Ag Finance Update

Real Estate Lending Pushes Farm Debt Higher

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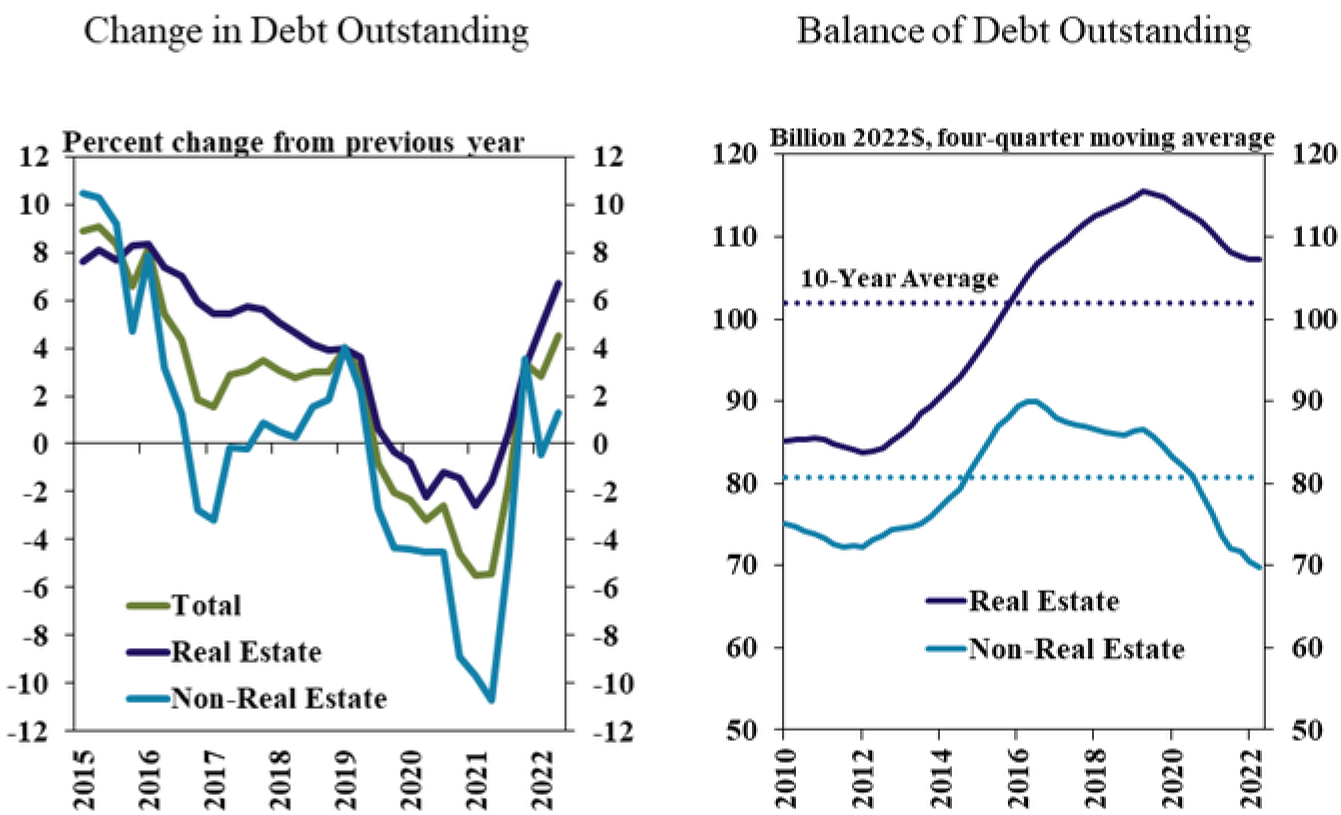
Strong growth in farm real estate debt pushed agricultural loan balances higher at commercial banks in the second quarter. Outstanding farm debt increased about 5% from the previous year, the fastest pace in nearly six years. While agricultural real estate loans continued to build, production lending rose modestly following subdued demand in recent years. Loan performance also improved further. Recent loan growth supported a slight improvement in interest margins and income at agricultural banks from last quarter, but bank liquidity remained abundant.

The agricultural economy remained steady over the past quarter, providing ongoing support to farm finances. The price of most major commodities remained elevated and the outlook for profit opportunities across the sector in 2022 was positive despite heightened volatility in some markets. With substantially higher production costs and weather risks, incomes could be pressured if commodity prices drop more notably, and credit needs could also be pushed higher. Despite growing risks, farm balance sheets remained strong alongside high liquidity, and a sharp increase in farm real estate values also continued to support agricultural credit conditions.

