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AgLetter

CHANGES IN FARMLAND VALUES ARE MIXED ACROSS THE DISTRICT

Our survey of 360 agricultural bankers indicated that farmland values held steady, on average, during the fourth quarter of 1998 in the Seventh Federal Reserve District. District farmland values rose 1 percent for all of 1998, as weakness during the second half offset the gains registered earlier in the year. This is the smallest calendar-year increase since 1991 and comes on the heels of two consecutive annual 10-percent gains. However, these averages mask sharply divergent trends among the individual District states. In addition, the demand for new farm loans increased modestly from a year earlier, as did available funding for new farm loans. Interest rates registered a slight decline, but farm loan repayment rates continued to show weakness. As a result, bankers indicated that the quality of their agricultural loan portfolios declined. Furthermore, bankers reported that credit conditions were worse in Illinois, Indiana, and Iowa than in either Michigan or Wisconsin.

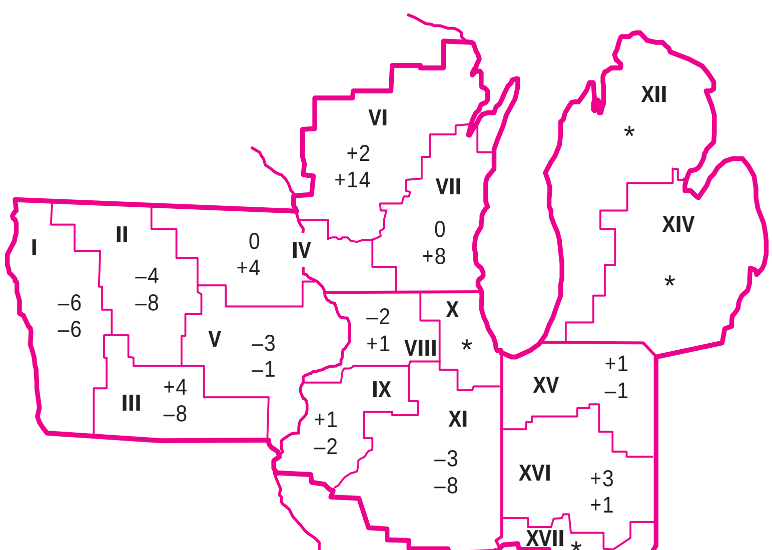
There was considerable variation among District states with respect to both the quarterly and the annual changes in farmland values (see map). While farmland values declined during the fourth quarter in both Illinois and Iowa, they rose in the other three states. Furthermore, the pattern of change in farmland values among District states for the year tended to mirror that of the fourth quarter. Bankers in Illinois and Iowa reported annual declines of 4 percent and 5 percent, respectively, while those in Michigan and Wisconsin reported double-digit gains. Indiana fell between the two extremes, with bankers there reporting no net change for 1998. Farmland values in both Wisconsin and Michigan have been held up by strong returns to dairy operations, and anecdotal reports suggest that strong recreational demand is also an important factor in supporting farmland values in these two states.

The bankers' outlook for future changes in farmland values was similar to that reported three months earlier and may have even improved slightly. Half the respondents reported they expect farmland values to be stable during the first quarter of 1999, while 43 percent expect a decline. Not surprisingly, the degree of optimism was relatively stronger in Wisconsin and Michigan. However, it was somewhat surprising (and encouraging) that the bankers did not exhibit increasing pessimism toward farmland values given the rapid decline of hog prices during the fourth quarter and the sluggishness of corn and soybean prices. The partial recovery in hog

Percent change in dollar value of "good" farmland

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

	October 1, 1998 to January 1, 1999	January 1, 1998 to January 1, 1999
Illinois	–2	–4
Indiana	+2	0
Iowa	–2	–5
Michigan	+5	+14
Wisconsin	+1	+12
Seventh District	0	+1



*Insufficient response.

prices in early January and predictions of further gains in coming months may have added a bit more optimism to the mix. In addition, several bankers noted that many of their customers enjoyed above-average crop yields this past fall, which offset the impact of low grain prices.

