FRB CHICAGO

AGRICULTURAL LETTER

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Land value and credit conditions survey

Our quarterly surveys of agricultural banks in the Seventh Federal Reserve District provide regular updates on the views of those bankers regarding farmland values and credit conditions in their area. The most recent survey was mailed on July 1 and it drew responses from 450 bankers. The results suggest that farmland values continued to edge higher in most areas, rising nearly 1 percent on average in the second quarter and nearly 6 percent during the year ending with June. The survey also found that farm loan demand continued very strong this spring while the ability of banks to lend to farmers tightened. Interest rates charged on farm loans turned up in the second quarter, the first significant upturn since early 1989.

The second quarter uptrend in District farmland values was evident in all states except Indiana. The bankers from the District-portion of Indiana reported a second quarter decline of nearly 1 percent. Elsewhere, the bankers from Illinois, Iowa, and Wisconsin reported a second quarter rise of about 1 percent in farmland values while the bankers from Michigan reported a gain of 2 percent. Relative to a year ago, the reported gains in farmland values ranged from roughly 5 percent in Iowa and Michigan to around 7 percent in Illinois and Wisconsin.

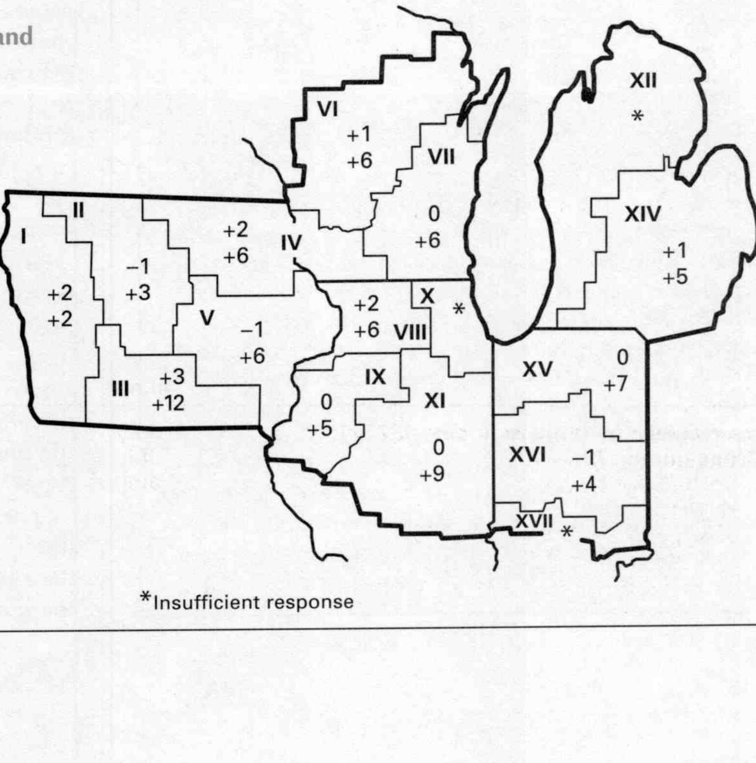
Although the uptrend in farmland values continued this spring, the rate of gain slowed from that registered during the fall and winter quarters. Moreover, the proportion of bankers that felt the uptrend would continue into the next quarter declined slightly in the most recent survey. Overall, 28 percent of the bankers felt that land values would trend upward this summer while the bulk of the remainder felt that land values would hold steady. The share projecting a continued uptrend in the most recent survey was down nearly 10 percentage points from the share reporting an uptrend last quarter. The declining share of bankers expecting a continued uptrend in farmland values was more apparent in Illinois and Indiana than elsewhere in the District.

While the uptrend in farmland values is likely to continue, recent gains in interest rates and downward pressures on farm earnings may tend to hold the line on the rate of increase. As discussed below, interest rates charged on farm mortgages rose about 50 basis points (one-half of a percentage point) during the second quarter. The increase leads to higher interest charges on debt-financed farm real estate purchases while higher rates in general add to the returns on alternative investments that potential land buyers might consider. Moreover, sizable gains in meat production are weighing

Percent change in dollar value of "good" farmland

Top: April 1, 1994 to July 1, 1994
Bottom: July 1, 1993 to July1, 1994

	April 1, 1994 to July 1, 1994	July 1, 1993 to July 1, 1994
Illinois	+1	+7
Indiana	−1	+6
Iowa	+1	+5
Michigan	+2	+5
Wisconsin	+1	+7
Seventh District	+1	+6



*Insufficient response

heavy on livestock prices and trimming the earnings of livestock producers. The financial health of crop farmers will hinge heavily on this year's harvest. The banner corn and soybean prospects for Iowa and Wisconsin will undoubtedly prove much more appealing to farmers in those states than was the case with the flood-reduced harvest of a year ago. But for farmers in all areas, the financial underpinnings offered in a bumper harvest could be significantly offset by lower crop prices. While land buyers factor more than just recent crop prices and production prospects into their deliberations, the recent declines in crop prices may cause some tempering in the demand to acquire farmland.

