Agricultural Lending by Commercial Banks

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http://www.agmanager.info

Background

During periods of low profitability like many farmers are currently experiencing, cash becomes critical to the farm business. Not only does low profitability directly affect cashflow but low farm profitability also discourages lenders from providing debt capital to farmers. This scenario played out during the farm crisis of the 1980's where many farmers couldn't obtain the cash needed to continue operations. This article examines the current state of agricultural loans issued by commercial banks to see if these loans are under performing.

Agricultural lending by commercial banks has increased nearly every year since since 2003. When adjusting for inflation, lending has increased yearly since 2010. Figure 1 below shows the dollars of agricultural loans by commercial banks since 1985. Both the actual dollar amount and the inflation adjusted loan amounts are shown. Data for all three figures is from the St. Louis Federal Reserve FRED database (https://fred.stlouisfed.org).

While actual loan amounts by commercial banks to agriculture are at all time highs, when adjusting for inflation, agricultural loans are still below the levels of the farm crisis of the 1980's. Figure 1 illustrates one of the potential problem facing farmers if the current low profitability levels continue. Commercial banks reduced their loans by $30 billion from 1985 to

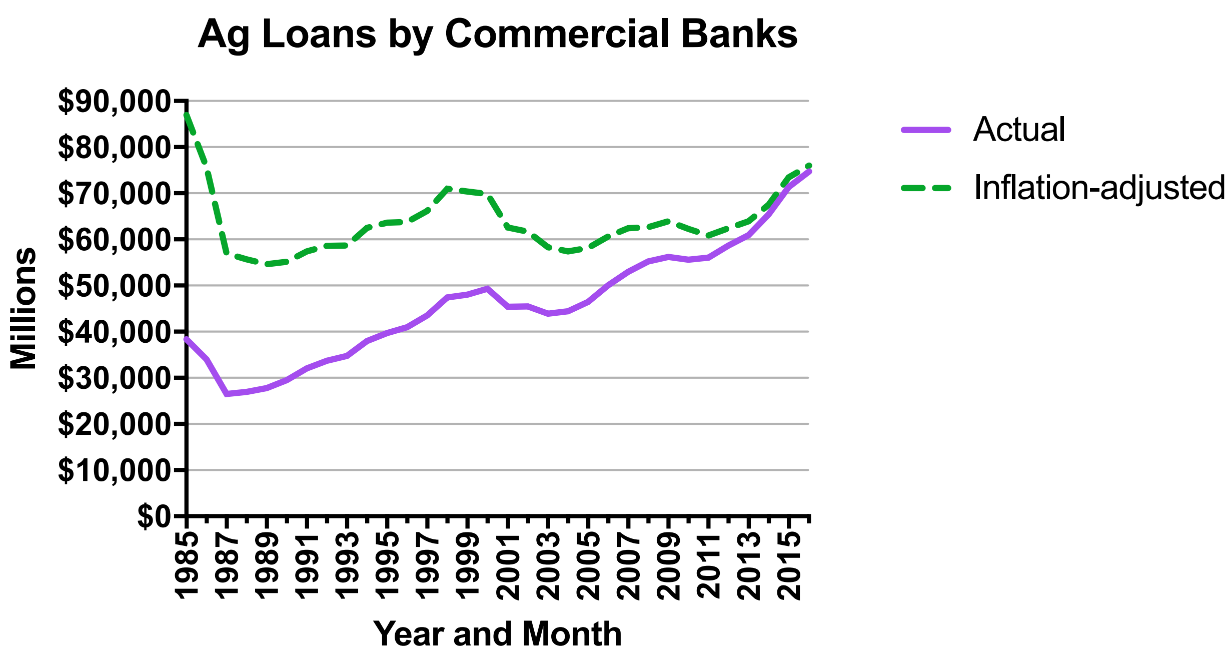

