

OPINION

Farm Credit System faces danger

BY BERT ELY

The Farm Credit Administration is moving rapidly to implement its revolutionary new philosophy to promote potentially destructive competition among Farm Credit System lenders.

The federal regulator quietly adopted its philosophy in mid-July. Now, it has dropped the next shoe by issuing a proposed rule to implement the new philosophy.

The proposal faces a 30-day congressional review. Not surprisingly, it was sent to Congress just before legislators adjourned for the year.

This means one of the most important changes in the history of the Farm Credit System will not get much congressional consideration this election season.

Once the congressional review period ends, the proposed rule will be published in the Federal Register for 90 days of public comment before it is made final.

Essentially, this rule will give seven of the eight Farm Credit System banks (the St. Paul Bank for Cooperatives is the exception) as well as the 193 lending associations the ability to lend or provide "related services" anywhere in the United States.

Each institution that begins to lend "beyond its designated territory must adopt a board policy and a business plan that adequately guide these activities."

One can reasonably infer that the Farm Credit Administration will not have to approve these expansion plans. Instead, "FCA examiners will evaluate each (expansion) program in view of the potential risks and possible effects on the institution's financial condition."

Since the Farm Credit Administration is becoming more of a promoter and less a regulator of institutions in the Farm Credit System, how aggressively can it monitor the expansionist urges of the institutions' chief executives as they fumble their way, at taxpayer risk, outside their designated lending territories?

Taxpayers, bankers, conservative institutions in the Farm Credit System and staffers at the Farm Credit Administration

on rural America.

Of the 200 institutions eligible to lend outside of their designated territory, it is most likely that only a few larger institutions will take up this challenge.

CoBank, with almost \$19 billion of assets, \$1.4 billion of capital at the end of last year, and 11 offices across the country, is well-positioned to begin cherry-picking larger agricultural credits everywhere.

AgriBank, which serves 12 states, mostly in the middle and upper Midwest, is almost as big as CoBank and, therefore, could expand readily into other states.

FCS of the Midlands, a pair of very aggressive associations that serve Iowa, Nebraska,

damental congressional objective for the Farm Credit System, which is "to encourage farmer- and rancher-borrowers' participation in the management, control and ownership" of the credit system.

Because of the joint and several liability of Farm Credit System debt, aggressive institutions would place more conservative institutions at greater risk.

These mega-institutions would also pose a severe insolvency threat to the Farm Credit System Insurance Fund, which had \$1.36 billion of assets on June 30.

As taxpayers learned to their dismay in the 1987 bailout of the Farm Credit System, they will pick up the pieces if these mega-institutions become reckless lenders to rural America.

Although the proposed competition rule gives ample lip service to the notion that Farm Credit System institutions should "serve eligible and creditworthy farmers" as well as "be responsive to the needs of young, beginning and small farmers" that would be less the case

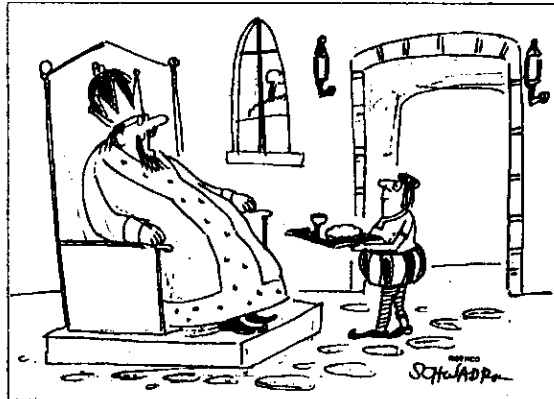
than it is today.

Ironically, the Farm Credit System and its regulator may be the largest long-term losers from this policy.

The lack of ownership accountability for very large lenders in the Farm Credit System, plus the absurdity of showering them with enormous tax benefits (\$430 million in 1997), eventually will lead to their privatization.

Before then, questions about the ability of the Farm Credit Administration to regulate these mega-institutions will increase as it becomes more evident that they have captured their regulator.

Hence, the Farm Credit Administration would shrivel and then disappear, perhaps to be folded into a super-regulator for all government-sponsored enterprises.



"Not chicken a la king again!"

South Dakota and Wyoming could easily expand southward into the Wichita and Texas districts, which are the most vulnerable to cherry-picking.

In order to build market share, the expansionist institutions would have to cut interest rates below local Farm Credit System lenders.

This competition could set off a price war within the system, which would make it even harder for commercial banks to compete for agricultural loans, particularly for real estate loans, where the Farm Credit System has a tax advantage of 107 basis points, or 1.07 percentage points.

This competition also will drive further consolidation within the Farm Credit System as large, aggressive lenders crush smaller, less efficient associations.

Because of consolidation, within a few years most Farm Credit System loans might be