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AgLetter

FARMLAND VALUES AND CREDIT CONDITIONS

Summary

Farmland values for the second quarter of 2011 climbed 17 percent from the level of a year ago in the Seventh Federal Reserve District. The value of "good" agricultural land increased 4 percent in the second quarter compared with the first quarter of 2011, according to a survey of 226 agricultural bankers in the District. Over 60 percent of the respondents forecasted farmland values to stabilize in the third quarter of 2011, yet about one-third still expected farmland values to move higher.

Agricultural credit conditions were stronger in the second quarter of 2011 relative to a year earlier, as illustrated by a decrease to 2 percent in the portion of agricultural loans perceived by respondents as having "major" or "severe" repayment problems. Repayment rates for non-real-estate farm loans were higher than a year ago, while renewals and extensions of these loans were lower. Funds availability for lending was up relative to the second quarter of 2010. The demand for non-real-estate loans remained weaker than a year earlier. Interest rates on agricultural operating loans and mortgages dropped under the lows set six months ago. The average loan-to-deposit ratio for the District inched up to 70.3 percent in the second quarter of 2011 from 69.8 in the previous quarter.

CONFERENCE ANNOUNCEMENT
Rising Farmland Values: Causes and Cautions

On November 15, 2011, the Federal Reserve Bank of Chicago will hold a conference to explore the factors contributing to large increases in agricultural land values and cash rental rates in the Midwest. For more details, including the agenda, and to register, go to www.chicagofed.org/webpages/events/2011/agriculture_conference.cfm.

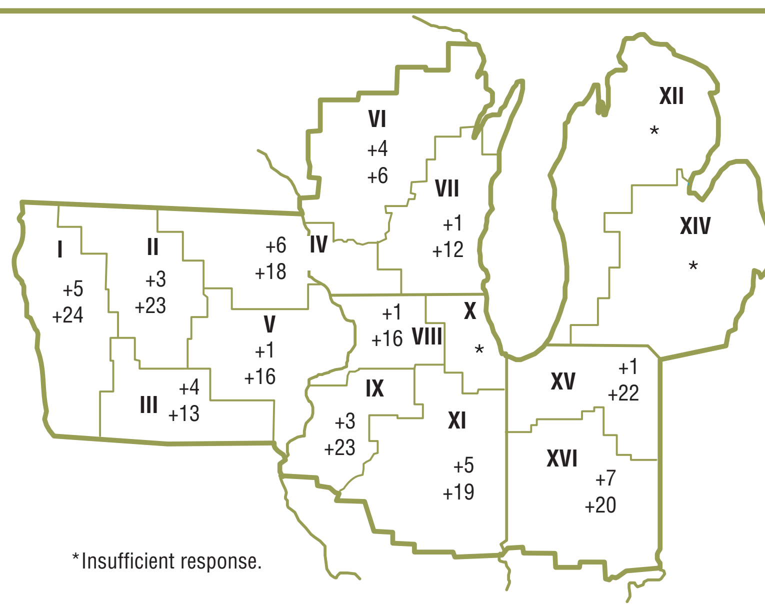
Farmland values

At 17 percent (see chart 1 on the next page), the year-over-year increase in the value of District farmland for the second quarter of 2011 was the largest recorded since the 1970s. Among the District states, only Wisconsin had a smaller year-over-year increase in farmland values in the second quarter of 2011 than in the first quarter of 2011. Agricultural land values in Indiana and Iowa climbed 20 percent or more in a year, and agricultural land values in Illinois climbed almost as much. "Good" agricultural land in the District rose 4 percent in the second quarter of 2011 relative to the first quarter of 2011 (see table and map below). The District had a smaller quarterly increase than last quarter; also, none of the District states had a quarterly increase that exceeded the previous one. Bankers in the survey commented that there were more summer auctions

Percent change in dollar value of "good" farmland

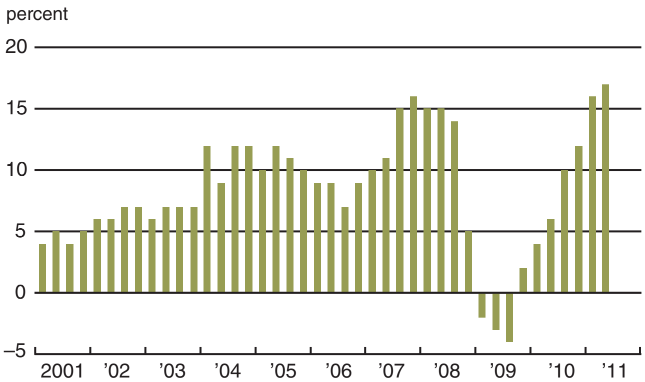
Top: April 1, 2011 to July 1, 2011
Bottom: July 1, 2010 to July 1, 2011

	April 1, 2011 to July 1, 2011	July 1, 2010 to July 1, 2011
Illinois	+3	+19
Indiana	+5	+21
Iowa	+3	+20
Michigan	+3	+12
Wisconsin	+4	+8
Seventh District	+4	+17



*Insufficient response.

