Farm Credit System Insurance Corporation

BOARD ACTION

FCSIC BOARD OF DIRECTORS ACTION ON

Insurance Fund Progress Review and Setting of Premium Range Guidance for 2018

BM-21-SEP-17-04

Effective Date: September 21, 2017

Source of Authority: Section 5.55 of the Farm Credit Act of 1971, as amended (12 U.S.C. § 2277a-4).

THE FCSIC BOARD HEREBY APPROVES:

- Notifying the Farm Credit System that, for prudent planning purposes, the insurance premium rate on adjusted insured debt will likely be between 9 and 11 basis points for 2018 and the assessment of an additional 10 basis points for nonaccrual loans and other-than-temporarily impaired investments will likely be continued.

DATED THIS 21st DAY OF SEPTEMPER 2017

BY ORDER OF THE BOARD

Dale L. Aultman

Dale L. Aultman
Secretary to the Board

MEMORANDUM

FCSIC
FARM CREDIT SYSTEM INSURANCE CORPORATION

September 21, 2017

To: Chairman, Board of Directors
Chief Executive Officer
Each Farm Credit System Institution

From: Jeffery S. Hall
Chairman

Subject: Premium Projection Range for 2018 – 9 to 11 basis points

At its meeting today, the Farm Credit System Insurance Corporation's Board of Directors reviewed the status of the Farm Credit Insurance Fund (Insurance Fund) and projections for the likely level of premium rates for 2018. The Farm Credit Act directs FCSIC to collect annual premiums equal to 20 basis points (0.20%) of outstanding adjusted insured obligations while authorizing the Corporation, in its sole discretion, to uniformly reduce the premiums charged to System banks.[1]

Insured debt reported by the Federal Farm Credit Banks Funding Corporation through August 31, 2017 was $256.1 billion, down from $257.8 billion at year-end 2016, a decrease of $1.7 billion (0.7 percent). Using preliminary results, at August 31, 2017 the Insurance Fund was 2.1 percent of adjusted insured debt or $234 million above the 2 percent secure base amount (SBA)[2]. This is a positive change from yearend 2016 results when the Insurance Fund was 1.96 percent of adjusted insured debt or $88 million below the SBA.

Based on our August survey, System banks anticipate growth in insured debt of 3.7 percent in 2017, which is a decrease from the 5 percent growth projected by System institutions in January 2017. The survey also includes estimated growth rates for 2018 ranging from 2.8 percent to 4 percent, with a weighted average growth estimate of 3.4 percent. We note, however, that growth in insured debt has averaged 7.04 percent annually from 2012 through 2016, with growth in every month from September through December.

[1] FCSIC is required by statute to maintain the Insurance Fund at a "secure base amount" of 2 percent of the aggregate outstanding obligations of insured System banks --- adjusted downward to provide System banks credit for holding government-guaranteed loans and investments – or such other percentage the Corporation determines to be actuarially sound to maintain the Insurance Fund taking into account the risk of insuring the System obligations. To date, the Corporation has not determined any other amount to be actuarially sound and therefore is required to maintain 2 percent of adjusted insured debt obligations in the Insurance Fund.

[2] If the Insurance Fund exceeds the secure base amount at the end of any calendar year, FCSIC allocates those amounts, minus operating expenses and insurance obligations, to "allocated insurance reserve accounts" (AIRAs) established for the benefit of the System banks and holders of Financial Assistance Corporation stock (System banks and certain System associations) in accordance with the formula found at 12 U.S.C. § 2277a-4 (section 5.55 of the Farm Credit Act). Once FCSIC determines that the allocation is appropriate and that the funds in the AIRAs are not otherwise needed, FCSIC may pay the amounts in the AIRAs to the account holders.

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The Board considers the following factors in setting premiums:

- Current level of the Insurance Fund and projections for growth in insured obligations;
- Likelihood and probable amount of any losses to the Insurance Fund;
- Financial condition of the Farm Credit System banks and associations;
- Health and prospects for the agricultural economy; and,
- Risks in the financial environment that could cause problems, including volatility of interest rates, increased competition, and use of sophisticated investment securities and derivatives.

The Corporation's June 2017 allowance for loss review for all banks and associations concluded that no losses to the Insurance Fund were probable at this time. Overall, the System remains fundamentally safe and sound and liquidity risk to the Insurance Fund remains low. The current agricultural lending environment is increasingly competitive and earnings may diminish as net interest margin compresses. Credit quality ratios declined slightly, but remain strong overall and FCSIC staff believes the System is well-positioned to appropriately adjust to changes in its operating environment to remain competitive and profitable in 2017 and 2018.

We anticipate that insured debt outstanding will continue to grow in 2017; however, the Insurance Fund may be above the SBA at yearend. After all yearend results are finalized, including System institutions reporting on their condition and performance, and any excess in the Insurance Fund is transferred to the AIRAs, the Board will consider exercising its authority under the statute to make payments from the AIRAs (see footnote 2).

