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Wants

FEDERAL RESERVE BANK OF CHICAGO

AGRICULTURAL

ISSN 0002 - 1512

August 3, 1984

Number 1635

LETTER

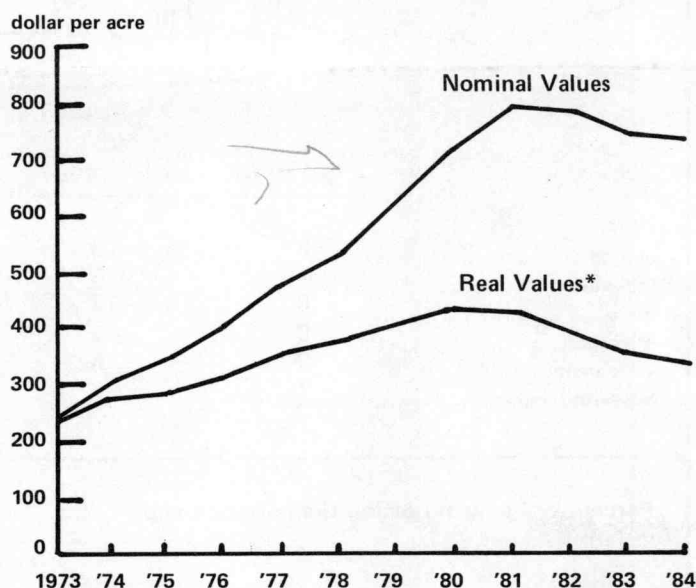
DISTRICT FARMLAND VALUES continued to decline in the second quarter, reflecting low farm sector earnings in recent years and lackluster earnings prospects for the near future. A July 1 survey of 550 agricultural bankers in the Seventh Federal Reserve District indicates that the value of good farmland declined 1 percent during the three months ending in June. This marks the third consecutive quarterly decline in District farmland values, following a slight upturn in the first half of 1983. As a result, District farmland values are almost 8 percent below the level of a year ago and about 20 percent below the 1981 peak. Compared to other states, the decline in land values since the 1981 peak has been particularly apparent in District states.

Farmland market trends in District states continued to vary widely in the second quarter (see map on page 2). Land values in Illinois and Indiana registered large declines, with bankers in those states indicating drops of about 2 and 4 percent, respectively, in the second quarter. Bankers in the remaining District states indicated that farmland values were virtually unchanged during the three-month period.

Relative to a year ago, all District states reported declines in farmland values. For the District as a whole, land values were down almost 8 percent from the mid-1983 level. The year-to-year decline was most pronounced in Iowa where land values registered a 13 percent drop. Declines in the other District states ranged from 2 percent in Michigan to about 5.5 percent in Wisconsin.

Many of the surveyed bankers commented that there was a large amount of land for sale, but few transactions were taking place in their areas. They indicated that the problems of highly leveraged farmers under serious financial stress increased the amount of land on the market, while there was little interest on the part of buyers. Many bankers cited high interest rates, which present cash flow problems to many potential buyers, as contributing to the weakness in the land market.

Average farmland values in the U.S.



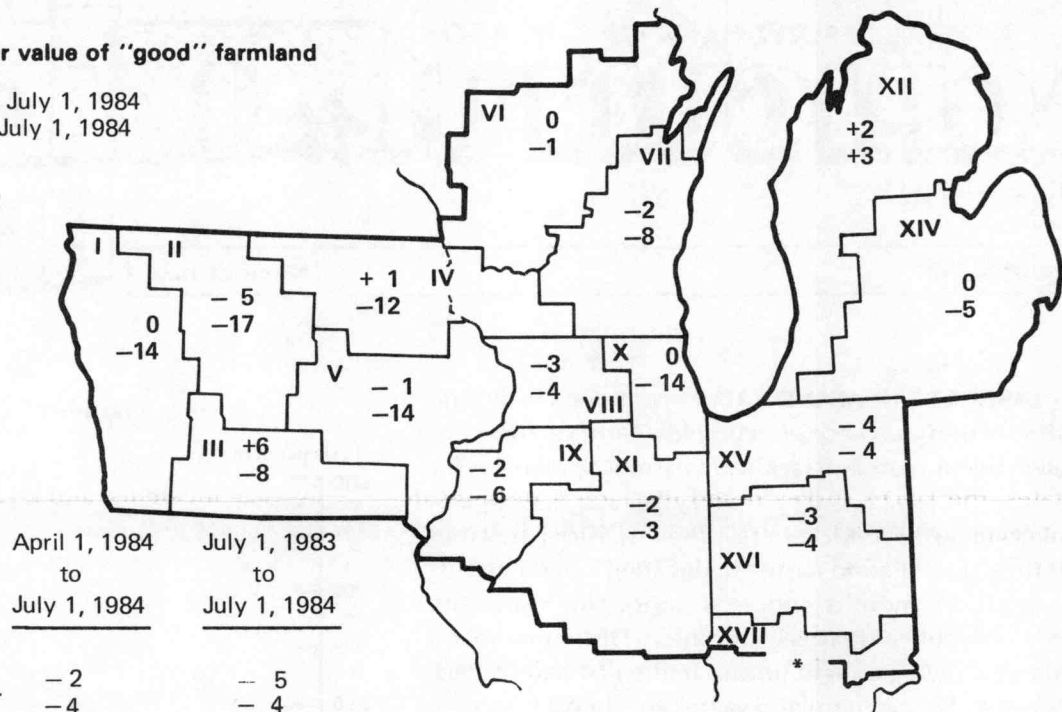
*Adjusted by GNP implicit price deflator.

