The Agricultural Newsletter
from the Federal Reserve Bank of Chicago
Number 1932 May 2006

AgLetter

FARMLAND VALUES AND CREDIT CONDITIONS

Summary

An April 1, 2006 survey of 237 bankers in the Seventh Federal Reserve District showed that increases in agricultural land values were diverging within the District. On average, District farmland values slowed to 9 percent growth from the previous year, but double-digit increases in Michigan and Wisconsin outpaced the rest of the District. The value of "good" agricultural land increased 3 percent for the first quarter of 2006, with the two northern states also exceeding the District average. With about 20 percent more of the bankers expecting increases versus decreases in farmland values from April through June, growth should continue, though more slowly in Illinois and Iowa. Almost half of the respondents replied that the demand to purchase farmland was higher over the winter than a year ago, although the share purchased by farmers had declined even as the amount of farmland on the market and sold had risen. Cash rental rates for farmland rose the most in the southern states of the District, resulting in a 3 percent climb overall.

As interest rates continued to march upward, credit conditions slid in the first quarter of 2006 relative to the previous year. Repayment rates dipped for non-real-estate loans, and renewals or extensions of loans picked up in that quarter compared to a year earlier. Yet, there was a jump in the demand for loans and a slight increase in the availability of funds. About 10 percent of the banks continued to tighten collateral requirements, as in recent quarters.

CONFERENCE ANNOUNCEMENT

Globally Competitive Agriculture and the Midwest

In late September 2006, the Federal Reserve Bank of Chicago and the Chicago Council on Foreign Relations will hold a joint conference on the linkages between global competition in agriculture and the Midwest. Please check the conference website at **www.chicagofed.org** under "Upcoming Events" for more information and the forthcoming agenda.

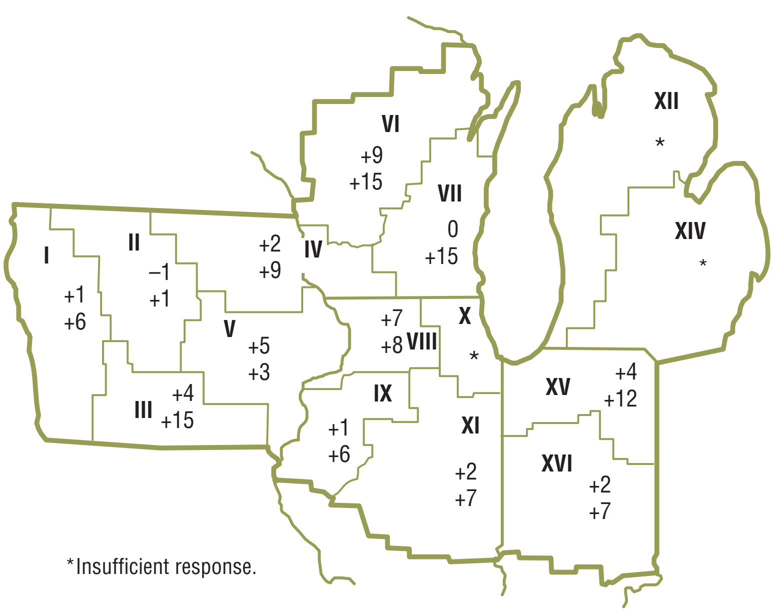
Farmland values

With slower growth in Illinois and Iowa outweighing faster growth in Michigan and Wisconsin, the average year-over-year increase in the value of "good" agricultural land for the District eased to 9 percent as of the first quarter of 2006 (see map and table below). Illinois and Iowa showed slower gains of 7 percent and 6 percent, respectively, and Indiana held steady with a 9 percent gain, while Michigan and Wisconsin had increases in the teens for farmland values. The changes in farmland values for the first quarter of 2006 followed similar patterns, though the District average increased to 3 percent. The most likely explanation

Percent change in dollar value of "good" farmland

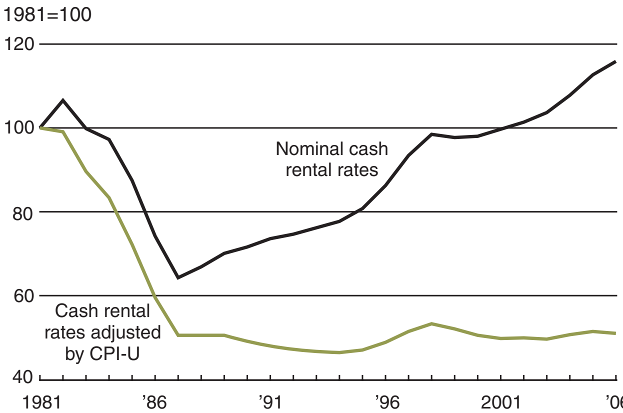
Top: January 1, 2006 to April 1, 2006
Bottom: April 1, 2005 to April 1, 2006

	January 1, 2006 to April 1, 2006	April 1, 2005 to April 1, 2006
Illinois	+2	+7
Indiana	+3	+9
Iowa	+2	+6
Michigan	*	*
Wisconsin	+5	+15
Seventh District	+3	+9



*Insufficient response.

