Semiannual Report to Congress
on
Farmer Mac

(Federal Agricultural Mortgage Corporation)

as of

June 30, 2003

by the

Office of Secondary Market Oversight
Farm Credit Administration

Contents

Preface

This report to Congress summarizes the Federal Agricultural Mortgage Corporation's (Farmer Mac or Corporation) business performance for the first half of 2003 and financial condition as of June 30, 2003.

The Senate Committee on Agriculture, Nutrition, and Forestry and the House Committee on Agriculture requested[1] that the Farm Credit Administration (FCA or agency), in a cooperative effort with the Department of the Treasury (Treasury), monitor, review, and report semiannually on the operations and financial condition of Farmer Mac. As the safety and soundness regulator of Farmer Mac, FCA prepares this report and provides a copy to Treasury for review and comment prior to its release. The committees requested that the semiannual reports be provided "during the capital deferral period and beyond, if necessary." At the time of the congressional request, Farmer Mac's capital had been steadily eroding, and efforts to build loan volume had met only limited success.

On February 10, 1996, the President signed into law the Farm Credit System Reform Act of 1996 (1996 Act), which contained significant revisions to Farmer Mac's statutory charter. These revisions included new program-related authorities and the mandate that Farmer Mac recapitalize to a core capital[2] level of at least $25 million within no longer than 2 years from enactment of the 1996 Act. The 1996 Act also required the agency to delay the implementation of a Farmer Mac Risk-Based Capital Rule for at least 3 years, to be effective not before February 10, 1999 (the capital deferral period).

The FCA Board approved a final Farmer Mac Risk-Based Capital Rule on February 21, 2001. The final rule became effective on May 23, 2001. Due to a 1-year trial implementation period, Farmer Mac was not required to comply with the Risk-Based Capital Rule until May 23, 2002. Farmer Mac made its first official submission of the Risk-Based Capital Stress Test for June 30, 2002, and has been in compliance with the test's regulatory capital[3] requirement in each quarter since that date (see Table 3, page 16, and the Net Worth Analysis section on page 8).

Farmer Mac has grown substantially as new business strategies were implemented subsequent to the 1996 legislative changes. On- and off-balance sheet program activity, as illustrated in several places throughout this report, is now approaching $5.6 billion. Non-program investments increased to nearly $1.6 billion, resulting in Farmer Mac managing or guaranteeing assets of nearly $7.2 billion at June 30, 2003. Changing business strategies and significant growth of program assets have caused equally rapid evolution in the Corporation's risk profile over the past 5 years. That evolution is marked by an increase in the size and complexity of financial and operational risks to be managed.

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[1] The request was by letter to FCA dated December 22, 1995, from the Chairmen of the Senate Committee on Agriculture, Nutrition, and Forestry and the House Committee on Agriculture.

[2] Core capital is defined as the sum of the following, as determined in accordance with Generally Accepted Accounting Principles (GAAP): (1) the par value of outstanding common stock, (2) the par value of outstanding preferred stock, (3) paid-in capital, and (4) retained earnings.

[3] Regulatory capital is defined as core capital plus the allowance for losses, as determined in accordance with GAAP.

Corporate Profile

Farmer Mac is a federally chartered instrumentality of the United States created in 1988 to establish a secondary market arrangement for agricultural real estate and rural housing mortgage loans.

The Corporation conducts its business through two programs, Farmer Mac I and Farmer Mac II. In the Farmer Mac I program, Farmer Mac purchases or commits to purchase qualified loans or securities backed by qualified loans. Farmer Mac recently also began buying participation interests in qualified loans. Under the Farmer Mac II program, Farmer Mac purchases the guaranteed portions of loans backed by the United States Department of Agriculture.

Farmer Mac is a publicly traded corporation, whose stock is traded on the New York Stock Exchange under the symbols "AGM" (NYSE:AGM) for Class A and "AGMa" for Class C shares (detailed below). Farmer Mac has three classes of common stock:

1. Class A Voting Common Stock may only be held by banks, insurance companies, and other financial institutions that are not institutions of the Farm Credit System. No owner of Class A stock may hold more than 33 percent of the outstanding shares of Class A stock.

2. Class B Voting Common Stock may only be held by institutions of the Farm Credit System and are not exchange-traded. There are no restrictions on the maximum purchase or holdings of Class B stock.

3. Class C Non-Voting Common Stock has no ownership restrictions.

The Farmer Mac Board of Directors (Board) is comprised of 15 members. Five are elected by Class A common stock shareholders. Five are elected by holders of Class B common stock. The President of the United States appoints the remaining five, and one of these is appointed by the President as chairperson.

Farmer Mac is regulated by the FCA through the Office of Secondary Market Oversight (OSMO), which was established in 1992 as required by Public Law 102-237. OSMO provides for the examination and general supervision of Farmer Mac's safe and sound performance of its powers, functions, and duties. Farmer Mac also is subject to certain disclosure and reporting requirements of the Securities and Exchange Commission (SEC). The Corporation regularly files SEC documents including 10K, 10Q, and 8K reports and is required by regulation to forward to the FCA copies of all substantive SEC correspondence, including these reports.

Highlights of Operations

Farmer Mac's financial condition as of June 30, 2003, and performance for the first half of 2003 is reflected by the following:

Financial Condition

- Net worth increased 10.4 percent to $202.7 million from $183.6 million at yearend 2002.
- Farmer Mac's statutory minimum core capital requirement was $138.8 million. The Corporation's core capital available to meet this requirement was $202.9 million,[4] 46 percent above the statutory requirement.
- Farmer Mac's risk-based regulatory capital requirement was $45.4 million. The Corporation's regulatory capital available to meet this requirement was $224.8 million. The Net Worth Analysis section contains additional information on statutory minimum core capital and the risk-based regulatory capital requirements.
- Farmer Mac remains in Enforcement Level I with core capital and regulatory capital exceeding statutory minimum and regulatory risk-based capital requirements, respectively. The Net Worth Analysis section and Table 3 contain additional information.
- Non-program investments remained relatively stable and were $1.597 billion at June 30, 2003.

