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AGRICULTURAL CREDIT CONDITIONS in the Seventh Federal Reserve District were characterized by continued sluggishness in farm loan demand and farm loan repayment rates in the second quarter. Renewals and extensions of farm loans continued at a high level, as did interest rates. Agricultural bankers had ample funds for lending to farmers, but the average loan/deposit ratio continued to trend lower. These and other findings represent the consensus view obtained from a recent survey of nearly 550 agricultural banks in the District.

The continuing sluggishness in farm loan demand extends a trend that has prevailed for the past two and a half years. Over 40 percent of the bankers reported farm loan demand in the second quarter was even weaker than a year ago, while 25 percent reported farm loan demand was stronger. The overall measure of loan demand, at 85, was up slightly from the previous quarter, but still indicative of a constrained level of farm borrowing (see table on page 2).

Several factors underlie the continued weakness in farm loan demand. In an environment of depressed farm earnings and high interest rates, cuts in livestock production, very weak capital expenditures by farmers, and lower prices for some major inputs have lowered cash outflows and the borrowings needed to purchase farm inputs. Inventories of hogs on farms in Illinois, Indiana, and Iowa on June 1 were down a tenth from last year. Borrowing needs of livestock producers were further reduced in the second quarter by lower feed costs and by a smaller inventory of cattle on feed in Iowa. In April and May, unit retail sales of tractors and combines to farmers in District states were off 35 and 60 percent, respectively, from the year before. Borrowing needs of crop farmers this spring were held in check by a slight reduction in acreage, lower fuel costs, and stable to lower prices for seed and fertilizer.

While demand for new borrowings by farmers remains weak, the portfolio of farm loans held by banks is being sustained by slower repayments and more renewals and extensions of existing loans. The proportion of bankers noting that second quarter farm loan repayments were slower than the year before substantially exceeded the nominal proportion noting faster repayments. As a result, the overall measure of farm loan repayments held at a very low level. Similarly, two-thirds of the bankers reported an increase in renewals and extensions while only 3 percent noted fewer renewals and extensions than a year ago.

The availability of funds for lending to farmers remained ample at banks in the second quarter, extending the trend of the past two years. Deposits at District agricultural banks in mid-June were 3 percent higher than in mid-March and 10 percent higher than a year ago. The deposit growth outstripped loan growth, pushing the average loan/deposit ratio at District agricultural banks contraseasonally lower in the second quarter. At mid-year, the ratio was 3.5 percentage points lower than a year ago and 10 percentage points lower than the summer 1979 peak. In conjunction with the lower loan/deposit ratio and bankers' perceptions of ample funds for lending, 55 percent of the bankers indicated they would like to have a higher loan/deposit ratio. Only 14 percent would like a lower loan/deposit ratio.

Interest rates charged on farm loans by District agricultural bankers declined only nominally in the second quarter. As of mid-year, the typical rates charged by banks on both feeder cattle and farm operating loans averaged 17.2 percent. The averages were only 10 basis points lower than three months earlier and 55 basis points below the upward trending levels of the year before. Rates charged on farm real estate mortgages averaged 16.7 percent at mid-year, down only nominally from 3 months ago and up from 16.4 percent a year ago.

For the past several quarters, banks have been at a competitive disadvantage with respect to interest rates charged by other agricultural lenders. This situation continued in the second quarter, with the interest rate differential in some cases widening. Rates charged by federal intermediate credit banks (FICBs) that indirectly serve farmers—mostly through production credit associations (PCAs)—in District states declined 30 to 50 basis points from April to July. FICB rates in District states