Interest rates on farm real estate loans continued to rise during the second quarter. The mid-year rates charged on farm real estate loans by surveyed banks averaged 13.9 percent, up from 13.4 percent at the end of the first quarter and 13.2 percent a year ago. Among District states, the rates charged on farm real estate loans ranged from 13.5 percent in Wisconsin to 14.1 percent in Indiana. Loan rates at the Federal Land Banks serving District states moved up as well. After remaining quite stable over the previous three quarters at an average of 11.5 percent, FLB interest rates on new farm mortgages averaged 12 percent on July 1.

The expectations of surveyed bankers concerning farmland values exhibit very little optimism. One-third of the bankers expect land values to continue to decline during the third quarter of this year, while only 1 percent of the surveyed bankers expect farmland values to trend up during the next few months. However, the remaining majority of the bankers foresee stable farmland values in their areas this quarter.

Percent change in dollar value of "good" farmland

Top: April 1, 1984 to July 1, 1984
Bottom: July 1, 1983 to July 1, 1984

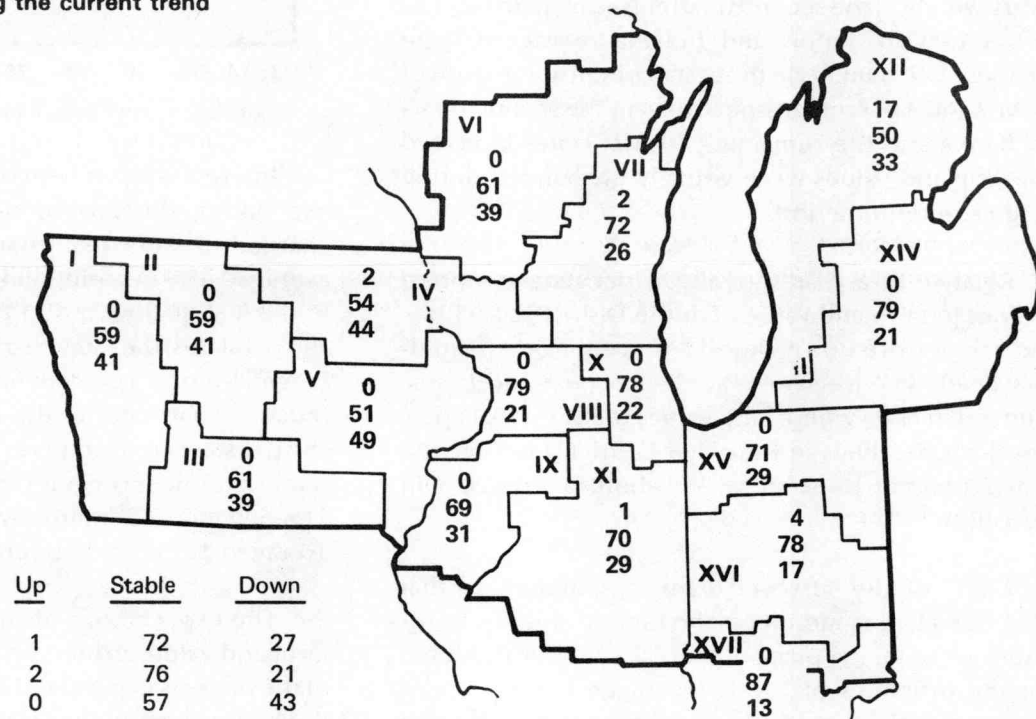


Illinois	-2	-5
Indiana	-4	-4
Iowa	0	-13
Michigan	0	-2
Wisconsin	0	-6
Seventh District	-1	-8

* Insufficient response.

Percent of banks reporting the current trend in farmland values is;

Top: Up
Center: Stable
Bottom: Down



	Up	Stable	Down
Illinois	1	72	27
Indiana	2	76	21
Iowa	0	57	43
Michigan	4	72	24
Wisconsin	2	66	32
Seventh District	1	67	32

Farmland values nationwide have followed a trend similar to the District states in recent years. But trends have been highly variable among individual states and the declines in District states have outstripped the national average. A recent USDA report indicated that, on average, farmland values in the 48 contiguous states declined 1 percent in the year ending April 1, 1984. Among the individual states, however, land values increased in 24 states, declined in 17 states, and remained stable in the other 7 states.

Farmland values last year appreciated the most in Texas, the Northeast, and the Rocky Mountain states. The sharpest declines were registered in the Corn Belt, Lake states, and Northern plains areas. Among these states, the USDA survey noted the largest declines in farmland values were in Iowa and Nebraska, 11 percent and 12 percent, respectively, in the year ending April 1.

