

**Remarks by  
The Honorable Nancy C. Pellett  
Iowa Bankers Association  
June 9, 2004  
Longworth House Office Building, Washington, DC**

Thank you for that generous introduction and good afternoon to all of you.

I am very pleased that you invited me to join you today. It is an honor to spend time with people like you who care about agriculture and rural America...and it is a bonus for me to also spend some time with fellow Iowans.

I want to talk to you today about some of the challenges I believe agriculture and rural America face. And I want to talk about some of the opportunities I see for partnering among financial institutions to better meet these challenges. Before I get into these areas, though, I want to share some background information about myself and the agency I lead.

My intention is to provide you with a perspective that may help you better understand what my approach may be, as issues come before the Farm Credit Administration Board.

(Chairman Pellett briefly described her Iowa roots and farming background)

My knowledge of agriculture is deep, and my understanding of rural America is deep, as I have worked it, and lived it, my whole life. My experience has given me a strong passion to be involved and to make a difference for agriculture and rural America.

And that, ladies and gentlemen, is the principal reason why I came to the Farm Credit Administration.

So, let me tell you a little bit about my Agency.

The Farm Credit Administration is an independent federal agency that oversees the operations of about 100 or so lending institutions that comprise the Farm Credit System nationwide.

Our mission at FCA is to ensure that Farm Credit System institutions remain capable of providing agriculture and rural America with a dependable source of credit.

We accomplish this mission in two ways.

First, we conduct a basic financial safety and soundness examination of each Farm Credit System institution. If we see problems in how an institution conducts its business, we have authorities available to us to ensure problems are corrected promptly.

The second way we accomplish our mission is to develop regulations that govern how Farm Credit System institutions conduct their business. Twice a year we publish what is called our unified agenda, which describes the regulations we will be working on over the next six months.

We are a small agency by most standards with a budget of just over \$40 million and a staff of less than 300.

Though small, we have a rich history of service to agriculture, and our record speaks loudly about how well government can actually work. We are at the forefront of developing increasingly efficient programs that not only ensure safety and soundness requirements are adhered to, but also ones that result in minimal disruption to the business activities of the financial institutions we oversee.

I must tell you that I am very proud to bring the perspective of production agriculture and rural America to the FCA Board discussions, and ultimately the FCA Board decisions, that will affect how the System will operate in the future.

I also want to emphasize a few things we do not do. FCA does not run the System...we are an arms length regulator. We do not engage in the day-to-day management decisions of the institutions we regulate. We do not speak for or represent the System any more than the OCC or FDIC does for your institution.

Although commercial bankers have undergone a period of modernization through Gramm-Leach-Bliley and more recently, Sarbanes Oxley, the System's basic statute has not changed significantly since the mid-1980s and has not been updated to reflect market changes since 1971. As a result, the Farm Credit Act does not accommodate many of the market conditions and economic forces that exist today. Consequently, FCA, through its regulations, policies and examinations, must fill in the gaps, to the extent permitted by law, much like OCC and the Federal Reserve Board did prior to recent bank modernization laws.

There are 400 commercial banks in Iowa and almost 75 percent of them are defined as agricultural banks. This represents the highest state-wide concentration of agricultural banks in the country. Your agricultural loans increased in 2003 by 8 percent, considerably more than the national average of 5 percent. This statistic suggests that agriculture continues to prosper in Iowa and that farmers are confident in their bank relationships.

The System has a smaller presence in Iowa. USDA data shows that at yearend 2002, the System had 28 percent of the agricultural mortgage market, compared to 37 percent for commercial banks. It had 10 percent of the agricultural operating loan market, compared to 65 percent for commercial banks. Overall, commercial bank agricultural loan volume in Iowa is almost two and a half times that of the Farm Credit System.

Your main touch-point with the Farm Credit System in Iowa would be through Farm Credit Services of America which is headquartered in Omaha. FCS of America provides over \$7 billion in funds to borrowers in Nebraska, South Dakota, and Wyoming as well as Iowa. It is funded by AgriBank, headquartered in St. Paul, MN, which is one of the 5 Farm Credit Banks nationwide.

I will be interested to see how Rabobank, a recent entry into the Iowa agricultural lending market fares with its large capital base, asset size, and diverse range of financial products and services.

Let me turn to some thoughts on rural America.

In 1970, 26 percent of the American population was considered rural. By 2000, Americans living in rural areas had dropped by a fifth to 21 percent of the population. Over the same time period, the total American labor force grew by 70 percent, while agricultural employment actually declined 5 percent. Additionally, the number of farms in operation declined from 3 million in 1970 to around 2 million in 2000, or a drop of one third.

