

# FEDERAL AGRICULTURAL

Rating Analysis - 9/1/16

Debt: \$14.8B, Cash: \$1.8B

Est. Share Value: \$40.58 Price: \$40.98

\*EJR Sen Rating(Curr/Prj) A/ A

\*EJR CP Rating: A1

EJR's 3 yr. Default Probability: 1.5%

EJR 3 yr. Recov. Rate: 68.4%

Federal Agricultural Mortgage Corporation Class C's (AGM) operating income were \$23.7M for the quarter ending June 2016 vs \$39.1M for the prior year. Net Income for the June '16 quarter was \$15.3M vs the prior year's \$25.5M income.

AGM's total interest inc in June '16 qtr grew by 16.3% YoY to \$77.2M attributed to increases in Investments and cash equivalents, Farmer Mac Guaranteed Securities and USDA Securities and Loans all increased by 112%, 8% & 16% resp. Int exp rose by 24.3% to \$42.9M. Net interest inc grew by 7.8% YoY due to increase in short- term interest rates on assets and liabilities as well as growth in outstanding biz vol and increase in cash basis interest inc from Farm & Ranch loans. Prov for loan losses grew from \$110K to \$364K in 2Q16. Losses on fin'l derivatives and hedging activities by \$4.7M led to non-int loss of \$234K vs \$18.2M non-int inc in 2Q15. These led to 39.8% decline in net inc by 2Q16. Mkt Cap is \$429M. Affirming.

CREDIT POSITION	Annual Ratios		Ratios for 4 Rolling Quarters				
	Dec-15	PDec17	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16
Fixed Chg Cov(x)	1.8	2.0	1.7	1.7	1.8	1.7	1.6
Return on Equity (%)	12.4	14.2	9.4	9.5	10.9	12.7	10.1
PT Ret. on Avg Assets(%)	0.7	0.8	0.7	0.6	0.7	0.7	0.6
Ret on Perm Cap (%)	0.7	0.9	0.7	0.7	0.7	0.7	0.6
T Debt/Cap(w Debt)(%)	96.2	96.2	95.9	96.1	96.2	96.4	96.2
Short Term Debt/ Total Debt (%)	64.7	69.1	55.9	61.3	64.7	63.9	68.2
Implied Sen. Rating	A-	A	A-	A-	A-	A-	A-

INDUSTRY RATIOS	AA	A	BBB	BB	B	CCC
Fixed Chg Cov(x)	2.3	1.8	1.3	0.9	0.7	0.5
Return on Equity (%)	4.5	4.0	3.5	3.0	2.5	2.0
PT Ret. on Avg Assets(%)	6.0	4.0	2.0	0.0	-2.0	-4.0
Ret on Perm Cap (%)	20.0	10.0	7.0	4.0	2.0	-2.0
T Debt/Cap(w Debt)(%)	85.0	90.0	95.0	97.0	98.2	100.0
Short Term Debt/ Total Debt (%)	47.5	62.2	75.3	84.9	90.7	94.2

PEER RATIOS	Other	Fixed	Return	Return	Return	Ratio-	
	NRSRO	Charge	on Avg	on Perm	T Debt/	Implied	
	Sen.	Cov(x)	ROE(%)	Assets	Cap(%)	Cap(%)	Rating*
Federal Home Loan Mortgage Corporation	AAA	1.2	216.9	0.8	0.5	99.9	BBB
Federal National Mortgage Association	AAA	1.2	269.9	0.5	0.5	99.9	BBB
Starwood Property Trust, Inc.	BB	2.4	10.7	0.5	2.5	56.6	AA-
Walter Investment Management Corp.	B+	0.7	-32.7	-2.1	-1.1	95.4	B
Ocwen Financial Corporation	B	0.6	-28.9	4.6	-2.5	87.2	B

Note, Annual Implied Sen. Ratings are smoothed  
Rating Change Anticipator (1 is best, 100 worst): 41.2 Last EJR Sen.: A

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## REVENUE & PROFITABILITY

The Company's revenues declined at an average annual rate of 0.7% over the last five years while operating margin rose to 1.05% for the fiscal year ending December 2015, above the 0.97% average over the prior four years. Return on Assets rose to 0.44%, above the 0.35% average for the prior year.

