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AgLetter

FARMLAND VALUES AND CREDIT CONDITIONS

Farmland values in the Seventh Federal Reserve District were unchanged, on average, during the third quarter (July 1–October 1), according to our survey of 346 agricultural bankers. However, the bankers believed that farmland values were up a modest 2 percent for the twelve-month period ending October 1. The respondents also reported the demand for farm loans softened in the third quarter, but that loan-to-deposit ratios and farm loan interest rates moved higher. Furthermore, the bankers anticipate the fall and winter months will bring continued downward pressure on farm earnings, resulting in weak loan repayments, and perhaps an increase in sales of capital assets among financially stressed farmers.

The movement in farmland values varied across the individual District states, yet continued to follow the familiar pattern identified in recent surveys, i.e., considerably greater strength in Michigan and Wisconsin compared to the other three states. This pattern has been in evidence now for almost two years, but the differences among the individual states usually averaged out to little change for the District as a whole. For the third quarter, bankers reported a small decline in farmland values in Indiana

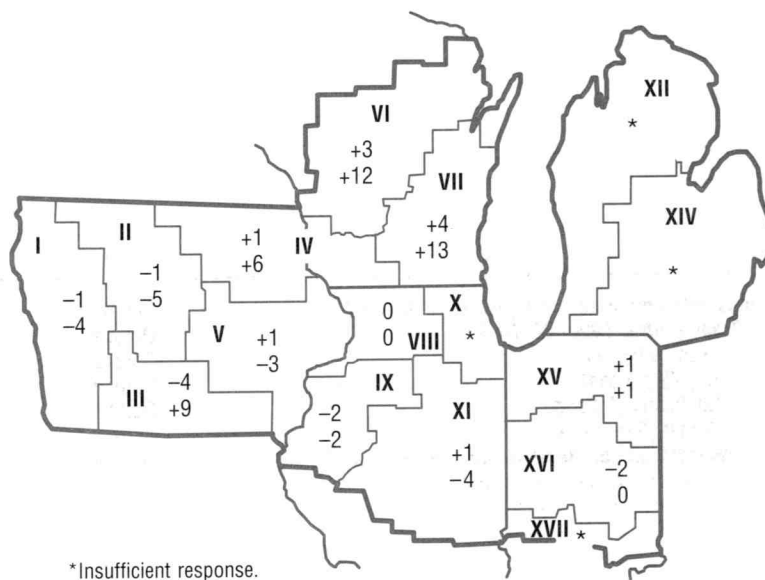
and Iowa, but no change in Illinois. In contrast, those in Michigan and Wisconsin reported significant gains of 4 percent and 3 percent, respectively. For the twelve-month period ending October 1, farmland values in Illinois and Iowa were down a modest 3 percent and 1 percent, respectively. Bankers in Indiana reported a small twelve-month increase of 1 percent, while those in Michigan and Wisconsin again reported solid gains.

Looking ahead, a rising majority of District bankers foresee stability in farmland values in the near term. Approximately 60 percent reported they anticipate no change in farmland values during the fourth quarter (compared to the 47 percent that fell into this category during the prior survey), while a third anticipate a decline. Nonetheless, there is considerable uncertainty among farmers and bankers in rural communities. The source of this uncertainty becomes apparent when reviewing several performance indicators of the farm economy, which provide a mixed picture at best. First, net cash income to the farm sector is projected by the U.S. Department of Agriculture (USDA) to reach \$57.9 billion this year, a 5 percent increase over last year and the third highest ever. While this would at first appear to be a promising development, it includes

Percent change in dollar value of "good" farmland

Top: July 1, 1999 to October 1, 1999
Bottom: October 1, 1998 to October 1, 1999

	July 1, 1999 to October 1, 1999	October 1, 1998 to October 1, 1999
Illinois	0	-3
Indiana	-1	+1
Iowa	-1	-1
Michigan	+4	+8
Wisconsin	+3	+12
Seventh District	0	+2



a record-high level of direct government payments (\$22.5 billion), which is not sustainable over the long haul due to political and budgetary pressures.