Financial and Program Performance

- Net income for the period ended June 30, 2003, was $16.8 million, a 24 percent increase over the same 6-month period in 2002 and nearly 80 percent of full-year earnings in 2002.
- Both on- and off-balance sheet program-related activity grew, reaching $5.593 billion from $5.528 billion at yearend 2002, representing an increase of just over 1 percent.
- Long-Term Standby Purchase Commitment (Long-Term Standby, Standby, or LTSPC) volume outstanding totaled $2.791 billion, up 4 percent during the first half of 2003. Standby volume represents 56 percent of Farmer Mac I program activity (50 percent of all program activity) and dominates the Corporation's off-balance sheet Farmer Mac I guarantees (see Chart 3 below).
- Outstanding AgVantage bonds totaled $23.6 million, down $4.5 million.

[4] The difference between core capital ($202.9 million) and net worth ($202.7 million) is attributable to a negative $203,000 in other comprehensive income (OCI), which is added back to calculate core capital. OCI represents unrealized net income/losses on certain available for sale securities and financial derivatives in accordance with Financial Accounting Standards Board statements (FASB) 115 and 133.

- Post-1996 Act Farmer Mac I loan volume purchased or guaranteed that was 90 days or more past due, in foreclosure, in bankruptcy, or Real Estate Owned (REO) was 1.64 percent of all post-1996 Act Farmer Mac I loan volume outstanding. This compares to 1.45 percent at June 30, 2002. See the Delinquencies section on page 10 for a further discussion of seriously delinquent loans and other high-risk assets.

- The allowance for losses increased to $21.9 million at June 30, 2003, compared to $20.9 million at December 31, 2002. Charge-offs on loans net of recoveries during the first half of 2003 were $2.2 million, compared to $1.3 million over the same period in 2002. Farmer Mac incurred no charge-offs in 2000. See the Allowance for Losses and Chargeoffs section on page 11 for further analysis and discussion of trends.

Overview of Financial Performance for Six Months Ending June 30, 2003

Program Activity

Farmer Mac's on- and off-balance sheet program-related activity continued an upward trend, reaching $5.593 billion at June 30, 2003, an increase of $65 million, or 1.2 percent, from December 31, 2002. On-balance sheet activities decreased slightly less than one percent, while off-balance sheet program activities increased by nearly 3 percent.

On-balance sheet program assets include agricultural mortgage-backed securities (AMBS),[5] loans, REO, and AgVantage bonds. During the first half of 2003, the principal amount of on-balance sheet program assets was down $26.6 million, or 1 percent, excluding REO. The impact of this decline on Farmer Mac's profitability was more than offset by increases in off-balance sheet Standby commitments of $109 million and non-program assets of $42.7 million.

Farmer Mac continues to hold more loans and AMBS in portfolio than they sell to investors. This is the result of Farmer Mac adopting a retained portfolio strategy in the third quarter of 1998 due to economic considerations. That is, Farmer Mac generally retains rather than sells AMBS when the estimated present value of the net interest income to be generated over the life of the AMBS is greater than the potential one-time gain on the sale of AMBS.

Total off-balance sheet program activity was $3.138 billion at June 30, 2003, up from $3.048 billion at yearend 2002. Long-Term Standby program activities accounted for the great majority of the overall off-balance sheet increase of nearly 3 percent, or $90 million. While off-balance sheet AMBS continued to decline, down $17 million. Farmer Mac's Standby program increased by $109 million, or 4 percent, in the first half of 2003. Under the Long-Term Standby program, a financial institution acquires a Farmer Mac guarantee on a defined pool of loans for an annual fee paid to Farmer Mac. The institution retains the loans in-portfolio. Farmer Mac's guarantee is to purchase loans from the pool under certain

[5] AMBS are of two types based on different kinds of agricultural mortgages. Farmer Mac I is comprised of mortgages secured by the first liens on agricultural real estate or rural housing loans purchased from lenders and represents the primary source of Farmer Mac business activity. Farmer Mac II consists of the portion of certain types of loans guaranteed by the U.S. Department of Agriculture.

specified conditions at the request of the institution. While the Standby program is available to agricultural lenders generally, Farm Credit System institutions account for all Standby program volume to date.

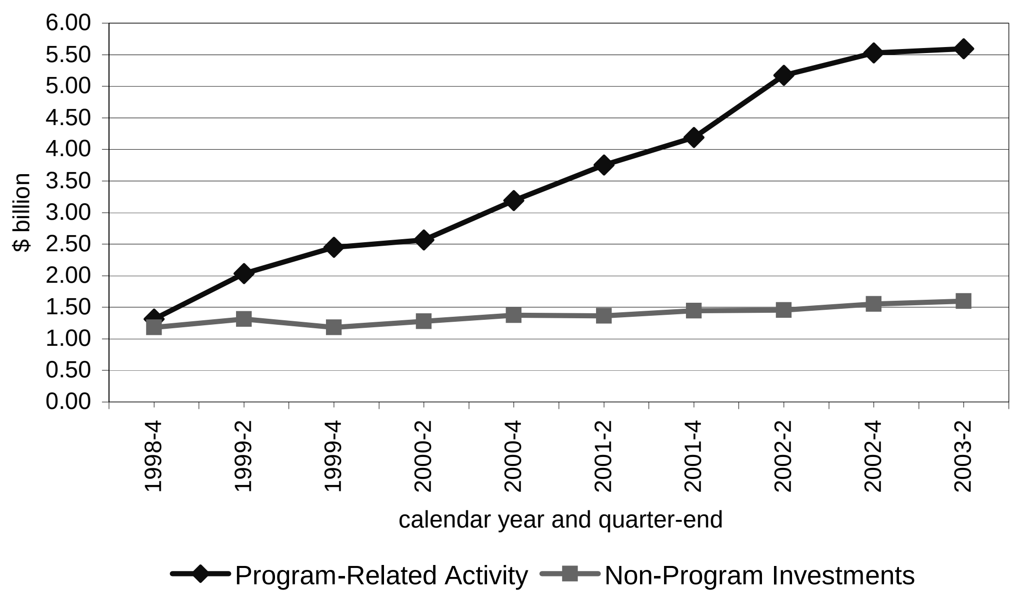
The Long-Term Standby program has grown significantly since its inception in 1999. Since June 30, 2001, Standby growth has exceeded 80 percent. By the end of the second quarter, 2003, Long-Term Standby outstanding balances of $2.791 billion represented nearly 90 percent of all off-balance sheet program volume and more than half (56 percent) of all Farmer Mac I program activity (i.e., excluding AgVantage and Farmer Mac II programs). See Table 5 for line items of both on- and off-balance sheet program activity and Chart 2 for a summary of total program-related activity.

