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Farmer Mac's AgVantage - An Opportunity for Community Banks

by John Dean

Do you ever need long-term funds to meet the long-term lending needs of your ag customers? Have you experienced reductions in your deposit base or do you anticipate that possibility at some point in the future? Have you supported your industry's initiatives in Washington to give agricultural banks greater access to funding from the Federal Home Loan Banks?

I think that most community bankers would answer "yes" to some or all of these concerns. I certainly would. Most would also say they are still waiting for a solution that actually provides the source of loan funding they need! The new Farmer Mac AgVantage will do just that and is available to you today.

AgVantage provides a simple, flexible source of liquidity without requiring the sale or participation of your agricultural mortgage loans as was necessary previously to obtain loan funding through the Farmer Mac program. AgVantage lets you turn your portfolio of agricultural mortgages into a ready supply of long- or short-term cash to support additional lending activity. Here are some of the highlights:

- Apply for certification as a Farmer Mac AgVantage bond issuer.
- Sell AgVantage mortgage-backed bonds to Farmer Mac.
- Pledge qualified agricultural mortgages as collateral for AgVantage bonds.
- Receive long-term lendable funds at low fixed or variable AgVantage rates.
- No sale of agricultural mortgages is required.

John Dean is a Glenwood, Iowa, banker and member of the Farmer Mac Board.

Any lender can participate in AgVantage. All you need to do is apply to Farmer Mac for certification as an "agricultural mortgage marketing facility," otherwise referred to as an "issuer." The application process involves the submission of a short, simple application and the response time is quick. Approval is based on certain financial, technical and stock ownership requirements similar to those for becoming a "seller" in the Farmer Mac cash window program. Lenders who make agricultural mortgage loans that conform to Farmer Mac's underwriting and servicing standards and have a credit rating acceptable to Farmer Mac (basically a B- or better rating from Lace or a comparable rating) would be eligible.

As a certified AgVantage issuer, you obtain lendable funds by issuing and selling mortgage-backed bonds to Farmer Mac. AgVantage bonds are the obligations of the issuing lender secured by a pledge of qualified Farmer Mac agricultural mortgages. The bonds may range in maturity from short-term to 15 years and have low fixed or variable rates of interest (e.g., on April 1, 1998, the typical rates for 30-day, 1-year and 15-year bonds were 5.84 percent, 5.98 percent and 6.58 percent, respectively). The bonds are issued at an agreed yield, based on market pricing at the time of commitment, and have a conventional structure with monthly interest-only payment, principal due at maturity. Fixed-rate bonds may be

prepaid subject to the payment of a fee, depending upon market rates of interest relative to the rate on the bond. Variable rate bonds may be prepaid at any adjustment date without penalty. Subject to program requirements, you determine the maturity and nature of rate on your bonds.

Using AgVantage is a piece of cake. Farmer Mac issues indicative bond rates to issuers each week by facsimile (also available on Farmer Mac's Web page at www.farmermac.com).

You should monitor these rate indications and when you want to participate, just call Farmer Mac for a commitment to purchase the AgVantage bonds you will issue. Once you have

the commitment, you will receive standard bond forms from Farmer Mac. You need to fill in the bond amount and terms and return the bonds to Farmer Mac to complete the sale. Closing on the bonds should occur approximately a week later.

Your bonds must be collateralized by a pledge of Farmer Mac qualified agricultural mortgage loans, but you act as the underwriter and the servicer on the loans. Two types of collateral pledge are available to you. If your bank has a B+ or better credit rating, you can make a general pledge equal to at least 150 percent of the principal amount of the bonds. With a rating of B- or better, or if you prefer this option, you would make a specific pledge of identified collateral equal to at least 120 percent, on a market-to-market basis, of the amount of the

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bonds. In either case, the pledged collateral remains on your institution's books and is not sold or participated out. This process will have no effect on your asset base or regulatory capital requirements. Also, as long as you have pledged qualified loans at least equal to 100 percent of the principal amount of the bonds, you have the option of using other high-quality cash-equivalent assets to meet the over collateralization amount. You may substitute other eligible collateral at any time and the qualified loans you pledge do not have to match the terms (maturity, interest rate type, etc.) of the bonds you issue and sell to Farmer Mac. Lastly, there is no requirement that the pledged loans have any payment limitations associated with them.

If a deterioration or significant adverse change in an AgVantage issuer's financial condition were to occur, Farmer Mac could require that the pledged collateral be delivered to the AgVantage custodian. Improvement in an issuer's financial condition back to at least a B- rating would result in the collateral being returned from the possession of the custodian.

The minimum issue of AgVantage bonds by an issuer on a particular sale

date is \$500,000, but you may go higher in increments of \$100,000. The maximum principal amount of bonds a single issuer can sell Farmer Mac is the lesser of five times the issuer's capital, 20 percent of the issuer's assets or \$50 million (\$25 million in the case of bonds with terms over five years). These limits will be reviewed from time to time and in specific instances may be increased or decreased by Farmer Mac, depending on the particular circumstances involved with a specific issuer.

I believe that AgVantage is a very helpful addition to the Farmer Mac program which demonstrates that the people there have been listening to the feedback community bankers have been providing about the secondary market program that was being offered. AgVantage is also responsive to the request of community bankers for Farmer Mac to provide a source of liquidity that does not require them to sell their high-quality agricultural mortgages.

For more information about the AgVantage program, contact Farmer Mac at 800-879-3276. *jal*