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# Pieces of Eight

An Economic Perspective on the 8th District

THE FEDERAL RESERVE BANK of ST. LOUIS

*Primer on Government-Sponsored Enterprises*

*Development in the Delta: What does the Future Hold?*

*Who is Holding Agricultural Debt?*

## THE EIGHTH FEDERAL RESERVE DISTRICT


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**Pieces of Eight—An Economic Perspective on the 8th District** is a quarterly summary of agricultural, banking and business conditions in the Eighth Federal Reserve District. Single subscriptions are available free of charge by writing: Research and Public Information Department, Federal Reserve Bank of St. Louis, Post Office Box 442, St. Louis, MO 63166. The views expressed are not necessarily official positions of the Federal Reserve System.

Banking & Finance

# Government-Sponsored Enterprises: A Profile

*by Michelle A. Clark*

*Thomas A. Pollman provided research assistance.*

As the United States' largest source of credit and underwriter of risk, the federal government plays a major role in the savings and investment decisions of the private sector. Until the savings and loan (S&L) crisis, however, not much attention was being paid to the increasing obligations the government was incurring through federal insurance programs, direct loans and loan guarantees. The rapidly escalating cost of the S&L bailout has attracted the attention of policymakers and the taxpayers who will pay for most of the cleanup. Is a similar crisis brewing for other federally assisted credit and insurance programs?

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) instructs the Treasury Department and the Government Accounting Office (GAO) to examine the total potential exposure of the federal government and, hence, taxpayers to federally sponsored institution and program defaults. At year-end 1989, the value of federally assisted credit and insurance outstanding totaled $5.8 trillion, a figure greater than the gross national product for 1989. The Bush Administration has estimated that 88 percent of all outstanding housing mortgages at year-end 1989 had explicit or implicit federal government support, while 73 percent of total farm debt and almost all student loans were federally backed. Loan defaults and write-offs cost the government $14.4 billion in 1989 while losses from insurance programs totaled $67.2 billion, nearly all of which were related to insolvent banks and S&Ls.[1]

Although the deposit insurance programs make up the largest portion of total federal credit, the fastest growing component during the past 20 years has been credit extended by government-sponsored enterprises (GSEs). This article, the first in a two-part series, outlines the structure of GSEs, their role in providing credit to the private sector and the reasons policymakers are concerned.

## Purpose and Structure

No precise definition of a government-sponsored enterprise exists. A broad definition would include the 45 organizations listed in table 1. These organizations are federally chartered or owned enterprises designed to channel funds to sectors of the economy deemed worthy of special support. Though all are corporate in structure, GSEs are diverse in nature and are involved in activities ranging from rail and mail service to pension guarantees. The vast majority of GSE credit, however, is devoted to housing, agricultural and education finance.

Though enterprises such as the Government National Mortgage Association (Ginnie Mae) and the Federal National Mortgage Association (Fannie Mae) both provide funds to the housing market, they are very different organizations. Ginnie Mae is an agency of the Department of Housing and Urban Development (HUD), and its debt securities are backed by the full faith and credit of the U.S. government. Fannie Mae, on the other hand, is a privately owned corporation, and its debt securities are not guaranteed by the federal government. A narrower definition of GSEs encompasses only those privately owned enterprises like Fannie Mae whose debt securities have an implicit rather than explicit government guarantee. Because most of the concern about possible losses centers on these more narrowly defined GSEs, this article will focus on them.

## GSE Operations

Most GSEs do not extend credit directly to the public; rather, they provide funds that other financial intermediaries make available to individuals and businesses. These funds are channeled to private lending institutions either through loan agreements or by buying the assets of private lenders, thus providing lenders with funds to make new loans. Most GSEs obtain their funds by selling securities or debt in the money and capital markets.

The close ties these enterprises have with the federal government accord them certain privileges and advantages not enjoyed by other private financial intermediaries, some of which are outlined in table 2. Most of these GSEs have a line of credit with the Treasury, allowing them to exchange debt for funds up to some specified limit. Some GSEs are not required to pay federal income tax, and most are exempt from state and local income taxes as well. Because these GSEs are privately owned, however, they are also free from many of the constraints under which government-owned agencies operate. GSEs are not subject to the appropriations process of the federal budget nor is their rate of growth and financing activity controlled by Congress. In addition, these agencies can borrow directly from the Treasury or from financial mar-

**Table 1**
**U.S. Government-Sponsored Enterprises**

- Amtrak
- College Construction Loan Insurance Association (Connie Lee)
- Commodity Credit Corporation (CCC)
- Communications Satellite Corporation
- Corporation for Public Broadcasting
- Department of Housing and Urban Development (HUD):
  - —Federal Housing Administration (FHA)
  - —Government National Mortgage Association (Ginnie Mae)
- Department of Veterans Affairs:
  - —VA Mortgage Insurance
- Export-Import Bank of the United States (Exim Bank)
- Farm Credit System Financial Assistance Corporation (FAC)
- Farmers Home Administration (FmHA)
- Federal Agricultural Mortgage Corporation (Farmer Mac)
- Federal Crop Insurance Corporation
- Federal Deposit Insurance Corporation (FDIC)
- Federal Financing Bank
- Federal Home Loan Banks (FHLBanks)
- Federal Home Loan Mortgage Corporation (Freddie Mac)
- Federal Maritime Administration (MarAd)
  - —Title XI Ship Financing
- Federal National Mortgage Association (Fannie Mae)
- Federal Prison Industries, Incorporated
- Federal Farm Credit System:
  - —Banks for Cooperatives
  - —Farm Credit Banks
- Federal Reserve Banks
- Financing Corporation (FICO)
- FSLIC Resolution Fund
- General Services Administration (GSA)
- National Credit Union Administration Central Liquidity Facility
- Legal Services Corporation
- National Credit Union Share Insurance Fund (NCUSIF)
- Overseas Private Investment Corporation (OPIC)
- Pennsylvania Avenue Development Corporation
- Pension Benefit Guaranty Corporation (PBGC)
- Private Export Funding Corporation (PEFCO)
- Rural Telephone Bank
- Resolution Funding Corporation (Refcorp)
- Resolution Trust Corporation (RTC)
- Saint Lawrence Seaway Development Corporation
- Securities Investor Protection Corporation (SIPC)
- Small Business Administration (SBA)
- Student Loan Marketing Association (Sallie Mae)
- Synthetic Fuels Corporation
- Tennessee Valley Authority (TVA)
- United States Postal Service (USPS)
- United States Railway Association
- Washington Metropolitan Area Transit Authority

SOURCE: "U.S. Government-Sponsored Enterprises (GSEs)," *Moody's Special Comment* (February 1990).

kets; other lenders under the direction of the federal government obtain their funds from the Federal Financing Bank, which borrows from the Treasury.

As mentioned previously, the largest portion of GSE credit is devoted to housing, agriculture and education. The activities of the major GSEs in these three areas are described below.

### *Housing—Fannie Mae & Freddie Mac*

Although Fannie Mae has been in existence almost 30 years longer than Freddie Mac, both enterprises were created to fulfill the same purpose: to provide credit to the primary mortgage (or mortgage origination) market by maintaining a continuous presence in the secondary mortgage (or mortgage sales) market, regardless of economic conditions. Both GSEs satisfy that mandate through two types of transactions: 1) purchasing mortgages from loan originators for their own portfolios, thus providing lenders with funds to originate more mortgages and 2) issuing mortgage-backed securities (MBSs) in exchange for lenders' mortgages (called swaps). Lenders can hold MBSs in their portfolios or sell them in the money market.