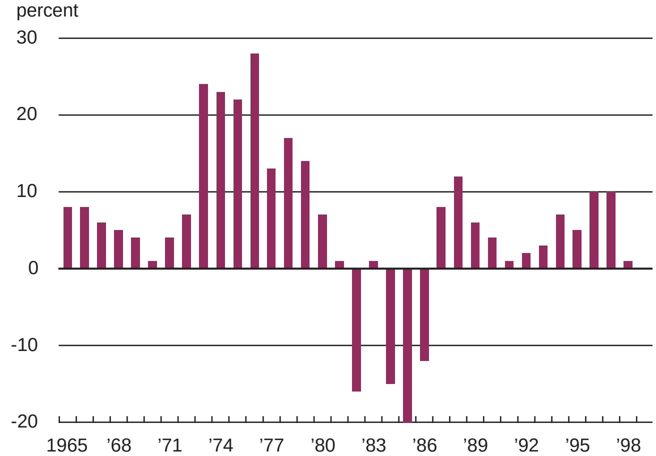
Turning to credit conditions, the survey respondents reported the demand for new farm loans was up modestly from a year earlier. The measure of loan demand came in at 113, similar to that reported three months earlier. Overall, this measure represents the 33 percent of the bankers that reported a year-over-year increase in loan demand during the fourth quarter, less the 20 percent that reported a decline. The remainder (47 percent) indicated that loan demand was unchanged from a year ago. In general, loan demand registered firm gains in Illinois and Iowa, but declined in Wisconsin and Michigan. Little change was reported by the Indiana bankers.

Farm loan repayments continue to suffer from low commodity prices and registered a year-over-year decline for the seventh consecutive quarter. The loan repayment index stood at 57, the lowest reading since 1985. Overall, only 8 percent of the respondents noted an improvement in loan repayments, while 51 percent reported a decline. The most widespread weakness in loan repayments was noted by bankers in Illinois, Indiana, and Iowa, in large part because of the precipitous decline in hog prices during the fourth quarter and the continuing weakness in grain prices. However, loan repayments during the fourth quarter improved (relative to a year earlier) in Wisconsin thanks to record-high milk prices.

In general, the funding situation for new agricultural loans at District banks improved during the fourth quarter. Bankers reported an increase in the level of funds available for agricultural lending as well as a small increase in overall liquidity. For the District, 28 percent of the bankers reported a year-over-year improvement in the level of funds available for agricultural lending, while 6 percent reported a decline. The reminder, about two-thirds, indicated there had been no change from a year earlier. The breakdown was similar for all District states except Wisconsin, where the improvement in fund availability was markedly better. In addition, the improvement in liquidity at District agricultural banks during the fourth quarter followed the typical seasonal pattern. The average loan-to-deposit ratio for all District banks dropped from 72 percent on October 1, 1998 to 70.3 percent on January 1, 1999. About half the of the respondents indicated a desire to increase lending levels.

Interest rates charged on new farm loans eased during the fourth quarter of 1998. The average rate for new farm real estate loans declined 27 basis points during

Annual percentage change in Seventh District farmland values



the quarter to 8.06 percent as of January 1. In addition, the rate charged on new farm operating loans dropped 34 basis points to 9.09 percent. Among the individual District states, the average rate on farm operating loans ranged from 8.83 percent in Illinois to 9.43 percent in Michigan. The average rate charged on new farm real estate loans ranged from a low of 7.85 percent in Iowa to a high of 8.48 percent in Wisconsin as of January 1.

Unit sales of farm tractors and combines registered strong year-over-year gains during the first half of 1998, but fell off rapidly in the second half as farm commodity prices deteriorated. District agricultural bankers expect this weakness to continue in 1999, as nearly 70 percent of the respondents stated they believe that spending by farmers on machinery and equipment will decline this year. Furthermore, a large share of the bankers indicated that capital expenditures on other categories--land purchases / improvements, buildings / facilities, and trucks / autos--will decline as well. But in a now-familiar pattern, a larger proportion of the bankers in Illinois, Indiana, and Iowa anticipate cuts in capital spending than in Michigan or Wisconsin. In fact, the proportion of respondents in Wisconsin that expect an increase in capital expenditures exceeded the share that anticipate a decline.

To help gauge the impact of the decline in farm commodity prices, bankers were also asked whether they had changed their credit standards for approving agricultural loans during the fourth quarter. Approximately half the respondents reported they had indeed tightened their standards to some extent, relative to a year earlier, while most of the remainder indicated their standards remained unchanged. A larger share of banks in Illinois, Indiana, and Iowa reported some tightening of their standards than in Michigan or Wisconsin.