	Dec-11	Dec-12	Dec-13	Dec-14	Dec-15	PDec16	PDec17
Interest Income (mill \$)	275	265	235	231	265	292	322
Growth Rate (%)		(3.65)	(11.06)	(2.05)	14.85	10.30	10.30
Net Interest Income/Total Interest Income (%)	44.16	46.09	41.68	25.96	47.51	52.41	53.91
Loan Loss Coverage(%)	NMF	NMF	NMF	NMF	NMF	NMF	NMF
Pretax Return On Avg Assets (%)	0.37	0.74	1.01	0.53	0.72	0.80	0.82
Oper Return/ Earning Assets (%)	0.58	1.02	1.41	0.80	1.05	1.15	1.15
Non-Interest Inc/Revs (%)	3.6	11.4	2.9	6.16	13.00	13.20	13.58
Efficiency Ratio(%)	27.8	25.8	(11.1)	23.89	21.21	21.42	23.00
Return on Assets (%)	0.1	0.4	0.6	0.34	0.44	0.50	0.51

## LEVERAGE & ASSET LIQUIDITY

The Quick Asset Ratio has become weaker recently, slipping to 8.6:1 for the FYE December 2016.

	Dec-11	Dec-12	Dec-13	Dec-14	Dec-15	PDec16	PDec17
Quick Asset Ratio(%)	9.2	7.1	6.5	10.4	8.6	8.5	8.3
Quick Assets/ ST Dep & Debt(%)	0.1			-	-	-	-
LT Debt/ Capital (%)	88.1	89.5	89.7	87.5	90.0	89.3	88.6
T Debt/Cap(w Debt)(%)	94.8	95.1	95.6	94.3	96.2	96.2	96.2

**ASSUMPTIONS FOR FINANCIALS**
**Valuation Driver: Interest Income Growth:**

Federal Agricultural has grown its interest income at 14.9% per annum in the last fiscal year which is more than the average for its peers. We expect Company's revenues will grow approximately 10.3% per annum over the next couple of years and 9.3% per annum for the next couple of years thereafter.

**Valuation Driver: Net Interest Margin:**

Company's net interest margin has been more than its peers and we assumed no growth in net interest margin over the next two years.

Income Statement	Peer Median	Co. Avg.	Assumptions	
			Yr 1&2	Yr 3,4,5
Interest Income Growth%	(3.4)	14.9	<b>10.3</b>	<b>9.3</b>
Interest Expense (% of outstanding debt)	3.7	1.0	<b>1.0</b>	<b>1.0</b>
Net Interest Margin (% of earning assets)	0.3	1.2	<b>1.2</b>	<b>1.1</b>
Provisions for Loan Losses(% of earning assets)	0.0	0.0		
Trading Account Profit Growth%	0.0	(96.8)	<b>2.0</b>	<b>2.2</b>
Commissions & Fees Earned Growth%	(11.7)	(44.1)	<b>(10.0)</b>	<b>(9.0)</b>
Other Operating Income Growth%	(37.4)	(88.5)	<b>(10.0)</b>	<b>(10.0)</b>
Non-Interest Expense Growth%	8.3	33.1	<b>20.3</b>	<b>18.3</b>
Net Non-Operating Loss Growth%	(68.7)	(100.7)		
Income Tax Rate%	31.7	31.7	<b>31.7</b>	<b>28.5</b>
Special Items (millions \$)	0.0			
Cash & Near Cash Growth%	0.0	(11.2)	<b>6.0</b>	<b>6.0</b>
Accounts & Notes Receivable Growth%	(7.0)	4.5	<b>4.5</b>	<b>4.5</b>
Marketable Secs. & ST Investments Growth%	0.0	0.0	<b>6.3</b>	<b>6.3</b>
Loans & Mortgages Growth%	(0.4)	0.0		
Real Estate Investments Growth%	0.0	0.0		
Other Long-Term Investments Growth%	(24.9)	10.4	<b>10.3</b>	<b>10.3</b>
Long-Term Investments before Reserves Growth%	(3.7)	10.4	<b>10.3</b>	<b>10.3</b>
Loan Loss Reserves (% of Earn. Assets.)	0.0	0.0	<b>5.0</b>	<b>5.0</b>
Loans Net of Reserves Growth%	0.0			
Net Fixed Assets Growth%	0.0	0.0		
Other Assets Growth%	0.0	0.0		
Demand Deposits Growth%	0.0			
Short-Term Borrowings Growth%	(16.4)	23.9	<b>10.3</b>	<b>10.3</b>
Customer Deposits Growth%	0.0	0.0		
Other ST Liabilities Growth%	0.0	0.0		
Long-Term Borrowings Growth%	0.3	(9.2)	<b>0.5</b>	<b>0.5</b>
Deferred Tax Liability Growth%	0.0	(93.5)	<b>3.0</b>	<b>3.0</b>
Other Long-Term Liabilities Growth%	(6.2)	33.4	<b>13.4</b>	<b>13.4</b>
Shares sold (% of shares out.)	0.0	(0.5)	<b>(0.4)</b>	<b>(0.4)</b>
Additional ST debt (1st year)(millions \$)	0.0	0.0	<b>0.1</b>	

