*The Agricultural Newsletter*
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# AgLetter

## FARMLAND VALUES AND CREDIT CONDITIONS

### Summary

Persistently strong nonfarm demand and historically low interest rates, along with a relatively small expansion in the amount of available farmland for sale, led to a 12 percent increase in the value of "good" agricultural land over the past year in the Seventh Federal Reserve District. In addition, higher prices in the first quarter of 2004 for corn, soybeans, milk, and pork contributed to the most favorable market conditions in recent years for the District agricultural sector. Based on a survey of 288 agricultural bankers as of April 1, 2004, the quarterly jump in farmland values was 5 percent, on average, for the entire District. Two-thirds of the respondents expected farmland values to rise in the next three months, even after the recent substantial increases. Pressured by farmland value increases, cash rental rates for farmland were up 4 percent from a year ago. A sustained movement toward cash rental arrangements in the District continued, while crop-share arrangements gave ground.

Credit conditions improved again this quarter, as higher prices for key agricultural products paved the road for gains in loan demand and loan repayment rates. With the continued availability of funds above year-ago levels, a slightly smaller percentage of banks increased collateral requirements. Renewals and extensions of loans were down from a year earlier in the first quarter, according to the bankers. Building on the stronger loan demand of the previous quarter, the respondents anticipated higher loan volumes in the second quarter than a year ago. As of April 1, 2004, interest rates on agricultural loans dropped once again. Farm real estate loan rates fell below the low established last year. Loan-to-deposit ratios were the highest in over a year, averaging 73.2 percent.

### Farmland values

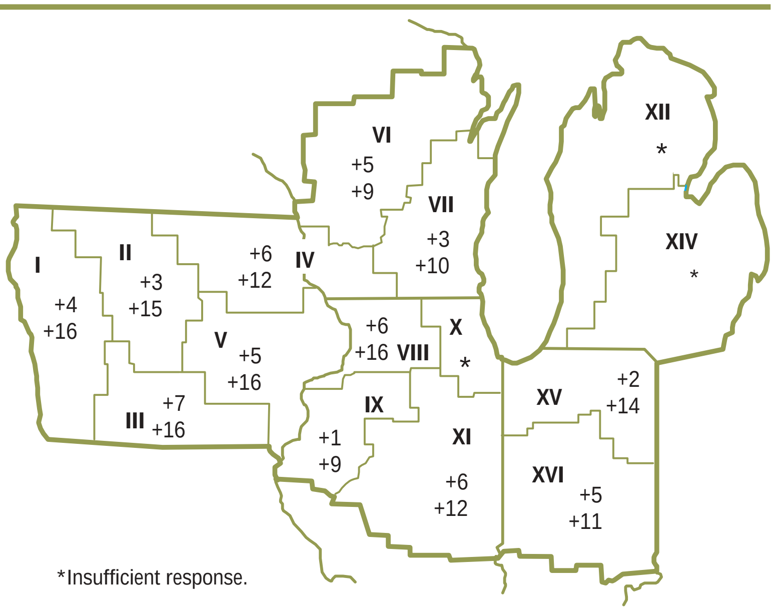
The value of "good" agricultural land rose again in the first quarter of 2004, as the survey indicated that results were similar among District states (see map and table below). From January 1 to April 1, the rate of change in farmland values for Illinois and Iowa paced the District at 5 percent, while the other District states had 4 percent increases. The average year-over-year increase in District farmland values was 12 percent, an acceleration from the end of 2003. Michigan, at one end of the range, recorded an 8 percent gain, while Iowa at the other end reported a 15 percent gain. With the dramatic increase in milk prices in 2004, Wisconsin farmland values rose at nearly the same pace as the District average, even as dairy operations continued to recover from low milk prices last year.

Spurred in part by agricultural price increases, higher demand for the purchase of agricultural land than a year

**Percent change in dollar value of "good" farmland**

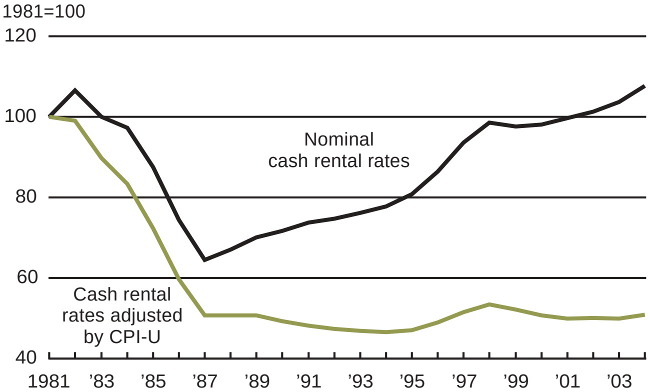
*Top:* January 1, 2004 to April 1, 2004
*Bottom:* April 1, 2003 to April 1, 2004

| | January 1, 2004 to April 1, 2004 | April 1, 2003 to April 1, 2004 |
|---|---|---|
| Illinois | +5 | +12 |
| Indiana | +4 | +12 |
| Iowa | +5 | +15 |
| Michigan | +4 | +8 |
| Wisconsin | +4 | +9 |
| Seventh District | +5 | +12 |




*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.

ago was reported by 80 percent of the respondents. In the three primary corn and soybean producing states (Illinois, Indiana, and Iowa) over 80 percent indicated they saw higher demand to purchase farmland, with one percent or less seeing lower demand. In Wisconsin, reversing the situation of last year, 63 percent of the reporting bankers saw greater interest in the purchase of agricultural land, whereas only 5 percent saw lower demand.

