FRB CHICAGO

AGRICULTURAL LETTER

FEDERAL RESERVE BANK OF CHICAGO
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## District credit conditions

Credit conditions at District agricultural banks appear to be following recent trends. The responses of 535 agricultural bankers to a recent survey indicate that ample funds are available for lending to farmers, but that farm loan demand remains weak. Interest rates charged on farm loans at the survey institutions, after declining steadily since mid 1984, edged slightly higher during the second quarter, but remain well below year-earlier levels. Farm loan repayment rates continued to improve and the proportion of bankers' farm loan portfolios experiencing significant repayment problems dropped markedly from a year ago.

The measure of nonreal estate farm loan demand at District agricultural banks remained weak during the second quarter, continuing the trend of the last two years. At 75, the second quarter measure of farm loan demand represents a composite of the 15 percent of the survey respondents noting an increase in demand compared to a year ago less the 40 percent noting a decline. The remaining 45 percent of the respondents noted no change from a year ago in the level of farm loan demand at their banks. The measure of farm loan demand varied considerably across the District states, showing particular weakness in Iowa and relative stability in Indiana.

The weak farm loan demand evident in the survey responses is consistent with the overall drop in farm debt that has occurred over the last few years. Much of the decline in commercial debt outstanding is attributable to the growth in Commodity Credit Corporation loans and government income support payments, which have added to the liquidity of farmers. Producers' streamlining of their operations and reducing capital expenditures have contributed to the decline as well. In addition, large acreage cutbacks and lower production costs have dampened farm operating loan demand.

Fund availability at District agricultural banks is not a constraint on rural credit flows. As has been the case for the last several years, District agricultural bankers reported an ample supply of funds available for lending to farmers. The second quarter measure of fund availability, at 140, was down slightly from the very high levels reported in the last several surveys, but continues to indicate that adequate funding is available. Reflecting this, less than 7 percent of the respondents noted a reduction in fund availability compared to a year ago, while 47 percent reported an increase. The remaining 46 percent of the bankers noted that fund availability was unchanged from the previous year's high level during the second quarter. The measure of fund availability remained high across all District states, ranging from 126 among banks in Michigan to 155 among Iowa's agricultural banks.

While loan demand is still regarded to be weak in the face of ample funds, loan-to-deposit ratios did record a notable increase in the second quarter. As of midyear, loan-to-deposit ratios among the responding banks averaged 50.5 percent, up from 48.8 percent three months earlier but still well below historical levels. In 1979, loan-to-deposit ratios at District agricultural banks averaged 67 percent, but have trended down since that time. As has been the case for the last several surveys, agricultural banks in Illinois and Iowa reported the lowest average ratios, less than 46 percent, while the average of the ratios of Michigan banks approached 62 percent.

The extended decline has dropped loan-to-deposit ratios well below the levels that District bankers would prefer. Among the survey respondents, 77 percent expressed a preference for a higher loan-to-deposit ratio, while only 6 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 59.6, was more than 9 percentage points higher than 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 56 percent in Illinois and Iowa to almost 68 percent in Michigan.

Interest rates charged on loans to farmers by District agricultural banks edged slightly higher during the second quarter, interrupting the steady downturn reported in the 10 previous quarterly surveys. Average rates on feeder cattle loans and operating loans among the surveyed bankers stood at about 11 percent at the end of the second quarter, about 10 basis points higher than three months earlier. Rates charged by surveyed banks on farm real estate loans at the end of June averaged slightly less than 10.5 percent, indicating an increase of almost 20 basis points from three months earlier.

## 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 |
| Apr-Jun | 75 | 140 | 118 | 10.98 | 50.5 | 6 |

[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.

Surveyed bankers noted continued improvement on farm loan repayment rates during the second quarter. At 118, the measure of loan repayment rates is a composite of the 26 percent of the respondents that cited higher loan repayment rates during the period less the 8 percent that noted a decline from the same period last year. The remaining 65 percent of the survey respondents reported no change in the rate of loan repayment compared to the second quarter of 1986. This marked the third consecutive quarterly survey in which the proportion of bankers reporting higher loan repayments exceeded the proportion noting declines.

Much of the indicated strength in loan repayments was accounted for by significant improvement among

Iowa banks. Higher repayment rates compared to a year earlier were reported by 46 percent of the respondents from that state and only 2 percent noted a decline, boosting the composite measure of loan repayment rates in Iowa to 144. In contrast, responses of agricultural bankers in Michigan—where weather problems sharply lowered last fall's harvest—indicated that almost 20 percent reported year-to-year declines in repayments and only 5 percent noted improvement. Loan repayment rate measures among the remaining District states were all above 100, indicating a larger number of bankers noting increases than noting declines.

