FEDERAL RESERVE BANK OF CHICAGO

# AGRICULTURAL LETTER

ISSN 0002 - 1512

November 12, 1982 Number 1590

**AGRICULTURAL CREDIT CONDITIONS** in the Seventh District during the third quarter were characterized by continued softness in farm loan demand, declining interest rates, and ample fund availability. Average loan-to-deposit ratios rose slightly, but farm loan repayment rates slowed and renewals and extensions of farm loans increased. These findings from a recent survey represent the consensus of 525 bankers in the Chicago Federal Reserve District.

Farm loan demand at District agricultural banks remained soft. The overall measure of farm loan demand, at 87, was up nominally from the previous quarter, but still indicative of a constrained level of farm borrowing (see table on page 2). Nearly two-fifths of the rural bankers reported farm loan demand in the third quarter was less than a year ago, while 26 percent reported it higher. The continued weakness in farm loan demand at rural banks no doubt reflects farmers' efforts to pare operating expenses and capital expenditures down to essential needs in the wake of the continuing squeeze on farm earnings.

**Interest rates charged** on farm loans by District agricultural banks fell to a two-year low in the third quarter. By the end of the quarter, interest rates charged on feeder cattle and operating loans averaged 15½ percent, down about 160 basis points from three months ago and down 3 percentage points from the peak of a year ago. Interest rates on farm real estate loans averaged 15½ percent, down slightly more than 1 percentage point from three months ago and 2 percentage points from the peak of a year ago. Among District states, average rates varied little. Rates on operating and feeder cattle loans ranged from 15¼ percent in Illinois to 16 percent in Indiana. Rates on farm real estate loans varied from 15¼ percent in Wisconsin to 16 percent in Indiana.

Lower rates on farm loans partially reflect the declining costs of funds at rural banks. Rates on deposits at agricultural banks have become increasingly reflective of market interest rate trends. Rates paid on many of the more popular deposit-type instruments, for example, are now tied to short-term U.S. Treasury bill rates. Since U.S. Treasury bill rates have trended lower in recent months (see back of *Agricultural Letter*), some deposit rates also have declined significantly, lowering costs of new loanable funds to banks. Despite the downtrend, however, rural banks remain at a disadvantage with respect to interest rates charged on farm loans by other lenders. At the end of the third quarter, rates charged by production credit associations—banks' major competitor for nonreal estate loans—averaged about 14 percent. Federal land bank rates on farm mortgages averaged between 12 and 13 percent. Rates charged by the Farmers Home Administration were lowered this month to 11.5 percent, down from 14.25 percent on farm operating loans and 13.25 percent on farm ownership loans in the third quarter. Rates charged by the CCC on regular, reserve, and storage facility loans taken out this month were lowered to 9.75 percent, down from an average of 13 percent in the third quarter.

**Bank liquidity** is a function of many variables, but several measures in the latest survey indicate that the liquidity pressures on District agricultural banks eased from a year ago. In the third quarter, for instance, the index of fund availability, at 136, was at a relatively high level and up considerably from the level of a year ago. Three times as many bankers reported that fund availability in the third quarter exceeded year-ago levels as reported it lower. However, deposit growth at District agricultural banks in the third quarter was modest by historical standards. Deposits at agricultural banks that are members of the Federal Reserve System rose less than 1 percent in the third quarter. Nevertheless, deposits were still up 9 percent from a year ago and ample to accommodate the weak loan demand.

Other evidence of liquidity is reflected in the loan-to-deposit ratios at rural banks. At the end of the third quarter, the loan-to-deposit ratio was a low 57.8 percent.

## 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 |
| July-Sept | 87 | 136 | 36 | 15.56 | 57.8 | 15 |

[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.

Although this was up slightly from the previous quarter, it was down from a year ago and considerably below the peak of three years ago. In District portions of Illinois and Indiana and in Iowa, average loan-to-deposit ratios were up from the second quarter, but in Michigan and Wisconsin average loan-to-deposit ratios were down. Over half of the rural bankers responding to the survey viewed their ratios at the end of the quarter as being lower than desired. Only a seventh indicated that the loan-to-deposit ratio was higher than desired.

