Successful Ag Lending: Accomplishing Your Mission in Stressful Times

By Ed Harshbarger, Director
Risk Analysis Division

Two key conclusions emerge from FCA's recent symposium. First, in today's era of increasing risk for the farm sector, lenders need to be cognizant of the full range of risk management tools available to the producer and advise their borrowers in the use of these tools. Second, farmers and lenders need to prepare for a possible cessation of the Government largesse that has been provided to agriculture during the last 3 years. The recent provision of an additional $15 billion in Government funds for financial assistance and crop insurance is not likely to recur in 2001. Since the 1996 Farm Bill, experts have predicted that the burden of managing farm income and farm policy risks will shift to the producer and their lenders. As we look toward a new farm program in 2002, this prediction may well come true.

Both Secretary of Agriculture Dan Glickman and Dr. J.B. Penn outlined likely features in the new farm bill at the symposium. However, their "guiding principles" may be overshadowed by a host of diverse political pressures that the new Congress will face after this fall's elections. Both speakers agreed that the current ad hoc approach to policy formulation is flawed because it overrides market signals and overstates asset values. They urged Congress to develop a coherent long-term policy that not only is fair and equitable, but also emphasizes access to foreign markets, since exports are so critical to future income growth. In the final analysis, economic and fiscal considerations likely will prevail over efforts to materially raise the Federal safety net, leaving much of the risk management burden on the shoulders of producers.

The symposium dealt with different types of risks encountered by farmers and various tools for managing them. The speakers talked about ways to manage yield and price risks, long a traditional challenge in agriculture, along with emerging risks in the trade, technology, and environmental areas. For many people, the environment, and how we care for it, deserves close attention in the policy debates, just as GMO issues raise controversial questions in the technology area. Crop insurance likely will be a centerpiece in the new farm program, given the $8 billion subsidy for 5 years. However, some critics question whether large subsidies are a wise use of resources, especially if they encourage farmers to produce in marginal areas or take risks elsewhere. Also, crop insurance, or a successor product, may not give many producers the type of income protection they need on a multi-year basis at an affordable price.

Michael Reyna, Dan Glickman, and Ann Jorgensen

Another important part of the symposium looked at mission. Dr. Gene Swackhamer reminded us that the Farm Credit System (FCS or System), as rural America's Government-sponsored enterprise (GSE), is expected to fulfill its public purpose in both good times and bad. Various speakers outlined important strategies that would enhance the System's ability to meet its public purpose responsibilities in the areas of ensuring borrower rights, lending to young, beginning, small, and minority farmers, and supporting the needs of rural America during stressful times. To remain relevant as a GSE provider of funds, the System must adapt rapidly to the changing needs of agriculture and rural America in the exciting years ahead.

Highlights of FCA Symposium

May 25-26, 2000

"Any future policy must support the important role the **Farm Credit System** plays in helping farmers succeed,"

Dan Glickman, U.S. Secretary of Agriculture, keynote speaker for FCA Symposium, May 25, 2000

The Mission of the Farm Credit System

Dr. Gene Swackhamer's keynote presentation challenged the audience to rethink the concepts, conflicts, and purposes of the FCS mission. He noted that the mission arises from the public charter for the FCS, but unlike its charter, the System's mission has and must continue to change over time to serve the farming needs of rural America. He states that the mission was intended to meet an ongoing purpose: to be a reliable source for available credit at reasonable rates for all reasonable purposes for the nation's agricultural rural areas.

With the 1971 Act, the FCS banks took over the day-to-day leadership of the System, and in the mid-1980s, FCA's role shifted towards that of an independent regulator. The banks recentralized the System and oversaw the expansion of FCS lending through this period. Swackhamer noted that, since the collapse and financial rescue of the System in 1987-89, the associations have become more autonomous, which has reduced the leadership role of the FCS banks.

As the associations become more independent, they are less likely to share a common sense of mission, or even to accept the need for a public policy mission at all. However, with a decentralized structure, emergency situations may pose significant leadership challenges for the associations. Swackhamer also noted that FCA's role of watchdog might expand with the emergence of stronger and more independent associations.

Looking more closely at the System's future, the life cycle of GSEs can go in 4 directions, including:

- privatizing (e.g., Sallie Mae);
- becoming a utility (e.g., the TVA) ;
- dissolving (e.g., the FCS Assistance Board); or
- adapting its mission to meet the changing needs of its constituency.

Swackhamer argues that the FCS has adapted its mission to fit its changing circumstances and it has done so very well. In part, the System has been successful at doing this because of its cooperative structure allowing the owner/borrower to directly influence its adaptation.

