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THE ROLE OF BANKS IN FINANCING AGRICULTURE

By ...

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BANKS HAVE BEEN, ARE NOW, AND PROBABLY WILL CONTINUE TO BE, A MAJOR ELEMENT IN THE FINANCING OF AGRICULTURE. THEIR COMMITMENT TO FINANCE AGRICULTURE HAS REMAINED CONSTANT OVER THE YEARS EVEN THOUGH FUNDS HAVE BEEN TIGHT AT VARIOUS TIMES. AS A MATTER OF FACT, THE RELATIVE AMOUNT OF FARM LOANS MADE BY BANKS HAS INCREASED OVER TIME. IN 1940 THEY PROVIDED ABOUT 15 PERCENT OF THE APPROXIMATELY 9.6 BILLION DOLLARS OF TOTAL OUTSTANDING FARM DEBT (EXCLUDING CCC LOANS). BY 1948 THEY PROVIDED 26 PERCENT AND IN 1972 AND EACH OF THE SUCCEEDING YEARS THEY ACCOUNTED FOR MORE THAN 29 PERCENT OF THE GREATLY INCREASED TOTAL.

THE TREND IN TOTAL FARM DEBT SINCE 1940 IS INTERESTING. IT WAS APPROXIMATELY 9.6 BILLION DOLLARS IN THAT YEAR. THE TOTAL INCREASED ONLY 1.1 BILLION IN THE NEXT DECADE, BUT THEN IT TOOK OFF LIKE A SHOT. IT DOUBLED IN THE FIFTIES, MORE THAN DOUBLED AGAIN IN THE SIXTIES, AND IN THE FIRST EIGHT YEARS OF THIS DECADE HAS INCREASED BY ANOTHER 130 PERCENT. ON JANUARY 1, 1978, TOTAL FARM DEBT OUTSTANDING, EXCLUDING CCC LOANS, WAS 12 TIMES ITS SIZE IN 1940, OR \$115.2 BILLION. OF THIS TOTAL, BANKS SUPPLIED 29.1 PERCENT (OR \$33.5 BILLION), THE FARM CREDIT SYSTEM 30.7 PERCENT, THE FARMERS HOME ADMINISTRATION 6.2 PERCENT, AND LIFE INSURANCE COMPANIES 7.6 PERCENT. INDIVIDUALS AND OTHERS SUPPLIED THE REMAINING 26.5 PERCENT.

OVER THE PERIOD SINCE 1940 NON-REAL ESTATE FARM DEBT HAS INCREASED MORE RAPIDLY THAN REAL ESTATE FARM DEBT. BANKS HAVE BEEN THE MAJOR SOURCE OF SUCH FUNDS. THEY SUPPLIED 30 PERCENT OF THE \$3.0 BILLION OUTSTANDING NON-REAL ESTATE DEBT IN 1940. THIS PERCENTAGE INCREASED STEADILY UNTIL 1970. BANKS HAVE SUPPLIED MORE THAN 50 PERCENT OF THE NON-REAL ESTATE FARM LOANS IN 1972 AND LATER YEARS. THE ALABAMA BANK PERCENTAGES ARE HIGHER.

AS YOU MIGHT EXPECT, BANKS HAVE NOT BEEN AS IMPORTANT A SOURCE OF FUNDS FOR FARM REAL ESTATE LOANS, BUT THEY ALWAYS HAVE BEEN A SIGNIFICANT FACTOR IN THAT FIELD TOO. IN 1940, THEY PROVIDED 8.1 PERCENT OF THE APPROXIMATELY \$6.5 BILLION DOLLARS IN FARM REAL ESTATE DEBT. AND SINCE 1947 THE PERCENTAGES HAVE REMAINED RELATIVELY CONSTANT AROUND 12 PERCENT AS FARM REAL ESTATE DEBT GREW TO \$64.2 BILLION IN 1978. AGAIN, AS YOU MIGHT EXPECT, THE FARM CREDIT SYSTEM HAS BEEN THE MAJOR SOURCE OF FARM REAL ESTATE FUNDS, ACCOUNTING FOR 33.4 PERCENT IN 1978. "INDIVIDUALS AND OTHERS" SUPPLIED A SLIGHTLY LARGER AMOUNT. INTERESTINGLY, THE COMMERCIAL BANKS IN ALABAMA SUPPLIED 23.3 PERCENT OF THE TOTAL FARM REAL ESTATE DEBT (\$191.6 MILLION OUT OF \$824.0 MILLION), WHICH WAS ALMOST DOUBLE THE NATIONAL AVERAGE. THE FOUR SOUTHEASTERN STATES, INCLUDING ALABAMA, SUPPLIED ABOUT A THIRD MORE THAN THE AVERAGE FOR THE FIFTY STATES.

