S&P Global Ratings

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American AgCredit ACA

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American AgCredit ACA

Major Rating Factors

Issuer Credit Rating
BBB+/Stable/--

Strengths:	Weaknesses:
• Track record of low loan losses and solid profitability • Access to favorably priced funding through CoBank • Strong risk-adjusted capital (RAC) ratio	• Exposure to cyclical commodity prices and unpredictable agricultural conditions • Limited business diversification • Higher-than-peer growth could indicate greater risk appetite

Outlook

The stable outlook reflects our expectation that over at least the next two years, American AgCredit (AAC) will continue to report good earnings, maintain an S&P Global Ratings RAC ratio between 10%-15%, and have uninterrupted access to funding and liquidity from CoBank. In addition, we expect asset quality will remain solid as the U.S. continues its economic recovery following the COVID-19 pandemic.

Downside scenario

We could lower our ratings on AAC if capital ratios were to decline meaningfully from current levels such that the RAC ratio were to fall below and remain lower than 10%, if credit quality metrics weakened substantially, or if we perceived that the association's high growth targets were leading it to loosen its underwriting standards.

Upside scenario

Conversely, we could raise our ratings on AAC if its capital ratios grew, and we believed its RAC ratio would remain above 15% on a sustainable basis, if the pace of balance sheet growth moderated, and if loan and revenue diversification improved. We would also look favorably on an increase in the association's proportion of on-balance-sheet liquidity.

Rationale

Our rating on AAC and its subsidiaries American AgCredit FLCA and American AgCredit PCA balances the company's solid credit history, good earnings, strong capital ratios, and the substantial funding and borrowing capacity that it receives as a member of the Farm Credit System (FCS) against its concentration in the cyclical agricultural sector and high growth rates compared with peers.

AAC's performance has been solid over the past several years, despite volatility in the agricultural markets caused by changes in U.S. trade policies and the COVID-19 pandemic. Earnings have remained strong and above peers', reflecting strong loan growth, low provisions, declining efficiency ratios, and the low-cost funding it enjoys as a member of the Farm Credit System. Although the robust loan growth has pressured capital ratios, they remain strong, buttressed by recent issuance of preferred stock and subordinated debt. AAC's asset quality is consistently healthy, with low levels of nonperformers and loan losses. That said, we believe the loan portfolio, which consists entirely of agricultural-related loans as mandated in AAC's charter, remains highly vulnerable to shifts in market conditions. We expect AAC to continue to generate good earnings, with strong asset quality, and to maintain healthy capital ratios over at least the next two years.

Anchor: Adjusted to reflect regulated status, low competitive risk, and favorable funding

Our starting point--or anchor--for our rating on AAC is 'bb+', in line with that for other U.S. companies that we rate under our nonbank financial institutions criteria. Because of AAC's public policy role, access to government-related entity (GRE) funding, and regulated status, we raise its anchor to 'bbb+', three notches above our anchor for other finance companies and equal to that of U.S. banks. This is to account for the Farm Credit Administration's regulatory oversight, the company's favorable funding through its position in the FCS, and its strong competitive position.

Table 1

American AgCredit, ACA Key Figures

		--Year-ended Dec. 31--			
(Mil. $)	**2021***	**2020**	**2019**	**2018**	**2017**
Adjusted assets	15,447.6	15,094.1	12,663.4	10,914.0	9,964.8
Customer loans (gross)	14,581.4	14,170.9	11,844.8	10,214.8	9,306.9
Adjusted common equity	2,377.6	2,214.1	2,113.9	2,002.4	1,920.0
Operating revenues	282.3	485.6	396.8	345.8	315.7
Noninterest expenses	102.0	228.8	190.7	173.9	153.9
Core earnings	177.3	247.3	200.7	169.4	159.1

*Data as of June 30.

