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GROWING RISK

With crop prices and profits already down, farmers in the Midwest need a trade war with China as much as they need another Dust Bowl. The nation's roughly 1,800 ag lenders share their anxiety, especially since 2019 looms as a make-or-break year for so many customers.

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Seeking Savers, Not Rate Chasers

As the rates paid for deposits start to rise, digital banks experiment with new strategies to stay competitive without getting into a price war

By Kevin Wack

Online banks have long paid some of the industry's highest rates on deposits. But as the competition for consumer dollars heats up, two digital players are tweaking that strategy — in an attempt to avoid those who chase the best rates and reward loyalty instead.

Simple, which is backed by BBVA Compass, has begun to offer a 2.02% yield specifically for deposits that customers put in a "savings goal" account (once a $2,000 minimum is reached).

And CIT Bank has begun paying yields of 2.15% to customers who save at least $100 each month.

Both offers are examples of digital banks experimenting as they strive to remain competitive in a rising-rate environment without getting into a price war. The requirement that customers make regular contributions to savings in order to qualify for the higher rate figures to discourage rate chasers.

"We're not really looking for hot money," said Dickson Chu, executive chairman at Simple. The target is "consumers that actually want to save for something."

Online banks, which typically use high rates to lure consumers away from brick-and-mortar institutions, are at the forefront of the embryonic battle for deposits.

The leading online banks pay the market rate for 95% of their deposits, according to a May report from Vining Sparks. Meanwhile, the top national retail banking franchises pay the market rate for only 63% of their deposits.

As of September, online banks were paying a median of 1.78% annual percentage yield on savings accounts of at least $1,000, up from 1.18% a year earlier, according to a report from Keefe, Bruyette & Woods. By contrast, national banks were paying a median of just 0.16%, which represented a small increase from 0.13% in September 2017.

Traditionally, digital banks have lured depositors by offering attractive rates with no strings attached. And some of them still use that approach. Ally Bank, which has enjoyed annualized deposit growth of 14% over the last five years, was paying 1.90% on balances of all sizes in early October.

Other digitally oriented banks, including PurePoint Financial, a division of MUFG Union Bank, pay their best rates only to customers who maintain a large enough balance. The downside of that approach is that the money may disappear when another bank offers a higher rate.

CIT Bank is offering a 2.15% annual percentage yield to depositors who meet one of two conditions. They must either maintain a balance of at least $25,000 or make a monthly deposit of $100 or more.

The latter offer is designed to encourage customers to save on a consistent basis. "We are looking to build long-standing relationships with our customers and offer them smart savings products to meet their needs," said Ravi Kumar, head of internet banking at the Pasadena, Calif.-based CIT.

Simple, which launched as a startup in 2012 and was later acquired by BBVA Compass, has traditionally used a different value proposition than most digital players to attract deposits. Rather than paying high rates, it positioned itself as a partner in enhancing customers' financial health. Now Simple is adopting more of a hybrid approach.

Its latest offer gives customers a financial incentive to maintain bigger balances. The 2.02% annual percentage yield kicks in once the customer has set aside $2,000 for a specific savings goal.

The new offers from digital banks could prove more effective at persuading existing customers to build their existing balances than they are at luring new customers, said Hank Israel, an analyst at Novantas.

"While these types of offers have an attractive rate, they are being compared to similar rates at other online banks with no conditions," Israel said. When customers must take certain actions in order to qualify for the higher rate, they may balk, he said.

Aaron Fine, a partner at Oliver Wyman, identified another potential pitfall of requiring consistent savings behavior to qualify for the highest rate.

"The challenge with something that's goal-based is, the person is likely to spend the money when they get there," he said.

California Crackdown

New state laws impose quotas for women on boards and mandate small-business loan disclosures

Three new laws in California could have a big impact on banks and other lenders in the nation's most populous state.

The most prominent of the three requires publicly traded companies that are headquartered in California to add more women to their boards.

The other two relate directly to lending. The state imposed new disclosure requirements for certain small-business loans by nonbanks and expanded a voluntary program that aims to encourage consumer loans with borrower-friendly terms.

Under the first law, publicly traded companies with six or more directors must have at least three women by the end of 2021. Boards with five directors must include at least two women, and smaller boards must have at least one.

The measure's supporters have cited a study by Credit Suisse, which found that among companies with a market capitalization of more than $10 billion worldwide, the shares of those with female directors outperformed the shares of comparable companies with all-male boards by 26%.

Still, the landmark California law is likely to face legal challenges. Business groups have argued that corporations are governed by the laws of the state in which they are incorporated — which is often Delaware — not the laws of the state where they are headquartered.

When signing the bill on the last day of September — a Sunday — Gov. Jerry Brown said that it is "high time" that corporate boards include women, and made an apparent reference to the nation's focus on gender equity issues amid the fight over elevating Judge Brett Kavanaugh to the Supreme Court. But he also acknowledged the legal concerns raised about the bill.

"I don't minimize the potential flaws that indeed may prove fatal to its ultimate implementation," the Democratic governor wrote in his signing statement.

"Nevertheless, recent events in Washington, D.C. — and beyond — make it crystal clear that many are not getting the message."

The second bill signed by Brown instructs state government officials to develop interest rate disclosure standards for commercial loans of $500,000 or less, making California the first state in the nation to establish consumer-style disclosure rules for small-business loans.

The measure is a response to complaints that high-cost loans by online lenders often carry misleading terms and place an unsustainable

strain on the finances of small-business owners. Banks and credit unions, which generally do not offer high-cost business loans, will be exempt from the disclosure rules.

Under the third law, a broader category of loans will qualify for an existing state program that aims to provide borrower-friendly credit products.

Lenders that choose to participate in the program agree to limits on the ratio between borrowers' monthly debt service payments and their monthly incomes, for example.

That program previously applied only to unsecured loans of between $300 and $2,500, but will now be expanded to include loans of up to $7,500.

The new law was backed by, and is expected to benefit, Insikt, a San Francisco-based online lender that operates a subsidiary certified as a community development financial institution. The company hailed the measure as a win for borrowers who, it said, deserve better alternatives than they have today.

But some consumer advocates have opposed the measure. The Center for Responsible Lending had urged Brown to veto the bill, arguing that it amounts to a giveaway to a single company and would expand unsound lending practices.