Second Quarter Commercial Bank Call Report Data

An acceleration of farm real estate debt drove further growth in agricultural loan balances. Agricultural real estate loans grew by almost 7% from a year ago and outstanding balances remained above the average of the past 10 years (Chart 1). Non-real estate farm debt showed additional signs of rebounding, increasing modestly following nearly two years of considerable retraction; but balances remained well below the recent average.

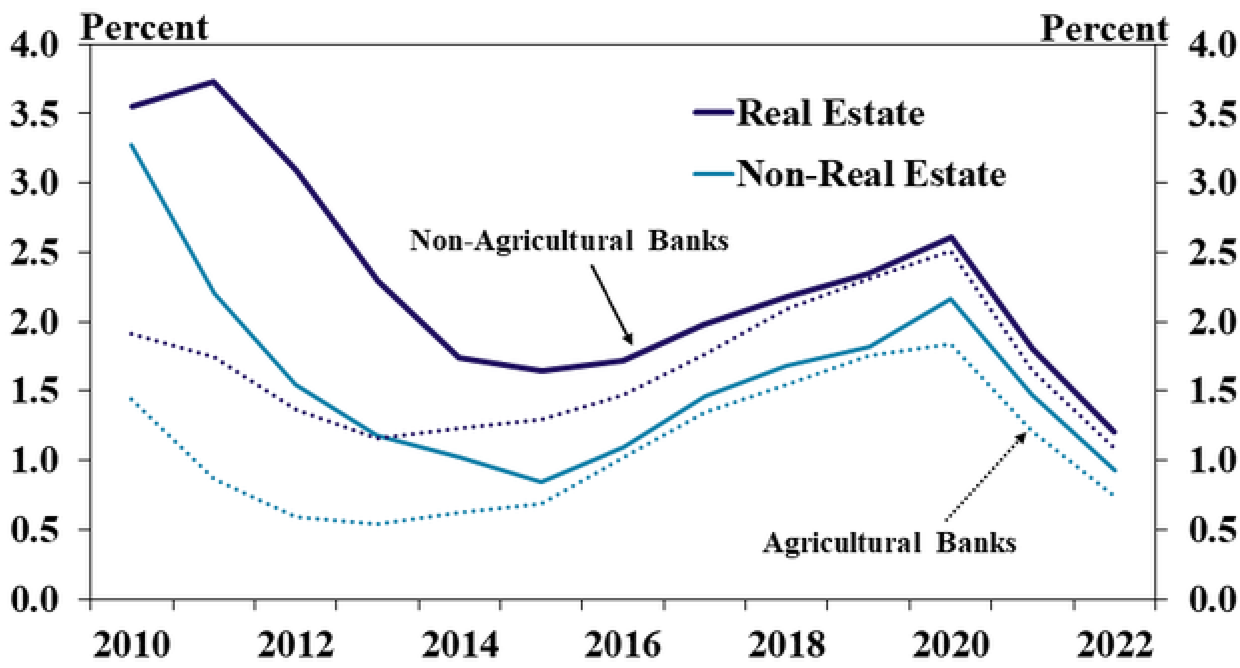
Chart 1: Farm Debt Outstanding at Commercial Banks



Sources: Reports of Condition and Income and Federal Reserve Board of Governors

As debt balances grew, loan performance continued to improve alongside strength in farm finances. The delinquency rate on real estate and non-real estate farm loans at both agricultural and non-agricultural banks declined for the seventh consecutive quarter (Chart 2). Problem loan rates on real estate loans reached a historic low and delinquencies on production loans also edged towards all-time lows.

