Ag Risks – Impact on Ag Lending

1st Farm Credit Services
Normal, Illinois
Key Risks We Manage Today

- Concentration risk
- Underwriting risk
- Collateral risk
- Spread/earnings risk
- Human capital risk
- Reputation risk
- Technology security
- Regulatory risk
My Comments today will focus on how we manage:

• Concentration Risk

• Underwriting Risk

• Collateral Risk
Location of 1st Farm Credit Services
16 branch offices
Net farm income and net cash income, 2000-2013F

$ billion


Net cash income
Net farm income

F = Forecast.
Data as of August 27, 2013.
Figure 1. Actual and Projected Operator and Farmland Returns for Regions of Illinois, Actual for 2003 through 2012, Projected for 2013 and 2014.

- North
- Central-High
- Central-Low
- South
Net Income w/o Land Costs (FBFM - Northern IL Corn)

36 yr average = $89/acre

2007-2012 average = $207/acre

Net Income w/o Land Costs
# Marketplace Industry Segments

**Top 5 Commodities, 2011 (USDA)**

<table>
<thead>
<tr>
<th>State</th>
<th>Corn/Soybeans</th>
<th>Hogs</th>
<th>Cattle</th>
<th>Poultry</th>
<th>Dairy</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Illinois</td>
<td><strong>81.6%</strong></td>
<td>7.2%</td>
<td>3.1%</td>
<td>2.0%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Iowa</td>
<td>57.9%</td>
<td>22.4%</td>
<td>11.4%</td>
<td>3.1%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Minnesota</td>
<td>50.6%</td>
<td>14.2%</td>
<td>7.0%</td>
<td>9.7%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Indiana</td>
<td>66.8%</td>
<td>10.3%</td>
<td>3.6%</td>
<td>6.2%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ohio</td>
<td>56.5%</td>
<td>7.4%</td>
<td>5.1%</td>
<td>11.5%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Missouri</td>
<td>44.7%</td>
<td>10.1%</td>
<td>16.9%</td>
<td>4.0%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wisconsin</td>
<td>25.1%</td>
<td>10.5%</td>
<td>44.7%</td>
<td>2.2%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Michigan</td>
<td>33.5%</td>
<td>5.4%</td>
<td>22.1%</td>
<td>7.4%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Managing Concentration Risk

- Seek diversification of Assets & Income
- Participate loans to transfer/share risk
- Keep hold limits well below regulatory limit
- 3 resources on staff focused on portfolio management.
- Portfolio management guidelines
- Stress testing – black swan events
- Strong capital position
- Conservative underwriting
- Crop Insurance and Gov’t loan guarantees
1st FCS Portfolio Industry Segments

- Corn/Soybeans: 47.7%
- Landlords: 11.7%
- Misc. Capital Markets: 11.3%
- Other Crops: 10.8%
- Swine: 3.5%
- Grain Elevators: 2.1%
- General Livestock: 1.8%
- Crop Service/Fertilizer: 1.6%
- Dairy/Milk: 1.6%
- Nursery/Green: 1.5%
- Ethanol/Power: 1.3%
- Cattle: 0.8%
- Rural Homes: 0.5%
- Poultry/Eggs: 0.5%
1st FCS Portfolio Loan Segments

- Real Estate: 72%
- Intermediate Term: 14%
- Operating: 2%
- Rural Home: 12%
Credit Underwriting
Managing Underwriting Risk

• Specialized staff
• Granular PD rating process
• Discounting pro-forma capacity analysis.
• Most r/e assets on borrower Balance Sheets valued below market
• Track and manage underwriting exceptions
• Locking in longer term rates on R/E portfolio
• Loan terms
• Internal audit validation process.
Interest Rate Term

Farm R/E Portfolio - Total Principal

- 43% <2yr
- 48% >7yr
- 9% 2-7yr
Collateral Risk

(R/E portfolio)
1st Farm Credit Services Benchmarks 1999-2013
19 Farms – 26 year appraisal history

<table>
<thead>
<tr>
<th>BENCHMARKS</th>
<th>2013</th>
<th>3 Yr</th>
<th>5 Yr</th>
<th>10 Yr</th>
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</thead>
<tbody>
<tr>
<td>All Class 1A Benchmarks</td>
<td>$13,864</td>
<td>30.3%</td>
<td>50.4%</td>
<td>93.3%</td>
</tr>
<tr>
<td>All Class 2B Benchmarks</td>
<td>$11,064</td>
<td>26.5%</td>
<td>50.0%</td>
<td>101.3%</td>
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<tr>
<td>All Class 3C Benchmarks</td>
<td>$8,042</td>
<td>30.1%</td>
<td>48.2%</td>
<td>87.8%</td>
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<tr>
<td>All 1st FCS Benchmarks</td>
<td>$10,902</td>
<td>27.9%</td>
<td>47.6%</td>
<td>90.5%</td>
</tr>
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Managing Collateral Risk

- Specialized appraisal staff
- Benchmark Farm System allows us to maintain updated EMV’s (estimated market values) on majority of R/E loans.
- Limit loan amortization and require more frequent payment schedule.
- Debt per acre guideline, and sliding amortization term and L/AV rule as land value/acre increases
- Cross-collateralize loans
- Low avg. L/AV and avg. loan term
- Test portfolio exposure with 40% & 60% decline.
1st FCS R/E portfolio 6/30/2013

