

AgLetter



FARMLAND VALUES AND CREDIT CONDITIONS

Summary

Though agricultural land values increased 14 percent in the third quarter of 2008 from the third quarter of 2007 in the Seventh Federal Reserve District, there was a shift in expectations toward more stable farmland values. Compared with the second quarter of 2008, the value of "good" farmland rose 2 percent, based on responses from 213 agricultural bankers to the October 1 survey. Higher demand by farmers to purchase farmland was anticipated to be offset by lower demand from nonfarm investors. Thus, the sentiment of respondents favored agricultural land values to level off in the fourth quarter of 2008.

District bankers reported that agricultural credit conditions in the third quarter had improved from a year ago, though the improvement wasn't as strong as in the second quarter of 2008. Demand for non-real-estate loans picked up in the third quarter of 2008. Funds availability was weak for District banks, while required amounts of collateral increased at more banks. District loan repayment rates were higher, and loan renewals and extensions were lower than in the third quarter of 2007. Interest rates on agricultural operating loans fell in the third quarter, while farm real estate loan rates edged up. At 78.8 percent, loan-to-deposit ratios averaged closer to desired levels than three months ago.

Farmland values

The value of "good" farmland rose 14 percent in the District from the third quarter of 2007 (see map and table below). This year-over-year increase was down slightly compared with the increases of both last quarter and a year ago. Iowa led the way with an increase of 17 percent, while Indiana trailed with an 8 percent rise in farmland values from the previous year. District agricultural land values were up 2 percent from the second quarter of 2008. The quarterly gains for District states were smaller than last quarter for Illinois, Indiana, and Iowa, while Michigan experienced a larger gain and Wisconsin's gain was unchanged.

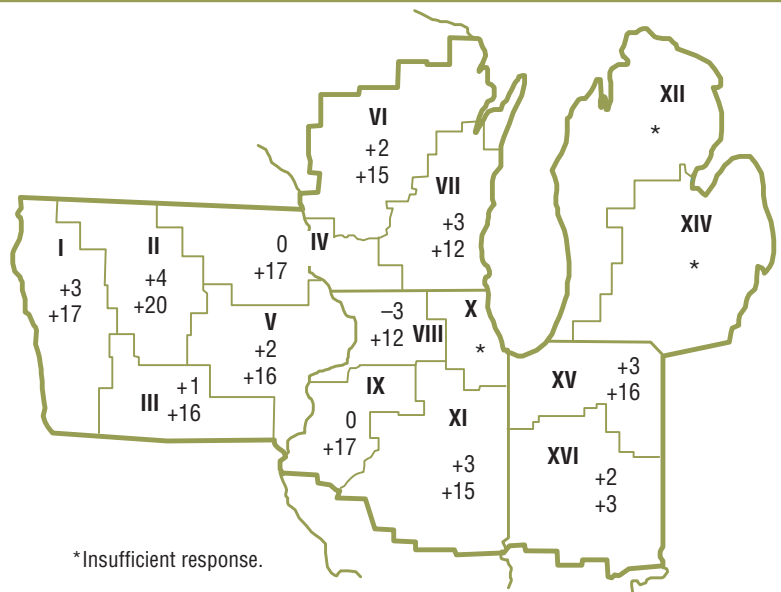
Responding bankers anticipated agricultural land values to remain stable during the fourth quarter of 2008, as the 16 percent expecting increases was offset by the 17 percent expecting decreases. With two-thirds of the respondents expecting no change, these results appeared to foretell the end of a remarkable run of double-digit growth in annual farmland values. Only in Wisconsin were there more respondents that predicted farmland values to rise rather than fall during the October through December period.

