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FRB CHICAGO

AGRICULTURAL LETTER

FEDERAL RESERVE BANK OF CHICAGO
February, 1994 Number 1849

Agricultural banks report varying conditions

Our latest quarterly survey of agricultural bankers in the Seventh Federal Reserve District found widely differing views with respect to the market for farmland and agricultural credit conditions. The differing views among the 450 bankers that responded to the survey were closely correlated with the severity of last year's flood-related crop losses. In general, however, the survey indicated that farmland values continued to trend upward in most areas. In addition, farm loan demand was indicated to be stronger in most areas, but ample funds for lending and stable to declining market rates of interest led to further declines in the rates charged by banks on loans to farmers. Farm loan repayment rates weakened in areas hit hardest by the flood, but improved in most other areas of the District. The bankers' expectations about capital expenditures by farmers revealed similar geographical differences.

The weighted average quarterly rise for District farmland values edged up to 1.2 percent for the final three months of 1993. The reported increase for all of last year averaged nearly 3.5 percent. Both the quarterly and the annual gain reported in the most recent survey were the largest noted in any of the surveys taken during the last three years of a relatively lackluster market for farmland. More revealing, however, was the differing views as to

the strength of the farmland market. The bankers from the District portions of Illinois and Indiana reported large gains for both the fourth quarter and all of 1993 (see map below). A fourth quarter surge pushed last year's rise in farmland values in Illinois to 7 percent, the second largest increase for any year since the uptrend in farmland values resumed in 1987. Last year's reported 6 percent rise in Indiana was the largest for that state since 1989. Alternatively, the bankers from Iowa, Michigan, and Wisconsin indicated that farmland values in those states were unchanged during the fourth quarter and up only modestly (1 to 3 percent) for all of last year. The 1 percent rise for Iowa last year was the smallest increase for that state since 1986.

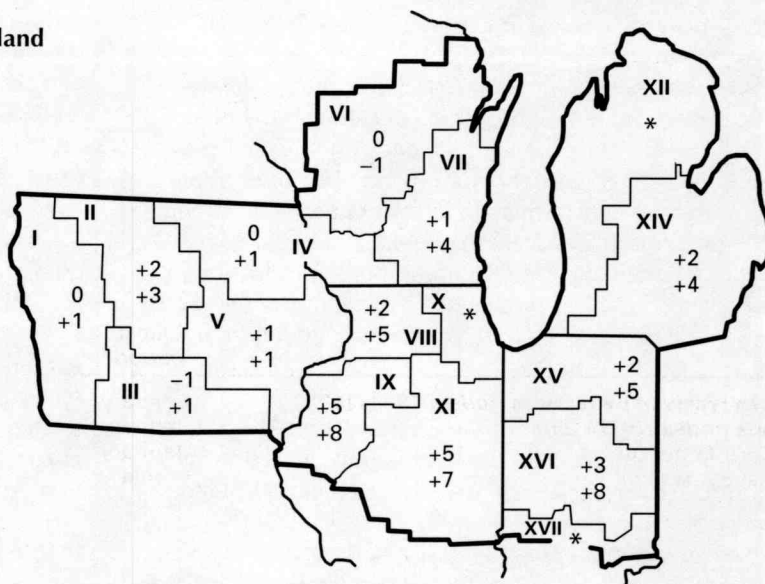
Further evidence of the differing impressions of the momentum in the farmland market was apparent in the trends expected by bankers this winter. In Illinois and Indiana the bankers were about evenly divided, with 50 percent projecting a continued uptrend in land values and the remaining 50 percent expecting land values to be stable. The share projecting a continuing uptrend in farmland values into the next quarter was comparatively large by the standards of past surveys. In the other three District states, only a small share of bankers (10 to 15 percent) projected an uptrend, a few projected declines, and the large remaining majority (80 to 90 percent) projected that land values would be stable in the first quarter.

Percent change in dollar value of "good" farmland

Top: October 1, 1993 to January 1, 1994

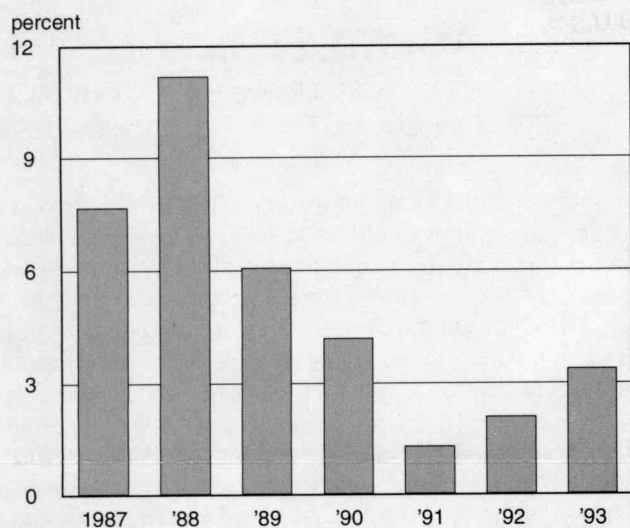
Bottom: January 1, 1993 to January 1, 1994

