Helping Farmers Weather The Hairy Storm

lending profitability business customers

Summary: Farmers are struggling these days with low market prices. Some advice to help you with your agricultural business customers.

In a strange twist of fate, a story is told of a man in 1567 with the longest beard in the world. It seems he was trying to run away from a fire and tripped over his own beard. Guess it still makes sense not to let any facial hair get too out of control perhaps.

Bankers that are active in agriculture (Ag) lending know it is important to stay on top of things to avoid potential issues. Farmers are struggling with low prices for wheat and row crops, especially in the corn-, beans-, and wheat-producing Midwest and Great Plains. The current projected carryout (amount of product left over after accounting for all projected use) is large.

As your college economics courses taught you, a surplus pushes prices down and that's exactly what's happening to farmers right now. In addition, global crop production, worldwide consumption patterns and trade issues also affect and complicate Ag price pressures.

Bankers can't create business plans for Ag customers necessarily, but you can help affected clients deal with price risk. Your bank can encourage Ag customers to develop and stick to business plans that exploit opportunities to lock in profits or protect downside risk, for example.

Given the Fed plans to continue raising interest rates this year, and that market volatility is an ongoing risk, bankers may want to revisit Ag lending portfolios. One area perhaps is to seek out such customers and help them get long-term financing at fixed rates. This can put these customers in a stronger position to ride out the ups and downs of shifting Ag prices.

Recently updated Fed supervisory letters also provide some good tips and reminders. Here, the Fed indicates that on the good news front, farm producers have experienced strong profitability over the past three years and their use of debt overall remains relatively low. That is positive, however the Fed then balances that out by indicating that while these factors have generated optimism for the future viability of agricultural producers, risk in the agricultural sector has also increased due to volatility in agricultural commodity prices, farmland values, and farm production costs. Basically, it is important for bankers to have strong risk management capabilities and processes around Ag lending right now, because changes can be abrupt and adverse.

The current market may force more farmers to borrow, and may also add to the difficulty of repaying existing loans. After all, a farm's working capital is its first protection price volatility, and many Midwestern farmers are seeing their working capital shrink. Further, as interest rates rise, Ag borrowers may find it more challenging to stay current on existing loans, which could spill over into bank balance sheets.

No one is going Chicken Little here right now and saying the sky is falling, but banks operating in the Ag lending space should be aware of recent heightened volatility to keep the loan book clean and free of issues down the road.

Stay on top of and ramp up monitoring of some of these key factors to avoid getting nicks and cuts in your Ag book: commodity prices, production costs, farmland values, global markets, borrower cash flow, and credit controls to name a few. This extra scrutiny could help you avoid any hairy situations with agriculture lending.

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