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EJR 3 yr. Recov. Rate: 68.4%

## ANNUAL INCOME STATEMENTS

Below are Federal Agricultural's annual income statements with the projected years based on the assumptions listed on page 3.

### ANNUAL INCOME STATEMENTS (MILLIONS \$, EXCEPT PER SHARE AMOUNTS)

	Dec-12	Dec-13	Dec-14	Dec-15	PDec16	PDec17
Interest Income	265	235	231	265	292	322
Interest Expense	143	137	171	139	139	148
Net Interest Income	122	98	60	126	153	174
Provisions for Loan Losses	2	0	-3	0		
Trading Account Profit		-1	39	1	1	1
Commissions & Fees Earned	25	27	25	14	13	11
Other Operating Income	-23	-7	-32	-4	-3	-3
Non-Interest Expense	32	-13	22	29	35	42
Operating Income	90	130	73	108	129	141
Net Non-Operating Loss	-1	-1	0	0	0	0
Income Tax Expenses	22	34	3	34	41	45
Income Before XO Items	69	98	70	74	88	96
Extraordinary Item Net of Tax						
Minority Interests	22	22	22	5	5	5
Consolidated Net Income	47	75	48	69	83	91
Total Cash Preferred Dividends	3	3	10	21	21	21
Net Income	44	72	38	47	61	70
Common Dividends	7	8	6	20	21	21
Total Revenues	267	255	262	276	162	182
Comprehensive Income per Share	3	6	3	2		
Basic EPS Before Abnormal Items	4	6	3	4	8	
Basic EPS Before XO Items	4	6	3	4	8	9
Basic EPS	4	7	4	4	7	8
EBITDA						

### REVENUE & PROFITABILITY

Interest Income (mill \$)	265	235	231	265	292	322
Growth Rate (%)	-3.6	-11.1	-2.0	14.9	10.3	10.3
Net Interest Income/Total Interest Income (%)	46.1	41.7	26.0	47.5	52.4	53.9
Loan Loss Coverage(%)	0.0	0.0	0.0	0.0	0.0	0.0
Pretax Return On Avg Assets (%)	0.7	1.0	0.5	0.7	0.8	0.8
Oper Return/ Earning Assets (%)	1.0	1.4	0.8	1.1	1.2	1.1
Non-Interest Inc/Revs (%)	11.4	2.9	6.2	13.0	13.2	13.6
Efficiency Ratio(%)	25.8	-11.1	23.9	21.2	21.4	23.0
Return on Assets (%)	0.4	0.6	0.3	0.4	0.5	0.5

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## ANNUAL BALANCE SHEETS

Below are Federal Agricultural's balance sheets with the projected years based on the assumptions listed on page 3. As of Dec17, the Company's total cash is assumed to increase from \$749M to \$1.4M while its Long-Term Borrowings is assumed to rise from \$12.3B to \$16.1B.

