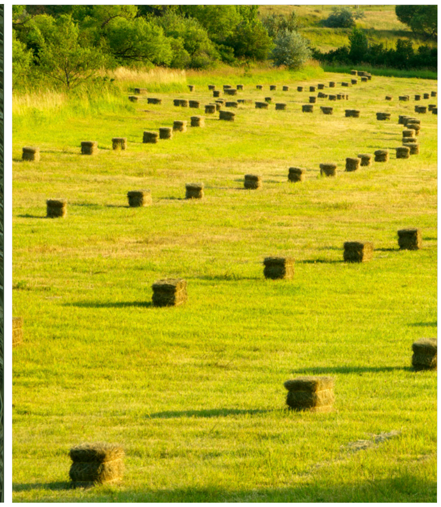
SURVEY *of* TENTH DISTRICT

Agricultural Credit Conditions

1st Quarter 2012

Federal Reserve Bank *of* Kansas City



Farmland Values Rise with Crop Prices

By Jason Henderson, Omaha Branch Executive, and
Maria Akers, Associate Economist

District farm income rose sharply in the first quarter as crop prices rebounded and drought conditions eased. After sliding at year-end, crop prices rallied in the first quarter with shrinking crop supplies and intense competition for planted acreage. Higher crop prices improved marketing opportunities for farmers still holding some of the 2011 harvest in storage. In addition, a majority of District bankers expected farmers would adjust their 2012 crop mix to maximize profits.

Timely rains and a mild winter bolstered winter wheat crop conditions, brightening farm income prospects in Oklahoma and Kansas. Strong export demand and low cow inventories underpinned a first-quarter rise in cattle prices, but profit margins varied with production costs. District bankers indicated high feed costs and poor pasture conditions were factors delaying herd expansion, particularly in the southern Plains.

Strong farm incomes continued to fuel demand for farmland. District farmland value gains accelerated in the first quarter even as record-high farmland values enticed more landowners to sell. For the first time since the survey began in the late 1970s, the annual value of District cropland rose more than 20 percent for two consecutive years. First-quarter ranchland values climbed higher as well, jumping 16 percent above year-ago levels. Looking forward, about a third of survey respondents expected the upward trend in farmland values would continue through the next few months.

"Strong farm incomes continued to fuel demand for farmland."

Farm credit conditions strengthened further in the first quarter while demand for farm loans dwindled. Agricultural producers continued to pay down debt and used more cash for operating expenses, capital spending and farmland purchases. Collateral requirements for farm loans eased slightly, and District bankers indicted ample funds were available at lower interest rates for qualified borrowers.

