



Farm Credit Services

“The Ag Loan Process”

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Welcome

- On behalf of the Farm Credit Services in Arkansas we are proud to be sponsors of the 2005 Arkansas Women in Ag Conference.
- Also, the opportunity to discuss Ag Lending from our perspective as women involved in ag lending.

Arkansas Farm and Finance Facts

- According to the 2002 Ag Census there are 47,474 farms in Arkansas.
- 18,484 of those farms reported interest expenses.
- 13,461 farms reported that they have a loan secured by real estate.
- Arkansas has a total ag debt market of approximately \$4.7 billion dollars.

Lending to Farmers and Ranchers

- For almost 90 years the Farm Credit System has been serving farmers, ranchers and rural home owners in Arkansas.
- Farm Credit Services operates as a cooperative –owned and controlled by the members served.
- Its purpose was to provide sound and constructive credit to farmers and ranchers at competitive interest rates thus benefiting as borrowers and as stockholders.

Sound and Constructive Lending

- The ag loan process is usually the start of long term relationship created with a call to a lender, a visit to their office with a borrowing purpose or even a loan officer visiting a prospective customer at their farm about financing opportunities.
- As with any relationship trust is built or grows with the understanding of each others needs and the ability of the borrower to benefit from the lender's competitive products and services.

Loan Purpose & Eligibility

- Purpose and eligibility can be the first step in the ag loan process.
- Purpose most times will dictate the loan terms and amortization, repayment etc.
- Eligibility at Farm Credit means borrower is: a Bona fide farmer (full or part time), a Rural Resident, involved in a farm related business, or involved in a process/marketing business.
- Some lenders may use purpose and eligibility to determine if the loan would be maintained "in house or sold into the secondary market.

In Good Times or Bad

- At Farm Credit we pride ourselves in being a lender that strives to maintain a borrower/lender relationships both in “good times as well as bad.”
- In order to do that we examine a number of credit factors that can impact the loan.
- Be it borrower, Farm Credit or a local bank, in a lending transaction someone is taking risk.

The Five C's Process

- Almost every ag lender you seek for an agriculture loan purpose will begin evaluating you and your operation using the “Five C's of credit”.
- There may be some variations between lenders regarding the definitions and loan underwriting analysis of the Five C's, however, most loan files will contain a detailed credit write up assessing the borrower's loan request as it relates to their analysis of the Five C's.

The Five C's of Ag Lending

- Character – people and credit history
- Capital – financial position
- Capacity – ability to repay debt
- Collateral – security and margin in loan
- Conditions – additional terms or loan requirements if necessary

What is analyzed? Using the Five C's

The 5 C's -Character

- Character- a lender will analyze character in a variety of ways, however, in today's world, the standard is using a credit bureau report as an indicator of character and your history in repaying loans on time.
- Credit Score - ideal
- Also, knowledge of you, your family and reputation in the community are important in determining character.

The Five C's- Capital

- Capital is your financial position as measured on a balance sheet or financial statement including
 - Assets
 - Liabilities
 - Net Worth
 - Ownership Equity as a percentage
 - Working Capital
 - Current Ratio

The 5 C's –Assets & Liabilities

- Assets: Short-term, Intermediate, and Long-term
- Liabilities: Short-term, Intermediate, and Long-term

Short-term: less than 12 months
Intermediate: 1-10 years
Long-term: 10 or more years

The 5 C's Assets & Liabilities cont.

- Assets...Anything owned of value.
Verification sources: statements, appraisal reports, etc.
- Liabilities...Anything owed on an asset.
Typically, a credit report is requested to ensure creditability.

The 5 C's – Net Worth

- Assets – Liabilities = Net Worth
- Net Worth is a measure of a customer's financial worth.
- Evaluating Net Worth gives you an understanding of lifestyle and family living expenses.

The 5 C's - Ownership Equity

- Ownership Equity = Net Worth / Total Assets
- The amount of equity held in items of ownership.
- This tells you how much equity there might be in other sources of collateral.

The 5 C's – Working Capital

- Working Capital = Current Assets – Current Liabilities
- Shows you the amount of liquid assets available to pay current liabilities.
- Shows you how well the consumer utilizes and maintains resources.

The 5 C's - Current Ratio

- CR = Assets / Current Liabilities
- It's how much "money" the person has compared to what they owe within a year i.e. credit card debt, accounts payable, notes due within one year.

The 5 C's - Capacity

- CDRC = Capital Debt Retirement Capacity
- Also a measurement of Cash Flow
- Calculated by adding Net Earnings, Depreciation, and Interest
- This is how much the consumer has in total cash flow to pay for debt

The 5 C's - CDRC Margin...

- The amount of money left over after paying for the new debt plus any existing debts.

The 5 C's – Collateral

- To reduce risk lenders require collateral or security for loans; basically for protecting their risk position should the borrower default.
- The loan purpose, loan terms, and/or financial position generally drive the collateral or security requested or pledged by the borrower for the loan.

The 5 C's - Loan to Value

- The LTV or “Loan to Appraised Value” is a measurement of risk
- $\text{Loan amount} / \text{Appraised Value} = \text{LTV}$
- This benefits both borrower and lender to know how much equity the collateral would yield
- Standards vary depending on subject: House, Land, Equipment, Cattle, etc...

The 5 C's - Conditions

- Conditions are applicable by the lender to monitor and control their risk.
- They may include loan agreement requirements that offset weaknesses of another credit factor i.e. capacity, loan to value, or capital.

Importance of Credit Score

- Today more and more ag lenders use credit score as a way to assess credit worthiness of borrowers.
- Farm Credit uses credit scoring as a tool in our “On-the-Spot” loan process.
- Minimal information is required for making the loan and the credit bureau score is relied on more heavily.

Importance of Credit Score

- No derogatory accounts
- Request annually, new free credit reporting
- No collections/bankruptcies/tax liens/etc...
- Contact creditor and close any unused account when cutting up your card
- Rolling balances for cheaper rates lowers impact your score
- Bureaus link inquiries to not hurt your score (Home or Car Shopping)

Preparing for a Loan

- Earnings Information (tax returns, etc.)
- Completed Application and Balance Sheet
- List of Machinery, Equipment,
- Cash Flow, Business Plan, Budget
- Real Estate description of farms
- Offer and Acceptance w/ complete legal description (if new purchase)
- Contractor's Bid on Construction
- Employment Verification
- Other information as needed



Farm Credit Services

- We are committed to helping you maximize your financial success.
- We offer a variety of loan products and related services providing solutions designed around your needs and cash flow.
- Agriculture expertise
- Local service and relationships with lending professional customers want and count on
- Competitive interest rates & flexible options



Farm Credit Services

- Arkansas' number one agricultural lending choice
- The only source for all your farm, family and rural living needs
- We want to be your lender – let us show you how we can maximize your financial success today!

With a farm economy this diverse, it's good to know we're a financial partner who's just as diversified.

Just like Arkansas, we're a diverse resource for farmers. Our experienced staff can help with everything from crop loans to crop insurance, farm equipment, land appraisal, life/disability insurance, financial planning and a whole lot more. We're working hard to help you succeed for the state of farming today.

1-800-444-FARM www.farmcredit.com



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