### ANNUAL BALANCE SHEETS (MILLIONS \$, EXCEPT PER SHARE AMOUNTS)

#### Base Case

#### ASSETS

	Dec-12	Dec-13	Dec-14	Dec-15	PDec16	PDec17
Cash & Near Cash	786	749	1,363	1,210	1,283	1,360
Accounts & Notes Receivable	145	151	146	153	160	167
Marketable Secs. & ST Investments						
Loans & Mortgages						
Real Estate Investments					0	0
Other Long-Term Investments	8,888	9,207	9,169	10,123	11,166	12,316
Long-Term Investments before Reserves	8,888	9,207	9,169	10,123	11,166	12,316
Loan Loss Reserves						
Loans Net of Reserves	8,888	9,210	9,169	10,125	11,166	12,316
Net Fixed Assets	4					
Other Assets					4,053	4,053
Additional Assets	2,854	3,252	3,618	4,053		0
Total Assets	<u>12,676</u>	<u>13,362</u>	<u>14,297</u>	<u>15,541</u>	<u>16,662</u>	<u>17,896</u>
Earning Assets	8,888	9,207	9,169	10,278	11,166	12,316

#### LIABILITIES

Demand Deposits						
Short-Term Borrowings	6,567	7,339	7,354	9,111	10,071	11,119
Customer Deposits						
Other ST Liabilities					0	0
Long-Term Borrowings	5,035	5,001	5,471	4,967	4,967	4,968
Deferred Tax Liability	54	1	9	1	1	1
Other Long-Term Liabilities	427	447	681	908	1,030	1,168
Other Liabilities						
Total Liabilities	<u>12,084</u>	<u>12,788</u>	<u>13,515</u>	<u>14,987</u>	<u>16,068</u>	<u>17,255</u>
Total Preferred Equity	58	58	205	205	205	205
Minority Interest	242	242	236	0	0	0
Share Capital & APIC	117	122	124	129	128	127
Retained Earnings & Other Equity	176	153	217	220	261	310
Total Shareholders' Equity	<u>593</u>	<u>574</u>	<u>782</u>	<u>554</u>	<u>594</u>	<u>642</u>
Total Liabilities & Equity	<u>12,676</u>	<u>13,362</u>	<u>14,297</u>	<u>15,541</u>	<u>16,662</u>	<u>17,897</u>
Shares Outstanding			11	11	11	11

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## Comments on the Difference between the Model and Assigned Rating

In this case, there has been little change in the recent results and therefore we have used our best judgement in making adjustments which are reflected in the results for the projected ratings. We have assigned a rating of "A" whereas the ratio-implied rating for the most recent period is "A-"; the median rating for the peers is significantly lower than the Company's rating.

## Changes in Industry Ratios

We have not made any adjustment in the industry ratios at this time.

**SEC Rule 17g-7(a) Disclosure**

Below are the disclosures as required by Paragraph (a) of Rule 17g-7.

**1. The symbol in the rating scale used to denote the credit rating categories and notches within categories and the identity of the obligor, security, or money market instrument as required by Paragraph (a)(1)(ii)(A) of Rule 17g-7:**

For the issuer FEDERAL AGRICULTURAL with the ticker of AGM we have assigned the senior unsecured rating of A. There are three notches in our rating categories (e.g., A-, A, and A+) other than those deep into speculative grade; for CC, C, and D there are no notches.

**2. The version of the procedure or methodology used to determine the credit rating as required by Paragraph (a)(1)(ii)(B) of Rule 17g-7:**

We are using the methodology available in our Form NRSRO Exhibit #2 dated Jun. 10, 2016 available via [egan-jones.com](http://egan-jones.com) under the tab at the bottom of the page "Methodologies".

**3. The main assumptions and principles used in constructing the procedures and methodologies used to determine the credit rating as required by Paragraph (a)(1)(ii)(C) of Rule 17g-7:**

The credit rating assigned reflects our judgement regarding the future credit quality of the issuer. Regarding the specific assumptions used, please refer to page 3 of this Rating Analysis Report.

**4. The potential limitations of the credit rating as required by Paragraph (a)(1)(ii)(D) of Rule 17g-7:**

Our rating pertains solely to our view of current and prospective credit quality. Our rating does not address pricing, liquidity, or other risks associated with holding investments in the issuer.

