S&P Global Ratings

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Compeer Financial ACA

Primary Credit Analyst:
Lidia Parfeniuk, Toronto + 1 (416) 507 2517; lidia.parfeniuk@spglobal.com

Secondary Contact:
John Orsatti, New York; john.orsatti@spglobal.com

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Compeer Financial ACA

SACP: bbb+			Support: 0		Additional factors: 0
Anchor	bbb+		ALAC support	0	Issuer credit rating
Business position	Moderate	-1	GRE support	0	BBB+/Stable/--
Capital and earnings	Strong	+1	Group support	0	
Risk position	Adequate	0	Sovereign support	0	
Funding	Adequate	0			
Liquidity	Adequate				
CRA adjustment		0			

ALAC--Additional loss-absorbing capacity. CRA--Comparable ratings analysis. GRE--Government-related entity.

Credit Highlights

Issuer Credit Rating
BBB+/Stable/--

Overview

Key strengths	Key risks
Strong risk-adjusted capital ratio	Concentrated lending to agricultural sector, given its charter
Access to favorably priced funding through AgriBank	Somewhat limited geography, although nationwide footprint continues to expand
Historically, strong credit risk management	Exposure to cyclical commodity prices and unpredictable agricultural conditions

Compeer Financial ACA's capital ratios have fallen, but we expect its S&P Global Ratings risk-adjusted capital ratio will remain in the range we consider strong. In 2023, the association's risk-weighted assets (RWAs) rose on strong loan growth and an increase in its investment in AgriBank FCB. It also built less equity than in the previous year as earnings fell slightly on higher provisions for loan losses. As a result, its S&P Global Ratings risk-adjusted capital (RAC) ratio declined to 13.4% at year-end 2023 from 14.7% a year earlier, while its Common Equity Tier 1 (CET1) regulatory capital ratio fell to 12.6% from 13.2%. We expect the RAC and regulatory capital ratios will decrease modestly further in 2024 to reflect still-relatively strong loan growth. We project that in 2024, the RAC ratio will be 12.6%-13.0%, still in the middle of the 10%-15% range we consider strong.

The rise in net charge-offs Compeer reported in 2023--compared with 0 in 2021 and 2022--does not foreshadow a material weakening in asset quality. Compeer's net charge-offs (NCOs) rose to 26 basis points (bps) from zero in 2022, but that still compares favorably with most U.S. regional banks. We do not believe the rise is indicative of broad-based weakness in the loan portfolio but, rather, isolated to a small number of loans. We do not expect a further increase in NCOs in 2024.

As an agricultural credit association (ACA), Compeer is concentrated in agriculture, but continues to add geographic diversity through its Agri-Access and Capital Markets Group (CMG) programs. Compeer has a designated lending territory throughout 144 counties in Illinois, Minnesota, and Wisconsin and is chartered to serve agricultural producers and processors, rural borrowers, and related agribusinesses. That leaves it with higher industry concentration risk than most regional banks have. However, with about 40% of its loan portfolio outside this region, up from about 35% in 2017, geographic diversification has improved somewhat. It also has diversified the types of agricultural businesses it lends to, in part through its Agri-Access program and Capital Markets business. In those businesses, Compeer purchases participations and partners in primarily syndicated loan transactions. It also earns fees in those businesses.

Compeer will continue to benefit from its relationship with AgriBank, which allows it to readily access funding. As the company is a farm credit association, Compeer's primary funding source is its line of credit with its Farm Credit System (FCS) bank, AgriBank. Compeer is able to match-fund its loans for the most part with low-cost borrowings, which primarily neutralize interest rate risk and maintain a relatively stable net interest margin (NIM). As a nondepository institution, Compeer does not face the risk of deposit flight and higher deposit costs. Although we view on-balance-sheet liquidity as slim, we do not expect Compeer will lose access to its AgriBank funding.

Outlook

The stable outlook indicates S&P Global Ratings' expectation that Compeer will continue to generate good earnings with manageable asset quality metrics over at least the next two years. Although we expect capital measures will weaken, we expect Compeer will maintain an S&P Global Ratings RAC ratio comfortably in our strong range of 10%-15%.