Despite covering more loans, the program is still voluntary. Lenders in California that choose not to participate can still charge unlimited interest rates on consumer loans above $2,500. Loans below that amount are subject to separate interest rate restrictions in the state.

Brown, who will leave office in January following his fourth term as governor, said that he signed the bill reluctantly. He said that the interest rates allowed even in the expanded state program are unacceptably high, but he also noted that loans outside of the program are even pricier.

He invoked the Bible as he exhorted state lawmakers to enact tighter restrictions.

"From the time of Moses, usury has been condemned. Loans that exploit low-income borrowers are especially abhorrent," he wrote. — *Kevin Wack*

Busy Time In Subprime

Resurging credit card niche attracts another new player

The credit card startup Petal, which targets U.S. consumers with no credit history and those with blemishes on their borrowing records, is going national.

The broad release of the Petal Visa card comes more than a year after the New York company began testing its product.

Petal said that it has a waiting list of more than 100,000 consumers and plans to use $34 million in new financing, most of it from the investment bank Jefferies, to fund the expected surge in card balances.

Petal is the latest startup to dive into the subprime credit card market, which has experienced a resurgence after cratering in the wake of the 2008 financial crisis. The Build card from FS Card Inc., the Arrow card from LendUp and the Ollo card from Fair Square Financial are all competing for customers who do not qualify for mainstream offers.

Petal sees an opportunity to lend to consumers who have never borrowed, those whose credit histories are limited and those with low credit scores that may exaggerate the risk of lending to them.

Rather than relying on credit scores, the venture-backed startup links into its customers' bank accounts and analyzes their monthly cash flow, which it then uses to gauge their ability to manage debt. "And that's data that your traditional credit card issuer isn't looking at," Petal's chief executive, Jason Gross, said in an interview.

Petal is positioning itself as a white hat lender in a segment of the card market that traditionally has relied heavily on fee income. The company does not charge late fees — or any other fees. Of course, borrowers who fail to pay on time do incur interest charges.

"We think of it as a credit card that's a little bit less greedy," Gross said. "Our belief is that if customers succeed, we will as well."

Petal's website listed annual percentage rates between 14.49% and 26.49%, depending on the company's determination about the chances that the borrower will repay. By way of comparison, the average interest rate on cards for consumers with bad credit was 24.18% as of late September, according to CreditCards.com.

The Petal card, issued by WebBank in Salt Lake City, comes with a mobile app that allows users to schedule payments, and also shows them how much it will cost to carry a balance each month.

The startup lender has the backing of Valar Ventures, a firm co-founded by the billionaire investor Peter Thiel. Valar led Petal's $13 million Series A funding round, which was announced in January.

"I think that simple proposition of being fair and transparent is really compelling, and will be enough for them to build a really big business," Valar co-founder James Fitzgerald said in an interview. — *Kevin Wack*

Survivor Sets New Priorities

'Every day has been better than the last,' says Fifth Third shooting victim

One thing Whitney Austin remembers about that morning is noticing the spider web patterns on the glass revolving door at 38 Fountain Square. A rock had hit her car window recently and made a similar pattern, so she thought little else of it.

She noticed, too, the people in the square waving. They were trying to get her attention and stop her from walking into the building. Absorbed in a conference call on her cellphone, she paid them no mind and walked straight into the line of fire.

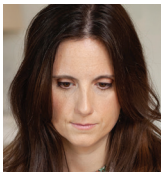
That September day, Austin became one of two surviving victims of the shooting at Fifth Third Bancorp's headquarters in downtown Cincinnati. Four others, including the gunman, died that day.

Like so many, Austin had been increasingly horrified by news of mass shootings elsewhere, but she never thought she'd be drawn into a national issue so directly.

"There's no logical explanation for why I survived and others didn't," said Austin, who was shot 12 times.

She has started a foundation that aims to reduce gun violence, even though she is still recovering. "Everybody would handle it differently, but for me, what was most natural was to fight. If you survived, you have a responsibility to move forward with your story and do everything you can to make a difference with gun violence," she said.

Austin, 37, a product manager in charge of developing unsecured digital loans, spoke to American Banker by phone from her home in Louisville, Ky., about a month after the shooting. She had just dropped her two young children off at school and settled in with the family's new kitten cuddled up next to her. The kitten is named "Al," for Al Staples, the Cincinnati police officer who helped Austin to safety after the shooter was killed in a gunfight with police.


Jaclyn Cotton

Whitney Austin

In recounting her story, Austin was matter-of-fact. Though she suffered multiple bullet wounds to her chest, Austin escaped that day with no vital organs damaged. She is working to regain the full use of her right arm and must undergo more arm surgery before she can return to work.

"It's painful to not be able to brush your teeth or feed yourself all that well," she said. "But that's a small price to pay. I was shot 12 times, and somehow I survived. I'm physically strong and I'm mentally strong, so really every day has been better than the last."

Perhaps because she never saw the shooter or the carnage while slumped at the bottom of that revolving door, she has been able to focus more on the future than on the events of that day, she said. She wants to help others, and she wants to achieve a better work-life balance.

Austin's Fifth Third family, as she's dubbed her colleagues, really turned out for her after the shooting — lifting her spirits with hospital visits, care packages and cards.

Working with the National Compassion Fund, the Fifth Third Foundation also donated $1 million to start the Cincinnati Strong Foundation to help other victims of the shooting and their families. Brian Sarver, a contractor with CBRE, was the other victim who survived. The three killed were Luis Calderon, a finance manager for the bank's commercial line of business; Richard Newcomer, a contractor with Gilbane Building Co.; and Prudhvi Raj Kandepi, a contractor with TEK Systems. Authorities had yet to determine the motive of the shooter, Omar Santa Perez.

"This has to stop — we have to find a way to stop the gun violence in this country," Chief Executive Greg Carmichael told the Cincinnati Enquirer the day after the Sept. 6 tragedy. "I don't have the answers, but we have to find a path forward."

For Austin, that path forward involves WhitneyStrong, a new charitable foundation she's formed to help other victims of gun violence and pursue bipartisan solutions to reduce gun violence in America. Austin does not have answers yet either — she doesn't believe that eradicating guns is a realistic goal — but she is looking for those answers with all the precision and thoroughness of the product manager that she is.

"I pull in data, I pull in experts, I'm very certain about what it is I'm pursuing before I publicly announce it, and that is exactly the approach that I'm taking with the WhitneyStrong Foundation," she said.