Farmers should boost demand for farmland again this fall and winter, though not as strongly as a year ago. Still, demand among nonfarm investors should ease. Responding bankers expected higher rather than lower

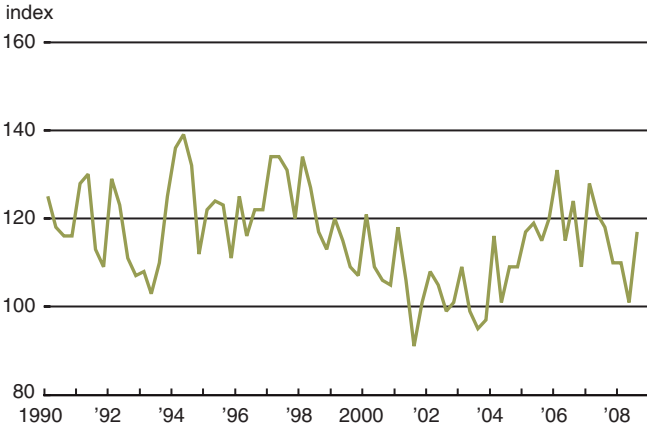
Percent change in dollar value of "good" farmland

Top: July 1, 2008 to October 1, 2008
 Bottom: October 1, 2007 to October 1, 2008

| | July 1, 2008 to October 1, 2008 | October 1, 2007 to October 1, 2008 |
|------------------|---------------------------------------|--|
| Illinois | +1 | +15 |
| Indiana | +2 | +8 |
| Iowa | +2 | +17 |
| Michigan | +5 | +13 |
| Wisconsin | +1 | +15 |
| Seventh District | +2 | +14 |



1. Demand for non-real-estate farm loans



interest by farmers in acquiring agricultural land (37 percent versus 16 percent). Almost half of the Illinois bankers predicted higher demand among farmers; only 10 percent predicted lower demand. With 25 percent of the respondents predicting higher demand for farmland among nonfarm investors and 37 percent lower demand over the next three to six months, upward pressure on farmland values from funding sources outside of agriculture will likely diminish. Iowa, Michigan, and Wisconsin bankers were primarily responsible for this result, as Illinois and Indiana bankers foresaw no change in demand from nonfarm investors.

Higher net cash earnings for crop farms could boost demand for farmland, but lower net cash earnings for livestock operations would limit demand. As corn and soybean prices peaked during the summer, the effects on net farm income diverged as livestock operations struggled with surging feed costs. For crop farms, 62 percent of respondents predicted increases in net cash farm earnings, versus 25 percent decreases, over the next three to six months compared with earnings a year earlier. However, respondents foresaw drops in net farm earnings for dairy farmers (9 percent up and 41 percent down) and for cattle and hog farmers (8 percent up and 67 percent down).

U.S. soybean production was forecasted to rise 9 percent from 2007 to 2.92 billion bushels; U.S. corn production was forecasted to dip 8 percent to 12.0 billion bushels—still the second largest harvest after the 2007 one (estimates from the U.S. Department of Agriculture). As the growth in ethanol production slowed, it was still projected that almost a billion more bushels of corn would be converted into ethanol in the 2008–09 crop year (4.0 billion) than in the previous year. However, projected declines in livestock feeding and exports reduced total corn usage from 12.8 billion bushels to 12.5 billion bushels for the 2008–09 crop year, putting downward pressure on corn prices this

fall. Similarly, soybean prices have dropped with exports projected to be slightly smaller in the 2008–09 crop year and total usage dipping to 2.93 billion bushels. With agricultural exports down in volume and value, District net farm income will likely suffer, especially since the strengthened value of the U.S. dollar raised the relative prices of U.S. exports.

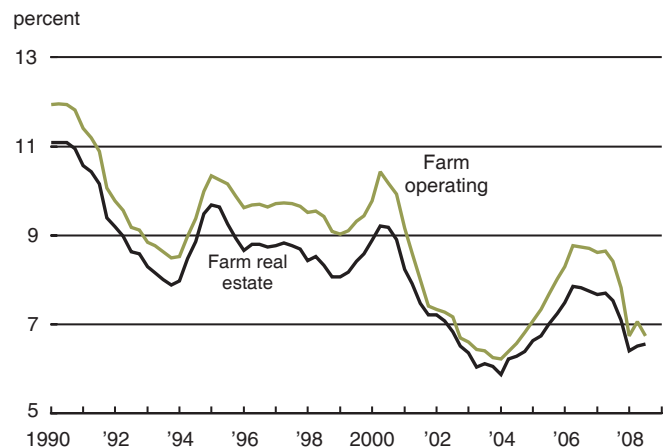
Twenty percent more of the respondents anticipated higher rather than lower volumes of farmland transfers from the previous fall and winter, though 44 percent foresaw unchanged volumes. So, farmland sales should outpace those of a year ago, but the increase will likely be smaller. Illinois and Iowa could see the largest rises in farmland transfer activity in the District.

