Agricultural Finance Databook

NATIONAL TRENDS IN FARM LENDING

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Farm Lending Soars at Commercial Banks

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Farm lending at commercial banks accelerated in the fourth quarter after solid gains in previous months. According to a November survey of U.S. commercial banks, bank lending for feeder livestock and current operating expenses rose sharply compared to last year. Escalating feed and livestock costs contributed to higher lending activity to livestock operations. In addition, high fuel costs during harvest and rising fertilizer and seed prices prompted crop producers to pre-pay for 2013 crop inputs. As a result, non-real estate loan volumes for current operating expenses, including crop inputs and feed, doubled year-ago volumes, and loan volumes for feeder livestock remained well above a year ago.

Banker survey respondents also reported a fourth-quarter spike in farm machinery and equipment loans. After picking up in the third quarter, lending for farm machinery and equipment surged as farmers made capital purchases prior to the expiration of accelerated depreciation at the end of 2012. In addition, lending for other intermediate loans for unspecified purposes also rose sharply during the quarter.

During the third quarter, farmland values climbed higher following an early harvest. The drought appeared to have little effect on the demand for farmland, especially in the Corn Belt and Central Plains where prices reached another record high. With a robust farmland market, commercial banks reported a surge in farm real estate loan volumes heading into the fourth quarter. Elevated farmland prices and potential changes in tax policies motivated more land owners to sell before the end of the year. As a result, most agricultural bankers expected gains in farmland values to moderate during the next year and level off at record high levels.

With ample funds for farm loans, strengthening loan demand fueled intense competition for agricultural lending activity among financial institutions. Farm interest rates fell to new lows, with some banks easing collateral requirements. Interest rates were the lowest at large banks that offered more loans with floating interest rates. Loan-to-deposit ratios firmed with higher loan volumes, and the average return on assets at agricultural banks reached a five-year high during the third quarter.

Section A
Fourth Quarter National Farm Loan Data

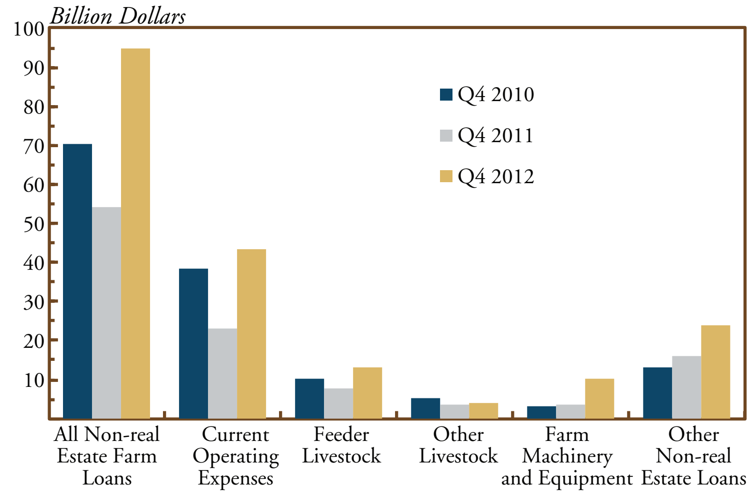
According to the national Survey of Terms of Bank Lending to Farmers, conducted during the first full week of November, the volume of loans made to farmers jumped during the fourth quarter. Total volumes for non-real estate farm loans rose at the fastest pace in three years during the quarter as commercial banks made more loans at higher average amounts (Chart 1). Farm real estate loan originations also accelerated during the quarter. Farm interest rates fell to historic lows, with sharper declines at large commercial banks that used floating interest rates on farm machinery loans.

Rising production costs fueled farm lending during the fourth quarter. Loan volumes for feeder livestock rose further as prices for feeder livestock remained high due to short supplies resulting from past herd liquidations. Current operating loans to livestock producers also remained high with elevated feed costs. In addition, rising fertilizer and seed prices enticed some crop producers to pre-pay for 2013 inputs, which boosted current operating loan volumes even higher.

A rush of capital spending before potential tax law changes lifted intermediate-term farm lending during the fourth quarter. Tax provisions allowing accelerated depreciation on qualifying farm asset purchases such as machinery, equipment, and special–use or single–purpose agribusiness buildings, including grain bins, drying systems, and livestock barns, were set to expire at the close of 2012. Producers taking advantage of the tax incentive helped to more than double the volume of farm machinery and equipment loans compared with last year. Intermediate-term loans for other, unspecified purposes also rose sharply according to the loan survey data.