Given the natural conflict between private ownership/profit interests versus public purpose/mission, Swackhamer asked if equal weight should be given to owner interest and the public interest as the price of a partnership. He concluded that the cooperative character of the System, if preserved through cooperative tax and patronage dividend benefits, could allow it to fulfill its the public mission while maintaining some of the benefits of privatization. But the System and FCA must be prepared to fill any leadership vacuum that may arise in this dynamic operating environment.

Financing the Needs of Rural Communities

Supporting rural communities has long been viewed as vital to the success of agriculture. Rural communities provide the needed infrastructure and supply systems that allow agricultural producers to thrive. Agriculture and rural communities are so interdependent that Congress expressly provided that the mission of the FCS was to provide sound and constructive credit to both agriculture and rural areas.

FCA Board Member Ann Jorgensen led a group of FCS representatives through a discussion of the needs of rural communities and residents, current market trends, and tools that help the FCS better serve its rural customers. She identified three key areas where agriculture and rural communities need a greater supply of credit—value-added agribusiness, rural infrastructure, and rural housing.

The financing of value-added agribusinesses creates off-farm employment opportunities that supplement family farm income. Rural infrastructure projects could significantly help rural communities prosper and grow. Many rural areas desperately need new and improved services and amenities to help them compete in today's environment, especially "broadband" telecommunications systems.

As the GSE for rural America, the System plays a big role in funding quality affordable housing in rural areas. Improving rural America's housing stock attracts business and industry to rural America. These businesses provide an ongoing source of off-farm income that helps agricultural producers diversify and stabilize their incomes.

Jack Batchellor discussed how First Pioneer Farm Credit meets the needs of its rural customers by helping them expand into new businesses. Many producers are finding excellent opportunities in related farm businesses such as feed, equipment, fertilizer, and other supplier businesses that support their farm business. First Pioneer also tries to focus on all aspects of the customers business, and looks for opportunities to use various guarantee programs.

Jim Garrison of FCS of Mid-America highlighted the benefits of consumer[1] lending in rural areas. Their consumer lending portfolio provides them with some stability to help offset risks in the rest of the loan portfolio. Garrison noted that their consumer lending portfolio has consistently experienced very low nonaccrual and charge-off rates over the years.

Tom Griffin of AgFirst ACB stressed that high-quality, affordable housing helps stabilize rural communities that support the needs of agricultural producers. AgFirst has a strong commitment to helping develop a sustained secondary mortgage market for rural housing, part-time farming, and agricultural real estate loans. They operate a nationwide loan purchase program as a certified pooler for Farmer Mac and a lender/servicer for Fannie Mae. The secondary market sales enhance AgFirst's ALM position and improve its return on capital through lower capital requirements.

YBS and Minority Farmers

Each FCS institution has a statutory responsibility to develop programs for young, beginning, and small farmers. They also have a responsibility not to be discriminatory in their lending practices. This often requires outreach efforts to ensure minorities are not ignored. Large pockets of minority and female farm operators present special opportunities for System lenders. Tom McKenzie, who chaired the session, and all the present-

1. Lending to farmers or part-time farmers for non-farm purposes.

ers from the System concluded that lending to YBS farmers is not only good for business, but it is the right thing to do.

David Woolfolk, FCS of Northeast Kansas, was a leader in helping to implement the legislation of the 1980s. He provided an historical perspective on YBS programs and explained why these initiatives continue in the System today.

Why seek out YBS Farmer Relationships?

- **It's a legislated mandate.**
- **It's an FCS initiative.**
- **It's good for business.**
- **It's the right thing to do.**

Source: Woolfolk Presentation

Gary Dyer, Southwest FCS, chairs the System's advisory work group on YBS farmers. He discussed the "Young and Beginning Farmer Rancher Program" implemented by his association, which uses a two-prong strategy. One features special lending programs with liberalized equity standards (but not repayment standards). The other provides a 2-year training program to improve the managerial and operational abilities of young, potential farmers.

Lynn Bedard, Office of Thrift Supervision, provided a perspective on lending to minorities by commercial banks. She described the characteristics of successful outreach programs and emphasized the importance of strategic partnering with minority groups as a way to penetrate these markets. She also emphasized that to properly implement minority outreach programs, the Board of each institution must be actively involved in the process.

Ensuring Borrower Rights

The Farm Credit Act contains specific provisions to protect the rights of agricultural or aquatic producers who borrow from System banks and associations. FCA developed regulations to implement these statutory borrower rights in 1988. These regulations address several borrower rights issues, including distressed loan restructuring, the right of first refusal, and the review of adverse loan actions.