Downside scenario

We could lower the ratings on Compeer if we expect it to pursue:

- Aggressive loan growth that could put meaningful pressure on current capital ratios, or
- Growth resulting from loosening underwriting standards that leads to weaker credit performance.

Upside scenario

We could raise the ratings if the association unexpectedly boosts its capital ratios and we expect its S&P Global Ratings RAC ratio to rise above 15% and remain there on a sustainable basis. An upgrade would also be contingent on maintenance of good asset quality and earnings.

Anchor: We Lift Our Anchor For Farm Credit Associations In Line With The Anchor For U.S. Banks

Our starting point--or anchor--for our rating on Compeer is 'bb+', in line with that for other U.S. companies that we rate under our nonbank financial institutions criteria. Because of Compeer's public policy role, access to government-related entity 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 (FCA's) regulatory oversight, the company's favorable funding through its position in the FCS, and its strong competitive position.

Peers include AgTexas Farm Credit Services, American AgCredit ACA, Capital Farm Credit ACA, CoBank ACB, and AgriBank. Ratios and figures are as of year-end 2023, unless otherwise specified.

Business Position: Geographic And Industry Lending Concentration

Our assessment of Compeer's business position reflects the association's good market position in three states as an agricultural lender within the FCS and solid track record. We balance those strengths against Compeer's concentration in agricultural lending, with large exposures to cash grains, farm real estate, dairy, and swine.

Compeer is structured as a cooperative, owned by the client stockholders to whom it provides loans and other services with almost $32.0 billion in assets, including $28.3 billion in loans at year-end 2023. The association operates its retail operations through over 35 office locations, serving 144 counties in Illinois, Minnesota, and Wisconsin. Lending to a number of less-correlated agricultural sectors helps mitigate its agricultural concentration.

Approximately 40% of Compeer's loan portfolio is outside of its designated territory. Through loan syndications, CMG focuses on generating revenue and loan volume, including for Compeer. In addition, Compeer provides correspondent lending programs with financial institutions that are dispersed throughout the U.S. under the trade name Agri-Access, primarily focused on purchasing participations in agricultural real estate loans and leases. It also services loan portfolios for other institutional investors. This provides portfolio diversification, helps reduce concentration risk, and provides growth. We expect CMG and Agri-Access will continue to fuel growth outside of the designated territory.

Compeer's net interest income (NII) typically makes up about 70% of revenues, with noninterest income, like patronage income and other fee income, providing good revenue diversification. That split compares favorably with the approximately 78%-22% split between NII and noninterest income that we see for peers at the median. We expect overall revenue growth to moderate to the mid-single-digit level and perhaps slightly higher in 2024, compared with about 14% in 2023. Farm income peaked in 2021 and 2022 and then fell somewhat in 2023. Elevated costs and high rates have been a hurdle for farm income, which we expect will drop further in 2024.

U.S. Department of Agriculture grain carry-over inventory has risen. Solid grain production in 2023 coupled with a dip in export volumes led to a price drop as inventory rose and affected profitability. This trend has continued in 2024. On a positive note, Compeer's grain portfolio is geographically diversified, helping lower the risk of weather unpredictability.

Farmers are still in a relatively strong financial position. Most have sufficient equity to provide flexibility to cope with weather and trade pressures. Although farm land tends to be the greatest fixed asset of most grain farm operations and tied to interest rates, we do not view it as a major area of risk because of Compeer's strong first-lien positions and low loan to values (LTV) lending.

Capital And Earnings: S&P Global Ratings RAC Ratio Has Fallen But Should Remain Comfortably Within The Strong Category

Compeer's CET1 ratio fell to 12.6% in 2023 from 13.2% at year-end 2022 while its S&P Global Ratings RAC ratio fell to 13.4% from 14.7%. The drop in capital ratios primarily reflected an increase in Compeer's investment in AgriBank and high loan growth, resulting in higher RWAs. It also reflected less of an increase in equity in 2023 compared with 2022, as earnings fell on higher provisions. We expect the 2024 RAC ratio will decrease to 12.6%-13.0% due to still-relatively high loan growth but will remain comfortably within our strong range of 10%-15%.

Compeer is required to invest in AgriBank's capital stock as a condition of borrowing. The investment requirement increased to 3% from 2.55% in 2022, resulting in higher RWAs.