She also has put more emphasis on work-life balance. Before, she would do whatever she could to optimize her work day, sometimes starting with a to-do list of 20 or more items. When she returns to work, she will set three key priorities for herself every day.

"Anything else that gets accomplished, that's wonderful, but I'm not going to hold myself to, 'I'm going to do 20 things' because that is not realistic and it's not healthy to have that much focus on your job," she said.

"I think I will be better at work-life balance. We'll see what happens in reality." — *Laura Alix*

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'Private Banking for Everybody'

Umpqua's Tinder-like app lets customers choose their own banker based on personal details like hobbies

By Penny Crosman

Umpqua Bank has rolled out a new app that is something like Tinder for bankers, and it is making the technology available to other banks.

Customers can use the app — called Go-To — to choose a banker to work with, based on a profile that includes a photo and personal details such as hobbies. They also can ask for additional information.

"I look at Go-To as private banking for everybody," said Cort O'Haver, the Portland, Ore., bank's chief executive.

The app is a cornerstone of what Umpqua refers to as its "human-digital movement," he said. "It epitomizes what we are trying to do: use technology to better customers' lives and make banking more convenient and do all the things they need to do with a human."

Umpqua began piloting the app last year; at that time it was called BFF, a popular abbreviation for "best friends forever."

The name was changed because, research showed, it didn't resonate with the bank's target demographic: 35-to-55-year-olds with jobs and homes. Younger people liked BFF, though.

In addition to the name change, Umpqua added Android capability (the pilot only worked on iPhones) and made several upgrades to the program, with more to follow.

One of the most notable upgrades in the works is the ability for small-business owners to use the app. That is happening with the help of the fintech provider Seed.

The banking unit of the $26.5 billion-asset Umpqua Holdings asked all employees to download the Go-To app and start using it in July. The bank began marketing it to customers in September.

Go-To is now enterprise software that other banks can rent ifrom Pivotus, Umpqua's Silicon Valley software subsidiary.

O'Haver said he is open to the idea

of having artificial intelligence and machine learning injected into the Go-To app in the future to handle things like balance requests and password resets.

But he's not keen on the concept of having customers interact with the bank entirely through automated chatbots.

"The idea of technology for technology's sake because, for companies, it's a cheap way to provide customer service is not working so well," he said. "People don't really want a robot; they want a person."

The guts of Go-To

At its heart, Go-To is a secure texting environment with a dashboard bankers can use to manage their customer conversations.

The hard part, O'Haver said, is training people to be Go-To bankers.

"If you were to use this at a call center in India, I don't think it would work," he said. "We did this so customers can feel like they have a real connection with somebody in the company."

Go-To bankers are trained to know enough about most of the bank's products to answer basic questions, and to pull in a specialist, like a mortgage banker or small-business banker, to handle more difficult requests.

The bank is still testing one aspect of the original premise of BFF: that bankers in branches with slow foot traffic could handle this virtual banking work during their downtime.

"I don't want to take away from the store experience," O'Haver said. "I don't want anyone to ever walk into an Umpqua store and see someone texting as opposed to welcoming them."

So for now, most of the Go-To bankers work in a fulfillment center, though they can meet with customers at branches upon request.

The Go-To bankers can't be available 24/7 because of the one-to-one relationship. But Umpqua has found they don't have to be. When customers pick a banker and know that person works 9:00 to 6:00, they respect that, O'Haver said. "Someday we may have pods of three" to accommodate off-hours requests, O'Haver said. "But we've found that people are willing to wait until the next day."

Bringing in small businesses

Small-business owners have a greater need for something like Go-To, O'Haver said. "They're working long, tough hours, and they know banks don't usually dedicate people to their relationship," he said.

Seed will soon provide small-business account onboarding within the Go-To app. Eventually there may be a whole suite of small-business banking tools in Go-To.

"I'll call it Treasury management-lite. It's a pretty powerful small-business tool, and we can do it anywhere in the country," O'Haver said.

In addition to laying the groundwork to support small businesses, the bank helped the Go-To bankers develop their profiles to include the right amount of personal and professional detail.

"We found that was a way to help people connect based on a shared interest or experience," said Eve Callahan, executive vice president at Umpqua.

Eventually, Go-To could serve much larger commercial clients.

"How can technology make the CFO of a company more efficient, provide better information to the CEO and board, and provide a better solution?" O'Haver mused. "We have ideas about how to use it for commercial clients."

New Way to Car Shop — From a Bank

USAA road-testing augmented reality app for car buyers

If USAA's pilot app works as intended, it's going to get a lot easier for its customers to shop for a car.

By using the app, customers can point their phone at a vehicle and get an augmented reality overlay that provides information such as the make, model and year, along with the price range and quotes for insurance and a loan to purchase it.

The app is designed to save customers time and embed USAA into the car-buying process.

"People's attention spans are so short right now," said Patrick Kelly, assistant vice president of digital product development at USAA. "Giving them all the information at the right moment to make a decision takes a lot of workload out of the process."

USAA began letting 1,000 of its employees and customers use the app in late September, with plans for roughly one month of testing.

If the idea sounds familiar, it should.

Capital One announced in March it was working on an augmented reality experience for car buying.

The service, which it intends to make available through the Capital One Mobile app in the next few months, will let users scan cars via their mobile phones to view information related to each vehicle. The company has been testing the functionality since previewing it at the SXSW Interactive Festival.

USAA itself also launched a car-buying app in 2010 called Auto Circle.

What's new here is the augmented reality element, which, according to Kelly, greatly simplifies the overall

experience. "If you were going to shop for a car on any car-shopping website — CarMax, Autotrader — you would have to physically input all the information about the car yourself: new, used, what year, what make and model, what features," Kelly said. "This takes all that data entry out of the picture. All you have to do is point it toward the car you like, we'll take care of the lookup, and we will grab information about that car."

How it works

The app contains computer vision software from Blippar that uses artificial intelligence to recognize the car shape and logo and pair that with a manufacturer's database.

The software's accuracy rate at identifying a make, model and year range is close to 100%, Kelly said. (It's hard to know the exact year without looking at the inside of the car, he said; auto manufacturers usually keep a similar body style for four or five years before making a change.)

The app will list vehicles in the area for sale that match the make, model and description.

"When you select one of those cars exactly, then that exact content goes back into the engine to give you a more accurate quote," Kelly said.

USAA hasn't decided yet whether the car-buying app should be standalone or built into USAA's mobile banking app. Currently, it's a separate app, so it can be tested without affecting the banking app.

