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Subcommittee on Conservation, Credit, Energy and Research
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Mr. Chairman and members of the Subcommittee, thank you for the opportunity to appear before you to discuss credit conditions in rural America, focusing on the current status and operations of the farm loan programs at the Farm Service Agency (FSA).

Credit Conditions

Reports from the Federal Reserve and other sources indicate there is a tightening of credit for farmers and ranchers around the country. A combination of limited or negative returns in much of the livestock industry, reduced profit margins in crop production, and increased sensitivity to credit risk has caused many farm lenders to raise their credit standards, reduce the amount they are willing to lend in agriculture, or both. Many lenders report that increased scrutiny from regulators has caused them to raise credit standards significantly.

Activity in FSA's farm loan programs certainly indicates that less commercial credit is available to farmers at the present time. Farm Loan programs demand is usually counter-cyclical to the general farm economy; when the farm economy is strong, farm loan activity is flat. During times of financial stress in the farm economy, demand for farm loan program loans increases. This makes sense, since a basic requirement to qualify for

the programs is to be unable to meet the criteria for commercial credit. This year, the programs are experiencing demand levels that have not been seen in over 20 years. As of May 30, 2009, demand for direct operating loans was up by 81 percent, demand for direct ownership loans was up 132 percent, and demand for guaranteed operating loans has increased by 31 percent An unusually high number of direct operating loan applications are from new customers this year. As of May 26, 45 percent of the direct operating loans approved in FY 2009 were for customers who did not have existing FSA operating loans. Normally, that number is about 20 percent.

Performance and Portfolio Condition

Farm loan programs continue to emphasize the importance of processing applications in a timely manner. Between FY 2001 and FY 2008, farm loan programs reduced its direct loan application processing timeframes by thirteen days (30 percent), and reduced guaranteed loan processing timeframes by five days (28 percent). As of May 30, the average time from applications receipt to final decision for direct loans was 27.7 days, and for guaranteed loans, 8.55 days. It is remarkable that even though loan demand has surged, there has been no deterioration in application processing time. This is a testament to the dedication of FSA field staff and the effectiveness of the IT solutions farm loan programs has deployed.

The quality of our portfolio has continued to improve, due in large part to our modernization efforts, better customer service and the dedication of FSA employees, as well as the much improved farm financial environment of the past seven years. At the

same time, we realize that given the increased financial stress the agriculture economy and the increased workload resulting from a larger case load, portfolio performance is likely to somewhat deteriorate in the future. We are committed to using all the authorities available to assist borrowers and will strive to minimize any deterioration in portfolio performance.

Loss Rates. In FY 2008, losses in the direct loan program fell to their lowest level since 1986 – just 1.7 percent (Chart 1).

Losses for FY 2008 in the guaranteed loan program were 0.3 percent, the lowest rate since we began monitoring this trend in 1985 (Chart 2).

Delinquency Rates. As with losses, the direct loan delinquency rates are at historic lows at 6.5 percent for FY 2008 (Chart 3). This is the result of steady and dramatic decreases from a 23.8 percent delinquency rate in FY 1995. The decrease was facilitated by expanded authority, since 1996, to offset federal payments, salaries and income tax refunds to delinquent borrowers.

In the guaranteed program, the FY 2008 delinquency rate was 1.18 percent, the lowest since 1995 (Chart 4).

Foreclosures. Foreclosure rates continue to be very low in the direct loan program. In 2008, FSA participated in 169 foreclosures, including cases initiated by other lenders

against individuals who also had loans with FSA. This is compared to 311 foreclosures the agency participated during 2003. This represents less than one-fourth of 1 percent of the agency's direct loan caseload.

Inventory Properties. Inventory farm properties – those that have come into government ownership through voluntary conveyance or foreclosure – are also at historic lows with just 79 farms covering 9,600 acres in FY 2008. In 1995, FSA held nearly 1,800 farms covering 598,000 acres. Many of those inventory properties were sold to established and beginning farmers, providing those individuals with prime opportunities to expand or create new operations.

Graduation Rates. Federal law requires FSA to "graduate" its borrowers to commercial credit when they have made sufficient progress to be able to qualify for loans from other lenders. They are assisted by the agency in refinancing their direct loans with FSA guaranteed loans from commercial lenders. Some 2,918 direct loan borrowers were able to graduate in FY 2008, which is consistent with graduation rates over the past 5 years.