Trend Charts Reflecting On- and Off-Balance Sheet Business Activity

Chart 1 shows trends in program-related activity and non-program investment levels. At June 30, 2003, total program-related activity continued an upward but modest trend to $5.593 billion, while non-program investments also trended upward slightly to a total of $1.597 billion.

Chart 1

Trends in Farmer Mac Program-Related Activity and Non-Program Investments



The following chart breaks out program-related activity into four major components:

1. AMBS Held by Farmer Mac*	--	$1.471 billion (26 percent);
2. Loans and REO	--	$0.984 billion (18 percent);
3. AMBS Held by Investors	--	$0.347 billion (6 percent); and,
4. Long-term Standby**	--	$2.790 billion (50 percent).
Total		$5.593 billion (100 percent)

* This includes $23.6 million of AgVantage bonds.

** The Long-term Standby program was initiated in January 1999. Standbys are now the dominate component (56 percent) of the Farmer Mac I program activity, see Chart 3 below.

Chart 2
Composition of Farmer Mac's Program-Related Activity

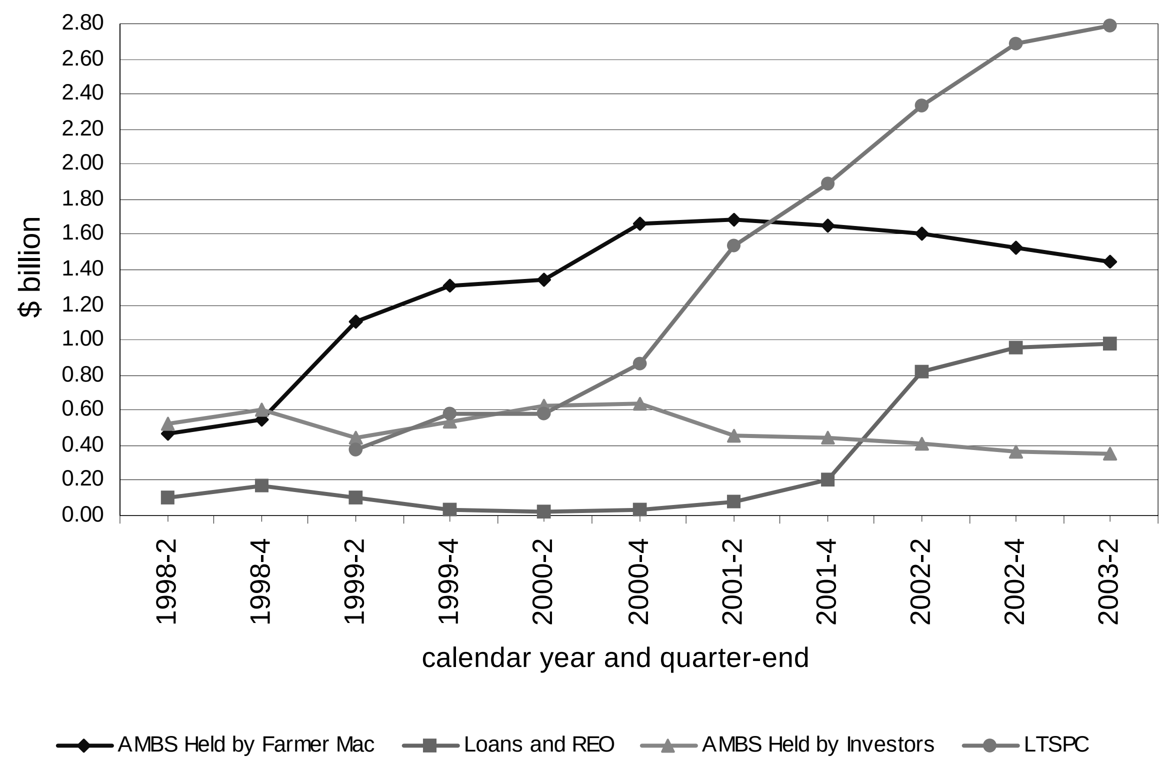
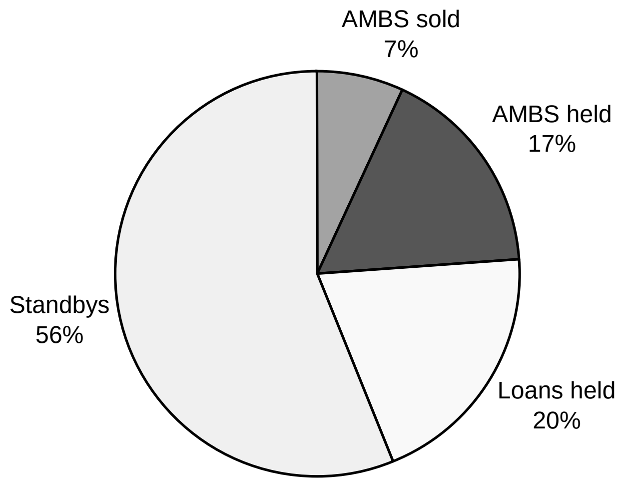


Chart 3
Farmer Mac I Program Activity
June 30, 2003



Funding of Program and Non-Program Investments

By statute, Farmer Mac is authorized to "…sell any…obligations, and otherwise exercise all the usual incidents of ownership of property necessary and convenient to the business of the Corporation." Coincident with this, Farmer Mac Board policy authorizes the issuance of debt obligations, principally discount notes (DNs) and medium-term notes (MTNs), to fund Farmer Mac I and II programs, and to conduct other activities of the Corporation, such as maintaining investments in non-program assets for liquidity purposes. The liquidity portfolio is available to meet maturing debt obligations in the event of a short-term disruption in the capital markets that prevents Farmer Mac from issuing new debt. The liquidity portfolio consists of non-program investments, which are defined as investment securities, cash, and cash equivalents.

