The Financial Crisis: Linkages and Impacts in Agriculture
Bruce J. Sherrick
Department of Agricultural and Consumer Economics
University of Illinois

What is now often simply called "The Crisis" refers to a set of interconnected financial market transactions with culminating results including: a drop in the Dow from around 14,000 to under 6,500; effectively frozen term debt markets in late 2008; unprecedented government interventions aimed to improve investor confidence and unfreeze funding channels; government takeovers of GSEs and private firms; virtual elimination of the investment banking sector; and widespread failures of firms that in many cases were considered blue-chip industries only months earlier. These effects followed a period of unprecedented ag-commodity price volatility during summer 2008 which left many producers unable to effectively hedge, added to the difficulty in managing input commitments, and altered capital replacement and/or expansion decisions. The Crisis hopefully peaked in the fourth quarter of 2008, but it may be years before the economy fully recovers, and it remains to be seen how the effects will ripple through the ag sector.

What are the key linkages in the agricultural sector and how will the impacts play out? While many have compared the degree of stress to that of the 1980s, This Crisis is not generally viewed as including widespread agricultural credit events, and responses in the sector have been largely sympathetic or through other connections to the general economy.

"It's not the '80s"

First, relative to the previous ag crisis of the 1980s, the sector entered The Crisis in relatively good financial health. Compared to most other sectors, agriculture has exceptionally low leverage. USDA data indicate that the overall ag debt-to-asset ratio was only 9.1% as of 2008. Further, 2008 was a year of record agricultural income, following several other years of relatively high income levels. Further buffering the impacts, land values represent over 85% of the assets in the sector and averaged 14.5% (IL) annual increases the past five years. While the double digit annual increases have since stemmed, there have been few indications thus far of substantial declines and most certainly not of the magnitude experience in residential real estate.

Credit markets

Much of the funding for credit provided to agriculture is fungible with credit supplied elsewhere. Summary measures of the costs of funds to support agricultural credit are shown in table 1 which reports the Farm Credit System's cost of funding relative to Treasuries. Information is provided as of three dates - the pre-crisis period of July 2008, during the height of the crisis in November, and recently when short term
spreads returned to attractive levels. Relative to other agency funding experience, and particularly with respect to the 1980s, the funding for agricultural credit remained available, and was, at least on an ex post basis, managed very well by the funding agency.

Increased energies for regulatory reform do seem to pervade the policy debate, and agriculture will not be immune to the effects "Let's not waste a good crisis" seems a common sentiment, and a popular posturing response by politicians in any case. In the end, there will likely be increased public disclosure and improved informational systems supporting loans and other forms of capital transfer, and there will be likely be improved risk-pricing (more responsive loan rates to borrower risk), but there is not likely to be a fundamental rationing of credit in agriculture as there may be in some other worse-hit sectors.

Table 1. Farm Credit Funding Spread over Treasuries (bps)

<table>
<thead>
<tr>
<th>Date</th>
<th>3-month</th>
<th>1-year</th>
<th>5-year</th>
<th>10-year</th>
<th>30-year</th>
</tr>
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<td>7/1/2008</td>
<td>75</td>
<td>53</td>
<td>98</td>
<td>95</td>
<td>89</td>
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<tr>
<td>11/1/2008</td>
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<td>191</td>
<td>246</td>
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<td>4/1/2009</td>
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<td>36</td>
<td>114</td>
<td>140</td>
<td>147</td>
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(sources: calculated from FFCB and Federal Reserve data)