Credit conditions

Credit conditions continued to improve in the third quarter of 2008, though not by as much as in the second quarter. Demand for non-real-estate loans has grown for nearly five years in a row at surveyed banks. With 36 percent of the bankers reporting higher demand for non-real-estate loans from a year earlier and 19 percent reporting a decline in demand, the index of loan demand was 117 (see table on the next page). Since 1988, there have been only five quarters in which the index indicated loan demand was down (see chart 1). Only in Wisconsin did more bankers report non-real-estate loan demand was down rather than up.

The growth in funds availability slowed during the July through September period. With 16 percent of the bankers reporting they had more funds available during the third quarter of 2008 than they had a year earlier and 13 percent reporting they had less, the index of funds availability was 103. Available funds dipped in Indiana, Michigan, and Wisconsin. Collateral requirements at District banks have progressively tightened this year. Almost a quarter required higher amounts of collateral than a year earlier.

2. Quarterly District farm loan interest rates



Credit conditions at Seventh District agricultural banks

| | Loan demand (index) ^b | Funds availability (index) ^b | Loan repayment rates (index) ^b | Average loan-to-deposit ratio (percent) | Interest rates on farm loans | | |
|-------------|-------------------------------------|--|--|--|---|---|---------------------------------------|
| | | | | | Operating loans ^a (percent) | Feeder cattle ^a (percent) | Real estate ^a (percent) |
| 2006 | | | | | | | |
| Jan-Mar | 131 | 102 | 87 | 76.7 | 8.30 | 8.27 | 7.48 |
| Apr-June | 115 | 101 | 85 | 78.0 | 8.76 | 8.66 | 7.85 |
| July-Sept | 124 | 95 | 87 | 79.1 | 8.73 | 8.70 | 7.82 |
| Oct-Dec | 109 | 116 | 130 | 76.6 | 8.71 | 8.70 | 7.74 |
| 2007 | | | | | | | |
| Jan-Mar | 128 | 113 | 131 | 78.4 | 8.61 | 8.60 | 7.67 |
| Apr-June | 121 | 115 | 117 | 77.8 | 8.65 | 8.63 | 7.70 |
| July-Sept | 118 | 118 | 122 | 78.1 | 8.42 | 8.40 | 7.53 |
| Oct-Dec | 110 | 126 | 149 | 77.2 | 7.82 | 7.89 | 7.09 |
| 2008 | | | | | | | |
| Jan-Mar | 110 | 129 | 147 | 75.9 | 6.74 | 6.86 | 6.41 |
| Apr-June | 101 | 124 | 137 | 75.2 | 7.06 | 6.77 | 6.51 |
| July-Sept | 117 | 103 | 115 | 78.8 | 6.74 | 6.85 | 6.56 |

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

^aAt end of period.

^bBankers 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.

Non-real-estate farm loan repayment rates were higher than in the third quarter of 2007. With 24 percent of the bankers reporting higher rates of loan repayment and 9 percent reporting lower rates, the index of loan repayment rates was 115. In addition, loan renewals and extensions were down from those in July, August, and September a year ago, with 8 percent of the bankers indicating an increase and 22 percent indicating a decrease. In contrast with the rest of the District, there was a decline in loan repayment rates for Wisconsin, and there were higher levels of renewals and extensions in Indiana.

Interest rates on agricultural operating loans matched the low seen in the first quarter of 2008 (see chart 2 and table above), but other farm loan rates edged higher. As of October 1, the District average for interest rates on new operating loans decreased to 6.74 percent. Interest rates on operating loans ranged from 6.20 percent in Indiana to 7.22 percent in Wisconsin. Interest rates for farm real estate loans rose to 6.56 percent, on average. Illinois had the lowest rate for farm mortgages, 6.50 percent, and Wisconsin had the highest rate, 6.79 percent.

