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Agletter



FARMLAND VALUES AND CREDIT CONDITIONS

Summary

The Chicago Fed's July survey of agricultural banks in the Seventh District indicated that, on average, farmland values increased a little over 1 percent from the end of March 2001 to the end of June. Data provided by more than 300 bankers also indicated that the year-over-year increase in the value of "good" farmland was about 5 percent. Both the quarter-to-quarter and year-over-year changes were in line with those reported in the four previous surveys. As is usually the case, the District average masked substantial variation in the reported changes across the five states (see map and table below).

Credit conditions, on balance, were similar to those reported in recent surveys. For example, the proportion of bankers reporting an increase in collateral requirements on loans was slightly lower in the July survey than at the end of the first quarter, but slightly higher than in the survey a year ago. Respondents also observed that demand for agricultural loans was down somewhat, while the availability of funds had increased. In addition, a summary measure of the "rate of loan repayment" in the second quarter of 2001 was slightly more positive than in the first quarter of 2001 or the second quarter of 2000. At the same time, a summary measure of the incidence of farmer requests for "loan renewals or extensions" increased in the most recent survey and was at its highest level since fourth quarter 1999. Interest rates on farm related loans continued to decline.

Farmland values

Farmland values in the District continued to increase, on average, through the second quarter of 2001. However, the rate of change remained diverse across the region.

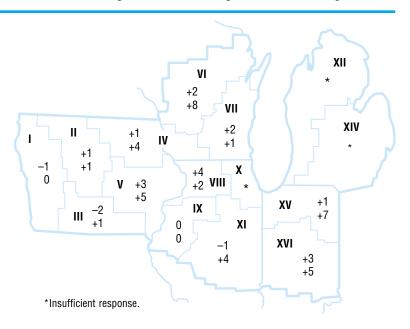
Respondents in Illinois and Iowa reported virtually no change, on average, in "good" farmland prices from the end of the first quarter to the end of the second quarter. On a year-over-year basis, they indicated prices had increased about 3 percent and 2 percent, respectively. In both states, the weakest farmland market appeared to be the western and southern areas (see map). These areas have generally shown the District's lowest gains in farmland values since mid-1998. Given the location of this relatively weaker land market, two factors might have had an impact. First, more adverse weather and crop conditions in these areas, relative to other areas of the District, negatively influenced farmderived income in recent years. Second, these areas tend to be relatively more remote from the influence of metropolitan centers where an increase in demand for non-farm development and recreational use has put upward pressure on farmland prices in recent years.

On the other end of the spectrum, the increase in farmland values in Indiana and Wisconsin was broader in the second quarter of 2001, compared with the two previous

Percent change in dollar value of "good" farmland

Top:April 1, 2001 to July 1, 2001Bottom:July 1, 2000 to July 1, 2001

	April 1, 2001 to July 1, 2001	July 1, 2000 to July 1, 2001
Illinois	0	+3
Indiana	+3	+6
lowa	0	+2
Michigan	*	*
Wisconsin	+2	+5
Seventh District	+1	+5



surveys. On a quarterly basis, as well as year-over-year, farmland values rose across these states (see map). Positive crop conditions (particularly in Indiana, the most favorable of the Seventh District states this year) and higher milk prices (benefiting Indiana corn and soybean growers and Wisconsin dairy farmers) likely contributed to the trend.

Relative agricultural conditions in the District states, and the consequent impact on farmland values, were also reflected in bankers' expectations for land prices in the third quarter of 2001. Summary measures indicated that the proportion of Indiana, Michigan, and Wisconsin bankers that expected increases in farmland values was well above the proportion that expected declines. For example, 22 percent of Wisconsin bankers expected farmland values would increase while only 6 percent thought they would decline. Indiana bankers were more closely aligned with 13 percent expecting an increase and 11 percent a decrease.

On the other hand, those bankers in Illinois and Iowa who indicated an expected change in farmland values were more likely to predict a decline in the third quarter. Eleven percent of Illinois respondents expected farmland values would decline, while 4 percent thought they would increase. Iowa bankers split with 12 percent expecting a decline and 10 percent an increase. Importantly, across the District, the proportion of bankers that thought third-quarter farmland prices would be little changed from second-quarter levels ranged from lows of 72 percent and 75 percent in Wisconsin and Michigan, respectively, to highs of 79 percent and 85 percent in Iowa and Illinois, respectively.