Business position: Solid market position limited by concentration risk

Our view of AAC's business position is based on its solid market position as an agricultural lender in seven states and its role as an association operating within the FCS. With $15.4 billion in assets as of June 30, 2021, AAC is the fourth-largest association in the FCS and the largest in the CoBank district. However, its concentration in agricultural loans--with large exposures to vineyards and wineries, field crops, tree fruits and nuts, dairy, and other agricultural commodities--somewhat offsets these strengths. In addition, AAC's loan growth in recent years, spurred in part by its shift to an increasingly digital lending platform, has been high at an average of 14% annually over the past five years. We view the deepening of the association's market share to 28% from 25% because of this growth favorably. However, we also see such outsize growth as a sign of increased risk appetite. That said, we view AAC's management and governance as satisfactory, given management's extensive experience in the agricultural lending industry and its solid risk management with a record of strong asset quality and conservative underwriting.

Both American AgCredit FLCA and American AgCredit PCA are wholly owned subsidiaries of American AgCredit ACA. As of June 30, 2021, American AgCredit FLCA and American AgCredit PCA collectively held approximately all the group's assets and generated all its net income. American AgCredit FLCA provides long-term real estate mortgage loans, and American AgCredit PCA provides short-term and intermediate-term loans to agricultural borrowers.

Table 2

American AgCredit, ACA Business Position

		--Year-ended Dec. 31--			
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Return on average common equity	15.6	11.5	9.8	8.7	9.0

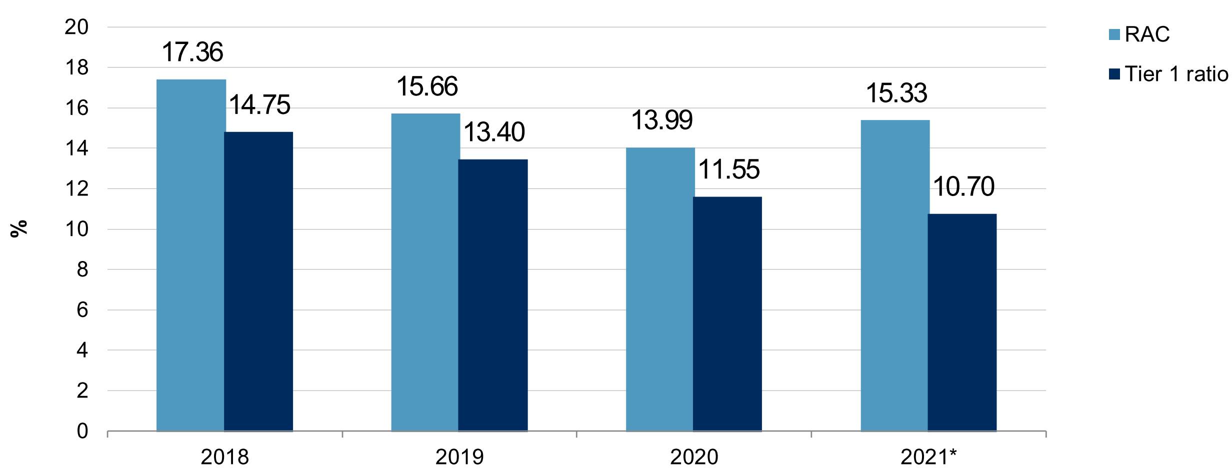
*Data as of June 30.

Capital and earnings: Strong risk-based capital

Our assessment of AAC's capital, leverage, and earnings incorporates the company's high regulatory capital ratios, combined with low credit loss provisions and satisfactory retention of earnings after patronage payments. However, outsize loan growth has pressured capital ratios, with the association's common equity Tier 1 ratio falling to 10.70% as of June 30, 2021, from 15.4% at year-end 2017, while its total capital ratio decreased to 11.50% from 15.6% over the same period. We calculated an S&P Global Ratings RAC ratio of 15.3% as of June 30, 2021, which is just above the 10%-15% range we consider strong. We believe continued above-average loan growth could pressure capital ratios further, and AAC's RAC ratio will decline to below 15% within the next two years. The company's issuance of $300 million of preferred stock in June 2021 offset in part the redemption of an existing preferred issue and had only a modest impact on AAC's capital ratios. The company pays a patronage, or refund, to its members of approximately 57% of earnings annually. We expect the company to pay a similar percentage going forward.