1. **Year-over-year changes in Seventh District farmland values, by quarter**



of farmland than usual, particularly as demand for farmland remained strong from both farmers and investors.

Some bankers expressed concerns about the risks facing farmland markets, especially with regard to declines in crop prices. However, these views formed a minority, as just 2 percent of responding bankers expected farmland values to fall in the third quarter of 2011. Thirty-six percent of survey respondents anticipated higher farmland values in the third quarter, and 62 percent expected no change.

Higher crop prices have boosted the expected stream of earnings from crop production, supporting further gains in farmland values. Based on data from the U.S. Department of Agriculture (USDA), crop revenue for 2010 in the District jumped 34 percent above that for 2009, despite below-trend corn yields. The District value of corn for grain produced in 2010 was $31.8 billion, and the value of soybeans was $16.6 billion. In 2011, corn and soybean prices have stayed well above the levels of a year ago. Relative to a year earlier, July corn prices were 85 percent higher and July soybean prices were 37 percent higher.

The USDA estimated that the nation's 2011 harvest of corn for grain will be 3.8 percent larger than the 2010 harvest. It also estimated that the five District states' 2011 harvest of corn for grain will be 7.0 percent larger than the previous year's harvest. Soybean production was estimated to decline 8.2 percent for the U.S. and 8.1 percent for the five District states. Total usage of corn, at 13.2 billion bushels, would result in U.S. ending stocks of 714 million bushels—the tightest in 15 years. Total soybean usage in the U.S. of 3.15 billion bushels would leave ending stocks at 155 million bushels, tighter than a year ago. The USDA estimated price intervals for the 2011–12 crop year of $6.20 to $7.20 per bushel for corn and $12.50 to $14.50 per bushel for soybeans. Based on the midpoints of these projected price ranges, the values of U.S. corn and soybean crops would be 30 percent and 6.0 percent higher in 2011 than in 2010, respectively.

In addition, livestock prices in July 2011 were well above the levels of 2010. Prices for hogs, cattle, and milk were 23 percent, 20 percent, and 39 percent higher this July than last July, respectively. The livestock sector has experienced higher revenues, but higher feed costs have limited the rise in income for the sector. The combination of higher revenues for crop and livestock production has been an impetus for the significant increases in agricultural land values seen this year in the District.

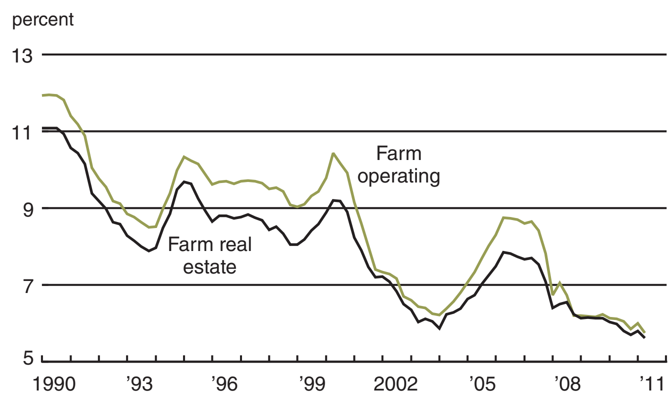
Credit conditions

Higher farm revenues also aided agricultural credit conditions in the District. Agricultural loans with "major" or "severe" repayment problems decreased to 2 percent of District loan volume. In the District's major corn- and soybean-producing states, between 1 percent and 2 percent of farm loan volume was problematic, but Michigan and Wisconsin had close to 4 percent of loan volume with troubled status. Repayment rates for non-real-estate farm loans improved during the second quarter of 2011 compared with a year earlier. The index of loan repayment rates was 133, as 36 percent of the surveyed bankers reported higher rates of loan repayment and 3 percent reported lower rates. Renewals and extensions of non-real-estate agricultural loans in the second quarter of 2011 were lower than in the same quarter of 2010, as 4 percent of respondents saw increases and 27 percent saw decreases.

The index of non-real-estate agricultural loan demand fell to its lowest level since 1987. With 16 percent of the responding bankers observing higher demand and 37 percent observing lower demand, the index of non-real-estate agricultural loan demand was 79. At 70.3 percent, the District average for loan-to-deposit ratios remained near the previous quarter's post-1997 low. The ratio desired by the banks was 78.7 percent—with 24 percent of the banks at or above this level.