Selected measures of credit conditions at Seventh District agricultural banks

	Loan demand	Fund availability	Loan repayment rates	Average rate on feeder cattle loans[1]	Average loan-to-deposit ratio[1]	Banks with loan-to-deposit ratio above desired level[1]
	(index)[2]	*(index)*[2]	*(index)*[2]	*(percent)*	*(percent)*	*(percent of banks)*
1977						
Jan-Mar	161	115	79	8.71	59.4	28
Apr-June	169	103	66	8.74	61.2	38
July-Sept	161	77	52	8.79	63.5	46
Oct-Dec	147	86	59	8.85	62.3	41
1978						
Jan-Mar	152	79	64	8.90	63.7	44
Apr-June	148	73	81	9.12	64.5	46
July-Sept	158	64	84	9.40	65.8	52
Oct-Dec	135	62	93	10.14	65.4	50
1979						
Jan-Mar	156	51	85	10.46	67.3	58
Apr-June	147	62	91	10.82	67.1	55
July-Sept	141	61	89	11.67	67.6	52
Oct-Dec	111	67	79	13.52	66.3	48
1980						
Jan-Mar	85	49	51	17.12	66.4	51
Apr-June	65	108	68	13.98	65.0	31
July-Sept	73	131	94	14.26	62.5	21
Oct-Dec	50	143	114	17.34	60.6	17
1981						
Jan-Mar	70	141	90	16.53	60.1	17
Apr-June	85	121	70	17.74	60.9	20
July-Sept	66	123	54	18.56	60.9	21
Oct-Dec	66	135	49	16.94	58.1	17
1982						
Jan-Mar	76	134	36	17.30	57.8	18
Apr-June	85	136	41	17.19	57.3	14

[1]At end of period.

[2]Bankers responded to each item by indicating whether conditions during the current quarter were higher, lower, or the same as in the year-earlier period. The index numbers are computed by subtracting the percent of bankers that responded "lower" from the percent that responded "higher" and adding 100.

ranged from 13 percent to 14.15 percent in July. Since PCA loans are funded through FICBs, this suggests that effective PCA rates to farm borrowers, including stock purchase requirements, remained below bank rates in most areas. Rates charged by the Farmers Home Administration (FmHA) on farm operating loans have held at 14.25 percent for several months, while rates on farm ownership loans have held at 13.25 percent. Rates on CCC loans declined from 13.9 percent in April to 13.5 percent in July.

Activity at other farm lenders has varied considerably this year. Although up from year-earlier levels in June, farm loans made by PCAs for the entire second quarter were off 1.6 percent from the year before. That marked the third consecutive quarter that loans made by PCAs have lagged year-earlier levels. As a result, the portfolio of farm loans held by PCAs at the end of June was down 1 percent from last year. (The decline is a rarity in the long history of growth at PCAs.) The mid-year portfolio of farm loans held by PCAs in District states was down nearly 2.5 percent from a year ago.

Current data on other short-term lenders is not as readily available as for PCAs. In the first quarter, however, the portfolio of nonreal estate farm loans held by the FmHA leveled off, but remained 12 percent above the year-earlier level at the end of March. The portfolio of farm loans held by the CCC continued to grow rapidly in the first quarter and was more than double the year-earlier level at the end of March. CCC lending in the second quarter, however, probably slowed significantly as the movement of grain under CCC loan tapered off.

Farm mortgage lending activity at both FLBs and life insurance companies has slowed substantially this year. In the first and second quarters, new loans made by FLBs lagged year-earlier levels by 20 and 37 percent, respectively, with the second quarter volume at a four-year low. The slowing has narrowed the year-over-year gain in the portfolio of farm mortgages held by FLBs from 21 percent last December to 15 percent at the end of June. Farm mortgages acquired by life insurance companies have been trending sharply lower since mid-1979. In the first five months of this year, acquisitions were off 42 percent from the year before and off 73 percent from the same months in 1979. Because of the prolonged slowing, the portfolio of farm mortgages held by life insurance companies at the end of May was no higher than it was a year ago.

The financial conditions surrounding farmers and their lenders are of growing concern. This year marks the third consecutive year of depressed farm earnings, despite a recovery for livestock producers. Crop farmers in particular remain in a cash flow squeeze that—for those highly leveraged—is aggravated by high interest rates. Land values in many areas have already weakened substantially, and many analysts look for further declines the rest of this year. Farm income prospects for the year ahead are far from certain. But good crop developments to date this year, coupled with lackluster export prospects, increasingly portend another surplus harvest and another year of financial struggle for many crop farmers.