Chart 1

S&P Global Ratings Risk-Adjusted Capital Versus Tier 1 Ratio



*As of June 30, 2021. Source: S&P Global Ratings.

We expect AAC's profits to increase in 2021, with increased net interest income propelled by loan growth, continued low provisions given low net charge-offs (NCOs), and slightly improving efficiency measures. Noninterest revenue typically contributes more than 20% of total revenue. AAC's revenue growth has outpaced expense growth in recent years, indicating improving efficiency at the association.

Table 3

American AgCredit, ACA Capital And Earnings

		--Year-ended Dec. 31--			
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Tier 1 capital ratio	11.0	11.6	13.4	14.8	15.4
S&P Global Ratings' RAC ratio before diversification	15.3	14.0	15.7	17.4	N/A
S&P Global Ratings' RAC ratio after diversification	10.9	10.0	11.1	10.8	N/A
Adjusted common equity/total adjusted capital	88.8	92.7	94.3	94.1	93.8
Net interest income/operating revenues	77.2	76.0	77.5	77.5	80.9
Fee income/operating revenues	3.2	4.5	3.5	5.2	5.2
Market-sensitive income/operating revenues	0.1	(0.7)	N/A	0.1	0.2
Cost to income ratio	36.1	47.1	48.1	50.3	48.8
Preprovision operating income/average assets	2.4	1.9	1.7	1.6	1.7
Core earnings/average managed assets	2.3	1.8	1.7	1.6	1.7

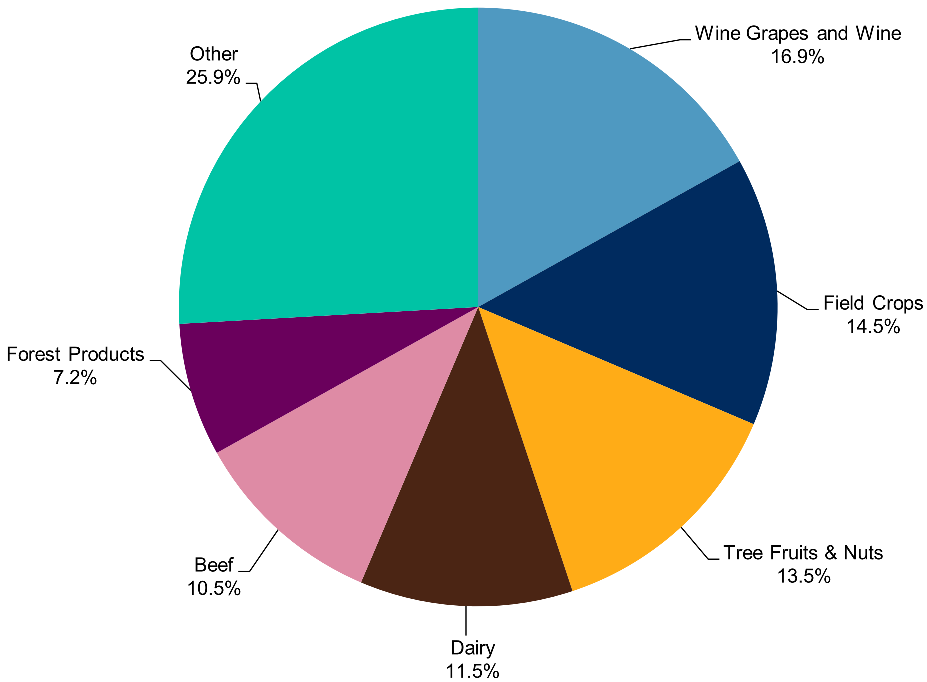
*Data as of June 30. N/A--Not applicable.