FIGURES ON LOANS MADE DIRECTLY TO FARM INTERESTS BY BANKS TELL ONLY PART OF THE STORY, OF COURSE. THE U.S. TREASURY REGULARLY SURVEYS A GROUP OF APPROXIMATELY 6,000 COMMERCIAL AND MUTUAL SAVINGS BANKS (OUT OF A TOTAL OF APPROXIMATELY 15,000) TO DETERMINE THE OWNERSHIP OF TREASURY OBLIGATIONS AND THE DEBT OF FEDERAL AGENCIES. ON APRIL 30, 1978 BANKS HELD A TOTAL OF APPROXIMATELY \$10 BILLION IN SECURITIES ISSUED BY THESE AGENCIES; THUS BANKS SUPPLIED ALMOST ONE-FOURTH OF THE FUNDS RAISED IN THE CREDIT MARKET BY THE CONSTITUENT ELEMENTS OF THE FARM CREDIT SYSTEM AND THE FARMERS HOME ADMINISTRATION. THUS, BANKS, DIRECTLY OR INDIRECTLY, SUPPLIED 3/8'S OF THE TOTAL FARM DEBT OUTSTANDING AS OF JANUARY 1, 1978.

THERE IS NO STEREOTYPED AGRICULTURAL BANK--THEY COME IN ALL SIZES AND SHAPES, JUST LIKE PEOPLE. ALMOST ALL BANKS MAKE SOME AGRICULTURAL LOANS. SOME OF COURSE MAKE ONLY A FEW, BUT IN MANY BANKS FARM LOANS ARE THE LARGEST CATEGORY IN THE LOAN PORTFOLIO. THOSE WITH THE LARGER PERCENTAGES OF FARM LOANS IN THEIR PORTFOLIO USUALLY ARE SMALLER BANKS FOR BANKS IN THE AGRICULTURAL AREAS OF THE COUNTRY USUALLY ARE SMALLER THAN THOSE IN THE MAJOR CITIES. APPROXIMATELY 73 PERCENT OF THE COMMERCIAL BANKS IN THE UNITED STATES EACH HAD TOTAL RESOURCES OF 25 MILLION DOLLARS OR LESS ON JANUARY 1, 1977. THESE BANKS HELD 16 PERCENT

OF THE TOTAL DEPOSITS IN ALL BANKS, BUT THEY MADE 51 PERCENT OF THE FARM LOANS BY DOLLAR AMOUNT. OVER TWO-THIRDS OF THE FARM LOANS WERE MADE BY BANKS WITH DEPOSITS OF LESS THAN \$50 MILLION AND ALMOST THREE-FOURTHS WERE MADE BY THOSE WITH DEPOSITS OF LESS THAN 100 MILLION.

SMALLER BANKS AS A GROUP TYPICALLY MADE MORE SHORT- AND INTERMEDIATE-TERM LOANS AND FEWER FARM REAL ESTATE LOANS THAN DID THE LARGER BANKS. THE GROUP HAVING UNDER \$25 MILLION IN DEPOSITS HAD 53 PERCENT OF THE SHORT- AND INTERMEDIATE-TERM LOANS AND ONLY 43 PERCENT OF THE REAL ESTATE LOANS HELD BY BANKS. THE LARGEST BANKS, THOSE WITH TOTAL DEPOSITS OF OVER \$100 MILLION, HAD 24 PERCENT OF THE PRODUCTION AND EQUIPMENT LOANS HELD BY BANKS AS A WHOLE AND 53 PERCENT OF THE REAL ESTATE LOANS. THE ROLE OF THE LARGER BANKS IS NOT COMPLETELY DISCLOSED BY THESE PERCENTAGES, HOWEVER, FOR THEY ARE THE SAFETY VALVE AND ASSIST THE SMALLER BANKS BY TAKING PARTICIPATIONS IN THEIR LARGE LOANS AT ANY TIME AND IN OTHER LOANS AT THE PEAK OF THE LENDING SEASON WHEN THE RURAL BANKS DO NOT HAVE ENOUGH FUNDS TO FINANCE THE HARVESTING AND MOVING OF CROPS.