Credit conditions in the District

Credit conditions reported in the latest survey were similar in tone to those reported by the bankers during the past year—for the most part more positive than reported during 1999. At the same time, the bankers continued to note the importance of the federal farm program "safety net" to the financial viability of their customers and, by implication, the strength of their own balance sheets.

At the time of the July 1 survey, the U.S. Department of Agriculture's (USDA's) \$42.4 billion estimate for net farm income in 2001 indicated it would be the lowest since 1995. In mid-August Congress passed and the President signed legislation granting \$5.5 billion in supplemental farm assistance. Given the additional funding and revised expectations of higher commodity prices at the farm gate, the latest USDA estimates indicate that net farm income in 2001 will increase to about \$50.4 billion, which would be the second highest level on record (\$54.8 billion in 1996). This environment should contribute to relatively positive credit conditions for District farmers and agricultural banks through the current year.

Looking at specific measures of credit conditions as of July 1 relative to a year earlier, 23 percent of respondents indicated they had increased loan collateral requirements, compared with 26 percent who indicated they required additional collateral in the April 1 survey. There was substantial variation in this response, however, ranging from a high of 33 percent in Illinois to a low of 14 percent in Wisconsin. The relatively smaller proportion of bankers requiring increased collateral in Wisconsin represented a marked change from three months earlier, when 27 percent of Wisconsin bankers reported an increase in collateral requirements (in part this may reflect the recent sharp increase in milk prices). None of the respondents reported a reduction in collateral requirements.

Bankers were also asked to indicate their experience, relative to a year ago, with regard to the rate of loan repayment (see table on page 3) and farmers' requests for loan renewals or extensions. Based on the loan repayment index (see footnote 2 of table on page 3), the repayment rate for the District overall improved in the second quarter relative to the first quarter. However, the index, which stood at 73, also indicated that, a larger percentage of bankers reported a reduction in the rate of loan repayment than those who saw an increase. This pattern, in fact, has been in place since 1996. The index measure for loan renewals and extensions told a similar story. A larger proportion of bankers reported increases in requests for loan renewals or extensions than those who reported a decrease. This index, for the District overall, stood at 132 in the latest survey, little changed from responses in the first quarter survey or the second quarter of 2000. There was substantial variation across states in both of these measures. Of particular note was the change recorded in the responses of Wisconsin bankers, where both repayment rates (increased) and renewal/extension rates (decreased) showed substantial relative improvement.

Another measure of financial stress was reflected by the bankers' experience with regard to the volume of farm loans with repayment problems. For the District on average, respondents noted that 5.4 percent of their loan volume was in the "major" or "severe" problem categories. This proportion remained fairly stable over the past year, but was well below the 7.1 percent reported in January 2000.

Finally, interest rates continued to decline on farm related loans. After peaking in the second quarter of 2000, real estate loan rates declined 130 basis points to 7.91 percent, on average, at the end of the second quarter of 2001. During the same period, farm operating loan rates dropped 183 basis points to 8.60 percent. The relatively larger decline in operating loan rates resulted in a substantial reduction in the interest rate differential between operating and real estate loans. This spread decreased from 122 basis points in the second quarter of 2000 to 69 basis points at the end of the second quarter 2001, the smallest differential since early 1995. Narrowing of the spread may reflect a reduction in the risk premium on less-well-secured operating loans.

Looking forward

As noted, respondents indicated that some weakening in loan demand was evident in the second quarter. When asked

Credit conditions at Seventh District agricultural banks

	ns at Seventin	District agricult			Interest rates on farm loans		
	Loan demand	Fund availability	Loan repayment rates	Average loan-to- deposit ratio ¹	Operating Ioans ¹	Feeder cattle ¹	Real estate ¹
	(index)²	(index) ²	(index)²	(percent)	(percent)	(percent)	(percent
1998							
Jan-Mar	134	113	84	68.9	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
1999							
Jan-Mar	120	119	40	69.9	9.03	9.01	8.06
Apr-June	115	107	50	71.7	9.11	9.08	8.18
July-Sept	109	94	63	72.7	9.32	9.28	8.42
Oct-Dec	107	104	72	72.7	9.44	9.41	8.59
2000							
Jan-Mar	121	95	77	72.9	9.78	9.72	8.89
Apr-June	109	76	72	75.5	10.43	10.14	9.21
July-Sept	106	82	77	76.9	10.17	10.14	9.18
Oct-Dec.	105	92	81	74.9	9.92	9.90	8.90
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

1At end of period.