Farm loan repayments slowed this summer. At 36, the measure of loan repayment rates equalled the 20-year low established in the first quarter. Over 65 percent of the bankers reported that loan repayments were down from a year ago compared with only 2 percent who indicated repayments were up. The rest indicated repayments were about the same. In addition, renewals and extensions of farm loans continued at fairly high levels in the third quarter. The measure of renewals and extensions, at 167, was the second highest ever in the history of the survey.

The slowing in farm loan repayment rates and the high rate of renewals and extensions undoubtedly reflect the stressed conditions in agriculture. Crop prices have declined sharply in recent months, averaging well below the cost of production for many producers. Although the livestock sector has been the one bright spot in agriculture this year, cattle prices recently have declined below year-earlier levels, trimming the profitability in operations that had been evident for much of this year. Low commodity prices have prolonged and intensified the financial distress of many farmers, forcing a larger-than-normal number of them to refinance or restructure debts.

**Activity at other commercial farm lenders** has slowed considerably this year. Farm loans made by production credit associations in the third quarter were down 6 percent from the year before. This was the fourth consecutive quarter of year-to-year declines in PCA lending, marking an unprecedented departure from the previous 25 years of sustained growth. As a result, loans outstanding at PCAs at the end of the third quarter were down 2 percent from the year-earlier level.

Lending activity in the farm mortgage market is also down substantially this year. Steepening year-to-year declines in the amount of new money loaned by federal land banks have been evident since last December. In the third quarter, new money loaned by FLBs was 50 percent below the year-earlier level and the smallest amount in five years. With the slowing in new lending, the year-to-year gain in the portfolio of farm mortgages held by FLBs narrowed from 21 percent last December to 12 percent at the end of September. In addition, the acquisition of farm mortgages by life insurance companies in July and August continued the three-year slide that has pulled farm mortgage lending by life insurance companies to a 10-year low.

Lending activity at the Farmers Home Administration was up, for the most part, during the third quarter but trailed year-earlier levels for the fiscal year as a whole. Obligations under the Farm Ownership Loan Program in the third quarter were up over a tenth from the year before. But for fiscal 1982 (which ended on September 30), the $660 million in lending under the Farm Ownership Loan Program was nearly a fifth below the year-earlier level. In contrast, obligations under the Farm Operating Loan Program were up during the third quarter, and lending under that program during fiscal 1982, at $1.3 billion, exceeded the year-earlier level by 48 percent. Lending under the FmHA's Emergency (Disaster) Loan Program in the third quarter was off 40 percent from the year before and—at $2.2 billion—off 57 percent for the entire fiscal year. In addition, no loans were made under the Economic Emergency Loan Program in 1982, following lending of $1.2 billion in fiscal 1981. Though final budget approval has not been given, proposals set the FmHA farm programs at $3.8 billion in fiscal 1983, 6 percent below fiscal 1982 obligations. About $1.5 billion each has been set for the Farm Operating Loan Program and the Emergency (Disaster) Loan Program. The Farm Ownership Loan Program has been allocated about $800 million. Further curtailment in FmHA lending activity, given the widespread financial difficulties of farmers, may bring about a clamor for higher lending authorizations.

**The outlook for credit conditions** is shrouded by a number of uncertainties, particularly with respect to interest rate trends, future commodity prices, farm income prospects, and spending patterns of farmers. Market rates of interest have declined substantially in recent months. If rates hold at current levels or decline even further, pressures on the costs of funds at rural banks will subside further, resulting in lower rates on farm loans.

However, farm loan demand is likely to remain soft. Declining asset values and past and prospective operating losses have lowered the credit-worthiness of farmers and their desire for new financing to cover capital purchases. Borrowing to finance operating capital may be tempered by the recent moderation in the rise in input prices and efforts to trim operating costs. Borrowings by livestock producers could strengthen with the long-awaited expansion in hog production or increased movement of cattle into feedlots. However, the existing financial vulnerability of some producers is likely to be an offsetting factor to larger borrowings.

