

The Farm Economy and Outlook for Ag Lending



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February 26, 2016

The views expressed are those of the author and do not necessarily reflect the opinions of the Federal Reserve Bank of Kansas City or the Federal Reserve System

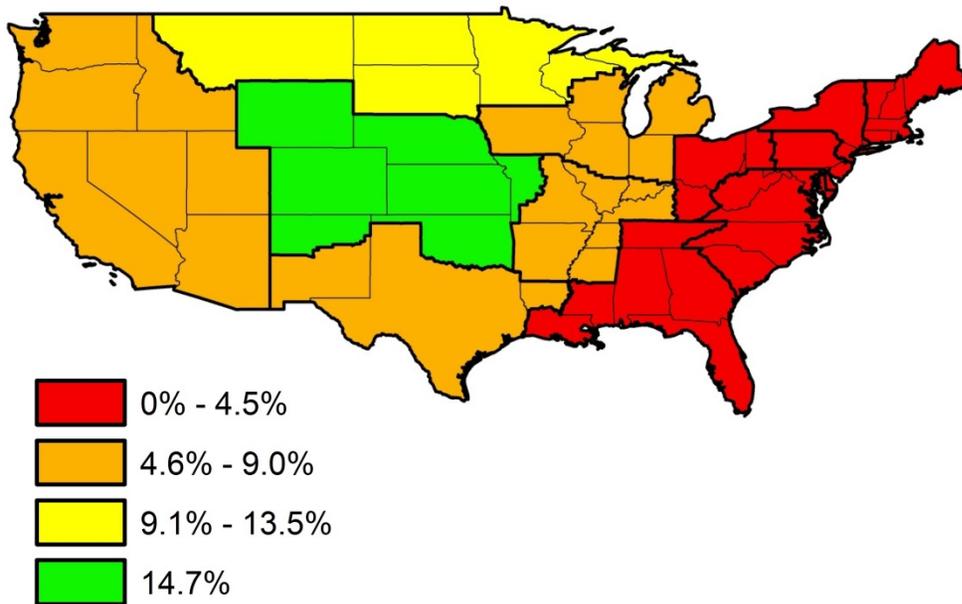
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Of the 12 Fed Districts, the 10th District is the most concentrated in agriculture by some measures.

Average Farm Income as a Share of Total Personal Income

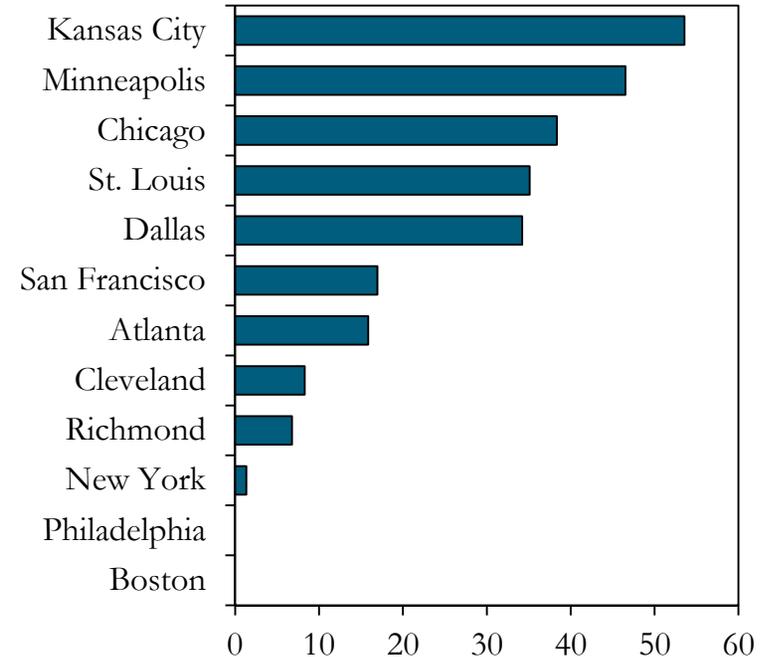
Average Across Counties by Fed District



Source: BEA.

Proportion of “Farm Dependent” Counties

Percent



Source: BEA, USDA, and staff calculations

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Pop Quiz

1. Weakness in the farm economy is:

- a) persisting
- b) intensifying
- c) gradual
- d) all of the above
- e) none of the above

2. Outside economic factors could best be described as:

- a) tailwinds
- b) headwinds
- c) irrelevant



Pop Quiz

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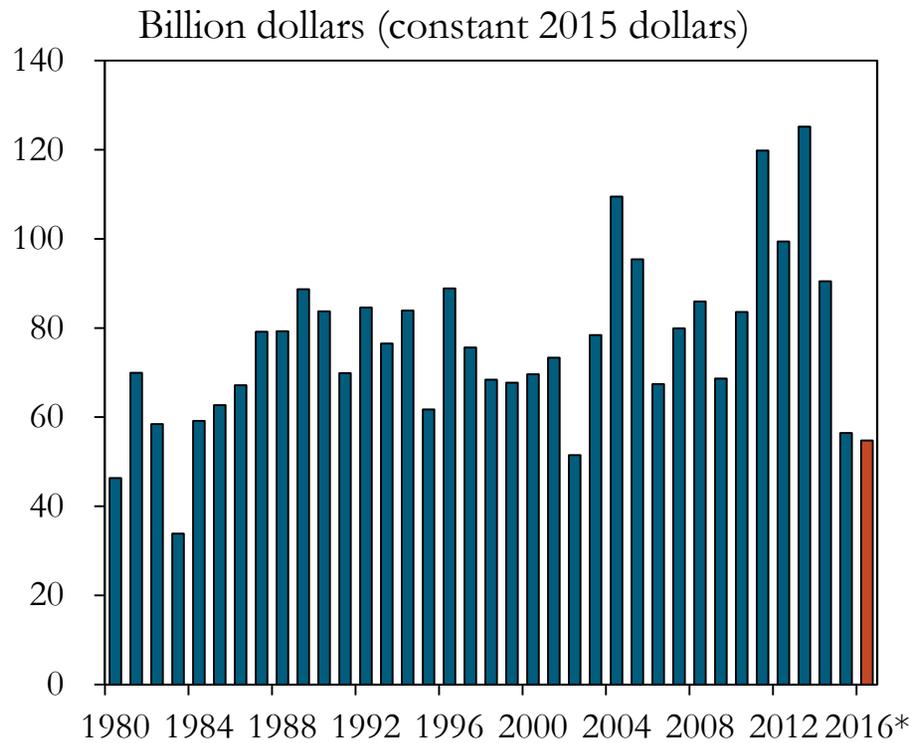
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Farm income has dropped sharply, and is expected to remain low.