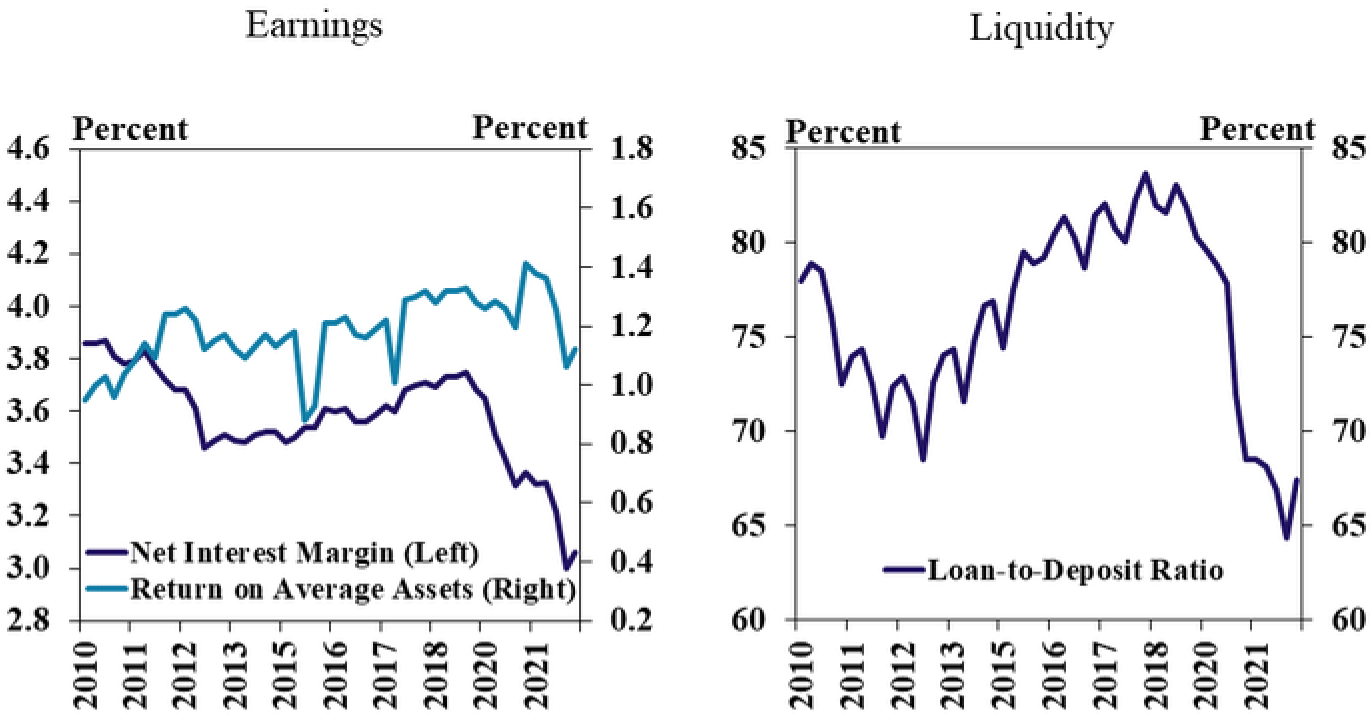
Chart 2: Farm Loan Delinquency Rates, Q2



Note: Delinquent farm loans include all agricultural loans past due 30 or more days or non-accruing. Agricultural Banks include all banks with farm loans comprising at least 25% of total loans.
Sources: Reports of Condition and Income and Federal Reserve Board of Governors

Earnings performance at agricultural banks improved slightly alongside recent growth in lending and an increase in interest rates. Following two years of steady contraction, the net interest margin increased slightly during the quarter and supported a modest improvement in bank profits (Chart 3, left panel). The uptick in interest income coincided with growth in loan balances, but liquidity among farm lenders remained ample (Chart 3, right panel).

