

# Agricultural *FINANCE* Monitor

agricultural credit conditions in the Eighth Federal Reserve District

2012 ■ Fourth Quarter

The third quarterly survey of agricultural credit conditions was conducted by the Federal Reserve Bank of St. Louis from December 17 through December 31; the results presented here are based on the responses from 61 agricultural banks within the boundaries of the Eighth Federal Reserve District.<sup>1</sup> The Eighth District includes all or parts of seven Midwest and Mid-South states. Because these initial data are not adjusted for any seasonal irregularities (should they exist), users are cautioned to interpret the results carefully. In particular, users are cautioned against drawing firm conclusions about longer-run trends in farmland values and agricultural lending conditions.<sup>2</sup>

In addition to our standard survey questions, we asked four special questions on farmland sale trends for this edition of the *Agricultural Finance Monitor*. In particular, we were interested in knowing (i) how the volume of farmland sales in 2012 compared with that in 2011, (ii) the share of farmland purchased by farmers, (iii) the motives for land purchases by non-farmers, and (iv) how the majority of farmland buyers financed their purchase.

## Survey Results

On net, respondents reported that fourth-quarter District farm income and spending were higher than one year ago (see Table 1). Bankers indicated that farm income in the St. Louis and Louisville zones was on pace with a year earlier (fourth quarter of 2011), while the southern portion of the District (i.e., the Little Rock and Memphis zones) reported a notable increase in income and spending. Importantly, income in the Memphis zone in the fourth quarter was higher than a year earlier because corn and soybean yields in the southern portion of the District were significantly higher than in northern areas. Farmers in the south were thus able to profit from the rise in commodity prices stemming from last year's drought.

The District's relatively strong performance in the fourth quarter contrasts sharply with the widespread anticipation

### Selected Quotes from Banker Respondents Across the Eighth Federal Reserve District

*An influx of unplanned income arising from crop insurance payments due to the drought increased capital spending. Cattle prices are high, but herd numbers are down in our area. (Arkansas)*

*The 2012 drought greatly reduced production, but all of our bank's borrowers carried crop insurance, and many had higher levels of coverage. This has resulted in good income for most, and most will carry that income into 2013. (Illinois)*

*We see land values trending higher. Recently farmers have been borrowing more to purchase real estate as some banks have loosened their down-payment requirements due to lack of loan demand. (Missouri)*

*The majority of farmers are now leaving the banks and refinancing their farm debt with the Farm Credit agencies. They are taking advantage of the long-term fixed rates that Farm Credit services provide. (Missouri)*

NOTE: These are generally verbatim quotes, but some were lightly edited to improve readability.

in the previous survey that last summer's drought would significantly lower income and capital spending in the St. Louis and Louisville zones (see Table 2). In the aggregate, bankers in the current survey indicated no decrease in income and spending and outcomes were a bit better than expected in all zones.<sup>3</sup> Many bankers cited the effect of crop insurance in alleviating the expected negative impact of the drought. Regarding this development, see the boxed insert of selected quotes from survey participants. According to the U.S. Department of Agriculture, estimated crop insurance claims will reach \$21 billion nationwide for 2012—more than any other year by far. Missouri and



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The Eighth Federal Reserve District is headquartered in St. Louis and includes branch offices in Little Rock, Louisville, and Memphis; the District includes the state of Arkansas and portions of Illinois, Indiana, Kentucky, Mississippi, Missouri, and Tennessee.

In the survey, bankers were asked two types of questions: (i) estimates of current dollar values and interest rates and (ii) expectations for future values. Dollar values and rates refer to the fourth quarter of 2012. Regarding expectations for future values, bankers were asked whether they expect values to increase, decrease, or remain constant (either relative to a year ago or relative to current values; see table descriptions). A “diffusion index” value was then created for “income and expenditures” and for the 3-month trends in “land values” and “cash rents” (per acre). The diffusion index was created by subtracting the percent of bankers that responded “decrease” from the percent that responded “increase” and then adding 100. Index values from 0 to 99 indicate overall expectations of decreasing values; index values from 101 to 200 indicate overall expectations of increasing values; and an index value of 100 indicates an even split.