Equitable treatment and participation

Secretary Vilsack has been extremely clear that improper and inequitable treatment of those that USDA and FSA serve will not be tolerated. On April 21, 2009, he announced several actions in a comprehensive approach to ensure fair treatment of USDA employees and constituents. These actions included an initiation of several improvements in processing civil rights complaints, requesting an external analysis of program delivery by

USDA service center agencies, and 90 day suspension of FSA farm foreclosures, which has provided us time to review these files to ensure that all producers have received their statutory protections. I, and all the members of the FSA management team remain fully committed to equal access and opportunity for all those FSA serves. I will closely monitor the operations of farm loan programs and all other FSA programs to assure our producers, program applicants, and employees receive fair, equitable treatment. I want to update you on a few key activities dealing with these important issues.

Foreclosure review

As you know, section 14002 (b)(1) of the Food, Conservation, and Energy Act of 2008 (the 2008 Farm Bill) required the USDA Office of Inspector General (OIG) to conduct a review to determine whether foreclosure proceedings, with respect to farm loans made to socially disadvantaged farmer and ranchers, were consistent and in conformity with the applicable laws and regulations governing foreclosures. Foreclosure is never a desired outcome. When an account ends with foreclosure, both the agency and the borrower have failed. However, I am glad to report that the OIG review found no instances of inconsistency or improper treatment of any borrowers in that unfortunate circumstance. These results speak to the commitment of farm loan program managers and field staff to assure that all applicants and borrowers are treated fairly and equitably. I am committed to maintaining, and where possible further improving performance in this area.

Program participation

An examination of the composition of FSA's loan portfolio indicates that FSA finances minority farmers at a much higher rate than those groups' proportion of the farm population (Chart 5). For example, while the 2007 Census of Agriculture indicates that 1.40 percent of farm operators are Black or African American, this group makes up 3.42 percent of FSA's direct loan portfolio, almost 2.5 times the proportion in the total farm population.

FSA has significantly increased the amount of loan funds provided to socially disadvantaged applicants. Between 1995 and 2008, the FSA direct SDA caseload increased from 3,260 to 14,068. Between 1997 and 2008, the FSA guaranteed socially disadvantaged caseload increased from 1,730 to 3,014.

In the 2008 Farm Bill, Congress re-affirmed the focus for FSA programs on beginning farmers and ranchers. FSA continues to strive to reach more beginning farmers and has increased the amount of loan funds provided to beginning farmers and ranchers. The FSA direct loan beginning farmer caseload increased from 3,474 in 1995 to 18,785 in 2008. Guaranteed caseloads for beginning farmers and ranchers were first reported in 1997. The FSA guaranteed beginning farmer caseload increased from 3,617 in 1997 to 8,648 in 2008.

IT Modernization

FSA has made significant strides in modernizing the IT systems used in farm loan programs delivery and management. Performance in delivery and operations this year

illustrates the high level of performance and functionality of farm loan programs IT systems. So far, in FY 2009, FSA has processed 41 percent more loan requests than in FY 2008, but service levels have not declined. Average processing times for direct and guaranteed loan applications have been fairly steady. This is a tribute to the dedication and diligence of farm loan programs field staff, but without the modern IT systems they could not have maintained an acceptable level of service. For example, Business plans for FSA borrowers are now processed through a Web based state of the art system. This off-the-shelf IT solution provides access to "real time" data on our portfolio while sharing data among our automated systems. This system also provides a reporting option. This system has allowed our loan officers to conduct more extensive and meaningful financial analysis of our borrower's farm businesses reducing risk to the government while enhancing their opportunities for success and graduation to commercial lending. FSA loan officers now order applicant credit reports from the three major reporting companies through this system as well, which also expedites processing.

Farm loan programs has also implemented modern, web-based systems to manage the loan application, approval, and funding process. This system provides real-time management data on application activity and allows the Agency to better cope with funding problems and act quickly when necessary. For example, when the Agency received supplemental funding in the American Revitalization and Recovery Act, over 2,000 farmers were waiting for desperately needed direct operating loans to pay 2009 planting and other farming expenses. When funds were made available to FSA, the agency was able to process obligations over night, and funds began flowing into farmers'

bank accounts only 3 days later. I am proud to say that FSA was one of the first agencies in the government to get stimulus funding flowing to those who desperately needed it. The modern, web-based IT systems in place for farm loan programs were a key factor in our ability to provide such timely service.