	October 1, 1993 to January 1, 1994	January 1, 1993 to January 1, 1994
Illinois	+4	+7
Indiana	+2	+6
Iowa	0	+1
Michigan	0	+3
Wisconsin	0	+2
Seventh District	+1	+3



*Insufficient response

District farmland values registered a bigger increase last year



The apparent geographical differences in the bankers' views on the strength of the land market would appear to be mostly related to the differential effects of last year's flood on crop production. Overall, farmers in Indiana and Illinois enjoyed a better than average corn and soybean harvest last year. In contrast, the corn harvest in Iowa and Wisconsin fell roughly 40 percent below the 1986-91 average (excluding the drought year of 1988) and the soybean harvest in Iowa was off more than a fourth from average. The implications of the contrasting harvest results were further amplified as crop prices rose sharply over the last two months of 1993. Corn prices rose the most and in January averaged some 40 percent higher than the year before and the highest for any month in nearly ten years. The bankers from Illinois and Indiana probably saw the combination of an average harvest and high prices as translating into aggressive bidding on farmland and—as discussed below—improving conditions with respect to farm credit issues. Conversely, the far more pessimistic view of the bankers from Iowa and Wisconsin likely reflected a view that the huge crop losses in those states would only be partially cushioned by the higher prices and by higher deficiency and disaster payments. Moreover, a brief period of very low or negative returns to most hog farmers in late 1993 probably added to the pessimistic views among bankers in Iowa. Similarly, comparatively large declines in milk production in Wisconsin and the anticipated implications of the use of BST beginning in early 1994 may have added to the pessimism in that state.

Bankers from most areas of the District reported that the demand for farm loans in the final months of 1993 was up from year-earlier levels. The overall measure of farm loan demand rose to 125 (see table on page 3). That reading represents a composite tabulation that starts with a base number of 100, adds the 40 percent of the bankers who reported a year-over-year rise in farm loan demand,

and subtracts the 15 percent who reported a decline in demand. By far the strongest reading on loan demand came from the bankers in Iowa, 156 versus readings that ranged from close to 100 in Michigan and Wisconsin to about 116 in Illinois and Indiana.

Paradoxically, the strong loan demand indicated for Iowa might reflect the survey's simultaneous findings of an extraordinarily low farm loan repayment rate and a surge in renewals and extensions of existing farm loans in some areas. The latter findings were widespread among the bankers from Iowa and—to a lesser extent—those from Wisconsin, the two District states hit hardest by the weather-related crop losses of 1993. In marked contrast, the bankers from the other three District states—where last year's above normal crop harvest gave farmers greater opportunities for capitalizing on the recent surge in crop prices—reported a strengthening in farm loan repayment rates and a slowing in loan renewals and extensions for the fourth quarter. Reflecting the geographical contrast in views, the overall reading of the fourth quarter farm loan repayment rate was 95, up slightly from the previous quarter. However, the overall District average blended a wide range of readings for individual states that—at the low end—fell to 34 and 84 for Iowa and Wisconsin, respectively, and—at the upper end—clustered between 124 and 150 for Illinois, Indiana, and Michigan. In other words, to translate the two extreme readings, the share of bankers in Iowa that noted a year-over-year decline in loan repayments exceeded the share that reported an increase by an overwhelming 66 percentage points. For Indiana, conversely, the share of bankers that indicated an increase in loan repayments swamped the share that noted a decline by 50 percentage points.

The evidence of a slowing in farm loan repayment rates was overwhelming from the bankers in Iowa and Wisconsin. However, it does not appear that those banks have responded by arbitrarily tightening their farm lending standards, at least in terms of their collateral requirements. The share of the bankers that reported they had increased their farm loan collateral requirements edged down to 12 percent in the most recent survey, marking the lowest reading for this item in the past two decades of quarterly surveys. Moreover, the share of the bankers from hard-hit Iowa and Wisconsin that had raised their collateral requirements was only slightly above the share from Illinois and Michigan and somewhat below that for bankers from Indiana. In short, it appears that the improved financial conditions that have occurred among agricultural banks in recent years will permit them to treat last year's flood-related setback to their farm borrowers as a temporary aberration that can be handled over time without resorting to more stringent lending standards.

