Remarks by
The Honorable Leland A. Strom
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Thank you for that very nice introduction, and good morning to all of you. I appreciate the opportunity to be here with you today.

What challenging times these are! Since I became FCA Chairman eight months ago, so many things have happened so quickly. Some of the world's largest financial institutions have failed. Fannie Mae and Freddie Mac have been taken over by the Government. And the Government has provided, and is poised to provide, unprecedented financial assistance to help end the crisis. Who could have imagined all of these changes?

In light of these developments, I believe this meeting is more timely than ever. It will give us an opportunity to think through the challenges and develop and coordinate our responses to them. This morning I'd like to share with you some of my thoughts and perspectives.

However, before I do that, I want to recognize my two colleagues on the FCA Board, Nancy Pellett and Dallas Tonsager. Nancy provided outstanding leadership to the Agency during her four-year tenure as Chairman, and she continues to do so as a Board member.

And Dallas, with his passion for agriculture and rural America, is a tremendous asset to the Board, the Agency, and U.S. agriculture. Nancy and Dallas, please stand so you can be recognized for your outstanding dedication and service.

I would be remiss if I did not also thank the FCA staff for all of your hard work and commitment.

A week ago this morning we again witnessed the smooth transition of leadership for our nation with the inauguration of a new president. It was an exciting and historic moment for our country. I and my fellow Board members along with the staff of the Farm Credit Administration are looking forward to working with President Obama's administration to ensure that farmers, ranchers, and other rural Americans have access to the credit they need to be prosperous.

But, as the President stressed in his inaugural address, these are difficult times. He referenced the "winter of our hardship," and said that we need to "pick ourselves up and dust ourselves off." Today, the United States and many other countries are in the worst financial crisis in 75 years.

Until recently, this crisis was limited to the housing sector and the financial markets tied to it, predominantly that of Fannie Mae and Freddie Mac. This and the failure of many other financial institutions have undermined the confidence of Wall Street and produced a credit crisis that few could have predicted.

Government Response

In response to this crisis, Congress and Federal officials have taken unprecedented steps to rescue financial institutions and restore order to credit markets.

They created the $700 billion Troubled Asset Recovery Program, commonly referred to as TARP. So far, this program has been used to inject money into struggling institutions in an effort to stabilize markets.

The Federal Government has also provided more than $8 trillion in “pledges of support.”

And while this assistance is intended to help end the crisis, the assistance has in itself presented a challenge: It has produced greater uncertainty, making it much more difficult to predict what will happen next, when the eventual turnaround will come, or what consequences the recent and future Government actions may bring.

Effect on Agriculture

So far, the agricultural industry has been largely spared the effects of the current financial crisis. The financial condition of agriculture looks positive. Farm income is strong and debt ratios are low. For this we can be grateful.

But the overall numbers don’t reflect the pressure of increasing input costs, which have plagued livestock and ethanol producers. And increasing input costs may soon trouble other producers as well if commodity prices continue to soften. Grain prices, which reached historic highs in the summer of 2008, have dropped substantially. If prices stay at these levels, this may hurt the profitability of grain farmers this year. Aquatic producers, fishermen, specialty growers, and many others are also being impacted significantly.

The possibility of a decline in farmland values is also very real. We have already seen declines in real estate values that were inflated by high commodity prices, urbanization, and other non-farm influences.

The current recession, which began in December 2007, is expected to cause unemployment rates to rise significantly over the next several quarters. These conditions will likely lead to lower off-farm income, an important source of loan repayment for many System borrowers.

Also, this recession is global and likely to affect worldwide demand for agricultural products.

Condition of the System

Fortunately, the Farm Credit System remains safe and sound. The System is financially strong and well positioned. It has good credit quality, adequate capital, strong earnings, and sufficient liquidity.

Yet with so many threats to agriculture and the general economy, the System does face risk. It faces risks to its credit, capital, liquidity, funding, and overall operations.

As the leaders of the System, you have the daunting task of navigating your institutions through this tumultuous period. I urge you to be prepared and to be proactive.

FCA’s Response

But you are not in this alone. As the regulator of the System, FCA is committed to helping ensure the safety, soundness, and strength of your institutions.

What the Agency Has Done

We have demonstrated this commitment by our recent actions.

For example, we are working with other financial regulators to raise their awareness of the impact of their actions on FCS institutions. I, along with Jamie Stewart of the Funding Corporation, recently met with Donald Kohn, Vice Chairman of the Federal Reserve Board. I also met with Sheila Bair, Chairman of the Federal Deposit Insurance Corporation. Since then, FCA staff has had follow-up contacts with staff at the Fed and FDIC, as well as regular contacts with Treasury, to further enhance our communication and to improve their understanding of the System and FCA.

And in November we adopted a Market Emergency Standby Resolution. This resolution will go into effect only in the event of a serious market disruption. It would temporarily allow Farm Credit banks to fund their assets with short-term liabilities even if doing so would cause the liquidity reserve of one or more System banks to drop below the 90-day minimum requirement.

We also increased the System's discount note ceiling to $60 billion from $40 billion to give it more flexibility to raise funds if financial markets are not open to term debt.

To support market access at competitive rates, we have maintained close contact with the Funding Corporation and the Farm Credit banks.

Throughout 2008, we provided guidance to System institutions. We issued Informational Memorandums addressing such issues as collateral evaluation requirements; and asset growth, market volatility, and best practices for fast-growing institutions.

These are a few of the specific actions we've already taken. I'd now like to discuss the three objectives I see as key to meeting the challenges of this crisis. As we move forward, these three objectives will be the focus of FCA.

