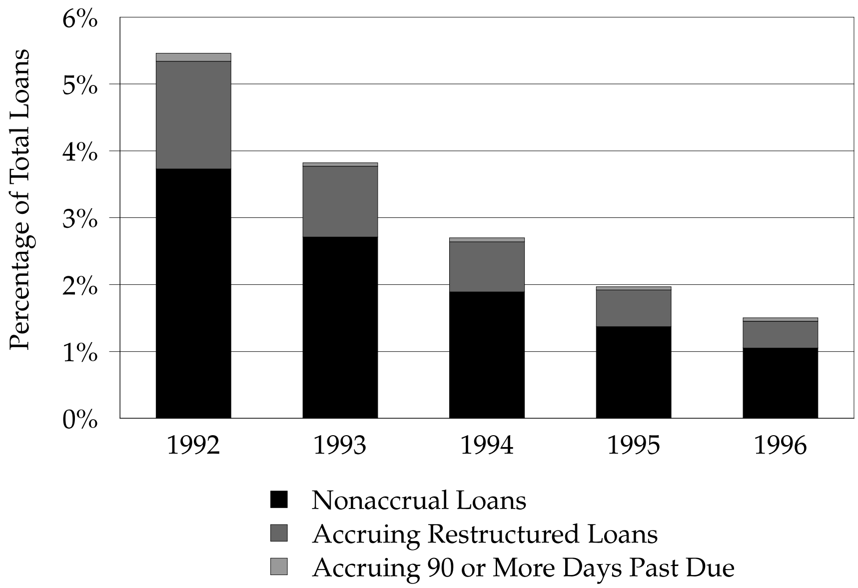
Loan quality continued to improve. Nonperforming loans[8] fell $231 million (20 percent) from 1995 balances to $919 million at yearend 1996. Nonperforming loans now represent 1.5 percent of the portfolio, compared with 2.0 percent at yearend 1995 and 5.5 percent at yearend 1992 (Figure 9). Nonaccrual loans dropped 19.5 percent over the year to $645 million. Of these loans, 61 percent are current as to principal and interest payments.[9] All Farm Credit districts reduced nonperforming loans during 1996. Nonperforming loans in the St. Paul BC increased $19.8 million during 1996. Much of this increase was due to increased exposure associated with hedge-to-arrive contracts. Loan delinquencies (accruing loans 30 or more days past due) as a percentage of accrual loans remained at a relatively low level (less than 1 percent), but increased slightly from 1995.

The System's allowance for loan losses was up slightly from yearend 1995 in relation to the loan portfolio, from 2.86 percent to 2.89 percent at yearend 1996. The allowance is nearly 275 percent of the amount of nonaccrual loans, compared with 209 percent in 1995. Nonaccrual loans are the loans posing the greatest risk of loss to the System.

Figure 9

Nonperforming Loans in the Farm Credit System, 1992–1996

(As of December 31)



Source: Federal Farm Credit Banks Funding Corporation Annual Information Statements.

8. Nonperforming loans consist of nonaccrual loans, accruing restructured loans, and accruing loans 90 days or more past due.
9. FCA regulation 621.6(a) states: "A loan shall be considered nonaccrual if it meets any of the following conditions: (1) collection of any amount of outstanding principal and all past and future interest accruals, considered over the full term of the asset, is not expected; (2) any portion of the loan has been charged off, except in cases where the prior chargeoff was taken as part of a formal restructuring of the loan; or (3) the loan is 90 days past due and is not both adequately secured and in process of collection."

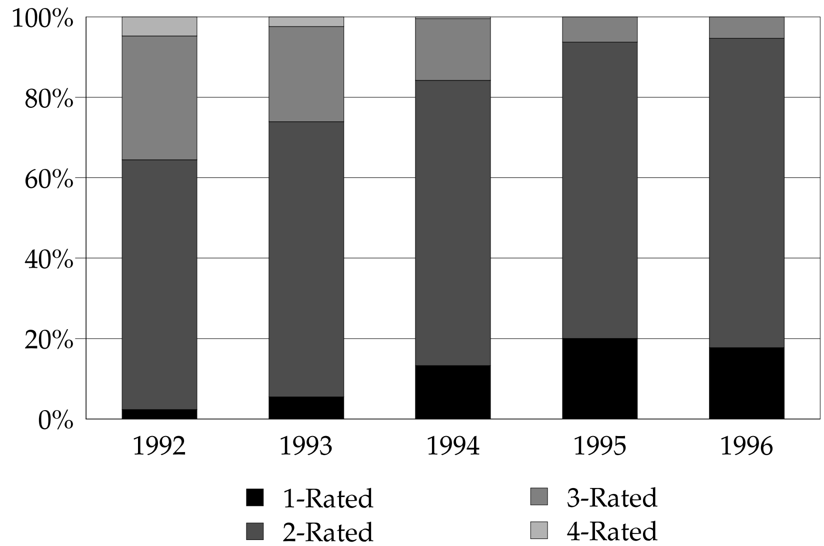
CAMEL Ratings

The overall improvement in the financial performance and condition of the FCS continues to be evident in the CAMEL (capital, asset quality, management, earnings, and liquidity) ratings given as a result of FCA's examinations. At yearend 1996, there were no 4- or 5-rated institutions (Figure 10). The percentage of 3-rated institutions has dropped from 30.8 percent at yearend 1992 to 5.3 percent at yearend 1996.

Figure 10

CAMEL Ratings for Farm Credit Banks and Associations

(As of December 31)



Notes: CAMEL ratings are based on capital, asset quality, management, earnings, and liquidity. Ratings range from 1 (a sound institution) to 5 (an institution that is likely to fail).
Source: FCA Examination Reports.

Enforcement Activity

Consistent with this trend of improving financial conditions, enforcement activity has declined. FCA may use its various enforcement authorities to ensure that FCS institution operations are safe and sound and in compliance with applicable statutes and regulations. These authorities include the power to execute agreements or issue orders to cease and desist, to levy civil money penalties, to remove officers and directors of FCS institutions, and to establish financial and operating reporting requirements.

During the 12-month period ended December 31, 1996, the Agency did not enter into any agreements with or issue orders to cease and desist to FCS institutions. The Agency issued five supervisory letters and three follow-up letters to institutions operating under existing enforcement actions.

Improving financial and credit conditions, coupled with satisfactory compliance with enforcement actions, resulted in the Agency's termination of 12 enforcement actions or follow-up letters during 1996. At yearend 1995, eight FCS institutions with aggregate assets of $8.3 billion were under some form of enforcement action. At yearend 1996, only six institutions with $941 million in assets were under enforcement action.

Farm Credit Leasing Services Corporation

The Farm Credit Leasing Services Corporation (Leasing Corporation) is a service corporation owned and funded by the Farm Credit System banks. The Leasing Corporation's headquarters are in Minneapolis, Minnesota, and sales offices are located throughout the United States. It specializes in equipment leasing to agricultural producers and their cooperatives, rural electric and telephone organizations, and FCS entities. Funds required by the Leasing Corporation to originate leases are advanced by its owners.[10] The Leasing Corporation was chartered in 1983, and in 1984 acquired the net assets of Interregional Service Corporation.

Since 1984, Leasing Corporation business volume and profitability have increased steadily. Industry press stated that the Leasing Corporation had the 6th largest lease portfolio among independent U.S. lessors and was the 51st largest U.S. lessor overall. At the end of its fiscal year in September 1996, the Leasing Corporation had more than 31,000 contracts outstanding to more than 8,200 customers. The Leasing Corporation's return on equity has been more than 10 percent since 1989 and was 15.6 percent for 1996. Net earnings of $8.2 million were higher than 1995's $7.1 million due primarily to a 17.6 percent increase in rental revenue on an increased volume of operating leases. The Leasing Corporation's capital-to-asset ratio was 9.6 percent at the end of its 1996 fiscal year and declined to 8.8 percent at December 31, 1996, after a dividend.

Business volume increased sharply. Total assets were up 16.1 percent to $616.3 million from the end of the 1995 fiscal year. Lease placements were up 24.2 percent to $415 million, another record. Approximately $191 million of the placements were with cooperatives and $224 million were with agricultural producers. The majority of these placements, $295 million, were added to the Leasing Corporation's lease portfolio and the rest, $120 million, were syndicated with FCS banks, associations, and others. The lease portfolio consisted of agricultural equipment (43 percent), manufacturing and material handling equipment (14 percent), automobiles and light trucks (13 percent), trucks (12 percent), irrigation equipment (8 percent), and other (10 percent). The portfolio was split between agricultural producers (60.5 percent) and cooperatives (39.5 percent).

Asset quality declined slightly during fiscal year 1996. Nonaccrual leases were $9.6 million at 1996 fiscal yearend, up from $4.8 million the year before. The allowance for doubtful lease collections as a percentage of outstanding leases was unchanged at 1.8 percent.

Farmer Mac

The Farm Credit System Reform Act of 1996 (1996 Act) made several important changes to Farmer Mac's charter that allowed it to act as a pooler, purchase qualified loans, issue securities backed by those loans without a subordinated reserve, and eliminate the diversification requirement from its underwriting standards. The 1996 Act also raised the statutory capital requirements but delayed full implementation of those requirements for an additional 3 years. Risk-based capital regulations were also delayed until 1999. The new statute provided FCA authority to appoint a receiver if Farmer Mac were unable to continue operations in a safe and sound manner. The 1996 Act also provided that loans made by System institutions and designated for sale into the secondary market at the time the loans are made are not subject to borrower rights. The effect of these statutory changes is to give Farmer Mac expanded business authorities, relaxed operating requirements, and 3 additional years before full capital requirements become effective.

10. The owners of the Leasing Corporation are the Farm Credit banks that obtain their funds from the sale of Systemwide obligations and from surplus.

Farmer Mac operates two programs. In Farmer Mac I, pools of agricultural real estate loans are formed,[11] securities backed by those loans are created, and Farmer Mac provides a guarantee of timely payment of principal and interest to security holders. With the new authorities provided by the 1996 Act, Farmer Mac opened a "cash window" in 1996 for the purchase of qualified loans directly from lenders. In Farmer Mac II, lenders sell guaranteed portions of Farm Service Agency or Rural Economic and Community Development loans to Farmer Mac, which pools the guaranteed portions of those loans and creates securities backed by guarantees of timely payment of principal and interest.

Farmer Mac generated income on loans held for securitization and on capital gains when those loans were securitized. These new income streams and increased income from guarantee fees and Farmer Mac securities held in portfolio produced $393,000 of after-tax income. Farmer Mac also earned $384,000 on the early retirement of debt to bring net income for the year to $777,000, a $1.4 million improvement over 1995's $647,000 loss.

Farmer Mac expenses increased in 1996 by $1.3 million to $5.1 million in response to the new business opportunities provided by the 1996 Act. Although there were increases in most areas, the largest increases were $433,000 in salary and related expenses, primarily because 5 new staff members were added, bringing the total to 21, and $416,000 in professional fees.[12]

Capital increased in 1996 by $35.5 million to $47.2 million, the first increase since Farmer Mac began operations in 1989. The increase was due to the sale of approximately $35 million in new stock (mostly Class C nonvoting) in 1996 and earnings of $777,000. The yearend capital substantially exceeded the amount that would have been required had the new 1999 statutory minimum capital standards been in effect in 1996 rather than delayed for 3 years. Most of the new stock issued was purchased by one commercial bank and by institutional investment funds. As of yearend, one commercial bank owned 20 percent of all voting stock.

