

DALLAS FED

AGRICULTURAL HIGHLIGHTS

Federal Reserve Bank of Dallas

November 1987

Localized Problems Pull Down Loan Quality at District Agricultural Banks

Although nonperforming loans as a percentage of all loans at agricultural banks in the Eleventh Federal Reserve District continue to increase, the problems are largely confined to areas of West Texas.¹ The nonperformance rate is actually going down at District agricultural banks outside those areas, which matches the experience of agricultural banks outside the District. Within the banking system, the concentration of local economic disturbances is one problem that could be avoided with statewide branching.

Nonperformance Rate Down Outside District

At agricultural banks outside the Eleventh District, the proportion of all loans that are nonperforming declined to 4.13 percent during the second quarter of 1987, compared with 5.27 percent in the second quarter of 1986 (Chart 1). At the same time, the nonperformance rate on just *farm* loans at these banks fell to 5.68 percent, compared with 7.85 percent a year earlier. (The nonperformance rate of nonfarm loans also fell.) These improvements in loan quality reflect not only increased government farm payments and increased livestock profit margins but also the renewed health of the local economies.

District Nonperformance Rate Rises

In contrast to the improved loan quality at the agricultural banks outside the District, average loan quality at agricultural banks in the District has deteriorated. The nonperformance rate

at these banks was 4.23 percent in the second quarter of 1987, up from 3.99 percent in the second quarter of 1986. As of mid-1987, the nonperformance rate at District agricultural banks exceeded that for agricultural banks in the rest of the nation. The increase in the District nonperformance rate, however, does not reflect general agricultural conditions in the District.

The rise in the District nonperformance rate resulted from a sharp deterioration in loan quality at agricultural banks in the Texas Southern Plains (roughly the area around Lubbock and eastward toward Abilene). Many farmers there became financially stressed when poorly timed rains, low temperatures, and hail reduced the

area's cotton production 46 percent from 1985 to 1986. As a consequence, the nonperformance rate for Southern Plains agricultural banks rose to 6.04 percent in the second quarter of this year, up from 4.61 percent in the second quarter of 1986. In stark contrast, the nonperformance rate at District agricultural banks outside the Southern Plains fell to 3.55 percent, down from 3.78 percent a year earlier. In fact, these banks had a lower nonperformance rate than did agricultural banks outside the District.

Geographical Concentration Harmful

The recent experience of the Southern Plains agricultural banks ill-

(Continued on back page)

Agriculture Can No Longer Bail Out the Merchandise Trade Account

During some years in the 1970s, agricultural trade surpluses more than offset nonagricultural merchandise trade deficits. Even as late as the early 1980s, agricultural trade surpluses had the effect of reducing total merchandise trade deficits by almost half. In the current marketing year, however, shrunken agricultural trade surpluses will count for little compared with the swollen nonagricultural trade deficits.

Agriculture's Importance to Total U.S. Trade Declining

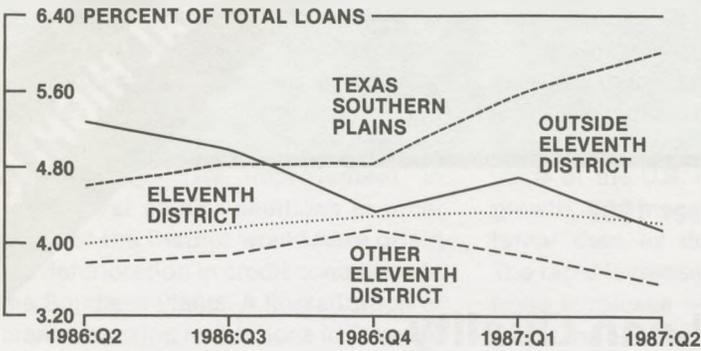
Agriculture's share of U.S. trade has been declining for most of this century (Chart 2). In 1930, agricultural products

constituted almost half of U.S. merchandise imports and nearly a third of U.S. merchandise exports. Yet by the mid-1980s, agricultural exports made up only 15 percent of merchandise exports, while agricultural imports were less than 6 percent of merchandise imports. This outcome can be explained by the large growth of world and U.S. income since 1930 and the fact that the demand for agricultural products increases only modestly when income rises.