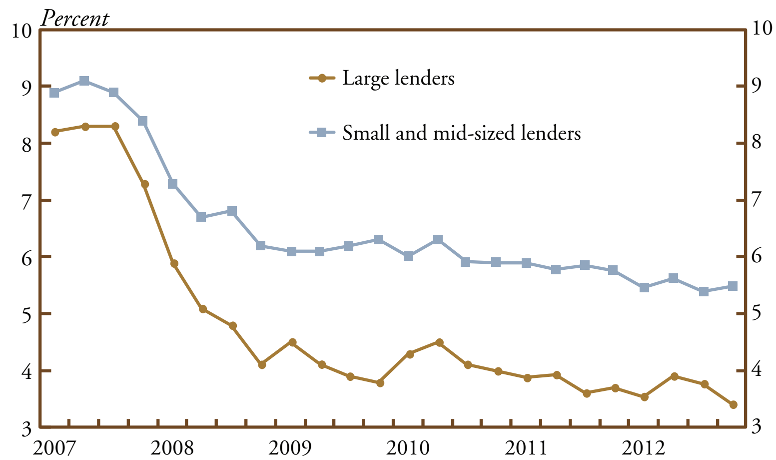
Non-real estate farm loan portfolios expanded rapidly at agricultural banks of all sizes. Average effective interest rates fell at large lenders, or those with more than $25 million in farm loans, and they captured a greater percentage of the growth in non-real estate farm loans compared to small- and mid-sized banks where interest rates held relatively steady (Chart 2).

Chart 1: Non-real Estate Farm Loan Volumes by Purpose



Source: Agricultural Finance Databook, Table A.3.

Chart 2: Average Effective Interest Rates on New Non-Real Estate Farm Loans by Size of Lender



Source: Agricultural Finance Databook, Table A.5.
Note: Large lenders typically had more than $25 million in farm loans, small and mid-sized lenders typically had less than $25 million in farm loans.

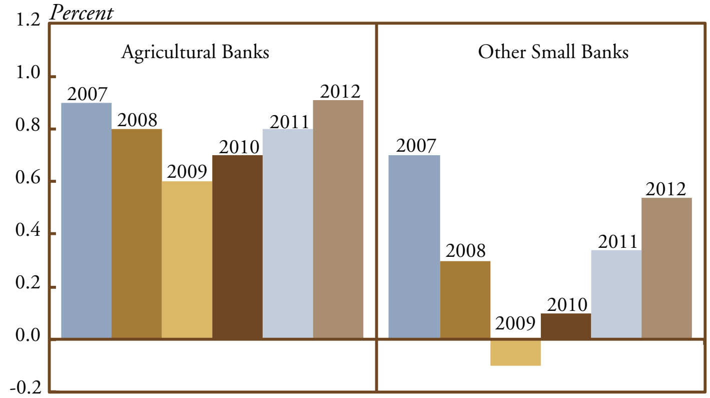
Section B
Third Quarter Call Report Data

The financial performance of agricultural banks strengthened in the third quarter, especially when compared with other small banks. The rate of return on assets at agricultural banks was 0.9 percent at the end of the third quarter, surpassing the 0.5 percent return at other small banks (Chart 3). Similarly, the average rate of return on equity at agricultural banks was almost 8.0 percent in the third quarter, compared with roughly 5.0 percent at other small banks. Stronger profits lifted average capital ratios at agricultural banks to record highs.

Commercial banks saw a jump in farm lending during the third quarter after drought and rising input costs cut farm income. Farm debt outstanding at all commercial banks rose 4.0 percent above year-ago levels in the third quarter, driven by non-real estate loan originations. The volume of non-real estate farm loans swelled more than 5.0 percent compared with last year, and farm real estate loan volumes rose more than 3.0 percent annually. Despite higher loan volumes, an increase in deposits kept the average loan-to-deposit ratio at agricultural banks near historic lows.

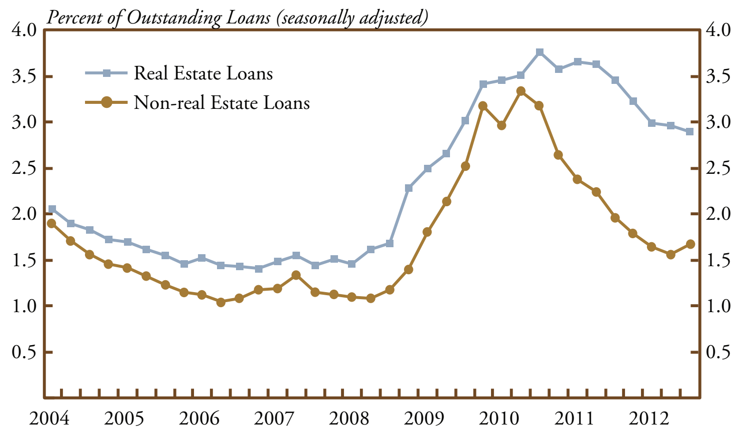
Farm loan delinquency rates held relatively steady. During the third quarter, delinquency rates on farm real estate loans dipped to 2.9 percent and remained well below delinquency rates on non-farm residential or commercial real estate loans (Chart 4). At the same time, delinquency rates on non-real estate farm loans edged up to 1.7 percent, but remained near its four-year low. Low delinquency rates contributed to a slight decline in charge-off rates for both real estate and non-real estate farm loans at commercial banks. Still, delinquency and charge-off rates remained substantially higher at the largest 100 U.S. banks, when compared with other commercial banks.