From business inception through 1996, Farmer Mac guaranteed approximately $897 million of Farmer Mac I securities; $420 million in principal balance was still outstanding at yearend, of which Farmer Mac held $206 million. From business inception through 1996, Farmer Mac issued and guaranteed approximately $278 million of Farmer Mac II securities; $211 million in principal balance was still outstanding at yearend, of which Farmer Mac held $199 million. These retained securities provided a substantial portion of Farmer Mac's interest income. In 1996, Farmer Mac used its revised charter to issue $149 million in Farmer Mac I securities. It also issued $93 million in Farmer Mac II securities.

Farmer Mac increased its holdings of other investment securities from $65.6 million at yearend 1995 to $85.8 million at yearend 1996. The increase was due primarily to the purchase of floating rate mortgage-backed securities issued by U.S. Government instrumentalities.

Of the loans underlying Farmer Mac I securities, 0.7 percent of the aggregate principal amount of the loans was either past due 90 days or more, in foreclosure, or in acquired property. This figure was up slightly from the 0.5 percent reported at yearend 1995. Because all troubled loans were in pools backed by a 10 percent subordinated interest, none of the loans were deemed likely to result in a loss to Farmer Mac. The new loans purchased by Farmer Mac do not have the subordinated interest attached, and their default rates are unknown.

The 1996 Act removed commodity and geographic diversification requirements. Despite this, Farmer Mac's geographic diversification improved slightly and its commodity diversification remained about the same when compared with 1995. Approximately half of the loans underlying Farmer Mac I securities originated in the Pacific Coast

11. Rural housing loans are also permissible, but none were pooled in 1996.
12. Had Farmer Mac elected to record expenses for employee stock compensation awards per Statement of Financial Accounting Standards (SFAS) 123, net income would have been reduced $140,000 to $637,000.

region, and concentration in this region increased in 1996. Concentrations in most other areas of the country decreased. Approximately 30 percent of the loans underlying Farmer Mac I securities were used for permanent plantings, and concentration in this type of loan increased in 1996. In general, both geographic and commodity concentrations were higher for loan pools backing Farmer Mac I securities sold and guaranteed than for those backing Farmer Mac I securities retained by Farmer Mac. Median loan-to-value ratios for loan pools backing Farmer Mac I securities guaranteed and sold to investors increased materially from the low 40 percent range in 1995 to the low 50 percent range for 1996. Median loan-to-value ratios for loan pools backing Farmer Mac I securities retained by Farmer Mac declined slightly from the high 50 percent range in 1995 to the low 50 percent range in 1996.

Farm Credit Insurance Fund

The Farm Credit System Insurance Corporation manages the Insurance Fund in carrying out its mission of protecting investors. The Insurance Fund balance at yearend 1996 was $1.039 billion, an increase of $137 million (15 percent) from 1995. The increased fund balance resulted from premiums of $86 million and interest income of $61 million, less operating expenses of $1.5 million and a provision for estimated insurance obligations of $8.5 million. FCSIC's total assets were $1.169 billion. Its total liabilities included a $130 million liability for the present value of FCSIC's obligation to provide for future repayment of assistance provided to the Federal Land Bank of Jackson in Receivership and $275,000 in accounts payable and accrued expenses.

Funding the Farm Credit System

Farm Credit System banks obtain most of their loan funds through the sale of debt securities. Securities outstanding include: Federal Farm Credit Banks Systemwide Bonds, discount notes, medium-term notes (MTNs); the Federal Farm Credit Banks Global Debt Program, and Federal Farm Credit Banks Consolidated Bank Debt Securities. Under the Farm Credit Act of 1971, as amended, all Systemwide debt issuances are subject to approval of the Farm Credit Administration. Pursuant to authorizations by FCA, the maximum amount of discount notes, MTNs, and global debt securities that the banks may have outstanding at any one time is $25 billion, $40 billion, and $5 billion, respectively. Although Systemwide bond issues are individually approved by FCA, there are no specific limits on the amount of Systemwide bonds that can be outstanding.

The debt securities are not obligations of, nor are they guaranteed by, the United States or any agency or instrumentality thereof, other than the Farm Credit System banks. The debt securities are the joint and several obligations of the Agricultural Credit Bank, Farm Credit Banks, and the Bank for Cooperatives, and are backed by their combined resources and insured by the Farm Credit System Insurance Corporation. Certain other bonds issued directly by certain individual banks are the obligations solely of the issuing bank.

The Farm Credit Act and FCA regulations require each bank to maintain specified eligible assets at least equal in value to the total amount of debt securities outstanding for which it is primarily liable as a condition for participation in the issuance of Systemwide debt securities. As of December 31, 1996, the combined Farm Credit banks reported eligible assets of approximately $67.3 billion and debt securities and accrued interest payable of $61.7 billion at that date. For the comparable period a year ago, the combined Farm Credit banks reported $64.4 billion in eligible assets and $59.1 billion in debt securities and accrued interest payable at December 31, 1995.

Funding activities are handled by the Federal Farm Credit Banks Funding Corporation, which offers securities to the public through a selling group of approximately 70 investment dealers and dealer banks. During 1996, competitive pressures in the brokerage industry provided the Funding Corporation the opportunity to also use an auction process to sell 1-year bonds at more favorable issuance costs as compared with use of the selling group. Average spreads for all Systemwide debt issuances during 1996 were 16 basis points above comparable Treasuries, a slight decline from 1995. In 1996, FCA approved the Funding Corporation's request to establish a $5 billion Global Debt Program, which is targeted to reach new investors in the overseas pool funds as well as to lower funding costs as opportunities arise. In the fourth quarter of 1996, the System entered the international debt capital market for the first time, with an inaugural $500 million issue denominated in U.S. dollars.

Debt securities outstanding at yearend 1996 totaled $61.1 billion as compared with $58.5 billion at yearend 1995 (Table 2). The increase was used mainly to fund loan growth. Bonds and discount notes outstanding declined slightly while MTNs increased. Total issuances of Systemwide debt securities were a record $261.3 billion in 1996, as compared with $242.7 billion in 1995 (Table 3). The bulk of the System's debt issuance continued to be in the form of discount

Table 2

Farm Credit System Debt Outstanding as of December 31, 1996, and December 31, 1995

(Dollars in Millions)

	As of December 31, 1996			As of December 31, 1995		
	Outstanding Balance	Average Rate[1] (Percent)	Remaining Maturity[2] (Months)	Outstanding Balance	Average Rate[1] (Percent)	Remaining Maturity[2] (Months)
Bonds[3]	$20,127	5.73	7.3	$21,004	6.08	10.8
Medium-Term Notes	27,309[4]	5.91	28.8	22,321	5.99	25.2
Discount Notes	13,648	5.52	1.9	15,194	5.71	1.5
Total	$61,084	5.76	15.7	$58,519	5.95	13.9

1. Data in this column are the average rate of the outstanding balance.
2. Data in this column are the remaining maturity in months for the outstanding balance.
3. Includes Systemwide bonds, consolidated bank debt securities, and other bonds issued by individual banks ($18.8 billion, $0.4 billion, and $0.9 billion outstanding at December 31, 1996, respectively; and $19.7 billion, $0.7 billion, and $0.6 billion outstanding at December 31, 1995, respectively).
4. Includes $0.5 billion of global debt securities issued during 1996 and outstanding at December 31, 1996.

notes, with $209.5 billion issued. Approximately 88 percent of discount notes issued were concentrated in maturities of less than 60 days.

Moderate growth and low inflation combined with one 25-basis-point decrease in interest rates by the Federal Reserve (the discount rate was reduced from 5.25 percent to 5.0 percent on January 31, 1996) left interest rates on System debt in 1996 averaging slightly lower than in 1995. The average interest rate on total outstanding Systemwide debt securities at December 31, 1996, was 5.76 percent, a decline of 19 basis points from the previous yearend. The remaining maturity of Systemwide debt securities at December 31, 1996, was 15.7 months (1.3 years) as compared with 13.9 months (1.2 years) at the previous yearend. The remaining maturity of MTNs and discount notes extended by 3.6 months and 0.4 months, respectively, while the remaining maturity of Systemwide bonds shortened by 3.5 months.

The System's use of MTNs continued to increase in 1996. MTNs outstanding at December 31, 1996, totaled $27.3 billion as compared with $22.3 billion at yearend 1995. MTNs offer System banks more flexibility than bonds because they can include structured features, and the issue and settlement dates, as well as repricing characteristics, of MTNs can be negotiated to better manage cash flows. MTNs are often swapped to achieve the debt characteristics desired by the individual System banks. Because MTNs can have more complex structures, they are issued in higher minimum denominations ($100,000) than bonds ($1,000).

Table 3

Farm Credit System Debt, 1992–1996

(Dollars in Millions)

Year[1]	Rate[1] (Percent)	Spread[1, 2] (Basis Points)	New Issues (Dollars)
Discount Note Issues			
1992	3.61	N/A	119,942
1993	3.15	N/A	126,392
1994	4.48	N/A	148,370
1995	5.76	N/A	198,459
1996	5.25	N/A	209,523
3-Month Issues			
1992	3.61	7	16,150
1993	3.13	4	15,195
1994	4.37	11	14,890
1995	5.86	17	16,534
1996	5.30	14	19,938
6-Month Issues			
1992	3.73	4	8,749
1993	3.25	2	8,100
1994	4.71	7	7,830
1995	6.02	8	5,944
1996	5.35	6	5,194
Medium-Term Notes			
1992	5.69	16 [3]	5,536
1993	5.07	19 [3]	6,903
1994	6.11	20 [3]	5,205
1995	6.53	32 [3]	13,001
1996	6.29	34 [3]	17,953
Global Debt Issues			
1996	6.44	39	0.5
All Term Debt Issues			
1992	4.56	10	7,068
1993	3.66	5	6,670
1994	5.10	9	8,519
1995	5.93	6	6,261
1996	5.53	(1)	6,937
All Debt Issues			
1992	3.70	8	161,301
1993	3.18	5	164,933
1994	4.54	11	185,835
1995	5.80	16.5	242,702
1996	5.31	16	261,304

Note: N/A=Not applicable.

1. Averages for the year.
2. Spread means the number of basis points above comparable U.S. Treasury rates.
3. Does not include floating rate notes.

Source: Farm Credit System Annual Information Statement and Farm Credit System Funding Corporation Annual Report.

Corporate Activity

During calendar year 1996, the FCA Board approved 10 corporate applications, including 4 mergers; the reaffiliation of 1 Production Credit Association from the Texas District to the Wichita District; and 5 charter amendments for association name changes, headquarters relocations, and territory changes. Mergers of Federal Land Bank Associations in the Texas District accounted for 3 of the 4 mergers that occurred in 1996. The remaining merger occurred in the Western District.

In November 1996, the Western Farm Credit Bank, located in Sacramento, California, and AgAmerica, FCB, headquartered in Spokane, Washington, announced plans to pursue joint management. The joint management became effective March 1, 1997, and is expected to reduce the costs of the banks' wholesale operations. AgAmerica, FCB obtained FCA's approval to relocate its headquarters office to Sacramento, site of the banks' joint operations. As a result of the Farm Credit System Reform Act of 1996, FCA and stockholders of Farm Credit System institutions no longer approve joint management agreements between System institutions.