Since the Civil War, the United States generally has been a net exporter of agricultural products. Simi-

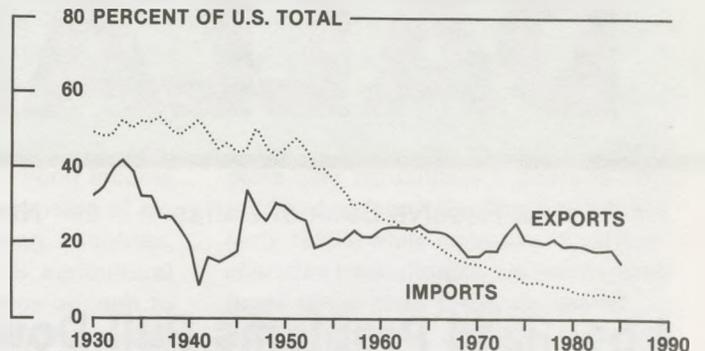
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Chart 1
NONPERFORMANCE RATE OF LOANS
AT AGRICULTURAL BANKS



SOURCES: Board of Governors, Federal Reserve System.
 Federal Reserve Bank of Dallas.

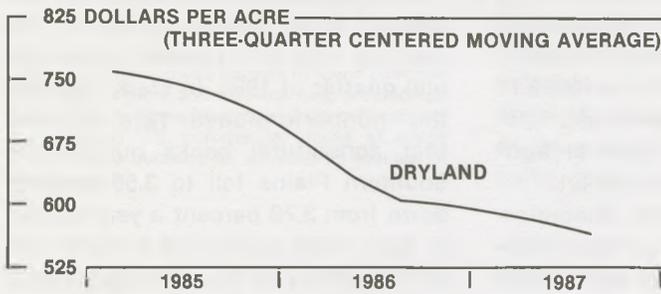
Chart 2
AGRICULTURE'S SHARE OF U.S.
MERCHANDISE EXPORTS AND IMPORTS



SOURCES: U.S. Department of Agriculture.
 Federal Reserve Bank of Dallas.

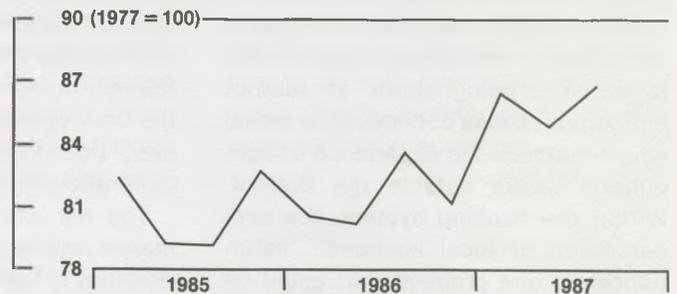
SELECTED INDICATORS OF THE TEXAS AGRICULTURAL ECONOMY

TEXAS FARM REAL ESTATE VALUES



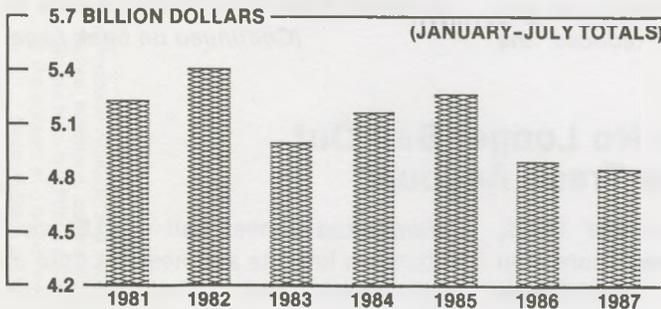
SOURCE: Quarterly Survey of Agricultural Credit Conditions,
 Federal Reserve Bank of Dallas.

PRICES RECEIVED/PRICES PAID



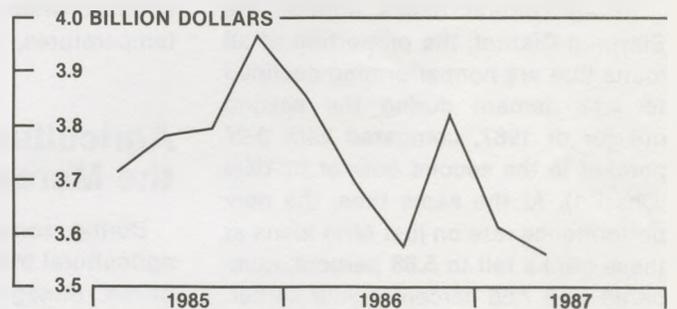
NOTE: Index is constructed by dividing prices received by farmers in Texas by prices paid by farmers nationwide. (No separate series exists for prices paid in Texas.)
 SOURCES: U.S. Department of Agriculture.
 Federal Reserve Bank of Dallas.