Looking forward

Agricultural credit conditions were predicted to continue to improve during the fall and winter, based on the responses from the bankers. More bankers (33 percent) expected the volume of farm loan repayments to rise over the next three to six months compared with a year ago than decline (13 percent), except in Wisconsin. In addition, 20 percent of the respondents anticipated a decrease, versus 10 percent an increase, in forced sales or liquidation of farm assets among financially stressed farmers this fall and winter. Once again, Wisconsin bankers broke from

the rest, with 36 percent forecasting more forced sales or liquidations and 12 percent fewer.

For the fourth quarter of 2008, 45 percent of the bankers expected higher non-real-estate loan volume and 18 percent expected lower volume than in 2007. Respondents predicted increases in operating loans (49 percent more forecasted increases rather than decreases), farm machinery loans (15 percent), grain storage construction loans (7 percent), and Farm Service Agency (FSA) guaranteed loans (11 percent). Livestock loans were seen as declining. More bankers forecasted higher (24 percent) rather than lower (10 percent) real estate loan volume during the October through December period. In Wisconsin, only volumes for operating and FSA guaranteed loans were anticipated to expand in the fourth quarter of 2008.

David B. Oppedahl, *business economist*

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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 (<i>index, 1990–92=100</i>) | October | 145 | -5.8 | 3 | 26 |
| Crops (<i>index, 1990–92=100</i>) | October | 157 | -9.8 | 5 | 38 |
| Corn (\$ per bu.) | October | 3.99 | -20.5 | 21 | 56 |
| Hay (\$ per ton) | October | 157.00 | -2.5 | 23 | 44 |
| Soybeans (\$ per bu.) | October | 8.66 | -19.1 | 4 | 57 |
| Wheat (\$ per bu.) | October | 5.79 | -22.1 | -24 | 26 |
| Livestock and products (<i>index, 1990–92=100</i>) | October | 128 | -3.8 | -2 | 10 |
| Barrow and gilts (\$ per cwt.) | October | 50.80 | -3.8 | 18 | 8 |
| Steers and heifers (\$ per cwt.) | October | 93.8 | -5.5 | -3 | 0 |
| Milk (\$ per cwt.) | October | 17.6 | -3.3 | -18 | 29 |
| Eggs (¢ per doz.) | October | 1.020 | 2.2 | 9 | 89 |
| Consumer prices (<i>index, 1982–84=100</i>) | September | 219 | 0.0 | 5 | 8 |
| Food | September | 218 | 0.6 | 6 | 11 |
| Production or stocks | | | | | |
| Corn stocks (<i>mil. bu.</i>) | September 1 | 1,624 | N.A. | 25 | -17 |
| Soybean stocks (<i>mil. bu.</i>) | September 1 | 205 | N.A. | -64 | -54 |
| Wheat stocks (<i>mil. bu.</i>) | September 1 | 1,857 | N.A. | 8 | 6 |
| Beef production (<i>bil. lb.</i>) | September | 2.27 | 0.0 | 8 | 5 |
| Pork production (<i>bil. lb.</i>) | September | 1.97 | 9.4 | 13 | 13 |
| Milk production (<i>bil. lb.</i>)* | October | 14.4 | 2.9 | 2 | 6 |
| Agricultural exports (<i>mil. dol.</i>) | September | 9,118 | -5.9 | 16 | 70 |
| Corn (<i>mil. bu.</i>) | August | 180 | 14.7 | -3 | -20 |
| Soybeans (<i>mil. bu.</i>) | August | 44 | 12.8 | -11 | -14 |
| Wheat (<i>mil. bu.</i>) | August | 144 | 18.2 | -7 | 79 |
| Farm machinery (<i>units</i>) | | | | | |
| Tractors, over 40 HP | October | 9,987 | 13.0 | -4 | 4 |
| 40 to 100 HP | October | 6,199 | 6.4 | -12 | -12 |
| 100 HP or more | October | 3,788 | 25.6 | 15 | 51 |
| Combines | October | 984 | -33.6 | 46 | 55 |

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.