**Table 1**

**Income and Expenditures, Land Values, and Cash Rents**

	St. Louis	Little Rock	Louisville	Memphis	District
<b>Income and expenditures (versus year-ago levels)</b>					
Farm income					
2012:Q4 (actual)	103	125	100	167	116
2013:Q1 (expected)	77	100	100	100	87
Household spending					
2012:Q4 (actual)	119	138	100	122	120
2013:Q1 (expected)	97	100	114	89	98
Capital spending					
2012:Q4 (actual)	113	138	114	122	118
2013:Q1 (expected)	84	86	100	89	87
<b>Land values</b>					
Quality farmland	\$6,340	\$2,557	\$5,000	\$3,194	\$5,230
Expected 3-month trend	153	113	138	144	144
Ranchland or pastureland	\$2,728	\$2,150	\$2,050	\$1,894	\$2,396
Expected 3-month trend	138	114	133	133	133
<b>Cash rents</b>					
Quality farmland	\$214	\$91	\$202	\$139	\$187
Expected 3-month trend	145	133	150	133	143
Ranchland or pastureland	\$71	\$51	\$82	\$60	\$67
Expected 3-month trend	132	125	100	113	123

Illinois farmers have been the recipients of 23 percent of the \$13.7 billion in claims that have already been paid out on the 2012 crop.<sup>4</sup>

With fourth-quarter income at higher-than-expected levels, household spending, outlays for capital expenditures, and loan repayment rates in the fourth quarter were also stronger than expected across the District. By contrast, loan demand, while still positive, turned out to be a bit softer than initially expected. A notable exception was in the Memphis zone, where loan demand was reported to be much stronger than expected.

With the notable exception of respondents from the St. Louis zone, expectations for farm income in the first quarter of 2013 are on par with 2012 (see Table 1). Compared with the other three zones, proportionately more bankers in the St. Louis zone expect farm income in the first quarter of 2013 to fall below levels from a year earlier (first quarter of 2012). For the District as whole, bankers also expect household spending to remain close to year-ago levels, but lean toward a decrease in capital spending in the first quarter of 2013 relative to a year ago. Tax provisions allowing accelerated depreciation on quali-

**Table 2**

**Expected and Actual 2012:Q4 Variables (versus year-ago levels)**

	St. Louis	Little Rock	Louisville	Memphis	District
<b>Farm income</b>					
Expected	70	113	67	100	82
Actual	100	125	100	175	116
Difference	30	13	33	75	35
<b>Household spending</b>					
Expected	89	125	117	113	102
Actual	111	138	100	125	116
Difference	22	13	-17	13	14
<b>Capital spending</b>					
Expected	56	125	33	113	73
Actual	104	138	117	113	112
Difference	48	13	83	0	39
<b>Demand for loans</b>					
Expected	133	113	150	75	122
Actual	119	100	83	125	112
Difference	-15	-13	-67	50	-10
<b>Availability of funds</b>					
Expected	122	125	100	114	119
Actual	111	138	133	114	119
Difference	-11	13	33	0	0
<b>Rate of loan repayment</b>					
Expected	81	113	83	125	94
Actual	104	138	100	113	110
Difference	22	25	17	-13	16

NOTE: All variables are reported using a diffusion index. See the note above Table 1 for details about interpreting diffusion indexes. For comparison purposes, we compute diffusion indexes using only those banks that responded to the given question in both the 2012:Q3 and 2012:Q4 surveys. Components may not sum to totals due to rounding.

fyng farm asset purchases were set to expire at year-end 2012. This factor may have contributed to a lift in capital asset purchases by farmers and agricultural bank lending in the fourth quarter. Further, rising fertilizer and seed costs may have enticed some crop producers to pre-pay for 2013 inputs. While boosting current loan volume, this factor may contribute to a more tempered outlook for near-term loan growth.

Finally, Table 1 also shows that bankers continue to report an upward trend in land values and cash rents. Compared with the previous quarter’s survey, bankers reported that land values (quality farmland, ranchland, or pastureland) increased by an average of 4 percent. As in our previous two surveys, bankers expect land values and cash rents to continue to rise. Gains in quality farmland

are generally expected to outpace gains in ranchland or pastureland (nonirrigated) in almost all zones.

Overall, Eighth District bankers continue to report strong lending conditions (see Table 3). With the exception of loan demand in Louisville, bankers indicated an increase in loan demand, funds availability, and loan repayment rates in all zones in the fourth quarter of 2012 relative to the fourth quarter of 2011. Moreover, there is a strong sentiment toward greater loan demand and funds availability in the first quarter of 2013 relative to 2012. Interest rates, both fixed and variable, continue to show modest declines.