Farmer Mac has policy limits on the maximum amount of MTNs and DNs that may be outstanding at any one time for the purpose of funding Farmer Mac I and II and the liquidity portfolio, and on the maximum amount of non-program investments that may be held in the liquidity portfolio. Farmer Mac's Board also has set limits on the aggregate amount of credit exposure to any one issuer of investment instruments.

Farmer Mac's significant program-related growth compared to a relatively stable level of non-program investments continued to show a lessening dependence on non-program investments over the last several years. At June 30, 2003, non-program related investments amounted to 28.6 percent of program-related assets (on- and off-balance sheet assets). This compares to 48 percent at December 31, 1999, and 90 percent at yearend 1998. The relationship between program and non-program investments activity is depicted in Chart 1. As the proportion of program activity has grown relative to non-program investments, net interest income (NII) from non-program investments to support net income before taxes (NIBT) was stable at under 30 percent. Prior to 2000, NII from non-program investments constituted half or more of NIBT.

FCA examines and monitors Farmer Mac's non-program investments on an ongoing basis to ensure that non-program investments primarily serve the Corporation's statutory mission and are not used solely for income generation. The FCA Board plans to address non-program investments and liquidity through a Notice of Proposed Rulemaking in 2003; see the Regulatory Activities section for further details.

<u>Net Worth Analysis</u>

Farmer Mac's net worth, or capital as reported in compliance with GAAP, at June 30, 2003, was $202.7 million. Capital increased $19.1 million, or 10.4 percent, from yearend 2002.

The Corporation's core capital *(core capital is defined in footnote 2 on page 1)* remained above the statutory minimum prescribed by Section 8.33 of the Farm Credit Act of 1971, as amended (Act). At January 1, 1999, statutory minimum core capital requirements became fully phased in at 2.75 percent of on-balance sheet assets and 0.75 percent of off-balance sheet guarantees. Farmer Mac's statutory minimum core capital requirement was $138.8 million at June 30, 2003. Core capital of $202.9 million was available to meet this requirement.

Farmer Mac's application of the risk-based capital stress test as of June 30, 2003, produced a regulatory capital requirement *(regulatory capital is defined in footnote 3 on page 1)* of $45.4 million. Farmer Mac's regulatory capital to meet this requirement was $224.8 million.

Farmer Mac remains in Enforcement Level I as defined in Section 8.35 of the Act. That is, Farmer Mac's core capital equaled or exceeded the minimum core capital requirement set forth in Section 8.33 of the Act and its regulatory capital equaled or exceeded the risk-based capital requirement. Enforcement Levels II – IV require that FCA place certain supervisory restrictions on Farmer Mac.

See Chart 4 for trend of net worth and Table 1 for more details.

<u>Net Income Analysis</u>

Farmer Mac's net income for the first half of 2003 was $16.8 million, a 24 percent increase over the same period in 2002. The increase in net income primarily resulted from:

- A large net gain of $7.6 million in financial derivative and trading asset positions that do not receive hedge accounting treatment (Core Earnings,[6] an alternative non-GAAP measurement, ignores such paper gains and losses).
- Net interest income increasing 14 percent to $16.8 million, and
- A 20-percent reduction in the Corporation's operating expenses.

The increase was partially constrained by:

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[6] Core earnings, reported for the first time for the quarter ending March 31, 2003, are a non-GAAP measure of financial results that excludes the effects of unrealized gains and losses on available-for-sale securities and financial derivatives. Farmer Mac began reporting core earnings to present a less volatile measurement of earnings.

- The provision for losses increasing 25 percent to $5 million year-to-date, and

- The provision for income taxes increasing 68 percent to $8.6 million year-to-date, compared with just over $5 million for the same period at June 30, 2002.

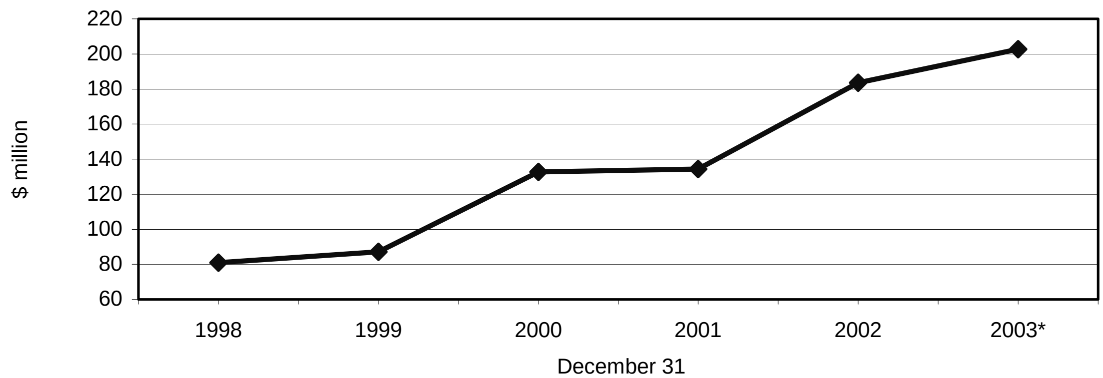
See Chart 5 and Table 2 for additional information on net income trends.

Trends in Net Worth and Net Income

Charts 4 and 5 below reflect recent years' trends in Farmer Mac's net worth and net income, respectively.