In the future, USAA will consider adding affordability widgets that will help the customer make a decision faster.

Brad Leimer, former head of innovation at Santander and co-founder of the consulting firm Unconventional Ventures, said he's used an app called TrueCar that combines car shopping and auto loans. But adding insurance is a step further. "It's important to make things more convenient, because nobody wants to spend time in a dealership," Leimer said. "You're embedding convenience into an existing experience and enhancing that through the technology."

It is the kind of effort banks need to make to stay relevant in the face of online lender and fintech competition, he said.

"We need to be changing the way we are looking at building experiences around typical consumer needs: buying a car, buying a home, and making it more convenient for the customer to make these large purchases and credit decisions with as much information as possible," Leimer said.

"The smartest institutions are experimenting with and looking at this idea of how augmented experiences, throwing data on top of reality, will help people."

Moving fast

A small team of developers at USAA — the people who built its Auto Experience (the most recent iteration of what used to be Auto Circle) — created a prototype of the new app within about three weeks. They then spent two months refining and testing it for production. Kelly wouldn't say what this cost or when any return might come.

"That's part of what the pilot is for — to evaluate what the market would be," Kelly said.

USAA hopes its app will help bring in new customers and appeal to its several hundred thousand existing customers who buy a new car every year.

Those who wanted to participate in the pilot could sign up on USAA's innovation website, usaalabs.com. USAA said testing would end Nov. 1, after which it would analyze the results and incorporate feedback from participants into the app.

The way USAA does product development lends itself to such short pilots. "It used to be we would go out and do ethnographic research, a qualitative study and quantitative study, then do a conjoint analysis to make sure all the features are right before we ever get to the point of launching a product," Kelly said. "And we would make sure there was no risk."

Technology now turns on a short cycle so such a rigorous approach to product development doesn't let a company keep up with the market, he said. "We have to find a lighter weight, faster way to get out there and see if there's even demand for these types of new interfaces," Kelly said. "That whole market research phase is expensive and lengthy. I can let the pilot do the hypothesis testing for me instead of doing hypothesis testing in a lab. It's much faster to market this way."

— Penny Crosman

Ag Loans in An Instant

Online lending for farmers is a new frontier

Online lending so far has been focused on consumers and small businesses seeking simple applications and quick approvals.

But Bremer Bank in St. Paul, Minn., sees opportunity in a new niche.

The bank has signed a contract to use Numerated Growth Technology's online lending software to make fast, automated loans to farmers. Numerated built the new agricultural loan software in collaboration with the $12 billion-asset Bremer, the 11th-largest ag lender in the country.

"We see this as a gap in the market," said Dan Flaningan, strategy director at Bremer Bank. As someone running an ag business, a farmer is essentially a business owner, he added.

Bremer's ag customers tend to have smaller family-owned farms. Farmers who are out in the fields during the day have limited time to go to a bank branch. "Our ag clients are the ones that are more digitally savvy," Flaningan said. "They're more apt to use mobile deposit functionality, because obviously time is important to them. Making a potentially big commitment to drive into town to a branch to deposit a check is not advantageous to them as a business owner."

The bank plans to test the new software during the fourth quarter and launch it next year.

Flaningan declined to discuss details about the software, such as what new types of data are being pulled in to underwrite the ag loans.

Numerated is the tech spinoff from Eastern Bank that's run by Dan O'Malley, who had been Eastern's chief digital officer.

"I think this speaks to how quickly digital and online lending is spreading to be able to do it in such a conservative category as ag lending. But at heart the engine is the same," said O'Malley, who, like Flaningan, declined to go into specifics.

O'Malley said banks that just offer an online loan application rarely increase their loan volume. "We learned that at Eastern — if all you do is put up an online application, you will not do more loans," he said. "You have to transform how your employees and your marketing are talking about the bank and selling loans if you want to make money and grow."

The Numerated software prequalifies all the prospects in a bank's footprint. When a local businessperson calls, a banker can tell them they're eligible for a type of loan and what the terms would be. "The banker is not required to go through credit training in taking the application; they can be not credit-trained and still be able to sell loans because the system is doing the credit work for them," O'Malley said.

The software makes loan decisions within about 45 seconds, he said.

— Penny Crosman

GROWING RISK

With crop prices and profits already down, farmers in the Midwest need a trade war with China as much as they need another Dust Bowl. The nation's roughly 1,800 ag lenders share their anxiety, especially since 2019 looms as a make-or-break year for many customers.

BY JOHN ENGEN

It's a stormy late-September afternoon in northern Iowa — a common occurrence in this year of discontent for many of America's farmers. Just outside of Fort Dodge, a bustling regional farm town of 25,000, wind and rain pound against the corrugated-metal roof of Dan Thompson's oversized garage as he explains the latest challenges managing his 1,700-acre corn-and-soybean farm.

It's rained more than 30 inches since his crops went in last spring, about double normal levels. The harvest began a day earlier, and early indications aren't good. "We're saturated. Close to 10% of our acres are flooded out, where we have nothing left," Thompson said. "But you can't control the weather."

Consider it an apt metaphor for the state of farming in an era of overproduction and tariffs. Storm clouds have been gathering over America's heartland for much of this decade, with falling crop prices and profitability, and rising debt levels, leaving farmers in increasingly precarious financial positions.

Worse, while farmers can tinker with their own production (subject to the weather), they are powerless to control the broader market forces that influence what they get paid.

Per-bushel prices for corn and soybeans, staple crops across the farm belt, have fallen by roughly half over the last six years. The latest wild card — a budding, potentially nasty trade war with China, the world's biggest consumer of soybeans — has sparked another price drop and made things uncomfortable.

"Locally, we're staring at a net-loss year. We're going to have worked all year and not made any money doing it. And we don't know what to expect next year," said Thompson, sitting at a table in the shadow of his 15-foot-high combine with soft country music competing with the rain in the background. "People are living on equity. You can only do that so long before you're done."

Many of the nation's 1,800-some ag lenders, their fates tied to those of their farmer clients, are feeling similar angst. Chinese tariffs on soybeans, wheat and other commodities have knocked prices down as much as 20%, adding a layer of uncertainty to planning for the 2019 planting season that promises to test the effectiveness of risk-management practices at these banks.