In 1996, the FCA Board adopted a policy to allow unlike associations whose territories are not identical to submit merger proposals to FCA for consideration when such mergers promote efficiencies, result in viable financial institutions, and have minimal adverse effect on other FCS institutions. In adopting the new policy, FCA recognizes that permitting only mergers of unlike associations with identical territory would limit the potential for achieving additional structural efficiencies at the association level. Should a nonexclusive charter be issued under this policy, the FCA Board would consider applications from affected associations to convert to an Agricultural Credit Association or to propose an alternative acceptable to FCA.

Prior to adoption of the policy referenced above, FCA generally had not permitted the merger of unlike associations whose territories were not identical, except for several ACAs formed as a result of Section 411 of the Agricultural Credit Act of 1987. FCA took this position to protect exclusive charters, discourage intra-System competition, and prevent the administrative difficulties caused by charters that would have authorized different lending authorities in different parts of an ACA's territory (bifurcated charter).

During 1996, the FCA Board approved the merger of a PCA and a Federal Land Credit Association in the Western District to form an ACA under the new policy. The charter issued to the newly formed ACA includes portions of territory served by an adjoining PCA (in the south) and FLCA (in the north). Each of these affected associations is jointly managed with a separate FLCA and PCA, respectively (the companion associations). The companion associations were permitted to expand their territories to match their borders with the territories of the affected associations. The result was that each of the jointly managed associations now has congruent territories with small portions of their territories overlapping the newly formed ACA's territory. Consequently, there is competition between the ACA and the jointly managed associations in those overlapping areas.

Table 4 illustrates the bank and association structure in each Farm Credit district. Table 5 provides a 5-year trend in the number of banks and associations. Figure 11 depicts the chartered territories of Farm Credit System banks.

Table 4
Farm Credit System Banks and Associations[1]
(As of January 1, 1997)

Bank Affiliation	PCAs	FLBAs	ACAs	FLCAs	ACB	FCBs	BC	Total
CoBank[2]	0	0	5	0	1	0	0	6
AgFirst	1	0	39	0	0	1	0	41
AgriBank, FCB	19	0	11	19	0	1	0	50
FCB of Wichita	18	22	0	0	0	1	0	41
FCB of Texas	16	38	0	0	0	1	0	55
Western FCB	10	0	5	11	0	1	0	27
AgAmerica, FCB	1	0	1	1	0	1	0	4
St. Paul BC[3]	0	0	0	0	0	0	1	1
1/1/97 Total	65	60	61	31	1	6	1	225
1/1/96 Total	66	70	60	32	1	6	1	236
Increase/(Decrease)	(1)	(10)	1	(1)	0	0	0	(11)

1. PCA=Production Credit Association; FLBA=Federal Land Bank Association; ACA=Agricultural Credit Association; FLCA=Federal Land Credit Association; ACB=Agricultural Credit Bank; FCB=Farm Credit Bank; BC=Bank for Cooperatives.
2. CoBank, ACB has authority to serve cooperatives nationwide and ACAs in CoBank's Northeast Region.
3. The St. Paul BC serves cooperatives nationwide.

Table 5
Five-Year Trend in Numbers of Farm Credit Banks and Associations
(As of January 1)

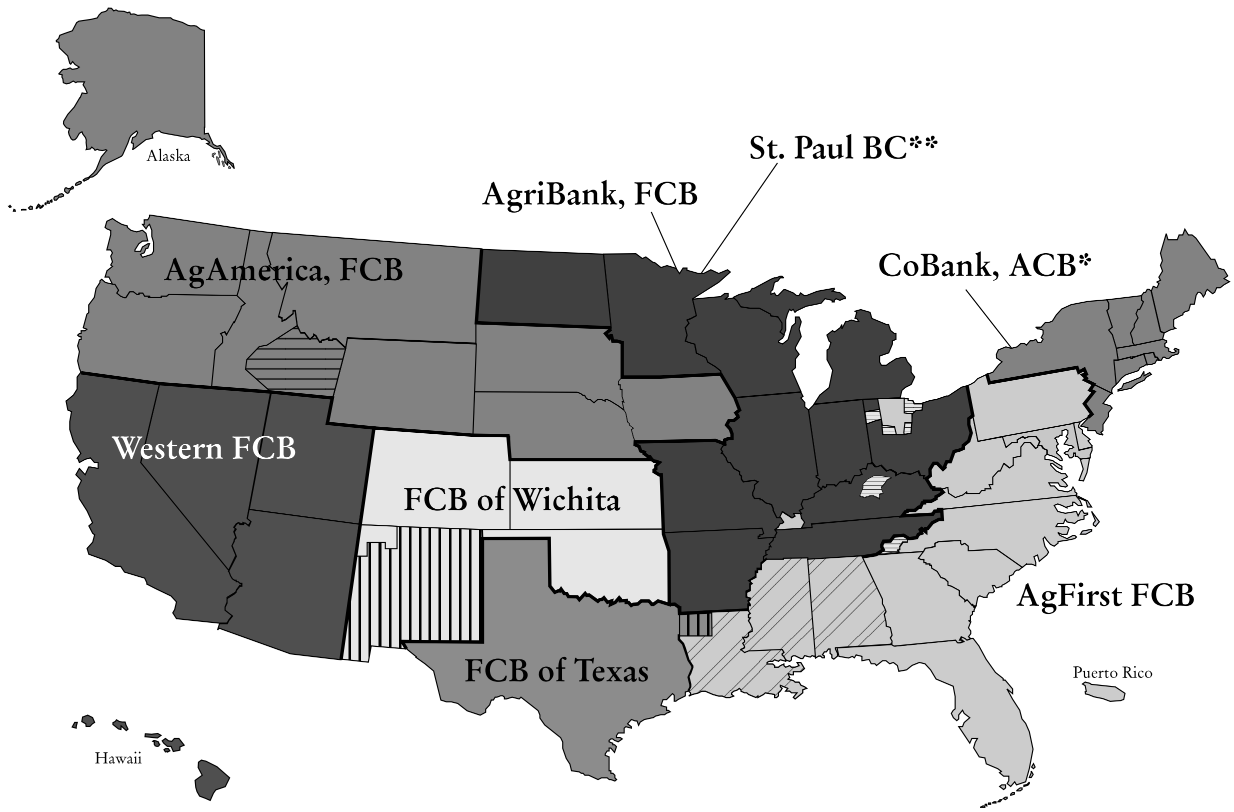
Year	PCAs	FLBAs	ACAs	FLCAs	ACB	FCBs	BCs	Total
1997	65	60	61	31	1	6	1	225
1996	66	70	60	32	1	6	1	236
1995	69	71	60	32	1	7	1	241
1994	69	73	66	30	0	9	3	250
1993	70	77	69	27	0	10	3	256[1]

1. This number does not include the Federal Intermediate Credit Bank of Jackson, which merged into the Farm Credit Bank of Columbia on October 1, 1993.

Figure 11

Chartered Territories of Farm Credit System Banks

(As of January 1, 1997)



AgAmerica, FCB	Western FCB	FCB of Wichita	FCB of Texas	AgriBank, FCB	CoBank, ACB	AgFirst FCB
1 ACA	5 ACAs	22 FLBAs	38 FLBAs	11 ACAs	5 ACAs	39 ACAs
1 FLCA	11 FLCAs	18 PCAs	16 PCAs	19 FLCAs		1 PCA
1 PCA	10 PCAs			19 PCAs		

The Albuquerque and Eastern New Mexico PCAs are funded by the FCB of Texas. The Southern New Mexico PCA is funded by the FCB of Wichita.

The FLBAs in Alabama, Louisiana, and Mississippi generate and service loans for the FCB of Texas. The First South PCA is funded by AgFirst FCB.

The Northwest Louisiana PCA is funded by the FCB of Texas.

*The CoBank, ACB serves cooperatives nationwide and ACAs in the indicated area.

**The St. Paul BC also serves cooperatives nationwide.

The AG CREDIT, ACA (Ohio), Central Kentucky ACA (Kentucky), Chattanooga ACA (Tennessee), and Jackson Purchase ACA (Kentucky) are funded by the AgFirst FCB.

The Mid-America ACA, funded by AgriBank, FCB, is also authorized to lend in this territory.

The Eastern Idaho ACA is funded by the Western FCB.

Young, Beginning, and Small Farmers[1]

The Farm Credit Administration is required by the Farm Credit Act to report annually to Congress on special programs developed by the Farm Credit System to serve young, beginning, and small farmers and ranchers. Since 1982, FCA has provided Congress summary statistics in such reports as well as an overview of the kinds of programs offered.

This 1996 report includes both highlights for 1996 and a summary comparison for the 1988–1996 period. Data for earlier years are not directly comparable, because the definition of "small farm" was made more restrictive in 1988.[2] Some comparisons are made with the 1992 Agricultural Census, which provides approximate benchmarks.

Definition of Young, Beginning, and Small Farmers

Information is reported for five different classifications of loans:[3] (1) all System loans for farming purposes, which provides a second benchmark, and four different categories[4] of loans to young, beginning, and small farmers (YBS). The four mutually exclusive YBS categories are (2) loans to young farmers, where the primary borrower's age is under 35; (3) loans to beginning farmers, those who have less than 6 years of farming experience; (4) loans to small farmers, those with annual gross sales less than $40,000 and assets less than $100,000; and (5) loans to young, beginning, and small farmers, defined as those satisfying at least two of the three criteria in (2), (3), and (4). The fifth classification is the most restrictive.

For each of the YBS categories, a loan is included only if the primary borrower meets the eligibility criteria. An unknown number of farmers who themselves would meet one or more of the eligibility criteria are nevertheless excluded from the data, because the primary borrower on the loan is ineligible for any YBS category. This would normally occur with multi-operator farms, including multigeneration partnerships and family corporations. To this extent, the reported data understate the number of YBS farmers who benefit from FCS financing.

1996 FCS Lending to Young, Beginning, and Small Farmers[5]

The FCS had 593,850 total loans outstanding under its farm lending authorities[6] at the end of 1996 for an aggregate amount of $44.1 billion. This total represents 2,305 more loans than a year earlier and an increase in amount of $2.28 billion (Table 6).

The four YBS categories accounted for a combined total of 111,599 loans for a total of $5.7 billion and an average loan size of $51,416 (Table 7). This portfolio represented 18.79 percent of all FCS loans and 13.0 percent of loan

1. Throughout this section reference is made to young, beginning, and small farmers. These classifications of borrowers also include ranchers and producers or harvesters of aquatic products.
2. For the entire period, two criteria were used to classify small farms. The sales criterion stayed constant at gross agricultural sales less than $40,000. Before 1988, the second criterion was a net worth of $100,000 or less. In 1988, the criterion was changed to farm assets of less than $100,000, which is a more restrictive standard.
3. FCS data are for loans, rather than number of persons who are borrowers, and are summarized for all the types of banks and associations that have retail farm mortgage or operating loans. Data are from special reports filed annually with FCA by the Farm Credit banks.
4. It is unclear whether Congress intended for young, beginning, and small farmers to be a single classification or three separate classifications. This analysis permits either to be used.
5. Some of the previously published annual data have been restated to include subsequent adjustments reported to FCA (see Table 6).
6. Data include all loans made under Titles I and II of the Farm Credit Act, but exclude loans to cooperatives under Title III. As of September 30, 1996, this farm loan portfolio was for the following primary loan purposes: agricultural real estate, 62.1 percent; agricultural non-real estate, 30.8 percent; rural housing, 3.6 percent; processing and marketing, 0.7 percent; farm-related business, 0.6 percent; aquatic, 0.2 percent; and unclassified, 2.0 percent.