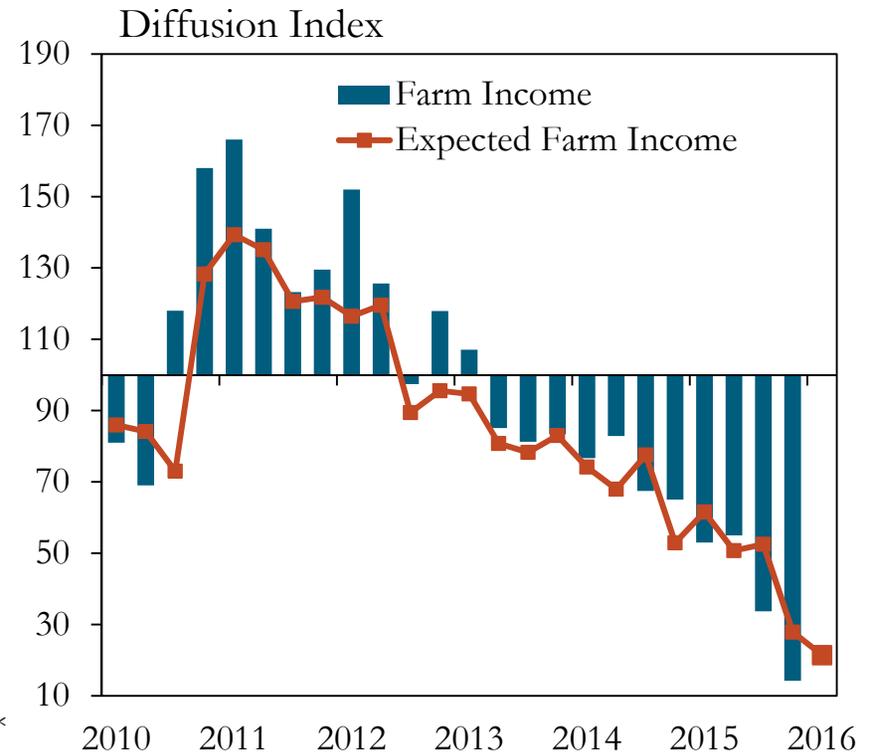
U.S. Real Net Farm Income



Sources: USDA and Federal Reserve Bank of Kansas City.

* Forecast for 2016.

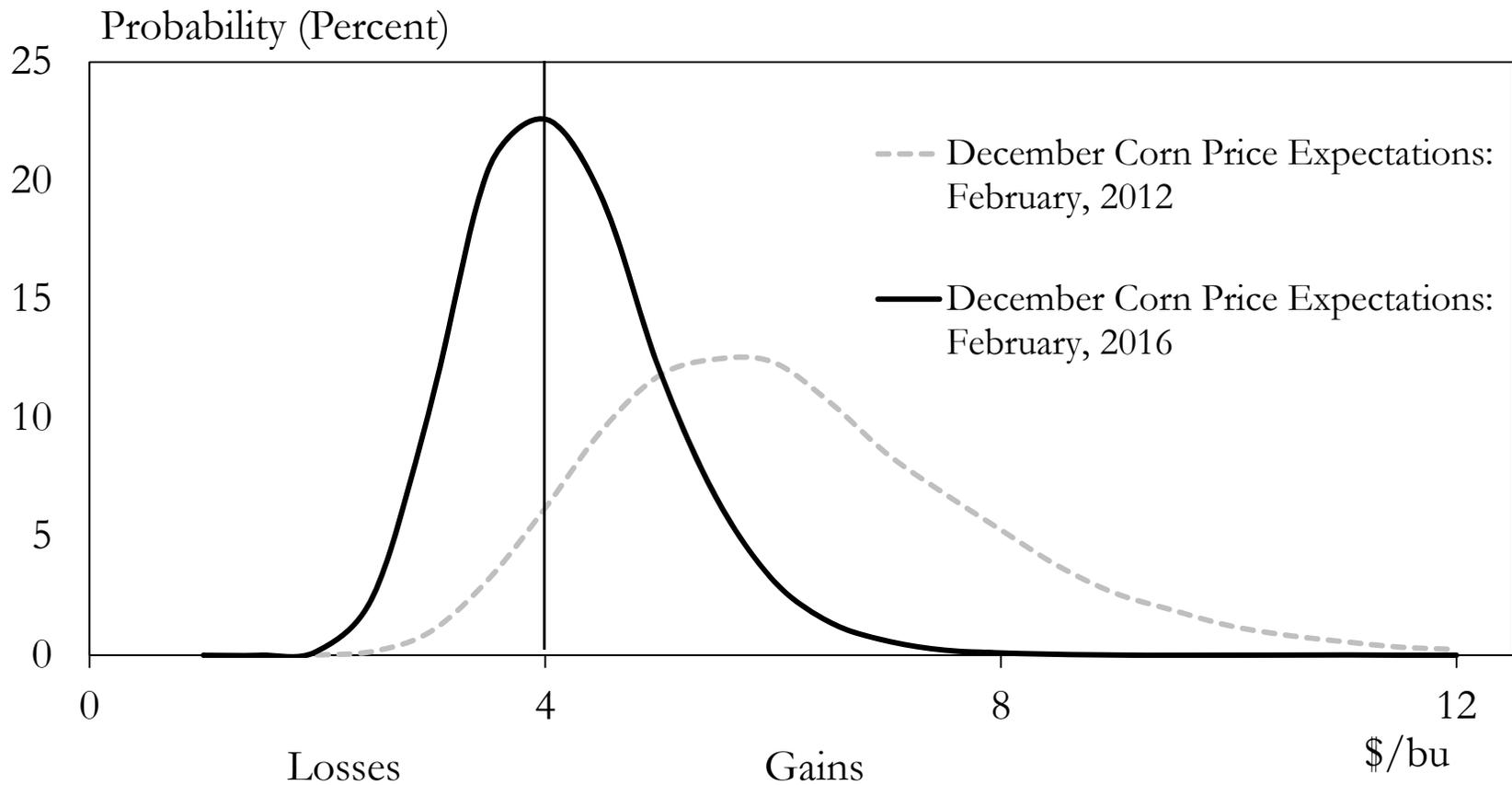
Tenth District Farm Income



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Expected crop prices have shifted dramatically in recent years.