Chart 4

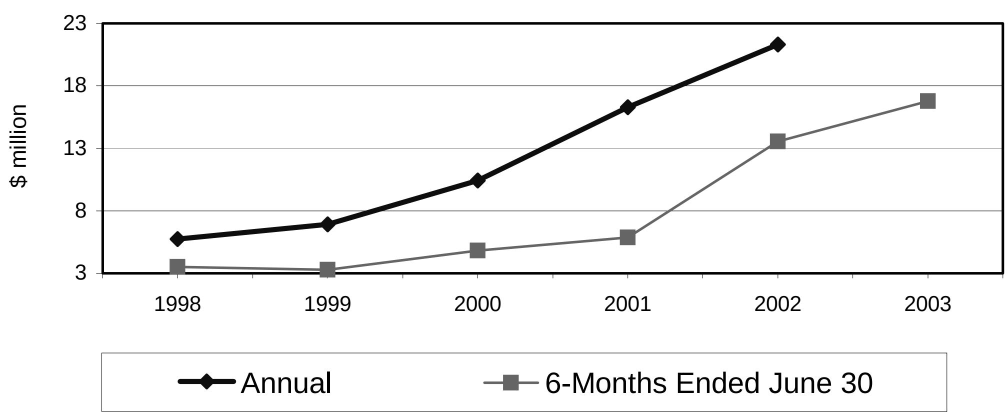
Trend in Farmer Mac Net Worth



* As of June 30, 2003

Chart 5

Trend in Farmer Mac Net Income

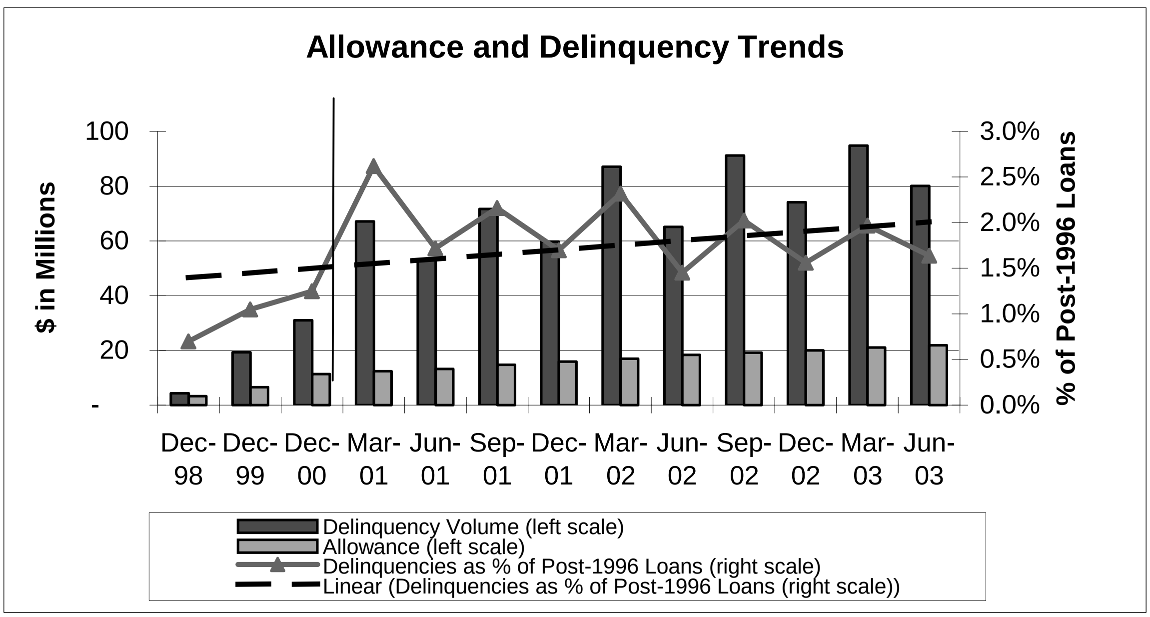


Delinquencies

Farmer Mac assumes 100 percent of the credit risk on post-1996 Act Farmer Mac I loans and Standby obligations. Pre-1996 Act Farmer Mac I loans are supported by subordinated interests representing at least 10 percent of the initial balance of the loans underlying the securities. Given the first loss position of the subordinated interest, Farmer Mac does not expect to incur any losses on the pre-1996 securities.

Farmer Mac has experienced significant growth in program assets since early 1999. Seriously delinquent post-1996 Act Farmer Mac I loans have also trended upward as a percent of such assets – see the Linear Trend Line in Chart 6 below. Seriously delinquent post-1996 Act Farmer Mac I loans (90 days or more past due, in foreclosure, in bankruptcy, or REO) were 1.64 percent of the outstanding balance of all post-1996 Act Farmer Mac I loans and Standby obligations at June 30, 2003, up from 1.45 percent a year earlier.