The responses to the credit-related questions in the most recent survey found further strengthening in farm loan demand and a marked tightening in the liquidity position of bankers. In the most recent survey, nearly 49 percent of the bankers indicated that farm loan demand in the second quarter exceeded the year-earlier level. Only 10 percent reported a decline while the remaining share—41 percent—reported that farm loan demand was unchanged from last year. As indicated in the table on page 3, the net share of bankers reporting an increase in loan demand translates into an overall reading of 139 for second quarter farm loan demand.

Farm loans at banks, March 31, 1994

	Real estate	Nonreal estate	Total	% change from: Year ago	5 years ago
	(-------billion dollars-------)				
Illinois	$1.71	$2.01	$3.73	4.8%	20%
Indiana	.98	.83	1.81	1.4	8
Iowa	1.82	3.37	5.19	11.6	45
Michigan	.26	.38	.64	–0.3	–1
Wisconsin	.98	1.15	2.13	5.6	26
District states	5.76	7.74	13.50	6.7	26
United States	21.25	35.55	56.79	7.6	29

The variability in the views of the surveyed bankers regarding farm loan demand is also evident in the latest reports that track the portfolio of farm loans held by all banks. Those reports show that farm loans at banks in the five District states approximated $13.5 billion as of the end of March, up 6.7 percent from a year earlier. As noted in the table, the change in farm loans among banks in individual states has varied widely, both over the last year and over the past five years. In marked contrast to the performance elsewhere, farm loans at banks in Michigan have edged lower in recent years. At the other extreme, farm loans at banks in Iowa rose nearly 12 percent last year and 45 percent over the last five years. The reasons behind the widely differing growth rates in bank loans to farmers are not entirely clear.

This reading slightly exceeds the last cyclical high in farm loan demand that occurred in 1989 and is the highest reading for any quarterly survey since the late 1970s. Among individual District states, the measure of loan demand varied widely, ranging from 110 in Michigan to 160 in Iowa.

The indicated second-quarter strength in farm loan demand at banks no doubt reflects expanded crop plantings and slightly higher farm input prices. Reports from the U.S. Department of Agriculture show the acreage planted to principal field crops in District states rose 3 percent this year while prices paid by farmers for such things as fuel, fertilizer, seed and chemicals ranged from 1 to 6 percent higher as of mid-year. In addition, farmers in Iowa experienced a sharp decline in receipts from crop sales during the early months of this year, a trend that differed markedly from the pattern in other District states and no doubt reflects the aftermath of last year's flood. The lower crop receipts in Iowa and the narrowing returns to livestock producers have probably caused farmers to rely more on debt financing as a means of acquiring operating capital this year. In addition, the indicated strength in farm loan demand at banks probably reflects the pick-up in capital expenditures by farmers this year. Reports from the Equipment Manufacturer's Institute show that unit retail sales of farm tractors and combines though the first seven months of 1994 were up 8.5 percent from last year's pace.

While farm loan demand continued to strengthen, the available evidence shows the prolonged period of ample liquidity at agricultural banks may be ending rather quickly. The latest reading on the availability of funds at banks for making farm loans was down sharply and equal to the lowest level for that measure in 14 years. Moreover, the average of the reported loan-to-deposit ratios among the surveyed banks rose to .625, the highest since 1980. Among District states, the average loan-to-deposit ratios varied widely, largely reflecting the tendency of the larger-sized banks—which are more prevalent among the survey respondents from Wisconsin, Michigan and Indiana—to have higher ratios. In terms of the extent of the rise in the average loan-to-deposit ratios over the past year, the biggest gain by far was for banks in Iowa. As of mid-year, the loan-to-deposit ratios reported by Iowa banks averaged .612 up from .559 a year ago. This coupled with evidence of slower deposit growth among Iowa banks suggests that the aftermath of the last year's flood in Iowa is influencing deposit trends as well as loan demand and loan repayments.

Interest rates charged on farm loans by District agricultural banks rose considerably in the second quarter, marking the first significant upturn in more than five