"When times are good, it's easy to be a lender," said John Taets, Thompson's banker and regional president for the $1.5 billion-asset Northwest Bank's ag-heavy Fort Dodge branch. "When times get a little more challenging, you find out who's prepared for the long haul."

Even before the trade skirmish, some banks had been quietly scaling back their lending commitments to farmers, counseling them to reduce expenses. Some ag loans have been restructured three or four times, and equity for collateral, once plentiful, is running low. Rising interest rates make extending the terms of loans less attractive.

"Banks have been taking a much more defensive approach to ag lending," said John Blanchfield, owner of Agricultural Banking Advisory Services in Damascus, Md.

That includes underwriting loans based on cash flows more than collateral values, moving risk off their balance sheets by selling loans into secondary markets through Farmer Mac, and stress-testing individual loans and portfolios to stay ahead of trouble.

Surveys indicate that a growing number of loan applications from farmers are being outright rejected. Expect to see more in the months ahead.

"As conditions grow more uncertain, I think we're going to see some pain come out of this — a transition from a very easy credit environment to a tight environment where it's tough for anyone to get a loan," Blanchfield said.

"There are banks out there that will experience problems," he added. "What we don't know is how bad things will get."

The numbers around farm banking belie the notion that trouble could be on the horizon. In 2017, 96% of ag banks made money, though the group's total net income declined by 3.1%, to $4.7 billion, according to the American Bankers Association.

Loan delinquencies and charge-offs remain near all-time lows, and capital levels have more than doubled over the past decade, implying that banks are positioned to handle some turbulence. "Most of the banks have been doing relatively well," said Nathan Kauffman, an economist with the Federal Reserve.

Even so, signs of stress are showing. In 2011 and 2012, while the rest of the economy was in recession, the farm economy exploded. Crop prices soared to record levels — corn briefly touched $7.50 per bushel, while soybeans neared $18.

Equipment dealers and Main Street businesses thrived, and more than a few farmers spent some of their winters in the Caribbean. They also built up equity as farmland values climbed to new heights. Banks did well.

Since then, prices have been edging downward. Even before the tariffs, corn was going for under $4 per bushel, with soybeans in the $10 range.

Most other metrics have been moving in the wrong direction. Net farm incomes dropped more or less steadily from $124 billion in 2013 to $75 billion last year, according to the U.S. Department of Agriculture. Farm debt has increased $132 billion in the last decade, to $407 billion, while the financial assets of these borrowers — investments and bank deposits, for example — have fallen by $62 billion.

Loan quality, while still solid in most places, isn't quite as pristine as it was several years back. Foreclosures and farm bankruptcies are ticking up. Some agricultural producers are in year three of losses, bankers confide, and likely won't be able to hold on much longer.

The total of outstanding farm loans at banks rose 5.9% in 2017, to $106 billion, according to the ABA. But in a troubling sign, most of those were farmland loans, which jumped 7.7%.

"Farm real estate debt has increased significantly, but it's not because farmers are buying real estate," Blanchfield said. "It's because banks are refinancing unpaid carryover debt into long-term debt. Some customers are on their third or fourth time. There isn't much equity left."

In some ways, farmers are victims of their own success. They've evened out their revenue the only way they can: using genetically modified seeds and other technology (and some luck with the weather) to squeeze more bushels out of an acre. (Per-acre corn yields

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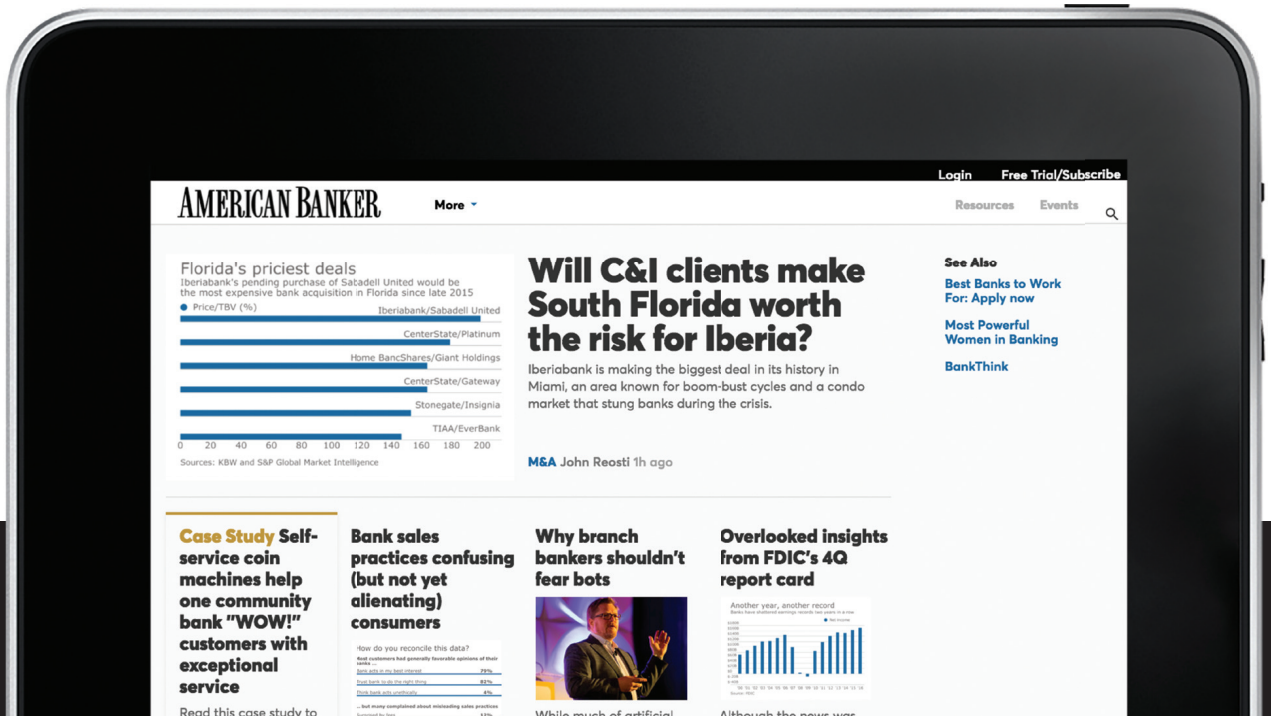


have risen from 80 bushels to 180 in the last three decades, and are closer to 200 in Iowa.)