Chart 6



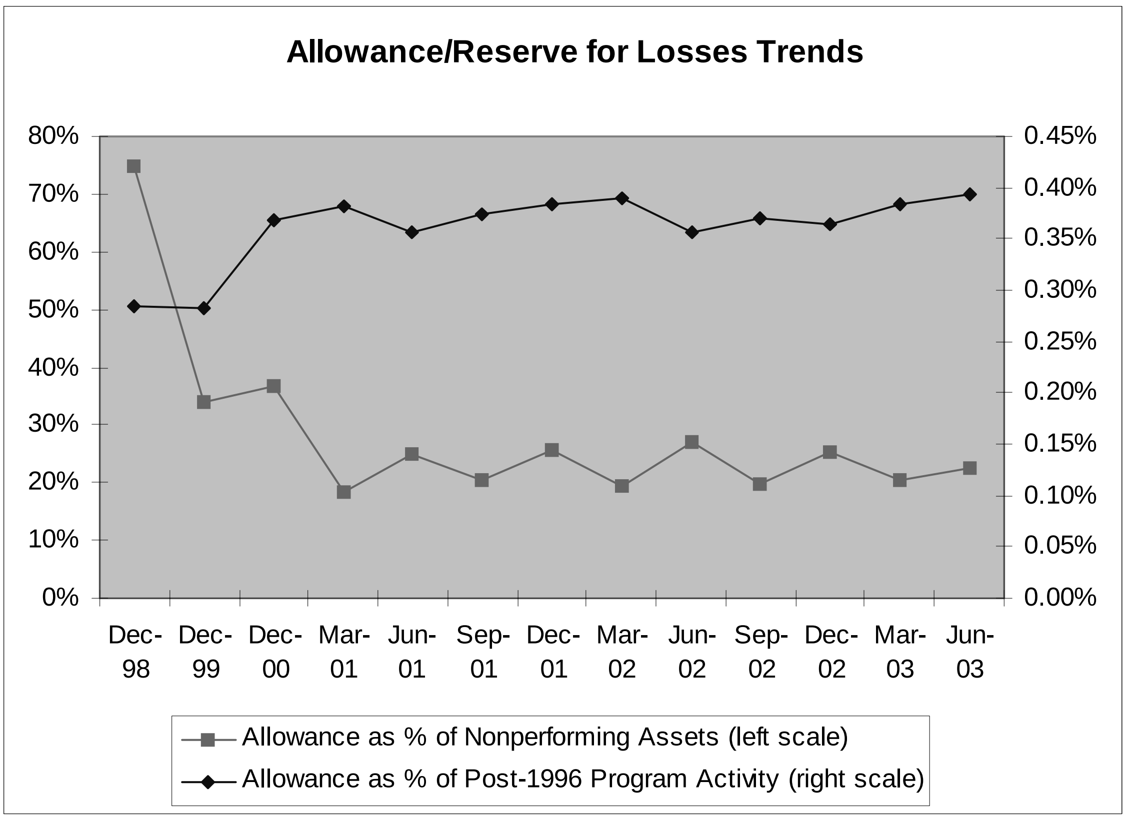
Growth of seriously delinquent loans has been trending upward as a percent of post-1996 program activity. Since 1998, the dollar volume of delinquencies (red bars in Chart 6) has risen faster than the overall delinquency rate of post-1996 Act loans. The rapid growth of program assets, led by the Long-Term Standby program, has allowed Farmer Mac to maintain the delinquency rate within a range of roughly 1 percent to 2.5 percent of post-1996 Act program activity over the last 2 years. Farmer Mac attributes the upward trend in the amount of seriously delinquent post-1996 Act Farmer Mac I loans to a sizeable segment of its portfolio reaching peak default years (3-5 years from origination).

Allowance for Losses and Charge-offs

The Corporation's allowance for losses at June 30, 2003, increased to $21.9 million, from $18.3 million at June 30, 2002. The provision for losses for the 6-month period ended June 30, 2003, was $5.0 million, compared to $4.0 million for the same period in 2002.

Chart 7 below illustrates that Farmer Mac's non-performing asset coverage by the allowance/reserve declined to 22 percent as of June 30, 2003, compared to 27 percent a year earlier. The allowance for loan losses has remained at between 0.35 and 0.40 percent of total covered assets, i.e., post-1996 program assets. Post-1996 program activity is used as a proxy for covered assets here because of the small relatively risk-free characteristics of pre-1996 program assets.

Chart 7



Charge-offs on loans, net of recoveries, through 6 months ending June 30, 2003. totaled $2.2 million, compared to net charge-offs of $1.3 million and $920 million taken in the same period in 2002 and 2001, respectively. There were no charge-offs in 2000.

Regulatory Activities

FCA regulates, examines, and supervises Farmer Mac through authorities granted by Title VIII of the Act. The agency is authorized to promulgate regulations, examine all books and records of Farmer Mac, and ensure safe and sound operations of Farmer Mac through enforcement supervisory actions that are comparable with those of other financial regulators, such as the Comptroller of the Currency. For example, the statute provides the FCA Board with enforcement powers for cease and desist orders, civil money penalties, and the suspension or removal of directors or officers. The FCA Board has in the past used all available authorities when necessary.

<u>Examination</u>

By statute, FCA must examine Farmer Mac's operations once each year. The FCA like other federal financial regulators does not make public institution-specific examination findings, recommendations, or supervisory follow-up activities. Ongoing monitoring and follow-up on examination findings and recommendations are conducted through the agency's Office of Secondary Market Oversight and is independent and separate from other such activities affecting other institutions of the Farm Credit System.

The current examination is being conducted with an "as of" date of August 31, 2003. The examination is comprehensive, risk-based, and focused on what is commonly referred to by Federal financial regulators as a "CAMELS" assessment. A CAMELS assessment includes analyses of the institution's Capital, Assets, Management, Earnings, Liquidity, and Sensitivity to market risk. The 2003 examination also includes an in-depth evaluation of Farmer Mac's information technology, internal controls, and accounting treatment for high-risk assets and derivative transactions. At this report, the 2003 examination remains in progress.

<u>Regulations</u>

In September 2003, the FCA Board adopted a revised Unified Agenda and Regulatory Performance Plan, which include two regulatory projects related to Farmer Mac. The first will propose regulatory standards for Non-Program Investments and Liquidity requirements for Farmer Mac and is targeted for FCA Board consideration in late 2003. The second project involves technical adjustments and other enhancements to the Risk-Based Capital Stress Test (12 CFR 650), and is targeted for consideration by the FCA Board in summer 2004.

<u>General Accounting Office Report</u>

At the request of the Chairman and Ranking Member of the United States Senate Committee on Agriculture, Nutrition, and Forestry, the General Accounting Office (GAO) began a study of Farmer Mac and the FCA's oversight during the latter half of 2002. GAO's report, <u>Farmer Mac: Some Progress Made, but Greater Attention to Risk Management, Mission, and Corporate Governance Is Needed</u>, was issued on October 16, 2003, and is available at the GAO's web address: www.gao.gov.