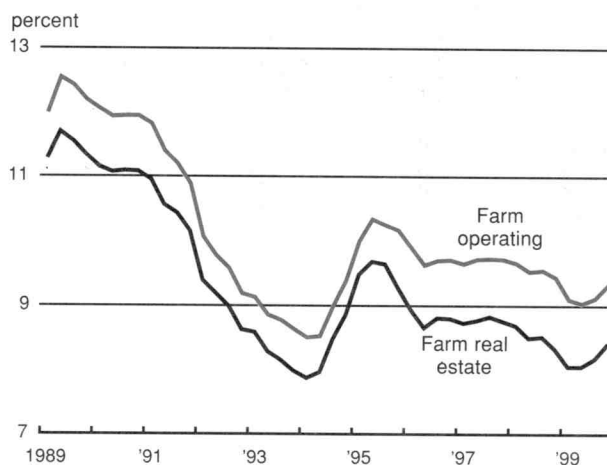
Exports are another important performance indicator for the farm sector. The USDA predicts the value of farm exports will register a 2 percent increase during the current fiscal year (October–September), which comes on the heels of a three-year decline. While Midwest farmers will benefit from the anticipated increase in the value of soybean, meal, red meat, and dairy exports, this will be offset by a decline in the export value of soybean oil and corn. In addition, the reluctance of the European Union to allow imports of corn and soybeans containing genetically modified material has cast a pall over U.S. farm exports. Finally, farmers have benefitted from firm fed cattle and milk prices in recent months, but hog, corn, and soybean prices are still relatively weak. However, many bankers wrote in to say that strong corn and soybean yields are going a long way towards offsetting low prices.

Economic conditions in the agricultural sector have taken many farmers out of the market for farmland and increased the relative importance of nonfarm investors. The majority of respondents expect that farmer interest in purchasing farmland over the fall and winter will decline relative to a year earlier. The exception is Wisconsin, where the demand by farmers is reported to be stable to somewhat higher than a year ago, no doubt reflecting several months of strong milk prices and favorable feed costs. In addition, the bankers reported the demand for farmland among nonfarm investors is expected to be stable to rising during the fall and winter, relative to a year earlier, and appears particularly strong in Wisconsin. This interest on the part of both farmers and nonfarm investors in Wisconsin suggests that demand-side strength will provide near-term support to farmland values in that state.

Turning to credit conditions, the index of nonreal estate loan demand came in at 109 for the third quarter, down slightly from three months earlier. The index reflects the 32 percent of the respondents that indicated farm loan demand increased—relative to a year earlier—less the 23 percent that stated there had been a decrease. A larger segment, 46 percent, indicated that demand was steady. The responses from bankers in individual states suggested that loan demand was up in Illinois and Iowa, relative to a year earlier, but fairly stable in the other three states.

Call report data suggest that farm loan volume at agricultural banks grew more slowly this year within the District than in the rest of the U.S. Moreover, further gains in loan volume will likely be modest at District banks throughout the fall and winter. According to the surveyed

Quarterly District farm loan rates



bankers, nonreal estate farm lending over the next six months is expected to increase relative to a year ago in Iowa and Illinois, but will probably be steady in the other three states. The anticipated gains are primarily due to operating loans, as machinery lending is expected to remain weak. In addition, bankers reported they expect to make greater use of Farm Service Agency loan guarantees to improve the credit quality of their loan portfolios, especially in Iowa. In comparison, lending for farm real estate is expected to be stable to declining during the fall and winter, relative to a year earlier. However, Wisconsin bankers show more optimism than do their counterparts in the other District states.

Interest rates charged on new farm loans rose during the third quarter, on average. The interest rate on new operating loans came in at 9.3 percent, 20 basis points higher than three months earlier. In addition, the average rate charged on new farm real estate loans was 8.4 percent, up 25 basis points from three months earlier. Among District states, the average farm operating loan rate ranged from a low of 9 percent in Illinois to a high of 9.9 percent in Michigan, while the average real estate farm loan rate ranged from a low of 8.2 percent in Illinois to a high of 8.9 percent in Michigan. The average loan-to-deposit ratio for the District registered a typical seasonal increase in the third quarter; at a level of 72.7 percent, it tied the previous high reported for this survey. Regarding the availability of funds for farm lending, the situation was essentially stable relative to a year earlier, with 71 percent of the respondents indicating there had been no change.

With respect to farm loan repayment rates, only 4 percent of the respondents reported an increase in repayment rates relative to a year earlier, while 41 percent reported a decline. The remainder, about 55 percent, indicated that

