Agricultural Finance Databook

NATIONAL TRENDS IN FARM LENDING

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Farm Loan Volumes Rise and Agricultural Finances Strengthen

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Non-real estate farm loan volumes rose in the first quarter, led by a surge in capital spending that boosted intermediate-term loan volumes. According to loan survey data from the week of Feb. 6, 2012, loans for farm machinery and equipment held at high levels with a sharp jump in the volume of intermediate-term loans made for unspecified purposes. With low cow inventories lifting feeder cattle prices, banks also made larger short-term loans to the livestock sector. However, strong farm income for crop producers kept operating loan volumes relatively flat heading into planting season. Farm loan portfolios at small and mid-sized banks increased by almost a third compared to last year, and farm loan portfolios at large lenders grew by more than 20 percent.

Though loan volumes rose at both large and small agricultural lenders in the first quarter, the composition of their farm loan portfolios varied. Large banks made more intermediate-term loans that were typically rated as moderate risk. Small and mid-sized banks had a larger share of short-term operating and livestock loans that were generally rated as low risk. However, small and mid-size lenders also had a higher concentration of long-term farm real estate loans in their farm loan portfolios compared with large lenders, heightening their exposure to a potential correction in the farmland market.

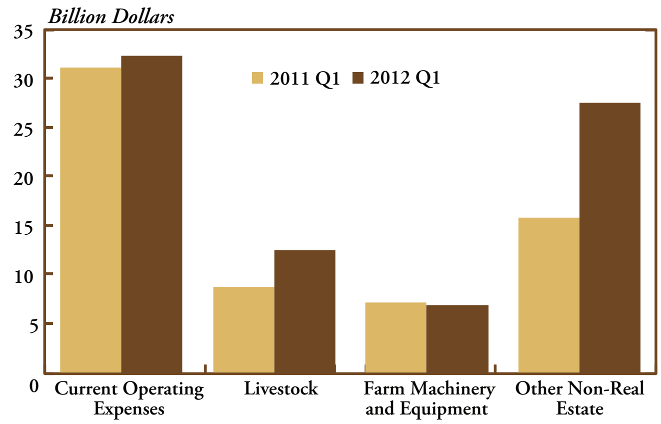
Agricultural banks ended 2011 with their best financial performance in three years. The return on assets at agricultural banks in the fourth quarter rose for the second straight year, and annual net income distributions strengthened. Producers paid down debt with elevated farm incomes, reducing delinquency rates and net charge-offs for both farm real estate and non-real estate loans. Bankers reported plenty of funds were available for farm loans at historically low interest rates.

Farmland values continued to climb even with more farmland for sale at year-end. As farmland values soared by as much as 40 percent compared to last year, an increasing number of landowners auctioned off their land holdings. While non-farm investor interest helped keep bidding brisk, farmers remained the main purchasers of farmland, particularly when prices reached record levels.

Section A
First Quarter National Farm Loan Data

A rise in capital spending and larger loans to the livestock sector expanded non-real estate farm loan portfolios in the first quarter. According to loan survey data collected Feb. 6-10, 2012, non-real estate loan volumes rose 26 percent compared with last year, driven by a spike in intermediate-term, large loans for unspecified "other" purposes (Chart 1). In addition, first quarter loan volumes for farm machinery and equipment approached the peak levels seen last year. Average effective interest rates on farm machinery and equipment loans edged up to 4.8 percent in the first quarter.

Chart 1: Farm Loan Volumes by Purpose

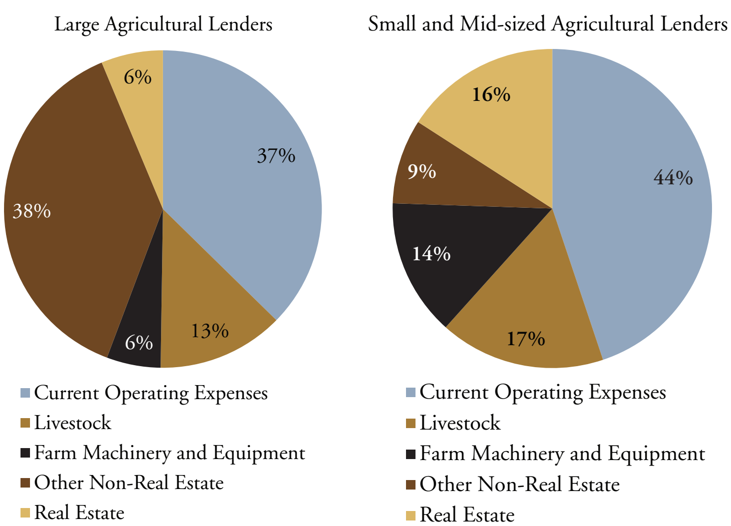


Source: Agricultural Finance Databook, Section A

High feeder livestock prices boosted the volume of short-term loans made to the livestock sector in the first quarter. A steady decline in cow inventories limited supplies and supported higher prices for feeder cattle. With strong demand for meat, particularly from foreign markets, livestock feeders borrowed to maintain production levels. In fact, the average size of feeder livestock loans rose above $100,000 three out of the last four quarters. Average effective interest rates on feeder livestock loans increased to 5.2 percent in the first quarter.