The oldest and most popular MBS issued by these agencies is the pass-through security (Fannie Mae) or the participation certificate (Freddie Mac).[2] These pass-through securities have proved extremely popular because the agencies guarantee the timely payment to investors of the principal and interest on loans underlying the securities, even if the agency has not received payments on the loans from the mortgage servicer. Fannie Mae and Freddie Mac receive fees for their guarantee. The issuance of a pass-though security represents both a securities sale and a sale of the underlying pools of mortgages; as a result, mortgages purchased and then securitized by Fannie Mae and Freddie Mac are not assets of the organizations nor are outstanding agency-issued MBSs liabilities. Thus, unless retained by the corporation, mortgage pools and outstanding MBSs do not appear on the agencies' balance sheets.

Unlike their sister agency Ginnie Mae, both Fannie Mae and Freddie Mac are authorized to purchase conventional (non-FHA/VA) mortgages up to specified limits. Fannie Mae and Freddie Mac are huge players in the residential mortgage market: in 1989, Fannie Mae's mortgage portfolio

**Table 2**
**Government-Sponsored Enterprise Links to the Federal Government**

| | Federal National Mortgage Association | Federal Home Loan Mortgage Corporation | Federal Home Loan Banks | Farm Credit System | Federal Agricultural Mortgage Corporation | Student Loan Marketing Association |
|---|---|---|---|---|---|---|
| President or presidential appointees select some board members | Yes (5/18) | Yes (5/18) | Yes (6/14) (a) | No | Yes (5/15) | Yes (7/21) |
| Treasury lending authorized | $2.25B | $2.25B | $4.0B | No (b) | $1.5B (c) | $1.0B |
| Treasury approval of debt issuance | Yes | Yes | Yes | No | No | Yes |
| Eligible for Fed open market purchases | Yes | Yes | Yes | Yes | n/a (d) | Yes |
| Use of Fed as fiscal agent | Yes | Yes | Yes | Yes | Yes | Yes |
| Eligible to collateralize public deposits (all U.S. government; most state and local) | Yes | Yes | Yes | Yes | Yes | Yes |
| Eligible for unlimited investment by national banks and Fed member state banks | Yes | Yes | Yes | Yes | Yes | Yes |
| Eligible for unlimited investment by thrifts regulated by FDIC or OTS | Yes | Yes | Yes | Yes | Yes | Yes |
| Exemption of corporate earnings from federal income tax | No | No | Yes | Yes (e) | No | No |
| Exemption of corporate earnings from state and local income tax | Yes | Yes | Yes | Yes | No | Yes |
| Exemption of interest paid from state income tax | No | No | Yes | Yes | No | Yes |
| Subject to GAO audit | Yes (f) | Yes (f) | Yes | No | Yes | No |
| Federal regulator | HUD | HUD | FHFB | FCA (g) | FCA | None |

n/a = Not applicable
B = Billions
(a) Each bank
(b) Treasury is authorized to guarantee up to $4 billion of Financial Assistance Corporation bonds.
(c) Upon required certification from FAMC, borrowing from Treasury authorized to make payments under guarantee.
(d) Entity newly created.
(e) Federal Land Banks, Farm Credit Banks and Financial Assistance Corporation.
(f) Mortgage transactions may be subject to GAO audit under rules that may be prescribed by the Comptroller General.
(g) The Farm Credit System Assistance Board also has certain powers with respect to the Financial Assistance Corporation and the System institutions needing financial assistance.

SOURCE: Statutes and regulations pertaining to the GSEs as summarized in the *Report of the Secretary of the Treasury on Government Sponsored Enterprises* (May 1990).

and MBS issues represented 14 percent of all residential mortgages outstanding, while Freddie Mac's represented 12 percent. Both GSEs acquire funds to finance their activities through short- and long-term debt issues. Of the $116.1 billion in Fannie Mae debt outstanding at year-end 1989, 30 percent was short-term debt; 64 percent of Freddie Mac's $26.1 billion in outstanding debt was short-term at year-end 1989.

Despite numerous similarities in their structure and purpose, Fannie Mae and Freddie Mac operate quite differently from one another. In terms of assets, Fannie Mae is by far the larger of the two GSEs. At year-end 1989 Fannie Mae had $124.3 billion in assets, making it the sixth largest U.S. corporation; the only financial companies with more assets were Citicorp (number one) and American Express (number four). Fannie Mae's assets were 3.5 times the assets of Freddie Mac at year-end 1989 primarily because Fannie Mae keeps much larger portions of the mortgages it purchases than Freddie Mac.

### *Agriculture—Farm Credit System & Farmer Mac*

The Farm Credit System (FCS) is an umbrella organization under which numerous lending institutions and affiliated service and other entities provide credit to the agricultural sector. The system's banks and associations provide credit and related services to farmers, ranchers, producers and harvesters of aquatic products, rural homeowners, certain farm-related businesses, agricultural and aquatic cooperatives and rural utilities. The system is composed of 12 Farm Credit districts that serve borrowers in all 50 states and Puerto Rico. Eleven of 12 districts have Farm Credit Banks, which provide funds for long-term mortgage loans to farmers and ranchers, and supervision and support services to other affiliated institutions and associations. In addition, three federally chartered Banks for Cooperatives provide credit and leasing services to agricultural cooperatives, rural utility systems and other eligible customers. Systemwide assets totaled $64 billion at year-end 1989.

Because the institutions and associations of the system are cooperatively owned by their borrowers, all borrowers must be stockholders of the system institution from which they borrow. FCS activities are funded through the sale of systemwide debt securities that are the joint and several obligations of the Farm Credit Banks and the Banks for Cooperatives.[3] Other funding is provided from the sale of consolidated systemwide notes and bonds. At year-end 1989, the system had $57 billion in publicly traded debt securities outstanding.

Farmer Mac, created in 1987 when the FCS was restructured following a government bailout, provides a secondary market for agricultural real estate loans with federally backed credit enhancement. Farmer Mac issued $21 million of common stock in November 1988 and used the proceeds to purchase investment securities; at mid-1990, however, the GSE had not yet begun secondary market operations. Once Farmer Mac is up and running, lenders or originators will be able to sell their agricultural real estate or rural housing loans to certified marketing facilities, or poolers, approved by the agency. The poolers will then issue securities backed by pools of qualified loans. As with pass-through MBSs, the principal and interest payments on the underlying mortgages will be passed through to the buyers of the securities. Farmer Mac provides credit enhancement through its guarantee of timely payment of principal and interest.

Unlike the housing GSEs, Farmer Mac has a subordinated participation interest structure. Under this system, poolers issue securities backed by the first 90 percent of the pool with the payments guaranteed by Farmer Mac; securities may be issued backed by the retained subordinated interest of the pool, but these securities are not backed by Farmer Mac.

### *Education—Sallie Mae*

As with the housing GSEs, Sallie Mae was established to provide a secondary market for guaranteed student loans (GSLs). Prior to the creation of Sallie Mae, very few lending institutions participated in the Guaranteed Student Loan Program (GSLP) because GSLs are relatively illiquid, long-term assets whose interest rates are set by the federal government, often at below-market rates. Sallie Mae assists funding for higher education through two primary activities: 1) the purchasing of loans guaranteed by the federal government or indirectly guaranteed through state or nonprofit agencies with federal reinsurance and 2) collateralized lending to financial institutions and other GSLP participants to finance student loans (called warehousing advances). Sallie Mae services (collects interest and principal payments) approximately half the loans it purchases.

Sallie Mae experienced very rapid growth in the 1980s, with its assets rising from $9.1 billion at year-end 1983 to $35.5 billion at year-end 1989. As of year-end 1989, Sallie Mae had purchased from 1,600 lenders the student loans of approximately four million borrowers. Sallie Mae finances its activities through sales of debt securities; at year-end 1989, Sallie Mae's outstanding debt was $34.5 billion, with slightly more than half of the debt in the form of long-term notes.

## The Issues

Because of the special ties the privately owned GSEs have to the federal government, the market perceives these GSEs to have implicit government backing. Investors in GSE debt or GSE-guaranteed securities assume Congress would use taxpayer funds to prevent a GSE failure. This market perception allows GSEs to borrow money at rates just slightly higher than what the U.S. Treasury pays for funds and increases the incentives for GSEs to seek greater returns by assuming more risk. The asymmetry between GSEs' cost of funds and expected returns exists because returns flow to stockholders, while losses in excess of capital are ultimately incurred by taxpayers. Thus, the gains from excessive risk are "privatized," while the losses are "socialized."