Table 6
Farm Credit System Young, Beginning, and Small Farmer Loans: Number and Dollar Volume for All FCS Institutions, 1988–1996

	Young Farmers[1]		Beginning Farmers[1]		Small Farmers[1]		Young, Beginning, and Small Farmers[1]		All Farm Loans[2]	
Year	Number of Loans	Amount Outstanding ($ thousands)	Number of Loans	Amount Outstanding ($ thousands)	Number of Loans	Amount Outstanding ($ thousands)	Number of Loans	Amount Outstanding ($ thousands)	Number of Loans	Amount Outstanding ($ thousands)
Totals, All Farm Credit System Institutions										
1988	43,579	1,965,226	32,199	1,876,435	80,427	1,623,621	29,821	737,903	656,278	40,826,979
1989[3]	41,988	2,062,363	20,374	1,459,598	73,231	1,769,099	23,703	690,395	618,999	39,829,801
1990	35,790	1,755,960	20,332	1,566,324	68,672	1,559,395	23,796	787,109	598,895	39,675,459
1991	32,778	1,832,000	15,376	1,431,672	60,349	1,406,119	23,012	807,631	611,457	39,368,851
1992	31,735	1,872,308	13,926	1,450,559	68,296	2,076,059	23,940	910,741	609,030	40,288,982
1993	32,640	1,884,482	12,831	1,396,963	59,028	1,080,281	21,250	820,433	609,835	39,880,735
1994[3]	27,974	1,598,979	13,860	1,505,462	45,331	1,077,901	16,506	760,179	590,913	41,312,760
1995[3]	29,713	1,727,405	16,629	1,784,870	40,842	950,721	22,335	868,115	591,545	41,835,541
1996	27,647	1,672,811	22,405	2,207,263	39,152	943,672	22,395	914,273	593,850	44,113,932
Percentages										
1988	6.64	4.81	4.91	4.60	12.26	3.98	4.54	1.81	N/A	N/A
1989	6.78	5.18	3.29	3.66	11.83	4.44	3.83	1.73	N/A	N/A
1990	5.98	4.43	3.39	3.95	11.47	3.93	3.97	1.98	N/A	N/A
1991	5.36	4.65	2.51	3.64	9.87	3.57	3.76	2.05	N/A	N/A
1992	5.21	4.65	2.29	3.60	11.21	5.15	3.93	2.26	N/A	N/A
1993	5.35	4.73	2.10	3.50	9.68	2.71	3.48	2.06	N/A	N/A
1994[3]	4.73	3.87	2.35	3.64	7.67	2.61	2.79	1.84	N/A	N/A
1995[3]	5.02	4.13	2.81	4.27	6.90	2.27	3.78	2.08	N/A	N/A
1996	4.66	3.79	3.77	5.00	6.59	2.14	3.77	2.07	N/A	N/A

1. Classifications are based on the following standards. The four categories are mutually exclusive.
   Young farmer: Less than 35 years old.
   Beginning farmer: Less than 6 years of farming experience.
   Small farmer: Farming assets less than $100,000 and gross agricultural sales less than $40,000.
   Young, beginning, and small farmers: All borrowers meeting at least two of the three standards.
2. Includes all farm loans made by the Farm Credit System, the majority of which are not to young, beginning, or small farmers.
3. Some of the previously published annual data have been restated to include subsequent adjustments reported to FCA.

N/A = Not applicable.

volume outstanding. Borrowers meeting the most restrictive standard for YBS farmers, Category 5, had 3.77 percent of the number of loans and 2.07 percent of the dollar amount (Table 8).[7] The number of loans to Category 5 borrowers (young, beginning, and small farmers) totaled 22,395 for an aggregate amount of $914 million. Both amounts and percentages were virtually identical to 1995. The percentage of number of loans going to YBS farmers ranged up to 6.59 for Category 4 borrowers (small farmers), which had 39,152 loans. The percentage of total loan dollar amounts to YBS farmers varied according to the definition used, from 2.07 to 5.0 percent. The largest loan amounts were to Category 3 borrowers (beginning farmers) and equaled $2.2 billion (Table 7).

Table 7

1996 FCS Number of Loans and Loan Volume Outstanding by Type of Borrower

Borrower Group	Number of Loans	Dollar Amount (in thousands)	Average Size (Dollars)
All Farmers	593,850	$44,113,932	$74,285
Young Farmers	27,647	1,672,811	60,506
Beginning Farmers	22,405	2,207,263	98,516
Small Farmers	39,152	943,672	24,103
Young, Beginning, and Small Farmers	22,395	914,273	40,825
Subtotal – All YBS Farmers	111,599	$5,738,019	$51,416[1]

1. Average loan size for all young, beginning, and small farmer borrowers.
Source: Annual Young, Beginning, and Small Farmers Reports submitted by Farm Credit banks.

Table 8

1996 Percentage of Total FCS Number of Loans and Loan Volume Outstanding by Young, Beginning, and Small Farmer Borrower Groups

Borrower Group	Percentage of Number	Percentage of Dollar Amount
Young Farmers	4.66	3.79
Beginning Farmers	3.77	5.00
Small Farmers	6.59	2.14
Young, Beginning, and Small Farmers	3.77	2.07
Total – All YBS Farmers	18.79	13.00

Note: The data do not total 100 because FCS borrowers who do not qualify for inclusion in one of the YBS categories are not included.
Source: Annual Young, Beginning, and Small Farmers Reports submitted by Farm Credit banks.

7. The 1992 Agricultural Census found that 4.1 percent of all farmers are young and have operating debt, while 3.6 percent are young and have real estate debt. However, number of loans is not directly comparable with number of farm operators.

YBS Farmers by Association Type in 1996

The following tables break out activity by three types of lending associations: Production Credit Associations, which provide nonmortgage or operating and intermediate-term loans only; Federal Land Bank Associations and Federal Land Credit Associations combined, which provide or service mortgage loans on real estate; and Agricultural Credit Associations, which provide all types of loans. Table 9 summarizes the number of loans outstanding by type of borrower; Table 10 describes loan volume outstanding by type of borrower.

PCAs have the largest percentage of number of loans outstanding for young farmers (7.0 percent). FLBAs/FLCAs have the lowest percentage of number of loans to young, beginning, and small farmers (1.29 percent). This distribution is due to the fact that leasing land rather than purchasing it using mortgage credit lowers the capital threshold required to enter farming, and thus lessens the need for mortgage financing. Therefore, a higher percentage of YBS farmers can be expected to use operating or intermediate-term credit provided by PCAs instead of mortgage credit provided by FLBAs and FLCAs.

ACAs serve a significantly higher percentage of the number of small farmers than do the other association types (10.2 percent outstanding), perhaps because ACAs predominate in the areas of the United States that have more nonfarm rural industry and more part-time farmers. ACAs also serve a slightly higher share of loan volume to beginning farmers and young, beginning, and small farmers (5.45 percent and 2.89 percent, respectively). PCA share of loan volume to young farmers is the largest of any institution type, 5.21 percent (Table 10).

Table 9
1996 FCS Percentage of Total Number of Loans Outstanding to Young, Beginning, and/or Small Farmers, by Institution Type
(As of December 31, 1996)

Borrower Group	PCA (Percentage)	ACA (Percentage)	FLBA/FLCA (Percentage)
Young Farmers	7.00	5.27	2.35
Beginning Farmers	4.15	3.97	3.23
Small Farmers	3.43	10.20	2.32
Young, Beginning, and Small Farmers	4.51	5.02	1.29

Source: Annual Young, Beginning, and Small Farmers Reports submitted by Farm Credit banks.

Table 10
1996 FCS Percentage of Total Loan Volume Outstanding to Young, Beginning, and/or Small Farmers, by Institution Type
(As of December 31, 1996)

Borrower Group	PCA (Percentage)	ACA (Percentage)	FLBA/FLCA (Percentage)
Young Farmers	5.21	4.50	2.44
Beginning Farmers	4.46	5.45	4.66
Small Farmers	1.65	3.32	0.89
Young, Beginning, and Small Farmers	2.22	2.89	1.04

Source: Annual Young, Beginning, and Small Farmers Reports submitted by Farm Credit banks.

Trends in FCS Lending to Young, Beginning, and Small Farmers, 1988–1996

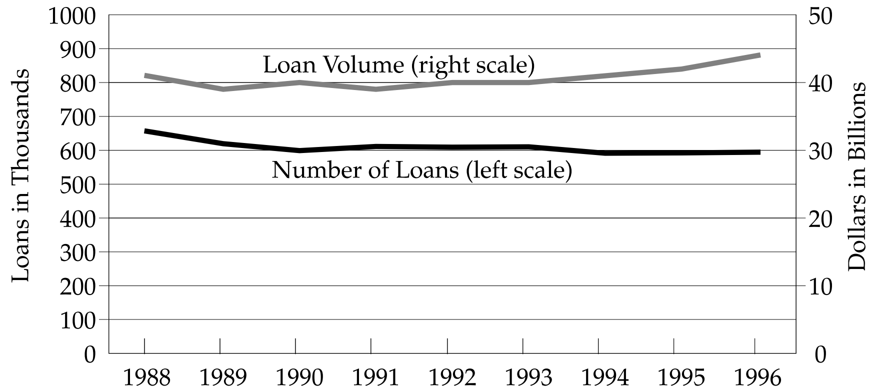
Compared with 1988, the total number of System loans outstanding to farm borrowers has dropped by 62,428 (9.5 percent) to 593,850, but loan volume outstanding is up from $40.8 billion to $44.1 billion. However, both the number of loans and loan volume outstanding increased from 1995 to 1996. Figure 12 illustrates these trends.

The same downward trend from 1988 to 1996 holds for number of loans in each category of YBS farmers, but trends in loan volume differ among categories. Loan numbers were down in all YBS categories, especially small farmers.[8] Loan volume in the small and young farmers categories was also down, 42 percent for small farmers and 15 percent for young farmers. But loan volume was up substantially for beginning farmers (18 percent) and for YBS farmers (24 percent). Most of these gains occurred in 1996. These trends are shown in Figures 13 through 16, which trace the number of loans and the dollar volume for each category of borrower for the past 9 years.

Figure 12

All Farmers: Number of Loans and Loan Volume Outstanding, Farm Credit Banks and Associations, 1988–1996

(As of December 31)



Source: Annual Young, Beginning, and Small Farmers Reports submitted by Farm Credit banks.

Declining Trend in Farm Numbers

FCS trends in the number of YBS farmers parallel the declining trends in farm numbers and new entrants in the overall farm sector. The number of farms in the United States has decreased continuously from its peak of 6.8 million in 1935, as is normal in the process of economic development. This trend has meant that new entrants only partially replace the retiring generation of farmers. A significant portion of the assets of retiring farmers is consolidated into existing operations, which do not provide new farming opportunities. Consequently, the average age of farmers is relatively high.

The System's YBS farmers lending programs reflect this economic environment of fewer entry opportunities for each succeeding generation. The U.S. Department of Agriculture has estimated that the gross number of new entrants to farming averaged 100,000 per year for 1978–1982, dropped to

8. The definition of small farmer has remained constant since 1988 at farm assets of less than $100,000 and gross sales less than $40,000, but the minimum viable size has tended to increase steadily. Increasingly, this category is part-time farmers. Because of limitations on authority to finance nonfarm needs of such borrowers, the FCS has served fewer such borrowers.

