First Quarter Financial Report 2020-21

For the period ended June 30, 2020

Farm Credit Canada
Advancing the business of agriculture

Canada

Farm Credit Canada

Farm Credit Canada (FCC) is a financially self-sustaining federal commercial Crown corporation reporting to Canadians and Parliament through the Minister of Agriculture and Agri-Food. FCC provides financing and other services to almost 100,000 customers. We're a team of more than 2,000 employees operating from 99 field offices located primarily in rural Canada and our corporate office located in Regina, Saskatchewan.

Contact Corporate Communication at communications@fcc-fac.ca for more information.

First Quarter Financial Report 2020-21

For the period ended June 30, 2020

This report was prepared in accordance with the Treasury Board of Canada Standard on Quarterly Financial Reports for Crown Corporations and should be read in conjunction with disclosures and information contained in FCC's Annual Report and Corporate Plan Summary.[1]

Financial results

This document contains the corporation's unaudited financial results for the first quarter, which ended June 30, 2020.

Net income overview

($ millions)

	Three months ended			
		June 30, 2020		June 30, 2019
Net interest income	**$**	**311.7**	$	290.6
Provision for credit losses		**(41.9)**		-
Non-interest income		**5.0**		4.0
Administration expenses		**(113.7)**		(109.7)
Fair value adjustment		**(1.8)**		(1.1)
Net income	**$**	**159.3**	$	183.8

Net income for the three-month period ended June 30, 2020, decreased by $24.5 million over the prior year. This was mainly due to an increase in provision for credit losses of $41.9 million and an increase in administration expense of $4.0 million, partially offset by an increase in net interest income of $21.1 million.

Net interest income for the three-month period ended June 30, 2020, increased by $21.1 million over the prior year primarily due to loan portfolio growth, higher loan fees and higher investment income. The net interest margin for the three-month period ended June 30, 2020, decreased to 3.03% from 3.10% for the comparable period in 2019-20. The decrease was mainly due to a higher investment portfolio as a precautionary measure to increase liquidity in response to COVID-19.

The provision for credit losses for the three-month period ended June 30, 2020, was $41.9 million higher than the prior year. This was primarily due to increased credit risk in the portfolio due to current economic conditions and the overall increase in portfolio size.

Administration expenses increased $4.0 million year-over-year due to increases in salaries and professional fees, partially offset by decreases in travel and training and benefits.

Loans receivable

FCC experienced overall growth in loans receivable of $1,370 million since March 31, 2020, bringing its loans receivable to $39,783 million at June 30, 2020. Loans receivable growth of 3.6% for the three months ended June 30, 2020, was higher than the loans receivable growth of 3.2% for the first three months of the prior fiscal year. The increase in disbursement volume year-over-year, partially offset by the increase in repayments and the increase in opening loans receivable, resulted in a higher growth rate.

Cash flow

Cash and cash equivalents decreased by $408.4 million since March 31, 2020, to $1,316 million at June 30, 2020, compared to an increase of $103.8 million for the first three months of the prior fiscal year. For the three-month period ended June 30, 2020, cash of $1,177 million and $346.3 million were used in operating activities and investing activities, respectively, while $1,114 million was provided by financing activities.

[1] These documents are available at www.fcc-fac.ca/en/about-fcc/governance/reports.html

Outlook against Corporate Plan Summary

The outlook for financial performance relative to the 2020-21 corporate plan remains uncertain as the long-term impacts of COVID-19 and further support needs to the industry remain unclear. FCC continues to monitor the situation and evaluate the impact of COVID-19 on portfolio growth, credit quality and net income. Net income and return on equity may be at risk of being slightly below the Corporate Plan objectives. This would result from increasing credit risk leading to higher allowance and provision for credit losses impacting net income. The corporation's total capital ratio is higher than planned and well positioned to absorb these potential income impacts. Higher capital levels may also impact return on equity due to the higher than planned equity balance.

Enterprise risk management

FCC has an enterprise risk management framework to identify, manage and respond to risks effectively, consistently and in a co-ordinated manner. The corporation is exposed to four main categories of risk: financial, operational, strategic and reputation. Financial risks include the sub-categories of credit, market and liquidity.

The FCC Board of Directors oversee the corporation’s risk governance framework, which is supported by policies and committees that guide corporate decision-making. The Risk Committee of the Board reviews risk results through a quarterly risk report.