In line with the above, the proportion of bankers expecting a year-over-year increase in the amount of farm loans to be made during the early months of this year exceeded

Credit conditions at Seventh District agricultural banks

	Loan demand (index) ²	Fund availability (index) ²	Loan repayment rates (index) ²	Average loan-to-deposit ratio ¹ (percent)	Interest rates on farm loans		
					Operating loans ¹ (percent)	Feeder cattle ¹ (percent)	Real estate ¹ (percent)
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

¹At end of period.

²Bankers 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.

the proportion expecting a decline by a substantial margin in each of the District states. An anticipated increase in farm operating loans was strongly indicated in every District state and especially so in Iowa and Wisconsin where farmers may have to rely more on debt financing to acquire the inputs needed for their operations this year. Expectations with respect to the amount of other types of farm loans varied widely among the District states, as did the expectations for farm capital expenditures in general this year. For example, a large plurality of the bankers from Illinois, Indiana, and Michigan are expecting first-quarter gains in loans to finance farm machinery and equipment and loans secured by farm real estate. Similarly, a large proportion of the bankers from these states are expecting strength throughout 1994 in overall capital expenditures by farmers, especially for machinery and equipment and for land purchases and improvements. In marked contrast, the responses from Iowa and Wisconsin pointed to a first quarter decline in loans to finance farm machinery and equipment and weakness throughout 1994 for all types of farm capital expenditures.

Interest rates on farm loans made by District banks continued on a downtrend through the end of last year. The District-wide averages of the typical rates charged by the surveyed banks as of the end of the year edged down to 8.50 percent for both farm operating and feeder cattle loans. The average for loans secured by farm real estate retreated to 7.88 percent. The ending 1993 averages were roughly 10 basis points lower than three months

earlier and 60 to 70 basis points lower than a year ago. The most recent declines extended the prevailing downtrend that began in early 1989. Since then, the rates charged by banks on farm loans have retreated about 400 basis points (4 percentage points), dropping to the lowest levels reported in almost 20 years. Whether the downtrend will continue this year is debatable. The modest degree of recent firming in short-term market rates of interest might be countered by more competitive pricing from the revitalized Farm Credit System. Regardless of the trend, most analysts believe that farm loan interest rates will remain at relatively low levels for the foreseeable future.

Gary L. Benjamin

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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)	January	148	2.1	7	6
Crops (index, 1977=100)	January	137	3.0	17	10
Corn (\$ per bu.)	January	2.83	6.0	39	18
Hay (\$ per ton)	January	85.70	1.8	14	25
Soybeans (\$ per bu.)	January	6.85	3.2	23	24
Wheat (\$ per bu.)	January	3.61	0.3	7	2
Livestock and products (index, 1977=100)	January	157	0.6	-1	3
Barrows and gilts (\$ per cwt.)	January	43.30	5.1	3	15
Steers and heifers (\$ per cwt.)	January	72.50	0.7	-8	0
Milk (\$ per cwt.)	January	13.60	0.0	9	1
Eggs (¢ per doz.)	January	61.9	-1.9	-3	7
Consumer prices (index, 1982-84=100)	December	146	0.0	3	6
Food	December	143	0.6	3	4
Production or stocks					
Corn stocks (mil. bu.)	December 1	5,936	N.A.	-25	-9
Soybean stocks (mil. bu.)	December 1	1,554	N.A.	-15	-13
Wheat stocks (mil. bu.)	December 1	1,586	N.A.	0	10
Beef production (bil. lb.)	December	1.95	3.0	5	9
Pork production (bil. lb.)	December	1.55	3.0	2	8
Milk production* (bil. lb.)	December	10.4	4.1	-2	0
Receipts from farm marketings (mil. dol.)	September	16,033	13.0	-5	9
Crops**	September	8,153	29.6	-8	8
Livestock	September	7,656	-2.2	2	8
Government payments	September	224	220.0	-57	115
Agricultural exports (mil. dol.)	November	3,903	0.8	0	-3
Corn (mil. bu.)	November	145	-4.1	-25	-3
Soybeans (mil. bu.)	November	72	-1.7	-14	-20
Wheat (mil. bu.)	November	116	11.1	2	-16
Farm machinery sales (units)					
Tractors, over 40 HP	December	4,958	-9.0	13	6
40 to 100 HP	December	2,417	-22.6	5	11
100 HP or more	December	2,541	9.1	21	1
Combines	December	904	-23.3	12	3

N.A. Not applicable

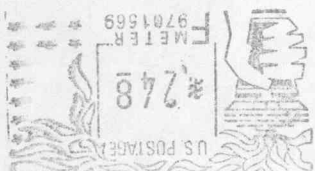
*21 selected states.

**Includes net CCC loans.

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