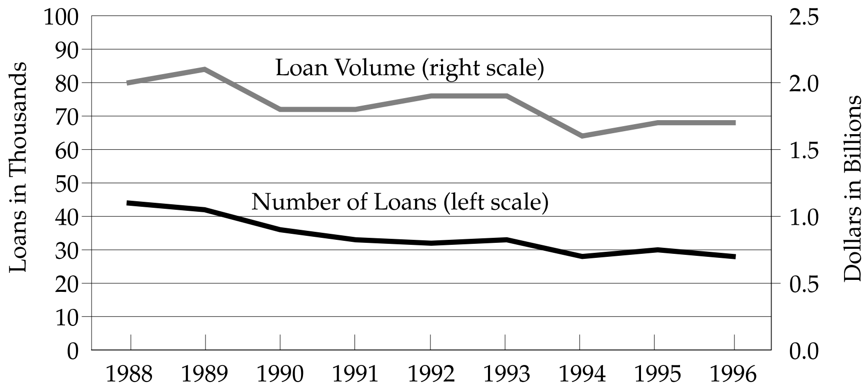
75,000 per year for 1982–1987, and dropped again to about 67,000 per year, for 1987–1992. From 1982 to 1992, the number of exits fluctuated much less, but it always exceeded the number of entrants. Entrants, like exits, occurred among all age groups, but the largest percentage occurred among young farmers (under age 35), who are also likely to be beginning farmers. The net decrease in numbers of farms varied from 3,000 per year during the favorable income years of 1978–1982 to 20,000 per year during the farm financial crisis of the mid-1980s. The decrease in the number of farms continued to grow to 32,500 per year for 1987–1992, even as farm incomes recovered, and it is projected to grow further in the 1992–2002 decade.

The declining number of farms combined with the enlargement of existing farms means fewer farm units are available for new entrants with each succeeding generation. The large number of farmers in older age groups as of 1992 means that the exit rate will be increasing again in the decade ahead. A portion will be replaced by new entrants. But another portion of retiring farmers' operations will continue to be consolidated into existing farm units.

Figure 13

Young Farmers: Number of Loans and Loan Volume Outstanding, Farm Credit Banks and Associations, 1988–1996

(As of December 31)

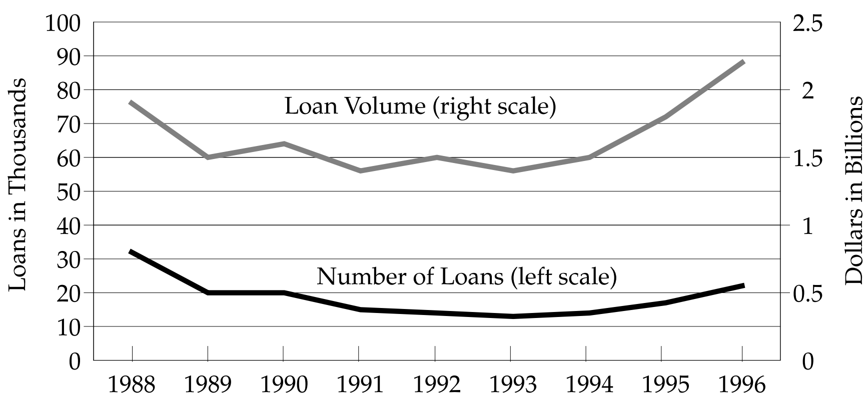


Note: Young means less than 35 years old.
Source: Annual Young, Beginning, and Small Farmers Reports submitted by Farm Credit banks.

Figure 14

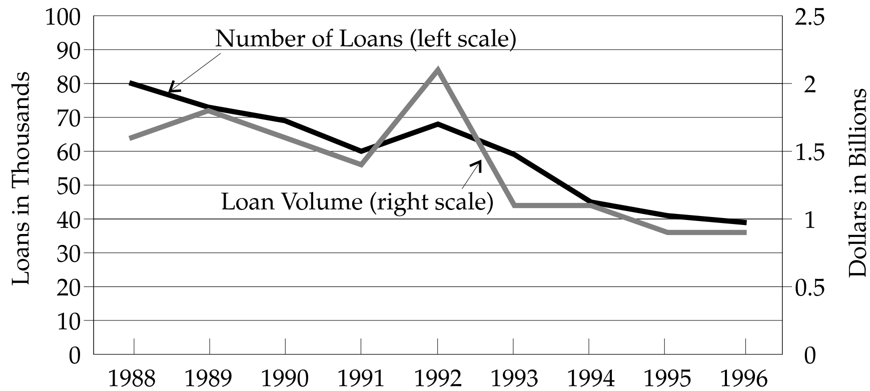
Beginning Farmers: Number of Loans and Loan Volume Outstanding, Farm Credit Banks and Associations, 1988–1996

(As of December 31)



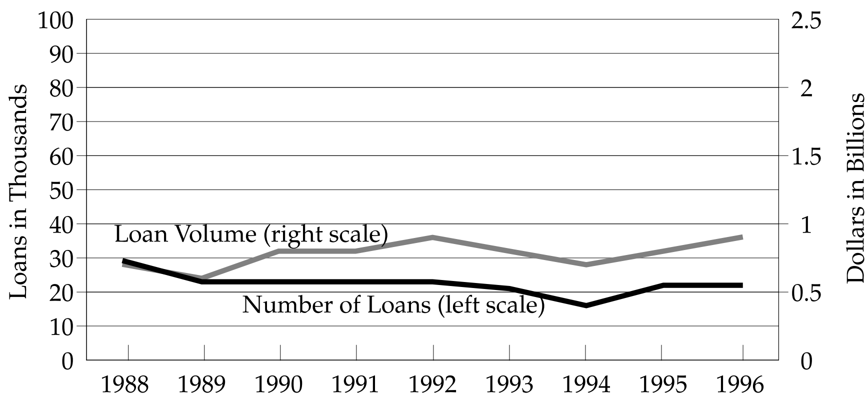
Note: Beginning means less than 6 years of farming experience.
Source: Annual Young, Beginning, and Small Farmers Reports submitted by Farm Credit banks.

Figure 15
Small Farmers: Number of Loans and Loan Volume Outstanding, Farm Credit Banks and Associations, 1988–1996
(As of December 31)



Note: Small means annual gross sales less than $40,000 and less than $100,000 in assets.
Source: Annual Young, Beginning, and Small Farmers Reports submitted by Farm Credit banks.

Figure 16
Young, Beginning, and Small Farmers: Number of Loans and Loan Volume Outstanding, Farm Credit Banks and Associations, 1988–1996
(As of December 31)



Note: Includes all borrowers meeting at least two of the three standards.
Source: Annual Young, Beginning, and Small Farmers Reports submitted by Farm Credit banks.

Two other economic forces help define the market limits within which the FCS operates:

(1) Limits on the scope of FCS lending to part-time farmers. Along with leasing of capital assets, the strategy of combining farm and nonfarm jobs has been a means of overcoming the barriers to entering farming. But YBS farmers who follow this part-time strategy may not be eligible for full financing of their farm and nonfarm needs from the FCS because of limitations imposed by statute and FCA regulations on eligibility and scope of financing. As a result, YBS part-time farmers may be more likely to seek loans from institutions free of such limitations, including commercial banks.

(2) The gradual shift from single-proprietor farming organizations to multioperator businesses (described in the fourth paragraph of this YBS report). This shift means that an increasing share of YBS operators are not the primary borrower and thus not counted in the statistics, even though they benefit from FCS loans.

The congressional requirement that the Farm Credit System have YBS programs cannot be expected to reverse such economic development trends. Special programs can help lower the financial requirements for individuals, enabling them to compete for a limited number of entry opportunities. Capital requirements can be a significant entry barrier, because an individual farm operating unit is among the most capital-intensive of businesses. Methods for lowering the financial requirements include leasing or renting capital assets and having FCS banks and associations provide special credit programs. The System's ability to lower financial requirements is limited by the requirement that the borrower meet sound credit underwriting standards.

District Programs for Young, Beginning, and Small Farmers

Section 4.19 of the Farm Credit Act requires each FCB and ACB to have policies and programs that specifically address the needs of YBS farmers. The bank policies generally provide that maximum use will be made of the flexibilities available within individual lending and service programs, that cooperation is expected with other lenders, and that Federal and State lending and guarantee programs will be used. The bank policies also generally require associations to have programs meeting these requirements, and may offer bank assistance in carrying out the programs. In each case, required programs must be within sound credit underwriting standards and within the capital resources of the institution if additional risks are assumed.

Although association programs vary greatly among institutions, they have important common elements. The programs that focus directly on lending include pooling higher risk credits with normal-risk credits in loan pricing; relaxing credit underwriting standards on a portion of the loan portfolio and then creating specific allowance for losses; creating specific programs for targeted groups; providing additional counseling and analysis to control risks on loans that would not otherwise be made; utilizing insurance, individual guarantors, or co-makers on loans to YBS borrowers; and using automated or simplified loan procedures for small loans to reduce costs of providing credit to these borrowers.

Other programs provide targeted marketing to potential borrowers, including support of 4-H, Future Farmers of America, and young farmer and college student groups through prizes at agricultural fairs, scholarships, meeting sponsorship, or other activities. Still others offer counseling, special education, or training on financial management to current or potential borrowers, create advisory groups on appropriate programs, and offer outreach through farm meetings and organizations. Several districts require detailed annual reporting on the number and extent of these activities, which helps ensure a continuing focus on YBS customers. In these districts, the number of annual counseling sessions, meetings, and outside activities typically runs in the hundreds.

Farm Credit System Financial Tables

The financial tables that follow were developed by the Farm Credit Administration from Call Report data submitted by each Farm Credit System institution. The Call Report information submitted is routinely reviewed for accuracy. Although FCA believes the Call Report data are reliable, the financial data submitted by each Farm Credit System institution and contained in the Call Reports have not been audited by FCA, nor does FCA express an opinion on their content. In addition, because of significant intercorporate relationships that exist between and among FCS institutions, it is not possible to add financial data for each group of like institutions presented in this report and obtain data for the combined FCS.