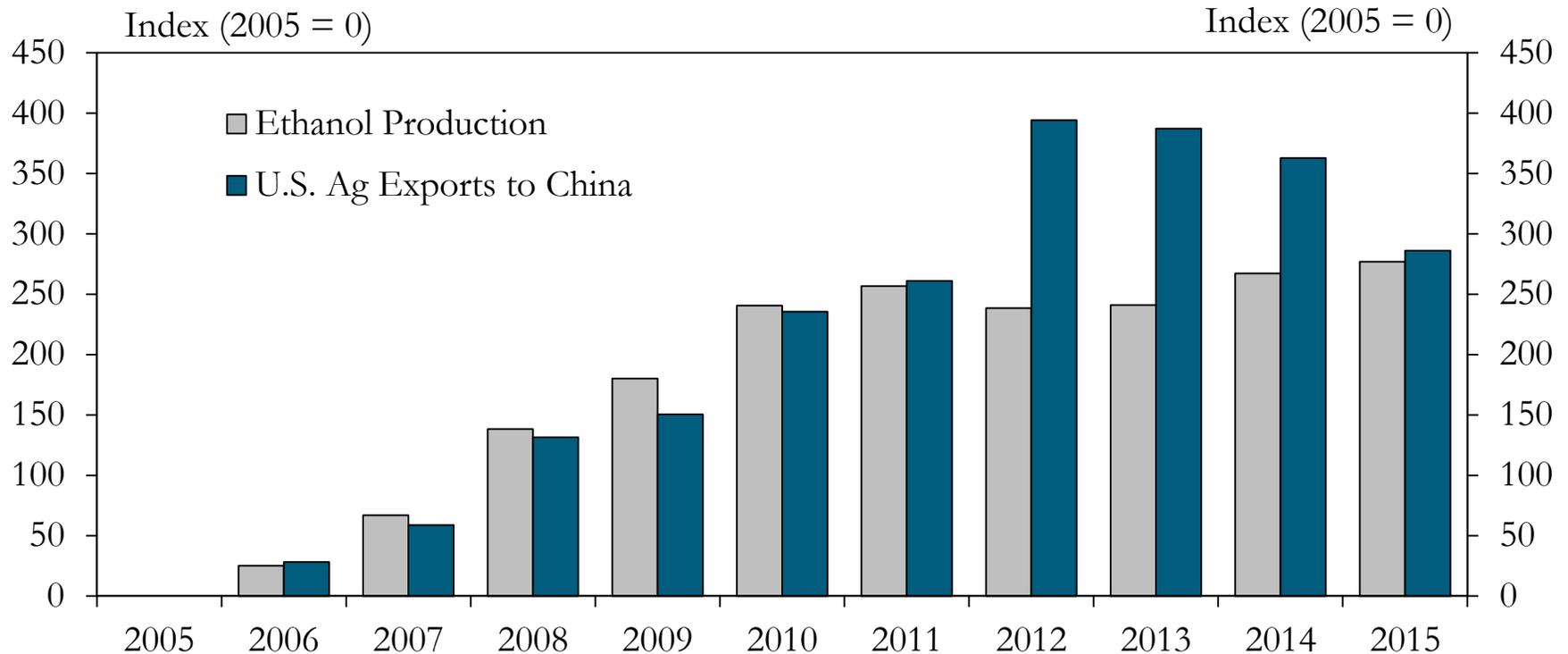
Source: Calculations based on data from barchart.com

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Increased production has driven crop prices lower, but demand strength will be a key long-term driver.

U.S. Ethanol Production and Ag Exports to China



Sources: USDA, Energy Information Administration and Renewable Fuels Association

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Recent developments in China have accentuated concerns surrounding future demand.

China Stock and Manufacturing Indexes



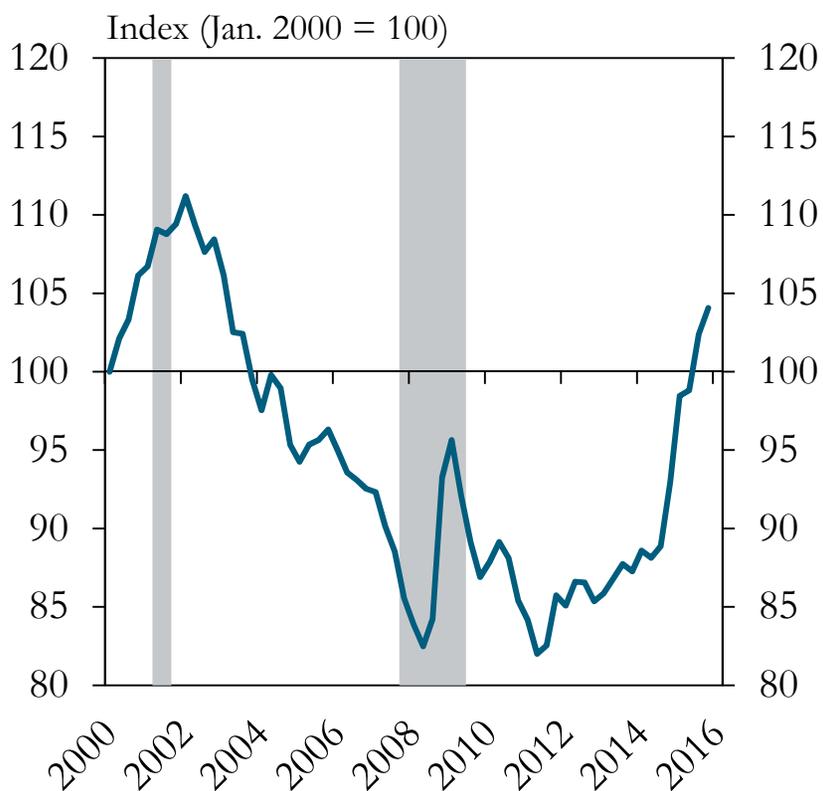
Source: Yahoo! Finance

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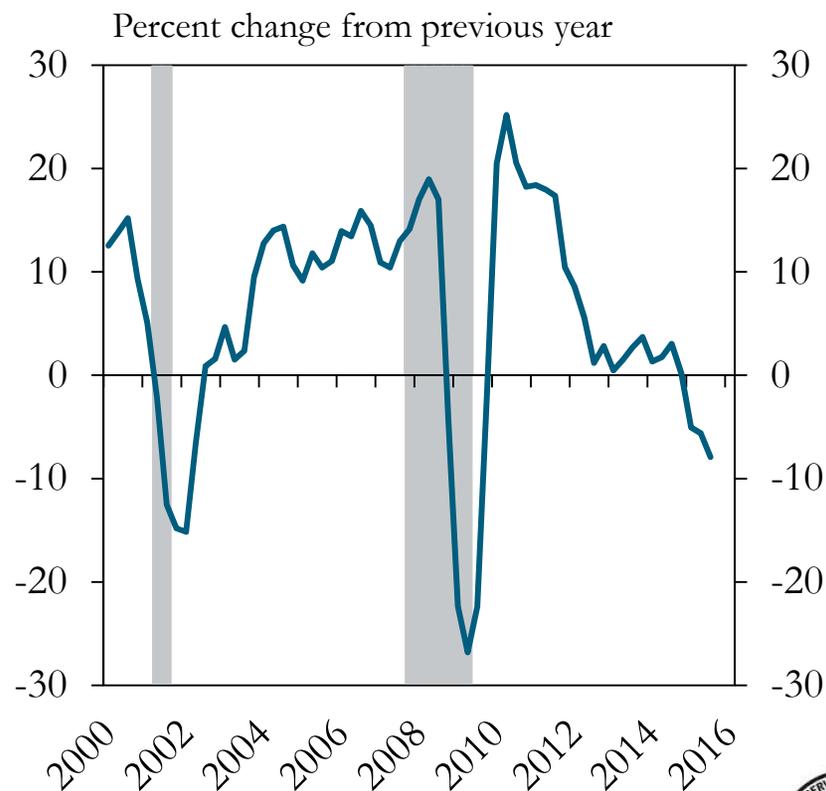


In general, U.S. exports have been weak, driven by further strengthening of the U.S. dollar.