The financial vulnerability of farmers could be aggravated in the months ahead by the apparently low adaptation of farmers to changes in the feed grain and wheat programs. This year, disaster payment provisions of the federal government's feed grain and wheat programs have been largely eliminated in areas where the expanded federal crop insurance program is available. However, the bankers that responded to the latest survey indicated that, on average, only one out of every six District farmers purchased federal crop insurance this year. Coverage is higher in Iowa where apparently a fourth of the farmers purchased the insurance. But bankers in the other District states reported that only 10 to 13 percent of the farmers acquired federal crop insurance. These low proportions imply that fewer farmers will be eligible for disaster benefits in the event of weather-related crop losses. Similarly, compliance with the "reduced acreage program" (RAP)—and thus eligibility for price support and income benefits—is also quite low. Iowa bankers estimated that about 43 percent of the feed grain acreage in that state was in compliance with the RAP requirements. But the compliance estimates from bankers in the other District states ranged from a low of 19 percent in Illinois to 23 percent in Wisconsin. (Subsequent USDA reports place compliance in both Illinois and Indiana at 19 percent.) The low compliance rates increase the chances that a bumper 1982 harvest will hold corn prices below the loan rate for an extended period, resulting in a further accumulation of financial stress for farmers. Only farmers in compliance with RAP requirements will be eligible for regular and reserve CCC loans and—if applicable—deficiency payments.

Characterizing the current financial plight of agriculture is difficult. The oft-repeated comparison of current conditions with the Depression era is clearly an overstatement of the situation in agriculture today. While net income of the farm sector, adjusted for inflation, is the lowest since the early 1930s, those earnings today are spread among a third fewer farm operating families. Moreover, most farm families have earnings from nonfarm sources. In 1981, for example, 8 out of every 10 farmers who borrowed from an FLB had earnings from nonfarm sources. Among those borrowers, net nonfarm earnings in 1981 were expected to be $45,000.

Nevertheless, there is little doubt that significant problems exist. The incidence of farmers having to liquidate some or all capital assets to meet debt servicing requirements and/or family living expenses is considerably above the norm of the recent past. Current prospects seem to portend an even higher incidence of liquidations in the months ahead. With three-fourths of the farm sector assets in real estate, and the comparatively few transactions in farm real estate—particularly now—increased liquidations may continue to weigh heavily on land values.

Declining land values erode the unrealized equity of landowners. Yet there is evidence that a large proportion of the agricultural assets are held in financially strong hands. Some analysts estimate that approximately half of all farmland is held debt-free. Moreover, the equity in farm sector assets at the beginning of this year, on a per farm basis, was 3.6 times the level of a decade ago. Even adjusted for inflation, the equity per farm was no lower than in 1976 and was 60 percent higher than a decade ago. Farmers with relatively little or no debt will be able to weather the current stress with far less disruption to their operation than highly leveraged farmers.

Gary L. Benjamin

Selected agricultural economic developments

Subject	Unit	Latest period	Value	Percent change from Prior period	Percent change from Year ago
Index of prices received by farmers	1977=100	July	137	0	− 4
Crops	1977=100	July	125	0	− 9
Livestock	1977=100	July	149	0	+ 1
Index of prices paid by farmers	1977=100	July	157	+ 0.6	+ 5
Production items	1977=100	July	151	0	+ 2
Producer price index* *(finished goods)*	1967=100	June	280	+ 0.8	+ 4
Foods	1967=100	June	263	+ 0.4	+ 4
Processed foods and feeds	1967=100	June	256	+ 0.6	+ 2
Agricultural chemicals	1967=100	June	294	− 0.3	+ 2
Agricultural machinery and equipment	1967=100	June	309	+ 0.6	+ 8
Consumer price index** *(all items)*	1967=100	June	291	+ 1.2	+ 7
Food at home	1967=100	June	283	+ 1.0	+ 5
Cash prices received by farmers					
Corn	dol. per bu.	July	2.54	− 1.2	−19
Soybeans	dol. per bu.	July	6.05	− 1.1	−15
Wheat	dol. per bu.	July	3.29	− 3.0	− 9
Sorghum	dol. per cwt.	July	4.19	+ 0.5	−13
Oats	dol. per bu.	July	1.78	− 5.3	− 2
Steers and heifers	dol. per cwt.	July	63.80	− 3.2	0
Hogs	dol. per cwt.	July	58.00	+ 0.7	+18
Milk, all sold to plants	dol. per cwt.	July	13.10	0	− 2
Broilers	cents per lb.	July	28.6	0	− 5
Eggs	cents per doz.	July	55.2	+ 7.0	− 6
Income *(seasonally adjusted annual rate)*					
Cash receipts from farm marketings	bil. dol.	4th Quarter	143	− 2.9	− 2
Net farm income	bil. dol.	4th Quarter	26	− 9.5	+28
Nonagricultural personal income	bil. dol.	June	2,513	+ 0.3	+ 7

*Formerly called wholesale price index.

**For all urban consumers.

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