DATA FOR THE SOUTH, ONE OF THE FIVE AGRICULTURAL REGIONS IN THE UNITED STATES, SHOW EQUALLY STRONG SUPPORT FOR AGRICULTURE THERE. BANKS WITH DEPOSITS UNDER \$25 MILLION CONSTITUTED APPROXIMATELY 72 PERCENT OF ALL BANKS IN THE REGION AND HELD ABOUT

ONE-FOURTH OF THE TOTAL BANK DEPOSITS. THESE "MIGHTY MITES", HOWEVER, HELD 54 PERCENT OF THE NON-REAL ESTATE FARM LOANS, 52 PERCENT OF THE REAL ESTATE FARM LOANS, OR 53 PERCENT OF ALL OUTSTANDING FARM DEBT IN THE REGION THE FIRST OF LAST YEAR.

HAVE WE DOCUMENTED THE STATEMENT THAT BANKS HAVE BEEN, ARE NOW, AND PROSPECTIVELY WILL BE A MAJOR SOURCE OF FUNDS FOR FARMERS? IF SO, LET US MOVE ON TO THE CURRENT AND THE PROSPECTIVE AGRICULTURAL LOAN SITUATION AS FAR AS BANKS ARE CONCERNED. THAT PROBABLY IS OF MORE INTEREST TO YOU. I WOULD CHARACTERIZE THE CURRENT SITUATION AS STILL BEING TIGHT, BUT BETTER THAN IT WAS LAST YEAR, WITH SOME IMPROVEMENT IN THE SITUATION STILL TO COME. MOST FARMERS HAVE BEEN ABLE TO GET CREDIT AS SHOWN BY A 12 STATE SURVEY MADE IN MARCH 1978 BY THE ECONOMICS, STATISTICS, AND COOPERATIVES SERVICE OF THE U.S. DEPARTMENT OF AGRICULTURE. THE SURVEY COVERED OVER 5,300 BANKS IN GEORGIA AND 11 MIDWESTERN STATES. MANY OF THE ANSWERS IN THE SURVEY MAY BE CHARACTERIZED IN THE FORM OF "ON THE ONE HAND--BUT ON THE OTHER HAND--". LOANS IN THE BANKS COVERED BY THE SURVEY AVERAGED 61 PERCENT OF THEIR TOTAL DEPOSITS, WHICH MAY BE A LITTLE HIGH. THIRTY-NINE PERCENT OF THEM SAID THAT THE LOANS ON JANUARY 1, 1978 WERE ABOVE THE DESIRED LEVEL, BUT ON THE OTHER HAND 41 PERCENT SAID THAT THEIR LOANS WERE BELOW THE DESIRED LEVEL. AS FAR AS THE QUALITY OF THE BANK LOAN PORTFOLIO IS CONCERNED, 24 PERCENT INDICATED

THAT THE QUALITY OF THE PORTFOLIO HAD DECREASED IN THE LAST YEAR OR TWO BUT 26 PERCENT BELIEVED THE QUALITY HAD INCREASED. THE COMPARISON OF THE QUALITY OF FARM LOANS TO OTHER LOANS IN THE PORTFOLIO IS QUITE INTERESTING. TWENTY-FIVE PERCENT OF THE BANKS REPLYING INDICATED THAT THEY THOUGHT THEIR FARM LOAN PORTFOLIO WAS OF BETTER QUALITY THAN THE OVERALL LOAN PORTFOLIO OF THE BANK, AND ONLY 13 PERCENT THOUGHT THAT THE FARM LOANS WERE OF POORER QUALITY. THAT LEFT 62 PERCENT THAT THOUGHT THAT THE QUALITY OF THE FARM LOANS WAS ABOUT THE SAME AS THAT OF OTHER TYPES OF LOANS IN THEIR PORTFOLIO.