Credit conditions at Seventh District agricultural banks

	Loan demand	Fund availability	Loan repayment rates	Average loan-to-deposit ratio[1]	Interest rates on farm loans: Operating loans[1]	Feeder cattle[1]	Real estate[1]
	(index)[2]	(index)[2]	(index)[2]	(percent)	(percent)	(percent)	(percent)
1989							
Jan-Mar	138	115	84	53.8	12.54	12.48	11.70
Apr-June	138	107	92	55.9	12.42	12.36	11.55
July-Sept	124	109	106	57.1	12.19	12.15	11.34
Oct-Dec	119	124	123	55.8	12.05	12.02	11.15
1990							
Jan-Mar	125	124	122	55.2	11.93	11.88	11.08
Apr-June	118	125	119	56.5	11.95	11.88	11.09
July-Sept	117	122	115	57.0	11.94	11.87	11.08
Oct-Dec	116	123	100	56.9	11.82	11.76	10.94
1991							
Jan-Mar	128	127	98	56.5	11.40	11.37	10.57
Apr-June	130	122	74	58.1	11.19	11.17	10.43
July-Sept	113	122	81	58.5	10.88	10.89	10.15
Oct-Dec	109	132	69	57.4	10.06	10.08	9.39
1992							
Jan-Mar	129	128	77	57.3	9.77	9.80	9.19
Apr-June	123	123	79	58.1	9.57	9.56	8.99
July-Sept	111	123	90	59.3	9.18	9.16	8.63
Oct-Dec	107	127	93	58.7	9.12	9.13	8.59
1993							
Jan-Mar	108	131	102	58.0	8.85	8.83	8.29
Apr-June	103	129	95	59.2	8.77	8.74	8.16
July-Sept	110	122	90	59.2	8.63	8.59	7.99
Oct-Dec	125	126	95	59.7	8.50	8.50	7.88
1994							
Jan-Mar	136	121	94	59.9	8.52	8.48	7.97
Apr-June	139	107	90	62.5	8.98	8.95	8.48

[1]At end of period.
[2]Bankers responded to each item by indicating whether conditions during the current quarter were higher, lower, or the same as in the year-earlier period. The index numbers are computed by subtracting the percent of bankers that responded "lower" from the percent that responded "higher" and adding 100.

years. The average of the rates reported for feeder cattle and for farm operating loans rose to nearly 9.0 percent, up almost 50 basis points from three months ago. Rates on farm loans secured by real estate averaged about 8.5 percent in the most recent survey. The range in average rates for farm operating loans among the five District states stretched from a low of nearly 8.75 percent for banks in Illinois to a high of nearly 9.5 percent for banks in Michigan. The range in average rates on farm real estate loans was just as wide, stretching from 8.35 percent among banks in Illinois and Iowa to 9.10 among banks in Michigan.

Farm loan repayment rates continued to register varying trends this spring. Bankers from Iowa and Wisconsin continue to note that farm loan repayments lag year-earlier levels while those from Illinois, Indiana, and Michigan suggest that repayment rates are equal to or up from a year ago. The overall measure of the farm loan repayment rate edged down slightly—from 94 to 90—in the most recent survey as the responses from bankers in most areas of the District show slower repayment rates relative to a year ago. On a more encouraging note, however, the latest reading on farm loan repayment rates for Iowa banks—while still very low—was up considerably from the levels recorded in the previous two surveys.

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Selected agricultural economic indicators

	Latest period	Value	Percent change from: Prior period	Year ago	Two years ago
Prices received by farmers *(index, 1977=100)*	July	134	–2.9	–5	–3
Crops *(index, 1977=100)*	July	120	–5.5	–1	3
Corn *($ per bu.)*	July	2.25	–13.8	1	–3
Hay *($ per ton)*	July	82.50	–7.0	7	18
Soybeans *($ per bu.)*	July	6.02	–10.4	–8	8
Wheat *($ per bu.)*	July	3.03	–5.6	6	–4
Livestock and products *(index, 1977=100)*	July	148	0.0	–8	–6
Barrows and gilts *($ per cwt.)*	July	43.10	–0.7	–8	–6
Steers and heifers *($ per cwt.)*	July	65.20	0.8	–13	–12
Milk *($ per cwt.)*	July	12.60	–0.8	–2	–6
Eggs *(¢ per doz.)*	July	57.2	–1.7	–1	10
Consumer prices *(index, 1982-84=100)*	July	148	0.3	3	6
Food	July	144	0.5	3	5
Production or stocks					
Corn stocks *(mil. bu.)*	June 1	2,358	N.A.	–36	–14
Soybean stocks *(mil. bu.)*	June 1	555	N.A.	–19	–20
Wheat stocks *(mil. bu.)*	June 1	571	N.A.	8	21
Beef production *(bil. lb.)*	June	2,157	8.7	5	6
Pork production *(bil. lb.)*	June	1,411	1.0	2	6
Milk production* *(bil. lb.)*	July	11.0	–0.1	1	1
Receipts from farm marketings *(mil. dol.)*	April	13,561	–7.9	–9	2
Crops**	April	5,070	–9.6	–2	10
Livestock	April	7,155	–8.2	–6	3
Government payments	April	1,336	1.2	–34	–22
Agricultural exports *(mil. dol.)*	May	3,552	3.0	6	13
Corn *(mil. bu.)*	May	72	–16.4	–41	–31
Soybeans *(mil. bu.)*	May	28	–20.7	–21	–3
Wheat *(mil. bu.)*	May	86	13.7	–22	34
Farm machinery sales *(units)*					
Tractors, over 40 HP	July	4,280	–30.8	6	5
40 to 100 HP	July	3,207	–26.4	6	0
100 HP or more	July	1,073	–41.3	3	25
Combines	July	808	–3.6	37	52

N.A. Not applicable
*21 selected states.
**Includes net CCC loans.

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