Figure 1. Agricultural Loans by Commercial Banks - From 1985 to 2016

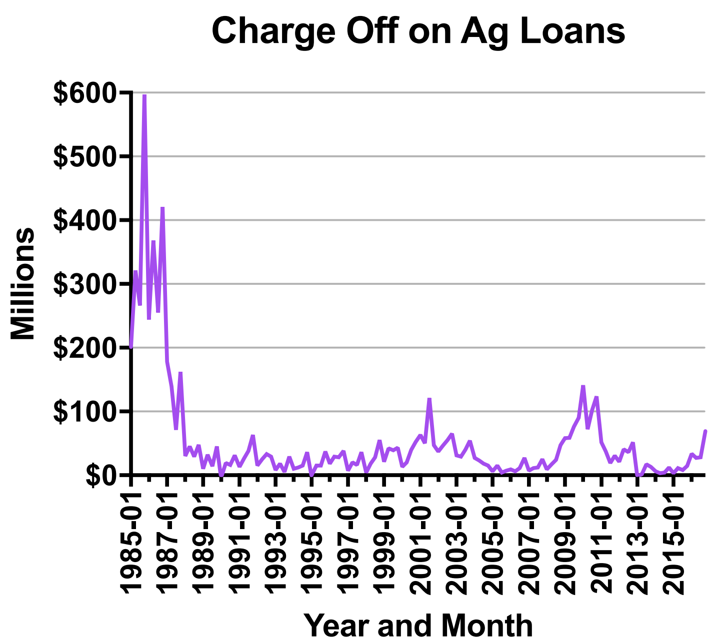

Figure 2. Charge Off on Agricultural Loans and Leases by Commercial Banks

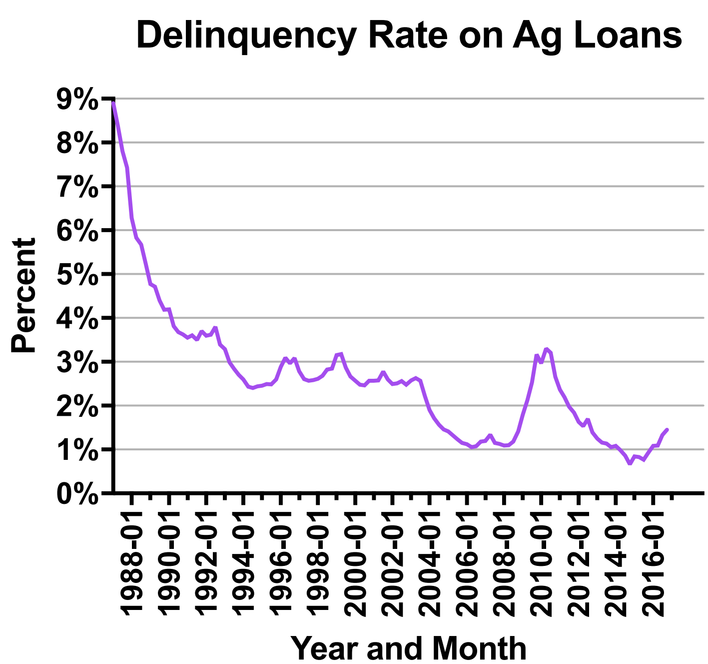

Figure 3. Delinquency Rate on Agricultural Loans by Commercial Banks

1987. During the farm crisis of the 1980's cashflow was one of the major problems facing farmers. Without access to cash from banks, farmers struggled. So far, data from the Federal Reserve hasn't shown a drop off in lending from commercial banks but the data only goes through the end of 2016.

Figures 2 and 3 show the loan write-offs and the delinquency rates of agricultural loans by all commercial banks, respectively. Figure 2 goes back to 1985 while Figure 3 goes back to 1987. Both graphs go through 2016. As might be expected, loan charge offs and delinquency rates are highly correlated.

Figures 2 and 3 illustrate two points. First, the rate of loan delinquencies and loan write-offs were very high during the farm crisis. Second, there is some delay before farm financial conditions start to affect loan performance.

Looking Ahead

Both the charge off on agricultural loans and the delinquency rate are relatively low compared to the historical numbers. However, both of these indicators are trending upward and are likely to go higher even if profitability improved immediately. An important question for farmers is how much will banks curtail agricultural lending? Just like the 1980's, farmer survival in this current crisis may come down to the ability of farmers to obtain operating loans.