Chart 1
Tenth District Farm Income and Farm Loan Demand

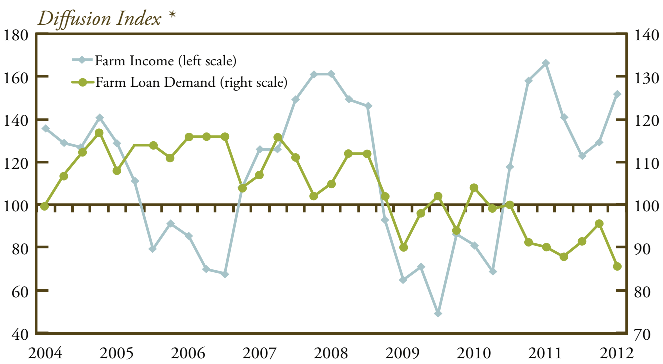


Chart 2
Tenth District Farm Income by State

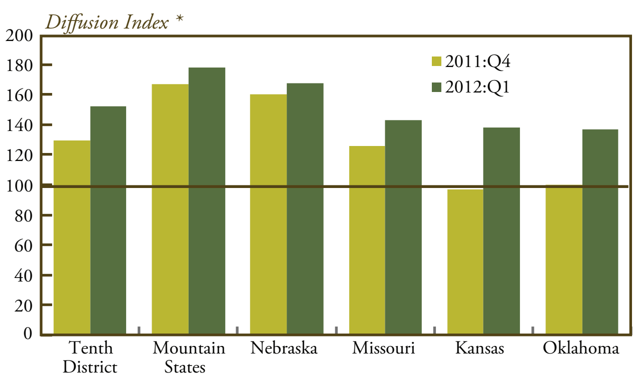
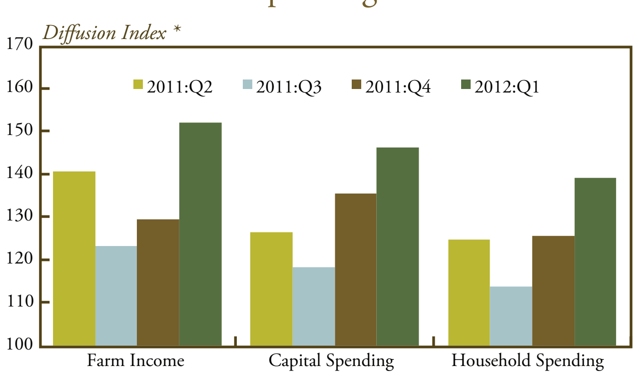


Chart 3
Tenth District Farm Income, Capital Spending and Household Spending



Higher commodity prices and easing drought conditions spurred strong farm income gains across the District. In the first quarter, more bankers reported higher farm income compared to last year as lean supplies and competition for acreage lifted crop prices from a year-end slump (Chart 1). Producers that held back part of last year's harvest stood to profit from the modest rally in crop prices. Looking ahead, survey respondents expected a shift in crop mix that would increase corn and wheat plantings at the expense of soybeans. Several bankers noted some farmers were converting pasture ground to row crops when feasible.

Bankers reported higher farm income in Kansas and Oklahoma as more rainfall across the southern Plains improved growing conditions (Chart 2). With a milder-than-normal winter, the wheat crop was ahead of schedule and in much better condition than last year. Despite rising cattle prices, many livestock operators that culled herds during the drought were not rebuilding cow inventories, partly due to high feed costs and limited grazing. Soaring energy production bolstered District farm income with rising land lease revenues from mineral rights.

Strong farm income lessened the need for debt financing and cut loan demand at agricultural banks. The index of farm loan demand fell to its lowest level since the late 1980s. Sluggish loan demand, however, did not indicate a slowdown in farm sector spending. According to survey respondents, farm income gains and high levels of liquidity spurred additional household and capital spending in the first quarter (Chart 3).

** Bankers responded to each item by indicating whether conditions during the current quarter were higher than, lower than 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.*

Chart 4
Tenth District Farmland Values—Quarterly Gains

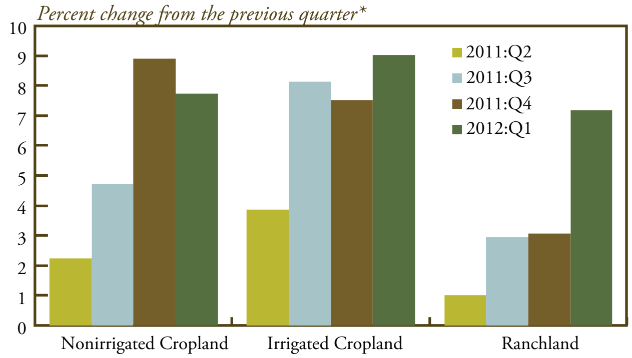


Chart 5
Tenth District Farmland Values-Annual Gains

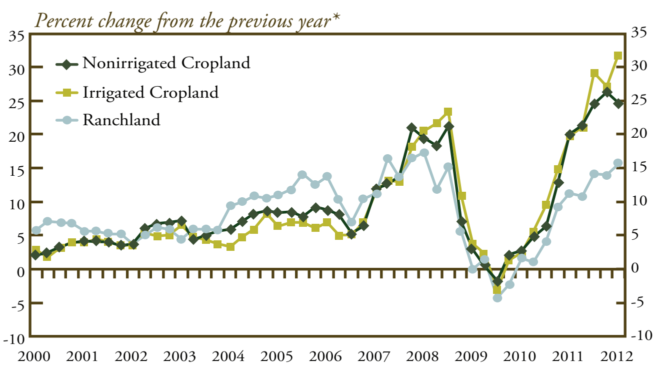


Table 1
Farmland Value Gains by State

*Percent change from the previous year**

	Nonirrigated	Irrigated	Ranchland
Kansas	24.0	25.9	22.3
Missouri	13.5	n/a**	7.1
Nebraska	38.6	41.4	26.1
Oklahoma	8.9	n/a**	6.1
Mountain States	17.4	19.0	12.0

District farmland values climbed higher in the first three months of 2012, posting sharp quarterly gains. Compared with the fourth quarter of 2011, the value of nonirrigated and irrigated cropland in the District surged by 8 and 9 percent, respectively (Chart 4). Ranchland values also shot up in the first quarter, appreciating more than 7 percent since the end of last year.