Risk position: Good asset quality measures

AAC's loan portfolio is somewhat more diversified by product and geography than that of many other associations. The portfolio comprises different product and commodity types. Similarly, AAC is geographically diverse, with the largest exposures to California (52%), Kansas (12%), and Colorado (9%) and the remainder of the portfolio spread across the U.S. and Guam. The association actively engages in loan participations with other Farm Credit institutions to manage risk and to improve portfolio diversification. About 21% of the loan portfolio was purchased and about 25% of total commitments sold as of June 30, 2021.

Chart 2

Loan Composition As Of June 30, 2021



Source: S&P Global Ratings.

AAC's loan credit quality is excellent, with NCOs averaging a minimal two basis point (bps) annually in the past five years. Similarly, AAC's nonperforming assets (NPAs; including troubled debt restructurings) have been stable and low at 44-51 bps of loans and other real estate over the past five years. We believe AAC's underwriting and concentration limits are conservative, as this record indicates. Although the association's allowance for loan losses, which measured 0.24% of loans as of June 30, 2021, is low on an absolute basis, we believe it is appropriate relative to the low level of NPAs and NCOs.

Table 4

American AgCredit, ACA Risk Position

		--Year-ended Dec. 31--			
(%)	**2021***	**2020**	**2019**	**2018**	**2017**
Growth in customer loans	5.8	19.6	16.0	9.8	16.2
Total diversification adjustment/S&P Global Ratings' RWA before diversification	40.7	39.8	40.9	60.6	N/A
Total managed assets/adjusted common equity (x)	6.5	6.8	6.0	5.5	5.2
New loan loss provisions/average customer loans	0.0	0.1	0.0	0.0	0.0
Net charge-offs/average customer loans	0.0	0.0	0.0	0.0	0.0
Gross nonperforming assets/customer loans + other real estate owned	0.5	0.5	0.5	0.5	0.4

Table 4

American AgCredit, ACA Risk Position (cont.)					
		--Year-ended Dec. 31--			
(%)	2021*	2020	2019	2018	2017
Loan loss reserves/gross nonperforming assets	48.3	49.5	42.7	42.9	47.5

*Data as of June 30. N/A--Not applicable.

Funding and liquidity: Concentrated funding source, offset by very stable access to low-cost funding

Unlike most other FCS associations, AAC manages its funding through a block funding arrangement with CoBank (most associations match-fund through their funding banks). AAC determines its funding strategy and product offerings, and CoBank executes debt issuance via the Funding Corp. on its behalf. Because AAC does not match-fund through CoBank, it manages its own interest rate risk. Board policies limit sensitivity to a 200-bps shift in interest rates to 10% of net interest income. As of Dec. 31, 2020, management estimated that a 200-bps rise in rates would increase net interest income by 2.1%, while a downward regulatory shock scenario would decrease net interest income by 0.1%. As part of its arrangement, AAC maintains liquidity coverage consistent with CoBank's requirements for 15, 30, 90, and 120 days of liquidity. CoBank allocates $3.7 billion of its investment portfolio to AAC for liquidity measurement purposes. In addition, AAC held $20 million of cash on the balance sheet as of June 30, 2021, and it had access to the additional liquidity available through its direct note with CoBank.

We view favorably AAC's long-term general funding agreement with CoBank, one of the four banks making up the government-sponsored FCS, which lends to associations like AAC. The five-year running agreement provides a low-cost, stable, and primary funding source for AAC. The direct note with CoBank provides it with enough funding for its lending activity, up to a maximum borrowing base, which is redetermined annually, though it can be renegotiated as needed. Although AAC is largely dependent on this primary source of funding, we see little risk that it would lose access to funding from CoBank, based on its long historical funding relationship with the bank since the founding of the FCS. Moreover, the association's issuance of preferred stock and subordinated debt in June 2021 demonstrates its ability to tap additional funding sources if needed. We believe AAC could likely obtain additional liquidity, if necessary, by issuing additional debt or preferred stock, or through whole loan or participation sales.