Value of U.S. Dollar*



Value of U.S. Exports

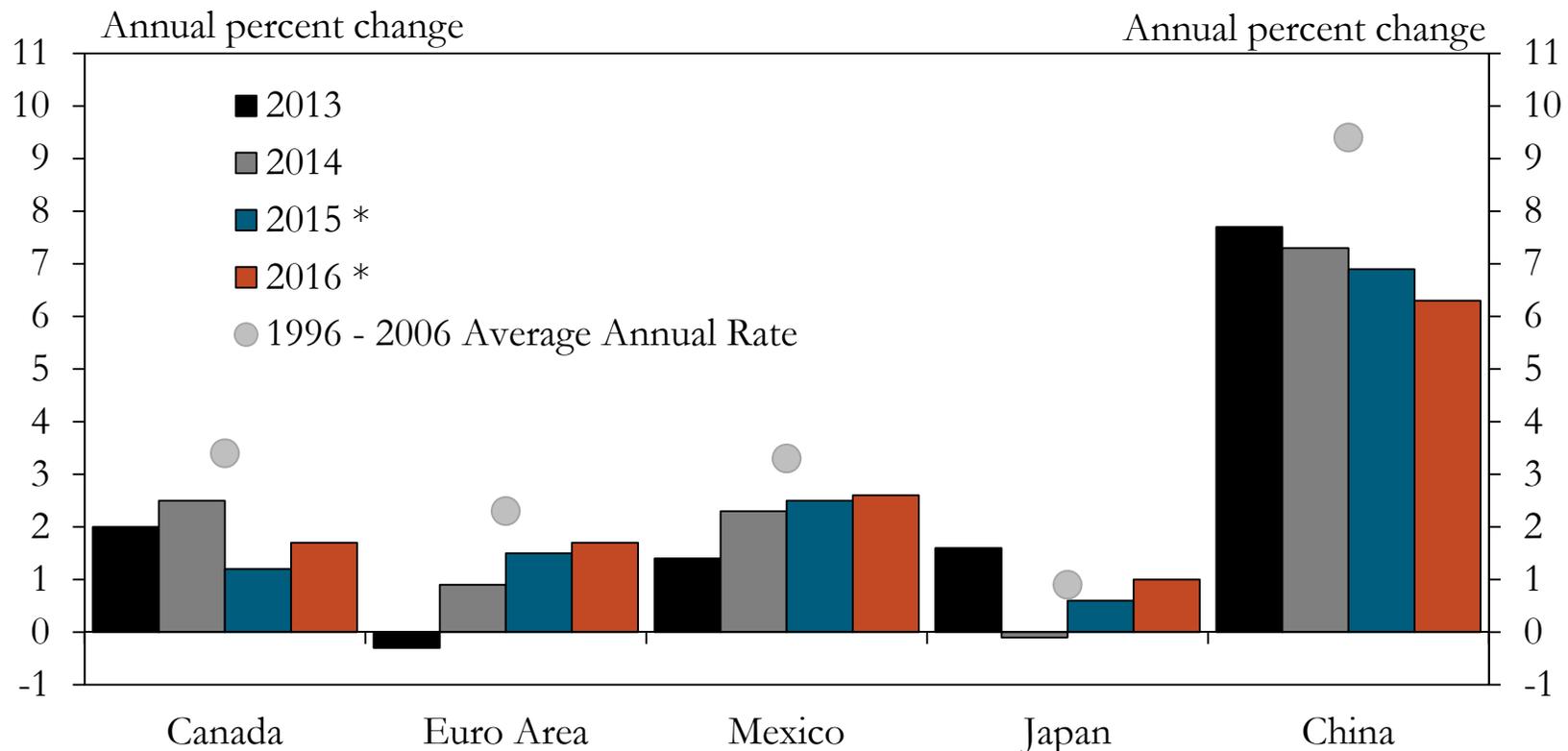


* Nominal Trade-weighted broad index
Source: Federal Reserve Board and Haver Analytics



The stronger dollar reflects relatively weak global economic growth in 2014 and 2015.

Global Real GDP Growth



* Forecast

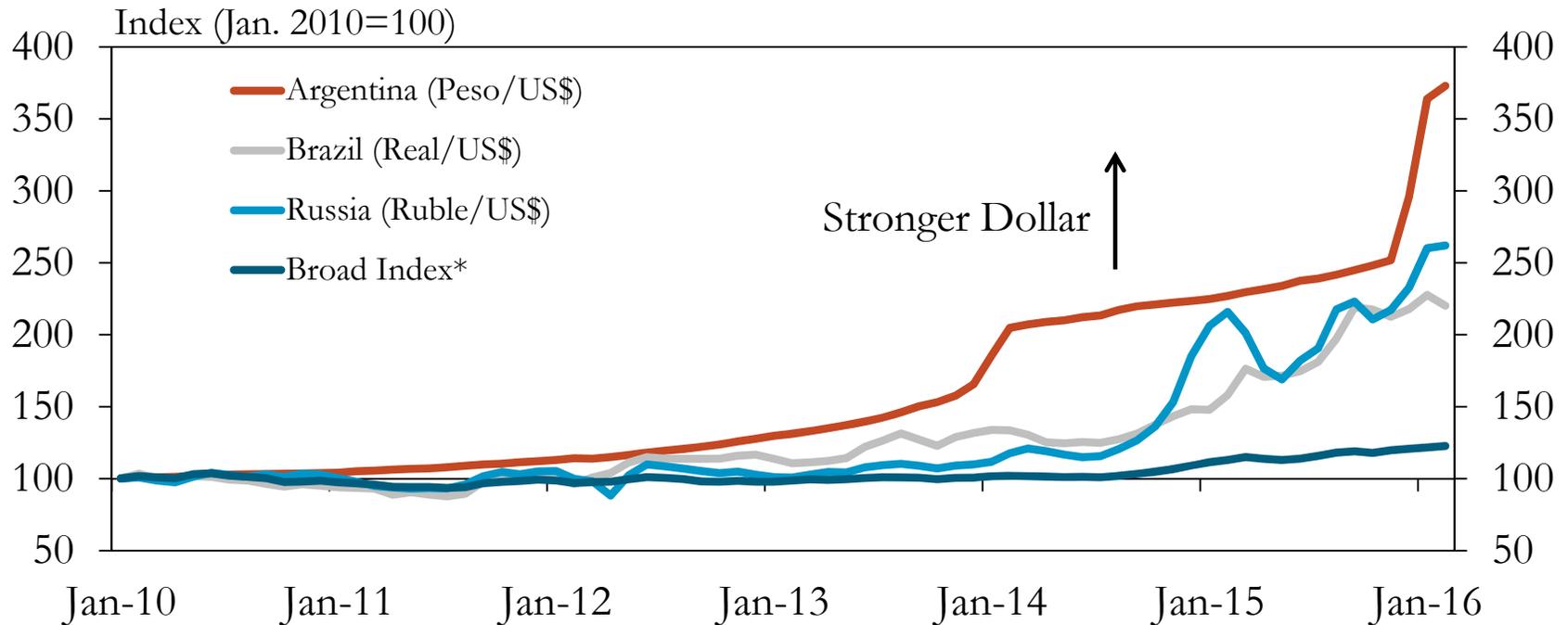
Source: IMF January 2016 Update

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The dollar has surged even more dramatically against key regions competing in global ag export markets.

