DALLASFED

AGRICULTURAL HIGHLIGHTS

Federal Reserve Bank of Dallas November 1985

Lower Interest Rates Not Likely to Save Financially Troubled Texas Farmers

The agricultural financial crisis is thought to be rooted in high interest rates, high debt levels, declining asset values, and low commodity prices. Analysis of farm financial data shows that even substantial declines in interest rates or increases in farm income probably will not save most financially troubled farms.

Who Is Hurting?

Most farmers with debt-asset ratios greater than 70 percent currently have problems both with servicing their debts and with declining net worth. Of the approximately 250,000 farms in Texas and Oklahoma, 11,000 to 14,000 have debt-asset ratios greater than 70 percent.

Texas and Oklahoma farms are divided into four categories by the amount of annual sales: small (less than $40,000 annual sales), medium ($40,000 to $100,000), large ($100,000 to $250,000), and very large (over $250,000). As the sales class gets larger (see table), the percentage of farms that are financially troubled *increases*, the percentage of total cash receipts produced by troubled farms *increases*, but the number of financially troubled farms *decreases*.

	Financially troubled farms, Texas and Oklahoma		
Size of sales class	Percent of class	Percent of overall cash receipts	Number in class
Small	3.9	0.5	8,500
Medium	4.4	0.5	1,000
Large	16.4	2.8	2,100
Very large	19.2	10.9	1,200

Source of Primary Data: U.S. Department of Agriculture.

Lower Interest Rates, Higher Incomes Not Enough

Only in the very large sales class would the *average* financially troubled farm stand much chance of returning to profitability. A rough estimate is that the *average* financially troubled very large farm would need about a four-percentage-point reduction in interest rates in order to have positive cash flow. Alternatively, if prices for farm products increased only 5 percent (holding farm input costs constant), then the *average* very large farm would have positive cash flow.

The *average* financially troubled farms in the other sales classes would not have positive cash flows even if interest rates fell to zero. Alternatively,

(Continued on back page)

Cotton Price Supports Sandbag U.S. Cotton Exports

World production of cotton has increased dramatically, but U.S. cotton exports have plummeted. Price supports have kept U.S. cotton prices from falling enough to be competitive on world markets. Though price supports make cotton farmers better off now, government stockpiling of cotton cannot substitute for export markets.

U.S. Cotton Policy Can Affect Texas Farm Income

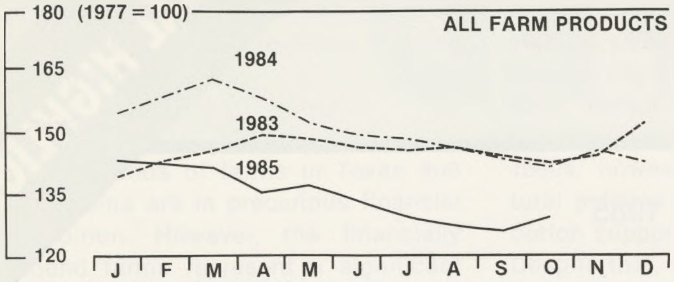
U.S. cotton agricultural policy support prices can have a large role in determining the level of U.S. cotton exports. When worldwide cotton supplies match anticipated use, U.S. cotton support prices have little effect. When cotton supplies exceed normal use, however, prices fall and support prices can come into play. Economic theory and common sense both predict that when price supports keep domestic cotton prices from falling to world market levels, competing foreign exporters will take over U.S. export markets, and domestic surpluses will build up.

Normally, 50 to 70 percent of Texas cotton is exported. Any substantial falloff in cotton exports, if not fully offset by government programs or an increase in domestic mill use, would seriously reduce farm income in Texas. With a $1 billion to $1.5 billion in cash receipts per year, cotton ranks second in the state behind cattle and calves.

(Continued on back page)

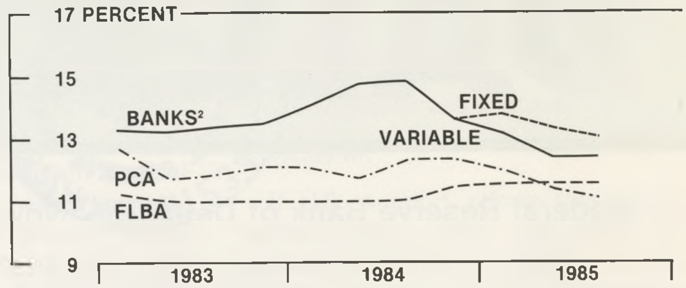
PRIME INDICATORS OF THE TEXAS AGRICULTURAL ECONOMY

INDEX OF PRICES RECEIVED: TEXAS



SOURCE: U.S. Department of Agriculture.