The 1 percent fall in U.S. farmland values last year marked the third consecutive annual decline. During this period, average farmland values nationwide fell about 8 percent, but remain slightly above the 1980 level. In contrast, the decline in farmland values in District states has been much steeper, dropping about 20 percent from the 1981 peak and approaching 1978 levels. Adjusting land values to reflect changes in purchasing power over this period results in even larger declines.

Despite the substantial drop in farmland values, much of the gains registered during the 1970s remain intact. Between 1972 and 1979, U.S. farmland values rose at an unprecedented rate, resulting in large real capital gains. Much of these gains are attributable to the boom in farm earnings that accompanied the surge in agricultural exports in the 1970s. Between 1969 and 1979 exports of corn jumped 300 percent, while wheat and soybean exports more than doubled. In terms of real purchasing power, farm income in the 1970s averaged 23 percent above the previous decade's level, and had risen almost one-third above the 1970 level by the end of the decade.

However, the gains in exports and income ended abruptly in the 1980s, and farmland values started to

decline. The export boom of the 1970s has given way to four consecutive years of declining export shipments. Moreover, continued high levels of production pressured prices lower, resulting in declines in farm sector earnings. In addition, the financial stress of many highly leveraged farm operations that had expanded during the 1970s became apparent.

These considerations have had a large effect on District farmland values. The importance of export crops to the region contributed to the above average rise in land values during the 1970s, as well as the proportionately large decline in land values during the past few years. Moreover, the potential for financial stress may be higher among some District states because of an above average incidence and level of debt. To the extent that financial stress increases the amount of land on the market, it can have a large effect on land values because of the relatively small proportion of farmland that is transferred in a year, typically less than 3 to 4 percent. In addition, financial stress, or the potential for it, can limit the willingness and the ability of prospective buyers to bid for farmland.

The skepticism of the surveyed bankers regarding the trend in farmland values in the coming months reflects these factors. Initial forecasts of exports of major midwestern crops do not point to significant increases in the coming fiscal year. Similarly, the farm income estimates for 1984 do not signal a boom in farm earnings. It is likely, then, that financial stress will remain a problem for some highly leveraged farmers. Moreover, lower milk support prices, and prospects for additional cuts in 1985, will place additional pressure on dairy producers. In addition, the formulation of the new farm legislation, at a time when pressure to limit the growth in government spending is mounting, has contributed to uncertainty regarding the future level of government support for agriculture. These considerations will likely contribute to further weakness in farmland values during the coming months.

Peter J. Heffernan

Selected Agricultural Economic Indicators

	Latest period	Value	Percent change from		
			Prior period	Year ago	Two years ago
Prices received by farmers (1977=100)	July	143	- 0.7	+ 9	+ 5
Crops (1977=100)	July	140	+ 3.7	+13	+12
Corn (\$ per bu.)	July	3.32	- 1.5	+ 6	+33
Oats (\$ per bu.)	July	1.77	- 1.7	+21	+13
Soybeans (\$ per bu.)	July	6.81	-14.8	+ 9	+14
Wheat (\$ per bu.)	July	3.29	- 4.6	- 1	+ 1
Livestock and products (1977=100)	July	145	+ 1.4	+ 5	- 1
Barrows and gilts (\$ per cwt.)	July	53.60	+ 7.0	+18	- 9
Steers and heifers (\$ per cwt.)	July	62.50	+ 1.6	+ 4	- 1
Milk (\$ per cwt.)	July	12.90	+ 0.8	- 2	- 2
Eggs (¢ per doz.)	July	59.9	- 1.8	+ 4	+ 9
Prices paid by farmers (1977=100)	July	166	0	+ 4	+ 5
Production items	July	156	- 0.6	+ 3	+ 3
Feed	July	137	- 2.8	+ 4	+11
Feeder livestock	July	154	+ 2.7	0	- 8
Fuels and energy	July	201	- 1.0	- 2	- 6
Producer prices (1967=100)	June	291	- 0.1	+ 2	+ 4
Agricultural machinery and equipment	June	337	- 0.1	+ 3	+ 9
Fertilizer materials	June	240	- 1.2	+ 5	- 3
Agricultural chemicals	June	449	+ 1.0	- 2	- 3
Consumer prices (1967=100)	June	311	+ 0.3	+ 4	+ 7
Food	June	302	+ 0.2	+ 3	+ 5
Production or stocks					
Corn stocks (mil. bu.)	June 1	2,137	N.A.	-57	-45
Soybean stocks (mil. bu.)	June 1	456	N.A.	-42	-29
Beef production (bil. lbs.)	June	1.98	- 3.6	+ 1	N.A.
Pork production (bil. lbs.)	June	1.16	- 9.8	- 9	N.A.
Milk production (bil. lbs.)	June	11.8	- 3.7	- 4	N.A.

N.A. Not applicable

AGRICULTURAL LETTER
FEDERAL RESERVE BANK
OF CHICAGO
Public Information Center
P.O. Box 834
Chicago, Illinois 60690

Tel no. (312) 322-5111



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