Currency Exchange Rates



*Nominal broad trade-weighted exchange value of the U.S. dollar
Sources: FRB, IMF and Haver Analytics.

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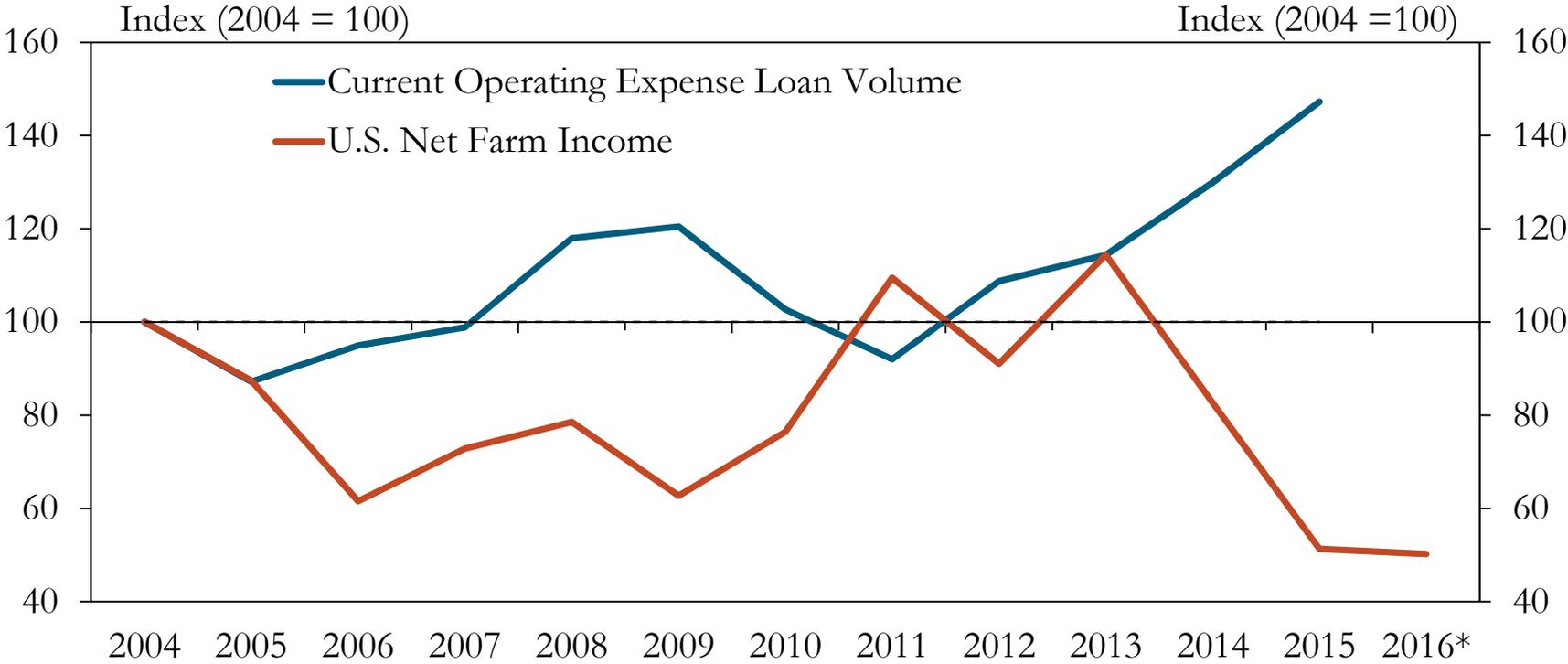


*The downturn in ag is intensifying.
Implications for lending?*



The drop in farm income has reduced cash flow, and increased short-term lending needs.

U.S. Farm Income and Operating Loans



Sources: Agricultural Finance Databook Table A.3 and USDA.



Credit conditions have gradually deteriorated.

Tenth District Credit Conditions

2015, Fourth Quarter

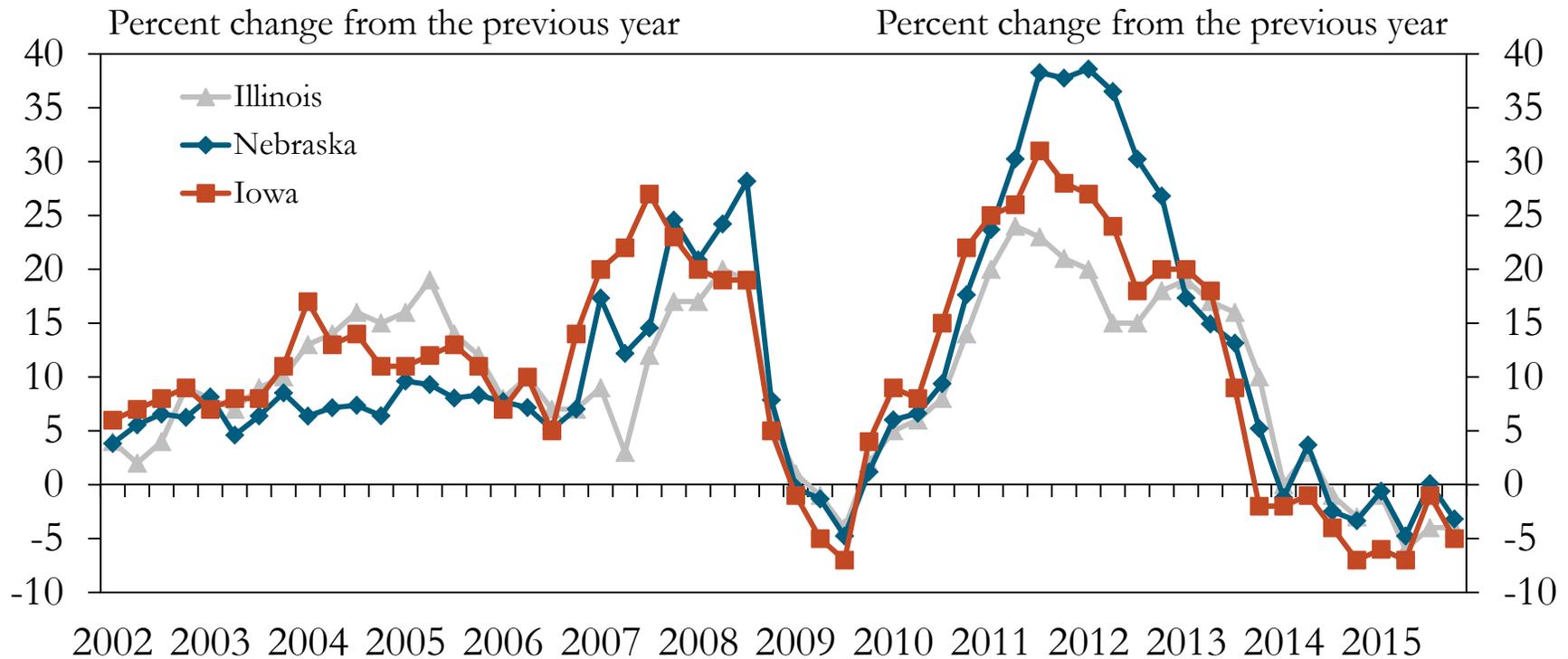


Source: Federal Reserve Bank of Kansas City, Survey of Ag Credit Conditions



Farmland values have also declined,
but only at a modest pace.