Quality of capital is strong, with the association's adjusted common equity to total adjusted capital at 98% versus the peer average of 91%.

Compeer's 39% expense ratio (by our calculation) is materially more favorable than the U.S. regional banks' median, given the association does not need to maintain a branch network. Profitability, measured by core earnings to operating revenue, at almost 46% is very strong compared with that of most U.S. regional banks, though not as strong as the peer average of almost 59%. We expect profitability to be higher in 2024 than in 2023 due to lower provisions. We expect modest NIM expansion in 2024 (expanded by 17 bps in 2023 from 2022) as interest rates appear to have leveled off and could begin falling later in the year.

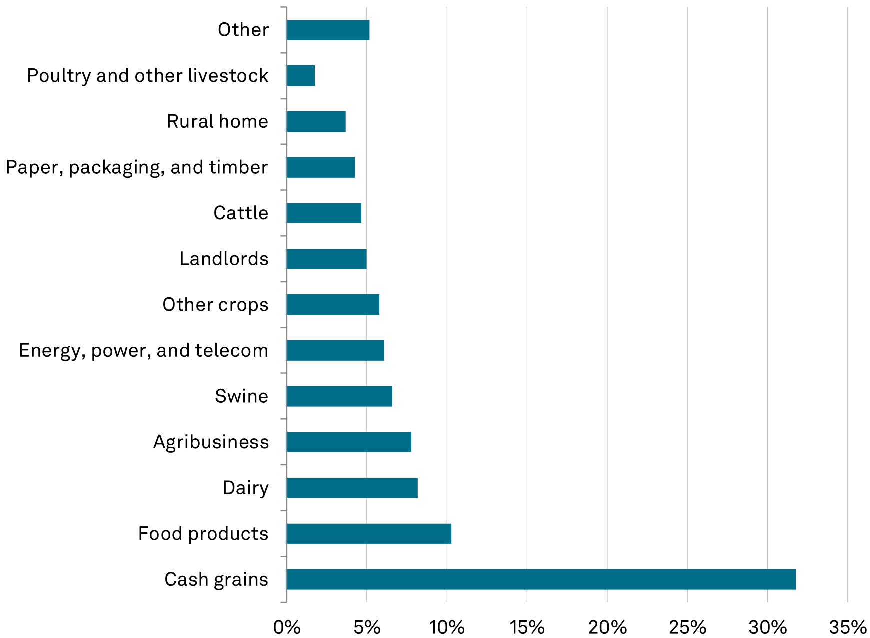
Compeer pays patronage to its customer-members. Total distributions were $210 million compared with $223 million in 2022 and included cash patronage, preferred stock dividends, and other distributions.

In a hypothetical severe stress test scenario that includes an agricultural element, designed and mandated by the FCA, Compeer's CET1 ratio would decrease by approximately 350 bps over a three-year period, but would remain above the regulatory minimum.

Risk Position: Concentrated In Agricultural Lending

Compeer's loan portfolio is highly concentrated to the agriculture industry, though specific commodity concentrations are not outsize. Although nonperforming assets (NPAs) and NCOs rose in 2023, they remain better than those of U.S. regional banks, with the exception of the reserve ratio. Adverse assets could increase in 2024, given the stresses in the industry, but we do not expect a material rise in NCOs, as the broad-based portfolio remains relatively strong.

Compeer Financial ACA -- loan composition by segment
As of Dec. 31, 2023



Source: Company filings, S&P Global Ratings.

In recent years, Compeer has chosen to use capital to expand the loan portfolio above historical levels. We understand that, following several loans that went bad, the company has reviewed its loan portfolio to ensure that underwriting standards remain within its risk appetite.

Delinquencies were up to 90 bps from 50 bps in 2022. Adjusted NPAs, excluding troubled debt restructurings to customer loans and other real estate, increased to 85 bps from 43 bps in 2022. NCOs rose to 26 bps from 0 bps in 2022, which reflected certain loans that went bad. These loans appeared to have been one-offs and do not reflect broad-based weakness in the loan portfolio. Consequently, provisions for loan losses rose to $113 million from negative $11 million in 2022. The ratio of loan loss reserves to gross nonperforming loans, at 31%, was weaker than that of similarly rated U.S. regional banks.

