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Using New Fund Sources: A Banker's Perspective

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My perspective of the job assigned to me as a country banker from Paragould, Arkansas, is to react to the excellent presentations we have heard during this symposium.

Peter Barry and others from academia have clearly presented the challenge that lies before us. While each new decade carries with it renewal of hope eternal, the environmental circumstances and the regulators, among others, present formidable challenges for agricultural bankers in the decade ahead.

The message I perceive disseminating from Governor Partee is that the Federal Reserve offers no quick cure for banks in general and for agricultural community banks in particular. I think we could well afford to give close attention to Governor Partee's admonition that banks pay close attention to both asset and liability management as they move into full-fledged deregulation. This is especially true when taking into account the great variety of new competitors agricultural banks have.

John Lee, of the United States Department of Agriculture, reminds us that there is a role for government in providing funds and making loans to farmers. The message I heard presented was that the role should be somewhat smaller than it is. 1 am convinced that there are significant opportunities for community banks desiring to serve farmers and agribusiness people in the future: to utilize the programs of the United States Department of Agriculture as well as other government-sponsored programs in obtaining new sources of loanable funds.

Recent laws providing FmHA-guaranteed disaster loans will permit farmers to deal with their banks and take advantage of interest subsidies when they are faced with catastrophic disasters brought on by natural and economic phenomena.

I am distressed that the money center banks continue to show little inclination toward rethinking and reviewing their role in financing agriculture. It appears to me that the money center banks shall continue to circumvent the historic correspondent relationship and compete directly through their loan production offices and other means for good loans in the breadbasket of America. I am sure that many money center banks will continue to provide sources of lendable funds circuitously through the purchase of participations and non-agricultural loans, through the sale of Federal funds and repurchase agreements, and by other mechanisms.

I am distressed at the lack of farsightedness on the part of money center banks. By expanding their branching network nationwide, by establishing loan offices and other devises that narrowly circumvent the present law, they are perhaps developing animosities on the part of country banks that will impede if not absolutely prevent orderly development of banking laws that would permit geographic expansion and the removal of other barriers that ought to be removed. Unfortunately, that seems to be the way the money center bank die is cast.

Country banks would be well advised to consider utilizing money center banks in the above roles as an additional source of loanable funds. I am encouraged at the word received from the regional correspondent banks, statements that give cause to believe regional banks are dedicated to preserving the historic correspondent bank relationship and to serving agriculture via this proven mechanism.

I am encouraged by the regional correspondents' commitment to continue to participate in loans, continue to allocate assets and — more importantly, perhaps — personnel who can understand and identify the needs of agricultural banks. It was appropriate that banks in the rural areas were divided into rural banks and agricultural banks. But I do take exception to the suggestion, implicit in many of their remarks, that agriculture bankers are a bunch of yo-yos. The fact is that agriculture banks are very well managed.

It appears to me that agricultural banks need to do a better job of loan documentation, loan preparation, and loan explanation, and a much better job of communicating with regional banks. Certainly, the decade ahead calls for the establishement and development of profitable relationships with our regional correspondent banks. These relationships depend on willingness on the part of the regional correspondent banks to devote assets and personnel to financing agriculture, and also depend to a large extent upon the agriculture banks taking the initiative to make changes, to be innovative, and to exploit the opportunities that exist by establishing these needed relationships.

The first banking conference I attended was a discussion on Alternative Sources of Funds for Funding Agriculture. It has been the subject of about every other banking conference that I have attended, disguised in other ways and called other things. A great deal has been said in the past twenty-odd years but very very little, frankly, has been done. And to me, the most fascinating possibility of a new source of funds is that so ably presented by Raymond Doll. I think it altogether appropriate that the American Bankers Association, the regional correspondent banks, and agricultural banks join together with the Federal Reserve and other agencies of the government in early formation and early implementation of Ray Doll's mechanism for the discounting of agricultural loans.

Savings and loans enjoy a nationwide market outlet for long-term real estate loans. Naturally, such loans must meet accepted documentation and rate structure criteria. Likewise, national corporations enjoy a similar market in commercial paper. The Federal credit unions enjoy a nationwide pool of capital.

The greatest competitor for good loans and assets of agricultural banks, the Farm Credit System, is fast approaching a monopolistic condition because of its ability to market, on a nationwide basis, bonds backed by agricultural loans. ,Because of this, there is a strong sense of urgency in the early implementation of Ray Doll's special mechanism for marketing bonds backed by agricultural paper, bonds that bear the guarantee of the Federal Deposit Insurance Corporation or some other appropriate agency.

In this symposium, a great deal of attention has been directed toward the Farm Credit System. You have heard the suggestions of officials of the system that the misunderstandings of facts, misunderstanding of intent, and misunderstanding of mission. A careful reading of the paper indicates that it is filled with factual errors. These errors indicate a gross misunderstanding and knowledge of commercial banks, at best, and perhaps of the Farm Credit System at worst.

For instance, the Farm Credit System is in no way like national banks. National banks pay taxes. Dividends paid on national bank stock is subject to an additional taxation. The owners of national bank stock pay taxes. The structure is different. While there is commonality of mission among national banks serving predominantly agricultural regions, the missions of banks are much broader than those of the Farm Credit System.

The contention that the system is not a deposit-gathering entity ignores the fact that any citizen who is not an employee of the system may purchase bonds in denominations as small as $1,000. Further, these bonds are not subject to Regulation Q and frequently bear interest far in excess of those that can legally—or profitably—be paid by agricultural banks.

Officials of the system discuss at length their concern over monetary constraint in the coordination of the system. However, the fact is that the system is not subject to those responsible for monetary policy in this country. The Farm Credit System marketed in excess of $93 billion in bonds last year, second only to those marketed by the United States government itself.

The Farm Credit System has consistently engaged in arbitrarily administering the laws under which it operates. A classic example of these abuses is the manner in which discount privileges have been extended to national banks, farm loan subsidiaries, and other entities eligible for discount. This fact is illustrated in that approximately 155 banks or bank-owned farm loan subsidiaries presently utilize the discount in times of extremely tight money supply. There is little doubt in my mind that the system has a perhaps nonrecognized drive and desire to become the dominant supplier of general credit on the farm scene.

Notwithstanding these problems with the Farm Credit System, there is substantial potential for agricultural banks to develop meaningful relationships under the provisions of the 1980 amendments.

The streamlining of participations offers unique opportunities for banks to join in concert with Federal Land Banks and Production Credit Associations to provide urgently needed capital to finance agriculture and agricultural business. The discounting privilege under the OFI carries with it a strong congressional mandate and a strong commitment from the officials of the Farm Credit System to fairly and equitably administer the discounting privileges of the Federal Intermediate Credit Banks.

In conclusion: While the challenges faced by agricultural banks are formidable, the opportunities have never been greater.

A variety of future sources of loanable funds will be available if agricultural banks have the courage and possess the initiative to access these funds. Among these is the broadening of the relationships between agricultural banks and money center banks. Another important ongoing source of loanable funds is the continued improvement of relationships between agricultural banks and regional correspondent banks. These have been the mainstay in financing agriculture in past decades and appear to be our best hope in the immediate future.

The creation of a mechanism of national marketing of bonds backed by agricultural loans is a matter of extreme urgency. I urge those who are interested in financing agriculture, and who are interested in commercial banking, to work unceasingly towards the implementation of Ray Doll's suggestion that an entity be created so that agricultural loans may be marketed vis-a-vis the bond market, thus enabling us to competitively serve agriculture and agribusiness in the decades ahead.