In 1995, FCA made several changes in the financial tables compared with previous years' reports. The Banks for Cooperatives financial tables were deleted because only one BC existed as of yearend 1995. The Farm Credit System Banks' table contains data for the Farm Credit Banks, the Bank for Cooperatives, and the Agricultural Credit Bank on a combined basis. The Federal Land Bank Associations Combined Trends in Selected Financial Measures was deleted. One table was added: Major Financial Indicators by System, Quarterly Comparison, which exhibits data for the past five quarters for combined Farm Credit System Banks, the combined Direct Lender Associations, and the Total Farm Credit System.[1]

1. This table is updated quarterly in FCA's quarterly *Risk Analysis of Farm Credit System Operations*.

Financial Table 1

Major Financial Indicators by System, Quarterly Comparison[1]

(Dollars in Thousands)

At and for the 3 months ended	31-Dec-96	30-Sep-96	30-Jun-96	31-Mar-96	31-Dec-95
Farm Credit System Banks[2]					
Gross Loan Volume	56,466,631	56,587,082	56,778,256	55,935,408	54,346,735
Formally Restructured Loans[3]	307,530	328,813	314,345	313,013	337,125
Accrual Loans 90 or More Days Past Due	6,283	15,220	45,244	35,302	8,767
Nonaccrual Loans	253,869	292,989	303,742	319,978	338,395
Nonperforming Loans[4]	1.01%	1.13%	1.17%	1.19%	1.26%
Cash and Marketable Investments	11,274,574	10,797,050	11,368,932	10,788,273	10,553,844
Total Capital/Total Assets[5]	8.46%	8.57%	8.39%	8.49%	8.56%
Total Unallocated Retained Earnings/Total Assets	3.87%	3.96%	3.83%	3.84%	3.78%
Total Net Income	120,947	154,142	160,344	186,801	113,330
Return on Assets[6]	0.71%	0.90%	0.94%	1.13%	0.70%
Return on Equity[6]	8.23%	10.57%	11.18%	13.22%	7.94%
Net Interest Margin	1.60%	1.62%	1.71%	1.79%	1.73%
Operating Expense Rate[7]	0.73%	0.60%	0.61%	0.61%	0.76%
Associations Excluding Federal Land Bank Associations (FLBAs)					
Gross Loan Volume	34,062,673	33,792,140	33,105,217	31,144,834	30,919,467
Formally Restructured Loans[3]	87,959	90,451	94,413	99,158	108,139
Accrual Loans 90 or More Days Past Due	21,775	18,345	45,157	48,535	21,571
Nonaccrual Loans	390,935	442,427	455,525	458,034	462,354
Nonperforming Loans[4]	1.47%	1.63%	1.80%	1.94%	1.91%
Total Capital/Total Assets[5]	16.69%	16.55%	16.63%	17.37%	17.06%
Total Unallocated Retained Earnings/Total Assets	12.06%	12.11%	12.02%	12.36%	11.87%
Total Net Income	160,551	142,343	149,676	170,738	143,921
Return on Assets[6]	1.76%	1.57%	1.75%	2.09%	1.72%
Return on Equity[6]	10.45%	9.44%	10.28%	11.90%	9.96%
Net Interest Margin	3.39%	3.28%	3.50%	3.72%	3.65%
Operating Expense Rate[7]	2.01%	1.82%	1.91%	1.96%	2.15%
Total Farm Credit System[8]					
Gross Loan Volume	61,178,000	60,909,424	61,178,699	60,405,383	58,589,076
Formally Restructured Loans[3]	246,000	264,543	272,723	298,738	320,194
Accrual Loans 90 or More Days Past Due	28,000	34,264	84,614	82,918	28,686
Nonaccrual Loans	645,000	735,411	759,227	778,085	800,764
Nonperforming Loans[4]	1.50%	1.70%	1.83%	1.92%	1.96%
Total Bonds and Notes	62,343,000	62,045,482	62,857,224	61,406,717	59,777,786
Total Capital/Total Assets	14.32%	14.24%	13.80%	13.79%	13.81%
Total Surplus/Total Assets	9.91%	9.82%	9.47%	9.36%	9.20%
Total Net Income	250,000	288,595	307,521	354,167	257,797
Return on Assets[6]	1.34%	1.54%	1.66%	1.96%	1.57%
Return on Equity[6]	9.51%	11.14%	12.21%	14.46%	11.47%
Net Interest Margin	2.93%	2.90%	3.00%	3.14%	3.07%

1. Some of the previously published quarterly data have been restated to include subsequent adjustments.
2. Includes Farm Credit Banks, the Bank for Cooperatives, and the Agricultural Credit Bank.
3. Excludes loans past due 90 days or more.
4. Nonperforming Loans are defined as Nonaccrual Loans, Formally Restructured Loans, and Accrual Loans 90 or More Days Past Due.
5. Total capital includes protected borrower stock.
6. Income ratios are for the quarter and are annualized.
7. Defined as operating expenses divided by average gross loans.
8. Cannot be derived through summation of above categories because of intradistrict and intra-System eliminations.

Source: Call Reports received from the Farm Credit System and the Federal Farm Credit Banks Reports to Investors of the Farm Credit System.

Financial Table 2

Farm Credit System Banks Combined Statement of Financial Condition[1]

(Dollars in Millions)

As of December 31	1996	1995	1994	1993	1992
Assets					
Loans	$57,300.7	$55,231.9	$51,563.9	$51,212.6	$50,320.1
Allowance for Losses	729.7	707.0	801.0	885.8	880.2
Net Loans	56,571.0	54,524.9	50,762.9	50,326.8	49,439.9
Cash and Investments in Securities	11,234.2	10,509.1	9,710.3	9,261.4	9,241.6
Other Property Owned	21.1	33.3	52.9	131.6	248.4
Other Assets–Net	722.7	686.3	647.8	662.4	702.6
Total Assets	**68,549.1**	**65,753.5**	**61,173.9**	**60,382.2**	**59,632.5**
Liabilities					
Consolidated Systemwide and Other Bonds	47,384.2	43,220.3	37,968.5	36,115.6	37,814.7
Consolidated Systemwide Notes	13,647.7	15,194.1	16,431.3	17,695.0	15,455.5
Other Liabilities	1,719.1	1,709.8	1,519.8	1,340.4	1,425.3
Total Liabilities	**62,751.1**	**60,124.2**	**55,919.6**	**55,151.0**	**54,695.6**
Net Worth					
Capital					
Capital Stock and Participation Certificates–Protected	0.5	0.5	2.7	7.1	113.8
Capital Stock and Participation Certificates–Unprotected	2,748.3	2,715.1	2,206.7	2,327.0	2,267.4
Preferred Stock–Financial Assistance Corporation	0.0	0.0	388.2	476.7	566.7
Other Capital	383.0	429.8	227.4	113.0	104.1
Total Capital	**3,131.8**	**3,145.4**	**2,824.9**	**2,923.8**	**3,052.0**
Earned Net Worth	2,666.2	2,483.9	2,429.4	2,307.3	1,884.9
Total Net Worth	**5,798.1**	**5,629.3**	**5,254.3**	**5,231.1**	**4,937.0**
Total Liabilities and Net Worth	**$68,549.1**	**$65,753.5**	**$61,173.9**	**$60,382.2**	**$59,632.5**

1. Includes six Farm Credit Banks, one Agricultural Credit Bank, and one Bank for Cooperatives.

Note: Totals may not add because of rounding.

Financial Table 3

Farm Credit System Banks Combined Statement of Income and Expense[1]

(Dollars in Millions)

For the Year Ended December 31	1996	1995	1994	1993	1992
Interest Income					
Loans	$3,981.7	$3,904.4	$3,283.5	$3,167.5	$3,559.1
Investments and Other	641.8	595.9	404.9	336.6	412.9
Total Interest Income	**4,623.5**	**4,500.3**	**3,688.4**	**3,504.1**	**3,972.0**
Interest Expense					
Consolidated Bonds	2,686.8	2,458.4	1,894.6	1,752.3	2,198.2
Notes and Other	816.5	996.6	709.1	521.2	627.6
Total Interest Expense	**3,503.2**	**3,455.0**	**2,603.7**	**2,273.4**	**2,825.8**
Net Interest Income	1,120.3	1,045.3	1,084.7	1,230.7	1,146.3
Less: Provision for Loan Losses	83.0	(7.8)	17.4	14.9	15.3
Net Interest Income after					
Provision for Loan Losses	1,037.4	1,053.1	1,067.3	1,215.8	1,131.0
Other Income	87.4	82.7	58.4	94.5	111.7
Operating Expenses					
Salaries and Employee Benefits	124.6	120.3	147.0	169.1	172.1
Occupancy and Equipment Expenses	25.3	27.9	32.8	38.8	40.5
Other Operating Expenses	207.2	250.7	311.0	330.0	321.1
Total Operating Expenses	**357.1**	**398.9**	**490.7**	**537.9**	**533.6**
Other Expenses	146.6	138.2	180.7	169.7	189.6
Extraordinary Items	1.2	(43.3)	(2.7)	(12.7)	(13.6)
Net Income	**$622.2**	**$555.3**	**$451.7**	**$589.9**	**$505.8**

1. Includes six Farm Credit Banks, one Agricultural Credit Bank, and one Bank for Cooperatives.

Note: Totals may not add because of rounding.

Financial Table 4

Farm Credit System Banks Combined Trends in Selected Financial Measures[1]

(Dollars in Millions)

As of December 31	1996	1995	1994	1993	1992
Loan Performance					
Performing[2]	$56,733.0	$54,547.6	$50,607.0	$49,804.6	$48,292.3
Formally Restructured[2]	307.5	337.1	397.4	490.5	696.0
Nonaccrual	253.9	338.4	524.8	906.7	1,323.5
Loans Past Due 90 Days or More	6.3	8.8	34.7	10.9	19.8
Net Chargeoffs on Loans	$30.7	($7.9)	($0.8)	$6.8	$31.2
Selected Ratios					
Return on Assets (%)	0.92	0.89	0.75	1.00	0.85
Return on Equity (%)	10.77	10.04	8.40	11.22	10.02
Net Interest Margin (%)	1.68	1.71	1.84	2.17	2.03
Capital as a Percentage of Assets	8.46	8.56	8.59	8.66	8.28
Debt-to-Capital Ratio	10.82	10.68	10.64	10.54	11.08

1. Includes six Farm Credit Banks, one Agricultural Credit Bank, and one Bank for Cooperatives.
2. Excludes loans past due 90 days or more.

Financial Table 5

Direct Lender Associations Combined Statement of Financial Condition[1]

(Dollars in Millions)

As of December 31	1996	1995[2]	1994	1993	1992
Assets					
Loans	$34,768.4	$31,627.2	$29,365.6	$26,416.2	$25,045.9
Allowance for Losses	955.0	886.3	748.5	601.1	566.0
Net Loans	33,813.5	30,740.9	28,617.1	25,815.2	24,479.9
Cash and Investments in Securities	170.1	166.0	115.8	47.2	71.1
Other Property Owned	33.5	30.6	47.3	56.7	70.6
Other Assets–Net	2,439.0	2,397.0	2,301.9	2,250.0	1,957.9
Total Assets	**36,456.0**	**33,334.4**	**31,082.1**	**28,169.0**	**26,579.5**
Liabilities					
Consolidated Systemwide and Other Bonds	N/A	N/A	N/A	N/A	N/A
Consolidated Systemwide Notes	N/A	N/A	N/A	N/A	N/A
Other Liabilities	30,371.8	27,646.4	25,710.3	23,136.9	22,279.2
Total Liabilities	**30,371.8**	**27,646.4**	**25,710.3**	**23,136.9**	**22,279.2**
Net Worth					
Capital					
Capital Stock and Participation Certificates–Protected	122.2	147.8	190.0	215.3	146.2
Capital Stock and Participation Certificates–Unprotected	1,034.1	1,119.9	1,267.8	1,262.8	1,231.2
Preferred Stock–Financial Assistance Corporation	0.0	0.0	0.0	0.0	0.0
Other Capital	15.4	15.2	14.9	111.4	108.8
Total Capital	**1,171.7**	**1,282.8**	**1,472.7**	**1,589.5**	**1,486.3**
Earned Net Worth	4,912.4	4,405.1	3,899.2	3,442.6	2,814.0
Total Net Worth	**6,084.2**	**5,688.0**	**5,371.9**	**5,032.2**	**4,300.3**
Total Liabilities and Net Worth	**$36,456.0**	**$33,334.4**	**$31,082.1**	**$28,169.0**	**$26,579.5**

1. Includes Production Credit Associations, Agricultural Credit Associations, and Federal Land Credit Associations. Figures for 1992 through 1996 are not comparable to previous years because of mergers of Federal Land Bank Associations and PCAs into ACAs, and creation of FLCAs and downloading of farm real estate loans from Farm Credit Banks.
2. Some of the previously published annual data have been restated to include subsequent adjustments.