TEXAS CASH RECEIPTS
FROM LIVESTOCK AND CROPS



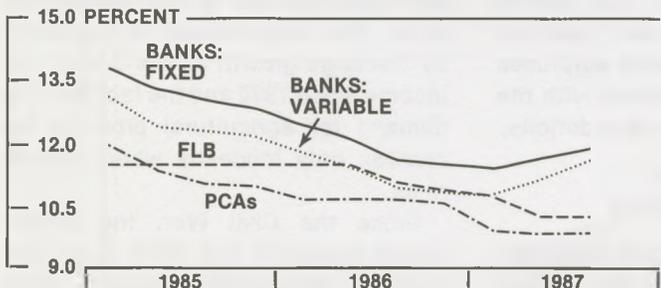
SOURCE: U.S. Department of Agriculture.

FARM DEBT OUTSTANDING AT TEXAS BANKS



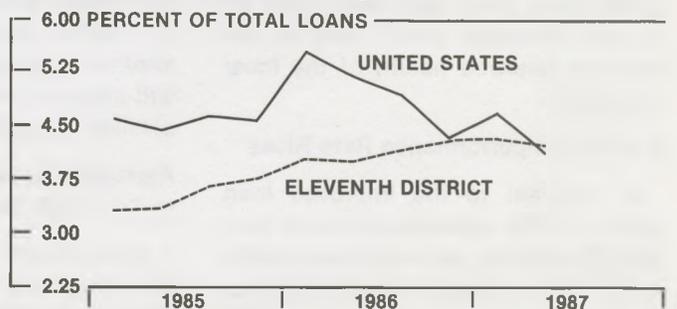
SOURCE: Board of Governors, Federal Reserve System.

INTEREST RATES ON TEXAS FARM LOANS



NOTE: PCA rate is for farm operating loans at production credit associations.
 FLB rate is for farm real estate loans at the Federal Land Bank.
 SOURCES: Farm Credit Banks of Texas.
 Quarterly Survey of Agricultural Credit Conditions,
 Federal Reserve Bank of Dallas.

NONPERFORMING LOANS
AT AGRICULTURAL BANKS



NOTE: Nonperforming loans consist of loans past due 90 days or more and still accruing plus nonaccrual loans.
 SOURCES: Board of Governors, Federal Reserve System.
 Federal Reserve Bank of Dallas.

AGRICULTURAL BRIEFS

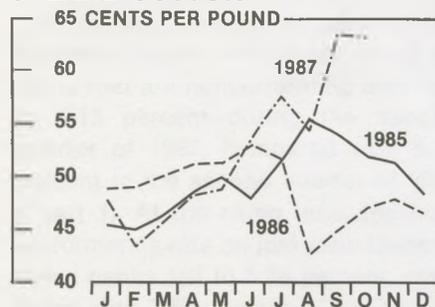
- Although agricultural land values in the Midwest and some sections of West Texas are rising, average District farm and ranch land values are falling. Land values in midwestern states rose about 3 percent in the third quarter, as profitable livestock operations and government programs to retire land made land purchases more feasible. The generous government cotton program and a strong demand for cotton have reversed the land market in West Texas around Lubbock. Land values there also rose about 3 percent in the third quarter, the second rise in land values following 11 quarters of decline. By depressing nonagricultural demand for land and by restricting off-farm sources of income for farmers and ranchers, the anemic general economy of the Eleventh District probably has prevented average land values from bottoming out.
- The quality of farm loans in District bank portfolios is improving. Agricultural bankers reported that as of October 1, 68.2 percent of

their farm loans had no significant repayment problems, compared with 63.7 percent a year earlier. Further, the proportion of farm loans that have severe repayment problems dropped to 4.1 percent on October 1, 1987, compared with 5.3 percent on October 1, 1986. Higher prices for livestock and cotton, plus continued heavy government support for many crop farmers, have made the difference.

- Government programs are critical to the economic well-being of most farmers, according to a survey of agricultural bankers. These bankers estimated that at current commodity and input prices, only 32 percent of their commercial farmer customers (those with at least \$40,000 in gross sales per year) could survive without government farm payments of any kind. The implication is that the subsidies provided by current agricultural policy keep significantly more resources tied up in the agricultural sector than would be the case if a free-markets policy were adopted.