²Bankers 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.

to indicate their near-term (third quarter 2001 relative to third quarter 2000) expectations for non-real-estate loan demand, their responses were fairly balanced. Twenty-three percent of the respondents expected an increase in loan volume and 20 percent expected a decline, giving a loandemand expectation index of 103.

The primary strength in non-real-estate lending was expected to occur in the operating loans category. Other lending, such as feeder cattle loans, dairy loans, and grain storage construction loans were expected to continue relatively weak in the third quarter. Most pronounced, however, was the weakness expected to occur in farm machinery lending, where the index dropped to 66. Iowa and Wisconsin bankers expected the greatest weakness in this category both recorded an index of 56 for farm machinery lending.

Another indicator of credit conditions is reflected in lenders' reliance on loan guarantees. Bankers were asked to indicate if they expect to rely more heavily on the USDA's Farm Service Agency (FSA) farm loan guarantees during the next three months (i.e., July–September) than they did during the same period a year ago. Their responses indicated the lowest level of reliance on FSA guarantees for several years. Nonetheless, 25 percent of the respondents indicated they would rely more heavily on FSA guarantees. The proportion of bankers expecting to reduce their utilization of the guarantees held stable at about 8 percent.

Finally, District bankers continued to expect a weakening in demand for farm real estate loans, relative to the third quarter of 2000. Ten percent of the respondents expected to see an increase in farm real estate loan demand in the third quarter of 2001. On the other hand, 25 percent expected a decline. This pattern matches their observations regarding changes in the institutional structure of agricultural lending. Bankers observed that a substantial increase in farm related lending from non-bank sources was occurring in District states. Farm Credit System (FCS) lending for farm operating loans was up, according to 44 percent of the respondents. FCS financed mortgages were also higher, according to 51 percent of the bankers. Only 3 percent to 4 percent of the bankers thought credit extension by the FCS for operating loans and real estate purchases had declined.

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SELECTED AGRICULTURAL ECONOMIC INDICATORS

SELECTED AGRICULTURAL ECUNUMIC INDICAT	IUKS		Percent change from			
	Latest period	Value	Prior period	Year ago	Two years ago	
Prices received by farmers (index, 1990-92=100)	Julv	106	-0.9	10	13	
Crops (index, 1990-92=100)	July	101	0.0	7	7	
Corn (\$ per bu.)	July	1.88	6.2	15	8	
Hay (\$ per ton)	July	96.30	0.5	20	23	
Soybeans (\$ per bu.)	July	4.92	10.3	9	17	
Wheat <i>(\$ per bu.)</i>	July	2.72	-0.7	17	23	
Livestock and products (index, 1990-92=100)	July	111	-0.9	12	17	
Barrows and gilts (\$ per cwt.)	July	52.00	-1.7	6	61	
Steers and heifers (\$ per cwt.)	July	74.10	-3.5	5	14	
Milk (<i>\$ per cwt.</i>)	July	16.30	1.2	29	18	
Eggs (¢ per doz.)	July	35.0	-2.2	-7	-13	
Consumer prices (index, 1982-84=100)	July	178	-0.3	3	6	
Food	July	178	0.3	3	6	
Production or stocks Corn stocks <i>(mil. bu.)</i>	June 1	3,924	N.A.	9	9	
Soybean stocks (mil. bu.)	June 1	708	N.A.	-9	-17	
Wheat stocks (mil. bu.)	June 1	873	N.A.	-8	-8	
Beef production (bil. lb.)	July	2.18	-4.1	-1	-4	
Pork production (bil. lb.)	July	1.43	-1.6	2	-4	
Milk production* (bil. lb.)	July	12.1	0.0	-1	4	
Receipts from farm marketings (mil. dol.)	May	14,784	3.6	-3	6	
Crops**	May	5,806	-5.9	-10	1	
Livestock	May	8,978	10.8	3	9	
Government payments	May	N.A.	N.A.	N.A.	N.A.	
Agricultural exports (mil. dol.)	May	4,143	-3.3	3	14	
Corn (mil. bu.)	May	113	-31.6	-22	-25	
Soybèans <i>(míl. bu.)</i>	May	40	-26.5	-13	5	
Wheat (mil. bu.)	May	71	-18.3	-21	-18	
Farm machinery sales (units)						
Tractors, over 40 HP	July	6,397	-10.7	1	14	
40 to 100 HP	July	5,181	-12.3	1	15	
100 HP or more	July	1,216	-3.3	2	11	
Combines	July	563	-4.1	10	58	

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

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