Notes: Totals may not add because of rounding. N/A = Not applicable.

Financial Table 6

Direct Lender Associations Combined Statement of Income and Expense[1]

(Dollars in Millions)

For the Year Ended December 31	1996	1995[2]	1994	1993	1992
Interest Income					
Loans	$2,878.2	$2,745.7	$2,258.9	$1,997.2	$2,098.0
Investments and Other	3.7	5.5	0.9	2.0	4.4
Total Interest Income	**2,881.9**	**2,751.2**	**2,259.7**	**1,999.2**	**2,102.4**
Interest Expense					
Consolidated Bonds	N/A	N/A	N/A	N/A	N/A
Notes and Other	1,769.9	1,690.2	1,301.2	1,146.2	1,331.2
Total Interest Expense	**1,769.9**	**1,690.2**	**1,301.2**	**1,146.2**	**1,331.2**
Net Interest Income	1,112.0	1,061.0	958.6	853.0	771.3
Less: Provision for Loan Losses	57.4	51.6	46.7	32.6	40.9
Net Interest Income after					
Provision for Loan Losses	1,054.6	1,009.3	911.9	820.4	730.3
Other Income	362.4	345.1	326.4	273.3	303.9
Operating Expenses					
Salaries and Employee Benefits	356.3	352.1	348.0	316.8	290.3
Occupancy and Equipment Expenses	48.9	45.7	42.7	38.7	35.0
Other Operating Expenses	218.7	212.1	193.3	165.4	153.1
Total Operating Expenses	**623.9**	**609.9**	**584.0**	**521.0**	**478.4**
Other Expenses	169.9	148.4	132.6	130.9	132.0
Extraordinary Items	0.2	0.2	0.0	80.6	8.0
Net Income	**$623.4**	**$596.4**	**$521.7**	**$522.4**	**$431.8**

1. Includes Production Credit Associations, Agricultural Credit Associations, and Federal Land Credit Associations. Figures for 1992 through 1996 are not comparable to previous years because of mergers of Federal Land Bank Associations and PCAs into ACAs, and creation of FLCAs and downloading of farm real estate loans from Farm Credit Banks.
2. Some of the previously published annual data have been restated to include subsequent adjustments.

Notes: Totals may not add because of rounding. N/A = Not applicable.

Financial Table 7

Direct Lender Associations Combined Trends in Selected Financial Measures[1]

(Dollars in Millions)

As of December 31	1996	1995[2]	1994	1993	1992
Loan Performance					
Performing[3]	$34,267.8	$31,035.1	$28,704.1	$25,706.1	$24,117.6
Formally Restructured[3]	88.0	108.1	129.6	137.1	228.3
Nonaccrual	390.9	462.4	513.4	556.5	659.9
Loans Past Due 90 Days or More	21.8	21.6	18.5	16.6	40.1
Net Chargeoffs on Loans	$17.4	$3.2	$4.5	($0.4)	$7.3
Selected Ratios					
Return on Assets (%)	1.79	1.86	1.74	1.92	1.65
Return on Equity (%)	10.51	10.68	9.95	11.15	10.52
Net Interest Margin (%)	3.46	3.63	3.51	3.48	3.26
Capital as a Percentage of Assets	16.69	17.06	17.28	17.86	16.18
Debt-to-Capital Ratio	4.99	4.86	4.79	4.60	5.18

1. Includes Production Credit Associations, Agricultural Credit Associations, and Federal Land Credit Associations. Figures for 1992 through 1996 are not comparable to previous years because of mergers of Federal Land Bank Associations and PCAs into ACAs, and creation of FLCAs and downloading of farm real estate loans from Farm Credit Banks.
2. Some of the previously published annual data have been restated to include subsequent adjustments.
3. Excludes loans past due 90 days or more.

Financial Table 8

Federal Land Bank Associations Combined Statement of Financial Condition[1]

(Dollars in Millions)

As of December 31	1996	1995	1994	1993	1992
Assets					
Loans[2]	N/A	N/A	N/A	N/A	N/A
Allowance for Losses[3]	N/A	N/A	N/A	N/A	N/A
Net Loans	N/A	N/A	N/A	N/A	N/A
Cash and Investments in Securities	$528.3	$447.7	$318.0	$263.9	$275.2
Other Property Owned	N/A	N/A	N/A	N/A	N/A
Other Assets–Net	415.3	400.1	219.3	268.5	473.4
Total Assets	**943.6**	**847.8**	**537.3**	**532.4**	**748.5**
Liabilities					
Consolidated Systemwide and Other Bonds	N/A	N/A	N/A	N/A	N/A
Consolidated Systemwide Notes	N/A	N/A	N/A	N/A	N/A
Other Liabilities	61.2	46.6	35.5	46.0	55.0
Total Liabilities	**61.2**	**46.6**	**35.5**	**46.0**	**55.0**
Net Worth					
Capital					
Capital Stock and Participation Certificates–Protected	8.2	9.8	11.6	17.7	140.1
Capital Stock and Participation Certificates–Unprotected	133.2	164.9	188.9	200.0	216.5
Other Capital	0.0	0.0	0.0	0.0	0.0
Total Capital	**141.3**	**174.7**	**200.5**	**217.8**	**356.6**
Earned Net Worth	741.0	626.4	301.4	268.7	337.0
Total Net Worth	**882.4**	**801.2**	**501.9**	**486.4**	**693.5**
Total Liabilities and Net Worth	**$943.6**	**$847.8**	**$537.3**	**$532.4**	**$748.5**

1. Figures for 1992 through 1996 are not comparable to previous years because of mergers of FLBAs and Production Credit Associations into Agricultural Credit Associations, and creation of Federal Land Credit Associations and downloading of farm real estate loans from Farm Credit Banks.
2. The FLBAs act as agents for the FCBs (formerly Federal Land Banks) in the lending process but do not hold loans themselves.
3. FLBAs in some districts have liability for losses on FCB (formerly Federal Land Bank) loans. Because FLBAs do not make loans, the FLBA allowance for loan losses is included in FLBA liabilities.

Notes: Totals may not add because of rounding. N/A = Not applicable.

Financial Table 9

Federal Land Bank Associations Combined Statement of Income and Expense[1]

(Dollars in Millions)

For the Year Ended December 31	1996	1995	1994	1993	1992
Interest Income					
Loans	N/A	N/A	N/A	N/A	N/A
Investments and Other	22.0	24.4	15.7	2.4	1.7
Total Interest Income	**22.0**	**24.4**	**15.7**	**2.4**	**1.7**
Interest Expense					
Consolidated Bonds	N/A	N/A	N/A	N/A	N/A
Notes and Other	N/A	N/A	N/A	N/A	N/A
Total Interest Expense	**N/A**	**N/A**	**N/A**	**N/A**	**N/A**
Net Interest Income	22.0	24.4	15.7	2.4	1.7
Less: Provision for Loan Losses	4.0	0.0	(2.7)	(1.4)	2.1
Net Interest Income (Loss) after Provision for Loan Losses	17.9	24.3	18.4	3.8	(0.4)
Other Income	161.8	335.1	79.4	168.5	208.0
Operating Expenses					
Salaries and Employee Benefits	37.7	36.1	35.2	45.0	47.0
Occupancy and Equipment Expenses	4.9	4.7	4.9	5.9	6.3
Other Operating Expenses	15.3	14.8	15.9	22.0	24.4
Total Operating Expenses	**58.0**	**55.7**	**56.0**	**73.0**	**77.7**
Other Expenses	0.1	0.1	0.1	0.1	0.0
Extraordinary Items	0.0	0.0	0.0	(0.4)	(0.6)
Net Income	**$121.7**	**$303.7**	**$41.8**	**$98.8**	**$129.2**

1. Figures for 1992 through 1996 are not comparable to previous years because of mergers of FLBAs and Production Credit Associations into Agricultural Credit Associations, and creation of Federal Land Credit Associations and downloading of farm real estate loans from Farm Credit Banks.

Notes: Totals may not add because of rounding. N/A = Not applicable.

Glossary

A

ACA—The acronym for Agricultural Credit Association.

ACB—The acronym for Agricultural Credit Bank.

Act—The abbreviated term for the Farm Credit Act of 1971, as amended.

AgAmerica, FCB—This is the Farm Credit Bank that was formed April 1, 1994, as a result of the consolidation of the FCB of Omaha and the FCB of Spokane. AgAmerica provides loan funds and support services to the associations serving Alaska, Idaho, Montana, Nebraska, Oregon, South Dakota, Washington, and Wyoming. On March 1, 1997, an agreement became effective that placed AgAmerica and the Western FCB under joint management and moved AgAmerica's headquarters from Spokane, Washington, to Sacramento, California.

Agency—When capitalized, the term refers to the Farm Credit Administration.

AgFirst Farm Credit Bank—Headquartered in Columbia, South Carolina, this institution provides loan funds and services to associations serving Delaware, Florida, Georgia, part of Kentucky, Maryland, North Carolina, part of Ohio, Pennsylvania, Puerto Rico, South Carolina, part of Tennessee, Virginia, and West Virginia. It also provides short- and intermediate-term financing to associations serving Alabama, Louisiana, and Mississippi. AgFirst was formed on April 1, 1995, as a result of a consolidation of the FCB of Columbia and the FCB of Baltimore.

AgriBank, FCB—AgriBank was formed on May 1, 1992, as a result of a consolidation of the FCB of St. Louis and the FCB of St. Paul. On October 1, 1993, the FCB of Louisville merged into AgriBank. AgriBank provides loan funds and services to the associations serving Arkansas, Illinois, Indiana, Kentucky, Michigan, Minnesota, Missouri, North Dakota, Ohio, Tennessee, and Wisconsin.

Agricultural Credit Association (ACA)—An Agricultural Credit Association is the successor entity resulting from the merger of a Federal Land Bank Association and a Production Credit Association and has the combined authority of the two institutions. An ACA borrows funds from a Farm Credit Bank or Agricultural Credit Bank to provide short-, intermediate-, and long-term credit to farmers, ranchers, and producers or harvesters of aquatic products. It also makes loans to these borrowers for certain processing and marketing activities, to rural homeowners for housing, and to certain farm-related businesses.

Agricultural Credit Bank (ACB)—An Agricultural Credit Bank is the successor entity resulting from the merger of a Farm Credit Bank and a Bank for Cooperatives and has the combined authorities of those two institutions. It also is authorized to finance U.S. agricultural exports and provide international banking services for farmer-owned cooperatives. CoBank is the only ACB in the Farm Credit System.

Assistance Board—The abbreviated term for the Farm Credit System Assistance Board.

Associations—A collective term often used to describe the local entities which serve as the delivery points for credit to farmers, ranchers, producers of aquatic products, and rural homeowners. The four types of associations are Agricultural Credit Associations, Federal Land Bank Associations, Federal Land Credit Associations, and Production Credit Associations.

B

Bank for Cooperatives (BC)—A Bank for Cooperatives provides lending and other financial services to farmer-owned cooperatives, rural utilities (electric and telephone), and rural sewer and water systems. It also is authorized to finance U.S. agricultural exports and provide international banking services for farmer-owned cooperatives. The St. Paul Bank for Cooperatives is the only BC in the Farm Credit System.

BC—The acronym for Bank for Cooperatives.

Basis Point—A basis point is one one-hundredth of 1 percent.