Currently, we are in the last phase of moving all of our automated farm loan programs systems to the Web. When the project is completed we will eliminate duplicate data collection and farm loan services will be delivered even more efficiently. Our employees will be able to conduct USDA business from any location where there is broadband, WIFI or dial-up Internet access. This will allow us to conduct business with producers at locations and times convenient to them. Additionally, this information will be stored on a centralized server allowing employees to quickly access portfolio information and provide real time management reports. However, there is still additional work to be done. We will continue working to improve our accounting systems to improve their capabilities to capture data and be more easily modified to cope with program changes. These improvements will enhance our capabilities in portfolio management.

Ongoing Challenges

As we look ahead in the ever-changing environment, FSA will face significant and ongoing challenges in the years to come. Some of the most prominent are staffing constraints, term limits, and maintaining program performance and success rates through these difficult times.

Staffing Challenges. We project that approximately 35 percent of FSA's current loan officers will be eligible to retire by the year 2012 and 45 percent can retire by 2014. This potential loss of experienced, seasoned credit experts comes at exactly the wrong time considering the increased workload from this year's influx of new borrowers; and creates the potential for major staffing challenges in the next few years.

FSA farm loan programs has an excellent employee recruitment and training program, but appropriations limit the number of new hires that can be brought into the system at any given time. On average, it requires about two years to hire and train a loan officer in order to provide the level of effective supervision, expertise and customer service needed to maximize every opportunity for success for FSA borrowers. The two year training window for new loan officers complicates an already cloudy staffing forecast.

FSA's portfolio and borrowers could be exposed to financial risk if retirement attrition projections for loan officers are even marginally accurate. A large percentage of FSA borrowers are either beginning farmers or financially stressed borrowers who need financial supervision, especially in these challenging times. FSA loan officers provide this supervised credit which requires a complete knowledge of FSA programs, finances, and agriculture enterprises.

Term Limits. The statute presently limits a borrower to direct operating loans in each of seven years, with an additional one-time, two-year waiver on an individual case basis:

- There are more than 4,800 FSA borrowers who can only receive direct operating loan assistance one more year from the agency; and
- There are more than 7,800 FSA borrowers who can only receive direct operating loan assistance two more years from the agency.

Without FSA direct loan assistance, many of these borrowers may be forced out of farming as they may not have access to the capital necessary for them to conduct their farming operations. Under the current credit environment, it is unlikely that many borrowers reaching their term limits will be able to obtain conventional financing. They will be left with nowhere to turn. It will be unfortunate if these borrowers are forced out of business because they reached their term limits during a period of unprecedented upheaval and uncertainty in the banking and financial sectors.

The statute presently limits borrowers with guaranteed operating loans to 15 years of eligibility, with receipt of a direct operating loan also counting as a year of eligibility for guaranteed operating loans. This provision has been suspended on several occasions; most recently the 2008 Farm Bill extended the suspension through December 31, 2010. How problematic this limit will be when the suspension ends depends on the agricultural economy and availability of conventional credit at that time. As of June 1, 2009, over 3,800 guaranteed loan borrowers would not qualify for additional loan guarantees if the limits were in effect.

Farm loan programs performance over the past few years has been outstanding, with delinquencies and losses near all-time lows. Under the challenging economic and financial environments agriculture faces, it is almost inevitable that program delinquency and loss rates will increase. However, we are committed to use all available options to minimize any increases in program delinquencies and losses.

We are fortunate to have many tools at hand to service accounts and assist borrowers through difficult times. The automated systems I have mentioned will assist us in timely farm planning and exploring many different possibilities to assist borrowers in finding a viable operating plan if that is possible. We have a wide array of loan servicing options available to include restructuring or deferring payments, and even to reduce debts in exchange for conservation contracts in some cases. We expect that our ability to manage our portfolio will only improve as we move forward with IT modernization. However, limited staffing and administrative resources combined with departures of experienced staff will limit FSA's ability to respond to this challenge, particularly if demand for new loans continues at a higher than normal level.

Conclusions

Through modernization efforts, maintaining focus on program objectives, and the hard work and dedication of FSA employees, FSA farm loan programs has made great strides in improving program performance. Loan failures and losses have declined which is a strong indication that the program mission of helping farmers become successful is being

accomplished. At the same time, increased assistance to small, beginning, and minority farmers, reflects remarkable success as well.