THE SURVEY SUBSTANTIATED THE FACT THAT THE AGRICULTURAL LOAN SITUATION IS TIGHTER THAN NORMAL. BANKS PARTICIPATING IN IT INDICATED THAT THERE WAS SOME INCREASE IN THE PERCENTAGE OF FARM LOAN APPLICATIONS NOT QUALIFYING FOR ADDITIONAL LOANS IN 1978. ABOUT 3 PERCENT OF THE APPLICATIONS FROM LAST YEAR'S BORROWERS DID NOT QUALIFY THIS YEAR WHEREAS THE NORMAL PERCENTAGE WAS APPROXIMATELY ONE PERCENT. THEY ALSO INDICATED THAT SIX PERCENT OF CURRENT BORROWERS COULD NOT OBTAIN ADDITIONAL FUNDS BECAUSE THEY HAD BORROWED UP TO THE LIMIT. THE SIX PERCENT FIGURE IS EXACTLY DOUBLE THE NORMAL THREE PERCENT FOR THIS CATEGORY.

THESE FIGURES WOULD HAVE BEEN MORE SERIOUS IF INCREASES IN FARM LAND VALUES HAD NOT CREATED ADDITIONAL EQUITY FOR FARMERS. THIS ENABLED A LARGER NUMBER THAN USUAL (7 PERCENT VERSUS 2 PERCENT)

TO REDUCE SHORT-TERM LIABILITIES BY REFINANCING THROUGH ADDITIONAL BORROWING ON FARM REAL ESTATE. SIMILAR CONCLUSIONS, WITHOUT ANY NUMBERS, WERE REACHED BY MEMBERS OF THE EXECUTIVE COMMITTEE OF THE AGRICULTURAL BANKERS DIVISION OF THE AMERICAN BANKERS ASSOCIATION AT A MEETING THIS SUMMER.

WE SHOULD EMPHASIZE ALSO THAT THE CURRENT SITUATION WOULD BE SIGNIFICANTLY WORSE IF IT WERE NOT FOR THE LOANS MADE BY THE FARMERS HOME ADMINISTRATION AND THE SMALL BUSINESS ADMINISTRATION TO CUSHION THE EFFECTS OF DROUGHT, FLOODS AND OTHER NATURAL DISASTERS. THEY ALSO HAVE MADE LOANS TO FARMERS WHOSE FINANCIAL CONDITION DID NOT QUALIFY FOR FURTHER BANK LOANS.

THE LATEST QUARTERLY SURVEYS OF AGRICULTURAL CREDIT CONDITIONS IN FIVE FEDERAL RESERVE BANK DISTRICTS ALSO INDICATE THAT THE CURRENT SITUATION IS TIGHTER THAN USUAL BUT THAT IT IS NOT DESPERATE. THE PERCENTAGE OF BANKS REPORTING SLOWER FARM LOAN PAYMENTS AT THE END OF 1977 RANGED FROM 55 PERCENT IN ONE OF THE DISTRICTS TO 70 PERCENT IN ONE OF THE OTHERS, BUT THIS REPRESENTS AN IMPROVEMENT OF SOMETHING BETWEEN 5 AND 10 PERCENT OVER THE SITUATION THAT EXISTED AT THE FIRST OF THE YEAR. INTERESTINGLY ENOUGH, ABOUT 40 PERCENT OF THE BANKS REPLYING SAID THAT THEIR RATIO OF LOANS TO TOTAL DEPOSITS WAS HIGHER THAN DESIRED.