1. Indexes of District cash rental rates



Note: Derived from Federal Reserve Bank of Chicago farmland value surveys and BLS Consumer Price Index series.

for the divergence of growth rates could relate to the different mixes of farming among District states. Michigan and Wisconsin had the most diverse agricultural sectors in the District, relying less on traditional corn and soybean operations. Also, improved weather in 2005 boosted the output of corn and soybeans in Michigan (6 percent for both) and Wisconsin (11 percent and 12 percent, respectively), whereas the rest of the District faced output reductions (except for Iowa soybeans). Moreover, the larger role of recreational buyers might have intensified competition for land in Michigan and Wisconsin. Wisconsin housing markets also have maintained more of their strength, keeping pressure on agricultural land from developers.

In addition, the amount of farmland for sale barely increased in Michigan and Wisconsin, whereas at least a third of the respondents indicated the amount was higher in the other District states. Overall, reports of more farmland up for sale (37 percent) outnumbered those of less farmland up for sale (17 percent). Moreover, between 35 percent and 40 percent of the bankers responded that the number and acreage of farms sold was higher than the same period a year ago, whereas 17 percent reported lower activity. With about half of Illinois respondents reporting a higher number of farms sold, Illinois led the District in farm real estate activity for another year.

The percentage of respondents that reported higher demand to purchase agricultural land than the first quarter of 2005 fell to 48 percent, with 11 percent reporting lower demand. In Illinois, Indiana, and Wisconsin, at least half of the bankers replied that demand for farmland was higher, with less than 10 percent noting lower demand. In Iowa and Michigan, the majority had not seen higher demand for farmland, though less than a quarter had seen lower demand. Also, the surveys indicated that farmers purchased an even lower share of the acreage sold compared to a year ago (9 percent reported a higher share versus 44 percent lower). Once again this phenomenon was most apparent in Illinois, with 61 percent responding that farmers bought a smaller share of the acres sold.

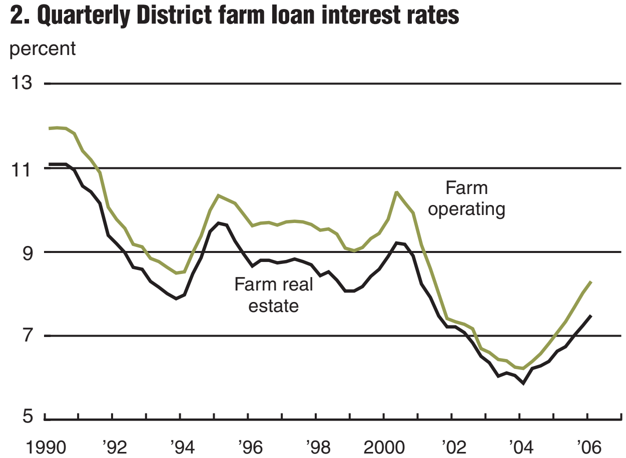
Slightly fewer bankers than last quarter expected farmland values to increase (27 percent), while 5 percent expected farmland values to go down during April to June. Over 40 percent of the respondents anticipated increases in Indiana and Michigan, with Wisconsin next closest at 30 percent. In Illinois and Iowa, less than a quarter of the bankers predicted higher farmland values, though only 5 percent foresaw farmland values going lower.

For farmland operated by someone other than the owner in the District, 79 percent was reported as cash rented and 19 percent as crop-shared, the same breakdown as a year ago. Cash rental rates were up 3 percent from 2005. The annual increases in cash rental rates for Illinois, Indiana, and Iowa kept pace with the District, but those in Michigan and Wisconsin trailed. The "real" cash rental rate for the District fell 0.8 percent from a year ago, adjusting for inflation using the Consumer Price Index. Even as nominal cash rental rates have increased above the levels of the early 1980s, the index of cash rental rates adjusted for inflation has barely managed to stay level after dropping in half in the 1980s (see chart 1).

Credit conditions

Credit conditions faltered in the first quarter of 2006, as higher input costs compounded the effects of lower agricultural prices for many District products. The responses showed that non-real-estate farm loan repayment rates were lower than those of the first quarter in 2005. With only 8 percent of the bankers indicating higher rates of loan repayment and 22 percent lower rates, the index of loan repayments dropped to 87, matching the lowest value of the past two and a half years. In addition, there were more loan renewals and extensions, with 23 percent of the respondents reporting increases and 11 percent decreases. The banks

2. Quarterly 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[1]	Feeder cattle[1]	Real estate[1]
	(index)[2]	*(index)*[2]	*(index)*[2]	*(percent)*	*(percent)*	*(percent)*	*(percent)*
2003							
Jan–Mar	109	130	79	72.4	6.61	6.75	6.36
Apr–June	99	138	84	72.7	6.43	6.52	6.04
July–Sept	95	129	86	72.9	6.41	6.47	6.12
Oct–Dec	97	127	104	71.8	6.26	6.35	6.05
2004							
Jan–Mar	116	131	128	73.2	6.22	6.28	5.87
Apr–June	101	117	118	73.7	6.39	6.46	6.23
July–Sept	109	111	112	74.5	6.57	6.61	6.28
Oct–Dec	109	121	127	74.1	6.81	6.80	6.39
2005							
Jan–Mar	117	112	116	74.4	7.07	7.08	6.63
Apr–June	119	101	103	76.3	7.33	7.30	6.74
July–Sept	115	97	87	76.9	7.68	7.65	7.02
Oct–Dec	120	110	90	75.8	8.02	7.95	7.25
2006							
Jan–Mar	131	102	87	76.7	8.30	8.27	7.48

Note: Historical data on credit conditions at Seventh District agricultural banks is available for download as a spreadsheet from the *AgLetter* homepage, http://www.chicagofed.org/economic_research_and_data/ag_letter.cfm.