<table>
<thead>
<tr>
<th>L/AV+TERM</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013 YTD</th>
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<tbody>
<tr>
<td>&lt;90</td>
<td>70.5%</td>
<td>69.6%</td>
<td>91.8%</td>
<td>90.2%</td>
<td>92.7%</td>
<td>93.6%</td>
<td>94.8%</td>
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<tr>
<td>90-95</td>
<td>13.8%</td>
<td>16.5%</td>
<td>6.6%</td>
<td>7.9%</td>
<td>5.4%</td>
<td>5.1%</td>
<td>5.0%</td>
</tr>
<tr>
<td>&gt;95-100</td>
<td>12.1%</td>
<td>13.1%</td>
<td>1.5%</td>
<td>1.6%</td>
<td>1.5%</td>
<td>0.9%</td>
<td>0.2%</td>
</tr>
<tr>
<td>&gt;100-105</td>
<td>1.5%</td>
<td>0.5%</td>
<td>0.1%</td>
<td>0.1%</td>
<td>0.0%</td>
<td>0.0%</td>
<td>0.0%</td>
</tr>
<tr>
<td>&gt;105</td>
<td>2.1%</td>
<td>0.2%</td>
<td>0.0%</td>
<td>0.2%</td>
<td>0.5%</td>
<td>0.4%</td>
<td>0.0%</td>
</tr>
<tr>
<td>AVG L/AV+TERM</td>
<td>76.0</td>
<td>77.3</td>
<td>69.8</td>
<td>71.2</td>
<td>69.2</td>
<td>70.0</td>
<td>64.4</td>
</tr>
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Year Loan Originated

Average L/AV by Year Loan Originated
### 1st FCS Real Estate Portfolio 6/30/10

<table>
<thead>
<tr>
<th>Remaining Term</th>
<th>0-5</th>
<th>5-&lt;10</th>
<th>10-&lt;15</th>
<th>15-&lt;20</th>
<th>20-25</th>
<th>&gt;25</th>
<th>Grand Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>L/EMV</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&lt;25%</td>
<td>1.9%</td>
<td>4.5%</td>
<td>7.1%</td>
<td>4.6%</td>
<td>1.6%</td>
<td>0.7%</td>
<td>20.3%</td>
</tr>
<tr>
<td>25%-&lt;50%</td>
<td>1.0%</td>
<td>5.4%</td>
<td>10.2%</td>
<td>13.6%</td>
<td>6.4%</td>
<td>5.1%</td>
<td>41.8%</td>
</tr>
<tr>
<td>50%-&lt;65%</td>
<td>0.3%</td>
<td>3.2%</td>
<td>5.0%</td>
<td>9.7%</td>
<td>4.3%</td>
<td>4.5%</td>
<td>26.9%</td>
</tr>
<tr>
<td>65%-75%</td>
<td>0.1%</td>
<td>1.3%</td>
<td>1.7%</td>
<td>4.9%</td>
<td>1.3%</td>
<td>0.8%</td>
<td>10.0%</td>
</tr>
<tr>
<td>&gt;75%</td>
<td>0.0%</td>
<td>0.0%</td>
<td>0.1%</td>
<td>0.4%</td>
<td>0.1%</td>
<td>0.2%</td>
<td>0.9%</td>
</tr>
<tr>
<td>Total</td>
<td>3.3%</td>
<td>14.4%</td>
<td>24.1%</td>
<td>33.2%</td>
<td>13.7%</td>
<td>11.4%</td>
<td>100.0%</td>
</tr>
</tbody>
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### 1st FCS Real Estate Portfolio 6/30/13

<table>
<thead>
<tr>
<th>Remaining Term</th>
<th>0-5</th>
<th>5-&lt;10</th>
<th>10-&lt;15</th>
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<th>20-25</th>
<th>&gt;25</th>
<th>Grand Total</th>
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<tr>
<td>L/EMV</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&lt;25%</td>
<td>1.9%</td>
<td>5.8%</td>
<td>8.5%</td>
<td>8.1%</td>
<td>4.7%</td>
<td>3.0%</td>
<td>32.1%</td>
</tr>
<tr>
<td>25%-&lt;50%</td>
<td>1.4%</td>
<td>5.4%</td>
<td>8.3%</td>
<td>21.0%</td>
<td>8.9%</td>
<td>7.6%</td>
<td>52.5%</td>
</tr>
<tr>
<td>50%-&lt;65%</td>
<td>0.3%</td>
<td>2.5%</td>
<td>2.2%</td>
<td>4.2%</td>
<td>2.0%</td>
<td>1.6%</td>
<td>12.9%</td>
</tr>
<tr>
<td>65%-75%</td>
<td>0.0%</td>
<td>0.1%</td>
<td>0.6%</td>
<td>1.2%</td>
<td>0.3%</td>
<td>0.1%</td>
<td>2.3%</td>
</tr>
<tr>
<td>&gt;75%</td>
<td>0.0%</td>
<td>0.1%</td>
<td>0.2%</td>
<td>0.0%</td>
<td>0.0%</td>
<td>0.0%</td>
<td>0.3%</td>
</tr>
<tr>
<td>Total</td>
<td>3.7%</td>
<td>13.9%</td>
<td>19.9%</td>
<td>34.4%</td>
<td>15.8%</td>
<td>12.3%</td>
<td>100.0%</td>
</tr>
</tbody>
</table>
Looking forward – 2014-2016

• Grain producer incomes declining
• Commodity price declines, lagging input cost declines
• Expect interest rates to increase
• Farm r/e values could decline 15-30%.
• Crop insurance coverage – remains a critical risk management tool.