FINANCIAL INTELLIGENCE
from FHLBANK TOPEKA

AGRICULTURE

THE FUTURE OF AG LENDING

How to handle growth in ag operating lines

With the decline in grain prices in 2013 and 2014, numerous economists were predicting increased agriculture operating lines. For once, they were spot on. The Federal Reserve Bank of Kansas City reports second quarter operating lines are up nearly $20 billion since 2011. Likewise, FHLBank Topeka member institutions are tracking similar to national averages with operating lines up over $4 billion since the end of 2011.

At the same time, delinquency rates on agriculture loans and non-real estate loans, such as equipment, are at historic lows. Visit the Fed's site for a graphical view of delinquencies.

Strong loan growth combined with historically low problem asset levels provides a good opportunity for banks that specialize in agricultural lending to grow their bottom lines. Over the past several years, farmers have prepaid operating lines more quickly due to high grain prices and strong yields. A variety of economic trends suggest farmers may need to carry balances longer moving forward, which will likely result in higher profits and increased funding needs for ag lenders.

Since late 2013, corn prices have been driven down by increased grain production resulting from ideal growing conditions. The Wall Street Journal reports U.S. storage bins for corn totaled 1.7 billion bushels on Sept. 1, 2015, which is up from 1.2 billion bushels one year earlier. Although grain prices have trended down, a much stronger world supply means corn and other grains are too high to compete in global markets. Like corn, soybean stockpiles were sizable as of Sept. 1, 2015 - more than double than last year. High prices, abundant domestic stockpiles, a strong U.S. dollar and ample exportable supplies in Australia, Canada, Russia

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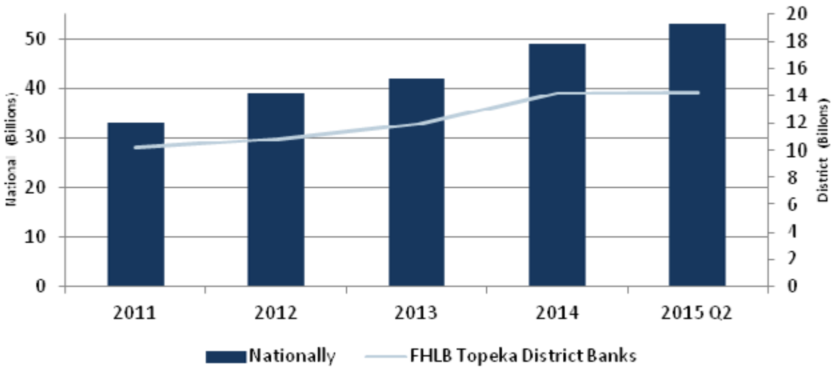
Find out more about Jeff and our funding experts at **FHLBTOPEKA.COM/ INTELLIGENCE.**

and the Ukraine are to blame. While this may result in a decline in corn and soybean production moving forward, farmers will likely need to carry a larger operating line during 2016.

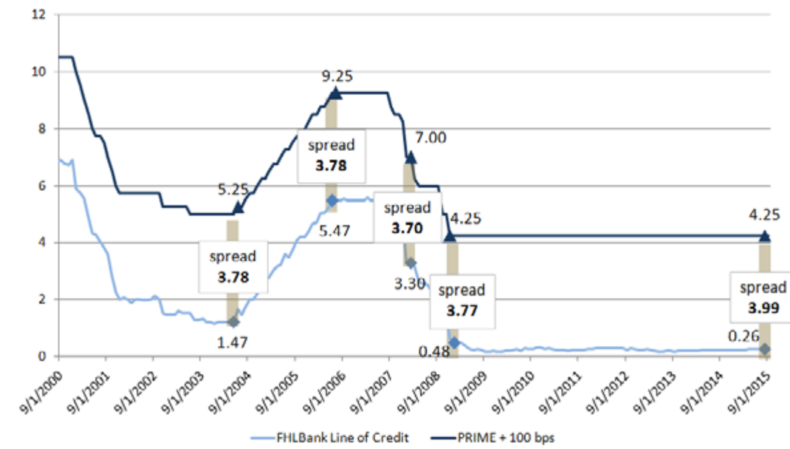
In the livestock markets, cattle and hog producers have increased their herds over the last couple of years, following an end to severe drought conditions and bouts of disease. The Chicago Mercantile Exchange reports hog slaughter is ramping up due to increased supply. Production is expected to be up by 10% since last year, which could drive hog futures down. Cattle slaughter is slightly down from a year ago due to cheaper competing meat and poor export demand. The USDA forecasts a slight increase in U.S. production for the first time since 2010 as cattle inventories recover, driven by improved pasture conditions and lower feed costs. While margins continue to be fairly tight, the increased herds and production should result in higher loan demand for your institution in 2016.

On a national basis, loans and leases are growing at an annual rate of 8%. Loan to deposit ratios for FHLBank Topeka member banks have increased to an average of 77% at the end of the third quarter 2015, up from 70% at the end of 2012. As farmers and ranchers increase their dependency on operating lines, you have an opportunity to put your deposits to work and increase profits. Keep in mind that in the previous rising rate environment, loans outpaced deposits, so you will need access to low-cost, flexible liquidity.

Ag Operating Loan Volume



FHLBank Line of Credit vs. Operating Line



One option to fund this growth is FHLBank Topeka's line of credit. The current line of credit rate combined with the 6% dividend on activity-based stock lowers the effective borrowing rate to nearly 0%. The graph below depicts a consistent spread in numerous rate environments between FHLBank's line of credit rate and an average operating line (U.S. Prime plus 100 basis points).

Some members run into collateral shortages at this time of year because they haven't identified adequate collateral to meet their potential liquidity needs and consequently are unable to take down an advance immediately when they need it. It's a good idea to make sure you have enough collateral pledged to cover your future liquidity needs. Check out our schedule of eligible collateral to see what qualifies.

Our Financial Services staff is available to help you identify additional collateral on your balance sheet. Contact them at 877.933.7803 or the Lending Desk at 800.809.2733.

Contact Jeff today for solutions that work for you.

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