The swift rise in District farmland values was also evident when compared with the prior year. The value of nonirrigated cropland rose 25 percent above year ago levels in the first quarter of 2012, on top of the more than 20 percent gain posted in 2011 (Chart 5). With dry conditions still prevalent in much of the District, the value of irrigated acreage vaulted more than 30 percent higher than a year ago, a new survey high. In addition, annual ranchland values surged 16 percent as high feed costs boosted demand for pasture ground. Nebraska once again led farmland value gains for the District, followed by Kansas (Table 1).

Record-high farmland prices prompted landowners to place more land on the market. Despite larger supplies, buyers remained willing to pay record prices at land auctions. Furthermore, survey respondents did not expect the farmland market to cool in the near future. About a third of District bankers anticipated farmland values would rise further while the remaining respondents expected farmland values to hold at peak levels.

**Percent changes are calculated using responses only from those banks reporting in both the past and the current quarter.*
***Not reported due to small sample size.*

Chart 6
Tenth District Farm Loan Repayment Rates and Renewals and Extensions

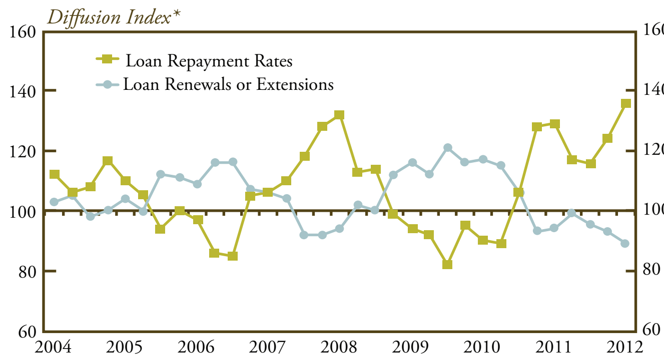


Chart 7
Tenth District Farm Loan Demand and Funds Availability

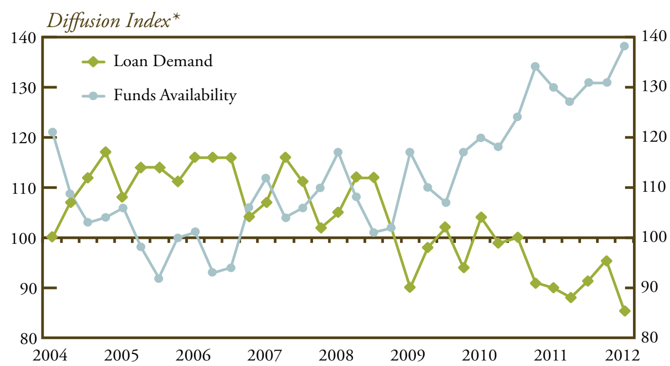
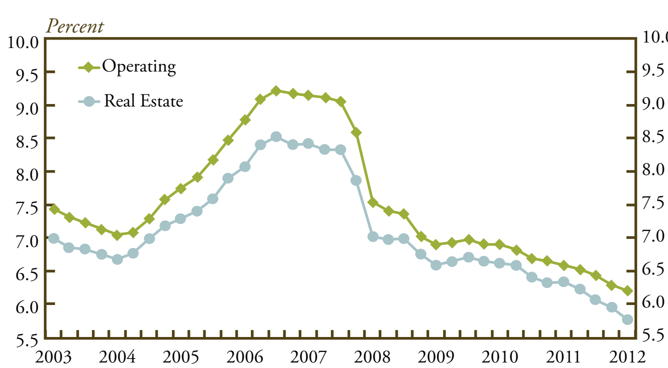


Chart 8
Tenth District Farm Interest Rates



District farm credit conditions also strengthened in the first quarter. With stronger incomes, the farm loan repayment index rose further, surpassing the recent high set in 2008 (Chart 6). Conversely, the number of loan renewals and extensions fell for the third straight quarter and dipped to a new low. The amount of carryover debt, however, varied by region. Nebraska had the lowest percentage of carryover debt while Oklahoma had the highest. Several bankers commented that proceeds from crop insurance and mineral leases were driving loan repayments in drought areas.