The rapid growth of these GSEs is another area of concern. During the 1980s the amount of GSE securities outstanding increased at a 19.2 percent annual rate, and stood at $863 billion at year-end 1989. To finance this growth, GSEs have been borrowing funds at an increasing rate, and this borrowing is expected to exceed federal borrowing in fiscal 1991. This tremendous growth in outstanding debt has raised concerns about the leverage of GSEs. High debt-to-assets ratios imply a greater risk of loss if an industry experiences a downturn; because GSEs cannot diversify their operations given their federal mandate, their profitability is highly dependent on the health of the industry they represent as well as general economic conditions. Many policymakers believe GSEs are under-capitalized, thus increasing the magnitude of losses in the event of insolvency. These issues, and recommendations to mitigate the risk of losses from GSE activities, will be addressed in the December 1990 edition of **Pieces of Eight**.

FOOTNOTES

[1]United States Office of Management and Budget. "Recognizing Federal Underwriting Risks," *The Budget of the U.S. Government, Fiscal Year 1991,* (1990). In addition to the budget, the following two documents were used extensively in researching this article: United States Department of Treasury, *Report of the Secretary of the Treasury on Government Sponsored Enterprises May 1990* and "U.S. Government-Sponsored Enterprises (GSEs)," Moody's Special Comment (February 1990).

[2]See Michelle A. Clark. "Competition Heats Up in the Home Mortgage Market," *Pieces of Eight,* (March 1990), pp. 9-13 for a detailed discussion of the workings of the pass-through securities market.

[3]In this case, a "joint and several obligation" permits a debt-holder to sue either agency or the two jointly in case of default. If just one agency is sued, that agency can sue the other for its share of the liability.

# Realizing the Delta's Economic Potential

*by Thomas B. Mandelbaum*
*Thomas A. Pollman provided research assistance.*

In 1988, Congress established the Lower Mississippi Delta Development Commission to make recommendations regarding the economic needs, problems and opportunities in the Lower Mississippi Delta, the nation's poorest region. Most of the Delta region, which includes 219 counties in seven states along the banks of the Mississippi River, can be found within the boundaries of the Eighth Federal Reserve District (see map). This article discusses the Delta's current economic conditions and the Commission's recommendations for improving them, as outlined in *The Delta Initiatives*, the Commission's final report that was released in May 1990.

## Historical Roots

The economic development of the Delta region reflects its geography. Agriculture, one of the region's dominant industries, has been fostered by the long growing seasons and fertile soils on the banks of the Mississippi River. The plantation farming system that once existed was labor-intensive, taking advantage of the services of slaves and tenant farmers. As farming became increasingly mechanized, particularly in the second half of this century, many farm workers were no longer needed. While many moved to industrial centers throughout the nation, others remained in rural areas and experienced unemployment and poverty, conditions that still exist. In addition to a large agriculture sector, the Delta economy is characterized by production of basic manufactured goods such as food products, apparel, appliances and automotive parts.

The economic geography of the Delta is dominated by the Mississippi River. The Mississippi River has long promoted trade among the nation's regions; however, only five bridges span the river between Memphis and Baton Rouge, hindering intraregional trade. Historically, the states have competed for footloose industries rather than worked together to improve conditions. The Commission is one of the first serious attempts to adopt a cooperative approach to the region's economic development.

## Current Conditions

Although per capita income in the Delta rose faster than the national average between 1970 and 1980, the region's average income remains relatively depressed and poverty is widespread. According to the 1980 Census, 20.9 percent of the Delta population was below the poverty level, substantially more than the U.S. average of 12.4 percent and even higher than Appalachia's 17 percent.[1] In some Delta areas, conditions are substantially worse. Almost 53 percent of the population of Mississippi's Tunica County were in poverty, making that county the nation's poorest. The poverty rate among the Delta's sizable African American population was 41.6 percent versus 29.9 percent nationally.

Since 1980, per capita income in the Delta has fallen even further below that in the rest of the nation, dropping from 79.9 percent of the national average in 1980 to 75.1 percent in 1988. The poverty of the Delta region is reflected in the living conditions. Relatively few physicians and registered nurses serve the Delta's residents. The region's 1984 infant mortality rate of 12.5 deaths per 1,000 births compares with a 10.7 national rate. The rate among African Americans in the Delta region is even higher, exceeding 18 deaths per 1,000. Because economic development requires a healthy work force, these health conditions are thought to have hindered efforts to improve economic conditions.

A recurring theme in the Commission's report, which is related to the Delta's health conditions, is that the low educational attainment and skill levels of Delta workers limit income growth, productivity and economic development efforts. The 1980 Census indicated that only 55.5 percent of Delta residents aged 25 years or older had graduated from high school, compared with 66.5 percent nationally. Almost 26 percent of Delta residents drop out of high school, compared with 20 percent nationally. Not surprisingly, the Delta region has one of the highest illiteracy rates in the nation. One factor undoubtedly contributing to the poor educational results is that educational expenditures per student in the Delta were 20 percent lower than the national average in 1982.

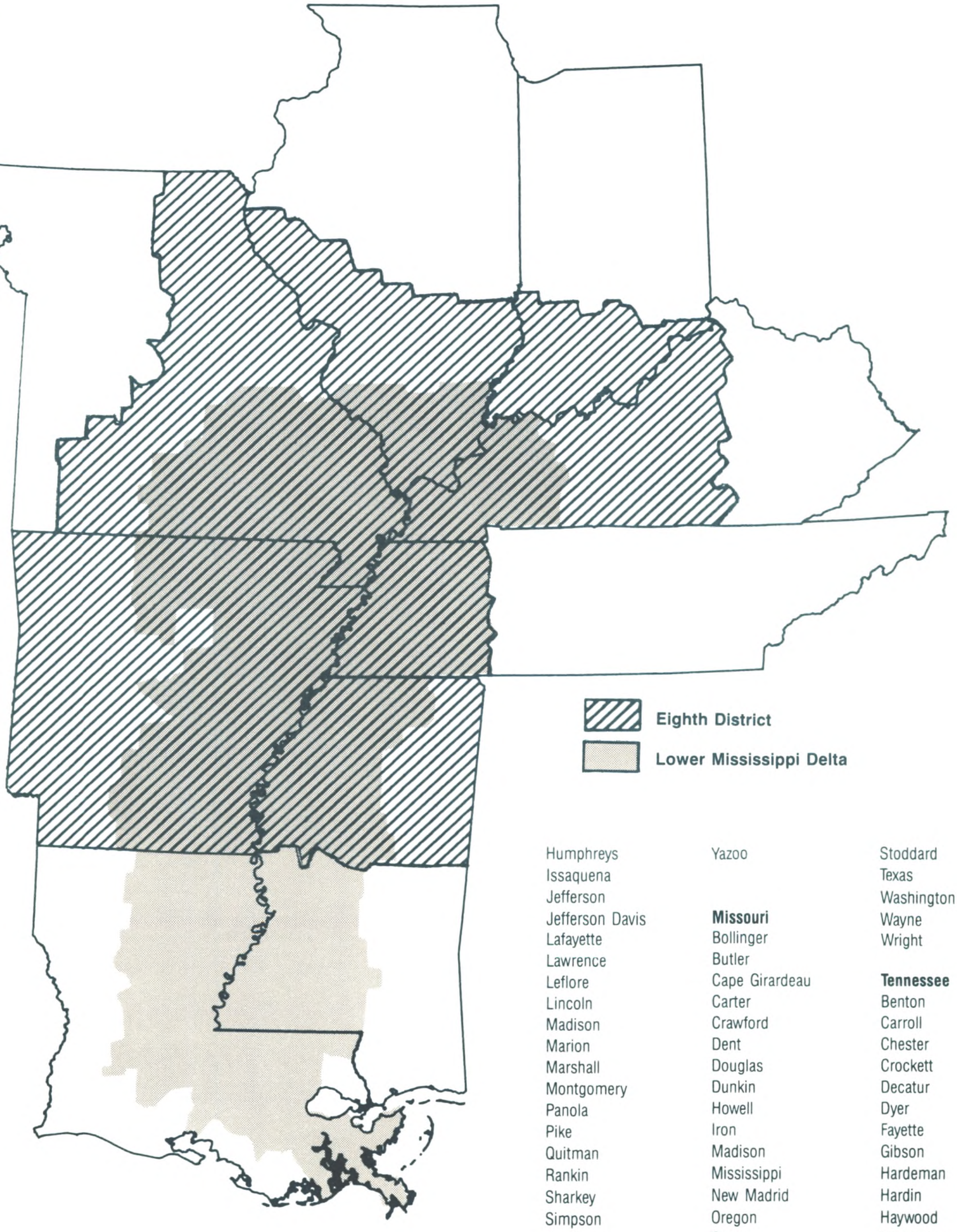
In light of the low income in the Delta, it is not surprising that the Delta's physical infrastructure is also below average. According to the 1980 Census, slightly more than a third of Delta housing units were defined as substandard, almost twice the U.S. rate.[2] Also, many highways, roads and bridges are in poor condition.