What the Agency Will Do

First, the Agency's overriding objective must be to maintain the safety and soundness of the Farm Credit System. We are required by Congress to ensure that the System can adequately serve its public purpose and mission-related responsibilities. To do this, we must maintain strong examination and supervisory programs.

Although the System is currently safe and sound, it has grown rapidly and is in the midst of great market volatility and economic uncertainty. Plus, System institutions grow more sophisticated and complex every year.

To ensure that we can provide the proper supervision and oversight of the System and Farmer Mac, we are increasing our examination staffing levels and staff resources.

This increase in staffing comes at a cost. In early February we will submit our 2010 budget request to Congress. In it we propose a 9 percent increase for fiscal year 2010.

This additional funding will enable us to add 23 full-time staff to support the Agency's safety and soundness programs. This will return our examination staff level back toward where it was about five years ago. These additional employees will help ensure that we can properly review the lending activities, portfolio management, credit controls, and financial management of your institutions.

As a result of our increased focus on examination activities, you can expect to see our examiners more often. They will be spending considerably more time on-site in your institutions. They will be performing more loan reviews to test your credit risk controls and your internal credit review. This is critical for the Agency to continue its tradition of being a strong and independent safety and soundness regulator. The bottom line is we must ensure the System remains safe and sound and meets its mission, especially in the current environment.

The Agency's <u>second</u> objective is to focus on establishing the right level of regulatory capital for Farm Credit System institutions. Along with liquidity and earnings, capital is a fundamental underpinning upon which the System's safety and soundness is built. Appropriate capital levels provide the foundation for maintaining strong liquidity and earnings positions.

In 2008 we conducted a series of detailed informational meetings as part of the Advance Notice of Proposed Rulemaking on possible regulatory changes to the System's capital rules. Our goal is to enhance the System's capital framework and more closely align minimum capital requirements to risks taken by System institutions. The Agency extended the comment period on this rulemaking action to December 31, 2008, and we will continue to pursue it in 2009.

And, finally, our <u>third</u> objective is to ensure that the System continues to meet its public policy purpose and mission-related responsibilities. For example, we will continue to encourage the System to serve young, beginning, and small farmers. We will carefully consider the Rural Community Investments rulemaking effort. And we will encourage System institutions to develop partnerships with other financial services institutions.

By focusing on these three objectives, I am confident that FCA can provide the System the guidance and support it needs to meet the challenges of this financial crisis and the needs of rural America.

Strategic Challenge to the System

But the System faces one challenge I haven't mentioned yet. The financial landscape has changed, perhaps forever. The Farm Credit System may be in a period of extraordinary strategic risk that could threaten its long-term GSE value, its mission, its structure, and its oversight as a separate GSE.

As a result of the financial crisis and the loss of confidence in financial institutions, there will be greater scrutiny of GSEs and their financial regulators.

This greater scrutiny will likely lead to regulatory and financial marketplace reform. This reform could even affect entities that have been doing things right – such as the Farm Credit System.

Therefore, it is important that you be prepared to strategically respond to this challenge. In addition, it would be wise to determine how the policies of the new administration, such as the emphasis on a greener economy, may affect agriculture and your institutions.

Of course, keeping the System safe and sound will go a long way toward maintaining investor and borrower confidence. This confidence may in turn help Congress recognize the value of the System continuing to fulfill its mission as a separate GSE.

And the System's survival and eventual triumph over the crisis of the 1980s is in itself a powerful argument to preserve the System and its status as a GSE.

The '80s were certainly hard times for the System. Like many of you, I was on an institution board during that crisis and witnessed firsthand just how rapidly conditions can deteriorate. I was amazed at how quickly we went from the best of times for agriculture in the early 1980s to the worst of times by the late '80s.

Then, over the ensuing two decades, System leaders restored it to financial health and built capital levels and investor confidence. I should add that FCA played an important role in this recovery, too. With its new authority as an arm's length regulator, FCA was able to ensure that System institutions adhered to safety and soundness standards. And the establishment of the Farm Credit System Insurance Fund also greatly helped restore investor confidence.

Both the System and FCA learned much during the crisis of the 1980s, and those lessons helped build a much stronger Farm Credit System, as well as a more effective regulator.

Our experience in overcoming that crisis will guide us and keep us strong through the current crisis.

Conclusion

I'll conclude today with this: It is in times such as these that the System, as a GSE devoted to agriculture and rural America, must continue to stand tall in the marketplace and be there for America's farmers, ranchers, agricultural cooperatives, and rural communities.

In fact, the System has already done much to help producers and rural America. During the extreme commodity volatility of early 2008, System institutions stepped forward to meet the critical financing needs of the grain elevator industry. The System also helped borrowers impacted by floods, worked with livestock producers as they made difficult choices, and made critical infrastructure projects possible through innovative bond financing.

In all likelihood, the financial markets will continue to be in turmoil for some time. I am confident, however, that the Farm Credit System will successfully navigate through these difficult and uncertain times and, in the end, will be all the better for it.

My one piece of advice is to prepare yourselves for the challenges ahead. Don't be reactive, be proactive.

Remember what we learned from the 1980s. Agriculture can change rapidly—from feast to famine and eventually back to good times again. Let the knowledge and wisdom you gained from the hardship of the '80s crisis help you chart a course through these very difficult times.

And know that, as your regulator, FCA stands ready to work with you to help you meet these challenges. In fact, in one of the breakout sessions later today, FCA senior staff will discuss some of the more pronounced risks that we see facing the System in 2009.

I have seen and witnessed much over the years as a farmer, as a System borrower, and as a System director. Today, as the Chairman of the System's regulator, I will strive in all earnestness to work with you in maintaining the safety and soundness of the System while it continues to meet its mission as a GSE to better serve agriculture and rural America in the decades to come.

Again, I appreciate the opportunity to be here with you.