**Table 3**

**Lending Conditions**

	St. Louis	Little Rock	Louisville	Memphis	District
<b>Loans (versus year-ago levels)</b>					
Demand for loans					
2012:Q4 (actual)	109	100	88	122	107
2013:Q1 (expected)	123	129	138	138	128
Availability of funds					
2012:Q4 (actual)	112	138	125	125	119
2013:Q1 (expected)	110	117	125	133	117
Rate of loan repayment					
2012:Q4 (actual)	109	138	113	111	114
2013:Q1 (expected)	97	100	100	113	100
<b>Interest rates (%)</b>					
Operating					
Fixed	5.24	6.75	5.38	5.96	5.56
Variable	4.59	6.15	5.21	5.22	4.99
Machinery/intermediate-term					
Fixed	5.45	6.61	5.50	6.25	5.74
Variable	4.77	6.13	5.36	5.40	5.18
Farm real estate					
Fixed	4.87	6.36	5.44	5.62	5.26
Variable	4.48	5.58	5.18	5.42	4.92

NOTE: Demand for loans, availability of funds, and rate of loan repayment are reported using a diffusion index. See the note above Table 1 for details about interpreting diffusion indexes.

**Special Questions**

Given the strong growth in farmland values over the past few years, we asked Eighth District bankers some additional questions to gauge the nature of lending activity in this market. In particular, we asked (i) how the volume of farmland sales in 2012 compared with that in 2011; (ii) the share of farmland purchased by farmers; (iii) the potential motives for land purchases by non-farmers; and (iv) how the majority of farmland buyers financed their purchase. Table 4 summarizes the responses.

In the District as a whole, bankers were roughly split over whether the volume of farmland sales in 2012 exceeded the levels in 2011. A majority of bankers in the St. Louis and Little Rock zones indicated increased sales, while bankers in Memphis reported the opposite. Interestingly, all bankers surveyed in the Louisville zone indicated a decrease or no change. On average, bankers indicated that 73 percent of the farmland purchased was purchased by farmers. Of the land not purchased by farmers (third ques-

tion in Table 4), nearly all bankers indicated investment as a common reason for purchases. The next most common reasons were for lease (either farming or hunting/fishing), while only a small number of bankers indicated residential or other recreational motives. [NOTE: respondents were given the option of selecting more than one reason.]

Finally, bankers indicated strong competition between commercial banks and the Farm Credit System to finance the land purchases, with a slight edge toward the Farm Credit System. One banker indicated that “the majority of farmers are now leaving the banks and refinancing with Farm Credit agencies.” A common view among District bankers seems to be that commercial banks are finding it difficult to compete with the Farm Credit System’s tax exemption and low cost of funds. Many respondents are thus concerned about the longer-term implications of this development for their farmland lending business. ■

**Table 4**

**Farmland Sales**

	St. Louis	Little Rock	Louisville	Memphis	District
<b>Change in sales volume</b>					
No change or decrease	36	38	100	56	47
Increase	64	63	0	44	53
<b>Share of land purchased by farmers</b>					
Average across respondents	77	58	83	64	73
<b>Reasons for purchasing land</b>					
Investment	96	88	100	88	94
Farm lease	14	50	20	13	20
Hunting/fishing lease	25	25	20	25	24
Residential	0	13	20	13	6
<b>Finance method</b>					
Cash	16	25	0	11	14
Commercial banks	41	25	43	44	39
Farm Credit System	44	50	57	33	45
Insurance companies	0	0	0	11	2

NOTE: Bankers were asked how the volume of farmland sales in 2012 compared to 2011, the share of farmland purchased by farmers, and how the majority of farmland buyers financed their purchase. Of the land not purchased by farmers, bankers were asked the reason for purchase. The table reports (1) the share of bankers indicating an increase or no change/decrease in sales volume from 2011 to 2012, (2) the average response to the fraction of land purchased by farmers, (3) the share of bankers that cited a given purpose as motivating land sales in their area, and (4) the share of bankers that indicated a given financing method as being the most predominant source of funding for farmland purchases in their area. Bankers were allowed to select all reasons for purchase in their area, so the share of responses to this question sum to over 100%.

**Notes**

<sup>1</sup> An agricultural bank, for survey purposes, is defined as a bank for which at least 15 percent of its total loans outstanding finances agricultural production or purchases of farmland, farm equipment, or farm structures.

<sup>2</sup> Readers are also cautioned that the number of responses in each zone is relatively small. Statistically, this tends to suggest that the summary statistics for each zone have a larger plus-or-minus margin of error than for the District as a whole.

<sup>3</sup> When comparing the current survey results with those of the previous survey, we consider only the responses of those bankers who responded to the relevant question in both the current and previous survey.

<sup>4</sup> See <http://www3.rma.usda.gov/apps/sob/state.cfm>. Data are current as of February 4, 2013.



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 Views expressed do not necessarily reflect official positions of the Federal Reserve System.