## Recommendations

In general, the Commission feels that to improve conditions in the Delta it is essential to improve education, develop leadership among Delta residents and change attitudes that have long held back

*Figure 1*

# The Eighth Federal Reserve District and the Lower Mississippi Delta




**The Lower Mississippi Delta includes the following counties and parishes:**

**Arkansas**
Arkansas
Ashley
Baxter
Bradley
Calhoun
Chicot
Clay
Cleveland
Craighead
Crittenden
Cross
Dallas
Desha
Drew
Fulton
Grant
Greene
Independence
Izard
Jackson
Jefferson
Lawrence
Lee
Lincoln
Lonoke
Marion
Mississippi
Monroe
Ouachita
Phillips
Poinsett
Prairie
Pulaski
Randolph
St. Francis
Searcy
Sharp
Stone
Union
VanBuren
White
Woodruff

**Illinois**
Alexander
Franklin
Gallatin
Hamilton
Hardin
Jackson
Johnson
Massac
Perry
Pope
Pulaski
Randolph
Saline
Union
White
Williamson

**Kentucky**
Ballard
Caldwell
Calloway
Carlisle
Christian
Crittenden
Fulton
Graves
Henderson
Hickman
Hopkins
Livingston
Lyon
Marshall
McCracken
McLean
Muhlenberg
Todd
Trigg
Union
Webster

**Louisiana**
Acadia
Allen
Ascension
Assumption
Avoyelles
Caldwell
Catahoula
Concordia
East Baton Rouge
East Carroll
East Felicia
Evangeline
Franklin
Grant
Iberia
Iberville
Jackson
Jefferson
Lafourche
LaSalle
Lincoln
Livingston
Madison
Morehouse
Orleans
Ouachita
Pointe Coupee
Plaquemines
Rapides
Richland
St. Bernard
St. Charles
St. Helena
St. James
St. John the Baptist
St. Landry
St. Martin
Tangipahoa
Tensas
Union
Washington
West Baton Rouge
West Carroll
West Felicia
Winn

**Mississippi**
Adams
Amite
Attala
Benton
Bolivar
Carroll
Claiborne
Coahoma
Copiah
Covington
DeSoto
Franklin
Grenada
Hinds
Holmes
Humphreys
Issaquena
Jefferson
Jefferson Davis
Lafayette
Lawrence
Leflore
Lincoln
Madison
Marion
Marshall
Montgomery
Panola
Pike
Quitman
Rankin
Sharkey
Simpson
Sunflower
Tallahatchie
Tate
Tippah
Union
Walthall
Warren
Washington
Wilkinson
Yalobusha
Yazoo

**Missouri**
Bollinger
Butler
Cape Girardeau
Carter
Crawford
Dent
Douglas
Dunkin
Howell
Iron
Madison
Mississippi
New Madrid
Oregon
Ozark
Pemiscot
Perry
Phelps
Reynolds
Ripley
St. Genevieve
St. Francois
Scott
Shannon
Stoddard
Texas
Washington
Wayne
Wright

**Tennessee**
Benton
Carroll
Chester
Crockett
Decatur
Dyer
Fayette
Gibson
Hardeman
Hardin
Haywood
Henderson
Henry
Lake
Lauderdale
McNairy
Madison
Obion
Shelby
Tipton
Weakley

regional progress. More specifically, the Commission presented 68 10-year development goals and more than 400 recommendations. Since they were released last May, these recommendations have received considerable attention and are being studied by the governments of the Delta states and by U.S. government agencies, including the Department of Housing and Urban Development. A group of congressmen from the Delta also meets regularly to discuss the status of the recommendations. A few of the key recommendations are discussed in the following sections.

*Human Capital Development*

There is broad agreement that it is essential to improve the education and job skills of Delta workers. In a study regarding Delta economic development finance, for example, two researchers report that bankers, local economic developers and state officials repeatedly emphasized that "without an improvement in our human capital...more money will do no good."[3]

Among the dozens of recommendations to improve the quality of education, the Commission suggests that the federal government fund magnet schools stressing mathematics and science in rural areas and restructure federal grants to establish services for low-income, rural students. States are urged to create a regional magnet high school near the National Center for Toxicological Research in Jefferson, Arkansas, to take advantage of the faculty expertise and research facilities; consider lengthening the school year; and, because of the shortage of math and science teachers, allow qualified non-teacher professionals to teach those subjects. In addition, the Commission urges states to continue to restructure their educational programs by emphasizing teacher professionalism and accountability, developing school-based management and making curriculum more relevant.

The literacy and job skills of Delta workers could be improved, according to the Commission, if the U.S. Department of Labor and U.S. Department of Education would allow states and localities more flexibility in the administration of federal training programs, such as those provided by the Jobs Training Partnership Act and Adult Basic Education. In addition, the Commission urges the enactment and funding of the National Literacy Act of 1989. In many areas, the administration of literacy training is scattered among a number of state and local agencies, hampering the programs' effectiveness. Therefore, the Commission urges Delta states to develop a coordinated literacy enhancement system to coordinate public, private and volunteer programs. One recommendation suggests that institutions of higher education form a "literacy corps" comprised of college students to supplement existing organizations.

The Commission encourages further cooperation among the Delta region's 104 colleges and universities so they can more effectively facilitate the region's economic development as well as compete for public and private research funds. To this end, a Summit on Higher Education is tentatively planned for November 1990 in Memphis.

*Encouraging Private Enterprise*

Historically, the Delta has relied heavily on the production of primary products, such as agricultural commodities, timber and raw materials. The Delta's private sector can be strengthened, according to the Commission, by diversifying its economy and expanding "value-added processing," that is, operations that use the Delta's primary products to produce finished or intermediate products. Examples include canneries and paper factories. To encourage value-added processing, the Commission suggests that Congress establish the Delta as a development zone and enact policies that would require that a certain percentage of federal expenditures in targeted value-added industries, such as food processing, be bought from rural Delta counties. Additionally, the federal government should fund research for the development of value-added industries in the Delta and institute tax incentives for firms locating in rural Delta counties.

To spur growth in manufacturing, the Commission recommends that Congress and Delta states establish a regional "cross-match program" that helps match regional producers of goods and services with buyers. After establishing a comprehensive database, the program would furnish detailed information on both potential markets for finished products and potential suppliers for inputs within the Delta to any interested Delta seller or buyer. One expected result would be greater intraregional trade.