Changes in High Quality Farmland Values



Source: Federal Reserve Banks of Kansas City and Chicago.

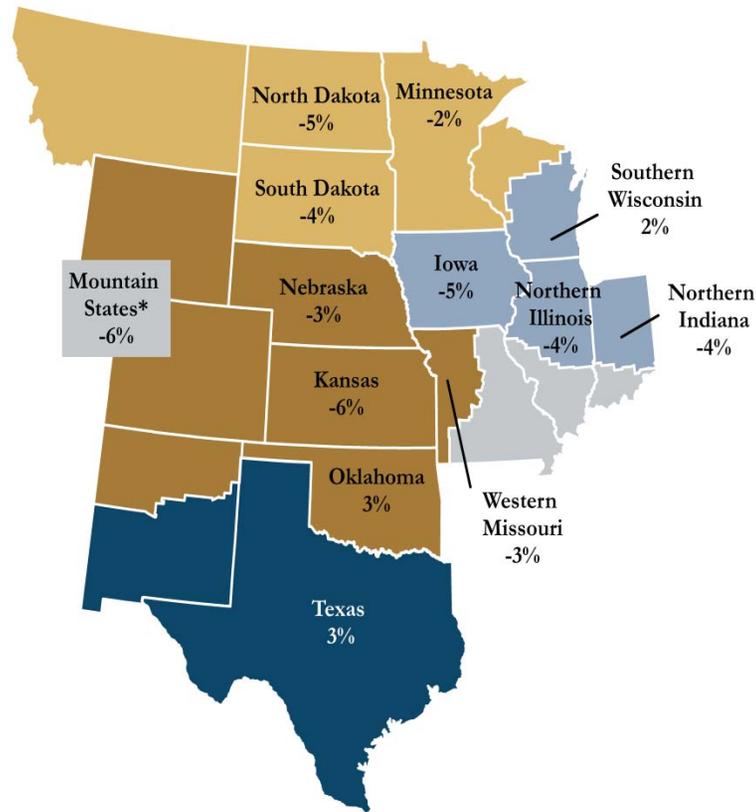
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Despite only modest reductions in average farmland values, the variation has increased dramatically.

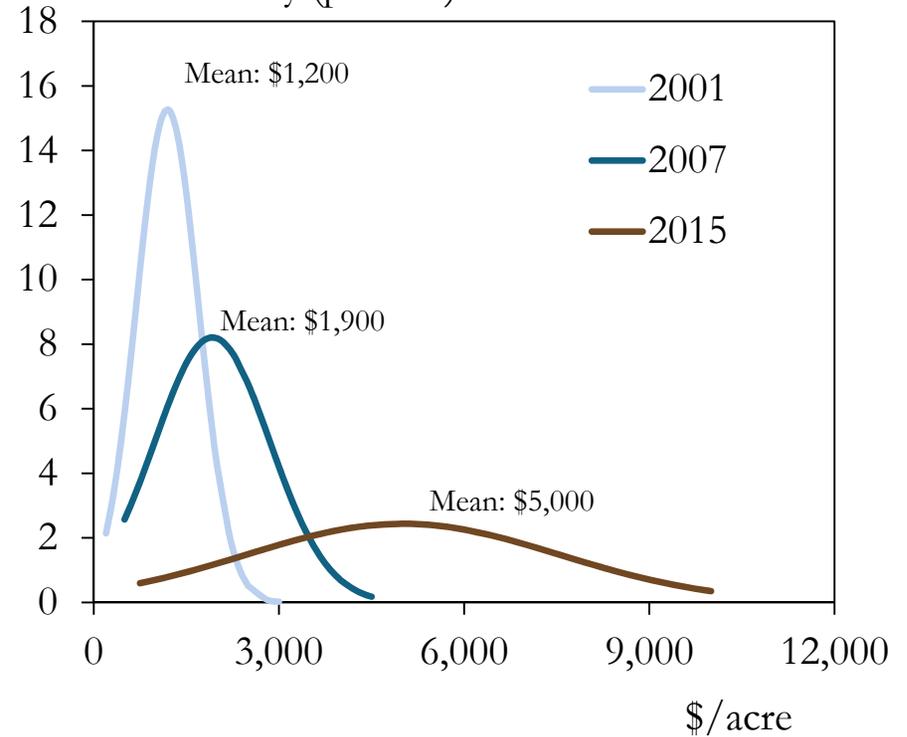
Value of Non-irrigated Cropland, Fourth Quarter 2015

Percent change from previous year



Distribution of Tenth District Irrigated Farmland Values

Probability (percent)