THIS IS APPROXIMATELY THE SAME AS THE 30 PERCENT REPORTED IN THE SURVEY BY THE ECONOMICS, STATISTICS AND COOPERATIVES SERVICE OF THE U.S.D.A. ONE FINAL FIGURE ON THIS SAME SUBJECT: THERE ARE APPROXIMATELY 5,000 BANKS IN THE COUNTRY IN WHICH AGRICULTURAL LOANS CONSTITUTE 25 PERCENT OR MORE OF THE TOTAL LOANS IN THE BANK. THESE 5,000 BANKS ACCOUNT FOR MORE THAN ONE-HALF OF ALL THE FARM LOANS MADE BY BANKS. OUT OF THIS SAMPLE OF 5,000, ABOUT 3/8'S OF THE BANKS HAD A LOAN TO DEPOSIT RATIO ABOVE 70 PERCENT IN MID-1977 BUT THIS HAD DROPPED TO ABOUT 1/4 BY THE END OF THE YEAR.

NOW LET'S GET OUT THE CRYSTAL BALL AND SEE WHAT IT TELLS US ABOUT THE PROBABLE FUTURE COURSE OF AGRICULTURAL CREDIT. THE STARTING POINT IS OUR CURRENT SITUATION WHICH WE'VE CHARACTERIZED AS BEING TIGHTER THAN USUAL BUT IMPROVING. THE IMPROVEMENTS RESULT FROM INCREASES IN PRODUCTION AND PRICES IN THE AGRICULTURAL SECTOR, INCREASES IN DEPOSITS OF BANKS, FROM CORRESPONDENT AND OUTSIDE BANKS TAKING OVER PART OF THE LARGE LOAN TOTALS, AND ESPECIALLY FROM THE EMERGENCY AND OTHER PROGRAMS REPRESENTED BY OTHER GOVERNMENTAL PARTICIPANTS ON THIS PANEL. THE PROBABLE FUTURE FARM CREDIT SITUATION WILL BE INFLUENCED STRONGLY BY THE GENERAL AGRICULTURAL CONDITIONS IN THE BALANCE OF THIS AND NEXT YEAR, THE GENERAL ECONOMIC CONDITIONS THROUGHOUT THE NATION, THE INTERNATIONAL TRADE SITUATION OF THE UNITED STATES, AND THE INTERNATIONAL ECONOMIC

CONDITIONS. I WON'T TRY TO DISCUSS THESE BROAD, IMPORTANT ASPECTS, BUT I BELIEVE THAT IN GENERAL THERE SHOULD BE SUFFICIENT CREDIT AVAILABLE FOR BANKS TO CONTINUE TO PROVIDE APPROXIMATELY 30 PERCENT OF THE TOTAL AMOUNT OF OUTSTANDING FARM INDEBTEDNESS. WHAT HAPPENS TO THE INDIVIDUAL FARMER CAN BE A DIFFERENT QUESTION, OF COURSE. WHETHER YOU OR ANY OTHER FARMER WILL BE ABLE TO BORROW FROM YOUR NORMAL BANK SOURCES WILL DEPEND UPON YOUR OWN INDIVIDUAL FINANCIAL CONDITION. ANALYZING THIS INVOLVES A STUDY OF THE NATURE OF AND RELATIONSHIP OF ASSETS AND LIABILITIES ON YOUR BALANCE SHEET, YOUR NEEDS FOR ADDITIONAL CAPITAL FUNDS IN ADDITION TO OPERATING MONEY, YOUR NET INCOME OVER THE PAST FEW YEARS AND ANY CHANGES IN THAT PROSPECTIVE INCOME IN THE NEXT YEAR OR TWO. THE BANKS SHOULD HAVE THE FUNDS AND ARE INTERESTED IN LENDING TO GOOD PRODUCERS SO THE GREAT MAJORITY OF THE ENERGETIC, CAPABLE FARMERS SHOULD HAVE NO DIFFICULTY IN OBTAINING BANK CREDIT FOR THE BALANCE OF THIS YEAR AND NEXT YEAR.

ON THE WHOLE, BANKS ARE MORE INTERESTED IN MAKING SHORT-TERM CROP AND LIVESTOCK LOANS AND INTERMEDIATE-TERM EQUIPMENT AND LIVESTOCK LOANS THAN THEY ARE LONGER-TERM REAL ESTATE LOANS, BUT THEY ARE AND WILL CONTINUE TO BE INTERESTED IN SOME REAL ESTATE LOANS. THIS IS EVIDENCED BY THE FACT THAT AT THE BEGINNING OF THIS YEAR THEY WERE HOLDING APPROXIMATELY 7.8 BILLION DOLLARS IN FARM REAL ESTATE LOANS, OVER 12 PERCENT OF THE TOTAL OF SUCH LOANS OUTSTANDING IN THE UNITED STATES.