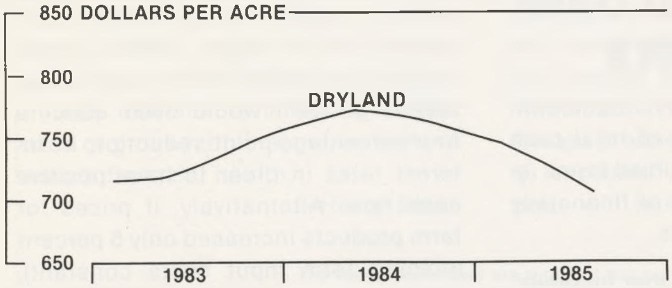
INTEREST RATES ON TEXAS FARM LOANS[1]



1. PCA: Production Credit Associations.
FLBA: Federal Land Bank Associations (Real Estate Rate).
2. Starting first quarter 1985 bank rate is decomposed into fixed and variable rates.

SOURCES: Quarterly Survey of Agricultural Credit Conditions,
Federal Reserve Bank of Dallas.
Federal Credit System.

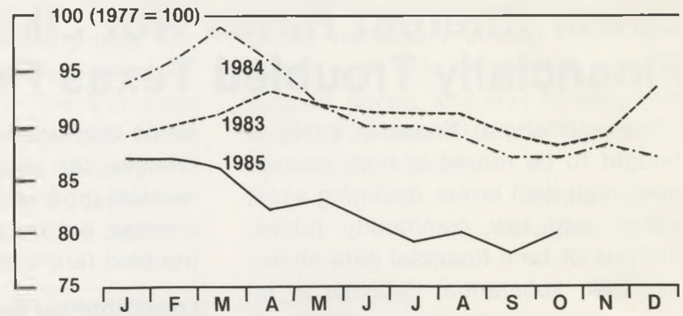
TEXAS FARM REAL ESTATE VALUES[1]



1. 3 quarter centered moving average.

SOURCE: Quarterly Survey of Agricultural Credit Conditions,
Federal Reserve Bank of Dallas.

PRICES RECEIVED/PRICES PAID[1]



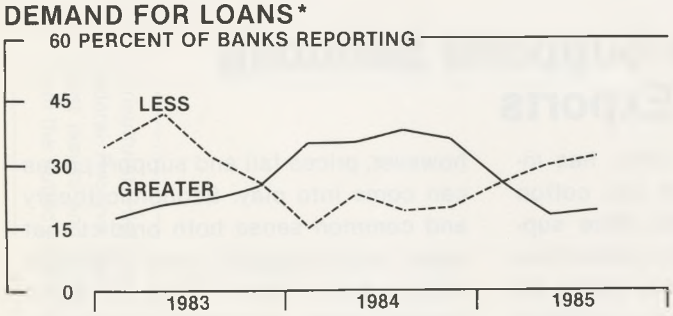
1. Prices received by farmers in Texas divided by prices paid by farmers nationwide (No separate series exists for prices paid in Texas).

SOURCES: U.S. Department of Agriculture.
Federal Reserve Bank of Dallas.

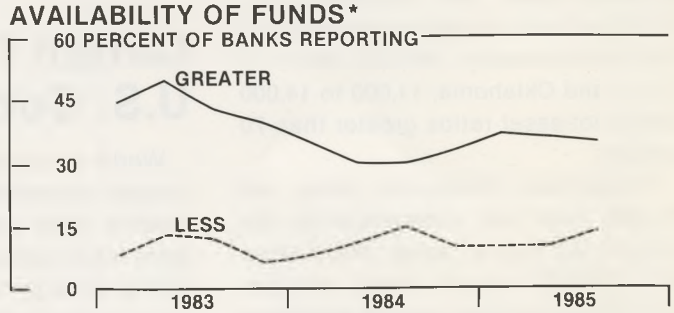
ELEVENTH DISTRICT AGRICULTURAL LOANS

Bankers report whether the variable is "greater," "the same," or "less" than a year ago.
Percent reporting "greater" or "less" are depicted below.