C

Call Report—A call report is a statement of condition and performance of a Farm Credit System bank or association. FCS banks and associations are required to file call reports quarterly with FCA.

CAMEL Rating—The acronym CAMEL represents the five key financial and operational criteria—capital adequacy, asset quality, management, earnings, and liquidity—that FCA examines in each Farm Credit System institution. CAMEL ratings range from 1, indicating a well managed institution that is basically sound in every respect, to 5, indicating an institution that is likely to fail.

CoBank, ACB—CoBank originally was formed by the merger of 10 of the 12 district Banks for Cooperatives and the Central Bank for Cooperatives on January 1, 1989. The resulting institution was the National Bank for Cooperatives. On January 1, 1995, CoBank became the only Agricultural Credit Bank in the Farm Credit System when it consolidated with the FCB of Springfield (Massachusetts) and the Springfield Bank for Cooperatives. Its headquarters is in Denver, Colorado, and it has the combined lending authority of a Farm Credit Bank (in its Northeast Region only) and a Bank for Cooperatives. It also is authorized to finance U.S. agricultural exports and provide international banking services for farmer-owned cooperatives.

F

Farm Credit Act (the Act)—The Farm Credit Act of 1971, as amended, is the statute under which the Farm Credit System operates. The Farm Credit Act recodified all previous acts governing the Farm Credit System.

Farm Credit Administration (FCA)—FCA is the independent Federal agency responsible for examining and regulating Farm Credit System institutions. FCA was created by Executive order in 1933 and derives its powers and authorities from the Farm Credit Act of 1971, as amended. The Agency's headquarters is in McLean, Virginia.

Farm Credit Administration Board—The three-member FCA Board is the policy-making body for the Farm Credit Administration. Members are appointed by the President with the advice and consent of the U.S. Senate to 6-year terms on the Board. Members may not be reappointed after serving a full term or more than 3 years of a previous member's term. The President designates one of the members as Chairman of the Board, who also serves as chief executive officer.

Farm Credit Bank (FCB)—On July 6, 1988, the Federal Land Bank and the Federal Intermediate Credit Bank in 11 of the 12 Farm Credit districts merged to become Farm Credit Banks. The mergers were required by the Agricultural Credit Act of 1987. FCBs provide services and funds to local associations which, in turn, lend those funds to farmers, ranchers, producers of aquatic products, rural residents for housing, and some agriculture-related businesses. As of December 31, 1996, there were six FCBs: AgAmerica, FCB; AgFirst FCB; AgriBank, FCB; Farm Credit Bank of Texas; Farm Credit Bank of Wichita; and Western Farm Credit Bank.

Farm Credit Bank of Texas—Headquartered in Austin, Texas, this institution provides services and short- and intermediate-term financing to associations serving Texas and parts of Louisiana and New Mexico. It provides services and long-term financing to associations serving Alabama, Louisiana, Mississippi, and Texas.

Farm Credit Bank of Wichita—Headquartered in Wichita, Kansas, this institution provides services and short-, intermediate-, and long-term financing to associations serving Colorado, Kansas, and Oklahoma, and short- and intermediate-term financing to part of New Mexico.

Farm Credit Leasing Services Corporation (Leasing Corporation)—The Leasing Corporation is a service entity owned by Farm Credit System banks to provide equipment leasing and related services to eligible borrowers, including agricultural producers, cooperatives, and rural utilities.

Farm Credit System (FCS or System)—The Farm Credit System is a nationwide network of financial cooperatives. Borrowers include farmers, ranchers, rural homeowners, agricultural cooperatives, rural utility systems, and agribusinesses.

Farm Credit System Assistance Board (Assistance Board)—The Assistance Board was created by the Agricultural Credit Act of 1987 to provide assistance to financially troubled Farm Credit Banks, protect the stock of System borrowers, restore Farm Credit System banks to economic viability, and preserve their ability to provide credit at reasonable and competitive rates. The Assistance Board terminated on December 31, 1992.

Farm Credit System Insurance Corporation (FCSIC)—FCSIC was established by the Agricultural Credit Act of 1987 as an independent U.S. Government-controlled corporation. Its purpose is to ensure the timely payment of principal and interest on insured notes, bonds, and other obligations issued on behalf of Farm Credit System banks. The FCA Board serves ex officio as the Board of Directors for FCSIC; however, the Chairman of the FCA Board is not permitted to serve as the Chairman of the FCSIC Board of Directors.

Farmer Mac—The abbreviated term for Federal Agricultural Mortgage Corporation.

FCA—The acronym for Farm Credit Administration.

FCB—The acronym for Farm Credit Bank.

FCS—The acronym for Farm Credit System.

FCSBA—The acronym for FCS Building Association.

FCSIC—The acronym for Farm Credit System Insurance Corporation.

FCS Building Association (FCSBA or Building Association)—FCSBA acquires, manages, and maintains facilities for FCA's headquarters and field offices. Formed in 1981, FCSBA is owned by FCS banks; however, oversight of its activities is vested in the FCA Board.

Federal Agricultural Mortgage Corporation (Farmer Mac)—Farmer Mac was created by the Agricultural Credit Act of 1987 to provide guarantees for the timely repayment of principal and interest on securities backed by pools of agricultural real estate or rural home loans. Farmer Mac is controlled by an independent 15-member board composed of 5 representatives from the Farm Credit System, 5 members from commercial banks and insurance companies, and 5 public members appointed by the President. Farmer Mac is regulated by FCA and is defined by statute as a System entity.

Federal Farm Credit Banks Funding Corporation (Funding Corporation)—Based in Jersey City, New Jersey, the Funding Corporation manages the sale of Systemwide debt securities to finance the loans made by Farm Credit System institutions. The Funding Corporation uses a network of bond dealers to market its securities.

Federal Funds Rate—The Federal Funds rate is the interest rate charged by banks with excess reserves at a Federal Reserve district bank to banks needing overnight loans to meet reserve requirements.

Federal Intermediate Credit Bank (FICB)—The Agricultural Credits Act of 1923 provided for the creation of 12 FICBs to discount the short- and intermediate-term notes of farmers made by commercial banks, livestock loan companies, and thrift institutions. The Farm Credit Act of 1933 authorized farmers to organize Production Credit Associations, which could discount notes with FICBs. As a result, PCAs became the primary entities for delivery of short- and intermediate-term credit to farmers and ranchers. On July 6, 1988, the Federal Intermediate Credit Bank and the Federal Land Bank in 11 of the 12 Farm Credit districts merged to become Farm Credit Banks. The mergers were required by the Agricultural Credit Act of 1987.

Federal Land Bank (FLB)—The Federal Farm Loan Act of 1916 provided for the establishment of 12 Federal Land Banks to provide long-term mortgage credit to farmers, ranchers, and later to rural home buyers. On July 6, 1988, the Federal Land Bank and the Federal Intermediate Credit Bank in 11 of the 12 Farm Credit districts merged to become Farm Credit Banks. The mergers were required by the Agricultural Credit Act of 1987.

Federal Land Bank Association (FLBA)—A Federal Land Bank Association serves as a lending agent for a Farm Credit Bank. FLBAs make and service long-term mortgage loans to farmers, ranchers, and rural residents for housing. An FLBA does not own loan assets, but makes loans only on behalf of the Farm Credit Bank with which it is affiliated.

Federal Land Credit Association (FLCA)—A Federal Land Credit Association is a Federal Land Bank Association that owns its own loan assets. An FLCA borrows funds from a Farm Credit Bank to make and service long-term loans to farmers, ranchers, and rural residents for housing.

FICB—The acronym for Federal Intermediate Credit Bank.

FLCA—The acronym for Federal Land Credit Association.

FLB—The acronym for Federal Land Bank.

FLBA—The acronym for Federal Land Bank Association.

FSA—The acronym for the U.S. Department of Agriculture's Farm Service Agency.

Funding Corporation—The abbreviated term for Federal Farm Credit Banks Funding Corporation.

J

Joint and Several Liability—The Farm Credit Act of 1971, as amended, authorizes each Farm Credit bank to join with other banks of the Farm Credit System in issuing Systemwide notes, bonds, debentures, and other obligations. Each bank is primarily liable for the portion of any issue of Systemwide obligations made on its behalf and is jointly and severally liable for the payment of any additional sums as called upon by FCA in order to make payments of interest or principal that any bank primarily liable is unable to make. "Jointly and severally" is a legal phrase used in definitions of liability meaning that an obligation may be enforced against all obligors jointly, or against any one of them separately.

L

Leasing Corporation—The abbreviated term for Farm Credit Leasing Services Corporation.

P

PCA—The acronym for Production Credit Association.

Production Credit Association (PCA)—The Farm Credit Act of 1933 authorized farmers to organize Production Credit Associations that could discount notes with FICBs. PCAs are System entities that deliver only short- and intermediate-term loans to farmers and ranchers. A PCA borrows money from its Farm Credit Bank to loan to farmers. PCAs also own their loan assets.

S

System—The abbreviated term for Farm Credit System.

U

USDA—The acronym for U.S. Department of Agriculture.

W

Western Farm Credit Bank—Headquartered in Sacramento, California, this institution provides loan funds and services to the associations serving Arizona, California, Hawaii, part of Idaho, Nevada, and Utah.

ADDITIONAL INFORMATION

This report is published in accordance with Section 5.17(a)(3) of the Farm Credit Act of 1971, as amended, which requires the Farm Credit Administration to make annual reports directly to Congress on the condition of the Farm Credit System and its institutions. These annual reports also must include a summary and analysis of reports submitted to FCA by Farm Credit banks on programs for serving young, beginning, and small farmers and ranchers. Further discussion of the financial condition and performance of the Farm Credit System may be found in the FCA report Risk Analysis of Farm Credit System Operations, published for the quarters ended March 31, June 30, and September 30. The report for the quarter ended December 31 was discontinued in 1995. Information previously contained in that report is now published as part of the Farm Credit Administration Report on the Financial Condition and Performance of the Farm Credit System. A discussion of the performance and financial condition of the Farm Credit Administration may be found in the Farm Credit Administration Annual Report. Depending on availability, these publications may be obtained without charge from:

Office of Congressional and Public Affairs
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090
Telephone (703) 883-4056 Fax (703) 790-3260
E-mail: info-line@fca.gov

Beginning with the report for the quarter ended September 30, 1996, Risk Analysis of Farm Credit System Operations is now available on FCA's web site at http://www.fca.gov.

Disclosure to investors in Farm Credit System securities is made by the Federal Farm Credit Banks Funding Corporation through annual and quarterly information statements published as part of the Report to Investors of the Farm Credit System, and through its Summary Report of Condition and Performance of the Farm Credit System, which is published each quarter. Copies of these reports are available from:

Federal Farm Credit Banks Funding Corporation
10 Exchange Place
Suite 1401
Jersey City, NJ 07302-3913
Telephone (201) 200-8000

The Farm Credit System Insurance Corporation, which ensures the timely payment of principal and interest on insured securities issued by FCS banks, publishes an annual report. Copies are available from:

Farm Credit System Insurance Corporation
1501 Farm Credit Drive
McLean, VA 22102
Telephone (703) 883-4380

In addition, FCS banks and associations are required by regulation to prepare annual and quarterly financial disclosure reports and make them available to their stockholders. Copies of these documents are available for public inspection at FCA headquarters in McLean, Virginia.

Copies Are Available From:
Office of Congressional and Public Affairs
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090
703.883.4056