However, more challenges lie ahead. Government resources are increasingly limited and the agriculture production landscape is changing. We are experiencing unique conditions in the credit and banking sectors, and to a large extent, in agriculture. These changes pose significant barriers and challenges to the groups that FSA farm loan programs are intended to assist. These issues create major challenges for the agency as well, since the success of the program depends on those whom the programs are intended to serve. To keep pace with these changes, we will continue efforts to modernize the delivery system, and to refine and adjust program requirements and operations to maximize the opportunities for our nation's small, beginning, and socially disadvantaged farmers and ranchers.

Because of our rural delivery system and experienced loan officers, the FSA farm loan programs staff is well positioned to continue the high quality delivery of existing programs and new initiatives to assist small, beginning, and minority family farmers. We look forward to working with this Subcommittee to address the challenges we face in accomplishing this worthwhile mission to strengthen family farmers and rural America.

Thank you for allowing me to share our Department of Agriculture perspective as you address this important issue. I am available to answer your questions now or at any time in the future.

Chart 1

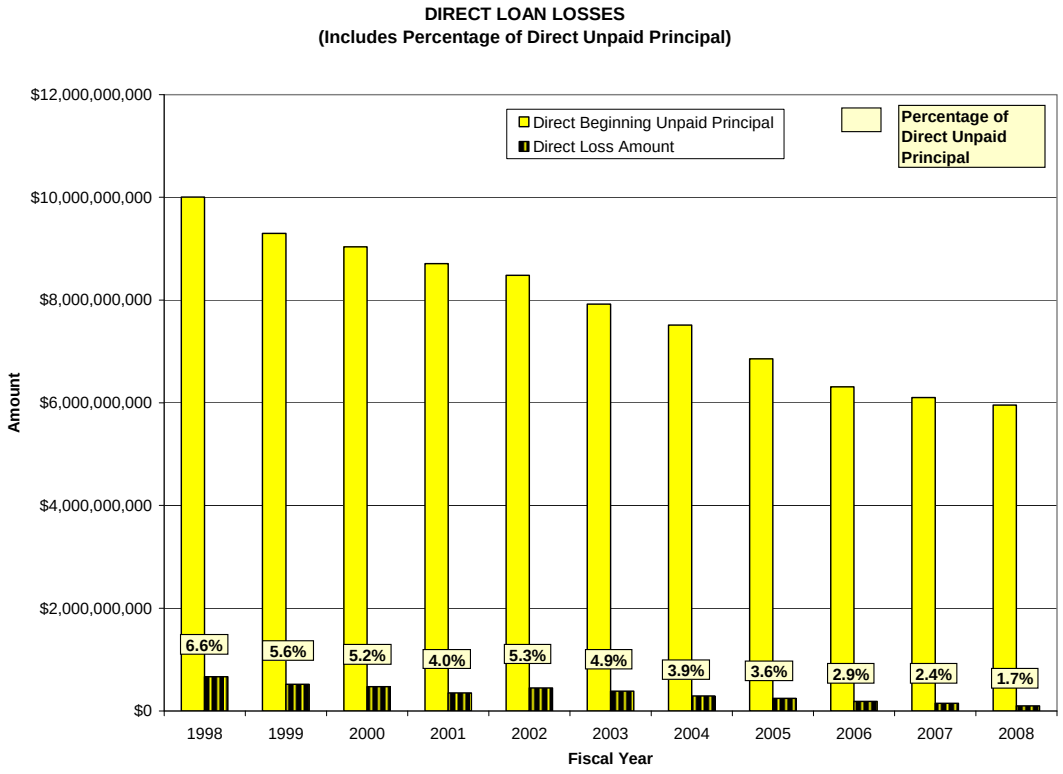
DIRECT LOAN LOSSES
(Includes Percentage of Direct Unpaid Principal)
Direct Beginning Unpaid Principal
Direct Loss Amount
Percentage of Direct Unpaid Principal
$12,000,000,000
$10,000,000,000
$8,000,000,000
$6,000,000,000
$4,000,000,000
$2,000,000,000
$0
Amount
6.6%
5.6%
5.2%
4.0%
5.3%
4.9%
3.9%
3.6%
2.9%
2.4%
1.7%
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
Fiscal Year