GAO concluded "Farmer Mac's financial condition has improved . . . [but] its efforts to measure and monitor its risks have not kept pace [with its more complex risk profile] and could be improved." With regard to mission accomplishment, GAO stated, "Farmer Mac has increased its mission-related activities, . . . but it is still not apparent if sufficient public benefits are derived from these activities. The lack of specific or measurable mission goals in its statute beyond providing a secondary market and stable long-term financing does not allow for a meaningful assessment of whether Farmer Mac's activities are having the desired impact on the agricultural real estate market." GAO also noted "[s]imilar to other publicly traded companies, Farmer Mac is faced with the challenges of updating its corporate governance practices to comply with Sarbanes-Oxley, SEC rules and proposed NYSE listing standards as they become effective." GAO provided six recommendations for improving Farmer Mac's risk management practices and four recommendations to further enhance its corporate governance practices.

The GAO report also concluded that "…FCA had improved its oversight of Farmer Mac, but continues to face significant challenges…" GAO provided five recommendations for FCA[7] that address: The Risk-Based Capital model governing minimum regulatory capital requirements; Off-site monitoring and regulatory reporting of Farmer Mac; FCA's plans to reduce capital arbitrage activities that can occur between Farmer Mac and FCS institutions; how other secondary market regulators of GSEs have developed regulations to require a government credit rating; and, the impact that Farmer Mac's activities may have on the agricultural real estate lending market.

FCA will respond to the GAO recommendations by providing plans to the agency's Congressional oversight committees within 60 days of the report's issuance as required by statute.

[7] See Appendix 1 for FCA's letter dated August 21, 2003, in response to GAO's draft report.

Historical Data

Table 1

FARMER MAC BALANCE SHEET
($000,000)

Date	Assets	Liabilities	Net Worth
12-31-98	1,936.0	1,855.1	80.9
06-30-99	2,565.5	2,481.2	84.3
12-31-99	2,590.4	2,503.3	87.1
06-30-00	2,703.3	2,609.8	93.5
12-31-00	3,160.9	3,028.2	132.7
06-30-01	3,209.1	3,098.4	110.7
12-31-01	3,417.2	3,282.8	134.4
06-30-02	4,037.6	3,852.6	185.0
12-31-02	4,222.6	4,039.0	183.6
06-30-03	4,267.8	4,065.2	202.7

Table 2

FARMER MAC STATEMENT OF OPERATIONS
($000,000)

Date	Net Interest Income	Total Other Income	Gains/ (Losses)[8]	Total Expenses	Adjust-ments[9] & Tax Provision	Net Income to Share-holders [10]	Core[11] Earnings
06-30-99*	7.527	3.307	---	5.874	1.687	3.273	N/A
12-31-99	14.958	7.616	---	11.983	3.670	6.921	N/A
06-30-00*	8.860	5.509	---	6.880	2.659	4.830	N/A
12-31-00	17.698	12.076	---	13.588	5.749	10.437	N/A
06-30-01*	11.875	7.379	(0.748)	8.230	2.953	5.871	N/A
12-31-01	26.939	16.367	(0.726)	17.155	7.693	16.280	N/A
06-30-02*	16.376	10.050	(0.006)	9.603	7.002	13.549[12]	11.092
12-31-02	33.686	20.609	4.359	18.774	9.897	21.295	N/A[13]
06-31-03*	15.983	10.594	7.635	7.667	9.756	16.790	11.665

* Asterisks indicate earnings for the first six months of each operating period. For comparison purposes, earnings should be compared to comparable periods.

8 Gains and losses reflect market value changes on financial derivatives and trading assets under the disclosure requirements of FASB 115 and FASB 133.

9 Adjustments include the cumulative effect of changes in accounting principles, extraordinary gains/losses, and preferred stock dividends.

10 Net Income to Shareholders reflects income available to holders of common stock, the equivalent of Net Income less preferred stock dividends.

11 Core earnings -- defined in footnote 6, page 8.

12 This number as of June 30, 2002, and going forward, is Net Income Available to Common Stockholders, or Net Income minus preferred stock dividends. Farmer Mac issued preferred stock in May 2002.

13 N/A--Not Available. Farmer Mac has yet to report core earnings for the fourth quarter 2002. This will be reported as part of fourth quarter 2003 disclosures.

Table 3

FARMER MAC COMPLIANCE WITH CAPITAL REQUIREMENTS AND ENFORCEMENT LEVEL

($000,000)

Date	Core Capital	Required Core Capital	Excess Core Capital	Regulatory Capital	Required Regulatory Capital	Excess Regulatory Capital	Enforcement Level[14]
12-31-98	80.7	50.2	30.5	N/A	N/A	N/A	I
12-31-99	88.8	79.6	9.2	N/A	N/A	N/A	I
12-31-00	101.2	96.9	4.3	N/A	N/A	N/A	I
12-31-01	126.0	110.5	15.5	N/A	N/A	N/A	I
12-31-02	184.0	137.2	46.9	204.0	73.4	130.6	I
06-30-03	202.9	138.8	64.1	224.8	45.4	179.4	I

[14] Section 8.35 of the Act provides for four levels of classification relative to Farmer Mac's capital adequacy, with Level I indicating that Farmer Mac meets both the risk-based and minimum capital requirements. Since Farmer Mac was not required to be in compliance with the risk-based capital regulation until May 23, 2002, the fact that Farmer Mac's core capital is above the statutory minimum core capital requirement warrants an Enforcement Level I classification prior to that date.