The Commission suggests that the Delta's economic expansion has been held back by a lack of capital to finance business start-ups and expansions. Banks in the Delta region possess substantial assets, almost $78 billion in 1989, but a comparatively small proportion of these assets are loaned to businesses and individuals: loans from Delta banks equaled 73.6 percent of their assets, somewhat less than the national average of 79.5 percent. In rural parts of the Delta region, loan-to-asset ratios are even lower; when the four counties that contain Little Rock, Memphis, New Orleans and Jackson, Mississippi, are removed, the Delta's loan-to-deposit ratio falls to 65.4 percent. The relatively low ratios in the Delta are thought to reflect the conservative lending practices of Delta bankers and/or lower loan demand.

To make more capital available for investment in the Delta, the Commission recommends the federal government, in cooperation with state governments and the private sector, establish a regional development bank that guarantees local bank-financed loans and provides equity, near equity and fixed-asset financing for Delta businesses. Funds would be targeted to assist small and minority businesses and firms needing venture capital or export credit.

### *Promoting Tourism*

Another potential source of economic growth is tourism. The Delta region is rich in history and natural beauty, but according to the Commission, these attractions are not widely publicized or developed. One program would establish and promote an African American Heritage Trail, linking existing historical sites and newly developed cultural museums.

## Conclusion

*The Delta Initiatives* provides a comprehensive plan for improving conditions in the nation's poorest region during the next 10 years. Analyses of many of the specific recommendations will undoubtedly produce conflicting assessments as to their effectiveness in promoting economic development. It is clear, however, that the poverty of the Delta region is not a new phenomenon and, at best, its eradication will take decades.

Many factors that influence the Delta's economic development are beyond the control of Delta businesses, institutions and residents. National and global economic changes have and will continue to affect economic activity in the Delta and will influence the effectiveness of any specific policy actions that are undertaken. Two economists suggest, for example, that given the Delta's concentration in the production of goods that are sensitive to changes in interest rates and imports, "...lower national interest rates and a lower American dollar could probably do more to benefit the region's economy than any other single action recommended here or elsewhere."[4]

Numerous recommendations require the influx of substantial expenditures or subsidies from Washington. Given the current fiscal environment in which Congress and the President are attempting to cut federal expenditures by tens of billions of dollars, it is likely that many of the proposals will never be funded.

Many of the recommendations, however, do not rely on outside forces but focus on how the Delta can help itself. Some recommendations require cooperation between state economic development agencies, universities and other institutions, a contrast to the competition that has characterized their relations in the past. Perhaps the most critical recommendations are those that seek to improve educational opportunities. As markets become increasingly global in scope and work becomes more technical, a workforce that is literate and highly skilled is essential. Though improvement in the quality of labor is a necessary condition for the Delta region's economic development, it is not sufficient. Without a corresponding rise in the demand for this more highly skilled labor by new and expanding firms in the Delta region, it is likely that many of the best-educated Delta workers will leave for better opportunities elsewhere.

FOOTNOTES

[1]Appalachia refers to the Appalachian Regional Commission's 90 target counties which are located in rural parts of Alabama, Kentucky, Mississippi, North Carolina, Ohio, Tennessee, Virginia and West Virginia.

[2]Substandard housing lacks complete plumbing facilities for exclusive use and/or central heating equipment.

[3]Raymond C. Lenzi and Kenneth Pigg, "Lower Mississippi Delta Economic Development Finance: A Proposal for a Delta Development Bank," Community Development Department, University of Missouri-Columbia (February 23, 1990), p.1.

[4]Ibid.

# Commercial Banks Lead Agricultural Lending

*by Jeffrey D. Karrenbrock*
*David H. Kelly provided research assistance.*

Commercial banks make more agricultural loans in both the Eighth Federal Reserve District and the United States than any other financial intermediary. This article briefly examines the market share of agricultural debt held by commercial banks and other large agricultural lenders. In addition, the market share and ratios reflecting the performance of agricultural loan portfolios are analyzed for two types of commercial banks: those whose loan portfolios are more heavily oriented to agricultural lending and those that are not.

## Agricultural Lenders

Agricultural debt, or loans outstanding, can be separated into two categories: real estate and non-real estate debt. Agricultural real estate debt includes loans made to purchase agricultural land as well as loans that are collateralized with agricultural land. Non-real estate debt is composed of production loans, which are used by farmers to finance purchases of agricultural inputs, and other loans for purchasing items such as farm machinery and implements.

The proportion of agricultural debt held by various agricultural lenders in the Eighth District and the United States is shown in table 1. In terms of total agricultural lending, commercial banks are the largest lenders, holding about 30 percent of total agricultural debt in both the District and the United States. This leadership position is a recent development for commercial banks. During the early 1980s, the Farm Credit System (FCS), a nationwide system of federally chartered agricultural lending institutions cooperatively owned by their borrowers, held the lead position in agricultural lending, but lost that role in 1986 and 1987 in the District and U.S. markets, respectively. The FCS is now the second-largest lender in the U.S. market, while the Farmers Home Administration (FmHA), the "lender of last resort" for farmers and rural residents, is the second-largest lender in the District.

Focusing on the real estate market, commercial banks hold more debt than any other lender in the District; however, the FCS is the largest real estate lender in the United States. The FCS is the second-largest real estate lender in the District and individuals hold the second-largest amount of real estate debt in the nation. With market shares exceeding 10 percent, the FmHA and life insurance companies are also important real estate lenders in the District and the United States.

In the agricultural non-real estate market, the FmHA is the largest lender in the District with commercial banks following a close second. This contrasts with the national market where commercial banks hold more than twice the amount of loans held by their closest competitor, the FmHA. Furthermore, the market share of non-real estate

**Table 1**
**1988 Market Shares of Agricultural Debt**

| | Eighth District[1] | | | United States | | |
|---|---|---|---|---|---|---|
| | Total | Real Estate | Non-real Estate | Total | Real Estate | Non-real Estate |
| Banks | 30.6 | 28.2 | 33.8 | 30.4 | 18.6 | 45.4 |
| Farm Credit System | 20.2 | 26.8 | 11.3 | 26.6 | 36.6 | 13.9 |
| Life Insurance Companies | 5.9 | 10.3 | — | 6.5 | 11.6 | — |
| Farmers Home Admin. | 26.7 | 18.0 | 38.4 | 16.3 | 11.6 | 22.3 |
| Individuals | 16.6 | 16.6 | 16.5 | 20.2 | 21.7 | 18.3 |

[1]Eighth District data is based on the aggregated data of Arkansas, Kentucky, Mississippi, Missouri and Tennessee.

SOURCE: Derived from data in the U.S. Department of Agriculture's *Economic Indicators of the Farm Sector: State Financial Summary*, 1988.

**Table 2**
**Selected 1989 Statistics for Commercial Banks That Lend to Agriculture**

| | Eighth District[1] | | United States | |
|---|---|---|---|---|
| | Agricultural Banks | Non-agricultural Banks | Agricultural Banks | Non-agricultural Banks |
| Loan Market Share | | | | |
| Total[2] | 51.0% | 49.0% | 51.4% | 48.6% |
| Non-real Estate | 53.0 | 46.9 | 54.8 | 45.2 |
| Real Estate | 48.9 | 51.0 | 45.0 | 55.0 |
| Performance Ratios[3] — Average 1984-89 | | | | |
| Agricultural loan losses | 2.50 | 1.59 | 2.20 | 2.06 |
| Agricultural non-performing loans | 7.08 | 5.17 | 5.87 | 7.52 |
| Performance Ratios[3] — 1989 | | | | |
| Agricultural loan losses | 0.35 | 0.35 | 0.36 | 0.25 |
| Agricultural non-performing loans | 4.21 | 2.96 | 3.20 | 4.74 |

[1]District data includes all agricultural lenders within the boundaries of the map shown on the inside front cover of this publication.

[2]Total loans equal non-real estate loans plus real estate loans.