Gary McNeely, FCS of Southern California, discussed the benefits of the borrower rights regulations. He also noted that the distressed loan notifications that System institutions must send distressed borrowers often result in receiving current information that can be used to address weaknesses or problems in the loans. McNeely acknowledged that while the borrower rights requirements can "frustrate" lenders, they also serve to "open the door" for communicating with distressed borrowers.

Ellen Huntoon, USDA, discussed the environment that existed when Congress drafted the legislation on borrower rights. Agricultural producers were going through tough times, with decreasing land values and increasing numbers of farm foreclosures. She stated that the borrower rights were enacted to ensure farmer-borrowers were heard during these difficult times—and were not a platform for borrower advocacy. She noted that the Agricultural Act of 1987 included provisions on the use of mediation for facilitating debt restructuring proposals. Huntoon discussed the use of mediation in Iowa to illustrate how this alternative dispute resolution technique, which introduces a third party into the process, has benefited agricultural borrowers and lenders.

David Hoelmer, AgStar FCS, provided an overview of the borrower rights regulations and discussed the impact they have had on System lenders. Hoelmer agreed with Huntoon that mediation works well and noted its success in Minnesota for addressing borrower loan disputes. While acknowledging the benefits of borrower rights, he also suggested some areas for possible revisions, such as the need for flexibility in implementing the borrower rights requirements when "sophisticated" borrowers are involved. He noted that in certain transactions such as large debt syndications, sophisticated borrowers should be able to waive these rights to help make their syndications more acceptable to financial markets. Hoelmer stated that borrower rights are often an impediment in these situations because the regulations do not permit borrowers to waive their rights.

The panelists recognized the need to periodically review the borrower rights regulations and believed FCA would benefit from the System's experience with the existing requirements as it considers revising the regulations.

Managing Customer Relations in Difficult Times

The first step towards maintaining good customer relations in stressful times is to realize that they are part of a bigger picture. Jerold Harris, CEO of the FCB of Wichita, emphasized that successful relationships do not begin or end with the event that caused the stress. Rather, customer relations are a dynamic process routinely embraced during good times and bad.

Dr. William Heffernan, from the University of Missouri, talked about how reactions to the stress of losing the family farm affect every aspect of a borrower's life. How well the lender understands and reacts to this stress is key to maintaining a productive long-term relationship. A dependable lender, who is creative in stressful times, can generate significant goodwill that will contribute to successful long-term relationships. Bill Clayton of AgFirst FCB reminded the group that because FCS institutions are cooperatives that are owned by the borrower, members may expect more help than they would from investor-owned businesses.

Not recognizing borrower stress, nor being prepared to deal with it, can have very negative consequences. Jerold Harris observed that in the mid-80s, the FCS was not well equipped to help borrowers because of poor training and weak risk identification skills. This inability to deal effectively with their customers resulted in borrower rights legislation that he believes the System could have avoided.

The development of a comprehensive strategy and plan is critical to maintaining good customer relations. There must be open communications with borrowers, and early identification of risks and potential stress factors. When difficult situations do occur, proactive and prompt responses can create mutual trust and respect and result in realistic long-term solutions.

Risk Identification and Management

Farmers and ranchers face a myriad of risks in producing and marketing their products. Identifying the source and nature of these risks and developing and implementing appropriate risk management strategies are essential tasks for both borrowers and lenders in today's fiercely competitive environment.

Production Risks

The most fundamental risk that farmers face is simply that the crop doesn't turn out as planned, better known as production risk. Joy Harwood from USDA's Economic Research Service outlined several ways to mitigate production-risk exposure:

- **Diversification:** varying enterprise mix and geographic locations.
- **Cultural practices:** early season varieties, irrigation, staggered plantings.
- **Insurance:** Federal multiple peril, private hail, and livestock mortality.

Harwood noted that while insurance is an important risk management tool, a broader safety net for farmers might include forward pricing, input leasing, custom work, off-farm income, savings, and borrowing.

Jerry Skees, of the University of Kentucky, stated that farmers, insurance companies, reinsurers, bankers, and agribusiness could all benefit from the new risk-management products. However, he warned about the effects of too much public subsidy in insurance programs:

- Greater risk-taking
- Cycle of losses
- Inflated asset values
- Higher land rentals
- Over-investment in the subsidized enterprises
- Negative consequences for the environment

Skees favors price subsidies (dollars per unit of production) over risk-transfer subsidies (vary with units of production and relative risk), because price subsidies reward productivity while risk-transfer subsidies reward those with relatively greater risk.