First quarter operating loan volumes remained below historical averages but were comparable to year-ago levels. Strong farm income during the past couple of years lessened the need for short-term operating loans to finance production inputs. Average effective interest rates on operating loans held steady at 5.0 percent in the first quarter.

Chart 2: Share of Total Farm Loan Volume (First Quarter 2012)



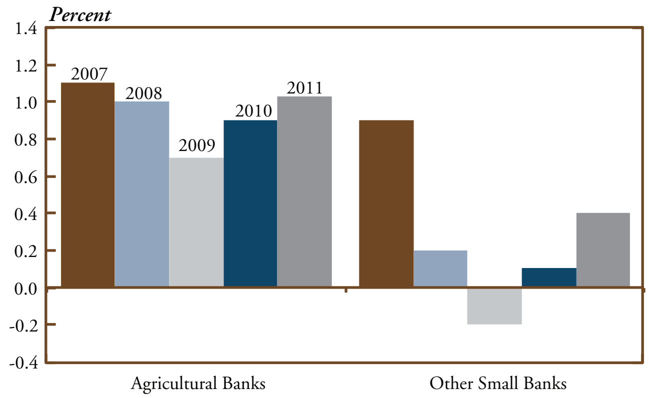
Source: Agricultural Finance Databook, Section A
Note: Large lenders had $25 million or more in their farm loan portfolio.
Small and mid-sized lenders had less than $25 million in their farm loan portfolio.

While loan volumes expanded at all commercial banks in the first quarter, the composition and risk ratings of farm loan portfolios varied by lender size. Farm loan portfolios at large agricultural banks (more than $25 million in farm loans) had a higher concentration of "other" loans for unspecified purposes (Chart 2). Operating loans represented the largest share of loan portfolios at small and mid-sized agricultural banks (less than $25 million in farm loans), with other loan categories more evenly spread. Large lenders classified the vast majority, 85 percent, of rated farm loans as moderate or higher risk while most farm loans at small and mid-sized lenders carried a low or minimal risk rating.

Section B
Fourth Quarter Call Report Data

Bank profits rose with higher loan repayment rates and declining loan delinquencies. The rate of return on assets at agricultural banks topped 1.0 percent, compared with 0.4 percent at other small banks (Chart 3). The average rate of return on equity at agricultural banks rose to 9.3 percent in the fourth quarter, well above the 3.8 percent reported for other small banks. In addition, the percentage of agricultural banks with negative income as a share of average equity fell to a 4-year low. With stronger profits, average capital ratios at both agricultural banks and other small banks rose compared with last year. Moreover, there were only four agricultural bank failures in 2011, a small share of the more than 90 commercial bank closures during the year.

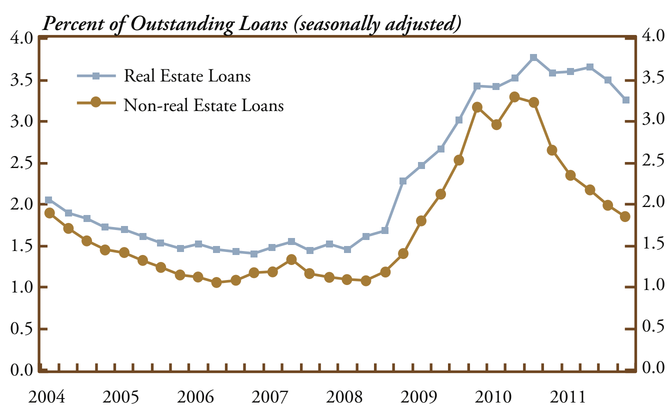
Chart 3: Rate of Return on Assets (Fourth Quarter)



Source: Agricultural Finance Databook, Section B

Non-real estate farm loan performance strengthened further in the fourth quarter. The share of delinquent non-real estate loans dipped below 2.0 percent for the first time in three years (Chart 4). Loan delinquency rates improved to 4.1 percent at the 100 largest banks, but remained much higher than the 0.8-percent rate at other commercial banks. Net charge-off volumes for non-real estate farm loans plummeted in 2011, falling by two-thirds compared with the previous year. A fourth quarter rise in loan volume lifted non-real estate farm debt outstanding at all commercial banks 3.1 percent above 2010 levels.