WHAT CAN YOU DO TO HELP ASSURE AN ADEQUATE LINE OF BANK CREDIT FOR YOURSELF IN PARTICULAR AND FOR YOUR FARMER FRIENDS IN GENERAL? FIRST AND MOST IMPORTANT, YOU CAN MANAGE YOUR OWN AFFAIRS PROFITABLY AND WELL. SECONDLY, KEEP YOUR BANKER FULLY INFORMED ABOUT YOUR CURRENT FINANCIAL SITUATION AND YOUR INCOME PROSPECTS. AND, DON'T LET A LOAN REMAIN PAST DUE EVEN IF YOU CAN'T PAY THE PRINCIPAL. THIRDLY, HELP YOUR BANKER OBTAIN THE FUNDS HE NEEDS TO MEET HIS LOAN DEMANDS. THAT MAY MEAN THE REMOVAL OF CEILINGS OR LIMITS ON THE INTEREST HE CAN PAY TO DEPOSITORS IN ORDER TO ATTRACT TIME AND SAVINGS ACCOUNTS. CONVERSELY, IT ALSO MAY MEAN THE REMOVAL OF CEILINGS ON THE INTEREST HE CAN CHARGE ON LOANS MADE BY HIM SO HE CAN EARN ENOUGH TO PAY THAT HIGHER RATE ON DEPOSITS. FINALLY, LET YOUR LEGISLATORS KNOW THAT LOANS FOR AGRICULTURAL PRODUCTION ARE AS IMPORTANT TO THE WELL-BEING OF THE AMERICAN PUBLIC AS ARE RESIDENTIAL LOANS OR OTHER TYPES TO WHICH SPECIAL PROVISIONS SOMETIMES APPLY.

THE BANKER HAS HIS OWN RESPONSIBILITIES TO FULFILL IN RETURN FOR WHAT YOU ARE DOING FOR HIM. HE MUST EXPECT TO COMPETE FOR FUNDS AND FOR LOANS IN THE OPEN MARKET WITHOUT GEOGRAPHIC OR STATUTORY PROTECTION FROM OTHER COMPETITORS. HE MUST KNOW THE CHANGING AGRICULTURAL TECHNOLOGY AND THE CREDIT NEEDS OF FARMERS. HE MUST PROVIDE A STABLE, CONTINUING SOURCE OF AGRICULTURAL LOANS-- NOT AN "ON AGAIN OFF AGAIN" SUPPLY AS MONEY MARKET RATES FLUCTUATE

UNDER TEMPORARY, SHORT-TERM INFLUENCES--AND IF HE DOES YOU SHOULD STICK WITH HIM THE SAME WAY THROUGH TEMPORARY FLUCTUATIONS IN RATES FOR YOUR DEPOSITS. AND, HE MUST CONTINUE TO NURTURE THE ECONOMY OF YOUR LOCAL COMMUNITY, INCLUDING THE AGRI-BUSINESS PART OF IT.

IN SUMMARY, WE MAY NOT BE ABLE TO REPEAT THE "FOUR BELLS AND ALL'S WELL" OF THE WATCH ON A SHIP, BUT I BELIEVE THAT WE CAN SAY WITH CONFIDENCE THAT THE AGRICULTURAL LOAN SITUATION OVERALL IS MANAGEABLE AND IS IMPROVING, AT LEAST AS FAR AS BANKS ARE CONCERNED, ALTHOUGH IT IS A BIT TIGHTER THAN NORMAL. THE BANKS SHOULD HAVE LOAN FUNDS AVAILABLE TO TAKE CARE OF THE CAPABLE FARMERS WHO HAVE BEEN BORROWING FROM THEM AND TO FINANCE THEM THROUGH THE BALANCE OF THIS YEAR AND NEXT YEAR WITHOUT UNDUE STRAIN EITHER ON THE FARMERS OR ON THE BANKS THEMSELVES.