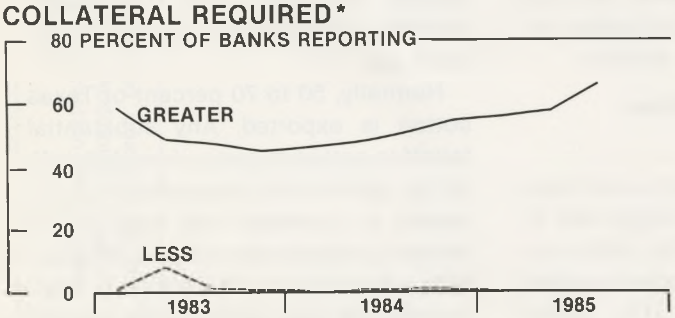
DEMAND FOR LOANS*



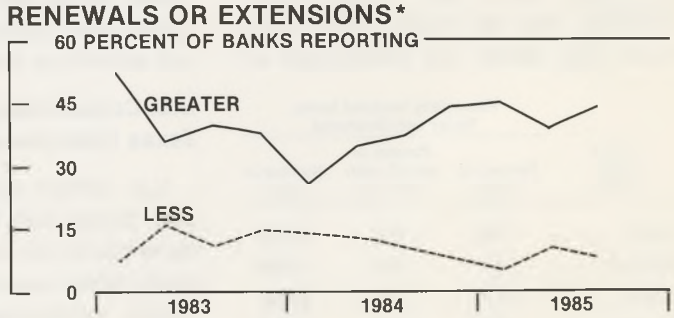
AVAILABILITY OF FUNDS*



COLLATERAL REQUIRED*



RENEWALS OR EXTENSIONS*



* SOURCE: Quarterly Survey of Agricultural Credit Conditions,
Federal Reserve Bank of Dallas.

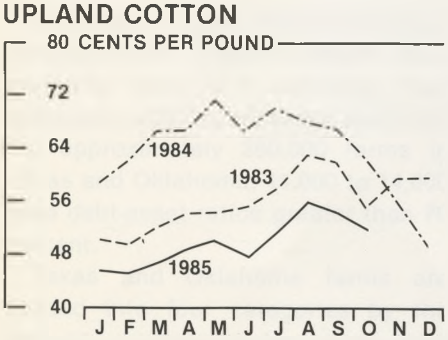
AGRICULTURAL BRIEFS

Farmer financial stress increases; land values, interest rates, and exports decline.

- Eleventh District agricultural bankers, in a recent Federal Reserve survey, now estimate that 3.7 to 5.5 percent of their agricultural borrowers will leave farming in 1985 because of financial stress. In April, their estimate was 3.5 to 4.8 percent. Surveyed bankers anticipate that they will not provide operating credit in 1986 to an average of 8.3 percent of their current farmer borrowers. These loans represent an average of 11 percent of the banks' present farm loans.
- Since summer 1984, *average* District land values have declined steadily until the second quarter of 1985 when they stabilized for a quarter. In the third quarter, however, preliminary survey estimates show ranchland dropped 1 percent to $572 per acre, dry cropland dropped 3 percent to $708 per acre, while irrigated cropland dropped almost 5 percent to $944 per acre. The contributing factors were the outlook for continued low commodity prices and less generous agricultural programs. Average land values would have fallen still more but for nonagricultural demand for land, principally in Central Texas.
- *Average* interest rates at Eleventh District agricultural banks declined during the third quarter, completing adjustment to second-quarter interest-rate declines in national credit markets. Short-term fixed-rate operating loans dropped to 13.2 percent from 13.4 percent. Those with variable-rate provisions dropped to 12.3 percent from 12.5 percent. Fixed-rate farm real estate loans dropped to 13.0 percent from 13.4 percent, but those with variable rates remained steady at 12.5 percent.
- During 1985–86, the high price support levels of U.S. agricultural policy seem to have priced U.S. agricultural exports out of the world market. The index of agricultural trade-weighted exchange rates shows the value of the dollar little changed from its level of a year ago. Although total world trade in some commodities is less this year than last, forecasts of U.S. exports have fallen more: 26 percent less wheat, 11 percent less coarse grains (corn, sorghum, and the like), and 44 percent less cotton. Of the major export crops, only soybean exports increased (13 percent).

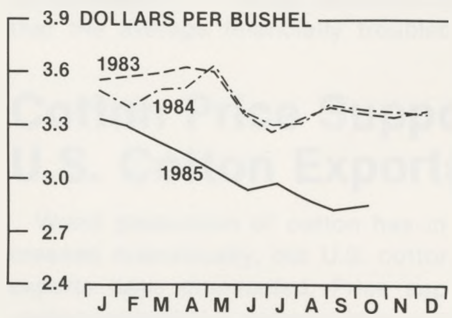
TEXAS COMMODITY MARKET PRICES

UPLAND COTTON



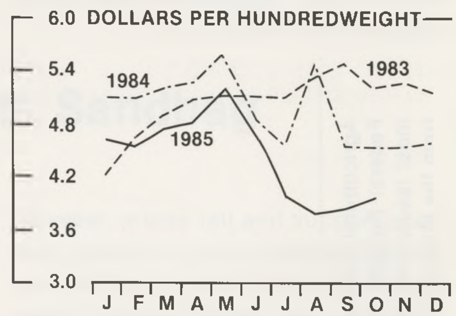
SOURCE: U.S. Department of Agriculture.