Chart 4: Delinquent Farm Loans



Source: Federal Reserve Board of Governors

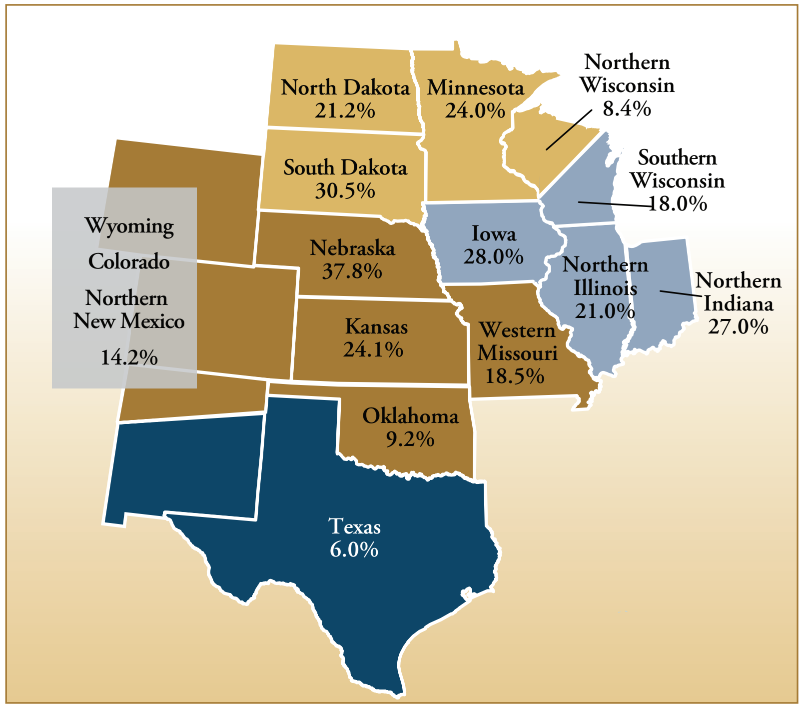
Loan performance measures for farm real estate loans also improved at year-end. The share of delinquent farm real estate loans fell for the second straight quarter, dropping to 3.3 percent. Still, the loan delinquency rate at the 100 largest banks was 5.2 percent in the quarter, far eclipsing the 2.7 percent at other commercial banks. Annual net charge-off volumes for farm real estate loans declined modestly from their peak in 2010. Compared with last year, farm real estate loan volumes at all commercial banks edged up 0.6 percent in the fourth quarter.

Section C
Fourth Quarter District Agricultural Conditions

Farmland values reached record highs in many crop-producing regions, even with an increase in the number of farms for sale. Since last year, the average value of nonirrigated cropland rose more than 30 percent in Nebraska and South Dakota and more than 20 percent in Kansas, Iowa, Minnesota, North Dakota, northern Illinois and northern Indiana (Map 1). Irrigated cropland also posted strong value gains, particularly in drought areas of the southern Plains, where supplemental water aided crop development. Bankers in the Kansas City District noted more farmland on the market compared with last year as record values enticed some landowners to sell. Still, robust demand for farmland, especially from farmers, drove prices higher. In fact, some bankers in the Chicago, Kansas City and Richmond Districts expected the upward trend in farmland values would continue into 2012.

Map 1: Non-Irrigated Cropland (Fourth Quarter 2011)

Percent change from prior year



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

Overall demand for farm loans remained weak in the fourth quarter despite additional capital spending at year-end. Bankers in the Chicago, Kansas City, Minneapolis and Richmond Districts noted increased capital spending at the close of 2011 as producers upgraded equipment and completed construction of farm buildings before tax depreciation rules expired. Still, most Federal Reserve Districts noted sluggish operating loan demand as many farmers paid cash for crop inputs. After falling in 2011, feeder cattle and dairy loans were expected to hold steady in the Chicago, Dallas and Richmond Districts. Interest rates for intermediate-term loans edged down, and interest rates on operating and real estate loans fell in all districts except Richmond.

Farm credit conditions strengthened further as farmers paid off loans in the fourth quarter. According to Federal Reserve surveys, loan repayment rates at agricultural banks continued to climb, most notably in the Chicago District. In the Kansas City and Dallas Districts, crop insurance and land lease revenues from mineral rights supported farm income and loan repayment rates in drought areas. In addition, loan renewals and extensions fell in all Districts but San Francisco. With weak loan demand, ample funds were available for farm loans and very few borrowers were referred to non-bank credit agencies. Bankers in the Chicago, Richmond and San Francisco Districts generally eased collateral requirements compared with last quarter, while slightly more bankers in the Dallas, Kansas City and Minneapolis Districts raised collateral requirements on non-real estate farm loans.