Along with heightened demand, the limited amount of farmland on the market contributed to the large increase in land values. Though 29 percent of the respondents reported an increase in the amount of farmland for sale in their areas, 20 percent reported a decrease. But, 36 percent of the bankers indicated that the number of farms sold was above the level of the year before, compared to 15 percent below. Similar numbers were reported for acres sold, indicating that the higher prices led to more farmland transfers. Following the trend of recent years, farmers purchased a smaller share of the acreage sold in all District states. About 10 percent of the bankers reported the share of acreage purchased by farmers was higher than the previous year, and 44 percent reported it was lower.

Even with the large movements in farmland values, 67 percent of respondents expected further increases during the April to July quarter, though a third expected farmland values to stay the same. Only in Michigan was the percentage of bankers that expected increases below half. The percentage of bankers in the other states that predicted higher farmland values ranged from 57 percent in Indiana to 77 percent in Iowa.

Another impact of higher commodity prices was a 4 percent annual increase in the average cash rental rate for "good" farmland in the District. Higher property taxes in some parts of the District also helped push up cash rents. The increase was double last year's 2 percent gain. Indiana and Wisconsin trailed the other states with increases of 3 percent and 2 percent, respectively. The inflation-adjusted cash rental rate for 2004 was 2 percent, the first strong increase since 1998 (see chart 1).

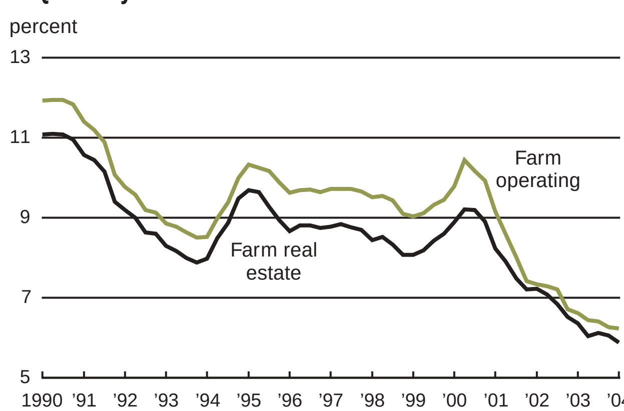
Crop-share arrangements were down to a fifth of rental arrangements for farmland operated by someone other than the owner, whereas cash rental agreements were up to three-fourths in the District. Illinois continued to gradually shift toward more cash rentals (60 percent) and away from crop-shares (37 percent). Indiana, Iowa, and Michigan were approximately 80 percent cash rentals and 20 percent crop-shares. With the highest concentration in one arrangement, Wisconsin had 93 percent cash rentals and 5 percent crop-shares. Other types of arrangements were no more than 3 percent in all District states.

## Credit conditions

Credit conditions improved once again in the District this quarter. Bankers reported that non-real estate farm loan repayment rates were better than the previous year for even more banks than in the last quarter of 2003. About 38 percent of the respondents noted higher rates of loan repayment, while only 10 percent noted lower rates. These numbers raised the index of loan repayments to 128, the highest in over a decade. In addition, there was a drop in renewals and extensions, with 28 percent of the bankers indicating a decrease, and only 7 percent indicating an increase. About 30 percent of lenders in Illinois and 40 percent in Iowa noted fewer renewals and extensions.

Another positive sign in the first quarter of 2004 was an increase in demand for non-real estate agricultural loans. With 31 percent of the bankers reporting higher demand for non-real estate loans, compared with 16 reporting lower demand, the index of loan demand jumped to 116, the highest in two years. Around 36 percent of the bankers reported they had more funds available from January to March than they had a year earlier. Accompanying this increase, only 5 percent of banks reported a lower amount of funds available for lending. The index of fund availability was 131, up slightly from last quarter and near the highest in a decade.

2. Quarterly District farm loan interest rates



### 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) |
| **2001** | | | | | | | |
| Jan-Mar | 118 | 101 | 67 | 75.0 | 9.16 | 9.17 | 8.23 |
| Apr-June | 106 | 109 | 73 | 75.1 | 8.60 | 8.58 | 7.91 |
| July-Sept | 91 | 127 | 86 | 74.9 | 8.01 | 8.07 | 7.47 |
| Oct-Dec | 101 | 129 | 75 | 72.8 | 7.41 | 7.51 | 7.21 |
| **2002** | | | | | | | |
| Jan-Mar | 108 | 118 | 66 | 72.7 | 7.33 | 7.48 | 7.22 |
| Apr-June | 105 | 120 | 71 | 75.1 | 7.28 | 7.35 | 7.08 |
| July-Sept | 99 | 124 | 76 | 75.7 | 7.21 | 7.26 | 6.84 |
| Oct-Dec | 101 | 130 | 88 | 73.2 | 6.70 | 6.78 | 6.51 |
| **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 |

[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.

