FRB CHICAGO

AGRICULTURAL LETTER

FEDERAL RESERVE BANK OF CHICAGO
May 8, 1987 Number 1707

District credit conditions

Credit conditions at agricultural banks across the seventh District remained largely unchanged during the first three months of the year. The responses of 530 agricultural bankers to a recent survey indicate that funds available for lending to farmers remain in ample supply, but that the demand for loans among farmers remains weak. Despite further declines in the interest rates charged on loans, the bankers reported a continued slide in their average loan-to-deposit ratios. Although difficulties persist for many financially strapped farmers, the bankers' responses suggest that further improvement in farm loan repayment rates occurred during the early months of the year.

The measure of nonreal estate farm loan demand at District agricultural banks, which has shown deterioration since mid 1985, weakened further during the early months of 1987. At 71, the first quarter measure of farm loan demand represents a composite of the 18 percent of the survey respondents noting a pickup in demand less the 47 percent noting declines from the same months last year. The remaining 35 percent of the bankers reported no change from a year ago in the level of farm loan demand at their institutions. The measure of farm loan demand varied considerably across the District states, showing particular weakness in Iowa and relative stability in Michigan and Wisconsin.

The weak farm loan demand is evident in the contraction in farm nonreal estate debt that has taken place. Nonreal estate debt owed by farmers dropped 8 percent last year, with declines reported by all lender groups except the Commodity Credit Corporation (CCC). Excluding the price support loans owed to the CCC, last year's decline in nonreal estate farm debt exceeded 12 percent. Although Farm Credit System lenders recorded the largest year-to-year decline in outstandings, about 24.5 percent, commercial banks saw their outstanding portfolio of nonreal estate farm loans shrink by 12 percent last year. In addition, outstanding nonreal estate loans to farmers from individuals and others also dropped 12 percent last year, while FmHA nonreal estate loans outstanding showed a decline of 2 percent.

The declines in outstandings among these lenders are partially attributable to the growth in CCC loans and the large government payments which have added to the liquidity of farmers. Moreover, efforts by producers to operate more efficiently, and forego large capital expenditures have contributed as well. In addition, lower production costs and acreage cuts have, and will continue to temper loan demand. More stringent lending practices in the face of eroding farm sector equity and cash flow difficulties of financially-stressed farmers have also limited new lending.

Fund availability at agricultural banks has not been a constraining factor on rural financial markets. As has been the case for the last several years, District agricultural banks have an ample supply of funds available for lending to farmers. The first quarter measure of fund availability stood at 149. Only 6 percent of the survey respondents indicated a reduction in fund availability compared to a year earlier, while 55 percent reported an increase. The remaining 39 percent of the surveyed bankers noted that fund availability was unchanged from the previous year's high level during the first three months of 1987. The measure of fund availability remained at a high level in all District states, ranging from 122 among banks in Indiana to 167 among Iowa's agricultural banks.

The prolonged weakness in farm loan demand and the ample supply of funds for lending has contributed to a declining trend in loan-to-deposit ratios at District

Farm debt outstanding[1]

	Amount Outstanding 12/31/86	Percent change from: Year ago	Two years ago	Three years ago
	(---billions---)			
Real estate debt				
Banks	$11.7	12	26	38
Federal Land Banks	35.0	−16	−23	−22
Life Insurance Cos.	10.2	−7	−12	−14
FmHA	9.5	−1	2	8
Individuals and others	23.1	−8	−16	−22
Total	89.4	−8	−13	−14
Nonreal estate debt				
Banks	29.6	−12	−21	−20
Production Credit Assoc.[2]	10.6	−25	−41	−45
Commodity Credit Corp.	19.0	12	118	75
FmHA	14.4	−2	4	12
Individuals and others	13.2	−12	−23	−29
Total	86.8	−8	−9	−12

[1] Excluding operator households.

[2] Includes FICB discounts to other financing institutions.

SOURCE: Federal Reserve Board.

Selected measures of credit conditions at Seventh District agricultural banks

	Loan demand (index)[2]	Fund availability (index)[2]	Loan repayment rates (index)[2]	Average rate on feeder cattle loans[1] (percent)	Average loan-to-deposit ratio[1] (percent)	Banks with loan-to-deposit ratio above desired level[1] (percent of banks)
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
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

[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.

agricultural banks. At the end of the first quarter, loan-to-deposit ratios among the responding banks averaged 48.8 percent, down .6 percentage points from three months earlier and at the lowest level since 1970 when the ratios were first reported quarterly on the survey. The latest decline extends the downtrend from the 1979 peak when loan-to-deposit ratios at District agricultural banks averaged more than 67 percent. As has been the case for the last several surveys, agricultural banks in Illinois and Iowa reported the lowest average ratios, less than 45 percent, while average ratios at agricultural banks in the remaining District states ranged between 55 and 60 percent.

The extended decline has dropped loan-to-deposit ratios well below the levels that District bankers desire. Among the surveyed bankers 78 percent expressed a preference for a higher loan-to-deposit ratio, while fewer than 5 percent indicated that their current ratio was above the desired level. For the District as a whole, the average of the bankers' desired loan-to-deposit ratios, at 58.4 percent, was nearly 10 percentage points above the average of their actual ratios. Among individual District states, the desired level of lending as a proportion of total deposits ranged from an average of just under 55 percent in Illinois and Iowa to almost 67 percent in Michigan.