Funds availability continued to be stronger, with 49 percent of the banks having more funds available and

2. **Quarterly Seventh District farm loan interest rates**



Credit conditions at Seventh District agricultural banks

	Loan demand	Funds availability	Loan repayment rates	Average loan-to-deposit ratio	Interest rates on farm loans: Operating loans[a]	Feeder cattle[a]	Real estate[a]
	(index)[b]	*(index)*[b]	*(index)*[b]	*(percent)*	*(percent)*	*(percent)*	*(percent)*
2009							
Jan–Mar	116	112	105	76.2	6.20	6.31	6.14
Apr–June	88	118	93	77.3	6.18	6.36	6.16
July–Sept	95	121	89	75.3	6.17	6.35	6.13
Oct–Dec	102	125	92	75.4	6.23	6.40	6.13
2010							
Jan–Mar	109	127	79	73.7	6.13	6.25	6.04
Apr–June	98	122	85	74.5	6.12	6.25	5.99
July–Sept	90	138	114	73.2	6.05	6.14	5.81
Oct–Dec	101	142	142	71.8	5.85	6.02	5.70
2011							
Jan–Mar	81	149	146	69.8	6.01	5.93	5.80
Apr–June	79	145	133	70.3	5.75	5.91	5.62

[a]At end of period.
[b]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 percentage of bankers that responded "lower" from the percentage that responded "higher" and adding 100.
Note: Historical data on Seventh District agricultural credit conditions are available for download from the *AgLetter* webpage, www.chicagofed.org/webpages/publications/agletter/index.cfm.

4 percent having less. The resulting index of funds availability was 145. Banks tightened their collateral requirements for loans in the second quarter of 2011 relative to the second quarter of the prior year, with 16 percent of banks requiring more collateral and 1 percent requiring less.

Farm interest rates were even lower than the previous records for the survey seen in the fourth quarter of 2010 (see chart 2). As of July 1, 2011, the District average for interest rates on new operating loans was 5.75 percent, over 300 basis points below the most recent peak of five years ago. Agricultural mortgage rates averaged 5.62 percent, about 220 basis points lower than five years earlier. These record low mortgage rates contributed to the surge this year in District farmland values.

During the second quarter of 2011, strengthening agricultural credit conditions, along with weaker loan demand, created a very competitive environment for farm lending. Banks faced competitive challenges in maintaining their agricultural loan portfolios, let alone expanding them. According to respondents, farm loans by banks diminished in the first half of 2011. This was especially true for operating loans: Only 21 percent of the responding bankers originated more loans for operations than normal, whereas 32 percent originated a smaller-than-normal amount of loans. Banks in Illinois, Indiana, and Michigan gave signs of higher volumes for farm real estate loans. Volumes for operating loans and mortgages by the Farm Credit System (FCS) were higher than typical in the first six months of 2011. In particular, 56 percent of respondents observed more farm mortgages by FCS lenders in their respective vicinities during the first half of 2011, while 5 percent observed fewer FCS mortgages. Similarly, merchants, dealers, and other input suppliers expanded their agricultural lending, according to 36 percent of the reporting banks, while 7 percent saw declines in this type of lending. Lending by life insurance companies to farmers was less than typical in the January through June period of 2011.

Looking forward

Responding bankers expected non-real-estate agricultural loan volumes to decrease in the third quarter of 2011 compared with the same quarter of 2010. Volumes for farm machinery and grain storage construction loans were forecasted to rise during the third quarter of 2011 from a year ago. For the July through September period of 2011, 21 percent of the respondents anticipated higher farm real estate loan volumes than in the same period a year earlier, while 13 percent anticipated lower volumes.

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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)*	July	181	1.1	31	39
Crops *(index, 1990–92=100)*	July	207	−0.5	41	39
Corn *($ per bu.)*	July	6.46	1.3	85	79
Hay *($ per ton)*	July	170	4.3	52	53
Soybeans *($ per bu.)*	July	13.40	1.5	37	24
Wheat *($ per bu.)*	July	7.18	−3.0	60	39
Livestock and products *(index, 1990–92=100)*	July	156	2.0	18	39
Barrows & gilts *($ per cwt.)*	July	72.40	2.8	23	65
Steers & heifers *($ per cwt.)*	July	115.00	4.5	20	35
Milk *($ per cwt.)*	July	22.10	4.2	39	96
Eggs *($ per doz.)*	July	0.88	−0.3	24	24
Consumer prices *(index, 1982–84=100)*	July	224	−0.2	3	4
Food	July	228	0.2	4	5
Production or stocks					
Corn stocks *(mil. bu.)*	June 1	3,670	N.A.	−15	−14
Soybean stocks *(mil. bu.)*	June 1	619	N.A.	8	4
Wheat stocks *(mil. bu.)*	June 1	861	N.A.	−12	31
Beef production *(bil. lb.)*	June	2.37	11.4	2	4
Pork production *(bil. lb.)*	June	1.82	3.4	−1	−2
Milk production *(bil. lb.)**	June	15.4	−4.3	1	4
Agricultural exports *($ mil.)*	May	10,869	−7.8	31	45
Corn *(mil. bu.)*	May	164	−4.8	−5	10
Soybeans *(mil. bu.)*	May	34	−48.5	7	−43
Wheat *(mil. bu.)*	May	127	−13.6	86	89
Farm machinery *(units)*					
Tractors, over 40 HP	July	6,468	N.A.	−3	−5
40 to 100 HP	July	4,237	N.A.	−8	−6
100 HP or more	July	2,231	N.A.	9	−2
Combines	July	856	N.A.	−28	−25

N.A. Not applicable.
*23 selected states.
Sources: Author's calculations based on data from the U.S. Department of Agriculture, U.S. Bureau of Labor Statistics, and the Association of Equipment Manufacturers.