[3]All ratios are given as a percent of total production loans.

SOURCE: Derived from data provided by banks in the Federal Financial Institutions Examination Council's *Consolidated Reports of Condition and Income.*

debt held by the FmHA in the District is almost twice its share in the nation. The disproportionate role of the FmHA in the District stems from its large role in Mississippi and Arkansas, where it holds 63 percent and 38.2 percent of non-real estate debt, respectively.

## Commercial Banks

Given the importance of commercial banks as an agricultural lender, their role merits closer examination. For purposes of this article, commercial banks lending to agriculture are further divided into two groups of banks that are termed agricultural and non-agricultural. A bank is defined as an agricultural bank if the ratio of its agricultural loans to total loans exceeds the average of such ratios at all U.S. banks at year-end; otherwise the bank is a non-agricultural bank. This distinction hinges on the relative importance of agricultural loans in a commercial bank's portfolio of loans. In absolute terms, however, some of the largest agricultural lenders in the District and the United States are not classified as agricultural banks. This is because their loan volume in other areas, such as commercial and industrial loans, far outweighs their exposure to agricultural loans.

### *Market Share*

Agricultural loan market shares held by agricultural and non-agricultural banks in 1989 are shown in table 2. Total agricultural loans at commercial banks are split almost evenly between agricultural and non-agricultural banks in both U.S. and District markets. Another similarity is that agricultural banks tend to hold slightly more of the agricultural non-real estate loans, while non-agricultural banks hold a larger portion of loans collateralized with agricultural real estate.

During the 1980s, agricultural banks lost market share to non-agricultural banks. Between 1980 and 1989, Eighth District agricultural banks saw their market share drop 7 percentage points in the agricultural loan market. This total market share decline stemmed from market share losses in non-real estate and real estate loans of 7.3 and 5.5 percentage points, respectively. U.S. agricultural banks faced a similar situation as their market share of total agricultural loans dropped 4.4 percentage points. Unlike the District market, however, virtually all of their market share decline came from market share losses in non-real estate loans.

### *Performance Ratios*

Two ratios reflecting the performance of agricultural and non-agricultural banks' agricultural loan portfolios are shown in table 2. Agricultural loan losses represent those loans that commercial banks have written off as bad debt, while non-performing loans are those loans that are 90 days or more delinquent or in non-accrual status. Both ratios use data on non-real estate loans only and are shown as a percent of total agricultural non-real estate loans. The average value of these ratios for 1984 to 1989 and their 1989 values are given in table 2.

In the District, non-agricultural banks had lower average ratios for both agricultural loan losses and non-performing loans over the five year period. This contrasts with the U.S. market, where agricultural banks had a slightly higher average agricultural loan loss ratio, but a lower average agricultural non-performing loan ratio than the non-agricultural banks. These figures suggest, at least at the District level, that non-agricultural banks did a better job of managing their agricultural production loan portfolios from 1984 to 1989. It is important to realize, however, that these current ratios are strongly influenced by events happening prior to 1984. Thus, the performance figures for 1984 to 1989 may be affected either favorably or unfavorably by banks' behavior prior to 1984. Different behavior between agricultural and non-agricultural banks can affect one's assessment of the 1984-89 performance of agricultural relative to non-agricultural banks. Lacking the data to examine the relative performance of these banks prior to 1984, some caveats in interpreting the performance ratios are in order.

During the downturn in the agricultural economy that occurred in the late 1970s and early 1980s, non-performing loans and loan losses began to grow at financial institutions. A simple example can illustrate how banks' timing of writing off bad debts could affect the average ratios reported in table 2. Assume agricultural and non-agricultural banks had similar levels of bad loans in the early 1980s and that non-agricultural banks wrote off their bad loans before 1984, while agricultural banks waited until the mid-1980s to start to write off their bad debt. In this case, non-agricultural banks would tend to have a lower ratio for loan losses than agricultural banks during the 1984 to 1989 period. This would give the impression that the non-agricultural banks had better managed their agricultural production loan portfolios in the 1984 to 1989 period, even though both groups of banks may have had similar amounts of bad debt during the entire decade.

Differences in the timing of write-offs would also affect the non-performing loan ratios. Once banks charge off a bad loan, the loan is no longer classified as non-performing. To continue the above example, if the non-agricultural banks wrote off their bad debt in the early 1980s, their volume of non-performing loans would also have declined in this period. Having eliminated these non-performing loans from their books in the early 1980s would mean a lower non-performing loan ratio in the mid-to-late 1980s for non-agricultural banks.

A second factor that affected the performance ratios is the volume of non-real estate loans at the banks from 1984 to 1989. Recall that the ratios presented in table 2 are simply the percentage of loan losses and non-performing loans to total non-real estate loans. If the volume of non-real estate loans were to increase (decrease) at a given type of bank, this would lower (increase) these ratios, assuming no change in loan losses or nonperforming loans resulted from the increase (decrease) in loans. Both agricultural and non-agricultural banks in the District and the United States had lower non-real estate loan volumes in 1989 than in 1984, which put upward pressure on their performance ratios. However, non-real estate loans at agricultural banks fell 26.2 percent and 27.2 percent in the District and nation, respectively, while non-real estate loans at non-agricultural banks only fell 12.6 percent in the District and 14.9 percent in the nation between 1984 and 1989. Thus, the upward pressure on the banks' performance ratios was relatively less for non-agricultural banks during the late 1980s.

These two performance ratios were at their highest values between 1985 and 1986 for both types of banks in the District and the United States. During this time, loan losses were running between 2.7 percent and 4.7 percent, while non-performing loans were running between 6.6 percent and 10.8 percent of total non-real estate loans. Since the mid-1980s, these ratios have improved each year. The 1989 values indicate how much these ratios have improved since the mid-1980s. Agricultural loan losses have declined to less than 0.4 percent of all production loans and non-performing loans are less than 5 percent for both types of banks in the District and the United States. This improvement in the agricultural production loan portfolio has been largely a function of the improved agricultural economy during the last half of the decade.

## Summary

Commercial banks hold the largest share of total agricultural debt in both the United States and the Eighth Federal Reserve District. Other financial institutions, however, play important roles in the individual real estate and production loan markets. Agricultural loans at commercial banks are split almost evenly between agricultural and non-agricultural banks. In the District, non-agricultural banks' agricultural loan portfolios outperformed agricultural banks', in terms of loan losses and non-performing loans, during the 1984 to 1989 period. These measures of performance, however, are affected by loan write-offs prior to 1984. Finally, the agricultural loan portfolios of all commercial banks, on average, have improved significantly since the mid-1980s in both the District and the United States.

