Survey of Agricultural Credit Conditions

Fourth Quarter 2006

FEDERAL RESERVE BANK *of* KANSAS CITY

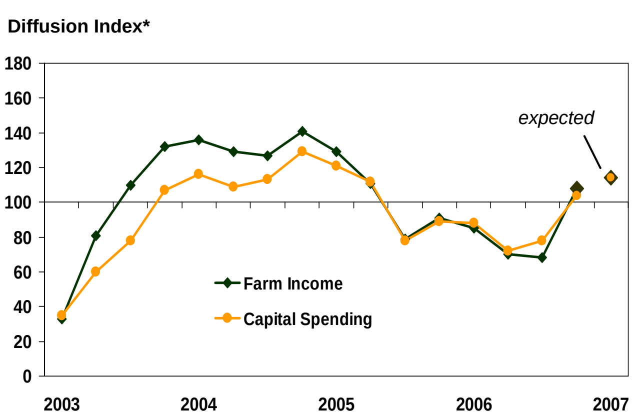
A mixed rebound in farm financial conditions

by Jason Henderson, Omaha Branch Executive and Maria Akers, Assistant Economist

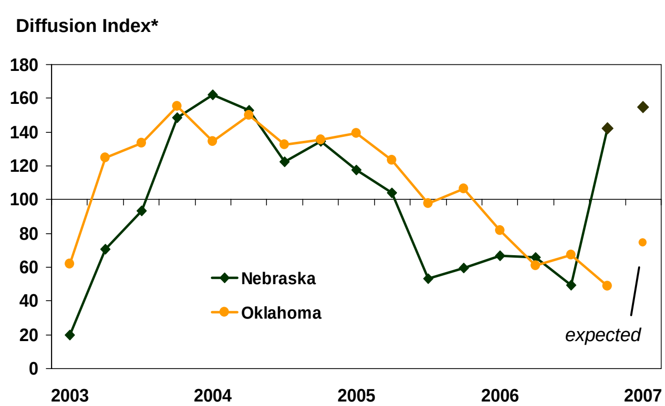
- District farm income rebounded in the fourth quarter compared to year ago levels, but the gains were not evenly distributed geographically or across agricultural sectors. Led by Nebraska, major corn producing states enjoyed a sharp rise in income that more than offset continued declines for Oklahoma farmers and flat income levels in the mountain states. The farm income index rose above 100 for the first time since mid-2005, and bankers expect to sustain that momentum through the first quarter of 2007.

- Ethanol-driven demand for corn presents a mixed outlook for the district. While crop farmers look to benefit from record-high commodity prices, livestock producers are watching their feed costs rise and profit margins shrink. Both farmers and ranchers are concerned about potentially higher input costs and the uncertain drought conditions in 2007.

Farm Income and Capital Spending



Farm Income



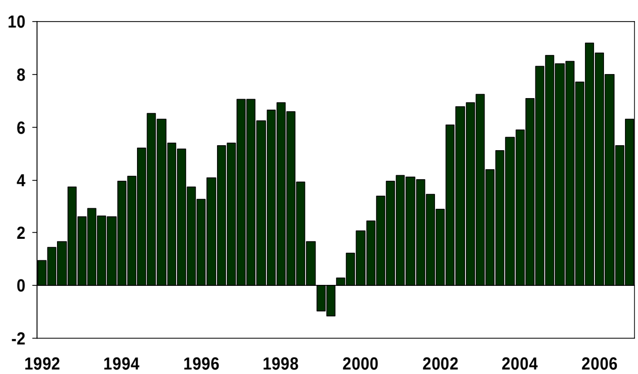
*Bankers responded to each item by indicating whether conditions during the current quarter were higher than, lower than, or the same as in the year-earlier period. The index numbers are computed by subtracting the percent of bankers that responded "lower" from the percent that responded "higher" and adding 100.

- Gains in district farmland values strengthened in the fourth quarter, fueled by higher crop prices. The largest gain was for irrigated cropland, which was not only up from last quarter, but also from a year ago. In contrast, gains slowed from last year for ranchland and nonirrigated land. Compared to a year ago, gains averaged 10.4 percent for ranchland, 6.3 percent for nonirrigated cropland, and 6.9 percent for irrigated cropland.

- Like last year, nonfarm investors were active participants in the farmland market, accounting for just over one-third of farmland purchases. With crop prices up, investor interest has shifted to return on capital. Recreational demand for farmland has stabilized at a high level. Bankers expect gains in farmland values to strengthen further in early 2007, partly due to the increased investor activity.