Chart 3: Rate of Return on Assets (Third Quarter)



Source: Agricultural Finance Databook, Table B.7.

Chart 4: Delinquent Farm Loans



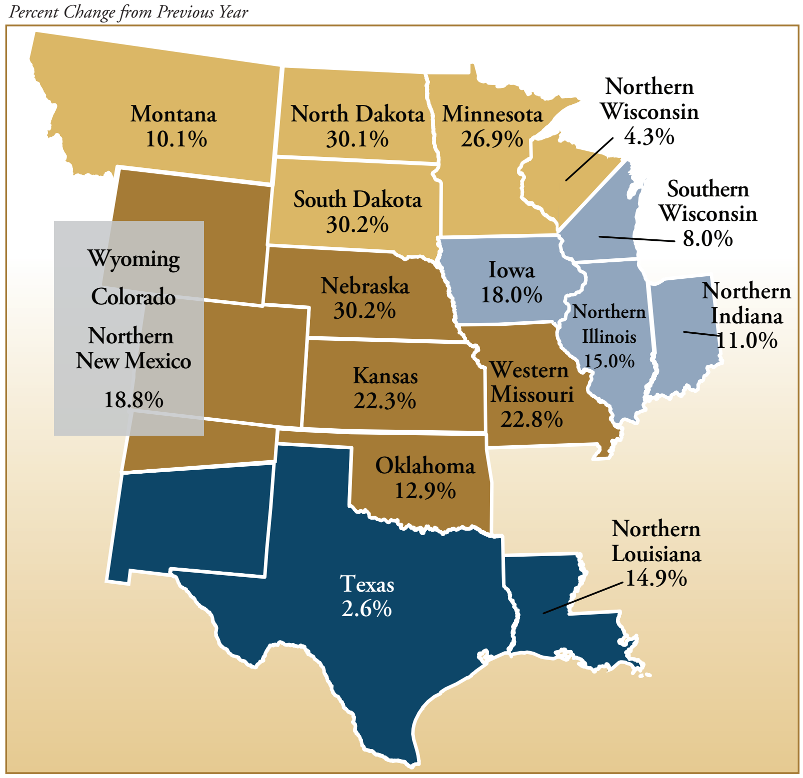
Source: Federal Reserve Board of Governors.

Section C
Third Quarter District Agricultural Conditions

Despite severe drought, farmland values continued to rise across most crop-growing regions in the third quarter. Bankers in the Corn Belt and the Central Plains reported strong year-over-year farmland value gains, with stronger gains in the western Corn Belt (Map 1). High crop prices and elevated crop insurance payments underpinned farm incomes and land values. Land lease revenues from energy production continued to propel farmland values in the Dakotas where non–irrigated cropland values were more than 30 percent above year-ago levels. In contrast, farmland values in Texas were little changed following a second year of poor growing conditions and parched pastures. Agricultural bankers in the Kansas City, Dallas and San Francisco Districts reported stronger annual gains in values for irrigated cropland compared with non-irrigated cropland and ranchland. Even with low soil moisture levels heading into 2013, very few bankers expected farmland values would retreat from their current highs, and most expected them to remain elevated in 2013.

Map 1: Value of Non-Irrigated Cropland (Third Quarter, 2012)

Percent Change from Previous Year



Source: Federal Reserve District Agricultural Credit Surveys (Chicago, Minneapolis, Kansas City, Dallas)

Bankers reported that farm lending varied with the severity of the drought. In the Kansas City and Dallas Districts, severe drought raised feed costs for livestock operators and trimmed farm incomes but spurred operating loan demand for feed. In contrast, rising incomes in the Minneapolis and San Francisco Districts dampened operating loan demand but boosted farm capital spending. Demand for dairy loans remained stable in the Chicago and Dallas Districts while demand for feeder cattle loans was expected to weaken. Richmond anticipated rising loan volumes driven by feeder cattle, operating and farm machinery loans. Most bankers reported lower interest rates for both real estate and non-real estate loans, with the exceptions of interest rates on short-term feeder cattle loans in the Dallas District, long-term real estate loans in the San Francisco District, and operating loans in both those districts.

Farm credit conditions eased somewhat in the third quarter. According to Federal Reserve District Agricultural Credit Surveys, fewer bankers reported higher loan repayment rates during the quarter. Still, loan renewals and extensions held at low levels in most districts. The availability of funds for farm loans remained high, and very few farm loans were referred to correspondent banks or non-bank credit agencies. Collateral requirements for non-real estate farm loans were mixed, as requirements eased in St. Louis and San Francisco, held steady in Chicago and Dallas, and tightened slightly in Richmond, Kansas City, and Minneapolis.