Federal Reserve Bank of Chicago - -

May 10, 1974

Agricultural Letter

Number 1273

FARM LOAN DEMAND continues strong overall, but an easing appears evident for some types of loans. Nearly one-half of the 750 bankers responding to an April 1 survey indicated the demand for non-real estate farm loans exceeded the year-earlier level during the first quarter. An unusually high proportion of bankers also indicated they expected this trend to continue during the second quarter. Nevertheless, for the second consecutive quarter, one-fifth of the bankers indicated the farm loan demand was softer during the past three months, and over one-half of the bankers projected a year-to-year decline in feeder cattle loan demand for the second quarter.

Rural banks apparently have adequate liquidity to meet the overall strong loan demand. Some 44 percent of the bankers indicated that their availability of funds was higher than a year earlier during the first quarter, while an unusually small proportion of only 11 percent reported a decline.

The combination of a strong loan demand and the availability of funds for lending is reflected in the continuing large increases in outstanding farm debt held by institutional lenders. Outstanding non-real estate farm loans held by commercial banks rose to $17.3 billion at the end of last year, a jump of 21 percent from the year-earlier level. Outstandings held by PCAs rose 18 percent during the same period. The available evidence indicates that both banks and PCAs have continued to expand their outstandings during the first quarter of this year.

A portion of the increase in farm debt held by institutional lenders represents debt that would otherwise have been extended by merchants and dealers. In recent years, merchants and dealers of farm supplies have acquired a sizable volume of short-term farm debt as a result of liberal credit policies adopted in efforts to promote sales. But recent widespread shortages and increased costs of receivables financing have curbed the extension of credit by merchants and dealers in most areas. For example, two-thirds of the bankers indicated that credit policies of fertilizer suppliers in their area were substantially more restrictive than normal; one-fourth indicated the current policies were slightly more restrictive, while only one-tenth indicated no change from normal practices. Similarly, one-half of the bankers indicated that credit extended by fuel suppliers was substantially reduced, while only 15 percent reported no change. Only one-third of the bankers indicated the credit policies of feed suppliers and machinery dealers were unchanged.

Reduced credit extended by merchants and dealers no doubt contributed to the sharp increase in expectations by bankers for a continued strong farm loan demand during the months ahead. Overall, three-fifths of the bankers foresaw a year-to-year rise in farm loan demand in the second quarter, well above the proportion of bankers typically holding such views. The bulk of the increase is expected to reflect demand for operating loans and machinery loans. Three-fourths of the bankers projected a rise in operating loan demand, while nearly two-thirds projected further increases in the demand for machinery loans. Contrasting with these expectations, however, was the anticipated easing in feeder cattle loan demand, particularly in Illinois and Iowa. Over one-half of the bankers expected feeder cattle loan demand to fall short of the year-earlier level in the second quarter, while only one-tenth projected an increase. These are the strongest indications of a decline in feeder cattle loan demand in the past decade. Such views no doubt reflect the substantial losses experienced in the livestock industry over several months.

Interest rates on farm loans held steady during the past quarter, but a resumption of the uptrend appears likely for the months ahead. Overall, the interest rate charged on feeder cattle loans averaged 8.3 percent on April 1, up 75 basis points from a year ago. Only one-tenth of the bankers were charging 7.5 percent or less, while two-fifths were charging 9 percent or more.

The suggested increase in farm loan demand for the months ahead coupled with the recent sharp advances in short-term market interest rates will likely add some upward pressures to interest rates on farm loans. Restrictive usury ceilings will likely curb the upward pressures on farm loan interest rates in Illinois and Iowa and may discourage further expansion in agricultural lending by banks in these states. The impact of less restrictive usury ceilings in Michigan and Wisconsin is evident in the wide range in interest rates charged by district banks. For example, 67 percent of the bankers in Michigan and 40 percent of the bankers in Wisconsin were charging 9 percent or more on feeder cattle loans at the end of the first quarter. In contrast, only 1 percent of the banks in Illinois and 3 percent of the banks in Iowa were charging such rates.

Gary L. Benjamin
Agricultural Economist