We believe a significant drop in commodity prices and farmland values would stress asset quality more meaningfully, leading to higher losses and weaker earnings. Conservative LTV ratios (average LTV is 50% and 59% on new mortgages), however, have generally mitigated shocks to agricultural prices. Conservatism is reflected in prudent underwriting parameters at loan origination, with Compeer generally limiting lending to no more than 65% of value.

Funding And Liquidity: Concentrated But Stable Wholesale Funding Through The FCS

As the association is a non-depository financial institution, its primary funding source is a wholesale credit agreement with AgriBank, one of four FCS wholesale funding banks. Although liquidity is intentionally limited, Compeer has approximately $2 billion of unused borrowing capacity with AgriBank, with little risk it would lose access to AgriBank funding.

Compeer's $28.3 billion ($26.3 billion advanced) line of credit with AgriBank is renewable every three years. In 2021, the association issued preferred stock and subordinated debt, but due to its structure as a farm credit association, it relies overwhelmingly on AgriBank for funding. In 2023, Compeer redeemed $100 million, or half, of its preferred stock, which makes up a small part of its capital structure, and did not replace it.

Because Compeer relies almost completely on AgriBank for funding and does not hold significant liquid assets, it has a stable funding ratio that is weaker than what rated commercial banks typically operate with. The same is true for the other farm banks and associations we rate. That said, the stability of the funding from AgriBank ameliorates that risk.

Compeer in effect is a beneficiary of the government-sponsored entity status of AgriBank and the FCS. Through AgriBank, Compeer is ultimately able to access the low-cost funds that the FCS raises from the market. As part of its cooperative structure, AgriBank currently requires Compeer to maintain an investment equal to 3.0% (up from 2.55% in 2022) of its average quarterly balance of its notes payable. In addition, Compeer's agreement with AgriBank incorporates covenants related to performance, credit quality, and capital levels, such that should these deteriorate, the cost of funding would increase.

We view Compeer's on-balance-sheet liquidity as solely limited, with a modest $1.6 billion investment portfolio, primarily government-guaranteed securities. Broad liquid assets, consisting mostly of those securities, are less than what we consider short-term wholesale funding, at 0.18x (versus the peer average of 0.28x). This shortfall largely reflects Compeer's small securities portfolio and the funding structure of farm credit associations. Nevertheless, we view liquidity as adequate because of an additional, approximately $2 billion of unused borrowing capacity with AgriBank.

Support: No Uplift To The Rating

Although the rating incorporates the ongoing funding benefits the association receives as an AgriBank owner, we believe there is a low likelihood that the U.S. federal government would provide extraordinary support directly to Compeer in the event of financial distress. Our assessment is that Compeer's individual role is of limited importance to the federal government. In addition, we view Compeer as having a limited link to the government. Its members privately own Compeer, 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

None.

Environmental, Social, And Governance

Environmental factors are a key consideration, given that Compeer is an agricultural lender. We are assessing and monitoring the association's policies and how Compeer incorporates this issue into its underwriting decisions. We believe that Compeer's governance structure is sound and permeated through the organization. Social factors are a positive consideration in our credit rating analysis of Compeer. As an association in the FCS, Compeer benefits from low-cost funding, which helps it support rural communities and agriculture. Moreover, its cooperative structure prioritizes access and benefits for its member-owners and leads it to maintain strong RAC with less focus on short-term profitability.

Group Structure, Rated Subsidiaries, And Hybrids

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

Key Statistics

Table 1

Compeer Financial ACA -- key figures

	--Fiscal year-end Dec. 31--				
(Mil. $)	**2023**	**2022**	**2021**	**2020**	**2019**
Adjusted assets	31,900	29,673	27,008	24,942	22,184
Customer loans (gross)	28,290	26,725	24,515	22,637	19,931
Adjusted common equity	4,773	4,503	4,220	3,943	3,719
Operating revenues	1,018	902	856	797	722
Noninterest expenses	400	375	349	312	288
Core earnings	465	503	489	433	390