[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.

increased collateral requirements a bit from last year, as 13 percent required more collateral in the first three months of 2006 and only 1 percent required less.

With tighter cash flows, the index of loan demand surged to 131, the highest value in eight years, as 40 percent of the bankers reported higher demand for non-real-estate loans and 9 percent lower demand. Agricultural banks had some additional funds available to lend in response to this demand, with 18 percent of the bankers stating that more funds were available from January to March than a year before and 16 percent stating that fewer funds were available for lending, lowering the index of fund availability to 102. Loan-to-deposit ratios averaged 76.7 percent, the second highest value ever recorded in the survey, but were still below the level desired by the responding bankers (80.1 percent). Bankers indicated that the use of farm loan guarantees provided by the Farm Service Agency (FSA) of the U.S. Department of Agriculture remained close to 5 percent of the District farm loan portfolio, possibly constrained by a lack of budgeted funds.

Agricultural interest rates continued to rise at the end of the first quarter of 2006, completing a second year of upward movement (see chart 2). As of April 1, 2006, the District average for interest rates on new operating loans was 8.30 percent, over 200 basis points above the cyclical low two years ago. Interest rates for farm mortgages have risen 161 basis points in two years to an average of 7.48 percent, almost half way back to the cyclical peak of 2000.

Looking forward

Respondents expected to make more agricultural loans in the second quarter of 2006 than they did in 2005. They primarily anticipated these to be operating loans, with 54 percent of the bankers foreseeing higher operating loan volume versus 7 percent lower. Loan volumes for feeder cattle, dairy, and farm machinery were expected to decline. An almost even split of the bankers anticipated higher versus lower real estate loan volume from April to June of 2006, leaving 60 percent expecting volumes to be the same.

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AgLetter (ISSN 1080-8639) is published quarterly by the Research Department of the Federal Reserve Bank of Chicago. It is prepared by David B. Oppedahl, business economist, and members of the Bank's Research Department. The information used in the preparation of this publication is obtained from sources considered reliable, but its use does not constitute an endorsement of its accuracy or intent by the Federal Reserve Bank of Chicago.

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)*	April	115	0.9	−5	−8
Crops *(index, 1990–92=100)*	April	129	9.3	8	4
Corn *($ per bu.)*	April	2.11	2.4	5	−27
Hay *($ per ton)*	April	106.00	9.2	7	19
Soybeans *($ per bu.)*	April	5.39	−3.2	−11	−44
Wheat *($ per bu.)*	April	3.90	2.9	16	1
Livestock and products *(index, 1990–92=100)*	April	104	−5.5	−15	−17
Barrow and gilts *($ per cwt.)*	April	39.60	−8.3	−23	−17
Steers and heifers *($ per cwt.)*	April	89.7	−3.5	−9	1
Milk *($ per cwt.)*	April	12.1	−4.0	−20	−33
Eggs *(¢ per doz.)*	April	51.2	−23.6	8	−33
Consumer prices *(index, 1982–84=100)*	April	202	0.9	4	7
Food	April	194	−0.2	2	5
Production or stocks					
Corn stocks *(mil. bu.)*	March 1	6,987	N.A.	3	33
Soybean stocks *(mil. bu.)*	March 1	1,669	N.A.	21	84
Wheat stocks *(mil. bu.)*	March 1	972	N.A.	−1	−5
Beef production *(bil. lb.)*	April	1.97	−10.7	5	1
Pork production *(bil. lb.)*	April	1.61	−13.8	−5	−6
Milk production *(bil. lb.)**	April	14.2	−2.6	4	8
Agricultural exports *(mil. dol.)*	March	6,324	13.2	15	9
Corn *(mil. bu.)*	March	182	30.6	28	7
Soybeans *(mil. bu.)*	March	96	−14.1	−1	26
Wheat *(mil. bu.)*	February	73	−15.7	−2	−25
Farm machinery *(units)*					
Tractors, over 40 HP	April	10,548	20.3	−6	−4
40 to 100 HP	April	7,947	24.5	2	5
100 HP or more	April	2,601	9.0	−24	−24
Combines	April	414	−0.5	−10	−11

N.A. Not applicable
*23 selected states.
Note: *AgLetter* will no longer publish data on receipts from farm marketings. Please contact the USDA for this data.
Sources: Data from USDA, U.S. Bureau of Labor Statistics, and the Association of Equipment Manufacturers.