Table 5

American AgCredit, ACA Funding And Liquidity					
		--Year-ended Dec. 31--			
(%)	2021*	2020	2019	2018	2017
Long-term funding ratio	62.5	61.9	54.9	52.8	62.2
Stable funding ratio	60.2	59.4	52.9	50.8	60.0
Short-term wholesale funding/funding base	45.5	45.5	55.1	58.9	47.8
Short-term wholesale funding/total wholesale funding	44.4	44.9	54.4	58.1	47.1

*Data as of June 30.

Support:

While the rating incorporates the ongoing funding benefits that the association receives as a member of a GRE, we believe there is a low likelihood that the U.S. federal government would provide extraordinary support directly to AAC in the event of financial distress. Our assessment is that AAC's individual role is of limited importance to the federal government. In addition, we view AAC as having a limited link to the government. Its members privately own AAC, and the government has no history of providing extraordinary government support directly to associations like it. Therefore, the issuer credit rating does not incorporate any uplift for extraordinary government support.

Additional rating factors: Group structure, rated subsidiaries, and hybrids

We view American AgCredit FLCA and American AgCredit ACA as core subsidiaries to the parent, American AgCredit ACA. We expect AAC to support both entities under all foreseeable circumstances, if needed. We rate AAC's hybrid securities, including its subordinated debt and preferred stock, relative to its group stand-alone credit profile (SACP) to reflect the possibility these instruments could face nonpayment risk before more senior instruments. As such, we rate the subordinated debt issued by the core subsidiaries 'BBB' (one notch below the group SACP for contractual subordination) and AAC's preferred stock 'BB+'(three notches below the group SACP for risk of deferral and coupon nonpayment).

Ratings Score Snapshot

Issuer Credit Rating: BBB+/Stable

SACP: bbb+

- Anchor: bb+
- Sector-specific anchor adjustment: (+3)
- Business position: Moderate (-1)
- Capital, leverage, and earnings: Strong (+1)
- Risk position: Adequate (0)
- Funding and liquidity: Adequate and Adequate (0)
- Comparable ratings adjustment: 0

External influence: 0

- Government influence: 0
- Group influence: 0
- Rating above the sovereign: 0

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Financial Institutions | General: Nonbank Financial Institutions Rating Methodology, Dec. 9, 2014
- Criteria | Financial Institutions | General: Issue Credit Rating Methodology For Nonbank Financial Institutions And Nonbank Financial Services Companies, Dec. 9, 2014
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Federal Farm Credit Banks, Oct. 15, 2021
- CoBank ACB, Oct. 5, 2021
- AgTexas Farm Credit Services Assigned 'BBB' Rating, Preferred Stock Rated 'BB'; Outlook Stable, Sept. 23, 2021
- Compeer Financial ACA, June 24, 2021
- American AgCredit FLCA, American AgCredit PCA Rated 'BBB+'; Joint Subordinated Debt At 'BBB'; Preferred Stock At 'BB+', June 4, 2021
- American AgCredit ACA Assigned 'BBB+' Rating; Outlook Stable, May 19, 2021
- Capital Farm Credit ACA, Jan. 12, 2021
- AgriBank FCB, Sept. 29, 2020

Ratings Detail (As Of October 20, 2021)*	
American AgCredit, ACA	
Issuer Credit Rating	BBB+/Stable/--
Preferred Stock	BB+
Issuer Credit Ratings History	
19-May-2021	BBB+/Stable/--
Sovereign Rating	
United States	AA+/Stable/A-1+
Related Entities	
American AgCredit FLCA	
Issuer Credit Rating	BBB+/Stable/--
American AgCredit, PCA	
Issuer Credit Rating	BBB+/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.