Enterprise Management Team members are accountable for setting the tone on the importance of managing risk in their functional areas, as well as developing and implementing sound risk management strategies and action plans to manage the corporation’s risks in accordance with its risk appetite.

FCC’s risk management process includes risk identification and assessment, measurement, control, monitoring and reporting. This is an ongoing process that considers the corporation’s known identified risks as well as changes to both the internal and external environment that may introduce new risks.

Strategic and emerging risks to the corporation are identified and assessed annually by the Board and executive leadership during the strategic planning process. The related risk trends are reassessed each quarter thereafter. The following risks are being closely monitored and could have potential financial implications for FCC’s customers and FCC:

- The spread of COVID-19 caused significant challenges for the Canadian economy and the agri-food sector. Physical distancing and the temporary closure of non-essential businesses has shifted consumption away from food services to eating at home. Canada’s supply-managed mechanism allows for price and volume management. This mechanism was unable to quickly react and adjust to the change in demand from restaurant and food service closures. Industries affected shifted to reduce production, pressuring profits.
- The pandemic reduced production capacity at Canadian and U.S. livestock processing facilities. This caused a significant backlog of livestock in Canada, negatively impacting the prices received by cattle and hog producers. Canadian government support has been announced for producers with animals remaining on feed longer than anticipated.
- African swine fever (ASF) continues to spread globally (now present in over 50 countries), increasing as a global risk. Many countries limit imports from suppliers with ASF. Canada produces more than twice as much pork than it consumes domestically, and significantly relies on export opportunities for Canadian pork. The impacts of the situation will continue to be monitored.
- Agriculture and agri-food are net exporters globally. As such, trade plays an important role in the stability of this industry. The Canada-United States-Mexico Agreement (CUSMA) took effect on July 1, 2020. CUSMA adds stability to the agriculture and agri-food sectors by preserving existing market access conditions. The overall impact to the dairy and poultry sectors will be determined over time.

A measure of overall stability in the agriculture sector is farmland values. Farmland is the most common form of loan collateral at FCC. Although appreciation in farmland values is forecast to soften in 2020 and 2021, demand for Canadian farmland is expected to remain strong despite trade and demand challenges. The agriculture and agri-food industry has seen a downward trend in short-term liquidity; however, total farm equity remains well above total farm debt. This equity provides FCC with financial options to work with current and new customers.

To support the agriculture and agri-food economic sector during the COVID-19 pandemic, FCC received an enhancement to its capital base to allow for additional lending and enhanced risk exposure. FCC created a support program to ensure producers, agribusiness and agri-food businesses can remain focused on business-critical functions in the current operating environment. To date, the program has included payment deferrals, additional lending through credit lines and operating term loans, and increasing the maximum amount of credit that can be provided to FCC’s largest customers. Although the activity increased overall credit risk to FCC, the additional capital base provides the necessary financial strength and support to respond.

Statement of management responsibility

Management is responsible for the preparation and fair presentation of these consolidated quarterly financial statements in accordance with the Treasury Board of Canada Standard on Quarterly Financial Reports for Crown Corporations, and for such internal controls as management determines is necessary to enable the preparation of consolidated quarterly financial statements that are free from material misstatement. Management is also responsible for ensuring all other information in this quarterly report is consistent, where appropriate, with the consolidated quarterly financial statements.

Based on our knowledge, these unaudited consolidated quarterly financial statements present fairly, in all material respects, the financial position, results of operations and cash flows of the corporation, as at the date of and for the periods presented in the consolidated quarterly financial statements.