Boosting production might solve the individual farmer's short-term problems, "but when everybody has more yield it creates more supply, which drives down prices and exacerbates the problem," explained Jayme Ungs, an Iowa-based ag team lead for U.S. Bank.

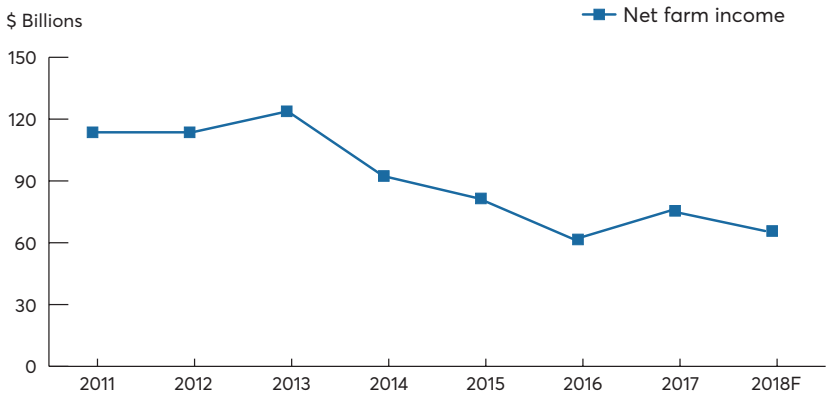
Presently, silos and bins across the Midwest are stuffed full of grain, waiting for a rebound in prices — and adding to the surpluses. "If we can't increase demand, we're stuck," Ungs said.

Some fear the table is being set for a replay of the devastating 1980s farm crisis, when overproduction, a global recession and high interest rates led to a drop in exports. Prices and farmland values imploded, and hundreds of ag banks failed.

The title of a session at last March's Kansas Ag Bankers conference reflected the concern: "How is this farm crisis different from the '80s and what lies ahead?"

For now, the biggest differences are lower interest rates and debt-to-asset ratios among farmers, and higher land values, said Allen Featherstone, a Kansas State economist who spoke at the session. "It's not a crisis yet, but there is definitely the potential for a crisis," he said in an interview.

What farmers earn



Note: F=forecast.
Source: USDA, Economic Research Service, Farm Income and Wealth Statistics
Data as of Aug. 30, 2018

To stave off trouble, bankers have been more proactive about communicating with their customers, helping plan family budgets and reviewing farm strategies. They are also counseling farmers not to make commitments that can't be met.

The tariff situation makes those conversations more complicated. Farmers live at the intersection of yield and price, supply and demand, and 50% of the U.S. soybean crop is exported — most of it to China, which accounted for about $12 billion in soybean exports last year.

When Beijing retaliated against tariffs on Chinese products with targeted tariffs of its own on U.S. soybeans, pork and other farm products, it had the effect of removing demand, sparking an abrupt 20% drop in prices for U.S. soybeans.

"Agriculture is usually the first casualty of any trade war, and this is no different," said Ernie Goss, an economist at Creighton University in Omaha, Neb.

This is Trump country, and farmers are guardedly supportive of the tariffs — provided they aren't in place for long. Many had bumper crops this year and locked in pricing on portions of their crops in the spring. They should be able to survive 2018 in good stead.

The big concern is 2019. As this fall's harvest wraps up, farmers and their bankers are having their annual face-to-face discussions about the next year's crop.

Most farmers need to buy their seeds, fertilizer and other inputs by the end of the year for tax and logistical reasons; bankers use the time to renew lines of credit, help with budgeting and get a general read on the health of the operation.

The goal is to determine a break-even price on whichever crop will be planted, based on the costs, and then see how profitable it might be. Ideally, they formulate a marketing plan that includes some forward sales in the spring.

A little informed guesswork typically goes into the process, rooted in price and yield forecasts from universities and the Chicago Board of Trade, but in this environment no one knows for sure what will happen.

Some analysts predict a protracted standoff. If that happens, will the government add to the $12 billion in emergency aid it is providing this year to affected farmers?

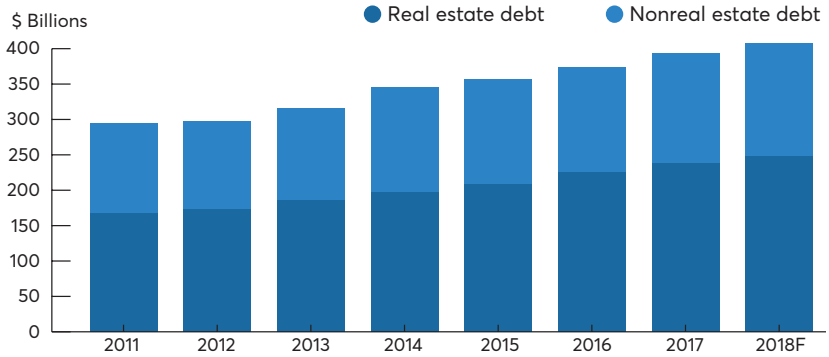
Others say China is so reliant on soybean imports to feed its population that it could buckle. "The farmers will make a fortune when this is over," Trump tweeted in September.

A new trade agreement with Mexico and Canada in September was greeted as a good sign in farm country.

But complicating matters further: A bill that will make changes to farm subsidies, crop insurance and other government payments, slated for approval by September, remained stuck in conference committee as of mid-October.

Throw it all together, and a sense of deer-in-the-headlights paralysis has spread through farm country. Farmers like Thompson don't know what to plant and are delaying their decisions as long as possible. Bankers have little visibility on cash flows and little basis for approving loans.

What farmers owe



Note: F=forecast. Dollar amounts adjusted for inflation.
Source: USDA, Economic Research Service, Farm Income and Wealth Statistics
Data as of Aug. 30, 2018

The tariffs "have put a cloud over everything," said Shan Hanes, chief executive of the $90 million-asset Heartland Tri-State Bank in Elkhart, Kan., and chairman of the American Bankers Association's Agricultural and Rural Bankers Committee.

Hanes said 75% of his bank's loan portfolio is direct ag, with the rest ag-related. His clients have survived recent low prices thanks to two consecutive years of perfect growing conditions and high yields.

"The challenge is that you can't really put together a cash flow for next year," Hanes said. "You can't count on double production again. You don't know about government payments. And you don't know about the tariffs.

"You need to be able to defend those loans to the examiners, and without firm numbers, they say you have to operate like it's zero," he said. "There are too many unknowns right now. That's not good for the farmers or the banks."