About 80 percent of the farm families today have off-farm income that exceeds their farm income. Hence, a significant need for farm families is job opportunities in nearby communities. Without these jobs, we see a migration from rural communities to metropolitan areas or regional economic hubs, especially during times of economic stress.

This population shift to metropolitan or regional economic hubs has aggravated deterioration in the rural infrastructure. The resulting declining tax base inhibits the ability of rural communities to invest in new or upgraded infrastructure needs for transportation, communication, education, and public health. If rural residents want improved public facilities, they often feel obliged to move to those areas where population growth and economic opportunities are creating the types of modern public facilities and amenities they seek. As you are well aware, the population shift often times leads to capital movement from local depository institutions to larger regional and national financial institutions, many of which do not work within the same regulatory structure and related restrictions that you do.

Ladies and gentlemen the voice of agriculture is just simply getting smaller every day. With fewer and fewer people directly involved in agriculture, there is less understanding of the needs of agriculture and rural America. These trends also indicate that only a fraction of the next generation will have rural roots or work in agriculture.

The challenge remaining for those concerned with the prosperity of rural America is clear. There remains a continuing demand for debt capital and an unmet need for equity capital, needed to promote and support the businesses and jobs that rural America must have to prosper. This is especially true for the value-added products that provide greater profit opportunities for agricultural producers.

As financial service providers, Farm Credit System lenders and commercial bankers share a common dedication to the prosperity of the rural and agricultural economy. You both engage in a number of business activities together and opportunities exist for expanding these mutually beneficial business relationships.

For example...System institutions have authority to enter into participations with commercial banks and other lenders in making loans to agriculture and rural America. These transactions reduce credit and interest rate risk and can be used to enhance earnings, capital, and liquidity. You can also use participations to diversify your portfolios or to fund large loans when lending limitations exist. Last year System institutions reported record participations and syndications with non-System lenders. This represents an ongoing trend over the last six years. I believe business relationships like this are good for agriculture and rural America and I expect this trend to continue.

System institutions have also partnered with commercial banks to offer a wide range of services to System and non-System borrowers. For example, one System lending institution entered into an agreement with a local bank that allowed the bank to offer cash management services to the System institution's customers. Another System institution entered into an agreement with a local bank, allowing the bank to offer checking accounts to System institution customers. These partnering arrangements capitalize on the unique resources and efficiencies of the financial institutions involved to bring added value to the rural customers they serve.

We recently issued a regulation that facilitates greater access to GSE funding through what is called the Other Financial Institutions (OFI) program. OFIs can be national banks, state banks, trust companies, agricultural credit corporations, incorporated livestock loan companies, savings institutions, and credit unions. This regulation makes it easier for OFIs to obtain GSE funding from system banks for short- and intermediate-term loans to farmers, ranchers, farm-related businesses, and rural homeowners.

I have asked staff to explore other available partnerships that could increase the flow of funds to agriculture and rural areas.

Perhaps a part of the need for equity capital can be met through USDA's Rural Business Investment Company (RBIC) program. The 2002 Farm Bill authorized RBICs and directed USDA to develop regulations to implement the program. This program is designed to copy the very successful Small Business Investment Company program administered by the Small Business Administration.

I believe that this program, when implemented, offers another opportunity for partnering between commercial banks and System institutions as the law, with certain limitations, permits System institutions to establish or invest in RBICs. As USDA implements this program, you may find technical and financial assistance available from System institutions, which, like yours, are committed to supporting the rural economy.

In summary, the more I look at the issue, the more I become convinced that vibrant rural communities are the most critical factor in keeping farmers on the land or getting new entrants to farming. So, to better support agriculture, I believe we must focus on, and fund, activities that benefit rural America. What that means, is that you, the commercial bankers, play a critical role in funding the needs of our rural communities...and if that challenge can be better met by partnering with others, such as the Farm Credit System, then I strongly encourage you to do so.

Please remember, it is not just banks, it is not just USDA, it is not just the Farm Credit System...it is all of you, in partnership with each other, that will make a difference in strengthening agriculture and the rural America of the future.

Ladies and gentlemen, throughout my term I intend to be a strong advocate for agriculture and our rural communities. While competition is healthy and necessary in our economy, cooperation and partnering could create economic strength for all parties involved, and can provide important benefits for your customers, agriculture and rural America. I believe regulatory barriers that impede cooperation and partnering need to be identified, closely analyzed, and removed, or at least modified.

As we look for ways to bring this about, I extend a personal invitation to each of you to share your ideas about what can be done to revitalize our rural economy and improve the economic well being of our agricultural producers. We would sincerely like to hear your ideas...especially ways that commercial bankers and the Farm Credit System might further cooperate and partner to help bring this about.

Thank you for sharing your time with me and if there are any questions I would be happy to address them.