Michael Hoffort, P.Ag.
President and Chief Executive Officer

Ross Topp, CPA, CA
Executive Vice-President and Chief Financial Officer

Regina, Canada
August 12, 2020

Condensed Consolidated Financial Statements
Consolidated Balance Sheet

(Unaudited) (thousands of Canadian dollars)		June 30, 2020		March 31, 2020
Assets				
Cash and cash equivalents	**$**	**1,316,086**	$	1,724,503
Short-term investments		**1,095,891**		756,369
Accounts receivable and prepaid expenses		**40,105**		39,378
Derivative financial assets		**9,656**		12,469
		2,461,738		2,532,719
Loans receivable – net (Notes 2 and 3)		**39,491,696**		38,158,149
Finance leases receivable – net		**115,450**		99,744
Investment in associates		**48,882**		39,499
Venture capital investments – net		**80,448**		83,004
Post-employment benefit assets		**181,631**		178,398
		39,918,107		38,558,794
Equipment and leasehold improvements		**25,722**		26,847
Computer software		**29,397**		31,536
Equipment under operating leases		**70,692**		80,227
Right-of-use assets		**181,035**		180,120
Other assets		**14,181**		13,972
		321,027		332,702
Total assets	**$**	**42,700,872**	$	41,424,215
Liabilities				
Accounts payable and accrued liabilities	**$**	**90,749**	$	78,392
Derivative financial liabilities		**525**		535
		91,274		78,927
Borrowings (Note 4)				
Short-term debt		**11,316,196**		9,952,320
Long-term debt		**23,352,187**		23,607,441
		34,668,383		33,559,761
Transition loan liabilities		**191,847**		195,223
Post-employment benefit liabilities		**152,042**		148,694
Lease liabilities		**181,686**		180,353
Other liabilities		**8,489**		7,981
		534,064		532,251
Total liabilities		**35,293,721**		34,170,939
Equity				
Contributed capital		**500,000**		500,000
Retained earnings		**6,890,545**		6,731,232
Accumulated other comprehensive income		**15,822**		21,237
Equity attributable to shareholder of parent entity		**7,406,367**		7,252,469
Non-controlling interest		**784**		807
		7,407,151		7,253,276
Total liabilities and equity	**$**	**42,700,872**	$	41,424,215

The accompanying notes are an integral part of the condensed consolidated financial statements.

Consolidated Statement of Income

(Unaudited) (thousands of Canadian dollars)	Three months ended June 30, 2020	 June 30, 2019
Interest income	$ 391,928	$ 431,729
Interest expense	80,261	141,162
Net interest income	311,667	290,567
Provision for credit losses	(41,898)	(21)
Net interest income after provision for credit losses	269,769	290,546
Net insurance income	5,880	5,985
Net income (loss) from investment in associates	771	(1,206)
Net foreign exchange loss	(1,663)	(356)
Other income (expense)	14	(369)
Net interest income and non-interest income	274,771	294,600
Administration expenses		
Salary and benefits	71,594	68,041
Other	42,115	41,646
Total administration expenses	113,709	109,687
Net income before fair value adjustment	161,062	184,913
Fair value adjustment	(1,777)	(1,160)
Net income	$ 159,285	$ 183,753
Net income attributable to:		
Shareholder of parent entity	$ 159,313	$ 183,736
Non-controlling interest	(28)	17

The accompanying notes are an integral part of the condensed consolidated financial statements.

Consolidated Statement of Comprehensive Income

(Unaudited) (thousands of Canadian dollars)	Three months ended June 30, 2020	 June 30, 2019
Net income	**$ 159,285**	$ 183,753
Other comprehensive income		
Transfer of net realized gains on derivatives designated as cash flow hedges to net income	**(5,415)**	(5,415)
Total comprehensive income	**$ 153,870**	$ 178,338
Total comprehensive income attributable to:		
Shareholder of parent entity	**$ 153,898**	$ 178,321
Non-controlling interest	**(28)**	17

The accompanying notes are an integral part of the condensed consolidated financial statements.

Consolidated Statement of Changes in Equity

(Unaudited) (thousands of Canadian dollars)		Balance March 31, 2020		Net income		Other comprehensive income		Contributions from non-controlling interest		Balance June 30, 2020
Contributed capital	**$**	**500,000**	**$**	**-**	**$**	**-**	**$**	**-**	**$**	**500,000**
Retained earnings		**6,731,232**		**159,313**		**-**		**-**		**6,890,545**
Net gains (transfer of net gains) on derivatives previously designated as cash flow hedges		**21,237**		**-**		**(5,415)**		**-**		**15,822**
Total accumulated other comprehensive income		**21,237**		**-**		**(5,415)**		**-**		**15,822**
Total equity attributable to parent		**7,252,469**		**159,313**		**(5,415)**		**-**		**7,406,367**
Non-controlling interest		**807**		**(28)**		**-**		**5**		**784**
Total	**$**	**7,253,276**	**$**	**159,285**	**$**	**(5,415)**	**$**	**5**	**$**	**7,407,151**

(Unaudited) (thousands of Canadian dollars)		Balance March 31, 2019		Net income		Other comprehensive income		Contributions from non-controlling interest		Balance June 30, 2019
Contributed capital	$	183,725	$	-	$	-	$	-	$	183,725
Retained earnings		6,202,132		183,736		-		-		6,385,868
Net gains (transfer of net gains) on derivatives previously designated as cash flow hedges		43,017		-		(5,415)		-		37,602
Total accumulated other comprehensive income		43,017		-		(5,415)		-		37,602
Total equity attributable to parent		6,428,874		183,736		(5,415)		-		6,607,195
Non-controlling interest		677		17		-		5		699
Total	$	6,429,551	$	183,753	$	(5,415)	$	5	$	6,607,894

The accompanying notes are an integral part of the condensed consolidated financial statements.