ALL WHEAT



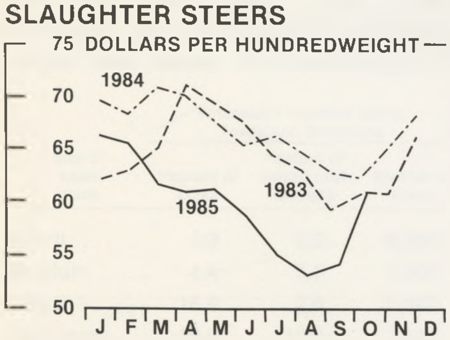
SOURCE: U.S. Department of Agriculture.

GRAIN SORGHUM



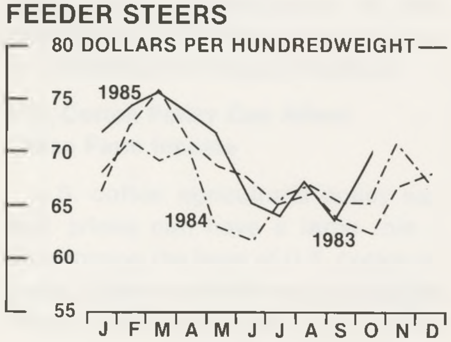
SOURCE: U.S. Department of Agriculture.

SLAUGHTER STEERS



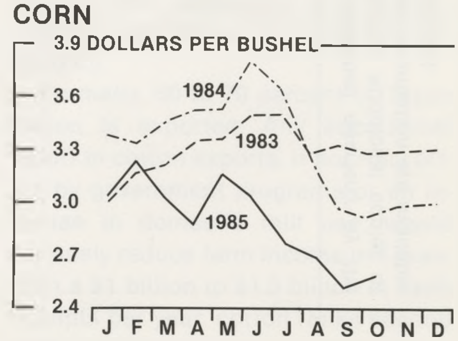
SOURCES: Texas Department of Agriculture.
Federal Reserve Bank of Dallas.

FEEDER STEERS



SOURCES: Texas Department of Agriculture.
Federal Reserve Bank of Dallas.

CORN



SOURCE: U.S. Department of Agriculture.

Interest Rates (cont.)

gross farm income would have to increase 27 to 128 percent, depending on sales class, for these farms to have positive cash flows.

Conclusion

Thousands of farms in Texas and Oklahoma are in precarious financial condition. However, the financially sound farms represent a significant part of the agriculture sector, ranging from 60 percent of farms in the largest sales class to almost 90 percent in the smallest sales category. Further, many farms with debt-asset ratios greater than 70 percent still have positive cash flow. But *average* financially troubled farms, except those in the highest sales class, would need dramatic and unlikely movements in either interest rates or gross farm income, or both, to restore financial health.

—Hilary Smith

Cotton Price (cont.)

Price Supports Bind, Exports Drop

From 1965 through 1984, U.S. cotton support prices were generally below world price levels, and cotton exports were competitive in world markets. U.S. exports steadily increased. In the 1980s, however, government agricultural policies moved away from tying cotton support prices to world prices. Despite that, the cotton support price did not really become binding until this year.

Last year, favorable weather conditions, attractive world prices, and changes in Chinese agricultural priorities have led to record world cotton production. World cotton prices fell; but largely because of support levels, U.S. cotton prices on the European market are averaging 15 percent above foreign-produced cotton. Consequently, expected 1985-86 U.S. cotton exports will fall to 3.50 million bales, a decline of 44 percent from last year. U.S. cotton surpluses are expected to double to 8.57 million bales, less than a million bales shy of this year's combined domestic use and exports.

Conclusion

If U.S. support prices stay above world levels, there are short-run benefits and long-run dangers. In the short run, U.S. cotton farmers' incomes are protected from the full decline in market prices. But in the long run, it is unlikely that government-held stocks will replace exports as an outlet for cotton. Thus, the adjustment to lower prices necessary among cotton producers will only be delayed by high support prices, and may be magnified because of the difficulty in recapturing lost export markets.

—Hilary Smith and Eric Weigel

Agricultural Highlights is published quarterly by the Federal Reserve Bank of Dallas. Additional copies of most issues and subscription information are available from the Public Affairs Department.