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AGRICULTURAL LETTER

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District credit conditions

Credit conditions across the Seventh Federal Reserve District during the summer months mostly followed the trends that have been evident for some time. Survey responses from about 500 agricultural bankers indicate that farm loan demand remains relatively strong and that banks have ample supplies of funds for lending to farmers. However, farm loan repayment rates slipped during the third quarter, reflecting pressure on some borrowers due to the drought.

After remaining quite weak during the past few years, farm loan demand at District agricultural banks has strengthened considerably in 1988. The strongest quarterly measure of farm loan demand this year was registered in the July-to-September period. At 120, the third quarter measure of farm loan demand is up from 113 in the previous quarter and 75 a year ago. The latest measure represents a composite of the almost 38 percent of banks that reported increased farm loan demand compared to last year during the quarter, less the 17 percent that reported a decline. The remaining 45 percent of the responding bankers noted that farm loan demand at their banks was unchanged from the comparable three month period last year. Among the individual District states, farm loan demand was particularly strong in Illinois, Iowa, and Wisconsin, which all registered loan demand measures above the district average. Indiana and Michigan, on the other hand, had a larger proportion of bankers reporting weaker farm loan demand compare to a year ago than those reporting a strengthening. However, the majority of the respondents from both states, more than 60 percent, noted no change from a year ago in the level of farm loan demand.

Funds available for lending to farmers at District agricultural banks remain ample. The third quarter measure of fund availability, at 115, is down from the very high levels of the last two years, but continues to indicate that adequate funding for farm loans is available at District agricultural banks. Only 9 percent of the survey respondents reported a decline from a year earlier in the availability of funds. In contrast, more than 24 percent continued to report increases during the third quarter, while two-thirds indicated that fund availability was unchanged from the high level of a year earlier. The measure of fund availability was high across the District, ranging from 106 among responding banks in Illinois to 122 among banks in Iowa and Wisconsin.

The pickup in farm loan demand in 1988 has reversed the downtrend in loan-to-deposit ratios at District agricultural banks that had been evident through the 1980s. After holding in the mid to upper 60 percent range in the late 1970s and early 1980s, the ratio of loans to deposits at District agricultural banks trended sharply lower as the sector underwent significant restructuring. For a six month period in late 1986 and early 1987, the ratio dropped below 50 percent. After hovering near that level for about a year, however, the ratio has move higher in 1988. At the end of the third quarter, the average of the loan-to-deposit ratios at the responding banks stood at 54.3 percent, up from 52.1 three months earlier. Agricultural banks in Illinois an Iowa continue to report the lowest average loan-to-deposit ratios among the District states, reporting averages of 50.8 percent and 47.5 percent, respectively, at the end of the third quarter. Bankers in each of the other District states reported loan-to-deposit ratios that averaged more than 60 percent, with Michigan bankers reporting the highest ratio at 67 percent.

Despite the increases recorded in loan-to-deposit ratios this year, most of the bankers who responded to the survey indicated a preference for a higher ratio. About two-thirds of the survey respondents indicated that their current loan-to-deposit ratio was below the desired level, while only 8 percent indicated that it was too high. The remaining fourth of the bankers were satisfied with their loan-to-deposit ratios at the current level. For the District as a whole, the average of the surveyed bankers' desired loan-to-deposit ratios, at 61.3 percent, was about 7 percentage points higher than the average of their actual ratios. Although well below the historical highs, the bankers' desired loan-to-deposit ratios are in line with the levels that were reported in the mid 1970s. Among individual District states, the desired loan-to-deposit ratios ranged from about 58 percent in Illinois and Iowa to as high as 70 percent among Michigan bankers.

Following a long downturn, interest rates charged on loans to farmers by District agricultural banks have moved higher in recent months. From the peak of more than 18 percent in 1981, interest rates on feeder cattle loans and farm operating loans trended down to

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)*
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
Oct-Dec	74	151	47	14.34	55.1	11
1983						
Jan-Mar	69	158	66	13.66	53.3	6
Apr-June	85	157	78	13.49	54.0	6
July-Sept	81	156	78	13.70	54.8	8
Oct-Dec	101	153	78	13.65	53.6	8
1984						
Jan-Mar	131	135	62	13.82	54.4	12
Apr-June	138	128	64	14.32	55.7	14
July-Sept	120	122	59	14.41	57.2	17
Oct-Dec	103	124	49	13.61	55.9	19
1985						
Jan-Mar	107	120	47	13.48	56.1	17
Apr-June	105	133	56	12.93	55.1	14
July-Sept	90	127	59	12.79	55.5	14
Oct-Dec	68	144	97	12.70	52.7	10
1986						
Jan-Mar	74	149	80	12.34	50.9	8
Apr-June	65	152	86	11.81	51.1	6
July-Sept	68	146	87	11.31	51.4	6
Oct-Dec	61	153	107	11.06	49.4	3
1987						
Jan-Mar	71	149	118	10.88	48.8	5
Apr-June	75	140	118	10.98	50.5	6
July-Sept	75	136	134	11.22	51.5	7
Oct-Dec	78	142	145	11.22	50.3	5
1988						
Jan-Mar	102	137	143	11.02	50.2	4
Apr-June	113	127	114	11.17	52.1	6
July-Sept	120	115	88	11.61	54.3	8

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.

about 11 percent last year. At the end of September, however, rates on short term loans to farmers had registered a substantial increase, rising about half a percentage point from three months earlier to their highest levels since early 1986. Rates charged on feeder cattle and operating loans were fairly consistent across four of the District states, with Michigan bankers reporting somewhat higher rates of 12 percent on these categories of loans.