**5. Information on the uncertainty of the credit rating as required by Paragraph (a)(1)(ii)(E) of Rule 17g-7:**

Our rating is dependant on numerous factors including the reliability, accuracy, and quality of the data relied used in determining the credit rating. The data is sourced from publicly-available 10Q and 10K statements, quarterly reports, 8K filings, earnings reports, and other similar sources. In some cases, the information is limited because of issues such as short operating histories, the lack of reported data, a delay in reporting data, restatements, inaccurate accounting, and other issues. Such shortcomings are not always readily apparent. EJR aims to identify such shortcomings and make adjustments using its best judgement.

**6. Whether and to what extent third-party due diligence services have been used in taking the rating action as required by Paragraph (a)(1)(ii)(F) of Rule 17g-7:**

EJR does not utilize third-party due diligence services.

**7. How servicer or remittance reports were used, and with what frequency, to conduct surveillance of the credit rating as required by Paragraph (a)(1)(ii)(G) of Rule 17g-7:**

Servicer or remittance reports normally pertain to structured finance issuers; this report does not pertain to a structured finance issuer (EJR is not an NRSRO for structured finance or sovereigns/ municipal issuers). Regarding surveillance, the minimum time period for corporation issuers is normally one year.

**8. A description of the data that were relied upon for the purpose of determining the credit rating as required by Paragraph (a)(1)(ii)(H) of Rule 17g-7:**

EJR uses 10Q and 10K statements, quarterly reports, 8K filings, earnings reports, and other similar sources for ratings on publicly-traded issuers. In the case of private issuers, EJR relies on information provided mainly by issuers.

**9. A statement containing an overall assessment of the quality of information available and considered in the credit rating as required by Paragraph (a)(1)(ii)(I) of Rule 17g-7: The information is generally high quality and readily avail.****10. Information relating to conflicts of interest as required by Paragraph (a)(1)(ii)(J) of Rule 17g-7:**

This rating is unsolicited.



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### 11. An explanation or measure of the potential volatility of the credit rating as required by Paragraph (a)(1)(ii)(K) of Rule 17g-7:

Our rating aims to assess the probability of the payment of obligations in full and on-time. Factors which affect such probability, and in turn our rating, include changes in the operating performance of the issuer, changes in capital structure, and merger and acquisition events.

### 12. Information on the content of the credit rating as required by Paragraph (a)(1)(ii)(L) of Rule 17g-7:

Regarding the historical performance of the credit rating, our rating transition matrix is available in our Form NRSRO, exhibit 1. The expected probability of default and the expected loss in the event of default is listed on the first page of this report.

### 13. Information on the sensitivity of the credit rating to assumptions as required by Paragraph (a)(1)(ii)(M) of Rule 17g-7:

Below is a summary of the impact of the 5 assumptions which independently would have the greatest impact on our "ratio-implied rating":

	Assumptions			Resulting Ratio-Implied Rating		
	Base	Optimistic	Pessimistic	Base	Optimistic	Pessimistic
Interest Income Growth%	10.3	14.3	6.3	A	A	A
Interest Expense (% of outstanding debt)	1.0	(2.0)	4.0	A	BBB	BB
Provisions for Loan Losses(% of earning assets)	-	(3.0)	3.0	A	A+	BB-
Commissions & Fees Earned Growth%	(10.0)	0.1	(8.0)	A	A	A
Loan Loss Reserves (% of Earn. Assets.)	5.0	3.0	7.0	A	A	A

### 14. If the credit rating is assigned to an asset-backed security, a description of: (i) the representations, warranties, and enforcement mechanisms available to investors; and (ii) how they differ from the representations, warranties, and enforcement mechanisms in issuances of similar securities, as required by Paragraph (a)(1)(ii)(N) of Rule 17g-7:

This credit rating is not assigned to an asset-backed security.

## ATTESTATION FORM

In compliance with the US Securities and Exchange Commission (SEC) Rule 17g-7(a), the Egan-Jones analyst who published the report is responsible for the rating action and to the best knowledge of the person:

- 1) No part of the credit rating was influenced by any other business activities,
- 2) The credit rating was based solely upon the merits of the obligor, security, or money market instrument being rated, and
- 3) The credit rating was an independent evaluation of the credit risk of the obligor, security, or money market instrument.

**Analyst Signature:**

**Today's Date**

September 01, 2016

Melody Baniqued  
Rating Analyst

**Reviewer Signature:**

**Today's Date**

September 01, 2016

Caroline Ding  
Rating Analyst