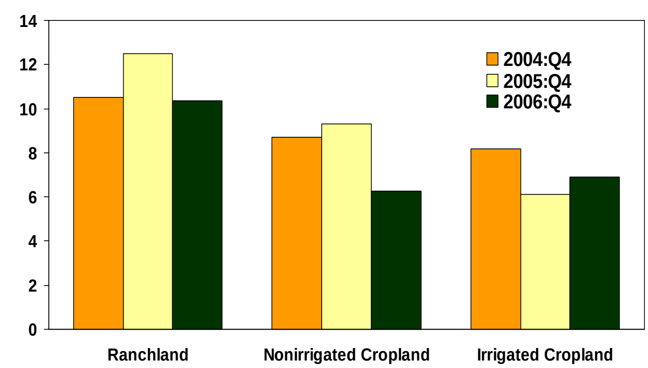
Nonirrigated Cropland Value Gains

Percent change from a year ago*



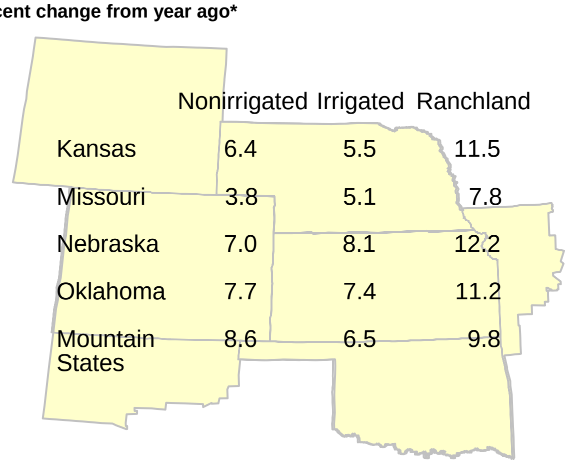
Farmland Value Gains

Percent change from year ago*



Farmland Value Gains by State

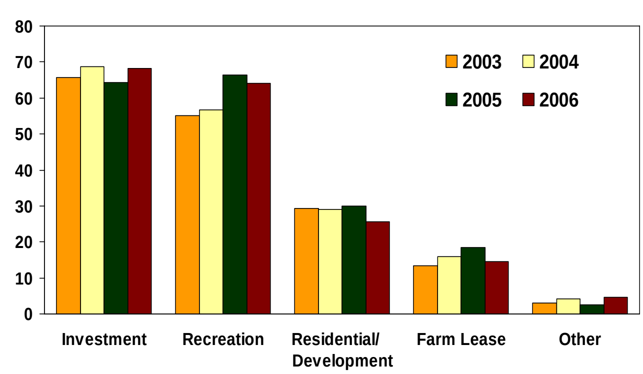
Percent change from year ago*



	Nonirrigated	Irrigated	Ranchland
Kansas	6.4	5.5	11.5
Missouri	3.8	5.1	7.8
Nebraska	7.0	8.1	12.2
Oklahoma	7.7	7.4	11.2
Mountain States	8.6	6.5	9.8

Reasons for Farmland Purchases by Nonfarmers

Percent of respondents**

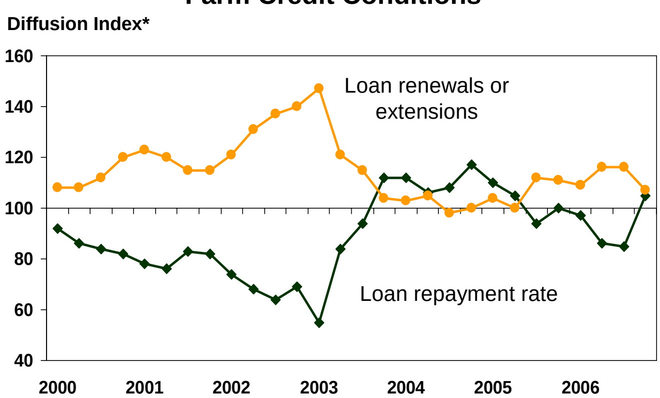


* Percent changes are calculated using responses only from those banks reporting in both the past and the current quarter.
**Respondents could choose more than one category; therefore, percentages will not add to 100.

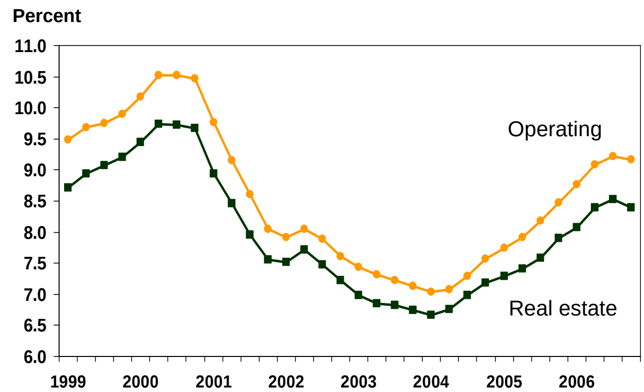
- Farm credit conditions improved along with farm balance sheets. Bankers reported higher loan repayment rates in the fourth quarter and fewer requests for loan renewals and extensions. Farm interest rates eased in the fourth quarter after steadily increasing for the last two years. Interest rates averaged 8.4 percent on farm real estate loans and 9.2 percent on farm operating loans.

- After holding steady for over a year, the loan demand index fell 12 points to 104 in the fourth quarter. Conversely, the funds availability index rose 12 points to 106, the first time the two indices have crossed since early 2004. Bankers anticipate an increased demand for farm loans in first quarter 2007, with a slight drop in funds availability. With income prospects up, farmers are expected to boost capital expenditures next year, pushing up credit demand.

Farm Credit Conditions



District Farm Interest Rates



*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.

Selected Comments from District Bankers

"As crop prices have increased, livestock prices have decreased. With a mix of half crop, half livestock in our area, we are in a stage of uncertainty." – *Western Missouri*

"With cattle going down and grain going up, plus the dry weather we have had, it is a hard call to know where we are going." – *SE Kansas*

"With the good yields and prices, I anticipate local farmers will replace old, worn-out equipment." – *NE Colorado*

"Exorbitantly high corn prices have brought outside investors into our area." – *NE New Mexico*

"Higher grain prices this fall have certainly been a help for debt servicing." – *NC Kansas*

Note: 268 banks responded to the fourth 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, Assistant 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 author and do no necessarily reflect the views of the Federal Reserve Bank of Kansas City or the Federal Reserve System.

For more information or to view past survey results, visit:
www.kansascityfed.org/agcrsurv/agcrmain