Table 2

Compeer Financial ACA -- business position

	--Fiscal year-end Dec. 31--				
	2023	**2022**	**2021**	**2020**	**2019**
Return on average common equity	10.05	11.57	12.04	11.35	10.82

Table 3

Compeer Financial ACA -- capital and earnings

	--Fiscal year-end Dec. 31--				
(%)	**2023**	**2022**	**2021**	**2020**	**2019**
Tier 1 capital ratio	13.13	13.95	14.64	14.69	15.47
S&P Global Ratings' risk-adjusted capital (RAC) ratio before diversification	13.41	14.70	15.48	15.75	16.67
S&P Global Ratings' RAC ratio after diversification	10.06	10.87	11.37	11.51	12.17
Adjusted common equity/total adjusted capital	97.95	95.75	95.47	97.53	97.38
Net interest income/operating revenues	69.59	67.70	64.55	65.87	66.78
Fee income/operating revenues	10.40	11.28	13.46	12.08	10.20
Market-sensitive income/operating revenues	(0.57)	(0.21)	(0.28)	0.07	0.53
Cost to income ratio	39.33	41.54	40.80	39.10	39.82
Preprovision operating income/average assets	2.01	1.86	1.95	2.06	2.02
Core earnings/average managed assets	1.51	1.77	1.88	1.84	1.82

Table 4

Compeer Financial ACA -- risk position

	--Fiscal year-end Dec. 31--				
(%)	**2023**	**2022**	**2021**	**2020**	**2019**
Growth in customer loans	5.85	9.01	8.30	13.57	6.18
Total diversification adjustment/S&P Global Ratings' risk-weighted assets before diversification	33.24	35.29	36.11	36.77	36.95
Total managed assets/adjusted common equity (x)	6.68	6.59	6.40	6.33	5.96
New loan loss provisions/average customer loans	0.41	(0.04)	(0.06)	0.13	0.11
Net charge-offs/average customer loans	0.26	0.00	0.04	0.08	0.01
Gross nonperforming assets/customer loans + other real estate owned	0.85	0.43	0.57	0.67	0.83
Loan loss reserves/gross nonperforming assets	31.36	46.24	45.25	58.42	47.19

Table 5

Compeer Financial ACA -- funding and liquidity

	--Fiscal year-end Dec. 31--				
(%)	**2023**	**2022**	**2021**	**2020**	**2019**
Long-term funding ratio	72.29	72.49	72.65	72.43	72.78
Stable funding ratio	73.43	73.26	73.44	73.67	74.43
Short-term wholesale funding/funding base	32.83	32.81	32.79	33.00	33.00
Broad liquid assets/short-term wholesale funding (x)	0.18	0.16	0.15	0.17	0.20
Broad liquid assets/total assets	4.92	4.37	4.11	4.60	5.29
Short-term wholesale funding/total wholesale funding	32.70	32.54	32.50	32.84	32.82

Compeer Financial ACA--Rating component scores	
Issuer credit rating	**BBB+/Stable/--**
SACP	bbb+
Anchor	bbb+
Economic risk	3
Industry risk	3
Business position	Moderate
Capital and earnings	Strong
Risk position	Adequate
Funding	Adequate
Liquidity	Adequate
Comparable ratings analysis	0
Support	0
ALAC support	0
GRE support	0
Group support	0
Sovereign support	0
Additional factors	0

ALAC--Additional loss-absorbing capacity. GRE--Government-related entity. SACP--Stand-alone credit profile.

Related Criteria

- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, April 30, 2024
- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings Detail (As Of May 6, 2024)*	
Compeer Financial, ACA	
Issuer Credit Rating	BBB+/Stable/--
Preferred Stock	BB+
Issuer Credit Ratings History	
27-Apr-2023	BBB+/Stable/--
14-Apr-2022	BBB+/Positive/--
05-Jun-2018	BBB+/Stable/--

Ratings Detail (As Of May 6, 2024)*(cont.)	
Sovereign Rating	
United States	AA+/Stable/A-1+
Related Entities	
Compeer Financial, FLCA	
Issuer Credit Rating	BBB+/Stable/--
Subordinated	BBB
Compeer Financial PCA	
Issuer Credit Rating	BBB+/Stable/--
Subordinated	BBB

*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.