Chart 2

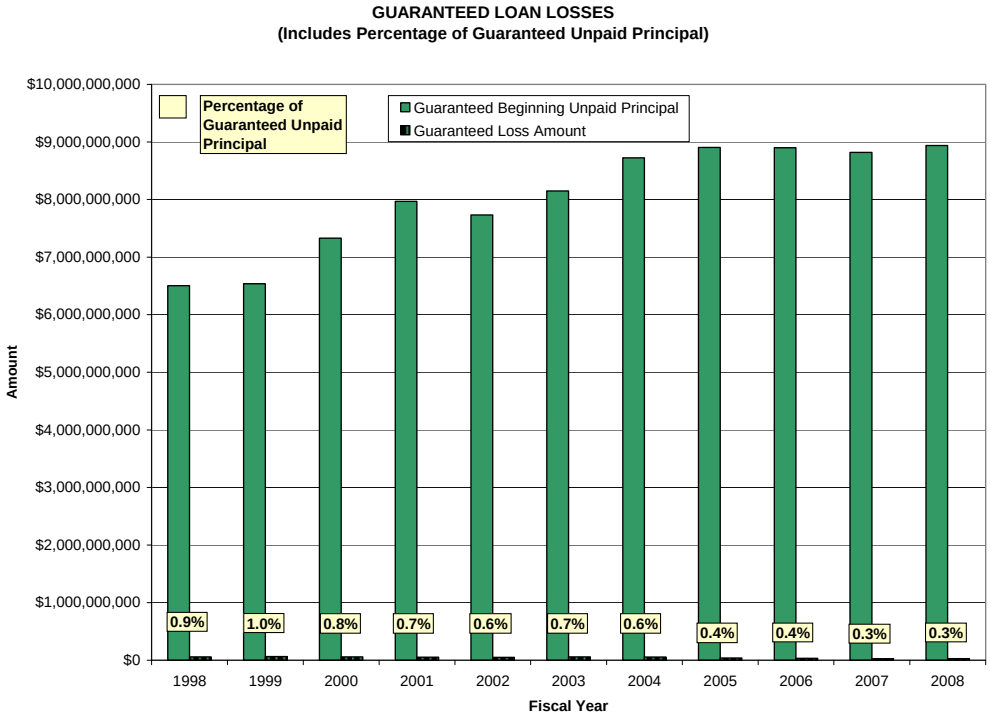

Chart 3

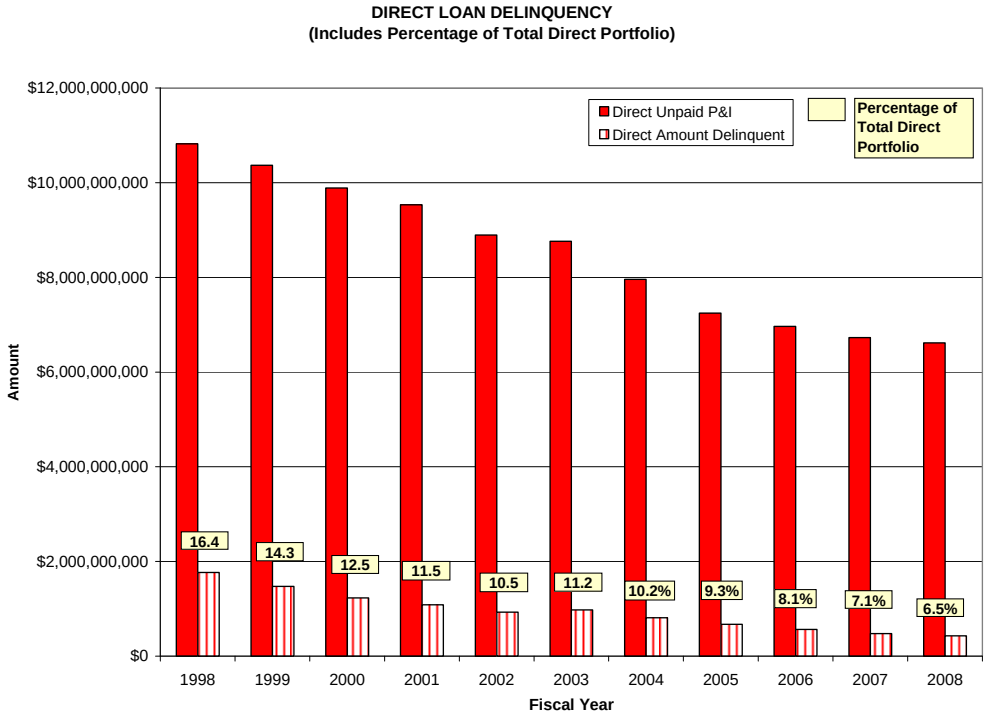

Chart 4

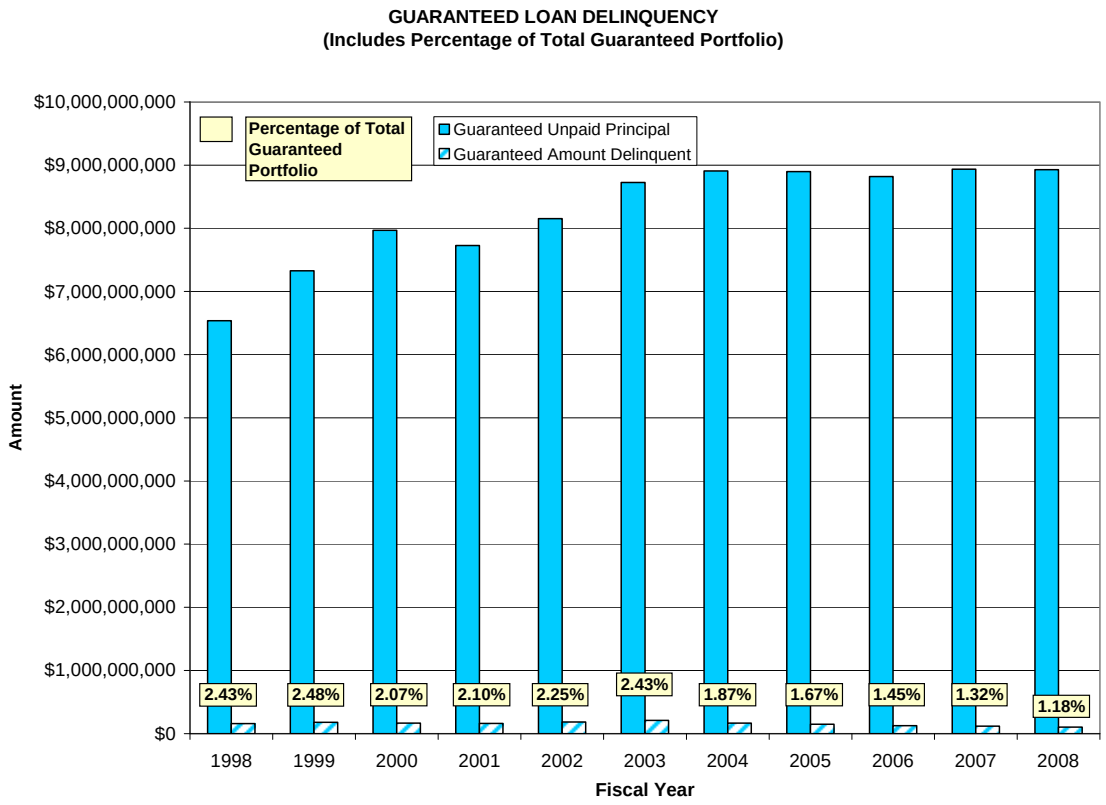

Chart 5

FY 2008 BORROWER CASELOAD BY RACE
(As Compared to 2007 Ag Census Data)

	Percent of 2007 Census Population	Percentage of FY 2008 Direct Caseload	Percent of Population being served by FSA Direct Farm Loans	Percentage of FY 2008 Guaranteed Caseload	Percent of Population being served by FSA Guaranteed Farm Loans
White	96.45	88.59	2.85	95.22	1.51
Black	1.40	3.42	7.60	0.60	0.65
Asian/Hawaiin	0.57	0.90	4.86	2.34	6.27
Amer Ind/Al Nat	1.58	3.29	6.44	1.58	1.53
* Hispanic	N/A	3.68	N/A	0.19	N/A
Other	N/A	0.12	N/A	0.07	N/A

* Hispanic Americans are not a separate category within the 2007 Census of Agriculture; therefore, no reliable comparison can be established.