# Eighth District Business

Statistics

| | Level | Compounded Annual Rates of Change | | | |
|---|---|---|---|---|---|
| | II/1990 | I/1990-II/1990 | II/1989-II/1990 | 1989[1] | 1988[1] |
| **Payroll Employment** (thousands) | | | | | |
| United States | 110,699.0 | 1.7% | 2.2% | 2.8% | 3.3% |
| District | 6,878.9 | −1.5 | 1.6 | 2.9 | 3.5 |
| Arkansas | 915.2 | 1.9 | 3.0 | 3.0 | 3.5 |
| Little Rock | 248.9 | −1.9 | 2.1 | 3.0 | 3.5 |
| Kentucky | 1,462.2 | −2.4 | 2.5 | 3.8 | 4.1 |
| Louisville | 479.9 | −1.7 | 3.0 | 4.1 | 3.1 |
| Missouri | 2,327.4 | −1.1 | 1.0 | 2.2 | 2.8 |
| St. Louis | 1,184.7 | −1.8 | 1.1 | 2.3 | 2.3 |
| Tennessee | 2,174.1 | −2.8 | 1.1 | 3.0 | 4.0 |
| Memphis | 465.4 | −1.1 | 1.5 | 1.5 | 7.3 |
| **Manufacturing Employment** (thousands) | | | | | |
| United States | 19,382.0 | −0.6% | −1.4% | 1.1% | 2.0% |
| District | 1,473.5 | −1.6 | −0.3 | 2.0 | 3.2 |
| Arkansas | 231.1 | 1.0 | 0.3 | 1.6 | 3.1 |
| Kentucky | 285.2 | 1.3 | 0.4 | 3.6 | 4.5 |
| Missouri | 436.9 | −0.1 | −0.7 | 1.2 | 2.3 |
| Tennessee | 520.3 | −5.5 | −0.5 | 1.8 | 3.4 |
| **District Nonmanufacturing Employment** (thousands) | | | | | |
| Mining | 49.6 | −0.8% | −0.6% | −4.8% | −5.3% |
| Construction | 294.9 | −15.0 | 1.9 | 1.0 | 0.3 |
| FIRE[2] | 338.0 | −2.2 | 0.5 | 0.3 | 0.5 |
| Transportation[3] | 397.9 | −1.3 | 0.1 | 3.5 | 4.3 |
| Services | 1,546.5 | −1.1 | 3.4 | 5.1 | 6.3 |
| Trades | 1,644.8 | −4.0 | 1.3 | 3.0 | 3.7 |
| Government | 1,131.3 | 3.5 | 3.2 | 2.2 | 2.4 |

| | I/1990 | IV/1989-I/1990 | I/1989-I/1990 | 1989[1] | 1988[1] |
|---|---|---|---|---|---|
| **Real Personal Income[4]** (billions) | | | | | |
| United States | $3,545.6 | −0.2% | 1.6% | 2.5% | 3.4% |
| District | 196.3 | 2.9 | 1.5 | 2.2 | 2.8 |
| Arkansas | 26.2 | 20.6 | 1.9 | 2.0 | 2.9 |
| Kentucky | 42.2 | 5.9 | 1.7 | 2.5 | 2.8 |
| Missouri | 68.7 | −1.7 | 1.2 | 1.9 | 2.1 |
| Tennessee | 59.2 | −0.7 | 1.5 | 2.4 | 3.6 |

| | Levels | | | | |
|---|---|---|---|---|---|
| | II/1990 | I/1990 | 1989 | 1988 | 1987 |
| **Unemployment Rate** | | | | | |
| United States | 5.3% | 5.2% | 5.3% | 5.5% | 6.2% |
| District | 5.3 | 5.7 | 5.8 | 6.5 | 7.2 |
| Arkansas | 6.8 | 6.4 | 7.2 | 7.7 | 8.1 |
| Little Rock | 5.9 | 5.5 | 6.3 | 6.4 | 7.1 |
| Kentucky | 5.7 | 6.0 | 6.2 | 7.9 | 8.8 |
| Louisville | 4.9 | 5.4 | 5.6 | 6.3 | 6.9 |
| Missouri | 4.8 | 5.8 | 5.5 | 5.7 | 6.3 |
| St. Louis | 5.1 | 5.9 | 5.5 | 5.9 | 6.5 |
| Tennessee | 5.0 | 5.1 | 5.1 | 5.8 | 6.6 |
| Memphis | 4.6 | 4.4 | 4.7 | 5.2 | 5.7 |

Note: All data are seasonally adjusted. On this page only, the sum of data from Arkansas, Kentucky, Missouri and Tennessee is used to represent the District.

[1]Figures are simple rates of change comparing year-to-year data.
[2]Finance, Insurance and Real Estate
[3]Transportation, Communications and Public Utilities
[4]Annual rate. Data deflated by CPI-U, 1982-84 = 100.

# U. S. Prices

| | Level | Compounded Annual Rates of Change | | | |
|---|---|---|---|---|---|
| | II/1990 | I/1990-II/1990 | II/1989-II/1990 | 1989[1] | 1988[1] |
| **Consumer Price Index** (1982-84=100) | | | | | |
| Nonfood | 128.9 | 3.8% | 4.5% | 4.7% | 4.0% |
| Food | 131.5 | 1.5 | 5.4 | 5.8 | 4.1 |
| **Prices Received by Farmers** (1977=100) | | | | | |
| All Products | 152.0 | 7.4% | 2.5% | 7.0% | 8.8% |
| Livestock | 172.0 | 3.1 | 10.3 | 6.7 | 2.7 |
| Crops | 131.3 | 13.2 | −6.4 | 7.2 | 18.3 |
| **Prices Paid by Farmers** (1977=100) | | | | | |
| Production items | 169.0 | 2.4% | 1.2% | 6.2% | 6.9% |
| Other items[2] | 183.0 | 4.5 | 3.4 | 4.4 | 4.4 |

Note: Data not seasonally adjusted except for Consumer Price Index.

[1]Figures are simple rates of change comparing year-to-year data.
[2]Other items include farmers' costs for commodities, services, interest, wages and taxes.

# Eighth District Banking

## Changes in Financial Position for the year ending March 31, 1990 *(by Asset Size)*

| | Less than $100 million | $100 million - $300 million | $300 million - $1 billion | More than $1 billion |
|---|---|---|---|---|
| **SELECTED ASSETS** | | | | |
| **Securities** | −2.3% | 10.6% | 7.0% | 18.5% |
| U.S. Treasury & agency securities | −0.2 | 15.2 | 13.3 | 28.7 |
| Other securities[1] | −9.0 | 0.5 | −6.5 | −2.4 |
| **Loans & Leases** | 0.2 | 6.7 | 14.3 | 5.3 |
| Real estate | 2.8 | 9.2 | 24.4 | 13.6 |
| Commercial[2] | −9.0 | −1.0 | 5.9 | 1.5 |
| Consumer | 0.8 | 7.1 | 12.7 | 6.5 |
| Agriculture | 7.0 | 28.1 | 30.8 | −3.1 |
| Loan loss reserve | −0.6 | 13.5 | 14.6 | 12.2 |
| **Total Assets** | −0.4 | 8.5 | 11.2 | 6.7 |
| **SELECTED LIABILITIES** | | | | |
| **Deposits** | −0.3% | 9.0% | 10.9% | 3.4% |
| Nontransaction accounts | 0.4 | 11.1 | 13.1 | 6.2 |
| MMDAs | −12.4 | 0.2 | 4.2 | 18.7 |
| $100,000 CDs | 4.3 | 7.8 | 4.7 | −11.8 |
| Demand deposits | −4.7 | 0.7 | 2.4 | −3.9 |
| Other transaction accounts[3] | −0.6 | 5.8 | 9.9 | 0.8 |
| **Total Liabilities** | −0.4 | 8.6 | 11.0 | 6.5 |
| **Total Equity Capital** | 0.2 | 8.1 | 13.3 | 10.8 |

Note: All figures are simple rates of change comparing year-to-year data. Data are not seasonally adjusted.