Table 4

Outstanding Farmer Mac Loans and Guarantees

	June 30 ($000,000) 2001	2002	2003	Change 2002-2003 Percent	Change 2001-2003 Percent
1. On-Balance Sheet					
a. Farmer Mac I (Post-1996 Act)*	$1,107.7	$990.2	$ 815.4	-17.7%	-26.4%
b. Farmer Mac I (Pre-1996 Act)*	65.0	37.7	28.1	-25.5%	-56.8%
c. Farmer Mac II	491.6	546.3	604.4	10.6%	22.9%
d. Loans Held for Investment	68.6	765.3	873.4	14.1%	1173.2%
e. Loans Held for Sale	10.4	24.3	48.9	-101.2%	370.2%
f. Loans Purchased from AMBS Pools	--	31.4	48.8	55.4%	N/A
g. Real Estate Owned	--	3.3	12.9	290.9%	N/A
h. AgVantage Bonds	20.4	28.1	23.6	-16.0%	15.7%
i. Subtotal	1,763.7	2,426.6	2,455.5	1.2%	39.2%
2. Off-Balance Sheet					
a. Farmer Mac I (Post-1996 Act)	365.7	338.4	282.9	-16.4%	-22.6%
b. Farmer Mac I (Pre-1996 Act)	0.7	0.15	--	-100%	-100%
c. Farmer Mac II	87.6	71.2	64.5	-9.4%	-26.4%
d. Long-Term Standby Purchase Commitments	1537.1	2,336.9	2,790.5	19.4%	81.5%
e. Subtotal	1,991.1	2,746.7	3,137.9	14.2%	57.6%
TOTAL (1.i. + 2.e.)	$3,754.8	$5,173.3	$5,593.4	8.1%	49.0%

*Principal amount versus book value.

Appendix 1

Farm Credit Administration

1501 Farm Credit Drive
McLean, Virginia 22102-5090
(703) 883-4000

August 21, 2003

Ms. Davi M. D'Agostino
Director, Financial Markets and
Community Investment
United States General Accounting Office
441 G Street, NW
Washington, DC 20548

Dear Ms. D'Agostino:

The Farm Credit Administration (FCA) appreciates the opportunity to comment on the General Accounting Office's (GAO) draft report entitled Farmer Mac: Greater Attention to Risk Management, Mission, and Corporate Governance is Needed (the Report). While we have some suggestions and clarifying comments regarding conclusions reached about FCA, overall we believe the Report is a fair representation of our work to oversee the safety and soundness of the Federal Agricultural Mortgage Corporation (Farmer Mac or Corporation).[15] Moreover, we expect the Report to add value to our work on several initiatives already underway at FCA.

The Report includes the following five recommendations for FCA's oversight of Farmer Mac:

- consider potential improvements to the Risk-based Capital Stress Test (RBC model);
- improve and formalize offsite monitoring including regulatory reporting;
- reduce potential safety and soundness concerns that may arise from "capital arbitrage" activities of Farmer Mac and Farm Credit System (FCS or System) banks and associations;
- examine how other secondary market regulators developed regulations to require government-sponsored enterprises to obtain a risk rating from nationally recognized statistical rating agencies; and
- assess and report on the impact of Farmer Mac's activities on agricultural real estate lending markets.

FCA will fully consider and incorporate the Report's recommendations into its oversight of Farmer Mac both through current regulatory and examination work in process and, as necessary, new initiatives.

GAO recognizes that work relating to several items discussed in the Report is currently underway within FCA. This work includes two projects on FCA's current regulatory agenda addressing Farmer Mac's liquidity and nonprogram investments, and revisions to the RBC model. Further initiatives include plans for updating Call Report formats and instructions to

[1] Farmer Mac is established separately by Title VIII of the Farm Credit Act of 1971, as amended (12 U.S.C. 2279aa-2279cc). Subtitles A and B of Title VIII authorize the FCA to examine the Corporation and provide for the regulation and general supervision of its safe and sound performance, including promulgation of regulatory capital standards.

improve offsite monitoring, and possible regulatory action on two items - the capital issues arising when System institutions enter into Long-term Standby Purchase Commitments (Standbys) with Farmer Mac, and FCS credit exposure to guarantors that do not have a credit rating, such as Farmer Mac. As part of that process, we will examine how other regulators have imposed credit rating requirements.

In addition, the Report includes suggestions for Congressional consideration. Regarding Farmer Mac's mission, GAO suggests Congress establish clearer mission goals for Farmer Mac. It also suggests Congress allow FCA more flexibility to establish capital standards commensurate with Farmer Mac's changing risk profile and in setting minimum capital standards. We support these suggestions and will assist Congress as they are considered. In addition, we will reexamine authorities provided in existing legislation for FCA to pursue these suggestions.

Without making a recommendation, the Report points out a potential conflict of interest resulting from a single regulator overseeing both primary and secondary market institutions. The Report also notes FCA's awareness of this potential conflict and alludes to our belief that we are successfully managing any associated risk. In response, we emphasize that FCA is committed to delivering the highest standard of financial institution supervision. Congress established FCA's Office of Secondary Market Oversight (OSMO) as a separate office to oversee Farmer Mac with foresight of the issue raised by the Report. FCA continues to preserve the independence of OSMO within its organizational structure. FCA will periodically reassess the changing dynamics involved in regulating both FCS lending institutions and Farmer Mac and will remain vigilant in addressing any concerns arising from this dual responsibility.

FCA's comments on the recommendations regarding the RBC model are enclosed. These comments focus on the unique aspects of risk analysis of agricultural credit and the scientific properties of the model we developed under guidance provided in Title VIII of the Farm Credit Act of 1971, as amended (Act). Generally, FCA would stress that the RBC model was developed based on reasoned and conservative judgment, the best available data, accepted econometric methodologies, transparent procedures, and, most significantly, in conformance with the governing statutory provisions of the Act.

As envisioned by FCA in the RBC model's final rule, ongoing changes to the model are anticipated based on: developments in regulatory guidelines (e.g., New Basel Accord); new types of business activity; institutional change; financial innovations; new data sources and availabilities; refinements in methodologies; financial market conditions; and statutory amendments. As part of our planned regulatory project on revisions to the RBC model, we also will consider GAO's findings and recommendations.

Again, we thank you for the opportunity to provide these comments and the technical comments that were provided separately. We hope you find them useful as the final report is published.

Sincerely,

Michael M. Reyna
Chairman and Chief Executive Officer

Enclosure