Price Risks

Joe Glauber, USDA's Deputy Chief Economist, stated that risk management strategies tend to focus on price or yield risk, but what concerns farmers most is revenue or income risk. In some cases, variability in production costs, which are beyond the scope of any farm bill, might pose an even greater risk than income variability. Futures, options, and cash forward contracts can provide stability within a crop year but cannot protect against secular price declines. Glauber warned that it is important not to confuse risk management with income enhancement. Since on-farm income is less than off-farm income for most farm families, risk management strategies that focus solely on farm income have a limited effect.

Gene Martin, of the Arkansas Farm Bureau, noted that farmers consistently spend too much time on production issues and not enough on marketing.

For a successful marketing plan, he recommends they:

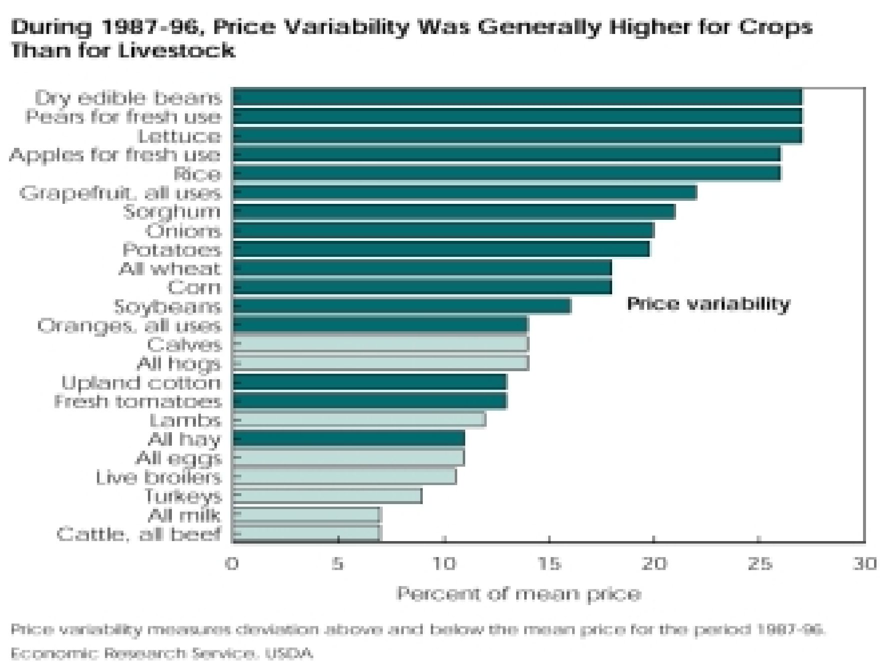
- Establish a realistic goal
- Identify the decision-making environment
- Develop price outlook
- Consider costs of production
- Consider risk-bearing ability
- Avoid emotional decisions
- Control ego

In Martin's view, timing is the key to success—when to take loan deficiency payments or market gains; when to price the crop and how to set basis, lock in futures, or do both. Doing things right can make a huge difference in net revenue.

Market Risks

Gregg Doud of World Perspectives, Inc., stressed the importance of understanding our competitive position in world markets to better understand the significant risks faced by both borrowers and lender. Examples of important economic developments are:

- Sharp increases in production in both exporting and importing countries
- Sluggish economic growth in some key importing countries
- Appreciation of the U.S. dollar against foreign currencies
- Declining U.S. market share in world trade
- Significant buildup of stocks in major exporting countries



Source: Goodwin Presentation

- Depressed commodity prices and reduced cash receipts
- Increased dependence on government payments.

The most serious threat to U.S. competitiveness in global commodity markets lies in countries like Brazil and Argentina that have significant production potential. The rapid adoption of new technologies in these countries and recent infrastructure investments have positioned them to respond to any further growth in trade.

Marketing risks in agriculture, according to Darrell Holaday of Advanced Market Concepts, differ from any other sector of the economy because of what he calls "production reality" and "psychological reality." The psychological reality — "I can't sell before I produce" or "What's my neighbor doing" — significantly limits farmers' ability to better manage their market risks.

Like the farmer, the lender's focus needs to change from a production orientation to a marketing one. The key to a lender's survival is to fully understand what it takes to make the customer successful. Holoday chided lenders for their reluctance to extend credit to cover margin calls during periods of rising commodity prices.