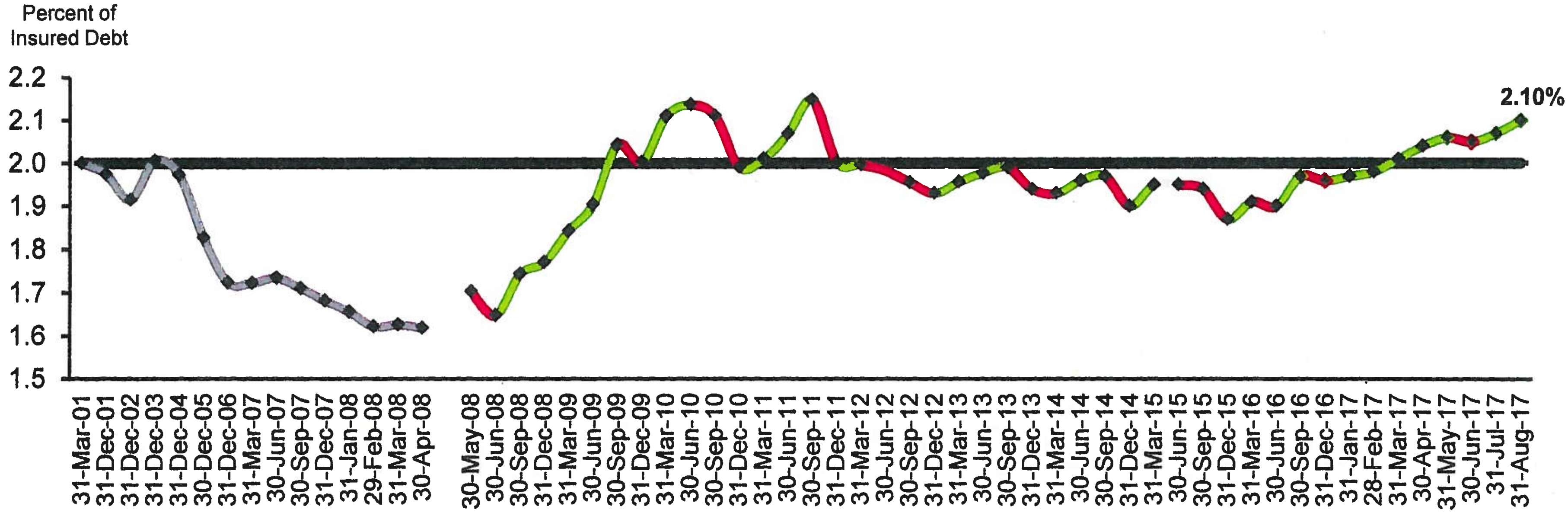
Because we anticipate that in the beginning of 2018 the SBA percentage will be at the statutory 2 percent, the Board of Directors believes that, for planning purposes, it would be prudent for System banks to anticipate a premium rate of between 9 and 11 basis points to cover growth in insured debt for 2018. Also, the assessment of an additional 10 basis points for nonaccrual loans and other-than-temporarily impaired investments will likely be continued.

The Board of Directors will make the premium decision for 2018 at its January meeting. At that time, the Board will take into account updated information on insured debt growth, projected growth and all of the other relevant factors affecting the System banks in determining premium rates.

If you have any questions concerning this matter please contact FCSIC's Chief Financial Officer, Emily Dean, at deanew@fcsic.gov or (703) 883-4387.

Attachment: Trend of Secure Base Percentage

Preliminary Trend of the Unallocated Insurance Fund Relative to the 2% Secure Base Amount
August 31, 2017



(1) A change in the secure base amount (SBA) calculation methodology requested by the Insurance Corporation was included in the Food, Conservation and Energy Act of 2008. The methodology allows the deduction of Federal and state-guaranteed investments from the SBA in a manner similar to that used for Federal and state-guaranteed loans.

(2) Insurance premiums are assessed with the objective of maintaining the SBA which is defined in the Farm Credit Act as 2% of adjusted insured obligations. At year-end 2009, additional excess funds above the SBA of $165.4 million were transferred to the Allocated Insurance Reserves Accounts (AIRAs). In February 2010, the $39.9 million that was transferred to the AIRAs in 2003 was paid to the accountholders. In April 2010, the $165.4 million that was transferred to the AIRAs in 2009 also was paid to the accountholders. The AIRAs balance is recorded as part of the Insurance Fund and is available to satisfy insurance obligations until the Corporation disburses payment to the Farm Credit Banks and FAC stockholders. At year-end 2011, excess funds above the SBA of $222 million were transferred to the AIRAs and paid to the accountholders in May 2012.

ATTACHMENT