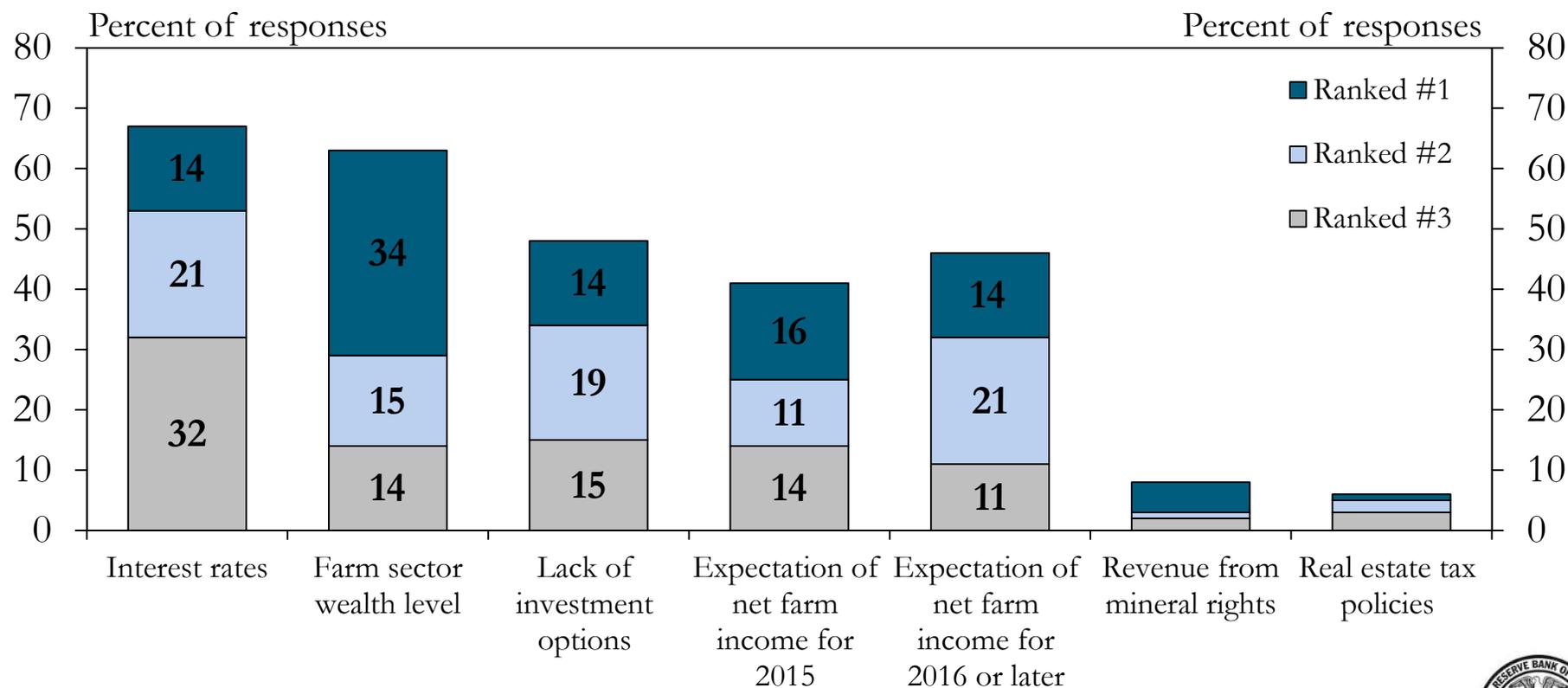
Source: Federal Reserve Bank of Kansas City

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Bankers have noted several key factors that have shaped the path of farmland values.

Factors Contributing to Farmland Values, 2015



Source: Federal Reserve Bank of Kansas City

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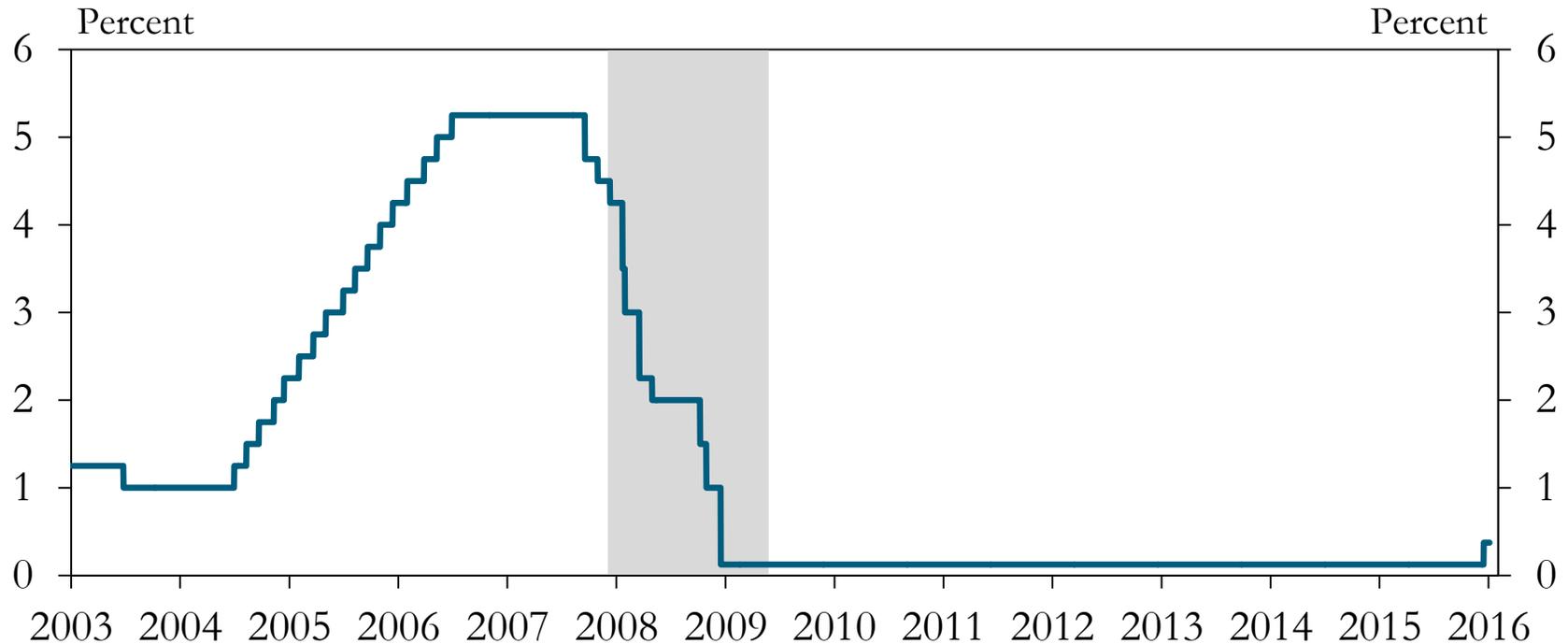


How might a changing interest rate environment affect the ag economy?



The Fed raised the Fed Funds target rate by 25 bp in December.