Environmental Risks

Barry Goodwin of North Carolina State University emphasized that environmental issues — soil erosion, chemical and fertilizer runoff, animal waste management, and GMOs — are central to today's policy debate. He noted that the amount of animal waste produced in this country equates to 5 tons per person. He warned that policies like deficiency payments, disaster payments, and crop insurance might actually encourage production in areas with more fragile soils and riskier yields. Goodwin concluded that people will engage in riskier practices when they know they have insurance or other support programs backing them.

Tom Hebert of Capitolink, LLC, described how Federal and state environmental regulations of agriculture were becoming more extensive with each year and challenged lenders to become familiar with these laws and the associated risk management issues of their borrowers. He specifically mentioned the Clean Water Act, Clean Air Act, Superfund, the Food Quality Protection Act, and the Endangered Species Act as they relate to agriculture, and noted that states generally make requirements more restrictive than the Federal government. Hebert concluded that more restrictive environmental laws were resulting in higher production costs, more litigation, increased uncertainty, and could be contributing to greater concentration in the farm sector. Under these conditions, some operators find that permits provide a degree of certainty and reduce exposure to frivolous harassment.

Technological Risks

Advances in biotechnology are yielding a new generation of products with exciting implications for farmers and consumers. Peggy Lemaux of the University of California-Berkeley noted that many of the early GMOs focused on input traits like disease resistance. The newest products on the horizon are "nutraceuticals," that use food as delivery vehicles for medicine, such as edible vaccines (see chart below). The new bio-based economy will use plants in a whole new way—to make products, like biodegradable plastics, which are currently being made from "nonrenewable" sources.

Adrienna Logan of Con-Agra, Inc., stressed the importance of consumer acceptance to U.S. agriculture. She described the key to consumer acceptance as two-fold. First, there is a need for continuing education that fully addresses both the benefits and risks of new products and technology. The lack of education and unbalanced reporting in Europe has had disastrous results for our exports. Second, there is a need for a new set of regulatory tools and procedures so that consumer resistance does not hinder new product development. Logan talked about Con-Agra's success in developing an information system that allows them to "track information from the farm gate to the dinner plate."

Ralph Hardy, President, National Agricultural Biotechnology Council, spoke of our transition from a fossil-based economy to a bio-based economy in the 21st century as a result of an explosion of discoveries in the life sciences. Last year, 5 percent of the corn crop went into bio-based fuel production. Biotechnology could provide the greatest opportunity that agriculture and rural America have ever seen as farmers produce, not only our food and fiber, but also the basic feedstocks for fuel, chemicals, and medicine.

New Bio-Based Products

Product	Process	Benefit
Golden Rice	ADD vitamin A	Nutrition source in 3rd world
Potatoes	ADD proteins	Increase nutritional values
Wheat	REMOVE allergens	Decrease common allergic reactions
Fuel	CREATE bio-based fuels	Help the environment
Algae	CREATE hydrogen gas	New energy source
Copper & Uranium ores	Biomining using plants and microbes	Less invasive to the environment
Indian Mustard	Remediation	Removes minerals & contaminants from ground soil
Bananas	ADD nutrients	Use as vaccines
Animal feed	ADD proteins	Substitute for antibiotics

Source: Lemaux Presentation

Risk Models

Richard Gallagher of Texas A&M University highlighted the expanding risk relationships between farmers and lenders. He encouraged lenders to use the latest analytical frameworks (or models) to assess both credit and portfolio risks in their institutions. A wide selection of risk-management software products is available from land grant universities and commercial vendors.

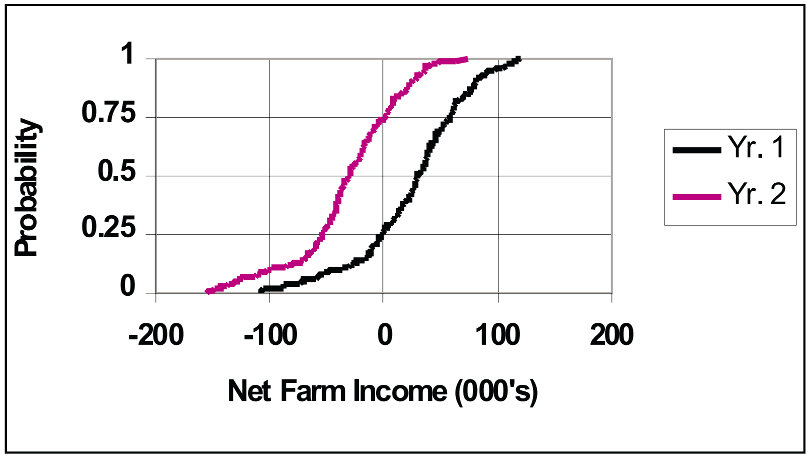
Simple correlation analysis of price and yields would help farmers select a less risky crop mix, while cumulative distribution functions of net farm income and loan collateral margin would help loan officers make more informed decisions (see graphs).