The average rate charged on farm real estate loans was up as well. At just over 11 percent, the rate at the end of the third quarter averaged about 40 basis points higher than three months earlier and was the highest rate reported in two years. Among the District states, the average interest rates charged on farm real estate loans by agricultural banks ranged from 10.86 percent in Iowa to 11.50 percent in Michigan.

The strong improvement in loan repayment rates that had been evident in the last seven quarterly surveys slackened during the third quarter, undoubtedly reflecting difficulties for some borrowers hurt by the drought. At 88, the measure of loan repayment rates is based on the 10 percent of respondents that noted improvement compared to a year ago, less the 22 percent of the respondents noting that repayment rates during the third quarter were below the year-earlier level. The remaining 68 percent of the surveyed bankers indicated that repayment rates were at the same level as a year earlier during the summer months.

Iowa banks continued to report better loan repayment rate performance than the other District states. With a measure of 103, it was the only state with a larger proportion of bankers noting a year-to-year improvement in loan repayments than noting a decline. Among the other District states, the measures of loan repayments were all below the District average, ranging from 78 in Illinois to 87 in Michigan. However, a substantial majority of the surveyed bankers in each of the District states reported that loan repayment rates were unchanged from the high level of a year earlier.

The surveyed bankers expect farm loan repayment rates to show further weakness during the fall and winter months. Half of the survey respondents expect the volume of farm loan repayments during this period to be down from a year earlier, while only 11 percent expect to see continued improvement. The remaining 39 percent of the bankers expect no change in the volume of loan repayments over the fall and winter months compared to the same period last year. The expected trend in repayments reflects the bankers' outlook for cash earnings of farmers. About two-thirds of the surveyed bankers expect the net cash earnings of crop and meat animal farmers through the winter to be lower than a year earlier. Only 18 percent of the bankers expect crop farmer earnings to show gains during the period, and only 13 percent expect incomes of cattle and hog producers to be higher than a year ago. The bankers were somewhat less pessimistic regarding the fortunes of dairy farmers, with more than half expecting net earnings to be unchanged from a year ago. However, 36 percent expect dairy earnings during the fall and winter to be lower than a year ago, while only 10 percent expect improvement.

As a result of these trends, many of the bankers expect an increase in liquidations of farm assets. Although about half of the survey respondents expect no change from a year ago, almost a third expect an increase in forced sales and liquidations of farm capital assets through the winter months. The remaining 18 percent of bankers expect fewer liquidations of assets among financially stressed farmers than occurred during the comparable months a year earlier.

During the final months of this year, the volume of lending at District agricultural banks is expected to pickup. More than a third of the survey respondents indicated they expect the volume of nonreal estate lending at their institutions to be be above the level of a year ago, while about 17 percent expected a decline compared to the fourth quarter of 1987. The remainder of the bankers, almost half, expect the volume of farm lending to be unchanged from last year. The apparent strength in nonreal estate lending comes almost entirely from operating loans. Almost 45 percent of the bankers expect the volume to be above last year, while only 13 percent see a decline in the volume of operating loans during the fourth quarter. With regard to feeder cattle, dairy, crop storage, and farm machinery loans, the number of bankers expecting a drop in volume is larger than the number expecting a rise. While more than 56 percent of the bankers expect the volume of farm real estate lending to hold at last year's high level, the remainder are about evenly divided between those expecting an increase and those expecting a decline.

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Selected Agricultural Economic Indicators

	Latest period	Value	Percent change from: Prior period	Year ago	Two years ago
Prices received by farmers *(1977=100)*	October	144	0.0	13	17
Crops *(1977=100)*	October	135	0.0	27	36
Corn *($per bu.)*	October	2.71	4.2	75	94
Oats *($per bu.)*	October	2.44	-4.7	52	120
Soybeans *($per bu.)*	October	7.71	-2.9	53	69
Wheat *($per bu.)*	October	3.89	3.7	48	69
Livestock and products *(1977=100)*	October	153	0.0	4	6
Barrows and gilts *($per cwt.)*	October	40.10	-3.6	-19	-25
Steers and heifers *($per cwt.)*	October	72.80	1.5	8	24
Milk *($per cwt.)*	October	12.80	3.2	-1	-3
Eggs *(¢per doz.)*	October	58.7	-8.0	17	1
Prices paid by farmers *(1977=100)*	October	174	1.2†	5	10
Production items	October	162	1.3†	8	14
Feed	October	142	-3.4†	35	43
Feeder livestock	October	196	8.9†	3	23
Fuels and energy	October	162	-2.4†	-4	8
Producer Prices *(1982=100)*	September	109	-0.2	3	6
Agricultural machinery and equipment	September	113	0.6	3	3
Fertilizer materials	September	98	1.2	9	17
Agricultural chemicals	September	108	0.6	4	5
Consumer prices *(1982-84=100)*	September	120	0.7	4	9
Food	September	120	0.7	5	9
Production or stocks					
Corn stocks *(mil. bu.)*	September 1	4,260	N.A.	-13	5
Soybean stocks *(mil. bu.)*	September 1	303	N.A.	-31	-43
Beef production *(bil. lbs.)*	September	2.04	-5.6	0	0
Pork production *(bil. lbs.)*	September	1.36	6.1	11	20
Milk production *(bil. lbs.)*††	September	9.88	-4.0	2	3

N.A. Not applicable
†Prior period is three months earlier.
††21 selected states.

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