With signs of improvements in agricultural loans, bankers reported a smaller tightening in collateral requirements from last quarter, with just 9 percent requiring a higher level of collateral in the past three months, as opposed to one percent lowering. Over 10 percent of banks in Illinois, Michigan, and Wisconsin required greater amounts of collateral.

Contributing to the increase in farmland values, banks reported that farm loan interest rates had declined again (see chart 2). As of April 1, the District average for interest rates on new operating loans was down to 6.22 percent, 421 basis points below the peak of 2000. And, at an average of 5.87 percent, interest rates for farm mortgages fell 334 basis points from their last peak in 2000.

The surveyed bankers were asked about their use of farm loan guarantees provided by the Farm Service Agency (FSA) of the U.S. Department of Agriculture. About 6 percent of the District farm loan portfolio is covered by FSA guarantees, a slight decrease from last year. The range of FSA guarantees as a percent of farm loans was from 5 percent in Indiana to 8 percent in Wisconsin.

### Looking forward

In comparison with the second quarter of last year, 31 percent of the bankers reported that they foresee higher non-real estate loan volume in the second quarter of 2004, primarily in operating loans and farm machinery loans, and 35 percent foresee higher real estate loan volume. Most respondents indicated that they expected loan volumes would remain the same in the second quarter of this year compared with a year ago. Anticipated loan volumes in the second quarter of 2004 were somewhat above the results from recent surveys, as fewer bankers foresaw lower loan volumes. Also, more bankers expected a decline in the use of FSA guaranteed loans.

Given the various pressures on farm income in recent years, such as low agricultural prices and the loss of off-farm income, two quarters of remarkable improvements in credit conditions have not erased all concerns. Farmers lacking financial capital or struggling to adapt to structural shifts in the agricultural economy still need to make some difficult decisions about the future of their operations, though the current climate may buy them some additional time.

David B. Oppedahl, *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** (*index, 1990-92=100*) | April | 124 | 2.5 | 23 | 32 |
| **Crops** (*index, 1990-92=100*) | April | 122 | 1.7 | 11 | 22 |
| Corn (*$ per bu.*) | April | 2.87 | 4.4 | 23 | 50 |
| Hay (*$ per ton*) | April | 89.60 | 9.5 | –4 | –9 |
| Soybeans (*$ per bu.*) | April | 9.54 | 2.9 | 64 | 113 |
| Wheat (*$ per bu.*) | April | 3.82 | –0.5 | 13 | 35 |
| **Livestock and products** (*index, 1990-92=100*) | April | 125 | 3.3 | 34 | 40 |
| Barrow and gilts (*$ per cwt.*) | April | 45.40 | –4.4 | 29 | 42 |
| Steers and heifers (*$ per cwt.*) | April | 89.70 | 2.0 | 14 | 27 |
| Milk (*$ per cwt.*) | April | 18.0 | 16.9 | 64 | 44 |
| Eggs (*¢ per doz.*) | April | 76.9 | –30.1 | 12 | 48 |
| **Consumer prices** (*index, 1982-84=100*) | April | 188 | 0.3 | 2 | 5 |
| Food | April | 185 | 0.1 | 3 | 5 |
| **Production or stocks** | | | | | |
| Corn stocks (*mil. bu.*) | March 1 | 5,271 | N.A. | 3 | –9 |
| Soybean stocks (*mil. bu.*) | March 1 | 906 | N.A. | –25 | –32 |
| Wheat stocks (*mil. bu.*) | March 1 | 1,019 | N.A. | 12 | –16 |
| Beef production (*bil. lb.*) | April | 1.96 | –7.1 | –9 | –11 |
| Pork production (*bil. lb.*) | April | 1.73 | –4.2 | 4 | 3 |
| Milk production* (*bil. lb.*) | April | 12.6 | –1.7 | –1 | 0 |
| **Receipts from farm marketings** (*mil. dol.*) | February | 15,323 | –18.9 | 16 | 21 |
| Crops** | February | 7,116 | –30.2 | 18 | 26 |
| Livestock | February | 8,207 | –5.8 | 15 | 18 |
| **Agricultural exports** (*mil. dol.*) | March | 5,809 | 11.0 | 20 | 31 |
| Corn (*mil. bu.*) | March | 175 | 20.4 | 30 | –1 |
| Soybeans (*mil. bu.*) | March | 77 | –10.5 | –16 | 20 |
| Wheat (*mil. bu.*) | February | 97 | –14.3 | 94 | 42 |
| **Farm machinery** (*units*) | | | | | |
| Tractors, over 40 HP | April | 11,009 | 52.7 | 30 | 37 |
| 40 to 100 HP | April | 7,529 | 53.3 | 25 | 36 |
| 100 HP or more | April | 3,480 | 51.3 | 44 | 38 |
| Combines | April | 470 | 77.4 | 0 | 12 |

N.A. Not applicable
*20 selected states.
**Includes net CCC loans.

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