Borrowing to finance operating capital may also be tempered by participation in the 1983 feedgrain and wheat programs. Farmers who sign up for the feedgrain program may receive up to one-half of the program's acreage diversion payment and price deficiency payment in advance. As a result, such cash inflows may provide farmers with the funds to trim existing debt levels or purchase inputs for the new crop. In the first three weeks of the sign-up, farmers enrolled the equivalent of a tenth of the 1982 base acreage and two-thirds of the participating farmers requested advance payments.

Nevertheless, rural bankers expect demand for some types of farm loans to pick up in the months ahead, perhaps as a result of the reduced lending on the part of other commercial farm lenders. Bankers expect the demand for operating and crop storage loans in the current quarter to exceed year-earlier levels. But demands for feeder cattle loans, farm machinery loans, and farm real estate loans are expected to be down.

Jeffrey Miller

## Selected agricultural economic developments

| Subject | Unit | Latest period | Value | Percent change from: Prior period | Percent change from: Year ago |
|---|---|---|---|---|---|
| **Farm finance** | | | | | |
| Total deposits at agricultural banks† | 1972-73=100 | October | 260 | + 1.3 | + 8 |
| Total loans at agricultural banks† | 1972-73=100 | October | 284 | + 0.6 | + 5 |
| Production credit associations | | | | | |
| Loans outstanding | | | | | |
| United States | mil. dol. | September | 21,875 | - 0.9 | - 2 |
| Seventh District states | mil. dol. | September | 4,503 | + 0.3 | - 3 |
| Loans made | | | | | |
| United States | mil. dol. | September | 2,079 | - 1.8 | - 5 |
| Seventh District states | mil. dol. | September | 419 | - 1.3 | - 7 |
| Federal land banks | | | | | |
| Loans outstanding | | | | | |
| United States | mil. dol. | September | 46,954 | + 0.3 | +12 |
| Seventh District states | mil. dol. | September | 11,211 | + 0.3 | +11 |
| New money loaned | | | | | |
| United States | mil. dol. | September | 292 | -20.7 | -57 |
| Seventh District states | mil. dol. | September | 66 | -14.0 | -60 |
| Interest rates | | | | | |
| Feeder cattle loans†† | percent | 3rd Quarter | 16.38 | - 5.0 | -10 |
| Farm real estate loans†† | percent | 3rd Quarter | 16.15 | - 3.5 | - 5 |
| Three-month Treasury bills | percent | 11/4-11/10 | 7.90 | + 4.2 | -32 |
| Federal funds rate | percent | 11/4-11/10 | 9.45 | - 1.6 | -33 |
| Government bonds *(long-term)* | percent | 11/4-11/10 | 10.54 | - 4.4 | -23 |
| **Agricultural trade** | | | | | |
| Agricultural exports | mil. dol. | September | 2,388 | - 4.2 | -25 |
| Agricultural imports | mil. dol. | September | 1,298 | - 4.3 | + 1 |
| **Farm machinery sales**[P] | | | | | |
| Farm tractors | units | September | 6,353 | +29.8 | -12 |
| Combines | units | September | 1,823 | +39.3 | -34 |
| Balers | units | September | 729 | -25.6 | -34 |

†Member banks in Seventh District having a large proportion of agricultural loans in towns of less than 15,000 population.

††Average of rates reported by District agricultural banks at beginning and end of quarter.

[P]Preliminary.

**AGRICULTURAL LETTER**
**FEDERAL RESERVE BANK OF CHICAGO**
**Public Information Center**
**P.O. Box 834**
**Chicago, Illinois 60690**
Tel. no. (312) 322-5112

FEDERAL RESERVE BANK OF CHICAGO
AGRICULTURAL LETTER



AG001
HEAD-DEPT. OF AGRIC.ECON.
INSTITUTE OF AGRICULTURE
UNIVESITY OF MINNESOTA
ST.PAUL.MN 55101