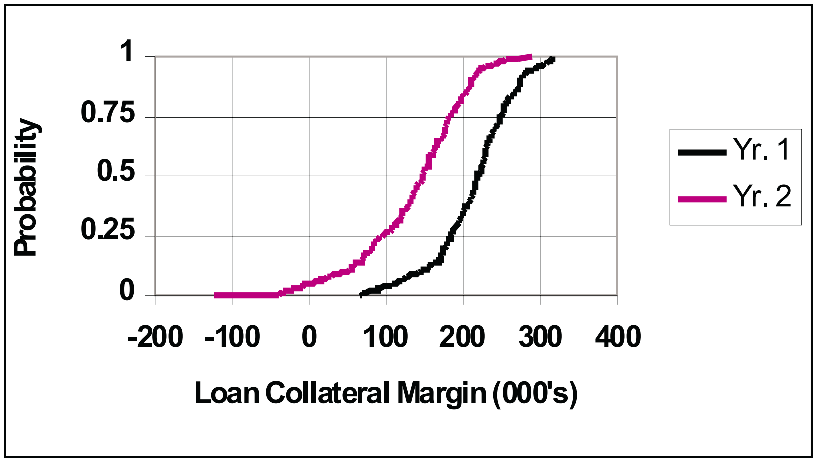
Gallagher stated that:

- Spreadsheet models can help lenders work with farmers to better handle "what-if" questions.
- Risk management models improve our understanding of the complex interactions between categories of risk.
- Range estimates are better than point estimates in measuring risk.
- Lenders need to use a probabilistic approach in loan decisions.
- Risk-based producer analysis is the key to credit and portfolio risk analysis.

Finally, Gallagher said it was the duty of the Farm Credit System to get risk models into producers hands to help them make better production and marketing decisions which would in turn help lenders make more informed loan decisions.

Cumulative Distribution Functions: Farmer vs. Lender





The CDF allows measurement of the yearly probability of specific income levels for the farmer and the corresponding probability of specific loan collateral margins for the lender. For example, in year 2 there is a 75% chance of an income loss with a 10% chance of a negative loan collateral margin.

Source: Gallagher Presentation

Policy Issues

U.S. Secretary of Agriculture Dan Glickman keynoted the symposium, talking about present and future U.S. farm policy, the current political climate, and what's happening in the legislative arena. His comments on farm policy struck a resonant chord as speaker after speaker noted the shortcomings of current farm policy and its inability to address the stressful circumstances U.S. producers face today. Under Secretary Gus Schumacher, Congressman Collin Peterson, Sparks Senior VP JB Penn, RMA Administrator Ken Ackerman, and Louisiana Agriculture Commissioner Bob Odom each in turn noted how current farm policy has failed

PRODUCERS' PERCEPTIONS OF LENDERS' ATTITUDES

Attitude	Crop Insurance	Forward Pricing
Recommends	48%	31%
Discourages	2%	1%
Doesn't Care	24%	32%
Doesn't Know	27%	36%

Lenders perceived as only moderately supportive; more lender education on RM tools is needed.

Source: Schumacher Presentation

to provide farmers an adequate safety net. Interestingly, none suggested a repudiation of the "Freedom to Farm" options provided by the '96 Farm Bill. However, each in turn spoke to the problems of worldwide financial crises, record worldwide production and related surpluses, U.S. agricultural trade competitiveness, and the inability of the farm safety net to adequately protect domestic producers against disasters. Perhaps as interesting was the almost universal recognition that no apparent solution to the farm policy problem is on the horizon. Moreover, recent emergency spending programs, totaling $23 billion over the last 3 years, have provided temporary fixes only and done little to solve longer-term policy issues.

Farm Policy Principles

Looking ahead, Secretary Glickman noted that the next farm bill would need to address these problems in order to win bipartisan support. He then identified several guiding principles by which a farm bill should be measured. These guiding principles include:

(a) equity and fairness for all producers, regardless of race, gender, or ethnic origin,
(b) conservation in all phases of agricultural activity,
(c) a more efficient and cost-effective emergency assistance program (both Glickman and Peterson criticized the AMTA-type formulas used for allocating emergency assistance as being an ineffective method of assisting distressed producers),
(d) program diversification that includes all agricultural products, not just wheat, corn, cotton, and other feed grains,
(e) improved rural economies,
(f) a recognition that credit is a critical element in effective farm policy, and
(g) an increasing share of the consumer's food dollar going to the farmer.