The funds availability index reached a new high in the first quarter as the farm loan demand index fell (Chart 7). Less than 1 percent of District bankers reported a decline in funds available for farm loans, while almost 40 percent had more funds available for qualified borrowers. With weak loan demand heightening competition between lenders, collateral requirements for farm loans eased slightly and interest rates continued to fall. In the first quarter, interest rates averaged 6.2 percent for operating loans and 5.8 percent for farm real estate loans (Chart 8).

With high levels of liquidity in the farm sector, District bankers reported that buyers were increasing the use of cash payments and equity to finance farmland purchases. In early 2011, survey respondents indicated new debt was being used to finance slightly more than half of the purchase price of new farmland sales. In the first quarter of 2012, bankers reported higher cash down payments and greater use of pledged equity from existing real estate holdings had lowered the share of new debt financing on new real estate purchases to 47 percent.

**Bankers responded to each item by indicating whether conditions during the current quarter were higher than, lower than 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.*

BANKER COMMENTS *from* *the* TENTH DISTRICT

"Oil and gas lease income and high cattle prices have caused a large pay down in our loans."

—Western Kansas

"Farmers are cash rich and very liquid. Demand for loans is down."

—South Central Nebraska

"Oil play and crop insurance has caused higher loan repayments and lowered loan demand."

—Western Oklahoma

"Water supply for irrigation may be short this year as snowpack is 80 percent of average."

—Southeast Colorado

"There is more liquidity in the farm sector than I have seen in my 30 years as a banker."

—Northeast Kansas

"Most cattle producers are delaying herd expansion."

—Central Kansas

"Land prices are higher and more buyers are out-of-town investors."

—Southeast Wyoming

"Demand exceeds supply of farms on the market. More farmers are paying cash for machine sheds and new equipment."

—Northwest Missouri

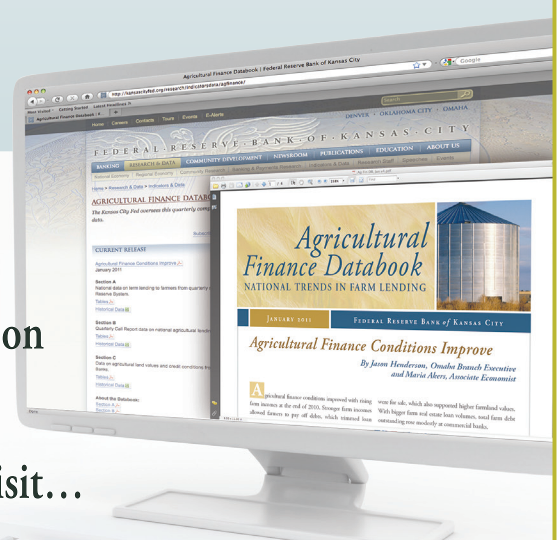
"Pasture that could potentially be tilled is bringing significantly higher prices."

—Southeast Nebraska

"In need of rain–crop insurance and oil lease money are keeping the skids greased."

—Western Kansas

__Note:__ 235 banks responded to the first-quarter Survey of Agricultural Credit Conditions in the Tenth Federal Reserve District—an area that includes Colorado, Kansas, Nebraska, Oklahoma, Wyoming, the northern half of New Mexico and the western third of Missouri. Please refer questions to Jason Henderson, Omaha Branch executive, or Maria Akers, associate economist, at 1-800-333-1040, or __Jason.Henderson@kc.frb.org__ or __Maria.Akers@kc.frb.org__. The views expressed in this article are those of the authors and do not necessarily reflect the views of the Federal Reserve Bank of Kansas City or the Federal Reserve System.



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