[1]Includes state, foreign and other domestic, and equity securities
[2]Includes banker's acceptances and nonfinancial commercial paper
[3]Includes NOW, ATS and telephone and preauthorized transfers

# *Performance Ratios* *(by Asset Size)*

| | Eighth District | | | United States | | |
|---|---|---|---|---|---|---|
| | I/90 | I/89 | I/88 | I/90 | I/89 | I/88 |
| **EARNINGS AND RETURNS** | | | | | | |
| **Annualized Return on Average Assets** | | | | | | |
| Less than $100 million | 1.08% | 1.13% | 1.08% | .82% | .92% | .74% |
| $100 million - $300 million | 1.05 | 1.08 | 1.04 | .97 | 1.04 | .83 |
| $300 million - $1 billion | 1.05 | 1.14 | 1.08 | .84 | .93 | .66 |
| $1 billion - $10 billion | .78 | .90 | .86 | .70 | .95 | .72 |
| More than $10 billion | — | — | — | .75 | .93 | .54 |
| Agricultural banks | 1.21 | 1.24 | 1.17 | 1.05 | 1.14 | 1.01 |
| **Annualized Return on Average Equity** | | | | | | |
| Less than $100 million | 11.66% | 12.42% | 11.96% | 8.98% | 10.29% | 8.42% |
| $100 million - $300 million | 12.84 | 13.17 | 12.69 | 12.12 | 13.02 | 10.68 |
| $300 million - $1 billion | 13.12 | 14.59 | 13.69 | 11.28 | 12.94 | 9.55 |
| $1 billion - $10 billion | 11.90 | 13.52 | 13.35 | 10.76 | 14.61 | 11.59 |
| More than $10 billion | — | — | — | 15.10 | 17.85 | 12.21 |
| Agricultural banks | 12.36 | 13.00 | 12.26 | 10.86 | 12.02 | 10.83 |
| **Net Interest Margin**[1] | | | | | | |
| Less than $100 million | 3.99% | 4.01% | 3.92% | 4.15% | 4.27% | 4.24% |
| $100 million - $300 million | 3.96 | 4.04 | 3.91 | 4.33 | 4.56 | 4.19 |
| $300 million - $1 billion | 4.13 | 4.17 | 3.98 | 4.35 | 4.51 | 4.15 |
| $1 billion - $10 billion | 3.66 | 3.82 | 3.62 | 4.23 | 4.27 | 4.09 |
| More than $10 billion | — | — | — | 3.23 | 3.52 | 3.30 |
| Agricultural banks | 3.89 | 3.93 | 3.85 | 4.00 | 4.14 | 4.03 |
| **ASSET QUALITY**[2] | | | | | | |
| **Nonperforming Loans**[3] | | | | | | |
| Less than $100 million | 1.68% | 1.70% | 2.10% | 2.08% | 2.88% | 2.69% |
| $100 million - $300 million | 1.66 | 1.73 | 1.93 | 2.03 | 1.88 | 2.24 |
| $300 million - $1 billion | 1.42 | 1.52 | 1.61 | 2.44 | 2.59 | 2.44 |
| $1 billion - $10 billion | 1.90 | 1.92 | 2.46 | 2.46 | 1.90 | 2.40 |
| More than $10 billion | — | — | — | 4.61 | 4.63 | 5.31 |
| Agricultural banks | 1.81 | 1.96 | 2.66 | 2.24 | 2.50 | 3.30 |
| **Loan Loss Reserves** | | | | | | |
| Less than $100 million | 1.47% | 1.48% | 1.51% | 1.56% | 1.53% | 1.67% |
| $100 million - $300 million | 1.51 | 1.42 | 1.34 | 1.49 | 1.47 | 1.55 |
| $300 million - $1 billion | 1.38 | 1.38 | 1.36 | 1.71 | 1.64 | 1.69 |
| $1 billion - $10 billion | 1.69 | 1.65 | 2.15 | 1.96 | 1.69 | 1.91 |
| More than $10 billion | — | — | — | 3.82 | 3.62 | 4.36 |
| Agricultural banks | 1.74 | 1.89 | 1.90 | 2.07 | 2.13 | 2.16 |
| **Net Loan Losses**[4] | | | | | | |
| Less than $100 million | .07% | .07% | .08% | .10% | .12% | .16% |
| $100 million - $300 million | .08 | .10 | .08 | .10 | .12 | .13 |
| $300 million - $1 billion | .10 | .07 | .08 | .16 | .16 | .15 |
| $1 billion - $10 billion | .21 | .10 | .19 | .35 | .19 | .23 |
| More than $10 billion | — | — | — | .45 | .20 | .26 |
| Agricultural banks | .04 | .04 | .08 | .07 | .09 | .15 |

Note: Agricultural banks are defined as those with 25 percent or more of their total loan portfolio in agriculture loans.

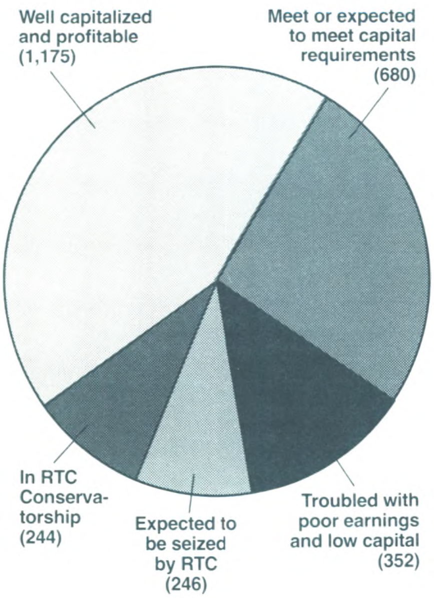
[1]Interest income less interest expense as a percent of average earning assets
[2]Asset quality ratios are calculated as a percent of total loans.
[3]Nonperforming loans include loans past due more than 89 days, nonaccrual, and restructured loans.
[4]Loan losses are adjusted for recoveries.

# Resolving the Thrift Crisis—A FIRREA Update

*by Michelle A. Clark*

Just over one year has passed since President Bush signed the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA). Although the legislation addressed a variety of issues facing U.S. financial institutions, its main thrust was a "housecleaning" of the savings and loan (thrift) industry. Over the course of the 1980s, the industry incurred massive losses and failures arising from local recessions, fraud, mismanagement and a regulatory structure that encouraged excessive risk-taking. Although estimates of the cleanup's ultimate cost vary substantially, most estimates are in the $130 billion to $500 billion range. As of August 1990, the industry consisted of almost 2,700 institutions in various stages of financial health, a breakdown of which is detailed below.

State of the Thrift Industry
Number of Institutions by Category
August 1990




*Source: Office of Thrift Supervision; Resolution Trust Corporation*

Less than one-half of all thrifts are currently categorized as healthy, that is, well-capitalized and profitable, by the Office of Thrift Supervision (OTS). An additional 25 percent already meet or are expected to meet new minimum capital requirements in the near future. Absent a protracted economic downturn, the OTS expects these two groups of thrifts to survive the industry restructuring. The remaining third of the industry consists of troubled institutions and those already seized or expected to be seized by the government.

In addition to provisions that restructured the regulatory oversight and allowable activities of thrifts, a number of FIRREA's provisions facilitated the closure or sale of insolvent thrifts. To that end, the Resolution Trust Corporation (RTC) was established. The RTC is responsible for managing and disposing of bankrupt thrifts and for selling the repossessed real estate acquired by the now-defunct Federal Savings and Loan Insurance Corporation (FSLIC). The RTC was given three years starting in 1989 to liquidate or sell insolvent thrifts that were once insured by FSLIC and that are in conservatorship (federally operated) or receivership (closed). The agency has an additional four years to dispose of acquired assets, such as residential and commercial mortgages. The RTC's toughest task will be selling so-called "white elephant" properties, many of which are located in the country's softest real estate markets.

As of August 27, 244 thrifts in 36 states and Puerto Rico were in RTC conservatorship. These federally controlled thrifts had $144 billion in assets and $118 billion in deposits as of year-end 1989. California and Texas, with 76 thrifts between them in the conservatorship program, account for about a third of all thrifts in conservatorship and more than a quarter of the total assets of thrifts in the program. In contrast, just 21 of the thrifts in conservatorship are located within the Eighth District; their combined assets amounted to 3.5 percent of the U.S. total. Within the District, Arkansas thrifts appear to be the most troubled, as almost a quarter of the state's thrifts are in conservatorship. The state-by-state breakdown for the District is as follows:

**Eighth District Thrifts in RTC Conservatorship**

| State | Number in Conservatorship | Total Assets (in US$ millions) |
|---|---|---|
| AR | 9 | $2,588 |
| IL | 6 | 1,281 |
| IN | 0 | --- |
| KY | 1 | 50 |
| MO | 2 | 714 |
| MS | 3 | 385 |
| TN | 0 | --- |
| TOTAL | 21 | $5,018 |

SOURCE: Resolution Trust Corporation Fact Sheet, August 27, 1990.