Consolidated Statement of Cash Flows

(Unaudited) (thousands of Canadian dollars)		Three months ended June 30, 2020		June 30, 2019
Operating activities				
Net income	**$**	**159,285**	$	183,753
Adjustments to determine net cash (used in) provided by operating activities:				
Net interest income		**(311,667)**		(290,567)
Provision for credit losses		**41,898**		21
Fair value adjustment		**1,777**		1,160
Net (income) loss from investment in associates		**(771)**		1,206
Amortization and depreciation		**9,602**		9,063
Net unrealized foreign exchange losses		**21,931**		550
Net cash outflow from loans receivable		**(1,427,855)**		(1,200,937)
Net cash outflow from finance leases receivable		**(14,412)**		(14,597)
Net change in other operating assets and liabilities		**9,301**		17,588
Interest received		**420,988**		445,522
Interest paid		**(86,920)**		(129,624)
Cash used in operating activities	**$**	**(1,176,843)**	$	(976,862)
Investing activities				
Net cash (outflow) inflow from short-term investments	**$**	**(338,880)**	$	57,692
Acquisition of venture capital investments		**(4,535)**		(1,886)
Proceeds on disposal and repayment of venture capital investments		**3,400**		815
Disbursements to investment in associates [1]		**(8,613)**		(5,373)
Repayments from investment in associates [1]		**-**		410
Purchase of equipment and leasehold improvements		**(992)**		(1,064)
Purchase of computer software		**(1,416)**		(3,202)
Proceeds on disposal of equipment under operating leases [2]		**4,710**		5,151
Cash (used in) provided by investing activities	**$**	**(346,326)**	$	52,543
Financing activities				
Long-term debt issued	**$**	**2,275,000**	$	2,775,000
Long-term debt repaid		**(1,383,034)**		(1,532,796)
Short-term debt issued		**3,073,504**		2,069,927
Short-term debt repaid		**(2,847,668)**		(2,281,073)
Principal repayment of lease liabilities		**(3,515)**		(3,325)
Cash provided by financing activities	**$**	**1,114,287**	$	1,027,733
Change in cash and cash equivalents	**$**	**(408,882)**	$	103,414
Cash and cash equivalents, beginning of period		**1,724,503**		770,517
Effects of exchange rate changes on the balances of cash held and due in foreign currencies		**465**		384
Cash and cash equivalents, end of period	**$**	**1,316,086**	$	874,315
Cash and cash equivalents consists of:				
Cash	**$**	**827,219**	$	807,575
Short-term investments		**488,867**		66,740

[1] In 2019-20, Investments in Associates were shown as a net cash outflow of $4,963 as at June 30, 2019.

[2] Comparative figures in 2019 were reclassified. See Note 7 in the March 31, 2020 annual report.

The accompanying notes are an integral part of the condensed consolidated financial statements.

Notes to the Condensed Consolidated Financial Statements (Unaudited)

1. Significant accounting policies

Basis of presentation

The condensed consolidated interim financial statements (interim financial statements) comply with the Standard on Quarterly Financial Reports for Crown Corporations issued by the Treasury Board of Canada.

These interim financial statements do not include all of the information required for complete annual financial statements and should be read in conjunction with the annual audited financial statements for the year ended March 31, 2020.

Unless otherwise stated, all dollar amounts presented in the Notes to the Condensed Consolidated Financial Statements are in thousands of Canadian dollars, which is the functional currency of Farm Credit Canada (FCC).

Accounting policies

The accounting policies adopted in the preparation of these interim financial statements are consistent with those followed in the annual, audited financial statements for the year ended March 31, 2020.

Accounting standards issued but not yet effective

FCC has reviewed the new standards and amendments that have been issued by the International Accounting Standards Board (IASB) but are not yet effective and determined that the following may have an impact on FCC in the future. Management is in the process of assessing the impact of this standard on FCC's financial statements and accounting policies. A number of other new standards, amendments and improvements that have been issued but are not yet effective are not listed below as FCC determined that they will not have a significant impact on the consolidated financial statements.