The anxiety being felt in the Midwest doesn't necessarily extend to all parts of the country. Kent Steinwert, CEO of F&M Bank, a $3.5 billion-asset ag bank in Lodi, Calif., said his bank's farm clients in the central valley are suffering few ill effects from recent sluggish pricing or the threat of tariffs.

"We have virtually no problems in our portfolio today. Our clients are profitable," he said.

"There could be some short-term pain in the large crops like corn and soybean, but in the long-term the U.S. will be better positioned to export something as simple as broccoli or avocados," Steinwert added.

What's the same most everywhere is the ag bank business model, which appeals for its setting, simplicity and the strong bonds it elicits. The institutions average around $100 million in assets, and some are much smaller.

The relationships are often intimate, which allows for meaningful conversations, but also makes delivering bad news more difficult. Everywhere, it seems, the ag bank is central to the community's life.

At the Bank of Newman Grove in Nebraska, farmers regularly stop in to check the latest crop prices posted by the teller window. An old rain gauge on the one-story building's roof feeds into a handmade vial and is considered the bible for local measurements.

"You can go on the internet, but people still want to know what the bank got" for rainfall, said Jeffrey Gerhart, the $30 million-asset bank's owner and CEO.

To Gerhart, a fourth-generation banker who learned the business around the family dinner table, the definition of ag banking is simple: "If you're my farm customer and you do well, I do well. If you get into trouble, I get into trouble," he said. "And if enough of my clients get into trouble, I'm in big trouble."

The aw-shucks facade and blue jeans attire mask the complexities of a business dominated by variables beyond anyone's control.

Ag bankers serve as community leaders, the rudder to help farmers through patches of tight liquidity, financial advisers and business mentors,
and even informal marriage counselors. Many host conferences with

outside speakers to build relationships and educate their clients.

They must know the value of the dollar, the nuances of crop insurance and other government programs, tax laws, growing conditions in other parts of the world and anything else that affects farm profitability.

Surprises occur frequently. This summer, for example, Chinese tariffs on hogs dropped prices to 28 cents per pound from 55 cents, causing widespread alarm. Then a deadly African swine fever epidemic began sweeping the globe, and prices rebounded to 45 cents.

"Sometimes the unknowns can work in your favor," said Jim Myhra, a Fargo, N.D.-based director of farm and ranch management for U.S. Bank. "The banker has to be on top of that."

Communication is crucial. Hanes makes a point to schedule loan renewal meetings for weekends or nights, when he can meet with the entire family around the kitchen table to discuss the family finances. "One of our most critical roles is making sure the husband and wife are on the same page," he said. "When prices dip, divorces go up."

Thompson, the farmer, frequently calls Taets to bounce around ideas. "I have no problem calling John and saying, 'Hey, I'm thinking about doing this. What do you think?' " Thompson said. The topics range from money management to equipment purchases or even farming strategies.

"He sees things that are working, or not working, for other growers, and helps me decide what to do," Thompson said.

The nature of the business means that ag bankers must constantly walk a tightrope between wanting to help their customers, oftentimes friends from church or other local organizations, and doing what's right to protect the bank and satisfy regulators.

In harder times, "you find out who's prepared for the long haul," says John Taets of Northwest Bank in Iowa.

Lender liability is another concern. Farmers sometimes want to be told what to do, but giving direct advice can open the bank to legal action if it turns out to be wrong. Better, they say, to refer back to budgets and let farmers make their own decisions.

"The ag banker is a highly revered counselor to many farmers, but they don't want to even appear to be offering management advice," Blanchfield said.

Those heart-to-hearts have been getting more strained as commodity prices have declined, and the tariffs have introduced a new level of uncertainty that will add to the unease if things aren't settled.

Taets sent early renewal forms to his ag clients in October. Around Thanksgiving time, he or one of his bankers will visit each client's home to plot a budget and game plan for next year.

"We'll go through last year's production, their capital needs and financial information to figure out profitability. If they're having challenges, do we need to restructure? What do we need to do to make sure their operation is viable?" Taets explained.

Tough love is the order of the day. Ungs said his team has been doing more "sensitivity analyses" with farm clients, shocking their cash-flow projections to get everyone on the same page and help tweak expenses and crop-insurance levels.

"Smart bankers are challenging their customers to think more about profitability. 'Here's where you think you'll be for the year, but what if yields are down this much or prices fall below a certain level?' " he said.

"The tariff situation is a wild card, because we have no control over it," Ungs added. "It could last longer than people think, so we have to make some assumptions around it and plan for the worst."

The worst-case scenario looks something like this: A prolonged trade war leads to further price declines. More land owners — 30% of farmland is owned by nonoperators, such as local professionals or private-equity firms, which rent it to farmers as an investment — exit, causing land values to decline further.

Farmers need more working capital from banks to make up for the pricing shortfall, but lack the collateral lenders need to satisfy regulators because of falling land values.

Some might borrow from elsewhere — say, the captive finance arms of equipment makers, which could get them into more trouble. Others fail or are forced to sell, perpetuating the cycle.

"The real concern is liquidity," the Fed's Kauffman said. "To what extent do the reductions in working capital translate into bigger problems for banks?"

Even if the trade war is settled quickly, the long-term forecast for the heartland looks stormy. Bankers should keep their umbrellas ready. ◻

Stay? Give Us a Reason

By Cate Luzio

I made the tough and risky decision to leave financial services about eight months ago. During my 20-year career, I led various women's groups and diversity initiatives, regionally and globally. We talked about hiring more senior women, promoting more women into senior roles, and having parity in leadership. Yet, after all this time, not much has changed.

Management is trained to focus on numbers, but numbers can be misleading. If you only have a few senior women at the top, their promotion or transition can significantly impact the overall diversity profile. And, if a senior woman leaves, it can have a devastating effect on representation. We see the same thing happening with female CEOs at Fortune 500 companies — there are so few and everyone notices when one leaves.

Women leave for many reasons, but young women look up and either see too few people like them in senior roles or, worse, too few opportunities. In my view, if you can't see it, you can't be it.

So the infamous leaky pipeline keeps leaking. You can't miss the obvious absence of women across all levels in banking. If we don't push for hiring more, we will never reach gender parity. We won't see any change at the top unless we make progress throughout.

Banks need to cast the net wide when recruiting, both internally and externally. Instead, they rely heavily on spearfishing, and we see the same senior women being poached from one bank to another (just take a look at the Most Powerful Women in Banking list).