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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)
1995							
Jan-Mar	122	96	98	64.8	10.33	10.26	9.68
Apr-June	124	104	93	66.1	10.24	10.20	9.64
July-Sept	123	104	98	67.3	10.16	10.14	9.27
Oct-Dec	111	123	119	64.9	9.89	9.88	8.93
1996							
Jan-Mar	125	125	117	65.0	9.62	9.63	8.66
Apr-June	116	114	108	65.8	9.69	9.69	8.81
July-Sept	122	113	112	68.2	9.70	9.68	8.80
Oct-Dec	122	110	94	67.6	9.64	9.61	8.73
1997							
Jan-Mar	134	110	105	67.6	9.71	9.65	8.77
Apr-June	134	97	94	69.7	9.72	9.68	8.83
July-Sept	131	97	93	70.2	9.71	9.69	8.76
Oct-Dec	120	109	95	70.7	9.65	9.63	8.69
1998							
Jan-Mar	134	113	84	68.9	9.52	9.51	8.50
Apr-June	127	102	74	72.7	9.54	9.55	8.52
July-Sept	117	104	60	72.0	9.43	9.41	8.33
Oct-Dec	113	121	57	70.3	9.09	9.07	8.06
1999							
Jan-Mar	120	119	40	69.9	9.03	9.01	8.06
Apr-June	115	107	50	71.7	9.11	9.08	8.18
July-Sept	109	94	63	72.7	9.32	9.28	8.42

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.

farm loan repayments were coming in at a pace similar to last year. This marks the tenth consecutive quarter in which the number of bankers reporting a year-over-year decline has exceeded the number reporting an increase, and underscores the continuing financial difficulties faced by farm banks and their primary customers. Bankers also indicated they expect the weakness in farm loan repayments to continue throughout the fall and winter.

Bankers were also asked to weigh in with their outlook for this fall and winter regarding net farm earnings and asset liquidation among financially stressed farmers. About 75 percent expect a year-over-year decline in net cash earnings for crop farmers, while 60 percent anticipate a decline in earnings for cattle and hog farmers. In comparison, the consensus for dairy is that net cash earnings will be stable to declining. It seems unusual that such a large proportion of the respondents believe earnings to cattle and hog farmers will decline given that beef cattle prices are relatively strong and hog prices, while still low, are currently above year-earlier levels. However, the responses may simply reflect the impact of many months of low commodity prices and resulting concern for the future—especially for small and mid-sized farm operations—that permeates many farm-oriented communities

in the Midwest. Finally, over 60 percent of the respondents in Illinois, Indiana, and Iowa believe there will be an increase in the liquidation of capital assets among financially stressed farmers this fall and winter, relative to a year earlier. However, the survey was conducted prior to Congressional approval of the emergency farm aid package in late October, which may help ease the situation for those farmers having financial difficulties.

Mike A. Singer and Nawsheen Rabbani

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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, 1990-92=100)	October	92	-5.2	-7	-14
Crops (index, 1990-92=100)	October	88	-7.4	-12	-23
Corn (\$ per bu.)	October	1.66	-5.1	-13	-35
Hay (\$ per ton)	October	73.70	-1.1	-12	-26
Soybeans (\$ per bu.)	October	4.49	-1.8	-13	-31
Wheat (\$ per bu.)	October	2.49	-3.1	-10	-30
Livestock and products (index, 1990-92=100)	October	97	-1.0	-1	0
Barrows and gilts (\$ per cwt.)	October	28.20	-17.5	0	-41
Steers and heifers (\$ per cwt.)	October	70.10	4.5	14	4
Milk (\$ per cwt.)	October	15.50	-1.9	-12	10
Eggs (¢ per doz.)	October	50.1	-11.6	-24	-24
Consumer prices (index, 1982-84=100)	September	168	0.5	3	4
Food	September	165	0.2	2	4
Production or stocks					
Corn stocks (mil. bu.)	September 1	1,796	N.A.	37	103
Soybean stocks (mil. bu.)	September 1	348	N.A.	74	164
Wheat stocks (mil. bu.)	September 1	2,459	N.A.	3	18
Beef production (bil. lb.)	September	2.28	-1.4	4	7
Pork production (bil. lb.)	September	1.62	3.4	2	9
Milk production* (bil. lb.)	September	11.2	-2.6	5	6
Receipts from farm marketings (mil. dol.)	July	15,030	-9.9	-5	-4
Crops**	July	6,292	1.0	-16	-19
Livestock	July	8,061	-0.4	-1	2
Government payments	July	677	-71.4	N.A.	N.A.
Agricultural exports (mil. dol.)	August	3,949	6.2	7	-11
Corn (mil. bu.)	August	184	-1.5	34	29
Soybeans (mil. bu.)	July	37	2.5	27	59
Wheat (mil. bu.)	July	116	20.1	31	22
Farm machinery sales (units)					
Tractors, over 40 HP	September	4,624	0.1	2	-27
40 to 100 HP	September	3,404	-10.3	-2	-16
100 HP or more	September	1,220	47.9	17	-46
Combines	September	498	59.1	-58	-58

N.A. Not applicable

*20 selected states.

**Includes net CCC loans.

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