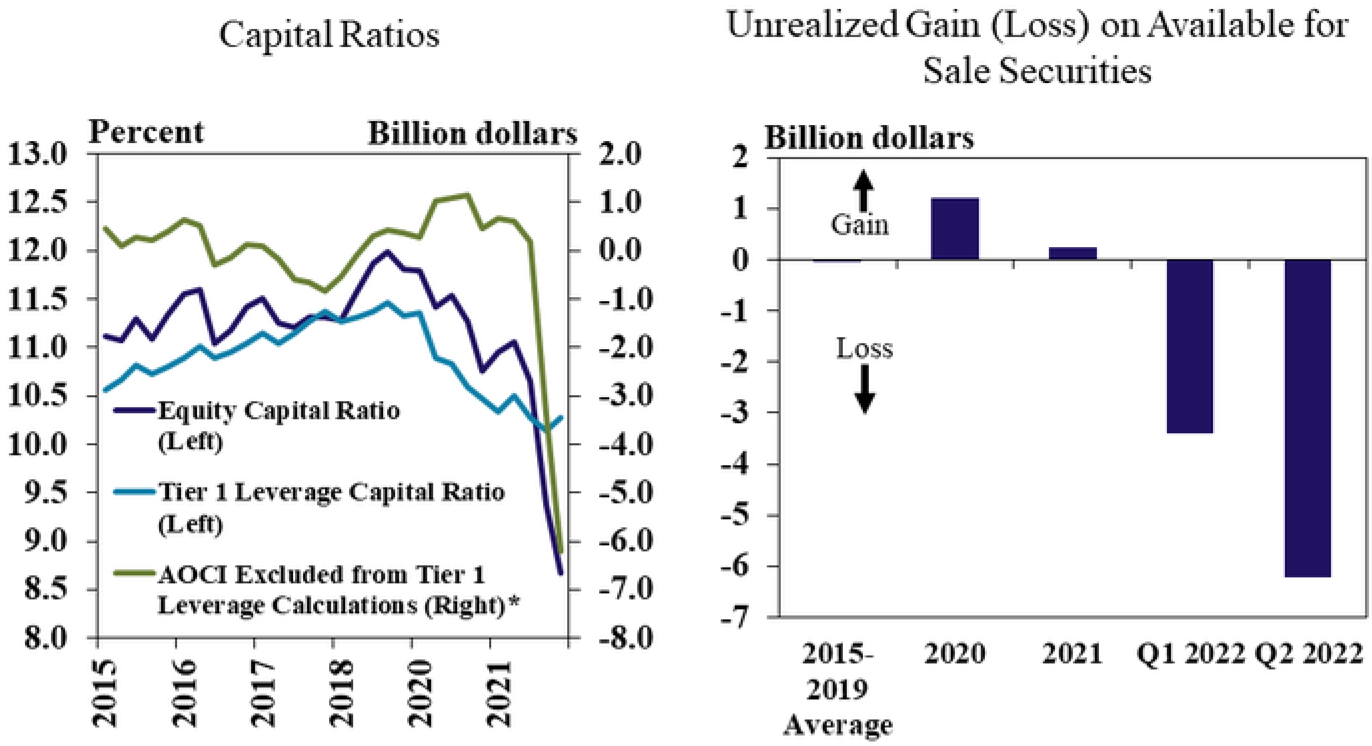
Chart 3: Select Financial Indicators at Agricultural Banks



Source: Reports of Condition and Income and Federal Reserve Board of Governors

Capital ratios at agricultural banks monitored for regulatory purposes steadied, but some measures of equity dropped considerably due to recent developments in securities markets. The Tier 1 Leverage Capital ratio remained sound and increased slightly from the previous quarter, but the equity capital ratio dropped sharply (Chart 4). Substantial accumulated loss that is excluded in the measure of Tier 1 Leverage Capital accounted for the difference between the two measures. The losses were attributed to significant downward adjustments to the value of longer-term investment securities held by banks that would only affect income following a sale and are typically excluded from measures of capital used to gauge overall conditions at most banks.

Chart 4: Capital and Accumulated Other Comprehensive Income (AOCI) at Agricultural Banks



*Banks may elect to "opt-out" of including AOCI in the calculation of Tier 1 Leverage Capital utilized for regulatory purposes. However, these amounts are included in the calculation of the equity capital variable utilized in the Ag Finance Update – Commercial Bank Call Report data tables.
Note: All ratios and items above are calculated using the panel of 1,062 agricultural banks from Q2 2022.
Source: Reports of Condition and Income and Federal Reserve Board of Governors

Data and Information

Commercial Bank Call Report Historical Data

Commercial Bank Call Report Data Tables

About the Commercial Bank Call Report Data

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Nate Kauffman is Senior Vice President and Omaha Branch Executive at the Federal Reserve Bank of Kansas City. In his role as the Kansas City Fed's lead economist and representative in the state of Nebraska, Nate provides strategic direction and oversight for the Omaha Branch, regional research, and economic outreach throughout the state. He serves as a local connection to the nation’s central bank and is responsible for briefing the Kansas City Fed’s president – a member of the Federal Open Market Committee – on regional economic and business activity.In addition, Nate is the Kansas City Fed’s principal expert in agricultural economics. He is a leading voice on the agricultural economy throughout the seven states of the Tenth Federal Reserve District and the broader Federal Reserve System. Nate oversees several Bank and Federal Reserve efforts to track agricultural economic and financial conditions. He also speaks regularly on the agricultural economy to industry audiences and the news media, including providing testimonies at both U.S. Senate and U.S. House Agriculture Committee hearings.Nate joined the Federal Reserve in 2012. He received his Ph.D. in economics from Iowa State University. Prior to receiving his Ph.D., Nate spent three years in Bosnia and Herzegovina coordinating agricultural economic development projects.Nate lives in Omaha with his wife and four children.

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