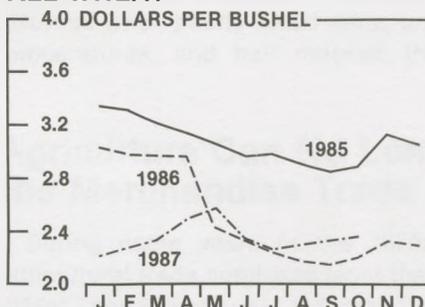
TEXAS COMMODITY MARKET PRICES

UPLAND COTTON



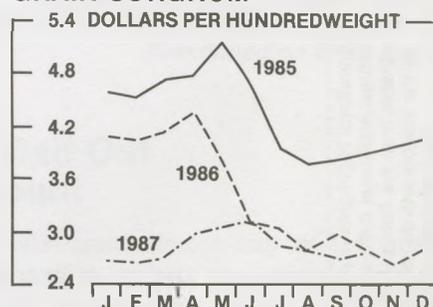
SOURCE: U.S. Department of Agriculture.

ALL WHEAT



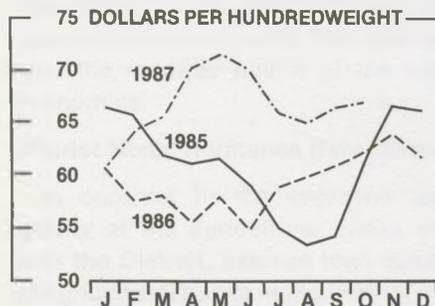
SOURCE: U.S. Department of Agriculture.

GRAIN SORGHUM



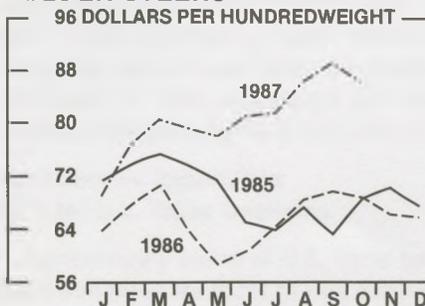
SOURCE: U.S. Department of Agriculture.

SLAUGHTER STEERS



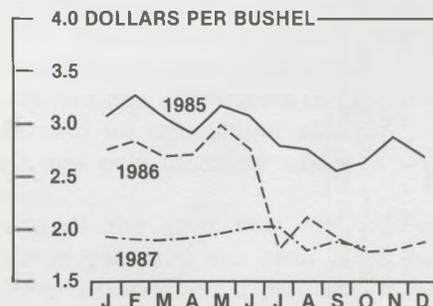
SOURCES: Texas Department of Agriculture.
Federal Reserve Bank of Dallas.

FEEDER STEERS



SOURCES: Texas Department of Agriculture.
Federal Reserve Bank of Dallas.

CORN



SOURCE: U.S. Department of Agriculture.

Loan Quality (cont.)

illustrates one of the drawbacks of geographical concentration in bank lending. If their loan portfolios had been geographically diversified across the District, the nonperformance rate at these banks would not have risen so dramatically. The improvement in agricultural credit conditions in other areas of the District would have offset the deterioration in credit conditions in the Southern Plains. A liberalization of branch-banking restrictions in Texas to allow statewide branching would increase the ability of banks to diversify their loan portfolios geographically, thereby lessening the stress on the banking system associated with localized economic shocks.

—Jeffery W. Gunther

1. Nonperforming loans consist of loans past due 90 days or more and still accruing plus nonaccrual loans. Agricultural banks are defined here as insured U.S. commercial banks at which farm loans account for at least 25 percent of total loans.

Bail Out (cont.)

larily, U.S. *nonagricultural* trade was in surplus for much of this century, but in 1971 it turned negative and has stayed so since then. During the 1970s, there was an agricultural export boom, powered by the low exchange rate value of the U.S. dollar, world income growth, and massive expansion of external debt by developing countries. The rapid increases in U.S. agricultural trade surpluses were large enough to offset the nonagricultural merchandise trade deficit completely in the years 1974-76. Even in the early 1980s, U.S. agricultural trade surpluses offset almost half the nonagricultural merchandise trade deficit. The U.S. agricultural export boom ended in the 1980s as the dollar rose in foreign exchange markets, the world slipped into recession, and the less developed countries struggled with a debt crisis. At the same time, U.S. agricultural imports rose steadily as foreign agri-

cultural products became cheaper in dollar terms.

Agriculture Now a Minor Player in U.S. Trade

Today, the surplus of agricultural exports over agricultural imports is one-third to one-fourth the size it was in the early 1980s, while nonagricultural merchandise trade deficits are two to three times larger than those registered six and seven years ago. The projected agricultural surpluses of \$5 billion to \$10 billion for the 1987-88 marketing year will be swamped by likely nonagricultural merchandise trade deficits of more than \$140 billion during the same period. The secular trend of agricultural shares of merchandise exports and imports indicates that U.S. agriculture is unlikely ever again to play a major role in determining the size of trade deficits or surpluses.

—Hilary H. Smith