Regarding this latter point, Glickman explained the need for "new market opportunities for farmers with additional investments in cooperatives" and the promotion of "farmer cooperatives, direct marketing, and farmers markets." He called for "encouraging the use of crops in the production of renewable energy sources" and "greater opportunities for farmers in value-added, consumer-ready goods, [and] organic agriculture." Interestingly, 5 percent of last year's corn crop went into ethanol production.

Current Farm Policy

As Ken Ackerman pointed out in his remarks, the symposium coincided with one of the most productive legislative periods for agriculture in the areas of trade, crop insurance, and emergency assistance.

Secretary Glickman highlighted the importance of the China Permanent Trade Relations Bill just passed by the House and the Africa trade bill recently passed by Congress as significant milestones for domestic agricultural producers. He highlighted the relaxation of trade sanctions and noted that last year's overseas food aid was 8 million metric tons, or 4 times that of the previous year. He noted that $5 billion in export credits were made available last year in countries that otherwise would not have purchased U. S. agricultural commodities. Last year we also invested $90 million in the Market Access Program. The payoff for these efforts was an increase in exports for the first quarter of this year and the first projected increase in year-to-year farm exports since 1995.

J.B. Penn and other speakers highlighted the growing dependence on international markets (from 14 percent of cash receipts in 1970 to 27 percent in 1998) as the most prominent long-term policy risk facing agriculture. In fact, Gus Schumacher pointedly noted that any increased domestic productivity either went to foreign consumers or went into storage. Congressman Peterson suggested that current agricultural trade policy was so prejudiced against U.S. producers that the U.S. should adopt a protectionist policy similar to the European Union in an effort to force the Europeans to the bargaining table.

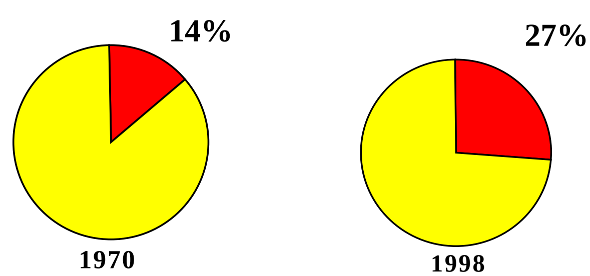
Farm Safety Net Policy

Secretary Glickman stated that the crop insurance reform bill, passed the same day he addressed the symposium, would help improve the farm safety net. He, Ken Ackerman, and Congressman Peterson noted that the bill makes crop insurance more affordable by subsidizing buy-up coverage, improves coverage by authorizing a pilot livestock insurance program and improves coverage of specialty crops. It addresses deficiencies in the program by providing for multi-year losses, expanding risk management education, and improving crop coverage for non-approved crops.

J.B. Penn and Ken Ackerman noted that although market conditions for agriculture next year are unlikely to improve significantly, additional emergency assistance next year will be unlikely now that Congress has provided an additional $8.2 billion over the next 5 years for disaster assistance. Congressman Peterson further noted that while the just-passed crop insurance bill goes a long way toward correcting deficiencies, it needs much more reform. He hopes Congress will continue to address these needed reforms next year.