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	70.6	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

[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.

Bankers also noted a marginal decline in credit quality when compared with the reading taken six months earlier. They indicated that, on average, 92 percent of their farm loan portfolios were classified as having either no significant repayment problems or only minor problems. In comparison, 95 percent of the average portfolio received a similar rating last July. The slip in credit quality corresponds to the fall in commodity prices, the decline in the loan repayment index, and the reported increase in loan renewals or extensions. However, the quality of agricultural loan portfolios was stable to slightly improved in Michigan and Wisconsin.

During the fourth quarter free-fall in hog prices, a topic of increasing concern was the number of hog farmers operating under production contracts and the extent to which "ledger" contracts were employed in the industry. Under a ledger contract, the producer is protected from cash prices that fall below a negotiated floor price, but must pay back the money to the packer / buyer when prices rise above the floor price. This arrangement could cause a sizeable potential liability to build up for producers during periods of extremely low hog prices. To provide insight into this situation, the latest survey asked about these topics. First, the respondents indicated that, on average, about 23 percent of the hog operations they finance operate under some sort of production contract. The share was largest in Iowa (30 percent) and lowest in Wisconsin (15 percent). Second, a much smaller share, about 7 percent, of the hog operations financed by our survey respondents operate using ledger contracts.

Bankers also reported that the share of their agricultural loan portfolios devoted to financing livestock operations has declined over the past ten years, and has been replaced by a greater emphasis on financing grain operations. On average, just under two-thirds of the farm loan portfolio is used to finance operations where grain is the primary enterprise, compared with a share of almost 50 percent ten years ago. In comparison, the average share of District agricultural loan portfolios devoted to financing operations where livestock is the primary enterprise slipped from 46 percent to about one-third over the past ten years.

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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)*	January	98	–1.0	–5	–8
Crops *(index, 1990–92=100)*	January	98	–2.0	–11	–15
Corn *($ per bu.)*	January	2.01	0.0	–21	–25
Hay *($ per ton)*	January	78.80	0.5	–17	–20
Soybeans *($ per bu.)*	January	5.22	–2.8	–22	–27
Wheat *($ per bu.)*	January	2.86	–0.3	–14	–29
Livestock and products *(index, 1990–92=100)*	January	96	–1.0	2	–2
Barrows and gilts *($ per cwt.)*	January	26.10	76.4	–28	–52
Steers and heifers *($ per cwt.)*	January	62.40	3.5	–6	–4
Milk *($ per cwt.)*	January	17.70	–1.7	20	31
Eggs *(¢ per doz.)*	January	71.9	–5.1	–3	–6
Consumer prices *(index, 1982–84=100)*	December	164	–0.1	2	3
Food	December	162	0.1	2	4
Production or stocks					
Corn stocks *(mil. bu.)*	December 1	8,050	N.A.	11	17
Soybean stocks *(mil. bu.)*	December 1	2,187	N.A.	9	20
Wheat stocks *(mil. bu.)*	December 1	1,892	N.A.	17	55
Beef production *(bil. lb.)*	December	2.10	4.8	4	8
Pork production *(bil. lb.)*	December	1.80	6.9	10	26
Milk production* *(bil. lb.)*	December	11.4	5.2	3	4
Receipts from farm marketings *(mil. dol.)*	September	18,659	11.9	–12	–12
Crops**	September	8,934	25.6	–9	–15
Livestock	September	7,806	–0.2	–8	–3
Government payments	September	1,919	6.3	–35	–29
Agricultural exports *(mil. dol.)*	November	4,671	–3.9	–15	–21
Corn *(mil. bu.)*	November	168	6.8	39	–31
Soybeans *(mil. bu.)*	October	135	386.1	–20	41
Wheat *(mil. bu.)*	October	113	21.0	23	12
Farm machinery sales *(units)*					
Tractors, over 40 HP	December	5,239	2.5	–16	2
40 to 100 HP	December	3,559	–3.1	9	13
100 HP or more	December	1,680	16.7	–44	–15
Combines	December	858	–48.4	–34	–32

N.A. Not applicable

*20 selected states.

**Includes net CCC loans.

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