Management should start by rethinking its behavior and look for talent within the organization to groom for bigger roles. To retain more women, develop them.

Look outside of banking too. There are women across industries with skills that can be adapted. I was not a banker or even in finance when I joined the industry. Yet someone (yes, a man) saw a different kind of talent in me and wanted to invest in — and, of course, capitalize on — that. Why isn't this happening more? It takes time and money, resources and effort. That's much harder than spearfishing.

All of this has a staggering effect. Lack of investment in the female pipeline equals no bench strength and ends up perpetuating the diversity problem at a very real cost to banks.

But before you invest in your existing pipeline, you need to build it. One of the bigger issues is attracting talent into the organization. As banks recruit, they look for certain qualities and skill sets and target mostly the same schools. Because there is a formula, there is little thinking outside the box. I'd argue for expanding the selection of schools and majors. Think international relations or forensic science.

Leveraging some of the top talent from various lines of business into human resources — those who truly understand how these businesses work — would help. It might seem basic, but it's not happening to a wide degree.

Banks also need to create an environment that women want to be a part of, that they find inspiring and that allows them to envision a career path. Setting expectations early and investing in development programs is critical. If women don't see a path, or don't believe that the leadership team is invested, they won't want to join that bank, especially if it entails leaving another industry to make that jump.

Spearfishing is just one way that companies lose people, but women also exit because it is an environment that becomes easy to say goodbye to. After two decades, I left to start my own company, ironically focused on moving more women into the pipeline across all industries, not just banking. It wasn't that I didn't love what I did, I just couldn't "walk the talk" anymore when I didn't see much changing. I got a seat at the table, but I realized once I got there that the table still had too few women. When you get to a certain level, and you are confident in yourself and your work and know what you want, putting up with the undermining office politics and lack of support starts to feel like a toxic situation. We are less likely to stick around because we have other things that matter to us.

It shouldn't have to be like that. We need a bottom-up and top-down approach. Until we focus on growing the pipeline, the needle will continue to be hard to move. □

Cate Luzio is the founder and CEO of Luminary and a repeat honoree in our Most Powerful Women rankings.

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BLOOMBERG NEWS

JAMIE DIMON

"And by the way, this wealthy New Yorker actually earned his money. It wasn't a gift from daddy."

JPMorgan Chase chairman and CEO, making a series of digs at President Trump, only to later express regret and insist he will not run for office

TYLER DICKSON

"It's better to do the right thing a bit slow than the wrong thing too soon."

Co-head of Citigroup's new Banking, Capital Markets and Advisory division, on his company combining those groups long after competitors did so

BRAD MILLER

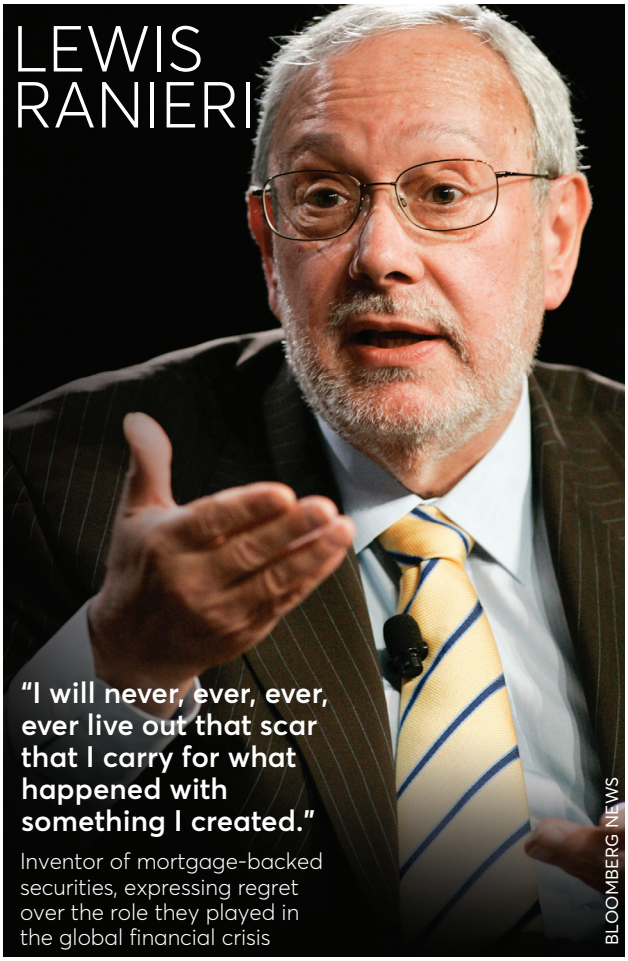
"Some folks that softened Congress' crackdown on Wall Street shortly after went to work for the companies that benefited from the softening."

Former U.S. representative from North Carolina, on the revolving door between Congress and Wall Street

ERIC BLANKENSTEIN

"Do I regret some of the things I wrote when I was 25? Absolutely. The tone and framing of my statements reflected poor judgment."

CFPB's fair-lending enforcement officer, disavowing blogs he wrote in 2004 that called most hate crimes hoaxes and questioned if use of the N-word is racist



LEWIS RANIERI

"I will never, ever, ever, ever live out that scar that I carry for what happened with something I created."

Inventor of mortgage-backed securities, expressing regret over the role they played in the global financial crisis

BLOOMBERG NEWS

ELIZABETH WARREN

"Oh yeah. Give me a chance."

U.S. senator for Massachusetts, saying she still wants to break up the big banks

PAULINA GONZALEZ

"To be faced with this question in order to do banking seems as un-American as you can get."

California Reinvestment Coalition's executive director, on Bank of America asking customers to prove citizenship

IAN BYRNE

"Saying sorry is one thing. But scandals are only over when customers say they are over."

Social media analyst, on the public's reluctance to forgive Wells Fargo

CHARLES RANDELL

"Be warned."

Chairman of the U.K.'s Financial Conduct Authority, threatening to fine accountants over lax auditing of financial companies

PRESIDENT TRUMP

"The problem with banker Jamie Dimon running for President is that he doesn't have the aptitude or 'smarts' & is a poor public speaker & nervous mess — otherwise he is wonderful. I've made a lot of bankers, and others, look much smarter than they are with my great economic policy!"

In a tweet after Dimon said he was "smarter" than the president and could beat him in an election

BLOOMBERG NEWS