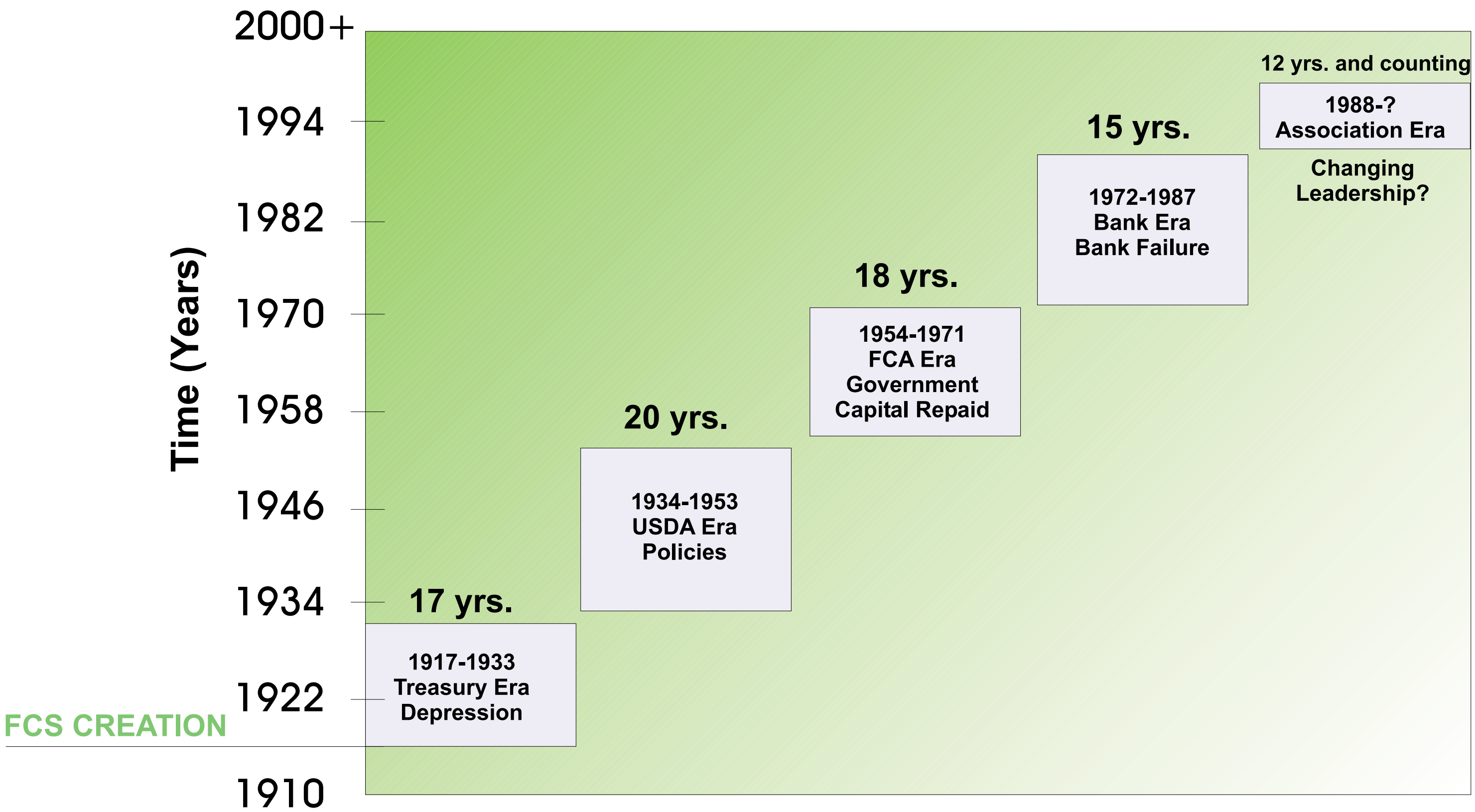
Schumacher and Ackerman challenged agricultural lenders to be more active in addressing the needs of borrowers by educating them and assisting them in the effective use of risk management tools, including crop insurance. As shown in the table on page 6, a recent study of agricultural producers revealed that they perceive at least half their lenders either don't care or don't know about some of the most common risk management tools.

Exports as a % of Crop and Livestock Sales



Source: Penn Presentation

THE FARM CREDIT SYSTEM 83 YEARS OF EVOLUTION



Source: Swackhamer Presentation

Farm Policy Risks

J.B. Penn identified the most prominent near-term policy risks as a sizable drop in farm disaster assistance in 2001 and an uncertain economic/fiscal setting for the next farm bill. The longer-term risk he said was the lack of a coherent international trade policy for agriculture. Like Secretary Glickman and Congressman Peterson, Penn noted that high levels of disaster assistance over the last several years have not been properly targeted to those in need and are unlikely to be sustained in the future. Borrowing from an old Chinese proverb, Penn likened this to placing farmers on the back of a tiger with no dismount strategy.

Based on recent USDA data, Penn showed how commercial farms (as compared to smaller farms) tend to obtain above-market prices for their commodities, are more sophisticated in their use of risk management tools, and tend to have lower costs of production. In fact, commercial farms can generally survive without AMTA or disaster payments. This not only makes smaller farmers higher credit risks, it makes them more susceptible to merger and consolidation. However, as Congressman Peterson noted, defining the family farm and placing targeted assistance where it is most needed is very difficult, and increases the cost of agricultural assistance. Several speakers went one step further in noting that the high cost of recent emergency assistance will make it increasingly difficult to obtain needed congressional support for the next farm bill.

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