Reflecting the improvement in loan repayment rates, bankers reported that a declining proportion of their farm loan portfolios were experiencing difficulties. Across the District, an average of 3 percent of the bankers' portfolios were characterized as experiencing severe repayment difficulties. These loans are expected to result in some losses to the bank or require forced sales of borrowers' assets. However, the proportion of the farm loan portfolios falling into this category is down sharply from the year-ago level of 6 percent. Declines were registered in all of the District states, with only Michigan bankers reporting an above average 4 percent of their portfolios with severe repayment problems.

In addition to the improvement shown in the most stressed proportion of the farm loan portfolios, a drop in the average of the respondents' portfolios experiencing less severe but still major problems was reported as well. Farm loans requiring additional collateral or long term workouts, on average, accounted for about 7 percent of the surveyed bankers' portfolios, down from 12 percent a year earlier. Across the District, farm loans falling into the major repayment problem category ranged from an average of less than 6 percent of the banker's portfolios in Indiana and Wisconsin to almost 9 percent in Michigan.

As a result of these improving trends, the average proportion of farm loans at the responding agricultural banks with little or no repayment problems jumped to 90 percent compared to 82 percent a year earlier. The average proportion of farm loans falling into this category ranged from 87 percent in Michigan to 92 percent in Indiana and Wisconsin.

The improvement in farm loan repayment rates and the condition of the banks' farm loan portfolios stems from a number of factors. Returns to livestock producers improved greatly last year and remained strong through the first half of this year. The Whole Herd Dairy Buyout Program and the Conservation Acreage Reserve have improved the cash flow of participants and facilitated the restructuring of operations. In addition, price support loans and deficiency payments have provided a large supply of funds for farmers participating in the programs. Together, these factors have allowed for a sharp reduction in outstanding debt and reduced the demand for new financing from banks and other lenders.

Given these trends, credit demand at District agricultural banks during the third quarter is expected to remain weak. Only a tenth of the surveyed respondents expect the volume of nonreal estate lending at their institutions to be above a year ago, while 37 percent expect further declines. Demand for dairy, crop storage, farm machinery, and operating loans are expected to be particularly weak. A sharply higher volume of feeder cattle loans, however, is expected by Iowa banks. Farm real estate lending across the District is expected to remain relatively strong during the third quarter. About 28 percent of the bankers expect farm real estate lending to be up from a year ago, while 52 percent expect no change. Only a fifth of the bankers expect year-to-year declines in farm real estate lending at their institutions. The expected strength in farm real estate loan demand is consistent with the recently expanded role banks have played in financing farm real estate transfers, particularly in the Corn Belt.

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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)* | July | 128 | -2.3 | 2 | 2 |
| Crops *(1977=100)* | July | 106 | -4.5 | 0 | -12 |
| Corn *($per bu.)* | July | 1.59 | -5.9 | -21 | -39 |
| Oats *($per bu.)* | July | 1.35 | -10.6 | 49 | 3 |
| Soybeans *($per bu.)* | July | 5.20 | -3.0 | 2 | -4 |
| Wheat *($per bu.)* | July | 2.30 | -6.1 | 2 | -21 |
| Livestock and products *(1977=100)* | July | 150 | 0.0 | 5 | 15 |
| Barrows and gilts *($per cwt.)* | July | 61.00 | -1.0 | 1 | 30 |
| Steers and heifers *($per cwt.)* | July | 66.60 | -0.9 | 18 | 25 |
| Milk *($per cwt.)* | July | 11.90 | 0.0 | -1 | -2 |
| Eggs *(¢per doz.)* | July | 51.4 | 1.0 | -13 | -3 |
| **Prices paid by farmers** *(1977=100)* | July | 164 | 1.2† | 3 | 1 |
| Production items | July | 149 | 1.4† | 3 | -1 |
| Feed | July | 105 | 4.0† | -2 | -9 |
| Feeder livestock | July | 182 | 1.7† | 18 | 24 |
| Fuels and energy | July | 170 | 3.7† | 12 | -17 |
| **Producer Prices** *(1967=100)* | | | | | |
| Agricultural machinery and equipment | July | 298 | 0.3 | 4 | 1 |
| Fertilizer materials | July | 342 | 0.0 | 0 | 1 |
| Agricultural chemicals | July | 217 | 0.2 | 4 | -5 |
| | July | 479 | 0.1 | 0 | 5 |
| **Consumer prices** *(1967=100)* | June | 340 | 0.4 | 4 | 6 |
| Food | June | 334 | 0.5 | 5 | 8 |
| **Production or stocks** | | | | | |
| Corn stocks *(mil. bu.)* | June 1 | 6,332 | N.A. | 27 | 123 |
| Soybean stocks *(mil. bu.)* | June 1 | 865 | N.A. | 2 | 42 |
| Beef production *(bil. lbs.)* | June | 1.96 | 5.8 | -3 | 3 |
| Pork production *(bil. lbs.)* | June | 1.09 | 1.5 | 2 | -3 |
| Milk production *(bil. lbs.)*†† | June | 10.5 | -4.3 | -1 | -1 |

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


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