Interest rates charged on loans to farmers by District agricultural banks declined slightly during the first three months of 1987, recording a tenth consecutive quarterly drop. Average rates charged on feeder cattle and operating loans by the surveyed banks at the end of the period stood at about 10.9 percent, 18 basis points lower than the year-ending 1986 level but almost 150 basis points lower than twelve months earlier. Rates charged on farm real estate loans at the end of March averaged less than 10.3 percent among the respondents. Among the District states, rates on both real estate and nonreal estate loans were lowest in Illinois. Nonreal estate farm loan rates tended to be slightly above the District average in Iowa, while Michigan bankers reported the highest average rate on farm real estate loans.

For the District as a whole, bankers noted further improvement in loan repayment rates during the first three months of 1987. Within the context of the 20 year history of the quarterly surveys of credit conditions, the first quarter measure of loan repayment rates reached an unusually high level of 118. The measure is based on the 32 percent of the responding bankers that cited higher loan repayment rates during the period as contrasted with the 14 percent that noted a decline from a year ago. The remaining 55 percent of the survey respondents reported no change in the rate of loan repayment compared to the first three months of 1986. This was the second consecutive quarter in which the proportion of bankers reporting higher loan repayments exceeded the share noting declines.

Most of the indicated strength in loan repayments stemmed from the responses of Iowa bankers. More than half of the survey respondents in that state noted higher repayment rates than a year ago and only about 3 percent reported a decline, boosting the composite measure of loan repayment rates in Iowa to an extremely high 151. Agricultural bankers in Indiana and Michigan, on the other hand, reported loan repayment rate measures below 100, indicating that more bankers reported year-to-year declines in repayment rates than noted increases. The measures of loan repayment rates reported by Illinois and Wisconsin bankers were near the District average.

The continued improvement in the farm loan repayments across most of the District is likely attributable to a number of factors that have maintained farmers' cash flows. Livestock returns remained favorable through the period, which would contribute significantly to the repayment situation across the District but particularly in Iowa. In addition, heavy use of government price and income support programs by District farmers and the concomitant loan programs and accelerated deficiency payments contributed to the cash flow of participants. The Whole Herd Dairy Buyout Program and the Conservation Acreage Reserve have also injected funds and spurred reductions in outstanding indebtedness.

These same factors will likely continue to dampen loan demand by farmers in the coming months. During the second quarter, nonreal estate farm loan demand is expected to remain weak. Only 14 percent of the bankers expect nonreal estate loan volume to be up from a year earlier, while 45 percent expect a decline in the volume of nonreal estate lending to farmers at their institutions. Farm real estate lending at District agricultural banks, on the other hand, is expected to be relatively strong. About 42 percent of the respondents indicated they expected the volume of farm real estate lending to be higher than last year during the second quarter, compared to about 22 percent expecting a decline. Farm real estate loan volume is expected to be particularly strong compared to last year in Iowa, while Michigan bankers' responses suggest some weakening.

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AGRICULTURAL LETTER (ISSN 0002-1512) is published bi-weekly by the Research Department of the Federal Reserve Bank of Chicago. It is prepared by Gary L. Benjamin, economic adviser and vice-president, Peter J. Heffernan, economist, and members of the Bank's Research Department, and is distributed free of charge by the Bank's Public Information Center. The information used in the preparation of this publication is obtained from sources considered reliable, but its use does not constitute an endorsement of its accuracy or intent by the Federal Reserve Bank of Chicago.

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Selected Agricultural Economic Indicators

	Latest period	Value	Percent change from: Prior period	Year ago	Two years ago
Receipts from farm marketings *($ millions)*	December	15,317	-2.9	0	-1
Crops*	December	7,840	-9.3	-10	4
Livestock	December	5,660	-16.7	1	-4
Government payments	December	1,816	438.9	86	-6
Real estate farm debt outstanding *($ billions)*					
Commercial banks	December 31	12.7	2.2†	11	25
Federal Land Banks	December 31	37.9	-5.0†	-16	-23
Life insurance companies	January 31	10.8	-1.7	-8	-12
Farmers Home Administration	December 31	11.0	-3.7†	-7	-12
Nonreal estate farm debt outstanding *($ billions)*					
Commercial banks	December 31	31.2	-7.3†	-12	-21
Production Credit Associations	December 31	10.7	-11.3†	-24	-40
Farmers Home Administration	December 31	16.4	-6.8†	-2	5
Commodity Credit Corporation	December 31	19.0	20.5†	12	112
Farm loans made *($ millions)*					
Life insurance companies	January	79	-47.2	156	224
Interest rates on farm loans *(percent)*					
7th District agricultural banks					
Operating loans	April 1	10.89	-2.1†	-12	-19
Real estate loans	April 1	10.26	-2.3†	-12	-22
Commodity Credit Corporation	May	6.25	4.2	-4	-33
Agricultural exports *($ millions)*	February	2,221	-0.7	-9	-24
Corn *(mil. bu.)*	February	99	-5.5	-18	-41
Soybeans *(mil. bu.)*	February	74	3.6	-20	2
Wheat *(mil. bu.)*	February	76	-1.0	-2	-18
Farm machinery sales[p] *(units)*					
Tractors, over 40 HP	March	2,907	68.1	-2	-47
40 to 139 HP	March	2,425	69.2	4	-43
140 HP or more	March	482	62.8	-23	-61
Combines	March	76	2.7	-51	-67

*Includes net CCC loans.
†Prior period is three months earlier.
[p]Preliminary

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