Standard	Details	Date of initial application
IFRS 17 – Insurance contracts	In May 2017, the IASB issued IFRS 17, which provides a single principle-based standard to account for all types of insurance contracts. IFRS 17 provides updated information about the obligations, risks and performance of insurance contracts and increases transparency in financial information reported by insurance companies, which will give investors and analysts more confidence in understanding the insurance industry. It also introduces consistent accounting for all insurance contracts based on a current measurement model. FCC is assessing the impact of this standard and the extent of the impact of the adoption is unknown at this time.	April 1, 2023

2. Loans receivable – net

($ thousands)	Term to maturity Within 1 year	1 - 5 years	Over 5 years	June 30, 2020	March 31, 2020
Floating	$ 4,020,206	$ 12,265,585	$ 384,453	$ 16,670,244	$ 16,220,498
Fixed	3,874,753	14,142,153	5,129,174	23,146,080	22,220,880
Loans receivable – gross	$ 7,894,959	$ 26,407,738	$ 5,513,627	39,816,324	38,441,378
Deferred loan fees				(33,477)	(28,078)
Loans receivable – total				39,782,847	38,413,300
Allowance for credit losses				(291,151)	(255,151)
Loans receivable – net				$ 39,491,696	$ 38,158,149

3. Allowance for credit losses – loans receivable

As at June 30, 2020 ($ thousands)	Stage 1	Stage 2	Stage 3	Total
Allowance for credit losses, beginning of year	$ 25,618	$ 158,240	$ 71,293	$ 255,151
Transfer to stage 1	2,786	(2,758)	(28)	-
Transfer to stage 2	(3,279)	8,047	(4,768)	-
Transfer to stage 3	(2)	(2,548)	2,550	-
Changes due to new loans originated	10,162	6,069	1,142	17,373
Loans receivable that have been derecognized during the period	(846)	(3,716)	(2,175)	(6,737)
Net remeasurement of loss allowance	(4,457)	26,215	7,042	28,800
Writeoffs	-	(10)	(3,525)	(3,535)
Recoveries of amounts previously written off	-	47	39	86
Losses covered under Hog Industry Loan Loss Reserve Program	4	1	8	13
Total allowance	$ 29,986	$ 189,587	$ 71,578	$ 291,151

As at March 31, 2020 ($ thousands)	Stage 1	Stage 2	Stage 3	Total
Allowance for credit losses, beginning of year	$ 31,780	$ 115,402	$ 50,828	$ 198,010
Transfer to stage 1	33,669	(32,976)	(693)	-
Transfer to stage 2	(11,523)	39,075	(27,552)	-
Transfer to stage 3	(107)	(17,208)	17,315	-
Changes due to new loans originated	25,376	12,573	34,997	72,946
Loans receivable that have been derecognized during the period	(13,764)	(9,788)	(9,934)	(33,486)
Net remeasurement of loss allowance	(36,411)	91,543	34,999	90,131
Writeoffs	-	(2,529)	(29,757)	(32,286)
Recoveries of amounts previously written off	-	143	1,368	1,511
Losses covered under Hog Industry Loan Loss Reserve Program	(2)	5	(278)	(275)
Changes to allowance model parameters	(3,400)	(38,000)	-	(41,400)
Total allowance	$ 25,618	$ 158,240	$ 71,293	$ 255,151

4. Borrowings

Short-term debt

($ thousands)	June 30, 2020	March 31, 2020
Government of Canada debt		
Floating-rate borrowings	**$ 3,533,578**	$ 2,990,733
Fixed-rate borrowings	**6,847,494**	6,417,486
	10,381,072	9,408,219
Capital markets debt		
USD fixed-rate promissory notes[1]	**630,940**	525,385
Retail and institutional fixed-rate notes	**304,184**	18,716
	935,124	544,101
Total	**$ 11,316,196**	$ 9,952,320

[1] $463.0 million USD (March 31, 2020 – $370.1 million USD)

Long-term debt

($ thousands)	June 30, 2020	March 31, 2020
Government of Canada debt		
Floating-rate borrowings	**$ 13,405,596**	$ 13,212,981
Fixed-rate borrowings	**9,946,591**	10,105,409
	23,352,187	23,318,390
Capital markets debt		
Retail and institutional fixed-rate notes	**-**	289,051
Total	**$ 23,352,187**	$ 23,607,441