Federal Funds Target Rate



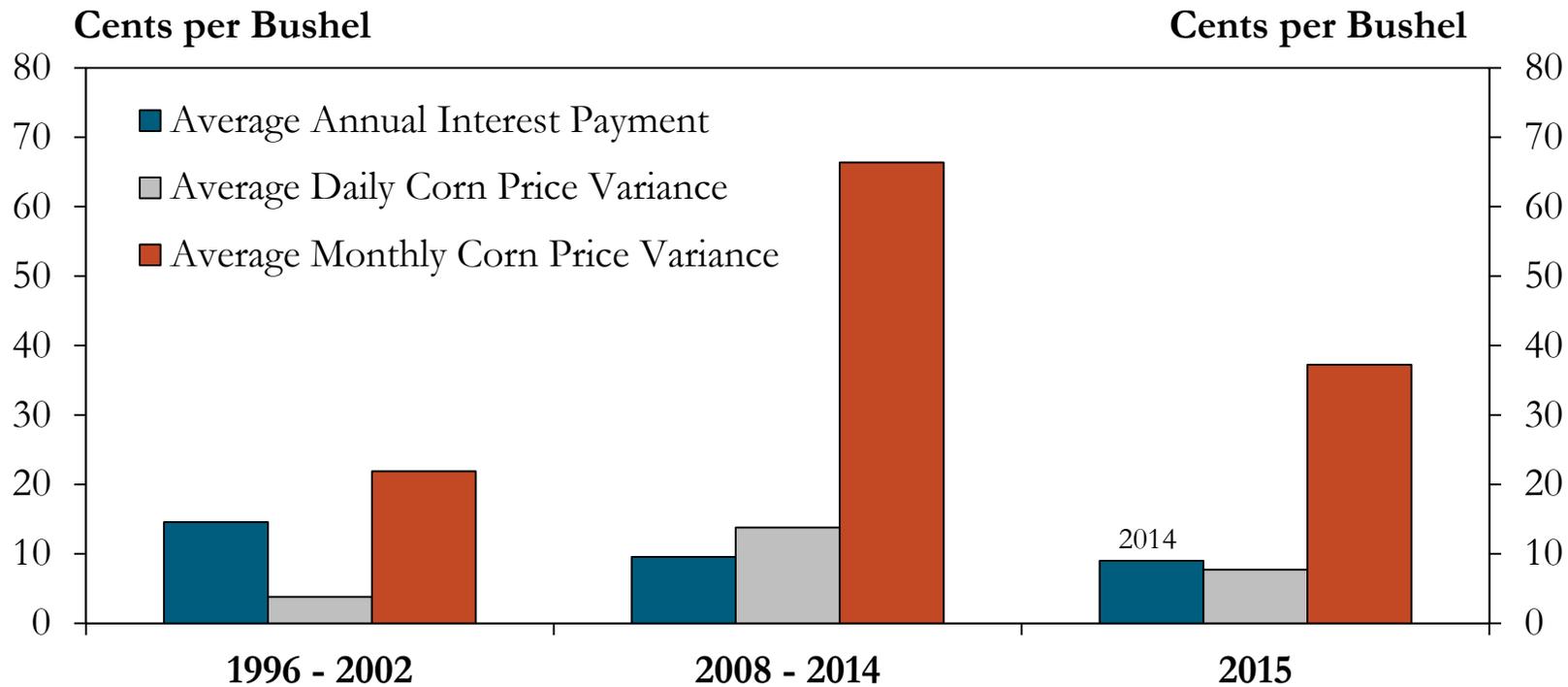
Sources: Federal Reserve Board and Haver Analytics

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Interest expenses, however, are small when compared to fluctuations in commodity prices.

U.S. Corn Producers: Interest Costs and Price Fluctuations



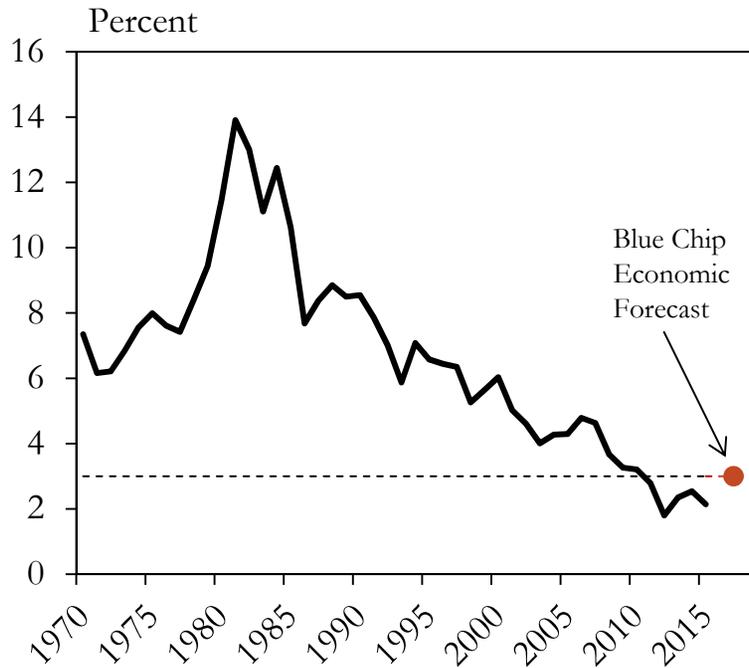
Sources: USDA, barchart.com and author's calculations.

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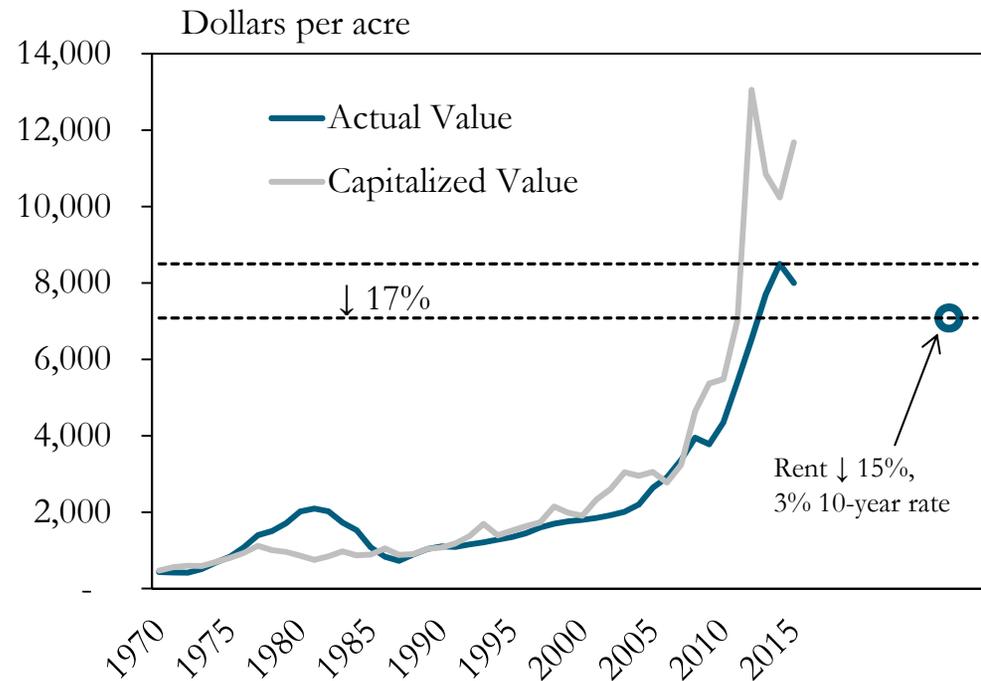


Expectations of future interest rates and cash rents suggest farmland values could decline further.

10-Year Treasury Yields



Iowa Cropland Values



Sources: USDA, Haver Analytics, Blue Chip Economic Forecasts and author's calculations

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Concluding Points

- Farm income has continued to weaken with low commodity prices.
 - Supply-side headwinds: strong U.S. and global production.
 - Demand-side headwinds: ethanol, export markets, and China.
- Effects of the downturn in the farm economy:
 - Tightening credit conditions.
 - Pressure on cash rents and farmland values.
 - Consolidation (opportunities for some).
 - Accelerating decline where rural = ag.



Questions?

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